

Journal of Hospitality Financial Management

The Professional Refereed Journal of the International Association of Hospitality Financial Management Educators

Volume 19 | Issue 1

Article 6

Summer 7-2011

Revenue Management as a Multi-disciplinary Business Process

Bonnie Buckhiester

Buckhiester Management Limited

Follow this and additional works at: <https://scholarworks.umass.edu/jhfm>

Recommended Citation

Buckhiester, Bonnie (2011) "Revenue Management as a Multi-disciplinary Business Process," *Journal of Hospitality Financial Management*. Vol. 19 : Iss. 1 , Article 6.

Available at: <https://scholarworks.umass.edu/jhfm/vol19/iss1/6>

This Invited Article is brought to you for free and open access by ScholarWorks@UMass Amherst. It has been accepted for inclusion in Journal of Hospitality Financial Management by an authorized editor of ScholarWorks@UMass Amherst. For more information, please contact scholarworks@library.umass.edu.

REVENUE MANAGEMENT AS A MULTI-DISCIPLINARY BUSINESS PROCESS

Introduction

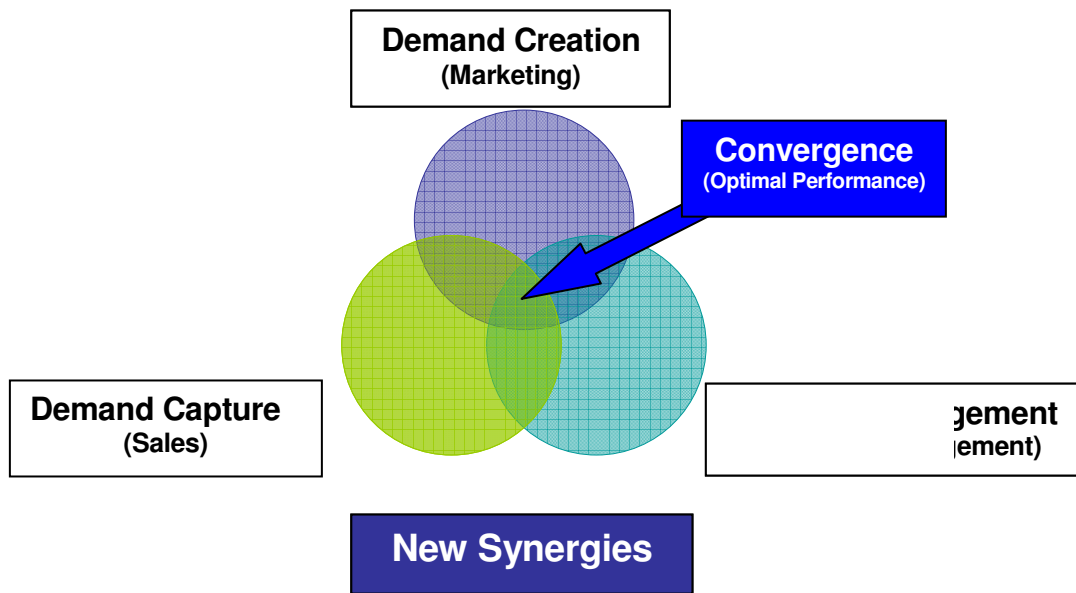
Hotels and resorts have been implementing various forms of yield management for decades. Reliance on instincts to guide selling strategies was often the centerpiece of decision-making. However, it is no surprise that where rudimentary procedures were once enough, today's volatile marketplaces and complex electronic distribution environments command a much higher level of sophistication than ever before. As hotels try to survive in fast-paced, fragmented markets, many have yet to reach their full revenue potential that a well-managed, well-resourced revenue management program can yield.

A sophisticated revenue management regimen includes both science and instinct; it is both tactical and strategic; and it is much more a collaborative effort than an individual one. All of these elements must work in tandem if a hotel or resort is to optimize demand. The industry can no longer afford to characterize the revenue management discipline as an application – such as in the case of a revenue management software system. It also cannot narrowly focus the discipline on electronic distribution – as in the tasks associated with opening and closing rates, dates and lengths of stay – more appropriately termed inventory management.

Instead, revenue management must be treated as a highly structured, multi-disciplinary business process. One that if followed judiciously enables a property to develop revenue management as a sustainable core competency with full integration of both strategic and tactical skills. The diagram below depicts this iterative business process as developed and trademarked under the name *REVRoadMap®*.

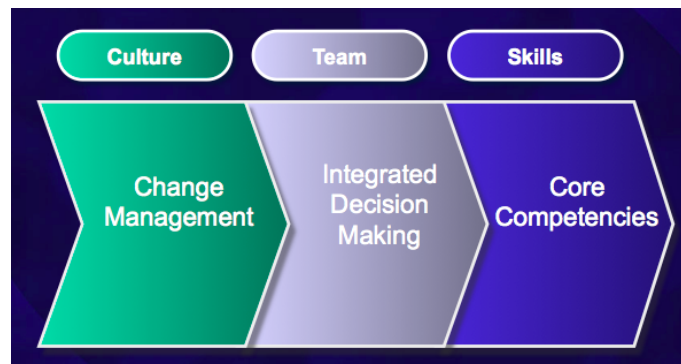


Even with a fundamentally holistic approach to revenue management as *REVRoadMap®* provides, there is often chronic disconnect between demand creation, demand capture and demand management. This is due largely to the manner in which consumer buying behavior is evolving and the extraordinary impact of the Internet. Without a fully holistic approach to revenue management, hotels are unable to optimize demand. Today, a hotel must pay equal attention to all segments of business and deploy a truly collaborative, synergistic approach to the relationship between *marketing, sales and operations*. This includes a carefully blended emphasis on the customer, the competition, the market, and the electronic playing field. Converging these disciplines is key.



By paying attention to these new synergies, hotels and resorts can significantly improve their overall revenue management efforts. The core methodology is the treatment of revenue management as a process-driven discipline, with the underlying premise to strive for incremental improvement by introducing revenue management fundamentals one step at a time and then revisiting each component regularly.

In addition, at each stage the hotel must address development in three distinct areas. In a word, these are the building blocks of a successful revenue management program. They include culture, teamwork and skills. A successful revenue management program must advance in all three areas if revenue maximization is to be achieved. Experience shows the most challenging 'building block' is the change management piece. Although teams can be built and skills developed, changing the way a hotel does business is a formidable challenge.



To do justice to a fully integrated revenue management program would go far beyond what this article can achieve in the time and space allotted. However, in an effort to illustrate key concepts here are examples from three of the six *REVRoadMap*® components: Product Alignment, Competitive Benchmarking and Strategic Pricing.

Product Alignment

Product alignment is a comprehensive process that defines markets so that customer needs can be assessed and product can be matched to meet those needs. Proper product alignment is vital as it plays a significant role in creating value for the product. Additionally, if done right it can set a hotel apart from the competition and provide a unique competitive advantage. The most significant part of a product alignment cycle is defining the end users' needs. It is important to remember that these needs are situational and change from market segment to market segment.

This component of the revenue management business process is all about aligning room categories to customer demand. Most hoteliers genuinely feel they have a good handle on product alignment. And yet the incidence of upgrading accommodation at check-in is endemic in the industry. Imagine walking into an Apple store ready to buy an 8-gigabyte iPhone and they say "I'm sorry we don't have any 8-gig iPhones in stock, but we'll give you a 16-gig phone for the same price". This would be a highly unlikely scenario.

In simpler terms product alignment is the practice of manipulating individual room type inventory based on demand. It's about how to increase the "absolute" value of inventory without impacting pricing integrity. It's also about tracking upgrades and calculating lost revenue, thereby identifying the true value of what's being forfeited. Product utilization acts as the acid test for a hotel's assumptions about user needs - if a hotel has appropriately matched product to various segments then utilization should be fairly balanced. In other words, room categories in the property management system should not show hugely negative figures as a result of un-checked "run of house" selling strategies. Clearly this is an indication that room types are not being fully leveraged.

There are innumerable strategies to combat the self-inflicted wounds of upgrading and one involves reevaluating the price/value relationship of room inventory. In revenue management terms this is called inventory stratification. The premise is to identify the price/value relationship of each room type and leverage this based on the guest's perception of value. It might be assumed that most hotels have perfectly fine-tuned product stratification, but more often than not there's either untapped value or an attempt to try to create value where none exists. Inevitably, room inventory is either over-stratified or under-stratified; that is, too many room categories or too few. A hotel with too few room types is missing opportunities to leverage more popular room product. One with too many is trying to leverage a room attribute that simply is not perceived by the guest as having any value. Below is an example of a hotel with too few room categories. Efforts were made to identify value from the guests' perspective, resulting in re-stratification of the room inventory.

Sample Inventory Stratification

Annual Occupancy: 80.00%

Current Stratification

	Room Type	Rack Rate	# RMS	Daily Revenue	Annual Revenue
1	SD - standard double room	\$125.00	46	\$4,600	\$1,679,000
2	SQ - standard queen bedded room	\$135.00	46	\$4,968	\$1,813,320
3	SK - standard king bedded room	\$145.00	46	\$5,336	\$1,947,640
4	DD - deluxe double bedded room	\$150.00	50	\$6,000	\$2,190,000
5	DQ - deluxe queen bedded room	\$160.00	50	\$6,400	\$2,336,000
6	DK - deluxe king bedded room	\$170.00	50	\$6,800	\$2,482,000
7	Suite - separate bedroom and parlour	\$225.00	12	\$2,160	\$788,400
	Totals		300	\$36,264	\$13,236,360

Identify Opportunities

- 1 The Front Desk staff say the Park View rooms are requested almost as much as the Harbour Side rooms.
- 2 The most popular rooms are on the higher floors.
- 3 We frequently run out of rooms with balconies.
- 4 Business people usually ask for the deluxe rooms, therefore a few extra business amenities have been added.
- 5 It is very difficult to find a summer weekend when the top floor suites are available. They are the very popular.
- 6 The various room types are spread throughout the hotel, they aren't divided into specific floors.

New Stratification

	Room Type	Rack Rate	# RMS	Daily Revenue	Annual Revenue
1	PVS - park view standard room	\$125.00	25	\$2,500	\$912,500
2	PVSB - park view standard room w/balcony	\$140.00	40	\$4,480	\$1,635,200
3	HVS - harbor view standard room	\$155.00	47	\$5,828	\$2,127,220
4	HVSB - harbor view standard room w/balcony	\$170.00	26	\$3,536	\$1,290,640
5	PVE - park view executive room	\$150.00	46	\$5,520	\$2,014,800
6	PVET - park view executive top floors	\$165.00	32	\$4,224	\$1,541,760
7	HVE - harbor view executive room	\$180.00	40	\$5,760	\$2,102,400
8	HVET - harbor view executive room top floors	\$195.00	32	\$4,992	\$1,822,080
9	1BPV - park view suite	\$225.00	4	\$720	\$262,800
10	1BPVB - park view suite w/balcony	\$255.00	4	\$816	\$297,840
11	1BHE - harbor view suite w/balcony	\$285.00	4	\$912	\$332,880
	Totals		300	\$39,288	\$14,340,120

Current Stratification Total Annual Revenue Potential	\$13,236,360
New Stratification Total Annual Revenue Potential	\$14,340,120
Revenue Variance	\$1,103,760
% Variance	8.34%

In this example, the absolute value of the room inventory increased by 8.34% or \$1.1M, simply by recognizing that the park view was popular and guests were willing to pay more to be on that side of the building. As a city-center property, this hotel did not believe the park view could be leveraged because the park was relatively small and definitely not a landmark. But when front desk agents were asked about which rooms were popular and why, the hidden popularity of the park view was revealed.

The reverse of this scenario is over-stratification, where a hotel attempts to leverage a room category with a questionable value proposition. For example, a hotel that charges more for the higher floors, but finds this to

be a constant source of negative guest feedback. In this scenario, the hotel adds breakfast, increases the price, and sells the room category with ease.

These initiatives seem simple and more common sense than strategic. But hotels often miss out on the “hidden revenue” in room product. A good way to detect revenue opportunities is to look at RevPAR by room type. Too few hoteliers pay sufficient attention to this metric even though the data is readily available in most property management systems. Using this data to optimize consumer demand is a very effective revenue management tactic. A low room type RevPAR is the surest sign of a value proposition out of alignment. And for branded hotels that offer upgrades to preferred guests as a policy, establishing a solid value proposition, selling the room category for what it's worth, and then having fewer higher category rooms available at check-in time can mitigate revenue losses. Hotels that don't believe they are leaving money on the table should track the value of upgrades for a period of time. The resultant revenue leakage is likely to be significant, far more than expected.

Competitive Benchmarking

Competitive benchmarking as a process is about making objective comparisons to other organizations. It is also about implementing strategies that will enhance the hotel's competitive position including not only to price, but also providing the impetus to improve products and services.

Deciding on the appropriate competitive set is critical because it ultimately plays a role in how the product is positioned. If the hotel is targeting the same guest as the other hotels in the competitive set, current market conditions and how these properties react to these conditions will impact how and what product and rates are sold. The incorrect competitive set could mean a hotel is constantly underselling its product leaving money on the table from guests who would have paid more; or turning away business because the other hotels are perceived as better value for similar rates. In either case, the property is not optimizing revenues and using erroneous market assumptions to drive strategies.

Inappropriate competitive sets make virtually all market intelligence reports worthless. The primary reason to look at any competitive set is to better predict both channel and segment rate thresholds. The best indication of who true competitors are is by asking guests where they would have stayed if the hotel could not accommodate them; or asking top producing clients which other properties in a particular category are the most popular for their customers. Tracking rate positioning in various channels also helps to better define these thresholds.

How a competitive set is defined varies significantly from one Hotel Company to another. Variables that need to be considered include: location, size, market segments served, brand/independent, quality of product & service, shared major accounts, and price positioning. It's not uncommon for a hotel or resort to track more than one competitive set. It's also not unusual for hotels to benchmark performance against the wrong competitive set. There are many reasons why this might be the case – including wishful thinking by ownership interests – i.e. allowing ego-driven competitive set choices. An unfortunate fact, based on our extensive consulting experience, is that up to 50% of hotels are benchmarking against the wrong competitive set.

In choosing a competitive set, the hotel must be realistic in terms of how it competes in the marketplace. If market penetration indices are considerably above or below 100%, or widely out of balance, these could be indications that the competitive set has not been chosen properly. Since so many strategic and tactical decisions are made based on market share results, it stands to reason that accurate competitive benchmarking is a crucial part of RM strategies.

In hospitality there are three major types of benchmarking commonly used:

1. **Process benchmarking** compares procedures and processes. Its purpose is to determine how the competitor achieves superior results in areas like customer service, innovative product offerings, etc. An extraordinary competitive benchmarking example is noted in a 1996 publication (*Source: Patterson, J. 1996, Benchmarking Basics, Looking for a Better Way, Crisp Publications Inc., California*). Apparently the German army compared the way they moved their people, horses, ammunition, food and setup tents with an American circus. It's almost inconceivable that the powerful German Army compared itself to a circus.
2. **Performance benchmarking** compares performance measurements – the Smith Travel Research market share reports are a good example of a commonly used performance-benchmarking tool. In this instance, specific measurement categories are determined in advanced and tracked over time.
3. **Strategic benchmarking** examines business fundamentals. This process looks at how a business is defined – for example who are the target customers? What needs of the customer are being served? What resources and skills are used to serve the customer better? How are products and services provided? The traditional SWOT analysis (Strengths, Weaknesses, Opportunities & Threats) falls into this category.

Most hotels use a combination of all of these benchmarking methodologies when comparing to the competition. However, hotels often do not distinguish between the three methodologies, which would be helpful, as it would provide a more structured framework in which to conduct comprehensive competitive benchmarking.

The key to fundamentally sound benchmarking is to take subjective opinions and intangible variables and translate them into quantifiable scores. This process begins with establishing a position or baseline against which competitors are rated. From this point competitors are scored based on being equal to, better than or worse than the subject hotel. Using a scoring scale of -3 to +3, this process results in a quantitative evaluation of product variables customized to the hotel.

A simple benchmarking example is noted below. The subject hotel is positioned at zero, which establishes a baseline. Then based on the research done, each competitor is rated in several separate categories or variables. In this example, quality variables are noted on the left (such as quality of service & curb appeal), and respective scores on the right. Hotel revenue management team members should complete the analysis individually then compare results so that inherent biases can be taken into consideration and corrected.

Sample Competitive Benchmarking

Competitive Set

Your Hotel Ranking	Quality Variables	Comp. 1	Comp. 2	Comp. 3	Comp. 4	Comp. 5
0	Quality of location	0	1	-2	1	3
0	Curb appeal	3	1	-3	1	2
0	Hotel accessibility	0	0	0	1	2
0	Quality of guest service	1	1	0	3	-1
0	Overall professionalism	1	1	-2	3	-1
0	Friendliness of staff	1	2	-1	3	-2
0	Impression of décor	0	0	1	0	1
0	Uniforming of staff	0	-1	0	1	2

In addition, 'distinct advantage' variables should also be identified and rated. These include areas that are unique to a hotel that go beyond the physical product such as corporate and regional advantages, like the existence of a corporate level sales force, etc. This is an advantage that most guests wouldn't notice, but is

still an important factor in evaluating the competitive environment. The diagram below shows some typical 'distinct advantage' variables.

Your Hotel Ranking	Distinct Advantage Variables	Comp. 1	Comp. 2	Comp. 3	Comp. 4	Comp. 5
265	Number of guest rooms	250	325	219	207	360
0	Variety of suites	-1	1	-3	0	-2
0	Meeting room capacity & variety	1	0	-3	3	1
0	Size of ballroom	2	3	1	-3	2
0	Aggressive catering team	0	1	1	-1	1
0	General Manager community involvement	-1	0	0	2	-1
0	Community perception of hotel	0	1	0	1	2
0	Guest recognition program	2	0	1	-3	2

By combining the scores of both the quality and distinct advantage variables (see example below), an aggregate score is created and a ranking established. A closely matched competitive set typically ranges from -10 to +10, but every hotel is different and the correct range must be determined individually. However, huge differences are a sign the competitive set may not be realistic. In the example below Competitor #2 has a combined score of +24. The question to be addressed is whether this hotel really belongs in the competitive set or not. The hotel should revisit the set choices and identify a reasonable range that fits that unique competitive environment.

Your Hotel	Aggregate Scores (Quality & Distinct Advantage)					
0	Total Quality Score	4	18	-3	21	7
0	Total Distinct Advantage Score	2	6	-1	-3	3
0	Combined Score	6	24	-4	18	10
5	Overall Competitive Set Ranking	4	1	6	2	3

By quantifying the competitive research, it is much easier to establish a ranking and to objectively evaluate the subject hotel's position in the market place. Translating intangible quality variables into a quantifiable format produces actionable data.

As benchmarking practices evolve, social media is having a profound impact. The use of reputation management market intelligence is becoming more and more common. Hotels are carefully monitoring online chatter and starting to benchmark guest experience against similar hotels. Now that confidential third parties are gathering data, traditional guest comment card feedback categories (rooms, housekeeping, dining, staff, value, etc.) can be benchmarked. As traditional competitive benchmarking makes room for new evaluation trends, the measurements might well be distinguished as 'soft metrics' and 'hard metrics'. Below is an example of how these metrics might be delineated:

HARD METRICS	SOFT METRICS
Annual budget	Competitor popularity rating/ranking
Last year	TripAdvisor rating/ranking/categories
Forecast	OTA & other peer review ratings/rankings
Market share	# Facebook fans
GDS share	# Twitter followers/tweets/retweets
OTA share	# Photos and/or videos shared
Divisional profit	# Blogs/bookmarks
EBITDA	# Foursquare venue stats

The use of reputation management market intelligence to benchmark against similar hotels (example: mid-scale full service hotels) will soon eclipse traditional guest comment card feedback and hotels will continue to disaggregate this data to access drill-down benchmarking metrics across all categories of feedback, comparing their performance to their competitive set(s). The practice of comparing market share improvement to social media metrics will also become commonplace. Social media is adding a new dimension to benchmarking with the consumer fully engaged in the process.

Strategic Pricing

Hotels are constantly looking for better ways to deal with predatory pricing and generally imprudent competitive pricing tactics. Strategically changing business mix and tactically “doing the math” before resorting to price reductions is the first line of attack. Nevertheless, price as a primary strategic weapon prevails in virtually every market. But there are options for hoteliers embroiled in price war battles that are far less damaging than dropping price.

First, there’s a big difference between dropping price and lowering average daily rate (ADR). A shift in business mix might very well dilute the ADR when no prices are changed (or dropped) at all. Certainly a shift in mix is a traditional strategy that hoteliers have used for years. Perhaps the most common is a hotel that decides to take an airline crew to establish base business when in ‘good times’ crew business would not be accepted. But this is an obvious example of long-term strategic business mix manipulation, thought out and executed well in advance. To complement this strategy a hotel must also identify medium-term strategic solutions and short-term tactical solutions to price wars.

This process must begin by asking the right questions; before dropping price a hotel must find the answers to these questions:

- Is the hotel detecting rate resistance?
- Are prices comparing similar products (apples to apples)? Market intelligence reports compare price-to-price – not product-to-product.
- Is the price point being considered attracting the right customer?
- Where does the customer position the hotel?
- Where does hotel staff think the price point should be?
- Does the competitor’s price make sense?
- Is the hotel tracking turndowns and denials?
- Has a break-even analysis been conducted to determine if a lower price is viable?

With the ever-increasing percentage of online hotel bookings it’s difficult to get an accurate read on the level of rate resistance; but many hotels have this data from central reservation systems and or property management systems. At the very least, a low-tech reservation-tracking sheet helps to gauge resistance. In the example below, it’s interesting to note that business is not being turned away because the hotel is sold out, but rather for a myriad of other reasons (stay controls, room type availability, and rate resistance).

Sample Daily Reservation Call Tracking Sheet

Month: November
Year: 2010

Today's Date: 20-Oct-10

Agent Name: Susan

Day	Date	Denied due to Stay Control	Denied due to Rate Resistance	Denied due to Rm. Type not Avail.	Denied due to Sold Out
Mon	1				
Tue	2				
Wed	3				
Thu	4		//		
Fri	5		//	/	
Sat	6		//	//	
Sun	7		/	/	
Mon	8		///		
Tue	9		///		
Wed	10		////		
Thu	11		//		
Fri	12		/	//	
Sat	13	////	/	//	
Sun	14				
Mon	15				

Total Calls	
///// ///// ///// ///// ///// ///// ////	
Total	48

Non Revenue Generating Calls	
///// ///// ///// //	
Total	21

If price resistance is in fact the problem, then the first choice is to add value before dropping price. The next is to ensure that any promotional rate is fenced properly. Fences are simply tactics applied to rates to prevent one segment of demand from buying down into the next. In broad terms there are 4 types of fences:

1. **Product** – example: limit the offer to certain room types
2. **Availability** – example: offer better deals on longer stays (pay for 5 nights, stay 7, etc.)
3. **Customer** – example: limit the offer to repeat guests as a reward
4. **Transaction** – example: a restricted booking window for a stay taking place over a specific period of time

Successful promotional specials that do not create huge trade-down are those that are fenced appropriately.

If adding value and offering well-fenced promotions still produces insufficient results, price positioning may be the only option. But before engaging in this dangerous option it's vital that a break-even analysis be conducted. This is simply a calculation of how much incremental revenue and room nights must be generated in order for the price reduction to be beneficial. If, for example, an online travel agency representative suggests a lower price to drive volume, exactly how many additional room nights must be generated? Below are three examples of break-even analysis based on three very different hotels.

Scenario	2-Star Hotel	3-Star Hotel	4-Star Hotel
Current level of room nights sold	315	315	315
Current price	\$89	\$139	\$239
Reduced price	\$74	\$99	\$169
% Discount	16.9%	28.8%	29.3%
Dollar difference customer sees	\$15	\$40	\$70
Revenue needed to break-even	\$28,035	\$43,785	\$75,285
Total rooms sold @ new price to break even	379	442	445
Incremental room nights needed	64	127	130
% Increment rooms to break even in revenue	20.3%	40.4%	41.4%
Estimated variable cost	\$15	\$30	\$35
Profit per room before	\$74	\$109	\$204
Profit per room after	\$59	\$69	\$134
Profit needed to break even	\$23,310	\$34,335	\$64,260
Units needed to break even in profit	395	498	480
% Incremental "units" to break even in profit	25.4%	58.0%	52.2%

The hotel must ask the question of whether the price drop will generate this much incremental business. The next step is to consider profitability, not just top-line revenue. In these examples the level of incremental room nights required to break even in profit ranges from a low of 25.4% to a high of 58.0%. It is rare, if not totally unlikely, that an online travel agency representative is going to guarantee this level of incremental business.

The next question is what if the hotel does nothing? What if prices were held firm even at the expense of volume? How much could the hotel afford to lose? If, for example, the hotel sees volume drop by 5% in this market segment, there will of course be an impact on profitability but other factors must be taken into consideration. Industrial psychologists say it takes a 30% discount to influence a buy. None of the price adjustment scenarios noted above offers discounts at the 30% level. Conversely, dropping price offers much greater risk in other factors:

- Increases sales quickly but at a much higher risk – providing short-term gain, but long-term damage
- Generates higher costs with less revenue
- Offers lower rates than the guest is already willing to pay (trade-down)
- Is likely to illicit a competitor's response
- Makes comebacks harder (after 9/11 it took most markets 5 to 6 years to get average rates back up to pre 9/11 levels; building average rates following the Great Recession is proving even more formidable).

Finally, and most importantly, research indicates discounting in the hotel business does not increase volume as much as it decreases revenues. In the end, the hotelier must ask the right questions, add value where possible and manage promotions with logical and effective fences. As a last measure, the use of break-even analysis reveals the reality of price reductions.

Bonnie Buckhiester is the President of Buckhiester Management Limited, a leading Revenue Management consulting and developmental training firm. In the past, she has held several important positions in hospitality and tourism such as Senior Vice President Operations for a major North American hotel REIT, General Manager for two 4½-diamond hotels, and General Manager Operations for a major tour operator.