Innovation and Growth in Tourism

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Innovation and Growth in Tourism

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FOREWORD

A number of OECD countries face growth problems in tourism. Globalisation implies that, to remain competitive, OECD countries should be at the cutting edge of the development of new products and ideas in tourism. With innovation, this report touches therefore an important dimension of the tourism economics rarely examined at international level. *Innovation and Growth in Tourism* aims to provide an important contribution for research and policy work in this area.

Innovation and Growth in Tourism clarifies the conceptual issues behind the dynamics and the characteristics of innovation in tourism and how innovation is transforming the tourism business models. For example, one of the new basic innovations which transform tourism is the trend towards an "experience economy".

Innovation and Growth in Tourism shows that innovation processes in tourism are mainly aimed at increasing productivity, profitability and quality, thus improving the overall competitiveness of the tourism economy. Innovation is to be considered as a major driving force for structural changes in the tourism industry. It shows, for example, that the small and medium sized enterprises (SMEs) are mainly introducing innovation by imitation.

Competition is the main driver of innovation in the tourism sector but co-operation is essential to stimulate structural change and innovation in tourism. This is certainly a main rationale for governments to intervene in the fragmented tourism sector, as new structures and innovation can only emerge if there is cooperation. *Innovation and Growth in Tourism* illustrates the need to push the diffusion of best practices in tourism innovation (e.g. in the areas of environment, education, ICT), notably in micro and small tourism enterprises and the important role to be played by public authorities.

"*Innovation and Growth in Tourism*" was the theme of an OECD conference held in Lugano, Switzerland on 18-19 of September 2003, in cooperation with the Swiss State Secretariat for Economic Affairs.

Sergio Arzeni
Director, OECD Centre for Entrepreneurship,
SMEs and Local Development (CFE)

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CHAPTER 1. CAN THE STATE PROMOTE INNOVATION IN TOURISM? SHOULD IT?

This text has been drafted by Ambassador Dr. Eric Scheidegger, Member of the Board, State Secretariat for Economic Affairs, Switzerland.

Abstract

A number of developed economies face growth problems in tourism. The tourism industry also suffers from below-average labour productivity. There is a lack of innovation in tourism. This text questions the existence of mechanisms, such as innovation processes, that can be put in place to help governments to support quality improvements and increased profitability and to overcome this weakness in growth. Can the State promote innovation in tourism? Should it?

Growth problems in the industrialised countries

Tourism is seen as one of the most promising areas of growth for the world economy. The World Tourism Organization expects international arrivals to increase by a respectable 4% in the next 20 years, *i.e.* about the same rate of growth as in the recent past. Since 1990 international arrivals have enjoyed an annual growth rate of about 4.3%.

If we take a closer look however we will see that the rate of growth over the past decade has varied considerably from one region of the world to another.

The Asia and Pacific region enjoyed the highest annual rate of growth with an average of 7.2%. Within this region three areas benefited from double-digit growth, namely Hong Kong, China (21%), China (11%) and Japan (10%). The growth in arrivals in North America was limited to 2.4%, with the United States as the world's leading destination showing signs of stagnation (-0.1%). The average growth rate for Western Europe was similar at 2.2%. In Switzerland there has been virtually no growth in international tourism for a decade.

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While in developing countries tourism is frequently a motor for rapid growth, a number of tourism countries of the West face growth problems. This raises questions that are not easy to answer: Is this the result inevitable in countries that have been transformed into modern high-tech service economies? Are there mechanisms that can be put in place to help us to overcome this weakness in growth?

Innovation as the motor of growth

The United States is often described as the locomotive of growth for the economy of the entire world. The Geneva-based International Labour Organisation published a report[1] which puts the output per employed person in the United States at a remarkable USD 60 000. Europe's biggest economies achieve an output of between USD 40 000 and 45 000 per employed person. Their productivity is thus lower. The performance of the US economy is impressive. The fact that workers put in longer hours on the other side of the Atlantic does not detract from this achievement.

On-the-job discipline alone does not lead to growth and prosperity. It takes modern installations and machinery, as well as investment, to make labour efficient and increase productivity. The most developed countries scarcely suffer from any lack of effective capital. There is no indication that the dynamic growth found in the USA and a few other economies is above all due to more hard work or a greater input of capital.

Since the pioneering work of the Nobel Prize winning economist Robert Solow, if not before, we have known that an increase in investment does not always lead to an increase in output per hour and hence to economic growth. It is technological progress or innovation, which stimulates the wealth of nations. Solow demonstrated that at most only a fifth of productivity growth is attributable to capital input. The real source of growth, as identified by Solow, is technological progress[2]. The Nobel Prize winning economist did not however take his analysis of the innovation process in the economy any further. He seems to have regarded it as a sort of black box. The first to take a look "Inside the Black Box," is Professor Rosenberg[3].

1. See Key Indicators of the Labour Market (KILM).

2. SOLOW Robert (1970) *Growth Theory: an Exposition*, New York: Oxford University Press, p. 109.

3. See Innovation and economic growth, p. 38.

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Tourism's productivity dilemma

The tourism industry is one of the least productive sectors in the economies of the most developed countries. We may take Switzerland as a typical example. The productivity of labour in tourism is USD 50 000 per employed person. Swiss banks achieve productivity of USD 250 000, the chemical industry USD 120 000 and the machine manufacturing industry USD 67 000. The proportions are similar for comparable sectors in most other industrialised nations.

Such differences in productivity must be interpreted with caution however. The branch of the Swiss economy with the greatest productivity is the electricity and water supply industry for example, with USD 280 000 per employed person. Here however, as with banks indeed, the input of capital per employed person is exceedingly high. Moreover no direct link can be found between these differences in labour productivity and such factors as the growth dynamic or the competitiveness of a given sector.

Indeed it is not the current rate of productivity or the level of prosperity that determines the future of an economy. An economy will above all be successful when its rate of innovation is high.

Branches that suffer from below-average labour productivity tend to face procurement problems in the factor markets. This is particularly true of tourism, which due to low productivity increasingly finds it hard to attract the necessary capital, and more difficult still to attract highly qualified staff. There are of course good reasons for this weakness in productivity, beginning with the fact that tourism is a labour-intensive industry. But that does not help us to solve the problem. We need to identify, and then to adopt, whatever measures are necessary to increase the productivity of this industry.

Inventions and patents do not in themselves produce growth

Tourism itself is not a field in which we can point to innovations that have changed the course of history. The invention of alpine tourism by adventurous English gentlemen in the 19th century did, it is true, begin a gradual process of development which over many decades transformed the impoverished villages of our mountains into the prosperous "jet set" destinations of today, such as Zermatt and St. Moritz. As inventions go however this development is not on quite the same level as the steam engine, the jet engine, the microprocessor or the laser.

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It is understandable therefore that private and public funds are first and foremost attracted to high-performance industries. Switzerland has invested above all in such fields as information and communication technology, biotechnology, life sciences and nanotechnology. For it is in these fields that the greatest productivity gains are to be expected. Switzerland indeed has the greatest number of patents per capita in the world. I would have preferred to be able to say at this point that we enjoy the highest rate of growth!

Major breakthroughs in technology are a rare occurrence. But they do not automatically lead to economic growth. When a group of researchers at the Geneva-based European Organisation for Nuclear Research (CERN) developed the forerunner of today's Internet in 1972, the world at large remained ignorant of this epoch-making event for years to come. The economic boom triggered by the dot-com start-ups was still 35 years away, although it was doomed to be short-lived. This new branch of the economy does however seem to be on the way to recovery, and heading in the direction of sustainable growth.

Even a fundamental innovation is not sufficient to ensure the sustainable growth of an economy. It is not so much the one "big leap" as the countless small steps following it that eventually lead to real growth. It is in this second stage of development that many new goods and services, that have no need of a patent, can be successfully launched on the market.

Breakthroughs in major scientific disciplines have without doubt done much to increase the general prosperity of the Western world. But it is not these advances in knowledge which in themselves bring growth. Innovation research has shown that economic growth depends not only on the creation of new knowledge in the form of innovations, but on their dissemination and application. Such fundamental innovations only bring significant growth when they begin to spread from one sector of the economy to another.

A key innovation like the internet has done more than stimulate growth in the field of information technology (IT). Sustainable economic growth is only possible when inter-industry multipliers come into play. In this view, the key innovation of the internet can only be transformed into economic success when other industries start to use and improve the new technology. In this inter-industry innovation process tourism can play a key role in translating high-tech innovations into economic growth. Tourism is already one of the most important sectors of e-business today.

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A lack of process innovation in tourism

Technological improvements in the transport sector have more than once set in motion a rapid and irreversible process of change in the field of tourism. The construction of the first railways in the 19th century made it possible to travel long distances comfortably and at great speed for the first time in history. Mass production of the automobile brought about a further quantum leap in general mobility. The spread of the automobile was the *sine qua non* for the development of individual tourism among the masses. In the middle of the 20th century the jet airplane added a new dimension to travel, bringing the world closer to the state of a "global village".

Today the countries that pioneered tourism are facing the consequences of this continuous rapid development. Europe's leading position as prime mover in the field of tourism is threatened as distances continue to shrink. It is as if our protective patent had run out. A downward price spiral has been set in motion. The European tourist of today can choose between two weeks of skiing in the Alps or snorkelling in the turquoise waters of Bali -- all for the same price, and with comparable quality.

Even when the attraction of locations like the Matterhorn or Lake Lugano continue to provide competitive advantages, acting as barriers to market penetration, the traditional tourism countries would be foolish not to adapt as quickly as possible to the changing market conditions. In Switzerland we must learn to accept with good grace the fact that other countries have "Matterhorns" of their own.

In this new situation process innovations become essential for survival. Above all this means concentrating our efforts on bringing down costs. This should be the preamble to quality improvements, increased profitability and lower prices. Process innovations are indeed possible in a number of areas. Full use must be made of economies of scale in purchasing and marketing. The hotel trade needs to specialise to an even greater degree. Quality management must be extended beyond the individual level to cover the entire chain of services, from the time a guest arrives to the time of departure.

Can the State promote innovation? Should it?

The purpose of our meeting is to discuss the innovation process as applied to tourism, and to chart the paths that can lead us back to growth. Such a debate is long overdue in tourism. Switzerland is a paradigmatic example of a traditional, highly developed tourism country that is suffering from lack of growth. Many observers

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have reassured us of course that Switzerland has lost none of its tourism potential. But you cannot live on potential. We need to become proactive, to develop new products and processes that will safeguard the future of Switzerland as a leading tourism country in the new millennium.

Many economists are sceptical when it comes to the promotion of innovation by the State. We must not be so naive as to think that the State is able to restore the faltering motor of innovation to its highest performance level. The Swiss government nevertheless supports innovative industry-wide tourism projects which are put forward by initiatives which are submitted by more than one operator. Its programme "Promotion innovation and cooperation in tourism" can be considered as a successful instrument to adapt Switzerland's tourism offer to the new requirement of the world market.

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CHAPTER 2. INNOVATION AND TOURISM POLICY

This text has been drafted by Prof. Peter Keller, Chairman of the OECD Tourism Committee.

Abstract

This text provides a synthesis of the key policy questions which relate to innovation and tourism. After a review of the competition and structural changes in the tourism sector of OECD countries, the paper summarises the main characteristics of the innovation process in tourism; and explains the peculiarities of tourism that affect innovation such as the small size of tourism businesses or the importance of destination goods. Finally, it sets an agenda for an innovation-oriented tourism policy and justifies why the State should promote innovation for tourism services.

The magic role of innovation

International tourism has undergone a fundamental change. New destinations are successfully competing against the traditional tourism countries, which in many cases have exhausted existing resources and the potential for rationalization. Additional inputs of capital and labour are costly in such circumstances and do not always lead to the desired level of growth. Tourism policy therefore increasingly focuses on the promotion of innovation. The aim is to achieve a new burst of growth at the lowest possible cost in terms of incentives. Innovations are expected to add consumer surpluses and to increase profits for the suppliers of tourism products and services.

There is indeed something magical about innovations. They are the essential motor of growth in market economies. The ability to innovate is crucial not only to the survival of individual companies, but to the entire economy of a modern nation. Nonetheless, innovations can only perform the function of providing economic growth in the presence of favourable State incentive systems. It is not the State however that creates innovations. Rather they are the result of processes which, having been subjected to extensive analysis are today well known and have become quite routine. This is as true of innovations in the field of tourism as in any other sector.

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The tourism industry does of course have a number of specific characteristics which can influence the innovation process in ways that are both positive and negative. Tourism is best defined on the demand side. It has heterogeneous and ephemeral industrial structures. Tourism is important to many sectors of the economy. And it has an inherent geographical dimension. It is an industry in which the State plays a major role as co-producer.

Innovation can thrive in tourism, but only in conditions of the greatest possible competition that make the renewal of existing structures possible. These structures need to be either developed further or entirely replaced. New structures are needed, of a kind that will increase productivity and growth. Governments must not attempt to devise counter-productive laws and regulations to hinder the inevitable process of restructuring.

With these considerations in mind we need to address the following questions in greater depth:

- What fundamental changes have occurred in international tourism? Why are innovations an absolute necessity in the most mature tourism economies?

- How does innovation promote growth? What is the true scope of innovation in the national economy?

- How does innovation function in tourism? How does the very special nature of the tourism industry influence the process of innovation?

- What are the most important aspects of an innovation-oriented tourism policy? What is the most important determinant for the content of such policy?

- What market order objectives justify an innovation-oriented tourism policy?

Competition and structural change in the developed tourism countries

The shock of globalization

The relentless process of globalization, together with liberalization and the extension of the international tourism market led to unexpected losses of market

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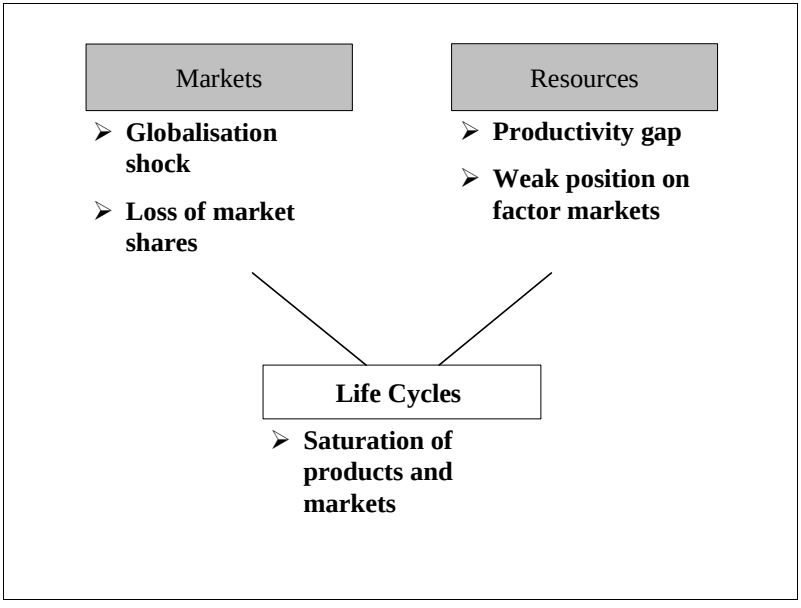
share for the developed tourism countries. The emerging destinations are often able to count on resources that are relatively unknown and thus uniquely attractive. They are in a position to introduce new products and services capable of competing on the international market. In doing so they can take advantage of what has been called the "advantages of backwardness". Thanks to a lower level of development the new tourism countries have benefited from temporary competitive advantages in the form of lower wage costs and favourable exchange rates (Figure 2.1).

Figure 2.1. Productivity and growth problems of SMEs in highly developed tourism countries



Source: P. Keller.

Despite the advantages that traditional tourism countries obtain from a high level of development, many years of specialization in tourism and a great deal of competitive experience, their ability to compete on price suffers greatly from high wages and exchange rates. The economic framework conditions in the industrialized countries slow the speed of growth and put pressure on the rate of growth.

Cost disease of personalized services

Moreover the increasing automation of the industry and rationalization in the field of the progressive services in various economic sectors in all of the more

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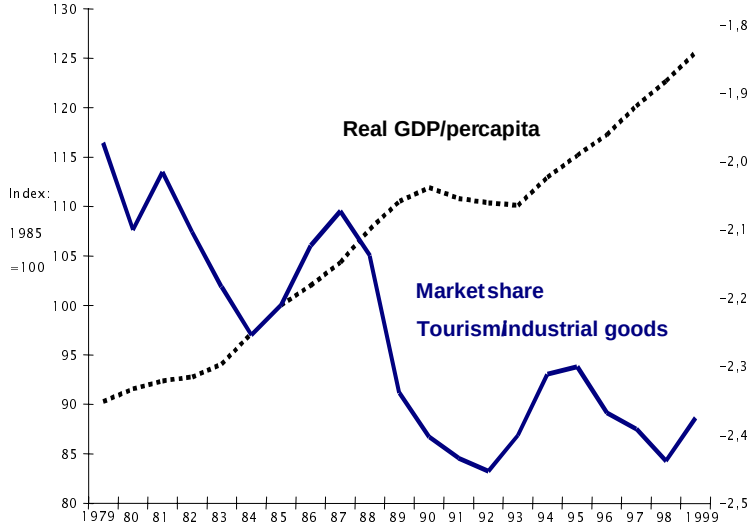
developed countries enables these sectors to grow significantly faster than tourism, which tends to be less productive. It is for this reason that the share of the gross domestic product (GDP) that goes to tourism-dependent sectors, compared to industry and branches with progressive services, is shrinking in all OECD countries (Figure 2.2).

Small-to-medium-sized enterprises (SMEs) in labour-intensive branches of tourism suffer from the cost disease. They have below average productivity and are under pressure in domestic factor markets. They have no choice but to resort to price increases to compensate for their relative lack of productivity. This further weakens their international competitiveness.

Figure 2.2. Shrinking market share of tourism in highly developed countries



Source: WIFO, OECD

Innovations are therefore needed to make tourism products and services more attractive, as are new ways to rationalize in an effort to win back at least part of the room for manoeuvre in setting prices.

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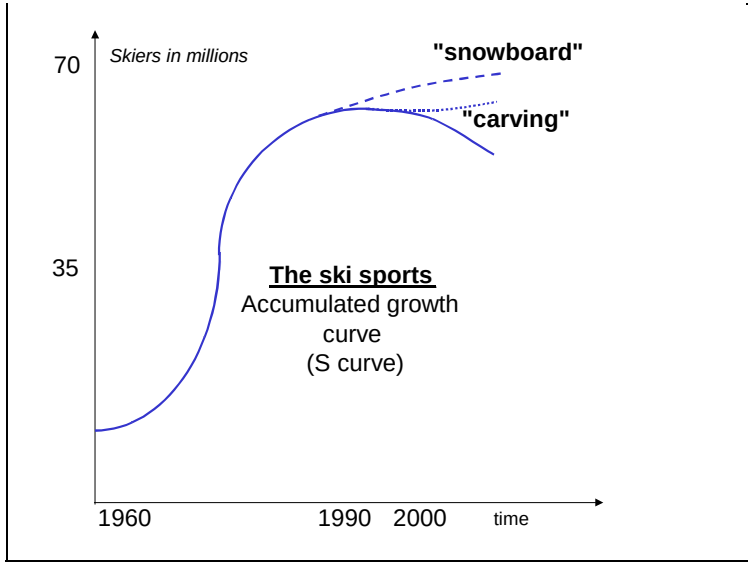
Saturation of products

Innovations obey the law of natural growth. They therefore have a life cycle that always takes the form of a bell curve. The innovation cycle begins with a product's launch in the market, followed by a rapid growth phase and a sharp increase in turnover, before reaching the peak value in the product's phase of maturity.

As can be seen from the example of downhill skiing, the innovation cycles of tourism products can come full circle. This tourism-linked sport enjoyed a boom in the 1960s and 1970s. As a result of new demand trends and above all the loss of its monopoly position as a winter sport, the number of adepts of downhill skiing has been in decline, even though suppliers have introduced new equipment such as snowboards which are accessible to a wider audience and have created a new market niche (Figure 2.3).

Figure 2.3. Innovation cycles of destinations: end of cycle and lack of opportunities for repositioning in the markets



Source: P. Keller.

Destinations are also subject to innovation cycles, as can be seen from the example of the Alpine region. Despite being Europe's second largest recreation area the Alps have lost much of their market share in the past 10 years. They have gone "out of fashion". The mistake was to forget that what makes a destination is not the

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regional planning authority, nor even the brains of the destination manager. It is the market that decides whether or not a destination is worth a visit. Tourists choose destinations that they find attractive and which offer the greatest utility.

Innovation as a growth machine in market economies

The market economy and free trade

It is possible to describe the conditions which must be fulfilled before innovations can become the engine of economic growth. Innovations flourish only when the economic framework conditions are favourable, encouraging competition and thus the creative destruction or renovation of existing structures. Only free and open market economies meet these conditions. Innovations develop best in deregulated and liberalized environments.

The freest possible market economies are built on competition - in conditions which protect individual property rights from unwarranted State interference and excessive taxation. Such conditions help to create open borders and thus free trade. Capitalists are free at any time to seek the most profitable business opportunities. Innovation also means looking actively for the most lucrative alternatives. It unleashes new growth potential. The most innovative economies enjoy the steadiest rates of growth (Keller, 2006).

Empirical evidence of the economic importance of innovation is best found in the United States. Here, in a deregulated internal market of continental proportions, the potential for reaping huge rewards is great. It is hardly surprising therefore that an important part of the main innovations of modern tourism were “made in the USA” (Keller, Bieger, 2005). Notable examples are the introduction of the hub-and-spokes system and the low cost carrier in civil aviation, international hotel chains, standardized gastronomy, the rent-a-car business, leisure parks and finally the credit card, which has done so much to eliminate exchange rate problems.

Oligopolistic competition as a driver of innovation

Favourable State framework conditions are not the only way to promote innovation. Competition structures, which are the result of the economic development process, exert a major influence. Neither perfect competition nor monopolistic competition are innovation-friendly. There is no reason for a monopolist to innovate. Innovation is driven by the oligopolistic competition that leads to standardization, industrialization and concentration. Tourism is an industry

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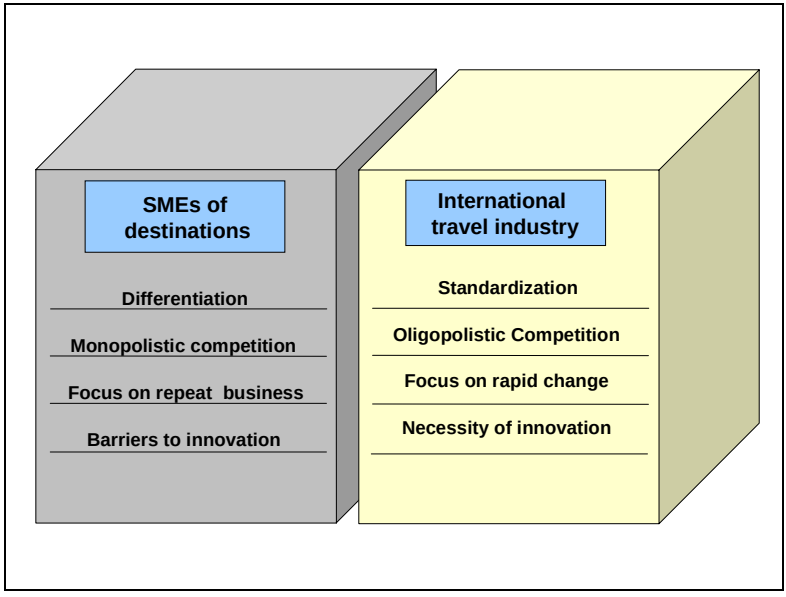
with a dual structure, in which competition can be either monopolistic or oligopolistic (Figure 2.4).

The uniqueness of destinations in tourism, as a location-specific sector of the economy, leads to monopolistic competition. Tourism can take advantage of this uniqueness in the form of a brand rent and a correspondingly greater willingness to pay on the part of the visitor. This leads to differentiation and quality based strategies.

Figure 2.4. Oligopolistic competition as a driver of innovation



Source: P. Keller.

Uniqueness and high quality enable tourism-related industries to compensate for the cost and price disadvantages that go with the high number of small businesses in this sector. Providers of services must try as far as possible to attract and above all to keep repeat customers. Customers who remain loyal are usually those reluctant to change their habits. They do not contribute to innovation-oriented behaviour on the part of the entrepreneurs who manage the tourism-related SMEs in destinations.

The opening of intercontinental and exotic markets resulted in the emergence in the countries that were the main source of tourists of an international travel industry,

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dominated by big corporations. Airlines, hotel chains and rent-a-car companies are able to control the flow of visitors thanks to standardized products. These corporations are in a situation of oligopolistic competition. They must constantly innovate to ensure that their products always offer quality at an affordable price, enabling them to compete against all-comers. Competition in the international travel industry is thus to a great extent innovation-based.

Innovation characteristics that produce growth

It is not the level of development an economy has already achieved that determines its future success. Economic growth depends far more on a country's willingness and ability to constantly call itself into question and adapt to changed circumstances.

In this context innovations not only lead to the creative destruction of existing structures. They further develop and complete the offer that already exists in a given economy. They thus have an effect which is cumulative (Baumol, 2002).

A steady flow of innovations thanks to constant investments in research and development produces disproportionately high growth in the gross domestic product (GDP). Innovations thus have the power to speed up the rate of growth. Innovations also have the nature of public goods, since thanks to a process of dissemination via imitation they tend to benefit the entire economy rather than just individual companies.

Essential characteristics of the innovation process

Basic innovations are not subject to planning

Fundamental or basic innovations are not subject to planning. They result from new discoveries which often never reach the market in the form of goods or services, or do so only after a very long time. The consequences of basic innovations, which according to Schumpeter stimulate Kondratieff cycles and lead to longer lasting periods of economic prosperity, are impossible to predict (Nefiodow, 1990).

Fundamental innovations in the means of transport have had a revolutionary impact on tourism in ways that no one could have foretold. Trains, planes and the automobile shortened distances, reducing travel time and costs (Keller, 2005). These innovations led to the creation of large tourism centres, significant spatial growth, and the opening up of remote markets (Figure 2.5).

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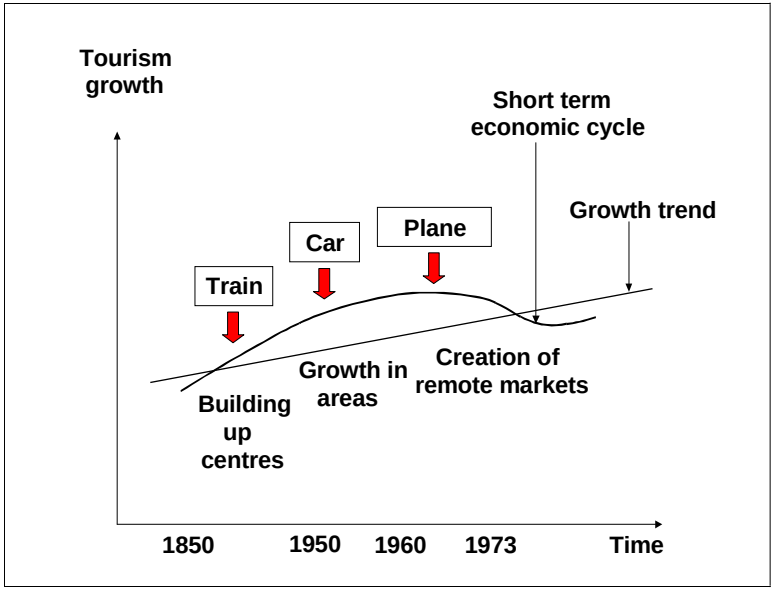
No one would have ever imagined that man's long cherished dream of learning to fly would eventually give birth to the modern industry of civil aviation which is a core tourism related industry. And indeed it is amazing when you think about it that the flimsy machine the Wright brothers made from bits of wood, fabric and wire, and which remained in the air only long enough to cover a distance equal to two football fields, signalled the beginning of civil aviation - and the end of the monopoly of winter tourism by the alpine countries.

Figure 2.5. Basic innovations in transport: major impact on tourism development



Source: P. Keller.

The State supports the basic research that leads to fundamental innovations. The particle physics scientists of the CERN research centre in Geneva, which is funded by various countries, invented the internet in 1974. However it took about two decades for this innovation to become accessible to the world, rolling out the revolutionary "information highway". This technology has engineered radical changes in the production and marketing of tourism (Rosenberg, 1982).

Lasting influence of independent innovators

Innovations are by definition unique. A thing can be introduced only once as an innovation, not twice. Innovations are based on ideas, which often lead to the market launch of new and revolutionary products. Why it is that such ideas and their

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possible applications occur only to a gifted few, who live in the same world as the rest of us, is difficult to explain.

In market economies fundamental innovations frequently occur with the arrival of new enterprises on the market. They are mainly the work of independent innovators, who stand head and shoulders above "mainstream" managers, the latter increasingly consisting of academics, technocrats and bureaucrats.

These pioneers are entrepreneurs who are quick to spot new social trends, to develop new products, processes and ways of organizing, and to find new markets. Today's tourism structures are above all the work of such entrepreneurs, who have put new business ideas into practice at great personal risk.

It was entrepreneurs of this stamp who a century and a half ago built the first Palace Hotels and mountain railways. They dramatized the holiday experiences of the "leisure class" of that fin de siècle period -- in the same way as Walt Disney was to do many years later with his theme and leisure parks.

There are still pioneers today. Family firms like Hilton and Marriott created the first hotel chains, offering standardized and industrialized products to meet the special requirements of business travellers. The concept of the "low cost carrier", first developed by Southwest Airlines and today able to compete successfully with the network carriers, is another modern success story.

Innovation as a matter of routine

The "spirit of enterprise" is an important resource for the process of innovation. As the various branches of the tourism industry reach maturity pioneering companies become a rarity. Business opportunities are sought in new sectors and markets. Entrepreneurship as a resource decreases.

In such circumstances fundamental innovations are not to be expected. Innovations become a matter of small steps, part of a process of "feedback". One innovation leads to another, producing slightly improved products and more efficient processes (Figure 2.6).

The innovation process thus becomes just another component of the investment process. Most branches of the economy launch new products which add to customer utility each year. It is taken for granted that auto manufacturers in particular must come out with new and improved models virtually on an annual basis. Tourism products and services do not benefit from a similar culture of innovation.

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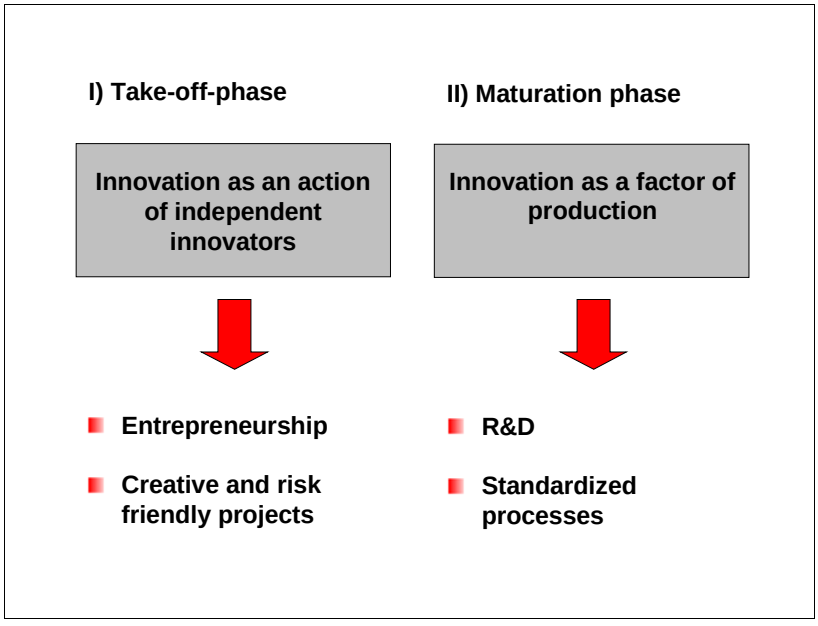
The bigger corporations include funds for research and development in their annual budgets and create divisions to make innovation a matter of routine. They protect these innovations with patents and recoup the cost of the innovation process through monopoly rents.

Figure 2.6. Creative risk-taking and standardized processes



Source: P. Keller.

Peculiarities of tourism that affect innovation

A mix of "high tech" and "high touch"

Tourism was one of the first sectors of the economy to adopt information and communication technologies (ITC). Airline companies took advantage of telematics for their information and reservation systems. They then launched the so-called "Global Distribution Systems", which today allow travel agents acting as the local distribution channel to access the most favourable connections and prices in a matter of seconds, for immediate booking. Network carriers still make use of these neutral systems, despite the high cost of both the technology and the distribution system.

Internet technology opened up new distribution and management opportunities for tourism. It is possible to introduce telematic information and reservation systems

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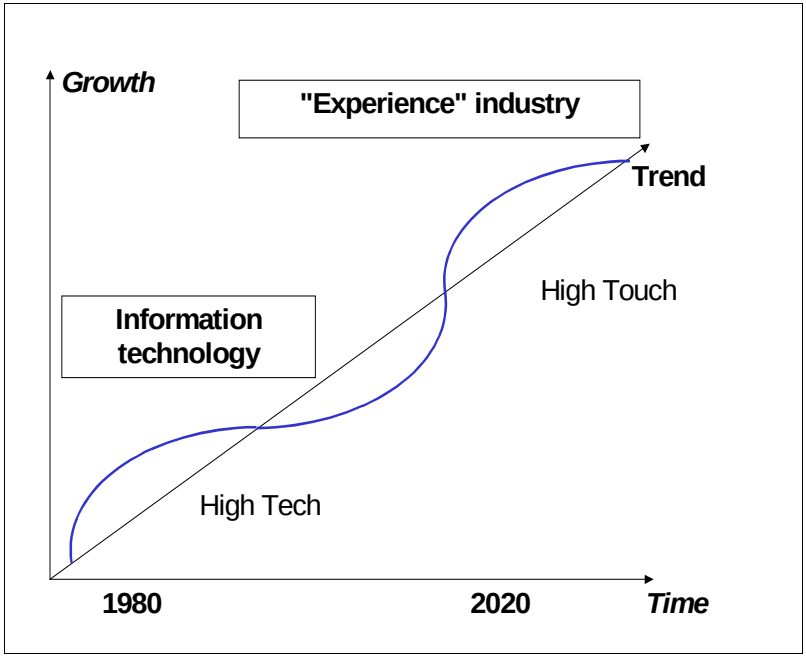
at the destination level, which as well as for multimedia advertising make it possible to book multioptional products and services. Tourism has become one of the foremost branches of "e-commerce". The utilization of ITC for the management of tourism networks and the rationalization of operational processes is as yet in an early stage. There can be little doubt that ITC will be increasingly important as a tourism production factor. Tourism is no longer in the small family business league. Backstage it is increasingly a "high tech" field of activity.

Doubts are frequently raised about the very existence of innovation "front stage" in the area of tourism services which have an element of intangibility. A guest's perception of the quality of the services and buildings in a tourism resort is emotional and subjective. A good welcome and a hospitable atmosphere are important elements of service production in a tourism environment. In this field there is often a little difference between learning processes in the firm and applied innovations (Sundbo, 1997).

Figure 2.7. Tourism a new 4th sector between "high tech" and "high touch"



Source: P. Keller.

Nevertheless, in recent years tourism has often been viewed as a sort of factory turning out dreams. Today's providers of tourism services imagine and dramatize

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their guests' experiences well in advance. They have become "managers of emotion" who do their best to make sure that the architecture and design of buildings provide the lifestyle that potential guests dream about. They create special atmospheres which are known by the term "high touch" (Figure 2.7).

This process of imagineering and putting on stage tourism services or bundles of services can be considered as an important innovation at the level of the welcome provided to visitors, going beyond mere comfort and the quality of service. Tourism is today part of the new fourth sector. It is an "experience industry", creating new value for customers. It is rapidly becoming a "high tech" sector.

The dissemination of innovation in tourism

Tourism enterprises cannot count on the input of special research departments, as they can in the processing industries. Generally speaking, the innovation process has not been made a matter of routine in tourism. In tourism innovative, successful competitors at the product level will soon find themselves being imitated. At the process level innovations tend to be outsourced. Imitation and outsourcing are the most important means of disseminating innovation in the field of tourism (Figure 2.8).

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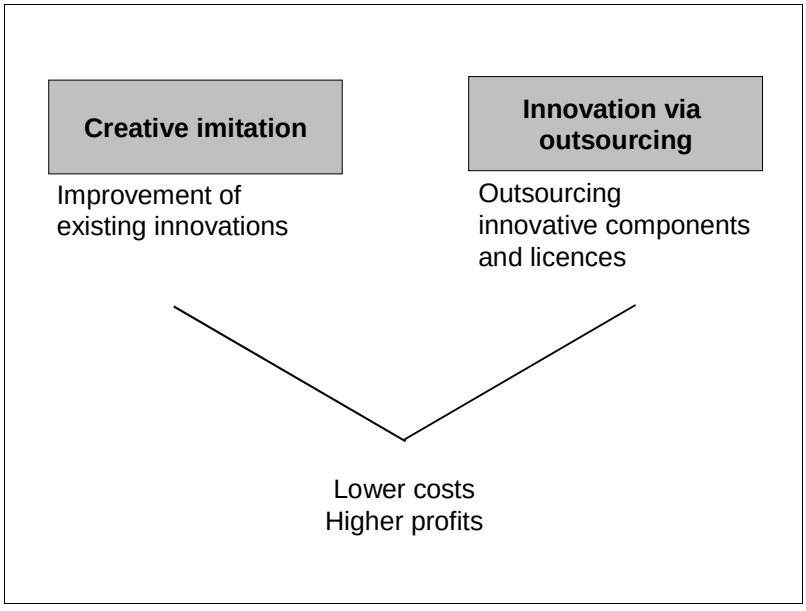
Figure 2.8. Creative imitation and innovation by way of outsourcing



Source: P. Keller.

Imitation can pay dividends. It is possible to borrow innovative components from the products and processes of competitors and to further improve upon them. This is known as "creative imitation". The advantage of this process is that the greatest part of the development and implementation costs are borne by independent innovators or particularly innovative destinations. Innovative applications in tourism thus go hand in hand with a "free rider" problem.

In most cases the outsourcing of innovations is handled by firms of consultants or academic experts who specialize in applications for tourism-related sectors of the economy. Their dissemination is therefore unlikely to be systematic. The trigger is likely to be operational or financial difficulties at the corporate level. In the case of destinations the innovations usually involve cooperation between various service providers.

Spatial limitation of product innovation

Tourism depends to a great extent on the natural or manmade attractions around which destinations are formed. These attractions are destination goods, such as unique mountain landscapes or monuments, chalets with window boxes full of flowers, the open-air facilities used by restaurateurs (Figure 2.9).

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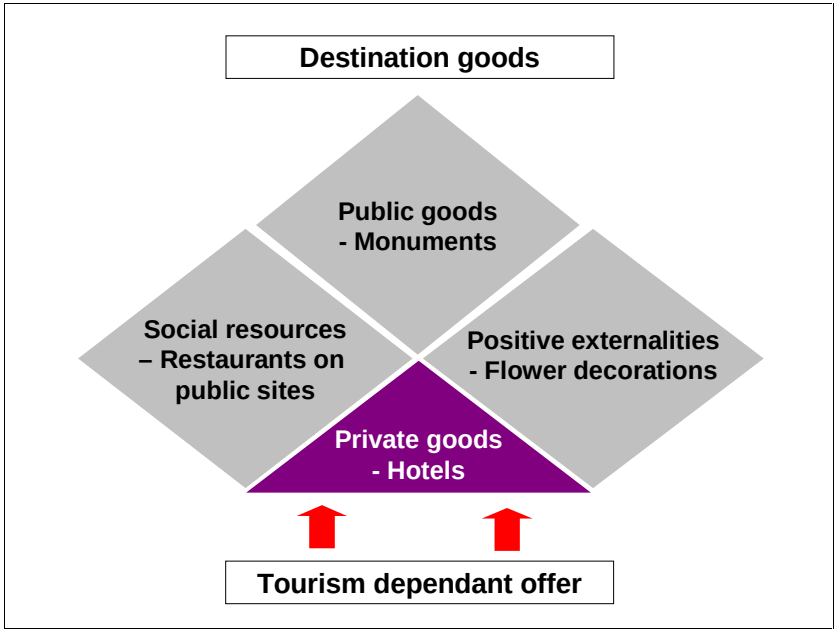
This dependence on attractions limits the potential for product innovation in destinations. Geographical specificity is intrinsic to the product and cannot be "reinvented" just anywhere. Downhill skiing requires suitable sites in high mountains. Local destinations cannot simply reposition themselves in the market at will. A seaside resort cannot transform itself into a city of art.

Major changes at the level of natural and cultural attractions can have a significant influence on the spatial development of tourism. Idyllic rural areas can be overwhelmed by creeping urbanization. With the retreat of agriculture, landscapes that are an important tourism resource are transformed into a kind of wilderness. This is a situation that cries out for innovative adaptation. Looking ahead, the trend towards climate change may lead to an ever more pressing need for product adaptations on a worldwide basis.

Figure 2.9. Importance of destination goods



Source: K. Koch.

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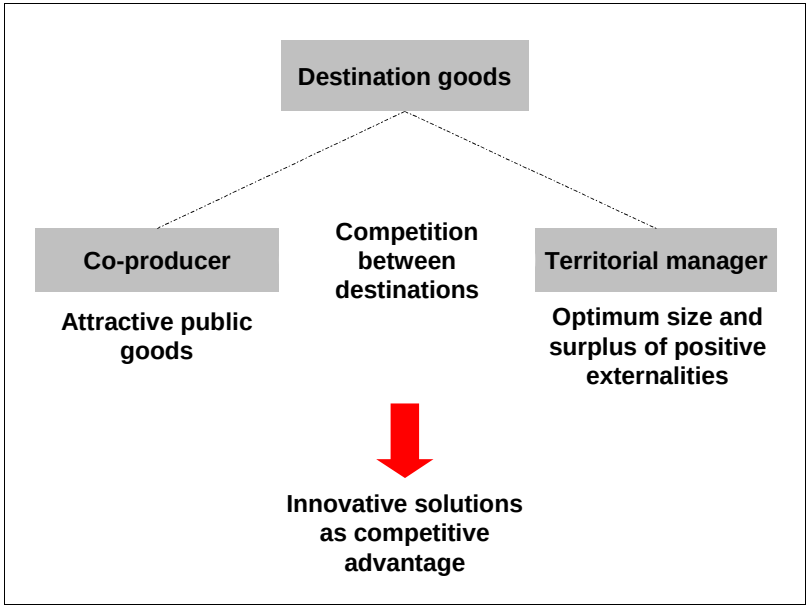
The State as co-producer

The State has a role to play as a tourism co-producer, making available most of the attractions, protecting and caring for them and increasingly helping to market them.

Competition in tourism is not confined to service providers. The most decisive competitive struggle is that which takes place between destinations, and it is at this level that destinations require considerable State support (Figure 2.10).

Innovation at the level of State controlled destination goods, such as beautiful landscapes or key infrastructure, can make it easier for destinations to compete more successfully in the field of tourism.

Figure 2.10. The State as a co-producer



Source: P. Keller.

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Agenda-setting for an innovation-oriented tourism policy

Market, resource and location based views

The purpose of an innovation-oriented tourism policy is to improve productivity and stimulate growth. Above all it must take into consideration the creative power of the market. Tourism can only be defined in terms of demand, which is to a great extent influenced by socio-economic change. Ever since the industrial revolution social innovations such as paid holidays and the emergence of a leisure and experience society have influenced the development of tourism markets, products and structures (Figure 2.11).

An innovation-oriented tourism policy needs to concern itself with the resources that stimulate the process of innovation. These include what are known as "innovation creation mechanisms". These mechanisms promote a spirit of enterprise and the development of new business models, attracting additional investment for the renewal of equipment and installations.

Finally one must not forget that the tourism innovation process takes place in a given location. There are a number of exogenous and endogenous factors which influence this process.

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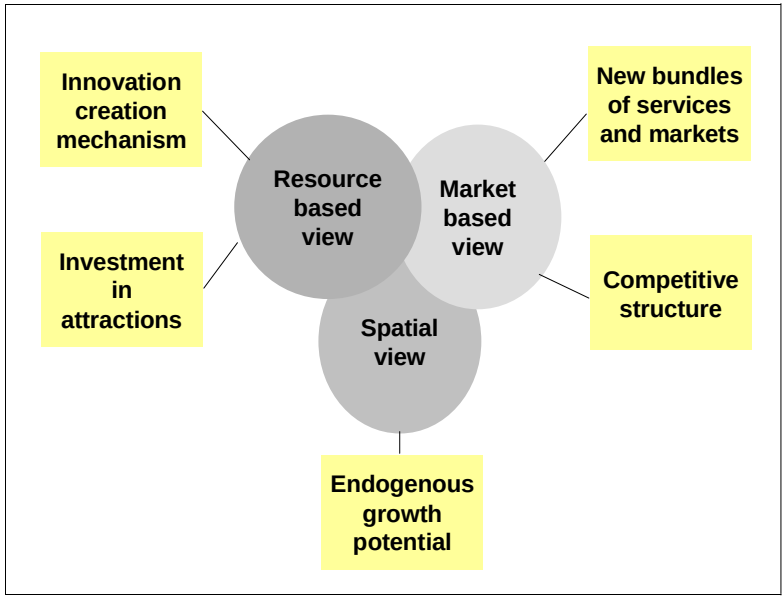
Figure 2.11. Model for an innovation-oriented tourism policy



Source: P. Keller.

Role of innovation creation mechanisms

The level of development already reached by a country plays a less important role than the so-called innovation creation mechanisms. These help to eliminate the barriers to innovation and to make innovation processes a matter of routine. This is a useful way of improving tourism's poor labour productivity (Figure 2.12).

Creative entrepreneurs, well trained managers and specialists, sector specific knowledge and the support of research and development -- all of these can help to create the framework conditions needed to improve existing structures and take full advantage of the endogenous growth potential of destinations.

Education creates personalized knowledge in the form of human capital. This is effective mainly in the long term, and like personal commitment and hard work is only a variable, albeit one which improves the productivity of labour. Today's trend towards formal education and a more academic approach to tourism specialization is of dubious benefit. "Learning on the job" and "hands-on training" are important in a sector like tourism where there is a constant need to recruit new staff. Also important is the learner's nearness to the market. At the level of the destination,

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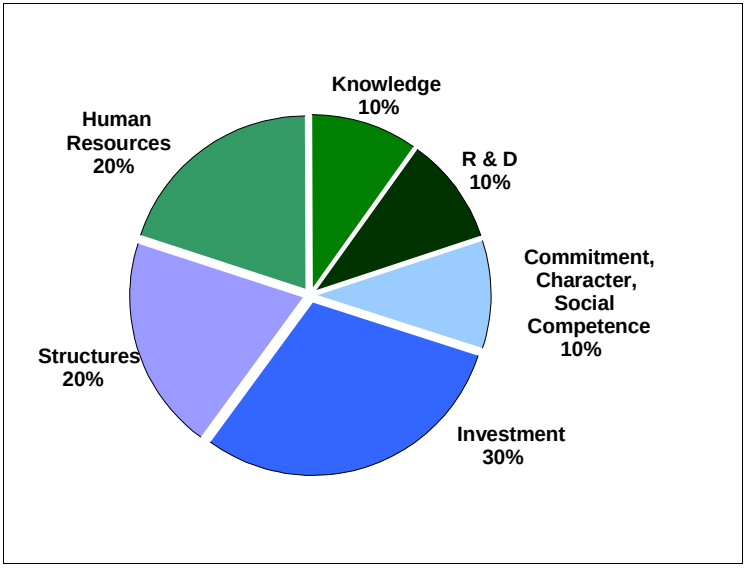
learning reaches its optimum thanks to the "face-to-face" communication that take place between customers, management and staff.

Innovation creation mechanisms also include the production and dissemination of knowledge that is available outside the enterprise. Productivity increases when a company is able to share in a knowledge pool, either at the branch level or the level of the national economy. The dissemination of knowledge promotes innovation and ensures that implementation can take place in small steps. It is often difficult to distinguish between what is innovation and what is merely product improvement in destination-oriented tourism.

Figure 2.12. Determinants of labour productivity in the field of tourism: the importance of innovation creation mechanisms



Source: P. Keller.

Another innovation creation mechanism is information technology, which is an important production factor in tourism today. Efficient information technology infrastructure and software applications are vital factors in tourism development.

Improving competitive structures

The small business structure typical of destinations is not really suited to rapid growth. The purpose of an innovation-oriented tourism policy is to speed up restructuring with the help of tailor-made promotional programmes including for the

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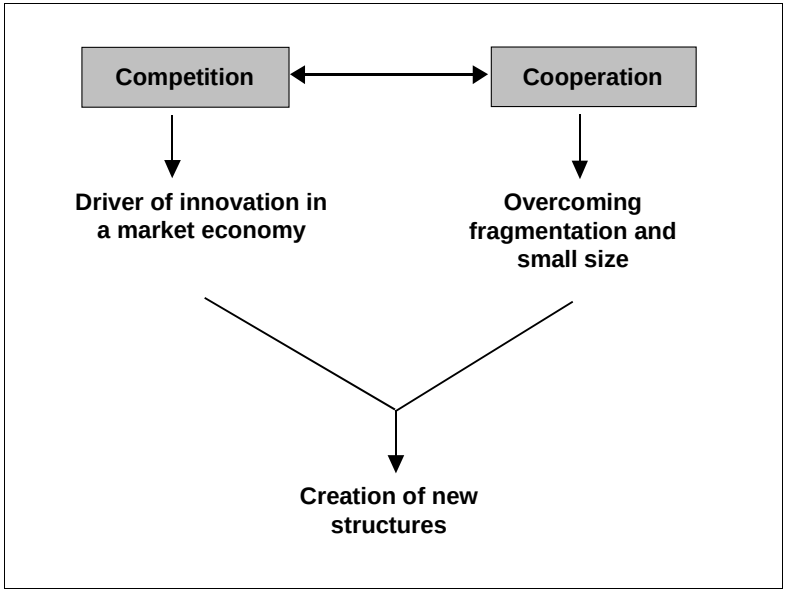
creation of entirely new structures. As in the field of technology so too in tourism, development policy can be made to focus on efforts to improve the structures of the innovation process (Figure 2.13).

Such programmes are in the twilight zone between competition and cooperation. Competition is indeed the motor of innovation. But without cooperation the fragmented world of the destination with its small businesses is incapable of innovating and offering the customer additional utility.

Figure 2.13. Competitive market structures



Source: P. Keller.

Cooperation only makes sense from an industrial economics point of view when the objective cannot be achieved alone, or when it is not possible to purchase the solution in the marketplace. Cooperation should only be considered after a company has explored all possible avenues of growth in-house. Structures will become more competitive once a company has grown in size.

Taking full advantage of the endogenous growth potential

Tourism development depends on a large number of exogenous factors which neither companies nor governments can influence. These include the source market potential, accessibility and the related transportation costs and the existing

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attractions a given place. These factors limit the opportunities for product innovation. On the other hand, they play an important role for the development of tourism clusters in a given space. The geographical advantages of a place and the connected built economic structure are endogenous growth factors and the bedrock of innovation (Koch, 2004).

Major attractions give the firms that settle around them an opportunity to grow, to increase their returns and to internalize positive agglomeration impacts. They lead to fast growing destinations which cast a shadow that limits growth in the hinterland where, as a result of economies of scale that are constant rather than increasing, only niche activities are possible.

In conditions of global competition and in mature markets international overnight tourism increasingly concentrates on the best locations. An innovation-oriented tourism policy should not attempt to stand in the way of this kind of restructuring. It should concentrate on efforts to strengthen the centres, and at the same time promote niche activities in the outlying areas.

Existing tourism centres with their multi-optional range of products and services are unique competitive systems which cannot be copied without major investments. The geographical proximity of a group of interconnected companies and associated institutions such as tourism offices have a positive impact on the performance. These highly diversified clusters offer favourable conditions for product and process innovation. Proximity is important and creates knowledge spillovers. Destination or tourism clusters are a sort of "marketing park", making it possible to take full advantage of the endogenous growth possibilities of a given place (Porter, 2000).

Reasons for the promotion of innovation

The promotion of innovation by the State is a matter of controversy from the market policy point of view. There are nonetheless valid reasons for adopting an innovation-oriented tourism policy, essentially relating to market imperfections and redistribution objectives (Keller, Smeral, 1998).

Innovations are a way of making sure that the economic structures of destinations will always be dynamic. Existing products and services have to be upgraded. And since it will be necessary to attract new companies, location promotion policy must be a part of innovation policy.

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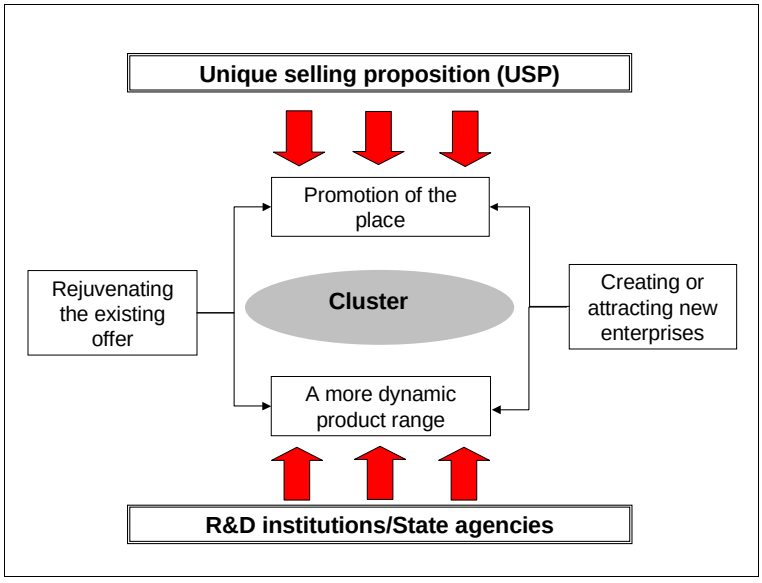
Figure 2.14. R&D Division for tourism clusters



Source: P. Keller.

Tourism locations or clusters are potentially a good breeding ground for innovations. However in view of the predominance of small business structures they lack the in-house R&D facilities needed to "automate" the innovation process and make it a matter of routine. The State can help to create centres of excellence to pool know-how and then disseminate it at both the local and national levels, at the same time providing support for applied research and development (Figure 2.14).

The State can also encourage private initiatives, which on the basis of cooperation between different companies and economic sectors can clear the way for new structures. In tourism the creation of new products and improved processes cannot succeed without cooperation, since in most cases their production involves a plurality of service providers.

The more specific the nature of the cooperation, the higher the transaction and organization costs will be. The private sector is often unable to afford the transaction costs in the case of major projects requiring highly specific and intensive cooperation, such as the development and implementation of an information and reservation system at the level of a destination.

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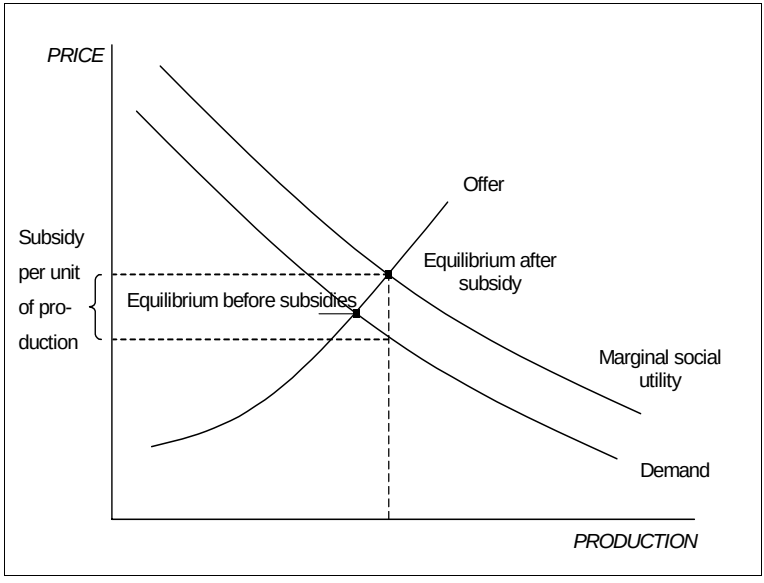
The State does not provide incentives for innovative projects in the area of tourism purely out of a spirit of magnanimity. Such support is justified by the fact that a flourishing tourism industry helps to increase general prosperity. State support can help to increase demand for tourism services. And the higher output will create new jobs (Figure 2.15).

Figure 2.15. Impact on prosperity of marginal social utility



Source: P. Keller.

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PART II. CHARACTERISTICS OF THE INNOVATION PROCESS IN TOURISM

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CHAPTER 3. INNOVATION AND ECONOMIC GROWTH

This text has been drafted by Nathan Rosenberg, Professor of Economics (Emeritus), Stanford University.

Abstract

This paper illustrates why technological innovation is considered as a major force in economic growth and focuses on some of the most distinctive features of innovation in the highly industrialized economies of the OECD area. In particular it attempts to examine a primary feature, the "uncertainty" that dominates the search for new technologies, with several cases drawing on American experience. It also touches on the impact of technological innovation and how it is transforming the tourism business model.

Technological innovation, a major force for economic growth

It is taken as axiomatic that innovative activity has been the single most important component of long-term economic growth. This paper begins by drawing on the findings of a very influential paper published by my colleague at Stanford, Prof. Moses Abramovitz, in the mid-1950s[4].

In the most fundamental sense, there are only two ways of increasing the output of the economy: (1) you can increase the number of inputs that go into the productive process, or (2) if you are clever, you can think of new ways in which you can get more output from the same number of inputs. If you are an economist you are bound to be curious as to which has been more important – and to what extent. Essentially what Abramovitz did was to measure the growth in output of the American economy between 1870 and 1950. Then he measured the growth in inputs (of capital and labor) in the same time period. He made what he thought were reasonable assumptions about the growth in a unit of labor and how much growth in a unit of capital should add to the output of the economy. It turned out that the measured growth of inputs (i.*e.*, in capital and labor) between 1870 and 1950 could only account for about 15% of the actual growth in the output of the economy. In a statistical sense, then, there was an unexplained residual of no less than 85%.

4. ABRAMOVITZ, M. (1956) *Resources and output trends in the United States since 1870.*

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Surprisingly enough, no economist had ever undertaken this exercise before - partly because it was only after the Second World War that reasonably accurate estimates of inputs and outputs for the American economy, over an extensive period of time, became available. Now, in any statistical exercise in which you are trying to tease out the relative importance of some variable, and you find yourself with a residual of 85%, you know you are in big trouble! Yet a number of other economists in the late 1950s and 1960s undertook similar exercises, using different methodologies, different time periods, and different sectors of the economy, with roughly similar results – they found themselves left with a very large residual that could not be accounted for. Robert Solow[5], who later won a Nobel Prize in Economics, was one of those other economists who discovered a very large residual, using a very different methodology and different time period. As it happened, he got the same result for the size of the residual – 85%. It was precisely the size of this residual that persuaded most economists that technological innovation must have been a major force in the growth of output in highly industrialised economies.

Although it might be tempting to say that the 85% residual was a negative finding, negative findings can sometimes be extremely useful. In this case the large size of the residual served as a kind of "wake-up call" to the economics profession because most economists for the previous 200 years had been building models in which economic growth was treated as if it was primarily a matter of adding more inputs into the productive process, especially inputs of capital. The large residual told economists that they had to look elsewhere in order to account for economic growth.

So I am going to focus my attention on some of the most distinctive features of innovative activity in the world of the highly industrialised economies of the OECD countries, and I will draw, in several cases, on the American experience. Actually, I want to focus primarily on a single feature that dominates the search for new or improved technologies, and some of the consequences that flow from this feature. The key word is "uncertainty."

Dealing with uncertainties

It is easy to conclude that, in advanced high tech countries with large, powerful firms, uncertainties will no longer be a major concern. After all, in the United States today, there are more than 16 000 firms that currently operate their own industrial research labs, and there are at least 20 firms that have annual R&D budgets in excess

5. SOLOW Robert (1970) *Growth Theory: an Exposition.*

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of USD 1 billion. In fact the top 20 American firms spent a total of USD 54 billion on R&D in the year 2000. Surely, you might think, such firms are no longer preoccupied with nagging problems flowing from uncertainties and the attendant financial risks.

Now, if you thought this, you would be wrong, very wrong, and for two compelling reasons. The first reason, as I have already suggested, is that the conduct of R&D in the high tech sectors of OECD economies has become hugely expensive. The second reason is that the outcome of this R&D spending is fraught with financial risks that derive from a variety of sources. What are these sources?

- Expenditures on scientific research may simply fail to discover new scientific knowledge of any potential usefulness whatever.

- Even if new scientific knowledge does emerge from research findings at the scientific frontier, it may never lead to a new marketable product. Or, equally important, it may require such a long period of expenditures on new product design or development that business decision makers may conclude that the realization of a new product is likely to be unacceptably costly – *i.e.* unprofitable.

But even if research does eventually lead to a valuable new product concept, many further questions remain to be addressed:

- How well will the new product perform, not only technologically, but in economic terms? Will a high performance be attained, but only at a prohibitively high cost? The Concorde airplane was a simply magnificent achievement in terms of engineering design and speed, but it was also an unqualified financial disaster. It was calculated, when the Concorde project was begun, that 300 of the planes would need to be sold, merely in order to cover its development costs. In the event, only 16 were sold.

- How rapidly will performance improve and how rapidly is the cost of production likely to decline?

- How appropriable is the product for the innovating firm? By "appropriable" I mean, how great is the likelihood that the innovating firm will be able to capture any profits that might be generated by its innovation? This may depend on whether the innovation is patentable.

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If not patentable, how soon is it likely to be imitated by competing firms that spent none of their own money in inventing the product? [This is the "free rider" problem].

– It is possible that a government regulatory agency, or a court decision, may destroy expected profits through regulatory requirements or a judicial ruling. In the US pharmaceutical industry the Food and Drug Administration requires that new pharmaceutical products go through a protracted period of testing before they may be sold to the public. Many new pharmaceutical products must be tested for several years before they can be marketed – in some cases the testing period may be more than a decade, as in the cases of vaccines or new contraceptive technologies. Estimates of the cost of bringing a wholly new pharmaceutical product to market in the US now routinely exceed the USD 500 million marks.

  Additionally, almost everyone in Switzerland must be familiar with ABB's devastating financial losses due to its acquisition of an American firm called Combustion Engineering. It turned out that ABB eventually "inherited" (if that is the right word) the unexpected liabilities of its subsidiary. These liabilities resulted from the decision of an American court, in a gigantic class action suit, involving the potential damage to human health resulting from Combustion Engineering's extensive use of asbestos. The class action suit has already involved more than 200 000 claimants, with over 100 000 more claimants still waiting in line.

– Finally, how soon will a superior new product come along, either from a competitor or from the introduction of some entirely new technology? It is no paradox to say that one of the greatest uncertainties confronting new technologies is the invention of still newer technologies.

There is one further source of uncertainty that I feel obliged at least to insert here, even though it has nothing to do with innovation, and even though you are already painfully familiar with its consequences to tourism. That is, of course, the possibility of encountering acts of terrorism. Terrorism has already had a devastating impact on travel, especially travel by air as well as travel to countries (or areas) where the risks of terrorism are perceived to be high. No other industry is as vulnerable to terrorism as tourism**.**

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Thus, it is fundamental to an understanding of the nature of innovation to recognize that uncertainties are still at the heart of innovative activities. The basic fact of life here is that it is extremely difficult to forecast how the market will respond to the introduction of some new technology. One obvious reason is that, in societies that have become as affluent as most of the OECD member countries, it is difficult in the extreme to anticipate how certain new products (or services) will fit in with consumer preferences and priorities.

A few examples of innovation

Let me expand on this point by citing for you an absurdly incorrect failure to anticipate consumer reactions, on the part of a group of people who were certainly both intelligent and well informed: the reporters and editorial staff of *The New York Times*. In 1939 the *New York Times* reported on the success of recent experiments that obviously foretold the arrival of a potentially fascinating new product: television. But the *New York Times* did not think that television had much of a future – at least not in the United States. This most prominent and influential of all American newspapers solemnly declared: "Television will never be a serious competitor for radio, because people must sit and keep their eyes glued on a screen; the average American family hasn't time for it."[6] How do you explain the complete failure to anticipate that TV was to become the most influential and widely-used household consumer good of the 20th century? Frankly, I don't know how to answer that question, but it has been characteristic of many of the most important innovations of the 20th century that no-one correctly forecast their future impact. Indeed, far from being unwilling to keep their eyes glued to a television screen, a disturbingly high percentage of American families seem to have very little time for anything else!

Suppose we now consider a much more recent innovation: the mobile phone. In 1983, when AT&T was being divested in an anti-trust suit, it was considering whether it should attempt to retain the frequencies that would be essential for the operation of mobile phones. AT&T therefore hired one of America's best-known consulting firms to forecast the likely number of American subscribers for mobile phones by the year 1999. The forecast that was eventually given to AT&T was that there might be as many as one million subscribers to mobile phones in 1999. In fact, the number of subscribers passed the 70 million mark in that year!

6. New York Times (1939) C*ommentary after television introduced to a broad spectrum of the American public at the World's Fair.*

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How can you account for what now appears (in retrospect, of course) to have been an absurd underestimate? Partly, there was a failure to appreciate the very large number of ways in which such phones would be useful. But the underestimate was also caused by neglect of another consideration that is important in accounting for the future demand for innovations. The fact is that most major innovations enter the world in a very primitive condition, and go through a long process of technical improvements and cost reduction. The airplane first left the ground in 1903. The initial flight was less than the length of a football field, and the airplane was not an innovation of great commercial significance until the late 1930s. Why not? It took fully one-third of a century because many thousands of design improvements were necessary before airplanes became sufficiently safe and reliable to become widely used by the general public. I suspect, if any of us had been present at that first flight in December 1903, we would not have left the scene with visions of regularly-scheduled flights crossing the Atlantic Ocean in six hours or so, with passengers in a reasonably comfortable state.

The situation with respect to the mobile phone in 1983 was, in some important respects, very similar. Those phones were primitive. They were so heavy and bulky that they hardly deserved to have been called "mobile." The quality of voice transmission was extremely poor. And, most important, the original mobile phones of 1983 sold for around USD 3 000, compared with much less than USD 100 in the United States today.

Consider one other recent technology: the laser. In 1960 the laser was merely a fascinating scientific breakthrough of no obvious usefulness to anyone. But, as a result of the intense competitive pressures generated in market economies to develop and introduce new products, the laser came to serve as the platform for a bewildering variety of new applications. It has become the primary instrument of research in the science of chemistry. It is the instrument of choice in a wide range of surgical procedures. There are in fact five medical journals in English that deal entirely with the use of lasers in medical practice [dermatologists, ophthalmologists, surgeons, etc]. The laser is essential for the high quality reproduction of music in compact discs (CDs). Transactions at supermarket checkout counters have been speeded up by lasers that can "read" (*i.e.* scan) the bar codes on each item purchased. The best computer printers today make use of the laser. Lasers, together with optical fibers, have totally revolutionized the worldwide telecommunications system. Last, but surely not least, the US Food and Drug Administration has recently approved the laser as a much less painful substitute for the dentist's drill.

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The behavior of lasers had been predicted, on a purely theoretical basis, by Einstein, using no more than a blackboard and a piece of chalk, as long ago as 1916. But it took over 40 years before scientists could actually create a laser beam (Light Amplification by Stimulated Emission of Radiation).

Finally, the *computer*. The first digital, electronic computer was operating at the University of Pennsylvania's school of engineering at the end of 1945, and a number of firms were already engaged in the manufacture and sale of computers by 1950. And yet, as late as 1956 Howard Aiken, a brilliant physics instructor at Harvard and one of the great pioneers in computer development, continued to conceive of the computer as no more than a highly specialized scientific instrument. In 1956, in testifying before a congressional committee he was still, obviously, thinking of the computer as no more than an instrument suitable for only a narrow range of scientific research purposes. Aiken stated in that congressional testimony: "...if it should ever turn out that the basic logics of a machine designed for the numerical solution of differential equations coincide with the logics of a machine intended to make bills for a department store, I would regard this as the most amazing coincidence that I have ever encountered."[7] That is, of course, precisely how it turned out, but it was hardly a coincidence. A technology that was originally invented for one specific purpose - the numerical solution of large sets of differential equations - could easily be reprogrammed to solve problems in entirely different contexts, such as the making out of bills for a department store. But it was obviously not obvious. Now, nothing could be further from my intention here than to hold Aiken up for ridicule. Quite the contrary, he was a brilliant scientist and inventor, and yet he hadn't the most elementary sense of the potential impact of the invention to which he had made very large contributions.

The impact of a technological innovation

The impact of a technological innovation will generally depend not only on its inventors, but also on the creativity of the eventual users of the new technology.

Consider the electrification of factories. So long as factories depended on steam as their primary power source, the organization and layout of activities on the factory floor had to be determined by proximity to a single power source: the steam engine. Each machine on the factory floor, in turn, drew upon this power source through a clumsy and extremely wasteful transmission system of leather belts and pulleys. The introduction of electricity, with separate electric motors attached to

7. AIKEN Howard (1956), *The Future of Automatic Computing Machinery.*

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each machine, allowed the layout of work to be organized in a far more flexible and efficient way, depending on the sequence of activities required by the needs of the production process rather than by the location of the steam engine. The parallels with the introduction of the computer are obvious. But it is also relevant to point out that economic historians have recently devoted a great deal of attention to the electrification of American factories. The consensus of their studies is that it took about 40 years – from the 1880s to the 1920s – before the application of electric power produced a measurable increase in factory productivity. And one could also make a plausible argument that the interface between people and computers is a far more complex one than the interface between people and electric power. In thinking about high tech innovation, we tend to be excessively preoccupied with the work of the scientists and engineers whose R&D activities have created the new technologies in the first place. This is a case of misplaced emphasis. The benefits that can be made to flow from lasers, microprocessors, computers and information technology generally will ultimately depend not only on its inventors, but also on the creativity of the potential users of the new technology.

Of course, it is also important to remember that the computer itself has been transformed since the giant mainframes were supplemented (and, to a considerable extent, replaced) by desktop personal computers. The result has been an explosion of new efficiency opportunities, insofar as data processing could now be carried out in ways, and in places, with a degree of flexibility that was not possible with mainframes alone.

Merely applying much greater computer speed to patterns of work that were designed for an older and slower technology, is likely to yield very little in the way of productivity improvement. Redesigning the work process is a very complex problem in its own right, and it necessarily takes a long time, as the early history of electricity amply demonstrates. The introduction of the PC has required the reorganization of long-standing business practices, along with the design of new, complex software, tailored specifically for the employees of the business firm. This, in turn, continues to require the application of managerial skills of a very high order of sophistication in determining how the patterns of work might be optimally redesigned in order to exploit the vastly expanded capabilities of the latest generation of computers.

Innovation in tourism

With respect to the tourism sector, what appears to be called for is an intimate familiarity with consumer needs and preferences in particular specialized markets,

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and a speedy and imaginative approach to how these needs might be catered to in a more efficient, but also a more attractive and user-friendly manner. But my uninformed speculation suggests that Information Technology, and the Internet and World Wide Web in particular, are going to transform the role of travel agents, and doubtless sharply reduce the size of the travel agent industry, unless this industry can identify a new bundle of services that can be provided to potential travelers. Any household with access to the Internet – and therefore access to Google – now has immediate access to detailed information about almost any conceivable location on the earth's surface as a possible candidate for a visit.

Needless to say, ticketing for airplane travel can also be arranged on the Internet, which also provides invaluable information about the various prices of airplane tickets. In fact, an American research company (Forrester) has recently calculated that travel is now the largest on-line business in the world. The Internet is obviously transforming the tourism business in many ways, and easy access to information is growing rapidly in each of the separate components of the industry, and making it increasingly competitive. The ultimate uncertainty is figuring out new ways of rendering the tourist industry at least minimally profitable. I am happy to leave this subject to your deliberations over the next two days.

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CHAPTER 4. PRODUCT IMPROVEMENT OR INNOVATION: WHAT IS THE KEY TO SUCCESS IN TOURISM?

This text has been drafted by Klaus Weiermair, Professor and Head of the Center for Tourism and Service Economics, University of Innsbruck.

Abstract

This paper is built like a three–layered clubhouse sandwich with the first layer providing some theoretical and conceptual insights regarding expected innovation behaviour in tourism based on the available relating to tourism and industrial economics. The second layer provides insights regarding the causes and effects of innovation and product development in tourism, based on empirical research carried out at this Center, and interviews carried out by the author both in Europe and North America with major companies active in national and/or global tourism, including tour operators, airlines and theme parks. The last layer of the sandwich draws conclusions and discusses the results of the research with respect to tourism policy making.

Relevance and importance of innovation and product development in tourism

It is fair to say that most sectors in Western economies have undergone strong technological changes moving towards flexible manufacturing based on information technology (IT) with global outsourcing, creating the so-called "dot.com" or "new" economy, which closely corresponds to what Schumpeter calls the creative destruction of existing institutional arrangements and patterns of exchange in order to create new wealth through innovation. He also sees an increased willingness to take calculated risks by new or "genuine" entrepreneurs[8].

Even though much innovation emanates or originates in the service sector, so far there has been relatively little discussion as to its importance in tourism. *A priori* one should expect that innovation and product development (or differentiation) should constitute unique selling propositions and a strategy for gaining new markets[9]. Even though tourism as a typical service sector is now a very mature

8. Schumpeter J. (1934), *The Theory of Economic Development.*

9. BULLINGER, H.J. (1999), *Entwicklung innovativer Dienstleistungen.*

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market and requires innovation and/or new tourism attractions[10], the actual situation in tourism is characterised by minor, indeed almost cosmetic changes in the product offered, plus an ever growing number of crises (Iraq war, "9/11", SARS etc.). As early as 10 years ago Poon noted: "The tourism industry is in a crisis – a crisis of change and uncertainty; a crisis brought on by the rapidly changing nature of the industry itself. (…). New technology, more experienced consumers, global economic restructuring and environmental limits to growth are only some of the challenges facing the industry[11]."

It is only in the past decade that destination management has barely managed to adjust to completely changed environmental and competitive structures and processes. Existing destination strategies no longer satisfy market requirements[12]. Small-sized and fragmented alpine tourism companies in particular face increasing competition[13] and are confronted with declining numbers of tourists[14]. This is also true of coastal tourism. The challenge for the future is to provide increased value for money either through innovation-driven changes in production and marketing processes that reduce costs or product changes that offer more varied tourism experiences for quality conscious customers[15]. Two major markets the tourism industry will have to deal with in future are:

- The growing proportion of senior citizens in most western economies
- China, which is expected to be the largest importer of tourism by the year 2010

In the rest of my presentation I shall address the following points:

10. Weiermair, K. (2001) *Neue Organisations-, Koordinations- und Führungsprinzipien im alpinen Tourismus.* Keller, P. (2002) *Innovation und Tourismus.*

11. Poon, A. (1993), *Tourism, technology, and competitive strategies, p. 3.*

12. Weiermair, K. (1998) *Threats and Opportunities of Information Technologies: The Case of Small-and Medium-sized Tourism Enterprises.*

13. Smeral, E. (2003) *Die Zukunft des internationalen Tourismus.*

14. BARTALETTI, F. (1998) *Tourismus im Alpenraum.*

15. Weiermair, K. (2001) *Neue Organisations-, Koordinations- und Führungsprinzipien im alpinen Tourismus*; Weiermair, K. (2003) *Neue Urlaubs- und Reisemodelle zwischen Abenteuer und Entspannung.*

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1. Which areas of the tourism value chain or the "tourism experience" are important for innovation?

2. Which can we say about the dimensions of innovation?

3. What are the primary motives for innovation?

4. Which are the success factors for innovation in tourism?

Definition of the term "innovation"

There are various definitions of the term "innovation", which derives from the Latin "innovatio" which means the creation of something new. The diversity of definitions lies in the different purposes for examining this phenomenon[16]. Probably the most useful definition is that provided by the late Schumpeter[17] who distinguished five areas in which companies can introduce innovation:

1. Generation of new or improved products

2. Introduction of new production processes

3. Development of new sales markets

4. Development of new supply markets

5. Reorganisation and/or restructuring of the company

The above definition clearly distinguishes innovation from minor changes in the make-up and/or delivery of products by extending product lines, adding service components or product differentiation. Successful innovation, *e.g.* innovation that is also profitable to the tourism firm in a competitive market, must increase the value of the product or tourism experience. Since the value equation is "quality perceived by customers, divided by the price (cost) of this quality", to be successful innovation

16. JOHANNESSEN, J. A. et al. (2001) *Innovation as newness: what is new, how new, and new to whom?*

17. Schumpeter, J. (1997) *Theorie der wirtschaftlichen Entwicklung. Eine Untersuchung über Unternehmergewinn, Kapital, Kredit, Zins und Konjunkturzyklus.*

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must increase value either by improving the quality or by lowering the price (cost) [18].

Producing and marketing tourism products is not the same as producing and marketing industrial products. Tourism's specific characteristics often pose constraints or problems that can serve as stepping-stones for increasing the value of products via innovation. The differences are as follows: tourism produces and sells product bundles (or "experiences") which are very intangible; its products cannot be stored (simultaneous production and consumption); the consumption of tourism products involves the active participation of the customer (prosumer); tourism production/marketing may often involve major capital assets (airlines, hotel chains, car rental firms); the intermediation, distribution and final consumption stage may often require interaction of different personnel categories (*e.g.* travel agencies, restaurants, coaches, etc.).

Typically when a tourist spends his holidays in a destination, he does not consume the products of just one supplier, but a package of services as a whole[19] . Many suppliers participate in the creation of a tourism experience. This requires vertical cooperation as the tourist's overall quality assessment depends on cumulative quality perception [20]. As far as the tourist is concerned, the product is a complete experience; encompassing everything from the time he leaves home to the time he returns.

Tourism services are personal services created by internal (supplier) and external (client) factors[21]. The client himself has to be proactive and in most cases must travel to the destination (a constraint which could serve as a stepping stone for innovation). He participates either passively (*e.g.* using cable cars) or actively (*e.g.* skiing) in the process of service production. In accordance with the *uno-actu* principle, offers not taken up cannot be stored making efficient capacity utilisation one of the big problem areas in tourism. This applies to all tourism services in

18. HESKETT, J.L. (1986) *Managing in the Service Economy.*

19. Kaspar, C. (1991) *Tourismuslehre im Grundriss.*

20. Koch, K. (1998) *Zusammenarbeit im Tourismus - die industrielle Kooperation als Vorbild.*

21 Smith, S.L.J. (1994) *The Tourist Product.*

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accommodation, catering, travel agents, transport systems, and all other businesses in the tourism value chain[22].

The intangibility of tourism products implies a large amount of risk and uncertainty about customer value (quality-price ratio). A guest who books a holiday package does not know what to really expect, or how he will eventually feel about the quality of his vacation. It is particularly important for destinations to create confidence, to determine quality criteria and to introduce measures to reduce risks for the customer.

Overall, tourism services are very capital-intensive and depend on external partners and other factors. Similarly, the capability and the motivation of staff (human resources) is an essential factor, suggesting the need for both capital and labour related types of innovation. Finally tourism needs local infrastructure. The local population should have a positive attitude to tourism, and local industry should act as a supplier for tourism businesses and shops[23].

Potential areas for innovation in tourism

What are the implications for innovation from these special characteristics of tourism products? First of all, in today's saturated markets customers look for "experiences" rather than destination specific products. It will therefore become increasingly important to use innovation and product development to create rewarding tourism experiences rather than isolated components. Experience-based holiday proposals will become the main motive for the holiday decision[24]. The creation of experience should cover "entertainment", "educational", "aesthetic" and "escapist" elements and/or product features as shown in the work of Pine and Gilmore (1999). Experience in this context means content, *i.e.* the nucleus of the holiday. The destination is like a stage and the different tourism companies are the actors on that stage. Continuous learning and the acquisition of knowledge from the customers will become essential[25].

22. MURPHY *et al.,* 2000.

23. BIEGER, T. (2002) *Management von Destinationen.*

24. BARTALETTI, F. (1998) *Tourismus im Alpenraum.*

25. HJLAGER, A.M. (2002) *Repairing innovation defectiveness in tourism.*

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The individualisation of mass tourism[26] and the extensive involvement of customers in the tourism experience creation process are transforming tourism into an "information" and "relationship" business. Customer involvement helps provide information about needs and wants, suggesting new paths for client data and yield management[27]. New information and communication systems will be needed to collect and to analyse information for the development of new products and services. It is important in this context not to imitate the innovations of others, but to build on a company's or destinations own strengths and core competencies, which can be further improved through knowledge management [28].

Given the intangibility of tourism products, the tourist may be uncertain about the quality of the services provided. Despite or because of this intangibility, tourism products can be enhanced in value by adding sensations (design, fragrance, light, colour, emotional attachment). Such product changes can only enhance the emotional value of the "tourism experience".

As a labour and capital-intensive industry tourism needs to build networks that can help pool resources, acquire know-how and minimise risks. This can help develop new markets, economise the resources invested and create new entrepreneurial options. Similarly, IT-based innovation in distribution and marketing as well as company alliances or other forms of cooperative marketing can help to reduce cost, thereby increasing customer value, market share and/or market extension.

On the economics of innovation and product development in tourism

I shall now analyse the economic motives underpinning entrepreneurs' innovative behaviour and the various types of innovation that can be distinguished.

26. Poon, A. (1993) *Tourism, technology, and competitive strategies.*

27. Weiermair.K., Mathies, Ch. (2002) *Use and misuse of yield management practices in tourism: A lesson from the airline industry.*

28. Weiermair, K. (1998) *Threats and Opportunities of Information Technologies: The Case of Small-and Medium-sized Tourism Enterprises.*

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What drives innovation in tourism?

There are three factors that determine the level and pace of innovation in tourism, *i.e.:*

- Supply or supply–related determinants.
- Demand drivers.
- The level and pace of competition.

Supply factors

New technologies have resulted in the development of new skills, new materials, new services, and new forms of organisation. This has been especially true in the last two decades, in which technological innovation has played a crucial role. In tourism, technology has created a new form of business called "e-tourism", which is today the most successful form of "e-commerce".

This has created a need for new tourism management skills (e-marketing), such as coaching and interactive skills in the fields of wellness or adventure tourism. New information services for guests emerged as databases made it easier to process customer profiles and behaviour. New forms of network organisation also emerged particularly in the field of cooperative tourism marketing, assisted by new technologies.

Demand-side changes

There have been changes on the demand side as well as on the supply side. Social progress in the areas of work versus leisure time, the population pyramid, individualisation and increased demand for quality have modified leisure and tourism behavior[29]. New lifestyles have been created by flexible work hours, higher

29. Poon, A. (1993) *Tourism, technology, and competitive strategies*; HORX, M. (2002) *Die acht Sphären der Zukunft. Ein Wegweiser in die Kultur des 21. Jahrhunderts;* FOOT, D. (2002) *Leisure Futures: A Change in Demography?* BIEGER, T., LAESSER, C. (2002) *Future Living: Conditions and Mobility: Travel Behaviour of Alpine Tourists;* Weiermair, K. (2003) *Neue Urlaubs- und Reisemodelle zwischen Abenteuer und Entspannung.*

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incomes, more leisure time and the increased value of holidays that are now seen as an essential part of life.

Basic driving forces for quality service are punctuality, accountability, convenience, speed, and price. Aesthetical considerations, personal attention, and multiple options are secondary and viewed as "added features". They nonetheless help to create a special "value for money" for the customer.

Customer orientation plays a fundamental role in service innovation. Valuable information can be gained from the behaviour of the customer, who is closely involved in the production of any tourism service. Companies need to be ready to adapt to the changing interests and values of their guests. The most successful new products offer a special or unique value based on innovation with the client's interests and needs in mind. Such innovations lead to a higher market share, improved efficiency and make it easier to achieve turnover and profit objectives[30].

Competition

Many tourism branches and in particular transportation, airlines, hotel chains, tour operators and car rental agencies are highly concentrated and act as global players in the industry. As markets mature further technological advances in the IT field and the slowing of demand can transform normal rivalry into ruinous competition.

Globalisation and deregulation have further heightened competition. As in other fields of economic activity they favour process innovation (networking, reservation and yield management systems, etc.) rather than product innovation, the latter being too easy for rivals to imitate[31].

Types of innovation

A useful distinction between types of innovation in tourism has been made by Hjalager, who adopted concepts developed by Abernathy and Clark (1985) and developed a model to measure innovation levels (degrees) in tourism using core

30. HUBNER, H. (2002) *Integratives Innovationsmanagement. Nachhaltigkeit als Herausforderung für ganzheitliche Erneuerungsprozesse.*

31. Weiermair, K. et al. (2002) *Innovation and Innovation behaviour in hospitality and tourism: Problems and Prospect*: *Tourism in Asia: Development, Marketing and Sustainability.*

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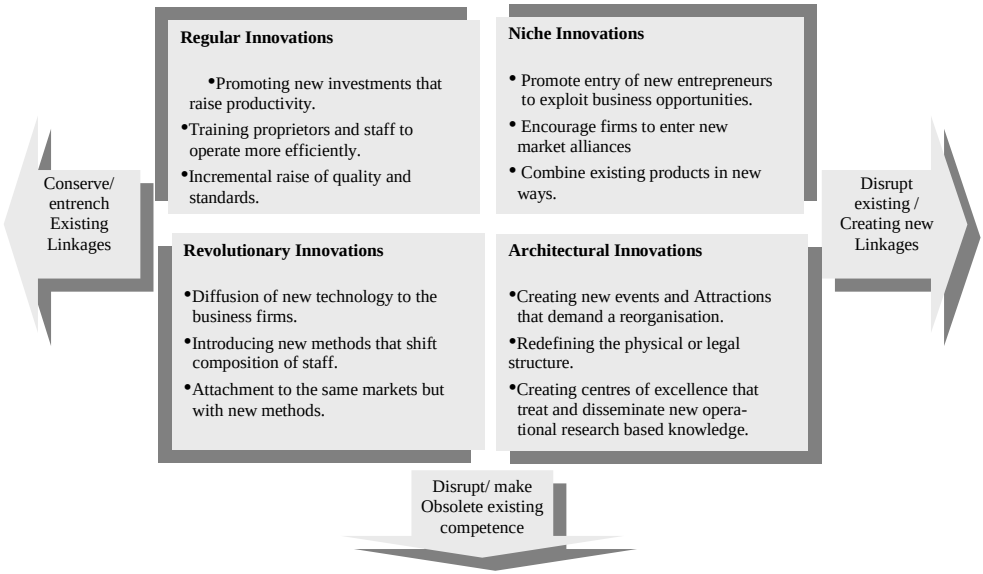
competencies as the unit of analysis. Such differentiation seems particularly suitable to innovation in tourism, which is often based on core competencies[32] involving internal and/or external factors. Internal company resources are the most important determinants for the positioning and competitive advantages of a company that are difficult to imitate[33]. Hjalager (2002) distinguishes four types of innovation dealing with either the breaking up or deepening of relationships with clients or the market and the abandonment or preservation of competencies (Figure 3.1).

Figure 3.1. Innovation types, adopted from Abernathy and Clark[34]



Source: Hjalager 2002, p. 467.

While niche innovations emphasise new forms of cooperation (*e.g.* cooperation with a tour operator) and do not affect existing competencies, architectural innovations (*e.g.* arctic tourism) introduce new structures and redefine relationships with customers and existing markets. External branch structures and target groups

32. Schwaninger, M; Flaschka, M. (1995) *Managementsysteme revolutionieren Dienstleistungsunternehmen.*

33. GOMEZ, P., PROBST, G. (1995) *Die Praxis des ganzheitlichen Problemlösens.*

34. ABERNATHY, W. & CLARK, K. (1985) *Innovation: Mapping the Winds of Creative Destruction*, Research Policy, 14, pp. 3-22.

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remain unchanged when a revolutionary innovation is realised, although services have experimented changes by adopting new technologies. Regular or incremental innovations are realised with existing competencies and existing relationships. Examples of this are: increased productivity, quality improvements or further training of staff members (*e.g* of a hotel) [35].

These systematic categories seem to be useful, although the shortening of product life cycle noticed in the past decade has also to be recognised. The same holds for innovations, which implies a dynamic change of innovations belonging to one of the four types mentioned (Figure 1).

Empirical evidence gathered so far

The Center for Tourism and Service Management, University of Innsbruck (Austria) is currently gathering data on innovation and product development at the level of the destination. Below I report on a different set of data, gathered from interviews carried out in North America and Europe with major national and global tourism firms including tour operators, travel agencies, individual hotels, hotel chains, cable car companies, theme parks, one provider of e-tourism (databases), restaurants, and charter airlines. Our main interest was to assess the prevalence of process versus product innovation in different settings. The findings are summarised in the figure below (Figure 3.2).

Although all firms see information technology and its applications in e-tourism as a major change none recognise it as an innovation, since it came from outside the industry. A second change, accepted as an "innovation" involves new forms of business alliance and cooperative marketing to extend markets. This may involve teaming up with non-tourism partners and/or suppliers (lower cost of acquiring new customers). Most firms mentioned strategic partnerships in the fields of human resource management, product changes, and adding new destinations. In North America, major objectives were cost reduction followed by revenue generation, while in Europe increasing customer value followed by profit maximisation are seen as the most important incentives for innovation. However, minimising costs is only a subordinate goal for innovative firms in Europe.

35. HJALAGER A.M. op. cit.

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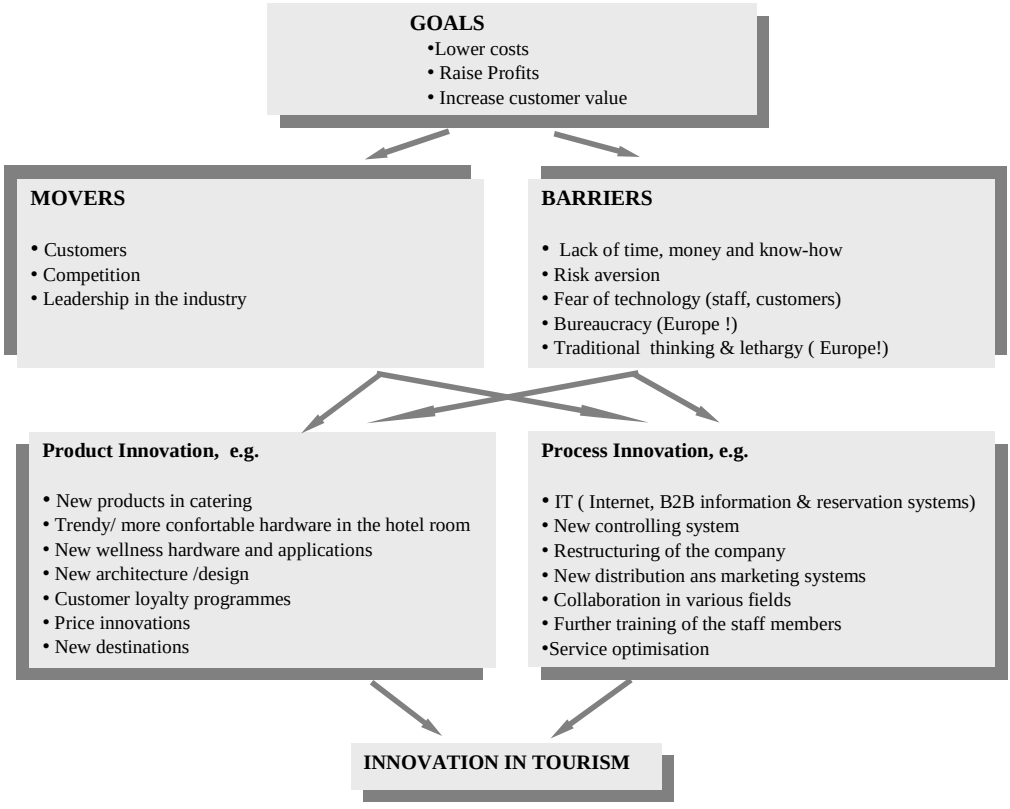
Figure 3.2. Product versus Process Innovation in Tourism



Source: Center of Tourism and Service Management, University of Innsbruck (Austria).

Most firms recognise the importance of product development. However it rarely involves entirely new products or entirely new markets, being rather a process of individualising the mass market (products) by product differentiation, product line extension via branding policies or by changing the cost (price)/quality ratio of the product. All firms try to simultaneously lower cost and at the same time achieve product uniqueness, *e.g.* through choice of destination, hotels or other packaging changes. Other reasons are the availability of firm-specific technologies and supplier relationships. Often innovation is inspired by environmental constraints, *e.g.* a long-lasting strike at United Airlines incited one major Hawaii tour operator to create its own charter airline.

Competition in mature markets (particularly skiing and golf) leads to pressure to add more experience to products, extreme examples being the offer by Space

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Adventure (American tour operator) of a place on a package tour to the International Space Station in 2005 for USD 20 million, and so-called scalpel safaris combining cosmetic surgery with a trip to the bush in South Africa[36]. Another example would be the 18-hour "voyage of the imagination" programme on a schooner. This package allows guests to masquerade as poor immigrants working their passage. Just two programmes were planned for 2003, but a third had to be added due to the demand[37].

Quality assurance, marketing practices, and customer and employee satisfaction were among the most important areas of innovation in which progress has been reported (no one said they have achieved total satisfaction). Cable car companies see security as an important area for innovation. The other factors were considered less important because of the little progress reported so far.

Most successful innovations involved new forms of distribution (online booking), agent relationships and reduced costs for product delivery. Cooperative marketing and other forms of strategic alliance were also mentioned. Niche marketing (special interest groups) together with small product changes should also be taken into consideration. Exceptions include a few tour operators and one theme park where product development played the key role (copyright was issued in this case).

Customers were mentioned in almost all interviews as the prime movers of innovation, followed by competition and the ambition to be the industry leader. Major barriers that firms had to face include lack of time, money or know-how, and risk aversion, all internal factors. Respondents, particularly in Europe, singled out bureaucracy and politics as the external factors most likely to stand in the way of innovation efforts.

All experts interviewed agreed that the most promising vehicles for innovation are cooperation, alliances and/or networks in various fields such as technology, marketing, distribution, and human resource sharing.

36. The Economist (2003) *New routes to the beach.*

37. CLARK, J. (2003) *Day trips turn to night at museum Sleepove.*

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Implications and prospects for tourism policy

Our empirical inquiry produced the following facts and/or proposals:

- The private sector only undertakes innovations if they promise to be profitable (the main driving factor).

- High cost and the risk of innovation combined with intensive or even ruinous competition make process innovation the most attractive option as a way to reduce cost (and price).

- Most companies, except a few tour operators and cable car producers/operators pioneering new products, prefer product differentiation strategies.

- There is a negative correlation between company size and innovative activity.

- Small firms are usually imitators, poaching innovations or product changes from "across the street" or in the region (rarely from farther afield)

This brings us back to the familiar tourism policy question: how much should governments spend on process or product innovation projects in view of the externalities, the prohibitive risk and cost and the indivisibility of research and development activities vis-à-vis a multitude of small user firms. Furthermore if a government does decide to involve itself, how much should be invested?

Many economists would agree with the following:

- Governments should not subsidise outright innovation, so as to avoid opportunism and rent-seeking behaviour.

- They should leave it to the market, intervening only in the case of market failure.

- They should encourage innovative firms to achieve economies of scope, innovating on the basis of cooperative alliances and other forms of networking.

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- Government's role should be limited to that of a facilitator, coach or "incubation" partner, passing prototypes to the private sector at the end of the innovation process (Examples include the Irish Tourism Board's development of a travel reservation and information system, or in Austria the development by the Tyrol Tourism Board and the Future Foundation Tyrol of new products including family wellness holidays in Tyrol and other areas in the Alps).

Another approach which works well in regions or countries with destinations too far apart to compete is the Canadian Product Club Programme created in 1996, which currently promotes research and development in 45 product categories. The programme has 250 coordinating partners and more than 5 000 businesses cooperate[38].

A final point is the importance of a properly functioning and regulation-free market. On this score there is a clear difference between the barriers to innovation that preoccupy North American tourism companies and those feared by European firms. Bureaucracy is the main concern of the latter.

38. www.canadatourism.com.

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PART III. ROUTINISATION OF THE INNOVATION PROCESS IN TOURISM

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CHAPTER 5. HAS INNOVATION BECOME A ROUTINE PRACTICE THAT ENABLES COMPANIES TO STAY AHEAD OF THE COMPETITION IN THE TRAVEL INDUSTRY?

This text has been drafted by Martin Brackenbury, Former President of the International Federation of Tour Operators (United Kingdom).

Abstract

Since innovation is at the heart of any successful company's agenda its role in ensuring competitiveness deserves our full attention. This paper attempts to examine the ways in which tour operators, who assemble packages that include travel and accommodation, approach innovation and competitiveness. It looks in particular at groups which have achieved the complete vertical integration of travel agents, tour operators, airlines, incoming tour operating ground handlers, and accommodation including hotels, apartments and cruise ships. In addition it focuses on the practical, structural and operational challenges faced by companies competing in this sector of tourism.

Innovation and Economic Growth

Why has capitalism produced economic growth that is so much greater than can be achieved through other systems? Is it simply that price competition drives down the cost of goods and services and the savings is passed on to consumers as lower prices?

The answer is a clear "no". Price is not a sufficient explanation. No one would buy a new car that was designed 30 years ago such as a Trabant, whatever the price. New products have emerged to better satisfy the needs of current consumers. Cars that are faster, safer, more reliable, more comfortable, more economical and less polluting. Moreover cars are not just functional tools. They also meet emotional and social needs. People identify themselves with their cars in the same way as they do with their clothes, shoes, hairstyles, and holidays.

Companies that do not produce new products that better satisfy emotional and social as well as practical needs will disappear. As a general rule companies in any sector that fail to replace 10 per cent of their revenue stream annually with

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innovative new products will go out of business in five years, unless they are suppliers of simple products like cement.

If new products are important for economic growth and survival, what about processes? The companies that survive are those that manage to be profitable despite relentless price competition. To achieve this requires a complete re-examination of all processes, structures and product components from sub-contracted suppliers. These transformations are not achieved without significant innovation, which may at times be virtually invisible, at least to the consumer.

As might be expected innovation has been researched by a number of distinguished academics. William Baumol[39] stresses that large companies rely on systematic innovative activity within the firm as a competitive weapon. However, innovation carries with it significant risks. We tend only to remember the individuals who have been singularly successful at creating new economic and intellectual wealth for the rest of us to enjoy. The sad fact is that many innovations fail.

Carl Franklin in his book, '*Why innovation fails*'[40], quotes a study by three academics – Donald Lehmann, Jacob Goldenberg and David Mazursky – in which they looked at 197 product innovations of which 111 were successes and 86 were failures.

What they found was that the successful innovations had some, or all of the following features:

- They were only moderately new to the market.
- They were based on tried and tested technology.
- They saved money.
- They met customers' needs.
- They supported existing practices.

39. BAUMOL, William J. (2002) *The Free-Market Innovation Machine:Analyzing the Growth Miracle of Capitalism*. Priceton University Press.

40. FRANKLIN Carl (2005) Why Innovation Fails: Hard-won Lessons For Business. Spiro Press.

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The products that failed:

- Were based on cutting-edge or untested technology.
- Were created with no defined solution in mind.
- Followed a 'me-too' approach.

Particularly interesting is their list of 'Idea Factors'[41] establishing where the ideas for the innovations came from and how they determined the success or otherwise of the ensuing products. I have seen all of these factors at work in the tourism sector.

They categorised these 'idea factors' as:

- Market research.
- Trend following.
- Need spotting – looking for an answer to a known problem.
- Solution spotting – finding a new way of using an existing piece of technology, such as computers and lasers.
- Mental inventions.
- Random events – innovators stumbling upon something of significance.

They then plotted the success to failure rates of the six different idea factors. The lowest success rates went to 'trend following' and 'mental inventions' with three times as many failures as successes. 'Need spotting' and 'solution spotting' produced twice as many successes as failures. 'Market research' produced four times more successes than failures. The winner was 'random events' which produced 13 more successes than failures.

41. GOLDENBERG Jacob, LEHMANN Donald R., MAZURSKY David (2001) *The Idea Itself and the Circumstances of Its Emergence as Predictors of New Product Success.* Management Science Volume 47, Issue 1, pp. 69 – 84.

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It seems that firms face a dilemma – they must innovate or perish. But by innovating they run a considerable risk of failure.

William Baumol notes that firms faced with costly innovations that might well be rendered obsolete by their competitors participate in technology sharing and licensing arrangements. Innovation thus becomes a routine feature of economic life.

Clearly the competition authorities need to be convinced that such arrangements are not going to be used to create market power and thus artificially raise prices to consumers. Baumol feels that this mechanism of collaboration helps to account for the unparalleled growth of modern capitalist economies, enabling firms to come far closer to economic efficiency than is often understood.

So what evidence do we find of innovation in products and processes in the larger leisure travel groups in Europe and in travel agents (tour operators/airline/accommodation/hotels/ apartments/cruise ships)?

Background

Before answering this question, some background information is necessary. Vertical integration and consolidation began among tour operators in the 1960s in the UK when Riviera, Luxitours and Gaytours were consolidated into Thomson Holidays. Since then Tour Operator Brands have been acquired, often retaining their original identity, sometimes being absorbed and re-branded. The same process occurred in Germany, the Scandinavian and Benelux countries, France, Italy and Spain.

Europe now has six very large companies TUI (Germany), Thomas Cook (Germany), Rewe + LTU (Germany), MyTravel (UK), First Choice (UK), Kuoni (Switzerland).

TUI is by far the biggest, with 22 million customers, 81 brands, 89 aircraft, 3 715 travel agents and 287 hotels (with 153 000 beds) and 32 incoming agencies.

What, you might ask, has happened to the small independent tour operator? In Sweden there are virtually none, while in the United Kingdom the number of licensed tour operators continues to grow (currently 1 440). These companies can thrive and prosper in highly differentiated market niches. It does appear that where there are customers with highly differentiated requirements (*e.g.* bird watching, walking or sailing) tour operators arrive on the scene to satisfy that need. This suggests that barriers to entry are low, and indeed they are. However the economic

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model for the small independent tour operator (low risk, low commitment, high flexibility) is completely different from that of the large, fully integrated group (higher risk, high commitment, very limited flexibility within any seasonal time frame).

According to the International Air Transport Association (IATA) there are 771 charter aircraft in Europe operated by 26 companies some of which are fully integrated flying divisions of the major companies. These charter companies operate modern fleets (average age 4.5 years) with very high fuel efficiency, at high intensity (circa 4 200 hours per year) and with very high load factors (>90 per cent). Charter fleets were the first low cost carriers. In 2002 they operated more that 1 million flights to 561 airports worldwide and carried 1 18 million passengers. They have been instrumental in opening up originating source markets through the use of local airports, flying direct to holiday destinations. The major tour operators typically have in-house fleets that account for around 80 per cent of their production, with the rest supplied by other airlines. These charters and the low cost (no frills) carriers have operating costs that are roughly half those of the main network scheduled carriers, and this is reflected in the prices charged to consumers. It should be noted that these operating costs exclude any contentious contributions from airports.

The tour operators sell their products in packages – flights, accommodation and transfers – or as individual elements, either directly via direct mail and the Internet or through travel agents. Although the major companies have their own distribution channels they still rely on independent travel agents for part of their distribution. The structure of this distribution varies from one national market to another. For example Sweden is almost all-direct selling while the United Kingdom is about 60 per cent through travel agents. In no European market does the Internet account for more than 10 per cent of package holiday sales. It is worth noting that low cost carriers sell more than 80 per cent online.

Needs and perceptions differ not only from country to country but from one market segment to another within a given country. There has been no European homogenisation -- markets have remained national and idiosyncratic. It is for this reason above all that suppliers in destinations, such as hotels and other types of accommodation use tour operators, who know their customers.

At the most basic level one can see marked differences in accommodation preferences. In Scandinavia about 90 per cent prefer apartments to hotels, while in Germany 80 per cent prefer hotels to apartments and in the United Kingdom the

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ratio is about 50/50. It is interesting to note that Turkey, a key non-EU competitor, has decided to invest almost 100 per cent in hotels – thus cutting itself off from half the market. Not surprisingly, it does a brisk trade with Germany in this context.

In the early 1980s there were no sizeable hotel chains in the leisure sector. Since then a number of independent resort hotel chains have emerged, mostly through take-overs, but also by direct investment or franchising. The most obvious example is Sol Melia based in Mallorca.

The major integrated groups have also entered the hotel sector. First Choice with Barcelo, MyTravel with the Sunving spelling Group, and TUI with hotels branded for different segments. However in most cases owned hotels do not account for more than 10-15 per cent of the capacity of these groups. Thus 85-90 per cent of hotel capacity is provided through contracts with thousands of independent hotels and other accommodation suppliers.

More recently some of the major operators have decided to acquire their own local ground-handling agents in the destination, to provide transfers and excursions. For the most part these are contracted out to a plethora of local suppliers.

Motivations for consolidation and vertical integration

Small operators can grow at a very rapid rate for a limited period. Subsequently, since the overall market is growing relatively slowly any additional growth must be at the expense of other tour operators. A customer that would have opted for company A is induced to choose company B. An individual firm's ability to grow will be limited by competitive responses, which are generally to the advantage of consumers since they take the form of price reductions. This competition on price does however tend to accelerate overall growth in the market. Shareholders who wish to ensure continuous growth can always resort to mergers and/or acquisitions.

The road to growth involves many difficult and important decisions along the way. For example, when a tour operator reaches a certain size the lack of a guaranteed supply of charter seats raises the question of starting its own charter airline. The problem is that this solution means that the risk of not filling enough seats and thus not being able to pay the leaser lies with the tour operator.

So capturing the profit and exercising control are key motivations -- control over distribution through both travel agents and selling direct to consumers, and control of airline seats and (to some extent) beds and incoming agencies.

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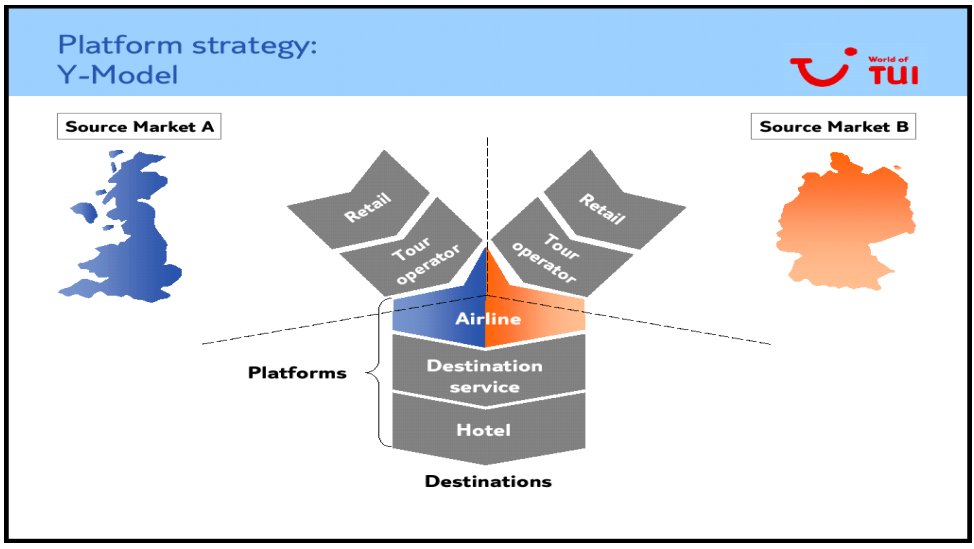
To illustrate this TUI have what they call the 'Platform Strategy: Y-Model' (Figure 4.1).

Figure 4.1. Platform strategy: Y-Model



Source: TUI.

This shows how source markets can be managed separately, creating synergies by using three platforms: the airline, destination service and the hotel.

This is an opportunity to guarantee quality, create synergies and develop a master brand as a basis for group identification.

The results of consolidation and vertical integration

For consumers

Consolidation and vertical integration have brought about lower costs, particularly in the airline sector. To some extent this has been the result of higher productivity across the entire value chain. Fierce competition in this sector has ensured that most of the cost savings has been passed on to consumers in the form of lower prices.

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Quality consistency has also improved. Customers can depend upon the promises made being fulfilled. Choice has been increased as tour operators seek to offer a wide range of innovative holidays to consumers.

For companies

The larger companies thought that by growing geographically and integrating vertically they would reduce risks and increase profits. Smaller tour operators feared that the purchasing power of the larger companies and their own effective exclusion from distribution channels would make it impossible to compete.

The actual picture looks very different however. The larger companies have an in-built lack of flexibility, particularly on the airline side, and have found it difficult to cope with new circumstances. The smaller companies in contrast have been rapid and flexible in their responses. As a result all the major companies have had to significantly downgrade profit expectations over the past 18 months. There is no evidence that the biggest tour operators are able to wield market power, *i.e.* to raise prices and make unwarranted profits.

For suppliers

Fierce competition in the source markets in the originating countries has led to significant pressure on all parts of the value chain to deliver quality at lower prices. Wherever there is an excess supply of beds prices have been adjusted downwards. Where beds have been in short supply the response of hoteliers has been either to raise prices, at the risk of being uncompetitive, or an attempt to pass the risk of filling beds to the tour operator. Some hoteliers have combined these two approaches. In some cases accommodation owners have significantly updated their products to make them more desirable and competitive.

The contribution of innovation to survival and success

Leaving aside the social innovation of paid holidays, Europe's main integrated tour operators have relied on technological innovation for success. One of the main technological advances has been the advent of highly reliable and economical commercial jet aeroplanes for short haul travel, particularly Boeing 737s. Long haul flights became attractive once twin-engined planes demonstrated their ability to fly reliably across the seas for extended periods to overcome seasonality. These innovations reduced prices significantly, for example to the Caribbean from Europe with medium-sized aircraft (Boeing 757s & 767s). Further technological improvements in the efficiency of air travel are continuing to bring prices down. The

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other main external developments have been the huge technological advances in telecommunications and computers. Thanks to intelligent applications by certain companies based on this new technology it is now possible to keep track of millions of transactions and pieces of information at a reasonable cost. The Internet has allowed comparison of prices and information thus increasing transparency and transferring power to consumers, a development which is likely to reduce the sector's profitability over time.

Innovations in company structures have been aimed primarily at eliminating costs, as illustrated by the TUI structure.

There have been attempts to collaborate at the level of distribution, computer systems, air travel, health and safety and tools for sustainable development.

It has been argued at a recent World Travel and Tourism Council' Summit that polarisation is occurring in the middle market, which has so far been the main market for tour operators concerned with quality: a highly price sensitive segment on the one hand and on the other affluent clients for whom niche products must be developed. In addition he noted a significant increase in the desire of consumers to assemble their own package. Plans that will enable them to do just that are already at an advanced stage. In his view the classical tour operator is set to disappear.

As with Baumol[42] these examples show that innovation in products and processes is a routine part of corporate practice, particularly in the case of the vertically integrated tourism concerns and the companies that face fierce competition on which I have focused my attention. However, since these are not high-tech businesses the scope for innovation is rather limited and in any case the innovations are easy to copy. Is that why price competition and its impact on productivity has been the main concern of management in this sector for the past ten years, rather than product innovation?

But how much visible innovation capable of influencing the consumer has there really been in this sector? If one compares the brochures advertising Mediterranean beach holidays 20 years ago with those of today, it is immediately clear that the language is not the same and the photos are more honest... but what about the experience itself? Although the airport experience is definitely worse, on arrival at the hotel or apartment one can be more certain of consistent quality today. As for the destination, little has changed when it comes to the things to see and do or buy.

42. BAUMOL William, op.cit.

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There may be more restaurants and discos or opportunities for sailing and diving, but there is no real change at the level of such complementary products and services. The same can be said of skiing destinations, despite the introduction of snowboarding.

So clearly successful niche products have been developed to provide a satisfying tourism experience enjoying sun and sea, sailing, being entertained, learning, strolling, trekking, climbing, visiting people, resting and relaxing, playing games, eating and drinking, finding new thrills and excitement and so on. The products offer different levels of quality and comfort as well as exclusivity. They offer special facilities for different categories: singles, couples, families, and in the latter case for single families, young families or families with teenagers.

It is perhaps not surprising in such circumstances that tour operators look for new destinations in the developing world, which must of course offer the required level of safety. Increased variety together with lower prices is a sure way to attract consumers. Travel agents and tour operators however would like to see more innovation in destinations. To that end the Business Council of the World Tourism Organization is planning a new study on innovation. As well as entrepreneurship in information technology and capacity building, it will also look at public/private partnerships and other forms of collaboration necessary to engage these actors and secure the innovations.

What opportunities are there for improving productivity in tourism? Clearly they are fewer than in certain other sectors of the economy. Improving performance and technical skills through training is one possibility, but the hospitality sector tends to lose newly trained staff to other sectors offering lure higher rates of pay. A more promising area is the production and use of energy in tourism. We will no doubt continue to see reductions costs for aircraft purchases and operating costs – but these will benefit long haul rather than short haul traffic. Improving the travel experience at airports is critical as this is already affecting people's willingness to take short breaks. The terrorism threat has had a disastrous impact on an already bad situation. Innovative solutions must be found to deal with the terrorism threat wherever tourists are found -- at airports and in the air, in ground transportation, in hotels, at historic sites -- if we are ever to regain consumer confidence.

In conclusion, yes innovation is becoming a routine practice that can help companies to stay ahead of the competition. Equally important to meet the challenges of tourism today and find solutions satisfactory to all is active dialogue between the public and private sectors.

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CHAPTER 6. A DYNAMIC CONCEPTUAL APPROACH TO INNOVATION IN TOURISM

This text has been drafted by Xavier Decelle, Senior lecturer, Institute of Advanced Tourism Studies and Research, University of Paris 1 Panthéon-Sorbonne, France

Abstract

The importance of innovation has long been underestimated in the service sector. In contrast to the radical innovations vital for growth in manufacturing, in the service and particularly tourism innovation has played a secondary role and capital has been scarce. There has consequently been little government interest. This situation has changed with the emergence of new information and communication technologies (NICTs), which have had a major impact on tourism. There has been much research into the dissemination of new modes of production and the resulting organisational upheaval and marketing adjustments. But the information revolution has not been the only source of innovation in tourism, an area in which many other questions need to be addressed.

Methodology

This contribution is based on part of the 2002-2003 report to the National Tourism Board "Tourism and Innovation: Assessment and Outlook". Our method has been to:

- Examine statements made during interviews with tourism industry leaders in the light of recent theoretical findings on innovation in services.
- Assume a context of complexity: tourism products are composite goods.
- Take an approach that is comparative (at the industry level), multidisciplinary (at the academic level), and systemic (tourism's location-specific nature and government intervention are core considerations).
- Avoid the pitfalls of "common sense" and such myths as "the innate unproductiveness of service activities", "inability to innovate" ("Can one imagine a hotel-restaurant performing research?"), "low capital intensity", "inability to generate substantial productivity gains" or "low quality of jobs in tourism".

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Defining innovation

Innovation can be defined in many ways. Its leading theoretician, Joseph Schumpeter (1883-1950) had a broad vision of the concept, encompassing new products, new production processes, new markets, new raw materials and new forms of organisation. For Schumpeter the common thread between all these changes is that they involve "carrying out new combinations" which are qualitatively important and introduced by dynamic business leaders ("entrepreneurs"). There has been no major change linked to any particular theorist in the definition generally accepted today.

Today however we above all need to take into account the risky nature of the innovation process, and the fact that in the final analysis it is the consumer who will be the judge of the value it is supposed to create:

"…a process of creating new value … geared first towards customers, as the main arbiters of business competitiveness, but one that can also involve other stakeholders as major beneficiaries, such as the organisation itself (employees), shareholders (profitability), external partners, etc."[43]

Innovation does not mean creation ex nihilo

Innovation is not identical with creativity, which means the production of new ideas, new approaches and new inventions. Innovation is the application of such new and creative ideas and inventions. From this it follows that people and organisations may be innovators without being creators.

Innovation is the sum total of a social process which produces an invention that may or may not find a use. Since to be successful inventions must be adopted, the time lag between invention and innovation can be considerable. Such an invention may in fact involve only marginal changes. Does a thing have to be new at the level of a country to be accepted as "innovative"? Can the level be that of a market, or even just a firm? There seems to be agreement on this, least of all in the programmes of the European States. Innovation is indeed a "chaotic concept"!

43. [Translated from] Jean-Paul Flipo (2001), *Innovation dans les activités de service*, Éditions d'Organisation.

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Innovation does not necessarily mean progress (technical, economic or social)

Innovation imposes discontinuity, Schumpeter's "creative destruction". A product that brings greater satisfaction to the user or a process that improves the efficiency of a firm, will at the same time render an existing product or process obsolete. It therefore creates victims or, at the very least, readily appears as a threat to certain interests. The advent of superstores triggered the decline of small shops. New information and communication technologies disrupted the world of tourism distribution. Innovation in tourism impacts not only on competitors but also on territories, and it does not always advance the cause of sustainable tourism development!

Innovation does necessarily bring success

The job of an innovator is not like that of a manager, who according to traditional economic theory must concentrate on improving existing practices. An innovator must accept risk, and the more radical the innovation the greater the risk. Successful innovations are "the trees that hide the forest" of failures. Risk may act as a deterrent to innovation. But there is also risk in ***not*** innovating, such as falling technologically behind, losing ground to innovative competitors, inertia, and ultimately failure.

In the words of Bernard Bellon: "*Nine out of ten innovations are never completed, 99 out of 100 innovations serve no purpose. The one that succeeds makes the effort worthwhile*".[44]

Innovation in tourism and innovation in other service sectors

What is unique about innovation in tourism services?

Although innovation in tourism is more or less similar to innovation in any service industry, manufacturing models and even examples from agriculture can help us understand the process better.

- Comparing the approach to innovation in tourism and in other service industries such as retailing, banking and recreation.

44. [Translated from] Bernard Bellon (2002), *L'Innovation créatrice*, Economica.

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Tourism products are "experience goods" ***par excellence***, validated ***ex post facto*** by consumers. This is consistent with the trend towards "customisation" or "mass production of the made-to-measure"[45]. Tourism is spatially rooted, has a "heritage" background, attractions and some kind of accommodation. The sequential dimension of consumption affects the quality of the overall experience. Retailing can shed light on the manner in which tourism products are distributed and consumed. Tourism has features in common with cultural, sporting and recreational pursuits. Tourism and leisure activities are both subject to industrialisation. The influence of innovations in urban tourism on the supply of leisure activities (casinos, museums, special events, etc.) accentuates the convergence to the point where it becomes difficult to establish a clear boundary.

- Services differ from industrial models in various ways: marketing, the role of R&D, lack of patentability, responsiveness to markets, low technology content, etc. Innovation in services cannot be analysed in the same way as in manufacturing. Taking an evolutionist approach Keith Pavitt classifies service firms, and especially those performing services for individuals, as "supplier-dominated", and essentially users of technologies developed in the realm of manufacturing. Innovation tends to be non-technological, focusing on such areas as professional know-how, brands and design, which play a major role.

- The industrialisation of services and the impact of new information and communication technologies (NICTs) are making tourism more innovative. This can be seen from the preponderance of tourism services in electronic commerce.

- Classification of innovation in tourism.

  - Technological and non-technological

  - Product or process related, organisation or market related, ad hoc

  - Radical, incremental or architectural

45. BRESSAND Albert *et alia* (1988) *Les services au cœur de l'économie relationnelle.*

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Based on Schumpeter's idea of "creative destruction" the Abernathy-Clark model[46] involves a dual classification of innovations: degree of obsolescence of knowledge subsequent to an innovation, and degree of change in industrial linkages prompted by the innovations. This has been applied to tourism by Anne-Mette Hjalager (2002)[47]. It is worth noting that certain concepts do not have the same meaning for all authors, indicating that there is still room for research in this field.

Synthetic approach

The Barcet model[48] reflects a more synthetic vision of innovation. The author's model divides the sequential process (co-production) linking a customer and a service provider at four levels, from customer expectations to the means and resources deployed by the provider. This may be summarised as follows:

Levels 1 and 2 represent demand for services: innovation in the customer's system (beyond the providers' reach) and "product-service" innovation, the emphasis being on the customer's expectation of results.

Levels 3 and 4 represent supply of services: process innovation that is either internal or intended to alter the customer/service provider relationship, and innovations in means or resources, generally intended to rationalise internal operating conditions or to position a given service more strategically within total supply.

Zone 2, which is the overlap between supply and demand, constitutes the core for the construction of innovation.

The set of innovations instituted around a new air service such as Air France's shuttles can be represented as follows:

46. See graphic representation of the *Abernathy-Clark model* in: WEIERMAIR, Klaus (2004) *Product improvement or innovation: What is the key for success in Tourism?,* p.30, Figure 1.

47. HJALAGER, Anne-Mette (2002) *Repairing Innovation Defectiveness in Tourism.*

48. BARCET, André (1996) *Fondements culturels et organisationnels de l'innovation dans les services.*

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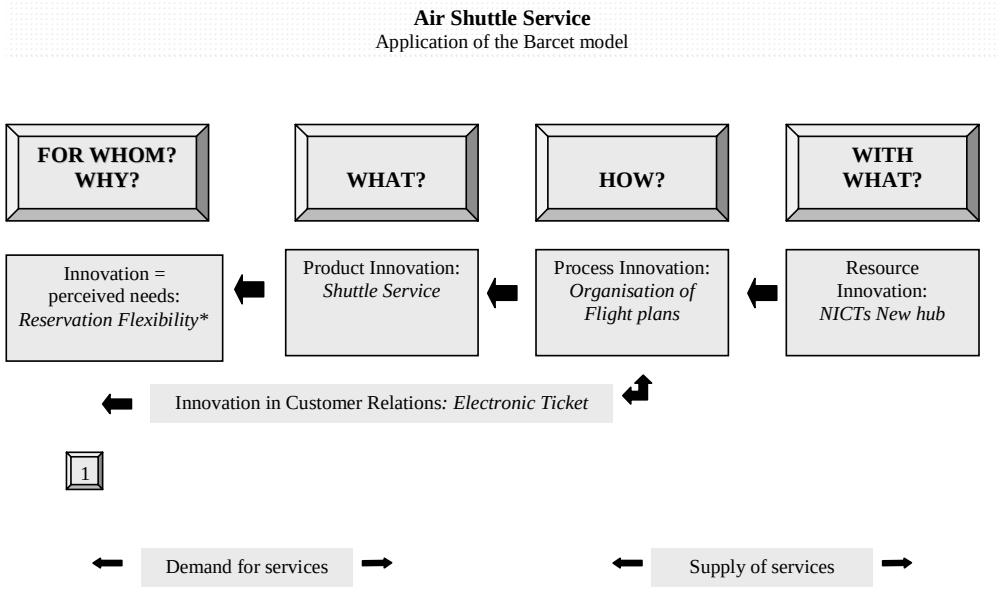
Figure 6.1 Application of the Barcet model

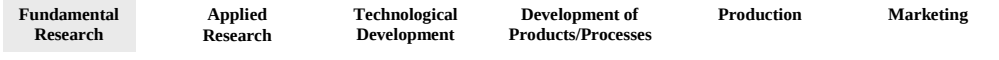


Source: Xavier Decelle.

The dynamics of innovation in tourism: which models?

The dynamics of innovation in tourism can also be interpreted using the innovation modelling efforts found in economic literature and management sciences. Modelling expresses a certain approach to innovation, the forms in which it evolves and the forces driving that change in a formal, simplified way. With no pretension of being exhaustive, one could cite:

Figure 6.2 Linear models



The (regular) linear perception of the dynamics of innovation is the oldest. It is the one that underlies Schumpeter's work. It proceeds directly from the invention to the marketing of the invention. This vision is consistent with a perception of progress (technical, economic and human) that is direct and irreversible. For

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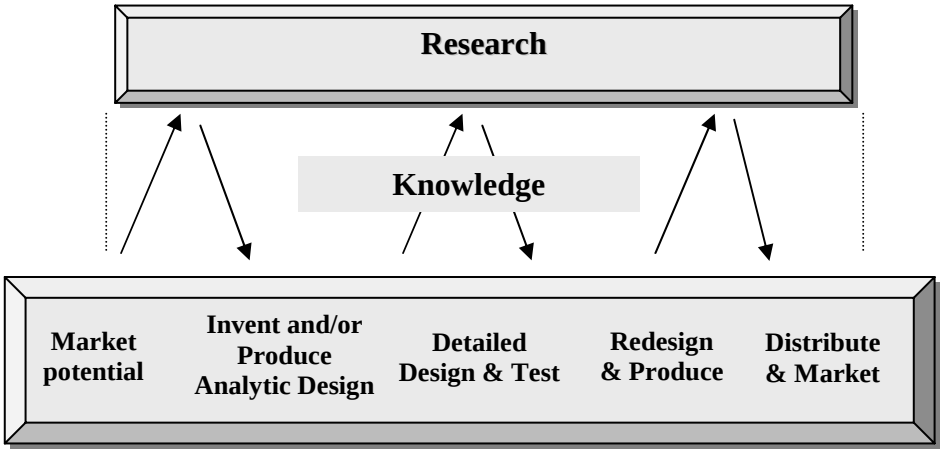
tourism, it can be used to understand the approaches taken to the dissemination of technological innovations imported from other sectors, such as NICTs.

Figure 6.3 Chain-linked models



Source: Kline, Steven J. and Nathan Rosenberg, *An Overview of Innovation*

Here, one-way causality ceases. These models show, first, that innovation appears as a "coupling phenomenon"[49] between technique and market, which operates in an interactive mode[50]. Second, this research shows that it is the progressive nature of innovation activities that dominates[51]. Demand-pull innovations, driven by new demand and expressing new needs, thus get better coverage here. We have already stressed the importance of these coupling phenomena in the transformations currently taking place in tourism.

49. FREEMAN, C. (1974) The Economics of Industrial Innovation. Harmondsworth: Penguin Books.

50. MOWERY, D. and ROSENBERG, N. (1979) The influence of market demand upon innovation: A critical review of some recent empirical studies, Research Policy 8, 102-153.

51. ROSENBERG, N. (1976) *Perspectives on Technology*. Cambridge University Press, Cambridge.

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Logistic models: life cycle

- Product cycle and cycle of dissemination of new tourism products:

  Reference to the product life cycle theory also enables the various phases in the dissemination cycle of new tourism products to be presented in a summary manner, along with their properties and a characterisation of the various segments of tourist industry supply.[52] As a rule, this dissemination does in fact follow a logistic curve with three phases:

  Incubation: small number of innovative firms, demand still virtual, innovators' rents.

  Take-off: extension of the market and the number of firms; possibilities for imitation ans difficulties for effectively protecting the innovator's intellectual property rights. As the market becomes more structured, segmentation, differentiation and branding strategies develop.

  At the end of the cycle, saturation expresses the limits of the market and the banalisation of the product; price competition and concentration movements.

  This modelling can also be used to specify the technical and economic "age" of such forms of tourism as rural, industrial and spatial tourism, etc. In addition, it is close to analyses of the life cycle of tourism destinations based on the approach of Butler (1980).

- The reverse cycle of Richard Barras: adoption of NICTs in tourism distribution:

  The impact of new technologies on services is a particular focus for the reverse cycle model of Richard Barras.[53] The application of NICTs to service activities can be understood from a cyclical standpoint:[54] at first, there is incremental process innovation intended to enhance the efficiency of a

52. CACCOMO, J-L., SOLONANDRASANA B. (2001), L'innovation dans l'industrie touristique, enjeux et stratégies.

53. BARRAS Richard (1986); *Towards a Theory of Innovation in Services*.

54. This is a cycle that is reversed in relation to the traditional view which postulates, initially, a radical (product or process) innovation that then generates incremental innovations.

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service by substituting capital for labour (*e.g.* automation of the back offices of tourism operators), and then an accumulation of knowledge and IT progress making radical process innovations possible that improve the quality of service (including front-office operations such as changes in reservations). Today, we would appear to have come to the third phase of the cycle, characterised by product innovations, the role played by network technologies and the domination of product differentiation strategies by firms in the sector.

Period	Nature of the innovation	Objective	Means	Example
1 ▼	Incremental process innovation	Productivity gains	Substitution of capital for labour *Agencies acquire IT equipment*	Back office automation
2 ▼	Radical process innovation	Improvement of service quality	Accumulation of competencies (IT)	Front office operations: reservations
3	Product innovation	Product differentiation	Network technologies	New on-line products: auctions, "last minute"

- Technological innovations, life cycles and competitive advantages – matrix of Air France strategies:

Company strategies can try to utilise their portfolio of competencies by combining their own positioning[55] on the innovative product market (via BCG Matrix, Figure 4)[56] with the life cycle of innovation. Given the latter's influence on competitive impact this can highlight appropriate strategies.

55. In a knowledge-based economy, this can incorporate recognition of accumulated competencies. TREMBLAY Pascal (1998), *Le nouvel âge du tourisme stratégique.*

56. Boston Consulting Group (1970) BCG Growth-Share Matrix; *A graphical approach to resource allocation within a multi-segmented corporation*.

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Table 6.1 Interpretation of Figure 6.4

Technological innovations	Strategies
NEW MOBILITY TECHNOLOGY: *"QUESTION MARK" TECHNOLOGICAL INNOVATIONS* Cutting-edge technological innovation at the research (launch) phase or being tried out by other industries, having uncertain but promising differentiation potential.	Invest cautiously if the technology meets the needs of Air France's customers. Develop partnerships with the new technology industry.
WEB SITE AND DERIVATIVE PRODUCTS: *"STAR" TECHNOLOGICAL INNOVATIONS* Cutting-edge technological innovation being tested (growth); potential for differentiation is great and will impact the company's future.	Step up penetration efforts: Air France site, Opodo site, Skyteam.
HUB: *"CASH COW" TECHNOLOGICAL INNOVATIONS* Key technological innovation being operated or in the maturity phase; strong competitive impact.	Develop the hub at Roissy-Charles de Gaulle Airport, captive clienteles (barriers to entry), international presence and consolidation of competitive advantages over other carriers and high-speed trains (TGV).
CONCORDE *"DOG" TECHNOLOGICAL INNOVATIONS* Basic technological innovation exploited extensively by the company and its competitors (decline phase); low competitive impact.	Keep Concorde because of the image associated with the company in terms of prestige and refinement or cease operations (the decision eventually taken).

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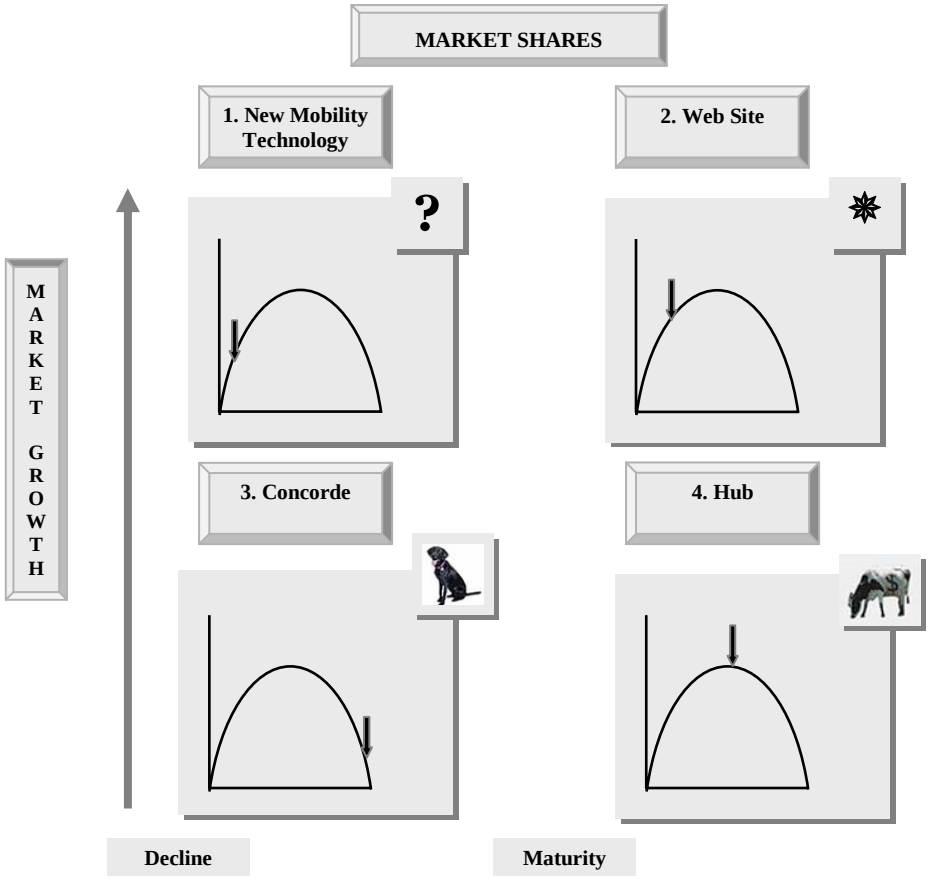
Figure 6.4. BCG Growth-Share Matrix



Source: Boston Consulting Group.

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Structural approach: the framework for innovation in tourism

From traditional tourism to "new tourism": a regulationist approach

	Heteronomy	**Autonomy**
Provision of simple services	**Fordist tourism** ▪ Evaluation of quality: price ▪ Form of uncertainty: quantifiable risk ▪ Competition: price-based *Stays in clubs, organised tours*	**Simple tourism** ▪ Evaluation of quality: conviviality and relationships ▪ Form of uncertainty: of little importance ▪ Competition: on prices and proposed attractions *Camping, family tourism, seaside holidays, rural tourism, etc.*
Provision of complex services	**Organised, customised tourism** ▪ Evaluation of quality: satisfaction of individual expectations, importance of service ▪ Form of uncertainty: uncertainty vis-à-vis others ▪ Competition: quality-based *Luxury cruises, sophisticated organised travel (high-end sporting stays).*	**Self-organised customised tourism** ▪ Form of uncertainty: radical ▪ Competition: on the basis of prices and originality of activities *Backpacking in off-beat locations*

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For industry operators, to what extent does the emergence of "new tourism" entails a shift in learning strategy from controlling productivity to better exploiting knowledge of demand?[57] Is not innovation in tourism based more on the objective of product differentiation[58] (non-price differentiation) than competition on price? Today there are many models of tourism practices superimposed one on another, with no clear model to follow. In offering their products, firms must adapt to the protean nature of tourism demand.

The tourism cluster: "co-opetition", social capital and externalities

Taking an approach like that of Michael E. Porter, we can look at clusters as a grouping of all of the firms and other elements that help make a region competitive, including the industries cited above, education and training facilities and infrastructure. A distinction can be made in tourism between geographical clusters (such as the French Riviera) and activity-based clusters (such as "green" tourism, wine-country tourism).

The emphasis is thus on a systemic dimension: complementarity, co-localisation, synergies and integration (networking). The cluster's virtuous operation suggests ability for operators to work together - what Porter calls "social glue", which corresponds more or less to Pierre Bourdieu's concept of "social capital". The market behaviours of operators illustrate the concept of "co-opetition" – a mixture of competition (at the marketing stage) and conduct of a more co-operative sort (at the production stage, and earlier at the innovation stage).

In tourism, small operators in particular are more sensitive to competition from their partners than to the benefits of working together. Most collaboration tends to involve destination marketing driven by the authorities.

In coming years the competitive advantages of firms will not be determined primarily by the efficiency of the production factors but by their ability to exploit the resources available in the cluster in which they operate. In addition to improving competitiveness, clusters play a major role in the ability of operators to innovate (lower experimentation costs, better visibility, better responsiveness to shifting

57. TREMBLAY, Pascal (1998) *Le nouvel âge du tourisme stratégique*.

58. The personalisation of service may even be taken so far as to provide regular customers with special treatment based on an information system for tracking and analysing their behaviour and preferences, such as at the Ritz-Carlton.

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demand). This is the motivation behind a genuine "national system for innovation in tourism".

Cognitive approach: innovation in tourism and the dynamics of knowledge

The "learning" tourism firm: evolutionary approach

One of the items on the agenda of evolutionary theory was to incorporate in economic theory the principles of biological evolution and natural selection. A distinction has to be made between codified knowledge -- which is formal, recognised, taught, explicit (technical, theoretical, managerial) -- and tacit knowledge, i.e. learning and know-how that can be spontaneously mobilised. Know-how and tacit knowledge dictate economic agents' responses. When well educated and trained, they delve spontaneously into the store of answers at their disposal to come up with the correct reply, without necessarily being able to explain either their choice or the particular know-how behind it.

The frameworks of evolutionary analysis

- Routines. These are the corporate equivalent to individual know-how. They stem from a whole series of learning processes including broad areas of tacit knowledge. Agents' behaviours are based on routines. Choices are limited by the ability to identify opportunities.

- Learning has a number of important characteristics:

  - It is cumulative and implies skills that are more organisational than individual.
  - It engenders knowledge that becomes part of organisational routines.
  - Routines are not transferable and are part of the firm's specific assets.[59]

Over and above the factors of production that they mobilize, firms differ by virtue of the nature of the know-how accumulated in implementing the said factors. Basically, it is know-how and organisational skills that distinguish one firm from another.

59. A good example of the idiosyncrasy of tacit knowledge is that of the inimitable quality of the violins made in Cremona in the early 18th century by a handful of instrument makers of undoubted genius, including Stradivarius.

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It is the nature of the skills accumulated in a firm and its ability to develop in-house the learning needed to continue to evolve in a changing environment that determine the path it will take.[60]

It is that specific path which explains any changes in the firm's principal activity. Examples of this include Preussag's move from heavy metalworking to tourism (TUI) and the penetration of the travel sector by the big mass marketing companies.

Insufficient production of tourism innovations: knowledge as a public good

If innovation is driven by codified knowledge, the latter tends to circulate freely. Similarly, in tourism, product innovation is visible and can be immediately imitated. This type of new knowledge is therefore what economists call a "public good", and we know from the work of Arrow that market mechanisms can only result in a sub-optimal level of innovation production in this context since innovators cannot keep the property rights to their innovations.

1. Insufficient tacit knowledge in tourism SMEs

Inadequate know-how and routine-driven innovations in small-to-medium-sized enterprises (SMEs) in tourism are shortcomings that justify stepping up the circulation of codified knowledge, which concerns all the institutions responsible for this function in the tourism system. The shortcoming in question reflects two separate problems:

- *The diffusion of a genuine entrepreneurial spirit and rigorous professionalism* in the tourism SME sector. It is certainly conceivable that the ability to innovate of entrepreneurs in this sector is affected by the increasing instability of their environment (bankruptcies, buyouts, NICTs, low barriers to entry, etc.). They may also suffer from a certain "limited rationality", preferring their activity's territorial and family roots to maximum profitability. Some indeed come from a traditional farming background (green tourism, camping and caravanning), small shops and craft trades. There have been some notable improvements thanks to the efforts of trade associations and the authorities, as well as the approach of a new generation.

60. CORIAT, B. & WEINSTEIN, O. (1995) *Les nouvelles théories de l'entreprise*, PUF.

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- *The mismatch between training and the jobs available in tourism* appears to be much more responsible for blocking the momentum of innovation than any supposed deficiency in the "human capital" of the firms.[61] Admittedly, as in other sectors such as BPW, SMEs in the tourism sector depend considerably on unskilled labour. A parliamentary report by A. Franco[62] (2003) points to many malfunctions: the lack of any real tourism content in training systems, jobs that lack appeal because of their resemblance to domestic work and to the leisure sector. Seasonal jobs often require no qualifications.

Furthermore, innovation in tourism tends to substitute capital for labour, rendering the skills of the labour force obsolete. Restaurant chains that use cold chain technologies for example, such as vacuum packing and pre-cooked products, rely less on the traditional skills of cooks. Such restaurants make intensive use of technological inputs from non-tourism industries.[63] The ensuing loss of know-how limits the internal opportunities for innovation.

2. Inadequate incentive mechanisms

This concerns both tourism operators and their employees:

- Operators exhibit three types of anti-innovative behaviour:

    - Since destination marketing is often supported by public bodies SMEs tend to take a "free rider" attitude to tourism innovation. Many fail to understand the need for the kind of co-operative behaviour that is crucial to the effectiveness of the tourism cluster.

61. The most common vacancies are for unskilled jobs. In the health care sector (HCR) a growing number of young people are now educated up to (BEP) -*Brevet d'études professionnelles*- and *baccalauréat* level, despite the fact that the vast majority of job offers are at level 5 (CAP) -*Certificat d'aptitude professionnelle*-. The composition of the jobs available is closely correlated to the either innovative or not, nature of the firm.

62. Mission undertaken by Arlette Franco, Member of Parliament for the Pyrénées-Orientales, May 2003.

63. HJALAGER, A.M., op. cit.

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- The increasing complexity of aids to innovation is causing the "transaction costs of innovation" to rise64 and discouraging many SME managers in tourism who are subject to routine management constraints.
- Risk aversion is also more marked among SME managers, who prefer to avoid risk rather than to manage it, even though managing risk is essential for innovation. Could the fabric of tourism SMEs be devoid of "Schumpeterian" entrepreneurs?[65]

– Employees may be discouraged from innovation by perceived job status, working conditions and pay:

- Status suffers from the seasonal nature of many jobs, multiple activities, insecurity, limited career prospects, and the perceived unlikelihood of being rewarded for efforts to innovate.
- Working conditions and pay largely explain why such jobs are unattractive. The problem of working hours in hotels and catering is well known, as is the low level of pay. As a result there is a substantial turnover of labour, which limits the opportunities for passing on tacit skills. Such conditions also explain the passiveness of employees, who have no incentive to take risks.

3. Channels for the transfer of knowledge in tourism

Since innovation in tourism is unlikely to qualify for protection by the intellectual property rights (patents) associated with industrial R&D, the channels for knowledge transfer are not the same (collaboration in fundamental research, laboratories). The role of trade and the institutional framework are vital (Figure 5).

64. I should like to thank Professor P. Keller for his comments on this question at the OECD Conference on Innovation and Growth in Tourism, Lugano, 18 September 2003.

65. Does this not confirm the correctness of Schumpeter's second model (in "Theory of Economic Development", 1942) in asserting that the structure of monopolistic markets is more conducive to innovation, thanks to the scale of the monopoly rents, than the fragmented structure in which SMEs exhaust themselves in ruinous price wars?

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As well as the ability to derive new knowledge from in-house activities (learning by doing) it is important to consider a tourism firm's ability to:

- Acquire and absorb existing innovations, "internalise" knowledge that is codified and convert it into tacit know-how or routines[66] (this illustrates the relevance of Solow's paradox to tourism[67]).
- Disseminate its innovations, *i.e.* externalise them in the form of codified knowledge that can be more easily circulated.

This ability depends on structural factors: the size of the firm[68], type of organisation (see Chandler) and whether or not it belongs to a group. On this point it seems clear that hotels, which are part of an integrated or voluntary chain, have a much stronger propensity to innovate, with central management playing a vital role. However, it is the cognitive factors that would appear to be crucial: the proactive or reactive nature of routines, managerial skills (knowledge management) and wage skills (qualifications, interaction, etc.).

The role of the national system of tourism innovation is also essential in at least four ways:

- Development of research, quality of training[69].
- Tourism policy and the efforts of such institutions ad the French Agency for Tourism Engineering and the departmental and regional tourism committees.
- Direct production of innovation by public operators (carriers, the authorities) using government funds and substantial human capital.
- Indirect dissemination (percolation) by means of incentives (tax exemption) and assistance (subsidies).

66. BAKER, M. et al. (1998) *The productivity paradox and the hospitality industry*, School of Management Studies, University of Surrey, UK: "The impact of investment in NICTs on the performance of the hotel and catering sector under consideration is correlated with the level of management skills, particularly skill in setting up and managing information processing systems".

67. R. Solow, winner of the Nobel Prize for economics, said in 1987: "You can see computers everywhere, except in productivity figures", putting into perspective the hopes placed in the technological revolution.

68. The relative ability to innovate of SMEs and larger organizations has been a matter of controversy from the time of Schumpeter.

69. A reference to the hoped-for impact of the new BTS in tourism in France.

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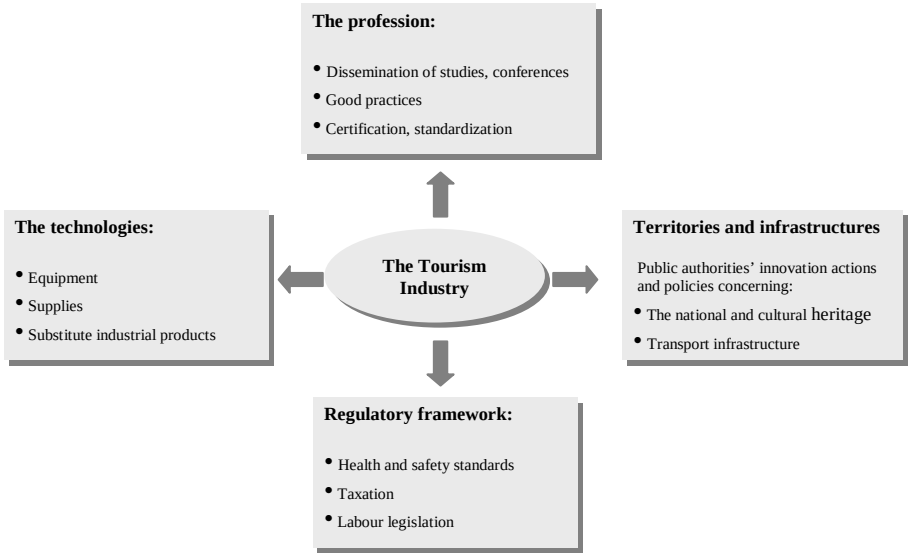
Figure 6.5. Channels of knowledge transfer in tourism



Source: A-M Hjalager

Conclusions

The success of innovation promotion in tourism will require efforts to overcome the obstacles referred to in this study. The public authorities and other tourism stakeholders can contribute in the following ways:

- Improving the internal dynamics of innovation by making companies adopt a proactive attitude, putting more emphasis on economic intelligence rather than simply monitoring changes in technology.

- Improving the efficiency of the national system of innovation, and specifically:

  - The training of operators, staff (see recommendations of the Franco report).

  - Developing the role of public and private actors, strengthening the French Agency for Tourism Engineering and regionalising its efforts.

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  - Stimulating research and creating a genuine French-speaking, multi-disciplinary network.

- Improving incentives for operators and employees.

- Maintaining the coherence of the tourism industry and its linkage with society as a whole: innovation in tourism is not possible without mobilisation of the population, and in particular cultivation of the fundamental values of hospitality.

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PART IV. INITIATIVES ENHANCING INNOVATION IN TOURISM

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CHAPTER 7. THE FRENCH INITIATIVE FOR INNOVATION IN TOURISM: HOW TO REJUVENATE SUPPLY AND INCREASE THE PRODUCTIVITY OF THE TOURISM SECTOR?

This text has been drafted by Mr. André-Jean Guerin, Former Director of the French Agency for Tourism Engineering

Abstract

This paper is divided into three sections. The first examines the forms of innovation in tourism through two main questions: what innovation in tourism is? and which innovations have brought genuine changes to this sector? The second section describes undertakings in the public sector. The third part looks at structures, agencies and networks designed specifically to support innovation and exchange of experiences.

What does innovation look like in tourism? Some noteworthy examples.

In his latest book, Marc Boyer[70] begins his chapter on the history of tourism in France by mentioning four dates:

- 1741: Publication of "Relation of a journey to the glaciers of Chamouni" by Windham and Pococke.
- 1838: Publication of "Memoirs of a tourist" by Stendhal.
- 1936: Act on paid holidays.
- 1950: Club Mediterrannée opens its first village.

70. BOYER, Marc (2003) *Le tourisme en France (vade mecum)*, COLOMBELLES : Editions Management et Société.

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The history of tourism in France obviously cannot be summed up by these four dates alone. Other milestones that deserve a mention are:

- 1492: Besides the discovery of America, this was also the year in which Charles VIII climbed the Mont Aiguille in the Dauphiné, a first in the development of mountaineering.
- 1552: Charles Estienne publishes the first portable guide for travellers on the roads of France .
- 1747: Briseux publishes the "Art de bâtir des maisons de campagne" (how to create a country home).
- 1763-1765: Dr. Tobias Smollett sojourns in Nice, where a street still bears his name, and writes his "Letters to Nice".
- 1779-1796: Horace-Bénédict de Saussure, «Voyages dans les Alpes», 4 volumes.
- 1787: de Saussure climbs Mont Blanc after having encouraged and rewarded the first ascension by Jacques Balmat and Dr. Michel Paccard.
- 1822: First seaside resorts in France established in Dieppe, Boulogne, etc..
- 1850-1860: Construction of major railway networks.
- 1852: Decree on traffic police, subsequently applied to bicycles and the first "touring cars".
- 1863: Creation of Monte Carlo and its casino.
- 1867: First music festival organised in Orange (Les Chorégies).
- 1889: First tourist office opens in Grenoble..
- 1900: Publication of the first edition of Michelin Guides.
- 1910: Creation of the French National Tourist Office.
- 1919: Acts of 14 March and 24 September on the classification of spas and tourist resorts.
- 1935: Act of 19 November establishing the Commissariat Général au Tourisme (French Tourism Commission).
- 1946: First post-war automobile salon and launch of the Renault 4 CV (La bombe).

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A further example is the changing perception of mountains and their use. Mountains, originally seen as forbidding places, were often abandoned by their inhabitants and avoided by travellers. In the middle of the 18th century the perception changed and in the spotlight of the Romantic Movement they eventually came to be regarded as "sublime". Mountain climbers, initially from Britain, sought to conquer the summits and those who had successfully achieved celebrity.

In the past few centuries, new practices in tourism have always been pioneered by people with strong personalities, whose social position often placed them above the conventional customs and practices of their time, who commanded substantial financial resources, and who in many cases were part of a circle that has access to the highest levels of government. I refer in particular to those adventurous aristocrats who were eventually imitated by their royal masters. They gave way to the stars of show business that in turn were admired and imitated by the upper middle classes. In our more democratic era tourism became accessible to the masses. Innovations in tourism begin as cultural developments before becoming social phenomena. The authorities have always been involved in this process, at first through the behaviour of those in the highest positions, and subsequently through government's role as the regulator of economic processes including tourism.

French initiatives and programmes

France has achieved enviable results in tourism, including the number of international visitors it attracts (77 million), the scale of consumption recorded by its Tourism Satellite Account (EUR 101 billion) and a comfortable surplus in the tourism balance of payments (EUR 15 billion). This success has been achieved despite the fact that public funding for tourism is particularly low in France. Out of a budget of EUR 273 billion, the French government earmarks a mere EUR 75 million for the French State Secretariat for Tourism. Is this false modesty on the part of France? Does France take an ironic view of tourism? Are we showing disdain for the tourists who set their sights on visiting France, and for the associated buying power?

Let us briefly focus our attention on French efforts to support the development of tourism at all levels, i.e. central government, the regions, the departments and local authorities.

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Government determines the framework in which tourism must operate

The State is responsible for ensuring a peaceful society, individual freedom, the rule of law, security in terms of food and health, reliable public services, etc. This general framework is important for the development of tourism.

The State provides the legislative and regulatory framework for all activities including tourism.

- The classification of tourist resorts – which as we have seen dates back to 1919 – has a number of implications. A classified commune has certain privileges, notably with regard to complementary funding allocations. Local officials pay great attention to classification procedures and their implementation. Working groups made up of elected officials and local and national civil servants are currently discussing ways to improve the legal basis, an Act that is almost 100 years old. This is important since classified communes attract the largest number of tourists.

- France has a three-tier classification for accommodation: hotels, holiday rentals and camping sites. There is a similar classification system for tourist offices. French systems seem to be the object of envy in certain quarters. However, in the hands of government officials they can prove cumbersome and remote from the situation on the ground. A second stage of decentralisation measures, in the context of major reforms pursued by the government, requires transferring responsibility for classification to more local bodies and in the case of tourist accommodation, to the *departments*.

- The Act of 23 December 1992 divides institutional responsibilities in tourism between central government, the regions, departments and local authorities. The regions, which are responsible for planning, set medium-term objectives for tourism development. They draw up a regional tourism development plan and establish the procedures for meeting its objectives. Each department is free to draw up its own plan for the development of tourism and leisure activities, but these must be based on the regional guidelines.

- Tourism is a service sector activity and thus labour intensive. This is not a bad thing in the current situation of relatively sluggish economic growth, since it is one the few sectors in France still able to create jobs. However its seasonal nature is a limitation that tends to make these jobs less attractive.

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This is unfortunate since the quality of the welcome given to tourists depends on the attractiveness of jobs in the tourism sector and the professionalism of staff. Over the past few years, new legal and social provisions have attempted to resolve this dilemma and improve the working environment as well as the security and "sustainability" of jobs in tourism, particularly for seasonal workers. The measures taken include a new employment contract for seasonal workers, the development of employers' groups, better access to training and recognition of the skills acquired, improvement of medical care, various allocations and particularly housing benefits in line with the European network of housing for seasonal workers, with union representation. A recent meeting of the Interministerial Tourism Committee added a fundamentally new dimension, requiring that a given percentage of new or renovated tourist accommodation granted tax benefits be reserved for seasonal workers.

The public authorities provide infrastructure

There can be no tourism without people who spend a night away from home. Consequently, there can be no tourism without transports. There is surely no need to recall the role played by the State and territorial authorities in the construction and maintenance of transport infrastructure. France's infrastructure includes ports and inland waterways, a national railway network, airports and, of course, roads including a dense network of motorways. Several large and costly motorways have been built in France to provide tourists with access to the Alps or the Massif Central. A major effort has also been made to equip France with high-speed trains, the celebrated *TGV*. Less well known is the role the regions play in the organisation of public bus and train services. Paris is Europe's leading tourist port, a fact that justifies the major programme of work currently being carried out in the Seine – upstream and downstream from Paris as well as within the conurbation. This programme, due to be completed in 2007, will bring about considerable improvements in fluvial passenger transport.

Lets us now consider what is usually taken for granted and therefore remains invisible. No holiday, tourist accommodation or tourist attraction would be possible without the availability of basic public services such as the supply of drinking water and wastewater disposal, electricity and gas supplies, postal services and telecommunications. The French authorities have done their best to provide the necessary infrastructure to all inhabitants. This has naturally benefited summer visitors, holidaymakers, owners of weekend homes and tourists of all kinds.

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Besides infrastructure the authorities at all levels have been involved in providing tourism superstructures on a massive scale. The high ranking our country has achieved for the number of visitors to winter sports facilities is largely attributable to the "Snow Plan" of the 1960s and 1970s. During these two decades the French government helped the departments in mountain areas to develop new facilities for all major ski resorts. Similar efforts have been made to help tourism along the coasts of the Languedoc and Aquitaine regions as well as in Corsica.

Currently French authorities at all levels are collaborating in the development of high-speed digital communications infrastructure and completion of the national cell phone network. This is a powerful incentive for the development of new personal services and particularly those directed at tourists such as Internet information and booking services, geopositioning, information about local services and electronic guides.

The public authorities encourage innovation, research and development

If we were to limit ourselves to technological developments uniquely relevant to tourism we would find the going difficult. If on the other hand we take a broader view and include research and innovations that affect tourism more or less directly, then we shall find no shortage of examples.

High-level sports are a major stimulus for applied research, leading to innovations that are rapidly adopted by manufacturers of products for leisure activities and tourism including clothing and particularly outdoor apparel, and equipment ranging from skis to pleasure boats, recreational vehicles, and a host of other items too numerous to mention.

Aeronautical research is another field that one does not immediately think of as a source of tourism development. And yet tourism has been one of the main beneficiaries.

Another important source is agro-food R&D. Thirty years ago the *rosé* wines of Provence that are so popular today did not even exist. People like to visit places known for their wines, cheeses and other products. The famous "AOC"[71] labels guaranteeing a wine's true origin are the result of a marriage between tradition and modern quality assurance. Agro-food technology in such areas as the cold chain and

71. Appellation of Origin.

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processed products has also improved competitiveness in one of tourism's core sectors, catering, helping it to keep pace with modern lifestyles.

The public authorities provide natural and cultural resources

The importance of the attractiveness factor in tourism is illustrated by a survey carried out by the CREDOC[72] for the Tourism Directorate in 1996. It found that 38.9 per cent of repeat visitors to seaside resorts, and 33.4 per cent of frequent visitors to the mountains cited the beauty of the local natural surroundings as the main reason for their loyalty.

The French Conservatory for Coastal Areas and Lake Shores (*Conservatoire de l'Espace Littoral et des Rivages Lacustres*) was created in 1975. At present it owns 68 000 hectares of natural area and controls 861 kilometres of lakeshore at 500 sites. In 1986, the Coastal Areas Act marked a major milestone in a national policy adopted in the 1970s, aimed at controlling urban development on France's coastlines. Thanks to this law tourist facilities built with "one foot in the water" have been kept to a strict minimum.

France's first national park, the *Vanoise*, dates back to 1963. Today there are seven national parks and several more are planned. A network of 40 regional nature parks completes the system for the protection of large natural areas. In 1985 the Mountain Areas Act restricted development in fragile mountain environments, particularly for tourism facilities. Also worth mentioning is the NATURA 2000 network covering around 15 per cent of France, incorporating ecological measures designed to protect fauna and flora of all kinds and their biotopes.

A tax that contributes to protect vulnerable natural areas is another key measure. Departments that choose to levy this tax take a percentage of the duties payable on new constructions. The proceeds are used for the purchase, rehabilitation, maintenance and management of vulnerable natural areas for public use. Between 1990 and 2001 this tax rose between EUR 700 and 800 million.

An area in which the authorities at all levels also play a key role is that of protection of France's cultural heritage. As this is so closely related to the very strong French sense of identity as to be almost self evident, I shall not dwell on it here.

72. Centre de Recherche, d'Études et de Documentation sur la Consommation.

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One aspect of the protection of natural and cultural resources that does deserve mentioning is the promotion of tourism in areas facing economic difficulties, a field in which tourism development and regional development go hand in hand. So-called "Rural Revitalisation Zones" are numerous throughout France and include many urban areas. Tax benefits are granted to the owners and operators of tourist accommodation facilities within these zones. One of the many beneficiaries is the company *Pierre et Vacances*.

Instruments for shaping national tourism supply

The example of agricultural development in France

First a slight detour into agricultural development in France. This sector currently includes nearly 700 000 farms, employs approximately 1 million people and generates value-added of EUR 32 billion, accounting for 2 per cent of gross national product.

Agricultural development is based on a technological and financial system dating back to 1947 but recently revised. The aim is to support individual farmers and in particular to assist in finding solutions to technical problems and with investment in "optimisation".

This system works through chambers of agriculture in each department, producers associations, cooperatives and various technical institutes. Expertise is provided by 7 000 engineers, technicians and advisors, plus a similar number of researchers, both public and private.

It was recently decided to make agricultural enterprises pay a special tax on their annual income towards development in this sector, and this is expected to generate EUR 90 million to help consolidate national programmes.

Resources will thus be pooled on a nationwide basis so that various local professional associations can finance projects that offer both professional and social benefits while assisting individual entrepreneurs, particularly young farmers just starting out.

What support is available for tourism development?

159 chambers of commerce and industry, as well as 20 regional chambers, grouped together in the Federation of French Chambers of Commerce and Industry, provide professional assistance. In 2001 these chambers had total income of

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EUR 3.4 billion, mainly coming from tax revenue. They have a wide range of activities including the management of infrastructures such as ports, airports, conference facilities, etc. Although this leaves them few resources to devote to small tourism firms they are nonetheless instrumental in the development of hotels and restaurants as well as leisure and tourism services.

Tourism promotion is also in the hands of tourist offices operated by local authorities, tourism committees at the departmental level run by general councils, and regional tourism committees run by the regional councils. Few tourism offices are involved in development policies that require special know-how and consultancy services, except in the large cities. There is little involvement at the departmental or regional tourism committee levels. Authorities are currently debating whether or not it is time to provide such resources internally.

Support is provided at the national level by the following:

- A specialised office in the Tourism Directorate commissions and distributes studies.
- The French National Tourism Observatory, administered by the State Secretariat for Tourism, publishes statistical studies and carries out studies and analyses in partnership with tourism professionals and local operators.
- The Mountain Tourism Development and Studies Service provides support for central government and local authorities, particularly for the development of winter tourism activities.
- The French Agency for Tourism Engineering, which is discussed in greater detail below.

French Agency for Tourism Engineering

This national agency, administered by the State Secretariat for Tourism, celebrated its tenth anniversary in 2003. It is the direct successor of the French Tourism Studies and Development Service created in the 1960s to advise the government on economic initiatives as well as regional and tourism development. Its structure has been adapted to today's more decentralised approach to tourism promotion, in accordance with the principle of subsidiarity. The following will help to understand its *modus operandi*:

- Studies on markets, customer bases, behaviour, trends based on an approach which is more European and global than specifically French.

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- Coordination designed to enable local authorities to access information on initiatives and projects elsewhere in France and in competing countries, enabling them to develop better solutions.
- Interdisciplinary expertise and advice based on an array of skills beyond the scope of any single region or profession, making it possible to assemble a complex supply of tourism products combining both private and public sector services.
- Efforts to improve professional standards in the fragmented field of tourism engineering (most design bureaux have no more than one or two employees).

The Agency's decision-making bodies include representatives from all branches of the tourism sector, and notably from central government, other authorities at all levels, professional tourism federations, public institutions, private enterprises, and so on.

The French Agency for Tourism Engineering undertakes new initiatives every year in the following areas:

- Analysis of general statistics.
- Understanding customer bases and activities.
- Public management of tourism.
- Development of tourism projects.
- Marketing of tourism products and services.
- Quality of products and services.
- Assessment.

The Agency also provides expertise and advice in all these areas:

- Maintains surveillance.
- Initiates studies.
- Updates databases.
- Advises tourist operators.
- Publishes documents.
- Organises technical seminars and training.

The Agency operates on a partnership basis and maintains close relations with various networks including:

- Consultancies, particularly those relating to private tourism engineering.

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- Regional tourism committees.
- Departmental tourism committees.
- "Classified" communes.
- The French Federation of Chambers of Commerce and Industry.

In its first decade of life the French Agency for Tourism Engineering has established itself as an essential reference point for all actors involved in the supply of tourism goods and services, recognised for its professionalism, its locomotive role in this sector, its efforts to stimulate innovation, and its encouragement of exchanges of information and experience.

The Agency above all helps to develop French tourism goods and services that meet state-of-the-art requirements at the national and international level. It does this with a staff of about 50 employees, equivalent to 40 full-time posts. Its annual budget is around EUR 4.5 million.

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CHAPTER 8. INNOVATION IN THE FIELD OF MARKET COMMUNICATION AND MARKETING: THE AUSTRALIAN INITIATIVE

This text has been drafted by Bob Pegler, Former Minister-Counsellor at the Permanent Delegation of Australia to the OECD

Abstract

In the last two decades, the Australian tourism industry has grown from a fledgling sector to a major industry. However, tourism has experienced difficult and challenging times of late. In the past 10 years the tourism industry has faced the change of consumer demand and demographics, increased competition and unstable global geopolitics. This paper examines the current challenges and barriers faced by the Australian tourism industry and attempt to reveal its innovative approach to cope with these recent challenges and barriers.

Marketing Australia

Outlook of tourism market

In the past two years tourism globally has been impacted by an overall weak economy combined with a series of shocks, which began with September 11. The uncertainty of the global environment continued this year with the war in Iraq, the SARS outbreak and ongoing terrorism threats. World passenger figures last year (2002) show an increase of 3.1 per cent to over 700 million passengers despite the difficult climate. What the figures don't reveal is the changes that have resulted from the challenging environment.

According to the World Tourism Organisation the main changes are that consumers now give preference to destinations closer to home, taking a 'wait-and-see" approach to travel plans, and leaving bookings to the last minute. However, the UNWTO[73] notes that some products and sectors have been more resilient and others

73. World Tourism Organisation.

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have even benefited. These include non-hotel accommodation such as apartments, and B&Bs, and special interest trips with high motivation factors related to culture, sports or visits to family and friends. Long haul destinations have been most affected by these trends. Short-haul travel is expected to enjoy comparatively stronger growth. Overall it is likely that year on year growth will be between 2 and 5 per cent. Globally, there will continue to be a strong desire for travel and there will be pent up demand for long haul destinations including Australia.

Forecasting key market trends

International tourism is one of Australia's most valuable industries, contributing AUD 17.1 billion to the economy annually. Over the past two decades inbound tourism has been a stellar performer with average annual growth of 8.5 per cent. However, in the past two years inbound tourism has seen two consecutive years of flat performance - with 1.5 per cent decline in arrivals in 2001 and 0.7 per cent decline for 2002. It now faces a third year of negative or flat growth. Australia's recovery from the recent decline due to SARS is already underway, but greater efforts are required in a number of markets. There are indications for example that people from a number of markets such as the United Kingdom are travelling again in increasing numbers.

Challenges

A lot has happened over the last couple of years to change the operating environment. The global travel industry is reeling under the impact, and the task of selling a destination is a difficult one.

The changing consumer

A major area of change is the consumer. In the past 10 years holiday and work patterns and people's shopping habits have changed. Work/leisure shifts, globalisation and technology are key factors, which will affect future holiday profiles. Tomorrow travel will not be about the destination but about experiences tailor-made for the traveller. This will create new demand, reflecting a desire for authenticity, for instant gratification, self-fulfilment and possibly a blending of business and leisure travel. Tourism market trends in Canada for example show a growing market for women-only travel experiences.

Over the past year the Australian Tourist Commission (ATC) has launched a project to develop medium and long-term industry models. One of the consequences of reduced consumer confidence towards long haul travel in these uncertain times is

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the switch to short haul destinations. Current trends -- staying closer to home, taking shorter holidays -- represent another challenge for a long haul destination like Australia.

Demographic change will be a huge factor in the industry's future in the next decade. Australia has great potential with the over 50s segment, particularly from Japan (Table 8.1), and will need to refresh and represent the product to capitalise on this growing market of retiring baby boomers. This segment is looking for rejuvenation, learning and fulfilment. There are some real business opportunities here for suppliers.

Table 8.1. The Ageing Consumer (Median Age of Population*)

	2000	2005
Japan	41.3	53.2
Asia	26.1	38.7
Europe	37.7	47.7
North America	35.4	40.2
Oceania	30.7	39.9

* The median age in a number of major markets will be between 45 and 55 years by 2050. Japan, currently has the oldest population in the world with a median age of 41.3 years. The median age is expected to be 53.2 year by 2050.

Source: Australia Tourism Commission.

Changes in consumer demographics will require operators to be smarter, more selective and ready to tap into the needs of individual travellers. Micro-segmentation of the key travel markets Australia targets will make it possible to focus on and develop experiences to suit the needs of the discerning new consumer.

At the same time there have been changes in how consumers plan and book their travel. Increasingly, new technology is playing a greater role in how consumers plan and even purchase their travel.

More consumers are opting to travel independently rather than as part of an organised group tour.

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Barriers to travel

Despite being one of the most desirable destinations in the world, Australia faces a few image problems, which act as barriers. Research shows that consumers in a number of markets view Australia as costly, too far away, offering too much to see and do in just a two week holiday. Moreover since we're also seen as good environmental citizens who take care of our natural wonders, potential travellers feel no sense of urgency to visit, on the understanding that: "Australia will always be there".

Aviation, which is the lifeline for Australian tourism, has been experiencing turbulence since September 11. Recent world events have seen conditions worsen and this is reflected in the bottom lines of the world's major carriers. There has also been transferral of profits from the traditional full service carriers towards the new Value Based Airline (VBA).

Australia too has been impacted, with a number of players exiting the market and those who remain reducing services. Preliminary traffic figures (IATA) for June 2003 show an 11.8 per cent drop in international passenger traffic over June 2002, with SARS-hit Asia-Pacific carriers experiencing a 35.8 per cent drop. Even so this is a considerable improvement compared to the 21 per cent and 55 per cent reductions recorded respectively for May. Capacity cuts in Asia Pacific region (-27.2 per cent) and North America (-12.5 per cent) passenger services helped to bring the industry-wide load factor to a more normal level of 73.7 per cent, from the 65.0 per cent low recorded for May. Load factors out of the United States have been as high as 90 per cent in some months, resulting in a serious shortage of seats.

Recovery in the coming months depends on capacity being restored. Already we have seen heavy discounting on some routes to drive a quick recovery in passenger traffic. Overall the aviation sector is picking up traffic from consumers that may have deferred travel as a result of the war in Iraq and SARS. Growth in capacity has been particularly instrumental in helping the number of visitors from the United Kingdom and Germany to recover.

Since the events of September 11 the ongoing threat of terrorism has made consumers worldwide more concerned about personal security and safety, and this has impacted on travel. The recent bombing of the Marriott in Indonesia has again brought concerns about the links between travel and terrorism to the forefront. The Australian Government has implemented a number of security initiatives to ensure that Australia will remain a safe destination.

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Increased competition/costs

Global events in the last two years have caused a massive crisis of confidence and impacted on travel worldwide. There are now 175 National Tourist Offices competing for a share of the international travel market. Competition for inbound tourists has intensified and a number of Australia's competitors are pouring more money into marketing programmes to increase market share.

Not only is more money being allocated, but competition is getting smarter. International tourism marketing is becoming increasingly sophisticated with many destination offices now combing their efforts. Media costs in some of Australia's major markets are so high that TV advertising isn't possible. The affordability of media space is another problem, particularly in Japan and the United States. The cost of a 30-second ad on a popular NBC TV show in the United States -- Australia's 4th largest market -- is USD 500 000, an entire week's budget. Australia can comfortably launch a full TV campaign in New Zealand, but can no longer afford this in many other markets.

So we have to look at other media, and innovative approaches. Australia hopes to work with partners, such as Japan Airlines, in these markets, to boost spending.

Australia's innovative approach

To overcome these barriers we must develop a smarter marketing approach, strive for innovation and develop unique marketing activities. ATC, the Australian Government agency charged with promoting Australia, is represented in 20 countries around the globe. It is more than an advertising agency. Building the awareness of Australia as a tourist destination is important, but there are many other programmes that address the complexities of marketing Australia. The integrated approach adopted focuses on both the consumer and the travel trade.

Establishment of strategic direction

All ATC marketing activities are driven by understanding and insight into the markets and consumers targeted. Key activities include the Visiting Journalist Program, direct marketing, online marketing via Australia.com, celebrity endorsements, consumer and trade promotions, Aussie Specialist Program[74] and trade events.

74. www.tourism.australia.com/Marketing.asp?sub=0399

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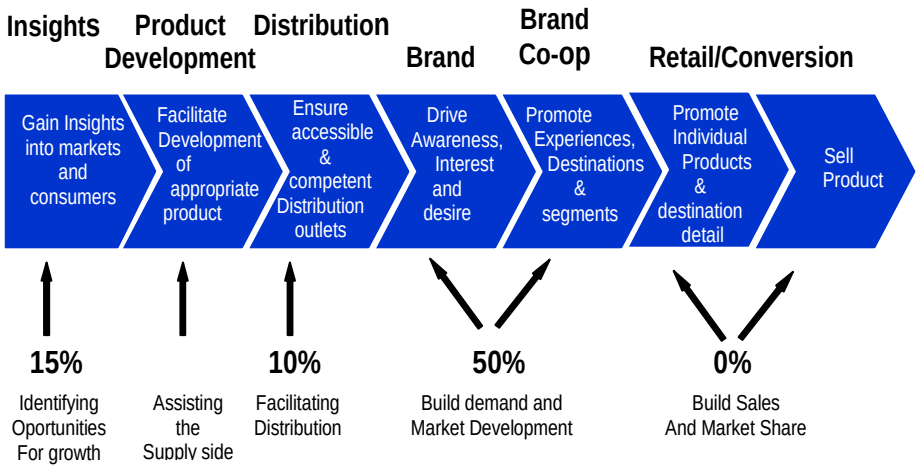
Australia was the first destination to build an international brand image, when the ATC launched "Brand Australia"[75] in 1996. Brand Australia highlights the spectacular natural environment, the distinctive personality of the Australian people and the free spirited nature of lifestyle and culture. Since its inception this powerful brand has been shaping a unique global image of Australia as a world-class tourist destination (Figure 8.2).

Figure 8.2. ATC Strategic Direction [76]



Source: Australia Tourism Commission.

During the Sydney 2000 Olympics awareness of Brand Australia was at an all time high. After the games the focus shifted to partnership marketing. Recently however it was decided that the current Brand Australia was no longer as relevant and needed refreshing. The ATC is currently working on this and trying to better differentiate Australia from its competitors. The aim will be to deliver a core message that will be compelling and uniquely Australian.

The ATC focuses its efforts on markets that offer the best opportunities, with activities in 20 countries (Table 8.2).

75. www.tourism.australia.com/Marketing.asp?sub=0291

76. www.atc.australia.com

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Table 8.2. Focusing the efforts

STRATEGIC POSITIONING	UNDERSTANDING AND INSIGHTS	FOCUS	SYNERGY AND LEVERAGE
MAXIMISE YIELD AND VISITATION POTENTIAL		USA	UK China
ENCOURAGE GROWTH POTENTIAL	Germany	Singapore Korea	Japan New Zealand Canada
MAINTAIN, SUPPORT AND DEVELOP	Italy	Ireland France India Hong Kong, China	Middle East
LIMIT TO SUPPORTING INDUSTRY INITIATIVES		Switzerland Netherlands Malaysia Thailand Chinese Taipei	
PROVIDE STRATEGIC SUPPORT AS REQUIRED		Latin America Sweden Denmark Philippines South Africa Indonesia	

Source: Australia Tourism Commission.

Tourism Ambassador Program

The Ambassador Program is an initiative that the ATC implemented last year, using high profile Australians to recommend the country as a desirable tourist destination. The concept has paid dividends.

Swimming champion Ian Thorpe was the first, becoming Australia's Holiday Ambassador to Japan. This was a great success in Japan, generating AUD 20 million in publicity. This year two more Ambassadors were announced. Supermodel Megan Gale was named Australia's first Tourism Ambassador to Italy. Her endorsement will significantly boost Australia's profile with Italian travellers. Australia's five-time world champion surfer Layne Beachley was appointed Tourism Ambassador for the Youth market. The Tourism Ambassador Program is one way to cost-effectively communicate the essence of Brand Australia to the consumer. But of course all Australians can be ambassadors for their country.

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Flexible advertising campaigns

The ATC conducts tailor-made advertising campaigns in key travel markets. These campaigns also target specific types of traveller such as backpackers – particularly in Europe (a main source), the United States and increasingly such Asian countries as Korea and Japan.

Flexibility is important in the ATC's advertising activities. Over the past two years we have had to respond quickly to external shocks affecting consumer sentiment on travel. Some campaigns were put on hold, ready to launch new ones as soon sentiment improved. Earlier this year the ATC put a number of campaigns on hold due to the uncertainty caused by the Iraq conflict and SARS and reallocated funds to recovery campaigns.

As of May the ATC launched a series of recovery campaigns totalling AUD 33.2 million and spanning more than 10 countries, including the United States, the UK, Japan, Singapore, Hong Kong, China and New Zealand. We thus capitalised on improved consumer sentiment, with impressive results.

Other innovative approaches include leveraging opportunities such as film releases. Promotional campaigns to coincide with the release of the film "Finding Nemo" are running in the United States, Japan, and China. The ATC is currently exploring similar opportunities to coincide with the release in Europe.

The ATC co-ordinates Australia's participation at major travel trade events around the world and has led trade missions to a number of countries to raise Australia's profile as a destination. The Australian Tourism Exchange is the ATC's premier event to showcase Australia's diverse range of tourism products. More than 2 000 delegates from Australian companies meet with 500 key overseas tourism wholesalers to develop new business opportunities for Australian inbound tourism operators.

Australia.com

The Internet is a powerful medium for targeting the consumer and - australia.com – the ATC's consumer Web site plays a major role in all PR and marketing activities. This site is used as the call to action in major advertising campaigns and provides a vehicle to reach a large number of consumers around the globe.

The site offers a choice of over 60 tailored language/country combinations, including French, German, Italian, Spanish, Portuguese, Japanese, traditional Chinese and simplified Chinese. In 2002/03 australia.com delivered over 42 million pages to consumers globally and approximately 6 million user sessions. The largest

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audience for australia.com was from North America, accounting for 37 per cent of pages viewed, followed by Europe with 19 per cent, Japan and Korea with 12 per cent, other Asian countries with 5 per cent and New Zealand and the Pacific with 2 per cent.

The Internet has become a powerful tool in travel planning and decision-making. Twenty-five per cent of all visitors to Australia used the Internet to research information prior to travelling. Internet use for trip planning is strongest in the United Kingdom, United States, Japan and Singapore.

Conclusions

In the last two decades, the Australian tourism industry has grown from a fledgling sector to one of our major industries. However, tourism has experienced difficult and challenging times. The shock of September 11, 2001 and the collapse of Ansett airlines a few days later were followed by the second Gulf War, SARS and a weakening global economy. In the past 10 years the tourism industry has also faced changing consumer demand and demographics, increased competition and unstable global geopolitics.

It might take a while before we can gauge the effectiveness of the new approach. However we are confident that measures which include a new strategic direction, flexible advertising campaigns and proactive application of the Internet for tourism promotion, will improve the environment of the Australian tourism industry and help us to meet the recent challenges and break through the barriers.

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CHAPTER 9. MALTA: A PERMANENT PROCESS OF INNOVATION IN TOURISM

This text has been drafted by Dr. John C. Grech, Chairman of the Malta Tourism Authority

Abstract

The Malta Tourism Authority, set up by an Act of Parliament on 1 September 1999, conducted an in-depth evaluation of the Malta tourism offer. It came to the conclusion that Malta was no longer competitive in the basic "sun and sea" package, due to the wider ranging offers by larger and often newer destinations able to handle much larger volumes. Given that the basic sun and sea product is highly price competitive because it is a volume business, Malta could not stand its own ground. It was clear therefore that what had basically fuelled the growth of the Maltese industry in recent decades could no longer sustain the growth and development of the industry. Malta therefore had to think creatively and to innovate in order to rejuvenate the Malta tourism offer.

Malta: A unique value proposition

Malta had to base its product on something different from the basic availability of sun and beautiful sea, which will always feature in our product. Malta's history has been influenced by happenings in the Mediterranean and subjected to many varied cultural influences. Malta in fact has the oldest freestanding man-made structures in stone anywhere in the world and can pride itself on 23 known pre-historic temple sites as well as a whole chain of other structures, remains and buildings. The Maltese have a cross-cultural profile and a language rooted in Arabic. Malta is located exactly in the middle of the Mediterranean Sea equidistant between east and west and acting as an interface between north and south. Malta has also the uniqueness of having two official languages Maltese and English. Malta also features in the Acts of the Apostles as an island that was converted to Christianity in AD 60, which is documented in the said Acts.

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Promoting Malta as an experience

Malta thus has a number of exclusive features that in various combinations add up to a unique value proposition on which to base a whole series of specific products capable of appealing to various market segments, as well as and niche markets looking for something special in a destination. The size of the island and the high density of population mean that tourists in Malta are indeed visiting a country and not just frequenting a resort. Visitors can thus become immersed in the local culture and day-to-day life, with the acting population as part of the product. This is tantamount to saying that the actual experience will be much broader than any limited interest that may have been the starting point for their choice of Malta as a destination. So rather than promote Malta as a destination we need to promote it as an experience. This implies that the value provided to the visitor derives from the experience and not just from the services consumed. Promoting Malta as an experience has therefore become an essential part of the branding process, giving Malta a distinct feature and differentiating it from all other products.

Active cooperation with all Maltese tourism actors

This process entails not only a review of the overall approach, it also means asking operators to redesign and repackage individual products. This continuing process requires active interfacing with all stakeholders. Both local suppliers and international distributors have to be converted to the new philosophy. This is being achieved, but there is still a long way to go. The local community is being encouraged through active dialogue to really become part of the Malta experiences. It must see itself as the host, and the visitor as the guest, in a relationship that must be characterised by open and genuine hospitality that goes beyond routine transactions. The public authorities are being integrated in this process. The Malta Tourism Authority has run a public awareness campaign since 2000 and regular meetings are organised with the local and central authorities. This process is under permanent development and in fact needs to be intensified and constantly repackaged to ensure unflagging support.

Revisiting the distribution model

The distribution aspect is very important. Specialised Malta tour operators tend to be more responsive than the traditional global operators. We are therefore encouraging the kind of special interest travel that is usually organised by clubs, societies and others with a particular interest in the experience that Malta has to

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offer. Malta has developed a user-friendly website that appeals to a growing number of surfers. Currently the website www.visitmalta.com is visited by 4 000 persons per day, each downloading an average of ten pages. A corporate website[77] manages relations with stakeholders.

A permanent process of innovation

This is undoubtedly an ongoing process of innovation. Malta has outgrown its original tourism product. It has to be redesigned, repackaged and repositioned on the market, and the distribution overhauled. Tourism is a service and people industry. Visitors expect to receive the services for which they pay. Since Malta is working hard to convert its tourism product into an experience the social dimension is paramount. People must see themselves as more than just suppliers or clients, but as the context around which the "Malta experience"[78] is being redesigned right up to the stage of delivery. Infrastructure is also of great importance. This process began in 1999 and is still moving forward. We must still bridge the gap between what we promise and what we can deliver. Clearly the innovative process is not yet firmly rooted, nor has the social dimension of innovation been fully understood. Malta is working hard to create as much synergy as possible among stakeholders in the tourism industry. The Malta Tourism Authority provides leadership and is developing the strategy. One major objective is to commit as much educational resources as possible and encourage the necessary motivation to make this innovative process take firm root, including the required management of change. It is a real challenge, but one that cannot be avoided. We all need to keep one thing in mind when discussing tourism. However far we drift away into technicalities, we must never forget that tourism is a hospitality industry, and if it is to thrive and grow we must keep hospitality at its heart.

77. www.mta.com.mt, the official (MTA) Malta Tourism Authority's corporate and events website.

78. www.themaltaexperience.com/HomeB.html

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CHAPTER 10. E-TOURISM: AN INNOVATIVE APPROACH FOR THE SMALL AND MEDIUM-SIZED TOURISM ENTERPRISES (SMTES) IN KOREA

This text has been drafted by Chulwon Kim, Professor, College of Hotel & Tourism Management, Kyunghee University, Korea

Abstract

This paper deals with e-tourism, innovation and growth. The Internet is revolutionising the distribution of tourism information and sales. The Korean small and medium-sized tourism enterprises (SMTEs) with well-developed and innovative Web sites can now have equal Internet access to international tourism markets. This paper examines problems and solutions related to electronic commerce in the tourism industry and suggest recommendations for successful e-commerce strategies in tourism to be applied by the industry and the government of Korea.

Introduction

Although the definition of tourism innovation (e.g. product, service and technological innovations) remains unclear new technologies can make an essential contribution to tourism development.

The Internet's potential for tourism businesses is to make information and booking facilities available to large numbers of tourists at relatively low cost. It can also serve as a tool of communication between tourism suppliers, intermediaries and end-users. The OECD (2000)[79] has shown that the advent of Internet-based electronic commerce offers many opportunities for firms to expand their customer base, enter new product markets and rationalise their business. According to the World Tourism Organisation (2001)[80] e-commerce allows SMTEs to do business in new and more cost-effective ways.

79. OECD (2000) Realizing the potential of electronic commerce for SMEs in the global economy.

80. World Tourism Organization (UNWTO) (2001) *E-business for Tourism.*

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The UNWTO has also demonstrated how the Internet is revolutionising the distribution of tourism information and sales. An increasing proportion of Internet users are buying online and tourism's share of the online market is set to grow ever larger. The Internet is clearly having a major impact as a source of tourism information. However SMTEs face a number of obstacles to the adoption of new information technology, in particular e-business. These include the scale and affordability of information technology and difficulties of implementation in organisations that are rapidly changing and growing. Moreover solutions that work for large, stable, internationally oriented firms are of no use to small, dynamic, locally based ones.

Even so, SMTEs can now have equal Internet access to international tourism markets with the help of innovative Web sites. This implies equal access to telecom infrastructure, as well as to marketing management and education. According to a UN report (2001)[81], "it is not the cost of being there, on the online marketplace, which must be reckoned with, but the cost of not being there." It is certain that embracing digital communication and information technology is no longer an option, but a necessity. E-commerce is an opportunity for SMTEs to extend their capabilities and grow.

Recent research on e-commerce in tourism

The literature on e-commerce in the tourism industry was critically reviewed with a view to developing a framework suitable for this study. E-commerce is defined as the process of buying and selling or exchanging products, services and information via computer networks including the Internet[82]. However, the adoption of Information and Communication Technologies (ICTs) is only part of the story. Network access costs, information on electronic commerce, training and skill development are all part of the challenge for smaller companies.

81. *United* Nations Conference on Trade and Development (UNCTAD) (2001) *E-commerce and Development Report 2001*.

82. TURBAN E., LEE, J., KING D. and CHUNG, HM (2000). *Electronic commerce – A managerial perspective*.

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SMTEs are also more vulnerable to problems in the areas of authentication/certification, data security and confidentiality, and the settling of commercial disputes[83].

An SME[84] e-commerce study carried out for the Asia-Pacific Economic Cooperation forum (APEC) found nonetheless that SMEs are "significant players in business-to-business electronic commerce, which accounts for more than 80 percent of all e-commerce activities."

Most research suggested that government plays an important role in facilitating the use of electronic commerce in the tourism industry. Governments in partnership with the private sector should establish a more comprehensive and consistent policy approach to the use of e-commerce in tourism, and apply evaluation mechanisms to see what works and what does not[85].

Key factors for successful e-commerce

Research was performed to collect secondary data regarding e-commerce for the tourism industry at SME level. A questionnaire designed to obtain information on e-commerce activities, its benefits for tourism, the barriers and key success factors was developed on the basis of this data and provided an insight into the challenges the industry faces today. It essentially covered Korean SMTEs, defined as businesses that have 300 or fewer employees or sales ranging from USD 2 million to USD 20 million.

Benefits of e-commerce

The main benefits of e-commerce mentioned include 'providing easy access to information on tourism services,' 'providing better information on tourism services,' and 'providing convenience for customers'. Respondents seemed less aware of other

83. BUHALIS, D., SCHERTLER, W. (eds.) (1999), *Information and Communication Technologies in Tourism 1999.*

84. SMEs - Small and Medium Size Enterprises.

85. United Nations *Conference on Trade and Development* (UNCTAD) (2001) E-commerce and Development Report 2001. OECD (2000*) Realizing the potential of electronic commerce for SMEs in the global economy;* Korea Information Society Development Institute (2000) *The Activation of E-commerce for SMEs in APEC Region;* Asia-Pacific Economic Cooperation (APEC) (1999). *SME Electronic Commerce Study.*

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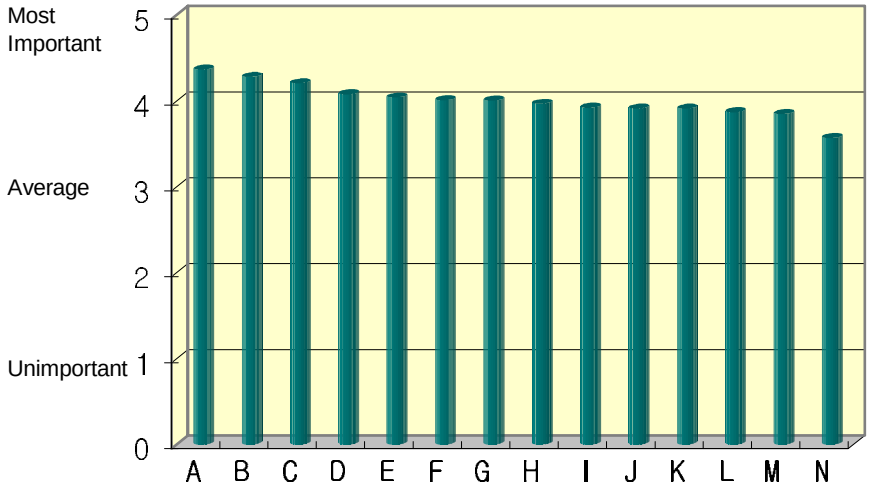
benefits of e-commerce such as 'creating new markets,' 'improving customer services,' 'establishing interactive relationships with customers', 'reducing operating cost', 'interacting with other business partners', and 'founding new business partners' (Figure 10.1).

Figure 10.1. Benefits of E-commerce



A: Providing easy access to information on tourism products and services; **B**: Providing better information on tourism products and services; **C**: Providing convenience for customers; **D**: Expanding choices by customers; **E**: Creating new markets; **F**: Establishing interactive relationship with customers; **G**: Improving customer services; **H**: Improving image and public recognition of the small & medium sized tourism enterprises; **I**: Saving time for providing tourism services; **J**: Providing customized & specialized tourism products & services; **K**: Reducing operating cost; **L**: Simplifying the process business; **M**: Interacting with business partners; **N**: Founding new business partners.

Source: Modified from APEC Tourism Working Group (2002).

E-commerce barriers

A number of barriers discourage SMTEs from adopting e-commerce in Korea. These include 'limited knowledge of available technology,' 'lack of awareness,' 'cost of initial investment,' 'lack of confidence in the benefits of e-commerce,' and 'cost of system maintenance.' Other factors are 'shortage of skilled human resources,' and 'resistance to adoption of e-commerce.' Also worth mentioning are 'insufficient e-commerce infrastructure' and 'small e-commerce market size' (Figure 10.2).

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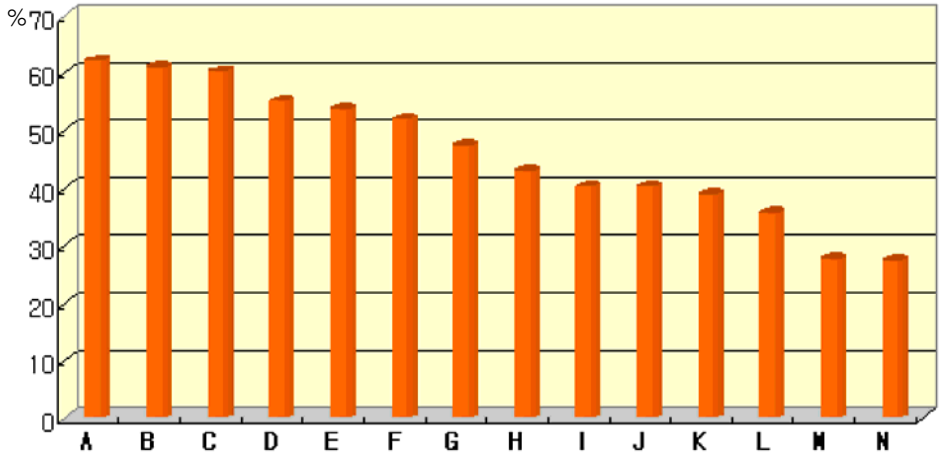
Figure 10.2. Barriers to adopting E-Commerce



A: Limited knowledge of available technology; **B**: Lack of awareness of e-commerce; **C**: Cost of initial investment; **D**: Lack of confidence in the benefits of e-commerce; **E**: Cost of system maintenance; **F**: Cost of securing skilled human resources for e-commerce; **G**: Shortage of skilled human resources; **H**: Difficulty with integrating e-commerce & existing system; **I**: Cost of training human resources for e-commerce; **J**: Insufficient e-commerce infrastructure; **K**: Lack of government support; **L**: Relatively small e-commerce market size; **M**: Fear of changes in corporate culture; **N**: Resistance to adoption of e-commerce.

Source: Modified from APEC Tourism Working Group (2002).

Successful e-commerce practices

The two main factors for conducting successful e-commerce are 'security of the e-commerce system' and 'user-friendly Web interface'. Also considered as important are 'Top management support,' 'IT infrastructure,' and 'Customer acceptance'. Few SMTEs recognise the importance of 'sharing knowledge and information between SMTEs' and 'business partnerships' (Figure 10.3) as strategies for success.

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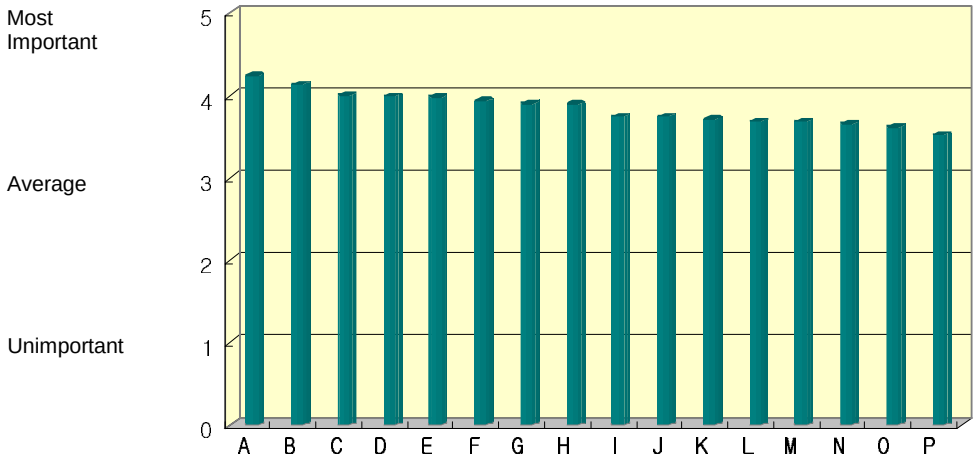
Figure 10.3. Important Factors for Successful E-commerce



A: Security of the e-commerce system; **B**: User-friendly Web interface; **C**: Top management support; **D**: Level of trust between customer and company; **E**: Information technology infrastructure; **F**: Customer acceptance; **G**: Cost of establishing and maintaining e-commerce system; **H**: Skilled human resources; **I**: Market situation; **J**: Integration with the existing corporate system; **K**: Specific tourism products or services for e-commerce; **L**: Corporate knowledge, culture & acceptance; **M**: Relationship with other business partners; **N**: Sharing knowledge and information between the small & medium-sized tourism enterprises; **O**: Internal communication; **P**: Government support.

Source: Modified from APEC Tourism Working Group (2002).

Importance and performance

The study used importance and performance (IP) analysis to examine e-commerce strategies. For 'importance' respondents indicated the importance of each of the 16 proposed factors for a successful implementation of e-commerce. For 'performance,' they indicated how well their member's economy performs regarding e-commerce, related to their response to 'Importance' (Figure 10.4).

Four IP categories emerge from the analysis: 'Keep up the good work' importance and performance both high); 'Concentrated efforts' (high importance, low performance); 'Low priority' (low importance, low performance); 'Possible overkill' (high performance, low importance).

Keep up the good work

Respondents considered the following factors as important: 'Security of e-commerce,' 'User-friendly Web interface,' 'IT (Information Technology)

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infrastructure,' 'Level of trust between customer and company,' 'Customer acceptance.'

Concentrated efforts

The factors in this category including 'top management support' and 'skilled human resources' are considered as very important but insufficiently performed. More efforts are needed.

Low priority

'Government support,' 'Sharing knowledge and information between SMTEs,' 'Integration with the existing corporation,' and 'Relationship with other business partners.' received low marks in importance and performance despite being critical for successful e-commerce. This implies that managers have limited knowledge and need more information on the importance of these factors.

Possible overkill

'Market situation' falls in the 'Possible overkill' category. The results show that managers use the Internet for market analysis (possibly competitor analysis) but do not consider it important. This seems to contradict certain previous findings indicating that SMEs do not often use the Internet for market research.

Remainder

Three factors including 'Specific tourism products or services for e-commerce,' 'Corporation knowledge, culture, and acceptance,' and 'Internal communication' fall somewhere between 'Low Priority' and 'Possible overkill.' One factor, 'Cost of establishing and maintaining e-commerce system' is between the 'Concentrated efforts' and 'Keep up the good work' categories. The assessment of these factors was fairly similar to that for 'low importance' and 'middle performance.'

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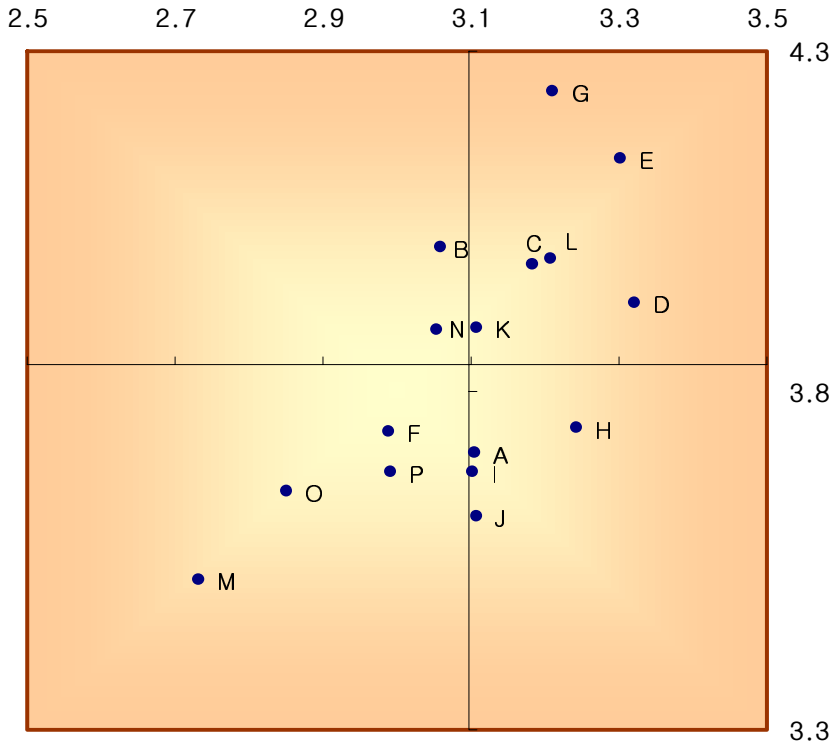
Figure 10.4. Importance-Performance (I-P) Analysis



A: Specific tourism products or services for e-commerce ; **B**: Top management support ; **C**: Information technology infrastructure ; **D**: Customer acceptance ; **E**: User-friendly Web interface ; **F**: Integration with the existing corporate system; **G**: Security of the e-commerce system ; **H**: Market situation ; **I**: Corporate knowledge, culture and acceptance ; **J**: Internal communication ; **K**: Cost of establishing and maintaining e-commerce system; **L**: Level of trust between customer and company ; **M**: Government support; **N**: Skilled human resources ; **O**: Sharing knowledge and information between the small & medium sized tourism enterprises internal communication ; **P**: Relationship with other business partners

Source: Modified from APEC Tourism Working Group (2002).

E-commerce strategies as a tool of innovation

For Rayport and Jaworski [86], the implementation of e-commerce strategy requires four critical forces: technology, capital, media, and public policy

86. RAYPORT, Jeffrey, JAWORSKI, Bernard (2002*), Introduction to E-Commerce.*

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infrastructures. An infrastructure is defined as the foundation of a system. E-commerce strategies relate to four infrastructures:

- *Technology*: Internet, computer hardware, servers, routers, cables, network technologies, software, and communications technology. Understanding the technology, what it can and cannot do, is essential for the formulation of a viable vision and strategy.

- *Capital*: how to secure funding for an e-business and subsequently value that business.

- *Media*: managers who run online enterprises must learn to manage the staff responsible for design interface, stylistic choices, editorial policies, appropriate content choices. An e-commerce manager is a publisher of digital content on the Web and should be able to make choices about the types of media employed (print, audio, video) and editorial policy (style, content, and look, feel).

- *Public policy*: e-commerce managers should understand current laws and how they may affect their businesses.

The best SMTE strategies depend on the company's e-commerce infrastructure and stage of development:

- External service providers have great potential for start-ups on the Internet. Marketing should be selective. Although it is possible to develop a strategy for international markets, earning a good reputation in the local market should be the top priority.

- Established SMTEs should focus on two key strategies: 1) expanding the range of services and products and 2) upgrading their quality. They should redesign their Web sites to focus more on 'customer retention' than 'customer acquisition', concentrating on the quality of service. The Internet is a useful tool to reach international markets. E-partnerships between SMTEs or with large firms are important (build an e-community).

Strategy should reflect the environment. Linkage to a site of destination management organization (DMO) is critical to success. Development of an online booking system is the most important technological aspect. Measures should be taken to overcome consumers' lack of trust and confidence including 'about us,'

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'frequently asked questions (FAQs),' and 'call centre' services. Established SMTEs should consider target market segments as well as building trust and confidence.

Implications for tourism policy

The role of government is very important, in particular active support to foster an entrepreneurial culture. Key policy should include; 1) improving the legal and regulatory framework, 2) moving government procurement online, and 3) facilitating transformation to e-commerce.

Important issues for consideration are: consumer protection, legal mechanisms for disputes (e.g. e-commerce mediation committee), intellectual property protection, validity and enforcement of contracts, taxation of Internet transactions (problem of tax avoidance), identification and residence of users. OECD and APEC guidelines can help. A programme of e-trust certification is one way to build consumer confidence. Medium-to-long-term strategy should include online government procurement, and government support for transformation to e-commerce. This support can take the form of tax reductions, financial support, the promotion of knowledge and information sharing between industries and research organisations.

A current Korean pilot project aims to create a business-to-business (B2B) network in all key industries. The government's 'System to Certify Venture Tourism Business,' indirectly supports industry. In 2001, 11 companies were selected as venture tourism businesses enabling them to obtain support. Applications are evaluated twice a year. Most domestic software companies in Korea do not have distribution channels of their own and pay a commission of almost 40% to the distributors. To solve this problem the government established software "cybermall", opened in 1998 and which provides product demonstrations. Products can be purchased electronically.

Other ways the government can help the growth of e-commerce include building capacity in information technology infrastructure, manpower training and planning as well as promotional and incentive measures. The government should be a facilitator, promoter and educator and should itself be ready to test new applications. OECD member countries are expected to facilitate international strategic alliances at government-to-government (G2G) and industry-to-industry (I2I) levels. Governments can also help remove regulatory obstacles to the growth of markets and businesses, and to create markets in emerging areas. Its ultimate

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objective is the promotion of private sector initiatives for e-commerce development[87].

Conclusions: recommendations for e-tourism innovations

This paper makes certain recommendations to the Korean e-tourism market, which may also be of use to the tourism industries of other countries.

The government should have a national vision, a strategic plan and policy guidelines for the e-commerce activities of SMTEs. The strategies should include all tourism stakeholders. Policymakers are also responsible for establishing the appropriate laws, regulations and service standards needed to build consumer confidence.

SMTE entrepreneurs need to adopt business models tailor-made to their own objectives and the environment, possibly combining various e-business models. External service providers have great potential for assisting SMTEs.

The integration of SMTEs into tourism associations might be one way to discourage competition at the destination level, replacing it with the development of networks that can benefit all concerned. Partnerships with other small or large firms could also help, especially in such management areas as branding, customer relations, and human resources.

Marketing via an e-shopping mall is a way to share start-up advertising and technical costs. Key words include: interactivity, mass customisation, real time and customer databases.

Established SMTEs may need to focus their websites more on 'customer retention' than 'customer acquisition'. They should also try to develop and manage their own digital brands: in the virtual world consumers are more dependent on recognised brands.

Finally policymakers and entrepreneurs need to work together to raise awareness of e-commerce, notably with the help of training and education programmes.

87. Khan, H. (2002), Best *Practices on E-Commerce Strategies for SMTEs in Singapore.*

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How is innovation transforming tourism business models? By tackling the subject of innovation, this report touches upon an important dimension of tourism economics rarely examined at the international level. It provides information about the dynamics and characteristics of innovation in tourism, and gives examples of how business models are evolving as a result. It also aims to provide an important contribution to further research and policy work in this area. The report includes a discussion of the conceptual issues regarding innovation in tourism, it illustrates national and industry practices enhancing innovation in tourism, and provides insights into the potential role of tourism policy in innovation.

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