

Why do budget airlines offer free loyalty cards to regular customers?

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Abstract:

The purpose of this paper is to understand the benefits to both the consumer and the supplier of budget airlines providing free loyalty cards. It has always been the case that luxury airlines offer loyalty cards to frequent flyers; offering upgrades, priority queuing and access to lounge areas; but this essay explores why budget airlines recently adopted a similar strategy, when their customers are primarily interested in price. I have decided to explore the reasons behind the consumer's choice when it comes to selecting an airline and the consequences faced by the suppliers that have caused them to adopt this new marketing technique.

Economic principles:

This essay uses the following economic principles: Firstly, it looks at the utility faced by the consumer when comparing two different budget airline flights and the opportunity costs associated with each. It also looks at the opportunity costs faced by the supplier when deciding to supply loyalty cards, as well as the short-term costs relative to the long-term benefits. Here, the market for budget airlines are in perfect competition, meaning flights are often very similar in price. This essay, therefore, looks into the impact on added utility created by loyalty cards to the consumer and the financial benefits to the supplier.

Introduction:

There are many differences between flying on a budget and a luxury airline; one of the main factors being price. Low cost airlines such as Easyjet and Ryanair offer a no-frills flight to those who are looking to get from A to B as inexpensively as possible. They primarily sell to customers who shop around and who choose to fly due to the cheaper price offered. This is contrary to those who book with a luxury airline, for example British Airways; these customers tend to book the luxury option due to the brand and the plush frills offered in addition to the basic flight.

Taking this into consideration, it seems worthless at first for budget airlines to offer loyalty cards to regular customers when most are only 'regular' due to the competitive price frequently offered. It simply appears to be an added cost to the

airline; most of these typical customers would still only chose the airline if it remained competitive; therefore it's useless to the consumer.

The customer:

It wasn't until I personally acquired a loyalty card myself that I began to understand the benefits to both the airline and the consumer. The benefits to the customer are highlighted when comparing two very similar priced flights, where the airline providing the loyalty card, say flight A, is marginally more expensive. We're currently in an economy whereby a large percentage of the population want to ensure they receive value for money; if a business isn't offering the cheapest price we require something of extra value.

As more entrants enter the low cost airline business and as other airlines are forced to reduce prices and become more cost efficient, competing on cost/price alone becomes less sustainable (Lawton and Solomko 2005). With Ryanair and Southwest Airlines dominating as price leaders in Europe and the US, other low cost airlines are forced to look to new methods and broaden their business model by incorporating other emphases; in EasyJet's case, loyalty cards.

Without the introduction of the loyalty card, most price-aware consumers would maximise utility by choosing the cheaper option, flight B. However, upon the introduction of the loyalty card, which offers free flight changes, date changes and passenger detail changes, it becomes clear that there are opportunity costs

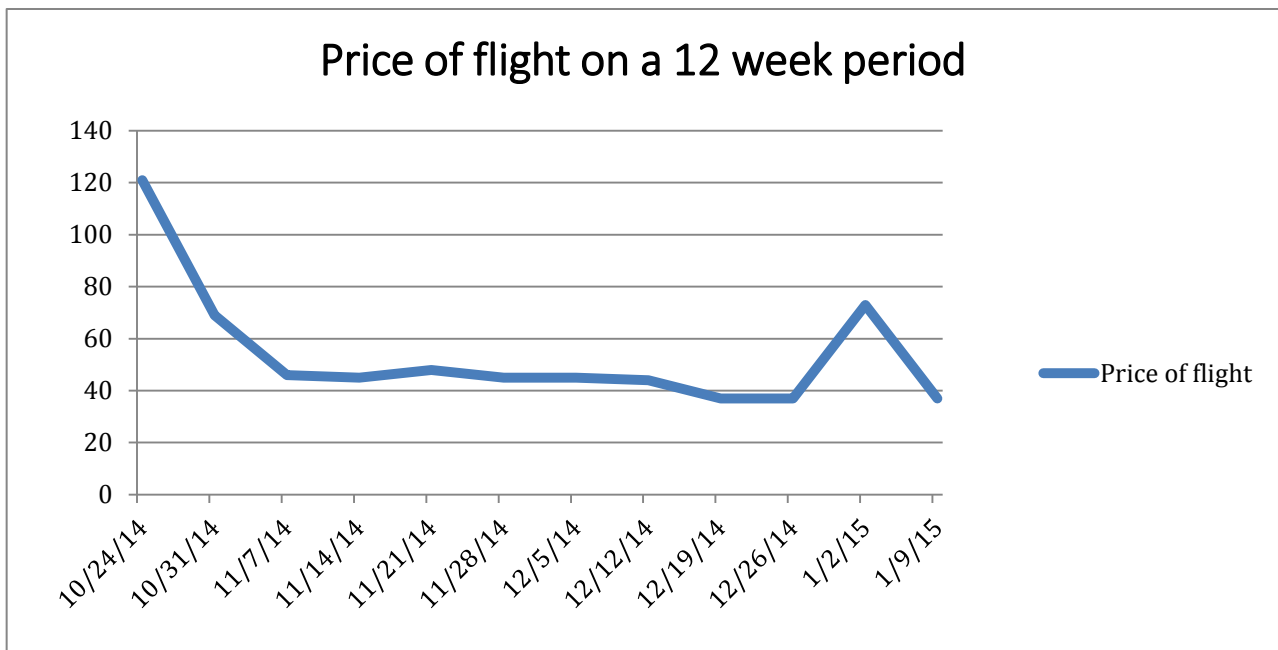
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associated with each flight as each involve sacrifices by choosing one over another (Sloman et al. 2012).

For instance, by choosing flight A, there is an opportunity cost of the added price (for this example say £10) which could be saved and spent on something alternative.

However, if the consumer chooses to purchase flight B, then there are also opportunity costs; in this case the opportunity costs involve risk. If the consumer has to change, or alter their flight they may face charges of around £30. Then, taking the £10 flight discount away from the £30 for possible incurred costs leaves an opportunity cost of £20, twice as much as that of flight A.

It further becomes clear when understanding the free date change service available on flight A and booking in advance. The prices of flights tend to generally be cheaper the further in advance you book. Therefore, by having the option to change a flight, the consumer can book a flight in advance, even if they aren't entirely sure whether they will be requiring its services. To understand this fully I have looked into the prices of a single flight from Edinburgh to London Stansted on a Friday at 17:15 along a 12-week period, all of which were recorded on the same day.



This research shows a steady decline on price, other than the peak over the New Year weekend, as the further in advance you purchase tickets, the cheaper they become. This has a huge advantage to the consumer if they know in advance when they are travelling, as they can book early. However, it becomes a problem to those who are uncertain when they are travelling, causing those passengers to book last minute; which is often the case for business travellers. EasyJet currently have 6.5 million business travellers a year, which account for almost 20% their annual passengers. (McCall n.d.)

These business travellers, who are often frequent flyers, can now take advantage of the free date change to book a flight that they require in the future but may not be certain on. They can then, if necessary, change the date of the flight last minute if the flight is no longer required.

The advantages to the consumer are therefore made apparent; from the added utility included in the less risky flight option, to the huge price advantage from advanced booking, means loyalty cards are most certainly a benefit to the consumer.

The supplier:

After understanding the benefits to the consumer, the benefits from the supplier's perspective become unclear. Why would they offer free date changes when it could potentially lose them income? This is not only due to the loss of income from the reduced flight price but, furthermore, if the ticket is altered last minute the company may not resell the ticket for the original date - meaning a lack of income completely.

Like the consumer, the supplier faces opportunity costs when selling the flights. If the supplier chooses to introduce loyalty cards, it effectively adds risk to the supplier for a small return. Nevertheless, for the airline this isn't an issue. The risk of the passenger changing their flight causes minimal costs to the airline. For the supplier, a simple change on their system is all that's required. Yet it immensely benefits the supplier by encouraging customers to book with them.

Furthermore, the supplier tends not to lose income from the altered flight as the consumer pays for the difference in price if the new flight is more expensive. The original flight can then be sold on for a more expensive price, as it will be sold closer to the date of flight.

The main cost for the supplier offering a loyalty card is the loss of income normally generated from changing flights. Airlines like Easyjet charge 'normal' customers a fee of £35 to alter any information on their flight. This loss of income, however, is inferior to the gain in customer satisfaction, and consequently customer loyalty. The short-term costs of loss of income are far outweighed by the long-term benefits of increased customers.

The idea of this loyalty system is mainly aimed at business users; the types of customers who travel regularly to the same locations. EasyJet can target their loyalty cards to these customers as they can be easily identified from their flight history. EasyJet can therefore compete with more expensive airlines, whose target market is often business users, by offering competitive advantages. Many travellers perceive budget airlines to be unreliable, with frequent schedule changes (Chiam et al. 2008) However, with the new loyalty card scheme, consumers who would normally choose a more expensive flight over the budget choice will feel like the company is more reliable, as loyalty is encouraged and rewarded. This will increase the airline's pool of potential customers, thus dramatically increasing revenue.

Conclusion:

From my research it is therefore clear that budget airlines offering loyalty cards to customers is beneficial to both the consumer and the supplier. For those consumers whose only concern lies with price, it makes no difference to their decision; they

always have the option to shop around to find a cheaper flight with an alternative airline. On the other hand, for those who are price-conscious but also want convenience, there is now the option to increase their utility by having the reduced risk as well as a cheap flight. This specifically aids frequent flyers who are often unsure of when they are travelling, or whose dates of travel are likely to change. In contrast, for the supplier the loyalty card encourages frequent flyers to stay loyal, and also encourages occasional flyers to choose their airline over another in order to receive these added perks. The lack of income normally associated with the benefits which are now given for free are inferior to the increased customer base and customer loyalty gained in the long run.

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