by Ron Pohl

Improving profitability can be achieved by focusing on four management areas

Maximizing profitability is a key practice in most businesses, as it should be, and there are an equal number of opportunities to find or improve existing profit levels. In today's ever increasing business environment and technological advancements, businesses continually strive to create more profit. The hotel industry is no different, but has the added complexity of public service. This means we cannot afford to negatively impact customer service.

The hotel business is as complex an operation as any in the business environment today and certainly more labor and capital intensive than most. Most often we must use operational efficiencies, product savings, and administrative controls to improve over past performance. Successful implementation of improved profitability is typically measured by departmental "margins" and "flow through".

"Margins" refer to the departmental profit and expense in relation to revenues and are measured as a percentage. For example, the Rooms Department's profitability typically ranges from 75-85%. Full-service and upscale properties will incur increased expenses while mid-priced limited-service hotels will have lower expenses.

"Flow through" is the measurement of revenues achieved at the top line (gross revenues) that is carried through to the profit line of the hotel's financial statement. Flow through is typically illustrated on the Profit & Loss Statement. A standard of 50 % flow through is expected by many owners. Similarly, flow through is also measured when revenues decline and management's ability to maintain margins/costs to the operating profit line. For example, if actual gross revenues increase or decrease from the budgeted gross revenues by $20,000, it is expected, that the bottom line would not be impacted by more than $10,000 due to the implementation of effective cost control procedures. Although the revenue stream is significant, so too are the costs associated with the revenues. We can never take revenues and expenses for granted; a good hotel operator controls every nickel and dime, not dollars.

In order for hoteliers to understand and effectively manage their business, several key processes must be incorporated into their daily, weekly and monthly operating procedures. Four key processes are presented here for your consideration:

Revenue management

The basis for revenue management processes is a huge topic in itself; however, we can't maximize profits without discussing revenue management practices. Smith Travel Research is forecasting general occupancy to decline slightly over the next two years while it predicts that average daily rate will increase approximately 5%. Driving revenues, especially room rates, have the greatest potential for increasing profitability than most other revenue streams and practices in the hotel.

Effective revenue management begins by understanding and tracking demand. Demand is measured in segments, by season, day of week, and pace until day of arrival. Knowing your hotel's demand will provide the opportunity to maximize revenue channels by opening, closing, restricting and/or raising or lowering rates. Measuring the results of those strategies will provide the intelligence to continually maximize revenues.

Equally important is understanding your competitors' rates. There are many good tools available to better understand what your competition is charging real time. Use them wisely and frequently. Don't be afraid to adjust rates often, as $1, $5, $10, or $20 rate increases per room equals improved RevPAR. Keep in mind that 90% of rate growth flows to the hotel's bottom line. Therefore, it is critical to have someone in each hotel responsible for revenue management. And don't forget to use your franchisor wisely; all have experts in their revenue management systems and are available to assist their franchisees or member properties.

Forecasting

The ability to accurately forecast revenue dictates one's ability to manage and control expenses. Revenues and expenses must be forecasted for each business unit/department within the hotel. Forecasts are used to plan and adjust spending in order to maintain profit margins. A minimum of three forecasts (14-day, 30-day, and 90-day), must be created on regular intervals to effectively manage the hotel's operation and improve profitability.

A 90-day forecast is used to identify current business trends and provide for spending adjustments for items with longer lead times and hiring needs. A 30-day forecast is the most accurate and is the last chance to adjust your spending to maintain profit margins. Finally, a 14-day forecast dictates staffing and scheduling needs. In all cases, strive to achieve forecast accuracy of plus or minus 3%.

Departmental expenses

Labor is the greatest expense in most hotels and has the greatest potential to be controlled and adjusted based upon the forecast. To ensure proper scheduling of personnel, managers should establish "productivity standards" for all positions. Most staffing and positions fluctuate with occupancy and therefore are either measured on a "Per Occupied Room" (p.o.r.) or "per guest" basis, depending on the type of hotel or the department doing the scheduling.

Generally, Housekeeping and Front Office operations use "p.o.r." for scheduling purposes, while Food & Beverage operations are based on "per guest". In both cases the ability to react quickly to changing demand will dictate management's success in maintaining margins. It is important to note here that there are other positions within the hotel that are considered static (e.g., maintenance staff or administrative positions) and are therefore not impacted by business levels.

Managing and maintaining productivity standards and eliminating overtime are important actions for managing labor expense. Staff turnover has a significant impact on labor cost and the level of guest service that is delivered, so do not underestimate the impact of turnover on your operation. Understand the main cause of turnover is usually not wages; it is the perceived environment in which the employees work.

Controllable or "other" expenses refer to the supplies or services required to operate our business and are the focus of maintaining or improving profitability. Many products can be purchased through Contracted Services offered by your franchisor and typically provide the best pricing because of economies of scale. Many also often include rebates from the vendor.

Complimentary breakfast and guestroom amenity standards are constantly being upgraded by leading hotel chains and are often times a competitive point of differentiation. Tightly control these costs and don't go beyond guest's expectations. Realize that guests typically choose a hotel based on location and a fair price; they expect a clean hotel with friendly staff, and competitive amenities, nothing more. Avoid "amenity creep" whenever possible as it only eats into your hotel's bottom line.

Some services at the hotel level are contracted individually, such as landscaping, elevator maintenance, and armored car deposit service. Always get annual bids for these services. But the lowest bid is not necessarily the best option that should be selected. Examine all costs in relation to the benefits provided and the track records of each vendor. Do not accept standard annual price increases with all vendors.

Another approach to better understanding expenses is the "zero based" approach. Typically, we begin with costs based on previous years' spending, starting with zero and asking why we are spending the money on a specific product or service. This provides a different perspective and allows hotel managers to question the rationale for each and every expense item. Try it; you might be surprised what you have been paying for that wasn't needed.

Green Initiatives

The Green hotel designation is no longer a marketing initiative or gimmick; it is a serious challenge involving many businesses across the nation and the world. This will have a significant effect on how we do business in the future. With some success over the years, there are several areas of our business that we have tried to incorporate "green" processes into our operations. Examples include recommending guest re-use guestroom linens and towels, replacing incandescent lamps with compact fluorescent bulbs, purchasing laundry ozone equipment, and instituting recycling programs. Today and in the future, processes like these and more will be the way hotels will be required to conduct business.

Prudent hotel operators will begin to implement as many of these processes as possible into their daily operation. As energy costs continue to skyrocket, utilities are a huge expense for hotels; efforts should be made on a daily basis to conserve. We are an electronic world and therefore reducing the use of office supplies/paper can have a significant impact on your bottom line. There are many products labeled as environmentally friendly and many more to come. When considering green initiatives, always review the validity of the product or service in conjunction with the projected "return on investment" prior to making a commitment.

In order to be successful at improving and maximizing profitability, begin with strategies focused on driving revenue. Hotel managers must have a thorough understanding of the market condition and its competition. Do not wait for your competitors to make the first move, take chances, measure results, and repeat. To effectively manage the business, managers must be able to accurately forecast their volume and necessary expenditures. Labor and other departmental expenses must be managed down to each dollar spent. One hundred dollars of unnecessary expense may require a hotel to sell two additional rooms to cover the cost and maintain the hotel's profitability expectations. Finally, operating environmentally friendly hotels is something to be considered at all levels of operation as these are opportunities to save money. ✧

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