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Keywords

operating arrangements, strategic management, chains, independent hotels, franchising

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Franchising and Other Operating Arrangements in the Lodging
Industry: A Strategic Comparison

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business strategy

Abstract

The objective of this paper is to compare, along three strategic dimensions, franchising with other types of operating arrangements in the lodging industry. The operating arrangements studied are, in addition to franchising, chain-managed and independent hotels. The three strategic dimensions include: (1) the variability or volatility of the task environment facing a hotel; (2) the business strategy chosen by a hotel's general manager; and (3) the level of sales revenue and profit margin achieved by a hotel.

The strategic management literature argues that an organization can only achieve superior performance when the characteristics of its task environment, its business strategy, and its decision structure (i.e. operating method or extent of vertical integration) are maligned. Thus, comparing franchising with the two other operating arrangements along these dimensions seems to be a first step in determining franchising's role in successful strategic coalignments. Hypotheses linking the different operating arrangements with task environment variability, business strategy, and performance were developed. A mail survey of hotel unit general managers, designed to test those hypotheses, was then described.

Chain-managed hotels were found to be more prevalent in stable and moderately stable environments than they were in volatile ones. A similar result was found for the independent units. Franchised units, however, were more prevalent in moderate and volatile environments.

Both chain-managed and franchised hotels predominantly followed the prospector business strategy while the independents were more closely associated with the defender strategy. A plausible reason for this is the importance chain managers and franchisors place on developing new markets and new products to achieve economies of scale. Evidently, in the lodging industry, the prospector strategy is best suited for achieving this.

Finally, no significant differences in the room revenue and profitability performance dimensions were found across the three hotel operating arrangements.

In terms of franchising in the hotel industry, the results indicated that franchised units: (1) were more prevalent in volatile and moderately volatile task environments, (2) more frequently pursued a prospector business strategy, and (3) did not earn average mom revenue or net profits significantly different from either independent or chain units.

**Franchising and Other Operating Arrangements in the Lodging
Industry: A Strategic Comparison**

Franchising can be investigated from at least two different perspectives. One perspective views franchising as a way of doing business; in other words, franchising, compared to other methods of operation, is a standardized business format followed by all firms in a franchise system. Examples include McDonald's, Holiday Inn, ServiceMaster, and H8R Block. Franchising can also be seen as a method of distribution. From this perspective franchising is an alternative to forward vertical integration or lesser degrees of vertical marketing programming such as wholesale sponsored voluntary chains or programmed merchandising agreements. Examples of this latter form of franchising include General Motors with its Chevrolet dealerships, American Oil with its Amoco gas stations, and John Deere with its farm equipment dealerships. These two views of franchising are not mutually exclusive. Franchising as a business format is an alternative form of vertical marketing programming. Similarly, vertically integrated (i.e., corporate ownership) forms of distribution are very often characterized by standardized business formats.

Regardless of which perspective is taken, franchising is often seen as being superior to other methods of doing business (Justis, Taylor, and Nielsen, 1986). Empirical support of this assertion is virtually nonexistent. Accordingly, the overall aim

of this paper is to begin to examine this situation empirically by comparing franchising with other methods of operation. These methods will be compared in terms of the task environments, business strategies, and performance levels characteristic of each.

The paper is organized as follows. First, the industry context for the empirical study is briefly described. Next, preliminary hypotheses, based on a review of the literature, are developed. Third, an empirical study designed to test these hypotheses is then described. Finally, the implications of the results of this study, for both researchers and managers, are discussed.

Conceptual Background

Context

The context for the empirical research undertaken here is the lodging industry. This industry was selected for two chief reasons. First, it represents a substantial segment of the economy, accounting for 1% of the U.S. domestic GNP, employing 1.4 million persons, and generating \$50 billion in sales (Dev, 1988). Second, several alternative operating methods are found in the lodging industry, including chain operations, franchise systems, and independent operations.

Operating Arrangements

In the lodging industry, a number of alternative operating arrangements exist. Among them are independent, franchise, and chain managed operations.

Independent operations are independently owned and managed hotel properties which are not affiliated with any other lodging units.

Hotels operated by an independent businessperson under license from a national organization such as Ramada Inns, Hilton Hotels, or Holiday Corporation are franchise units. Such hotels follow standardized operating and marketing procedures, benefit from national advertising, and are interlinked via a computerized reservations network.

Finally, lodging organizations which operate a number of units under a common name and, typically, under common management are chain-managed. Three different types of chain management in the lodging industry are possible: (1) chain-owned and -managed where the individual hotel property is owned by the corporation and operated by corporate employees; (2) chain-leased and -managed where the corporation leases an individual hotel from private investors and manages that property as if it were corporate-owned; and (3) chain-managed where the corporation simply manages the hotel property, possibly under a different name, for independent investors. (The term "chain" is

often used to refer to both the franchise and corporate (i.e., vertically integrated) operating arrangements. In this study, we use "chain" to refer solely to the corporate form of operation.)

In a sense, these three operating arrangements represent different degrees of vertical integration. Vertical integration refers to the extent to which an organization provides either for its own supply or for its own distribution.

An example of low vertically integrated operations would be an independent hotel buying cleaning supplies from a number of institutional supply distributors, the exact one depending upon which one can offer the lowest prices. On the other hand, high vertically integrated operations would occur when a chain lodging unit obtains its cleaning supplies from the corporate distribution center. Intermediate forms of vertical integration include franchising and other vertical strategic alliances.

Vertical integration offers hoteliers the advantages of economies of scale and increased control; however, these benefits come at the cost of substantial investment. Independent units, on the other hand, are much more flexible in their ability to adapt to changing demand and supply conditions. The trade-off, however, is that these firms do not achieve large economies of scale. Franchised properties fall somewhere in between the other two operating arrangements in terms of the investment required, their adaptability, and their potential for

scale economies (cf., Stern, El-Ansary, and Brown, 1989, p. 302).

Task Environment

The match among a firm's structure and strategy along with its environment determine the organization's level of performance and, hence, its survival (Thompson, 1967; Lenz, 1980). This match results from two forces. On the one hand, the choice of strategy and structure may be determined by the control or power that the organization can exercise over the elements of the environment (e.g., suppliers, customers, etc.). On the other hand, the predominant or immutable nature of environmental influences can dictate the most appropriate strategy and structure for the organization given its capabilities. Thus, the organization reacts to and affects its environment to achieve effective levels of performance.

In this study, our primary concern is with how a hotel's operating arrangement (i.e., one facet of the firm's structure) interacts with the hotel's task environment. Although other elements of organizational structure such as centralization, formalization, and specialization are important, they are beyond the scope of this paper.

In essence, past researchers have empirically examined two dimensions of the environment: dynamism (the rate of change,

variability, or volatility) and complexity (the number of environmental factors impacting the Organization and their diversity). Because previous research has shown that dynamism provided greater explanatory power of environmental uncertainty at the decision-unit level than complexity (Duncan, 1972), this study will focus on environmental dynamism.

Task environment is being defined here as an organization's customers, competitors, and suppliers as well as governmental agencies regulating its activities (Dill, 1958; Duncan, 1972). On the one hand, more variability in the environment is expected to be associated with independent operating arrangements in the hotel industry. As noted earlier, independents are better able to adapt changing demand and supply conditions than are the more vertically integrated operating arrangements (cf., Gultinan, 1974; Harrigan, 1983). This view is seconded by Day and Klein (1987, p. 58) who point out that:

Any cooperative arrangement [e.g. franchising and, in the vertical integration] entails long-term commitments, coordinating mechanisms, and other rigidities that infringe on the firm's ability to adapt to changing conditions.

On the other hand, greater environmental variability may lead hoteliers to more vertically integrated operating arrangements. There are three possible reasons for this.

First, the larger scale of more vertically integrated operations allows hotel managers to devote more, specialized resources toward understanding environmental forces. By virtue of these resources, more vertically integrated operating arrangements are better able to cope with environmental variability than are less vertically integrated ones (cf., Achrol, Reve, and Stern, 1983).

Another reason for expecting higher levels of environmental variability to be associated with more extensive vertical integration is that "By integrating, a firm can restructure dependence so that it becomes more manageable" (Dwyer and Welsh 1985, p. 401). For example, an expanding hotelier, under conditions of tight supply, might purchase a mattress-and-box-spring factory to insure plentiful supply for its new properties.

The theoretical arguments as well as the empirical findings that link environmental uncertainty to the extent of vertical integration are contradictory. Thus, our first hypothesis is somewhat tentatively stated:

Hypothesis I :

a. Vertically integrated operating arrangements (is., chain-managed) are more strongly associated with volatile task environments than are the other operating arrangements.

b. Franchise operating arrangements are more strongly associated with moderate task environments than are the other operating arrangements.

c. Independent operating arrangements are more strongly associated with stable task environments than are the other operating arrangements.

Business Strategies

An organization's strategy refers to the pattern of major minor decisions about its domain (Mintzberg, 1978; Miles and Snow, 1978). Business strategy deals with how an organization competes within a particular product/market segment (Hofer and Schendel, 1978). Because an individual business (hotel) (e.g., the New York Hilton) operates within a particular task environment, the individual property is the unit of analysis in this research.

Although no generally accepted typologies of business-level strategy exist, Walker and Ruekert (1987), Miles and Snow (1978) and Porter (1980) have attempted to develop such a typology.

In Porter's (1980) classification scheme, an SBU can choose among three alternative strategies: (1) "cost leadership" where the SBU strives to maintain a cost advantage over its rivals; (2) "differentiation" where the SBU attempts to create a product or service that is perceived universally as being unique; and

(3) "focus" where an SBU concentrates on a particular market segment or product/service offering.

The Miles and Snow (1978) typology offers a useful framework for classifying the different capabilities displayed by strategic business units within the same industry (Snow and Hrebiniak, 1980). The typology is based on an SBU's orientation toward product/market development and consists of the following four strategy types:

- Defenders: These organizations emphasize efficiency. Their competencies extend to production, applied engineering, and financial control.
- Prospectors: Prospector organizations emphasize innovation through product and market effectiveness. Their competencies relate mainly to product research and development, market research, and basic engineering.
- Analyzers: These organizations Mend aspects of both defenders and prospectors. They imitate the successful product innovations of prospectors (to avoid large investment and risk) and adapt them to efficient production using technology, and market them heavily. Competencies they have extend to production, applied engineering, and marketing.

- Reactors: Reactor organizations have no clearly defined competencies, pattern, or focus. In fact, this strategy is not viable in the long run.

As Walker and Ruekert (1987) note, Porter's (1980) typology is based upon the competitive actions an SBU might take, while the foundation for the Miles and Snow (1978) classification scheme is the intensity of product/market development. Since the latter is better suited to the overall aims of this study, we employ it.

Defenders emphasize efficiency; therefore, it seems likely that they require tight control over their operations. Such control enables scale economies in buying, production, and promotion and reduces any opportunism that might occur because of transaction-specific assets. Such control can best be achieved through vertical integration (cf., Harrigan, 1983; Walker and Ruekert, 1987). Thus, hotels operating as chain units are more likely to follow a defender business strategy.

In contrast, prospectors emphasize innovation in their approach to both products and markets. Flexibility is necessary to successfully implement this business strategy. Thus, the independent operating arrangement in the lodging industry is expected to be most closely associated with the prospector strategy (cf., Harrigan, 1983).

Although franchised hotel units are independently owned, they are a part of a larger organization. Among the primary reasons for franchise systems is their ability to achieve lower costs through economies of scale. In this respect, franchise systems mimic vertically integrated ones. In contrast, however, local ownership of franchised hotel properties offers flexibility for product innovation and market development not possible under the chain operating arrangement. For these reasons, we expect franchised units to follow a hybrid business strategy (i.e., the analyzer strategy).

The only study that has examined differences in business strategy across different levels of vertical integration is that by Dwyer and Oh (1987). They found, in the hardware industry, that independent retailers tended to focus on specific markets and merchandise categories more so than did wholesaler-sponsored voluntary chains or retail cooperatives. Thus, for independents, flexibility in matching products with markets appeared to be critical. Dwyer and Oh (1987) also found that cooperatives tended to stress affiliation through advertising: that **is**, promotional economies were important. In terms of the business strategies examined here, the independents of the Dwyer and Oh (1987) study seemed to follow a prospector strategy while the more vertically integrated hardware retailers appeared to pursue a defender strategy. [*The business strategies examined by Dwyer*

and Oh (1987) were based upon Porter's (1980) typology.

Therefore, the fit between the business strategies employed in this study (i.e., the Miles and Snow (1978) typology) and theirs is somewhat loose.]

These conceptual and empirical arguments are summarized in the second hypothesis which describes the relationship between the hotel's operating arrangement and the business strategy it is likely to follow.

Hypothesis 2:

- a. Independent operating arrangements are more strongly associated with prospector business strategies than are the other operating arrangements.
- b. Franchise arrangements are more strongly associated with analyzer business strategies than are the other operating arrangements.
- c. Vertically integrated arrangements (i.e., chains) are more strongly associated with defender business strategies than are the other operating arrangements.

Performance

The end result of an appropriate match among a hotel's particular task environment, its business strategy, and its operating arrangement should be reflected in greater organization performance. After all, improving performance is

the head of strategic management (Venkatraman and Ramanujam, 1986).

Performance may be evaluated on at least three key dimensions: efficiency, effectiveness, and adaptiveness (Ruekert, Walker, and Roering, 1985). Efficiency refers to how well the organization utilizes scarce resources in generating its outputs. For example, labor productivity, inventory turnover, and return on investment measure an organization's efficiency with respect to its labor, materials, and capital inputs, respectively. Effectiveness refers to how well the organization satisfies its various key constituencies. These constituencies can include customers, labor, management, local communities, and selected special interest groups. Finally, adaptiveness "... reflects the ability of the organization to adapt to changes in its environment" (Ruekert, Walker, and Roering, 1985, p. 15).

In this research, we limit our study of hotel performance to two key facets of financial performance: revenues and profits. Revenue per room indicates how intensively the hotel utilizes an important fixed asset, its rooms. Net income as a percent of sales, on the other hand, reflects how well the firm converts sales revenues into profits.

Chain hotels' units are expected to achieve higher revenues per room than are hotels operating under different arrangements.

There are two reasons for this. First is the importance of generating enough revenues to achieve economies of scale. Second, corporate overhead allocations and/or management fees are based upon gross revenues; thus, chain units are under pressure to earn higher room revenues than are units operated by the other methods.

As posited above, independent hotels are more likely to pursue a prospector strategy than are the others. To implement this strategy successfully, enough profits must be earned to fund the product and market development indicative of a prospector strategy. Therefore, independents are expected to earn higher returns on sales than are franchised or chain hotel units.

Franchised units utilize a hybrid business strategy and are vertically integrated somewhere between chain hotels and independent hotels. In addition, the fraction of their revenues claimed by other parties (i.e. the franchisor) is less than the chains, yet more than the independents. Accordingly, their revenues and profits are expected to fall between those for the two other operating arrangements.

Hypothesis 3, describing the link between a hotel's operating arrangement and its levels of performance, summarizes these arguments.

Hypothesis 3:

- a. Hotels which are chain units will generate higher revenues per room but earn a lower profit on sales than will those which are franchised or independent.
- b. Franchised hotels will generate higher revenues per room but will earn a lower profit on sales than will independents. Franchised hotels will also generate lower revenues per room but will earn a higher profit on sales than will chain units.
- c. Independent hotels will generate lower revenues per room but will earn a higher profit on sales than will either franchised or chain units.

Research Design

To test these hypotheses, a cross-sectional field study of general managers of lodging establishments was designed. The following sections describe the sample and the instruments used to measure the constructs of interest.

Sample

The hotels invited to participate in this study were selected from a national database of 25,711 lodging establishments (i.e., units or properties) in the United States maintained by the public accounting firm of Laventhol and Horwath. Of the total database, 2,000 units with 150 rooms or more were randomly selected to be included in the study.

Following extensive pre-testing by knowledgeable experts and practicing hotel managers (to insure the content validity of the measures used in this study), the questionnaire was sent to general managers of the sampled establishments. One week later, a reminder postcard was sent to stimulate response. Finally, follow-up telephone calls were made to those respondents that had provided all but the information on performance. One hundred seventy-six usable questionnaires were obtained. This 8.8% response rate compares favorably to that obtained by other researchers surveying lodging industry executives (cf., Schaffer, 1986; Ashley and Olsen, 1986; Evans and Dev, 1987; Laventhol and Horwath, 1987).

General characteristics of the responding organizations were examined to determine the effects of response bias. Their diversity in terms of their geographic region, size, affiliation with national lodging organizations, location within a geographic market, operating arrangement, extent of perceived environmental uncertainty, selection of business strategy, and financial performance prevented any one type of lodging establishment to dominate the sample; thus, the degree of generalizability from this sample is believed to be quite high (Miller, Kets de Vries, and Toulouse, 1982).

Instrumentation and Scaling

To measure the hotel's operating arrangement, each general manager was asked to indicate whether or not his property was: (1) managed by a chain, (2) a franchised hotel, or (3) an independently operated lodging facility.

The questionnaire used to measure perceived environmental volatility was adapted from the one used by Miles and Snow (1978, p. 200) in their study of the food processing and electronics industries. Specifically, items were adapted to reflect the task environment factors faced by the service industry in general and the lodging industry in particular (Sasser, Olsen, and Wycoff, 1978).

General managers' perceptions of the variability or volatility in the environments facing their hotels were obtained on 6-point semantic differentials ranging from stable to volatile. These differentials were based on 20 items descriptive of the components of an organization's task environment (i.e., suppliers, competitors, customers, and regulatory groups). See Table 1 for the complete list of the task environment components used in this study.

The general managers' responses to these 20 items were then averaged to obtain the perceived environmental volatility score. Note that larger numbers imply more volatility or variability in the hotel's task environment. These scores were then split into

their upper quartile, middle half, and lower quartile to reflect volatile task environments, moderately volatile or moderately stable task environments, or stable task environments, respectively. Each hotel's score was then placed in the appropriate category. Thus, each hotel could be described as operating in a volatile, moderate, or stable task environment.

No universally accepted operational measures for the business strategy construct exist. However, Snow and Hrebiniak (1980) and Schaffer (1986) have developed and empirically tested operationalizations of the Miles and Snow (1978) typology of business strategy. The Snow and Hrebiniak (1980) self-typing operationalization was used in this study. From four different business strategy descriptions, general managers were asked to pick the one which most closely characterized their hotel. Each one of these corresponds to one of the four Miles and Snow (1978) strategy types: Prospector, Defender, Analyzer, and Reactor. These four strategy descriptors appear in Table 2.

Both sales and profitability measures of hotel financial performance were included in this study.

In using financial information for the comparative analysis of different hotels, there are two basic differences among operations that prevent utilizing absolute figures such as sales and profits on their own. One is the difference in the number of rooms hotels have. A large property may generate high dollar

revenues simply because of its size. A second difference is in the rack rate (published room tariff) of different lodging operations. Thus, effective measures of financial performance must adjust for these two basic differences.

One measure that enables comparison of the financial performance of different lodging units, in spite of differences in the number of rooms and rack rate, is the IBFC ratio. The IBFC ratio is a measure of profitability and is calculated as:

$$\text{IBFC Ratio} = \frac{\text{Income Before Fixed Charges}}{\text{Total Sales}}$$

Income before fixed charges takes into account the resource allocation expense items under the control of a typical hotel manager. In the typical income statement, all items appearing prior to the income before fixed charges are, as the definition suggests, operating expenses. Thus, IBFC is not contaminated by the variations due to the unique financial structure of the hotel (interest expense) or the nature of the property ownership (owned, leased, etc.).

Another measure of hotel performance is a revenue-based one which also takes into account differences in number of rooms. This measure—Sales Per Available Room (SPAR) per day—is calculated as follows:

$$\text{SPAR} = \frac{\text{Total Sales}}{\text{Rooms Available Days Hotel Was Open}}$$

The raw data used to compute the IBFC and SPAR ratios were gathered in the survey and represented financial performance for 1987.

Validity and Reliability Issues

Coleman and Gaetan (1985) have demonstrated the internal consistency of the perceived environmental volatility measure employed in this study; furthermore, they have reported significant Pearson product-moment correlations ($p < 0.05$) among all six major components of the instrument (e.g., supplier, competitor, and customer activities). In this study, coefficient alpha, a measure of internal consistency, was computed to be 0.84, which surpasses Nunnally's (1978) suggested guideline. Thus, the perceived environmental volatility measure used here appears to be reliable.

Previous researchers, notably Snow and Hrebiniak (1980) and Ginn and McDaniel (1987), have provided evidence of the validity of the self-type business strategy questionnaire used in this study. Thus, the use of this operationalization in this study appears justified.

Given the relative objectivity of the measures of operating arrangements and of financial performance, validity questions center on their content validity. The operationalizations of these variables are universally accepted and uniformly used

within the lodging industry. In addition, they are highly relevant in relation to the other variables examined in this study. For these reasons, the operating arrangements and financial performance measures appear to be valid operationalizations of their respective constructs.

Results

Hypothesis 1

The first hypothesis specified the relationship between the three different hotel operating arrangements and the volatility or variability of the hotel's task environment. Chains were posited to be best suited for volatile task environments, franchised units for moderately stable or, conversely, moderately volatile environments, and independents for stable environments.

To test this hypothesis, a cross-tabulation of operating arrangement by task environment variability was constructed (see Table 3). The chi-square statistic tests the null hypothesis that there are no differences in task environment variability across the three operating arrangements. A significant ($p \leq .05$) chi-square statistic indicates that task environment variability does differ across the three different operating arrangements. Contrary to Hypothesis 1, however, an inspection of Table 3 reveals that both chain and independent units appear most frequently in moderate and stable task environments while

franchised units are most prevalent in moderate and volatile task environments. Therefore, Hypothesis 1 was rejected and it appeared as though our tentativeness in specifying this hypothesis was justified.

Hypothesis 2

This hypothesis specified the expected variations in business strategies followed by hotels operating under the three different vertical arrangements. Specifically, independents were expected to follow a prospector strategy, franchises an analyzer strategy, and chains a defender strategy. This hypothesis was also tested using cross-tabulations; Table 4 presents the empirical results.

The chi-square statistic is significant at the 0.05 level and indicates that different business strategies are associated with different hotel operating arrangements. An examination of the frequencies in Table 4, however, indicates a pattern contrary to what was expected. Chains and franchised units more frequently pursued the prospector strategy than they did the other ones. Independents more frequently followed the defender strategy. Thus, Hypothesis 2 must be rejected.

Hypothesis 3

The linkages between the extent of vertical integration (i.e., the three different operating arrangements) in the lodging industry and the two hotel performance measures were

specified in the third hypothesis. Chain hotels were expected to generate higher revenues per room (SPAR) and lower net profit ratios (IBFC) than were either independent or franchised units. Independents, on the other hand, were believed to be more profitable but earn lower room revenues than were the other two. Franchised hotels were expected to fall in between the chains and the independents in terms of both room revenues and profits.

Analysis of variance was used to test the null hypothesis of no statistically significant differences in hotel performance across the three operating arrangements (Table5). For both the room revenue (SPAR) and net profitability ratio (IBFC), the pattern of means supports the expected relationships between operating arrangements and performance. However, these differences are not statistically significant at the 0.10 level. Therefore, Hypothesis 3 must also be rejected.

In summary, all three hypotheses developed in this study were rejected. The following section explores some reasons for this result.

Discussion

Contrary to our hypothesis, chain hotel units were more prevalent in stable and moderately stable environments than they were in volatile ones. A similar result was found for the independent units. Franchised units, however, were more prevalent in moderate and volatile environments. The results

seem to demonstrate the superiority of franchise systems in handling environmental variability.

Although they were not explicitly tested, a number of plausible reasons may be advanced for this. First, as compared to corporate chains, franchise systems provide greater flexibility to respond to environmental fluctuations at the local level. Second, as compared to independent units, franchise systems are better able to cope with environmental variability because they can devote specific resources to absorb the variability facing individual units. Third, under conditions of environmental variability, attributing hotel-unit performance to that variability or to managerial effort is difficult for corporate chains. Managers may tend to over- or understate the impact of either their effort or the environment to make themselves look good; in other words, they may behave opportunistically. To counter this performance-monitoring problem, the organizations use franchising as a means of gaining control (Norton, 1988). In return for promises of high revenues and profits and for the unstated sharing of environmental risks, franchisees agree to operate their units "by the book." Thus, under such conditions, profit incentives motivate the franchisee to perform at higher levels than would company managers.

On balance, franchise systems appear to have the advantages of both independents and corporate chains in dealing with

environmental variability. This may explain the empirical results obtained in this study.

Contrary to our expectations, both chain and franchised hotel units predominantly followed the prospector strategy while the independents were more closely associated with the defender strategy. A plausible reason for this is the importance chains and franchises place on developing new markets and new products to achieve economies of scale. Evidently, in the lodging industry, the prospector strategy is best suited for achieving this. Future research should examine the relationship between the extent of vertical integration and the business strategy pursued much closer. For example, controlling for the degree of environmental volatility may shed more light upon this relationship (cf., Harrigan, 1983, p. 40).

Finally, no significant differences in room revenue and profitability across the three hotel operating arrangements were found. Additional research is needed to determine exactly why this is so; however, one plausible reason might be advanced. Critical to an organization's performance, as noted above, is the match of its strategy and structure to its task environment. Thus, the match between the degree of environmental variability, the business strategy pursued, and the operating arrangement employed should be an important determinant of a hotel's performance. Accordingly, the interaction among environmental

volatility, business strategy, and operating arrangement and its effect upon performance must be examined in future studies.

Limitations

As with any study, this one has a number of features which limit the generalizability of the empirical findings. Future researchers are urged to overcome these limitations. First, the sample was composed of larger hotels (i.e. those properties with over 150 rooms); smaller properties should be included in subsequent studies. Relatedly, future research should control for organizational size. In this study, chains tended to be large (i.e., over 260 rooms per unit) while franchised and independent operations tended to be moderately sized (i.e., between 160 and 260 rooms per unit). Second, only two dimensions of performance-net profit margin and revenue per room-were examined. Other dimensions of performance (e.g., effectiveness and adaptability) remain to be investigated. Third, the self-typing measure of business strategy has a number of weaknesses (McDaniel and Kolari, 1987). Future research is needed to overcome those limitations. Fourth, richer typologies of business strategy, such as the hybrid of the Miles and Snow (1978) and Porter (1980) classification schemes developed by Walker and Ruekert (1987), are needed. Fifth, other facets of environmental uncertainty (e.g., heterogeneity/homogeneity) should be included in future studies. And, finally, richer

measures of the degree of vertical integration are desperately needed.

Summary and Conclusions

The objective of this study was to compare franchising with other methods of operation in the lodging industry. The dimensions used for this comparison were: (1) the degree of task environment variability, (2) the business strategy followed, and (3) the level of performance achieved. The individual hotel property was used as the unit of analysis in this study. Data to make these comparisons were obtained from a mail survey of general managers of those properties.

In spite of the limitations noted above, this study has added much to our understanding of: (1) differences across different levels of vertical integration and (2) franchising in the lodging industry.

In terms of differences across the three operating arrangements (i.e., different levels of vertical integration), the following results were obtained. Hotels operated as either chain-managed or independent units were more prevalent in stable or moderately stable environments while franchised units occurred most often in moderately stable or volatile environments. While independents most often pursued the defender business strategy, chain-managed properties and franchised

properties followed the prospector strategy. Finally, no significant differences across the three different operating arrangements were found for room revenues or for net profits.

In terms of franchising in the hotel industry, the results indicated that franchised units: (1) were more prevalent in volatile and moderately volatile task environments, (2) more frequently pursued a prospector business strategy, and (3) did not earn average room revenue or net profits significantly different from either independent or chain units.

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Table 1. Components of a Lodging Facility's Task Environment.

Suppliers of Food, Beverage, and Operating Supplies

Prices charged
Product quality standards
Product/service specifications
Introduction of new products

Competitors' Actions

Supply of rooms
Rates charged
Renovation and refurbishment
New services/facilities offered

Customers' Demand

For your services
For new facilities/services

The Financial/Capital Market

Interest rates
Availability of credit

The Labor Market

Wage and salary rates
Availability of employees

Government Regulatory Agencies (i.e., changes in laws or policies)

Regarding rates you can charge
Regarding room, food or beverage quality
Regarding provision of your services
Affecting personnel/labor decisions
Affecting sales and marketing
Affecting accounting/bookkeeping

Table 2. The Miles and Snow (1980) Business Strategy Typology
Adapted to the Lodging Industry

Defender

This type of hotel attempts to maintain a secure niche in a relatively stable customer market segment. The hotel tends to offer a more limited range of services than its competitors, and it tries to protect its position by offering quality at lower prices. Often this type of hotel is not at the forefront of developments in the market-it tends to ignore market changes that have no direct influence on current areas of operation and concentrates instead on doing the best job possible in a limited market segment.

Prospector

This type of hotel typically serves a broad customer/market base that undergoes periodic redefinition. The hotel values being "first in" in new facilities/services, even if not all of these efforts prove to be highly profitable. The hotel responds rapidly to early signals concerning areas of opportunity, and these responses often lead to a new round of competitive actions. However, this hotel may not maintain strength in all of the market segments it serves.

Analyzer

This type of hotel attempts to maintain a stable and limited line of services, while at the same time moving out quickly to follow a carefully selected set of the more promising new developments in the market. The hotel is seldom "first in" with new facilities or services. However, by carefully monitoring the actions of competitors in areas compatible with its stable customer/service base, the hotel can frequently be "second in" with a more cost-efficient facility or service.

Reactor

This hotel does not appear to have a consistent customer/market orientation. The hotel is usually not as aggressive in maintaining established markets and

services as some of its competitors, nor is it willing to take as many risks as the competitions. Rather, the hotel responds in those areas where it is forced to by pressure from customers, suppliers, competitors, or government regulation.

Table 3. Perceived Environmental Volatility by Hotel Operating Arrangements.

Operating Arrangement	Frequency/Row Percentage			Total
	Stable Quartile	Moderate Half	Volatile Quartile	
Chain Units	15 34.09	25 56.82	4 9.09	44 25.00
Franchised Unit	24 24.24	42 42.42	33 33.33	99 56.25
Independents	13 39.39	12 6.36	8 24.24	33 18.75
Total	52 29.55	79 44.89	45 25.57	176 100.0

Table 4. Business Strategy by Hotel Operating Arrangements.

Operating Arrangement	Frequency/Row Percentage				Total
	Reactor	Analyzer	Prospector	Defender	
Chain Units	2 2.27	15 34.09	25 54.55	4 9.09	44 25.00
Franchised Unit	4 4.04	23 23.23	51 51.52	21 21.21	99 56.25
Independents	1 3.03	6 18.18	11 33.33	15 15.15	33 18.75
Total	6 3.41	44 25.00	86 48.86	40 22.73	176 100.0

Table 5. Analysis of Variance of Hotel Performance Measures.

Operating Arrangement	n	Mean Value	
		IBFC	SPAR
Independents	33	0.393	66.09
Franchised Units	99	0.347	64.02
Chain Units	44	0.281	84.93
F-ratio		1.69	1.99
df		2, 173	2, 173