Article

How Fast Do New Hotels Ramp Up Performance?

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Abstract

Using an event study methodology and data from 3,494 new entrants in the U.S. lodging industry, this paper examines how quickly new hotels ramp up their performance after opening. For the years 2006 through 2009, new entrants entered with average daily rates (ADRs) above incumbents, and took seven quarters (1.75 years) to ramp up occupancies to the levels of comparable incumbent hotels. These averages include performance behavior of brand-managed, franchisee-managed, and unaffiliated independent hotel new ventures compared with incumbent hotels in similar geographic markets, locations, and price segments. Overall, new hotels reached comparable revenue per available room (RevPAR) performance by the second quarter of the second year of operation. RevPAR ramp-up was earlier for brand-managed hotels (first quarter of the second year), an outcome primarily attributable to higher occupancies and lower initial ADRs. Independent hotels took substantially longer than other new entrants to reach the RevPAR performance of existing hotels. Based on the faster ramp-up of new branded properties, the chief implication is that hotel developers should consider affiliating with a brand for quicker stabilization and short-term gain. The speed of hotels' ramp-up also calls into question the conventional view that new hotels represent a relatively risky investment.

Keywords

competitive strategy, strategy formulation, strategy implementation, strategic management, entrepreneurship, strategy and organizational performance, pricing, marketing and sales, product development, hotel management, operations

The perception that opening a hotel is a risky proposition invites the following research question: How long does it take for new hotels to reach the performance levels of comparable existing properties? A diverse and extensive literature exists to suggest that new ventures of all kinds face a risky beginning due to the "liability of newness" (Nagy and Lohrke 2010). This principle suggests that existing operations have a performance advantage due to routines that deliver consistent and reliable services and products with an efficient use of resources (Henderson 1999). Stinchcombe (1965) argued that the liability of newness is the result of entrepreneurs learning new roles, the lack of appropriate routines and formal structures, and the absence of stable external ties with key stakeholders. Key aspects of the organizational evolution of the firm (Churchill and Lewis 1983) include gaining confidence in new management processes and establishing organizational routines (Nelson and Winter 1982). Subsequent research has shown that dynamic and highly competitive environments create barriers to new venture success, particularly when incumbents provide highly differentiated services or products and engage in retaliatory competitive actions (Aldrich and Auster 1986). The market acceptance and brand recognition held by experienced incumbents, along with strong supplier relationships and sophisticated distribution channels, can serve as formidable hurdles for new entrants.

To compete with established competitors, new ventures often contract with franchise systems to take advantage of existing brand and operating knowledge and market acceptance (Barthélemy 2008). Barriers to new entry success are likely to be diminished for firms that enter the market under a brand umbrella, which provides expertise and tacit knowledge (Altinay 2005). The expertise offered by affiliation with a large branded hotel company may reduce the risks associated with new entry, and strengthen new entrant's capabilities (Hoopes and Postrel 1999). For the new venture, using an integrated operating system and tapping into existing shared resources is both efficient and effective in overcoming the established competitors' advantages (Barney 1991). Franchising is a popular approach for new

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hotel ventures in the United States, with around 70 percent of hotels affiliated with a chain. Even so, a substantial number of new properties are independent of a brand.

The purpose of this study is to explore how long it takes new entrants to ramp up their performance to obtain performance parity with comparable existing competitors. In manufacturing environments, the period between completion of development and full capacity utilization or performance stabilization is known as production ramp-up (Terwiesch and Bohn 2001), and we adopt that terminology for this study. While limited academic literature specifically addresses ramp-up or performance stabilization in hotels, a notable exception is the work of O'Neill (2011) who examined stabilization of occupancy in new hotels by recording the point at which occupancy levels no longer increased by one percentage point from the previous year. He considered the first year that the hotel reached its stabilized occupancy levels to be the end of the ramp-up period. O'Neill's (2011) exploratory study supported the conventional wisdom of a three-year build-up period.

In this article, we use the terms *stabilize* and *ramp-up* interchangeably to mean how long it takes a new property to achieve comparable performance levels with incumbent hotels with similar characteristics. We believe this approach is consistent with the manufacturing literature that focuses on competitive comparisons. Our study also explores average daily rate (ADR) and revenue per available room (RevPAR) ramp-up as well as occupancy, and it takes into consideration the different hotel operating forms that we mentioned earlier. In particular, we are interested in whether branded new entrants are able to ramp up their performance more quickly than independent hotels. While both franchised and independent operators may encounter the liability of newness and the need to acquire knowledge-based resources, franchised new entrants may face lower entry barriers, as we suggested above. In addition, we explore whether franchised hotels that are operated by the brand differ in ramp-up from those that are operated by the franchisee. Brand-managed hotels may bring a stronger commitment to operating procedures and more extensive know-how than franchisee-managed new businesses (Contractor and Sumit 1998). As we determine whether and how quickly new entrants reach the performance of incumbent hotels, we also compare the ramp-up times of franchising with independent and unaffiliated hotels because of the importance that operating form (i.e., brand managed, franchisee managed, and independent) may play in facilitating new venture success (Enz, Canina, and Palacios-Marques 2013).

Risk and Success in New Ventures

While the failure rate of new ventures is high, entry into some industries, such as those with radical new products and technological innovations, may be riskier than entry into service industries characterized as more operational than knowledge based, where technological resources and research skills are less critical to drive start-ups (Bharadwaj, Varadarajan, and Fahy 1993). In a study of new venture success, Shepherd, Douglas, and Shanley (2000) argued that the liability of newness was dependent on the degree of novelty associated with the new venture, and that management's ability to obtain needed information helps to raise the possibility of survival. They argue that over time, novelty and risk decline as ignorance decays (in keeping with the work of Nelson and Winter [1982] within evolutionary theory). In the lodging industry, it is possible that risk reduction is greater from the start (due to extensive available knowledge), and thus the liability of newness is less likely to lead to failure. If this is the case, we would expect new entrants to fare as well as incumbents after entry. Nevertheless, new ventures would face a ramp-up time as they gradually obtain and utilize information about customers. As new entrants accumulate experience that ensures consistency and high levels of service they should also be able to exact a higher price and enjoy higher demand. What is not clear is the actual length of this ramp-up time, although the industry uses various rules of thumb. In light of the structure of the lodging industry, characterized in the United States as mature, concentrated, and heavily franchised, along with the availability of customer information and easy access to customers via online travel agencies and global distribution systems, we argue that new hotels should be the beneficiaries of relatively short-time horizons for ramp-up, as the following hypothesis suggests:

> **Hypothesis 1:** New hotel entrants will achieve higher performance than incumbents within a relatively short ramp-up period.

Conventional wisdom would suggest that franchising is less risky than going into business on one's own. Franchisors provide a proven brand and operating system (Lafontaine 1999), access to distribution, and operational expertise (Caves and Murphy 1976). Institutional theory suggests that a new venture that deploys common resources and activities is perceived as more legitimate (Nagy and Lohrke 2010). A viable risk reduction strategy for an entrepreneur interested in opening a new hotel might be to enter into a franchise agreement to lessen the property's overall novelty in the marketplace. Hence, we would expect that access to a brand's distribution channels would facilitate higher occupancy levels at start-up, and brand standards would help to secure strong initial pricing practices.

In a recent study, Enz et. al. (2013) found that affiliation with a franchise had a significant positive effect on performance in the first six months of operation for full service hotels in the United Kingdom; these benefits were not sustained over time, however, nor did this apply to limited service hotels. The lack of a sustained effect may be due to the possibility that key information technologies are developed

externally (e.g., by third-party vendors such as online travel agencies), are nonunique, and are easily available.

The study described in this article contributes to this literature by comparing new entrant performance with comparable incumbents. To determine the time necessary to ramp up performance, care must be taken to match new entrants to comparable incumbent businesses located in the same geographic markets and operating locations. Other things equal, we would expect franchised hotels to experience quicker ramp-up and thus have a lower liability of newness than independent hotel new entrants.

Given the managerial expertise of a brand operator, we would further expect that this expertise would permit brand-managed hotels to outperform franchisee-operated properties. Finally, an owner who enters a new market without brand affiliation must either build or already possess knowledge, in addition to possessing labor and capital. Since it may take time to acquire this expertise, to build consistency in service delivery, and to build customer acceptance, we would expect that independent hotel new ventures would be slower than branded properties to obtain comparable performance with that of incumbents. Hence, we would argue that their more limited access to distribution, lack of a brand name, and an inability to tap an existing operational learning curve (less collective knowledge to tap into) would lengthen the time period of ramp-up for unaffiliated hotels. This discussion suggests the following hypotheses:

Hypothesis 2a: Brand-managed new hotel entrants will achieve higher performance than incumbents in a shorter time period than will franchise-operated and independent new hotels.

Hypothesis 2b: Franchisee-managed new hotel entrants will achieve higher performance than incumbents in a shorter time period than will independent new hotels.

Method

Data Sources

Our sample consists of 3,494 new hotels opening in the U.S. market from 2006 through 2009 and the comparable hotels already in operation at that time. We analyzed Smith Travel Research (STR) data for these hotels, which include measures of rooms available, rooms sold, and revenues for each property on a monthly basis, as well as other identification variables such as opening date, location, and operating form (i.e., brand managed, franchisee managed, and unaffiliated). To identify the 3,494 new entrants in our final sample, we first eliminated all hotels in the STR data that did not have a specified opening date, leaving a total hotel sample of 28,913 properties. From this sample, we extracted a total of 3,919 properties that had opened during the period under study, and then eliminated any hotels missing performance data for the opening year and hotels that did not match with comparable incumbent hotels (as we explain in a moment). Due to variable starting dates, the new entrant sample of hotels had from two years to six years of observations, including hotels that started in the first quarter of 2006, through hotels that started in the last quarter of 2009.

We chose properties in the STR database to serve as the comparable hotels as follows. Comparison incumbents must be distinguished from new entrants by having opening dates that are at least four years prior to those of the new entrants, and hotels that did not meet that standard were excluded. That way we avoided comparing a new entrant with a recently entered incumbent competitor. For example, a hotel that opened in 2007 would be compared with hotels that had been opened in 2003 or before. All incumbent hotels selected for the comparison groups had complete data for the years and quarters to match the new entrants.

Performance Measures

We first transformed STR's monthly data into quarters for each year of the study beginning with the opening quarter. We used the industry's well-accepted primary performance variables of occupancy rate, average daily rate, and revenue per available room. Furthermore, these measures are closely related to operating profit per available room (Canina, Enz, and Harrison 2005), which takes into account costs of operation. To ensure the viability of our measures, we checked the relationships as in the study by Canina, Enz, and Harrison (2005) using PKF Hospitality Research data. A Pearson correlation between RevPAR and operating profit per available room for a group of 2,740 properties with data from 2007 to 2010 (10,960 data points) was 0.813 ($p < .01$), suggesting a strong relationship between these variables.

Occupancy, which represents the percentage of available rooms occupied for a given period, was computed by dividing the number of paid guest rooms occupied for a period by the number of rooms available for sale in the same period. ADR was calculated as the total guest room revenue for a given period divided by the total number of paid occupied rooms during the same period (Enz, Canina, and Walsh 2001). Finally, RevPAR (revenue/supply) shows the economic efficiency of the property, and is traditionally used as a performance indicator in the lodging industry (Chung and Kalnins 2001). RevPAR was measured as the room's revenue divided by the annual number of available rooms. Each property was considered as a single case, and all available data for each hotel across time were assembled.

Event Study Analysis Approach

To determine a new entrant's ramp-up period, we used event study methodology, which consists of a set of econometric techniques to measure and interpret the effects of an event on a specific firm's performance. The event in this instance

is entry into the market. We applied a portfolio-matching approach that paired each new entrant with similar incumbent firms. Our approach followed the methodology used by Barber and Lyon (1996) and Hendricks, Singhal, and Stratman (2007) for the selection of comparison groups for each property, although special adjustments were made to conform to our research purpose, as described next.

Incumbent comparison groups. Our procedure for selecting firms to include in the comparison groups was based on a series of filters in keeping with prior studies. We established comparison groups who fulfilled three criteria: they were in the same geographical tract, property location, and ADR price range. The first filter, geographical tract, requires that the comparison properties are in one of 616 tracts or submarkets determined by STR. The hotels in a tract reflect the options available to a consumer who desires to visit a particular location, and those hotels are therefore competing in the same geographical area for a given consumer. The second filter, property location, captures whether a hotel is located in an urban, suburban, airport, metro or town, or resort or interstate site. Even if two properties are in the same tract, they are probably not competing if one is located at an airport and the other is in a suburban area. The final filter, ADR range, is an indicator of the level of quality or amenities of a given hotel. Comparison groups must comprise hotels of similar quality levels. Research on the composition and characteristics of hotel competitive sets found that comparison variability among hotels was less for the ADR cluster-based competitors than competitor groups determined using product type (Jin-Young and Canina 2011). Furthermore, Barber and Lyon (1996) and Lyon, Barber, and Tsai (1999) found that using matching portfolios of similar firms facilitates well-specified tests. Thus, we concluded that ADR offered a more rigorous filter than product type to ensure greater similarity when comparing new hotels with incumbent hotels. That said, to ensure that the use of an ADR filter did not bias our findings, the study was also conducted using STR's product segment variable. Comparing the results with an ADR filter versus the STR price segment measure revealed comparable results.[1] Based on this comparison, with tract and location variables controlled, the room rate is a good estimate for the quality level of the hotel as seen by customers.

In sum, the following steps were used to determine our incumbent comparison groups:

Step 1. For each new entrant, we identify all incumbent hotels in the same geographic tract and location that had an ADR within 90 to 110 percent of the new entrant hotel's average rate for the event year. Most of the sample (a total of 3,424 new entrants) were paired with a comparison group in this step. The average size of the comparison group was 5.34 incumbents.

Step 2. If a new entrant did not fit the rate criterion in Step 1, the ADR filter was increased 10 percentage points above and below, so the ADR filter was 80 to 120 percent, with no change in geographic tract or location. Another 70 new entrants were paired with a comparison group in this step. The average size of the comparison group was 2.41 incumbents.

Step 3. Finally, we removed the remaining 342 new entrants that did not fit the criteria in Step 2, because no comparable incumbent property could be found in the same market.

For each of 3,494 new hotel properties in the final sample, we estimated abnormal performance as new entrant's performance minus the median performance of the comparison group (Hendricks, Singhal, and Stratman 2007). The level of performance for both the new entrant and comparison group is calculated by comparing the level of performance for each quarter. This method is preferred to comparing each quarter with the previous quarter or with a base quarter as these methods might lead to bias in the results. We can expect an increase in the performance of the new properties in the first quarters until they reach the expected performance in that market. For each hotel in the sample, we pooled the observations across time and converted calendar quarter and year into event quarter and year. That is, the opening quarter and year is Q1Y1, the next time period is the second quarter of the first year, Q2Y1, and so on. For example, if the opening quarter is the third quarter of year 2008, then Q1 is the third quarter and Y1 is 2008, Q2 is the fourth quarter and Y1 is 2008, and Q3 is the first quarter and Y1 is 2009.

It is recommended in event studies to conduct nonparametric tests in conjunction with parametric tests to strengthen the inferences and assure consistency in the results (McWilliams and McWilliams 2000). We used median values for our comparison because outliers can significantly affect the performance values of the comparison groups. In addition, we ran the nonparametric Wilcoxon signed-rank test on the median values and the binomial sign test of the percentage of hotels experiencing positive abnormal performance in addition to the *t*-test of means as a way of mitigating the possible effects of extreme observations in the data set.

Results

Exhibit 1 presents the sample means, medians, and standard deviations for each of the key performance variables (occupancy, ADR, and RevPAR) for each of the five event years examined in the study. Given that the sample of new hotels spans several years, with different hotels entering in, each event year the sample size will vary by event year. As the data reveal, occupancies, ADRs, and RevPARs all increased for each year of the study period.

Exhibit 1:
Means and Standard Deviations for Occupancy, ADR, and RevPAR by Event Year.

	Year 1			Year 2			Year 3			Year 4			Year 5			Year 6		
	Mean	Median	*SD*	*Mean*	Median	*SD*	*Mean*	Median	*SD*	*Mean*	Median	*SD*	*Mean*	Median	*SD*	*Mean*	*Median*	*SD*
Occupancy	40.39	40.00	16.66	56.73	57.28	13.76	61.56	62.48	13.78	62.91	64.05	13.60	64.32	65.51	13.25	66.52	68.08	12.88
ADR	98.89	92.59	35.09	97.60	91.20	36.61	97.07	91.25	38.30	96.38	90.60	37.21	96.37	91.63	32.42	98.61	94.03	34.88
RevPAR	41.11	36.89	25.58	57.05	52.06	29.29	61.68	56.63	32.51	62.60	57.75	32.47	63.96	60.25	29.13	67.95	64.54	32.07
Sample size		3,391			3,494			3,491			2490			1370			576	

Note. ADR = average daily rate; RevPAR = revenue per available room.

For brevity, Exhibit 2 shows the results on median abnormal performance in occupancy, ADR, and RevPAR values for all new entrant hotels over the first eight quarters of operation (although the analyses span five years[2]). The percentage of sample firms with performance greater than the comparison incumbents' median is also provided, along with the Wilcoxon signed-rank test *Z*-statistic for the median (in parentheses), and the binomial sign test Z-statistic for the percentage positive (in parentheses). The parametric *t*-tests for means were consistent with the nonparametric tests of medians; hence, outliers did not influence the results. Again for presentational clarity, Exhibit 2 reports just the nonparametric test results for the first two years of new hotel operation. As Exhibit 2 reveals, in the first quarter of operation, only 5.4 percent of the new entrant hotels do better than the incumbents' median occupancy, and 5.44 percent beat existing hotels' RevPAR. The median abnormal performance in the first year first quarter is −31.47 percent for occupancy, and −US$28.44 for RevPAR. In contrast, for ADR, 62.65 percent of the new hotels do better than the median of incumbent hotels in their starting quarter. These results clearly suggest that over half of new entrants enter with comparable market rates, and that their RevPAR results are primarily shaped by the new entrants' lower occupancy.

The new entrants' abnormal results are positive and significant for occupancy in the fourth quarter of the second year, and in the third quarter of the second year for RevPAR. The median occupancy in sample properties was 1.37 percent higher than their comparison groups and significantly different from zero ($p < .001$), and almost 54 percent of the new hotels experienced positive abnormal results in occupancy. By the third quarter of the second year, the median abnormal performance in occupancy for the new entrants was 1.04 percent in RevPAR, positive and significantly different from zero. Nearly 54 percent of new entrants did better than the median RevPAR performance of their comparison incumbent hotels.

The results support the first hypothesis, that new hotel entrants achieve higher performance than incumbents relatively quickly—in well under three years. In this study, that moment occurred in the fourth quarter of the second year. With regard to RevPAR, the test statistics revealed that new entrants' RevPARs exceeded those of comparison incumbent hotels in the third quarter of the second year of operation. For occupancy, the new entrants reached comparable occupancies with incumbents by the fourth quarter of the second year, while over half of new hotels began with higher rates than incumbents.

Exhibit 3 shows the ramp-up of new entrant performance compared with competitors on the three performance measures over the entire five-year period of the study. The graph depicts the new entrants' generally higher ADRs, and shows that these new hotels remained at higher price levels for the entire five-year period of the study. In contrast, occupancy levels took almost two years to surpass those of incumbents. Nearly 51 percent of the new entrants did better than the median occupancy of the hotels that belonged to their comparison group by the third quarter of the second year. The pattern of RevPAR ramp-up mimics that of occupancy during this time period. As occupancy stabilizes over time and ADR gradually rises, RevPAR reflects a modest increase.

Ramp-up by Operating Form

Turning to the test of Hypotheses 2a and 2b, regarding the ramp-up for chain-managed, franchisee-managed, and independent hotels, we examine the median abnormal performance of new entries in each category, as shown in Exhibit 4. The median abnormal occupancy performance is positive and significantly different from zero in the fourth quarter of the second year for both brand-managed and franchisee-managed new entrants. In contrast to that performance by the brand-managed and franchisee-managed entrants, the Wilcoxon signed tests revealed that independent hotels achieved significantly higher occupancies in the second quarter of the fifth year. Almost from the beginning new entrants were able to produce statistically significant and positive median abnormal ADR performance: in the second quarter, the abnormal ADR performance was US$2.02 for brand-managed properties, US$2.84 for franchisee-managed hotels, and US$3.26 for independent hotels. The RevPAR performance of brand-managed new entrants ramped up by the second quarter of the second year, followed by franchisee-managed hotels in the third

Exhibit 2:

New Entrant Performance Ramp-up Compared with Incumbents in the First Two Years.

		Occupancy		ADR		RevPAR	
Time Period	Sample Size	Median (Wilcoxon Signed Test Z-Statistic)	% Positive (Binomial Sign Test Z-Statistic)	Median (Wilcoxon Signed Test Z-Statistic)	% Positive (Binomial Sign Test Z-Statistic)	Median (Wilcoxon Signed Test Z-Statistic)	% Positive (Binomial Sign Test Z-statistic)
Opening year							
1st quarter	3,127	−31.47 (−46.95)***	5.4 (−49.86)***	2.75 (−15.7)***	62.65 (−14.13)***	−28.44 (−46.66)***	5.44 (−49.82)***
2nd quarter	3,472	−14.42 (−40.18)***	17.83 (−37.9)***	1.67 (−16.1)***	61.46 (−13.49)***	−13.01 (−39.59)***	18.58 (−37.01)***
3rd quarter	3,472	−7.83 (−27.2)***	29.81 (−23.8)***	0.97 (−11.69)***	57.46 (−8.78)***	−6.96 (-25.84)***	30.99 (−22.41)***
4th quarter	3,487	−4.46 (−17.46)***	37.05 (−15.27)***	1.17 (−10.06)***	57.64 (−9.01)***	−3.55 (−14.87)***	38.83 (−13.18)***
Second year							
1st quarter	3,489	−1.96 (−8.56)***	44.08 (−6.98)***	1.34 (−11.15)***	57.52 (−8.87)***	−1.41 (-5.38)***	46.26 (−4.4)***
2nd quarter	3,486	−0.42 (−2.42)*	48.97 (−1.2)	1.9 (−13.43)***	59.32 (−10.99)***	0.26 (−1.22)	50.69 (−0.8)
3rd quarter	3,482	0.33 (−1.48)	50.86 (−1)	2.02 (−13.78)***	59.85 (−11.61)***	1.04 (−4.82)***	53.22 (−3.78)***
4th quarter	3,483	1.37 (−5.65)***	53.95 (−4.64)***	2.25 (−14.66)***	60.29 (−12.13)***	2.49 (−9.36)***	55.96 (−7.01)***

Note. ADR = average daily rate; RevPAR = revenue per available room.

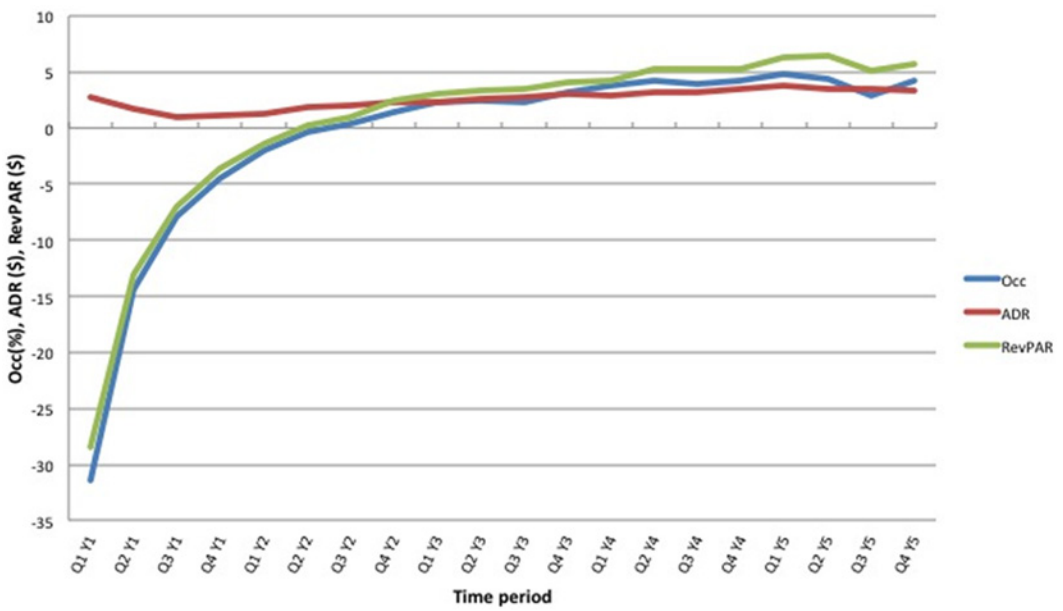
*Significantly different from zero (50% in the case of percent positive) at the .05 level for the two-tailed test.

**Significantly different from zero (50% in the case of percent positive) at the .01 level for the two-tailed test.

***Significantly different from zero (50% in the case of percent positive) at the .001 level for the two-tailed test.

Exhibit 3:

The Ramp-up of New Entrant Performance Compared with Competitors (Median Abnormal Performance Percentage for Occupancy ADR and RevPAR).



Note. ADR = average daily rate; RevPAR = revenue per available room.

Exhibit 4:

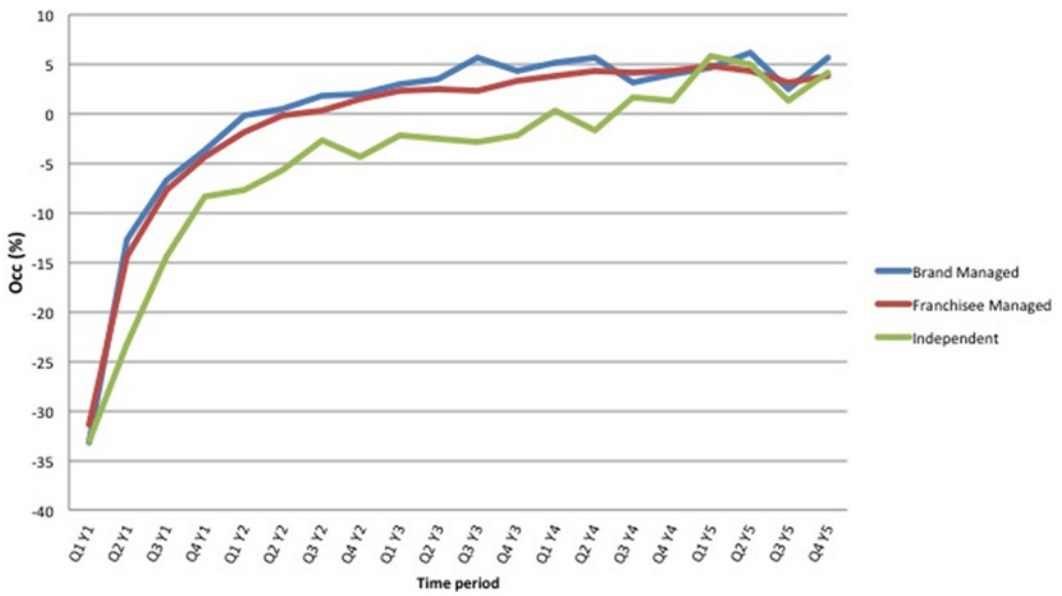
New Entrant Abnormal Performance Compared with Incumbents By Operating Form.

	Operating Form		
Abnormal Performance	Brand Managed	Franchisee Managed	Independent
Occupancy			
Median (%)	1.91	1.52	4.99
Wilcoxon signed test (Z-statistic)	−2.04*	−6.00***	−2.16*
Ramp-up year/quarter	2nd year, 4th quarter	2nd year, 4th quarter	5th year, 2nd quarter
ADR			
Median (US$)	2.02	2.84	3.26
Wilcoxon signed test (Z-statistic)	−3.59***	−16.41***	−2.90**
Ramp-up year/quarter	1st year, 2nd quarter	1st year, 1st quarter	1st year, 3rd quarter
RevPAR			
Median (US$)	4.84	0.97	3.83
Wilcoxon signed test (Z-statistic)	−3.16**	−4.60***	−2.08*
Ramp-up year/quarter	2nd year, 2nd quarter	2nd year, 3rd quarter	5th year, 2nd quarter

Note. ADR = average daily rate; RevPAR = revenue per available room.
*Significantly different from zero (50% in the case of percent positive) at the .05 level for the two-tailed test.
**Significantly different from zero (50% in the case of percent positive) at the .01 level for the two-tailed test.
***Significantly different from zero (50% in the case of percent positive) at the .001 level for the two-tailed test.

Exhibit 5:

Occupancy Ramp-up of New Entrant Performance Compared with Competitors for Brand-Managed, Franchisee-Managed, and Independent Hotels.



quarter of the same year. Unaffiliated new hotels took till the second quarter of the fifth year to ramp up and exceed the RevPAR performance of incumbent hotels. These results provide support for Hypothesis 2a, revealing that brand-managed new entrants achieved ramp-up to higher median performance than incumbents in a shorter time period than did either franchise-managed or unaffiliated new hotels. We also found support for Hypothesis 2b that franchisee-managed new hotels did better than the median performance of their comparison hotels more quickly than did independent new entrants. In the case of RevPAR, it took independents almost three years longer to do better than the median performance of their comparison incumbent hotels. These results are shown graphically in Exhibits 5, 6, and 7. Exhibit 5 shows the occupancy results, Exhibit 6 addresses ADR, and Exhibit 7 summarizes RevPAR outcomes.

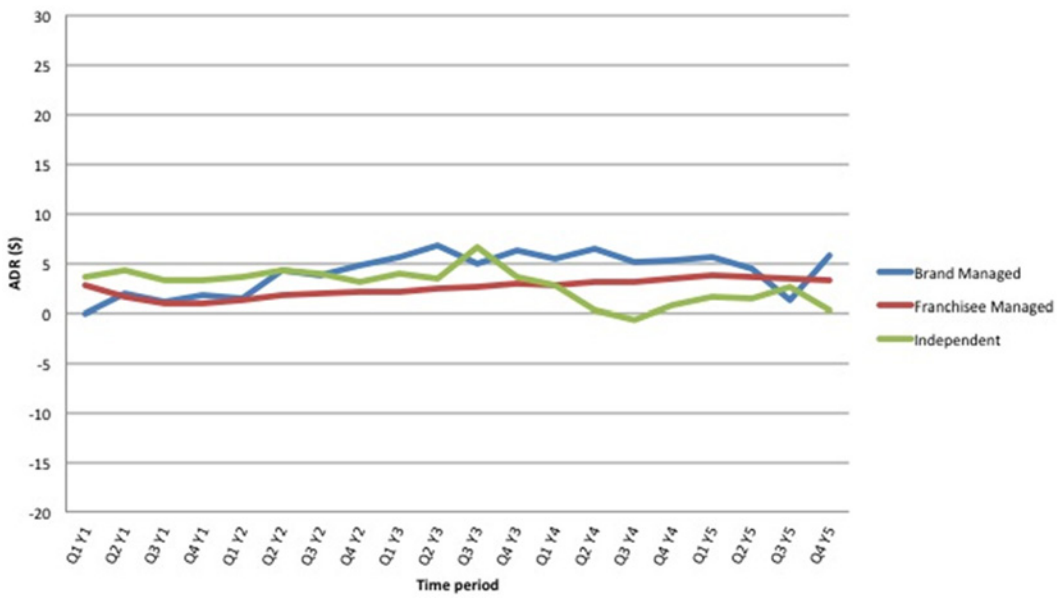
Discussion and Conclusion

The findings of this study indicate that new hotels fare quite well compared with established hotels, particularly if they enter the market using a brand, whether brand- or franchisee-managed. This finding is particularly interesting given that hotel age is a significant predictor of hotel performance (Canina, Enz, and Harrison 2005; O'Neill and Mattila 2006). Overall new branded entrants begin with higher prices and ramp up their occupancies quickly. It is possible that franchised hotels are able to achieve the quickest ramp-up in occupancies because of their access to customers, distribution, and marketing infrastructure. Our results show that branded hotels, and particularly brand-managed new hotels, were able to produce market-comparable occupancy and RevPAR rates two years faster than new independent hotels. These results provide support for existing theory that articulates the importance of established distribution channels and investments in marketing to significantly reduce entry barriers (Caves and Porter 1977).

While new ventures are often regarded as risky and subject to the liability of newness, we found little evidence that new ventures in the hotel industry face these hazards. Quite the contrary, new entrants were able to begin with price premiums and generally increase demand quickly, suggesting that the hotel industry may not be as risky for new entry as is generally thought. It may also be the case that elements of differentiation used by incumbents to establish a competitive position are easy for new entrants to imitate. The level of comparability among lodging products and the use of a business-format franchise model that facilitates the transfer of knowledge to new entrants appear to reduce the threats of new entry. However, all hotel operations would be advised to begin working on demand before opening to achieve a vertical ramp-up. It is interesting to observe how quickly new entrants were able to match (or erase) the performance advantage of comparable hotels, suggesting that all hotels would be well advised to work on more sustainable

Exhibit 6:

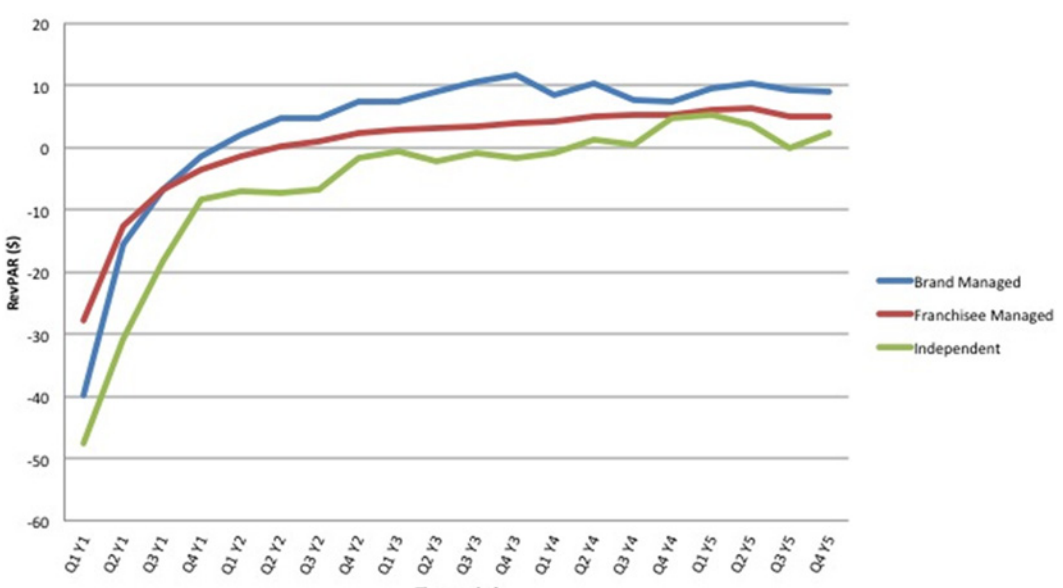
ADR Ramp-up of New Entrant Performance Compared with Competitors for Brand-Managed, Franchisee-Managed, and Independent Hotels.



Note. ADR = average daily rate.

Exhibit 7:

RevPAR Ramp-up of New Entrant Performance Compared to Competitors for Brand-Managed, Franchisee-Managed, and Independent Hotels.



Note. RevPAR = revenue per available room.

elements of differentiation to establish real entry barriers and make imitation more difficult. Innovative practices in channel management, management communication, and the strengthening of cultural and local ties (Vila, Enz, and Costa 2012) or through new social requirements such as green and responsible attitudes (Millar and Baloglu 2011) are but a few ways in which operators might begin the process of building unique elements of differentiation.

One limitation of this study is that we did not consider profit, because those figures are not available. We did not take into account the operational fees that franchised and branded new entrants incur, because of our focus on top-line revenue versus bottom-line profits. We would have preferred to explore gross operating profit per available room (GOPPAR), in part because attention should be given to the possibility that independent hotels that were not subject to these fees may have experienced lower costs than the branded hotels we studied, and thus fared better than suggested by revenue data.

Future research should continue to refine these findings and explore whether more or less complex hotels with different levels of novelty ramp up at the same rate. It is possible that luxury and economy hotels ramp up at different speeds, for instance. As we noted earlier, the contribution of this study is its demonstration, using a five-year event study methodology, that new hotel ventures may be far less risky than previously thought, and that they can pose a serious threat to current competitors given their ability to enter with strong prices and secure and sustain higher occupancy levels in a relatively short time. For those interested in entering a hotel market, our advice would be to enter with a branded product preferably managed by the brand itself to assure the quickest and strongest ramp-up in performance.

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Notes

1. The data using price segment versus ADR are available upon request from the authors.
2. The detailed results for all five years are available from the authors.

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