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WHITE PAPER

AN ANALYSIS OF ONLINE DISTRIBUTION MODELS FOR SELLING HOTEL'S EXCESS INVENTORIES

TRAVELSURF

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I. INTRODUCTION

It's an established fact that online distribution in general has been very beneficial for the travel industry. It has brought new markets for hotels at nominal costs and has made the consumer more informed, provided more options to search, shop, purchase, and usually find better 'deals'.

While the Internet has changed the way hotels conduct their business, the basics of the business have not changed.

A hotel room is still a perishable product, the incremental cost of renting a room is still low, most of the time hotels are left with unsold inventories that need a market – A market where hotels can sell these surplus rooms at discounted prices (to generate additional demand) without disrupting pricing and rate parity structures on other channels.

That's what hotels did before the Internet days and that's what hotels need to do now.

However, when it comes to selling surplus hotel inventories online the current business models have fallen short, in that they do not provide an efficient means for hotels to sell off their vacant rooms and for consumers to purchase best suitable deals.

Hotels face 3 major challenges in this regard:

1. How to sell unsold rooms online without adversely affecting sales of their regular inventories
2. Generate highest possible yields from the sale, and
3. Maintain rate parity across other channels.

II. CURRENT DISTRIBUTION MODELS

Existing online distribution models that are currently being used for selling excess hotel inventories can broadly be grouped into three categories, the OTA Model, the Reverse Auction Model, and The Packaging Model.

A. **The OTA Model** enables consumers to search multiple hotels, do price comparisons among products, and once satisfied book the hotel room of their choice.

   In all cases the consumer is quoted a purchase price and can only reserve the room at the price quoted. Specific examples include Expedia, Hotels.com, Lastminute.com, Orbitz.com, Travelocity, MakeMyTrip, Yatra, among others.

B. **The Reverse Auction Model** enables a consumer to make an offer for a certain category / classification of hotel (such as a four star hotel in Downtown Chicago). The consumer puts out a binding, blind offer for a hotel room without knowing who the actual supplier is, or understanding the details of the hotel product being purchased (Example, not knowing which hotel will be assigned among the classification, what type of room will be offered, etc). The hotel room detail, along with the name of the hotel, is communicated to the consumer only after the offer is accepted for one of the hotels and the transaction is processed and the credit card charged. Examples of this model are Priceline.com and Hotwire.com.

C. **The Packaging Model** enables hotel to make the room rate opaque by combining other services with the room and quoting the package total price, thereby hiding the discount.

III. SHORTCOMINGS OF CURRENT DISTRIBUTION MODELS BEING USED FOR SELLING EXCESS INVENTORY

All of the above models listed have some serious shortcomings when it comes to selling surplus hotel inventories.

The online models have failed the industry because the solutions are either biased in favor of the consumer while ignoring the interests of the hotel, or are weighted in favor of hotel with little consideration for the consumer.

The challenge for an online distribution model, especially for selling surplus rooms, is to find that fine balance between two contradictory interests – The consumer's interests vs. the hotel's interests.

The solution has to ensure that both parties benefit. And, the benefit cannot only be in terms of convenience, ease of use, and customer experience. The key benefit for both parties has to go beyond these basic expectations. There has to be a financial advantage for conducting business online – the consumer has to get the best possible "deal" and the hotel has to sell its rooms at optimum "yield". The benefit simply cannot be at the expense of one over the other.

It is a fact that in order to sell the unsold/excess inventories the price for the product needs to be reduced substantially to create additional demand. The problem lies in how this discount is controlled and how this reduction in price is exposed or communicated to the consumer. Let's take a look at each one of the models.

A. THE OTA MODEL:

The biggest flaw of the OTA model from the hotel's perspective for selling surplus inventories is that discounts offered get exposed to the general public. This obviously is extremely detrimental for the hotel. The moment discounts are published online it becomes common knowledge, and makes the likelihood of selling "regular" inventories at higher prices extremely unlikely. It therefore discourages hotels from offering the real discounts on this model to generate additional demand.

Even if discounts were posted, a product that is offered at a low published price to the general public for a prolonged period produces the undesirable effect of creating a lower perceived value for the product in the mind of the consumer.

In earlier days of the OTA model, hotels had lost control over product pricing as the selling price to consumer was dictated by the portal.

The compromised solution of "Rate Parity" across channels, an attempt on part of the hotels to take back control over pricing, and on part of the OTAs to remain a viable model, has opened a new can of worms for hotels. With the introduction of "Rate Parity" the opportunity to sell unsold rooms has further been reduced, as hotels can no longer offer a higher discount on a portal and implement "Rate Parity" at the same time.

Given the limitations of the OTA model it is not a viable option for hotels to sell their unsold rooms.

B. THE REVERSE AUCTION MODEL

The Reverse auction model of priceline.com and hotwire.com attempt to address some of the pitfalls of the OTA model by not exposing the discounted price to the general public. However by doing so, they compromise the flexibility and the value derived by the consumer from the OTA model.

The Reverse Auction model is flawed for the following reasons:

The focus of the model remains on price alone. Price is used as the primary differentiating criteria among hotels. The model treats all hotels within a classification as generic commodities that have no unique differentiating features. Therefore it falsely assumes that the best "deal" for the consumer is the one with the lowest price.

It should be understood that hotel products are not commodities and do not compete on price alone. They compete on many fronts including quality of service, brands, service standards, easy access, convenience, and the overall experience delivered to consumer. While short term discounting of price is used as an incentive to lure the consumer this alone is not the differentiating factor among "similar" (as defined by the model) hotel products.

The other pitfall of the Reverse Auction model is that it erroneously assumes a fair product classification can be accomplished by segregating products by the classification done by governmental and other authorities (such as star rating in the hotel industry) and by the amenities offered.

This is a misguided assumption since an existence of a certain amenity or the product falling under a certain classification does not make two hotel products similar.

Product classifications fall even weaker and vague in other parts of the world outside of the North American continent. In Asian countries a four star rated hotel could have the same standard of service as some other 3 or even 2 ½ star property.

In India only a very small percentage of hotels (less than 15%) even carry star ratings, yet many of the non-star rated hotels are quite comparable to star rated hotels.

For example: A consumer selecting Internet service as an amenity with a certain star classification of hotel may not deliver the desired result to the consumer. Internet service could mean the service is available only in the hotel's business center for an additional fee, or in the hotel lobby and not in the hotel guest room or it could mean the service is available throughout the hotel. Yet all of these hotels could get qualified for the offer.

For example: A consumer may elect to stay at a particular hotel because of the proximity to a particular address. In this case staying at a hotel within a block from this address would be more preferable than at a particular star category hotel. Staying further away may require hiring a taxi every day, getting up early, facing rush hour traffic, etc. etc. So the subjective "value" for a hotel at a distance, even if it's a better class of hotel may be lower in this particular instance for the consumer.

That does not mean the consumer is not willing to stay at the other hotel but rather he may not be willing to offer the same price he'd be willing to pay for the one closer.

These inconveniences to the consumer could be termed as the '**P**ain **C**onsideration **F**actor' – **PCF**. And the consumer's PCF could be different for every hotel product he is considering to purchase. The higher the PCF the lower the 'value' for the consumer. A flat one price offer, as per the reverse auction model, blindly thrown out at a group of unknown hotels does not allow the consumer to factor in his PCF.

The model ignores the importance of product research conducted by consumers prior to buying the product. The consumer by placing a blind offer for a particular classification of hotel product does not get the opportunity to examine the product and understand its unique benefits for the consumer.

It is likely that the consumer at the beginning of his search may not even be aware of the benefits provided by a particular hotel product. The awareness of specific benefits of a product may result from the consumer's pre-purchase research activity. It may also be that some of these benefits will get communicated to the consumer by the hotel during this research phase. The reverse auction model of Priceline & Hotwire ignores this important activity that may be instrumental in the consumer choosing a particular hotel product over the other.

Product and service reliability, security issues, service standards, consumer's brand loyalty cannot be defined by blindly picking a hotel classification and placing a single offer for these "not so similar" hotel products. It could result in the consumer ending up with a totally different product than what the consumer bargained for.

C. THE PACKAGING MODEL:

The packaging model does make the discounted room rate opaque as the price gets buried into the total price of the package. However, this type of model can only attract a very small segment of the potential business as only consumers who need and planned to purchase the extra services offered in the package can benefit from it. The model is not geared toward disposing of a large amount of surplus inventories due to the very narrow focus of the model.

IV. THE ULTIMATE MODEL TO SELL HOTEL EXCESS INVENTORY

So what should the Ultimate model for selling hotel excess inventories be?

As stated earlier, the key to developing this ultimate model is, the contradictory interests of all parties have to be finely balanced so no one party gets an unfair advantage over the other.

I. For the hotel it should provide:

a. A universal platform (B2C) and a direct (B2B2C) channel (complementing the hotel's direct booking engine) to dispose its surplus inventories without exposing the discount to general public.

b. The model should not adversely affect the hotel's pricing and rate parity structures on other channels and segments.

c. The model should not result in a negative perceived value and image of the hotel in the eyes of the consumer.

d. The model should not commoditize the hotel product and should allow the hotel to make its "pitch" to the consumer.

e. The model should empower the hotel by keeping the hotel management in control all through the process of the sale and provide control over discount levels management is willing to offer.

f. And last but not least, the model should deliver the optimum yield on the sale to the hotel.

II. For the consumer the model should:

a. Provide the opportunity to purchase the hotel product at a price he is comfortable paying.

b. The model should provide the opportunity for the consumer to understand the 'value' of the product he is considering to purchase.

c. The model should enable the consumer to consider and evaluate multiple hotel products before making his decision to purchase one of them.

d. The model should deliver the satisfaction to the consumer that he has bought a product that best fits his needs at the best price.

e. The model should help the consumer understand the unique benefit of each product and assist the consumer in arriving at his perceived value for each product based on his specific requirements.

f. The model should keep the consumer in control of its purchase and deliver a pleasant shopping experience and satisfaction.

In short, the ultimate model needs to negate the shortcomings of the OTA and Reverse Auction models and it needs to be a universal solution that can reach out to a large audience.

V. A NEW, GLOBAL PATENT PENDING, BUSINESS MODEL FOR SELLING SURPLUS INVENTORIES

Travelsurf has developed a brand new business model called YC@YP (YOUR CHOICE @ YOUR PRICE), specifically designed for selling hotel surplus inventories. It has introduced this model on its B2C portal www.Travelsurf.com

The YC@YP model has automated the entire offline negotiating process and brought it into the online world and made it better - improved upon the model, made it more sophisticated, informative, effective, and efficient.

On Travelsurf.com, hotels list their surplus rooms, showcase their property/rooms/services while exposing only the "retail" price (Rack Rate) for their products. Travelsurf.com members (consumers) can search for hotels, create a 'short list' of hotel products (after understanding each hotel product's value). Members then proceed to make individual, binding offers for each of the hotel on their short list, and indicate their preference incase multiple hotels accept the offer. Hotels & consumers can counter each other's offers online and negotiate the ultimate Win-Win deal. The entire process is conducted online and is fully automated. To isolate the product from other segments, all offers on Travelsurf are non-refundable, non-cancellable and non-changeable. Consumers place binding offers, Travelsurf pre-authorizes the consumer's credit card through its payment gateway, Once a deal is consummated between the consumer and hotel, payment is processed and money delivered to the hotel.

The model ensures the consumer has the opportunity to research products, compare them with other similar and not so similar hotel products, and access the benefits of each one before placing the offers.

A consumer may place individual offers on different star rated hotels at the same time.

The model keeps the hotel and consumer in control of the negotiations all through the process and delivers a pleasant shopping experience and satisfaction.

Unlike the blind offer model of Reverse Auction, where consumers do not know what they are buying until they buy it and have paid for it. In YC@YP model consumers know exactly what they are buying and can place multiple independent offers (PCF factored) at a number of hotels simultaneously and can negotiate the best deal.

(i) BENEFITS FOR THE HOTEL

- ✓ The YC@YP model delivers to hotels the opportunity to reach potential consumers at low cost and sell its surplus hotel products at optimum margins, highest possible price.

- ✓ Hotel discounts are not exposed to general public and kept confidential. And by doing so, YC@YP ensures that hotel's other channels are not disturbed and the model does not have a negative impact on hotel's mainstream distribution channels.
- ✓ YC@YP model provides hotels access to built-in yield management tools so the hotel may optimize its yield, by taking into consideration the demand and supply of inventories, the advance purchase, size of the deal, the general market demand for similar products, before deciding on accepting or countering an offer.
- ✓ In order for the hotel to realize optimum value for its product, it is crucial that the hotel product is not commoditized and therefore in YC@YP model, hotel is provided the opportunity to make its "pitch" to consumer - and communicate its product's value proposition in comparison to other products. This helps the hotel to negotiate the best price for its product.
- ✓ When a deal is reached between the hotel and the consumer YC@YP model ensures that the payment for the product is efficiently and securely transferred from the consumer to hotel.
- ✓ YC@YP model provides hotel with the opportunity to "up sell" its product or promote complementing products or services once the original sale is completed.
- ✓ YC@YP provides hotel with ongoing market intelligence and extensive data mining opportunities. Hotel can access information regarding demand in the market for similar products, the average value of accepted offers, the average value of offers rejected, counter offers, average yield, etc.
- ✓ YC@YP market intelligence reporting can help the hotel fine-tune its product pricing even in other market segments based on the information provided and thereby improve its yield from other channels as well.
- ✓ Since all sales on the model are non-refundable, non-changeable and non-cancellable with payment in advance, the model helps the hotel improve its cash flow.

(ii) YC@YP BENEFITS FOR THE CONSUMER

- ✓ Provides consumers the opportunity to buy the products of their choice at a price they are comfortable paying
- ✓ Enables consumers to conduct multiple negotiations with hotels simultaneously.
- ✓ Since products being considered may have different value for the buyer, consumer has the option to make multiple individual PCF adjusted offers to a number of hotel products at the same time.
- ✓ Consumer can offer a different price for each hotel product based on the benefit to the consumer. Consumer can also indicate his priority preference in case more than one hotel accepts the consumer's offers.
- ✓ To assist the consumer in negotiating the best price, YC@YP provides sophisticated offer management tools to place offers, receive counter offer and the option to re-counter the hotel's counter, and repeat this process if necessary until a satisfactory deal is reached or until either party decides to terminate negotiations.
- ✓ To exert pressure on hotel to accept consumer's offer YC@YP model places time restrictions on hotel to act on the offer quickly. Hotel is aware that consumer may be negotiating with other hotels at the same time.
- ✓ YC@YP enables consumers to place offers with the hotel's competitors at the same time and simultaneously negotiate with other hotels.
- ✓ In the event a deal is not reached with one hotel, the consumer has the opportunity to purchase the next best product without having to start the purchasing process all over again.
- ✓ YC@YP ensures that all these options and decisions are available to consumer throughout the purchasing experience, that he is in constant control of his actions, and throughout the purchase process has a pleasant, convenient, shopping experience that is not dragged out for a long time.

VI. CONCLUSION

Given the soft economic environment where a majority of hotels are experiencing 30% - 45% of their inventories left unsold, it is imperative for hotels to sell these surplus inventories and generate optimum yields in order to stay profitable. The perishable nature of the hotel product makes it even more important that these inventories are sold in a timely manner and the sale does not affect the hotel's other distribution channels and market segments.

With the introduction of "Rate Parity" the opportunity for hotels to sell-off these unsold rooms at discounted prices has become much harder. Market pressures, hotel's cash flow pressures, combined with the present distribution models are forcing surplus hotels rooms to be sold as commodities with little differentiating criteria except for price.

It may be erroneously assumed that reduction in prices is beneficial for the consumer. However, this is not the case. Products sold at unsustainable prices will ultimately erode the level of service and standards offered to the consumer.

Many in the industry have come to accept this as "cost of doing business in the Internet age" – certainly a wrong assumption. New models, like Travelsurf's global patent pending model YC@YP, need to evolve and further fine-tuned so they may serve the industry better.

We invite you to share your thoughts, feedback and suggestions by emailing your feedback to feedback@travelsurf.com .

We look forward to hearing from you.

ABOUT THE COMPANY

Travelsurf (India) Pvt Ltd. (previously known as TSN Distribution Pvt Ltd.) specializes exclusively in the development of online distribution channels for the travel industry. The company is head quartered in Hyderabad, India and is opening offices in United States and Canada in 2011.

Travelsurf offers a suite of distribution channels including its new patent pending YC@YP model. Travelsurf.com – company's recently launched B2C branded portal - was released to the India market early 2011 and is experiencing a high level of acceptance from the hotel industry and from consumers. The company also offers a 'white label' YC@YP Direct engine that can be implanted into the hotel's website alongside the hotel's booking engine. The complementing engine is used by hotel to sell off its surplus inventories directly and when a 'sold out' status is reached on the YC@YP direct engine, traffic is re-directed to the hotel's booking engine. Travelsurf also offers 'white label' YC@YP B2C solutions to hotel chains, hotel associations, OTAs and other travel partners.

For further information, partnering opportunities, and Travelsurf franchise opportunities write to info@travelsurf.com.

ABOUT THE AUTHOR

Jim Burney Travelsurf's CEO has over 35 years of experience in the Lodging and related industries. During this period he has operated and managed hotels in North America, worked as an Independent Hotel Consultant, and as the Senior Hospitality Director for a multi-national computer company servicing the hotel industry.

Jim is a serial entrepreneur and has operated his own hotel technology companies since 1985. He's been involved in the design and development of a number of innovative technologies for the travel industry, and has a number of "firsts" to his credit. He was the first in the industry to introduce in 1986 a Unix based hotel management system running on micro-computers. During the second half of 1980s he drove the sales efforts for his PMS product to become the single most widely used PMS in Western Canada with a user base in 5 countries.

Jim's previous company Inter-Soft was the first to incorporate yield management technologies directly into the hotel management system in 1989. In 1994 Jim focused his company's attention toward online distribution. And, in 1995/96 Inter-Soft introduced the first OTA portal for the lodging industry, offering comparison shopping and seamless connectivity with its PMS system. Jim has been active in the research, design and development of a number of other technologies including a voice recognition technology based restaurant management system, Internet travel auction system, online travel distribution malls, and most recently the next generation Internet distribution network for Travelsurf.

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