

## What Determines Foreign Hotels' Investment Location Choice in China?

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### Abstract

*This study aims to investigate influence factors of the foreign hotels' location choice by a conditional logit model. Here 826 budget foreign hotels and 801 superior foreign hotels in China from 2000 to 2015 are taken as samples to study the determinants of their location choice. Results show that location factors, the level of tourism development and the hotel business environment have significant influence on the foreign hotels' location choice. Additionally, by examining location models for different levels of hotels, the influence of these three factors on location choice of the budget and superior foreign hotels are proved to be different. This result is helpful to explain the different location distribution of budget foreign hotels and superior foreign hotels, moreover, it can be used to as a guide for the local government to adjust their economic policies to allure foreign hotels and thus improve the development of their tourist industry.*

**Keywords:** Location choice; Multinational hotel groups; China hotel development; budget hotels and superior hotels

### 1. Introduction

As an important part of the three pillars of tourism, the hotel is an important foundation and characteristic attraction for the development of tourism in the region and country. According to China residential industry development report, in 2016, the number of foreign hotels in China increased by 83 times compared with 1978, and the number of beds increased by more than 90 times, satisfying the huge market demand of 139 million inbound tourism and 5.01 billion domestic tourism. With the continuous development of economic globalization and the vigorous development of tourism, global expansion has become an inevitable choice for hotel companies to realize their own development. The rapid development of China's tourism industry has expanded the demand for the hotel accommodation industry, and China has become an important market for foreign hotels' expansion. On the one hand, the investment of foreign hotels has a certain spillover effect on the local hotel industry, and can fuel local economic growth and improve employment opportunities. On the other hand, the distribution of foreign hotels in the province-level regions of China's expansion is seriously unbalanced and adversely affects the coordinated development of the national economy. Therefore, it is helpful to study the distribution characteristics and influence factors of foreign-funded hotels' location choice in China.

### 2. Literature review

In the process of rapid overseas expansion of foreign hotels, location is widely recognized as one of the most important features of hotels. Literatures on this field mainly focus on two aspects: one is location choice from global perspective; the other is from a certain national or regional perspective. Firstly, from the global perspective, the factors affecting the location choice of hotels are summarized as: the total amount of OFDI in the host country, GDP, GDP per capita, investment environment, total tourism revenue and per capita disposable income. Adam, I, Amuquandoh, F.E (2014) and Li, M., Fang (2015) believe that the host country's transportation facilities, laws and regulations, social culture and other location factors affect the hotel owner's location decision. Adam (2014) and Chung (2001) proposed that the agglomeration economy has a significant impact on hotels' location choices.

In addition to the factors related to the host country, Du Jiang(2006) believes that the location characteristics of the home country impact location choice of hotels, such as: economic development level, relevant policy measures, tourism development level, market demand, domestic outbound tourism trends, etc. The above-mentioned literatures are all from a global perspective to study the influence of regional differences between countries on the choice of hotel location. Although the perspective is different from this paper, it also has important reference value for provincial location research.

Secondly, from a certain national or regional perspective. Daniel Puciato (2016) studied the influence of the attraction of Polish cities on the location choice of chain hotels. It finds that the following factors are important for investors: land prices, economic development level, level of internationalization and urbanization. Ruben Lado-Sestayo (2016), by studying the distribution of the hotels in Spain, finds that the regional market demand level, market structure, and market entry barriers have an important impact on the location choice of hotel investors. The above is mainly to analyze the location distribution of hotels from the perspective of other countries; China's economic development status and location characteristics are very different from other countries. Some scholars from China try to analyze the location characteristics and influence factors when foreign hotels enter into the Chinese market. He Canfei (2010) analyzed the regional distribution of foreign star-rated hotels in 26 cities of China, and believed that foreign star-rated hotels tend to follow foreign customers, and at the same time gain cost savings and competitiveness through the integration with domestic hotels. Hanqin Qiu Zhang (2012) Chen Liying (2015) and other scholars study the distribution characteristics of foreign hotels in China's three major economic sectors: eastern, central and western, and summarize the market factors, business environment factors and major event factors affecting the choice of hotels' location.

At present, in the study of location choice behavior of foreign hotels in China, some scholars divide China into three major economic sectors for research, and some scholars only study some specific cities in China. This paper believes that these region divisions are too monotonous, lacking a comprehensive analysis of all provinces and cities in China, and cannot accurately describe the regional distribution characteristics and influencing factors of foreign hotels in China. Therefore, this paper searches the hotel group's official website and CTRIP website one by one, collects the distribution data of foreign hotels in 31 provinces and cities in China from 2000 to 2015, conducts empirical analysis on the location choice behavior of foreign hotels, and comprehensively explores the characteristics and influencing factors of foreign hotels' location choice in China's provincial areas. Furthermore, this paper finds that the expansion trend of budget foreign hotels and superior foreign hotels in China is significantly different. Then, we compare and analyze the influencing factors of the two types of foreign hotels in China by splitting the sample.

### **3. Methodology**

#### **3.1 Data collection**

China Hotel Chain Development and Investment Report2016 announced the top 30 foreign hotel brands in 2016. The top 30 foreign hotel brands are subordinate to 12 multinational hotel groups, namely Wyndham Hotel Group and Inter-Continental. Starwood Hotels & Resorts Worldwide, InterContinental Hotels Group, Shangri-La Hotels and Resorts, Hilton Hotels, Accor Hotels, Marriott, Best Western International, Carlson Hotels Worldwide, Kempinski Hotel, and Nikko Hotels Group. This paper research the 1,627 hotels operated by the 12 multinational hotel groups in China from 2000 to 2015 to study their location selection behaviour in the provincial level of China.

The hotel industry data comes from the official website of 12 multinational hotel groups. After identifying the specific member hotels, the Ctrip website will be used to check the opening time and specific location of the hotel one by one, and then analyze the location choice of each hotel. The hotel industry data covers all brand hotels under the 12 hotel groups. According to the number of services, management level, equipment and facilities, service quality and other factors of each brand hotel, and referring to the Ctrip website classification, 1627 hotels are divided into two categories: Super 8 and Ibis Hotel are classified as budget hotels (826); other international hotel brands are classified as superior hotels (801).

#### **3.2 Characteristics of foreign hotels 'regional distribution**

##### **(1) Overall foreign hotels**

The internationalization of hotel companies began after the Second World War. Foreign famous hotel companies generally adopted the international development strategy. In the 1980s, foreign hotel companies began to enter the Chinese market. After exploration, slow growth, stable expansion, and stagnation, it has entered the stage of Comprehensive expansion since 2000.

Figure 1 shows the location distribution of hotels established by foreign hotels in various provinces and cities in China, which are the provincial distribution of all foreign hotels in 2010 (a) and 2015 (b). From the comparison of the two figures, it can be clearly seen the rapid expansion of foreign-funded hotels in China in recent years, and obvious location characteristics of this expansion. Firstly, as of 2010, foreign hotels are concentrated in coastal provinces and Sichuan provinces with developed tourism. Secondly, from the distribution map of foreign hotels in 2015 (Fig. 1b), it can be seen that while developing provinces with high economic development levels, foreign-funded hotels are expanding to other second- tier and third-tier cities, especially the tourist cities with sunlight, beaches and oceans such as Hainan, Shandong, and Liaoning.

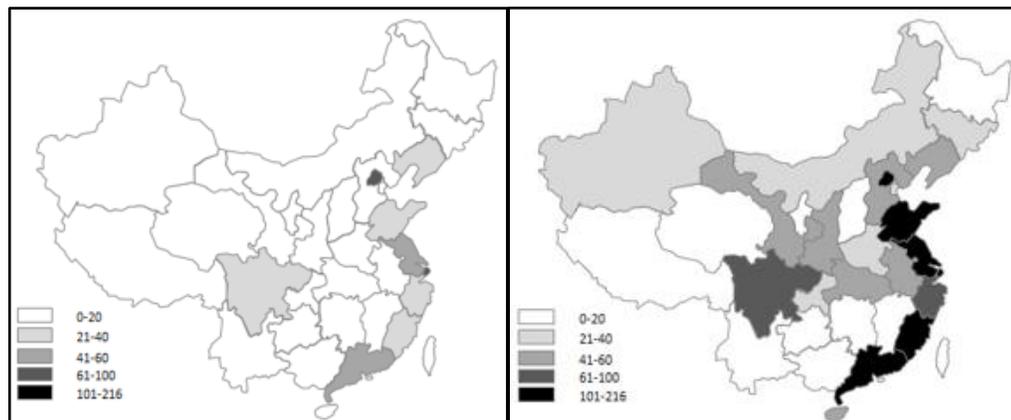


Fig.1a Fig.1b

Fig.1 The provincial distribution of foreign hotels in 2010 (a) and 2015 (b)

Data Sources : China Tourism Statistics Yearbook

(2) Budget foreign hotels and superior foreign hotels

Based on the data of new-built foreign budget hotels and superior foreign hotels from 2006 to 2010 and 2011 to 2015, the distribution maps are as follows (Fig. 2, Fig. 3).

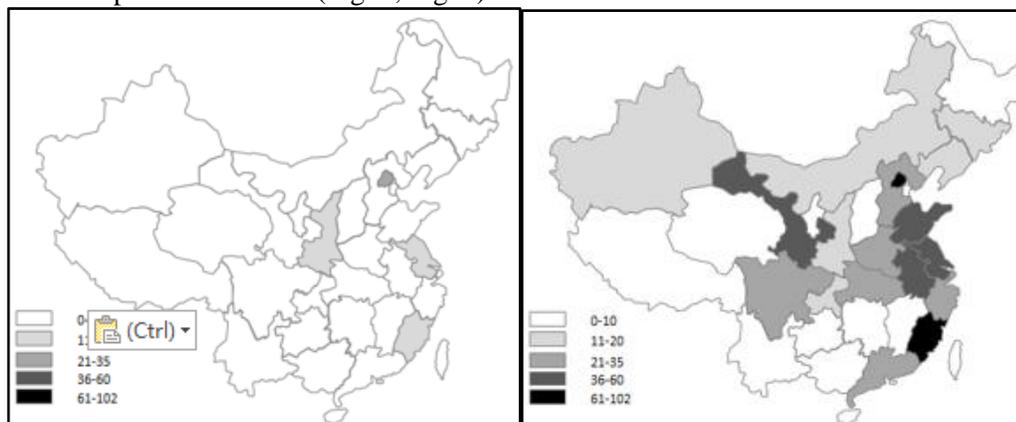


Fig.2a Fig.2b

Fig.2 The provincial distribution of new-built budget foreign hotels in 2006~2010 (a) / 2011~2015 (b)

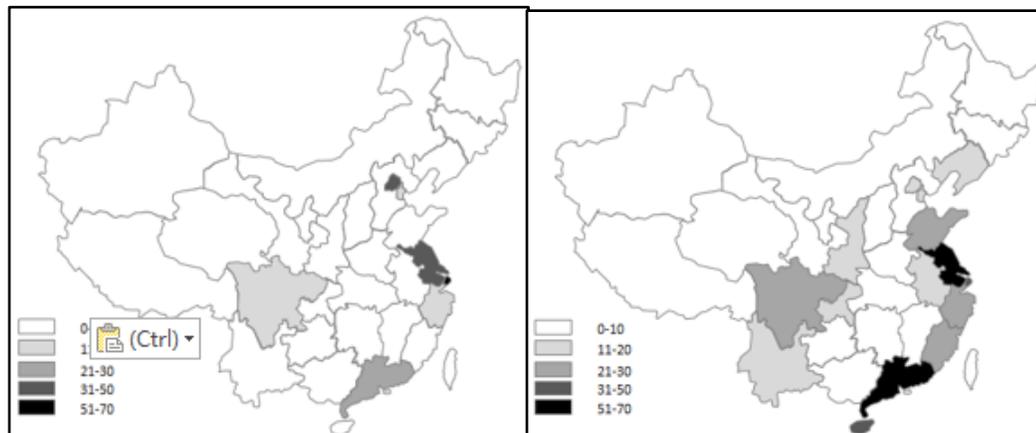


Fig.3a Fig.3b

**Fig.2 The provincial distribution of new-built superior foreign hotels in 2006~2010 (a) / 2011~2015 (b)**

From the above figures we can clearly see the difference in the expansion trend of the two types of hotels. The superior hotel market in developed regions tends to be saturated. In the past few years, superior hotels have invested heavily in provinces that are underdeveloped but with rapid tourism development. The number of new-built foreign hotels in the highly developed provinces is showing a downward trend (Fig. 3a, Fig. 3b), especially in Shanghai and Beijing. Budget foreign hotels continue to expand into other provinces while expanding to highly developed regions (Figure 2a, Figure 2b).

The difference in the expansion trend of budget foreign hotels and superior foreign hotels in China is worthy of a comparative study of the factors affecting the location choice of the two types of hotels.

### 3.3 Theoretical assumptions and variable selection

Based on previous research, this paper attempts to classify the influencing factors affecting the location selection of foreign hotels in China's provincial areas as the local location factor, the level of tourism development and the hotel operating environment. The specific explanatory variables and definitions are shown in Table 1.

**Table 1 Influential factors indicators of foreign hotels' location choice in China**

Influencing factor	Variable name	Variable interpretation
Local location factor	GDP	Regional Gross National Product (Ln)
	Per capita GDP	Per capita regional Gross National Product (Ln)
	Urbanization level	The proportion of urban population
	FDI	FDI (Ln)
	International trade	Regional international trade volume (Ln)
	Industrial structure	Third industry accounts for GDP share
The level of tourism development	The number of inbound tourists	Number of inbound tourists (Ln)
	Inbound tourists' consumption expenditure	Daily average spending per inbound tourists (Ln)
The hotel operating environment	Number of star-rated hotels	The number of regional star-rated hotels (Ln)
	Star-rated hotel occupancy rate	Average occupancy rate of regional star-rated hotels
	Labor wage	Average wage level of residential labor (Ln)

#### (1) Local location factors

Existing research indicates that the location choice of foreign hotels is preferred to countries and regions with high levels of economic development. GDP and per capita GDP of 31 provinces and cities are selected as explanatory variables to measure the level of regional economic development in this paper. Yuan Bo (2014), Fuxin (2015) and other scholars have found that the location choice of FDI has a certain relationship with the level of urbanization in the host country or region. This paper uses the proportion of urban population in the total population to measure the level of urbanization.

Judging from the expansion trend of foreign hotels in China, hotels may be located in areas with close external links. Areas with high internationalization may reduce barriers to entry for foreign hotels and provide more business customers for hotels. Based on this, this paper uses regional foreign direct investment and international trade to measure the degree of regional external relations.

A large number of studies have found that the introduction of FDI will improve the industrial structure of the region and contribute to the proportion of the tertiary industry in the economy, and the optimization of industrial structure provides a better investment environment for the service industry. This paper introduces industrial structure variables as explanatory variables.

(2) The level of tourism development

The level of regional tourism development determines the number of tourists, which in turn determines the source market of foreign hotels. The number of regional inbound tourists and inbound tourists' consumption expenditure are used to measure the level of tourism development in the region in this paper.

(3) The hotel operating environment

The agglomeration economy will affect the location choice of foreign hotels. On the one hand, the major competition in the hotel sector with similar standards may limit the possibility of future profits of commercial entities; on the other hand, it can bring economic benefits brought by agglomeration, the supply level and competitive environment of hotel market will also affect the location choice of foreign hotels. The regional labor wage level of this industry not only affects the operating cost of foreign hotels, but also reflects the quality of local labor. Based on this, this paper introduces three explanatory variables, the number of regional star-rated hotels, average occupancy rate of regional star-rated hotel, and the average wage level of residential labor.

Among them, the relevant variables of local economic development level and workers' wages are derived from the China Statistical Yearbook from 2001 to 2016, and other variables are derived from China Tourism Statistics from 2001 to 2016. Yearbook.

**4. Empirical results**

This paper uses the conditional logit model with STATA software for empirical analysis. Table 2 lists the empirical estimates of all foreign hotels, superior foreign hotels, and budget foreign hotels.

**Table 2 Conditional log it model estimation results**

Variable name	Overall foreign hotels	Superior foreign hotels	Budget foreign hotels
GDP	-0.37	-2.58**	3.05**
Per capita GDP	0.21	-1.36	2.67**
Urbanization level	0.14**	-2.02*	0.18
FDI	5.51***	5.78***	0.61
International trade	0.37	1.11	0.15
Industrial structure	2.41**	0.29	2.86**
The number of inbound tourists	3.22***	2.80**	6.96***
Inbound tourists' consumption expenditure	2.17**	1.83***	1.93*
Number of star-rated hotels	4.89***	0.02*	6.36***
Star-rated hotel occupancy rate	0.13*	2.32	0.51
Labor wage	4.91***	4.51***	0.20
Sample size	50188	24615	25573
LR chi2 (10)	1034.18	644.19	525.38
Prob>chi2	0.00	0.00	0.00
Log	-5058.36	-2408.99	-2570.28
Pseudo R2	0.09	0.12	0.09

Note: \* indicates a 10% significance level, \*\* indicates a 5% significance level, and \*\*\* indicates a 1% significance level.

4.1 Analysis of the results of overall foreign hotels

From the empirical results of overall foreign hotels, the following can be seen: Firstly, the empirical results of the three explanatory variables of GDP (X1), GDP per capita (X2), and international trade (X5) are not significant, but this does not indicate Regional Gross National Product and the level of international trade have no effect on

the location choice of foreign hotels, but the effect on all foreign-funded hotels is not obvious under the provincial-level regional distinction in China.

Secondly, the level of urbanization (X3), FDI (X4) and industrial structure (X6) are significantly correlated and consistent with expectations. This shows that foreign hotels believe that high levels of urbanization, high degree of internationalization and high level of tertiary industry structure can bring more market opportunities and customers.

Two variables of tourism development level, the number of inbound tourists (X7) and the inbound tourists' consumption expenditure (X8) all passed the significance test, and the coefficient is positive, which proves that foreign hotels favor the developed tourism regions. The main target markets of multinational hotels are commercial tourists and leisure holiday tourists. Inbound tourists have a high awareness of foreign brands, and they prefer to choose well-known foreign hotels compared to local hotels in China. Cities with developed tourism, more floating population, increase demand for hotels, foreign hotels will have a better business environment.

From the perspective of operating environment, the following can be seen: firstly, the number of existing star-rated hotels (X9) is high in level of empirical significance, and the correlation coefficient is positive. This shows that the role of agglomeration economy will affect the decision-making of location choice of foreign hotels. When foreign hotels choose provincial-level locations in China, they will tend to choose areas with high concentration of hotels.

Secondly, the local star hotel occupancy rate (X10) has a low level of significance, indicating that the occupancy rate of existing hotels has less impact on the location choice of foreign hotels. Labor wage (X11) are positively related to hotel investment decisions. Although the higher the wages of workers, the higher the operating costs for hotels, the foreign hotels still choose to invest in areas with high wages, indicating that the hotel industry has higher requirements for workers' labor levels, willing to sacrifice a small amount of profit to pursue a higher quality workforce.

#### **4.2 Comparison of results between superior foreign hotels and budget foreign hotels**

In this paper, the total 1,627 foreign hotel sare divides into 801 superior foreign hotels and 826 budget foreign hotels. The empirical results show that there is a significant difference in the intensity of the explanatory variables for different types of location choice. Among them, the number of inbound tourists (X7) has similar results for the two types of hotels, indicating that the number of inbound tourists in the region has generally promoted the introduction of foreign hotels. By comprehensively comparing the empirical results, the following differences can be seen:

Firstly, among the location factors, the results of GDP (X1) are significant in superior and budget hotels, but the correlation coefficient is reversed. This result is different from the previous research results for hotels, but it is reflected the current distribution trend of foreign hotels in China (Fig. 2, Fig. 3). The location choice of superior foreign hotels pay more attention to the FDI (X4) . The closer the regional contacts are, the higher the degree of internationalization, and the greater the attraction to superior foreign hotels. Budget foreign hotels prefer the regional industrial structure level (X5), and the higher the proportion of the tertiary industry in the region, the greater the market potential.

Secondly, the level of tourism development, the number of inbound tourists (X7) and the consumption expenditure of inbound tourists (X8) have a significant positive effect on the location choice of the two hotels, while the level of inbound tourists consumes has a greater intensity of the location choice of superior foreign hotels.

Thirdly, the hotel operating environment, through the comparison of the number of star hotels (X9) and labor wage (X11), we can find that the location choice behavior of budget foreign hotels has a more significant agglomeration effect, while superior foreign hotels' investment has a higher demand for the quality of the destination workforce.

#### **5. Discussion and conclusion**

This paper takes the provincial-level regional location choice of foreign hotels in China from 2000 to 2015 as the research object, and examines the influence of location factors, tourism development level and hotel business environment. Furthermore, it compares superior foreign hotels and budget foreign hotels. The conclusions are as follows:

- (1) The location choice of foreign hotel enterprises in China's provincial-level regional investment is affected by the level of regional development and the level of external relations. The closer the external relations, the more likely foreign-invested companies are to invest in them. The impact of regional economic development level on the location choice of foreign hotels is related to the type of hotels. On the one hand, superior foreign hotels started earlier, and the markets of superior hotels in developed regions have become saturated. In order to seek more potential markets, they have turned to less developed provinces or cities. On the other hand, budget hotels are booming and provinces and cities with high levels of economic development can provide a better business environment. This is also a reasonable location choice behavior adopted by hotel companies to adapt to different market conditions.
- (2) The location choice of foreign hotels in China's provincial-level regional investment is affected by the development level of regional tourism development. The more developed the regional tourism industry, the greater the possibility of foreign-funded hotel companies investing in the province.
- (3) The choice of foreign hotels in China is affected by the concentration of local industry. The more hotels there are, the more foreign hotels may choose to invest in the area. On the one hand, the similarity of services provided by enterprises makes it easier for newly-entered enterprises to obtain legality. On the other hand, the successful investment experience of original hotel companies will attract more hotel industry.

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