

Cornell University School of Hotel Administration

The Scholarly Commons

Articles and Chapters

School of Hotel Administration Collection

6-2013

The Relationship between New Venture Entry Mode and Firm Performance

Cathy A. Enz

Cornell University School of Hotel Administration, cae4@cornell.edu

Linda Canina

Cornell University, lc29@cornell.edu

Daniel Palacios-Marques

Universitat Politecnica de Valencia

Follow this and additional works at: <https://scholarship.sha.cornell.edu/articles>



Part of the [Entrepreneurial and Small Business Operations Commons](#), and the [Hospitality Administration and Management Commons](#)

Recommended Citation

Enz, C. A., Canina, L., & Palacios-Marques, D. (2013). *The relationship between new venture entry mode and firm performance*[Electronic version]. Retrieved [insert date] from Cornell University, School of Hotel Administration site: <http://scholarship.sha.cornell.edu/articles/612>

This Article or Chapter is brought to you for free and open access by the School of Hotel Administration Collection at The Scholarly Commons. It has been accepted for inclusion in Articles and Chapters by an authorized administrator of The Scholarly Commons. For more information, please contact hotellibrary@cornell.edu.

If you have a disability and are having trouble accessing information on this website or need materials in an alternate format, contact web-accessibility@cornell.edu for assistance.

The Relationship between New Venture Entry Mode and Firm Performance

Abstract

Grounded in the knowledge-based view of the firm, this paper compares the performance outcomes from different modes of new venture entry. Data from new hotels entering the United Kingdom between 2006-2010 was used to explore how entry mode (i.e., franchised or independent) impacts post-entry firm performance. Controlling for market demand and market segments, this study found that affiliation with a franchise made it easier for new owners to ramp up revenues in the first six months if the service had a high level of operational complexity (e.g., full-service hotels). After this initial benefit period no significant performance benefit accrued to branded frill-service hotels. In contrast, hotels that offered less complex services obtained higher levels of performance when relying on independent status vs. brand affiliation between six and twenty-four months after entry. Implications of the results are offered in the context of determining the value of explicit versus tacit knowledge obtained from external sources versus going it alone as an entrepreneur.

Keywords

hotels, market entry, entrepreneurs, independent hotels, franchise

Disciplines

Entrepreneurial and Small Business Operations | Hospitality Administration and Management

Comments

Required Publisher Statement

© Springer. Final version published as: Enz, C. A., Canina, L., & Palacios-Marques, D. (2013). The relationship between new venture entry mode and firm performance. *International Entrepreneurship and Management Journal*, 9(2), 129-145. doi:10.1007/s11365-011-0192-1

Reprinted with permission. All rights reserved.

The Relationship between New Venture Entry Mode and Firm Performance

Cathy A. Enz, Cornell University
Linda Canina, Cornell University
Daniel Palacios-Marques, Universitat Politècnica de Valencia

Grounded in the knowledge-based view of the firm, this paper compares the performance outcomes from different modes of new venture entry. Data from new hotels entering the United Kingdom between 2006-2010 was used to explore how entry mode (i.e., franchised or independent) impacts post-entry firm performance. Controlling for market demand and market segments, this study found that affiliation with a franchise made it easier for new owners to ramp up revenues in the first six months if the service had a high level of operational complexity (e.g., full-service hotels). After this initial benefit period no significant performance benefit accrued to branded frill-service hotels. In contrast, hotels that offered less complex services obtained higher levels of performance when relying on independent status vs. brand affiliation between six and twenty-four months after entry. Implications of the results are offered in the context of determining the value of explicit versus tacit knowledge obtained from external sources versus going it alone as an entrepreneur.

Franchising is an important mode of entry for entrepreneurs in the service sector. However entrepreneurs often go it alone by entering a new market as an independent and unaffiliated venture hoping to offer rare and unique new services. Understanding the relative performance of franchised vs. unaffiliated modes of new market entry is important for future entrepreneurs as well as for effective strategic management. Within the strategy literature the knowledge-based view of the firm argues that firms have a set of knowledge assets that are used to create value (Grant 1996). Using this perspective knowledge is a particularly important resource for building capabilities that when viewed as unique, valued, and difficult to imitate can confer competitive advantage and subsequent performance (Barney 1995). Since knowledge can be accessed from external sources through franchising, or generated

internally it is valuable to compare the performance outcomes of new ventures that acquire knowledge assets through different forms, and thus have different modes of entry.

Firms that sell a business-format franchise provide franchisees (i.e., owners) of new ventures accumulated learning, and experience based on a proven brand, access to distribution, functional area expertise, and infrastructure. A franchisor sells access to information and the right to use its brand name, while the franchisee provides labor and capital in the form of employing employees, financial resources and physical assets (Michael 2009; Combs et al. 2004). This mode of new venture entry relies partly on explicit knowledge that can be transferred across businesses, individuals, locations, and time, referred to as codified knowledge as well as the existing tacit knowledge of the entrepreneur. An entrepreneur who enters a new market without brand affiliation must either build or already possess knowledge, in addition to labor and capital. In this entry mode the entrepreneur's knowledge is less likely to be codified, and thus embodied in the owner's actions and those of key employees.

While entrepreneurs are likely to possess tacit knowledge regardless of their mode of entry, the resource-based view of the firm would suggest that it is the tacit or "unique" knowledge resources that confer advantage and deliver above average rates of return. Given this argument it would be reasonable to argue that entrepreneurs without brand affiliation would be as likely as those with a brand to achieve high levels of performance. Of course, if a brand affiliated entrepreneur could build relatively more unique resources than an independent entrepreneur because their purchase of codified brand knowledge frees up time to focus more on building and incorporating tacit knowledge then we would expect the brand affiliated entrepreneur to have more performance success. Clearly how an entrepreneur builds or acquires their knowledge base at entry defined by their entry mode, is a strategic decision that we argue has implications for post-entry performance.

In this paper we are interested in exploring how the entry mode of a new business (i.e., franchised or independent) impacts post-entry performance over the first two years of operation. Our arguments are grounded in the knowledge-based view of the firm and derived from the literature on organizational learning and knowledge acquisition (Grant 1996; Levitt and March 1988). The context of our study is the service sector in the United Kingdom (UK) because of the critical role of knowledge-based assets in service firms and the impact these firms have on overall economic growth in developed countries. For example, in the UK services represent 74 percent of gross domestic product (Office of National Statistics 2011). We focus on hotels because little work has been done on soft service firms that sell experiences using low-wage service employees in partnership with the knowledge of external sources such as franchisees, even though these types of services dominate the business landscape

(Walsh et al. 2008; Leon-Darder et al. 2011). 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 (i.e., Andriessen 2005; Goldstein and Ward 2004; Hitt et al. 2001; Wang 2005). In addition, we selected the lodging industry as our setting for this investigation because of the popularity of franchising in this service sector and the large number of new entrants into the industry. Finally, recent work on knowledge assets in hotels found that investments in brand affiliation (explicit external knowledge) were a strong predictor of firm performance, but that for complex hotel operations investments in service employees (tacit knowledge) was also a strong predictor of firm performance (Walsh et al. 2008). This emerging area of study in low-wage service firms is an important complement to the services literature, while also offering a large number of entrepreneurs with the option of entry using either a franchise or independent entry mode.

This paper begins with a review of the literature on organizational learning, experience and knowledge assets. We discuss the linkage between tacit and explicit knowledge assets and the market entry strategies of franchised versus independent entrepreneurs. The level of firm operating complexity is introduced as a possible factor in determining the level of knowledge required for new business entry. Based on the discussion, we explore how the mode of entry of new hotel businesses impacts firm performance over the first two years of operation.

Organizational Learning, Experience and Market Entry

Organizational learning is a process whereby organizations increase their knowledge and add to their bundle of capabilities (Levitt and March 1988). The learning in organizations is often formalized in rules and routines that are institutionalized and deployed in the future (Cyert and March 1963). The accumulation of learning over time comprises the knowledge and skill that we refer to as experience. In the literature on diversified firms, pre-entry experience was found to have an impact on post-entry performance when entering into a new industry (Ganco and Agarwal 2009; Helfat and Lieberman 2002). For these diversifying entrants, their financial, managerial, marketing, and technological capabilities provide resource based advantages. Other researchers have found that experienced firms who enter new industries have a performance advantage that is due to their access to distribution channels and complementary assets (Mitchell 1991). The relevance of the experience is particularly important in influencing performance of new entrants in a new industry (Carroll et al. 1996). 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 (Dimov and Martin de Holan 2010). In addition, research has found that prospective customers rely on a firm's brand as a signal of new entrant product quality, which may confer a performance advantage on entrepreneurs who are brand affiliated (Erdem et al. 2006; Kirmani and Rao 2000). These studies suggest that prior experience does contribute to future performance.

The experience and the knowledge that grow out of building a franchise may make it faster and easier for franchisees to ramp up revenues and succeed in a new venture. Given the previous literature on the importance of experience, a new franchisee can vicariously capture existing franchisor knowledge without having to make mistakes associated with new learning. Under these conditions of assimilation and knowledge transfer we would expect that brand affiliated firms would have a better likelihood of high performance than their independent business counter parts. Increased knowledge accumulated by the franchisor through a high volume of service transactions could be shared with a new franchisee and thus benefits might accrue as a result of the former partner's economies of scale (Chesbrough 2011). The "liability of newness," thought to plague new ventures because of their lack of specific capabilities could be mitigated by affiliation with and exploitation of an existing franchise system's knowledge (Stinchcombe 1968). In addition, established brands have legitimacy in the marketplace. However, knowledge that is sold to a new entrant is explicit, such as procedures and operating standards. In contrast to tacit knowledge, explicit knowledge is thought to be easy to replicate among many users (at lower costs for the franchisor) but with less unique advantage.

Tacit Knowledge, Open Innovation and the Independent Entrepreneur

Established franchises may encumber new entrants with existing processes, systems, internal politics and cultural factors that contribute to structural inertia (Christensen 1997). Indeed the absence of access to existing and conventional knowledge may allow non-brand affiliated new entrants to engage in creative destruction (Schumpeter 1934). However, innovation may flourish for these new entrants, particularly in environments where prior experience is less useful because it is not applicable/transferable or the value of previous learning deteriorates (Ganco, and Agarwal 2009). Lock-in effects of affiliation with a brand may also preclude partnerships with other viable firms, such that independent entrepreneurs may be in a position to more flexibly form external relationships with various partners and suppliers using alliances as a portfolio of options (Gulati et al. 2000; Geyskens et al. 2006).

Systematically obtaining, retaining, and exploiting knowledge inside and outside of an organization's boundaries is referred to as open innovation (Lichtenthaler 2011). Open innovation asserts that firms can use both external knowledge as well as internal ideas through an array of

interorganizational relationships many of which are reciprocal, temporary, informal, and even non-contractual (Chesbrough 2011). Independent entrepreneurs have chosen not to “buy” a business model (i.e., franchise affiliation), but they may still be actively externally sourcing particular technologies or engaging in external knowledge communities. Hotels for example often partner with celebrity chefs to operate a restaurant inside the hotel, or work with local tourism associations to enhance a destination. In these cases, critical knowledge- management processes may be shared. Traditional conceptions of the liability of newness (Stinchcombe 1965) are at odds with the conditions facing firms today in which Web-based commerce allows new ventures to obtain more easily specialized skills from a wide range of firms (Morse et al. 2007; Cox and Mason 2007). With the proliferation of user-facing social networks in areas such as travel and tourism, independent entrepreneurs can also collaborate with users in the external exploration of new knowledge (von Hippel 1988). Innovative independent entrepreneurs may wish to keep their options open by making smaller investments in external knowledge versus a long-term commitment to a franchise to assure as much flexibility as possible (van de Vrande et al. 2009).

If explicit knowledge such as that provided by franchisors is easily available in the open market for sale on a shorter-term basis, then tacit knowledge embedded in actions may become a more important source of performance advantage (Meliá et al. 2010). Indeed, tacit knowledge does not have easy transference and is located among the employees where the knowledge lies. Because it is unique and difficult to transfer, tacit knowledge is more intangible and thus an important source of competitive advantage. Tacit knowledge is linked to context and because it is location dependent, independently operated new entrants may be better able to adapt to local needs and build more organic and less rigid operating structures than franchised new entrants (Levinthal and March 1993; Brookes and Roper 2010). Combining the flexibility of open external knowledge sourcing with the difficulty of imitation of tacit knowledge, entry to new markets as an independent entrepreneur may yield higher post-entry performance than lock-in with a brand affiliation.

Operating Complexity

Not all new ventures within the service sector have the same levels of operating complexity. The level of operational complexity in a service may alter the degree to which explicit and tacit knowledge is needed and the overall degree to which prior experience is helpful. In the lodging industry fairly well structured and carefully defined segments exist based on the extent to which hotels are differentiated on quality and services offered (Mazzeo 2002). The classifications are an indication of the “credible commitment” made by firms to a particular level of service quality (Ingram 1996). The more complex the

new venture, the more likely the “liability of newness,” and the greater the value that may be obtained from franchisor knowledge. In contrast, new ventures with less service complexity may be easier for independent entrepreneurs to successfully operate.

According to both entrepreneurs and venture capitalists, the most common reasons why new ventures fail are internal (Zacharakis et al. 1999). The lack of entrepreneur management skill and experience, along with the lack of capital are key reasons for high failure rates in many services (Enz 2010; Enz and Harrison 2008). For some services low barriers to entry make it possible for inefficient operators lacking skill, experience, and solid financial backing to enter the industry (English et al. 1996). Because of the high fixed costs and the operating complexity of opening a new full-service hotel, brand affiliation may yield a performance advantage for these types of firms.

In addition to differences in operating complexity requiring more or less knowledge acquisition, the literature on agglomeration economics would suggest that physical proximity to some types of competitors (i.e., geographic clusters) in an industry leads to higher performance (Baum and Haveman 1997). Competitors with less operating complexity may enjoy performance benefits as a result of co-location with others in the industry without making similar resource investments (Baum and Haveman 1997; Canina et al. 2005; Enz et al. 2008). In a study of U.S. hotels, Canina et al. (2005) found that lower-level hotels gained performance benefits by co-locating next to hotels in higher service quality segments. Performance spillover benefits for lower-end hotels would suggest that entrepreneurs who enter in less complex segments may be the beneficiaries of advantage regardless of their own assets. This idea is intriguing in the context of this study because it suggests that for entrepreneurs who start a less complex business the knowledge investments of other firms can be extracted without their cooperation or consent. In light of this body of research and taking into consideration operating complexity, defined by the level of service provision promised in different segments of the industry, this study will explore new starts separately for high-end full service hotels and low-end limited service hotels.

Performance Over Time

By examining new venture performance within the first two years of operation we can compare franchised with independent hotels over time. With time, new ventures refine their routines and their capabilities grow (Cyert and March 1963). Performance advantage would then likely reside in franchised new ventures early on because of their existing routines and established capabilities. The longer a venture exists the more organizational learning is possible, and thus over time the advantages of brand

affiliation should subside. Independent new ventures because of the lack of experience and existing routines may be at an initial performance disadvantage but, over time, may have greater performance advantages because of their flexibility and the acquisition of new knowledge that may more closely align the new venture with market needs.

While we have made the argument that new franchisees will be more successful than independent entrepreneurial enterprises at entry due to experience, and their explicit knowledge assets, it is also possible that the opposite outcome might be the case. Independent entrepreneurs may benefit from open innovation, and tacit knowledge, A review of the extant literature would suggest that there is inconclusive evidence to offer a compelling argument for one entry mode over the other being most likely to elicit a performance advantage (Ganco and Agarwal 2009). In addition we have argued that agglomeration spillover and timing are critical dynamics that must also be factored into our consideration of entry mode. 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. The lack of systematic empirical research on entrepreneurial learning, and the absence of studies that contrast knowledge acquisition and creation in franchise vs. independent new ventures suggest that the current study stands to make a contribution to our understanding of the role of knowledge-based assets in new venture entry. By introducing time intervals and the level of service quality into our discussion, a more refined examination is possible.

The previous discussion suggests that there is not a clear and compelling argument to hypothesize that one mode of entry is preferable to another in predicting post-entry performance. While brand experience might favor a franchise entry mode, non-branded entrants are not encumbered by existing processes, cultural factors, high levels of standardization or structural inertia (Cox and Mason 2007). In addition, the service complexity of the business may influence performance. While previous research in hotels has found that the greater the investment in brand affiliation the higher the level of performance for existing businesses (Walsh et al. 2008), the benefits of brand versus independent status for new entrants has been left unexplored. In this study we examine entry mode and firm performance taking into consideration the level of complexity of the service business, however we do not directly measure the types of knowledge entrepreneurs bring to their new ventures.

Methodology

Data Sources

Our sample consists of 104 hotels that entered the U.K. market over the 2006-2010 period. The location types of these hotels include urban, suburban, airport, interstate, resort and small metropolitan towns. The data for new hotels was obtained from Smith Travel Research (STR) Global, an independent research organization that tracks lodging performance for hotels worldwide. STR has one of the most comprehensive data sources available on the lodging industry, and the data was obtained through strict and exclusive confidentiality arrangements.

The Smith Travel data consist of monthly hotel-level performance data—room revenue and rooms sold for each property and for the competitive set of each property. In addition, Smith Travel supplied categorical variables that describe characteristics of each firm. These data include 1) the number of rooms in the hotel; 2) the product/service quality segment category of the hotel (these variables will be clarified later); and 3) whether the property is chain-affiliated.

Primary Variables

One of the most important performance measures in the lodging industry is revenue per available room, commonly called RevPAR (Chung and Kalnins 2001; Ismail et al. 2002). This measure of performance serves as the basis for long-term business planning, and is used as a guide by investors, hotel owners, and firm-level general managers. RevPAR is calculated by taking the revenue generated by rooms sales and dividing that by the number of rooms available for sale in the time period (Enz et al. 2001). RevPAR was calculated monthly for each hotel and served as the dependent variable in this study. Two additional performance measures were used in this study; average daily rate (ADR) and hotel occupancy. ADR is computed as monthly room revenue divided by monthly rooms sold. Occupancy is defined as the percentage of available rooms that were sold during the month, calculated by dividing the monthly number of rooms sold by monthly rooms available.

To determine entry mode, new hotels were characterized as either having a hotel chain affiliation or being independently operated using a zero/one indicator variable that represents a hotel as either brand affiliated (1) or independent (0). The assignment of a new hotel to one of these operating forms was based on information provided by the hotels and classified in the hotel census database of STR global.

Control Variables

Market demand and market segments are two critical control variables included in this study because they can have a significant impact on firm performance. Since demand conditions vary across hotel properties, the occupancy percentage of competitor hotels was included as a proxy for market demand. The competitive set consists of a group of comparable hotels that are used by a hotel for performance comparisons. The data provider in collaboration with each hotel select a minimum of four competing hotels that are included in 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.

The lodging industry is highly segmented on attributes such as amenities and service levels (Kent et al. 2010). Standard industry classifications are used to identify individual hotels as luxury, upper-upscale, upscale, upper-midscale, midscale, and economy. Appropriate testing of the model requires controlling for these market segments. As explanation, consider a situation in which two hotels enter the market, an upscale chain hotel and a luxury independent hotel. If the upscale hotel has an average room rate of \$200 and the luxury hotel's rate is \$600, then the only way the chain hotel could have higher RevPAR than the independent hotel is if its occupancy were three times higher. Since 100% is the highest possible occupancy rate, the luxury hotel would have to be nearly empty for this to happen. Although this is an extreme example, it demonstrates that the revenue of upscale hotels will typically not exceed that of luxury hotels. Consequently, it is important to control for market segment. By controlling for market segment, we are able to separate the effects of mode of entry from other characteristics of the hotel properties. 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

Ordinary least squares (OLS) was used to analyze the differences in performance due to mode of entry controlling for market demand conditions and the market segment of each property. Specifically, RevPAR, occupancy and ADR are the dependent variables, the entry mode (chain affiliated) indicator variable is the independent variable of interest and the market demand and market segment of the hotel are control variables.

To examine the differences due to service complexity and time, the model was estimated for subsamples based upon two levels of service complexity (i.e., full versus limited service) and four half years that occurred over the two year period. New entrants were grouped according to whether they were full-service high-end hotels, or limited-service hotels as indicators of the degree to which a group

of firms are providing a complex and highly differentiated level of service or a lower level of service at a modest price. The luxury, upper upscale and upscale hotels were classified as full service while upper-midscale, midscale and economy hotels were classified as limited-service hotels.

The two service complexity subsamples were divided further into four subsamples categorized by the number of half years since entry, namely, 0-6 months, 6-12 months, 12-18 months and 18-24 months after entry. For each of the two service complexity groups, the model was estimated for each of the four different post-entry time periods in order to establish whether or not the impact of mode of entry on performance is sustained over time, dissipates with time or reverses over time.

Results

Descriptive statistics and correlation coefficients for all of the variables are presented in Table 1. There were 104 new properties that entered the market over the 2006-2010 period of which 83% were chain affiliated and 48% were full service properties. The three performance variables are positively and significantly related. Since RevPAR is the product of occupancy and ADR the strong correlations are appropriate and consistent with what would be expected. Market demand is also significantly and positively correlated with hotel RevPAR, occupancy and ADR. This is not surprising since a rise in competitors' occupancy may imply an increase in local demand which in turn will cause ADR to increase as well as the property's occupancy to increase and as a result RevPAR will increase. The correlation between RevPAR and service complexity is positive and significant. Since service complexity is an indicator variable in which full service hotels take a value of one and limited service hotels a value of 0, higher quality and hence higher priced hotels will tend to have higher RevPAR. The negative correlation between market segment and RevPAR shows the importance of controlling for the differences in market segments within the two service complexity groups. The correlation does not account for RevPAR differences due to market segments. This negative correlation implies that on average RevPAR for economy hotels is lower than that for luxury hotels.

Table 1 Descriptive statistics and pearson product moment correlations

Variable	Mean	Std. Dev.	1	2	3	4	5	6
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

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 results of the regression analyses are shown in Table 2 for limited service hotels in each of the four post-entry time periods. The results in Panel A of Table 2 indicate that the performance advantage of entering the market as an independent hotel is greater than using franchising as the entry mode. No significant difference in RevPAR was explained by entry mode in the first six months of operation for new hotels. Even though the magnitude of the entry mode (chain affiliation) is large, -10.10, it is insignificantly different from zero. However, after the initial six months, statistically significant differences were found favoring a non-brand affiliation for market entry.

In order to more fully understand new entry mode on performance we conducted two additional regression analyses using hotel occupancy (demand) and average daily rate (price) as dependent variables shown in Table 2, Panels B and C, respectively. The additional analyses revealed that entrepreneurs that entered a market as independents achieved significantly higher prices than franchise hotels in all four of the post-entry time periods. The ability of one mode of entry to deliver greater occupancy was not significant for the first three time periods, but revealed that independent hotels delivered significantly higher occupancy during the time period 18-24 months after entry.

Table 3 shows the regression models for full service hotels. For these more complex service enterprises, deploying a franchising approach to market entry had a significant impact on post-entry performance in the first six months of operation. Entry mode of a new business did not significantly

predict performance in the three subsequent time periods. Supplemental analysis on the performance measure of occupancy showed new entrant franchise hotels obtained significantly higher occupancy levels six to twelve months post-entry, but these subsided over time. No significant differences in price (ADR) were found based on entry mode. Overall, entrepreneurs who selected 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 entrepreneurial counterparts who entered with a franchise affiliation. When entering full-service hotel markets, franchisee entrepreneurs had a temporary advantage in the first six months of operation, after which time the selection of entry mode was not a significant predictor of new venture performance.

The economic importance of the differences in the mode of entry is shown in Table 4. On average limited service franchised hotels earned about \$1.6 million less in room revenue over the first two years of operation than independent limited service hotels. On average, this represents about 19.4 percent of their annual room revenue. Turning to full-service hotels, Table 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 2.5 percent less annual rooms revenue than franchised new entrants, on average.

Discussion and Conclusions

This study compared the performance outcomes of new ventures that relied on different modes of entry. The results suggest that affiliation with a franchise makes it easier for franchisees to ramp up revenues in the first six months, if the product or service has a high level of operational complexity such as that found in full-service hotels. Entrepreneurs who purchase a franchise appear to benefit from the experience and knowledge that the brand brings in the first six months of their operation. It also appears that a franchise can help to offset the “liability of newness” that plagues new ventures that lack specific capabilities such as marketing expertise. The more complex the new venture the more likely the liability of newness can be diminished through brand affiliation. However, the results also suggest that the knowledge and skill that the brand of full-service hotels provided to the new operator does not provide a sustained performance advantage. An established brand may offer legitimacy and security for customers and marketing expertise that might explain the enhanced occupancy in the second half of the first year for the more expensive and complex hotel services explored in this study. It is interesting that a franchise mode of entry did not deliver a price premium for full-service hotels. Overall the role of experience, reputation, and explicit knowledge transfer thought to be provided by affiliation with a

brand franchise was not as important in determining post-entry performance for the entrepreneurs in our study. Perhaps because hotel services are based on local presence and cannot be exported the experience of the franchise may be less valuable than previously thought.

Table 2 Results of regression analysis of mode of entry on performance for limited service enterprises

Independent Variables	Age in months											
	0-6			6-12			12-18			18-24		
	Coef	Std Error	P-value	Coef	Std Error	P-value	Coef	Std Error	P-value	Coef	Std Error	P-value
Panel A: Dependent Variable RevPAR												
Entry Mode (Chain Affiliation)	-10.10	7.11	0.16	-22.05	11.20	0.05	-18.13	5.60	0.00	-24.88	5.05	0.00
Market Demand	1.54	0.08	0.00	1.59	0.09	0.00	1.63	0.09	0.00	1.50	0.11	0.00
Market Segment	-13.09	2.16	0.00	-11.72	2.06	0.00	-13.30	2.28	0.00	-15.53	2.47	0.00
Intercept	15.09	15.35	0.33	24.54	15.18	0.11	24.76	12.67	0.05	49.32	12.54	0.00
R-Square	0.58			0.57			0.58			0.52		
N	327			272			263			218		
Panel B: Dependent Variable Occupancy												
Entry Mode (Chain Affiliation)	1.93	5.10	0.71	2.04	6.74	0.76	0.60	2.94	0.84	-5.67	2.45	0.02
Market Demand	1.14	0.06	0.00	1.09	0.05	0.00	1.09	0.05	0.00	1.07	0.05	0.00
Market Segment	-4.40	1.55	0.00	1.47	1.24	0.24	-1.99	1.20	0.10	-5.19	1.20	0.00
Intercept	-8.06	11.00	0.46	-19.72	9.13	0.03	-0.39	6.64	0.95	21.64	6.09	0.00
R-Square	0.57			0.60			0.66			0.66		
N	327			272			263			218		
Panel C: Dependent Variable ADR												
Entry Mode (Chain Affiliation)	-26.80	10.69	0.01	-43.93	13.25	0.00	-28.74	6.19	0.00	-29.48	6.08	0.00
Market Demand	0.93	0.12	0.00	0.96	0.11	0.00	0.89	0.10	0.00	0.86	0.13	0.00
Market Segment	-18.28	3.24	0.00	-18.13	2.44	0.00	-16.18	2.52	0.00	-14.90	2.98	0.00
Intercept	142.00	23.07	0.00	150.69	17.95	0.00	127.29	14.01	0.00	123.68	15.10	0.00
R-Square	0.23			0.37			0.37			0.29		
N	327			272			263			218		

Table 3 Results of regression analysis of mode of entry on performance for full service enterprises

Independent Variables	Age in Months											
	0-6			6-12			12-18			18-24		
	Coef	Std Error	P-value	Coef	Std Error	P-value	Coef	Std Error	P-value	Coef	Std Error	P-value
Panel A: Dependent Variable RevPAR												
Entry Mode (Chain Affiliation)	22.18	7.81	0.00	17.99	9.50	0.06	-13.29	10.81	0.22	-17.89	11.60	0.13
Market Demand	4.42	0.30	0.00	4.61	0.42	0.00	4.01	0.41	0.00	3.53	0.41	0.00
Market Segment	-46.90	5.70	0.00	-46.85	6.68	0.00	-66.31	6.90	0.00	-46.19	6.26	0.00
Intercept	-112.81	24.96	0.00	-120.14	34.01	0.00	-0.32	35.15	0.99	-11.79	35.08	0.74
R-Square	0.44			0.38			0.45			0.44		
N	307			250			210			152		
Panel B: Dependent Variable Occupancy												
Entry Mode (Chain Affiliation)	1.17	1.93	0.54	4.31	1.60	0.01	-0.15	1.60	0.93	3.55	2.05	0.09
Market Demand	1.10	0.07	0.00	1.12	0.07	0.00	0.90	0.06	0.00	1.08	0.07	0.00
Market Segment	1.91	1.41	0.18	1.80	1.13	0.11	0.57	1.02	0.58	1.54	1.11	0.17
Intercept	-27.44	6.16	0.00	-21.17	5.74	0.00	6.10	5.21	0.24	-10.73	6.19	0.09
R-Square	0.45			0.53			0.55			0.64		
N	307			250			210			152		
Panel C: Dependent Variable ADR												
Entry Mode (Chain Affiliation)	12.82	9.96	0.20	7.63	11.28	0.50	-17.88	12.21	0.14	-28.66	15.17	0.06
Market Demand	3.94	0.39	0.00	3.98	0.50	0.00	3.31	0.46	0.00	2.64	0.53	0.00
Market Segment	-77.14	7.27	0.00	-67.80	7.93	0.00	-80.27	7.80	0.00	-71.58	8.19	0.00
Intercept	71.68	31.84	0.03	33.48	40.38	0.41	128.17	39.69	0.00	163.98	45.88	0.00
R-Square	0.37			0.32			0.41			0.38		
N	307			250			210			152		

Table 4 The economic impact of the differences in entry mode

Service complexity	Age in months	Average number of rooms	Average RevPAR	Entry Mode (Chain Affiliation) Coefficient	Room Revenue			
					Independent	Chain Affiliation	Difference	Percentage Difference
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	19.40%
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	–2.54%

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 limited service and full service, respectively.

What is particularly interesting in the context of service enterprises is the finding that independent entrepreneurs who choose not to “buy” a business model obtained higher levels of performance when offering limited service products. This finding offers preliminary support for the value of flexibility at entry and thus the importance of open external knowledge sourcing. The agglomeration co-location benefits often found with lower-quality hotels may also help to explain why limited-service branded hotels did not obtain even an initial advantage post-entry. In addition, it is possible that tacit knowledge, which is acquired through practice is a powerful source of advantage, yielding higher performance over time. It took six months post-entry for limited service independent hotels to gain a performance advantage, but after that time these new businesses had a sustained advantage when compared to their franchised counterparts. In the hospitality industry a major element of frontline employees’ work activities require personal interactions with guests that rely on tacit knowledge and are slow to build (Hallin and Mamburg 2008). Hence, the selection of an entry mode that facilitates a greater investment in tacit knowledge may be a key to long-term success in service firms in particular.

Hallin and Mamburg (2008) have argued that to date most of the work on knowledge management published in hospitality is anecdotal, limited, inconclusive and descriptive. This study is one of the few empirical efforts to study knowledge management in the hospitality context, and suggests that tacit knowledge in service enterprises may be even more important to performance than the easy to transfer explicit knowledge bought in the marketplace through brand affiliation. Given that this study was conducted in hotels in the U.K., it is also possible that European customers have a

stronger preference for non-branded services. Future research should be conducted in other regions of the world to determine whether entry mode might be linked to customer culture preference.

One limitation of the current study is the lack of direct measures of knowledge assets. Using mode of entry as an indirect indicator of explicit and tacit knowledge assets is not ideal. Future studies should aim to find more direct and quantifiable indicators of various types of knowledge acquisition and use. Nevertheless, the current study shows a strong price and revenue advantage for entrepreneurs who enter markets without the external resources and experience of existing brands. In the context of service firms, particularly when dealing with limited service delivery by low-skilled workers, going it alone may be anything but. 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 powerful and less costly ways of obtaining explicit knowledge from others. Future research could explore the role of collaboration from external knowledge providers in helping independent entrepreneurs gain advantage.

Finally, the practical implications of our results (as shown in Table 4) allows us to put dollars on the benefit obtained from the two different entry modes. New ventures in the limited service domain reaped a 39% revenue advantage with the gains increasing over time by entry as independent enterprises. In contrast, new ventures in full service hotels only gained a 5% revenue advantage by affiliation with a franchise, with all of the gain being provided in the first six months. If the fees attached to brand franchises were factored into the analysis this gain would overtime be reduced even further. Perhaps now is the time for entrepreneurs in the service sector to rethink the importance of using franchising as a new venture entry mode, particularly if the business does not require a high degree of complexity in service delivery.

References

- Andriessen, D. (2005). Implementing the KPMG value explorer. *Journal of Intellectual Capital*, 6, 474—488.
- Barney, J. (1995). Looking inside for competitive Advantage. *The Academy of Management Executive*, 9 (4), 49-61.
- Baum, J. A., & Haveman, H. A. (1997). Love thy neighbor? Differentiation and agglomeration in the Manhattan Hotel Industry 1898-1990. *Administrative Science Quarterly*, 42, 304—338.
- Brookes, M., & Roper, A. (2010). The impact of entry modes on the organizational design of international hotel chains. *Service Industries Journal*, 30(9), 1499-1512.

- Canina, L., Enz, C. A., & Harrison, J. (2005). Agglomeration effects and strategic orientations: evidence from the U.S. lodging industry. *The Academy of Management Journal*, 48(4), 565-581.
- Carroll, G., Bigelow, L., Seidel, M., & Tsai, L. (1996). The fates of de novo and de alio producers in the American automobile industry: 1885-1981. *Strategic Management Journal*, 17, 117-137.
- Chesbrough, H. (2011). *Open services innovation: Rethinking your business to grow and compete in a new era*. San Francisco: Jossey-Bass Publishing.
- Christensen, C. M. (1997). *The innovators dilemma: When new technologies cause great firms to fail*. Boston: Harvard Business School Press.
- Chung, W., & Kalnins, A. (2001). Co-locate effects and performance: a test of the Texas Lodging Industry. *Strategic Management Journal*, 22, 969-988.
- Combs, J. G., Michael, S. C., & Castrogiovanni, G. J. (2004). Franchising: a review and avenues to greater theoretical diversity. *Journal of Management*, 30(6), 907-931.
- Cox, J., & Mason, C. (2007). Standardization versus adaptation: geographical pressures to deviate from franchise formats. *Service Industries Journal*, 27(8), 1053-1072.
- Cyert, R. M., & March, J. G. (1963). *A behavioral theory of the firm*. Englewood Cliffs: Prentice-Hall.
- Dimov, D., & Martin de Holan, E. (2010). Firm experience and market entry by venture capital firms (1962-2004). *Journal of Management Studies*, 47:1 January 2010.
- English, W., Josiam, B., Upchurch, R., & Willems, J. (1996). Restaurant attrition: a longitudinal analysis of restaurant failures. *International Journal of Contemporary Hospitality Management*, 8(2), 17-20.
- Enz, C. (2010). *Strategic hospitality management: Concepts and cases* (2nd ed.). New York: Wiley Publishing Inc.
- Enz, C., & Harrison, J. (2008). Innovation and entrepreneurship in the hospitality industry. In R. Wood & B. Brothers (Eds.), *The handbook of hospitality management*. London: Sage Publishing.
- Enz, C., Canina, L., & Walsh, K. (2001). Hotel industry averages: an inaccurate tool for measuring performance. *The Cornell Hotel and Restaurant Administration Quarterly*, 42(6), 22-32.
- Enz, C., Canina, L., & Liu, Z. (2008). Competitive dynamics and pricing behavior in U.S. hotels: the role of co-location. *Scandinavian Journal of Hospitality and Tourism*, 8(3), 230-250.
- Erdem, T., Swait, J., & Valenzuela, A. (2006). Brands as signals: a cross-country validation study. *Journal of Marketing*, 70(January), 34-49.
- Ganco, M., & Agarwal, R. (2009). Performance differentials between diversifying entrants and entrepreneurial start-ups: a complexity approach. *Academy of Management Review* 34(2), 228-252.

- Geyskens, I., Steenkamp, J., & Kumar, N. (2006). Make, buy, or ally: a transaction cost theory meta-analysis. *Academy of Management Journal*, 49(3), 519-543.
- Goldstein, S. M., & Ward, P (2004). Performance effects on physicians' involvement in hospital strategic decisions. *Journal of Service Research*, 6, 361-372.
- Grant, R. M. (1996). Toward a knowledge-based theory of the firm. *Strategic Management Journal*, 17, 109-122.
- Gulati, R., Nohria, N., & Zaheer, A. (2000). Strategic networks. *Strategic Management Journal*, 21, 203-215.
- Hallin, C. A., & Mamburg, E. (2008). Knowledge management in the hospitality industry: a review of empirical research. *Tourism Management*, 29, 366-381.
- Helfat, C. E., & Lieberman, M. D. (2002). The birth of capabilities: market entry and the importance of pre-history. *Industrial and Corporate Change*, 11, 725-760.
- Hitt, M. A., Bierman, L., Shimizu, K., & Kochhar, R. (2001). Direct and moderating effects of human capital on strategy and performance in professional service firms: a resource-based perspective. *Academy of Management Journal*, 4, 13-26.
- Ingram, P (1996). Organizational form as a solution to the problem of credible commitment: the evolution of naming strategies among U.S hotel chains. *Strategic Management Journal*, 17(Special Issue), 85-98.
- Ismail, J. A., Dalbor, M. C., & Mills, J. E. (2002). Using RevPAR to analyze lodging-segment variability. *The Cornell Hotel and Restaurant Administration Quarterly*, 43(6), 73-80.
- Kent, S., Hackel, E., & Padmanabhan, S. (2010). *Lodging primer: Americas*. The Goldman Sachs Group, Inc.
- Kirmani, A., & Rao, A. R. (2000). No pain, no gain: a critical review of the literature on signaling unobservable product quality. *Journal of Marketing*, 64(April), 66-79.
- Levinthal, D. A., & March, J. G. (1993). The myopia of learning. *Strategic Management Journal*, 14, 95-112.
- Levitt, B., & March, J. G. (1988). Organizational learning. *Annual Review of Sociology*, 14, 319-340.
- Leon-Darder, Villar-Garcra, & Pla-Barber: (2011). Entry mode choice in the internationalization of the hotel industry: a holistic approach. *The Service Industries Journal*, 31(1), 107-122.
- Lichtenthaler, U. (2011). Open innovation past research, current debates, and future directions. *The Academy of Management perspectives*, 25(1), 75-93.

- Mazzeo, M. (2002). Product choice and oligopoly market structure. *The RAND Journal of Economics*, 33, 221-242.
- Meliá, M. R., Perez, A. B., & Dobón, S. R. (2010). The influence of innovation orientation on the internationalization of SMEs in the service sector. *Service Industries Journal*, 30(5), 777-791.
- Michael, S. C. (2009). Entrepreneurial signaling to attract resources: the case of franchising. *Managerial and Decision Economics*, 30, 405—422.
- Mitchell, W (1991). Dual clocks: entry order influences on incumbent and newcomer market share and survival when specialized assets retain their value. *Strategic Management Journal*, 12, 85-100.
- Morse, E. A., Fowler, S. W, & Lawrence, T. B. (2007). The impact of virtual embeddedness on new venture survival: overcoming the liabilities of newness. *Entrepreneurship Theory and Practice*, 31(2), 139-159.
- Office of National Statistics (2011). *Index of services*, <http://www.statistics.gov.uk/STATBASE/Product.asp?vlnk=9333>.
- Schumpeter, J. A. (1934). *The theory of economic development*. Cambridge: Harvard University Press.
- Stinchcombe, A. L. (1965). Social structure and organizations. In J. G. March (Ed.), *Handbook of organizations* (pp. 142-193). Chicago: Rand McNally.
- Stinchcombe, A. L. (1968). *Constructing social theories*. New York: Barcourt, Brace and World.
- van de Vrande, V, Vanhaverbeke, W, & Duysters, G. (2009). External technology sourcing: the effect of uncertainty on governance mode choice. *Journal of Business Venturing*, 24, 62-80.
- von Hippel, E. (1988). *The sources of innovation*. New York: Oxford University Press.
- Walsh, K., Enz, C., & Canina, L. (2008). The impact of strategic orientation on intellectual capital investments in customer service firms. *Journal of Service Research*, 10(4), 300-317.
- Wang, W (2005). An evaluation of the balanced scorecard in equity valuation. *Journal of Intellectual Capital*, 6, 206-221.
- Zacharakis, L., Meyer, G. D., & DeCastro, J. (1999). Differing perceptions of new venture failure: a matched exploratory study of venture capitalists and entrepreneurs. *Journal of Small Business Management* (July): 1-14.