GOPPAR, A DERIVATIVE OF REVPAR!

By Elie Younes and Russell Kett *March 2003*

Hotel managers, operators, investors, and analysts typically now use RevPAR as a basis for their hotel performance measure and analysis. This widely used measure reflects the guest rooms revenue on a per room basis, thereby monitoring the success or otherwise of the hotel's rooms inventory management. Hoteliers aim to maximise RevPAR by means of an occupancy and average rate trade off. Rooms revenue makes up a large portion of total revenue. Typically, full-service three- to five-star hotels derive about 50-65% of their revenues from rooms. Budget and extended stay hotels with limited additional facilities make up to 90% of their revenues from rooms.

While RevPAR is one of the most recognised and used performance measures in the hospitality industry, providing general market trends and some revenue indications, there are some pitfalls to be aware of when analysing a hotel's performance based solely on RevPAR.

This article shows the major pitfalls of RevPAR, and elaborates on the advantages of using a complementary performance measure, GOPPAR (Goh-Par).

RevPAR

RevPAR, or rooms revenue per available room, is calculated by dividing a hotel's net rooms revenue (after discount and sales taxes and net of breakfast or other meals) by the total number of available rooms or by multiplying a hotel's average daily room rate (ADR) by its occupancy.

Rooms Revenue (£)		Number of Rooms		Number of Days per year		RevPAR (£)
2,555,000	/	100	/	365	=	70

Average Rate (£)		Rooms Occupancy		RevPAR (£)
100	x	70%	=	70

Pitfalls of RevPAR

- ***Revenue Mix***: In some instances, rooms revenue accounts for no more than 50-55% of total revenue. These include hotels with substantial food and beverage (and meeting and conference) operations. In such cases, RevPAR would only reflect a portion of a hotel's revenue performance, disregarding all other sources of incremental revenues. This will result in an inaccurate analysis when comparing hotel performances. For example, Hotel X has an average rate of £70, 70% occupancy, and 100 rooms. Other departmental revenues (including food and beverage and other operated departmental revenues) for Hotel X are £500,000. On the other hand, let's assume that Hotel Y has the same size and average rate as Hotel X, but an occupancy level of approximately 60% and other departmental revenues of £1,000,000. While the RevPAR of Hotel X is approximately 15% higher than that of Hotel Y (£49 compared to £42), Hotel Y has higher total revenue than Hotel X; £2.28 million for Hotel X compared to £2.5 million for Hotel Y. If the two hotels have similar direct expenses (say 35% of revenues), and the quantum of overheads is the same for the two hotels, Hotel Y would end up making more money than Hotel X, despite having a poorer RevPAR;

- ***Size*:** RevPAR tends to penalise a larger hotel, when compared to a smaller property. Common sense suggests that it is often easier to have higher occupancy percentages in a 100-room hotel than in a 200-room hotel, especially when there are seasonal peaks and troughs (or even fluctuation between weekday and weekend occupancy levels). Consequently, the revenue per available room of a large hotel is likely to be lower than that of a smaller hotel, given similar market conditions. Therefore, hoteliers and potential investors need to consider the size of a hotel property when comparing the RevPAR performance of a specific hotel in relation to other hotel properties. It is not improbable that, due to economies of scale and incremental revenues, a large hotel has a healthier financial performance than a smaller hotel with a higher RevPAR. After all, hoteliers do not take RevPAR or percentages to the bank!

- ***Value Implications**:* Hotel values are typically based on net free cash flows rather than total revenues. While RevPAR is somewhat related to a hotel's value, it is not necessarily adequately correlated to the income capitalisation value of a hotel property. However, it can be said that *changes* in hotel values are often highly correlated to *changes* in RevPAR (reflecting an elastic relationship).

GOPPAR

GOPPAR, or gross operating profit per available room, is defined as total gross operating profit (GOP) per available room per day, where GOP is equal to total revenue less the total departmental and operating expenses. The following table illustrates the computation of GOPPAR.

Table 1 GOPPAR Illustration (£)

	Hotel A	% Total	Hotel B	% Total	Hotel C	% Total	Hotel D	% Total
Number of Rooms	**200**		**200**		**100**		**100**	
Number of Days in Historic Period	365		365		365		365	
Number of Rooms Available/Year	73,000		73,000		36,500		36,500	
Occupancy	70%		76%		70%		75%	
Average Rate	100		95		100		100	
RevPAR	**70**		**72**		**70**		**75**	
Revenues								
Rooms	5,110,000	64 %	5,270,600	72 %	2,555,000	67 %	2,737,500	65 %
Food and Beverage	2,000,000	25	1,200,000	16	750,000	20	1,000,000	24
Other Departments	850,000	11	900,000	12	500,000	13	500,000	12
Total Revenue	**7,960,000**	**100**	**7,370,600**	**100**	**3,805,000**	**100**	**4,237,500**	**100**
Departmental Expenses								
Rooms	1,022,000	20	1,054,120	20	638,750	25	684,375	25
Food and Beverage	1,200,000	60	720,000	60	487,500	65	650,000	65
Other Departments	400,000	47	423,000	47	250,000	50	250,000	50
Total Departmental Expenses	**2,622,000**	**33**	**2,197,120**	**30**	**1,376,250**	**36**	**1,584,375**	**37**
Total Undistributed Expenses	**1,600,000**	**20**	**1,600,000**	**22**	**900,000**	**24**	**900,000**	**21**
Gross Operating Profit	**3,738,000**	**47 %**	**3,573,480**	**48 %**	**1,528,750**	**40 %**	**1,753,125**	**41 %**
GOPPAR	**51**		**49**		**42**		**48**	

While GOPPAR does not indicate the revenue mix of a hotel property, and therefore does not allow an accurate evaluation of the rooms revenue department, it does provide a clear indication of a hotel's profit potentials. Furthermore, GOPPAR can, in most cases, better reflect the profitability, management's efficiency, and underlying value of hotel properties, as a whole.

Advantages of GOPPAR

- *Revenue Mix:* Since GOPPAR reflects the underlying operating profit of a hotel; it provides a clearer indication of the overall performance or cash flow potentials of a hotel property. Hotel companies, investors, valuers and developers can therefore evaluate hotel management's performance based not only on rooms revenue, but on total revenues and operating efficiency on a per unit basis;

- *Size:* GOPPAR accounts for all operating expenses, most of which include both fixed and variable portions. The fixed portion is mainly associated with the size and requirements of a hotel, while the variable portion relates to the volume of business attributed to the hotel. While a larger hotel will undoubtedly incur higher operating expenses than a smaller hotel, given similar market conditions, a smaller hotel is likely to have higher expenses **on a per available room basis** (due to the economies of scale of a larger hotel). For example, if a 400-room hotel incurs energy expenses of £175,000 per year (£437 per available room), a 200-room hotel in the same city may typically incur energy costs of £100,000 (£500 per available room). GOPPAR provides excellent performance measurements for hotels, regardless of size. While a smaller hotel can sometimes benefit from a higher RevPAR (because it is more effective in optimising occupancy and room rate), its operating expenses **per room** are likely to be higher than those of a larger property;

- ***Value Implications:*** Hotel values are based on net free cash flows or EBITDA (earnings before interest, taxes, depreciation and amortisation). GOPPAR has a greater and more reliable correlation with a hotel's value than RevPAR. We conducted a linear regression analysis between a hotel's value per room, RevPAR and GOPPAR. On a random sample of 30 (profitable) hotels our analysis indicates that, on a per room basis, GOPPAR has a direct correlation of between 85% and 90% with a hotel value, while RevPAR has a correlation of approximately 70% to 75% with a hotel's value. GOPPAR provides a more reliable measure for hotel valuations when compared to RevPAR, and should therefore be used as a more reliable basis for 'quick and dirty' hotel investment analyses. A high RevPAR does not necessarily imply a high bottom line and thus a high value; while a high GOPPAR reflects a high bottom line as well as a more reliable indication of value for the property.

The Trick!

It should be noted that GOPPAR is highly sensitive to any fluctuation in RevPAR. The profit margin of the rooms department is significantly higher than that of any other typical revenue generating department. Therefore, a slight fluctuation in RevPAR can have a significant effect on GOPPAR and, consequently, the underlying value of a hotel. In Table 2, we assume a 5% decline in both occupancy and average rate for Hotel C, resulting in a decline in RevPAR of approximately 10%. In addition, let's assume a decline of 2.5% in other revenues and that departmental expenses will fluctuate in relation to the volume of business. The GOPPAR for Hotel C therefore drops by approximately 16%, from £42 to £35.

Table 2 RevPAR Conversion to GOPPAR – Hotel C (£)

	Normal	% Total	10% Decline in RevPAR	% Total	% Change
Number of Rooms	100		100		—
Occupancy	70%		66.5%		-5 %
Average Rate	100		95		-5
RevPAR	**70**		**63**		**-10**
Revenues					
Rooms	2,555,000	67 %	2,305,888	66 %	-10
Food and Beverage	750,000	20	727,500	21	-3
Other Departments	500,000	13	485,000	14	-3
Total Revenue	**3,805,000**	**100**	**3,518,388**	**100**	**-8**
Departmental Expenses					
Rooms	638,750	25	622,590	27	-3
Food and Beverage	487,500	65	472,875	65	-3
Other Departments	250,000	50	242,500	50	-3
Total Departmental Expenses	**1,376,250**	**36**	**1,337,965**	**38**	**-3**
Total Undistributed Expenses	**900,000**	**24**	**900,000**	**26**	**0**
Gross Operating Profit	**1,528,750**	**40 %**	**1,280,423**	**36 %**	**-16**
GOPPAR	**42**		**35**		**-16 %**

The RevPAR conversion into GOPPAR is high (almost a one to one relationship), so a slight fluctuation in RevPAR could have an even more significant effect on GOPPAR. Therefore, analysts should not solely rely on one measure when analysing a hotel property (or a portfolio of hotels), and should regard GOPPAR as a complement to RevPAR.

Conclusion

RevPAR indicates the performance of a hotel in terms of rooms inventory management and provides some general market trends; however, it provides no cost indication of a hotel property and therefore how much money it is actually – or could be – making. On the other hand, GOPPAR provides a deeper indication of a hotel's profitability by taking into consideration management control and efficiency, and eliminating, to a certain extent, the potential advantage of a smaller hotel. In addition, GOPPAR offers an overall more robust performance measure, especially when comparing the financial performances of hotels with different sizes or in different markets. Furthermore, GOPPAR has a significant correlation with a hotel's bottom line and thus its underlying value. The use of GOPPAR as a complement to RevPAR for hotel performance analysis will therefore enable a more robust basis for hotel investment appraisal than relying solely on RevPAR.

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