



Routledge Research in Hospitality

VERTICAL DISINTEGRATION IN THE CORPORATE HOTEL INDUSTRY

THE END OF BUSINESS AS USUAL

Angela Roper



Vertical Disintegration in the Corporate Hotel Industry

Whilst the original products, services and core technologies of the global hotel industry have remained much the same, for the largest hotel chains, in particular, the industry has undergone, and continues to undergo, a structural transformation.

This book evaluates the ways that vertical disintegration has occurred and the causes of such an industry evolution, while providing a unique insight into the resulting new competitive landscape. Whilst underpinned by academic literature, it includes first-hand accounts from the most eminent senior executives from firms participating in and around the industry. It provides an in-depth perspective of a contemporary industrial phenomenon in a 'golden era' of growth and development, and it makes observations as to the profitable way forward for the corporate hotel industry.

If you want to know what is really going on in the international hotel industry, this is the book for you. Nowhere else will you get first-hand accounts from many of the industry's leading players. For those working, advising and considering investing in the sector, it is important to understand the changes in the industrial dynamics now, and for future strategies. This book is also a 'must read' for students, graduates and researchers seeking a critical and real-life evaluation of the contemporary hotel industry.

Angela Roper has been the Chair and Director of the International Centre for Hotel and Resort Management (ICHARM), University of West London, UK, which has strong links with the international hotel industry. She previously held senior academic positions at the University of Surrey, UK and Oxford Brookes University, UK. Having begun her academic career at the University of Huddersfield, she also worked as an Analyst for the Bank of Scotland Group. Angela has been researching the development of hotel chains for some 30 years.

Routledge Research in Hospitality

Published Titles

- 1 Vertical Disintegration in the Corporate Hotel Industry**
The End of Business as Usual
Angela Roper

Vertical Disintegration in the Corporate Hotel Industry

The End of Business as Usual

Angela Roper

First published 2018
by Routledge
2 Park Square, Milton Park, Abingdon, Oxon OX14 4RN

and by Routledge
711 Third Avenue, New York, NY 10017

Routledge is an imprint of the Taylor & Francis Group, an informa business

© 2018 Angela Roper

The right of Angela Roper to be identified as author of this work has been asserted by her in accordance with sections 77 and 78 of the Copyright, Designs and Patents Act 1988.

All rights reserved. No part of this book may be reprinted or reproduced or utilised in any form or by any electronic, mechanical, or other means, now known or hereafter invented, including photocopying and recording, or in any information storage or retrieval system, without permission in writing from the publishers.

Trademark notice: Product or corporate names may be trademarks or registered trademarks, and are used only for identification and explanation without intent to infringe.

British Library Cataloguing-in-Publication Data

A catalogue record for this book is available from the British Library

Library of Congress Cataloging-in-Publication Data

A catalog record for this book has been requested

ISBN: 978-1-138-64108-2 (hbk)

ISBN: 978-1-315-63070-0 (ebk)

Typeset in Times New Roman
by Apex CoVantage, LLC

**This book is dedicated to my wonderful daughter,
Ilanthe, who is everything to me.**



Taylor & Francis

Taylor & Francis Group

<http://taylorandfrancis.com>

Contents

<i>Illustrations</i>	ix
<i>Foreword</i>	xi
<i>Acknowledgements</i>	xiii
1 Introduction	1
2 Episodes of vertical disintegration	13
3 Hotels as a property asset class	27
4 The role of professional service firms	49
5 The provision of hotel management services	63
6 Becoming brand owners and managers	83
7 Separation of brand from management: capabilities as franchisors	105
8 Competition in distribution channels	125
9 Consolidation and substitutes	139
10 Conclusions	165
<i>Appendix A</i>	173
<i>Index</i>	177



Taylor & Francis

Taylor & Francis Group

<http://taylorandfrancis.com>

Illustrations

Figure

2.1	The disintegration of the Corporate Hotel Industry	23
-----	--	----

Tables

1.1	Demand sources 2016	3
1.2	10 largest hotel chains worldwide by number of rooms, 2015	4
1.3	Evolution of hotel chains, 1900–2017	6
1.4	Three different categories of hotel chains	8
1.5	List of Respondents	9
2.1	Global Major Hotel Chains' asset-light portfolios	17
3.1	Breakdown of the different organisation types reflected in the CBRE sample: European Investor Intentions Survey 2017	29
3.2	Perspectives on maximising hotel investment	43
6.1	Brand acquisitions by Global Major Hotel Chains, 1995–2015	88
6.2	Hotel chains' organic hotel brands	90
6.3	List of brands in Global Major Hotel Chains	94
7.1	What makes hotel franchise chains best in class?	112
7.2	Top 5 Brands in 2016	113
9.1	The growth of the Global Major Hotel Chains, 1995–2015	140
9.2	Chinese outward foreign direct investment in hotel chain portfolios	149
9.3	Selection of studies providing statistical analyses of the impact of Airbnb on hotels	156
9.4	Shattering the myths of the sharing economy	158



Taylor & Francis

Taylor & Francis Group

<http://taylorandfrancis.com>

Foreword

I have been involved with hotels for well over 50 years, having begun my career in hotel kitchens in Switzerland. I have been involved as an owner and operator of hotels as well as both a franchisor and franchisee on a global basis. Over the decades, I have seen many trends come and go and at an ever-increasing speed, although the fundamental precepts underpinning the lodging industry have remained relatively constant.

I am extremely pleased to be asked to write a foreword for this important book and to have taken part in its formation. It gives a unique insight not only into current developments but also into the underpinning motives for these. It is centred upon the corporate lodging industry, that part of the industry comprising the major hotel chains who are at the forefront of innovation and change influencing the entire hotel world.

Hotels are an important constituent of the tourism industry, the fifth largest industry globally. The industry is set to rocket in the next 20 years, responding to the rapidly evolving tastes and technology-led consumption patterns of contemporary consumers.

The book is an invaluable resource for those executives in and around the corporate hotel industry. It is an essential read for those having invested, or considering investing in the lodging industry in any of the many capacities that comprise this dynamic, but capital intensive, industry. It also provides a unique strategic insight for those teaching, studying and researching hotel chains. For those about to graduate in the fields of tourism and hospitality management, it facilitates the necessary knowledge and understanding of ‘the business of hotels.’

Given the global nature of tourism and the lodging industry in particular, this book has international appeal as the major hotel chains, owners and investors are not constrained by geographic boundaries.

The uniqueness of Professor Roper’s thorough and thoughtful book is that it provides a contemporary evaluation of the corporate hotel industry. Including quotations from first hand interviews and conversations with over 30 senior executives from hotel brands, operators and owners, hotel management companies, hotel owners and investors, consultants, lawyers, and bankers, it is distinctive in that it combines real-world and academic perspectives. It provides a rare understanding of the underpinning business motivations and needed returns of the corporate hotel business.

Laurence Geller, CBE

Mr Geller is currently founder and Chairman of Geller Capital Partners, a real estate investment organisation with particular focus on the lodging industry in North America and the UK and dementia care residences in London. He is also the Chancellor of the University of West London and founded the International Centre for Hotel and Resort Management at the university. He was previously founder, President and CEO of Strategic Hotels & Resorts and held senior executive positions at Hyatt Hotels Corporation, Holiday Inns and Grand Metropolitan Hotels.

Acknowledgements

This book has been a labour of love.

After 30 years as an academic and analyst researching hotel chains, it has been both a privilege and challenge to consolidate all my knowledge and experience into one book, as well as interpret contemporary trends affecting the structural evolution of the corporate hotel industry. Interviews with 32 respondents resulted in more than 50 hours of interview data, and I would like to offer my gratitude to all of these senior executives, in and around the industry, for providing me with their time and very insightful comments.

I would like to acknowledge the help and support of the donors of the International Centre for Hotel and Resort Management at the University of West London. These include InterContinental Hotels Group, Geller Capital Partners, Hilton, the Lord Forte Foundation and the Westmont Hospitality Group. Without their support, I would not have had the time or resources to carry out the independent research and writing of this book.

Thank you also to all my academic colleagues and friends – there are too many to mention – from the four Universities that I have had the pleasure to work at. These are the University of Huddersfield, Oxford Brookes University, the University of Surrey and the University of West London. My doctoral students over the years have inspired me to write this book and some of their work is included given its relevant contribution to our understanding of hotel chains.

Finally, I would like to thank all my family and friends for putting up with my unsociable behaviour over the last few months. I hope to make it up to them soon. Most importantly, thank you to Peter for making me reflect on the commercial implications of my arguments and for all his loving support.

Professor Angela Jane Roper, April 2017



Taylor & Francis

Taylor & Francis Group

<http://taylorandfrancis.com>

1 Introduction

Introduction

The hotel industry has experienced a ‘golden era’ of growth and development. Major hotel chains are undergoing unprecedented growth due to voracious demand, currently having the largest development pipelines (numbers of hotels in planning and under construction, but not yet open) in their histories. Whereas previously it was only a few luxury hotel brands – such as Hilton and InterContinental – which were seen internationally in capital and gateway cities, the explosion of the economy and mid-market segments has led to some brands, such as Holiday Inn, dominating globally. We have also just witnessed the biggest, and arguably the most important, hotel chain takeover in the industry so far. In September 2016, Marriott International’s acquisition of Starwood Hotels & Resorts Worldwide for over \$12 billion, created the world’s largest chain comprising 30 hotel brands and over one million hotel rooms.

At the same time, the leading large hotel chains are experiencing challenging times. They are opting to get out of hotel ownership and are being pushed to relinquish the operation of hotels. Added to this, in the booking process, hotel chains are surrendering some of their direct access to consumers to online travel agencies. They are also losing their supply dominance to alternative accommodation sectors, such as hostels, short-term home rentals, timeshares and cruises. For example, there are three million listings on the Airbnb platform and this is on the increase daily. The U.S. hotel market, as the largest and most concentrated in the hands of hotel chains, has enjoyed a period of robust growth and record-breaking performance over the last six years, but the most recent trends point to a shift in the cycle.

As a competitive response, what is being witnessed are hotel chains giving up parts of their value-chain, enabling new intermediate markets to emerge which has divided a previously integrated production/service process and facilitated the entry of sets of specialised firms. In terms of industry structure, the corporate hotel industry (that part of the industry which is organised and comprises hotel chains) is becoming vertically disintegrated (Jacobides, 2005). Disintegration can be observed in a significant number of industries, as producers recognize that they cannot themselves maintain cutting-edge technology and practices in every field required for the success of their products and services (Gilson, Sabel and Scott, 2009).

2 Introduction

Whilst the original products, services and core technologies of the global hotel industry have remained much the same, for the largest hotel chains, in particular, the industry has undergone, and continues to undergo a structural transformation. For those working, advising and looking to invest in the sector, the changes in the industrial dynamics of the industry are important to know and understand now, and for the future, in terms of setting appropriate strategies. This book evaluates in what way disintegration has occurred and the causes of such an industry evolution, and it provides a unique insight into the resulting new competitive landscape. Whilst underpinned by academic literature, it also includes first-hand accounts from the most eminent senior executives from firms participating in and around the industry.

Setting the scene

Tourism is the fifth biggest industry globally. The UNWTO estimated that there were more than 1.18 billion international tourist arrivals in 2015, a rise of 4.4 per cent on 2014. International travel is becoming increasingly viable for more people globally. Other macro factors favourable to the hotel industry are the growth of an aging population, the rise in Millennials travelling, as well as long-term macro-economic trends such as GDP growth, increasing disposable income and a rising middle class.

The global demand for hotels is currently insatiable; there are new hotel openings every day.

Demand for hotels

Whereas the demand for hotels may be voracious, it varies on a country-to-country basis contingent upon macro and micro-economic factors, which in turn determine different sources of demand.

The most straightforward way of identifying and understanding different sources of hotel demand are to categorise them as either business or leisure demand, and as originating domestically or internationally. On a global basis, each country market is characterised by different patterns in these demand sources, contingent upon the prevailing economic structure. Economic conditions likewise produce hotel chains of different size and structure and with varying degrees of prospects for growth.

Table 1.1 illustrates demand sources for five countries. The greatest proportion of hotel demand from domestic business and leisure travellers is generated in the U.S. and UK, as they have the most advanced microeconomic structures. Those countries with less advanced microeconomic structures have a greater dependency upon international hotel demand, from both business and leisure travellers.

These sources of demand are important to understand in the corporate hotel industry, as the biggest determinants of customer choice are thought to be the purpose of the use of a hotel as well as the occasion of use. These factors are continually being researched so that hotel chains meet the requirements of the ever-changing consumer world.

Table 1.1 Demand sources 2016

<i>Hotel room nights sold</i>	<i>Domestic business demand (millions)</i>	<i>Domestic leisure demand (millions)</i>	<i>Foreign business demand (millions)</i>	<i>Foreign leisure demand (millions)</i>	<i>Total hotel demand (millions)</i>
China	49 (12%)	29 (7%)	57 (14%)	273 (67%)	408 (100%)
France	21 (20%)	12 (11.5%)	11 (10.5%)	60 (58%)	104 (100%)
Germany	23 (23%)	19 (18.5%)	21 (20.5%)	38 (38%)	101 (100%)
UK	40 (34%)	17 (14.5%)	17 (14.5%)	43 (37%)	117 (100%)
USA	418 (5%)	500 (42%)	54 (5%)	215 (18%)	1187 (100%)

Source: Data refers to the number of hotel room nights sold and is adapted from National Statistics, UNWTO and Otus Analytics sources.

Hotel supply

The global hotel industry comprises an estimated 187,000 hotels and offers 17.5 million guest rooms (hotels are defined as properties with 20 rooms or more in the U.S. only and 10 rooms and more throughout the rest of the world) (STR Global). It generates revenues of \$550 billion (Hospitality, 2015). Independent hotels still dominate the accommodation market, but they are suffering longer-term decline, having to operate under ever-higher standards and perform as digital entrepreneurs. It is branded hotels which have therefore experienced the most growth, now accounting for almost a third of the global market and rising.

In line with many other industries, chains are now one of the dominant forms of organisation in the hotel industry; a single chain often having hundreds, even thousands, of units operating under a common trademark in diverse locations. Table 1.2 below illustrates the size of the ten largest hotel chains worldwide.

The developed hotel markets of Europe and North America remain the centre of the hotel universe in terms of supply and demand.

Vertical disintegration

Whilst hotel guests have experienced a profound upward improvement in the facilities of chain hotels over the past twenty years or so, what has probably gone largely un-noticed is the fact that the ownership, operations and brand trademarks of hotels have become separated and are often times in the hands of very different organisations. The Economist (2009) very aptly describes the current business model of the corporate hotel industry:

YOU book a room on the website of a famous international hotel chain. As you arrive to check in, its reassuring brand name is above the door. Its logo

4 Introduction

Table 1.2 10 largest hotel chains worldwide by number of rooms, 2015

Ranking	Hotel Chain	Origin	Numbers of hotel and rooms	
			Hotels	Rooms
1	Marriott International (including Starwood Hotels & Resorts)	USA	5,456	1,071,096
2	Hilton Worldwide	USA	5,456	737,922
3	InterContinental Hotels Group	UK	4,480	726,876
4	Wyndham Hotel Group	USA	4,963	671,900
5	Shanghai Jinjiang International	CHINA	7,760	640,000
6	Choice	USA	6,000	504,357
7	ACCOR	FRANCE	6,379	500,366
8	Best Western	USA	3,815	303,768
9	Home Inns	CHINA	3,903	311,608
10	Carlson Rezidor Hotel Group	USA	1,092	172,234

Source: Companies reported data as of 30 September 2015. www.hotelnewsnow.com/Articles/28560/The-10-largest-hotel-companies-by-room-count

is everywhere: on the staff uniforms, the stationery, the carpets. But the hotel is owned by someone else – often an individual or an investment fund – who has taken out a franchise on the brand. The owner may also be delegating the running of the hotel, either to the company that owns the brand or to another management firm altogether. The bricks-and-mortar may be leased from a property firm. In some cases, yet another company may be supplying most of the staff, and an outside caterer may run the restaurants. Welcome to the virtual hotel

(The Economist, 2009)

The picture painted above of the ‘virtual hotel’ is perhaps the extreme scenario, but what it does illustrate is how overtime hotel chains have given up parts of the value-chain. Previously, as well as designing and owning brands, they undertook the marketing, sales and distribution of hotels; owned or leased hotel buildings (with internally generated capital or loaned finance); managed hotels; oversaw day-to-day operations; employed all hotel staff; and owned or maintained strong links with suppliers. They were involved in all of the structured activities which taken together lead to the construction of a hotel experience for the consumer. With the exception of a few chains, this is no longer the case. Richard Solomons, CEO of IHG, sees the positioning of his company, the third largest hotel chain in the world, as follows:

Focus on what you’re good at and then outsource things you’re not, and, frankly, whether it’s the cleaning of the hotel room or whether it’s running a payroll or whether it’s owning the real estate, you don’t have to do it yourself. Interestingly, in some respects I think at IHG, we’re an ‘outsourcee’ in the sense that a hotel owner outsources to us revenue generation, good design,

and marketing. If it's a management contract the owner outsources operations as well. Effectively that's somewhat how we think about ourselves.

Relinquishing parts of the value chain has enabled new businesses to emerge which have divided a previously highly integrated production/service process into many profitable sub business units. Specialist firms have entered the marketplace, resulting in an industry which is becoming increasingly vertically disintegrated with various opportunities for service providers and business transformers. It is contended that for the corporate hotel industry, there have been profound implications of this structural disintegration: the number and nature of firms that participate in the industry has increased; entry into the industry has fallen in certain parts of the value chain; and the nature of competition has greatly altered (Roper, 2015). What have been the main drivers or motivations for this changed industry structure, and what might the future hold in terms of industrial evolution?

Before introducing the academic argument which underpins the book, it is useful to first provide a brief history of hotel chains and their internationalisation. The focus is more upon the international growth of chains because it is this which really sets them apart as big businesses. This is especially the case because, globally, the sector is still a fragmented industry dominated by domestic independent owner/operators who continue in business very much still as a 'way of life.'

A brief history of hotel chains and their internationalisation

Table 1.3 illustrates the evolution of hotel chains from 1900 until the present day, providing some overall observations of how they have developed overtime (for a more in depth treatment see Slattery, 2012).

The classic formation of a hotel portfolio is where an entrepreneur starts with one owner/operated hotel to which others are added as capital is made available and entrepreneurial drive to grow takes hold. Although early chain pioneers such as Conrad Hilton undertook hotel ventures in the early twentieth century, it wasn't until after WWII that hotel chains really began to internationalise. Hotel chains were the initial service businesses to expand overseas and played an important part in providing accommodation for pioneering international travellers, thus implementing a 'following consumers abroad' strategy. Pan American Airways developed the foremost modern international hotel chain in 1946, with its Inter-Continental Hotels chain (Potter, 1996), subsequently developing upmarket hotels in key global and commercial transport hubs. However, it wasn't until the 1960s that other airlines also followed this same vertically integrated strategy. Quek (2007: 217) provides some examples:

The acquisition of HHI by TWA in 1967, the merger of United Airlines and the Westin hotel group (previously known as Western International Hotels) in 1970, and the creation of Le Meridien Hotels by Air France in 1972 and Nikko hotel group by Japan Airlines in 1970, further illuminate this motivation [to follow customers abroad]. Underpinning the political and airline