



# Estimating the land opportunism of hotel investment in generating real estate appreciation and firms' market value

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## ABSTRACT

The scarcity of well-located land is becoming an important concern for business operations around the world. This study sheds lights on the mechanisms of land speculation by explaining how Chinese businesses' investment in hotels leads to real estate appreciation and firms' market value increase. This study proposes that hotel investment not only has the potential to increase firm value through the hotels' operational revenues; land opportunism may also lead to real estate appreciation and associated increases in market value. The study investigates the effect of land opportunism in the Chinese hotel investment context. Publicly listed companies that invest into hotel businesses to diversify their business were selected as the main sample. The findings show that hotel investment improves Chinese firms' value. Specifically, hotel investment increases these firms' real estate value and the hotel real estate appreciation drives the increases in the companies' value in the securities market. This mode of hotel investment is promoted by both local governments and hotel developers. It is possibly harmful to the hotel sector's sustainable development; thus, strict regulations may be needed to manage the land use policies.

## 1. Introduction

In recent decades, China's hotel industry has experienced tremendous growth. The annual average growth in the number of hotel properties has increased to about 20% over the past 30 years (Gu et al., 2012). Four- and five-star hotel expansion has been particularly significant in the last ten years. The number of starred hotels at the end of 2013 was 11,687, which is 13.7 times more than the number of starred hotels in 1991; however, compared to 1991, there are 121 times more four-star hotels and 35 times more five-star hotels. Interestingly, investments in hotels have been increasing despite oversupply, fiercer competition, and poor financial performance (Heung et al., 2008; Mak, 2008; Pine, 2002; Pine and Phillips, 2005). Although some scholars have been sounding the alarm since the mid-1990s (Gu et al., 2012; Zhang et al., 2006), their warnings seem to have been ignored by hotel developers (Gu, 2003) and policymakers (Bao and Li, 2012) in China. Therefore, it is reasonable to ask what drives rational and profit-pursuing hotel developers to make investment decisions that seem unreasonable. This study provides some answers to this question.

Hotels are deeply embedded in their local and regional conditions (Yang and Cai, 2016). Researchers have attributed the rapid expansion of China's hotel industry to a number of factors, including the fast

growth of the tourism market (Du et al., 2016; Gu et al., 2012; Heung et al., 2008; Zhang et al., 2013), favored policies, increasing per capita GDP, the rising proportion of the population that is non-agricultural, increasing length of highways (Zhang et al., 2013), and government intervention and promotion (Gu et al., 2012). Other researches argue that most recent hotel investment in China is not from the hotel sector, but from other industries, and is primarily a diversification strategy (Park et al., 2017; Wang and Xu, 2011). This last explanation helps to explain the surprising growth seen in both macro and industry perspectives. Since the 1990s, the Chinese economy has been very much associated with land development (Lin, 2009; Zhao et al., 2017); however, the importance of land opportunism in hotel investment, which plays a significant role in the Chinese economy, has not been examined.

Land opportunism underneath hotel investment might be showed in two aspects. First, revenues from the hotel industry are based on both hotel operations and real estate values (Gu et al., 2012; Hara and Eyster, 1990). Second, companies with hotel businesses often receive various benefits from local governments, including favorable land acquisition terms (Wang et al., 2010; Xu et al., 2012). Favorable land acquisition terms may increase the value of an investment. Therefore, ignoring the role of real estate in hotel investments hides the

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**Table 1**  
Land and real estate price in China.

Index	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	MV
PLCP	544	647	759	1037	1211	1524	1888	2441	2600	NA	1581
Speed 1(%)	NA	18.89	17.31	36.57	16.77	25.83	23.90	29.29	6.54	NA	21.89
APRRE	2197	2608	2937	3119	3645	3576	4459	4725	4993	5430	4179
Speed 2(%)	NA	18.71	12.62	6.20	16.86	-1.89	24.69	5.97	5.67	8.75	15.01
PLCP/APRRE (%)	24.78	24.82	25.85	33.25	33.22	42.61	42.34	51.66	52.08	NA	36.73

Note: Per unit land cost of properties firms is named as PLCP (RMB/Square meter), Speed 1 means its rising speed; Average price of residential real estate is named as APRRE (RMB/Square meter), and Speed 2 means its rising speed. MV is mean value. NA is because PLCP data missing in some years. Data is collected and calculated from China Statistical Yearbooks Database.

importance of land opportunism in the Chinese hotel industry.

Local institutional arrangements influence the economic activity in a region (Barca et al., 2012). In the Chinese context, the importance of land, the government's policies for land and real estate, and the maturing security market all provide an interesting environment for a natural experiment. This study illustrates how land opportunism impact firms' hotel investment using a sample of Chinese listed companies that have diversified their business into hotels. Specifically, the study examines whether hotel investment as a diversification strategy improves the net value of a firm's real estate holdings. Then, it investigates whether land opportunism in the Chinese hotel sector enhances firm value. The remainder of the paper proceeds as follows. The next section discusses the previous literature on hotel investment and develops the proposed hypotheses. The subsequent section describes the sample, data, and models, and then presents the empirical results and discussion. The paper concludes with a discussion of the study's limitations and suggestions for future research.

## 2. Literature and hypotheses

### 2.1. Land, real estate, and hotel investment

There have been few studies of the relationships between land, real estate, and hotel investment. Some studies have identified the macro and industry factors that influence multinational hotel investment (Endo, 2006; Guillet et al., 2011; Kristjánssdóttir, 2016; Wang and Xu, 2011; Zhang et al., 2013). Others have explored the links between land and hotel investment. For example, Sadi and Henderson (2001) suggest that reducing land rental rates by about 25% could reduce the capital costs of tourism projects and attract foreign direct investment (FDI) in the hotel and tourism sectors. When estimating the rate of return on hotel investments in three locations in the State of Hawaii in the United States, Cox and Vieth (2003) conclude that increasing the value of land in open areas can help to raise the price of hotel rooms and improve hotel revenues.

Tourism and hotel investment can also affect non-hotel or general real estate investment. Fereidouni and Masron (2011) find that tourism agglomeration had a positive and significant effect on foreign real estate investment (FREI) for selected OECD countries in the 1999–2008 period. Jiménez (2002) uses a two-equation simultaneous model to argue that tourism revenues are a determining factor in residential foreign investment in Spain. These findings reflect the complexity of hotel investments, which have many associated benefits such as integrating land, social, and market resources, attracting more guests to real estate communities, distributing the costs of real estate investment, and improving the image of local real estate, especially if the hotel is a high-star hotel (Hara and Eyster, 1990; Wu and Xu, 2010). Therefore, combining hotel development with general real estate development can be a profitable strategy to lower land costs and may promote the appreciation of land value (Hara and Eyster, 1990).

### 2.2. Chinese context of land, real estate, and hotel investment

In the Chinese context, real estate appreciation and the favorable land acquisition associated with hotel investment have become economically important. In recent years, China has experienced a drastic increase in the price of land and real estate (Wu et al., 2012a,b; Xu et al., 2012; Zhang et al., 2017). The “Notice of Promoting Reform of the Urban Housing System and Accelerating the Construction of Housing,” issued by the State Council in July 1998, brought a historic change to the property market and started modern private real estate development in China. In August 2003, the “Circular on Promoting the Sustained and Healthy Development of the Real Estate Market,” issued by the State Council, further identified the key role of “Properties” in the development of the national economy (Wu et al., 2012a). This revolution in housing commercialization led to a high demand for land for construction and an increase in real estate prices. For example, between 2003 and 2013, the price per unit of land for commercial properties increased at an average rate of 21.89% per year, and the average price of residential real estate increased at an average rate of 15.01% per year (Table 1). In recent years, due to the rapid expansion of urban areas onto agricultural land, the central government has implemented stricter controls on the conversion of agricultural land to construction land (Xu et al., 2012). Ironically, stricter central government policies increase the perception of land scarcity, which drives the value of land higher (Lin, 2009; Xu et al., 2012).

Land has become one of the most precious resources for businesses in China (Lin, 2009). Firms in many industries have tried to hoard land as an important resource (Du and Peiser, 2014). Manufacturing firms even invest their capital in land rather than in industrial or product upgrades (Zeng et al., 2011). A similar phenomenon occurred in Japan in the 1990s, when many securities investors encouraged Japanese hotel investment because of their belief in the significant capital appreciation of land (Hara and Eyster, 1990). Their assessments of company value were heavily focusing on real estate holdings and the chances of getting more reserved land, and somewhat ignored their main business (Hara and Eyster, 1990).

Governments in developing countries favor tourism investment because it was regarded to be effective in poverty alleviation and job creation (Davidson and Sahli, 2015). It is recognized as an effective tool to achieve UN sustainable development goals (UN, 2015). As this is true in China, restrictions on land use are more directly imposed on residential land than on tourism-related commercial land (Xu et al., 2012). Tourism, including hotel investment, has been especially encouraged by the Chinese central government because of its significant role in driving the economic recovery after the global financial crisis in 2008 (Xu et al., 2017). Local governments often perceive a five-star hotel as an indication of a modern city, a hallmark of regional development, or a platform to absorb more investment (Bao, 2014). However, like many other policies, this policy faces the principal-agent problems of opportunism by the policy beneficiaries (Barca et al., 2012), especially as real estate development under the name of tourism is less likely to be scrutinized (Xu et al., 2012).

A high-end hotel development often provides developers with a

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