



SMITH TRAVEL RESEARCH

## Rate Cutting: A look at Canada

By Jason Wight - HVS Canada

As we have now passed the halfway mark of 2009, we can begin to see the impact that the global recession has had on the Canadian lodging industry. On a weekly and monthly basis, we continue to see declines in occupancy and RevPAR, and now, increasingly, average room rate. Cutting rates to get "heads in beds" does not stem the decline in demand but instead magnifies the decline in RevPAR. The performance of various markets in Canada bears witness to this truth.

### A Really Short-Term Solution

Despite the constant talk about learning from the past downturn and the long-lasting effect that rate cutting has on the hotel industry, Canadian hotels have started to discount room rates, and we are now seeing rates decline across the nation. So, if we know that cutting the average room rate does not induce demand, why are hotels cutting rates? It comes down to market share. Hotels are shifting their approach from maintaining average rate to protecting and increasing market share by discounting, hoping to take demand from their competitors to increase occupancy and revenue. Although this may prove to work in the short term, it ultimately forces the competitors to take the same measures, resulting in rate wars that undermine every competitor.

In her article, "Avoid a lose-lose pricing position", Cathy Enz compares this rate

dilemma to game theory. In summary, the comparison demonstrates that competing hotels are better off if they maintain their rates. If one competitor drops its rate, it is a win-lose situation, but the winner will only benefit in the short term until the loser is forced to drop its rate, at which time they are both back at comparable rates, just lower, which ends up being a lose-lose situation.<sup>1</sup> This starts a downward room-rate spiral in which everyone is trying to obtain the short-term benefit of having the lower rate. The lower the average rate goes, the longer the road of recovery becomes, which completely nullifies the short-term benefit of having the lower rate.

When weighing occupancy vs. average room rate, it is also important to consider the costs associated with increasing occupancy. If the average rate is raised, that increase goes directly to the bottom line. Increasing occupancy possibly generates more revenue in the short term, but it also increases operating expenses, so the full amount is not realized at the bottom line. Therefore, it is more beneficial to the bottom line to maintain the average rate than it is to sacrifice rate for occupancy.

Since the last downturn in 2001 to 2003, the hotel industry claimed to have learned that cutting rates does not bring new demand into the market. There was even an extensive study done by The Center

for Hospitality Research at Cornell University in partnership with Smith Travel Research in 2004 titled "Why Discounting Doesn't Work", which confirmed this fact. The report clearly demonstrated that discounting among competitors did not induce demand into a market but rather captured market share from the competition.<sup>2</sup>

Going into this recession, there were many recommended strategies on how to add value for potential guests as an alternative to discounting rates. The value-added strategies benefit both hotels and guests. Hotels would be able to maintain their average rates, and guests would receive amenities or services that would normally be an additional charge. The industry now appears to be turning away from these strategies in favour of rate cutting, a technique that has time and time again proven to be counterproductive.

The Canadian hotel industry maintained its rate integrity until March 2009, but in April Canada posted negative ADR growth of -0.92%, and continued on this downward trend to -2.53% year-to-date through June. Although Canada as a whole posted its first average rate decline of the year in April, individual markets across Canada started to experience average rate decreases at different times. The average rate in the Toronto Downtown market started to decrease as early as November 2008, and the most recent markets to start

## Rate Cutting: A Look at Canada (Cont'd)

trending downward in average rate are Ottawa and Alberta North.

### Comparisons Throughout Canada

Looking at the performance of various markets throughout Canada in the first half of 2009, it is clear that cutting rates does not improve demand but seriously erodes RevPAR. The table shown includes major markets throughout Canada and their performance year-to-date through June for both 2008 and 2009. The markets are displayed in order of percent change in average rate.

supply, causing the occupancy to decrease only 8.65% to 63.4%. When comparing average rate performance, Edmonton managed to increase its rate by 1.11%, whereas Toronto Downtown slashed its rate by -13.59%. The resulting percent change in RevPAR for Edmonton was -10.65%, and the percent change in RevPAR for Toronto Downtown was -21.06%. The drastic reduction in average rate in the Toronto Downtown market resulted in a RevPAR decline double that of Edmonton despite both markets experiencing the same decline in demand. Rate cutting clearly does not pay.

cooperation will help position a market area for a strong recovery once demand starts to grow again. Once the average rate drops, it is extremely hard to build it back to the same level. Depending on the severity of the decrease in average rate, it can take up to five years to grow rates back to where they were. We need to remember that dropping the room rate does not induce new demand into a market. In the various Canadian markets, dropping rates did not increase the demand in any market area, but those that managed to hold rates steady fared better in RevPAR performance. We are in a very difficult

Canadian Operating Performance: June YTD

	Occupancy			Rate			RevPAR			Supply	Demand
	2009	2008	% Change	2009	2008	% Change	2009	2008	% Change		
Regina/Saskatoon	64.8 %	67.8 %	(4.42) %	\$117.35	\$108.12	8.54 %	\$76.04	\$73.31	3.72 %	2.7 %	(2.0) %
Winnipeg	66.0	69.7	(5.31)	109.62	108.12	1.39	72.35	75.36	(3.99)	0.0	(5.3)
Edmonton	65.3	73.3	(10.91)	125.79	124.41	1.11	82.14	91.93	(10.65)	3.4	(7.8)
Ottawa	66.9	69.9	(4.29)	137.49	137.75	(0.19)	91.98	96.29	(4.48)	2.6	(1.7)
Alberta North	45.7	61.0	(25.08)	147.86	149.96	(1.40)	67.57	91.48	(26.14)	4.3	(21.8)
<b>Canada</b>	<b>53.0</b>	<b>57.9</b>	<b>(8.46)</b>	<b>115.98</b>	<b>118.99</b>	<b>(2.53)</b>	<b>61.47</b>	<b>68.90</b>	<b>(10.78)</b>	<b>1.4</b>	<b>(7.2)</b>
Halifax	59.9	65.0	(7.85)	121.31	126.18	(3.86)	72.66	82.02	(11.41)	3.5	(4.6)
Calgary	63.3	70.1	(9.70)	145.88	153.80	(5.15)	92.34	107.81	(14.35)	(0.2)	(9.9)
Vancouver Downtown	65.6	74.0	(11.35)	154.10	164.00	(6.04)	101.09	121.36	(16.70)	2.1	(9.5)
Montreal Downtown	55.5	58.0	(4.31)	136.70	151.25	(9.62)	75.87	87.73	(13.52)	2.2	(2.2)
Toronto Downtown	63.4	69.4	(8.65)	148.16	171.46	(13.59)	93.93	118.99	(21.06)	0.9	(7.8)

Source: STR and HVS

The Edmonton and Toronto Downtown markets are interesting to compare because, although they are located on different sides of the country, they both experienced a -7.8% change in demand. Because demand declined at the same rate in both markets, these markets are positioned to reveal the effect of rate cutting on RevPAR. Since Edmonton had a 3.4% increase in supply, occupancy in the Edmonton market declined 10.91% to 65.3%. Toronto Downtown, on the other hand, experienced a 0.9% increase in

### Going Forward

So what should we be thinking about going forward? First of all, we need average rate to stop declining. Dropping rates magnifies the decrease in RevPAR, which the decreases in demand are already affecting. Operators can't control the global economy and the impact that it has on demand, but with the cooperation of all the competing hotels they can control room rates. Although it might not seem beneficial during these times to work together with competing hotels,

operating environment right now, but the industry's ability to hold room rates will determine how quick the recovery will be when the economy turns around. There is a strong correlation between growth in GDP and lodging demand, so if the Bank of Canada is correct in calling the end of the recession, then declining demand should come to an end sooner rather than later.<sup>3</sup>

#### Footnote:

1. Cathy Enz, "Avoid a lose-lose position." *Hotel News Now* (April 19, 2009), Retrieved August 14, 2009, from <http://www.hotelnewsnow.com/Articles.aspx?ArticleID=988&print=true>
2. Cathy A. Enz, Linda Canina, and Mark Lomanno, "Why Discounting Doesn't Work: The Dynamics of Rising Occupancy and Falling Revenue among Competitors." *The Center for Hospitality Research at Cornell University* (2004).
3. Jim Butler, "Hospitality Lawyer: The "amazing relationship" between GDP and hotel room demand. When the recovery comes, what will it look like for the hotel industry?" *Hotel Law Blog*, July 27, 2009. Retrieved on August 4, 2009, from [http://hotellaw.jmbm.com/2009/07/hotel\\_demand\\_and\\_gdp.html](http://hotellaw.jmbm.com/2009/07/hotel_demand_and_gdp.html).

July 2009	Number of Rooms	Occupancy Rate (%)		Average Room Rates (in \$CAD)		RevPAR (in \$CAD)		Room Supply % chg	Room Demand % chg
		2009	2008	2009	2008	2009	2008		
Nova Scotia Area	1,378	69.9%	65.3%	\$109.68	\$109.64	\$76.67	\$71.59	0.9%	8.0%
Halifax, NS	4,184	77.3%	74.8%	\$134.13	\$132.93	\$103.68	\$99.43	3.6%	7.2%
Montreal Downtown	10,315	70.8%	73.1%	\$137.64	\$143.12	\$97.45	\$104.62	3.1%	-0.1%
Montreal Area	2,361	57.4%	58.3%	\$104.68	\$103.44	\$60.09	\$60.31	0.0%	-1.6%
Quebec City, QC	4,027	79.4%	85.8%	\$154.21	\$186.92	\$122.44	\$160.38	0.0%	-7.5%
Quebec Area	4,466	66.5%	62.3%	\$131.54	\$135.72	\$87.47	\$84.55	0.0%	6.7%
Toronto Downtown	14,508	70.3%	74.6%	\$133.41	\$153.79	\$93.79	\$114.73	1.1%	-4.7%
Toronto North/East	6,748	63.8%	69.8%	\$105.77	\$115.86	\$67.48	\$80.87	1.4%	-7.4%
Toronto Airport/West	8,492	53.6%	60.8%	\$97.91	\$108.83	\$52.48	\$66.17	3.4%	-8.9%
Ottawa, ON	7,161	64.6%	67.8%	\$123.53	\$126.30	\$79.80	\$85.63	2.6%	-2.3%
Ontario East	4,784	63.8%	67.8%	\$114.20	\$115.47	\$72.86	\$78.29	1.4%	-4.5%
Windsor/ Ontario SW	2,709	49.6%	55.3%	\$109.51	\$113.67	\$54.32	\$62.86	-2.0%	-12.1%
London/ Kitchener	2,965	49.9%	53.9%	\$94.82	\$101.97	\$47.32	\$54.96	0.0%	-7.5%
Ontario North/ Thunder Bay	2,369	73.6%	76.2%	\$97.11	\$97.20	\$71.47	\$74.07	1.0%	-2.4%
Ontario NC/ Sudbury	4,813	65.6%	68.3%	\$117.98	\$121.65	\$77.39	\$83.09	4.6%	0.4%
Niagara Falls, ON	9,431	78.4%	81.7%	\$156.28	\$162.11	\$122.52	\$132.44	0.2%	-3.8%
Ontario Central	3,954	61.3%	61.9%	\$115.15	\$116.50	\$70.59	\$72.11	2.7%	1.7%
Mississauga, ON	4,597	62.0%	67.1%	\$100.57	\$108.56	\$62.35	\$72.84	-1.5%	-9.0%
Winnipeg, MB	3,493	65.4%	66.6%	\$106.50	\$107.17	\$69.65	\$71.38	0.0%	-1.8%
Regina/Saskatoon, SK	2,454	68.9%	63.4%	\$113.96	\$111.27	\$78.52	\$70.55	3.2%	12.2%
Calgary, AB	8,658	75.5%	79.8%	\$164.12	\$180.82	\$123.91	\$144.29	0.3%	-5.1%
Edmonton, AB	9,041	65.8%	71.9%	\$120.37	\$127.48	\$79.20	\$91.66	2.3%	-6.4%
Alberta North Area	3,918	53.1%	71.0%	\$162.31	\$183.24	\$86.19	\$130.10	5.1%	-21.3%
Alberta South Area	8,200	63.3%	72.1%	\$154.49	\$173.30	\$97.79	\$124.95	1.9%	-10.5%
Vancouver Downtown	8,268	81.4%	85.4%	\$168.07	\$193.31	\$136.81	\$165.09	1.6%	-3.1%
Vancouver/ Burnaby Area	2,071	70.5%	81.1%	\$125.23	\$137.05	\$88.29	\$111.15	4.9%	-8.9%
Richmond-Surrey/ East Area	3,993	70.5%	80.2%	\$120.45	\$133.81	\$84.92	\$107.32	0.0%	-12.1%
British Columbia Area	5,875	62.3%	67.0%	\$130.33	\$145.24	\$81.20	\$97.31	0.2%	-6.8%
Kamloops/ Kelowna Area	4,432	71.0%	75.2%	\$131.83	\$133.86	\$93.60	\$100.66	0.3%	-5.3%
Vancouver Island	4,400	73.3%	77.5%	\$142.71	\$153.57	\$104.61	\$119.02	2.2%	-3.4%
<b>Provinces</b>									
Alberta	31,377	64.3%	72.7%	\$140.51	\$152.19	\$90.35	\$110.64	2.3%	-9.4%
British Columbia	30,597	69.0%	75.1%	\$130.10	\$140.69	\$89.77	\$105.66	1.1%	-7.1%
Manitoba	4,383	62.4%	63.2%	\$98.58	\$93.46	\$61.51	\$59.07	0.1%	-1.1%
New Brunswick	4,754	68.7%	72.0%	\$116.46	\$112.94	\$80.01	\$81.32	1.0%	-3.6%
Newfoundland	1,833	83.2%	74.7%	\$118.84	\$120.78	\$98.87	\$90.22	0.5%	12.0%
Nova Scotia	5,562	72.7%	69.4%	\$123.01	\$123.43	\$89.43	\$85.66	2.0%	6.8%
Northwest Territories	204	INS	INS	INS	INS	INS	INS	INS	INS
Ontario	79,378	62.1%	67.2%	\$114.58	\$120.95	\$71.15	\$81.28	1.5%	-6.1%
Prince Edward Island	793	76.4%	76.9%	\$131.92	\$129.51	\$100.79	\$99.59	0.0%	-0.6%
Quebec	26,575	66.2%	68.7%	\$124.12	\$130.77	\$82.17	\$89.84	1.0%	-2.6%
Saskatchewan	6,611	71.0%	72.3%	\$106.25	\$97.45	\$75.44	\$70.46	2.0%	0.1%
Yukon Territory	784	71.5%	78.7%	\$112.05	\$111.56	\$80.12	\$87.80	0.0%	-9.1%
Canada	192,851	66.1%	70.0%	\$122.88	\$129.18	\$81.22	\$90.43	1.4%	-4.4%

July 2009 Year-To-Date	Number of Rooms	Occupancy Rate (%)		Average Room Rates (in \$CAD)		RevPAR (in \$CAD)		Room Supply % chg	Room Demand % chg
		2009	2008	2009	2008	2009	2008		
Nova Scotia Area	1,378	47.5%	51.5%	\$96.39	\$94.21	\$45.79	\$48.52	1.6%	-6.3%
Halifax, NS	4,184	62.5%	66.4%	\$123.63	\$127.30	\$77.27	\$84.53	3.5%	-2.6%
Montreal Downtown	10,315	57.8%	60.2%	\$136.99	\$149.80	\$79.18	\$90.18	2.3%	-1.9%
Montreal Area	2,361	50.3%	53.8%	\$104.73	\$105.83	\$52.68	\$56.94	0.3%	-6.2%
Quebec City, QC	4,027	58.6%	67.5%	\$134.06	\$152.24	\$78.56	\$102.76	0.0%	-13.1%
Quebec Area	4,466	54.2%	54.9%	\$133.64	\$137.41	\$72.43	\$75.44	-0.1%	-1.3%
Toronto Downtown	14,508	64.3%	70.1%	\$145.65	\$168.48	\$93.65	\$118.10	0.9%	-7.3%
Toronto North/East	6,748	54.1%	61.2%	\$111.72	\$120.11	\$60.44	\$73.51	1.4%	-10.3%
Toronto Airport/West	8,492	58.1%	67.0%	\$111.43	\$117.93	\$64.74	\$79.01	3.1%	-10.5%
Ottawa, ON	7,161	66.6%	69.6%	\$135.51	\$136.11	\$90.25	\$94.73	2.6%	-1.7%
Ontario East	4,784	50.9%	54.1%	\$105.69	\$105.38	\$53.80	\$57.01	0.6%	-5.4%
Windsor/ Ontario SW	2,709	49.9%	53.0%	\$114.04	\$108.68	\$56.91	\$57.60	7.6%	1.4%
London/ Kitchener	2,965	52.8%	56.1%	\$100.99	\$105.45	\$53.32	\$59.16	0.0%	-5.9%
Ontario North/ Thunder Bay	2,369	63.8%	64.3%	\$94.35	\$93.84	\$60.20	\$60.34	0.1%	-0.7%
Ontario NC/ Sudbury	4,813	50.5%	55.3%	\$105.85	\$105.44	\$53.45	\$58.31	3.4%	-5.6%
Niagara Falls, ON	9,431	51.8%	53.7%	\$130.23	\$135.64	\$67.46	\$72.84	-1.2%	-4.5%
Ontario Central	3,954	49.7%	54.3%	\$110.05	\$112.02	\$54.69	\$60.83	2.6%	-6.1%
Mississauga, ON	4,597	55.1%	61.3%	\$105.85	\$111.05	\$58.32	\$68.07	-1.9%	-11.8%
Winnipeg, MB	3,493	66.0%	69.3%	\$109.14	\$107.98	\$72.03	\$74.83	0.0%	-4.8%
Regina/Saskatoon, SK	2,454	65.5%	67.2%	\$116.47	\$108.55	\$76.29	\$72.95	2.7%	0.1%
Calgary, AB	8,658	65.1%	71.5%	\$149.01	\$158.22	\$97.01	\$113.13	-0.1%	-9.1%
Edmonton, AB	9,041	65.5%	73.9%	\$124.73	\$125.17	\$81.70	\$92.50	3.3%	-8.5%
Alberta North Area	3,918	46.8%	62.4%	\$149.99	\$155.53	\$70.20	\$97.05	4.5%	-21.6%
Alberta South Area	8,200	52.3%	59.2%	\$137.56	\$142.87	\$71.94	\$84.58	2.3%	-9.7%
Vancouver Downtown	8,268	67.9%	75.7%	\$156.47	\$168.85	\$106.24	\$127.82	2.0%	-8.5%
Vancouver/ Burnaby Area	2,071	60.3%	71.5%	\$115.53	\$119.99	\$69.66	\$85.79	2.6%	-13.4%
Richmond-Surrey/ East Area	3,993	62.9%	72.8%	\$117.97	\$124.02	\$74.20	\$90.29	0.7%	-13.1%
British Columbia Area	5,875	55.7%	61.3%	\$159.32	\$175.66	\$88.74	\$107.68	0.5%	-8.8%
Kamloops/ Kelowna Area	4,432	51.1%	56.3%	\$110.10	\$110.51	\$56.26	\$62.22	0.3%	-8.9%
Vancouver Island	4,400	60.9%	65.7%	\$117.75	\$122.88	\$71.71	\$80.73	1.9%	-5.5%
<b>Provinces</b>									
Alberta	31,377	57.8%	66.0%	\$130.30	\$133.42	\$75.31	\$88.06	2.4%	-10.4%
British Columbia	30,597	56.5%	63.4%	\$121.88	\$127.91	\$68.86	\$81.09	1.2%	-9.9%
Manitoba	4,383	59.3%	63.0%	\$94.40	\$90.60	\$55.98	\$57.08	0.1%	-5.7%
New Brunswick	4,754	50.5%	54.9%	\$108.67	\$108.93	\$54.88	\$59.80	2.4%	-5.8%
Newfoundland	1,833	70.4%	65.4%	\$111.51	\$113.24	\$78.50	\$74.06	0.5%	8.3%
Nova Scotia	5,562	55.1%	57.2%	\$113.71	\$116.55	\$62.65	\$66.67	2.4%	-1.3%
Northwest Territories	204	56.6%	60.6%	\$147.65	\$144.98	\$83.57	\$87.86	0.0%	-6.6%
Ontario	79,378	53.7%	58.7%	\$114.34	\$119.86	\$61.40	\$70.36	1.3%	-7.3%
Prince Edward Island	793	44.0%	43.0%	\$98.21	\$96.75	\$43.21	\$41.60	-0.3%	2.1%
Quebec	26,575	54.0%	58.8%	\$119.84	\$127.95	\$64.71	\$75.23	1.3%	-6.9%
Saskatchewan	6,611	65.1%	65.6%	\$105.34	\$96.82	\$68.58	\$63.51	1.5%	0.8%
Yukon Territory	784	56.5%	56.4%	\$100.49	\$99.59	\$56.78	\$56.17	-1.5%	-1.3%
Canada	192,851	55.0%	59.9%	\$117.10	\$120.85	\$64.41	\$72.39	1.4%	-6.8%

**DEFINITIONS**

Occupancy:	Rooms sold divided by rooms available.
Room Revenue:	Total room revenue generated from the sale or rental of rooms.
Average Daily Rate (ADR):	Room revenue divided by rooms sold.
Room Revenue Per Available Room (RevPAR):	Room revenue divided by rooms available (occupancy times average room rate will closely approximate RevPAR).

*If you have any questions regarding this publication please send a message to [bmacdonald@hvs.com](mailto:bmacdonald@hvs.com)  
Web Site: <http://www.hvs.com>*

*The Canadian Lodging Outlook is a joint publication of Smith Travel Research and HVS, Vancouver and Toronto, Canada. If you wish to reprint any of the articles presented through HVS's website, prior permission from HVS and the respective article's author must be granted. For further information please contact [info@hvs.com](mailto:info@hvs.com). Hospitality Valuation Services, HVS and HVS logo are registered service marks.*



Vancouver Office  
Suite 400 - 145 West 17th Street  
North Vancouver, BC  
Canada BC V7M 3G4  
(604) 988-9743  
(604) 988-4625 fax

Toronto Office  
6 Victoria Street  
Toronto, ON  
Canada M5E 1L4  
(416) 686-2260  
(416) 686-2264 fax

**HVS** is the leading consulting and appraisal firm specializing solely in the hospitality industry. **HVS** personnel have university degrees in Hotel Administration, or actual hotel work experience, and are taking further courses of study to obtain recognized real estate designations. **HVS** has consulted for over 10,000 hotels in 55 countries.

For a complete list of consulting and valuation offices [click here](#).



**SMITH TRAVEL RESEARCH**

STR provides information and analysis to all major Canadian and U.S. hotel chains. Individual hotels, management companies, appraisers, consultants, investors, lenders and other lodging industry analysts also rely on STR data for the accuracy they require. With the most comprehensive database of hotel performance information ever compiled. STR has developed a variety of products and services to meet the needs of industry leaders.

OFFICE:  
735 E. Main St.,  
Hendersonville, TN 37075  
(615) 824-8664



**HOTEL ASSOCIATION OF CANADA INC.**

The Hotel Association of Canada is a federation of provincial and territorial associations, hotel chains and suppliers with a mandate to represent members nationally and internationally and to provide cost-effective services that stimulate and encourage a free market accommodation industry.

OFFICE:  
Anthony Pollard,  
1206-130 Albert Street,  
Ottawa, Ontario K1P 5G4  
(613) 237-7149