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Revenue Management Automation: Luxury or Necessity?

2010-05-11

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HSMIAI *The issue of whether automation is a luxury or a necessity was first put to me a long time ago, even before revenue management really existed for hotels. As I tried to walk into my first computer science class in college, I was confronted by a sign that directed us away from the lab, with its gleaming new cathode ray terminals (which had just replaced the old card punch stations), and instead pointed down the corridor to a regular lecture hall.*

By Bernard Ellis, CRME, CHTP, Managing Director - Americas, IDEaS - A SAS Company, and member of the HSMIAI Revenue Management Advisory Board

From HSMIAI's Revenue Management Advisory Board -- The issue of whether automation is a luxury or a necessity was first put to me a long time ago, even before revenue management really existed for hotels. As I tried to walk into my first computer science class in college, I was confronted by a sign that directed us away from the lab, with its gleaming new cathode ray terminals (which had just replaced the old card punch stations), and instead pointed down the corridor to a regular lecture hall. Once in our seats, my fellow students and I expressed bitter disappointment to the young instructor that we don't get to play with the computers yet. His face turned stern, and he said that the computers were NOT a toy, that computation time was expensive, and that we would not be worthy of touching a keyboard until halfway through the semester. He preached that it bordered on immoral to fritter away precious processing resources on superfluous tasks. In fact, he scolded, using computers is only worth the human and financial capital invested in them if the objective meets at least one of these three criteria:

- To give faster access to data than would be possible using paper files
- To automate a highly repetitive task, performing it more efficiently and accurately than humans could
- To do complex math that is beyond what can be done by hand or with a pocket calculator

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If it doesn't meet one of these objectives of "necessity," then using computers to perform the task would be a violation of my college's Honor Code, and by the way, the computers were programmed to automatically report violations to the Dean! Big Brother had arrived exactly on schedule (just in case I hadn't dated myself well enough for you.). If only my instructor had known what superfluous uses of technology the future would hold, and that Pac-Man was only the beginning!

While the cost of technology has decreased exponentially since those days, we all know that senior hotel executives still remain skeptical of its ROI, and that if they are going to be buying techie toys, they'd rather be putting them in the hands of their guests than those of their employees.

As a first test of whether revenue management automation is a luxury or necessity, it would be useful to see if, even with today's lower cost structure, it still meets my instructor's criteria (sorry, I can't remember his name. He had the personality of...well, a 1980's computer science instructor!). Let's talk it through.

To give faster access to data than would be possible using paper files. Performing revenue management requires analyzing changing booking patterns from the past, present, and future, on dozens of dimensions. This requires having snapshots of what business was on the books multiple times a day throughout the whole booking cycle, which can be as long as two to three years in a group hotel. Every year, technology makes more data available to help the cause, such as competitive pricing information and ancillary revenue contributions. And, those who are managing multiple properties will need to gather this from all of the hotels in their estate. This is a lot of data, which would be impossible to gather multiple times a day. Check.

To automate a highly repetitive task, performing it more efficiently and accurately than humans could. Besides the grunt work of collecting the data from multiple systems mentioned above, the next step is to use that data to forecast the hotel's unconstrained demand, i.e., how much demand does the hotel have at its disposal, when putting aside constraints imposed by their hotel's size, or any other constraints they might create through pricing and inventory controls. Given that almost all segments have now been trained to wait for the last minute internet deal, booking curves have constricted for almost everyone. So even if you have an Excel whiz on staff who could forecast like a PhD, whereas a hotel once only needed to reforecast once every few weeks, then once a week, it now requires forecasting and reforecasting multiple times a day in some markets, by market segment, by length of stay, and other dimensions. And, once new pricing and restrictions are determined, they need to be updated in multiple channels, for every arrival date into the future. It's no longer feasible for humans to keep up with this repetitive task in most markets, and it needs to be automated. Check.

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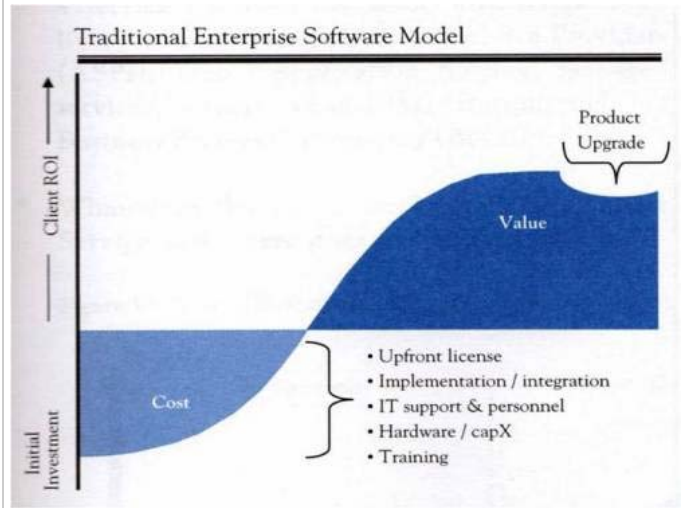
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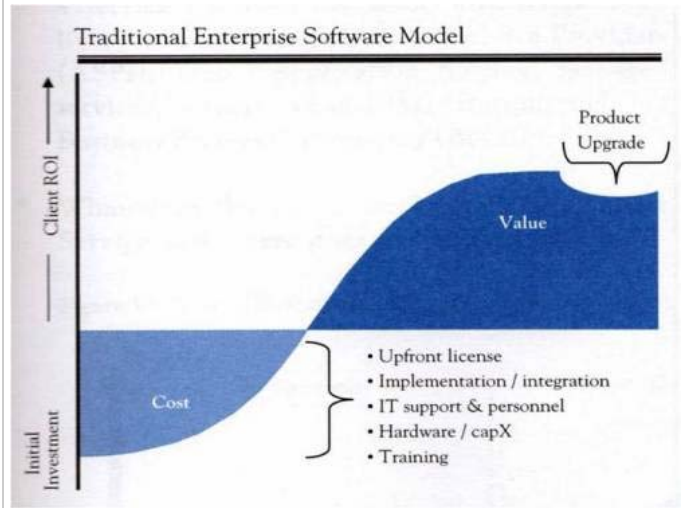
To do complex math that is beyond what can be done by hand or with a pocket calculator. The next step after you have a forecast of your unconstrained demand, which entailed some heavy math on its own, is to figure out what's the optimal mix of that business to accept, and at what price. Most people would agree that accepting the optimal mix of business, versus accepting demand first-come-first-served, will get you at least 4-6% higher RevPAR, and often a lot more than that. Of course these days, it's not usually a question of who to say "no" to -- you're going to say "yes" to everybody! The key question is: what is the optimal price to quote them to maximize your chances of getting the booking? While not everyone is a forecasting guru, almost no one can do an effective, timely optimization exercise without the help of automation, and figuring out at what point more discounting will not stimulate more demand is definitely a job better suited for an emotion-free computer. Check.

OK, so it meets my old instructor's definition of being a necessity, but we've been dodging the question of how much the technology actually costs. Early generations of revenue management automation required such a high up-front investment, that it was unaffordable by the masses, just like yachts and mansions, and therefore was a luxury by definition. The following graph shows what a leap of faith it was to make such a high up-front investment, then wait for the value to come along later, only to lose some of it again when re-investments needed to be made in hardware and software upgrades:



Source: TripleTree

Those days are over. Given that industry-leading revenue management technology is now delivered as Software as a Service (SaaS), the up-front investment is lower, deployment is faster, and therefore the return comes much faster as well. This graph shows how SaaS differs from the traditional model:



Source: TripleTree

- (1) Pay-as-you-go lessens the severity and upfront cost and risk. This shaded area is far smaller than what we saw in the traditional enterprise software model.
- (2) And (3) show that Rapid deployment results in a quicker risk adjusted return and #3 shows an accelerated use of the technology with deployments which are generally less than three months, sometimes much faster.
- (4) You have predictable operating costs rather than uncontrollable and costly maintenance so application performance can be much flatter.
- (5) It eliminates costly delays with future product version upgrades; there is no dip as seen in the previous chart due to costly delays.

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So, not only is the up-front investment lower, but the payback usually happens well within the first year of deployment. So, if you were to look at both the luxuries and necessities you have purchased in your life, how often was this the case?

About the Author

As IDEaS' Managing Director for the Americas, Bernard Ellis is responsible for all sales activity in the region. Bernard joined IDEaS following a successful tenure at SynXis where he was the Senior Vice President of Strategic Accounts and Channels. Prior to that, Bernard was an executive with Micros-Fidelio, where he managed sales for several major accounts. Bernard is a graduate of the College of William and Mary and holds a Masters degree from Cornell University's School of Hotel Administration. He sits on the boards of HSMAI's DC Chapter and Global Revenue Management Special Interest Group, as well as the advisory board for Cornell Hotel School's MMH revenue management career track. He also represents IDEaS on the AH&LA Technology and E-Business Committee. He is based in Washington, DC and can be reached at bernard.ellis@ideas.com

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