PRICING

IN

THE HOTEL INDUSTRY

(a theoretical and empirical investigation)

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SYNOPSIS

The aim of this thesis is to investigate the present procedures used for making price decisions in the hotel industry and to explore the potential use of price as a competitive variable.

Chapter I is a general analysis of pricing in theory and practice; this involves a critical review of current literature; an analysis of the economist's approach; a survey of the practices and procedures used in industry and an examination of price as a competitive marketing variable.

Chapter II outlines the characteristics and structure of the hotel industry as a basis for identifying the problems involved in price decisions and in order to evaluate the potential role of price as a competitive variable in this industry.

Chapter III reviews the pricing practices used in the hotel industry: actual methods, dynamic trends, spatial and quality variations are explored. The second half of the chapter contains the results of an empirical survey and describes the processes by which pricing decisions are made in the industry and records the problems encountered.

Chapter IV is normative in nature and suggests a procedure for approaching price decisions and the criteria that should be used. The potential and limitations of price as a competitive variable in various market situations is emphasised. The analysis is mainly at firm level.

Chapter V reviews the importance of marketing and role of marketing variables within the industry and enumerates broad changes in attitude that will be necessary at an industry level if optimal price decisions are to be achieved.
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CONTENTS

LIST OF TABLES .......................................... (i)
LIST OF FIGURES ......................................... (ii)
INTRODUCTION ........................................... 1
CHAPTER I: A REVIEW OF PRICING IN THEORY AND PRACTICE .. 3
CHAPTER II: THE STRUCTURE AND CHARACTERISTICS OF THE HOTEL INDUSTRY .................................................. 30
CHAPTER III: PRICING PRACTICES IN THE INDUSTRY ........... 53
CHAPTER IV: A RATIONAL APPROACH TO PRICING IN THE HOTEL INDUSTRY .................................................. 87
CHAPTER V: CONCLUSIONS .................................. 134
APPENDIX .......................................................... 138
BIBLIOGRAPHY .................................................. 164
<p>| Table 2.1 | Summary analysis of the major forms of accommodation in the U.K. | 32 |
| Table 2.2 | Distribution of Hotel Capacity in U.K. | 40 |
| Table 2.3 | Distribution of Hotels and Bedrooms between regions and locations | 42 |
| Table 2.4 | Hotel Establishments in U.K. by size | 45 |
| Table 2.5a | International Revenue patterns | 48 |
| Table 2.5b | International Expenditure patterns | 49 |
| Table 2.6 | Expenditure patterns for Hotels in U.K. | 50 |
| Table 3.8 | Price trends in Hotels | 61 |
| Table 3.9 | Single-double room price trends comparisons | 62 |</p>
<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>Breakeven Chart (Traditional)</td>
<td>23</td>
</tr>
<tr>
<td>1.2</td>
<td>Breakeven Chart (Contribution Approach)</td>
<td>24</td>
</tr>
<tr>
<td>4.1</td>
<td>Suggested layouts for assessment and analysis of pricing decisions</td>
<td></td>
</tr>
<tr>
<td>4.1a</td>
<td>Previous years performance</td>
<td>113</td>
</tr>
<tr>
<td>4.1b</td>
<td>Projected performance with rigid policy</td>
<td>114</td>
</tr>
<tr>
<td>4.1c</td>
<td>Projected performance with flexible policy</td>
<td>115</td>
</tr>
<tr>
<td>4.2</td>
<td>A visual presentation of the external and internal environment and their impact on pricing</td>
<td>119</td>
</tr>
<tr>
<td>4.3</td>
<td>A framework for reappraisal</td>
<td>133</td>
</tr>
</tbody>
</table>
Economists, management accountants and marketing specialists have directed most of their research efforts into investigating the problems encountered in manufacturing rather than service industries. This concentration of energy is reflected in published literature. The tertiary sector, however, is increasingly important and a large proportion of the U.K. work force is employed in this sector. It is necessary, therefore, to question and appraise whether the analysis and approaches developed for manufacturing industries are adequate to meet the needs of service units. Service industries are diverse in form and structure and in order to facilitate analysis in depth it was decided to concentrate on one industry. There were two prime reasons for selecting the hotel industry. Firstly, the hotel industry is under-researched and invites analysis. Secondly, the characteristics and supply and demand condition of the industry present decision makers with difficult and tantalising marketing problems.

One aspect of marketing has been singled out for specific examination - the price decision. Economists have given a great deal of attention to the theory of price. The concentration of their energy and effort in this field may be attributed to historical, technical and social factors. Kotler (1) points out that the characteristics of the economy when economics first developed as a systematic theory ensured that "the major variable differentiating competitive offerings was price" and that price had an "additional sensitivity as a marketing variable because of the low level of per-capita income". Also technically owing to the difficulty of measuring qualitative changes "price has more tractable properties

from the point of view of analysis". The social argument hinges on the fact that the "price mechanism affords an elegant rationale for the efficiency of a competitive free-enterprise system" and so on welfare grounds price determination has been given a central role.

Economists recognise that other marketing variables influence demand patterns: the importance and significance of the various forms of non-price competition have been investigated though the success has been limited owing to the analytical difficulties encountered. Throughout this thesis attempts have been made to encompass the other variables where relevant.

Though pricing in general has received a great deal of attention little empirical work has been conducted into the actual process of pricing. Silbertson in his survey of 'The price behaviour of firms' (1) states that "although many industry studies include a discussion of prices, it is comparatively rare for the process of pricing to be investigated in any detail .... this is partly because many, if not most, industry studies undertaken by economists have deliberately been carried out from the 'outside in' so to speak, i.e. they have concentrated on objective data rather than on material derived from interviews etc.".

The aim of this thesis is to analyse the problems facing decision makers in this industry and to examine critically whether the practices and procedures used enable optimal price decisions. Chapter IV which is normative in nature involves a synthesis of the disciplines of economics, management, accountancy and marketing.

CHAPTER I

A REVIEW OF PRICING IN THEORY AND PRACTICE

This chapter is a survey of pricing in theory and practice. It is of a general nature and serves to illustrate the different approaches to pricing at both the theoretical and practical level. It has been divided into three sections:

Section A examines and assesses the economist's approach to pricing problems;

Section B identifies and evaluates the pricing procedures used in practice;

Section C analyses the scope and potential use of price as a marketing variable.
SECTION A: THE ECONOMIST'S APPROACH TO PRICING DECISIONS

Economists base their analysis of price behaviour on the assumption that the firm's objective is profit maximization and that the individual firm can estimate its demand and cost functions.

The pricing decision is an integral part of the output level decision which can be solved using differential calculus.

If \( TR = f(Q) \) and \( TC = f(Q) \), where \( Q \) equals total production over a period of time, \( TR \) equals Total Revenue and \( TC \) equals Total Costs, then

\[
\pi_n = TR_n - TC_n
\]

where \( \pi_n \) = profits when \( n \) units are sold.

To find the output level \( Q \) that maximises profits one needs to differentiate with respect to \( Q \) and then equate to zero.

\[
\frac{\partial \pi}{\partial Q} = \frac{\partial TR}{\partial Q} - \frac{\partial TC}{\partial Q} = 0
\]

The optimum level of output therefore occurs when

\[
\frac{\partial TR}{\partial Q} = \frac{\partial TC}{\partial Q}
\]

(i.e. when the firm's marginal revenue equals its marginal cost (1))

providing that

\[
\frac{\partial^2 \pi}{\partial Q^2} < 0
\]

which ensures that the firm has reached a maximum rather than a minimum profit level.

The optimum output having been determined the selling price is determined by substituting \( Q \) into the relevant demand function for the individual firm. The nature of the demand function will depend

(1) (i.e. Revenue derived from extra unit sold equals the costs involved in producing it.)
on the competitive structure of the industry in which the firm operates.

The conduct and performance of firms is therefore closely related to the market structure and for this reason we need to analyse the main determinants of market structure before proceeding further.

Factors determining market structure include: the number of buyers and sellers in the market; the nature and degree of differentiation of the product or service; the consumers' awareness of price/quality differentials and their potential mobility. The nature of the production function also exerts a significant effect on market structure. Industries where for cost reasons the optimum size of the firm is large relative to total industry demand will invariably have a high degree of concentration while industries where increasing returns are absent or insignificant experience less concentration and usually a higher degree of competition.

Perfect competition and monopoly are the two limiting types of market structure.

A perfectly competitive industry would be marked by the following characteristics: a large number of sellers and buyers would be producing and purchasing a homogeneous product; information regarding prices and quality would be freely available and there would be no barriers or limitations on entry into or exit from the industry.

Under these conditions price would be determined by the market and the individual firm would produce at the point where marginal cost equalled price. In the long run price would be equal to the minimum long run average cost so that firms would earn 'normal profit' only. In the short term if market price increased following a change in demand, temporary above normal profits would
be feasible until new firms entered the industry. The firm however would be concerned with output rather than price decisions and because they could in no way manipulate market demand they may be regarded as 'price takers' rather than 'price makers'.

It is extremely unlikely that these conditions would exist in the real world and the model is used primarily as an analytical device for comparative purposes.

Monopoly exists when the industry comprises only one firm. In reality, because some sort of substitute is invariably available, pure monopoly does not occur. Theoretically however the monopolist is faced with a falling demand curve and given this fact he can either decide his output level or price, but not both, unless he is willing to restrict his profits. He can however earn excess profits over the long run by curtailing his production although the extent to which he exploits consumers may often be influenced by political considerations and the fact that too high a price might provide incentives for others to try and provide or develop close substitutes. Self-imposed constraints therefore often curtail his short run activity. Simon and Freimer (1) have aptly pointed out that "an understanding of monopoly pricing is important because in competitive situations the firm strives towards the goal of being able to price as a monopolist would".

In the real world most firms operate in a market structure between these two extremes. This area is covered by the general term 'imperfect competition', where varying degrees of competition and freedom are experienced by firms. The number of firms relative to the number of buyers, spatial factors and the degree of product differentiation will be the prime variables influencing the amount of

effective competition. Price and non-price competition will be used according to the particular characteristics of the industry but in most cases there will be great emphasis on differentiating one's product from that of one's competitors. The firm is then able to decide its own price/output strategy within the limits imposed by its most effective competitor.

Oligopoly is the term given to competition among the few where the interdependence of firms' behaviour is the inevitable problem. Firms have to consider not only the repercussions of their own actions but also the response of their rivals. Scherer (1) illustrates the problem:

"When either pure competition or monopoly prevail - there exist clear cut solutions to the firm's price and output decision problem, assuming only that managers seek to maximise expected profits and that they hold definite (though probabilistic) expectations concerning future demand and cost conditions. With rivalry among the few however this is not so. Each firm recognises that its best choice depends upon the choices that its rivals make. The firms are interdependent and they are acutely conscious of it. Their decisions depend then upon the assumptions they make about their rivals decisions and reactions and many alternative assumptions might be entertained."

The complexity of the situation emerges and there is no oligopoly theory at present that will explain satisfactorily the behaviour of firms in such an uncertain market situation. Pure oligopoly needs to be distinguished from differentiated oligopoly. In the former the lack of differentiated products makes interdependence very marked and room for price variation is limited

but in the latter the degree of freedom is much greater. Theories that have been developed do provide interesting insights into behaviour patterns, although they can only explain partially real world activities.

It is often suggested that the oligopolistic group will maximise joint profits and that this can best be achieved by some form of explicit or tacit cartel-collusion type policy. Apart from the illegality of such operations they are difficult to maintain as the firm willing and able to reduce price without its rivals knowledge will be handsomely rewarded in terms of increased business. However, a 'modus vivendi' may well be arrived at and maintained. In this situation the dominant firm may act as the price leader, and other firms will follow his lead and example.

C.J. Hawkins (1) points out that price leadership behaviour in oligopoly situations is well supported by empirical evidence and that it provides a practical solution to complex interdependence problems. He also stresses that in industries where fixed costs are high firms may have learned from experience that price wars benefit none of them. "Each can match the other's price cuts in the short run since it pays no one to cease production even if prices are cut below full cost, so long as variable costs are covered. Only if price is kept below full cost until existing plant and machinery become obsolete or fall apart does it pay anyone to leave the industry. And that may take ten years or more. Since the discounted value of profits ten years hence is low compared with profits in the near future, the net present value of the price-war policy is not likely to be very attractive. So firms may learn that, in capital-intensive industries at least, policies of 'live and let live' make a good deal of sense. Accepting a price leader is perhaps the most obvious and simplest of 'live and

let live' policies." The implication of this for Hotels will emerge in Chapters III and IV.

Shubik (1) using a games theory approach has stressed the strategic aspects of the behaviour of firms in this situation and explained how tests of strength, price wars, aggressive and defensive strategies may be utilized. Generalization however in such a situation is dangerous and must be treated with care, though it may well prove useful for particular cases. Baumol (2) while examining oligopoly points out,

"That in day to day decision making management often acts explicitly or implicitly on the premise that its decisions will produce no changes in the behaviour of those with whom they are competing".

He goes on to state,

"I am not arguing that management inhabits a fool's paradise in which interdependence is never considered. In making its more radical decisions, such as the launching of a major advertising campaign or the introduction of a radically new line of products, management usually does consider the probable competitive response. But often even in fairly crucial decisions and almost always in routine policy making, only the most cursory attention is paid to competitive reactions. This apparently dangerous attitude does not usually lead the businessman into serious difficulty because, I believe, his more ordinary decisions are rarely met by prompt aggressive countermoves of the sort envisaged in many of our models".

Baumol attributes this behaviour to the complexity of large

organisations, where the multiplicity of departments and the frequently divided and ill defined responsibility and relationships between centralized control and departmental authority is such that decision making becomes a lengthy process and "is too clumsy and too slow moving an apparatus for the effective interplay of strategy and counter strategy amongst competing firms". This attitude is probably valid if the market share of the firm in question is in no danger of being eroded away by a competitor.

Another facet of oligopoly worth noting is the fact that there is often a rigidity of prices. The rigidity may be explained in terms of the administrative expense and inconvenience of frequent price changes, but this is not wholly convincing. Kinked demand curve theory has also been utilized: firms are assumed to follow price cuts by their rivals but to ignore price increases. The demand curve does not therefore have constant elasticity and so the marginal revenue curve has a gap at the kink in the demand curve. A wide range of MC equal to MR combinations is therefore possible and so maximum profits can be achieved even without alterations in prices.

The validity of this explanation however is questionable: partly because of its unrealistic assumptions and also because it can only apply if firms face a very high degree of uncertainty. Once firms have become accustomed to their rivals and learned by experience then the degree of uncertainty would be reduced. Even if it was accepted that the kinked demand curve was a satisfactory explanation of why price does not change frequently it still does not explain why prices were fixed at that level in the first place.

Bain (1), Sylos-Labini (2) and Modigliani (3) have all analysed

the significance of 'barriers to entry' on the pricing behaviour of firms in oligopoly situations. The concept of 'limit pricing' is used but because so much depends on the nature of the barriers to entry generalization is difficult. Yet empirical investigation does seem to suggest that "the price tends to settle at a level immediately above the entry-preventing price of the least efficient firms which it is to the advantage of the largest and most efficient firms to let live". Sylos-Labini also concluded that where the cost variations were small the full cost principle acted as a guide and that costing margins varied according to the level of demand and the effectiveness of entry barriers. The choice of a limit price is really an investment type problem. The firm forgoes profits or cash flows in the short run in the expectation of higher cash flows in the long run. Galbraith's (1) "countervailing power" argument is also relevant here because if firms are faced with large powerful buyers the threat of their possible entry in the future will have a limiting effect.

Assessment of the Economist's Approach

The economist's approach has received a great deal of criticism, primarily on the basis of its assumptions and abstraction from reality. Kotler (1) argues that the economist's pricing models are based on "several highly restrictive assumptions which severely limit its applicability to actual pricing problems" and R. Cassidy Jnr. (2) commenting on economists' pricing models states that "price making is simply not conducted in this way in any real situation about which I have knowledge".

Firstly, the assumption that all firms maximise profits has received a great deal of attention and criticism. Alternative motivational forces are observable in practice and have been identified by numerous writers.

Machlup has illustrated the range of the possible "utility function" that may be considered by management, including variables contributing to the 'pride', 'prestige', 'self-esteem', 'conscience' or 'comfort' of the individual manager. The list could include the following items: total profits; growth rates of profits; rate of profit to investment; total sales and growth of sales; increases in market share; dividends paid out; retained earnings; investment; salary levels, bonuses, stock options and expense accounts; expenses for PR, Research and Development, and advertising; free time for leisure and other recreational purposes, etc. The list though not intended to be exhaustive illustrates the wide range of motivational forces that may be influential in any one firm but they are difficult to incorporate into models that are required to predict the behaviour of firms. Machlup however goes on to argue that for the purposes of competitive theory all assumptions other

(1) P. Kotler, op.cit., p.519.
than profit maximising are "irrelevant" because the competitive threat from potential newcomers ensures that the profits of firms are invariably only about "normal", so that profits below the maximum obtainable would in fact be net losses in an economic sense. Also if the number of firms is large "it suffices if some of them react as posited by the theory". (1)

Hague (2) however presents four arguments to explain why firms find it hard to maximise profits in the way economists assume. Firstly, there is ignorance about the 'present position of the firm' relative to other firms in the industry. Secondly, there is a great deal of uncertainty about the outcome of decisions taken. Thirdly, even if the necessary information is available there are difficulties in organising complex business organisations to take the correct decisions (especially within the time available). This point of view is reinforced by the Cyert and March (3) argument that the modern firm is typically run by a collection of individuals who though possessing specific goals are forced through the group decision making process to accept compromises. Also the division of ownership and control between shareholders and managers will obviously influence the motivation of the decision makers. Fourthly, Hague argues that human beings find multi-variable relationships difficult to handle.

These four arguments suggest that even if firms adopt a profit maximizing directive that they would find it extremely difficult to implement it in practice. Firms are therefore often forced to accept a satisficing approach, specifying a minimum level of

achievement for the objective that they wish to follow.

A second criticism of the economist's approach is that the demand curve is assumed to be measurable. In reality the demand level is not independent and can be influenced and altered, sometimes quite considerably by the firm using various sophisticated promotional techniques. This interdependence of price and other competitive parameters means that they need to be considered simultaneously. It is also dangerous to use a price elasticity measure and apply it to a wide range of potential price changes. Elasticity varies often significantly over the length of the demand curve and so prediction of the effects of changes in price or other variables is hazardous. The demand function is unlikely to be continuous and in practice may be stepped or discrete. Calculation of marginal revenue will invariably be extremely difficult and often impossible. Any attempt to measure marginal revenue more precisely will inevitably involve an increase, and sometimes a substantial increase, in information costs so that the benefit of this information would need to be carefully assessed.

A third problem is that the calculation of marginal cost is not an easy matter, and for the multi-product firm will at best be arbitrary, although the use of recent accounting techniques facilitates more accurate assessment. Economists models, however, concentrate in the main on 'one-product' firms - an unrealistic assumption in the modern world.

A fourth argument by Oxenfeldt (1) stresses that price theory "offers basically static models which are powerless against the problems in which changes over time are central". The emphasis on short-term profit maximization and the assumption that short-term

(1) A. Oxenfeldt, 'Models of Markets', p.80. (op.cit.)
profit maximization will lead to long-run profits ignores the fact that in a dynamic world the actions taken in one time period affect subsequent time periods significantly.

Fifthly, consumers are not as rational as economists lead us to believe. Apart from the fact that information is not always readily available regarding price or the availability of substitutes, restrictions on mobility and the cost of travel limits the centres of purchase. Also, and perhaps to an increasing extent in the modern world, time itself may be the limiting factor forcing consumers to accept a second best type of situation.

The consumer is also influenced by habit, fashion and advertising.

These criticisms are sufficient to cast a grave doubt on the practical problems of using the economist's approach but before proceeding any further it is now necessary to turn to the real world and examine the procedures actually used by firms when taking pricing decisions. A more accurate and realistic assessment of the economist's approach can then be undertaken.
SECTION B: PRICING PROCEDURES IN PRACTICE

Inevitably the problems associated with the economist's approach have necessitated the evolution and use of much more practical pricing procedures based primarily on cost rather than demand considerations.

Hall and Hitch in 1939 advanced the argument supported by empirical evidence that firms fix their prices on 'full costs' plus a margin for profit. Numerous studies, e.g. P.W.S. Andrews, D.C. Hague, R.H. Barback have investigated the role of cost plus pricing as an explanation of the pricing process used in industry. At some points much controversy has been aroused but Silbertson (1) after surveying the disputed area concludes that "the procedure of calculating prices very often starts with an average cost type of calculation but the qualifications that arise are concerned with the next stages of the process, including the exact method by which full costs are calculated".

An examination of the main pricing procedures used in practice follows: for the sake of analysis these are grouped under three headings according to their main distinguishing procedural characteristics. It is appreciated that this is somewhat arbitrary and that there may be individual cases where classification under these headings may prove difficult but they correspond broadly to real world situations.

I. COST PLUS PRICING

II. TARGET RATE OF RETURN PRICING

III. CONTRIBUTION PRICING

A detailed analysis of each of these approaches follows:

I. COST PLUS PRICING

This procedure involves a calculation of costs plus a percentage

mark up for profit. The costs used may be actual costs (i.e. current costs), expected costs (i.e. forecast or anticipated costs), or standard costs (i.e. budgeted estimates of costs at the ‘optimum’ level of output). Total costs may be averaged to provide an average cost figure and so include direct and indirect costs without distinguishing between them. In some industries identifiable direct costs are calculated separately, then a given percentage is added on to cover overheads and subsequently a percentage profit mark up is added, or these last two stages may be combined and a given percentage mark up added to direct costs.

In the Hotel and Catering industry the normal procedure for food and beverage pricing is to express the profit mark up in terms of gross profit margins: gross profit representing sales revenue minus direct material input costs. A similar procedure is used in most retail distribution outlets. A sales price of 100p, with a material cost of 25p, representing a 75% gross profit margin, i.e. a 400% mark up on cost.

The most significant disadvantage of cost plus pricing is that it fails to give sufficient attention to demand and the amount that consumers might be willing to pay for the product or service in question. If the percentage mark up is adjusted continually to allow for demand variations it could be argued that this objection to cost plus pricing is not relevant. From empirical studies though it appears that the percentage mark up is rarely finely adjusted to correspond with estimated demand variations.

Another objection to cost plus pricing is that it fails to take into account the nature and extent of competition facing the firm. This together with the previous point means that the shape and nature of the demand function are largely ignored. Kotler (1) points out

(1) P. Kotler, op. cit., p. 524.
that "any model that ignores current demand elasticity in setting prices is not likely to lead, except by chance to the achievement of maximum profits, either in the long or short run. As demand elasticity changes as it is likely to do seasonally, cyclically or over the product life cycle, the optimum mark up should also change. If mark up remains a rigid percentage of cost (or selling price) then under ordinary conditions it would not lead to maximum profits."

This viewpoint is reinforced by Cymax (1):

"One of the major weaknesses of conventional pricing is that it ignores demand. The point at which a price is set, relative to the price of a competitor's product, will have an important effect on the sales volume, a price decision must therefore be closely linked to an assessment of the distinctiveness of a company's product and the sales volume that the company wishes to achieve and this in turn depends on some assessment of the buyers' needs."

Kotler (2) however does point out "that under special conditions, however, a rigid mark up at the right level may lead to optimum profits. The two conditions are that the average (unit) costs must be fairly constant over the range of likely outputs and price elasticity must be fairly constant for different points". In reality it is hard to envisage these conditions being met and even if by chance they did coincide it is likely that over the long run dynamic factors would alter the relationships and profits would be adversely affected.

Businessmen often justify the use of cost plus pricing in that by this method all costs will be covered over the long run. It is therefore felt to be a secure method ensuring that bankruptcy will not

(2) P. Kotler, op.cit.
occur. In reality this security will only be possible if sales volume is equal to or greater than normal capacity or the estimated capacity figures used initially. Average cost pricing can therefore sometimes serve the businessman's interests very badly, e.g. high prices might be charged because costs are high at the current low output levels - whereas lower prices might increase the quantity demanded and therefore reduce unit costs. This security aspect is often reinforced by another belief that cost plus pricing will ensure that the firm will not easily be undercut unless it is grossly inefficient and that in times of inflation the firm can pass on cost increases without worrying unduly about his rivals' reactions. These arguments are unsatisfactory and do not in reality give the element of security that the businessman requires.

Much emphasis, especially by businessmen, is given to the fact that the technique utilizes the concept of 'fair profit' and ensures that the consumer is not exploited. In actual practice it may well mean that the consumer's welfare is adversely affected. For example the absorption approach will inevitably involve an arbitrary apportionment of fixed costs if the firm is a multi-product firm and this may involve the consumers of one product unwittingly subsidizing others. Not only does this result in a misallocation of resources within the firm but it does mean that on welfare grounds the price mechanism is not functioning freely to allocate national resources.

Another argument advanced is that this technique is beneficial to consumers in that it tends to ensure relative stability of prices. Consumers it is said prefer to have consistency rather than perpetually fluctuating prices. Very little research has been undertaken on this question of consumer aversion to price changes and so it is difficult to give an objective opinion on the validity of the argument. It is tempting to conclude that this is the
businessman looking for a rationale to cover the fact that on administrative grounds it is nearly always irksome and often extremely expensive to alter prices frequently.

Pappas and Brigham (1) conclude their survey of cost plus pricing by saying that "Cost plus pricing has long been criticised as a naive pricing technique based solely on cost considerations, the wrong costs at that". It does however continue to be used by the hard-pressed businessman and providing that demand is not volatile and the degree of competition not too fierce it may well enable him to achieve a satisfactory level of profits. This would tie in with the satisficing objective that we have previously discussed. In many industries rule of thumb methods based on a cost plus approach tend to be developed. In the Hotel industry one such traditional method is that based on the assumption that for every £1000 spent on a hotel bedroom a room rate charge of £1 per night should be levied. So that a 100-bedroomed hotel built at a cost of £1m averages £10,000 a room and therefore £10 per night on average should be charged. The previous points in the critique of cost plus methods are obviously relevant for these simple rule-of-thumb approaches.

Therefore, if a firm wishes to maximise profits or even register an above-average performance the above pricing methods will not permit this and alternative techniques and procedures will need to be employed.

II. RATE OF RETURN PRICING

This method emphasises the fact that profitability in the form of a specified return on capital employed is a major objective and that this is the main starting point for pricing determination. An

estimate of anticipated turnover is therefore required and from this allowing for the fixed costs that have to be covered a percentage addition to direct costs is calculated. The Hubbart Formula used widely in the U.S.A. and developed for the American Hotel-Motel Association is based on this approach. It involves calculating the required level of profits and then working backwards from an expected sales forecast to calculate the necessary profit margin required from the Hotel in total and then a departmental breakdown according to the sales mix and revenue sources. This form of target pricing does not remove the arbitrary element in setting the profit mark up percentage. Demand is largely ignored and most of the criticism previously levelled at cost plus pricing is again relevant.

No sales forecast can estimate the level of demand without taking price into consideration; yet in the Hubbart formula a sales forecast is necessary in order to determine price. This obviously involves a circular inter-dependence between occupancy and the price level. It would only be a suitable technique if demand was entirely non-responsive to price - a highly unrealistic assumption for most hotels.

It is however worth mentioning that this target rate of return procedure was that most frequently quoted by Kaplan, Dirlam and Lanzillotti (1) in their empirical investigation of pricing objectives and procedures in big business in the U.S.A., but none-the-less if the businessman wishes to use his resources efficiently other pricing procedures will need to be adopted.

III. A CONTRIBUTION APPROACH

From empirical studies it emerges that many firms use cost plus

pricing techniques in order to ensure that in the long run all costs, particularly fixed costs, are covered. J. Arnold (1) has pointed out that "it is accepted that fixed costs must be recovered. But the best way of recovering them may not be by allocation but by a policy of accepting projects that cover and more than cover their associated incremental costs. This should ensure that the firm achieves the largest possible surplus or contribution from which to pay fixed costs". Contribution may be calculated in terms of:

Total contribution = Total sales revenue minus total variable cost

or by using,

Unit contribution = selling price minus variable cost at given output level.

An accurate delineation of the fixed and variable cost behaviour patterns for the individual firm under consideration is therefore essential. This is a difficult but not impossible task though it does mean that the accountant has to reformulate his normal presentation of data.

J. Arnold (2) states "the fact that it may be technically difficult to distinguish between fixed and variable expenses and to relate them in a precise way in developing contribution analysis techniques is in no way a justification for not using the best technique available".

The contribution approach, unlike the absorption approach, lends itself particularly well to dealing with cost-volume-profit relationships.

Contribution sales analysis therefore permits a calculation of minimum short run prices and is especially valuable where demand

(2) J. Arnold, op.cit.
fluctuates or where spare capacity exists in the short run. The significance of the contribution approach to seasonal Hotel pricing will be developed in Chapter IV.

The use of breakeven charts can enrich the understanding of the relationship between cost, volume and profits. The use of breakeven charts depends on cost-revenue fluctuations being linear. Traditionally breakeven charts are presented by first drawing in the Fixed Costs and then the Variable Costs so that the Total Cost function is represented by line TCF. Total Revenue is then drawn and the breakeven point calculated by the point of intersection. Any volume to the left of point B means losses; to the right profits.

![Breakeven Chart - Traditional Approach](image)

**Figure 1.1 BREAKEVEN CHART - traditional approach**

If the procedure for including fixed and variable costs is reversed: variable costs being included first and then fixed costs added subsequently so that TCF is parallel to VC. The breakeven point is obviously still at B as in Figure 1.1 but the shaded area now represents Total Contribution.
Figure 1.2  BREAK EVEN CHART - contribution approach

Unless average variable cost and price (average revenue) are constant over the range of output under consideration, the contribution margin or unit contribution will vary. Therefore where variable costs change with output or where price falls as output increases it is often easier and more useful to deal in terms of Total Contribution rather than unit contribution. This is especially relevant if the functions are non-linear. (This shall be re-examined in Chapter IV.)

The three main cost orientated approaches to pricing policy have now been examined but cost, though an important regulatory factor (in particular for minimum price decisions) cannot be taken as the sole determinant of price.

Other considerations such as the nature and extent of competition and the characteristics of the industry will be extremely influential in determining the optimal price policy. These will be enumerated in the next chapter but before proceeding with the specific analysis of the Hotel Industry it is worth pointing out that price itself is a marketing tool and so it is necessary to examine the role that price plays in the real world as a marketing variable.
SECTION C. PRICE AS A MARKETING DEVICE

Price is one of the elements in the total marketing effort. D.V. Harper (1) points out that "price may be a neutral, moderately neutral, moderately active or an active instrument in the marketing program".

The extent of its importance will in general depend on the industry in question, the characteristics of the consumers including their attitude and awareness of price and the feasibility of using other marketing devices such as product/service variation, advertising and other forms of sales promotion.

One area where price is normally an active instrument of the marketing policy is in the launching of new products or services. Two alternatives present themselves. A low initial price may be charged so that the market will be captured and the entry of new firms over the long run will be inhibited. This is referred to as "price penetration" policies and involves a low mark up but high turnover. The alternative is referred to as a "market skimming policy" where a high initial price is charged and is a suitable policy only if demand is inelastic and the product/service differentiated is appealing enough to attract new customers.

Silbertson (2) has pointed out that this latter policy is a form of dynamic price discrimination and that "the more dynamic the industry, the shorter the pay-off period and the higher the price". Eventual price decreases are usually inevitable. A high level of judgment and awareness of the industry in question are necessary before a prescription can be made for the most suitable policy.

Price discrimination may also be used to increase profits substantially by levying prices that reflect different consumers

(2) Silbertson, op.cit., p.527.
preferences. "The essence of price discrimination is charging on
the basis of what the market will bear" (1). For price
discrimination to be effective two conditions need to exist. Firstly
buyers must be separated on a personal, group, geographical or time
dimensional basis so that the exchange of information becomes
difficult and secondly that resale of the product/service must not be
feasible. Services, of course, fit this last condition particularly
well and examples of price discrimination can be found in many service
industries. For example, electricity is sold at varying prices
according to user classification (industrial/domestic) and the time
(night/day) of consumption; on the railways price discrimination is
used between first/second class fares, peak and off-peak periods.
Bus fare concessions are given to children and Old Age Pensioners
providing rush hour periods are avoided. All these differences rely
on market segmentation and allow for differences in demand
elasticities.

Price can also be used as a promotional tool. Emphasis on
'minimum' prices and the 'value for money' concept has in many
consumer goods industries and in the distributive trades attracted
loyal 'repeat' customers. Supermarkets attract customers to their
outlets by means of 'loss-leader' pricing. This aspect of 'bait'
pricing as it is referred to in the U.S.A. has often been criticized
on ethical grounds. Similar practices are used when advertisements
mention 'basic' prices so that consumers are attracted to investigate
further often to find that the essential extras mean that the
advertised price was an illusion. Price can therefore be used as a
psychological weapon.

Interesting work has been done by A.N. Gabor and C.W.J. Grainger (2)

(1) Silbertson, p.527, op.cit.
(2) Gabor and Grainger, 'Price as an Indicator of Quality',
Economica (Feb), 1956.
on the theory that consumers assess quality on the basis of price. They stress that "price serves as an indicator of quality with far greater frequency than is generally believed" and though Palda has criticised Gabor and Grainger on the grounds of the leading questions of their survey he concedes that "situations in which a higher price may actually increase sales by shifting quality perception are those in which a consumer suffers from a lack of information and proceeding on well substantiated experience with reasonably competitive markets, assumes that price bears a direct relationship to cost and so on, mutandis, to quality" (1). A.R. Oxenfeldt (2) also agrees that "customers forecast the benefit to be attained from a product as much by price as by any other cues available to them". The importance of this theory will be examined later when we examine the significance of price as a marketing variable for Hotels.

The marketing executive also needs to know the degree of price awareness that exists towards the service that is being offered and also the degree of price consciousness. This means that the consumer's ability to remember and to compare prices as well as their sensitivity towards price differentials is very important. Nystrom has stressed how the price image of any firm to a customer is essentially a relative concept and is derived through time by numerous comparisons with competing firms. Products or services that are consumed fast and frequently enable the consumer to be aware of prices and to form a price image of the firm in question but if the items or service are purchased infrequently the learning process is essentially slow and a price image difficult to establish. If the service is also differentiated consumers may find it almost impossible to be rational in the strict economic sense and in this situation price may

(2) A.R. Oxenfeldt, p.216, 'Pricing Issues in Theory, Practice and Public Policies.'
well be again interpreted as an indicator of quality. A maximum and minimum level of price may therefore emerge and a threshold type of sensitivity analysis will be necessary to decide the band or range within which price fluctuations will be possible.

If the expected or threshold price limits are narrow and if they fall beneath the price that would emerge from normal cost-orientated pricing procedures then a fundamentally different approach to pricing decisions may well have to be utilized.

This would involve reversing the normal procedure of moving from costs to price and to commence with the 'approved' price and to work backwards adjusting the product/service quality or design to ensure a satisfactory profit margin. This procedure is called BACKWARD PRICING and is particularly suitable for service type industries where the elements of service, facilities etc. can often be fairly easily adjusted. This is a particularly useful marketing strategy if competition is keenly felt or where a competitor with a low cost structure is dictating market price levels. Superficially it may appear that pricing is taking on a passive rather than an active role but in reality price is acting as an active marketing variable and the other elements of the marketing mix are taking on a neutral but reinforcing role. This type of pricing policy is often particularly valuable when a new product/service is being planned because when the investment decision is being investigated a price assumption is necessary. This assumed price may then become the ceiling for product design etc.

Pricing is often constrained by factors outside the marketing executive or accountant's realm. These are legal and ethical considerations that are imposed on or recognised by the firm. Most firms feel inhibited in charging what the market will bear, afraid of unfavourable consumer reaction or adverse publicity. Pricing is
such a "conspicuous facet of business activity" (1) that it is easily observed and investigated.

Price fixing between firms is also illegal unless registered and approved by the Restrictive Practices Court of the U.K. Such approval is unlikely to be easily forthcoming because price fixing eliminates an important aspect of competition.

Firms are, therefore, constrained by ethical and legal restrictions on the extent to which they can raise prices.

Recently, government intervention in order to combat inflation has meant that regulations imposed by the Prices and Incomes Board and more recently the Price Commission have also had to be taken into account when pricing decisions are taken.

Actual price decisions however cannot be taken unless the characteristics of the industry, the firm and the consumers that are involved are specifically allowed for. The next chapter is devoted to surveying the Hotel industry, highlighting its particular features, in order to determine the role price is and should be playing as a marketing variable.

(1) D.V. Harper, p.121, op.cit.
CHAPTER II

THE STRUCTURE AND CHARACTERISTICS OF THE HOTEL INDUSTRY

GENERAL SUMMARY.

THE BASIS OF DEMAND.

SEASONAL CHARACTERISTICS.

SPATIAL CHARACTERISTICS.

ENTRY AND EXIT INTO THE INDUSTRY.

OWNERSHIP PATTERNS.

COST AND REVENUE PATTERNS.
THE STRUCTURE AND CHARACTERISTICS OF THE HOTEL INDUSTRY

The Hotel Industry for the purpose of this thesis includes all Hotels, Motels, Guest Houses and Boarding Houses that operate for profit (i.e. commercial reasons) in the U.K. with the exception that units having less than 4 bedrooms or 8 guests are omitted. Licensed and Unlicensed Hotels are included. This classification coincides with category 884 of the 1968 Standard Industrial Classification.

Hotels form part of the much wider accommodation industry which includes holiday camps, caravan sites and other residential establishments such as Hostels and University Halls. Although no coverage is given to these sections their relative size can be appreciated by examining Table 2.1.

The structure and performance of an industry is primarily the result of the interplay between demand and supply characteristics. The Hotel industry emerges as an essentially market orientated industry, constrained by certain unique supply characteristics.

Hotel activity is traditionally classified into three main and two subsidiary sections:

A. The provision of Accommodation.
B. The provision of Food.
C. The supply of Beverages.
D. Conferences.
E. Special Functions.

A brief outline of the basis of demand for these sections is given below.

A. ACCOMMODATION

The demand for hotel accommodation is a derived demand and dependent on the amount and extent of travel away from home. A necessary distinction for marketing strategy is between the Business
<table>
<thead>
<tr>
<th>Country</th>
<th>Hotel Bedrooms</th>
<th>Total Caravan Pitches</th>
<th>Holiday Camps Beds</th>
<th>University Accom. (sleeper spaces)</th>
</tr>
</thead>
<tbody>
<tr>
<td>England</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>London</td>
<td>52,858</td>
<td>280</td>
<td>-</td>
<td>4,967</td>
</tr>
<tr>
<td>South East</td>
<td>91,698</td>
<td>61,500</td>
<td>52,300</td>
<td>6,874</td>
</tr>
<tr>
<td>South West</td>
<td>87,693</td>
<td>47,750</td>
<td>35,150</td>
<td>3,050</td>
</tr>
<tr>
<td>East Anglia</td>
<td>18,843</td>
<td>43,760</td>
<td>17,500</td>
<td>2,885</td>
</tr>
<tr>
<td>Midlands</td>
<td>19,934</td>
<td>16,325</td>
<td>-</td>
<td>9,511</td>
</tr>
<tr>
<td>North East</td>
<td>27,942</td>
<td>35,710</td>
<td>11,300</td>
<td>9,252</td>
</tr>
<tr>
<td>North West</td>
<td>59,125</td>
<td>22,185</td>
<td>12,500</td>
<td>5,138</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>358,093</strong></td>
<td><strong>227,510</strong></td>
<td><strong>128,750</strong></td>
<td><strong>41,677</strong></td>
</tr>
<tr>
<td>Wales</td>
<td>32,305</td>
<td>60,370</td>
<td>17,550</td>
<td>3,310</td>
</tr>
<tr>
<td>Scotland</td>
<td>60,381</td>
<td>28,835</td>
<td>11,000</td>
<td>6,969</td>
</tr>
<tr>
<td>N. Ireland</td>
<td>5,996</td>
<td>7,000</td>
<td>-</td>
<td>700</td>
</tr>
<tr>
<td><strong>U.K.</strong></td>
<td><strong>456,775</strong></td>
<td><strong>323,715</strong></td>
<td><strong>157,300</strong></td>
<td><strong>52,656</strong></td>
</tr>
</tbody>
</table>

* Excluding London.  
† Including Isle of Man.

Table taken from N.E.D.O. Survey "Hotel Prospects to 1980's".

Table 2.1 Summary analysis of the major commercial forms of accommodation in the U.K. (January 1970)
and Non-business traveller; they are motivated by different reasons and therefore require different facilities and treatment. It is worth analysing these two categories separately and in a general fashion so that the main determinants will emerge clearly. Later on this categorization can be incorporated into the particular information that will be of direct benefit to an individual Hotelier when deciding on his marketing and pricing policy.

Non-business Demand

Travel within the non-business sector is primarily for vacation or holidaymaking purposes but some demand will be generated from emergencies and relocations. It is necessary to sub-divide this sector into domestic and international categories.

(a) Domestic Non-business Demand

The main determinants are:

1. Social and psychological attitudes towards travel, holidaymaking and leisure in general. These attitudes are influenced by occupation and social status, education, family circumstances, etc.
2. Real personal disposable income levels and the amount of money available for discretionary spending.
3. Holiday entitlements and their distribution annually.
4. Population and in particular its age structure.
5. The price and availability of alternative forms of accommodation, including that offered by overseas competitors.
6. Cost of travel.

(b) Overseas Non-business

Points 1–5 as recorded above are all relevant for this category
in that they will be the motivating and constraining determinants but 6 takes on additional relevance in that the cost of travel from the originating country to the U.K. can form a large percentage of total holiday costs. The influence of other international tourist centres and their relative costs allowing for exchange rates and possible government restrictions also exert a significant influence.

**Business Demand**

Again this sector may be sub-divided into domestic and overseas categories. Travel within this sector may be on a regular or occasional basis.

(a) **Domestic Business Demand**

This will depend on the following determinants:

1. The structure, pattern and organisation of industrial and commercial activity;
2. The level of economic activity and buoyancy of the home economy;
3. The nature, availability, and relative costs of various forms of communications and transport facilities.

(b) **Overseas Business Demand**

This will depend on the following:

1. The volume and nature of trading patterns in the U.K.;
2. Company and multinational company organisational structures;
3. Political influences, e.g. delegations etc.
4. The amount of amalgamation between business, vacational and recreational interests;
5. Costs of travel and the relative costs, merits and disadvantages of alternative communications.
B. FOOD

In most cases the level of demand in Hotel Restaurants is closely related to the occupancy level achieved. The same overall determinants are relevant.

There may however be circumstances where this inter-relationship does not hold. Some hotels are primarily accommodation units and apart from breakfast, supply no other meals. Even breakfast in some units seems to be less popular than previously. The Hotel Restaurant may enjoy a high level of casual trade, resulting from its locational advantages or the reputation of the Hotel Restaurant may be such that it independently attracts customers.

The level of demand is closely linked to location, the income level of the population and social habits regarding eating out but the chief determinants will be highly individual and apply to the individual unit itself. Generalizations other than recognising spatial and consumer characteristics are, therefore, potentially dangerous.

C. BEVERAGE

The level of demand is again closely related to occupancy levels and so the main determinants of demand are again relevant.

Individuality, uniqueness etc. will again play an important role.

D. CONFERENCES

This is such a growing field that it deserves special attention. Although facts and figures are difficult to obtain there is general agreement that "the potential is enormous" (1). The term Conference Tourism covers "congress, symposium, convention, meeting, assembly and seminar. It includes business and non-business conferences.

(1) See Trade Travel Gazette, September 1st, 1972.
It covers gatherings on a regional, national and international scale. It spills over into exhibitions, trade shows, fairs, and incentive travel, and may even include sports gatherings when stays of more than 24 hours are involved." (1).

The B.T.A. Conference on Conferences in 1973 estimated on a worldwide international basis that conference participants in 1972 numbered 3.5 million; conference nights 25 million and expenditure (estimated at £15 per night) amounted to £375 million.

America leads the field in conference activity: a number of cities have specialist purpose designed conference centres capable of taking 5000–10,000 delegates. In Europe most of the capital cities have specialist conference facilities. London on a comparative basis though possessing six hotels capable of taking 1000 or more delegates does not have a specialist conference centre.

For the U.K., total international conference participants are estimated at 0.3 million; conference nights at 2.1 million and expenditure at £30 million (£15 per night). Recent figures from the London Convention Bureau however suggest that £25 per night would be a more accurate estimate and so total expenditure would then read at £52.5 million. International Conference Trade is highly competitive. Co-operative approaches between Airlines, Hotels and Tourist Boards are probably essential for success.

Domestic conference travel is estimated at 3.05 million participants, 9.15 million participant nights and £100 million in total expenditure.

Aggregated this means that Total U.K. Conference trade in 1972 was estimated to have included 3.35 million participants; 11.25 million participant nights and £152.5 million expenditure.

Most of the U.K. conferences however tend to be small by international comparisons and probably in the U.K. "small events for less than 100 people constitute the majority of the market" and it is in this area that the absence of quantified information is apparent.

Sir George Young (1) suggested a classification on the following basis:

(a) International;
(b) Social;
(c) Professional and Industrial;
(d) Sales;
(e) Trade Association.

This is a useful classification for marketing purposes as we shall examine later.

Invariably group travel and/or accommodation arrangements are made. Middleton concludes that "of all branches of Tourism marketing, this is perhaps the most competitive, and an area for wheeling and dealing ... and for every known ploy in the salesman's repertoire". This has interesting implications for marketing policy especially when it is recognised that most conferences have a great deal of flexibility regarding their locational choice. The facilities available and price therefore become the main marketing variables and 'bargaining' becomes a significant weapon to ensure business. The fact that conferences often occur in the shoulder months of the year, e.g. May, June, September, October, mean that they are a very desirable form of extra business for any seasonal hotel.

Apart from Hotels, Universities in both the U.K. and abroad provide a significant additional range of facilities suitable for

(1) Sir G. Young, 'Hotel Accommodation in 1980's', Surrey University Press.
conference trade. The B.T.A. estimates that 50,000 beds are available out of term time in the halls of residence of some 50 British Universities and Colleges. This is a welcome source of additional revenue to the Universities and Colleges, and they are therefore willing to quote very competitive prices. They obviously do not compete with the 5/4 star hotel for accommodation facilities but often their specialist facilities (e.g. scientific equipment) ensures that for certain conferences they have a tremendous advantage. They also often offer attractive sites from the tourist point of view. They must therefore be regarded as a strong competitive force in this area.

E. SPECIAL FUNCTIONS

These again are specifically related to the particular hotel and its individual features and attractiveness to the type of customer arranging a special function. Little statistical information is available on this sub-section. It is essentially localized.

The demand for Hotel facilities fluctuates on a daily, weekly and seasonal basis. The extent of the fluctuation will depend on the nature and source of the individual units demand: holiday demand is obviously associated with holiday peak periods and weather variation; business accommodation demand is at a peak on Tuesday and Wednesday nights, lower on Mondays and Thursdays and almost absent for Friday, Saturday and Sunday. A 100% capacity utilization is therefore almost impossible but figures from the British Tourist Authority suggest that on average only 50% of potential capacity is used annually - by manufacturing standards this is remarkably low.

If a hotel bedroom was not "one of the most perishable products in the world" this problem of fluctuating demand could be met in the same way that it is approached by the average manufacturer who, if
faced with seasonal variations plans his production on an average annual basis and stockpiles his goods until required. A hotel bedroom however cannot be stored — if not filled on a particular night then the revenue lost can never be re-captured. This inability to stockpile presents hotels with some tantalising but fascinating marketing problems as we shall discover later.

There are distinct marketing advantages to be derived from the fact that hotels are service units and so 'retail' their product direct to the consumer: the absence of intermediaries means that it is much easier to collect information about their customers, indeed it can be personally collected; the gain and retention of customers goodwill is also directly under the control of the management; decisions regarding changes in price, quality of service etc. can be readily implemented if conditions necessitate this and in general a much greater degree of flexibility regarding marketing promotions can be exercised. This means that local and regional trends may be recognised and taken into account.

A possible disadvantage that derives from this service element is that the unit must deal with the customer at the location of his choice and that this limits the hotel's manouevrability. It is interesting to point out that historically the source of market demand has been a dominant influence on hotel location: in the nineteenth century the impact of the railways, in the twentieth century the influence of the motor car, and more recently the effects of air travel indicate how hotel location has responded to the requirements of travellers.

The industry is widely dispersed throughout the U.K. as illustrated in Table 2.3, and this dispersal indicates the necessity for the industry to be market orientated. For some purposes the
<table>
<thead>
<tr>
<th>Location</th>
<th>Number of hotels</th>
<th>Number of rooms</th>
<th>Average size (rooms)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Size of hotel (rooms)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4-10 11-25 26-50 51-100 over 100</td>
<td>Total</td>
<td>%</td>
</tr>
<tr>
<td>Coastal</td>
<td>14,053 4,496 1,051 367 68</td>
<td>20,035</td>
<td>56.3</td>
</tr>
<tr>
<td>Rural</td>
<td>3,775 815 145 33 3</td>
<td>4,771</td>
<td>13.4</td>
</tr>
<tr>
<td>Urban under 100,000</td>
<td>5,037 1,457 400 139 22</td>
<td>7,055</td>
<td>19.8</td>
</tr>
<tr>
<td>Urban over 100,000</td>
<td>1,415 613 219 107 61</td>
<td>2,415</td>
<td>6.8</td>
</tr>
<tr>
<td>U.K.</td>
<td>24,713 7,902 1,949 751 270</td>
<td>35,585</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: N.E.D.O. 'Hotel Prospects to 1980's'.

Table 2.2: Distribution of hotel capacity in the U.K. (January 1970) - all hotels
various regions may be regarded as separate markets, selling a unique monopoly-type service at a particular location. For example the one-night stay for business purposes leaves little room for flexibility and if there is only one unit providing the required services it may enjoy a monopoly position but the holiday stay is not so inflexible and hotels many hundreds of miles apart may unwittingly find themselves in direct competition.

The degree of competition facing the individual Hotelier is, unlike some product industries, difficult to identify let alone quantify accurately. The initial intuitive feeling that the few hotels in region A are in a monopoly or oligopolistic situation requires careful analysis regarding the extent and limits of competition before any firm estimate of the prevailing amount of competition can be accurately assessed.

In certain areas of the market competition is also felt from other units that supply accommodation, e.g. holiday camps, caravans, university halls, etc. Price and income constraints probably exert a significant influence in this area in determining the extent and depth of the competitive force.

The basic human requirements of food, shelter and warmth are easily obtained from the disposable income available to most consumers in the U.K. For this reason consumers' spending patterns involve a large proportion of discretionary spending. Hoteliers therefore have to compete with not just other hoteliers for consumers spending but also consumers goods and other service industries. Recognition of this competitive fact and its implications for marketing policy will be given more detailed treatment later.

As we have already seen in the first chapter, economists when explaining competitive forces pay a great deal of attention to potential competition which is closely correlated to the ease with which new firms can enter the industry. In the short run this is
<table>
<thead>
<tr>
<th>Region</th>
<th>Number of hotels</th>
<th></th>
<th>Number of bedrooms</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Location</td>
<td>Urban (under 100,000)</td>
<td>Urban (over 100,000)</td>
<td>Total</td>
</tr>
<tr>
<td></td>
<td>Coastal Rural</td>
<td></td>
<td></td>
<td>Coastal Rural Urban (under 100,000) Urban (over 100,000)</td>
</tr>
<tr>
<td>England</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>London</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South East</td>
<td>5,173</td>
<td>526</td>
<td>1,456</td>
<td>214</td>
</tr>
<tr>
<td>South West</td>
<td>5,275</td>
<td>1,192</td>
<td>1,359</td>
<td>290</td>
</tr>
<tr>
<td>East Anglia</td>
<td>1,020</td>
<td>134</td>
<td>281</td>
<td>95</td>
</tr>
<tr>
<td>Midlands</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>North East</td>
<td>924</td>
<td>311</td>
<td>359</td>
<td>398</td>
</tr>
<tr>
<td>North West</td>
<td>3,843</td>
<td>376</td>
<td>744</td>
<td>290</td>
</tr>
<tr>
<td>Total</td>
<td>16,235</td>
<td>2,814</td>
<td>4,952</td>
<td>2,936</td>
</tr>
<tr>
<td>Wales</td>
<td>1,769</td>
<td>665</td>
<td>669</td>
<td>143</td>
</tr>
<tr>
<td>Scotland</td>
<td>1,882</td>
<td>1,241</td>
<td>1,365</td>
<td>558</td>
</tr>
<tr>
<td>N. Ireland</td>
<td>149</td>
<td>51</td>
<td>69</td>
<td>57</td>
</tr>
<tr>
<td>U.K.</td>
<td>20,035</td>
<td>4,771</td>
<td>7,055</td>
<td>3,724</td>
</tr>
</tbody>
</table>

= Excluding London.

Source: N.E.D.O. Survey 'Hotel Prospects to 1980's'.

Table 2.3: Distribution of hotels and bedrooms between regions and locations (January 1970)
limited, however, in the long run entry into the Hotel Industry can be accomplished in basically two ways: an existing unit can be purchased and modified or a completely new unit constructed.

Conversions are usually limited to the smaller sized units that were originally private houses. Planning restrictions are virtually the only impediment to entry for this adaptive process. Conversions of the more spacious country house type units which provides a larger unit also seems to have become a more frequent occurrence recently.

The construction of a completely new purpose built unit involves a high capital cost outlay. For example the new Inter-Continental Pan-American Airways Hotel scheduled to open in London in March 1975 has an estimated cost per room of £22,000 (1). Two reasons contribute to the high cost of new units: firstly economies of scale mean that units have to be large and purpose-built to be operationally viable and secondly locations suitable for hotels are on sites that invariably have numerous alternative profitable uses - a high price therefore has to be paid to secure the site. Finance for hotel construction is also relatively difficult to obtain. Thus high initial cost outlay may therefore be regarded as a possible barrier to entry.

In manufacturing industries, especially consumer goods' markets, new firms find it difficult to break into an established market because of the high degree of product differentiation and consumer loyalty that has been developed and reinforced by expensive and effective sales promotion techniques. In the Hotel Industry expenditure on this sort of non-price competition has been limited, although it is now increasing, and so the new unit though it may have to offer some inducement to attract customers will be unlikely to find it prohibitively expensive or an insurmountable obstacle to entry.

(1) D. Harris, The Times, August 7th, 1974.
There are however no significant technological or managerial impediments to entry and the U.K. Hotel Industry seems to attract a large proportion of 'novice' hoteliers with limited knowledge and experience. Some countries refuse permission for hotels to be run by inexperienced or unqualified managers, but in the U.K. an active market for hotels in the small-medium sized categories is evidence of the ease of entry.

This ready market for small hotels means that exit from the industry is relatively painless for the smallest units and conversions to other uses are also often possible. However the large purpose-built blocks are more difficult to sell if unprofitable. This reinforces the view that the correct location is of fundamental importance to the viability of a hotel.

In Chapter I it was pointed out that the objectives, behaviour and performance of firms is closely related to the form of ownership.

The predominant form of ownership in the Hotel Industry is the independently owned, usually owner-managed unit. This is hardly surprising as we have already pointed out that the size of the market and its distribution throughout the U.K. constrains the size of units (see Table 2.3).

Most hotels are small unlicensed, so much so that 92% of all hotels have 25 or fewer bedrooms and 70% have 10 or less. The average licensed hotel has 17.5 bedrooms while the unlicensed has 8.4 bedrooms.

The small hotel often provides for its owner a way of life: he may cherish the independence that it gives him, he may value highly the social aspects of the business or the fact that the seasonal nature of the business enables him to enjoy a quiet and relaxing few months during the year. Research Report No.7 of Committee of Small Firms (1)

(1) Committee of inquiry on Small Firms (Bolton Report) No.7, H. ..0.1071.
<table>
<thead>
<tr>
<th>Size (Rooms)</th>
<th>Licensed</th>
<th></th>
<th>Unlicensed</th>
<th></th>
<th>All Hotels</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Hotels %</td>
<td>Rooms %</td>
<td>Hotels %</td>
<td>Rooms %</td>
<td>Hotels %</td>
</tr>
<tr>
<td>4 - 10</td>
<td>17.9</td>
<td>8.9</td>
<td>51.5</td>
<td>27.4</td>
<td>69.4</td>
</tr>
<tr>
<td>11 - 25</td>
<td>11.5</td>
<td>14.5</td>
<td>10.7</td>
<td>11.9</td>
<td>22.2</td>
</tr>
<tr>
<td>26 - 50</td>
<td>4.6</td>
<td>12.5</td>
<td>0.9</td>
<td>2.3</td>
<td>5.5</td>
</tr>
<tr>
<td>51 - 100</td>
<td>2.0</td>
<td>10.5</td>
<td>0.1</td>
<td>0.8</td>
<td>2.1</td>
</tr>
<tr>
<td>over 100</td>
<td>0.7</td>
<td>10.7</td>
<td></td>
<td>0.5</td>
<td>0.8</td>
</tr>
<tr>
<td>Total</td>
<td>36.7</td>
<td>57.1</td>
<td>63.3</td>
<td>42.9</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: N.E.D.O. Survey Hotel Prospects to 1980's.

Table 2.4 Hotel establishments in the U.K. by size (January 1970)

concluded that: "The owner-managers of small businesses see themselves as making a very special contribution to the economy in a qualitative sense";

"There was a feeling of emotional involvement, a determination to find a way round difficulties and a pride in performance which, it was felt, larger firms with their rigidity and bureaucratization could not equal ...";

"The need to attain and preserve independence" seemed to be the underlying motivation and it was apparent that "money was not their prime motivation".

To a large extent this may be summed up by the statement - "the management of small companies is in many respects a way of life".

But on the other hand the fact that he has his capital tied up in the hotel, the fact that he is responsible for all the decisions and the benefactor from all the profits made might make him very conscious of the profit level.
As property values have risen sharply and as the amount of specialized labour-saving equipment that is necessary to remain competitive has increased the amount of capital that is tied up in the operation of even a quite small hotel has meant that in terms of opportunity cost it is an expensive proposition to own and run a hotel that is not providing an economic return on the capital invested and so looking towards the future it is likely that the 'amateur' hotelier motivated by factors other than profitability is likely to decline and the emergence of more professional owner managers will increase the importance of the 'profit level' as a general objective. It has been estimated that the 'benefits in kind' enjoyed by the small owner-managed hotelier in 1969 were of the order of £1500 - £2500 per annum (1). This would represent a significant proportion of their total profits and so in assessing the profitability of small owner-managed hotels this 'real' benefit must not be overlooked.

Private Companies and Partnerships are also numerous in the Hotel Industry. In the latter the individual characteristics of the partners will determine how the unit is organised.

The private company ensuring limited liability for the shareholders is a popular form of organisation in the industry. If outside finance is required for growth however this form of organisation is at a disadvantage. Even though some of the advantages of Private Company status were withdrawn in the 1967 Companies Act this form of organisation still gives considerable advantages from the point of view of retention of control (often on a family basis) and flexibility.

The large public company is playing an increasingly important part in the industry. Large companies tend to own large hotels. In 1964 the Board of Trade estimated that the top 4% of licensed hotel groups handled 42% of total turnover. This of course is as a result of their

concentration in large combination centres, e.g. in London, the average licensed hotel has 117 bedrooms, the unlicensed hotel 15.5. The large companies are regarded as the pace and trend setters in both the operations and marketing fields. Unlike the small independent hotelier who operates in a well-known local environment and who can respond to the needs and requirements of localised demand the large multiple unit organisation though enjoying economies of scale cannot provide the degree of differentiated service required and it is noteworthy that their influence in rural and coastal areas is much less than in the more concentrated centres of population where greater standardization is feasible.

The large hotel company will have a great deal less flexibility regarding its overall objectives than the small company described above. The public company with quoted shares will find that in order to keep shareholders happy with its performance a minimum return on capital employed is more or less a necessity and if expansion or growth that requires a new issue is planned then a return not merely equal to but about that of other companies in the industry becomes essential. However, there are cases of hotel companies which have capital appreciation rather than earnings as their chief objective and although they are an increasing section they are certainly still a minority in this industry.

The Cost and Revenue Structure of the Industry

It is difficult to outline the cost and revenue structure of the industry owing to the disparity of the size and characteristics of the units as outlined above. The sales mix of the individual hotel will decide its particular cost structure and for decision making purposes it is the individual pattern rather than the general that is important.

However, the hotel industry has high fixed costs: on average
estimated to be at 60% of total costs. Fixed costs are those which do not fluctuate as the volume of business (e.g. occupancy, meal covers) alters: rent, rates, interest payments, depreciation and insurance fall into this category; certain labour costs are also inevitable if the hotel is open because a skeleton staff is required almost regardless of occupancy levels; a proportion of heating, repairs and maintenance may also be in this category. At the same time the fact that the industry provides a service means that it also requires a large amount of labour, which forms approximately 32% of operating expenses. In the present situation of labour difficulties further investment in labour-saving devices are tending to increase fixed costs even more.

A survey of worldwide Hotel Operations in 1973 indicated the following distributions of Expenditures and Income (1).

<table>
<thead>
<tr>
<th>Revenue Sources</th>
<th>1973</th>
</tr>
</thead>
<tbody>
<tr>
<td>Room Sales</td>
<td>43.5%</td>
</tr>
<tr>
<td>Food Sales</td>
<td>30.5%</td>
</tr>
<tr>
<td>Beverage Sales</td>
<td>15.1%</td>
</tr>
<tr>
<td>Minor Operated Departments</td>
<td>7.3%</td>
</tr>
<tr>
<td>Store Rentals</td>
<td>1.4%</td>
</tr>
<tr>
<td>Miscellaneous Income</td>
<td>2.2%</td>
</tr>
<tr>
<td></td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Table 2.5a International Revenue Patterns for Hotels

Expenditure | 1973
---|---
Payroll and Related Expenses | 32.0%
Food Cost | 10.8%
Beverage Cost | 4.0%
Departmental Expenses (including cost of sales in minor operated departments) | 15.5%
Administrative and General | 4.4%
Advertising and Promotion | 2.7%
Heat, Light and Power | 3.7%
Repairs and Maintenance | 2.8%
Rent | 7.6%
Depreciation | 4.6%
Other Capital Expenses | 7.2%
Profit before Tax | 4.7%
| 100.0%

Table 2.5b International Expenditure Patterns for Hotels

This survey (1) also suggested that the percentage of occupancy required to cover net cost of operations and fixed charges was approximately 60%.

Cost information referring to 1972 and the U.K. would give a very similar pattern (2).

(1) Horwath and Horwath International, op.cit.
<table>
<thead>
<tr>
<th></th>
<th>100.0%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of goods sold</td>
<td>33.5%</td>
</tr>
<tr>
<td>Wages (etc.)</td>
<td>31.0%</td>
</tr>
<tr>
<td>Supplies</td>
<td>1.2%</td>
</tr>
<tr>
<td>Light, Heat, Power</td>
<td>3.9%</td>
</tr>
<tr>
<td>Other Services</td>
<td>3.4%</td>
</tr>
<tr>
<td>Other Expenses</td>
<td>3.5%</td>
</tr>
<tr>
<td>Equipment</td>
<td>1.1%</td>
</tr>
<tr>
<td>Rent and Rates</td>
<td>3.2%</td>
</tr>
<tr>
<td>Repairs and Maintenance</td>
<td>3.6%</td>
</tr>
<tr>
<td>Renewals and Rentals</td>
<td>1.5%</td>
</tr>
</tbody>
</table>

Table 2.6  Expenditure Pattern for Hotels in the U.K.

Leaving a gross surplus of 14.1%. This profit figure would tie in with those suggested in the N.E.D.O. Survey and Inter Firm Comparison Survey where median figures are available broken down into Sales - Mix, Size, Ownership and Location categories.

Recent accurate figures for the U.K. are not available for comparative purposes and to allow for sales mix influences, reference may be made to Reports of the Inter Hotel and Motel Comparison Unit. However these are not included here as only median values are given in their published reports and allowing for the size of the sample it is difficult to make these generally applicable and are, therefore, not suitable for this purpose. For participants in the survey itself, however, more detailed information is available in the appendices.
MARKETING TECHNIQUES

Marketing methods in general are in no way as sophisticated or as aggressive as in manufacturing. There are some exceptions but these stand out as notable examples.

A fairly recent development in the industry is the formation of marketing groups and these offer tremendous advantages to the small independent Hotelier - 'Interchange', 'Prestige', 'Inter Hotels and Centre Link are examples. Their prime purpose is a national marketing service but they also give valuable advice regarding marketing philosophy and techniques. Referral Bookings and Joint Package tour programmes are also obvious advantages.

The benefits derived from group membership are not limited to small units. The Centre Link scheme gives Centre Hotels Limited representation in areas where Centre does not think it is viable to build and by carefully selecting 3-star Hotels that maintain Centre's image benefits are enjoyed by both parties. The recent link-up between British Transport Hotels and Interchange can also be viewed within this framework.

British Rail, The National Bus Company, various Airlines, and other transport concerns also facilitate and organise group-type travel and/or marketing schemes.

Advertising was not extensively used until recently - and it is rarely aggressive - it tends to be informative. A few attempts have been made at eye-catching advertisements but even so these are usually limited to a description of facilities and the invitation to write for a Brochure. The tariff is rarely included in general advertisements, Bargain Break being the occasional exception. Advertising for brand new units, e.g. in London, emphasises and attempts to establish the quality/image of the hotel (e.g. aura of respectability is often aimed at).
Brochure design in light of the above is very important. The most attractive and inviting are those using colour photographs with people using and seen to be enjoying the facilities. The selection of people should convey an image of the type of customer aimed at. The written description of all facilities should be in appropriate type that is easily readable. The tariff can be printed separately so that it can be changed if necessary as price alterations occur, but it is worth remembering to include a name or unique feature for identification in case the tariff gets separated from the main brochure.

SUMMARY

The Hotel Industry is therefore a very fragmented, wide dispersed industry comprised of mainly small units, but some very large companies exert a significant influence. Independent buyers predominate, but group and package travel is increasingly becoming more important. On the supply side unique characteristics of high fixed costs combined with seasonal demand and a highly perishable product means that marketing of the facilities available to ensure high utilization must be given top priority. At the same time occupancy at inadequate price levels means that profitability will be adversely affected so an intricate balance has to be achieved in the marketing philosophy.

The next chapter identifies the pricing practices of the Hotel Industry as a preliminary to appraising the effectiveness of these pricing practices.
CHAPTER III
PRICING PRACTICES IN THE INDUSTRY

SECTION A: PUBLISHED INFORMATION

Price comparison problems.
Qualitative differentials.
Locational variations.
Seasonal variations.
Group bookings.
Conferences.
Price trends through time.

SECTION B: SURVEY INFORMATION

Category I - The individual proprietor (8 - 24 Beds).
Category II - The individual proprietor (25 - 199 Beds).
Category III - Units or groups with 200 - 1999 Beds.
Category IV - Groups with more than 2000 Beds.
Price as a quality indicator.
Price sensitivity.
Backward pricing.
Locational influences.
Inclusive 'All-in' pricing.
Flexible pricing.
Conferences.
Special functions.
Food and beverage.
A rigorous appraisal of the effectiveness of the pricing practices used in any industry if it is to be useful must be based on comprehensive and accurate information. The search for information is invariably a time-consuming and often tedious task: the hotel industry proved no exception. Certain aspects were however quite fascinating and surprisingly interesting.

Information was assembled and assimilated from numerous and diverse sources over the period January 1970 - December 1974. This information falls into two categories, namely, published and personally collected. The latter was obtained by personally interviewing hoteliers.

SECTION A: PUBLISHED INFORMATION

This information on prices and the price level is generally available to the public and can readily be acquired from Hotel Brochures, price lists, tourist guides, etc. One of the problems with this type of information is to ensure that the tariffs quoted are comparable. Unfortunately no standardized approach is adopted by the Hotel industry: the quoted price is frequently 'from a given amount' and may merely refer to a room-accommodation charge, extras being added on for some or all of the following - breakfast, position and/or size of room, facilities provided, e.g. bath, shower, telephone, television, etc. Recently more and more hotels, especially the larger units, seem to charge for breakfast as a separate item, so comparisons between these and hotels charging a composite bed, breakfast charge need to be undertaken with care.

A further complication is that some Hotels add on a separate service charge (on average between 10-15%). This practice is most
common amongst the top-quality range of hotels although there are even here some exceptions.

The treatment of value-added tax also varies. Most hotels add this to the bill but some hotels are now quoting an 'all-in' inclusive price which includes the relevant accommodation service and V.A.T. charges.

The above problems are further complicated by the fact that hotels like most consumer goods are highly differentiated. Unlike consumer goods however categorization on an objective basis is extremely difficult. Consumer goods can be objectively tested and compared accordingly to qualitative differences (1). In hotels however 'service' and in particular 'atmosphere' are almost impossible to measure by either cardinal or ordinal means, since they are assessed subjectively by each individual according to his psychological make-up. The star-rating system which is commonly used provides an indicator in an ordinal sense of the standard of the facilities and service provided but for rigorous comparative purposes further information, preferably first hand, would be needed.

All these variations in practices and qualitative differences mean that superficial comparisons can be dangerously misleading and further investigation is inevitably needed if the information is to be interpreted in a meaningful manner.

However, certain points do emerge from a perusal of published information (bearing in mind the previous qualifications regarding generalizations).

### Qualitative Differentials

Qualitative features account for the main variations in price

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(1) e.g. Consumers Association Testing of Products and Reports published in 'Which' magazine.
levels (1). In London the differences between room charges for two-star and five-star categories being exceptionally large. On average the differential is $300-400$ but examples can be found of even larger percentage differentials. The differential between two and four-star categories is however narrower on average around $100\% - 125\%$.

In the provinces the variations attributable to qualitative differences are not as marked: the two and four-star differential being approximately $50\% - 60\%$.

In seaside areas these differentials are possibly even narrower. The two - four-star hotel differential being often slightly less than $50\%$. The differential between two and five-star hotels being significantly less than that in London hotels. However, this varies between resorts, suggesting that the qualitative features of the individual five-star hotels varied enormously and in general fell below those in London.

Country and small town hotels displayed no discernable common pattern.

Televisions in rooms attract a nominal charge of 10p-20p, if a charge is made. Private baths increase the tariff by £1.20 according to the Cornwell Green Bertram Smith survey but a more realistic figure is 60-75p per person per night. Swimming pool and sauna facilities often increase the price level substantially unless they are used as mitigating factors for other deficiencies, e.g. location.

Locational Variations

Correlations are as one would expect observable between tariffs and location. City centre locations command premium rates as do uninterrupted sea views in coastal areas. Within the larger cities

(1) Differentials were calculated from the figures given in Cornwell, Green, Bertram and Smith, 'Hotel Tariff Studies', 1966-1975.
there are substantial variations for fairly similar hotels according to their location. In London this is particularly marked: Park Lane locations being at a premium in particular and envied by other hoteliers excluded from this lucrative area. Within other large urban areas similar trends are observable though not to the same degree.

On a regional basis, areas outside London are significantly cheaper. Traditionally it was thought that as one proceeded from London prices fell. With increased communications and mobility, this is no longer automatically true. The influence of groups with fairly standardized approaches to actual units and often a common image for marketing purposes has meant greater standardization in prices. In fact some groups are using standardized charges for provincial hotels. In areas where there are few hotels the group hotel unit is often regarded as a price leader — this means that a national rather than regional pattern emerges.

Charges are often varied slightly according to the length of stay, Full Board for a week or longer in most hotels working out cheaper than bed, breakfast and individual meal charges at restaurant rates. The average concession for seven days plus seems to range from 5-10%. In seasonal hotels some off-season long stay visitors are given much greater concessions than this.

The treatment of children varies enormously. In general those under three and sharing the parents' room are charged a nominal amount only—often classed as 'cot' charges. Within the 3-13 age category substantial variations can be found. Children sharing parents' rooms are sometimes only charged for meals taken, in other units 75% of adult charge is made. Children occupying separate rooms are often given no more than a 10-15% concession. In some units no concessions are made and the upper age limit for concession varies according to the establishment.
Dogs are charged at sums varying from 50p - 100p per night exclusive of food which is charged as an extra, if supplied. Many hotels however refuse to accept dogs and often there are restrictions on the size and kind of dog and the rooms into which dogs may be taken.

Telephone facilities: the practice of charging for this service differs from hotel to hotel. Telephone calls made by guests are either booked on to the guest's bill at G.P.O. standard rates in which case the overheads involved are indirectly included in the general accommodation tariffs, or a surcharge is added to the actual telephone call cost to cover the service and overheads involved. This latter policy has recently attracted much unfavourable comment and there is an increasing tendency for hotels to provide direct external dialling systems for the customer to use personally and therefore eliminate the need for calls to be routed through the hotel's telephone system.

Seasonal Variations

Most hotels experience seasonal demand variations. Traditionally hotels often printed a normal tariff and added a peak season supplementary charge. The surcharge varied accordingly to the individual hotel but 15 - 20% was a commonly used figure.

Recently this approach has been modified. The normal quoted tariff for most hotels now refers to charges at their most busy times. Their quieter periods being shown at reduced tariffs and marketed as 'winter breaks', 'bargain breaks', etc. The English Tourist Board's 'Lets Go' Autumn Holiday campaign for the 1974/75 season gives details of 626 hotels (including 33 hotel/marketing groups) which offer substantial discounts for the off-season holiday. These discounts are now shown against the normal rate "so members of the public can judge for themselves which hotels offer the best bargains".

Winter weekend packages were pioneered by Grand Metropolitan
Hotels in 1964 when in co-operation with British Rail the company operated Stardust Mini Holidays from the provinces to London. In its first year it is reported (1) to have cost £1000 to promote, producing 300 bookings. However by 1974/75 season £1m was being spent on the promotion, which included T.V., press and some commercial radio advertisements (2). The success of this promotion was reported by Patricia Tisdall (3) who quoted Mr. Derek Taylor, the marketing Director of G.M.H. as saying "that bookings have broken all records and were expected to top the 100,000 mark". The link with British Rail is particularly valuable to Grand Metropolitan Hotels and they are estimated to have 70% of the London weekend market and are regarded as 'brand leaders' in this field.

Numerous other groups exploit the winter weekend/break market. For the 1974/75 season they included (4):

"Adda Hotels Ltd; Anchor Hotels and Taverns Ltd; British Transport Hotels; C. and H. Hotels Ltd; Centre Hotels Ltd; City Hotels Ltd; Crest Hotels Ltd; Devere Hotels; Falcon Inns Ltd; Hickmet Hotel; Holiday Inns International; Hotels of the Cinque Ports; Imperial Hotels; Ind Coope Hotels; Interchange Hotels; Inter Hotels; Mine Host Hotels; Mount Charlotte; Myddleton Hotels; Norfolk Hotels; Prestige Hotels; Queens Moat Houses Ltd; Royal London Hotels; Scottish and Newcastle; Strand Hotels; Swallow Hotels; Torquay Leisure Hotels, and Trust House Fortes."

A tremendous variety of packages and short holidays are offered by these groups. Independent Hoteliers are at a substantial disadvantage for marketing purposes unless they belong to marketing groups. The

(2) Catering Times, October 3rd, 1974.
(4) Catering Times, September 26th, 1974.
emphasis is on 'value for money' and price competition. Concessions
given vary from 10-60%. Those marketed through travel agents involve
invariably a minimum 10% commission charge.

Group Bookings

Tour organisers and companies making business bookings usually
receive discounts from the hotels with which they deal.

Information regarding the extent of this discount is not readily
available and in times of fierce competition is a carefully guarded
trade secret. D. Harris (1) reported that until 1973 hotels in
London (from 'the central area out towards London Airport') who relied
on package tour bookings were able to keep occupancy high by offering
discounts of 20% in peak periods and 40-50% in the off season. In
1973 however he stated some of these units gave discounts of 30% in
the peak periods. Miles Quest in the Catering Times has suggested
that groups may form as much as 75% of the London summer business. On
this estimate this means that normal tariffs are rarely achieved.

The above evidence however is not sufficient for analysis and will
be supplemented by collected information later in this chapter.

Conferences

Prices for conferences depend a great deal on the duration, number
of delegates, facilities, etc., and the normal 'price is based on a
quote given to a potential organiser which is then accepted or refused.
No published information is available in this area and will again be
dealt with later. Special functions fall into the same category.

Interesting work on the dynamic aspects of changes in hotel prices
through time has been undertaken by R. Kotas (2) who surveyed on a
sample basis changes in hotel prices as recorded in hotel guides from
1962 to 1971.

(2) Richard Kotas, 'Price Trends in British Hotels', Departmental
Monograph, University of Surrey.
During the first half of the 1960's hotel room rates increased at approximately the same rate as the retail price index but from 1965 to 1971 the level of room rates rises was "considerably in excess of the Retail Index. For example in 1967 the Retail Price Index rose by 3.1 points and room rates in British hotels by 19.3 points. Numerous factors contributed to this rise and include the introduction of Selective Employment Tax in 1966 and the Training Board Levy; the rising cost of land which is a major item in hotel building costs; high interest rates and modernization programmes, and pressures on available hotel accommodation. It is noteworthy that the latter point is a demand pull explanation but that the remainder are cost push. This is a point that we shall return to later.

<table>
<thead>
<tr>
<th></th>
<th>1962</th>
<th>1965</th>
<th>1968</th>
<th>1971</th>
</tr>
</thead>
<tbody>
<tr>
<td>Index of Retail Prices</td>
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<td>109.5</td>
<td>121.6</td>
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</tr>
<tr>
<td>Index of Services</td>
<td>100</td>
<td>108.3</td>
<td>128.0</td>
<td>168.6</td>
</tr>
<tr>
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<td>108.7</td>
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<tr>
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<td>137.2</td>
<td>180.0</td>
</tr>
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<td>Large Provincial Cities</td>
<td>100</td>
<td>111.8</td>
<td>141.9</td>
<td>171.6</td>
</tr>
<tr>
<td>Smaller Towns</td>
<td>100</td>
<td>111.1</td>
<td>140.2</td>
<td>177.3</td>
</tr>
<tr>
<td>Coastal Resorts</td>
<td>100</td>
<td>104.5</td>
<td>138.7</td>
<td>172.8</td>
</tr>
</tbody>
</table>

Table 3.8 Price Trends in Hotels

Large Provincial Cities and Coastal Resorts recorded a below average rise while the smaller towns and in particular London exceeded the average.
Table 3.9  Single-Double Room Price Trends Comparisons

In all cases single rooms rose by a larger amount than double rooms. The explanation is probably due to the fact that single rooms are primarily used by businessmen and are less price sensitive than double rooms.

Price trends were also recorded according to the price level. Two price categories were used. The lower category of price (i.e. below 45/- for London and 30/- elsewhere) all recorded a higher percentage rise than the higher category, which can probably again be explained that in lower priced accommodation variable running costs form a large percentage and as costs increased these have been passed...
Variations in trends according to the size of hotel illustrated that the larger the hotel the greater the price rise. This is of course contrary to what one would expect from an economies of scale point of view: the survey for the sake of continuity did not cover the new purpose built hotels of the late 60's so a slight bias may be present. On the other hand the newer larger purpose built units have high fixed costs and these have been reflected in higher prices. So existing units may well on a comparative basis have enjoyed excessive profits.

In areas outside London a threefold category for size was used. Hotels with up to 40 rooms are classed as small, those with from 40 to 80 rooms as medium, and over 80 as large.

This indicated that for Large Provincial Cities and for Smaller Towns the medium sized category increased prices both for single and double rooms by more than the other units. This ties in with the cost analysis of the previous chapter where it was pointed out that medium sized units neither enjoy the advantages of family labour and loyalty or the cost economies of the larger units and are increasingly coming under pressure.

Studies on hotel tariffs have been undertaken regularly in the U.K. since 1966 by Cornwell, Greene, Bertram, Smith and Co. These studies were designed to provide information for hoteliers regarding the national and regional trends in hotel tariffs so that they could be used to assess present price levels relative to competitors and then used as an aid to determine future pricing policies. Information was originally collated and assessed on a half yearly basis - this is now done on an annual basis only.

When the survey started in 1966, covering 180 sample hotels (of two to four star rating, situated in towns and cities with populations
over 100,000) only three London hotels were charging more than £5 per night for a single room. In January 1975 only one London hotel in their sample still offered accommodation at £5 per night, and they stated that "the £6 per night room is rapidly disappearing". In fact 40% of the London hotels in the sample charge over £9 per night. In the provinces "31% of the sample charge £5+ while 67% quoted £6+" so that the survey concludes that "the £5 per night room has almost disappeared".

The information from these surveys has, in conjunction with Kotas's previous work, been used to bring the price trend survey up to date. In 1972 charges for single rooms in London increased by 10%, double rooms by 9%. In the provinces single rooms by 5% on average and double rooms by slightly less than 3% overall. From December 1973 to January 1975 average price changes in U.K. Hotels were of the following magnitude: singles 13%; singles with bath 15%; double 13%; double with bath 12%. The cost of living index rose by 18.6% in this period and so for the first time since 1966 rises have been below the inflationary tendencies. This may well be due to the fact that some of the units sampled fell within the Price Commission's influence but the regional pattern of changes also suggest that intense competition and excess capacity have also played a role.

It is noteworthy that London price rises were below those of the provinces. In London over the total area increases were: single 11%; single with bath 12%; double 8%; double with bath 8%. For the provincial areas increases were 14%, 16%, 16% and 13% respectively.

A more detailed breakdown of the regions within London provides a more interesting pattern of divergence. Taking the prices of single rooms with bath for illustrative purposes, at Heathrow airport only a nominal 1% price increase is recorded; in Kensington and Earl's Court, another fiercely competitive area, the increase was 5%. In the West
End and Victoria however the rise was 22\% while in the Strand, Holborn and City 16\% was recorded. In provincial areas for the same period December 1973 to January 1975 Scotland recorded 22\%, the South-East 18\%, the East Midlands 16\% and Yorkshire 12\%.

It is noteworthy that in nearly all cases the rise in single rooms, as in Kotas's work, showed a greater rise than for double rooms (no doubt reflecting the lower price sensitivity of businessmen and the increase in overhead costs).

A similar picture is observed if international surveys are analysed. In the late 1960's London was one, if not the most, expensive Capital city to stay in. Yet there is evidence that by late 1974 it had fallen back in the league tables and an 'American Business Week' survey in January 1975 indicated that the price of a double room in a first class hotel would be priced in Paris at £26 and in London at £20.

The conclusions to be drawn from these surveys suggest that the price levels of hotels are not closely related to cost changes but are essentially much more market orientated and related to the nature and extent of competition. In particular the presence of excess capacity (e.g. around Heathrow) illustrates how price rises have had to be contained in the very competitive situation of recent years as compared to the freedom enjoyed by London Hoteliers in the late 1960's.

This contrasts markedly with manufacturing industries where changes in demand can be met by changes in output at least in the short run rather than immediate adjustments in price. There is also evidence to suggest that in reality the amount of price adjustment to market demand is much greater than that indicated by quoted tariff adjustments. This aspect will be analysed in more detail in the following section, where previously unpublished information is used.
SECTION B: SURVEY INFORMATION

The pricing practices used in the hotel industry present a bewildering pattern of diversity. The contrasts are numerous and marked: they include simple and complex techniques; rigid and flexible systems; frivolous and serviceable schemes; prosaic and enterprising strategies and they range from the blatantly inadequate to the highly successful.

This diversity means that any general survey of the practices and procedures used is difficult. However the information obtained has been grouped under generalised headings. Details of the sample is given in Appendix I. This involves a certain amount of arbitrariness as overlaps occur but it is useful in that it aids the identification of the features that exert a significant influence on pricing policies and procedures in the industry.

Category I - The Individual Proprietor. Size Group 8 - 24 Beds.

The attitude of the small individual proprietors towards price policies confirmed the viewpoint of A.W. Zelomek (1) when he stated that "for smaller firms, particularly family-owned firms, formal pricing strategies are completely lacking".

Numerous questions of interest arise from this finding: were the policies absent because they were regarded as unnecessary? Were the units insufficiently motivated to develop such policies? Were the units lacking in the technical expertise necessary to develop such policies?

The objectives of the hoteliers in this category are almost impossible to quantify: they were essentially qualitative and mostly non-pecuniary. All the owners resided on the property and enjoyed what they considered to be "an enhanced quality of life".

given replies included: "Preservation of my/our independence"; "It is a way of life"; "A style of living"; "A pleasant interesting occupation involved with people". A surprising number quoted "a really good holiday" and in particular "a cruise" as one of their objectives. On further questioning only a very few of them considered a minimum profit as necessary to keep them engaged in hotel/guest house activity. A few of them observed that an added advantage was that their properties provided a hedge against inflation. Nearly all the units were run by husband and wife teams, the wife playing an active role.

In operational terms a high level of occupancy became their central operational objective. The price at which this was achieved being regarded in most cases as outside their control: they were basically price-takers. There were clear indications that they all, almost eagerly, abdicated the pricing decision to following the example set by their competitors, and they were in one area particularly willing to follow the 'advice' of the Local Hotels and Guest Houses Association regarding a recommended floor price. An annual price setting exercise seemed the norm.

Within this 'market' price they tended to adjust the inputs, insofar as this was feasible, and so unwittingly they were operating a backward pricing type of exercise. This tendency was being reinforced by cost inflation which was disturbing their equilibrium and previous complacency: in many units adjustments in the quality and type of food offered was the only realistic approach. However all the units had 'value for money' as one of their criteria for assessing the price charged and commonly believed that the rate charged by competitors or recommended by the H.C.H.A. represented "what the market would bear".

The units which were differentiated from their competitors however faced a much more difficult exercise and the element of uniqueness
created problems which, because of their limited technical expertise, they found difficulty in solving.

The predominant marketing methods were repeat bookings, "word of mouth" recommendations, and listings in A.A., R.A.C., H.C.H.A., Tourist and Town Guides. This meant that the marketing media used were informative rather than persuasive.

Nearly all the units had a rigid pricing policy; a few gave quite minor (5-10%) concessions if the length of stay was longer than average (the assessment of average however differed). A few units however showed great ingenuity in making use of price as a seasonal marketing device. A coastal hotelier, in conjunction with another hotelier, used package tour bookings at substantially reduced rates in low season months, illustrating an implicit knowledge of marginal/variable costing and opportunity cost although none of these terms figured in his vocabulary.

Similarly, an Interchange member made use of 'Getaway Breaks' and illustrated how these were only discontinued if occupancy reached 100% and other bookings had to be refused. Only then would "the price reduction mean a loss" - a classic example of the successful businessman's intuitive recognition of the economist's concept of opportunity cost.

Apart from notable exceptions the satisficing objectives of these units together with the constraints meant that price played a passive role and one can therefore conclude that as most of the units were price takers, formal pricing policies were for many regarded as redundant and unnecessary.

**Category II - Individual Proprietor. Size 25-199 Beds.**

In this category profit took on a more meaningful role as an objective, partly because most of them were aware of the large amount
of capital invested in their hotels. Maximum profits however figured as the objective for only one hotelier who played the part of the economist's classical Entrepreneur: his energy and ingenuity being directed at maximizing profits although his reason for seeking profit was not so much for its own sake but because he regarded profit as the 'signal' by which he could assess his performance in the challenging 'game' of business.

Many of the units however regarded the achievement of a minimum level of profit as a necessary requirement for their continuation in the industry. Growth and a hedge against inflation were also quoted as significant motivating influences. One large individual proprietor with Private Company status, London based with a prime site, stated that "there are no allowances for capital investment in this industry therefore capital employed need not be taken into account", illustrating a gross misconception of opportunity cost.

Price in general was regarded as a potential competitive device. The pricing methods used however were cost orientated procedures on estimated occupancy with an ultimate check on the pricing policies of rival competitors. It was difficult to ascertain historically how often the competitors check necessitated adjustments. The reality appeared that checks were made to ensure that no major disparity existed but that a fairly wide margin was available for flexibility because within this size range the degree of differentiation was considerable. The consumer therefore was unable to make direct or meaningful comparative judgments, and most hoteliers recognised this limitation.

The marketing methods used were more varied but could not be classed as imaginative. Some of the seasonal units (including the Entrepreneurial figure mentioned above) gave substantial discounts to secure business (see Discounts Section below) but there were also cases of seasonal hotels that failed to appreciate the major drawback of an
average cost approach to pricing. "Price reductions would mean profits lost"; "Costs are always the same therefore why should price be lower?"; "Electricity costs too much in the winter and so it is better not to have extra guests" were some of the replies received to questions regarding seasonal price differentials. In fact the overall impression of this category is that though they appeared motivated to secure an adequate return on their investment, their lack of technical expertise prevented this being achieved. By chance none of the units belonged to a marketing group. It is interesting to speculate as to the extent to which membership of a group leads to the re-education of the cost-orientated towards a market-orientated approach.

The individual unit which does not have this supporting back-up from a marketing group is increasingly going to find that this lack of technical expertise is a significant impediment to the full utilization of the resources under his control.

However in the country as a whole numerous large groups would have hotels of this size and as we shall see later their attitude towards price/marketing is certainly more sophisticated than those covered separately in this sample.

**Category III (Units of 200-1999 Beds).**

The objectives of the units varied and ranged from the qualitative "the best hotel in London ... and therefore long run profitability" and quantitative "a target percentage return on capital employed". This latter objective was the recurrent theme although the effects of inflation on the assets employed meant that the assessment of capital employed was arbitrary. None of the units regularly revalued property assets.

On the whole costs figured prominently in their procedure for deciding on price. As many of the units were four star rated service/
quality figured prominently in their scale of marketing policies and there was a general assumption that their customers were willing to pay for this, regardless of the price charged. The general illusion was that there was a price immunity; yet the reality of their occupancy figures suggested that apart from the five star units with established reputations, this was not true.

Some of these units however gave discounts on a seasonal and block booking basis. The London discounts were substantial and strictly related to the bargaining positions of the interested parties. Marketing methods used varied from simple reputable word of mouth to international images carefully promoted.

Price was certainly given a great deal of consideration in the London area where competition was fierce. All the decision makers were aware of the basis on which pricing decisions should be made.

Category IV - Large Groups

The objective of all the groups in this section was a given rate of return on capital employed: the lowest quoted figure was 15% before tax and the maximum 25% after tax. Notional values rather than realistic property valuations were used by many of the groups. Hardly any of the groups were achieving their objectives in 1974 and many of them accepted this situation quite passively, arguing that the excess supply situation in London, the effects of inflation and the Government's restrictions of price increases were circumstances beyond their control. It was however interesting how the attitude of the groups differed with regard to the excess supply situation in London. Some were of the opinion that they should "weather out the storm" and accept low occupancy. Others however were aggressively keeping occupancy high by allowing substantial discounts.

Apart from a few groups who had fairly standardized hotel units
most of the groups controlled a diverse range of hotels varying in size, location and quality. In these circumstances questions were related first of all to 'group' thinking and then made more specific by taking a representative selection of different individual units and then reapplying the questions again to evaluate the answers in the light of particular circumstances. In a few of the groups there appeared to be a definite lack of communication between central management and the managers of individual hotel units regarding the objectives behind given pricing policies and strategies.

In one large group some of the individual units even regarded price as an autonomous variable being imposed by Head Office. The potential of price as a local competitive variable was therefore eliminated and the morale of the individual managers suffered from this bureaucratic system. In this group there were even cases of individual hotels being unaware that they were offering bargain weekend rates which had been nationally advertised by the central marketing department. The overall degree of expertise of the marketing department of this group however appeared suspect in that only limited information was available on the characteristics of consumers and further market research was not anticipated. It was tempting to conclude that the marketing only gave an illusion of sophistication.

Other groups however approached the problem in a much more rigorous and scientific style. The most successful groups tended to be those that either ran standardized hotels so that central decision making was a realistic operational approach to all types of marketing decisions or groups who allowed their differentiated units a large degree of independence to allow for particular, local and regional characteristics. This involved, of course, engaging better quality managers, however in terms of staff morale and performance it appeared that the benefits outweighed the costs.
In all the groups targets for individual units were inevitably adjusted in the light of an assessment of last year's performance; the approach was therefore essentially incremental. It is difficult to see how an alternative that is operational could be devised. Even so where individual managers set their own targets, satisficing must occur and under achievement will result.

**Price as a Quality Indicator**

The most interesting facet to be revealed in the survey was the confirmation of the hypothesis that in this industry price is taken by customers to be an indication of quality. This was confirmed by questions asked amongst students (a theoretically price sensitive group) and other members of the public. Information and Accommodation Bureaux who are continually in contact with public seeking and appraising accommodation also confirmed this viewpoint.

The effect of this on marketing strategy varied according to the qualitative characteristics of the individual unit.

The luxury hotel recognised that they had to be very certain not to underprice themselves: there was definite evidence to suggest that in London there is a form of active competition to ensure that "one is one of the most expensive hotels"; being able to afford to stay at an expensive hotel is a status symbol. The pricing problem is therefore analogous to that of Rolls Royces and is essentially what the market will take. With many of the five star hotels convinced that 90% of their customers are almost price insensitive it is interesting to envisage whether a price ceiling does exist. It would appear that the prices charged at present by the five star units covered in the survey are not yet near this ceiling because occupancy levels are high despite the overall depressing market situation.

At the other end of the scale units of one or the marginal two
star rating had a problem, the antithesis of the above. They had to ensure that they did not quote prices at anything more than a fraction below the average recognised norm for their area otherwise this created adverse reactions in the customer, who would be suspect of the quality. In other words they too had to be extremely careful not to fall below the price threshold floor.

In the area between these two extremes, the effects of this quality/price image is not so restrictive. Groups (including marketing groups which enforce minimum quality standards) by marketing their particular image on a national or large regional basis are able to eliminate this 'quality suspect' image from consumer minds and still continue to use price as a market capturing device.

The success of Backward Pricing exercises by groups eg Centre Hotels, Crest-Esso Hotels, and Holiday Inns would validate this approach.
It was intended to elicit information regarding the responsiveness of demand to price changes. This was to be approached by using questions 4 and 9 in the survey. By the time the interviews were conducted in late 1974, the original intention was overtaken by the large inflationary price increases that had recently occurred not just in this industry but throughout the economy. So the following points are recorded on a tentative basis only.

There was a general feeling that the price sensitivity of the average customer was increasing. This was partly because the liquidity problems of companies had forced them to put ceilings on accommodation allowances for businessmen and also because many hoteliers thought that hotels were increasingly being used by a new 'set' of customers for leisure-type purposes and that these people were looking for value for money when spending their discretionary income.

In this context it was surprising how little information was collected, tabulated and retained regarding customers using particular hotels. In hotels of up to 50 beds this information was subconsciously acquired by the hotelier but for units of 50+ the information available steadily decreased. Many of the groups with their apparently sophisticated marketing departments admitted that there were substantial gaps in their information facilities.
BACKWARD PRICING

No apparent correlation appeared between the use of this approach to pricing and either location or ownership.

The occurrence of inflation over the last few years combined with labour difficulties meant that many of the units had had to resort to some form of backward pricing technique to preserve their profit margins. This type of adjustment in inputs (service, food, facilities) was common amongst the smaller hotels, although they did not see it as a pricing exercise but rather as a cost control exercise. Adjustments in food costs and the introduction of 'economy' meals was mentioned frequently for hotels in the lower quality categories, partly no doubt because this was the only feasible adjustment, service and facilities already being limited.

Units or groups however which used backward pricing as a deliberate pricing technique showed an above average return on the capital employed. Drest-Esso Hotels, Trust House Fortes Post Houses and Centre Hotels are classic examples of such pricing policies, and in particular their newer units which were designed at a particular price - so that the investment and pricing decisions were fully integrated.

Centre Hotels refused to participate in the survey but the philosophy of Centre Hotels (Cranston) Ltd. is well documented and set out explicitly in their Corporate Identity Statement contained in the Company's Reports and Accounts for year to 31st March 1974. The objective is "to earn the best possible return for its shareholders ... We offer a satisfactory product, responsive to market needs and geared to a pre-determined price structure". Bedroom selling prices are directly related to capital costs and this means that the investment and pricing policies are intricately bound together and for success rely on an accurate identification of consumer needs and potential demand from the beginning of the exercise. This quality at a price, Marks and
Spencer's type exercise, has meant that from 1965 when Mr. H. Edwards first took over 'Cranston London Hotel' assets the return on capital employed has been above the average for the industry and this has permitted the internal growth and rapid expansion of the group.

Looking towards the future, many of the units interviewed had been considering implementing such backward pricing policy measures and if inflationary pressures continue at the recent levels then such policies will become essential marketing methods for most hotels. The "unique-top-of-the-market" bracket being the only exceptions.
LOCATIONAL INFLUENCES

The interviews were not designed to elicit information on national regional differentials but evidence came to light which suggested that for local areas oligopolistic market structures exist and that the really large groups carry great responsibility in influencing the price level at local levels.

If this is analysed in the context of the lack of group price flexibility previously mentioned then the group units tend to be regarded as local leaders in true oligopolistic style. They are therefore used as measuring rods - other units evaluating their service-price level against them, making appropriate allowances.

There was no evidence to suggest that they exert a downward pressure by exploiting group economies of scale and so unwittingly and perhaps unwillingly they have had a disproportionate influence on increasing regional price levels as indicated in the first section of this chapter.

These theories regarding the impact of groups are tentative and greater in depth research on a dynamic basis would be necessary to confirm this hypothesis. Regrettably facilities were not available for these theories to be investigated at this stage by the author.
INCLUSIVE ALL-IN PRICING

Of the units surveyed all-in pricing was the exception. Few had analysed critically the advantages and disadvantages of all-in pricing; the respondents illustrated their conservatism and aversion to change by repeatedly stating "We have always added on service charges and will continue to do so". The fact that V.A.T. now further complicates the calculation had persuaded a few to quote an all-in price. Many of those questioned believed that all-in pricing made the price appear too high and regarded it a sounder marketing policy to 'bait' price by quoting the minimum: the argument being that extras were not noticed anyhow.

Questioning of potential hotel users however illustrated that those who are reluctant to use hotel facilities are put off by the possibilities of substantial extras. As we shall see later the success of certain marketing ventures of off-peak promotions coincided with the use of an all-in price. Of the hoteliers interviewed who used the all-in price: all thought that it had great potential as a marketing tool; most thought that it economised on time and effort, and perhaps more significantly none of those using an all-in price were contemplating reverting to other methods. All-in pricing was used by every hotel who was a member of a marketing group: perhaps proof of their more sophisticated and scientific attitude towards marketing.
FLEXIBLE PRICING PROCEDURES

These may be categorised under two headings, namely:

A: Those appertaining to variations over time used in off-peak periods of a weekly or seasonal nature,

B: Those appertaining to a particular characteristic of the user and given on the basis of the extent or length of the demand. These are commonly referred to as discounts.

Category A as we have seen earlier on in this chapter involves giving price concessions for off-peak periods to boost occupancy levels. The concessions given are calculable from published peak and off-peak price lists. Within this sample concessions varied from 10 - 70% of high season charges which is comparable with the general pattern previously discussed.

It emerged conclusively that for this type of promotion the independent hoteliers suffered from substantial constraints and limitations: they could not compete with the effective marketing of the groups. The Golden-Rail scheme of British Rail however provided some opportunity for the independent unit.

The large groups approached off peak pricing in various ways. One group aimed when pricing bargain weekends to cover variable costs plus £1 per night per person: another group aimed at variable cost plus £1.50 per person per stay (not usually more than three nights). Agent's fees if relevant also had to be taken into account and allowed for: they were often quoted at £1 per booking.

The groups emphasised that inclusive prices were a selling aid and that price acted as an effective communication device in encouraging new participants to enter the market. Some of the groups had undertaken marketing surveys on those participating in the various schemes and most of the evidence seemed to suggest that the cheaper schemes had attracted non-regular hotel users and one group in the upper end of the
market stated that whereas their regular customers came from the
marketeers social class AB range that their special offers had attracted
members of the Group C range.

An interesting illustration of the psychology behind these
promotions was related by a Scottish hotelier with a hotel used during
the week almost exclusively by businessmen. In order to utilize
capacity at weekends he advertised a bargain weekend, including a
dinner/dance on Saturday evening at half the normal price: there were
only a few takers. He then readvertised some months later the dinner/
dance at the same price, with the offer of free accommodation—meals
to be charged at normal prices. The result was numerous bookings
which proved, he said, "that everyone loves something for nothing".
An illusion in fact, because allowing for the meals taken the new
concession was approximately 35\% and not the previous unacceptable 50\%
off normal tariff.

Category B: Discounts are given for numerous reasons. Many hotels,
but in particular small units, gave nominal discounts of 10—15\% for
long lengths of stay.

Large numbers of hotels gave discounts to potential users (e.g.
industrial firms or institutions) in their area. This guarantees
regular bookings and the discounts are related to the expected volume.
20\% appeared to be the maximum for this category. In general
independent units or small groups indulged in this practice to a much
greater extent than the local members of large groups.

Throughout the country discounts are given to package tour
organisers. The amounts conceded are essentially the result of a
bargaining process: the discounts given by the same hotel sometimes
varying significantly and being correlated to normal or expected
occupancy figures. These tended to vary from 25—60\% on average.
Although a few units gave 80% as their maximum discount given to special customers who offer quantity bookings on a consistent basis.

One of the problems met in the negotiating process is that prices have to be set a long time in advance. With inflation at present rates this necessitates considerable skill.

In London where excess supply is prevalent even in the high season, discounts are a way of ensuring a minimum occupancy level. They are certainly substantial and frequently amount to 70 - 80% of the high season charge. Quality hotels in the vicinity of London Airport have been forced into a particularly vicious price cutting exercise and prices as low as £2 per night for accommodation for regular customers have been reached. This is very close to variable cost and can only be endured in the long run if they are contained to a very small percentage of occupancy. There is however a general tendency for package type deals to be providing well over 50% of occupancy levels and many units have to rely on approximately 85% of their occupancy being filled at reduced rates. Many of these units run at an overall loss.

To a large extent the size of the discounts are related to the success or failure of the Sales Department but this can fluctuate even within the same unit from week to week. An example illustrates this: a London four star hotel in Autumn 1974 had discounts for one week ranging from 15 - 70% and in the following week from 10 - 40%. Occupancy and rooms booked were almost identical.

There was a general feeling that the information provided by accountants regarding the floor price for price quotations was difficult to obtain although many of the groups indicated that the situation in London had forced them into ensuring that this management accounting information was available so that decisions could be realistically and quickly made.
CONFERENCES

This represented probably the most competitive of the pricing decisions and was essentially market orientated. "Bargaining" was continually stressed as the main determinant.

Facilities and capacity constraints were thought by most conference-gearad units to be the chief determinant of selection. Large expenditures had therefore often been undertaken to provide the required facilities; the capacity constraints for existing units were recognised as immutable in the short run and price therefore took on an exceptionally vital role.

The price quoted reflected in most cases the need to obtain conference business and so varied according to whether the contract was desperately needed. In these cases margins were pared down to the minimum; sometimes to estimated variable costs.

Conferences which were purely conferences in the narrow sense tended to be very price conscious; but the type of conference where social factors also influenced the organiser's choice was not so responsive to price levels and therefore gave the hotel greater freedom in determining its price level. The selling of conferences, therefore, required a high degree of expertise on behalf of the salesmen; something that the non-group member hotelier frequently regretfully noted. It was generally recognised that there was great potential for future development in this area but the small independent units were being forced to recognise their limitations.
SPECIAL FUNCTIONS

These were all approached initially from a cost plus exercise and cost was related to the facilities required. 66-75\% gross profit on sales was a norm surprisingly for both small and large, low, medium and top quality units.

Most units depending on the type of function required, provided a selection of menus at various prices and the choice was then left to the organiser/customer. There was a marked tendency for the most expensive to be chosen. Nearly all the units stated that if they were not interested in laying on a particular function they tended to quote a ridiculously high figure rather than give an outright negative reply.

Numerous hoteliers provided anecdotes of how this procedure often brought lucrative problems in that the quotes were sometimes accepted. An illustration again of how quality is assessed on the basis of price.
FOOD AND BEVERAGE

Food and beverage, like special functions, were almost invariably cost orientated. Within the sample the mark-up on food permitted a 50-75% gross profit margin on sales. Beverage prices had rather narrower margins and they depended so much on the image and style of the units that generalization is impossible. There appeared to be little use of beverage prices as a marketing device.

Most of the hotels recognised that restaurants and bars had to accord with the overall image of the hotel. They recognised too that their reputation and image were established within these areas. Many of the units surveyed stated that the restaurant ran at a loss: yet the calculation of attributable costs varied enormously.

Very few units analysed the departments contribution to overall profits, and though they recognised that an integrated approach should be used some failed to do this in practice.

Within hotel restaurants it appeared that fixed price menus were increasing in popularity. This was regarded as administratively advantageous. Not only does it appeal to the budget conscious, it also has gained popularity in the traditional up-market restaurants. Examples can be found ranging from the Savoy, Inn-on-the-Park and Trust House Fortes Post Houses 'Around a Pound' lunch. This practice is not confined to lunch, but is used for dinner too, e.g. T.H.F.'s Dinner and Theatre ticket at around £5.50 as advertised in the Catering Times, November 1974.
The above account illustrates the diversity of approach encountered: this is not a case for concern because in such a diverse industry different approaches will obviously be needed to allow for individual circumstances.

However the cost-orientation of many of the units gives rise to concern and before an assessment is made of the effectiveness of the pricing procedures we will now turn to a normative study of how in the light of the particular supply and demand characteristics of the industry pricing theoretically should be approached.
CHAPTER IV
A RATIONAL APPROACH TO PRICING IN THE HOTEL INDUSTRY

INTRODUCTION

SECTION A
Specification of Objectives
(a) Identification of Firms Objectives
(b) Pricing Objectives

SECTION B
Analysis of the Environment
(a) External Information
   (i) Market Demand
   (ii) Competition
(b) Internal Information
   (i) Cost
   (ii) Revenue

SECTION C
Selection of Most Appropriate Policy
General Analysis
Specific Examples

SECTION D
Implementation of Decision

SECTION E
Reappraisal of Decision
A rational approach to pricing decisions would involve a synthesis of the conceptual approaches examined in Chapter I with specific allowance for the distinguishing characteristics of the hotel industry examined in Chapter II. Hotels are service centres and therefore of necessity market orientated; emphasis will therefore be given to developing a marketing approach emphasising how a demand orientated approach is essential for accommodation, integrating this with a cost approach to food and beverage which enables in certain circumstances ease of operation.

The first stage in any decision making process is to set out quite explicitly the stages by which the decision is to be reached (1). Pricing decisions prove no exception.

A logical procedure for hotels, large or small, would involve the following stages:

1. SPECIFICATION OF OBJECTIVES.
2. ANALYSIS OF THE ENVIRONMENT IN WHICH THE DECISION IS TO BE MADE.
3. SELECTION OF THE MOST APPROPRIATE POLICY/STRATEGY.
4. IMPLEMENTATION OF THE DECISION.
5. REAPPRAISAL OF THE OUTCOME.

Each of these stages will now be examined in detail so that the main points that should be considered by any hotelier will clearly emerge. The procedural stages are universally applicable to units in the industry. The actual decision made at stage 3 however is very much dependent on the unit in question and no uniformly applicable normative model can be used that would automatically lead to an optimum decision. In a dynamic world the optimum policy may well very substantially over time. It is stressed that owing to the complex nature of pricing problems a framework is essential.

(1) A recognised approach to decision making.
1. **SPECIFICATION OF OBJECTIVES**

This requires the recognition and explicit specification of the objective of the firm as a whole and it is only within this framework that the objectives of pricing policy and pricing strategy can be effectively formed in operational terms.

**Identification of the Firm's Objective**

This task is rarely as easy or as straightforward as one would imagine. Though most firms would state that they are in business to make a profit, the size or level of that profit has to be made much more explicit if it is to be used in an operationally significant way.

The economist's assumption of profit maximization if it is interpreted in its most literal and narrow sense would mean that "in practical terms that nothing - absolutely nothing - which conflicts with profit yields him (i.e. the entrepreneur) any utility at all" (1). We discussed in Chapter I how other utility functions are influential in motivating both owners and managers of firms. Constraints and conflicts are therefore likely to emerge and have to be reconciled if objectives are to be made specific and operational rather than vague and indefinable.

Most firms do not need to be profit maximizers unless they operate in a very competitive market structure and for this situation to arise we have seen in previous chapters that there would need to be no limitations on entry into the industry and an almost homogeneous product. Except for certain geographical areas where competition is extremely fierce and where excess capacity exists most hoteliers do not find themselves in this situation where profit maximization is the only means to survival. In reality therefore most hoteliers can specify the overall objective of their firm in terms of a 'quantifiable and

and specified level of performance*. This viewpoint is reinforced by Hague (1) who argues that even if profit maximization is accepted as the chief objective "the process of budgeting will often convert maximizing procedures into satisficing ones".

The hotel industry, as we have already examined, is characterised by a diverse organisational structure and varies from the small owner-occupier to the large chain type group. Any generalised normative statement about the objectives that firms should set would therefore be unrealistic but size and objectives are closely related. The individual psychological characteristics of the owner will determine the objectives set by the small unit and the large company will invariably have to determine in the light of its past performance and future plans what will be the acceptable return on capital employed that it should aim for.

Any conflicts between objectives must be resolved at this initial stage; to allow the conflicts to continue unresolved will impede effective decision taking. Conflicts emerge in different ways. The small hotelier who wishes to enjoy a quiet life for six months of the year may find that the required rate of return on capital employed may not be achieved unless he remains open throughout the year. He has to decide which he desires most. The large group may find that the profit level and their social obligations to staff may conflict, or the long term growth strategy of the firm conflicts with short term profit targets. These situations must be resolved and the individual hotelier has to decide on his main objective according to the environment in which he finds himself operating and it is only after the overall objective has been accepted that the role of price as a competitive parameter may be determined.

The significance of price as a marketing variable will obviously depend on the individual characteristics of the hotel in question but it is worth pointing out a few general points that need to be considered before both the advantages and limitations of using price as a competitive device can be fully appreciated.

Location, quality and price are the main marketing mix features of any hotel. Location is not a variable and is essentially fixed once the investment decision has been implemented; quality is variable but only within certain limits that were decided when the fixed equipment was installed (e.g. bathrooms, lifts); the service element of quality is variable and within the control of the hotelier providing the structural characteristics of the hotel permit this to be provided on an economic basis. Increasingly however owing to the labour conditions of the industry these are proving more and more difficult to provide except in the top range of the market where customers expect and are willing to pay for service in the traditional sense. We are, therefore, left with price as a variable, directly under the control of the individual hotelier.

In Chapter II it was stressed that capacity utilization was one of the main factors influencing the profit ability of any hotel; it was also stressed that demand fluctuates and cannot be stored. Until recently this problem seems to have been approached from the supply side by increasing capacity to meet peak demand and leaving facilities idle during the off season periods. There is however another possible approach to the problem and that is to use promotional means to switch demand from the peak periods into quieter periods and also to attract new potential customers into time periods when capacity is under-utilized.

Tariff structures may therefore be designed to increase the
efficient use of resources throughout the year. The opportunity for using price as a promotional tool therefore does exist but it is wise to stress at the outset that it cannot be used in isolation from other marketing devices, and it is only if it is used in conjunction with and reinforced by other measures that it is likely to be successful. The public image that the hotel wishes to create will also influence the selection of the marketing mix and the significance of price within these constraints must be appreciated.

The small firm under the direct control of the owner will obviously be able to implement his decisions effectively. The larger firm should however at this stage identify the weaknesses of organisational structure that will impede pricing objectives being met. "It is not enough for top-management alone to understand the objectives" (1). It is vital, as Oxenfeldt has pointed out, that pricing responsibility should be vested in men suited by training, interest and temperament for the task. Joel Dean has pointed out that in normal times pricing is often the businessman's least pressing worry and it is often only when profitability falls to dangerously low levels that the significance of effective pricing is realised.

Large firms owning more than one hotel will have to make a definite decision at this stage regarding the amount of centralized control they will exert over the pricing policy of the individual units under their control.

An overall rigid control policy may be adopted and then the price policy will be arbitrarily enforced on the individual units. An advantage of this system is that it ensures that the decision is made by a pricing expert and if the firm utilizes a group marketing philosophy it will ensure that the 'image' of the firm is projected satisfactorily. However this standardized arbitrary approach cannot allow for regional

(1) Hague, p.94, op.cit.
and local variations and it would be extremely unlikely that maximum 
profits would result from this method.

An alternative is to allow the individual units complete freedom 
regarding their pricing policies. Though this provides scope for 
regional or local differentials it will rarely enable the group as a 
whole to maintain adequate control and administrative constraints, 
including that of finding suitably qualified unit managers, means that 
it is rarely practicable.

The advantages of centralized decision taking can be incorporated 
with the required individual flexibility, if the firm provides a guide 
line or framework for the individual units and then, allows suitable 
variations to be made according to the particular external environment 
in which the unit is located. The variations would normally be kept 
under careful scrutiny by Head Office to ensure that they are 
compatible with the overall objectives of the firm and the amount of 
freedom may be varied according to the individual need.

To summarize, it is worth re-quoting from Hague, that (1) "the 
important thing is for those taking pricing decisions to isolate the 
objectives that are relevant to each individual decision" and "at the 
very least they must understand how objectives are to be ranked in 
taking each decision and then give priority to the most important ... At 
best they should decide on a mutually-consistent set of objectives 
for each decision".

Those are the general points that should be considered when 
deciding on the pricing objectives. Before practical decisions can 
be taken specific attention must be given to the external environment 
in which the particular firm finds itself working. The main elements 
worth concentrating on are enumerated in the next section.

(1) D.C. Hague, p.94, op.cit.
2. AN ANALYSIS OF THE ENVIRONMENT IN WHICH THE DECISION IS TO BE MADE

No firm operates in isolation and for this reason it is essential to be fully aware of the environment in which the firm operates. Particular constraints on the individual firm may originate from factors outside its own control, but some may have their origin within the internal organisational and structure of the firm itself. This stage, in essence, is one of collecting information and analysing its importance and relevance to the decision impending.

I. External Information

First, let us concentrate on the external environment in which the firm operates. This stage involves the collection and processing of the information which will be directly relevant to pricing decisions.

Information is rarely completely free and so the cost of collecting information should be carefully appraised and set against the potential or expected benefits to be derived from the expenditure. There will be a minimum level below which decision making will be merely guesswork and so a positive return will be automatically expected but it is also feasible that too much information may be available. Hague (1) argues that "this will be the case when a number of interrelated variables have to be taken into account in making a particular decision. Even if the precise nature of the relationships between the variables in question is known, the human brain is incapable of handling more than one or two quite simple relationships of the kind met with in most pricing problems". This is a very real problem to the small firm in the industry. The large firm however can take advantage of the fact that "with computers things are different. They can handle large amounts of complex information with ease". The sort of sensitivity analysis undertaken by the N.E.D.O. study (2) is a noteworthy example of how the

(1) D.C. Hague, p.95, op cit.
interrelationships between various marketing parameters and the resultant profit changes can be clearly analysed. Marketing groups or associations should in the future be able to provide this sort of information for the smaller hotelier unable to collect or process such information on his own. A minimum level of information is an essential prerequisite to effective decision taking and the main areas where information is essential are discussed below:

A. Market Demand

This involves identifying the source of past, present and anticipated demand.

Segmentation into the relevant subsections is essential to identify the pattern and interrelationships that exist.

The most useful format may well follow the categorization below:

- ACCOMMODATION
  - BUSINESS
    - Domestic
    - Foreign
  - NON-BUSINESS
    - Domestic
    - Foreign

- FOOD AND BEVERAGE
  - Dependent on Accommodation
  - Independent of Accommodation

- OTHER RELEVANT AREAS, e.g. Conferences, Special functions, Sub-Depts., e.g. Hairdressing, etc.

A profile of consumers will then need to be constructed: this information should be readily available to the established concern.

The direct involvement of the hotelier with his customer means that a realistic picture of consumers, their individual characteristics, needs and preference can be compiled. Average income levels, social backgrounds, purpose of visit, nationality and length of stay is the type of information necessary in order to assess whether the facilities
on offer and the prices charged for accommodation, food and beverages are compatible with the preferences of the customers the hotelier is attempting to attract. It is often surprising to marketing experts from other industries that so little emphasis and attention is directed towards this readily available information within the hotel industry.

The segmentation is particularly important in order to ensure a successful marketing strategy. The division between business and non-business demand segments illustrates how motivations, drives and therefore requirements for success varies with the type of market demand.

The businessman travelling from necessity and not merely for pleasure will have a much more functional approach to the selection of a hotel; ease of access, the provision of a quick efficient service and the availability of special services, e.g. telephones, may well be the deciding factors. Hotels for the casual or the occasional visit will not be selected with the same rigour as those that are regularly visited. The businessman's choice will not be influenced ostensibly by price because the payment will not be coming out of his own pocket, but if his firm operates a ceiling price for accommodation or meals then he will be concerned with the qualitative aspects he can obtain within the price ceilings. In times of low business activity this restrictive influence is likely to be more significant. Many large industrial and commercial firms negotiate direct with the larger hotel groups on a national and even international basis, discounts being given in order to secure regular business. Small hoteliers are therefore at a disadvantage in this respect but membership of a group marketing scheme may well prove advantageous in this situation. It is obvious that the individual unit should be fully aware of the commercial activity within the area and the amount of use that is made of hotel facilities.
B. Competition

Information regarding the nature and extent of the competition facing the unit is essential if rational decisions are to be made and Chapter I emphasised the significance of market structure on the behaviour of firms.

The first step is to identify actual competitors and secondly to assess the degree of competitiveness that they offer. This survey must be comprehensive and not merely limited to the immediate vicinity in which the hotel is located. Local competition is easily identified but even if there are no hotels of comparable quality/service/price combinations as the unit in question it does not mean that one is immune from competition and it is necessary to identify whether there are competitors further afield, even abroad, that are likely to be equally attractive to customers. National and International comparisons, therefore, need to be systematically made.

It would also be inappropriate to concentrate the search for competitors solely within the hotel industry. In the lower end of the market, competition is experienced from holiday camps and self-catering units of one sort or another. The price or non-price attractions of these need to be carefully assessed because they are realistic substitutes for the average holidaymaker looking for reasonably priced accommodation.

Another aspect which needs to be taken into account is the fact that apart from the business sector consumer expenditure in hotels is discretionary. This means that in an age of affluence and increasing leisure time hotels have to compete with a whole range of other miscellaneous consumer goods and services if they wish to increase their proportion of consumers' discretionary spending. In most consumer goods markets aggressive advertising and sales promotion techniques are recognised ways of increasing their share of consumer spending.
Looked at in this light, the profit seeking hotelier should not confine his analysis of competition too narrowly but be outward looking and seek to attract new customers as well as to retain the interest of existing ones. He should build up a profile of the customer using his facilities and assess their reaction to price; an estimate of their awareness and sensitivity will be necessary. Then he can decide whether price can be used as a persuasive or communicative device.

The degree of interdependence of accommodation, food and beverage departmental sales will also need close perusal: invariably they are complementary services and the demand interrelationships will be complex. An attempt however should be made at identifying the sources of demand for restaurants and bars.

The information so far accumulated will be historical or current. Planning however involves looking into the future and it is anticipated market demand that is relevant for decision making. The information therefore has to be analysed and predictions made regarding the future. The National Economic Development Council and British Tourist Authority publications are a source of national and international trends; local and regional trends depend on developments within the local community.

National groups are obviously at a considerable advantage for discerning and predicting overall trends but often find themselves at a disadvantage for local and regional analysis: the reverse of course is true for the smaller owner managed units who though intimately aware of local developments may well find themselves outpaced by changes in national and international trends.

An assessment of the degree of competition offered is a task which involves skill, judgment and experience. Qualitative differences in facilities and service offered are fairly easy to assess but care must be taken if comparisons are made from issued tariffs. It should be
ascertained whether various extras are free or the extent to which extra payments are necessary. An additional problem here is that the real price charged as we have seen may differ quite considerably from issued tariffs, and it is therefore necessary to collate information regarding the nature and extent of discounts given. These may differ both seasonally and regionally. In areas where excess capacity exists the discounts are likely to be substantial and an individual hotelier who ignores this practice would find his profits adversely affected unless he could offer some substantial off-setting advantages in lieu.

Competitors may be offering special 'inclusive terms' that appear very competitive. However if they are operating a 'Backward' Pricing policy and reducing certain inputs this would be an illusion distorting the real price differentials. An assessment of rivals' marketing philosophy is also useful at this stage as it would indicate the type of customer and market segment that they are aiming at.

From this assessment of competition decision makers will be able to calculate the amount of freedom available in the setting of prices and if possible the price threshold of the consumer, indicating maximum and minimum limit prices, may be identified.

Other external information which is useful at this stage are the occupancy survey reports of the various Tourist Authorities. These are useful for comparative purposes: in England for example the information covered by the English Hotel Occupancy Survey (1) is analysed and presented on the basis of location and price: assessments of the price/quality image projected by the individual unit therefore can be made. If these are unfavourable then the need for readjustment in marketing will be apparent. Scottish and Welsh areas are also covered by their respective tourist authorities.

(1) English Hotel Occupancy Survey, published monthly by English Tourist Board and annually summarized by their Research Unit.
II. Internal Information

The accounting department invariably provides most of the internal information used by firms; unfortunately the accounting information that is collected in many firms was originally designed to provide historical information to owners, shareholders or tax authorities regarding the profit performance and capital value of the firm, and is not suitable for decision making without further modification. In a large firm the co-operation of management accountants, economists, production departments and the marketing section would be necessary. On this basis a comprehensive picture of the structure and behaviour of costs can be constructed so that optimum decisions could be reached.

Firstly if the most efficient use of resources is required then decisions should not be based on average values but should be based on an assessment of the true opportunity cost involved in providing the service in question. Opportunity cost measures the cost of a given course of action in terms of the opportunities sacrificed.

Cohen and Cyert (1) have stressed that "the cost of a productive factor is the maximum value that this factor could produce in an alternative use". Joel Dean (2) has put this viewpoint in a rather different way by emphasising "in business problems, the message of opportunity costs is that it is dangerous to confine cost knowledge to what the firm is doing. What the firm is not doing but could do is frequently the critical cost consideration which it is perilous but easy to ignore".

In reality the correctness of estimates of opportunity cost are hard to test because "once one course of action is taken all the alternative actions are ruled out" (3). Nevertheless this approach is fully justified even if it only makes the decision maker critically

(3) D.C. Hague, p.179, op.cit.
aware of the alternatives he is foregoing.

Another point worth stressing is that pricing decisions are concerned with future actions. The relevant costs are therefore expected future costs. Historical costs will undoubtedly provide a reference model for calculating expected costs and in some cases may present an adequate guide-line. In times of inflation when cost increases are large increased emphasis should be given to the dangers of using historical cost as a basis for decision making in a dynamic world. This point is relevant to all firms but perhaps more pertinent to firms whose publicity material (e.g. brochures) has to be prepared well in advance. This would also be true of deals negotiated with package tours or agencies where a 12-15 months time lag is not unusual.

The next stage involves the appropriate distinction between various costs. The distinctions between fixed, semi fixed and variable costs were analysed in Chapter II and will not be re-analysed here. The distinctions however should be utilized in order that cost-profit-volume relationships for the individual firms in question should emerge clearly.

Horngren (1) has stressed that "the real benefit of preparing breakeven charts is in the enrichment of understanding of the interrelationships of all factors affecting profits, especially cost behaviour patterns over ranges of volume".

At this stage in order to overcome the considerable problems of using this technique where costs and revenue are non-linear, management should concentrate its effort on constructing these charts only for the relevant range of changes in occupancy that are being analysed. This will for most hotels differ seasonally and so separate analysis needs to be undertaken according to the seasonal variations experienced by the firm in question. This information should already be recorded

internally, if not use will have to be made of external information as suggested in the previous section.

A hotel is really a multi-product firm but unlike multi-product firms in manufacturing the goods produced are highly complementary. Except for circumstances, as previously mentioned where this interdependence does not hold, the services provided will therefore have to be regarded almost as a single service. For control purposes departmental expenses will have to be charged against department revenues but for pricing an integrated and 'total' approach will be essential.

(b) Revenue

Information will also need to be assembled regarding past sales revenue and the present situation. Ideally one would want to have information that correlated sales fluctuations to changes in variables such as price, income, quality variations, facilities, sales promotions, etc., so that a total picture of all the factors influencing Revenue can be assembled.

For food and beverage pricing information regarding consumer s' choice from menus, wine lists, etc., their average spending power, etc. will be an essential part of the volume forecasting that is necessary as an initial basis for price determination in these areas.

With detailed information regarding the cost structure, competition, patterns of demand and market trends available and presented in a logical way, the next stage is for the price decision maker to identify and evaluate all the alternatives that are available.
3. SELECTION OF MOST APPROPRIATE POLICY/STRATEGY

This is the most rigorous, difficult and crucial stage of the decision making process. It is imperative that a logical approach, recognising the need for pricing to be fully integrated and compatible with other marketing decisions, is consciously developed. It is worth re-stressing at this point that hotels are significantly restricted by the fact that output is not flexible and that capacity constraints operate.

The first step involves identifying the range of alternatives open to the individual unit. It is rare for no possible alternative to exist but commonplace for the range of options to be fairly numerous. Some of these for legal or ethical reasons may be impracticable. An evaluation of the merits and defects of each real option will therefore be necessary and for hotels the most suitable pay-off measure will invariably be in terms of profits. Great care should be taken that 'occupancy' is not over-emphasised because a hundred per cent occupancy at too low a price does not necessarily generate maximum profits. Skill should also be exercised in distinguishing between long and short run effects.

All pricing decisions contain elements of risk and uncertainty; firms may therefore approach the problem by identifying the probability of certain outcomes and then selecting a policy using decision makers, 'Maximin', 'Maximax' or 'Laplace' criteria. For the large groups with sophisticated techniques and the personnel available this approach may be realistic. The average hotelier however will be forced through practical necessity to be much more prosaic and his eventual choice will depend to a much greater extent on his judgment and personal assessment of the risks involved (1).

In an industry as diverse as the hotel industry a standardized or

(1) Many small Hoteliers seem because of the personal risks involved to be using maximin criteria rather than maximax.
uniform approach to the selection of a pricing policy would involve an arbitrariness that would be totally unacceptable and in many instances positively harmful. A flexible approach is essential because the alternatives open to any particular unit are profoundly dependent on the individual characteristics and features of the unit. The particular external environment in which it operates is another major determinant.

For this reason no attempt will be made to construct a universally applicable pricing model but decisions that are common to all situations are analysed at first in a general way. Suggested policies for particular situations are then presented in a more specific manner. At the outset two options face the individual unit: either they can price at the market level or they can pursue an individualistic policy.

**PRICE-TAKERS**

The former involves an abdication of pricing decisions to imitating the actions of particular rivals and competitors. In a very competitive situation, where there is little differentiation between units, this may well be an appropriate solution. These are the price takers of the economist's perfectly competitive model discussed in Chapter I, and a common occurrence for the small unit in the industry as examined in Chapter III.

It is often feasible for units operating under this system to earn a satisfactory rate of return on capital invested and as we have discussed earlier many small independently owned hotel units are not profit maximisers. Certainly this abdication of a time consuming, mind stretching task to one's competitors makes life a great deal easier. As no research or information apart from the price charged by
one's competitors is required it is also the least cost method. As the present survey revealed many small units accepted the market price and then made small adjustments to the inputs so that their particular required objective could be achieved.

It is not necessary that a rigid price level should be followed throughout the year. Seasonal variations may be incorporated within this policy according to the lead set by the market or the price leader. In the same way departmental mark-ups and contributions are decided on a comparative basis.

PRICE MAKERS

The alternative open to the unit which does not wish to follow the market and be a passive price taker is to adopt an individualistic approach and to become a price maker. Three options present themselves:

(a) He may accept the role of price leader and determine the price level of the relevant market segment in which he operates,

(b) He may deliberately choose to price above the market level, or

(c) He may decide to price below the market level.

The option selected will reflect the individual characteristics of the hotel unit, but the following points will need to be taken into consideration.

As we have already analysed the main revenue creating departments in a hotel are accommodation, food and beverage. In some units other facilities are provided but they rarely provide a major proportion of the revenue. The inter-dependency of the departments must be taken into consideration: the level of demand for food and beverages is in
many hotels intricately related to the room occupancy level but in some hotels the reverse may be true and the occupancy level itself may be influenced by the quality and reputation of the restaurants and bars.

The pricing approach will obviously be influenced by the Sales-mix of the individual units: it is the sales-mix that largely determines the revenue and cost structure. Very few hotels offer 'en-pension' terms alone and so separate price lists will inevitably have to be drawn up for accommodation, food and beverage. The pricing structures must on no account be determined independently but should be made as a 'total business pricing' or fully co-ordinated effort (1). Each department's variable cost should be identified and from this their contribution to overheads should be assessed. This is essential in order that the pricing can be market-orientated. It is not necessary to maximise the contribution of each department; it is the total contribution of the hotel as a unit that needs to be considered and for this purpose it may well be necessary for some of the departments to subsidise others.

The floor for short run tactical pricing decisions will be variable cost: the ceiling will be the amount that consumers are willing to pay. The former is fairly easy to identify, the latter is extremely difficult and requires flair, judgment and experience. The hotel industry's high overhead costs means that the difference between variable cost and the theoretical ceiling will be substantial: far larger than that in many other service or manufacturing industries. This means that the price discretion open to the price maker at least in the short run is very large and that this point combined with other features of the industry that enable price discrimination, means that the problems involved are more acute, subtle and difficult than in other industries.

**Accommodation pricing permits the widest degree of price discretion**

because the variable cost element is lower than for food or beverage where the cost of materials inevitably forms a larger proportion of the final selling price. Accommodation charges must therefore be carefully related to the level of demand and an absorption approach should not be used.

Food pricing will need to be based on an effective food cost control system: the problem of installing an adequate control system is difficult in this industry because of the sales instability on a daily, weekly and seasonal basis (1). This instability demands that great emphasis should be given to volume forecasting so that a basis is available to ensure that the necessary gross profit margin on sales is achieved. In the short run labour and other overheads are fixed and cannot be allocated to individual items of output. Price has therefore to be regarded as a series of contributions covering food cost, labour cost, overheads and net profits (2). It is customary in food and beverage pricing to use a gross differential profit margin on sales as a basis for pricing. This facilitates ease of operation and is also useful for control purposes. The gross profit margin required on food costs will depend on the amount of contribution to total profits that is required from the restaurant in question, the estimated turnover expected and the particular sales-mix chosen. Items on a menu need not all generate the same gross profit margin and it may well be more useful at times to aim at a given contribution per cover. The use of cyclic menus is a useful aid to improve the reliability of volume-forecasting as over time a pattern emerges of consumer choice and through the learning process an accurate sales mix history can be compiled and extrapolated into the future. Standard yields and standard recipes will also provide an improved basis for menu costing and pricing.

With inflation it is necessary to ensure that the cost basis used for

(2) See Kotas, R. and Davis, B. (op.cit.), p.21.
pricing is current and not historical.

The gross profit margin selected must reflect the consumers' tastes and preferences, their spending power, their awareness and sensitivity to price levels and above all the degree of competition that is offered by rival competitors. Some units of course will be very price sensitive, others will enjoy relative immunity and a price inelastic demand: the role price has to play will reflect these considerations. In the former case care will have to be taken not to overprice as it would involve a considerable reduction in total revenue; in the latter the danger of underpricing is very real.

Beverage pricing will involve a similar procedure to that of food: to a certain extent in most units the problems will however not be so complex as the question of perishability does not arise. Gross margins will have to be determined in the same way although the room for manoeuvrability will be reduced. The relative margins achieved within the sales mix can be adjusted according to the image that the unit wishes to project. Studies should be made of the way that potential customers assess the price-level of beverage sales. In some units it may well be the price of spirits, in others it may be the price of beers or minerals: these items should be given particular attention and care should be taken that the traditional mark-ups should not necessarily be applied automatically and without careful consideration of the attitudes of the consumer. Adjustments in the gross profit margin on items within the range on offer will inevitably be necessary if an optimal price strategy, fully integrated with the overall marketing philosophy of the unit, is to be achieved.

Effective marketing will usually mean that a distinction has to be drawn between drinks sold at a bar and those accompanying a meal in a restaurant. Howley (1) has emphasised that in licensed hotels only

a minority of customers order wine at lunch-time and on average only 56% of those dining in the evening. He argues that this means that there are a large number of potential consumers and that it would be to the advantage of the hotelier to encourage further wine consumption. Various suggestions are made, one of which suggest that, apart from high-spending units where wine is frequently regarded as a complementary good to the meal itself, in many units more effective pricing could stimulate the demand. Clearly listed wine prices on the menu rather than on a separate wine list for the customer to peruse at leisure is one suggestion and the feasibility of reducing the traditional 50% gross profit margin on wines in units that are price elastic is suggested as another possibility.

There are only a very few hotels in the U.K. which do not experience peak demand periods either on a weekly or on an annual basis. Most hotels are faced with the problem of fluctuating demand patterns; the extent to which these are going to influence the pricing strategy will depend on the extent and duration of capacity under-utilization.

The practice of charging differential tariffs on the basis of variations in demand over time is well established in other service industries such as electricity and transport areas where high fixed costs and a non-storable product provide similar problems to the hotel industry. In these industries marketing techniques concentrate on the price differential for attracting consumers. In these areas the use of price as a communicative and persuasive device is very effective and so hoteliers should assess very carefully the feasibility of using price concessions in the off-season, not merely as a temporary expedient but also as a means of encouraging the entry of new potential customers to the industry as a whole. It is this long-run implication for promotional purposes that appears at present to be appreciated by only a minority of the industry.
It is worth quoting Hague's (1) advice on the question of variable cost pricing: "We should therefore perhaps emphasise at the earliest possible moment, that neither we, nor anyone else in his senses, advocates actually charging marginal cost except when a firm is in quite desperate trouble. The aim is not to charge marginal cost but to relate price to marginal cost" and to determine "what is the optimal margin over and above marginal cost for us to charge on this occasion".

By manufacturing industry standards hotels are in "quite desperate trouble" for a significant part of the year. Low occupancy means that capacity is under-utilized and though demand in the high season is often greater than supply the 'service' cannot be stored and is therefore highly perishable. Variable cost should therefore be the basis for pricing policy in the off-season. Care must however be taken that price concessions in out-of-season periods will not merely transfer demand from high season and so create surplus capacity in the high season when it is most lucrative and customers will need to be reassured that they need not be apprehensive about the quality of service offered. Within the last three years in particular the use of price concessions as a means of attracting off-season custom has been increasing and is now generally accepted by the public as a 'true bargain' and has encouraged many people to take a weekend break or second miniholiday.

Another advantage of using differential pricing is that in the present situation of labour shortages a unit may find it highly beneficial to keep a skeleton force of highly skilled labour on a permanent basis and so for the off-season in terms of opportunity cost it may even be acceptable to go below variable costs if the benefits of staff retention are estimated to outweigh losses. Great care would need to be exercised however if this policy was to be adopted and a rigorous

(1) D.C. Hague, op.cit., p.136.
cost-benefit analysis of the decision to remain open all year would be necessary.

Another point to take into consideration is that beverage sales are so dependent on accommodation sales that often these will provide a further substantial contribution to profits so that apparent losses on accommodation sales will be recovered from increased turnover in other departments. Few units reduce prices in the Food and Beverage departments in the off-season but there is no reason why reductions should not be made in Food and Beverage Gross Margins. Often this may be achieved, in an era of rapid inflation, by holding price rises that were due in the off-season until the beginning of the peak demand period so that prices appear more competitive.

The alienation of regular customers is the main point that has to be taken into account when contemplating variable food and beverage prices. There is however no reason why the pricing of special promotions or the table d'hote menu should not reflect the level of capacity utilization throughout the year. Dinner/dances for example can be successfully priced at different levels throughout the week to correspond to demand variations. The amount of flexibility and discretion in food and beverage pricing is much narrower in the case of food and beverage than for accommodation.

An alternative to accepting business in the off-season that contributes something towards overheads is to charge higher and higher prices in periods of peak demand. Until recently this approach was adopted by many hoteliers. This undoubtedly has had an adverse effect on the demand for hotel accommodation overall and has contributed to the substantial growth in substitute forms of accommodation. For the long term marketing prospects of the industry therefore it is essential as far as possible to hold down prices in the peak season by accepting a price that may be below average cost but above marginal cost in the
off-season.

Lewes (1) in his survey of the Holiday Industry of Devon and Cornwall concluded that "there is no doubt that over-large differentials are unpopular with holiday-makers although a degree of price change over the season seems to be accepted in the case of accommodation. It might be that a gradual increase in differentials would be preferable to a general increase in prices and that there is a case for more flexibility in pricing."

From a psychological point of view consumers in general always appreciate 'a bargain': it would therefore seem to be preferable for hotels to fix a basic price for accommodation and then to offer concessions for the off-season rather than the present practice in some units of quoting a minimum charge and then adding on surcharges for the high season.

The criteria for deciding on off-peak price concessions is in essence quite simply stated. If capacity would otherwise remain idle unless price concessions are used to attract extra business then providing the price is above variable cost it is always beneficial. A contribution is made to total overheads that would be incurred regardless of the occupancy level. The use of appraisal forms such as that illustrated in Figure 4.1 may aid the actual decision making. A unit which has not attempted variable pricing could set out the previous year's occupancy, revenue and costs. Variable and fixed costs should be identified, estimated occupancy, budgeted costs, etc. compiled and predictions made regarding the impact of flexible pricing. As the uncertainty would be high, estimates could be made on a probability basis giving best possible, worse possible and most probable outcomes. This would facilitate a more rational decision than a single estimate.

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Column 3 minus Column 4 = Profit or Loss.

Figure 4.1(a): Previous Years performance.
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<thead>
<tr>
<th>Next years expected outcome with rigid pricing</th>
<th>Price</th>
<th>Occupancy projections</th>
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Revenue - costs = Profit or Loss.

Figure 4.1(b): Projected performance with rigid price policies
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<th>Next years expected outcome with flexible pricing</th>
<th>Prices</th>
<th>Occupancy projections</th>
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Revenue - costs = Profit or Loss.

Figure 4.1(c): Projected performance with flexible price policies
It is extremely rare for a hotel having proceeded through the stages so far suggested to be able to ignore external considerations. A decision therefore will have to be made regarding the degree of manoeuvrability open to the firm regarding the range of possible prices they could charge. If the degree of competition is high then even though the hotelier intended to pursue an individualistic policy he may be forced to be a price taker as previously suggested.

However he may decide that there are substantial advantages in pricing above the market level. In this case it would probably be necessary for the relevant market segment in which he is operating to be price inelastic, and this implies that the unit would need to be in the top range of the market, serving consumers to whom price is relatively unimportant. It should be checked that any fall in occupancy would be adequately covered by the higher profit rate earned.

As suggested in Chapter I, the work of Gabor and Grainger has suggested that for various reasons many consumers assess quality by price. Higher prices are, therefore, interpreted to mean higher quality. As there are few objective criteria on which to assess the quality of a hotel any assessment of the value to be derived from hotel usage is necessarily subjective and almost totally dependent on the personal preferences and perceptions of the customer. The hotel industry therefore enjoys a much greater immunity from the effects of comparative consumer evaluations than manufacturing or even other service industries. An additional factor is that a prior assessment of value is impossible and customers can only determine whether the high price was justified after they have sampled the offering. This means that units relying on regular or repeat customers cannot price above the market level unless the facilities, location or atmosphere are unique or distinctly different from the alternatives available, so that high prices are warranted. There are of course some customers who for
prestige reasons are willing to pay for 'unique' characteristics or historical reputations. This as we have seen is true of many of the well-known London hotels.

A decision to price below the market level will mean that demand is assumed to be very responsive to price. As has been previously indicated there is a danger (apart from off-season variations) that consumers judging quality by price will regard a lower price in an unfavourable light and withhold their custom. On the other hand price considerations are important in the lower end of the market and so to ensure high occupancy levels pricing below the market level can bring substantial benefits. This can also be used as a device to discourage entry of new units or the expansion of competitors who have identified the market segment as an above average potential profit earner. This means that short run limitations on profits are accepted as a means to ensuring long-term profitability or even survival itself.

Looking at the present over-capacity in London it is interesting to speculate that if prices had been contained in the late 1960's whether so many new hotels would have been built and what the effect on long term profit levels would have been.

In the oligopolistic market structure that exists on a local and regional basis the fear of price wars are a constraint on using price decreases as an active means to boost occupancy and attention needs to be paid to the possibility that aggressive price wars may be disastrous. In these circumstances it may well be that a form of Backward Pricing will inevitably be the only realistic approach.

However, it should be stressed that it is only in certain circumstances that such an approach will prove possible. Apart from the brand-new unit where the qualitative and service inputs can be comprehensively adapted, established units will be limited and constrained by the existing physical structure of the unit itself.
Substantial alterations to the service element are often extremely difficult, although minor variations are nearly always feasible. In a very competitive situation where overt price competition is impossible, or undesirable the possibility of backward pricing must be given careful consideration. A visual representation of the impact of internal and external environment on the range of pricing options is given in Figure 4.2.

The above approach to pricing has been essentially market orientated. Costs have not figured largely in the calculations and this has been deliberate: pricing in an industry with the supply features and fluctuating demand of the hotel industry must be demand orientated.

Costs should be used to ensure that an adequate rate of return is derived from the price under consideration. If the margin is insufficient and providing all forms of cost control have already been used and there are no opportunities for other forms of sales promotion then two broad possibilities emerge.

Either an adjustment has to be made in the inputs to ensure an adequate return or the image of the hotel has to be altered to appeal to a market segment willing to pay a higher price. This may involve building conference facilities and encouraging the businessman or installing facilities (e.g. an internal heated swimming pool) which will allow higher prices to be charged without an occupancy fall and hopefully to boost occupancy as well.
Figure 4.2: The external and internal environment and the impact on pricing options.
FACTORS INFLUENTIAL IN DETERMINING THE PRICE POLICY/STRATEGY CHOSEN

The remaining section concentrates on highlighting some of the significant factors that will influence the individual units choice of pricing policy. This singling out of some of the major determinants is an attempt to offset the generalized approach that has been used so far.

(a) Location

The influence of location on hotel profitability is considerable as we indicated in Chapters II and III, and is the reason why effective feasibilities studies should be undertaken prior to investment decisions. Here it is proposed to emphasise the extent to which location impinges on pricing policy.

A good location means that the unit will have a much greater degree of freedom regarding pricing policy because the overall marketing task will be much easier. It is difficult to generalise on the factors that make up a good location: the same features may enhance one unit but restrict another. Accessibility to communication routes, proximity to areas of scenic beauty or historical interest that appeal to tourists or proximity to areas of commercial/business activity are general headings under which the main locational advantages may be classified. A realistic assessment of the particular merits and drawbacks of the location for the unit under consideration is imperative when deciding on the pricing policy to be adopted.

A poor location imposes considerable problems on management and means that an effective marketing strategy has to be devised to offset the locational disadvantage. The significance of price as a marketing variable therefore has to be closely assessed. Poor location can be compensated for by providing value for money - this means that the price charged must be regarded as reasonable if repeat bookings etc. are to be achieved and if location is poor a greater emphasis will have to be
given to attracting regular customers rather than relying on the 'passing trade'. A lower mark up will probably have to be accepted. Within this context Backward Pricing may provide a suitable framework for ensuring that price appears competitive to potential customers. It is always worth considering carefully the extent to which changes in marketing and the service element are feasible in order to compensate for poor location. The use of price as an information device to attract potential customers and initiate inquiries is certainly worth careful consideration.

(b) Qualitative Features

The range of hotel accommodation services provided within the U.K. is very wide and shows a far greater degree of differentials than is indicated by the commonly used star-rating procedure which divides hotels into five major classes.

For pricing purposes each category becomes a separate market, delineated according to the customer's tastes, preferences, his income and socio-economic background and the availability of substitutes. The distinctions however are not rigid and marginal differences mean that between each category is a 'grey' area where markets overlap and where competition may be vigorous.

Luxury 5-star rating hotels: These hotels are frequented by very high income and asset-owning individuals, who with a very few exceptions are unlikely to be influenced by tariff charges. Qualitative considerations are therefore a major consideration of management and price takes on a passive role. Great care has to be taken to provide the level of luxury and service that are required. As we have seen high prices are a status symbol so management must attempt to identify the ceiling price that customers are willing to pay. The dangers of under-pricing are more real than those of over-pricing.
Four-star Hotels: These hotels again are frequented by high income groups but the emphasis on the uniqueness of the hotel and the quality of service is reduced. In most areas customers will face a relatively wider choice of hotels and so comparative assessments are likely to be undertaken and this must therefore be taken into consideration.

Again care must be taken that price is not regarded as an indicator of quality before any price type promotion schemes are undertaken. However in this category price is probably significant to a larger percentage of the customers and advantages and disadvantages of quoting an 'all in' price should be thoroughly investigated.

Four-star hotels which experience seasonal fluctuations in demand may well find it profitable to offer special rates for off-season promotions especially as the type of customer using the hotels are likely to belong to the socio-economic group that would favour a spring/autumn mini-holiday or winter weekend break. These customers are also likely to enjoy the sort of occupation that permits off-season holiday breaks to be taken. Special Interest promotions, e.g. Golf, Music, Gourmet, Riding, etc. are often useful marketing angles to take for these promotions.

Three-star Hotels: These are frequented by individuals who from necessity rather than choice are forced to pay attention to the price level. Price is therefore much more influential and can be used as an attractive marketing variable. Competition is much fiercer in this category and attention must be paid at least at the lower end of this category to alternative forms of holiday accommodation outside the industry. For off-season promotions pricing can be used with great effect especially if an 'all-in' price is quoted. The exclusion of
service charges and V.A.T. though it might entice a customer once will not ensure repeat bookings and the 'bait' pricing effect is not successful for long run promotions. In this category price may be used as a promotional tool and as an information device to encourage the more regular use of hotel facilities. Special interest promotions are again an attractive marketing aid.

Two-star and one-star categories: These represent the lower end of market where lower income groups are obviously going to be very much aware of prices charged and differentials between competitors. For this reason the room for manoeuvrability of pricing strategy is limited and there is often no option but to follow the market.

Attention must be paid to the fact that in this category the customer's option to take other forms of accommodation (e.g. rented self-catering accommodation) becomes a very relevant factor in determining prices charged.

A large proportion of units in this category are small owner-managed units who as we indicated in Chapter II may not all be motivated by profit maximization so that price takes on a neutral role in their marketing strategy, acting as a significant constraining influence on the amount of service and facilities offered. Backward Pricing will again in this situation be relevant.

(c) Age of Unit

The age of the unit exercises a considerable influence on pricing strategy. The brand new unit is obviously faced with the most challenging problem regarding pricing strategy but first let us consider the well-established unit.

(i) The Established Unit

If the unit is running successfully then the role of price as a competitive variable will not need fundamental reappraisal. However
it would be useful for the unit to assess the extent of customer
loyalty and/or other reasons for its success so that future performance
can be predicted in the light of expected trends.

Joel Dean (1) has stressed that "the amount of price discretion
that a seller has depends on a number of conditions" including
competition and potential competition: it also depends on "the stage
of consumer acceptance of the product".

For most products there is a definite product cycle: sales build
top slowly, reach a maximum after a few years, and then decline. There
is no reason to suspect that hotels are in any way exempt from this
dynamic tendency and so attention should be paid to the stage of
development and an assessment made as to whether pricing policy or
other marketing variables should be amended as time proceeds.

The established unit which is not recording a satisfactory
performance will need a thorough reappraisal. The reason may be
attributable to its location, which has been discussed; it may be
production/service defects or it may be on marketing grounds. If the
latter then the role of price will need to be re-examined. If a rule
of thumb cost plus approach was being used then the defects as related
in Chapter I should be analysed. The potential benefits of a new
market orientated price structure or a Backward Pricing approach should
be investigated to see if a solution is possible. It may well be that
off-season promotions will contribute sufficient to overheads to enable
a satisfactory performance to be achieved.

(ii) The New Unit

This is a situation where the degree of uncertainty will be at a
maximum and where historical factors can provide no guidance. On the
other hand because the slate is clean management will have a greater
degree of freedom to implement policies without suffering from the

(1) J. Dean, p.402, 'Managerial Economics', op. cit.
limitations, constraints and consequences that previous non-optimal
decisions may impose.

The degree of differentiation and the amount of competition will
be the prime variables affecting the degree of manoeuvrability open to
the unit. As the initial price charged will exert an influence on
the future pattern of demand two opposing tendencies will emerge.

A low price charged initially will attract customers, especially
if demand has a high price elasticity, so that the market is captured
and this will also forestall the entry of new firms over the long run.
However, a danger of this approach lies in the fact that if costs are
under-estimated for the future, which is probable in inflationary
times, then it may prove difficult to raise prices to maintain profits
without alienating customers. This type of low initial price is
referred to as 'price penetration' policies. Hotels however have,
unlike manufacturing plants, capacity constraints and so if high
occupancy is achieved and further extension limited, further increases
in demand will not increase profits and so low initial prices will not
bring the long run advantages that they do in manufacturing industries.

A high initial price may however be more profitable if the demand
is inelastic. This is as we have previously pointed out feasible for
hotels where the difficulty of 'valuing' the service is formidable.
High initial prices especially if it attracts customers looking for
something 'different' will provide a quick pay-off for the firm in
question and of course it is always feasible to lower prices as
competitive pressures grow.

However, as there are few restrictions on entry in the hotel
industry such a market skimming policy may have only limited relevance
for hotels unless a prime site or other unique characteristic permits
this.

An approach such as that suggested by Oxenfeldt, where he
recommends that the high skimming price and low penetration price should be regarded as the maximum and minimum price levels and a realistic price selected between these two extremes is a much more practical and safe policy for the average new hotel unit.

The new unit's philosophy will undoubtedly be influenced by the source of demand. There are three possible ways that this may arise:

(i) Unsatisfied demand: existing units in the area may have inadequate capacity to satisfy the high level of consumer demand and so the new unit may aim at reducing the gap between supply and demand;

(ii) Displacement demand: existing units may be unable or unwilling to provide the sort of facilities required and the new unit may be designed to capture these dissatisfied customers;

or (iii) Created demand: new demand patterns may be created in a previously unexploited geographical area.

The identification of which source is relevant to the particular unit will decide the pricing policy pursued. Category one gives little room for freedom in pricing; in two the policy adopted will depend on the facilities offered and the degree of differentiation; in three the possibility of using market penetration or market skimming will be realistic alternatives.

Pricing will however for any new unit be an important competitive tool and the use of aggressive price policies will be much more likely to bring success in this type of situation. It is however worth stressing that pricing decisions are implicitly made when feasibility studies are undertaken regarding the location of a new unit. The type of philosophy towards pricing policy for a new unit will therefore be made well in advance of opening and after the initial planning stages changes will only be possible within fairly narrow limits.
(d) Package Tours

The attitude of a unit towards the 'package' trade will depend on numerous factors, the most important of which are location, size, projected image and occupancy levels. In some cases such trade will be avoided at all costs, in others it will be recognised as the only way to ensure adequate profitability.

Whatever particular reason makes package business desirable it is essential from the outset of negotiations to recognise that the wholesaler or industrial buyer will be much better informed than the normal individual consumer. He will be capable of assessing qualitative features; he will be aware of competitor's offerings and the supply relative to demand situation in the area and so there will be a much greater emphasis on price.

Bidding techniques are occasionally used but normal practice is a bargaining process between the two parties. Negotiating skill is therefore essential and Oxenfeldt has suggested that in any negotiations, negotiators should "develop ruses that lead their 'adversary' to disclose the strength of his desire to conclude the transaction". This of course is a two way process and the eventual outcome will depend on relative strengths, and the relative desire or need to reach an agreement.

Variable cost is the floor below which price should not fall: the difference between revenue and variable costs represents the contribution to overheads and profit. Additional revenue received in Bars (or restaurants if relevant) should also be taken into account.

There are considerable advantages in using package business to boost occupancy. The discounts given are confidential and may be varied from group to group: this discrimination is possible because of the market segmentation and if used on the basis of varying demand elasticities can enhance profitability of the unit considerably.
Another advantage is that the administrative problems and inconvenience of changing price lists etc. is avoided.

One disadvantage is that price needs to be fixed well in advance; fifteen months is not unusual. Care therefore needs to be taken, in inflationary circumstances, not to pare the margins too low. In some cases built in allowances for high inflation rates may be made at the time of agreement.

Regular bookings of package tours means that the uncertainty regarding occupancy levels is much reduced; this means production and control are much easier to plan in advance.

The need for expenditure on other forms of promotion activity, e.g. advertising, is also reduced.

These financial advantages need to be carefully taken into account when price concessions are made in order to secure group bookings.

Discounts given to certain groups or large firms require the same sort of analysis and approach as above. The basic distinction between whether they are 'the bread' or merely 'the jam' will decide the extent of the discount allowed.
(e) **Conferences**

As we saw in Chapter II conferences are becoming an increasing important source of business for hotels in the U.K. and because of the substantial advantages they bring the competition to secure conference business has become quite fierce.

An important difference between conference and other hotel accommodation demand is that the rigid location requirements do not hold. Flexibility of location means that there is greater emphasis on the other competitive variables.

It would probably be true to say that for most conferences the quality and quantity of the facilities available are the most relevant factors in choosing a hotel or area. Suitable exhibition rooms, committee rooms, secretarial facilities, visual aids, etc. are prerequisites but if more than one hotel can offer satisfactory facilities then the choice will be decided on price. Bidding procedures may be adopted although direct bargaining predominates.

In some industries bidding for contracts involves firms in costly and time consuming preparations. But in hotels, providing variable cost figures and expected occupancy levels for the relevant times are already available the bid will be relatively painless and will depend on management's assessments of the need to obtain business. In industries where information regarding all bids received is made public, firms can assess the probability of a successful bid on the basis of past experience and the level of the bid made, but in the hotel industry where such information is not obtainable the selection of bids to maximise expected profits has to be replaced by judgment on behalf of the individual responsible taking into account all the variables involved.

Fifty per cent of all conferences last 3-4 days (1), the inter-

national average being 6-7 days, so, in just the same way as package
tours create extra demand in Bars, so too will conferences. This
additional source of revenue must be taken into account.

If hotels are competing with each other for the conference, price
competition is obviously going to occur. However if a conference is
going to be held in a certain town and the accommodation to be provided
by numerous hotels then reduced prices are rarely necessary unless
demand is considerably less than the supply available.

(g) Special Functions and Promotions

The same approach is required here as for the previous two
sections. The initial approach will depend on whether excess capacity
exists and the opportunities available for ensuring fuller utilization.

The reply will determine the price policy to be adopted and will
obviously depend on the sort of special promotion under consideration.

Some examples:

Musical of Gourmet weekends: Emphasis on facilities and special
attractions, i.e. non-price variables. Prices probably set so that contribution
is fairly high yet still possibly below normal rates. This will ultimately
depend on the demand elasticity.

Winter weekend breaks: Use of off-season spare capacity -
emphasis on price for complete 'all-in' weekend. Contribution to overheads
usually low but positive. New customers
can be attracted to use hotel facilities
and may become regular customers of the
future.
Pensioners' Holidays: Use of off-season spare capacity - emphasis on price to attract price conscious pensioners who can holiday outside main holiday periods. Publicity may be obtained fairly cheaply by circulating O.A.P. clubs. Competitive market price essential.

Price thresholds of consumers need to be allowed for. Price as a status symbol may be relevant for some units. Price discrimination may be used to reflect varying demand elasticities in the market and if necessary to shift demand into off peak periods.

Dinner-Dances:
4. IMPLEMENTATION OF THE DECISION

With the most appropriate policy to meet the given objectives now decided upon it only remains for the unit to ensure that the policy is implemented as effectively as possible.

For the small unit, locally controlled, there will be few problems. The large group will require administrative controls and checks to see that if the decisions were centrally made they will be implemented and fully appreciated by the local or branch manager.
5. REAPPRAISAL OF THE OUTCOME

Hague stresses in his book 'Pricing in Business' that "Pricing must be a continuous feedback process" (1) and that the decision once taken must not be ignored.

It is essential that the price setters should ensure that information is collected regarding the actual results of their decisions. These can then be compared with the intended or expected results. Variations will need to be examined and reasons sought for the discrepancies. This re-appraisal process will enable the price setters to 'learn' from their past performances whether their assumptions regarding the interrelationships of the numerous variables were correct. It will also help them to improve their ability to deal with the dynamic conditions that exist in the real world.

![Diagram of Analysis of Performance]

- **Satisfactory**
  - Continuation of present pricing procedures and policies

- **Unsatisfactory**
  - Search for explanation
    - Objectives unrealistic
      - Respecified in operational terms and in light of external environment
    - Inappropriate procedures and policies
      - Reassessment of alternatives available i.e. price and marketing quality of service
      - Modified existing procedures
      - Selection of new options

Figure 4.3. A Framework for Reappraisal

The characteristics of the Hotel Industry are such that marketing should be given a dominant role in the management function. The marketing mix chosen for each individual hotel unit will necessarily vary according to the sector in which it operates and will reflect the image it wishes to project.

Location, as we have previously stressed, is often the key to success or failure. Its role as a relevant marketing variable however is fixed once the investment decision has been made and if an active marketing policy is required attention will have to be concentrated on other marketing variables. Price is the only marketing variable that generates income; other marketing variables incur and alter costs. Too often an appraisal of the role of price as a competitive device and variable is only undertaken when a firm finds itself in trouble and at this stage it is too late.

In other service and manufacturing industries the role of price as a potential competitive device has been more fully explored, utilized and exploited than the hotel industry. There is no evidence to suggest that the hotel industry in general is a special case where normal and accepted marketing approaches do not apply; in fact the under-utilization of capacity at the present time suggests the reverse. The industry however is extremely traditional in outlook and apart from some sectors who have adapted to changed circumstances there is an apparent reluctance to use aggressive marketing techniques. In far too many cases price is treated as a financial decision rather than being viewed in its marketing dimension. Price decisions are therefore often approached from a cost rather than a market-orientated basis. The role of price as a communicative device and psychological weapon has not been appreciated. This view was confirmed by the answers given in
the survey undertaken and reported in Chapter III.

There are notable exceptions (as recorded in Chapter III) and those units and/or groups who have appreciated the potential of price competition and combined it successfully with their marketing strategy have recorded an impressive rise in profitability relative to other units in the industry. Off-season promotions emphasising price are a classic example of the use of price to tempt first time customers into the industry as well as encouraging established customers to use facilities more often. Hotels in the future if they are to survive, and certainly if they wish to prosper, will have to compete not merely with each other, but with other industries for the discretionary element of consumer spending. These industries are so much more advanced, using sophisticated marketing techniques to attract customers that it is essential that the industry as a whole must undertake a co-ordinated effort to 'pull in' new customers. It is in this area that the role of price as a competitive device must be seriously investigated and implemented where necessary.

There are of course areas within the industry as has been indicated in the previous chapter where price cannot play an active role and has to remain a passive variable. Even so the pricing decision must be carefully integrated with the other marketing variables.

If the role of price as a competitive variable is to be fully exploited by the industry certain changes in outlook will be necessary.

Accountants will have to provide the relevant cost information from which optimal price decisions can be made. The historic absorption approach will need to be replaced by a variable cost-contribution type analysis. The allocation of overheads both between departments and on a seasonal basis will have to be questioned and given meticulous attention if the procedure is to be retained.

Marketing managers will need to conduct further research into
consumer attitudes and needs. The information search should concentrate on building up an intimate knowledge of the type, tastes and requirements of consumers. Consumers' reaction and sensitivity to price, their awareness of price levels, the range and extent of price thresholds, the impact of including price in advertisements, are a few of the identifiable areas where further research and analysis can be done. This thesis has attempted to identify some of the general relationships but for actual decision-making specific information appertaining to individual units will be essential. In small owner-managed units much of this information is already available because of the personal involvement of the owner-manager with customers. It needs however to be fully utilized and exploited if successful marketing strategies are to be employed. Many large units however will have to devote resources into the collection, collation and analysis of such information if their performance is to be improved.

Small independent units though possessing an intimate knowledge of consumer characteristics and preferences will however have to ensure that they equip themselves with the necessary technical expertise if they wish to make effective price and marketing decisions. In many cases this may be feasible by joining a marketing consortium who will provide the necessary specialist advice. Those who decide to go it alone will have to make a conscious effort to educate and equip themselves with the necessary expertise.

For the industry as a whole objectives will have to be made more operational and pricing objectives will need to be clearly identified. The units which decide that price competition is not relevant to their marketing needs will still need to give pricing the status it deserves as a revenue generator. The units that decide to use price as a competitive device will have to ensure that the approach to pricing remains flexible, adaptable, and is frequently re-appraised in the
light of dynamic market conditions.

It is hoped that this thesis which has attempted to integrate the approach of marketeers, economists and management accountants, will have gone some way in identifying the problems involved in pricing decisions, and to providing a logical framework to aid and guide decision makers in this service industry who face such tantalising, yet fascinating, pricing problems. A framework however cannot eliminate the need for experience and flair.

In the face of uncertainty and risk it is the ability to appreciate the complex inter-dependency of variables that will determine the effectiveness of price decisions. Judgment will therefore continue to play a major role and though pricing should be approached in a scientific style for success it will require a sophisticated blend of technical expertise, intuition, and flair, but above all - judgment.
The reasons for conducting an independent interview-type survey can be summarised under the following two headings.

I. The inadequacy of published information in giving any indication as to the processes by which actual pricing decisions are made in the industry made the collection of new information imperative.

II. A postal survey though it would theoretically have had a larger coverage might well have provided an inadequate return both qualitatively and quantitatively because of the type of information required. An initial trial run of a few large firms confirmed this.

For these reasons an interview-type approach was adopted. Theoretically this approach can adopt three alternative forms:

(a) A formalised interview where specific pre-determined questions are asked in a set order;

(b) A non-directed free interview where the respondent is allowed to talk freely;

and (c) A combination of (a) and (b) where standardized questions are covered at some point in the interview but not necessarily in a predetermined form and where prompting and probing is allowed if necessary.

The form selected was the latter because it permitted the degree of flexibility that in fact proved so essential to ascertain the philosophical approaches towards price decisions in the Hotel Industry. This is vitally important if complex attitudinal questions are being asked. Also unlike postal questionnaires one can ensure that the questions are answered by the intended respondent - in this case the person responsible for pricing decisions. The major disadvantage was that the procedure was slow and very time consuming. Only on a few
occasions was it possible to undertake more than one interview a day. Such a procedure does however require that the interviewer is alert to the possibility of personal bias and the questions therefore have to be carefully worded so that the respondent is not influenced in his reply. A merit of this approach, which counteracts to a certain extent the above drawback (and which is not feasible in a postal survey) is that differently worded check questions may be used during the interview to ensure that questions answered are a true reflection of the respondent's behaviour or attitude.

For this reason careful attention was paid to the selection and wording of questions. Advice was taken from numerous sources and a 'pilot' trial run taken which confirmed that the first part of the interview was to be devoted to a free non-directed talk by the interviewee, followed by questions covering the essential points. Slight adjustments in wording obviously had to be made for the individual proprietor and the large group. The procedure adopted was that for groups where necessary questions were repeated for each type of hotel owned according to locational quality characteristics (and if deemed necessary size).

Interviews for small units usually took approximately 45-60 minutes; for groups, especially those with a wide variety of hotels, it was invariably considerably longer. If pricing decisions were a group or committee decision, then attempts were made to contact all those responsible so that the various angles could be covered. This often involved more than one interview, e.g. the marketeer, the accountant and for some groups individual units' managers. Some of these supplementary interviews were conducted by telephone because of the pressure of time and financial constraints. All interviews were undertaken between June and December 1974.

A copy of the questionnaire is given. For interviewing purposes
the questions were spread out with large spaces to record answers. The questions in brackets are prompt questions that were used if the initial question was not understood, misinterpreted or where individual circumstances necessitated changes.

Brief outlines of answers were recorded only during the interview, a more detailed account was written up immediately afterwards. If the respondent seemed to be inhibited by the recording of his observations, then notes were not taken but recorded subsequently.

A sample questionnaire and some actual completed forms are included.

The sample was chosen on the basis of ownership, size, locational and qualitative differentials. An outline structure was taken from the N.E.D.O. Survey 'Hotel Prospects to the 1980's'. Within these categories willingness to co-operate became a crucial factor.

Initial contact was made by letter, setting out the purpose of the inquiry etc. The larger groups were tackled first and in the beginning individual type-written letters were used. Initial response however was poor. In fact out of the first ten letters only two replies were received - both negative. Personal handwritten letters were then used, with an attempt to include in each letter an individual reference to the group concerned. These had a much higher success rate. For the refusals however a tenacious follow-up procedure was used to ensure that those selected were eventually interviewed. For this purpose personal recommendations by mutual friends and acquaintances was also extremely useful.

In the end all but one of the large groups initially selected were interviewed. Apart from two groups who made a great deal of their information regarding costs, discounts, occupancy, etc. available there was a marked reluctance on behalf of this category to divulge
The small private Hoteliers were those however who generated the greatest problems in terms of initial reluctance to co-operate. A persistent rumour, in the Oxford area, that I was from the tax office, seemed to move in advance of my requests. This meant that similar units had to be found elsewhere so resulted in the small units taking up a disproportionate amount of time and energy. However, of those that did co-operate most were extremely generous with their time and information, often allowing free access to their accounts and occupancy tables, etc. over the years so that the dynamic effects could be explored.

The eventual number of hotels covered, including those group controlled, amounts to 506 units and 67,231 Beds representing approximately 14.7% of estimated number of Hotel Beds. 30 hotels were interviewed in depth; total interviews were 46.

Constraints of time and travelling expenses meant that most of the interviews were conducted in the south of England. However, a few units in both Scotland and Wales were also covered. It could be argued that this might well bias the results; however it is pointed out that the Head Offices of most of the large groups are in or near London, and that this mitigates against the above bias because national coverage has been obtained though travelling was limited.

The units covered have been ranked according to the number of beds for which the interviewee was responsible.

**Category one** includes units controlling 8-24 beds. 80% of these were privately owned and managed. The remainder had various forms of ownership, e.g. brewery leased, but were essentially individual proprietors. 60% were located in towns; 20% in country; 20% seaside. 20% had three star rating; the remainder falling in the 1-2 star category.
Category two includes units controlling 25-199 beds. All were single units. The form of ownership was almost exactly equally distributed between individuals, private and public companies. 25% were country hotels; 47% seaside; 38% in towns. 40% had a 3/4 star rating, 60% a 2 star.

Category three includes miscellaneous units of 200 -1999 beds. This category consisted of mainly 4 and 5 star units and all were situated in urban areas.

Category four includes groups responsible for 2000+ beds. The smallest group had six hotels. All were public companies except for one nationalised concern. Most of the groups owned large units, many of 200+ beds. The star rating included a few two and five star units but most were in the 3/4 star category.

A great deal of the information collected was highly confidential (e.g. occupancy and discounts) and only given in exchange for a firm promise that the anonymity of the respondents would be guaranteed. For this reason the descriptions and reports in the text are of a very general nature but have of necessity to be so disguised so that they cannot be attributed to the respondents who so willingly co-operated. Some of the replies in the specimen questionnaire sheets have also for this reason been deleted.
1. HOW DO YOU APPROACH PRICING DECISIONS?
   (Where do you start?)
   (What information do you use?)

2. Is your pricing influenced mainly by a) Operating costs?
   b) Competitors prices?
   c) What the market will bear?

3. Do you operate BACKWARD PRICING?
   (i.e. calculating what extras you can provide within a given price).

4. How price CONSCIOUS is the average customer who uses your hotel?
   A B C D E

5. For your firm/group to what extent is price taken by customers to
   be an indication of QUALITY?
   Does this affect your pricing strategy?
6. How much notice do you take of the prices charged by your competitors?
Do you price above, below or equal to them?

7. Do you reduce your room rates in the off season (or for weekends)?
If not, why not? If so what determines the size of the price reductions?
How successful have these been in attracting customers?

8. (a) Do you give price discounts?
(b) If so, to what sort of customer?
(c) How much?
(d) Do you have the authority/courage to tell me the discounts given?

9. If you increased your prices by 10% what do you think would happen to occupancy?
If you decreased your prices by 10% what do you think would happen to occupancy?
If you increased your prices by 20% what do you think would happen to occupancy?
If you decreased your prices by 20% what do you think would happen to occupancy?

10. What are the objectives of your firm?
(Maximum profits?)
(Minimum level of profits?)
(Return on capital?)
(Occupancy?)
(Other?)
11. How do you attract customers to your hotel?

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

13. Can price compensate for poor location?
1. HOW DO YOU APPROACH PRICING DECISIONS?
   (Where do you start?)
   (What information do you use?)
   "Minimum charge as recommended by local Hotel and Guest Houses Association, All-in-Bed, breakfast charge."

2. Is your pricing influenced mainly by a) Operating costs
   Check made that overheads are covered by suggested price.
   b) Competitors prices
   c) What the market will bear
   "This usually so"

3. Do you operate BACKWARD PRICING?
   (i.e. calculating what extras you can provide within a given price).
   NO

4. How price CONSCIOUS is the average customer who uses your hotel?
   A   B   C   D   E

5. For your firm/group to what extent is price taken by customers to be an indication of QUALITY?
   Does this affect your pricing strategy?
   "Customers are suspect if price below 'normal'"
6. How much notice do you take of the prices charged by your competitors?

Do you price above, below or equal to them? Slightly below or equal, below achieved by not charging regulars for extras - hence repeat custom assured.

7. Do you reduce your room rates in the off season (or for weekends)? No

If not, why not? If so what determines the size of the price reductions? Demand not seasonal.

How successful have these been in attracting customers?

8. (a) Do you give price discounts? 'Not as a regular practice'.

(b) If so, to what sort of customer? Sometimes 'hard-up' cases.

(c) How much? Varies - not more than 15%.

(d) Do you have the authority/courage to tell me the discounts given?

9. If you increased your prices by 15% what do you think would happen to occupancy? If all members of HGHM moved up - nothing.

If you decreased your prices by 10% what do you think would happen to occupancy? I wouldn't go below HGHM recommended price.

If you increased your prices by 20% what do you think would happen to occupancy? As above for 15%.

If you decreased your prices by 20% what do you think would happen to occupancy? As above.

10. What are the objectives of your firm? 'Way of life' - 'meeting people'.

(Maximum profits?)

(Minimum level of profits?)

(Return on capital?)

(Occupancy?)

(Covering of costs) 'Good holiday every year'.

(Other?)
11. How do you attract customers to your hotel?

- Local institution main source
- Combined with listing in local tourist and H.G.A. lists.

12. To what extent do you think price can be used as a marketing device for your hotel/in your industry?

- Don't know.

13. Can price compensate for poor location?

- Don't know.
1. HOW DO YOU APPROACH PRICING DECISIONS?
(Where do you start?) Initially survey of competitors - then
(What information do you use?) a comparative evaluation of
service and location differentials.
Question then asked 'will the market permit us to
charge these prices.'

Food = 'more care oriented than accommodation
but still competitors carefully watched'.

2. Is your pricing influenced mainly by a) Operating costs
b) Competitors prices ✓
c) What the market will bear ✓

3. Do you operate BACKWARD PRICING? Yes.
(i.e. calculating what extras you can provide within a given price).
Inflation in the last 18 months has forced us to cut
some elements of service and menu content to permit
adequate profit margin.

4. How price CONSCIOUS is the average customer who uses your hotel?

A B C D E
Tourist  Businessman

5. For your firm/group to what extent is price taken by customers to
be an indication of QUALITY? Until recently: consumer's sensitivity
to price had not increased.

Does this affect your pricing strategy?
At present tourists in particular are now looking at
and asking about price before booking.
Therefore "price has to right".
6. How much notice do you take of the prices charged by your competitors?
   Do you price above, below or equal to them? ♦ On a par allowing for service differential

7. Do you reduce your room rates in the off season (or for weekends)?
   Yes.
   If not, why not? If so what determines the size of the price reductions? 0% approx. off normal price.
   How successful have these been in attracting customers? Very. Occasionally fully booked in autumn/spring when normally quiet. Been in winter proves attractive.

8. (a) Do you offer price discounts? Yes
     (b) If so, to what sort of customer? Regular customers only
     (c) How much? Nominal 5-10%
     (d) Do you have the authority/courage to tell me the discounts given?

9. If you increased your prices by 10% what do you think would happen to occupancy? Nothing.
    If you decreased your prices by 10% what do you think would happen to occupancy? Nothing.
    If you increased your prices by 20% what do you think would happen to occupancy? Slight fall maybe
    If you decreased your prices by 20% what do you think would happen to occupancy? Regular trade - nothing
     Special offers or functions maybe increase but slight.

10. What are the objectives of your firm?
     (Maximum profits?)
     (Minimum level of profits?)
     (Return on capital?): Satisficing
     (Occupancy?): Quality of life
     (Other?): Hedge against inflation
11. How do you attract customers to your hotel?

- Interchange member.
- Regular customers.
- Many Americans from personal recommendations.

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

Yes - providing discounts are substantial.

13. Can price compensate for poor location?

- Not relevant to this hotel.
- For industry probably yes if skilfully used.

Special functions - Cost plus procedure used.

Conference - fairly small - price quoted related to 'need' for extra business and depends on bargaining power, facilities required, etc. "Very lucrative sector."
1. HOW DO YOU APPROACH PRICING DECISIONS?
(Where do you start?)
(What information do you use?)
Accommodation - nearly all inclusive weekly basis.
Room charges varied according to size, furnishing and view. Sea views with balcony - premium charge reassessed each year to allow for inflation.
Food = Cost x 4.

2. Is your pricing influenced mainly by a) Operating costs  ✓
   b) Competitors prices x "Never"
   c) What the market will bear

3. Do you operate BACKWARD PRICING?  NO.
   (i.e. calculating what extras you can provide within a given price).
   Not relevant to this type of Hotel.

4. How price CONSCIOUS is the average customer who uses your hotel?
   A B C D E

5. For your firm/group to what extent is price taken by customers to be an indication of QUALITY?  Yes, it is taken as an indication.
   Does this affect your pricing strategy?
   Tempting to exploit this and charge more.
6. How much notice do you take of the prices charged by your competitors? Do you price above, below or equal to them? 

"Take no notice at all"

7. Do you reduce your room rates in the off season (or for weekends)? No. If not, why not? If so what determines the size of the price reductions? How successful have these been in attracting customers?

We would lose money if open in winter. We close down. "The electricity is too expensive."

8. (a) Do you give price discounts? Never. 
(b) If so, to what sort of customer? 
(c) How much? 
(d) Do you have the authority/courage to tell me the discounts given? Would attract the wrong sort of person.

9. If you increased your prices by 10% what do you think would happen to occupancy? Don't know. 
If you decreased your prices by 10% what do you think would happen to occupancy? Don't know. 
If you increased your prices by 20% what do you think would happen to occupancy? Don't know. 
If you decreased your prices by 20% what do you think would happen to occupancy? Don't know.

10. What are the objectives of your firm? (Maximum profits?) Property = inflation hedge. (Minimum level of profits?) (Return on capital?) (Occupancy?) (Other?)
11. How do you attract customers to your hotel?

Rely on advertising in local tourist guides.
Also 30% customer regular annual visitors

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

Does not influence people's choice.

13. Can price compensate for poor location?

Has to be less if location poor.

[NB. Occupancy apart from limited peak season no where near 100%]
1. **How do you approach pricing decisions?**
   (Where do you start?)
   (What information do you use?)
   
   Service element of prime importance.
   Cost plus guide line but what the market will take main criterion.
   Food = Gross Profit of 62% only. Room margin above most xxxxxx
   Liquor = 65-60% margin.

2. Is your pricing influenced mainly by
   a) Operating costs
   b) Competitors prices
   c) What the market will bear ✓

3. Do you operate backward pricing? **No**
   (i.e., calculating what extras you can provide within a given price).
   Totally unsuitable for 5 star hotel.

4. How price conscious is the average customer who uses your hotel?
   
   A B C D E
   'Money no object to most of customers'.

5. For your firm/group to what extent is price taken by customers to be an indication of QUALITY? **Very much so**.
   Does this affect your pricing strategy?
   Yes. We therefore price high.
6. How much notice do you take of the prices charged by your competitors? Check that we are at worse equal. Do you price above, below or equal to them? But preferably above.

7. Do you reduce your room rates in the off season (or for weekends)? No. If not, why not? If so what determines the size of the price reductions? How successful have these been in attracting customers? Not relevant - no real off season.

8. (a) Do you give price discounts? No. All private bookings.
(b) If so, to what sort of customer? X
(c) How much? X
(d) Do you have the authority/courage to tell me the discounts given? X

9. If you increased your prices by 10%, what do you think would happen to occupancy? Nothing.
If you decreased your prices by 10%, what do you think would happen to occupancy? Nothing.
If you increased your prices by 20%, what do you think would happen to occupancy? Nothing.
If you decreased your prices by 20%, what do you think would happen to occupancy? Nothing.

10. What are the objectives of your firm? Long term profitability (Maximum profits?)
(Minimum level of profits?)
(Return on capital?)
(Occupancy?)
(Other?)
11. How do you attract customers to your hotel?

'Service'
'High Quality Staff'
'Reputation'

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

Must be kept high otherwise image would suffer.

13. Can price compensate for poor location?

Not relevant to this hotel but maybe in other...
1. HOW DO YOU APPROACH PRICING DECISIONS? Separate treatment for
   (Where do you start?)
   (What information do you use?)
   Accommodation - procedure different for new and established units.
   New units - designed at cheapest possible level so unobtrusive
   possible to appeal to businessmen requiring standardized
   accommodation.
   Existing units - price kept still if performance satisfactory.
   Repurchased only if unsatisfactory - by location - prices not
   can be.
   Food - break even requirement only.
   Liquor - competitive followed.
   Value for money main theme.
   Prices decided by representatives annually on committee basis.

2. Is your pricing influenced mainly by a) Operating costs ✓
   b) Competitors prices ✓
   c) What the market will bear

3. Do you operate BACKWARD PRICING? Yes.
   (i.e., calculating what extras you can provide within a given price).
   Entirely a backward pricing exercise from
   drawing board stage.

4. How price CONSCIOUS is the average customer who uses your hotel?
   A  B  C  D  E

5. For your firm/group to what extent is price taken by customers to
   be an indication of QUALITY? Not for this category.
   Does this affect your pricing strategy?
   Deliberately try to price below market level
   but quality of product standardized.
6. How much notice do you take of the prices charged by your competitors?
   Do you price above, below or equal to them?
   
   This feasible because of cost controls.

7. Do you reduce your room rates in the off season (or for weekends)? Yes.
   If not, why not? If so what determines the size of the price reductions?
   £1 per head margin required
   How successful have these been in attracting customers?
   
   Moderately.
   
   Site mainly business centres.

8. (a) Do you give price discounts? Yes.
     (b) If so, to what sort of customer? Business men.
     (c) How much? Small as rate already competitive.
     (d) Do you have the authority/courage to tell me the discounts given? 10% approx.

9. If you increased your prices by 10% what do you think would happen to occupancy? Nothing.
    If you decreased your prices by 10% what do you think would happen to occupancy? Occupancy good. No need to contemplate.
    If you increased your prices by 20% what do you think would happen to occupancy? Drop.
    If you decreased your prices by 20% what do you think would happen to occupancy? Increased demand.

10. That are the objectives of your firm?
    (Maximum profits?)
    (Minimum level of profits?)
    (Return on capital?) ✓ 15% on Capital (Other?)
    (Occupancy?) Also property inflation hedge
11. How do you attract customers to your hotel?

Businessman aware of by sales network.

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

Price and location / varies according to type of hotel / equally important.

13. Can price compensate for poor location?

No if location very bad.

eg. Some of our hotels never attract any weekend bookings even though prices have been dropped almost to variable cost.

Conferences: facilities and service rather too limited. Main emphasis given to regular room accommodation sales to business...

Special functions: very minor role.
1. HOW DO YOU APPROACH PRICING DECISIONS? Profit objective set for each unit. 
(Where do you start?) This based on estimated capital employed - or lease payments required. Targets however adjusted by 'ability to pay'. Group charges units 10% of revenue receive cost-volume relationships calculated - yet recognition that procedure arbitrary - recent shift from cost orientation towards 'what market could take'.
(What information do you use?) Food - % Cost of dishes + labour + fixed cash element (20% Scrap 10%).
Mark-up decided on sales mix basis and outcome similar to gross % profit mark-up - advocated easier to operate at unit level.
Accountants large influence on price determination. 
Managers very limited influence.

2. Is your pricing influenced mainly by a) Operating costs ✓ 
   b) Competitors prices ✓
   c) What the market will bear - more relevant recently

3. Do you operate BACKWARD PRICING? Yes for new hotels.
   (i.e. calculating what extras you can provide within a given price).
   Brief to architect to design with a price in mind.

4. How price CONSCIOUS is the average customer who uses your hotel?
   A B C D E
   Businessmen

5. For your firm/group to what extent is price taken by customers to be an indication of QUALITY? In Restaurants and for functions in XXX hotels yes.
   Does this affect your pricing strategy? XXX not so much.

Exclusiveness is what customers are willing to pay for.
6. How much notice do you take of the prices charged by your competitors? Varies from hotel to hotel 
Do you price above, below or equal to them?

7. Do you reduce your room rates in the off season (or for weekends)? No. If not, why not? If so, what determines the size of the price reductions? Prefer to be half empty at normal prices than full at low prices. How successful have these been in attracting customers?

No variable costing procedures available.

Maybe next year this will be attempted.

8. (a) Do you give price discounts? Yes.
(b) If so, to what sort of customer? Groups, businessmen.
(c) How much? Nominal.
(d) Do you have the authority/courage to tell me the discounts given? 8-20% on normal prices.

This is not as much as some London competitors are giving but we would prefer 'weather out the storm'.

9. If you increased your prices by 10% what do you think would happen to occupancy? Very little.
If you decreased your prices by 10% what do you think would happen to occupancy? Very little.
If you increased your prices by 20% what do you think would happen to occupancy? Drop maybe.
If you decreased your prices by 20% what do you think would happen to occupancy? 'Bad image' may cancel.

10. What are the objectives of your firm? Growth and expansion.
(Maximum profits?)
(Minimum level of profits?) Chief
(Return on capital?) Chief
(Other?)
11. How do you attract customers to your hotel?

"No real marketing plan"

Some experimental market research just begun on service required/location etc.

12. To what extent do you think price can be used as a marketing device for your hotel in your industry?

Feasible  

All-in Price should prove useful in future

13. Can price compensate for poor location?

Not relevant to groups!

Conferences → facilities emphasised

Bargaining powers and strategy determine eventual price

Special functions → "What the market will bear"


Dean, Joel. 'Managerial Economics', Prentice-Hall, 1951.


Devletoglou, Nicos B. 'Consumer Behaviour – An Experiment in Analytical Economics'.


