

Don't Touch That Phone!

Competitive Strategy For Resellers of Premise-Based Telecommunications Services

Hoteliers and owners of commercial properties today face an increasingly competitive environment for the resale of telecommunication services to guests and tenants. This strategic planning paper describes several competitive strategies available to hoteliers and property owners when competing for telecom revenues. It assesses the competitive position of hoteliers and owners. It re-examines their calculation of telephone costs, margins, and pricing. It establishes alternate methods for pricing and then measuring telecommunications profitability. This paper introduces the idea of telecommunications revenue yield management as an emerging strategy for hoteliers and property owners.

Don't Touch That Phone!

A Hotelier's Competitive Strategy For Telecommunications Revenue

Don't Touch That Phone!

Face it. Parents are sending their sons and daughters out into the world with cautionary advice like: "And remember now ... don't touch that hotel room phone".

I was humored by a little discovery in my Milwaukee hotel room a couple months back. Next to the telephone sat the guest telephone "rate card". On the rate card, a prior guest had scribbled the word "scam". Evidently, some guests don't listen to their parents anymore. Or maybe hoteliers need to reconsider their competitive assumptions for telephone.

Competition And Its Effects.

Our guests "scam" comment clearly represents a point of view that no brand image-maker could enjoy. Such

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perceptions of telephone rates have the unfortunate effect of both limiting phone use (and therefore revenues) while at the same time labeling the hotelier as a "highway robber".

An implicit assumption here is that this guest will, where possible, choose alternatives to the use of that guest room phone. And such alternatives now exist. The most obvious is the cell phone.

Clearly, your telephone rate structures were mainstream, acceptable, and profitable a few years back. What happened? Maybe the following:

- The price points in the public telecommunications markets have shifted downward in the last ten years. During that time, the gap between hotel, domestic and corporate long distance rates has steadily increased.
- The past decade has seen innovation in telephone pricing models. Cell phones have introduced bulk purchases of call time. Friends and family plans provided

differentiated group rates. Meanwhile, hoteliers remain attached to per call billing under an "AT&T Operator Assist" (or related rate structure) basis for surcharging.

The effect of competition is to make those that are slow to compete look as if they offer a bad deal. Hoteliers look like they are providing a bad deal. Telephone is no longer a captive market for the hotelier. Hoteliers are now competing for guest connectivity revenue. Actually, they have not really yet begun to compete.

The strategic technology in competing for telecom revenues is not the PBX...it's the communications accounting and billing system.

The cell phone business has redefined the business models for telephone. The public has reacted positively to the packaging and pricing in the broader telephone market. Those pricing models have set consumer expectations. And hoteliers have not tracked to those changing expectations, nor have they reacted to the changing pricing models and price points.

And they could not track to them even if they wanted. With maybe one exception in the marketplace, hospitality call accounting vendors have followed a low cost (and subsequently low innovation) product strategy. While traditional carriers consider their billing system the most strategic element of their infrastructure, hoteliers consider their call accounting system to be non-strategic. The call accounting technology possessed today restricts the hoteliers from following the competitive market even if they wanted to. The weapon for competing in telecom is the communications accounting and billing system. And hoteliers and their vendors have under-invested in such technology.

But Why Bother?

One might argue that telephone is becoming a commodity and that competition is rising fast. You might also argue that hotels cannot compete with the fast moving telecommunications world. Others opine about how the telecommunications world has gone "low margin". Such businesses are clearly no fun. Or are they?

Interestingly, it turns out that hoteliers will continue to have several rationales for continuing their resale of guest or tenant connectivity. Why? Because ...

1. The general public continues to demonstrate a willingness to pay usage/access fees for both telephone and Internet. In the converging voice and data world an argument persists, that bandwidth will be ubiquitous and free. But who makes such arguments? Answer: People whose business models thrive on plentiful and cheap bandwidth! (Specifically web portal companies, e-commerce companies, web services companies, network equipment companies, and content or media companies.) Providing free telecommunications access transfers profits up the value chain to carriers and service providers.
2. Are you convinced that your network infrastructure investments are over? Not if history is our guide. Your infrastructure investments will continue. Terminating revenue at a time of rapid evolution (revolution) and instability in network technologies seems premature. More specifically with the growth of voice of internet and video, your network management investments could actually accelerate. Elimination of guest or tenant revenue eliminates your return on investment calculations. Could that stall future infrastructure investments?
3. In giving away guest telecom, hoteliers will not significantly reduce current or future infrastructure costs. You still need to own and operate a phone system. In fact, do you believe that free or cheap telephone rates will increase your guest's phone usage? If you do, then your current phone system and trunk capacity will need to be expanded.

Your costs will actually increase! See the fictional memo below for an illustration.

In giving away or substantially reducing telecom rates, will your costs actually increase?

A memo from the near Future...Is bandwidth usage transferable? What if companies begin transferring their telecom costs to you the hotelier? Would it work?

From: ABC Consulting Travel Department
To: All Employees
Re: Use of Hotel Telephones While Traveling

Please check the telephone policy at your hotel. Some of our preferred travel hotels are now offering free and highly reduced rates for telephone usage. Free is better than any telecommunications rate available to our company. Therefore, please implement these policies while staying at hotels with unlimited long distance.

1. It is now mandatory that you use in-room hotel telephones when traveling at hotel with unlimited long distance. Please note that personal calls are prohibited on company cell phones and otherwise however personal long distance call can be made using the phones in our hotel rooms.
2. Discontinue your use of all company 800 numbers. Dial directly to all corporate numbers including modem dial-up for company services.
3. Discontinue use of your corporate calling cards. All corporate calling cards will terminate in the coming months.
4. Eliminate or curtail your use of cell phones while at hotels. Cell phone group plan minimums will be re-negotiated downward to reflect reduced usage in the coming months. When possible, call people back using landlines.
5. Note that high-speed internet access charges from your hotel room are not expense-able at hotels with unlimited long distance. Use of modems is expected at these hotels.

As a traveling professional, please work to minimize your telecommunications costs by focusing your telecom usage to your hotel rooms.

Please note that we continue to expect that you stay at hotels with competitive room rate and those with preferred pre-negotiated room rates with our company. Telecommunications is itself not a reason for you to select your hotel.

4. Your bandwidth cost is cheap today. But given the health of the telecommunications industry, those rates may or may not remain low. Could your cost of bandwidth from carriers stabilize or even increase given reduced competition and an industry

drive for renewed profitability? Until the industry stabilizes, setting long-term expectations for pricing seems premature.

5. The idea of bundling telephone (and/or internet) service usage costs into the rack rates is not sustainable in a competitive market. When bundled, the hotel up the street that is charging directly for telephone connectivity enjoys a natural room rate advantage. Moreover, despite technology vendor claims that connectivity sells rooms, room rates are more important.

Most importantly, telephone is very profitable because the actual incremental cost of buying phone services is quite low ... if you are viewing your costs from the proper perspective.

Telephone Resale is Profitable

In the land of accounting, it can be said that how you understand your costs will determine how you will understand your profits. This is particularly true today when selling telephone services to guests, visitors, and tenants. There is a reasonable argument to be made that hoteliers have been viewing telephone profits through the wrong lens.

Change Your Definition of Telecommunications Profit. Telephone is not room service. When you do not provide dining and room service, you can forget the kitchen. But, if you do not resell telephone services ... you will still buy and operate the telephone system. Telecom infrastructure (including phone cabling, phone sets, PBX's, and certain services) exists as a necessary asset for both staff and guest reasons. It represents capital investment required even if you did not resell telecommunications to tenants, visitors, and guests. So nobody wonders "hey, should we put phones into our hotel?" It is a moot point.

This reality has one simple effect. Since telecommunication infrastructure represents an asset inseparable from, say, the light fixtures, then the cost of telephone infrastructure (or at least a substantial part of it) need not be a part of your calculation for telephone services profitability. Telephone services become incremental revenue extracted against the total fixed asset of the property. Telecommunications infrastructure costs are, for the most part, not

variable to the resale of guest telephone services.

So how do you calculate telephone profits? Profit is your telephone revenue minus the amortized direct costs of your telephone billing and accounting technology (call accounting) and the variable costs of carrier minutes and trunking purchased to enable those profits. No PBX in the calculation. No phone technician in the calculation. No cabling infrastructure in the calculation. Indeed, there is no longer an independent asset-based return on investment calculation for a telephone system.

This simple change in profitability perspective introduces an important insight. Every carried guest telephone minute can be profitable. The first minute you sell can be just as profitable as the last one. It therefore seems prudent to implement a telecommunications strategy that increases carried minutes and that makes costs variable where possible to the carried minute.

.... create the idea of "yield management for guest room telephone"... a dynamic management of pricing for telecommunications.

This change in profitability perspective also implies that you may have more flexibility in pricing and margins than you previously thought. And this leads to the question; "How can I price and package telephone services to maximize its revenue contribution to my standing investment in this hotel?" This is a yield management question.

Yield Management For Telephone.

With telephone established as profitable and actually reasonably competitive, we can consider the idea of revenue maximization. Yield management presumes the idea that there is an optimal combination of pricing and service bundles from which to maximize profits. Yield management is an emergent idea in filling hotel rooms and is well established for airlines. Yield management presumes that hoteliers adopt a dynamic management style for pricing of telecommunications. It stands in contrast to

today's hoteliers and their largely static view of telecom bundling and pricing.

So let's create the idea of yield management for guest room telephone. You have a fixed number of minutes you can sell over a trunk. Let's figure out how to maximize profits for traffic carried over those trunks (and how to not annoy guests). The starting point for this exercise might be to reconsider some static assumptions about hotel telephone services.

Yield Management Strategy #1 Sell All The Carried Minutes (Not Just Some of Them)

The first question of yield management is; "What are you managing for yield? And if you are managing more of it, can you get more yield?"

The history of telephone system billing has dictated that some calls are free (local and 800) and some cost money (long distance). Of course, long distance revenue essentially funds local service and the telephone infrastructure. Not surprisingly, such an imbalance has created artificially high pricing for long distance carried minutes and subsequently triggered reductions in long distance carried minutes (check out your old economics book for theories on price elasticity of demand if you need convincing of this outcome). Meanwhile, of course, non-revenue carried minutes (local and toll free) are increasing in part anyway because they are subsidized by long distance.

There is a straightforward solution. Charge for every minute of guest phone usage. Examining cell phone pricing methods can be instructive. Cell phones charge for every carried minute using a single integrated pricing structure. They charge for local, long distance, or toll free. They charge for incoming and outgoing carried minutes. The carriers charge based on tiered rate plans with surcharges and special exceptions all over the place in the fine print. But the important starting point is that they charge for all carried minutes. They have more potential yield to manage.

One hotelier of note expressed concern to us that charging for "all" the minutes would raise the ire of their guests. The reason provided was that local calls were free from their home phones. But consider this: you are not competing directly with the home service. You

(like the local exchange carrier) are competing directly with the cellular carrier. The cellular carrier has already made this transition to billable carried minutes for you. And the public has responded positively. Cell phones are setting the expectation for rates. Hotel and home rates are followers. Compete against cell phones (not home phones).

Yield Management Strategy #2 Make Your Pricing Structures Dynamic.

Your competition, the cell phone providers and long distance carriers, need to move a mountain to move a price. They manage in between government regulators and the need to price for entire markets. You can move faster.

You can move a price for any number of competitive reasons; an understanding of guest dynamics, soliciting corporate groups for meeting space events, or some local or regional insights. Move the ability of your sales group to negotiate telecommunications arrangements (within limitations).

Yield Management Strategy #3 Establish Different Pricing Methods For Different Guests and Groups

Telephone rates today are attached to hotels and rooms. If you occupy a room then you pay the phone rates associated with that room. But why? The room in which your guest stays does not define your special relationship with that guest. Amenities and business arrangements are attached to guests more often than rooms! Leading hospitality call accounting systems enable hoteliers to dynamically associate telephone rate plans to specific guests or to specific groups to which that guest is affiliated. Owners of a ski condominium pay a different rate than the renter of that condominium. Employees of a company attending an event pay a different rate than other employees or families vacationing at the hotel. This has interesting implications. It implies that groups can be analyzed for their profitability and that a hotel's sales organization can establish profitable negotiated rates with corporate customers.

Yield Management Strategy #4 Develop Optimized Pricing Structures (That Simultaneously Drive Usage, Profits, and Guest Satisfaction)

Hoteliers typically surcharge telecommunications as a percentage over standard carrier rate tables (like the AT&T Operator Assist rates). These tables made sense back in 1985. They were stable structures, widely understood and accepted, and consistent with guest arrangements on their home telephone.

However, these rates today have a problem for building-based resellers of telephone (aside from the fact that they are no longer stable and not easily understandable). The problem is that they are front-loaded. They aggressively charge guests in the first minutes of the call while the incremental cost per minute falls for longer calls. Hint: brief telephone calls with disproportionately high costs are noticed by parents who share their findings with their kids.

Is a front loaded rate structure most profitable? Would it be wiser for profit and for guest services reasons to back load, mid-load, tier, or flatten your rate structures? Leading hospitality call accounting systems provide the ability to manage customize-able pricing plans. Such systems enables the creation or pricing plans specific to guest demographics and telephone usage behavior that both maximize revenue and operate consistently with guest expectations.

It is easy to say that hotel telephone prices are too high. It is harder to determine which price points maximize profits. Could you reduce telephone rates and thereby increase profits? Likely yes. The question is where is the right price point. And what will it take to overcome the guest expectation that use of the phone will be financially painful.

Yield Management Strategy #5 Negotiate Carrier Contracts To Maximize Carried Minute Profits

Some in the world seek to simplify their carrier contracts. They single-mindedly reduce cost by negotiating low flat per minute rates across a few broad categories of telecom activity. This need not be the singular goal of a contract negotiation. Why? It could be that contracts with marginally higher rates across many contract

jurisdictions can generate greater profitability. This happens when you have negotiated using two approaches.

- ❑ You negotiated hard for your low profit carried minutes and compromised on high margin minutes.
- ❑ You negotiated hard for high volume minutes and compromised on low volume minutes.
- ❑ You negotiated hard for minimum annual commitments and were able manage telecom demand to fulfill those commitments.

Profitability yield management requires the ability to connect the cost of any category of carried minute (as defined in a carrier contract) to its revenue. All of this speaks to systems or processes that aggregate and monitor your telecommunications activity around the structure of your carrier contract.

Yield Management Strategy #6 Demand An ROI From Call Accounting Systems

The enabling technology for pursuing telecommunications yield management-based strategies is the call accounting system. The capabilities of such systems implement yield management strategies.

Conversely, call accounting systems also prevent, delay, or complicate formulation and implementation of a yield management strategy. Why? Because call accounting vendors have not focused on product capabilities that enhance your competitive position. Most call accounting products today have been built first to save you money on their acquisition and installation.

A call accounting solution that installs in 45 minutes can provide a one time upfront savings in time and effort. But this savings may represent a small fraction of the impact costs, effort, and potential profit. A call accounting solution with limited capability to enable yield management establishes a profitability leak that keeps on leaking. Such a leak exists for the life of the system. In addition, it is hard to detect because it is an opportunity lost. Similarly, data accessibility and analytical limitations create ongoing costs filled by process inefficiencies, expanded telecom staffs or teams of consultants offering a range of revenue management and cost management services and reports. These are costs that keep on costing.

Change the method by which you evaluate a call accounting system. Evaluate future call accounting systems for their return on investment (ROI) over two to five years. How will such systems enable a yield management strategy? This evaluation would balance the following against a system's cost:

- How would the system reduce operational process costs?
- How would the system increase carried minutes and their margins?
- How would the system improve your negotiation position with carriers?
- How would the system reduce or eliminate the time and effort to consolidate information for enterprise wide analysis?

Yield Management Strategy #7 Centralize Your Call Accounting.

One structural shift in call accounting emerges quickly as having a significant ROI. That structural change is the operation of a single, central call accounting system. Call accounting vendors have presumed that call accounting is best implemented as a distributed basic on-property stand-alone solution. Delivery of dynamic billing methods across properties is best implemented from a single integrated database (hundreds of little data bases is not easily manageable across hundreds of little properties ... even if the functionality actual existed on those systems and you had remote access). Leading properties are shifting to centrally managed hospitality call accounting solutions. Such solutions enable yield management across multiple properties from a single integrated database.

Competing In Turbulent Times

The days of the boring but stable telecommunications industry are over. And thus, the days of hoteliers managing a static long distance resale business with cheap tools are over. The challenge is clear. How do you integrate the resale of profitable carried minutes into a guest experience? And how do you not become the topic of cautionary conversation between parents and the next generation of travelers? The era of yield management has arrived for telephone revenues.

About the Author

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