PTG CONSULTING℠

White Paper

Strategic Pricing in a Downturn Market

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Read Time: 15 min

Introduction

Hotel Pricing Strategy

This is one topic that is discussed over and over by hoteliers everywhere. Pricing is one of the most challenging strategies to get "right" — yet it plays a critical role in determining the success of the hotel.

There are many factors that go into setting your room rates, and there is no "one-way" to determine the optimal pricing. Most hotels begin by setting their retail pricing first and then deriving pricing for each segment based on the retail price. So what happens when hotels decide to discount their retail prices? How does this impact the segmentation pricing? What does this look like on an STR report? Can this change the consumer perception of the hotel?

My colleague, Michael Sherwood, has written this thought-provoking article exploring the topic of retail pricing and the holistic impact it has when hotels discount. Reading this, you will gain insight into how retail pricing discounts:

- impact the overall hotel pricing strategy
- change the consumer perception of a hotel's position in the market
- create a domino effect on hotel's business mix
- ultimately impact the hotel's profitability and bottom line

Additionally, Michael shares some common assumptions hoteliers make when reviewing the STR report and the critical revenue losses that can result from decisions based on these assumptions.

As a hotel owner, an operator, or anyone with input into revenue-related decisions for your hotel, or if you simply have an interest in learning more about strategic pricing, I strongly urge you to take 15 minutes to review this paper. I promise you will discover thought-provoking ideas for your next revenue meeting.

Kathleen Cullen
Senior Vice President
PTG Consulting

Setting Retail Prices During a Downturn: Decrease or Remain Steady

By Michael Sherwood
Vice President, Revenue Management Services
PTG Consulting

The hospitality industry has survived and thrived through varying degrees of economic boom and downturn over the past 30 years — from strong performance during the 1990s and mid-2000s and consistent improvement over the past eight years (2020 aside) to rapid drops caused by the Gulf War, 9/11, and plummeting ADR rates during and after the 2008 financial crash. Unlike these historical events, the COVID-19 pandemic has impacted the entire world concurrently, resulting in adverse effects throughout the travel industry, within every space and market globally, for a sustained and ongoing period.

Today, we take a more strategic approach to the practice of Revenue Management, more so than during the early 1990s and the post-9/11 period. When COVID-19 first began to have an impact on travel in early 2020, industry experts in countless articles and "best practice" webinars warned, "DO NOT lower rates."

> "Panic is highly contagious, especially in situations when nothing is known and everything is in flux."
> — Stephen King

Of course, faced with rapidly decreasing occupancy rates, our gut reaction (fear) takes over and we set aside lessons learned through strategy and patience. Factor in an STR report with a steep decline in Occupancy Index (MPI) and increased ADR Index (ARI), your competition dropping their room rates, and someone higher up the ladder telling you, "our rates are too high, we need to drop our price," the choice seems obvious. We lower the rates.

Retail Rates & the STR Report

What does retail pricing have to do with STR results? Everything.

A hotel's entire Rate Strategy is based on its retail pricing. However, it is critical to understand that the STR results are a representation of a much larger picture beyond just how retail pricing is set; they are a depiction of the hotel's overall mix of business health. Many factors go into the results of an STR report. One of the major considerations, often overlooked, is the mix of business. Evaluate the breakdown of segments for your hotel and your competitive set. Which segments are experiencing a decline in occupancy: Transient? Group? Contract? Is your competitive set's growth in these segments causing your MPI to decrease? A hotel might lose 10 points in Occupancy Index (MPI), decide to lower its retail price, and discover the decline was actually due to Group business lost from the previous year, or that the competitive set saw an increase only in Group business. In these circumstances, **a rash decision to modify pricing will result in a loss of rate and revenue opportunities.**

Now, what if the decline was in transient business? Maybe reduced production from a lower-rated negotiated account caused occupancy to decline and ADR to increase. Or a strategy was implemented to reduce the amount of lower-rated opaque business for the hotel, which would also have an impact on occupancy and ADR performance. The decline in MPI had nothing to do with retail pricing. Too often hotels make decisions to adjust retail pricing based on STR results without understanding the impact past decisions had on MPI. And of course, the same situations also apply to a hotel's competitive set.

> Shifts in a competitor's mix of business can also impact the results of your hotel's STR Report.

Should You Lower Prices?

During any downturn, there are declines in every column and row of the STR report, and the need to drive occupancy is even more important, especially considering the need for cash flow, but before you decide to lower retail pricing, ask yourself two questions.

1.

Does the customer know you are at 10% occupancy?

Likely not. Always keep in mind that you are selling an experience, and that experience has a perceived value. By lowering rates, the guests' perception of what type of experience you offer changes.

2.

How will a customer know your rates are lower?

Many times, a hotel will simply adjust its BAR rate on OTA channels and its own website. Let's assume the OTA channel's strong marketing presence drives incremental business by reaching new customers who don't book at your usual price point. You get the booking, but at a cost — the amount of the discount and the margin or commission. And the customer booking on your website? You originally captured them at a higher rate, but they booked at a lower price point. Did you receive a huge influx of bookings as a result of the retail price decrease? Maybe. But probably not.

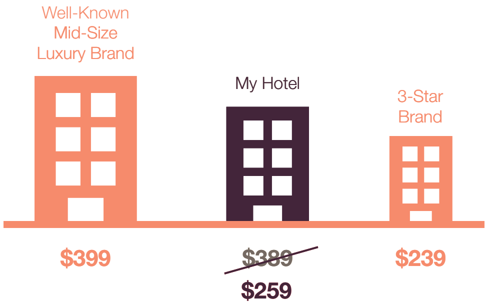
Lowering your price to build incremental business will likely not create a huge influx of bookings, and it is impossible to tell if customers booked because they already planned to or because you changed the perceived value of the experience.

Reality Vs. Perception

Let's take a look at the effects of lowering retail rates.

Price Positioning

Begin by completing a "Price Positioning" exercise, objectively evaluate the competitive landscape to identify your true competitors and understand where your hotel should be positioned in price, based on features, benefits, services, and amenities. Objectivity is key during this process. Center your analysis on how customers perceive your hotel (and its competitors), rather than on your own opinion. Understanding where you should be positioned, especially during a downturn, is critical for success.



Pricing Perception

This is even more important in the world of independent hotels. I like to use the following example in my Revenue Management Workshops to show the importance of price perception for independent hotels.

Assume "My Hotel" is a luxury independent hotel in a market full of branded hotels. The rate leader in the market is a well-known, mid-size luxury brand, priced at US$399/night. Most customers have a clear understanding of the product, services, and amenities they will receive.

"My Hotel" is also a luxury hotel, although it is not as widely known to the traveler. Because "My Hotel" provides similar services, amenities, features, and experiences, it is priced in line with the well-known luxury brand. As long as images and online content support the appropriate level of services and products at "My Hotel," comparable pricing to the well-known luxury brand hotel supports a perception for the customer that "My Hotel" is of the same quality.

Once "My Hotel" decides to radically lower its BAR rate due to low demand, placing itself closer in price to the 3-star brand hotel in the market, consumers will assume "My Hotel" is aligned in quality with the more familiar 3-star brand hotel as well.

The Domino Effect

The decision to lower retail price has a far greater impact than simply changing guest perception (Table1). In most cases, hotels use dynamic pricing to determine the price point of other rates. These are set to either float off the retail price, or are used as a benchmark to show value.

1.

Dynamic Rates

Lowering your retail price automatically lowers all of the other rates in your hotel. For example, if you adjust a BAR rate by -15% from US$200 to US$170, ALL of the rates that are automatically priced based off BAR will subsequently decrease.

2.

Static Rates

Rates fixed with negotiated accounts, for example, now lose the original value of their discount, as the rate differential decreases.

3.

Gross Operating Profit

Changes made to retail pricing can positively or negatively impact Gross Operating Profit (GOP). An increase in occupancy and rate can help “flow” profit down to GOP, and conversely, the decrease in occupancy and rate can impact the overall profit loss.

Impact from Price Decrease

Original Price			Lowered Price		
Occupancy	**Rate**	**% BAR**	**Rate**	**% BAR**	**Decrease**
Package	$220.00	10%	$187.00	10%	($ 33.00)
BAR	$200.00	—	$170.00	—	($ 30.00)
Consortia	$180.00	-10%	$153.00	-10%	($ 27.00)
Discounts (AAA)	$180.00	-10%	$153.00	-10%	($ 27.00)
Promotions	$170.00	-15%	$144.50	-15%	($ 25.00)
Static Negotiated	$160.00	-20%	$160.00	-5.9%	none

Table 1

Finally, the more you lower your rates, the more your clientele changes. This change in customer expectations and perception of your product impacts service levels, causes less ancillary spend, increases guest complaints and wear and tear on the product, and decreases employee morale. Unfortunately, the impact of this price decrease can be felt across all departments.

Impact on GOP

Yes, pricing directly impacts GOP, but it is also critical to understand that the percentage of revenue contribution is directly impacted by fluctuations in occupancy versus ADR.

Occupancy Impact on GOP & Flow

Table 2 shows the direct GOP and FLOW impact for a hotel that has increased revenues by increasing occupancy. In this example, the hotel's occupancy increased by 3.4 points annually. The growth in occupancy brought an overall increase of US$1.1M in room revenue and US$1.9M in total revenue for the hotel.

Because increased expenses come along with increased occupancy, the variable costs associated with the additional rooms sold increase hotel expenses by an additional US$1.07M. As a result, the hotel realizes an increase of US$911K in GOP, flowing 45.8% of the profits to the bottom line.

Average Rate Impact on GOP & Flow

The next example (Table 3) shows the hotel increasing GOP and FLOW with the same room revenue increase as the previous example, but this time doing so as a result of ADR growth. In this case, the hotel did not have the additional occupancy and the resulting increase in other departmental revenues, or the additional costs. So, the hotel was able to FLOW an additional US$148,083 in GOP variance, compared to Table 2.

GOP Growth Through Occupancy

	Original	Increased OCC%	Variance
Available	146,000	146,000	—
Room Sold	103,076	108,040	+4,964
OCC%	70.6%	74.0%	**+3.4**
Rate	$232.35	$232.35	—
RevPAR	$164.04	$171.94	+$7.90
Room Revenue	$23,949,709	$25,103,094	**+$1,153,385**
Total Revenue	$44,664,650	$46,654,832	**+$1,990,182**
Total Expenses	$30,355,497	$31,433,887	**+$1,078,390**
GOP	$14,309,153	$15,220,945	**+$911,792**
GOP Margin	32.0%	32.6%	+0.6
GOPPAR	$98.01	$104.25	+$6.25
Flow			**45.8%**

Table 2

GOP Growth Through Average Rate

	Original	Increased ADR	Variance
Available	146,000	146,000	—
Room Sold	103,076	103,076	—
OCC%	70.6%	70.6%	—
Rate	$232.35	$243.54	**+$11.19**
RevPAR	$164.04	$171.94	+$7.90
Room Revenue	$23,949,709	$25,103,094	**+$1,153,385**
Total Revenue	$44,664,650	$45,818,035	**+$1,153,385**
Total Expenses	$30,355,497	$30,499,007	**+$93,510**
GOP	$14,309,153	$15,369,028	**+$1,059,875**
GOP Margin	32.0%	33.5%	+1.5
GOPPAR	$98.01	$105.27	+$7.26
Flow			**91.9%**

Table 3

Occupancy Impact on GOP & FLEX

Now, view the impact in reverse, as if the hotel experienced a decline in room revenues from lowered occupancy. In Table 4, we show the same hotel, but this time, occupancy has declined by 3.4 points to 67.2%; room revenue was reduced by US$1.1M; and total revenues dropped US$1.9M, based on the assumption that lost occupancy means less spending in hotel outlets. Although the hotel's total expenses decreased US$1.07M as a result of servicing fewer guests, the GOP dropped more than US$911K.

Average Rate Impact on FLEX

Finally, take a look at the impact on GOP when the hotel has the same decline in room revenue due to ADR (Table 5). Room revenue again decreased by US$1.1M, along with total revenue. There was less reduction in expenses because the hotel had to service the same number of guests, and GOP dropped by US$1.05M, which is an additional loss of US$148K when compared to the GOP from the earlier example (Table 4).

GOP Decrease Through Occupancy

	Original	Decreased OCC %	Variance
Available	146,000	146,000	—
Room Sold	103,076	98,112	(4,964)
OCC%	70.6%	67.2%	**-3.4**
Rate	$232.35	$232.35	—
RevPAR	$164.04	$156.14	($7.90)
Room Revenue	$23,949,709	$22,796,324	**($1,153,385)**
Total Revenue	$44,664,650	$42,674,468	**($1,990,182)**
Total Expenses	$30,355,497	$29,277,107	**($1,078,390)**
GOP	$14,309,153	$13,397,361	**($911,792)**
GOP Margin	32.0%	31.4%	-0.6
GOPPAR	$98.01	$91.76	($6.25)
Flow			**45.8%**

Table 4

GOP Decrease Through Average Rate

	Original	Decreased ADR	Variance
Available	146,000	146,000	—
Room Sold	103,076	103,076	—
OCC%	70.6%	70.6%	—
Rate	$232.35	$221.16	**($11.19)**
RevPAR	$164.04	$156.14	($7.90)
Room Revenue	$23,949,709	$22,796,324	**($1,153,385)**
Total Revenue	$44,664,650	$43,511,265	**($1,153,385)**
Total Expenses	$30,355,497	$30,261,987	**($93,510)**
GOP	$14,309,153	$13,249,278	**($1,059,875)**
GOP Margin	32.0%	30.5%	-1.6
GOPPAR	$98.01	$90.75	($7.26)
Flow			**91.9%**

Table 5

An ADR decline has a much greater impact on GOP than occupancy decline.

Flex: The percent of decrease in revenue that contributed to the decrease in GOP. The lower the better.

Flow: The percent of increase in revenue that contributes to the GOP. The higher the better.

Case Study

Maintaining Retail Pricing During a Downturn

Summary

A mid-size independent hotel that has been historically dependent on Group Sales business, due to its ideal location less than a mile from the city convention center, was forced to re-think its strategy when the pandemic created rapidly shrinking occupancy levels. With no end to the decline in sight, the hotel turned to experts at PTG Consulting for guidance.

We began by conducting an objective competitive set analysis, including an intense review of retail pricing before and during the pandemic. With experience earned over years of successfully working with independent hotels, we encouraged the hotel to turn its attention to transient business, implemented a strategy that centered on maintaining retail pricing, and created a slight daily price increase to place the client's rates (and the perception of its value and experience) in alignment with its top competitors. Our client got nervous when its competitive set attempted to drive demand by lowering rates, but we advised patience, and they held firm. They maintained their prices and increased their overall share of the transient segment. While still falling behind the occupancy achieved by their competitors, the difference in our client hotel's average rate put them ahead, realizing a 104.4% RGI (Revenue Generation Index) over the three months studied.

Background

This mid-size, independent hotel in the 150–300 rooms size category, is located in a highly competitive downtown market represented primarily by branded hotels, with a combination of smaller limited service and upscale hotels. This hotel focused historically on Group business, was consistently ranked 7/7 in occupancy and 4/7 in ADR, and has very little corporate account production and transient leisure business because it is located less than a mile from the city convention center, not in an ideal location for the non-Group customers.

Situation

The hotel relied heavily on Group business before the pandemic and had to find new business and put occupancy on the books. Fast.

Action

PTG Consulting began by examining the hotel's pricing before the pandemic. We found that, for an average week, its BAR ranked between 4 to 6 out of 7 on most days (Table 1). Also noticeable was the variance of the client hotel's price compared to the average price in the competitive set. Mid-week the hotel was priced US$20 to US$40 lower than the average price of its competitive set. We quickly identified that the hotel's retail pricing was too low, and worked with the hotel's team to reset its pricing strategy.

Action (continued)

Within the first month of the pandemic, when the client's competitive set began to drastically drop their retail price, PTG Consulting advised setting and holding a minimum rate for weekdays of US$149 and weekends of US$179. Regardless of how low the competitive set dropped its price, PTG Consulting insisted that the hotel hold its rate. A typical week going forward (Table 2) showed the client hotel as number one in price positioning.

Hotel & Comp Set Rates (Original Pricing Strategy)

Source: OTA Insights

Comp Set – Rate Shops	STAR Chain Scale	Share	Sun	Mon	Tue	Wed	Thu	Fri	Sat
Client Hotel - Independent	Indep	16.1%	$139.00	$159.00	$159.00	$159.00	$139.00	$159.00	$159.00
Brand - Limited Services	Upscale	13.1%	$154.00	$179.00	$289.00	$229.00	$214.00	$129.00	$134.00
Independent Full Service	Indep	5.2%	$139.00	$149.00	$149.00	$149.00	$149.00	$159.00	$185.00
Independent Full Service	Upper Upscale	22.1%	$155.00	$175.00	Sold out	$199.00	$155.00	$145.00	$165.00
Brand - Full Service	Upscale	11.6%	$174.00	$184.00	$225.00	Sold out	$174.00	$164.00	$164.00
Brand - Limited Services	Upper Upscale	12.0%	$109.00	$129.00	$149.00	$149.00	$109.00	$99.00	$99.00
Brand - Full Service	Upscale	19.8%	$169.00	$169.00	$199.00	$219.00	$164.00	$149.00	$159.00
Daily Price - Subject Hotel Ranking			**5**	**6**	**4**	**4**	**6**	**2**	**4**
Comp Set Average Price			**$149.20**	**$163.20**	**$203.00**	**$181.50**	**$160.20**	**$139.20**	**$149.40**
Variance to Comp Ser Avg Price			**($ 7.20)**	**($ 24.20)**	**($ 44.00)**	**($ 22.50)**	**(21.20)**	**$19.80**	**$9.60**

Table 1

Hotel & Comp Set Rates (Post-New Pricing Strategy)

Source: OTA Insights

Comp Set – Rate Shops	STAR Chain Scale	Share	Sun	Mon	Tue	Wed	Thu	Fri	Sat
Client Hotel - Independent	Indep	16.1%	$149.00	$149.00	$149.00	$149.00	$159.00	$179.00	$179.00
Brand - Limited Services	Upscale	13.1%	$129.00	$134.00	$130.00	$121.00	$130.00	$125.00	$134.00
Independent Full Service	Indep	5.2%	$129.00	$139.00	$139.00	$139.00	$159.00	$179.00	$199.00
Independent Full Service	Upper Upscale	22.1%	$145.00	$129.00	$145.00	$129.00	$129.00	$145.00	$145.00
Brand - Full Service	Upscale	11.6%	$129.00	$129.00	$129.00	$129.00	$129.00	$129.00	$129.00
Brand - Limited Services	Upper Upscale	12.0%	$89.00	$89.00	$89.00	$89.00	$89.00	$89.00	$89.00
Brand - Full Service	Upscale	19.8%	$129.00	$139.00	$139.00	$139.00	$139.00	$139.00	$149.00
Daily Price - Subject Hotel Ranking			**1**	**1**	**1**	**1**	**1**	**1**	**2**
Comp Set Average Price			**$124.20**	**$124.20**	**$126.40**	**$121.40**	**$127.20**	**$133.40**	**$139.20**
Variance to Comp Set Avg Price			**$24.80**	**$25.00**	**$22.60**	**$27.60**	**$31.80**	**$45.60**	**$39.80**

Table 2

Results

The competitive set's attempt to drive demand by lowering rates did not work.

Remember that our client hotel historically thrived on Group business, which is now non-existent for the client and represented just 1.2 occupancy points for its competitive set. By driving low rates, the competitive set achieved 10.4% transient occupancy compared to the client's 7.3%. However, the competitive set's incremental occupancy came at a cost — a lower price.

Its Transient average rate finished at US$98.10, a decrease of 29.3% from the previous year, which was also US$48.71 less than the client's ADR. Overall, the transient RevPAR for the client hotel exceeded the competitive set's, leading to a 104.4% RGI.

What if the competitive set did not lower retail pricing? Would they have been able to generate the same occupancy? Perhaps occupancy might have been slightly lower however, it is likely that they would have achieved a higher RevPAR overall if they had simply maintained their retail pricing.

STR Results

Occupancy	Transient	%Change	Group	%Change	Contract	%Change	Total	%Change
Client Hotel	7.3	-75.1	0.0	-100.00	0.0	0.0	7.3	85.8
Comp Set	10.4	-79.7	1.2	94.8	0.1	-88.2	11.7	-84.3
Index (MPI)	69.7	22.5	0.0	-100.0	0.0	0.0	61.9	-9.6

ADR	Transient	%Change	Group	%Change	Contract	%Change	Total	%Change
Client Hotel	146.81	3.8	0.0	-100.00	0.0	0.0	146.81	-5.1
Comp Set	98.10	-29.3	105.54	-38.6	84.28	-2.3	98.67	-33.3
Index (ARI)	149.70	46.9	0.0	-100.0	0.0	0.0	148.80	42.1

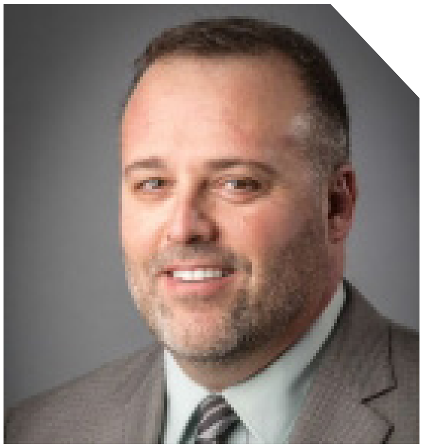
RevPAR	Transient	%Change	Group	%Change	Contract	%Change	Total	%Change
Client Hotel	10.66	-74.2	0.0	-100.00	0.0	0.0	10.66	86.6
Comp Set	10.21	-85.6	1.24	-96.8	0.12	-88.5	11.58	-89.5
Index (RGI)	104.40	78.9	0.0	-100.0	0.0	0.0	92.10	28.4

Table 3

PTG Consulting Difference

PTG Consulting develops long-term winning strategies for independent hotels. Our experienced Revenue Management professionals work in a "Revenue for Hire" capacity to provide various levels of support and engagement tailored to your hotel and your team's unique needs, including pricing strategy and positioning, channel mix distribution, objective competitive set evaluation, and long- and short-term revenue management resources.

We are experts in the independent hotel space, which requires great understanding and a distinct approach. We know that one size does not fit all, and will work with you to understand your goals and challenges before customizing a highly actionable and detailed plan that will work for your specific needs.



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Michael Sherwood is responsible for revenue-related consulting services including the "Revenue for Hire" program, Revenue Management Workshops, consulting projects, and more for PTG Consulting. Most of his 34-year career in the hospitality industry, which includes Preferred Hotels & Resorts and Larkspur Hotels and Restaurants, has been devoted to Revenue Management. As a development analyst at Bristol Hotels and Resorts, he was responsible for completing market studies and development proformas for new hotel acquisitions.

In 2010, Michael received his Revenue Management Certification through Cornell University, and he has been a Certified Revenue Management Executive (CRME) through HSMAI since 2013.

About PTG Consulting

PTG Consulting is an award-winning strategic partner for the tourism and hospitality industry's most dynamic brands, destinations, and independent hotels. Through our global network of experts, we deliver integrated solutions that inspire, engage, and convert.

As part of the Preferred Hotel Group family, our connections to travel trade decision-makers, industry influencers, media, and travelers carry weight. With a diverse global portfolio of independent hotels and distinctive destinations, and exclusive access to sustainable tourism expertise at our fingertips, the Preferred name affords us deep influence and resources worldwide.

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