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## **HIGHLIGHTS**

- A narrow range of unbundled products are shown in this study to be the most commonly purchased ancillaries for airlines
- There are statistically significant differences in willingness to pay for different ancillary products and services between long and short haul passengers, by journey purpose and length of haul
- Airlines can use the study's disaggregated WTP results to determine which ancillary products and services to focus on

# **AN ANALYSIS OF ONGOING TRENDS IN AIRLINE ANCILLARY REVENUES**

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## **AN ANALYSIS OF ONGOING TRENDS IN AIRLINE ANCILLARY REVENUES**

### **ABSTRACT**

Globally airline ancillary revenues have increased by 121% from 2010 to 2014 – and the trend is set to continue as carriers are quickly implementing structural changes to accommodate these revenues streams. This paper examines the performance of the two core classifications of ancillary revenues, which are unbundled products and commission based income. It also investigates the willingness of passengers to pay (WTP) for these services together with what type of ancillary items are acceptable at a particular price point. The study found that passengers value a narrow range of perceived ‘necessity’ products and services such as food and drink, checked baggage and seat assignment as opposed to perceived ‘optional’ unbundled or commission based products/services. It also found significant differences in WTP for specific ancillary services based on carrier type (FSC/LCC/Charter), length of flight (long and short haul) and journey purpose (business, leisure, VFR).

Key words: ancillary revenue, unbundled products, commission based income

## **1. Introduction**

Achieving profitability in the airline industry over the last few years has improved but remains challenging. The industry has only returned marginal profitability through the decades which can be directly attributed to its high fixed cost structure, overleveraged balance sheets, low barriers to entry, high barriers to exit, network fragmentation, strong unions, cyclical macroeconomics, fluctuating fuel prices, a unique regulatory environment, and monopolistic/oligopolistic suppliers – which are just a small sample of the ongoing barriers that impede profitability. However, IATA (2014a) reported that airlines worldwide generated net profits of almost \$20 billion in 2014, which were the highest in the industry to date but the overall net margin remains miniscule at just 2.7% which nets a return of around \$6 per passenger (IATA, 2015).

IATA's financial outlook forecasts into the near future are encouraging as it anticipates: strengthening GDPs; increasing passenger and cargo demand; improving industry structure and efficiency gains; together with increased traction in ancillary revenue earnings (IATA, 2014). These ancillary revenues are producing a fast paced paradigm leap in spawning addition income streams. O'Connell and Warnock-Smith (2013) describe ancillary revenue as income beyond the sale of tickets that is generated by direct sales to passengers, or indirectly as a part of the travel experience. Ideaworks (2014) estimated that these ancillary revenues amassed US\$49.9 billion from 116 airlines in 2014 as shown by category in Table 1, which is up by 121% from 2010. In comparison IATA reported that air cargo, which has been an embedded component since the inception of the airline industry only produced US\$62 billion in revenue in 2014. Clearly this exponential growth in ancillary revenue has positive ramifications that significantly benefit carrier financial performance while Ex-IATA Director General Bisignani (2014) stated that the practice is poised to become an integral aspect of the business model of airlines worldwide.

**Table 1 Worldwide Estimate of Ancillary Revenue – by Carrier Type for 2014**

<b>Airline category</b>	<b>Total Ancillary Revenue</b>	<b>Frequent Flyer Revenue</b>	<b>A la Carte activity</b>
Traditional Airlines	\$17.5 billion	\$10.5 billion	\$7.0 billion
US Major Airlines	\$15.4 billion	\$10.0 billion	\$5.4 billion
Champs	\$9.3 billion	\$0.5 billion	\$8.8 billion
Low Cost Carriers	\$7.7 billion	\$0.4 billion	\$7.3 billion
Worldwide totals	\$49.9 billion	\$21.4 billion	\$28.5 billion

Source: Ideaworks (2014)

At the 2014 IATA World Passenger Symposium, senior economists within IATA presented compelling research that proved that there is a positive correlation between airlines that had a high percentage of revenue from ancillaries and carriers that benefitted from high operating profits as a percentage of revenue. This research suggests that airlines should consider placing an increasing focus not only on selling their core airline products, but also on upselling and cross-selling of air and non-air ancillary products to increase the share of the wallet per passenger (IATA World Passenger Symposium, 2014). Aviation consultancy Oliver Wyman published a report in 2014 entitled ‘Airline Economic Analysis’ stating that airlines have found that passengers are less price-sensitive when it comes to ancillary fees, which renders it as an opportunistic revenue source that is being increasingly exploited (Wilson, 2014).

This study aims to examine the performance of the two core classifications of ancillary revenue, which are unbundled products and commission based income using a passengers’ willingness to pay method (at particular price points). It also aims to establish a willingness to use ranking between different ancillaries and passenger/carrier types based on the responses to a comprehensive passenger survey, the results of which add to the body of knowledge on the ancillary products airlines could focus on based on revealed passenger preferences by market segment, carrier type and length of haul.

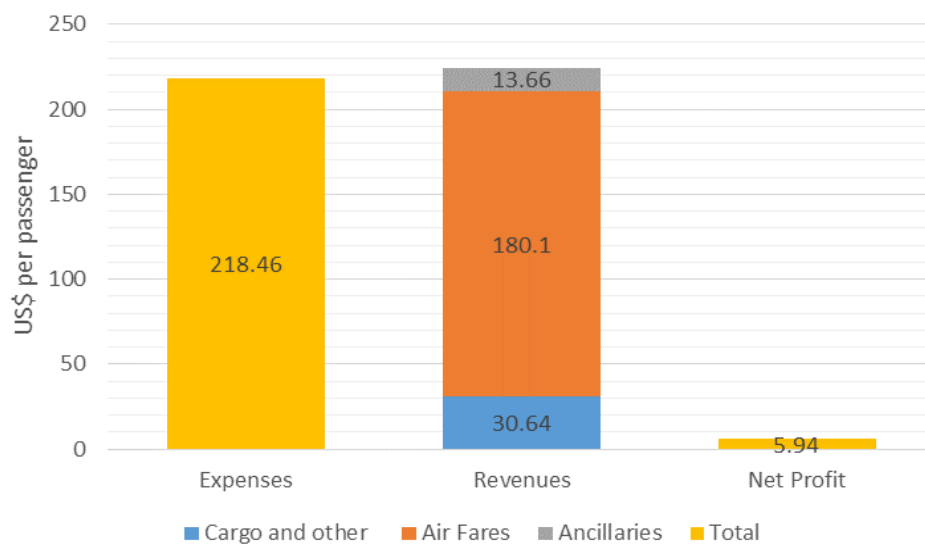
The study is broken down into 5 sections. Section 2 reviews the fast moving developments in ancillary revenues, Section 3 discusses the data collection phase and presents the descriptive results, Section 4 details the hypothesis testing results and Section 5 concludes.

## **2. Ancillaries: Recent developments**

Airline yields have continued to deteriorate over the last few decades as more entrants have joined the fray and today airlines operate in fiercely competitive ‘electronic markets’ which have made fares very transparent - while this has also forced archaic fare rules to be dismantled. This results in more ‘Y fare’ (unrestricted economy) passengers dropping down to lower fare buckets. In-turn, revenue management systems encounter less demand for higher fares and so makes them less available, leading to higher load factors, but lower yields. It is becoming more apparent that the traditional revenue management systems can no longer maximise revenues. However ancillary revenue is fast becoming an embedded engine that turns over increased revenues, which has become a core competency for many airlines within the marketing mix – thus its implementation is gaining much traction in airline boardrooms throughout the world. IATA now recognises that ancillary revenues have become a key component of the improved financial performance of the industry. The importance of ancillary revenue is evident when its \$49.9 billion projection is compared to the overall transport of 3.3 billion passengers globally and without such an income from ancillary components, the industry would be making a loss from its core seat and cargo products as shown in Figure 1. The scientific evidence to date is quite patchy and mainly focusses on the impact of the practice of unbundling fares on customer satisfaction and acceptance levels. Tuzovic et al. (2014) showed that the implementation of ancillary fees led to perceived traveler betrayal and anger, Waguespack et al. (2015) focused on fairness and transparency issues in relation to unbundled fees in the US airline industry and in contrast Scotti et al. (2016) found no impact of one particular category of unbundled charges, that of checked bags on underlying customer satisfaction levels in the US domestic market. Research to date is therefore still narrow in focus and in its infancy states with very little research on markets

outside the US, on other classifications of ancillary revenue such as commission based products and on the subject of ancillary revenues from a commercial airline business perspective rather than purely from a consumer standpoint (i.e. researching how airlines can devise commercial driven ways for customers to move from viewing ancillary revenues purely as fees/charges to creating value adding services and products for at least some categories of non-core product).

**Figure 1 Worldwide airline financial results per departing (US\$) passenger for 2014**



IATA (2014b)

As a group, the 2007 top 10 carriers generated total ancillary revenue of nearly \$2.1 billion. Seven years later, some of the original airlines remain on the top 10 list. But the total revenue volume for the top 10 has undergone drastic change by surging to \$20.4 billion by 2013 as shown in Table 2. The increase in ancillary revenues is primarily triggered as carriers expand their revenue footprint by: unbundling the fare and charging for additional products that were once encapsulated within the fare; together with commission based incomes; by turning frequent flyer programmes into innovative profit centres and through diverse advertising gateways that generate payoffs as illustrated in the proceeding section.



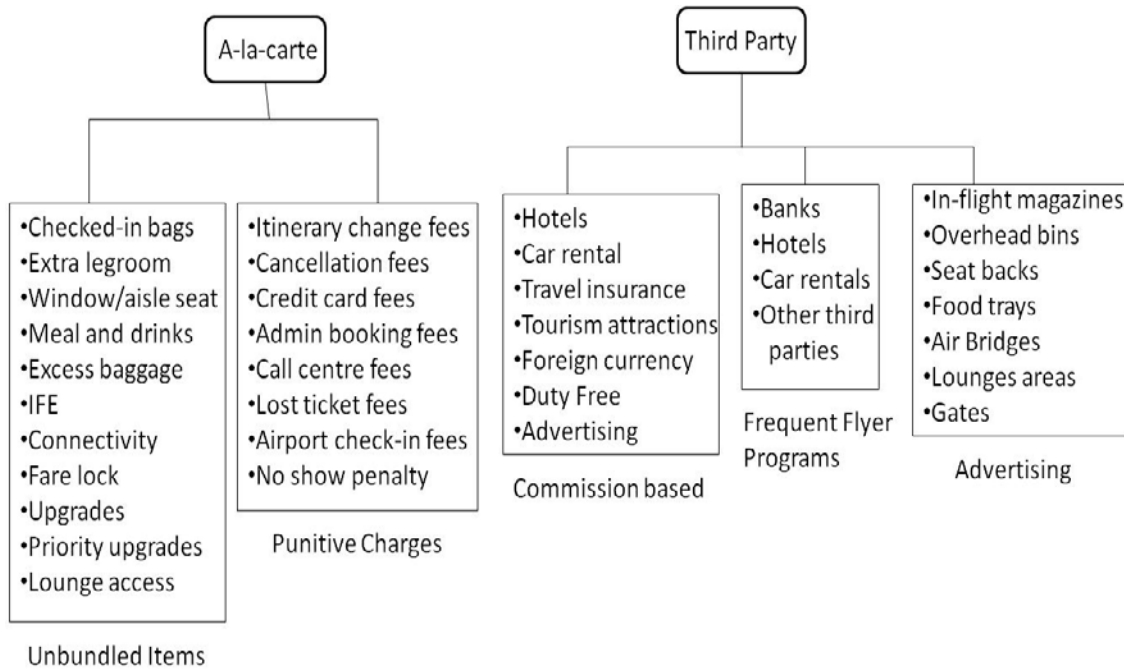
**Table 2 Top 10 airlines that generate ancillary revenues in 2013 and 2007**

Annual Results 2013 (US\$bn)		Ancillary Source 2013	Annual Results 2007	
United	\$5.7	Various	United	\$0.6
Delta	\$2.5	Various	Ryanair	\$0.5
American	\$2.1	Various	easyJet	\$0.3
Air France/KLM	\$1.7	Various	Alaska Air Group	\$0.2
Ryanair	\$1.7	Various	Aer Lingus	\$0.1
Southwest	\$1.6	Various	Air Berlin	\$0.1
easyJet	\$1.4	Various	Korean Air	\$0.1
Lufthansa Group	\$1.3	Various	WestJet	\$0.1
Qantas Airways	\$1.3	80% FFP	Austrian	\$0.1
US Airways	\$1.1	Various	Alitalia	\$0.1
<b>Total</b>	<b>\$20.4</b>		<b>Total</b>	<b>\$2.1</b>

Source: Ideaworks, 2013

Ancillary Revenues can be grouped into two distinct categories. Firstly, the a-la-carte entity which comprises unbundled items for sale and punitive charges, which are penalties that are imposed for indecision and poor planning by passengers. The second category is third party ancillary streams, comprising commission based incentives, revenues from frequent flyer programs and advertising, which are shown in Figure 2.

**Figure 2. The attributes of a-la-carte and third party ancillary revenue streams**



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traditionally have been included in the price of the airline ticket. The low-cost carriers initiated this process by disassembling the fare into various individual components, becoming known as the ‘unbundled flight products’, which included separate charges for items such as: pre-assigned seats; checked baggage and excess baggage; priority boarding; in-flight entertainment; in-flight Wi-Fi internet access and food and beverage. Baggage is the largest generator of such revenues with US carriers garnering around \$3.5 billion in 2014. A recent study by Scotti et al (2016) looked into the possible impact of unbundled baggage charges by US airlines on customer satisfaction levels and found that there was no evidence of a negative relationship given that the introduction of baggage charges actually led to a reduction in the number of aircraft delays, something which is important to time-sensitive travelers flying domestically in the US.. Cargo, which has been transported along with passengers since the inception of the industry, produced a lower \$3 billion for the US carriers (US DOT, 2015). British Airways, for example, earned £45 million from baggage fees in 2013 along with an additional £40 million from assigned seating (British Airways, 2014). Corporate travel departments, travel agents, online travel agents and other travel retailers that are powered by GDSs are now able to offer and book the same ancillary services that were offered only through airline websites, kiosks or call centres. Booking these a-la-carte services via a GDS intermediary

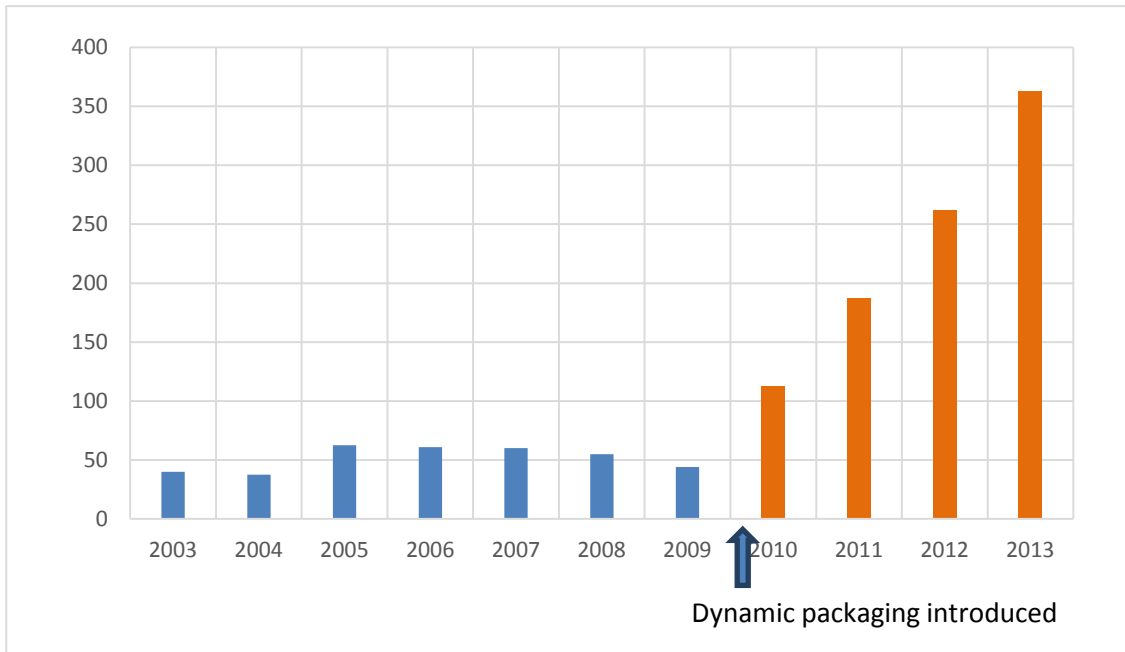
remains an important cornerstone as the 2014 IATA global passenger survey found that 41% of passengers rely on indirect channels to purchase tickets (IATA, 2014). An IATA commissioned report by Harteveldt (2012) stated that around 16% of LCC ticket sales moves through GDS interfaces (IATA, 2013). GDSs remain an entrenched appliance in distributing airline inventories to customers worldwide and have mutated in order to incorporate ancillary revenue streams.

Punitive charges are another key revenue driver as consumers are financially impacted if they choose to alter their travel itineraries and for purchasing tickets via credit cards. Reservation changes made by passengers travelling on US carriers in 2014 totalled \$2.9 billion (US DOT, 2015). The fastest growing fee is the credit card burden – most carriers pass on this cost to their passengers (Adeniran, 2012). Research through the airline websites reveals that KLM charges €7.50 for credit card transactions on European flights and €15 for international bookings, while Monarch Airlines issues a 2.5% levy or £5.00 per booking (whichever is greater) with EasyJet charging 2% of the reservation price. Appendix 1 gives a detailed comparison of a-la-carte fees for a number of airlines in 2015 and there are significant variances occurring. Analysis by Ideaworks (2012) argues that unbundling has reached maturity as there is little opportunity remaining for ‘big revenue’ items to be extrapolated. The next paradigm upsurge is to offer purchasable ancillary services that bring more value adding comfort and convenience amenities to economy class travel.

## **2.2 Commission based ancillaries**

The internet has shifted power from the supplier to the consumer. It allows a customer to combine multiple travel components such as hotel accommodation and car hire from an airline website, as they are obvious products that naturally complement the sale of an airline seat. O'Connell and Warnock-Smith (2013) stated that it integrates tourism related data onto one transparent platform and in effect, consumers become their own travel agents by building a tailor-made package that suits their specific requirements. This process known as dynamic packaging is handled seamlessly in one transaction and requires only one payment from the consumer. It is dynamic because pricing, constraints and ultimately choice are determined online based on a real-time inventory. Research by Google analysis reveals that the typical traveler uses 22 websites to research a trip in multiple shopping sessions before booking (Harteveldt, 2012). Airlines have been leaking huge volumes of revenues to suppliers for decades and dynamic packaging directly through airline websites aims to significantly curtail this trend. The global car rental business is worth \$42 billion each year and is an increasingly important source of ancillary revenue for airlines (Alten, 2009). Figure 3, for example, shows the revenue impact from dynamic packaging on British Airways Holidays since it introduced the concept, which triggered an exponential revenue growth in 4 years as it vastly reduced leakages to third party providers (Guestlogix, 2015). The managing director of BA Holidays stated that the number of hotels and resorts in the range of 3, 4 and 5 star amenities had increased to more than 6,000 by 2010 (Bentley, 2010). A passenger survey initiated by GuestLogix found that more than half would take advantage of destination-related offers onboard a flight, particularly services that could be utilised immediately such as entertainment and attraction tickets, ground transportation and tours (Ascend, 2012).

**Figure 3. Revenues from British Airways Holidays (£Millions)**



Source: Guestlogix (2015)

### **2.3 Frequent Flyer Programme (FFP) activities**

The primary objective of FFP is to retain travelers, thereby mitigating the risk of losing business and any erosion of existing customer bases. This category consists of sales of points and mileage to programme partners such as co-branded credit cards, hotel chains, car rental companies, online retailers and also the sale of points or mileages directly to the programme members. There are bonus points given for silver, gold and platinum members, which are incentives for high valued travelers. According to a survey of business passengers flying Delta Air Lines, 64% are unmanaged travelers who are not controlled by corporate travel policies, which in-turn creates a big opportunity for the US incumbent to develop a strong personalised relationship (Atmosphere Research Group, 2014). An airline's FFP membership is fast becoming a core competency of the business evolution as around 50% of United Airlines \$37 billion revenues for 2012 were generated through the members of its MileagePlus program (Ideaworks, 2013). These programs have become a huge source of revenue for carriers. United Airlines, for example, disclosed mileage sales of around \$2.8 billion in 2012, which represented 7.6% of the carrier's annual revenue (United Airlines, 2012). The amount spent on United's co-branded credit card increased by 35% and active card members increased 16% over the last 3 years.

These co-branded credit cards are now offered in 15 countries (Garrido, 2014). In 2010, approximately 62% of American Airlines AAdvantage miles were sold to third parties (mostly banks), while only a third were accrued by members flying on the carrier (AMR, 2010). The majority of the 114 billion miles sold by American during 2010 were purchased by Citibank, which is the primary issuer of credit cards linked to the carriers FFP. Many of these miles go unclaimed, which advantages the operating carrier as today's airlines have garnered very high load factors thereby leaving little incentives to redeem miles for tickets that would essentially displace revenue passengers. According to a report by International Travel News (2013), the Economist estimated that there were 14 trillion unused miles/points accumulated worldwide in 2004. Skift (2013) announced that the Economist and WebFlyer revised the number of unredeemed miles to 23.8 trillion by 2012. Retana (2013) echoed this theme by reporting that 25% of United/Continental allotted mileage was expected to expire or go unredeemed by the end of December 2012. There is now a paradigm shift from a mileage award mechanism towards a revenue based accrual system – Delta, United and Qantas have quickly transformed by awarding miles based on the fare paid rather than the distance travelled. The FFP member status is also correlated to the number of miles awarded in order to incentivise loyalty and repeat patronage. United Airlines, for example, awards 7 miles for each dollar spent for premier silver members while premier platinum receives 11 miles for each dollar expended (United Airlines, 2015).

## **2.4 Advertising**

This category includes sales of advertising by the airline in-flight magazines, overhead luggage bins, seat backs, air-bridges, exclusive lounges, gate areas and also placement of samples and consumer products associated with a commission fee. Ryanair (2015) states that its overhead bin, tray table and boarding card advertising media offers an effective communication platform as the advertisements become lodged into the long term memory of its passengers. The inflight magazine is populated with upmarket luxury advertisements together with a wide range of articles from sports to entrepreneurial stories to capture and attract passengers' attention. Over 150 airlines worldwide now offer in-flight magazines, thus making it a potential revenue generator. In 2009, the Wall Street Journal reported that more than 80% of passengers read the magazines that airlines place in front of them and

readers average around 30 minutes a flight with the magazines (Michaels, 2009). According to Lufthansa, its magazine reaches the top 20% of households in terms of income in Germany and has more readers than Time Magazine Europe, Newsweek Europe, and The Economist (Huson, 2015). In 2008 Lufthansa charged €19,500 for a 30 second in-flight TV spot, whereas with British Airways it cost advertising companies as much as €43,443 for the same 30 second slot (IMM International 2008).

Today, airlines have exclusive control of the passenger from check-in to departure, and it will become increasingly important for airlines to continue to explore new retailing opportunities at the airport. Airlines have been limited in their ability to influence travelers across the entire customer journey. Bisignani (2014) revealed that siloed data, coupled with decades of cost-saving initiatives (instead of value creation), has left travelers around the world feeling disconnected and underappreciated. This is reiterated in a recent study conducted by Timetrade (2013) and Businessinsider (2015) who found that around 60% of retailing executives report a personalised customer experience as the No. 1 shopping factor missing today. Retailing strategies of the future should consider customisable content through flexible channels for a range of purposes: product and service status; news; advertising, branding and infotainment. Advances such as dynamic online advertisements on items such as car rental and hotels based on previous browsing sessions and predictive product suggestions based on purchase history will condition consumers to think that all online interactions will be tailored to suit their individual preferences.

Customer data profiling for personalisation could be the next paradigm leap in passenger analytics providing a 360-degree view of customer insights that combines structured and unstructured data from internal and external sources and triggers actionable insights across the customer journey. This “master data profile” could be the nuclei of successful retailing strategies by providing the ability to personalise offers and target customers. Industry collaboration by the authors deduces that around a terabyte of customer data is circulating at any given time within a large carrier’s system, airlines that use this can create a seamless customer-data environment. This can become a reality as SITA (2015) researched that 97% of air travelers now carry their own device when travelling, with 81% carrying a smartphone, 43% a tablet, 43% a laptop and 17% carrying all three. This high penetration creates huge ancillary opportunities in terms of personalisation of communications with passengers throughout the start-to-end travel process.

### **3 Methodological approach and descriptive results**

There are two levels of research question used in this study. The aggregate level question relates to the overall Willingness to Pay of airline passengers as a homogenous group, for a range of unbundled and commission based ancillary products and services. There is also a disaggregate level question which relates to whether type of carrier chosen, flight length and journey purpose of passengers led to any variation in Willingness to Pay for the same set of ancillary products. An appropriate empirical strategy for these research questions was to allow a sample of travelers to reveal their ancillary WTP preferences by asking them to state their purchases and purchase intentions for their previous flight.

For the data analysis phase, descriptive statistics were used for the aggregate level question while the disaggregate level questions were converted into the following testable hypotheses:

#### Hypothesis 1

Journey purpose has an impact on WTP for ancillary products and services

#### Hypothesis 2

Type of carrier has an impact on WTP for ancillary products and services

#### Hypothesis 3

Length of flight has an impact on WTP for ancillary products and services

Two of the three disaggregate level variables are categorical and thus non-parametric hypothesis testing was used. For length of flight the sample was broken down into flights of more than 4 hours and flight of less than four hours so a paired sample hypothesis test was used.

An online survey was arranged in November 2014. The questionnaire was uploaded to the “Questionpro” website and over 400 survey invitations were sent using a convenience sampling approach through social media to Cranfield University Air Transport MSc graduate alumni who work in aviation throughout the world. These



aviation professionals were specifically targeted as they are knowledgeable about unbundled and commission based products thereby reducing the chances of obtaining confused or unusable responses. It also ensured the credibility and relevance of the responses as it harnessed the respondents' collective wisdom and experience. The downside of this approach was that it was not possible to guarantee statistical significance at the hypothesis testing stage for the whole population of air passengers. A total of 220 responses were collected of which 170 were fully completed from 37 countries giving a response rate of 43%. A fair spread of respondent attributes was also obtained with 66% of respondents being male and 34% female while there was a normal distribution of ages with 60% of respondents in the mid 25-44 years category and the remainder spread evenly in the younger and older age categories. A combination of attribute and trip related questions were asked, which sought to combine a representative sample of passengers (by carrier type, journey purpose and length of haul) with their revealed preferences in relation to flight attributes and ancillary products/services. Preference questions were partly based on the on-line survey questions carried out in O'Connell and Warnock-Smith (2013).

### **3.1 Analysis of trip-related factors**

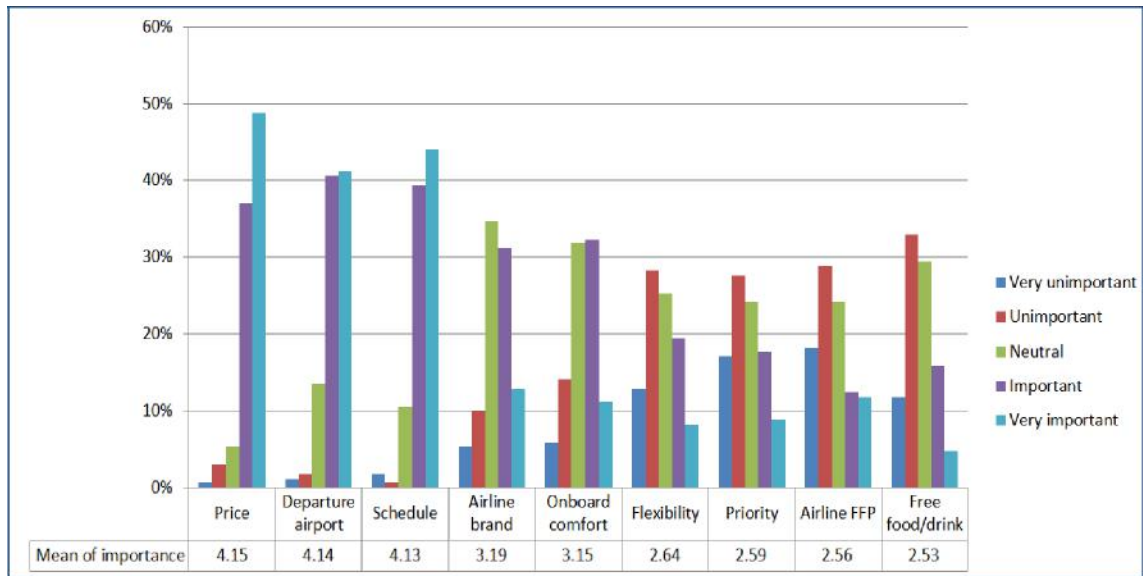
Flight purpose for the majority of respondents was holiday, while business trips accounted for around one-third of trips, with one-fifth of the journey's being to visit friends and relatives. A small proportion of this sample indicated other purposes such as a study trip. Most respondents purchased their most recent flight directly from an airline's website (43%). Interestingly, almost one fifth of respondents stated that somebody else booked their ticket for them. Almost two thirds of respondents had flown their last flight with full service airline and nearly one third with a low cost airline. All three of these trip-factors act as attribute variables and help to explain exposure and attitude to various categories of ancillary revenue.

### **3.2 Analysis of priority and preferences**

Figure 4 and Table 3 show the importance of various flight attributes to respondents. As shown, price, schedule and departure airport were considered the most important factors, whilst on-board comfort, priority and free food and drink were the least important to them.

This would suggest that getting the basic package right in terms of price, departure airport and schedule provides a highly important platform for airlines to access passenger preferences in relation to secondary products and services. Equally, regardless of how enticing airline secondary products and services are, if the basic product is lacking there would be precious little opportunity to generate secondary revenues.

**Figure 4 Importance of flight attributes to the respondents**



Source: compiled by author

**Table 3 Standard deviation of the flight attributes**

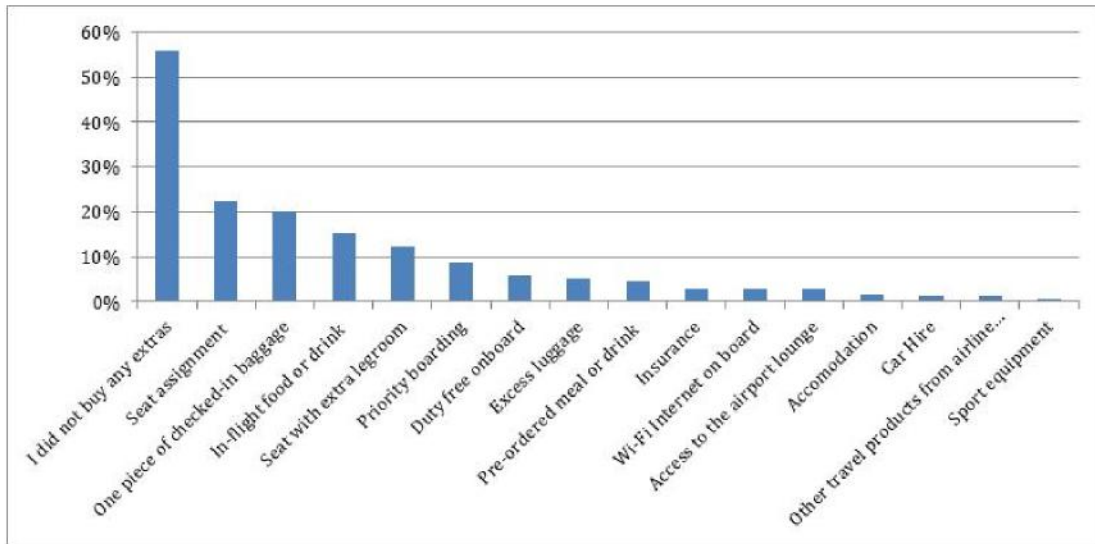
		Price	Departure airport	Schedule	Airline brand	Onboard comfort	Flexibility	Priority	Airline FFP	Free food/drink
N	Valid	170	170	170	170	170	170	170	170	170
	Missing	0	0	0	0	0	0	0	0	0
Std. Deviation of importance		1.24	.996	1.13	1.28	1.25	1.32	1.33	1.36	1.19
Very important: 5, Important:4, Neutral: 3, Unimportant:2 and Very unimportant:1										

Source: Compiled by authors

### 3.3 Analysis of recent purchase behaviour

Respondents were asked what ancillary services they purchased on their most recent flight. The questions were a combination of an airline’s a-la-carte and travel related products from third-party service providers such as accommodation, car hire and travel insurance through the airline website/call centre.

**Figure 5 Ancillaries purchased by respondents on their most recent flight**



Source: compiled by author

Figure 5 shows that more than half of the respondents stated they did not purchase any ancillaries on their recent flight. Amongst passengers who purchased extras, seat assignment, checked-in baggage and inflight food/drink were the most popular categories, all of which can be considered unbundled products.

### 3.4 Analysis of willingness to use and willingness to pay

Respondents were asked to express their willingness to pay for a-la-carte products and services offered by the airline over a short-haul and a long-haul flight. The percentage of respondents who were willing to pay for each a-la-carte item and the maximum, minimum and the average amount that they were willing to pay for these products are listed in Table 4.

**Table 4 Willingness to use and pay for a-la-carte products by length of haul**

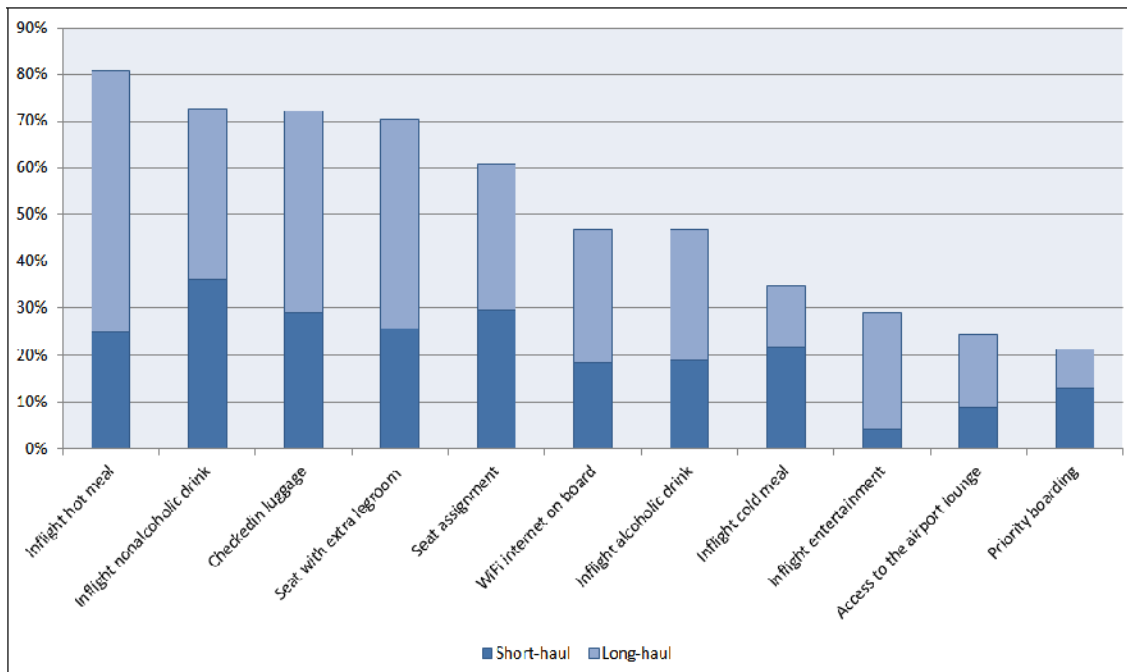
	Short-haul				Long-haul			
	%Frequency	Min	Max	Mean	%Frequency	Min	Max	Mean
Inflight hot meal	24.7%	£3.00	£20.00	£6.14	56.5%	£3.00	£20.00	£8.43
Inflight non-alcoholic drink	35.3%	£1.50	£3.99	£2.07	37.1%	£1.50	£3.99	£2.11
Checked-in luggage	28.8%	£1.00	£15.00	£4.16	42.9%	£2.00	£30.00	£11.59
Seat with extra legroom	24.7%	£3.00	£30.00	£10.78	45.3%	£3.00	£40.00	£14.71
Seat assignment	29.4%	£2.00	£10.00	£4.34	31.2%	£2.00	£11.99	£6.33
Wi-Fi internet on board	18.8%	£15.00	£29.99	£21.49	28.8%	£10.00	£59.99	£24.59

Inflight alcoholic drink	18.8%	£5.00	£34.99	£16.55	27.6%	£5.00	£34.99	£17.63
Inflight cold meal	21.8%	£2.50	£10.00	£3.52	13.5%	£2.50	£4.99	£3.65
Inflight entertainment	4.1%	£2.00	£5.00	£2.99	25.3%	£2.00	£9.99	£6.30
Access to the airport lounge	8.8%	£2.00	£9.99	£6.01	15.3%	£2.00	£9.99	£6.49
Priority boarding	12.4%	£1.00	£5.99	£4.65	8.2%	£1.00	£10.00	£4.86

Source: Compiled by authors

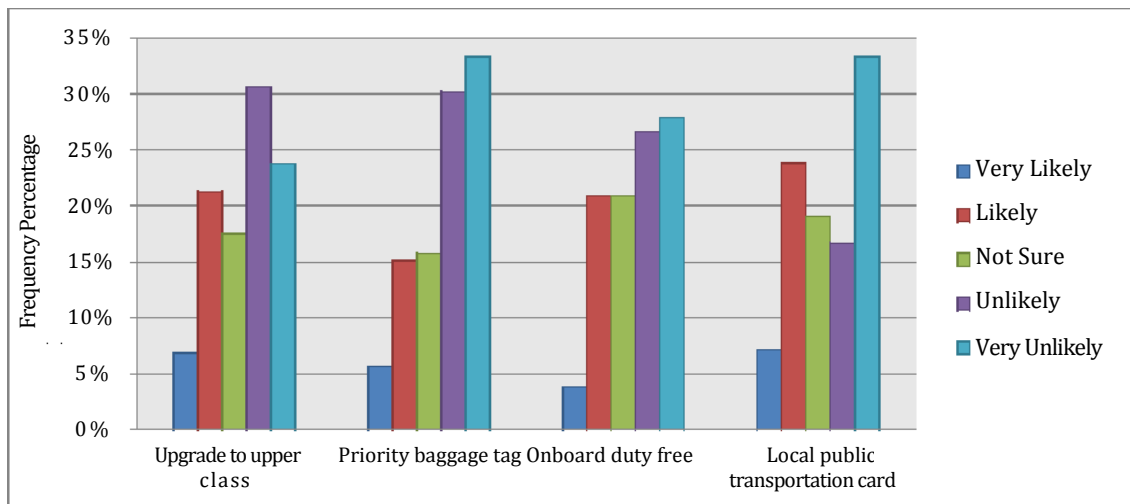
Table 4 and Figure 6 (below) show that the majority of respondents on a long-haul flight would buy an in-flight hot meal for an average of £8.43 and on short-haul flights would buy a non-alcoholic drink for average £2.07. At the other end of the spectrum very few respondents would be willing to purchase in-flight entertainment on a short-haul flight (4.1%) and priority boarding on a long-haul flight (8.2%). Clearly there are different values placed on specific ancillary products and services for long-haul and short-haul passengers, which should be borne in mind by airline commercial departments before offering secondary products and setting price levels.

**Figure 6 Distribution of willingness to use a-la-carte products by length of flight**



Source: Compiled by author

**Figure 7 Probability of buying other ancillary products**

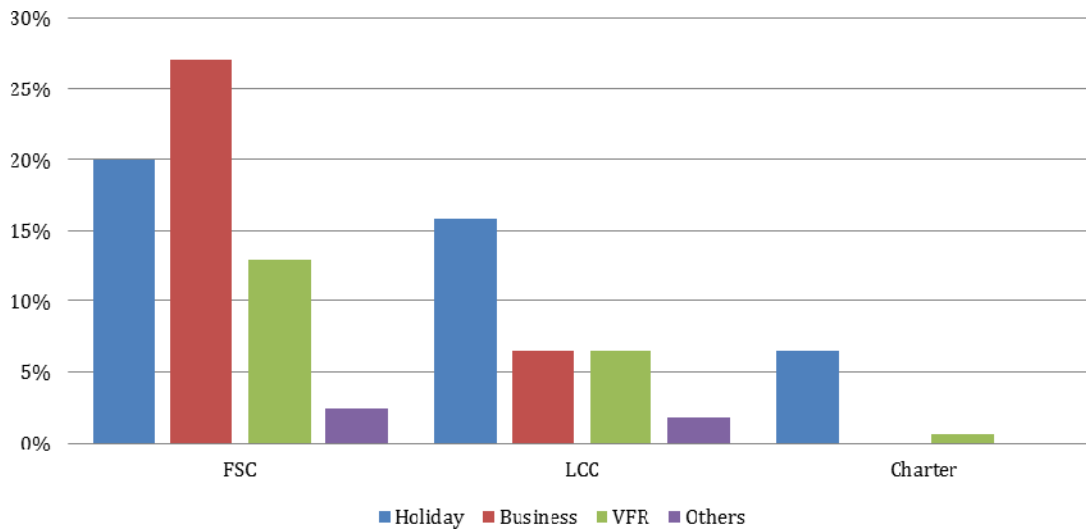


Respondents were also questioned about whether they would consider buying other ancillary products such as an upgrade to upper class, priority baggage tags, on-board duty free and local transportation tickets. The majority stated that they are very unlikely or unlikely to purchase these items (see Figure 7), suggesting that scope for ancillary revenues is large but within a small range of what are perceived to be value adding products and services.

### 3.5 Analysis of responses based on type of carrier

Figure 8 shows that the main journey purpose with Full-service carriers (FSC) was business whereas taking a holiday was the main purpose of LCC and charter airline passengers.

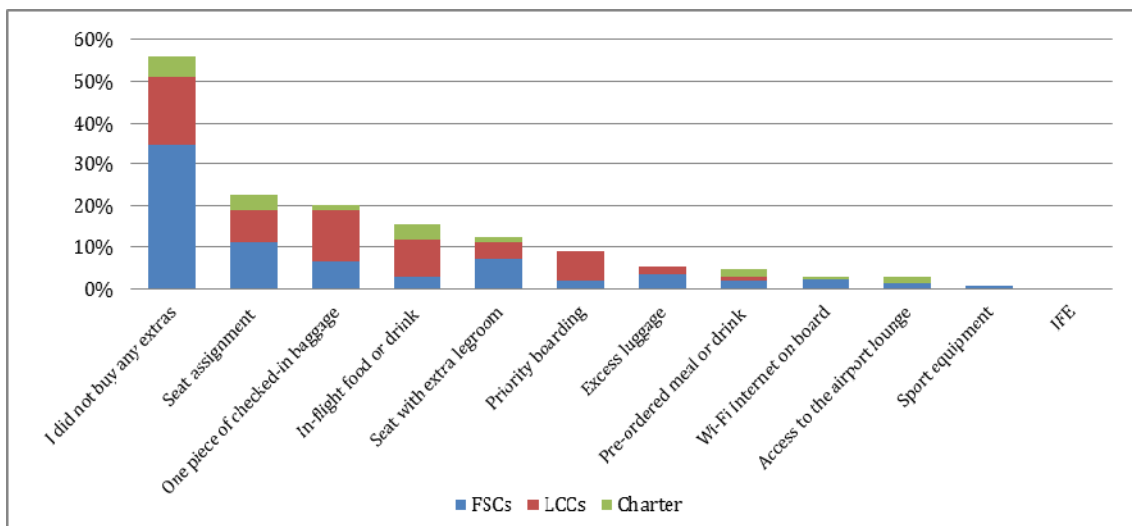
**Figure 8 Distribution of respondents based on carrier type and main purpose of their recent trip**



Source: Compiled by authors

Figure 9 shows that majority of respondents who flew with an FSC did not buy any ancillary products on their last flight. The most popular products for FSC travelers were seat assignment and extra legroom seat. Conversely, a higher proportion of LCC passengers purchased some form of ancillary product with most purchasing checked-in baggage, while the most popular products for charter passengers was jointly seat assignment and in-flight food and drink. None of the respondents paid for inflight entertainment on their most recent flight.

**Figure 9 Respondents' purchase of ancillaries on their most recent flight broken down by type of carrier**

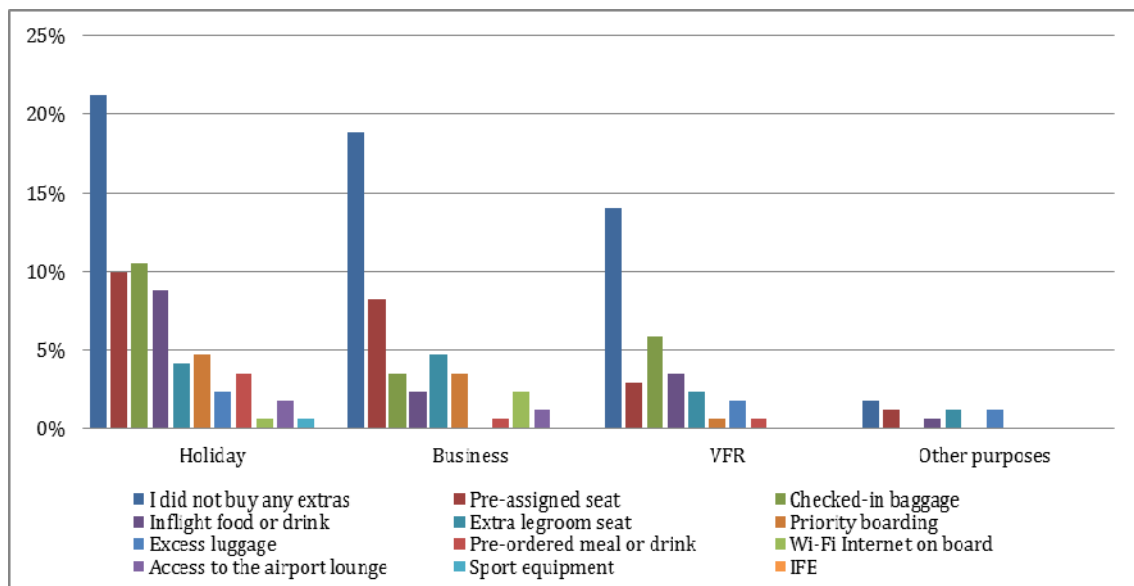


Source: Compiled by authors

### 3.6 Analysis of responses based on journey purpose of most recent flight

Figure 10 shows that the top items of ancillary products purchased by holidaymakers in this study were checked-in baggage, pre-assigned seats and in-flight food and drink. The top purchases of business travelers were seat assignment and seats with extra legroom. The VFR sub-group mostly purchased checked-in baggage and in-flight food and drink, which was largely in line with holidaymakers. The top purchases of respondents in other journey purpose categories were excess luggage, seat assignment and seats with extra legroom. It is also worthy of note that for all classes of journey purpose the largest percentage of respondents did not make any ancillary purchases.

**Figure 10 Respondents’ purchase of ancillary products and services based on main purpose of flight**



Source: Compiled by authors

## 4. Hypothesis test results

### 4.1 Hypothesis 1

Table 5 shows that there is a significant correlation between journey purpose and WTP for one piece of checked-in baggage and excess baggage (p-value  $\leq 0.05$ ) therefore the  $H_0$  hypothesis for these two items is rejected and  $H_1$  is accepted. As a result, journey purpose has an impact on WTP for one piece of checked-in baggage and excess baggage. When compared with the descriptive results (Figure 10), it follows that holidaymakers place a greater value on baggage and extra-baggage, which many airlines charge for as an unbundled product. It was also the item that VFR passengers were most likely to pay for in comparison to other items adding further weight to the notion that journey purpose has a direct effect on WTP for certain ancillary items over others.

The p-value for the rest of ancillary services and products listed in the above table is  $> 0.05$  consequently  $H_0$  hypotheses for these products are not rejected. It can be concluded that there is no significant association between journey purpose and WTP for all other items.

**Table 5 Chi-square test for purpose of flight and WTP for ancillary products and services**

	Value	df	P-value
<b>Pearson Chi-Square for Checked-in baggage</b>	<b>7.955</b>	<b>3</b>	<b>.047</b>
<b>Likelihood Ratio for Excess Baggage</b>	<b>10.843</b>	<b>3</b>	<b>.013</b>
Likelihood Ratio for Priority boarding	3.853*	3	.278
Pearson Chi-Square for Seat assignment	1.954	3	.582
Likelihood Ratio for Extra Legroom	1.954*	3	.582
Likelihood Ratio for Sport equipment	1.726*	3	.631
Likelihood Ratio for Pre-ordered meal	4.123*	3	.248
Pearson Chi-Square for In-flight food/drink	4.870	3	.182
Likelihood Ratio for Wi-Fi	5.609*	3	.132
Likelihood Ratio for Access to the Lounge	2.845*	3	.416
* Since more than 20% of cells have expected count less than 5, therefore Chi-square test assumption is violated and Likelihood Ratio test result is used instead.			

Source: Compiled by authors



## 4.2 Hypothesis 2

Table 6 illustrates that there is also a significant correlation between type of carrier and WTP for one piece of checked-in baggage, priority boarding, pre-assigned seats, pre-ordered meals, in-flight food/drink and access to airport lounges ( $p\text{-value} \leq 0.05$ ) therefore  $H1$  hypotheses for these items are accepted. The correlation and statistical significance for food and drink purchases is especially high when the sample is split by carrier type. As there are fewer LCCs that provide complimentary food and beverage, seat assignment and checked-in baggage, it has clearly had a marked effect on the number of travelers valuing the purchase of such services in comparison to travelers flying with full-service carriers.

Since the  $p\text{-value}$  for excess baggage, extra legroom seats, sport equipment and Wi-Fi internet on-board is  $> 0.05$  consequently  $H0$  hypotheses for these items are not rejected. It can be concluded that there is no significant association between type of carrier and WTP for these ancillary items.

**Table 6 Chi-square test for type of carrier and WTP for ancillary products and services**

	Value	df	P-value
<b>Pearson Chi-Square for Checked-in baggage</b>	<b>19.723</b>	<b>2</b>	<b>.000</b>
Likelihood Ratio for Excess baggage	1.356*	2	.508
<b>Likelihood Ratio for Priority boarding</b>	<b>17.984*</b>	<b>2</b>	<b>.000</b>
<b>Pearson Chi-Square for Seat Assignment</b>	<b>6.692</b>	<b>2</b>	<b>.035</b>
Pearson Chi-Square for Extra Legroom	.370	2	.831
Likelihood Ratio for Sport equipment	.948*	2	.622
<b>Likelihood Ratio for Pre-ordered meal</b>	<b>6.765*</b>	<b>2</b>	<b>.034</b>
<b>Pearson Chi-Square for In-flight food/drink</b>	<b>27.683</b>	<b>2</b>	<b>.000</b>
Likelihood Ratio for Wi-Fi	4.167*	2	.125
<b>Likelihood Ratio for Access to the Lounge</b>	<b>11.776*</b>	<b>2</b>	<b>.003</b>
* Since more than 20% of cells have expected count less than 5, therefore Chi-square test assumption is violated and Likelihood Ratio test result is used instead.			

Source: Compiled by authors

### 4.3 Hypothesis 3

Since all respondents were asked to express their opinion about WTP for extras over a flight of less than four hours and a flight more than four hours, instead of using a Chi-square test, a paired samples test is used instead to examine the impact of flight length on WTP for ancillary products and services.

**Table 7 Paired sample test result for Length of flight and WTP for ancillary services**

Paired Samples Test									
		Paired Differences					t	df	P-value
					95% Confidence Interval of the				
		Mean	Std. Deviatio	Std. Error Mean	Lower	Upper			
Pair 1	Short-haul Cold meal & Long-haul Cold meal	.08235	.41315	.03169	.01980	.14491	2.599	169	.010
Pair 2	Short-haul Hot meal & Long-haul Hot meal	-.31765	.60003	.04602	-.40850	-.22680	-6.902	169	.000
Pair 3	Short-haul Non-alcoholic drink & Long-haul Non-alcoholic drink	-.01765	.45474	.03488	-.08650	.05120	-.506	169	.614
Pair 4	Short-haul Alcoholic drink & Long-haul	-.08824	.37430	.02871	-.14491	-.03156	-3.074	169	.002
Pair 5	Short-haul Extra legroom & Long-haul Extra legroom	-.20588	.54281	.04163	-.28807	-.12370	-4.945	169	.000
Pair 6	Short-haul Pre-assigned seat & Long-haul Pre-assigned seat	-.01765	.42792	.03282	-.08244	.04714	-.538	169	.591
Pair 7	Short-haul Checked baggage & Long-haul	-.14118	.47799	.03666	-.21355	-.06881	-3.851	169	.000
Pair 8	Short-haul Priority Boarding & Long-haul	.04118	.27426	.02103	-.00035	.08270	1.958	169	.052
Pair 9	Short-haul IFE & Long-haul IFE	-.21176	.42396	.03252	-.27596	-.14757	-6.513	169	.000
Pair 10	Short-haul Wi-Fi & Long-haul Wi-Fi	-.10000	.37131	.02848	-.15622	-.04378	-3.511	169	.001
Pair 11	Short-haul Lounge access & Long-haul Lounge access	.06471	.26965	.02068	-.10553	-.02388	-3.129	169	.002

Source: Compiled by authors

Table 7 displays that length of flight impacts on passengers' WTP for cold and hot meals, alcoholic drinks, extra legroom seats, checked-in baggage, IFE, Wi-Fi and access

to the airport lounges ( $p\text{-value} \leq 0.05$ ). Therefore,  $H1$  hypotheses for these items are accepted.

However, the P-value for non-alcoholic drinks, pre-assigned seats and priority boarding is greater than 0.05, therefore the  $H0$  hypotheses for these items is valid and it can be concluded that flight length does not have any impact on WTP for these services. Length of haul has had a statistical impact on WTP for the largest range of ancillary products and services when contrasted against the impact of carrier type and journey purpose, indicating that passenger perceptions of length of haul create additional opportunities for airlines to sell value adding ancillary products and services

## 5. Conclusions

By conducting an on-line survey in November 2014 among frequent travelers and air transport professionals with a positive response rate, and an appropriate sample size/distribution, this study has shown that airlines could benefit greatly from understanding ancillary preferences and WTPs based on type of carrier, length of journey and journey purpose.

Willingness to Pay (and to Use) for various ancillary services were shown to differ between Low-cost carrier and full-service carrier passengers, short-haul and long-haul flights and overall journey purpose (business, leisure, VFR). Significant statistical differences were found with regards to the purchase of food and drink, extra baggage, priority boarding and seat assignment with LCC holiday-makers on a short-flight much more willing to purchase food and drink than anything else and long-haul, business travelers flying with a full-service carrier much more likely to value the benefit of extra legroom, for instance. Airlines could use this information from a management perspective to undertake more accurate targeted marketing activity and to determine which categories of ancillary product to focus on.

It was also found that commission based ancillary revenues receive a lower willingness to use and pay than some unbundled products/services and a narrow range of unbundled products appear to be commonly purchased, namely checked baggage, food and drink and seat assignment across most sub-categories of trip related factor. In other words, there is an overall tendency for travelers to place greater value on 'necessity' ancillary products/services rather than those perceived to be optional 'nice-to-have' extras.

Airlines and researchers are encouraged to investigate disaggregated market data further in relation to ancillary revenues as an important feed into commercial strategies. Against a backdrop of poor airline margins, intelligence based development of ancillaries revenue streams is a must. Future research should also incorporate FFP and advertising categories of ancillary revenue as this research has shown that they represent a significant proportion of total non-core revenues for some airlines. Additional revealed preference data from infrequent travelers and non-experts could also produce a fresh perspective on ancillary preferences.

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## Appendix 1: Comparing Airline Charges 2015

Airline	Check In	Priority Boarding	Advanced Seat Selection	Inclusive Luggage Allowance	Baggage Fees/ Excess Fees	Sports/ Music Equipment	Meals Refreshments	Other Charges	Credit Card Charges
Aer Lingus	All check in types included.	N/A	SH: £5 - £14 for standard seats. LH: £18 - £40.	LH: 1 x 23kg bag SH: N/A.	SH: 1st 15kg bag 20 – 30 EUR (online) and 60 EUR (airport). LH: 2nd and subsequent £65. Overweight bags: £65.	£25 (online) or £32 (call centre / airport) per item per flight.	LH: meal and soft drink included. SH: meals from £6.50 (online).	Date/Itinerary/Route change: £35 (online), £40 (phone/airport) or LH £120. Plus fare difference. APD refund fee: £13.50 Name change: £80 per passenger.	No charge.
American Airlines	All check in types included.	Group 1 Boarding: 15-40 USD.	4-169 USD (includes extra legroom/ preferred seats).	1 x 23 kg bag	2nd 23kg bag: £65. Overweight bags: 100 USD. Oversized bags: 100 USD.	Equipment can be carried as part of the inclusive allowance. Excess charges apply, some items have individual charges e.g. bikes: 15	Meal and/or refreshments included appropriate for length of journey.	PayPal: £4.50 per ticket. Round the world itineraries: £25 per passenger. Same day flight change: 75 USD.	£4.50 per ticket.
British Airways	Included in ticket price.	N/A	Free of charge 24 hours before departure. Extra leg room seats: SH from £5 and LH from £50.	Most fares include at least 1 x 23kg bag (some fares are hand baggage only)	Extra 23kg bag. Flight to/from LGW: £36 (online), £40 (airport). All other destinations: £40 (online), £65 (airport).	Equipment can be carried as part of the inclusive allowance. Standard excess charges apply.	Meal and/or refreshments included appropriate for length of journey.	PayPal: £5 per booking APD refund fee: £15-30. Name change: free of charge within 24 hours of booking. Spelling mistakes can be corrected without charge.	£5 per booking.
Delta	Included in ticket price.	10 USD.	Included in ticket price, extra leg room seats: 9-59 USD.	At least 1 x 23kg bag included in most fares transatlantic fare.	2nd 23kg bag: 100 USD.	Equipment can be carried as part of the inclusive allowance. Excess charges apply.	Meal and/or refreshments included appropriate for length of journey	On board Wi-Fi: from 4.99 USD. In flight alcoholic drinks vouchers: 5 USD	No charge.
EasyJet	Online check in only. Airport	Speedy Boarding is	Advanced seat selection and	N/A	1st 20kg bag: £11-21 (online), £30	Small equipment: £30 (online), £40	Available for purchase	Cancellation fee: £30. Name/ flight	2% per booking.

	check in is not available.	included for passengers who have purchased extra leg room or up front seats	extra leg room seats: £0.99 - £15.99.		(airport), £45 (boarding gate). Excess charges: £3 per kg (online), £10 per kg (airport).	(airport). Large equipment: £35 (online), £45 (airport).	on board.	change: £35 (online), £40 (airport). Rescue fee: £65. APD refund fee: No charge.	
Emirates	Included in ticket price.	N/A	Standard seating can be requested free of charge.	30 kg per passenger.	Extra 5kg: £113. Extra 10 kg: £225.	Equipment can be carried as part of the inclusive allowance. Standard excess charges apply.	Meal and/or refreshments included appropriate for length of journey.	On board Wi-Fi: 2.75 USD per phone, 7.50 USD per tablet. Free on A380's.	No charge.
Flybe	Included in ticket price.	N/A	Standard seats: £6.50 (online), £8 (phone/airport). Extra leg room: £15 (online), £16 (phone/airport).	N/A	1st bag at 15 kg: £16.50 (online), £18 (phone). 20 kg: £17 (online), £20 (phone), £40 (airport). 23kg: £22 (online)	Equipment: £30 (phone/ airport) e.g. bikes or surf boards.	Available for purchase on board.	Ticket/route change: £35 (online). Name change: £40 (phone/airport) Call centre booking fee: £8. APD refund fee: £25.	3% per booking.
Jet2.com	Airport check in is £15 for passenger who check in luggage.	N/A	Seat selection: from £4 (online). Extra leg room: from £10 (online). Prices vary on route.	N/A	22kg: from £10 (online) price varies on route. Passengers who check bags must also pay for airport check in: £15.	Equipment e.g. golf clubs or skis: from £30 (online).	Available for purchase on board. Meals can be pre ordered from £6.50 (online).	Boarding pass reissue fee: £17.50 (for passengers who check in online but don't bring a printout) PayPal: 2% per booking. APD Refund fee: £25 per booking. Flight/name change: £35.	2.5% per booking.
Monarch Charter	Online check in is only available for passengers who purchase allocated seats.	N/A	Standard seat allocation SH: £8. LH: £10.	1 x 20 kg bag is usually included. Passengers should check with their tour	Extra 3kg SH: £37.50 LH: £50	Up to 25kg: £25 (airport only). 25-32kg: £35 (airport only).	Available for purchase on board. Meals can be pre ordered from £7.99 (online).	PayPal: no charge. ADP refund fee: £25.	2% of total or £5 per booking whichever is highest.

				operator					
Norwegian Air Shuttle	Included in ticket price.	Fast track: £10.	Standard seats: £7-25.	N/A	1 x 20 kg bag: £7-50 depending on route and if purchased online or airport. Excess: £9 per kg.	Snow / golf 20kg: £20-33 (online), £30-54 (airport). Bikes / surfboards 25kg: £30-50 (online), £40-60 (airport). Musical instruments 20kg: £30-54 (online).	Available to purchase on board.	Ticket change: £36-75. Name change: £36. Call centre booking charge: £15. APD refund fee: £5.	1.99% per booking.
Ryanair	Airport check in: £70 Online check in: 2hrs-7days before departure included in fare. Online check in 7-30 days before departure is available for passengers who have paid for advance seat selection.	From £2 (online), from £4 (airport). Also included with premium seat allocations.	Premium seat (inc priority boarding): from £10 (online), from £15 (airport). Regular seat: from £5 (online), from £7 (online). Check in 7-30 days is also included for passengers who pay for seat allocations	N/A	1st or 2nd x 15 kg bag: £15-£25 (online), £30-70 (airport/ phone). 1st or 2nd x 20 kg bag: £25-45 (online), £40-75 (airport/ phone). Excess fee: £10 per kg.	Up to 20kg: £50 (online), £60 (airport).	Available to purchase on board.	Boarding card reissue: £15 (for passengers who have checked in but cannot produce their boarding pass). Flight change: £30-60 (online), £45-90 (airport). Call centre booking fee: £20 per booking. Name change fee: £110 (online), £160 (airport, phone) APD refund fee: £17 per passenger.	2% per booking.
Thomas Cook Airlines	Online check in is included but conditions may vary for holiday bookings, check with your tour operator.	N/A	SH: from £6.50, MH: from £9.50, LH: from £14. Children half price.	Some package holidays may include hold luggage, passengers are advised to check with their travel agent. From May 2015 all LH will include 20 kg.	1 x 20 kg bag: SH - £19 (online), £39 (phone), MH - £22 (online), £48 (phone), LH (ex USA) - £28 (online), £48 (phone). USA flights - 23 kg bag £50 (online), £70 (phone).	Varies depending on item, e.g. golf club 15 kg: £60 per return trip. Ski/snowboard equipment: £70 per person per return trip.	SH: £6.50 (online), MH: £9 (online), LH: £11 (online). Children half price.	Name or flight change: short and MH over 25 hours before departure or LH over 80 hours before departure - £35 + fare difference (online), £55 + fare difference (phone).	2% per booking.

Source: UK CAA (2015)

