

T2RL'S First View is our rapid analysis of breaking news. It helps provide perspective, putting the facts in the context of our wider and deeper knowledge of the market.

Active Regulators Demand Systems Flexibility

T2R Staff

The Facts

Spirit Airlines has been fined \$50,000 by the US Department of Transportation for failing to disclose all of its taxes fees and charges in promotional Tweets. In the UK Monarch airlines has been censured by the Advertising Standards Authority for advertising discounts that weren't. This year has seen many other examples of regulators cracking down on travel companies in the name of consumer interests.

The Analysis

The move to online distribution by the majority of airlines has brought them increasingly under the scrutiny of politicians anxious to project an image of being consumer champions. When the United States deregulated the airline industry in 1978 GDS distribution was in its infancy. Most ticket purchases were made in an opaque manner by travel agents talking on the telephone to airline reservations clerks. Even with the spread of the GDSs the process remained obscure to consumers but that has changed completely over the last ten years. On both sides of the Atlantic airlines are now firmly in the direct-to-consumer business and as a result their business practices have come under much closer scrutiny.

The judgement against Spirit set the precedent that even in a communications medium restricted to 140 character messages airlines are required to conform with consumer legislation. The most recent concerns of the legislators have been with transparent disclosure of the full cost of an airline journey, to include all taxes fees and charges. However there is more to come. Already the US government has decided that from January next year airlines will be obliged to:

- Promptly notify passengers at the boarding gate, on airline websites and via their phone reservation systems of flight cancellations and delays of more than 30 minutes.
- Allow customers to cancel reservations without payment for at least 24 hours if they're made at least a week before departure.
- Include all government taxes and fees in advertised fares.
- Not raise a fare after a ticket has been bought unless it's a result of government taxes and fees and the flier agrees to any increase.

This is not all. Senator Mary Landrieu of Louisiana has introduced the Airline Passenger Basic Airline Standards to Improve Customer Satisfaction (BASICS) Act, which would require airlines to allow passengers one checked and one carry-on bag for free. Most airlines in the United States have seen baggage charges grow to be the difference between profit and loss. Their executives will no doubt be lobbying against the Senator's bill but 2012 is an election year and it is hard to know what populist measure might gain support in the frenzied political atmosphere that will generate.

In T2RL's view airlines will have to accept the fact that their services are subject to political influence and that legislators are liable to introduce rules that may or may not be justified - or even internally consistent. Where lawmakers have any understanding of technology issues at all they are almost invariably conditioned by e-commerce developments from the last few years. The old arguments that changes need months or even years to be developed and introduced will be very hard to sustain.

This leaves the systems vendors in the airline industry in a very challenging position. The traditional players especially may struggle. Last week Tom Klein, President of Sabre Holdings, gave an interview in which he stressed the importance of airlines waiting for standards to be agreed and implemented before moving ahead with innovations in merchandising. This seems to be a very short-sighted view and one unlikely to be supported by legislators with an eye to popular opinion.

Smaller and more nimble companies are likely to be much better placed to help airlines respond to rapidly changing demands. Companies such as Datalex and EZ Travel have the ability to deploy solutions at the rate demanded and should see increased opportunity with the increasing rate of environmental change.

However the small companies do not have the capacity to replace the industry giants in all respects. The barriers to entry are large, not least the investment requirements to build systems scalable to manage hundreds of millions of passenger bookings. The established systems will be with us for a while yet. The answer to the challenge lies in architecture. Major systems providers are already providing APIs to their services. They have the opportunity to remain in place, providing the heavy lifting while smaller and more agile providers develop the flexible and innovative solutions.

The Speculation

If we accept the need for smaller and more flexible providers to meet airlines' needs in a rapidly changing world where does this leave the established vendors? The business of providing the back-end databases is unlikely to attract the same margins as that of developing cutting edge customer facing applications. If they are to avoid being commoditised the major suppliers will have to develop a strategy.

One way forward would be to establish self-contained enterprises to act as "skunk-works" quasi independently from the parent company. A single major vendor could establish multiple teams, as independent profit centres, competing with each other as well as with the external suppliers. Keeping them isolated from the centre would ensure that they retained the small business approach.

We have begun to see this kind of thinking in Sabre's announcement of an "App Store" in September 2011. It needs to develop much further if the major players are to remain relevant.