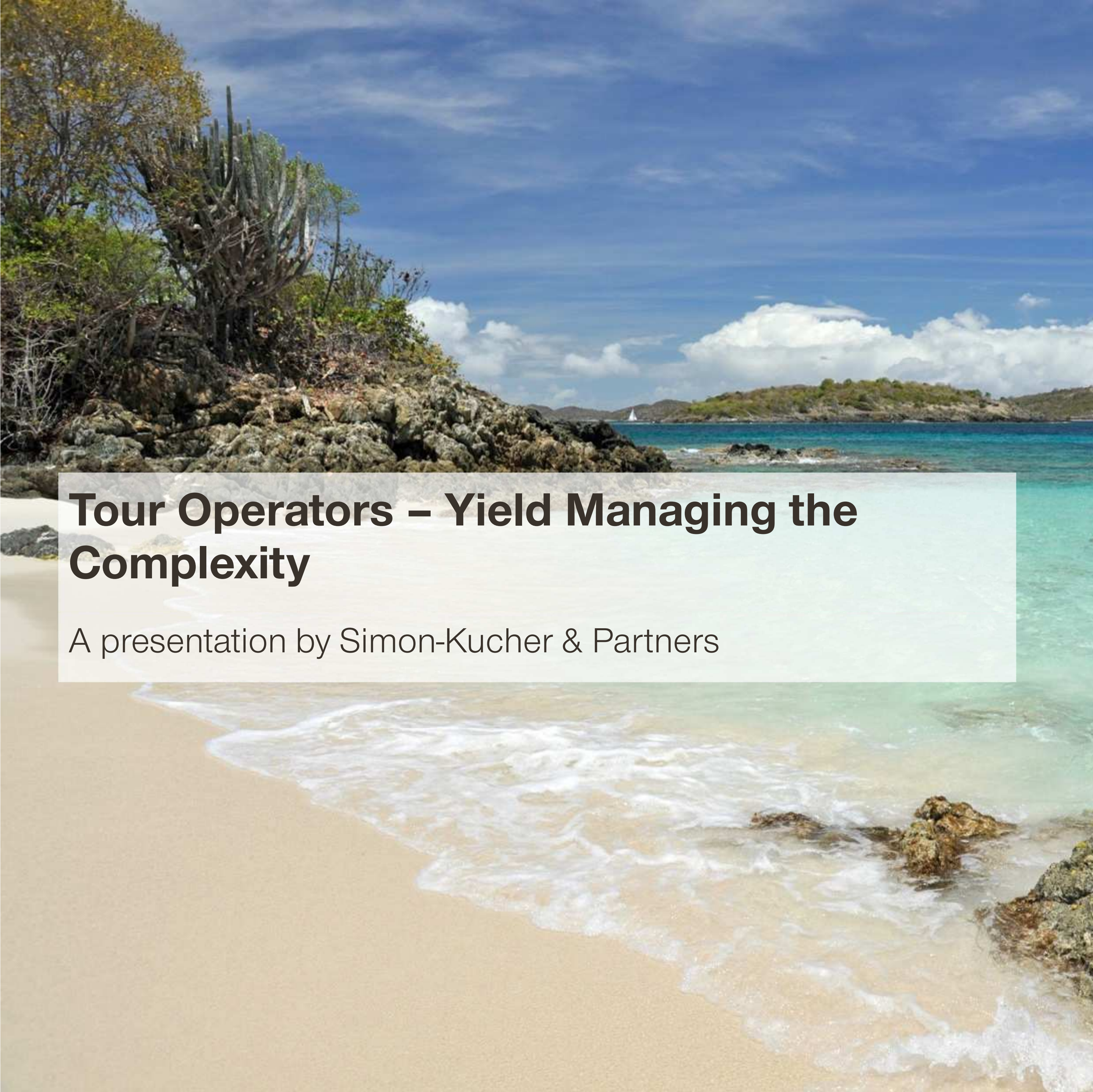

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Strategy & Marketing Consultants

30 years

Tour Operators – Yield Managing the Complexity

A presentation by Simon-Kucher & Partners

London, 7th June 2016

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Source: Simon-Kucher

Agenda

- **About Simon-Kucher & Partners**
- Unique features of Tour Operators
- A step by step guide to yield management for TOs
- Key takeaways
- Q & A

Simon-Kucher is the world's leading pricing adviser

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Strategy > 400

Marketing > 500

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- Pricing strategies and processes
- Product-portfolio (re-)design
- Growth and competitive strategies
- Sales strategies and sales channel optimisation

*Source: German manager-magazin Aug 2007 & 2011 / Institute für Management und Beratung; Survey among 264 top-managers; Maximum 500 points

Relevant project topics in Travel & Hospitality

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Hotel chains

B2B negotiations and rate design

Revenue management

Channel strategy

Product strategy

Sales dialogue (product portfolio)

Up-sell and bundling

Tour operators

Product strategy

Dynamic packaging

Initial pricing

Revenue management

Channel strategy

Discounting strategy

Capacity management

Airlines

Product strategy

Sales dialogue (product portfolio)

Revenue management

Channel strategy

Discounting strategy

Others

Airports (retail, fees & car parks)

Car rental

Coach operators

Train operators

Travel agents

Online travel agents

B2B services within travel

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When I try to explain Revenue Management to a normal human being...

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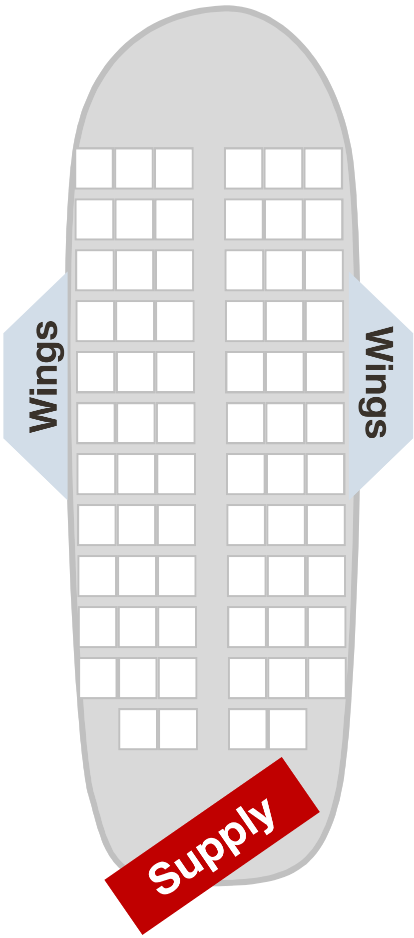
I have a plane with 120 seats that has to depart on the 10th July @ 09:00



...and I know how much I will sell at different price points

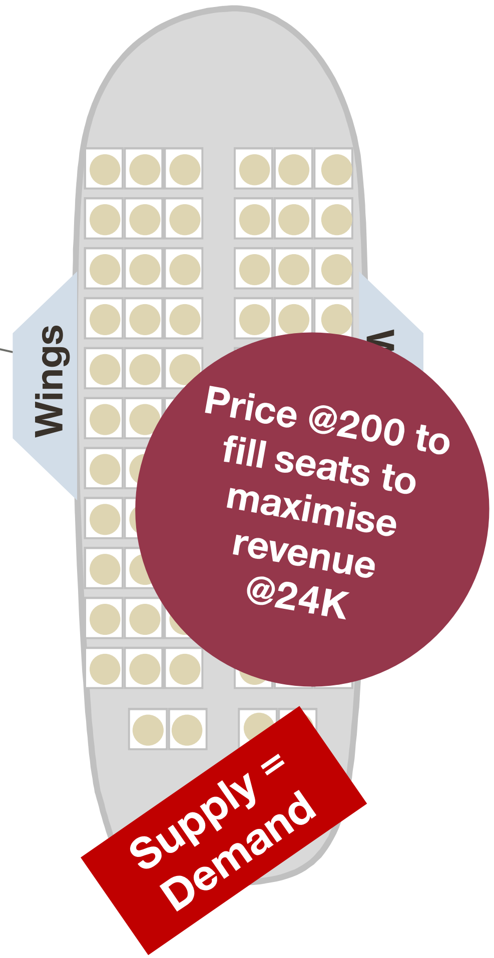
@ £	Seats booked
£240	80
£220	100
£200	120
£180	140
£160	160
£140	180
£120	200
£100	220

Lower revenue so not worth leaving empty seats

Higher revenue but capacity not there

Demand

I combine supply & demand to find revenue optimal price



For tour operators it becomes a bit more complex as multiple dimensions need to be managed in parallel

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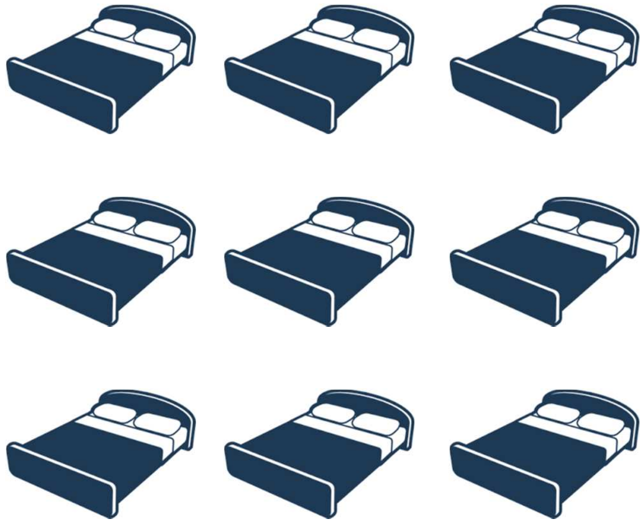
An airline has to RM each flight

LGW-PMI @ 09:00

- In simplest terms, airlines will have to **maximise revenue** for each **flight's capacity**
- ...some interdepencies exist between flights (e.g. returns) and connecting routes

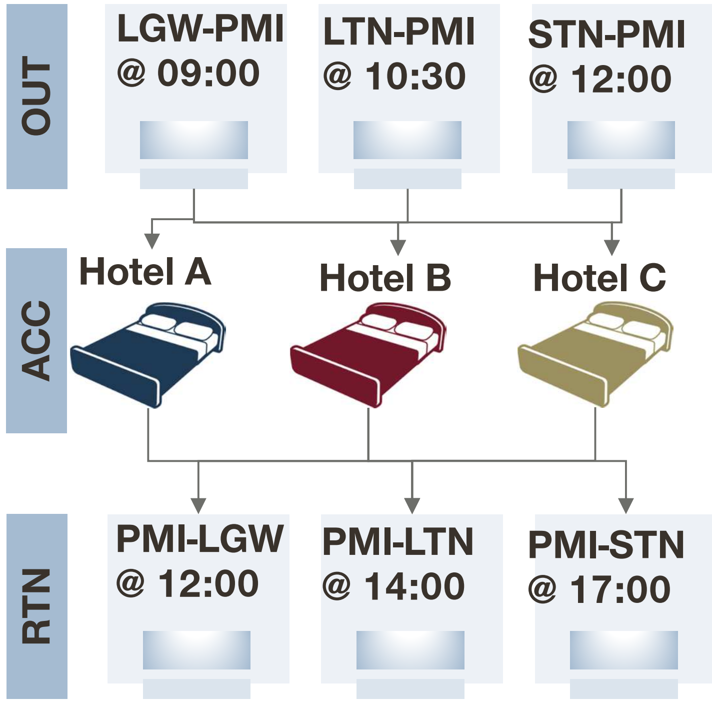
A hotelier has to RM each stay-night



Majorca 4* Santa Lucia Hotel

- In simplest terms, hotels will try to RM to **maximise revenue** for each **stay-night's capacity**
- ...interdependencies exist, as customers book specific durations (length of stay)

A tour op has 3 dimensions to RM



- A tour operator has to RM multiple levels of inventory
- Each **outbound** flight
- ...can be used by **multiple hotels**
- ....for **multiple nights**
- ...and matched with **multiple returns**

...and costs are not fixed/sunk with many instances of having a marginal cost on each sale

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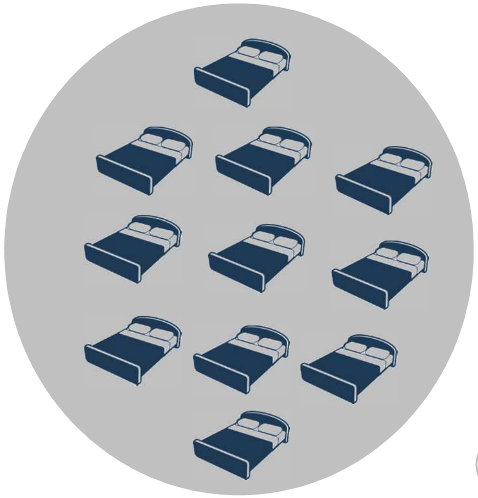
A tour operator does not always have fixed/sunk cost as they broadly contract hotel capacity through 3 ways:

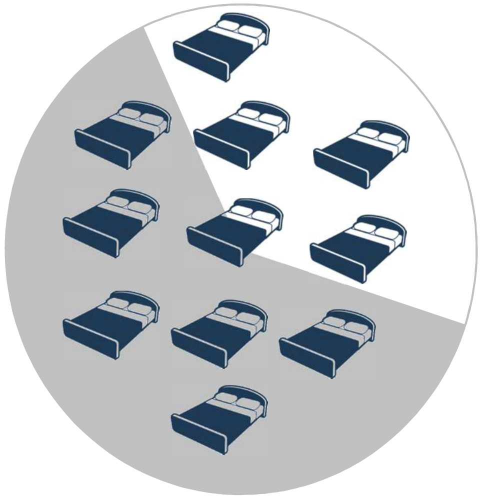
Committed hotels (contract)



% commitment

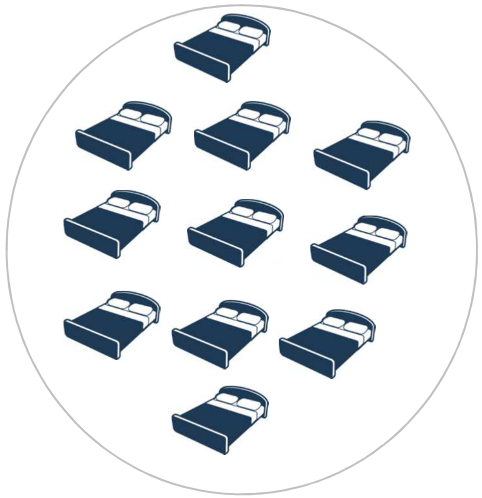
- Tour operator “pre-pays” an agreed allocation of rooms for a season at a preferential rate
- Tour operator then effectively acts as a hotelier for these rooms as they are pre-paid and will have no variable cost for selling/fulfilling them

Part-committed hotels



- Tour operator “pre-pays” a proportion of the cost for an allocation (e.g. 70%)
- The remaining capacity (e.g. 30%) is on a PAYG basis at a different rate
- Variable cost mainly 0 (within the part-commitment) but then becomes >0 when part-com reached

Fully variable hotels



- Tour operator gets an allocation of capacity but doesn’t pre-pay to commit; only pays for each room it sells
- ...however, there are release dates on the capacity if unsold
- Variable cost > 0

In tour-operator world, you have to maximise margin, accounting for the variable cost of your rooms and/or flights as rooms & seats are not already sunk costs

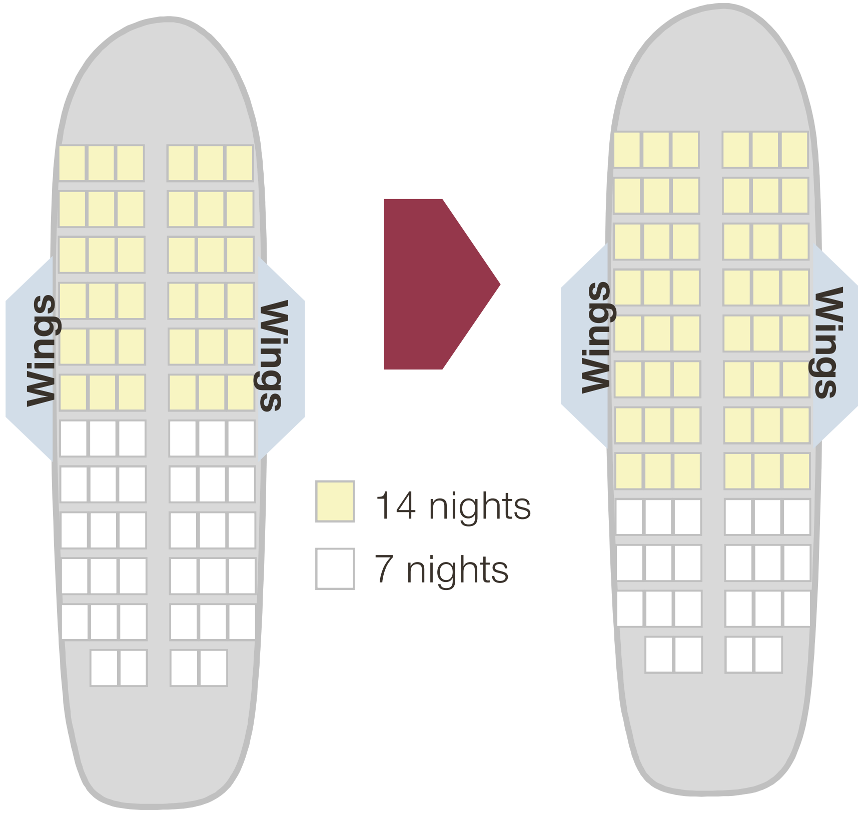
This is why Tour Ops Yield Manage

Plus, changing price is not always the most optimal RM recommendation

Adding capacity instead of raising prices

- For tour operators that offer escorted tours, **rather** than **increasing prices** on popular tours
- ...they opt to add a **new tour** in similar dates (e.g. increase capacity)
- Equally, for poorer performance tours, **consolidation, provided is feasible,** is often recommended

Changing capacity mix/set-up



- Large **tour operators** who have some flight capacity, **split capacity by duration** (e.g. protecting some seats for specific duration)
- This provides instances where **a change in the allocation of capacity** by duration **may** be more **profitable** than touching prices (e.g. middle of school holidays shift to 14 from 7 nights)

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Before moving to yield management, you need to first establish if this is applicable to you

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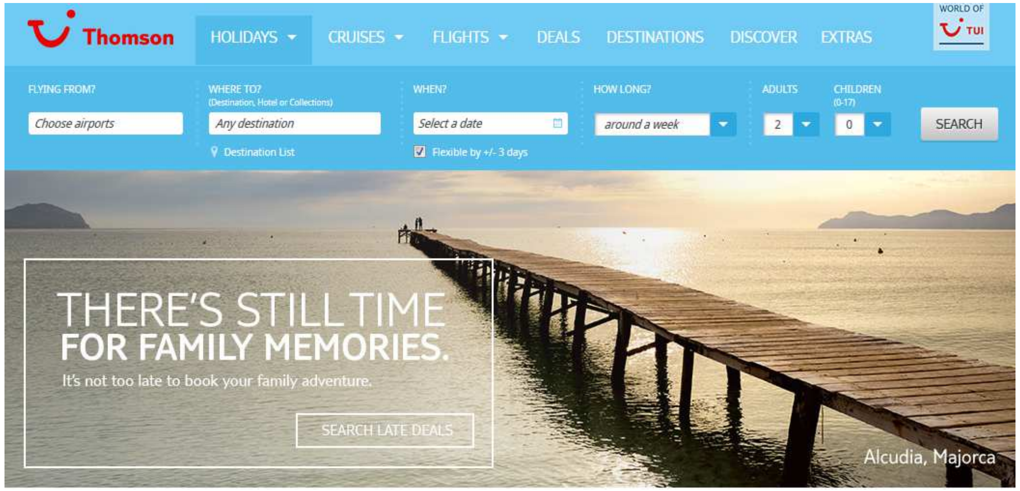
Yield management and dynamic pricing is not always relevant for your market/company

Escorted tours

- Members of the tour spend holiday together → need to ensure everyone paid similar price to avoid "dissatisfaction" of customers
- In some cases, demographics of target market, may have big resistance to "fluid" or "dynamic" price
- Purchase through consultation with brochure price being relevant rather than on-line

⊗ **Dynamic pricing & yield management less acceptable/justifiable to customers; tendency to re-price ad-hoc (brochure cycles)**

Traditional tour operators



- Market fairly used to price fluctuating from brochure price (thanks to the Late Deals 90s era)
- Purchase less involved, with a significant proportion sold on-line
- Customers relate it to airfares & hotels, where RM is typically more acceptable

✓ **Dynamic pricing & yield management more acceptable to customers**

...and if you do yield manage, do you have a pre-defined strategy on how price should evolve?

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Price up evolution

- Price increases as you move closer to departure
- Tends to be used by low-cost airlines, coaches, trains where earlier bookers are more elastic

May not be relevant to most operators in the UK as early bookers are more service/product sensitive

Price down evolution

- Price decreases as you move closer to departure
- Very prominent in the 90s where late deals and price-breakers appeared to push late sales
- Trains customers to book late

Although relevant from an elasticity perspective, it creates a dangerous expectation

Every day optimal

- Price is optimized every day based on market conditions and available capacity
- No clear set-up or expectation to customer when to book to get best price

Most applicable in the UK market

...and to keep your mind sane, you should simplify your problem to the key components to drive your decisions

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Outbound flight performance

Accommodation performance

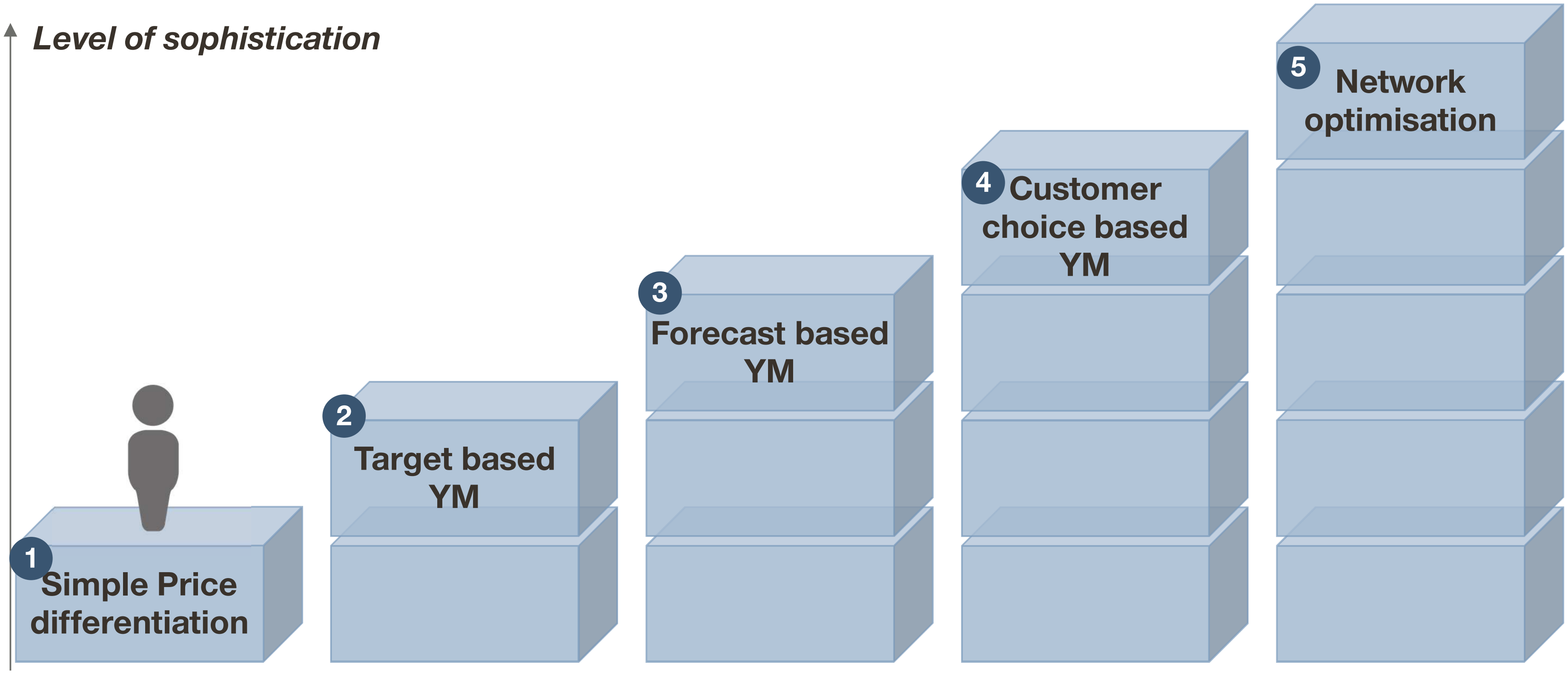
Inbound flight performance

Package price based on performance of each component that feeds to package

Margin of each package can also shape pricing recommendation, especially in very popular flights/hotels

To simplify your problem, evaluate the performance of each core component on the package and trigger pricing action for the package based on the combined performance of the components

You should evolve Yield Management on a step-by-step basis



Price changes	Manual	Auto & manual	Auto & manual	Auto & manual	Auto & manual
Forecasts	✗	✗	Based on rate of sale	Based on rate of sale, price & external factors	Based on rate of sale, price & external factors
Price optimisation	Gut-feel based	Rules-based on current performance	Rules-based on predicted performance	Price optimisation	Price & capacity optimisation
Alert functionality	✗	✓	✓	✓	✓

1 Start with the basics – seasonality of price

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- Ice-cream
- Late breakfasts

Visit thomson.co.uk to find out more about what's included

Price seasonality to align with peaks/troughs in demand are the first step to revenue management

2016/2017 prices from

Departure on or between Prices are in £'s per person	Nights	01 May 25 May	26 May 30 May	31 May 08 Jun	09 Jun 22 Jun	23 Jun 29 Jun	30 Jun 06 Jul	07 Jul 21 Jul	22 Jul 18 Aug	19 Aug 22 Aug	23 Aug 28 Aug	29 Aug 20 Sep	21 Sep 19 Oct	20 Oct 31 Oct	01 Nov 28 Feb	01 Mar 04 Apr	05 Apr 30 Apr
Sensimar Elounda Village Half Board Bungalow With Sea View / 2 Adults	7	505	789	725	739	805	865	865	1019	1069	1059	845	619	635	-	-	595
	10	639	945	939	975	1085	1125	1139	1395	1365	1355	1055	795	819	-	-	715
	11	695	995	989	1025	1095	1135	1169	1415	1379	1369	1095	825	855	-	-	755
	14	769	1139	1059	1175	1295	1339	1389	1695	1649	1515	1279	1005	1045	-	-	855

These prices are a guide and apply to selected flight departures between each date range. All prices can go up and down, please check at the time of booking for the most up to date price. Under occupancy charges and flight supplements may apply. Age restrictions may apply. See our A-Z at the back of the brochure for any additional charges and information.

Peaks | Troughs

..if relevant to your market, you can introduce a lead-time based price evolution

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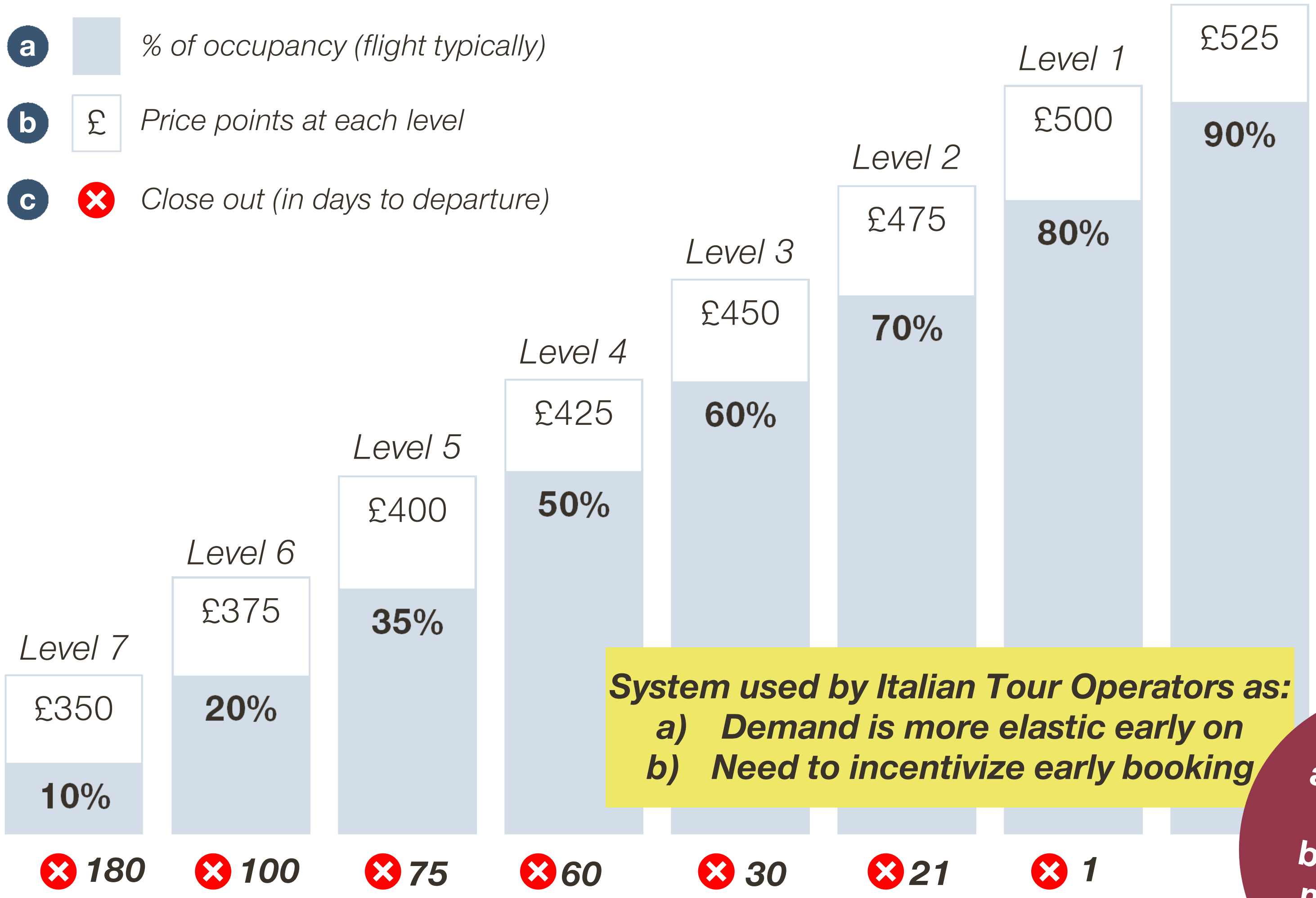
This **only makes sense** if you feel **early-bookers are more elastic** than later ones **and** you want to **incentivize early booking**

Lead time based differentiation

a — *% of occupancy (flight typically)*

b — £ *Price points at each level*

c — *Close out (in days to departure)*



System used by Italian Tour Operators as:
- ***a) Demand is more elastic early on***
- ***b) Need to incentivize early booking***

Only applicable if earlier bookers are more price elastic

Three key levers that essentially revenue manage sales

- a **% occupancy** – have price build-up based on capacity utilisation
- b **Price points** – Start low and go-up as you move closer to departure
- c **Close out** rules – are essentially used to drive price up as occupancy increases but also as you move closer to departure → they will, in combination with % occupancy, reflect how is occupancy expected to build-up as a minimum

Moving to the next step in yield management will typically require a booking curve

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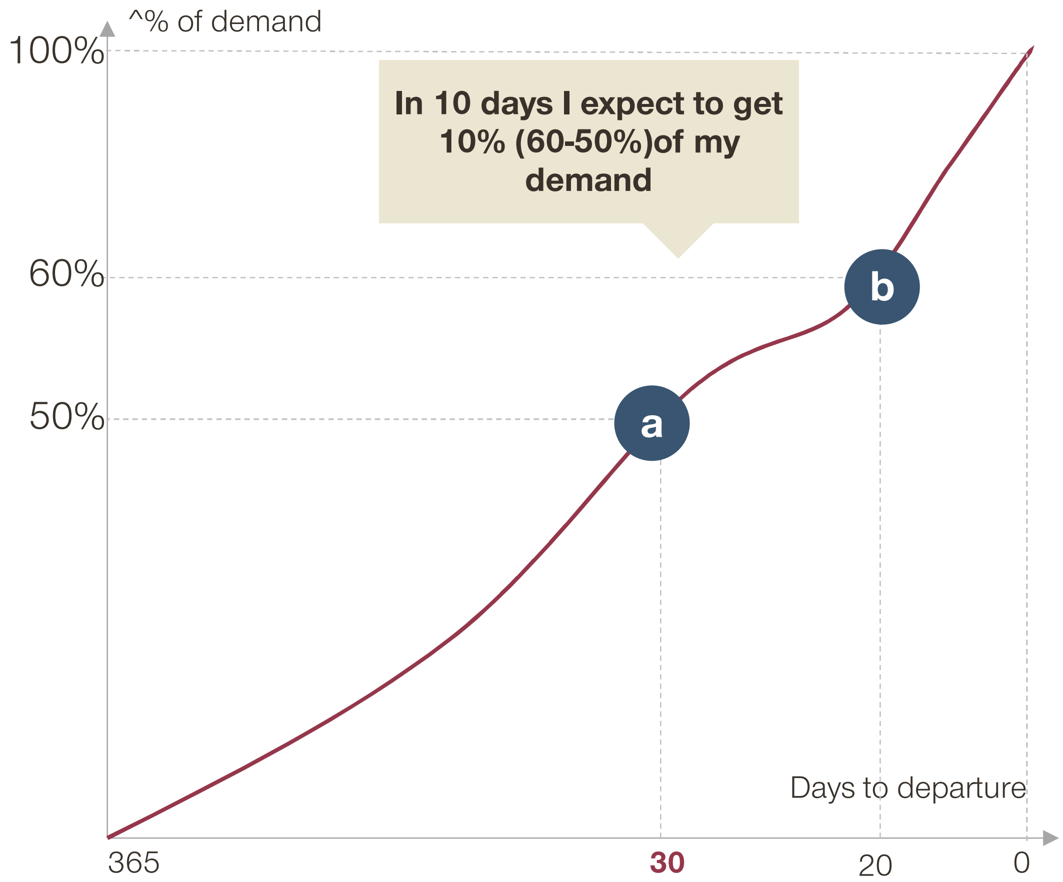

- Booking curves are crucial as they tell you how you expect demand to come through – e.g. by 30 days I should have sold 50% of my stock and at 20 days 60%
- They are usually developed through a combination of:
  - Historical bookings/revenue
  - Overrides on what you want to achieve this year in terms of strategy to avoid always repeating what you did last year
- The typical balance you have to be aware of is getting enough data to build a sensible one and at the same time not compromise key differences in booking behaviour between dimensions (e.g. 14 nights book earlier).

Booking curves are crucial in any Yield Management solution that goes beyond simple price differentiation

2 Booking curves can be used as targets to drive a target-based RM solution

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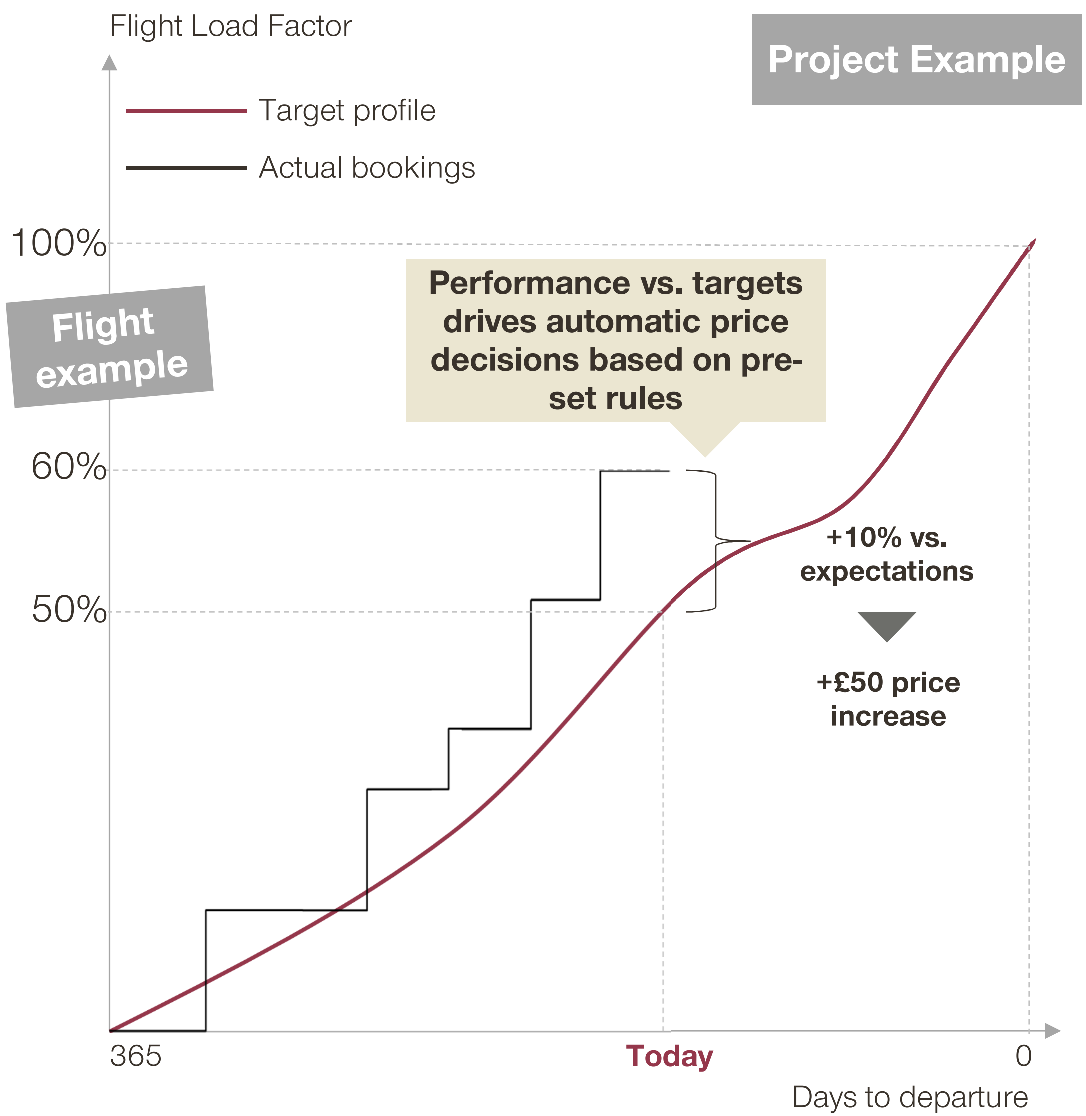
For this UK tour operator an RM was built that changed price based on "distance from an expected performance" rather than a forecast.



- For each flight departure date a **target profile** of how the contracted seat capacity should fill-up is set up based on:
  - Historical build-up of bookings on a similar week
  - Strategic objectives (e.g. company wants to shift bookings earlier/later)
- Each flight is **scored** based on three measures:
  - Distance to **expectation**
  - Performance vs. **other flights** in the resort
  - How that resort airport performs compared to **other resort** airport in the same category (e.g. Short-haul)
- The resulting flight score is used to drive price decisions through a rules-based mechanism
- A similar process is done for hotels

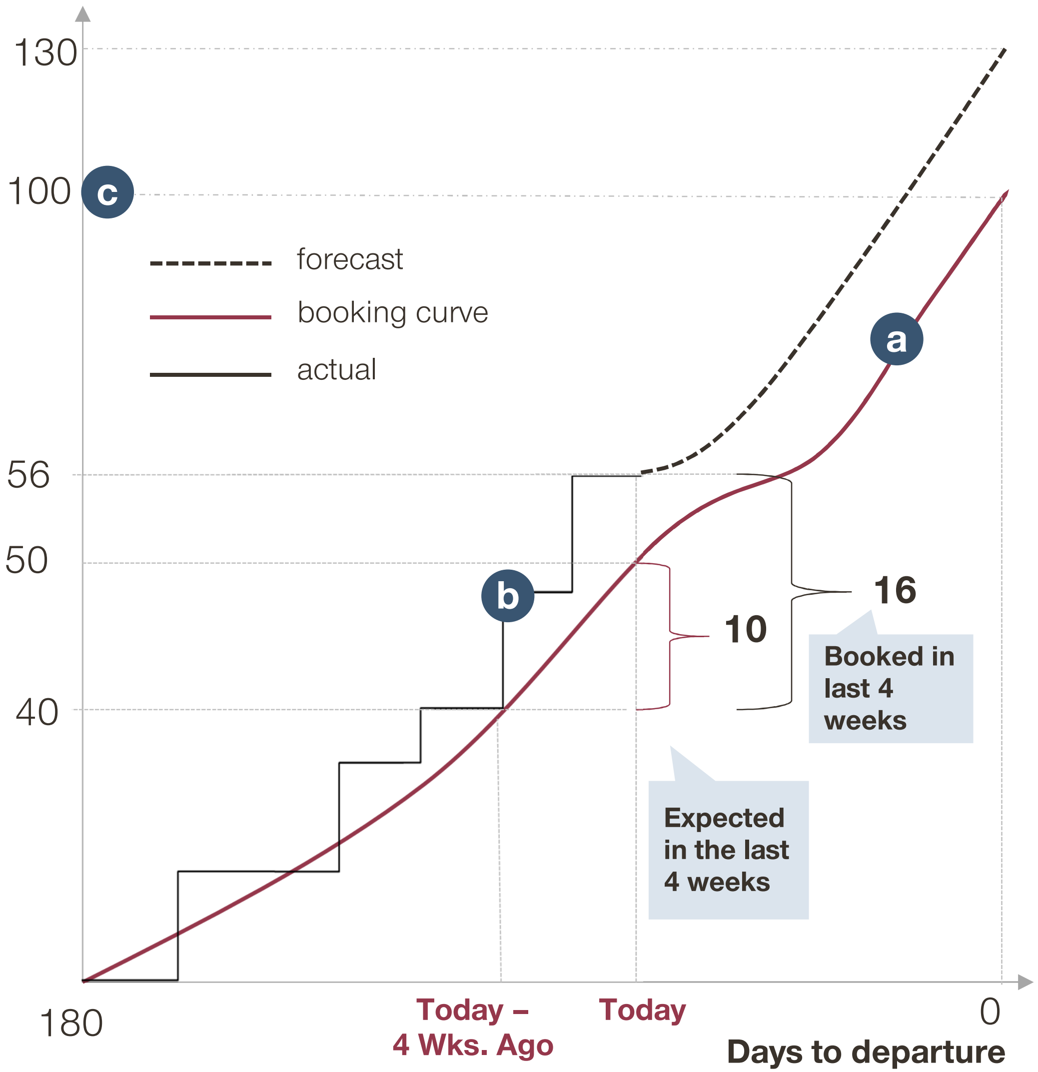
Score centile	Price change	Cumulative cap
Top 10%	+£50	+£150
10-20%	+£20	+£100
20-30%	+£10	+£30
30%-70%	£0	+£30
80%-90%	-£20	-£40
Bottom 10%	-£30	-£100

Score dictates price change, which is capped to a cumulative from brochure price. Price decisions are revisited based on "time since last price change" and/or booking activity

3 Booking curves are also used in forecast based systems

Below is an illustration of how we set-up a rate of sale forecast for a tour operator

Project example



Main components:

- **a** Booking curve that shows expectation of demand at current price
- **b** Sales to date
- **c** Target (capacity)

Rate of sale forecast (last 4 weeks example)

- My booking curve tells me that to fill the **100** I should have got **10** pax booked in the last 4 weeks
- Instead I got **16** pax booked
- If I assume this rate of sale will continue, I forecast to get **1.6** (16/10) times what I expected
- From now till departure I expect to get 100 – 50 = 50
- If I apply this recent of rate of sale that expectation will jump to **50*1.6 = 80**
- This will translate to a forecast of **56** booked + **80** expected = **136**

NOTE: Typically 2-3 rate of sale forecasts are created, each with different base (e.g. last day, last 7 days, last month) and a weighted avg is used to generate a forecast

3 Forecast based system can be combined with margin rules to drive pricing decisions

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Project Example
Tour operator

Resort	Egypt – Sharm
Budget month	2014_08
Budget week	Week 34
Flight	MXP-SSH
Day of week	Saturday
Current occupancy	91%
F'cast occupancy	197%
Seats capacity	100

A

Forecast occupancy of flight → >100% flight will sell out

Forecast occupancy of hotel and expected margin per passenger

Rules based pricing based on forecasts of hotel and flight

Hotel	Capacity	Fore-cast	Contrib-ution Margin	Pax booked	Total pax forecast	Forecast pax (to come)	Apportion	Comula-tive build up	% build up	Price decision
Hotel 1	5	20%	967€	-	-	-	0%	69	91%	DOWN
Hotel 2	10	0%	746€	-	-	-	0%	69	91%	DOWN
Hotel 3	272	98%	597€	45	76	31	39%	100	132%	UP
Hotel 4	5	64%	534€	2	2	-	0%	100	132%	STAY
Hotel 5	30	68%	520€	2	6	4	5%	104	137%	STAY
Hotel 6	30	120%	340€	20	65	45	56%	150	197%	UP
Hotel 7	50	80%	120€	-	-	-	0%	150	197%	UP
				69	**150**	**81**				

B C

A System produces forecasts for each flight on the programme as a % of capacity (>100% flight will fill out) based on current rate of sale.

B Equally, system produces forecasts for the hotels that will be sold with each flight, and the resulting margin per passenger each booking could bring

C Based on forecasts and expected margin per person, rules based engine recommends a price change (e.g. UP – put price up; DOWN – put price down; STAY: Leave price as it is)

System produces a forecast for both the flight and the hotel components of package

Based on forecast of flight & hotel, price recommendation is made

Crucially, margin is also used to determine where to best increase price when relevant stock is constrained (e.g. flight capacity)

4 A customer choice model enhances forecasts with insights from external market ..

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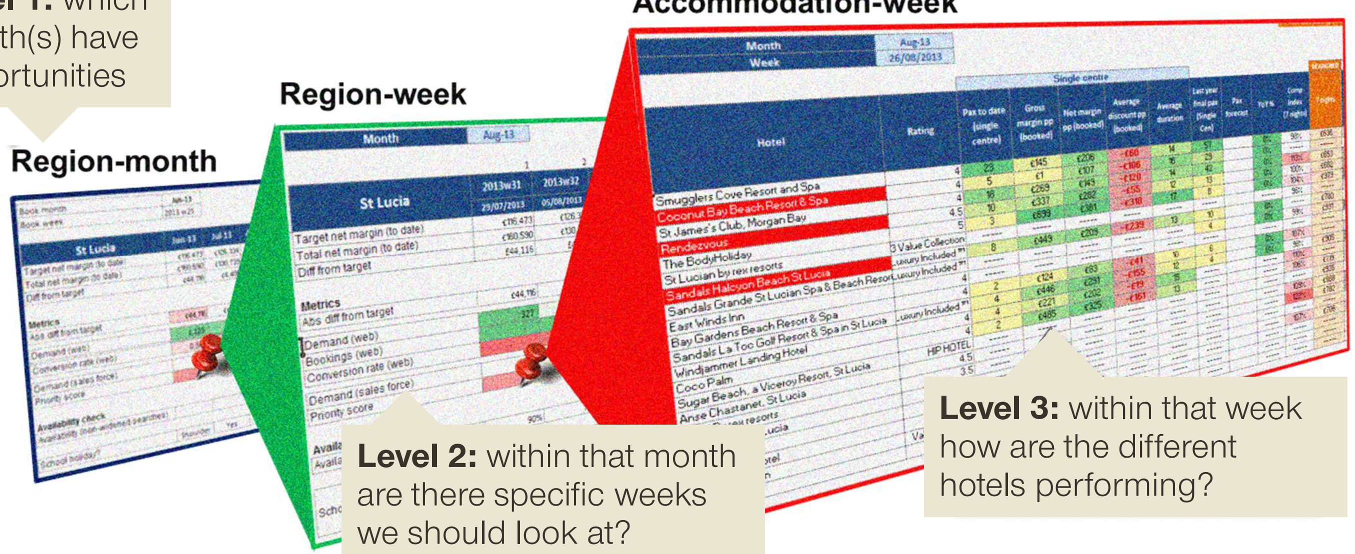
For this travel company, we developed an RM that on a daily basis used information on a rate of sale forecast, web-demand data and competitor prices to recommend price changes.

Sales to date
(pax, margin, price)

Demand data
(searches)

Availability
(failed searches)

Level 1: which month(s) have opportunities



Level 2: within that month are there specific weeks we should look at?

Level 3: within that week how are the different hotels performing?

Forecasts of demand
(based on RoS
& booking curves)

Rate architecture

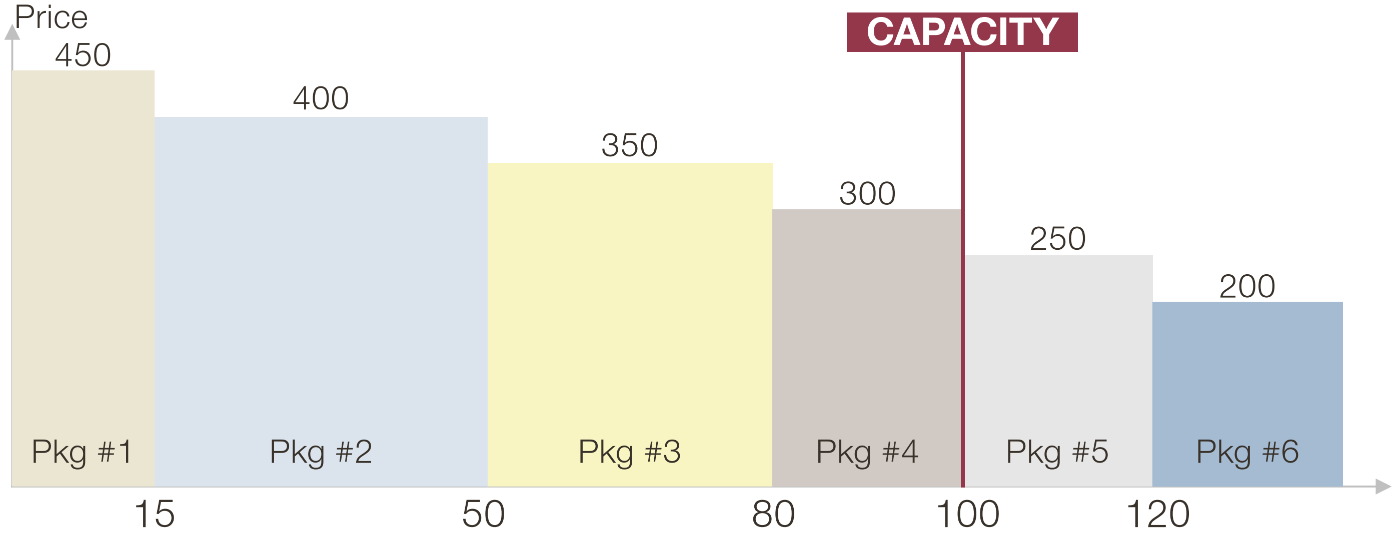
Competitor prices

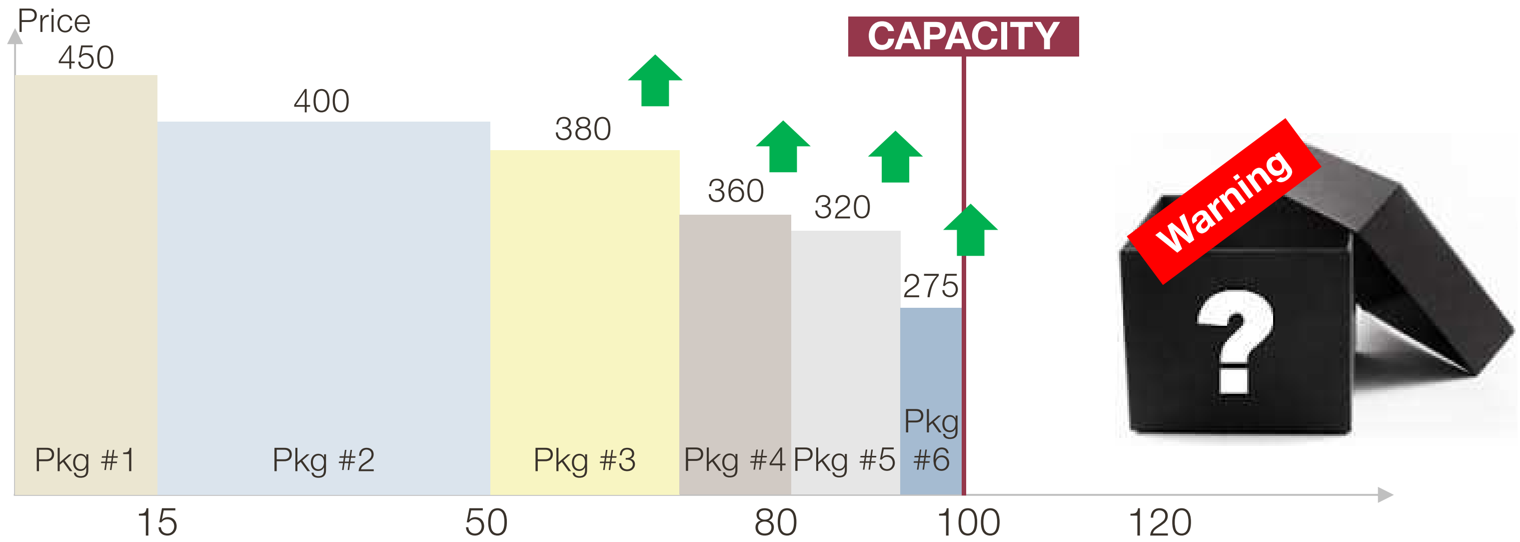
Project Example
Tour operator

Forecasts are enriched by a selection of KPIs which feed into pricing decisions:

- **Recent sales volumes**
- **Price positioning vs. competitors**
- **Web demand – are my forecasts low due to low demand or high price?**
- **Failed searches (i.e. do I have less bookings because my availability is restricted rather than my price is too high)**

5 A network optimiser optimises the revenue mix based on forecast & predicted impact of pricing action





A network optimiser will take the forecasts of demand and based on how the forecasted demand looks vs. available capacity will recommend price changes accounting for all interdependencies (e.g. flight to hotel and hotel to flight or even between hotel nights)

Optimisation is done in multiple dimensions (outbound flight, inbound flight and each stay-night at the hotel)

Margin is crucial as optimiser will tend to price-up the lower-margin products to maximise overall margin

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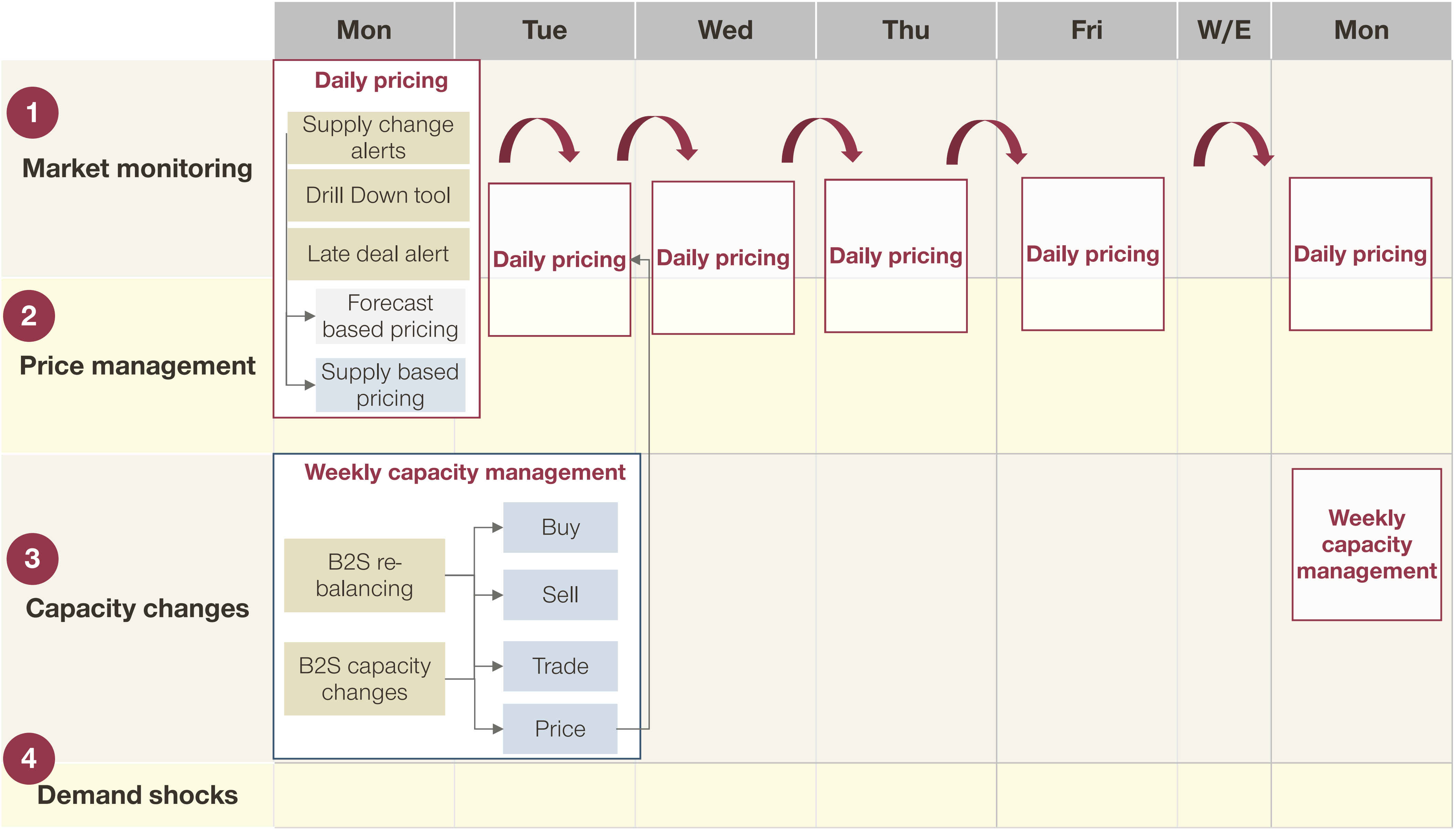
Whatever you choose, you need a process, a set of reports and a team to yield manage



Process | Tool | Decision

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- **Key takeaways**
- Q & A

Key takeaways

- **Tour operator yield management** is **complicated** as there are multiple dimensions to optimise and consider (flight out, accommodation nights and flight-in)
- ...and there is a mixture of packages/instances where a **variable cost applies** to each additional transaction
- ...while **pricing** is not the **only** thing you can manage through **yield management** – capacity is another.
- Before moving to yield management **establish if it is the right solution for you** and whether you want it to have a pre-defined strategy
- If you do **move to yield management**, **break-down** your problem by evaluating the performance of **components** to drive your pricing and revenue management decisions.
- **Start simple** with price differentiation reflected through price seasonality
- Once that is set-up you can **build up sophistication step-by-step**, starting from target based, to forecast-based, choice-based model and eventually a network optimisation
- You don't need to do all steps – sometimes **network optimisation** is overkill and too much of a **black box**
- Ensure you have the **relevant reports** and **processes to support yield management** – else your attempt will fail.

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Thank you

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