

Hospitality Practice

Fall 2006

Optimizing Hospitality Profitability

**Discovering Opportunities to
Improve Revenues and Lower
Expenses**

EDGEWATER
TECHNOLOGY 

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EXECUTIVE SUMMARY

There are clear opportunities for Hospitality organizations to optimize their profitability by reducing operating expenses and improving revenues. To uncover these opportunities, Edgewater Technology recommends organizations adopt the following guiding principals:

- Take a fresh approach to examining infrastructure and technology;
- Determine whether existing infrastructure and technology assets should be repurposed, retained or eliminated;
- Avoid overly complicating the revenue management strategy;
- Consider outsourcing as a way to reduce costs, but also weigh its effect on quality of service; and
- Tie labor expenses to revenue drivers such as occupancy, F&B sales and convention attendance.

In this research brief, Edgewater presents three quick case studies of organizations that applied one or more of these guidelines to either enhance revenue or reduce expenses.

REALIZING OPPORTUNITIES TO IMPROVE PROFITABILITY

Many organizations have unrealized opportunities to improve their profitability.

Successful Hospitality organizations must continuously seek new ways to reduce expenses and grow revenues. Continuing improvements in technology and software have created new opportunities for profitability improvements, but technology improvements must be based on careful Return on Investment (ROI) modeling. If implemented properly, initiatives to improve profitability can be fiscally successful without negatively impacting the guest service quality – in many cases, they can even offer improvements.

To uncover opportunities to improve profitability, Hospitality organizations should:

- Be willing to take a fresh approach to examining infrastructure and technology;
- Review existing infrastructure and technology assets to determine whether they can be repurposed, retained or if they are no longer of value;
- Look to both increases and decreases in room rates as methods to drive increases in revenue;
- Establish a common business intelligence platform for the enterprise that will streamline operational analysis to reduce expenses and strategic analysis to increase revenue;
- Consider outsourcing as a way to reduce costs, but carefully examine the ROI and the target roles and responsibilities to reduce negative impact on guest service levels; and
- Drive labor expenses down by tying labor scheduling to revenue drivers such as occupancy, F&B sales and convention attendance.

During an executive breakfast that Edgewater recently hosted, **Hospitality Management Strategies**, a roundtable of industry leaders convened to examine four key opportunities to improve revenue or reduce expenses.

1. At the property level, there are significant opportunities to offer improved telecommunications and data services at reduced cost..
2. Simple and often counter-intuitive innovations in revenue management strategies can grow revenue and improve the business mix.
3. In addition, Ranzal & Associates conducted a live demonstration illustrating how an enterprise's operational and strategic analytical requirements can be supported from one single platform. A single platform can meet enterprise operational and strategic analytical requirements and enable companies to fully execute their business strategies.
4. Outsourcing non-core business functions and tying labor usage to business forecasts can achieve significant cost savings.

BLACKSTONE REAL ESTATE ADVISORS: *MODERNIZING TECHNOLOGY TO REDUCE EXPENSES AND TO IMPROVE SERVICES*

Uncovering the Opportunity

David Thor is a Senior Information Technology Advisor to the Blackstone Commercial Real Estate Group. As Blackstone acquires Hospitality organizations, they also acquire their Information Technology (IT) organizations. As an equity investment firm, Blackstone is frequently both an acquirer and a seller of both companies and of properties, yet as they dispose of assets, the IT organization is sometimes sold. This repeated cycling of IT staff and infrastructure presents the following challenges:

- Unable to build an IT staff familiar with the array of deployed technology;
- Utilize outdated technology;
- Utilize orphaned technology; and

- Need to add and remove properties from the infrastructure as they are acquired or sold.

Developing the Solution

Some Hospitality organizations shy away from implementing new data and telecommunications technologies, fearing a disruptive infrastructure implementation will erode guest satisfaction, or technology costs will be difficult to recover. David was convinced implementing new IP technologies provided a clear path to better guest service and lower operating costs. Below were his recommended steps:

- Put all properties and offices on a private IP network;
- Centralized property technology in a datacenter including:
 - Point of Sale Systems;
 - Property Management Systems; and
 - Ancillary Services (sales, finance, HR/payroll, timekeeping, etc.).
- Aggregated voice and data services into the private network including:
 - Stand-alone local facilities;
 - Long distance facilities;
 - Guest Internet access;
 - Back office data; and
 - POTS reduction.
- Move telecommunications facilities and infrastructure from the properties to centralized facilities.

Results and Lessons Learned

By approaching the voice and data strategy with a phased approach, the property level yielded significant savings at various stages, as shown in the following figure.

	Phase 1 Savings	Phase 2 Savings	Phase 3 Savings
Operating Company	Aggregate to Single Loop	Dial Tone in a Cloud	PBX in a Cloud
A	53%	25%	33%
B	25%	22%	36%
C	20%	25%	

The properties now have dumb terminals to run their applications, legacy phones, when connected to the new technology, act as IP phones and a few legacy technologies (such as alarms and elevators) which remain on POTS lines. David attributes the success of this initiative to:

- Reducing operating expenses wherever possible;
- Moving quickly while maintaining flexibility;
- Simplifying IT accounting;
- Transferring all possible services to IP
- Taking advantage of infrastructure synergies across operating organizations.

LUXURY RESORTS: *IMPROVING REVENUE MANAGEMENT*

Uncovering the Opportunity

For the emerging Luxury Resorts (“LXR”) brand, Revenue Management was seen as an opportunity to drive increased profitability. Since the organization had roots in a variety of different chains and stand-alone properties, there were a number of different approaches being taken at the various properties. Jeff Garzia, an LXR Vice President of Profit Optimization, discussed how LXR dealt with the following issues:

- Too many room types;
- Revenue managers at each property – regardless of size; and
- Inaccurate room inventories.

Developing the Solution

Jeff was able to resolve these issues by dramatically simplifying LXR's approach to Revenue Management with iHotelier central reservations system which enabled LXR's room inventory to be consistent across channels. They reduced the number of room types which allowed the revenue managers to focus on improving the revenue mix. Additionally, they evaluated the revenue manager staffing model, allocating properties based on the size and business volume.

These steps allowed LXR to better focus on both the appropriate rates and business mix to drive revenue.

Results and Lessons Learned

Jeff provided two examples of how this approach is already achieving results. For a non-flagged property in the Northeast US competing in a local market filled with flags, LXR invested in a significant property renovation while the revenue management team evaluated the business. The company realized the convention business was going to remain a key driver of the business, however by reducing the amount of negotiating business; they were able to grow the retail business, driving RevPAR improvements better than their competitive set.

The second example was for LXR's west coast properties. LXR reduced their retail ADR by 8.5%. A rate reduction might seem counter-intuitive, but this more than doubled the retail share of their business from 19% to 41% and reduced the negotiated share from 54% to 38%.

Jeff attributes these successes to the following:

- Defining the organization to fit with the corporate culture;
- Establishing guiding principles and best practices;
- Building a plan to optimize business mix, rate and inventory management and distribution strategy;
- Developing and executing comprehensive marketing plans; and
- Leading the communication of profit optimization practices and results to the rest of the organization.

RANZAL & ASSOCIATES:
PROVIDING OPERATIONAL AND STRATEGIC BUSINESS INTELLIGENCE

Uniting Strategy with Planning and Execution

Many organizations today are faced with the challenge of sharing accurate and timely information across their organization to enable them to execute their business strategy. Effective execution of strategy requires a closed loop process between strategy, planning and execution. Multiple systems, different reports and department-level spreadsheets often create more questions and conflicting answers, and fail to provide real Business Intelligence (BI).

Organizations who have not implemented robust BI capabilities often incur significant costs for programmers to write specific queries to answer one-off questions and significant effort within the finance department just collecting their data. BI solutions free up more finance department time for analysis and provide a platform for answering not only today's questions, but those that might arise in the future as the organization grows and changes strategy.

Steve Litt of Ranzal and Associates conducted a live demonstration of BI capabilities from a single platform that can support the analytical requirements of an entire organization. Focusing on both daily hotel operations and strategic marketing, Steve demonstrated how a powerful BI solution can provide the ability to:

- Rapidly drill through summary information (like the P&L) to detailed transactions;
- Easily manipulate data to compare brands, regions or individual hotels; and
- Quickly identify highly profitable or at risk customer segments and extract those customers for marketing activities.

BI solutions can deliver a single information platform utilizing common underlying data that supports both summary-level dashboards for senior executives and detailed transactions for analysts.

LUXURY RESORTS:

EXPLORING OUTSOURCING AND LABOR MANAGEMENT TO REDUCE EXPENSES

Uncovering the Opportunity

Mike Teplin, Senior Vice President of Finance for LXR, discussed initiatives LXR has undertaken to lower their labor costs. As Mike pointed out, labor accounts for the largest portion of expenses – approximately 45-50% which makes labor costs a natural for cost-cutting, however hospitality is a labor intensive industry. The challenge in cutting costs is ensuring any cuts do not negatively impact the product being presented to customers.

Mike discussed two steps LXR has taken to control labor costs – **outsourcing** and **labor management**.

Developing the Solution

LXR looks at outsourcing with the following philosophy: **Work which can be done outside the four walls of a business at the same level of service or better and at the same cost or less, should be centralized, outsourced or offshored.** LXR outsourced its IT maintenance, AP and payroll processes.

Those costs, which cannot be outsourced, can often be better controlled by more closely tying staffing levels to business volumes which is the main focus of their labor management program.

Results and Lessons Learned

Outsourcing has resulted in saving of between 35-55% for LXR. The keys to successfully outsourcing are:

- Go offshore for the right reasons;
- Choose your model carefully;
- Get your people on board; and
- Treat your partners as equals.

The labor management program has already resulted in \$6.2 million in savings during the first 9 months of its rollout. Below are the keys to LXR's successful labor management program:

- Implement a program in phases – not all at once;
- Look for permanent changes that can be made at one time;

- Analyze pay weeks – make the days most likely to require overtime occur early in the week;
- Convert to bi-weekly or semi-monthly;
- Build staffing guides that allow labor to fluctuate with business volume;
- Examine departments with consistent overtime;
- Study how work gets done in the largest departments;
- Be proactive;
- Use trends not budgets;
- Know the rules – labor laws and union contracts may affect what you can do; and
- Look at opportunities to combine positions with similar functions.

UNDERSTANDING THE HOSPITALITY LANDSCAPE

The Hospitality industry is currently in a boom period. Across all segments from economy to luxury, occupancy is rising and new construction is still lagging. With organizations looking to seize competitive advantage, much of today's investment is in guest-facing initiatives such as new bedding, flat panel televisions and improved internet services. Many of these initiatives are working in the current bull market. But, when the market begins to turn down, they may begin to eat into profitability. Also, as hotels begin to approach full capacity the goal of many of these project changes from growing occupancy to retaining it.

Since there is an upper limit on occupancy, continuing to grow profits requires looking at more than simply selling more rooms. Edgewater believes that the companies that will show the best results are those that look into methods to grow revenue beyond growth in occupancy and those that do the best at controlling expenses.

FOUR BEST PRACTICE RECOMMENDATIONS IN PROFIT OPTIMIZATION FROM EDGEWATER AND EXECUTIVE ROUNDTABLE PARTICIPANTS

1. Examine existing technology and review the cost and benefits of upgrading versus replacing.

While it is often less expensive to retain and upgrade existing technology, there can be significant reduction in operating expenses can arise from effectively deploying newer technology. The key to making this decision is envisioning not only the direct impacts, but also how new technology affects other costs.

2. Raising rates and growing occupancy are not the only ways to drive revenue growth.

If a property is at or near capacity, there is little opportunity to sell more rooms. At the same time, even in an overheated market, raising rates may cut into sales. In this type of climate, the key is to look at the mix of sales to see if there are opportunities to move to higher rates by, for example, shifting volume from lower-ADR negotiated rates to retail rates.

3. Look at outsourcing as an investment.

While outsourcing can result in significant savings, it needs to be approached carefully. Before handing over your processes, be sure that they have been optimized, and clarify roles and responsibilities for all business processes. Your outsourcing vendor can be your partner and help you define the split at the organizational level, but you need to determine how to refine your internal organization structure to work efficiently with an outsourced model. After your outsourced partner begins performing key business tasks, it will not be easy to change how they do so and it will often be more expensive to clean up mistakes than to get things done well the first time. Do not only look at cost, but carefully define turnaround time and problem resolution processes.

4. Labor costs should track to business volumes.

It may seem obvious, but properties send people home early or call people in at the last minute. Labor management cannot guarantee this will never happen – after all, even the best forecast will miss from time to time, but, if the pieces of the program are well prepared,

such circumstances can be minimized. This begins with the forecasting. If the business can accurately forecast volumes, it will be easier to accurately forecast labor needs. The next step is to be sure you have good staffing guides. If your guides do not translate your business volumes into appropriate staffing levels, you will either have more staff than is needed or too little staff to provide service levels that will safeguard guest satisfaction and repeat bookings.

ABOUT EDGEWATER TECHNOLOGY

Founded in 1992, Edgewater Technology is an innovative technology management consulting firm. We provide a unique blend of premium IT services by leveraging our proven industry expertise in strategy, technology and corporate performance management. Headquartered in Wakefield, MA, we go to market by vertical industry and provide our clients with a wide range of business and technology offerings.

To learn more, visit <http://www.edgewater.com/Industries/Hospitality/> or call 800-410-4014.