

BMTP 5013/D Financial Management for the Hotel Industry

Cost Behaviour

Register



Recap-What did we learn last week?

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- Demand and Supply

Question

- Why is it important for hotel companies to consider the unique characteristics of the hospitality industry?
- What is supply?
- What is demand?

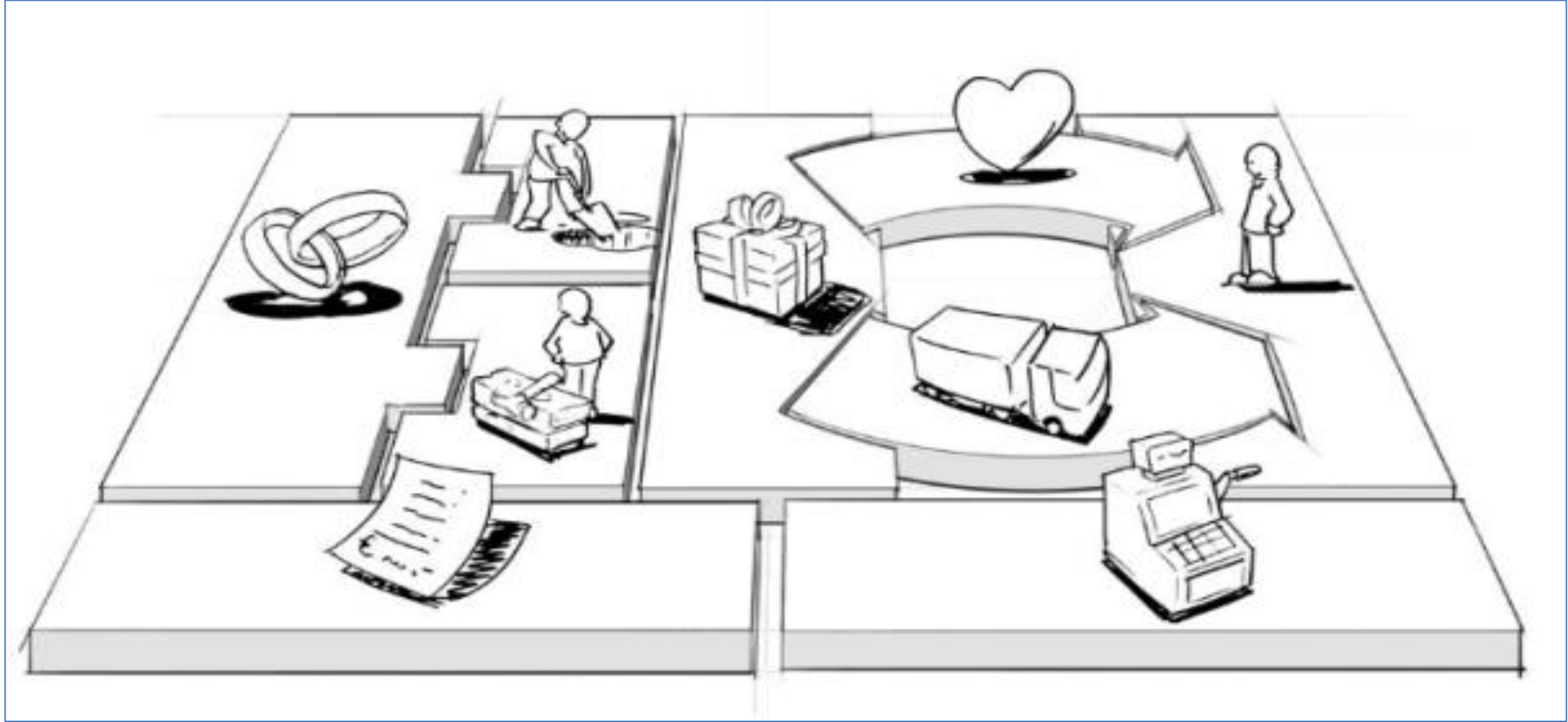
Where Are We Now?

Module:	Operations Management
Week	Lecture Topic
1	Introduction to Role of Financial Management in business operations
2	Hospitality and tourism industry characteristics and Financial Management implications
3	Introduction to Supply and Demand and financial planning
4	Cost structure
5	Introduction to budgeting
6	Revenue Management
7	Reading Week
8	P&L and Balance Sheet
9-11	Assignment Support
12	Assignment Submission

Today's Objectives

1. Discuss cost structure and its importance

Describe the picture below



Cost structure

What is cost structure?

Cost structure

- “The Cost Structure describes all costs incurred to operate a business model”
 - Creating and delivering value
 - Maintaining Customer Relationships
 - Generating Revenue
- Links to
 - Key Resources
 - Key Activities
 - Key Partnerships

Osterwalder and Pigneur, 2010



Cost Structure

Why should hospitality and tourism managers pay attention to their organisation's cost structure?

Cost Structure

- Understanding your cost is important for running a profitable business. A proper understanding of cost is needed to make some investment decisions, pricing decisions, deciding when to keep a product, keeping track of your overall business opportunity among many other things.
- Keeping track of cost is critical to make strategic business decisions. Cost structure, also can be termed as cost analysis. Mastering cost structure help to make solid business decisions.

Cost/Management accounting is:

- Optional, organisations do not have to use it (although most do in some form).
- Information may be approximate.
- More important to be timely than accurate.
- Can be produced for any segment of an organisation.
- There are no prescribed rules.
- Can be for periods in the past, present or future.
- Produced when required.
- Prepared for management.

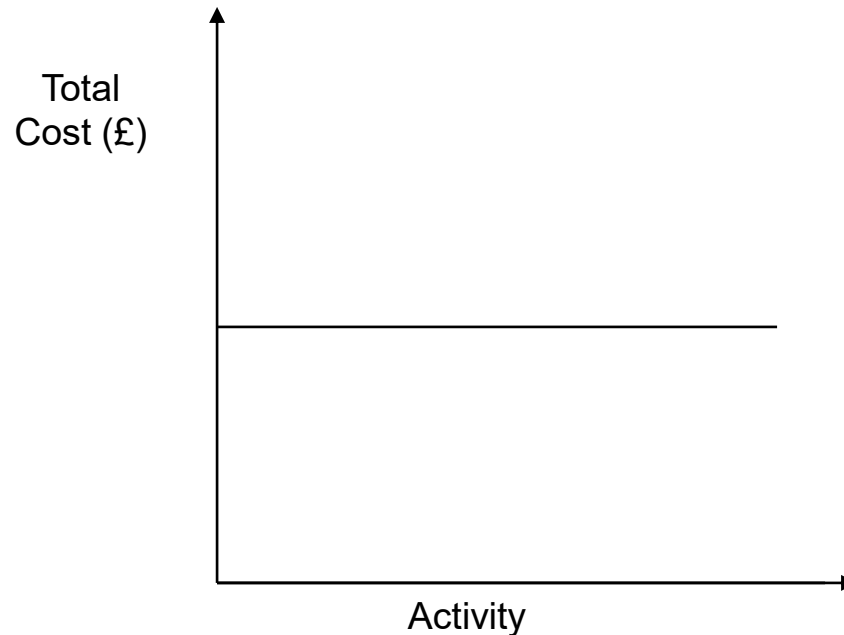
Cost Behaviour

If a business cost £750,000 to run last year, how much will it cost to run this year if business activity is forecast to increase by 25%?

Cost Behaviour

Fixed Cost

This type of cost is incurred for a period and within certain output limits tends to be unaffected by fluctuations in the level of output.

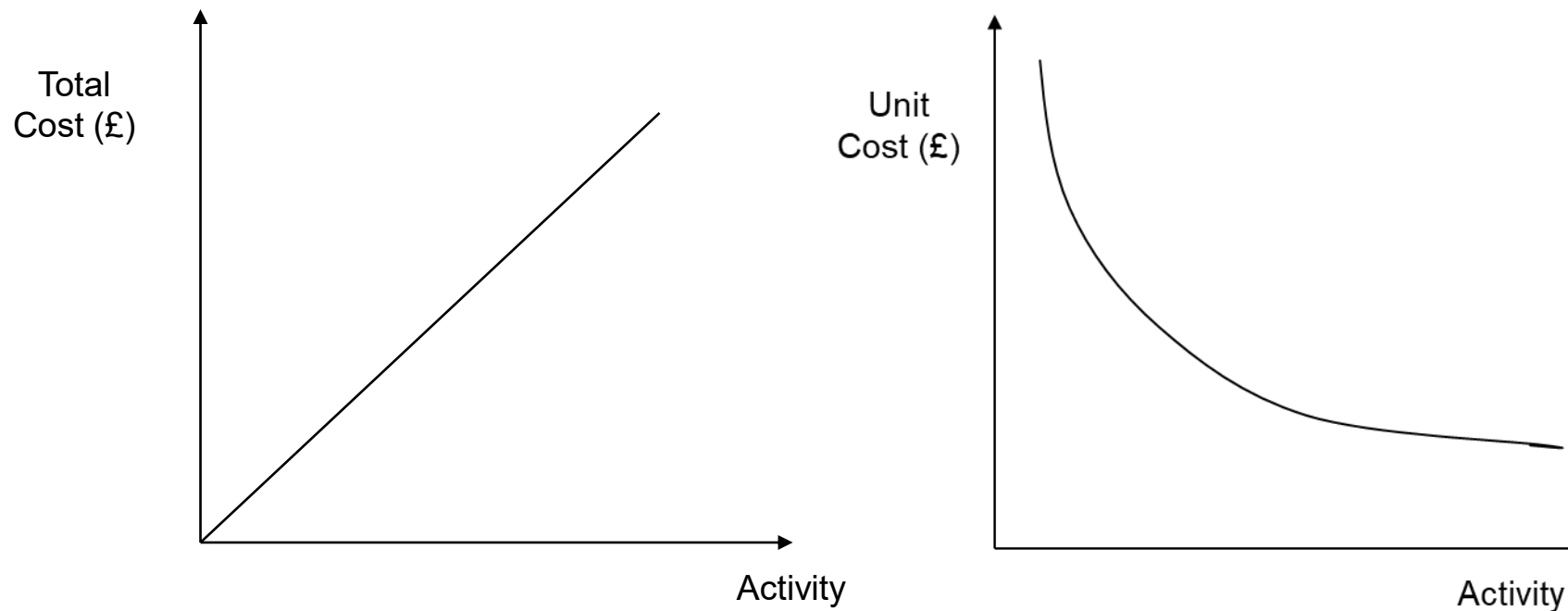


- Fixed Costs are sometimes known as capacity cost, since they result from outlays made for buildings, equipment, skilled professional employees and other items needed

Cost Behaviour

Variable Cost

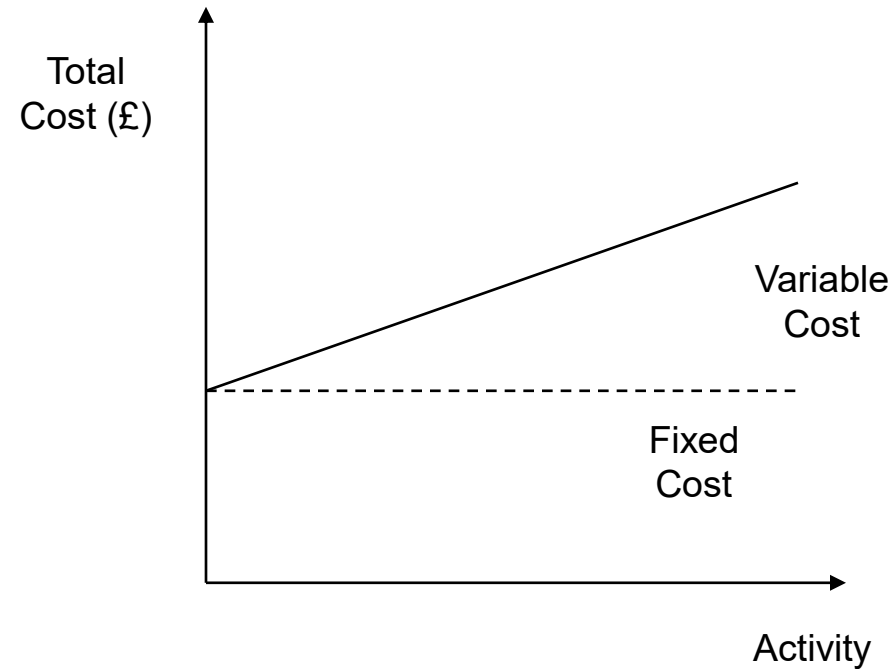
A cost which varies with the level of activity – the more that is produced the higher the cost.



Cost Behaviour

Semi Variable

A cost which has both a fixed and variable element.

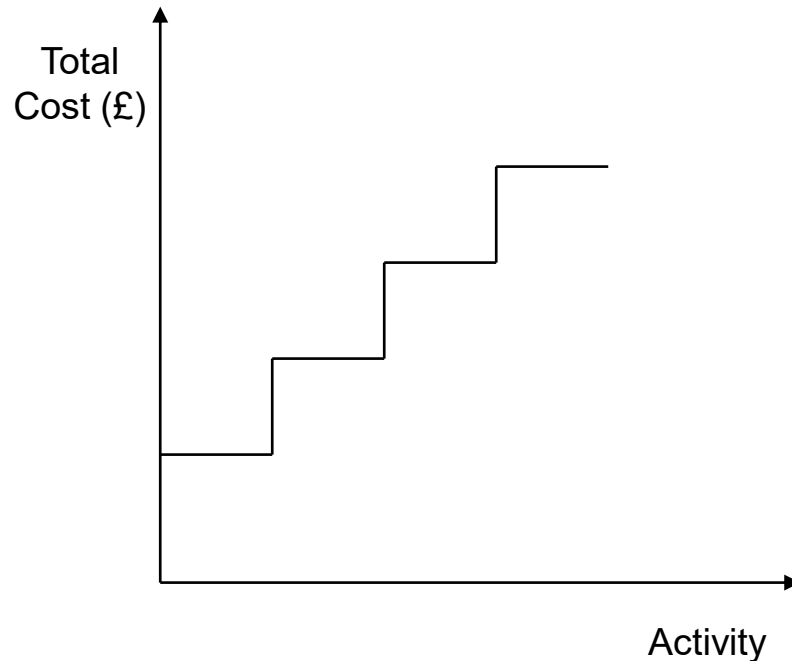


Cost Behaviour

Stepped Cost

A cost which is fixed for a particular range of activity levels, but once the upper limit of that range is passed a new higher level of fixed cost is incurred.

The engaging of resting/hibernating resources



Examples of Step Cost in Events

A stepped cost (also called step-fixed cost) remains constant within a certain level of activity but increases suddenly when activity exceeds a threshold. Unlike purely variable costs, stepped costs do not increase gradually—they increase in “jumps.”

1. An event requires:

- 4 security staff for up to 500 attendees
- 8 security staff for 501–1,000 attendees
- If attendance increases from 500 to 501, security cost jumps significantly.

The cost remains fixed within each attendance band but increases once capacity exceeds a threshold.

2. A conference venue holds up to 200 delegates.

If registrations exceed 200, the organiser must:

- Hire a larger venue, or
- Rent additional breakout space
- This creates a sudden increase in venue costs.

3. An event company may manage:

- Up to 3 events per month with current staff
- If a 4th event is added, a new event coordinator must be hired
- Salary costs jump once workload exceeds current staffing capacity.

Examples of Step Cost in Tourism

1. Hotel housekeeping staff. A hotel may:

- Operate with 5 housekeepers for up to 70% occupancy
- Need 2 additional staff when occupancy exceeds 70%

Labour cost increases in a step once demand passes a threshold.

2. Tour bus capacity. A tour operator:

- Uses one 40-seat bus for up to 40 tourists
- Must hire a second bus once bookings exceed 40

Transport costs jump when the first bus reaches full capacity.

3. Restaurant seating in a resort. A resort restaurant:

- Can serve 100 guests with one chef team
- Must hire an additional chef team if guest numbers exceed 100

Kitchen labour costs increase in a step rather than gradually.

Group Activity

Classify the following examples as either Variable Costs or Fixed Costs: raw materials expenses, sales commissions, direct labour costs, insurance, employee salary, and rent.

Group discussion

Which of these hotels is likely to be a riskier investment?

	Hotel A	Hotel B
Revenue	£600,000	£600,000
(-) Variable Costs	£390,000	£320, 000
(-) Fixed Costs	£60,000	£90, 000
Operating Income	£150,000	£190,000
(-) Interest	£10,000	£50,000
Net Income	£140,000	£140,000

Which of these hotels is likely to be a riskier investment?

	Hotel A	Hotel B
Number of Units Produced	£60,000	£60,000
Price per unit	£10	£10
Variable costs per unit	£6	£5
Fixed Operating costs	£60,000	£90,000
Fixed Financing costs	£10,000	£50,000

Hotel A and B analysis

Both hotels have the same **net income (£140,000)**, but the **risk profile** differs when we analyse their **cost structure** and **interest obligations**. Let's break it down.

- **Hotel A**
- **Variable Costs:** £390,000 (65% of revenue)
- **Fixed Costs:** £60,000
- **Interest:** £10,000
- Hotel A has **higher variable costs** and **lower fixed costs and interest payments**.
This means its costs fluctuate with sales, so if revenue drops, costs also fall — **lower financial risk**.

Hotel A and B analysis

- **Hotel B**
- **Variable Costs:** £320,000 (53% of revenue)
- **Fixed Costs:** £90,000
- **Interest:** £50,000
- Hotel B has **higher fixed costs** and **significantly higher interest expenses**.

This makes it more **leveraged** (i.e., reliant on debt financing) and **less flexible** in covering costs if sales decline — **higher financial risk**.

Hotel A and B analysis

Conclusion

- **Hotel B** is likely to be the **riskier investment** because:
- It has **higher fixed financial commitments** (fixed costs + interest).
- It is **more sensitive to revenue fluctuations**, meaning a downturn could quickly reduce profitability.

Hotel A, with lower fixed and financing costs, would be considered **safer** and more resilient to market changes



Case studies

Case Studies-Please refer to the word document

1. Hotel and Tourism case studies
2. Hospitality and Events case studies

25 minutes

Announcement

No Financial Management class on **Reading Week: Monday 26th - Friday 30th October 2026**

Lecture resume: **Tuesday 3rd November 2026**

If you have any questions in the
meantime, please send an email from
your student account

e.wavei@uwtsd.ac.uk

Next week.....

Revenue Management & Introduction to Budgeting