An Investigation of the Relationship between Service Quality and Profitability in UK Budget Hotels

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by

Dia Zeglat
PhD Candidate
School of Management
University of Surrey
Guildford, GU2 7XH
Email: d.zaglet@surrey.ac.uk
Tel: +44 (0) 7908666165
Fax: +44 (0) 1483689511

Yuksel Ekinci (PhD)
Senior Lecturer in Hospitality Management
School of Management
University of Surrey
Email: y.ekinci@surrey.ac.uk

Andrew Lockwood (PhD)
Forte Professor of Management
School of Management
University of Surrey
Email: A.Lockwood@surrey.ac.uk
Abstract

Conceptual studies indicate that improved quality will have a positive impact on business performance. A number of empirical studies have attempted to examine the relationship between quality and business performance, for example, the Profit Impact Marketing Strategy (PIMS) project, which investigated the impact of quality, market share, productivity and price on financial performance (Buzzel and Gale, 1987; Brennan et al 2003). Drawing conclusions from 43 case studies, past experiments and opinion surveys, Hardie (1998) suggests that service quality will influence some intermediate variables of which later will have affect the firm’s performance and profitability. Although the number of studies on business performance has increased, the outcome of the empirical studies has so far produced mixed results on the relationship between business performance and service quality. Some of the empirical studies have shown a positive relationship between service quality and financial business performance, while others found no relationship or even a negative relationship. Despite the long term interest in the relationship between service quality and financial performance, the impact of quality on business performance seems to be weak, indirect or more complicated than has been proposed. Hence the direction and nature of the relationship between these two concepts continues to be debatable (Babakus et al., 2004; Zeithaml, 2000).

The purpose of this study is to investigate the nature of the relationship between service quality and profitability in UK budget hotels. To do so, the first part of the paper reviews the literature concerning the theories linking service quality and business performance. The second part develops a research model which suggests that service quality has a positive and indirect relationship with profitability via customer satisfaction, customer retention, productivity, market share and premium price. The third part of the paper examines the direct and indirect relationships between service quality and financial performance from the hotel managers’ perspective. The primary data were collected from a leading budget hotel chain in the UK. A self administered questionnaire was sent to 477 hotel managers and, of these, 208 usable questionnaires were returned. Findings of the structural equation modelling showed some significant relationships between service quality, mediating variables such as customer retention and financial business performance indicators such as Return on Capital Employed (ROCE) and market share. The final part of the paper presents the conclusions of the study; the managerial implications and recommendations for future research.
References


