

# The Evolution of Electronic Distribution:

## Effects on Hotels and Intermediaries

The rise of internet-based room reservations presents hoteliers with a strategic challenge of controlling their distribution, while also working with intermediaries that can help sell rooms.

BY BILL CARROLL AND JUDY SIGUAW

Electronic distribution of room information, prices, and availability has changed the channels that people use to reserve hotel rooms. The most notable development is that reservations, which used to come through travel agents and hotel chains' call centers, are now being generated online by individual customers and corporate travel planners who are as likely to use online intermediaries as they are to contact hotels or chains directly. Because of the rapid evolution in electronic distribution, hotel properties and chains find themselves in an amorphous relationship with intermediaries that seek to distribute hotel rooms, including global distribution systems (GDSs), online travel-distribution intermediaries, wholesalers, travel agents, and travel planners. Consequently, as shown in Exhibit 1, electronic-distribution-channel options constitute a complex web of choices through which suppliers and buyers of hospitality services must carefully navigate to ensure favorable financial results.

To facilitate the development of appropriate channel strategies, this article reviews current practices in electronic distribution for the hospitality industry. We first discuss the various players in the rapidly evolving landscape of electronic distribution, and then examine the factors driving the changes. Next, we examine the strategies being employed by the various players as they seek control of electronic-distribution channels. Finally, we explore implications for hotel and distribution-industry executives.

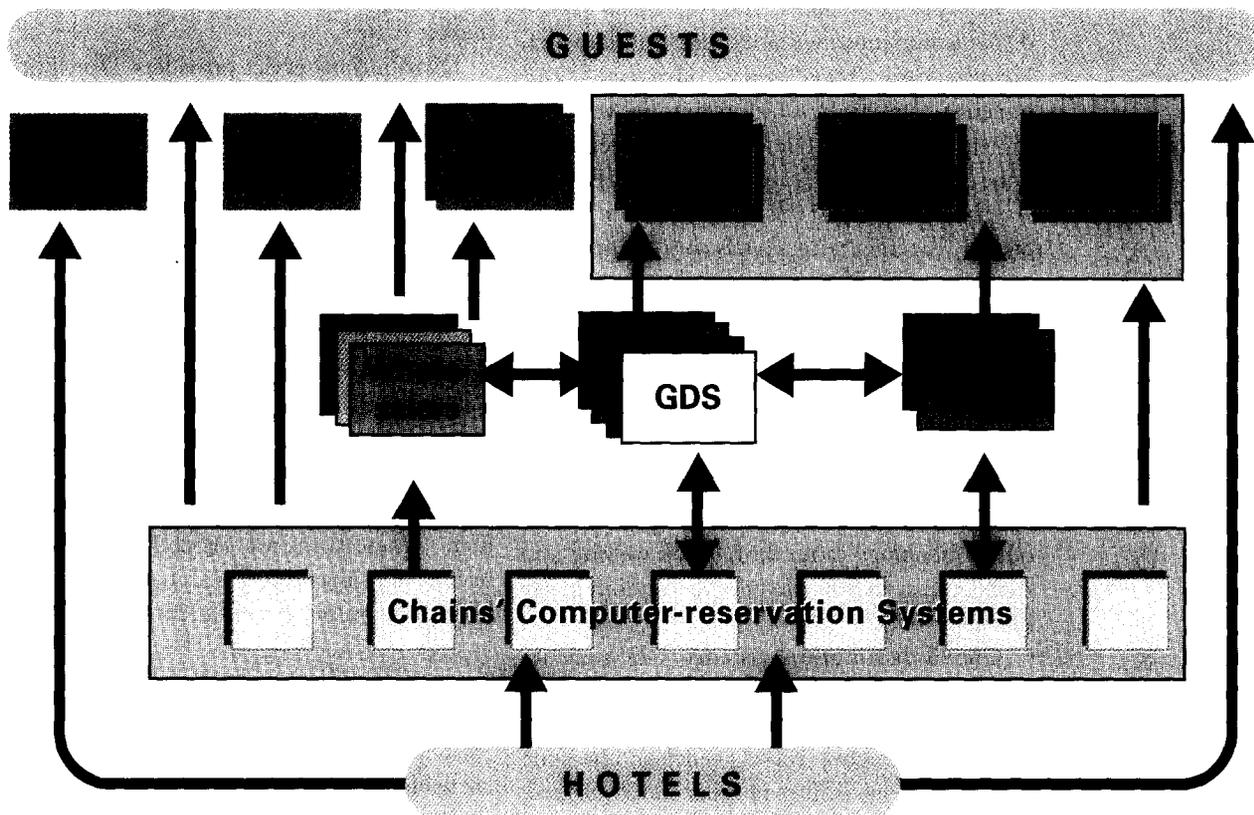
### Electronic Distributions' Emerging Dominance

Electronic hotel distribution can make booking a hotel's services more efficient and responsive, as compared to the former approaches using the telephone or mail. Consequently, by 2005 an estimated 1 in 5 hotel bookings will be made online,

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## EXHIBIT 1

## Electronic-distribution model



up from 1 in 12 in 2002.<sup>1</sup> Online intermediaries will capture about half of those bookings, while hotel chains' websites will control the other half. Most of these online bookings will be made by leisure and unmanaged business customers.

Evidence further suggests that for every booking made online, a corresponding number of bookings are based on internet research but are made via a call to a travel agent, a central reservation center, or the hotel property. Hotel-chain executives have told us that up to 20 percent of customers who look at the chain's website end up calling the chain's reservation center to make a booking.<sup>2</sup> Similarly, among online travelers (those who both traveled by air in the prior year and

used the internet in the prior month), 55 percent looked online but booked offline.<sup>3</sup> Business travelers looking to manage travel costs and improve their travel experiences are turning to the internet (or an intranet when their company uses one). That strategy places travel choices directly in the hands of travelers and travel planners who operate according to specific travel budgets and policies. Various estimates suggest that online corporate (managed) travel in the United States will be \$18 billion in 2003 and \$33 billion by 2005.<sup>4</sup>

<sup>1</sup> PhoCusWright, Inc., *Hotel and Lodging Commerce 2002–2005*, November 2002.

<sup>2</sup> Based on the authors' structured interviews with eight senior hotel-chain executives, June 2002.

<sup>3</sup> PhoCusWright, Inc., *Consumer Travel Survey*, March 2003. An online traveler is defined as someone who has taken a trip via air within the last year and has used the internet within the last 30 days.

<sup>4</sup> Max Starkov and Jason Price, "Are Hoteliers Ready to Meet the New Challenges in Online Business Travel?" *HITEC Online*, March 12, 2003; and PhoCusWright, *Online Corporate Travel 2001–2003*, January 2002, Ch. 3.

## Electronic-distribution Competitors

The firms that compete in electronic distribution are internet-based companies, GDSs, DSPs, travel agents, and the hotel chains themselves.

**Internet companies.** Internet-based travel-distribution intermediaries, such as Expedia, Hotels.com, Travelocity, Hotwire, and priceline.com, are revolutionizing the way customers choose and book hotels. Six years ago none of these companies existed. In 2001 Expedia was the eighth largest travel agency in the United States.<sup>5</sup> Together with Hotels.com, Expedia accounts for over 70 percent of online hotel bookings not made directly with the property or through hotel chains.<sup>6</sup>

**Hotel chains.** Hotel chains increasingly use their own websites, in concert with other marketing and sales efforts, to drive hotel information delivery and online bookings. Marriott reported that in 2002 over 75 percent of its online bookings came through its website and that the firm had invested over \$1 million in site improvements.<sup>7</sup>

**Global-distribution systems.** GDSs are repositioning themselves to become marketing and service companies for their suppliers and subscribers (principally travel agencies); changing their focus from airlines to other travel-industry segments; and leveraging their strong near-term cash positions to purchase or affiliate with other intermediaries to provide end-to-end links between end users and suppliers. GDSs' online connection is through their support of other intermediaries, plus mergers, acquisitions, and partnerships with selected online players. Objectives and approaches differ among the four major GDSs (as we explain below), and their evolution is still in flux.

**Travel agencies.** Traditional travel agencies (sometimes called "brick and mortar" agencies) are also transforming themselves. Faced with reduced or eliminated airline commissions, agencies are consolidating and charging fees for ser-

vices to travelers and firms. Facing financial pressure, they are increasingly using the internet as a cost-saving and service-extending tool. They are replacing commissions with incentive payments from suppliers, including hotels, for shifting market share.

**Distribution-service providers.** Distribution-service providers include large companies (e.g., Pegasus) and relatively small firms (e.g., Wizcom and Trust International). DSPs provide switches that link hotel CRSs with GDS and online sites, commission- and fee-payment services, representation services, and PMS services. Other companies, such as GetThere and Highwire (renamed Travelport by Cendant), provide services to travel agencies and businesses that facilitate travel management and enforce corporate travel policies. Finally, a set of DSPs (e.g., TravelCLICK and Leonardo) provide specific targeted services, such as competitive information and content management. These firms are searching for niches or partnerships that ensure viability in the evolving hotel-distribution environment.

## Marketing and Customer-relationship Management

Participants in electronic-distribution channels are using the internet to change the way they interact. Because the internet allows intermediaries and hotels to identify who is using the system, these electronic operators can, with users' permission, be more intimate in communications, transactions, and information gathering than has formerly been the case. Hotels and intermediaries can tailor sales and marketing efforts to users' specific needs or search criteria. System functionality allows users to target information searches, make choices, and efficiently execute transactions, whether directly or in concert with a hotel's reservations center or a travel agency's call center.

Hotels, hotel chains, and intermediaries increasingly retain information about their customers to enhance service and improve online marketing and sales efforts. Encouraging customers to manage their loyalty-program points on the website is one way that hotels do this. Some travel agencies assist their business customers by providing individualized, end-user-oriented travel-

<sup>5</sup> Top-50 Travel Agencies Survey, *Travel Weekly*, May 2001.

<sup>6</sup> *Hotel and Lodging Commerce 2002-2005*, p. 5.2.

<sup>7</sup> Jorge Sidron, "Marriott.com Posts Sales Record," *Travel Weekly*, February 24, 2003.

planning and -management applications. Such services help clients manage travel costs, enforce travel policies, and support individuals' travel planning and booking. The applications' parameters ensure that business travelers select the corporate-preferred chains and participate in prenegotiated hotel-rate programs. Companies like Cendant's Traveport and GetThere provide applications and other support for travel agencies so that the agencies can provide travel-management services of this kind.

Going a step further, travel intermediaries use customer-preference information to offer tailored packages and content displays to encourage bookings and to improve look-to-book ratios. Additionally, travel and meeting planners use the websites' on-screen tools to make choices about facilities and services. In addition to providing information, the websites facilitate planners' decision-making and help them manage their events (see the box, starting on the next page, that shows some of the services offered to travelers and meeting planners from several websites).

### Economic Incentives for Shifts in Distribution

Without doubt, economic pressure is driving many of the changes in electronic distribution, as we explore next.

**Hotels and chains.** Hotels and hotel chains are using electronic distribution to reduce costs by shifting transactions from intermediaries to the hotels' own facilities through direct connections and websites. This saves intermediaries' fees, including travel-agency commissions of 5 percent to 10 percent and GDS fees of \$3 to \$5 per transaction. The hotels also gain some call-center productivity when callers have already checked information on the web and thus do not make information-only calls and instead make brief booking calls.<sup>8</sup>

Besides reducing costs, electronic distribution can enhance customer retention. For business customers, this means effective corporate-traveler programs—typically offering reduced rates based on anticipated volume in connection

with a hotel's reduced distribution costs. For leisure and unmanaged business customers, chains promote loyalty programs with their websites, employ a portal strategy, and use internet-based marketing to encourage customers to visit their site and choose their brand rather than a

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competitor's. For event planners, hotels assist with improved facility selection and meeting management. Not only does that encourage brand loyalty, but failing to offer such functionality may put the chain at a competitive disadvantage.

### Online Travel Agencies and Wholesalers

Intermediaries, too, have an economic incentive to shift distribution—namely, the desire to extract more revenue from both hotels and customers.

Expedia, for instance, has taken an industry-leadership position in deriving revenue from hotel-distribution displays and transactions. From September 2000 through August 2002 Expedia's revenue from hotel bookings grew from less than one-third of total revenue to over 60 percent.<sup>9</sup> Online wholesaler Hotels.com, which like Expedia is a subsidiary of USA Networks, grew its revenue by 70.4 percent for the nine months ending September 2002 over the same period in 2001.<sup>10</sup> Dramatic revenue growth for both firms came primarily from hotel reservations. Each gives users access to low-price rooms online, along with the ability to compare properties and prices for selected destinations. Both negotiate net rates from hotels with mark-ups in the range of 20 percent to 30 percent.

*text continues on page 44*

<sup>9</sup> Expedia.com, "Investor Relations," *Financial Reports*, Fiscal Year 2002.

<sup>10</sup> Security and Exchange Commission Filing: Hotels.com, quarter ending September 30, 2002.

<sup>8</sup> Based on the authors' structured interviews with eight senior hotel-chain executives, June 2002.

## How Electronic Distribution Affects Marketing and Customer-relationship Management

On these two pages are examples of how hotel chains are attempting to develop customer-relationship strategies using the worldwide web.



▲ Marriott.com's home page

Marriott.com's home page allows users to easily find and book a hotel, or to visit other web pages where they can:

- book special offers for weekends and weekly getaways, including packages with airfare and car rental;
- search for activity-based holidays such as golf and spa services at Marriott properties;
- manage Marriott loyalty points; and
- search and evaluate Marriott meeting sites and facilities, including associated planning tools and requesting a proposal from Marriott.

Marriott.com also offers a full set of similar tools designed for use by travel agents.

Marriott's on-line services for meeting planners (see example at left) allows them to share data to assist in decision-making and event management.



Marriott.com's meeting planners' page

#### ◀ Expedia's home page

Offering a broad portfolio of travel services, Expedia's site allows users to search for and book flights, hotels, cars, and cruises independently or combined with one another in user-designed packages. Expedia also offers special-interest packages for golf, spa, romance, and weekend getaways. The site promotes last-minute offers and provides such traveler services as weather, currency exchange, and directions.

#### ▲ Travelport's services to business clients

The Cendant subsidiary Travelport offers internet applications to travel agencies, so those agencies can, in turn, offer travel-management services to their business clients.

#### ◀ Site59's customer-registration page

Site59, a last-minute weekend-getaway site, allows the user to register for e-mail updates on various experience-oriented getaways.

To accomplish their net-rate-with-markup strategy, Expedia, Travelocity, and Hotels.com show their merchant properties first—and not necessarily in ascending price or quality order. Hotels.com does allow users to sort by price or quality rating, but Travelocity allows neither one. Given that hotels want to appear as early in the list as possible, controlling the order in which hotels are present on the screen gives intermediaries negotiating leverage with regard to hotels' rate and inventory availability.

GDSs are altering both the way they display information and how they derive revenue from hotel-room distribution, and they are expanding their activities to include ownership of and alliances with online agencies.

Priceline.com and Hotwire have wholesale programs similar to Travelocity's. For closely located and classified properties, Priceline.com offers marked-up net-rate supplier inventory closest to the users' bids. Hotwire displays only one property per location and hotel class—presumably, the one that offered Hotwire its best net rate.

**Global distribution systems.** GDSs currently account for an estimated 15 percent of hotel revenues.<sup>11</sup> GDSs, too, are altering both the way they display information and how they derive revenue from hotel distribution. Their user base of traditional travel agents is declining along with their erstwhile primary revenue source, airline fees. To sustain revenues, the GDSs (namely Sabre, Galileo, Amadeus, and Worldspan) are turning to hotel bookings and the provision of services to their travel-agency base. The GDSs are expanding their activities to include ownership of and alliances with online agencies. Sabre, for instance, owns Travelocity and GetThere, a business-oriented site. Galileo is owned by Cendant, which also owns Trip.com and Cheap Tickets, both consumer-direct portals, and Travelport (formerly Highwire), a business-oriented online travel agency and service pro-

vider; and Lodging.com, an online hotel-room wholesaler. Amadeus owns OneTravel.com, an online wholesaler; e-Travel, a business-oriented online agency; and several online leisure-oriented agencies. Worldspan, the smallest GDS, has taken an alternative tack, however. It has shunned expansion as a distributor and aims to be "a travel-technologies-services company."<sup>12</sup>

In addition to expanding their activities, the GDSs are improving their ability to influence hotel bookings through their displays. Sabre introduced Sabre Exclusives in 2002, a program similar to one of Expedia's, which allows hotels to appear relatively high up on the list presented to travel agents if the hotels give Sabre favorable net rates. Sabre marks up those net rates by 20 percent to 40 percent to its travel-agent subscribers. Sabre retains the residual revenue after waiving the booking fee and paying the agency a commission on the hotel's behalf. To encourage agency use, Sabre offers a reward program for agents who book "Exclusives" inventory.

With the Sabre Exclusives markup, hotel chains pay a relatively high price to get a prominent display position. It would cost the hotel more to agree to a net rate with a 20- to 40-percent markup than it would to provide the same (full) rate itself or to offer that rate through a traditional travel agency. That calculation works as follows. Say that a hotel wants to sell a two-day booking at \$125 per day. If the hotel sells that booking directly it takes in roughly \$250 (less variable costs). If sold through a travel agent, that booking would net \$222 (\$250 less a 10-percent commission—\$25—and a transaction fee of \$3). If the same booking (that is, a \$125 daily rate) is sold using Sabre Exclusives with a 30-percent markup, the hotel chain would take in \$192.30, because the net rate provided to Sabre would have to be \$96.15 per day.

Despite the economics behind that calculation, the question becomes whether a hotel can afford not to participate, provided it wants to encourage distribution of rooms via Sabre. The GDS's display shows the Sabre Exclusives prop-

<sup>11</sup> *Hotel and Lodging Commerce 2002–2005*, pp. 4–10.

<sup>12</sup> According to Paul Blackney, CEO of Worldspan, PhoCusWright Executive Conference, 2002, November 16, 2002.

erties first, even if their rates are higher than the rates for the same rooms listed in Sabre by the properties themselves. It's fair to say that the hotel chain is paying for enhanced positioning through that program.

The actual amount of revenue received by an individual property through wholesale programs like those of Sabre, Expedia, Travelocity, and Hotwire cannot be easily determined by outsiders. The net revenue depends on the financial arrangements between chains and their properties, deals negotiated between the chains and the wholesalers, and whether the properties are dealing directly with the wholesalers or through their chains. If a property deals directly with an online intermediary and is able to by-pass financial payments to the chain (e.g., through a reservations-based fee structure), wholesalers' contributions to revenue can be better for the property than is the hypothetical calculation we gave above.

Further muddying the matter of revenues and markups, some wholesalers (and online agencies) have a strategy that calls for rapidly expanding the number of properties participating on their site. That entails dealing with the chain rather than with individual properties as a way to accelerate participation. If the wholesaler feels that it can increase the number of properties or reduce its sales cost, it might be inclined to negotiate a better deal with the chain than it offers individual properties. Again, such confidential deals make it difficult to determine the economics of property-level distribution. As a final point, the dynamics among properties, chains, and wholesalers are placing pressure on chains to demonstrate their value to properties relating to wholesaling and distribution—thus further roiling the negotiations picture.

While the other GDSs have not followed Sabre's lead in promoting a pay-for-position approach, they are acutely aware of their transaction and distribution value to hotels. For example, Cendant offers end-to-end service from switches (e.g., Wizcom and Trust International) through Galileo to Cendant's online leisure portals (i.e., Trip.com, CheapTickets, and Lodging.com) and its travel-agency service, Travelport. As well, Cendant supports a traditional off-line call center, Trilegiant. With a verti-

cally integrated distribution network, Cendant is able to offer multi-faceted deals to hotels and chains that integrate end-to-end distribution. Deals are brokered based on Cendant's ability to shift share, reduce distribution costs, and generate revenue at lower margins than competitors can offer.<sup>13</sup>

**Traditional travel agencies.** Even traditional agencies are looking for ways to exploit the internet, grow their share of revenues from sources other than airlines, and implement

**Traditional travel agencies are looking for ways to exploit the internet, grow their share of revenues from sources other than airlines, and implement alternative-pricing schemes.**

alternative-pricing schemes. Unlike online agencies and wholesalers, traditional agencies' objective often is not to sustain growth and profits so much as simply to survive the loss of airline commissions.

As we indicated above, travel agents' difficulty is a result of the changes in airline commissions, the agencies' former revenue mainstay. In 1999 domestic-airline revenue was 53 percent of travel-agency revenue. In 2001 that figure had dropped to 45 percent—a 15-percent drop in just two years—and airlines have continued to diminish their commission payments.<sup>14</sup> To build other revenue sources, agencies started charging user fees for many transactions, and also sought increased fees and commissions from hotels, cruise lines, and companies involved in travel packages. To earn override commissions, the largest agencies and consortia are offering to shift their considerable customer base from one supplier to another, including hotel chains. Some mega-agencies (notably Carlson Wagonlit) have actually begun to take on inventory risk (for instance, buying wholesale cruise-cabin inventory) to get lower net

<sup>13</sup> According to Michael McCormick, executive vice president, Hospitality and Leisure Services, Cendant Travel Distribution, March 31, 2003.

<sup>14</sup> *Travel Weekly 2002 Travel Industry Survey*, August 2002.

rates from suppliers and then using their sizeable market reach to sell that inventory at retail.<sup>15</sup>

Along that line, large travel agencies, such as American Express and Carlson, maintain their own websites. As with other websites, these are intended to enhance service delivery, reduce costs, and retain business. They allow clients to make a booking online; search for a weekend getaway; plan a vacation; or obtain information about a destination and its attractions, restau-

To counteract intermediaries' attempts to control distribution channels, hotel chains are enhancing and promoting their own websites; managing access to low-price inventories; and shifting transactions to their own distribution channels.

rants, and entertainment venues. Essentially, mega-agencies and consortia are exploiting the internet's interactive display to market themselves and to personalize their message and eliminate the costs of having live agents interacting with and providing information for clients. Exhibit 2 shows the sort of information and functionality available on the Rosenbluth site, for instance.

### Challenges and Competitive Strategies

To counteract intermediaries' attempts to control distribution channels, hotel chains are enhancing and promoting their own websites; managing access to low-price inventories; and shifting viewership and transactions to their own distribution channels. For example, Choice, Cendant, Starwood, and Six Continents have programs that reward customers with the lowest available rate for booking on their sites instead of those of intermediaries.<sup>16</sup>

Five major chains—Hilton, Hyatt, Marriott, Six Continents, and Starwood—have joined with Pegasus to form TravelWeb, an online booking engine that will offer the lowest online rates and

serve as a quasi-switch for the hotels' wholesale inventory. By being a portal that can accept higher net rates than will its competitors, TravelWeb has the potential to place pressure on margins sought by companies like Expedia and Hotels.com. TravelWeb, acting as a portal, can offer prices plus terms and conditions that are more favorable than those offered by competitors. Further, acting as a quasi-switch, TravelWeb could facilitate inventory management across all portals.

In principle, TravelWeb is a good idea for its partner hotel chains. The question is whether the benefits will outweigh the costs to promote, develop, and maintain this site and infrastructure against already established and well-funded online intermediaries. As well, TravelWeb is made up of rival hotel chains that must cooperate in the development and promotion of the enterprise.

**Distribution challenges for properties.** Individual properties face two major challenges from electronic distribution: (1) control over price and availability and (2) the management of website content. To maintain price control, properties and the chains that operate them must structure rates effectively, apply terms and conditions to avoid dilution and arbitrage, monitor competitiveness, and manage rate accuracy and availability.

The chief problem with pricing is that internet searches have made pricing structures nearly transparent. With a few key strokes and no training, a motivated consumer can search for the lowest rate for hotel accommodations at a specific location (or at several locations) and for a specified quality level. The consumer is then free to book through the site of her or his choice—and not necessarily the one where the low price was first discovered. Alternatively, the customer (or his or her agency) can compare the rates being offered at third-party sites to some pre-negotiated, brand-specific corporate or group rate; compare those rates to the prices listed on the chain's or property's own website; and, finally, call the property or chain directly to negotiate an even lower rate.

That same transparency applies to rate competitiveness. Except as noted above, most of the major sites allow users to sort hotel properties in low-to-high-price displays (or by quality level) for a specified location. In such displays, uncom-

<sup>15</sup> "Carlson Wagonlit to Manage Risk Inventory," *Travel Weekly*, November 7, 2002.

<sup>16</sup> Motoko Rich, "Hotels Offer Price Guarantees to Undercut Travel Sites," *Wall Street Journal*, March 12, 2003.

## EXHIBIT 2

## Incentives for shifts in distribution



The Rosenbluth International home page shows the information and functionality typically available on websites of large travel agencies or consortia. Rosenbluth was recently purchased by American Express.

petitive pricing is immediately visible—resulting in two negative outcomes for a high-price hotel. First, it probably loses the booking to a competitor, and (worse) frequent uncompetitiveness risks future exclusion from equivalent quality searches or choices. In such an environment, competitiveness, consistency, and accuracy of rates displayed and made available via multiple channels must be managed effectively.

**Resisting commoditization.** Perhaps the greatest threat from electronic distribution is the risk that consumers will come to view hotel services as commodities to be purchased only according to price. This fate befell the airline industry when its operators started competing almost solely on price—with consequences still being felt today. Far from being a commodity, a hotel's service involves many dimensions beyond location—among them, the cleanliness and appointments of guest rooms, lobby ambience and space, and the property's services. If hotels can

promote these dimensions through their websites (or through those of third-party intermediaries that support extended content), that information can influence guests' choices.

Our review of major chains' websites and those of major online agencies shows that the industry is well aware of this principle of differentiation. The sites we examined make extensive use of information and multimedia displays to create a full and differentiated picture of the hotel experience. As with pricing and availability, chains and properties must effectively manage the content on their branded displays, as well as those posted by intermediaries. Obviously, inaccurate or uncompetitive displays will affect consumers' choices. Based on our discussions, industry executives believe that to be the case.<sup>17</sup>

<sup>17</sup> A fruitful area for future research is measuring the return to travel suppliers of accurate content in online displays.

**EXHIBIT 3**

Competitive business-client strategies in electronic distribution

Cendant's Travelport, an online business-oriented agency service provider, ascribes a number of benefits to using its booking engine, as shown here (at right).

Similarly, Hilton's web pages (below) are designed specifically to attract and serve its business clients.



Travelport's booking-engine benefits ▶



▲ A web page for Hilton's business travelers

Wholesaling goes mass market. One of the more recent and, perhaps, most problematic pricing issues for hotels is the development of online mass wholesaling. Hotels have used wholesaling for many years, mostly with selected operators and locations. Expedia, Travelocity, Hotwire, Hotels.com, and, most notably, priceline.com have taken the practice to a mass market.

Because it is a great threat to maintaining ADR, mass wholesaling in its many forms must be carefully managed by the industry. While mass wholesaling may be a necessary, market-clearing evil in an occupancy downturn (or a cunningly designed growth strategy for intermediaries), both the margins and the extent of electronic wholesaling need to be controlled. The chief problem with mass wholesaling is the transparency of pricing that we just discussed. Customers will inevitably discover large differences between wholesale and other (retail) rates—encouraging arbitrage and diluting rates in the absence of appropriate rate fences.

Wholesaling is insidious. While discounted prices can be used to clear the market of unsold inventory, wholesaling is typically intended to steal customers from competitors. In that regard, it works only as a short-term tactic. As the practice spreads and additional competitors participate, the potential for creating incremental revenue diminishes. A long-term danger of mass wholesaling is commoditization, as we just discussed. Certainly, the internet has the potential to deliver visually rich and personalized content. Yet if the message that consumers receive is essentially a "price only" message, the value-added aspect of hotel selection is compromised. Moreover, customers will use the low, wholesale-driven prices as their benchmarks for future prices.

Even more problematic for chains is the matter that third-party providers themselves effectively become a brand. As entities like Expedia become prominent in the consumer's mind, those entities are identified as brands in their own right. To the extent that they can produce bookings and supply other services, they could become an alternative for chain membership by properties.

The challenge for hoteliers is to emphasize both the value and the price aspects of hotel selection, even if they are forced into wholesaling. Although hoteliers should always try to attract users to their own websites, they should favor wholesalers that offer value-adding options when wholesaling is necessary. As an example, Travelocity and Expedia offer expanded-content displays coupled with increased flexibility in inventory and net-rate management. Their displays allow individual properties to show multiple rates that include extensive information (to explain the differences in the rates).

**Unmanaged-business segment.** Properties, chains, and intermediaries all have their sights set on the unmanaged-business segment, comprising business travelers who have their expenses reimbursed by the firm, but are not subject to formal travel policies (or are covered by policies that are not enforced). This segment represented 11 percent of travelers in 2000, or an estimated \$20.5 billion in travel spending in 2003.<sup>18</sup>

<sup>18</sup> PhoCusWright, *Online Corporate Travel 2001–2003*, January 2002, Ch. 3.

Both online and traditional travel agencies see opportunities in providing travel-management services to unmanaged business clients. As well, they see opportunities for using the internet (or an intranet). Agencies can generate additional user-fee revenue by providing cost-saving services and can improve margins by offering favorable supplier deals for their unmanaged business clients. Intermediary services include (1) enforcement or reporting of travel-policy compliance;

Chains can and do offer services to businesses via their internet sites to reduce their own costs and to create brand and service loyalty.

(2) management of travel to preferred suppliers and pre-negotiated (reduced) rates; (3) comparison of (private) negotiated rates with public rates to find the lowest price; (4) use of rates negotiated with preferred suppliers; and (5) provision of support services for travelers. For the client these services can provide savings, convenience, and improved control over travel expenses.

To the extent that the internet (or an intranet) is used for self-booking and direct links are provided to suppliers, further savings are possible. Chains can interact directly with business clients to offer lower rates for self-booked and direct-connect reservations, thereby reducing the chains' costs by bypassing intermediaries. Chains can and do offer services to business via their internet sites to reduce their own costs and to create brand and service loyalty. Agencies that track customer use for their business clients can help those clients get rate concessions from hotels and chains or aggregate sufficient volume themselves to negotiate lower rates for their business clients. Exhibit 3 shows examples of the services provided by agencies and the chains themselves for business clients.

Advantages for the unmanaged business traveler and travel planner are mixed. On the one hand, agencies provide applications that (1) allow travelers to plan, book, and change their itin-

eraries (within travel-policy guidelines), (2) produce online (always available) travel reports, (3) generate on-the-spot expense reports for travelers, and (4) provide online support for travelers (e.g., detailed maps and destination information). On the other hand, the traveler or travel planner gives up the convenience of having an actual travel agent handling all the arrangements. Given the savings and potential advantages of online travel management for the business client and his or her agency, the adoption rate (the percentage of eligible travelers who use the internet in this way) is increasing at an estimated 20.3 percent.<sup>19</sup>

Hotel chains also see the unmanaged-business segment as a target. Rates charged to this segment are likely to be higher than are those offered to large corporate accounts. In soliciting the unmanaged traveler, chains see the obvious benefit of wooing business from the competition. Finally, by encouraging direct booking, chains avoid intermediary payments and, over time, create a loyal relationship with the client or business traveler. As shown in Exhibit 3, chains such as Hilton have specifically designed their sites to offer advantages and services for this target segment.

### Looking Ahead

Based on our review of trends in electronic distribution, we see the following developments on the horizon.

- (1) Expect hotel chains, the GDSs, and (perhaps) TravelWeb to challenge the current major online retailers and wholesalers. Hotel chains will continue to invest in their own websites and offer direct links to selected customers and wholesalers.
- (2) As the economy (and hotel demand) improves, rising occupancy will reduce the markups required by wholesalers, along with the need for wholesaling in general.
- (3) While hotels will continue to be successful at building business on their websites, growth will not come at the

expense of online travel agencies. Leisure travelers prefer having the wide property selection that is available through third-party online retailers.

- (4) Hotels' commission payments to intermediaries will give way to pay-for-performance programs aimed at shifting market share and providing other value-added services.
- (5) Chains will challenge travel agencies and GDSs on service and sales to the small and medium-size enterprise market as a way to continue growing.
- (6) As the distribution picture becomes increasingly complicated, hotels will gain experience in effectively managing price, availability, content, media, and display positioning in many distribution channels. New DSPs will emerge, and existing companies (e.g., Pegasus, Wizcom, and Trust International) will expand their services to help properties and chains implement their goals.<sup>20</sup>

Armed with sophisticated information and enjoying the rising occupancy that accompanies a recovering economy, hotels will slowly but steadily gain improved (but never complete) control over their pricing and inventory. ■

<sup>20</sup> A set of "middleware" providers are linking systems for property management, revenue management, and content management to enhance inventory and price control.



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<sup>19</sup> *Ibid.*