

Case Study

Blue Ocean Hackathon: Market Creation in a Highly Competitive Industry



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This case study was written by Oh Young Koo, Institute Executive Fellow of the INSEAD Blue Ocean Strategy Institute, under the supervision of W. Chan Kim and Renée Mauborgne, Professors of Strategy at INSEAD. It is intended to be used as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

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Bora has just returned to South Korea from her trip to Sydney, Australia. A few months ago, she saw an advertisement for a \$1,200 five-day package tour in Sydney. Given that the flight alone typically costs around \$1,000, this was a huge bargain; in this case, \$1,200 covered the flight, accommodations, meals, transportation, and tour activities. Bora booked the trip and looked forward to the start of her vacation.

On the first day, a group of nine people, including Bora, toured downtown Sydney, starting with visits to Martin Place and St. Mary's Cathedral. Then the tour guide led the group to a health supplement company. After a presentation about the small-vessel disease, a lecturer informed the group about policosanol, a health supplement that was available on site for much cheaper than it sells in Korea. Bora could not help but purchase policosanol supplements, convinced that it was indispensable but also feeling an implicit pressure to buy something.

The following day, the group visited a sheep-shearing farm to experience a local activity. However, instead of actually observing sheep shearing, they met the farm's owner, who spilled a glass of Coke onto a sheepskin rug to demonstrate how it could be cleaned spotlessly. After the demonstration, they were guided to a store that stocked garments, Ugg boots, and sheepskin rugs.

Over the course of her trip, Bora spent over \$1,000 on policosanol supplements, a sheepskin rug, and natural cosmetics, none of which she had expected to purchase. She returned home with lots of memories – of Sydney Opera House and spectacular night views from the Harbour Bridge – and a bag full of impulse purchases from specialty stores.

Bora's package-tour story will sound familiar to many Koreans. Fierce competition among travel agencies has driven down prices to less than the average cost of airfare to attract customers. However, customers end up spending extra money on forced shopping, high-pressure extra activities that they have to pay for, and compulsory tipping of the guide and driver.

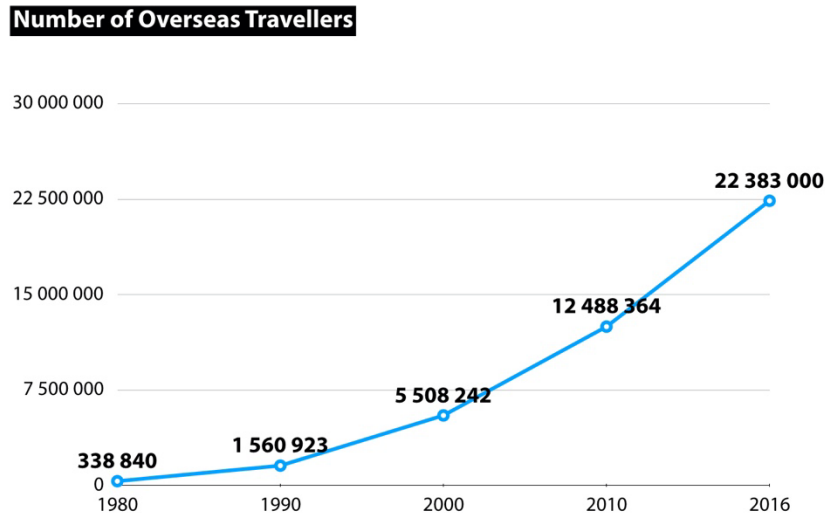
An Overview of the Travel Industry in Korea in 2012

According to Visa Global Travel Intentions Study 2015, Koreans travel abroad more frequently than Chinese and Japanese: 90% of study respondents had traveled abroad, taking an average of five trips in the previous two years.¹ Since the 1980s when overseas travel was unregulated, the number of Korean travelers has grown rapidly. In recent years, that growth accelerated thanks to low-cost carriers and five-day workweeks that freed Koreans to enjoy weekend getaways.

1 Gwon, Hyerim. "Koreans travel most frequently among Koreans, Chinese, and Japanese." *Asia Today* 28 July 2015. (In Korean) Accessible at <http://www.asiatoday.co.kr/view.php?key=20150728010016654>

Exhibit 1

Number of Overseas Travelers in Korea



Source: Aggregated from Overseas Traveling Survey by Korea Tourism Organization (<http://kto.visitkorea.or.kr/kor/notice/data/statis/tstatus/abrstatus.kto>) by the author

Accordingly, the travel industry has grown exponentially over recent decades, offering cheaper and more varied tour products. Yet people arrange and experience their trips in the same ways they always have. When Koreans plan leisure trips, they first choose between a package tour or independent travel. A package tour represents the integration of multiple elements, including flights, transfers, accommodations, meals, sightseeing, and tour guides; it is offered as a single product to a group of people, typically between 10 and 45 in number, so that people can benefit from group discounted prices. By contrast, independent travels require individuals to arrange each travel component separately, and book a flight via travel agency A, accommodations via travel agency B, a rental car via rental car company C, and so forth. These two formats offer a distinctive travel experience in the same destination. For package tourists, almost everything is prearranged—hotels, restaurants, and the tour itinerary—so that they just need to stick to the schedule and follow the instructions of the local tour operator, who is responsible for arranging the logistics, interpreting the language as needed, and providing comprehensive information (from history and culture to expertise concerning tourist sites) about the destination. The quality of the travel experience may differ depending on the knowledge, social skills, and personal character of the local tour operator. Traveling as a group allows minimal free time or flexibility, often leaving package tourists with the sense that they have missed out on an authentic local experience.

Independent travelers enjoy total freedom of choice, allowing their personal preferences to dictate decisions about sightseeing, local activities, hotels, and restaurants. Without the help of a local guide, however, they must face the foreign situation on their own: conducting interactions in the local language, researching tour activities, making logistical arrangements, and resolving unforeseen problems. The quality of travel varies depending on how well prepared such travelers are. (Exhibit 2 summarizes the advantages and disadvantages of package tours and independent travels, respectively).

Exhibit 2

Package Tours vs. Independent Travels

	Package Tour	Independent Travel
Pros	Convenience Efficiency Cheaper Security (Safety) Social interaction (within a group) Easy to obtain flight tickets, arrange hotels in peak times	Freedom Flexibility Customization Social interaction with locals
Cons	Inflexibility No freedom No customization Lack of local experience Tight schedule	Time consuming Lack of local assistance Limited information Difficulty in peak times

These two travel formats serve very different customer groups based on the value they provide. According to survey², most package tourists cite convenience as the most important criterion in selecting package tours over independent travel, whereas independent travelers prioritize freedom over convenience.

For decades, the majority of Korean travelers have opted for package tours as a way to overcome the language barrier and cultural differences. They have willingly exchanged freedom and flexibility for the safety and comfort of being escorted by local guides. However, a growing number have started to avoid package tours, as overseas travel becomes a familiar experience. The purpose of travel itself has changed, from “sightseeing” to “experiencing.” Independent travel has, moreover, been facilitated by the information available on the internet and online booking sites. The advent of Google Maps, for example, has made it possible for travelers to tour around wherever they want.

Despite the increasing popularity of independent leisure travel, travel agencies have continued to focus on package tour products, which accounted for a much larger market share in terms of sales and profit margins. Among the mainstream travel agencies, package tours accounted for 77% of sales.³

Package Tour Industry

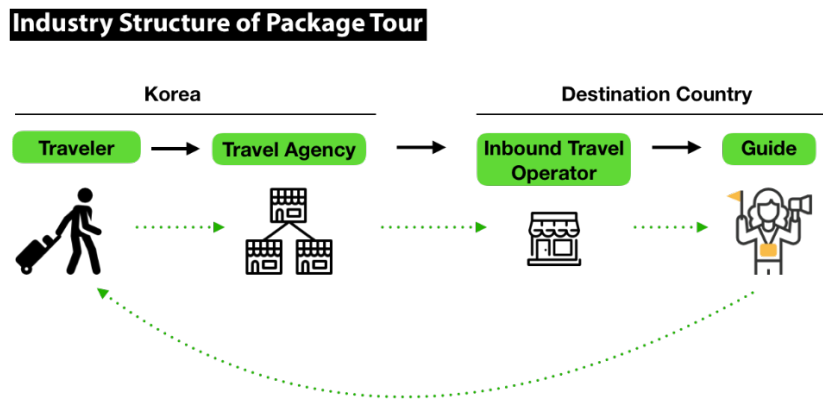
A tour product is developed, advertised, and sold by a travel agency in Korea. Then, the tour is delivered by an inbound travel operator and a guide in the destination countries. The inbound

2 Shin, Jihoon. “Traveler’s preference.” *Korea Travel Times* 7 July 2014. (In Korean) Accessible at http://www.traveltimes.co.kr/bbs/board.php?bo_table=News&wr_id=90055&code=E

3 Jung, Yeonbi. “Statistics on 2012 Package/Independent travels.” *Global Travel News* 3 January 2013. (In Korean) Accessible at http://www.gtn.co.kr/mobile/news_view.asp?news_seq=52422&s_key

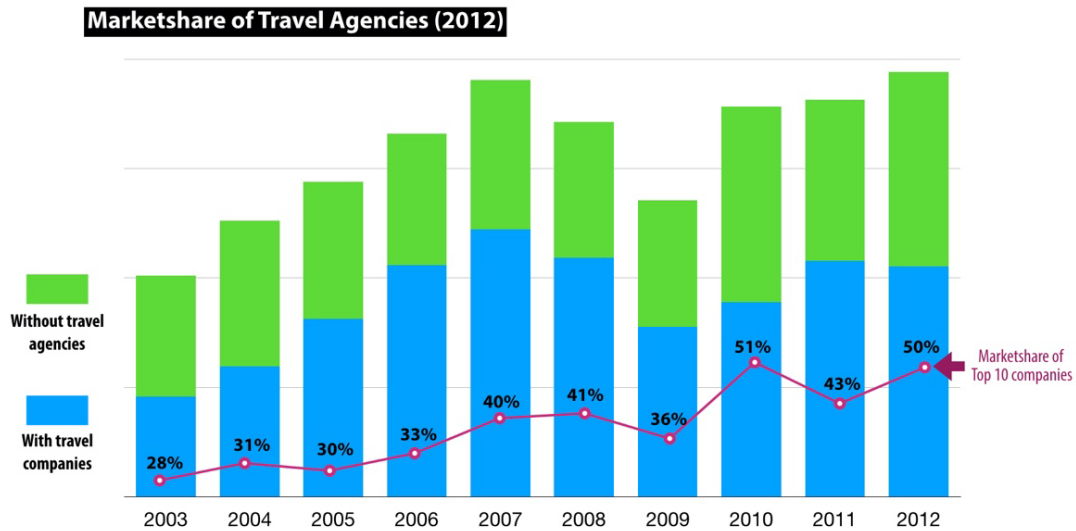
operators subcontracted by Korean travel agencies are usually small independent companies that employ Koreans as full- or part-time local guides. They operate tour programs, contract with certain hotels, arrange local transportation and excursions, and so forth. These local operators are responsible for following the prearranged travel itinerary at the price set by the Korean travel agencies, giving the latter far greater bargaining power. (Exhibit 3 summarizes the structure of the package tour industry).

Exhibit 3
Supply Chain of Package Tour Industry



By 2012, between 4,000 and 5,000 travel agencies existed in Korea and the top 10 travel agencies accounted for 50% of the market, and this dominance continued to grow, especially for the top two agencies (see Exhibit 5) Hana Tour and Mode Tour, which together held over 50% of the package tour market in almost every region. Two-thirds of Korean package tours in South East Asia were from these two companies.

Exhibit 4
Market Share of Travel Agencies in Outbound Traveling (2012)



Source: Global Travel News (http://www.gtn.co.kr/mobile/news_view.asp?news_seq=52444&s_key)

Exhibit 5
Market Share of the Top Two Korean Travel Agencies by Destination Region (2012)



Source: Global Travel News (http://www.gtn.co.kr/mobile/news_view.asp?news_seq=52421&s_key)

Meanwhile, small Korean travel agencies were focused on niche markets such as trekking, pilgrimages, golf trips, business trips, and so forth. An increasing number of local tour operators bypassed Korean travel agencies to organize their own on-site tour programs, such as a one-day walking tour in Paris, which they marketed and sold directly to travelers (like Korean travel agencies but without the flights, transfers, and accommodations). These small tour operators, however, offered the same types of guided tour as typical package tours did. In addition, they had limited access to customers and relied on word-of-mouth and online marketing.

Competition in the Package Tour Industry

The travel industry in Korea has followed a typical strategy of market competition. First, it segmented the market by price and offered tour products at a variety of price points. Once customers have planned on their tour destination, they can trade up or down between luxury-class, standard-class, and budget-class package tour products. There was little difference among these products except for the quality of accommodations, flights, and meals and the number of activities on offer.

The price of package tours has dropped over time. In 1999, a package tour in Europe (five countries, 12 days) cost \$3,376. In 2016, the same package tour cost around \$2,400, 30% cheaper than 17 years earlier.⁴

4 Kang, Sehee. "The Package Tour Price Going Backwards as Times Passes." *Global Travel News* 3 November 2016. (In Korean) Accessible at http://www.gtn.co.kr/mobile/news_view.asp?news_seq=66409

Exhibit 6

Comparison between Travel Categories

Hanoi, Vietnam (5 Days) April 8, 2018 – April 12, 2018			
	Budget class (AVP106180408VJ6)	Standard class (AVP102180409VJ3)	Luxury class (AVP103180408OZ)
Price	\$278	\$648	\$1,234
Flight	VietJet	VietJet	Asiana Airlines
Accommodation	Three/Four Star Hotels	Four Star Hotel	Five Star Hotels
Tour programs	Basic tours; many optional tours all at extra cost	Some optional tours included at the given price	Special tours included in the price
Meals	Basic meal choices in package tourist restaurants	Basic meal choices Extra: Luxury cruise buffet	Upgraded meal choices Extra: Luxury cruise buffet & Sheraton hotel dinner
Compulsory tipping	Tips for guide and driver (\$40 per day, per person)	Tips for guide and driver (\$40 per day, per person)	No tipping
Shopping included	4 times	3 times	2 times

Source: Aggregated from Hanatour website (<http://hanatour.com/>) by the author. Product number is noted under the name of each tour class.

As these products were undifferentiated, companies spent heavily on marketing. In 2012, the top 24 tour companies spent \$14.7 million on newspaper ads alone.⁵ In addition, promotions through alternative channels attained more importance. Companies increased their investments in home shopping channels and search engine marketing, trying to create various products to target specific customers, like honeymooners and golfers. However, these efforts were easily imitated by competitors.

Severe competition among tour companies increased the cost of marketing and development, which in turn increased the overall costs that affect the price for potential travelers. However, with undifferentiated package tour products, companies could not raise their prices (in line with increased marketing costs) but were pressured to lower them. In order to remain profitable amid falling prices and increasing costs, Korean travel agencies reduced fees for inbound travel operators. That is, instead of giving up their margins, Korean travel agencies used their bargaining power with subcontractors to make inbound travel operators sacrifice their fees.

5 Pyeon, Sunghye. "Over 50 travel agencies spent 20 billion won for newspaper ads." *Global Travel News* 3 January 2013. (In Korean) Accessible at http://www.gtn.co.kr/mobile/news_view.asp?news_seq=52418&s_key

This lowered the quality of tour services and reduced the rates paid to local guides. The latter tried to recoup their losses by charging commissions from specialty tourist shops, negotiating with hotels for lower room rates with reduced services, and forced tips. As their wages increasingly came from such commissions from tour activities and shops, guides were increasingly incentivized to allocate more time to shopping excursions and optional tours that travelers had to pay extra for. Eventually, this kind of package tour involved compulsory shopping trips and optional extras such as supplementary attractions, cultural shows, or local restaurants at additional cost.

Disgruntled Customers

For customers, the eager anticipation felt before overseas travel often transforms into dissatisfaction over the course of the tour. Although the tour itinerary advises them of flight and hotel information in advance, the package tourists get an unpleasant surprise when they arrive at their destination to discover that tipping the guide and shopping excursions are compulsory. They feel that local guides function as salespeople rather than local escorts because they rely on stores to pay them commissions based on tourists' purchases.

This is particularly true for travelers on budget package tours, who are brought to shopping centers three to six times in the course of a trip. Such travelers feel pressured to buy certain goods; if not, they may receive inferior treatment by the guide over the following days. Travelers who refuse to join shopping excursions or optional activities must spend that time waiting on the tour bus for safety reasons. "I felt like we were stopping by main tourist spots on our way to shopping centers and optional tours," observed one frustrated traveler.⁶ There are instances of tension between guide and tourists: "I was told that, if I didn't take the optional tour, the rest of the group wouldn't be able to go because of me," another traveler reported to the Korea Consumer Agency.

Due to unexpected shopping and optional tours, travelers end up spending extra money, especially when the price of the package tour is low. For example, the cheapest tour products, typically less than \$300, spend an additional 86.4% over the package tour price.⁷ Ultimately a 'cheap' package tour is not a bargain if the total cost is not significantly different from that of a standard package tour.

Customers are looking for change: 83% of package travelers approve of government intervention to rectify the malpractices of tour operators.⁸ As customers become frustrated with current offerings, it has become increasingly difficult for travel agencies to retain their loyalty. 89% of customers use the same travel agency for the second trip (presumably giving them a second chance) but only 8.6% of travelers choose the same company for the third time.⁹ Frustrated package tourists have migrated to the independent travel market as it has become easier and more convenient to make cheaper and more informed travel arrangements online. Travel agencies must compete ever more intensely for a share of the shrinking demand for package tours. At the same time, package tour companies have endeavored to make a dent in the rapidly growing

6 Lee, Sungbum. "Is 'Optional Tour' really optional in the package tour?" *Gukje News* 29 May 2017. (In Korean) Accessible at <http://www.gukjenews.com/news/articleView.html?idxno=718033>

7 Korea Consumer Agency (2013). *Status of Overseas Package Tour Products and Comparisons among Travel Agencies*. (In Korean)

8 *Ibid.*

9 Pyeon, Sunghye. "Statistics on Repurchase Rates/ Sales Breakdown by Tour Product Category." *Global Travel News* 3 January 2013. (In Korean) Accessible at http://www.gtn.co.kr/mobile/news_view.asp?news_seq=52423&s_key

independent travel industry, diversifying their business portfolios with products such as airtel, which combines flight and hotel booking. However, even in this market, the ease of online price comparisons has kept the profit margins low. Global online tour agencies such as Expedia, Booking.com, and Agoda have already established a strong position in this market with global networks of entrenched resources.

While package tours suffered from shrinking demand and declining profitability declining. the independent travel market was becoming intensely competitive thanks to online price comparison sites that have established thin profit margins. In this situation, what strategy could travel agencies pursue to achieve profitable growth?

Package Tour or Independent Travel: Which Will You Choose for Your Next Trip?

Nari, who works for a Korean conglomerate, is planning a holiday in France this summer. She is too busy to make her own travel arrangements, which include booking flights and hotels, as well as researching local activities. She could purchase a package tour product, leaving everything in the hands of a travel agency, and yet she prefers to relish her freedom as she explores a new, foreign destination. She doesn't like the idea of being forced to spend time in tourist attractions with unfamiliar members of a tour group. A colleague who visited a friend in Paris the previous summer has given her a list of places to go and things to do. Nari wishes she had a friend with whom she could experience Paris in all its glory.

Eugene is an urban planner for the Seoul Metropolitan Government. He is going on a business trip to Germany to conduct a study of environmental policies imposed by municipalities. He wants to go to Freiburg, Germany's ecological capital, but it's a three-hour drive from Frankfurt. After contacting several travel agencies to arrange a day trip to Freiburg, he has still found no guide familiar with the area or willing to charge a reasonable price for a customized trip. Eugene has a dilemma – to use an expensive tour guide or gamble on making an independent excursion with only a two-page guidebook to provide information.

Might there be a new way for people like Nari and Eugene to travel? How might it be possible for each of them to enjoy an authentic, meaningful trip? Prepare for the in-class exercise, Blue Ocean Hackathon, for formulating a market-creating strategy using the worksheets provided.

Visualized recap of the Korean Travel Industry

See for yourself the short video clips that illustrate vividly how the travel industry in Korea competed and the real pain points of packaged tour buyers. Scan the QR codes below or click them to watch the videos that are only two to three minutes long. The narrated storytelling with customer/guide interviews will show you the reality of the industry landscape.



<https://teach.blueoceanstrategy.com/qr/bosh1>



<https://teach.blueoceanstrategy.com/qr/bosh2>

Blue Ocean Hackathon: Hands-on exercise to create a Blue Ocean alternative that can unlock hidden demand

Hack-away the conventional logic of market competition and create a novel strategy for opening a new market space in Korea's crowded travel industry. As a team, you will follow the steps described below, using the tools of Blue Ocean Shift. For an effective class exercise, the As-Is Strategy Canvas is provided in Appendix 1.

Ask your instructor for worksheets for this exercise.

Step 1. Discover hidden blocks to utilities in the package tour industry by developing the Buyer Utility Map in Worksheet 1.

Step 2. Identify noncustomers of the package tour industry by analyzing the Three Tiers of Noncustomers in Worksheet 2.

Step 3. Explore ways to reconstruct the market boundaries by using the Six Paths Framework in Worksheet 3.

Step 4. Create a new strategic profile that can break the value-cost trade-off by taking actions on the Eliminate-Reduce-Raise-Create Grid in Worksheet 4.

Step 5. Envision your new strategy vis-à-vis the current industry standard (the As-Is Strategy) by creating a To-Be Strategy Canvas in Worksheet 5.

In the classroom lecture after this exercise, you will be introduced to a start-up that successfully created a Blue Ocean and managed to unlock new demand in Korea's divided travel industry.

Appendix 1
Strategy Canvas of Package Tour Industry

