

Pressure-Testing Benchmarks (Whitepaper)

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Introduction

The quality of benchmarking practices in the corporate travel industry still lags behind the professional standards in many other industries. The primary problem is too many benchmark providers and participants still focus more on individual benchmark comparisons than the integrity and value of the process itself. As a travel industry consultant, I'm continuously relying on benchmarks to help clients strategically assess, leverage and manage their corporate travel programs. To offset the quality challenges, my office has begun incorporating the "AAA-Pressure-Test" principle for all benchmark processes. This is the same testing my office uses when helping clients setup reporting processes for their travel programs and it states that all data and/or processes must meet the following three criteria:

Accurate - any information and data that goes into a formula and final reported result must be validated for accuracy.

Actionable - Reported results should answer questions and provide clear direction, versus creating more questions or confusion.

Align-able – Reported or final results must align to an internal department or company project, goal or P&L.

Specific to benchmarking, the application for this pressure test is as follows,

Accurate Test: It is important to validate and then re-validate the accuracy of all collected data and benchmark results. For statistical benchmark results, I apply the *Simpson Paradox* and challenge all reported results from a 360 degree view for accuracy. The Simpson Paradox is based on the theory that numbers don't lie but they can certainly mislead. A good example of the Simpson Paradox is looking at batting averages in the baseball industry. Baseball players are commonly evaluated each season on their annual batting average. Over a two year period of time the seasonal batting averages of two players were tracked for comparison. In each of the two seasons, Player "A" had a higher batting average than Player "B". Relying solely on the standard industry formula (seasonal batting average), most would automatically conclude that Player "A" was the top performer during this two year period. However, if you combine the two seasons into one extended season, the overall performance of the two players was equal.

Category	* Batting Average		# Hits		# At Bats	
	<i>Player "A"</i>	<i>Player "B"</i>	<i>Player "A"</i>	<i>Player "B"</i>	<i>Player "A"</i>	<i>Player "B"</i>
Season One	.311	.306	81	118	260	385
Season Two	.287	.282	106	70	369	248
Combined	.297	.297	187	188	629	633

** Batting Average equals # Hits divided by # At Bats.*

This example is one of many to illustrate how standard, accepted statistics can fool you. Misleading statistics and benchmarks are more common for corporate travel buyers than in other industries due to the number of varying unit factors and because many baseline metrics rely on untested and supplier-centric formulas that have been passed down as accepted standards or best practices. This is especially true for benchmarking or measuring average pricing, discounts, airline market share, etc.

Actionable Test: The determination on whether a benchmark or metric will become actionable is typically performed by a partially biased party leading the project or process. Consequently, everyone thinks their data, metrics and benchmarks are actionable when in fact they're very seldom truly actionable. For benchmark results, there are two tests to determine if they will become actionable. The first is the basic definition of the principle;

“Reported or final results should answer questions and provide clear direction to repeat or improve upon results, versus creating more questions or confusion.”

The second test is to make sure each individual reported benchmark (e.g., metric, statistic, policy, practice or process) includes at least three Performance Measurement Indicators (PMI). A PMI, as referenced in my original whitepaper on benchmarking (“Four Key Practices to Accurate Benchmarking”), is the controlling factor that influences the performance of your benchmark. Factoring PMIs in your benchmark process will help you determine the “how” and “why” of your performance to implement action to repeat or improve upon results.

Align-ability Test: The align-ability test is basically an additional insurance policy for the two tests above (*Accurate and Actionable*). For benchmark practices this involves two tests. The first is the standard definition of the principle;

“Reported or final results must always align to an internal department or Company project, goal or P&L.”

If your benchmark results do not align to one of the above you're probably wasting your time with random benchmarking. The second test is for external benchmarking and is to make sure other companies participating in the benchmark are a good match or aligned with your company. The most common practice is to search out companies with similar size travel volumes or within your respective industry sector. While both match-criteria offer the potential for useful benchmark comparisons, they're as likely to produce misleading or unbalanced results. An alternative and more important match-criteria is to align with companies that have similar expense ratio factors for travel expenses. An expense ratio factor can be determined by dividing your T&E expense by the total company operating expense. The average T&E expense ratio factor for most companies is between 0.5% and 2.0%. I have also witnessed extremes from 0.25% on up to 8%. A small fractional difference in the expense ratio factor can produce misleading or unbalanced results when benchmarking. For example, the difference between an expense ratio factor of 0.50% and 2.0% is not 1.5%, but 4X the value ($4 \times 0.50 = 2.0\%$).

Example

	<u>Total T&E Expense</u>	<u>Total Company Operating Expense</u>	<u>T&E Expense Ratio Factor</u>
Company A:	\$10M	\$1.9B	0.5%
Company B:	\$10M	\$500M	2.0%

At first glance, the companies appear to align because they both spend 10M on travel (Total T&E Expense) and the difference in their expense ratio factor is only 1.5%, which for most analysis is insignificant. However, the real difference is substantial because Company “A” would need to increase its Total T&E Expense to 40M and maintain the same Total Company Operating Expense to obtain a 2% expense ratio. To put this in perspective, the impact or weighted value of the 10M in T&E expenses on Company “B” is four times greater than Company “A”. One should expect different policies and processes (more or less restrictive) and even different pricing and discounts (higher or lower) between the two companies. These two companies are not well aligned for most benchmarking purposes, unless you include the expense ratio factor as a PMI.

The second match criterion is to determine what percentage of the T&E expense is a pass through charge to a customer or other third party. For example, some companies will bill a small or large percent of travel expenses directly to an external customer or other third party. The net cost or impact of T&E expenses at these companies is not the same for companies incurring 100% of the expense. One should expect different policies, practices and even pricing and discounts. Companies with different practices are not well aligned for most benchmarking purposes, unless the criterion is also factored as a PMI.

Summary

As we head out of the recession corporate travel volumes will most likely increase, or at least the patterns will change. The market will also change as travel providers and suppliers introduce new pricing, services and alliances to increase revenue. These changes will render many historical benchmarks and accepted practices obsolete. One of the keys to strategically positioning your company and maximizing the return of your corporate travel program is to invest a little extra time pressure testing benchmarks, projections and other reported results in all projects and processes.

For more information on benchmarking and other innovative ideas to strategically assess, leverage and manage your corporate travel program you can contact Donald L. Swartz, Principal - Corporate Travel Buyer Resources, at 561.694.6743 and dswartz@ctbrtravel.com