

Ankle Biter Syndrome

By Rick Swig

Full service hotels everywhere are being molested by ankle biters. These ferocious pests stem from the current wave of new hotel development. The pests? These are a combination of limited service products from the mid-priced quality of Marriott Courtyard and Hilton Garden to the economy extended stay units of Extended Stay America or Homestead Village.

These lodging units have sprouted up willy nilly on affordable land parcels on the peripheries of major cities to serve the urban sprawl of the commercial enterprise and meet the demands of the individual business traveler. While the suburban markets have clearly been impacted, metropolitan areas as far flung as Phoenix, Dallas, Denver, Salt Lake City, and Atlanta have also felt the bite.

Why pests? Although allegedly not directly competitive with full service products, they have begun to bite away pieces of full service market share with considerable price/value benefits. Here are brand new products competing against aging full service hotels (mostly at best nearing a decade old).

The new hotels have taken advantage of new technology with better telephone switches, larger televisions, improved HVAC plants, plus in most cases irons, ironing boards, high quality am/fm clock radios, and even hair dryers. As mileage programs have expanded to include the hotels for business travelers, differentiation is even further lessened. Sure mattress, linen, and guest room size may be lower quality, and there is no room service. but what about that free breakfast?

For developers these hotels are cheaper to build and require little creativity, as far as design and concept development. Furthermore, these hotels can be financed, as their revenue yields and expense margins support even conservative appraisals and income/debt coverage ratios.

These hotel products have arrived in the nick of time. Public companies from all segments are increasingly concerned for quarterly earnings and are starting blitz attacks on the spending habits of their road warriors with moratoriums on travel.

Fatigue stemming from the abundant increases in full service guestroom rates during

the last several years is apparent in travel managers everywhere. Supply in many areas has begun to neutralize demand, as it seems to have softened. Corporate guidelines are being drawn and many full service hotels are being quartered, as some of their staple customers are being quartered somewhere else due to more affordable incentives.

It's not that demand has become depressed, but rather is less dynamic than it was a year ago with national occupancy down slightly over 1% over the last twelve month period. Where hotel occupancies have been nearing capacity, that opportunity still exists but the achievement may be more difficult and will require the shifting of market mixes.

In 1998 and 1999 many full service hotels with advantages of meeting space shunned mid-week groups for the more lucrative Commercial transient segment. Now, these same hotels will have to diversify once again with a broadened market focus, as an offset to the impact of the ankle biters.

Repositioning means adjusting services and staff to different requirements of customer demands. Marketing plans will have to be redrawn. Some sales departments will have to be retrained to migrate from virtual order taking tactics back to an aggressive selling and servicing posture. This will have trickle down effects to other departments, including banquets and kitchen, to provide expanded services to broader market segments.

The full service segment will have to find more ways to differentiate itself from the ankle biter segment to stem the tide of migration and reduced market penetration. As the ankle biters have managed to throttle disparity through the display of the aforementioned guestroom featured bells and whistles, the full service products are now challenged to create renewed benefits in support of their positioning.

Not only are there product positioning issues, but there is also the challenge of pricing as well. As many hotels have reached their occupancy capacity, revenue growth has become contingent on average daily rate (ADR) growth. Ankle biter competition has also brought price/value based on lower ADR levels, which are more easily off set by limited service overheads. Full service hotels on the other hand are forced with generating even greater revenues to off set expenses.

Full service hotels have never been managed so efficiently. Technology and better productivity management have lowered employee counts and increased margins. There is little room to cut without compromising either product or service, which would be competitively self-defeating.

Competition for human resources, both hourly and salaried, is creating a supply and demand curve, which is not benefiting the full service hotel segment at a time when it may most need the help. Pressures from both minimum wage increases and the competition for experienced (or inexperienced for that matter) human resources is pressuring wages upwards, especially in locations with still booming economies.

The entire hotel segment will be faced with shrinking profit margins, as there is more ADR stabilization and higher costs of providing service. As full service hotels may now have to trend away from high revenue and high yield segments to branch out to lower rated and higher cost ones, there is risk of even greater profit margin reduction.

This scenario creates the opportunity for several trends. Wall Street will continue to be bearish on the hotel industry, as there are more reasons to project growth reduction that increase. Full service hotel development will continue to be difficult in markets vulnerable to ankle biters. Finally, as individual hotels try to create more revenue from the same capacity, there may be more pressure to increase rates and manage the balance between customer price resistance with potentially negative occupancy impacts and the ability to continue to grow REVPAR. Whatever the result, welcome to the new millennium and yet another era of challenging evolution.