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Research

Cost controls propelled profits at US hotels in 2017

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Results from CBRE Hotels' Americas Research's "Trends in the Hotel Industry" study show U.S. hoteliers saw revenue growth in 2017 while keeping rising expenses low.

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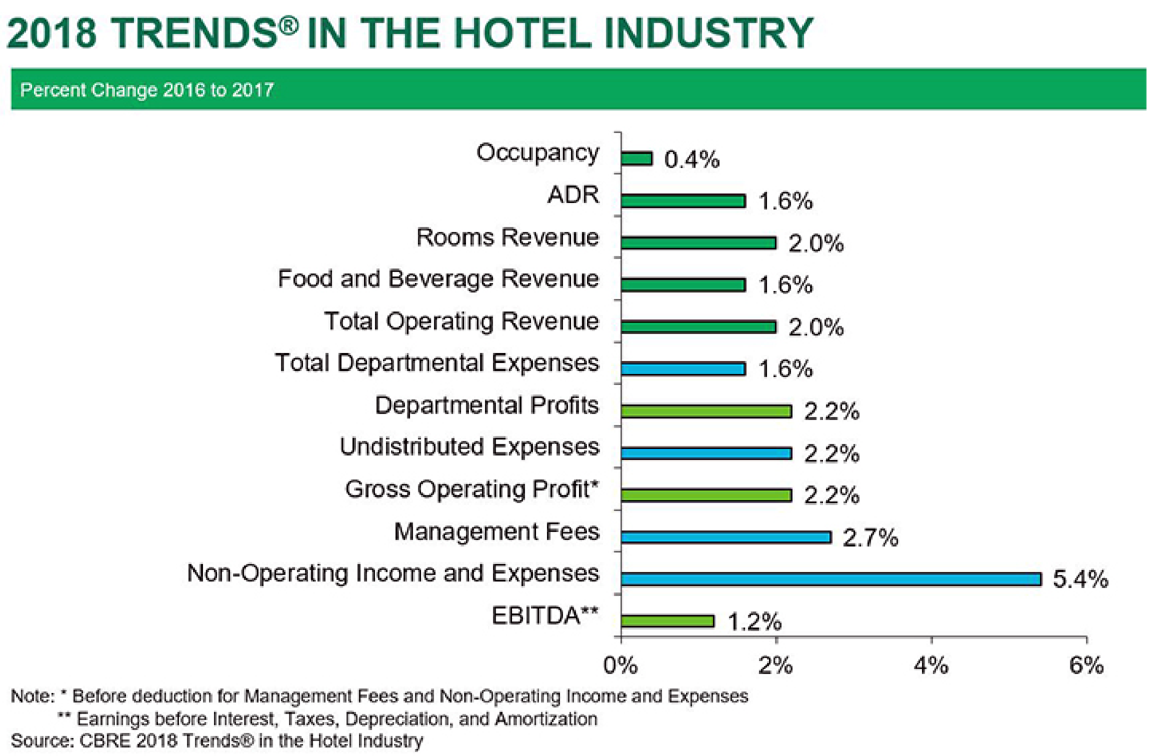
REPORT FROM THE U.S.—Hoteliers in the U.S. enjoyed an eighth consecutive year of increasing profits in 2017 despite another slowdown in the rate of revenue growth.

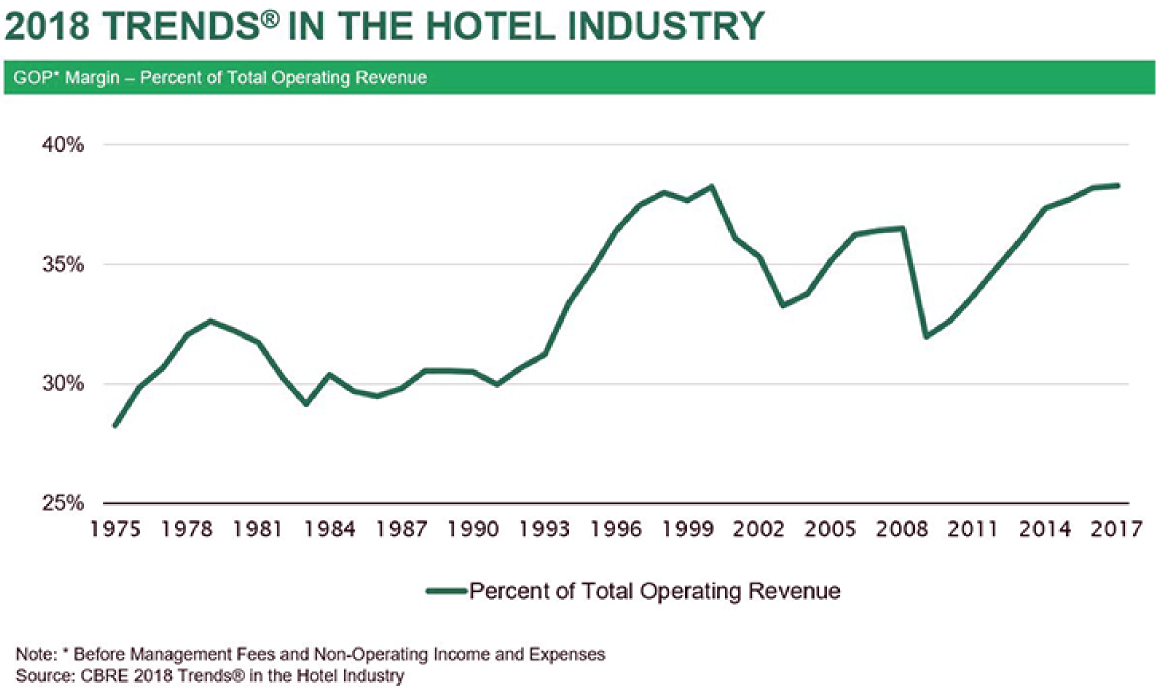
According to the recently released 2018 edition of "Trends in the Hotel Industry" by CBRE Hotels' Americas Research, total operating revenue increased by 2% in 2017 for the average hotel in its survey sample. Fortunately, by limiting the growth in operating expenses to 1.9%, managers at these properties realized a 2.2% increase in gross operating profit for the year.



It is becoming increasingly difficult for U.S. hotels to achieve both revenue and profit gains. Within the survey sample, only 59.1% of the properties enjoyed an increase in total operating revenue in 2017, while just 52.3% attained growth in profits. These are the lowest levels observed since the depths of the recession in 2009. Increasing competition from new supply, muted growth in average daily rates and upward pressure on labor costs make the current operating environment one of the most challenging CBRE has seen since we started tracking industry performance in the 1930s.

Efficient and productive

Over the years, U.S. hoteliers have been able to effectively respond to difficult operating conditions. By matching the 2% gain in revenue with a stingy 1.9% rise in expenses, the GOP margin for the surveyed hotels increased to 38.3% in 2017. This is the highest profit margin recorded by CBRE since 1960 and an indication of superlative operating efficiencies and productivity.



U.S. hoteliers continue to effectively manage labor costs, the largest expense for hotels. The labor market is very tight, especially in the leisure and hospitality industry. According to the Bureau of Labor Statistics, the current level of open jobs in the sector equates to 5.3% of the total personnel currently employed. This is the highest level since 2000 and indicative of the difficulty hospitality managers are having finding qualified employees.

The tight labor market has put upward pressure on industry wage rates. Per the Bureau of Labor Statistics, the average hourly compensation rate for hospitality employees rose 3.8% in 2017. For the hotels in the "Trends" sample, total labor costs—salaries, wages and benefits—increased by 1.8%. This implies a reduction in the number of hours worked. In addition to controlling the schedule, hotel managers gained greater productivity from their staff. With fewer hours, the employees at these same hotels serviced 0.4% more occupied rooms, as well as greater volumes of food-and-beverage revenue.

Overhead concerns

While labor costs continue to be controlled, hotels reported an increase in non-labor related expenses in 2017. During the year, labor costs increased by 1.8%, and all other costs rose by 2%. Some of the greatest increases were observed in the undistributed departments where—in aggregate—expenses grew by 2.2%. Compared to the operated departments, undistributed costs are relatively fixed in nature and therefore less controllable by management.

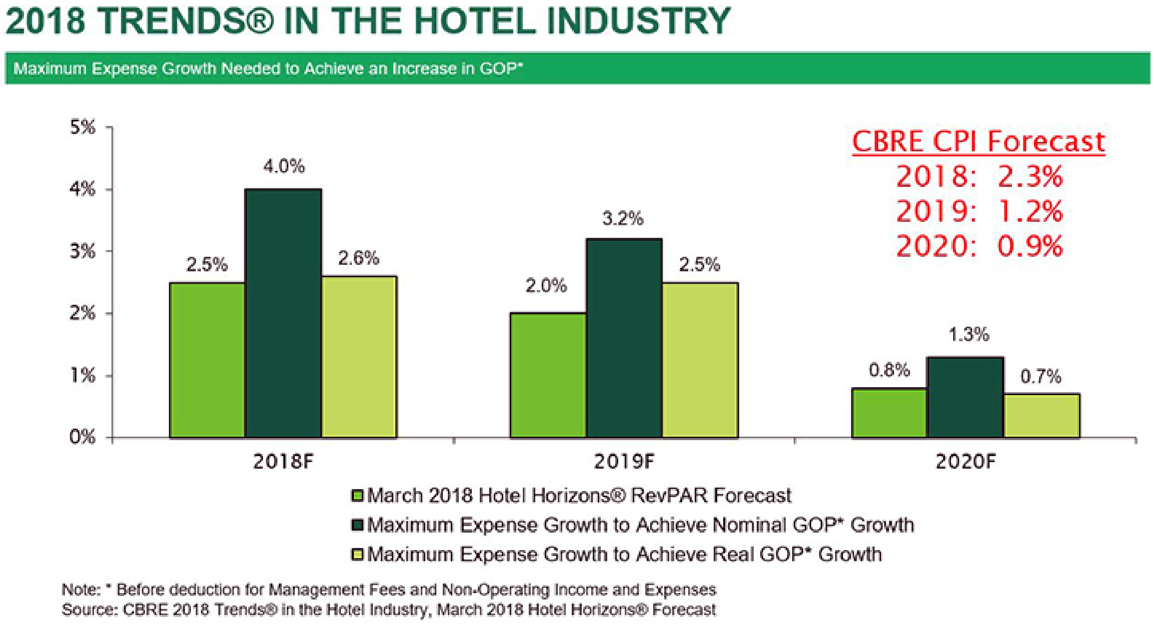
The most obvious cost increase among the undistributed departments during 2017 was utilities, which grew by 1.4%. The 1.4% growth rate is not an alarming increase, but this is the first time since 2013 U.S. hoteliers have not benefited from a decline in utility costs.

There were some non-labor related costs that rose more than revenue in 2017. These include technology-related expenditures, franchise fees, credit card commissions, and the cost of complimentary food, beverage and services. Below GOP, management fees and property taxes also increased at a greater pace than the 2% growth in revenue.

Property owners did find some solace in the 4.2% insurance costs decline in 2017. However, given the number of natural disasters that occurred during the year and the sluggish start to the stock market in 2018, we might see a boost in premiums this year.

Can profits continue to grow?

According to the March 2018 edition of CBRE's "Hotel Horizons" forecast report, annual RevPAR gains for U.S. hotels are projected to range from 0.8% to 2.5% from 2018 through 2020. Given this rate of revenue expansion, can hotels continue to achieve profit growth? For hotels to achieve profit growth that keeps pace with inflation, expense growth must be limited to 2.6% or less over the next few years. Keeping in mind that the annual average expense growth rate since 1960 is 4%, this will be an enormous challenge.



It is a very interesting period for hotel owners. On the one hand, lodging revenues seem comparatively durable, and hotels are achieving record profit margins. On the other hand, a profit growth slowdown amplifies the looming reality that renovation requirements and other capital-intensive needs become more apparent as the current up-cycle persists.

Robert Mandelbaum is Director of Research Information Services for CBRE Hotels' Americas Research. To purchase a copy of the 2018 edition of Trends® in the Hotel Industry report, please visit https://pip.cbrehotels.com/trends.

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