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MKT-700-X4076 Marketing Capstone 23TW4

3-1 Milestone Two: Financial Analysis and Pricing Structure (Artifact 2)

TRU by Hilton

Professor White

May 7, 2023

I. Financial Analysis

Financial background:

The hotel and hospitality industry are one of business and pleasure. It goes hand in hand with the travel industry. People will always need to travel for business. However, in the past few years, during the pandemic, travel was severely limited. Now, that things have begun to return to normal, recreational (vacation) travel has begun to pick up and business travel bans are slowly being lifted which are both good news for the hotel industry. As further proof of leisure travel booming, a hospitality survey at the end of the year in 2022 found that 89% of those surveyed planned one vacation that year and 24% had 3 or more planned, (De Peuter-Rutten, n.d.).

Currently, for the first time since pre-pandemic times, revenue per available room (RevPAR) recovery is exceeding expectations. However, labor shortages are creating challenges for hotels to run at full power. To meet these challenges, hotels are adjusting amenities they offer, increasing their reliance on technology and outsourcing.

According to IBIS World, in 2022, "the market share size, measured by revenue, of the hotels industry was 224.9bn. The market size of the hotels and motels industry increased by 20% in that same year," (IBISWorld - Industry Market Research, Reports, and Statistics, n.d.).

According to IBIS World, the main factor currently affecting growth of the hotel industry on the United States is inbound travel by non-U.S. residents and a "medium-low growth risk score." The biggest opportunity for growth for the U.S. hotel industry is consumer spending. When consumers have more disposable income to spend, they travel more. When they don't have the disposable income, they spend less on travel. In fact, it's probably one of the first things to go. Consumer spending is expected to increase in 2023, therefore creating a growth opportunity for the hotel industry," (IBISWorld - Industry Market Research, Reports, and Statistics, n.d.).

Financial Analysis Proposal: TRU by Hilton

According to Stories by Hilton, for the third quarter in 2022 net income was $346 million, exceeding the high end of guidance. Adjusted EBITDA was $732 million, exceeding the high end of guidance. System-wide comparable RevPAR increased 29.9 percent, on a currency neutral basis, compared to the same period in 2021, (Geheren, 2022).

Key Data Financial Analysis

Economic conditions:

Forecast: According to Hilton, "full year 2023 net unit growth is expected to be between 5.0 percent and 5.5 percent. Full year 2023 system-wide RevPAR is expected to increase between 4 percent and 8 percent on a comparable and currency neutral basis compared to 2022; full year net income is projected to be between $1,382 million and $1,454 million; full year Adjusted EBITDA is projected to be between $2,800 million and $2,900 million. Full year 2023 capital return is projected to be between $1.7 billion and $2.1 billion," (Hilton, 2023).

The Hotel Market

Forecast: Growth

In 2020, due to the pandemic, the hotel industry was nearly on the brink of collapse. In 2023, thanks to the resilience, ingenuity, and ability to pivot of hotel chains across the U.S., hotels are poised to enter a new era in the way they operate. However, even with their adaptability hotels still face challenges such as staffing shortages and economic factors including inflation and borrowing costs will replace COVID as top concerns.

According to the AHLA, the U.S. hotel industry is projected to achieve a promising 1.3 billion occupied room nights in 2023, slightly exceeding 2019's total. The current projection is a 56.9% improvement over 2020's low of 831.64 million occupied room nights during the pandemic. From 2021 to 2022, U.S. hotel demand improved by 11.1%. Occupancy is slowly but surely heading toward full recovery. (AHLA, 2023)

In 2022, it was anticipated that it would be an uneven and volatile year for hotel recovery. At the start of the year, concerns of new CoVid variants and potential outbreaks caused a decrease in travel demand, especially with the postponement of the return of conferences and conventions of group business. During that same time, supply chain issues and staffing shortages threatened to disrupt hotel operations and service levels. During all these challenges with remote work common place, a rise of bleisure (business and leisure) travelers and digital nomads (remote workers who used their flexibility in location to explore new destinations) saw a huge shift in consumer attitudes and behaviors. This caused 2022 to become known as the year of the “new” traveler.

U.S. hotels met the challenge and catered to these new travelers evolving travel preferences and in doing so the hotel industry almost recovered to pre-pandemic numbers.

Product Life: Changing

There are four distinct stages in a product's life cycle. These stages include introduction, growth, maturity, and decline. A brand usually incurs higher marketing costs when introducing a new product to the market but also experiences higher sales as that product is accepted and adopted by consumers. (Kopp, 2023)

The typical hotel life cycle occurs over a 7-to-10-year basis. Money becomes available to lend, new hotels are constructed then, occupancy levels inevitably decline as these new hotels are

absorbed into the market, (Buchanan, 2017). TRU by Hilton will try to increase longevity by evolving to meet and exceed the Gen Z consumer's wants and needs. Gen Z is still young so over the next decade, these consumers will be getting married and having children so their needs may change. TRU by Hilton plans to evolve with Gen Z.

Pricing Strategy:

TRU by Hilton uses value-based pricing while keeping in mind it's competitor's pricing. Value based pricing is based on the fact that products and services can only cost as much as consumers are willing to pay for that product or service. TRU offers maximum value for a minimum price by taking into consideration what its target demographic is looking for in a hotel and then providing that at a budget-friendly price.

Value-based pricing takes into consideration these three things:

1. How much consumers are willing to pay for a hotel room.
2. Customers are willing to pay more for a room if they appreciate the benefits that the hotel provides therefor raising the perceived value.
3. What other similar hotels are charging will influence how valuable travel consumers perceive a hotel to be.

Value-based pricing works great for TRU by Hilton because their target demographic are Millennials and Gen Z who not only appreciate a great deal but value the minimal but meaningful vibe of TRU. According to Forbes, "Tru by Hilton is designed to appeal to younger, tech-minded, design-savvy travelers on a budget, with rates about $90 to $100 per night," (Bender, 2016). Pricing should not need to increase, as the product is not new and already priced

very reasonable to appeal to Millennials. The product is already in existence, we are only pivoting in the direction of the target demographic.

The forecasted prices for products have been created as follows:

When Hilton introduced TRU by Hilton, it was already focused on appealing to Millennials. This is why the brand chose to bring all the next-generation hospitality trends to one cost-effective platform. In 2016, at the inception of TRU, Hilton was already focused on luring the youngest travelers into their Hilton HHonors program, (Oates, 2016). Normally, high end hotels see less than 1% growth in occupancy and less than 5% growth in revenue per available room. However, midscale chains average roughly a 2% growth in occupancy and a substantial more than 6% growth in revenue per available room.

Competitive Pricing:

Room rates run on average $90-$100 making them more cost effective and budget friendly to young travelers than their competitors. For reference:

La Quinta in Chicago, IL for 2 guests today, prices can range from $104- $269 per night.

Fairfield Inn in Chicago, IL for 2 guests today, prices can range from $200 - $320 per night.

Comfort Inn in Chicago, IL for 2 guests today, prices can range from $ 97- $127 per night.

Pricing Formula:

One reason a hotel like TRU didn't exist at the midscale price point before it's 2016 creation is because these hotels are often created by more upscale brands who can't afford the maintenance of these budget friendly midscale properties and those properties got downgraded to economy chains. TRU avoided this situation by making sure these properties were cheaper to build and maintain. According to Mashable, "The typical hotel will have 98 rooms and sit on 1.5 acres of

land. It will cost $84,000 a room to build, excluding land. Compare that to Hilton's Hampton Inn brand: Those typically have 130 rooms, sit on 2 acres, and cost $110,000 a room to build," (Plautz, 2021). According to Hilton CEO Chris Nassetta, Hilton knows that the target demographic is young travelers, but the goal is to, "Get them loyal to our system and trade up as they move on in their lives."

If it costs $84,000 a room to build and there are typically 98 rooms in each TRU property, it costs $8,232,000 to build each property. Each room will need to generate a minimum of $84,000 a year (an average of $230 a night) in sales to breakeven in that first year. However, as each room costs $90- $100 per night to rent, at $90 per night, in one night, a fully booked TRU property can earn $8,820 which means in one year that TRU property could earn $3,219,300. At $100 a night, those same 98 rooms can earn a whopping $3,577,000 a year. Breakeven for build at $90 a night would be 2.6 years. At $100 a night, breakeven wouldn't be covered for 2.3 years. If the lifecycle is 10 years for a hotel, most earnings after that initial 2.5 years would be profit.

International Pricing Strategy:

Currently, TRU by Hilton only has properties in the United States and Canada with plans to expand into the Caribbean and Latin America, with a new regional prototype and hotel developments in Brazil, Costa Rica, Dominican Republic, Mexico and Puerto Rico. To price internationally, TRU will have to take into consideration the disposable income and average income of the locals, as well as the culture and people's attitudes towards hotel stays and current rates of other competing brands in those locations. It will also be critical to be sure that stay prices are converted to the local currency using the current exchange rates. For example:

Mexico: 1 USD = 17.40 pesos

Dominican Republic: 1 USD = 54.60 pesos

Brazil: 1 USD = 4.96 Brazilian real

Ethical and Legal Considerations with Localized Pricing Strategies:

Localized pricing strategies is legal and effective in driving sales. It doesn't make sense to treat all regions the same because each geographical location (especially international locations) has different cultures, priorities, economic situation, costs of living and exchange rates. To do business internationally, you must consider each country as an independent market because it is. Pricing cannot be a one size fits all situation. Pricing in the U.S. may not be feasible in a developing country, nor would it cost the same to produce and maintain the property and all of that needs to be considered.

Pricing Discounts and Promotions

Discount pricing should be implemented for bookings after 4 pm the day of stay, to sell the rooms and fill the property with lowest prices happening after 8 pm on the day of the stay. Promotional rates are usually offered during times of low occupancy periods (off season) to all guests to promote occupancy. There are other pricing promotions like early bird rates, stay for more days and pay less per night. To entice consumers these special rates may also added incentives and amenities such as free Wi-Fi, free breakfast buffet, free tea and coffee, etc.

Additional Costs: Upgrades

At TRU by Hilton, there are no hidden costs. The only additional cost a consumer might incur is purchasing items from the market in the lobby. There is normally not a charge for parking, Wi-Fi or a resort fee and if there is this can be offset by becoming a Hilton rewards member (which is free).

Channels of Distribution

Options for channels of distribution for TRU by Hilton include the typical hotel industry methods including a mix of direct web channels (i.e., the hotel's website, phone, email, Live chat or Messaging services), indirect channels (i.e., online travel agents), Global distribution systems (i.e., a network allowing travel agents to access hotel inventories and sell rooms to their clients) and wholesalers.

I. TRU by Hilton Budget

Future Expendatures & Capital Investments:

Estimate of Costs to Establish the Franchise

Estimated initial investment TRU by Hilton Hotel (98 rooms)

Type of Expenditure	Amount	Method of Payment	When Due	To Whom Payment Is To Be Made
Franchise Application Fee (Note 1)	$75,000	Lump sum	With Franchise Application	Us

Type of Expenditure	Amount	Method of Payment	When Due	To Whom Payment Is To Be Made
Product Improvement Plan (Note 2)	$0 to $7,500	Lump Sum	Before we prepare PIP	Us
Market Study (Note 3)	Varies	As arranged	As arranged	Supplier
Environmental Assessment (Note 4)	Varies	As arranged	As arranged	Supplier
Real Property (Note 5)	Varies	As Arranged	As Arranged	Seller
Construction and Leasehold Improvements (Note 6)	$4,860,000 to $7,200,000	As Arranged	As Arranged	Contractors
Designer And Engineering Fees	$135,000 to $360,000	As Arranged	As Arranged	Suppliers
Furniture, Fixtures and Equipment (Note 7)	$900,000 to $1,800,000	As Arranged	Before Opening	Approved Suppliers
Inventory and Operating Equipment (Note 8)	$90,000 to $180,000	As Arranged	Before Opening	Suppliers
Signage (Note 9)	$15,300 to $67,500	As Arranged	Before Opening	Suppliers
Computer Hardware and Software (Note 10)	$45,720 to $107,700	As Arranged	45 days before opening	Affiliate or Supplier
Guest Internet Access Program (Note 10)	$60,500 to $75,500	As Arranged	45 days before opening	Affiliate or Supplier
Delphi Sales and Events System (Note 10)	$2,500 to $15,000	As Arranged	As Incurred	Supplier
Required Pre-Opening Training (Note 11)	$7,500 to $17,500	As Arranged	As Incurred	Us and Suppliers
Accessibility Consultant Fee (Note 12)	$2,500 to $10,000	Lump Sum	On Request	Us or Supplier
Construction/ Renovation Extension Fees (Note 13)	$0 to $10,000	Lump Sum	When Requested	Us
Organizational Expense (Note 15)	$50,000 to $103,000	As Agreed	As Agreed	Suppliers
Permits and Licenses (Note 16)	$45,000 to $135,000	Lump Sum	As Arranged	Suppliers

Type of Expenditure	Amount	Method of Payment	When Due	To Whom Payment Is To Be Made
Miscellaneous Pre-Opening and Project Management Expenses (Note 17)	$90,000 to $270,000	As Arranged	As Arranged	Suppliers
Contingencies (Note 18)	$486,000 to $684,000	As Incurred	As Agreed	Suppliers
Additional Funds (Note 19)	$50,000 to $250,000	As Arranged	Before Opening	Suppliers
Other Required Pre-Opening Services Fees (Note 20)	$1,500	As incurred	Before Opening	Us
Total (Note 21)	**$6,916,520 to $11,436,700** THESE FIGURES DO NOT INCLUDE REAL ESTATE , MARKET STUDIES, INSURANCE, INTEREST OR SEPARATELY IDENTIFY THE COST OF IMPROVEMENTS UNDER A CONVERSION, RE-LICENSING OR CHANGE OF OWNERSHIP LICENSE.			

(Hilton Hotel, 2019)

Operating Budget (Monthly)

II. Annual Sales Revenue and Profit Forecasts:

Hilton projected that its annual profit forecast would increase after third-quarter earnings exceeded conservative estimates. This is due to travelers eager to hit the road again after slowly coming out of the pandemic. Americans are choosing to spend more money on travel despite rising costs and inflation. This is probably in part due to the surge of bleisure travel and remote work arrangements. Why work in your dreary home office when you can do the same work from Costa Rica? This will likey extend travel season beyond the typical times.

According to Hilton CEO Christopher Nassetta, "The third quarter marked an important milestone in our recovery as system-wide RevPAR exceeded the same period in 2019 for the first time since the pandemic began," (Nieto, 2022).

End of the year quarterly earnings for Hilton, showed that the net income for 2022 was somewhere between $1.22 to $1.24 billion, an increase from the prior projection of $1.15 billion to $1.22 billion.

According to Fox News, “Hilton also changed its earnings per share for 2022 to between $4.46 and $4.54 compared to its prior forecast of $4.21 and $4.46. Hilton's third-quarter profits rose by 44% at $1.31 per share, exceeding expert estimates of $1.24 per share,” (Nieto, 2022).

Sales Revenue Targets:

According to Hilton’s Q1 2023 Earning Release, “full year 2023 system-wide RevPAR is expected to increase between 8 percent and 11 percent on a comparable and currency neutral basis compared to 2022; full year net income is projected to be between $1,331 million and $1,385 million; full year Adjusted EBITDA is projected to be between $2,875 million and $2,950 million. Full year 2023 capital return is projected to be between $1.8 billion and $2.2 billion,” (Hilton, 2023).

According to Macrotrends, “Hilton Worldwide Holdings annual revenue for 2022 was $8.773B, a 51.57% increase from 2021. Hilton Worldwide Holdings annual revenue for 2021 was $5.788B, a 34.39% increase from 2020,” (*Hilton Worldwide Holdings Revenue 2011-2023 | HLT*, n.d.).

As the TRU by Hilton brand is already in existence and not a new product, we are just refocusing who the target demographic is there is no need to provide year 1, 2 and 3 target, profit or breakeven sales.

III. TRU by Hilton Market Share and ROI

According to CSI Market, Hilton achieved an ROI of 10.39 % in its first quarter of 2023, this is above Hilton's average return on investment of 7.97%. Hilton's investments during the 12 months ending in the first quarter of 2023 are valued at $12 billion. This is an improvement of ROI compared to 2022's fourth quarter.

Hilton's market share in the 12 months ending in Q1 of 2023 was 10.17%, (*Search for Shares, Industries, News and Economic Indicators - CSIMarket*, n.d.).

FEEDBACK: Alignment With Strategic Goals (MISSING)

Demonstrates alignment of proposed pricing structure to the company's strategic goals

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