REPORT INTO CHANGES TO HOSPITALITY COST STRUCTURES AND RISKS FOLLOWING THE PANDEMIC

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This report was developed from the findings of a research study conducted post the Covid-19 pandemic in 2022. The research study looked at the changes to the hotel industry as a result of the pandemic and how it affected the industry. In total, twenty-two General Managers were interviewed between November 2021 and February 2022. These General Managers were in charge of four- or five-star hotels in nine countries: Switzerland, France, Spain, Malaysia, Hong-Kong/China, Thailand, Dubai, Israel, and Saudi Arabia. The report focuses on changes to hospitality cost structures and risks and the strategies employed by General Managers to ensure the survival of their business.

Adjusting Costs in the Leanest Possible Way: Focus on the Essentials

In countries where governments required hotels to temporarily shut down due to Covid-19 restrictions, executives (the General Managers and his/her executive management team) still had to ensure the property remained fully maintained to prevent assets from deteriorating. For example, this included having staff run hot water regularly through the waterpipes to avoid bacteria forming; cleaning and dusting open-spaces, floors, and corridors; keeping gardens neat and hosed down, or checking the swimming pool regularly. In countries where governments authorised hotels to remain open, executives had to decide whether it made economic sense to do this or to simply shut down. This decision was based on a ***cost-efficiency rationale achieved by switching to a leaner mode of operating.***

"The pandemic has forced us to become more cost-efficient in the way we run our operations. Running the hotel on negative revenues for months has been an opportunity to think of leaner ways of operating the hotel, in order to better prepare for what awaits us in the future."

(General Manager of a five star hotel, Switzerland).

General Managers employed different strategies to become more cost efficient during the period and in the aftermath of the lockdown as will be described in the next sections. They are also considering how to best prepare their hotels for future crises, as explained in the final part of the report.

Cost Cutting Measures Taken During the Pandemic

General Managers were forced to explore different options to ensure cost cutting during the pandemic following a logic of a 'lean approach', resulting in different measures taken, as described below.

Labour Cost Adjustments - this involved adjusting labour costs in response to the evolution of an ever-changing situation (i.e., the evolution of the pandemic and increasing/loosening of government restrictions). For instance, the decision to run the hotel with a reduced staff capacity required restructuring operational teams in line with the hotel's occupancy rate. As such, HR managers had to find the optimal Full-Time-Employment (FTE) number to reduce payroll costs while optimising shift working periods among staff. Some General Managers described a detailed process by which they first decided to cut what they called 'the casual workers.' A secondary step, if necessary, was to then reduce the number of 'interns.' This allowed for some flexibility, given that casual workers and interns could be re-hired once demand went up again (although this was described as being a real cash-flow management exercise). In instances where demand was too low, some General Managers described how they also had their HR department cut the number of 'fixed staff.' Casual workers and interns were not the only staff who were targeted. Executives were not immune to changes wrought by the pandemic. Financial benefits enjoyed by executives such as high salaries and bonuses, were reduced. In addition to relieving hotels from cost burdens, this also sent a clear signal that every employee was expected to make a financial sacrifice.

Leveraging Unpaid Leave - using 'unpaid leave' in order to save on payroll, not only for operational-level staff but also for employees in managerial positions was a second strategy General Managers employed. Reductions in staff salaries broadly varied– ranging from 15% to 50% (in some extreme cases). Wage reduction depended both on country-level work regulations, as well as the number of subsidies that employees received from the government and corporate contractual & HR policies.

Offering Early Retirement – a third strategy was to offer early retirement to some senior employees, particularly when they were no longer considered a good fit for their roles.

The Costs from Staff on Sick Leave or Abusing the System - many hotels found that a significant number of staff went on sick leave (and presented a valid medical certificate) during both the first strain of Covid-19 and later with the emergence of the Omicron variant. This simultaneously forced the remaining staff into taking on a heavier workload and instigated significant costs to recruit temporary staff to replace those on sick leave. Not all sick leave was legitimate, however. Some hotels found their employees were playing the system, which was coined as 'Covid's perverse effect.' Employees knew that if they were found to be coughing or sneezing several times, they would typically be asked to return home and to test for Covid-19 and to remain at home in quarantine until such time as the test results were given. Some employees decided to abuse this system and pretended to feel ill so that they could stay home for a while before receiving their results. Meanwhile their colleagues had to absorb all their work, which often led to staff exhaustion.

Rethinking Facilities Usage - dictated by a reduced number of guests and staff, many General Managers were forced to rethink usage and the opening/closing of the hotel's restaurant(s), bar(s), terrasse(s), SPA, swimming pool, etc. to reduce operational costs to their bare minimum. Further costs were reduced, such as air conditioning, heating, elevator usage, electricity costs, etc. While stocks of perishable goods (adapted to occupancy rate) were also carefully monitored to minimize food waste.

Applying Lean Sales Techniques - hotel chains applied lean sales techniques to optimize revenue whenever a hotel in the chain was closed. This involved negotiating with guests to put them in better rooms in one of the hotels of the group that remained open. However, regardless of whether this solved the problem for the guest, it still represented a cost of negotiating with them. It also put staff who had to deal with often stressed-out guests with high expectations, under emotional pressure to reduce costs while maintaining a high-quality guest service and safeguarding the chain's reputation. Importantly, marketing costs were incurred to attract corporate and leisure guests. For instance, 'loyal guests' were lost due to the pandemic and efforts were made to attract them once again to hotels.

Negotiating Payment Terms - following a cost-efficient lean approach forced executives to rethink ways in which they could lower their fixed costs. In some instances, this was possible by renegotiating contracts with suppliers, or by renegotiating the deadline for the payment of debts, for instance, the possibility of paying in several tranches, deferred in time – for example, in tranches of 25%).

Receiving Government Support to Reduce Costs - in some countries there was financial assistance or support given by the government to pay employee salaries. This aided hoteliers by reducing the fixed salary cost burden significantly. The social charges, however, were still part of the hotel's financial responsibility, so the benefit only went so far to help. However, in Switzerland for example, there were *ad hoc* readjustments of RHT ("Réduction Horaire de Travail" – a reduction in working hours) i.e., reimbursement of a percentage of the RHT to the State. There were also administrative costs related to applying for RHT, due to some restaurants abusing the system, resulting in the government asking for the signature of staff when the hotel applied for RHT. Additionally, the payment of unused vacation days to staff were a problem as they represented sunk costs as these vacation days had not been taken.

Reviewing Contractual Rights & Obligations - some General Managers reflected that they should have taken a closer look at their staff's contractual rights and obligations. This would have given the General Managers the flexibility of putting employees on furlough again, depending on how travel demand would evolve (for example if the high season had not been busy). The rationale behind this was to optimize *when* to reincorporate employees into their operations and when to stand them down. The flexibility in firing and re-hiring staff depended on increase/decrease of demand – representing a 'lean' approach. In addition, in some hotels, changes were made to staff remuneration systems shifting from a variable 'service charge' to a fixed salary system. This did result in happier staff.

Optimizing Timing of Hotel Re-Openings - other GMs mentioned that they waited too long to re-open the hotel. They wished they (or top management of the group their hotel belongs to) would have re-opened the hotel earlier. Others even expressed that at the group/chain-level, it would have been wiser to reopen the hotels at a slower pace, to optimize the process of re-opening, rather than doing everything at once and too quickly and not being able to offer a full service or a service that did not meet expected quality standards.

Finally, Hygiene & Safety protocols were supported by costs related to material and systemized processes (i.e., setting-up sanitizers, masks, systematic disinfection of surfaces in rooms, etc.).

Post-Lockdown Staff Shortages and Recruitment Cost Implications

After lock-down, there were significant staff shortages in all hotel operations. In some cases, 40% of fixed staff did not return to work as they had left the industry for more stable work elsewhere. This added significant costs to hotels and had two consequences:

1. This 'stretched' current employees who had to take on a heavier workload.
2. To rapidly replace the 40% who left, General Managers had to be less selective and hire 'less competent' people, resulting in additional lost time for permanent staff to train less competent staff (the cost of training relates to the time it takes to train 'less competent' staff meaning that the permanent staff wastes valuable time in its operations).

Losses of staff were across the board and included F&B, housekeeping, Restaurants/Bars, Kitchen, Chefs, and Reception. This shortage led to large opportunity costs, as there was insufficient staff to fulfill demand in the cleaning of hotel rooms, serving/cooking in the restaurant, etc.

General Managers identified two solutions to overcome the shortages:

1. Moving from fixed costs to variable costs through outsourcing.
2. Remote online training.

Moving from Fixed Costs to Variable Costs - some activities which were usually supported by fixed costs (for example, inhouse cleaning staff) were outsourced to run more optimally as variable costs. For instance, one solution was to hire a cleaning company that employed ten members of staff compared to the hotel's twenty members of housekeeping staff. At the same time, permanent staff were paid an adequate salary (fixed costs) in order for them to stay and not leave the hotel.

Offering Remote Online Training - a further solution involved providing remote online training for staff to keep them up-to-date operationally. In other cases, to allocate staff resources efficiently to operational areas where they were most needed, some staff were sent off as a 'task force' to a resort (a project) to work. The rationale behind this was to set the resort up before it could open after Covid-19.

Future Cost Measures

As well as the measures they had to take to reduce and manage their costs during the pandemic, General Managers also have an eye on the future and how adaptable they need to be. Various strategies are being considered to remain agile in the face of changing circumstances.

Creation of Strategic Clusters – clustering functions and positions into 'strategic clusters' can create cost synergies. This also has the benefit of fostering knowledge and experience sharing. There are two identified approaches to achieve this:

1. Several hotels from the same chain could share the same Heads of Department who will oversee Reservations teams, Sales & Marketing teams etc., located in different hotels. In other words, the Head of Department has a larger geographical oversight than a single property and is able to share best practice and ideas across various properties.
2. Merging different functions into one department, for example, call center and maintenance could be combined, or F&B, Bakers and Butchery functions could be clustered together.

Use of Digital Technologies for Operations – hotels should apply technology to streamline operations by using artificial intelligence, chatbots, and other automation tools. Increased use of QR codes for menus or at check-in/out. While these costs are initially high, in larger establishments with a high number of restaurant covers or guest arrivals/departures, hotels benefit from economies of scale as they save time with staff, printing costs and from an F&B perspective, gives more flexibility to change menu options. Another point to add was to accelerate the implementation/usage of digital communication such as Microsoft Teams which reduces hotel staff's travel costs, particularly when travelling across for a hotel group. However, technology does come at a high cost and there was a question over whether smaller independent hotels could survive, possibly being bought out by larger chains more able to invest.

Recruitment and Remuneration – there are two aspects to this. The first is recruitment – with many people leaving the industry, recruitment costs are likely to continue to increase, particularly when travel is incurred to job fairs. The second is the need to rethink the remuneration schemes on offer. In some hotels, staff travel across borders where they can live cheaper in one country while earning more in another. When travel bans were put in place, local talent were not interested in the level of pay offered to work in hotels as their cost of living was higher than what was on offer. It was also considered by General Managers that in the future it will become more difficult to recruit competent staff who have more options. If the pool of talent reduces, then less competent staff will need to be recruited thus driving up training costs. One suggestion was to outsource some activities and operations and keep a smaller number of permanent staff on the roster but pay them better.

Initiatives to Managing Future Risks

Although the pandemic seems to be on the wane, General Managers are still reflecting on the lessons they can take forward to better manage risk and any likelihood of further pandemics or global crises. Initiatives General Managers are considering implemented into their regular routines include:

- Keeping abreast of the news and tracking issues is an important habit to develop.
- Follow the evolution of the stock value of the hotel chain (where relevant) as this gives an understanding of how investors/the market perceive the strength of the brand and its ability to bounce back or bounce forward (transform threats into opportunities).
- Developing agility in forecasting and planning, particularly over last-minute booking and cancellations and how to best manage cashflow risk, alongside cancellation and refund policies. Any future crisis may not lead to government support and General Managers will have to consider how they can manage without this support. One possibility is to consider insurance, although this has additional costs that may not make it worth it.
- Focus on customer segmentation to ensure that marketing and offers attract different segments. For example, some hotels were able to shift focus to different customer segments that they had otherwise not attracted by rethinking the offer i.e., from international guests to domestic/local. Similarly, focusing on different markets who are able to travel.
- Managing suppliers during slow-downs or production stoppages. General Managers need to consider how to manage the risk of finding new suppliers or re-engaging with existing suppliers for any future crises.

In Conclusion

Although the Covid-19 pandemic hit the hospitality industry hard, many General Managers learned useful lessons to prepare for any future crises. Interviewees in the sample focused on how they could best manage their costs by applying various strategies. As a result, they became more agile and built resilience in the face of adversity.

As the world returns to a post-pandemic ‘normality’ and particularly with the uplift in travel and leisure, it will be easy to simply return to pre-pandemic ‘business as usual’ ways of thinking and operating. This, however, would be unwise. General Managers should try to continue to flex their muscle in maintaining the efficiencies and flexibility they have been able to develop. Additionally, taking a step back and rethinking recruitment, remuneration and ways of working would be prudent in the face of the difficulties experienced by the hospitality industry.