

Reinventing Reward Programs

How miles and tiers could disappear

Presentation for Mega Event 2018 Long Beach, CA

NOVEMBER 1, 2018



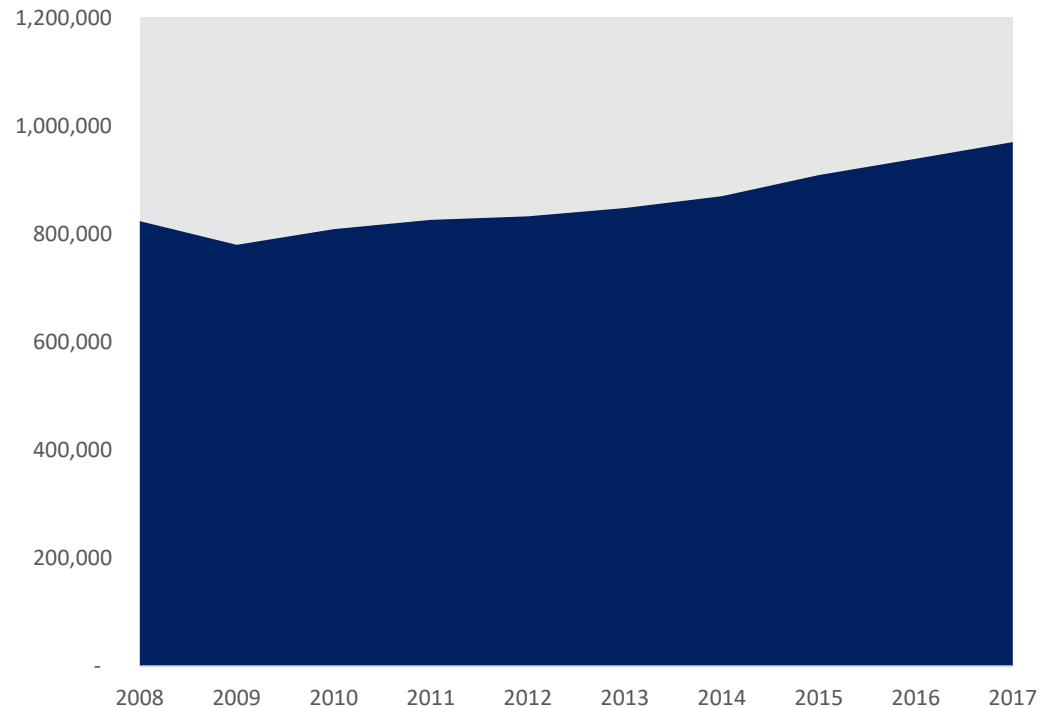
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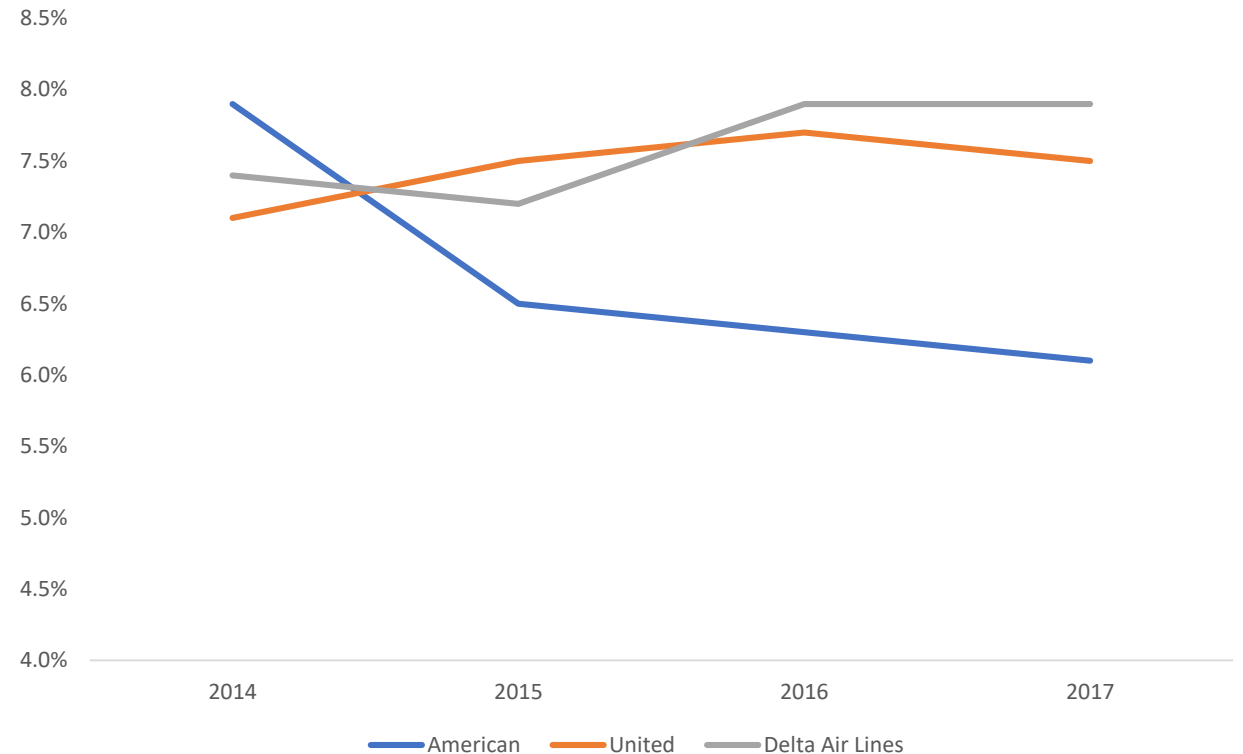
US airline industry continues to grow



Total system RPMs US Carriers



% RPMs for Award Travel



Source: company reports, MIT Airline Data Project



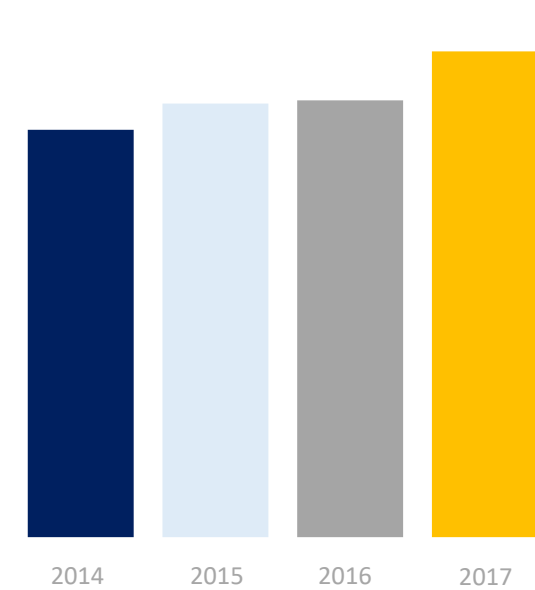
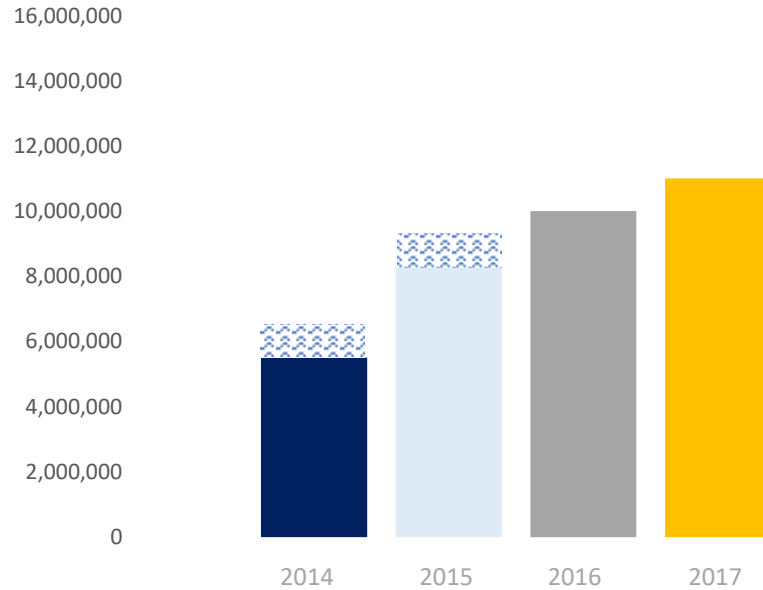
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Legacy programs continue to show growth



Total number of redemptions (air and non-air for 2014 to 2017)



Source: company reports.  = Estimate. AA did not report non-air redemptions prior to 2016

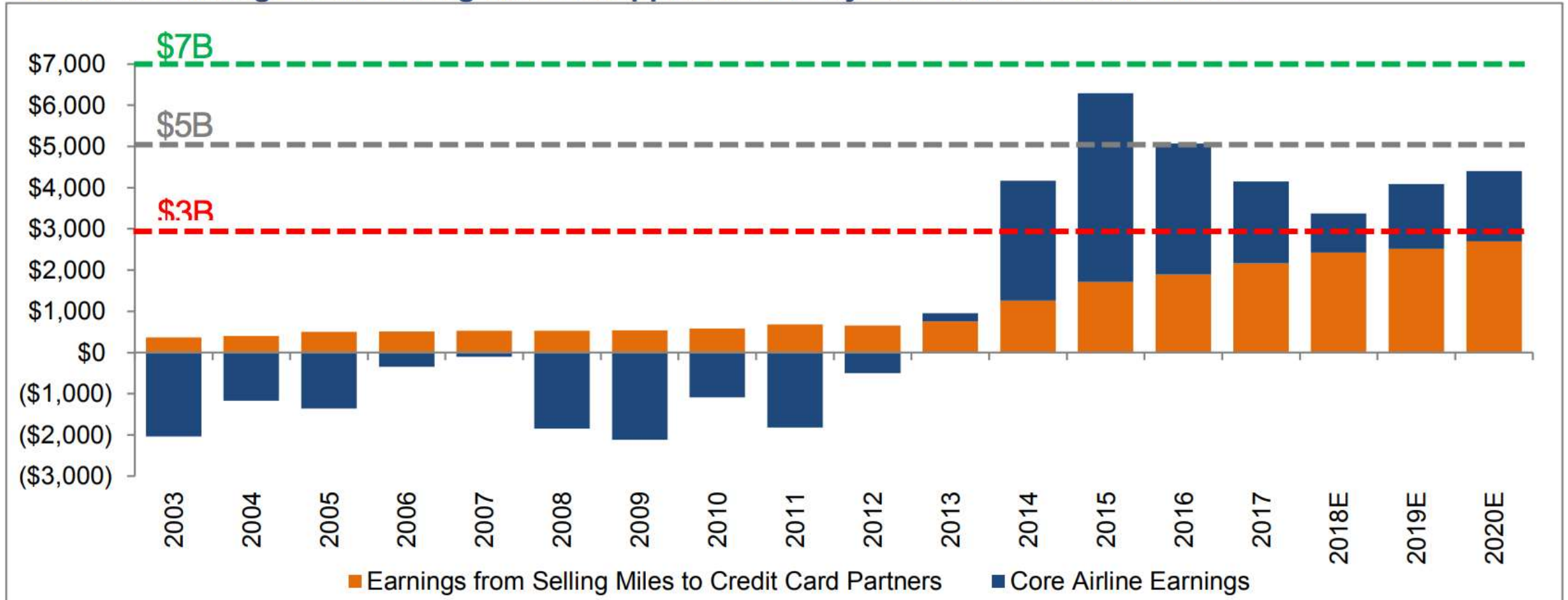


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FFPs are positioned as financial powerhouses

Exhibit 1: Earnings from Selling Miles to Approach \$3B by 2020 for American Airlines



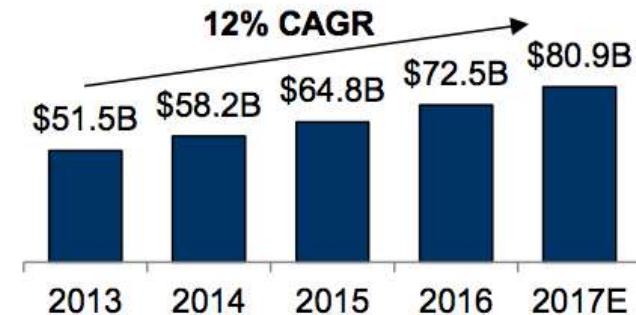
Source: Stifel ("Here's Where Doug Parker Gets His \$3B, \$5B, \$7B From; FF #133'), 6 March 2018.

FFPs are positioned as financial powerhouses

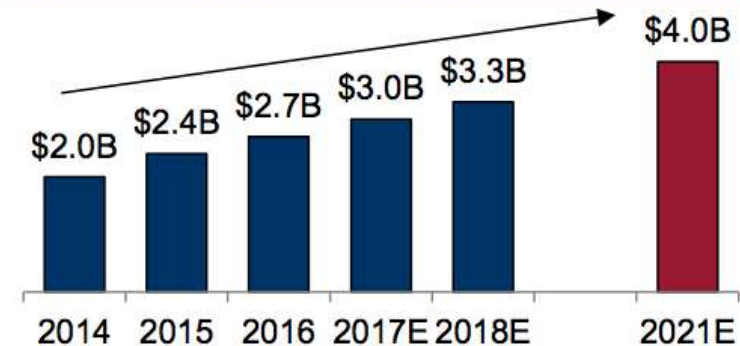
Ascending brand, leading partnership with Amex driving growth in high-margin revenue

- Delta's brand and product initiatives have stimulated additional demand for SkyMiles as a currency
- American Express co-brand spend has grown 12% annually since 2013
 - 2017 another record year with ~1 million card acquisitions
- Delta is the largest co-brand partner for American Express and their only U.S. airline card partner
 - \$3 billion 2017 contribution, up 50% since 2014 and set to grow another \$1 billion through 2021
 - Co-brand revenue stream largely tied to consumer spending trends vs. solely airline ticket sales

Delta-Amex Co-Brand Spend

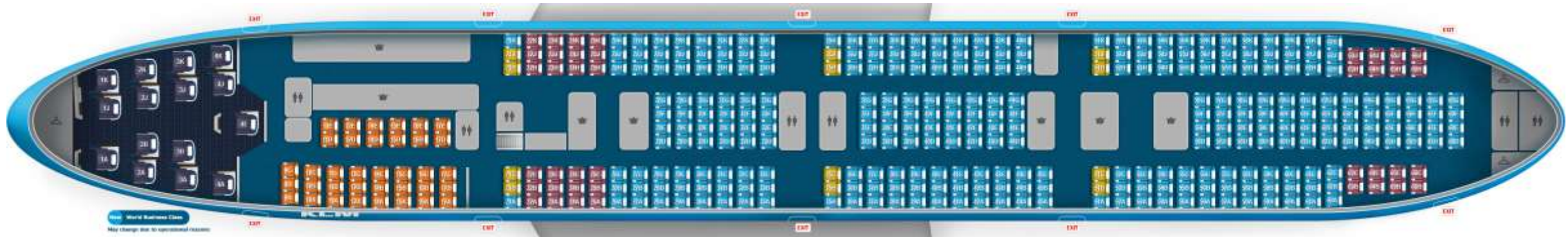


Delta-Amex Co-Brand Contribution



Source: Delta Air Lines Investor Day 2017

Revenue Management and FFPs



dilution

displacement

marginal cost

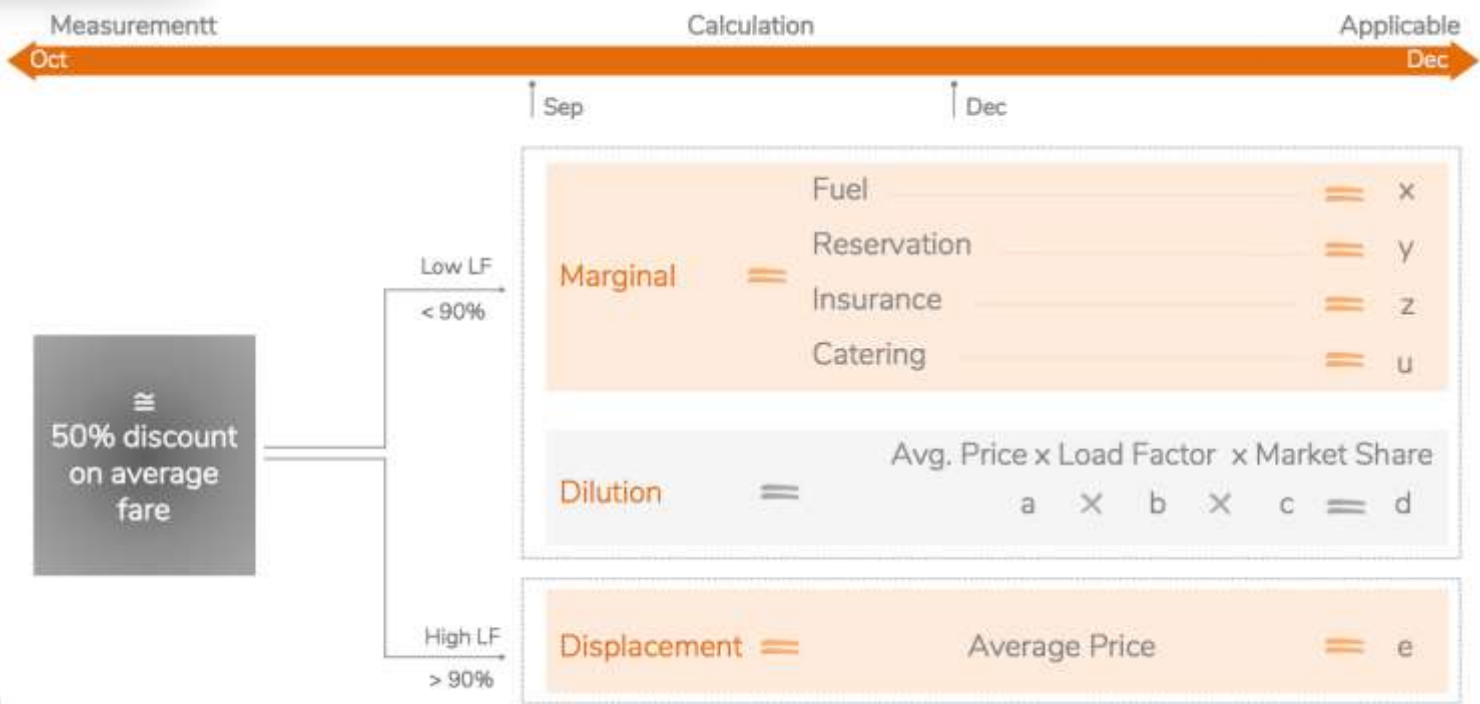
spill and re-capture

variable cost

take-along

Image: Air France-KLM

Revenue Management and FFPs



- Fixed
- Dynamic
- Hybrid
- Member-value driven

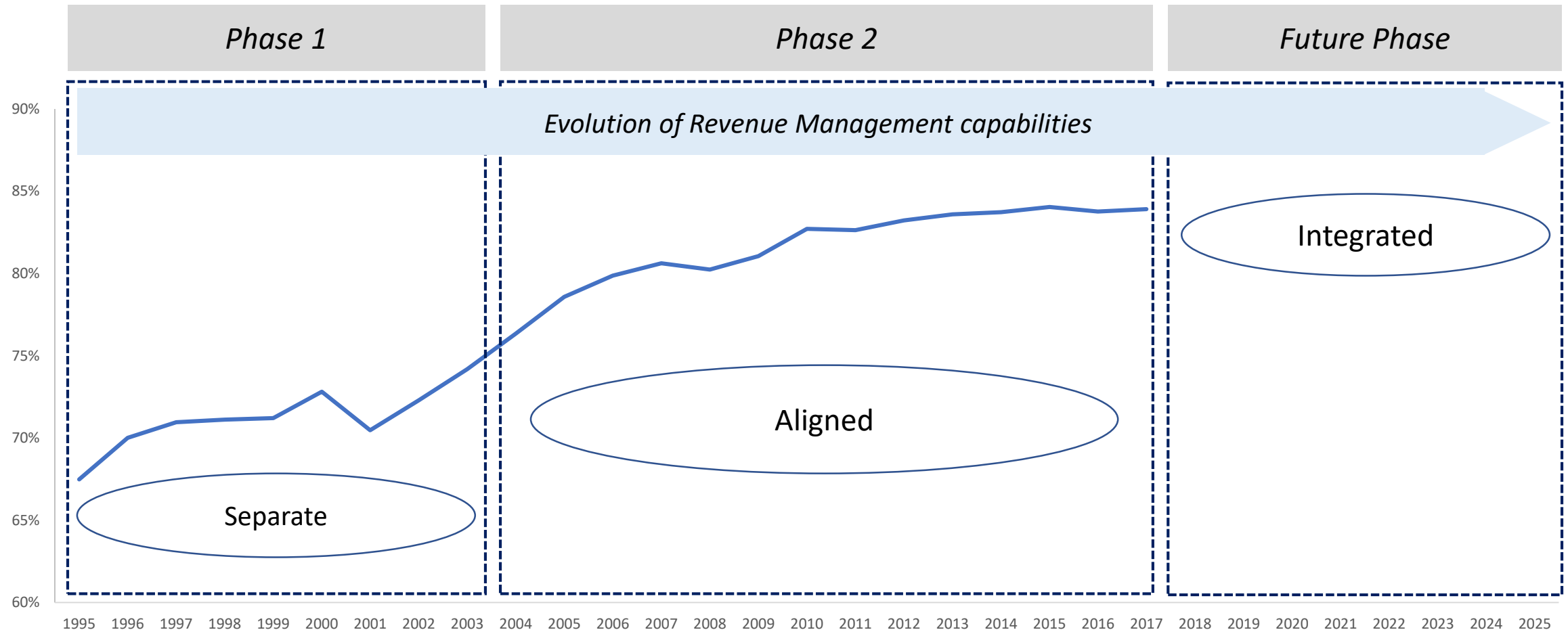
Source: Smiles 3Q 2018 Investor Presentation



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Phases in the RM FFP relationship



Source: MIT Airline Data Project; On Point Loyalty analysis

Main stages of RM development

1980s



- Introduction of RM systems in response to deregulation and increased competition

- Assumes distinct market segment for a particular flight

1990s



- Development of “Origin-Destination” RM systems following the restructuring of airline networks around large, connecting hubs

- Evaluates contribution across the network instead of single flight

2000s



- Collapse of existing RM systems following the removal of the Saturday-night minimum stay requirement

- Lowered fare fences create a more amorphous market
- Dispersion in willingness to pay

Today

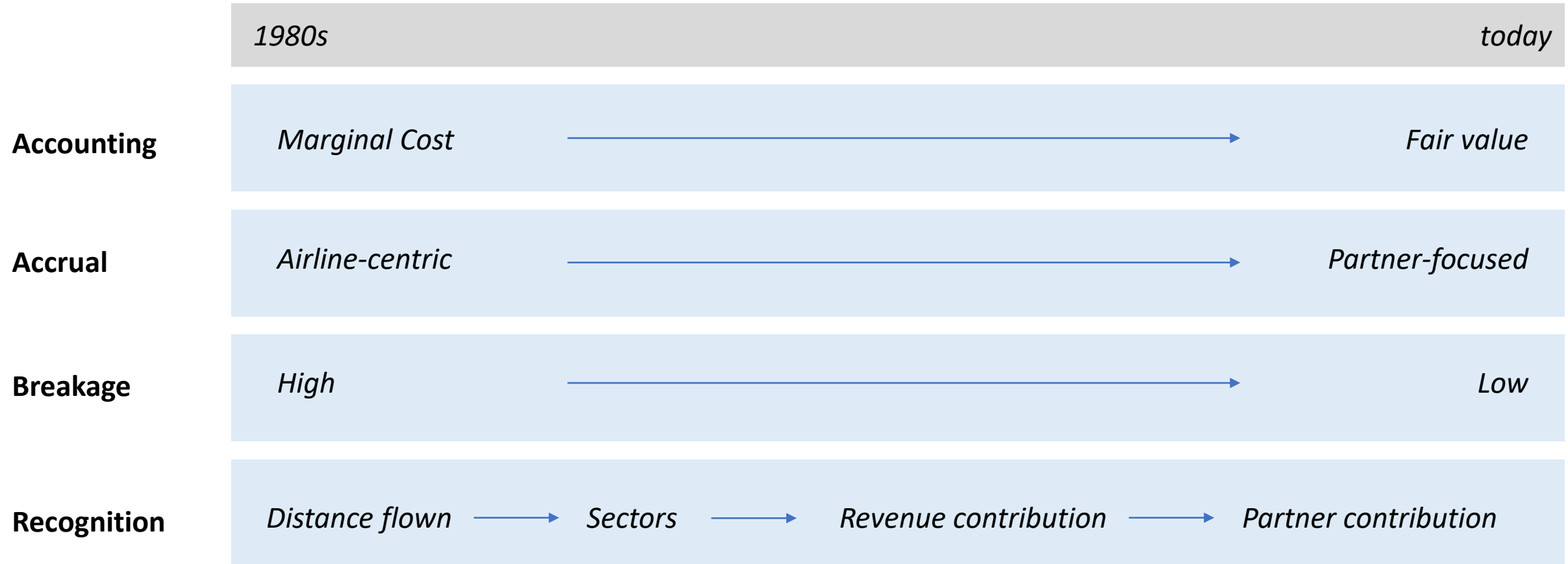


- New distribution capabilities, more data, allow RM to restructure its approach

- Move to personalized pricing
- Using more data in RM decisions

Source: Carrier, E., & Fiig, T. (2018). Special Issue: Future of Airline Revenue Management.

FFPs have evolved as well in many aspects



Moving towards the Integrated Phase

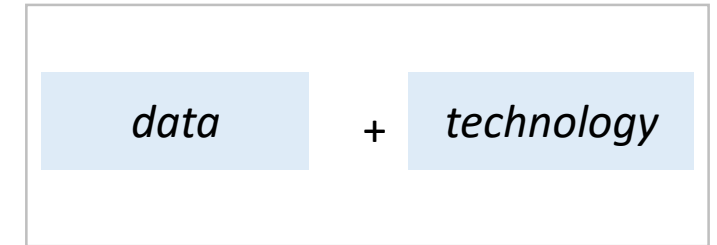


1980s	1990s	2000s	Today
<ul style="list-style-type: none"> Introduction of RM systems in response to deregulation and increased competition Assumes distinct market segment for a particular flight 	<ul style="list-style-type: none"> Development of "Origin-Destination" RM systems following the restructuring of airline networks around large, connecting hubs Evaluate contribution across the network instead of single flight 	<ul style="list-style-type: none"> Collapse of existing RM systems following the removal of the Saturday-night minimum stay requirement Lowered fare fences create a more amorphous market Dispersion in willingness to pay 	<ul style="list-style-type: none"> New distribution capabilities, more data, allow RM to restructure its approach Move to personalized pricing Using more data in RM decisions

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	1980s	today
Accounting	Marginal Cost	Fair value
Accrual	Airline-centric	Partner-focused
Breakage	High	Low
Recognition	Distance flown → Sectors → Revenue contribution → Partner contribution	

+



Shifting underlying economic fundamentals

#1: Redemptions generate comparable yields



LAX → ATL
\$321
27,500 miles

LAX → ORD
\$277
25,000 miles

LAX → ORD
\$274
25,000 miles



Source: company website for RT December 1, return December 6 in Main Economy cabin



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Shifting underlying economic fundamentals

#2: Miles are becoming a form of payment

ContDom & Intercont MaM LH Tix



Source: Lufthansa - Riedle, S. Amadeus Conference Prague. 2018





Increasing adoption of RM tactics by FFPs

#1: Restricting access to award inventory

Airlines limiting access to first class redemptions:



Increasing adoption of RM tactics by FFPs

#2: Increasing access to award inventory




Making it easier to spend your Avios


Spending your Avios is one of the most rewarding parts of the Club, and we understand the importance of being able to spend them on the flight you want, when you want. As a Gold Member you'll get access to additional reward seats in economy cabins at the standard price.

If there is no availability in your chosen cabin or on the flight, with the Gold Priority Reward you have the option of using double the regular Avios to secure a seat of your choice on the flight, providing you book 30 days or more in advance. All you have to do is call us to make the arrangements.





Award Travel Benefits				
Priority award waitlisting	✓	✓	✓	✓
Standby for international awards	✓	✓	✓	✓
Unrestricted access to United Everyday Awards on United- and United Express-operated flights	✓	✓	✓	✓
Better availability for United Saver Awards in economy	✓	✓	✓	✓
Better availability for United Saver Awards in select premium cabins			✓	✓
Reduced or waived change-in award booking fee	✓	✓	✓	✓
Reduced or waived award redeposit fee [®]	✓	✓	✓	✓
Reduced or waived award change fee	✓	✓	✓	✓



Improved flight award availability	Senator Premium Award (improved flight award booking availability)	Best flight award availability: HON member + 3 travelling companions up to 14 days before departure, if seats are still available in Business, Premium Economy and Economy Class (for flights operated by LH, OS, LO, LX, SN)
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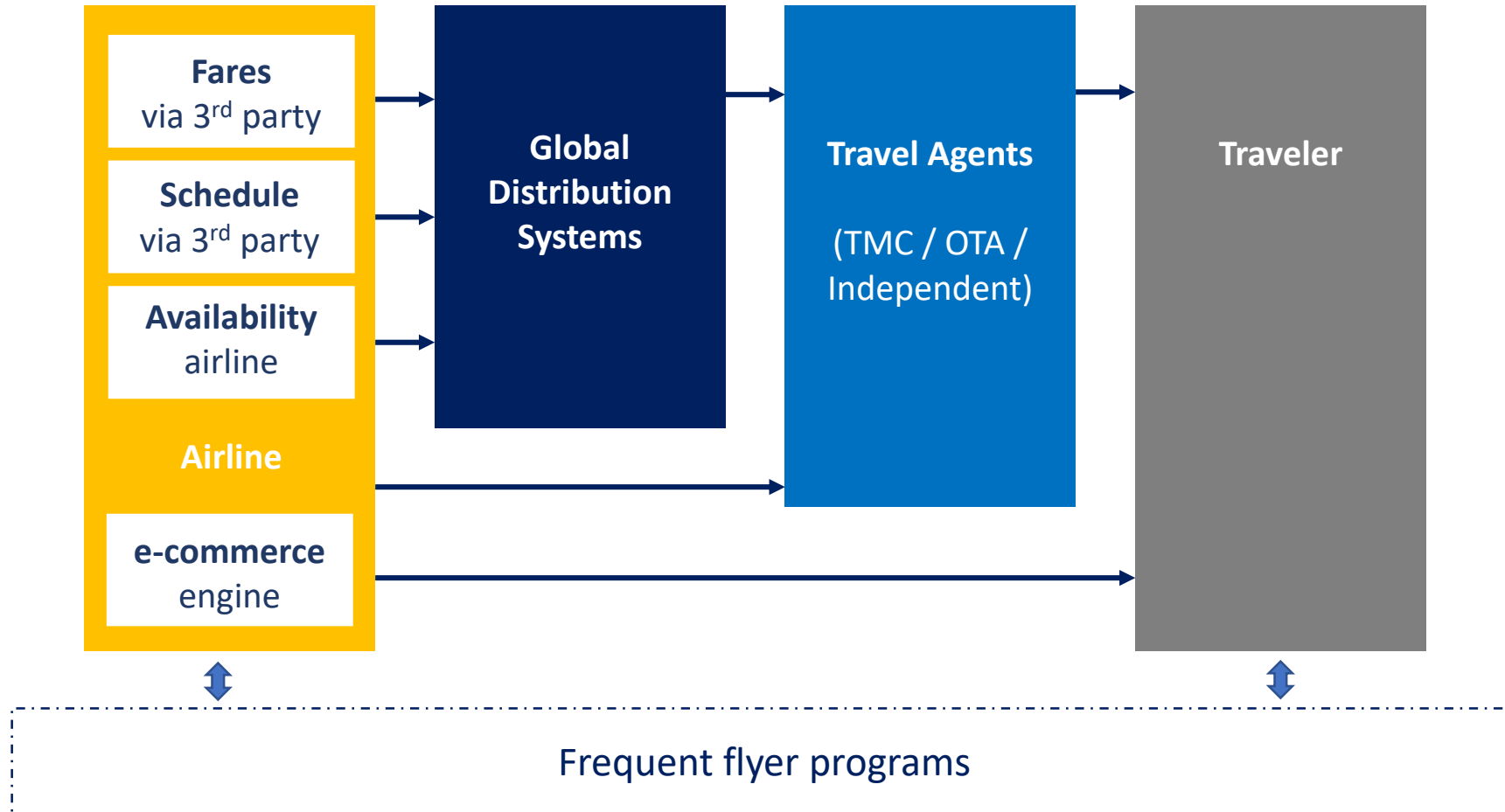
Priority redemption

You will be given highest priority to Saver Awards flight availability.

Source: company websites



FFPs were designed to track and reward customers

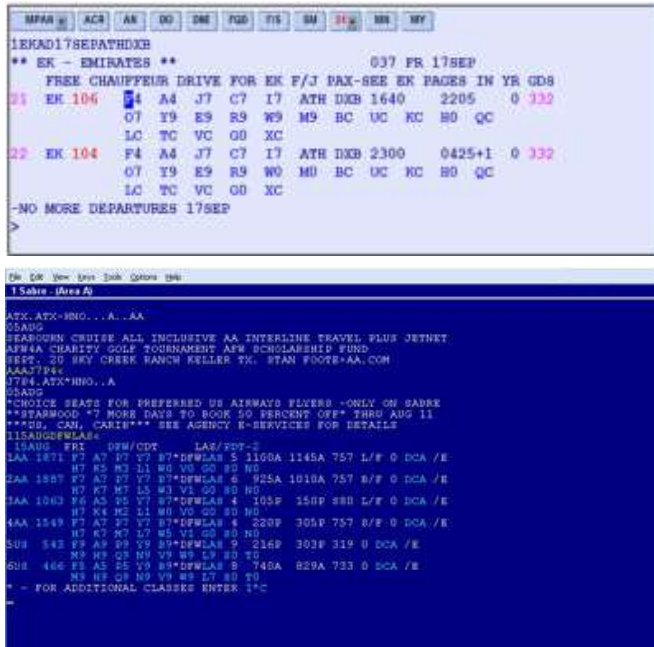


Source: IATA, On Point Loyalty

Future RM capabilities will transform the FFP



Past



Present



Future

- Personalized Dynamic Pricing
- Full visibility on customer value
- Ability to recognize and reward members individually

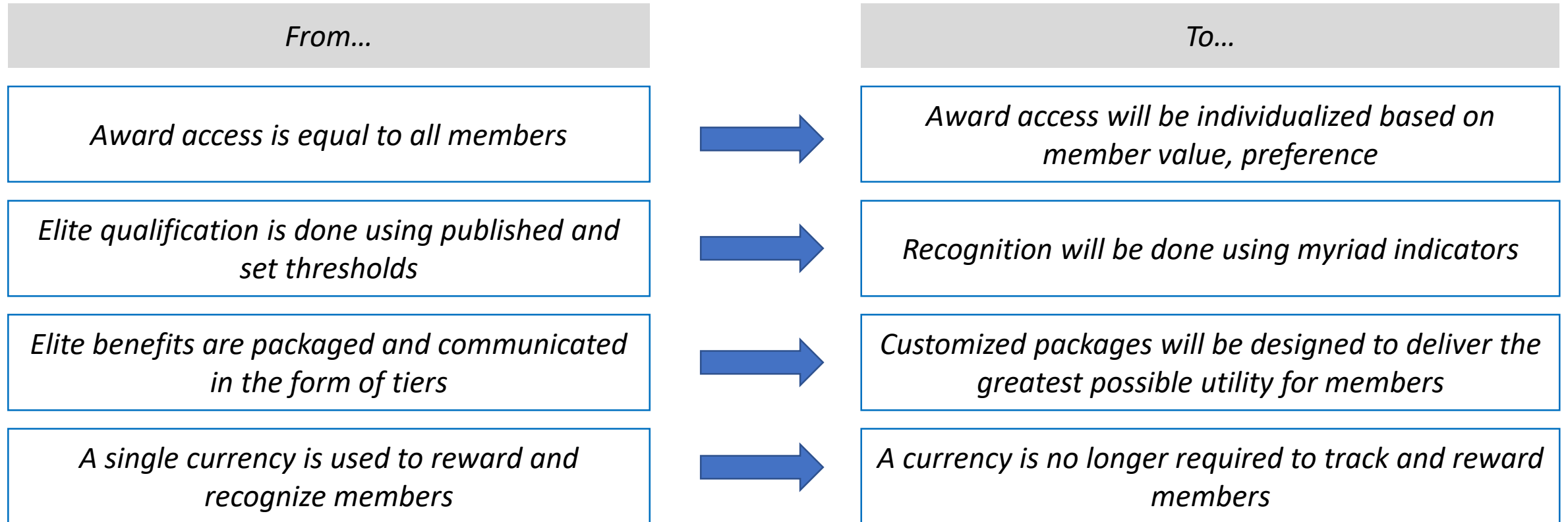
Source: IATA, On Point Loyalty



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Re-inventing the FFP in the future



Conclusion



The FFP-RM relationship has changed as a result of the underlying economics

Displacement will reduce over time as miles become an integral part (form of payment)

Access to high—value award seats will be individualized

Airlines will become increasingly savvy in reserving high-value rewards for high value customers

Technological advances will alter the FFP design

Future capabilities to determine and recognize individual customer value and preferences will change the design of FFPs



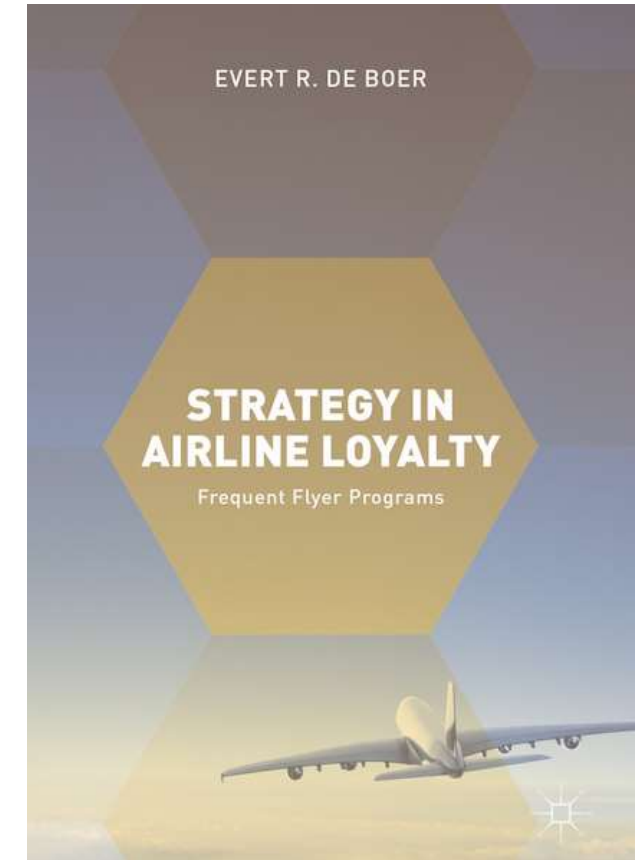


www.onpointloyalty.com

**About the presenter:**

Evert R. de Boer has researched and worked in airline loyalty strategy since 2000. He has collaborated with more than 20 airlines globally on frequent flyer programs in management and advisory roles, and has published numerous articles and white papers on the subject. His latest publication, *Strategy in Airline Loyalty*, offers a comprehensive overview of the airline loyalty landscape.

Following his Master of Science degree in Business Administration at the University of Maastricht, Evert de Boer has completed executive education programs at a number of institutions including the London Business School, the Walter A. Haas School of Business at University of California, Berkeley, and the Desautels Faculty of Management at McGill University.





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