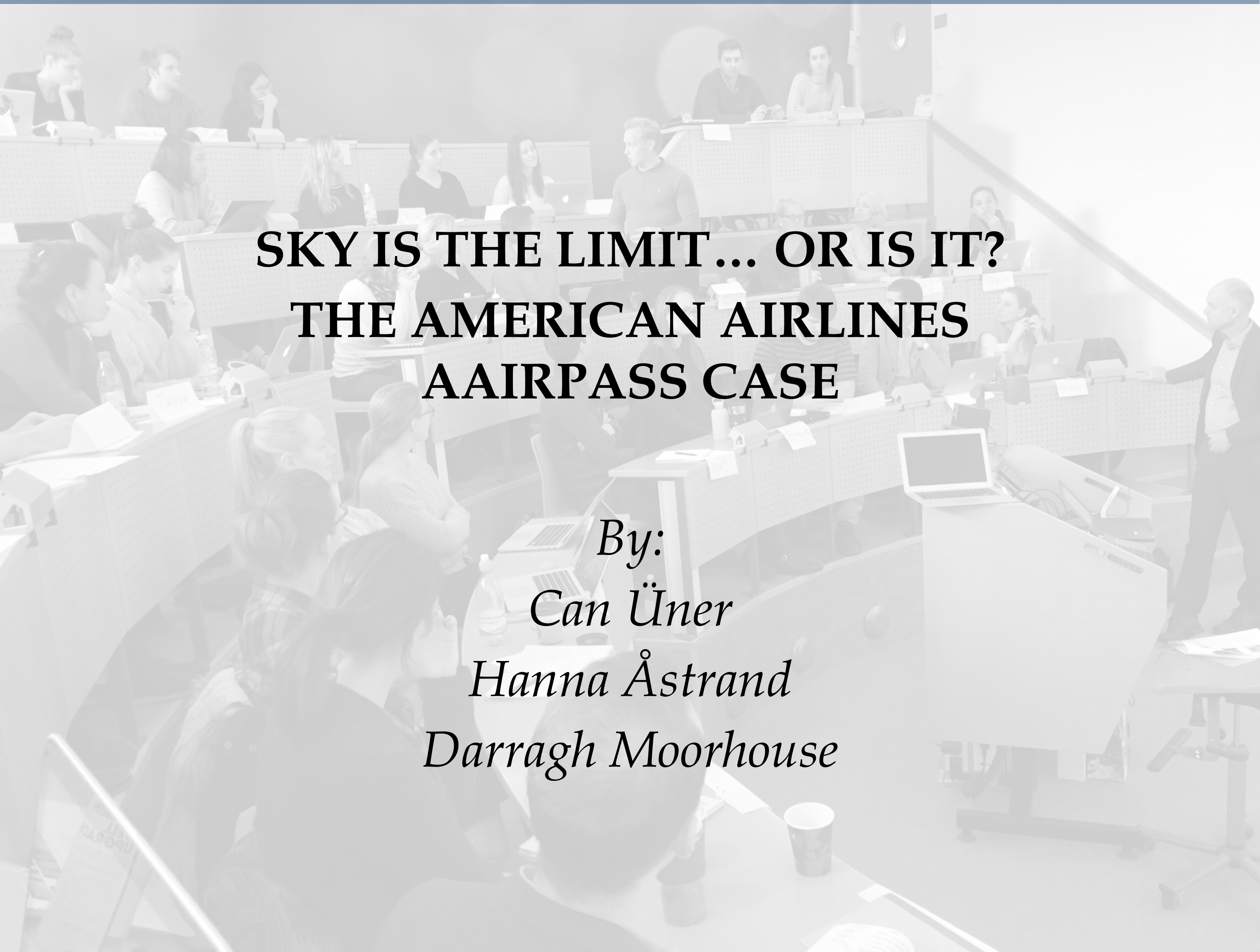
CORPORATE BRAND MANAGEMENT AND REPUTATION

MASTER CASES



SKY IS THE LIMIT… OR IS IT? THE AMERICAN AIRLINES AAIRPASS CASE

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Corporate Brand Management and Reputation: Master's Cases

The "Corporate Brand Management and Reputation: Master's cases" is a case series for applying the case method of teaching and learning in higher education. The cases are relevant to brand strategists in private and public sector organizations, as well as academics and students at universities, business schools, and executive education.

The cases are written by groups of master's students as a course project. The specially developed case format is defined as: *"A management decision case describes a real business situation leading up to a question(s) that requires assessment, analysis, and a decision reached by discussion in class. The alternative approaches and recommendations from the class discussion are followed by a description of the choices made by the case company. This description is then discussed by the class."*

The student groups select the topics of their case providing updated and relevant insights into the corporate brand management. The cases can be used as "written cases" (handed out and read in advance, later to be discussed in class) and/or as "live case" (presented by the teacher following a discussion in class). Each case includes teaching notes, visuals with speaker's notes, learning objectives, board plans, and references.

The mission of the series is *"to develop cases for discussion providing insights into the theory and practice of corporate brand management and reputation, with the intent of bridging the gap between academic teaching and managerial practice."*

The series is a result of co-creation between students and teachers at the elective course Corporate Brand Management (BUSN35 – five-credit course/eight-week half-time studies), part of the master's program International Marketing and Brand Management at Lund School of Economics and Management, Sweden. The cases represent the result of the intellectual work of students under the supervision of the head of course.

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Sky is the limit… or is it?
The American Airlines AAirpass Case

WRITTEN CASE

MANAGEMENT DECISION CASE

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Unlimited Flights to Financial Ruin: The American Airlines AAirpass Debacle

Picture this: it's the early 1980s, and air travel is booming. Business travellers are taking to the skies like never before, and airlines are competing fiercely for their attention. But amidst this battle for customers, one airline dared to do something bold, something that would change the game forever. American Airlines launched the AAirpass program, a revolutionary concept that offered wealthy individuals the chance to fly first-class, anytime, anywhere, for the rest of their lives - for a cool $250,000. The AAirpass was more than just a ticket - it was a status symbol, a statement of wealth and privilege, and it would soon become the stuff of legend. Nowadays, the American Airlines Airpass is known as an all-inclusive membership program that offers elite status, flight discounts, and other perks, for an annual fee. However, high-flying dreams turned into nightmares and in this case, we will discuss how one of the oldest airlines in the world came up with the idea that unlimited first class became a costly mistake.

Background and History

American Airlines was founded in 1926 by a group of investors, including Charles A. Lindbergh and the CEO of Robertson Aircraft Corporation, the predecessor company to American Airlines. The company was originally known as American Airways, known as a mail carrier, and operated a route between St. Louis and Chicago. American Airlines is one of the oldest and largest airlines in the world. In the early years, American Airways faced stiff competition from other airlines, as well as the challenge of operating in a nascent industry with limited infrastructure. To expand its operations, the company acquired several smaller airlines, including Universal Aviation Corporation and Colonial Air Transport.

By the mid-1930s, American Airways was operating a network of routes across the United States. In 1934, the U.S. government passed the Air Mail Act, which allowed the Post Office to contract with private airlines to carry mail. This led to a boom in the airline industry, as airlines competed for lucrative mail contracts. American Airways was one of the companies that benefitted from this, winning several key mail routes and expanding its operations even further. Again in the same year, the company changed its name to American Airlines, reflecting its focus on passenger service as well as mail delivery.

There had been another development in 1934, American Airlines became the first airline to offer scheduled passenger service with an all-metal aircraft, the Douglas DC-3. This new aircraft was faster, more comfortable, and more reliable than previous aircraft, and helped American Airlines to establish itself as a leader in the industry. Over the years, the airline continued to expand its operations, introducing passenger service and new innovations improve the flying experience for its customers in 1936 and growing steadily to become one of the largest airlines in the world. Today, the company is still one of the most recognized airlines in the world.

In the 1950s and 1960s, American Airlines was a pioneer in many aspects of air travel to improve the passenger experience such as; in-flight movies, expanded meal service, and the first airport lounges. In 1953, American Airlines introduced the first coast-to-coast jet service in the United States, using the Boeing 707. This allowed passengers to fly from New York to Los Angeles in just over five hours, compared to more than 15 hours on a propeller-driven plane. In general, American Airlines was known for its commitment to innovation and technology during this period, which helped to improve the speed, comfort, and convenience of air travel for customers.

By the 1970s, American Airlines was facing stiff competition from other airlines, as well as pressure from rising fuel prices and the economic downturn of the era. In 1978, the Airline Deregulation Act was passed, which removed government control over airline routes and fares, allowing airlines to compete more freely. This led to a wave of consolidation and restructuring in the industry, with many airlines struggling to adapt to the changing landscape. Throughout its history, American Airlines has been recognized for its commitment to customer service and safety. The airline has won numerous awards for its in-flight amenities, airport lounges, and overall experience. Today, American Airlines is one of the largest airlines in the world, serving more than 350 destinations in over 50 countries. In the 1970s and 1980s, the airline faced intense competition from other carriers, particularly in the lucrative business travel market. To differentiate itself and retain high-value customers, American Airlines began to offer new and innovative products and services, such as the AAdvantage frequent flyer program and new airport lounges.

American Airlines Organizational Structure & Business Model

Before the deregulation of the airline industry in the late 1970s, American Airlines' business model was somewhat different from what it is today. Prior to 1980, American Airlines had a relatively traditional organizational structure, with a hierarchy of executives and managers overseeing various departments and functions. The company was led by a CEO, who oversaw a group of senior vice presidents responsible for areas such as finance, marketing, operations, and customer service.

One notable acquisition that American Airlines made prior to the 1980s was the purchase of Air California in 1979. This acquisition gave American Airlines a larger presence on the West Coast of the United States, as well as access to new routes and markets. Air California was later rebranded as American West, and the airline continued to operate under that name until it was merged with US Airways in the late 1990s.

After the 1980s, American Airlines continued to make a number of acquisitions over the years, as well as partnerships and alliances with other airlines (such as British Airways, Iberia, Japan Airlines, and Finnair) in an effort to expand its reach and market share. These moves were part of the company's larger strategy to grow and evolve with the changing airline industry, and they helped to establish American Airlines as one of the major players in the global aviation market.

The 1980s and the Aviation Industry

In the early 1980s, American Airlines began to face increased competition from other carriers, particularly in the lucrative business travel market. To differentiate itself and retain high-value customers, the airline began to offer new and innovative products and services, including new airport lounges and the AAirpass program. In an attempt to raise some badly needed funds quickly, the airline sold this unlimited first-class product as either a five-year or lifetime pass. The decision for an unlimited AAirpass came about after the airline posted a US$76 million loss in 1980. This was due to the 1978 Airline Deregulation Act, which had the effect of bringing about new competition and reduced ticket prices.

Prior to the Deregulation in 1978, the US government heavily regulated the airline industry by controlling routes, fares, and other aspects of airline operations. However, with the Airline Deregulation Act of 1978, the government eliminated many of these regulations, allowing airlines to operate more freely. This led to increased competition and lower fares, but also made it more challenging for airlines to maintain profitability. By 1980, the Civil Aeronautics Board reported that the number of US airlines had increased by 35%, and the number of passengers had grown by 25%, compared to 1978. As a result of deregulation, new airlines began to enter the market and existing airlines faced increased competition. American Airlines was one of several major carriers, including United and Delta, that competed for market share and high-value customers. There are also other key developments in the aviation industry from the early 1980s that influenced the launch of the program.

In the early 1980s, the number of business travellers increased significantly as companies expanded their operations and began to do more business internationally. According to data from the US Department of Transportation, the number of domestic business trips in the US increased from 81 million in 1980 to 111 million in 1985, a growth rate of nearly 40%. International business travel also increased during this time, with the number of US-originating trips to Europe growing from 2.5 million in 1980 to 3.5 million in 1985.

Airlines began to invest in new technology and marketing initiatives to improve the passenger experience and differentiate themselves from competitors. For example, the American Airlines AAdvantage program, which launched in 1981, was the first frequent flyer program in the industry. The program allowed passengers to earn miles for flights, which they could then redeem for free flights, upgrades, and other rewards. By 1982, the program had over 2 million members. Other airlines followed suit with their own loyalty programs. Additionally, airlines began to invest in new technology, such as computer reservation systems and in-flight entertainment systems. By the mid-1980s, over 80% of all US travel agencies were using computer reservation systems, which made it easier for customers to book flights and travel packages.

Overall, the early 1980s were a time of significant change and innovation in the airline industry. Deregulation led to increased competition and lower fares, while the growth in business travel and innovations in technology and marketing created new opportunities and challenges for airlines. The AAirpass program was one example of how American Airlines sought to differentiate itself and capture a share of this changing market.

Incident

The Golden Idea

In this critical time, one of the ideas to save the company was to offer an unlimited lifetime air pass in first class. A smart, attractive idea and good marketing, there is always seating so one more passenger will not be a problem. Remember flying in the 80s, when the pass first was offered, cost a lot more than today. Adjusted for inflation, the cost of flying today is about 50% less than it was in 1980.

When the air pass was first offered in 1981 it was at the cost of $250 000, plus an additional $150 000 for a companion pass. This companion pass was not locked to one other specific person, the pass holder could bring a new companion every flight if one wished. Thus, the total sum for the AAirpass and the companion pass was $400 000, which equals a total amount of $1.3 million in 2023. The deal gave the traveller “free”, or at least unlimited, first-class travel to anywhere in the world, on any American Airlines flight, for the rest of his life. And if that was not enough, the deal included the most luxurious air travel service one could possibly get at the time: access to the faster queue, the highly desirable Admirals Club, VIP lounges, and private booking agents. These booking agents solved any flights for the pass holders, even the toughest booking puzzles, for example, last-minute bookings during festival seasons, or the only plane leaving during a snowstorm. In other words, quite a unique possibility for the multi travellers. AA targeted constantly flying high-end businessmen and marketed the AAirpass as paid off in only one year. In the first year, 28 people signed up. In the following years, more people found the offer and in total 66 people bought the AAirpass. At the moment, the purchases gave AA better cash flow but in the long run, it did not help them overcome the financial crisis. Too soon they realized they undercharged it since more people than they imagined jumped at the deal. In fact, they came to realize it was a terrible deal they had created.

The Loophole Searchers

The plan was that the deal would work similarly to an all-you-can-eat buffet, where very few eat the value they paid. In theory, it would be possible to sit down and have 20 steaks, but that is almost non-existing in reality. For AA, the problem was the super travellers who travelled way more than the airline had anticipated. Unlike at the buffet, it became clear that a few of these super travellers found ways to overuse the scheme which caused AA a huge loss. Three of the problematic super travellers were Mike Joyce, Steve Rothstein, and Jaques Vroom. For example, Joyce flew 16 round trips from Chicago to London in 25 days. Rothstein, who bought the pass in 87, used his pass to book more than 10 000 flights in the following 21 years, more than a flight per day. Rothstein flew from Chicago to London for lunch, back to Boston for a baseball game, and then home to Chicago for dinner. Sometimes he used his pass to fly to Rhode Island, only to grab his favourite sandwich, and then fly return. The third pass holder mentioned above, Vroom, would fly out to pick up his father to come and babysit for a few hours because the companion pass was cheaper than paying a local teenager. He also helped fly home AIDS victims to see their families. Between the years 1990 and 2008, he flew 38 million miles or 61 million km, which means 2 million miles or 3 million km per year. That is 75 laps around the globe per year.

Gold Can Turn To Sand

In itself, no oversteps had been made by the super travellers. The biggest problem was the amount of booked flights the super travellers made for backup plans, such as if the weather turned bad or the weekend plans got cancelled, never having to worry about any cancellation fees. With the private booking agent, it was not a difficult job either. What caused the most trouble for AA was the bookings made but not flown on since AA was still responsible for taxes of them, $491 per ticket, and not seldomly with a companion. Obviously, something had to be done. Unfortunately, the actions were not against any terms or conditions of the scheme. Yes, the pass holders were abusing their privilege but they had spent hundreds of thousands of dollars for it. Imagine a pass holder making 3 alternative bookings for a weekend, and not he nor the companion would use any of them in the end, that would leave AA with a loss of almost $3000. AA estimated that each of these super travellers was costing them over $1 million per year. Rothstein had in the first 4 years made 3009 reservations, almost always with 2 seats, but cancelled 2523 of them. Many times, these bookings were cancelled at the last minute and the cancelled seats either went un-used or lower class passengers were given free upgrades. Further on, Rothstein and some other super travellers often helped strangers out, offering them a first-class ticket or helping them get home if their flights were cancelled. Normally this would not be a problem but the cardholders booked under fake names, such as Bag Rothstein, since they didn't yet know who they would bring. These so-called "speculative bookings" under made-up names were for a companion they had no intention of travelling with, for example, Mr Bag Rothstein. The pass holder would then check in himself and thereafter cancel the intended companion's booking, the one with a fake name, only to be reinstated to accommodate a different companion, who already possessed paid-for coach seats on the very same American flights. In this way, the new companion got a free upgrade to first class, and the pass holder supposedly felt that he acted like a fellowman. In 2008 Rothstein had travelled over 16 million km or 10 million miles, which equals 20 travels to the moon and back.

The Airpass' Last Breath

During the following decade, AA tried to save themselves from the worst miss calculations by increasing the membership fees of the Unlimited AAirpass. The price, not including companion, went from $250k in the release year 1981 ($900k in 2023) to $600k in 1990 ($1.4m in 2023) and then increased further to $1.01m in 1993 ($2m in 2023). Already the year thereafter, in 1994, AA completely stopped selling the pass. One last attempt with the air pass was made in 2004, this time the price was $3m ($4.7m in 2023), plus the additional companion pass for another $2m. In today's value, that's a total of $7.8 million. This time there were zero takers. For that cost, you might just as well buy your own plane.

There was a new financial crisis in 2008. By now, AA had spent more than $40m in total to provide first-class flights to these two pass holders, Rothstein and Vroom, and their companions only. Other users weren't too far behind either, they all wrapped up miles far beyond what the airline had anticipated.

Management Question

Taking on the role of the Executive Board for American Airlines, how would you answer the following Management Questions:

- ***How would you rectify the situation having launched the AAirpass system two years previous and discovered it is not profitable?***

- ***How do you think the AAirpass offering would unfold in the 21st century in the context of corporate reputation?***