

Strategic Analysis of a Port Authority's Cruise Ship Business

by

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PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF
THE REQUIREMENTS FOR THE DEGREE OF

Master Of Business Administration

EMBA Program

in the Faculty

of

Business Administration

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SIMON FRASER UNIVERSITY

Summer 2005

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ABSTRACT

This paper is a strategic analysis of a port authority's cruise ship homeport business and aims to analyse the effect of recent changes in the North American cruise industry on the port authority.

An industry analysis is conducted to identify key success factors to succeed in the cruise ship homeport business and specifically identifies the challenges of competing in a marketplace where the primary motivation to grow the business is based on economic benefit to the local community rather than to the port authority itself. The paper identifies the difficulties of rivalry when it leads to both ports considering expansion when both would be better off not to expand.

A cooperative strategy is explored to determine opportunities and threats for the port authority in relation to management preferences, resource limitations and organizational capabilities. The paper concludes with recommendations on how to proceed with a cooperative strategy to benefit both ports.

DEDICATION

This project is dedicated to my partner Bob, with gratitude for his support, encouragement, and tolerance throughout my course of study.

ACKNOWLEDGEMENTS

I would like thank Dr. Neil Abramson for his guidance and constructive feedback in preparing this paper. In addition, I would like to express my sincere appreciation to my many colleagues who have provided me with much insight into the cruise industry.

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GLOSSARY

Cabotage: The restriction of the operation of sea, air, or other transport services within or into a particular country in favour of host country's own transport services.

Homeport: The port in which a ship or vessel is based. For a cruise ship, it is the port where a vessel is based for a particular itinerary or season. Passengers embark and disembark from this port and it is where the vessel would typically receive its stores, equipment and supplies.

Port of Call: A visit or stop to a port during a cruise ship's voyage where typically the ship will dock and allow passengers to get off the ship – varying between a few hours to a full day.

Revenue Passenger: Most ports measure cruise ship passengers as the number of passengers from which it receives revenue, either during embarkation and debarkation. It is not the number of passengers travelling on the actual cruise ships since they are generally counted twice for revenue purposes.

Shoulder Season: The shoulder season is generally regarded as the few weeks at the beginning and the end of the typical season where vessels when vessels are being repositioned to various worldwide cruise markets. In Vancouver the shoulder season is generally regarded as the months of May and October.

LIST OF ACRONYMS AND ABBREVIATIONS

CAGR: Compound Average Annual Growth Rate

CLIA: Cruise Line Industry Association

CMA: Canada Marine Act

GRT: Gross Registered Tonne

PILT: Payment in Lieu of Taxes

Sea-Tac: Seattle-Tacoma International Airport

TEU: Twenty-Foot Equivalent Unit container

USCBP: U.S Customs and Border Protection Services

VPA: Vancouver Port Authority

YVR: Vancouver International Airport

1 INTRODUCTION

1.1 Purpose of Paper

This paper is a strategic analysis of the Vancouver Port Authority's (VPA) cruise ship business and specifically examines the competition between the ports of Vancouver and Seattle for the Alaska cruise trade. Until the year 2000 the port of Vancouver had a virtual monopoly as the sole homeport for the Alaska cruise business. Since 2002, the port of Vancouver's cruise business has been in decline whereas the port of Seattle has experienced significant growth.

In 2005, Vancouver's four berths and Seattle's three berths will be virtually at capacity on the weekends – the favoured departure days for cruise lines. From an infrastructure utilization perspective it would be beneficial for both port authorities if cruise lines spread their sailings to the weekdays as opposed to adding additional capacity to accommodate weekend demand. However, in a competitive environment, classic game theory would suggest that the situation faced by the two port authorities is akin to a “prisoner's dilemma.” A prisoner's dilemma is a term used in game theory as a situation in which two players each have two options whose outcome depends crucially on the simultaneous choice made by the other (Soanes. & Stevenson, 2003).

The dilemma relates to the decision of the two port authorities to expand or not expand. While both port authorities would be better off by not expanding (forcing cruise lines to take midweek berths), the potential threat of the other port expanding could cause both ports to expand, thus making both ports worse off.

This paper examines the potential for the VPA to implement a new cruise strategy that is based on what Brandenberger and Nalebuff (1996) refer to as *co-opetition* rather than competition with the port of Seattle as a means to sustainably grow the cruise ship industry for both ports and to add to the economic vitality for their communities.

1.2 Port of Vancouver

The port of Vancouver is Canada's gateway to Asia-Pacific, trading \$43 billion in goods with more than 90 trading economies and is the homeport for the Vancouver-Alaska cruise (InterVistas, 2005 p. iii). The port of Vancouver is the largest port in North America in terms of total foreign exports; it is the largest port on the West Coast of North America in terms of total cargo volume; and, is the largest port in Canada both in terms of total cargo handled and total containerized cargo throughput (VPA, March 29, 2004). In 2003, the port of Vancouver was the 43rd largest port in the World, measured in total tonnage (American Association of the Port Authorities, 2005).

The port of Vancouver is one of the world's finest natural, deep-water harbours, covering 233 km of coastline in British Columbia from Roberts Bank at the Canada - U.S. border, along the south shore of Burrard Inlet, Indian Arm and the north shore of Burrard Inlet. In 2004 the port of Vancouver handled 73.9 million tonnes of cargo and 930,000 revenue passengers¹ through its 25 major marine cargo and passenger terminals (VPA, January 18, 2005). By contrast, in 2004 the port of Seattle handled 16.69 million tonnes of cargo and 550,000 revenue passengers (Port of Seattle, 2005b)

¹ The Vancouver Port Authority measures passengers as "revenue passengers" as it derives a separate revenue charge for each passenger that passes through its terminals, either through embarkation or disembarkation. It should not be confused as the number of passengers travelling on the actual cruise ships – they are counted twice for revenue purposes. This is common practice for most cruise ship ports.

The port of Vancouver is a highly diversified port that includes four principal business sectors: bulk (coal, sulphur, potash, agricultural products, petroleum products, and chemicals), break-bulk (forest products and steel), containerized cargoes and cruise ship passengers. Bulk and break-bulk cargoes account for 87 per cent of total cargo throughput; containerized cargoes represent the remaining 13 per cent of cargo throughput, and in 2004 more than 1.66 million TEUs² were handled at the port's three container terminals (VPA, n.d. Statistics).

In addition to its cargo and passenger facilities, the port of Vancouver is home to a variety of marine and port services that support its ability to function as a full service port. These include operations such as customs, pilotage, tugboats, water taxis, ship fuelling and provisioning, ships' garbage/waste removal and disposal, environmental protection/clean-up services, ship building and repair, marine constructors and ship chandlery.

These terminals, facilities and services make the port of Vancouver a major economic generator, both locally and nationally. Across Canada, Port activities generate 30,100 direct jobs, 21,200 indirect jobs, and a further 17,900 induced jobs. In total, the port of Vancouver is responsible for 69,200 jobs and \$1.46 billion in wages. Port activities generate \$1.8 billion in Gross Domestic Product and \$4 billion in economic output (InterVISTAS, 2005a p. iv).

The port of Vancouver is administered by the Vancouver Port Authority (VPA) and is located within eight separate municipalities in the Lower Mainland of British Columbia: the City of Burnaby, the City of North Vancouver, the City of Port Moody, the

² TEU is defined as a Twenty-foot Equivalent Unit. TEU is the common measure of containerized cargo

City of Vancouver, the Corporation of Delta, the District of North Vancouver, and the Village of Belcarra as shown in Figure 1-1 below.

Figure 1-1: VPA Jurisdiction



Source: VPA. Copyright. Used with Permission

1.3 Vancouver Port Authority

The VPA is a non-shareholder for-profit corporation established by the government of Canada in March 1999, pursuant to the Canada Marine Act (CMA), and is accountable to the federal Ministry of Transport (VPA, 2005c). Federal management of

the port of Vancouver has evolved since the establishment of the Port over ninety years ago. In 1913 the Three Harbours Agreement placed the Vancouver Harbour under the authority of a board of three local Harbour Commissioners. In 1936 the Harbour Commission was centralized under the authority of the National Harbours Board in Ottawa, and in 1983 the administration of the federal port system was reorganized once again and decentralized under the Canada Ports Act into seven autonomous local crown corporations, including the Vancouver Port Corporation (VPA, 2005b). In 1998 the CMA was adopted by Parliament to provide further local autonomy by creating a system of 19 Canadian port authorities that are competitive, efficient and commercially oriented.

The VPA operates in accordance with its Letters Patent, which establishes the management, leasing and licensing of federal real property (over 500 hectares of land and 6,000 hectares of water) in Burrard Inlet and at Roberts Bank (VPA, 2005b p.3). The Letters Patent identify the operations and activities permitted by the VPA and its subsidiaries and establish the payment of an annual stipend payable to the federal government based on 2 per cent of its gross revenues. The VPA does not pay federal, provincial, nor local property taxes, however, it is subject to the Payments in Lieu of Taxes Act, 2000 (PILT), which establishes payments to local governments and taxing authorities for federal real property. By statute, the VPA is not eligible for federal funding³ and must remain financially self-sufficient. The VPA's corporate mission, vision, and values are identified in Table 1-1 below.

³ With the exception of funding relating to port security. In 2004 the Canada Marine Act was amended by removing legal impediments to federal contributions for port security funding (Transport Canada, 2004).

Table 1-1: The VPA's Mission, Vision & Values

<i>Mission</i>	<i>Vision</i>	<i>Values</i>
To facilitate and expand the movement of cargo and passengers through the port of Vancouver in the best interests of Canadians.	The port of Vancouver will be the port of choice on the west coast of North America.	<u>Our Commercial Customers:</u> We strive to be our customers' strategic advantage by providing facilities, technologies and services that are competitive, innovative and commercially viable. <u>Our Environment:</u> We operate in a manner that respects and sustains our natural, social and community environments. <u>Our Financial Health:</u> We manage our business to ensure financial self-sufficiency. <u>Our People:</u> We provide a challenging and rewarding work environment for committed and effective people. <u>Our Reputation:</u> We conduct ourselves in a manner that earns trust and respect.

Source: Adapted from VPA, 2005b

The majority of the Port's terminals, industrial and commercial operations are leased by the VPA to third party operators – the most notable exceptions are the Port's cruise ship passenger terminals. While these terminals are operated by the VPA, service contractors provide most terminal services, including stevedoring, maintenance and security.

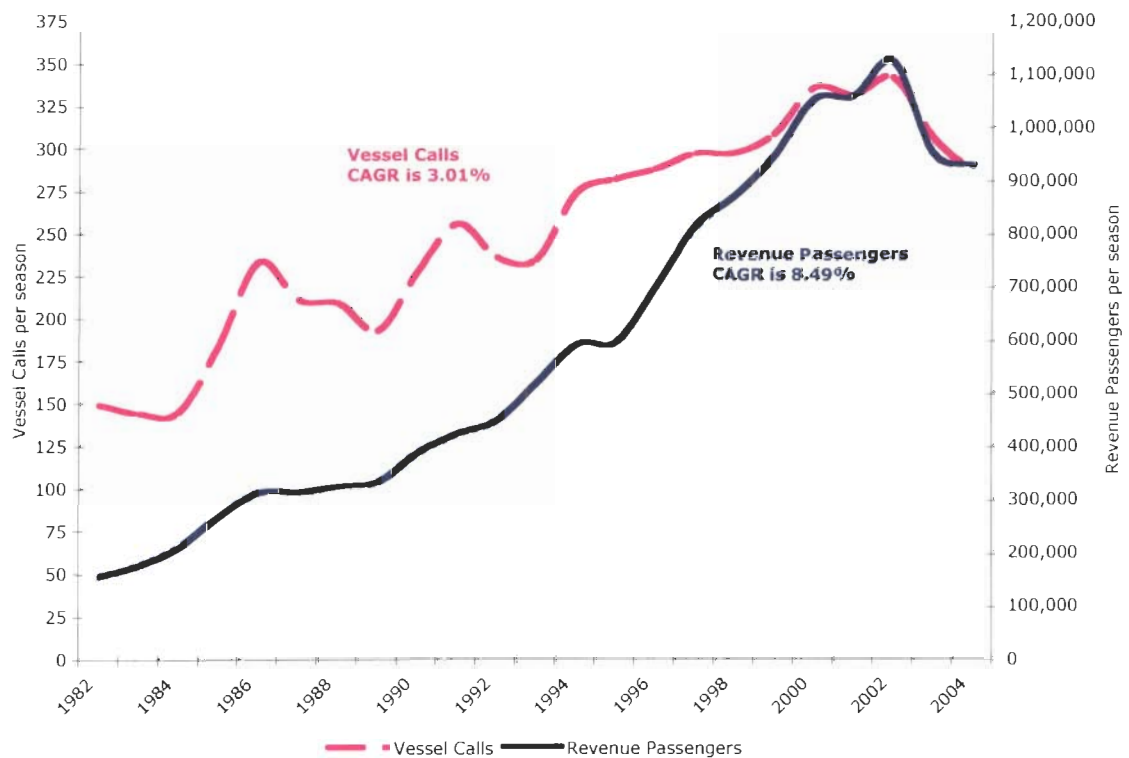
1.4 Port of Vancouver's Cruise Ship Operations

1.4.1 History of Operations

While passenger ships have operated in the Vancouver harbour since the establishment of the Port in early 1900s, modern cruises began operations in 1982 with regular itineraries from Vancouver through the Inside Passage to Alaska. The Alaska cruise market operates in Vancouver during a 5-month cruise season extending from May to September every year.

Between 1982 and 2004, the number of revenue passengers has grown at a compounded average annual rate of 8.49 per cent and the number of vessel calls has grown at a compounded average annual rate of 3.01 per cent. Figure 1-2 below illustrates the changes in revenue passengers and vessel calls in the Port of Vancouver for this period.

Figure 1-2: Port of Vancouver Revenue Passengers and Vessel Calls 1982 - 2004

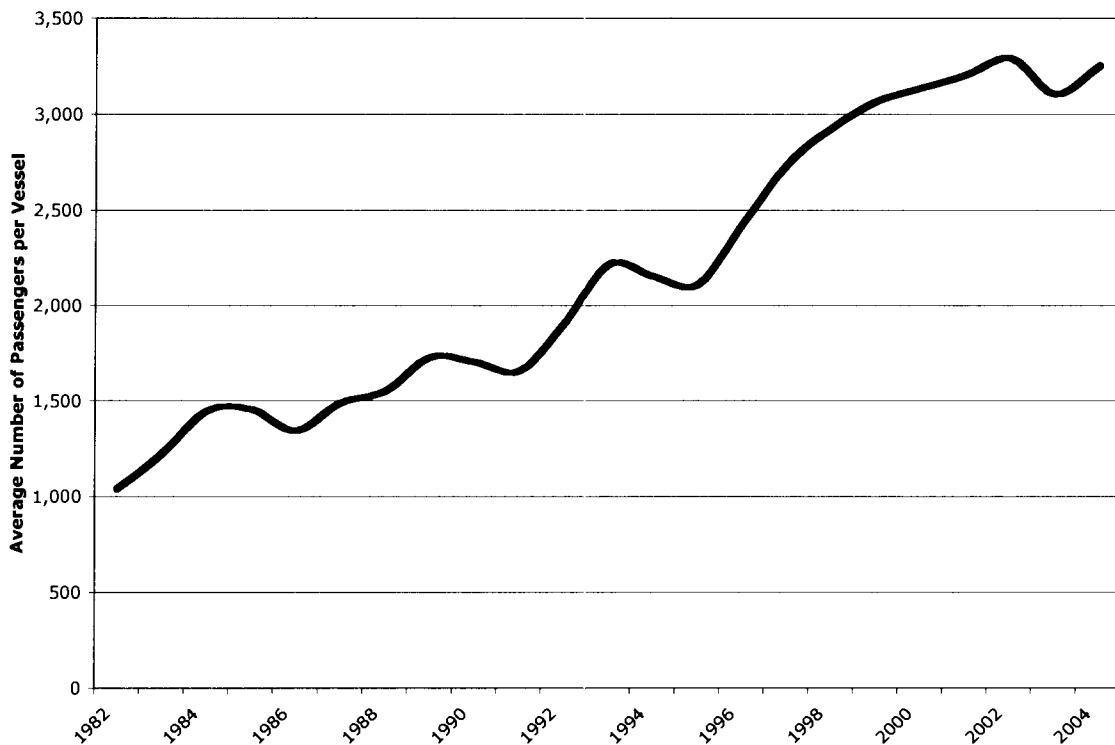


Source: Based on data provided by the VPA with permission.

During the 20-year period between 1982 and 2002, revenue passengers at the Port increased from 155,000 to over 1.1 million for a compounded average growth rate of 10.6 per cent per year for this period (VPA, 2005b p.144). Since 2002 the Port has seen declines in revenue passenger volumes, and expects to experience the third year of decline in 2005 (Harris, 2005).

Vessel calls have also followed the same general growth trend of revenue passengers, however at a much lower rate over the past twenty years due to the increase in cruise ship size and the number of passengers that each ship can accommodate. The growth in the number of revenue passengers per vessel for the period between 1982 and 2004 is shown in Figure 1-3. In 2004 the Port handled approximately 930,000 revenue passengers and 286 vessel calls.

Figure 1-3: Port of Vancouver Average Revenue Passengers per Vessel 1982-2004



Source: Based on data provided by the VPA with permission.

In 1982 the average number of revenue passenger per vessel was approximately 1,000. Cruise ship vessels have grown quite dramatically over the past twenty years such that the average number of revenue passengers per vessel was in excess of 3,200 in 2004.

1.4.2 Terminals and Facilities

The Port has two cruise ship terminals located at Canada Place and Ballantyne terminal, both located on the south shore of Burrard Inlet. The two terminals provide four dedicated berths and one overflow berth that can be used periodically during the cruise season. The two terminal facilities have been developed and expanded at various times over the past twenty years.

As can be seen in Figure 1-4 Canada Place is located in downtown Vancouver. It is the Port's premier cruise ship terminal and twenty years after it was first developed, Canada Place cruise ship terminal still remains one of the most innovative cruise ship terminals in the world given its iconic design, downtown location, and multi-use tourism complex.

Two of the three berths at Canada Place were part of the original 1985 development, which also included a 4-star hotel, offices, retail, convention facilities, and public promenade and plazas. The VPA financed the cruise ship terminal component of this project, which at the time had a capital cost of approximately \$23 million.⁴

Canada Place was originally constructed as a five berth facility, with two berths located on the east and west sides of the pier, and an additional berth at its north end. With the advent of considerably larger cruise ships, the east and west sides of Canada Place were only able to accommodate one vessel each and the north berth became unusable. In 2001, the VPA expanded the cruise ship facilities at Canada Place by adding a third berth, increasing the size of the passenger terminal, ground transportation

⁴ Only includes portion of the development attributed to cruise ship facilities. The government of Canada and private developers financed the remainder of the development. The government of Canada developed the convention facilities and other public facilities as the Canada Pavilion for the 1985 World Exposition.

and loading areas, as well as developed additional space for other uses in the facility for a total capital cost of \$89 million.

Figure 1-4: Canada Place



Source: Vancouver Port Authority. Copyright. Used with permission.

The existing east berth of Canada Place is 506 metres (1,660 feet), the west berth is 329 metres (1070 ft.) long, and the north berth is 274 metres (900 feet). The landside terminal facilities are 17,380 m² (187,077 square feet) in size and can accommodate vessels with combined passenger loads of approximately 6,000 passengers.

The Ballantyne cruise ship terminal is located immediately east of the downtown in the heart of the industrial port as shown in Figure 1-5 below.

Figure 1-5: Ballantyne Terminal



Source: Vancouver Port Authority. Copyright. Used with permission.

In 1995, the VPA undertook a major redevelopment of its secondary cruise ship facility. Ballantyne includes one cruise ship berth as well as an alternate berth that can be used periodically throughout the cruise season. The redevelopment project included the construction of a combined cruise ship and forest products terminal, and the refurbishment of existing berths for a capital cost of approximately \$48 million.

Ballantyne's main (east) berth is 366 m (1,200 feet). The landside terminal facilities are 8,717 m² (93,829 square feet) in size and can comfortably accommodate the largest vessels that call the port.

The VPA has invested over \$150 million (in 2005 dollars) in the development of cruise ship facilities since modern cruise ships began calling in the Port. Table 1-2 summarizes the VPA's investment in cruise ship passenger facilities since 1985.

Table 1-2: VPA Investment in Cruise Ship Facilities

<i>Development</i>	<i>Year constructed</i>	<i>Inflation Since Developed⁵</i>	<i>Cruise Component of Development</i>	<i>Present Value⁶</i>
Original Canada Place	1985	2.69%	\$ 23,000,000	\$39,110,279
Ballantyne Redevelopment	1995	1.96%	\$ 24,000,000	\$29,141,339
Canada Place Expansion	2001	2.18%	\$ 75,000,000	\$81,756,983
Total				\$150,008,601

Source: Based on data provided by the VPA with permission.

1.4.3 Itineraries and Markets

During the 2005 cruise season 30 cruise ships will call Vancouver's two cruise ship terminals (VPA, Vancouver-Alaska Cruise). The principal market served by cruise ships calling the port of Vancouver is Alaska, however other secondary markets are also served during the shoulder season.⁷

⁵ Estimated based on the Bank of Canada's inflation calculator tool at http://www.bankofcanada.ca/en/inflation_calc.htm

⁶ Represents the present value of the original investment in 2005 dollars.

⁷ The shoulder season is generally regarded as the few weeks at the beginning and the end of the typical season where vessels when vessels are being repositioned to various worldwide cruise markets.

There are two typical Alaska cruise itineraries where Vancouver serves as the principal homeport: a seven-day round trip and a seven-day one-way. The round trip cruise embarks and disembarks its voyage in Vancouver and typically travels as far north in Skagway Alaska. The one-way itinerary embarks in either Vancouver or one of the two ports outside Anchorage, Alaska (Seward or Whittier) and travels to the opposite port within seven days. Repositioning cruises occur during the shoulder season (typically May and October) and include a variety of itineraries that vary in duration and ports of call. Some of the typical repositioning cruises include ports of call to and from the California/Mexico Coast and Caribbean markets.

The Pacific Northwest cruise itineraries are shorter in duration (3 or 4 days) and include ports of call in relative close proximity to Vancouver. This itinerary was first introduced in 2000 cruise season and was not continued in 2001 – it is being reintroduced into the 2005 season. The breakdown of Vancouver vessel calls by itinerary is shown in Table 1-3.

Table 1-3: Port of Vancouver Cruise Itineraries

<i>Itinerary</i>	<i>2002</i>		<i>2004</i>	
	Vessel Calls	% of Total	Vessel Calls	% of Total
Alaska Round-Trip	156	46%	126	44%
Alaska One Way	118	35%	105	37%
Alaska In-Transit	14	4%	16	6%
Reposition	26	8%	26	9%
Pacific Northwest 3/4 Day	26	8%	7	2%
Other ⁸	2	1%	6	2%
TOTAL	342	100%	286	100%

Source: Based on data provided by the Vancouver Port Authority with permission

⁸ Includes specialty cruise such as Around the World etc.

1.4.4 Financial Contribution of the Cruise Industry to the VPA

The main sources of revenue the VPA receives from its cruise ship business come from berthage fees, harbour dues, passenger embarkation and disembarkation charges, cruise vessel services and facilities charges. Other sources of revenue include rental from service providers in the cruise terminals (car rental and retail kiosks, etc.).

The passenger fee is the VPA's largest source of revenue from the cruise business. In 2004 total revenues from the cruise business was approximately \$11.8 million. The passenger fee is \$11.00 per passenger for every embarkation or disembarkation. The fee is applicable to every passenger on the vessel whether or not the passenger actually embarks or disembarks. While the fee schedule provides volume discounts to vessels based on the number of passengers, the fee is not differentiated by the day of the week or whether or not the service is a homeport or port of call service.

The CMA requires the VPA to publish a fee tariff for its services and use of its facilities. Published fees for the VPA's cruise business are summarized in Appendix 1 on page 94.

1.4.5 Economic Impact

The economic impact of cruise ship activity in the port of Vancouver has three basic sources: spending by cruise lines and tour operators for supplies, services, fuel, transportation; spending by passengers while in port; and spending by the ship crews while in port.

The Economic Impact Study Update for the port of Vancouver released in 2005 estimates that the Port's cruise ship operations in 2004 generated over 13,000 total jobs

(equivalent to 8,900 person years of employment), paid over \$487 million in wages, added \$567 million to Gross Domestic Product, and produced a total economic output in excess of \$1.3 billion as summarized in Table 1-4 below.

Table 1-4: Port of Vancouver 2004 Cruise Industry Employment and Economic Impacts in Canada

<i>Impact</i>	<i>Jobs</i>	<i>Person Years</i>	<i>Wages</i> <i>(\$ millions)</i>	<i>GDP</i> <i>(\$ millions)</i>	<i>Economic Output</i> <i>(\$ millions)</i>
Direct	3,856	5,584	\$181	\$234	\$566
Indirect	3,896	2,602	\$157	\$200	\$533
Induced	3,742	2,499	\$150	\$133	\$266
Total	13,222	8,957	\$487	\$567	\$1,365

Source: InterVISTAS, 2005. p. 21.

The economic impact study also suggests that in 2004 nearly \$15 million in taxes was paid by cruise passengers, mainly through the goods and service tax and the provincial hotel tax. This represents approximately 2 per cent of the total port of Vancouver tax contributions⁹ (InterVISTAS, 2005 p. 25).

⁹ Includes taxes paid by the VPA, port related employers and employees and cruise passengers.

2 EXTERNAL ANALYSIS

2.1 Industry Analysis

2.1.1 The North American Cruise Industry

The cruise market is strong throughout the world, and especially in North America. Cruise industry analyst Bermello, Ajamil & Partners [Bermello] (2003) attribute the success of the cruise lines to grow this business based on the following four factors: (i) cruise lines have been highly successful in introducing new vessel inventory and developing new products and itineraries that have generated a sustained interest in cruising; (ii) they have created products that have converted land-based resort guests into cruise passengers; (iii) they have consistently delivered a high level of passenger satisfaction; (iv) they have learned to quickly shift their business model to meet changing market conditions, and (v) they have effectively controlled competition, operational costs and generated new revenue sources beyond tickets sales in areas such as on-board spending, shore excursions and landside investments (p. 6).

Modern cruise ships have become an experience in and of themselves. Some ships carry more than 3,000 passengers and include on-board amenities that can include a rock-climbing wall, planetarium, wireless internet access, hydrotherapy pools, yoga instruction, as well as the requisite array of haute cuisine options (Abbot, 2005)

2.1.1.1 Major Cruise Lines

Nineteen major cruise lines are members of the Cruise Line Industry Association (CLIA), which represents 95 per cent of the cruise capacity marketed from North America (Cruise Line Industry Association [CLIA], n.d.). These cruise lines include: Carnival Cruise Lines, Celebrity Cruises, Costa Cruise Lines, Crystal Cruises, Cunard Line, Ltd., Disney Cruise Line, Holland America Line, MSC Italian Cruises, Norwegian Coastal Voyages, Norwegian Cruise Line, Oceania Cruises, Orient Lines Inc., Princess Cruises, Radisson Seven Seas Cruises, Royal Caribbean International, Seabourn Cruise Line, Silver Sea Cruises, Swan Hellenic, and Windstar Cruises (CLIA, 2004 p. 39).

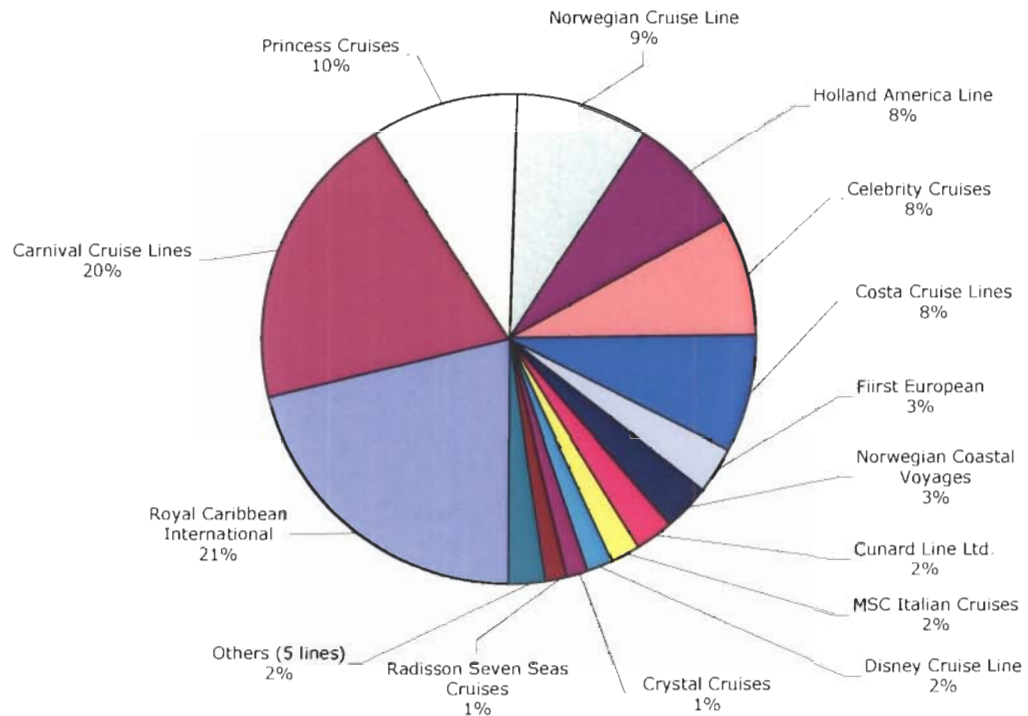
2.1.1.2 Ship Capacity

In 2004, CLIA-represented cruise lines operated 142 ships around the world; and over 50 per cent of their total North American passenger capacity¹⁰ is provided by three cruise lines – Royal Caribbean International, Carnival Cruise Lines, and Princess Cruises, as shown in Figure 2-1 (CLIA, 2004 p. 40). A full list of each cruise line and their respective capacity and number of ships is shown in Appendix 2 on page 95.

Between 1981 and 2003 capacity grew at an average annual rate of 7.9 per cent and is expected to grow at an average annual rate of 4.9 per cent to 2007 (CLIA, 2004 p. 42).

¹⁰ As measured in by the total number of lower berths – the typical measurement of capacity by the cruise industry.

Figure 2-1: North American Cruise Passenger Capacity 2004



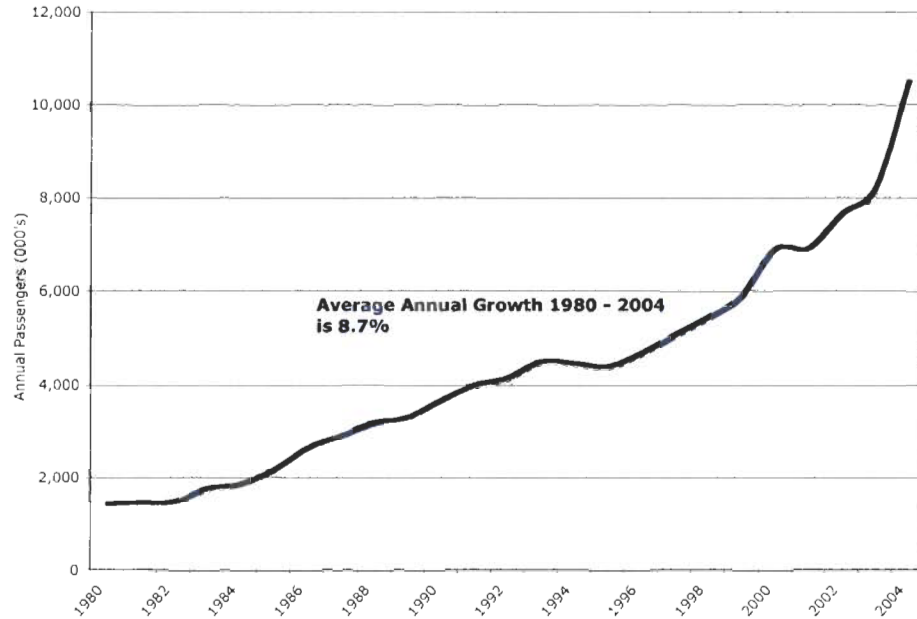
Source: Based on data from CLIA, 2004 p. 39.

2.1.1.3 Passenger Growth

CLIA member cruise lines handled a record 10.5 million passengers in 2004, completing a record-setting, five-year building boom that introduced 62 new ships to North America alone. Cruise passenger growth since 1980 has been an average of 8.7 per cent per year as shown in Figure 2-2.

The majority of the passenger base, and the predominant source of growth over the past few years has been in North America. In 2004, over 84 per cent of the passengers were from North America, and during the past 15 years North American passenger totals have increased on average 8 per cent per year, with 2004 growth estimated at 11 per cent over 2003 levels (CLIA, 2005).

Figure 2-2: Worldwide Cruise Passenger Growth, 1980-2004



Source: Based on data from CLIA, 2004 p. 2 and CLIA, 2005a

CLIA Chairman Andy Stuart attributes the cruise industry’s growth “... to the lines offering tremendous value for the money, cruising’s all-inclusive nature, more close-to-home ports – appealing to the drive market, reducing the need to fly and lower cost; and the industry’s ability to evolve, meeting customers’ needs (Mathisen, 2005 p. 18).”

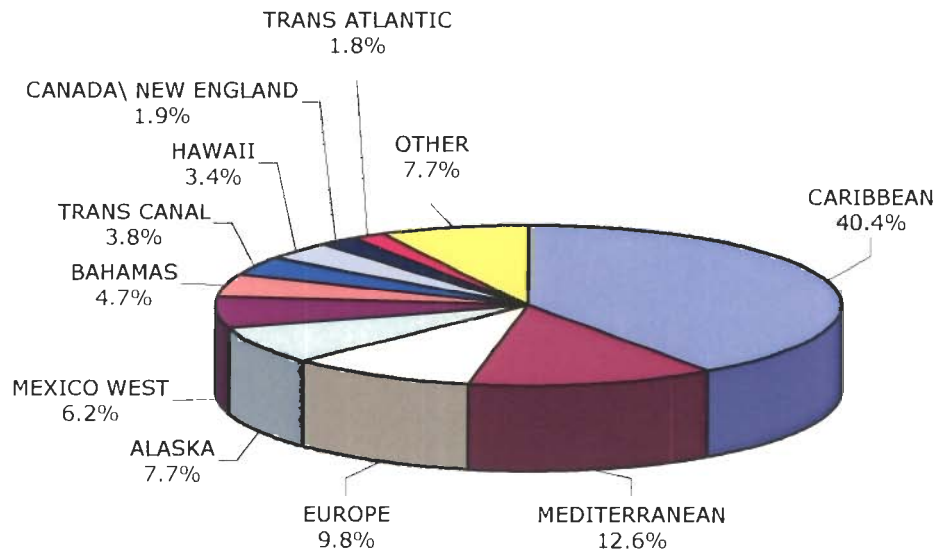
2.1.1.4 Major Cruise Regions

There are twenty-four primary cruise regions in the world. The largest and most established market is the Caribbean area, representing 45.1 per cent of the worldwide market¹¹ in 2004 (comprised of both the Caribbean and Bahamas sub-regions). Other major markets in 2004 include Europe 22.4 per cent, (Europe and Mediterranean sub-regions), Alaska 7.7 per cent, Mexico West Coast 6.2 per cent, Trans-Panama Canal 3.8

¹¹ As represented by the total capacity in each market measured in bed days.

per cent and Hawaii 3.4 per cent (CLIA, 2004). The top ten cruise areas and their share of the market in 2004 is shown in Figure 2-3 below. The detailed capacity for each cruise sub-region for 2000 and 2004 is shown in Appendix 3 on page 96.

Figure 2-3: Top 10 Major Cruise Areas, 2004



Source: Based on data from CLIA, 2004, p. 43

More than 19 ports in North America are used by cruise lines as homeports or embarkation points for various itineraries. The top five cruise ports in North America as measured by the number of embarkations in 2003 were Miami, Port Everglades (Fort Lauderdale), Port Canaveral (Northern Florida, 45 minutes west of Orlando), Vancouver, and New York. The full list of homeports and their respective share of embarkations in 2003 is shown in Table 2-1 below.

Table 2-1: North American Homeport Embarkations, 2003

<i>Port</i>	<i>Embarkations</i>	<i>%</i>
Miami	1,965,000	24.8%
Port Everglades	1,213,000	15.3%
Port Canaveral	1,089,000	13.8%
Vancouver	464,000	5.9%
New York	438,000	5.5%
Tampa	409,000	5.2%
Los Angeles	403,000	5.1%
Galveston	377,000	4.8%
San Juan	325,000	4.1%
New Orleans	288,000	3.6%
Long Beach	272,000	3.4%
Seattle	158,000	2.0%
Seward, Alaska	147,000	1.9%
San Diego	81,000	1.0%
Boston	69,000	0.9%
Baltimore	57,000	0.7%
San Francisco	51,000	0.6%
Philadelphia	24,000	0.3%
Houston	15,000	0.2%
Other North America	75,000	0.9%
Total North America	7,920,000	100.0%

Source: Business Research & Economic Advisors, 2004 p. 8

2.1.1.5 Cruise Market Potential

The cruise market potential in North America remains healthy. In 2004 CLIA commissioned TNS/NFO Plog Research to undertake a cruise market profile to study the size of the cruise market potential in the United States, to investigate consumers' perception of cruising, and to measure cruising intent among key categories of consumers (TNS/NFO Plog Research [TNS], p. 2). The study found that 45 million people have cruised at least once, and of these, almost 23 million have cruised in the past three years (p.6). It concluded that the likely number of people who will take a cruise in the next three years is 29.7 million (p.11).

2.1.1.6 North American Cruise Passenger Profile

The average North American cruise passenger's last cruise was approximately 6.2 days, where he or she spent approximately U.S. \$1,651 per person for the cruise and on-board expenses (not including airfare) and more than half took their first cruise within the past five years (TNS, 2004 p. 14).

The demographic profile of the average cruise passenger is summarized in Table 2-2 below.

Table 2-2: Demographic Profile of Average North American Cruise Passenger

<i>Characteristic</i>	<i>Average Cruise Passenger</i>
Average Age	50 years
Average Household Income	U.S. \$99,000 per year
Gender	
Male	50%
Female	50%
Marital Status	
Married	83%
Divorced/Separated	8%
Single	9%
Employment Status	
Full-time	58%
Retired	19%

Source: Based on data from TNS/NFO Plog Research [TNS], p.16

In terms of the economic profile of potential cruise passengers, the TNS study suggests that of the 29.7 million who will cruise in the next three years, 73 per cent (21.8 million) would be affluent consumers (household incomes in excess of U.S. \$60,000) and 47.5 per cent (14.1 million) would be most affluent consumers (household incomes in excess of U.S. \$80,000) (p. 11).

2.1.1.7 Vessel Characteristics

The evolution of the cruise ship has been one of the key mechanisms driving industry growth. A total of 23 new ships are in contract or planned to be added to the North American fleet before the end of 2009 (“World Orderbook,” 2005). A complete list of the vessels under construction or on order, including the cruise line and vessel size is provided in Appendix 4 on page 97.

The introduction of new cruise ships has required homeports and ports of call to evolve to meet the needs of much larger ships. This provides challenges in terms of accommodating the actual vessel as well as the passenger facilities to handle a larger number of passengers. In 2003, the average length of a cruise ship was approximately 197 metres (648 feet) and had a capacity of 1,090 passengers and was approximately 17 years old. With the retirement of older vessels and the addition of newer vessels, it is likely that over the next decade the average vessel length will be in the 244-metre (800 feet) to 305-metre (1,000 feet) range, with passenger capacities in excess of 1,500. (Bermello, 2003, p. 42). The average size of the 23 cruise ships currently under construction or on order is 101,000 tonnes and is capable of handling 2,628 passengers – these vessels would have lengths in the 290-metre (950 feet) to 335-metre (1,100 feet) range (see Appendix 4 on page 97 for details of the ships under construction or on order).

In addition to the increase in their size, the latest generation of cruise ships are considerably faster than their predecessors. The introduction of gas turbine engines has allowed cruise ships to reach speeds beyond 23 knots which allows ships to not only travel much faster, but it also expands the distance a ship can travel in a typical itinerary.

2.1.1.8 Emergence of the Drive Market

The “drive market” is a common term in the North American cruise industry used to identify markets in close proximity to predominantly U.S. homeports – typically within a 3 to 4 hour drive. While the trend for increased U.S. based drive market operations started in the late 1990s, heightened traveller fears of commercial flights following the terrorism events of September 11, 2001 and the U.S. war with Iraq have further strengthened this market (Bermello, 2003 p. 8).

In 2005, there are more than 30 close-to-home port options for U.S. travellers, especially on the East Coast of North America (Abbott, 2005). The main beneficiaries to the revival of the cruise market on the U.S Atlantic coast for homeport operations include New York (including Brooklyn and Cape Liberty, New Jersey), Boston, Philadelphia, Baltimore and Norfolk, Virginia. Homeports on the U.S Gulf and Pacific Coasts have also seen significant increases in traffic with the emergence of the drive market. The homeports benefiting from this new market include New Orleans, Galveston, Los Angeles (including Long Beach), San Diego, San Francisco and Seattle. In fact, a 2004 survey suggests that seven in ten potential cruise passengers (both previous and intended passengers) indicated that having more cruise embarkation points would increase their likelihood of cruising in the next three years (CLIA, 2004 p. 23).

While security concerns and the hassles of air travel created this market, a side benefit has been the lowering of the total cost of a cruise vacation by eliminating the need to fly. This has had the effect of opening up a larger market for cruise lines in major U.S metropolitan centres. The 2004 passenger survey also suggests that for cruise passengers the largest benefit to having more cruise embarkation points available is the cost savings

and the convenience it provides – in terms of the convenience of driving to the ship and because it eliminates the need and hassle of flying (p. 23).

2.1.2 Cruise Markets in the Pacific Northwest

Cruise markets in the Pacific Northwest are dominated by the Alaska cruise region, which is the fourth largest cruise area in the world. Within this cruise region, there are eight separate itineraries: Inside Passage round-trip, Alaska one-way, Pacific Northwest, British Columbia, Alaska Coastal, Inside Passage Introductory, Alaska Reposition, and Pacific Coastal. Figure 2-4 below shows some of the major homeports and ports of call in the Pacific Northwest.

Figure 2-4: Ports of Call and Homeports in the Pacific Northwest



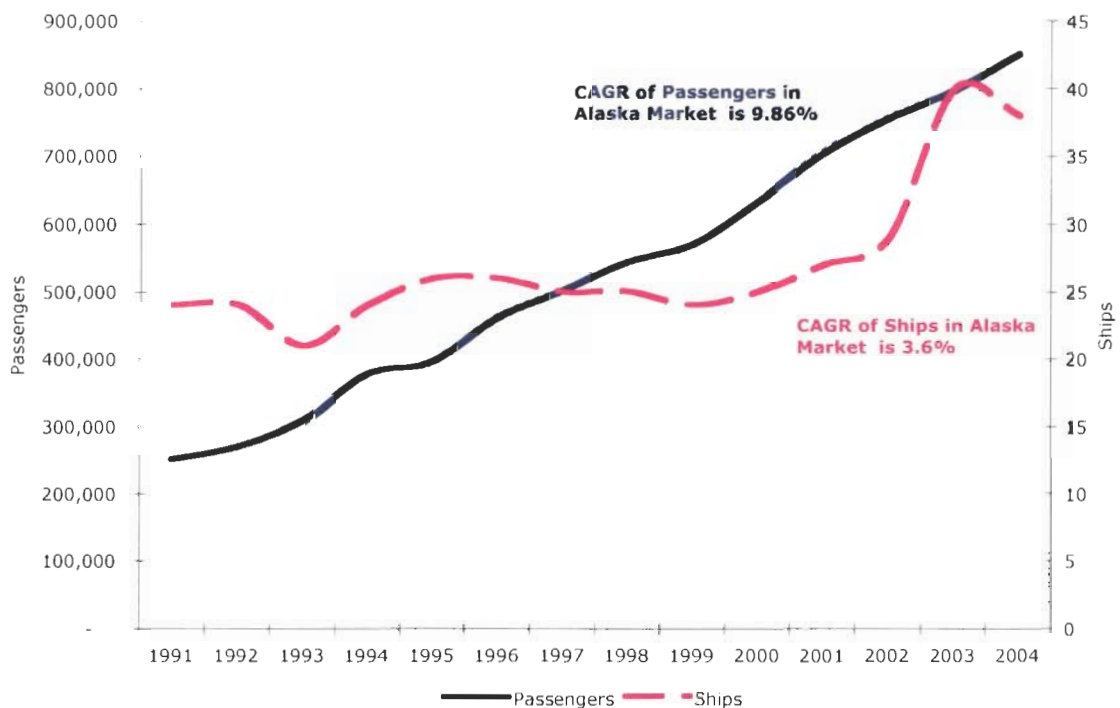
Source: Vancouver Port Authority. Copyright. Used with permission.

The two dominant itineraries include the Inside Passage round-trip and Alaska one-way. Inside Passage cruises are round trip voyages originating in Vancouver or

Seattle, travelling as far north to Skagway, Alaska and returning to the same port. The Alaska one-way itinerary starts either in Vancouver or one of the two ports outside of Anchorage (Seward or Whittier) and travels to the opposite port.

As noted in Figure 2-3 on page 20, the Alaska cruise is the fourth most popular cruise marketed to North Americans with a 7.7 per cent market share in 2004 (CLIA, 2004 p. 43). Alaska remains a very popular cruise with passenger capacity growing at a rate of 9.86 per cent per year since 1991 as shown in Figure 2-5 below. In 2004, thirteen cruise lines served the Alaska market with a total of 38 ships and a passenger capacity of 851,697.

Figure 2-5: Alaska Market Growth 1991-2004



Source: Based on data from "Market Reports," 2004 p. 345.

2.1.2.1 Cruise Ship Facility Owners

In North America, most ports, harbours and coastal waters are controlled by some level of government. As such, cruise ship facilities are typically developed on public lands, and in most cases by some form of government agency. Government agencies vary by jurisdiction, but can include port authorities, local governments, First Nations, or economic development agencies. While most owners of port facilities are locally controlled or sponsored, some ports in Canada are agencies of the federal government – such as the ports of Vancouver and Prince Rupert.

2.1.2.2 Homeports

There are currently five homeports serving cruise itineraries in the Pacific Northwest: Vancouver, Seattle, San Francisco, Whittier, and Seward. These homeports can be both competitive and complementary to each other. For example, the ports of Vancouver and Seattle are competitors for inside passage cruises, and the ports of Whittier and Seward are competitors for one-way cruises. However, Whittier and Seward do not directly compete with Vancouver or Seattle, as they are necessary embarkation or disembarkation points at the opposite end of the one-way itinerary.

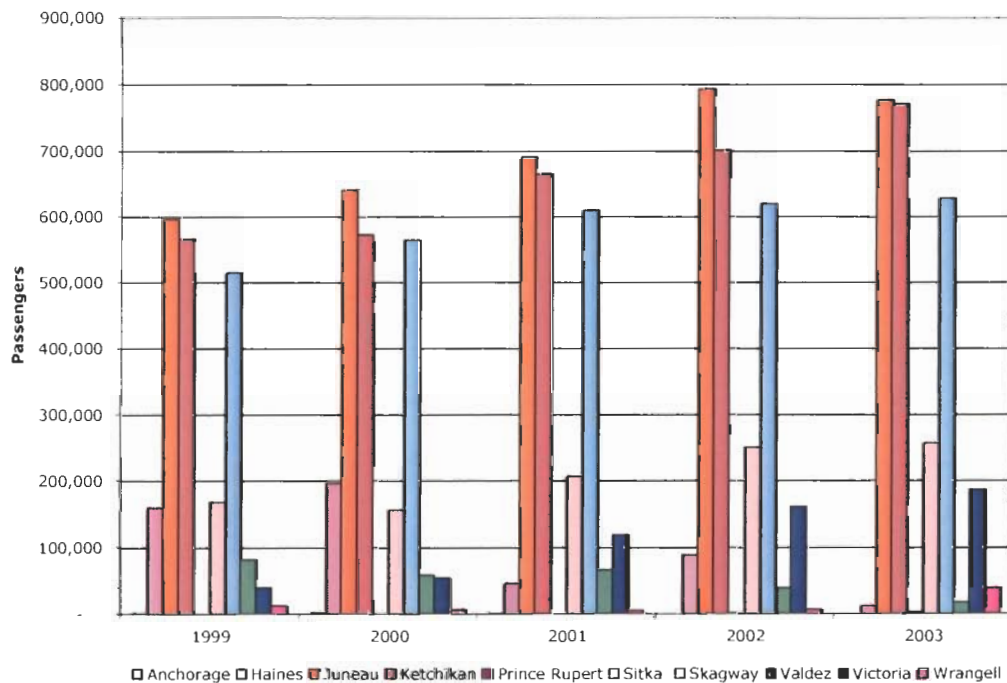
Although San Francisco is also a homeport, it provides a specialized service to Alaska that requires in excess of 14 days sailing. This market is quite limited and not anticipated to grow substantially (Wirtz, personal communication, March 2005). For the purposes of this analysis, San Francisco is considered to be outside of this market and thus a substitute.

2.1.2.3 Ports of Call

In Alaska, three main ports of call capture almost 90 per cent of all cruise traffic: Ketchikan, Juneau, and Skagway. Other ports of call in Alaska include Anchorage, Haines, Sitka, Valdez, and Wrangell. In British Columbia, ports of call include Campbell River, Nanaimo, Prince Rupert, and Victoria. There are other minor ports that may be called on a periodic basis during the regular season or between seasons as part of a ship repositioning. The Port of Vancouver is in a unique position as it can serve both as a homeport and a port of call.

Figure 2-6 below indicates the number of passengers visiting the various ports of call between 1999 and 2003.

Figure 2-6: Pacific Northwest Ports of Call Passengers 1999-2003



Sources: Data provided in "Cruise Ports" 2004 pp. 253-254, supplemented by data provided by Northwest Cruiseship Association, the Victoria Harbour Authority and the Prince Rupert Port Authority.

2.1.2.4 Vancouver-Alaska Cruise Passenger Profile

In 2003, the VPA, the Vancouver International Airport Authority (YVR), Tourism British Columbia, and Tourism Vancouver commissioned Grant Thornton LLP to conduct a detailed survey of passengers sailing on the Vancouver to Alaska cruise. The study found that U.S. residents continue to comprise the majority of cruise passengers (79%), however the number of Canadian residents had increased from 12% in 1999 to 17% in 2003 (p. 47). The study also found that the average length of cruise was 6.9 nights, which is 0.7 days longer than the North American average. In terms of passenger demographics, the study found that the average age of passengers on the Vancouver-Alaska cruise is getting younger. In 1999, the average age of the a cruise passenger was 60; whereas in 2003, it is was 55 – which is still five years older than the average North American cruise passenger (p.48). Women are also more prevalent on the Vancouver-Alaska cruise compared to the North American market as a whole. The demographic profile of the average Vancouver-Alaska cruise passenger is summarized in Table 2-3 below.

Table 2-3: Demographic Profile of Average Vancouver-Alaska Cruise Passenger

<i>Characteristic</i>	<i>Average Cruise Passenger</i>
Average Age	55 years
Average Household Income	56% of U.S. passengers have household incomes in excess of U.S. \$80,000 per year
Gender	
Male	45%
Female	55%
Education	
Undergraduate Degree	23%
Graduate Degree	41%

Source: Based on data from Grant Thornton, p.49

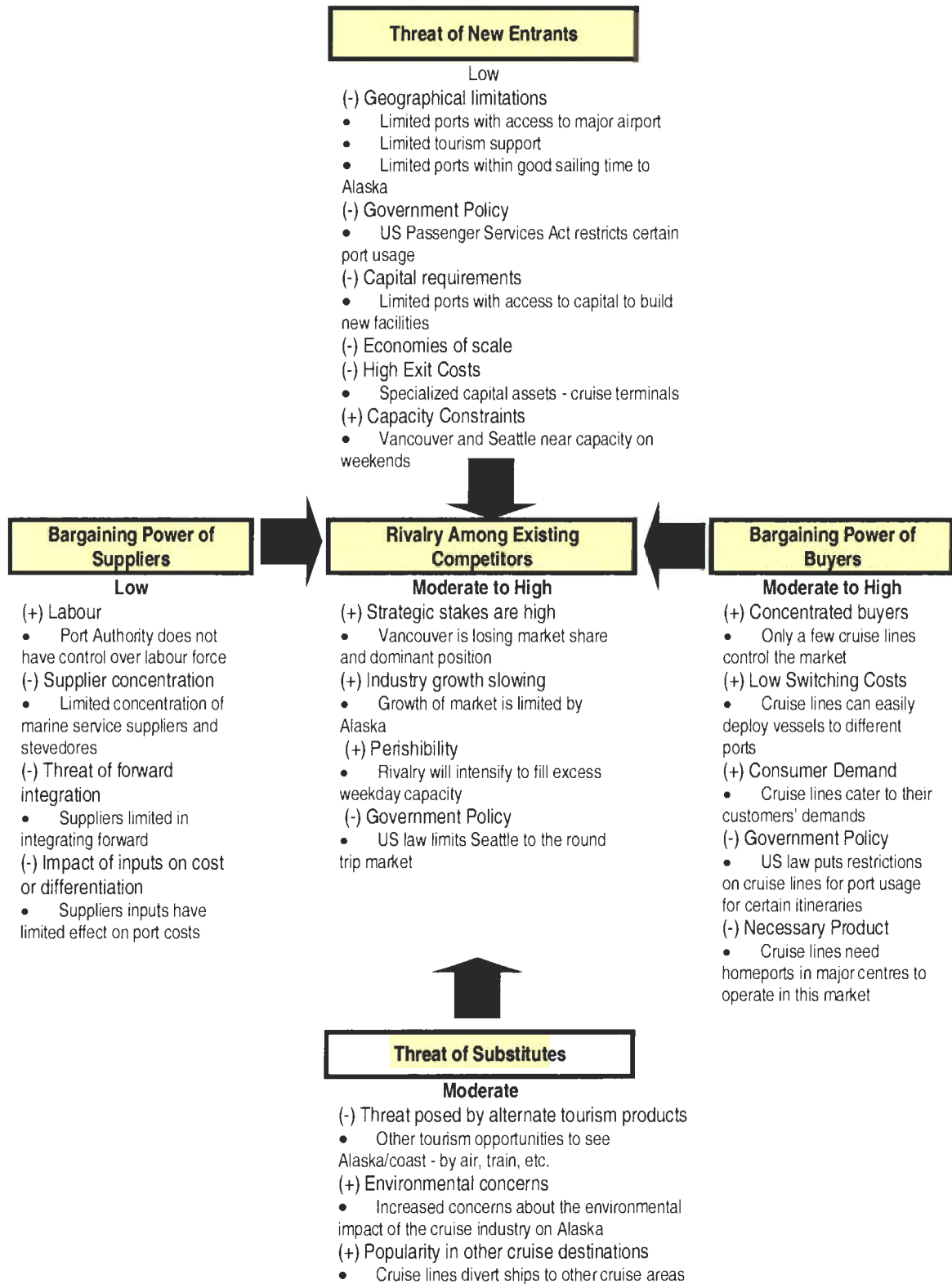
2.1.3 Five Forces Analysis

The competitive environment for the providers of cruise ship facilities in the Pacific Northwest can be examined using Michael Porter's Five Forces Model of Competition (1997). The threat of new entrants, the bargaining power of buyers, the bargaining power of suppliers, the threat of substitutes, and the degree of rivalry among existing competitors comprise Porter's five forces, and is depicted in Figure 2-7. The first four forces are reviewed in detail and a competitive analysis is provided after the industry value chain on page 55.

2.1.3.1 Threat of New Entrants (low)

The economic benefits derived from the cruise ship industry generate significant interest by many port communities in the Pacific Northwest to establish a local cruise ship business. Over the past few years a number of smaller ports, including Victoria, Prince Rupert and Campbell River have entered into the industry as a port of call in the Seattle to Alaska itinerary. While the potential for other ports to enter into the port of call market remains high, this is not the case for the homeport market. The potential for ports to enter into the homeport market remains relatively low for a variety of factors including geographical limitations, the impact of government policy, large capital requirements, and high exit costs.

Figure 2-7: Five-Forces Analysis for Pacific Northwest Cruise Facility Market, 2005



Source: Based on Bukszar, 2005 adapted from Porter, 1997

Geographical Limitations

Geographical limitations are a large impediment to another port considering entry into the homeport market in the Pacific Northwest. Homeports require convenient access to large airports with sufficient airlift capacity and service to major centres in North America. In the Pacific Northwest, this would limit locations to ports in Vancouver,¹² Seattle,¹³ Tacoma, Portland,¹⁴ Anchorage and perhaps Bellingham.¹⁵ Homeporting also is more conducive to ports in cities where there is appropriate tourism infrastructure for pre and post passenger stays.

The location of a homeport is also governed by its proximity to its cruising area. While this does not require a port to be located immediately within the area, McCalla (1998) suggests that homeports need to be intermediate between passenger origins and cruising destinations. As such, for the Alaska cruise market a homeport must be situated to allow a cruise ship sufficient time to sail to the key destinations in Alaska, allow for ports of call along the way, and return within a desired period of time. Until recently, the typical sailing speed of a cruise ship limited the southern extreme of the Alaska cruise itinerary to Vancouver. However, advancements in technology now allow cruise ships to travel much faster – and therefore much further – making it possible to sail from Seattle and reach popular Alaska destinations and return within a week. These geographic considerations continue to limit other major centres such as Portland from establishing themselves as a serious threat of entry into the homeport market in the Pacific Northwest.

¹² Including the Port of Vancouver and the two Fraser River ports (see Figure 1-1 on page 4 for locations)

¹³ Including the Port of Everett

¹⁴ Including the Port of Vancouver, Washington.

¹⁵ While Bellingham only has a regional airport it is in relative close proximity to both SeaTac and Vancouver International airports.

Government Policy

Over forty countries around the world, including the United States and Canada have cabotage laws designed to protect domestic marine shipping industries (Maritime Cabotage Task Force). In the United States, cabotage laws are commonly referred to as the Jones Act, which includes the Passenger Services Act of 1886 that governs domestic passenger trades and limits foreign vessels from transporting passengers between U.S. ports or places. However, the law allows passengers to embark a foreign vessel at one U.S. port and disembark (at the conclusion of the voyage) at the same U.S. port, provided that the vessel makes an intermediate stop at a foreign port (Transportation Institute). While not as restrictive, Canada has similar cabotage laws that restrict foreign vessels from transportation passengers between two Canadian ports.

Since most of the world's major cruise lines are foreign registered vessels, the effect of this law is that cruises departing from a U.S. or Canadian homeport must stop in a foreign port before returning. These laws put limitations on cruise itineraries and thus the combination of ports that can participate in this business.

Capital Requirements

Cruise ship facilities are typically developed by government or government agencies such as a port authority, First Nation, or an economic development agency. Even in those rare cases where a cruise ship facility is developed by the private sector, it usually involves some form of government investment. Decisions to develop cruise ship facilities are typically not justified solely on the basis of financial return, but also on the economic impact it brings to the local community. The capital investment required to develop cruise ship facilities can vary quite significantly depending on site

characteristics, whether or not it is intended to accommodate a port of call or a homeport vessel,¹⁶ and the nature of the development required (i.e. retrofit of an existing marine terminal or new construction). The retrofit of an existing dock intended for a port of call may only cost a few million dollars, while developing a new purpose built homeport facility could cost in the range of \$60 to \$80 million.¹⁷ Given the capital requirements of building new facilities, especially for a homeport, there are a limited number of communities or port authorities in the Pacific Northwest that would have access to the capital required to develop such a facility.

Economies of Scale

In order to participate in the cruise ship facility market, a port must have at least a large marine berth with access to a shore side facility of sufficient capacity for very large cruise ships. While it is possible to use an existing cargo berth on a periodic basis for a port of call, it is more likely that a homeport berth would need to be located in a dedicated facility. As such, in order to participate in the market, a port must enter with the full capacity of a berth – it is generally impossible to bring on incremental capacity when it is required. Therefore, the scale economies required to enter this industry act as a barrier to entry.

High Exit Costs

Related to the scale economies noted above, there are high exit costs to this industry that serve as a barrier to entry, especially for homeport facilities. Cruise ship

¹⁶ Cruise ship terminals intended for homeport activities require much more extensive infrastructure including passenger embarkation and disembarkation areas, baggage handling facilities, storage facilities for equipment and stores, etc.

¹⁷ In 2001 the Vancouver Port Authority completed the expansion of its Canada Place cruise ship terminal. The cruise component of the project cost approximately \$75 million.

facilities are not easily converted to other port facilities (e.g. cargo terminals) without significant cost. In fact, it is very unlikely that unique downtown homeport facilities such as those located in Vancouver and Seattle could be converted into cargo facilities. In addition, because cruise ship terminals are often developed to foster tourism in local communities, there are likely high political costs to exiting this business.

Capacity Constraints

Perhaps the only factor that would suggest that there could be a threat of entry into this market relates to the capacity constraints experienced by existing homeports on the weekends. Cruise ship lines prefer to start and end their voyages around the weekend, and while both Vancouver and Seattle have excess capacity mid week, both are at capacity on the weekend. These capacity constraints forces cruise lines to develop products that depart on other days of the week. However, if there were a weekend berth available, cruise lines would gladly move take a weekend berth over a weekday berth.

Effect on Competitive Rivalry

Despite existing capacity constraints on weekends, various other factors, including a limited number of port cities which have convenient access to an international airport, the effect of cabotage legislation, and the high capital costs of developing a new homeport facility, it would be unlikely for another port to enter into the homeport market. As such, the threat of new entrants into the market would be characterized as low. Accordingly, it would be expected that in markets where there is a low threat of new entrants, and where there are few existing competitors, that this force would have a limited effect on competitive rivalry.

Effect on Industry Success Factors

Analysis of the threat of new entrants in the market suggests that geographic location of the homeport is critically important to its success – whether it is its proximity to an international airport, a location that can draw from a large population base for the drive market, or located within a city that has appeal to the cruise passengers as place to spend a day or two at the beginning of the end of the cruise.

In addition, the ability of a homeport to fund or raise the capital to develop homeport cruise facilities is also critically important to its success in the industry. The cruise business in the Pacific Northwest is generally limited to a 5-month period that favours weekend usage, and as such it is difficult for a port to justify development purely on the basis of financial return. Therefore, it is vital for ports to be able to minimize the cost of development and have access to funding from government or development agencies (for economic development purposes) to defray capital costs.

2.1.3.2 Bargaining Power of Buyers (moderate to high)

The power of buyers is the impact that customers have on a producing industry. The buyers of cruise ship terminal facilities are the cruise lines.

Concentrated Buyers

In the Pacific Northwest there are three major cruise companies operating seven separate brands as highlighted in Table 2-4 below. Almost 83 per cent of the market is controlled by two cruise companies suggesting that these buyers have a significant amount of leverage over the owners of cruise ship terminals.

Table 2-4: Cruise Line Operators in Alaska, 2003

<i>Cruise Company</i>	<i>Brand</i>	<i>No. of Ships</i>	<i>Passenger Capacity</i>	<i>% of Market - Cruise Line</i>	<i>% of Market - Cruise Company</i>
Carnival Corporation	Carnival Cruise Lines	1	39,900	4.7%	
	Holland America Cruise Lines	7	195,894	23.0%	
	Princess Cruises	7	256,690	30.1%	57.8%
Royal Caribbean Cruises Ltd.	Royal Caribbean International	3	113,800	13.4%	
	Celebrity Cruises	3	99,600	11.7%	25.1%
NCL	Norwegian Cruise Line	3	105,200	12.4%	12.4%
Others		14	40,613	4.8%	4.8%
Total		38	851,697	100.0%	100.0%

Source: Data from "Market Reports." 2004 p. 345

Low Switching Costs

Cruise ship lines enjoy a significant amount of power because of their flexibility of moving from port to port without penalty or consequence. For example, in the port of Vancouver cruise lines make their berth requests in April of the preceding season, however only pay for the berth if they use it and are able to cancel the berth request without prior warning or financial consequence of cancelling. This is common practise with most port authorities (G. Wirtz, personal communication, February 10, 2005). It is easier for cruise lines to switch a port of call than it is a homeport, given the necessary supporting services that need to be coordinated at a homeport (i.e. ground transportation, provisioning, airlines etc.). However, given that the major cruise lines have existing operations in both Vancouver and Seattle, switching can be made between the two ports with relative ease.

It is also worth noting that the cruise lines' customers – cruise ship passengers – have even less costs associated with switching between cruise lines for repeat business.

As such, passengers have enormous power over the cruise lines and would exert tremendous pressure on the cruise lines if they do not like a homeport's facilities or location.

Consumer Demand

The consumer's demand for various itineraries and ports of call provides the cruise ship lines with a base of power as the lines try to respond to shifts in consumer preferences. In recent years, consumer demand has shifted towards cruises which are closer to home and do not require air travel. This has been partly in response to the hassles of air travel due to new security requirements and the added convenience of driving to the cruise ship. Heightened security requirements following the events of September 11, 2001 also make the crossing of international borders more inconvenient for travellers. Responding to consumer demands, cruise lines began shifting some of their homeport operations from the port of Vancouver to the port of Seattle. Homeporting in Seattle provides a far greater potential for a drive market as well as eliminating the need to clear border inspection at the airport and cruise terminal. Thus, consumer demand has the effect of increasing the power of the cruise lines over homeports.

Government Policy

The effect of Canadian and American cabotage legislation puts limits on the flexibility of offering certain cruise itineraries. Legislation specifically restricts American homeports to round trip itineraries – and therefore one-way cruises must include a Canadian homeport – which is limited to Vancouver. As such, the impact of

cabotage legislation diminishes some of the power of the cruise lines since they limited alternatives for homeports. This effect tends to moderate the power of the buyers in this market. These cabotage laws also require visits to Canadian ports of call on round trip itineraries.

Necessary Product

A second moderating effect on the cruise lines' power is that in order to operate, cruise lines need to have cruise terminals – both ports of call and homeports. And given the continued attractiveness of this market to the cruise lines, cruise lines must either homeport in Vancouver or Seattle. In addition, they need to have interesting ports of call.

Effect on Competitive Rivalry

While legislative impediments and the fact that cruise terminals are a necessary element of the product offered by cruise lines offset the buyers' bargaining power, it is the limited number of cruise lines and their ease of switching in this market that suggests that the power of buyers would be characterized as moderate to high. The power of the cruise lines, especially in their ability to switch homeports with limited consequence has a tremendous influence on the rivalry between existing homeports in this market.

Effect on Industry Success Factors

Since cruise lines have tremendous control over the homeports, it is critically important for a homeport to have good intelligence about the cruise industry. Cruise ships are highly mobile and cruise lines have shown that they can quickly respond to changes in the marketplace and will move to different ports or itineraries if they so need.

Facility operators need to maintain close contact with the cruise lines and move in lock step with them.

2.1.3.3 Bargaining Power of Suppliers (low)

In order to assess the power of suppliers in the cruise ship facility market in the Pacific Northwest it is important to consider the level of concentration of the suppliers, the control over labour, as well as the impact of inputs on cost or differentiation in the market.

Supplier Concentration

The principal input to the operation of a cruise ship terminal for a port authority (or an owner of a facility) is some form of operational service contractor, which is typically a stevedore company. While service contracts can vary from port to port, as a minimum they include the provision of longshore labour and administration. Other contracted services can include maintenance, security, and ground transportation coordination. In most ports there are at least two or more qualified stevedore companies that are capable of providing these services. While service contracts can differ in their length of time, port authorities will engage in a competitive process to select a suitable supplier. As such, even in those instances where there may be a small number of suppliers, the actual power of the suppliers remains limited in the overall industry.

Labour

While stevedore companies manage the labour force as part of their contract, it is worth noting that longshore labour is highly organized through the International

Longshoreman and Warehouseman's Union (ILWU),¹⁸ which can have tremendous power over the industry in times of labour unrest. The ILWU have a monopoly on labour and there is very little a port authority or operator can do to influence the labour environment.

Impact of Inputs on Cost or Differentiation

While not an actual supplier to cruise terminal operators, it is worth noting the potential effect of local suppliers to the cruise ship lines themselves. Cruise ship lines depend on a range of marine, tourism and hospitality supplies and service while in their homeport. These include bunker fuel, ship supplies, provisions, hotels, airlines and local transportation to name a few. In most ports it can be expected that there would be a range of suppliers to provide these inputs, and thus would limit the power of these suppliers. However, the availability and cost of these supplies as a sum can influence the cost or differentiation strategy of the local port.

Effect on Competitive Rivalry

Supplier power in the cruise ship industry in the Pacific Northwest can be characterized as low given that there are a number of suppliers for both port authorities and the cruise ship lines. Their concentration is limited and therefore have limited ability to significantly influence the industry as a whole and has a minor effect on rivalry.

¹⁸ The ILWU has jurisdiction on the entire west coast of North America. It is divided into separate contracts for Canada and the U.S. and there are typically separate locals in each port.

Effect on Industry Success Factors

Given the limited influence of the power of suppliers in the market, there are no specific success factors emanating from this force for the cruise homeport industry in the Pacific Northwest.

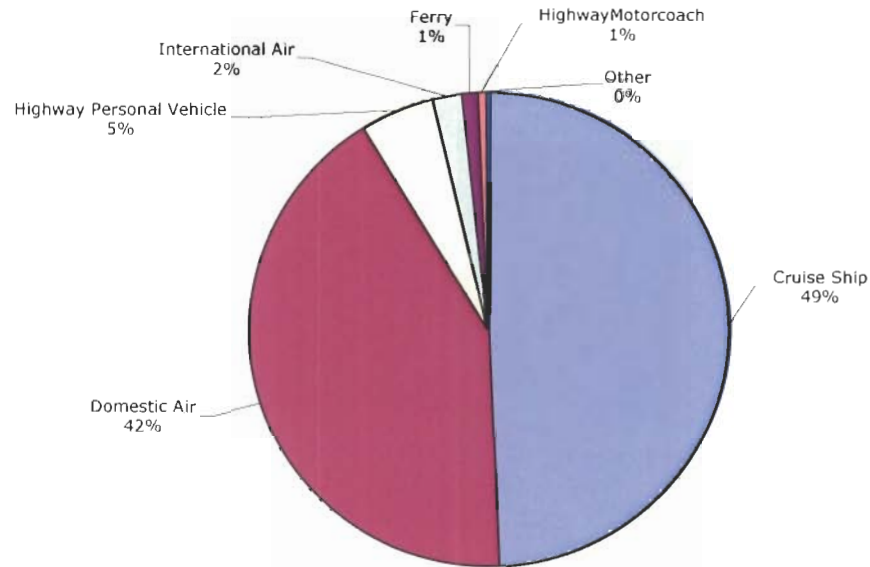
2.1.3.4 Threat of Substitutes (moderate)

Competition arising from a threat of a substitution comes from products outside of a particular industry. For the cruise ship industry in the Pacific Northwest, the threat comes from alternate tourism products, the potential decrease in cruising due to environmental concerns, and the potential competition from other cruise areas.

Alternative Tourism Products

Given that the major destination for cruise ship passengers is Alaska, typical substitutes could include individual driving tours, organized bus tours, air travel packages, adventure tours, and other specialized travel packages (small ship adventure, float plane, etc.). As shown on Figure 2-8 below, cruise ship passengers represented 48 per cent of all visitors to Alaska in the summer of 2004 (Alaska Department of Commerce, Community and Economic Development, 2004). While other forms of tourism offer different travel opportunities to popular Alaskan destinations, few offer a comparable experience to cruising. Cruising is a unique experience that combines the travel experiences from the water aboard a ship that offers a range of recreational amenity (fine dining, entertainment, gaming, etc.).

Figure 2-8: Alaska Visitor Arrivals by Mode of Entry



Source: Adapted from Northern Economics Inc., 2004 p. 9

Environmental Concerns

The cruise industry has continued to be under increased scrutiny for the pollution of waterways and smoke stack emissions in Alaska, British Columbia and Washington State. In the past five years all of the major cruise lines serving Alaska have all paid fines for incidents related to waste disposal or smoke stack emissions (Bermello, 2003 p. 105). While each line has put in place on-board environmental programs to assist in monitoring and preventing these incidents from occurring in the future, there is the potential that on-going environmental concerns could threaten this industry. Many of the smaller Alaskan communities that receive these vessels are becoming increasingly concerned about the impact of cruise ships on their pristine environment and many of these concerns are getting the attention of the mainstream media. While not considered a

significant problem, it is possible that if these concerns persist, it could affect the popularity of cruising in the Pacific Northwest.

Other Cruise Destinations

Another threat of substitution for the cruise industry in the Pacific Northwest is the popularity of other cruise venues around the world. The Pacific Northwest competes with other cruising opportunities during the summer months including Europe, the East Coast of North America, Mexico, and the Caribbean. Despite this competition, the Pacific Northwest – and Alaska in particular is the fourth most popular cruises in the world and it continues to attract the same proportional share of the North American market as the industry grows. In fact, a 2004 survey suggests that interest in an Alaska cruise remains high as it was ranked second behind the Caribbean/Eastern Mexico, as the most appealing place for a next cruise by regular cruisers (TNS, 2004 p. 36). Cruise passenger growth in the Alaska sector is expected to remain relatively healthy expanding to approximately 1.2 million passengers by 2022 (Bermello, 2003 p.111). It is also worth noting, however, that in 2003 only 13% of Alaska cruise passengers had taken a previous Alaska cruise in the past, suggesting that most repeat cruisers like a variety of cruise itineraries (Grant Thornton, 2003 p. 51).

Effect on Competitive Rivalry

The prospects for continued growth in this cruise region should mitigate any threat of substitution, whether it is the potential for tourists to visit Alaska by means other than cruise ship, or Alaska falling out of favour with potential cruise ship passengers. As such, the threat of substitutions is characterized as moderate.

However, while Alaska remains a popular cruise destination, growth in the entire North American cruise market, including Alaska, is projected to slow down from the growth experienced over the past few years. Average annual growth in Alaska cruise ship passengers between 1991 and 2004 was 9.86 per cent; in future years, growth is expected to slow to an average growth rate of less than half (4.5%) to the year 2017 (Bermello, 2003). The slowing of growth in the market should increase rivalry for homeports vying for a share of the business.

Effect on Industry Success Factors

Analysis of the threat of substitutes suggests that is important for homeports to be active participants in the promotion of not only of their port city, but also of the entire cruise area. A 2003 survey of Vancouver cruise passengers indicates that the most important factor in choosing a cruise is the itinerary (schedule, port of call, shore excursions, etc.) and suggests that the location of the homeport is not an important factor (Grant Thornton, 2003 p. 43). Accordingly, it would be beneficial for a port to further influence a passenger's decision to chose a cruise based on the homeport location. Given cruise passengers' preference not to repeat the Alaskan cruise experience more than once, it would be beneficial for a homeport to have a variety of itineraries based out of their facilities in order for the port to participate in more than one cruise market.

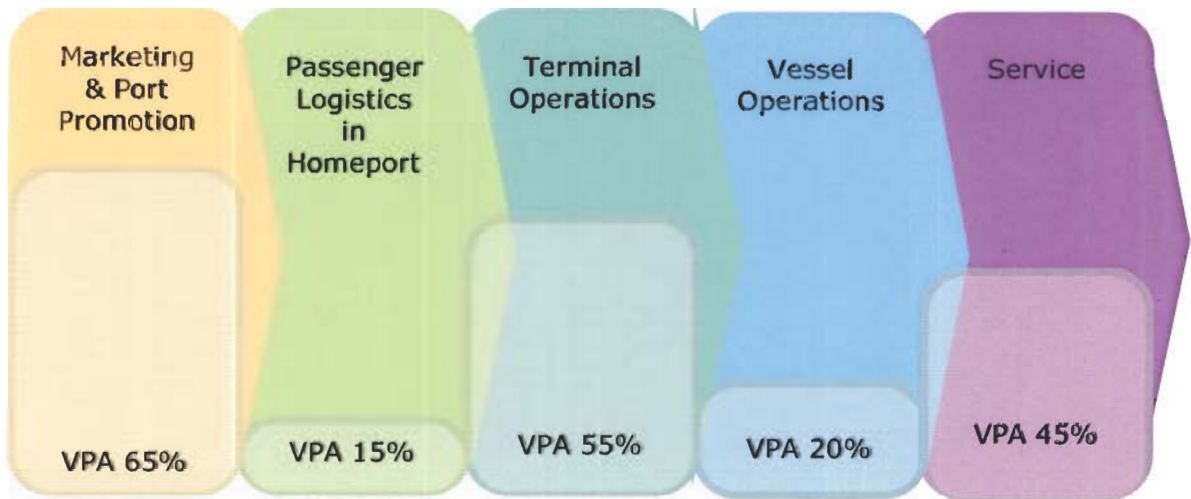
2.2 Industry Value Chain

The provision of a cruise ship homeport includes a variety of service activities directed towards cruise ship lines and their passengers. As such, the value chain for cruise ship homeport activities include the following five functions: marketing and port

promotion, passengers logistics, terminal operations, vessel operations, and service to cruise ship lines, passengers and their intermediaries (e.g. cruise line agents).

To properly understand the VPA’s role in the cruise business it should be recognized that the VPA regards itself as principally a landlord port. Throughout the 1990s the VPA removed itself from the day-to-day operations of most other terminal facilities in the port – long term lease arrangements are now in place for all other operations except cruise. If there were not such a large financial penalty for doing so, the VPA’s preference would be to also lease its cruise terminals.¹⁹ As such, the VPA continues to play an active role in all five of the primary activities identified in the cruise homeport value chain, shown in Figure 2-9 below.

Figure 2-9: Cruise Ship Homeport Services Value Chain



VPA Represents the VPA’s involvement in the Homeport Value Chain

Source: Adapted from Porter, 1985

¹⁹ As a federal organization, the VPA makes *payments in lieu of taxes* (PILT) as opposed to paying property taxes for the properties it is deemed to “occupy.” If a property is leased, the tenant would be required to pay full property taxes -- which is approximately double PILT. Given the low margins in this business and the tax situation in Seattle (the port of Seattle is a taxing authority -- the VPA is a tax payer), the potential benefit of leasing the facility does not justify the added cost.

Of the five functions of a cruise homeport's value chain, it is passenger logistics and terminal operations that are most critical to the success of the homeport.

2.2.1 Marketing & Port Promotion

Like most service-oriented industries, marketing and promotional activities are important to the success of the cruise ship homeport. Marketing of a homeport includes all of the activities to induce the cruise lines to select a particular port as its base. It also includes the broader outreach to the cruise lines' customers – as well as those who influence customer decisions, such as travel agents. Since most port authorities are also attracted to the cruise ship business because of the impact it brings to the local economy, there is also a need to promote the opportunities and benefits of the industry to the local community. There are a number of players who have a role in the marketing and promotion of homeport activities. These include port authorities and/or cruise ship terminal operators, local tourism agencies, support industries, as well as business and industry associations.

The VPA has a fairly large responsibility in the marketing and promotion of the overall cruise ship homeport industry in Vancouver. There are five main activities provided by the VPA's cruise marketing group: (i): ongoing analysis of the cruise business, including forecasting and gathering information about its customers and competitors; (ii) direct marketing to cruise lines, through customer relationship management, participation in industry conferences, and advertising in industry publications etc.; (iii) participation in the promotion of local tourism services to the cruise lines and to travel agents; (iv) provide leadership in developing marketing partnerships

with other ports and tourism agencies; and, (v) by implementing appropriate berth assignment and pricing strategies.

The influence of travel agents is an especially important linkage in cruise industry since approximately 83% of all cruise vacations are booked by travel agents (E. Englezos, personal communication, June 13, 2005). The VPA is involved in a number of marketing efforts with the travel trade, including the distribution of promotional materials, maintenance of website geared to travel agents, sponsorship of *Cruise-a-thon* - a biannual conference in Vancouver for travel agents, as well as participation in cruise *Fams*, which are familiarization tours put on by the cruise lines for top selling travel agents.

A major marketing initiative of the VPA includes its involvement in Cruise BC. Cruise BC is an association of ports, destination marketing agencies and government formed in 2003. Its purpose is to provide a forum for its members to work together, and to work collaboratively with cruise lines, to strategically develop the potential that exists to make Canada's Inside Passage and BC's port cities world class cruise destinations (Cruise BC). Members of Cruise BC include: Campbell River Port of Call, Government of Canada, Greater Victoria Harbour Authority, Nanaimo Port Authority, Port Alberni Port Authority, Prince Rupert Port Authority, Province of British Columbia, Tourism BC, Tourism Vancouver, Tourism Victoria, and the VPA.

Effect on Industry Success Factors

As noted in section 2.1.3.4 above (Threat of Substitutes), promotional and marketing activities are one of the key factors of success for a cruise ship homeport. The importance of these activities relates to marketing efforts aimed at the cruise line as well

as travel agents and potential passengers. While it is relatively easy for homeports to focus marketing efforts on the cruise lines, it is much more difficult and costly to focus efforts on passengers, and as such are often undertaken in conjunction with tourism agencies.

In addition, as noted in section 2.1.3.2 (Bargaining Position of Buyers) it is important for homeports to have good intelligence about the trends effecting the cruise industry and the cruise lines in specific, and as such forecasting and information gathering as part of the marketing effort is paramount.

2.2.2 Passenger Logistics

Passenger logistics in the cruise ship homeport industry include a range of services and activities involving the transfer of passengers to and from their home to the cruise ship terminal. The players involved in these functions include airlines, airport authorities, customs and immigration (Canadian and U.S.), ground transportation providers (buses, taxis, rental car agencies, etc.), cruise lines, cruise line agents, port authorities, and terminal operators.

Port authorities and/or terminal operators have a relatively minor function in facilitating the movement of the passenger to and from the terminal. Their primary role is to coordinate ground transportation functions in and out of the actual cruise ship terminal.

The VPA's role in passenger logistics to and from the cruise ship terminal relates primarily to ground transportation coordination at the terminal. During the cruise season the VPA hires summer students who act as traffic attendants and are responsible for

directing traffic in and out of the terminal. The VPA is also involved in coordinating communication between the various parties who need to gain access to the terminals.

Effect on Industry Success Factors

Streamlined and efficient passenger logistics has become one of the most important factors for successful homeport operations. As noted in section 2.1.3.1 (Threat of New Entrants), homeports must be located where there is convenient access to an international airport that has sufficient airlift capacity and service to major centres in North America. Passengers want to minimize the time it takes to get on to the cruise ship – including direct flights to the homeport city and streamlined processing (security, customs, immigration, etc.) at the airport. And while port authorities typically have a minor role in these functions, their ability to influence or improve these functions can directly influence their success as a homeport.

2.2.3 Terminal Operations

Terminal operations include all of the activities relating to the shore side component of the cruise ship terminal. These include property management and maintenance of physical infrastructure; the processing of vehicles, passengers, baggage, and stores; regulatory operations, including passenger security clearance, customs and immigration; and, the provision of complementary goods and services for passengers and crew (e.g. food and beverage, car rental). There are many players involved in operations at the terminal, including port authorities and/or terminal operators, cruise ship lines and/or their agents, government agencies, stevedore companies, transportation providers, third party service providers and vendors.

The VPA is directly responsible for over half of the activities involved in the operation of its cruise ship terminals, including those that it directly operates and those, which it outsources, or contracts to others.

The largest component of the VPA's cruise business value chain is in terminal operations. These activities include: operations management, terminal maintenance, terminal security, retail leasing and management, stevedoring, janitorial and passenger and baggage screening. Many of the key terminal operation functions such as stevedoring, passenger and baggage screening and security have already been outsourced to organizations that have expertise in these areas.

While the port of Seattle has not moved to the extent of leasing its cruise ship terminals, it has managed to outsource all of the terminal operation functions to a stevedore contractor. The VPA realizes that while it continues to operate its cruise ships facilities, the organization's ability to focus on those areas where it adds greater value is diluted and becomes less strategic. To this end, the VPA is currently identifying additional functions that can be outsourced without jeopardizing its tax status.

Effect on Industry Success Factors

Terminal operations are a core function of a homeport, and the degree terminal operations can be done smoothly and efficiently, the more positive the experience for the cruise line and their passengers. What cruise lines value today is not the same as what they valued a few years ago. A few years ago, cruise lines favoured the marketing appeal of modern downtown terminals; however, today they prefer terminals that have convenient access to airports, good signage, large parking lots, and comfortable and easy passenger processing areas. They no longer look at the terminal as an important part of

the cruise experience – terminals do not need to be fancy to be favoured by cruise lines (G. Wirtz, personal communication, May 13, 2005). And since convenience has become so important to the cruise lines' customers, it is also important to have quick and efficient processing for both terminal security and custom and immigration functions.

2.2.4 Vessel Operations

Vessel operations for homeport activities include all of those activities relating to safely bringing the cruise ship into the port, as well as the servicing of the vessel to prepare it for the next voyage. Services and activities relating to bringing the vessel into port include pilotage, environmental and safety inspection, and vessel traffic management. Vessel operations while at berth include vessel maintenance and minor repair, bunkering, and servicing functions such as garbage and waste disposal, loading of provisions, etc. Organizations involved in these activities include port authorities, cruise ship lines and their agents, regulatory agencies, oil refineries, and marine service providers.

The role of the VPA in vessel operations is fairly minor in comparison to other organizations; however, it includes ensuring safe operations in the harbour, the provision of routine regulatory inspections, and the management of vessel traffic.

Effect on Industry Success Factors

Vessel operations are fairly standard in most homeports, and as such there are no specific success factors emanating from this component of the cruise ship homeport services value chain.

2.2.5 Service

Service activities for a cruise ship homeport include a variety of services to the cruise lines, passengers, and the coordination of the various service providers and other participants in the industry. This also includes creating an enjoyable experience for passengers from point of origin to boarding the cruise ship. These services are provided by all of the players in the logistic chain (airlines, airports, ground transportation providers, port authorities), terminal and vessel services, and various tourism support in the host community

The VPA plays a fairly important role in the service that is provided to the cruise lines and the experience provided to their passengers. The types of service provided include general customer service to the cruise lines and their agents, regulatory facilitation, stakeholder coordination, and providing an enjoyable terminal experience for passengers.

One of the VPA's key strengths in its cruise business is providing leadership in bringing the various cruise stakeholders together to solve joint problems and to facilitate communication for collective action, especially in relation to operational issues.

Effect on Industry Success Factors

While not as critical as passenger logistics and terminal operations, homeports can derive significant value for the service component of the value chain – especially if the service relates to improving efficiencies or making the homeport experience more enjoyable for the cruise ship passenger. Port authorities can do this by facilitating process improvements, and the degree to which they are able to do so can directly impact its success as a homeport.

For example, in April 2005, the VPA announced a program it established with the YVR, in cooperation with Canadian and U.S. border services to streamline passenger processing and improve transit times through Vancouver. The program, called “U.S. Direct,” allows passengers arriving at YVR to transfer directly to a same-day departing cruise without clearing customs. The program also works in reverse when passengers are departing Vancouver (Simpson, 2005). Providing these and other similar services to the industry help to ameliorate the natural or legislative disadvantages of a homeport location and can help temper cruise lines customer power in the industry.

2.3 Industry Assessment

From the analysis undertaken in sections 2.1.2.4 (Five Force Analysis) and 2.2 (Industry Value Chain), there are six key factors that are important to the success of operating cruise ship homeport facilities in the Pacific Northwest. These include:

1. *Geographic Location*: including the proximity to an international airport, a location that can draw from a large population base for the drive market, or a location within a city that has marquee value to the cruise passengers as place to spend a day or two at the beginning or end of the cruise.
2. *Passenger Convenience*: providing streamlined and efficient passenger movements from place of departure to vessel embarkation – including convenient air access into the homeport city, customs clearance, and terminal security.

3. *Efficient Terminals*: providing cruise ship terminals that can efficiently handle the latest generation of cruise ships and the associated volume of passengers in a secure environment.
4. *Ability to Fund Terminal Development*: ability to minimize the cost of facility development and/or access to funding from government or development agencies to defray capital costs.
5. *Market Intelligence*: understanding the dynamics of the cruise ship industry so that the homeport can respond swiftly to the needs of their cruise line customers.
6. *Influence Passenger Decisions*: actively participating in the marketing of the homeport city to try to influence the passenger's decision about their choice of homeport.

2.4 Competitive Analysis

This competitive analysis of the cruise ship homeporting industry in the Pacific Northwest is a duopolistic analysis of the ports of Vancouver and Seattle.

2.4.1 Port of Seattle

The port of Seattle was established in 1911 and was the first autonomous municipal corporation in the United States specifically tasked to develop harbour and port facilities to encourage commerce (Port of Seattle, 2004a p. I-1). In 2003, the port of Seattle was the 10th largest port in the United States measured in terms of total cargo value (American Association of Port Authorities, 2005).

The port of Seattle is a port district with five commissioners elected at large by the voters of King County. It operates the Seattle-Tacoma International Airport, provides freight and passenger terminals, acquires and improves lands for sale or lease for industrial or commercial purposes, and creates industrial development districts (Port of Seattle, 2004a p. I-1). Seaport facilities are located in Elliot Bay and include more than 607 hectares (1,500 acres) for containers, general cargo and break bulk cargo, fishing support facilities, cruise ship facilities, conference facilities, office buildings and industrial property.

The port of Seattle's 2005 Business Plan identifies the mission of its cargo and cruise services sector as follows,

Provide cargo facilities, equipment and services to encourage current and new customers to move greater amounts of cargo through the Port of Seattle, and accommodate the efficient movement of containerized and other forms of cargo through the Port of Seattle. Provide cruise ship services and facilities that maintain and grow the cruise business in the Seattle area. All of these services will enhance the economy of the region and provide a reasonable rate of return to the Port of Seattle and the citizens of King County (Port of Seattle 2004a p VI-5).

The port of Seattle is a taxing authority. For 2005, it proposes to collect a total of U.S. \$62.7 million from the property tax payers of King County. By statute, the Port is permitted to levy up to U.S. \$0.45²⁰ per U.S. \$1,000 of assessed land value for general port purposes (Port of Seattle, 2004a p. IV-1). While the levy, by statute, maybe used for general port purposes, port of Seattle policy sets out that the levy is to be used to fund capital investments – the fund has traditionally not been used to fund airport projects (p. IV-5).

²⁰ While the port of Seattle is permitted to levy up to U.S. \$0.45, it rarely levies the maximum amount. The proposed levy for 2005 is U.S. \$0.2539 (Port of Seattle, 2004 p. IV-1).

2.4.1.1 Port of Seattle's Cruise Business

The port of Seattle is strategically located at the southern end of the Alaska cruise region and has seen tremendous success in developing its cruise business over the past few years. However, it has taken many years of marketing its facilities before cruise lines began homeport operations in Seattle. The port of Seattle's interest in developing a cruise ship business began in the early 1980s when it developed a mixed-use project in its downtown waterfront at Pier 66 (also known as Bell Street Pier). The development included a cruise ship terminal, conference facilities, maritime museum and other commercial uses. The cruise facility was left largely vacant for many years as the Port was unable to attract cruise lines to the facility – cruise lines continued to favour Vancouver as the homeport for its Alaska business.

Industry analysts Bermello, Ajamil & Associates (2003) attribute the cruise lines preference for the port of Vancouver during this time for the following reasons: (i) shorter sailing distances to Alaskan ports; (ii) the high calibre of tourist facilities in Vancouver; (iii) reasonable facility and labour costs; and, (iv) multiple cruise facility and berthing options (p. 56).

The port of Seattle's breakthrough came in 1998 when the Port was able to secure a long-term agreement with NCL for homeport services for one of its vessels deployed in the Alaska market. Some of the reasons why NCL selected Seattle included a shortage of weekend berth capacity in Vancouver, its desire to differentiate its product from other larger cruise lines (such as Holland America, Princess Cruises and Royal Caribbean International which had homeport operations in Vancouver), it wanted to begin to exploit the new emerging drive market, and to take advantage of favourable airfare costs through

Seattle's airport (Bermello, 2003 p. 57). The success of its new venture with NCL prompted the Port to convert an underutilized container terminal south of the downtown, known as Terminal 30, into a two berth cruise terminal in 2003.

The port of Seattle's cruise business has grown from just over 100,000 passengers in 2000 to 560,000 passengers in 2004 (versus the port of Vancouver's 930,000 passengers). In 2004, it experienced an increase of 62 per cent from 2003 levels. Correspondingly, ship calls grew from 99 in 2003 to 150 in 2004 (versus the port of Vancouver's 286 vessel calls), and Seattle became the market leader in Inside Passage (round trip) cruises to Alaska (Port of Seattle, 2004).

The port of Seattle takes pride in the economic benefits that the cruise industry brings to its community. The Port estimates that in 2004 the cruise industry generated 1,732 local jobs with a payroll of U.S. \$59 million, and that the industry was responsible for U.S. \$208 million in local business revenue and U.S. \$5.8 million in state and local tax revenue. The Port also estimates that visitors spend U.S. \$3.7 billion in Seattle and King County annually, contributing more than U.S. \$300 million in state and local tax revenues (Port of Seattle, 2005).

2.4.1.2 Seattle's Cruise Terminals

The port of Seattle has two cruise ship terminals: Pier 66 and Terminal 30. Pier 66 has one berth of 472 metres (1,550 feet) and a passenger terminal area of 6,300 m² (68,000 square feet),²¹ and is located in downtown Seattle as shown in Figure 2-10 below. Terminal 30 has two berths, each approximately 305 metres (1,000 feet) in length and a terminal area of 8,825 m² (95,000 square feet), and is located south of the

²¹ The terminal area was almost doubled from the size of its original development.

downtown in the industrial port as shown in Figure 2-11. Terminal 30 was an underutilized container terminal that was converted to a cruise ship terminal by adding prefabricated passenger terminal buildings adjacent to the existing cargo wharves. While the terminal facilities would be considered modest from a passenger amenity perspective, the terminal site is large with ample parking, and convenient access to the regional freeway system.

Figure 2-10: Port of Seattle's Pier 66 Cruise Ship Terminal



Source: Courtesy of port of Seattle.

2.4.1.3 Port of Seattle's Cruise Strategy

As a public agency, the port of Seattle's Commission meetings and proceedings are publicly available, including the Port's 2005 Budget, Business Plan and Draft Plan of

Finance, approved by the Commission in December 2004. The business plan identifies the Port's cruise strategy as follows,

For the cruise business, our strategy is to market Seattle as a homeport and a port of call to cruise lines serving Alaska and the Pacific Northwest. Through doing this, we will increase cruise passenger volumes and ship calls. We also create value for our customers by making our cruise terminals efficient and cost effective (Port of Seattle, 2004a p. VI-5).

Figure 2-11: Port of Seattle's Terminal 30 Cruise Ship Terminal



Source: Courtesy of port of Seattle.

The plan sets out 2005 business goals and objectives for a variety of the Port's business sectors including cruise. The Port has a target net operating income (NOI) before depreciation for its cruise business of U.S. \$900,000 and an objective to increase cruise passengers by 40 per cent. (p. III-3). The business plan also suggests that a decision for a fourth berth should be made in 2005 (p. VI-7)

For the 2005 cruise season, the Port of Seattle anticipates 14 different vessels will make a record 169 stops in Seattle, with a revenue passenger count reaching an all-time high of 685,000 – an increase of 22 per cent from 2004 levels (Port of Seattle, 2005b). By comparison, the VPA anticipates handling 286 vessel calls and 929,000 revenue passengers in 2005 – a slight decrease of 0.1 per cent from 2004.

2.4.2 Characterization of Rivalry

As noted earlier in this paper, port authorities and other owners of cruise ship facilities do not justify terminal development purely on the basis of financial return. The cruise ship season in the Pacific Northwest lasts only five months a year and in most cases cruise facilities are very expensive to build relative to the amount of revenue that is generated. As such, a large attraction to this industry is the economic benefits that it brings to local communities.

Port authorities and their local communities go to great lengths to lure cruise ship lines to establish a regular call or homeport operations. In fact, port authorities do not measure the success of their business by revenue earned, but rather in terms of the amount of money passengers spend in their communities, the number hotel nights booked, and how many jobs have been created. It is this quest for economic impact from this lucrative industry that intensifies rivalry and in some situations creates an oversupply of facilities.

While it may not appear to be an overly attractive industry because of this rivalry and the power of the cruise lines, it is an industry that has the potential to create positive economic benefits that can mitigate the risk of participation. Thus, to put the

attractiveness of this industry into perspective, it is also important to acknowledge government and public support of this type industry in many communities.

The Five Force analysis summarized in Figure 2-7 on page 31 identifies the impact of the threat of new entrants (low), the bargaining power of buyers (moderate to high), the bargaining power of suppliers (low), and the threat of substitutes (moderate) on the rivalry in the cruise ship homeport industry in the Pacific Northwest. In addition to these four forces, competitive rivalry also has a dynamic of its own. Some of the influences that effect rivalry for ports in the Pacific Northwest include the changes in the dominant homeport in the market, the impact of slowing growth, perishability of the product, and the impact of government policy.

Strategic Stakes are High

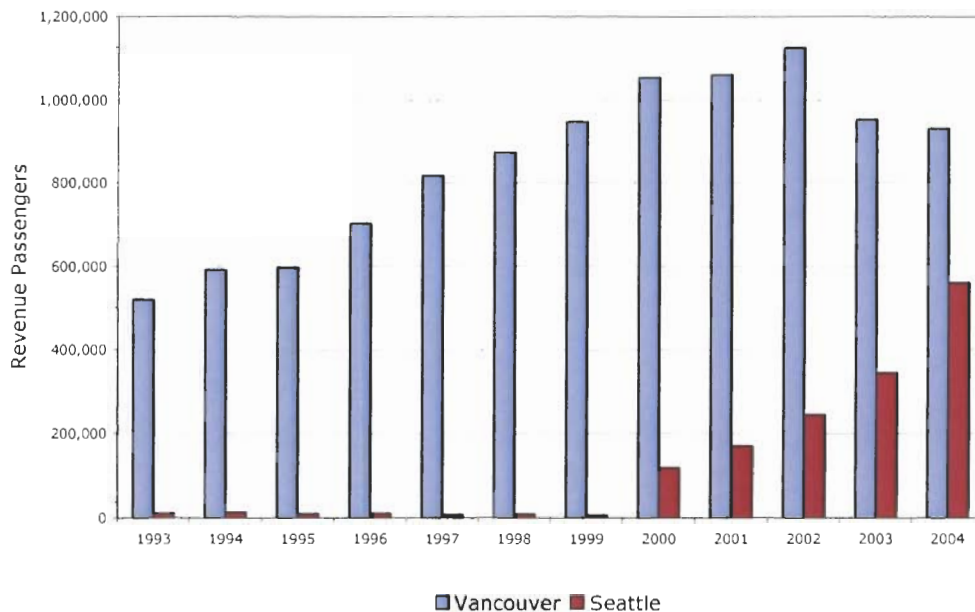
A significant factor increasing rivalry for homeports is the recent increase in market share by the port of Seattle, largely at the expense of the port of Vancouver. Until the year 2000 Vancouver had a virtual monopoly on the Alaska homeport business. During the 20-year period between 1982 and 2002, revenue passengers at the port of Vancouver increased from 155,000 to over 1.1 million for a compounded average growth rate of 10.6 per cent per year for this period (VPA, 2005b). Since 2002, the port of Vancouver has seen a decline in passengers, largely to the benefit of the Port of Seattle as shown on Figure 2-12 below.

In a few short years the port of Seattle has become the dominant homeport for the round trip market to Alaska and this trend is expected to increase.²² This loss in

²² Vancouver will remain the dominant homeport for the One-way market due to cabotage legislation.

dominant position only serves to intensify the rivalry between the ports of Seattle and Vancouver.

Figure 2-12: Alaska Homeport Revenue Passengers 1993-2004



Source: Based on data provided by the VPA with permission and from Cruise Industry News Annual 2004 p. 250.

Industry Growth Slowing

Growth in the Alaska cruise market is projected to slow down. Average annual growth in cruise ship passengers between 1991 and 2004 was 9.86 per cent. In future years, growth is expected to slow to an average growth rate of less than half (4.5%) to the year 2017 (Bermello, 2003). The slowing of growth in the market should increase rivalry both for homeports and ports of call, as each port will be vying for a share of the business.

Perishability

The *product* sold by cruise ship terminal owners is a facility that has both capital and operating costs associated with it whether or not it is used. Since the cruise season in the Pacific Northwest is quite limited – typically the end of April until the beginning of October – ports want to ensure they can get the maximum utility of their facilities. As such, perishability enhances rivalry since each port is trying to lure cruise lines into using their facility.

Government Policy

The key factor that moderates the effects of rivalry between ports for homeport facilities is the U.S Passengers Services Act. As such, cruise lines have little choice but to use the Port of Vancouver as its southerly homeport for this popular cruise. Since the Port of Vancouver does not need to compete for the one-way itinerary, rivalry between the ports of Vancouver and Seattle is restricted to the Inside Passage round trip cruise.

While there are a number of factors at play that suggest that rivalry could intensify, cabotage legislation tempers these effects and therefore rivalry between existing competitors would be characterized as moderate to high.

2.4.3 Assessment of Competitive Position

The cruise ship homeport market in the Pacific Northwest has evolved over the past few years to create two strong rivalrous homeports that both want to grow their cruise business to create economic wealth in their communities. The port of Vancouver's competitive position has diminished and its long-term prospects to realize the growth results it achieved in the 1990s is highly unlikely to return. In fact, the current long-term

forecast for revenue passengers in the port of Vancouver is a modest 1.34 million revenue passengers by 2020 (VPA, 2005b).

An assessment of the six key homeport success factors noted in Section 2.3 on page 54 is provided in Table 2-5 below.

Table 2-5: Competitive Assessment of Vancouver and Seattle

<i>Homeport Key Success Factors</i>	<i>Rating (1 to 5)</i>	
	Vancouver	Seattle
Geographic Location	4	4
Passenger Convenience	3	5
Efficient Terminals	3	3
Ability to Fund Terminal Development	3	4
Market Intelligence	4	3
Influence Passenger Decisions	3	2
Total Score (out of 30)	20	21

This assessment shows that both ports have different strengths and weaknesses, with the port of Seattle having a slight advantage over the port of Vancouver. However, the gap between the two ports is not wide and there is room for both ports to improve their performance in most of these success factors. A summary of the strengths and weaknesses of each port for all six factors is reviewed below.

Geographic Location

Vancouver and Seattle have positive location attributes that allow both ports to ensure successful homeport operations. Vancouver and Seattle are both within a comfortable sailing distance to key Alaskan destinations and have significant tourism

infrastructure and large international airports necessary to support the industry. While Vancouver has a slight advantage in being closer to Alaska, Seattle benefits in a location that has greater airlift capacity to key American cities and, located in the United States where passengers are not required to clear customs when they arrive at the airport or when they board the cruise ship. Seattle also has a greater ability to capture the drive market given that it has a larger metropolitan area to which it can draw.

Despite Seattle's location advantages noted above, Vancouver also has a location advantage over Seattle because it is not located in the United States. Vancouver benefits from cabotage legislation for the popular Alaska one-way market, and is likely to do so without competition. As noted in Table 1-3: Port of Vancouver Cruise Itineraries on page 13, the port of Vancouver had 105 Alaska one-way vessel calls in 2004 – which represented 37% of the port's total vessel calls.

As such, the ports of Vancouver and Seattle have different, yet relatively equal strengths in terms of their geographic location.

Passenger Convenience

Providing convenience for passengers means ensuring that the entire system of moving the passenger from their place of origin to boarding the vessel is as fast as possible. While many of the functions that effect passenger convenience are outside the direct control of a homeport, they ultimately impact on the success of the homeport. Seattle has two specific advantages over Vancouver as it relates to passenger convenience.

The first relates to its airport connections. The Seattle-Tacoma International Airport (Sea-Tac) has three times as many direct connections to North American destinations than YVR, and in 2003 over 20% of the port of Vancouver's passengers who arrived by air arrived at Sea-Tac and were bussed to Vancouver (Grant Thornton, 2003 p 65).

The second advantage of the port of Seattle relates to customs clearance. American passengers leaving the port of Seattle's cruise ship facilities do not require customs clearance at Sea-Tac nor at the Port's cruise ship terminals. With the advent of tighter border controls, customs clearance has become an onerous and time-consuming process that creates long delays at both airports and cruise ship terminals. The port of Vancouver is disadvantaged because U.S. Customs and Border Protection Services (USCBP) require its operations to be located at the Canadian port of departure (both airports and seaports). Accordingly, U.S. passengers must clear Canadian customs at YVR and U.S. customs at the port of Vancouver's cruise ship terminals on the embarkation, and in reverse for debarkation. Since nearly 80% of the port of Vancouver's cruise ship passengers are from the U.S. at an average age of 57 years old (seven years older than the average North American cruise passenger), the added hassle of customs clearance in Vancouver is a major inconvenience to passengers. And despite the VPA's and YVR's recently launched U.S Direct program, (detailed in Section 2.2.5), the port of Seattle has a natural competitive advantage over the port of Vancouver.

Efficient Terminals

Efficient terminals relate to how easy it is for the cruise lines to operate in the homeport, in terms of the ability of the facilities to handle the latest generation of large

cruise ships and the associated volume of passengers. It also relates to other operational aspects of the terminal, including access, ground transportation, and security.

Both Vancouver and Seattle have two cruise ship facilities, each with one located in the downtown and another located in the industrial port. While downtown cruise ship terminals have an appeal from a cruise marketing perspective, they are often more challenging environments from an operations standpoint, especially relating to ground transportation and security because they are more publicly accessible. Cruise ship facilities that are located in more isolated and unglamorous areas outside of the downtown core are becoming the preferred location for cruise lines from an operational perspective because they often have more terminal space available for busses, taxis, passenger vehicles, and delivery trucks. Both Vancouver's Ballantyne terminal and Seattle's Terminal 30 are more indicative of this type of operation, however Seattle's Terminal 30 facility consists of a modest prefabricated building. Given that the ports of Vancouver and Seattle each have their own unique strengths and weaknesses relating to their respective terminal efficiencies, it can be concluded at the present time that neither homeport has a significant advantage over the other, and both could make improvements to make their terminals more efficient.

Ability to Fund Terminal Development

The port of Seattle has an advantage over the port of Vancouver in its ability to fund cruise ship terminal development. While both ports are public entities, they differ in that the port of Vancouver is essentially a taxpayer, while the port of Seattle is a taxing authority. The port of Seattle collects a levy from the residents of the King County that is used to fund capital investments, and as such has a greater ability to fund cruise ship

terminal expansion; whereas the VPA not only pays property taxes (in the form of PILT), but the CMA specifically prohibits the VPA from obtaining funds from the government of Canada. As such, to fund future cruise infrastructure, the VPA must self-fund development from its passenger revenues or seek investment from other sources such as local government, the provincial government, or the tourism industry – none of which has been done before.

Market Intelligence

The VPA has a slight advantage over the port of Seattle in understanding the dynamics of the cruise ship industry given its length of experience in the market. The VPA has been building relationships with cruise lines and industry stakeholders over the past 20 years compared to Seattle's five years in the business. Despite Vancouver's slight advantage, both ports could improve their ability to understand the market and its players in order to properly position their products as the industry continues to grow and evolve.

Influence Passenger Decisions

The VPA has an advantage in its ability to influence passengers' decisions given the various marketing initiatives that it is involved in with the travel trade. While the port of Seattle has recently initiated marketing efforts with travel agents, it is not nearly as comprehensive as the VPA's travel trade program (E. Englezos, personal communication, June 14, 2005). In addition, the VPA was instrumental in establishing the Cruise BC marketing program, which is much more extensive than a comparable program which the port of Seattle is a member.

2.5 Strategic Alternatives

The assessment of the competitive position of the port of the Vancouver's cruise business in relation to the port of Seattle's, as noted in section 2.4.3, provides insight into the potential opportunities that the VPA can explore to meet its objectives for this business sector. The VPA's main objectives for its cruise ship business includes growing the business in order to maximize the economic impact to the local community, and to do so in a manner that is financially viable and sustainable in the long term.

Ideally, the strategic alternatives considered by the VPA should exploit advantages, reduce disadvantages, and find new values that can offset the advantages of the port of Seattle. Two opposing strategic alternatives for the VPA are outlined below.

Strategic Choice 1: Continue Head-to-Head Competition

This strategy contemplates the VPA continuing head-to-head competition with the port of Seattle for the Alaska cruise market. Given that both Vancouver and Seattle's cruise ship berths are essentially at capacity on the weekends, the strategy would likely require the VPA to develop another terminal to add a fifth berth for weekend usage. In this type of competitive market, it is also assumed that the port of Seattle would also want to expand by adding a fourth cruise ship berth. Finally, this strategy assumes that the VPA would continue to pursue the Cruise BC marketing initiative as the principal means of diversifying its market

Strategic Choice 2: Develop a framework for Cooperation

This strategy requires the VPA to take a departure from its current competitive strategy by developing a framework of cooperation with the port of Seattle. Based on the

assumption the VPA and the port of Seattle are in a *prisoner's dilemma* as it relates to their respective cruise businesses – whereby neither port would be better off if it expanded cruise ship facilities given the likelihood of a simultaneous move by the other port in also expanding. If both ports expanded, neither would experience any significant increase in revenue passengers and would merely shift existing weekday berth utilization to the weekends. By cooperating and not expanding, both ports would force cruise lines to utilize weekday berths and thereby improve berth utilization and return on existing investment.

A strategy of cooperation could vary along a continuum that at one extreme would be as simple as signally to each other not to expand, at the opposite extreme it could include developing cooperative marketing programs focussed on growing the entire market instead of fighting about how to divide it up.

Since it is not in the interests of either port to expand their facilities at the present time, they may wish to find ways to encourage the cruise lines to use weekday berths. While it is the cruise lines that develop their itineraries, the two ports could encourage and promote the use of both ports – as a homeport and a port of call. For example, for the Alaska round trip market, the port of Seattle could encourage cruise lines that homeport in Seattle on the weekend to include the port of Vancouver as a port of call during the week; and, for Pacific Northwest Cruises, cruise lines could be encourage to homeport in the port of Vancouver and include the port of Seattle as a port of call. This would enable ports to receive the financial benefits of greater berth utilization with the port of call business, and also bring economic impact to their communities with homeport service. One of the ways in which the two ports could encourage cruise lines to consider these

type of creative arrangements would be by providing preferential berth assignments to cruise lines that not only better utilize weekend and weekday berths, but also that utilize both Vancouver and Seattle in their itineraries.

3 INTERNAL ANALYSIS

The following section conducts an internal analysis of the VPA to determine if Strategic Choice No. 2 (Cooperation with the port of Seattle), as identified in section 2.5, is a viable strategic alternative for growing the VPA's cruise ship business compared with the option of head-to-head competition. This includes a review of the current management preferences of the VPA to determine if the proposal is feasible, an analysis of the resources required to undertake the proposed strategy, and finally a review of the organizational capabilities required to implement the strategy.

3.1 Management Preference Analysis

3.1.1 Management Preferences

Crossan, Fry and Killing (2005) suggest that current management preferences may be examined by evaluating management's values and beliefs of four specific components of a strategic proposal. These include goals, product/market focus, value proposition, and core activities (p. 134). This section evaluates the VPA's current management preferences for its cruise ship business for each of these components and concludes with an overall assessment of whether or not the VPA's management could pursue a strategy of cooperation.

Goals

The VPA's management predisposition to the goal of its cruise ship business is currently in flux. Prior to the recent competition from the port of Seattle, management's

goal was clearly on revenue passenger growth and market dominance. That goal has, however, been shifting towards a desire to stabilize the business and improve the return on investment while at the same time maximizing the economic benefits that come to the community from the business.

Product/Market Focus

The product/market focus preference of the VPA's management is to diversify the market beyond Alaska to include the BC Coast through the Cruise BC initiative. Management believe that the diversification of the market will counter the negative impacts of competition from the port of Seattle for the Alaska round trip cruise.

Value Proposition

The VPA's management believe that its value proposition comes from the high quality of the service and facilities provided to its cruise line customers. This belief may also be evolving given the changes seen in the market over the past few years and management may be open to different views on the port of Vancouver's value proposition.

Core Activities

The VPA's management preference for its core activities has been to reduce the organization's role in the operation of its cruise terminals. This strategic preference has been difficult to achieve, however, since it has property tax implications (for a further explanation see footnote 19 on page 46). Notwithstanding this, management's predisposition is that the organization has a role in facilitating and marketing the

business, but it does not need to be directly involved in operations nor diversify into complementary businesses.

3.1.2 Management Preference Assessment

Management preferences must be considered in the context of past experience. The VPA's cruise business was once one of its shining stars, generating double-digit annual growth rates for over ten years. It has now lost its lustre and has become the most underperforming business sector in the VPA's portfolio. And while the VPA has always known, and has tried to ready itself for eventual competition from the port of Seattle, it never expected to lose so much market share so quickly. In the late 1990s, management began preparing for competition by focusing the organization on service, improving operations and facilities, and expanding capacity by adding a third berth to Canada Place. Obviously, the VPA could not have predicted how the industry would change following the terrorism events of September 11, 2001 – the emergence of the drive market, the reduction of flights to Vancouver, and the increased hassles for passengers to cross borders and clear security.

In addition to not expecting these market changes, the VPA's management was even more surprised at how quickly Seattle responded to the opportunity. The port of Seattle was able to achieve revenue passenger levels in five years that took the VPA 15 years to grow. Given this history, and a possible sense of resentment towards the port of Seattle for taking such a big share of the VPA's business, management may not be easily convinced that cooperation with the port of Seattle is the most appropriate strategic choice.

Yet, the Industry Analysis from the previous section illustrates that port of Seattle does not have a significant strategic advantage over the port of the Vancouver to the extent that Seattle would be any more inclined to favour head-to-head competition. The port of Seattle has grown quite quickly and would also benefit by not having to build additional facilities – especially since one of its terminals is currently located in a temporary building, and it does not appear that Seattle is making much of a financial return on this business.

There is evidence to suggest that the management at the port of Seattle would welcome a more cooperative model. In addressing the Vancouver Board of Trade on January 14, 2005, Mic Dinsmore, the Chief Executive Officer of the port of Seattle noted that although the two ports compete with one another, they are uniquely positioned to experience significant growth across a number of business sectors including cruise, and that the two ports should open a dialogue and communicate more (Banister, 2005). To further illustrate that the port of Seattle's cruise interests are aligned with the VPA's, Dinsmore remarked that the port of Seattle is attempting to increase its cruise business by changing from just a weekend port to offering service on other days of the week (Banister, 2005).

Dinsmore's speech should provide the VPA's management with a strong signal that the port of Seattle is willing to cooperate and that it is not interested in growing its business by adding more cruise berth capacity for weekend usage. If this signal can be viewed as a credible commitment, then it is possible that the VPA's management could be open to the possibility of cooperation, or at least willing to test out the idea of cooperation in some limited manner.

Depending on the degree of cooperation, it is possible that this strategy could be aligned with the VPA's management's goals of growing the business (albeit at a slower rate), receiving a fair return on investment, diversifying the market beyond Alaska, and reducing the VPA's role in cruise terminal operations.

It is Dinsmore's hope that the two ports can learn from one another and grow together (Banister, 2005). With success, a cooperative strategy has the potential to evolve beyond learning from each other to working together where it is mutually beneficial, such as joint marketing initiatives to promote the entire cruise region. If executed properly, it is possible that the strategy could go beyond cruise to include other competitive business sectors. In fact, Dinsmore specifically noted that there are many areas where the VPA and the port of Seattle can work together including improving security, obtaining capital investment and managing expansion to accommodate the exponential increase in trade with China.

Cooperation does not happen overnight and acceptance of such a strategy should be based on a series of smaller steps and initiatives to build trust between the two organizations to grow confidence in the strategy. The building of trust must be based on developing personal and professional relationships that can be tested over time. Much like a classic game theory scenario, each player will need to read and understand the signals sent by the other to determine the motivation and intent to cooperate and compete (Crossan, et. al, 2005 p. 58). The VPA can start by sending a signal back to the port of Seattle that it too is not interested in expanding capacity, and then take them up on the invitation to start the dialogue. One way for the VPA to signal back to Seattle that it is

interested in cooperation is by refocusing its own marketing efforts on the benefits of the cruise region rather than the benefits of the port of Vancouver.

3.2 Resource Analysis

3.2.1 Resource Requirements

In addition to ensuring that the proposed strategy has the potential to be supported by management, it is also important to understand the various resources required to implement the strategy. This section examines the resources required to implement the two opposing strategies including marketing, financial, operations, human resources, political and reputation.

3.2.1.1 Marketing

If the VPA continues with head-on competition with the port of Seattle, it would need to increase its marketing efforts and expenditures to ensure that cruise lines and their customers understand the port of Vancouver's value and are able to further differentiate this value from the port of Seattle's. These efforts would be even more critical, if as part of the competitive strategy, the VPA expands its cruise ship facilities. This would mean more direct contact with cruise lines to ensure the added capacity is utilized. In addition, it is likely that the VPA would need to expand its marketing efforts through the distribution chain (i.e. travel trade, travel agents etc.) so that Vancouver is the preferred homeport when passengers choose where to start their Alaskan cruises.

However, a proposition to increase cruise marketing efforts beyond existing levels could be met with some resistance given that there is an ongoing debate within the VPA

about the value derived from such efforts. In fact, marketing budgets for travel trade were reduced in 2005 in order to decrease cruise operating costs.

If the VPA were to proceed with a more cooperative strategy with the port of Seattle, it would need to refocus its marketing efforts, but not necessarily increase the cost of these efforts. As noted in section 2.4.3, the VPA has a competitive advantage in marketing intelligence, and as such, offers strengths to the relationship that can benefit the port of Seattle.

Nielsen (1987) suggests that there are seven different initiatives that can be undertaken as part of a cooperative marketing strategy. These include: (i) pooling similar marketing resources and risks, (ii) trading different resources, (iii) expanding total consumer market demand, (iv) increasing the number of cooperative marketing players, (v) des-escalating destructive competition, (vi) cross-subsidizing markets, and (vii) implementing joint marketing contingency plans (p.62).

While not all of these initiatives are necessary to enable marketing cooperation between the ports of Vancouver and Seattle, the most plausible initiatives include the pooling of similar marketing resources, trading marketing resources, and expanding total consumer demand.

A pooling initiative can vary in degree, but includes some form of bringing together of the marketing resources of the two ports. This could include a formal joint marketing strategy, creating an entity much like the existing Cruise BC group, or a less formal, yet complementary marketing arrangement. Marketing resources currently devoted to the Cruise BC initiative could be broadened and/or diverted to a new entity focussed on the larger Pacific Northwest/Cascadia region including the port of Seattle

and perhaps other ports of call in Puget Sound. Some new marketing resources that could be required include those to develop a new cooperative *brand* for the two ports that can be used to leverage individual marketing efforts.

Trading different marketing resources would include the sharing of market research information about the cruise lines and the cruise industry in general, to avoid duplication and to save money for the two partners. Nielsen (1987) suggests that trading different and complementary marketing resources requires that firms understand their own and their partner's strengths and weaknesses, and requires the negotiating of skills among the partners to ensure win-win trades (page 63).

Expanding the total consumer demand would likely be a key focus of the cooperative marketing efforts between the two ports. This can be done by refocusing advertising away from the benefits of the individual port to a focus on the positive attributes of the entire cruise region.

Many of the marketing resources for a cooperative model would need to be created or retooled. These include the development of a new marketing and advertising campaigns, re-examination of existing pricing strategies, and the development of new public and government relations initiatives. Development of these new resources is achievable and could be done without added financial cost if developed, in part with the port of Seattle.

3.2.1.2 Financial

As an organization, the VPA has a solid financial position. In 2004, the VPA had a net income of nearly \$23.8 million, and a net operating margin of 51.6%. Key financial

indicators of the VPA's financial performance, including its operating revenue, net income, profitability, net operating margin, and financial leverage for the years 2002, 2003, and 2004 are shown in Table 3-1 below.

Table 3-1: VPA Key Financial Indicators, 2002-2004

<i>Financial Indicator</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>
Operating Revenue (thousands)	\$96,022	\$102,908	\$100,856
Net Income (thousands)	\$25,155	26,833	\$23,793
Profitability (Net Income/Revenue)	26.2%	26.1%	23.6%
Net Operating Margin (EBITDA/Revenue)	55.4%	50.7%	51.6%
Leverage (Long Liabilities /Equity)	7.35%	7.32%	6.37%

Source: Based on data from VPA, 2004c and VPA, 2005d.

Despite the VPA's financial health as an organization, its cruise ship passenger business is not meeting financial expectations. As noted in section 1.4.2, the VPA has invested in excess of \$150 million (present value) in the development of its cruise ship facilities, the most recent project being a \$75 million redevelopment and expansion of the Canada Place cruise ship terminal in 2001 that included an additional berth.

Based on the revenue passenger forecasts at the time, the VPA made the decision to expand its facilities on the expectation of receiving a 10% rate of return over a 20-year investment period. In 2004, the VPA's cruise revenues were approximately \$11.8 million, which is 18% lower than was what expected at the time of making the decision to expand Canada Place. In fact, reforecasted revenues to the end of the original investment period suggest that revenues will be 63% lower than what was originally forecasted.

Notwithstanding the VPA's solid financial position and its ability to finance additional capital investment, it is certain that the rationale for further cruise expansion would not be justified from a financial perspective. In fact, a discounted cash flow analysis of potential new revenues that would be gained from expansion would only justify an investment of \$33.7 million, based on meeting the VPA's hurdle rate of 10%. The cost of building a new one-berth cruise facility would likely be in excess of \$85 million (T. Glasheen, personal communication, June 2004). The financial rationale for such an expansion would be even further reduced if port of Seattle retaliated by expanding as well.

Given the financial implications of cruise expansion to the VPA, a strategy that required additional investment would be difficult from a financial resource perspective. This includes trying to compete head to head with the port of Seattle, given the likelihood competition would lead to Vancouver needing to add a fifth berth to its cruise portfolio in order to retain and grow its market share. A strategy of cooperation, however, would require minimal additional financial resources to implement provided that both ports do not add capacity, at least in the short run.

3.2.1.3 Operations

The different strategies for the VPA's cruise business will not have a material effect on operational resources except to the extent that a more competitive strategy would require operations to become more efficient because there would be continual pressure to reduce costs to improve margins, whereas a cooperative strategy would have less of a demand to reduce or streamline operational costs.

3.2.1.4 Human Resources

Human resource requirements would vary depending on whether a more competitive or cooperative strategy is chosen. With a more competitive strategy, the VPA will require individuals who are very good in operations, marketing, and logistics, while a more cooperative strategy would require people who have these same skills but are also skilled in developing and building strategic alliances and partnerships.

3.2.1.5 Political

As noted in section 3.2.1.2 above, the expansion of cruise ship facilities in the port of Vancouver would not meet the VPA's financial investment criteria and would likely require investment from government if it were to proceed (on the basis of the potential economic benefits it could bring). To date, the VPA has self-funded cruise ship terminal development and it would take significant resources to gain the support of government for to fund further expansion given the various demands for government funds, especially in light of the recent significant tourism investments made both by the provincial and federal governments for convention centre expansion project in Vancouver. In addition, in order to obtain federal investment in cruise ship facilities changes would be required to the CMA which specifically restricts ports from receiving funding from the federal government.

In order to implement a cooperative strategy general political support will be required. As an organization created by federal legislation, and with a Board that includes some members who are appointed by the various levels of government, the VPA needs to ensure that there is broad political support for its strategies and actions. It will need to ensure that this strategy is viewed as being in the best interests of Vancouver and

Canada as a whole. The VPA will also need to expend resources to ensure that politicians and those who influence them understand that a cooperative strategy is not only be better from a financial perspective, but enables the VPA to grow the business in a sustainable manner in order to bring lasting economic benefits to the region.

3.2.1.6 Reputation

While there are no material effects on the VPA's reputation if it proceeds with a competitive strategy, the VPA would need to obtain support from the local community and its local stakeholders in order to pursue a cooperative strategy. It is important to ensure that there is support for this strategy from the local tourism agencies that work in conjunction with the VPA to support the cruise industry. Tourism agencies' strategies would have to be in alignment with the VPA's cooperation strategy.

3.2.2 Strategy-Resource Assessment

It would appear that the VPA is in relatively good position to implement a cooperative strategy based on the assessment of resources. For the most part, the VPA either has the resource readily available or can easily adapt existing resources to meet the needs of this strategy. Table 3-2 below provides a summary of these resource requirements and the gaps that need to be addressed in each strategy.

Table 3-2: Summary of Resource Requirements for Strategy Options and Gaps

<i>Competition Strategy</i>		<i>Cooperative Strategy</i>	
Attributes	Gaps	Attributes	Gaps
<i>Marketing</i>			
<ul style="list-style-type: none"> • More direct contact with cruise lines • Increase advertising • Increase marketing efforts towards travel agents and passengers • Additional marketing costs 	<ul style="list-style-type: none"> • Increased marketing costs (possible to close gap) 	<ul style="list-style-type: none"> • Broaden and refocus marketing efforts • Sharing of marketing resources • Refocus advertising on the cruise region as opposed to the port 	<ul style="list-style-type: none"> • Develop new marketing program (possible to close gap)
<i>Financial</i>			
<ul style="list-style-type: none"> • Likely require cruise facility expansion • Expansion can not be justified based on financial return • Financial performance will diminish 	<ul style="list-style-type: none"> • Develop new facilities (very difficult to close gap) 	<ul style="list-style-type: none"> • Additional financial resources not required • Cruise facility expansion does not need to occur until it is financially feasible 	<ul style="list-style-type: none"> • None
<i>Operations</i>			
<ul style="list-style-type: none"> • Will lead to downward pressure on operational costs 	<ul style="list-style-type: none"> • Develop operational efficiencies (difficult to close gap) 	<ul style="list-style-type: none"> • No material impact 	<ul style="list-style-type: none"> • None
<i>Human Resources</i>			
<ul style="list-style-type: none"> • Need for experts in specific functional areas 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Need for strategic alliance/partnership skills 	<ul style="list-style-type: none"> • Develop new skills (possible to close gap)
<i>Political</i>			
<ul style="list-style-type: none"> • Need to obtain investment from provincial and/or federal government for expanded facilities • Changes needed to the CMA to allow federal investment 	<ul style="list-style-type: none"> • Develop political support and obtain government investment (difficult to close gap) 	<ul style="list-style-type: none"> • Would require general political support to pursue strategy 	<ul style="list-style-type: none"> • Develop political support (possible to close gap)
<i>Reputation</i>			
<ul style="list-style-type: none"> • No material impact 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Need to obtain support from local community • Support will be need from local tourism agencies 	<ul style="list-style-type: none"> • Develop local support (possible to close gap)

While both strategies require the VPA to address various resource gaps in order to implement, it would appear that the gaps identified in the cooperative strategy are more achievable. The cooperative strategy requires the development of new marketing programs, augmenting human resource skills, and developing political and local support for the strategy, while the competitive strategy requires much more substantial resources given the requirement to develop additional facilities in order to compete.

In addition to the resource requirements noted above, it is important to consider the various strengths that the two organizations could bring to a cooperative relationship. The port of Seattle has strengths in bringing capital investment to its port, while the VPA has strengths in developing cruise marketing programs. Each party has the ability to augment weaknesses with the strengths of the other. Having different strengths and weaknesses brings balance to the relationship.

3.3 Strategy-Organization Analysis

The organizational capabilities required to implement a strategy of cooperation needs to be examined in relation to the VPA's structure, culture and systems.

Structure

As noted earlier in this paper, the VPA has evolved from once a centrally controlled branch office of the National Harbour's Board to a semi-autonomous agent of the crown with far greater local controls. A nine-member Board of Directors appointed by the three levels of government governs the VPA. The VPA has approximately 160 employees belonging to 16 separate departments, organized in four divisions reporting to a Vice-President, who along with the President and Chief Executive Officer comprise the

Executive Management Team. The VPA has a highly centralized hierarchical organizational structure, which would be fairly common in a commercialized governmental entity such as a port authority. The VPA further organizes itself into a variety of cross-departmental working committees, groups, and teams that address day-to-day operations as well as special projects and initiatives. An example of an ongoing operational team includes the Cruise Team, which provides coordination of cruise operations. The team includes representation from a variety of internal departments including Business Development, Trade Development (includes the cruise marketing function), Operations & Harbour Master, Security, Engineering & Maintenance, and Real Estate. Other ad hoc teams are created to address specific initiatives, such as a new cruise marketing program. Typically these teams would comprise of a lead department that would bring together representatives of other departments to have input into an initiative. Depending on the complexity of the initiative or issue, the lead department (via the department head) would seek a decision from the Executive Management Team. It is also very common for the VPA to organize external committees and teams to deal with planning, coordination, operational issues, and initiatives

Despite the hierarchical nature of the organization, the VPA has demonstrated a fair amount of flexibility to change departmental and reporting structures to achieve strategic goals. For example, it has created a special purpose team charged with developing and implementing the anticipated growth of containerized cargoes in the port. Therefore, in order to pursue a cooperative cruise strategy with the port of Seattle, the VPA could develop appropriate teams and committees, both internally and externally, to achieve new a strategic cruise goal.

Recognizing how key decisions are made in the VPA, it would be most appropriate that the strategy be led by a joint VPA/port of Seattle coordinating committee comprised of key executives from both organizations. There would also be the need to have special purpose teams, similar in focus to the VPA's existing Cruise Team. Other teams could be formed to address marketing initiatives, cross-organizational learning (terminal operations, security, etc.), as well as a group charged with monitoring and enhancing the relationship.

Culture

The VPA has developed a culture of competition with other ports – both formally (in corporate materials) and informally (through group norms). Comparisons are constantly made about the port of Vancouver's position relative to other ports – how it ranks against its most immediate competitors, the rest of Canada, North America, or the world. A culture of competition is engrained in the organizational body and individual employees. Changing the corporate culture to enable the organization to cooperate with the port of Seattle in its cruise sector may be a paradigm shift for some employees. This is a potentially a large gap that would need to be addressed in order to implement a cooperative strategy. This can be addressed, in part, by ensuring that the purpose of the new strategy is properly explained to all, and sufficient time and effort is devoted to gain the buy-in and support of employees, especially those who would be responsible to implement the strategy.

Systems

The VPA has a variety of formal and informal administrative and decision-making systems it uses to undertake its business. More formal systems include policies and procedures for delegated limits of authority, both in terms of dollar value and other approval limits. In recent years, many of these authorities have been dramatically increased to enable more responsibility and decision-making powers across the organization. While it is not expected that any of these systems would have a material effect on the success of a specific cruise strategy, recent increases in responsibility will benefit either of the two cruise strategies under consideration.

3.4 Assessment of Cooperative Strategy

This internal analysis concludes that cooperation with the port of Seattle is a viable strategy for the VPA to pursue for its cruise business provided the strategy addresses the issues noted in Table 3-3 below.

Table 3-3: Assessment of Cooperative Strategy

	<i>Issue</i>	<i>Possible Resolution</i>
Management Preference	<ul style="list-style-type: none"> • VPA’s management needs confidence that the port of Seattle is interested in cooperation; 	<ul style="list-style-type: none"> • Signal to the port of Seattle that the VPA does not want to expand either; • Start the dialogue and begin with small steps to grow the relationship;
Marketing Resources	<ul style="list-style-type: none"> • VPA’s marketing approach is currently based on a competitive strategy; 	<ul style="list-style-type: none"> • Develop a new joint marketing program with the port of Seattle focussed on the cruise region and diversifying the market to benefit both ports;
Human Resources	<ul style="list-style-type: none"> • VPA employees do not have the skills necessary to implement a cooperative strategy; 	<ul style="list-style-type: none"> • Implement training programs to develop the skills necessary for a cooperative strategy
Reputation	<ul style="list-style-type: none"> • VPA needs to ensure there is political support as well as broad support from stakeholders for the strategy; 	<ul style="list-style-type: none"> • Educate and inform key influencers about the need for, and the benefits of the strategy;
Organizational Structure	<ul style="list-style-type: none"> • VPA needs to ensure that the organization is structured so that the strategy can succeed; 	<ul style="list-style-type: none"> • Develop an appropriate structure to implement a cooperative strategy including a senior management coordinating committee and other special purpose teams;
Organizational Culture	<ul style="list-style-type: none"> • VPA’s current corporate culture is based on being competitive with other ports; 	<ul style="list-style-type: none"> • Develop internal change management programs to ensure support for the cooperative strategy;

4 RECOMMENDATIONS

It is recommended that the VPA pursue a strategy of cooperation with port of Seattle to enable both ports to sustain and grow their cruise ship business to benefit the local economies of their respective communities. Both ports need to ease the escalation of competition by not expanding berth capacity at the present time and embrace a new model of co-opitition. To the extent that it is legally possible, the two ports should focus on working together to expand the entire cruise market in the Pacific Northwest.

The VPA should build action plans that focus on the following strategic considerations:

1. In order to implement this strategy it would need equal support from the VPA and the port of Seattle. While the port of Seattle has signalled that it is interested in cooperation, the first step towards implementing the strategy will be to start the dialogue at a senior level in both organizations to develop the framework and strategic support from both organizations.
2. Once the framework of cooperation is established between the organizations, it will be necessary for both to reach back to their respective stakeholders, staff, and other influencers to substantiate their decision to pursue this strategy and obtain support for this new direction. It is quite likely that the cruise lines will be concerned about this new strategic direction, and as such, the two ports would need to provide

confidence to their customers that this new strategy will provide the needed stability to focus on the long term growth of this cruise region, which will be a benefit to all.

3. Depending on how much cooperation the two organizations are committed to pursuing will determine the range of cooperate initiatives to be considered. And while it can be expected that at the very least there will be cooperative marketing initiatives, it would be important that all initiatives and tactics be developed jointly.
4. Building trust between the two ports will not occur over night, and as such, the VPA should focus on building the relationship and developing appropriate internal and external committees to manage the relationship and the tactics to implement the strategy.
5. In addition to implementing the cooperative strategy, the VPA must not lose sight of other factors that will continue to influence its success as a homeport. The VPA should continue to improve the efficiency of its cruise ship terminals to benefit its cruise line customers, as well as work with other agencies and government to ensure streamlined and efficient passenger movements through the entire logistics chain.
6. The VPA needs to continuously monitor the relationship and the success of the strategy. Many factors that affect the strategy can change quickly, and it would be prudent for the VPA to be developing means to evaluate the success of the strategy and provide joint mechanisms to monitor the relationship and its success for both ports.

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Appendix 1: Summary of Published Cruise Fees

<i>Type of Fee</i>	<i>Fee Detail</i>	<i>Fee</i>
Harbour Dues Fee	Charge to a vessel for each harbour entry. <i>Intended for recovery of investments and costs associated with harbour operations.</i>	<ul style="list-style-type: none"> • \$0.075/GRT for the first 5 arrivals each year
Berthage Fees	Fee relating to the physical size of a vessel alongside berths. <i>Intended to recover investments and costs associated with the wharf apron and berth dredging and maintenance.</i>	Canada Place: <ul style="list-style-type: none"> • \$9.46 per metre of vessel for first 12 hours • \$0.84 per metre of vessel per hour or portion hereof after the 12th hour All Other Terminals: <ul style="list-style-type: none"> • \$0.192 per metre of vessel per hour
Passenger Fees	Fee for each passenger embarkation and disembarkation. <i>Intended for recovery of investments and costs associated with provision of cruise terminal facilities and infrastructure.</i>	<ul style="list-style-type: none"> • \$ 11.00 each – first 15,000 pax • \$ 10.75 – 15,001st to the 45,000th pax • \$ 10.50 – 45,001st to the 75,000th pax • \$ 10.25 – 75,001st to the 105,000th pax • \$ 10.00 – 105,001st + pax
Services And Facilities	Fee for passenger vessel for the use of Port property. <i>Intended for recovery of investments and costs associated with provision of cruise infrastructure.</i>	<ul style="list-style-type: none"> • \$22.00 per metre of berth used, minimum 12 hours • \$2.00 for each additional hour or part thereof
Cruise Terminal Fresh Water Supply Fee	Fresh Water supplied to vessels	<ul style="list-style-type: none"> • \$1.06 per tonne

Source: Table created by author based on VPA, 2005 p. 17

Appendix 2: North American Passenger Capacity by Cruise Line

<i>Cruise Lines 2004</i>	<i>No of Lower Berths</i>	<i>No of Ships</i>
Carnival Corporation		
<i>Carnival Cruise Lines</i>	40,984	19
<i>Costa Cruise Lines</i>	15,567	10
<i>Cunard Line, Ltd.</i>	5,079	3
<i>Holland America Line</i>	16,319	12
<i>Princess Cruises</i>	19,740	11
<i>Seabourn Cruise Line</i>	624	3
<i>Swan Hellenic</i>	360	1
<i>Windstar Cruises</i>	604	3
Subtotal	99,277	62
Crystal Cruises	2,964	3
Disney Cruise Line	3,508	2
First European	6,622	6
MSC Italian Cruises	4,181	4
NCL Group		
<i>Norwegian Cruise Line</i>	17,958	10
<i>Orient Lines Inc.</i>	845	1
Subtotal	18,803	11
Norwegian Coastal Voyages	6,092	14
Oceania Cruises	1,368	2
Radisson Seven Seas Cruises	2,764	6
Royal Caribbean Cruise Lines (RCCL)		
<i>Celebrity Cruises</i>	16,018	9
<i>Royal Caribbean International</i>	43,470	19
Subtotal	59,488	28
Silver Sea Cruises	1,356	4
Total	206,423	142

Source: Based on data from CLIA, 2004, p. 39

Appendix 3: Cruise Regions, Capacity for 2000 and 2004

<i>Destination</i>	<i>2000 Total Bed Days</i>	<i>2004 Total Bed Days</i>	<i>Avg Annual Growth Rate 2000-2004</i>
Africa	502,773	17,640	-56.7%
Alaska	4,197,332	5,913,967	8.9%
Antarctica	48,499	219,296	45.8%
Bahamas	3,200,346	3,656,705	3.4%
Bermuda	988,391	1,324,690	7.6%
Canada\ New England	1,107,689	1,488,585	7.7%
Caribbean	21,510,142	31,210,605	9.8%
Europe	3,744,693	7,560,171	19.2%
Far East (Orient)	201,582	403,538	18.9%
Hawaii	857,390	2,629,458	32.3%
Indian Ocean	120,698	10,544	-45.6%
Mediterranean	6,277,064	9,704,398	11.5%
Mexico West	2,680,934	4,827,262	15.8%
Mississippi	347,140	-	-100.0%
Party Cruises	68,203	14,888	-31.6%
South America	825,670	1,088,569	7.2%
South Pacific	1,155,217	683,506	-12.3%
Southeast Asia	244,620	20,372	-46.3%
Trans Atlantic	1,015,625	1,425,596	8.8%
Trans Panama Canal	2,573,444	2,930,528	3.3%
Trans Pacific	52,400	11,600	-31.4%
U.S. Coastal East	1,402,429	60,072	-54.5%
U.S. Coastal West	217,518	643,792	31.2%
Unclassified	108,676	989,750	73.7%
World	414,342	462,934	2.8%
Total	53,862,817	77,298,466	9.5%

Source: Based on data from CLIA, 2004, p. 43

Appendix 4: Cruise Ships Under Construction or On Order 2005-2009

<i>Cruise Line</i>	<i>Ship</i>	<i>Tonnage</i>	<i>Capacity</i>
<i>2005</i>			
Carnival Cruise Line	Carnival Liberty	110,000	2,974
P&O Cruises	Arcadia	85,000	1,968
Norwegian Cruise Line	Pride of America	70,000	2,000
Norwegian Cruise Line	Norwegian Jewel	93,000	2,400
<i>2006</i>			
Costa Cruise Lines	Concordia	110,000	3,000
Holland America	Noordam	84,000	1,800
MSC Italian Cruises	Musica	90,000	2,550
Norwegian Cruise Line	Pride of Hawaii	93,000	2,400
Princess Cruises	Crown Princess	116,000	3,100
Royal Caribbean International	Freedom of the Seas	160,000	3,600
<i>2007</i>			
AIDA	Unnamed	68,500	2,030
Carnival Cruise Line	Carnival Freedom	110,000	2,974
Costa Cruise Lines	Unnamed	112,000	3,000
Cunard Line Ltd.	Queen Victoria	90,000	2,000
MSC Italian Cruises	Orchestra	90,000	2,550
Norwegian Cruise Line	Unnamed	93,000	2,400
Norwegian Cruise Line	Letter of intent	89,000	2,430
Princess Cruises	California		
Princess Cruises	Princess	116,000	3,100
RCI	Unnamed	160,000	3,600
<i>2008</i>			
Norwegian Cruise Line	Option	89,000	2,430
Carnival Corporation (cruise line not determined)	TBA	110,000	3,000
Carnival Corporation (cruise line not determined)	TBA	116,000	3,100
<i>2009</i>			
AIDA	Unnamed	68,500	2,030
Average		101,000	2,628

Source: Based on data from "World Orderbook," 2005 p. 20.

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