Evaluating Economic Viability of the Lodging Industry. Independent vs Chain Hotels

Dr. Soultana Tania Kapiki

Department of Tourism Management

Alexander Technological Educational Institute of Thessaloniki

P.O. Box 141, GR-57400 Sindos Thessaloniki, Greece

E-mail: tkapiki@tour.teithe.gr

ABSTRACT

Purpose: the purpose of this paper is to evaluate the economic results of the independent hotels in comparison with the chain hotels as well as report good practices for the viability of the lodging industry.
Methodology: an empirical survey took place in Greece and it concerns the period 2008-2011. The study was conducted via on-line questionnaires and the sample consists of 165 hotel units. Thirty five of them are independent hotels and the rest (130 units) belong to 35 hotel chains. The hotel classification varies from 2 to 5 stars and most properties are resort and city hotels.
Findings: the main findings of the survey show that for the period 2008-2011 the independent hotels are more profitable compared to the chain hotels. The sector's best practices include conducting a market and financial feasibility study before developing any property; purchase of assets in different cities and regions so that a drop in one market will not affect the others; developing mixed-use enterprises; balancing the needs and expectations of the hotel chains' various stakeholders; environmental certification and commitment; continuous investments and sufficient working capital to support the penetration in new markets; carefully planned and effectively implemented strategies contributing in the success, profitability and viability of the enterprise.
Research limitations: this research was limited to the Greek hotel sector. Another limitation was the reluctance of some hotel managers to share the financial data of their property. Despite this fact, the sample is enough for reliable findings and conclusions, since the sample's size (bed capacity equal to 76.777 that accounts for the 10,85% of Greece's total 2*-5*capacity) is considered representative.
Originality/value: a financial analysis, the application of both benchmarking and empirical analysis for the hotel economic assessment, as well as the identification of good practices for the hospitality properties' viability are among the main contributions of this study.
Based on the findings of the survey, investors and hotel operators may have a clearer picture of whether it is preferable to invest their funds in the development of an independent hotel or they should turn to chain ownership.

KEY WORDS: economic viability, lodging industry, independent hotels, chain hotels, good practices.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

INTRODUCTION

Economic viability (sustainability) in hospitality involves using the assets of the property optimally and efficiently so as to allow it to continue functioning profitably over the longer term.

The viability of individual tourism enterprises depends on the ability to identify markets that will continue to deliver business in the long term; to understand what potential consumers are looking for; and to adapt to trends and changes in source market conditions, travel patterns and tastes. This requires effective and on-going market assessment to guide development in the hospitality properties (UNEP, 2005).

Few studies concerning the economic viability of the independent and chain hotels exist in the contemporary literature and thus, we decided to conduct a survey in hotels located in Greece so as to identify answers to the research problem.

The purpose of this study is to evaluate the economic results of the Greek independent hotels in comparison with the chain hotels as well as report good practices for the financial viability of the lodging industry.

In order to achieve the study purpose, the following procedures take place. First, we present the Greek hotel supply as well as the total market size in value (turnover) of the Greek hotel enterprises for the years 2008 – 2011 (Tables 1 and 2).

Then we quote the branded hotels operating in Greece in 2009 (Table 3), and, separately for the independent and chain hotels the sample's key data, such as the number of hotels, their classification, the total bed capacity and number of employees, the location and the total market share in terms of the overall amount of beds (Table 4).

Second, benchmarking as well as empirical analysis is performed and the mean for several key indicators of the sampled hotels for the period 2008-2011 is shown in the Table 5.

Third, selected good practices that have been identified through this study are presented as suggestions for the viability of the lodging industry both in Greece and worlwide.

Literature Review

Hotel properties can be grouped by ownership and affiliation into two basic equity structures: independent hotels and chain hotels. An independent hotel has no affiliation with other

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

properties. Chain hotel ownership may take a number of forms, including management contracts, franchises and referral groups (Kasavana, Brooks, 2005).

When new hotels are developed and planned feasibility studies are conducted usually by independent consultants. A feasibility study can help investors decide whether the hotel project they are considering is economically viable. Among other elements the study includes competition analysis and financial estimates (Angelo, Vladimir, 2007).

Furthermore, prospective owners can use academic surveys, such as the one included in this paper in order to determine their ownership and affiliation.

The decision to be a franchise or chain affiliated hotel is one of the most critical decisions in a hotel investment. For many hotels the costs associated with purchasing and maintaining a franchise (6-8% or more of revenue) represents the 2nd largest (after labour) expense category. While for many hotels affiliation can represent the difference between financial viability or failure, affiliation does not ensure successful financial performance. And in fact, certain types of hotels, depending upon their market positioning and segmentation, perform much better as independents (Raleigh, 1999).

The economic viability is part of the sustainable development strategy of many hotels. The objective is to create superior value to their shareholders and guests and the strategy is based on the concept of the "triple bottom line," which combines economic viability (profit) with social responsibility and environmental protection. A company must use sustainable development principles to grow revenues and save on costs thus remaining profitable to be sustainable (Houdre, 2008).

Hotels' reason to go sustainable is not limited to the pursuit of an environmental friendly approach. These environmentally friendly actions in hotels are usually related to economic benefits, competitiveness, brand image and meeting customers' expectations (Rahman, et al., 2012).

Whatever the origin is, the hospitality industry pays more attention to be sustainable because of the multiple benefits discovered. But the main motivation to be sustainable seems to be minimizing cost for economic benefits (Ozdogan, et al., 2013).

The pattern of concentration in the European hotel industry reflects the structure of the economies. Experience and market service economies (e.g. the UK and France) have the highest hotel concentration (chain room percentage of the country's total room capacity), while industrial economies such as Greece and Portugal have the lowest structural scores in the EU (Slattery, 2004).

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

The hospitality sector is the pillar of the Greek tourism industry but nonetheless, the large (over 1.000 beds) hotel groups and the international hotel chains operating in Greece in 2011 control only 228 hotels and 116.400 beds (ICAP 2012).

Aimed at understanding the structure of the Greek hotel industry we quote below some key figures and indicators for the Greek hospitality sector (Tables 1-3).

The Greek hotel supply in the years 2008 - 2011 was as follows (Table 1):

Table 1: Hotel supply in Greece (2008-2011)

Hotel Capacity / Indicator	2008	2009	2010	2011
Hotels	9.385	9.559	9.732	9.648
Rooms	375.100	383.000	397.700	397.322
Beds	715.857	732.279	763.407	763.668
Distribution of beds per class	5* 78.464 4* 183.900 3* 169.941 2* 227.146 1* 56.406	5* 91.770 4* 187.494 3* 171.202 2* 226.707 1* 55.106	5* 102.428 4* 196.862 3* 177.923 2* 230.358 1* 55.835	5* 108.552 4* 193.381 3* 180.365 2* 226.539 1* 54.831
International arrivals per bed	22,3	20,4	19,7	21,47
Average hotel size in rooms	41	40	41	41,18
Average occupancy	56,7%	51,1%	48,1%	N/A
Revenue per available room (RevPAR)	N/A	15.328 €	13.274 €	14.491,2 €

Sources: SETE, Greek Chamber of Hotels, ICAP & ITEP (2008 - 2012)

The market size (in value) of the upper class hotel enterprises is equal to the total sum of turnovers (sales) of all the Greek 5, 4 and 3-star hotels. The total market value of the Greek hospitality industry for the years 2008-2011 is presented in the Table 2.

The market size (in value) of the 5*-3* Greek hotels has increased by 8,8% in 2011 in relation to 2010. The revenues of the 4-star hotels represent the largest share (about 46%) of the Greek hospitality sector total value.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

Table 2. Total market size in value (turnover) of the Greek hotel enterprises 2008-2011

Year	Market size (in € 000) (5*- 3* hotels)	Change (%)
2008	3.430.000	5,2
2009	2.980.000	-13,1
2010	2.850.000	-4,4
2011	3.100.000	8,8

Source: ICAP, Hotel Enterprises (2008-2012)

According to the latest Greek Hotel Branding Report, branded hotels in Greece account only for 4% of the total number and 19% of total availability of rooms, while in other European countries this figure lies between 25 and 40% (http://www.msolutions.gr/projects/tourism/). The Table 3 below shows the branded hotels operating in Greece in 2009.

Table 3. Branded hotels operating in Greece (2009)

	No. of hotels	Share of the country's hotels	Total room capacity	Share of the country's total room capacity	Average no. of rooms per hotel
International Hotel Brands	104	1,1%	21.667	5,4%	208
National Hotel Brands	155	1,6%	31.639	7,9%	204
Local Hotel Brands	167	1,7%	23.267	5,8%	139
Cypriot Hotel Brands	26	0,3%	6.723	1,7%	259
All Branded Hotels of Greece	*431*	*4%*	*77.464*	*19%*	*180*

Source: Koutoulas Hotel Database

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

METHODS AND DATA

In order to gather the required information as well as analyse the hotel companies financially and identify the industry's best practices towards viability, we applied a methodological approach that includes the following steps:

- We grouped the lodging enterprises operating in Greece into two major segments: individual properties and chain hotels.
- We then developed and sent an on-line questionnaire to 200 independent hotels and to the headquarters of 250 hotel chains (the latter publish consolidated balance sheets), aiming to collect key financial data for the period 2008-2011 as well as identify those practices having contributed to their viability. The hotel categories vary from 2-5 stars (although the responses from 2-star hotels are quite few) and the vast majority are city and resort hotels.

The questions included in the questionnaire can be classified into three basic groups:

(a) Those concerning the hotel key data, such as: number of hotels (included in the chain); classification, bed capacity; number of employees; location;
(b) Questions asking for the property's economic performance in the last four years; and,
(c) Questions identifying good practices for the viability of the hospitality sector.

The technique used for selecting the 450 recipients of the questionnaire was the cluster sampling (independent/chain hotels) and then a simple random sample of these two groups was selected.
The questionnaire was sent in January 2013 and by May 2013 we received 35 completed questionnaires from individual hotels and 42 from chain hotels. From the 42 answered questionnaires, seven were not complete and were excluded from the sample, therefore the final number of the hotel chains is 35. The response rate to the questionnaire was 17% and the sample's size (bed capacity equal to 76.777 that accounts for the 10,85% of Greece's total 2*-5*capacity) is considered representative.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

Whenever necessary, the data collected through the questionnaires were compared against published balance sheets and performance data and in case of variations the hotel managers were contacted again for further clarifications and additional information.

For the economic assessment of the sampled hotel properties we used the variables *efficiency* and *profitability*. More specifically, for the purposes of this study the efficiency of hotel enterprises is assessed by using the indexes Return on Equity and Return on Capital Employed. For the assessment of profitability the indexes of Gross Profit, Operating Profit, Net Profit and EBITDA margin are used (ICAP, 2012)[i]. Therefore, the hoteliers were invited to provide the above data for the period 2008-2011.

EBITDA (earnings before interest, taxes, depreciation and amortization) can be used to analyse the profitability between companies and industries because it eliminates the effects of financing and accounting decisions (Ransley, 2004).

- Following the collection of the answered questionnaires, elaboration of the answers and calculation of various financial indicators took place.

The sample's key data are presented in the Table 4.

Table 4: Sample key data

<table>
<tr><th colspan="3">Independent Hotels (35 hotels)</th><th colspan="3">Chain Hotels (35 chains: 130 hotels)</th></tr>
<tr><td>Number of Hotels</td><td>Classification</td><td>Total Bed Capacity</td><td>Number of Hotels</td><td>Classification</td><td>Total Bed Capacity</td></tr>
<tr><td>19</td><td>5*</td><td rowspan="2">19.623</td><td>40</td><td>5*</td><td rowspan="4">57.154</td></tr>
<tr><td>16</td><td>4*</td><td>61</td><td>4*</td></tr>
<tr><td colspan="3" rowspan="3">Total Number of Employees: 4.837</td><td>25</td><td>3*</td></tr>
<tr><td>4</td><td>2*</td></tr>
<tr><td colspan="3">Total Number of Employees: 13.052</td></tr>
<tr><td colspan="3">Location:
City hotels (7)
Resort hotels (28)</td><td colspan="3">Location:
City hotels (21)
Resort hotels (108)
Airport hotel (1)</td></tr>
<tr><td colspan="3">Total market share in terms of the overall amount of beds (Hotel Categories 5*& 4*): 6,55%</td><td colspan="3">Total market share in terms of the overall amount of beds (Hotel Categories 5*, 4*, 3* & 2*): 8%</td></tr>
</table>

Source: author's own elaboration

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

For the economic assessment of the sampled hotels we benchmark and set out in the Table 5 below the indicators: Efficiency (Return on Equity & Return on Capital Employed) and Profitability (Gross Profit Margin, Operating Profit Margin, Net Profit Margin & EBITDA Margin). The results of the analysis are presented in two separate columns per year, one for independent hotels and one for chain hotels. In this way, the comparison for each index and year is more distinct.

Table 5. Benchmarking of sampled Hotels' Key Indicators (Mean 2008-2011)

Index	2008		2009		2010		2011	
(%)	INDEP.	CHAIN	INDEP.	CHAIN	INDEP.	CHAIN	INDEP.	CHAIN
Return on Equity	-2,50	-3,41	-5,81	-29,47	-11,02	-12,47	-12,68	-2,09
Return on Capital Employed	-1,48	0,45	-0,205	-1,62	-2,618	-1,80	-0,835	-0,74
Gross Profit Margin	17,37	15,84	15,66	14,93	14,19	9,52	18,77	15,27
Operating Profit Margin	-1,48	-7,83	-6,20	-11,19	-9,94	-12,59	-2,77	-7,91
Net Profit Margin	-4,96	-5,48	-6,92	-11,76	-11,43	-12,49	-3,68	-9,23
EBITDA Margin	22,69	18,70	21,26	17,76	19,71	15,02	25,40	20,02

Source: author's own elaboration

The benchmarking analysis of the sampled hotels' key indicators (Table 5) shows that for the period 2008-2011 the Greek independent hotels are more profitable compared to the chain hotels.

CONCLUSION

The decision to be an independent or chain affiliated hotel is one of the most critical decisions in a hotel investment. The present study has proved that the independent hotels in Greece perform better than the chain hotels.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

All the Efficiency and Profitability Indexes of the independent hotels for the period 2008-2011 are much improved in relation to the respective indexes of the chain hotels. The EBITDA Margin in particular of the individual hotels is much higher in 2011 (25,40%), a year during which the Greek upper class hotels increased sales and market size (in value). Irrespective of a hotel's development process, both chains and unaffiliated (independent) hotels should focus on sustainable earnings and value. Towards this goal effective asset management is expected to be applied in the complete cycle of a property's development and operation.

The Greek as well as all the hotel enterprises in the world perpetually struggle for profitability and viability.

The identified through this study good practices that follow below can be applied by the hoteliers towards revenues enhancement and viability of their property:

1. Before developing any property, prospective owners should conduct a market and financial feasibility study. Among other information, the feasibility study will provide the project promoters with answers such as whether the investment is profitable and viable.
2. A number of local and global factors (e.g. international tourist arrivals, economic growth, the stock market, etc.) have broad profitability consequences for hotel operators who manage an international portfolio of hotels. One strategy that hotel investors might use for minimizing risk would be to purchase assets in different cities and regions, on the theory that these investments would not be correlated, and a drop in one market should be offset by a boom in another (Liu, Moulton & Quan, 2013).
3. Mixed-use developments incorporating retail, entertainment, bars and restaurants, residential and hotel accommodation are increasing in number and scale (Ransley, 2004). It has been found that the mixed-use enterprises operating in Greece had a much higher volume of turnover (sales) in the last 4 years (2008-2011) in comparison to the averages of the total Greek hotel industry (Kapiki, 2012).
4. Some very successful and well-known hotel chains report that in order to remain financially viable and operationally sustainable, their properties balance the needs and expectations of various stakeholders (owners, investors and shareholders, colleagues, guests, business partners, suppliers, local community representatives and all others they work closely with) while aiming to contribute to the sustainability challenges facing our

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

world (Shangri-La Asia Limited, 2010 Sustainability Report & Sarmaniotis et al., 2013).

5. Environmental certification (e.g. the Green Key, the EU Eco-label, the ISO 14001, etc.) contributes significantly in the enhancement of revenues and viability of the hospitality industry. Various surveys show that the majority of the profitable hotels are environmentally certified and apply successful sustainability initiatives. These hotels are committed to economic viability, and social and environmental responsibility (Kapiki, 2012).
6. Due to the economic crisis, the hotel companies can replace the loss of the internal market by attracting more foreign tourists. In order to achieve this, they have to develop or adjust their product to the demands of new guests. Therefore, continuous investments (e.g. in renovations and/or new facilities) are needed and also sufficient working capital to support the penetration in new markets.
7. At the operational level, carefully planned and effectively implemented strategies contribute in the success, profitability and viability of the enterprise. The strategies that have been identified as successful towards the sector's profitability (in order of significance) are: corporate expansion and continuous investments; guest-centred philosophy; teamwork, highly motivated, productive and competitive staff; exceptional and personalised services; contemporary technological systems; effective marketing techniques; and, several strategic alliances.

Limitations and Future Research

A limitation to this study was the fact that it concerns only the Greek hotel sector. Another limitation was the reluctance of some hotel managers to share the financial data of their property. In spite of this, the sample is enough for reliable findings and conclusions, since the sample's size (bed capacity equal to 76.777 that accounts for the 10,85% of Greece's total 2*-5*capacity) is considered representative.

Future research is suggested to include both international and local companies, for more objective conclusions. It should also include and analyze more variables, such as the hotel effectiveness and more specifically the indexes Average annual occupancy, Turnover, Revenue per available bed (RevPar) and GOPPAR (gross operating profit per available room) for a long period (e.g. a decade) and benchmark them with the industry averages. The analysis and comparison should be made by the hotel class and location and among several countries.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

This is likely to provide a more precise perspective on why and to what extent companies should invest in affiliated or non affiliated hotels.

References

Angelo, M. R., Vladimir N. A. (2007). *Hospitality Today - An Introduction*, 6th Edition, Educational Institute, American Hotel & Lodging Association, USA

Association of Greek Tourism Enterprises (SETE). *Greek Tourism: Facts & Figures* (2010-2012) & *Hotel Capacity per class and Prefecture* (2010)

Hellenic Chamber of Hotels. *Hotel Capacity 2009 - 2012*

Houdre, H. (2008). Sustainable Hospitality: Sustainable Development in the Hotel Industry, *Cornell Industry Perspectives*, No. 2

ICAP, Sector Studies, *Hotels*: Publications 2007-2009, 2011, 2012

Investing in Tourism in Greece (http://www.msolutions.gr/projects/tourism/)

ITEP & Hellenic Chamber of Hotels (2013). *Performance of Greek Tourism and developments in the basic figures of the Greek Hotel Market 2011 – 2012*

ITEP (Research Institute for Tourism). *Developments in the key figures of the Greek hotel market in the years 2010 – 2011*

Kapiki, S. (2012). Implementing Sustainable Practices in Greek Eco-friendly Hotels, *Journal of Environmental Protection and Ecology*, Vol. 13, No. 2A, pp. 1117–1123

Kapiki, S. (2012). Profit Optimization Strategies in Integrated Resorts - Case Study of the Sani Resort, Chalkidiki. International Conference *'Competition and Innovation in Tourism: New Challenges in an Uncertain Environment*', pp. 193-205

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297

Kasavana, L. M., Brooks, M. R. (2005). *Managing Front Office Operations*. Educational Institute of the American Hotel & Lodging Association, USA

Koutoulas, D. (2009). *The 2009 Greek Hotel Branding Report*, (http://www.sete.gr/files/Media/GreekHotelBrandingReport2009.pdf)

Liu, C. H., Moulton, P. C., Quan D. C. (2013). Common Global and Local Drivers of RevPAR in Asian Cities, *Cornell Hospitality Report*, Vol. 13, No. 12

Ozdogan, O. N., Hancer, M., Oter, Z. (2013). A Debate on Food Cost & Sustainability: the Role of Executive Chefs in All Inclusive Hotels. The 11th Asia Pacific CHRIE conference "*Facing the Challenges, Grasping the Opportunities-Winning in the hospitality industry in uncertain times*", Macau SAR, China

Rahman, I., Reynolds, D., Svaren, S. (2012). How "green" are North American hotels? An exploration of low-cost adoption practices, *International Journal of Hospitality Management*, 31, 720– 727

Raleigh, L. E. (1999). *Evaluating Hotel Franchise & Chain Affiliation Programs*, International Society of Hospitality Consultants, 05/1999 (http://www.ishc.com/)

Ransley, J. (2004). *Developing Hospitality Properties & Facilities*, 2nd Edition, J. Ransley & H. Ingram (Eds), Chapter 14: Product development and brand management, ELSEVIER BUTTERWORTH HEINEMANN

Sarmaniotis, C., Assimakopoulos, C., Papaioannou, E. (2013). Successful implementation of CRM in luxury hotels: Determinants and measurements, *EuroMed Journal of Business*, Vol. 8(2)

Shangri-La Asia Limited (2010). Sustainability Report (http://www.hotelschool.cornell.edu/research/chr/events/roundtables/sustainability/documents/Shangri-LaAsia2010SustainabilityReport.pdf)

Slattery, P. (2004). *Developing Hospitality Properties & Facilities*, 2nd Edition, J. Ransley & H. Ingram (Eds), Chapter 4: Development strategy, ELSEVIER BUTTERWORTH HEINEMANN

UNEP-United Nations Environment Program (2005). *Making Tourism More Sustainable*: *a Guide for Policy Makers* (*http://www.unep.fr/shared/publications/pdf/DTIx0592xPA-TourismPolicyEN.pdf*)

Endnote

---

[i] The indexes used for the assessment of the sample's efficiency and profitability are calculated as follows:

Efficiency indexes

Return on Equity = $\frac{\text{PROFIT BEFORE TAX}}{\text{EQUITY}} X100$

Return on Capital Employed = $\frac{\text{PROFIT BEFORE TAX}}{\text{LIABILITIES}} X100$

Profitability indexes

Gross Profit = $\frac{\text{GROSS PROFIT}}{\text{SALES}} X100$

Operating Profit = $\frac{\text{OPERATING MARGIN}}{\text{SALES}} X100$

Net Profit = $\frac{\text{PROFIT BEFORE TAX}}{\text{SALES}} X100$

EBITDA = $\frac{\text{EBITDA}}{\text{SALES}} X100$ (EBITDA is the total resulting as the sum of Operating margin + Financial costs + Accounted depreciation costs), ICAP, 2012.

Conference Proceedings ISBN 978-86-7031-310-1, pp. 287-297