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Mr. Trabulsi

Food & Beverage

Key Considerations In Outsourcing Hotel Food & Beverage

By [Larry Trabulsi](#), Senior Vice President, CHMWarnick

As my colleague, Michael Doyle, asked in his article [Why should hotels outsource, or challenge a traditional operations model?](#) The most common answer is to maximize profitability. Industry-wide, Food and Beverage revenue represents over 25% of total hotel revenue, yet generating a meaningful profit margin in F&B (which is difficult to measure with accuracy) can be challenging. In many hotels (particularly lifestyle and boutique hotels) F&B can be an integral part of the guest experience, and a large source of revenue (and maybe profit) for the hotel. But unlike other, less visible departments, outsourcing F&B can be more challenging, yet also more rewarding.

In addition to increased profitability, there are other factors that can be favorable to outsourcing. For many properties, enhanced F&B can contribute to the overall identity of a hotel that the hotel by itself (and current management company) cannot. This identity can help to attract local customers who may never have considered eating or drinking at the hotel; and for hotel guests for whom great F&B may be a deciding factor in where to stay. In mixed-use projects with a residential component, this identity and presence may also help to position and ultimately sell real estate ("have room service prepared by x"). Another benefit of bringing a third-party into a hotel is that it can complement, or fill a void, with other existing outlets that may be self-operated. Examples may include a high-end celebrity chef driven restaurant to go along with a more traditional, three meal a day restaurant.

Out-sourcing this key area can have numerous risks as well, with the biggest risk being loss of control over operations (in the event of a full out-sourcing, such as a lease). Examples we have seen include reputational risk to the hotel due to poor service/reviews, health department issues, and financial issues with the partner. While an agreement may outline a process and remedies for the hotel owner, separation and execution of remedies, may be easier said than done. These risks need to be weighed against the possible benefits.

Before going down the path on an outsourcing, a hotel owner needs to do their homework. To assist with these assessments, the owner may need to bring in outside expertise. Project team members may include a real estate broker, who has knowledge of the local restaurant market and can provide a dose of reality to a situation (even though brokers sometimes see things through rose colored glasses); attorneys with experience in negotiating similar deals; and other F&B consultants or asset managers who can identify solutions to many operational issues.

The first step is an internal assessment (both financial and operational) of the proposed operation. The financial assessment should focus on the "before" (i.e. current performance) and "after" (i.e. with an outsourced opportunity). This exercise should encompass a full hotel profit and loss statement, and not just departmental profit. At one hotel that I recently reviewed, the P&L statement reflected a breakeven at the F&B departmental level, but upon further analysis (due primarily to undistributed costs that were tied to the restaurant), the "actual" loss was over \$300,000/year. This exercise should be as detailed as possible, and may get to individual staffing levels to uncover the true operating profit or loss of outlets.

From an operations perspective, the owner should understand how the proposed operation fits into the overall mix of other outlets within the hotel (or in a mixed-use complex, other operations within the complex). Would the proposed operation compete, or complement other outlets? Is there a risk of sales erosion (perhaps by meal period)? From an operational perspective, an owner needs to understand how the proposed operation fits



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AUGUST: Food & Beverage: Multiplicity and Diversity are Key



Creativity and Science Have Merged on Hotel Menus

By [John Signorelli](#), Executive Chef, St. Regis Houston

We, as Chefs, respectfully kick around the terms Hybrid, Old-World, and Artisanal often enough. Chefs know that hybrid, old-world, artisanal, or obscure ingredient usage in dishes bring a particular wow-factor to the plate. Sourcing and utilizing artisanal grains, starches, legumes or vegetables which are under-appreciated and under-utilized, or quite possibly forgotten about over time, is a highlight feature of today's creative chefs, many of whom will grow the ingredients themselves and feature on special menus, unlike any other. [READ MORE](#)



Designing Menus That Balance Traditional Fare with Modern Dietary Needs

By [Elli Fortney](#), Executive Chef, Topnotch Resort

into the hotel. Additionally, the internal assessment needs to look at the facility (proposed space). Does the space have its own kitchen? How is it accessed by patrons? Generally speaking, a restaurant in a poor location, with limited visibility and foot traffic, may not be successful regardless of who is operating it!

An internal assessment is only part of the equation. An owner needs to undertake a local market/competitive market assessment. What is in the current market? What is missing? What is doing well? Who is dining where? Does my hotel and proposed outlet even have a chance of attracting the local market? Who is operating restaurants and making deals? Is anything changing in the local market or surrounding neighborhood? As mentioned above, is the management company amenable to losing some control of an operation, and what are the risks and benefits to ownership?

The internal assessment must also take into consideration the relationship with the hotel management company, from an operational, financial and contractual perspective. Operational issues can include union versus non-union workforces, understanding the applicability of brand standards (which may be defined currently, but will likely change over time), rules of conduct within the hotel (including employee entrances) and allowable differences in uniforms and appearance standards. Financial issues can include understanding cost allocation models that may need to arise (i.e. bathroom cleaning, garbage, etc.). Contractual issues can include is outsourcing allowable under the terms of the Hotel Management Agreement (HMA), how will an outsourcing impact the management company financially (i.e. gross restaurant revenues may decrease and become rental income), and possibly performance test and termination issues. Additionally, liquor license issues should be identified early in the process to understand restrictions that may exist.

From an owner's hotel investment perspective, while maximizing profitability is a key factor, any decision to outsource F&B services, or otherwise, should also consider the owner's investment time horizon and ability to contribute capital. With regards to capital contribution, each ownership group needs to be prepared to deploy capital (and sometimes defer other capital projects) to execute on an outsourcing strategy. Additionally, before executing on an outsource opportunity, the owner should discuss the opportunity with their lender, as lenders typically view these agreements as encumbrances on their collateral.

The output of these assessments should help to frame operating parameters that can work along with hotel operations, and a sense of buy-in from all parties on a path to proceed upon for some sort of outsourcing agreement. Below is a summary of the most common types of agreements.

- **Lease Agreement** - Lease agreements essentially create a Landlord/Tenant relationship where the restaurateur (i.e. the tenant) leases space within the hotel (i.e. the landlord) for a defined space or spaces. The lease agreement typically spells out payment terms, usually in the form of rental income, which may have fixed and variable components. The variable component is typically expressed as a percentage of revenue above a "break" point. The Lease Agreement also typically spells out how various expenses, such as utilities, refuse, and other overhead, will be treated. From a hotel owner perspective, key attributes to a lease include the credit-worthiness of the tenant, and exit strategy if business does not go as expected over the term of the lease.
- **Management Agreement** - Under a typical management agreement, the hotel brings in a 3rd party to oversee the F&B operations. Typically, the employees (with the possible exception of key personnel, such as a General Manager or Executive Chef) remain as employees of the hotel management company, but are executing on the third party's concept.
- **Licensing Agreement** - A licensing agreement is similar to a management agreement, but may include more brand names and trademarks. A prime example of a licensing agreement may be a full-service Starbucks in a hotel lobby that is staffed by hotel employees.
- **Consulting Agreement** - A consulting agreement may allow for a 3rd party (such as a local, well-known chef) to provide advice on a restaurant's operations. This typically includes menu development (which may occur several times a year), as well as staff training and design input.

While the section above makes the various forms of agreements seem separate and delineated, it is not uncommon to see hybrid agreements. An example might include a management agreement with a minimum payment to the owner in the form of a "deemed rent" that can shed some of the risk of the operation.

Regardless of the structure, there are several other considerations that need to be addressed in each form of agreement (and even considered beforehand). These include:

- **Term and Termination** - Owners prefer to have as much flexibility as possible if things do not go well, and security if things do go well. The negotiation process of each of these agreements will likely cause some compromises to be made. If flexibility is a key issue for an owner, it may be beneficial to include upfront termination fees and formulae for termination for convenience (or upon sale).
- **Fee Structure** - The owner needs to avoid (or minimize) fee payments to both a third-party manager, and the hotel manager. Additionally, incentive fee structures should be well-defined and not require a PHD in Physics to calculate. Our preferred formula is a Return on Investment calculation: e.g. if the Owner makes x% on their invested capital

The dining experience in the hotel and resort environment has been changing for decades. Gone are the days when most Americans eat meat and potatoes, and the occasional salad, for dinner. Immigrants from all over the world who settled into the urban areas of our country brought culturally significant dishes that opened up a whole new supply chain of ingredients, and introduced flavor profiles unfamiliar to the food scene. [READ MORE](#)



Cultivating the Food-Focused Culinary Traveler

By Robert Habeeb, President & Chief Executive Officer, First Hospitality Group, Inc.

As so many hotel owners and operators can attest, food-focused travel is on the rise. The trend is unmistakable: more and more hotel guests are selecting destinations and planning itineraries around regional, local, or even restaurant-specific food and beverage options. These guests, referred to as culinary travelers, not only make food and drink experiences a priority during their travels, they are often willing to go well out of their way to make those experiences happen. Experience is the key word here. We are in an experience economy and consumers are placing a great deal of value on the F&B experience. Look at the trend in roof top bars for example. [READ MORE](#)



Our Guests' Elevated Palates Means Revisiting Our Heritage

By Krista Heinicke, PR Manager for Food & Beverage, The Broadmoor

Our guests are as discerning as they are trailblazing, much like our founder and bon vivant Spencer Penrose. Catering to the taste buds and elevated palates of today often means revisiting our past. This rings true for The Broadmoor, because not only are we the longest-running Forbes Five Star, AAA Five Diamond resort in the country, but as stated by Executive Chef David Patterson, "What we're doing at the greenhouse, is the most romanticized version of being a chef." [READ MORE](#)

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(which may increase over time), then the Manager should participate (within reason) of the profits thereafter.

- Services to be Provided, or Not Provided - Items to consider include branded or themed banquets and catering menus, room service, etc.

F&B outsourcing, if done with appropriate due diligence (surrounded by qualified advisors or asset managers) can add significant value to a hotel owner through increased profitability and asset visibility. However, every opportunity needs to be evaluated carefully to mitigate risks and to ascertain specific nuances of an individual hotel or local marketplace.

Larry Trabulsi, is a Senior Vice President of CHMWarnick, the leading hotel asset management and owner advisory services firm in the U.S. Mr. Trabulsi brings 20 years of hospitality operations, advisory and asset management experience to CHMWarnick. He is a senior member of a team of asset managers, who oversee a client portfolio of over 65 hotels, 27,000 guestrooms and \$15 billion in client investments. Mr. Trabulsi has extensive capital planning and renovation oversight experience and has been involved in single renovation projects of over \$30 million. Mr. Trabulsi can be contacted at 978-522-7000 or trabulsi@chmwarnick.com. Please visit <https://www.CHMWarnick.com> for more information. **[Extended Bio...](#)**

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FEATURE FOCUS

Hotel Group Meetings: Blue Skies Ahead

After a decade of sacrifice and struggle, it seems that hotels and meeting planners have every reason to be optimistic about the group meeting business going forward. By every industry benchmark and measure, 2017 is shaping up to be a record year, which means more meetings in more locations for more attendees. And though no one in the industry is complaining about this rosy outlook, the strong demand is increasing competition among meeting planners across the board – for the most desirable locations, for the best hotels, for the most creative experiences, for the most talented chefs, and for the best technology available. Because of this robust demand, hotels are in the driver's seat and they are flexing their collective muscles. Even though over 100,000 new rooms were added last year, hotel rates are expected to rise by a minimum of 4.0%, and they are also charging fees on amenities that were often gratis in the past. In addition, hotels are offering shorter lead times on booking commitments, forcing planners to sign contracts earlier than in past years. Planners are having to work more quickly and to commit farther in advance to secure key properties. Planners are also having to meet increased attendee expectations. They no longer are content with a trade show and a few dinners; they want an experience. Planners need to find ways to create a meaningful experience to ensure that attendees walk away with an impactful memory. This kind of experiential learning can generate a deeper emotional connection, which can ultimately result in increased brand recognition, client retention, and incremental sales. The September Hotel Business Review will examine issues relevant to group business and will report on what some hotels are doing to promote this sector of their operations.

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