



Research paper

Risk determinants in the hotel sector: Risk credit in MSMEs

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ABSTRACT

This paper analyses the determinants of credit risk in the Spanish hotel sector, employing panel data models covering a sample of 734 micro, small and medium-sized enterprises (MSMEs) over the period 2005–2011. Among other things, this study is relevant because credit risk is an important variable for several stakeholders. However, the existing literature has neglected the role of location as a determinant of credit risk and has focused on hotel characteristics. This paper analyses both types of variable simultaneously. Overall, the results highlight the importance of the hotel's location as a determinant of its credit risk. Specifically, seasonality, the level of market concentration and the distance to the tourist destination centre have a significant impact on the financial stability of the hotel. Other factors related to hotel characteristics that prove significant are diversification, liquidity, indebtedness, operational efficiency and profitability.

1. Introduction

A company's credit risk significantly affects its various stakeholders, above all its investors, managers and financial institutions. If this risk results in the bankruptcy of the company, the consequences can be very negative for these groups, threatening their profitability and even their survival. Therefore, it is important to analyse the factors that can determine or explain credit risk, with the aim of enabling managers and policymakers to mitigate it. This study is particularly relevant in analysing a sector that exerts considerable influence on the international economy, as is the case with tourism, which has been and continues to be a very important source of resources and employment. According to the World Tourism Organization, the tourism sector represents around 9% of world gross domestic product (GDP) and approximately 30% of world exports of services, it being the main export sector in many countries. In addition, its long-term prospects position it as one of the engines of economic growth in coming years, with the hotel sector playing a very important role because accommodation is one of the main components of tourism spending (IET, 2012).

The objective of this paper is to analyse the determinants of credit risk and thus financial stability in the hotel sector by studying the Spanish market. These determinants consider variables related to hotel characteristics and location. The sample consists of 734 micro, small and medium-sized enterprises (MSMEs) during the period 2005–2011 and contains information on the 97 tourist destinations that represent the entire hotel offer in Spain. This temporal horizon of seven years is

significant because it represents different economic scenarios affecting the hotel industry. Thus, there is a stage of growth in the level of demand (2005–2007), then a stage with a significant drop related to the global economic crisis (2008–2009), and a recovery phase (2010–2011) in the hotel sector. Therefore, the purpose of this empirical study is to enable the decisions of hotel managers and policymakers to adequately consider their impact on the level of credit risk in the hotel sector. In fact, previous literature emphasises the role of hotel managers in credit risk management, but when we delve deeper into the impact of location it can be seen that policymakers could also play a relevant role.

Previous research on financial stability in the hotel sector has focused on equity market risk and has usually concerned hotels in the US (Kim et al., 2012); yet credit risk is also very relevant, as highlighted above. Likewise, the size of the samples analysed has tended to be small and generally studies have considered only quoted hotels, thus not representing most of the companies in the hotel sector, which are small and medium sized and are not publicly traded. Indeed, such hotels represent approximately 90% of the hotel offer in Spain so it is important to provide MSMEs with stable access to finance.

According to Yoshino et al. (2015), bank borrowing is more difficult for riskier MSMEs. Moreover, Yoshino and Taghizadeh-Hesary (2015) indicate that the rating of MSMEs through an efficient credit rating system is very important because it helps banks make more rational decisions to grant financing to these companies and reduce their risk. However, current credit ratings such as Standard and Poor's are focused on large companies, which are used by banks to evaluate their credit

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decisions with respect to these companies. In fact, credit risk analysis firms and institutions have shown increasing concern over recent years in developing specific methodologies for MSMEs. In particular, credit risk analysis firms recognize that they should adjust their methodologies because MSMEs act in different legal, liquidity and competition contexts with respect to large firms. Moreover, [Standard and Poor's \(2014\)](#) recognize that leisure industry, including hotel firms, requires a specific analysis framework to study credit risk. The interest of credit risk analysis firms and policymakers in the development of a specific methodology for MSMEs justify the analysis of credit risk determinants focused on these firms. This research contributes to literature because it uses a large sample of MSMEs (734 hotels), which are representative of the Spanish hotel sector.

A second contribution of this research is related to the determinants of credit risk that are analysed. Although there are studies that underline the importance of location in relation to hotel activity ([Chen and Chang, 2012](#); [Lado-Sestayo et al., 2016](#); [Sainaghi, 2011](#)), previous literature has not evaluated variables related to the location of hotels when studying their financial stability. Moreover, regarding diversification, there is no consensus about its effect on risk in the previous literature. Thus, this paper analyses not only traditional determinants in the literature, such as size, level of leverage, efficiency, profitability and liquidity, but also variables that characterise the location and diversification of the hotel.

Finally, the third contribution is related to the geographic scope of this research, which is Spain. The Spanish tourism sector has a great impact on the national economy. In addition, Spain is one of the top five countries in Europe in terms of international tourist arrivals and has a wide hotel offer ([UNWTO, 2016](#); [Lado-Sestayo et al., 2016](#)). Indeed, according to the Spanish Ministry of Tourism, Spain is one of the most important tourist markets in the world and has a great variety of tourism and tourist destinations (sun and beach tourism, rural tourism, etc.). The Spanish National Statistics Institute indicates that more than 85% of international tourists visited Spain for leisure tourism in 2016. Thus, this research considers information on the 97 tourist destinations that define the entire Spanish hotel offer.

The paper is organized as follows. A review of the related literature is presented in Section 2, while Section 3 presents the empirical analysis. Section 4 explains the results and the paper concludes with Section 5.

2. Related literature and hypotheses

Risk analysis in the tourism sector has focused on equity market risk. Thus, there are studies on systematic risk in hotels ([Kim et al., 2012](#)) and restaurants ([Borde, 1998](#); [Gu and Kim, 1998, 2002](#); [Kim et al., 2007](#)). Regarding non-systematic risk, two studies focusing on the US market are [Gu and Kim \(2003\)](#), which analysed only hotels, and [Hsu and Jang \(2008\)](#), which considered hotels and restaurants. Similarly, in the Chinese context, [Chen \(2013\)](#) evaluated the determinants of systematic and non-systematic risk in the Chinese hotel sector.

Although the study of risk from this perspective is important, it is also necessary to study credit risk in the hotel sector. As indicated above, the financial stability of a hotel affects various stakeholders, not just managers and shareholders (who are most affected by equity market risk). Investors, banks, workers, suppliers and institutions, among others, also have an interest in a company that manages its credit risk properly and does not result in bankruptcy. In general, a dynamic hotel sector made up of active and financially healthy companies is important for the real economy of a country.

The study of credit risk should consider two key variables, namely the location and the diversification of the hotel. Location as a variable can be highly relevant in evaluating a hotel's credit risk because, as [Bull \(1994\)](#) indicates, hotel services can only be consumed at a specific place and time. In this regard, there are three theories that study different dimensions of location and consider geographic factors, factors related to the existence of agglomeration economies and factors related to the

competitive environment ([Yang et al., 2014](#)).

From the point of view of geography, the proximity (or accessibility) of the hotel to points of tourist interest (centrality) relates to the existence of space monopolies, which can significantly affect a hotel's financial stability ([Sainaghi, 2011](#)). Previous studies consider the city centre as a relevant place because there are a large number of tourist attractions there ([Lado-Sestayo et al., 2017](#)). This confirms the importance of the location for leisure, urban and business hotels ([Sainaghi and Baggio, 2014](#)). This proposition is based on the model of Egan and Nield (2000), which postulates a concentric spatial distribution of US hotels in relation to the city centre. Also, the greater number of hotels in the city centre generates economies of agglomeration. Previous literature has indicated that there is a positive relationship between agglomeration and profitability, which could affect the stability of business results and consequently financial stability ([Canina et al., 2005](#)). In sum, centrality can contribute to a lower level of credit risk.

In relation to the competitive environment, the structure–conduct–performance (SCP) paradigm developed by [Mason \(1939, 1949\)](#) and [Bain \(1951, 1956\)](#) stands out. According to these authors, the market structure reflects the behaviour of competitors in such a way that a high market concentration generates collusive behaviours. Thus, hotels located in concentrated markets will earn higher and more stable incomes, reducing their credit risk ([Lado-Sestayo et al., 2016](#)). The relationship between market concentration and financial stability has been studied in the financial sector. In this context, the competition–fragility hypothesis has been proposed. Consistent with [Hellmann et al., \(2000\)](#) and [Allen and Gale \(2004\)](#), this approach indicates that the benefits associated with collusive markets allow companies to assume lower risks and retain profits. In contrast, due to the lower profitability obtained in competitive environments, companies will be willing to assume a greater risk if they thus obtain increases in their profitability. Several studies have confirmed this hypothesis in the financial sector, such as those of [Jiménez et al. \(2010\)](#), [Dick \(2006\)](#), [Beck \(2008\)](#) and [Berger et al. \(2009\)](#), but there is no empirical evidence for it in the hotel sector.

Seasonality is another relevant factor that should be considered in the study of credit risk. Some authors suggest that seasonality may contribute to a price increase when there is a high level of demand but may also have an impact on the probability of hotel bankruptcy ([Lado-Sestayo et al., 2016](#); [Cuccia and Rizzo, 2011](#); [Sainaghi, 2010](#)). In particular, seasonality can generate a reduction in profitability because the sector has high fixed costs even when the level of demand is low. Consequently, seasonality makes it difficult to manage staff and assets when the hotel manager wants to adjust them to the level of demand that exists in each period ([Karamustafa and Ulama, 2010](#); [Ashworth and Thomas, 1999](#)). From the investors' point of view, [Butler \(2001\)](#) indicates that seasonality is an obstacle to obtaining financing in the hotel sector. In fact, [Park \(2013\)](#) finds that investors overreact to seasonality in the hotel sector. In short, seasonality can negatively influence financial stability in the hotel sector ([Ganguin and Bilardello, 2005](#)).

Thus, it is important to analyse these factors related to location when studying credit risk in the hotel sector. Therefore, the following hypotheses are investigated:

- H1.** Hotels near the tourist destination centre have a lower credit risk.
- H2.** Hotels that operate in tourist destinations with low market concentration (high level of competition) have a higher credit risk.
- H3.** Hotels operating in more seasonal markets have a higher credit risk.

The hotel business model can also influence financial stability. In particular, hotels can increase their diversification to seek synergies and reduce their level of credit risk. However, there is no consensus on the effect of diversification on the level of risk in the previous literature ([Cheng and Chang, 2012](#)). On the one hand, [Bowman \(1980\)](#) argues that diversified companies achieve higher performance because they

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