An important challenge faced by hotels is how to set their premium room price differential over their standard rooms and how to manage the upsell process. Offering standby upgrades, where the customer is only charged if the upgrade is available at the time of arrival, is one technique that has become increasingly popular in practice for monetizing the premium room inventory that may otherwise go unused. We develop a model of premium room and standby upgrade pricing under uncertain market size and examine how and when the standby upgrades can provide additional revenue for a hotel. When the guests are myopic, we show that the standby upgrades can be used as a powerful price discrimination tool, especially for hotel properties with low standard-to-premium room ratios and/or low target occupancy rates. On the other hand, when the guests are strategic, the benefit of the standby upgrades is significantly diminished. In contrast to the myopic case, we show that standby upgrades provide little additional revenue when the hotel property has a low standard-to-premium room ratio and/or low target occupancy rate. Finally, we investigate the revenue penalty incurred when a hotel incorrectly identifies either the type of guest behavior or the proportion of guests who will be exposed to standby upgrades. Our findings thus provide guidance on the hotel types and environments that are most suitable for standby upgrades.

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