

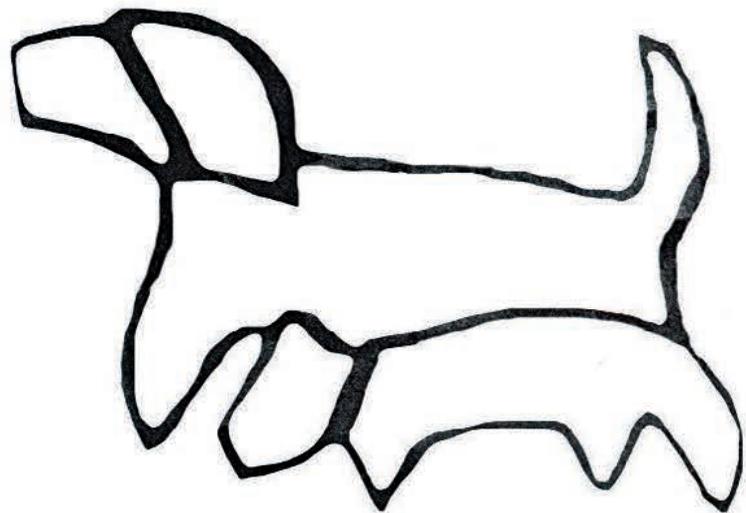


# LOYALTY PROGRAMS THAT PERFORM

DYNAMIC-AWARDS PRICING  
STRATEGIES FOR BETTER  
LOYALTY RESULTS

With a long history in the airline industry, today's loyalty programs are evolving toward greater relevancy and customer satisfaction, while providing greater benefits for carriers that strategize based on dynamic awards.

By John M. Reistrup



CARRIERS HAVE TRADITIONALLY PUBLISHED FIXED AWARD CHARTS WITH DEDICATED LIMITED AWARD SEAT INVENTORY SET ASIDE FOR THEIR LOYALTY PROGRAMS. YET, OFTEN, THERE IS A HIGHER SEAT-AWARD PRICE OR “ANYTIME-OR-PREMIUM AWARDS” TO GET ACCESS ON HIGH-REVENUE-DEMAND FLIGHTS ...



More than 35 years ago, American Airlines launched AAdvantage, the first loyalty program in the airline industry, and most major airlines quickly followed suit with their own loyalty programs.

Today, nearly every retailer, financial institution, airline and hospitality firm offers a loyalty program to compete for their customers' share of wallet and attention.

As a result, loyalty programs have proliferated, with most airline loyalty programs generating more accrual balances from non-airline activities, especially from co-brand credit-card programs and financial-services partners, than from traditional airline flight activity.

Going forward, airlines must assure that loyalty programs continue to evolve, thus making those programs more appealing and meaningful to customers while increasing customer lifetime value and optimizing profitability.

### A HISTORICAL PERSPECTIVE

It is a fundamental economic problem that over the years, airline loyalty programs have become less effective. That's largely because of the increased restrictions that have been placed on the programs, such as when and how an airline's customers can use reward points for airfare purchases.

The essential result is that customers today aren't feeling as "rewarded," so they aren't being as loyal to the airline based on the airline's loyalty program, and they are more apt to split their business across airlines, or to churn all together.

These are real loyalty issues that carriers need to address. In fact, there are numerous further challenges that today's airlines face with their loyalty programs including demand outpacing capacity for rewards, increased government regulations, outdated fixed award structures and processes; and accrual and redemption structures that are not aligned.

### DEMAND OUTPACING CAPACITY

Airlines have consistently high load factors in many regions of the world based on revenue-management optimization, network/capacity management and right-sizing, which has essentially added complexity as to how to allocate capacity for rewards to try to satisfy the seemingly insatiable reward demand, while at the same time mitigating displacement and dilution expense.

### INCREASED GOVERNMENT REGULATIONS

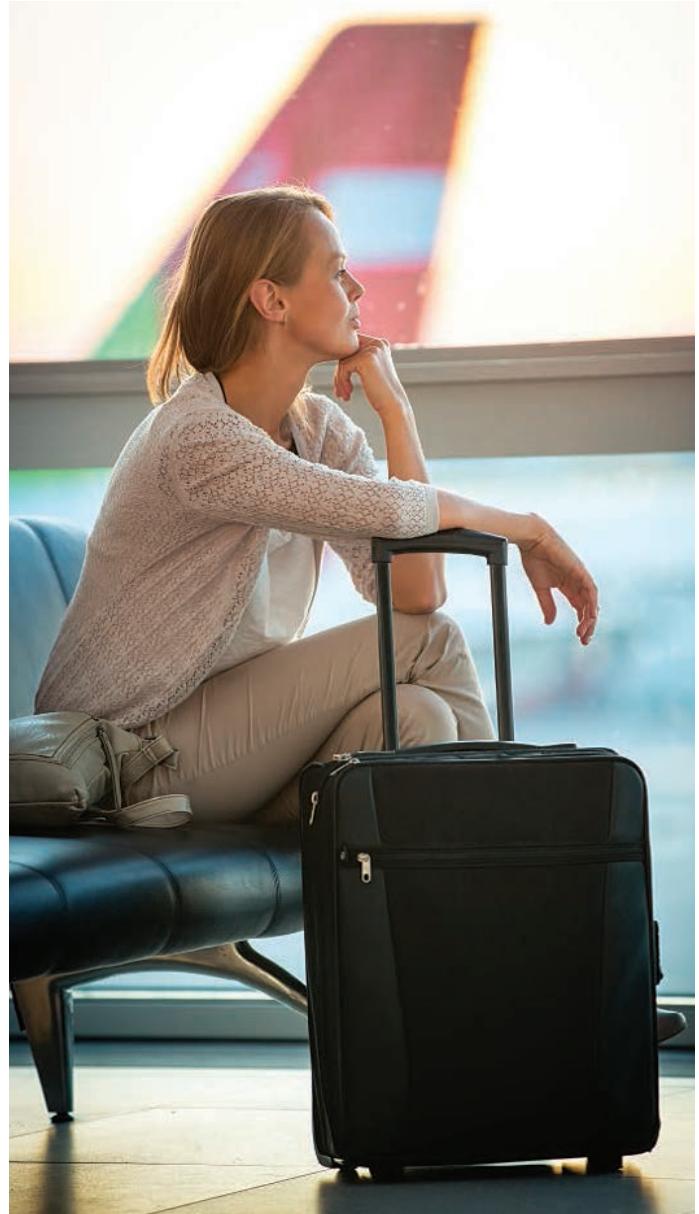
International financial reporting standards (IFRS) and regulations require airlines to include all loyalty-program mileage or point liabilities on their balance sheets at "fair value," thus essentially obligating some airlines to increase allocations of cash set aside for liability to support their programs. As a result, improper IFRS compliance could hinder loyalty-based partnership revenue growth.

### OUTDATED FIXED AWARD STRUCTURES AND PROCESSES

Carriers have traditionally published fixed award charts with dedicated limited award seat inventory set aside for their loyalty programs. Yet, often, there is a higher seat-award price or "anytime-or-premium awards" to get access on high-revenue-demand flights, which has been a popular way to charge customers up to double the price while limiting the lowest-award-seat availability. Such processes still rely heavily on high-fare-class or revenue-booking designator for redemptions, with allocations to control capacity and allotment for redemption tickets and use of other tools such as blackout dates and extra fees to reduce exposure. As a result, customers are increasingly priced out of the market, with limited awards seats and double-points required, often making the seats disproportionately more expensive than the equivalent revenue fares available for purchase on the same flight, compounding customer disappointment and dissatisfaction.

### LACK OF ACCRUAL AND REDEMPTION STRUCTURES ALIGNMENT

As of late 2016, many airlines had already introduced a form of revenue based accrual for air travel, thus intending to reward more for profitable behavior rather than keeping the emphasis on distance flown and the number of flights. This revenue-based-accrual trend is expanding worldwide, but many carriers have not changed their award structures to align with these new accrual programs.



▲ TODAY'S AIRLINE LOYALTY PROGRAMS HAVE EVOLVED TO GENERATE MORE ACCRUAL BALANCES FROM NON-AIRLINE-RELATED ACTIVITIES, SUCH AS CO-BRAND CREDIT-CARD PROGRAMS AND FINANCIAL-SERVICES PARTNERS, RATHER THAN FROM TYPICAL AIRLINE FLIGHT ACTIVITY.

## A STUDY IN STRATEGY

Development of a dynamic award strategy will enable airlines to overcome many of these challenges and actually cause airlines' loyalty programs to further evolve ... in a positive direction.

Dynamic awards can be based on an expanded set of criteria to price and sell award seats, as more thoroughly aligned with an airline's overall pricing and revenue-management strategy and economics.

The airline can customize the rules engine to convert revenue pricing to points or miles based on conversion criteria, resulting in an expanded award program, thus placing a higher priority on customer centricity by increasing access to virtually any seat in any class of service on every aircraft.

In addition to opening up any seat on the aircraft for any awards customer to redeem, dynamic awards can also have a positive effect on driving ancillary revenues and merchandising.

Loyalty points can then become a true form of payment within the dynamic awards strategy, and can, therefore, be used as tender to satisfy punitive transactions such as baggage fees, as well as fees of a more aspirational nature, such as optional passenger services that are designed to enhance the customer's experience.

Also, dynamic awards support mixed-currency transactions that can give customers with lower mileage balances the opportunity to redeem for flights (even though those passengers may have previously been unable to do so). Mixed-currency transactions such as cash-plus-miles are powerful sales drivers, and they are effective alternatives to discounting, thus helping preserve yields.

Rewards as drivers of greater business opportunity translate to much more complete and tangible value within just about any airline's loyalty and revenue structure.

## LOYALTY AND CUSTOMER CENTRICITY

The consulting team at Sabre works with airlines to design, model and deploy their dynamic-award strategies. Based on feedback and input from airlines, as well as extensive operations research initiatives, the technology company has brought to market a robust dynamic-award-pricing offering that expands options for airline customers, providing the most valued loyalty customers a greater incentive to fly with a specific airline, and use the airline's partners and credit cards.

In several ways, this is a paradigm shift that fundamentally enables airlines to incentivize and reward customers based on profitable behavior, a strong complement to the changes some airlines have made in their loyalty-accrual structure based on revenue.

"The deployment of dynamic award pricing on the Sabre Dynamic Rewards platform has enabled us to satisfy more customer demand and increase customer engagement while reducing liability," said Justin Davissen, Virgin Australia's Velocity loyalty program general manager. "As we deployed points as a form of payment in our revenue-booking flow, we had a dramatic uptick of redemptions because customers could easily shop in points or in monetary currency with the click of a button, or even a mix in points and cash. This increased our conversion rates dramatically, and positioned points as a form of payment."

As practically applied, a dynamic-awards strategy promotes transparency by declaring value in terms of return-on-spend. In other words, the consumer gets more value from his or her loyalty currency through a greater number and variety of redemption options, thereby encouraging more earning with the consumer's airline of choice.

The broader range of options varies for customers depending on an individual airline's level of sophistication, data and analytics.

SABRE'S MOST LOGICAL AND TYPICAL APPROACH OF ENGAGEMENT WITH ITS AIRLINE PARTNERS OCCURS IN FOUR PHASES:

1. Thorough assessment,
2. Analysis and strategy,
3. Action and deployment,
4. Advance, which encompasses the optimization of the program over time, with reporting and analytics.

When an airline implements dynamic rewards within its loyalty program, it is important to baseline the program with competitive benchmarking, as well as technical, organizational and financial impact analysis.

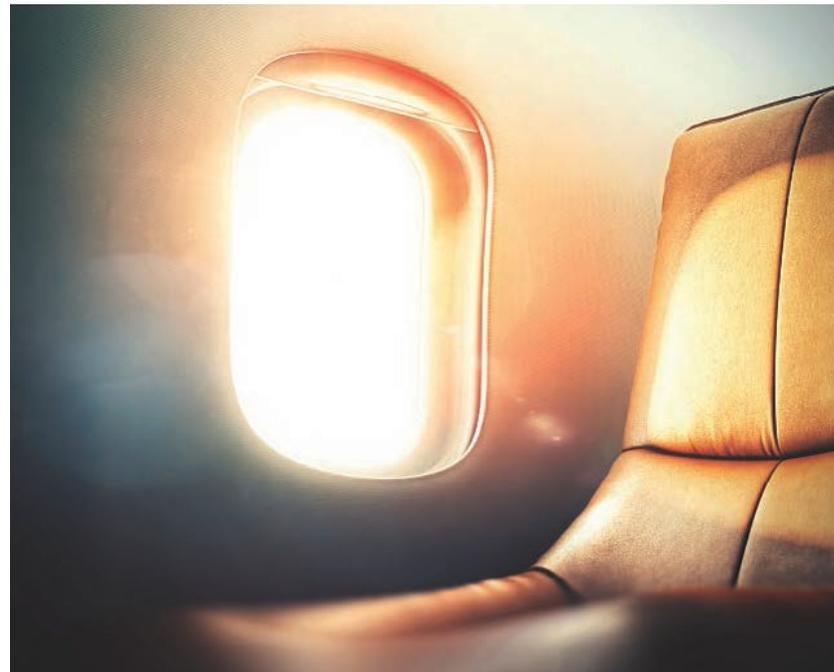
Each carrier must evaluate its current member behavior, assess program liability and look closely at cost-per-point or mile, breakage and the rate of redemption versus qualified balances.

Dynamic awards can actually price rewards automatically on every route, with every seat.

As such, an airline needs a conversion model based on consumer behavior, leveraging the data from its revenue-management, loyalty/analytics and financial systems to find the right balance, as well as provide a variable award-pricing structure.

Development of the strategy enables different rates to be calculated on a variety of inputs and configured into the offering, including consumer targeting/profiles, markets, partners, cash-plus-point purchases, promotions and seasonality.

In the end, with merchandising representing an extremely valuable profit center for an airline, a carrier's loyalty strategy can now include redemption to drive higher conversion for these purchases.



▲  
DYNAMIC AWARDS NOT ONLY ENABLES AN AIRLINE TO OPEN UP ANY SEAT ON AN AIRCRAFT FOR ANY AWARDS CUSTOMER TO REDEEM, IT ALSO DRIVES ANCILLARY REVENUES AND MERCHANDISING OPPORTUNITIES.

## FUTURE OF DYNAMIC AWARDS

Individual airlines today are identifying and acting on a broader capability to evolve their loyalty programs in a strong trend toward increasing program profitability that aligns with a carrier's overall revenue-management strategy, all fitting into a cohesive plan.

Most importantly, airlines are addressing customer demands by increasing the benefits through a larger set of robust offerings, as well as expanding purchasing power through customers' loyalty-program memberships.

Airlines are, thereby, providing greater incentives toward customer loyalty, as well as more thoroughly rewarding customer experience, thus effectively encouraging loyal customers to stay with the airline over many years to come. ASCEND

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