

Changing Channels: Airline Distribution

Distribution has mostly been a good news story for the world's airlines. But the story isn't finished.

They say it's not only what you know but who you know. Airlines have another maxim even more central to the industry's financial fate: It's not just what you sell. It's where you sell it.

During the past decade, the critically important task of selling airline tickets hasn't gotten less complicated. In fact, the channels through which tickets are sold have multiplied, with the distribution strategies airlines use becoming more varied, nuanced, occasionally controversial and even confrontational. But this much is clear: airline ticket distribution has become remarkably less expensive and more productive.

The numbers speak for themselves. In 2009, 75% of Southwest's ticket sales came through its website, the lowest cost of all sales channels, up from 25% in 2000. In 1999, Continental earned \$165m from sales through its website. By 2009

that figure reached \$3.2b. In 2008, IATA remarked that the industry as a whole saw sales and distribution unit costs decline by 13% since 2001. In the critical period from 1996 to 2001 in the U.S., when airline websites were taking off, GDS fees rose 31%, according to a study conducted by the GAO. But in roughly that same period, the percentage of people booking on airline websites rose from 7% to 30%. Google pointed out earlier this month that the figure is now about 50%.

While airplanes and workers have also become more efficient in the past decade, nothing has fallen in price so consistently as distribution-related outlays. And for an industry that's experienced a painful spike in fuel prices, this distribution deflation has proved critical to the industry's fortunes.

Better yet, distribution should continue to contribute positively to the airline industry's health. Changes are currently under way that could provide airlines with additional cost benefits, stemming from greater negotiating power with third parties, new computing technology and potentially new entrant intermediaries that promise more direct (and thus lower cost) links between airlines and their highest paying customers.

Perhaps even more importantly, new trends in the area of distribution point not just to further cost wins for airlines but also imminent revenue gains. The industry's hugely important ancillary revolution, for example, already sees airlines generating lots of new revenue inflight, lots of new revenue at

See also:

- The US Airways experience, below
- Credit card merchant fees, p. 2
- Social media, p. 3

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Distribution: One Airline's Experience

To examine just how much airline distribution has changed in the past two decades, *Airline Weekly* scrutinized the annual reports of one carrier, US Airways, through the years. To begin, start in 1993. That year, US Air (as it was then known) generated most of its ticket revenue from travel agents and even owned 11% of what would become the Galileo reservation system. Like the rest of the U.S. industry, it paid travel agencies a standard commission worth 10% of ticket prices.

A big change happened in 1995. That year, US Air and others kept the standard 10% payout but capped the total amount paid to \$25 for a one-way flight or \$50 for a round trip. Agencies, incidentally, responded with a lawsuit alleging that airlines illegally colluded. That same year, US Air closed a reservation center in Reno, Nev.; introduced a personal computer booking tool called Priority TravelWorks and said it was exploring two new technologies: electronic ticketing and airport kiosks.

By 1997, the renamed US Airways lowered its agency base commission from 10% to 8% while keeping total

payout caps in place. The next year, it replaced Priority TravelWorks with a website capable of handling bookings. At the time, travel agents still accounted for 74% of the carrier's ticket sales.

More changes came in 1999. E-ticketing represented more than half of all sales and US Airways sold its 7% stake in Galileo. Internet booking was in its infancy, with about 6% of bookings coming from online sources, half of these from its own website and most of the rest from a young headline-grabbing online travel agency (OTA) called Priceline. And in October 1999, travel agency commissions dropped again, this time from 8% to 5%.

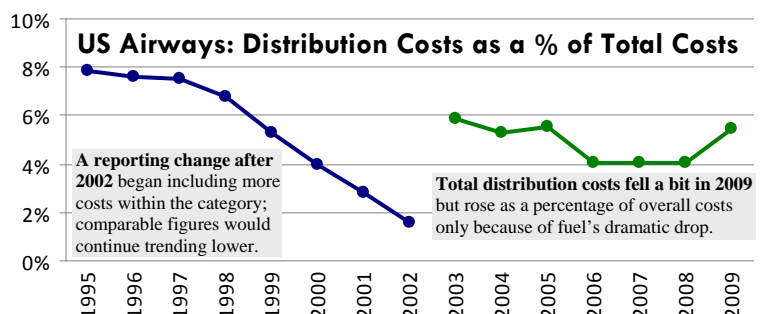
As late as 2000, travel agents still booked the vast majority of all US Airways tickets. But online bookings had grown to 11% and a number of agreements with new online travel agencies were signed.

In 2002, the airline eradicated agency base commissions entirely, leaving "overrides" (commissions paid to agencies for hitting certain performance targets) as the only

payouts left. No surprise, then, that commissions as a percentage of overall operating expenses fell from more than 8% in 1993 to less than 2% in 2003. Internet bookings rose to 20% of the total, about half from usairways.com and half from OTAs. E-tickets, meanwhile, rose to 90% of the total, boosted by a new \$25 fee for non-elite travelers still using paper.

Interestingly, US Airways commented at the time that just as traditional agency bookings were becoming less expensive due to commission cuts, OTA bookings were becoming more expensive. OTAs could charge extra for preferential display placements, unlike the regulated GDSs.

But that changed too with GDS deregulation in 2004, opening new opportunities to negotiate lower transaction fees. Merging with America West added to the airline's bargaining power, and by 2006, selling costs had dropped by \$49m y/y. Two years later, usairways.com reached 25% of total sales while OTAs contributed another 32%. Also in 2008, the company levied fees for bookings made through its call center or ticket offices. And last year, the ever-evolving US Airways got 27% of bookings from its website, 5% through other internal channels and a full 36% from OTAs. What will these figures look like in future years? ◉



Card-Carrying Costs

Airlines complain about credit card processing costs but must be careful what they wish for

Yes, overall airline distribution costs have dropped dramatically during the past two decades. But one subset of those costs has continued to rise: the fees paid by airlines to process credit card transactions.

When people purchased tickets in person at a city ticket office or local travel agency, they often paid with cash or a personal check, especially in the years before credit cards proliferated in many global regions. Online purchases, on the other hand, require an electronic form of payment, which more often than not means a credit card.

Consumers are happy to pay with credit cards, especially in countries like the U.S. where they can't be charged extra for using them and often get rewards for doing so—maybe even miles on the airline from which they are purchasing tickets. But airlines pay dearly for the convenience—sometimes more than \$2 for every \$100 charged.

An economist would point out that by definition, airlines pay the fees because doing so is worth it. Still, airlines complain that 2% of revenue is out of proportion with the value delivered considering all the other costs that go into providing air travel.

With the help of other vendors, airlines are fighting back. Many accept payments via PayPal, an online platform first popularized among eBay users to exchange money but which also cuts airlines' transaction costs in about half compared to credit cards. A company called Acculynk produces a system that enables PIN-based internet transactions using debit cards. In many cases, these same "check cards" can be used for either PIN-based transactions (traditionally a keypad at an automated teller or retail store) or as "credit" cards, even though no revolving credit is provided—but PIN-based transactions, until recently not possible online, cost only about half as much to process as transactions that go through the credit card networks. And airlines themselves have long owned the Universal Air Travel Plan, or UATP, which enables low-cost transactions for airlines that accept its card.

Some countries, Australia most notable among them, have strictly limited the fees that credit card networks can charge merchants such as airlines. Fees there are about a quarter of what they are in less regulated countries. The U.S. Senate is considering similar legislation. Airlines should cheer moves like that, right?

Not necessarily.

A dirty little secret is that airline complaints about merchant fees aren't wholehearted, especially for airlines with robust frequent flier programs and co-branded credit cards. That's because when someone purchases a ticket from an airline using that airline's co-branded card, much of the processing cost comes back to the airline in the form of revenue to purchase the miles awarded to the cardholder. Airlines contractually can't disclose what percentage of their credit card transaction revenue comes from their own cardholders, but an executive at one airline with a major co-branded card business told *Airline Weekly* that percentage is well into the double digits. Even more importantly, these cardholders make most of their purchases at merchants other than airlines, meaning a big transfer of wealth from other retailers to airlines.

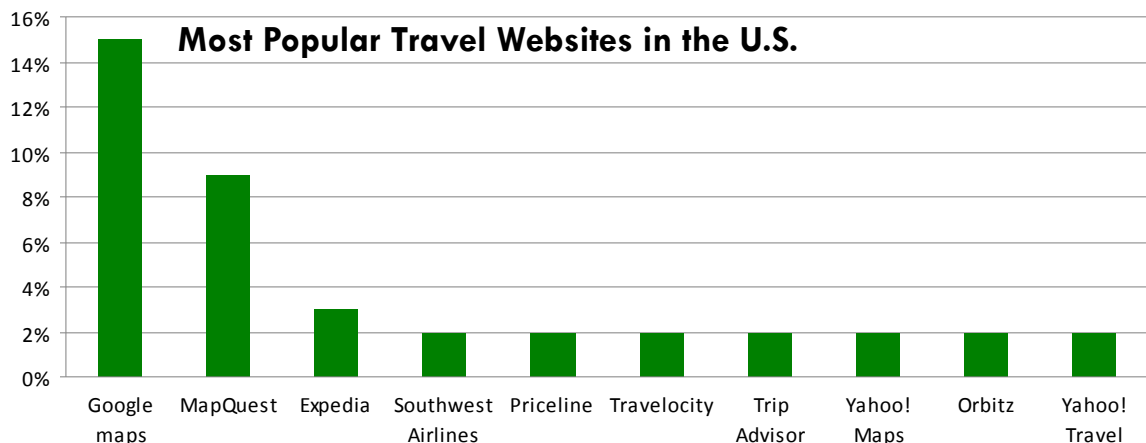
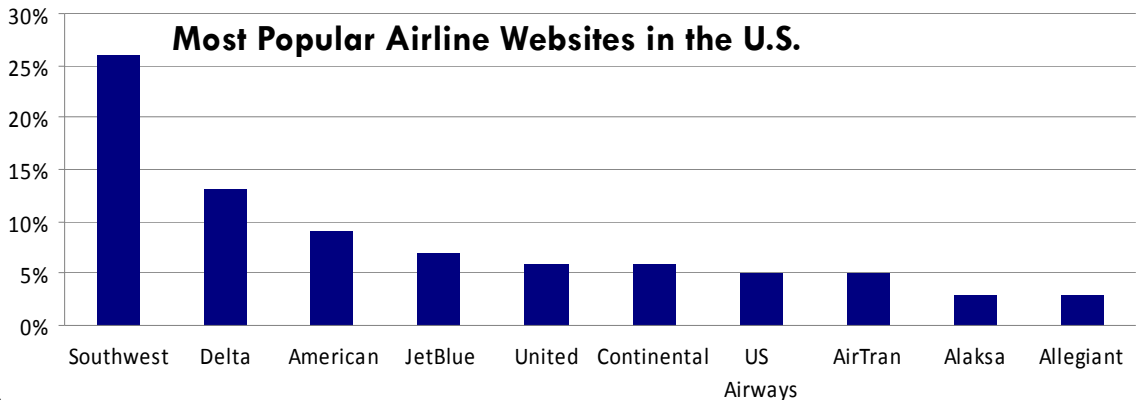
In Australia, banks now charge cardholders high annual fees to compensate for the lost merchant fee revenue, especially for cards offering rewards like frequent flier miles. Overall credit card use has declined. Airlines elsewhere might want to think twice before killing the goose. ○

Search Share

Southwest's site the most popular among U.S. airlines and the only airline to crack the top 10 among all travel sites

Why is Southwest so dominant? It's the busiest U.S. domestic carrier, so its position atop the rankings is no shock. But even given the traffic it carries, its share is disproportionately large: it carries a bit more domestic traffic than Delta (and much less traffic overall) and yet Southwest's website is twice as popular. The main reason for this is that Southwest doesn't distribute its inventory widely outside its own website and call centers: most passengers have to go directly to the airline. Why don't all airlines pursue a similar strategy? One reason is that although distribution costs narrowly defined stay low, Southwest has to spend an enormous amount of money on advertising to build its brand so that customers know to seek it out. And even so, it probably misses out on some traffic (and thus revenue). But it's possible that—as with a lot of things at Southwest (think bag fees)—what Southwest does makes sense for Southwest but wouldn't make sense for other airlines. ○

Source for data in these two graphs: Hitwise, based on searches for the week of June 26, 2010.



Airlines Ask: What's the Distribution Solution?

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the airport and lots of new revenue when travelers purchase their tickets via “supplier direct,” i.e., airline websites. But very little ancillary revenue has thus far been generated from indirect purchases, i.e. those via GDS-equipped travel agents.

This isn't just about selling food or taking money for bags. The very way in which airlines are marketing and merchandizing their fares varies widely based on whether the buyer is using direct or indirect sales channels. Airlines, for example, are increasingly grouping fares with similar rules and perks into “families” and assigning each family a recognizable brand name. But that's much easier for an airline to display on its own website than on the GDS screens that travel agents view—or on an online travel agency's multi-airline fair matrix. To put it simply, the business model for selling airline tickets and services has evolved rapidly in recent years, but mostly with respect to the tickets and services that are being sold directly. Indirect sales, notwithstanding the fact that many take place online, are much as they've always been: travelers see the lowest base fares, or perhaps refundable fares if they requested those.

Indirect sales remain critical to all but a few low-cost carriers (many of whom themselves are increasingly opting to distribute through intermediaries), leaving a wide swath of airline customers

unexposed to the airline industry's most innovative sales and revenue-generating techniques. Fortunately, this asymmetry is on the verge of disappearing.

Looking Back: A Powerful New Weapon

Distribution began to evolve rapidly with the advent of the internet in the mid- to late-1990s. Carriers now had a new medium to sell directly to the public far more effectively. Not that they didn't sell directly before—since the industry's early days, airlines operated call centers and city ticket offices that interacted directly with travelers. But these channels required a substantial amount of labor and real estate, which wasn't cheap. In any case, travelers were far more inclined to buy their tickets from travel agents, who used unbiased electronic airfare supermarkets—what today are called global distribution systems (GDSs). For a long time, travel agencies were responsible for about four-fifths of all airline tickets sold.

The internet didn't make direct airline sales channels any less biased. Their websites, after all, weren't usually programmed to sell competitors' products. But the new medium did enable airlines to offer more convenience—travelers could now shop from their personal computers in their homes or offices—with negligible costs: no salaried call center operators, no real estate leases in midtown

Manhattan, no commissions to agents and no transaction fees to GDS companies. No wonder distribution costs fell so steeply.

For airfare shoppers, the allure of airline websites was further enhanced by mileage bonuses, special “web-only” fares and useful features like flight status updates. Over time, airline websites became progressively more functional, offering services such as tour packages, the ability to redeem award tickets and online check-in. Airline by airline, market by market, region by region, the industry's cherished goal of reducing the influence of costly middlemen advanced. Some industry observers even predicted the demise of travel agents and their electronic airfare supermarkets altogether.

Alas, that didn't happen, and it likely never will.

Agencies Fight Back

Despite all the progress made by airlines, travel agencies were able to use the internet to their advantage too. Many built websites of their own, promoting their key advantage—impartiality—while new exclusively online agents like Expedia and Priceline emerged. These two sites in particular became enormously popular, encouraging a group of major U.S. airlines themselves to establish an unbiased online travel agency (OTA) called

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Pro-Social Behavior

Airlines tweeting to followers and finding fans, but will social media move beyond a niche

Anyone who doubts the power of social media need only think back to last summer, when a Canadian country music singer frustrated with a lack of response from United Airlines about a broken guitar got the airline's attention—and the attention of more than eight million other people—by producing a music video about his experience and posting it on YouTube.

“United Breaks Guitars” remains that airline's most notorious experience with social media—a category that includes YouTube along with Facebook and Twitter—but more quietly, United is also among airlines using social media to not only address issues like broken guitars, but also to distribute its seats.

Most major airlines and many smaller ones now have some kind of social media presence, but their efforts vary widely from static Facebook pages “liked” by “fans” and providing occasional information to actively learning about and resolving customer service issues to—in a few cases—distribution.

According to a tally by blogger Stephen Michaelson, no airline has nearly as many Twitter “followers” as JetBlue. That's what happens when you offer deals like free round-trip tickets to your followers who sign up to receive your messages

(of no more than 140 characters, like all “tweets”) with information about where in New York City to go to claim the tickets. Thousands of people battled—peacefully—for 1,000 free tickets. More than 1.5m people follow JetBlue, which more commonly offers cheap tickets—as little as \$10—bookable online for an extremely limited time (sometimes just an hour or so) to specific destinations, often for midweek travel.

For airlines like JetBlue and the few others like United that also promote certain deals only on Twitter, it's a distribution strategy but also a revenue management strategy. Airlines typically segment more price-sensitive leisure travelers by offering lower fares far in advance of travel dates based on historical booking patterns while holding more expensive seats for last-minute (and usually less price-sensitive corporate) bookers. If those bookings don't materialize, airlines now have another way to distribute that distressed inventory in a semi-stealth way without broadly publishing the bargain fares and perhaps leaving money on the table with people willing to pay more.

Southwest doesn't distribute its inventory via social media, but it does have the most Facebook fans, according to Michaelson. It hired a company called Radian6, a social media consultancy that also works for companies like Microsoft and Pepsi,

to help it manage social media—a sign, perhaps, that social media are evolving from early Wild West days to something more structured, if still not exactly formal.

The airlines mentioned here are all in mature markets, as are others active in social media such as WestJet, Virgin America and some European carriers. Airlines elsewhere in the world, with a few important exceptions such as AirAsia, have been less quick to embrace the trend. Most hedge their bets, with a presence but not many resources devoted, while Ryanair—ever the contrarian—proudly has no social media presence whatsoever (after dabbling in Twitter early on). Are they all missing out?

They might not be crazy. JetBlue has dozens of staff members working on social media, raising questions about just how low cost a venue it is after all (although they spend much of their time working on customer service issues, not distribution). And many airlines' full-content deals with GDSs prevent them from truly offering fares that aren't available elsewhere.

Most of all, airlines' social media fortunes will probably vary with social media itself—whether users will begin to tire of the platforms once the novelty wears off, or whether what we've seen so far is just the beginning.

Hey Good Looking, Whatcha Got Booking?

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Orbitz in 2001, complete with cost-lowering direct IT links to airlines. The idea was to stem the flow of customers to independent OTAs, which still asked for commissions and depended on fee-charging global distribution systems. Companies that own the GDSs, meanwhile, also started OTAs. Sabre launched Travelocity, and Amadeus launched Opodo. Soon Travelport, owner of the Galileo and Worldspan GDSs, bought Orbitz. A separate group of websites called “aggregators” or “meta-search engines” searched everywhere—airline sites and non-airline sites alike—to find the best fare for a given itinerary in exchange for a finder’s fee from the selected site. Some airlines like Ryanair, however, adamantly resist third-party attempts to even touch their websites.

Many smallish offline travel agencies did indeed collapse after airlines felt strong enough to stop paying “base” commissions, that is, a fixed percentage of the ticket price. Others survived by consolidating. But big agencies and the new breed of OTAs remained popular with passengers and powerful enough to continue extracting commissions from airlines, albeit lower ones than in the past. The largest and busiest agencies also supplemented their income with incentive payments from both airlines and GDSs for steering volume and revenue their way. Agencies also sold ads on their websites and in some cases bought heavily discounted airline tickets in bulk from airlines, subsequently marking them up and re-selling them to passengers. That technique, however, proved less popular than originally envisioned, although it did work well for selling hotel rooms. Agencies also began charging fees to their customers, although major OTAs eliminated those in 2009.

Airlines and OTAs eventually reached a truce, recognizing that each needed the other. While the most dynamic online activity by airlines and OTAs took place in North America and later Europe, carriers from around the world soon signed distribution pacts with OTAs, sometimes promising not

to withhold their best fares in exchange for lower commissions. There were occasional flare-ups between the two sides—American’s decision to withdraw international fares from Expedia in 2007, for example—but selling through all the major OTAs is today an almost universal practice among the world’s major airlines, with the exception of some LCCs like Ryanair and Southwest. Few carriers even bother offering mileage bonuses to customers booking on their own websites anymore,

In the end, the two sides reached a grand bargain: Airlines would get lower fees and other concessions in exchange for promising that all fares and schedules would be made available.

even after OTAs began re-claiming some shoppers by waiving their booking fees.

What About the Big Spenders?

The wrangling and eventual truce between airlines and OTAs ultimately resulted in lower distribution costs for airlines. But this still only covered one segment of the flying public, and a more price-sensitive segment at that. Travelers using airline websites and OTAs to book their tickets are in large part leisure travelers. But for many airlines, it’s the business traveler that ultimately drives the most revenue. And their buying habits are far more complex.

While many small and independent businesses self manage their travel and happily book wherever they can find the best fares and schedules, large corporations tend to buy travel in a different way. For starters, they’re sometimes large enough to negotiate exclusive contracts with airlines, establishing a unique set of non-public fares, discounts based on volume or revenue and perks for employees such as upgrades or lounge access. Large corporations also tend to send employees on complex itineraries involving multiple flight legs, multiple airlines and multiple currencies, something airline websites often can’t handle. They also have policies in place that govern, for instance, which employees can fly premium class and when. In addition, corporations and their internal travel departments require extensive accounting trails of their travel expenses and data reports that their finance departments can analyze.

To manage all of this, these corporations rely heavily on help from a special breed of travel agencies: travel management companies (TMCs). The biggest of these, including American Express, Carlson Wagonlit and BCD Travel, serve as more than just passive booking agents for their corporate clients but also as travel consultants, helping them design policies, manage data and, most importantly, save money. The large TMCs are themselves influential enough to shift substantial revenue and market share from one airline to another, earning them exclusive airline contracts of their own. These too contain preferential fares and

perks, which can then be passed on to their corporate clients. TMCs also supplement their client fee income with incentive payments from airlines for hitting revenue or share targets.

Muscle in the Middle

For all their muscle, the TMCs still couldn’t provide their corporate clients with what they need without depending on global distribution systems, those electronic supermarkets filled with airline and other travel inventory from all corners of the earth. These technologically sophisticated GDSs can also, incidentally, handle the complex itineraries that corporate travelers often require. As such, they and their transaction fees remain key components of today’s airline distribution chain.

Oddly enough, the GDSs were originally created by airlines themselves, starting with American’s debut of the IBM-built Semi-Automated Business Research Environment in the 1960s. Now known by its more familiar acronym, “Sabre” and other systems began their lives as in-house reservation tools but were ultimately given to travel agencies, carefully programmed to disfavor rival airlines. But when this practice was abruptly outlawed by U.S. regulators in the 1980s, these systems lost their usefulness as core assets and were sold off, only to become airline adversaries in the sense that they levied ever-increasing transaction fees on their old parents. Nor could airlines do much about it given existing regulations that standardized GDS pricing and participation rules across the industry.

But sure enough, airlines did manage to exert some pressure on GDSs by using the internet to sell more tickets directly, just as they exerted pressure on travel agencies. A self-distributed ticket went through an airline’s internal reservation system which, though often built by the same GDS companies, didn’t carry the same transaction fees, never mind agency commissions. Pre-internet, only about a fifth of bookings were direct, with the rest through GDS-using travel agencies. But as that figure increased, GDSs felt the pressure.

A big change occurred in 2004, when the U.S. and Canada reversed course and deregulated the relationship between airlines and GDSs. Free to play hardball, airlines withdrew many of their best fares from the GDSs and demanded lower booking fees. The GDS companies, in turn—seeing their supermarket shelves deprived of popular products—reminded airlines about those big-money corporate travelers who won’t book an airline if its inventory isn’t available in their systems. They also stressed their selling power in markets where a particular airline wasn’t necessarily a dominant provider: American, for example, needed extra help selling in a market like Chicago where it competed neck-and-neck with United.

The screenshot shows the Alaska Airlines website interface. At the top, it says "Alaska Airlines | Horizon Air". Below that are navigation tabs: Reservations, Deals, Day of Flight, Destinations, Mileage Plan™, and More... There are also links for No Fees, Hotel Rooms, Car Rentals, Vacation Packages, Schedules, Electronic Timetables, and Route Map. A search bar contains "SEARCH SELECT BOOK TRAVEL LOGS RESERVE CONTACT". Below the search bar, it says "Available Flights" and "Lowest one-way fare on this page \$115.00 \$125.70 including Taxes & Fees". There are buttons for "Select Flight" and "view flights by Price". The main content is a table of flight options from Seattle (SEA) to Los Angeles (LAX) on Friday, July 16. The table has columns for Operated by, Departure, Arrival, Flight, Stops, Total Scales, Revenue, Value, Full Price, and Cost Class. There are seven rows of flight options, each with a "View fare" link.

Operated by	Departs	Arrives	Flight	Stops	Total Scales	Revenue	Value	Full Price	Cost Class
Alaska	6:00 am	9:45 am	AS256	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00
Alaska	7:00 am	9:40 am	AS245	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00
Alaska	8:00 am	10:45 am	AS232	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00
Alaska	9:00 am	11:42 am	AS238	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00
Alaska	10:00 am	12:35 pm	AS240	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00
Alaska	11:00 am	1:43 pm	AS276	0	\$115.00	\$145.00	\$245.00	\$332.00	\$372.00

FAMILY FEUD: Fare families like those offered by Alaska Airlines and others don’t translate well to travel management companies’ GDS displays or online travel agencies’ multi-airline fare matrices. But that could change.

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It's Not What You Sell...

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In the end, the two sides—actually each individual airline negotiating separately with each individual GDS company—reached a grand bargain: Airlines would get lower fees and other concessions in exchange for promising that all fares and schedules would be made available. The exact terms of each contract varied but this “lower fees for full content” principle became the defining characteristic of airline-GDS relations and remains so today. A corollary to this was a new “home and away” GDS pricing model, whereby airlines paid less in markets where they were already strong (British Airways in London, for instance) and more where they needed extra help (British Airways in Paris, Los Angeles or Tokyo).

The story doesn't quite end there. The new arrangement between airlines and GDSs—often cemented in multi-year contracts that are still in place today—also presented some unsettling developments for agencies. They would now have to pay fees for accessing airline content through the GDSs, unless they participated in a so-called “opt-in” offered by systems like Sabre, Galileo, Worldspan and Amadeus. This protected the agencies from the airline fees but often entailed a new fee, albeit a smaller one, from the GDS. GDS incentive payments to agencies were in some cases reduced as well. And this applied even to travel manage-

ment companies, although the largest of the breed retained negotiating leverage to avoid certain charges or incentive reductions. Of course many travel agencies, TMCs or otherwise, had little choice but to pass on these new charges to their customers, i.e., the actual ticket buyers.

Along the way were various disputes ranging from Air Canada's fierce battles with the GDSs to worries among corporate travel buyers about Amadeus and the fact that three airlines (Lufthansa, Air France/KLM and Iberia) still owned part of it. But overall, airlines got what they wanted from their negotiations with both GDS companies and travel agents: significantly lower costs. GDSs, of course, also lowered their own costs as computing power got cheaper and companies merged. This helped deflate airline distribution costs as well, while leaving GDS companies with solid profit margins—certainly higher than those earned by most airlines, anyway.

GDS fees have reached low enough levels, in fact, that even LCCs traditionally loathe to engage third party distributors are now signing up in droves. Even the mighty Southwest is now selling tickets through the Galileo and Worldspan systems—and probably got a good deal to do so. After all, from a GDS's perspective, stocking the largest U.S. domestic airline on your supermarket shelves can go a long way toward getting travel agencies to

use your GDS rather than a rival's. In addition, GDS companies are eager to sell other high-margin products like internal reservation systems and airfare search programs, perhaps lowering GDS fees to carriers that agree to buy them.

JetBlue, AirTran, WestJet, easyJet, Air Berlin, Vueling, Norwegian, AirAsia and Virgin Blue are all now GDS participants, in some cases passing on the associated booking fees to travelers. The GDS-LCC relationship has become so important, in fact, that the former have developed new work-around technology to accommodate even carriers not using IATA's billing and settlement plan (BSP) or the Airline Reporting Corporation (ARC) settlement plan, once a prerequisite. At the same time, LCCs are increasingly joining these settlement plans and installing more advanced internal reservation systems more accommodative to GDS distribution. Newer versions of Navitaire's reservation system, extremely popular with LCCs, can handle GDS distribution as well. In the end, it's no surprise that LCCs are becoming more willing to sell through GDSs, not just because of today's lower fees and a new ability to negotiate favorable deals but also because chasing big-money corporate revenue is now a necessity in the era of expensive fuel. When oil is 20 bucks a barrel, saving a few dollars by avoiding

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...But Where You Sell It

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GDS fees really counts. When oil is 80 bucks, any such GDS savings are almost negligible.

Not Satisfied

For all the savings they've achieved on the distribution line item during the past 10 to 15 years, airlines aren't satisfied. American and Delta each recently said, rather controversially, that they'd eventually like to see a model whereby third parties *pay them* for access to their unique content. However dreamy that idea might sound, airlines are busy forging relationships with new entrant distributors that promise direct IT connections between travel agents and airlines' own internal reservation systems. One such new entrant, Farelogix, claims to execute transactions 75% less costly than what GDSs charge per booking. This can be good for agencies, too, which value close IT links to the airlines whose inventory they're selling, though it could mean some have to forfeit valuable GDS incentive payments. It's also another "moving part" to manage, assuming they'll long require some GDS connectivity anyway to book airlines—think small, developing world flag carriers in particular—that won't soon support the new platforms.

Airlines also recognize the leverage they have with agents and GDSs regarding their ancillary products. While carriers themselves are eager to open new markets for these products, the intermediaries are just as eager to sell them. Airlines could thus play hardball again and withhold these products unless given further concessions, including fee cuts. A few deals have already been reached—United's agreement with Sabre to sell economy plus upgrades through its GDS, to name but one. Another example is Travelport's creation of a unique tool for travel agents to book Air Canada tickets as a customer would on the carrier's website, complete with branded fare families.

Stakeholders throughout the distribution chain—including ATPCO, which carriers use to file their fares with the GDS systems—are now creating industry standards and IT practices to enable efficient selling of ancillary products and services. But few airlines are currently filing anything but standard airfares.

Later this year, the major GDS companies expect to introduce new travel agency desktop systems designed to give agents more versatility and better workflow. They'll provide traditional GDS content but also allow agents to, in some cases, access inventory directly from airlines. Travelport's Universal Desktop, for example, will debut this summer using technology purchased from a now-defunct startup (G2 SwitchWorks) that made headlines with its direct-connect approach several years ago. Amadeus and Sabre will similarly introduce their next-generation Amadeus One and Sabre Red desktop solutions later this year.

At the same time, GDS companies are improving their corporate booking tools (Sabre's GetThere and

Travelport's Traversa, for example), devising more powerful fare shopping technology and upgrading their computing power. All of these advancements helped the GDS sector grow revenues 10% in Q1, according to Amadeus.

This growth sets the backdrop for a new round of airline-GDS negotiations in the U.S. starting next year. Once again, carriers will be looking for lower fees, but they'll be focusing even more on new revenue opportunities. They could have additional leverage this round thanks to consolidation, with

The industry is also embracing the raging trends of social networking and mobile telephony. Carriers have turned websites like Facebook and Twitter into burgeoning distribution channels.

giants like the bulked-up Delta and United more indispensable to the GDS supermarket shelves than ever.

Beyond America and Europe

The U.S and European markets, of course, are just two of many. Other regions are experiencing much greater industry growth even while distribution activity often remains far less dynamic. Tour operators, for instance—a breed of travel agents that organize group holidays—continue to wield great leverage in Asia. GDS regulations are in many cases still strict, while in China, only one state-owned GDS provider (TravelSky) dominates the market. This could make emerging markets ripe for distribution changes, with airlines trying to boost online bookings, OTAs expanding their presence and foreign GDS companies itching to enter China. IATA is waging a global battle to lower airline distribution costs, even going so far as to label the "western GDS" companies "leeches" at its annual general meeting this year. Those GDSs charge \$4 per transaction, it said, while TravelSky charges an average of just \$1.20. (*The Beat*, a business travel newsletter, counters that Chinese airlines own TravelSky anyway and that it charges close to the \$4 "western GDS" average for international itineraries impacting foreign carriers.)

What Else Lies Ahead

Back in the U.S. and Europe, carriers like Ryanair and Allegiant are well on their way to doing something altogether novel: becoming virtual travel agents themselves. Their websites are now storefronts with a large array of non-air travel products including hotels, tour packages, rental cars, event tickets and much more. These airlines, in other words, have turned the distribution chain on its head, refashioning themselves as third-party travel distributors. They of course earn commissions and fees for this service, creating an ancillary source of income all its own. More established carriers are in some cases trying to follow this model as well.

Airlines are also innovating in the area of payment methods, allowing customers to buy tickets using cash, debit cards, PayPal and other forms besides credit cards. The increased flexibility not only creates new markets by reaching new customers but also saves money by avoiding credit card transaction fees. United not long ago even demanded that some of its smaller travel agency partners bear the cost of all credit card transactions. In addition, Brazilian carriers and others allow customers to pay in installments, easing cash flow concerns for lower-income travelers.

Remarkably, even the city ticket office is coming back. While still a dinosaur in developed markets like the U.S., airlines in regions with lots of computer-less consumers like Brazil, the UAE and the ASEAN region are opening bricks-and-mortar storefronts in downtowns to attract customers and spread their brands. Gol, Air Arabia and AirAsia are all practitioners of this approach. Mango in South Africa, for one, even sells its tickets in supermarkets. At the other end of the scale, full-service global airlines are refining their corporate contract practices to take advantage of new trends including alliance joint ventures and product bundling. Delta and Air France can now jointly propose to a corporation, for example, that its travelers will be protected from all bag fees.

The industry is also embracing the raging trends of social networking and mobile telephony. Carriers have turned websites like Facebook and Twitter into burgeoning distribution channels, granting offers to travelers who willingly choose to receive them. At the same time, new websites and tools designed specifically for mobile devices like Blackberries and iPhones make travel buying on the go easier than ever. You can now buy a ticket on your mobile device on the way to the airport.

Still, these new forms of direct distribution won't erase the influence of travel agents, travel management companies and GDSs. Many remain far more profitable than the airlines whose products they sell, which helps explain why even non-travel goliaths like Google are entering the space. But make no mistake, airlines are thrilled with the progress they've made in dramatically lowering the price they pay to sell their own tickets. If their more profitable distribution partners help them earn additional revenues in the coming years, all the better. So for all the headaches airlines endure—from uncontrollable fuel spikes to labor strikes—they're at least driving great success by following their all-important dictum: It's not just what an airline sells. It's where an airline sells it. ○

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