Why Frequent Flyer Programs Are Not Loyalty Programs

Many people believe frequent flyer programs (FFPs) and customer loyalty programs are basically the same. However, they are not interchangeable. In fact, research shows that 66 percent of business travelers are open to switching to another airline’s FFP, even if they carry elite status with their current carriers. Therefore, airlines should not rely on FFPs alone to retain customers. Rather, they need to implement customer loyalty strategies that include FFPs to create return customers.

By Jonathan P. Ewbank | Ascend Contributor
Often within the airline industry, the terms “frequent flyer program” and “loyalty program” are considered synonymous. Are frequent flyer programs really loyalty programs? Can an FFP actually build loyalty? Before answering that question, let’s discuss the topic of loyalty and why it is important. In business, loyalty drives sustained revenue growth and long-term profits. During the past decade, airlines with the highest consumer loyalty (as measured by Net Promoter Score®) have averaged revenue growth three to five times greater than the competition.

Why does consumer loyalty translate to increased long-term profits?
Research shows that loyal consumers reduce costs by:
- Developing long-lasting relationships with the company, thereby spreading out customer acquisition costs,
- Complaining less, lowering resolution costs,
- Using self-service offerings such as Web check-in and kiosks.

Loyal customers also increase revenue because they:
- Are less sensitive to price changes,
- Refer other customers through word-of-mouth,
- Spend more than the average consumer.

The net result is that every customer is worth more, or less, than what he or she actually spends. This, of course, is why it is important to assess and segment customers based on their total worth to the company, known as customer value. There are several methods for and varying opinions about how to measure customer value, but the core intent of all customer valuation models is to capture:
- How much the consumer spends (on an annual basis or over the projected life of the relationship),
- How frequently he or she purchases from the company,
- The last time he or she made a purchase.

A more robust model would also estimate the net effect of word-of-mouth, acquisition costs and operating costs associated with servicing the customer. But for argument’s sake, a basic customer value model is used; in this case the recency, frequency and monetary value (RFM) model, in which:
- Recency = How recently did the customer purchase?
- Frequency = How often does he or she purchase?
- Monetary Value = How much does he or she spend?

In analyzing customer value (via the RFM model) it becomes evident that FFPs do not accurately or effectively measure loyalty. FFPs do not necessarily measure “recency,” but they reward and punish it. For example, a customer will lose his or her status if he or she does not use the product.

The term “frequent flyer program” suggests that a customer is rewarded for “frequent” purchases, but in reality, most programs provide incentives for miles flown and not how often a ticket is purchased.

Based on this model, “passenger A,” who flies first class with the same airline from Chicago to Dallas eight times a year, will be deemed less loyal than “passenger B,” who purchased a bargain economy ticket one time to go from Los Angeles to Hong Kong, because the distance between Los Angeles and Hong Kong and back is longer than the eight Chicago/Dallas trips combined.

Finally, assessing and rewarding loyalty based on miles does not attach monetary value to a passenger’s worth. In the example above, “passenger A” may spend US$10,000 per year, compared to “passenger B,” who may have only spent US$2,000.

As a result, Delta Air Lines and United Airlines have recently announced that they will begin rewarding miles based on the price paid rather than distance traveled.

If the two airlines are the originators of an industry trend, as some analysts have speculated, FFPs will certainly become more effective in measuring customer value and rewarding loyalty accordingly.

Money Versus Miles Airlines have traditionally rewarded their customers for miles flown as opposed to the amount of money they have spent on airfare and ancillary products and services. Delta Air Lines and United Airlines, however, have recently shifted their frequent flyer model to reward miles based on price paid rather than distance traveled.
In doing so, airlines will be better aligned with segmenting passengers based on the 80/20 rule (80 percent of airline revenue is generated by 20 percent of the passengers), according to the International Journal of Marketing Studies.

When further dividing the referenced 20 percent, according to Harvard Business Review, 2 percent of passengers generate 25 percent or more of the revenue, and 18 percent generate approximately 55 percent of the revenue.

This point raises another issue. If enrolled in an airline’s FFP, the 2 percenters are afforded all the benefits of “elite” status, but what about the other 18 percent? Certainly some of these passengers would hold silver or gold status (assuming they are enrolled in an airline’s FFP), but the airline is not building the same type of relationships with them that “elite” customers garner, despite their contribution to the majority of the airline’s revenue.

The preceding points assume that those who use an airline’s product most frequently and are most loyal are also members of its FFP. However, only 20 to 30 percent of an airline’s passengers are enrolled in its FFP, according to Airline Business. This might be fine if 100 percent of the airline’s top revenue-generating customers (the aforementioned 20 percent) are FFP members. However, in reality, 8 percent to 42 percent (based on Sabre Airline Solutions’ research) are not, depending on the type of program offered. Therefore, every airline has thousands (sometimes millions) of loyal, high-value customers with whom they are not fostering relationships with and who are not afforded a single benefit and, unfortunately, are treated as first-time consumers each time they fly.

For many airlines, customer relationship management as a strategy relies heavily on data collected within the FFP. As a result, these airlines create customer-centric strategies and make organizational decisions based on a small subset of their customer base, as well as incomplete information.

This approach might work if an airline is guiding the organization based on the preferences of its most loyal customers. And, one might assume that FFP members are loyal brand advocates, correct?

Research suggests otherwise. According to a recent Deloitte study:

- Only 38 percent of FFP members said they would be willing to promote an airline’s products or services,
- 75 percent of regular travelers belong to more than one FFP,
- 66 percent of business travelers are open to switching to another airline’s FFP, even if they hold elite status with their current carriers,
- 72 percent of business customers who travel 50,000 or more miles a year belong to at least two FFPS.

This is not to say FFPS are bad for airlines; quite the contrary. FFPS are one of the most valuable aspects of an airline’s loyalty program in the competitive market, with more than 120 million members worldwide. For the majority of airlines, FFPS generate a significant amount of revenue at substantially lower costs. FFPS also increase yields. Research cited in the Journal of Revenue and Pricing Management shows that elite customers will pay a 2 percent to 12 percent price premium for similar itineraries.

However, FFPS should be viewed and treated as what they are … a separate business function from the airline. A customer who is loyal to an FFP is not necessarily loyal to the airline and vice versa.

Rather, a customer loyalty strategy should encompass measures that will ultimately build product loyalty and brand advocacy. It should not simply be based on FFP benefits that may increase membership. Airline leaders should reassess their organization’s loyalty strategy by asking:

- How do your FFP members describe their experiences with your airline?
- How is customer feedback shared throughout the organization?
- Is there a 360-degree view of the customer?

How effectively is customer data used to drive customer-centric actions and continuous improvement (Lean Six Sigma)?

Long-term, sustained, customer-centered profit growth is possible for airlines that effectively answer these questions and build strategies that promote true customer loyalty.

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