

Pricing your tourism product

One of the key factors for success in the tourism industry is how you price your product. To ensure consumers purchase your product and distributors promote it, the price must be consistent, accurate and competitive.

Whether you are selling your product in the domestic or international market, it is important to precisely determine and understand the individual elements that make up the total price, and their impact on your product. In the tourism industry, price is often referred to as rate.

KEY PRICING FACTORS

In determining the rate for your product, you need to consider your operating costs, profit margin and distribution network costs (often referred to as commissions).

Operating costs

Operating costs include both fixed and variable costs.

Fixed costs

These are costs that are independent of output. They remain the same regardless of level of sales. Fixed costs include:

- rent;
- buildings;
- machinery;
- and insurances.

Variable costs

These are costs that vary with output. Generally variable costs increase at a constant rate relative to labour and capital. Variable costs include:

- wages;
- gas;
- electricity;
- cleaning, maintenance, repairs;
- materials used in production, etc.;
- stock, including stationery, linen, food, petrol, machinery and uniforms;
- bank fees;
- and marketing including research, advertisements, promotions, brochures, consumer or trade events, familiarisations for industry or media and travel costs.

Profit margin

Be realistic when calculating your costs to ensure you obtain a profit while retaining a competitive edge. It is important to check what your competitors are offering and determine which of your products can sustain a higher profit margin.

Distribution network costs

The distribution network consists of retail travel agents, domestic and overseas wholesalers and inbound tourism operators (ITOs). Your distribution network assists in distributing your product and raising your profile to consumers.

Some operators may choose to sell their product directly to consumers, however, using a distribution network to sell a product can improve sales and profitability. Working with distribution partners will incur costs, known as commissions. Commissions are the fees paid to your partners to distribute and sell your product. This is their income, which pays for the services they provide. These are not upfront costs, but costs incurred after a sale is made.

To include your product in their brochure, some distributors charge a fee or ask for a marketing contribution towards the brochure production costs. Be sure to find out if this is a requirement before agreeing to any brochure inclusion, and ensure that it will be an effective return on investment for your company.

Distribution network costs will vary depending on whether you are selling your product to the domestic and/or international market. If you are selling your product to the domestic market with distribution partners, you would generally choose to distribute via retail travel agents, domestic wholesalers and online travel sites. If you are selling your product to the international market with distribution partners, you would generally choose to distribute via a combination of ITOs, overseas wholesalers, retail travel agents and online travel sites.

Each level of the distribution network receives a different rate of commission, so it is important to research your distribution partners and understand where they fit in the distribution network.

Contact Destination NSW or your regional tourism organisation to find out where a distributor fits into the network.

ADDITIONAL PRICING FACTORS

Other factors to consider when pricing your product are:

Competition

Find out what your competitors are charging. Competitors' pricing strategies influence the maximum rate at which your product can be sold.

Demand

Demand for your product is generated by both existing and potential customers. Make sure you understand market demands and their impact on rate. Consider what can be added to your product to improve sales without sacrificing profit.

Target markets

Determine which markets you intend to target – domestic (intrastate or interstate), international (western/eastern or both). Research your target market in relation to product needs, price sensitivity, length of stay and disposable income.

Seasonality

Determine the fluctuations in business between high and low seasons.

ESTABLISHING YOUR RATES

In the tourism industry, you will hear of two different rates, the nett rate and the retail rate. The latter is also referred to as the gross, sell, rack or door rate.

When issuing your rates to distribution partners, clearly mark them as gross or nett with applicable validity dates.

Your nett rate

Nett Rate = operating costs + your profit margin

The nett rate is calculated by adding together all the fixed and variable costs of operating your business and the profit margin that you wish to make per sale. The nett rate is the absolute minimum you could sell your product for and still make a profit.



HANDY HINT

Allow for product development, maintenance and marketing costs on an ongoing basis. These factors should be covered in your rate structure without eroding your profit margin.

If you are using distributors (retailers, wholesalers and ITOs), the nett rate is what you as the operator receives from the sale of your product. Distributors will require your nett rate to add their mark up or commission.

For more information on pricing your product using distributors, go to Tourism Australia's publication *Planning for inbound success* under the Industry Resources tab at www.tourism.australia.com

Your retail rate

Retail rate = nett rate + distribution (commission) costs

Once you have established the costs of operating your product (nett rate), you can then factor in the costs for using distributors to sell your product. This will give you a retail rate. You provide your retail rate when dealing directly with customers (that is, the general public). This includes featuring it on your webpage and on any promotional material that is targeting the customer directly. The retail rate is the amount the customer pays and should be consistent across the entire distribution network.

Distribution costs are the commissions that you pay a third party to sell your product on your behalf. Commissions should not be considered a discount because they are a cost of doing business. You should treat the commission as your cost for employing a sales team to help you reach your target markets.

Industry standards for commissions paid from the retail rate for traditional distributors are:

- 10% of the retail rate for retail agents who sell directly to customers;
- 20% of the retail rate for wholesalers who sell to retailers or directly to customers;
- and 30% of the retail rate for ITOs who sell to wholesalers, who then on sell to retailers or customers.

(The commission rates listed are a guide only and rates may vary depending on individual contract details.)

Note: You do not need to pay commission to each of these distributors separately. If you use an ITO and the commission is 30%, they will then pass 10% on to the wholesaler and 10% on to the retail agent.

Commission levels for online travel sites vary, depending on how the site is operated, so make sure you do your research, before establishing a distribution deal with online partners.

Bad business

If you do not follow the industry standards for commission, the distributors will not sell your product to their partners and you will miss out on valuable sales and promotional opportunities.

It is important to maintain a good relationship with your distribution partners as they will be able to offer you marketing opportunities at a fraction of the cost of doing it yourself.

Examples of bad business decisions are:

- giving the ITO and wholesaler the same commission;
- providing only a 5% difference between commissions to an ITO, wholesaler and retail agent;
- and giving better rates to online travel sites for last minute bookings than the rates given to distributors.

HANDLING BOOKINGS

When handling booking enquiries, it is important to confirm who you are dealing with so that you quote the correct price. It is also imperative that you show both your nett and retail rates to all distributors. This will prevent any incorrect product pricing.

Which rate?

- Customers booking directly with you should be quoted the retail rate.
- Retail agents should be quoted the retail rate and they will then deduct their 10% commission.
- Wholesalers should be quoted 20% less than the retail rate.
- ITOs should be quoted 30% less than the retail rate.

Rate guarantee

Distributors follow a tourism calendar year from 1 April to 31 March. This is linked to their brochure production cycle. It is important to guarantee your rates for the tourism year in order to make your product compatible with distributor schedules. You should also have rates in place for up to 18 months in advance because distributors are quoting and selling this far ahead.

Domestic vs international

You should not have different rates for local and overseas visitors unless there is a variation in the product being offered. Customers should be paying the same rate whether they book directly with you, with an international travel wholesaler or via the internet.

You do not want to run the risk of customers comparing rates and discovering that one customer has paid much more than the other for the same service or experience. Nor do you want to disadvantage your distribution partners.

MANAGING YOUR BUSINESS MIX

It may seem that distributors receive a large portion of your takings, so it is important to understand the volume of business coming from each distributor as a percentage of your total business.

Below is an example of a possible business mix for an operator working in both the domestic and international market:

Sales	Amount	Nett Revenue	Commission Paid
Direct to consumer	40 rooms @ \$100	\$4000	Nil
Retail agent	30 rooms @ \$90	\$2700	\$300 (10%)
Wholesaler	20 rooms @ \$80	\$1600	\$400 (20%)
ITO	10 rooms @ \$70	\$700	\$300 (30%)
TOTAL		\$9000	\$1000

- **Total rooms sold:**
 - 100 rooms @ \$100 = \$10,000
 - Commission paid = \$1000
- Average commission paid = 10%

If a product has a retail rate of \$100 and 40% of business is booked directly by the customer, then no commission is paid. If 30% of business comes from retail agents then commission is paid at 10%. A further 20% of business comes through wholesalers with a commission of 20% and the remaining 10% of sales are made through ITOs with a commission of 30%.

If you make 100 sales, the total nett revenue is \$9000 and commission paid would be \$1000. While you are paying up to 30% commission on individual bookings, overall, the average commission on each booking is just 10%.

Maintaining the best yield is an important part of maximising your profit, but you can make a significant impact on your profits by influencing your mix of distribution sources. Generally, international business received via the distribution system will make up only a small percentage of your total business mix, and the cost of each sale as a percentage of your total income will be relatively small.

COMPETITIVE PRICING

Discounted prices

Discounts are often applied in the off season or to assist with yield management and can also be useful in gaining immediate business on websites such as www.needitnow.com, www.wotif.com or www.lastminute.com.

Usually, discounted pricing does not differentiate a product from the competition – as it can be quickly matched by competitors. Be cautious not to devalue your business by regularly discounting. This is also called dynamic pricing.

Value-adding

Value-adding is adding features to your product that enhance the perceived value. In comparison to discounting, value-adding can create a competitive edge and attract a greater market share. It can also help to prevent business fluctuations for products subject to regular peaks and troughs.

Examples of product value-adding are:

- a purchase incentive, such as champagne on arrival or complimentary parking;
- a package, such as three nights accommodation including tickets to a particular attraction;
- and bundling your products with others in the region to offer an experience.

PACKAGE PRICING

The following pricing methods are applied to packages and the most appropriate method depends on the type of product being sold.

Disguised pricing

Generally, discounted package components, such as accommodation, meals, entry fees, transport, are presented as one upfront cost. This method disguises the exact cost of individual components and also the extent of discount provided by individual operators. In general, a minimum of three elements should be included to disguise pricing.

Visible pricing

By offering a range of activities, attractions and options with each component costed at its full price, the final package cost may be too expensive to be appealing. This can be overcome by offering a flexible package with each component priced separately and available for purchase individually. The customer is then able to select their preferred package components according to their travel preferences and budget.

For more information on pricing, go to:

- your local business enterprise centre:
www.beca.org.au;
- your local tourist information centre or regional tourism organisation;
- and Tourism Australia's publication *Planning for inbound success* under the Industry Resources tab at www.tourism.australia.com

PRICING TIPS

- Do have a totally consistent rate schedule.
- Ensure you show any seasonal variations in product and clearly identify the rates and dates for each season.
- Don't have too many rate periods as it is confusing and makes your product more difficult to sell for distributors.
- Keep a record of who you have distributed rates to, so you can update them.
- Make sure validity dates and booking conditions are stated on rate schedules. Conditions might include child rates and ages, cancellation charges, amendment charges, free of charge (FOC) policy, minimum night stays, days of operation etc.
- Guarantee your rates for the period 1 April to 31 March and have rates available up to 18 months in advance.
- Ensure commissions for all distributors are factored into the retail rate.
- Be sure of different pricing levels for different distributors and quote accordingly.