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ANCILLARY REVENUE OPPORTUNITIES IN TURKISH DOMESTIC AVIATION MARKET

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Abstract

This study aims to explore ancillary revenue opportunities for Low Cost Carriers (LCCs) operating in Turkish domestic aviation market. The data collected through the survey yields valuable data regarding the ancillary services that Turkish domestic passengers value the most and their Willingness to Pay (WTP) for these ancillaries. The findings indicate that respondents are willing to pay for many of the ancillaries included in the survey although the amounts willing to be paid are highly variable among different segments. The results also reveal that demographic characteristics of the respondents such as "Age", "Gender" and "Occupation" and data related to their intended trip such as "Flight destination" and "Purpose of flight" has a significant impact on their WTP for various ancillaries. The differences in respondents' WTP for various ancillaries as well as their historic consumption habits and preferences would help airlines to segment their customers and optimize their ancillary offerings accordingly. In addition, the impact of demographic factors and trip related factors on customers' WTP may help airlines to tailor their ancillary offerings by using correct pricing and promotional tools.

Keywords: Ancillary Revenue, Willingness to Pay, Low Cost Carriers, Turkish Domestic Aviation Market, Pricing of Ancillaries

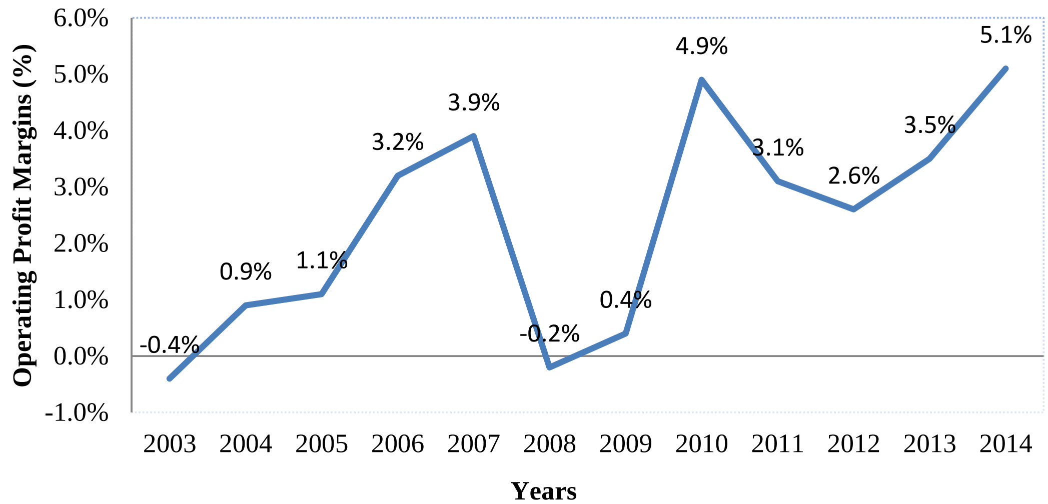
INTRODUCTION

Importance of Additional Revenue Streams in the Airline Industry

Airlines are operating in a highly competitive industry and are facing serious industrial challenges such as rising input costs, severe global economic slowdown, environmental uncertainties and many external events, which erode passenger demand for air travel.

Moreover, the extreme competition and over-capacity problem within the industry results in a downward trend in average ticket fares and consequently in declining yields (O'Connell, 2011). The increased use of internet as a major distribution channel has further driven the price of air travel down dramatically over the past 30 years (Garrow et al., 2012). The average operating profit margin of the whole airline industry has been 2.8% in the last 10 years (Figure 1) (IATA, 2014). As the traditional revenue streams through ticket sales come under pressure, airlines have started to search for new ways for maximizing their revenues (Schoinas and O'Connell, 2011). They have increased their dependence on ancillary revenue streams to increase profitability and to differentiate their service from competitors by creating additional value to the customer (Hellqvist et al., 2012).

Figure 1: Airline Industry Operating Profit Margins



Source: (IATA, 2014)

Airline ancillary revenues, which are also referred as "non-ticket revenues", are "additional revenues beyond the sale of tickets generated by direct sales to passengers or indirectly as part of their travel experiences or from the third parties" (Sorensen and Lucas, 2011).

Ancillary services have become an increasingly important source of revenue for airlines. Global ancillary revenue collected by 59 airlines worldwide reached USD 31.5 billion in 2013. This amount constituted 4.4% of the total global airline revenue of USD 717 billion in 2013 (IATA, 2014). In 2013, average ancillary revenue per passenger for the 59 airlines was USD 16 (Table 1).

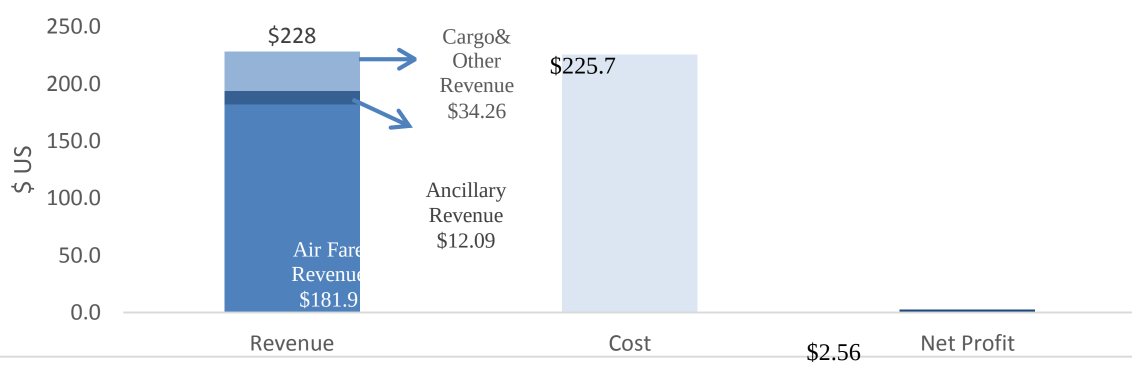
Table 1: Annual Financial Disclosures of Ancillary Revenue

	2007	2008	2009	2010	2011	2012	2013	2014
Worldwide Estimate of Ancillary Revenue	$2.45 billion (23 Airlines)	$10.25 billion (35 Airlines)	$13.47 billion (47Airlines)	$21.46 billion (47Airlines)	$22.6 billion (50 Airlines)	$27.1 billion (53 Airlines)	$31.5 billion (59 Airlines)	$38.1 billion (63 Airlines)
Global Airline Revenue	$510 Billion	$570 billion	$476 billion	$547 billion	$597 billion	$680 billion	$708 billion	$746 billion
% of Global Airline Revenue	0.5%	1.8%	2.8%	3.9%	3.8%	5.4%	4.4%	5%

Source: (Ideaworks, 2014)

The importance of ancillary revenue for the airlines is illustrated on Figure 2. In 2012, airlines generated USD 228 average revenue per passenger consisting USD 12 ancillary revenue. If the ancillary revenue was excluded from the total revenue, the industry would make a loss of USD 9.53 per departing passenger.

Figure 2: 2012 Worldwide Airline Financial Results per Departing Passenger



Source: (IATA, 2013)

Types of Ancillary Revenue

Ancillary revenues are grouped under four headings: Revenue from à-la-carte products and services, revenue from third party products and services (commission-based), revenue from Frequent Flyer Programs (FFPs), and revenue from advertising sold by the airline (Sorensen and Lucas, 2009). Traditionally, airlines used to offer services such as baggage, on-board meal service, assigned seats and checked baggage allowance included in the ticket fare. Low Cost Carriers (LCCs) have changed this idea and have subdivided the traditional airfare into distinct parts and charging each item separately (O'Connell and Williams, 2011). The LCCs brought the term "à-la-carte" to the airline industry, within which the ticket fare only includes "the seat" and passengers need to pay extra for every other service they want to receive. These extra services include items traditionally included in the ticket fare such as assigned seats and checked baggage allowance as well as more premium items that were not traditionally included in the ticket fares such as on-board Wi-Fi access, airport lounge access, and priority check-in (O'Connell and Williams, 2011; Guestlogix, 2012). Revenue from à-la-carte services are also generated through "punitive fees" which airlines charge passengers for services such as itinerary changes and cancelations, booking through GDSs, counter check-in and printing boarding pass at the airport. Through "à-la-carte pricing", LCCs aim to make air travel more affordable for some passengers and, at the same time, to provide more options for others who are willing to have more premium service similar to that of legacy carriers (O'Connell and Williams, 2005). "Punitive fees", on the other hand help airlines to modify consumer behaviour and reduce costs (Sorensen and Lucas 2012).

Ancillary revenues also include commissions earned by airlines for the sale of third party services such as hotel accommodations, car rentals and travel insurance (Sorensen and Lucas, 2011). These commissions are generated through the sales of these third party serviced depending on the agreement with the service providers, usually around 10-20% (Guestlogix, 2012). The third party products that are sold on-board or through airline websites are also included in this group. Commission based ancillary revenues is regarded as a win-win situation both for passengers and for the airlines as these revenues are not directly generated from passengers, but from third parties.

Although ancillary revenues through frequent flyer programmes (FFPs) have been more common for Full Service Carriers (FSCs), recent years have witnessed the launch of loyalty schemes by LCCs. In order to make their loyalty programmes more attractive, both FSCs and LCCs began to search for alternative rewards with FFPs by partnering with banks and major credit card companies.

The "Ancillary Revenue Champions" table, which lists the carriers that generated the highest percentage of their operating revenue through ancillary products, illustrates the importance of ancillary revenue are for airlines (Table 2). LCCs dominate the list, as ancillary revenue is naturally a larger part of the total revenue for these carriers. Spirit Airlines ranked first with generating the highest percentage (38.4%) of its total revenues through ancillaries in 2013. Wizz Air took the second place with 34.9% and Allegiant came in the third place with 32.6%.

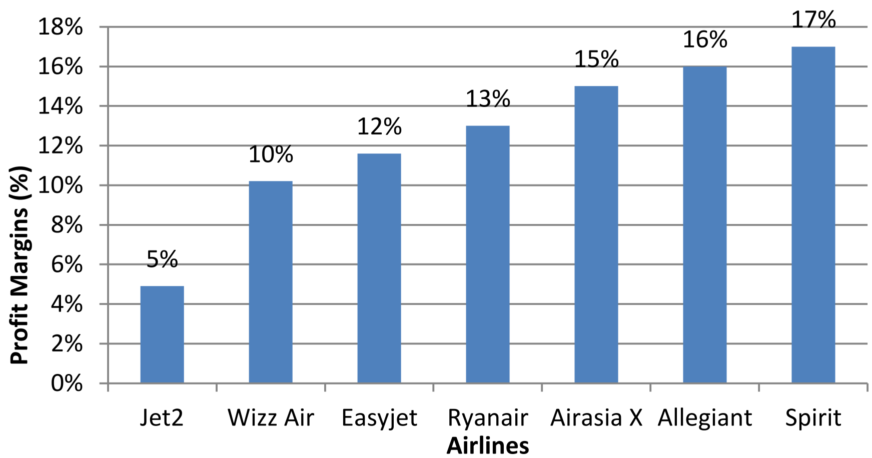
Table 2: Ancillary Revenue Champions -Ancillary Revenue as a % of Total Revenue 2013

Spirit	38,4%
Wizz Air	34,9%
Allegiant	32,6%
Jet2.com	27,7%
Ryanair	24,8%
Tiger Airways	23,6%
Jetstar	20,6%
AirAsia X	19,6%
easyJet	19,2%
AirAsia Group	17,6%

Source: (Ideaworks, 2014)

It is also very remarkable that the operating margins of the carriers listed on “Ancillary Revenue Champions” list are well above the industry average margin of 3.5% in 2013 (Figure 3). The contribution of ancillary revenues on their profitability would be an undeniable fact.

Figure 3: Airline Operating Profit Margins 2013



Source: (ATW, 2014; CAPA, 2014; CAPA, 2014a)

Having recognized the importance of it, LCCs are looking for new ways of increasing their ancillary revenue by becoming more innovative with their ancillary offerings. For instance, Air Asia X launched a ‘Quiet Zone’ on their flights where children are not able to book seats and passengers flying in this zone are asked to keep noise to a minimum for a fee of USD 12 (Airlinetrends, 2012). The company also launched a “‘Red Carpet” service at eight airports, where passengers receive priority check-in and boarding, fast track through security, lounge access, as well as priority luggage service for a certain fee (Airlinetrends, 2012a). Moreover, Air

Asia X provides empty seat option, which offers passengers a chance to reserve one or two empty seats next to them for a fee unless someone books the seat. Vueling, a Spanish LCC, also sells its passengers a similar option (Sorensen and Lucas, 2012). Ryanair has launched a smartphone application called "Ryanairtalk" which enables passengers to make cheap calls. The application charges passengers EUR 0.13 per minute for calling any mobile phone in Europe and EUR 0.03 per minute for calls to landlines (Ryanair, 2013). Singaporean LCC, Scoot, decided to offer a limited number of iPads on-board to economy passengers for USD 17.5 (UXMilk, 2012). All these and many others demonstrate that there are many ancillary revenue opportunities to be discovered by airlines.

In order to make customers purchase more ancillaries, airlines started a new concept named "Re-bundling", where several à-la-carte ancillary items are brought into a group and offered under a single price (Guestlogix, 2012). For instance, Vueling offers passengers hold the middle seat empty, board the aircraft early, and provide a drink and snack for EUR 60 (IBT, 2012). It was found that re-bundling is likely to increase profits when the correlation of consumers' valuations for individual items included in the bundle is small or negative. In other words, if the items for which the customers do not have the same favourites are bundled, the customer who is not normally buying the non-favourite product appears to buy it (Eisenmann, 2011). This helps airlines to sell more à-la-carte services than when they are sold individually. In addition, when they are bundled together, the prices of individual à-la-carte items in the bundle become less transparent (Morello and Lopatko, 2012).

Some airlines add these re-bundled options in ticket fares and create "Branded fare" groups. They then give these fare groups the names that reflect their contents. For instance, WestJet, the Canadian LCC, introduced three branded fare groups, which are "Econo", "Flex" and "Plus". "Econo" is the cheapest fare and it only includes one free checked bag and high fees are charged for any other extras. "Flex", on the other hand, offers one free checked bag and lower fees are charged for other extras. "Plus", is the highest fare targeting business traveller and it provides extra-legroom seats, two checked bags and free name or itinerary changes (Westjet, 2013). Branded fares help airlines to simplify things with all-inclusive fares instead of offering them separately. This reduces the choice complexity and makes comparison and purchase decisions easier for passengers (Tnooz, 2013). Frontier, the first U.S. LCC to offer 'branded fares' in 2008, found that 33% of its passengers bought one of the bundled fares rather than the 'no frills' fare (Eyefortravel, 2012). However deciding on which ancillary items to bundle and which items to offer separately is a big challenge for airlines. Determining the right bundle of features requires market segmentation and analysis of the features desired by each segment (Eyefortravel, 2013). Moreover, it is important make sure that offering branded fares bring more revenue than offering items separately on an à-la-carte basis.

Pricing of Ancillaries

Pricing ancillary items is a big challenge for the airlines. Some of the approaches that airlines use to price ancillary items are as follows:

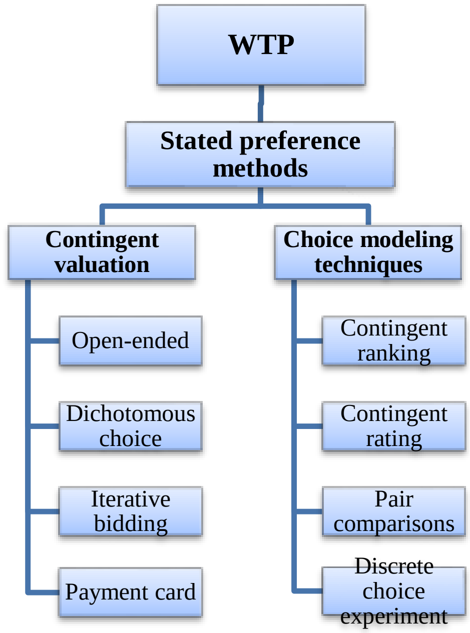
- ✓ "Expert Judgment", where initial prices are estimated based on experience and intuition
- ✓ "Competitive Match", where the competition is monitored and the price to offer is decided based on market share and market position
- ✓ "Test and Learn", where the price is launched, monitored and adjusted based on customer behaviour
- ✓ "Data-driven Optimization", where customer segmentation, customer surveys and other tools are utilized to optimize products and their pricing (Moore, 2012).

Different passenger segments have different price sensitivity and Willingness to Pay (WTP) for different ancillaries. "Data-driven Optimization" approach, which aims investigating user preferences and estimating "Willingness to Pay (WTP)", therefore has become very important for applying the correct pricing and maximizing ancillary revenue (Moore, 2012).

There are two basic methods for estimating WTP: "Revealed preference (RP)" methods and "Stated Preference (SP)" methods (Adamowicz et al., 1994). RP methods require actual market data drawn from the past behaviour of consumers in the market. In cases where actual behaviour of the target market is not observable or available, SP methods are used to obtain data through surveys where consumers state their preferences and WTP when faced with choices. The main survey categories under SP methods are the Contingent Valuation Methods (CVM) and Choice Modelling Techniques (Figure 4). CVM, a widely used as an attractive method for collecting WTP data, aims to measure the value of a good or a service as a whole by asking people directly their WTP. Alternative question types of CVM are as follows:

- ✓ **Open-ended questions:** "How much are you willing to pay?"
- ✓ **Dichotomous choice (DC):** "Would you pay USD X to for the service / product?"
- ✓ **Iterative bidding (IB):** Series of dichotomous choice questions followed by a final open-ended WTP question. The bidding increases until the respondent says no with the final question being an open-ended WTP question.
- ✓ **Payment card (PC):** Respondents select their maximum WTP amount from a list of possible options presented (Competition Commission, 2010).

Figure 4: Willingness-to-Pay (WTP) Methods



Source: (Bateman et al., 2002; Kjaer, 2005)

Importance of Personalization

Personalisation and putting the passenger in control by offering extra value services and differentiated products is at the heart of ancillary revenue generation (Flightglobal, 2011). Understanding customers' needs before, during and after their journey, and offering relevant products and services are the key factors for a successful ancillary revenue strategy (Schnadt, 2013). Airlines are increasingly keen to tailor their sales to customers' requirements and preferences. They aim to increase ancillary revenues significantly by using the customer data such as demographics, purchase history and preferences effectively. Industry reports reveals that 78% of the airlines plan to personalize the content they provide via their direct distribution channels by the end of 2015 (SITA, 2013).

An attention must be drawn to the richness of data from mobile devices and social media, which provide airlines significant opportunities to tailor their services to the specific passenger needs. The use of internet on mobile devices and tablet computers is giving airlines more options to promote and sell ancillary products. Moreover, airlines have a strong interest in generating revenue by selling services directly through a passenger's mobile phone through their mobile apps. In 2014, 37% of ancillary sales came through websites, while 2.4% of them via mobile phones. It is expected that by 2017 ancillary sales through mobile channel will become mainstream and will constitute 11.6% of total ancillary revenue (SITA, 2014).

As the use of social media expands, airlines continue to find innovative ways to communicate with individual travellers in an effort to determine and evaluate preferences and tailor ancillary offerings in response. Communicating with customers through new touch points such as social media, mobile phones and web is crucial in ancillary revenue generation (Schnadt, 2013).

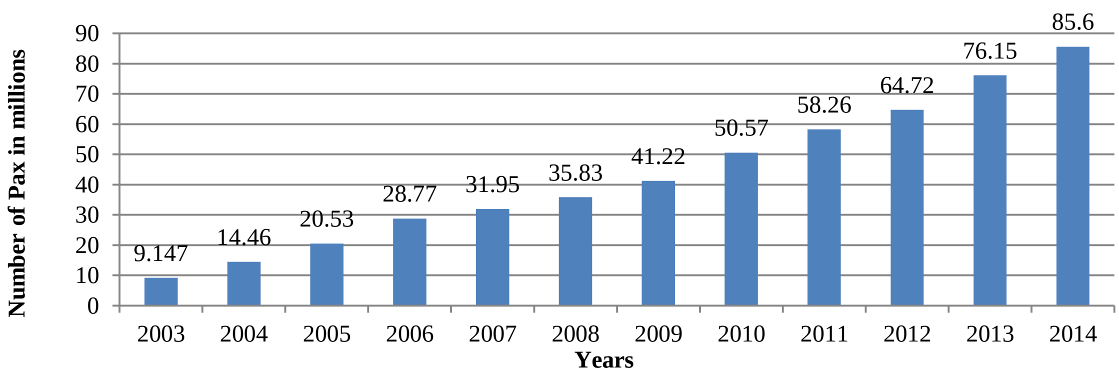
It is important to mention a new trend in ancillary revenue generation, where passengers are encouraged to purchase ancillaries in advance, particularly while booking their tickets. Many airlines now agree that it is important to make passengers pay in advance before they get to the airport for any ancillary offerings (Sarasin et al., 2012).

Turkey and Its' Civil Aviation Industry

Turkey has been one of the fastest growing aviation markets in the world with a Compund Annual Growth Rate (CAGR) of 15.4% between 2003 and 2014 (DGCA, 2015). Before 2003, Turkish aviation industry was not opened to competition and Turkish Airlines (THY) was the only carrier that had the right to apply domestic scheduled flights in Turkey. In 2003, domestic routes were opened to competition. This revolutionised the aviation industry in the country. Lower ticket fares and increased Gross Domestic Product (GDP) per capita in Turkey have made air transportation more affordable. The domestic passengers demand had a CAGR of 22.5% between 2003 and 2014 (DGCA, 2015).

In 2003, when THY was the only carrier that had the right to offer domestic scheduled flights to 26 destinations, the number of domestic passengers were 9.1 million. By 2014, 6 airlines are operating domestic flights to 53 destinations from seven airports and the domestic number of passengers carried equals to 85,6 million (Figure 5). Among them, Pegasus and Onur Air position themselves as LCCs, whereas BoraJet operates as a regional carrier, and Sun Express and Atlasjet as full-service carriers.

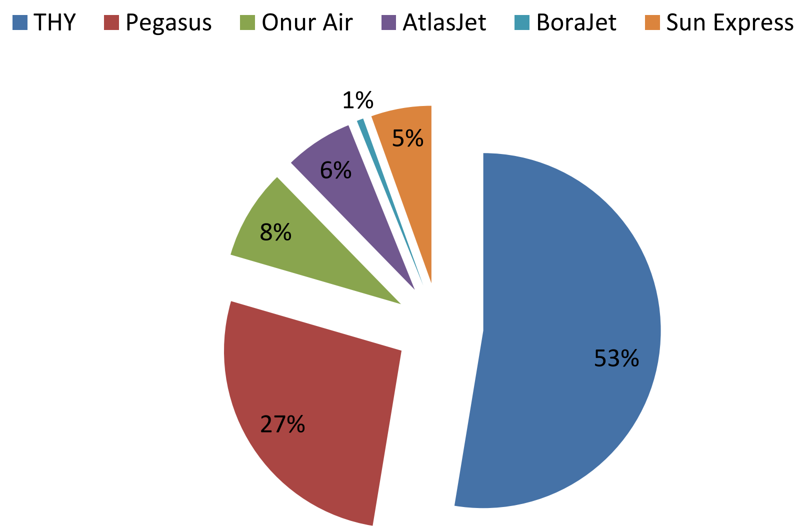
Figure 5: Turkish Air Transportation Industry Domestic Passenger Traffic



Source: (DGCA, 2015)

2013 data reveals that, THY is the market leader with 52.6% market share in Turkish domestic aviation market. Pegasus had the second highest market share with 27% (Figure 6).

Figure 6: Airline Turkish Domestic Pax Traffic Market Share 2013



Source: (TOBB, 2014)

The "ancillary revenue" concept is very new in Turkish domestic aviation market. In 2013, THY, the flag carrier, generated USD210 million ancillary revenue through its Frequent Flyer Programme "Miles&Smiles", which represented 2.1% of the company's total revenue (Ideaworks, 2014). As an average, the company generated USD4.3 (EUR 3.8) ancillary revenue per passenger in 2013. Pegasus Airlines is the only LCC adopting a serious ancillary revenue strategy in Turkey. The company generates revenue through a number of à-la-carte options to the core air passenger services, through commission-based services, and also through its co-branded credit card (Ideaworks, 2014). In 2014, Pegasus Airlines generated USD10.1 (EUR 9.32) ancillary revenue per passenger (Pegasus, 2014). Onur Air generates ancillary revenue through excess baggage charges, in-flight catering sales, exit/front seat, and airport transportation. The company also generates commission-based revenue through the sales car hire and travel insurance. On domestic flights, the company generates only 2% of its revenues through ancillaries. The ancillary revenue per passenger is considerably low compared to Pegasus (Cetin, 2013). However, the "ancillary revenue" concept is still in its childhood in Turkish aviation industry and there are many opportunities awaiting to be discovered by the carriers.

RESEARCH METHODOLOGY

The main aims with this study are as follows:

- ✓ To investigate the ancillary services that Turkish domestic passengers value the most
- ✓ To measure Turkish domestic passengers' WTP for various ancillaries
- ✓ To investigate the impact of demographics and trip related factors on Turkish domestic passengers' WTP for various ancillaries

A survey was conducted among 450 passengers flying with one of the private airline companies from Istanbul Ataturk Airport to various domestic destinations between 27th of May and 1st of June 2013. In order to maintain the confidentiality, the airline will be referred to as "Airline A" in the following sections.

"Airline A" operates low fare scheduled domestic services to 14 destinations from its main base - Istanbul Atatürk International Airport. This location was chosen as it maximised the potential of acquiring respondents. Respondents were randomly selected to answer the questionnaire by three interviewers near the boarding gates of the corresponding flights in domestic routes. As passengers had dwell time while waiting for the boarding and they were more willing to answer the questionnaire. Between these dates, 23,864 passengers were carried in domestic routes from Istanbul (Domestic Network Manager, 2013). At 95% of confidence interval, the sample size required for the survey was 378 passengers. Therefore, the sample size of 450 passengers represented a reasonable balance between robustness of results.

The questionnaire was divided into 4 parts. Questions in part 1 collected information about respondents' intended trip such as the destination he / she is flying to, purpose of the flight, and the way of booking the ticket. Respondents were also asked to reveal the number of domestic flights they had in the last 12 months.

In the second part of the survey, respondents were asked to declare information about their past purchase behaviours for various ancillary services. In this part, the priorities of the respondents in terms of different service levels were also assessed.

The third part of the survey collected information about respondents' WTP for various ancillary services and assessed their attitudes towards optional services offered by the airlines. In this part, stated preference method was used including a mixture of CVM questions such as dichotomous choice and payment card (Figure 4). Based on the findings from other airlines and suggestions by industry experts in Turkey, various ancillary services which may be suitable to apply in Turkish domestic market were identified to be included in this part. Prices of similar ancillaries offered by different airlines abroad are used as a base and price options were decided together with Domestic Network Manager (2013) of "Airline A" (Expert Judgement Technique, see pg. 7).

The forth part of the survey gathered demographic and socio-economic information of the respondents such as gender, age, occupation and monthly income. Passengers' usage of smartphones and social media is also assessed in this part.

LIMITATIONS AND RESEARCH ASSUMPTIONS

Conducting a survey was decided to be the best method to reach the objectives of the research. However, the survey was applied only to "Airline A" passengers. The results of the survey may vary for different carriers. The results may also be different for passengers if conducted at different airports in Turkey.

It is assumed that the respondents answered the questionnaire sincerely by providing true answers. In order to avoid the potential response bias that may be caused due to boredom of respondents while answering the questionnaire, the questions were made multiple-choice and easy to answer. It did not last more than 12 minutes for a respondent to answer the questionnaire. It is also assumed that the customers' valuations of the items would represent their actual purchasing behaviour.

ANALYSIS

The sample consisted of 450 useable responses comprising 62% males. The sample had a considerably young population with 70% of the respondents are between the ages of 19 and 35. In addition, the sample consisted of individuals with different income levels (Figure 7). This may be due to the high competition in Turkish domestic aviation market and affordable ticket prices that enable people from various income levels to be able to fly domestically. In Turkey GDP per capita per month was 1,715 TL (Turkstat, 2015).

Figure 7: Distribution of Monthly Income

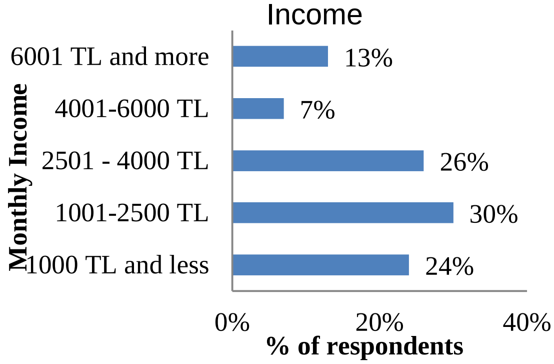
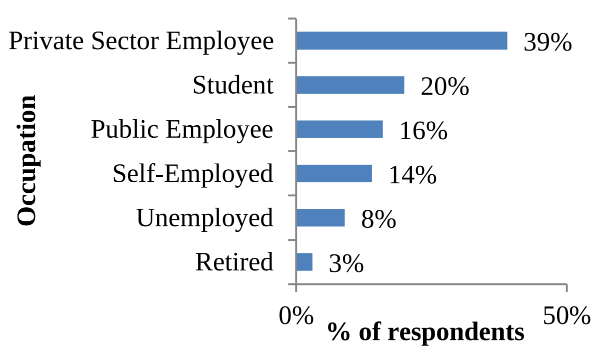


Figure 8: Distribution of Occupation



Distribution of occupation of the sample is given on Figure 8. Unemployed respondents represented 9% of the sample, which was close to Turkey's unemployment rate of 9% in 2013 (Turkstat, 2014). The sample consisted of passengers flying to 12 different domestic destinations (Figure 9). Respondents who were flying to Antalya, Izmir, Samsun and Erzurum constituted 61% of the sample.

Of the total sample, 32% of the respondents flew for Leisure purpose, 27% for Visiting Friends and Relatives (VFR), 24% for Business, 6% for Education and 11% for other purposes. In addition, 65% of the respondents bought their tickets online through the airline's webpage, 20% through travel agencies, 7% through airport sales office, 3% through airline's call and 5% through other ways.

Figure 9: Domestic Flight Destinations Included in the Analysis

Source: (Great Circle Mapper, 2013)

In order to simplify the analysis process, short names were created to represent ancillary services included in the survey. The explanations of short names are presented on Table 3.

Table 3: Explanation of Short Names of Ancillary Services

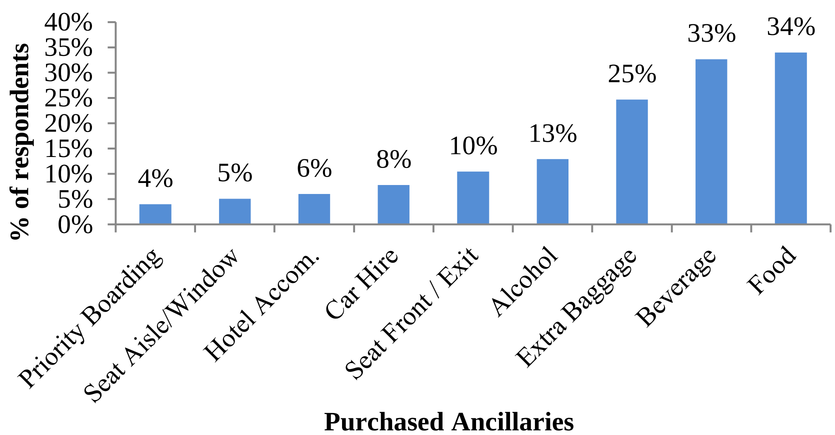
Airport transfer: Fee for transferring the passenger from or to the airport
Alcohol: Fee for having one alcohol drink on-board
Baggage priority: Fee for having a priority tag on the checked baggage, which allows the passenger to receive it ahead of everyone at the destination airport
Beverage: Fee for having one beverage on-board
Breakfast: Fee for having breakfast menu including pastry, bread, cheese, olives, butter, honey etc. with tea / coffee on-board
Concierge: Fee for a concierge service where an agent meets and assists the passenger at the airport and ease him/her through check-in, security and baggage delivery

Table 3...

Destination booklet: Fee for receiving a “destination booklet”, which includes map, train/bus timetables, important contact details, hotels and key sites of interest, as an email
Empty seat: Fee for keeping the seat next to the passenger empty
Exit / Front seat: Fee for reserving exit/front seats with more legroom
Extra baggage: Fee for carrying one extra (2nd) baggage
Farelock: Fee for freezing the ticket fare on the same level for three days
Food: Fee for having a sandwich or snacks on-board
Fresh food: Fee for having fresh food (daily made fresh sandwiches and salads) on-board
Hot food: Fee for having hot food on-board
Baggage Delivery: Fee for baggage delivery service where passengers do not wait for the luggage and is delivered to his/her home, hotel or office after the flight
Mobile notification: Fee for receiving mobile notification about the flight status, boarding time, gate number, delay etc. after booking.
Pillow: Fee for having pillow on-board
Priority check-in / boarding: Fee for priority during check-in and boarding, where passengers do not wait on the queue and board the aircraft ahead of everyone.
Reserved seat: Fee for reserving window or aisle seat
Snapshot: Fee for having a snapshot photo service on-board
Ticket flexibility: A “no restriction” fee for removing all cancellation and change restrictions on the ticket
Turkish coffee: Fee for having Turkish coffee on-board
Turkish tea: Fee for having Turkish tea on-board

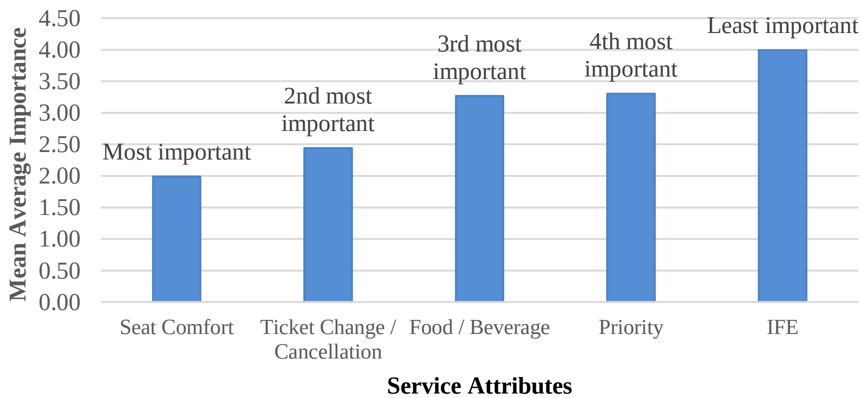
The three mostly purchased ancillaries by the respondents during their domestic flights were “Food and beverage” sold on-board and “Extra baggage” (Figure 10). These past purchase behaviours may represent the settled travel habits of Turkish people. It can be interpreted that Turkish domestic passengers value eating and drinking on-board and they tend to travel with extra baggage or heavy load. On the other hand, only minority of the respondents purchased other ancillaries mentioned in Figure 10 during their domestic flights.

Figure 10: Past Purchase Behaviours of Respondents



In the second part of the survey, respondents were asked to rank five different service attributes in terms of their importance on a scale of 1 to 5 for their domestic flights, where “1” was the most important and “5” was the least important. According to the results, respondents valued “Seat comfort” and “Ticket change and cancellation” as the two most important service attributes. Having “Food and beverage” on-board were also very popular among respondents (Figure 11). The maximum flight duration from Istanbul to farthest destination is 110 minutes, therefore it is not surprising that “In-flight Entertainment (IFE)” was ranked as the least important service attribute. Figure 11 may help airlines to determine which ancillaries to focus on. Ancillaries related to comfort, flexibility, food and beverage are valued the most by the respondents and offering such ancillaries may provide revenue opportunities for airlines.

Figure 11: Importance of Service Attributes for Passengers



Note: The smaller the value the more important the factor

In the third part of the survey respondents were asked to select their WTP amount from a range of options. Table 4 illustrates that majority of the respondents were willing to pay for “Farelock”, “Ticket flexibility”, “Food”, “Beverage” and many other ancillaries.

Table 4: Willingness to Pay Data

	% of Respondents Willing to Pay	**Mean WTP Value**
Farelock	90%	Low
Ticket flexibility	83%	Medium
Food	73%	Low
Beverage	69%	Low
Hotfood	64%	Low
Concierge	63%	Medium

Table 4…

Airport transfer	60%	Low
Baggage priority	57%	Low
Extra baggage	57%	Medium
Front / Exit Seat	57%	Medium
Breakfast	55%	Low
Alcohol	53%	Medium
Destination booklet	52%	Low
Mobile notification	50%	Low
Turkish coffee	49%	Very low
Priority check-in/ boarding	49%	Low
Wi-Fi	48%	Low
Fresh food	47%	Low
Snapshot	46%	Low
Turkish tea	46%	Very low
Reserved seat	44%	Low
Pillow	44%	Low
Baggage delivery	44%	Low
Empty seat	43%	Low

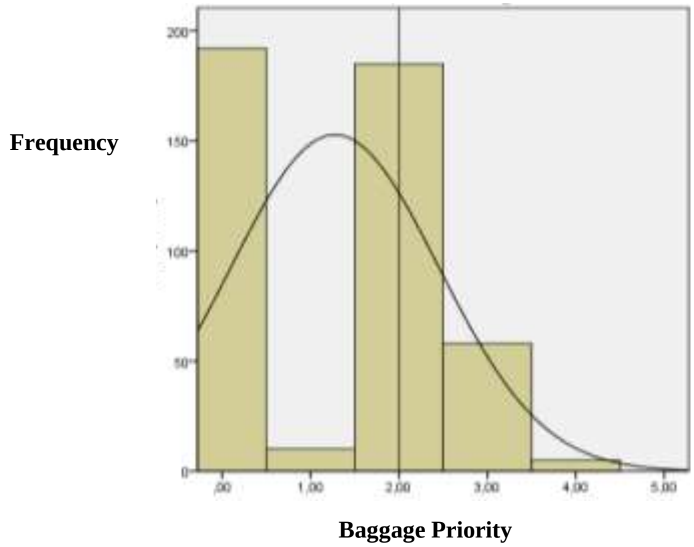
Although only minority of respondents are willing to pay for some ancillaries, these items may still bring considerable revenues to airlines. For instance only 43% of the respondents were willing to pay for “Empty seat”; however this percentage is quite sufficient for this ancillary since offering only a limited number of empty seat options on every flight would be logical.

Table 5: WTP Coding for Baggage Priority

Price	Likert Code		Frequency
0-0,99 TL	0	Very low	192
1-2 TL	1	Low	10
3-5 TL	2	Medium	185
5-8 TL	3	High	58
9-12	4	Very High	5
Total			450

In order to better interpret the WTP data, price range options for each ancillary item were coded on a 5-point Likert scale by 0 being “Very Low”, 1 being “Low”, 2 being “Medium”, 3 being “High” and 4 being “Very high” by considering its max and min WTP amounts. The mean results for each ancillary were then calculated (Figure 12). For instance, although 57% of the respondents were willing to pay for “Baggage Priority”, the mean WTP value corresponds to “low” scale (Table 5).

Figure 12: Distribution of WTP for Farelock – Histogram SPSS Output



On the other hand, "Ticket flexibility", which was also willing to be purchased by majority of the respondents, brings "medium" revenue considering its max and min WTP amounts (Table 4). This data would help airlines in deciding which ancillaries to launch, since both the % of passengers willing to pay for each ancillary item, and the revenue potential of each item should be considered.

The third part of the survey also aimed to assess respondents' attitudes towards optional services offered by the airlines. Selling lottery tickets or scratch cards on-board was an idea adopted from Ryanair, the Irish LCC. However, the survey respondents indicated that they were not interested in the idea at all (Figure 13). On the other hand, majority of the respondents were interested in buying "Local public transportation cards" of their destination if sold on-board (Figure 14). Selling these transportation cards could be another ancillary revenue opportunity for Turkish domestic carriers.

Figure 13: Willingness to Buy Lottery Tickets / Scratchcards Onboard

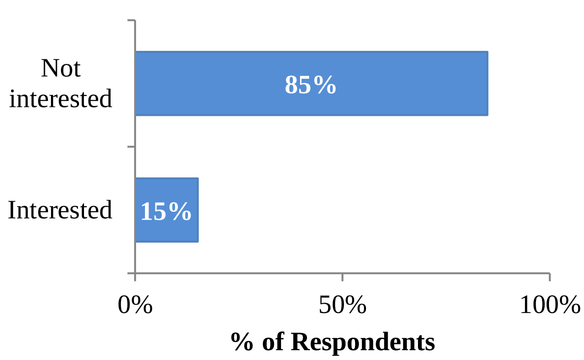
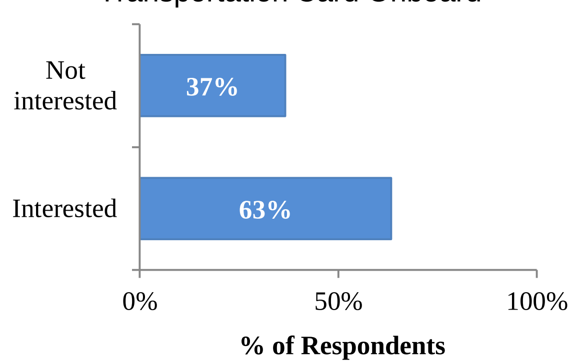


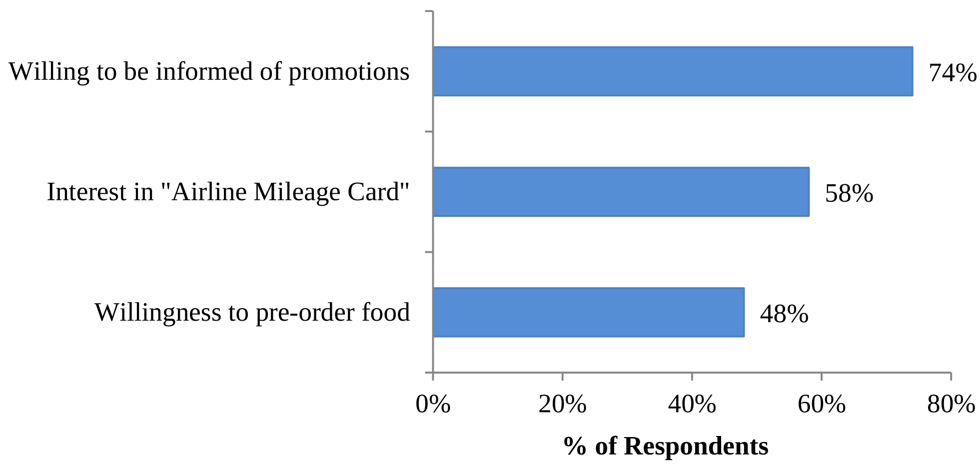
Figure 14: Willingness to Buy Public Transportation Card Onboard



Moreover, 58% of the respondents were interested in having an “Airline Mileage Card” in partnership with one of the banks where they could earn miles or points with every purchase they make with that card (Figure 15). This may provide another favorable opportunity for airlines to generate additional revenue through sale of miles to banks or other institutes for new and alternative ways of using collected miles.

Also, 74% of the respondents were ready for giving their contact details to be informed of airline promotions (Figure 15). This would also provide a golden opportunity for airlines to keep in touch with its passengers more effectively through e-mails and mobile text messages with suitable ticket and non-ticket ancillary offerings based on their past purchase trends and demographic characteristics.

Figure 15: Other Willingness and Interests of Respondents



The data related to past purchase behaviours reveals that pre-ordering was not very common among the respondents in their domestic travels. Majority of the respondents used to purchase the ancillaries either on-board or at the counter (Table 6). However almost half (48%) of the respondents stated that they were willing to pre-order food while booking their tickets (Figure 15). This would be another important ancillary revenue opportunity which airlines may make use of. By encouraging customers to pre-order ancillaries while booking their tickets, airlines can generate additional revenue while satisfying customers with variety of offers and saving costs by not loading unused food on-board.

Table 6: Payment Methods of Past Purchases

	While booking	On-board	Both
Beverage	9%	72%	19%
Alcohol	9%	66%	26%
Food	8%	71%	20%
	While booking	**At the counter**	**Both**
Extra Baggage	41%	33%	26%
Seat Front / Exit	30%	34%	36%
Seat Aisle/Window	33%	29%	38%

Hypothesis Testing

As part of the research, it was aimed to analyse the impact of demographics and trip related factors on passengers' willingness to pay for ancillary services. As the WTP data was categorical, Chi-Square analysis was used to reach the goal.

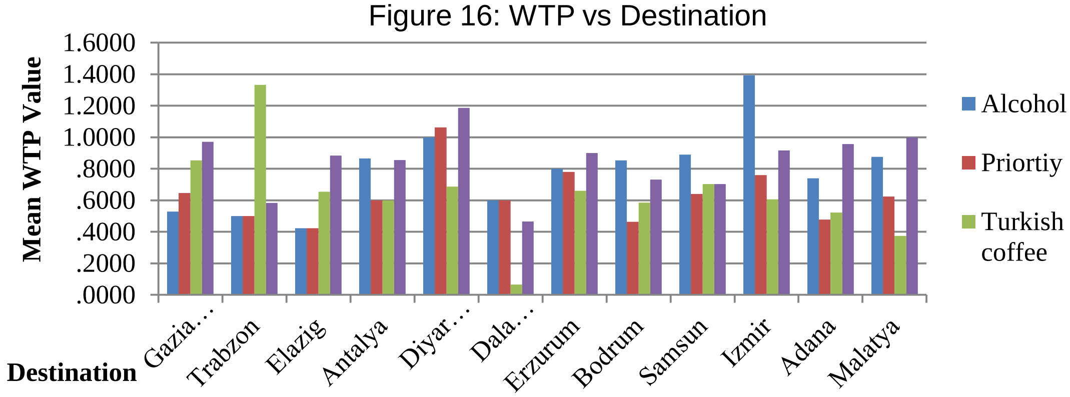
Ho: Flight destination has no effect on WTP for ancillaries listed on Table 3.

Table 7: Pearson Chi-Square p-values for Flight Destination

Flight Destination - Alcohol	,000
Flight Destination – Priority Check-in / Boarding	,050
Flight Destination – Turkish coffee	,001
Flight Destination – Mobile notification	,008
Flight Destination – Destination booklet	,039

According to the analysis it was found that "Flight destination" had an effect on respondents' WTP for "Alcohol" "Priority check-in / boarding", "Turkish coffee", "Mobile notification, and "Destination booklet" ancillaries. For the rest of the ancillaries, "Flight destination" had no effect on respondents' WTP (Table 7).

Figure 16: WTP vs Destination



Respondents flying to Izmir had the highest WTP amount for “Alcohol” ancillary whereas Elazig passengers had the lowest (Figure 16). This was in accordance with the finding that alcohol consumption is highest in the western part of Turkey (Hurriyetdailynews, 2014). The figure also revealed that Diyarbakır passengers had the highest WTP amount for “Priority check-in/ boarding” and “Mobile notification” ancillaries. According to an interview made with Ground Operations Manager of the company, it was declared that Diyarbakır passengers were usually impatient and very intolerant even to small delays. This declaration is closely parallel with the findings. In addition, Diyarbakir passengers were willing to pay higher amounts for “Mobile Notification”. This may also be an indication that these passengers are more willing to receive updated information about their flights regularly in order to avoid last minute surprises and problems. An interesting finding was that Trabzon passengers were willing to pay highest average amount for “Turkish coffee”.

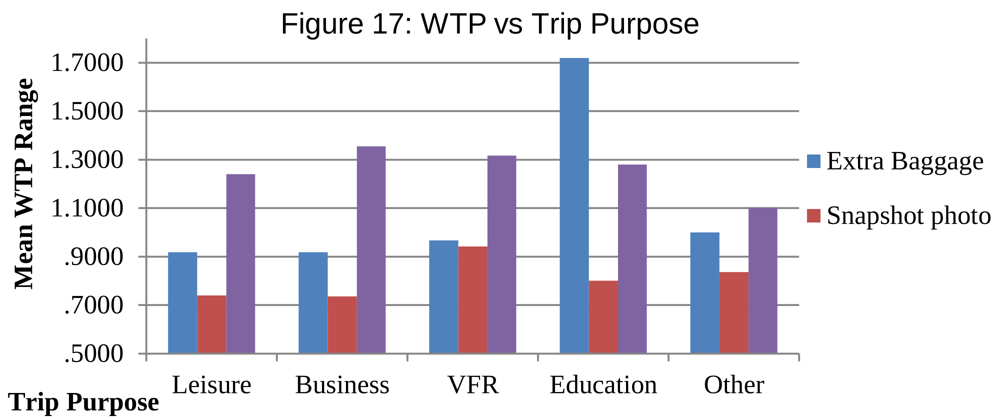
Ho: Trip purpose has no effect on WTP for ancillaries listed on Table 3

Table 8: Pearson Chi-Square p-values for Trip Purpose

Trip Purpose - Extra Baggage	,028
Trip Purpose – Snapshot	,003
Trip Purpose – Baggage priority	,049

The analysis revealed that “Trip Purpose” had an effect on respondents’ WTP for “Extra baggage” “Snapshot” and “Baggage priority” ancillaries (Table 8).

The data revealed that respondents flying for education purpose were willing to pay the highest amount for “Extra baggage” (Figure 17). This may be due to carrying study materials or too much belongings from where they study to home and vice versa. The analysis also revealed that respondents flying for VFR purpose were willing to pay the highest amount for “Snapshot” compared to respondents flying for other purposes. Moreover, business passengers had the highest mean WTP value for “Baggage priority”. Business passengers usually want faster service and receiving their baggage quickly at the destination airport seems to be important for them.



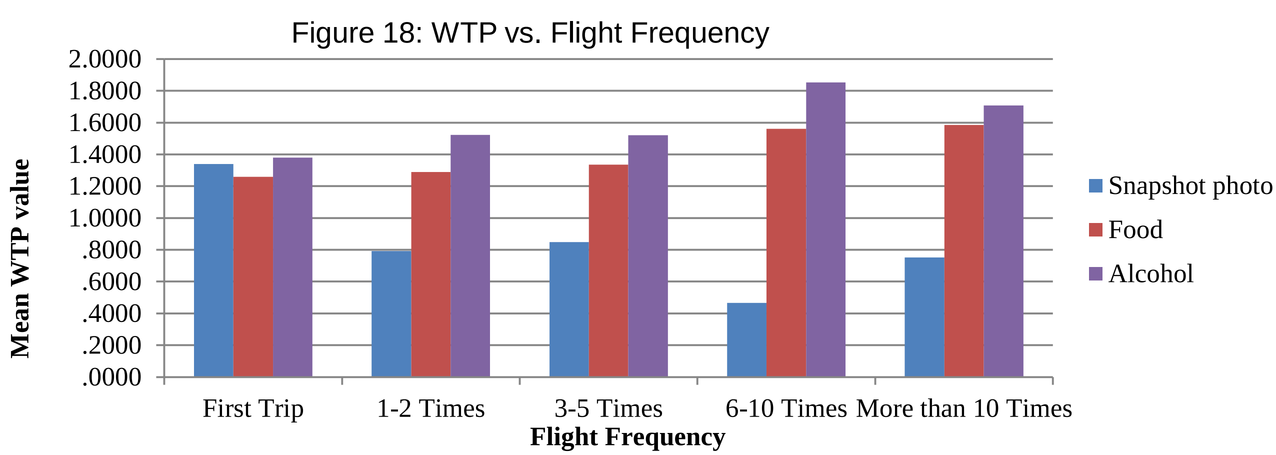
Ho: Flight frequency has no effect on WTP for ancillaries listed on Table 3.

Table 9: Pearson Chi-Square p-values for Frequency

Frequency – Food	,008
Frequency – Alcohol	,005
Frequency – Snapshot	,001

The analysis revealed that "Frequency" had an effect on respondents' WTP for "Food", "Alcohol", and "Snapshot" ancillaries (Table 9).

The data revealed that respondents, who were flying domestically for the first time this year, were willing spend the highest average amount for "Snapshot" than all other respondents. The reason may be that flying for these respondents is a rare thing to do and that they want to keep the in-flight photo as a memory. Although there was no linear relationship between the WTP value and flight frequency, respondents flying 6 times and more were willing to spend higher amounts for "Food" and "Alcohol" ancillaries (Figure 18).



Ho: Gender has no effect on WTP for ancillaries listed on Table 3.

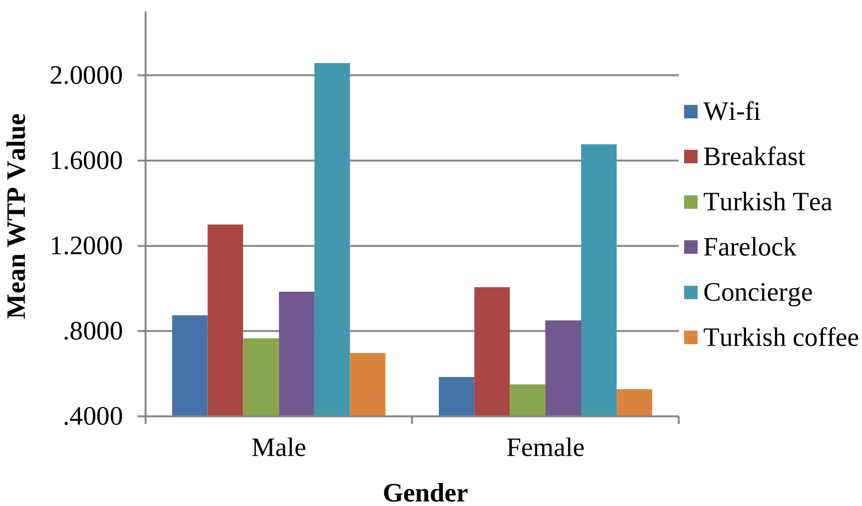
Table 10: Pearson Chi-Square p-values for Gender

Gender - Wi-Fi	,031
Gender – Breakfast	,039
Gender – Farelock	,016
Gender – Concierge	,019
Gender – Turkish coffee	,045
Gender – Turkish tea	,008

It was found that “Gender” had an effect on respondents’ WTP for “Wi-Fi”, “Breakfast”, “Farelock”, “Concierge”, “Turkish coffee, and “Turkish tea” ancillaries (Table 10).

The data revealed that male respondents were willing to pay higher amounts than females for “Wi-Fi”, “Breakfast”, “Farelock”, “Concierge”, “Turkish coffee, and “Turkish tea” ancillaries (Figure 19). This may indicate that men give more importance to eating and drinking on-board and in-flight connectivity than women. The findings may also indicate that premium services such as “Concierge” and flexibility options such as “Farelock” seem to be more important for male passengers. Male passengers may be targeted to promote these ancillaries even more.

Figure 19 : WTP vs Gender



Ho: Age Group has no effect on WTP for ancillaries listed on Table 3.

Table 11: Pearson Chi-Square p-values for Age Group

Age – Alcohol	,020
Age - Pillow	,005
Age - Exit/front seat	,000
Age - Reserved seat	,001
Age - Priority check-in/boarding	,001
Age - Baggage priority	,004
Age - Extra baggage	,003
Age - Concierge	,013
Age - Baggage delivery	,016
Age - Empty seat	,017
Age - Snapshot	,000
Age - Destination booklet	,000
Age - Wi-fi	,000
Age - Airport transfer	,047
Age - Turkish tea	,048

“Age Group” had an effect on respondents’ WTP for, “Alcohol”, “Pillow”, “Exit/front seat”, “Reserved seat”, “Priority check-in / boarding”, “Baggage priority”, “Extra baggage”, “Concierge”, “Baggage delivery”, “Empty seat”, “Snapshot”, “Destination booklet”, “Wi-fi”, “Airport transfer” and “Turkish tea” ancillaries (Table 11).

The data revealed that young respondents (younger than 25) tend to pay higher amounts for these ancillaries (Figure 20, Figure 21, and Figure 22). This may indicate that young passengers are willing to spend more money while traveling compared to other age groups. Respondents between 19 and 25 years old are willing to spend highest amounts for “Alcohol”. Since alcohol can be consumed only after the age of 18 in Turkey, respondents at this age group may be more willing to spend higher amounts to enjoy the legality of alcohol consumption in their very first years.

Figure 20: WTP vs. Age Group -1

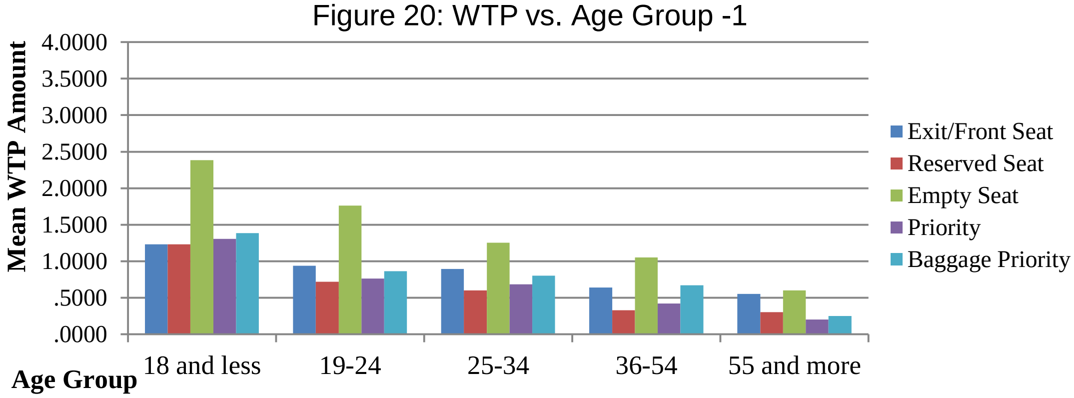


Figure 21: WTP vs. Age Group -2

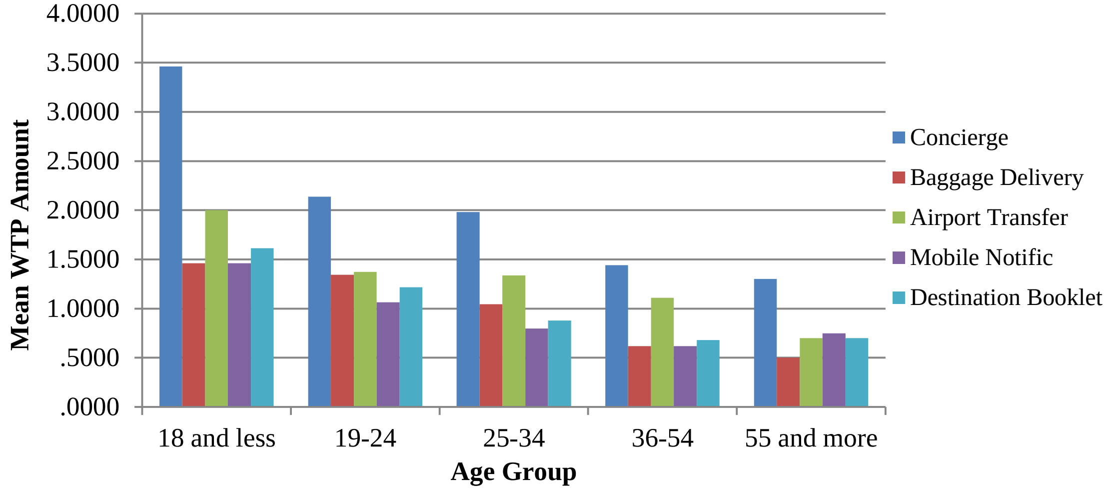
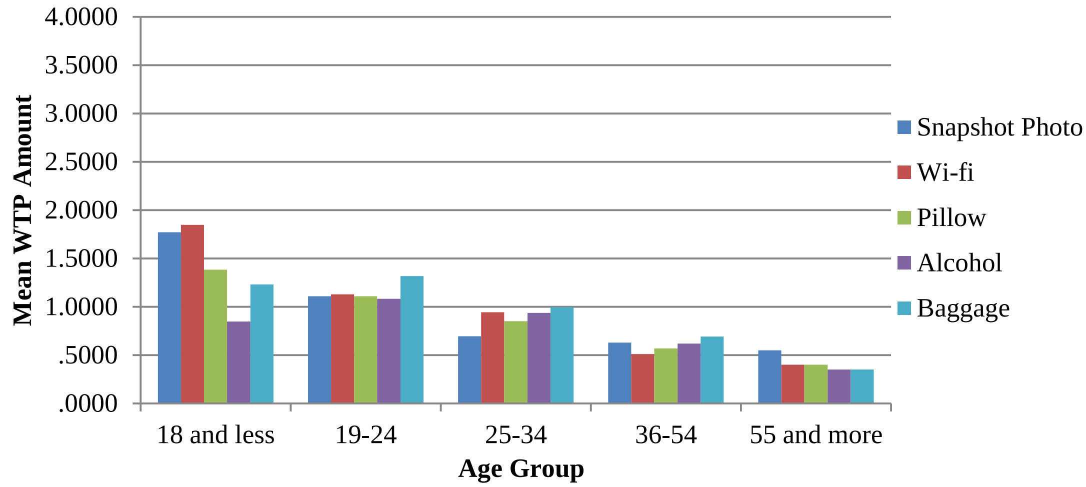


Figure 22: WTP vs. Age Group -3



Ho: Occupation has no effect on WTP for ancillaries listed on Table 3.

Table 12: Pearson Chi-Square p-values for Occupation

Occupation – Reserved Seat	,028
Occupation - Extra baggage	,004
Occupation - Wi-Fi	,040
Occupation - Hotfood	,022
Occupation - Farelock	,035
Occupation - Concierge	,024
Occupation – Destination booklet	,001

It was found that “Occupation” had an effect on respondents’ WTP for “Reserved seat”, “Extra baggage”, “Wi-Fi”, “Hotfood”, “Farelock”, “Concierge” and “Destination booklet” ancillaries (Table 12).

The data revealed that students were willing to pay higher amounts for “Reserved seat”, “Extra baggage”, “Wi-fi”, “Hotfood” and “Destination booklet” ancillaries (Figure 23 and Figure 24). This may indicate that students are willing to spend more money while traveling compared to other occupation groups. This finding is parallel with the finding on Figure 20, Figure 21 and Figure 22, as the students are mostly younger than 25 years old. Targeting younger age groups and students may help airlines to generate high revenues especially through selling mentioned ancillaries.

The analysis also revealed that self-employed respondents were willing to pay the highest amount for “Concierge” than respondents’ in other occupation (Figure 24). It may be due to the fact that self-employed businessmen or businesswomen may need more premium service at the airport and want to be treated differently with concierge service. Although retired respondents were willing to spend the lowest amounts for many of these ancillaries, they were willing to pay higher amounts for “Snapshot”.

Figure 23: WTP vs Occupation -1

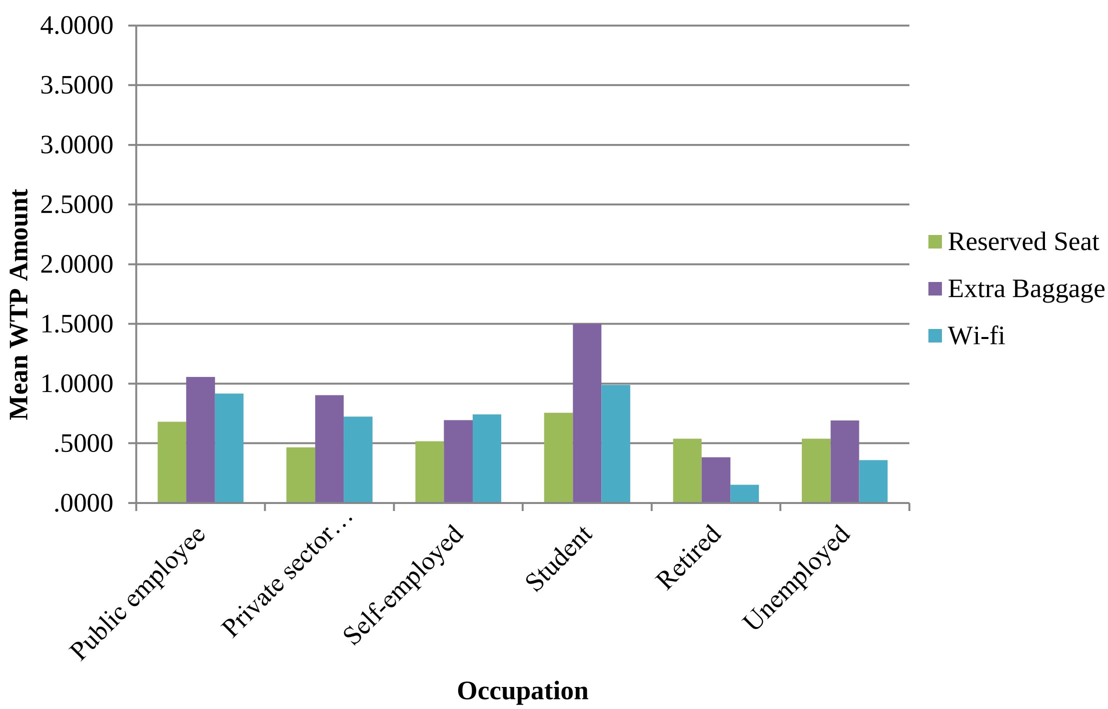
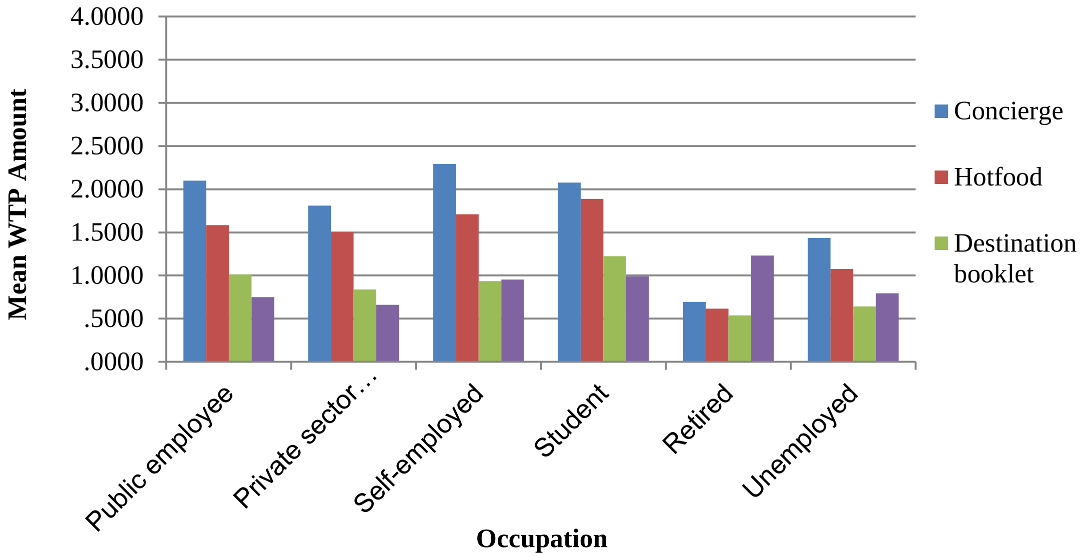


Figure 24: WTP vs Occupation -2



Ho: Income level has no effect on WTP for ancillaries listed on Table 3.

Ho: Way of ticket booking has no effect on WTP for ancillaries listed on Table 3.

The analysis revealed that “Income” and “Way of booking” had no effect on respondents’ WTP for ancillary services.

Re-bundling Opportunities

It was found that ancillaries that were not very popular among respondents were “Reserved seat”, “Pillow”, “Empty seat”, “Turkish tea” and “Turkish coffee”. Some of these unpopular ancillaries may have low correlation with popular ancillaries such as “Farelock”, “Ticket flexibility”, “Food”, “Beverage”, “Hot-food” and “Concierge”. As the literature suggests, re-bundling is likely to increase profits when the correlation of consumers’ valuations for individual items included in the bundle is small or negative. In other words, if the unpopular items are bundles with popular ones, the customer who is not normally buying the unpopular product appears to buy it. As a result, airlines sell more à-la-carte services than when they are sold individually.

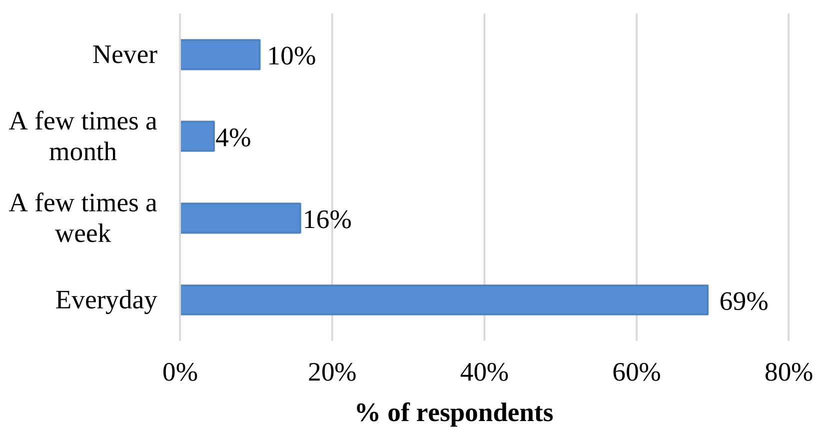
Therefore, in order to create a re-bundling opportunity for airlines, a correlation analysis for the percentage of respondents’ WTP for various ancillaries was conducted. According to the correlation analysis, some items which have low correlation with others and which may be re-bundled as a single item price were discovered (See Appendix A). Based on the analysis, it is suggested that the following group ancillaries could be bundled and offered customers under branded fares groups:

- Farelock + Front/exit seat + One beverage
- Farelock + Priority check-in/boarding + One beverage
- Flexibility service + Front/exit seat + One beverage
- Flexibility service+ Fresh food (salad or sandwich) + Turkish coffee
- Concierge service + Front/exit seat + one beverage
- Concierge service + Fresh food (salad or sandwich) + Turkish coffee
- Baggage delivery service + One cold food + One beverage
- Empty seat option + Breakfast or Fresh food + Turkish coffee
- Snapshot + One cold food + One beverage
- Airport transfer + Breakfast or fresh food + Turkish coffee
- Hot food + Baggage priority + Turkish coffee

Mobile Phone and Social Media Usage

Majority of the respondents (78%) were using smart phones. As explained before, mobile devices have a huge potential for generating ancillary revenue. Moreover, as can be seen on Figure 25, majority of the respondents use social media almost every day. However, among 403 social media users, the percentage of the respondents following the airlines page on social media is only 35%.

Figure 25: Social Media Usage of Respondents



It is recommended that airlines provide smartphone or tablet applications, which synchronizes with the customers' social media accounts. In this way, they can generate additional information about the passengers and offer them the most suitable ancillaries.

CONCLUSIONS

Determining what ancillaries to offer is a challenge for airlines. The key to success is not to offer many ancillaries, but to offer selective ones targeted to various flyer segments. Therefore understanding behaviours and preferences of different customer segments and providing value-added services that address their needs becomes crucial for an effective ancillary revenue strategy.

This study revealed that Turkish domestic passengers were willing to pay for many of the ancillaries included in the survey. Moreover, it was revealed that demographics and trip related factors such as flight destination and purpose of flight had a significant impact on passengers' WTP for different ancillaries. The impact of demographic factors and trip related factors may be taken into while tailoring the ancillary offers to different travellers. Stated preference (SP) and willingness to pay (WTP) data obtained through passenger surveys as well as historic consumption habits may also be used to optimize ancillary offerings and their pricing. The differences in respondents' WTP would help airlines to segment their customers and tailor their ancillary offerings accordingly. Moreover, certain customer segments that are more likely to pay for ancillary services than others segments may be considered for promotions, bundled offers and discounts. However, it is essential to analyse the revenue contribution of each ancillary service offered for each customer segment to ensure profitability, which is beyond the aim of this research.

Some ancillaries that were not very popular among respondents can be bundled with popular ones and in this way airlines sell more à-la-carte services than when they are sold individually. However, while implementing bundles or fare families, airlines must ensure that offering bundled fares are more profitable than offering individual services separately on an a la carte basis, which requires further research.

There are certain unique offers that Turkish domestic passengers would ignore such as selling lottery and scratch cards should never be attempted in order not to annoy them. "Nickel and dime" situations should be avoided.

Investment in mobile technology is critical in helping airlines to differentiate their services and to generate additional revenue. It is recommended that airlines provide smartphone or tablet applications, which synchronizes with the customers' social media accounts. In this way, they can generate additional information about the passengers and offer them the most suitable ancillaries. In addition, airlines should efficiently use their booking engine that is the strongest tool in their hands and where most of the ancillary revenue comes from.

Finally, the planning, pricing and revenue management of ancillary services is becoming a highly important issue that needs to be focused on. In the near future, investment in the right technology to vary ancillary fees based on purchase date, peak travel periods and other factors like the way done for ticket prices would become crucial.

SCOPE FOR FURTHER RESEARCH

The concept of ancillary revenue is still new in Turkish airline market and there has not been any study conducted about it until now. Further research could be conducted in order to explore more ancillary revenue opportunities in Turkish aviation market and to identify passengers' WTP for potential new ancillaries. In addition, for industry wide acceptance and validity, the survey included in this analysis could be undertaken with a significantly higher sample size. Further research could also be conducted surveying respondents at different parts of the country in order to explore local variations in WTP for different ancillaries. Moreover, a similar research that focuses fully on Full-Service Carriers (FSCs) could also be conducted. Finally, an investigation into other ancillary revenue categories such as revenue through advertising and frequent flyer programs (FFPs) could be carried out in order to have a complete understanding of the ancillary revenue concept in the market.

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APPENDİCES

APPENDIX A: Correlation Table between Ancillaries' Willing to be Purchased

Correlations

	Food	Bever age	Alcohol	Pillow	Exit/ front Seat	Reserv Seat	Priority	Bag. priority	extra Bag.	Wifi	Airport Transfer	Fare- lock	Flex- ibility	Con- cierge	Bag. Delivery	Empty seat	Mobile notif.	Dest. booklet	Hot food	Break- fast	Fresh food	Turkish coffe	Turkish tea
Food	1	,801**	,397**	,495**	,510**	,452**	,390**	,429**	,490**	,417**	,494**	,053	,160**	,151**	,126**	,085	,125**	,160**	,220**	,253**	,259**	,180**	,223**
Beverage		1	,424**	,538**	,541**	,488**	,437**	,473**	,502**	,471**	,491**	-,021	,172**	,169**	,129**	,156**	,129**	,176**	,249**	,280**	,308**	,139**	,243**
Alcohol			1	,368**	,409**	,281**	,367**	,382**	,472**	,445**	,423**	,011	,116*	,150**	,151**	,153**	,125**	,198**	,245**	,195**	,194**	,173**	,176**
Pillow				1	,589**	,599**	,566**	,535**	,517**	,523**	,459**	,015	,214**	,213**	,161**	,205**	,228**	,238**	,253**	,201**	,215**	,163**	,191**
Exit/front seat					1	,672**	,597**	,582**	,582**	,588**	,566**	-,011	,172**	,205**	,144**	,238**	,234**	,304**	,213**	,171**	,209**	,191**	,185**
Reserv seat						1	,686**	,618**	,555**	,599**	,579**	,028	,171**	,205**	,140**	,256**	,277**	,313**	,216**	,177**	,202**	,119*	,179**
Priority							1	,786**	,651**	,595**	,626**	,004	,207**	,178**	,225**	,198**	,245**	,250**	,194**	,208**	,210**	,225**	,190**
Baggage priority								1	,646**	,588**	,639**	-,015	,200**	,172**	,252**	,192**	,207**	,223**	,176**	,198**	,182**	,220**	,257**
Baggage									1	,642**	,630**	-,008	,229**	,164**	,280**	,219**	,216**	,232**	,251**	,216**	,227**	,198**	,149**
Wifi										1	,636**	,002	,200**	,196**	,218**	,209**	,240**	,274**	,289**	,206**	,178**	,142**	,192**
Airport Transfer											1	-,015	,142**	,148**	,238**	,187**	,222**	,282**	,214**	,209**	,236**	,187**	,204**
Farelock												1	,027	,008	-,033	,047	,105*	,064	,054	-,002	-,022	,033	,078
Flexibility													1	,179**	,075	,221**	,197**	,135**	,138**	,134**	,139**	,099*	,037
Concierge														1	,178**	,290**	,171**	,222**	,319**	,177**	,132**	,107*	,138**
Baggage Delivery															1	,215**	,130**	,121*	,222**	,209**	,189**	,159**	,120*
Empty seat																1	,363**	,311**	,331**	,103*	,170**	,098*	,092
Mobile notification																	1	,507**	,251**	,161**	,185**	,123**	,094*
Destination booklet																		1	,262**	,153**	,104*	,126**	,146**
Hotfood																			1	,312**	,354**	,182**	,232**
Breakfast																				1	,648**	,390**	,457**
Fresh food																					1	,439**	,482**
Turkish coffe																						1	,510**
Turkish tea																							1

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).