Chapter - 1

INTRODUCTION

This chapter deals with background to the research problem, the concept of frequent flyer programme, airline service quality, objectives, scope, significance and organization of the study.

1.1 Background

Service industries worldwide were valued at $350 billion, accounting for 20 percent of all world trade in 1980 and that figure had nearly tripled to $1,000 billion by 1992. Bateson & Hoffman (1999) estimated that the service sector accounts for 58 percent of worldwide gross national product. According to UN National Account Statistics cited by Prasad et al. (2014), the services sector has the highest sector wise contribution in global GDP with a share of 67.5 percent in world GDP of US $ 70.2 trillion in 2011. Air transport currently provides 56.6 million jobs and accounts for more than US $ 2.2 trillion of the global gross domestic product (GDP). India is considered as the 9th largest aviation market handling 121 million domestic and 41 million international passengers.

The total number of passengers travelling by air has significantly dropped by 4.79 per cent in 2012-13 to 94.8 million, in comparison to 12.05 per cent growth achieved in 2011-12. Out of this, there is a relatively high fall of 5.24 per cent in domestic travel compared to international travel with 4.09 percent decline.
However, the total number of passengers travelled by air during the first half of 2013-14 grew by 6.3 per cent compared to the decline of 4.8 per cent, in 2012-13.

With the growth of service sector in Indian economy especially in the aviation sector, it is crucial for the airline service providers to understand their customers, design offers and deliver the desired value to their customers. As per the report (see figure 1.1) on air passenger market analysis data published by International Air Transport Association (IATA), April 2014, there is a steady growth in air passenger market both in international and domestic, which is normally calculated in RPK i.e. Revenue Passenger Kilometer (Peter Belobaba et al., 2009).

Figure 1.1 Total passenger market based on revenue passenger kilometers (RPK)

![Total Passenger Market](image)

*Source: IATA website: Air passenger market analysis data, April 2014*

This study focuses on passengers’ buying intention for an airline influenced by its attribute-level performances of various service based attributes and level of satisfaction derived from these attributes and also on various attribute-level performances of airline loyalty programme. These attribute-level performances
would influence passenger’s satisfactions which lead to re-buy intention. Passenger satisfaction is hypothesized as an after effect of the attribute-level performances of loyalty programme (FFP) and Airline Service Quality (ASQ). These perceived satisfactions obtained through loyalty programme and service quality performances are separately measured and its effects on re-buying intentions of passengers are assessed with a single structured model. Critical areas affecting re-buy intentions identified as passenger perceived value, brand image and trust are linked in a structural model to know the effect of these factors on the re-buy intentions of airline frequent travelers, which are hypothesized in this study.

As per IATA statistics (IATA website, 2014) the global airline industry (total market) passenger load factor as a percent of Available Seat Kilometers (ASK) is reported to be at 79.4 per cent in April 2014 (see figure 1.2) and those empty seats have a very short shelf life; once the aero plane takes off, the possibility of any revenue from the empty seats is lost forever.”

Air Transport Action Group (ATAG, 2008) cited by Peter Belobaba et al. (2009) claims that the global airline industry consists of over 2000 airlines operating more than 23,000 commercial aircraft, providing service to over 3,700 airports.
1.1.1 Frequent Flyer Programme (FFP)

According to International Air Transport Association (IATA) special report on FFP estimates, there are at least 130 airline loyalty programs and more than 150 million members. Ravindra Bhagwanani, Managing Director of FFP consultancy Global Flight, stated that it is hard for airlines to ignore the focus on the cash generation aspect of FFPs and evidence suggests that FFPs can make a big difference to the bottom line of airlines. In addition, “FFPs are major direct cash generators for larger carriers through the sale of miles to credit card and other partners, without that revenue source, there would be very few major airlines in North America in business today” (Bhagwanani, 2012 cited in IATA, Airlines International special report on FFP, 2012).

A Frequent Flyer Programme (FFP) can be referred as a permanent incentive programme offered by an airline to reward its member passengers and encourage repeat business. The reward is usually based on either travel
purchase volume or number of trips. FFP was first introduced by American Airlines in 1981. The objective of FFPs was to maintain customer loyalty, provided this scheme profited the airlines. They were based on the argument that passengers need to find that changing airlines away from one offering loyalty bonuses is difficult and costly (Klemperer, 1995). Therefore, FFP plays an important role in the airline passenger retention, and not many empirical studies trying to measure the secluded effect of FFPs exist.

In the airline industry, frequent flyer programme has become one of the most widely used marketing tools for retaining customers and motivating service usages. In spite of its growing popularity, little is known about the factors that influence passenger’s perceptions and responses to such programs (Kivetz and Simonson, 2002).

The concept of FFPs is considered to be an excellent example of the use of relationship marketing to build customer loyalty (Palmer & Mayer, 1996; Rodriguez, 1997). Although research has shown that FFPs serve as an influential factor to the travelers in selecting a carrier, the benefits of running such schemes have been debatable because of the enormous operating costs involved.

Nevertheless, it is a well-known fact that companies that maintain and develop a loyal customer base increase their profits, as indicated by Zeithaml and Bitner (1996). These benefits typically include:

- Increasing purchases
- Lower costs
• Free promotion through word of mouth
• Employee retention, and
• Lifetime value of a customer

Nearly every full service airlines have a point reward system. The frequent flyer programme is able to provide the following advantages to the airlines (Sahoo & Vyas, 2007):

• Save approximately 40% of an airline's acquisition cost per active member
• Generate incremental advertising revenue and in-flight merchandise sales
• Issue a personalized and magnetically encoded membership card, and deliver a greeting pack to new members within 2 - 3 minutes of starting the enrolment process, and
• Enlist and fulfill new members as well as providing retention services to existing members

In addition to, or as part of their frequent flyer programme, most of the major airlines also issue co-branded credit cards or are associated with Diners Club or American express. Most airlines have unoccupied capacity on a reasonably regular basis.

According to Whyte (2003), FFP provide the following advantages to its members:

• Lounge—including services in lounges and clubs
• Preferred seating
• Priority check-in
• Increased baggage allowance
• Partner benefits (alliances/hotels/car rentals)
• Booking service
• Occasional upgrades, including certificates, and
• Priority baggage

Anthony and Chin (2002) indicated the importance of network coverage of an airline as an attribute preferred by airline passengers, especially business travelers. Business passengers will find it easier to accumulate FFP mileage if an airline covers most of his business destinations or has good coverage through alliances and partnerships with other airlines. Some important attributes of FFP shown in the literature focuses on areas which include firstly, the class of service, the bonus for travel in premium classes, and the type of fares that qualify for point accrual and also the easiness in redeeming travel benefits. The second is the partner network inclusive of hotel, car rental and other retail services. The third element axis on the terms and conditions that decide the flexibility of the FFP reward system which consists of covering the validity of miles, booking procedures, blackout dates, transferability of awards and the capacity provided for award travel. The fourth element of the programme is customer service. The last element is the privileged programme, catering to that essential customer segment of frequent high-yield travelers.

Petersen (2006) indicates that loyalty programme grow at a rate of 11 percent per annum and fastest growing segment of these programme are "mileage consumers," not frequent flyers. It was also viewed as in a typical year, about 500 billion frequent flyer miles are earned by members (leftover after redemptions).
Loyalty programmes are so popular now that more than half of all the purchases made in the US using credit cards are made with cards linked to loyalty programmes (Petersen, 2011).

The review of literature showed no clear cut categorization of underlying factors which indicate attribute level performance dimensions of Frequent Flyer Programmes. It was also examined whether any set of indicators exist to measure the attribute level performance of frequent flyer programme and found that these indicator items are yet to be explored and validated.

1.1.2 Airline Service Quality (ASQ)

Delivering high-quality service to passengers is essential for airline existence. Therefore airline operators need to realize what passengers expect from the services (Chang 2002). Service quality conditions influence a firm’s competitive advantage by retaining customer patronage, and with this comes market share (Park et al., 2004; Morash and Ozment 1994). It is argued that quality in airline service is difficult to describe and measure due to its heterogeneity, intangibility, and inseparability, and only the customer can truly define service quality in the airline industry (Butler and Keller, 1992).

Industry-specific characteristics present in many service industries limit generalizations; perspectives should be tested across various industries as suggested by leading services researchers (Lovelock, 1984; Fornell, 1992). Hence it is evident that service characteristics vary according to its multi-dimensional service settings and this aspect was considered while measuring service quality performance attributes of airlines used in this study.
1.2 Research Problem

1.2.1 Background to the problem formulation

In India, all airlines except Indigo airlines are not making any profit from their operations as per the latest statistic published by Director General of Civil Aviation (DGCA - website, 2014). Airline industry today faces crisis attributed by overwhelming operational expenses due to heavy increase in fuel prices and employee cost. These burdens on expenses cannot be adjusted by increasing price levels due to high competition in the market especially from low cost carriers. Apart from this, by looking at the peculiar nature of the airline industry it is known that – all marketing mix variables such as ‘place’ and ‘price’ are not fully under the control of airline operators in a given period (for e.g. schedules/ routes, airline-fare fixed for a route for a season).

What makes airlines distinctive are the other two Ps i.e. ‘the Product’ (Service) and ‘the Promotion’ based attribute-level performances. Evidences provided in literature argue that it is always profitable to retain existing customers than acquiring new ones which is costlier than retaining a loyal customer. Existing literature indicate that the re-buy intentions of frequent air travelers are based on the satisfaction derived from the performances of both FFP and Airline Service Quality (ASQ) attributes.

The airline usage of frequent travelers is on an increase especially among business category. Many of these frequent travelers are members of frequent flyer programmes (FFP) offered by different airlines.
ASQ attributes are also influencing frequent travelers in the ultimate preference for an airline to travel. There can be variations in the passengers’ intention to continue with the same airline due to the variations perceived in FFP and ASQ attribute performances.

As per the data obtained from the official publication of the Airline Passenger Experience Association (2011), the important factors (Figure 1.3) that make the frequent flyers loyal to an airline are good customer service, opportunity to earn frequent flyer miles, onboard experience etc. However the interdependence of these factors and the degree at which these factors affect re-buy intention of various groups and contexts are yet to be investigated.

*Figure 1.3 Factors that influence frequent flyers*

![Factors that influence frequent flyers](image)

Source: www.Apex aero, Airline Passenger Experience (2011), official publication of the Airline Passenger Experience Association, Quarter IV.

Airline passengers can differ in their affinity for repeat usage of an airline for their frequent travel plans. Frequent Flyer Programme (FFP) with its variance in benefits attracts passengers to choose an airline, whereas Airline Service Quality (ASQ) attributes will also have an effect in passengers’ selection or re-buy decisions. This study is looking for the measurement of unknown interaction due
to the differences in the level of satisfactions that exhibit among airline passengers who look for service quality attributes as well as frequent-flyer attributes and the extent to which each type of attribute influence their buying intention.

This study focus on the link between satisfactions obtained from loyalty programme attributes, which are very much part of relationship marketing (Gronroos, 1993; Gwinner et al., 1998), and service quality attributes.

Therefore, understanding the joint and intervening effect of airline service quality variables and FFP variables in re-buy intentions of customers will help the airlines to formulate their plans effectively, thus increasing profitability of the operations.

1.2.2 Research Gap

Attribute-level performances of ‘Airline service quality’, ‘Frequent flyer programme’ as exogenous variables (antecedent factors) and passenger satisfactions, passenger trust and brand image as mediating variables in a single conceptual framework which will explain the effect of Airline service quality & loyalty programme satisfactions on passenger re-buy intentions is yet to be investigated according to the review of previous studies. Hence a research gap is identified in this regard and that forms the basis for the research work.

1.2.3 Statement of the Research Problem

Passengers are lured by FFPs and the quality of the service offered by various airlines which lead to severe competition in the industry. Hence, the effect of the variables such as attribute-level performances of FFP and ASQ, perceived
value, satisfaction from FFP and ASQ, passengers’ trust, and brand image of the airline on re-buy intentions calls for probing. Also, there is a need to transport the interrelationships in a single framework to have a holistic view of the effect of the variables on re-buy intentions.

1.3 Objectives of The Study

This study was designed to assess the effect of attribute-level performance of service quality and frequent flyer programmes on the re-buy intentions of airline frequent passengers and also to develop a structural model of various antecedents of re-buy intentions.

Specific Objectives

1. To find out the attribute-level performance dimensions of Airline Service Quality (ASQ) & Frequent Flyer Programmes (FFP)
2. To find out the effect of ASQ and FFP performance dimensions in the formation of airline passenger satisfactions
3. To compare the variations due to the differences in demographic profiles, status of frequent flyer programmes, years of airline travel experience etc on the satisfaction and re-buying intentions of frequent passengers
4. To assess the mediation role of ASQ and FFP driven satisfactions on re-buy intention of airline passengers
5. To study the effect of passenger’s trust on re-buy intention
6. To determine the role of brand image on re-buy intention
7. To assess the influence of perceived value on affecting passenger satisfaction levels
1.4 **Significance and Scope of The Study**

This research is significant from both an application perceptive of airline marketing management and an academic point of view. It looks for the measurement of interaction effects due to the differences in the levels of satisfaction among airline passengers with respect to service quality attributes and frequent-flyer programme attributes.

Low cost carriers are not offering full- fledged loyalty programme in India and the passengers of low cost airlines are not coming under the preview of this study as it deals with intentions of frequent passengers using Frequent Flyer membership cards only. Passengers’ with different status groups and the variations due to FFP status, if any, with respect to affinity towards an airline service was assessed in this study.

The scope of the study is limited to the frequent flyers using loyalty programme cards. Variations in the usage of FFP cards and inclinations towards loyalty programme in determining re purchase intentions with respect to the airline, in which passengers travel the most were measured. The non travel specific factors of FFP such as benefits from usage of credit cards and other partner benefits linked to the loyalty programme were not covered under the scope of this study.

The study did not focus on any airport or any airline and the variations that may arise due to the variations in the facilities provided by the airports are not coming under the scope of this study.
The place wise differences, if any, in the re-buy intention behavior of frequent flyers were not addressed as the personal data such as name and address were not requested during the time of collection of data. This enables the respondents to provide unbiased information. Moreover it cannot be assumed that the frequent flyers travel only in and around their place of residence.

1.5 Theoretical Background

According to the classic consumer behavior theory (Ajzen, 1991; Blackwell et al., 2001), the increase in the frequency and volume of transactions will be greater to the extent that consumers generate a positive attitude towards the company and its activities (Dick & Basu, 1994; Taylor & Neslin, 2005; Uncles et al., 2003). Loyalty programmes tend to attract customers who are more loyal to the firm (Dowling & Uncles, 1997; Kim, Shi, & Srinivasan, 2001; Long & Schiffman, 2000; Magi, 2003; Meyer-Waarden, 2007; Sharp & Sharp, 1997; Wright & Sparks, 1999). So the influence of loyalty programme in the re-buy intention of passengers can be postulated.

The theoretical framework proposed by Parasuraman, Zeithaml, and Berry (1988); Carman (1990); Legoherel (1998); Singh (1988); Smith et al. (1999); Zeithaml and Bitner (2000) have generally accepted that service quality determines consumers’ re-purchase intentions. Some authors argued that the influence of service quality on consumer loyalty is mediated by consumer satisfaction with the firm (Anderson & Sullivan, 1993; Cronin, Brady, & Hult, 2000; Gotlieb, Grewal, & Brown, 1994, Roest & Pieters, 1997). Thus, the quality
perceived by consumers in the service offered by a firm paves way to satisfaction with the service, which in turn determines consumers’ loyalty towards the firm.

Yang et al. (2012) found that service quality has a significant positive effect on customer value, airline image and behavioral intentions. Their study results accepted the hypothesis that customer value has a positive impact on behavioral intentions.

Bass & Wayne (1972), used Fishbein attitude model for the study of brand preference in which customers attitude towards a particular brand is based on the importance of each attribute given by the customer and their belief towards each attribute of the brand.

In the literature on service quality, a number of theoretical positions were observed aimed at defining this concept and examining its impact on consumer behavior. In this logic, the theoretical framework proposed by Parasuraman, Zeithaml, and Berry (1988) has been widely accepted and recognized, as these authors posit five factors of service quality: tangibility, reliability, response capacity, security, and empathy. Other variables taken into consideration were quality that focusing on the result and on the process (Lehtinen & Lehtinen, 1991; Parasuraman et al., 1988).

The individuals' attitudes have been included as determinants of behavior in the majority of overall models of consumer behavior (Blackwell et al., 2001; Engel, Blackwell & Miniard, 1986; Howard, 1989; Howard & Sheth, 1969), as well as in
other more specific behavior models (Ajzen & Fishbein, 1980; Bagozzi & Warshaw, 1990; Gatignon & Robertson, 1985; Schifter & Ajzen, 1985).

Attitudes are conceptualized as an overall predisposition, whether favorable or unfavorable, towards the development of certain behavior, and they are considered to be a fundamental antecedent of behavior and behavioral intention (Kalwani & Silk, 1982; Ajzen, 1991; Ajzen, 2001; Ajzen & Fishbein, 2005). The influence of attitudes has been scarcely considered in studies on customer loyalty programme. According to the classic theory on consumer behavior, the use of a loyalty programme (based on the number and volume of purchases made subject to the rules and incentives of the loyalty programme) would influence the consumer attitude towards loyalty programme.

Garbarino and Johnson (1999) demonstrated that satisfactions and trust play different roles in the prediction of the future intentions for low and high relational customers, also proved the mediation role of trust and satisfaction. It is found that trust is mediating only for high relational customers but not for low relational groups, whereas future intentions of low relational customers are driven by satisfaction.

Self-regulatory process explains consumer behavior in three parts (Chang and Wang, 2011). A brief description of the three components is:

1. The appraisal process (the evaluation of internal or situational conditions as they apply to one’s console);
2. Emotional reactions (satisfaction); and
3. Coping responses (behavior).

This research study is based on the theory of self-regulation processes which explain the concepts; appraisal processes that lead to emotional reactions, which subsequently lead to coping responses (behavior). The cognitive evaluations in this model are similar to the service quality and customer perceived value of products as propounded by Bagozzi (1992) in his Theory of Self Regulation (TSR).

1.6 Expected Contributions from the Study

Contributions from the findings are important due to the following four reasons:

1. It focuses on airline loyalty programme, a tool that is used extensively in airline marketing, which is under researched.
2. It considers re-buy intention behavior of frequent passengers who use airline frequent flyer programme taken as dependent variable, a factor that has scarcely been observed in airline literature.
3. It examines the influence of explanatory variables linked to passenger perception of airline service quality, attitude of airline passengers toward loyalty programme, mediation roles of satisfactions, brand image and trust.
(4) It examines the role of passengers’ perceived value about airline, and its effect on 'loyalty programme – service quality' satisfaction link which in turn influence passengers to re-buy the airline for future travel.

The findings of this study will provide better understanding of the influence of airline service quality as well as frequent flyer programme attribute dimensions on making re-buy intentions of airline frequent passengers. This study will facilitate airlines managers (or similar service providers who use loyalty programme) to better understand the management and control of the major attribute dimensions perceived by the consumers. It will help managers in focusing more attention to those performing attributes thereby enhancing efficiency. This study will flip some insight in the measurement and understanding of the effect of satisfactions derived from both ASQ and FFP attribute-level performances in the re-buy intention of frequent passengers. This study provides the effect of perceived value in moderating the relationship between satisfaction and re-buy intention. The study findings would aid airline marketers to understand the coincident effect of FFP and ASQ satisfaction in making re-buy intentions of airline frequent passengers while considering the difference in FFP status and travel experience level of passengers.

1.7 Organization of the Study

This study is organized into two parts with seven chapters.

Part one consists of four chapters. First chapter deals with introduction of the topic, about airline frequent flyer programme, airline service quality,
background of research problem, problem statement, objectives, significance, scope of the study, the theoretical foundation and the expected contribution from the study. Chapter two gives a detailed review of literature relevant to the variables considered in this study linking different constructs depicted in the conceptual frame work of the study. Conclusive observations based on the review of literature and plausible research gaps and the subsequent formation of the research problem are provided at the end of this Chapter. Chapter three deals with research methodology covering details regarding research design, the conceptual model based on literature review, survey instruments for data collection, scales used for measurement of constructs, operational definition of constructs, validity of scales/ instruments used for the study, hypotheses of the study, population of the study, sampling design and its method and estimation of sample size. Fourth chapter deals with factor analysis of data for exploring sub dimensions of exogenous variables and its validation using Confirmatory Factor Analysis (CFA).

Part two consists of remaining three chapters, under which chapter five deals with analysis of the data with descriptive statistics of the sample, testing of hypotheses, test of mediation, moderation and also the structural equation model with its output results. Chapter six is wrapped up with the discussion of the findings and interpretation of results in tune with the research problem of the study. Chapter seven deals with the conclusion, implications for the airlines, limitations and scope for further research.