Modelling the Structure of the Korean Package Tour Industry in Australia

Abstract

This paper examines the structure of the Korean package tour industry in Australia. Because of the demand by Korean consumers for cheap package tours, Korean tour wholesalers have lowered the wholesale package price to travel retailers to maintain market share. Rather than suffering a fall in profit from lower receipts, the Korean wholesale sector has forced the Inbound Tour Operator sector in Australia to absorb the cost of low retail prices. Unable to absorb lower revenue, the Inbound Tour Operators have been forced to recover losses through a range business practices that include the payment of commissions from tourist specialist shops, reduced tour quality and forced shopping. The operation of the Korean inbound market that facilitates the operation of such business practices is modelled in this paper.

Key Words: Package tours, Inbound Tour Operators, Korea, Australia

Introduction

Consumer satisfaction is a key indicator of the ability of a destination to deliver an appealing product for tourists and is an indicator of the ability of a destination to deliver on promises made through destination marketing. Sustained growth is more likely to occur in markets where consumers are satisfied (Heung and Qu, 2000). In recent years there has been growing criticism of the business practices used by operators in the cheap package tour market from Korea, as well as from China and Taiwan. Where unsuitable business practices impact adversely on consumer satisfaction, the reputation of the destination may decline, leading to a fall in visitor numbers. This paper develops a model of the operation of business practices used to sustain the incomes of Inbound Tour Operators (ITOs) operating Korean package tours in Australia.

Package tours are tours where members travel in a group, pay for a bundle of travel services including airfares, accommodation, meals and transport and are escorted by a guide over the course of the tour. Such tours provide an opportunity for ITOs to employ a range of business practices to minimise their costs while maximising revenue. Strategies such as directing group members to specific shops in return for a commission have been cited as evidence (Whipple and Mach, 1988) of the type of business practices which may lead to a diminution of overall consumer satisfaction with Australia or any other country where such practices are employed.

A number of reports (TQ, 1999; CIE, 2000; ATC, 2003; BTR, 2004) have examined the impact of business practices in the inbound package tour market and have found serious grounds for concern that such practices were having a negative affect on customer satisfaction. Unfortunately, these reports failed to look beyond the Australian element of the package tour and ignored the impact of price in the origin markets. While not extensively debated in the literature, a number of authors (Prideaux and Kim, 1999: Kim and Sohn, 2002; Tse, 2003) have identified problems that have arisen in inbound markets as a result of such business practices.

Methodology

This research identifies relationships between the various participants in the inbound market and proposes a model to illustrate the relationships between the various components of the Korean package tour sector in Australia. The research team undertook a review of previous reports on the issue and conducted semi structured interviews with government officials, tour guides involved in the Korean inbound market, inbound operators and representatives of companies involved in supplying goods and services to inbound operators in the Korean market. Interviews were also conducted in Korea with representatives of firms and organizations conversant with the operations of the Korean outbound sector.

Causes of the Business Practices

A package tour typically includes airfares, accommodation, guides, sightseeing, tour escorts and transfers. In many cases, the package will also include meals and entrances to attractions in the destination country. It is also common practice to offer optional extras such as supplementary attractions, cultural shows and visits to superior restaurants. Such elements are priced outside the standard tour inclusions to minimize the initial purchase price. As a consequence, tourists have two travel budgets, the first covering the cost of the package tour, and the second to cover holiday expenses including shopping. In normal circumstances there is minimal intersection between the two budgets, except in cases where tour guides take tourists to specific shops (or other businesses) and receive a small commission. The emergence of the business practices identified in this research is linked to changes in the nature of the relationship between consumers, retailers, tour operators, ITOs and wholesale companies as well as to government regulations. Often the changes are the result of competitive pressures in the generating country, particularly in the retail and wholesale sectors. Although the relationships in the travel supply chain that occur in the generating country may impact on the destination country, the tourism industry operators in the destination country have little ability to influence the nature of these relationships . Where ITOs are price takers rather than price makers, the pressures emanating from the supply chain in the origin country become even greater. Based on the findings of previous reports and the findings of this research, the major factors that cause the development of business practices in the Korean market include:

- The nature of the market power relationships exist between Wholesale Travel Agents (WTAs) and Retail Travel Agents in Korea and ITOs in Australia.
- High competition among retail travel agents in Korea with WTAs forced to lower their prices to capture business. WTAs may either lower the overall quality of the package tour product or pass the price cuts down the supply chain by reducing the daily rates paid to ITOs
- Profit taking by WTAs in Korea has occurred at the expense of ITOs
- The short term profit horizons of many product suppliers in Australia
- In Australia, there is no requirement for tour guides to hold a licence as a condition of employment and the inbound market is poorly regulated

- High percentage of Koreans travelling on package tours
- Little experience in travel by Koreans generally and limited access to independent advice on the destination (CIE, 2000).

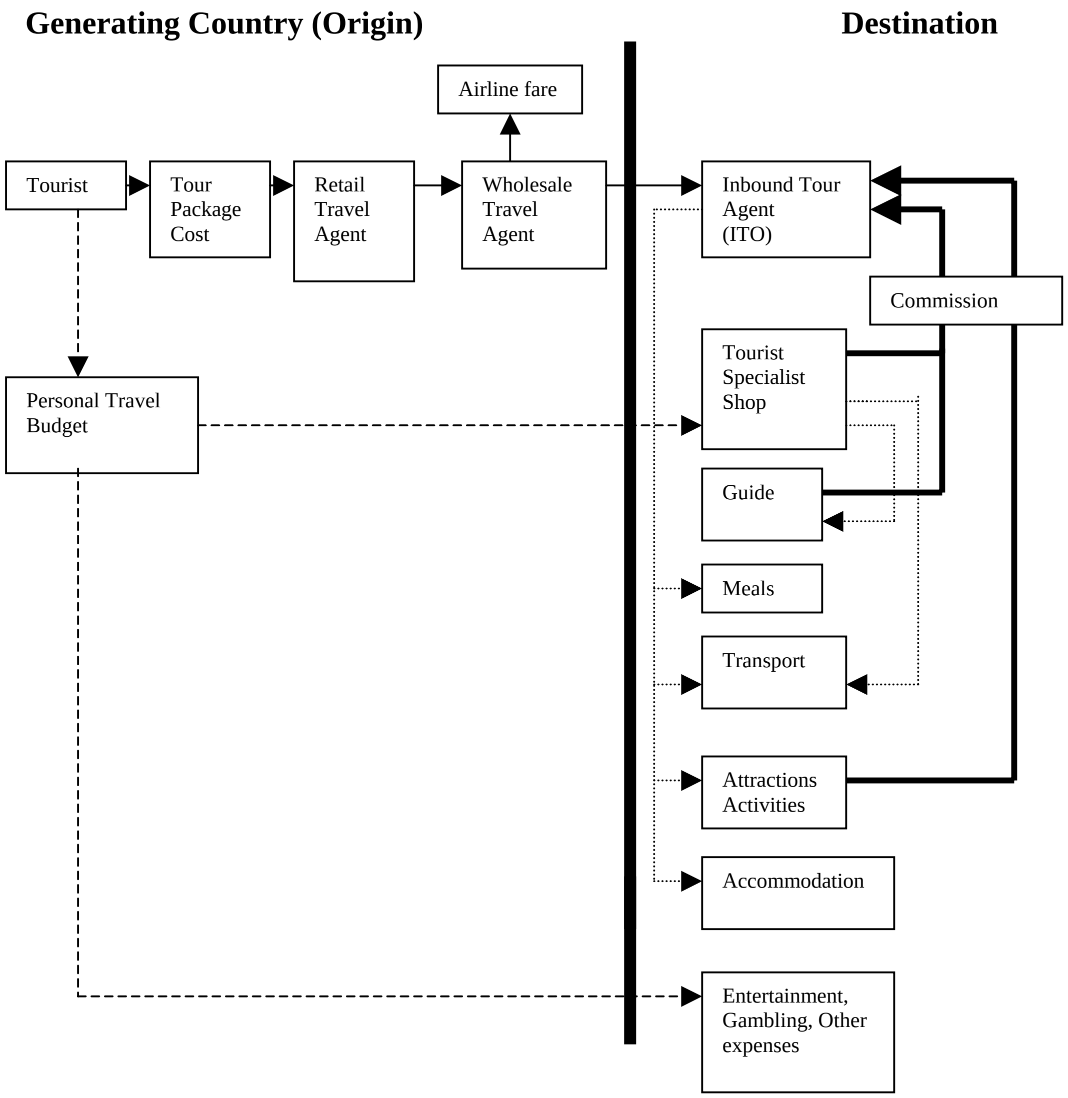
How The Business Practices Operate

In Korea where price, rather than quality is the key selling point of package tours, the supply chain has responded in a manner that minimises the initial price of package tour and pushes the revenue shortfall to the destination country, in this case to Australia., The remaining elements of the supply chain then engage in business practices to recover these losses. The revenue losses incurred by Korean WTAs because of the low retail prices of package tours are then pushed onto the destination country through the payment by WTAs of daily tour fees that are below the daily costs incurred by ITOs. The methods used by ITOs to recoup losses from low tour fees include negotiating lower room rates with hotels, using hotels of a lower standard than advertised, shopping commissions, forcing guides to cover their wages through tips and on-selling the right to direct customers to tourist specialist shops by tour guides. Shopping commissions are the most common business practice and involve the ITO negotiating with specific shops to pay a commission for each sale to a tour member and/or negotiating with tourist shops to provide a range of services including guides and coach transfers at no cost to the ITO. Where shopping commissions are used as the primary method of recovering ITO costs, package tour members are given minimal choice about the shops which they visit and accommodation is usually arranged at hotels that are some distance from tourist shopping precincts. In Asian cultures where the purchase of gifts for relatives and associates is a cultural requirement (Hobson, 1966) the ability of ITOs to gain substantial commissions is higher than in markets where there is no cultural requirement to purchase gifts.

When shopping is controlled by ITOs, the practice of ‘over-shopping’ emerges and generates negative impacts on the visitor experience. In some cases, the combined self-interest of the tour operator and retailers will create pressure to increase the amount of shopping within the tour. By reducing the range of other activities previously promised to tourists, they may hope to maximise the revenue from tourist purchases. This may result in a negative overall tourist experience. Pan and Laws (2003) have investigated this situation in Australia and have found that it is imperative to establish benchmarks for the standard of services offered to visitors if Australia is to retain its competitive advantage as a tourism destination. Another practice that is sometimes used is to combine the roles of guide and driver.

According to industry sources, Duty Free shops have developed a pivotal role in the operation of inbound tours to Australia. In some cases Duty Free shops (tourist specialist shops) have evolved into de facto ITOs, arranging many elements of the itinerary. Another reported practice involves specialist shops paying a predetermined price or poll tax. This practice delivers exclusive rights to shops over the travel itinerary. In such situations, the tourist specialist shop may assume responsibility for providing the guide in the destination country and for arranging coach transfers. The shop pays the guide a fixed daily amount or, more commonly, a commission. In these circumstances the guide is acting as a de facto salesperson on behalf of the tourist shop.

Figure 1 **Operation of the Korean Inbound Industry in Australia**



A number of difficulties arise when the traditional role of guides changes and guides are representing the interests of a third party rather than the interests of the tour group members. These include the possibility of unethical advice being provided to tour members with a view to encouraging them to purchase goods thereby leading to higher commission payments for the guide. Some of these issues have been highlighted by Xu and Weiler (2000).

The explanation for continued support of low cost package tours is, to a large extent, found in the nature of Korean society.. Many Koreans have a poor standard of oral English although they may have some competence in written English. Package tours are particularly popular because they minimize the need for tourists to communicate with citizens of the host country. The collective nature of Korean society which underpins the continued popularity of group travel may also be important (Kim and Prideaux, 1999).

Tourist specialist shops operating in the Korean inbound sector usually employ staff who speak fluent Korean. Aside from the importance of being able to communicate in their own language, the ability of staff to explain the benefits of particular items is important, particularly when they are purchased as gifts The purchaser is expected to be able to explain the quality and purpose of the item to the person who is considering its suitability as a gift.Korean travel industry. Stakeholders also indicated that in general, Korean consumers have little confidence in the capacity of non- Korean speakers to supply them with the advice required to make an informed purchase, particularly in the case of health products.

Figure 1 outlines the structure of the relationships between the various sectors of the Korean inbound market and illustrates the convergence of the travel and shopping budgets. This has come about as the retail cost of an Australian package has fallen to near or below cost., The losses have been carried by the ITO sector. To offset these losses, ITOs have developed business arrangements with tourist specialist shops exploiting their monopoly over shopping opportunities for group members in exchange for an agreed payment. In effect, the customer is paying higher prices for goods purchased at tourist shops to offset the low tour package prices paid in Korea. In the longer term, visitors derive no benefit from low retail package tour prices and, because of the inefficiencies inherent in this system, ultimately pay a higher price.

Conclusion

If the current practice of Korean WTAs pushing revenue shortfalls onto the Australian ITO sector is corrected, it could eliminate the need for ITOs to resort to business practices to boost revenue to make up for the cost-push from the origin market. While not addressed in this paper the issues involved will undoubtedly require government intervention including the licensing of tour guides and penalizing guides and ITOs who participate in these practices. More effective consumer legislation is also required in Korea to eliminate the unsustainable practice of under-pricing the retail cost at the point of sale but recovering the loss at the point of delivery. While the current situation in the Korean inbound market relates back to the retail practices of travel agents in Korea, the willingness of ITOs in Australia to accept below cost ground fees is a contributing factor. If ITOs resisted the pressure to accept loss making ground fees, the need for business practices would disappear. However, in view of the relative power imbalance between the ITO and WTA sectors this will only occur if more rigorous regulations are introduced.

The danger for Australia is that without corrective action, the various practices used by ITOs to generate revenue will lead to increased consumer dissatisfaction which will ultimately translate into reduced package tour demand..

References

Australian Tourist Commission, 2003. Assessing The quality of the Chinese visitor experience in Australia, visitor satisfaction modeling. *Teleconference Presentation To ATC Asia*, 9 May 2003, Sydney, ATC.

Hossain, A. and Bolin, R., 2004. Report on dissatisfied visitors on guided group holiday tours: responses by visitors from Japan, Korea, China and Taiwan. Canberra: Bureau of Tourism Research.

Centre for International Economics, 2000. *Regulatory options for inbound tour operators*. Sydney: CIE.

Heung, S. and Qu, H., 2000, Hong Kong as a travel destination: an analysis of Japanese tourists' satisfaction levels and the likelihood of them recommending Hong Kong to Others. *Journal of Travel and Tourism Marketing*, 9, (1/2), 43-56.

Hobson, J.S.P., 1996. Leisure shopping and tourism: The case of the South Korean market to Australia. *Turizam*. 44 (9-10), 228-244.

Kim, B-S, and Sohn, dehyun, 2003. Price Competition in the Korean group package travel industry and consumer damage: a triangulation approach, First Asia Pacific Forum for Graduate Students Research in Tourism, 22 May, Tourism Activities Centre, Macao SAR, The Hong Kong Polytechnic University, pp.592 –601.

Pan, G and Laws, E., 2003. Tourism development of Australia as a sustained preferred destination for Chinese visitors. *Asia Pacific Journal of Tourism Research*, forthcoming.

Prideaux, B. and Kim, S. M., 1999. Bilateral tourism imbalance – Is there a cause for concern? The case of Australia and Korea. *Tourism Management*. 20(4), 523-532.

Tourism Queensland, 1999. *Inbound Tourism: An Integrated Approach to Future Regulation.* Brisbane Tourism Queensland.

Tse, W., 2003. An analysis of industry response to the influx of visitors from China to Hong Kong, *First APAC-CHRIE Conference*, 21-23 May 2003, Seoul.

Whipple, T. and Mach, T. S., 1988. Group tour management: does good service produce satisfied customers? *Journal of Travel Research* (Fall), 16-21.

Yu, X. and Weiler, B., 2001. Mainland Chinese pleasure travellers to Australia: A leisure behaviour analysis. *Tourism, Culture & Communication*. 3, 81-91.

The views put forward in this paper are based on a technical report undertaken by the authors and commissioned jointly by the Australian Council of Tourism Ministers and Sustainable Tourism Co-operative Research Centre (SRCRC 2004). The authors wish to thank the Australian Council of Tourism Ministers for permission to publish some of this material.