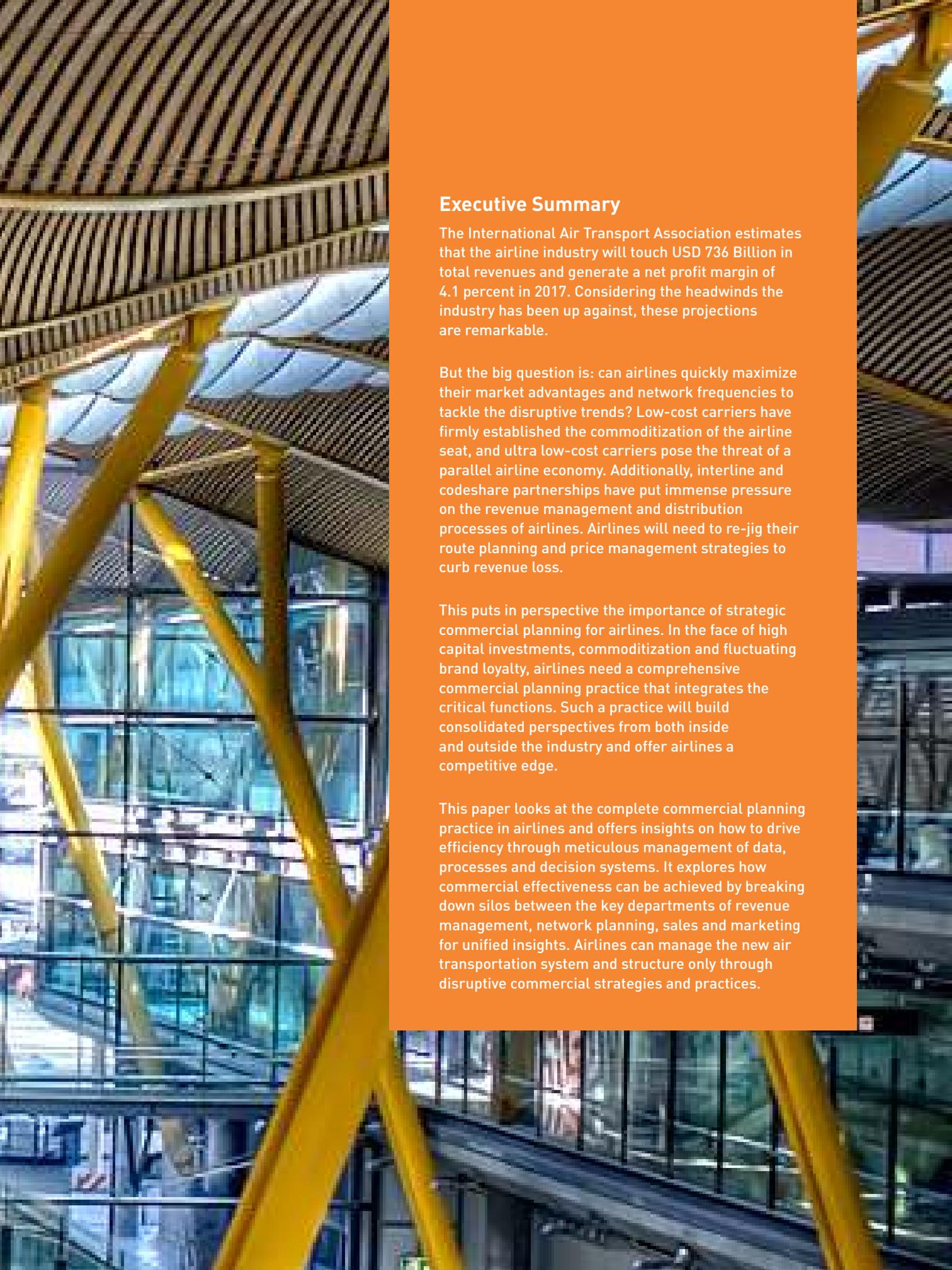


Raj Sivakumar
SVP Travel Technology
Kashyap Mansata
General Manager – Capability

COMMERCIAL PLANNING PRACTICE: ENABLING AIRLINES TO SCALE GREATER HEIGHTS







Executive Summary

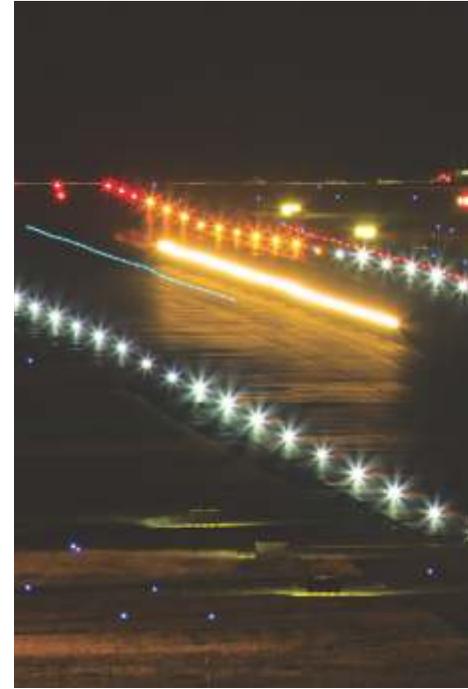
The International Air Transport Association estimates that the airline industry will touch USD 736 Billion in total revenues and generate a net profit margin of 4.1 percent in 2017. Considering the headwinds the industry has been up against, these projections are remarkable.

But the big question is: can airlines quickly maximize their market advantages and network frequencies to tackle the disruptive trends? Low-cost carriers have firmly established the commoditization of the airline seat, and ultra low-cost carriers pose the threat of a parallel airline economy. Additionally, interline and codeshare partnerships have put immense pressure on the revenue management and distribution processes of airlines. Airlines will need to re-jig their route planning and price management strategies to curb revenue loss.

This puts in perspective the importance of strategic commercial planning for airlines. In the face of high capital investments, commoditization and fluctuating brand loyalty, airlines need a comprehensive commercial planning practice that integrates the critical functions. Such a practice will build consolidated perspectives from both inside and outside the industry and offer airlines a competitive edge.

This paper looks at the complete commercial planning practice in airlines and offers insights on how to drive efficiency through meticulous management of data, processes and decision systems. It explores how commercial effectiveness can be achieved by breaking down silos between the key departments of revenue management, network planning, sales and marketing for unified insights. Airlines can manage the new air transportation system and structure only through disruptive commercial strategies and practices.

Commercial Planning Practice: Enabling Airlines to Scale Greater Heights



Raj Sivakumar & Kashyap Mansata

Commercial planning is a balancing act for airlines in their pursuit of higher revenues

Introduction

According to the International Air Transport Association (IATA), the commercial airlines industry posted one of its strongest performances in 2016 – in terms of both net profit and return on invested capital. Despite the impressive growth, airlines are weighed down by major challenges. Rising oil prices, slowdown in traffic growth, capacity expansion and price competition – these are realities the industry must address as it consolidates the advantages of high performance in a volatile future. Airlines also continue confronting challenges on both cost and revenue, and achieving break-

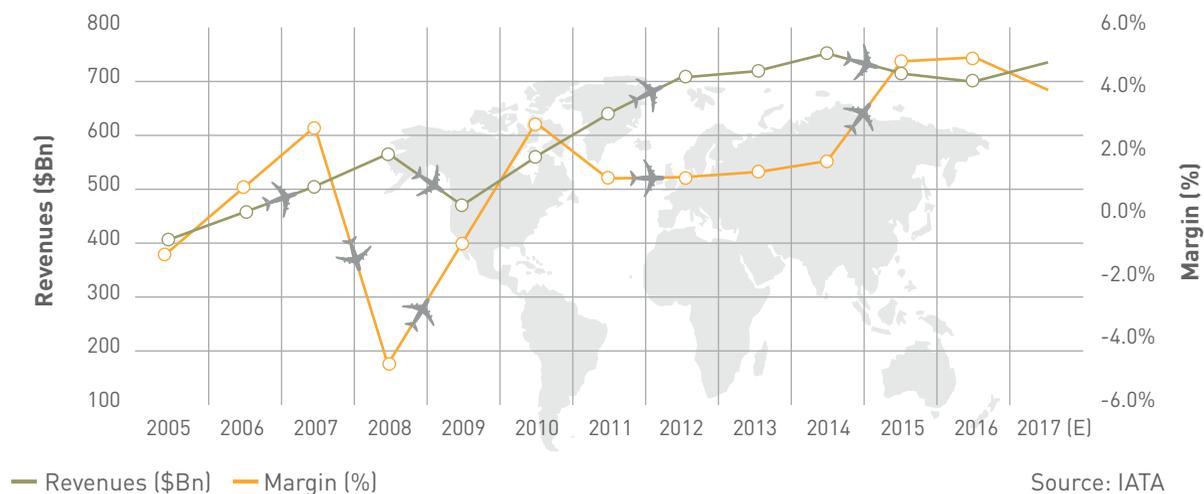
even load factors against competition posed by Low-cost Carriers (LCCs) and Ultra Low-cost Carriers (ULCCs).

For the past decade, airline net profit margins have hovered around one to two percent. The industry continues to see a huge churn with bankruptcies, mergers and acquisitions for both consolidation and survival.

Such an ecosystem pushes airlines' commercial planning to perform a tightrope walk. They need to remain commercially viable and realize the full potential of their network amidst the 'moment-to-moment' swings in pricing,



Figure 1. The Highs & Lows - Global Airline Profitability



inventory, sales and marketing. It is about protecting profitability and preventing the chipping away of

revenues. Above all, it is also about the agility to identify and execute well-timed commercial

adjustments for better revenues, margins and market share amidst rising competition.

Smart and efficient commercial planning is a critical differentiator in the current environment. It will allow airlines to maximize revenues and profitability as well as track new markets, business and opportunities. It will build holistic perspectives from both inside and outside the industry to enable airlines to compete better in a complex and competitive market place.

A strong commercial planning practice hinges on the collaborative working between the various functions of network planning, revenue management, sales and marketing. The deluge of commercial data needs to be

The Road Ahead

- More worldwide long-haul routes
- Four billion air travelers and 55.7 million tons of cargo
- Capacity expansion to decrease to 5.6 percent from 6.2 percent in 2016
- Global passenger load factor expected to drop to 79.8 percent from 80.2 percent in 2016

consolidated into a single version of truth and mapped effectively with external market and competitive data for the right insights and

decisions. The problem, however, is that these functions often operate in silos. Commercial planning can help address the disruptive changes by aggregating the siloed functions into a seamless practice.

If done right, strategic commercial planning can achieve maximum profitability for airlines. It will create a sustainable model that will exponentially change the business dynamics. It can become more innovative and customer-oriented through sharper data insights and analytics. It will help in superior decision-making that collectively leverages the best performance drivers.



Role of Key Functions in Commercial Planning

Let's first take a brief look at the four key functions and their role in commercial planning:

- **Revenue Management:**
Capacity, load factors, pricing, revenue integrity and analysis, passenger yield, cargo and ancillary services
- **Network Planning:**
New market planning, network structure, fleet planning and schedules, alliance management, hub connectivity
- **Sales:**
Sales planning, Point of Sale (POS) strategy, account management, incentives and promotions, passenger mix for optimized revenues, tactical pricing, competitor analysis, channel management, cost-of-sale strategy
- **Marketing:**
Marketing strategy, promotions and campaigns, social media management, reputation management

Figure 2: Holistic View - Four Pillars of CPP



Each of these functions needs to understand data in the right context and take decisions based on holistic insights. It calls for:

- Consistency and accuracy in how data is collected, analyzed and acted upon across functions and geographies
- Executing smart sales analytics (such as POS performance, cost of sale, class mix, ancillary revenues and partner performance) to respond to changing market and customer needs
- Minimizing revenue leakages, including deliberate and unintentional Reservation Booking Designator (RBD) violations
- Leveraging intuitive decision-support systems to maximize revenue creation and protection
- Efficient analysis of traffic mix for accurate decisions on pricing, networks, inventories and demand

Together, these functions need to influence key external factors such as taxation, infrastructure and fuel-efficient aircraft to enhance sustainability.

Let's now take a granular look at each of these functions.

1. Revenue Management: Plugging the Leaks

Revenue leakage is the fulcrum on which profits and losses are balanced. The complexity of airline operations makes the industry vulnerable to revenue leakages that can seriously undermine revenue optimization efforts. A key responsibility of revenue management is to ensure billing and receipt of the correct fares, fees, and charges to interline partners through the right tools and standards.

The Price Problem in Revenue Integrity

- Special fares – corporate fares, net fares, agency fares
- Currency fluctuations
- Dynamic nature of the distribution channel
- Interline/code-share agreements between airlines
- Multiple fare products (one-way vs. return, instant purchase vs. advance purchase)
- Different itinerary mix (local vs. connecting)

A holistic approach to revenue management and revenue integrity is important. Efficient revenue management aims to protect the airline's revenue integrity through lean and tight financial processes that:

Accurately maintain financial data flows from direct and ancillary services to the account books

Provide real-time insights and visibility into how revenue and cost drivers affect profitability

Integrate digital and physical transactions to maximize return on assets

Prevent fraud and comply with regulatory requirements

Leverage analytics to provide insights-driven decision-making

Pricing is a key factor in revenue integrity. RBDs provide a good means of aligning demand at multiple price points to forecast demand. Maximizing flight revenues through the right demand-price forecasting is a critical responsibility of the revenue management function.

The revenue management stream of a commercial planning



practice drives profitability by improving revenues and managing costs.

A robust revenue generation process intelligently uses data and analytics to quickly, intuitively and consistently identify performance trends and deviations to influence cost and revenue drivers.

2. Network Planning: Driving Operational Success

Between 2012 and 2014, a total of 9,600 new commercial aircraft were ordered by different categories of airlines to manage the projected growth in passenger traffic. Managing the risks and financial challenges of such investments are linked to network planning. The important questions to be addressed include:

How will the higher fixed operating costs of leasing new aircraft be managed?

What are the right network strategies to offset costs with maximum passenger revenues?

Can new destinations be viably linked to connecting hubs?

What is the optimal mix of fleet replacement, new routes, upgrading existing markets and code-sharing with alliance partners?

Network planning plays a key role in profitability and operational success. Within this function, there's a need to continuously evaluate competition and improvements around current route structures and schedules. New markets that will generate incremental profits should be identified. Quality industry data and analytics can provide insights to identify profit-generating

networks and schedules, right down to cabin reconfiguration levels.

Airline partnerships in the form of alliances, joint ventures and sharing arrangements are powerful means of expanding the network reach, leading to higher revenues and reduced costs. A strategic goal of commercial planning is to determine the best business models for penetrating new markets at optimum costs and minimum risks. Would creating a subsidiary be the best way, or should the airline take an equity stake? Should it be a partial acquisition, a merger, or a co-branding arrangement? What would work best in the short, medium and long terms? A responsive and automated network planning function can provide answers to these questions.

It can also analyze market segments, code-sharing, flight frequencies and enable fare and fleet optimization. It should maximize synergies in interline partnerships and processes so that issues of revenue and tax reconciliation are not show stoppers to higher profits. The ultimate aim of an efficient commercial planning practice should be to drive innovations that improve productivity and profitability.

Provide details of high-yield categories

Analyze revenues and cost of sale for different channels such as travel agencies, global distribution systems and OTAs

Granular insights into customer relationships can enable airlines to apply merchandising techniques and leverage up-selling and cross-selling opportunities. In such cases

commercial planning has the responsibility to manage commission payments. Based on data analysis, it determines whether to opt for fixed amounts per transaction or a percentage of the transaction value. Agile processes and automated systems will help ease the load of administrative work so that business development teams can focus on innovatively building additional revenue streams.

3. Sales: Innovating for New Revenue Streams

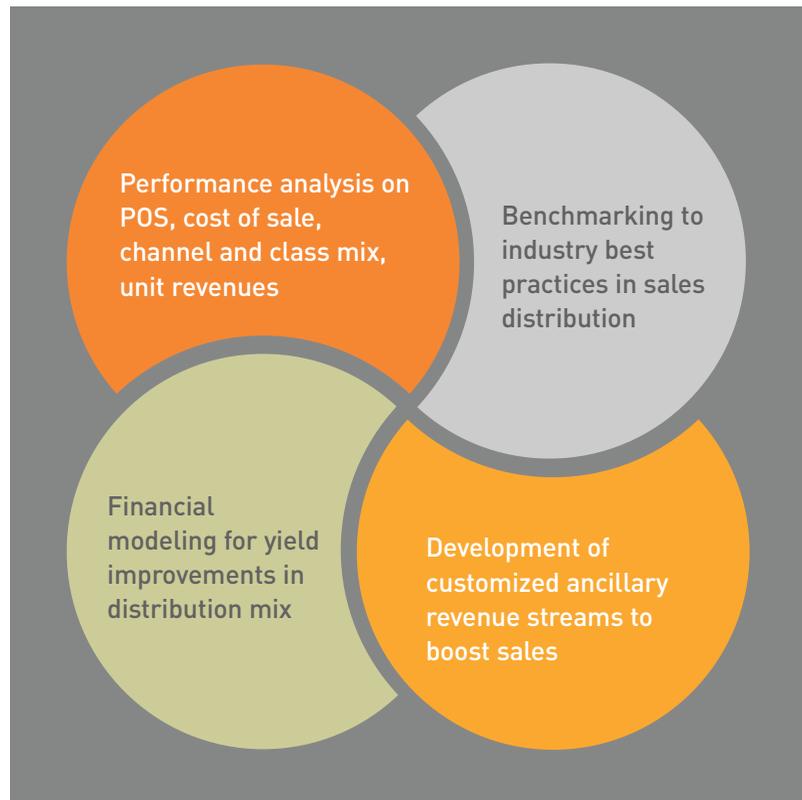
Today's sales channels have minimized the brick-and-mortar points of sale and moved towards online channels, both proprietary and through Online Travel Agencies (OTAs). Third-party sales relationships have also emerged, such as referral channels, co-branding and loyalty programs.

A well-defined commercial planning practice enables sales and business development in the following ways:

- Identify the right channel mix and distribution processes through segmented revenue and cost analysis

- Determine optimal distribution costs for better margins

Commercial Efficiency in Sales Distribution



4. Marketing: Catering to Evolving Customer Needs

In a commoditized environment, airlines are witnessing swift changes in their passenger mix. Millennials, digital natives and the new middle class in emerging markets bring varied expectations of customer experiences. This calls for smart commercial planning and management with regard to branding, loyalty programs, payment models, and individualized marketing campaigns and promotions.

Commercial planning will need to intelligently leverage new data management processes and technologies to identify the right investments in merchandizing, loyalty management programs and virtual networks. This requires sharp insights to enable the right investments in real-time integrated systems, technologies and processes. An efficient commercial planning practice recognizes that satisfying customer experiences drives revenue growth. It carefully weighs the investments the airline needs to make to sustain customer

loyalty. It also looks at ways and means to involve partners and suppliers in sharing marketing costs.

Intelligent systems can help the commercial planning practice to analyze:

- Customer traits, behaviors and preferences
- The commercial feasibility of new products and services
- Potential for revenue generation in specific customer segments

The Interplay Between the Key Commercial Functions

Strategic commercial planning involves immense complexity and interplay between the above commercial functions. For an airline, the product is the flight that is sold between any city pair. Numerous factors will need to be considered for this seemingly simple action. From the type of demand, propensity to pay, existing transportation facilities, infrastructure availability to cost of setting up operations and size of aircraft — the list is long. The complexity increases exponentially

when new flights are added or the flight time is tweaked or code-share agreements are added. There needs to be significant synergies among the four functions to understand data in this context and take decisions that will lead to profitability.

However, as mentioned earlier, as each of these functions often operate in silo, they refer to their own data sets, a subset of the overall data, and take decisions based on the partial data. Further, the key performance indicators for each function is different and when they operate in isolation, the result is less than optimal.

For instance, the revenue management team will opt for enhancing the class-mix on their flights to optimize demand. However, the sales team will try to sell more lower fares in line with their efforts to improve the relationship with corporates and agents. The network planning team may add a flight to the schedule to improve utilization of the aircraft. But the marketing team may form alliances by offering freebies. This causes friction between the teams and results in overall dissatisfaction.

Figure 3. Connected - Key Attributes of Each Function



What airlines need is an efficient commercial planning and analytics platform that pools data for various commercial functions from different sources (within the industries across geographies) to perform a variety of analyses. The platform should include a wide range of decision-support, data visualization and analytical tools. It should enable deep dives into passenger preferences, continuously streamline business processes, and integrate the true

drivers of sales and revenue. It should provide a cloud-based big data repository to store and mine information. Compatibility with the airline's reservation, revenue accounting and management systems is important, and it should offer cross-device support for decision-making 'on the go'. Additionally, enterprise users should be able to access accurate reports and dashboards capturing key performance indicators, trends and other relevant data in real time.

Such a commercial analytics solution needs to smartly integrate and leverage data residing in the commercial planning practice. It should deliver actionable insights for speedier responses and help airlines achieve revenue optimization. The outcomes of the right platform and solution include empowered decision-making, increased productivity, revenue maximization and competitive advantage.

Conclusion: Smart Commercial Planning

IATA estimates that 7.2 billion passengers will travel by air in 2035 (this is almost double the 2016 figures of 3.8 billion). Such huge internal customer data generation can significantly enhance passenger segmentation, customer experiences and business processes to boost revenues.

With insights driving business decisions today, it has become imperative for the airline industry to mine huge volumes of complex data from disparate sources and speedily convert them into insights. This is pivotal to unlocking the emerging opportunities in managing revenue generation and leakage, product and service innovation, personalization, customer retention, distribution channels, partners, reputation and feedback.

The ultimate aim of an airline's commercial planning practice is to drive business strategy. Every airline has a unique positioning, and the strategic objective of the practice is to leverage unified systems to craft optimal business models.

Cracking the customer experience code in the digital era demands constantly evolving best practices that include:

- Close collaboration of all commercial functions
- Optimally assigned fleet that balances operational constraints and demand
- Competitively positioned pricing strategy
- A single version of the truth across all commercial functions driven by business intelligence

Ultimately, efficient commercial planning rests on seamlessly shared next-generation data, practices and methodologies. A strategic commercial planning practice is the answer to help airlines address challenges and stay ahead of the competition curve in a changing marketplace.

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