

Revenue Optimization Primer: Airport Concessions by Alex Hopson, Associate

Revenue Optimization within airport concessions programs is an integral part of a comprehensive revenue management program. Now that domestic airports are in the third generation of airport concessions models, most airports already employ concessions professionals to administer their non-aeronautical revenue market sector.

These professionals have generally honed their concessions programs to be business-centric revenue centers, as opposed to purely incidental monies as in years past. But now that robust concessions programs have been established, how do concessions professionals know if they are reaching their full revenue potential? A majority of airports measure concessions success in terms of whether the program meets a sales goal or rent payment level. However, many airports base their current and future goals solely on prior years' performance. This approach does not take into account the possibility of a location or an entire sector within a concessions program that may be chronically and/or systemically under-performing, or paying insufficient rent. The airport may simply be perpetuating the same inadequate goals year after year. Airports need to employ a system of revenue management that incorporates Revenue Optimization as a critical component.

Definition of "Revenue Optimization"

Revenue Optimization is the application of disciplined analytics that predict consumer behavior, provides the proper product/service at the correct location at the optimal time with

appropriate prices to maximize revenue growth. At the heart of Revenue Optimization is understanding customers' perception of product/service value and accurately aligning product/service prices, placement, and availability within each customer segment. Please note that the "customer" within the airport environment goes beyond the traditional notion of the air-travelling public and must include employees and all potential airport concessions patrons.

Revenue Optimization can result in increases in top-line, gross concessions revenues of between 3% - 20% of existing programs.

Revenue Optimization as Problem Solving

Revenue Optimization involves solving two

important problems in order to achieve the highest possible revenue. The first is determining which objective functions to optimize. An airport must prioritize the optimizing of prices, total sales, and percentage rent payments, as well as such non-tangible functions of customer loyalty and goodwill, etc. Secondly, the airport must decide which optimization technique to utilize. Most airports utilize consultant firms for the large scale number-crunching and statistical optimization. For example, consultant firms generally utilize a combination of various forms of linear programming, or more complex methodologies such as regression analysis (a statistical tool that seeks to find the ideal relationship between several variables through complex models and analysis) for determining the best outcome from a set of relationships and to optimize performance and maximize revenue. Lastly, *discrete choice models* can serve to predict customer behavior in order to target them with the right products/services for the

right price., according to R. Phillips in the 2005 Stanford Business Book *Pricing and Revenue Optimization*.

Within these optimization models, consulting firms will evaluate the viability of the following:

- Any master concessions plans,
- the individual lease terms of all the concessions,
- the operational floor-plans and areas devoted to concessions,
- total airport traffic,
- flight schedules,
- demographics of customers within specific areas of the airport terminal(s),
- historical gross revenues,
- airport rent payments,
- product service/price points, and
- concessions categories and the concessions concepts within each category.

Additional Factors to Incorporate

With the exception of airports operating on a developer model, Revenue Optimization should be performed by airports upon their concessions programs inclusive of direct leases, prime operators, multiple prime operators, master concessionaires, etc. Often airports will rely upon the expertise of their concessions operators, and may falsely believe that the concessionaires are constantly striving to do everything within their power to grow the concessions revenue beyond the MAG payment level. Unfortunately, while many operators do optimize their programs, their priorities may

not be in sync with those of the airport. For instance, prime operators will often push their contractual limit on product pricing because they have selected gross revenue return as their highest and/or sole priority during their internal optimization evaluation. Municipal and State-administered airports have priorities that must take into account other considerations, which may not always be aligned with a prime operator's priorities.

Concessions operators are generally receptive to airport optimization analysis, but implementing post-analysis techniques into existing contractual constructs may require the assistance of professional aviation consultants. Ideally, revenue optimization procedures may be written into contracts at the time of issuing an RFP, but airports should not be dissuaded to wait until an existing contract expires to perform a Revenue Optimization analysis study.

Results: Increases Up to 20%

By continuing to utilize Revenue Optimization processes, airports may expect increases in top-line, gross concessions revenues of between 3%-20% of their existing programs. Revenue Optimization techniques will demonstrate enhanced concept variety and placement, customer attraction, product and services offerings, accuracy in inventory levels, and pricing points in order to achieve the highest revenue possible. Established airport concessions programs can benefit from an inclusion of their non-aeronautical revenue business centers and should actively pursue enhanced concessions performance through revenue optimization.

Steven Baldwin Associates focuses solely on airport management consulting for airport operators, owners, and policy makers. As a leader in developing best practices in contemporary airport management, the principal and associates at SBA have decades of hands-on experience running airports and consulting for them. *For more information, contact us at info@baldwinllc.com or visit our website at <http://www.baldwinllc.com>.*