

NETWORK INTERACTION IN THE HOSPITALITY INDUSTRY AND ITS IMPACT ON THE FINANCIAL CONDITION OF THE HOTEL COMPANY

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ABSTRACT

The study describes the main theoretical aspects of the network interaction in the hospitality industry. The statistical data characterizing the hotels in Russia has been considered. The research presents the specificity of functioning of the Russian hotel chains at the world level. The authors introduce the methodical approach to the assessment of the financial condition of the hotel enterprises from the position of the management company. The paper proposes the algorithm of the comparative rating evaluation of the investment attractiveness for including hotel into a network. The network interaction for the hotel industry enables to assess the financial condition.

Keywords - Network Interaction, Hospitality Industry, Financial Condition, Hotel Company

INTRODUCTION

Modern conditions, characterized by global processes in the world economy, actualize the search for new forms of business organization focused on collaboration and partnership. "Local tourism innovation is often developed in entrepreneurial networks where collaboration is the crucial factor" (Boesen, Sundbo & Sundbo, 2017, p.2).

The strategic goal of the business structures is adapting to the changes in the external environment that are associated with deep differentiation of demand, increasing complexity of production technologies, the significant increase in capital intensity of investment projects.

Today, in the post-industrial phase of social development, the processes of specialization and cooperation of enterprises from different branches and spheres of activity, are aimed at minimizing the costs and increasing the level of competitiveness. However, the high centralization and specialization do not always mean the effective management of large companies.

The purpose of this article is to analyze and summarize the extensive experience in the evaluation of accommodation facilities generated in developed Western market and test it in the current economic condition in Russia.

LITERATURE&THEORY

At the end of the XX century, a famous specialist in the field of strategic management Peter Doyle (Doyle, 2002) noted that the creation of business networks based on cooperation with external suppliers and the possibilities of joint usage of the specialized equipment is indispensable for the long-term success.

According to the Russian researches (Alexandrov, 2010), the network is a special form of cooperation of independent companies or individual performers, coordinated through the market mechanisms and interrelated chain of orders and contractual relationships. The enterprises of this type have business agreements with research firms, centres for the development of new products or technical innovations.

The cooperation between legally independent companies involves a stable, long-term bond to exploit a specific market opportunity, each company being responsible for the individual duties and all of them being responsible for reaching the common objective (Nieves & Juan Carlos, 2002). Though, a network organization is an association of independent individuals, social groups and/or organizations, it operates in a coordinated manner basing on achieving the agreed goals and having a common corporate image and corporate structure. The definition of network structure (Milner, 2000) reveals the nature of the formation of network organizations and coordinates the market mechanisms instead of command methods. Milner also noted that the network organization can be replaced the bureaucratic centralized structures "chain of orders for the supply of products" (Milner, 2000).

A study of the scientific literature on this issue shows that the key prerequisites for the formation of a network business are:

- the fragmentation and turbulence of the markets;
- a large range of manufactured goods;
- high output modified versions of products that require additional investment;
- the degree of capacity utilization with the possibility of relocation partners in the processing chain;
- localization of the suppliers near the markets, etc.

The analysis shows that functioning of network organizations is based on the following key principles:

- The members of the network are independent. The principle of independence assumes that all the members of the network organization have a certain level of freedom when choosing the priorities of their own activities.
- A network organization can have a variety of leaders. That means that any member of the organization, possessing the required resource (financial, industrial, etc.) and mobilizing it to achieve the common goals, assumes a part of the responsibilities for reaching these goals.
- A network organization has a common goal, which involves cooperation and can be expressed in combining the necessary resources, the development of a regional marketing network, consolidation of the efforts, etc.

- The links in the network organization are voluntary and assume flexibility of the business structure (Alexandrov, 2010).

METHODS

An international hotel chain is an association of a certain number of hotel enterprises in several countries with the same brand (or several brands), which have a shared reservation system, corporate culture, service standards and quality. This enables getting a greater profit by saving on the scale of production and customer loyalty. International hotel chains operate through several forms of management: contract management, leasing and franchising.

Table 1
Key performance indicators of the collective accommodation facilities in Russia

	January-March 2017	January-June 2017	January-September 2017
The number of collective accommodation facilities	15170	18545	20730
The number of the rooms, thousands	1401	1723	1852
The number of the nights spent, thousands	33327	88066	166885
The number of the accommodated persons, thousands	9772	23722	42396
among them:			
the citizens of Russia	8713	20782	36371
the foreign citizen	1060	2941	6024

A management contract is an agreement about the management between the business owner and the hotel chain.

Currently, the administration is performed by the management company which runs the business of a hotel company professionally. Leasing (or lease) is the investment of funds for the acquisition of a certain property. The lessor, the lessee and the lease seller are involved in the transaction.

Franchising is a form of long-term business cooperation between the hotel chain and the hotel company. The hotel chain (the franchisor) provides the hotel company (the franchisee) with the license (franchise) to conduct activities under the name of the owner in a limited area, for the term and conditions specified in the contract.

Table 2
Hotels and similar accommodation facilities

	2005	2010	2011	2012	2013	2014	2015	2016
The total number of the hotels and similar accommodation facilities	4812	5953	6357	6706	6998	7898	8391	14948
the number of the rooms they provide, thousands	404	458	495	516	565	698	704	1035
Of the total number of the hotels and similar accommodation facilities:								
hotels	3663	4220	4444	4666	4856	5445	5697	9243
the number of the rooms they provide, thousands	330	366	386	397	439	550	540	750
motels	48	99	123	132	138	155	167	275
the number of the rooms they provide, thousands	3	3	6	4	6	7	7	9
hostels	516	507	500	484	495	492	535	881
the number of the rooms they provide, thousands	35	38	40	45	45	41	43	53

The majority of international hotel chains prefer to enter into a franchise agreement, but the other forms of management are no less popular. As a rule, large hotel chains use different forms of management. For example, Starwood Hotels&Resorts Worldwide is simultaneously the owner of the hotel real estate, the managing company and the franchisor with a multi-brand portfolio of the hotel real estate. The international hotel chain Accor uses all the above-mentioned forms of the hotel management around the world.

The following international hotel chains are represented in Russia: Hilton Worldwide, The Rezidor Hotel Group, Accor Hospitality, Marriott International, InterContinental Hotels Group, Starwood Hotels & Resorts, Hyatt International, Swissotel Hotels & Resorts, Hyatt International, Lotte Hotel Group, Kempinski Hotels, Rocco Forte, Four Seasons Hotels & Resorts, Sokos Hotels, Domina, Ramada Worldwide.

Table 3
The best hotel groups in the world in 2010-2016

Ranking		Group	Country	Hotels		Rooms		Changes in the number of rooms available	
2015	2016			2016	2015	2016	2015	Aбс.	%
1	1	Hilton Worldwide	USA	4840	4697	710295	68673	23422	3,4
2	2	Marriot International	USA	4278	4073	708268	672083	36185	5,4
3	3	Wyndham Hotel Group	USA	4117	3854	701899	662821	39078	5,9
4	4	Chois Hotels Int	USA	7645	7485	660826	645423	15403	2,4
5	5	Accor	USA	6376	6340	504808	506058	-1250	-0,2
6	6	Starwood Hotel and Resorts	FRA	3717	3576	484296	461719	20577	4,5
7	7	Best Western	USA	1207	1161	346599	339243	7357	3,3
8	8	Home Inns	USA	3900	4046	302144	314318	-12174	-3,9
9	9	Jin Jiang (inc. Louvre Hotels	CHI	2609	2180	296075	256555	39520	15,4

Most of the hotels and apartments of foreign brands operating in Russia are concentrated in Moscow (38 % hotel area of foreign operators in the Russian market). The majority of the hotels in Moscow, including a quarter of all rooms and apartments, are operated under various international brands. Though the bigger part of the Moscow hotels is represented by luxury five-star hotels, there is a lack of hotel rooms of the international quality available at the average price range.

From the financial and economic point of view, the question of the effectiveness assessing of including a single enterprise of the hospitality industry in the network remains relevant.

It's well-known that the valuation of hotels is a challenging task. Therefore, many methods of determining the cost of business have been developed. They vary from the method developed by Coca-Cola multiplier (the rule of 10 000) to the methods of discounted cash flows (DCF).

“Numerous researchers and academicians apply discounted cash flow (DCF) analysis merely to compute the interest earned and charged during the credit period but not to the revenue and other costs which are considerably larger than the interest earned and charged” (Wu, Al-Khateeb & etc, 2016).

Every method has its own peculiarities and the limits of application.

The cost of hotels can be evaluated for a variety of different purposes, such as:

- the owner is planning to realize the existing asset and needs to verify the relevance of the price;

- the developer is creating a project of the hotel construction and must justify the amount of the required investments to the interested parties;

- the hotel can be a collateral in a loan agreement. It is necessary to determine the collateral value that can be obtained in case of default of the borrower;

- the investors are planning to buy a hotel and need to assess its value.

Depending on the purpose of the assessment, the intentions of buyers and sellers, the quality and quantity of the original information, certain methods of evaluating the cost of hotels are selected.

RESULTS

Hotels are unique in comparison with other real estate objects. Their value does not depend on the ability to generate the cash flow from rent, but on the daily diverse operations, such as:

- renting rooms for guests;

- catering services (F&B);

- functioning of the Spa complex, gym, etc.

Besides, such objects are characterized by significant investments in movable property (furniture, equipment, interior elements, etc.). In this regard, the forecast of the future cash flows generated by hotels is a complex task which involves a high degree of uncertainty.

In accordance with the RICS (2012) valuation standards, hotels belong to the trade related properties and, as a rule, participate in transactions of purchasing and selling depending on their trading potential. When the property represents an operating enterprise, it usually includes the following components:

- registered rights to the land parcel;

- registered rights to improve the land parcel;

- commercial inventory, which includes furniture, trade fixture and equipment (FF&E) installed for getting profit;

- non-material component: the market assessment of trade potential with the proposed possibility of obtaining (prolonging) the validity of existing licenses, permits, certificates and tolerances.

Depending on the purpose of the evaluating of the hotel cost and the quantity and quality of the background information, sometimes a need in identifying the cost of immovable and movable property arises. Although a unified concept of identifying this figure hasn't been developed, in this paper we are trying to propose some possible variants.

CONCLUSIONS

In our opinion, a number of primary factors and indicators should be taken into account when evaluating the entry of an individual hotel company into the network.

The primary factors are necessary to carry out on the first stage of evaluation. The following indicators should be analyzed for entry into the network:

-the carrying value of fixed assets and infrastructure (this indicator reflects the current value of the assets for collective accommodation, while their availability and quality are essential for the consumer);

- the level of equity (this indicator reflects the security of the hotel company's own capital, it is also used in the calculation of additional indicators that represent the effectiveness of financial and economic activities);

-profitability of sales (core activity) (the indicator reflects the efficiency of the main production and allows you to plan the profit from the main activity less other income);

-production cost (works, services) represents a cost estimation used in the process of production (works, services), natural resources, raw materials, materials, fuel, energy, main funds, labor resources as well as other costs of its production and sales (Turmanidze, 2008).

These figures can be easily estimated with the help of well-known methods [4]. The next stage of the assessment is the evaluation of the hotel rating allowing to estimate the hotel attractiveness which is important for including the hotel in the network. The calculation of the final rating indicator is based on the comparison of the hotels for each indicator with the imputed values of the reference hotel.

In general, the algorithm of the comparative rating evaluation of the investment attractiveness of the hotel for including it in the network represents the sequence of the following actions:

1. The source data is formed into a summary table.
2. The maximum value for each indicator is determined and it is entered in the corresponding cell of the reference hotel (m+1).
3. The indicators of the table are standardized in accordance with the corresponding figure of the reference hotels in the formulas:

$$x_{ij} = \frac{K_{it}^n}{K_{it}^{n+1}} \quad (1)$$

x_{ij} - standardized indicators of the state j-hotel.

K_{it}^n, K_{it}^{n+1} - standardized indicators of the state j-hotel in n and n+1 year

4. The values are defined for each type property:

$$R_j = \sqrt{k_n \sum_{i=1}^m (1 - x_{ij}^n)^2 + k_{n+1} \sum_{i=1}^m (1 - x_{ij}^{n+1})^2} \quad (2)$$

R_j - rating score for j-hotel;

k_n, k_{n+1} - weighting coefficient in n and n+1 period.

5. The hotels should be presented in the descending rating order. The hotel with a minimum value of R has the highest rating.

There is no restriction in the number of the indicators compared and the number of the hotels for applying this algorithm in practice.

Thus, the algorithm of the comparative rating evaluation of the investment attractiveness for including a hotel into the network has been developed and proposed. A number of primary factors and indicators should be taken into account when evaluating the entry of an individual hotel company into the network. The network interaction for the hotel industry enables to assess the financial condition. The analysis makes it possible to research the methodical approach to the assessment of the financial condition of the hotel enterprises.

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