ANCILLARY REVENUES IN SOME SECTORS OF THE TOURIST INDUSTRY

di Renata Imbruglia

Sapienza Università di Roma
renata.imbruglia@gmail.com

Abstract

The aim of this paper is to highlight the role of ancillary revenue, revenue generated from the sale of goods and services that differ from or enhance the main service or product lines of a company. They are also called extra-core business. The recent world economic crisis has strongly reduced profits for many companies. Ancillary revenue is part of the strategy that has been embraced by many enterprises in different sectors of the tourist industry. We consider the hotel industry, the cruise and air transport sectors.

Keywords: ancillary, industry, revenue, services, tourism.

1. Introduction

The aim of this paper is to investigate the role of ancillary revenue, revenue generated from the sale of goods and services that differ from or enhance the main services or product lines of a company. It is also known as extra core business and in the last years, it has increased out of proportion, creating additional opportunities for growth. Examples include concessions at sporting events, pay-per-view movies offered by airlines, and carwash services sold by gas stations. Ancillary revenue may in some cases exceed primary revenues, leading to changes in business models.

The recent world economic crisis strongly reduced profits for many companies; therefore, companies have since then carried out cost reduc-
tion policies. However, in spite of such measures, a policy of maximization of revenues became necessary. Ancillary services were able to fill this gap and the importance of revenues deriving from extra core business has further increased becoming a huge portion of many companies’ total revenues.

Since the model was introduced by Low Cost Carriers (LCCs), the strategy has gained inspiring success and has been adopted by many other sectors of the tourist industry.

The practice of unbundling the travel experience by charging additional fees for services leads to a double result: on the one hand, the consumer is able to purchase the tourist product at a competitive price and can then add a number of different additional paying services; on the other hand, this practice provides a real personalization of the travel experience, based on personal requests, thus creating a tailor-made product.

We will consider ancillary services in three different sectors of tourist industry: hotel industry, the cruise and air transport sectors.

2. Ancillary services

Ancillary revenues are revenues generated from goods and services that differ from or enhance the main product or service (ancillary to the core business) and are accessories to it.

All these services are able to improve the consumer experience and it has become more and more evident that nowadays companies in many sectors are investing in ancillary services not only to boost their revenues but also to present a more competitive and tailor-made offer to consumers.

Consumers therefore have the choice to add additional paying services, according to their own needs and income.

As the focus is on the single customer rather than the product, it becomes necessary to get to know customers thoroughly, with their preferences and requests in order to develop a successful strategy. By charging additional fees for services, companies can enlarge their offer focusing on unsatisfied requests.
In order to create a strategy based on selling ancillary services, these services must create value added without increasing costs. Thanks to this strategy, ancillary revenues providing additional profit account for an increasing percentage of the total revenues, and are exempt from additional costs.

Remarkably, the ancillary strategy is not a recent invention. Examples of these services can be found everywhere. The car sector has been applying this strategy all along, by selling the core product at a competitive price, and offering a number of additional paying services.

However, it is the industry of tourism, more than other sectors, which has been benefiting from increasing revenues. A large number of tour operators, hotel chains, cruise companies and above all airline companies are strategically exploiting the sale of a wide range of products and services that are ancillary to their core business.

The strategy has been introduced by LCCs: they started to unbundle the travel experience, selling the core product (the airplane ticket) at a competitive price, and then charging separate fees for many services that were traditionally included in the price of the ticket. Revenues generated from direct sale to passengers and indirectly by unbundling other services have become an important financial component.

As a matter of fact, the rising cost of fuel combined with the international financial crisis, and the development of the ancillary sector led full service carriers to adopt the strategy. The American company United Airlines places great attention upon the issue by studying new methods and creating a business unit called merchandising, which is totally responsible for ancillary revenues.¹

Not surprisingly, many companies, and not only airlines have a business model based on the creation and development of ancillary services.

According to a study commissioned by Amadeus, it is estimated that sales revenues of tourist activity linked to ancillary services will increase by 30% in the next 3 years.²

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¹ In 2009 United gained 1.2 billion euro from ancillary services, and in 2011 over 4 billion euro followed by Delta with more than 2 billion euro.
² Forrester Research, 2011.
2.1. Unbundling and fares regulation

As already stated, LCCs were the first to introduce ancillary services, and for this reason, we refer to them when tracing back the birth of these services in many sectors of tourism industry.

The LCC, also known as «no frills», based their competitive strategy on the reduction of fares; the flight fares were lower than traditional carriers. This was made possible by unbundling the travel experience, separating many amenities, entertainment on board and services from the flight fare, along with cost reduction policies (namely bypassing busy and expensive hubs, and reducing staff on board).

The idea was to unbundle the travel experience, by separating services not essential to the flight, and thus creating a no frills product.3

The unbundled services, however, are still available but considered as accessories and separate fees are charged for them. The revenues become ancillary revenues. As a consequence of this strategy, low cost companies can offer very competitive low fares, and differentiate themselves and gain competitive advantage.

By adopting the unbundling strategy, low cost companies can charge additional fees for services which do not increase their costs; these services are traditionally included in the airfare of traditional carriers.

Ancillary revenues correspond to all revenues that differ from the core business (from non-ticket sources for airlines companies). We can classify them into two categories: (a) direct revenues generated by the companies themselves and (b) indirect revenues that come from cross-selling strategies, sales due to partnerships, which give existing customers the opportunity to purchase additional products or services.

a. Direct ancillary services with a la carte pricing, are all the services that can be sold before or during the flight: on board sales of food and beverages, checking of baggage and excess baggage, pre-assigned seats or better seats, call center support for bookings, early boarding.

3 No frills also means low cost. The creation of this strategy is usually attributed to Europe’s largest low fare airline, Ryanair. In 2001, M. O’Leary, Chief Executive of the airline, during an interview stated: «The other airlines are wondering how they can increase fares. Instead, we wonder how we could get rid of them». 
etc.; the a la carte sale is made possible thanks to the unbundled fare strategy, which, as stated above, allows airlines to offer a basic product (the flight) and to customize the ticket by adding or declining a number of services. This provides for a real personalization and differentiation of airline products, but it is limited by the possibilities of unbundled items.

b. The second source of ancillary revenues has the advantage to be more thus more lucrative, and concerns commission-based products. Those are products and services proposed thanks to partnership agreements: hotel accommodation, car rental, travel insurance, airport transfer, entertainment devices, etc. services that can be offered during the flight booking process (this will lead to a package) or offered as additional, through co-branded booking engines on the airline’s web site.

Moreover, there are additional revenues generated by advertising, frequent flyer programs, or derived by strategic airline alliances. We will go into more details later, when dealing with the air transport sector. Of course, direct and indirect ancillary revenues are complementary.

The importance and the development of ancillary revenues in the last years demonstrates how this activity has become a crucial component of tourist enterprises, in order to provide profits in a time of global economic recession.

However, when talking about this practice, the problem of transparency cannot be ignored. Oftentimes, a company offering ancillary services to the core business does not allow the consumer to have a clear and beforehand understanding of what the final price will be. For this reason, consumers’ authorities for transparency have been alerted. The fear is that what appears as a low and appealing price offer could easily turn into a more expensive purchase than what would have been with another company. However, the consumer backlash from charging (and sometimes overcharging) fees can damage the company’s reputation. This is the reason why companies should find ways to increase ancillary revenues without harming their brand.4

4 Strong criticism on the lack of transparency on final fares was raised in various articles. In August 2012, Newsweek magazine labeled the ancillary policy of some companies
In the U.S., the air transport authorities have started to pursue a reduction of deceptive fares, fares which give profits to companies by hiding the real price of the flight, by issuing a regulation that forces carriers to show fares with taxes included. The LCCs, more than any other sector, were the most concerned by this criticism.

As a matter of fact, the increase in the price of fuel and the international economic crisis have induced many companies, not merely in the air transport sector, to adopt the unbundling strategy for their services in order to create additional revenues. These accessory activities, spreading through different sectors of the tourist industry have determined a change, from the traditional all-inclusive package to the tailor-made service, which is more suitable for the modern consumer.

2.2. Strategic reasons to introduce ancillary services

It can be argued that ancillary services are a strategic variable, through which companies achieve a «differentiation of their product», which is similar to the (vertical or horizontal) differentiation discussed in the analysis of the industrial structure.\(^5\)

To differentiate a product is to reach a competitive advantage, trying to increase the value perceived by consumers with respect to competition products. Previously, it was mentioned that this could be achieved in different ways. In the case of ancillary services, the increase in value seems to occur with respect to the core product; as a matter of fact, the different ancillary services can add levels of quality to the product, and consumers can choose based on the amount of money they can afford to spend.

What is produced is similar to a vertical differentiation, because it creates a situation in which each additional service purchased determines a quality level higher than the previous one. All consumers as aggressive with a strong public outcry. Those awful airline fees from United, American, Delta, and the rest add up, Newsweek, 2012, retrieved on the website http://www.thedailybeast.com.

would think that reaching the highest level is the best option, but the choice is limited by their income.

A company that offers a product without the option of ancillary services, would have to choose what kind of product to offer and what income bracket it wants to target: focus on quality would lead to a higher price, thus leaving out the middle and low income segments, whereas choosing a competitive price would result in a lower quality level, and would then exclude the consumers’ group interested in the quality of the product.

By offering ancillary services, companies can sell the core product at a competitive price, managing to attract consumers belonging to the lower end of the spectrum; at the same time, consumers who have higher income have the opportunity to add a number of services and then they can choose the combination of consumption that can lead to greater satisfaction.

2.3. Ancillary services and technology

The relationship between technology and tourism cannot ignore the nature of the products traded in the tourist market: these are goods and services with high information content that, however, are intangible and therefore cannot be tested at the time of purchase. The development of ancillary services cannot ignore the diffusion of new technologies, especially in tourism.

Telephony, the internet and mobile internet in particular, have become an indispensable vehicle to optimize the spread of the services offered. The tourist sector has always employed computer systems to manage bookings.

The Computer Reservation Systems (CRS) was created to optimize the booking activities of some American air carriers. Changes in CRS came through in the 1980s, with the most advanced Global Distribution

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6 Sabre, the first CRS was created in 1959 by American Airlines; then Apollo was created, to meet the requirements of United Airlines.
Systems (GDS)\(^7\); through large databases, they allow the creation of a single point so that bookings can be optimized and sales activities rationalized. Basically, the GDS, by collecting a large amount of information enable travel agents to make booking reservations in real-time from all the most important air and hospitality services, from rental companies, maritime companies, rail services etc.

Due to today’s expansion of digital technologies, the GDS, once meant to organize and facilitate bookings and purchases, have become efficient systems not only able to change the services offered, but also the habits and shopping experiences of consumers; it is indeed on this factor that the different stakeholders in the tourist sector are relying in order to sell their services.

In 2011, a study published by Amadeus, the first GDS for travel agencies, has developed a hypothesis about how travelling will change in the next five years due to mobile technology\(^8\).

The study provides an overview of the different mobile services available in 2010 and the response by consumers; surveyed companies reported that they had found that the traditional check in had been replaced by the mobile one and admitted that they were watching the online activity with great interest. In particular, they identified that mobile devices had the potential to turn visitors into customers, especially for what concerns the sale of ancillary services (meals, fees for extra baggage, speedy boarding, lounge access etc.) in the following 1 or 2 years. The study clearly reflected that already by 2010, most companies were implementing the sale of ancillary services through the web.

The agreements signed between the GDS and the different carriers around the world, have allowed companies to make additional services also available through the web. All this confirms that technology is a driving force for the sale of services and additional revenues. The combination of mobile technology and ancillary services also offers to the consumer/user the opportunity to customize their experience by selecting the goods and services that can be most satisfying. Thanks to online

\(^7\) The most renown GDS are: Amadeus, Sabre, Galileo and Worldspan.

\(^8\) The always-connected traveller: how mobile will transform the future of air travel, Global Airline Traveller Survey (2010).
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purchases and the availability of ancillary services online, consumers can design and change their travel experience whenever they wish to do so.

3. Ancillary revenue in some sectors of tourism industry

Now, we turn to the analysis of the diffusion of ancillary services in the tourist industry and the role of revenues that they generate. We consider only some sectors of the industry which, seems have experienced major changes over the last years: namely, hotel chains, cruise companies and, last but not less important, airline companies.

3.1. Ancillary services in the accommodation sector

Although ancillary products and services were first introduced by airlines, the practice is now used throughout all the tourist industry; a growing number of companies are strategically taking advantage from the sale of products and services ancillary to the core business.

Over the years, the accommodation sector, whose core business is to sell rooms, came to realize the potentials related to the use of ancillary services. The recent world economic crisis and the harsh competition faced, showed that an exclusive policy of cost reduction involved the risk of worsening the product/service quality, hence drastically reducing total revenues. The industry became more consciousness and started to reconsider the product/service, bearing in mind the profitability measured in terms of returns, based on the single customer rather than just on the product or destination. As a matter of fact, many companies in the accommodation sector have developed the hotel revenue management, a strategy aiming at optimizing their flow of revenue. The system was introduced in the American air transport sector in the 1970, under the name of Yield Management, to rationalize profits, as airlines were often unable to sell all the available seats, and would lose profits due to the fact that their flights were half full. The strategy turned out
to be very profitable; controlling the number of seats that could be sold at different fares provided a profitable form of price discrimination. The revenues were high because different types of customers with very different elasticity of demand purchased different types of tickets.

The policy was based on the well-known slogan «To sell to the right customer, at the right time at the right price».

The Yield Management in the hospitality sector aims at maximizing yield (i.e. revenues) of room occupancy: \( \text{yield} = \frac{\text{total room revenue}}{\text{potential room revenue}} \times 100 \). Revenues are generated by applied fares, whereas rack rate should be considered to forecast potential revenues. In real facts, revenue management could be considered an evolution of the Yield Management. The name is derived from the fact that being the rack rate fixed, the management can control the effective revenue to maximize the yield. Increased competences are needed besides a control of the price; it is therefore essential to carry out a study of the market with marketing tools, forecasting models, data collection along with information technology instruments to understand and possibly forecast the demand.\(^9\)

Forecasting the hospitality demand is very difficult to achieve; its complexity lies in understanding, forecasting, anticipating a demand which continuously differs from historical data and is affected by changes in consumer’s purchasing habits of tourist products (for example a new booking, the on-line purchase system, as well as the entry of low cost companies that could transfer tourists to completely new destinations).

Ancillary services are sold by hotels; as long as hotels have the tools to promote such sales, there are numerous opportunities for increasing customer spending: fees for the internet, parking, breakfast, etc. are just some examples that we will see in more details. Mobile technology is a tool that can help boost additional revenues and enhance the customer’s experience in the hotel.

Hotel chains now address all management efforts to the sale of ancillary services, following the example of LCCs. Modern forecasting systems have started to record performance out of no room departments. The idea is to consider revenues per person rather than only

\(^9\) Talluri - Van Ryzin, 2004; Chen - Chiang, 2007.
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revenues per room (revenues per available room), known as total revenue management. On the other hand, the revenue maximization has to be extended to all departments of a hotel, thus widening the offer of ancillary services, choosing the right services according to the season and to different segments of customers. Hotels can offer a broad range of additional services, from traditional catering services (restaurant) up to the modern business corners; the direct sale of these services account for a relevant percentage of potential revenues since they do not need intermediation (thus sale costs), unlike rooms. The large hotel chains are more likely to have broad purchasing options: they have space available for sports and spa/wellness and trained staff in different departments for promoting ancillary services.

Hotel chains are now mainly focusing on ancillary revenue maximization related to the business traveler market. Nowadays, companies have to face limited budgets leading to a choice of hotels that balance quality and accessible price. This is a case when the loyalty factor can make the difference: when more and more business travelers organize their own trips using the internet, they choose the facilities that according to them have a greater value. Large hotel chains whose target is to attract business travelers, have to offer additional services to increase the perception of the hotel.

Quality services such as efficient technological devices, good catering services, relax as well as convention and meeting rooms can make the difference. While hotel options can be purchased beforehand (e.g., upgrade) or after the customer’s stay (customized promotion for the next stay), the time to maximize ancillary revenues is when the guest is actually in the hotel.

Mobile technology appears to be one way of accomplishing this by increasing the visibility of ancillary products and services at each point of contact with guests. Hotels with their own app or mobile website version can make customized, location-based offerings available on smart phones and tablets. When tablets are available in the hotel rooms, they boost sales of room services and on-demand films and games. Hotels have now realized the importance of this market, as many of them have

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10 Dandapani, 2013.
added a tool for booking spa treatments or ordering room services on their mobile site or app\textsuperscript{11}.

Hotels can differentiate catering service. A good quality service can be a way to do so, and at the same time can create value added. Seasonality and local food move in this direction. Breakfast is very important for different sections of tourists and it is a service that is always rated in the customers’ review. A high level of service is required regardless of the fact that it is mostly a free service. Among the ancillary services offered to business travelers, but not exclusively to them, an important role is played by spa and wellness activities. Customers can either practice sports or enjoy wellness facilities and fitness areas. Besides meeting and convention rooms equipped with supplementary technical devices, refreshments served using the hotel catering facilities represent an important source of revenues\textsuperscript{12}.

Another very important source of revenues for the accommodation sector is represented by sales in the hotel itself: it is important both for generating ancillary revenues and for the value of the product. When sales concern high quality products or products strongly bound to the community, hotels don’t simply offer an ancillary service, rather they provide a «shopping experience». This is the case for example, of the sale of food, wine and local craft products which turn into a distinguishing element for the hotel, requiring a careful selection of the items, as the style of the hotel could be reflected in such products (Tab. 1).

It is not easy to carry out ancillary sales in this sector and managers are facing the challenge of how to increase sales. PhoCusWright has identified the points of contact for each stage of the travel cycle and the different opportunities for hotels to increase ancillary sales\textsuperscript{13}.

\textsuperscript{11} Lenoir, 2011.
\textsuperscript{12} Marriott International, which was a pioneer of the Yield Management adjustment to the accommodation sector, and always very focused on revenue maximization, provides the business segment with high quality service generating good results as far as ancillary revenues and preferences are concerned.
\textsuperscript{13} Different opportunities for ancillary sales have been identified for each stage of the travel cycle (before, during and after the stay). For example booking and departure before the stay; room services, check in/out during the stay; loyalty program, customized email promotions after the stay. PhoCusWright, 2013.
Tab. 1
Ancillary hotel offerings by category.

<table>
<thead>
<tr>
<th>Category</th>
<th>Examples</th>
<th>Additional information</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Food and drinks</strong></td>
<td>Breakfast</td>
<td>Breakfast often represents over 50% of total ancillary revenues.</td>
</tr>
<tr>
<td></td>
<td>Meals</td>
<td></td>
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<tr>
<td></td>
<td>Beverages</td>
<td></td>
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<tr>
<td></td>
<td>Fruit basket</td>
<td></td>
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<tr>
<td></td>
<td>Wine/champagne</td>
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<tr>
<td></td>
<td>Birthday cake</td>
<td></td>
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<tr>
<td></td>
<td>Mini bar</td>
<td></td>
</tr>
<tr>
<td><strong>Transportation</strong></td>
<td>Airport transfer</td>
<td>More attractive to leisure travelers than business travelers.</td>
</tr>
<tr>
<td></td>
<td>Limousine service</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Bike rental</td>
<td></td>
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<tr>
<td></td>
<td>Mass transit ticket</td>
<td></td>
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<tr>
<td><strong>Business and entertainment</strong></td>
<td>Wi-Fi</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Use of business center</td>
<td></td>
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<tr>
<td></td>
<td>Meeting equipment (projector, microphone, etc.)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>On-demand films and games</td>
<td></td>
</tr>
<tr>
<td><strong>Spa and wellness</strong></td>
<td>Treatments</td>
<td>Often run by a third party. The hotel receives a commission.</td>
</tr>
<tr>
<td></td>
<td>Massage</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Pool</td>
<td></td>
</tr>
<tr>
<td><strong>Upgrade</strong></td>
<td>Room category</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Package</td>
<td></td>
</tr>
<tr>
<td><strong>Sports</strong></td>
<td>Access to in-house sports facilities (tennis court, golf course)</td>
<td>Open to the public. Limited space.</td>
</tr>
<tr>
<td></td>
<td>Classes</td>
<td></td>
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<tr>
<td></td>
<td>Personal trainer session</td>
<td></td>
</tr>
<tr>
<td><strong>Miscellaneous services</strong></td>
<td>Flowers</td>
<td>Some packages are offered subject to product availability.</td>
</tr>
<tr>
<td></td>
<td>Extra bed/crib</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Connecting rooms</td>
<td></td>
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<tr>
<td></td>
<td>Personal butler service</td>
<td></td>
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<tr>
<td></td>
<td>Animals allowed in the rooms</td>
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</tr>
</tbody>
</table>
Having the right technology can definitely create such opportunities. The GDS of traditional travel agencies and online agencies do not provide customers with access to all ancillary products and services in the hotel. This means that hotel managers have a competitive edge, if they can offer these products on their hotel website and they have high-performance management systems.

Hotels should assess their potential future sales and anticipate how much inventory is needed. Some products are limited in number (e.g., spa treatments), while others can be sold without restriction (e.g., breakfast). It is also essential that product and service availability be updated in all reservation systems\(^\text{14}\).

Above all, in order to increase ancillary revenues, hotels should communicate effectively with their clients, know their preferences and requests, multiply opportunities for interaction, and adopt mobile technology, working in partnership with local public institutions. If hotel management suggests personalized products and services adapted to the right stage (before, during or after the stay), these products will be perceived as value-added services and not sales.

3.2. Tuscany case

As far as the Italian reality is concerned, generally hotels are smaller than in other countries, especially if compared to North America; nevertheless many of them are becoming aware that great opportunities can come from ancillary services. Tuscany is a good example of this strategy with its many hotels and other accommodation facilities which combine the beautiful landscape and food and products typical of this area. As a matter of fact, Tuscany has contributed with an efficient territory marketing and a research study on tourist expenses\(^\text{15}\).

The study aimed at identifying a number of services that could improve the ranking of Tuscany as a destination, on the one hand by strengthening the offer of all traditional tourist products such as sea-

\(^{14}\) Lenoir, 2013.

\(^{15}\) Osservatorio Regionale del Turismo in Toscana, 2009.
side, cultural, thermal baths, etc., and on the other hand by creating new tourist products related to the activities that have registered increasing interest, such as food and wine tourism, typical local products, sports, environmental and ecotourism, in order to increase the economic returns from tourism. Above all the other types, wine and food tourism appeared as the new target for tourists, and strongly increased in the last years. Wine and food routes along with the promotion of typical, local food products gave the possibility to develop tourist destinations and to strengthen the regional identity. Moreover, the natural and environmental ecotourism offer increased as a result of a better knowledge of the area as well as the environmental awareness of the new tourists.

The accommodation sector in Tuscany responded mostly in a positive way, adopting the suggestions published in 2010, to «create a slow and sustainable tourism» which resulted in a unique experience for tourists, and at the same time created ancillary revenues\(^{16}\).

Last but not less important, it is worth to mention among successful ancillary services, thermal treatments sold by hotels directly or in partnership with thermal facilities, which are quite abundant in Tuscany.

At large the rich and varied landscape of Italian regions along with the fruitful cooperation between the regional offices for tourism and all the stakeholders working in the sector, are important keys to develop ancillary services, and therefore revenues.

4. **The cruise sector**

Cruise line products appeared in the tourist industry roughly at the end of the 1960’s due to air transportation competition. Until that time, shipping companies were able to transfer passengers to the destination of their choice in the shortest time possible, on the so-called ocean liners

\(^{16}\) Among ancillary services suggested by hotels in Tuscany, there are bike rides; horse riding exploring paths away from main roads; cooking lessons; wine tasting guided tours in wine cellars, often in partnership with local wine producers; tours to olive plantations with olive oil tasting.
which were dedicated to transport. Later on, companies were forced to think about a new product which might increase the demand. It became necessary and urgent to modernize companies and create a new product. A cruise ship or cruise liner is a passenger ship used to transport passengers, which at the same time makes the journey itself and the ship’s amenities part of an unforgettable experience, together with the different destinations which are encountered along the way.

Transportation is not the prime purpose, as cruise ships operate mostly on routes that return passengers to their originating harbors. Therefore, all activities on board were enhanced: transatlantic ships which previously were mostly used for transportation between Europe and the United States, were now being adapted to meet a new demand 17.

At the beginning, cruises were connected to the luxury segment of consumers, that is to say, a small number of passengers whose status was reflected in a high quality service (a market niche). Towards the end of the 1970’s, cruise line products, still maintaining their initial fascination, started to increasingly look like a mass market product, which targeted families and young people, and provided both a cruise experience and amusement 18.

Carnival Cruise was probably the first company to offer a real new product, it was then followed by other big cruise lines: Royal Caribbean Cruise line, Princess Cruises, Norwegian Cruise line and Costa Cruises in the Mediterranean area.

In general, cruises include sleeping accommodation, meals in dining facilities, and many on-board activities such as entertainment, pool activities, and sports programs. The 1980’s were characterized by an incredible boost both in demand and supply; as a result, cruise ships grew by size, becoming bigger and bigger. The gradual evolution of the design of passenger ships from ocean liners to cruise ships has seen passenger cabins shifting from inside the hull to the superstructure with private verandas and modern cruise ships have added amenities to attract tourists.

Cruise line products have become a major part of the tourist industry, accounting for about U.S. $ 30 billion, with 20 million passengers transported worldwide in 2012. The industry’s rapid growth has favored the demand of newly built ships since 2001.

Passenger traffic has grown enormously: from 500,000 in 1970 to 6.8 million in 1995, with growth rates of about 10% per year in the 1980’s. Likely enough, the cruise line sector is probably the only macro sector of the tourist industry which has not experienced any decline, even during the recent world economic crisis. In 2012, passengers were about 17 million, with a positive forecast also for 2013 (about 18 million), as well as for the next years 19.

Costa Cruise was the first Italian cruise company, although now it has been acquired by Carnival corporation, and it shares the market with MSC (Mediterranean Shipping Company) founded in the 1995. During the last few years, the Mediterranean area has been the one with the highest percentage increase, second only to the traditional Caribbean market.

Passengers’ movement in the Italian harbors has increased constantly over the last years. According to a study of Risposte Turismo, a movement of more than 11 million passengers was recorded in 2011, with an increase by 8% with respect to 2009 and a five-fold increase since 2000.

In Italy, the movement is mostly concentrated in five regions: Lazio with 20% of the total, Liguria (18%), Veneto (17%), Campania (14%) and Sicily (11%).

In 2011, Civitavecchia was the harbor with the highest movement of passengers (about 2 millions); and good results were also registered in Venice, Naples and Genoa. Should the 2012 data and the forecast for 2013 be confirmed, Lazio is still ranking first in terms of passengers’ movement, followed by Veneto and Liguria 20.

Cruise line products typically include a wide variety of services mainly divided into core products (transportation and hospitality ser-

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19 Data based on CLIA (Cruise Lines International Association) which accounts for about 85% of the world’s total passengers. For this reason, the figure of 17 million referring to 2012 should be revised, going up to about 20 million. CLIA, 2013.

vices) and many other on-board activities, such as entertainment, sports programs, etc. and suggested visits and excursions. Some services are directly included in the price of the cruise fare, whereas others can be purchased on board, as ancillary services.

Cruise liners, the fastest growing segment of the travel industry, until recently, were also the most likely to offer packages (all inclusive fares) as opposed to a la carte pricing. However, in the last few years, they have become more willing to take all the opportunities to generate ancillary revenues on board or on shore.

All major companies claim that ancillary services are needed to keep rates low enough to attract segments of tourists with a lower spending capacity enabling a larger part of the population to go on a cruise. Cheap fares increase the demand and on board purchases are expected up to the point that «cruise ships no longer make money by carrying passengers; they make money by marketing a variety of services to them». Every single passenger can complete their own package according to their tastes and habits, in the end being responsible for the final price 21.

In most of the cruise liners, the fare does not include a variety of services which will turn into on-board activities or other revenues. The opportunities to generate revenues on board or on shore are many and varied.

Among the ancillary services available on board, it is worth mentioning: casino, video poker areas, slot machines and other games, which are offered almost worldwide by cruise companies. Other on-board ancillary services are: internet cafes, telephones, pay per view movies, videos, movies, laundry, babysitter services, wellness, spa and beauty treatments, sporting activities, shopping, extras coming from restaurants, bars, discos, 4D movie theaters, theaters, formula 1 simulators, etc.

In addition to revenues generated due to on-board activities, one must consider those generated by the purchase of excursions as a relevant part of the total. The volume of business generated by ground excursions has an impact on the cruise liners but on the destinations as well.

21 CLIA, 2011.
4.1. The Venice case

A study carried out by the University Ca’ Foscari of Venice analyzes cost and benefit of cruise liners stopping in the city \(^{22}\). The study gave a monetary indication of positive as well negative externalities due to cruise tourism, without taking into consideration the sustainability of this kind of tourism for the city. The harbor authorities and the Venice passenger terminal provided figures of the number of passengers and their average staying in order to roughly determine the expenses made by cruisers and on-board staff.

Expenses by cruisers, expenses by staff, pilotage and mooring charges and Venice Terminal Passenger profits in 2012 accounted for more than 220 million euro. However, many studies on the issue underline the importance of monitoring the amount of revenues generated as well as the negative environmental impact on the city and the area around \(^{23}\).

5. Ancillary revenue in air transport

As discussed before, the air transport sector was the first sector to introduce the unbundling of the travel experience. LCCs were the first airlines to boost their revenues, directly by selling products to passengers or indirectly as part of the travel experience. Ancillary services have generated significant revenues, additional to the core business, that have become a necessary ingredient during years in which the increase in the price of fuel greatly impacted costs sustained by the airlines. The world economic crisis and the oil price above $ 100 per barrel in 2008, had a strong impact on airlines and air transport. The IATA (International Air Transport Association) *Annual Report* on the air transport market indicate that there were positive trends starting from 2010, after the decline of 2009, which was the worst year in the whole aviation history. In 2010, the number of passengers increased as well as corporate yield, although not enough to recover the decline due to the 2008-2009

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\(^{22}\) Tattara, 2013.

\(^{23}\) Chiellino - di Cesare - Frisone, 2012.
recession. According to them, the increase in demand experienced since 2011 has to be prudently considered, because of the uncertain economic situation; this increase is mainly due to international demand and the growth of European carriers.\(^{24}\)

As an opposite trend, air transport revenues grew since 2010, reflecting an increase in passengers volumes and strong ancillary growth. Ancillary revenue has been defined by IdeaWorks as «revenue beyond the sale of tickets that is generated by direct sales to passengers, or indirectly as a part of the travel experience». Airlines can boost their revenues by charging separate, additional fees for services; on the one hand, it is a source of revenues for the airlines, and on the other hand, it allows them to engage in strategies of differentiation.\(^{25}\)

According to the study published by IdeaWorks and Amadeus, the prominence of ancillary revenues has further increased in the last few years. The data of the joint study show the top 10 earners in the airline industry when it comes to ancillary revenues. The study examined the disclosed data on financial performance of 96 airlines around the world, including low cost and other scheduled carriers, to produce detailed information on which is the airline making the most from revenues connected to ancillary products and services. The total amount of ancillary revenue is estimated to 1.7 billion euro in 2006, 7.8 billion euro in 2008, 11 in 2009, and about 22 in 2012. It is clear that this kind of revenue has become a financial necessity for airlines all over the world: in the last two years, a 66% growth has been recorded.\(^{26}\)

Once largely limited to low fare airlines, the ancillary sector is now a priority for a large number of airlines worldwide, with new activities among carriers in Europe. The revenues demonstrate how the industry’s use of ancillary services has flourished in the past few years (Tab. 2).

\(^{24}\) IATA is the trade association of the world’s airlines and represents 84% of total air traffic (2012).

\(^{25}\) The creation of this strategy is likely to be attributed to Europe’s largest low fare Airline, the Irish Ryanair.

\(^{26}\) IdeaWorks - Amadeus, 2012. The estimates include revenues from a la carte features such as baggage fees, food sold onboard of the aircraft, commissions from the sale of hotel accommodations, car rentals, insurance and partners’ revenue generated by frequent flier programs.
Ancillary revenues in some sectors of the tourist industry

Tab. 2
Top 10 airlines – Total ancillary revenue.

<table>
<thead>
<tr>
<th>Annual results 2012</th>
<th>Primary source</th>
<th>Annual results 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 5.352.000.000</td>
<td>United</td>
<td>$ 5.171.000.000</td>
</tr>
<tr>
<td>$ 2.576.660.000</td>
<td>Delta</td>
<td>$ 2.534.000.000</td>
</tr>
<tr>
<td>$ 1.987.000.000</td>
<td>American</td>
<td>$ 2.113.000.000</td>
</tr>
<tr>
<td>$ 1.655.000.000</td>
<td>Southwest</td>
<td>$ 1.418.285.709</td>
</tr>
<tr>
<td>$ 1.574.698.320</td>
<td>Quantas Airways</td>
<td>$ 1.180.000.000</td>
</tr>
<tr>
<td>$ 1.388.674.580</td>
<td>Ryanair</td>
<td>$ 1.105.741.611</td>
</tr>
<tr>
<td>$ 1.205.727.600</td>
<td>Air France / KLM</td>
<td>$ 1.100.869.561</td>
</tr>
<tr>
<td>$ 1.147.743.960</td>
<td>EasyJet</td>
<td>$ 1.086.000.000</td>
</tr>
<tr>
<td>$ 1.073.300.000</td>
<td>US Airways</td>
<td>$ 667.473.195</td>
</tr>
<tr>
<td>$ 720.900.300</td>
<td>Korean Air</td>
<td>$ 610.000.000</td>
</tr>
</tbody>
</table>


LCCs have always conducted an aggressive use of the ancillary revenue model. Without any doubt, many airline passengers are already paying these fees. The oil price spike of 2008 led many of the world’s largest airlines to join the revolution. United, American, and Delta — all stalwart legacy alliance members — issued new baggage fees for travel within the U.S., across the Atlantic, and to a growing list of destinations all over the globe.

Remarkably, there is a domino effect associated to that. The close ties created by joint ventures, codeshares, and global alliances encourage product integration.

It is not easy for consumers when policies and fares vary under the common umbrella of Star, Oneworld, or SkyTeam alliance, the three largest passenger airline alliances. The bag fees issued by one major partner slowly become common law as partners seek a seamless travel experience. And the billions in revenue that result represent an important benefit to an industry on the hunt for better profits.

Instead of viewing this new world as fee-based, the right perspective should rather be service-based. For example, Alaska Airlines added
a baggage fee with a significant payout if the carrier fails to deliver on
time. Consumers are more willing to pay additional fees if they feel
value has been added. In service industries, offering better value has
always been the key to increasing revenue.  

The consistent growth of extra revenue from three key sources
demonstrates how this activity has become a crucial component of air-
line income. Carriers worldwide rely upon the revenue from frequent
flier activities, a la carte features, and commission-based products, to
create profits in an era of ever-rising fuel costs, while keeping fares
modest in a recession-weary world.

The different types of revenues have already been mentioned, but
now they can be considered again, in relation to the air transport sector.

Direct revenues or a la carte features are often services that used
to be included in the ticket fare and are now purchased a la carte, due
to unbundled fares. This fare structure allows airlines to offer a basic
product (the flight plus some services depending on its length) and cus-
tomers can design their package by adding or cutting services. This is
also known as a la carte pricing. Typical activities include: checking of
baggage and excess of baggage, onboard sales of food and beverages,
assigned seats or better-positioned seats, priority check in, early board-
ing, call center support for reservation, on-board entertainment, fees
charged for purchases made by credit cards. All these features lead to
a real personalization and differentiation of airline products, however
limited by the unbundling.

A second source of ancillary revenues are commission-based prod-
ucts: commissions earned by airlines for the sale of hotel accommoda-
tions, car rentals, travel insurance proposed during the flight booking
process or through a cobranded booking engine on the airline’s website
and can also include the sale of duty-free and consumer products on the
aircraft, based on cross selling.

An important source of ancillary revenue is constituted by adver-
tising slots sold by the airline: revenues generated by ads placed on
in-flight magazines, as well as advertising messages displayed in gate
areas and airport lounges.

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Ancillary revenues in some sectors of the tourist industry

Last but not less important, there are *Frequent Flyer Programs* (FFP): these are loyalty programs offered by many airlines, where customers accumulate miles or points according to the distance they have flown on the main airline or its partners. The points can be spent either for a free flight or for other services sold by program partners such as hotel chains, car rental companies, retailers, co-branded credit cards.

Looking at Table 2, among the primary source there are the carrier’s primary ancillary revenue method (for the top 10 companies) and the item «Various» includes a number of activities we mentioned above, whereas Quantas and TAM, the biggest Brazilian airline, rely upon partner revenues generated from FFP for a relevant percentage of their disclosed ancillary revenue.

When dealing with ancillary revenue in percentage over total revenue, it can be noted that LCCs dominate. The percentage goes from almost 40% for the first, Spirit, to about 20% for Ryanair and EasyJet, who are the most successful and pioneers of this practice. The tenth position is held by Flybe which still accounts for 17.7% of the total.

*Tab. 3*

*Top 10 airlines – Ancillary revenue as % of total revenue.*

<table>
<thead>
<tr>
<th>Annual Results 2012</th>
<th>Primary source</th>
<th>Annual Results 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>38.5% Spirit</td>
<td>Various</td>
<td>33.2% Spirit</td>
</tr>
<tr>
<td>29.9% Allegiant</td>
<td>Various</td>
<td>27.1% Jet2.com</td>
</tr>
<tr>
<td>26.5% Jet2.com</td>
<td>Various</td>
<td>27.0% Allegiant</td>
</tr>
<tr>
<td>21.8% Ryanair</td>
<td>Various</td>
<td>20.8% EasyJet</td>
</tr>
<tr>
<td>20.8% Tigerair</td>
<td>Various</td>
<td>20.5% Ryanair</td>
</tr>
<tr>
<td>19.5% EasyJet</td>
<td>Various</td>
<td>19.1% Tigerair</td>
</tr>
<tr>
<td>18.7% AirAsiaX</td>
<td>Various</td>
<td>17.8% AirAsia Group</td>
</tr>
<tr>
<td>18.6% Jetstar</td>
<td>Various</td>
<td>17.0% Flybe</td>
</tr>
<tr>
<td>18.2% AirAsia Group</td>
<td>Various</td>
<td>16.5% AirAsia X</td>
</tr>
<tr>
<td>17.7% Flybe</td>
<td>Various</td>
<td>15.3% Jetstar</td>
</tr>
</tbody>
</table>

The performance of ancillary revenue strategies could be improved. Technological tools and the involvement of partners (strategies of cross-selling) to make unbundled fares easier to sell are essential. In recent years, several major intermediaries of the travel industry such as GDS, agreed on finding standards that would facilitate the distribution of ancillary services. On the other hand, a larger and diversified offer of ancillary services is needed. It must be noticed that an excess in the offer of services could generate negative backlash and reaction in the consumers, although they are usually willing to pay in exchange of services. And the consequences from overcharging fees might damage the carrier’s reputation.

Moreover, consumers complain about the habit of airlines of expanding the ticket fare by adding additional costs which appear later in the online purchasing transaction; information about the fees is not fully disclosed through all ticket distribution channels used by consumers, making it difficult for them to compare the total cost of the flights offered by different carriers.

British airways was the target of public outcry after its decision to impose a 4.5 £ charge when booking in economy class and pay by credit card.

The large and increasing use of credits cards to buy online airline tickets implies a fee. As a matter of fact, if an extra-fee is demanded for a certain procedure, there should be a choice; if not, it is perceived as a mockery. It is important that airlines find ways to increase ancillary revenue without damaging their reputation.

5.1. Ancillary revenue generated by baggage fee policy

Baggage fees have been so important until now that they will likely become the industry’s largest source of ancillary revenues.

Before the introduction of the first and second bag fees, U.S. based carriers reported baggage revenue of about 470 billion $ in 2007, mostly charges for overweight and oversized luggage. In 2012, baggage fee revenues rose to 3,500 billion $. What happened is that, from the moment airlines first imposed fees for checked baggage, the number of checked
bags per passenger declined, contributing to a decline in the bag handling costs, such as ramp labor and mishandled bags expenses 28.

Ancillary revenues saved the U.S. airline industry during the difficult years of 2008 and 2009. In 2012, baggage fee revenues were nearly equal to the total profit declared by U.S. airline industry and slowly, airlines all over the world followed the American fee structure, although only a minority of them clearly explained this policy. As far as baggage fees are concerned, LCCs provide a better and more complete information. They ask consumers to arrange checked-in baggage during the booking process; drop down menus specify prices and allow customers to choose the number of bags to be checked in. The importance of baggage fees as a source of ancillary revenue for a large number of companies should be a warning to them not to adopt actions that are too aggressive, that could provoke public outcry. Far too often, optional services are difficult to understand, preventing the consumers from knowing exactly and in advance the final price 29.

5.2. The case of Alitalia

Ancillary revenues, as detailed above, have substantially increased over the last few years and are expected to increase further, becoming a necessary source of revenues for all international carriers. With regards to Alitalia, the most important Italian airline, its ancillary revenues in 2009 were still largely accountable to loyalty partners and sale fees, whereas revenues from unbundled services and bag fees were very low.

Among the reasons for such a result, a wrong strategy is maybe the most relevant to be blamed: the responsibility for ancillary revenue was spread among a number of departments; the services were randomly available on the website, and the company mainly focused on selling air tickets 30.

30 This paragraph is based on material provided by Alitalia. Sarcone, 2013.
Alitalia started to adopt a new ancillary revenue strategy: baggage fees, commission on services, unbundling services, FFP, and understood that passengers would eventually get used to pay for services, but at the same time, the worldwide economic crisis would reduce their spending capacity making them more demanding and aware of quality and value of services. Passengers are very heterogeneous, and market segmentation is important to offer tailored services and prices.

The results were already clear in 2011, although the majority of sales were still carried out through travel agents, preventing sales from the web site.

It was obvious that in the same years airlines were boosting their revenues by a larger offer of services with no additional costs, and by adding value to the traveler’s experience with the ancillary services.

The company’s strategy was to improve the offer including and/or implementing ancillary services such as on board catering, fast track, on flight entertainment, advertising, revenues coming from unbundling and cross selling. In spite of the reduction in the passengers traffic, in 2012 the company recorded a positive trend of revenues from unbundled services and boutique (+57% with respect to the previous year). It seems that more than 80% of the entire revenues in the last year comes from four main sectors: boutique, unaccompanied minor fee, insurance, and extra comfort seats\(^{31}\).

It is worth pointing out that the strategy of unbundling is changing the internal structure of the aircraft. The new design will enable to charge extra fees for optional services (such as extras comfort seats), without reducing the level of comfort for all passengers.

6. Conclusion

In conclusion we have tried to highlight a very important issue: revenue that is derived from goods or services other than a company’s primary product offering. We have considered ancillary services in 3 different

\[^{31}\text{Sarcone, 2013.}\]
sectors of tourist industry. In all the sectors examined the importance of ancillary revenues has further increased in the last years allowing many companies to overcome the difficult economic crisis; they made it possible for companies to keep the core product price low so to not further discourage consumers demand. On the other hand the target is to be able to propose more and more services and products not to lose or annoy their customers. The challenge will be the optimization of ancillaries to sell the right services to the right customers at the right moment.

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Riassunto

In questo lavoro ci si propone di analizzare il ruolo dei ricavi ancillari, i ricavi generati dalla vendita di beni e servizi diversi e accessori rispetto al prodotto base. La crisi economica mondiale ha reso più difficile per le imprese conseguire profitti. L’offerta di servizi ancillari rientra nelle strategie adottate da molte imprese del settore turistico. Sono stati considerati il settore dell’ospitalità alberghiera, quello crocieristico e quello del trasporto aereo.

Parole chiave: ancillare, industria, ricavi, servizi, turismo.