



Modulization in the Service Industry

*A case study on modulization tendencies in the Norwegian package
tour market.*

Anders Christian Rønning

Advisor: Associate Professor Tor Fredriksen

Master Thesis – MSc International Business

NORGES HANDELSHØYSKOLE

This thesis was written as a part of the Master of Science in Economics and Business Administration program - Major in International Business. Neither the institution, the advisor, nor the sensors are - through the approval of this thesis - responsible for neither the theories and methods used, nor results and conclusions drawn in this work.

Foreword

The topic of this thesis came about more by chance than sudden epiphany, one might say. While researching a similar topic, I came across the article that forms the theoretical basis for this thesis and became intrigued by the development of the service industry. Having read many a book on management during my years at NHH, I felt they had an inherent bias towards explaining traditional industrial organizations, I therefore decided to focus on the service sector.

There is always a sense of incompleteness when you finish writing a thesis. The field of study is never so narrow that there is not more to study, analyze and shed light on. This is especially true of this thesis, as it not only deals with an entire industry, but also supports a theory on the development of the service industry, especially concerning mass-producing service companies. The topic should be interesting to a wide range of scholars and students as both the service industry, and in particular innovation in the service industry, is under-researched.

I would like to express my gratitude to my advisor, Associate Professor Tor Fredriksen at the Department of Strategy and Management at NHH, for excellent advice and fast responses, as well as the three interviewees, which upon their own request will remain anonymous. Finally, my trusty 12" PowerBook G4 deserves honorable mention for flawless performance.

Sincerely

Anders Christian Rønning

Summary

The thesis argues that Norwegian package tour companies follow a path towards modulization of their service offerings, meaning that a service is divided into smaller standardized parts so that the customer can put together his own version of the service. This approach solves the dilemma between rationalizing service production, especially mass-produced services, and offering the customer individual choices to satisfy their needs and deliver added value. The thesis will also argue that innovation is entwined with the changes relating to modulization, and that it is imperative for service companies to embrace innovation as a part of their transformation. The modulization theory is taken from Jon Sundbo's article: *Modulization of Service Production and a Thesis of Convergence Between Service and Manufacturing Organizations* (1994). The results show that the case companies clearly follow trends leading to modulization and are in the advanced stages of applying it to their service products. This trend is likely to continue and be gradually applied to all their product offerings in the future.

Contents

Table of Contents

FOREWORD	2
SUMMARY	3
CONTENTS	4
<i>Table of Contents</i>	4
<i>Tables</i>	8
<i>Figures</i>	8
1. MODULIZATION IN THE SERVICE INDUSTRY	9
1.1 INTRODUCTION	9
1.2 THESIS QUESTION	9
1.3 SCOPE OF THE THESIS AND REASONS FOR EXAMINING THIS.....	9
1.4 OVERVIEW OF THE DIFFERENT PARTS OF THE THESIS.....	10
2. SERVICE INNOVATION	12
2.1 INNOVATION IN THE MODULIZATION FRAMEWORK	12
2.2 INNOVATION AND DEGREE OF NEWNESS.....	12
2.2.1 <i>Incremental Innovation</i>	13
2.2.2 <i>Radical innovation</i>	14
2.2.3 <i>Semi-radical innovations (Ameliorative innovation)</i>	15
2.3 DIFFUSION OF INNOVATION.....	16
2.3.1 <i>Diffusion of innovation theory</i>	16
2.3.2 <i>Criticism of the diffusion theory</i>	19
2.4 SOURCES OF INNOVATION	19

2.5	INNOVATION AND THE SERVICE INDUSTRY	21
2.5.1	<i>Innovation in the service industry</i>	21
2.5.2	<i>What is the service industry?</i>	21
3.	TRENDS IN SERVICE PRODUCTION	24
3.1	INTRODUCTION	24
3.2	SUNDBO (1994) – MODULIZATION OF SERVICE PRODUCTION	24
3.3	TO SUM IT ALL UP	29
4.	SOURCES AND ANALYTICAL METHOD	31
4.1	SOURCES AND ANALYTICAL METHODOLOGY	31
4.1.1	<i>Written sources</i>	31
4.1.2	<i>Oral sources</i>	31
4.1.3	<i>Analytical methodology</i>	32
4.2	REASON FOR USING THE PACKAGE TOUR INDUSTRY	34
5.	OVERVIEW OF THE PACKAGE TOUR INDUSTRY	35
5.1	INTRODUCTION	35
5.2	THE PACKAGE TOUR INDUSTRY IN EUROPE	35
5.2.1	<i>History</i>	35
5.2.2	<i>Development and consolidation</i>	36
5.2.3	<i>Profitability – Costs and Income</i>	37
5.2.4	<i>Major players</i>	38
5.2.5	<i>Trends in the package tour industry</i>	39
5.3	THE PACKAGE TOUR INDUSTRY IN NORWAY	43
5.3.1	<i>Tour operators and their structures</i>	43
5.3.2	<i>Customers – who are they</i>	44

5.3.3	<i>The package tour value chain in Norway</i>	45
6.	ANALYSIS	48
6.1	INTRODUCTION	48
6.2	TRENDS IN MARKET DEMANDS ON SERVICE FIRMS AND THE SERVICE FIRMS' REACTIONS.....	48
6.2.1	<i>More possibilities and increased market competition</i>	48
6.2.2	<i>Price as a central competition factor</i>	49
6.2.3	<i>Demand for increased productivity</i>	50
6.2.4	<i>Demand for quality</i>	51
6.2.5	<i>Development of strategies</i>	52
6.2.6	<i>Innovation and renewal</i>	53
6.2.7	<i>More technology</i>	55
6.2.8	<i>Internationalization</i>	56
6.2.9	<i>Mergers and acquisitions</i>	57
6.3	DEVELOPMENTS IN PRODUCTION ORGANIZATIONS RELATED TO MODULIZATION IN MASS-PRODUCING SERVICE FIRMS	59
6.3.1	<i>Large-scale operations</i>	59
6.3.2	<i>Standardization of products in a combination system</i>	60
6.3.3	<i>Standardization and rationalization of the production process</i>	61
6.3.4	<i>The separation of production and marketing</i>	62
6.3.5	<i>Specific innovation organization</i>	63
6.3.6	<i>Self-service</i>	65
7.	CONCLUSION AND IMPLICATIONS	67
7.1	INTRODUCTION TO CHAPTER	67
7.2	IMPLICATIONS FROM TRENDS IN MARKET DEMANDS ON SERVICE FIRMS AND THE SERVICE FIRMS' REACTIONS	67

7.2.1	<i>More possibilities and increased market competition</i>	67
7.2.2	<i>Price as a central competition factor</i>	68
7.2.3	<i>Demand for increased productivity</i>	68
7.2.4	<i>Demand for quality</i>	69
7.2.5	<i>Development of strategies</i>	69
7.2.6	<i>Innovation and renewal</i>	69
7.2.7	<i>More technology</i>	70
7.2.8	<i>Internationalization</i>	71
7.2.9	<i>Mergers and acquisitions</i>	71
7.2.10	<i>Conclusion on trends in the service industry at large</i>	72
7.3	IMPLICATIONS FROM DEVELOPMENTS IN PRODUCTION ORGANIZATION RELATED TO MODULIZATION IN MASS-PRODUCING SERVICE FIRMS	73
7.3.1	<i>Large-scale operations</i>	73
7.3.2	<i>Standardization of products in a combination system</i>	73
7.3.3	<i>Standardization and rationalization of the production process</i>	74
7.3.4	<i>The separation of production and marketing</i>	74
7.3.5	<i>Specific innovation organization</i>	75
7.3.6	<i>Self-service</i>	75
7.3.7	<i>Conclusion on the mass-producing service firm</i>	75
7.4	THESIS QUESTION CONCLUSION.....	76
7.5	FUTURE RESEARCH QUESTIONS.....	77
	REFERENCES	78
	APPENDIX	82
	INTERVIEW GUIDE	82

Tables

Table 1 - Innovation sources	20
Table 2 - UK Tour Operator Profit Margins	37
Table 3 - Package Tour Operator Profitability	39
Table 4 - Aircraft Utilisation Rates in the UK	40
Table 5 – Ownership trail of package tour brands in Norway	43
Table 6 - Market share developments 1998 - 2002	44

Figures

Figure 1 - Disruptive Innovations over the last 20 years	16
Figure 2 - Diffusion of innovation curves.....	17
Figure 3 - Activities in the package tour value chain	45

1. Modulization in the Service Industry

1.1 Introduction

Mass-producing service firms are under constant pressure to cut costs, deliver better quality and introduce innovative services in order to satisfy their customers while still keeping them in focus. This presents the problem: how can service firms standardize the production process and service products while keeping the customers feeling that they are treated individually and well? The hallmark of any service is close customer orientation; too much standardization will spoil the experience since the customer is ultimately involved in the production process. This involvement is known, among other terms, as prosumption.

1.2 Thesis Question

New technology has changed the chain of distribution in parts of the service sector. Customers can now buy services directly from the producers by skipping the traditional middleman, thereby achieving cost savings. Traditional service providers have to respond to this challenge by altering the way they sell their services and offering customers added value. This thesis proposes that service companies will modularize their service offerings in order to create added value for the consumer and retain their market share. Specifically the thesis will use a case study about the degree to which Norwegian charter tour companies have modularized their service offerings.

1.3 Scope of the thesis and reasons for examining this

The scope of this thesis will be describing and analyzing the four largest charter tour operators in Norway in the context of using modulization as a basis for business model change through dividing their products into modules. The case analysis will describe how the charter tour operators can use the modulization approach to deliver value added service to their customers, based on a framework taken from Jon Sundbo's article: *Modulization of Service Production and a Thesis of Convergence Between Service and Manufacturing*

Organizations (1994). This will be done with an emphasis on the use of innovation in achieving the change. An introduction to the European charter market is included to give the reader a better understanding of the interplay between the large European travel corporations that own the Norwegian package tour companies, and the decisions made on the national level. The focus of the analysis however, will be the Norwegian market. The thesis of convergence between service and manufacturing organizations is beyond the scope of this thesis.

1.4 Overview of the different parts of the thesis

Chapter 2 is titled Service Innovation and starts off with an introduction to the role innovation plays in the modulization framework. It is then explained what innovation is and what the different levels of innovation, such as incremental and radical, mean. The diffusion of innovation theory is presented, together with criticism of the same theory, to give the reader insight into how innovations spread in the marketplace. We also look at the sources of innovation, and what innovation in the service industry means, as well as a look at the characteristics of the service industry itself.

Chapter 3 presents the framework for the analysis in detail, based on Jon Sundbo's article Modulization of Service Production and a Thesis of Convergence Between Service and Manufacturing Organizations (1994). Nine trends related to market demands on service firms and their reaction to these trends are presented, followed by an in-depth look at developments in production organizations related to modulization in mass-producing service firms.

Chapter 4 aims to bridge the theoretical part of the thesis with the empirical part. The first sub-chapter deals with the different types of sources used in the thesis and the analytical method used in the empirical study. The second sub-chapter outlines the reasons for choosing the package tour industry to test the thesis question.

Chapter 5 gives an insight into the package tour industry in Europe and Norway. The chapter starts off with a brief overview of the industry's history in Europe and then outlines the development and consolidation phase leading up to the current situation. Profit margins are presented along with information about the largest tour companies in Europe and current

trends in the industry. The background information on the industry in Europe is important since large European corporations control 94% of the market in Norway (Roper et al. 2005, p. 197). The Norwegian market is presented in more detail, since it is the unit of analysis including an introduction to the package tour value chain based on an article by Roper et al. (2005).

Chapter 6 presents the analysis, based on written and oral sources, of the theoretical framework, following the structure of the theory closely. The analysis will focus on information collected during interviews with senior managers in the industry in Norway, with other relevant information added as appropriate. This information will then be discussed in comparison with the theory presented in chapter 3.

Chapter 7 deals with the conclusions and implications of the findings in chapter 6, as well as suggesting further research topics in this field. It is split in a sub-chapter on the trends in market demands on the service firms and their reactions, and a chapter on the developments in the production organization related to modulization in mass-producing service firms, as is done in the theory. A final conclusion on the thesis question is given.

2. Service Innovation

2.1 Innovation in the modulization framework

This chapter gives an introduction to key concepts in the thesis. The trends that lead to modulization all involve changes to the business, and most of these changes require the company to alter their service offering in new and innovative ways. To fully understand how innovation can change a business we need to know what it is, the different levels of change it brings, how it spreads in the marketplace, and the sources from where it comes. To give some underpinnings to the theory presented in the next chapter, especially since innovation research has a large bias towards production organizations, a segment on innovation in the service industry is included. At the end of the chapter the service industry itself is presented.

2.2 Innovation and degree of newness

Innovation has many different definitions attached to it. The ordinary dictionary will define it as something similar to: “The introduction of something new” and/or “ a new idea, method or device” (Merriam-Webster Dictionary & Thesaurus). Encyclopædia Britannica has no clear-cut definition of the word as it is used in many different settings. It does argue that strictly speaking, an innovation should be something entirely new, be it an idea or a product, however nobody lives in a complete vacuum, and innovations must therefore, explicitly or implicitly, be based on some measure of previous experience (www.eb.com - history of technology – Innovation). Traditional theories on innovation, based on studies of the manufacturing industries, agreed that innovation is a radical act, which is the introduction of a new element or a new combination of old elements (Sundbo, 1997: 435). Regis Cabral (1998) puts innovation in a network- and economics perspective: "Innovation is a new element introduced in the network which changes, even if momentarily, the costs of transactions between at least two actors, elements or nodes, in the network." Scholars identify at least five different areas of innovation, although there is significant deviations in how many definitions are used, together with a debate on the whole taxonomy of the innovation field.

-
- Product innovation – Involves the introduction of a new good or service that is substantially improved.
 - Process innovation – A new or significantly improved production or delivery method.
 - Marketing innovation – Development of new marketing methods with improvements in at least one of the four P's, price, place, promotion, and product.
 - Organizational innovation – Includes creating new organizations, business practices, organizational behavior, and ways of running the business.
 - Business model innovation – Changing how the business captures value.

(Wikipedia – Innovation: 2006-04-04).

Another aspect of innovations is the difference between incremental and radical innovation. Davila et al. for example use three generic types of innovation: incremental, semi-radical and radical (Davila et al. 2006: 38). Specifically they argue that semi-radical innovations involve substantial changes to either the business model or technology of an organization, but not to both. Other authors, such as Gallouj (2002), operate with a few more generic types of innovation.

2.2.1 Incremental Innovation

Incremental innovation is evolutionary, meaning small changes along a trajectory, with relatively high odds of success and low uncertainty about the outcome (Wikipedia – Innovation: 2006-04-05). Usually the focus is on cost or feature improvement in existing processes, products or services. The process is formal, a detailed plan of action can usually be developed at the beginning of the process, and often involve cross-functional teams (www.1000ventures.com). The goal is often to get as much value as possible from existing products or services without having to make significant changes or major investments. Incremental innovation comes from many parts of the organization and it does not necessarily concern the product or service in it self. Incremental innovation in the business model using standard management techniques such as quality control techniques, market research to better target customer needs, financial analysis, and supply chain management

happens almost every day in many companies (Davila et al. 2006: 42). An article by Banbury and Mitchell (1995) define important incremental innovations as “refinements and extensions of established designs that result in substantial price or functional benefits to users”. The authors go on to argue that it is the users’ judgment that determines the impact of the innovation, and hence defines whether or not it is an important incremental innovation or just an incremental innovation (Banbury and Mitchell 1995: 163).

Most companies want to avoid commoditization of their products, meaning that a product or service becomes indistinguishable from others like it and customers buy on price alone. Companies use incremental innovations to achieve added value and differentiation of their products in order to combat commoditization. A case in point would be Gillette razors, which have continually altered their product (added blades and battery power) to avoid a situation where the product would be viewed as just another commodity, and price competition would become the dominant feature of the business (Davila et al 2006: 43). Another key aspect is that a company may introduce an important new innovation and then see the product fail, only to discover that the class of goods or services introduced survives in the hands of competitors. This means that innovation must meet a market success constraint (Banbury and Mitchell 1995: 163).

2.2.2 Radical innovation

Radical innovations are large leaps in product, process or services technology with unprecedented performance features, involving low odds of success and high uncertainty about the outcome (Wikipedia – Innovation: 2006-04-05). It is much more difficult to have a formal process for radical than incremental innovations. This is because radical innovations occur sporadically, often as the result of one employee’s sudden epiphany, and the road to a finished innovation is often non-linear (www.1000ventures.com). Rensselaer Polytechnic Institute (RPI) says: “We define a radical innovation as one that has the potential to offer either new-to-the-world performance features or a dramatic (5-10X) performance improvement in known features or a dramatic (30-50%) reduction in cost”; a statement echoed by many other scholars. This defines radical innovations in terms of objective parameters but does not say anything about markets and consumers. Urban et al. (1996) call radical innovations really-new products, and argues that they “shift market structures, represent new technologies, require consumer learning, and induce behavior changes.” This

provides us with the view that markets are created or permanently altered by a radical innovation, something that has a major impact on strategy, as well as pointing out that it does something with the consumer. The consumer not only has to learn to use the product or service, an investment in it self, but the consumer's behavior must change. As most people are loath to change their ways and require extensive persuasion to learn how to use a product (persuasion can be that others use the product, the benefit is inherently clear, or it gives status or comfort for instance) few radical products will succeed in the marketplace. Radical innovations are important because they improve or create competitive advantages and create opportunities to enter new markets.

2.2.3 Semi-radical innovations (Ameliorative innovation)

Semi-radical innovations are radical innovations to either the business model or the technology of an organization, but not to both. A semi-radical innovation will usually bring about incremental innovation in the other dimension (Davila et al. 2006: 48). Ryanair moved away from the hub-and-spoke network of major carriers to point-to-point operations, while still using the same airplanes (technology) as the competitors; this is an example of semi-radical innovation. The theory and definitions behind radical and incremental innovation applies together to the respective dimensions that are changed.

Radical innovations in the business model can substantially improve corporate performance and even alter whole industries. Many successful and admired companies started life as a radical business model innovation, DELL, IKEA, Amazon.com are a few examples. A radical innovation can be disruptive, meaning that it changes the competitive landscape, as opposed to incremental and radical innovations that describe a relative change in technology or the business model elements. The focus of the term is on the effects of innovation and success can bring huge rewards, however as this is the product of internal sources of change, it is not something that can a company can decide to do, it is the result of leveraging innovations (Davila et al. 2006: 57). Disruptive innovations are not very common as the graph clearly demonstrates. However, their effects reverberate for many years.

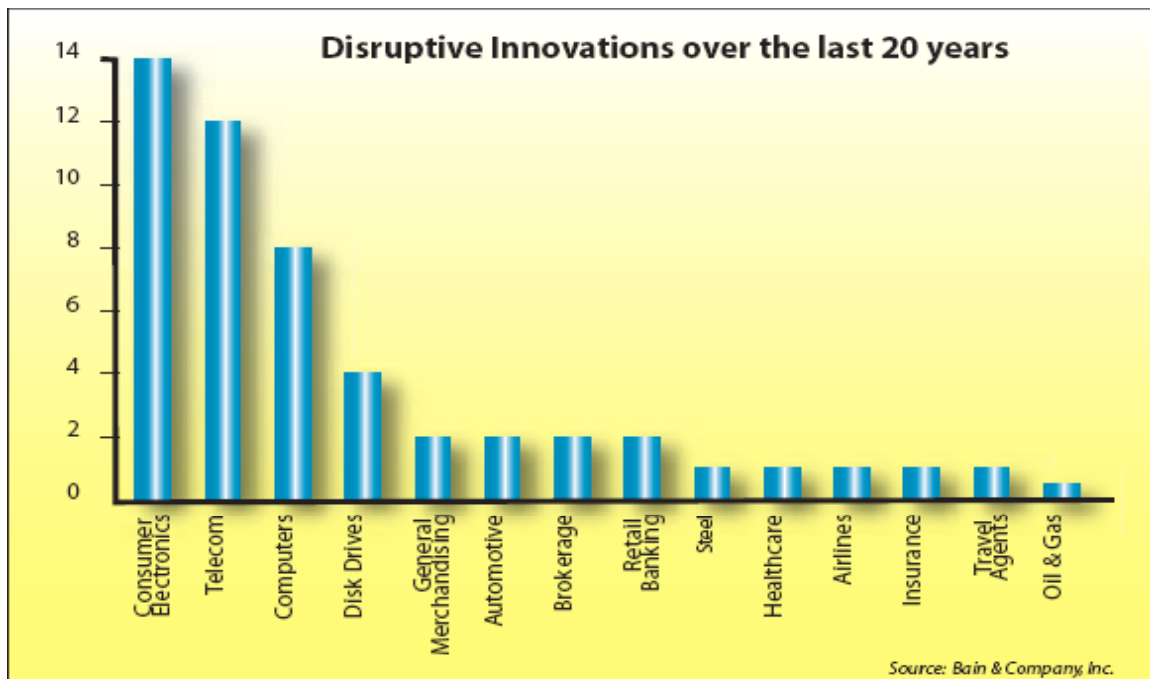


Figure 1 - Disruptive Innovations over the last 20 years

Source: Rigby, D. and Corbett, A. (2002).

2.3 Diffusion of Innovation

2.3.1 Diffusion of innovation theory

Everett Rogers first formalized diffusion of innovations theory in a 1962 book called “Diffusion of Innovations”. “Diffusion is the process by which an innovation spreads”. In the book he categorized the adopters of a new innovation or idea in five groups according to their propensity to adopt the innovation or idea. The percentages are the original proposed by Rogers, and will vary with the nature of the innovation, and as such they are guidelines more than anything.

- *Innovators (2,5%)* Innovators want to be on the cutting edge. They have the ability to work with complex and often underdeveloped ideas as well as the financial means to help them cope with the potential losses and uncertainties from the innovations.

- *Early adopters (13,5%)* are often the opinion leaders. Others follow where they go and they provide the other potential adopters with information and advice about the innovation. Early adopters are visionaries.
- *Early majority (34%)* are often pragmatic people and adopt the innovation just ahead of the average of the population. They undertake deliberate and sometimes lengthy decision-making, and link the early adopters with the bulk of the population. This leads to rapid diffusion of the innovation throughout the population.
- *Late majority (34%)* tend to adopt an innovation because of economic necessity and peer pressure. They tend to be more conservative and have fewer resources than the early majority and therefore require more evidence of the value of an innovation before adopting it.
- *Laggards (16%)* are the most skeptical when it comes to spend their often limited resources on a new innovation. As a group they are fairly isolated from the rest of the population.

(Dorf and Byers, 2005: 249)

There are two different graphs showing the diffusion of innovation, the bell curve and the S-curve:

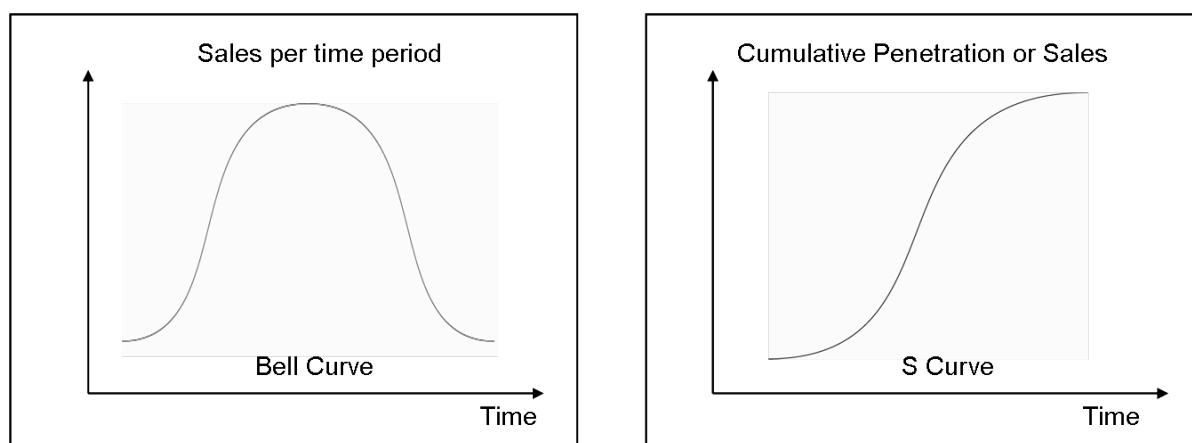


Figure 2 - Diffusion of innovation curves

Source: Wikipedia – Image:Scurvebellcurve.png

Diffusion of innovation is not only related to new products or services, but also new beliefs or a new fashion in the sphere of leisure. Diffusion is selective, meaning that only people

who are motivated to do so adopt it. One reason for adoption of an innovation by large groups of people is the example set by higher-status groups. The higher-status groups act as reference groups for the groups of lower perceived status and the innovation is diffused down the social status ladder. In modern Western societies the typical innovators and early adopters are young, affluent, urban, have good educations and high status jobs (EB.com: social change). Cruising on the ocean used to be reserved for high status wealthy individuals, but today cruise vacations are available for large parts of the population. This form of leisure activity has diffused down the social ladder.

The critical point in the bell curve is migrating from early adopters to early majority. The gap between visionaries and pragmatists is called a chasm. Crossing the chasm involves recruiting pragmatists as customers, because once that is done other early majority adopters will see the innovation and be willing to try it (Dorf and Byers, 2005: 249). As seen in the graph in the appendix on the spread of products into American households, some innovations diffuse rapidly, while others take a long time to diffuse fully, if they ever do. This must be taken into account when launching a new innovation, not all products or services are intended for all people, and the diffusion process may take much longer than originally intended, especially if the product or service does not measure up well to the motivational characteristics explained below.

We can generally classify five characteristics of an innovation that determines the motivation of people for adopting an innovation.

- *Relative advantage*: perceived superior performance compared to product or service it replaces. The advantage can be both in terms of economics and performance.
- *Compatibility*: how well the innovation fits with the potential adopters values, know-how, practices and experiences.
- *Complexity*: how difficult to understand or use the innovation is. Higher rates of perceived complexity results in lower rates of adoption.
- *Trialability*: the extent to which potential adopters can experiment and experience the innovation. Higher trialability results in higher rates of adoption.
- *Observability*: the extent to which the adoption and benefits of the innovation is visible to potential adopters. Higher observability leads to higher rates of adoption.

(Dorf and Byers, 2005: 247)

2.3.2 Criticism of the diffusion theory

Diffusion modeling studies are generally concerned with tracking the patterns innovations follow as they spread across a population of potential adopters over time (the rate of diffusion). Typically the innovation is considered diffused at the point of purchase or physical acquisition of the innovation. This approach can in certain cases lead to wrong assumptions since innovations may not be used or only used to a certain degree, a so-called assimilation gap, after the purchase. This is especially true for innovations that require high degrees of knowledge to use (Fichman and Kemerer 1999). Another problem is the so-called Pro-Innovation bias. “The pro-innovation bias is the implication in diffusion research that an innovation should be diffused and adopted by all members of a society, that it should be diffused more rapidly, and that the innovation should be neither re-invented nor rejected.” The biases leads researchers to ignore the study of ignorance about innovations, discontinuation or rejection about innovations are underemphasized, failure to do anti-diffusion research (the study of bad innovations such as drugs and cigarettes, and the programs designed to prevent diffusion), and to overlook re-invention (Rogers 1995: 100).

Examples of the assimilation gap are:

Photo editing on a personal computer: How many people can actually do it, compared to the number of people having photo-editing applications on their computer?

MMS-enabled handsets: Almost all new mobile phones in Europe have MMS-capabilities, yet can we conclude that only the laggards are not using it?

2.4 Sources of innovation

There are many sources of innovation. Some of the more common are: universities, end customers (users), research laboratories, manufacturers, suppliers and independent inventors. As we see from the table, the source of innovation differs very significantly between categories of innovation.

Innovation type sampled	Innovations developed by					Total
	User	Manufacturer	Supplier	Other	NA*	
Scientific Instruments	77%	23%	0%	0%	17	111
Semiconductors and printed circuits board process	67	21	0	12	6	49
Pultrusion process	90	10	0	0	0	10
Tractor shovel related	6	94	0	0	0	11
Engineering plastics	10	90	0	0	0	5
Plastics additives	8	92	0	0	4	16
Industrial gas-using	42	17	33	8	0	12
Thermoplastics-using	43	14	36	7	0	14
Wire termination equipment	11	33	56	0	2	20

*NA = number of cases for which data coded in this table is not available. (NA codes are excluded from calculations of percentages in table.)

Table 1 - Innovation sources

Source: Hippel (1988) – Excerpt from McKinsey Quarterly.

This means that product users almost always develop major product innovations in some fields, such as scientific instruments, whereas in other fields manufacturers or suppliers develop the important innovations (Hippel 1988: 4). This result has far reaching implications for companies based on their assumptions regarding the sources of innovation. Most companies organize around the common assumption that they develop new products themselves and manufacture it for commercial purposes. In the event that end users are the drivers of innovation, an in-house R&D department should be geared towards finding innovations among the users, not develop them in-house (Hippel 1988: 9).

2.5 Innovation and the service industry

2.5.1 Innovation in the service industry

Innovation in the service industry (also known as the tertiary sector of industry or service sector) is much less researched, and the debate about a definition is ongoing. Sundbo (1997) states: “An innovation is a large-scale activity which is reproduced. Either the innovation (e.g., a new product) is made in many copies, or many people follow the same new pattern of activity”. More specifically we can say that service innovation is considered to consist of both product and process innovations (Maitland and Tapia, 2005: 12).

Many authors have pointed out that innovation in the service industry lacks the protection afforded by patents and therefore service firms do not innovate as much as the manufacturing industry. Sundbo (1997) points out that this is only the case in non-technological innovations, and perhaps also only in product innovations, since process and organizational innovations are much harder to imitate and in many cases are not patentable. The advent of the information technology age has heralded many new services previously unheard of, and Barras (1986) concludes that services are increasingly technology driven, and as such are not stopped by the lack of patent protection.

Sundbo (1997) outlines his view on innovation in the service industry through the strategic innovation paradigm. This paradigm emphasizes the firm’s strategy as the main innovation determinant. He says that innovations are for the most part market-driven and are formulated within the company’s strategic framework. To prevent activities from becoming uncontrolled, all innovations must be kept within the company’s strategy. Top management in Sundbo’s study guided the innovation process by making decisions on whether or not an innovation should be implemented. However, they are not the driving force of the innovation process. It was other members of the organization, managers, employees, and groups who initiated and executed the innovation process. Individual employees can present ideas, but the organization takes over and develops the ideas.

2.5.2 What is the service industry?

The service industry, also known as the tertiary sector, can be defined in many ways. A thesaurus defined it concisely as: “Work done for others as an occupation or a business”

(Roget's II). A more comprehensive definition of service is found in Hill (1977). Firstly, some change is brought about in the condition of some person or good, with the agreement of the person or economic unit owning the good. Secondly, the change is the result of the actions of some other economic unit. These two points provides the key concept of a service that can then be defined as "A change in the condition of a person, or of a good belonging to some economic unit, with the prior agreement of the former person or economic unit". The production part of a service is the activity that affects the person or good belonging to some economic unit, whereas the output itself is the change in the person or good affected (Wickström 1996: 318). In essence, this says that services are interactive, involving some degree of customer participation.

Prosumption – Alvin Toffler coined the word prosumer in his book "The Third Wave" from 1980. His point was that the customer would become so involved in the production process that it will become increasingly difficult to determine just who is actually the consumer and who the producer (Toffler 1980). Wikström (1996) writes that flexible new production plants and IT combines to make the consumption process more efficient and that this results in a movement towards a much closer relationship between producers and consumers. The consumer is no longer regarded as a passive receiver, but rather as an active participant in a common process.

Services cannot be stored the same way goods can, be it for short or long periods. This has nothing do to with the durability of services; many of them are in fact permanent. Services cannot be stocked, as a stock of changes is a contradiction in terms, a logical impossibility (Wickström 1996: 319).

Reich (1991) has specified three categories of service work, where the standardized mass service is divided into two: that which can be stored and transported and that which must be produced at the place of consumption but nonetheless is standardized.

1. *Routine production services*. Standardized mass production of services. It is service that can be stored and transported. Examples include work on databases.
2. *In-person services*. Traditional services produced for one customer, and cannot be stored or transported. The work is repetitive and standardized.

3. *Symbolic-analytic services*. Problem-solving advisory service, typically consultancy work. The work is complicated, non-routine and individual.

(Sundbo 1993: pp. 254-255)

3. Trends in Service Production

3.1 Introduction

Service firms have evolved rapidly in the last 35 years as a response to demands for increased productivity, better quality and lower prices. Traditional models of how service firms are run have been challenged, and new and innovative solutions for delivering services to the customer are evolving. The challenges posed by new technology are driving companies to change their business models and offerings. To achieve change companies need to be innovative, indeed, innovation can be seen as a measure of the degree of change a business goes through. The thesis seeks to explain this development in the context of the modulization framework presented in this chapter. Modulization in itself can be seen as a process innovation and evolves over time. Although not as easily recognizable as innovations achieved through scientific breakthrough or a sudden epiphany, the changes are profound and lasting.

3.2 Sundbo (1994) – Modulization of service production.

In this seminal article, Sundbo (1994) outlines his view on the contemporary service firm. He states that there is a modulization tendency in service firms. This means that service companies attempt to combine rationality and cost saving while focusing on the needs of the individual customer. They do this by standardizing service products, but in modules that can be combined individually by single customers. This concept is somewhat similar to bundling, although the choice of bundling, unbundling or rebundling is made on the basis of the market situation, whereas modulization takes into account both the market situation and the internal production organization. Modulization is also discussed as a general trend common to many service firms over a historic period. Sundbo identifies two major changes in the service market leading up to the modulization trend. The first change occurred in the 1970s and early 1980s when growth in demand for services, and a change in the way of producing and delivering the services, led to an increased focus on the satisfaction of the individual customer and created a corporate culture for that purpose. These changes were

expressed in the models of the Service Management School. The second change seems to have happened in the beginning of the 1990s (at least in Denmark) when competition increased in temporarily stagnated markets due to a recession, forcing a change in service production and delivery systems that is leading to modulization.

Trends in market demands on service firms and the service firms' reactions

1. More possibilities and increased market competition

In many countries services were expanding and there was enough market for everyone, and many possibilities to introduce new services. A great number of new entrepreneurial firms appeared. This in turn eventually makes competition tougher and makes it harder to exploit new opportunities.

2. Price as a central competition factor

The increased competition leads to price wars, and in the case of Denmark around 1993, a recession further draws the customers attention to the price. Innovations introduced by service firms have enabled customers to become more critical in assessing both service price and quality. An example of this is the development of fee-less banks; customers used to pay the fees without much fuss, today they shop around more and have a much better understanding of fees at different banks.

3. Demand for increased productivity

Nearly all firms in Sundbo's surveys stated that an increase in productivity is necessary to survive in the market. The increased competition and focus on price will drive this development. This is not surprising, as services have traditionally had lower productivity than manufacturing, although service productivity has risen more rapidly than in manufacturing in the late 1980s and beginning of the 1990s.

4. Demand for quality

Quality will increasingly be a factor in the competition, making firms compete on both price and quality. Even standardized quality certification, such as the ISO 9000 system, is slowly making its way into the sector. A quality control system will press the service systems towards standardization. It is only possible to avoid faults by standardizing the processes.

Many service firms are trying to manage this situation by focusing on specific customer segments whose needs are well known and steady.

5. Development of strategies

The analysis of the Danish companies showed that strategy is usually of greater importance to service firms than manufacturing firms. The increased competition means many service firms now use market segmentation and product specification. This allows them to specify who their customers are and which products they want to deliver them. The flip side of having such a strategy is that it invariably leads to more standardization in production and to a certain degree in delivery and marketing. The strategy also functions as an internal control mechanism, since too much variation in the presumption situations and too many innovative ideas shift the focus from the strict service offering and allow costs to spiral out of control. The company has to focus on specific customer segments to avoid this.

6. Innovation and renewal

Renewals of service production systems and service products have increased over the last 20 years, but they have usually been unsystematic and invented in a single presumption moment. This has made it difficult for companies to exploit the innovations on a large scale. The study of Danish service firms however, shows that the firms are increasingly aware of the utility of systematic innovation and have felt a growing need to organize and manage the innovation process in a systematic way. Innovation is one of the factors pressing companies towards modulization, so that they can benefit from innovation projects and easily incorporate it into their service offering.

7. More technology

Information technology has developed very fast and has had a great impact on service production. This has allowed for many new opportunities, and increasingly service firms use it in the whole value chain and even in the presumption moment. In some industries, such as the financial services industry, information technology has made some aspect of the service a self-service, where the customer himself produces the service. Increased use of technology makes services more like manufacturing. Some services can now be stored and sold as commodities, the academic databases used in writing this thesis is an example of that (although the act of looking up articles was a self-service resulting in a change). More

technology also means more control over the production process, standardization, and leads to higher capital intensity.

8. Internationalization

The trend of internationalization emphasizes the production process. Service firms generally only succeed in expanding internationally if they have a special product or concept that can be identified, like McDonalds' burgers or Hilton Hotels. The primary reason for failure in setting up shop in a different country is the cultural factor, since interaction with the foreign country's citizen is required, local competitors have an advantage. If a service company wants to go international it must develop a standard concept, or buy a foreign service company that acts as a standard concept. Knowledge transmission is possible when acquiring a foreign company, but it is difficult to benefit from the economies of scale. Modularization can help companies leverage economies of scale and also assist in developing standard concepts.

9. Mergers and acquisitions

There is a tendency towards concentration via mergers and acquisitions in the Danish market. Reasons for this are cost problems and access to knowledge and service concepts in other businesses. The results are increased modularization, large-scale production and more knowledge.

In this thesis we use the example of charter tour operators who cater to the mass market. According to Reich's (1991) classification we put the charter tour companies in the general mass-producing service firm category (comprising the two first categories), and more specifically in the in-person services group. This group contains the traditional individual services produced for a single consumer. The services cannot be stored or transported, but are nonetheless standardized and repetitive. In order to lower prices the development has gone in the direction of standardization. How can you then keep the customer focus and make the customer feel they are treated individually and well? Modularization was found to be a general tendency in most service industries. Sundbo also found a series of development tendencies specific to the organization and function of the mass-producing service firms.

Developments in production organization related to modularization in mass-producing service firms.

1. Large-scale operations

The tendency in many service industries is towards mergers and acquisitions, and all these companies are looking for economies of scale. The advantages of economies of scale are: lower production costs, more benefits from large scale innovation projects, better known brand image, more possibilities in becoming international and exporting. An implication of this is that the entrance barriers to the service industry for entrepreneurs have become higher due to the demand for standardization, conceptualization, professionalization, and more technology.

2. Standardization of products in a combination system

The first stage is to do a product specialization and market segmentation, starting with a narrow and specific definition of the service provided (conceptualization). This means that the idea of the service product is standardized, although the actual product might not be yet. The next stage is standardization, ensuring that the product will be the same in every situation. By having a selection of standard elements the service company can ensure that the customer has more than one option and is free to combine the elements to their individual liking.

3. Standardization and rationalization of the production process

Even though service production is still a complex process, companies try to repeat the process and rationalize and standardize it as much as possible, by giving employees more specialized tasks. However, it does not mean that the work is Tayloristic in its nature. This process also makes the companies more independent of the employees who can more easily be replaced by technology. Standardization and rationalization makes it easier to plan and control the production process. It is also easier to expand the business to new locations or change the individual service components, since it is now more standardized.

4. The separation of production and marketing

More than before, modulization separates the service distribution organization from the production organization. This means that, for example, branch offices have less scope for offering tailor made solutions to the customers, since they have to follow the instructions from head office and offer a choice of standard modules. Divisions of labor between production firms and retail firms are also becoming evident, such as basic bank services

offered through an Internet-bank, where more advanced investment products are purchased from larger commercial banks. Insurance companies specializing in life insurance and pensions may well sell general insurance, but in turn buy coverage and handling from other specialist general insurance companies.

5. Specific innovation organization

As companies develop standardized products and systematize their production processes they have an opportunity to develop an innovation organization system. This will not be organized along the lines of R&D departments common to the manufacturing industry, but innovations will be made either in ad hoc project groups or as a collective process, involving the whole organization.

6. Self-service

Self-service occurs when services can be standardized and stored with the use of technology. The moment of production and consumption does not need to occur simultaneously. This is the case with several Internet related services, such as banking and software. Self-service thus resembles the presumption model, but differs in a crucial dimension; there is no personal relationship between the service firm and the customer. An implication of this is that services can become even more productive than manufacturing, since the service can be stored and the customer actually produces the service when it is being delivered, while only the production process can be automated in manufacturing. This is also evidence that price has replaced individual concern for the customer.

3.3 To sum it all up

Sundbo's research concerned the trends in the market demands on service firms and their reaction to these trends. The study also dealt with the sub-section of mass-producing service firms, and especially how the production organization reacts to these trends. In addition he sees a convergence between the service firm and the manufacturing firm, a question outside the scope of this thesis. The thesis question asks how service companies will react when technology changes the service distribution chain, put differently, their reaction when market conditions change. The theory predicts that as a result of these changes services will become

more fragmented, with opportunities for the customers to design an individual service experience by choosing from a menu of standardized parts.

The traditional distribution chain for package holidays is challenged by Internet-companies connecting the customer directly to flight operators and hotel owners. Other package tour companies focusing on niche markets are also threatening to take market share from the established market leaders. In order to counter this new competition the established package tour companies will have to come up with innovative ways of delivering their services. This thesis approaches a solution to this problem by arguing that the package tour companies should follow an innovative modularization path. To shed light on the problems confronting the industry, the first chapter of the analysis, chapter 5, will describe the current market situation in Europe and Norway and describe the package tour value chain in Norway. Chapter 6 is devoted to a systematic examination and discussion of the trends in market demands and the service firms' reaction to these trends, and developments in the production organization related to modulization in the package tour companies. Chapter 7 draws conclusions and explores the implications of the discussion in chapter 6.

4. Sources and Analytical Method

4.1 Sources and analytical methodology

4.1.1 Written sources

The written sources used in the thesis are many and varied. However, there are a few that have been extensively used. Roper et al. (2005) is a main source in chapter 5 since it is the only up-to-date comprehensive study of how Norwegian package tours are designed, distributed and produced. Their description of the package tour value chain is described in detail, and several tables and figures have been used. The theoretical framework is based on Sundbo (1994), and his article is extensively quoted, along with another article from 1997 (Sundbo, 1997). There are a few references to Wikipedia in the thesis where it was deemed appropriate and the nature of the information was non-contentious. Otherwise the sources are a mixture of academic journals, academic books, newspaper articles and websites. The varied nature of the sources stems from the fact that there was very little research about the industry, but at the same time it receives relatively much general publicity.

4.1.2 Oral sources

Interviews are oral sources and special precaution should be taken when drawing conclusions or generalizing the findings to larger groups because of the small scale of the method and often unrepresentative samples that are used. In this case the sample is small, but represents around 94% of the market and as such is represents all the mass-producing service firms in the package tour industry in Norway.

The interviews in this thesis are standardized, open-ended interviews (structured interviews), meaning that all respondents are asked the same questions, with the interviewee option of adding relevant information at the end of the interview. This interview form leads to faster interviews, and are easier to analyze and compare than general interviews or informal, conversational interview forms (Valenzuela and Shrivastava).

Three people were interviewed for this thesis. They were all top-level managers in three of the largest package tour companies in Norway. All of them had substantial business experience from the package tour industry in Norway and abroad, having worked in the travel and package tour industry for 20, 8 and 30 years in various positions respectively. They will, at the behest of the managers themselves, remain anonymous and in this thesis be referred to as:

- Manager 1 (M1) from Company 1 (C1)
- Manager 2 (M2) from Company 2 (C2)
- Manager 3 (M3) from Company 3 (C3)

The interviews were taped using a microcassette recorder and later transcribed. All interviews were conducted at the managers place of business. They were held in Norwegian, as this is the mother tongue of the interviewees, and doing them in English would create a strange atmosphere, and possibly generate inferior information. There is an English-language interview guide in the appendix. All quotes and information is translated from Norwegian to English by the author.

4.1.3 Analytical methodology

The thesis is based on qualitative research following a case study approach. The theory used in the thesis is not well suited to quantitative analysis, and is itself based on two multiple case studies (Sundbo, 245: 1994). A case study is characterized by investigating a phenomenon within its real-life context. "Social science has not succeeded in producing general, context-independent theory and has thus in the final instant nothing else to offer than concrete, context-dependent knowledge. And the case study is especially well suited to produce this knowledge." (Flyvbjerg 2004,p. 422). Generally speaking, the view that one cannot generalize on the basis of a case study is considered perhaps the most damaging to the case study as a scientific method. This view is not correct, as there have been many instances where a single case has proved enough. The classic "All swans are white scenario" serves as a reminder of this, as well as Galileo's experiment from the Tower of Pisa that rejected Aristotle's law of gravity (Flyvbjerg, 2004).

The theory outlines specific trends in market demands and tendencies in the developments of the production organization. During the interviews one question for each trend or tendency

was asked in order to test the theory. The answers from some of the leading figures in the companies are compared and contrasted with what the theory predicts. Both findings supporting the theory of modularization, and the ones rejecting it, are presented. As always in qualitative research due care must be taken so that the researcher is not biased towards supporting the theory presented. In other words, all evidence pointing towards the discounting of the theory is presented, so that an informed and unbiased conclusion can be written. Another issue that is dealt with in the discussion is the degree to which it is possible to draw conclusions. In quantitative research this can be measured by statistical tests, such as number of standard deviations, tests of statistical significance, T-scores, F-distribution, etc. In qualitative studies, the support for and against a theory is harder to analyze, since there are no uniformly accepted standards. Spencer et al. (2003) writes that there is now much better documentation of the different approaches to carrying out qualitative analysis, but that it stops short of describing how classification and explanations are achieved or how hypotheses or theories are generated. "In other words: there is now much greater visibility about how qualitative data analysis is 'managed' but rather less about the intellectual processes involved in 'generating findings' from the evidence collected." To give the reader an understanding of how the findings in this thesis were generated, the following principles, outlined by Spencer et al. (2003) for understanding and interpreting substantive meanings, will be adhered to in the analysis:

- *Remains grounded in the data:* The ideas and concepts that emerge should be rooted in the data and not superimposed.
- *Permits captured synthesis:* Reduction of the data at hand has to be carefully handled so that the original terms, thoughts and views of the study participants are not lost. Emphasis should be placed on capturing the synthesis, that way the findings can also be traced back against the original material.
- *Facilitates and displays ordering:* Organize and sort data so that it can be inspected in related blocks of subject matter.
- *Permits within and between case searches:* When searching through the analytical data for defining characteristics, clusters, associations it is important that the researcher can move through the whole data set so patterns can be found. There are three different types of search that can be made:

- *Thematic* categories and patterns *across* different cases.
- *Associations* between phenomena *within one case*.
- *Associations* in phenomena *between groups* of cases.

4.2 Reason for using the package tour industry

Technology changes the chain of distribution in many service firms, and with it the market demands put on the companies. Sundbo's theory deals with these changes, and specifically includes a separate part on mass-producing service firms. In order to test this theory it was necessary to find a mass-producing service industry where technology plays an increasingly large part of the distribution chain, and the market forces at the same time offers the consumer more choice, information and power. The packaged tour industry was chosen because it fits all these criteria. It is a sector dominated by mass-producing service firms that, according to the hypothesis, will have to undergo substantial change and use innovation in order to respond to new market demands. Smaller, more nimble competitors are challenging the predominantly vertically integrated business model. Additionally, it is a large sector in the economy that is relatively under-researched in Norway. The dominance of a few large players, it could reasonably be said that it is an oligopolistic market, means that the vast majority of the market can be examined within the scope of a master's thesis.

Another interesting aspect of the package tour industry is that almost everyone has a relationship with it. Few people have never taken a package tour holiday, and everyone has an opinion on what constitutes good and bad service. The product is consumed as it is produced, and since it is a product with high involvement, from choosing the type of vacation to the physical usage of the service, the customers demand good services and give feedback, especially if they considered the service to be inferior to their expectations. The package tour companies also sell their service mostly to end consumers, prompting them to undertake substantial customer research. This in turn should provide the interviewed managers with a good sense of direction of where the industry is headed in the future.

5. Overview of the Package Tour Industry

5.1 Introduction

Package tours are a major industry throughout the world, particularly in Europe. Growth came very quickly for the first firms, especially those who started sending sun-hungry Northern and Central Europeans to countries around the Mediterranean by airplane. The market for affordable holiday travel proved vast and expanding as disposable income grew. The industry in Europe and Scandinavia is now becoming more and more concentrated with a few companies dominating the market. There are some obvious economies of scale that can be leveraged across markets, but customers themselves are very diverse from one country to the next, causing many managerial challenges (Roper et al., 2005). This chapter describes the package tour industry on a European and Norwegian level, highlighting some of the biggest challenges facing the industry.

5.2 The package tour industry in Europe

5.2.1 History

Apart from the first organized tours (In 1841 the company Thomas Cook chartered a train to take a group of protestors from Leicester to Loughborough, twenty miles away) and subsequent ocean voyages, train trips etc., the package tour industry, as we know it, combines charter flights or long-haul bus transportation with transfer and accommodation. Most tour operators also offer additional services such as excursions, guides and entertainment. In 1950 Vladimir Raitz pioneered the first mass market packaged holidays abroad from the UK with charter flights from Gatwick Airport to Corsica (Wikipedia – Package Holiday). Nordic air charter was born in 1953 when the Swedish company Svensk-och Bussenresetjänst sent a chartered DC3 with 32 passengers from Bromma to Hamburg, where they had busses stationed (Roper et al. 2005, 195). By the late 1950s and 1960s packaged tours offered regular people in Britain the first affordable travel abroad (Wikipedia – Package Holiday).

Since the 1970s charter air travel has become the dominant driving force in European leisure travel by offering a low cost alternative coupled with convenient connections. Laws (1997) argue that no mass-market tourism destination can attract enough visitors to support a full tourism infrastructure development without charter flights (Buck and Lei, 2004). The package tours are sold through various channels; travel agents, direct by phone or over the Internet are chief among these (Wikipedia – Package Tour).

The Danish clergyman Eilif Krogager, who lived in Allerup, close to Tjæreborg, arranged the first packaged tours in Scandinavia. He noticed that Danes were keen on exploring Europe in the after-war years, and in 1950 he hired two busses and took the first Scandinavian packaged tour tourist to Spain. A year later he formed his own bus company, Nordisk Bustrafikk (later Tjæreborg) (Wikipedia - Pakketur). The company quickly grew and by 1959 had 80 busses; the first prop planes were bought in 1962 and went into service between Denmark and Las Palmas in Gran Canaria. Tjæreborg built their first resort in 1968 in Spain (www.tjaereborg.dk). Charter tourism continued to grow despite setbacks and difficult conditions in the 1970s, with unfavorable political conditions in major destinations such as Greece, Spain and Cyprus. The price of goods and services also rose in conjunction with the oil crises of that decade and the Arab-Israeli war (Roper et al., 2005).

5.2.2 Development and consolidation

Charter tours to overseas destinations became more and more popular in the 1980s. Companies started to offer trips to Florida and other destinations in America (www.tjaereborg.dk). Many companies came in and out of the business in the 80s, but towards the end of the decade a few large companies dominated the markets. Competition further intensified in the 1990s as some of the large European companies began to require still larger volumes to achieve profitability. Since scope for growth in the home markets was gone, growth came from a wave of cross-border acquisitions (Roper et al., 2005).

In a market concentration case in the European Court of First Instance the package tour industry was divided into two categories, short-haul and long-haul flights. Short-haul flights were deemed to last not more than 4 hours, and everything else is a long-haul flight (The Court of First Instance). This is a relevant definition in regards to segmentation of the market, but mostly it is important in regards to strategic acquisitions and mergers, since market power is typically in the hands of a few large operators.

5.2.3 Profitability – Costs and Income

In 2003 the typical profitability for major UK tour operators is just 3,5% of turnover. This means that for a typical 350 GBP holiday, the tour operator only makes about 12 GBP (Buck and Lei, 2004). Other sources mention better numbers. Datamonitor (2005) writes that the industry average for the years 2001 to 2005 was:

Operating margin	14,8%
Net profit margin	10,8%
Return on average assets	4,9%
Return on investments	8,7%
Return on average equity	20,8%

Table 2 - UK Tour Operator Profit Margins

Right from the start package tour companies' main goal has been to cut costs, thus increasing the number of people who can afford to travel with them. In the early days the tour operators used older-generation airplanes that were bought cheaply. Later, when the number of customers increased and the tour operators started serving long-haul destinations they switched to modern aircrafts, today typically Boeing 757 and Airbus A320, in order to cut unit operating costs and improve quality. New planes also helped the image of charter airlines. In fact, charter tour operators have a higher intensity in the usage of their planes than most scheduled carriers (see table 4). Charter airlines also have substantially more seats in each plane, typically an Airbus A320 in scheduled flights have 149 seats whereas charter airlines cram 180 seats in. This coupled with the high load factor (percentage of seats sold per flight) of around 91% results in very low flight costs, fully 10% lower than the no-frills airlines. Scheduled airlines usually have load factors of 70% – 80%, see table in appendix. Charter airlines also operate intensely achieving close to 24 hours of operation a day during peak season (Buck and Lei, 2004).

5.2.4 Major players

TUI AG – The largest tourism group in Europe with about 22 million customers and 19,6 billion Euros in turnover in 2005 (this also includes revenue from shipping activities). It has a vertically integrated model, encompassing nearly 3600 travel agents, 279 hotels, and 116 aircraft. Among the most known brand names are: Air Tours, Star Tour, Thomson, and Arke. It operates several airlines, among them Corsair, Hapag-Lloyd Flug, Thomsonfly, and Britannia Airways. TUI AG has had profitability problems lately, with 2% operating margin and 1,4% net profit margin in the period from 2001 to 2005, well below industry average.

MyTravel Group plc was established in 1972 and has enjoyed rapid growth since then. They serve about 6 million customers every year and have many well known brand names, including Airtours Holidays, Panorama, Direct Holidays, MyTravel, Saga Solreiser, Ving, Tjæreborg, Skibby Rejser among many others (Mytravelgroup.com, 1). MyTravel has recently completed a financial restructuring, after many years of substantial losses.

Kuoni Travel Holding Ltd. is one of Europe's leading leisure travel corporations, and has been in business since Alfred Kuoni founded the company in 1906. Kuoni has branch operations in 27 countries and a turnover of about 2.37 billion Euros. They operate with several well-known brands, such as Kuoni, Apollo and Voyages Jules Verne among others (Kuoni, 1). In their mission statement Kuoni says: "We motivate our staff by encouraging entrepreneurial spirit and innovation at all levels" (Kuoni, 2). In the years 2002 to 2004 Kuoni made small profits, and suffered a small loss in 2005.

Thomas Cook AG is, according to their website, the number two tourism group in Europe, with 7.7 billion Euro in turnover and 13.2 million customers. It is one of the best-known leisure travel brands in the world. They have 2400 travel agencies, 76 aircrafts and 33 brands (among them: Neckermann, Aquatour, Condor). The company is owned by Deutsche Lufthansa AG (50%) and KarstadtQuelle AG (50%) (Thomas Cook AG). It has returned to profitability in 2005 after many years of poor performance.

Profitability Numbers Package Tour Companies
In millions of Euro
TUI Group AG

	2005	2004	2003	2002
Turnover	19619	18046	19215	20302
EBITA	849	912	1072	805
Group profit	495	572	315	41

MyTravel Group plc

	2005	2004	2003	2002
Turnover	4281,2	4575,6	6026,5	6969
EBITA	30,5	-131,9	-1061,6	-146,5
Group profit	-61,2	-269	-1313,4	-95,6

Kuoni Travel Holding Ltd.

	2005	2004	2003	2002
Turnover	2366,8	2319,9	2113,4	2572
EBITA	77,3	82,7	65,7	83
Group profit	-26,9	48	42,3	19,7

Thomas Cook AG

	2005	2004	2003	2002
Turnover	7661,2	7478,8	7241,5	8062,6
EBITA	193,2	22,1	-79,1	62,2
Group profit	105,4	-176,4	-251	-119,5

For MyTravel GBP converted to Euro at interbank rates at end of financial year dates
 For Kuoni CHF converted to Euro at interbank rates at the end of financial year dates

FxConverter at www.oanda.com (FxConverter).

All numbers come from the respective corporate websites (Profits 2002-2005).

Table 3 - Package Tour Operator Profitability

5.2.5 Trends in the package tour industry

Charter airlines increasingly face competition from low-cost airlines on some of their routes and no-frills, low costs carriers have started to eat into charter airlines' market share. Part of the reason is that charter companies normally give limited flexibility in choosing departure dates, and almost no choice in choosing return days. On key routes from the UK to Palma,

Malaga, Alicante, Faro and Ibiza the charters' market share decreased from over 90% in 1998 to 75% in 2001 (Buck and Lei 2004: 76). In order to compete with this new threat MyTravel launched a no-frills airline MyTravelLite in October 2002 (which was later aborted) and TUI AG has teamed up with Germanair to launch the low-cost carrier Hapag-Lloyd Express in Germany. Seat-only sales have also been growing quite fast recently. On the busiest routes, more frequent flights have been scheduled, allowing for more choice of start and return dates for the customer. A few charter airlines have also adopted the low-cost carriers method of selling the first seats cheap and then increase the price as the date of departure comes closer, instead of the normal charter pricing method where the seats are expensive in the beginning and then lowered as the departure date approaches. There are many pitfalls for the charter airlines in adopting such strategies, and the mix must be well managed to avoid increasing sales costs and lower load factors. Maintaining this balance is one of the principle challenges in the years to come (Buck and Lei, 2004).

Table 2: Aircraft utilisation rates, UK scheduled and charter airlines, 2002

<i>Airlines</i>	<i>Average daily utilisation (hours)</i>	
	<i>Boeing 757</i>	<i>Airbus A320</i>
Scheduled:		
British Airways	7.2	7.1
British Midland	–	8.6
Charter:		
Air 2000	9.2	12.0
MyTravel Airways	10.7	11.5
Britannia	10.0	–
Thomas Cook Airlines	11.3	9.8
Monarch	8.2	9.2

Source: CAA, 2003; Compiled using CAA (2002) data.

Table 4 - Aircraft Utilisation Rates in the UK

Buck and Lei (2004)

Package tours have lost substantial market share since its heyday. In the UK in 1994, of 27 million holidays, 15 million – 56 percent – were packages. In 2004, some 43 million holidays were sold, of which 20 million – 46 percent – were packages. This means that while the market in the UK has grown by about two-thirds, the package tour sector increased by only a third, also the 20 million in 2004 is lower than in the years 2000, 2001 and 2002

despite the attacks of September 11 and the impact it had on the travel industry (guardian.co.uk).

As previously mentioned, margins are wafer thin in the short haul mass-market, due to competition among the tour operators, but also from low-cost carriers. However, low cost carriers seem to have a natural 4-hour flight time limitation. This has prompted many tour operators to make changes to their product mix, introducing more profitable long haul routes to destinations seen as more exotic, such as Turkey, Thailand and Brazil. This cannot be done overnight, as they need new airplanes and access to substantial tourism infrastructure, but it is well underway.

The composition of the tourist population will change, with increasing proportions of senior citizens. The consumers will place greater emphasis on individual/self-determined holidays, and on educational and more active recreational pursuits (Moutinho, 2000).

Dynamic packaging (sometimes referred to as the modular travel market) has been a hot topic in the package tour market for a while. Dynamic packaging allows the customers to choose their own flights, accommodation and car hire, usually from only one seller or as part of a package. The pricing of dynamic packaging is always based on current availability, and add-ons such as airport parking and show tickets are often available. Putting together and ordering a dynamic package tour is in most cases done online (Wikipedia, keyword: Dynamic packaging). Trisept Solutions, a technology company that sells dynamic packaging infrastructure, says the difference between a vacation package and a dynamic vacation package is that the latter is a vacation package where the travel components originate from two or more separate inventory management systems. It is important to notice that the customer is not necessarily aware of where the inventory originates, and receives a single priced itinerary. The goal is to offer the customer a very large selection of inventory to choose from, while at the same time making the whole experience seamless (Trisept Solutions).

There are four major contenders in the battle over dynamic packaging, each with its set of challenges and opportunities:

Traditional Tour Operators

- The traditional static package does not offer the kind of flexibility sought by many consumers.
- The companies will face an ever-increasing threat to their core business unless they embrace the new architecture for dynamic packaging. This means they have to upgrade their systems to handle complex online packaging from multiple suppliers.

Traditional Travel Agencies

- Standard commissions are being cut, and many are focusing on cruises and tours as a new revenue stream.
- Some travel agencies embrace a wholesale/retail model pioneered by the online travel agents.
- Essentially, an online travel agent just tries to duplicate the traditional travel agent agency-customer relation through a web-browser, but most traditional travel agents have no system in place to capture the offline interaction with the customer.

Online Travel Agencies

- Online travel agents have quickly moved in on the packaged tour market to increase their revenues.
- Pioneered the concept of a combined retailer/wholesaler.
- Must now create the next generation of a dynamic packaging engine.

Suppliers

- Are capable of launching their own dynamic vacation planning tools on their sites.

- See the opportunity to have a supplier-driven relationship with their best customers. They also have to shore up their brand-values by entering the vacation planning market.

(Rose, N., 2004)

5.3 The package tour industry in Norway

5.3.1 Tour operators and their structures

There are four principal players in the Norwegian package tour industry, owned by three of the largest leisure travel groups in Europe. The ownership trail of the main package tour brands in Norway can be seen below:

Table 2. Ownership trail of main package tour brands in Norway.

Brand	Origin	Ownership changes over time
Star Tour	Stjern Resor established in Sweden and launched the Star Tour brand in Norway in 1973 (prior to this the brand operated in Norway but from a base in Sweden).	<ul style="list-style-type: none"> • Acquired by Fritidsresor (Sweden) in 1980. • Fritidsresor acquired by Thomson Group plc (UK) in 1997. • Thomson acquired by Preussag (Germany) in 2000. Now known as TUI AG.
Ving	Ving Resor established in Sweden, 1958.	<ul style="list-style-type: none"> • Acquired by SAS (Sweden, Norway, Denmark) in 1971. Re-structured as Scandinavian Leisure Group in 1989. • Acquired by Airtours plc (UK) in 1994. Now re-named MyTravel plc.
Saga	Saga established by Braathens airline in Norway, 1959.	<ul style="list-style-type: none"> • Acquired by SAS (Sweden, Norway, Denmark) in 1989. Re-structured as Scandinavian Leisure Group in the same year. • Acquired by Airtours plc (UK) in 1994. Now re-named MyTravel plc
Apollo	Apollo Resor established in Sweden in 1986.	<ul style="list-style-type: none"> • Acquired by Kuoni (Switzerland) in 2000.

Source: Range of company data.

Table 5 – Ownership trail of package tour brands in Norway

(Roper et al., 2005)

Together these four brands have a 94% market share, and as seen in the table below the only major shift in the last years is the growing market-share of Apollo, a relatively late entrant to the market.

Table 3. Leading tour operators in Norway 1998–2002.

	1998	1999	2000	2001	2002
Star Tour	42%	39%	39%	38%	34%
Ving	30%	28%	26%	25%	24%
Saga	25%	24%	23%	23%	24%
Apollo	–	6%	7%	9%	12%
Others	3%	3%	5%	5%	6%

Source: Adapted from <http://corporate.fritidsresor.se/templates/Page.asp?id=2111>. Retrieved on 9 November 2004.

Table 6 - Market share developments 1998 - 2002

(Roper et al., 2005)

5.3.2 Customers – who are they

Roper et al. (2005) found some characteristics applicably to a relatively large population of the Norwegian customers:

- They seek security (i.e. like having guides, transfer etc.) and want sun and beach holidays with good weather.
- Give holiday travel high priority, are well educated and likely to enjoy active holiday activities.
- Some come from remote areas and/or are part of a fast ageing population.
- Are aware of their nationality and traditions and carry this with in them in turns of the demands they make. They behave similar to home and expect the destinations to accept this behavior.

StarTour says 75% of its customers are couples, the rest are families with children (Finansavisen, 2006).

5.3.3 The package tour value chain in Norway

This sub-chapter is based on Roper et al. 2005

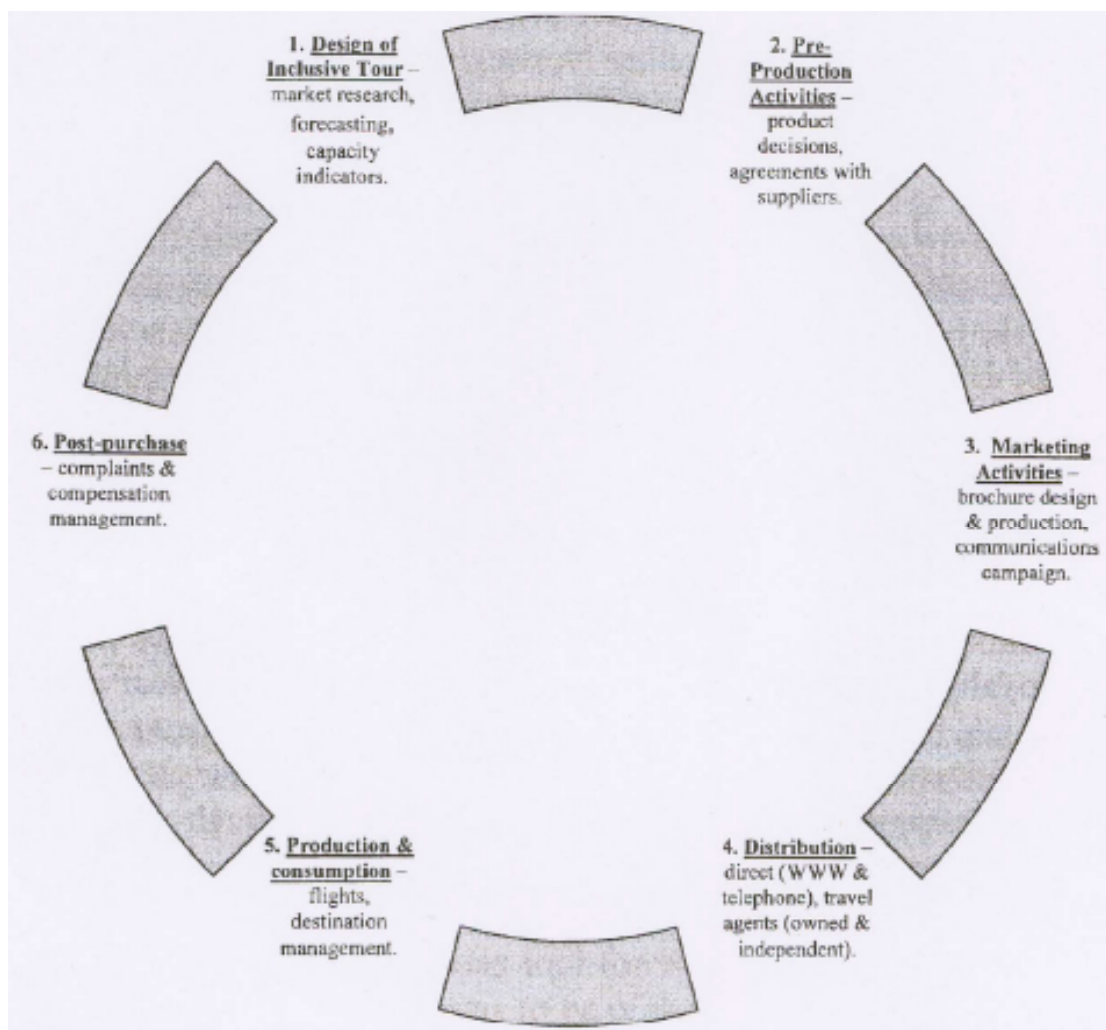


Figure 3 - Activities in the package tour value chain

The research was based on a multi case study research strategy with data collected from interviews, secondary data sources and document analysis encompassing the four leading brands, Ving, Saga, StarTour and Apollo. The researchers identified six stages in the 12-18 month cycle of designing, distributing and producing/consuming Norwegian package tour products.

Design of inclusive tour

The offices of all the four leading brands conducted market research and forecasting in-house to decide on the capacity and content of tours offered in the coming one or two seasons. The most important data related to price, customer preferences and macroeconomic

forecasts. The companies often segmented customers into categories such as “family market”, “ticket-only” and “lates market”. In the end though, the Norwegian companies were primarily driven by flight capacity from Norway to the destinations, as they had to take into account the number of flights they had to fill during a season.

Pre-production

The regional headquarters, located in Stockholm for all four brands, made the pre-production decisions and activities. The Norwegian subsidiary prepares a request based on the design stage, outlining the destinations, destination services, resorts, types of accommodation – the product mix – and then sends it to the regional headquarters for processing. The proposal was evaluated and final decisions were made as to which destinations would be serviced and at what price in negotiation with the Norwegian office. Effectively the Norwegian organization buys services from the regional headquarters. This offers less flexibility for the national organizations, but ensures that economies of scale are taken advantage of. Central coordination also ensures that capacity shifts between Scandinavian countries are possible.

Marketing activities

The main marketing channel for the package tour companies is the venerable brochure, although the Internet is taking over more and more. The main brochure is launched in October and substantial efforts go into all aspects of the brochure’s appearance. Most Norwegian customers are unaware that foreign companies own the four leading brands in Norway, something that is reflected in the main brochures since they all use the Norwegian brand names Ving, StarTour, Saga Solreiser and Apollo.

The webpage designs are made using an international platform, with local discretion in layout aspects and content. The pages are all in Norwegian. Other marketing activities were made locally, or used international ads that were localized by translation to Norwegian.

Distribution

There are three main distribution channels, direct with the tour company by means of telephone or Internet, or through the travel agents. Competition is fierce and travel agents usually only sells trips from one of the companies, due to contractual clauses and the fact that many of them are owned by the tour operators as part of their vertical integration strategy. All competitors agreed that a presence in high street was necessary for sales,

branding and gathering first hand market data. Sales are shifting more and more towards the direct channels, especially the Internet, but this is a gradual process.

Production and Consumption

Package tours are produced and consumed simultaneously. The companies are integrated backwards by owning airlines, transportation companies and accommodation at the resort, but they also frequently purchase these services from other companies. This leads to co-production where several companies provide parts of the product, but the tour operator is responsible, and bears the risk, for the overall product quality. Purchase of additional components is handled regionally.

Many customers seek security, and as a result the companies all have tour representatives at the locations. Since it is deemed sufficient that the tour representative is of Scandinavian origin due to similar languages, this part of the product is also regionally coordinated. General management at the destinations showed an increasing tendency to be taken over by corporate level employees, i.e. managers from Kuoni, MyTravel etc. This is a real benefit of being part of an international group, and increases the service level at the destination.

Post-purchase

The large package tour companies handle complaints from their own customers in Norway, and there is also the option of treatment in the trade association. The trade association says complaints are rising proportionally faster than the number of tours sold. Most complaints involve the hotel standard or travel delays.

6. Analysis

6.1 Introduction

Since the primary concern of the analysis is to prove or disprove the theory presented in this thesis, the layout will follow the original layout of the theory in detail. Each point will be described and discussed, the conclusions and implications that can be drawn from the discussions are to be found in chapter 7. The analysis is mainly based on three interviews. The interviewees have opted to stay anonymous since the number of senior managers in the industry in Norway is very small.

6.2 Trends in market demands on service firms and the service firms' reactions

6.2.1 More possibilities and increased market competition

M1 and M2 stresses that the market for packaged tours have remained steady for the last three or four years, at around one million passengers per year, in spite of increased competition from low-cost carriers. The internal competition in the marketplace is high, but in many instances they also have to compete with other forms of vacation for each Norwegians pocketbook. M1 feels that there is also a perception among customers that low-cost carriers are very cheap since they advertise fares as low as 1,- NOK for a Ryanair flight, even though the vast majority of seats are nowhere near that price. This leads to a problem for the package tour operator in how to price his vacations and communicate the added value a package tour has over individual booking. M2 states that, with the advent of the low-cost carriers, seat-only capacity has gone up dramatically leading to over-capacity and further pressure on the margins.

Manager M3 thinks the barriers to entry are higher today than they used to be, and that in the end the competition between the companies is as much about the financial strength of their parent companies as anything else. Hypothetically, (and without consideration of the legal aspects of such business behavior), the companies with financially strong parents could

easily squeeze at least one of the competitors from the market. This is also the reason many of the small tour operators are for sale; they simply have no chance to stand up to the big three if they start encroaching on their turf (M3).

As written in chapter 5.2.2 – Development and consolidation, the early years of the business was dominated by entrepreneurial firms trying out different business models, as predicted by the theory. The consolidation seen in later years led to increasingly fierce competition, leading up to the point described here, where the big are staying big, and it is difficult to survive as a small operator. Quoting from Sundbo 1994 “However the opinion of the service firms is, generally, that the increased competition will continue and that it will be harder to exploit the possibilities in a new period of recovery than it was at the beginning of the 1980s”. Another example of the strong competition in the market is the relatively low profitability in the industry, with small margins, especially for off-season trips and standard packages. The industry is now past the mature point and, one might argue, also past the consolidation phase. Usually this state doesn’t end until a semi-radical or radical innovation comes along to challenge either the business model or the technology or both, enabling a challenger to change the nature of the business and the industry. A potentially semi-radical innovation could be a new generation of dynamic packaging software and Internet-based travel agencies. The advent of Web2.0, with its open source attitude, and the sharply declining cost of network hardware, means enterprising entrepreneurs could quickly set up online travel agencies that use auction based models and build communities around their travel agency to keep customers and get a hold of large amounts of valuable customer data.

6.2.2 Price as a central competition factor

The companies in the Norwegian package tour industry have a slightly different strategy, with some going for low-cost vacations, while others tend to offer a slightly higher standard at somewhat higher rates. Nonetheless M1 and M2 both stress that price competition will become more important in the years to come, and most likely two segments will emerge. The first segment will have rock-bottom prices and compete mainly on price, whereas there will also be a segment where companies can charge a little extra for certain service elements, but also compete on price, albeit within their category, more of a best-buy focus.

M2 says the market clearly responds to price, but also to quality, and the company that is best able to keep costs down while at the same time develop their products will win. This

means there will continue to be a strong price-pressure in the business. In addition, having low prices is important to get customers in the first place.

M3 also stresses the two-segment approach, with competition in one segment almost exclusively on price, while the second segment will pay extra for certain services, but only the ones they want and decide to pay for. In the end he predicts that with increased wealth in Norway, people are going to want to pay for comfortable apartments, oceanfront settings and convenient flight times.

The latest entry into the Norwegian market is Apollo in 1999 (acquired by Kuoni in 2000). In order to gain market share quickly they had to undercut the competitor's prices, and since you lose money in the first years it is important to have sound financial backing. This is partly because you need to have a certain market-share in order to business in the first place, and partly because the market responds well to price. Interestingly M3 (partly M1 and M2 also) focuses on a two-tier solution, where one part of the market will remain very cost conscious, and the other part will assess both quality and price, something a large number of customers are able to do due to their experience in buying package tours.

With distribution through the Internet, it is very easy for the consumers to check the prices of the competitors, and at the same time access much more information about hotels and the area they are in. Distribution through the Internet allows the companies to continually alter the price of their vacations using yield management techniques, much like the airlines do today. This transparency fuels price competition and enables the consumer to better assess the quality of the product upfront.

6.2.3 Demand for increased productivity

M1 thinks they have become considerably more productive in all areas. They have become much better at analyzing "What do we want to spend money on?" After a merger some years ago they had 270 employees, now they are only 100, but doing basically the same job as before. Considering that personnel are a large cost in services, this is a tremendous gain. The biggest contributor to these gains is the Internet as a new distribution channel. He assumes that they will have an Internet sales ratio of about 75% in two to three years, a number closely echoed by others in the business. Predicting beyond this number is hard given the large number of customers, and the fact that not everyone is comfortable with navigating the

Internet, much less making a purchase online. Nonetheless, the need for face-to-face customer contact in the package tour industry is waning.

M2 states that Scandinavian workers are among the most productive in the world. He thinks that as the Internet takes more and more sales they are able to free up people in other channels, such as phone and high street shops, and so do more one-to-one sales or proactive sales, using capacity better and thereby increasing the activity level in all sales channels. He also thinks the package tour companies will use more channels to communicate with customers such as SMS and via the Internet but on different types of terminals (i.e. handheld devices, game consoles, etc).

M3 stresses that although productivity has gone up, it has also become more “square”, meaning that for the customer who fits into the “charter box”, leaving on a Sunday and coming home on the following Sunday and enjoys it, the industry is very efficient. The more combinations and freedoms a company includes during a trip, the less efficient they become.

Productivity and increased competition and price pressure goes hand in hand. All three interviewees state that productivity has gone up. Although productivity in services is difficult to measure, the fact that 100 employees now do the same job 270 people did only a few years ago is testament to a significant increase in productivity, especially since the number of passengers has been stable over the last years. It is clear that the Internet is a much more efficient sales channel for standardized products than having physical shops. However, in some of the service encounters, such as the work done by tour guides on an excursion, increased productivity will be harder to come by.

6.2.4 Demand for quality

M1 says the industry delivers much better quality now than they did 10 or 15 years ago. They monitor quality through comprehensive customer surveys, measuring value for money and perceived quality in relation to price. The customer is demanding and the competition brutal so they have to pack a better, or at least as good a, vacation than the customer can do themselves on the Internet, this means that they continually have to improve quality to stay ahead in the game.

Charter flights now offer the best service of all airlines, except business class, according to M2. He says there has been a clear development in the industry towards better quality, and

that customers demand better service now than before. At the destination, the demand for good quality entertainment and food is increasing. Customers also expect more to be included in an all-inclusive vacation package, and that everything is predictable. The customer wants to choose between different concepts, so the demand for clear concepts and quality is increasing.

For M3, the biggest development is that the customer wants much more freedom than before. They want the practical aspects of charter, a flight from A to B and cheap accommodation as a result of the large volumes the package tour companies buy before each season. The companies have responded in turn, allowing customers to choose whether or not they want transfer or rent their own car, they choose more themselves than in the past. He thinks customers want to be left alone, but receive excellent assistance when they want, instead of having a tour guide knocking on the door every day asking the customers if they want to see a show or take part in the excursion of the day.

As M1 says, the competition is now so fierce that the companies simply have to focus on quality to remain competitive. Companies also increasingly ask their customers what they want and monitor quality through customer surveys. As evidenced in section 6.3.5 standardization is not only a tool for efficiency, but also ensures a consistent quality, something that would imply that the customer is more likely to get what he/she ordered, which is the benchmark in this case since hotels have different ratings. Expensive hotels with a higher rating is regarded by the customer as being of higher quality, so it is important to remember that in some areas of the product, a relative quality concept must be adopted. This is underlined by M2 who states that customers now demand perfect predictability in the service offering. Another quality aspect that M3 notes is the ability for the customer to choose which parts of the service they want, and then pay only for that, something that ties in to the core of the modulization concept.

6.2.5 Development of strategies

M1 says that the use of strategies have changed mainly the distribution area. The production strategy is basically just filling the planes they own and controlling attractive hotels in attractive locations. They have a load factor of about 98,5 %, far better than low cost carriers. Recently, instead of selling the total package from A to Z, they picked out elements to make options available to the consumer. This raises the distribution issue and has lead to

increased internal control of the production. Travel agencies are an expensive sales channel since they take a cut out of all sales they make, and the travel agent employees have to know 18 – 20 suppliers which transfers into around 12 booking systems, whereas if we sell directly, our own employees have to be experts in just one or two products and work exclusively with our booking system, says M1. You get much better service by booking directly and this has influenced the distribution strategy.

Increased competition leads to an increased need for strategy, according to M2. Things are moving much faster today than they did before. The focus on winter and summer season is very production oriented, created by the industry itself. One can now imagine advertising the future travel program online continuously as hotels are contracted. This means that in the longer term, pricing strategy becomes extremely important, whereas in the short-term launch dates will matter more. This means that you have to “live the strategy” and work very closely with them. It takes about two and a half years to bring a new destination on stream, so that frames the long lines, but things change more quickly now so this period is getting condensed, while we live the strategy in the short run.

M3 focuses on the availability of new and better management tools, especially in the financial management field. This means companies can see earlier if they make money on a destination or not, leading to non-profit making destinations being dropped earlier than they would have otherwise.

Strategies are more important now than ever, since the market place shifts rapidly there is a need to live the strategy. M1 says that the distribution strategy is especially important, and that this has led to increasing internal control, making the process more standardized. This strategy has led to trying to shift the distribution channel into the company, meaning that they try to minimize sales through travel agencies, both to cut costs and to ensure a high quality standardized approach. New financial management tools also mean that a strategy can be evaluated and changed much faster, leading to better control as the markets move faster.

6.2.6 Innovation and renewal

They have no specific innovation team or department in Company 1, but they say they encourage all employees to participate by coming up with new ideas. As a company they feel

that they try out many new ideas and quite forward-looking, possibly so much so that the analysis beforehand is insufficient, but M2 says at least they are not afraid to try. It is all about monitoring what the customers want and then try to adapt to those demands. This is especially noticeable when it comes to hotel concepts and innovations, such as bigger apartments, bunk beds for children, spas or activities in the hotel. They also tried adding a sort of “business class” on their planes after customers complained about legroom, it turned out that when it came down to it, customers were not willing to pay for it. Part of the problem is that the aircraft feels crowded and small due to the high 98,5% load factor, whereas seat pitch in reality is the same as most commercial airlines have. All in all there are many opportunities to develop products on the foreign side of the business.

Another innovation is to drop price lists since the market for vacations is a spot market, comparable to a stock exchange. The company has also gotten a long way towards eliminating their very expensive catalogues since they discovered that 90% of their customers seek information on the Internet before they travel anyway. They also moved aggressively to electronic documents, 75% of customers no longer receive any written materials when they order a vacation. Customers can also check in using check-in machines. This frees up many resources that can be spent on more relevant and up-to-date information on the web, as well as lowering prices.

Company 2 started a systematic innovation program in the mother company last year to foster and develop new ideas. The local organization in Norway then started its own program to work with the results of this innovation program. The organization of it is ready and will be implemented in January 2007. They will have idea campaigns for the different strategic areas and use that as an innovation tool. There was no system in place before, and those who had an idea did not have a system to support them in sharing it.

Manger 3 states that the industry is becoming more and more boring every year. Everything is squarer, there are fewer and bigger destinations and he feels the industry is less risk taking than it used to be, but says his company are still experimenting with various smaller destinations. The pioneering times are over and the national companies have to send profits to the group. Small destinations are expensive to run and get cut from the programs.

Company 1 seems to follow a classic ad hoc approach to innovation in the service industry where all employees are expected to come up with novel ideas, and there is no management-

initiated system of storing, analyzing and implementing new ideas. They have however taken the innovative step of removing price lists, but it is not clear whether this is an intentional innovation or the result of market forces. Company 2 on the other hand is working consciously to implement a systematic innovation in the organization, in sharp contrast to their previous non-systematic ad hoc approach. Interestingly they are dividing up the projects according to strategic area, something that may well support a modulization approach. Manager 3 feels that industry is moving away from experimentation, and as such is less innovative. They don't have a systematic approach to innovation in Scandinavia, but there is a department at headquarters devoted to it.

6.2.7 More technology

New technology has not only influenced the distribution channel, but also brought a new breed of workers into the organization, according to Manger 1. In certain departments the employees are a much more technology oriented than before. They think the Internet before print material, they use different jargons than we are used to and communicate differently. Company 1 has worked consciously towards having an Internet platform running as a thread through the company, and not only in the customer interface, but in the whole organization. The intranet is now the primary means of communication between company employees.

M2 stresses that the most important thing that can be achieved with new technology is what they can do for their customers. They are also continuously developing their system in order to produce new products, such as splitting up the package tour into just flights and just hotel, enabling them to use yield management even more efficiently. Technology is also used to recognize the customers and find out how to better serve their needs. "Really, in all areas, technology plays an extremely large role for us, from production via mid-office and all the way to the customer". According to M2, the systems becomes of vital importance since they "don't really sell goods, it's more of an immaterial product, a service".

M3 feels the package tour industry lags other industries in using customer data, and thinks this has something to do with the fact that their service is infrequently used. Of course, it would be possible to send newsletters and such, but getting information about the behavior of the customers is very difficult. When it comes to using the Internet, the charter industry is very good. It was one of the first industries online. M3's company was online in 1999, and people always ask him why they don't do this and that and the other, send letters and

catalogues for example. The trouble is the lack of customer data, and also the cost of communicating with the customers, since the margins are so low in the industry. This is the reason most companies have started using emails to reach their customers.

It is clear that information technology has had a great impact on the whole value chain in the package tour industry, as evidenced by M2 explaining that technology plays an extremely large role for them in all areas. Company 1 has experienced not only a shift in the value chain due to the Internet but also a shift in the type of people working for the company. Internet-savvy employees, web designers, content managers and programmers are joining a workforce that has been low-tech for a long time. This might help speed up the transition from staid service providers to innovative and flexible market oriented companies. M2 stresses that the most important achievement is what they can do for their customers, a market oriented approach. Company 2 is transforming itself, seeing that technology can help them split the traditional package tour into different parts, and be able to do yield management on it. This goes to show that technology can spur service innovation. As M3 points out, some of the potential of new technology can be difficult to harness in a particular industry because, as is the case with package tours, it is a service the majority of the customers buy infrequently. The local grocery store gets much more and better customer data from their bonus programs than any of the 3 companies represented in this thesis ever will. This shows that technology does not solve all challenges.

6.2.8 Internationalization

The industry has become much more international in the last years according to M1. The companies were initially privately held, also large companies, and people tended to be satisfied when they made a profit, without anyone sitting and calculating the margins and percentages and so on. “Oh, we made a profit this year, that’s nice”, then they were happy. When the entrepreneurs grew too old they sold the companies to financial investors who groomed them and made them ready for the stock market. Eventually they got bought by other corporations and merged. Today there are three large groups, StarTour is owned by TUI AG, which is an old German industrial company, Ving and Saga is owned by MyTravel, which is traded on the London Stock Exchange, and the Swiss Kuoni group, which owns Apollo and is organized as a foundation. Through these ownerships the industry in Norway has become part of a larger international network. This is most noticeable for

people working with accounting and finance, who now report to the larger group entity. The owners mostly leave Company 1 alone, as long as they deliver good results, and M1 thinks the old and somewhat worn adage “Think global, act local” very much applies to the package tour industry.

M2 says the industry has become more and more international because of a desire to utilize resources and systems as much as possible. This again is driven by the focus on costs and economies of scale, and the internationalization is happening faster and faster.

The industry has become considerable more international, and this has happened because of the ownership structure now in place, so M3. Companies owned by the same group share hotels, airplanes etc. 10 years ago there were still many Norwegian and Swedish package tour operators left, today there is only Lilleput left in Norway. The industry has also become much more governed by international groups, with some of the companies having all contracts made out of Germany, some in England and some in Stockholm, depending on whom you talk to.

It is perhaps somewhat strange to speak of internationalization, when the industry business idea is sending people abroad on vacation. However, the industry is international in ownership due to economies of scale, and large international companies have been buying foreign package tour companies with much of the same concept of mass-produced vacations. The theory predicts difficulties in benefiting from economies of scale. This is obviously not the case in the package tour industry, as buying or leasing hotels and airplanes is capital intensive, and airplanes are mobile, making it easy to benefit from sharing. On the other hand modulization should enable the larger leisure travel groups to leverage economies of scale on the new products since they can funnel people from all over Europe to the same destinations. Standardized concepts are also cheaper to run and develop with access to a large market. When it comes to standardization it is important to recognize that although the overall framework and logistics can be the same, customers from the Nordic region might not find the same concepts equally appealing, so some differentiation should be applied.

6.2.9 Mergers and acquisitions

M1 says the main reasons for the concentration of companies in the package tour industry that it requires a substantial amount of capital and carries enormous risk. “In good years it’s

not rocket science to make money in this business, but when the market is butting against you, and you don't have the capital base necessary, it's extremely difficult". Some companies have formed alliances on their own initiative, while others have found out that they can't grow enough organically, and then analyze the marketplace for potential acquisition targets. Interestingly, most companies who were bought don't exist anymore, but there is hardly room for further consolidation today, and the large companies are doing fairly well and are valued quite high by analysts.

M2 focuses on economies of scale, and thinks this is the main reason for the wave of consolidation. You need to have a certain platform and volume to be successful.

M3 notes that the margins are very low, so basically you just make good money during the general summer vacation and Easter, and then some money during fall break and Christmas. During the rest of the year you lose money, or make very little. The other aspect is unforeseen events, like the Tsunami. Most of the passenger base disappeared over night and the company is stuck with airplanes that don't fly. Nothing is more expensive than having an airplane on the ground, it costs about 800 NOK per day per seat in leases and fees that have to be paid, and a small actor has less ability to withstand these incidents that are occurring more and more frequently.

As the theory predicts, one of the main reasons for mergers and acquisitions in the service industry is cost problems. All interviewees agree that this is the driving factor behind the consolidation in the package tour industry. It is easier to withstand turbulence in the markets and unforeseen events when you have capital and diversification through a large program of destinations. Small niche actors cannot hedge risk nearly as well through their operations. The other explanation in the theory, access to knowledge and service concepts, is more dubious since almost all the smaller companies bought to make the larger national companies are fully integrated, without retaining their own brand name. Their knowledge is transferable to the buyer, but service concepts are harder to transfer, and lose some of their value if the brand name associated with it disappears.

6.3 Developments in production organizations related to modulization in mass-producing service firms

6.3.1 Large-scale operations

There are both positive and negative sides to large-scale production, according to M1. To a certain extent you can lose sight of the individual customer, but then again there are many other small operators and actors that are very good at tailoring individual packages to fulfill every desire the customer might have. They sit down with the customer and spend a lot of time to get it just right, and also charge for this kind of advice. We have chosen not to be in this market because there are many others who can do it better. Instead we have a very professional organization in regards to purchasing large volumes. We report our wishes based on our market, and then hotels and airplanes are purchased at the Nordic level, says M1.

M2 says that the obvious positive effect of large-scale production is clout when negotiating with the different destinations. The company can guarantee large volumes, which helps in negotiations with hotels. There are no commercial disadvantages, but, and this is an ongoing discussion, large-scale tourism may spoil a destination.

The large package tour companies have somewhat different production strategies, and we go in for smaller destinations, although we also have to have some large ones as well, says M3. Our business idea is to have smaller destinations, so that when you open the balcony door you don't meet your neighbor back home on the next balcony. The downside of having large hotel units is that the customer doesn't get to experience the country they're in. "I have worked many years in this type of large units where you meet Gunilla from Sundsvall in the reception, you get a menu in Swedish, and then you meet Per from Voss in the bar at night, and then there are all the other Scandinavians, and then you put the kids in a 'miniclub', and then the teenager gets to do a 'teen safari', and then there's bingo in the afternoon, and a show at night". It used to be very good for the industry because it got people who were afraid of traveling to travel. Today it's a bit ridiculous, even though it sells well and many people still want it, it is a downside to having big contracts where you buy entire hotels and run it. It creates a miniaturized Scandinavia, only in the sun.

There should be something genuine about the place you travel to and a travel guide in the background that the customer can call if they have a problem, but they shouldn't contact you and ask if you got sunburn today. One of the industry's problems is that the concept of package tours has become a bit vulgar, but in reality there is nothing more exclusive than charter, since it is the shortest time between A and B, according to M3.

The package tour industry is more concentrated with fewer companies than before, after a wave of mergers. It is much harder to enter the business today than it was before, when smaller companies dominated. Scale economics are very important to stay competitive and a certain size is needed to support advanced booking systems, fill aircrafts and hedge risk. The risk is that the product becomes so similar that it turns into a commodity, where only price is important. It can be argued that buying a vacation is a high-involvement purchase situation and that this will offset some of the standardization elements. Perhaps customers are going to demand new concepts and innovations to the standard package tour as they tire of standardized mass-produced offerings. Obviously, some customers are merely looking for sun and beaches to relax, but as people become more experienced travelers, they are likely to want at least the possibility of doing something more original and authentic.

Mass-tourism has both a cultural and environmental impact on the local and regional community. The issue of how much tourism is good thing will intensify in the years to come, possibly resulting in a change in public opinion and more regulatory measures related to the larger holiday destinations, making mass-tourism less desirable.

6.3.2 Standardization of products in a combination system

M1 says that their products in many ways are standardized, but that they haven't become more or less standardized than before. The products have always been standardized, and this gives the customer predictability, and the airplanes are the same, and the hotels have the same standard and are often located in the same area. There is a general charter tour wrapping, and there are some meta-values that separate the operators from each other. M1 feels that price and service level is what separates the companies the most.

Products are standardized and adapted to a Nordic context, based on the assumption that the Nordic countries are relatively homogenous, but not in a European context. The market and the products in the UK or in Germany are substantially different, according to M2.

M3 argues that the products are standardized since a foreign company owns them, and that they have standards that are equal to or higher than the EU-standard. The demands have become tougher and tougher, and this means that it is probably an advantage for the customer that the operator is foreign owned.

All interviewees agree that the products they sell are standardized, so that the experience for customers choosing the same combination will be the same. M2 points out that this standardization applies to all Nordic customers, as they use the same hotels, the same type of aircraft and transfer modes. There is also some standardization due to EU-demands and foreign company ownership, making many of the back office systems standardized across borders, such as web page layout (not content).

6.3.3 Standardization and rationalization of the production process

According to M1, one difference is that before you often had to pay big advances to the hotels up front to reserve the beds. Today the situation is a bit different, as we don't have to pay out so much in advance any more since there is a bigger spot market now than it used to be. The biggest difference however, is that it goes much quicker. We used to work forever with sending out order lists, travel around and contract hotels. There is much less traveling involved today as most business is carried out over the Internet or the phone. We have also built up long-standing ties and trust with suppliers, enabling us to pick up trends in demand and act on them, whether it be selling unused beds or getting extra beds. It only takes about 24 hours from the time we decide to add another hotel until it's on the Internet complete with pictures, video and description.

M2 says that the production process is much more integrated, continuous and market oriented than it used to be. "Fewer people are working faster and more integrated in the whole organization. It used to be that the product division did its own thing, and then you sort of had to sell whatever they came up with". This was a few years ago, but since then there has been approach where you work very market oriented, also with production. "This has been a very good development, and cost efficiency-wise it's also a lot better". The whole process is faster, more and more continuous and less and less dependent on seasons.

M3 offers some details on changes in the production process. One big difference is that the contractors no longer live in the country of the destinations. Some of the larger groups also

have a joint contracting unit that contracts for all the countries they are represented in. Company 3 does this out of Stockholm, and M3 feels that a Scandinavian knows better what Scandinavians want than a German, even though tourists are becoming more global. Things have also become more market oriented, because the marketing departments, or sales departments know better which destinations the customers prefer than the production departments. Companies also contract whole hotels much more frequently than they did in the past when they often bought eight, nine or ten rooms for the season. The whole process is also faster, both due to electronic communication and the fact that hotels have consolidated into large groups, much like the package tour industry themselves, and this leads to fewer negotiation partners, speeding up the process. The incremental innovations introduced in using the Internet more and more help the industry slash costs across the line.

M2 mentions that there are fewer people working faster and more continuous, an example of incremental innovation in the production process. They have largely done away with seasons, making the production process more similar throughout the year. Another testament to rationalization of the production process is the speed with which a new hotel is incorporated in the product offering, Company 1 at least is able to do this in 24 hours, a remarkable efficiency gain from just a few years back. Contracting has been standardized and now only occurs from a limited number of offices. The speed and ease of electronic communication has played a major part of the rationalization process. Instead of buying a limited number of rooms, buying up all rooms in a hotel clearly leads to a more standardized product.

6.3.4 The separation of production and marketing

According to M1 there is an eternal struggle between people in marketing and people in production. The trick is to balance it out and get people to pull in the same direction. M1 defines himself as a “production guy” and says marketing people are always willing to spend more money than production people, whereas marketing people always think production people are too slow and don’t listen to market demands enough. “This is the way it’s been since I started, a kind of tension, but I think it’s healthy because if you agree on everything and the process is too streamlined you miss out on that dynamic”

In company 2 there has been a recent development to emphasize USPs, Unique Selling Propositions, in the places we are so that we can give the customer a clear and fact-based

explanation of why we offer exactly what we offer. And when we talk about production, we also talk about concept development, and this is very market related since it is attached to target groups and clearly defined needs. When they work with their productions, it's based on leads from a strategy area called Product and Content, and the whole width of the company is part of that steering committee, which also contributes to some product development projects and concept development projects, making the work very integrated. It used to be less integrated, when the strategy areas were less clearly defined, the breadth of participation in this area was smaller, leading to fewer contributions and the market demands and conditions less clear.

Company 3 is very market driven, meaning that the organization in Norway decides which destinations they will sell, how they will market them and at what price, according to M3. He says the market has become more driven by the market itself, although some companies are still forced to sell products imposed on them by headquarters, making it product driven. Companies are much more professional in selling what the market wants today, than they were before.

M3 points out that part of being owned by a large international corporation is that you sometimes have to do what headquarters decide. This is a clear separation of production and marketing, where the production is carried out abroad, and the local organization has to sell it. There has been a shift in the organizations, where previously the production department(s) made a program for the upcoming season and then marketing had to sell it as best they could, all three companies now want marketing to decide the what and the where of the product, and then it's up to production to find out how. Company 2 is also trying to bridge the gap between marketing and production by involving both in strategic planning, something not mentioned in the theory, and a departure from previous efforts where production took the lead.

6.3.5 Specific innovation organization

Company 1 does not have a specific innovation organization. They say that they encourage all employees to think cleverly and come up with new ideas about how they can do things differently. There is no incentive system in place for the employees who come up with viable ideas that are implemented. Three years ago employees didn't feel the organization was listening to their suggestions, but today almost 80% feel that the organization is good at

seizing new ideas and trying them out. “We said that it’s better to come up with ten ideas, where one might be very good, than not come up with any at all”. M1 says they have tested an incredible amount of new ideas, mostly on their webpage, since their employees pick up ideas from browsing the web. “It’s the whole organizations damned duty to be a part of development, and personally contribute to create development for yourself, but also for the sake of the organization”.

Company 2 organizes its innovation according to strategy areas in a predetermined specific way. They have idea campaigns in every strategy area. Based on these idea campaigns they take the best ideas further and conceptualize them with business cases, and eventually projects. There are an enormous amount of ideas that boil down to perhaps one or two projects. For instance, the company has a project going with virtual guides, meaning that there is no physical guide at the resort, but a guide you can contact via SMS, and then you have a call-center instead of the physical presence.

Company 3 has no innovation department or organized group in Norway, but the group has one at headquarters. When they want to explore new destinations the top management team in Scandinavia travels to potential destinations and pick four or five that fits the criteria. They then send a contractor down to investigate prices, security aspects etc. Ideally they would want to ask their customers what they really want, the problem is that they don’t have a good established connection with the customer base, and the customers usually say something like “Oh, my dream is to go to Hawaii, but I always end up going to the Canary Islands”.

Company 1 represents the typical attitude towards innovation in the service industry. They have no specific plans or groups dealing with the issue, and no incentive system, and rely on individual employees to champion their own idea. This makes it difficult for employees who do not have stature, or are simply too modest to champion an idea, to make their proposals known and gain acceptance in an organization. Company 2 on the other hand, behaves as predicted by the theory, and is in the process of implementing a collective process for catching, analyzing and implementing novel ideas and innovations. It can be argued that Company 3 has an innovation system, but it is likely too far from regular employees to make much of a difference in terms of gathering their innovative ideas. The system they use for picking new destinations is more part of the regular running of the business than an innovation attempt. The limited answers they get from customers illustrate the difficulty in

making customers part of the innovation process, and they essentially have to hope that someone picks up signals from individual service encounters, and has the necessary drive and belief in a new idea to make it heard in the organization. As stated in the theory the companies have an opportunity to organize the innovation process following standardization and systematization of the production process, but it is clear that not all organizations see the need or desire to follow through with such an effort.

6.3.6 Self-service

M1 says there most definitely is self-service in the package tour industry, in fact they try to get as much as possible as fast as possible, especially on the Internet. Obviously they don't think that the customer can do everything themselves without any help, therefore they have a service department that gives support both on travel advice and technical issues. The customers often want self-service, as the case with check-in machines, they don't tend to think "Oh crap, I have to do the job myself", they regard it as something positive "I've saved time, I might have saved some money on this, and it's faster". In several of our hotels we are implementing something called "help yourself desk", since in some hotels we have had a service counter with two or three people booking excursions, restaurants and sights. Now we have developed an interactive stand with lots of terminals and screens where the customer can browse through the various offers in the area on his own time. The feedback has been very positive, and people are used to working in this manner. The customers do not call information anymore; they look up the number in the online yellow pages.

Our Internet site is self-service, and this is also a prioritized area for us, according to M2. The new thing now is dynamic packaging, where the customer can go online and buy parts of what used to be a package, meaning just the charter hotel, for example a concept hotel that you pack with a regular scheduled flight, or other elements. This is part of the "do-it-yourself" trend that we see a lot of in continental Europe, and to an increasing extent in Norway. We also have to change the service concept in our hotels, since we believe most customers are self-reliant, whereas we might be keeping our old service concepts artificially alive. Most of our customers have traveled a great deal more than just a few years ago, and their needs are different now. It is a bit difficult to switch, since all customers that have traveled with us previously have come to expect a certain presence from our guides, but we

believe that we can make do with fewer guides, and that their role will be very different from what they have now.

Company 3 thinks the Internet is self-service, since you can add and subtract parts of your package, and that its use will increase greatly in the future.

The defining aspect of self-service is that it can be stored with the use of technology. This can be thought of as presumption moment without a personal contact between customer and service firm, and it applies to all the three self-service encounters described by Manager 1. The Internet-based booking system allows customers to book their vacation independent of Company 1's normal business hours. Check-in machines also gives customers freedom to check in when they want, although naturally within a time frame, and they don't have to wait for a service counter to become available. Finally, the innovative interactive stand designed to give customers information about excursions, restaurants etc. works around the clock, given increased freedom to travelers. Manager 2 stresses the "do-it-yourself"-trend that leads towards breaking up of the traditional charter package in favor of vacation packages based on individual modules, something Manager 3 also stressed. M2 also thinks they can make do with fewer guides at the resort locations, since customers are much more self-reliant these days. All in all this represents a large shift for the industry, and in some ways it chronicles the efforts that have been made both by the package tour companies and customers themselves to gain travel experience and becoming more independent.

7. Conclusion and implications

7.1 Introduction to chapter

The discussion of the empirical findings and the discussion around them in chapter 6 are crystallized in this chapter to a set of conclusions and implications following the same rigid structure. As in all qualitative research, a certain element of interpretation is required and there is usually room for debate on some issues. The conclusions reached in this chapter are robust and the results follow a stringent analysis according to principles outlined in chapter “4.1.3 Analytical methodology”, to further enhance their validity.

7.2 Implications from trends in market demands on service firms and the service firms’ reactions

7.2.1 More possibilities and increased market competition

Dynamic packaging represents both a threat and a great opportunity for the industry. There are many unexplored possibilities in the market still and there is a chance for companies to avoid the commoditization trap by focusing more on incremental innovations, they just need many more of them at a higher pace than today. It is almost always easy for competitors to emulate incremental innovations, so a company will need to come up with new service concepts in order to create a potentially long-lived competitive advantage, as well as technological innovations. In so far as the threat from a new generation of web-based travel agencies, the best assets the package tour industry has are ownership of airplanes and some hotels, and long-standing ties with hotels and other on-site service providers. Taken together, this represents a formidable barrier for anyone going head-to-head in competition with the established players. A word of caution is in order though, since there is an overcapacity in seats available in Europe due to the recent number of new low-cost airlines. The aircrafts are the most capital intensive part of the package tour business, and given a drop in air travel there might well be many airplanes on the market for hire by enterprising entrepreneurs with

a fresh business model in mind, giving rise to a semi-radical innovation that can send the industry into disarray.

7.2.2 Price as a central competition factor

All three executives agree that the market responds well to price, making it a central competition factor. As mentioned by at least two of the executives, there is a spot market for vacations, the ultimate price competition. This suggests that the industry is in danger of the commoditization mentioned above, or at least the low-cost segment of the industry. The second segment, those willing to pay a little extra for more creature comforts and certain services, will probably avoid the commoditization trap, but only if they incrementally improve their products.

Interestingly, incremental innovations in the use of web-based booking has lowered costs in the business, and in the process, wittingly or unwittingly, also contributed to the ease with which consumers can check prices. Some of the packaged tour companies have also started selling only hotel rooms or flights, making the prices there are comparable with prices on flights and hotel rooms sold by other vendors. This makes a modularized approach transparent for the customer, making this option even more tempting, at least for some customer segments, and may in the end spur a downward trend in the standard pre-packaged vacation.

7.2.3 Demand for increased productivity

One of the big challenges for the package tour companies in the coming years is to balance the often, but not always, contradictory needs for increased productivity and better quality service. Increased productivity can quickly become a prerequisite to stay in business in this industry, as the price competition heats up. The two-tier approach espoused above may well solve some of these problems, but there is a limit to how efficient a service operation involving travel can become. There will be a need for stewardesses, bus drivers and hotel staff in the foreseeable future, and this further underlines the need for systematic innovation in the industry. M3 makes valid points about the industry becoming “square”. Standardization has made the vacation experience inexpensive, but also a bit too sterile and devoid of charm, especially for those customers who want more than spending seven full

days at the beach. Modulization is one approach to divide the standardized package up into smaller standardized packets and letting the customer choose among the selection. It is also easy for the companies to scale the number of activities and other modules up and down, since it can be done in real-time on the web.

7.2.4 Demand for quality

The trends towards an increased focus on quality shows clear signs of modulization, the customer expects good consistent quality, something standardization has helped deliver, but they also want more choice, something which is difficult to combine with the predictability they are now used to through the standardization process. One way of doing it is to modularize the service offering into standard packages, and then letting the customer choose. The customers will feel more in control of their own vacation, while the company can balance the need for predictable quality, costs and number of options.

7.2.5 Development of strategies

It is clear that strategies have become more important in the last years, both because of stronger competition and a shortened time frame for making decisions. Pricing is a big issue since the market is moving towards a spot market. This necessitates a pricing strategy in the long run, supported by tactical decisions in the marketplace on a day-to-day basis. All three companies seem to have essentially the same distribution strategy, trying to get as many customers as possible to order online, thereby gaining huge savings in catalogue printing and significantly added flexibility in marketing. Innovations in the financial management field also plays a part, since it is now easier to generate reports on how the company is doing and tying that in to both strategy and tactics. Better financial management tools are also important if the package tour companies are to manage a modulization strategy, as yield management becomes very important, especially in spot market conditions.

7.2.6 Innovation and renewal

The companies in the industry have very varying attitudes towards innovation and renewal. Only one company has a proper innovation system in place, or rather will have by the beginning of next year, and this is a bit surprising as their competitiveness is critically linked

to incremental innovations, especially in the distribution channel. The implication of this is to weaken the competitive advantage they enjoy in terms of brand name, ownership of infrastructure and ties with suppliers. The problem is not so much that many innovations are not used, because they are, but that it happens due to individual employees suggestions, and not by conscious planning and effort. This probably results in less innovation than what could have been achieved given a proper system to catch and promote ideas coming from the employees as well as the customers. When a company has a system in place it can also better track the diffusion of different types of innovations in their customer base, all customers are not going to use the innovation from the outset, which makes forecasting how long it will take for a certain number of customers to start using a new innovation easier and more reliable. Most innovations in the industry will not suffer from an assimilation gap, since they are not storable, and are used in the course of using the service. Knowledge of how an innovation diffuses is also important to make changes and redesigns of the innovation in order to facilitate faster diffusion. A cost-benefit analysis, as well as a timetable, is critical data in an investment decision, and these data will be non-existent or much worse without sound innovation planning and can help overcome the pro-innovation bias.

7.2.7 More technology

New technology has had a dramatic impact on service production in the package tour industry. The effect is especially pronounced in the distribution chain, which has undergone major changes in the last five years. From being reliant on old technology like brochures, telephone orders and high street shops, this is now synthesized in the form of informative, easy to use websites, where the customer gets rich data such as pictures and video. Ordering is automatic on the web, and the customer can pay immediately with major credit cards. Technology has helped not only the customer interface, but also all manners of back office and mid-office functions as well, from better financial management software to shortening the time to market of new destinations from months to as little as 24 hours. One obstacle that has not been overcome is the lack of reliable customer data on individual customers. This is partly the fault of the companies themselves and partly attributable to customer purchase frequency. Up to date customer data on preferences, segment etc is extremely valuable and the industry should strive to establish sensible ways of getting it. This could be done by forming communities on the website, say a discussion forum for each hotel or each

destination, and having the community members fill out surveys, possibly in exchange for rebates, prizes or other incentives.

Technology also ensures a new level of standardization in the distribution chain, the majority of customers will meet the company and book their vacation on the same website. Speedy communications also gives the company more control over the production process.

7.2.8 Internationalization

In the case of package tour operators, internationalization means ownership structure and collaboration. The industry has gotten much more international through ownership in the past 10 years or so due to widespread consolidation. According to Sundbo's theory, local firms have an advantage, something that applies to the Norwegian market also, since the international owners have kept the four biggest brand names. MyTravel even has two brand names in Norway, Ving and StarTour. It is fair to say that the Norwegian companies have acted as standard concepts, and that the concept is quite similar to the concept in continental Europe. The theory also predicts that it is difficult to benefit from economies of scale. This is obviously not the case in the package tour industry, where sharing airplanes and shifting hotel room capacity among companies within a group results in great savings. There are also synergy effects in making corporation wide templates for websites and back-office systems and sharing tour guides. However, modulization can help companies leverage even more economies of scale at the destinations. The corporations can give the consumer more choice if they developed standardized activity concepts and shared it among all brands in the group, or the brands present at a destination. Internationalization should help lower costs, bring more choice to the consumer, but also limits competition, if perhaps not on price, then on new ideas. This lack of new ideas could present an opportunity for smaller competitors to develop new vacation concepts.

7.2.9 Mergers and acquisitions

The evidence for increased mergers and acquisitions in the package tour industry over the last decade are irrefutable. The main reason for this is the amount of capital required to achieve economies of scale and the inherent risk in the industry. A vertically integrated package tour company needs a large customer base to operate efficiently; mergers and

acquisitions provide a rapid customer base since growing organically takes a long time. This brings with it a larger selection of destinations within a brand, opportunities for leveraging knowledge and innovations, but also more standardization. This standardization should lead to modulization of the product offering, offering added value to the customer.

7.2.10 Conclusion on trends in the service industry at large

The established players should be able to keep Internet-based travel agencies at bay by establishing new service concepts and innovating more. This will also help alleviate the problem of spot-market pricing, and should enable the package tour companies to charge a premium on added services. This is consistent with the theory predicting tougher competition and the central role of pricing. The demand for increased productivity and higher quality services are sometimes at odds with one another. Modularizing the service offerings will give the companies a better chance of covering different market segments. Strategies are more important today than in the past, due to strong competition and a fast moving industry, and are especially helpful in pricing decisions. The industry is only belatedly learning the value of systematic innovation systems, and only one of the three companies surveyed had a proper system in place. All three companies invested substantially in information technology quite early, from online booking to check-in machines. This has especially benefited the distribution chain, which is now very efficient. The industry development follows the theory closely in regards to demands for increased productivity and quality. Strategies, innovation and the increased use of technology are also trends predicted by theory that the companies have followed, although two of the companies have yet to develop systematic innovation systems. Internationalization has swept the industry, and foreign corporations own all three companies. However, contrary to predictions in the theory, benefiting from economies of scale in the area of air transportation and hotel room purchases as a result of internationalization has not been a problem. The buying corporations have kept the brand name of the companies though, suggesting that local knowledge and brands is still valuable and hard to transfer, as suggested by the theory. The tendency towards concentration via mergers and acquisitions is very clear in the Norwegian market, as predicted by theory.

7.3 Implications from developments in production organization related to modulization in mass-producing service firms

7.3.1 Large-scale operations

All three leading companies have large-scale operations. The entrance barriers to the package tour industry are high if you want to be in the mass-producing segment. It takes time to build a customer base and brand recognition, and it is nigh on impossible to do this without first losing money, perhaps for several years. There are several implications of large-scale operations, the most obvious being low costs per unit, and hence the ability to offer reasonably priced vacations to a large number of people. It is a fast and efficient method of traveling to places that would otherwise have been difficult to access, both in terms of traveling there, but also since the infrastructure would be less developed. This brings us the negative sides of large-scale operations. Too many tourists at one place is bad for the environment and leaves a feeling of mass-tourism that even mass-tourists want to avoid. The companies could offer more and better entertainment, day-trips and excursions in modules to offset the mass-produced boredom and non-authentic experiences some destinations suffer from. But all in all, the companies have developed according to this point in the theory, since they have been through a stage of mergers and acquisitions.

7.3.2 Standardization of products in a combination system

The package tour industry has come a long way towards standardization; one might argue that it is the foundation for their business model. There are examples of the companies moving beyond the traditional package standardization and developing a selection of standard elements, such as splitting the stringent bond between the air transportation part of the package and hotel rooms. This is the last part of the standardization trend. Customers can now buy just airfare or just hotel rooms, but the percentage of customers doing it is relatively small as of yet, although this is likely to rise quite rapidly.

7.3.3 Standardization and rationalization of the production process

Internet bookings are a prime example of both standardization and a rationalization of a part of the production chain. It is standardized in the sense that the customers go through the exact same booking procedure. It is rational since it is in fact the customers themselves who do all the punching in of details. As companies grow bigger, it is clearly in their interest to follow a standardization and rationalization path, and this part of the theory ties in with mergers and acquisitions, large-scale operations and the standardization of products. The implication is that the package tour companies can become too rigid and not innovate enough, if something new challenges the systems already in place.

7.3.4 The separation of production and marketing

The package tour industry is vertically integrated, usually owning the vast majority of sales channels and air transportation, and some hotels. The rest of the required infrastructure, mostly hotels, transfer busses and various other smaller assets are leased or rented. There is a tendency to move away from a production viewpoint more towards a marketing viewpoint, where the marketing division (or service distribution organization, as it is called in the theory) submits their take on the market demands and then expect production to produce it. The production departments are now mostly located abroad, as the big companies seek economies of scale in negotiations and administration. The branches, in this case being the national brands, must sell whatever the head office decides they can produce. But, in a reversal of roles the last years, the head office strives to produce according to the input they get from marketing. The implication is that, although there is a clear separation of the two functions, they seem to operate much better together now than before. M2 underlines this point when he says they now have steering committees where people from the whole company is involved, making the process more integrated. The theory is mainly correct in relation to the packaged tour industry, but there is more emphasis on the marketing division reporting the market needs, than any decrease in marketing department power. Better relations between the two parts of the company may well encourage modularization as a compromise between production and marketing.

7.3.5 Specific innovation organization

The theory argues that systematic innovation is vital, but that R&D departments are not used. To have a systematic innovation effort a company needs to have specific processes to catch new ideas. Company 1 and 3 do not have systematic innovation systems in place, and rely on the traditional service company method of leaving it up to individual employees. Company 2 on the other hand follow the theory and has set up such groups, choosing to organize them along the lines of strategy areas. This is not to say that Company 1 and 3 does not use ad hoc groups or a collective process as seen in the Danish case studies, it is just that they have not developed innovation organization systems. This increases the likelihood of losing important new ideas, and lessens the chance of implementing them.

7.3.6 Self-service

Package tour companies have moved aggressively to transfer booking to their self-service Internet sites, and are developing other methods of self-service, such as check-in machines and virtual guides. This is done to rationalize operations and provide services independent of office hours or guide availability at the destinations. Customers seem to appreciate it, however, the service contact is gone. If a customer books a vacation online today, the only representative they will meet is the stewardess and the guide on the transfer buss, if indeed the flight is not outsourced and they have a rental car. It is difficult to measure how much impact personal service contact has, but without it, there are no mitigating positive experiences with a service company to mitigate frustrations caused by a problem. Brand loyalty could become harder to maintain when the only connection with the brand is a website. There are opportunities as well, if the companies can avoid using guides on time consuming trivialities, they can then be set to perform more value added services, such as excursion, shows and personalized services.

7.3.7 Conclusion on the mass-producing service firm

All three companies have large-scale production after the mergers and acquisition wave discussed previously. The barriers to entry are also significantly higher than before, something evidenced by Apollo having to price their products low in order to gain market share and critical mass. The theory on mass-producing service firms say that there is a

tendency towards large-scale production and high barriers to entry, precisely what has happened in the Norwegian package tour industry. The companies examined in this thesis are all in the last stage of the standardizing their products in a combination system having started to split up their main product in a series of standard elements. To achieve this they have also standardized their production process, doing some in-house and other parts together with firms in the international group, in line with tendencies in the theory. The process is also much faster, and on the way to become continuous, rather than seasonal. The marketing departments in the companies have gained power, and the process of service production and service distribution has become much more integrated than before in a departure from the theory, which states that there is a tendency towards separation. Innovation has clearly become more important lately, and one of the companies has established a systematic innovation system, the other relying more on a collective process or small groups, as the theory predicts. Self-service is now an integral part of the charter tour experience, and has produced substantial savings for the industry, especially in reduced personnel and brochure printing costs. The customer welcome this since it, to a greater or lesser extent, allows them to buy the service when they want.

7.4 THESIS QUESTION CONCLUSION

The Norwegian package tour market has followed a modulization tendency very similar to the one outlined in Sundbo's article on modulization. There is a clear need for mass-producing service companies to cut production and distribution costs in the face of increasing competition, higher quality demands and a stagnating market. The Norwegian package tour operators have found an answer to this in attempting to combine rationality and cost savings with a focus on the needs of the individual customer. The companies surveyed do this by employing new technology and new innovations to become more efficient and divide up their service in modules, which can be combined individually by the consumer. This process is not completed, but the thesis proves that the tendency towards modulization is firmly entrenched and follows a clear path.

There is however a dark cloud on the horizon, namely that the package tour industry has not been able to grow while the travel market itself has expanded quite rapidly. The implication is that to grow further the industry needs to offer more added value, new concepts and more choice. This thesis proposes that the answer is increased modulization of the service

offerings. The entire product range need not be divided in modules, pre-packaged tours will probably always have a certain market, but the need to act is quite obvious. Customers are a notoriously fickle bunch.

The results of this thesis show that the modulization tendency is clear in the package tour market, and it is reasonable to conclude that at least some of the trends apply to the Norwegian service industry. The results should be especially interesting for other mass-producing service industries in Norway whose challenges are similar in nature to that of the package tour industry.

7.5 Future research questions

We have seen a tendency in this thesis towards the formation of a spot market for package tours. The modulization framework predicts increased competition and a standardization of services. The transformation from pricing services in advance towards spot market pricing should provide ample material for study. One can even imagine that pricing for mass-produced services will occur as a continuous auction, much like on EBay and similar auction sites.

Trends in the manufacturing industry is showing increased use of mass-customization, where the customer gets his product built to order, even though it is mass-produced. The mass-producing service sector is experience a modulization trend. Given that employees are relatively expensive production inputs, there is a possibility for the manufacturing industry to deliver products that are more customized than the service industry, a sharp reversal of what has been seen before. Comparing the trends in the two industries and exploring the relationship between mass-customization and modulization could yield very interesting data on the future developments of both industries, as well as insight into the general blurring of the boundaries between service and production.

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Appendix

Interview Guide

Estimated interview time: 1 to 1,5 hours

Place: At interviewee's place of work

Type of interview: Standardized, open-ended (structured)

Start of interview:

- A brief introduction about the research project is given.
- I explain that I am looking for answers about the interviewee's thoughts on the industry and not about the specific future strategy of the company. I want to draw on his experience to create a picture of the industry's development, past, present and future.
- Confidentiality issues are resolved, as well as what happens to the material, including the tapes of the interview. The interviewee will get a copy of the thesis after it has been graded.

Questions:

1. Could you tell me a little about your professional background and experience in the package tour industry?

Section 1: *Trends in market demands on service firms and the service firms' reactions*

2. How do you rate the market competition in the past and the possibilities offered then, compared to what we see now, and what you think the future will bring?
3. What are your thoughts on the developments in price competition? Is it becoming more or less important?
4. How would you describe the productivity development in the industry?
5. Quality is a much-used word in connection with package tours. Do you think there has been a development in how the customers perceive and demand quality in the industry?
6. Has the development of strategies as a tool changed during your years in the industry?

-
7. Has there been a shift in how innovation is organized and exploited in the industry?
 8. What impact has new technology had on service production in the packaged tour industry?
 9. Do you see the industry as having become more or less international?
 10. In the beginning of this industry there were many small companies, while today there are only a handful. Why do you think that is?

Section 2: *Developments in production organization related to modulization in mass-producing service firms:*

11. What are the implications of large-scale operations?
12. Do you think there has been widespread standardization of the products you sell?
13. How would you describe the development of the production process?
14. How has the relationship between production and marketing evolved during your career?
15. How does the company you work for organize its innovation efforts?
16. Is there an element of self-service in the industry, and if so, what is it?

Section 3: *Finishing the interview*

17. Is there anything you would like to add, perhaps something important about the development of the industry we have not discussed yet?

I now explain how I will use this interview in the research.

Thank you very much for your time.

Interview ends.

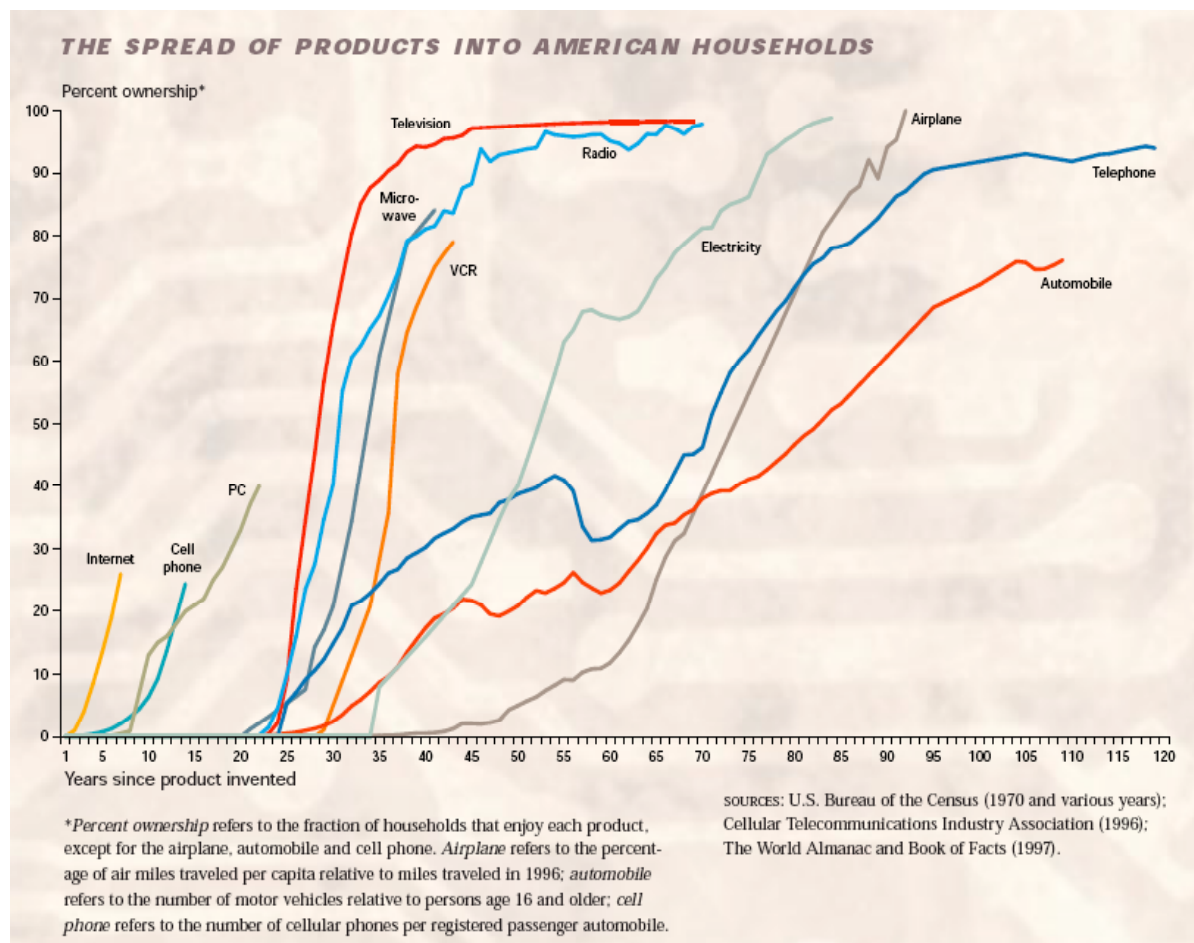
Table 3: Size and average load factor of UK airlines 2001

Rank	Airlines	Passengers (million)	Average load factor (%)
1	British Airways	31.8	70
2	Britannia Airways	7.9	91
3=	BMI British Midland	7.2	65
3	MyTravel Airways	7.2	92
5	Air2000	6.9	91
6	Thomas Cook (JMC)	6.0	91
6=	EasyJet	6.0	81
8	Virgin Atlantic	4.8	76
9	Monarch Airlines	4.7	90
10	Go Fly*	3.7	75
10=	KLM UK (Buzz)*	3.7	66

Note: Go Fly was acquired by easyJet in August 2002 while Ryanair took over Buzz in February 2003.

Source: CAA (2002)

Buck and Lei 2004



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