

Rethinking Product and Distribution: The Opportunities to Link Product Strategy and Distribution Strategy in the Travel Industry

**Eric K. Clemons — The Wharton School
D. J. Young — The InterContinental Hotels Group**

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1. Introduction

For a variety of reasons, many primary service providers (airlines and hotel chain operators, rather than the various intermediaries that handle bookings) need to rethink their distribution strategy:

- The power of traditional electronic intermediaries (the Global Distribution Systems, or GDSs, that link travel agencies to the individual reservations systems of hotels and airlines) can be abused; they represent a multi-billion dollar expense to airlines and still have the potential to extract significant additional fees from hotel chains.
- New non-traditional electronic third party intermediaries (TPIs) like hotels.com and Expedia have obtained enormous power in hotel distribution and have learned to abuse it, charging commissions two or even three times greater than industry norms and misrepresenting hotel category and room availability in order to discipline uncooperative hotel operators. They have captured double digit shares of individual bookings and are making significant inroads into corporate travel as well, raising the possibility of deep discounting on an ever-increasing number of hotel room-nights.
- Airlines and hotel operators need to learn to use the distribution channel defensively, to regain some control over their distribution and their pricing
- As importantly, operators need to learn to use the distribution channel offensively, for competitive advantage, by informing customers of the full range of available offerings and by helping customers to book precisely the mix of services that they value most highly.

This need to rethink distribution strategy is occurring at the same time that airline and hotel operators have an opportunity to reposition their product offerings and redesign both their product portfolio and their product positioning strategies.

- TPIs sell bookings on the basis of lowest possible price, and strive to ensure product *adequacy*; customers do not and indeed should not expect perfect fit with their preferences for the lowest available price in any market. Analysis of data shows that customers booking on price-based TPIs are concerned with achieving a satisfactory experience at the best price, not with achieving and paying for delight. While TPIs may provide sufficient generic information, like detailed reviews from other consumers, to allow a potential traveler to assess quality in a

generic sense, there is no capability for the guest to specify precisely what he wants, no automated capability for the TPI to communicate preferences to the hotel, and no capability to ensure that the traveler's preferences will or even can be honored.

- In contrast, airlines and hotel operators want to position their products as value-based, rather than solely price-based, and as products that for any given price provide the customer with the best available match with his preferences that can be obtained at that price. In some instances this will require providing delight, and require meeting travelers' specific desires as well as needs. When serving the most attractive segments of the travel market, ideal positioning of services will provide resonance and delight for a fair price, rather than solely providing the bare minimum *satisficing* product at the lowest possible price.

Fortunately, a travel provider's strategy for its portfolio of service offerings and its strategy for the service distribution of its services can be tightly linked to provide competitive advantage. Redesigning and repositioning the portfolio of service offerings can drive an increase in consumer demand. This in turn can shift the basis of power in the distribution channel, as consumer demand can weaken the power of players in the existing distribution system and drive customers to newer, more neutral distribution alternatives.

- Resonance marketing allows airlines and hotel operators to become truly different, in ways that resonate with customers. This enables them to provide extraordinary value to travelers, and to retain extraordinary profits.
- Resonance marketing can resolve channel conflict in favor of airlines and hotel operators. Rethinking the nature of service offerings can provide consumer demand, so that intermediaries lose the power to *discipline and punish* uncooperative service travel providers. As importantly, new sets of attributes and new service capabilities can overwhelm the limited information display capabilities of traditional travel intermediaries, and thus can be used to move distribution away from GDSs and TPIs, towards the primary service providers' own websites

We have all noticed that many customers are trading up while even more are trading down. Customers who trade up stay in first class hotels that offer ever-increasing amenities, like the use of \$400,000 Maybach 6.2 automobiles at the Four Seasons in Manhattan as shuttles around town. Customers who trade down fly Jet Blue. More significant than trading up and trading down, which have been present for decades and are well understood, is the emerging trend towards trading out, customers who substitute an exotic get away at an EcoTourism location like Una Ecopark in Brazil, or a physical assessment and health location like Canyon Ranch. More customers trade out than trade up, and the margins from serving them are far better than serving customers who have traded down.

2. Unrewarded Excellence

Being good enough simply is no longer good enough.

Companies make better products, in more varieties, at lower cost, with higher quality by any measures, and yet their growth and profits have stalled. Customers are abandoning their traditional products, and instead purchasing power bars, non-carbonated beverages, super-premium ice cream, craft beers, and bagged coffee. Or customers are abandoning traditional service providers for low price alternatives like Jet Blue, which reminds passengers to “please remove your trash when exiting the plane.”

The prices that companies can now earn from their existing portfolio of products and services is limited by three factors.

- The *compromise discount*: The compromise discount exists because consumers pay less for products that are not perfect for them.
- The *uncertainty discount*: The uncertainty discount exists because when customers purchase unfamiliar products and services, they do not yet know exactly what they are getting; when they do not know exactly what they are getting there is a chance that what they actually experience is a less perfect match with their preferences than what they expected. This uncertainty means that there is a significant chance that that what they actually receive will suffer from a real compromise discount. Dealing with uncertainty has been difficult and expensive, and things like initial promotional prices, free samples, and advertising can be the largest costs associated with a new product launch.
- The *competition discount*: The monopolist provider of a commodity product or service can charge his profit maximizing price, that is, can charge the price that results in the greatest total profits. A service provider with competitors whose offerings are similar experiences true price competition. A monopolist can charge whatever he wants, subject to customers’ valuation of and willingness to pay for, his offerings. With price competition, prices are driven down to much lower levels; with perishable products, like airplane seats and hotel room nights, prices can get driven down to the marginal cost of flying an additional passenger or of cleaning a hotel room.

These are the same three factors that have always dominated marketing strategy, but their impacts has changed rapidly and dramatically, and in many cases the changes have been unnoticed.

- Changes to the *uncertainty discount*: The uncertainty discount has never been lower. Online reviews, from the manufacturer or service provider, from third party professional rating services, and from websites that report consumer experience, reduce uncertainty and facilitate informed selection.
- Changes to the *compromise discount*: The compromise discount is growing. As more information becomes available, and as more products and services are

launched in response, consumers have come to expect that they will be able to find precisely what they are looking for. This awareness leads to a sense of entitlement, and consumers who do not get what they want now expect to pay discount prices as if they were purchasing generic offerings.

- Changes to the *competition discount*: The monopolist provider of a commodity product or service can charge his profit maximizing price, that is, can charge the price that results in the greatest total profits. A service provider with competitors whose offerings are similar experiences true price competition. A monopolist can charge whatever he wants, subject to customers' valuation of and willingness to pay for, his offerings. With price competition, prices are driven down to much lower levels; with perishable products, like airplane seats and hotel room nights, prices can get driven down to the marginal cost of flying an additional passenger or of cleaning a hotel room.

These changes both create the current problems faced by primary travel providers and suggest the approach they can take to resolving these problems and restoring both growth and profitability.

New marketing strategies must deal with increasingly complex, bifurcated customer behavior. Customers take the cheapest possible flights, then stay at the Four Seasons on Hawaii — they trade up on hotels, but trade down on airlines. Other customers book the cheapest adequate hotel, but play golf at their favorite courses and book their favorite restaurants, trading down on hotels, but trading out on golf courses and restaurants. In brief, customers find the lowest prices for things that don't matter to them, but find the best fit with their preferences among the available offerings for things they care most passionately about.

3. A Short Review of Resonance and the New Brand Positioning Strategies

The art of hyperdifferentiation enables modern firms to produce and sell almost any combination of goods and services, without destroying economies of scale and therefore without destroying their costs of production, distribution, sales, and marketing [1]. Of course, not everything is of interest to all consumers, and not everything is of interest even to any consumers; not everything that can be made and sold should be made or can be sold.

Resonance marketing guides hyperdifferentiation, allowing firms to focus on goods and services that meet consumers' unmet desires, longings, and cravings, and to focus on serving unserved or underserved market segments. Resonance marketing gives consumers exactly what they want and eliminates the compromise discount; by appealing to consumers' passions rather than their pocketbooks, resonance marketing makes each product appear unique, creates little mini-monopolies, and eliminates the competition discount as well.

Resonance marketing is not simply about being different, and it does not seek to make products better in any absolute sense. Resonance marketing is not about having a product that is better for *all* customers but about having some product better for *each* customer. This requires hundreds or even thousands of products within a single category; where once there was one powerbar (PowerBar) there are now hundreds of power bars, each highly specialized. There are powerbars for men or for women. There are powerbars that specialize in slow release energy to soothe golfers' nerves, high protein energy bars for weight lifters, even powerbars that are easy for triathletes to wrap around bicycle handlebars. There is no single best power bar, just as there is no single best hotel or airline or bank or broker.

Why is this happening now? Consumer preferences have not changed, and consumer behavior rarely changes this quickly without some change in their environment. In this case the change is a dramatic increase in informedness.

- Informed customers are unwilling to pay high prices for commodity offerings; they do not need to, since competition in an informed and transparent marketplace increases the competitive discount and destroys profit margins. Harry Potter novels at Amazon and Barnes and Noble sell at minimal profit margins. Similar discounting has affected brokerage fees, travel agent commissions, and the price of coach airfare. Likewise, if the product is not precisely what they want, informed customers treat it as if it were a commodity; the compromise discount has increased as well.
- In contrast, informed customers are willing to pay for what they want, and for products and services that truly match their preferences. The uncertainty discount has been largely eliminated. The Pro V1 is both the best-selling and the most expensive ball in golf. Pebble Beach golf course is both the most expensive course in America and is so thoroughly booked that it is almost impossible to reserve a round for a foursome.
- Informed producers and the role of proper design and proper customer targeting. Informed producers and complexity management. Capital One Financial, test-and-learn, and 10,000 products

4. Rethinking Distribution

4.1. Travel Agent Reservations Systems

Historically, the geometry of a distribution channel appeared to determine the destiny of channel participants; the channel member closest to the point of contact with the customer exerted enormous power over customers' selections, and came to exert more power than the brand of the primary producer. Wal-Mart has more influence over consumers' purchases than most consumer packaged goods manufacturers, and Home Depot has more control over what hardware consumers buy and the prices they pay than hardware manufacturers. Likewise, both the Global Distribution Systems that link agencies to airlines and hotels own reservation systems and the electronic third party intermediaries that allow customers to book online can and do exert enormous power over airlines and hotel operators.

The old world of global distribution systems and travel agents had geometry as shown in figure 1. Each airline sold through all the reservations systems, and all of the reservations systems sold to numerous travel agencies. Each travel agency, however, dealt with only a single reservations system, thus each airline had only a single channel into each agency. In a real sense, each reservations system represented a small parallel monopoly rather than an oligopoly player; an airline that was dropped by any of the reservations systems was cut off from a significant number of agencies and suffered an immediate drop in bookings, in load factor, and in revenues. Reservations systems charged airlines fees that were in no way commensurate with their costs to provide those services, and in some years in the early 1980s operating a reservations system was more profitable than operating an airline.

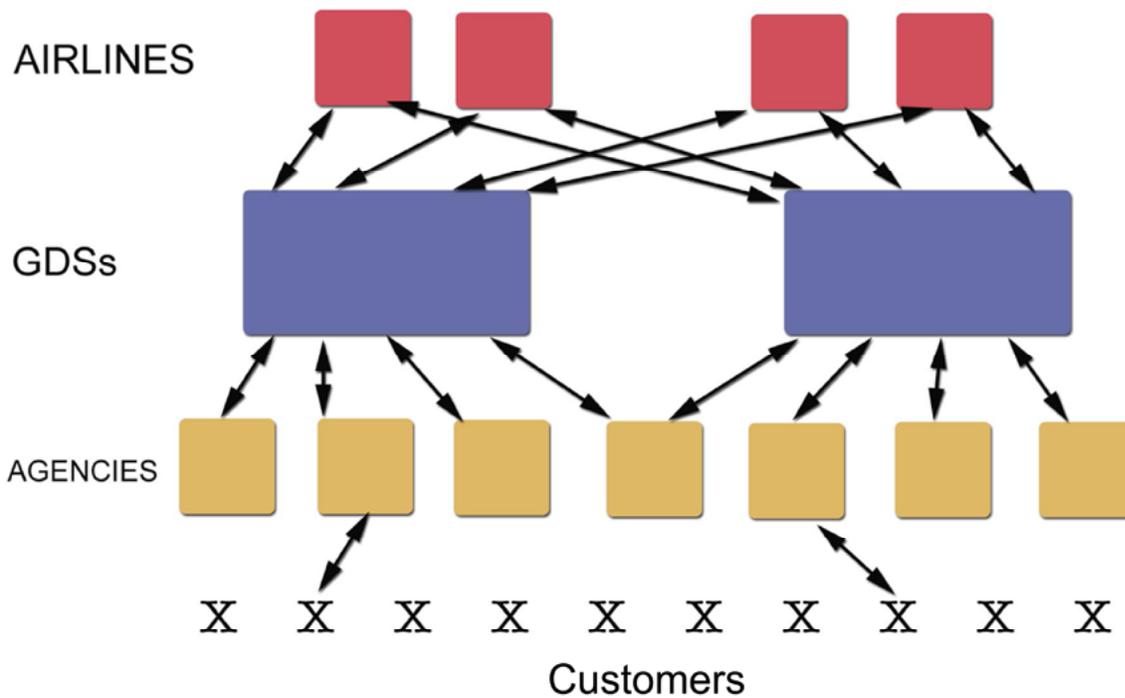


Figure 1.—Geometry is destiny, and the power of the reservations systems was determined by the fact that they were closer to customers than the airlines were.

4.2. ATM Networks

In contrast with the enormous power enjoyed by and used by CRSs, local ATM networks like NYCE in New York and MAC in Philadelphia exerted almost power of their member banks. Each bank controls its own ATMs, which account for vast majority of the transactions performed by its own customers. Denial of service by the ATM system network vendor would not really have been full denial of service, since each bank would have been able to operate its own ATMs and provide at least basic *us-on-us* service to customers using the bank's cards at the bank's machines. This is shown in figure 2.

Moreover, each bank adhered to the same communications standards. Denial of service by the ATM vendor, and thus denial of interconnection *us-on-others* service when the bank's own customers took their cards to other bank's ATMs, would have been at worst a short term problem, since denial of interconnection service could easily have patched around. Indeed, networks like Cirrus and Plus were already available. Consequently, ATM networks did not have the parallel monopoly power of reservations systems; Indeed, even when the last two ATM networks in Philadelphia merged, the remaining ATM network did not have monopoly power. At least to some extent, geometry really is destiny.

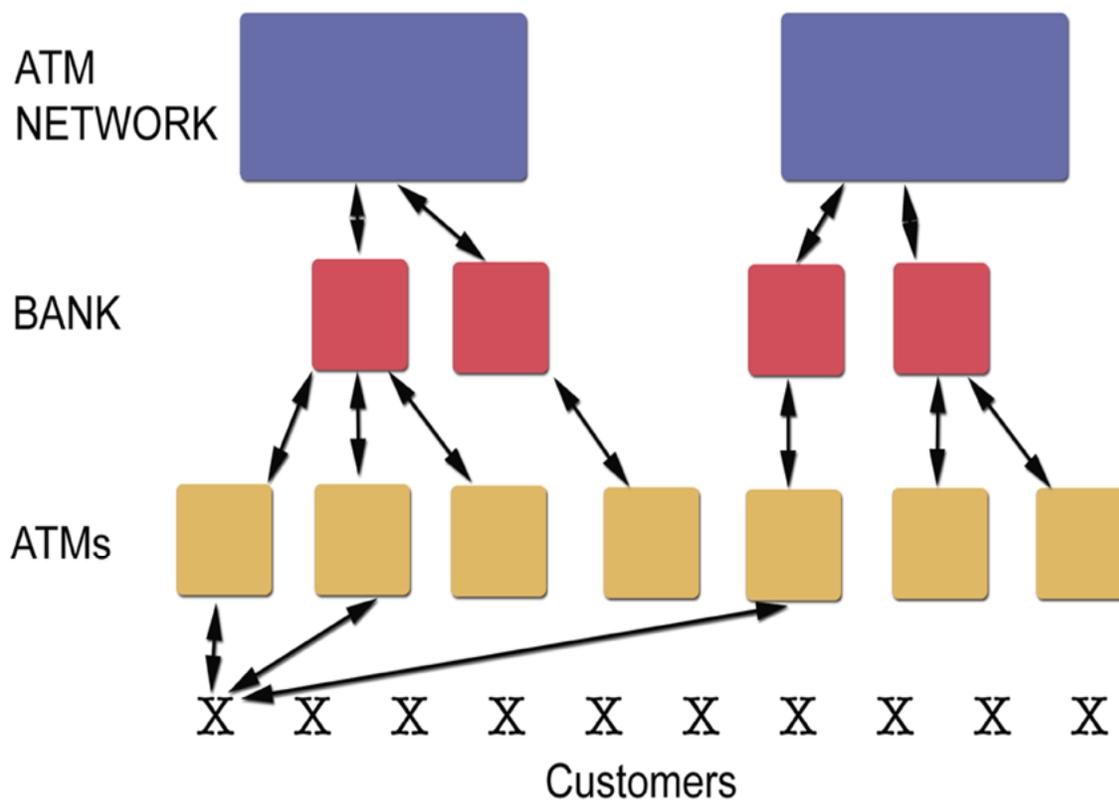


Figure 2.—And again, geometry is destiny. Even monopoly ATM service providers had only limited power over their participating banks, since the banks were closer to their customers and to their ATMs and consequently truly controlled the banking relationships.

4.3. Point-by-Point Comparison of CRS and ATM Networks

A point-by-point comparison clearly shows the differences between the power of CRS service providers and ATM network operators.

CRSs

Point of presence far removed from airline
Difficult for airline to develop substitute service
Bypass threat not credible
Asymmetric losses; the airline lost full ticket price, the CRS generally sold a different ticket
Lack of transparency; the customer did not know that the flight was still available

ATMs

Point of presence close to bank
Easy empowerment and substitute service
Easy bypass
Losses favor the bank and not the network, since the customer will stay, and will transact eventually
Transparency favors the bank, since the customer knows that the bank is still there and it is the network that has failed

5. Repositioning Products

Hotels historically have been classified simply by their vertical market segmentation, also known as their price points. Thus hotels were seen as up market (Four Seasons, Ritz Carlton), upper mid-market (Crowne Plaza), mid market (Holiday Inn), or down market (Motel Six). Airlines offer first class, business class, coach, or no frills service. With few exceptions, all focused on the fat spots in each crude price-based segment; that is, they tried to attract as many customers as possible within each segment by offering a single, high-quality product or service that would appeal to all customers within the segment.

And yet there is so much more that can be done. Hotels can differentiate themselves in a variety of ways, first by offering services that qualify them as destination resorts, or by offering services that qualify them as virtual office business destinations. Each of these two cruder segments can then be divided into finer and finer mini-segments, appealing to the desires, longings, and cravings of specific groups of travelers. Taking a page from McDonalds old playbook, hotels should be able to allow guests to “have it your way,” from sliding window variable check-in times to spa-category rooms, from full business services when you are at the hotel to access to a full service concierge for leisure arrangements even when you are not.

Commitment to this finer degree of segmentation creates opportunities for more comprehensive anthropological observation to drive more differentiated product design. In an era of informedness and the customer resonance this enables, the right product will create demand. And — fortunately for airlines and hotel operators! — GDSs and TPAs can't handle more complex product design yet. If customers are truly aware of the features offered by specific flights or specific properties, truly desire them, and are truly committed to booking them, they will move towards distribution channels that permit them to book what they want. This will drive customers to the airlines' and operators' own websites, or to travel agents who use them, undercutting GDSs and TPAs.

5.1. Implementing a New Product Positioning Strategy

A belief in hyperdifferentiation tells us that with today's complexity management technologies, we can produce and sell almost any combination of goods and services. The ability of a world class hotel like the Ritz Carlton in Naples Florida or the InterContinental in Hong Kong shows how experiences can be matched precisely to the needs and preferences of each guest; with proper training and proper systems support, comparable levels of customer service can be offered more broadly. Thus, for example, the InterContinental in Hong Kong provides a range of services. There is a broad range of restaurants, from functional American-style snack shops to world class Chinese and Continental cuisine. There are additional services available on an a la carte basis for guests who desire them; for example, there is a spectacular business lounge, with internet, wireless internet, and concierge services for everything from travel bookings to foreign exchange wire transfers. The lounge offers a range of food throughout the day, cappuccino and espresso, and wines and other beverages. It has space for small business meetings, and comfortable places for families to dine together while getting coached on their daily activities by the lounge staff. While not all guests will value, or will pay for, lounge access, those who want it find that it makes the hotel stay for more productive or far more enjoyable.

Resonance marketing tells us that when the customer knows what is available and finds what he truly wants, he willingly pays for it. Not every form of differentiation is cost effective for every guest, simply because not every guest will value it or pay for it. Resonance marketing guides differentiation, and focuses it, customer by customer and service by service, on creating value and using this value to create revenue opportunities. Again, a customer who knows what is available will know what he wants, and a customer who knows what he wants will want to book it, ensure that it is available, and ensure that he gets it. Some guests will want a room while others want a small suite, some will want a suite with a view of Hong Kong Island and Victoria Harbor, and some will want to book the lounge and pre-book various combinations of business car services, restaurants, and activities.

In the hotel industry in particular, we now have the ability to eliminate the compromise discount, increasing guests' willingness to pay for services received. The improvements and increases in information available to each prospective guest reduces the guest's uncertainty about what he will receive and likewise reduces the uncertainty discount to the point where services can be introduced and profitably priced and sold. As importantly, by positioning itself to appeal to and to serve specific guests with specific needs, hotels cease being interchangeable beds away from home and become centers of productive and meaningful activity; when hotels are no longer seen as interchangeable alternative properties are no longer seen as competitors and substitutes, reducing or eliminating the competition discount. That is, successfully implementing resonance marketing creates virtual mini-monopolies, largely take price out of the decision. Resonance marketing appeals to customers' passions, not to their pocketbooks.

5.2. Harnessing Resonance Marketing

Resonance marketing rewards extremes when customers are selecting unfamiliar delight-based products. For example, no one really needs premium beer, and consumers buying premium beer want to be delighted rather than merely satisfied. Consumers who are paying premium prices they want beers that they love, rather than simply like. That is, consumers who hate your beer and consumers who like it are identical in terms of contributions to sales; neither will buy your beer. All sales are to consumers who love the product; hence it is the strength of the top reviews, rather than the average of all reviews, that determine sales. Victory Brewing's Hop Devil is so extreme that it is the most despised of Victory's beers, and many consumers refuse to take a second sip after trying it. However, consumers who love Hop Devil cannot find anything like it, and it accounts for more than 50% of Victory's total sales. Average reviews and the median consumer's response are not good predictors of sales in a resonance marketing environment for a delight-based product; only the most favorable reviews are significant predictors.

Customer informedness also punishes extremes, in this case for consumers seeking risk-free low cost alternatives when trading down rather than customers for delight-based products who are trading out. Our experience with analyzing data from hotels shows that the mean of online guest satisfaction evaluations and the mean of the hotel's own guest satisfaction surveys have no power to predict the ability of the property to book itself to customers shopping online. In contrast, the strength of the negative online evaluations is a very powerful predictor; more precisely, the length, word count, and specificity of complaints detailed in a properties' negative online customer reviews is the best predictor of a property's inability to sell online.

Resonance marketing is based on extreme preferences and perfect informedness. Consumers' have always had preferences, and, indeed, preferences often change quite slowly. It is informedness, and in particular the impact of informedness on consumers' ability to satisfy their preferences, that is new. Indeed, it is so new that companies are still learning how it affects strategy. The travel industry will be at the forefront of this learning because the prices of goods and services is high, the range of preferences is extreme, and most products can be described online with a high degree of precision, accuracy, and specificity.

5.3. The Theory behind Resonance Marketing Pricing In The Travel Industry

The motivation behind resonance marketing is simple; products that are not differentiated are seen as substitutes for each other, and thus as seen as direct competitors. The presence of direct competitors reduces the prices that each can charge, and if the market suffers from excess capacity each may end up reducing prices to its marginal cost, destroying all profits.

The nature of a price war is clear. With two gas stations on the same corner, or two convenience stores side by side, one may be tempted to reduce its prices by just a little;

while this does not drastically reduce profits from each customer, it can move a large number of customers in from the competitor, significantly increasing profits. The competitor will respond by reducing prices, generally by a little more, to recover lost profits by regaining its customers and attracting those of its competitors; the result of this sort of price war is a collapse of prices and of profits. This is precisely the situation that many hotels experienced after September 11, and it has been exacerbated by the pure price-based competition encouraged by TPIs like hotels.com, PriceLine, Expedia, and others.

Resonance marketing requires customers who are truly informed about the products and services available to them. When products are sufficiently different but consumers' uncertainty about them remains high firms cannot capture the full value of their differentiation. The uncertainty discount may destroy the ability to charge any premium price for services offered. This has historically limited the launch of new product and service offerings. Huge consumer package goods firms address the uncertainty discount by providing samples, offering discounts, and undertaking huge and costly advertising and informational programs with the launch of each new offering. Individual hotels cannot engage in similar activities to promote the attributes of their individual property, and even large chains cannot engage in similar activities to promote the attributes of each individual property. The most successful new launches of hotels and airlines tended to be simple, uniform products like Holiday Inn Express and JetBlue.

Resonance marketing works in the travel industry because we can now use information about our guests to determine precisely what to offer each, and because we can now communicate precisely what is available to each. With the right set of product designs, and the right communication, we can be just about perfect for each of our customers. We no longer suffer from the competition discount or the uncertainty discount, and our guests no longer suffer from the compromise discount.

6. Linking Product and Distribution

6.1. Overwhelming Traditional Intermediaries' Capabilities

Because their capabilities, their interfaces, and their databases were designed for the simpler product offerings and simpler product inventories of the 1980s, GDSs and TPIs cannot handle special requests. When Air Canada introduced highly complex menus of services, such as a discount flight that did not allow you to choose your seat assignment, combined with a small additional tariff that did allow you to pre-select your seat, they were unable to implement this through the existing GDSs. Other similar menu selection options, like time of hotel check in, choice of room view, pre-booking of exercise equipment for the room, or the selection of a Kosher, vegetarian, or Hallal meal for a flight, are likewise beyond the capability of GDSs or electronic TPIs. Conditional bookings, like the desire to checkout on Friday, unless tickets for a specific play are available, or on Saturday if the concierge can get the tickets for Friday, are beyond all systems capabilities today.

If services such as these are offered to travelers, and if there is sufficient demand for special products and services will drive consumers either to the websites of the service providers themselves or to travel agents who can use these websites. If consumers truly desire these offerings, they will book them or have them booked, which will drive order flow through the booking services that have the necessary functionality. This will weaken the power of GDSs and TPAs over travel distribution, and will restore the ability of service providers to exercise some control over their pricing strategies and over the products and services that they make available to each guest.

This would be an example of demand trumping geometry. It would not be the first example. Customer demand in financial services has already shown that geometry is not always destiny in a network.

6.2. Consumer Demand Can Trump Geometry and Shift Power

The securities industry provides us with an example where customer demand was so great that it overturned the power relationship predicted by geometry. That is, being closer to the customer gave the network intermediary no ability to influence customer behavior, and therefore provided the network intermediary no ability to extort payments from the primary service providers by threatening to give them less than full service or threatening to deny service entirely. Customers would have known about any such manipulation and for financial reasons would not have accepted other than full, complete, and unbiased access to all service providers.

Historically, customers traded securities either on traditional exchanges like the New York and London Stock Exchanges, or on electronic alternatives like Nasdaq. A new category of market emerged in the 1980s and became more widely available in the 1990s; electronic communications networks provided alternative venues like Instinet, which allowed investors to trade directly with each other, without using or paying for the intermediaries associated traditional trading venues. Although a few of the ECNs captured enough liquidity and order volume to be significant, mostly they accounted for an insignificant share of the trading volume. Lack of existing customer orders precluded additional customers from trading there; that is, customers don't try to trade where customers don't already trade. The owners of the ECNs might attempt to attract order flow by offering small lots at attractive prices, but mostly traders who wanted to buy or sell large positions received inferior prices on ECNs since the lack of existing volume meant that a large order to buy would significantly bid up the price, just as a large order to sell would drive down the price.

Lava Trading was the first firm that got into the "order routing" business, linking trading firms to all ECN markets. Customers could place a large order, instructing Lava to sweep all the ECNs for all shares at a given price, and could fill larger orders without affecting the price. The seriously increased competition among ECNs, improved their prices, and attracted more order flow. As order flow increased, the ECNs became more liquid and more attractive, attracting still more order flow. ECNs now account for more than half of the shares traded in Nasdaq securities.

The geometry of Lava's network looks remarkably like the geometry of the GDS business (compare figure 3 to figure 1 above).

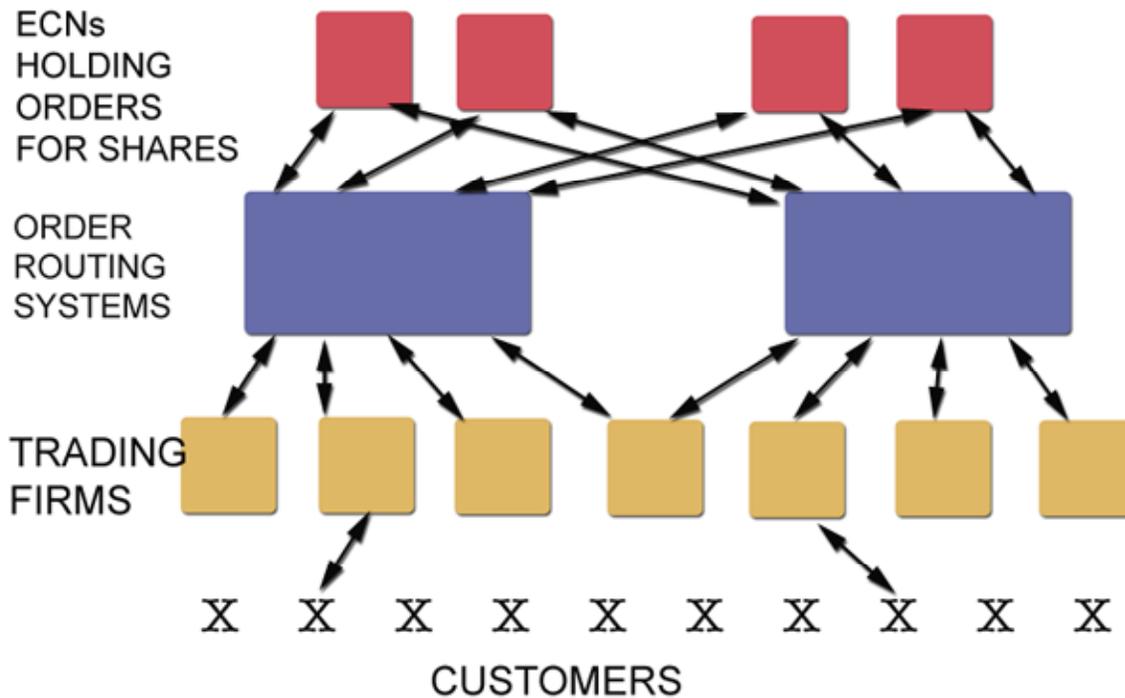


Figure 3.—Geometry is not always destiny, and the power of the order routing systems vendors was determined by customer demand for complete information, not by the fact that systems vendors were closer to customers than the ECNs were.

Although the geometry of Lava's order routing system connecting trading firms to ECNs and the geometry of GDS reservations systems connecting travel agencies to airlines look very similar, the evolution of the two industries and the profitability of the service providers have been quite different. Every firm on Wall Street wanted order routing systems and order routing systems became a must have product; very similar things could be said about the adoption and utilization of reservations systems in travel agencies. Lava's sales growth was quite literally exponential, and revenues grew rapidly. Of course, rapid growth of the market and rapid increase in sales and revenues attracted competitors, and Lava's prices and margins deteriorated; trading firms paid lower prices over time, as of course travel agencies had in the reservations business.

The most significant differences occurred in the overall profitability of the two industries; Lava's profits actually declined, while GDSs have been able to preserve profits by maintaining the prices that they charge participating airlines; as we described in section 4.1 above, GDSs operate as parallel monopolies, many agencies choose on or another of the systems, and airlines feel that they must be present in all systems in order to ensure access by agencies and their customers. This need to be present in all systems

has freed the GDSs from direct price competition and allowed them not only to charge but also to discipline uncooperative airlines.

In contrast, Lava has no ability to discipline ECNs or to charge them. As with most travel agencies, securities trading firms took only one system, for example Lava's system or the system of a competitor such as royalblue, and thus the ECN order routing industry appears to be a set of parallel monopolies rather than an oligopoly. Unlike the GDS business, however, no order routing system can risk suspending trading to any ECN, since trading firms and their customers demand full access to all orders available on all ECNs. Lava's value proposition was based on getting customer the best price available on any of the markets including all ECNS, and providing access to all orders posted on all markets and ECNS. Transparency in the securities industry ensures that customers would actually know if they were denied access to orders residing on one or more of the ECNs, systematically across the trading day or even for a single sweep of orders across ECNs at a single point in time. The stakes were high enough that customers cared enough to make certain that Lava actually provided full access and best execution; denying customers access to the orders of any ECN, to discipline the ECN and force it to pay higher fees, would quickly have destroyed Lava.

Contrast this transparency and the power it gives to customers and takes from Lava with the situation in hotel reservations. If an individual property does not provide hotels.com with the lowest priced rooms, hotels.com will report the property as sold out; it does not provide the more accurate indication that no rooms are available through hotels.com, or that rooms are available at higher prices. This and other forms of strategic misrepresentation have allowed hotels.com to demand significant and costly concessions from hotel operators, both chains and individual properties.

6.3. Bringing Product Strategy and Distribution Strategy Together Overwhelming TPIs and GDSs while Motivating Bypass and Book-Arounds

With sufficient differentiation, customers will not be able to use electronic intermediaries; either they will book directly through hotel websites and call centers, or by calling the hotels, or they will use intermediaries like traditional travel agencies that will do so for them. As importantly, with sufficient differentiation, customers will choose to bypass and book around traditional intermediaries, that is, they will demand access to differentiated offerings and services, and will book them through whatever mechanisms are available. Strong customer demand will create a situation in which intermediaries lose their ability to manipulate customer bookings, and thus lose their ability to extort primary providers of travel services. Consumer demand will trump geometry.

6.4. Enlisting Travel Agencies as Allies

Travel agencies clearly need help now, in order to strengthen their value proposition and in order to increase the range of services that they can actually provide to customers. Recently conducted studies by Forrester confirm that most customers use a

travel agency to book the hotel or the flight that they have already selected; these customers are clearly positioned for a transition to the use of hotels.com or Orbitz to book for themselves, without using an agency. Likewise, this same Forrester study confirms that TPIs are rapidly gaining market share even in corporate travel, in terms of actual volumes two of the top three revenue producing corporate agencies are now electronic third party booking systems. Finally, and most damaging over the long term, even a significant fraction of agencies report using TPIs when doing research for customers on flights and on properties.

If the agency can't do anything customer or TPI can't already do, agencies will continue to lose market share and revenues. Adding new services, booked away from GDSs and TPIs, provides services that the customer cannot immediately perform for himself online. This benefits the agency as well as consumer and can enable service providers adopting a differentiation strategy to gain important agency support

7. In Conclusion

May hotel management companies are already exploiting a unique opportunity to redefine their products and redefine what each brand and even what each hotel stands for. This works because, and only because, it is now possible to redefine the product attributes of each group of properties, and indeed to change what each property has on offer, to upgrade what each can provide each customer, and to communicate these changes to each customer. Initially these changes were undertaken to provide competitive advantage relative to other hotel management companies.

At the same time hotel management groups have begun redesigning their distribution strategies and their web services. Companies are seeking to shift bookings away from calling each individual hotel, and even working even more determinedly to move customers away from using TPIs; companies want consumers, corporate travelers, and their travel agents, to move towards increased use of central reservations or the groups' own websites. The changes were undertaken to cut the costs of sales and distribution, and to demonstrate greater order flow and greater value added to the owners of individual franchised properties.

Fortunately, these two changes are tightly and naturally linked. The redefined product requires more powerful reservation tools than the GDSs and the TPIs currently provide. If the redefined product creates consumer demand for new services, this demand will drive traffic to the new reservations tools that can enable travelers to specify precisely what they want, and that can enable primary service providers to confirm for these travelers precisely what they are going to get.