

A NEW IDEA FOR AIRLINE LOYALTY: CASH BACK REWARDS FOR FREQUENT FLYERS

News / Airlines



Just in time for Thanksgiving, American Airlines has announced the [end of the Frequent Flier Era](#) as we've known it.

Starting next year, the airline's customers will earn miles based on how much they spend on a ticket rather than how far they fly. In making the shift, American becomes the last of the big three U.S. airlines to adopt a revenue-based frequent-flier program.

The switch makes good economic sense for the airlines. But if the goal of such programs is to reward and incentivize loyal passengers, then it's time to replace mileage rewards with something else entirely: cash.

Interestingly enough, American invented the frequent-flier program back in 1981. In the super-competitive years following deregulation, others followed suit in hopes of enticing passengers to stick with a single carrier for all their flights. At the time, there was still some correlation between distance flown and the cost of a ticket. So using mileage as the basis for rewards made sense.

Over the years, however, as airlines have grown more sophisticated about adjusting prices in response to passenger demand, the link between distance and cost has broken down. These

days, some short-haul domestic routes with high demand (and low capacity) are more expensive than popular and competitive international flights. As a result, those airlines still committed to mileage-based rewards programs — Alaska and Hawaiian are the last large U.S. holdouts — are kicking back more miles to a passenger who buys a cheap fare from Minneapolis to London than one who pays a more expensive full fare to fly to Cincinnati (long one of the most expensive U.S. airports). That's a bit like a credit card company offering cash rebates for how often you charge, not for how much.

Such a system might still make some sense if American and other U.S. airlines were burdened with lots of empty seats. But in recent years, U.S. airlines have cut back on their flying capacity in order to prop up prices, leading to much fuller flights. There's less need to reward passengers simply for getting on a plane, especially if they haven't paid much for the privilege.

Meanwhile, airlines have figured out that passengers like miles so much, other companies are willing to pay for them. According to a [November report from IdeaWorksCompany](#), a consultancy specializing in airline loyalty programs, more than half of the ancillary revenue (a miscellaneous, non-fare category that includes baggage and change fees) earned by airlines in 2014 came from frequent-flier programs. Those revenue streams include everything from marketing member information to other companies, to selling points to credit card companies. For example, American Express paid Delta \$600 million for SkyMiles points in 2014. Those points, in turn, will be kicked back to its Delta cardholders, typically on a dollar-per-mile basis.

Under a revenue-based model, nobody would have to wonder any longer if a particular reward ticket was worth the cost of the miles. The only problem is that there's no free market for award tickets; the airlines set the price. If American wants to raise the cost of a reward ticket from 25,000 miles to 35,000 miles, there's nothing a customer can do but accept the devaluation of his or her mileage. That might suit the airlines, but it wouldn't do much to instill customer loyalty.

There's a better way. Rather than reward passengers with miles, airlines should simply start handing out cash rebates. Passengers who fly more would receive a higher percentage of their cash back, while those who fly less would still see their accounts filling with dollars and cents. The transparency alone would be a draw. As airlines competed to offer bigger cash-back rewards, customers could better judge who really deserved their loyalty.

Meanwhile, the airlines would win by giving out a currency — dollars and cents — that's constantly being eroded by inflation, especially since passengers tend not to spend their frequent-flier rewards. (One airline analyst claims there are 17.5 million unredeemed miles sitting in frequent-flier accounts worldwide.) Ticket prices could be adjusted upward or downward for frequent fliers, giving the airlines even more pricing power. Passengers and airlines would need time to adjust to the new system, of course. But long-term, it'd ensure that every flier knew whether it was worth going that extra mile to demonstrate loyalty.

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