PART I

Introduction

1 The Need for Strategic Financial Management

LEARNING OUTCOMES

After reading this chapter, you should be able to:

- Understand why you need to study financial management.
- Define the key elements of financial management.
- Explain why finance is not accounting.
- Explain the importance of financial management today.
- Understand how to create your own financial management information system.

Introduction

Beautiful, glorious Canada is home to more than 40 million people and is very much a multicultural society with two official languages, English and French. Canada is a democratic nation with an advanced open market economy. Canada enjoys wide vast space; it is the second-largest country in the world in terms of land mass. To this end, Canada is a user-friendly nation for immigrants and it welcomes more than 1 million new settlers each year. Canada is attractive because it offers excellent education, health care, and job opportunities; it has safe communities; and, across most of the country, the population is sparse. An interesting fact is that most of the major cities, in which a large share of the country's population live, are in relatively close proximity to the US border. Some examples: Toronto, Canada's largest city with a population of almost 3 million, is about two hours away from Buffalo, New York by car; Calgary is three hours from the US border; Montreal is one hour away; and Vancouver is only 45 minutes away from the US border.

Canada is also a member of the G7 (the wealthiest seven nations in the world) with a 2022 **gross domestic product (GDP)** of about US$2,139.84 billion (Statista, 2022). Part of what makes Canada so prosperous is the success of its national tourism product, which caters to both domestic and international visitors. Before the onset of the Covid-19 global pandemic, Canada enjoyed almost 32.4 million international arrivals in 2019 (World Tourism Organization, 2022).

Gross domestic product (GDP)
The total value of goods and services produced in a defined region within a defined period of time

As you may conclude from the numbers provided above, Canada's hospitality and tourism industry should be, and is, a significant contributor to the national economy. The diverse and dynamic tourism industry is composed of several different sectors. These sectors include accommodations, commercial and institutional foodservice venues, commercial airlines, resorts, casinos, tour operators, golf courses, nightclubs, sports venues, and more. Each sector plays an important part in the Canadian economy and contributes to the finances of businesses, governments, and households alike. The accommodation sector alone generates about Cdn$22 billion in revenue each year (Hotel Association of Canada, 2022).

According to Statistics Canada, the tourism industry in Canada generally generates over Cdn$105 billion per year and makes up just over 2 percent of GDP (Statistics Canada, 2022). More than 1.9 million people are employed either directly or indirectly in Canadian hospitality- and tourism-related operations (Tourism HR Canada, 2022).

FIGURE 1.1 Front Desk Agents at Work

Source: Shutterstock

The industry's future looks bright because the Canadian federal government has made a commitment to support the industry in the years ahead. In fact, the Canadian government anticipates that tourism-related revenue will increase by 25 percent by 2025 (Western Economic Diversification Canada, 2019). As such, a wide and deep variety of exciting career opportunities exist within the industry today and they will continue to grow. Great news indeed for existing and aspiring professional hospitality managers!

Why Study Financial Management?

It is hoped that readers of this text will recognize the value and benefit of studying and obtaining a working knowledge of financial management. Accordingly, learning financial management concepts and tools should be considered imperative, not just desirable. This mindset applies to all people planning a career in hospitality finance or as successful professional hospitality operations managers in some capacity. Regardless of your career goals, either in the short term (perhaps you are working in the industry now) or the long run (you will work in the industry in the future), knowledge of financial management is important. Also, no matter what sector of the industry you prefer, a solid working knowledge of financial management skills and competencies is transferable, adaptable, and applicable—and will be critical for success in any type of hospitality operation.

One of the most important points to understand is that financial management concerns, goals, challenges, and victories permeate all facets of a hospitality enterprise. No hotel property, restaurant, operating division, or department is immune to the need for sound financial management. From ensuring there is enough cash on hand to cover payroll, to paying for that last food inventory shipment, to having the financial capacity to cover rising gas prices, to securing debt financing to pay for much-needed renovations, mastering financial management concepts and techniques will be extremely beneficial for anyone who wants a rewarding career as a hospitality professional.

Furthermore, there is a bonus that comes with studying and understanding the main tenets of financial management: what needs to be done in business finance is in many ways similar to what should be done in personal finance. The concepts, terminology, and methodology that are learned by studying hospitality financial management can and will be transferrable to your own personal finances. As you already know, the need to make wise financial decisions will affect you each and every day, whether at work, at home, or at play. The commitment to go to college or university on a full-time basis is a significant financial decision and a wise investment in your future. Even when you go out for dinner with friends, financial decisions will need to be made. For example, how much are you willing to spend on the meal? At the end of the meal, you must decide on who pays what, how much should be provided for a gratuity, and finally what the method of payment will be—cash, credit, or debit.

Thinking ahead and visualizing what your future work may entail, it's important to understand that prudent financial management is a key component of successful operations management in hospitality enterprises. The security, health, and vitality of a hospitality enterprise's financial performance and position will be influenced by the financial manager's capabilities. Nevertheless, despite the best efforts of hospitality managers, financial outcomes will also be shaped by both internal and external factors.

Managers can control the internal elements, and therefore management can plan, implement, and evaluate financial performance on a consistent and timely basis. Internal elements include things like pricing policies, menu design, hours of operation, level of service, human resources policies, quality of product, guest satisfaction, working environment comfort, and employee morale, for example. Furthermore, strong financial management requires ongoing analyses so that smart decisions will be made, leading to prudent actions that will ultimately improve the financial success of the enterprise. The financial manager needs to compare and evaluate actual results to what was planned or expected, and make the required adjustments with the resources available on a timely basis so that there will be continuous improvement.

However, the external elements will always be more difficult to deal with, because management has little to no control of these variables. Government policy, weather, consumer behaviour, foreign direct investment, geopolitical events, the macroeconomic climate, and competitive actions are just some examples of the many factors that shape the external operating environment. Other factors may not have been given consideration or even thought to be possible—for example, the Covid-19 global pandemic that began in 2019.

In light of all this, the management team must be well prepared so that, if something adverse and unexpected takes place, the hospitality enterprise will be able to sustain itself financially during the negative event (e.g., riot, construction, pandemic, wildfire, fierce competition, earthquake, snowstorm, union strike, or tornado). It is crucial for management to have an effective and efficient external information capture and analysis system so that the political, economic, competitive, and technological environments are monitored constantly, without prejudice, and appropriate actions are taken when necessary, in a timely manner.

Financial crises are another compelling reason it is so important to harness financial management skill sets and competencies. Looking back through the years at the difficulties encountered in Canada and around the world when financial crises take place, these events need to be carefully considered and evaluated. Undertaking this historical review and understanding what happened is a good first step to recognizing the important value of sound financial management.

Historical Considerations

The Great Depression (1929–1939)

This historical assessment begins with the Great Depression, which was one of the worst financial crises of all time. It began in 1929 and lasted until 1939. A whole decade of unprecedented financial hardship was experienced in Canada and the throughout the world. More specifically, between 1929 and 1932, worldwide GDP fell by more than 15 percent (Lowenstein, 2015). Some economists have put that number as high as 20 percent, which in perspective is quite staggering. This point is relevant because GDP is an accurate indicator of the quality of life or standard of living for a particular country, province, state—or the world, for that matter. As a result, if there is a large decline in the GDP, one can assume that the quality of life and the standard of living has fallen sharply as well. In fact, the evidence supports this: unemployment rose dramatically and inflation increased, the supply of money decreased, and industrial production fell by almost 50 percent (Amdeo, 2022). This significant financial disaster caused considerable financial pain around the world. Millions of people became unemployed, hungry, and homeless, and they almost entirely lost trust and confidence in governments and financial institutions. Also, because financial institutions were failing, there was a run on the banks (panic withdrawals from demand deposit accounts), which made the situation significantly worse by placing greater demand on a depleted money supply. Many economists believe that the Great Depression was brought on by excess industrial production capacity, heavy and burdensome debt loads, and a significant drop in demand for both domestic and international goods and services. Putting these ingredients together all at once made for a very bad financial cocktail. This severe hardship endured by the global community has also been referred to as the "dirty 30s."

That nickname was very appropriate here in Canada due to the significant drought experienced on the prairies during that time. In fact, the drought was so crippling that the prairies became known as the "Dust Bowl," because the drought produced ongoing severe dust storms, and therefore it was not possible to grow any agricultural products. This, of course, caused heartbreaking despair to Canadian farmers. The lack of agricultural goods being produced and sold only compounded the financial stress Canada was already experiencing.

This period of financial difficulty got no help from mother nature. Instead, the weather contributed to making a bad situation worse by not providing much-needed rain on the prairies. As a result, the value of Canadian wheat fell significantly in the global export market, which caused many settlers in Alberta, Saskatchewan, and Manitoba to give up and move to either British Columbia or Ontario to start again and hopefully improve their lives.

Like in other countries around the globe, certainly millions of Canadians became unemployed, hungry, and homeless during the 1930s. It was an extremely difficult time for Canada and Canadians. In hindsight, many experts believe that if appropriate financial management had been undertaken by the government, the central banks, financial institutions, and households, perhaps the Great Depression would not have been as severe as it was. On a more positive note, many valuable lessons were learned by governments, economists, and financial managers from what was most definitely a very difficult time, the renowned dirty 30s.

The Great Financial Crisis (2007–2010)

Continuing this historical financial journey, we now fast forward to 2007–2010, when the world experienced the Great Financial Crisis, also known as the Great Recession or the Global Financial Crisis. This unexpected circumstance was not as bad a financial disaster as the Great Depression in terms of time and GDP performance. The Great Financial Crisis lasted about 19 months, in comparison to a whole decade for the Great Depression (Bondarenko, 2022). Also, the US economy contracted only about 4 percent during the Great Recession, in comparison to about 30 percent during the Great Depression (Duignan, 2022). In 2008–09, the Canadian economy entered a recession. The main contributing factor was the US housing bubble. As such, Canadian GDP fell by 3.3 percent due to a significant decline (16 percent) in exports. Additionally, investments in buildings and machinery decreased by 22 percent (The Canadian Encyclopedia, 2023).

However, this more recent financial crisis still created a significant amount of uncertainty with respect to the behaviour of government and financial institutions. It was brought on mostly by the poorly managed (with little to no oversight) subprime mortgage market, which led to a significant US housing bubble (a run on housing demand fuelled by speculative buying) that eventually popped in a big way. As a result, business and consumer confidence plummeted and stock exchanges around the world started to lose total capitalization value (caused by investors selling off their asset portfolios) at an alarming rate. In Canada, the Toronto Stock Exchange (TSX) lost over 5,000 points (a third of its value) in 2008 as Canadian investors took their money to the sidelines (CBC News, 2009). Accordingly, consumers once again lost faith, trust, and confidence in governments and financial institutions.

One of the unexpected by-products of this change in consumer attitude and perception was the sudden growth in the acceptance and popularity of digital currency—and in particular Bitcoin and the use of blockchain technology—as investors and households sought out alternatives to traditional investment conventions and platforms. Holders of Bitcoin and other cryptocurrencies were convinced that using this unit of currency, store of value, or medium of exchange was less volatile and risky than continuing to use government currency. This phenomenon will be discussed along with the use of blockchain technology for financial management in Chapter 5, Financial Instruments.

It is important to recognize that the international financial community can be affected (for better or worse) by what is taking place in one country or one part of the world. As such, one needs to understand that the macro financial community is truly international and interconnected. If there is a negative impact on one country's finances, it is only a matter of time before that negative impact influences other countries' financial status and well-being. For an example of just how closely knit the international financial community is today, look at the **Society for Worldwide Interbank Financial Telecommunications (SWIFT)** payments system, which expeditiously handles millions of financial transactions, both domestic and international, around the globe every day. These financial transactions, predominantly payments and demand deposits, include the use of credit cards, debit cards, cheques, and of course the electronic transfer of good old cash. As a result of the SWIFT banking infrastructure, financial transactions that used to take weeks to complete can be accomplished relatively quickly, usually within 24 to 48 hours in Canada, the UK, Europe, and the United States. In other countries it may take up to five days or, as is the case with India, it could take as long as three months (B2BPay, 2022).

Society for Worldwide Interbank Financial Telecommunications (SWIFT)
Payment system that handles millions of financial transactions across the world every day

Cycling back to financial crises and thinking about the international financial community, both the Great Depression and the Great Financial Crisis originated in the United States, but these events affected the financial well-being of other countries around the world, including Canada. And, of course, they had an impact on the global hospitality industry as well.

The Great Financial Crisis of 2007–2010 hit the United States particularly hard, and many argue that it was significantly more painful, financially and emotionally, than the Great Depression of 1929–1939, just due to the size and scope of the collateral financial damage that occurred between 2007 and 2010.

The Great Financial Crisis affected millions of Americans. Many ended up losing their jobs or becoming homeless. Those who were able to hold onto their homes were left with negative equity as the crisis caused many homeowners to have "upside-down mortgages," where the mortgage became worth more than the actual market value of the house.

Additionally, many financial institutions (banks, insurance firms, and trust companies) had to be propped up by governments and some legacy financial institutes, such as Lehman Brothers in the United States, ended up going bankrupt and closing their doors forever.

Black Monday (1987)

Continuing this review of financial crises, it is important to mention the financial disaster known as Black Monday. Black Monday occurred on October 19, 1987. The world's largest stock exchange, The New York Stock Exchange (NYSE), went into almost total freefall as investors were selling their stocks as quickly as possible.

In particular, the Dow Jones Industrial Average (an index of the NYSE) lost 22 percent of its capitalization value in one day, causing an immediate stock sell-off on other exchanges around the world (Corporate Financial Institute, 2022). Retail investors (everyday people) as well as institutional investors (banks, insurance firms, investment houses, etc.) all became involved in panic selling until stock market activity was suspended by the Securities and Exchange Commission (SEC). Suspending trading provided the SEC and other authorities and regulatory bodies time to investigate and provide information to the public as to what specifically had happened and why panic selling was happening.

In hindsight, most financial experts attribute Black Monday to a combination of geopolitical events: (1) the Kuwait and Iran missile crisis and (2) a significant worldwide spike in the price of oil combined with the growing acceptance and use of computer-assisted trading software (CATS). CATS can either directly or indirectly cause investors to sell their stock holdings prematurely, thus leading to a wholesale market decapitalization like what occurred on Black Monday. This can happen because CATS uses the Internet to receive a live market data feed. If a stock starts to decline and reaches a certain market value (known as a "trigger point") then the software will automatically start to sell that stock. As you can imagine, if the significant institutional investment firms start selling off a stock in large volumes, other traders will almost certainly take notice and follow suit, even if they do not know why a sell-off is taking place (due to both a follow-the-leader and herd mentality). This is obviously neither a good nor healthy market scenario. Fortunately for the investing public, as well as governments and market economies around the world, changes and improvements have been made to CATS so that this type of event will probably not occur again in the future.

Covid-19 Global Pandemic (2019–2023)

Finally, the Covid-19 global pandemic of 2019–2023 must be included here as well. It is believed that the Covid-19 virus originated in Wuhan, China. The first case in Canada was identified in Toronto on January 23, 2020 and confirmed on January 25, 2020. A 56-year-old man who had recently travelled to Wuhan and had returned to Toronto fell ill. This man was admitted to and successfully treated at Toronto's Sunnybrook hospital (Ogilvie, 2020).

As a result of the Covid-19 pandemic, an economic loss of about US$7,592 billion, a decrease in the GDP of about 31 percent, occurred in the United States during the first year alone (Kornreich, 2022). In Canada, the unemployment rate rose to 13.5 percent, the highest it had been since 1976 (Tencer, 2020). The total dollar value cost for Canada has been pegged at more than Cdn$1.5 billion per day during 2020 (Lorinc, 2021). This health crisis created another significant financial crisis, evidenced by the large and small businesses that had to close their operations until public health guidelines and protocols could be established and put into action (see Figure 1.2).

Canada endured almost 4 million cases of Covid-19, resulting in approximately 42,000 deaths. The Covid-19 pandemic wreaked havoc on the Canadian economy and ravaged the Canadian hospitality and tourism industry.

The Accommodation Sector

Canada's accommodation sector is quite extensive. According to the Hotel Association of Canada, there are about 8,300 accommodation properties with around 461,000 guest rooms located across the country, which employ almost 310,000 individuals (Hotel Association of Canada, 2022).

Within the accommodation sector, there are three key performance indicators (KPIs) that serve as guideposts to how well a property or the sector in general is performing from a financial management perspective. These three KPIs are (1) average daily rate (ADR), (2) rooms occupied percentage, and (3) revenue per available room (RevPAR).

In 2019, before the pandemic, the ADR, which is calculated by dividing total rooms revenue by the number of rooms sold for the day, was Cdn$164. In 2020, it dropped down to Cdn$129 (Canadian Press, 2021). This illustrates that the pandemic had a significant negative impact on Canadian ADR values in that first year of the pandemic. In 2023, the accommodation sector began recovering toward pre-pandemic performance ADR.

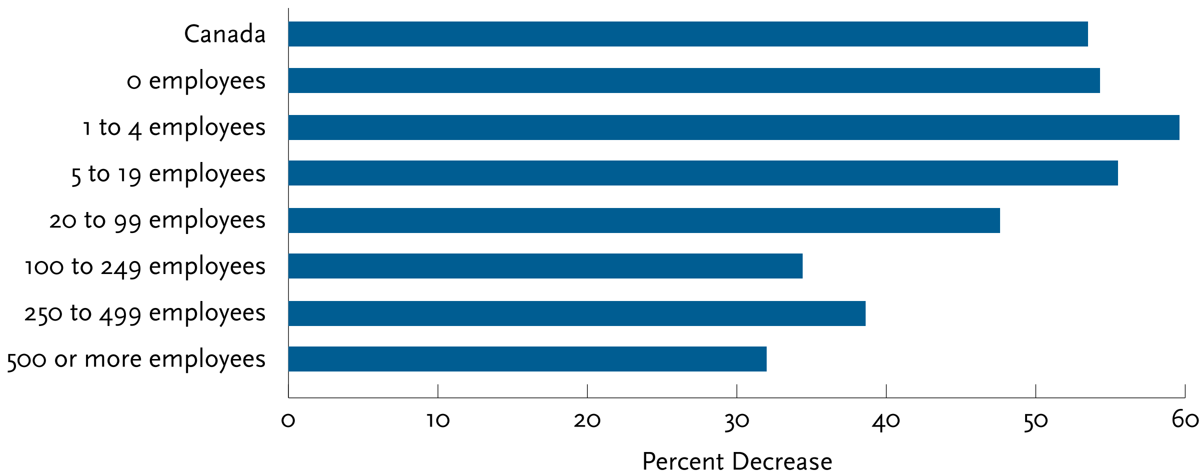
Also, for accommodation properties, the rooms occupied percentage or occupancy (Occ %) is calculated by dividing the total number of rooms occupied by the number of rooms available for sale. In Canada, the Occ % was 65 percent in 2019, 33 percent in 2020, and about 40 percent in 2021 (Canadian Press, 2021). It is important to note that most accommodation properties require at least 60 percent occupancy to break even (meaning that total revenue is equal to total costs). As a result of these dismal occupancy values, a lot of Canadian properties were forced to shut rooms or entire floors. Other properties made the decision to pause or shut down operations entirely because of the heavy financial losses they were incurring.

The third KPI within the accommodation sector is revenue per available room or **RevPAR.** This is calculated by multiplying the ADR by the Occ %. RevPAR is the most meaningful performance metric for accommodation properties because it identifies how efficiently the property is generating revenue. For example, ADR might be on the increase, but if the Occ % is decreasing at a greater pace it means the RevPAR will go down. Or the opposite could take place, where ADR is decreasing at a greater rate than the Occ % is increasing and once again RevPAR will go down.

RevPAR
Revenue per available room

For Canadian properties, RevPAR was Cdn$107.80 in 2019 (Smith Travel Research, 2020), Cdn$42.57 in 2020 (Smith Travel Research, 2021), and Cdn$58.10 in 2021 (Smith Travel Research, 2022). These are disappointing RevPAR values for 2020 and 2021. The 2022–2023 RevPAR values continued trending upward as travel bounced back from pandemic lows.

FIGURE 1.2 Impact of COVID-19 on Business Revenue in Q1 2020



Note: Employment levels were self-reported by respondents. Respondents were asked to exclude business owners, contract workers, and other personnel who would not receive a T4.

Sources: Canadian Survey on Business Conditions: Impact of COVID-19 on businesses in Canada, March 2020 (Table 33-10-0234-01).

The Foodservice Sector

The foodservice sector is also a major contributor to the Canadian economy. According to Restaurants Canada, prior to the Covid-19 pandemic there were almost 100,000 foodservice operations in Canada employing 1.2 million people and either directly or indirectly generating more than 4 percent of Canada's annual GDP (Restaurants Canada, 2018).

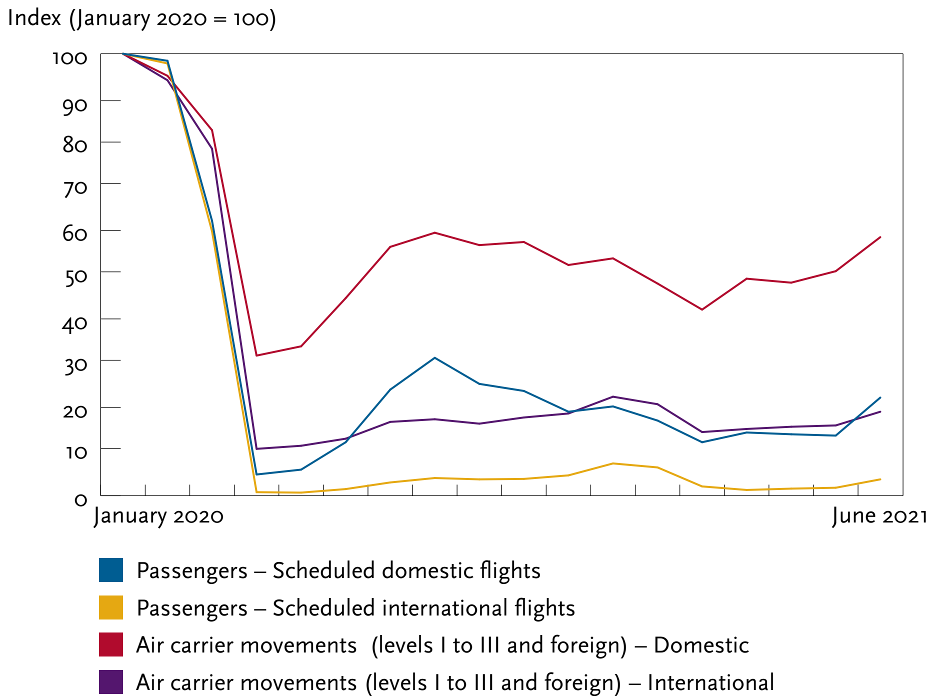
During the pandemic, the Canadian foodservice sector lost over 10,000 restaurants and about 400,000 jobs (Restaurants Canada, 2021a). Operations that did survive the pandemic were creative in offering home meal kits, curbside service, take out, and home delivery. Most foodservice operations were in a weak financial position and had to take on additional debt to stay afloat, even if it meant that they were barely functioning at or around their break-even point. Once again, this highlights the need for financial management acumen.

Commercial Aviation Sector

In 2020, international passenger arrivals across the globe were down by 74 percent in comparison to 2019. This significant decrease in international travel translated into an estimated loss of US$1.3 trillion in global export revenues as international tourism is considered an export for the host tourism nation (Hiltner & Fisher, 2021).

In Canada, the federal government imposed international travel restrictions beginning in March 2020. As a result, from March 2020 to July 2021, air passenger volume declined by a massive 88.3 percent (Statistics Canada, 2021). This is shown in Figure 1.3.

FIGURE 1.3 Decline in Airline Passenger Volume 2020-2021



Sources: Statistics Canada (https://www150.statcan.gc.ca/n1/daily-quotidien/210826/cg-b001-eng.htm)>

Additional consequences of the pandemic on the commercial aviation sector of Canada's hospitality and tourism industry include Canada's second-largest (WestJet), third-largest (Air Transit), and fourth-largest (Porter) airlines all suspending or cancelling flight operations to some degree (Neustaeter, 2020). Air Transit and Porter stopped all flights for several months and furloughed most of their employees as revenue generation came to a complete stop. It was just not financially viable to try to maintain the status quo. Canada's largest airline and legacy carrier, Air Canada, continued to fly, but with both reduced routes and decreased service frequency, making air travel extremely difficult and uncomfortable (Evans, 2021). Air Canada also endured severe financial hardship; it lost about Cdn$20 million per day at the height of the pandemic (Canadian Press, 2020).

Globally, all airlines were forced into a precarious position; due to the pandemic and public health concerns they had to cancel flights, costing them millions of dollars in lost revenue. On the flip side, as airlines began recovering, they faced staff shortages (CBS New York, 2021). With so many pilots, ground crews, mechanics, and flight attendants either let go or furloughed, it was a real challenge for airlines to rehire staff members effectively. Canadian airports faced their own labour difficulties in accommodating the significant increase in passenger volume beginning in 2022. During the pandemic, airports also let staff members go, and many of those individuals have chosen not to go back to work in airports as transportation safety officers, airline food service personnel, counter service agents, merchant sales representatives, and other roles.

The Covid-19 pandemic caused a serious economic contraction in Canada and around the world. The hospitality industry was hit hard, both domestically and internationally, as people stopped travelling for leisure and business meetings, conventions, and special events were cancelled. As a result, many Canadian accommodation providers, airlines, and foodservice entities either suspended service, closed, or scaled back operational capacity, leading to substantial financial challenges and pain.

Many valuable lessons have been learned from these financial crises, such as the need for improved CATS, financial managers with strong competencies and skill sets, knowledgeable investors, greater government oversight, and the promotion of financial management education. Many governments today support starting financial management education (sometimes called financial literacy) at the high school level.

Through financial difficulties such as the Great Depression, the Great Financial Crisis, Black Monday, and the Covid-19 global pandemic, the world has certainly been disrupted and challenged. More recently, on February 24, 2022, Russia invaded Ukraine. Since the conflict in Ukraine's Crimea region has existed since 2014, most military experts believe that it will be years before absolute peace is restored in that part of Eastern Europe. This military conflict has caused more stress on a worldwide logistical supply system that was already under pressure because of the Covid-19 pandemic. The logistical supply chain that most have taken for granted in the past has dealt with mass layoffs, extended factory shutdowns, and closed borders during the pandemic.

Russian Invasion of Ukraine in 2022

The international tourism industry had just begun a healthy recovery from the Covid-19 global pandemic at the start of 2022. Unfortunately, that positive development became somewhat compromised as the industry experienced the negative impacts of Russia's invasion and illegal occupation of parts of Ukraine.

In 2022 and 2023, most of the world imposed economic sanctions on Russia. In turn, Russia instructed the domestic population to remain in Russia and not travel. Russians spent US$22.5 billion on international travel in 2019 and represented a significant proportion of tourists patronizing European countries. Turkey, Spain and Italy, are favoured destinations. Russians also like to travel to China and Thailand.

The Russian invasion of Ukraine had a negative impact on international travel by air and caused a disruption in flight schedules in terms of frequency and routes available throughout most of 2022. Travel by land in Eastern Europe was also adversely affected. These were additional challenges to the international hospitality industry and forecasted revenues from international guests needed to be revised accordingly.

Macroeconomic Environment

Adding to the supply management stresses being felt by businesses and consumers alike, in 2023 both Canada and the United States were also experiencing the highest inflation rates they had seen in several decades. At the time of this writing, Canada had a 7.7 percent inflation rate and was experiencing its highest and fastest-growing cost of living since 1991. Unfortunately, Canada's inflation rate was not within the desired target range. The Bank of Canada mandate clearly states that Canada should have an inflation rate within the 1–3 percent acceptable band. A 7.7 percent or higher inflation rate is simply too high. To make matters even worse, Canada was in a period of **stagflation** in late 2022, where there is high inflation and unemployment and relatively stagnant GDP growth. This creates serious challenges for a financial management team.

Stagflation
A period in which there is high inflation, high unemployment, and low GDP growth

In the United States, a similar situation occurred. Their inflation rate was at 8.6 percent in 2022, the highest since 1981. The ugly problem that results from high inflation in Canada, the United States, or elsewhere, is that it takes more dollars to purchase the same basket of goods or services, relatively speaking, because the purchasing power of the dollar is reduced. This places more stress on the financial management team. In a high inflation period, it is more important than ever to have financial management skill sets.

The external shocks outlined in this section have caused significant and, in some cases, almost irreparable financial damage to the Canadian hospitality and tourism industry. As identified above, one can look at each sector of the industry: airlines, accommodations, foodservice, entertainment, and tourism, and the same conclusion can be drawn—that is, severe financial hardships have occurred and may continue for years to come because business and consumer confidence have deteriorated and business risk has intensified because of rising interest rates, a stagnant economy, and a decreased money supply. As we can see from history, as well as the current challenges in the hospitality and tourism industry, the need for sound, pragmatic financial management has become greater than at any other time in the modern era. Learning as much as possible about financial management concepts, tools, models, techniques, and methodology is more than justified as a robust and wise investment in your professional hospitality management career.

What is Financial Management?

As acceptance of the importance of and need for pragmatic financial stewardship, this conversation should begin with an examination of the meaning and purpose of financial management. What exactly is financial management? Within the business community, many would say that it represents all the actions and processes of planning, organizing, directing, controlling, and adjusting the entire organization's financial elements and concerns (see Figure 1.4). Planning is a good place to start as you work through an understanding of financial management.

Planning

The first step in astute financial management involves **planning**. The financial management team must understand the hospitality entity's current financial situation and think about the appropriate course of action to be undertaken to ensure that the operation has sufficient cash on hand to pay short-term maturing financial obligations as they come due; for example, meeting payroll requirements and tax obligations, or paying vendors and suppliers for goods and services received. Planning also requires ensuring that there is sufficient borrowing power in place should the need arise to establish debt financing, or having a strong asset value and ability to generate revenue should the hospitality enterprise try to attract more capital, either privately or publicly. The requirements for successfully raising capital will be discussed in Chapters 5, 6, and 9.

Planning
Developing a company's vision, mission, and goals as well as articulating the tactics and strategies that will be used to successfully achieve these objectives

Planning involves thinking about and committing to a strategic action plan that will accomplish what the organization needs. Planning requires reviewing current resources (human, financial, physical, and organizational) and matching existing resources to what is required to achieve the company's mission, goals, and objectives.

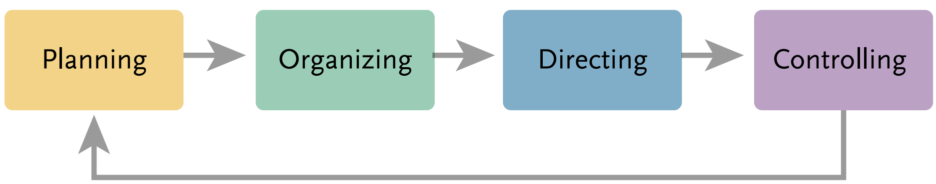
The planning process must also take into consideration the needs of the owners and/or investors. The financial manager must ensure that those who have made a financial commitment to the operation are satisfied with the return they are receiving on their invested funds.

Financial controls, policies, procedures, internal regulations, and oversight are all part of the planning process as well. These are necessary management elements that will help increase the probability that the operation will be financially secure and successful.

Organizing in financial management is the process by which the strategic financial plans can be successfully executed. This is carried out by comparing resources on hand to resources that are required for the task at hand. This review should

Organizing
The assignment and deployment of required resources to achieve the company mission, vision, and goals

FIGURE 1.4 The Financial Management Process



provide management with confirmation that the resources required are available for deployment.

Management will also formulate the mission and objectives to be achieved by the hospitality enterprise. These charter elements will speak to financial goals and requirements. The identified and agreed-upon company mission will be accomplished by ensuring the right resources (human, financial, organizational, and physical) have been deployed, embraced, and leveraged at the right time and location for each specific task or objective in the strategic plan. This includes having qualified individuals (the management team and subordinates), proper equipment and tools (e.g., computers and software), organizational resources (policies and procedures), and clear articulation of timelines and objectives (an implementation schedule). The hospitality enterprise wants to utilize its resources to an ideal capacity that will translate into a strong strategic financial position for the organization. For example, Mr Johnny Canadian has over 20 years of financial management experience, holds an undergraduate degree in hospitality management, is a Chartered Professional Accountant (CPA) as well as a Certified Financial Analyst (CFA), and is working as a financial performance analyst for the Great Canadian Hotel Company. As one can see, Mr Canadian would be a valuable employee and is an excellent fit in that position for the hospitality firm.

FIGURE 1.5 An Example of Output Generated from Financial Planning

Five Year Financial Plan Output
Project Template
The Great Canadian Hotel Company

		2026	2027	2028	2029	2030
Income Statement Summary	Revenue	$57,892,000	$59,049,840	$60,230,837	$61,435,454	$62,664,163
	Direct Costs	$21,998,960	$22,438,939	$22,887,718	$23,345,472	$23,812,382
	Gross Margin	$35,893,040	$36,610,901	$37,343,119	$38,089,982	$38,851,781
	Fixed Costs	$18,000,000	$18,360,000	$18,727,200	$19,101,744	$19,483,779
	Earnings Before Tax	$17,893,040	$18,250,901	$18,615,919	$18,988,238	$19,368,002
	Tax Expense	$4,294,330	$4,380,216	$4,467,821	$4,557,177	$4,648,320
	Net Income	$13,598,710	$13,870,685	$14,148,098	$14,431,061	$14,719,682
Balance Sheet Summary	Total Current Assets	$21,000,000	$24,833,122	$28,742,906	$32,730,887	$36,798,626
	Total Fixed Assets	$187,562,000	$191,313,240	$195,139,505	$199,042,295	$203,023,141
	Total Assets	$208,562,000	$216,146,362	$223,882,411	$231,773,182	$239,821,767
	Total Current Liabilities	$17,582,026	$17,933,667	$18,292,340	$18,658,187	$19,031,350
	Total Long Term Liabilities	$129,632,478	$132,225,128	$134,869,630	$137,567,023	$140,318,363
	Total Equity	$61,437,496	$65,987,567	$70,720,441	$75,547,972	$80,472,054
	Total Liabilities and Equity	$208,652,000	$216,146,362	$223,882,411	$231,773,182	$239,821,76
Cash Flow Summary	Cash from Operating Activities	$574,326	$585,813	$597,529	$609,479	$621,669
	Cash from Investing Activities	$2,258,796	$2,303,972	$2,350,051	$2,397,052	$2,444,993
	Cash from Financing Activities	$1,000,000	$1,020,000	$1,040,400	$1,061,208	$1,082,432
	Net Increase in Cash	$3,833,122	$3,909,785	$3,987,980	$4,067,739	$4,149,094

Directing

Directing is the process whereby managers provide guidance and instructions to oversee the performance of employees. Managers will communicate, coach, and monitor work progress to ensure resources are moving in the right direction, at the right time, the right cost, and the right pace to ensure that the mission and objectives of the enterprise will be achieved.

Directing
The provision of specific instructions, communication, coaching, and leadership to ensure the company mission, vision, and goals are achieved

Directing is often overlooked. This is unfortunate because directing is very important—it is warmly referred to as the heart and soul of the management process. This makes perfect sense logically, because if management is not providing direction and guidance for the employees then where will they find the road map and instruction to successfully carry out the mission?

Controlling

Controlling is the last of the four core elements of financial management. The hospitality enterprise is not going to be financially successful without having proper financial controls in place.

Controlling
Monitoring and measuring performance; intervening and taking corrective action when performance deviates from the strategic plan, goals, and objectives

It is not uncommon to have an individual employed by a hospitality business whose job title is "controller" or "comptroller." Both job titles speak to the importance of being in control of all things financial. As such, individuals working in this capacity are the financial managers, and they are responsible for administrating and controlling the business's finances. Part of their responsibility is to ensure they have a solid understanding of where the money is coming from and where the money is going for the hospitality operation.

In the art of controlling, a system needs to be designed and built. A main component of the control system is projecting the illusion that the firm is in complete and total control of all valuable resources. The harsh reality is that the management team will never have complete and total control. However, creating the illusion that control is always 100 percent bona fide and in all locations is achieved by ensuring staff are aware of the controls (manual and automated) that are in place and what systems and technology are in play at all times.

Control also requires an information system in which the location and dollar value of assets can be found in a timely manner. The control component of financial management must also facilitate the constant measurement of performance, comparing actual results to what was planned for in budgets and pro forma statements (a forecast of expected financial performance and position).

A good financial control system can measure and evaluate financial performance, goals, and objectives to a pre-established set of standards over an acceptable period of time. When significant variances occur between actual financial performance and what had been planned for, then an investigation and analysis should be undertaken quickly, before the problem or potential problem can cause further financial hardship for the hospitality enterprise.

Adjustments

Generally, a good financial manager will be involved with ongoing planning, organizing, directing, and controlling for the hospitality enterprise. At each level of operations, the management team must act professionally and in their capacity as consistently prudent financial stewards. This goal of sound operational financial management can be achieved by closely monitoring and managing operational elements such as monitoring cash flow, evaluating methods of financing, hitting target returns on investments, creating value, and seeking out lucrative assets that can enhance and improve the entity in terms of financial performance (net income) and position (balance sheet posture). This activity can be summarized as "adjustments."

From a holistic perspective, when one thinks of financial management in a hospitality context there are three basic questions that need to be asked by the management team all the time. These questions will challenge the financial managers' efforts to sustain financial viability and profit growth: (1) what assets should we acquire (what are we going to buy)? (2) How will the asset acquisition be financed (how are we going to pay for it)? (3) What should be done with the return on our investments (if we make money from these newly purchased items, what should we do with that money)?

Capital budget
The financial plan for the acquisition of long-term assets or the expenditure of significant capital on renovations and/or upgrades

Another significant component of strong financial management is capital budgeting. **Capital budgeting** relates to the first question asked above: what assets should we acquire? In this context, the financial manager is seeking out assets that will either improve existing operations or create additional value or wealth. Items in the capital budget basically include long-term assets. Long-term assets are anything of use, value, or benefit to the business that will not be consumed, expired, used, or exhausted within one operating cycle or one fiscal year, whichever is the longer of the two. Examples of capital items would include physical buildings (e.g., a hotel or stand-alone restaurant), vehicles, equipment, furniture, and fixtures. These capital items are also referred to as "big-ticket" items because of their high monetary value.

When capital budgeting decisions are undertaken, the financial management team will employ several financial models that help them evaluate projected costs, cash inflows, and expected return on investment. The financial management team will select capital items to include in the capital budget that will provide the best possible return and the least amount of risk to the hospitality enterprise. Capital budgeting models and techniques will be covered in Chapter 10, Budgeting.

The next component of successful financial management is thinking about the second question: where will the money come from to pay for the capital items in the capital budget?

To answer this question, one must recognize that in finance there are three main sources of financing that can be utilized alone or in combination: debt, equity, and internally generated funds. With respect to debt and equity, there are different possibilities or forms in which financing can be achieved. The different forms of debt and equity financing will be discussed in Chapters 3, 9, and 11.

Internally generated funds (IGF)
Funds generated as a result of profitable operations

However, with respect to **internally generated funds** (**IGF**), there are two conditions that must be satisfied. First, the operation must be up and running. If the hospitality operation does not yet exist (or is not open for business) there are no IGF. Second, IGF can be generated only if the hospitality operation is profitable. If the operation is up and running but is losing money (negative net income), then it is not possible for IGF to be generated.

Weighted average cost of capital (WACC)
The financial cost of every dollar that comprises the firm's capital structure

Astute financial management is one of the most important aspects of running a hospitality enterprise. The financial manager must understand the existing capital structure of the enterprise and the actions that need to be taken to lower the **weighted average cost of capital** (**WACC**) as much as possible. Calculating the

WACC and effectively applying actions to reduce the WACC will be covered in Chapter 11, Capital Structure.

The current Canadian economic environment illustrates why the hospitality enterprise needs strong and pragmatic financial management. Whenever interest rates go up, more money will be going out the door to service the existing debt load. A good financial manager thinks about how best to transition that existing debt into more equity when examining the current capital structure. Or perhaps the enterprise could rely more on IGF and less on debt, in whatever form it may be.

This chapter has spoken to the justification for studying financial management. However, there is an important point that has not yet been identified. When you think about financial management, your mantra needs to be: the main goal or ultimate mission of the financial manager is to maximize the wealth of the owners. Regardless of the form of business ownership, whether it be a sole proprietorship, partnership, corporation, or cooperative, the overall mission to be undertaken by the financial manager remains the same—maximize the wealth of the owners (shareholders, partners, or sole proprietor). It is not to maximize revenue or gross operating profit or total asset dollar value. It is to maximize the owner's wealth. That is accomplished by creating value, and value is generated through sound financial management practices, analysis, competent decision-making, and prudent action.

Finance Is Not Accounting

There is some belief within the business community, as well as the general public, that finance and accounting are the same. They are not. Although accounting is important to finance, just as finance is important to accounting, they are different disciplines. For the most part they are both objective and quantitative, but they serve different purposes. Each provides solutions to a wide range of challenges in their own lane of specialization. Perhaps one could think of the two separate professions as being very close cousins, but they are not twins and not the same person.

Finance is also not economics, but it is closely associated with the discipline of economics. So, as with accounting and finance, students who are in a formal program of hospitality management will be required to take at least one economics course. Both micro- and macroeconomics are important to students of finance because these courses help explain how individuals, governments, households, and businesses behave and act rationally when given a set of constraints and within a particular operating environment.

Factors to be considered in financial management decisions come from, and are influenced by, the macroeconomic climate. These elements should not be ignored. The financial management team must pay close attention to what is happening with interest rates, unemployment, inflation, business and consumer confidence, foreign exchange rates, and the GDP growth rate.

Microeconomics is, as the name implies, a more focused look at entity behaviour in comparison to macroeconomics. It is a social science that is concerned with and aimed at consumer behaviour, willingness to pay, and the decision-making process of businesses and individuals. Microeconomics provides the financial manager with an understanding of how and why different goods will have different values, which is important for pricing and forecasting demand. The discipline also provides knowledge on how individual entities can benefit from efficient production and market transactions, and how individuals best coordinate and cooperate with one another. Generally speaking, microeconomics provides a more complete and detailed understanding than macroeconomics, and it is therefore important to the financial manager at the operational strategic business unit level.

For those who study hospitality management either at the undergraduate or graduate level, or for professional development purposes, courses in financial accounting and, often, management accounting are undertaken prior to an enrolment in a financial management course. This makes perfect sense because financial accounting serves as a strong foundation and comprehensive reference for financial management application and strategy. Furthermore, one should be able to understand an income statement, a balance sheet, and a statement of cash flows—where the numbers come from and what they mean—before attempting to make any significant financial decisions.

Accounting is a well-grounded, diverse discipline and profession. It is not an absolute but a science that continues to change and improve over time. Accounting treatments and procedures are constantly evolving, changing, and adapting to the needs of the business and government communities. The art and science of accounting is very diverse, with many branches of the profession that one could specialize in over time, although general practitioners are always in demand. Just how varied is the accounting profession? Here are a few examples of the wide variety of accounting types that exist today: financial, management, estate, wealth, tax, audit, cost, forensic, public, and government, to name a few.

Financial Accounting

Financial accounting is primarily concerned with providing useful, accurate, relevant, and timely information for external end users, such as owners, investors, government officials, financial institutions, suppliers, and vendors. The financial accounting team focuses on providing financial information that speaks to earnings and asset holdings. They also look for opportunities to augment, leverage, and improve the business's financial viability and stability. This is a continuous process that requires due diligence and professional judgment at all times.

Management Accounting

Management accounting is primarily concerned with providing useful and timely information to internal end users, such as corporate head office, general managers, unit managers, division directors, and department heads. This information assists managers in making sound operational decisions that will increase value, effectiveness, and efficiencies for the hospitality enterprise.

Tax Accounting

Tax accounting is, as the name implies predominantly focused on tax, including tax law, tax returns, tax payments, application of taxes, and tax treatment. Tax accountants can work independently or for private individuals, corporations, governments, or tax authorities. For the hospitality operation, tax accounting can be a very complex task; there will always be a need to maximize possible tax credits and minimize tax expense. Plus, there is the likelihood that an audit will be requested by the Canada Revenue Agency (CRA) from time to time. Audits conducted by the CRA involve a thorough examination of financial records, statements, and filings. This audit adventure can be somewhat stressful for the financial manager, because all documented financial transactions may be reviewed and questioned. It is not uncommon for the CRA to challenge the financial manager with respect to what has been claimed as an expense or tax credit in relationship to what qualifies as an expense or tax credit, and for how much. The CRA may also investigate the capital cost allowance values that have been employed to ensure that the amortization or depreciation charges that have been exercised have not been too generous and are within the prescribed legal boundaries.

Audit Accounting

Audit accounting speaks to the attest function—that is, to test the truthfulness, validity, and accuracy of the financial records and statements. Auditors accomplish this by employing statistical methods in the sampling and review of the accounting process, financial records, and financial statements that have been generated and presented to end users. Auditors can be either internal or external. Most large hospitality enterprises will have their own internal audit staff who travel from one property to another to conduct operational audits. This practice is undertaken by large hospitality firms (e.g., hotel and restaurant chains) on a quarterly basis.

The external audit involves a third-party accounting firm. All hospitality firms that are publicly traded (i.e., their stock is traded on an exchange) must have an external audit performed on a regular basis to comply with SEC regulations, Canadian securities regulations, other authorities and requirements, and/or the law. Usually, the external audit will take place twice each calendar year or about once every six months. The first time is to ensure that the financial accounting process is underway and that the record-keeping and financial-statement-generation processes are current, verifiable, and sound. The second time is to sample and test the financial statements to ensure that they are accurate, faithful, reliable, verifiable, and present a truthful representation of the financial performance and position of the hospitality enterprise. At the conclusion of the external audit, the auditors will provide an "unqualified opinion" if they have no concerns or issues with respect to the quality and validity of the financial records and statements. An unqualified opinion is a gold medal for the financial accounting team.

If there is some degree of concern, the auditors will issue a "qualified opinion." A qualified opinion can speak to either a scope limitation, a concern developed during the audit of the financials that was not widespread, or the absence or incompleteness of a footnote disclosure (an explanation or reason for why this transaction or event occurred).

A qualified opinion is not a gold medal. It is the auditors expressing an opinion that the financial records and statements have for the most part been presented with accuracy and truthfulness and are fairly presented, except for a specified area identified by the auditors. In general, a qualified opinion is still acceptable to concerned end users—such as financial institutions, suppliers, and investors—as long as the specified deficiency is addressed and rectified by the management team in a prompt and efficient manner.

Estate Accounting

Estate accountants handle the settlement of an estate when an individual has died. The assets, liabilities, and property of that person will be packaged conclusively in their estate. The estate is then managed by an appointee, who was designated by the deceased prior to their death to perform the task of executor. The executor must work with government (tax), financial institutions (bank accounts), investment houses (agents/brokers), insurance entities (life insurance claim), and family members to ensure the correct, legal, and prompt execution of the deceased person's will. The work of an estate accountant can be quite challenging if there are no formal records and documents to work with. It is important to recognize that tax liabilities and other debts do not go away after a person has died. That is why it is so vital to make sure that a will with all the required information (a balance sheet is very helpful) for the proper and smooth execution of the estate has been written and is in the safe custody of a law firm.

Wealth Accounting

Wealth accountants can work for corporations, financial institutions, governments, and private individuals. A wealth accountant records, monitors, advises, and reports on the asset value of the entity by which they are employed. They also seek out opportunities to enhance, augment, or improve their client's or employer's current position and provide recommendations accordingly. Finally, wealth accountants can also make recommendations as to when to sell off assets from their employer's portfolio as a defensive strategy, in case there is a significant change in the competitive, political, or economic environment. It is not uncommon for financial institutions to ask clients to have a net worth of at least US$2 million to qualify for having a wealth accountant assigned to their account or portfolio of investments.

Cost Accounting

Cost accountants are financial specialists who calculate and specify the true costs associated with the provision of a service or the manufacturing of goods, either in process or finished. They are responsible for gathering accurate information about the costs of inputs (materials and labour), transportation, storage, processing, packaging, sales, and marketing, as well as distribution. Cost accountants are concerned mainly about profitability and keeping the costs incurred within budget.

Forensic Accounting

Forensic accountants are highly specialized individuals—they are basically financial detectives. They conduct investigations and are responsible for identifying assets and tracking and tracing financial transactions. They will review and analyze the financial affairs of businesses and individuals when necessary. Once these actions and processes have been completed, they will prepare a formal report providing full disclosure of their discovery and findings, and they may testify in a court of law as required for cases involving financial crime.

Public Accounting

Public accountants provide their expertise as financial consultants to businesses and individuals. They provide a wide range of services, but mostly they generate and provide financial statements that will be released to the general public, hence the title "public accountant." They also will prepare tax returns and file complex tax documents as instructed by their clients.

Government Accounting

Government accountants work for the government, whether that be at the county, regional, municipal, provincial, territorial, or federal level. These individuals review all financial records and statements and ensure they are in full compliance with the required guidelines, policies, and regulations as stated by law for government agencies and institutions. Government accountants are specialists with respect to understanding government policy issues and concerns. As such, they help guide senior bureaucrats with respect to financial operating practices and procedures to increase the likelihood of specific financial objectives being met for that particular government ministry, department, or agency.

Hospitality Accounting

Those working in the hospitality industry should be aware of the Hospitality Financial and Technology Professionals association, commonly known as **HFTP**.

Hospitality Financial Technology Professionals (HFTP)
https://www.hftp.org/

HFTP is an international professional association with more than 5,000 members. It offers the Certified Hospitality Accountant Executive (CHAE) professional credential, which is well recognized throughout the global hospitality industry. For the aspiring accountant, it is one more professional credential that should be pursued. Hospitality accountants working in the accommodation sector will make use of the Uniform System of Accounts for the Lodging Industry (USALI) and the Uniform System of Accountants for Restaurants (USAR), and those working in the club (resort) sector will use the Uniform System of Accounts for Clubs (USAC). These accounting systems provide guidance, uniformity, comparability, and consistent reporting within their respective sectors of the hospitality industry. As a metaphor, the uniform systems provide an opportunity for financial managers to compare apples to apples, and not apples to bananas. As one can see, accounting as a profession is wide and deep in scope with a range of required professional skill sets.

Accounting Summary

As you can see, the accounting profession has many branches. It may be helpful to consider a working definition of the intriguing art and science of accounting: Accounting can be defined as the professional practice of recognizing that economic transactions have occurred. Accounting then captures those economic transactions by making official records as to what has taken place and identifying the specific dollar amounts involved. The accounting function is a necessary element of any hospitality business for a number of different purposes, including decision-making, revenue and expense forecasting, and the measurement and evaluation of financial performance and position.

Accountants make use of accrual, double-entry accounting methodology and are engaged in the accounting cycle. This is a formal process whereby the records of economic transactions are summarized, analyzed, and reported using financial statements. The most important financial statements include an income statement, a balance sheet, a statement of cash flows, and a statement of retained earnings.

An income statement provides the end user with information about the enterprise's financial performance for a given period of time. How well is the hospitality enterprise doing in terms of revenue generation and profit? The easiest way to think of an income statement is to think of a scoreboard at a sports event. One look at the scoreboard and you know whether your team is winning or losing and by how much.

The balance sheet provides the end user with a snapshot of the firm's financial position at a given point in time. The balance sheet identifies the firm's assets and liabilities, and the owners' equity. It gives valuable information about the firm's debt-to-equity, leverage, liquidity, and solvency situations.

A statement of cash flows is also known as a statement of changes in financial position. This important financial document gives the end user vital information about where cash has come from (cash inflows) and where cash has gone (cash outflows). This statement is reporting only on cash movements and does not take accrued or deferred transactions into consideration. It identifies only cash increases and decreases from operations, investment, and finance activities. The statement of cash flows is a very important financial document to the hospitality enterprise because, typically, most operations in the industry have cash-on-hand challenges.

The Importance of Financial Management Today

As discussed earlier in this chapter, Canada and its hospitality industry are faced with a host of financial challenges. These challenges include operational recovery from the global pandemic, high inflationary pressure, a shortage of skilled labour, low GDP growth, low consumer confidence, high interest rates, and geopolitical turmoil. This section examines each of these challenges.

Operational Recovery

The priority for most operations in the hospitality industry is to recoup revenue that was lost during the global pandemic. The steps that need to be taken in order to achieve this goal include providing goods and services that offer value and satisfaction to the customer. First, hospitality operations need to provide an incentive to get customers to come back and to spend money. This can be done by ensuring that the product–service mix projects attractive value. This is accomplished by leveraging strategic pricing so that the price points on those goods and services are in strong alignment with the willingness of the client to pay. Second, the financial manager needs to make sure that there is sufficient operating cash on hand to support the level of service and quality of product that is being provided to the prospective guest and, perhaps most importantly of all, to ensure that payroll obligations will not be jeopardized.

Inflation

At the time of writing, Canada's inflation rate was 7.7 percent, the highest it has been since January 1983, when it was at 8.2 percent. This high inflation rate means you need more dollars today than you did last year to purchase the same basket of goods. It also represents future demands by employees for higher wages so that they can keep up with the rising cost of living. This is a negative situation because it will lead to cost-push inflation, also known as wage-push inflation, where prices on all goods and services will eventually increase. This is because the increased cost of labour causes an increase in the cost of raw materials and finished goods. This greater cost of production will decrease the existing supply conditions, because with higher costs to produce the same amount of goods, manufacturers are not motivated to maintain or increase existing supply levels. Additionally, because the demand for these goods remains the same, the increase in production costs unfortunately gets passed on to consumers, creating cost-push inflation.

Accordingly, prudent financial management is required to ensure investment in assets that will help reduce operating costs and perhaps foster an environment where there is less dependency on human labour. McDonald's is a perfect example of this, as they continue to spend millions of dollars each year on research and development for the possible introduction of automation and robotics into their global operations. Even today, McDonald's has introduced automated beverage dispensers for the drive-through windows and automated french fry stations. They also have self-serve kiosks, reducing the need for counter cashiers. Plus, they are in final testing stages of a voice recognition order system for the drive-through for about ten stores located close to the company's headquarters in the Chicago area.

Skilled Labour Shortage

In Canada, as well as in the United Kingdom and the United States, the hospitality industry is finding it challenging to recruit and secure skilled labour. There are a number of factors contributing to this problem. Let's look at two significant ones. First, Canada has an aging population: around 23 percent of Canadians are now over the age of 45, and only about 15 percent are 18–44 years of age. This is not a good demographic fit to support the needs of the hospitality industry.

Second, those in the 18–44 age band are generally not interested in pursuing a career in the hospitality industry. This is due to the perception that the industry has poor working conditions, long hours, hours that do not fit with their social activities, and low wages. Furthermore, their perspective of hospitality is often perceived as culinary only, ignoring all the other wonderful career opportunities that exist in this dynamic industry. To make matters worse, there is a lingering perception that working in a hospitality operation may increase the likelihood of getting Covid-19 (Tourism Canada HR, 2021).

Weak GDP

A weak GDP as well as a weak GDP growth indicates an economy that is not running at full capacity. If the economy is not running at or near full capacity, it means that there will be less demand for luxury and discretionary goods and services. Unfortunately, spending money on food away from the home or taking an overnight trip that requires staying at an accommodation property requires individuals, businesses, and households to have discretionary income available for expenditure on these goods and services.

Low Consumer Confidence

Consumer confidence in Canada is at about 50 percent (Trading Economics, 2023). This is not a positive number, since it means that only one in two Canadians feels good about the current economic environment and outlook. When consumer confidence is low, consumers will typically hold off on purchasing any big-ticket items, such as houses, cars, appliances, furniture, and long-stay vacations. Also, consumers will save more and spend less. They will be very selective about what they spend their dollars on, and most likely they will not be spent on discretionary leisure time products or services. Once again, this is not helpful for the hospitality industry, which is trying to recover from the devasting impacts of the global pandemic.

High Interest Rates

Canada is experiencing high inflation, and with the high inflation comes increasing interest rates. The Bank of Canada increased the overnight lending rate multiple times in an effort to contain and reduce inflationary pressure.

Higher interest rates deter businesses and households from borrowing money. This is because higher interest rates represent a greater cost incurred with any form of debt financing taken on by a business or household. Even with suppliers and vendors, increased short-term lending rates will put more financial pressure on hospitality operations. Higher interest rates translate into greater cost, which can decrease operating profit for the hospitality enterprise.

Geopolitical Turmoil

The world today is not the same world as five or ten years ago. The conflict in Ukraine, a potential conflict in the Asia Pacific basin, wealth and class disparity in India, and gang wars mixed together with drug-related crimes in Mexico are just a few examples of current political conflicts around the world that cause uncertainty and harm for international tourism.

As one can surmise from all of these issues, the hospitality industry faces many challenges both in Canada and around the globe. The need for astute, pragmatic financial management to help mitigate financial injury to the enterprise caused by these issues should be clear to hospitality professionals everywhere.

Create Your Own Financial Management Information System

Whether you are a student or an industry practitioner, it is a wise investment to set up and establish your own financial management information system (FMIS) so that you are not blindsided by an unexpected event or circumstance. Getting your own FMIS up and running is relatively easy and puts you on the path to financial awareness. It will ensure that you are in the know and understand what is happening in the financial community, both domestic and international, on any given day. To accomplish this task, there are some great free websites that provide helpful, current, and relevant information that should be monitored on a daily basis—for example, The Financial Post, Money Magazine Canada, CNN Money, Trading Economics, MarketWatch, Forbes, Reuters, and Yahoo Finance. Helpful information pertaining more specifically to the Canadian hospitality industry can also be found on the websites for Restaurants Canada, the Hotel Association of Canada, and the federal government's Travel Canada.

You should get yourself into a good morning habit of making your beverage of choice and then sitting down in front of the computer for about 30 minutes to sift through the news and data with respect to all things financial. This will give you the information you need for the day and help guide you with respect to choices or decisions that need to be made.

How to Create Your Own FMIS

1. Have a morning beverage of your choice.
2. Get your computer up and running.
3. Go to Yahoo Finance (https://ca.finance.yahoo.com/)
4. Read the headlines and take the time to read the articles that have caught your attention.
5. Take a good look at the markets ribbon that is positioned at the top of the web page.
6. Make some notes about anything you think is interesting and/or important.
7. Make sure you identify the date and time you were viewing the information.
8. Repeat this process with at least another two websites, such as CNN Business (https://www.cnn.com/business) and The Financial Post (https://financialpost.com/).

A good financial manager is one who is financially aware. That is to say, that person is going to engage in the following four-step process on a consistent basis before any significant financial management decisions are made:

1. News
2. Data
3. Analysis
4. Speculation

The first step, news, is to glean the financial stories from your newly established FMIS. Make notes and highlight key points that are relevant to the hospitality operation's concerns and needs. The second step is to obtain as much relevant current data as possible from websites and service providers, such as Smith Travel Research (STR), Statistics Canada, Hotel Association of Canada, Restaurants Canada, Tourism Canada, Yahoo Finance Canada, Trading Economics, etc. The third step, now that data has been secured, is to pair it with the highlighted notes you obtained from the news stories and perform some financial modelling and analysis. The financial modelling and analysis methods will be identified and explained in Chapters 7 through 14. Finally, in step 4, speculation, you look at the outcomes or products that have been determined from the third step, analysis, and exercise your own professional judgment as to the best course of action given the analysis that has just been completed and the new information that has been generated as a result of this process.

Chapter Summary

Successful financial managers make the time to read the financial news and communicate with their professional colleagues. They are engaged in professional association activities so that they are up to date and understand what opportunities and threats exist today, as well as what may come in the days ahead. As previously mentioned, all things in life, whether at work or home, either directly or indirectly involve financial management. To this end, sound financial management skill sets and competencies are needed to help ensure success for the hospitality enterprise in today's challenging operating environment.

CHAPTER REVIEW QUESTIONS

1. What is the four-step process that financial managers need to take before making any significant financial decisions? Explain each step in the process.
2. What has been learned from the great financial crises to help prevent financial managers today from making the same mistakes?
3. Why is it so important to study and hone financial management skill sets and competencies to have success in the hospitality industry?
4. What is CATS and what purpose does it serve? Explain and elaborate.
5. Why are key economic indicators such as inflation, interest rates, and GDP so important to the financial manager? Explain and elaborate.
6. The Canadian hospitality industry is currently facing several different challenges that make for a very difficult operating environment. What do you see as the most significant challenge the industry faces today? Explain why.
7. How is financial management different from accounting? Explain and elaborate.

APPLY YOUR KNOWLEDGE

1. You are having coffee with your friend José. José wants to know what financial management is, and more specifically what are three questions a financial manager should be asking, or at least thinking about, daily. How would you respond?
2. Your classmate is still not sure that there are differences between financial accounting and management accounting. What would you say is the one major difference between the two?
3. You walk into the office of the finance director for a downtown hotel. You are in awe of a beautiful poster that is hanging on the office wall. The poster states, “The most important goal of the financial manager is …”

KEY TERMS

Capital budget, 17
Controlling, 16
Directing, 16
Gross domestic product (GDP), 4
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Organizing, 15
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Stagflation, 14
Weighted average cost of capital (WACC), 19

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