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TITLE: Evaluating Strategies for Packaging Travel

ABSTRACT: Packaging has been a popular means of selling travel for over a century and in no small way has been responsible for the development of mass markets. In the light of this, it is surprising to find that there has been little research into the packaging phenomenon, especially from the point of view of an evaluation of packaging strategies. Principally, the literature documents flows of packaged travel or trends in sales. Very few researchers have attempted to model consumer preferences for packages. This paper reviews previous published work on packaging, but then characterises it as a form of price bundling, the general term used in marketing to describe a strategy of tying the sale of one product to the purchase of another. This more general framework is used to explain strategic motivations for popular packaging methods with an emphasis on consumers' decision-making in the presence of bundles. The paper examines the claim that the travel package, and especially the fully-inclusive tour, is at an advanced stage in its product life-cycle and that it will provide little stimulus to further growth in travel. The bundling paradigm suggests that unbundling travel can succeed, but there will remain a place for packaged travel products.

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INTRODUCTION

As early as the 1860's, the potential of new transport technologies to broaden the market for long-distance travel had been recognised. For example, Thomas Cook began chartering trains for temperance meetings but soon found that, if he sold the transport as part of a package including accommodation, meals, entertainment and, perhaps, a guided tour, there was a ready market. A century later, air transport technology was gaining consumer acceptance for long-distance travel and again packaging emerged as a successful marketing strategy, this time establishing the foundations for a global tourism phenomenon of massive proportions.

During the 1950's and 1960's, when commercial aviation was becoming a viable activity, airlines offering scheduled services had focused their attention on business people and on travellers who were prepared to pay high air fares, and these operators showed no readiness to broaden the market by discounting. However, travel agents in the UK began to prove that it was possible to charter entire aircraft and to develop profitable packages at competitive prices. The emerging package tour industry generated strong growth in airline travel and packaging has remained a key element of tourism marketing ever since.

By 1986, there were more than 10 million international travel packages sold in the UK alone and, though the rate of growth of this market appears to be declining, long-haul destinations are becoming more popular (Pearce 1987, Beachey 1990). In the case of the USA, it seems that one-third of all travel abroad by residents is on some form of package (Sheldon and Mak 1987). Also, the spectacular growth in outbound tourism from Japan has been achieved through the efforts of tour wholesalers (Bailey 1988) with approximately 70 percent of Japanese tourists travelling abroad on holiday buying a travel package (Bureau of Transport and Communications Economics 1992).

For Australia, an example of a long-haul destination, approximately 20 percent of all visitors and 30 percent of all visitors on holiday arriving in the country are travelling on a form of inclusive travel package or in a group tour. Also, fully-inclusive tours make up about 10 to 15 percent of the international business of Australia's largest tour wholesaler and the domestic airlines, prior to deregulation, were generating between 7.5 and 10 percent of their sales from packages (King 1991).

Given the significance of packaging as a strategy to develop travel markets, it is surprising to find that there is a paucity of published research on the subject. One line of investigation has been to map flows of packaged travellers (Pearce 1987, Beachey

1990). Another has been to document industry trends (Kale, McIntyre and Weir 1987, Quiroga 1990, Ryan 1991, Middleton 1991). Others have described the users of packages (Thompson and Pearce 1980 and Milman 1990), or they have looked at the way the travel industry constructs and promotes its packaged products (Sheldon 1986, Reimer 1990 and Reid and Reid 1990). The dominance of tour wholesalers in Japan has prompted some interest in distribution and business practices in that country (Bailey 1988, March 1993).

Whilst some researchers have criticised the industry for concentrating too much on mass tourism and for giving insufficient attention to changing consumer preferences (Gilbert and Soni 1991), there have been few attempts to understand consumer demand for packages or to analyse the strategic marketing objectives of different forms of packaging (Kinberg and Sudit 1979). Although packaging has evolved within the travel industry for over a century, the research community has shown little interest in evaluating packaging and package pricing strategies. Furthermore, the implications of packaging for traditional demand forecasting and travel demand analysis remain unexplored.

The basic feature of travel packaging is that two or more services are sold in a joint offer. This widespread practice is known generally as "bundling" and is the subject of an emerging literature in economics, business and marketing. Important themes are how to evaluate bundling strategies, understanding the impacts of bundling on consumer demand, the potential to use bundling as a form of price discrimination, and the role of bundling strategies in competition. This paper appeals to these bundling arguments to characterise travel packaging and then uses this foundation to analyse popular forms of travel packaging in terms of their likely effects on consumer demand. Also, attention is focused on the use of bundling strategies over the life cycle of products in order to provide insights into developments in the market for packaged travel. First, though, some of the most common forms of packaging will be described.

ANALYSING PACKAGING STRATEGIES - BUNDLING PARADIGMS

Bundling Arguments

Bundling is a marketing strategy employed across a wide range of industries wherein consumers are offered two or more products/services in a joint form. Versions of this that have attracted a considerable amount of attention from economists are "tie-in pricing" and "block booking". IBM, in leasing its tabulating machines at a low rate and then tying its customers into buying their tabulating cards at a relatively high price, exemplified the former, and Paramount's insistence on distributing its films in blocks illustrates the latter. One argument was that IBM was using (commodity) bundling to extend its market power into an otherwise competitive market, tabulating cards being relatively easy to supply.

However, the explanation that has dominated debates since the 1970's is that bundling was used as a form of price discrimination; IBM, by applying a mark-up on the cards, was able to extract a larger surplus from customers who used the machines more intensively. Paramount, it was believed, was using its block booking arrangements to set different prices in different markets for individual films, but still appeared to be non-discriminatory in its charging because all customers were faced with the same set of prices.

To explain further, assume that a monopolist knows the reservation price of each consumer, the maximum price the consumer is prepared to pay before deciding not to buy that product. The most profitable course of action is to set a price for each consumer just equal to his/her reservation price, a practice known as "first-degree price discrimination". Usually, this is illegal, or at least it is impractical, and bundling can provide a profitable, second-best option.

How bundling fills this role this is illustrated in Figures 1 to 3. An important assumption is that the products are independent in demand so that the consumer's reservation price for the bundle is simply the sum of the reservation prices of the components (Adams and Yellen 1976). In Figure 1, the monopolist has two products, say trips and electrical appliances and is constrained to set a single price for each product, p_1 and p_2. A particular consumer who will pay no more than r_1 for the trip and no more than r_2 for the electrical appliance will buy only the electrical appliance; the consumer is unwilling to buy the trip at its current price. Assuming that there is a distribution of consumers placed in (two-dimensional) "reservation price space" the effect of setting individual prices for each of the products is to segment the market into four mutually exclusive groups: those who buy neither (area A), those who buy both (area D), buyers of appliances only (area C), and buyers of trips only (area B).

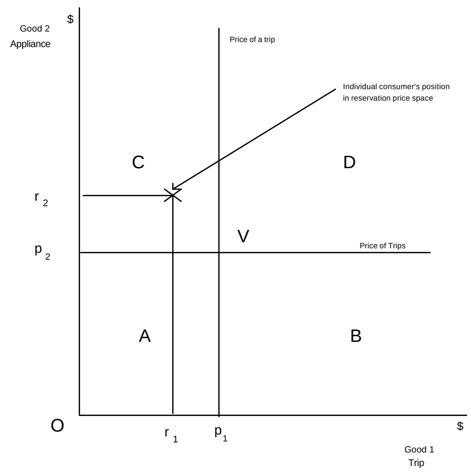

Figure 1. Pure Components Pricing

An alternative (Figure 2) is to offer the bundle alone (pure bundling) at price p_b. In this case, the market is segmented into two areas covering consumers who buy both (area D) and consumers who buy neither (area A). The third case is when the monopolist sells the trips and electrical appliances as separate components **and** also sells a bundle (mixed bundling). In Figure 3, the bundle has been offered at a discounted price $p_b < p_1 + p_2$. If no discount were offered, the bundle price line would pass through point V, but under the assumptions in the Adams and Yellen model, there would be no advantage to the firm in pursuing this option. The implicit prices of the less preferred components would be identical with their actual prices and there would be no change in consumer behaviour. Deciding whether this strategy is more profitable than the alternatives of pure components or pure bundling pricing requires analysis of the various demand segments differentiated according to positions in reservation price space. For example, those consumers lying in area UVT previously purchased both components, but now they can buy the two at a lower bundle price with a consequent loss of revenue. Against this there are new customers for both products in the area VXY.

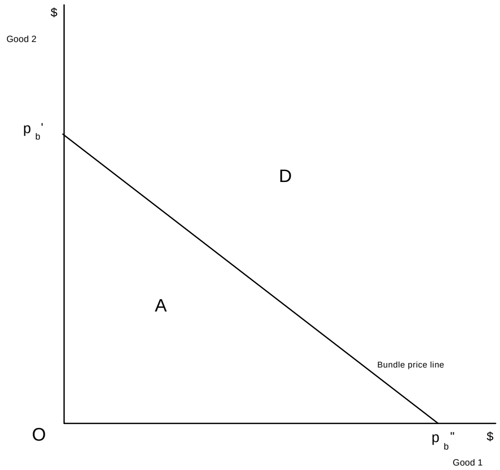

Figure 2. Pure Bundling

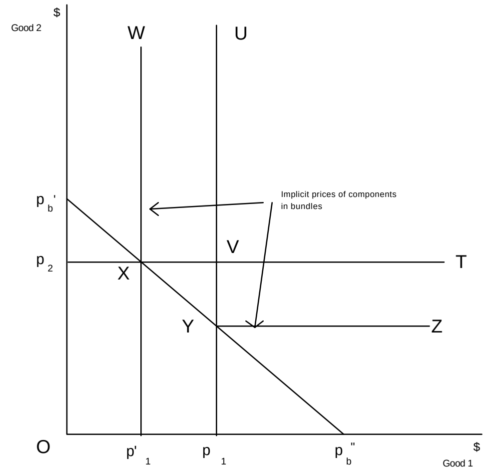

Figure 3. Mixed Bundling

The interesting gains come in the areas UVXW and TVYZ where (previous) purchasers of single components have been induced into buying the second product (cross-selling). Take a consumer placed in area UVXW who is characterised by having a relatively high reservation price on product 2 and a relatively low reservation price on product 1. With separate component prices, only product 2 would be purchased. However, given this preference and given the bundle price, it is as though the consumer faces an implicit price for product 1 that is equal to the difference between the price of the bundle and the price that the consumer would have had to pay to purchase product 2, and this implicit price is now sufficiently low to induce a purchase.

So, the use of a mixed bundling strategy adds some degrees of freedom for the regulated monopolist; high prices can be set on each of the components for those consumers who value one but not the other, whilst the discounted bundle is designed to appeal to more price conscious consumers. Which strategy is the most profitable, of course, requires an understanding of how consumers are distributed in reservation price space and a knowledge of the relative mark-ups on each of the components.

In a competitive situation, the prices of the components would be driven down to marginal costs of production and there would be no scope for offering a discounted bundle. Bundling in competitive industries was thought to be uninteresting; it could be profitable only when there are complementarities in production, and the general presumption was that these were likely to be insignificant in practice. The "bundling as price discrimination" model continues to be extended in the literature, but the prevalence of bundling in competitive, service industries has prompted renewed interest in the topic.

Appreciation is growing in economics that price discrimination can arise in markets that have a large number of sellers. For example, Stiglitz (1989) has argued that, if information is costly, there can be a variety of market imperfections including price rigidities and equilibrium price distributions even with homogeneous products. As the number of firms increases, the cost of searching out the low cost seller increases so that, paradoxically, firms in markets with a few sellers can have a greater incentive to engage in price competition than firms in markets with a large number of sellers. However, an even richer set of possibilities is suggested in the marketing literature wherein price is treated as one element of a marketing mix chosen deliberately in the pursuit of business and marketing objectives (Kotler 1991). Within this framework, bundling has been cast as just one of the many pricing strategies open to business, hence the common term for the practice has come to be "price bundling".

An extensive list of marketing descriptions of bundling testifies to its widespread use (Eppen et al 1991). More generally, the variety of bundling practices is evident in the motives that have been attributed to it, including:

- a desire to take advantage of complementarities in production (economies of scope)
- exploitation of complementarities in demand
- maintenance of control over product performance
- a means of average pricing when production results in units with variable quality that is difficult for buyers and sellers to assess ex ante
- using bundling to ensure that as many market segments are tied to the lead product with the resultant capture of a larger total market
- as a means of building customer loyalty, reducing incentives for customers to sample other supplier's products
- as an introductory strategy to define the position of a product
- to induce customers to trade-up and to purchase additional components or to buy higher quality
- discouragement of some forms of free riding
- avoidance of controls on price on individual products
- extension of monopoly power in one market to an otherwise competitive market
- price discrimination

Mostly, bundling has been observed when the firm has a product line and when there is scope to reduce costs of production, increase overall yield by directing consumers to combinations that have higher mark-ups, to expand markets and to maintain control over product performance. The products tend to be related in some way and it is possible that business arrangements are designed precisely in order to bring these products together, the travel industry being a good example of this. However, bundling practices are proliferating and numerous examples of seemingly unrelated products such as travel and electrical appliances have been linked in joint promotions. The popularity of bundling/packaging is likely to encourage follow-the-leader or copy-cat behaviour but, as Eppen et al point out, implementing a bundling strategy requires ... *a serious commitment to an analytical decision-making process* (Eppen et al 1991: 40). Evaluation of bundling strategies is addressed below, but it is necessary now to place the argument in context by more carefully characterising travel packaging as a bundling phenomenon.

Travel Packaging

Insofar as the Australian travel industry is concerned, packaging has had to be developed in the absence of a significant air charter operation. Although competition among the scheduled airline operators appears to be strong, it is notable that two carriers, Qantas and Air New Zealand, carry over 50 percent of all international traffic into and out of Australia. These same two carriers have strong links with the two dominant tour wholesalers active in selling international travel to residents, Jetset and Jetabout, the latter being entirely owned by Qantas. Attention was drawn above to the popularity of packaging in the outbound Japanese travel market and the dominance of large tour wholesalers in Japan; the two largest firms make over one-third of sales of overseas travel in Japan (March 1993). In the domestic Australian market, the two trunk route carriers have their own travel divisions with powerful distribution capabilities, and they have extensive ownership and other linkages with resorts, hotels, rental car companies, coach operators and regional airlines.

The general picture is that the travel industry to, from and within Australia is highly concentrated, at least in terms of the firms that are in a position to influence the sales of travel packages. This is not the only country where this observation has been made, Japan being a notable example, and concerns could arise that packaging cum bundling is used to pursue price discrimination or to entrench market power. Certainly, there is recognition in the industry that larger airlines are able to use packaging to advantage. For example, it has been reported that the alliance between Northwest Airlines and KLM resulted in ... *a travel-package option that most competitors cannot match*

(McKenna 1993). Also, Air New South Wales used its market power in travel packaging as part of an entry strategy to compete with the then independent East-West Airlines on the route between Sydney and the Sunshine Coast in 1980 (Air New South Wales 1989). An even more explicit statement about the use of packaging by airlines is that:

> *Bundling of air transport and ground tourist services has been used by airlines not only as a marketing tool, but occasionally as a means for differential pricing practices that were otherwise barred by regulation or cartelization.*
>
> [Kinberg and Sudit 1979: 52]

Debate on the matter in Australia has focused more on the apparent unwillingness of the two major carriers to promote packaging under the two-airline policy. Data on packaged travel are not readily available, but it has been reported that 7.5 percent of Qantas' domestic (Australian Airline's) passenger traffic is carried on a package. Ansett Airlines reports selling 100,000 packages each year, yielding 10 percent of its revenue, and the Queensland Tourist and Travel Corporation claims to sell another 80,000 to 100,000 packages each year (King 1991). The dominant method of packaging in the domestic travel market has been for the airlines to advertise special deals on accommodation and other travel services that can be added on to one of their discount fare deals. This has left little scope for wholesalers or even retail agents to develop their own packages.

It has been noted that deregulated airlines in the USA became more aggressive in their use of packaging of air transport, accommodation, rental cars and other ground services (Collison and Boberg 1987). The extent of complementarity in these services clearly is important, but joint sales and promotion have been extended to seemingly unrelated products. For example, purchasers of computers, cameras and film have been given coupons that entitle them to discounts on air fares, and the airlines have joined forces with unrelated companies such as Computerland, Kodak and Polaroid in joint promotions. This practice has become common in Australia, one example being the offer of a free flight with repeat purchases of petrol with the condition that customer must purchase accommodation for a specified number of nights. For example, BP advertises free flight tickets with Ansett Australia to a range of destinations provided that customer makes four purchases of $20 or more at a participating BP Service Station or a Food Plus Store. Qualifying customers receive a free flights booking voucher to be used with joint purchase of accommodation at specified resorts.

Since travel and accommodation are the key ingredients of any travel activity, most packages are based on some joint offer of these two services. A common strategy is to offer the accommodation at a reduced price if the consumer first pays for an airline ticket. For example, Qantas Jetabout Holidays promotes travel to South Pacific destinations on this basis, although it is usual to cite an all-inclusive price for the international air travel, greeting, and departure transfers with accommodation available at a range of resorts. Thai International allows its customers on flights from Australia to Europe to fly in Thailand free of charge conditional on a purchase of accommodation for a specified number of nights at a resort in Thailand. The more common example is the practice of domestic airlines selling accommodation to its customers at discounted rates.

Add-on pricing is uncomplicated and it can be developed and promoted at a relatively low cost. In contrast, fully-inclusive tours require a lead time for production and distribution of up to 18 months and usually involve significant investments in the form of payments for airline tickets and accommodation and for the preparation of promotional materials. The customer might be attracted to the deal because of a cost saving, but the arrangement can reduce the costs of searching and completing the travel transaction. One-stop shopping has its advantages, and the travel seller can use this opportunity to extract a higher margin from the transaction.

Fully-inclusive tours extend the range of benefits available at a single price. For example, Westbus Luxury Coaches offer a winter ski package from Sydney that includes the transport to the snow fields, entrance fees, accommodation, some meals, entertainment, and discounted access to ski hire, lifts and lessons. It is common for the domestic airlines to advertise packages for travel to the Great Barrier Reef or the Gold Coast based on airline travel, transfers, accommodation, use of resort facilities, and free nightly and daily activities and entertainment.

The fully-inclusive tour makes it possible for the consumer to reduce the costs of searching and purchasing, and again the travel seller might be able to extract some of this surplus, but the common presumption amongst travellers is that packages are cheaper than independent travel. Inspection of package prices suggests that there is some factual basis for this view even though the prices of Australian package tours are relatively high in Japan (Bureau of Transport and Communications Economics 1992).

Theme packages are exemplified by Ansett Australia's Melbourne Cup Holidays promotion in which it requires the purchaser to buy a ticket from within its range of offers and then makes accommodation available at attractive rates along with entry to racing events. Packages to attend *Phantom of the Opera* in Melbourne have generated a substantial amount of business. This type of package makes it possible for the customer to attend an event that might be otherwise difficult for an individual to arrange. By block booking tickets, the airline or travel wholesaler can arrange entry on a very favourable basis, and the package overcomes the logistics of attendance. The package enhances the performance of the service "attending the special event" and permits the travel industry to cross-sell its services.

Guided and escorted tours have been popular for international trips, especially when the customers are inexperienced travellers and when there are marked language and cultural differences between host and guest. Another context is when the customers are seeking information about the destination/attractions. For example, tours from Australia to China tend to be fully-inclusive tours with guide and interpreter services. Similarly, a large number of the visitors to Australia from Japan have involved an escort or local tour guides.

These types of packages provide all of the advantages of one-stop shopping, but they involve a greater degree of commitment by the tour operator to logistical support and control. Typically, these tours require that service providers meet high standards of reliability and consistency. The package has been designed on the basis of the tour operator's detailed knowledge of the attractions. The total service approach is appealing to inexperienced travellers because it demonstrates how their travel experience can be enjoyed.

The joint promotion, however, suggests some of the more subtle and complex motives in packaging. There is little consumer loyalty, for example, in buying petrol. The BP promotion discussed above illustrates a mechanism for encouraging repeat purchases. By linking the sales of petrol to an attractive benefit, travel, BP clearly aims to retain existing customers and to perhaps, attract new customers. However, for the travel suppliers, the advantage is that there is a large market of purchasers of petrol and the prospect of structuring a deal that will induce some cross-selling is very attractive.

Jetset, the market leader in outbound Australian travel, has said that fully-inclusive tours have declined from 25 percent of its total sales in 1986 to 10-15 percent in 1990, and these are mainly concentrated on nearby destinations (eg Fiji, Bali, Thailand) or on coach tours of Europe. The tendency amongst its customers now is to buy an air ticket and then to choose from a selection of accommodation and tour arrangements (King 1991). A similar trend appears to be occurring in Japan with more customers seeking to purchase discounted fares and to make their own ground arrangements at the destination (March 1993). In the UK, it is claimed that the intense competition that exists in the travel sales and distribution industry has led to too great a concentration on reducing the price of packages with a resulting deterioration in quality (Gilbert and Soni 1991). In the USA, there is a different argument that consumers are placing increased emphasis on all-inclusive prices (Troy 1993), and there are further reports that senior travellers, a segment of increasing importance, has a distinct preference for packaged travel (Javalgi et al 1992).

This presents a somewhat confused message about the likely future of packaging. Below, it will be shown that the bundling paradigm can shed some insights into this important matter. To summarise at this point, much of the motivation for travel packaging is likely to arise from production and demand complementarities, but there is a high degree of concentration in the industry and there is a possibility that bundling can be used as a subtle means of exercising market power. Attention is drawn to the warning that one motivation for price bundling is to make rivals in oligopolistic markets less aggressive (Carbajo et al 1990).

Finally, travel packaging exemplifies bundling, but it is not by any means the only way the advantages of bundling strategies can be reaped in long-distance travel. For example, an airline can operate a single-class configuration or it can offer a basic service and one or more luxury standards as options. Airlines provide more comfortable lounges for some customers, either because they have joined a club or because they are purchasing the luxury version of the service. These, and other marketing initiatives, can be interpreted as forms of bundling. Bundling arguments can be used in the context of cruising and integrated resorts to evaluate whether to price for use of individual facilities or services against a policy of setting an all-inclusive price. Finally, it has been demonstrated that the bundling framework can be used in the design stage of facilities for tourists (Bojanic and Calantone 1990a,b).

BUNDLING'S POSITION AS A PRICING STRATEGY

A Classification of Pricing Strategies

The foregoing discussion has illustrated the diversity of bundling practices in tourism that is not matched by an obvious attention to evaluation. Packaging/bundling is one option within a wide variety of pricing methods, and it is important to appreciate its distinctive features and to identify the conditions that favour different types of bundling. One way of proceeding is to distinguish among pricing strategies according to the way the particular mechanisms exploit the sources of shared economies involved in serving a number of market segments simultaneously (Tellis 1986). Further, pricing strategies target consumers according to differences in search costs, reservation prices, and non-search, transaction costs.

Some customers are aware that there are lower prices available and are prepared to wait and/or search whilst others will purchase at the first opportunity. The consumer's decision depends upon the expected gain, itself a function of the probability distribution of outcomes, the magnitude of the gains associated with those outcomes and the costs of searching. Non-search, transaction costs arise because of such factors as the need to travel to purchase, opportunity costs of money, and switching difficulties. These differences make it possible to set a range of prices in separate geographic markets or to maintain high mark-ups on products where customers would need to incur an investment (or sustain a loss) before they switch.

The main types of pricing were identified by Tellis (1986) as:

- differential pricing - setting a range of prices in different markets for the same physical product (for example, second market discounting, periodic or random discounting)
- competitive pricing encompasses responses to rival firms (eg predatory pricing, price signalling, geographic pricing)
- product line pricing for firms with multiple products

Bundling was classified as a form of product line pricing along with "premium pricing" and "complementary pricing". With premium pricing the firm has two market segments, those who are prepared to pay more for higher quality versions of the product and those who want a basic version at a lower price. The problem for the firm is that, if it supplies only one segment it makes a loss; the only profitable strategy here is to supply both the basic version and the enhanced version simultaneously. Complementary pricing takes the form of captive pricing, two-part tariffs and loss leadership, and it involves the sale of complementary products or services. For example, razors are sold at a low price and profits are earned on subsequent sales of blades. Loss-leaders can be used to get the customer into the store and then the costs of travelling to another store generates sufficient inertia that higher mark-ups can be earned on other lines.

Bundling also relies on consumers having different reservation prices for non-substitute products in a seller's line. However, "periodic" or "random" discounting need to be considered as alternatives to bundling. If consumers are heterogeneous because they are prepared to pay different amounts to consume the same product at different times (eg air fares in peak season versus shoulder and off-peak), then periodic pricing is most appropriate. Random discounting applies when there are variations in the costs of searching for lower prices and when some consumers are prepared to wait and search for a low price while others accept the first price on offer. In this case, a higher price can be set normally, and random discounts are offered from time to time to capture the price-conscious searchers. The critical factor favouring bundling, according to Tellis, is that the consumer can be induced to believe that there is only one opportunity to purchase at the discounted price, the purchase opportunity is perishable. With bundling, the firm is trying to maximise the total yield on the consumer's purchase decision. For example, each sale of an airline ticket is regarded as a perishable opportunity to sell related travel products.

The key contribution this type of classification scheme provides is that it demonstrates that firms can choose from among a wide variety of pricing methods and that each option is favoured by a particular set of conditions. Choice of any particular method, bundling for example, should be based on a sound appreciation of the conditions and of the alternatives. However, Tellis takes too narrow a view of the motives for bundling. For one thing, bundles can be developed from products that are unrelated in any direct way; bundling can be used to **create** the urgency to buy both products. Also, the motive for price bundling can be to influence the actions of rivals (Carbajo et al 1990). Finally, all of the practices cited as product line pricing by Tellis have been described elsewhere in the literature as versions of bundle pricing, and his criticism that price bundling had not been *presented adequately in the marketing literature* is left unresolved by his, or by others', classification schemes (see, for example, Cannon and Morgan 1991).

Evaluating Packaging/Bundling Strategies

Recent contributions in product line pricing illustrate the difficulty in simple characterisations of pricing strategies. An important observation is that the firm must choose an approach for each and every product, allowing for complementarity and substitution among the demands for its own products as well as taking account of the actions of rivals. In addition, it is necessary to consider whether to offer all products and whether it is better to sell products as bundles.

To illustrate this last point, suppose that a travel wholesaler can sell airline travel, accommodation and/or packages of both. In this case, the evaluation of selling strategies must encompass as many as eight options in which the firm offers consumers:

- no products (abandons the business)
- airline travel only
- accommodation only (stop selling airline travel)
- both travel and accommodation
- packages only
- air travel plus packages (but no separate accommodation)
- accommodation plus packages (but stop selling airline travel separately)
- air travel, accommodation and packages

The complexity of the problem expands as other travel products are considered for inclusion in the line; the number of options to consider is 2^{2N-1}, where N is the number of products in the line. Potentially, optimisation models can be used to decide which option maximises profits. Unfortunately, the path to developing a successful model is to impose restrictive conditions and the result is that the model can be applied only in a narrow set of circumstances (Hanson and Martin 1990); determination of optimal bundle prices presents considerable practical problems. What has emerged, though, from this line of research is an appreciation that:

> *Utilizing bundling forces a firm to think about its entire product line when determining optimal prices. It must also be alert to the effects of its other marketing variables, as some of the most basic intuitions carried over from single product models need not hold in the more complicated bundling regime.*
>
> (Hanson and Martin 1991: 163)

An alternative approach is to find a search procedure that will yield an optimal solution. One of the early contributions to this field of inquiry (Kinberg and Sudit 1979) dealt explicitly with travel packaging but the paper appears to have been ignored by researchers in travel and tourism. The first step in this procedure is to eliminate any proposed components of a package that are unprofitable if they are sold alone. Then all possible packages are scrutinised to ensure that there are no illogical combinations. A more difficult step is to test to see whether the act of bundling within the remaining packages has a positive impact on the level of demand. The procedure then requires that total profits of selling all remaining package combinations be calculated, and then the effect of eliminating one package at a time is observed. The search ceases when it is not possible to increase profits by eliminating any of the possible packages. Clearly this requires a considerable amount of information and is tractable only for relatively simple packaging contexts. More important, the solution only holds generally if profits are sub-additive; otherwise, the search procedure is even more difficult.

A more intuitive evaluation of bundling options can be provided by focusing directly on the role of the different sources of complementarity in demand by exploring their possible contribution to strategic marketing objectives (Guiltinan 1987). For example, consider a strategy of cross-selling (the objective is to get consumers who buy only one product to buy both) in the context where a travel agent sells more airline tickets than accommodation. Here there are opportunities to sell more accommodation to airline travellers than there are opportunities to sell airline travel to accommodation purchasers. In a cross-selling strategy, it would make sense to reduce the price of airline travel conditional on the purchase of accommodation, assuming of course that the demand responses are the same.

Now reflect on the sources of complementarity in demand and, depending on the importance of information and transaction costs, utility of joint consumption and image-enhancement effects, different bundling strategies are suggested. For example, search and transaction costs can be relatively high for long-distance travel. A journey abroad might require travel on several airlines and booking accommodation, local transport and other travel requirements can be a daunting task for a frequent flyer let alone less experienced customers. Travel agents are specialists in providing advice on these matters, but the practice is for agents to be paid through commissions on sales rather than on a consultancy fee basis. This provides the agent with a contractual link to the service provider and the customer has to weigh up the advantages of shopping around for further information or of accepting a risk that a better service/price option has been foregone.

Thus, accommodation, transport and other package elements complement each other because there are economies in purchasing them together. However, other sources of complementarity could be present. There are circumstances when the utility gained from travel will be greater when the components are purchased together. One example would be that travelling on the destination country's national airline is considered by some tourists to be a part of the experience. Image-enhancement effects also arise. An airline that can sell exclusive, luxury accommodation at the destination might enhance its own image.

It is conceivable that complementarity arises because the purchase of one product reduces the costs of gathering information about the other, but it is possible that this type of complementarity works in both directions. For example, a consumer evaluating a travel package could readily obtain information about airlines and air fares, but it is likely that it would be far more difficult to assess accommodation at the destination. The consumer could well adopt the attitude that the tour wholesaler or the airline responsible for putting the package together is in a better position to choose the accommodation component. So, purchasing air travel involves a reduction in the costs of becoming better informed about accommodation. In the case of air fares and car rental, there might be bi-directional gains because information might be gathered from closely-related sources. Products that enhance customer satisfaction are likely to offer uni-directional gains whilst image-enhancing combinations tend to have bi-directional effects.

Guiltinan shows how these observations together with a statement of corporate objectives in terms of the importance of cross-selling versus gaining new customers or retaining existing customers leads naturally to the adoption of different bundling strategies. For example, one-directional complementarity is favoured for cross-selling. Selling the leader in a mixed bundle at a discount conditional on purchase of the other product at the normal price (mixed-leader strategy), would be better in this case, for example, by selecting a bundling partner that enhances the utility of the lead product and/or selecting a bundling partner that gives the consumer reduced costs of information when purchased with the leader (which might also be offered at a reduced price). So, bundling accommodation with air travel might make it possible to sell more air travel. If bi-directional gains are required, selling both products in a mixed bundle at a single price (mixed-joint bundling) might be more appropriate.

Suppose that the objective is to generate new customers for both products (ie customers currently buy neither). If a mixed-leader strategy, discounting the price of the leader if the other product is purchased at the same time at its normal price, is adopted the demand for the leader must be enhanced if its partner is a strong complement. It helps if the leader's demand is price elastic, and this is more likely if the leader's attributes are of the type that can be searched and evaluated prior to purchase. In this case, a wider range of alternatives is likely to be considered so that demand for that product then becomes more responsive to price changes. An important consideration is whether the second product produces search economies for the leader (either uni or bi-directional). In a mixed-joint strategy, the customer can buy each separately or as a bundle. This could be successful if the reservation price of the bundle exceeded that of the sum of the reservation products to a sufficient degree; a price reduction for the bundle and an elastic demand also help. If, say, air travel and car rental have elastic demands (they tend to have search-based attributes) and their joint purchase reduces search costs of both, mixed-joint bundling might be worthwhile.

These examples demonstrate that deciding upon an optimal strategy depends on the particular conditions and upon the marketing objectives of the seller. However, the preceding comments dealt with demand relationships, and it is profits that matter ultimately. The gains to be had from bundling have to be offset against reduced profit margins from previous buyers of the separate services who now buy the bundle at a different profit margin together with the reduced margins from those people who already purchased both. In a cross-selling strategy, if the profit margins on the two services are different, the gains from bundling come from shifting consumers from the low margin service to the bundle. Under mixed-leader bundling, it is better to make the service with the lower profit margin the leader. With mixed-joint bundling, the strategy is more effective when sales levels are about equal and when profit margins are similar. Note that, when new customers are being sought, it might be possible to quarantine the effect of a mixed-leader case, making the strategy more attractive than in the cross-selling case.

The general conclusion from this analysis is that determination of optimal packaging strategies is difficult whether use is made of optimisation methods, search procedures, or intuitive arguments. In any case, attention is now focused on a key requirement in all approaches, a knowledge of the effects of packaging on consumer demand.

Bundles and Consumer Demand

The literature offers two distinct explanations about why consumers respond differently to bundles. In economics, bundling as a price discrimination argument has been dominant and, though the components of the bundle can be complements, most interest has centred on explanations of bundling when the reservation prices of the components are additive. The importance of bundling arises through the effect it has on reducing the amount of variation in the reservation prices in a distribution of consumers; though the average reservation prices of the components are additive, the variances in the distributions of reservation prices are not (Schmalensee 1984). That is, the predominant interest of economists has been in the properties of the distribution of reservation prices across consumers, but the assumption that a consumer simply adds the reservation prices of the components in valuing the bundle is widely held to be self-evident.

In psychology and marketing, there has been a more extensive investigation into the way consumers integrate information to arrive at valuations of multi-attribute bundles. One possibility is that consumers do not simply add their reservation prices when they evaluate a bundle; the so-called "preference reversal" effect. This has been tested using a hybrid conjoint analysis method in the context of guests' willingness to pay premiums for hotel amenities (Goldberg et al 1984). In particular, a hybrid conjoint analysis procedure was used to test whether, for different bundles of hotel amenities, the sum of consumers' valuations of the amenities taken one at a time differed from the value placed on the entire bundle. The general conclusion was that simple functions of respondents' self-explicated utilities for bundle components are not good predictors of their preferences for the bundle. The overall bundle price added significantly to the explanation of variance in the preferences for the hotel amenities.

More recent tests have been made on an alternative explanation of consumer's valuations of bundles, prospect theory, according to which consumers adopt a reference point and evaluate gains and losses relative to that point, and consumers' preference functions are concave for gains and convex for losses (Drumwright 1992). The implication of this is that consumers prefer to segregate gains and to integrate losses. That is:

> *Inasmuch as buyers view the separate products in a bundle as distinct benefits (many positive values or gains) for one price (a single negative value or loss), they will be more inclined to buy the products in the bundle than they would be if the products were offered separately (many positive values for many losses).*
>
> (Drumwright 1992: 313).

If consumers integrate joint outcomes in such a way that losses are cancelled out against the gains, there is scope to induce them to purchase products in a bundle that they would not purchase individually. So, a consumer faced with the decision to pay separately for all of the services provided in a travel package might act differently when offered an all-inclusive price. Whilst both the economics and marketing theories predict more will be purchased with bundling, the economic argument suggests that consumers will reject bundles that contain negative surpluses. In contrast, marketing theory accepts that bundles can lead consumers to consider the benefits one at a time while aggregating the losses so that negatively values on some components can be cancelled out against the gains. Drumwright designed an experiment in the context of automobile choice to see whether consumers buy more under bundling. Though of an exploratory nature, this work has revealed sufficient "anomalies" in consumers' valuations of bundles to lend support to the view that valuations of bundles can be super-additive or sub-additive.

Though some insights have been provided into the types of relationships among products that would produce successful bundles, there is limited empirical evidence about the structure of preferences for bundles. It is not possible, a priori, to favour one theory about preferences for bundles over another. However, experimental analysis of consumer preferences employing stated response methods, especially those appealing to a random utility framework, offers potential to explore these matters.

Given the importance of packaging to the growth of tourism, especially in an international context, it is surprising that there has been little interest by researchers on the specific effects of packaging on demand. Also, the effects of restrictions on promotional prices is overlooked in all but a small minority of cases (Hensher and Louviere 1983). One approach has been to estimate the demand for package tours (Askari 1971), but there is only one published study of the role of package attributes and personal characteristics on consumers' choices of packages versus independent travel (Sheldon and Mak 1987). These authors predicted choice of a package from mainland USA to Hawaii using a binomial logit model, but the context did not allow any testing of the effect of packaging on the overall level of demand or of the effect of packaging on the revenue earned by the suppliers of tourism services.

The probability of choosing a package was found to increase with the size of the discount on the package price, the age of the traveller and the number of destinations visited. The probability of travelling independently increased with duration of the journey, wealth of the traveller, size of party, and knowledge of the destination (ie repeat visitors). Changes in wealth and age had the greatest impacts on choice, followed by number of destinations, number of previous visits, and price differences had the least impact.

The finding on the influence of price is particularly interesting given the importance attached to this variable in aggregate travel demand models. If, as these results suggest, travellers are drawn to purchase packages depending on their personal characteristics and non-price attributes of the packages, doubt is cast on approaches using aggregate demand models that are not capable of discerning these influences. Admittedly, Sheldon and Mak took destination choice as given and "price" was defined in relative terms, but the approach demonstrates the value of using a behavioural choice model estimated on data obtained from individual consumers. If the price differential has a minor role in the decision to travel independently or to travel on a package, and if packaged travel represents a non-trivial share of the market, then care would need to be taken in modelling phenomena such as destinations visited, carrier or mode choice, and length of stay.

PROSPECTS FOR PACKAGING

Attention was drawn above to several, sometimes conflicting, observations that have been made about consumer demand for packages. These can be summarised as follows:

- there is intense competition in the packaged travel market that driving price and quality down
- senior travellers are more likely to purchase a package, and the increasing importance of senior travellers in travel markets suggests good prospects for packaging
- there is a general trend in developed travel markets towards all-inclusive pricing of travel
- experienced travellers prefer to make their own ground travel arrangements and they seek greater independence in their travel arrangements

The last of these points is particularly important for Australia because it appears that this is a prevailing view of consumers in the domestic market (Dangar 1988). An even more significant observation, perhaps, is that there are signs that the Japanese outbound market is shifting away from its overwhelming preference for fully-inclusive packages (March 1993). Taken together, these arguments might indicate that the travel market is at a mature stage in its life cycle.

The general understanding of the life cycle effect is that, after initial introduction, products pass through several stages of market development. Specifically, the following phases are observed in a wide variety of situations:

- introduction - the product is first placed on the market and the challenge is to demonstrate it to potential users and to achieve a critical mass of adopters. It is common for this phase to begin with slow growth and low profits.
- growth - through word-of-mouth and through promotion, customers begin to accept the new product and it enters into a stage of rapid growth
- maturity - the firm now faces imitators and, though total industry revenue is growing, rivalry is undermining profits and continued growth in industry sales is driven by price-cutting

- saturation - sales have reached a peak and the market has fallen into the hands of a small number of rivals
- decline - innovators are selling a different product, customers are deserting in increasing numbers and sellers are taking whatever profits they can (cutting any unnecessary expenses and curtailing investment in the product)

The line of argument that has been presented by some is that the fully-inclusive tour is a product of an immature travel market. The fully-inclusive tour has several advantages from the point of view of a consumer is who is not experienced in travelling and using travel services. Firstly, there is the convenience of one-stop shopping. Also, some consumers take the view that the risks they face (of not getting the service they intended to purchase) can be minimised by buying their products from the one seller. Because of this the seller needs to take a long-term view of maintaining quality in order to survive, and there is a greater likelihood of commitment to quality control. Another benefit is that the tour operator will develop the optimal set of combinations with a significant advantage to an uninformed traveller.

Over time, a greater proportion of the market becomes experienced in travel. Also, it is true that the suppliers of travel services begin to learn how to serve their customers and to provide better guarantees of service. This is akin to the development of component standards in industrial systems (eg microcomputers and software). One example is the branding of international hotels in a way that communicates a message about quality to the market. One-stop shopping becomes less important, and customers develop a taste for assembling their own travel plans. In the process, the market shifts from its reliance on all-inclusive tours to more loosely defined packages of air travel plus accommodation and opportunities are opened up for new actors to sell and distribute travel services.

A formal analysis of unbundling over the product life cycle has been presented in the context of industrial products such as microcomputers (Wilson et al 1990). In this account, the firm faces the choice of maintaining a position as a systems vendor, strengthening its competitive position through an emphasis on integrated system benefits, or it can choose to unbundle complete systems, giving it the opportunity to withdraw from the market for one or more of the components. Bundling is risky if consumers are idiosyncratic or if one-stop shopping becomes less attractive. Both bundling and unbundling strategies have advantages and disadvantages and neither is universally dominant.

Unbundling becomes more likely over time because of the diffusion of technology among firms and as standards evolve. Their model assumes the multi-product firm sells a complete system in competition with suppliers of components that customers assemble. An important feature of the model is the specification of some attributes that describe the individual components and others that vary at the level of the overall system. The importance of these two types of attributes then varies across consumers.

The system-level attributes included "systems integration" and "modularity". The former was defined as the degree to which the customer perceives that the multi-component system has been optimised from a systems point of view through, for example, the incorporation of proprietary interfaces, or by designing the system to take account of the strengths and weaknesses in components. Systems integration can be enhanced if a single source is responsible for the product and if search and transaction costs are reduced with one-stop-shopping.

System modularity was defined as the *perceived degree to which a system conforms to open standards* and the level of this attribute depends on the scope of the available standards as well as the degree to which they are followed. Higher modularity is valued because it opens up possibilities for mixing-and-matching and it allows consumers to switch brands more readily. Systems integration and modularity need not always be correlated, but bundled systems tend to be regarded by consumers as having a high level of systems integration and a low level of modularity.

Though Wilson et al developed this model to explain trends in the supply of industrial products, it appears to apply well in the case of travel products. For example, a Club Med holiday or a cruise exemplify high system integration but their customers find it difficult to compare the component services with independent services that can be mixed and matched. One of the interesting conclusions to emerge out of this framework is that, as markets mature, the initiator finds it can unbundle its system and exit component markets for which its margin is relatively small or negative. Other things remaining equal, growth in sales is a motive for unbundling, but this is unlikely to arise from systems integration. More likely, the market can grow if there is another supplier producing a superior component. Unbundling can enhance modularity, and this can attract new customers who place high importance on their freedom to assemble, a conclusion that has obvious parallels in the evolution of mass travel markets associated with declining importance of all-inclusive tours and increasing reliance on more flexible deals based around an air fare.

These arguments provide some insights into the directions travel packaging is evolving. Table 1 summarises key observations about the outbound travel market in Japan based on a recent analysis (March 1993). Until 1964, Japanese citizens were not permitted to travel abroad for recreational purposes. The first business to offer international travel packages to the public was a foreign airline, Swissair, and it was not until the following year, 1965, that the first Japanese product was put into the marketplace. This was a copy of Swissair's 16-day tour. In the early stages of market development, growth was strong, but absolute numbers remained small. The Japanese travel sales and distribution industry remained focused on domestic group travel and inbound visitors.

The introduction of wide-bodied aircraft with their extra capacity and lower fares, together with an appreciating Yen, helped to promote the next period of growth between 1970 and 1973. To this stage, the prices of travel packages had remained high and continued to be dominated by large "affinity" groups. The success of the Tokyo Olympics and the Osaka Expo had a "demonstration" effect that generated confidence in international travel. With international travel becoming more affordable, another major growth segment appeared - young, single women. In the period between 1964 and 1974, outbound travel by Japanese citizens increased eleven times over. The continuing improvement in Japanese purchasing power helped to maintain the impetus for the growth phase in the market during the 1980's, but the increasing taste for leisure, helped along by deliberate government policy to expand international travel, saw a third period of strong growth emerge. In the period between 1986 and 1991, the number of Japanese citizens travelling abroad increased at the average annual rate of 25 percent with the absolute number exceeding 10 million in any one year.

Since the late 1980's, entrants into the travel sales and distribution industry have come from a variety of backgrounds including the manufacturing and retail sectors, and new distribution practices such as media sales marketing are appearing. Forty percent of Japanese travellers have undertaken at least one overseas trip previously, and the rising popularity of travel magazines is helping to improve consumer knowledge. This is significant because there is evidence that the popularity of packages with second-time travellers is considerably lower than it is for novices (Bureau of Tourism Research and Jacobs 1992). A reduction in the numbers of tours leaving Japan with an escort is occurring in parallel with a shift in preference for cheaper, second-brand products, and there is an increase in sales of packages confined to air transport and accommodation. Innovators are attempting to promote growth in the "silver", "family" and "student" market segments, whilst others are promoting fly-cruise packages.

This account sketches out the life cycle pattern described above, although there is no evidence yet of a decline phase. Looking to the future, a key question is whether the packaged travel product will play an active role in promoting further growth in Japanese visitors to Australia or whether unbundling will become a more successful strategy. Systems integration will remain a strong motivation for packaging whilst there are advantages in one-stop shopping and whilst travellers remain constrained by a tight time budget. At the same time, greater consumer experience and knowledge will generate a taste for mixing and matching. To the extent that systems integration will be sacrificed for modularity, it is possible that the Japanese travel industry will seek opportunities to exit from the supply of some components that do not have high margins. An even more important issue is whether a trend towards unbundling would help to expand the market. The experience with industrial goods is that this is more likely to occur if travel sellers link their services with superior, but independently supplied components.

Table 1: Growth Pattern of Japanese Packaged Travel Market

Period	Event	Comment
1964	Government deregulates outbound travel	Citizens permitted to travel abroad on recreation
1964	Swissair offers first package	16-day tour of Europe
1965	Japan Air Lines offers first Japanese package	Copy of Swissair's product
1968	Japan Travel Bureau offers first international package	Beginning of JTB's successful "Look" packages
1969	JTB and Nippon Express Company join to promote packages	Alliance between travel group and Japan's largest transport operator
1970-73	Tour wholesalers promote cheaper packages	New market segments appearing - young, single women
1986-90	Introduction of low-priced, second brand packages	Low barriers to entry in industry and increase in numbers of sellers, coupled with low consumer loyalty promotes vigorous price competition. Market exceeds 10 million per year
1990's	Continued shift to second brands, reduction in escorted tours, more packages confined to travel and accommodation, growth in charter market for incentive travel, cheaper air fares	Growth in competition with new distribution systems. Consumer experience and knowledge improving. Nature of market segments changing

Source: Adapted from March (1993).

CONCLUDING COMMENTS

This paper commenced with the observation that there have been few published attempts to evaluate packaging despite its importance as a marketing tool in expanding travel markets for more than a century. Packaging can be characterised as a form of bundling, a practice that has been assuming greater significance in competitive, service industries. The motives for using bundling are varied, but bundling is observed most in situations where the firm has a product line and, through joint sales, has scope for reducing costs of production, increasing overall yield, expanding its markets or controlling the performance of its products. All of these motives are strong in the travel industry.

The nature of bundling is best understood in a strategic marketing context that embraces a wide variety of pricing methods. Since packaging cum bundling is one pricing method that can be chosen from amongst a wide variety of alternatives, it is desirable that greater attention is focused on evaluation frameworks. Simple classifications of pricing strategies can help to indicate the circumstances where different strategies are more likely to be successful, but a satisfactory treatment of bundling has yet to emerge. Bundling is an option within the class of product line pricing problems, and the literature on this subject testifies to the difficulty in developing optimisation models. An alternative line of research is to develop a search procedure that leads towards an optimal bundling mix. Although an early contribution in this field dealt specifically with travel packaging, travel researchers have not pursued the opportunity to extend the analysis and, in so doing, make an important contribution to the theory on bundling strategies.

There is a need for further research on evaluation methods, but meanwhile it is necessary to rely on intuitive reasoning to suggest when different approaches to packaging are likely to be most appropriate. In any case, the evaluation of packaging/bundling requires a sound understanding of consumer responses to bundles. One view is that consumers form independent valuations of the individual components and then simply sum these to arrive at an overall bundle valuation. Even in this case, bundling can be used to expand the market and to increase the firm's revenue. An alternative view is that consumers integrate information about bundle components in a non-additive way, and one version of this argument is that benefits are added but prices are not. That is, an all-inclusive price has less negative impact on a consumer than a set of individual prices. There is a developing literature on this matter and researchers interested in travel packaging can make contributions to management theory through rigorous studies of traveller behaviour. However, past experience is that travel researchers, in the main, have paid little attention to the role of packages on demand.

Finally, there is an argument that the travel package, or at least the fully-inclusive tour, is at an advanced stage in its product life cycle and that its role in promoting further growth in travel will diminish. Bundling arguments developed in the industrial goods area suggest that unbundling can be a feature of industry maturation, but it is by no means clear that unbundling is always the best policy. The desire of at least some consumers for a high degree of systems integration for short holidays and the convenience of one-stop shopping will ensure that a demand will be sustained for fully-inclusive tours. In yet other cases, independent suppliers of components of travel packages have an opportunity to forge alliances with tour wholesalers when their components can help expand the market or when the tour operator can stop providing services that it finds relatively unprofitable. In general, the outlook is that travel packages will change in variety and bundling of travel with non-travel products is likely to increase.

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