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Is more better? The relationship between meeting space capacity and hotel operating performance

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HIGHLIGHTS

- The association between meeting space capacity and hotel operating performance is investigated.
- RBV of the firm and competitive advantage concepts are used as the theoretical foundation.
- A large national database is used to test the hypothesis, and models are estimated via two-way cluster regression.
- Three industry-specific operating performance measures are used: Occupancy rate, ADR, and RevPAR.
- Findings demonstrate a curvilinear relationship between meeting space capacity and hotel-operating performance.

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ABSTRACT

This study examines the effect of meeting space capacity on hotel operating performance. We use Resource-Based View (RBV) of the firm as the theoretical foundation. We employ a national-level dataset with more than 20,000 hotels in the United States for the 2007–2012 period. We find that meeting space has a non-linear effect on hotel operating performance. That is, at low levels of meeting space, meeting space capacity is negatively related to hotel operating performance. At high levels of meeting space, meeting space capacity has a positive influence on operating performance. These findings provide insights for hotel owners, developers and practitioners in planning hotel meeting space capacity.

1. Introduction

Meeting spaces, along with food and beverage outlets, can be said to be one of the major demand generators for hotels. This is particularly true for hotels that aim to attract group business, given its stable nature relative to transient hotel guest patronage. In 2012, 1.8 million conventions, conferences, congresses, trade shows and exhibitions, incentive events and corporate/business meetings were attended by approximately 225 million attendees in the U.S. (PricewaterhouseCoopers, 2012). In recent years, full-service hotels have been the primary beneficiaries of this unprecedented increase in the size and volume of meeting, incentive, convention and exhibition (MICE) business. Hotels have joined forces with city councils, visitor bureaus, and tour companies in hosting major meetings and conventions, as they recognize the direct advantages of these gatherings. Hotels achieve these economic gains by booking a higher number of rooms and by generating greater revenues from other sources, such as food and beverage, spa, golf, and parking services. In this respect, the size and proper utilization of meeting space capacities serves as a potential driver of incremental room revenue for hotels.

Literature pertaining to MICE business employs a macro-scale perspective of the benefits of meetings and events. That is, previous studies investigate either the economic significance of such meetings and conventions for host destinations (Baloglu & Love, 2005; Boo & Kim, 2010; Chen, 2006; Davidson, 2003; Eisinger, 2000) or site selection criteria for meetings and conventions (Chacko & Fenich, 2000; Clark & McCleary, 1995; Zelinsky, 1994). However, the MICE literature has not explored micro-level effects of

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meetings and events on individual hotel performance. More specifically, whether hotels with extensive meeting facilities derive substantial economic benefits by charging higher room rates or by generating greater revenue per available room (RevPAR) compared to other hotels remains unclear. This is a critical question facing existing and prospective hotel managers, developers and investors, who often attempt to determine whether meeting facilities should be built during the planning stages of a prospective hotel. If the answer is affirmative, involved parties ask the following questions: How much physical space should be allocated to these meeting facilities? Do hotels with more meeting space perform better?

We set out to answer this question by examining the relationship between the meeting space capacity and operating performance of individual hotel properties. Our work departs from previous research streams, which largely examine macro-level contributions of MICE business outcomes on local economies. Rather, we focus on the operating performance of individual hotels that offer meeting and convention spaces to their guests. In particular, we examine the impact of property-level meeting/function space capacity on hotel occupancy levels, average daily rates (ADRs) and RevPAR. In this regard, we offer a more fine-grained explanation of how meeting space availability influences operating performance at the property level. We test our arguments through the lens of resource-based theory and based on the concept of competitive advantage. Thus, this study contributes to extant tourism literature by showing how internal resources, such as meeting spaces, affect the operating performance of hotels.

Our findings imply that the use of more meeting spaces is not necessarily desirable. Employing a large national-scale dataset, we find evidence of a convex curvilinear association between meeting space capacity and hotel operating performance. More precisely, we find that increasing meeting space capacity levels has a negative effect on hotel operating performance to a certain extent. Only after passing a certain threshold does meeting space capacity help hotels realize higher room revenue, occupancy, and ADRs. This finding constitutes a critical consideration for hotel developers and owners who are determining whether to invest in the construction of meeting/function spaces either upfront during the initial hotel construction phase or in later expansion/renovation stages. Investors must be aware that when meeting spaces are insufficient, the anticipated performance enhancements may hinder hotel operating performance.

2. Literature review and hypotheses

This section reviews key theoretical arguments that help explain the effect of meeting space capacity levels on hotel operating performance. We also provide reasoning for why meeting space emerges as an important internal company resource that helps businesses achieve a competitive advantage. We close this section by positing our core hypothesis.

2.1. Resource-based view (RBV) and meeting space capacity

In a seminal paper, Penrose (1959) contended that firms grow both internally and externally. That is, the success of external growth strategies, such as mergers, acquisitions and diversification, depends on the exploitation of resources within a firm. She further argued that a firm is composed of 'productive resources' and recommended that firms may use these resources to gain a competitive advantage only if valuable services provided through these resources are accessible to firms. Later, Rubin (1973) contributed to the RBV of firms by contending that access to resources is not sufficient in exclusivity. Rather, firms must process their raw resources to make them useful. Building on these arguments, Wernerfelt (1984) noted that firms could yield above-average returns by detecting and securing resources that are critical to the emergence of products demanded by consumers. These pioneering attempts to formulize the significance of firm resources in gaining a competitive advantage were limited to theoretical presumptions. Barney (1991) synthesized prior evidence into a comprehensive framework of the RBV of firms that relies on two major assumptions. First, the RBV assumes that firms in an industry may be heterogenous due to the unique resources they possess. Second, these resources may not be perfectly mobile, and thus, the acquired competitive advantage can be sustained for a long time (Barney, 1991). In light of these theoretical underpinnings of the RBV, we attempt to explain how it enhances our understanding of a major internal resource (i.e., meeting space) that serves as a critical success factor in creating a sustainable competitive advantage in the context of the tourism industry.

Meeting space capacity emerges as a valuable organizational resource that is presumed to help hotel companies generate superior performance relative to their competition. The decision to build meeting spaces on hotel property is closely related to the type of business a hotel caters to, the overall firm strategy and competition in the market. Therefore, attracting meeting business to a given property could prove highly desirable if gains associated with meeting business outweigh the costs of meeting space installation, maintenance and operations. Meeting business gains may include direct revenues, such as function space rental fees and food and beverage (F&B) revenues, as well as indirect revenues, such as rooms booked by meeting/conference attendees. The latter measure is indeed a derived demand, as not all meeting/conference attendees require overnight accommodations. However, a large majority of meeting/conference events last several days, thus serving as a substantial source of business for hotels. Indeed, hotel operators are primarily drawn to meeting/convention business services for room sales revenues because proceeds from room sales exceed direct revenues from meeting space rental fees and F&B sales (Fenich, 1998). In addition, most hotels do not charge for the use of meeting space as long as convention/meeting attendees book several hotel rooms. Therefore, what operators lose in free meeting space rentals is compensated by higher room rates and "guaranteed" banquet and F&B sales from meeting planners. Indeed, recent reports show that room rates are only the sixth most important criteria for meeting planners when selecting hotel venues (Mandelbaum, 2013), whereas the same study indicates that meeting space availability remains the most important factor.

2.2. Meeting space capacity and performance

Thus far, the existing body of knowledge pertaining to MICE business does not focus on the relationship between the meeting/function space capacity of individual hotel properties and their respective operating performance levels (i.e., occupancy rate, ADR, and RevPAR). Employing resource-based perspectives, we propose that hotel firms could utilize their available meeting/function space capacities to enhance their financial performance by attracting more group business and thus attaining higher occupancy levels. Closely associated with occupancy levels, we also expect that successful meeting space marketing will improve the hotel pricing power levels (i.e., higher ADR), which will in turn lead to an increase in RevPAR. We predict an overall positive influence of meeting space on RevPAR partially because meeting/convention business events occur over several days. As hotels achieve high occupancy rates by offering room blocks to conference attendees, transient guests may need to pay a premium if they wish to stay in the same hotel during the conference period. The following example may illustrate this situation. A 300-room hotel may offer a