Channel Management

My RevPAR is Rising But My GOP Is Not: Taking a Channel Diagnostics Audit

6/20/2013

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One of the lessons learned while conducting research for “Distribution Channel Analysis: A Guide for Hotels,” was that hotels will have to proactively manage distribution to deal with dozens of new channel partners or they risk reaching a point where costs will compromise profits. Distribution costs are often running second only to labor and, because of the varied commission models, owners and managers don’t often have visibility into what these costs mean to their financial status. Plenty of hotels are already there as evidenced by this common refrain: my RevPAR is rising and yet my gross operating profit (GOP) is not; I am managing operating expenses well, but I feel I am losing out in my reservation or marketing expenses.

High distribution costs also pose a threat to the franchise and brand model by creating a situation in which the hotels start to question the fees they pay for a hotel brand. Some no longer feel they should pay for third-party business (transient or group/meetings) since they argue they can acquire that business without the brand’s help. Most hotels are not well equipped to set objectives for an optimal channel mix, figure out the related profit contribution and manage to that target.

How much does it actually cost to acquire a customer? A central issue in marketing, this question goes to the core of hospitality distribution. How much does it cost to (1) attract the customer, (2) get the reservation and (3) get them to repeat this process for all subsequent visits to your destination? There are many discussions between owners and managers of hotels about the high cost of distribution. In order to manage and contain these rapidly rising costs, they first have to be identified and ultimately measured and monitored.

Attracting the Customer

With so many travelers spending the majority of their time doing online planning, the marketing resources have to move with this trend. There is certainly some offline media activity in hospitality, but the funds earmarked to attract new business are increasingly for digital initiatives. Some funds are spent for direct response programs to get a travel shopper to click on an ad or link to lead them to a booking engine, and some spending is applied to branding programs to reinforce the brand’s image and build relationships. It is always difficult for a hotel to decide how much money to spend on direct response as compared to branding.

Direct acquisition efforts may be in the form of performance-based models where a brand will offer to run search engine marketing for a hotel and charge a percentage only on the sales that actually materialize, or many hotels conduct their own online marketing initiatives separate from brand programs. Because most new media opportunities are online, these options become central to distribution management. Google, Facebook, Apple, Kayak, Bing, Twitter and many others are now vying for the right to refer their consumers to hotel websites and collect a fee for that service. The list of consumer sites that want to play a part in moving the travel shopper along the sales path is growing rapidly. These costs become part of the process of getting the traveler to reach your booking engine instead of your competitors. Testing the media in these sites and figuring out how much should be spent to achieve an acceptable return will be a new challenge to hotel management.

Then, there is the expense connected to branding and relationship building. This can be likened to courtship–how can you expect one party to accept the offer of marriage without developing the relationship first? Hotels need to account for that effort as part of their marketing funds. Many branded hotels will benefit from their flag’s initiatives. Advertising, national sales efforts, partnership programs, national or international visibility and the power imbued in the sign above the front door all contribute to getting customers to choose your brand over another. Most of the funds for attracting customers will be in the sales and marketing budget and this spending, whether it is direct response or branding, is a component of a hotel’s distribution costs.

Booking Costs

Once the traveler has chosen your hotel, they have to make a reservation. He or she may choose a range of ways to accomplish that. The guest may use your website, call the hotel or central 800 number, use an online travel agency (OTA), tap a travel agent who uses the GDS or come to the hotel directly to make a booking. Most of these options include an electronic component and all have some cost associated with them. These costs are generally commissions and/or transaction fees and are often recorded in a hotel’s rooms division schedule of accounts.

However, some brands will include search marketing as a type of commission and this may be charged to sales and marketing or to the rooms department depending on the way the hotel is directed to record the transactions. Then, there is the method that accounts for net-rated business. For online travel agents, travel management companies or wholesalers that negotiate a net rate with the hotel, there is no explicit record of this cost in the hotel's P&L since the commission is essentially pre-paid as a discount to the agent who then marks it up and keeps the difference. Ideally, a hotel can track this expense so they can manage it and gain clarity as to how much they are paying in direct reservation costs.

Retention Efforts

Finally, there is the element of distribution costs related to retaining the customer and getting them to return for subsequent visits. Costs such as loyalty program-related expenses are often logged in the sales and marketing budget. The provision of gifts or other in-room amenities for repeat guests may be charged to the rooms department. When a guest comes back to the hotel, he or she may book in a different channel from his or her first visit. Once engaged as a returning guest, there may be a bias to use a direct channel such as a hotel's website, either to enable the tracking of stays or points or because he or she may be encouraged to rebook through special links or bounceback emails that lead to the hotel's booking engine. While the likelihood to book direct by returning guests will generally mean lower reservation costs, there is still a cost incurred for any reservation method.

See sidebar below with steps to conduct a channel diagnostic audit.

Determining an optimal mix of business by channel and segment and calculating what that mix means in terms of ADR, RevPAR, occupancy and net ADR will help a hotel figure out exactly what the direct distribution cost implications are for the channel mix it is aspiring to achieve. Digging deeper into the costs to attain that revenue objective in terms of sales and marketing expense–the other part of the distribution cost equation–will direct a hotel to spend its customer acquisition funds at a level that ensures that gains in net ADR find its way to the GOP where it is most valued.

Cindy Estis Green is CEO and co-founder of Kalibri Labs, a company that offers analytics solutions that enable hotels to measure and monitor business mix and the resulting contribution to operating expenses and profit. A 35-year industry veteran, she is the co-author of the industry bestseller, "Distribution Channel Analysis: A Guide for Hotels," published by the HSMAI Foundation and AH&LA.