Journal of Air Law and Commerce

Volume 27 | Issue 4 Article 2

1961

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THE SELECTION OF TRAVEL AGENTS FOR THE SELLING OF AIR TRAVEL

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INTRODUCTION

FOR the first time in the history of commercial air transportation the volume of passenger business measured in passenger miles carried by the domestic airlines of the United States, exceeded that moved by the railroads of this country during the year 1957. The postwar increase in its share of the common carrier market from a little over six per cent in 1946 to a figure approaching fifty per cent today certainly establishes the airlines as the fastest growing form of public transportation. And yet, many of those familiar with the industry predict that the next ten years will see more growth in air passenger transportation than was accomplished in the last twenty-five. It is often pointed out that only a relatively few persons flying relatively great distances account for the large passenger mile figure of airline volume. Most of the population has never been in an airplane. The growth in population can be expected to add several million more potential customers for everything, including air transportation. The airlines plan to meet the future needs for air transport with faster, larger jet aircraft, more effective airway techniques, larger airports, and more efficient ground handling of passengers and baggage.

But with all these bright hopes for the future, the airlines are facing increasingly higher costs, and competition of increasing intensity. In case after case, the Civil Aeronautics Board has opened the doors to competition between airlines by issuance of new route permits. To competition with surface transportation, both public and private, a new dimension of active intra-modal competition, has been added. In a large part, this accounts for the argument of some who feel that with the added capacity for producing available seat miles which the new jets make possible, the airlines are providing a surplus of available air transportation service. In any case, the pressure upon the marketing function, which with the possible exception of the war years, has always been great in this industry, can be expected to increase. Finding enough passengers to use the expanding productive capacity is a vital problem for the individual airline as well as for the industry.

The glamour of high speed aircraft and its fantastic capacity to shorten distance in terms of time has tended to over-emphasize the productive features of airline transport. The effective performance of the marketing function while not necessarily taken for granted, may not have been fully appreciated. This paper is intended to be a commentary on the background of decisions concerning the selection of a marketing channel for the sale of air travel with particular emphasis upon the selection of travel agents for this purpose.

Like all common carriers of passengers, the airlines from their early beginnings have used agents in the sale of their services. The sale of air travel by agents was disorganized and somewhat unsatisfactory from the viewpoint of all concerned prior to World War II. Since 1945, a more stable and useful agency arrangement has been forming. The recent Air Traffic Conference Agency Resolution Investigation disclosed that the number of agents increased from 597 in 1945 to 2400 in 1956 and that the commissions paid to agents increased from nothing in the war years to $13,200,000 in 1956. During the latter year, 20.2 per cent of the domestic airlines' business was sold through travel agents. While current data is not available, there is reason to believe that the trend continues.

FACTORS AFFECTING CHOICE OF AIR TRAVEL SALES CHANNELS

When should airlines use travel bureaus as sales agents and when should they use their own offices and their own employees? The difficulty of answering this question stems from the fact that the individual airline operates in so many different markets and that its markets have so many different segments or strata. The product is air travel of a particular type, between two particular points, undertaken by people for a particular reason. As viewed by the purchaser, air travel between Chicago and New York for business or commercial purposes is not the same product nor is it sold in the same market as air travel between New York and Miami, nor the same as air travel New York to Shannon as part of a three week post-convention sight-seeing tour of Europe. There are different segments, as defined by the users concept of the service, of different markets as defined by the particular distances overcome. To reach the potential purchasers in these different segments of these numerous and different markets can give rise to different costs due to differences in concentration of "potential" buyers, repetition of purchase, amount of ancillary services which must be provided, and the amount of searching or shopping which characterizes the behaviour of patrons in certain segments.

Superimposed, as it were, are certain endogenous and exogenous factors. The opportunity cost of using travel agents in a given market may vary among carriers due to different load factors and different marginal production costs as well as marginal selling costs via carriers own ticket offices. The extent to which the management is growth as against current profit oriented may have a bearing upon the decision to use or not to use agents. Perhaps the most important external consideration is whether the carrier, in the particular market under consideration, is faced with inter-agency or intra-agency competition.[1] Is competition only with surface carriers in this market or is there another air carrier whose behavior directly affects the sales outlet choice and vice versa? The latter is perhaps the typical situation. With new route awards in recent years there are few significant markets left where there is only one air carrier offering service. However, in order to simplify the problem of marketing channel selection it will be useful to assume no other carrier competition for the present.

Inter-Agency Competitive Markets

The principal physical characteristics of the product, air transportation, is the capacity to move a passenger from a particular place to another place within a certain time with a certain measure of convenience and comfort. The carrier may be said to be for example, in the Chicago-New York air travel market. This geographic description may be expanded further to local or long haul, feeder or trunk. The time necessary to accomplish the movement as well as the timing, that is, the time of day are important features. This degree of comfort as described the terms first class or coach is another characteristic. At least in respect to the points mentioned, the air travel

[1] The term inter-agency refers to those markets where the airline faces competition only from other agencies forms or modes of transport such as rail or bus. Intra-agency refers to competition between two or more airlines in a particular market.

produced and sold is subject to certain physical limitations and identifiable characteristics.

To reach the potential buyers of this service and more particularly in selecting a channel or channels that will reach them most effectively, a physical description of the product is not enough. More to the point are the market characteristics of the potential users and their concepts of the use characteristics of the service.

One of the relevant characteristics of the potential user of air service is his location. The first consideration has to do with concentration of potential buyers as against sparseness of buyers in a given area. A high rate of repeat business may overcome the absence of a concentration of purchasers.

Perhaps market characteristics of potential buyers should also include some measure of disposable income. Their reaction to seasonable unpleasantness of climate, family and cultural ties with people in distant places and any other factors that would provide an urge to travel should be considered. The amount of "education" of the user before he can be persuaded to use air transportation is important. Related to this are the many auxiliary services that must be provided for the relatively inexperienced traveler. Reference is made here to passports, hotel reservations, baggage arrangements, sightseeing, connecting line reservations and so forth.

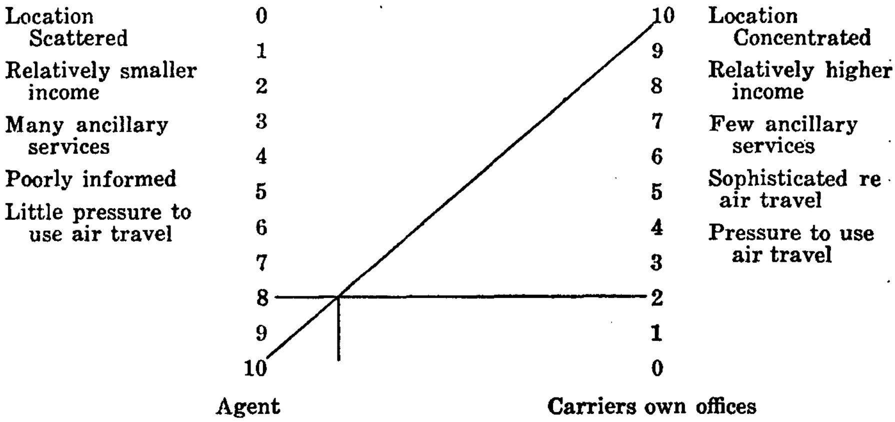
Use characteristics of product refers particularly to the general uses to which the product is put or the nature of the demand for it. Is it a consumer demand or a derived demand? The demand for air transportation for use in connection with vacations, pleasure or tour travel can be considered as rising directly from the ultimate consumer. The demand for air travel in connection with business or commercial pursuits could be considered a derived demand. The use to which the product is put is a reflection of the users concept of the product's utility. This utility is not as clear to the vacationer or tourist as it is to the businessman. For the former, the product needs considerably more adjustment before its usefulness can be realized. Such users are not as concentrated in location as are the business users. The purchase of air transportation for commercial uses may, in many areas, be concentrated in one man or one department regardless of who actually makes use of the service. This is not so in the case of pleasure travel (unless some intermediary specialist be placed in the channel to concentrate this demand). The rate of repeat purchases is generally considerably higher by commercial users than by pleasure travelers.

Market segment characteristics. From these limited characteristics of users and potential users of air transportation and their concepts of the uses of such service, certain characteristics of segments of the market for air travel can be defined. There may be, for example, a concentrated commercial segment of the Chicago-New York market for air travel, a scattered vacation segment of the New York-Hawaii market and other combinations.

The characteristics may be listed in two reciprocal categories as follows:

Location of user—	Location of user—
Scattered	Concentrated
Relative great distance from company sales outlet	Close to company sales outlet
Relatively smaller incomes	Relatively higher incomes
Many ancillary services	Few ancillary services
Poorly informed re travel	More sophisticated re travel
Relatively little "pressure" to use air travel	Competition may make use of air travel essential

The market segment diagram. The basis for the importance of these factors in the selection of marketing channels within the sales program is the cost differences that result from the requirements necessary to reach buyers in these different sectors of different markets. There are certain segments of a market where the use of intermediaries or indirect channels are more useful than in others. If the characteristics mentioned above can be given some measure of value the following diagram has some conceptual usefulness in suggesting when agents or direct sales offices should be used.



In the early history of air travel when the potential users were relatively scattered, when they were poorly informed regarding the service and when there was no particular necessity to fly, a great deal of missionary selling and special promotional effort was necessary. Maximum sales outlets appeared desirable.

Add to this the rather sharp limitation of the early airlines' financial resources. Under such circumstances the characteristic in the left hand column would be more descriptive of the market segment. Assume that their value totaled 8 and that the extent to which the potential user could be said to be concentrated, need few additional sales services and have some sophistication regarding air travel, totaled 2. A line may be drawn connecting these two values. Where this line intersects the diagonal (an iso-gram on which the sum of the value of all characterization always equals 10) indicates the bias either toward the use of agencies or the use of direct selling through the carriers own offices and with its own employees. In this case the use of agents is indicated. As the potential users of the service become more concentrated, more familiar with the service and as his purchases are repeated more often, the values on the left become less and the values on the right, greater; the horizontal line connecting them rises and intersects the diagonal further to the right indicating greater usefulness of direct marketing channels.

Criteria for selection. There is at any time a unique combination of user and use characteristics that apply to each segment of a market. The number of different combinations indicate and define the number of segments and the marketing differences between them. Effective channel selection results in the use of the most economical means of bridging the gap between the producer and user of air service.

Before the carrier can determine the need for the agent's services it should have some idea of the cost in terms of units sold to reach the market segment via some alternative, possibly its own ticket office. In some cases it may be clear on observation that the segment is so scattered in sales potential that a carrier operated ticket office could not possibly earn sufficient revenue to make direct costs. There could be, on the other hand, many cases where this is not clear and where the appointment of an agent could result in the duplication of existing facilities and the interception of traffic that could otherwise be sold by existing company ticket offices at less cost than the cost of using the agent intermediary. There are many ways in which this cost can be stated. The use to which the cost estimate is to be put should dictate how cost should be measured. Standard costs may be useful for production control and average cost may be best suited to the determination of the optimum number of inventory orders. As a general statement it is safe to say that those costs should be considered that are relevant to the decision. If the decision has long run implications, revenue and cost estimates should reflect this dimension to the extent that such estimates can be made. Unfortunately, however, the longer the estimates are projected into time the less accurate they become. Relevancy can best be estimated for the relative short run. Costs which are not changed by the dicision need not be considered. Only those costs which reflect a change are relevant. This suggests marginal cost. Thus we are faced with the conclusion that the agent should be used if the marginal gain that follows such a selection exceeds the marginal cost. This is the conclusion that would be expected from a model of certainty. The use of such a model however, overlooks and does not account for a most significant variable i.e., the interdependent effect of the action of a competitor in an oligopoly market.

Channel choice in intra-agency competitive markets

The domestic airlines of the United States operate in markets of imperfect competition. In some cases actual monopoly of air travel may exist. Generally speaking, their markets have the characteristics of an oligopoly. While air transportation may be an industry affected with the public interest, (it is certainly not unique in this respect), it is hardly a "natural monopoly" in the same sense in which the term applies to telephone or railway services. Whether substantially or significantly more competition could be developed in the industry if it were not for certain Federal regulatory policies, and further, whether this additional competition would or would not be desirable, is not the concern of this paper.

As in all oligopoly situations, airline managers, in making marketing decisions, must guess what readjustment they will have to make later to compensate for the reaction of other airlines in that market. In the early days of the air travel industry commissions on tickets were offered and paid to anyone from hotel porters to traffic managers of large corporations as well as travel bureaus. Within a short period of time several thousand persons were receiving airline commissions, and the amount was substantial.

> The airlines discovered before World War II . . . that they were bidding against one another for every ticket. Any reference to Joe, the shoe shine boy, the pool hall and drug store, I am informed are not hypothetical. They were prepared to pay a commission in those days for any ticket that could be produced. And one carrier could tell Joe, the shoe shine boy, "any time you can sell a ticket for us we will give you 5 per cent."
>
> And the next carrier would find that Joe, the shoe shine boy was pretty good at producing a passenger or two passengers a day. So they would give him 8 per cent and the third carrier would give him 10 per cent and so on.[2]

Air carriers who are not members of the Air Transport Association and who have had no formal arrangements for reaching an agreement in this

[2] U.S. Congress, House of Representatives, *Monopoly Problems in Regulated Industries*, Hearings before the Anti-trust Subcommittee of the Committee on the Judiciary. 84th Congress, 2nd Sess., February-June 1956 Part 1 Airlines. Testimony of Donald Markham, Assastant General Counsel, Air Transport Association Vol. 3, p. 1765.

area are said to have paid as high as 80 per cent for such selling service in recent years.[3]

The sale of air travel through such agency outlets constituted a serious problem. It was unsatisfactory in respect to cost measured directly in terms of selling expense and in terms of customer good will. It was apparent to airline management that this matter of agency representation was among the important problems requiring solution through joint industry action. To obtain such action was one of the reasons for the founding of the Air Transport Association of America in 1936.

A year later, Colonel Edgar S. Gorrell who was then President of the Association appeared before the House and Senate Committees on Interstate and Foreign Commerce with reference to various aspects of proposed legislation which culminated in the enactment of the Civil Aeronautics Act. Colonel Gorrell urged the Congress to provide for immunity for air carriers from anti-trust legislation for joint action and trade agreements. The problem of channel choice in the marketing of the service was singled out for specific mention.

> Some of the problems that may be readily cited . . . eliminating favors to hotel operators and others who may sell tickets; consolidating ticket agencies; regulating commissions to outside traffic agencies. . . .[4]

Power to grant the requested immunity was given by Congress to the Civil Aeronautics Board. The scheduled airlines formed the Air Traffic Conference within the Air Transport Association to set up the administrative procedure for appointment and retention of agents as well as establishment of commission rates. The first resolution filed with the Board in July 1940 has been modified on several occasions. The last modifications were the result of the Board's recent Air Traffic Conference Agency Resolution Investigation, Docket 8300. In general the agreement defines the relationship between the member airline and the travel agent, the rate of commission and provides for approval of "would be" agents by the Air Traffic Conference Agency Committee before the agent is eligible for appointment by a member carrier. The membership of the Agency Committee consists of traffic representatives employed by member carriers.

It is difficult to determine what actually goes on at an agency Committee meeting or what really determines how the members vote when considering the approval or retention of a travel agent.

> . . . in what is probably the usual smoke-filled hotel room—in which as many as eight hundred agency cases may be reviewed. . . . It is patent that from the standpoint of time alone, the procedure is inadequate for a mature decision. . . . Nor are any records kept of the Committee's deliberations or of votes on selection or retention of agents. The Secretary counts the show of hands on each vote but not actually record the count. The only record kept is the final action taken by the Committee on the individual cases of selection and retention of agents. This record consists of no more than a mere notation of the words "approved," "disapproved" or "deferred" made in pencil or ball point pen on the margin of an agenda sheet.
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> The record amply details the record-keeping practices of the carriers which have limited the availability of the contemporarily made documents, the most credible evidence of the carriers' agency practices. For example, the record shows that the documents pertaining to agents under review used by the representative of American Airlines at Committee meetings

[3] Speaking of agents representing non-scheduled carriers, William Longgood writing in the Washington Daily News of February 13, 1952 made the following comment. "The usual arrangement is for agents to sell passage on a commission of from 5 to 35 per cent. But some 'sharpies' have got up to 80 per cent from hard put carriers." Ibid. p. 1806.

[4] Initial Decision of James S. Keith, Hearing Examiner, *Air Traffic Conference Agency Resolution Investigation*, Docket 8300. Civil Aeronautics Board, Washington, November 3, 1958, p. 75.

> are destroyed at the close of each meeting. . . . United does not necessarily keep files on its agents, who have been removed from the list, nor does United keep its sponsorship files on agents throughout the years. . . . Eastern Airlines does not normally retain complete files on agents unless the files are currently active and of particular interest to Eastern. Air Traffic Conference's policy is to destroy old records, 'So as you have room for new records.'[5]

Existing agents may have their appointments cancelled by being taken off the approved list by the Agency Committee. Whatever members may feel objectively about an agent up for approval, one fact remains and that is that each member has an obligation to his employer. He is generally an official of an airline and responsible for the agency program of his Company. This responsibility must dictate the most important criteria to him, that is, does the approval or rejection of the agent under consideration further the ends of his company? The most important motivation of airline representatives voting on the Committee is the primary economic interest of their carrier employees. This often results in a conflict of interests of one or more members. Evidence introduced in the Air Traffic Conference Agency Resolution Investigation, Docket 8300, indicates that this results in considerable "horse trading" and the formation of blocs representing the interests of the differing groups. For example, there may be little need for representation by a travel agent as far as the dominant carrier in the market (defined in terms of city pairs e.g., Detroit to New York, Chicago to Washington, etc.) is concerned. Other carriers in that market who for one reason or another, perhaps because they were only recently awarded a route including this point, have a very low volume of business generated here may be anxious to encourage as much sales representation as possible. All carriers do not enjoy the same stage of development in all markets. The agent's commission is a very reasonable price to pay for traffic to fill space that would otherwise be empty. In the eagerness to obtain a greater share of this market the distinction between business and vacation travel may not be important. The first carrier will not "need" the agent and will vote against his approval. But the others may be able to muster support of the balance of the voting members perhaps by promising to vote in their interest in issues in which they are concerned. After the agent has been approved it may be better for the first carrier also to appoint him as an agent since it may be thought better to have him working for, rather than against the carrier.

Now a whole new set of problems arises. Cost analysis as it has been described may be irrelevant. Whether a carrier appoints an agent or not may depend upon its ability to convince other carriers that such appointment will not, at the very least, hurt their position or upon its ability to prevent the proposed agent's approval. A carrier may co-sponsor or appoint an agent, even though it does not need the agent (on the basis of analysis of the potential of the market segment in which he would operate and the cost of alternative channels), when it feels that it would be even worse off by not using him since he would otherwise solely represent the competition. The appointment of the agent becomes the lesser of the two evils. Many airline sales managers feel that as a result of this scramble for "equal representation" there are far too many air travel agent appointments and that considerable traffic is intercepted that could be sold at less cost through carrier owned ticket offices. From time to time efforts have been made to limit the number of approved agents. An amendment to the Agency Resolution was filed in April of 1953 which would have made a radical reduction in the rate of commissions paid on business travel and could have been

[5] Brief of Bureau of Air Operations to Examiner in *Air Traffic Conference Agency Resolution Investigation,* Docket 8300, Aug. 12, 1957, p. 35 and 13-14.

expected to result in the removal of many marginal agents. The proposal was withdrawn under pressure of protest by the American Society of Travel Agents and possible investigation by the Board. There is some indication that the member airlines were not in agreement regarding the proposal. Many of them evidently preferred to continue with agency representation as it existed. This was most likely to be true of the smaller carriers whose volume would not justify the overhead of company owned offices in all the points they serve.

Summary

Marketing channels are a bridge between the producer of a product or service and the consumer. It is important, indeed essential to successful channel selection, to recognize the heterogeneous nature of the market. It has been suggested that it is useful to describe the market for air passenger transportation in terms of the physical characteristics of the product and to further segmentize the market in terms of the use characteristics of the product and the characteristics of the users.

One is tempted to argue that airline management should be prepared to make channel selections with the greater precision that more accurate knowledge of cost would provide. This is, however, a dangerous oversimplification. Efforts to define and measure relevant costs of sales through company owned ticket offices generally appear to have made little progress. This is not to say that carrier officers are not aware of certain broad cost differences. The smaller trunk lines and local service carriers almost "instinctively" know that with their small volume, overhead would in many cases skyrocket unit costs well above the commission rate. For them the travel agents services are highly desirable in almost any market segment. The larger trunk lines appear to be more concerned about the comparison of channel costs than do the smaller trunk and local service carriers. They see a place for the travel agent in the sale of pleasure, vacation and creative travel in general, but prefer to handle their own commercial business at costs apparently less than the commission rate. They are not inclined to pay the costs of commission charges and loss of control of direct channels by letting agents "intercept" this traffic, although efforts to "break into" newly awarded route markets could reasonably be expected to modify this policy in those areas where an otherwise strong carrier has weak penetration.

Part of the cost of selling commercial traffic through company owned channels only, may well be the loss of traffic from other sectors such as vacation and pleasure travel that the agent may be developing. It may also include the loss of that part of the commercial traffic the agent controls and through this control is able to divert to a competing air carrier in the market in question.

The long run objectives of the carrier should not be overlooked. In the drive for long run maximization of return on investment it may be desirable to emphasize some feature that deliberately raises cost and reduces profit contribution in the short run. Consideration of short run profit contribution may be insufficient in some channel choice decisions. To enhance some long run factor such as identification and community relations, some carriers have indicated they operate their own sales offices at costs that are higher than those available through travel agents. It may be necessary to sub-optimize the short run objectives of the marketing function to the long run objectives of the carriers.

Marketing costs are very elusive. Often the costs of alternative channel opportunities can only be estimated and may be at best only a guess subject to confirmation by experiment. Such experiments may not always be possible and if possible may have seriously unfavorable long run effects. The difficulties of determining distribution costs are sufficiently awesome when the firm makes its purchases in a monopsonistic or perfectly competitive market. When the services of the agent are purchased in an oligoposonistic market the costs can only be determined after the action of other firms effected by the decision, is known.

In his brief to the Examiner, in the Agency Resolution Investigation, Bureau of Air Operations Counsel said, "It should be emphasized that we are not concerned here with the issue whether a particular airline will appoint a certain person as its sales agent. That is a matter within the sole discretion of the carrier acting independently."[6] Counsel misunderstands the nature of this market. No firm under such circumstances is free to act independently.

Bureau counsel further indicated, "that frequently a carrier will 'not stick its neck out' to sponsor an applicant but may be perfectly willing to appoint him once he secures a place on the list."[7] He implies some inconsistency on the part of the carriers in this connection. Counsel overlooks the change in circumstances that give rise to the apparent contradiction of choice. The carrier may consider an agent undesirable in the light of its own ends and vote accordingly which may also be an effort to keep others from appointing him. Once he is approved however, and has become, or appears about to become an agent for the competition, clearly it may now constitute less of a threat to the carrier's revenues, in an oligopoly market, to also appoint him.

The Air Traffic Conference recently modified the Agency Resolution to conform with the Board's order E-14012 which resulted from its investigation. The order compelled a change in the "ground rules" but the characteristics of the market are not changed. The Board has not changed the economic facts of life. Members of the Committee and airline marketing managers must find ways to adapt to these requirements. Evidence suggests that negotiation is carried on outside of the Committee and even at the local level. The new rules may drive some of these activities further underground.

While the record in the Air Traffic Resolution Investigation points to the belief that the interest of the Air Traffic Conference tends to become identified with the interests of the most economically powerful carriers in the group, it also appears that in their fear lest they be outdone in agency representation, airline marketing managers have appointed more agents than are economically useful. As a result considerable traffic is sold through higher cost channels. The air carriers may have been able to stop the bidding up of agent's commissions but they have not been effective in limiting the use of travel agents to that sector of the market where they can be the lower cost sales outlet. A significant amount of traffic that could be sold at lower costs through carrier owned offices is sold through agents because of excessive agency appointments.

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[6] Brief of Bureau of Air Operations in *Air Traffic Conference Agency Resolution Investigation*, Docket 8300, p. 5.

[7] Ibid., p. 25.