CASE 1

The Airline Market

"I will give you my position in about a week," said Jean Valjean, general manager of Le Centre Hotel, and he put down the phone and looked at the letter before him. The letter was from SKS Airlines requesting a one-year contract for 40 rooms each night at $72 per night. The problem facing Jean was a simple one: Does he take SKS and fill the 40 rooms for 365 days at $72, or does he refuse the business so that he can sell the rooms some nights up to the full rack rate of $175? Last year the hotel had 95 percent occupancy or above for 135 nights; overall occupancy was 68 percent with an ADR of $108, but on near or sell-out nights the hotel could usually get rack rate on incremental room sales. This year was expected to be about the same.

Background of the Hotel

Le Centre Hotel was located in the downtown area of a Canadian city in Quebec. It was viewed as a four-star corporate/convention hotel. It had 800 rooms including the Towers—a prestigious five-story hotel within a hotel. The Towers had its own check-in facilities, lounge, and special amenities and contained 140 rooms including 16 suites. The balance of the hotel offered a choice of king, queen, and double beds with an additional 24 suites and six rooms especially equipped for the handicapped.

The hotel operated three restaurants. Le Mistral on the 37th floor offered gourmet French cuisine and an exceptional wine list. It had a seating capacity of 84. Le Shoppe on the third floor was open for breakfast, lunch, and dinner and had a seating capacity of 260. L'Expresso, a European style "express" restaurant on the promenade level was for people in a hurry. It had a seating capacity of 60. In addition to the restaurants the hotel had five lounges. Other features of the hotel included a five-story glassed-in atrium; glass-enclosed year-round pool; and health club with gymnasium, sauna, whirlpool, and massage. The hotel had a multilingual staff.

Competition

For airline crews, all hotels in the area were Le Centre's competitors because airlines historically chose hotels based on price and location, as long as they met a minimum level of comfort and services. SKS, however, preferred four-star hotels near shopping and entertainment facilities. This made competitive about 10 properties located in the downtown area, so the decision would be made based on price and service. Jean was well aware that a number of competitors had expressed interest in the SKS business. He was also aware that if he took the contract and satisfied the SKS crew, he would have more negotiating power when the contract came up for renewal next year when the room rate could be increased. In the hotel business, it was always easier to renew existing room contracts than to solicit new ones.

The Proposal

Le Centre's target market included all forms of corporate groups, professional associations, and conventions. The SKS proposal appeared to be a good opportunity for Le Centre because it guaranteed 40 rooms per night (two overseas flights a day) for the entire year plus potential clients from their flights. The contract, if accepted, would require the hotel to have clean rooms immediately upon check-in, and to control the crews' wake-up calls. These services were standard tasks for Le Centre. However, because of the late departure of aircraft toward Europe, checkout time for SKS would be between 4:00 and 6:00 P.M. while the inbound crews would be arriving sometime between 9:00 and 10:00 P.M. the same night. This meant the hotel had to have extra maids on duty to have these rooms ready within two to four hours. In addition, when flight schedules were changed, this meant changes in wake-up calls. This extra service posed a problem during the summer months when the hotel was full of regular guests; the staff was reluctant to provide extra service to the crews at the expense of the other guests who were paying the full rack rate.

Experience with other airlines had shown that airline crews spend less money in the hotel than other guests during their stay, an average of about $15 each on food only. This was because their usual stay was only one night. If they had leisure time, such as if they were grounded for additional days, they preferred to explore the city; hence, food and beverage purchases were largely made outside the hotel.

Sales and Cost Data

Jean knew he would have to work fast on this proposal. He called in his assistant, Colette Chabot, and asked her to collect all the data required to estimate the comparative revenue and costs that would be involved to make a decision whether to accept the SKS offer.

Colette began with an analysis of room statistics for the previous year. These showed that, if the proposal had been in place, the number of regular guest rooms that would have been lost was equivalent to 105 nights sold out and 30 nights at an average of 97 percent occupancy. Analysis of the food and beverage statistics, not including banquets, for the previous year showed food revenue of $33 per occupied room and average beverage revenue of $22.50. The hotel's standard cost percentages were 36 percent for food and 32 percent for beverages. In analyzing the probable effect on

This case was originally prepared by Professor W. M. Braithwaite, University of Guelph. It has been revised and disguised for use here, with permission. All figures are in Canadian dollars. For conversion purposes, one Canadian dollar equaled about 0.80 US dollar at the time of the case.

operating costs, Colette found that on about 150 nights the SKS contract would require the equivalent of one additional front desk clerk for eight hours at an average hourly rate of $12.20. Fringe benefits were calculated at 35 percent of all payroll costs. In addition to this cost, Colette estimated the following variable costs per occupied room.

Housekeeping: one half hour per room at $10.60 per hour for the evening shift (part-time maids were available at this rate)

Laundry and linen: $1.25 per occupied room

Utilities: $1.50 per occupied room

Amenities: $2.50 per occupied room

Colette turned this information over to Jean for final analysis and a decision. As Jean sat in his office contemplating this information, he was reminded of a discussion at a recent meeting of general managers of all Le Centre hotels when they were told that one of the company's objectives for the coming fiscal year was a 12 percent return on investment. He was also very aware of the serious cash flow problem facing his hotel at that time. For the last fiscal year cash flow was negative by more than $2 million. With a $50 million long-term mortgage at floating rate interest and $4.2 million in annual municipal taxes to pay, the SKS business promised a steady and certain cash flow every week.