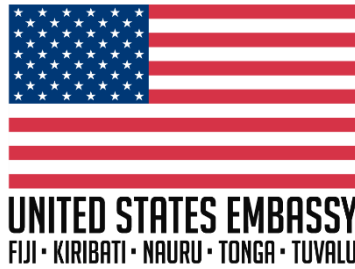




PACIFIC TOURISM
ORGANISATION



SPTO SME Recovery Toolkit

Chapter 4: Pricing

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Tools used for this chapter:

4.0	Template: Calculating prices for tours
4.1	Template: Calculating prices for accommodation

Chapter 4: Pricing



The last chapter of the handbook explained the importance of health, safety and security and the processes and measures that need to be in place to ensure the wellbeing of tourists, staff and community members.



In this chapter, you will gain guidance on pricing principles to ensure that your products are **priced competitively whilst providing a profit**. You will also benefit from general guidance on what factors to take into consideration when setting prices during the pandemic. At the end of the module, you should be able to:

- Understand the basic principles of pricing.
- Understand the implications of consumer trends on costs and pricing.
- Be able to apply basic pricing requirements to your own businesses.

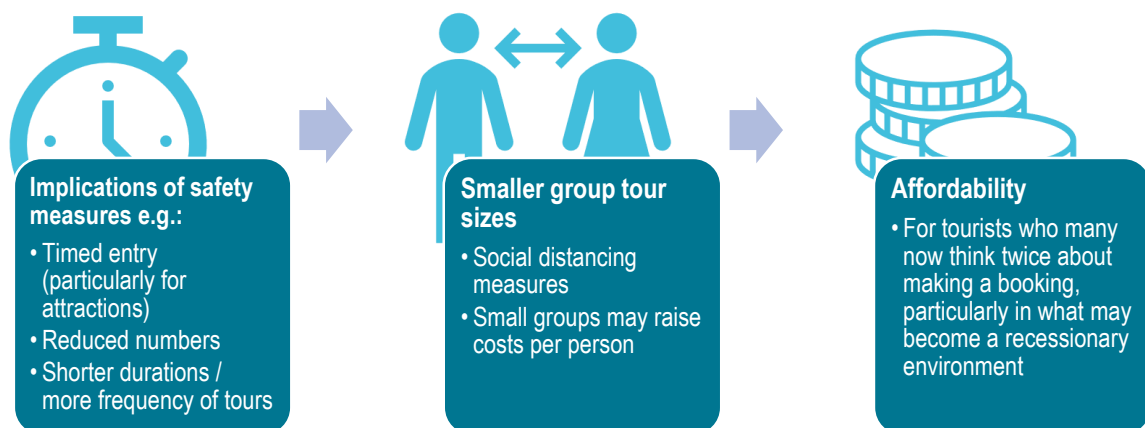
How to use this chapter of the handbook:

This chapter will walk you through the different steps to calculating prices. It is recommended that you read through each step at a time, review the examples provided and then reflect on your own business and situation.

Blank templates are provided in the toolkit to help you with working out your prices. You will see how to allow for mark-ups to be added by the different businesses that you might work with to sell your product such as inbound operators and travel agents. It is important to note that chapter 5 of the handbook will explain how they work in more depth.

How the pandemic is affecting pricing

The pandemic has forced tourism businesses to rethink how they package and sell their products and services. With the reduction in international tourists, there is greater reliance on the **regional** and **domestic** markets for business. You may therefore need to adapt your pricing structures to attract the few international tourists who are travelling and more visitors from the domestic / regional markets. Other factors that you will also need to consider when setting your prices are:

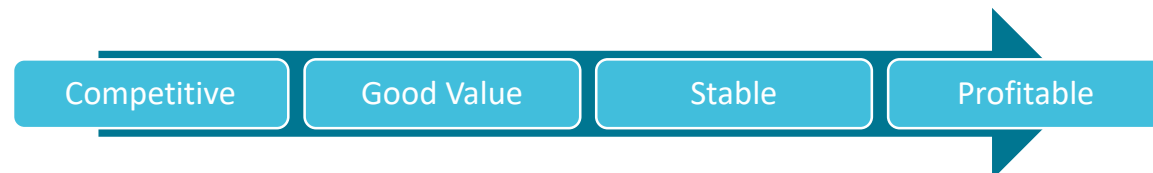


Consider how you will adjust your pricing to ensure you still make a profit.



Pricing Principles: What matters most?

Whether tourists are booking directly with you or via international tour operators, ground agents or online travel agents (OTAs) it is essential that a price reflects the following:



- ✓ **Competitive:** Tour operators will always compare a price to other attractions or accommodations. Tourists will shop around by comparing other similar options.
- ✓ **Good value for money:** Tourists must feel their experience is worth every cent.
- ✓ **Stable:** The price should ideally be fixed for up to one year, it is best to give the price in US\$.
- ✓ **Profitable:** The price must deliver a **profit for your business**. Tour operators and ground handlers need to also generate enough sales and make a decent profit margin to justify selling it.

What is a good price?

- ✓ A price that enables the **business to make a profit so that you earn a decent living** (as a main or additional income activity).
- ✓ A price that is **not too expensive** if compared to competitors **UNLESS** the product offers **something unique and can justify the higher price**.
- ✓ A price that **tourists are willing to pay**. Tourists are generally very price-conscious, and some travel on a very limited budget. *Remember all-inclusive visitors may have a very limited budget as all their meals are included in the price of their holiday. They may have budgeted for very little extra spending.*

If giving the price in a foreign currency, **currency fluctuation will need to be considered**. You may lose money if the exchange rate goes down and should plan for this.

What is 'good value for money'?

EVIDENCE OF 'GOOD VALUE'

Tour operators and ground handlers are less likely to ask small businesses to lower their overall price if they know part of the **money goes to the community** (e.g., donation, fund, payment to families or local artisans).

You must supply transparent costing to show this is the case, supported by evidence. There are templates to help with this.

The more expensive the product, the more tourists will expect in terms of **what is included**, level of **quality** and standard of **customer service**.

If the product does not include extras e.g. food, transport, guiding, tourists may have to pay for these things themselves so will bear this in mind when considering if the product is value for money

Common pricing types

Per person pricing: A set price per person e.g. adult and child prices. This is commonly used by activity/attraction and transport operators or backpacker accommodation and campsites. Options may include an adult, child and senior citizen price, with potentially a discount for groups.

Per unit pricing: A set price for one unit of the product e.g. price per night. This is the standard way to price accommodation. Usually, the advertised price is for two people so if the accommodation fits more than two guests it can have a mix of the per unit pricing with extra adult and extra child rates.

Single or double occupancy: This is common for B&B's or all-inclusive accommodations. There is a single rate and a double rate (which is not double that of the single rate).



Credit: David Kirkland & SPTO



Pricing Principles: understanding the costs

Fixed costs

- These are the **costs that remain constant** regardless of how many customers you have.
- Examples of fixed costs include transport, salaries, insurance, taxes, rent, internet, bank charges. Depending on your business, water and electricity may also remain fairly constant regardless of volume*



Variable Costs

- These are the costs that **will change or vary relative to how many customers** you have.
- Examples of variable costs include food, drinks, casual staff and other goods or services. Water and electricity utilities will be variable costs for accommodation providers. These can also be known as **incremental costs**



Carrying Capacity

- This is the **maximum number of tourists that the business can accommodate at any one time**.
- Factors to consider include: legal regulations, social distancing requirements for COVID-19, environmental considerations, the comfort of the visitors, practical considerations, such as how many visitors are able to hear and see a guide should all be considered.



If the product you're offering is not your main business (e.g. the main business is farming) then the business will need to **calculate the proportion of the fixed costs** that are related to that product. For example, for guided tours around a farm, a proportion of someone's salary will need to be allocated as a fixed cost for guiding.

Uncover hidden costs!

Not accounting for all of your costs will eat away at your profit so before you get started consider all of the value that you put into your product and identify the costs. Remember that **time and effort = money** so even if something is provided for free or small cost it still has a value and you should highlight this in calculating your costs. Examples of such costs include:

- Growing fruit and vegetables in your garden
- Attending paid for training such as first aid courses
- Training your staff on procedures and customer service.
- Transport costs relating to the running of your business
- Purchasing uniforms and providing equipment.

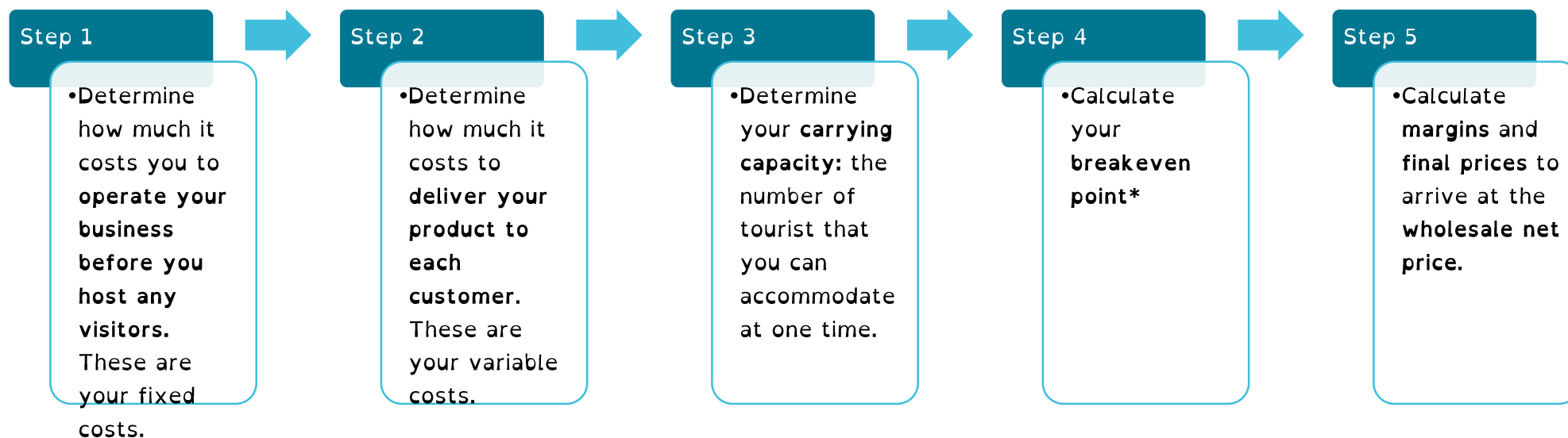
Keeping a record of these is also useful for tax reporting purposes to show all business expenses.



Credit: Jonathan Irish & SPTO

Pricing your tour product

The process for calculating price using the 'cost-plus profit' pricing strategy. This approach is illustrated in the 5 steps shown below and explained throughout this chapter of the handbook.



***BREAKEVEN** is the point of balance between either making a profit or a loss. It is where the cost and the revenue are equal. BUT this is not the final price (as seen by the customer).

A worked example is provided over the next four pages that illustrate the 'cost-plus profit' approach. There are also spreadsheet templates that contain the same examples. It is recommended that you open up the pricing template to view alongside these explanations.



[Tool 4.0](#)

Tours / experiences

Working with an example

A small farm which wants to open to visitors on certain days. The table below shows how to calculate fixed and variable costs per excursion trip.

Step 1:	
Fixed costs	\$ Cost per trip / tour
Overheads e.g. rent, insurance	40
Salaries	20
Total Fixed Costs (a)	60
Step 2:	
Variable costs	\$ Cost per person
Free gift e.g. handmade souvenir	3
Snack	4
Drink	1
Total variable Costs (b)	8
Step 3: Determine capacity limits	
Maximum Capacity	10

Total fixed cost is \$60.00 per trip and your total variable cost is \$8.00 per person.



Step 4

- Calculate your breakeven point
- **BREAKEVEN** is the point of **balance** between either making a profit or a loss. It is where the **cost and the revenue are equal**.
- BUT this is **not the final price** (as seen by the customer).

Step 4: Calculate Break even points

# of people in total group (d)	Total Fixed Costs (a)	Total Variable costs (b)	Total cost for group size (c)	Total cost per person (Breakeven point)
2	60	16	76	38.00
5	60	40	100	20.00
8	60	64	124	15.50
10	60	80	140	14.00

If 2 people visit the attraction on one trip the business would need to charge \$38 per person in order to **breakeven**.

If 10 people visit the attraction on one trip the business would need to charge \$14 per person in order to **breakeven**.

BUT this is **not the final price** (as seen by the customer).

The business now has to take into account the distribution chain and work out their margin to arrive at the **wholesale net price**.

Credit: David Kirkland & SPTO



Step 5

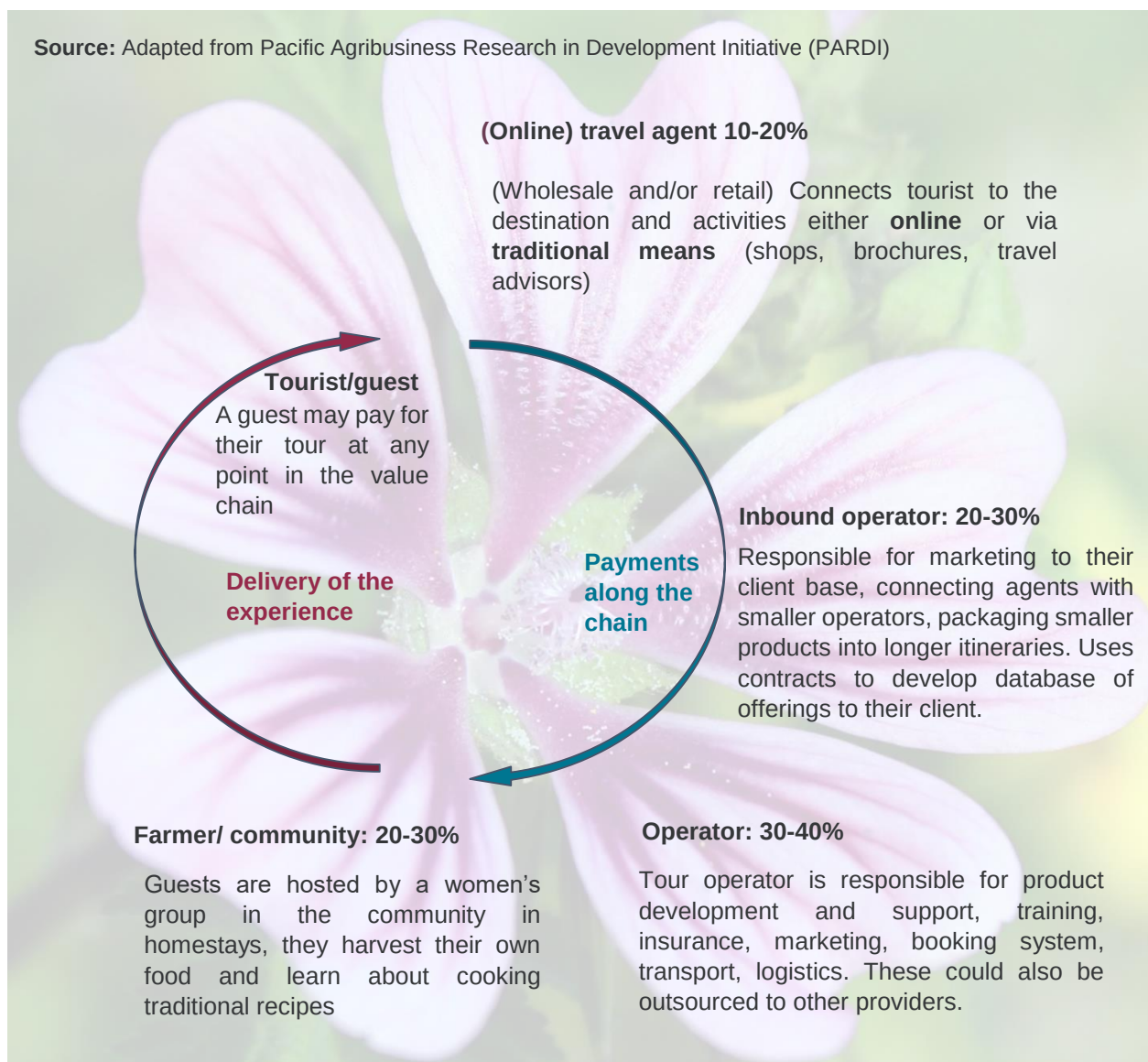
- Calculate margins and final prices
- The business now has to take into account the distribution / value chain and work out their margin to arrive at the **wholesale net price**.

Distribution Chain / Value Chain and Margins: How does it work?

All parties in the value chain must make a profit from selling the product by adding a **mark-up on top of the breakeven price**. The business's mark-up will often be lower than that of the ground agent / inbound agent and the tour operator. *(Note value chain members will be fully explained in chapter 5)*

Here is an illustration of the tourism value chain for a farm / community based tourism experience: the tourist payment is shared by the different actors in the chain. The amount paid in sales tax is not included, but can be a significant portion of the total sales price.

Source: Adapted from Pacific Agribusiness Research in Development Initiative (PARDI)



Calculating the final price

The following example is for illustrative purposes and shows a 'cost-plus profit' approach. **It is vital that you familiarise with how tour operators and OTAs apply commissions / mark-ups in your country** as this varies greatly in different regions. To do this connect with the relevant destination marketing organisation and other tourism businesses and associations in your country.

You 20% - 30%	+	Ground Agent / Inbound operator 20% - 30%	+	Tour Operator/ 30% - 40%	+	(Online) Travel Agent 10-20%	
Step 5: Add mark-ups							
# of people in total group (d)	Breakeven point	Your mark-up rate %	Net wholesale rate /	Mark up % for value chain	Final Price as advertised		
2	38.00	25%	47.50	50%	71.25		
5	20.00	25%	25.00	50%	37.50		
8	15.50	25%	19.38	50%	29.06		
10	14.00	25%	17.50	50%	26.25		

You can see that a product you might sell directly to customers or to an external agent would be priced at 47.50 per person for 2 people, but the price that the local agent or tour operator would **sell it for** would be **71.25**.

Make sure that your selling price can allow for a 50-60% external mark-up and still be competitive. If it does not, consider the following actions:

- You will need to either take a **lower profit**, which could work if you're dealing with large numbers of customers as you will achieve economies of scale but less so if you are offering a product to individuals or small groups.
- Review your 'offer' and associated costs and try to **reduce the cost** of delivering the product instead.

Other pricing strategies:

In addition to a 'cost-plus profit' approach as illustrated in this handbook it is also important to consider other factors or pricing strategies. This simply means the approach taken to calculate prices.

Competitor based strategy: If there are competing products offering similar experiences it is important to be match prices as long as you can still make a **reasonable profit** as has been illustrated. If you are unable to do this then you should revisit your costs and identify what can be reduced as it will not appeal to tourists if more expensive than other products without a clear unique offer.

Value-based strategy: If you have a unique tour or offer, for example, it takes place in a unique setting and you can demonstrate added-value (refer back to chapter 2) you may be able to set a higher price than other similar product offers.

How to negotiate prices with agents

When approaching a travel agent or tour operator to sell your tour product, you will need to show:

- **How** the price has been calculated
- **What** exactly will be delivered i.e. what will the customer get for the money?
- **Why** your product is appealing e.g. does it fill a gap in the market?
- **Why** it is good value for money e.g. compared to similar, or competing products?

There is more guidance on how to do this in the next chapter of the handbook. For now, complete the templates provided and work to really understand your costs.

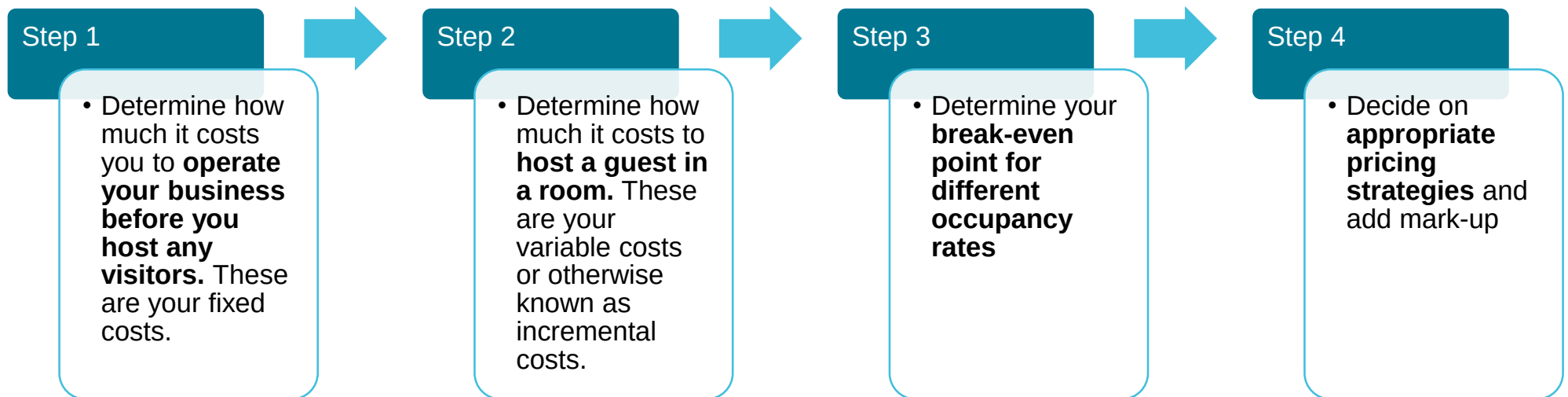
Credit: David Kirkland & SPTO



Being able to demonstrate the above will put you in a strong negotiating position and lower the likelihood of you having to reduce your selling price.

Pricing your accommodation

The process for calculating price is illustrated in the 4 steps shown below. Each step is explained.



*BREAKEVEN is the point of balance between either making a profit or a loss. It is where the cost and the revenue are equal. BUT this is not the final price (as seen by the customer).

A worked example is provided over the next four pages that illustrate the 'cost-plus profit' approach. There are also spreadsheet templates that contain the same examples. It is recommended that you open up the pricing template to view alongside these explanations.

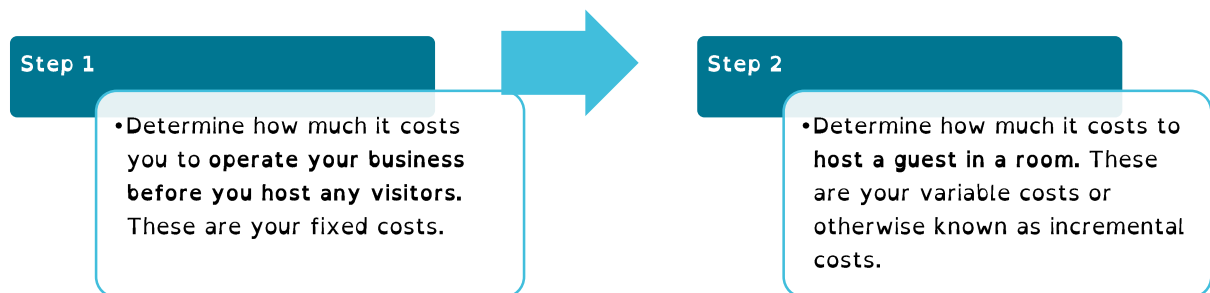


[Tool 4.1](#) Accommodation providers

A worked example is provided over the next four pages. For a template for these steps see [Tool 4.0](#)

Working with an example

The same **basic principles** apply to accommodation as for tours. Firstly, you must cover your costs and ensure you make a profit.



1. Consider your **fixed costs** - those that you must pay whether you sell a room or not. They include:

- Staff salary
- Mortgage or rent
- Insurance
- Internet
- Cable
- Some components of the utilities
- Marketing fees, etc

To do a calculation of your fixed costs, look at your expenses for those categories for the previous year (or month) or for a stable period prior to the pandemic and divide it by the number of room nights sold for the period. This will be an approximation of your fixed costs.

For example: Let us say the fixed costs add up to \$20,000 and the number of room nights sold is 240.

Divide the total cost of expenses by the number of room nights sold: $\$20,000 \div 240 = \83 .

Step 1: Calculate fixed costs	
Your Hotel	\$
Number of guest rooms sold during set period (a)	240
Fixed Costs	\$ Costs for set period
Rent / mortgage	5000
Staff	11000
Insurance	1200
Internet, telephone, cable	1000
Office / reception running costs	500
Marketing / comission fees	900
Any other expenses incurred e.g. one off repairs	400
Total for set period (b)	20000
Fixed cost per room night	83.33

2. You will need to know your **incremental cost** (or variable cost) to put someone in a room. This will be the additional cost that is incurred if you rent a room. Examples of these costs will be:

- Electricity cost (lights, AC, watching TV, etc).
- Water (bathing, washing hands, flushing toilets, etc).
- Housekeeping (the room must be cleaned after the customer leaves).
- Laundry (sheets, towels that were used).

To do a rough calculation of your incremental cost, look at your **expenses for those categories for the previous year (or month) and divide it by the number of room nights sold for the period**. This will be an approximation of your incremental cost for putting someone in a room.

For example:

Your expenses for these categories is \$12,000 last year and you sold 240 room nights. $\$12,000 \div 240$ room nights = \$50 incremental cost (roughly).

Step 2: Calculate incremental costs		
Incremental costs:		\$ Costs for set period
What do guests cost you to stay?		
Electricity (lights, AC, watching TV etc)		7100
Water (showers, sink, toilets)		2000
Wear and tear (e.g. bed mattress, flooring, replacements and repairs)		700
Housekeeping*		1000
Laundry (sheets, towels)		1200
Total for set period (c)		12000
Incremental cost per room night		50

*Housekeeping staff salaries will be partly a fixed cost if they are contracted to work for you, however cleaning products and equipment are incremental.

In this example, your nightly rate must be consistently over the breakeven point \$133 (\$83 + 50) in to make a profit as illustrated on the next page. However, there is an important question to answer - is it better to sell a cheap room than no rooms?

- If someone offers you less than the incremental cost to stay in a room for a night **you will lose money!**
- However, if the incremental cost is covered and there is a contribution towards the fixed costs this is better than an empty room. e.g. \$60 would contribute \$10 towards your fixed costs BUT you would **not make a profit AND you would need to make up the shortfall towards fixed costs at another time by charging a higher price**. This is where it helps to charge different rates at peak times and have special offers to cope with the changes in demand.

Step 3

- Determine your break-even point for different occupancy rates

A further working example:

Assuming total incremental (variable) cost for the period is \$12,000

Assuming total fixed cost for the period is \$20,000

Step 3: Calculate break even points			
total number of room nights	Fixed cost per room night	Incremental cost per room night	Breakeven points
100	200.00	120	320.00
140	142.86	85.71	228.57
200	100.00	60	160.00
240	83.33	50	133.33

The more room nights you sell, the lower your nightly rate needs to be in order to breakeven.

It's also important though to consider occupancy rates when doing this calculation. Assuming 240 room nights represents 80% occupancy, you would need to adjust your figures if you expected a lower occupancy (as in the example above) as the fixed costs would remain the same.

Step 4

•Decide on appropriate pricing strategies and add mark-

You will **up** then need to add your percentage mark-up to the break-even cost to ensure that you **cover your costs and make a profit**. To do this you will need to use an appropriate pricing strategy that best fits your business and product. The illustration below shows the cost-plus pricing method with a 25% profit margin for your business and then an additional mark-up to account for fees or commissions that may be charged for promoting and selling your rooms such as an OTA like Booking.com.

For direct bookings you would not need to add the second mark-up on top of your profit margin. You may also decide to absorb the booking commissions rather than add further mark-up so that you are competitive, especially if it means you overall take more bookings as a result of using global OTAs. There is more on this on the next page.

Step 4: Add mark-ups

total number of room nights (a)	Breakeven point	Your mark-up rate %	Net / wholesale rate	Mark up % for sales channels	Final Price as advertised
100	320.00	25%	400.00	15%	460.00
140	228.57	25%	285.71	15%	328.57
200	160.00	25%	200.00	15%	230.00
240	133.33	25%	166.67	15%	191.67

Pricing strategies:

A pricing strategy is simply the approach that you take to determine your price and this can help to ensure you consider a range of factors as well as your costs.

How much mark-up you add (and consequently your final selling price) will depend on the following additional factors:

- Demand
- Location
- Rating/standard of your facility or offering and value-added (refer back to chapter 2)
- Competition

Value-based strategy: If you have a unique property, or it's in a unique setting, with virtually no competition and your rooms are in demand, you may be able to set a higher room price than competitors.

Competitor based strategy: If your property is similar to others in a resort densely populated with tourist accommodation and there is low demand for rooms, you will need to set your price to remain competitive to attract bookings. It is common practice to combine each of the different pricing strategies as they relate to your business however, **remember it is vital that you always cover your costs and make a profit**.

Accommodation sales channels and costs

Taking Direct bookings

Selling directly to customers may be the most profitable as you will not need to pay a commission to a third party, however you will need significant exposure which can be time consuming and expensive (ways to optimise your online presence are covered in chapter 7) Working with the relevant destination marketing agency / organisation to get featured and promoted through their channels can support your direct sales. You might also want to consider other promotional strategies.



- Offer early booking discount rates.
- Offer seasonal and mid-week rates.
- Offer packages, promotions and extras. For example, pair the accommodation with an add-on such as free breakfast, or capitalize on events/holiday periods, or sell extras such as a shuttle service from the airport.
- Offer discounts for long stays.
- Referrals and return business: encourage customers to share positive feedback on social media to drive more bookings and increase awareness of your business. You can even give guests a promotional code for a discount on a future booking.
- Up-sell: include incentives for upgrading, for example, rooms with balconies, or king size bed.
- Cross-sell: offer discounts on tours after the guest has booked and before they arrive.

Selling through an Online Travel Agent (OTA)

If you are selling through tour operators and/or Online Travel Agents (OTAs) you will need to take their commission into account and sometimes they are very high. (Note that this will be explained in more depth in chapter 5)

The screenshot opposite is from TripAdvisor showing the different rates offered by different OTAs.

OTA	Price
Hotels.com	£65
Expedia.co.uk	£65
Opodo	£89
ebookers.com	£65
Tripadvisor	£65
Booking.com	£89
Snaptravel	£89

Working with Tour Operators

If you are working with tour operators and they are bringing you a significant volume of bookings, they will negotiate hard to get a cheaper room rate. The advantage of this is that it means you have to do less work and spend less on sales and marketing to get bookings. However, **there may be risks** involved. If that operator goes out of business it could have huge repercussions on your business. In 2019 when the British tour operator, Thomas Cook, went out of business, it left many hotels struggling financially.

Payment Conditions

How will payment be made?

It really depends on how many customers you expect to have and the length of the relationship. At the start, your business may be paid cash, but as the relationship strengthens, this will change to bank transfer. Tour operators and ground handlers only do business with companies that have a **bank account** and are fully legitimate.

When?

Different payment terms include:

- **After the product is delivered:** this is the most common agreement and the rule is to pay within a **30-day** period.
- **Before the product is delivered:** this is usually the case with smaller tour operators and ground handlers that specialise in tailor-made holidays.
- On the day the product is delivered: this is very rare.

*Make sure you agree payment terms and conditions **BEFORE** taking any bookings.*

Refunds and Cancellations

As a consequence of the pandemic and the uncertainties around travel, more tour operators are requiring flexible refund policies. **It is recommended that you consult the relevant tourism authority in your country for advice on the approach to take.** It is important to safeguard your business by having a clear refund and cancellation policy that protects you from having to bear the costs of cancelled bookings. The next page sets out important considerations for cancellations.

If working with a tour operator or ground agent, ensure you know how refunds and cancellations are dealt with and put money aside in case there are complaints.



Safeguarding your business in the pandemic

With the current downturn in business caused by the pandemic, it becomes even more important to safeguard your business. Nicole Kow, Marketing Lead at TrekkSoft recommends the following actions:

- Review your cancellation policies. If you do not already have one, it is time to write one. Flexible refund policies have become commonplace during the pandemic. Consider whether a flexible, moderate or rigid cancellation policy is right for your business. This involves thinking about the implications of cancelled bookings e.g., staff and suppliers that require advance notice / payment and what agreements you have with them
- Protect your profits and the long-term endurance of your business. For example, rather than issue a full refund, you could issue a voucher with an extended validity or reschedule the booking/tour to a different date.
- Review the cancellation policies you have with third parties to ensure that it is consistent across your sales channels, including on your own website.
- Adopt strategies to maintain your prices, instead of lowering them. Think about how you can create unique value (covered in Chapter 2) that justifies your price.
- Focus on existing customers who have not cancelled their trips. Consider ways to increase the value of the experience you offer to them. Creating additional options can help to increase revenue and provide tourists with an even more special / immersive experience. Be creative with ideas that allow tourists to get hands-on experiences!
- Create strategic partnerships with other local businesses to develop new products and differentiate your offer to make it more competitive. For example, consider how you might partner with another experience provider to create a package.

For more tips from TrekkSoft, see this article on their website: [Managing cancellations and refunds for tours and activities \(trekksoft.com\)](https://trekksoft.com/blog/managing-cancellations-and-refunds-for-tours-and-activities)ⁱ



Chapter 4: Key Takeaways

Understanding the principles of pricing is essential for the success of your business.

Once you understand the principles (fixed costs, variable costs, carrying capacity, etc) and the factors that can impact these: (location, competition, demand, etc), - you will be able to calculate and set a competitive price that will also enable you to make a profit.

The COVID-19 pandemic is likely to have an impact on pricing.

To comply with Covid-19 protocols, businesses are expected to implement new measures such as smaller group sizes at attractions and for activities, plus reduced numbers at accommodations and restaurants. Understanding how these measures will impact your profitability is key to your pricing strategy. With the uncertainties surrounding travel and likelihood of COVID-19 disrupting their plans, customers will also want to know that they can cancel or make changes to their bookings without penalties. Having flexible cancellation and refund policies will be necessary for businesses to remain competitive and maintain their tour operator and ground handler contracts.

In the next chapter, 'Getting Ready for Business' the roles of different value chain members will be explained and you will understand the various benefits and disadvantages of working with them.



Activity: Working out the costs

Before you are able to negotiate prices with agents, it is important that you have a transparent list of costs. Using the examples and templates provided in the Appendix, work through each of the steps in the pricing model to calculate your prices.

Use the checklist below to track your progress.

Pricing activities	✓
Step 1: Fixed costs are correctly identified.	
Step 2: Variable costs are correctly identified.	
Step 3: The stated carrying capacity is appropriate for health and safety (including COVID-19 considerations), the environment, comfort and enjoyment of customers	
Step 4: Wholesale price has been correctly calculated by identifying the breakeven point and adding your mark up (ie. the price at which you sell to agents).	
Step 5: A price list shows different mark-up amounts that are attractive to agents.	
Step 5: The final price is competitive and represents good value.	
Payment conditions have been fully considered including how to arrange refunds.	

References

· <https://www.treksoft.com/en/blog/managing-cancellations-and-refunds-for-tours-and-activities>