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Financial Management for the Hotel Industry

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## Introduction

Founded in 1881, as a boarding house in Dublin by William Jury, the Jurys Inn is a big hotel group in UK and Ireland. Currently it has hotels in 36 locations with around 4,000 employees. As UK is competitive market with many hotels and similar services, it is difficult for the hotel companies to be continuously successful in financial matters. Though UK is a big tourist destination and visitors' foreign countries travel UK for various business and official purposes, competing with so much other brands makes difficult for the hotel management to cope with financial challenges of operating hotels in UK. So, this report will look into the financial analysis of Jurys Inn.

## Suitable Financial Ratio Calculation for Jurys Inn.

### Profitability Ratios

The company's profit earning capacity relative to company's asset, revenue, shareholder's equity or even operating cost are measured through the profitability ratios (Kolb and Rodriguez, 2018). These are crucial financial ratios for the investors and also for the management body of the company. It shows, how capable the company is in profit generation.

#### *Net-Profit Margin*

Net-profit margin is highly used financial ratio that evaluates the percentage of net-profit in comparison with company's revenue (Steffy, Strunk and Zearley, 2020). It shows how the company's revenue reflects its net-profit. A company may have large amount in total revenue but the operational cost can cut down the profit to insignificant level. Formula of Net-Profit Margin,

$$\text{Net-Profit Margin} = (\text{Net-Profit} / \text{Revenue}) \times 100$$

| Year | Net-Profit | Revenue      | Net-Profit Margin |
|------|------------|--------------|-------------------|
| 2019 | 623,000.00 | 9,000,000.00 | 6.9%              |
| 2020 | 307,000.00 | 9,500,000.00 | 3.23%             |

#### *ROA Ratio*

ROA ratio is used to calculate the percentage of net-profit in relation with company's total asset in balance sheet. This ratio is for to evaluate company's efficiency in generating net-profit with the available assets (Fridson and Alvarez, 2019). Formula of ROA,

$$\text{ROA} = (\text{Net-Profit} / \text{Total Assets}) \times 100$$

| Year | Net-Profit | Total Assets | ROA ratio |
|------|------------|--------------|-----------|
| 2019 | 623,000.00 | 3,539,000.00 | 17.60%    |
| 2020 | 307,000.00 | 3,902,000.00 | 7.87%     |

### ***ROCE Ratio***

The ROCE is financial ratio that evaluates company's profit generation capability through using the employed capital efficiently (Oberholzer, 2017). This ratio is significant for both equity-holders and company's lenders. It is because, the ratio considers the investment employed by the both parties. Formula of ROCE,

$$\text{ROCE} = (\text{EBIT} / \text{Total Assets less Current Liabilities}) \times 100$$

| Year | EBIT       | Total Assets less Current Liabilities | ROCE ratio |
|------|------------|---------------------------------------|------------|
| 2019 | 633,000.00 | 2,684,000.00                          | 23.58%     |
| 2020 | 316,000.00 | 3,014,000.00                          | 10.48%     |

### **Liquidity Ratios**

Liquidity ratios are used by company's management and the investors to determine company's capacity to attain its current obligations. Having good liquidity ratio ensures that the company will not be in the risk of short-term loan default. But having too much liquid asset may impact the profitability (Subramanyam, 2018).

### ***Current Ratio***

Current ratio measures company's liquidity through simply comparing current assets company has to its current liabilities. It is both easy to calculate and interpret the result. Every company should have current ratio around 2:1 to prevent short-term loan default (Kolb and Rodriguez, 2018). Formula,

$$\text{Current ratio} = (\text{Total Current Assets} / \text{Total Current Obligations})$$

| Year | Current Assets | Current Obligations | Current ratio |
|------|----------------|---------------------|---------------|
| 2019 | 1,839,000.00   | 855,000.00          | 2.15:1        |
| 2020 | 2,152,000.00   | 888,000.00          | 2.42:1        |

### ***Quick Ratio***

Quick ratio is more specific and strict liquidity ratio as it only considers the current assets which have more liquid characteristics such as cash, receivables on account, securities that can be sold readily. These more liquid assets then compared with current obligations. Formula,

Quick Ratio = (Current Assets – Stocks) / Current Obligations.

| Year | Current Assets | Stocks     | Current Obligations | Quick Ratio |
|------|----------------|------------|---------------------|-------------|
| 2019 | 1,839,000.00   | 700,000.00 | 855,000.00          | 1.33:1      |
| 2020 | 2,152,000.00   | 750,000.00 | 888,000.00          | 1.58:1      |

### **Gearing Ratios**

Gearing ratios are financial matrices used in measuring debt compared to company's equity capital that the company requires to operate its business (Fridson and Alvarez, 2019). These ratios help to measure company's leverage amount and if the company is financially stable to run its operations.

### ***Debt-to-Equity Ratio***

This ratio indicates the use of debt in the company so that it can finance its assets compare to its shareholders' equity. There should be a balance in this ratio. Otherwise too much debt can risk shareholders' equity. Formula,

Debt-to-Equity Ratio = (Total Debt Amount / Total Equity Amount) × 100

| Year | Total Debt   | Total Equity | Debt-to-Equity Ratio |
|------|--------------|--------------|----------------------|
| 2019 | 1,005,000.00 | 2,534,000.00 | 39.44%               |
| 2020 | 1,038,000.00 | 2,864,000.00 | 36.24%               |

### ***Debt Ratio***

This ratio is used for determining how much contribution debt has on company's assets. It also indicates portion of assets that are obliged to the lenders. Formula

$$\text{Debt Ratio} = (\text{Total Debt} / \text{Total Assets}) \times 100$$

| Year | Total Debt   | Total Assets | Debt Ratio |
|------|--------------|--------------|------------|
| 2019 | 1,005,000.00 | 3,539,000.00 | 28.40%     |
| 2020 | 1,038,000.00 | 3,900,000.00 | 26.62%     |

## Understanding Essentialness of Financial Ratios in Hotel Management

Financial ratios are tools for the stakeholders of Jurys Inn to analyze and evaluate the performance of the hotel business. The management body of Jurys Inn use this ratio analysis company's financial strength, its weaknesses, its risks and take necessary actions to manage the situation. Hotel management is certainly a difficult job to successfully accomplish. The financial ratios are good helping tools for this challenging job. The following portion of the report will discuss the financial ratios' importance in hotel management.

### i) To Analyze Financial Statements

To manage a hotel like Jurys Inn in a successful manner, managers need to analyze the financial statements which provides essential data of the company's financial condition. Though financial statements provide raw data regarding company's financial performance, to fully interpret the data from financial statements managers and investors need to analyze them through financial ratios (Cote, 2018). Results of financial ratios give important insight regarding the financial statements and help the managers to take correct actions accordingly. The net-profit margin ratio of Jurys Inn shows that it dropped from 6.9% to 3.23% which less than half. Though the revenue increased 9,500,000.00 from 9,000,000.00, the net-profit margin shows opposite result as net-profit falls to 307,000.00 from 633,000.00. In here high revenue does not result in high net-profit which means the managers need to take necessary steps to reduce its costs to increase its net-profit.

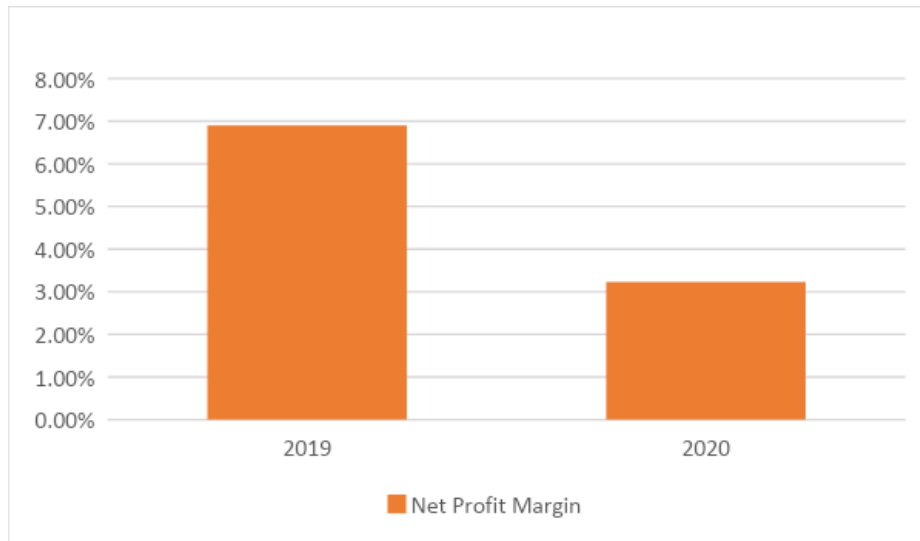


*Figure 1: Net-Profit Margin Ratio of Jurys Inn. Source: Author*

## ii) Understanding the Liquidity Condition of the Hotel

Though Jurys Inn is a company of service industry, it requires liquid assets to maintain daily operation and fulfill short-term obligations. For the maintenance of the hotel, hired labor must be paid in regular basis, food and sanitary suppliers need to be paid in a short-term and many other purposes the hotel needs maintain a strong liquidity (Brotherton, 2016). The Jurys Inn had good current ratios for both 2019 and 2020. In 2019 the hotel group had current ratio of 2.15:1 and it increased in 2020 to 2.42:1. The quick ratio which is stricter for liquidity also shows good sign for Jurys Inn. The quick ratio increases from 1.33:1 to 1.58:1.

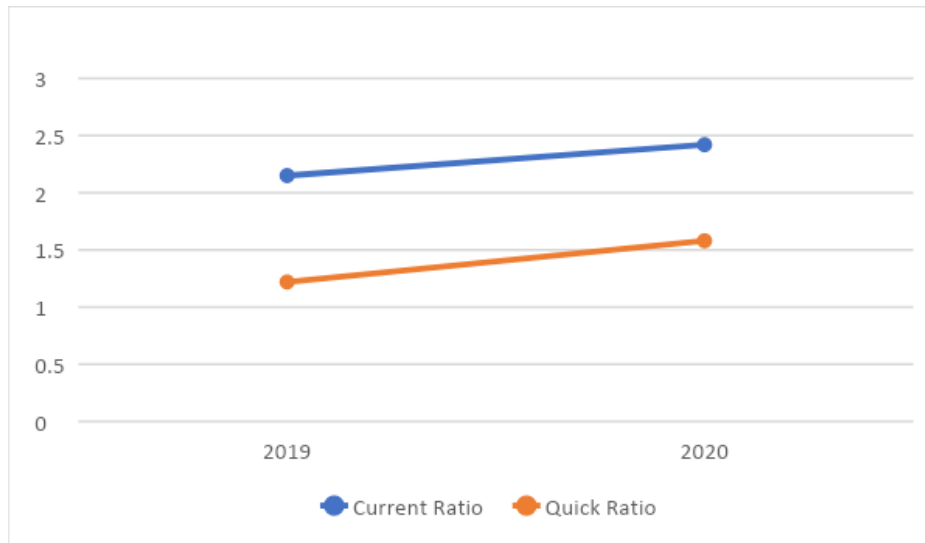


Figure 2: Current & Quick Ratios of Jurys Inn. Source: Author

### iii) Identifying Potential Risks of the Hotel

Financial leverage of a company is a great indicator of company's potential risks. Companies with high Debt-to-equity ratio are in the risk of high cost of debt or even bankruptcy (Gibson, 2016). Companies should of hotel industry should maintain a balance in its equity and amount of debt. Good balance of debt-to-equity ratio keeps both the risk and cost-of-capital low. The Jurys Inn had this ratio of 39.44% in 2019 and it decreased in 2020 to 36.24%.

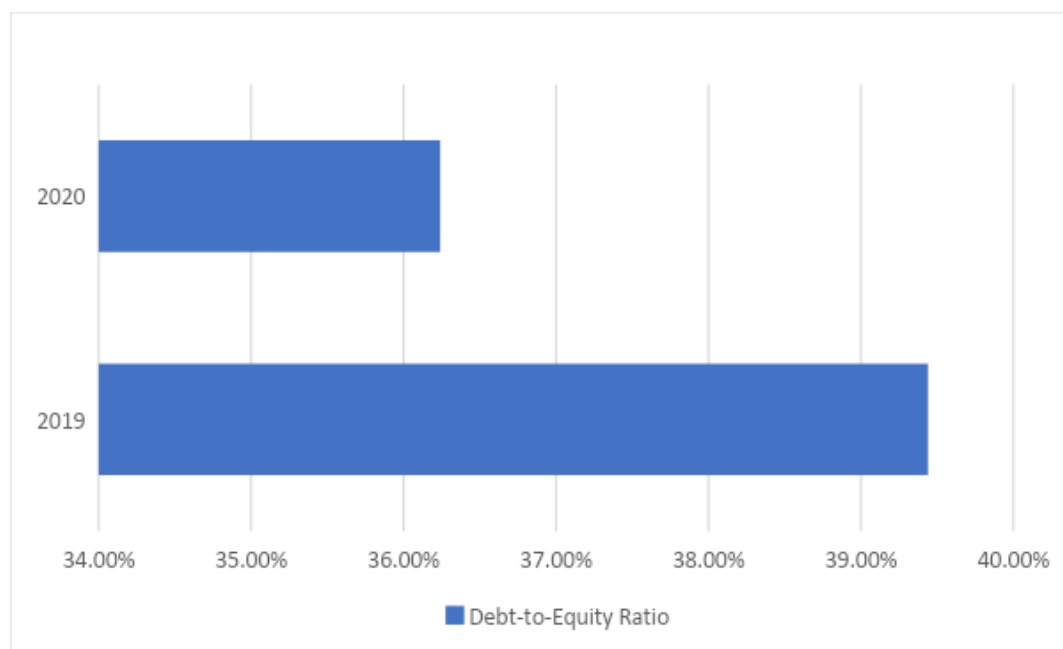


Figure 3: Debt-to-Equity Ratio. Source: Author.

# Beneficial Factors of Financial Ratios in Tourism Industry and Its Limitations

## Beneficial factors

### *i) Helps to identify which areas need improvement*

As the net-profit margin has decreased, it reflects that the Jurys Inn's revenue is not reflecting in high net-profits. The reduced amount of net-profit has affected every profitability ratios. The reason is that the cost of the company has creased significantly which reduced the net-profit. Therefore, the hotel group needs to control and reduce its costs to increase its net profit. Otherwise, high revenue will not result in high net-profit.

### *ii) Comparing with other companies in the tourism industry.*

Every hotel has its own financial structure and different values in financial statements. To compare financial performance of the companies in same industry there is no other way then financial ratio analysis (Kolb and Rodriguez, 2018). The financial ratios found from financial statements Jurys Inn can be compared with any other hotel and evaluate Jurys Inn's performance in the industry. A company can have stable financial ratio when comparing with its own ratios of different years but its would not give the complete idea of Jurys Inn's performance if the ratios are not compared with other hotels.

### *iii) Helps to understand the trend and future planning*

When financial ratios of Jurys Inn are compared over a period, financial analysts will find some trend in the company and also in the industry. If the trend of profitability is upward-slopping that indicates the company is continuously growing its business. If the trend is downward-sloping, the company must have done something wrong and it needs improvement. After analyzing the trend, the management can identify its necessary actions for the future. Therefore, the financial ratios also important for the tourism industry for its future planning.

## Limitations of Analyzing Financial ratios

### ***i) It is only useful for the companies in same industry***

Financial ratios of a company in hotel industry is only comparable to another company in hotel industry (Cote, 2018). It is because, companies in different industry have different financial requirement and can have different industry average for financial ratios. So, Jurys Inn's financial ratios can only be useful to compare with a company in hotel industry.

### ***ii) Ratios are subject to accounting assumptions***

To prepare financial statements accountants need to assume many things like depreciation, impairment, revenue recognition for long-term contract, etc. (Oberholzer, 2017). These assumptions changes for different financial periods which alters the result of financial ratios and make financial ratios irrelevant for comparison.

### ***iii) Use of different calculation methodology.***

There is lack of standardization of calculation methodology for financial ratios. If financial analysts of two different company in same hotel industry use different methodology to determine same financial ratio, the financial ratios will not be suitable for comparison. For example: to determine ROA, two different one financial analyst used average asset of the year while another financial analyst used the ending total asset. They will come up with different results which will be incomparable.

## Conclusion

Hotel industry in Europe is dynamic as new hospitality services like Airbnb are rising. To cope up with new business environment hotels like Jurys Inn need to be financially strong and capable to hold its position in the hotel industry. Though Jurys Inn's liquidity ratios and the gearing ratios are promising, the profitability ratio is very much uncomfortable for the company. It needs to improve its profitability to compete in the industry.

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