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

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Abstract

This paper is built like a three–layered club house sandwich with the first layer providing some theoretical and conceptual insights regarding expected innovation behaviour in tourism based on available material in tourism and industrial economics. The second layer will provide empirical insights and/or testing regarding the causes and consequences of innovation and product development in tourism based on recent empirical research carried out at the Center for Tourism and Service Economics, University of Innsbruck, and interviews carried out by the author both in Europe and North America with various larger national and global tourism firms, *e.g.* tour operators, airlines and theme parks. Finally the last layer will draw some conclusions and discuss research results with respect to issues and prospects in tourism policy making.

Relevance and importance of innovation and product development in tourism

It is probably fair to say that most sectors of economic activity in Western economies have undergone strong technological changes moving towards IT–based flexible manufacturing with global outsourcing, creating the ".com" or "new economy", which very much fits with what Schumpeter described as the creative destruction of existing institutional arrangements and patterns of exchange in order to create new wealth through innovation. His vision also included an increased willingness to take calculated risks by new or "real" entrepreneurs (Schumpeter, 1934).

Even though much innovation emanates or originates from the service sector, there has so far been relatively little discussion as to its importance and prevalence in tourism. *A priori* one should expect that innovation and product development (or differentiation) should constitute unique selling propositions and a strategy towards gaining new markets (Bullinger 1999). Even though the services and tourism sector have become very mature markets requiring innovation and/or new tourism attractions (Weiermair 2001, Keller 2002), the actual situation of the tourism industry is to be rather characterised by minor almost only cosmetic changes in product offerings interceded by an ever increasing number of crises (Iraq war, September 11, SARS etc.). Already ten years ago Poon (1993) noted: "The tourism industry is in a crisis – a crisis of change and uncertainty; a crisis brought on by the rapidly changing nature of the tourism industry itself. (…) The industry is in metamorphosis – it is undergoing rapid and radical change. New technology, more experienced consumers, global economic restructuring and environmental limits to growth are only some of the challenges facing industry."(Poon, 1993, p. 3)

In the past decade, destination management has also only barely adjusted to completely change environmental and competition structures and processes. Existing destination strategies can no longer satisfy market requirements (Weiermair 1998). Especially small-sized and fragmented alpine tourism companies must face increasing competition (Smeral 2003) and are confronted with declining numbers of tourists (Bartaletti 1998); this holds also true for coastal tourism. In the future the tourism industry's challenge is to provide increased value for money either through innovation–driven cost reducing changes in production and marketing processes or through product changes providing more varied tourism experiences for quality-conscious and saturated multi-option customers. (Weiermair, 2001; Weiermair, 2003). Next to such niche strategies the tourism industry will have two big future markets to work with:

– The rise of the ageing population in most western economies and

– China, which will become the largest importer of tourism by the year 2010.

In what is to follow in my presentation I will try to address the following points:

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

2. Which dimensions of innovations can be distinguished?

3. What are the primary motives for innovation?

4. Which are success factors for innovation in tourism?

Definition of the term "innovation"

There are various definitions of the term "innovation", which derives from the Latin "innovatio" which means the creation of something new. The diversity of definitions lies in the different purposes of examining this phenomenon (Johannessen *et al.,* 2001). Probably the most useable definition is that provided by the late Schumpeter (Schumpeter, 1997) who distinguished five areas in which companies can introduce innovation:

1. Generation of new or improved products.

2. Introduction of new production processes.

3. Development of new sales markets.

4. Development of new supply markets.

5. Reorganisation and/or restructuring of the company.

The above definition clearly distinguishes innovation from minor changes in the make up and/or delivery of products in forms of extension of product lines, adding service components or product differentiation. Successful innovation, *e.g.* innovation that is also profitable to the tourism firm in a competitive market, must increase the value of the product or tourism experience. Since the value is costumers' perceived quality divided by the price (cost) of this quality successful innovation must increase value by improving quality or by lowering price (cost) (Heskett, 1986).

The production and marketing of tourism products is distinct from industrial products and displays specific characteristics which often pose constraints or problems and hence serve as stepping stones for increasing the value of products via innovation. They are: tourism produces and sells product bundles instead of products (products being "experiences") which are very intangible, products cannot be stored (simultaneity of production and consumption), the consumption of tourism products involves the active participation of the customer (prosumer), and tourism production/marketing may involve large capital assets (airlines, hotel chains or car rental firms) or at the intermediation, distribution and final consumption stage may involve interaction personnel (*e.g.* travel agencies, restaurants, coaches, etc.).

Typically when a tourist spends his holidays in a destination, he does not consume a product of only one supplier, but a bundle of services as a whole (Kaspar 1991). A lot of different service suppliers participate in creating a tourism experience. This requires vertical co-operation, as the tourist's overall quality assessment depends on cumulative quality perception (Koch 1998). As far as the tourist is concerned, the product covers the complete experience from the time he leaves home to the time he returns to it.

Tourism services are personal services and will be created by an internal (supplier) and external (client) factor (Smith 1994). The client himself has to be proactive and comes in most cases to the destination (a constraint which might serve as a stepping stone for innovations). He participates either passively (*e.g.* using cable cars) or actively (*e.g.* skiing) in the process of service production. The uno-actu-principle implies that unused offer cannot be stored, making efficient capacity utilisation one of the big problem areas in tourism. This applies to all tourism services in accommodation, catering, travel agents, transport systems, and all other businesses related to the tourism value chain (Murphy *et al.,* 2000).

Intangibility of tourism products implies a large amount of risk and uncertainty about customer value (quality-price-ratio). A guest, who booked a certain holiday package, does not know with certainty what he can expect and how he will eventually perceive and judge the quality experienced in his vacation. Particularly for a destination it is crucial to create confidence, to determine quality criteria and to introduce measures to reduce risks for the customer.

Overall, tourism services are very capital-intensive and depend on external partners and other factors. Similarly, the capability and the motivation of human resources are essential, suggesting the necessity of both capital and labour related types of innovation. Finally tourism needs local infrastructure, the local population should have positive thinking about tourism, and local industry should act as a supplier for tourism businesses or shopping facilities (Bieger, 2002).

Potential areas for innovation in tourism

Which implications result for innovation from the characteristics of tourism products described above? First of all, in today's saturated markets customers look for experience rather than destination driven products. Hence, in the future it will be important to create a rewarding tourism experience through innovation and product development instead of offering singular tourism elements. New holiday forms offering experience will become the main motive for the holiday decision (Bartaletti, 1998). The creation of experience should cover "entertainment", "educational", "aesthetic" and "escapist" elements and/or product features as shown in the work of Pine and Gilmore (1999). Experience in this context means content, *i.e.* the nucleus of the holidays. The destination acts as a stage and the different tourism companies as actors on this stage. Continuous learning and the acquisition of knowledge from the customers will become essential (Hjalager, 2002).

With the individualisation of mass tourism (Poon, 1993) and the heavy involvement of customers in the tourism experience creating process, tourism has become an “information” and “relationship” business. The involvement of the customer is especially useful to get information about the needs and wants of clients suggesting new ways of client data and yield management (Weiermair/Mathies, 2002). New information and communication systems will be required to collect and to analyse information and to realise it in the newly developed product/service. Here it becomes important not to imitate innovative effects made elsewhere, but to build on a company’s or destination’s own strength and core competencies, which furthermore will be strengthened and further developed through knowledge management (Weiermair, 1998).

Given the intangibility of tourism products, the tourist may feel uncertain about the quality of the services. Despite or because of this intangibility, tourism products can be enhanced in value through adding sensations (design, fragrance, light, colour, emotional attachment). As a consequence of such product changes the emotional value of the “tourism experience” will be enhanced.

The work and capital-intensive tourism industry can bundle resources, acquire know-how and minimise risks by building up networks. As a result, new markets can be served, fewer resources must be invested and entrepreneurial options will be created. Similarly, IT based innovation in distribution and marketing as well as firm alliances or other forms of co-operative marketing will help to reduce cost, thereby increasing customer value, market share and/or market extension.

On the economics of innovation and product development behaviour in tourism

This part analyses the economic motives of entrepreneurs underpinning innovative behaviour and the varying types of innovation which can be distinguished.

What drives innovation in tourism?

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

– Supply and supply–related determinants.

– Demand drivers.

– The level and pace of competition.

Supply factors

The availability of new technologies led to the development of new skills, new materials, new services, and new forms of organisation. This is especially true for the last two decades where the role of technological innovation was crucial. In tourism, technology created a new form of business called e-tourism, which today is the biggest force in e-commerce.

Thanks to this development, new skills in tourism management (e-marketing) were necessary, as for example for a variety of coaching and interactive skills in the fields of wellness or adventure tourism. New information services for guests emerged as databases eased processing customer profiles and customer behaviour. Moreover, new forms of network organisation emerged particularly in the field of co–operative tourism marketing. They have also been enabled by using new technologies.

Demand changes

Not only supply has changed, but so have customer wants and needs. Secular shifts (working versus leisure time, population pyramid, individualisation, increasing demand regarding quality) led to modified leisure and tourism behaviour (Poon, 1993; Horx, 2002; Foot, 2002; Bieger/Laesser, 2002, Weiermair 2003). New life styles appeared through flexible working times, higher incomes, more leisure time and the changing value of holidays (now seen as a part of life).

Basic driving forces for the availability and quality of basic service quality elements are punctuality, accountability, convenience, speed, and price. All other elements like aesthetics, individual attention, and multiple options are secondary elements, which are considered as added features. But these secondary elements in particular create a special “value for money” for the customer.

Customer orientation plays a fundamental role in service innovation. Valuable information can be gained from the behaviour of the customer during the service process. As the customer is highly involved in the production of a tourism service, enterprises have to adjust to the changing interests and values of their guests. New products which offer a special or unique value to the customer are more successful than innovation without the consideration and participation of the client. Hence, innovation leads to higher market shares, a higher efficiency and easier realisation of aims regarding turnover or profit (Hübner, 2002).

Competition

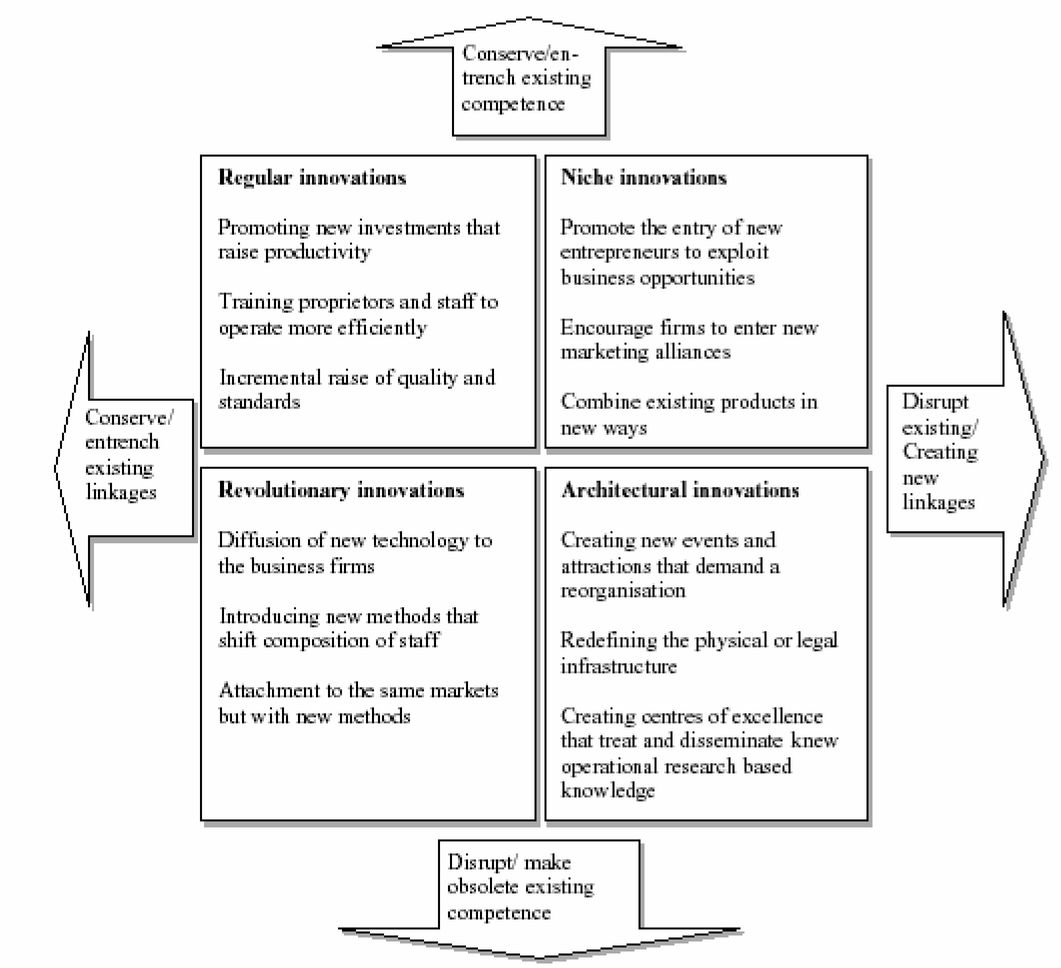
Many parts of the tourism industry but notably such businesses as transportation, airlines, hotel chains, tour operators and/or car rental agencies are highly concentrated and act as global players in the industry. With the maturity of markets, heightened technological change in the IT field and the slowing of demand, in many parts of the industry rivalry has turned into ruinous competition.

Globalisation and deregulation have further heightened competition. Similar to other fields of economic activity these market conditions enhance process innovation (networking, reservation and yield management systems, etc.) as opposed to product innovation which can be easily imitated by rival competitors (Weiermair *et al.*, 2002).

Innovation types

A useful distinction of innovation types in tourism has been made by Hjalager, who adopted concepts developed by Abernathy and Clark (1985) and who developed a model to measure innovation levels (degrees) in tourism using core competencies as the unit of analysis. This differentiation seems to be more suitable, as innovation in tourism is often based on core competencies (Schwaninger/Flaschka, 1995). Core competencies may comprise internal and/or external factors. Internal resources, *i.e.* resources of the company, are the most important determinants regarding positioning and competitive advantages of a company which are difficult to imitate (Gomez/Probst, 1995). Hjalager (2002) distinguishes four types of innovation dealing with either the breaking up or deepening of relationships to clients or to the market and the abandonment or preservation of competencies.

Figure 1: Innovation types, adopted from Abernathy and Clark



Source: Hjalager 2002, p. 467

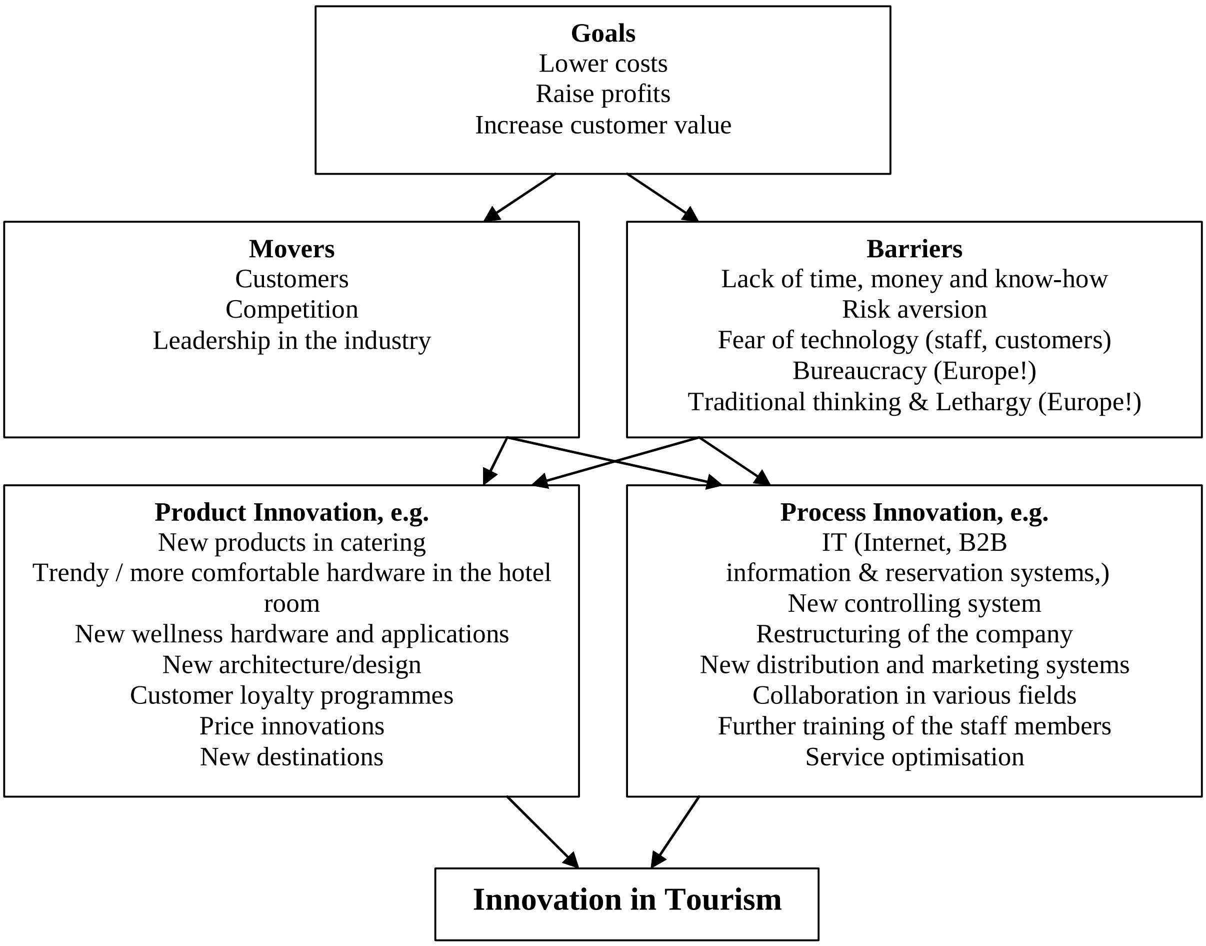
While niche innovations (*e.g.* co-operation with a tour operator) emphasise new forms of co-operation and do not touch existing competencies, architectural innovations (*e.g.* arctic tourism) introduce new structures and redefine relationships to customers and existing markets. External branch structures and the target groups remain unchanged when a revolutionary innovation is realised, although services have changed by using new technologies. Regular or incremental innovations are realised with existing competencies and existing relationships, some examples are increased productivity, quality improvements or further training of staff members *e.g.* of a hotel (Hjalager, 2002).

These systematic categories seem to be useful, but the shortened product life cycle noticed in the past decade also has to be recognised. The same is true for innovations, which implies a dynamic change of innovations belonging to one of the four mentioned types (Abernathy/Clark, 1985).

Empirical evidence gathered so far

At present, data collection on the elaboration of innovation and product development at the level of the destination is being carried out at the Center for Tourism and Service Management, University of Innsbruck, Austria. Results of this study are scheduled at the end of 2004. Below we report on another set of data which comes from interviews carried out in North America and Europe with larger national and global tourism firms (tour operators, travel agencies, individual hotels, hotel chains, cable car companies, theme parks, a provider of e-tourism (databases), restaurants, and charter airlines). In particular our interest was to assess the prevalence of process versus product innovation in different settings. The findings are shown in the figure below.

Figure 2: Product versus Process Innovation in Tourism



All firms recognised IT and its use in e-tourism as a major change although nobody saw it as an innovation (as it came from outside the industry). The second change described as innovation was new forms of business alliances and co-operative marketing in order to extend markets. This includes teaming up with non-tourism partners and/or suppliers (lower cost of acquiring new customers). Most firms mentioned strategic partnerships in the fields of human resource management, product changes, and adding new destinations. In North America, major objectives were cost reduction followed by revenue generation, while in Europe increasing customer value followed by profit maximisation can be seen as the most important incentive for innovation. However, minimising costs is only a subordinated goal of innovative firms in Europe.

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

Competition in mature markets (particularly skiing and golf) leads to pressure to add more experience to products, *e.g.* the offer of a seat on Space Adventure's (American tour operator) new package tour to the International Space Station scheduled for 2005 for USD 20 million, or so-called scalpel safaris, *i.e.* a combination of cosmetic surgery and a trip to the bush in South Africa (*The Economist*, 2003). Another example would be the 18-hour "voyage of the imagination" programme on a schooner. This package includes the participation of the guests who play poor immigrants who work for passage. Two programmes were planned for 2003, but a third had to be added thanks to strong demand (Clark, 2003).

Quality assurance, marketing practices, and customer and employee satisfaction were among the most important areas or fields for innovation with some progress reported (nobody said they have achieved total satisfaction). For example, cable car companies mentioned security in particular as a field of innovation. The other factors were considered less important and there was little progress reported so far.

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

The major movers of innovation are customers, who were mentioned by almost all interview partners, followed by competition and the ambition to be the leader in the industry. Major barriers that firms had to face were lack of time, money or know-how, and risk aversion which were all internal factors. As regards outside forces, particularly in Europe, bureaucracy and politics were pointed out as possible obstacles that prevent the realisation of planned innovation activities.

All experts interviewed agreed on the most promising vehicle for innovation, which is co-operation, alliances and/or networks in various fields such as technology, marketing, distribution, and human resources sharing.

Implications and prospects for tourism policy

From our empirical inquiry the following stylised facts and/or propositions can be derived:

– Private industry only undertakes innovations if they promise to be profitable (expected profitability is the biggest driving factor).

– A combination of high cost and risk of innovation and the existence of intensive if not ruinous competition make cost (and price) reduction through process innovation the more interesting innovative avenue.

– With the exception of a few tour operators and cable car producers/operators, who were pioneering new products most firms were pursuing product differentiation strategies.

– There is a negative correlation between firm sizes and innovative activity.

– Small firms are usually imitators, poaching innovation or product changes from across the street or across the region (rarely across the country, the continent or the world).

This poses the well-known policy question as to how much governments ought to spend on innovation projects in tourism on account of externalities and prohibitive risk and cost of process and product innovation and the indivisibility of research and development activities vis-à-vis a multitude of small user firms. Secondly if it is clear that governments should get involved, the question is how monies should be spent.

Many economists would argue that governments should:

– Not subsidise outright innovation on account of opportunism or rent seeking behaviour.

– Try to let the market do as much as possible and only intervene when there is market failure.

– Try to let the innovating firms in question achieve economies of scope and seek innovation through co-operative alliances and other forms of networking,

– Reduce the government’s role to a facilitator, coach or incubation partner, who turns prototype developments over to the private sector as soon as innovation activities have been carried out (*e.g.* the development of the travel reservation and information system in Ireland through the Irish Tourism Board or the development of diverse new tourism products such as family wellness holidays in Tyrol or Alpine areas through the Tyrol Tourism Board and through the Future Foundation Tyrol in Austria).

Another approach which works well in regions/countries with non-competing destinations (on account of distance) is the Canadian Product Club Programme, which was created in 1996 and which currently promotes product development for 45 product categories through research and development facilitation. 250 co-ordinating partners and more than 5 000 businesses co-operate through this product club programme (www.canadatourism.com).

A last point which deserves being mentioned is the provision of a well functioning, regulation-free market. Here we could see the difference between what North American versus European tourism firms considered innovation barriers, with the difference being bureaucratisation in the case of European firms.

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