



“2010 Airline Ticket Rate Forecast and Buyer Strategies”

Industry Forecast: 1 – 7% increase

CTBR Forecast: much larger increases (see below)

Airline Ticket Rate Forecast: Every fall the top travel management companies promote their annual business airfare forecasts or predictions for the following year. If you track their performances you know they're rarely accurate. This includes last year when most predicted moderate single and even double digit rate increases for 2009. As we all know ticket prices actually declined in 2009 in most markets, even after you factor new ancillary service fees. The lack of reliability in airfare forecasting is partially due to the uncontrollable factors that make up the industry. It is also largely due to the narrow industry perspective and rearview mirror forecasting used by most travel companies. For example, the common logic behind last year's forecast of higher ticket prices in 2009 was the trending practice of the airline's to cut capacity. It was also based on the assumption that oil prices would once again surge during the peak of 2009. During this same time my office was advising clients to budget for relatively flat changes in ticket prices and even a decline throughout 2009. This was based on the logic that we were experiencing the largest recession on record with no end in sight. It would be extremely difficult for the airlines to raise rates in 2009, even though they were scaling back capacity. My forecast was also based on the assumption oil prices would most likely not surge during the peak of 2009, due to pressures of the global recession.

So here we go again as we enter into the fourth quarter of 2009 and begin our 2010 predictions. Most of the top travel companies have already gone on record predicting small to moderate air ticket increases of 1% - 7%. I'm going against their predictions again and forecasting much higher rate increases. In fact, I believe it's more likely we will experience double digit rate increases in many markets (*as high as 12% – 20%*). These increases will become more noticeable during the second half of the year and run through at least 2011. My prediction is based largely on the natural cycles of any market. For example, ticket prices have been declining for multiple quarters and this trend will probably continue through the first quarter of 2010. Regardless of supply and demand factors, air ticket rates will naturally rebound upwards to some degree and eventually climb to the higher end of my forecast by the end of 2010 and into 2011. Other contributing factors that will drive up the cost for business travelers in 2010 and beyond, include;

1. AIRLINE CASH RESTRAINTS: Over half of all carriers (legacy carriers and LCCs) are at risk of running out of cash between 2010–2012. There are very limited opportunities for even the strongest of airlines to attract favorable financing. To avoid liquidation and/or to obtain attractive funding an airline must develop a positive business model, which will require higher base ticket prices for the business traveler.

2. RETURN OF THE BUSINESS TRAVELERS: Industry associations are spending large sums of money hiring researchers and analysts to promote the value of business travel. The value arguments primarily cover air travel related to servicing customers and new business development (external travel). External travel has not declined significantly at many companies. However, it should grow moderately over the next couple of years as corporations look to expand their businesses after several years of stagnant or declining growth. Internal business travel, which is associated with the largest percentage of the current travel decline, will most likely never rebound to its prior levels. Unlike during the small recession of 2000 and then again after 9/11 when business travel declined for only several months, this current decline has already surpassed 5–7 quarters for many companies. Corporations have finally embraced remote technologies to conduct virtual meetings and to collaborate on projects from remote sites. Some may have cut back too much, but most are developing a good balance. This leaves the airlines with their newest competitors (the employee desktop, new technology and remote/central meeting centers). Another head wind against a strong rebound is the declining service and frustrations of air travel. For myself there has been at least a half dozen circumstances this past year where I would have normally jumped on a plane, but instead I chose to conduct the meeting remotely or used an alternative mode of transportation. Unfavorable scheduling and too many prior bad flight experiences were the top factors in my decision, not cost. Going forward, it is more realistic to predict internal business travel will only partially rebound, versus rebounding to historical levels. This will force the airlines to increase ticket rates on the remaining business travelers. Even if business travel immediately rebounds in 2010, the airlines will not be able to adjust capacity fast enough. Adding or subtracting capacity is a slow process with a lot of governmental red tape. The airline industry is continuously reacting several months or quarters behind the demand. This time around the airlines will be very slow and cautious to add capacity.

3. AIRLINE OPERATING EXPENSES: There is no expected expense relief on the horizon for an airline. In fact, it is more likely one or more of their top three expenses will increase over the next 12-24 months (fuel, labor and equipment). Most OPEC nations and other top oil producing countries and traders are anxiously awaiting the opportunity to push oil prices up once the recession passes the first few recovery hurdles. It is certainly more realistic to project an increase in oil prices next year, than a decline or status quo. Most airlines lack the cash for hedging to protect themselves from future price increases. Labor expenses may also increase in the near future. Airlines have already pushed the envelope too far with layoffs, outsourcing, pay freezes and longer work schedule requirements. Labor will push for increases and will work together with governments to develop new regulations that may reduce flying time for pilots and current outsourcing policies of some airline maintenance jobs that could all lead to an increase in labor cost. New equipment costs (aircrafts) will also increase over the next several years. Many airlines need to sunset old fleet due to escalating maintenance cost and all airlines will be forced to purchase new aircraft with the latest fuel efficient technology to satisfy new emission standards forthcoming. Another growing equipment cost for the airlines next year will be the expense of reconfiguring aircraft to accommodate the change in cabin class demand. All of the above spells a recipe of disaster for the airline industry, unless they increase base ticket prices for the business traveler.

Ancillary Fee Forecast: Ancillary fees have provided some revenue relief in 2009, but ancillary fees alone will not save the airline industry. Going into 2010 the airlines will continue to test and challenge the market with new ancillary service fees to supplement base ticket revenue. Wifi connection charges will become common as the service expands to more aircrafts. The largest fees will be associated with premium coach services on both domestic and international flights as aircrafts are reconfigured and the airlines adjust to life with less full paying business/first class passengers. Premium coach services and fees have the potential to create the largest administrative challenges for managed travel programs (policy and expense management controls), and could potentially result in some of the largest price increases for a business traveler. On a positive note, several airlines have recently announced programs to bundle and sell ancillary services at a packaged rate. If this practice continues it should provide the starting point for establishing a market baseline which will help corporate travel programs negotiate their most common ancillary services fees with their standard airline negotiations.

Capacity Restraint Forecast. The historical impact to a business traveler from capacity cuts was being forced to squeeze into an overcrowded coach cabin or scrambling to secure a free upgrade. Capacity challenges in 2010 will be greater as some business travelers will need to postpone or cancel an important business trip because there will be no seats to book. A recent internal poll of travel buyers is already indicating a rise in this trend in some markets. This trend should increase throughout 2010.

Counter-Strategies for Buyers: In preparation for managing air spend in 2010, my office is advising corporate travel buyers to focus on the following three areas; The first is to quickly notify senior management and key stakeholders of the potential rate increases forthcoming over the next 12 – 24 months. Most companies are budgeting for consistent expenses in their upcoming annual budgets. Budget planners need to be prepared for potential double digit increases, compared to 2009 usage levels and rates. Additional capacity restraints should also be assessed and communicated internally based on your specific travel markets.

The second area is the sourcing and negotiations of airline agreements. As airfares increase, so does the potential value of your agreements. Regardless of the current term, the pricing element in any airline agreement is always a quarterly negotiations or renegotiations. It is important for travel buyers to begin reassessing their spend and strategically prepare to renegotiate existing agreements or negotiate new agreements in 2010. This will require developing new buyer centric metrics for measuring and leveraging your spend, instead of relying on the traditional skewed market share models of the airlines and the other similar metrics reported by your TMC or their consulting divisions. And, finally, travel policies and expense reporting processes will also need to be reviewed and adjusted in 2010, especially to address all of the ancillary services fees and options. Two out of every three travel policies and expense reporting systems that I have assessed this year have gaps that present unnecessary exposure to the company.

As in many previous years, the airline industry is facing another bumpy ride for 2010. Buckle up and get ready for another exciting year. For more information on managing your air spend or other areas of your corporate travel program, contact:

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