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Is premium pricing strategy a viable option to pursue higher revenue performance? A case study of relative pricing strategy in the Singapore lodging market

Xiaorong Chen
University of Nevada, Las Vegas

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Xiaorong Chen

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Abstract

Is premium pricing strategy a viable option to pursue high revenue performance? A case study of relative pricing strategy in the Singapore lodging market.

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Xiarong Chen

Dr. Billy Bai, Examination Committee Chair
Associate Professor
Tourism & Convention Administration Department, College of Hotel Administration
University of Nevada, Las Vegas

This is an exploratory research paper on how relative pricing affects an individual hotel's revenue performance in the Singapore lodging market. First, it measures the REVPAR effects for both a discounting and premium pricing strategy at a local hotel against its competitive set. The findings conclude that a premium pricing strategy is a better way to improve REVPAR performance due to the inelastic nature of the demand curve for hotel rooms in the Singapore market. The findings also show that there is a price limit to a premium pricing strategy, beyond which the growth of REVPAR stagnates because customers were willing to seek for alternatives in the market. Second, the study concludes that pricing strategies have little impact on guest satisfaction levels or customer loyalty as long as service standards were maintained. In fact, customers were willing to tolerate increased pricing up to a limit for high standards of service. This paper therefore recommends that premium pricing be adopted as a strategy by mid-tier hotels to increase REVPAR performance in both good and bad economic times.

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Part one

Introduction

Revenue management has been practiced in the lodging industry for more than twenty years(Kimes; 1989; Lieberman, 1993). Good revenue management exists when hotel rates and occupancy are positively correlated. In other words, hotels should increase the rate to capture the revenue opportunity when demand is high; conversely with a weakened demand, hotels should lower the price in order to fill the rooms. Indeed, pricing is one of the most critical factors that contribute to the bottom line.

Recent studies (Canina & Enz, 2004, 2005, 2006a, 2006b, and 2008) regarding competitive pricing focused on the price movement between individual hotels and their direct competitors in a particular market. The comprehensive study collected data from more than 6,000 hotels in the United States from 2001 to 2006. Canina and Enz (2008) found that hotels made more money when they had comparatively higher prices and didn't undercut competitors by discounting rates to fill rooms. In another study, Canina and Enz (2006a) suggested that consumers who purchased hotels in Asia markets were less motivated by discount prices. As these studies spanned huge geographical regions in both economic good time as and bad, these findings offered valuable insights for strategic pricing decisions at an industry level. However, there is limited research regarding how relative pricing could impact the individual hotel performance and how these findings could enhance revenue management.

The hotels in Singapore market enjoyed stable occupancy and constant revenue growth in the past ten years (STRGlobal, 2010). They have benefited from a comparatively stagnant hotel room supply and steady growth of visitors. However, the total room supply will be increased by about 25 % in five years time (Singapore statistics Bureau, 2010). In addition, the fast growing Online Travel Agents (OTAs), popularity of Meta search engines and travel review websites offer customer wider choices and accessibility in terms of hotel products. These changes will lead to more competitive landscape in the hotel industry in Singapore. Therefore, hotels will need to focus on their efforts on revenue management.

This paper was an exploratory study of competitive pricing practice at one Singapore hotel. It looked into how relative pricing can be analyzed and utilized at property level. The paper evaluated the hotel performance by analyzing the relationship in terms of relative occupancy, relative ADR and relative REVPAR from 2006 to 2009. As guest satisfaction and customer loyalty are critical factors that influence the revenue performance (Chaudhuri & Holbrook, 2001; Myung, Barrash & Feinstein, 2006; Peters, 1986, Zeithamel & Bitner, 1996), the paper also explored how price strategies affects guest satisfaction and loyalty during the same period of time. The revenue measures such as relative ADR, occupancy and REVPAR was sourced from independent consultancy firm of Smith Travel Research (STR). Guest Satisfaction Score (GSTS) index was obtained from the largest consumer research firm TNS Global. The remaining data was from the selected hotel of the case study.

Purpose

The main purpose of the paper was to understand the importance of relative pricing strategies and how they impact the hotel performance in a particular market. It looked into whether the hotel that charges a lower price relative to its competitive set gains relatively greater customer demand/occupancy. The study also examined how the demand will behave when the hotel charges a higher price than its rivals. More importantly, it evaluated how relative pricing strategies impact the overall revenue performance, that is, whether the hotel would benefit more by charging higher or lower price than its direct competitors.

In addition, the paper attempted to use quantitative measures to access the response of the pricing strategy from the customer's point of view. The relationship between relative ADR, GSTS and loyal customers' buying behavior was studied. This paper highlights the importance of service quality and customer loyalty to support successful pricing decisions that enhance the revenue performance.

Justifications

The study focused mainly on the relationship between price, occupancy and how it impacts hotel revenue performance in relation to its competitive set. Recommendations are made based on the historical data analysis. It assumes that the hotel had a constant competitive set for the period of the study. It further assumes that this competitive set did not vary its business mix and hence the ADR is more reflective of the retail price as explained in the methodology. However, pricing strategy is a complex issue which involves more than relative pricing. Other important factors such as the changes in distribution channels, business mix, and the capability of revenue managers are not elaborated in this paper.

Constraints

Due to the limited access to other hotel's data, only one hotel was studied. Therefore, the conclusion may only benefit hotels of a similar class and market position.

Part two

Introduction

One of the primary objectives of this paper is to explore the relationship amongst relative ADR, occupancy and REVPAR. The literature review focused on price elasticity of demand, segmentation, pricing strategies and revenue performance measures. The review also focused on literature regarding service quality and customer loyalty, and how price decisions affected guest satisfaction and customer loyalty.

Literature Review

The concept of revenue management originated in the airline industry in the mid – 1980s (Cross, Higbie, & Cross, 2009) and was successfully implemented (Baker & Collier, 1999). The car rental industry (Geraghty & Johnson, 1997) and the hotel industry (Baker & Collier, 1999) subsequently adopted it successfully. As a result, the definition of revenue management may vary according to the various industries' perspective (Kimes; 1989; Lieberman, 1993; Orkin, 1988; Sieburgh, 1988). Quite often, the terms of revenue management and yield management are used synonymously.

Pricing is one of the most important aspects in revenue management and studies have been done comprehensively in the academic field. Hotel pricing literature reveals insight into some factors influencing hotel pricing strategies. These influences include price elasticity to demand (Choi & Mattila, 2004), the importance of segmentation in relation to price (Strauss & Frost, 1999, p 10), pricing strategies (Enz 2003; Canina & Enz, 2004; 2005; 2006a; 2008) and revenue performance measures (Aaker, 2001; Berger,1997; Enz et al., 2003; Joni ,2006; Jeffrey & Barden, 2000; Marris, 1992, p 346). Last but not least, the literature also addressed the importance of service quality and customer loyalty in relation to price, to support successful pricing strategies (Cadotte & Turgeon, 1998; Cotter & Herrinton, 2007; Danziger *et al.*, 2006; Kandampully & Suhartanto, 2003; Iglesias & Guillen, 2004; O'Neill, Mattila & Xiao, 2006).

Price elasticity of demand.

Price elasticity of demand (PEOD) refers to the quantity demand of a good or service in relation to a change in its price (Alfred, 1890). It is calculated by dividing percentage change in demand by percentage change in price. When PEOD > 1, it indicates demand is price elastic; when PEOD < 1, it implies demand is price inelastic.

An overview of 41 studies reported that the average estimate of price elasticity of demand is -0.33 in the appliance market (Tellis, 1988). The more recent study of Dale and Fujita (2008) suggested that PEOD for household appliances is at -0.35. These findings suggest that demand in the appliance market is not strongly influenced by prices. Therefore marketers may leverage on the price inelasticity to pursue better revenue performance. In addition, Golder and Tellis (1998) discovered that PEOD varied from one product to another. For instance, the PEOD of air conditioners was -0.37 whereas the PEOD of clothes dryers was -0.14. Busse and Rysman (2010) found that the same product had different price elasticity in different regional in consumer markets which lead to different price strategies. For instance, a full-page Yellow Pages advertisement demands about $42,000 a year in suburban Maryland whereas the same advertisement cost about $ 100,000 in Washington DC annually. Choi and Mattila (2004) found that price in the hotel industry fluctuated according to demand. During high demand periods, rooms may only be available to those who are willing to pay higher prices; while during low demand periods, rooms are available to everyone at lower discounted rates. In short, when demand exceeds capacity, revenue management recommends that the hotel sells the limited capacity only to the most profitable mix of customers. When capacity exceeds demand, however, revenue management recommends that the hotel stimulates demand through discounting. In addition, good revenue management also makes it difficult for customers who would pay higher rates from taking advantage of lower discounted rates. For example, hotels in Singapore can sell at an average of SGD 600 for a four star hotel during Formula One season in 2008, whereas the same room may be sold at just SGD 220 for weekends during the off peak season. Enz (2003) reported that increased demand spawned through discounting did not overcome the loss in room revenue resulting from the discounted prices. The results implied that the hotel industry experienced an inelastic demand curve. If discounting does not attract enough additional guests to produce additional revenue, a better approach would be to raise prices or remain status quo.

Lieberman (1993) explained from the perspective of product attributes in relation to price. He elaborated that airlines and hotels possessed a fixed supply of inventory that perished daily. Hence it was necessary to rely on yield and revenue management to maximize daily sales, and to attempt to differentiate their products and services to shift demand up their inelastic supply curves.

Segmentation in relation to pricing strategies.

As market segmentation is an integral part of an organization's pricing strategies, it is crucial for one to understand the concept of segmentation. Ranchhod (2004) defined segmentation as part of the process of planning and executing activities that satisfied individual, psychological and social needs ethically and sincerely while also satisfying organizational objectives. Customer segmentation is one of the ways to differentiate a customer (Strauss & Frost, 1999, p. 10), for example, corporate versus leisure customer. Each segment has significant differences in needs. Hence, an organization can focus specifically on identifying those variables that customers are most likely to consider when evaluating the inherent value of a product or service offer. Once the segments are identified and their characteristics determined, the firm can implement segmented pricing or differential pricing. For example, some hotels in Singapore have weekend special packages that target only at local families. The package includes rooms with two adults' breakfast. A special kids' breakfast corner will be set up in the coffee house to enhance the value. Furthermore, movie tickets will be given as token if the family stays for two nights. Lieberman (1993) suggested that the inelastic nature of business travel forced corporate travel buyers to be price takers. However, these buyers are able to avoid their price-taking position by other means, such as negotiating a committed volume of room nights for better rates and/or requesting for the inclusion of complimentary extra value-added services and amenities.

Stephen (2006) commented that one of the benefits of segmentation was to sell the same item in each market segment at a different price. Similarly, Reichheld (1993) proposed that since not all customers were the same, identifying and focusing on the right group of customers was critical. He found that customers who bought at regular price were more loyal than those who bought at discounted price. Hence he questioned whether new customers should be acquired through promotions and other price reductions if their loyalty was not of a more permanent nature. To acquire loyal customers, a company has to identify the types of customers that appreciate superior value over discounted price and focus on them. Hence segmentation is very important and if carried out properly, the customer segments will be homogeneous and profitable to serve.

In the hotel industry, customers can be segmented accurately base on certain criteria such as the frequency of use or special events and festivals. With the ability to divide the customer base into specific segments, the hotels are able to implement differential pricing to their advantage (Awh, 1998; Yelkur & Herbig, 1997). Furthermore, with proper data and statistics, hotels can estimate the demand of each segment which is essential to implementing a differential pricing strategy. For instance, Scott (2004) found that consumer preferences for location flexibility and/or timing flexibility could be beneficial to segmenting online customer segments. Customers who rank low in both attributes are the ones looking for travel bargains. Therefore, discounted pricing would be attractive to them.

Firms may not necessarily price the product or service based on cost, but rather on the willingness to pay as suggested by Strauss and Frost (1999,p.10 -11). For example, first-class airline tickets are always priced much higher than economy fares. It is supported by Greaves (1995, p. 45) who commented that "it is not the cost of the materials that determines the products value, but rather the customers' perception of that value. Similarly, Canina and Enz (2008) also found that discounting did little to fill rooms particularly in the Asia Pacific lodging market. For instance, when hotels priced 2 % to 5% lower than its competitors, they experienced negative 3 % growth in occupancy. Only when hotels priced 10 % to 15 % lower than its direct competitors, did they gain a marginal 4 % occupancy growth than their rivals. This evidence strongly suggests that the price was essentially determined by the amount the consumer was willing to pay for the perceived vale of the product or services.

Service quality and customer loyalty in relation to pricing strategies.

Consumers evaluate service differently from products because of its characteristics the intangibility, inseparability, heterogeneity and perishability. For instance, if a customer books a hotel room, he/she does not evaluate it based on the room itself, but the total service delivery experience this is a combination of the tangible product, service, interaction with service staff, quality of the food and ambiance etc. This combination of attributes evaluated in a service situation cannot be separated (Bebko, 2000).

Customers frequently rate hotels based on their facilities and service. Many hotels have excellent hardware and continually upgrade them on a regular basis but it's the elusive service quality which leads to loyalty and customer satisfaction (Cadotte & Turgeon, 1998; Kandampully & Suhartanto, 2003). These findings conclude that service quality may be one of the most important factors that influence guest satisfaction. Danziger *et al.* (2006) had demonstrated that consumers still used star ratings to infer the price and the quality of hotels. Peters (1986, p54) also found that service firms which rated high on service quality had on average a 12 % higher price. The other benefit of good service quality was that it could attract potential patrons who were willing to pay and appreciate higher quality. In contrast, those companies which were rated lowly on service had an average of 1 % lower price. This is also consistent with Chen's (2002) study on airline tickets available for purchase over the Internet. Chen (2002) found that the more user-friendly the interface for a website was, the higher the ticket prices charged. Therefore, Henley, Cotter and Herrinton (2007) suggested that hoteliers enhanced the service quality and upgrade the hotel product to bring in increased revenue by increasing price.

Oliver (1997, p.132) defined consumer brand loyalty as “the commitment to choose to repeat a purchase or be the customer of a product or service in the future, despite external influences or the commercial forces that may potentially influence a change in behavior.” In the service industry, firms set customer satisfaction as its primary objective in order to survive and compete effectively (Jones & Sasser, 1995). In other words, focusing on satisfying the customer is the key to retaining its customers, especially the loyal ones. Iglesias and Guillen (2004) concluded that satisfied customers would repeat their purchases, spread their positive experience and therefore help companies to lower their marketing expenditures (Relihan, 1989; Heskett et al., 1997). More importantly, they became more loyal to the firm, and would be willing to pay premium prices for products and services (Zeithaml et al., 1996; Chaudhuri & Holbrook, 2001). On the other hand, acquiring a new customer is costly and may be between 5 to 10 times more expensive than retaining an existing customer (Gilbert & Getty, 1994). Therefore, O’Neill, Mattila, and Xiao (2006) proposed that hotel brands with more satisfied guests should have greater growth rates (i.e., larger increases in the total number of guest rooms), larger market share (i.e., higher occupancy rates), and relatively higher prices (i.e., higher average daily rates). Alpert, Wilson, and Elliott (1993) recommended that price reflected consumers’ preference. This was consistent with their value assessment according to price and quality perceptions. Several empirical studies have shown that price and quality perceptions influence value perceptions (Bolton & Drew, 1991; Ralston, 2003). They conclude that price perceptions have an important influence on customer value. Similarly, Varki and Colgate (2001) arrived at similar results in the banking industry. They found that price perception directly influenced customer satisfaction, the likelihood of switching, and the likelihood of recommendation to others. Hence, these findings suggest that hotel managers have to actively manage their customer's price perceptions so that it would have a positive impact on customer satisfaction and loyalty. Jones and Sasser (1995) further confirmed that one of the major factors that influenced financial performance was customer satisfaction and customer loyalty. Kashyap and Bojanic (2000) pointed out that the customer's perception of value varies significantly depending on the repetition of the visit. Other researchers suggested that customer loyalty is a measure of how likely customers are to return (Pritchard & Howard, 1997; Dick & Basu, 1994). In particular, when service firms focused on customer satisfaction, it would lead to increased loyalty. Eventually, the increased loyalty would substantially improve profits.

Overall, firms that achieved high customer satisfaction were rewarded with superior economic returns (Rust & Zahorik, 1993; Anderson et al., 1994; Bankeret al., 2005). When a firm is able to deliver a higher quality product or service to the right segments than its rivals, customers would more likely be satisfied and its perceived values are enhanced. This leads to both winning new customers and maintaining customer loyalty. Consequently, its market revenue and share would increase substantially. These findings confirm the importance of managing service quality, customer satisfaction, and loyalty in order to pursue high REVPAR growth.

Pricing strategies overview.

Overall cost leadership and differentiation are two generic competitive strategies used by firms to compete effectively against other firms in the same industry (Porter, 1980). Cost leadership implies that the organization sells the product or service below industry price in order to gain market share. Wall- Mart is a typical example of cost leadership strategy application. In contrast, a differentiation strategy calls for the product or service to offer unique attributes that are valued by customer. Customers perceive better value than that offered by their competitors so that firms can charge at a premium price (Porter, 1980). Luxury hotels tend to use this strategy by offering personalized service to differentiate themselves from others. However, in differentiating, organizations have to take cost into serious consideration to ensure the strategy succeeds profitably (Porter, 1985). The incremental cost of differentiating must not be more than the additional revenue gained as a result of differentiation.

In the lodging industry, early studies found that many hotels tended to adopt price discounting in the market due to the perishable nature of hotel rooms (Aronson & Barkoff, 2004; McGill, 1999; Smith, Leimkuhler & Darrow, 1992). Canina and Enz (2004) did a study of more than 6,000 hotels during 2001 and 2003. They found that more than half of the hotels in the study implemented a discounting strategy when competing with their direct competitors in their respective markets, even though the occupancy gain was at the cost of lower revenue. As the study was done during economic downturn immediately after 9/11, many of the hotels were using discounting to stimulate consumer demand. Interestingly, another similar study (Canina & Enz, 2006) was done in 2005 when the industry rebounded. It found that hotels were still continuing their discount strategy despite the fact that the overall economy had improved and REVPAR had increased by nearly 8 %, the highest in the past 10 years (Smith Travel Research, 2005). A more recent study by Canina and Enz (2008) stated that more than 53 % of hotels were still using discounting strategy when competing against their direct competitors in their respective market. The percentage of hotels practicing discount strategy only marginally decreased by 0.7 %, despite the much higher increase in REVPAR from 2003 to 2004. These findings implied that discounting price was more dominant in the market than premium price. Stephen (2006) discovered that for hotels operating with a high fixed cost and a low variable cost, found it difficult to balance the supply and demand for rooms in their daily operation. The perishable nature of room inventory together with low variable cost encouraged hotels to sell available rooms at a lower price rather than let it be lost. These reasons may explain why discounting is still one of the most popular practices in the market.

Despite the fact that more hotels practiced discounting strategy than premium pricing, Canina and Enz (2008) found that hotels in direct competition made more money when they maintained comparatively higher prices and did not discount to fill rooms. Although charging a high rate may lose occupancy to a certain extent, the magnitude of loss in occupancy is not as significant as the gain in revenue. Therefore, premium price gains revenue advantage although it has occupancy disadvantage. In short, premium price is more effective to achieve high revenue than discounting. Canina and Enz (2008) confirmed that Asian hotels couldn't steal market share by discounting. Regardless of whether these hotels achieved gains or losses in occupancy, they indeed recorded the smallest gain in REVPAR. In contrast, hotels that set premium prices over their rivals lost occupancy but gained the most in REVPAR. These important findings suggest that hotels might want to adopt a premium pricing strategy in order to achieve higher revenue.

Revenue performance measures.

Hotel operators and investors adopt a number of industry statistics as benchmarks to evaluate revenue performance. Hotel occupancy rates are used as an important indicator in hotel performance- related research (Jeffrey & Barden, 2000). Marris (1992) agreed that occupancy was the most frequently kept record by hotels. It is calculated as a percentage of the number of rooms sold over the number of rooms available. The higher the occupancy, the better it is. For instance, occupancy of 89 % is better than 85 % as it indicates more rooms are occupied for business.

Aaker (2001) suggested that products with similar attributes tend to sell for a similar price in a competitive market. Price theory asserts that the market price reflects the interaction between demand and supply considerations. Therefore, ADR is an important measure to evaluate a hotel's performance. ADR is calculated by dividing the daily room revenue over the number of rooms sold. It is a price mean of all the rooms sold for the day. A higher ADR reflects a high revenue per sold room. However, the limitation is that both measures focus on a single perspective. For example, if one compared Hotel Green with 81 % occupancy and an ADR of $100, to Hotel Orchard with 90 % of occupancy and an ADR of $ 90, the result would be one dimensional and inconclusive. Hotel Green would be valued better than Hotel Orchard from the ADR perspective whereas Hotel Orchard would be better than Hotel Green based on occupancy.

As hoteliers are more interested to evaluate revenue, Berger (1997) recommended REVPAR to evaluate hotel performance as it takes a balanced view of both occupancy and ADR. The REVPAR is calculated by dividing daily revenue by the number of rooms available or a product of occupancy and ADR (Alleyne et al., 2006). Going back to the previous example of Hotel Green and Hotel Orchard, they may appear to be performing differently depending on whether occupancy or ADR is taken into consideration. Yet both perform adequately because they achieve the same REVPAR through different means. Enz et al. (2003) suggested that occupancy, ADR and REVPAR to be used to derive a holistic view rather than focusing on an individual aspect. However, Joni (2006) explained that REVPAR focused only on the room revenue, but other revenue generated from other areas were not captured such as guest expenditure in the restaurants and spa service.

Network theory argues that firms are not free to choose any competitive action. Instead, they must make moves and countermoves within the confines of their geographic cluster (Burt, 1992). In other words, a hotel has to monitor and react to competitors' price movement accordingly. In fact, many owners and hoteliers feel the pressure especially when their direct competitors drop the price. Canina and Enz (2004, 2005, 2006a, 2006b, and 2008) recommended that relative ADR, relative occupancy and relative REVPAR were more effective measures as they captured competitive pressure under more equivalent market conditions. The individual hotel's occupancy is influenced by the action of their direct competitors. The management of a hotel is often under pressure to drop their prices to maintain relevance with their competitive set.

Summary

The above literature review addresses the importance of pricing strategy in revenue management, the important factors that influence pricing strategy and the statistical measures to evaluate the effectiveness of revenue management. Although price strategy is a complex issue where many factors play important roles in determining price, the literature suggests that a hotel might implement premium pricing to achieve high revenue regardless of economic recession or recovery. Equally important, the quality of the service and customer loyalty have to work together to ensure the success of pricing decisions. Overall, revenue management is not only about price; it is about the understanding of the market and the customers so that hotels can deliver the right service to the right customers at the right time at the right price.

Part three

Introduction

The relative pricing strategy practice is the primary focus of the paper. The literature review addressed the importance of relative pricing strategy and concluded that those hotels charging higher premiums would result in relatively higher growth of REVPAR. It also drew attention to crucial factors like service quality and customer loyalty which are critical to support premium pricing implementations. Part Three concentrated on how the relative pricing strategies affect the hotel performance. Two levels of the analysis were conducted in the study. The first was to study the impact of relative ADR on relative occupancy, and relative REVPAR. The second was to investigate the relationship of relative ADR with guest satisfaction and customer loyalty. Recommendations were made based on the historical data in this case study.

Methodology

Sample and data collection.

The secondary data was solicited from Smith Travel Research (STR), TNS Global and the case study hotel, which will be referred to as Hotel Orchard from here on. STR data consisted of the monthly ADR, occupancy and REVPAR for both the property and competitive set from 2006 to 2009. TNS is the independent consultancy firm that evaluated the hotel's GSTS index based on the survey conducted each month. The standard questionnaire provided by TNS covers areas related to the customer's entire experience such as the staff attitude, hotel room, and restaurant experience, value to money, and likelihood of return. Hotel Orchard had to randomly select guests for participation. The sample size was restricted to a minimum of 50 to a maximum of 80 guests per month. The answered questionnaires were then sealed and sent to TNS for scoring. (For detailed sample survey and report, see Appendices 1 & 2). Over a four year period, a total of 48 sets of data should have been collected. However due to insufficient sample size for October 2008 only 47 sets were available.

Data validity.

Hotels cater to multiple segments which may include transient, corporate, and travel agents. Pricing for corporate and travel agent segments were priced according to contracts and therefore rarely changed. Therefore, transient pricing was mostly reflected in the overall pricing trends.

STR has comprehensive guidelines for hotels to select their competitive set to ensure the data validity and integrity. No single company could account for more than 60 % of the total participating room supply of a competitive set. Furthermore, a competitive set had to include at least four participating properties which excluded the subject property and other properties from the same company. Finally, all participating hotels had to report their respective data before performance data for the entire set would be released (see Appendix 3). Hence, the data selected is relevant and valid to the study.

Data analysis.

The analysis adopted similar methodology used by other researchers in the series of studies (Enz & Canina 2004; 2005; 2006a; 2006b; and 2008). The first level of analysis involved relative ADR, occupancy, and REVPAR. First, data was grouped into three sets: ADR, occupancy, and REVPAR that included both Hotel Orchard and its competitive set. Second, data was calculated for the percentage difference for all three sets. For example, the percentage difference in ADR was calculated as the ADR of Hotel Orchard less the

ADR of the competitive set divided by the ADR of the competitive set and expressed as a percentage. This same method was used to compute the percentage differences for occupancy and REVPAR. Since this study is on how changes in ADR affects occupancy and REVPAR, the percentage differences in ADR were first re-grouped into 5 different clusters ranging from less than zero to greater than positive 10 %. For instance, <0, 0-2 %, 2-5 %, 5-10 %, and >10 %. The percentage differences for occupancy and REVPAR that corresponded to the percentage differences in ADR were also re-grouped into the same 5 clusters (See Appendix 4). The mean of ADR, occupancy and REVPAR of each cluster was then calculated and presented in Figure 1.

The second level of analysis involved relative ADR, GSTS index, and Priority Club Rewards (PCR) contribution. PCR is the loyalty program of Hotel Orchard. The PCR contribution is calculated by PCR members' monthly revenue divided by the total guest monthly revenue. The relative ADR, GSTS, and PCR contribution were grouped and analyzed in the same way as that done for ADR, occupancy and REVPAR (See Appendix 4).

Results and discussion

Table 1 shows the sample size of the study was 47 sets on calendar months. In the 4 year observation period, Hotel Orchard practiced premium pricing for 42 months which was 89 % of the period under study. It was able to maintain its price 5 – 10 % higher than its rivals for the longest period (36 % of the time). On the other hand, it exercised discounted pricing for only about 11 % of the total period.

Table 1

Data set showing details of Hotel Orchard pricing strategy

ADR percentage difference	Data sets	%
< 0	5	11
0 - 2	7	15
2 - 5	12	26
5 - 10	17	36
> 10	6	13
Total	47	100

Table 2 indicates a robust year on year revenue performance for Hotel Orchard from 2006 to 2009. The annual ADR was higher than its competitive set for all four years. As a result, it achieved higher REVPAR as well as higher occupancy for the entire observation period.

Interestingly, ADR in both Hotel Orchard and its competitive set fluctuated more than occupancy. The hotel ADR ranged from USD115.25 in 2006 to USD188.77 in 2008 whereas the competitive set ADR ranged from USD108 to USD 181.23. The occupancy ranged from 84.8 % in 2009 to 93.9 % in 2007 for Hotel Orchard, as compared to 76.5 % to 86.9 % for the competitive set. Overall, Hotel Orchard recorded average occupancy of 88 % whereas the competitive set recorded 83.3 % during the entire period. The range of ADR fluctuations was greater than that of occupancy fluctuations. For instance, hotel occupancy recorded 6 % growth whereas ADR achieved growth of 23 from 2006 to 2007.

Table 2

The hotel performance overview (2006 – 2009)

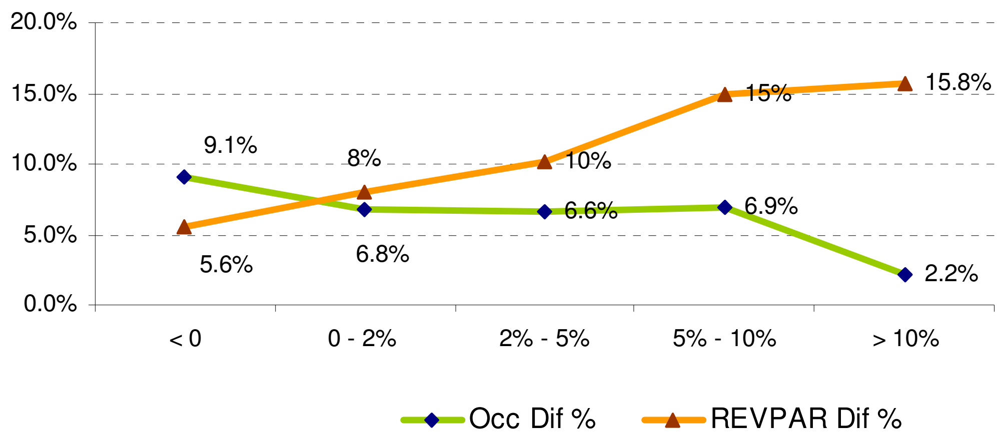
Year	ADR1	YOY Var.	ADR2	YOY Var.	Occ1	YOY Var.	Occ2	YOY Var.
2006	115.25		108		88.4		84.9	
2007	141.95	23%	138.67	28%	93.9	6%	86.9	2%
2008	188.77	33%	181.23	31%	85.3	-9%	82.8	-5%
2009	152.7	-19%	142.94	-21%	84.8	-1%	76.5	-8%
Mean	119.734		114.168		70.48		66.22	

*Note.*Occ1 equals to Occupancy of Hotel Orchard; Occ2: Competitive set average Occupancy; ADR1 equals to average daily rate of Hotel Orchard; ADR2 equals to competitive set average daily rate.

Figure 1 provides a snap shot of the relationship between occupancy, ADR, and REVPAR. It can be found that relative REVPAR had positive relationship with relative ADR whereas the relative occupancy had a negative relationship with relative ADR. The rising prices resulted in the occupancy decrease and upwards REVPAR growth. However, when Hotel Orchard dropped its prices relatively to the level of the competitive set, occupancies improved moderately, but the gain in occupancy was less than the drop in prices, which resulted in lowest REVPAR in this study.

Figure1

Relative ADR, occupancy and REVPAR percentage difference for Hotel Orchard (2006 – 2009)



The effects of premium pricing strategy.

As illustrated in Figure 1, it clearly shows that Hotel Orchard improved its REVPAR performance by adopting premium pricing. It achieved significantly higher REVPAR when it set higher prices than its competitors. Particularly this applies to the price range from zero to more than 10 %. On the other hand, the inelasticity of price to the demand in the study was illustrated by the premium price range from zero to 10 %. For example, when Hotel Orchard charged ADR 2 to 5 % higher than that of their competitive set, its occupancy was about 6.6 % higher whereas when the price premium increased to 5-10 %, the respective occupancy was 6.9 % higher. Despite the price increase of 3 %, the occupancy only changed by a marginal 0.3 % which led to the PEOD approximately 0.1. In short, charging higher rates did not result in significantly lower occupancies but substantially higher REVPAR instead. Since the demand was significantly inelastic at the price change from 0 to 10 %, the hotel would obtain a high REVPAR if it charged at 5 to 10 % higher. Although the highest relative REVPAR of 15.8 % was achieved when the hotel charged a premium price of more than 10 %, the demand dropped to the lowest level of 2.2 % which resulted in a flat growth of REVPAR.

The effects of discount pricing strategy

Figure 1 also shows that the improvement of demand through discounting by Hotel Orchard. For instance, when they priced lower than its rivals, the relative occupancy improved from 6.8 % to 9.1 %. However, the effort of lowering the price in relation to key competitors failed to bring in enough customers to cover the loss in revenue. As a result, the REVPAR performance was negatively affected. Therefore, although it achieved the highest relative occupancy of 9.1 %, it also recorded the lowest REVPAR of 5.6 % for the entire observation period.

Evidently, the desire to pursue increased demand by lowering prices did not translate into increased revenue in this study. In fact, when they implemented discounting price relative to their competitors, they actually experienced the lowest comparative REVPAR. In a nutshell, Hotel Orchard achieved relatively high occupancy advantage by steep price cutting but at the expense of a much lower REVPAR.

Occupancy vs. price strategies.

The relative occupancy in the study remained essentially stable regardless of the price changes as compared to the competitive set. For example, in the price range from 0 % to10 %, the change to relative occupancy was marginal. This finding indicates that market share remained fairly constant throughout this range of price changes. The evidence suggests that any modest occupancy gain obtained from discounting was not sufficient to cover the loss of revenue, resulting in lower REVPAR performance. It may also suggest that if the relative pricing was increased up to a tolerable 10 %, guests would still be loyal to Hotel Orchard, beyond which, they might look at other alternatives. In contrast, during the period when they priced higher than their rivals, the occupancy decrease was offset by their relatively higher ADR to yield the highest REVPAR.

It should be noted that the relative occupancy difference of the hotel remained positive as compared to its competitive set during the observation period. The occupancy advantage only diminished when they priced their rates more than 10 %. The significant changes only happened in two periods: a) one was when they increased price more than 10 %, and b) when the hotel practiced discounting price strategy.

REVPAR vs. pricing strategies.

Based on the data represented in this case study, Hotel Orchard achieved higher REVPAR than its competitors regardless of economic conditions. When it set relative price higher than its competitors, it achieved continuous high relative REVPAR growth. But discounting failed to stimulate enough demand to offset the loss in price. Therefore the REVPAR advantage was diminished as the discount increased. Overall, premium price strategy demonstrated stronger impact in improving relative REVPAR than discounting price strategy.

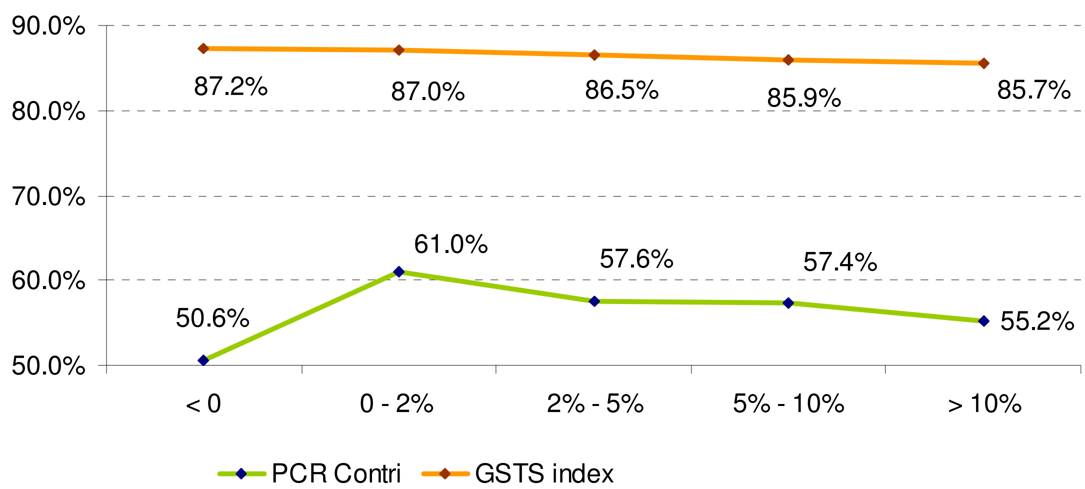
Pricing strategies in relation to guest satisfaction and loyalty.

The intangibility, heterogeneity, perishablity and inseparability (Parasuraman, Zeithhaml, & Berry, 1988; Kandampully &Suhartanto, 2003) of hotel service is a great challenge to develop a robust customer loyalty program. Moreover, Ernst and Young (1996) found that premium pricing can have a negative impact on the firm’s medium to long term profitability whereas developing customer loyalty can moderate the impact. Most importantly, Gronroos (2000) indicated that loyal customers contribute more to the organization due to the three reasons: a) they are willing to pay a premium price, b) the life time value of the loyal customer, and c) less marketing cost is incurred in targeting them as they are familiar with the product and service.

Figure 2 demonstrates the customers' response to the different price strategies. The GSTS index in relation to ADR reflects the overall guest response to the price changes whereas the PCR contribution in relation to ADR illustrates the loyal customers' reaction to the price.

Figure 2.

Hotel Orchard relative ADR in relation to guest satisfaction and customer loyalty (2006 – 2009)



As shown in Figure 2, the GSTS index had a marginal negative relationship as the price increased. The magnitude of GSTS index was much less than the magnitude of price changes implying that this negative relationship was not significant. For instance, it recorded the lowest GSTS index of 85.7 % when Hotel Orchard's ADR was greater than 10 % whereas the highest GSTS index was 87.2 % when it exercised discount pricing strategies. The gap in the GSTS index was only 1.5 % whereas the gap in price was greater than 10 %. More over, when the hotel shifted its price strategy from premium to discounting, there was an improvement of GSTS index by only 0.2 %. Hence, the negative impact was at minimal level for the observation period. Based on the data analysis, the results suggest the price strategies have minimal impact on guest satisfaction. This finding confirms that service firms that offer high service quality could charge high prices (Cadotte & Turgeon, 1998; Kandampully & Suhartanto, 2003; Danziger *et al,* 2006; Chen, 2002).

Figure 2 also shows that the hotel had more than 50 % of loyal customers business regardless of pricing strategies during the observation period. Such a high contribution reflects the hotel's consistent service quality. Most importantly, these loyal customers are the ones who are willing to pay high prices (Chaudhuri & Holbrook, 2001; Zeithaml et al., 1996).

Similar to the GSTS index, when the hotel charged higher prices than its rivals, there was a slight downward trend in PCR contribution. As the price went up, the PCR contribution decreased. However, the positive changes in ADR were far more significant than the negative impact in PCR contribution. For example, when the hotel raised price from 5 % to 10 % higher, the decrease of the PCR contribution was marginal (from 57.6 % to 57.4 %).

In contrast, the PCR contribution dropped from the highest level of 61 % to its lowest point of 50.6 % when the hotel switched pricing strategy from premium to discount. This may be due to the change in customer mix, whereby the discounted price may have attracted more price sensitive customers. Due to the fixed room capacity, the increase in demand from price sensitive customers left fewer rooms for loyal customers during those periods. Hence, PCR contribution declined. On the other hand, the hotel achieved the highest guest satisfaction at the same period of time, indicating the high quality serviced delivered. As many of the researchers concluded that loyal customers are those who enjoyed high quality of service and were willing to pay high prices (Chaudhuri & Holbrook, 2001, Strauss & Frost, 1997), the hotel would have achieved higher REVPAR if they had implemented premium price strategy throughout.

Although the hotel recorded the highest REVPAR when it charged the highest price (ie. greater than 10 %), the hotel recorded the lowest GSTS scores and the lowest loyal customer contribution. Meanwhile, the previous analysis amongst relative ADR, occupancy and REVPAR discovered that the growth of REVPAR at that cluster was also flat due to the significant loss in occupancy. These findings suggest that the hotel may need to strike a balance of short term and long term financial goals and avoid the danger of over pricing. This conclusion was supported by Ernst and Young (1996) which states that premium pricing can have a negative impact on the firm's medium to long term profitability. In addition, the fact that the hotel had recorded the second highest REVPAR with relatively high level of guest satisfaction and customer loyalty contribution demonstrates that the premium price at the 5 to 10 % level was more appropriate to achieving the right balance.

Conclusion and recommendations

The study explored the relationship between relative ADR, relative occupancy, and relative REVPAR from 2006 to 2009 at Hotel Orchard. In this study, Hotel Orchard demonstrates strong revenue management capability in relative pricing strategies. Demand was found to be not strongly influenced by pricing efforts. In fact for the premium pricing of 0 – 10 %, it revealed a distinct inelastic relationship between price and demand. On the other hand, discounting strategy also recorded a steady growth of REVPAR; however the REVPAR growth was at minimum as discounting was not able to pick up enough demand to mitigate the loss in ADR. Indeed, as the highest guest satisfaction score was recorded in the same periods, the hotel should have charged premium prices due to the high quality of service rendered (Cadotte & Turgeon, 1998). These findings suggest that Hotel Orchard should continue to leverage on premium pricing to achieve high REVPAR. However, the study also demonstrates that demand started to drop significantly beyond the 10% level, indicating that customers may only tolerate a price increase up to a certain limit before considering alternatives. Hotel management therefore has to strike a balance between short term and long term financial goals.

Another interesting finding was that the price strategy had little impact on overall guest satisfaction. A similar finding was also discovered amongst loyal customers. The constant high guest satisfaction score reflected the high service quality. More than 50 % of business came from loyal customers thereby confirming that service quality matters more than the price. As long as the hotel delivers high standards of service, it will lead to high guest satisfaction and strong customer loyalty (Cadotte & Turgeon, 1998; Kandampully & Suhartanto, 2003). More importantly, loyal customers are willing to pay a premium price (Gronroos, 2000).

Singapore government is well – known for its support for businesses. Its lenient visa application policy has a positive impact on the in-bound tourist markets, especially in bringing in more leisure visitors from Asia, like China, India, and Thailand. Tourism demand will continue to grow especially with the recent opening of the two Integrated Resorts - Marina Bay Sand and Resort World Sentosa. As such Singapore tourism will continue to enjoy growth in the near future. These positive factors will allow Hotel Orchard to continue with its premium pricing strategy. Meanwhile, they should maintain a high level of service quality to ensure customer loyalty, so as to ensure the success of their premium pricing strategy.

Limitation and future research

Previous studies concluded that hotels should adopt premium price strategies to pursue better revenue performance at a broader level (Enz & Canina, 2004; 2005; 2006a; 2006b and 2008). This case study arrived at the similar conclusion by using a specific hotel's data. With only one hotel studied, it might not be suitable to generalize the findings to the overall market. The hotel is a midscale hotel property so it may not be appropriate to generalize the results to luxury or budget markets. Therefore, there is clearly a need to study the impact on the different types of hotels so as to refine the conclusion. Moreover, as ADR is determined by segment, future studies may want to concentrate on the analysis of one particular segment. Customers' views on different pricing strategies should also be evaluated from the competitive set's perspective. GSTS score and loyalty customer contribution from competitor hotels would help in this regard.

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