From RevPAR to TRevPAR – How profitable is your Hotel?

Things are becoming more complex within Hotel Revenue Management. Learn about the evolution of Revpar and increase your revenue with Customer Alliance!

Origin of RevPAR

A hotel is like a living organism. In the rapidly changing market of hospitality industry, supply and demand can totally change, top to bottom, from one day to another. Hotel Revenue Management has therefore grown in complexity during the past decades.
So, let's take a look at the three major Key Performance Indicators used to measure the economic success of a hotel.

- **Average Daily Rate (ADR):** Average daily income per occupied room
- **Occupancy:** All occupied rental units of a hotel at a given time (measured in %).

In the past, many hotels either defined high occupancy rates or heavy room rates as their primary business goal to achieve. By doing this, however, they often ignored important aspects of their business performance.

This is why some years ago, Hotel Revenue Management introduced a new concept.

- **RevPAR:** Arguably the most important figure to look at when calculating an accommodations' financial performance. It provides relevant information about the REVenue Per Available Room, putting in relation the hotel's daily room rates with its occupancy.

### Examples for RevPAR calculation

Generally, there are two ways of calculating a hotel's RevPAR. The classic approach is multiplying the Average Daily Rate (ADR) with the occupancy.

$$\text{ADR} \times \text{Occupancy}$$

Alternately, the same result can be arrived at by calculating the following:

$$\frac{\text{Total Room Revenue in a Given Period}}{\text{Number of Available Rooms in Same Period}}$$

**So let’s do the math:**

For our case, we take a hotel with **100** rooms of which **60** rooms are sold for a given day, generating a total revenue of **4200€**.
By dividing the Total Revenue by the Number of rooms sold \((4200 \div 60)\), we get the value of \(70€\) as the Average Daily Rate.

Meanwhile, we find a 60% Occupancy rate (60/100 rooms occupied).

So, taking either the first calculation formula \((70€ \times 0.6)\), or the second \((4200€ \div 100)\), we arrive at a RevPAR result of \(42€\).

**Limitations of RevPAR**

Within current Hotel Revenue Management, RevPAR is believed to be the most accurate figure that can be looked at to calculate a hotel's performance. It is also used to compare hotels' economic performances.

However, if you take a closer look, there are some limitations to its relevance.

Let's take a look at two simple cases:

**A Hotel with 50 rooms in total**
- sells 50 rooms for 20€ each.
- sells 5 rooms for 200€ each.

In both cases, the hotel generates a revenue of \(1000€\) while maintaining a RevPAR of 20€.

So, if RevPAR remains the same right here, does that mean that the hotel will have the same **net operating income (NOI)** in both cases?

No! Unfortunately, traditional RevPAR calculations do not take into account things like **costs per occupied room** or **additional revenue per room** for each individual room that is sold.

*As a result, RevPar still isn't the perfect indicator of a hotel's financial success.*
Evolution of RevPAR

Because of this, successful Revenue Managers such as Ira Vouk – Vice President and Co-founder of iRates – have introduced the concept of Adjusted Revenue Per Available Room (ARPAR), also referred to as Total Revenue per available Room (TRevPAR).

Let’s take close a closer look at both concepts:

**TRevPAR** looks at the total revenue of the property. Consequently, it will include all consumer consumption (at the bar, from room service, breakfast, etc.). In short, it sums up all revenue factors generated by a hotel taking a meaningful look in it’s profitability.

\[
TRevPAR = \frac{\text{Total Revenue}}{\text{Number of available rooms}}
\]

Unfortunately, **TRevPAR** does not emphasize the importance of prices and quantities sold, does not consider cost factors and does not take into account the occupancy rate, where these numbers are required to fully understand the hotel's efficiency.

On the contrary, The **ARPAR** formula as used by Ira Vouk “is a clear reflection of the bottom line profit”. There are different ways of doing the relevant calculations, and the formula is expandable. However, in this article we want to emphasise that **RevPAR** alone is no longer significant enough to get the whole picture.

This is why we stick to Ira’s simplest formula to calculate ARPAR:

\[
ARPAR = (\text{ADR} - \text{Variable costs per occupied room} + \text{Additional Revenue per occupied room}) \times \text{Occupancy}
\]

Let’s go back and apply this formula to our hotel example:
A Hotel with 50 rooms in total

- sells 50 rooms for 20€ each.
- sells 5 rooms for 200€ each.

As we’ll recall, RevPAR came out to 20€ for both cases.
What about ARPAR?

In our scenario, we assume

- Variable costs per occupied room = 10€

and

- Additional Revenue per occupied room = 5€

Case 1:

\[(20€ - 10€ + 5€) \times 1 = 15€\]

Case 2:

\[(200€ - 10€ + 5€) \times 0,1 = 19,5€\]

In this case, we therefore find that Case 2 is the more profitable one for the hotel. Of course, this is only an example. The results of an ARPAR calculation will vary depending on the variable costs per occupied room and additional revenue per occupied room, which are themselves likely to be different for each hotel. Besides that, commission rates and the amount of direct bookings respectively will significantly influence a hotel's NOI.

*Calculate your ARPAR now!*
Final Words

According to findings from Robert Mandelbaum, Director of the Office of Research Information Services (ORIS), a low inflationary environment is projected for the near future. This means that any increases, both in occupancy and ADR, will drive up ARPAR in 2015 and 2016. “The resulting strong increases in revenue, combined with tempered growth in operating expenses, will result in double-digit gains in NOI for the next two years.”

In conclusion, things have become more complex within the field of Hotel Revenue Management. Hoteliers should be aware of many factors when measuring the performance of their property. At the same time, increasing complexity offers the opportunity to obtain a strong lead over competitors.

Get this lead with the help of Customer Alliance! We can take your hotel to the next level. Ask us about it in a >> Free Demo

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Further reading

- Ira Vouk (Things you didn’t know about RevPAR).