

Opinions

What's the ideal mix of OTA business for your property?

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Experts explain an EBITDA impact model that looks at changes in OTA and non-OTA production.



By Trevor Stuart-Hill and William Carroll

The groundswell of support for “book direct” initiatives is squarely aimed at reducing reliance on online-travel-agency production. Blindly following a course of action to simply reduce OTA transaction mix by an arbitrary percentage may not yield the best financial results. In fact, earnings before interest, taxes, depreciation and amortization may be negatively impacted by arbitrarily lowering the OTA transaction mix.

A highly simplistic and misleading calculation of EBITDA impact supporting “book direct” campaigns relies on the reduction of OTA room nights to be replaced by non-OTA production. The calculation is often based solely on exchanging OTA merchant margin expense with direct-to-property costs through the mix change without regard to the marketing (search) value of OTA display positioning.

While certainly possible, non-OTA production replacement will undoubtedly require additional sales-and-marketing expenses to maintain occupancy. While the simplistic approach to executing an OTA-to-direct booking mix may reflect a significant increase in EBITDA, realities regarding expense and risk are often marginalized. Even if a property is successful in achieving a transaction mix change, there is some EBITDA-neutral upper threshold that should be considered before execution to include the likely changes in sales and marketing expenses associated with the mix change.

A property wanting to improve EBITDA through a shift of channel mix should take a more analytical approach. For this purpose, we have created an EBITDA impact model* that accommodates varying shifts in OTA and non-OTA production. For illustration purposes, it is based on a 200-room limited service property running at 70% occupancy with a \$100 average daily rate. It also factors the interplay between the billboard and dilution effects. The model can

be applied for different size properties, ADRs and transaction mixes.

The billboard effect refers to the concept that having a presence on OTA sites allows a property to remain in the consideration set for a given guest’s search and will have some positive impact on direct-to-property bookings. In other words, a potential guest may search online via OTA channels to see what options are available to them. Some of those guests will not book a reservation through an OTA, but will instead confirm a reservation directly with the property call center or website. There is ample published research to suggest that this effect exists, such as “The billboard effect: Online travel agent impact on non-OTA reservation volume” from the Cornell Center for Hospitality Research Report.

The dilution effect is a term we have coined to reflect the opposite of the billboard effect. It refers to the diversion of transactions from property-direct channels to an OTA as a result of an extensive presence on OTA channels. The interplay of billboard and dilution effects points to the need to anticipate the impact that changing channel mix will ultimately have on profitability for a particular property.

To illustrate the points above, consider the following table that illustrates the EBITDA impact on a property where different levels of dilution and billboard impacts apply.

ESTIMATED IMPACT ON REPLACEMENT (AND NON-REPLACEMENT) OF OTA ROOM NIGHTS ON EBITDA GIVEN MARKETING SPEND AND CHAIN COSTS

SCENARIO #	DESCRIPTION	TOTAL REVENUE	CRITDA	EBITDA	% OCCUPANCY	ADR	% OTA ROOM NIGHTS	ROOM NIGHTS TO BE MADE UP	REQUIRED % INCREASE IN NON-OTA ROOM NIGHTS	% INCREASE IN MARKETING SPEND REQUIRED	% INCREASE IN MARKETING SPEND REQUIRED	\$ EBITDA IMPROVEMENT (OVER BASE CASE)	% MARKETING INCREASE CEILING TO BE EBITDA NEUTRAL	% CHAIN COST INCREASE CEILING TO BE EBITDA NEUTRAL
BASE CASE (REDUCTION IN OTA ROOM NIGHTS) B=0.0, N=0.0														
1	BASE CASE	\$5,110,000	\$4,532,059	\$577,941	70%	\$100.00	30%							
DECREASE OTA ROOM NIGHTS BY 33% B=0.0, N=0.0														
2	REPLACEMENT	\$5,182,270	\$4,578,167	\$604,103	70%	\$101.41	20%	5,059	14.1%	10.3%	\$31,654	\$26,162	8.5%	5.1%
3	WO REPLACEMENT	\$4,054,699	\$4,093,503	\$561,196	63%	\$101.10	22%							
DECREASE OTA ROOM NIGHTS BY 33% B=0.25, N=0.3														
4	REPLACEMENT	\$5,182,270	\$4,575,057	\$606,613	70%	\$101.41	20%	4,817	13.9%	9.8%	\$30,144	\$27,672	9.0%	5.4%
5	WO REPLACEMENT	\$4,679,876	\$4,115,122	\$564,754	63%	\$101.12	22%							
DECREASE OTA ROOM NIGHTS BY 33% B=0.5, N=0.1														
6	REPLACEMENT	\$5,182,270	\$4,590,540	\$591,730	70%	\$101.41	20%	7,036	19.7%	14.6%	\$44,027	\$13,789	4.5%	2.7%
7	WO REPLACEMENT	\$4,688,483	\$3,916,431	\$532,052	60%	\$100.96	23%							
INCREASE OTA ROOM NIGHTS BY 33% B=0.0, N=0.0														
8	INCREASE IN OTA	\$5,565,301	\$4,070,615	\$594,686	77%	\$99.10	36%							

(Click on the chart to expand)

The table highlights a few important points:

1. When a property billboard effect is substantial and/or dilution effect is minimal, reducing the OTA contribution would require significantly more non-OTA room nights to be booked than otherwise anticipated (perhaps as much as 40%) if the billboard effect were not considered at all.
2. A major EBITDA loss risk exists if a substantial billboard effect exists relative to a dilution effect at a property and the reduction in OTA room nights isn’t replaced by non-OTA room nights. In this example, EBITDA loss is 8%.
3. In the case that the dilution effect is significant relative to the billboard effect for a given property, reduction in OTA production would require fewer non-OTA replacement room nights with a much higher EBITDA-neutral threshold for sales and marketing expenses.

Interestingly, when this model is applied to understand the impact of increasing OTA mix by 33% (See table above), ignoring any billboard or dilution effects, EBITDA could actually be increased

by just under 3%.

For branded properties, the analysis becomes a bit more complex. Direct and indirect costs associated with chain-level efforts to drive property-direct bookings need to be understood. Pricing discounts, servicing costs, campaign funding and resulting impact on EBITDA should be considered. Alternative uses for book-direct campaign funding may be more property specific in terms of opportunity cost and benefit, but nevertheless is a factor to consider.

A recent report from Kalibri Labs titled “Book direct campaigns: The costs and benefits of loyalty” looks at the revenue performance of OTA-to-direct mix change focused on loyalty programs and chains. While the report failed to consider billboard or dilution impacts, it based results on both the mix shift and the growth of loyalty membership to measure longer-term net revenue impacts. This approach also focused mix changes on potential mercenary versus loyal guests.

There can be an array of potential values for both the billboard and dilution effects for properties. These can vary based on quality, property classification, current and proposed channel mix, seasonality, OTA and property/brand marketing initiatives plus the competitive environment. The other challenge is that the magnitude of impact for a given metric is not linear, but likely to be more exponential in nature the further one moves from the neutral (zero) point. From a practical stand point, a property may have to test for these impacts or do sensitivity analysis by evaluating alternate impact effects on EBITDA with mix changes.

To do this, a property could begin tracking answers to these questions:

- How did a particular guest learn about the property?
- Has this guest stayed previously? If so, has their booking channel shifted over time or remained the same? If not, how did they book and why?
- Is there a surge or drop in direct bookings based on OTA campaigns or sort-order placement? How does that compare to booking activity via the OTAs during the same period of time?

While it may be tempting to simply decry OTA contribution in favor of property-direct bookings, that approach could negatively impact profitability for a property. Billboard and dilution factors should be thoroughly considered prior to taking action.

*This model was developed and presented at the Cornell Center for Hospitality Research Summit, October 2017. Contact Trevor Stuart-Hill trevor@revenue matters.com for more information about the model and the presentation.

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