Revenue management techniques in hospitality industry – essay

Business

Introduction to Hospitality Industry The hospitality industry is part of a larger enterprise known as the travel and tourism industry.

It is one of the oldest industries in the world. In early days, traders, explorers, missionaries and pilgrims needed a break in their journeys requiring food, shelter and rest. People opened their homes and kitchens to these weary travellers, and an industry was born. Although accommodation today is varied and their services have changed and expanded over the ages, one thing about the hospitality industry has remained the same, guests are always welcome! From a friendly greeting at the door, room service, breakfast, to a host of facilities' the hospitality industry offers travellers a home away from home.

Hospitality is defined as " the friendly reception and treatment of strangers". For most people, hospitality means entertaining guests with courtesy and warmth. Hospitality is also an industry made up of businesses that provide lodging, food and other services to travellers. The main components of this industry are hotels, motels, inns, resorts and Restaurants. In a broad sense, the hospitality industry might refer to any group engaged in tourism, entertainment, transportation or lodging including cruise lines, airlines, railways, car rental companies and tour operators. However the two main segments are the lodging industry also called the hotel industry, and the food and beverage industry, also called the restaurant industry. The lodging industry is made up of businesses providing temporary housing, and such a business is called a lodging establishment and the people who stay in it are called guests or clients. What is Revenue Management? Revenue

Management is a technique to optimize the revenue earned from a fixed, perishable resource.

The challenge is to sell the right resources to the right customer at the right time. Revenue Management implements the basic principles of supply and demand economics in a tactical way to generate incremental revenues. There are three essential conditions for revenue management to be applicable: • That there is a fixed amount of resources available for sale. • That the resources sold are perishable. This means that there is a time limit to selling the resources, after which they cease to be of value.

• That different customers are willing to pay a different price for using the same amount of resources. Revenue Management is of especially high relevance in cases where the constant costs are relatively high compared to the variable costs. The less variable costs there are, the more the additional revenue earned will contribute to the overall profit. To illustate this, we can take the example of the luxury hotel which charges different prices for different customers. In India it is generally practiced in star hotels to maximise the revenues. the customer who is price sensitive and time conscious generally pays lesser tariffs than a customer who is willing to pay more and books the room one or two days before the stay.

Revenue Management in other words tries to maximise revenues by managing the tradeoff between a low occupancy and higher room rate senario (business customers) versus a high occupancy and lower room rate (vacation customers). IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17

May 2008, IIMK 271 Robert Cross, Revenue Management, Hard Core Tactics for Market Domination How does Revenue Management work? Identify the market segments: A Market Segmenting a market Price Price Market Segmentation Qty Sold Qty Sold Hotels should identify the type of customers and the price they are willing to pay for utilising the service. This can be done on the basis of the following parameters. Physical characteristics High Price Low priceView Pool view, ocean view, hill view Non scenic view Size Bigger rooms with more facilities Small rooms with few facilities Temporal Weekday bookings Weekend bookings Logical Fences Length of stay Short stay. One or two days. Longer stay.

Flexibility Cancellations and rescheduling are allowed at a low penalty. High penalty for cancellation and schedule change Time of purchase Bookings are made very close to date Bookings are made quite early Privileges Are rewarded loyalty privileges No privileges Size of Business provided Corporate business customers booking frequently Self funding vacationers booking rarelyPoint of sale Phisical delivery and confirmations By email or phone. Changing Demand over Time eg. Perishable Products Demand Segment 1 S2 S3 Time IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 272 Demand forecasting: Pricing and demand are inter-related and need to be coordinated. In the hospitality industry, demand for a room is cyclic in nature and follows a trend. Revenue management models help pinpoint demand by minimising uncertainity and producing the best possible forecast. Allocation: the revenue management also puts light on the allocation of inventory (hotel rooms) among different segments. For example , if a hotel has two price categories of rooms, say Rs.

4500 and Rs. 6000. Since the pricing is different for the two rooms, these rooms are each targeted at a different customer set. Based on the historical preference pattern of customers in each segment, it would be possible to estimate the number of customers who would be willing to pabuy these rooms at a given price with a reasonable variance. For example, an average 50 customers may be willing to pay Rs. 000 for some rooms, but it could also mean that the actual number of customers who turn up for Rs. 6000 could be 60 or even 40 with some probability, or 80 or 30 with a lesser probability.

Two Prices: Two Market Segments Price P1 P2 Q1 Q2 Quantity Supplied Overbooking: Overbooking is a practice of intentionally selling more rooms than available in order to offset the effect of cancellations. For example, suppose in the hotel industry, there are 180 rooms available, there is no certainity that all the rooms would be booed at a point of time. In the same way, during the season, there is a possibility of over booking. Therefore if the booking is done 181 customers instead of 180, the hotel may end up with only 173 or less than 180 customers. since the probability of exactly 181 customers turning up is low, the revenue from that aditional customer generally compensates more than the expected cost. For this example, the optimal number of customers that can be booked would be 186 as illustrated in the following figure. Overbooking: Determining the optimal level Revenue Revenue Gain Net Revenue Sales Revenue Overbooking cost Capacity Overbook QtyIIMK Part VII – Tourism Infrastructure, Technology & Operations

IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 273 Revenue Management as a Business Process Classification of Hotels Hotels are classified into five main types: • Economy / limited -service hotels • Mid-market hotels • All-suite hotels • First class or executive hotels • Luxury or deluxe hotels For the purpose of our research, Economy and Executive hotels are selected.

Normally hotels have four rate categories: (1) Rack rates, (2) Group and tour rates, (3) Special and promotional rates and (4) package rates. (1) Rack rates are normal room rates. It is based on the category of the room, type of bedding and occupancy.

Unless specified, guests are quoted the rack rates and are charged for the same. (2) Group and Tour rates are a discounted room rate for an organisation, which has blocked a large number of rooms. Most hotels have group rates that are lower than the rack rates. This rate is generally extended to a trade association or fraternal organisation that has scheduled a meeting, seminar or conference at the hotel. Discounts are also offered to a tour operator, in return for a commitment to purchase a minimum number of rooms over a given period of time. 3) Special and promotional rates are offered to corporate travellers, traveling sales representatives, military personnel, airlines staff or other regular clients.

Some times special rates are also offered along with an advertising campaign or to promote the hotel during lean periods. (4) Package rates are offered to the public along with other services such as banquet or a ball, or recreational facilities or a special event. Such a package normally includes accommodation, tickets to the concerned event and transportation from hotel to the venue and back. Other popular packages offered by hotels are honeymoon, weekend, Christmas, New Year or any other sports activity. The package rate is normally lower than the combined component or rack rate. Product Definition Competitive Benchmarkin g Strategic Pricing Demand Forecasting Distribution Managemen t Business Mix Manipulatio n IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 274 Analysis of star and economy hotels on the basis of tariff plans: Five Star hotels: Name and location Single Occupancy Double OccupancyFacilities (Room and Breakfast) Hotel Marine Plaza, Superior 11, 000 12, 000 Marine Drive Executive 12, 000 13, 000 Restaurants, conference rooms, swimming pool etc. Holiday Inn Superior 8, 800 11, 600 Executive 16, 000 20, 000 Same as above Hotel Sun and Sand Superior 8000 8500 Same as above Executive 12000 12000 Hotel Sea Princess, Juhu Superior 4500 5250 Same as above Executive 9500 13, 500 Ramada Palm Grove Superior 6000 7000 Same as above Executive 8000 9000 Economy Hotels: Single occupancy Double occupancy Hotel Highway Residency, Andheri 2350 2550 Hotel Amigo, Mumbai 2450 2550 Hotel Bentleys, Colaba 2000 2200From the above table it can be analysed that star hotels maximise their revenues throuh differential pricing strategies and by targeting different customers whereas Economy hotels Target at the right customers by charging the fixed prices. From this we can conclude that the occupancy rates are highest in the case of Economy hotels compared with the star hotels.

This is more clear through the case study. IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 275 A Case study on Bentleys Hotel (Economy) and Hotel GodwinHotel Bentleys, Colaba (Economy hotel) Bentley's is one of Mumbai's (formerly known as Bombay, India) best budget tourist hotels. It is highly rated in most Tourist / Traveller's Guides, including The Lonely Planet. Ideally situated in South Mumbai, it is in the heart of the downtown area, close to the business, entertainment and shopping areas.

The hotel has a clean, quiet, comfortable and homely atmosphere. Most rooms are deliberately maintained in the old Victorian ambiance. The hotel gets 95% of its customers as foreign tourists. The occupancy rate in this hostel is 110%. The rooms are occupied for the 365 days in this year.

Demand is more than Supply in this hotel. The customers are not provided with any food in this hotel. The hotel does not practice differential pricing for its customers. It charges single price for all of its customers irrespective of different nationality. Tourists generally would like to stay in this hotel for the wonderful service provided by the hotel.

Generally the hotel gets repeated customers and the customer loyalty is very good over here. Marketing Strategies adopted by the hotel to attract more tourists: • Reservation is done directly without the help of middleman like travel agents. • Hotel provides prompt service to the enquiries of the customers mails. Usually the queries are answered within an hour. • The services provided by the housekeepers are also very good. They are excellent in communication and they meet the customer demand promptly.

• Generally in this hotel, 80% of the customers are repeated which means there is customer loyalty to the maximum extent. • Usually the hotels provide one room to one customer in a day. But Bentleys uses its perishable capacity 3 times a day for the purpose of maximizing the revenue. Hotel Godwin, Colaba (Three Star hotel) The hotel has been accredited as a 3 star hotel and is situated in colaba. They find most of their customers from Gulf. HOTEL GODWIN, a 3 Star Hotel with 52 rooms has been serving the travelers and business community for well over 30 years and from the testimonials of its patrons, both Indian and Foreign, it is considered a real HOME AWAY FROM HOME. HOTEL GODWIN occupies an ideal location from the point of view of businessmen and tourists. Adjacent to Colaba Causeway, the fashionable shopping centre in South Mumbai, it is close to the tourists attractions like the Gateway of India; Museum, the business centers of Flora Fountain, Churchgate Reclamation and Nariman Point, Offices of National & International Airlines, and headquarters of both the main Railway line close by.

Prominent Clubs, Cinemas & Restaurants are near by. • They get the customers through travel agents in Mumbai and the other parts of India. • The average occupancy rate is 60% • Most of the customers are tourists.

• To get more customers they provide discounts in the off-season. They charge different tariff to different customers. • Usually they get repeated customers. • They do overbook the rooms to maximize the revenues. • There are 65 employees in the hotel.

Revenue management Strategies adopted by the hotels Findings • It is believed that the hotels, which are functioning at the large scale, are good in revenue management and they apply most advanced techniques to manage their revenues. But through this research on star and economy hotels, it can be said that the star hotels provide the state of the art facilities and services to the customers and very hygiene food to the customers. But when it comes to the occupancy rates measure in terms of foreign tourists, the economy hotels are exceedingly doing well. • The star hotels attract more business class customers by providing good and efficient services to them. The supply is more than demand in case of star hotels. • Economy Hotels give importance to the cultural values of the country. • The concept of overbooking is followed in both kinds of hotels.

IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 276 • The market segmentation is not there in case of economy hotels. But it is practiced in star hotels. • In both type of hotels the maximum number of customers are tourists. • Rooms are booked directly through internet by the customers in case of economy hotels and indirectly through the travel agents in case of star hotels. • Economy hotels do not practice revenue management techniques neither through its differential pricing nor through market segmentation. They just manage their revenues by applying the concept of logical booking. This can be seen by the following table.

Economy hotels: (revenue earned if given to a single person) Check In & out 12 noon. Therefore profit per day on a single room = Rs. 6000 Star Hotels:

check in & out 12 noon. (Revenue earned if given to a single person) Occupancy Check in Check out Tariff for a single person Revenue per day 1 12 Noon 12 noon Rs 4500 Rs 4500 Therefore profit per day on a single room= Rs. 4500 From the above table it can be analyzed that the revenue management styles of the different hotels are different. Economy hotels book the rooms on the basis of the check in and check out timings of the tourists and go for maximum utilization of the Resources.

Basic formulas applied by the hotels to calculate the revenue and room rates: Calculation of total revenue on the basis of the above formula: Available No. of rooms Occupancy percentage No. of days in the year Total Revenue Average Room Rate Star hotel (Hotel Godwin) 60% 365 Rs. 40541280 Rs.

3560 Economy Hotel (Hotel Bentley's) 110% 365 Rs. 29711000 Rs 2000 If one room is occupied thrice a day, then the economy hotel can have maximum revenue compared to that of the star hotels. The calculation is as follows.

Economy Hotel (Hotel Bentley's) 110% 365 Rs. 89133000 Rs. 6000 Challenges or problems in Revenue managementThe revenue management techniques and the models of overbooking if applied aptly would definitely maximize the revenues of the hospitality industry. But there are some hindrances that the hotels have to overcome. They are given below: • Measuring performance of an RM system is a major issue. Occupancy rates and yield are measures that are affected by external competition. Therefore an ideal measurement can be done using the opportunity model. I.

e. , if the hotel segments the market and fixes different rates for different customers, then it has to see that the revenue is generated from those rooms and it has to be utilized ideally. Occupancy Check in Check out Tariff for a single person Revenue per day 1 5 AM 12 Noon Rs 2000 Rs 2000 2 2 PM 7 PM Rs 2000 Rs. 4000 3 8PM 12Noon next day Rs 2000 Rs. 6000 IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 277 • Some customers do not like the practice of differential pricing.

In evaluating the efficiency of RM system, the trade off between generating short-term profits and creating long-term customer loyalty needs to be studied carefully. Revenue management can have impact on the motivational level of the employees. Revenue Strategy The objective of a revenue strategy is to capture the optimal profitability that can be produced from the projected demand. Interdepartmental Integration which helps in achieving the revenue strategies Conclusion From the research paper and findings, it can be concluded that the future of revenue management will evolve the following aspects: One-to-one Revenue Management • Sophisticated hotels will evolve to one-to-one revenue management; each individual will be a market segment in themselves In the future, technology will support calculating the total customer value and the potential total customer spend, based on history and future potential from demographics, to determine what rate and what availability to offer to a potential guest Total Customer Value Integration • The future of revenue management will include a focus on the Revenue Per Available Guest (RevPAG) and total customer value • The next generation of revenue management systems will create an offer based on the value of, or potential value of, each individual customer Function Room Yield Forecasting and yielding of function space will be a focus in the future for hotels • Many large hotel companies and revenue management systems are working to develop effective models in this area. Cost of Business Analysis • Different revenue streams and channels do not yield the same profit, even when the rate is exactly the same Revenue Management Service Delivery Sales & Marketing IIMK Part VII – Tourism Infrastructure, Technology & Operations IIML Conference on Tourism in India – Challenges Ahead, 15-17 May 2008, IIMK 278 • In the future, channel cost will be incorporated into rate and inventory decisions for each channel individuallyGoal Alignment • The goals of the entire hotel team, from property level to corporate, will need to be aligned in order for revenue management to reach its fullest potential. Automation • There is a gap between the sophistication of the revenue management practice and the technology available to support it • We need to adopt the new technologies as they are available and use our minds to manipulate them expertly to achieve ultimate success In short, the main aim of revenue management makes the following things possible • Ensures a systematic approach • Ensures pricing and rate integrity Values sound inventory management • Establishes a solid distribution network • Recognizes total lifetime value of business • Recognizes superior service experiences affecting profitability. Acknowledgements Manager of Bentleys Hotel, Colaba, Mumbai Manager of Hotel Godwin, Colaba, Mumbai References Defining Revenue Management-Barb Bowden Peabody Hotels Front Office Operations – by Michael Casavana.

Karvy Consultant Services. www. karvyglobal. com Maharashtra Tourism and Development Corporation Principles of Hotel Front Office Operations – by Sue Baker, Pam Bradley & Jeremy Huyton