



# Strategies for cross-border travel supply chains: Gaming chinese group tours to Taiwan



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## HIGHLIGHTS

- A game-based mathematical model and deriving strategic implications.
- A cross-border TSC from the case observation of Chinese group tours to Taiwan.
- Factors and effects for profit maximization of an individual reception operator.
- Destinations suffered from the low group fees are undergoing a prison dilemma.
- Fostering differentiated products and cooperative conditions are imperative.

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## ABSTRACT

In examining the relationship between tour group operators and reception travel agencies, an in-depth mathematical decomposition of product price structure is a key process in understanding its dynamic interactions. There are strategic positions regarding the imbalance between tour group and reception travel agencies, and fierce competition is recorded within the destination market. We construct a cross-border travel supply chain model and derive the influence of commission, reception fee, and administrative cost. An inadequate combination of these factors will lead to zero-commission tours. However, punitive and leadership countermeasures to the prisoner's dilemma for reception operators can be achieved not only from their own and management's self-disciplinary agreements by the destination authority, but also from support and actions under a consensus covering both group organizers and destinations. We provide strategic implications along with Taiwanese empirical evidence, and provide a reference and foundation for other destinations regarding market price-quantity simulations and strategic options.

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## 1. Introduction

There are numerous studies focusing on cross-sector *coopetition* (cooperation and competition) and tourism integration. Besides these relationships, an important issue that depicts the coopetition between grouping and reception travel agencies is the price structure and the operation of tourism products. The reception travel agencies need to consider negotiating with tour group agencies, increasing profit and distinguishing their products from other non-differentiated products, and catering to the quality demands of tourism authorities. Taking Taiwan as an example, most

travel agencies are small and medium enterprises with minimal capital and high labor costs. While facing international competition, the impact of and challenges posed by cross-sector connections are inevitable and internationalization is underachieved. Firms operating in the traditional solitary mode and engaging in price wars have lower and unstable profits, and have to appeal to the government for assistance and protection due to their weaknesses. According to statistics for the first quarter of 2016, the arrival of Chinese groups represents 55.45% of Chinese leisure trips. This explains the intensive interaction between tour group and reception travel agencies. Nevertheless, Taiwan has low-price products, high commissions, and low travel quality. In order to analyze this phenomenon, the decomposition of price and quantity for both grouping and destination supply chains is used. Furthermore, an in-depth analysis of the mindset and considerations adopted by

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agencies should also be considered in the game.

Tourism development between Taiwan and China has shown gradual progress under current negotiations and political consensus. Since 1987, Taiwanese residents have been permitted to visit China. Taiwan also implemented an open policy for groups of Chinese tourists in 2008. Although Taiwan was a late outbound destination for China, the policy had been a great breakthrough, increasing interaction and understanding, and prompting Taiwan's tourism to promote its economic benefits and boost the number of arrivals. Chinese arrivals to Taiwan increased and become the largest source of tourism to Taiwan two years into the enforcement of this policy, soaring to new highs among all source markets. As such, the Chinese outbound market is a new and significant opportunity for tourism in Taiwan. However, destination image and benefits can suffer from unethical approaches due to the lack of countermeasures from authorities. Seeking equilibrium between industries is beneficial, with sustainable development being a responsibility and challenge to tourism authorities. Regarding the importance of a balanced market, Taiwan masterminded an elaborate mechanism to maintain travel quality and destination standards. These measures cover quality requirements and intensive inspections, as well as blocking unreasonable reception fees and shopping-oriented tours. The regulations are designed from both administrative and business considerations and greatly increase the administrative costs of authorities and enterprises. As such, administrative effects should be examined constantly from the reactions of the industry and the consequences for the market.

According to basic economic theory, any enterprise should have sustainable growth and will strive to maximize its profit. Product advantages and price, customer volume, and the destination cost are the main factors affecting profits for typical travel agencies. Under strong competition, they will cut prices, although this leads to negative consequences for market prices and equilibrium quantities. In other words, travel agencies will have no choice but to cut prices in the absence of better solutions. The tourism industry and administrative authorities urge a cooperative alliance for mutual benefit, thus preventing this type of behavior from travel agencies. There are two types of business model of inbound group tour in destination. One is non-commission based model, of which most of the income of reception operators are from the group fee of tourists, while the income of commission based model are mainly from the commission of shopping. The zero-fare is an extreme phenomenon of commission based model known in Chinese outbound market, in which the tourists barely pay the group fee (Wong & McKercher, 2012). From the standpoint of reception operators, this study argues one of the situations to influence reception condition is the price-quantity in the business model. The structure and variation of the items related to revenue, such as group fee/reception price, commission, quantity of tourists received, and reception cost, are decisive the formation of business model. For the price-quantity situation, this study establishes a generalized equation derived from a widely recognized two-tier assembly model, which is then introduced as a two-tier tourism supply model, to give a functional explanation for the formation of business model as well as the price difference of zero-fare. Another situation is the game strategy which the reception operators apply. The cooperative strategy of reception operators could form strategic alliances and claim reasonable reception conditions against the grouping agencies with price-dominated advantage, also to prevent the price competition among reception operators. On the other side, a non-cooperative strategy could induce or worsen the commission based model. Besides the impacts of strategies adopted on income and reception quantity, a prisoner's dilemma is derived from the commission based model along with the generalized equation. Furthermore, for the appeal of an effective management

on the commission based business model for its negative reputation to destination (Zhang, Heung, & Yan, 2009a), this study incorporates the administrative impact on the non-cooperative business model with the equation. In section 3, the description includes the importance of the Chinese inbound market to Taiwan, the issues between grouping agencies and reception operators, the cooperative agreements which the reception operators had struggled portray the scenario in Taiwan. In section 4, the Cross-border equation is developed as a fundamental to equilibrium price/quantity and proceeding analysis. The empirical cases illustrate the results from different price/quantity and strategies are discussed in section 4.6. The verification and validation of the equation and model are proposed in section 4.7.

## 2. Literature review

Most of the research in recent years on the Chinese outbound market comprises destination, tourist, and source market-related studies. This literature is generally circumstantial, time-specific, and of similar design (Tse, 2015). The massive scale of Chinese outbound tourism is an important resource to neighboring areas. Boosting the economy by engaging in tourism development is also a key tourism policy of nearby destinations. Tourism development in Northeast Asia is growing increasingly competitive, and the Nash equilibrium strategy is commonly applied to explain interdependency among these destinations (Tran & Thompson, 2015). The dynamics of competition and cooperation between cross-border travel agents are equally imperative in forming the dominant strategy of a destination's tourism policy. Low price and inferior quality mass-market packaged tours in the Chinese outbound market are common, although there is a growing trend towards independent travel. Free individual travelers (FITs) emphasize experience rather than scenery. The shopping places, souvenir items, and consumption behaviors of FITs are self-organized, instead of commission-driven as is the case for tour guides (Arlt & Burns, 2013). Nevertheless, FITs are an increasing trend, but do not compete with the growing traditional tours. Low cost tours are consumer favorites and dominate the outbound market. Zhang, Yan, and Li (2009c) confirm the validity of their proposed nine factors causing zero-commission tours, using Atlas.ti qualitative analysis software for 30 cases. In suggesting further investigations in other countries, Zhang et al. (2009a,b,c) propose the implementation of both policy and business countermeasures to curb this phenomenon. According to the selection of day tour itineraries in Macau, Wong and McKercher (2012) show that experiential values are almost entirely lacking in itineraries of commission-based tours. Conversely, a better balance between experiential and operational considerations drives itinerary choices for zero-commission tours. One of the extensive debates on zero-commission group tours is quality deterioration, which is arguably the consequence of information asymmetries (Chen, Mak, & Song, 2011). Some studies support a taxation structure adjustment and point out that a change in tax rate for optional tours could adjust tourist arrivals and curb unreasonable commissions. When discussing the tax mechanism approach, the assumptions of profit distortion of related sectors and government intervention in the destination are debatable subjects (Guo, Shi, Dong, Guo, & Anderson, 2014).

The wrestle-or-handshake relationship between tour group agencies and travel operators is discussed in the zero-commission tour (also see zero-fare tour, zero-tour) issue. Zhang, Heung, and Yan (2009a) see the zero-commission model as a legitimate price-reduction strategy adopted by foreign operators to attract Chinese outbound tourists. They maintain that it should be regulated because of negative consequences that can in fact seriously

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