

FITTING THE BILL

DESIGNING A REVENUE-BASED ACCRUAL STRUCTURE



CASE STUDY



ABOUT US

On Point Loyalty is a global consulting and investment firm focused exclusively on the airline loyalty space.

We partner with leading airlines, technology providers, financial institutions and investors to shape and realize their airline loyalty vision.

With tailor-made solutions, ranging from strategy consultancy to outsourced operating models, we help our clients to define the future – and create a competitive edge.

Our suite of Financial Planning & Analysis tools puts insights at the fingertips of program managers.

AT A GLANCE

A leading airline operating a large international network realized there was room to improve its existing frequent flyer program set-up.

The airline brought in On Point Loyalty to develop different scenarios to improve the economics, enhance the marketing effectiveness and optimize the customer value proposition of the frequent flyer program.

On Point Loyalty performed a comprehensive analysis and recommended a new structure based on monetary spend with the airline.

The ultimate design not only better aligned customer value to recognition, but also created a foundation for sustainable growth in the future.

BACKGROUND

The original structure of most frequent flyer programs was straightforward – fly a mile, earn a mile. Although not perfect, it served its objective given the lower levels of fare dispersion and limited data availability.

But today a very different picture has emerged. Programs have grown significantly in membership size, and it has become standard for FFP members to account for up to half of the airlines' passenger revenues. Markets have become more competitive, and airlines now have access to robust and detailed fare data.

With the changes, a growing realization is taking place in the industry that distance traveled is not the ideal proxy for customer value. Even though linking accrual percentages to specific booking classes offers some respite, an increasing number of airlines is adopting revenue-based accrual. Perhaps most telling is that low-cost carriers, not hampered by legacy systems, generally chose revenue-based logics when they designed their new programs.

Many airlines are starting to realize that the growing disparity between the cost of the currency and yields will ultimately become unsustainable

THE APPROACH

Generally speaking, On Point Loyalty deploys project teams that are assembled specifically around the requirements of a client mandate. With our global roster of FFP experts, representing a wide range of disciplines, we are in a position to deliver the right mix of know-how and experience to our clients for each assignment. Delivery usually takes place through a combination of on-site meetings and presentations, complemented with offsite research work. Occasionally, we are in a position to link existing clients, enabling them to exchange ideas and approaches, ensuring the maximum possible knowledge transfer.

Together with the client, the On Point Loyalty team designed an approach to develop and test various accrual logics

As a starting point, On Point Loyalty came on board to perform an analysis of the existing program structure. As in any program, different segments of members received varying levels of payback as a result of the program design. The results were subsequently compared to an ideal future state, identifying gaps where relevant.

Together with the client, the On Point Loyalty team designed an approach to develop and test various accrual logics.

Next, On Point Loyalty performed a comprehensive evaluation, ranking the competing scenarios across a number of dimensions, including economic viability, program effectiveness and attractiveness of the customer value proposition.

Once the high-level program design was confirmed, On Point Loyalty worked with the airline's technology team and external partners to scope out an implementation plan.

REVENUE-BASED ACCRUAL INCREASES DISPERSION

Exhibit 1

Distance-based accrual programs typically award between 0% and 300% - depending on the cabin class booked

Typical accrual rates for a distance-based accrual program across cabin classes

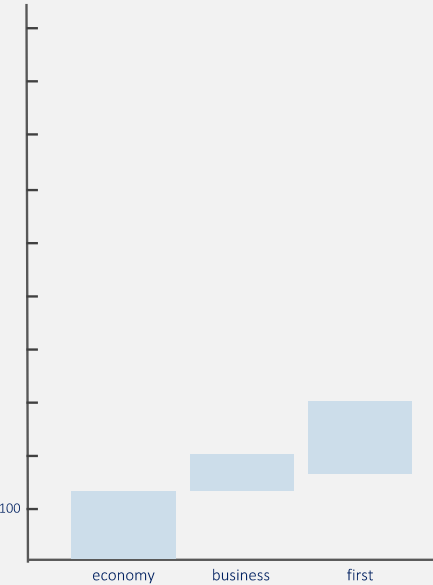
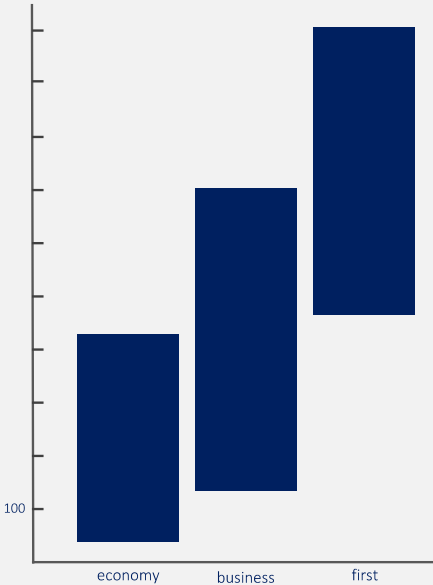


Exhibit 2

For revenue-based programs, the level of dispersion will be greater as first class can easily cost ten-times as much as economy

Typical fare ranges across cabin classes



RESULTS

A simpler customer value proposition Shifting from distance-based to revenue-based accrual allowed the airline to remove complex rules specifying percentages of accrual for each individual booking class. Instead, straightforward earn rates were introduced for each tier of the program, greatly simplifying the customer value proposition.

Stronger program economics Throughout the project, a consistent picture emerged: distance-flown favored long-haul travelers paying lower fares. In contrast, high-yielding passengers (both on the short-haul and long-haul) received relatively less in terms of miles awarded on a dollar-for-dollar comparison. The move to revenue-based accrual rectified this anomaly, resulting in better program economics.

A more effective loyalty program The revenue-based program also proved to be a more effective loyalty program, as the new structure provided an incentive to spend-up, rather than buy-up. With record load-factors, and a strong focus on yield improvement, this element was crucial to the airline.

The revenue-based program also proved to be a more effective loyalty program, as the new structure provided an incentive to buy-up, instead of buying more

About the authors

Evert de Boer is Managing Partner and is based in the Singapore office of On Point Loyalty. You may contact him at evert.deboer@onpointloyalty.com.

Xiao Yao Chin is Vice President, Strategy and is based in the Kuala Lumpur office of On Point Loyalty. You may contact her at xiaoyao.chin@onpointloyalty.com.

For further contact:

If you would like to discuss this case study further, please contact one of the authors.

