



Willingness to pay for airlines' premium economy class: The perspective of passengers



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ABSTRACT

This study investigates how much extra air travellers are willing to pay to upgrade to premium economy class by using a suitable econometric model. Since a large portion of travellers' willingness to pay for premium economy class is zero, the spike model is applied to overcome the issues that may occur when traditional statistical models are used. Three flight distances, short, medium, and long hauls were separately estimated to investigate the effects of flight distance on willingness to pay. Travellers' willingness to pay to upgrade from economy class to premium economy class round-trip was US\$138¹, US\$309, and US\$545 for short-, medium-, and long-haul, respectively. The research results should be a helpful reference for the civil aviation industry in strategic pricing planning.

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1. Introduction

Although in recent years, the economic downturn has lingered and the growth of international travel has slowed, the [World Tourism Organization \(2012\)](#) reports a growth of 3–4% in the number of travellers worldwide. With both higher knowledge levels and an increase in consumer awareness, people not only value leisure activities more but also ask for more in terms of service. People not only request sophisticated services but also hope for greater selection. However, in light of high fuel prices and a period of low-profit operation, competition in the airline industry has become increasingly fierce. To offer travellers a better flight environment and attract more travellers of all types, airline services are becoming more sophisticated and diversified.

Some airlines strive to bring elements of business-class service to economy class by offering not only service upgrades and innovations but also diversified premium economy class services as additional choices to meet travellers' needs. By providing more comprehensive and diversified services, airlines hope that travellers not only will perceive a high level of added value but will also establish loyalty. In the current economic-downturn environment, the concept of premium economy class service also offers travellers

who once travelled in business class an alternative to economy-class travel while still cutting costs. Conversely, this design offers a new option to economy-class travellers who are willing to pay extra to enjoy higher-level services. [Lee and Luengo-Prado \(2004\)](#) found that United's Premium Economy program helped it boost its average fare, while it was also effective in attracting passengers willing to pay higher fares for greater seat pitch. [Doganis \(2010\)](#) indicates that the premium economy class will be a successful and profitability cabin. [Cindy and O'Connell \(2015\)](#) even think that premium economy class cabins could very well become an embedded and sustainable product long haul travel in the near future. Accordingly, offering premium economy class not only provides airlines with self-competitiveness but can also sustainably enhance airlines' load factors and profitability.

In 1992, EVA Air was one of the world's first carriers to introduce a premium economy class. Premium economy class is a civil aviation service class that is higher than economy class but lower than business class. Different airlines have different names for premium economy class. For example, Eva Air calls its premium economy class Elite Class or Evergreen Deluxe Class. China Airlines calls its premium economy class Economy Extra. In terms of costs, business class fares are much higher than economy class fares. However, in Taiwan, premium economy class fares can be found on various travel websites and are usually approximately 10%–30% higher than economy class, proportional to travel distance. In addition, long-haul flight travellers hate cramped seats the most because such seats always cause discomfort during the travel. However,

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¹ 1 US\$ = 31.77 NT\$ at the time of study.

premium economy class offers relatively new equipment and more satisfying services, such as greatly expanded personal space (including seat width and seat pitch), premium personal necessities, and higher service levels than in economy class.

Premium economy class even relaxes limits on checked baggage. Travellers therefore experience a fairly comfortable seating environment and sophisticated services even during a long-haul flight. In addition, the primary reason for airlines to introduce a premium economy class different from economy and business class is to attract travellers who enjoy services better than those in economy class but are not willing to pay business-class fares. The trend of offering a premium economy class indicates that some airlines have already sensed that offering this type of premium class service will enhance their business strategy of improving occupancy rates. Hugon-Duprat and O'Connell (2015)'s findings show that implementing a premium economy seat only 1.6 times more expensive than an economy seat to produce, but it generates revenues that are 2.3 times higher than its cost of production. The trend also indicates that there is room for further development of premium economy class services.

However, in the existing literature, most of the discussions are on environmental issues (Lu and Shon, 2012; Haggmann et al., 2015), service quality issues (Zhang, 2012), and WTP issues which are not relevant to the WTP of premium economy class (Chang and Sun, 2012; Balcombe et al., 2009). It is therefore important for the aviation industry to understand the factors that affect travellers' choice of premium economy class and how much travellers are willing to pay, which are crucial topics in promotions of premium economy class. In addition, since approximately 44.8% of short-haul travellers, 31.3% of medium-haul travellers, and 29.9% of long-haul travellers, respectively, were not willing to pay extra for premium economy class, this study used the spike model to avoid estimation bias and thus provide a more realistic result.

This study mainly hope to understand how much air travellers are willing to pay to upgrade from economy to premium economy class. Because travellers' choice of airline cabin class is a reflection of a choice behaviour based on their perceptions of cabin service, the economic value of that service cannot be measured in monetary terms. From an economic point of view, service content is in the nature of non-market goods. One widely used approach for assessing non-market goods is the Contingent Value Method (CVM), which has an advantage in assessing the value of nonmarket goods in the conversion of the value of goods, primarily through surveys or similar interview methods. CVM asks respondents to subjectively determine the dollar value of non-market goods, and determines what maximum sum the respondents would be willing to pay for a given good. The value of willingness to pay (WTP) for the individual is elicited from answers to hypothetical questions in the survey. As a result, this study is based on random utility theory, combined with CVM, to establish a virtual market for travellers were willing to pay extra to upgrade to premium economy class under different pricing scenarios.

In the survey conducted for this study, approximately 44.8% of short-haul travellers, 31.3% of medium-haul travellers, and 29.9% of long-haul travellers, respectively, were not willing to pay extra for premium economy class. As a result, this study also used the spike model to avoid estimation bias and thus provide a more realistic result. In addition, previous research indicates that there are significant differences in WTP among travellers with different travel distances (Jou et al., 2013b). Espino et al. (2008) also stated that travellers were willing to pay more than the basic fare for additional legroom for this short haul flight, they even prepared to pay significantly more on long-haul travel. Thus, this study also aims to understand whether travel distance has any impact on travellers' choice of premium economy class and their WTP. Therefore, the

length of flight time was included in this study's analysis and investigation.

2. Literature review

Airlines offer a Premium Economy class to passengers willing to pay more for slightly better seats and, in some cases, better service. However, whether the public can accept premium economy class and the price the public is willing to pay for that class are important aviation topics that are worth discussion. Because participants' WTP can be zero, most research worldwide uses the spike model to overcome the problem of finding zero WTP. Based on research using the spike model, Jou et al. (2013c) investigate the public's future choice behaviour in the business cabin of high-speed rail and the price the public is willing to pay when services are added to those currently offered in the business cabin. This research uses the stated preference method (SP) to design a double-bounded dichotomous choice questionnaire for the survey. The spike model is used to resolve the problem of finding zero WTP in the binary choice estimation. The results indicate that fare is the primary factor that has an impact on high-speed rail travellers' choice to travel in the business cabin. Long-haul travellers are more concerned about the level of tranquillity and services in the business cabin, whereas short-haul travellers consider whether they can afford to pay the business cabin fare. In addition, Internet connection in the business cabin tends to attract potential customers who have a college education or higher.

Jou and Wang, (2013a) study focuses on Taiwanese drivers' WTP for moving violations such as speeding, running a red light, making a right turn on a red light, and driving under the influence. In their model estimation, they use the logit binary probabilistic model, along with the spike model that can handle zero WTP while minimising bias resulting from too many zero WTP responses. Model estimation results indicate that drivers' WTP is US\$23 for speeding, US\$4 for running a red light, US\$12 for making a right turn on a red light, and US\$584 for driving under the influence. Research results also indicate that the current minimum penalty for speeding is lower than the price drivers are willing to pay. In other words, the speeding penalty is not high enough to have any deterrent effect. According to Jou et al. (2013b), because Taiwan's electronic toll-collection pricing system and on-board unit (OBU) price are not determined by market supply and demand, the actual price that users are willing to pay cannot be determined. In addition, considering the possibilities of calibration bias due to high zero WTP, the spike model is used to estimate the price that freeway users are willing to pay for OBU and distance-based tolls for different travel distances. The results indicate that drivers are willing to pay US\$23, US\$26 and US\$41/OBU for short-, medium-, and long-haul travel on freeways, respectively, based on freeway distance segmentations. For short- and medium-haul drivers, because there remains a gap in the current fares, Jou et al. (2012) suggest offering a discount program. In addition, drivers' distance-based WTP is 0.81, 0.943, and 0.97/km for short-, medium-, and long-haul drivers, respectively, indicating that short-haul users' WTP is relatively lower. The results the study suggest implementing a distance-based, toll-differential pricing strategy. To alleviate the strong opposition to distance-based tolls from short-haul freeway drivers, the government can establish a distance threshold under which drivers need not pay any toll.

Focusing on related research in other countries, Kriström's (1997) two studies are the earliest to use spike models. The first study investigates the possible ferry-traffic damage caused by a Finland ferry carrying large number of passengers to and from the Stockholm archipelago. The study asked how much participants would be willing to donate per year to change the ferry's navigation

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