full range of travel management services. They will find stiff competition among suppliers, OTAs and some new Internet portals specializing in this business. Even as the GDS volume has been relatively flat or declining temporarily (a phenomenon magnified by the recession and therefore will rebound somewhat with the economy), connections to the GDS are required by all hotel types that want to tap the travel agency market, and need to be handled by a reliable CRS vendor, whether they are direct or through a switch.

Any tools that streamline time and costs related to third party connections will be welcome, and each hotel organization has to choose between an investment in a direct connection and the best set of switch connection tools that can do this. Organizations like OpenTravel Alliance, an industry non-profit, works with the distribution vendors and the hotel companies to standardize the messaging between systems, usually written in XML, so that the connection between a hotel and any new website can be more efficiently built.

No doubt, over the upcoming few years, the industry will continue to rely on a blend of direct XML messaging along with different forms of switch connectivity depending on development and maintenance costs for each channel involved.

OFFLINE AND TRADITIONAL WHOLESALERS

For decades before the Internet emerged as a marketplace, the wholesalers and tour operators have contributed by offering business that is largely package-based (hotel plus air and/or car and/or ground transportation or other activities/attractions) and are most dominant in fly-to destinations such as Mexico, Hawaii, the Caribbean in the Americas and in Europe as well as Asia-Pacific in most markets.

Wholesalers bring a combination of group-driven and individual business. The individual purchasers, long known as FIT travelers, come in through "receptive tour operators" who make local arrangements. This business is inbound to a country, often from other countries where the traveler is not familiar enough with the destination to make their own plans directly. Receptive operators provide unique services in providing packages and destination itineraries that are more personal and include many elements that are currently not easily served through other channels.

Wholesalers bring a great source of inbound opportunities for the North American market and, a large and vibrant business, it is mostly fly-drive and primarily destination-based but often includes primary markets and destination markets close to attractions and national parks.

On the international inbound business to North America, in response to the current distribution dynamic, receptive operators are reinventing themselves to protect their market niche. Their distinct offering is in service—a valued commodity today and likely well into the future. Historically, wholesalers on the group side were able to control most of the airline seats for limited airlift destinations, with a lock on the charter flights. Therefore, they controlled the matching of seats to beds. This market has long operated with deep discounts that are opaque to the consumer since they are bundled into the packages. They often commit to blocks of rooms and due to paper-based or manual operations, hotels have not always had the benefit of real-time updating of the room blocks, which can make forecasting difficult. However, increasingly, there are automated solutions that have improved this situation with B2B portals or channel management tools to control the room blocks.

The advent of the OTA caused a major disruption to this market, but it still fills a unique niche that is not supported through other distribution partners. Much of the inbound international tour business comes through traditional wholesalers, as well as package business requiring payment handling, ground operations and other types of local coordination and support. The costs to hotels in terms of net rate discounts vary; the FIT tends to be a bit higher than the OTA rates, but on the group side, it is similar to that of the OTAs; the higher level of servicing is often the justification for a premium. It is unclear if more of this business will shift to the newer online-only rivals, particularly as they try to harness more of the international inbound demand from emerging markets from Brazil, Russia, India and China (BRIC countries), but after ten years of OTA penetration, the traditional players have managed to hang onto a portion of the business and, for the foreseeable future, are likely to retain their small but specialized slice of the hotel pie.

CALL CENTER, 800 NUMBER, VOICE RESERVATIONS AND PROPERTY DIRECT

This study has largely focused on electronic distribution and all the technology that drives it. However, the role of the voice or property direct channel is significant in hospitality. This *Distribution Channel Analysis* study defines the property direct channel as handling those reservations coming in either as walk-ins, groups/meetings, contract and any other type of business handled directly by the property. Nationally, in the United States, in 2010, this property direct component of the hotel business demand was over half (51.5%) and the demand coming through the voice channel (either to an offsite call center or to reservation agents in a hotel) was 13.2%. The revenue generated for the voice channel was disproportionately high providing over 17.2% of the revenue. While there are many options for handling these distribution channels, they are often one of the most overlooked in terms of potential for revenue growth. Not all hotel types are as affected by the voice-based business as others. A recent HSMAI Resort Best Practices benchmarking study[10] of independent resorts that are upscale or luxury, shows that almost two-thirds of all reservations are handled by the resort by phone or through property personnel.

What are the implications for these statistics? If a hotel can convert at a higher rate or gain ancillary revenue sales (in those hotels with ancillary revenue offerings), higher profit margins will result. A call center conversion rate in the 30% range would be respectable, and the average room rates tend to be among the highest through the voice channel reflecting a premium of 31% at $127.78 over the 2010 national hotel average daily rate (ADR) of $98.05. At those rates, even if the room night demand is only 15%-20%, increasing one point of conversion can yield hundreds of thousands of dollars in revenue in a year. (Refer to the Distribution Costs and Benefits chapter for more detail on this topic.) Does the call routing system have technology to direct calls to the best salesperson for the type of call? Do inquiries about the property get followed up with a systematic sales technique so that qualified prospects can be converted effectively? If not, then the property may have holes in its revenue net.

In terms of other property direct opportunities, well organized and systemically deployed sales activities conducted by front desk and other hotel personnel are tried-and-true because they work well. Hotel management would do well if it recognizes that the on-property staff controls almost half of the property's revenue. How well do these systems work? Some effective tools could be upsell mechanisms that are automated and embedded in a front office PMS system, along with manual processes that are utilized with every guest contact. Intelligence to inform the staff about who the guests are and predict what they may buy could yield considerable incremental revenue. How quickly the industry has forgotten the opportunity in the call center and property direct channels; it seems that if it is not online, few pay attention anymore.

These direct channels, even without the support of the latest technology, would be worth investing in some time and effort in terms of process improvements and may prove to be the "low hanging fruit" that can yield great results quickly.

GROUPS AND MEETINGS

Some of the challenges posed by online distribution include the growing use of electronic group and meetings lead sites.

Many websites have come and gone in an attempt to facilitate the group booking in an online environment. It seems that the complexity involved in dealing with meeting space, catering, group blocks, conditions such as cutoffs, negotiations for room upgrades, amenities, comps etc. has made it difficult for all but the simplest of meetings.

The dominant function that has remained in these attempts is the referral and RFP engine. Many sites serve as intermediaries for the exchange of RFPs with hotel bids. Of late, a recurring issue in hotel sales departments includes the number of RFPs that a meeting planner may send out and the staffing and time commitment required to properly address these requests. If the referral sites allow too many hotels to be included in the bidding process, then the chances

[10] HSMAI, *Resort Best Practices Initiative Benchmarking Study*, August 2011, Cindy Estis Green, www.hsmairesortbestpractices.com

for each to get the business are substantially lower; however, the time still has to be spent to respond. If the staffing does not adequately reply to the requests in a timely manner, then the hotel appears to be lacking in its sales responsiveness. This is a difficult situation that may require some refinement in the guidelines used by the lead referral sites that would benefit from collaboration between the parties involved.

Another pattern that has become more prominent in the group and meetings market is the use of third party intermediaries. Conferon, Helms-Briscoe, among others, have taken a central role in the booking for many of the U.S. industry meetings. Some of the brands are exploring new approaches to take advantage of the online connectivity that is becoming part and parcel of the group/meetings business ecosystem. For instance, Marriott and Cvent have recently announced an ambitious connectivity implementation using the Cvent RFP and sourcing tool. The industry will be watching closely to see if this initiative has a positive impact on Marriott's share of group business.

When so much of the business is booked through these third parties, what is the role of the hotel or regional salesperson? Are they primarily responding to third party inquiries, competing with their own third party vendors to find additional groups and meetings and/or just servicing business sourced through outside suppliers? If this is the case, does that change the staffing levels, skill sets, travel budgets or other expectations for a hotel sales team? This report has not quantified the full extent of third party bookings for groups and meetings, but it is a topic deserving further study since it has implications for the profitability of those hotels with a large percentage of property direct group and meetings business.

INDUSTRY PERSPECTIVE

Doug Carr

FAIRMONT RAFFLES HOTELS INTERNATIONAL
Executive Director Distribution

FAIRMONT RAFFLES HOTELS INTERNATIONAL

How long have you been in hotel industry? How long have you been involved with distribution issues?

>> After a number of years in the airline industry I joined the hotel industry in 1989 working at an independent hotel in the Toronto airport area. Got into corporate office environments for chains in 1991 and have been at the chain level of hotel management companies ever since.

In what way does your current role involve distribution?

>> Both operationally and opportunistically my role is involved with getting our rates, inventory and product information into the hands of consumers and strategic intermediaries in whichever manner that best facilitates success.

Where would you say distribution fits into the overall hotel management landscape? Why does distribution matter?

>> Without distribution most other areas of the hotel management disciplines would not be able to do their job because it's all about being part of the scenario by which a reservation is made. Accounting has no money to count if someone doesn't check-in. Housekeeping doesn't have rooms to clean unless someone checks in. Front desk isn't busy if guests aren't checking in. Outlets and conference floors aren't busy if guests are not checking in.

The only way the industry will have people "checking in" is to insure that the rates, inventory and product information finds its way into the hands of the people that will buy it.

What are the top 3 current issues that will have the greatest impact on hotel distribution in the next two – three years?

>> Being effective in the mobile space. Being effective in the social media space. Tone, manner and language of product information — the ability to speak to the point of purchase in a manner and language that is meaningful.

A consumer on leisure is different than on business. A leisure consumer attending a wedding is different than someone searching for a "green" hotel. A travel agent needs to see / hear things differently than a tour operator or a convention meeting planner.

What is the smartest move you have seen in hotel distribution (by someone other than your own organization)?

>> Offering up a variety of ways to see room and rate information during the selling process. Some consumers shop by offer and then want to see what rooms they'll buy based on price. Some consumers want to see the room choices first and then decide which offer is best for them. Having one site with the flexibility to show / cluster / group the rooms and offers in a manner that's meaningful to the purchaser is really quite engaging.

What is the smartest move your organization has made related to hotel distribution?

>> Partnering with a technology provider that can truly give us a holistic view of our customers, how they buy, when they buy combined with a technology platform that's flexible. It's not just about a property technology solution or a centrally technology solution or a CRM technology solution — it's about a single technology solution that handles all of those areas.

What is the single biggest oversight or misstep you have witnessed (in your own organization or others in hospitality) in the last two years?

>> Underestimating mobile and social media.

What three things can you tell a hotel general manager, owner or asset manager about distribution that would have the greatest impact on unit level profit?

1. It's not about the cost of the distribution — it's about the revenue gain by being in the distribution channel. Don't view it as 15% cost of distribution, view it as 85% revenue.
2. Understand the full cost of distribution, not just the transactional cost of distribution. Large reservation offices with armies of people are way more expensive in most global markets than connected / distributive technology.
3. Distribution is not just rate and inventory — never lose sight of product information and digital assets, that's distribution as well.

What is the next thing that you predict will disappear or gradually fade away that is currently a part of the distribution scene?

>> Fax and email threads that deliver reservation data. It's archaic and not timely. Missed revenue opportunities and very expensive to manage.

If you had a crystal ball, what emerging technologies do you anticipate could be game changers, or at least have the greatest affect on the distribution landscape in the next 2-3 years?

>> Location based services — from both perspectives: where I am "right now" to where I want to be based on the location I just searched for or clicked to on a map.

Melissa Maher

EXPEDIA, INC

Global Vice President, Strategic Accounts and Industry Relations

How long have you been in the hotel industry? How long have you been involved with distribution issues?

>> I have been in the hotel industry about 15 years and involved in distribution issues just over 10 years.

In what way does your current role involve distribution?

>> Expedia has a deep and comprehensive view into consumer behavior and market trends that we share daily with our hotel partners. Our focus is to help our partners achieve their goals by working alongside revenue, distribution and ecommerce teams to identify ways in which to best utilize our diverse portfolio of channels and brands.

Where would you say distribution fits into the overall hotel management landscape? Why does distribution matter?

>> Distribution is the key to getting guests into the hotel. More and more, it's tied inextricably to marketing and exposure, brand building and global visibility for properties. Done right, distribution can be a major driver of revenue growth and profitability.

Strategic distribution is about:

Attracting high-value guests.

Channel diversification: Working with multiple distribution channels to generate demand and grow rate.

Maximizing occupancy at optimal rate.

Reaching demand that meets the needs of your property.

Identifying distribution channels which will give your hotel global visibility and vast exposure.

What are the top 3 current issues that will have the greatest impact on hotel distribution in the next two to three years?

>> Significant shift (continued shift) of travel spend from offline to online worldwide.

Growth of middle class in emerging markets and proliferation of international travel among these consumers.

Emergence of mobile and tablets as leading platforms for accessing internet.

What is the smartest move you have seen in hotel distribution (by someone other than your own organization)?

>> Creation of loyalty programs for independent hotels, such as Stash rewards.

Unique distribution for independents through companies like Magnuson Hotels.

Vast improvement of brand.com UI's. The focus that the brands have put into ease of booking and intelligent technology has been an extremely smart move.

Dedicated employees at chains and individual hotels to manage social media outlets, including integrating reviews (like Accor did with Trip Advisor on their own site) as well as a heightened focus on monitoring and responding to guest comments. As consumer generated content continues to grow in importance, ensuring that there is an ongoing touch point with the consumer is critical.

What is the smartest move your organization has made related to hotel distribution?

>> Building a global team of market managers to work locally, in market with hotels at the property level and a world class strategy and analysis team to feed insights back to hotels about opportunities in their global distribution strategy.

Rapid development of mobile applications via the acquisition of Mobiata.

Asia focus. Joint venture with low cost carrier Air Asia, which makes it easier for consumers in SE Asia to purchase travel packages to international destinations. Our investment and commitment to growing Elong in China.

What is the single biggest oversight or misstep you have witnessed (in your own organization or others in hospitality) in the last two years?

>> Hotels utilizing 3rd party distribution channels only during off-peak times. Minimizing/eliminating demand during peak times may result in lower ADR.

Too much focus on RevPAR and not enough focus on the total cost of distribution channels.

Heighted focus and discussion about OTA's which generate less than 10% of overall hotel demand.

continued >>

Melissa Maher

EXPEDIA, INC

Global Vice President, Strategic Accounts and Industry Relations

What three things can you tell a hotel general manager, owner or asset manager about distribution that would have the greatest impact on unit level profit?

1. Plan (way) ahead for high compression and low compression dates. If hotels have a strategic plan and are more focused on specific need and non-need time periods they can better manage rates by booking window thus growing rate.
2. Use international targeting and opaque packages to secure base of inventory farther out, and then yield up rate closer in, rather than dropping rate as stay dates close in
3. Keep all distribution channels open to generate demand, thus grow rate; don't give away room upgrades — discount upgraded rooms to entice upgrades at time of booking

What is the next thing that you predict will disappear or gradually fade away that is currently a part of the distribution scene?

>> A consolidation of daily deal sites; we predict only a few will prevail.

If you had a crystal ball, what emerging technologies do you anticipate could be game changers, or at least have the greatest affect on the distribution landscape in the next two to three years?

>> Growth in mobile/tablet applications — the ability for consumers to plan and book travel anywhere, at anytime.

Convergence of social media, enriched content and personalized offers into the travel marketplace.

Size and Structure of the U.S. Hotel Industry by Distribution Channel

3

During the past decade, the way in which hotels and hotel companies offer their rooms for purchase to the buying public has changed dramatically. Changing along with those purchase patterns is the increased flexibility consumers now have not only to book their room purchase but to research and evaluate their prospective decision.

ALL U.S. HOTELS SUMMARY

Now, potential buyers can not only get a look at the property, evaluate its amenities, and other features, but they can also easily compare it to competitors for their business. In addition, price points, specials and the like are available for easy access. For a more detailed discussion on the current and emerging booking and marketing channels and how each works please refer to the Distribution Landscape chapter.

As booking channel mix has evolved over the past decade with the inception and increasingly wide use of the Internet, there has been very limited and largely anecdotal information available about how customers book hotel rooms and how this has changed over time. In the spring of 2011, a large consortium of industry organizations and owners embarked on an ambitious effort to collect, aggregate, and report on booking channel mix for the U.S. lodging industry. That effort resulted in data from 25,500 hotels reflecting the number of hotel rooms booked, the revenue and in most cases the number of reservations associated with those bookings by channel, by month from January 2009 through June 2011. The data providers submitted data for each of the following booking channels and vendors within each channel:

Channel	Examples
Brand.com	Marriott.com, Starwood.com, a hotel's own website
CRS/Voice	1-800-Hiltons, 1-800-ichotels, Trust
GDS	Sabre, Galileo, Amadeus, Worldspan
OTA	Expedia, Priceline, Orbitz, Travelocity
Property direct/other	Walk-in, group/rooming list, contract, Passkey, management rates

In an effort to make the analysis more complete for each of the OTAs, a breakdown by vendor and business model was provided. Basically there are three different types of arrangements/business models that vendors in the OTA space have with the hotel industry and they are highlighted below:

- **Merchant** – hotel receives net rate after intermediary is compensated based on negotiated percentage with the hotel. On average, the percentage of the room rate kept by the vendor varies from between 15% and 35%, depending on pre-negotiated deals and if the booking is room-only or part of a package that includes other services such as airfare or car rental. The rate is net of commission so the hotel does not pay a separate fee after the guest's departure, but "pre-pays" it when it offers the OTA a net rate.
- **Retail** – Intermediary is compensated on a commission basis based on a pre-negotiated percentage. The commission is paid by the hotels after the total room rate is sent to the property. This is very different than the other OTA models that operate more often on a revenue split.
- **Opaque** – bidding method, brand not disclosed to consumer until after sale, hotel gets pre-negotiated rate with vendor. Vendor keeps difference between what the guest pays and the pre-negotiated room rate. Typically the percentage of the room rate kept by the vendor is 30% to 50%. Exhibit 1 (see next page),

Booking Channel Mix Analysis Highlights

- In absolute terms, both bookings and the room revenue associated with those bookings grew in every channel in 2010; however, as a share of total demand the biggest growth was in Online Travel Agencies (OTAs) and Brand.com, while declines were reported in Central Reservation System/Voice (CRS/Voice) and Property Direct/Other.
- Wide average daily rate (ADR) variability exists by channel with the highest ADRs realized through CRS/Voice and Global Distribution Systems (GDSs) and with the lowest ADRs booked through the OTAs, especially the opaque model.
- Significant differences exist in booking patterns by chain scale category.
- By chain scale, relative consistency exists in the percentage of total demand booked by OTAs, unlike the other channels.
- OTA share of both bookings and room revenue has grown consistently throughout the decade.
- Economy chain hotels have dramatically increased their usage of the OTA channels in the past two years. They are now, by far, the chain scale segment with both the largest number of rooms booked through these channels and the share of total room nights that represents.
- The merchant model was the most widely used OTA model in both 2009 and 2010.
- The retail model is the fastest growing OTA model, but still the smallest in terms of room nights booked.
- The OTA opaque model is the lowest yielding booking channel.
- Brand.com represents more than 20% of bookings for the higher ADR chain scale categories.
- Study results indicate that there is a correlation between booking share movement between brand.com and the OTA channels. When there is an increase in one the other declines and vice-versa; the degree of this correlation is not yet possible to define since the study only examined 30 months of data.
- CRS/Voice is still a vibrant channel with more rooms booked there than by either the OTAs or GDSs.
- Rooms booked through the GDS channel grew in 2010 as transient business demand rebounded.
- The number of rooms booked through Property Direct/Other is by far the biggest channel; however, the share of rooms booked in this broadly defined channel has been declining for the past several years and we expect that trend to continue as electronic bookings grow.

The study includes detailed booking channel data from almost 24,000 U.S. hotels, in which there were 2.7 million rooms, making this by far the most comprehensive and definitive source of this type of information. All of the major hotel companies that operate in North America participated in this effort along with a large sample of management companies and ownership groups.

Exhibit 1 summarizes the key definitions used in this analysis:

Exhibit 1 Definitions

Channels	Brand.com, CRS/Voice, GDS, Property Direct/Other
Major OTAs	Booking.com, Expedia, Hotels.com, Hotwire, Priceline, Travelocity, Travelweb, Other OTAs
OTA Business Models	Merchant, Retail, Opaque

Data from the recently launched "flash sale" sites such as Groupon, Living Social, SniqueAway, and Jetsetter, were not clearly identifiable in many hotel data sets so they are not isolated in the study data. The actual bookings made through these venues were made through one of the other channels collected. (see Exhibit 2)

As can be seen from Exhibits 2 and 3, in 2010 the US lodging industry sold just over one billion hotel rooms generating $99.2 billion in room revenue. These numbers were up from 940 million rooms sold and $92.4 billion, respectively, in 2009. With that level of growth in both key measures, it is not surprising that both the number of rooms booked through each of the channels shown and the revenue associated with each channel increased in 2010. The largest growth in absolute demand was seen in rooms booked through OTAs and brand.com channels while smaller growth was seen in Voice/CRS and GDS. That general trend continued into the first half of 2011, (see Exhibits 4 and 5) although there was a noticeable uptick in the number of rooms sold and the revenue generated through the CRS/Voice channel, as shown on the following charts.

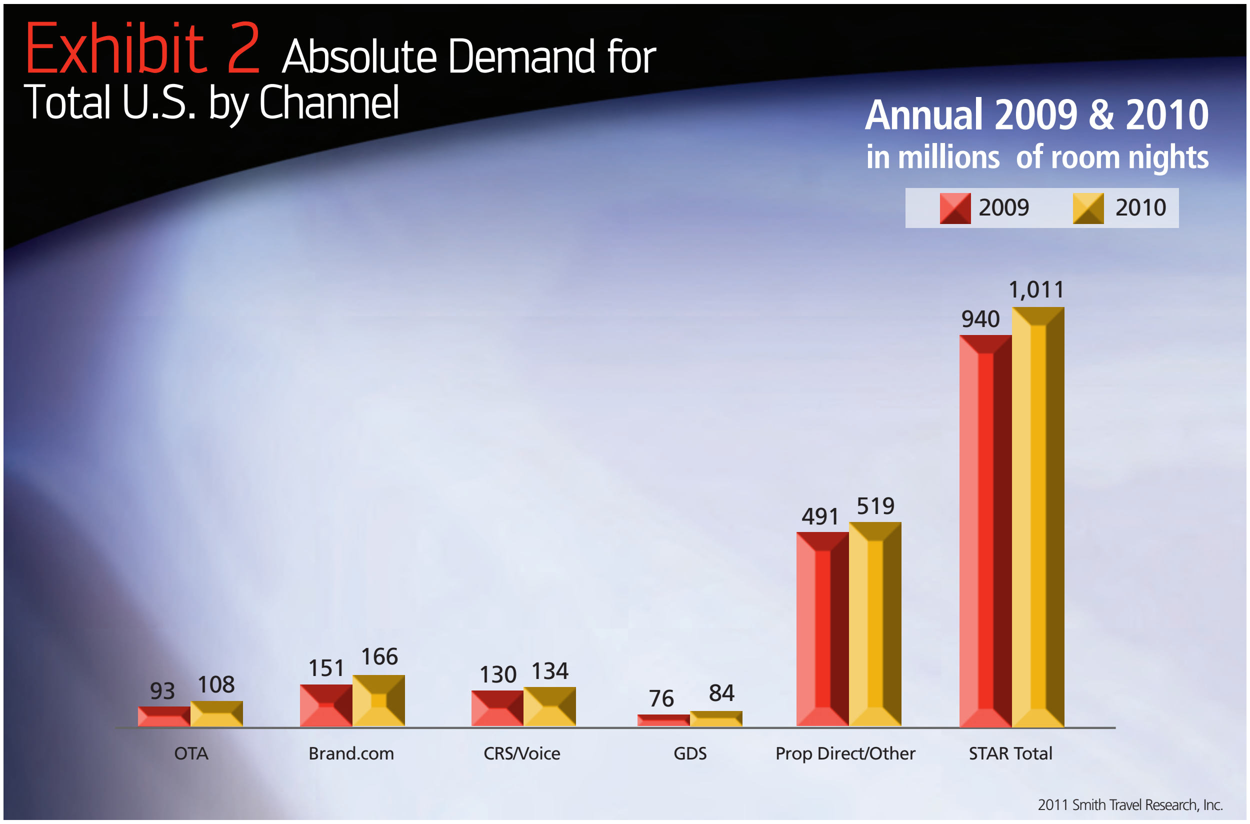


Exhibit 2 Absolute Demand for Total U.S. by Channel
Annual 2009 & 2010
in millions of room nights
2009
2010
93
108
151
166
130
134
76
84
491
519
940
1,011
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
STAR Total
2011 Smith Travel Research, Inc.

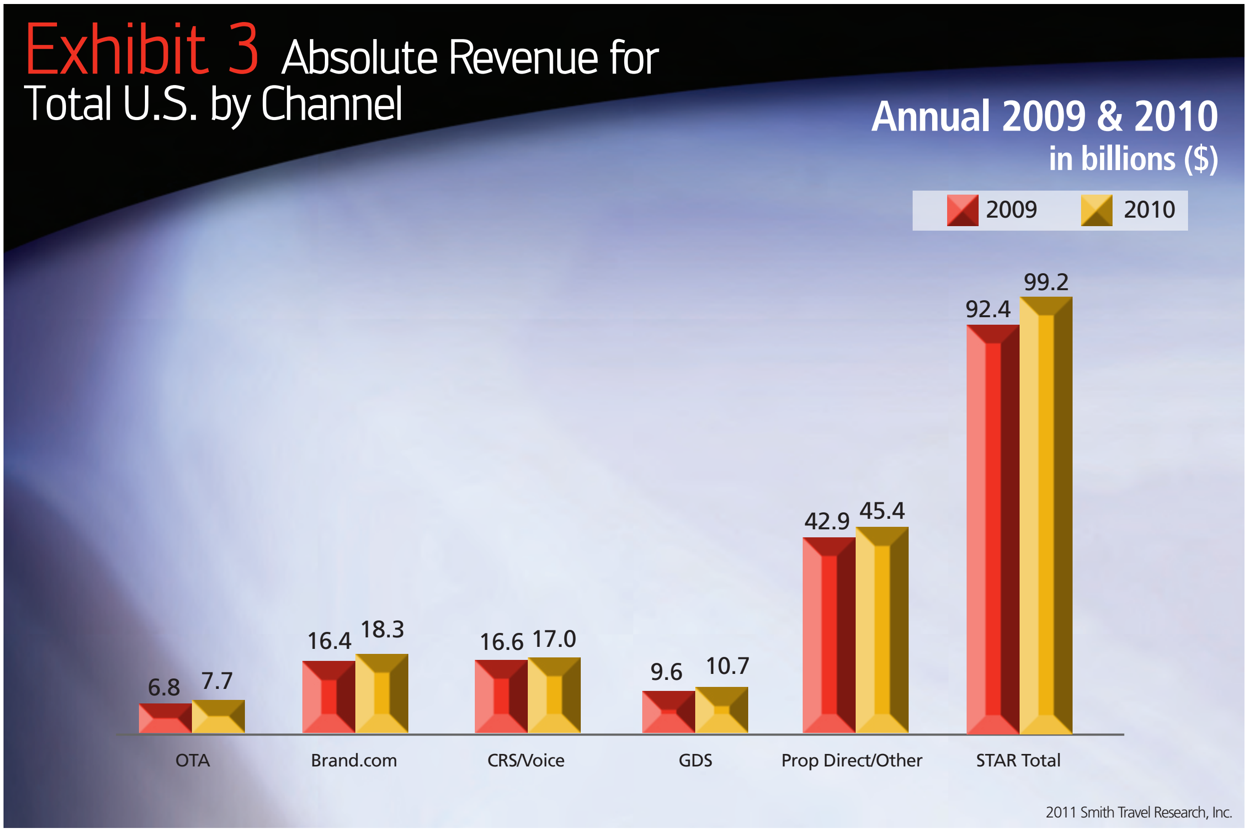


Exhibit 3 Absolute Revenue for Total U.S. by Channel
Annual 2009 & 2010
in billions ($)
2009
2010
6.8
7.7
16.4
18.3
16.6
17.0
9.6
10.7
42.9
45.4
92.4
99.2
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
STAR Total
2011 Smith Travel Research, Inc.

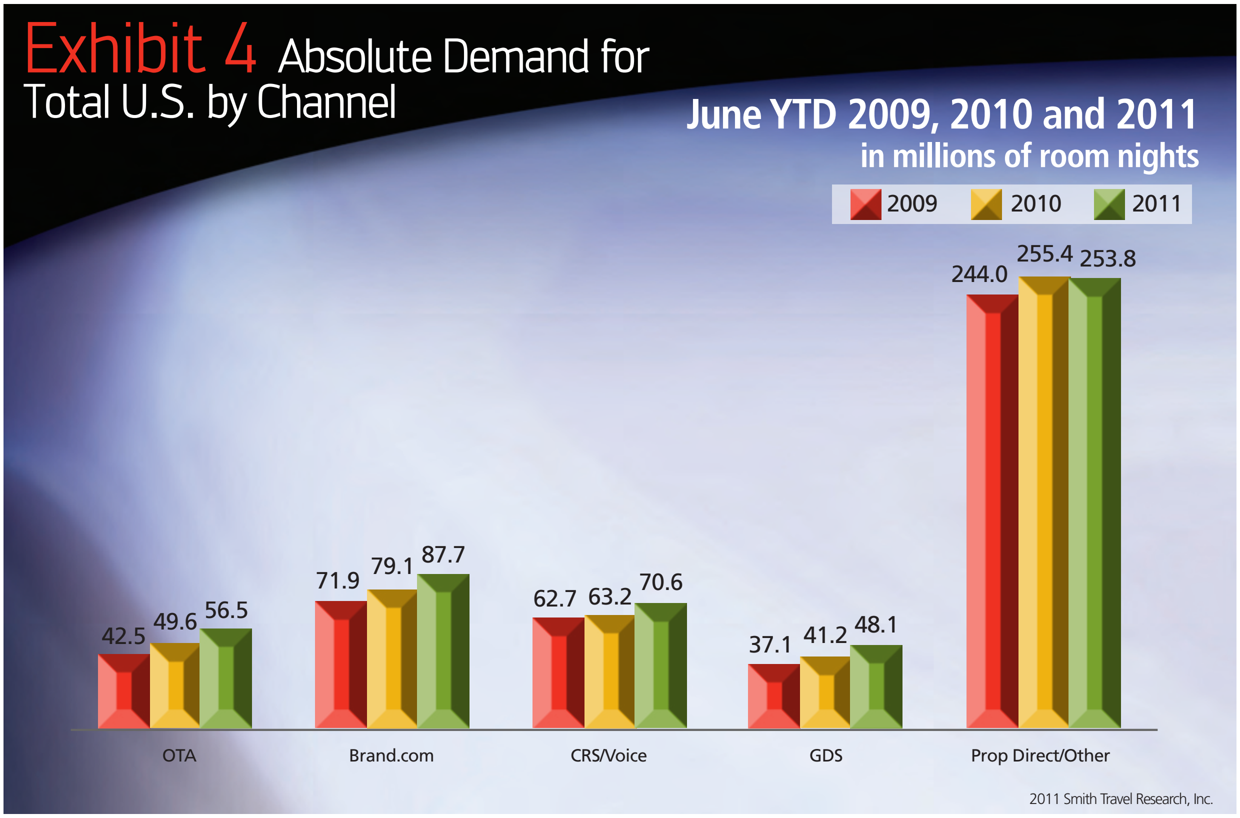


Exhibit 4 Absolute Demand for
Total U.S. by Channel
June YTD 2009, 2010 and 2011
in millions of room nights
2009
2010
2011
42.5
49.6
56.5
71.9
79.1
87.7
62.7
63.2
70.6
37.1
41.2
48.1
244.0
255.4
253.8
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
2011 Smith Travel Research, Inc.

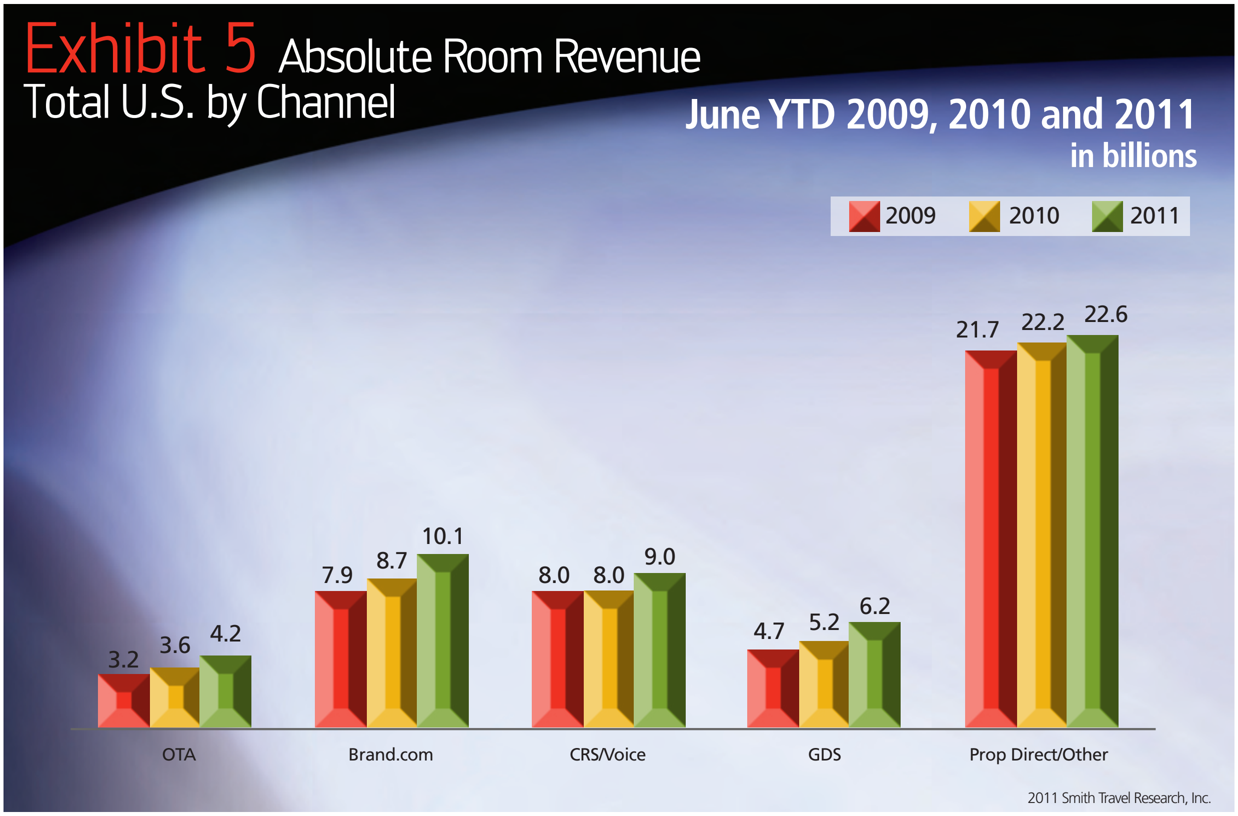
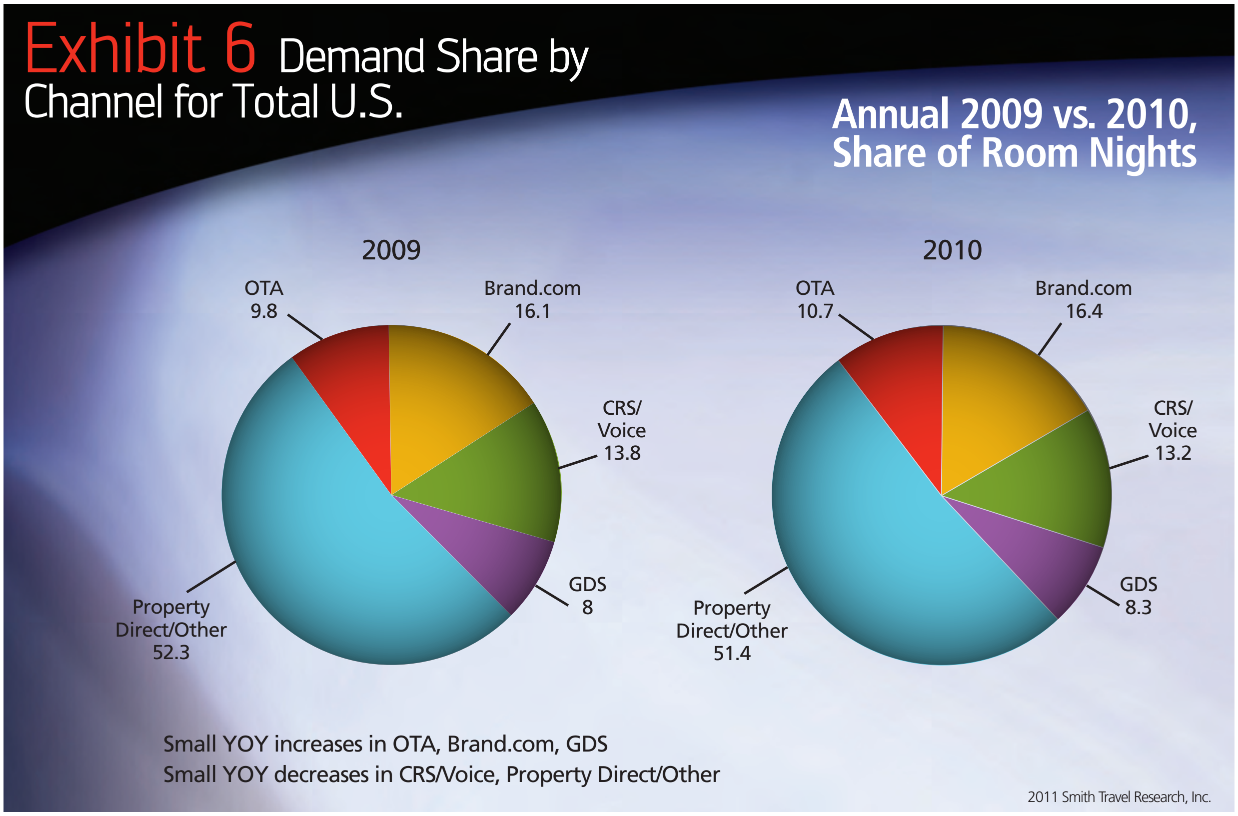


Exhibit 5 Absolute Room Revenue
Total U.S. by Channel
June YTD 2009, 2010 and 2011
in billions
2009
2010
2011
3.2
3.6
4.2
7.9
8.7
10.1
8.0
8.0
9.0
4.7
5.2
6.2
21.7
22.2
22.6
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
2011 Smith Travel Research, Inc.

Size and Structure of the U.S. Hotel Industry by Distribution Channel

The demand share by booking channel for both 2009 and 2010 for all U.S. hotels is presented in Exhibit 6. A look at the charts reveals that the majority of rooms are still booked directly with the property in both years. As described above, this is somewhat of a catch-all category, but, nonetheless, is, by far, the most widely used by a hotel's customers. Interestingly, booking through the brand website is the second most commonly used channel hovering at just above 16% for both years. When both categories are combined it is possible to see that more than two-thirds of all hotel room reservations made in the United States, in 2010, were in some way made directly through the property or its brand or property website, and adding in CRS/voice, the other "direct" channel, the direct volume for 2010 is at just over eight in ten of all room nights consumed, leaving third parties to provide the remaining 20%.

Also of note is the fact that more than 10% of total room bookings are now made through the OTAs, a booking option that did not even exist a little more than a decade ago. The difference in the percentage of rooms booked by channel between 2009 and 2010 revealed that the largest growth was seen in the OTAs, brand.com and GDS while slight declines occurred in the percentage of rooms booked through property direct/other and CRS/voice. Through the first half of 2011 (see Exhibit 7), the rate of decline in the percentage of rooms booked directly to the property accelerated from year-end 2010. It seems inevitable that the erosion in the dominance of this channel will continue as more business is booked electronically. A more detailed discussion of these recent changes will be covered in the discussion of each channel.



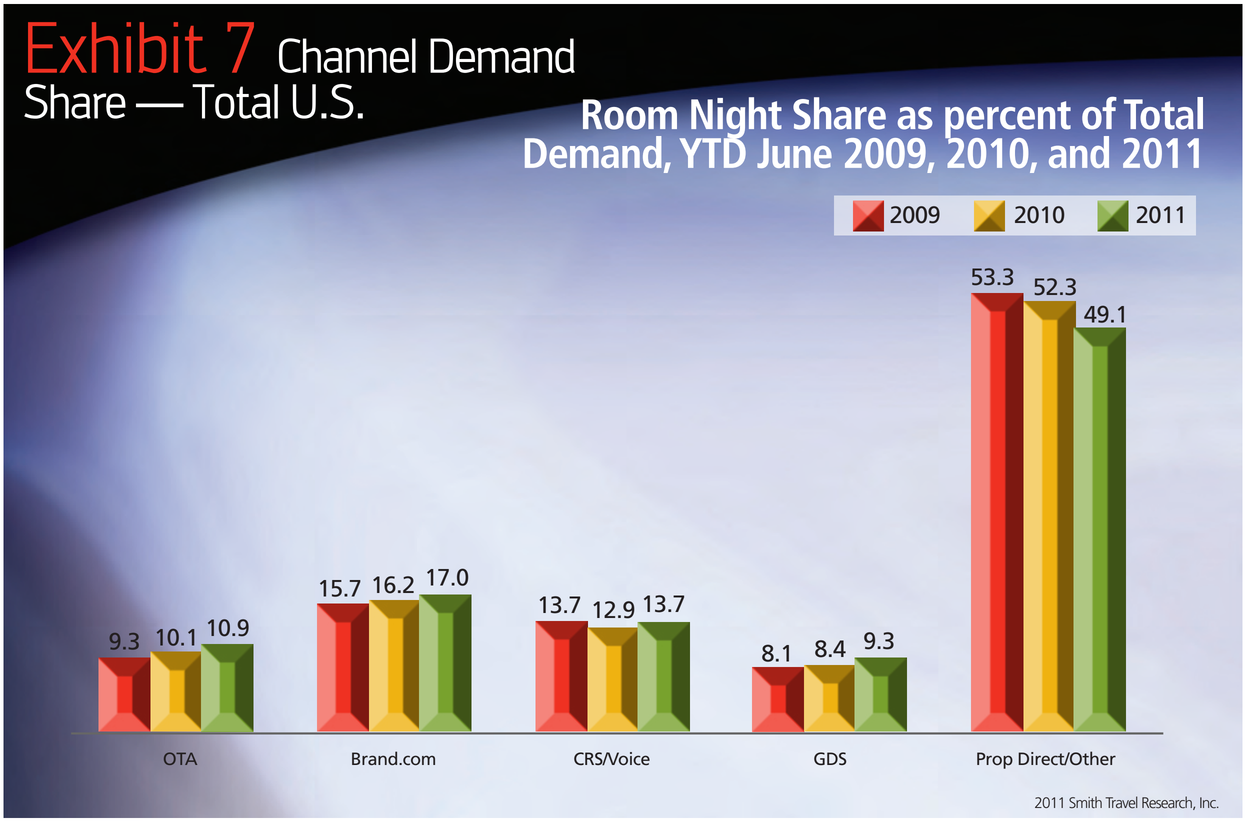


Exhibit 7 Channel Demand Share — Total U.S.
Room Night Share as percent of Total Demand, YTD June 2009, 2010, and 2011
2009
2010
2011
9.3
10.1
10.9
15.7
16.2
17.0
13.7
12.9
13.7
8.1
8.4
9.3
53.3
52.3
49.1
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
2011 Smith Travel Research, Inc.

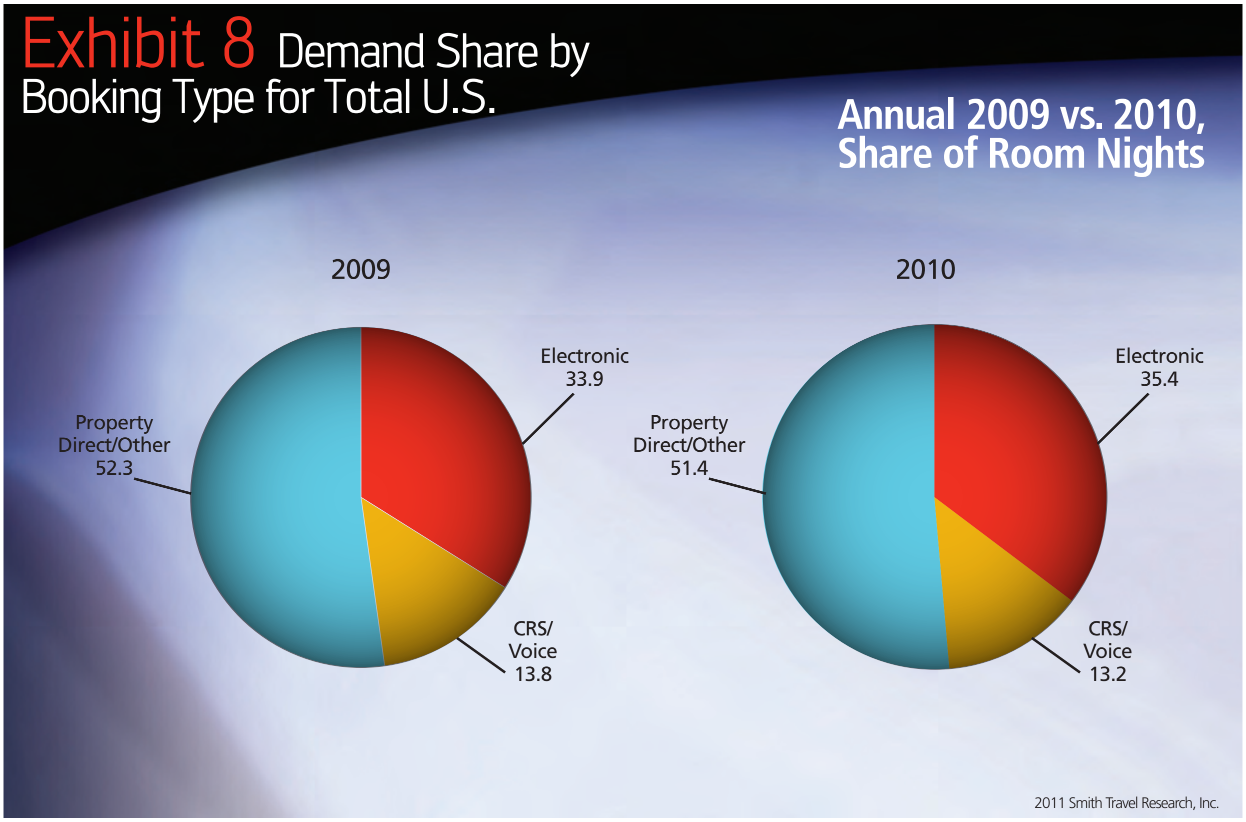
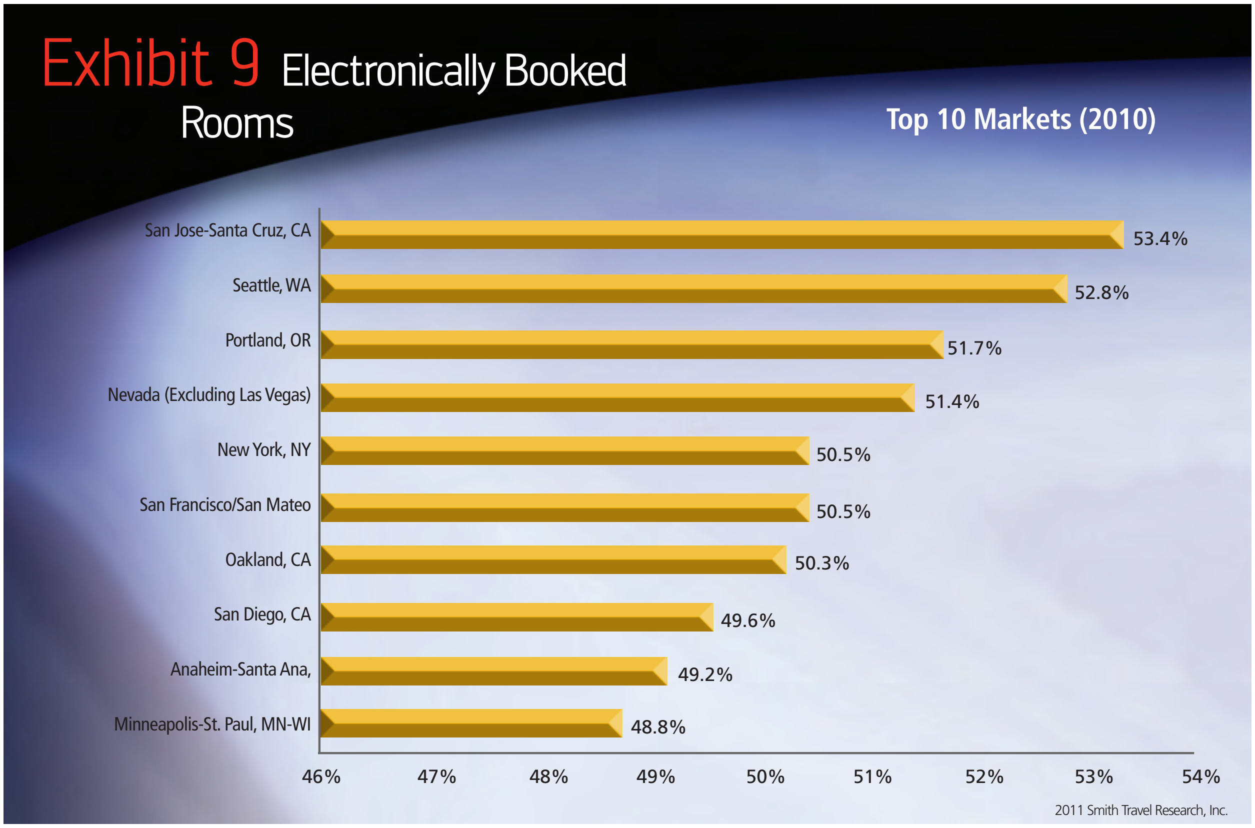


Exhibit 8 Demand Share by Booking Type for Total U.S.
Annual 2009 vs. 2010, Share of Room Nights
2009
Electronic 33.9
Property Direct/Other 52.3
CRS/ Voice 13.8
2010
Electronic 35.4
Property Direct/Other 51.4
CRS/ Voice 13.2
2011 Smith Travel Research, Inc.

Observing the bookings in a somewhat different way, it is clear that bookings through the electronic channels, (i.e., OTAs, brand.com, and GDS) now exceed 35% of all room bookings and are increasing (see Exhibit 8). This growth in the use of electronic channels was at the expense of the other two broadly defined categories, CRS/voice and direct to the property. The shift from off-line to online or electronic bookings will continue to capture an increasing share of hotel reservations. As will repeated several times throughout this book, the industry's ability to manage and exploit the opportunities presented by the Internet and its ever-evolving nature will be critical to enhanced future performance.

Not surprisingly, there is a large variation in the percentage of rooms booked, by market, via the Internet. Guests staying at hotels in West Coast markets (see Ex. 9) have a tendency to book their rooms electronically. Eight of the top ten markets with the highest percentage of rooms booked in this manner are on the West Coast, led by San Jose, California at more than 53%. Guests staying at secondary and tertiary markets, however, are much more likely to use more traditional booking channels. Understanding the dynamics of your own market and your own competitive set is critical to an efficient use of booking channels.



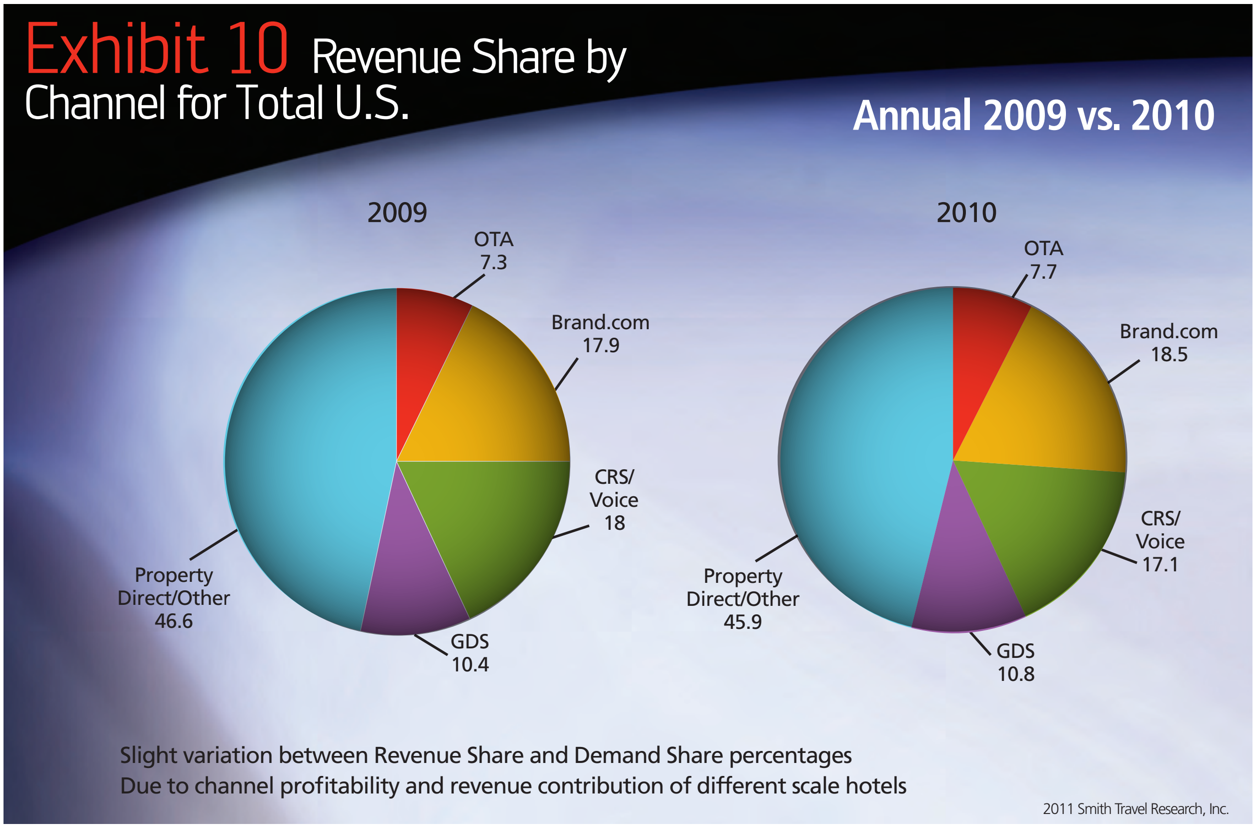


Exhibit 10 Revenue Share by Channel for Total U.S.
Annual 2009 vs. 2010
2009
OTA 7.3
Brand.com 17.9
CRS/ Voice 18
GDS 10.4
Property Direct/Other 46.6
2010
OTA 7.7
Brand.com 18.5
CRS/ Voice 17.1
GDS 10.8
Property Direct/Other 45.9
Slight variation between Revenue Share and Demand Share percentages
Due to channel profitability and revenue contribution of different scale hotels
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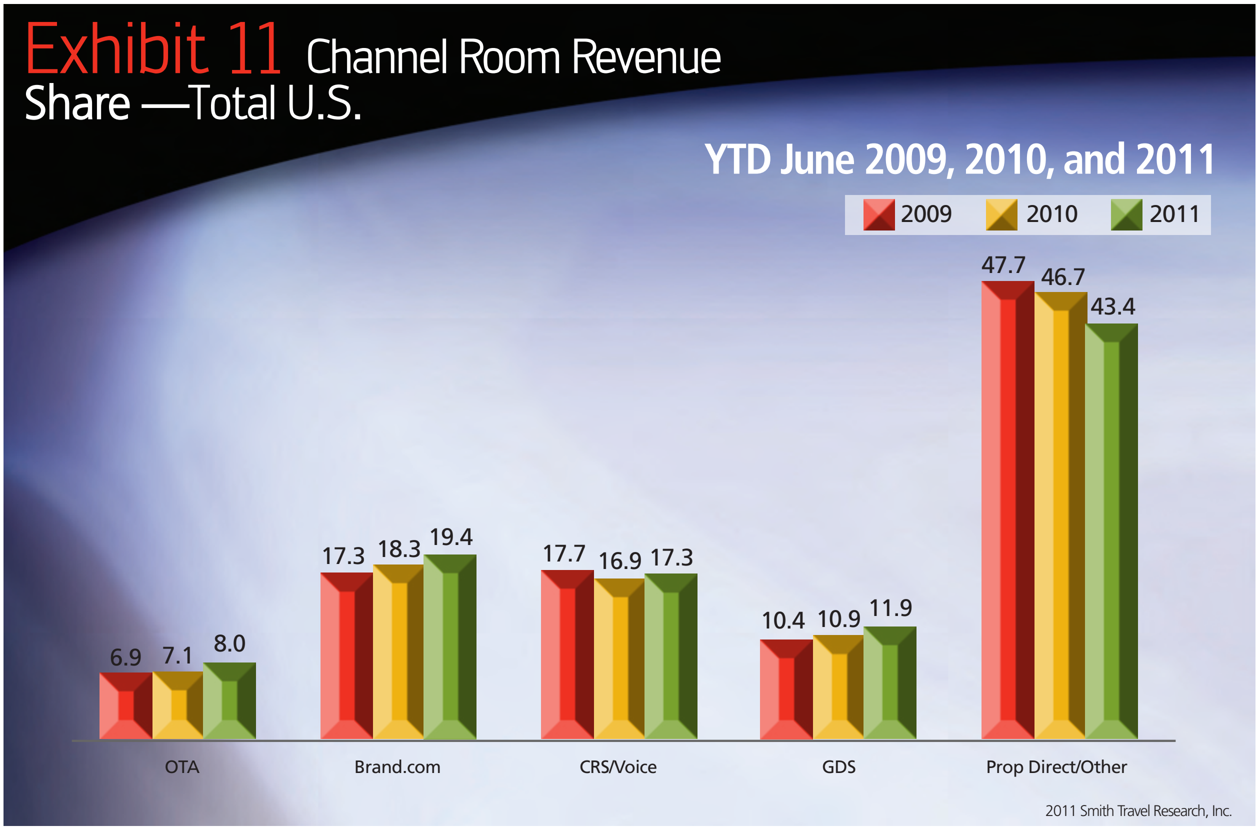
Exhibit 11 Channel Room Revenue Share —Total U.S.
YTD June 2009, 2010, and 2011
2009
2010
2011
6.9
7.1
8.0
17.3
18.3
19.4
17.7
16.9
17.3
10.4
10.9
11.9
47.7
46.7
43.4
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
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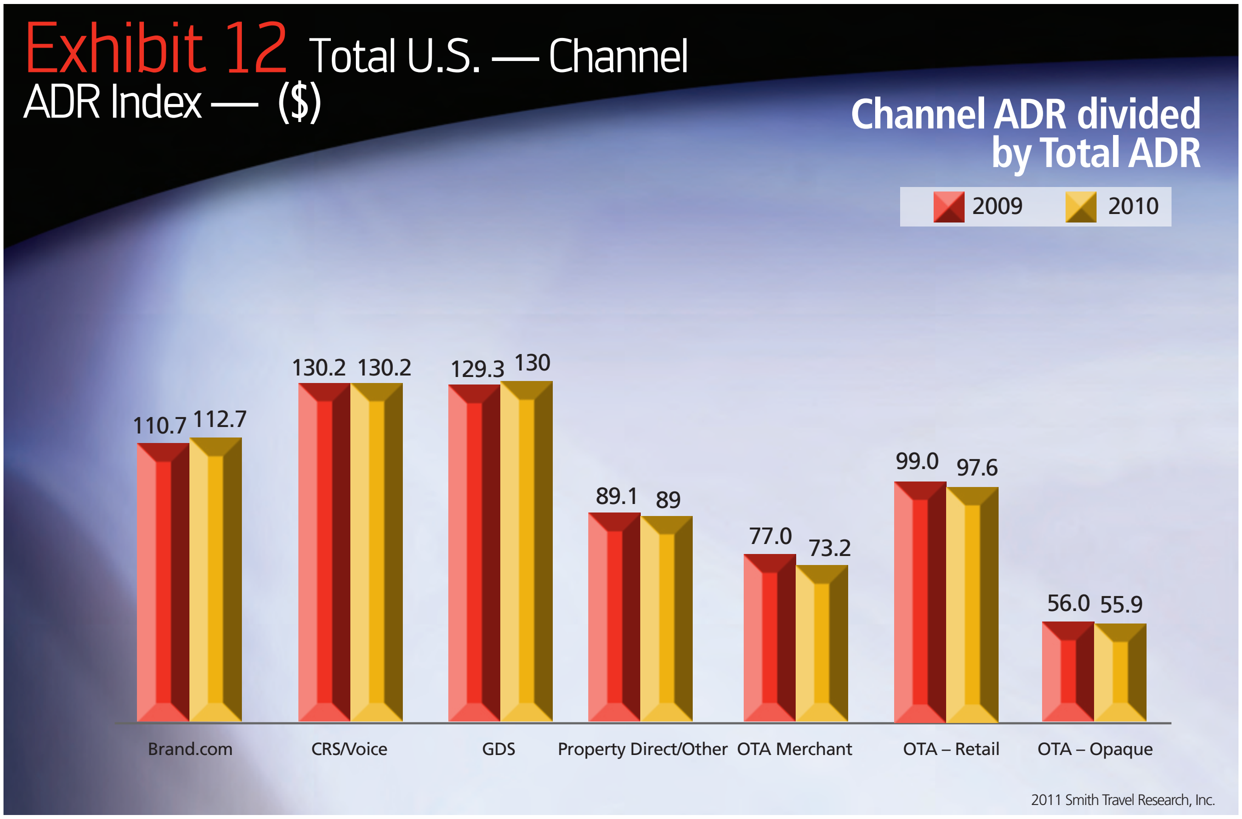
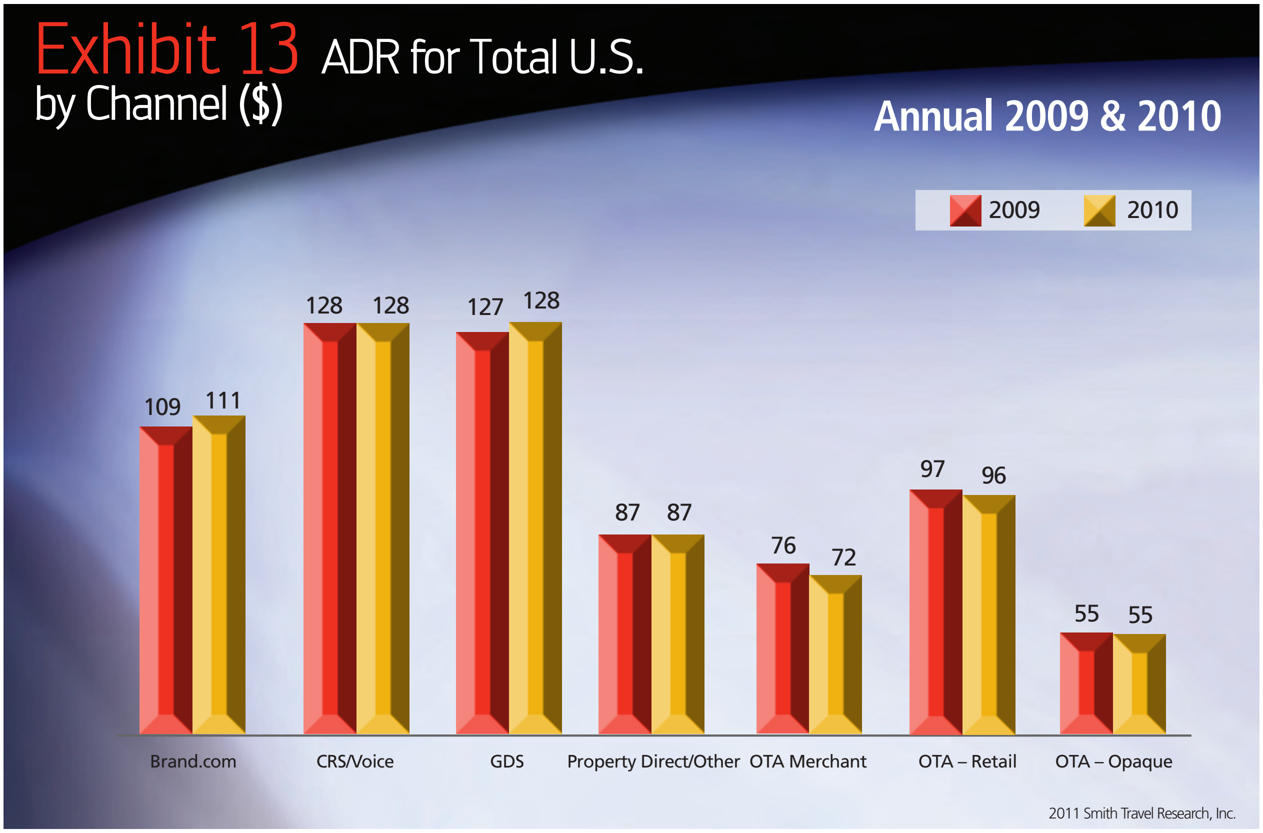
Shown on Exhibit 10 is the revenue share all hotels realized through each of the various booking channels in 2009 and 2010. While it would make sense that the revenue share would somewhat mirror the demand share, some discrepancies in their relative shares are obvious. For both the OTAs and property direct/other categories the revenue share associated with the channel is much less than the associated demand share, while just the opposite is true for the other three channels. As was the case with demand share the precipitous decline in revenue share contributed by property direct/other is also seen when viewing the June YTD data from 2009 to 2011(see Exhibit 11). Room revenue share increased for all other channels from June YTD 2010 to 2011.

To help understand the relative revenue efficiency to the property of each channel, see Exhibit 12, in which an ADR efficiency index for each of the channels in 2009 and 2010 is presented. Generally, an index of 100 would indicate that each booking yields the hotel a room revenue share that is exactly equal to room revenue per guest per transaction for an average of all bookings. A number greater than 100 means that the average booking through that channel yields more than its fair share of revenue through that channel while a number less than 100 indicates the average booking generates less than its fair share of revenue. Stated another way, if all channels had a booking efficiency index of 100 the ADR through every channel would be exactly the same.





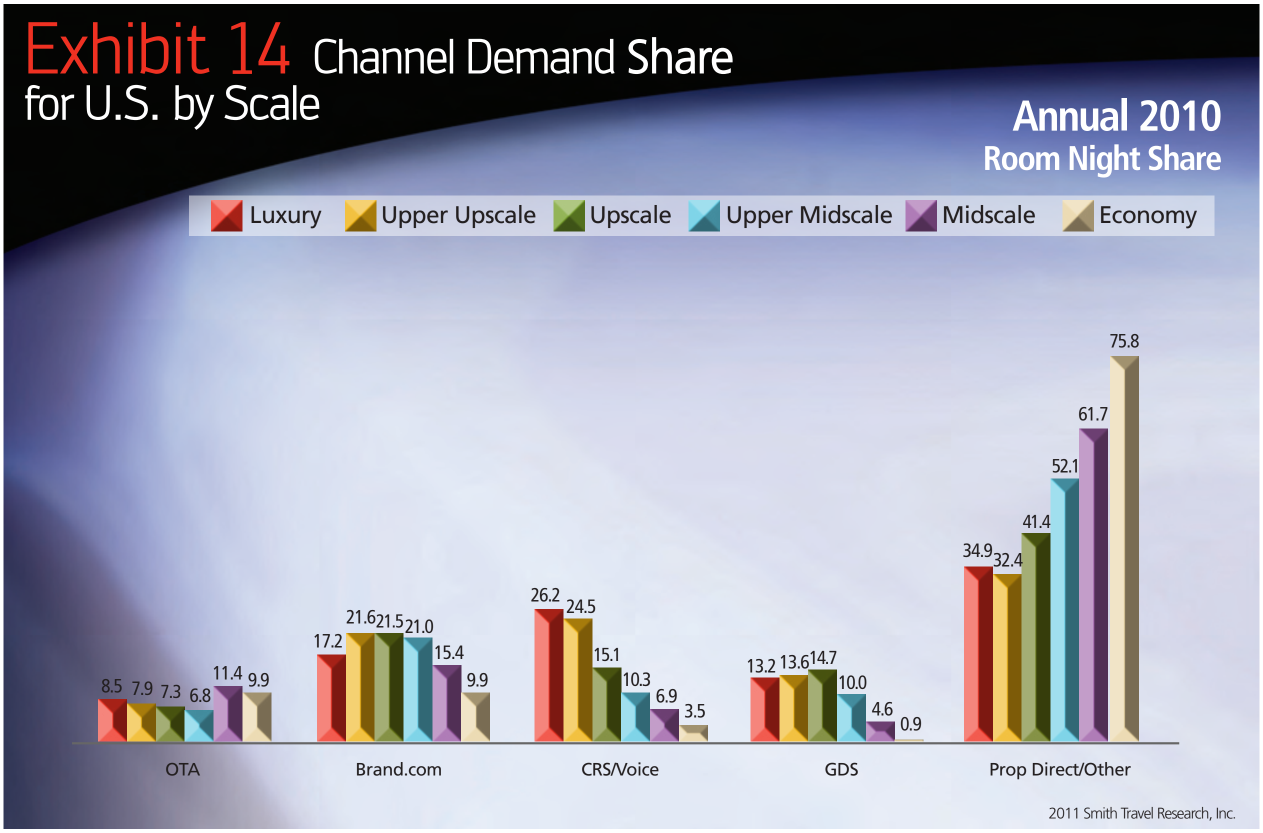
The calculation of the channel ADR efficiency index is relatively simple and is computed by dividing the ADR for each channel by the blended ADR for all channels, more commonly referred to as the property or segment ADR.

As with demand share, the room revenue share through OTAs, brand.com and the GDS increased in 2010, while the share generated through the other two channels declined. Again, these patterns remained consistent through the first half of 2011.

In trying to put the ADR efficiency index in perspective and to understand the effect bookings through the various channels can have on property level revenue for the total United States, the ADR achieved through each channel in both 2009 and 2010 are presented in Exhibit 13. The amount of revenue realized by the property, in 2010, can vary widely depending on the channel, from as low as $55 for the OTA opaque channel, to a high of about $128 realized through a GDS. Despite the fact that this analysis presents total U.S. results and therefore combines all the properties for which we have data, it nonetheless presents a picture of how the amount of revenue a property generates can be widely affected by how guests book rooms to that property. Another way to interpret Exhibit 13 is to assume that the entire United States was one hotel .If so, the average ADR of about $98 reported in each of the last two years was achieved through the blended room rates the property received from each of these channels. Though it is theoretical, it may be a good way to better understand the effects of each channel on revenue.

When looking at Exhibits 12 and 13 from a chain scale perspective, the values presented will show a much greater variability as the ADRs of the chain scale segments are either well above or below $100.

However, looking at channel efficiency through this singular lens of how much room rate revenue is generated by each of the respective distribution channels would not be wise because there are many other factors to consider before settling on the appropriate channel mix for a specific property. It is especially important to understand both the direct and indirect costs associated with



each booking channel. A broader discussion of these factors and how they should play into a distribution strategy is undertaken later in the Optimal Channel Mix chapter of the study.

At the total U.S. level, any analysis of the results presented requires an understanding of the methodology employed to arrive at those results. As with any data set in which it would be hoped to project to a broader industry definition, the first step is to determine the size and composition of the participating hotels relative to the total hotel supply. The associated sidebar describes the methodology Smith Travel Research utilized in projecting to total U.S. results.

As explained in the associated sidebar (next page), the demand and revenue shares at the total U.S. level are a function of what happens when you blend a varied data set, such as channel bookings, into an aggregated number. As can be seen in both Exhibit's 14 and 15 the channel demand share and channel revenue share varied widely for STR's chain scales in 2010. As is evident from the data provided on these two charts, booking patterns reported by properties in different chain scale segments can vary widely. As an example, the farther down the price scale you go the more likely room bookings are going to be made directly to the property. Conversely, higher end properties will tend to get a much larger percentage of their bookings through CRS/voice and GDS channels. In addition, while the room revenue shares somewhat mirror the demand share, not all chain scale segments are able to yield each channel in the same way. To that point, upscale hotels tend to do a much better job of maximizing room revenue from guests who book directly to the property while luxury hotels lag behind their chain scale counterparts in yielding revenue obtained through brand.com. Of course, much of that result is due to the respective revenue optimization strategies employed, but, nonetheless the results analyzed in this manner do highlight the respective booking channel differences seen in each of the chain scale segments.

When also considering the different room rates achieved by the properties in the different chain scale segments (Exhibit 16), and the number of rooms in each of the segments (Exhibit 17), it is not surprising that the blended U.S. results would yield findings that may not be reflective of an individual property, brand, or segment. In effect, like any measure that aggregates diverse industry segments, the blended results may differ greatly from those reported by the individual segments. The primary segments used for analysis are the STR chain scales. Please see the chain scale side bar for an explanation of this categorization. Another factor to consider, when examining total U.S. demand and revenue share results is the wide variance in ADRs realized by hotels in the OTA merchant, retail and opaque models vs. the other booking channels. As described earlier in this report, it's clear that the primary reason for the discrepancy is that what the guest actually pays for the room and what the hotel receives in revenue for that room are different because of how the OTAs are compensated. The hotel receives the rate with the commission already removed, while the guest pays the full rate directly to the OTA who keeps the commission as a fee for its services. Most hotel rates that are commissionable are received and recorded in full by the hotel and then the commission is paid after the guest's departure and booked as a hotel expense. Therefore, since the room rate realized by the hotel for OTA bookings is substantially less than room rates realized by the hotels through the other channels, it is not surprising that the revenue share of OTAs is well below the corresponding demand share. Exhibit 13, shown earlier, presents the average daily room rate achieved by booking channel for all U.S. hotels in 2010. The method-of-payment for the channel (either as net rate or a commission paid after departure) clearly affects the room rate attributable to the OTA channels.

Methodology

In order to arrive at the total US numbers presented in this study, STR took into consideration the following data sets:

- The sample of hotels contributing booking channel data
- The sample of hotels that currently participate in STR's monthly STAR program
- The universe of hotels in each of the STR chain scale segments

Initially, the data provided by each of the hotels for which booking channel data were received were categorized into their respective chain scale segments. Then all the raw booking channel data were accumulated in order to arrive at total room demand and room revenue results, by channel, by chain scale segment.

Once the totals were derived, the following measures were computed for each channel, by month for each respective chain scale segment:

- Average room rate
- Room demand share
- Room revenue share

These results were compared to the aggregated computations from the corresponding chain scale results regularly calculated for the STAR program. Recognizing that the varied samples for the two data sets would result in slightly different scale-wide results two assumptions were made about the respective data sets. First, the aggregated demand and room revenue results generated through the STAR program were assumed to be more accurate and reliable than the identical numbers arrived at by aggregating the booking channel demand and room revenue numbers. Second, the demand and room revenue shares calculated, by chain scale, by channel, using the booking channel data, were assumed to be an accurate reflection of chain scale segment patterns. Using those two assumptions drove the algorithms to adjust the raw demand and room revenue booking channel data so that they would match up exactly with the larger more established STAR results.

Once the monthly booking channel data were recalculated, then the values were accumulated to total U.S. and chain scale-specific results on a monthly and annual basis.

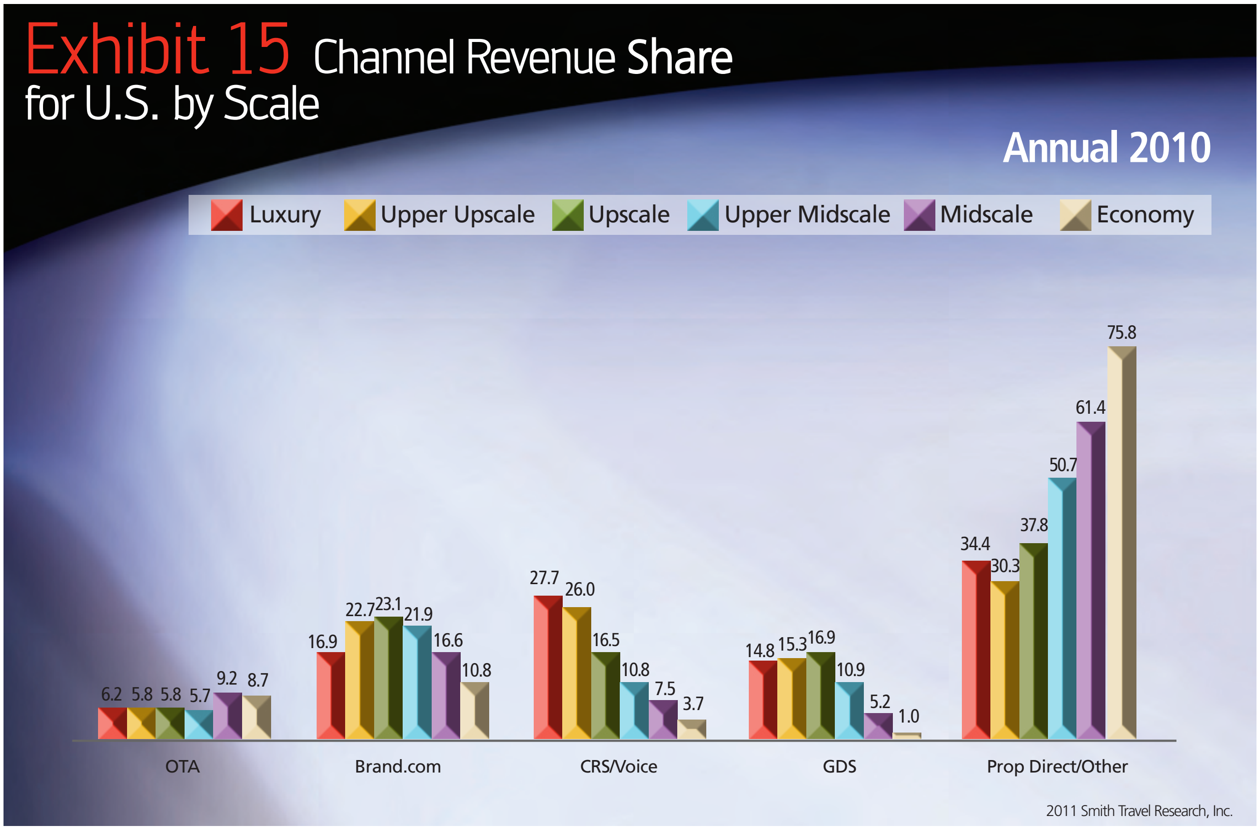


Exhibit 15 Channel Revenue Share for U.S. by Scale
Annual 2010
Luxury
Upper Upscale
Upscale
Upper Midscale
Midscale
Economy
6.2 5.8 5.8 5.7 9.2 8.7
16.9 22.7 23.1 21.9 16.6 10.8
27.7 26.0 16.5 10.8 7.5 3.7
14.8 15.3 16.9 10.9 5.2 1.0
34.4 30.3 37.8 50.7 61.4 75.8
OTA
Brand.com
CRS/Voice
GDS
Prop Direct/Other
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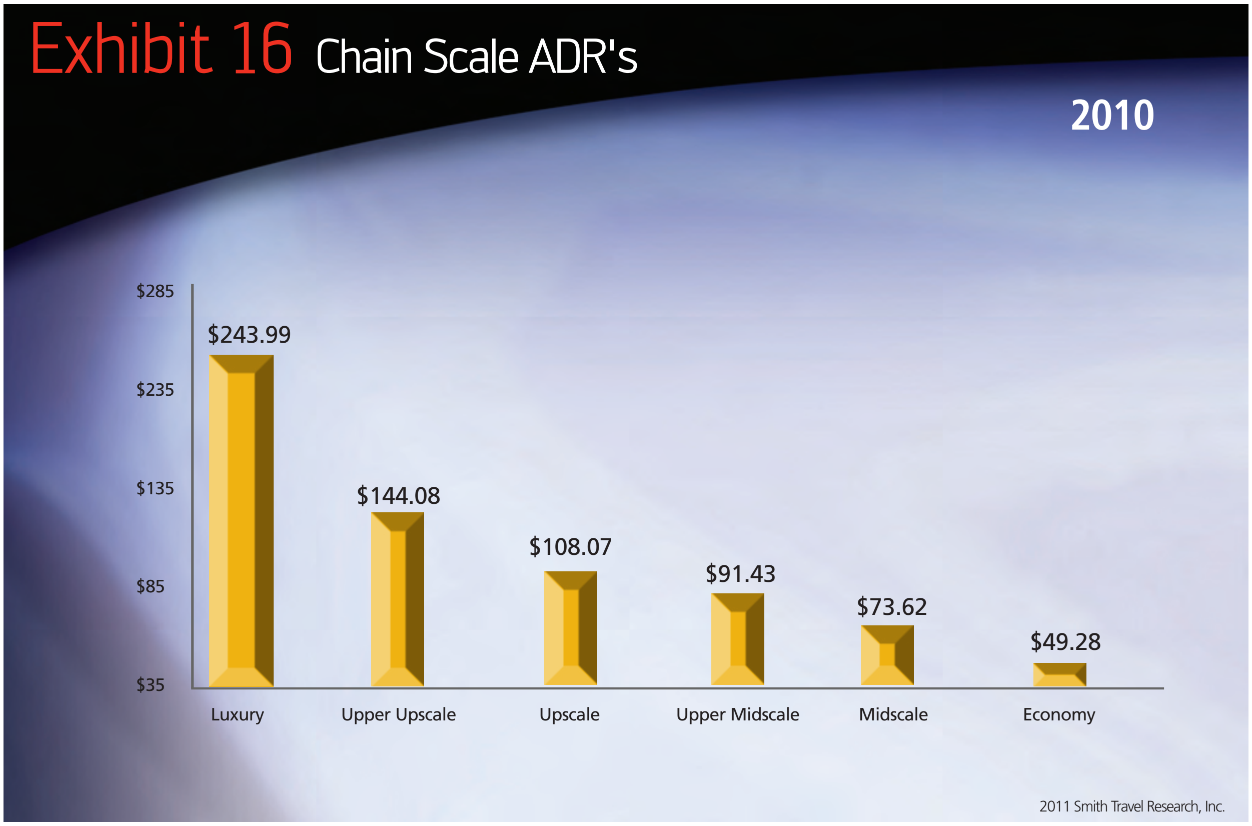
Exhibit 16 Chain Scale ADR's
2010
$285
$235
$135
$85
$35
$243.99
$144.08
$108.07
$91.43
$73.62
$49.28
Luxury
Upper Upscale
Upscale
Upper Midscale
Midscale
Economy
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STR Chain Scales

One of the ways that STR segments the U.S. lodging industry is through Chain Scale categories. The primary driver in the creation of these segments is to have the ability to measure relative performance of lodging brands against an aggregate of similarly priced and positioned competitors. To do that, lodging brands are grouped together in one of six categories based primarily on each brand's average daily room rate for the most recent calendar year. By using room rate as the primary factor to determine within which segment each brand is placed, the system avoids arbitrary and subjective categorizations.

The names of the current STR chains scales are as follows:

Luxury – the highest priced properties in most markets
Upper Upscale – typically meeting and convention hotels
Upscale – primarily business hotels in suburban locations
Upper Midscale – higher priced mid-tier properties
Midscale – moderately priced mid-tier hotels
Economy – typically lowest priced chain hotels in a market
Independents – no chain affiliation

Table 1 presents a snapshot look at the size and structure of the U.S. lodging industry for each of these seven segments in 1990, 2000, and 2010. Presented is the number of rooms that existed in each segment, the number of rooms sold in each segment, and the room revenue generated by each segment at the end of those three years. In addition, **Table 2** presents the relative share of each of these three key measures during each time period. At this point in time, it is easy to see structural changes in both the composition of the U.S. lodging industry and individual segment performance.

TABLE 1 — KEY U.S. CHAIN SCALE INDICATORS IN BILLIONS

	Supply			Demand			Room Revenue		
	1990	**2000**	**2010**	**1990**	**2000**	**2010**	**1990**	**2000**	**2010**
Luxury	53.9	69.7	123.3	36.2	51.0	81.9	1.7	4.3	7.3
Upper Upscale	385.5	452.5	541.2	258.8	326.5	364.7	8.6	16.6	19.0
Upscale	174.6	355.6	593.1	115.0	251.1	392.4	3.0	9.3	15.4
Upper Midscale	402.8	636.5	762.5	256.9	413.7	445.5	5.0	11.1	14.9
Midscale	416.2	537.5	572.0	251.5	308.5	296.0	4.5	7.3	7.7
Economy	492.3	727.4	781.0	315.5	426.2	403.9	4.2	7.3	7.3
Independent	1412.7	1406.2	1450.0	889.3	867.5	792.6	18.1	25.8	27.6
Total U.S.	3337.8	4185.4	4823.0	2123.2	2644.5	2777.0	45.1	81.7	99.4

TABLE 2 — ROOM SUPPLY, DEMAND & ROOM REVENUE SHARE PERCENT OF TOTAL INDUSTRY

	Supply Share			Demand Share			Room Revenue Share		
	1990	**2000**	**2010**	**1990**	**2000**	**2010**	**1990**	**2000**	**2010**
Luxury	1.6%	1.7%	2.6%	1.7%	1.9%	2.9%	3.8%	5.3%	7.3%
Upper Upscale	11.5%	10.8%	11.2%	12.2%	12.3%	13.1%	19.1%	20.3%	19.1%
Upscale	5.2%	8.5%	12.3%	5.4%	9.5%	14.1%	6.7%	11.4%	15.5%
Upper Midscale	12.1%	15.2%	15.8%	12.1%	15.6%	16.0%	11.1%	13.6%	15.0%
Midscale	12.5%	12.8%	11.7%	11.8%	11.7%	10.7%	10.0%	8.9%	7.8%
Economy	14.7%	17.4%	16.2%	14.9%	16.1%	14.5%	9.3%	8.9%	7.3%
Independent	42.3%	33.6%	30.1%	41.9%	32.8%	28.5%	40.1%	31.6%	27.8%
Total U.S.	100%	100%	100%	100%	100%	100%	100%	100%	100%

While the pace, quantity and revenue generated by bookings through the various channels are of critical importance, another factor to be considered when evaluating the relative values of each channel is the average length of stay associated with the bookings. Depending on the cost structure associated with the channel and if that cost is based on a per-booking or a per-room-night basis, the total value of the reservation to the property can be very different. In the Costs of Distribution chapter of this study a more detailed analysis will be presented of the cash flow through to the bottom line that a property can expect from a typical booking via each of the channels. Needless to say, the average length of stay is a critical component of that analysis.

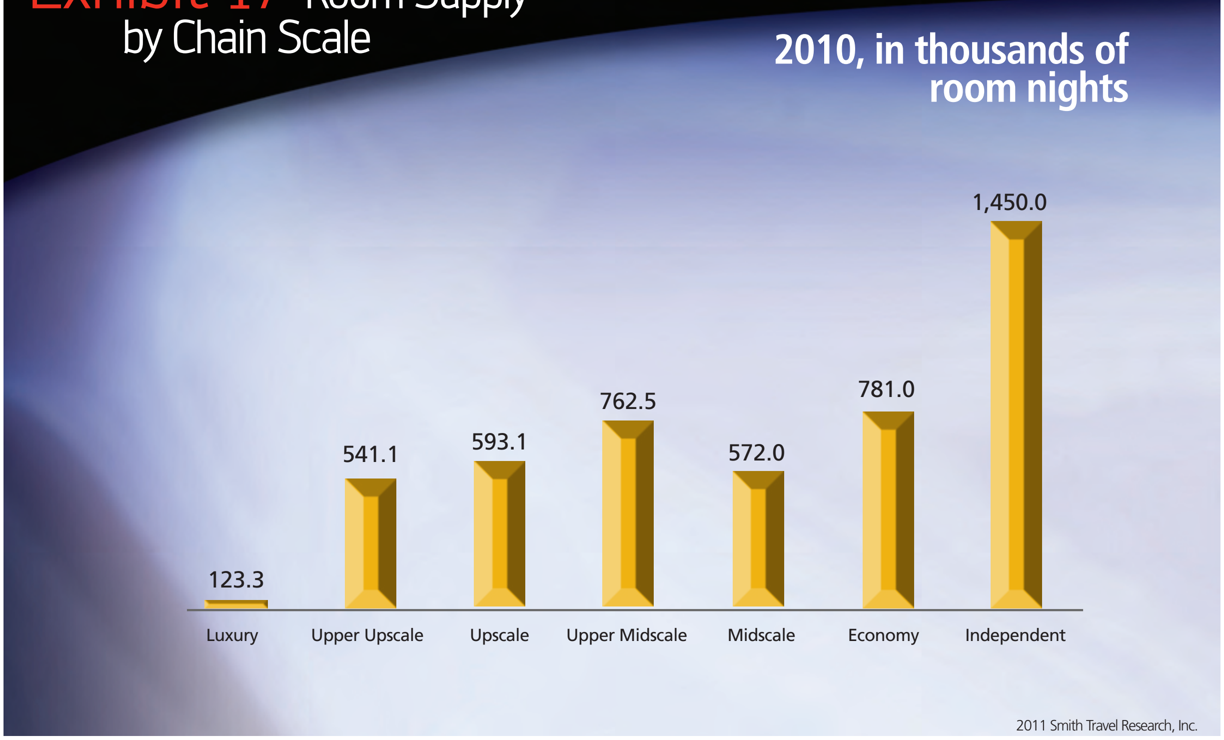
Exhibit 18 presents the average length of stay, by channel, for 2009 and 2010. Interestingly, length of stay by channel in 2009 was identical to 2010 for each of the channels. The average length of stay varied from a low of 1.7 nights for bookings through the OTA-opaque channel to a high of 2.4 nights for those who booked their reservation directly with the property. Generally speaking, most channels averaged a little more than two nights per reservation.

At this point there needs to be a closer examination of each of the broadly defined booking channels. In our discussion of these channels our primary focus of the analysis will be on the STR chain scales to help interpret variability in booking channel mix.

ONLINE TRAVEL AGENCIES (OTAs) — ALL MODELS

As anyone who has followed the U.S. lodging industry over the past decade knows, the growth and proliferation of third party online distribution sites have been dramatic. In the ten years since 2001, their combined share of the total customer spend has grown from 1.4% to an estimated 8.4% in 2011. In each year of the past decade, the OTA vendors have captured an increasing share of the total customer spend. If we were to add to the existing totals the estimates of the additional revenue customers spent on hotel rooms but that was not reflected in hotel revenue streams, the revenue share captured by this segment would have approached 10% in 2010. Exhibit 19 presents the OTA room revenue share for each of the years in the last decade.

Exhibit 17 Room Supply by Chain Scale



In absolute revenue terms, the dollar spend has grown from $1.4 billion in 2001 to more than $7.6 billion, in 2010, and it is expected to grow again in 2011. During that same period of time total U.S. lodging industry room revenue has increased from just over $78 billion in 2001 to approximately $107 billion in 2011 .The year-over-year growth in room revenue for both the total industry and the OTAs over the last ten years along with our estimate for 2011, are shown in Exhibit 20. A close examination of that exhibit reveals that while total industry room revenue has fluctuated rather dramatically from year to year, both up and down, the growth in hotel industry room revenues generated by the OTAs has grown every year. That is an especially salient point since regardless of the economic cycle in which the U.S. lodging industry operates, room sales generated through the OTA channels have continued to rise.

Exhibit 21 looks at the percentage change in room revenue for all US hotels and OTAs from 2004 through 2011. (The numbers for 2002 and 2003 numbers are not presented because during those initial growth years for the OTAs their percentage increases in room revenue were more than 100%). In each year, hotel room revenue growth captured by the OTAs exceeded that of the corresponding increase reported by the hotel industry. Perhaps the most dramatic variance was seen in 2009 when total U.S. room revenue declined 14.2%, a drop of more than $15 billion, while OTA room revenue increased 1.5%. At least one of the reasons for this wide disparity was the willingness of hotels to make more of their rooms available through these channels in 2009. In that stressful economic year, hoteliers were desperate to fill their rooms and began embracing any and all possible distribution channels. In addition, it appears that while certain chain scale segments actually reduced their reliance on this channel in 2010, in the aggregate, the growth in both demand and room revenue continued.

The percentage of total demand booked, by chain scale, through OTAs for 2009 and 2010 is shown in Exhibit 22. In that one year, there appears to be a bit of a structural shift in how the respective segments utilized this channel. For luxury and upper upscale chains, the OTA share of total booked room nights declined while it increased for each of the other segments, dramatically so for economy chains. A modified version of that pattern continued during the first half of 2011, with all segments, except luxury, reporting

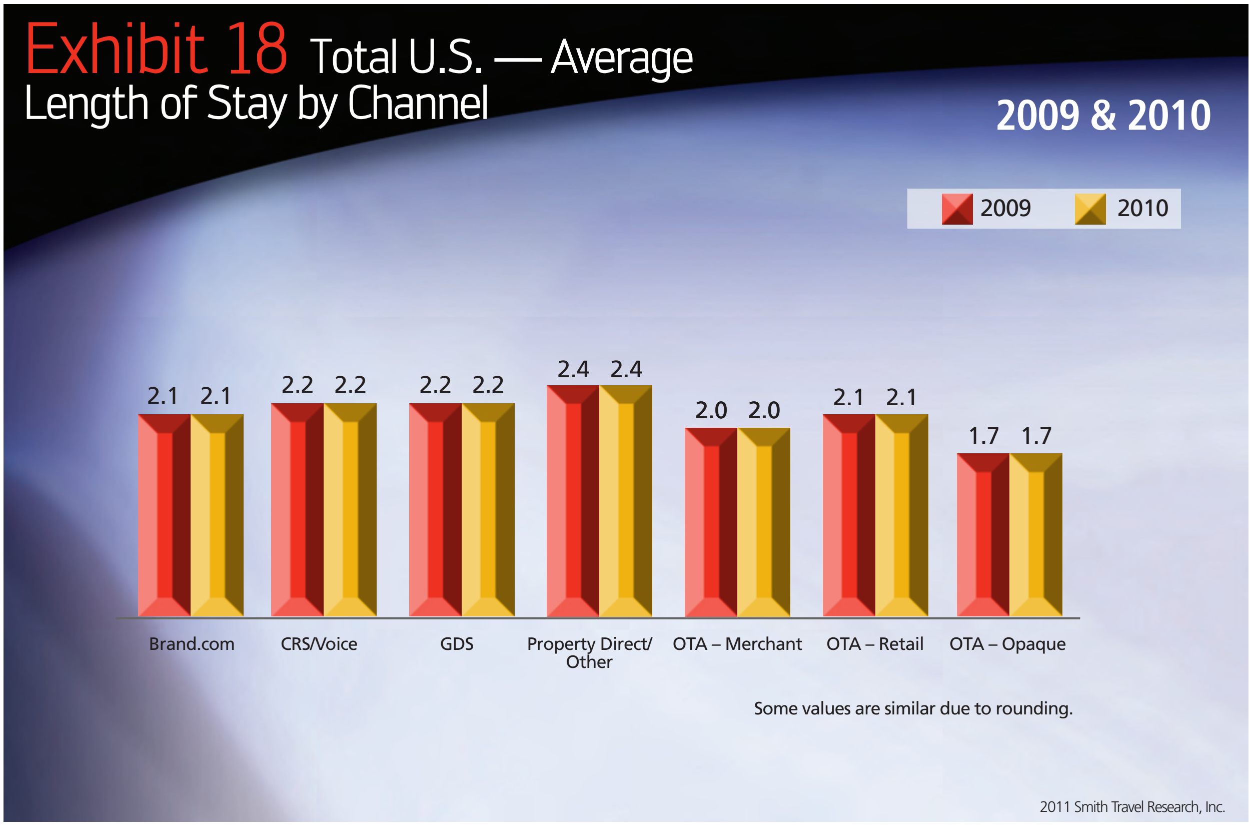


Exhibit 19 OTA Room Revenue Share

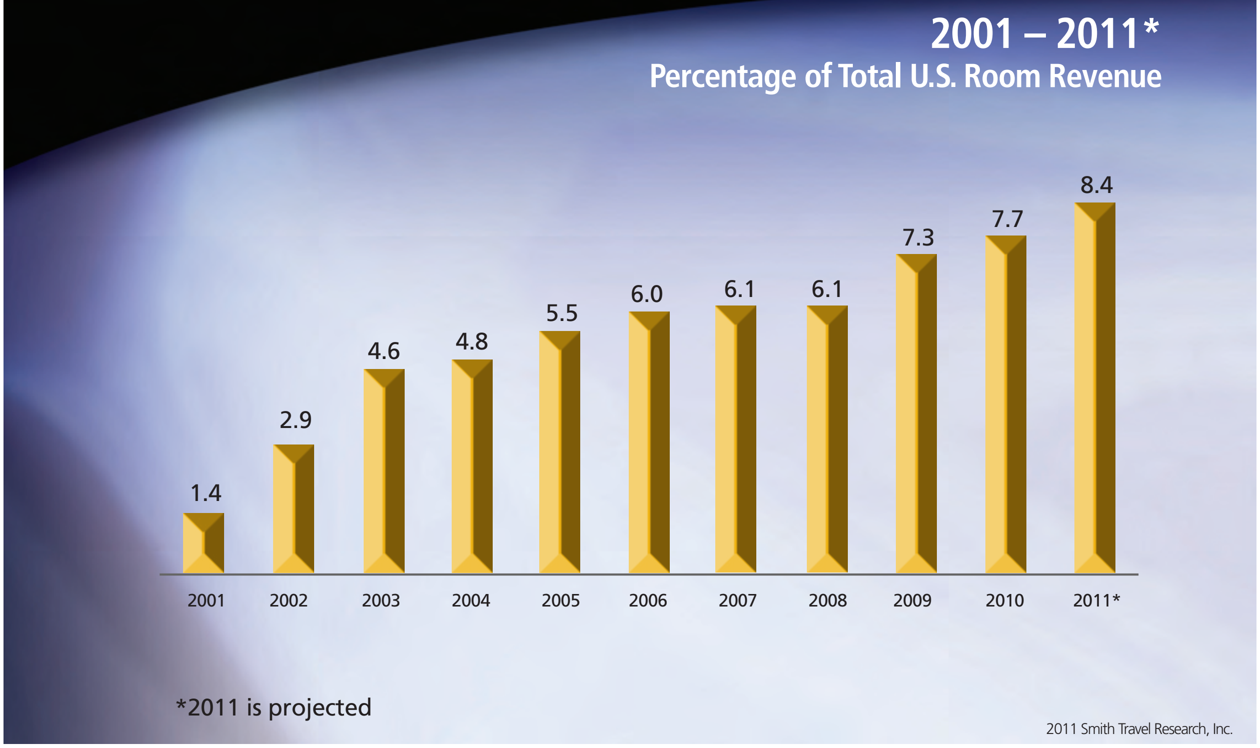
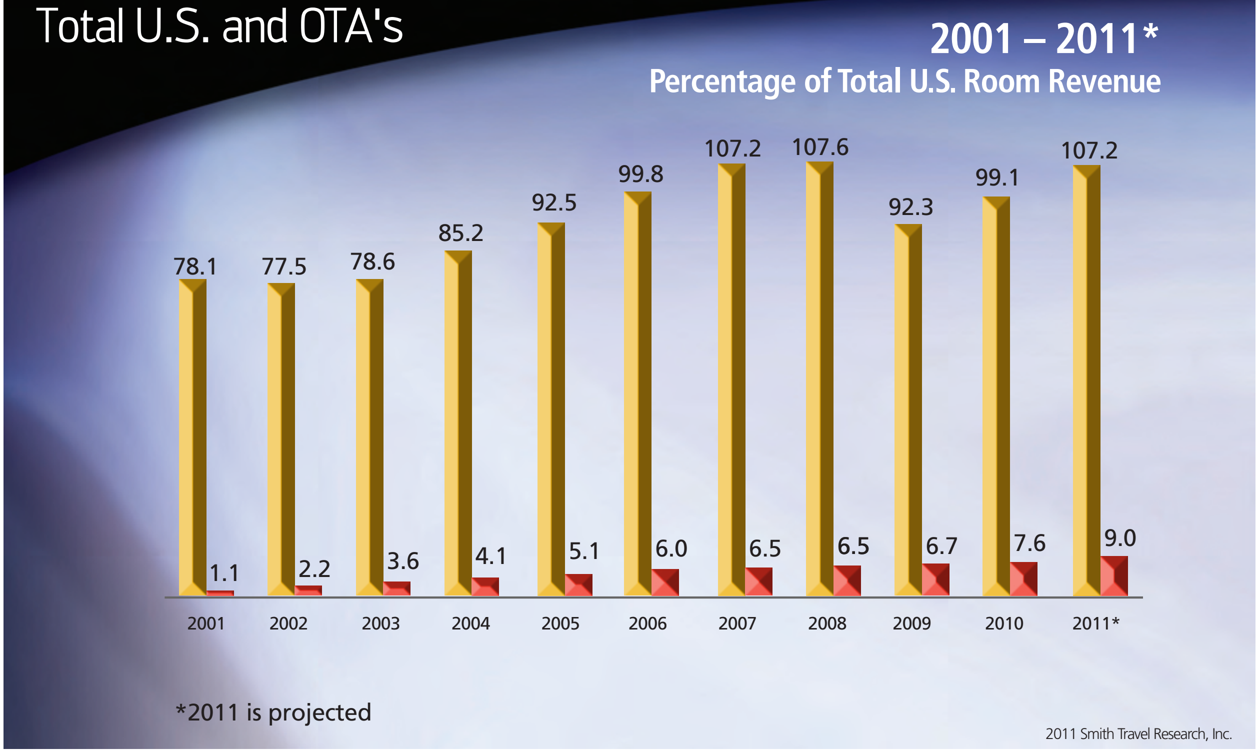
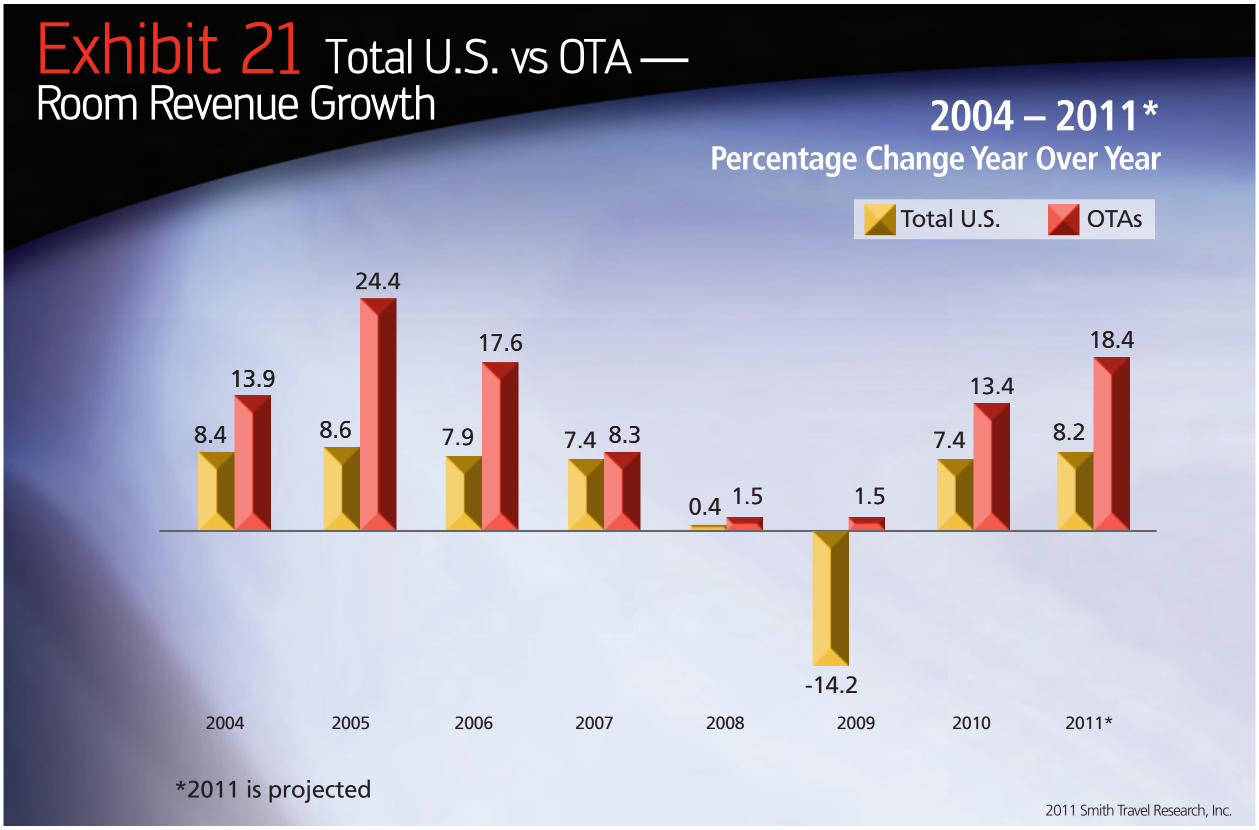


Exhibit 20 Absolute Revenue for Total U.S. and OTA's



increases in the June YTD 2011 time period (see Exhibit 23). Dramatic increases were still evident in the lower priced chain scale segments.

It is of note that despite the declines in share reported by luxury and upper upscale chains, the absolute number of room sold by OTAs for these two hotel segments was either flat or still increasing in 2009 and 2010 (see Exhibit 24). With the increase in demand share it is not surprising that there was a similar rise in absolute demand for the middle and lower priced segments.
The magnitude of growth in the number of rooms sold by OTAs for the economy segment is most easily seen when looking at the June YTD number for 2009, 2010 and 2011 (see Exhibit 25). In 2009, this segment reported that about 4.6 million rooms were booked via this channel as compared to the eight million booked during the first half of 2011. What makes this increase so dramatic is that in 2009 the number of rooms booked into economy hotels was very much in line with most of the other chain scale segments with all except luxury reporting total bookings in the four to five million range .In the first half of that year, the economy segment actually lagged behind both upper upscale and midscale chains in total bookings. Through the first six months of 2011, no other chain scale segment had as many rooms booked by the OTAs channels as did economy chains. In fact, during that time the economy chain scale segment had more than two million more rooms booked by OTAs than any other chain scale segment. With this dynamic at play, it is also not surprising that these chain scale segments would utilize the OTAs more extensively than their higher priced counterparts since the third party intermediaries tend to cater to last-minute-booking customers.



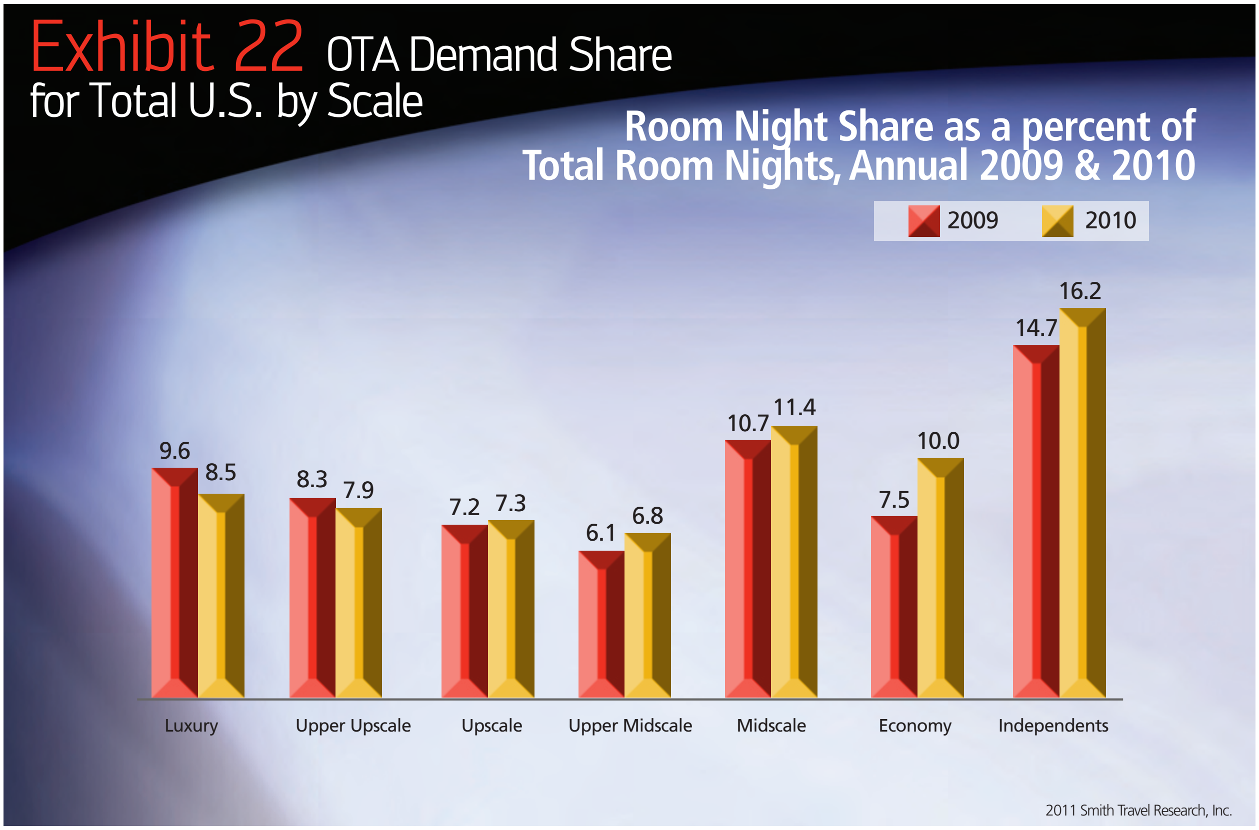


Exhibit 22 OTA Demand Share
for Total U.S. by Scale
Room Night Share as a percent of
Total Room Nights, Annual 2009 & 2010
2009
2010
9.6
8.5
8.3
7.9
7.2
7.3
6.1
6.8
10.7
11.4
7.5
10.0
14.7
16.2
Luxury
Upper Upscale
Upscale
Upper Midscale
Midscale
Economy
Independents
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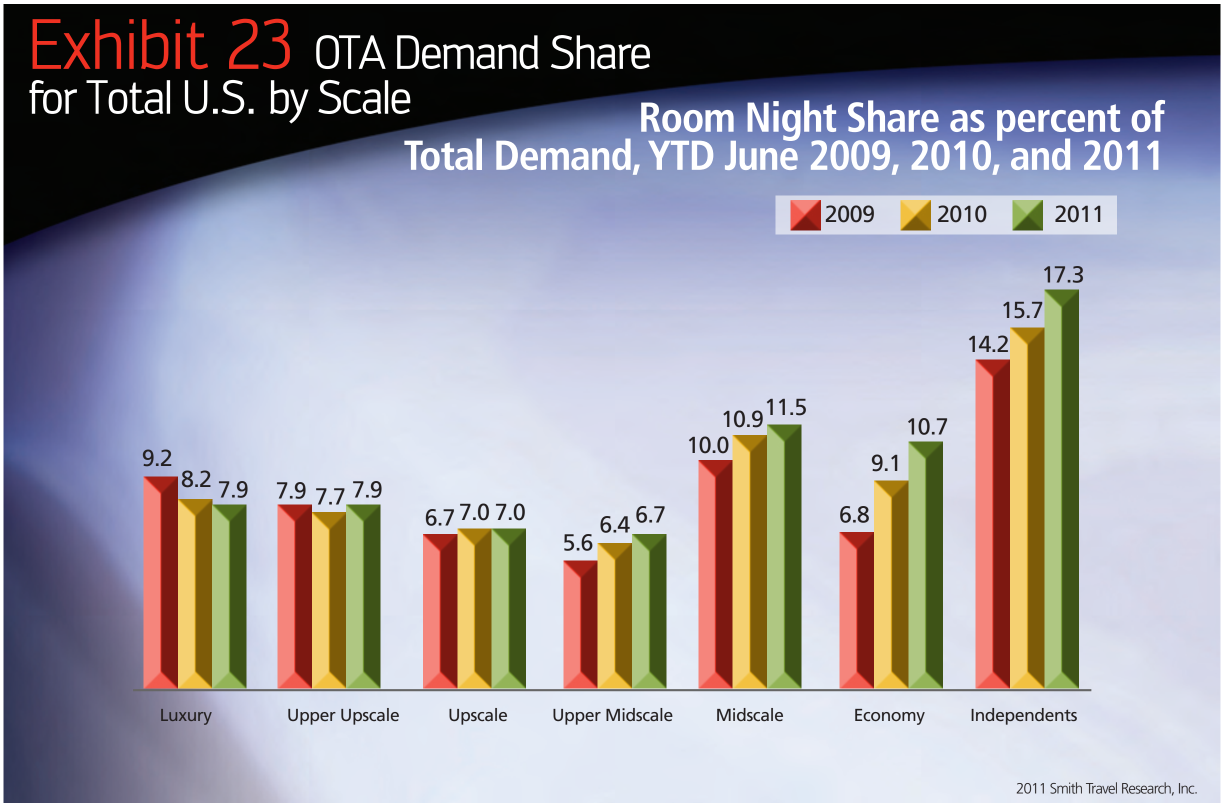
Exhibit 23 OTA Demand Share
for Total U.S. by Scale
Room Night Share as percent of
Total Demand, YTD June 2009, 2010, and 2011
2009
2010
2011
9.2
8.2
7.9
7.9
7.7
7.9
6.7
7.0
7.0
5.6
6.4
6.7
10.0
10.9
11.5
6.8
9.1
10.7
14.2
15.7
17.3
Luxury
Upper Upscale
Upscale
Upper Midscale
Midscale
Economy
Independents
2011 Smith Travel Research, Inc.

One possible reason for this dramatic change in the types of rooms booked through this channel is that the OTA vendors themselves may have altered their strategy. Prior to the economic recovery that began for hotels in early 2010, the primary vendors in this channel seemed to concentrate their sales efforts on both higher end properties and properties in the top 25 metro markets. While this focus served them well for much of the decade it now seems that they have begun to concentrate much more of their attention on the larger but lower priced ADR chain scale segments.

An examination of the OTA-generated room revenue patterns realized by the respective chain scale categories over the same time periods described above is very similar to what was just highlighted for the corresponding demand patterns, as room revenue growth accelerated most rapidly in the lower priced chain scale categories.

Also of note is the fact that each of the three OTA subsets defined above also showed increased activity in both demand and revenue in 2010 (see Exhibit 26). However, a slightly different picture of the evolving nature of consumer bookings is seen when you look at share of total demand and total room revenue in each of those years since there has been significant growth in the retail model. The growth cycle exhibited by each of the OTA models continued into the first half of 2011, with the retail model exhibiting, by far, the largest growth, as shown in Exhibit 27. A more detailed analysis of the three models follows.

OTA — MERCHANT MODEL

This is the most popular of the OTA business models accounting for just over 7% of all room night bookings in the United States in 2010. This was a slight increase over the almost 6.7% booked through this channel in 2009. If the first half of 2011 is any indication, the growth trajectory of demand generated by the OTA merchant model will continue to grow. In 2010, this channel provided the industry with more than 71.7 million room nights, which was up over 14% from the 62.6 million sold the year before.