

We Don't Have To Sell Any More? - By Robert Mandelbaum and Viet Vo

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As the industry enters what is projected to be an extended period of moderate, yet sustained growth for the next few years, expect to see the investment in unit-level marketing expenditures start to level off. Historically, marketing expenses grow at a greater pace than total revenue during recessionary periods and the following years of recovery. Industry owners and operators realize the need to 'spend money in order to make money.'

Conversely, we have observed that the annual growth in marketing department expenditures tends to revert to the long-term average of 2.7 percent during periods of prosperity. During the past few years, we have seen the annual investment in marketing drop from 6.1 percent in 2004 to 4.3 percent in 2006. The result has been a gradual decline in the ratio of marketing expenses to total revenue from 4.7 percent in 2004 to 4.5 percent in 2006.

In order to gain a better understanding of why owners and operators are starting to take on a less generous attitude toward their marketing departments, we examined the financial statements of approximately 2,000 hotels in PKF Consulting's Trends in the Hotel Industry database. For this article, it is important to note that franchise fees and national marketing assessments are excluded from property level marketing department expenses.

All Staffed Up

In 2006, salaries, wages and employee benefits, accounted for 57.4 percent of total marketing department expenses. Therefore, any movements in these cost categories will have a significant impact on a hotel's marketing budget.

Following the recession driven labor cuts of 2001 and 2002, hoteliers have re-staffed their sales force in an effort to capture group business and implement yield management strategies. By 2006, most properties were once again fully staffed and the re-hiring binge ended. During the year, total labor related costs within the marketing department grew just 2.8 percent, the lowest percentage increase since 2002.

Similar to the pattern observed in other departments, the growth in employee benefits outpaced the increase in salaries and wages. In 2006, marketing payroll costs grew 2.6 percent while employee benefits rose 3.7 percent. The stout rise in employee benefits can be attributed to higher insurance costs, obligated 401K participation, and rising social security benefits.

More Selling

While labor related costs have started to moderate, the increase in dollars spent in the 'selling' category of marketing expenses has been on the rise. The Uniform System of Accounts for the Lodging Industry defines activities such as trade shows, travel, and guest entertainment as selling expenses.

In 2006, selling expenses within the marketing department grew 9.2 percent, the greatest increase among all major cost categories in the marketing department. The trend of investment in more personalized, direct forms of selling has been a consistent over the past 10 years. In 1996, selling expenses represented just 20.2 percent of the total marketing department budget. This share increased to 29.7 percent in 2006.

Among the different property type categories, it is interesting to note that the greatest increases in selling expenses occurred among limited-service, midscale, and economy properties. Despite the lack of orientation towards group demand, it appears that the sales personnel responsible for these properties are still utilizing more personalized sales techniques to reach their transient customers.

Less Advertising

Once again, we have observed a decline in the unit-level dollars spent on hotel advertising. The cumulative expenditures for such items as collateral material, direct mail, in-house graphics, media buys, and billboards declined 0.8 percent in 2006. We attribute the continued decline in advertising dollars to enhanced support from franchisors and the efficiency of the Internet as a marketing channel.

Somewhat surprisingly, the greatest declines in property-level advertising were identified in the lower-rated economy and midscale chain-scale segments. Historically, these properties have relied heavily on advertising to reach such demand segments as highway travelers, seniors, and families on vacation. Given the great extent to which most of these properties are chain-affiliated, it appears that they have truly taken advantage of the new Internet related marketing channels available to them through their franchisor.

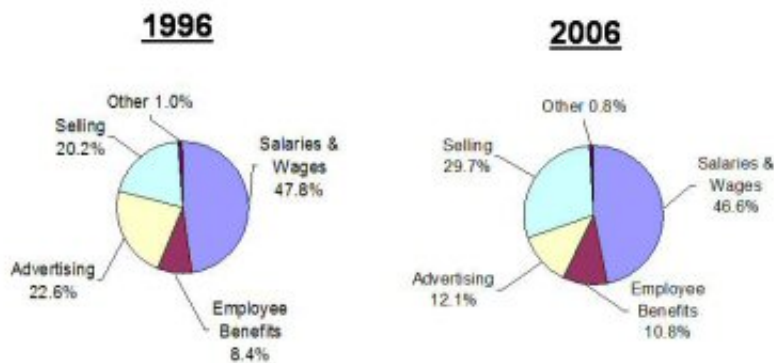
Conversely, we observed increases in the unit-level advertising expenditure being made by luxury and upscale properties. It should be noted that several of the relatively new 'select-service' brands reside within the upscale chain-scale segment. These trendy properties have become extremely popular among both business and leisure travelers. Given their orientation towards transient guests, the need to advertise becomes more important.

Another reason for the increase in advertising expenditures among hotels in the upscale and luxury chain-scale categories is the fact that several of these hotels have recently been involved in a transaction. Upon change of ownership and management, hotels frequently undergo renovations in an effort to reposition themselves. This change in market position requires additional advertising.

Dollars, Not Rooms

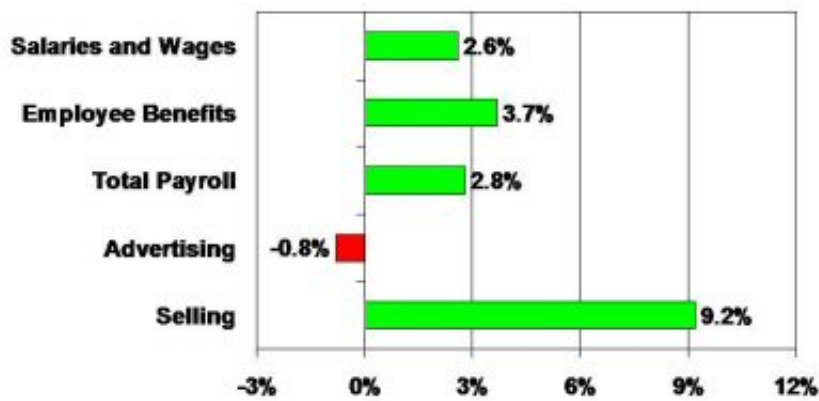
As we enter an expected period of prolonged prosperity, we believe marketing expenses will continue to increase, but at a more pace in line with the 2.7 percent long-term annual average. Because occupancy levels in most markets are above their long-term average, future increases in revenue will be generated mostly from increases in average daily room rates. Therefore, expect the focus of hotel sales personnel to shift from selling room nights to capturing more dollars. This will impact the distribution of expenditures within the marketing department.

Distribution of Unit-Level Marketing Department Expenses



Source: PKF Hospitality Research

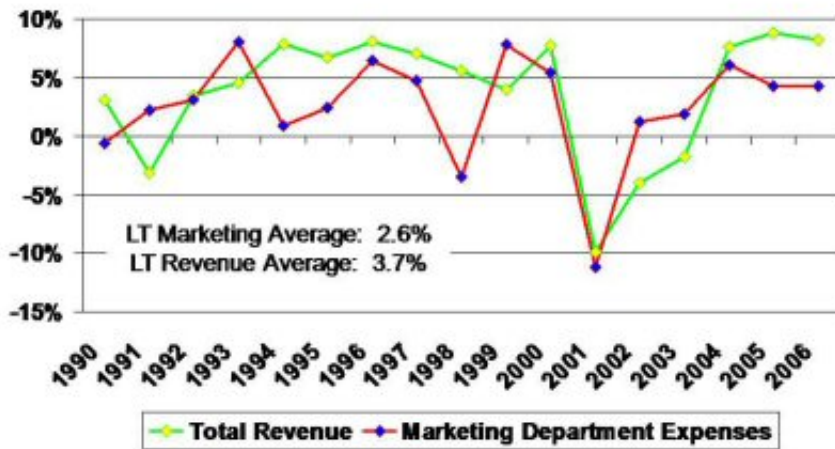
Change in Marketing Department Expenses 2005 to 2006



Source: PKF Hospitality Research

Marketing Department vs Total Revenue

Annual Change – 1990 to 2006



Source: PKF Hospitality Research

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