

# Uk tour operators analysis



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A tour operator combines tour and travel components to create a holiday, it designs travel routes for tourists and offer perfect arrangements of the airlines and hotels. In a word, a tour operator offers package holidays. A travel agent is a kind of retail business which is a buyer of tour operator, it sells travel-related products and services to customers on behalf of tour operators, airlines, hotels and other entities. Nowadays, tour operators and travel agencies are closely related to each other. Some tour operators own the distribution channel, they set up retail shops selling products and services directly to the final customers, or they establish close relationships with travel agencies under contracts. The development of the industry should be attributed to the development of transportation in the early age. With the invention of aircraft, the demand for travel increased rapidly. But in recent years, situations become more complex than ever before in such a changeable economic climate, UK's tour operator industry are fluctuated in growth. This part of report focuses on the market and development during the year 2005-2008. The Association of British Travel Agents (ABTA) was formed in 1950 by 22 leading travel companies, now represents over 5, 300 travel agencies and nearly 1000 tour operations. Its Members range from small, specialist tour operators and independent travel agencies through to publicly-listed companies and household names; from call centres to internet booking services to high street shops, occupy more than 90% of the British market. Thus statistics of ABTA can be used to conduct this report. According to the annual report of ABTA, during the year 2005-2006, bookings through ABTA members were 6% down on the prior year. The package holiday market continued to decline but specialist holidays, cruise tours and flight-only bookings all grew significantly. Company failure level rose substantially

from 33 in the previous year to 47 this year. The industry structure changed a lot: independent agents turned to favour dynamic packaging with concentration on niche markets including long-haul, cruising, UK holidays and self-packaging. Big operators drove bookings online and through their own retail networks. 2006 is one of the most challenging years in the industry's history, with traditional business model under great pressure and uncertain future for many others. During the year 2006-2007, 32.8 million overseas visitors who came in 2007 spent £16.0 billion in the UK, the volume remained stable but spending fell in cash terms for the first time since 2001. Financial statuses of ABTA members were quite positive: total net current assets of £5.11 million (6% up) and total income of £5.70 million (13% up). Company failure levels fell dramatically from 47 to 32 compared to the previous year. Several weaker players in the industry have been winnowed out of the market but the figures are still very encouraging. The industry remained in good health. Consolidation and merger activity has been a key feature of the outbound tourism market in 2007. New business models had made that the differences between the tour operator and travel agency become increasingly blurred. 2008 is again a challenging time for the industry: at one time the fuel price had reached \$150 a barrel which is the double of the price in 2007; sterling lost a large amount of its value against most currencies; what makes things worse is that the credit crunch caused the world's economic downturn, consumers changed their spending patterns, companies struggled to survive. In spite of these factors, UK outbound visits remained increase by 1.5 million from 69.2 million last year to 70.7 million this year. The number of company failures fell from 32 to 30 compared to the previous year. But unfortunately, because of the high cost of fuel, the UK's

third largest travel group-XL Leisure Group collapsed on 12 September 2008 leaving 85000 passengers still on their holidays. This failure resulted in one of the most extensive repatriations in the UK travel industry's history with 85, 000 passengers being flown home in a joint action by TUI, Thomas Cook and Virgin orchestrated by the CAA. Another important issue happened in 2008 is the merger of ABTA and the Federation of Tour Operators (FTO) which represents the continuing integration of travel agency and tour operator within the industry. The industry will benefit greatly from the combined different strengths that both organisations offer. The FTO's experience and expertise in operational issues fit ideally with ABTA's traditional functions.

## **PEST analysis of the remote environment**

### **(P)olitical/Legal**

#### **3. 1. 1 Political instability and Terrorism**

Political instability is described as a condition of a country where a government has been toppled, or is controlled by factions following a coup, or where basic functional pre-requisites for social-order control and maintenance are unstable and periodically disrupted (Cook 1990). It is clear that the political instability in a certain country is negatively influencing travelers' decision making with prospective travelers seeking substitute travel plans. It will reduce the demand for travel significantly as tourists concern about the safety first and nobody wants to travel in a dangerous environment that strikes, wars and terrorists attacks happen. Among all the factors influencing political instability, terrorism is the most significant one that affecting tourism in UK in recent years. After the heart-broken event of

terrorist attack on 11th September 2001, the concern about safety in travelling is increasing rapidly. A series of coordinated suicide bomb attacks on London's public transport system during the morning rush hour happened on 7th July 2005. The discovery of two car bombs set to detonate in London's bustling theater and nightclub district Friday, June 29th, 2007 has encouraged residents to remain alert. Following that case, a jeep rammed into a Scottish airport in Glasgow on June 30th, forced Britain to raise the threat level to "Critical" -the highest alert status. All of the events listed above had negative influences on tourism in UK and businesses of UK's tour operators. Report said that 15% of the advanced bookings were cancelled during the summer peak travel time in 2007.

### **Government and Tourism**

Government always participates in tourism activities through several kinds of ways: government makes policies for the development of tourism industry; government makes policies that will have impacts on tourism industry. In this part, the report will address issues like the carbon tax influences on the industry, VAT effects on the industry and financial incentives government used on the industry.

According to Conservatives 2007, aviation contributes just 5.5% of the UK's CO2 emissions but emissions from UK aviation increased significantly by more than 90% between 1990 and 2004. Government urged to take measures to reduce the negative impact of carbon emissions on environment: from 2001 to 2007, the original APD which is at a rate of £5.50 on flights from the UK to elsewhere in the European Union and the European Economic Area and £22.00 for other flights was introduced; a new tax which

doubled these charges was introduced from February 2007. These changes in carbon taxation would result in changes in prices of travel products using aviation and finally affect the demands for travelling and sales for tour operators. According to Karen Mayor and Richard S. J. Tol, due to the changes in February 2007, countries near the UK would see a small drop in visitor numbers, and the UK itself would see a larger drop (1.2%). The recent doubling of the boarding tax will reduce arrivals by some 528,800 people in 2010, this is a 1.3% reduction (Karen Mayor, Richard S. J. Tol, 2007).

UK government applies a rate of 15% VAT (Value Added Tax, temporary cut from 17.5%) which is the standard rate on tourism products, while most other EU countries apply reduced rate of VAT around 5% on tourism products. Report said that a cut to the 5% UK reduced VAT rate on tourist attractions admission and accommodation will boost employment and result in gains of up to £760 million savings in increased income and corporation tax. It also predicts an additional £440 million will be injected into the industry supply chain.

The Government had announced an 18% cut in funding for VisitBritain over the next three years on October 2007. Tourism Alliance Chairman, Ros Prichard OBE, stated " This cut in funding means that, in real terms, the Government will have reduced VisitBritain's funding by around 50% between 1997 and 2011." That is a catastrophe for UK's tourism industry, VisitBritain will be lack of funding to advertise and promote UK's attractions, financial incentives to the industry had been withdrawn and other capital allowances had been reduced, while funding for VisitBritain had been cut back just at the

time when they were needed the most, the growth in sales of the industry will suffer.

## **(E)conomic**

### **3. 2. 1 National economy and disposable income (impact of economic recession)**

The world is now suffering from the economic downturn caused by financial crisis, businesses collapse, jobs are destroyed, UK's economy is significantly influenced by the crisis. According to National Statistics Online, UK's GDP contracted by 1. 6% in the fourth quarter of 2008 when the crisis started. It is now 2% lower than the fourth quarter of 2007. For the year 2008 as a whole, GDP rose by 0. 7 per cent with a down trend of 3% in the previous year. UK's economy is experiencing the worst recession in over a century. The recession is a disaster for employment in UK, unemployment rate rose to 6. 7% (0. 6% higher than the last quarter and 1. 5% on last year). 29. 3 million people were in work in the period December to February according to the labour force survey (LFS). The number of people employed fell by 126, 000 this quarter and down by 227, 000 on the last year. All the situations listed above lead to the decrease of national income and disposable income. Tourism is sensitive to economic uncertainty and downturn: most travel activities involve disposable income, as total income drops, disposable income drops, people would conserve their money to cover the cost of life essentials, food, shelters and family necessities. The demands then decrease making tour operators suffer.

### **3. 2. 2 Fuel price**

Fuel cost is a major cost of airline companies, the cost will be paid by customers as fuel surcharge. Tour operators will raise the price of their products, especially for long-haul products when fuel price goes up. The travel enterprises will then be in danger of losing customers. When international crude oil price hit the record of \$148 a barrel in September 2008, both airline companies and travel enterprises struggled to make ends meet. The fuel surcharge of some long-haul flights was even same as the ticket price, this might change customers behaviour at some degree, people may stay closer to their home or switch to other entertainments. The economic crisis UK encounters leads to a substantial decrease of oil price which could possibly boost travel industry to some extent though the major influence is negative.

### **3. 2. 3 Exchange rate**

The exchange rate, or the value of the British Pound relative to the currencies of other countries, has had a significant effect on both inbound tourism and outbound tourism. In 2007, the weak dollar makes UK accommodation and food more expensive for visitors from America, the exchange rate put London 15th in its popularity table in July 2007 – down from number seven a year earlier according to Cheapflights. Due to the recent Pound depreciation, visitors from other European countries or America can expect to pay around 30% less than they would have done a year ago. British Tourist Authority (BTA) produced a study on ‘ The Price Sensitivity of Tourism to Britain’, the findings show that overseas visitors are highly sensitive to changes in the cost of staying in Britain: for every 1% movement in the exchange rate which increases the cost of staying in

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Britain, the UK's international tourism earnings will decrease by 1.3% (£160m). Research also found that more fixity in the exchange rate arrangements generates a positive effect on tourism and the more fix the exchange regime is, the greater the impact on tourism (María Santana-Gallego, Francisco J. Ledesma-Rodríguez, Jorge V. Pérez-Rodríguez, 2007).

## **(S)ocial**

Social factors like age, changing life style affect the industry through changing consumer behavior.

### **3.3.1 Age and tourism**

According to United Nations Statistics and National Statistics Online, for the whole world, since 1950 the proportion of older persons has been rising steadily, passing from 8 per cent in 1950 to 11 per cent in 2007, and is expected to reach 22 per cent in 2050; For UK, the percentage of the population of state pensionable age exceeded the percentage of the population under 16 for the first time in history in 2007. The industry now is facing an older growing society due to rising life expectancy, marketing of the industry should focus more on older persons: the advertising and products should target more at older persons.

### **3.3.2 Changing lifestyle**

There is a growing trend of buying online which could reduce a person's shopping trip frequency, the access to the world's products through internet reduces the flows of shopping tourists from one city to another or cross countries. More and more people tend to prefer clubs or watching TV at home rather than going out for a trip at weekends.

### **3. 3. 3 Growing concern about environment**

Tourism is one of the largest industries in the world with incredible developments each year, it contributes a lot to the world's economy while the huge infrastructural and resource demands of tourism (e. g. water consumption, waste generation and energy use) can have severe impacts upon local communities and the environment if it is not properly managed. A concept: sustainable tourism which is defined as "tourism which leads to management of all resources in such a way that economic, social and aesthetic needs can be fulfilled while maintaining cultural integrity, essential ecological processes, biological diversity and life support systems" by World Tourism Organisation becomes more and more popular. People concern more about the environment, they tend to favour ecotourism products. When developing new tourism products, tour operators should design their trips to be environmentally, culturally and socially friendly.

## **(T)echnological**

### **3. 4. 1 Technology development of transportation**

With the development of piston engine aircraft, the mass tourism boomed in 1950s. Transportation technology is always regarded as crucial in the development of tourism, places inaccessible before by car or train can be accessed swiftly by air. It is largely due to the improvement of transportation that tourism has expanded. The highlight of a trip is usually the experience in destination, visitors often neglect the process of getting to the destination. In this case, the faster the visitor can reach the destination, the more attractive the destination will be. The development of transportation especially the speed of the transportation tool will have a major impact on long-haul travel.

### **3. 4. 2 Internet and the industry**

The world enters a new information era with the development of internet technology. The world's internet users are increasing sharply. According to Internet World Stats, there were 43, 800, 000 internet users in UK in March 2009 which represents 70. 9% of the population, that is a 180% growth from the year 2000. Internet has become an essential part of people's life. For tour operators, internet provides tour operators platforms of advertising and transaction, which can make their products more accessible to the customers thus bring more sales and profits. Moreover, it is cost-effective and time-efficient using the internet. For customers, internet makes it easier for them to browse the products and make bookings. More and more people are now booking their holidays on the internet, tour operators need to focus on the website design as well as the security of the transaction system.

The internet technology makes it possible for meetings online, different companies can communicate or negotiate with their counterparts more efficient through videoconference. Face to face contact is not compulsory anymore. Business travel will suffer from that, there might be a decline in business travel sales for tour operators.

### **3. 4. 3 Virtual Tour**

Another developing technology which will have a strong impact upon tourism is virtual reality (VR), which is a technology allows a user to interact with a computer-simulated environment. Most current virtual reality environments are mainly visual experiences, displayed either on a computer screen or through special stereoscopic displays. According to Chemistry & Industry technology news (March 2009), recently, Mobile aroma recreation system

(MARS) devices, developed by researchers at the University of Warwick, UK, could be used to recreate these detected odours for VR users in real-time with the help of electronic noses. Electronic noses could one day be incorporated into virtual reality (VR) systems to add realism to simulations of holiday experiences. The new technology will make VR much more real than ever before, enable customers to experience the whole “live” holiday at home. On one side, virtual reality leads to the risk of diminishing the interest for travel; On the other side, “Virtual Reality can be used to recreate historic sites and events for such purposes as education, special project commissions and showcase features at national and World Heritage visitor centres. VR technologies are also being used to provide a means of protecting the fragile state of some heritage sites, helping to educate visitors not so much about their history but in how to explore, interpret and respect them,” says Professor Bob Stone, Scientific Director of Virtual Presence Limited, based in Manchester, UK.

Though tour operators can't change the remote environment, they should change their strategies to adapt to the environmental changes.

### **Porter's 5 forces Analysis of the competitive environment**

UK's tour operator market is a quite mature market with four major players. After a long history of consolidation, Thomson Holidays (part of The World of TUI group), Thomas Cook, MyTravel Group (formerly Airtours) and First Choice dominate the tour operator market in UK. The industry is full of vertical and horizontal integration, vertical integration includes forward integration-acquisition of the retail network namely travel agencies, backward integration-acquisition of suppliers like airlines, hotels and

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transportation companies. Horizontal integration includes mergers between big companies and mergers between big and small tour operators.

Michael Porter (1980) developed a framework for industry competitive analysis, consisting of five different competitive forces which refer to microenvironment. The frame work is shown in the figure below:

#### **4. 1 Threat of new entrants**

Tour operator industry is an industry which has relatively high entry barriers. UK's tour operator market is quite mature and its vertical integration had finished in the 1990s. Today all major tour operators in UK are highly vertically integrated and operate their own travel agencies, airlines, hotels and resorts, transportation companies and so on. Some of the tour operators become quite large multinational enterprises, they can reduce transaction cost due to large amount of orders, they enjoy the benefits of quantity discount and economies of scale. They always have esteemed reputation for organizing good tours. When people have demands for travel, they turn to those tour operators, people recognize their brand thus will be loyal to the companies. All of the factors mentioned above reduce the threat of industry entry, however, the threat still exists. With the individualistic change of demands and the changeable nature of tourism environment, new players are entering the tour operator industry focusing on niche markets. They supply special products designed for customers with special needs. The new players always rely on product quality to gain competitive advantage as well as filling gaps between new demand and supply. Ecotourism and adventure tourism was introduced by those new players. In order to expand the market share and cope with the threat new player had brought, major player began

to purchase the niche operators, series of mergers happened within the industry: Headwater is a tour operator specialized in organizing cycling holidays and walking holidays which enables customers to explore at their own pace. Simply Travel is a leading specialist tour operator in UK offering an off-the-beaten-track alternative to the package holiday, creating inspirational holidays and providing a high-level of personal service. Thomson acquired both of the two companies as departments of Thomson Holidays; Panorama used to be the largest tour operator in Ireland for Winter Sun departures from Ireland and Irish Ski holidays, it became one part of MyTravel Group and was given the responsibility of managing Manos Holidays after it was also acquired by MyTravel; First Choice took control of Meon Holdings specialized in villa holidays and Sunsail which is a tour operator specialized in watersports clubs, Yacht charter and Flotilla sailing. Large players can enhance their brand name attractiveness and achieve a long-term sustainable competitive advantage through acquiring new specialist players.

#### **4. 2 Rivalry among existing competitors**

The industry competitive environment has changed due to industry's horizontal integration, which is a tour operator offering one or several travel products takes over another that offers very similar travel products or services. The industry's competitive environment among existing competitors used to be full of disordered competitions, players competed with each other focusing on low price, they cut their price as much as possible to gain market shares, the whole industry became profitless and all the players suffered from that. In addition, their product quality was quite

low due to the reduction on cost, they tried to keep their profits at a certain level while the prices they offered must be low. After industry horizontal integration, situation has changed: mergers and take-overs not only take place among small and large tour operators but also happen among large tour operators. According to Air Travel Organisers' Licensing (ATOL) 2007 figures, the four big players in the industry occupy more than 80% of the tour operator market shares: Thomson accounts for 28% of total market shares while MyTravel Group has 21%, followed by Thomas Cook with 19% and First Choice with the proportion of 17%. All the four big tour operators offer full-range products from domestic holidays to outbound holidays, from business travel to leisure travel, from normal sight-seeing holidays to specialist holidays, differences among the four players are not significant. Companies compete with each other mainly based on brand identity and creating brand loyalty, a good brand offers distinctiveness and consistency to its target customers, thus branding strategy becomes dramatically important in companies marketing strategy to expand market shares. MyTravel Group launched "freedom card"-a kind of bonus card offers its members discounts bonus points and upgrades in order to maintain customer purchase and loyalty; Thomson also sought a way to keep their customers loyal to the company by setting up Founders Club - new shareholders were given membership in the "Thomson Founders' Club" which offered a 10% discount on Thomson holidays. Exit barriers of the industry are high due to some reasons listed below: Though investments on non-transferable fixed assets are quite low, redundancy costs are very high because those large travel companies often have a large number of employees thus it costs a lot to dismiss employees, in addition, there will be

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significant social problems if such large companies go bust. Those large tour operators usually have close relationships with their suppliers and buyers under restricted contracts, the penalty costs would be significant if they break the contracts.

#### **4.3 Threat of substitutes**

The development of information technology especially internet has brought new opportunities and threats to the tour operator industry. Through using computerized reservation system (CRS), tour operators can obtain efficient information distribution systems and networks. Internet plays an important role in purchasing holiday products in terms of provision, accessibility and flexibility.

With the emergence of internet technology, a kind of online holiday booking website was created. It can be seen as a kind of substitute to the traditional tour operators. Online holiday booking websites like Expedia. co. uk and Lastminute. com offers designed holiday routes, air tickets booking, hotel booking and so on just like what traditional tour operators do but in another much more efficient way. Customer can gain great benefits through using the new technology on booking, they have more choices and have easier access to the holiday products. The major tour operators are not resistant to the technology and are now investing heavily on their own virtual networks: MyTravel Group announces its intention to launch a new interactive digital television channel to be called ‘ Going Places TV’ and finally it was launched on channel 669 in February 2003; Thomson, recently enhanced its main website with a series of new features and content, in an attempt to retain customers and encourage them to book through the site. It also introduced



additional editorial content to help consumers, as well as to enable the site to be picked up by Google in natural searches. Takeovers and merger are quite common: MyTravel Group acquired WorldChoiceTravel.com (WCT), a fast growing, US based provider of travel reservation services in March 2001; Thomson acquired a teletext operator – Travel House in order to gain control of the virtual marketplace.

The technology of internet makes information shared much easier and more widely than ever before, people can gain knowledge about the destination, the way to get there and accommodations there by easily clicking on the relevant websites. Information asymmetry no longer happens in recent years, the usage of tour operator becomes less and less. Cheap budget airline companies and online hotel booking websites provide travelers opportunities to get low-price air tickets and accommodations, these are really threats to tour operators. People tend to organize their own trips, they choose their own destinations, drive their own cars, book hotels from hotel websites or booking websites or even live in their own houses, they will experience more freely holidays through doing that. There is a growing trend of using this do-it-yourself (DIY) approach in travelling which could be a substitute of tour operators. Most travelers concern about price when making decisions, when there is no price advantage booking from tour operators, travelers tend to favor DIY travel. Major tour operator like Thomson, MyTravel, Thomas Cook, First Choice offer a range of products featured with free concept, with only air tickets and hotel bookings at a low price with their popular trusted brand names.

#### **4. 4 Bargaining power of suppliers**

The bargaining power of the industry's suppliers should be described as low.

On one hand, there are few tour operators in the industry to bargain with: suppliers like independent hotels and airline companies widely exist in recent times while only few tour operators are operated due to the consolidations within the industry, the suppliers don't have too much power bargaining with the major tour operators but still have certain degree of bargaining power on smaller tour operators. On the other hand, vertical integration with the hotels, airline companies and other transportation companies makes the bargaining power of suppliers at the lowest point. The backward integration enables tour operators to establish close relationships with their suppliers by signing contracts of cooperation or even the purchase of the suppliers: First Choice launched its own airline quite early in 1987 which represents the beginning of forward integration, in 2000 a joint venture with Royal Caribbean Cruises Ltd is announced and later a company called Island Cruises was set up and put into operation in 2002; MyTravel Group acquired Europe's biggest resort complex, the Bellevue Hotel in Majorca, which comprised of 17 blocks of apartments and 8 swimming pools in January 2000. In June 2001 the company announced strategic alliance with Aqua Sol Hotels Limited, a leading hotel group in the Eastern Mediterranean. The Group's in-house airlines – Airtours International and Premierair – begin to trade as “ MyTravel Airways” in May 2002. Thomas Cook owns Thomas Cook Airline and has a fleet of 45 aircrafts, the company has a partnership with SENTIDO Hotels & Resorts – the international hotel chain based on a franchise concept with 4-star plus beach hotels. The major tour operators all

participant in the dynamic areas of tourism, there are few needs to bargain with suppliers, in a simply word, tour operators are “ self-sufficient”.

#### **4. 5 Bargaining power of buyers**

The bargaining power of buyers should also be described as low. The buyers being discussed here stands for travel agencies not the ultimate customers due to the nature of the industry. The most important factor that affects bargaining power of buyers is forward integration between tour operators and travel agencies. According to Bloomsbury Business Library – Business & Management Dictionary, forward integration is a means of guaranteeing distribution channels for products and services by building relationships with, or taking control of, distributors. Forward integration can free the supplier from the threat or influence of major buyers and can also provide a barrier to market entry by potential rivals (Business & Management Dictionary, 2007). Through forward integration, major tour operators take control of the distribution channel, they can sell their products in a more efficient and cost-effective way. Forward integration of tour operators and travel agencies makes it increasingly difficult for smaller independent tour operators who can't reach their customers through high street travel agencies. As major tour operators all have their own travel agencies, independent tour operators rely on independent travel agencies. The number of independent travel agencies is declining because they can't offer customers the same discount as the integrated chains, in this case, independent tour operators can't compete with major tour operators on price, the number of smaller independent tour operators also decreases. The development of internet technology also has an important impact on the bargaining power of buyers,

it has changed the pattern of traditional distribution, shocking the market by the rapid transformations which it generates across the whole industry.

These days, the online travel market is experiencing a profound evolution.

Trends in overall online travel market size are shown below:

Now the bargaining power of buyers is being threatened by “disintermediation” – the elimination of intermediaries, for example, the wholesalers found in traditional retail channels, in favor of direct selling to the consumer (Bloomsbury Business Library – Business & Management Dictionary, 2007). The disintermediation is caused mainly by the development of internet. Major tour operators have embraced the growth of online travel systems and the need for fast and efficient distribution systems and networks, they have built their own online distribution channels like websites and