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## BUSINESS

# Airlines Cash In on Loyalty Credit Cards

Carriers are expanding rewards offers to generate steady revenue from banks as fuel costs rise



Southwest representatives promoting the airline's loyalty program at Denver International Airport this month. PHOTO: ANDREW TANGEL/THE WALL STREET JOURNAL

By Andrew Tangel and Alison Sider

August 27, 2018

Airlines are inundating customers with credit-card offers, hoping to widen a lucrative and steady revenue stream as they rely more on income beyond fares.

Every major U.S. carrier earned more from credit-card and loyalty programs in the second quarter than during the year-earlier period, financial disclosures show. For many airlines, those increases outpaced overall sales growth. Much of the revenue comes from the credit cards associated with loyalty programs, though the programs don't necessarily require customers to have a credit card.

"It is amazing how much it continues to grow," said Kurt Stache, senior vice president for marketing, loyalty and sales at American Airlines Group Inc.

Revenue from American's loyalty program grew 7% to \$1.4 billion in the second quarter, while overall revenue at the world's top airline by traffic rose 4%. The loyalty program accounted for 12% of the carrier's overall sales, roughly flat from a year earlier.

Banks buy miles from airlines and award them to people who sign up for new cards and cardholders who make purchases on everyday items. The more cardholders spend, the more miles they rack up—and the more cash the issuing banks pay the airlines. Cards not tied to a particular airline work in a similar way, but the banks pay airlines when holders convert points to miles.

Airline credit cards essentially let carriers book revenue from a slice of customers' spending, though they have strong competition from credit



Delta expects its deal with American Express to contribute \$4 billion in revenue by 2021, up from \$3 billion in 2017. PHOTO: MIKE BLAKE/REUTERS

cards unaffiliated with airlines that may offer benefits such as 2% cash back.

Loyalty programs are among the top lucrative revenue sources airlines are tapping beyond ticket sales. Revenue from nonfare, ancillary sources such as bag fees and loyalty programs accounted for 11% of global airline revenue last year, up from 5% in 2010, according to industry consultant Jay Sorensen.

Loyalty programs are providing a buffer this year from higher fuel prices that have pushed airlines to trim capacity-growth plans and raise ticket prices. Consumers will keep using their cards to buy food and other staples even if the economy sours and they pull back on travel, consultants and executives expect.

“It’s reliable, stable, predictable revenue with healthy margin attached to it,” said Luc Bondar, vice president for loyalty at United Continental Holdings Inc.

As their name implies, loyalty programs and the credit cards associated with them aim to encourage repeat business. Southwest Airlines Co.’s Chief Revenue Officer Andrew Watterson said members of the carrier’s Rapid Rewards tend to fly more if they sign up for the credit card. The program contributed 15% of Southwest’s second-quarter revenue of \$5.7 billion, the largest percentage among major U.S. airlines.

Executives expect to make even more from loyalty programs in coming years. Delta Air Lines Inc. Chief Executive Ed Bastian told shareholders in February that the airline’s deal with American Express Co. is expected to contribute \$4 billion in revenue by 2021, up from \$3 billion in 2017.

Executives at discount carriers including Spirit Airlines Inc. and Sun Country Airlines say they plan to sweeten credit-card programs to keep up with the competition.

“This year is the busiest year I’ve seen in the last 10” for new travel-card issuance, said Brian Kelly, founder and chief executive of The Points Guy, a travel advice site.

Airlines hope new routes will help attract customers to sign up for their loyalty program cards, too. Southwest President Tom Nealon said plans to add service to Hawaii are spurring passengers to save the points they receive for signing up for its new card for a trip to the islands. United, which introduced a new loyalty card this year, hopes its growth plan involving more flights to smaller cities will make its cards more attractive.

Allie Nyquist and her husband got a United card this year, hoping to use their sign-up miles for their honeymoon in Tahiti. A 26-year-old medical student in Cleveland, Ms. Nyquist said student loans keep her on a tight budget.

“We are looking for any way we can to try and find a little extra room so that we can maybe go on a little bit bigger trip,” she said.

Airline cards allow customers to effectively get back some of the fees that retailers typically bake into prices for using credit cards, industry consultants say. U.S. merchants paid \$77 billion in such fees on \$3.6 trillion in transactions last year to payment companies including Visa Inc. and Mastercard Inc., according to the Nilson Report, a payment-industry trade publication.

Banks benefit from airline cards, too. They get access to customers who pay annual fees of \$100 or more for those rewards, tend to be more affluent and can spend up to five times as much as on other cards in their quest for miles, said John Grund, managing director in Accenture’s payments practice.

“It’s a magical formula,” he said.

Loyalty-program revenue also includes miles earned when passengers buy tickets with cash, but Stifel analyst Joseph DeNardi estimates the vast majority of airline miles are bought by banks.

As they expand their programs, sometimes making it more costly to redeem miles for flights, airlines risk disappointing loyal customers who are used to a strong return on their rewards, especially for international travel, said Hal Brierley, who advised American when it launched its frequent-flier program in 1981.

While airline rewards don’t always go as far as they once did, analysts say, some carriers have taken steps to make more seats available to customers looking to use points to fly and offer other ways to use rewards than buying tickets.

“It’s harder, when you have millions of people earning miles, to provide the fantasy seats that once existed,” Mr. Brierley said.

#### **Corrections & Amplifications**

A chart on airline baggage fees in an earlier version of this article incorrectly listed revenue figures in millions instead of billions. (Aug. 28, 2018)

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