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Hoteliers are Still Behind the Curve In Online Distribution

Travel suppliers in other travel sectors are well ahead of hoteliers in aggressively adopting online distribution | By Max Starkov and Jason Price

Travel suppliers in other travel sectors are well ahead of hoteliers in aggressively adopting online distribution. Airlines and car rental companies are pushing hard online and non-GDS distribution and are embracing the Internet as their main distribution medium. Online distribution is expected to contribute more than 22% of the airline total passenger revenue this year and more than 28% by 2005. Car rental companies expect 25% of their sales to be online this year. (PhoCusWright).

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The Online Travel Marketplace

The Internet: the greatest direct-to-consumer channel

Online travel purchasing is growing fast despite the softened economy. As demonstrated below and reported by PhoCusWright, the online travel market will grow to 27% of the overall travel market in 2004, from 7% of the market in 2000 and 15% in 2002. The $200 billion U.S. travel industry expects $49.5 billion of online bookings this year. This number will increase to $79 billion in 2005 (eMarketer/Jupiter Media Metrix). Jupiter Media also estimates the European online travel market will be worth more than 20 billion EURO by 2006.

Online vs. Offline U.S. travel market

	Online:	Offline:
2000	7%	93%
2001	10%	90%
2002	15%	85%
2003	17%	83%
2004	27%	73%

(2001, PhoCusWright)

Changing Mix of Online Travel

An increasingly growing number of online travelers book their business travel online. An estimated 29% of online bookings in hospitality and 21% of air bookings are unmanaged business travel related (Jupiter Research 2002). Expedia claims that 30% of all bookings on its website are business-related. Notice the rates of growth in both categories for online unmanaged and managed business travel in the following table:

Changing mix of online leisure and business:

	Online leisure / unmanaged business	Online managed business travel
2000:	$13.4b	$4.4b
2001:	$17.2b	$7.7b
2002:	$24.8b	$12.0b
2003:	$31.9b	$17.6b
2004:	$37.8b	$24.7b

2005: $46.2b $32.8b

(2002 eMarketer/Jupiter Media Metrix)

Travel Suppliers

The Internet has created an ideal medium for direct-to-consumer distribution. The airlines in particular have become experts in direct-to-consumer Web distribution. Southwest Airlines' online revenue exceeded $2.19 billion in 2001, followed by Delta with $1.8 billion and US Airways with $1.16 billion. JetBlue generates 65% of its revenues from its website, www.jetblue.com and is one of the few profitable airlines today.

Travel suppliers in the other travel sectors are well ahead of hoteliers in aggressively adopting online distribution. Described in table below, online distribution is expected to contribute more than 22% of the airline total passenger revenue this year and more than 28% by 2005 (PhoCusWright). Car rental companies expect 25% of their sales to be online in 2001 and 30% in 2005. On the retail side, recent airline commission cuts require travel agents to focus on non-air travel products and to look beyond the GDS as the sole inventory and booking provider.

Online share in main travel segments (% of all booking revenue):

	2001	2002	2003
Airlines:	14%	18%	22%
Car rental:	15%	20%	25%
Hospitality:	5%	10%	13%
Vacations and Cruises:	3%	4%	8%

(PhoCusWright, eMarketer)

HeBS estimates that the online share in hospitality will surpass the 2002 PhoCusWright projections and reach 14% in Q4 2003.

Jupiter estimates that while online travel will grow at an annual rate of 23% from 2000 through 2006, revenues specific to lodging will grow over 26% during the same period, from $3.8 billion to $15.5 billion. The explosion of the merchant model, aggressive Internet efforts by some of the major brands and by many independents and hotel management companies, increased popularity of pay-per-click models and email marketing strategies among hoteliers, are some of the reasons behind HeBS estimates. Here are few concrete examples:

- Many hoteliers reported increase in their website bookings of 25%-50% during the second half of 2002.
- The merchant model leaders reported big gains last year. For example Expedia: In Q4 of 2002: merchant revenue rose 184% up compared to Q4 of 2001. Expedia sold 3.2 million room-nights, 2.5 million of them—merchant (80%)
- The opaque rate model Hotwire reported 300% increase in its hotel bookings over the same period of 2001.

- There is a major shift away from GDS to Internet hotel distribution. TravelClick reports GDS bookings down 6.4% during first half of 2002 while GDS Consumer Internet Bookings were up 5%.
- Online leisure travel will grow by at least 23% this year alone (Jupiter).
- High self-booking adoption rates will give a big boost to the online managed business travel this year, which is expected to grow by 36% (Jupiter).
- Major brands, including Carlson Hotels, already report that 10%-15% of their revenues are generated from Internet sales. Marriott generated over $1 billion in sales from its website.

Case Study: US Major Airlines

Over the past year all major airlines adopted the "Direct Web Distribution Model" i.e. direct consumer sales via the Internet as the centerpiece of their online distribution strategy. The airlines were able to squeeze whatever they could from the old distribution system and enhance their new Web distribution strategies. The abolishment of travel agency base commission by the major airlines earlier this year was not only a cost-cutting measure, but also a direct result of the newly gained realization that the Direct Web Distribution Model works.

As seen from the following table the efforts of the airlines to embrace the "Direct Web Distribution Model" is well justified as the Internet is by far the least expensive distribution channel:

Airline Ticket Distribution Costs in the US, 1999-2000

	Travel Agents		Direct Sales	
	Offline	Online	Offline	Online
Ticket processing fee	$3.00	$60	$9.00	$60
Credit card fee	$6.00	$6.00	$6.00	$6.00
GDS booking fee	$8.40	$8.40	-	
Commissions	$22.80	$10.00	-	
Total:	$40.20	$25.00	$15.00	$6.60

(JP Morgan 2000)

The airlines have perfected website and precision e-mail marketing to promote their special offers and sell more airplane seats. Indeed, eMarketing has become the airlines' preferred marketing tool. Why? It is the least expensive channel and it works. For example, precision e-mail marketing offers up to a fivefold increase in response rates and a tenfold decrease in conversion costs than direct mail (IMT Strategies). Employing an email marketing strategy has saved the airlines enormous marketing dollars since 9/11. In place of full-page newspaper ads, the airlines are using precision e-mail marketing extensively to target specific market segments with unparalleled accuracy in their Web-only fare promotions and special offer campaigns. The Internet has firmly established itself as the airlines' distribution channel of choice. No wonder over 22% of all airline sales in 2002 will be transacted online via the Web.

Leisure and business travelers alike perceive the Internet as a source to find unique and competitive prices. Consumer surveys report a growing number of leisure and business travelers view the web as a source to secure "good" and "very good" deals over the travel agent and supplier toll free number.

Travel Suppliers vs. Online Intermediaries

As mentioned, the Internet is the ideal direct-to-consumer medium and many travel suppliers have adopted the direct distribution model no longer for incremental revenues but as the centerpiece the centerpiece of their Internet strategies.

The overall impression is that the situation is in favor of the travel suppliers:

	Direct	Indirect
2002:	52%	48%
2003:	53%	47%
2005:	55%	45%

(Jupiter Research)

PhoCusWright also predicts that there will not be a dramatic shift in market share among online travel channels over the next 3 years and online travel agency market share will slip from 49% in 2002 to 47% in 2003. This travel research company predicts that first-time online buyers and leisure travelers will prefer online travel agencies, while frequent business travelers will choose supplier websites.

Airlines vs. Intermediaries

Airlines are the most determined among all travel suppliers to sell directly to online consumers and they demonstrate formidable competitors in their struggle with online agencies to dominate the Internet. Unlike the offline world, where only 35% of bookings are direct sales and 65% come from agency sales, in the online world direct sales will constitute more than 62% of all air online bookings in 2002 (PhoCusWright, IDC).

PhoCusWright predicts that revenue from airline websites will grow at a slightly faster pace than revenue from online travel agencies, as airlines continue benefiting from frequent traveler usage of their website. Notice in the following table, the airline website share will grow from 55% in 2000 to 57% in 2003. PhoCusWright also predicts that airlines have great room for improvement as leisure travelers will continue to lean toward full-service online agencies.

US Airline Online Ticket Sales by Online Channel:

(excluding Southwest Airlines)

	1999	2000	2001	2002	2003	2004	2005
Airline websites:	41.7%	48.8%	50.8%	52.9%	52.9%	2.9%	52.9%
Online Agencies:	58.1%	51.2%	49.2%	47.1%	47.1%	47.1%	47.1%

(IDC, 2001)

The above figures exclude Southwest Airlines, which has a very unique direct-to-consumer online and offline business model, which skews the overall outlook. The table below shows how the situation looks like when Southwest Airlines enters the picture:

US Airline Online Ticket Sales by Online Channel:

(including Southwest Airlines)

	1999	2000	2001	2002	2003	2004	2005
Airline websites:	54.7%	59.5%	60.8%	62.1%	62.1%	62.1%	62.1%
Online Agencies:	45.3%	40.5%	39.2%	37.9%	37.9%	37.9%	37.9%

(IDC, 2001)

The airlines have found a very effective way to challenge the online travel agencies: by building their own online services. Orbitz.com, a joint venture of several major airlines launched in 2001, has become the third largest online agency after Expedia and Travelocity in less than 15 months. Another joint venture of the airlines, Hotwire is competing successfully with Priceline in the opaque rate market.

Car Rental Companies vs. Intermediaries

While few car rental companies disclose information, it is identified as a highly competitive market. Online travel agencies are increasing their market share due to their ability to offer price comparisons and packaging of car rental with air, hotel and vacation packages. PhoCusWright predicts that by 2003 56% of online care rental sales will come from car rental company-owned websites while 44% will come from online agencies and intermediaries.

	1999	2000	2001	2002	2003
Car Rental Company Websites:	60%	57%	58%	57%	56%
Online Agencies:	40%	43%	42%	43%	44%

(2001 PhoCusWright)

Still, in the online world car rental companies will enjoy more direct sales in 2002 (57%) than in the offline world, where their direct sales share is only 40%. (PhoCusWright)

Hotel Companies vs. Intermediaries

In the offline world hoteliers enjoy more direct sales (75%) than agency sales (15%-20%). In the online world hotels are less aggressive than the airlines about bypassing the agency channel. This year for example only 52%-53% of online hotel bookings will be direct sales.

Unlike the airlines, hotel suppliers have difficulty maintaining market share and finding the right formula to deal with online agencies and intermediaries. The lack of comprehensive Internet strategies, ineffective online distribution efforts and the explosion of the "merchant model" are partly to blame for the current situation. PhoCusWright projects that hotels will not be able to increase market share as new online travelers are lured by the one-stop and comparison shopping and discounted rates on the main agency websites. Hotel suppliers' market share fell from 55% in 2000 to 54% in 2001 and it will take extra efforts to maintain this share in the future.

	2001	2002	2003
Hotel Branded Websites:	54%	52%	53%

Intermediary Websites: 46% 48% 47%

(2002 PhoCusWright)

Hoteliers Take Notice

- At least 13% of hotel bookings will come from the Web this year. Three years from now the Internet will contribute over 20% of all hotel bookings (PhoCusWright, eMarketer)
- Size of the online hospitality market will exceed $7.9 billion in 2003 and reach $15.5 billion by 2006 (Bear Stearns, Jupiter Research)
- 53% of all Internet bookings in hospitality will be direct-to-consumer (i.e. via hotel-owned websites) (PhoCusWright).
- Jupiter estimates that while online travel will grow at an annual rate of 23% from 2000 through 2006, online revenues specific to lodging will grow over 26% during the same period from $3.8 billion to $15.5 billion.

From these national averages, how do you compare and where are your competitors? If you do not fare better than the national averages, you are already behind your proactive competitors.

Hoteliers are beginning to like what they see: online distribution cuts costs, attracts affluent customers and lessens the dependency on more traditional and expensive channels. As demonstrated below, Jupiter Research estimates that the size of the online hospitality market will exceed $6 billion in 2002, up from $4.1billion in 2001, and will reach $7.9 billion in 2003. Some hotels already generate 20%-30% of their bookings from the Internet.

U.S. Online Lodging Revenues:

(in Billions, E=Estimated)

2001E	$4.1
2002E	$6.0
2003E	$7.9
2004E	$10.0
2005E	$12.8
2006E	$15.5

(2002 Bear Stearns, Jupiter Research)

Over 192 million North Americans are active Internet users (Nielsen) and 40 million of them have already purchased travel online. The Internet offers vast, interactive, rich media and most importantly, growing distribution market.

Traditionally hoteliers have been successful in their direct-to-consumer sales efforts. Unfortunately in the online world hoteliers have difficulty establishing robust direct-to-consumer online strategies and often fall pray to the online intermediaries and discounters. The Internet, which is the greatest direct-to-consumer medium invented as of yet, should prove a fertile ground for the direct sales efforts of proactive, Internet savvy hotel marketers.

Conclusion

The Internet has changed the way travel is being negotiated, managed and purchased. In this economic environment travel consumers have embraced the Internet as the ideal medium to shop travel. By 2005 over 30% of all travel bookings will be completed on the Internet. Hoteliers are less aggressive than airlines and car rental companies in embracing direct-to-consumer online distribution. This year 13%-14% of all hotel bookings will come from the Web. 53% of them will be direct-to-consumer. From these national averages, how does your hotel company compare and where are your competitors? If you do not fare better than the national average, you are already behind your proactive competitors. The direct-to-consumer model should become the foundation, the centerpiece of any hotel company's online distribution strategy. It provides the hotel with long-term competitive advantages and lessens dependence on intermediaries, discounters and traditional channels about to become obsolete.

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