



Practice Case 10 (Travel Agency)

Question

A travel agency makes a 10% commission on all of its travel bookings. Their current profit before taxes is \$1MM, while the industry average ranges from \$2MM to \$3.5MM. Why are they making less than the industry average?

Recommended Solution

High Level Plan of Attack

- We need to understand the revenue stream and cost structure of the travel agency and conceptualize how each transaction contributes to the bottom line.
- Focus on the types of customers the agency services and how each type relates to profitability.

Lay Out Your Thoughts

- Use the Profitability Framework, with a focus on the cost side of the equation.
- Break your analysis down to the two types of customers: business and leisure.

Dig Deeper: Gather Facts/Make Calculations

- What is the total gross revenue for the agency per annum, on average? *\$10 million.*
- How does the revenue compare to other agencies with similar size? *They are about the same.*
- What about the product line? Does the agency handle any bookings other than travel tickets? *No. They just book tickets for their customers.*
- What are the different customer segments that the agency services? *There's the business traveler segment, which comprises about 40% of total revenue, and the leisure traveler segment with the remaining 60%.*
- How many total transactions does the agency process and what is the break down for each customer segment? *The total number of transactions is around one million per year. On average, about 300K go to the business segment, and 700K to the leisure.*
- Is there a cost associated with each transaction? *Yes, each transaction, regardless of which segment, costs \$9.*



- [Now you have all the necessary information to calculate the profitability of transactions for each segment. If you run the numbers, you will find the following information.]

<u>Segment</u>	<u>Share</u>	<u>Volume</u>	<u>Total Revenue</u>	<u>Revenue / Transaction</u>	<u>Cost / Transaction</u>	<u>Profit / Transaction</u>	<u>Gain</u>
Business	60%	300,000	\$ 6,000,000	\$ 20.00	\$ 9.00	\$ 11.00	\$ 3,300,000
Leisure	40%	700,000	\$ 4,000,000	\$ 5.71	\$ 9.00	\$ (3.29)	\$ (2,300,000)
			\$ 10,000,000				\$ 1,000,000

Key Findings

- The leisure travelers are draining your profitability. Either the cost per transaction is too high or the revenue per transaction made on the leisure is too low.

Recommendations

- Benchmark the cost structure of other travel agencies.
- Negotiate with the airlines on the possibility of charging a premium for leisure tickets or capture a larger commission through cost charged to the customer.
- Look into the possibility of reducing cost per transaction for the leisure travelers.
- Offer the leisure traveler other products to increase revenue per transaction such as hotel bookings and travel packages.
- Become a niche player and focus only on the business traveler