

China an Investment 'Heaven' for Multinational Hotel Groups

Thirty years after the Chinese government enacted its open-door policy China has become a 'heaven' for multinational hotel groups, argue the SHTM's Basak Denizci Guillet, Hanqin Zhang and Wendy Gao. In a recently published paper, the researchers analyse industry publications and related information on investments in China proposed by multinational hotel groups. They identify the issues related to expansion, the most prominent development trends and a possible restraint on investment. An understanding of these factors will help other multinational hotel groups when considering their own expansion plans in China.

Market Entry Overview

Since 1978 and China's economic opening to the outside world, hotel investment throughout the country has become decentralised and diversified. By 2000, there were more than 150 hotel management companies operating in China, a third of which were multinational. The researchers note that just over a decade later, "given the steady and strong growth in demand in business and leisure travel, China has become an investment heaven for multinational hotel management groups".

There are, however, initial barriers to entry, including economic and political systems, hotel ownership, hotel management capability and resources, and competition between local and foreign firms. When groups do enter the market they usually choose non-equity forms of investment such as management contracts and franchising, although joint ventures are becoming more common. They are then confronted with location choices influenced by agglomeration economies, the presence of sufficient infrastructure and institutional changes.

The researchers set out to determine the key issues that multinational hotel groups face as they grapple with these decisions in their efforts to expand into, or further into, China. Of particular interest was identifying "an overall outlook for the hotel industry as it relates to investments proposed by multinational hotel corporations".

Expansion Information Collected

To ensure that they could analyse the greatest amount of information possible, the researchers turned to secondary resources, including InfoBank China, the China Economic Review, Hotel News Resource and Ebcohost. These databases include information on business activity and hotel industry developments in China from a wide range of sources, including Western and Chinese newspapers, industry journals and the Ministry of Foreign Trade and Cooperation.

With a timeframe from January 2006 to December 2008, the researchers used keywords to identify proposed hotel developments, combining terms such as "new hotels", "additional properties" and "hotel market" with terms such as "mainland China" and "Chinese market". Their analysis focused on 336 relevant documents, which revealed that 15 hotel groups made more than four expansion announcements and 14 groups made less than three announcements.

Expansion and its Issues

The researchers identified 18 groups with existing operations in China that were planning to expand and 11 new groups, considering entry to the market. For all of the groups, the most popular locations selected were Beijing and Shanghai, and their target markets were MICE, deluxe and economy. The preferred business format was the management contract.

The issues that the hotel groups needed to address in their expansion included political and macroeconomic factors, planned locations, brand selection, competitors, the number of hotels or rooms to be considered, the development timeframe and human resource development. The researchers note that most of these issues are interconnected, with the lack or abundance of human resources in an area affecting where a hotel might be related, for instance.

Categorising the hotel groups largely into upscale and budget, the researchers determined that the upscale groups were expanding more actively. The upscale category included hotels newly opened by existing brands and those that existing brands planned to open by 2011. The issues affecting planned hotels included the influence of political and macroeconomic factors, location planning, brand selection, competitors, number of hotels or rooms, development timeframe and human resource development. The newly opened hotels faced issues related to business formats, service concept and culture, hotel classification and target markets.

Existing budget brands were at an initial stage of development in comparison to their upscale counterparts. However, the researchers note their importance, with around 90% of Chinese domestic travellers staying at budget hotels. The issues that budget groups faced in their expansion included opportunities to invest in limited service hotels, location distribution, number of hotels and business format.

Development Trends

Considering the rapid increase in multinational hotel group development in China, the researchers identify a number of distinct trends. Management contracts are still the most common business format for upscale hotels, but joint ventures are becoming more common. Direct investment and franchising are more popular for budget hotels, but foreign hotel groups are still cautious with franchising and have limited experience with it in China.

The researchers note that the deluxe, upscale and MICE hotels discussed in the documents “can be considered as new trends in the Chinese hotel industry”. There are also observable trends in the choice of hotel locations, with ongoing development in provincial capitals being joined by expansion into second and third tier cities, plus tourist locations. This is particularly true amongst established multinational hotel groups, with opportunities for cooperation with local entrepreneurs opening up in these cities for groups willing to accept outside investment in development projects.

Perhaps the most important trend is that mega-events have been attracting hotel investment in their environs. As these events have relatively long durations and attract large

numbers of participants, they generate very high demand for accommodation. All of the hotel groups indicated the influence on their expansion plans of the Olympic games in Beijing during 2008, the World Expo in Shanghai during 2010 and the Asian Games in Guangzhou the same year.

However, the continuance of these trends is contingent upon government policy. In terms of direct influence, the government intervened in the market by adding upscale hotel developments to the restricted list for foreign investors when the property market boomed in 2006. Indirectly, the government has influenced the market over a longer term by imposing stringent lending practices in an effort to curtail the foreign debt market.

Market Potential Curtailed?

Overall, the researchers argue that multinational hotel groups are increasing in confidence as they extend the length of their stays in China. The country is something of an investment ‘heaven’ for them 30 years after the implementation of its open-door policy, but government restrictions can still be felt. Despite the huge market potential, there is still a hidden hand helping to shape and potentially hamper expansion plans.

Points to Note

- Multinational hotel groups are expanding rapidly in China.
- Upscale and budget groups face similar but not the same issues in planning their expansion.
- Distinct trends are evident in business formats, hotel types, locations and the influence of mega events.
- Government policy has the potential to limit expansion plans.

Guillet, Basak Denizci, Zhang, Hanqin Qiu and Gao, Bo Wendy (2011). Interpreting the mind of multinational hotel investors: Future trends and implications in China. *International Journal of Hospitality Management*, Vol. 30, pp. 222-232.