

Airline Distribution

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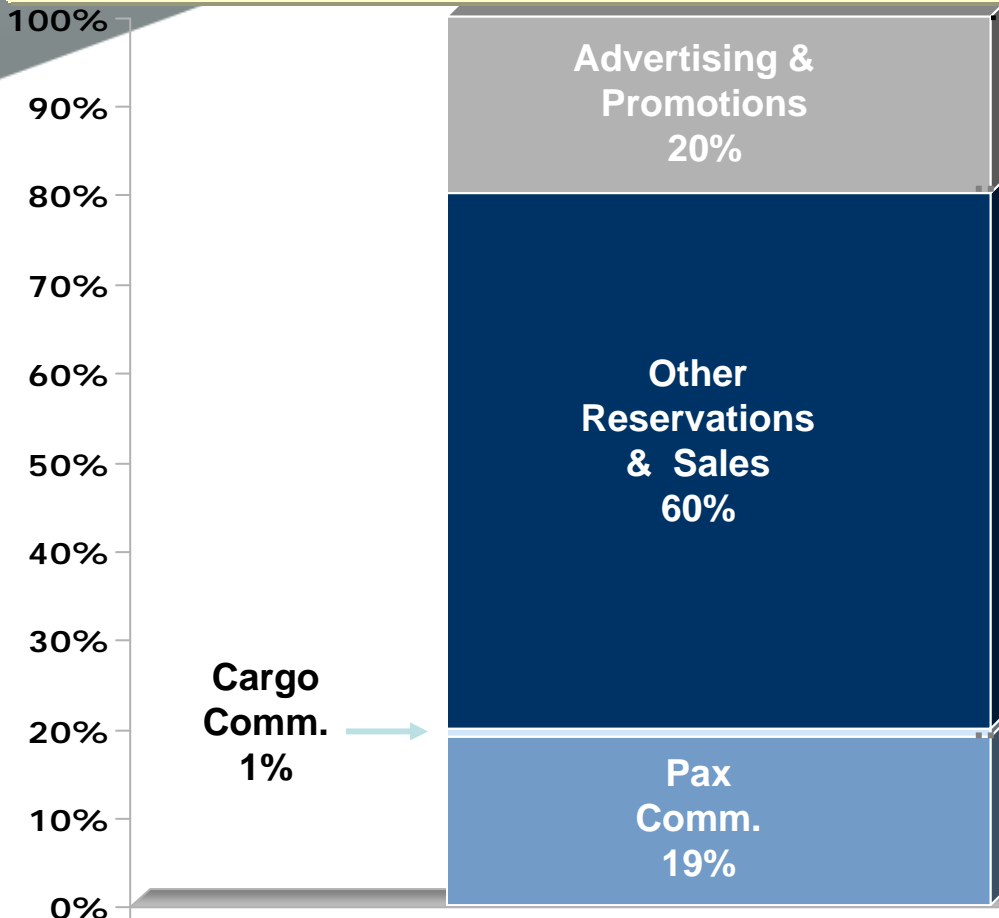
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- Airlines drive to reduce costs
 - Distribution has been around 20% of operating costs
- Airlines wishing to have more direct contact with their clients
- Technology has provided the possibility of a direct channel between the airline and its customers
- Disintermediation - as airlines doubt the ability of agents to influence customers' choice
- GDSs fees
- Large corporates are more professional in the way they purchase travel products

Star Alliance Carriers collective spend over USD \$11bn on distribution

Total Mainline reservations, sales, advertising and promotional cost, by category 2004 est.



Description	Cost Q3 03
Media	8%
Personnel	2%
Loyalty Programs	2%
Other	7%
CRS / GDS Fees	18%
Credit Card Fees	18%
Salesforce /Reservations	5%
Benefits	6%
Management & staff	3%
Other	8%
Passenger commissions	19%
Cargo commissions	1%

Sources: Form 41 4Q03, Star Alliance

The distribution value chain

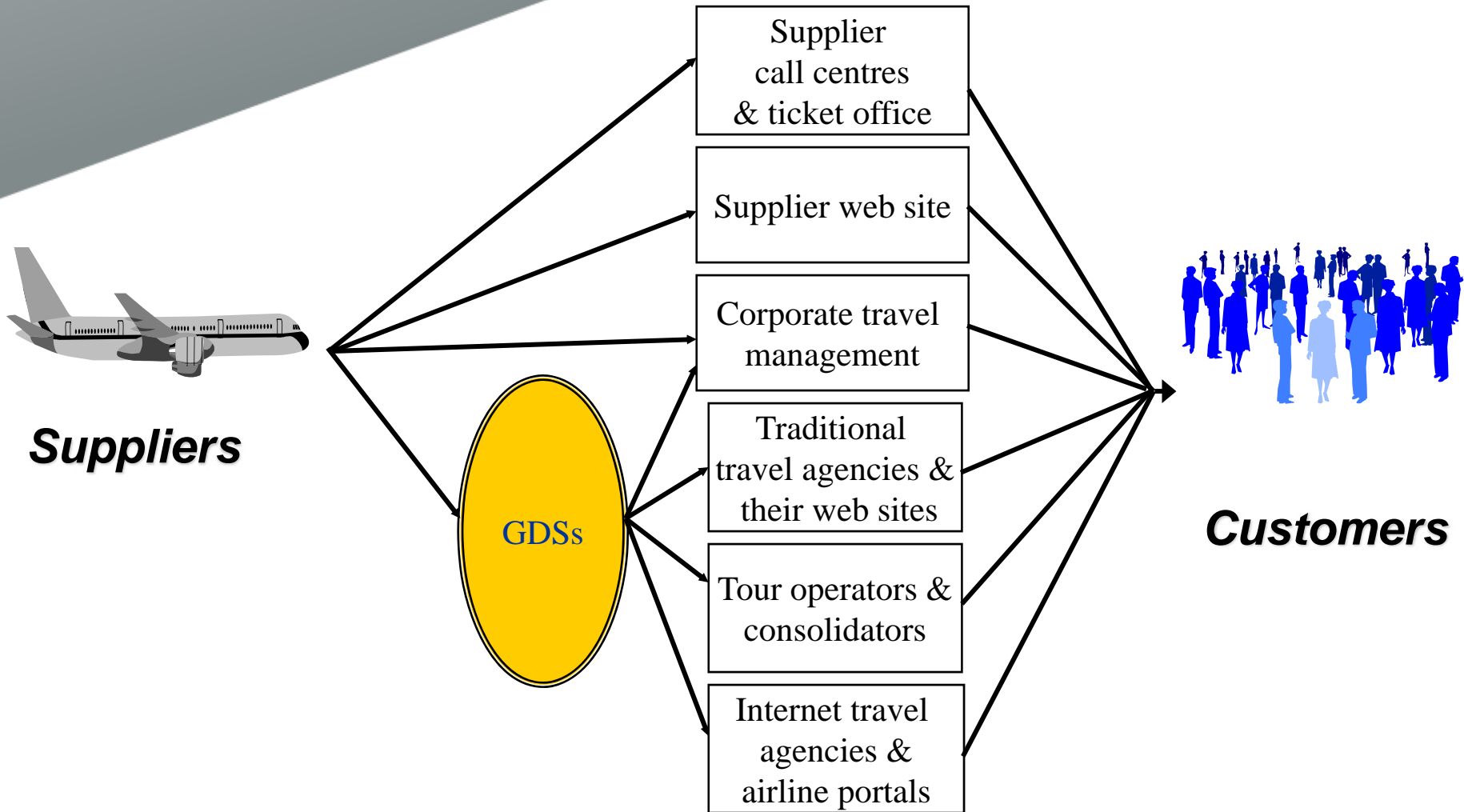
- Airlines spend \$5bn per annum on GDS fees
- Cost as % of ticket prices
 - GDS 8 - 11%
 - Travel Agency 1 - 2%
 - Mercantile fee 2 - 3%

Source: UATP(Universal Air Travel Plan), Airline Business July 2005 and July 2006

Airline Distribution Channels

- Direct
 - Sales offices
 - Call centres
 - Website
 - Corporate travel website
- Indirect
 - Traditional travel agents
 - On-line travel agents
 - Travelocity, Expedia, Priceline.com, last minute.com, ...
 - On-line travel portals
 - Orbitz in the US, Opodo in Europe, Zuji in Asia
 - Tour operators and consolidators

Airline Distribution Channels



Travel Agents' Traditional Services

- Marketing and sales
- Advisory service and itinerary planning
- Pricing and booking
- Subsequent amendments (back to advisory)
- Ticket issues
- Itinerary
- Invoice
- Delivery of documents (e-ticket or not)
- Accounting and credit
- Refund/Changes (back to advisory))

10% of total business is refunds and changes

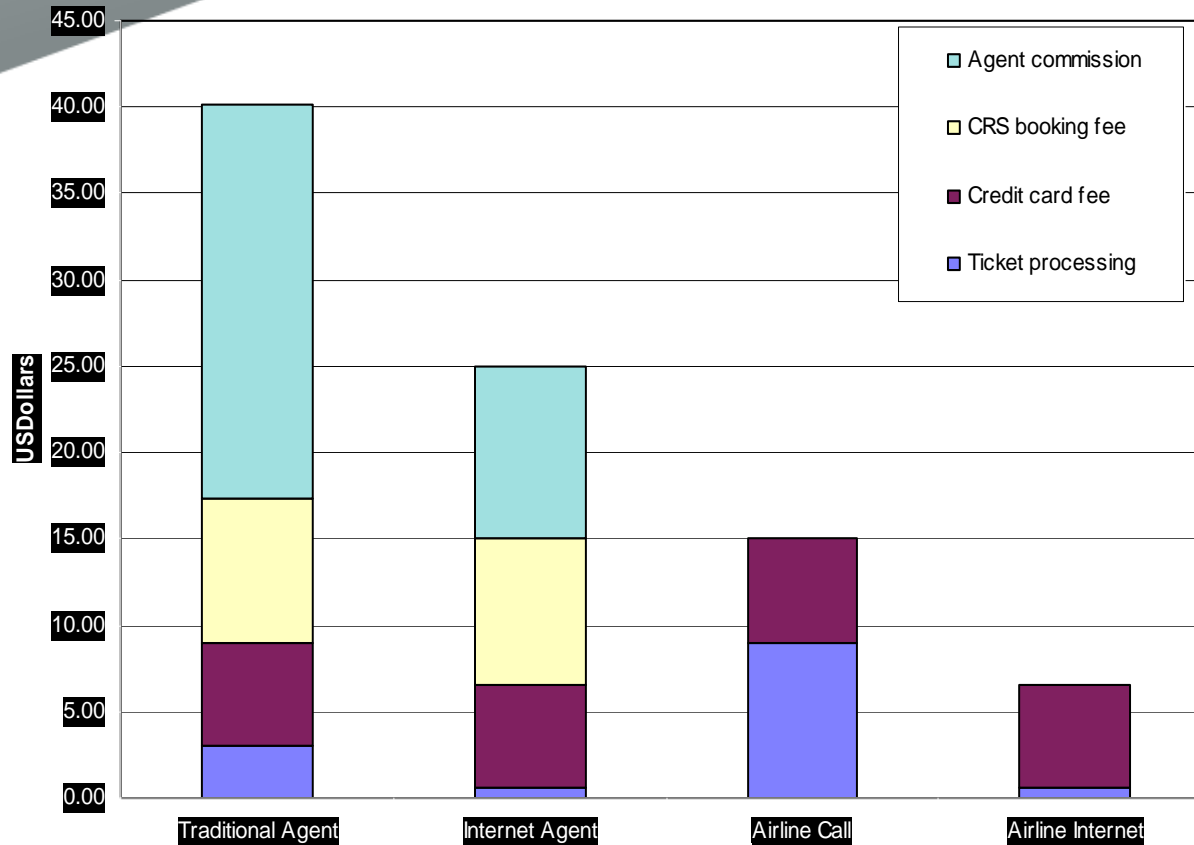
Travel Agents' other services

- Hotels booking
- Car hire
- Package holidays
- Foreign currency
- Travel Insurance

Travel Agent Remuneration models - Original Model

- **Commission**
a simple % of airline fare
- **Override payment**
additional commission for achieving targeted business levels
- **Net fares**
discounted fare offered to agent which could be sold to customers at what ever level the agent can achieve

Airline Distribution Costs by Sales Channel: \$300 Ticket (all channels)



Source: JP Morgan, 1999

Travel Agent Remuneration models

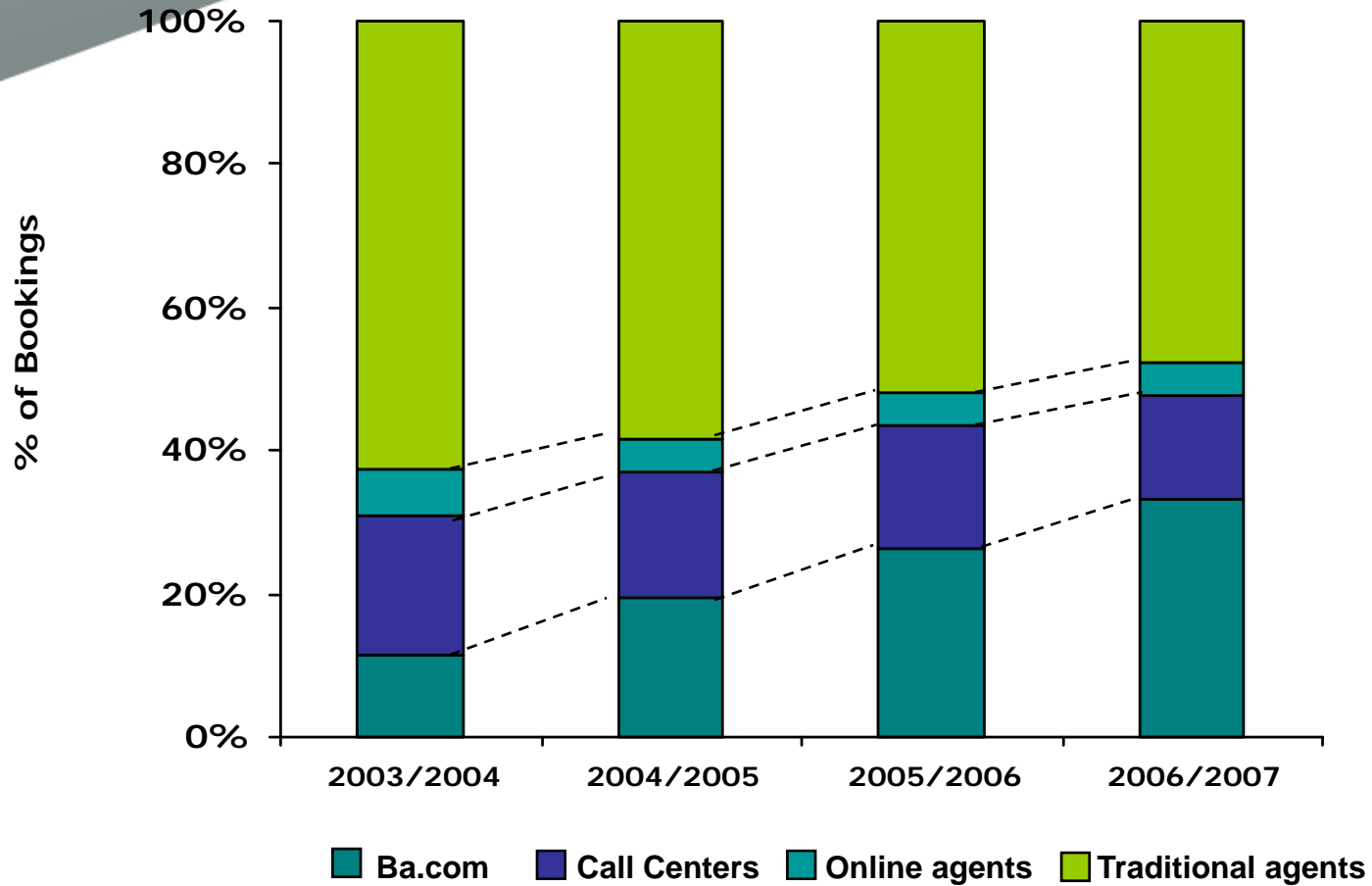


I WANT
TO COMPLAIN
ABOUT
SERVICE
FEES!

FINE - BUT IT
WILL BE TWO
QUID TO LISTEN
TO YOU...

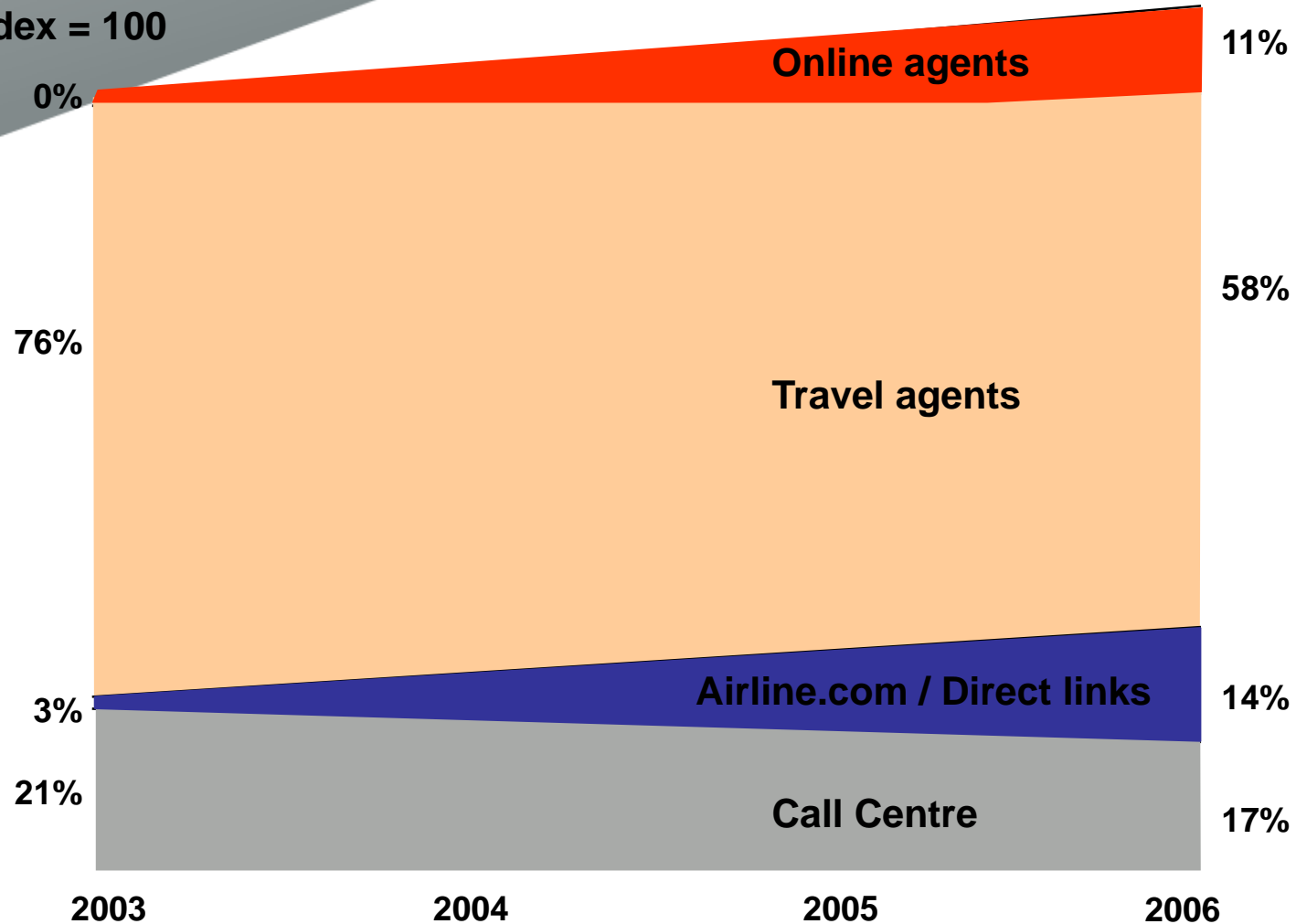


BA's Channel Shift



Channel shift

Share of revenue
Index = 100



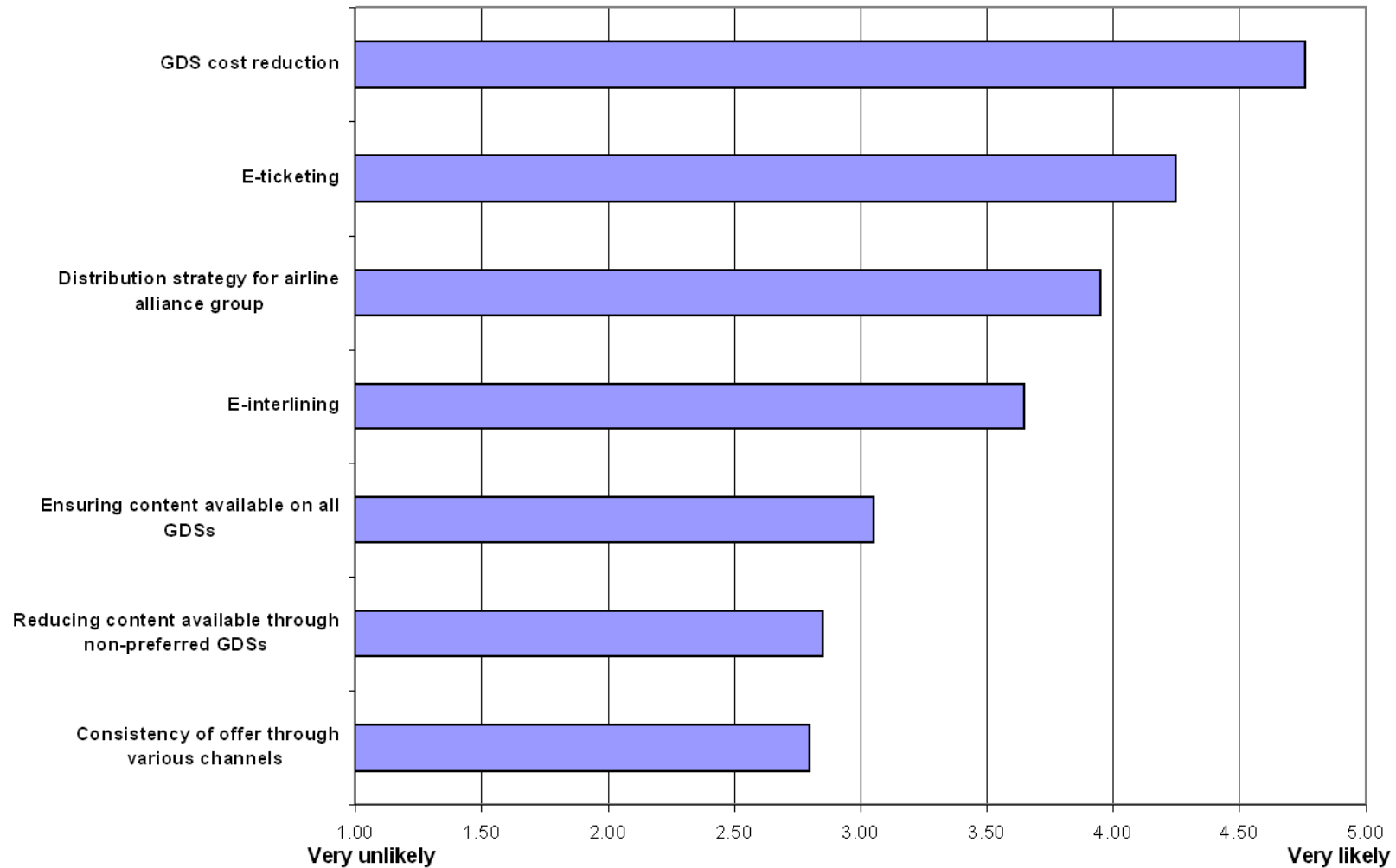
Source: Harrop, IG Management, 2006

Airline relationships with TMCs

Change in relationships with TMCs in three years	Score
Encourage direct booking for simple itineraries	4.22
Airlines & TMCs develop global strategies for large accounts	4.00
TMCs will aggregate content for corporates	3.94
Develop new fee structures for complex itineraries	3.59

Source: Alamdari and Mason, 2004

Strategic issues for airlines



Source: Alamdari and Mason, 2004

Changing Role of the Travel Agent

PAST

PRESENT

FUTURE

- Commissions
- Agent/Principal
- Travel Manager
- Local service
- Standard GDS
- High regulatory impact

- Low Commissions
- Transaction Fees
- On-line sales channel
- Procurement
- Multiple GDS
- Multi-market servicing
- Direct airlines sales
- Regulatory impact on decline

- High on-line adoption
- Procurement focus
- Solution provider
- Centralised multi-market servicing
- Value add proposition
- Regulatory impact changing

HIGH

TRANSACTION VALUE – Commissions

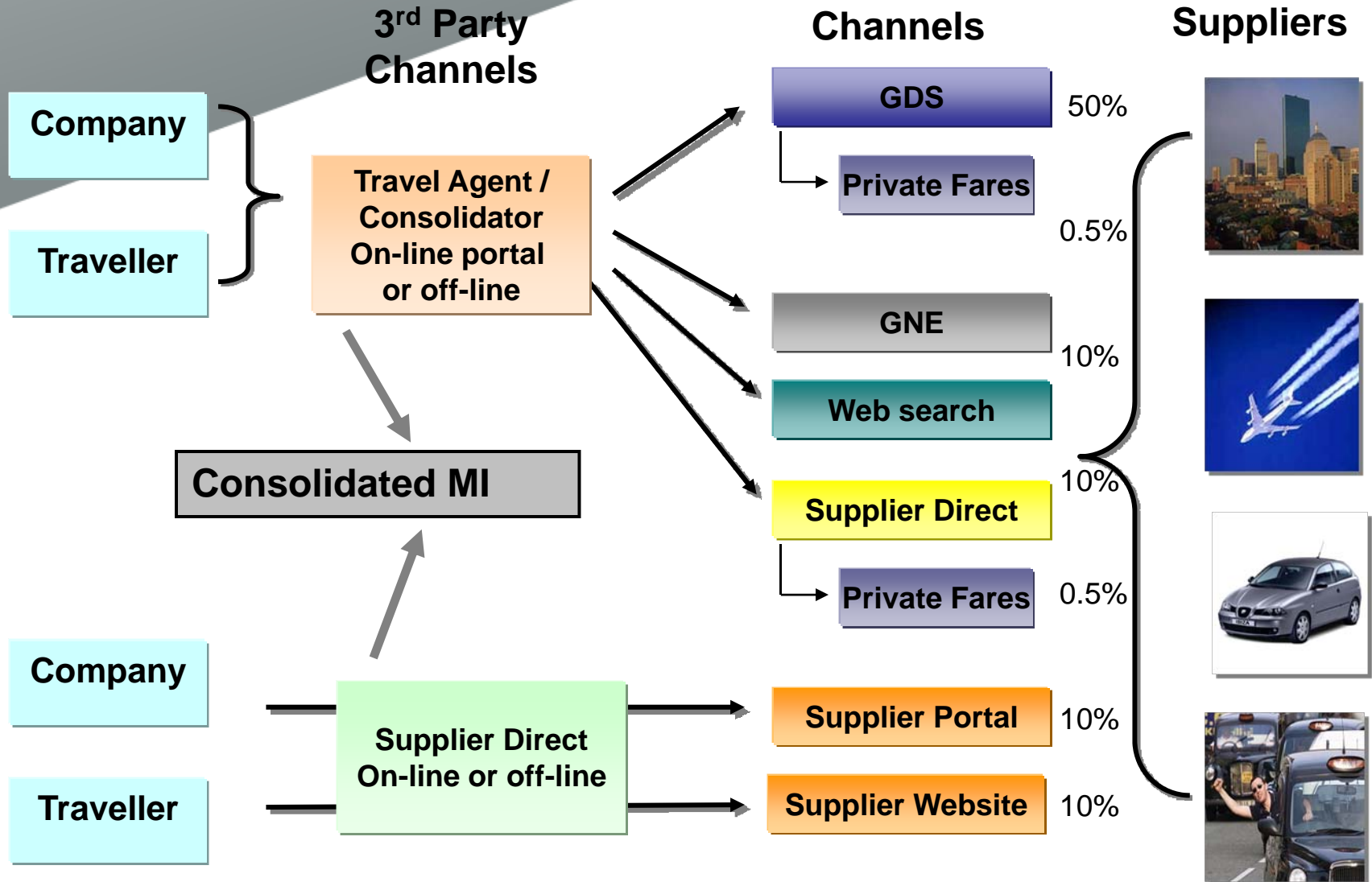
LOW

LOW

ADDED VALUE – income from customers

HIGH

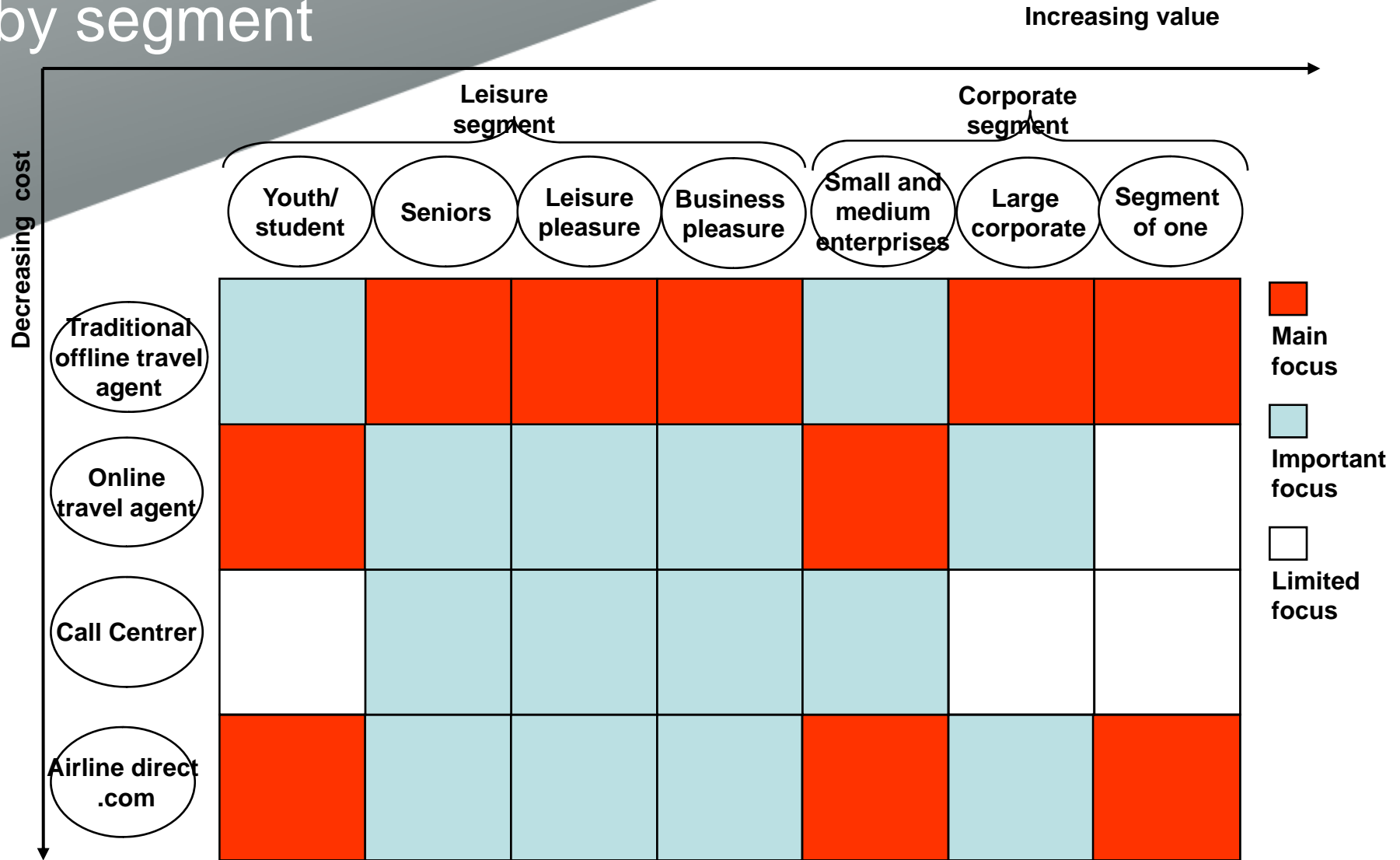
The Future is Channel Fragmentation



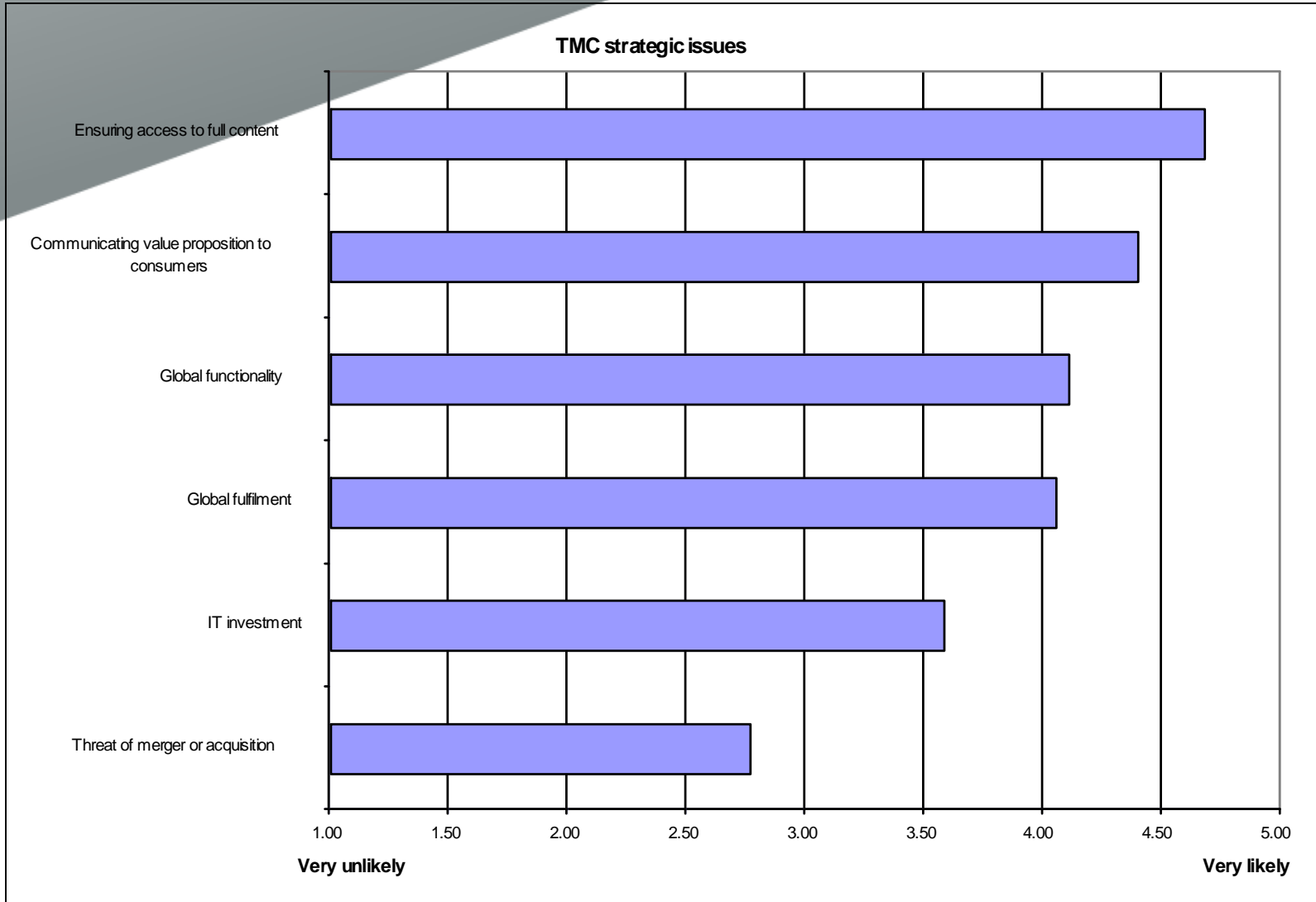
- **Direct Connects**
 - Single inventory and single supplier
 - No shopping alternative other than via the GDS
 - No data integration other than via the GDS
- **OnlineTravel Agents and MetaSearch Engines**
 - Expedia, Priceline, Travelocity, and Orbitz all use a GDS for functionality, faring and pricing, and data integration
 - SideStep, Kayak, Mobissimo use 'screen scrape' technology for web fare comparisons
- **“Global New Entrants” - G2 Switchworks and ITA Software**
 - Utilises Worldspan for functionality, faring and pricing, and data integration
 - Limited airline content access and no hotel or car access
 - Conceptual platforms that claims equal functionality w/o a GDS
 - Developing solutions with limited testing and unknown scalability
 - Initial launch provides only access to air and only 8 carriers vs. 400+ in GDS
 - Claim inventory aggregation and Super PNR data integration

Source: Harrop, IG Management, 2006

Distribution strategies by segment



TMC strategic issues



GDS market structure

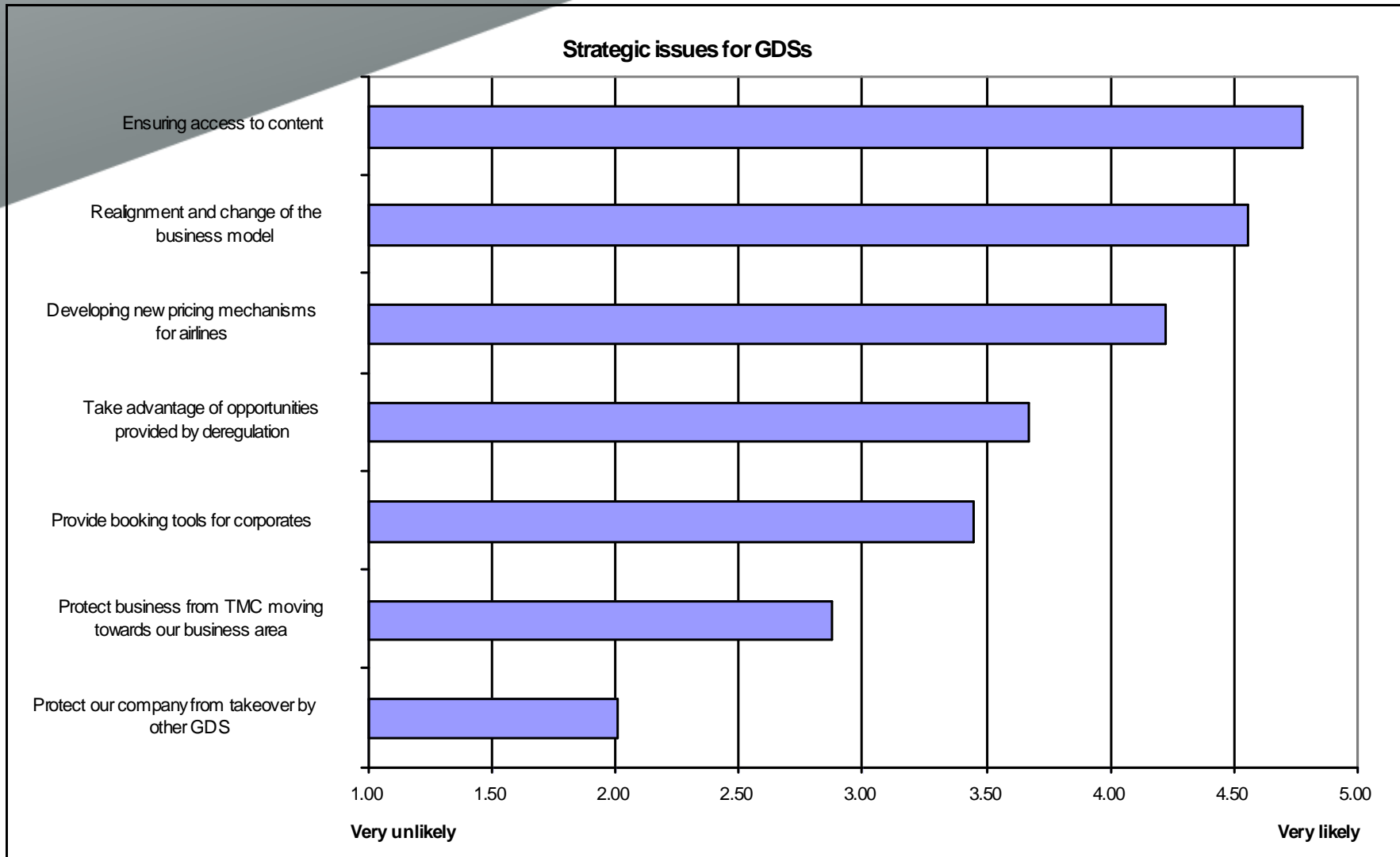
	USA / Canada	Central / South America	Europe / Middle East	Asia / Pacific	Global Average
Amadeus	9 %	38 %	49 %	15 %	26 %
Galileo	21 %	6 %	31 %	15 %	22 %
Sabre	42 %	50 %	13 %	4 %	24 %
Worldspan	28 %	6 %	8 %	4 %	14 %
Abacus				19 %	4 %
Topas				4 %	1 %
Infini				4 %	1 %
TravelSky				36 %	8 %

Source: Star Alliance, 2005

NB: Travelport which own Galileo purchased Worldspan in August 2007

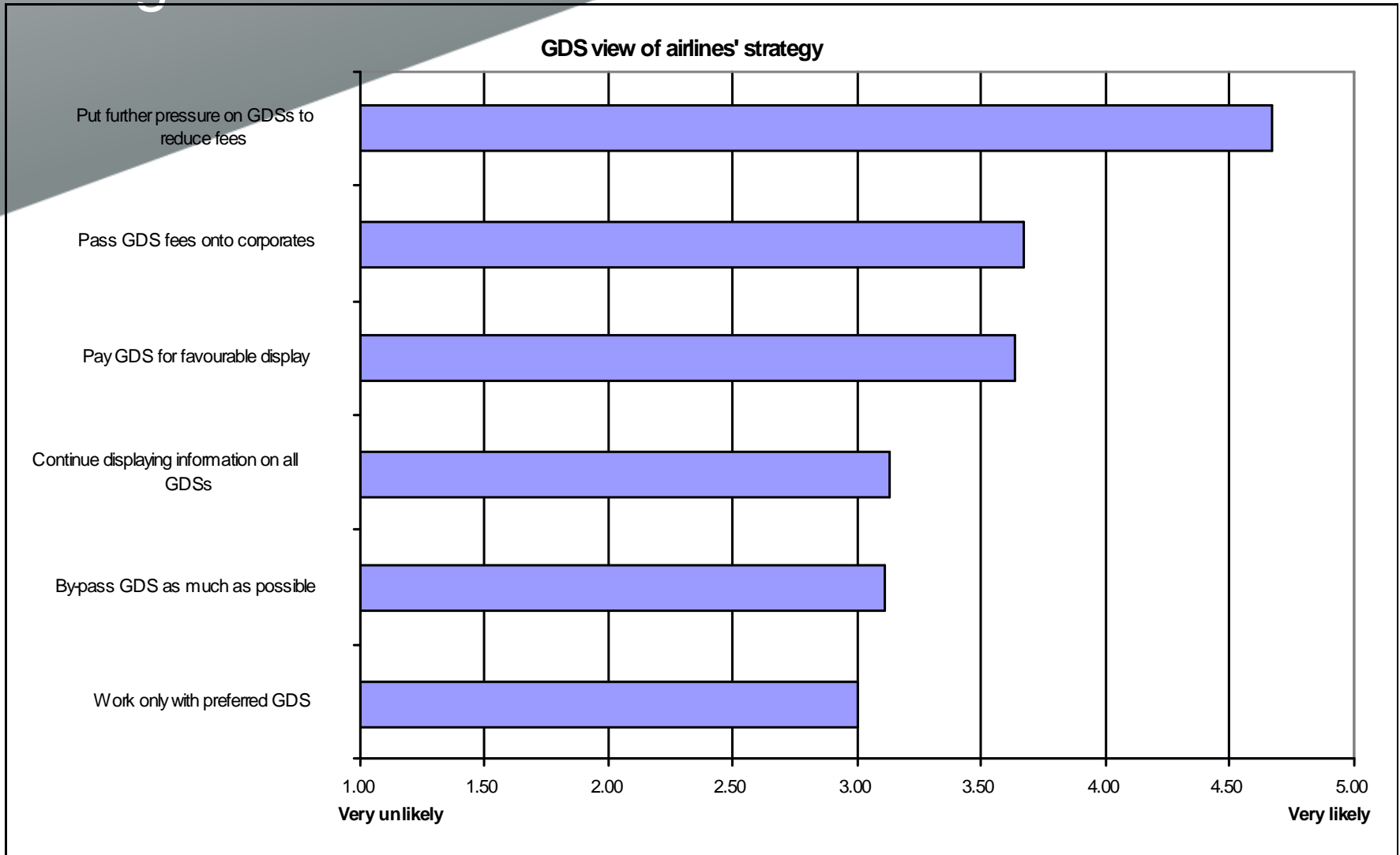
- Types of transactions flowing through the systems are getting more and more complex
- The average number of transactions per booking has increased by 60% as there are more lookers than bookers
- Prepared to reduce fees in exchange for having access to airlines' all content
- Are not prepared to remunerate travel agents the same as before and expect travel agents to bear some of the costs of a GDS booking

GDS strategic issues



Source: Alamdari and Mason, 2004

GDS' view of airline strategies



Source: Alamdari and Mason, 2004

GDS fee structure development

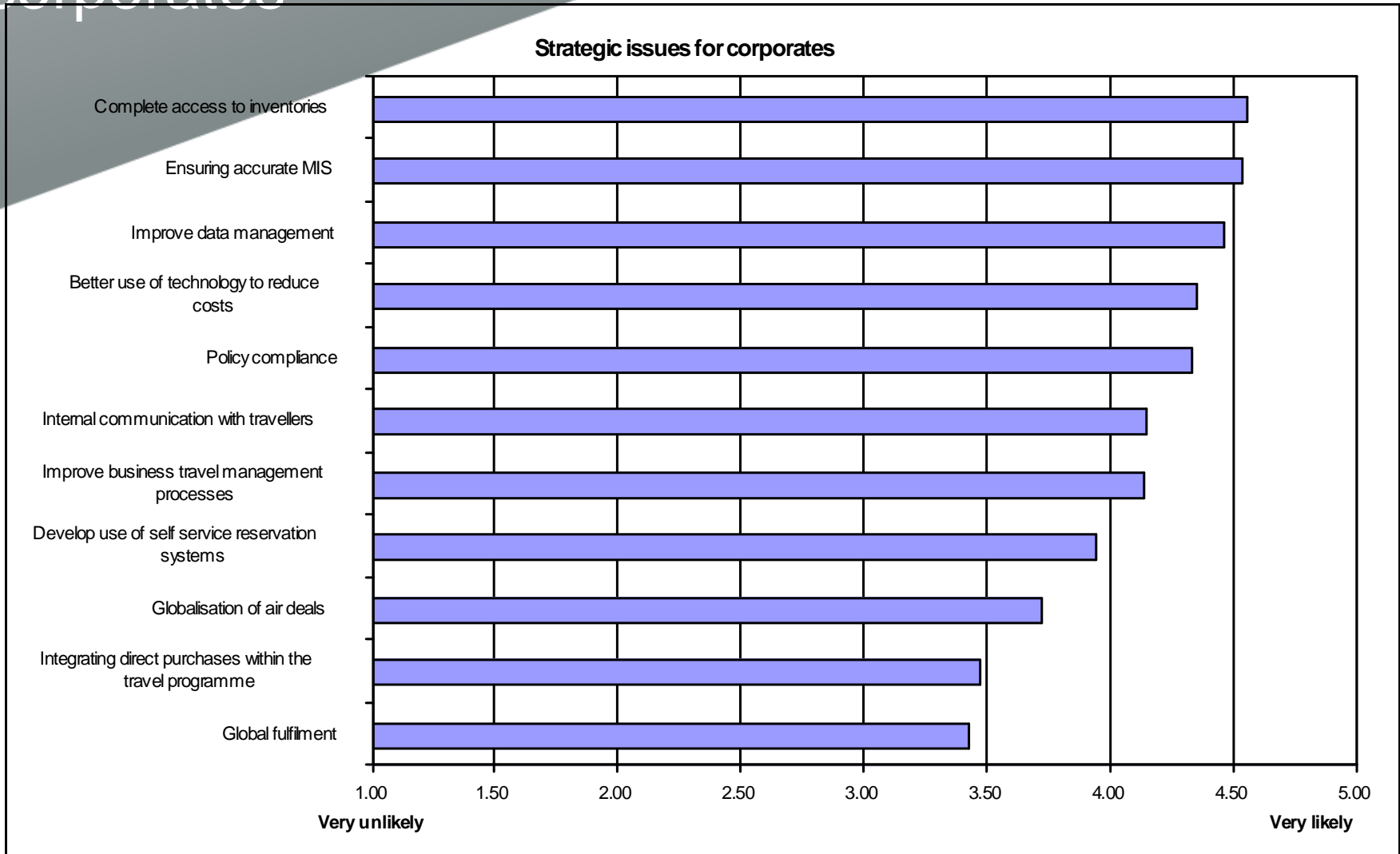
GDS fee structure development	Score
Variable pricing will become the norm	4.88
Pricing based on airline market share in each market	4.13
Channel access based pricing	3.88

Source: Alamdari and Mason, 2004

GDS New Fee Structures

- In US GDSs were deregulated in 2003
- DCA3 (Direct connect access for 3yrs) agreements expired 2006
- Sabre, Travelport and Amadeus have new full content agreements with all of the US majors.
 - Agents can “opt in” to work with airline’s preferred GDS
 - Agents get access to content and avoids \$3.50 per segment fees
 - But pay GDS \$0.80 per segment (EAS - Efficient Access Solution)
 - For large TMCs this is taken from the incentive fee the GDS pays have traditionally paid the TMC.
 - Agents can “opt out” and not use airline’s preferred GDS
 - pay the airline a \$3.50 per segment surcharge for any bookings
- TMCs still need access to full content so will pass on any additional costs to travellers in service charges

Strategic issues for corporates



- Travel manager needs to control / manage bookings to try to optimise the spend
- Travellers have more knowledge of prices as they scan the internet
- Travel managers discourage travellers booking on-line

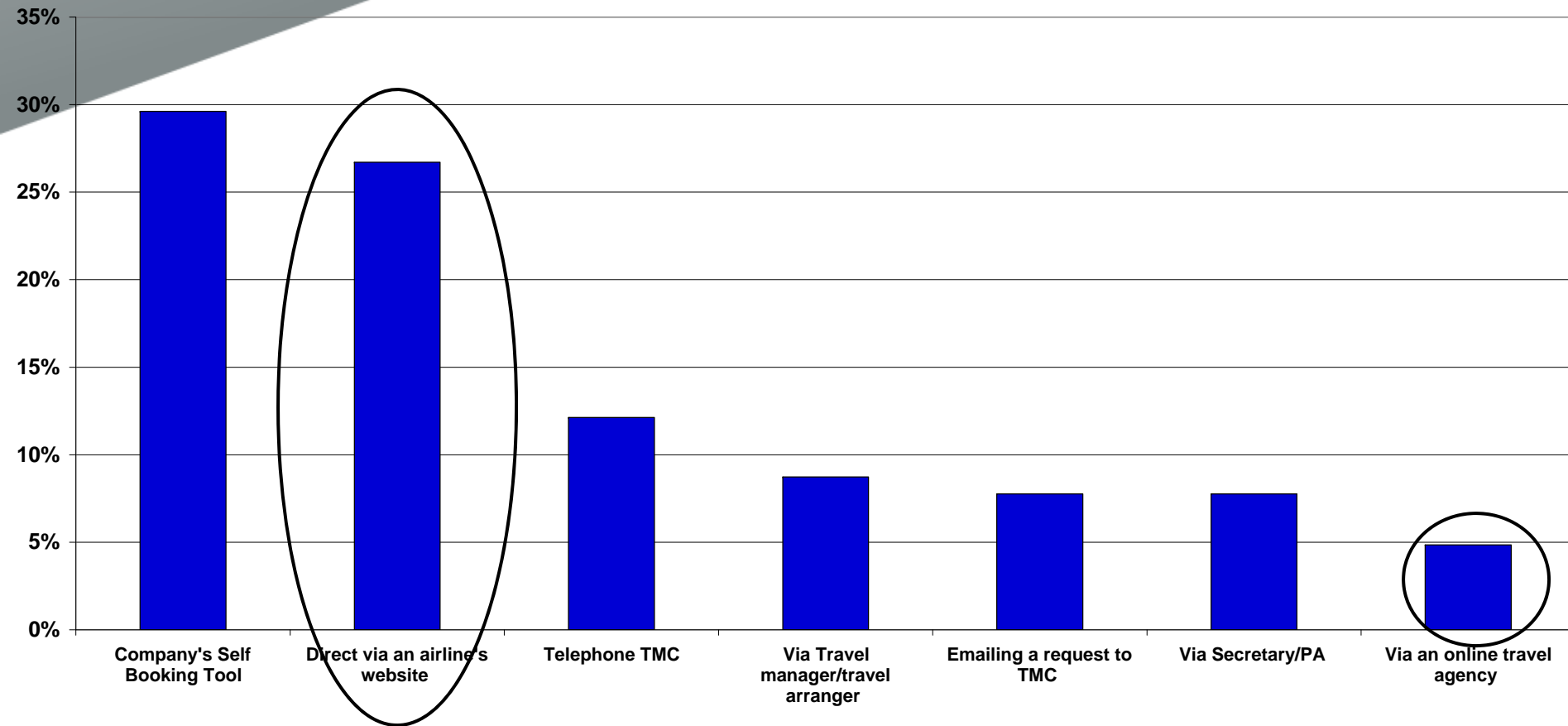
Control of travel spend would be ceded to travellers

Travel managers believe that travellers booking online hinder their role of minimising travel spend for the company

- Also a waste of executive's time

Online usage by business travellers

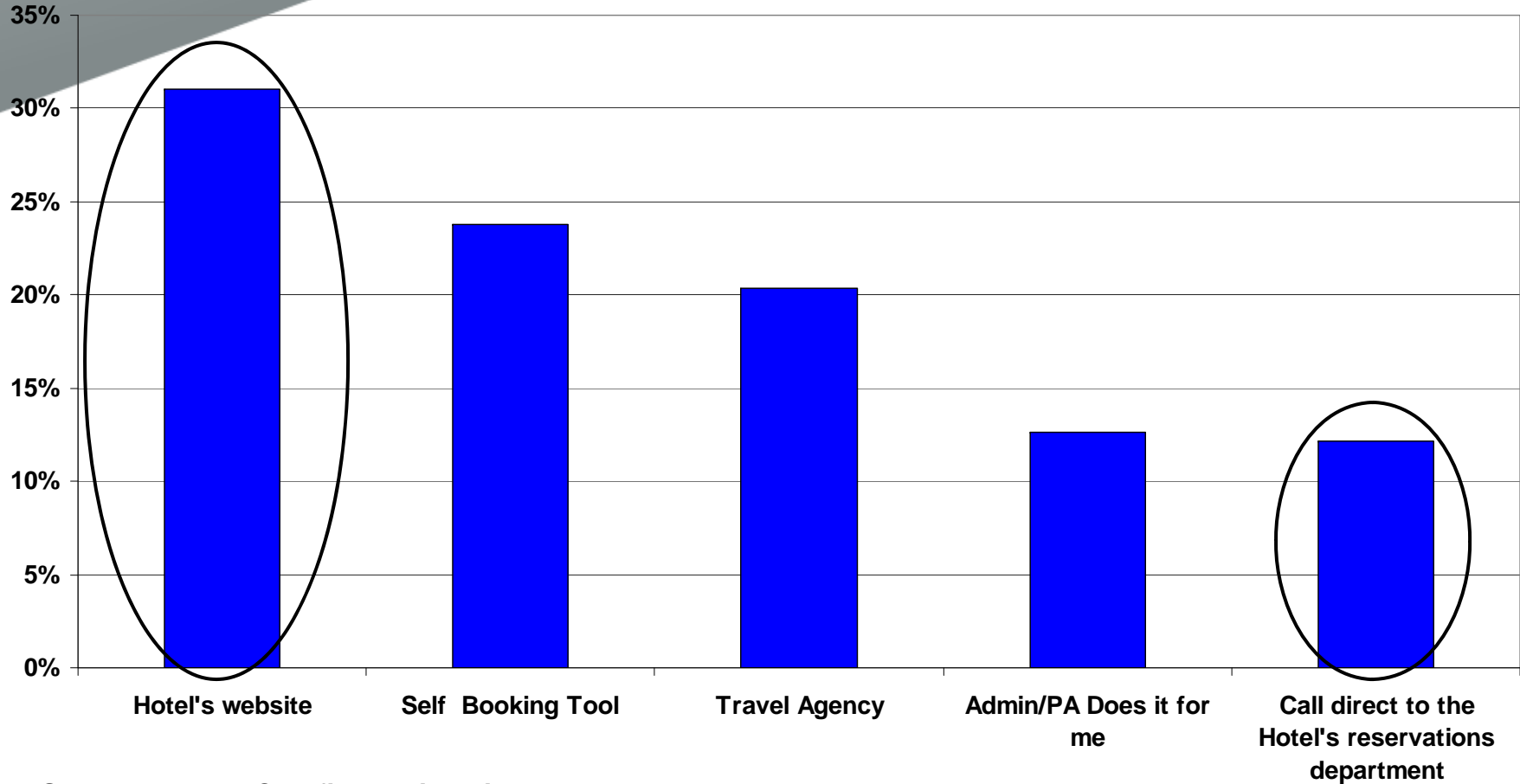
Channel used for last flight taken



Source: Mason, Cranfield University, 2006

Direct channels dominates hotels

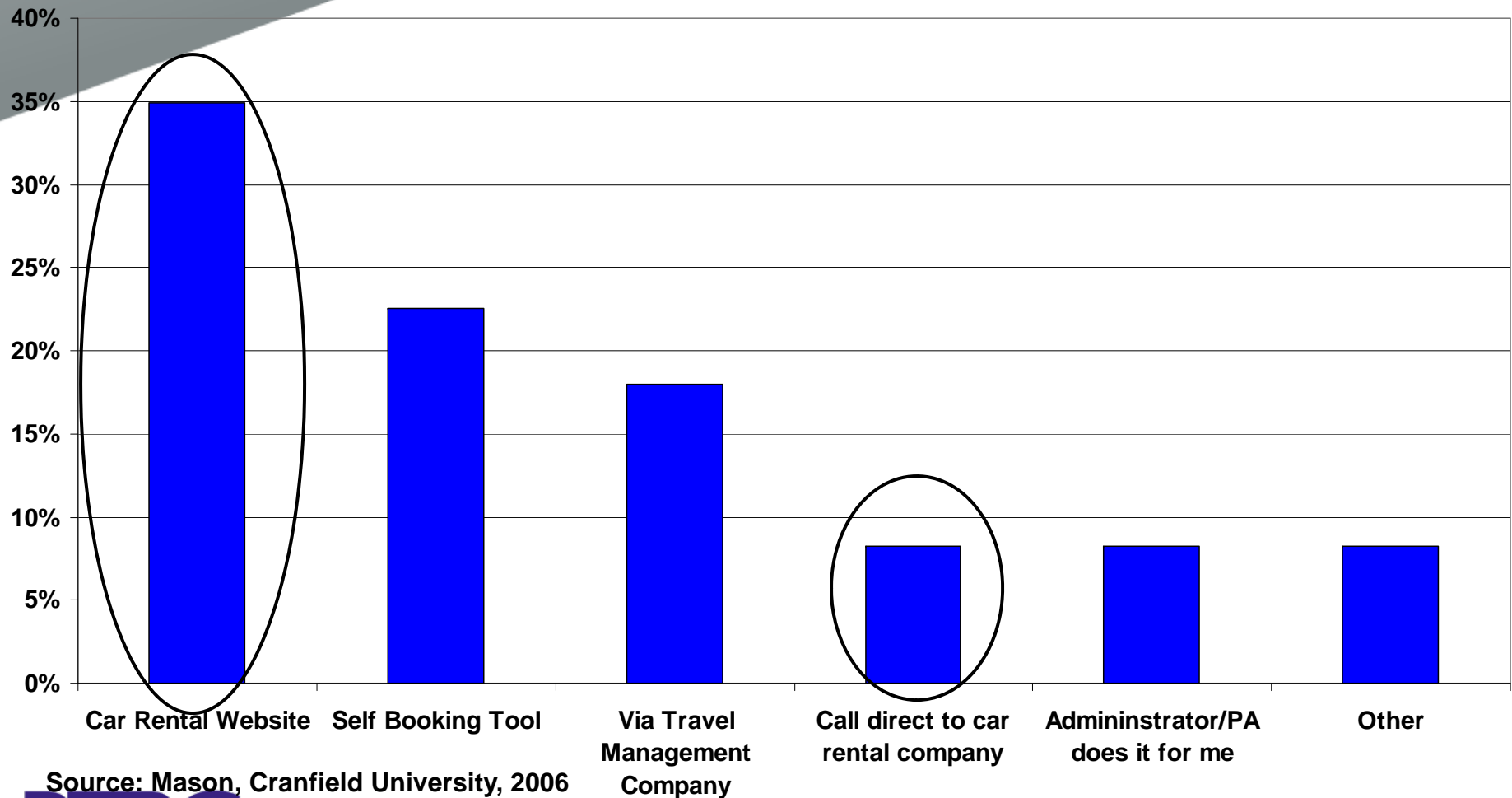
Hotel booking channels



Source: Mason, Cranfield University, 2006

Direct dominates Car Rentals

Car Rental booking channels



Source: Mason, Cranfield University, 2006

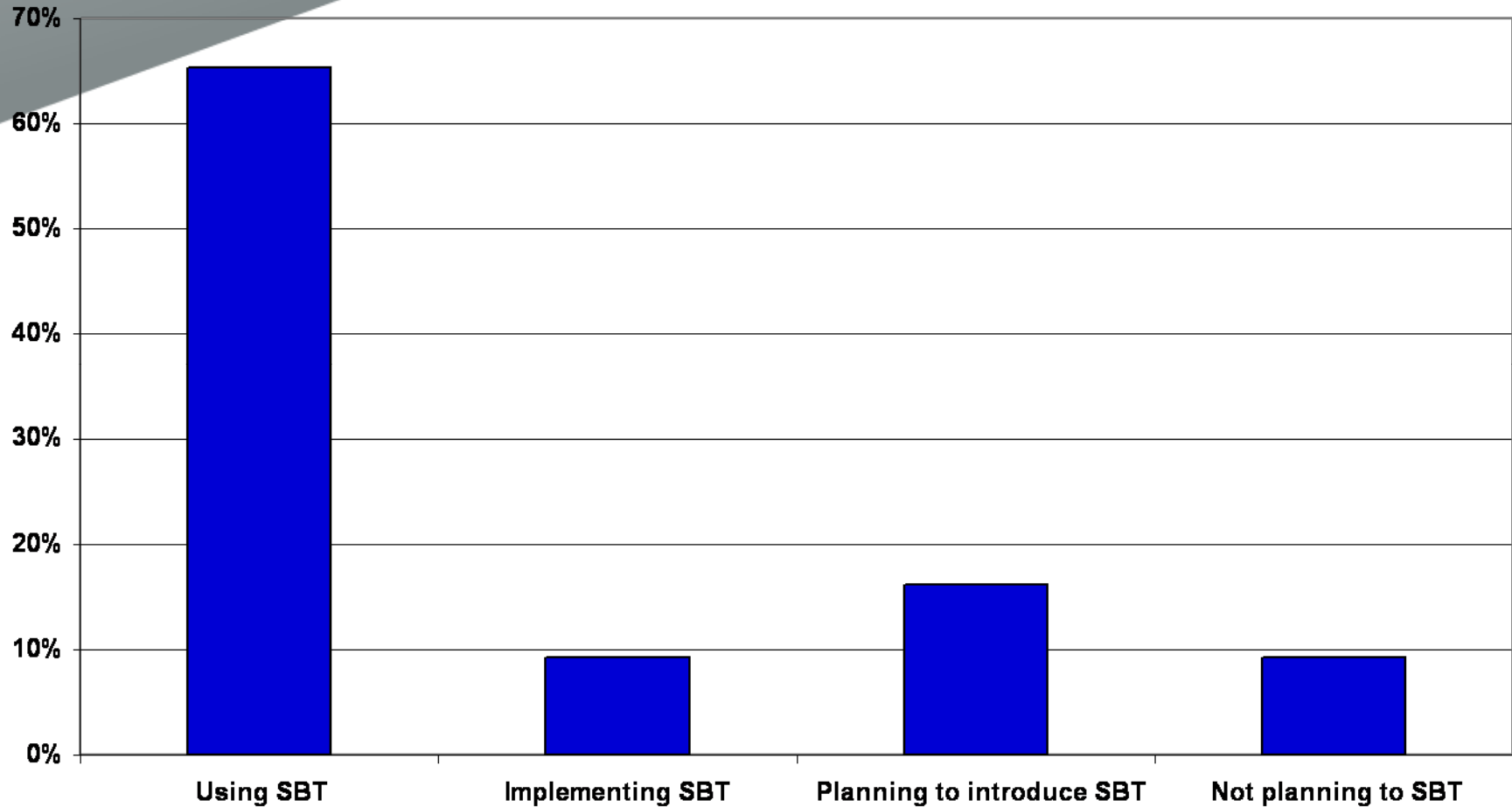
Direct booking may create difficulties

- When a traveller books direct...
 - Loses TMC support on that booking
 - Change tickets
 - Loses Management Information
 - Loses leverage against suppliers
 - May lose volume deals
 - Travel manager can't trace traveller if transport crashes/terrorist attack/act of god
 - Harder to reconcile expenses

Companies using Self Booking Tools

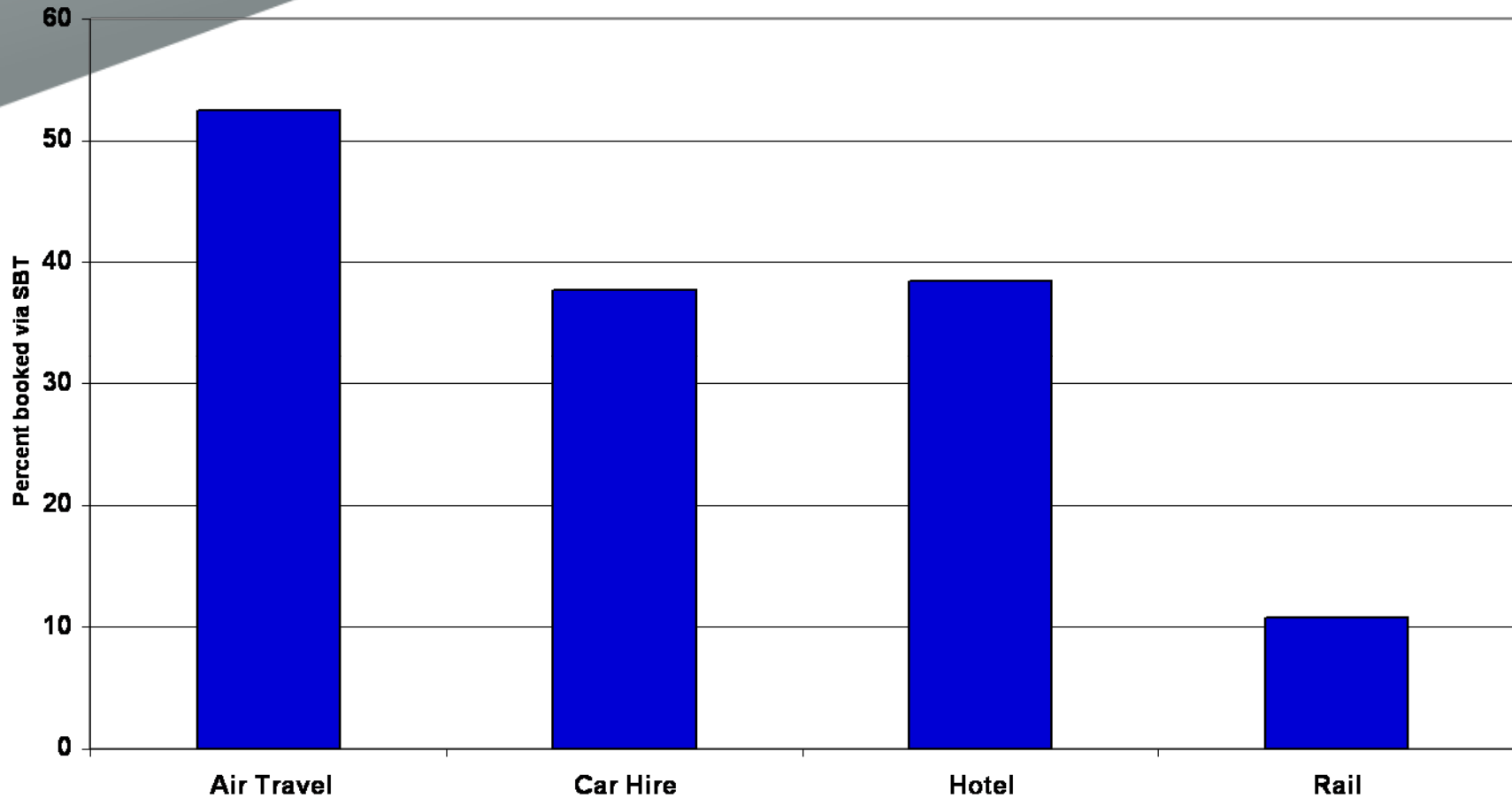
Survey of 424 large corporates

Current Self Book Tool position



SBT booking penetration

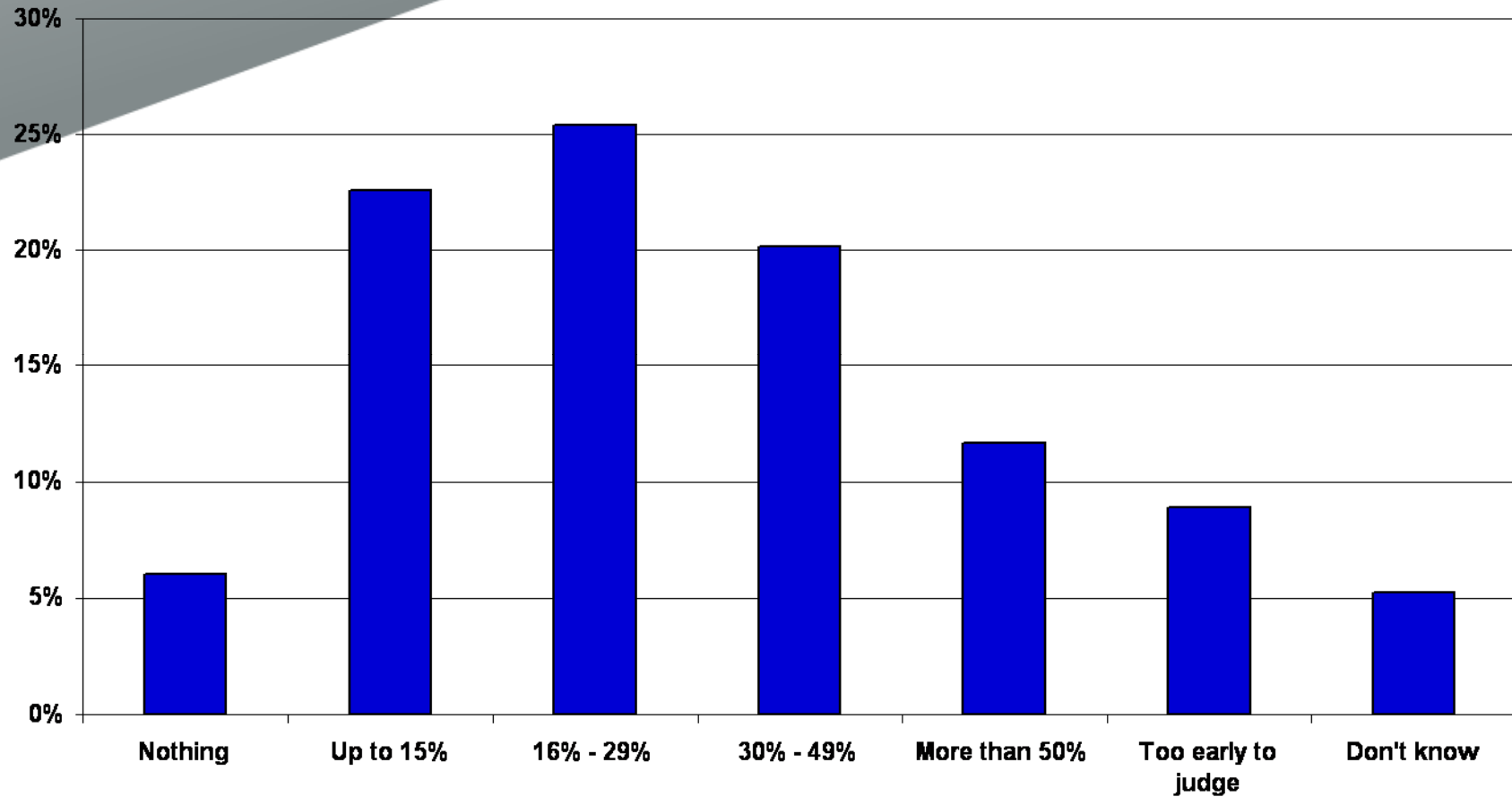
Proportion of bookings made via company SBT



Source: Mason, Cranfield University, 2006

SBT saves TMC costs

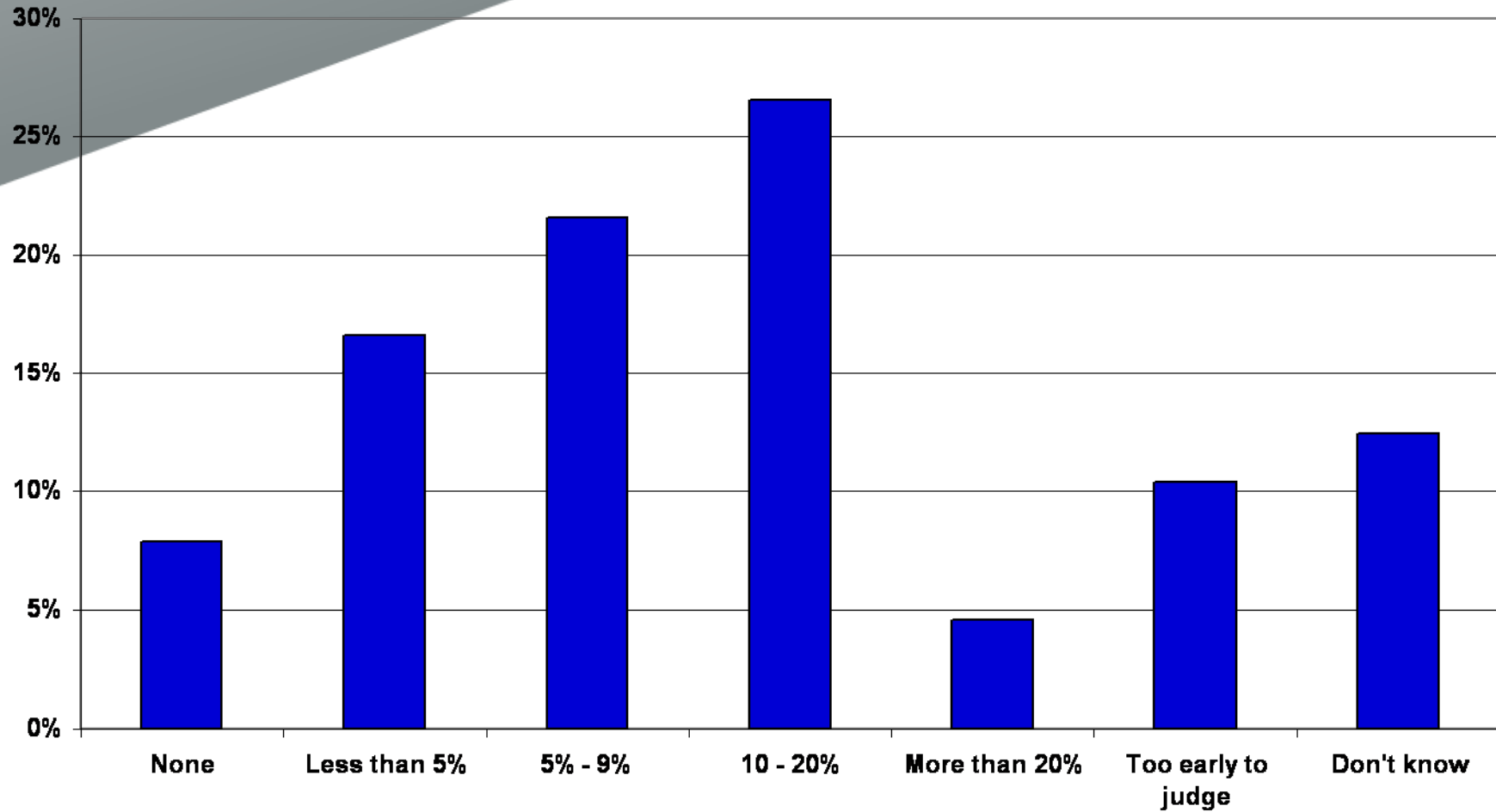
How much does an online booking save in travel agency/TMC costs?



Source: Mason, Cranfield University, 2006

SBTs reduce ticket prices

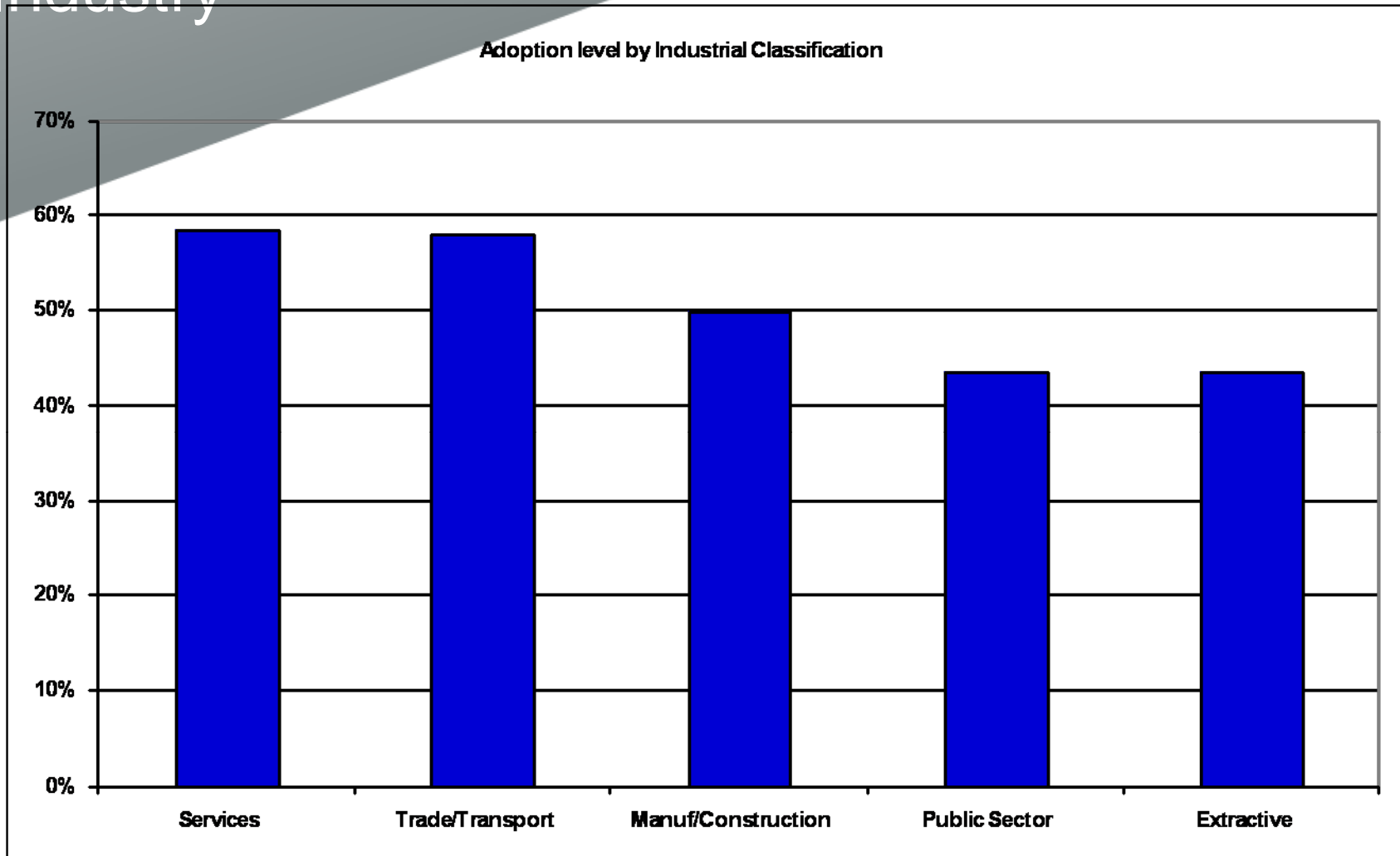
How has use of SBT reduced average ticket prices?



Source: Mason, Cranfield University, 2006

SBT adoption by Industry

Adoption level by Industrial Classification



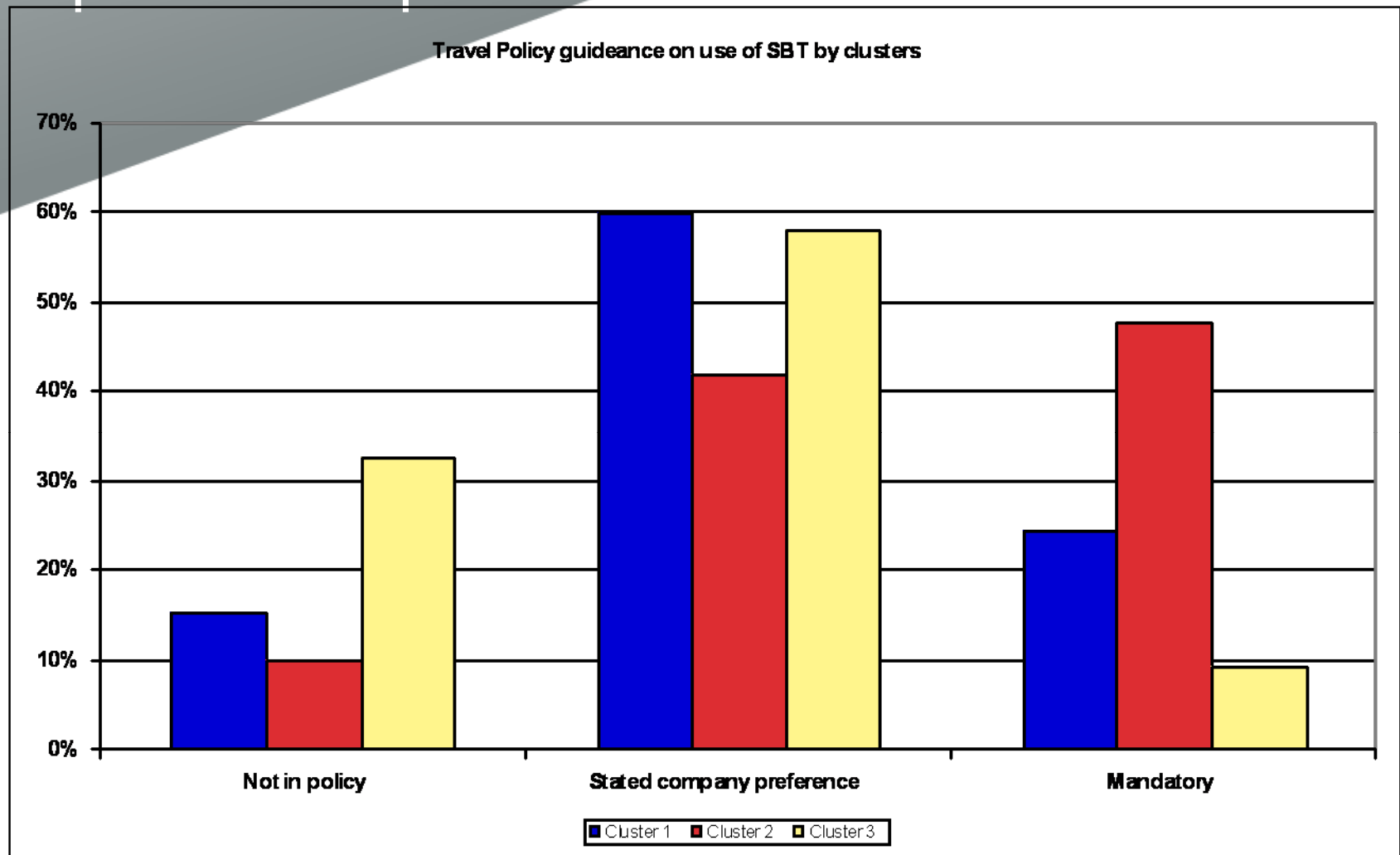
Source: Mason, Cranfield University, 2006

Three different groups of SBT users

	Cluster 1 Š Bureaucratically Hindered	Cluster 2 Š Wholehearted adopters	Cluster 3 Š Laggards in a Brave New World
Proportion of sample	36.7%	39.0%	24.3%
SBT adoption level on Air Travel	44.9%	81.2%	12.3%
SBT adoption level on Hotel bookings	37.1%	57.7%	11.0%
SBT adoption level on Car Hire	31.0%	62.9%	10.8%
Length of SBT implementation (months)	38	42	30
% Increase in adoption per month	2.44%	3.32%	0.82%
Satisfaction with SBT adoption level			
Very Satisfied	9.2%	50.0%	0.0%
Reasonably Satisfied	56.9%	48.5%	18.6%
Rather Disappointed	24.6%	1.5%	48.8%
Very Unhappy	1.5%	0.0%	11.6%

Source: Mason, Cranfield University, 2006

Making SBT mandatory improves adoption



Source: Mason, Cranfield University, 2006

Future of Airline Distribution - 1

- The drive to reduce distribution costs through increasing on-line sales, e-ticketing, self servicing, reducing travel agents commission and battle against GDSs will be an ongoing strategy.
- As US and European airlines have benefited from the savings of distribution costs, carriers from other regions will speed up their move towards distribution revolution to have a similar cost base for competition
- Airline alliances may push for common reservation booking platform
- Internet will continue to revolutionise travel distribution

- Travel agents will see their shares of airline ticket sales gradually deteriorating as a result of the emergence of alternative channels
- Small agents could become under threat due to: less leverage to get good airline deals, the development of IT is too costly, they cannot influence corporate choice
- The market will experience a growing dominance by a handful of large agents (traditional and on-line)
- traditional agency skills with face-to-face contacts have to be complemented by offering specialist services and capabilities to consumers through the internet