11-3-2011

A Comparison of the Performance of Independent and Franchise Hotels: The First Two Years of Operation

Cathy A. Enz Ph.D.
Cornell University, cae4@cornell.edu

Linda Canina Ph.D.
Cornell University, lc29@cornell.edu

A Comparison of the Performance of Independent and Franchise Hotels: The First Two Years of Operation

Abstract
Although franchising has become a dominant mode of entry for hotel owners, a substantial number of entrepreneurs open their property as an independent and unaffiliated hotel. Given the finance community's desire for a brand flag as a condition of many loans, this analysis used STR Global data to compare the performance of newly opened franchise properties to that of independents. A comparison of the financial results for the first two operating years of 104 franchised and independent hotels in the United Kingdom found that the performance picture for franchise properties was overall not superior to that of independent properties. For full-service hotels (those in higher chain scales), the data revealed an early advantage in RevPAR for franchise properties, but that difference faded as time went on. For limited-service hotels, the independents experienced stronger RevPAR from six months after opening through two years after opening.

Keywords
independent hotels, franchise hotels, revenue per available room (RevPAR)

Disciplines
Business | Hospitality Administration and Management

Comments

The Center for Hospitality Research
Hospitality Leadership Through Learning

A Comparison of the Performance of Independent and Franchise Hotels:

The First Two Years of Operation

Cornell Hospitality Report
Vol. 11, No. 21, November 2011

by Cathy A. Enz, Ph.D., and Linda Canina, Ph.D.

Cornell University

The Robert A. and Jan M. Beck Center at Cornell University
Back cover photo by permission of *The Cornellian* and Jeff Wang.

Cornell Hospitality Reports,
Vol. 11, No. 21 (November 2011)

Cornell Hospitality Report is produced for the benefit of the hospitality industry by The Center for Hospitality Research at Cornell University

Rohit Verma, *Executive Director*
Jennifer Macera, *Associate Director*
Glenn Withiam, *Director of Publications*

Center for Hospitality Research
Cornell University
School of Hotel Administration
489 Statler Hall
Ithaca, NY 14853

Phone: 607-255-9780
Fax: 607-254-2922
www.chr.cornell.edu

The Center for Hospitality Research

Hospitality Leadership Through Learning

Thank you to our generous Corporate Members

Senior Partners

ASAE Foundation
Carlson Hotels
Hilton Worldwide
McDonald's USA
Philips Hospitality
SAS
STR
Taj Hotels Resorts and Palaces

Partners

Davis & Gilbert LLP
Deloitte & Touche USA LLP
Denihan Hospitality Group
eCornell & Executive Education
Expedia, Inc.
Forbes Travel Guide
Four Seasons Hotels and Resorts
Fox Rothschild LLP
French Quarter Holdings, Inc.
HVS
Hyatt
InterContinental Hotels Group
Jumeirah Group
LRP Publications
Maritz
Marriott International, Inc.
Marsh's Hospitality Practice
priceline.com
PricewaterhouseCoopers
Proskauer
Sabre Hospitality Solutions
Sathguru Management Consultants (P) Ltd.
Schneider Electric
Thayer Lodging Group
Thompson Hotels
Travelport
WATG
Wyndham Hotel Group

Friends

4Hoteliers.com • Berkshire Healthcare • Center for Advanced Retail Technology • Complete Seating • Cruise Industry News • DK Shifflet & Associates • ehotelier.com • EyeforTravel • Gerencia de Hoteles & Restaurantes • Global Hospitality Resources • Hospitality Financial and Technological Professionals • hospitalityInside.com • hospitalitynet.org • Hospitality Technology Magazine • HotelExecutive.com • International CHRIE • International Hotel Conference • International Society of Hospitality Consultants • iPerceptions • JDA Software Group, Inc. • J.D. Power and Associates • The Lodging Conference • Lodging Hospitality • Lodging Magazine • LRA Worldwide, Inc. • Milestone Internet Marketing • MindFolio • Mindshare Technologies • PhoCusWright Inc. • PKF Hospitality Research • Questex Hospitality Group • Resort and Recreation Magazine • The Resort Trades • RestaurantEdge.com • Shibata Publishing Co. • Synovate • The TravelCom Network • UniFocus • USA Today • WageWatch, Inc. • The Wall Street Journal • WIWIH.COM

A Comparison of the Performance of Franchise and Independent Hotels:

The First Two Years of Operation

by Cathy Enz and Linda Canina

EXECUTIVE SUMMARY

Although franchising has become a dominant mode of entry for hotel owners, a substantial number of entrepreneurs open their property as an independent and unaffiliated hotel. Given the finance community's desire for a brand flag as a condition of many loans, this analysis used STR Global data to compare the performance of newly opened franchise properties to that of independents. A comparison of the financial results for the first two operating years of 104 franchised and independent hotels in the United Kingdom found that the performance picture for franchise properties was overall not superior to that of independent properties. For full-service hotels (those in higher chain scales), the data revealed an early advantage in RevPAR for franchise properties, but that difference faded as time went on. For limited-service hotels, the independents experienced stronger RevPAR from six months after opening through two years after opening.

ABOUT THE AUTHORS

Cathy A. Enz, Ph.D., is a professor of strategy and the Louis G. Schaeneman Professor of Innovation and Dynamic Management at the Cornell University School of Hotel Administration (cae4@cornell.edu). Her research focuses on business strategy, including Innovation, competitive dynamics, pricing strategy, change management, and human resources investment strategies. Among her recent publications are two books, *The Cornell School of Hotel Administration Handbook of Applied Hospitality Strategy* (editor) and *Hospitality Strategic Management: Concepts and Cases*, 2nd edition, and the award winning journal article titled "Competitive Pricing in European Hotels," in *Advances in Hospitality and Leisure* (with L. Canina).

Linda Canina, Ph.D., is an associate professor of finance at the Cornell School of Hotel Administration. Her research interests include asset valuation, corporate finance, and strategic management. She has expertise in the areas of econometrics, valuation, and the hospitality industry. Canina's current research focuses on strategic decisions and performance, the relationship between purchased resources, human capital and their contributions to performance, and measuring the adverse selection component of the bid–ask spread. Among other publications, her work has appeared in *Academy of Management Journal*, *Journal of Finance, Review of Financial Studies, Financial Management Journal*, *Journal of Hospitality and Tourism Research*, and *Cornell Hospitality Quarterly*.

A Comparison of the Performance of Franchise and Independent Hotels

The First Two Years of Operation

by Cathy Enz And Linda Canina

When an entrepreneur seeks to open a new hotel, the arguments in favor of purchasing a hotel franchise seem self-evident. Firms that sell a business-format franchise provide franchisees with accumulated learning and experience, a proven brand, access to distribution, functional area expertise, and ready-made infrastructure. On the other hand, an owner who enters a new market without brand affiliation must either develop or already possess operating knowledge sufficient to open and operate a brand new property. Given the fact that a franchise conveys a proven operating and marketing system, it is no surprise that many lenders generally prefer projects that include a brand flag. Yet, independent operators continue to open and thrive. We sought to sort out these apparently conflicting observations by assessing newly opened hotels' actual performance. In the study presented in this article, we compared the performance of new hotels in the United Kingdom that have opened with franchises as against those that have started as independent properties over the first two years of operation. By focusing on the lodging sector our work extends the existing knowledge-resource research on services that has been conducted primarily in financial services, accounting, and law firms in which service professionals or knowledge workers dominate.[1] Recent work on knowledge assets in hotels has found that investments in brand affiliation were a strong predictor of firm performance, but that for complex hotel operations investments in service employees was also a strong predictor of firm performance.[2]

[1] For example, see: D. Andriessen, "Implementing the KPMG Value Explorer," *Journal of Intellectual Capital*, Vol. 6 (2005), pp. 474-488; S.M. Goldstein and P. Ward, "Performance Effects on Physicians' Involvement in Hospital Strategic Decisions," *Journal of Service Research*, Vol. 6 (2004), pp. 361-372; M.A. Hitt, L. Bierman, K. Shimizu, and R. Kochhar, "Direct and Moderating Effects of Human Capital on Strategy and Performance in Professional Service Firms: A Resource-Based Perspective," *Academy of Management Journal*, Vol. 4 (2001), pp. 13-26; and W. Wang, "An Evaluation of the Balanced Scorecard in Equity Valuation," *Journal of Intellectual Capital*, Vol. 6 (2005), pp. 206-221.

[2] K. Walsh, C. Enz, and L. Canina, "The Impact of Strategic Orientation on Intellectual Capital Investments in Customer Service Firms," *Journal of Service Research*, Vol. 10, No. 4 (2008), pp. 300-317.

Brand Experience and Market Entry

Knowledge, often embodied as organizational learning that has been formalized in rules and routines, is a key asset brought to the table by a franchisor.[3] Numerous studies have confirmed that pre-entry experience has an impact on a new industry entrant's performance.[4] That experience could include financial, managerial, marketing, and technological capabilities. Other researchers have found that firms entering new industries have a performance advantage that arises from their access to distribution channels and complementary assets.[5] Not surprisingly, experience is particularly important in influencing performance of new entrants in a new industry.[6] For example, in a recent study of venture capital firms, both breadth and depth of experience contributed to the likelihood that firms made first-round entries.[7] Also weighing in the franchisor's favor is research showing that prospective customers rely on a firm's brand as a signal of product quality.[8] All of those studies point to the potential contribution that a brand makes to a hotel's performance.

Innovative Independent Hotels

A counter argument to the advantage conferred by a franchise suggests that established franchises may encumber new entrants with pre-determined processes, systems, internal politics, and cultural factors that contribute to structural inertia.[9] In the absence of established operating procedures, innovation may flourish, particularly in environments where prior experience is less useful, because it is not applicable to the particular market situation.[10] In particular, independent entrepreneurs may gain competitive advantage because they are in a position to more flexibly form external relationships with various partners and suppliers.[11] Beyond the possibility of strategic alliances, an independent operator may use what's called "open innovation" in which they systematically obtain, retain, and exploit knowledge found both inside and outside the organization.[12] Since independent hotel operators have chosen not to "buy" a business model they are in a position to actively examine new technologies or participate in external knowledge communities. This may include collaborating with others via social networks.[13] Innovative independents may wish to keep their options open by making smaller investments in external knowledge rather than a long-term commitment to a franchise to ensure as much flexibility as possible.[14]

Full-Service vs. Limited-Service Hotels

In comparing the opening results of franchised and independent hotels, we anticipated finding differences

3 R.M. Cyert and J.G. March, *A Behavioral Theory of the Firm* (Englewood Cliffs, NJ: Prentice-Hall, 1963).

4 M. Ganco and R. Agarwal, "Performance Differentials Between Diversifying Entrants And Entrepreneurial Start-Ups: A Complexity Approach," *Academy of Management Review*, Vol. 34, No. 2 (2009), pp. 228–252.

5 W. Mitchell, "Dual Clocks: Entry Order Influences on Incumbent and Newcomer Market Share and Survival When Specialized Assets Retain Their Value," *Strategic Management Journal*, Vol. 12 (1991), pp. 85–100.

6 G. Carroll, L. Bigelow, M. Seidel, and L. Tsai, L., "The Fates of *De Novo* and *De Alio* Producers in the American Automobile Industry: 1885–1981," *Strategic Management Journal*, Vol. 17 (1996), pp. 117–137.

7 D. Dimov and P. Martin de Holan, "Firm Experience and Market Entry by Venture Capital Firms (1962–2004)," *Journal of Management Studies*, Vol. 47, No. 1 (January 2010), pp. 130-161.

8 T. Erdem, J. Swait, and A. Valenzuela, "Brands as Signals: A Cross-Country Validation Study," *Journal of Marketing*, Vol. 70 (January 2006), pp. 34–49; and A. Kirmani and A.R. Rao, "No Pain, No Gain: A Critical Review of the Literature on Signaling Unobservable Product Quality," *Journal of Marketing*, Vol. 64 (April 2000), pp. 66–79.

9 C.M. Christensen, *The Innovator's Dilemma: When New Technologies Cause Great Firms To Fail* (Boston: Harvard Business School Press, 1997).

10 Ganco, and Agarwal, *op. cit*.

11 R. Gulati, N. Nohria, and A. Zaheer, "Strategic Networks," *Strategic Management Journal*, Vol. 21 (2000), pp. 203-215; and I. Geyskens, J. Steenkamp, and N. Kumar, "Make, Buy, or Ally: A Transaction Cost Theory Meta-Analysis," *Academy of Management Journal*, Vol. 49, No. 3 (2006), pp. 519-543.

12 U. Lichtenthaler, "Open Innovation Past Research, Current Debates, and Future Directions," *Academy of Management Perspectives*, Vol. 25, No. 1 (2011), pp. 75-93.

13 E. von Hippel, *The Sources of Innovation* (New York: Oxford University Press, 1988).

14 V. van de Vrande, W. Vanhaverbeke, and G. Duysters, "External Technology Sourcing: The Effect of Uncertainty on Governance Mode Choice," *Journal of Business Venturing*, Vol. 24 (2009), pp. 62–80.

according to hotel segment, or, more specifically, the level of operating complexity. It goes without saying that full-service properties are more complex to operate, and thus these might show greater initial performance if they are affiliated with a franchise, especially since brand affiliation is expected to yield a performance advantage for full-service properties. In contrast, new limited-service hotels might lend themselves to successful operation by independent entrepreneurs. Having said that, we note that we are talking about the initial opening results, a situation which does not allow extensive time for an independent to ramp up operations. That fact also seems to confer an advantage on the franchise system.

The First Two Years of Operation

The hotel industry recognizes the early years of operation as a time when a hotel's fortunes are notoriously unstable. Some analysts consider that a typical hotel's income might stabilize between years two and five, but other observers argue that hotels never really stabilize, due to the vagaries of the market and the need for continuous investment to maintain the facility.[15] By examining a new venture's performance during the first two years of operation we can also compare the initial results of franchised properties and independent hotels. By the second year of operation, a new hotel should have refined its routines and one should be able to gain a sense of how it will perform as time goes on.[16]

We have offered arguments that support the potentially better results both of franchises and of independents. Indeed, our literature review offers only inconclusive evidence in support of one entry mode over the other.[17] We do note that research in hotels has found that the greater the investment in brand affiliation the higher the level of performance for existing businesses,[18] but again the benefits of brand versus independent status for new entrants has been left unexplored. Consequently, because we had no *a priori* reason to believe that one entry mode would lead to stronger performance than another would, we do not offer directional hypotheses. In this study, therefore, we examine entry mode and firm performance taking into consideration the level of complexity of the service business.

Methodology: Data Sources

Our sample consists of 104 hotels that entered all locations in the U.K. market between 2006 and 2010 (including urban, suburban, airport, interstate, resort, and small metropolitan markets). The data for these new hotels were obtained from STR Global, an independent research organization which tracks lodging performance for hotels worldwide and which constitutes one of the most comprehensive data sources available on the lodging industry. We obtained our data through strict and exclusive confidentiality arrangements.

The STR data consist of monthly hotel-level performance data—room revenue and rooms sold for each property and for each property's competitive set—and also categorical variables that describe characteristics of each firm. These data include **(1)** the number of rooms in the hotel; **(2)** the product and service quality segment category of the hotel; and **(3)** whether the property is chain-affiliated.

Hotel Performance: RevPAR, ADR, and Occupancy

We measured the hotels' performance using the common industry metric of revenue per available room (RevPAR). Monthly RevPAR for each hotel was one of the dependent variables, along with the two factors that constitute RevPAR, average daily rate (ADR) and hotel occupancy, both also calculated on a monthly basis.

Chain Affiliation

In our ordinary least squares (OLS) regression, to capture whether a hotel was franchised or independent, we used a dummy variable of 1 (brand affiliated) or 0 (independent) as the independent variable in the equation, based on information provided by the hotels as classified in the hotel census database of STR global.

Market Demand and Segments

Market demand and market segments are two critical control variables included in this study because demand conditions vary across hotel properties. So, the occupancy percentage of competitor hotels was included as a proxy for market demand. STR specifies a hotel's competitive set as the group of comparable hotels that are used by the hotel itself for performance comparisons. STR and the hotel select a minimum of four competing hotels to constitute each hotel's competitive set. The occupancy level of the competitive set for each hotel in the sample was used to control for market demand.

Complexity and chain scale. We had to address two issues relating to the hotels' chain scale, which is a relatively standard industry classification based on price, amenities, and service levels. To address the issue of complexity of operation, we divided the hotels into two groups, based on chain scale. Taking the six chain scales, we divided them as follows: luxury, upper upscale, and upscale hotels were classified as full service, while upper-midscale, midscale, and economy hotels were classified as limited-service hotels. (In

---

15 For example, see: John W. O'Neill, "Hotel Occupancy: Is the Three-Year Stabilization Assumption Justified?" *Cornell Hospitality Quarterly*, Vol. 52, 2 (May 2011), pp. 176-180; and Daniel Lesser, "Hotels Never Stabilize," Hotel News Now, February 2010 (www.hotelnewsnow.com/Articles.aspx/2671/Hotels-never-stabilize), viewed November 2011.

16 Cyert and March, *op.cit*.

17 Ganco and Agarwal, *op.cit*.

18 Walsh *et al., op.cit*.

Exhibit 1

Descriptive statistics and pearson product moment correlations

T	Variable	Mean	Standard Deviation	Correlation Coefficients					
				RevPAR	Occupancy	ADR	Market Demand	Entry Mode	Market Segment
1	**RevPAR**	80.50	61.41						
2	**Occupancy**	62.78	18.10	0.55					
3	**ADR**	123.24	71.03	0.92	0.24				
4	**Market Demand**	69.19	11.58	0.54	0.72	0.36			
5	**Entry Mode (Chain Affiliated vs Independent)**	0.88	0.33	-0.19	-0.11	-0.21	-0.21		
6	**Market Segment (1=luxury, 6=economy)**	3.45	1.01	-0.47	-0.13	-0.55	-0.15	0.22	
7	**Service Complexity**	0.46	0.50	0.41	0.18	0.44	0.24	-0.30	-0.84

Notes: All correlation coefficients are significant at $p < .0001$; Entry mode, chain affiliated hotel owner versus Independent hotel owner is a dummy variable in which chain = 1 and independent =0; Market segment is an indicator variable in which luxury hotels = 1 and economy hotels = 6; Service complexity is a dummy variable in which full service hotels = 1 and limited service hotels = 0.

the equation, this was indicated by another dummy variable, in which full service was 1 and limited service was 0.) We also controlled for each hotel's market segment to avoid inappropriately comparing two different types of hotel. By controlling for market segment, we are able to separate the effects of mode of entry from other characteristics of the hotel properties. In the equation, the market segment variable is a categorical variable with values ranging from 1 through 6, where one is for luxury properties and six for economy properties.

Data Analysis Approach

In our OLS regression, we analyzed the differences in performance due to mode of entry, while controlling for market demand conditions and the market segment of each property. Once again, RevPAR, occupancy, and ADR are the dependent variables, the entry mode indicator variable (chain affiliated or not) is the independent variable of interest and the market demand and market segment of the hotel are control variables.

As we said, we examine the differences due to service complexity. Consequently, the model was estimated for subsamples based upon two levels of service complexity (i.e., full service versus limited service). We analyzed the first two years of operating results during the four half-year periods of the first two years, that is, 0–6 months, 6–12 months, 12–18 months, and 18–24 months after entry. We wanted to analyze the four different post-entry time periods to establish whether the impact of mode of entry on performance is sustained over time, dissipates with time, or reverses over time. We conducted separate regression analyses for the four different time intervals and two levels of service complexity to avoid restricting the coefficients and to allow for both the possibility that learning effects may occur over time and that the learning curve may differ for low- and high-complexity hotels.

Results

Descriptive statistics and correlation coefficients for all of the variables are presented in Exhibit 1. Of the 104 properties that entered the U.K. market from 2006 through 2010, 83 percent were chain affiliated and 48 percent were full-service properties. The three performance variables are positively and significantly related—no surprise, given that RevPAR is the product of occupancy and ADR. However, we note that the stronger correlation occurs between ADR and RevPAR, rather than between occupancy and RevPAR. Also not particularly surprising, market demand is significantly and positively correlated with RevPAR.

The correlation between RevPAR and service complexity is positive and significant. Since service complexity is greater in full-service hotels, they usually command higher rates and tend to have higher RevPAR. The negative correlation between market segment and RevPAR implies that on average RevPAR for economy hotels is lower than that for luxury hotels, a situation that reflects typical market realities.

Limited-Service Hotels

The results of the regression analyses are shown in Exhibit 2 for limited-service hotels in each of the four post-entry time periods. These data indicate that independent hotels' performance is initially not significantly different from that

Exhibit 2

Results of regression analysis of mode of entry on performance for limited-service enterprises

Panel A: Dependent Variable RevPAR

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	-10.10	0.16	-22.05	0.05	-18.13	0.00	-24.88	0.00
Market Demand	1.54	0.00	1.59	0.00	1.63	0.00	1.50	0.00
Market Segment	-13.09	0.00	-11.72	0.00	-13.30	0.00	-15.53	0.00
Intercept	15.09	0.33	24.54	0.11	24.76	0.05	49.32	0.00
R-Square	0.58		0.57		0.58		0.52	
N	327		272		263		218	

Panel B: Dependent Variable Occupancy

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	1.93	0.71	2.04	0.76	0.60	0.84	-5.67	0.02
Market Demand	1.14	0.00	1.09	0.00	1.09	0.00	1.07	0.00
Market Segment	-4.40	0.00	1.47	0.24	-1.99	0.10	-5.19	0.00
Intercept	-8.06	0.46	-19.72	0.03	-0.39	0.95	21.64	0.00
R-Square	0.57		0.60		0.66		0.66	
N	327		272		263		218	

Panel C: Dependent Variable ADR

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	-26.80	0.01	-43.93	0.00	-28.74	0.00	-29.48	0.00
Market Demand	0.93	0.00	0.96	0.00	0.89	0.00	0.86	0.00
Market Segment	-18.28	0.00	-18.13	0.00	-16.18	0.00	-14.90	0.00
Intercept	142.00	0.00	150.69	0.00	127.29	0.00	123.68	0.00
R-Square	0.23		0.37		0.37		0.29	
N	327		272		263		218	

of franchised properties, as shown in Panel A of Exhibit 2. Although the magnitude of the difference in RevPAR according to entry mode in the first six months appears large, at -10.10, it is insignificantly different from zero. However, after the initial six-month period, the superior RevPAR performance of the independent properties is statistically significant.

The difference in the two groups' RevPAR is driven primarily by the stronger average daily rate recorded by the independents rather than occupancy differences, as shown

Exhibit 3

Results of regression analysis of mode of entry on performance for full-service enterprises

Panel A: Dependent Variable RevPAR

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	22.18	0.00	17.99	0.06	-13.29	0.22	-17.89	0.13
Market Demand	4.42	0.00	4.61	0.00	4.01	0.00	3.53	0.00
Market Segment	-46.90	0.00	-46.85	0.00	-66.31	0.00	-46.19	0.00
Intercept	-112.81	0.00	-120.14	0.00	-0.32	0.99	-11.79	0.74
R-Square	0.44		0.38		0.45		0.44	
N	307		250		210		152	

Panel B: Dependent Variable Occupancy

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	1.17	0.54	4.31	0.01	-0.15	0.93	3.55	0.09
Market Demand	1.10	0.00	1.12	0.00	0.90	0.00	1.08	0.00
Market Segment	1.91	0.18	1.80	0.11	0.57	0.58	1.54	0.17
Intercept	-27.44	0.00	-21.17	0.00	6.10	0.24	-10.73	0.09
R-Square	0.45		0.53		0.55		0.64	
N	307		250		210		152	

Panel C: Dependent Variable ADR

	Age in Months							
	0-6		6-12		12-18		18-24	
Independent Variables	Coef	P-value	Coef	P-value	Coef	P-value	Coef	P-value
Entry Mode (Chain Affiliation)	12.82	0.20	7.63	0.50	-17.88	0.14	-28.66	0.06
Market Demand	3.94	0.00	3.98	0.00	3.31	0.00	2.64	0.00
Market Segment	-77.14	0.00	-67.80	0.00	-80.27	0.00	-71.58	0.00
Intercept	71.68	0.03	33.48	0.41	128.17	0.00	163.98	0.00
R-Square	0.37		0.32		0.41		0.38	
N	307		250		210		152	

in Exhibit 2, Panels B and C. The independent operators achieved significantly higher prices than franchise hotels in all four of the post-entry time periods. The occupancy difference was not significant for the first three time periods, but independent hotels delivered significantly higher occupancy for the final time period of the study (18–24 months after entry).

Full-Service Hotels

The story is different for full-service hotels, as shown in Exhibit 3. For these properties, the franchising approach to market entry had a significant impact on post-entry performance during the first six months of operation. After that initial advantage, however, the differences in RevPAR

Exhibit 4

The economic impact of the differences in entry mode

Age in Months	Average Number of Rooms	Average RevPAR	Entry Mode (Chain Affiliation) Coefficient	Room Revenue (Independent - Chain)			
				Independent	Chain Affiliation	Difference	Percentage Difference
Service Complexity: Limited Service							
0-6	4082.10	$50.36	0.00	$1,233,475.46	$1,233,475.46	$0.00	0.00%
6-12	4228.14	$58.16	-22.05	$1,475,358.86	$916,074.21	$559,284.64	61.05%
12-18	4201.98	$62.71	-18.13	$1,581,142.67	$1,124,066.31	$457,076.36	40.66%
18-24	3947.89	$61.38	-24.88	$1,454,038.88	$864,633.95	$589,404.94	68.17%
Sum				$5,744,015.87	$4,138,249.93	$1,605,765.94	38.80%
Annual Average				$2,872,007.93	$2,069,124.96	$802,882.97	38.80%
Service Complexity: Full Service							
0-6	5262.07	$95.92	22.18	$3,028,450.57	$3,728,630.91	-$700,180.34	-23.12%
6-12	5464.49	$109.33	0.00	$3,584,628.75	$3,584,628.75	$0.00	0.00%
12-18	5277.51	$116.72	0.00	$3,696,080.99	$3,696,080.99	$0.00	0.00%
18-24	5038.77	$115.08	0.00	$3,479,261.77	$3,479,261.77	$0.00	0.00%
Sum				$13,788,422.08	$14,488,602.42	-$700,180.34	-5.08%
Annual Average				$6,894,211.04	$7,244,301.21	-$350,090.17	-5.08%

Notes: If the coefficient of the entry mode (Chain Affiliation) variable was not significant at the 5% level or better, its value was set to zero. Room revenue difference was computed as Independent less Chain. The percentage difference was computed as the room revenue difference divided by Chain room revenue and divided by Independent room revenue for both limited service and full service.

faded, and we found no significant differences in franchised and independent performance in the three subsequent time periods. Our analysis found that the franchise hotels' RevPAR advantage seemed to be driven by occupancy rather than rate. In particular, the franchises obtained significantly higher occupancy levels in period two, six to twelve months post-entry, but that difference subsided over time. We found no significant differences in ADR based on entry mode.

In sum, we found that entrepreneurs who elected to enter markets with unbranded, independent limited-service hotels experienced higher post-entry performance six months to twenty-four months after entry than did their counterparts who entered with a franchise affiliation. For full-service hotels, franchisees had an initial advantage (in the first six months of operation), but after the first year, full-service properties lost their occupancy advantage and the two groups did not show significantly different performance.

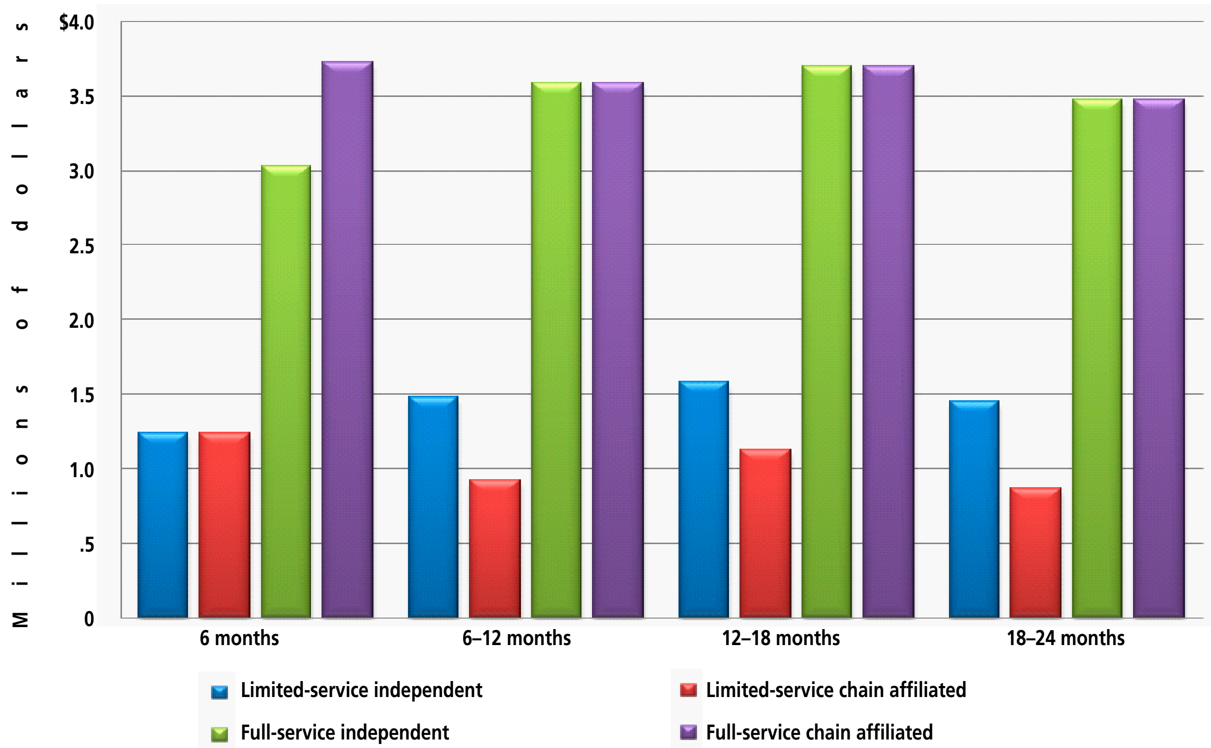
The economic importance of the differences in the mode of entry is shown in Exhibit 4 and Exhibit 5, which is on the next page. On average, limited-service franchised hotels earned about $1.6 million less in room revenue over the first two years of operation than did independent limited-service hotels, a difference of about 39 percent. Turning to full-service hotels, Exhibit 4 shows that for the first six months of operation independent hotels earned 23 percent less in rooms revenue than their franchise affiliated counterparts. Over the two-year period, this represents 5 percent less annual rooms revenue for unbranded new entrants.

Discussion and Conclusions

This study compared the performance outcomes of new hotels that purchased franchises to enter the market as against those that opened as independents. The results suggest that affiliation with a brand makes it easier for full-service hotels to ramp up revenues in the first six months, thanks to stronger occupancy. However, the results also suggest that the ready-made knowledge and skill that comes with the franchise system for full-service hotels do not provide a sustained performance advantage. While new full-service branded hotels did not have a significant ADR advantage over independent hotels, their occupancy advantage was brief and the overall RevPAR benefit lasted just six months.

Exhibit 5

Room revenue for new limited-service and full-service independent and chain-affiliated hotels in first two years, by month



The outcomes for independent limited-service hotels are particularly interesting. Independent owners of limited-service properties who choose not to "buy" a business model obtained higher levels of performance. The results suggest that independent hotels obtained higher ADRs than their branded counterparts right from the beginning, indicating a distinct possibility that their pricing strategy was the key to their higher performance. It took six months for limited-service independent hotels to gain a RevPAR performance advantage, but after that time these new businesses had a sustained ADR advantage when compared to their franchised counterparts.

Limitations. The chief limitation of our study is that it was conducted in just one country, albeit a cosmopolitan nation with many cultural groups. Given that this study was conducted in hotels in the U.K., it is possible that British customers have a stronger preference for non-branded services than those in other countries, and that financing of hotels is less driven by branding. Future research should be conducted in other countries and regions of the world to determine whether entry mode might be linked to customers' preferences connected with hotel brands. This study shows a strong price and revenue advantage for owner-entrepreneurs. While the traditional provision of explicit knowledge available for purchase via franchising may not yield a performance advantage, collaboration with others external to a new venture, in the form of open innovation and user-facing social networks, may be a powerful and less costly way to obtain the knowledge needed to operate a limited-service hotel.

Finally, the practical implications of our results (as shown in Exhibit 4) allow us to calculate the financial benefit obtained from the two different entry modes. New ventures in the limited-service domain reaped a 39-percent revenue advantage with the gains increasing over time by entry as independent hotels. In contrast, full-service hotels gained a 5-percent revenue advantage by affiliation with a franchise, with all of the gain occurring in the first six months. If the fees attached to brand franchises were factored into the analysis this gain would diminish considerably over time. In conclusion, these findings suggest that in the U.K. those who provide capital to fund hotel development may wish to rethink the importance of brand affiliation in delivering performance, particularly if the hotel is a limited-service product. ■

Cornell Center for Hospitality Research
Publication Index
www.chr.cornell.edu

Cornell Hospitality Quarterly

http://cqx.sagepub.com/

2011 Reports

Vol. 11 No. 20 Restaurant Daily Deals: Customers' Responses to Social Couponing, by Sheryl E. Kimes, Ph.D., and Utpal Dholakia, Ph.D.

Vol. 11 No. 19 To Groupon or Not to Groupon: A Tour Operator's Dilemma, by Chekitan Dev, Ph.D., Laura Winter Falk, Ph.D., and Laure Mougeot Stroock

Vol. 11 No. 18 Network Exploitation Capability: Mapping the Electronic Maturity of Hospitality Enterprises, by Gabriele Piccoli, Ph.D., Bill Carroll, Ph.D., and Larry Hall

Vol. 11 No. 17 The Current State of Online Food Ordering in the U.S. Restaurant Industry, by Sheryl E. Kimes, Ph.D.

Vol. 11 No. 16 Unscrambling the Puzzling Matter of Online Consumer Ratings: An Exploratory Analysis, by Pradeep Racherla, Ph.D., Daniel Connolly, Ph.D., and Natasa Christodoulidou, Ph.D.

Vol. 11 No. 15 Designing a Self-healing Service System: An Integrative Model, by Robert Ford, Ph.D., and Michael Sturman, Ph.D.

Vol. 11 No. 14 Reversing the Green Backlash: Why Large Hospitality Companies Should Welcome Credibly Green Competitors, by Michael Giebelhausen, Ph.D., and HaeEun Helen Chun, Ph.D.

Vol. 11 No. 13 Developing a Sustainability Measurement Framework for Hotels: Toward an Industry-wide Reporting Structure, by Eric Ricaurte

Vol. 11 No. 12 Creating Value for Women Business Travelers: Focusing on Emotional Outcomes, by Judi Brownell, Ph.D.

Vol. 11 No. 11 Customer Loyalty: A New Look at the Benefits of Improving Segmentation Efforts with Rewards Programs, by Clay Voorhees, Ph.D., Michael McCall, Ph.D., and Roger Calantone, Ph.D.

Vol. 11 No. 10 Customer Perceptions of Electronic Food Ordering, by Sheryl E. Kimes, Ph.D.

Vol. 11 No. 9 2011 Travel Industry Benchmarking: Status of Senior Destination and Lodging Marketing Executives, by Rohit Verma, Ph.D., and Ken McGill

Vol 11 No 8 Search, OTAs, and Online Booking: An Expanded Analysis of the Billboard Effect, by Chris Anderson Ph.D.

Vol. 11 No. 7 Online, Mobile, and Text Food Ordering in the U.S. Restaurant Industry, by Sheryl E. Kimes, Ph.D., and Philipp F. Laqué

Vol. 11 No. 6 Hotel Guests' Reactions to Guest Room Sustainability Initiatives, by Alex Susskind, Ph.D. and Rohit Verma, Ph.D.

Vol. 11 No. 5 The Impact of Terrorism and Economic Shocks on U.S. Hotels, by Cathy A. Enz, Renáta Kosová, and Mark Lomanno

Vol. 11 No. 4 Implementing Human Resource Innovations: Three Success Stories from the Service Industry, by Justin Sun and Kate Walsh, Ph.D.

Vol. 11 No. 3 Compendium 2011

Vol. 11 No. 2 Positioning a Place: Developing a Compelling Destination Brand, by Robert J. Kwortnik, Ph.D., and Ethan Hawkes, M.B.A.

Vol. 11 No. 1 The Impact of Health Insurance on Employee Job Anxiety, Withdrawal Behaviors, and Task Performance, by Sean Way, Ph.D., Bill Carroll, Ph.D., Alex Susskind, Ph.D., and Joe C.Y. Leng

2011 Hospitality Tools

Vol. 2 No. 4 ServiceSimulator v1.19.0, by Gary M. Thompson, Ph.D.

Vol. 2 No. 3 The Hotel Competitor Analysis Tool (H-CAT): A Strategic Tool for Managers, by Cathy A. Enz, Ph.D., and Gary M. Thompson, Ph.D.

Vol. 2 No. 2 Hotel Valuation Software, Version 3, by Stephen Rushmore and Jan A. deRoos, Ph.D.

Vol. 1. No. 7 MegaTips 2: Twenty Tested Techniques for Increasing Your Tips, by Michael Lynn

2011 Industry Perspectives

Vol. 2 No. 1 The Game Has Changed: A New Paradigm for Stakeholder Engagement, by Mary Beth McEuen

2011 Proceedings

Vol. 3 No. 7 Improving the Guest Experience through Service Innovation: Ideas and Principles for the Hospitality Industry, by: Cathy A. Enz, Ph.D.

Vol. 3 No. 6 Fresh Thinking about the Box, by: Chekitan S. Dev, Ph.D., and Glenn Withiam

Vol 3, No. 5 Building Brands in the Internet Age: Analytics, Loyalty, and Communication, by Glenn Withiam

www.chr.cornell.edu