

August 30, 2016

## Ancillary revenues on the up

*This article is based upon a report issued by IdeaWorksCompany.*



Jay Sorensen charts the growth in ancillary revenue rates for airlines and what it means for the future

“My organisation, Ideaworks published the first ancillary revenue review of top-performing airlines back in 2008. The top ten airlines generated \$8.4 billion that year. Fast forward to 2015 and the top ten tally has leapt to nearly \$26 billion. This group is now a billion-dollar club with annual ancillary revenue from \$1 billion to \$6.2 billion – which was top carrier United’s total.

Spirit Airlines topped the list for revenue share, at 43% of its total sales and was also top performer per passenger at \$51.80pp. The results are based on 135 airlines reviewed, 67 revealed figures.

While some mourn the passing of a simpler time when a long-haul ticket price was all-inclusive, consumer behaviour supports the popularity of lower-priced seat-only tickets. The array of choices provided by à la carte methods allows these consumers to click and pay a premium for more comfort and convenience. Ancillary revenue now represents a safety net which determines whether low fares can coexist with airline profitability. Even with a dramatic fall in oil prices, ever-present competition requires successful airlines to be ever-innovative in the quest for revenue. The potential for adding 10%, or even 43%, more revenue to the bottom line ensures ancillary revenue will continue to grow.

It’s a logical corollary that airlines with low average fares achieve the best “percentage of total revenue” results. Spirit Airlines for example had a system-wide total revenue per passenger of a very modest \$119 for 2015. Therefore, the \$52 earned from ancillary revenue represents a crucial 43.4% of Spirit’s total revenue per passenger.

A frugal consumer can fly Spirit at minimal expense and add optional extras such as checked bags, seat assignments, and onboard treats. Consumers have embraced this à la carte method; what else would explain Spirit's growth from 5.5 million passengers in 2008 to nearly 18 million in 2015?

Most of the other airlines in the top ten list deploy similar methods to encourage consumers to spend above the base fare. The growing market presence of Spirit, along with Allegiant and Frontier, has caught the attention of American, Delta, and United. These global leviathans are becoming unlikely practitioners by offering basic economy fares that mimic the à la carte approach. Regulators who criticise à la carte methods might pause to consider how the growing prevalence of seat-only fares is creating a new wave of deeply discounted options for consumers.

The same highly-competitive environment already exists within Europe with traditional brands like British Airways and Air France offering basic economy fares to compete with the likes of easyJet and Ryanair.

There is plenty of activity in the market to suggest ancillary revenue will continue to grow in total, as a percentage of airline revenue, and on a per passenger basis too."