



Report on the Potential for Developing Hotel Rooms in Little Chadwick

(Information in this report is valid only for the current game)

Introduction

With no overnight accommodation available in the village at the start of the first quarter, there is considerable scope for the pubs to make a profitable investment in hotel rooms, particularly given their proximity to Bluecoat Hall, the Handside Business Park and the Van Guessens Agricultural College.

Pubs converting upstairs rooms can expect a substantial initial outlay of cash, followed by additional revenues and costs on an ongoing basis.

Initial Outlay

Guest rooms cost £10,000 each to convert from the pubs' upstairs rooms. This is treated as an item of 'Capital Expenditure' meaning that the cost is spread out over (in this case) 10 years. You still have to pay the builders and the furniture stores £10,000 in one go, but the cost only hits your profit at the rate of £1,000 per year for the next 10 years. This is known as a depreciation charge and this way of accounting makes the cost of guest rooms rather more manageable. The room will be sitting on your company's Balance Sheet and the depreciation charge will appear amongst your pub's overheads.

Sales – hotel rooms

The main benefit from your rooms will of course be the revenue you get from selling them. More accurately, you are not selling your room – you're just letting someone borrow it for the night in return for a fee. This means that whereas the 'gross profit' on your drink and food sales is the difference between what you sell the stock for and what you paid for it, your hotel sales will all go into your hotel gross profit (as you're not giving your customers any stock). You will of course have to clean the room and heat it but these are overheads that get taken off later.

Your hotel sales figure will depend on two things – the number of rooms you have and the level of occupancy you achieve.

Like all items of capital expenditure, guest rooms take half a quarter to convert. So in the quarter that you order your room it will be available for 45 nights. In subsequent quarters it will be available for 90 nights. Once converted, these rooms cannot be 'unconverted'!

Factors affecting Occupancy

Your occupancy is the number of rooms you sold as a proportion of the number of rooms you had available to sell. For example, if you have four guest rooms in your pub, you have (4 x 90 =) 360 rooms to sell over the quarter. If you sell 216 rooms, your occupancy would be

$$216 / 360 = 0.6 \text{ (or 60\% , as occupancies are expressed as a \%)}$$

Your occupancy will depend on four factors:

Seasonality

You'd expect your occupancy in the summer to be 15-20 **percentage points** higher in the summer than in the winter; spring and autumn occupancies will be somewhere in between. Note: that doesn't mean you might sell 20% fewer rooms in winter – it means that your occupancy may fall from 50% to 30% (which, though a fall of 20 percentage points, is a fall of 40% in rooms sold – because 20/50 is 40%).

Price

Customers will compare your prices to your rivals'. It won't be a big factor for everyone but you do need to keep an eye on what the other pubs are charging.

Environment

Your occupancy is likely to be improved by refurbishment programmes, advertising, building a function room, providing a decent car park and offering good food. Your occupancy is likely to be reduced by loud music, discos, karaoke and adult entertainment.

Diminishing Returns

There will come a point where converting new rooms doesn't really improve things much. A seventh room, for example will cost as much as the others but will get used only when the other six are full. If you do convert rooms you will need to decide when to stop converting them!

Sales of food and drink to overnight guests

There is considerable scope for making additional money from customers who stay overnight in your pub.

The number of these customers (or 'sleepers') is of course higher than the number of rooms you sell, since many of the rooms will be sold to couples, especially in the summer when more of the sleepers are tourists. In fact, in the summer the average number of guests per room sold is about 1.75, in the spring and autumn it is about 1.5 guests and, in the winter, it is about 1.25.

In the winter, about 90% of those staying in the pub can be expected to dine there (provided food is offered in the evenings). In the spring and autumn this drops to about 80%. In the summer, the warmer weather means visitors may wander further away and only about 70% will dine where they're staying.

The average spend per head (before drinks) could be anything between £8.00 and £21.00, depending on food quality and margins.

Overnight guests average about 1 drink per evening.

Additional Costs

There will be an additional wage cost of between £2 and £3 for each room sold. Cleaning costs will be between £0.50 and £1.50 per room sold. Energy costs will average over the year at about 20p per room sold. Laundry costs will average about £1.50. Repairs will also increase. A cost per room sale of around £6.00 would be a reasonable working estimate.

The depreciation charge of £250 per room per quarter is unrelated to how many times the room is sold.

Tying Up Cash

There will always be a downside to tying up more cash in a business. You are currently being charged interest by your company for any cash you have invested in improving your pub. In assessing the advantages of building guest rooms, you will have to allow for this interest cost.