

Finding Optimal Room Rate for Sustainable Tourism

By Dr. Aurora Dawn Reinke, ISHC, ISSP-SA

Posted to Travindy on 27-Nov-2017 <https://www.travindy.com/2017/11/finding-optimal-room-rate-sustainable-tourism/>

The Journal of Hospitality Marketing & Management recently [published a theoretical model for the relationship between room rate and sustainability](#).¹ The study, which focuses on top line impact of sustainability, accounts for demand, price sensitivity, sustainability effort and costs, sustainability willingness to pay and demand, variable and fixed hotel costs. The authors determined factors that affect optimal room rate.

The negative factors were general price sensitivity, lower willingness to pay for sustainability, and the cost sustainability. Probably not surprising. We already know that higher price sensitivity tends to relate to lower room rates. This study shows higher price elasticity related to less investment in sustainability, which is more likely to occur in economy and budget hotels than in the luxury or midscale markets.

The three positive factors were:

- Hotel capacity, or primary demand. Large hotels not only have higher capacity but also the staff and financial means to implement, maintain, and grow sustainability. This relates to the *effort* factor.
- Customers' sensitivity to sustainability. Recognition and preference for certain activities and features results in willingness to pay a premium.
- Type of demand. Hotels with a blend of leisure and business customers, based on events and seasonal draw are more likely to see positive relationship between room rate and sustainability.

There is also a positive feedback loop effect: More investment in sustainability improves ability to implement (*effort*) and increases demand and willingness to pay. This leads to greater ability to invest. At a certain point however, there is a point of diminishing return, but improved efficiency in integrating sustainability results in costs savings that enable the hotel to hold prices at an optimal level, increasing demand and allowing for more sustainability.

Takeaway for Owners

Sustainability programs tend to be set at a corporate level within companies that own or manage a diverse set of properties, and one size does not fit all. Many owners have a mixed portfolio that includes a range of property sizes, market conditions (demand generators, competitors, etc.), brands, and star levels. Executives can use this research to create a sustainability strategy that accounts for these differences.

For example, there may be a subset of hotels that get minimal sustainability upgrades with sufficient cost savings to maintain or lower room rates. Another subset of properties will have a more integrated and intensive approach to sustainability because the macro and micro conditions produce the positive feedback

¹ Xu, X., Xiao, G., & Gursoy, D. (2017). Maximizing profits through optimal pricing and sustainability strategies: A joint optimization approach. *Journal of Hospitality Marketing & Management*, 26(4), 395–415. <https://doi.org/10.1080/19368623.2017.1245168>

loop presented above. Executives deeply committed to sustainability may even choose to require properties in their portfolio support an ongoing, profitable investment in environmental and social initiatives.

Similarly, revenue managers need to account for such factors. Using industry and past performance data, they can create what-if scenarios to optimize prices based on the input they already use, plus sustainability as an influencing factor.

Drawbacks

There are two downsides to point out. One relates to results of the study; the other relates to the methodology.

First, for economy and budget hotels, the revenue argument is not strong. We need research and tools that demonstrate the ROI in terms of employee retention and performance, and costs savings (many of which are well documented, and others in need of more research and data). The news is not all bad for sustainability advocates in this category; it just means using different models and approaches to make the business case.

Second, a weakness of the study is that “sustainability effort” is both complex and vague. The idea is that as a hotel gets more adept at executing sustainability efforts, the effectiveness and efficiency improve. But putting numbers or a rating to this can be complicated. Financial decision makers may need to do some research and data gathering to determine “effort level.” Furthermore, the authors recognize that sustainability could be broken down into social and environmental. Other studies show willingness to pay is higher for some sustainability efforts than others.

Calling All Math Geeks

If you’re a numbers-oriented person and not afraid of a scary looking equation, I recommend you read the [full article](#) and test the theory using your own data. I would love to hear about both the results and the experience of gathering the data and calculating your optimal room rate.