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HVS Monday Musings: Dynamic Pricing, Perishability, Decoupling in India's Service Industry

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We have heard these words often enough while discussing pricing, revenue management and demand management in our industry. We try and analyze our current approach and what the future may entail in case we wish our hotels to improve yields.

In some of our previous articles we discussed the need for the hotels sector to measure revenues per square foot as an industry benchmark for total revenue management. In this article we are initiating a discussion about pricing power & revenue management.

Airlines have been leading on dynamic pricing in the services sector
The aviation industry has the most advanced dynamic pricing strategies compared to any other industry. Their technology engines analyze demand on routes and make adjustment in pricing as in most cases technology is integrated across all channels of bookings i.e. CRO, Website, Apps and all other channels. Some of the most advanced airlines today are using AI backed demand forecasting and optimization.

Airlines have successfully made corporate volume businesses work at a certain percentage discount to the dynamic rates or alternately have given add-ons such as free cancellation, free meal or free seating rather than a fixed price, which reduces the ability to maximize revenues when the demand is strong.

Over the years, airlines have been successful in generating additional revenues known as "Ancillary Revenues" to drive more from the existing infrastructure. They have de-coupled services rather than coupling everything into one consolidated pricing, positioning it as customer benefits – customers need not pay for the 'service' that they do not use. A few examples include:

- Preferred Seat Charges
- Additional Baggage Charges
- Fast Track Check-in Lane Charges
- Priority Baggage
- Wi-Fi Charges in certain classes
- Meal charges etc.

Summary

Is it time for the hotels sector to embrace some of the revenue management practices followed by the aviation industry? Read on to know more.

Comments

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Airlines have successfully used the real estate within their product to generate advertising revenues as airline passengers are perfect target group for many products & services companies. Airline Movie Channels have advertisements, Seat Backs have Branding capability, Boarding Passes (back cover) are sold as advertising spaces and even the aircraft exterior is used as a billboard.

Another great focus for airlines has been to reduce intermediary costs and in quite a few cases the industry has been able to either move to a 'zero based' model or a 'fixed fee' model rather than a 'percentage of price sold', which helps to reduce the distribution costs for the airlines.

Dynamic pricing in the hotels sector

Let's now look at what the hotels did during the same period when the airlines were working on the above-mentioned strategies. Hotels continued to negotiate fixed pricing with their largest volume producers and in certain cases even last room availability, reducing their capability to maximize during peak times.

Are we as an industry changing enough? Yes, but the progress has been slow which is impacting yields in hotels as compared to the aviation business. The reason we can compare these two businesses is because both are highly perishable services-based industries.

If all brands and chains take the same route, we are sure the change can happen.

For Corporate Hotels the negotiated fixed rate volumes business is very high i.e. almost 40-60% of the business in some cases. Even groups from the same companies get negotiated on special fixed rates in certain cases rather than based on Best Available Rate (BAR). Hence, the so-called Revenue Management is limited to inventory management and for the other 20-30% of the business is picked up from online sources or Walk-ins, for whom hotels do optimize. This limited Revenue Management opportunity reduces the ability to maximize on revenues during peak demand or better demand days thus affecting ADRs.

While hotels are great at listing their room inventory online, which is a perishable product, they have never applied the same perishability logic to restaurant seats or banquets or board rooms and Spas. Why can't the booking engines of the chains be expanded to book and sell promotions & offers for restaurants and all other products / services with the same level of sophistication as for the rooms?

Hotels are also continuing to reduce de-coupling. Now rates are floated with Breakfast and Wi-fi included, week-end packages and other coupled products were introduced to drive higher capture factor for other revenues. So, are we saying that hotels can't create enough traction for an in-house customer to buy from them and should rather couple products? Is coupling really helping hotels across the board or only in certain areas?

For example, when hotels include Breakfast in the rate, do they add the same component that a walk-in customer pays? If not, then why? Are hotels not starting to create discounting across the board?

Are hotels using their customer base and the eyeballs they have, to sell advertising spaces effectively? In a few cases, hotels are using few show windows for displays etc. but can they not have Lobby Displays (like at airports), Façade advertising, In-Room Advertising displays or their own channels? Are Hotel Brands more superior to some of the world’s best airline brands that they don’t think they are leaving money on the table?

Going forward, hotels need to develop Revenue Management principles across the entire spectrum of the infrastructure at their property to increase the level of optimization and achieve higher yields to drive better ROI for all the stakeholders, especially the Owners who have huge capital investments, and bring this sector back on track as a preferred investment. As a start, all negotiated rates must be linked to Best Available Rate (BAR) and not be fixed in nature.