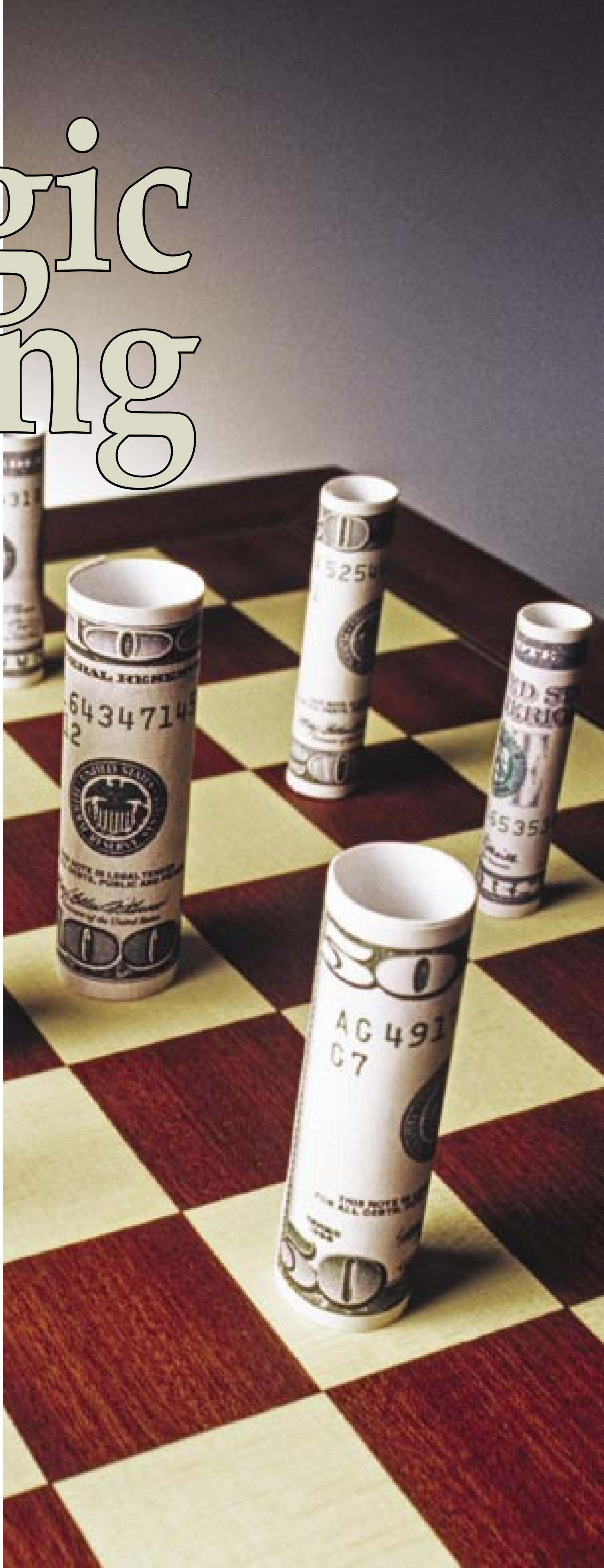
strategic pricing

new rules for an age-old game

by Victoria Edwards



I once worked for a General Manager who would frequently comment that "nothing has changed in the hotel industry since there was no room at the Inn in Bethlehem."

For the most part, I whole-heartedly agreed with him. And then something happened – the Internet. As a totally new and unique way of distributing inventory, the public access to GDS information and onward distribution highlighted our industry's two weaknesses regarding revenue management – demand forecasting and strategic pricing.

As an industry, we are aware of the benefits of optimizing revenues through various rate offerings. However, most hoteliers continue to focus on tactical pricing at the expense of strategic pricing. All aspects of revenue management have both tactical and strategic implications, the tactical being a much more short-term, action-oriented approach and the strategic encapsulating the big picture. All too often ownership demands or budget shortfalls push us to make decisions for short-term gain that have long-term pain associated with them.

The business process involved in pricing perishable hotel rooms should include the following six key considerations. If you can answer yes to all of these questions, you are well on your way to optimizing your pricing structure for your hotel.

1. Are your indexes balanced? In order for hotels to assess whether or not they are pricing themselves appropriately, they must be able to look at some form of external performance measurement. For some hotels this may be an informal market share report where the sales department collects competitors' month-end occupancy and ADR statistics. For most hotels in North America, these performance measurements come by way of the STR report from Smith Travel Research. Your indexes enable you to see how well you performed relative to your competition. If you are over 100%, you received at least your fair share of occupancy, rate, or RevPAR, depending on which index you are reviewing. Anything under 100% and your competition stole occupancy, rate or overall RevPAR from you. Balancing your indexes is important since it indicates whether or not you played the opportunities in the marketplace to your full advantage. As a general rule of thumb, your occupancy and rate indexes should not be more than 10 points apart. In other words, if you achieved a 119% occupancy index and a 101% ADR index, you left money on the table. You had guests who booked your hotel but would have paid more. Conversely, if you achieved a 109% ADR index and a 97.5% occupancy index, you turned business away to your competitors because your rate offering was above what guests were willing to pay.

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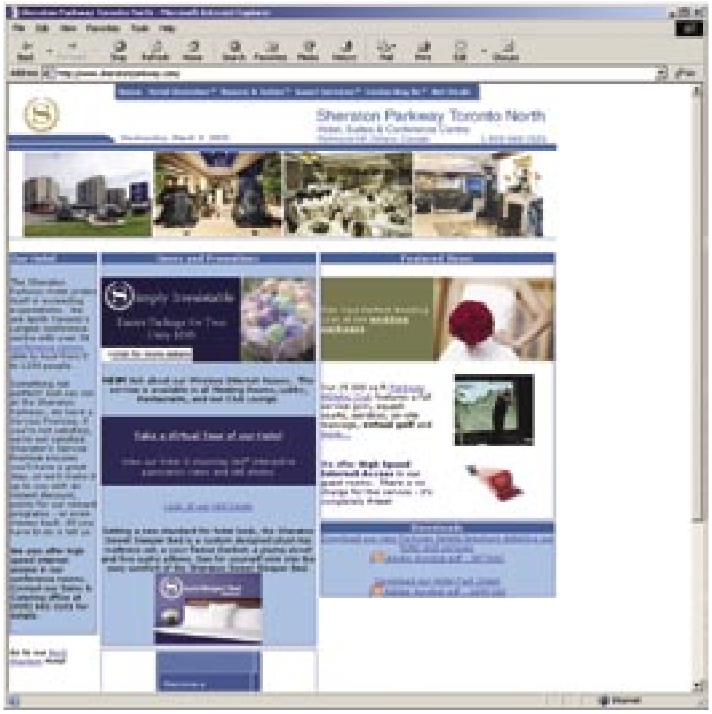
2. Are your prices positioned appropriately for your product? Ultimately, the guest is the one who decides the price. Every guest has a sense of the value of your product. They set this value based on your ability to fulfill their purchase needs and compared to available alternatives. In other words, what is your competition offering? This is the essence of market-driven pricing. It is critical that you understand exactly what your guests' needs are per segment and how your product answers those needs. Once that has been determined, look at your competitor's product and ask the same questions. You will then know where you should be positioning your rate.



3. Do you maintain rate integrity in all distribution channels? The buzz words that everyone has been talking about for the past couple of years are "rate parity." Do you have "rate parity" across channels? Most hoteliers have been lead to believe that rate parity means having exactly the same rate in all channels. But how can this possibly lead to rate integrity? If an online booker who has never stayed at your hotel can get exactly the same rate as consortia that produce significant volume at your property, how can you have rate integrity? The answer is – you don't have rate integrity.

Rate parity is about the exact same rate. Rate integrity is about value. In other words, rate integrity is about differentiating the value of your product across various channels through the use of appropriate fences. An effective pricing structure must be consistent, rational and include logical fences or added value.

The table below illustrates this point:

Channel	Rate	Fence
GDS	$129	Consortia only
3rd party Internet	$159	Pre-pay, no cancellation
CRO/In-house reservations	$169	Bfast, parking incl, 6pm cxl

4. Do your prices reflect current demand per segment? All demand is not created equal. Demand for your product can be divided into premium demand, retail demand & discount demand. Premium demand comes from a small section of your booking pool that is looking for a specific type

of product and is willing to pay more than the average market price. An example could be a couple on a honeymoon looking to book the best suite in the house. Retail demand comes from a relatively larger portion of the booking pool that wants certain product and service attributes at a fair and consistent price. The corporate market segment is a good example of retail demand. Finally, discount demand is made up of the bargain hunters who want a price that is below fair market value. Customers found at opaque sites are an example of discount demand.

Since all demand is not created equal, it is important to know exactly where your demand is coming from. If you do not know the source of your demand, you run the risk of having potential guests buy "down" into lower rate segments than they may have been willing to pay.

5. Do you measure rate response when you make changes? If you are going to change your rates, either by opening/closing certain rate types or by offering a new product such as a special/package, it is imperative that you measure rate response. How has your booking pace changed since the change? If you are converting a huge number of reservations, is the rate possibly too low? If your hotel is not tracking turn-downs then maybe the price is too high. Either way you are missing a piece of the pricing puzzle.

"Your pricing structure needs to be looked at from both a strategic and tactical perspective."

6. Do you consider contribution or profit per segment when setting your prices? Just as all demand is not created equal, different segments yield very different profit margins. Different distribution channels have different costs associated with them. Different segments have different product needs and, as such, the costs associated with servicing these products vary considerably.

The corporate segment usually requires reward points, complimentary local calls, free Internet access, books through a corporate travel services and uses a credit card to settle their account. The associated costs per room on corporate bookings tend to be quite high. I would encourage you to look at the net contribution per segment. You might be surprised to find that given your current pricing structure, your $109 tour room yields a better profit than a $149 corporate room. If this is the case, you may want to rethink your rates and your business mix.

Revenue management is a highly dynamic business process. Strategic pricing is one component of the process. Your pricing structure needs to be examined from both a strategic and tactical perspective. Finding the answers to the questions above will allow you to develop a consistent, structured value-based pricing model for your hotel.

Victoria Edwards is the vice-president strategic development for Buckhiester USA Inc., and the co-creator of REVolution™ a process-driven revenue management solutions product.