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Revenue Management in China's Lodging Sector: Practices and Challenges

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Learning outcomes

After reading this chapter, you should be able to:

- Understand hotel revenue performance in China by ownership, management, level of services determined by star-ranking system, and major hotel markets in China.
- Appreciate a macro review of hotel financial performance which demonstrates the diversity and complexity of hotel ownership structures, management organisations and regional variations in hotel revenue generation.
- Understand the challenges facing China's hotel industry for implementing effective revenue management systems, including insufficient forecasting based on past performance data, lack of a uniform system of accounts for the hotel industry, inadequate market segmentation for developing a differentiated pricing structure to capture consumers of different price points, inefficient management structure and knowledge of revenue management facing many state-owned enterprises (SOE) and domestic private firms.

■ Introduction

The lodging sector in the Chinese tourism industry became one of the earliest businesses to be exposed to international hotel management standards, when China first instituted joint-venture hotel development initiative in the early 1980s and later granted sole foreign investment of hotel development. Such knowledge transfer of hotel management from international management to hotel operations in China benefited, to some extent, from the effectiveness and efficiency of Chinese hotel operations, particularly in functional areas of financial

management: budgeting, internal cost control, yield or revenue management. However, due to the extreme complexity of hotel ownership structure, brand affiliation, variations of demand and supply in regional markets and business practice influenced by social and cultural factors in China, a myriad of business practices in hotel revenue management in China has been shaped by the complex set of political, business and cultural factors. This chapter reviews the array of hotel ownership structures and compares their associated financial performances. It then examines hotel revenue management practices determined by different cultural and business factors. Finally, it identifies and analyses the challenges facing revenue management in hotel operations and presents recommendations for effective revenue management in China's lodging sector.

■ Financial performance

□ Hotel ownership and financial performance

The current hotel ownership structure in China provides a living testimony to the phenomenal economic reform and transformation from the state owned enterprises (SOE) to a highly diversified ownership portfolio of public, private, joint venture and sole foreign investment, with different variations of ownerships under each structure. Table 7.1 exhibits the diverse and complicated ownership and business structures in the lodging sector in China. It is evident that hotels owned by the government have been reduced significantly compared to 35 years ago. Replacing the SOE hotels are the hotels developed by domestic private and collective businesses, organized in various legal forms. Only a very small proportion of the hotel stock in China is owned and financed by investors from Hong Kong, Macau, Taiwan and foreign countries. Absent from a national uniform system of accounts for hotel operations, one could just imagine that there must be many different standards and practices used for revenue management in China.

The financial performance of Chinese hotels at different star ranks demonstrates revealing aspects of revenue management at the national level (Table 7.2). Nationally, four of the five star-ranking categories were reported at quite similar performance levels of low 60% occupancy, except for the 2-star hotels reporting 57% occupancy in 2011. The average daily rate (ADR) and revenue per available room (RevPar) showed clearly differentiated lodging product supply by star ranking system. However, the rates and the revenues generated were considerably lower than countries in Europe, North America and some neighboring Asian countries such as Japan, South Korea, particularly in the 5-star and 4-star segments.

Table 7.1: Hotel ownership in China, 2011

| | Ownership | 5-Star | 4-Star | 3-Star | 2-Star | 1-Star | Total |
|---|-------------------------------------|--------|--------|--------|--------|--------|-------|
| Domestic Assets | SOE | 152 | 658 | 1711 | 1079 | 47 | 3647 |
| | Collective | 6 | 50 | 225 | 185 | 9 | 475 |
| | Stock cooperative | 4 | 55 | 117 | 73 | 1 | 250 |
| | Joint SOE | 1 | 1 | 5 | 3 | 0 | 10 |
| | Joint collective | 0 | 2 | 10 | 8 | 0 | 20 |
| | Joint SOE & collective | 0 | 1 | 4 | 5 | 0 | 10 |
| | Other joint ownership | 0 | 3 | 1 | 1 | 1 | 6 |
| | SOE – Sole ownership | 33 | 109 | 161 | 68 | 2 | 373 |
| | Other limited liability co. | 19 | 65 | 141 | 60 | 4 | 289 |
| | Equity trading company | 29 | 137 | 298 | 129 | 9 | 602 |
| | Private – sole ownership | 31 | 137 | 709 | 694 | 51 | 1622 |
| | Private – partnership | 11 | 35 | 149 | 147 | 7 | 349 |
| | Private limited liability co. | 56 | 323 | 851 | 389 | 18 | 1637 |
| | Private equity trading co. | 11 | 45 | 90 | 56 | 1 | 203 |
| Other | 9 | 35 | 142 | 89 | 4 | 279 | |
| Joint & sole assets from Hong Kong, Macau and Taiwan (HKMT) | Joint-venture from HKMT | 41 | 43 | 41 | 8 | 0 | 133 |
| | Cooperative with HKMT | 8 | 10 | 11 | 3 | 0 | 32 |
| | Sole ownership by HKMT | 19 | 33 | 23 | 3 | 0 | 78 |
| | HKMT equity trading co. | 8 | 6 | 9 | 0 | 0 | 23 |
| Foreign Assets | Joint-venture with foreign investor | 32 | 42 | 30 | 4 | 0 | 108 |
| | Cooperative with foreign Investor | 9 | 9 | 11 | 0 | 0 | 29 |
| | Foreign sole ownership | 26 | 19 | 19 | 7 | 0 | 71 |
| | Foreign equity trading co. | 6 | 1 | 10 | 1 | 0 | 18 |
| | Total | 615 | 2148 | 5473 | 3276 | 164 | 11676 |

Source: China National Tourism Administration, *2011 Statistical Bulletin of Star-Ranked Hotels in China*. China Travel & Tourism Press, June 2012.

It is interesting to note that the Chinese hotels at all five star categories generated significant revenues from food and beverage services, with over 40% of the total sales from food and beverage operations for the 4-star, 3-star and 2-star hotels. Such food and beverage revenue performance indicates that hotel food and beverage outlets are an essential part of the local society providing dining services and event functions for local residents, particularly so considering the low utilisation rates of the hotel rooms nationwide. When examining the efficiency of revenue generation measured by fixed asset turnover, the lower ranking hotels performed better than the 4-star and 5-star hotels: the 2-star hotels generated the highest revenue, ¥63 for ¥1 in fixed assets while the 5-star hotels had the lowest ratio of generating ¥45 revenue for every ¥1 in fixed assets. The different ratios of fixed asset turnover by different star-ranking categories reveal that the upscale and luxury hotels in China face the challenge of reducing capital intensity by efficiently utilizing the property's fixed asset to produce sales.