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Frequent flyer programs and low-cost airlines: Ongoing hybridization?

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Abstract

This paper provides further evidence of on-going hybridization between airlines business models focusing on frequent flyer programs (FFPs) which were viewed as a typical component within traditional concept of doing business in air services. Confronting list of European low cost airlines which in 2005 had not implemented FFPs we found that eleven airlines within the group analyzed started to use them after 2005. We revealed diversity among FFPs of low cost airlines which confirms a broader role of FFPs out of pure customers loyalty issues covering also issues like product policy, price policy and policy of horizontal cooperation. We discovered main difference between older and newer FFPs of low cost airlines in collecting and rewarding options with regard to services of partnership airlines as well as in implementation of membership levels and purchase of credited units. Evolutionary changes towards mature schemes of FFPs are predicted for low-cost carriers.

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1. Introduction

Frequent flyer programs (FFPs) started their history in 1981 when American Airlines implemented the first frequent flyer program in the US domestic market experiencing first impacts of ongoing liberalization. Following in general the paradigm of customer loyalty scheme known in other industries, in the course of more than thirty years airlines have developed these programs to comprehensive structures with complex market targeting creating in this

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way something what overlaps industry itself and what could lead to a new global business separated relatively out of airlines entities in future (de Boer, & Gudmundsson, 2012). Traditionally, frequent flyer programs were discussed as a typical component of full service network carrier business models which distinguishes legacy carriers against their low cost competitors. Afterwards, academic literature began to raise a question about prospects, risks and implementation guidelines of frequent flyer programs in low-cost airlines (Klophaus, 2005). As low cost airlines are in a state of continuous flux, swing of frequent flyer programs issue towards low cost airlines is strongly argued by observed hybridization between airlines business models (Klophaus, Conrady & Fichert, 2007). Also further interrelated themes like growth limits of being (purely) low cost offering no-frills product to passengers and eliminating services unnecessary for hole air transportation are under investigation nowadays. (de Wit, & Zuidberg, 2012) Our paper is motivated to provide evidence of using frequent flyer programs by airlines which cannot be labeled – at least from historical or perception point of view – as traditional ones or full service network carriers. Comparison of low cost carriers frequent flyer programs with regard to their structures, elements, conditions and features in the US and in Europe is another output of our research Thus, we answered three research questions:

- Can be on-going hybridization of airlines business models in Europe confirmed by frequent flyer programs implementation within low cost airlines?
- How do low cost airlines frequent flyer programs differ mutually?
- Is there any evolution of frequent flyer programs implemented in low cost airlines in time?

Our approach is in line with the statement of Martin, Román & Espino (2011) that FFP is a common strategy of airlines and at the same time a service quality attribute differentiating airlines' product.

2. Methodology

Focusing on low cost airlines and their frequent flyer programs one could argue that low cost concept of airline business model is clear and unambiguous only as an archetype in theory and such theoretical concept of low cost business model can not reflect real and mutually diverse business models through which airlines achieve competitive advantage(s) over competitors. (Tomová, 2013) Therefore, predefinition of low cost carriers was necessary starting point in our research to tackle with frequent flyer programs of carriers within low cost group. We used mainly Klophaus (2005) paper which provided evidence of frequent flyer programs (or other loyalty schemes) in eleven of almost 50 investigated European low cost carriers which that time (i.e. in 2005) 'can be classified as low cost airlines'. Another step required to take into account consolidation forces in industry which led to numerous bankruptcies and mergers changing dramatically a list of airlines suitable for our research. And, to have a reference airlines from market with longer history of liberalization (and hybridization, too) four US low cost carriers AirTran Airways, Frontier Airlines, JetBlue Airways and Southwest Airlines with FFPs yet implemented in 2005 were added to the researched sample.

Table 1. Implementation of FFPs in low cost carriers in Europe: 2005 and 2013 comparison

	2005 (as observed in cited Klophaus paper)	2013 (our observation)	
FFP (or loyalty scheme) implemented	Aer Lingus, Air Berlin Air Scotland, AlpiEagles, Condor, Flybe Helvetic, Maersk Air, Monarch, SnowFlake, Sterling	FFP implemented	<i>Aer Arann</i> , Aer Lingus Air Berlin, Condor, <i>Corendon</i> , Flybe, <i>Germanwings</i> , <i>Jet2</i> , Monarch , <i>Meridiana fly</i> , <i>Norwegian</i> , <i>Spirit Airlines</i> , <i>Swirefly</i> <i>Vueling</i> , <i>Wizz Air</i>
None FFP (or loyalty scheme) implemented	<i>Aer Arann</i> , Air Southwest, Air Wales, bmibaby, BudgetAir, <i>Corendon</i> , dba/Germania Express, globespan, easyJet ,EUjet, Excel Airways, FlyMe, flynordinc, <i>Germanwings</i> , Hapag-Lloyd Express,IcelandSky, InterSky, <i>Jet2</i> , <i>Meridiana</i> fly, MyTravelLite, <i>Norwegian</i> , Ryanair, SkyEurope, Smart Wings, Snalskjutsen, <i>Spirit Airlines</i> , <i>Swirefly</i> , Swedline, Thompsonfly, Transavia, Virgin Express, <i>Vueling</i> , Windjet, <i>Wizz Air</i>	FFP not implemented	easyJet Helvetic Ryanair Smart Wings Thompsonfly Transavia

Source: Klophaus (2005) and authors' findings. Compiled.

Comparability of the lists of airlines contained in Table 1 is relatively limited taking into account that Klophaus (2005) included in his analysis also other customer loyalty schemes and we worked only with implemented frequent flyer programs in our research. For example, Flybe was listed within the group of airlines which implemented FFP or some loyalty scheme in 2005 although FFP in its full sense was implemented by Flybe after 2005. That is a reason why we have decided to list it among low cost airlines which implemented FFP after 2005 in our further analysis. Four US low cost airlines we subsequently included had their frequent flyer programs yet implemented in 2005. None new comer low cost carrier during 2005–2013 was taken into account to keep the sample of European airlines researched ‘the same’. Constriction in number of low cost airlines in ‘the same sample investigated’ was caused by numerous mergers (Maersk Air in 2005, Virgin Express in 2006, Hapag-Lloyd Express in 2007, etc.) and bankruptcies (Eujet in 2005, Sterling in 2008, SkyEurope in 2009, Air Southwest in 2011, etc.) experienced within industry. Another objection can be raised against oneness of airlines analyzed in terms of business model characteristics applied in airlines within the sample. Klophaus, Conrady & Fichert (2007) found (using weighted low cost carrier index methodology) that Ryanair, Corendon, Wizz Air coincide with pure low-cost carrier model (each of them differently identifying only Ryanair as the purest low cost airline of them), while Easyjet, Aer Lingus and Vueling were characterized as airlines within hybrid carrier group with still dominating low-cost elements, then Transavia, Germanwings, Norwegian, Flybe and Meridiana fly were labeled as hybrid carriers with dominating traditional airline business model elements and even Air Berlin according the research cited considerably corresponds to traditional full service carrier business concept. Nevertheless, as it is obvious from Table 1 the list of airlines which can be specified at least as non-traditional (with exception of Air Lingus due to its history) and which built frequent flyer programs into their business models increased considerably in time. To reveal evolutionary trends in frequent flyer programs in non-traditional part of industry we subsequently split our sample to airlines which implemented their frequent flyer programs before 2005 and after 2005.

3. Empirical results

Four fields of frequent flyer programs were kept under review in our investigation:

- Earning (collection) of credited units scheme,
- Rewarding scheme,
- Other advantages (options) within FFPs,
- Other conditions of FFPs.

As frequent flyer programs are unique not only in terms of their structure, mechanism, effectiveness but also language used we followed main framework of FFPs focusing on main features and components on which frequent flyer programs are built up. We did not concern corporate FFPs in our research therefore only frequent flyer programs for individuals were analyzed. Our observations are gathered in Tables 2, 3, 4 and 5 covering the situation as of summer 2013.

With regard to schemes of credited units earning the data contained in Table 1 show that frequent flyer programs reflect overall product and price policy followed by airlines. If product is provided as unbundled, earning of credited units for other airline’s products (for example for on-board amenities) can be expected within frequent flyer scheme. On the other hand, if an airline follows more concept of bundled product like AirBerlin, it influences a scale of earning options. Similarly, when different travel class options are provided to customers, differentiation of customers according to travel class is included within FFPs earning scheme using FFPs also as a driver of price discrimination. Similar effect can be achieved when earning scheme is strictly layed along air ticket price balancing better in this way also revenue contribution of customers to capacities offered freely through FFPs. Differentiation according to destination is another solution in this regard we recorded in some FFPs implemented in low cost airlines.

Clear distinguishing line is observed in earning options within partnerships airlines when comparing FFPs of low cost airlines earlier implemented with those implemented later. FFPs implemented earlier more use services of partnership airlines as an earning option – a factor that reflects an airline’s horizontal cooperation policy as a part of

its business model. Intensification of horizontal cooperation policy influences substantially frequent flyer programs design being undermined by growth stages of airline's life-cycle.

Table 2. Credited units collection schemes in FFPs in analyzed low-cost airlines in 2013

	Low-cost airlines with FFP	(Units credited)	Accumulation of credited units principle	Other options for accumulation through		
				Other airline's services	Services of partnership airlines	Non- airlines partnership
FFP before 2005	AirTran Airways (US)	Credit	Fixed quantity of credits according to travel class	–	–	✓
	Frontier Airlines (US)	Mile	Miles flown x coefficient according to travel class	–	–	✓
	JetBlue Airways (US)	Point	3 points for 1USD spent	✓	✓	✓
	Southwest Airlines (US)	Point	Flight ticket price x number of points according to flight ticket type	–	–	✓
	Aer Lingus*	Point	Fixed points according to travel class and destination	–	✓	–
	Air Berlin	Mile	Number of miles flown x coefficient according to travel class	–	✓	✓
	Condor	Mile	Fixed quantity of miles according to travel class and destination	–	✓	✓
	Monarch	Point	20 points for every 1GBP spent	✓	–	–
	Corendon	Flight	Number of flights bought	–	–	–
	Flybe	Point	Quantity of points according to air ticket price	–	–	–
FFP after 2005	Germanwings	Mile	10 miles for 1 EUR spent	✓	–	✓
	Jet2	Point	1 point for every 1 GBP spent	–	–	–
	Meridiana	Mile	Quantity of miles according to destination	✓	–	✓
	Norwegian	Cash point	Points as a % of air ticket price according to air ticket type	–	–	✓
	Spirit Airlines	Miles	Miles flown x coefficient according to membership levels	–	–	✓
	Sverigeflyg	Point	1 point for every flight	–	–	–
	Vueling	Point	1 point for every 2 EUR spent	–	–	✓
	Wizz Air	Point	2 point for 100 HUF	✓	–	✓

Source: Compiled by authors. ✓ means yes. – means no

* Air Arann is in FFP partnership with Aer Lingus therefore it will not be analyzed separately.

Similarly, as it has been revealed for earning of credited units within FFPs, also rewarding schemes depicted in Table 3 mirror complex role of FFPs in airline’s policy of product, price and horizontal cooperation creating in this way uniqueness of any business model. Comparing a group of airlines with FFPs implemented before 2005 with FFPs implemented later, we have found that rewarding schemes are strongly impacted by policy of horizontal cooperation which may have roots in growth limits for being purely low-cost taking relevant markets through their O-D characteristics. Other options mentioned in Table 3 means airport charges, fuel surcharges etc.

Table 3. Rewarding schemes within FFPs of analyzed low cost airlines in 2013

	Low-cost airlines with FFP	Reward of credited units for flights	Other reward options through			Other options
			Other airline’s services	Partnership Airlines	Non – airline partnership	
FFP before 2005	AirTran Airways (US)	Fixed number of credits according travel class and destination	✓	✓	-	-
	Frontier Airlines (US)	Fixed number of miles according travel class and destination	✓	-	✓	-
	JetBlue Airways (US)	Points demanded when booking flight	-	✓	✓	-
	Southwest Airlines (US)	Price of air ticket x number of points according air ticket type	-	✓	✓	-
	Aer Lingus	Fixed number of travel class and destination	✓	✓	✓	-
	Air Berlin	Fixed number of miles	✓	✓	✓	✓
	Condor	Fixed number of miles according travel class and destination	✓	✓	✓	✓
	Monarch	Fixed number of points according destination	-	-	-	-
	Corendon	% discount from product price	✓	-	✓	-
	Flybe	Fixed points according to destination	✓	-	-	-
FFP after 2005	Germanwings	Fixed number of miles	-	✓	-	-
	Jet2	Fixed number of points according to destination	-	-	-	✓
	Meridiana	Fixed number of points according to destination	✓	-	✓	-
	Norwegian	1 NOK=1 point	-	-	-	-
	Spirit Airlines	Fixed number of points according to air ticket type and destination	-	-	-	-
	Sverigeflyg	Fixed number of points	-	-	✓	-
	Vueling	Fixed number of points according to air ticket type	-	-	-	-
	Wizz Air	1 HUF=1point	✓	-	-	✓

Source: Compiled by authors.

As for other features of frequent flyer programs on which they are built up, again a high level of diversity is typical for frequent flyer programs analysed in all investigated aspects such as black days, retrospective crediting, purchase of credited units, credit cards, cancellation conditions etc. Main dividing line between frequent flyer programs implemented earlier and later is seen in purchase of credited units and membership levels. Our findings show that frequent flyer programs are differently mature thus confirming clear-cut evolutionary tendency of frequent flyer programs within low-cost business model towards more complex and intricate structures.

Table 4. Other features in frequent flyer programs of analyzed low cost airlines in 2013. *Source:* Compiled by authors

	Low cost airlines with FFP	Membership Levels	Purchase of credited units	Credit card	Validity of credited units	Cancellation announced in advance	Retrospective crediting during	Blackout days
FFP before 2005	AirTran Airways (US)	✓	–	✓	12 months	no	3 months	✓
	Frontier Airlines (US)	✓	–	✓	at least one account activity during 18 months	no	180 days	✓
	JetBlue Airways (US)	✓	✓	✓	at least one account activity during 12 months	no	90 days	–
	Southwest Airlines (US)	✓	✓	✓	according validity of account	30 days	12 months	–
	Aer Lingus	✓	✓	✓	36 months	6 months	3 months	✓
	Air Berlin	✓	✓	✓	36 months	2 weeks	12 months	✓
	Condor	✓	–	–	36 months	no	90 days	✓
	Monarch	✓	✓	✓	36 months	6 months	6 months	✓
FFP after 2005	Corendon	✓	–	–	12 months	with announcement but not specified	no	–
	Flybe	–	–	✓	2 years	3 months	3 months	✓
	Germanwings	–	–	–	2 years	2 weeks	3 months	✓
	Jet2	–	–	–	2 years	6 months	28 days	✓
	Meridiana	✓	–	✓	2 years plus rest of the starting year	no	4 months	✓
	Norwegian	–	–	–	end of the	n.a.	no	n.a.
	Spirit Airlines	✓	–	✓	at least one activity during 3 months	no		✓
	Sverigeflyg	–	–	–	n.a.	n.a.	n.a.	n.a.
	Vueling	–	–	✓	3 years	no	90 days	–
	Wizz Air	–	–	✓	n.a.	n.a.	n.a.	–

The analyzed airlines differ also in the way how they make their frequent flyer programs eligible for their customers. Eligibility of frequent flyer programs is done by flights threshold which is necessary to be fulfilled for entering the program. Within the groups of analyzed airlines we have found this condition only in Aer Lingus and Monarch and in Corendon and Jet2 which indicates that this frequent flyer programs feature is not principally distinguishing feature between airlines which implemented their frequent flyer programs before and after 2005. Therefore, we can conclude that so called qualified flights are not typical for frequent flyer programs of airlines belonging to low cost (or hybrid) group what can be argued by their maturity, market share and fleet capacity reasons. Our analysis also did not reveal principal differences in the ways through which frequent flyer programs of more mature low cost or hybrid airlines in the US and EU are built.

5. Conclusions

Our investigation of frequent flyer programs within a group of eighteen air carriers which were traditionally labeled as low-cost indicates that frequent flyer programs ceased from being exclusively a part of full service network carriers world. Within a period of eight years frequent flyer programs were captured into the business models by further eleven European low-cost airlines, giving considerable increase against status quo in 2005. This finding is in line with Klopheus's (2005) prediction that the European market in low cost segment is radically changing what can be proved by numerous takeovers, bankruptcies and mergers and departing from being only aggressive low cost. Within a period of seven years between 2005 and 2012 Virgin Express, MyTravelLite, Maersk Air, Iceland Express, Hapag-Lloyd Express etc. were merged with other airlines companies while Air Scotland, Sterling, BudgetAir, SkyEurope, Snalskjutsen, Swedline, Windjet, FlyMe, Excel Airways etc. were bankrupt. Some low cost daughters of legacy network carriers were cancelled by their parent companies like Snowflake by SAS. Sharpening competition really brought re-evaluation of business models within a group of low-cost carriers as it was anticipated by Klopheus (2005) and low cost carriers started to use other service feature to differentiate themselves by product characteristics, frequent flyer programs including.

Moreover, we have revealed in this paper not only ongoing implementation of frequent flyer programs within this group of carriers but also their evolution in time what can be seen as a further evidence of airlines going hybrid. Frequent flyer programs of airlines which have implemented some drivers of full service network airlines business models are evolving in time towards structures that are very similar to frequent flyer programs of full service network carriers, i.e. legacy airlines. We have tested the fact within our research using information on frequent flyer programs of American Airlines, Lufthansa, United Airlines and SAS. Our conclusion about evolutionary tendencies in frequent flyer programs of low cost airlines is knotting on Klopheus (2005) statement about smaller complexity of frequent flyer programs if they are implemented in low cost carriers in comparison with those frequent flyer programs implemented in legacy network ones. This fact – on the other hand – bears on ongoing changes in airlines business models and simultaneously evolution of new 'hybridized' airlines business models.

Some researchers (Klopheus, Conrady & Fichert, 2012) explicitly consider frequent flyer program as a component of full service network carrier business model and use it as one of distinguishing factors in their new typology of airlines business models which contains also hybrid ones. However, as we discovered in this paper, overall concept of frequent flyer programs is not only an issue of customer loyalty because it reflects more broadly overall airlines product and price policies and policy of horizontal cooperation which are necessarily constituents of any airlines business model. Therefore, not only frequent flyer programs presence as the authors mentioned do in their paper but also configuration of frequent flyer programs can be seen as a distinguishing factor when describing airlines business models to specify their typology.

Another question that can be risen in this connection is about financial impacts of frequent flyer programs on unit costs and unit revenue (yield) ratios of airlines. In general, legacy network airlines and their low cost competitors use different business models to position themselves differently with regard to unit costs and unit revenue (yield) ratios. Low cost carriers compete by product/price concept of business model based on lower unit costs levels and consequently lower prices (lower yield) offering product without frills. By contraries, legacy full service network carriers compete by product/price concept of business models stemming from higher unit cost levels reflecting higher product quality and consequently higher yield. Analyzing airlines business models through costs and revenues ratios, some researchers like Mason & Morrison (2008), Lohmann & Koo (2012) and Daraban (2012) work with frequent flyer programs only indirectly as the indicators on both cost and revenue sides are without any doubt influenced also by frequent flyer programs. However, current research does not answer sufficiently a quantitative question how frequent flyer programs influence airlines unit costs and unit revenue ratios although – as we have yet mentioned – frequent flyer programs may be more or less implicitly present in levels of such costs and revenues ratios. Such analysis could come up with research of efficiency of different frequent flyer programs in different stages of their evolution what is partially also an issue of different airlines business models positioned along with whole spectrum, hybrid or hybridized business models including. In broader thread, the risen question is about individualization or customization in airlines industry and new future airlines strategies not regarding whether their origin is in traditional (full service network) doing business concept or not.

Thus, our empirical findings confirm diversity among airlines frequent flyer programs within low-cost or hybrid airlines, a fact which among other ones reflects that (some) airlines are not only going hybrid, but (all) airlines going differently through their differentiated, i.e. unique business models. Uniqueness of business models (as well as uniqueness of frequent flyer programs) calls for more research in future airlines strategies underlined by sound business models capable to compete to survive in the market.

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