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

by

Dia Zeglat

Thesis submitted in part fulfilment of the requirements for the award of Doctor of Philosophy
2008
Abstract

The purpose of this study is to examine the nature of the relationship between service quality and profitability in the UK budget hotel sector, by developing and testing a conceptual framework which suggests that service quality has a positive and indirect impact on profitability via customer satisfaction, customer retention, productivity, market share and premium price. This study collected three sets of data. The first data set was qualitative, obtained from four hotel managers using in-depth interviews; the respondents were invited to evaluate the research model. The second data set was secondary, Hotel Performance Data collected from 182 hotel units of a leading budget hotel chain in the UK. The third data set was quantitative, collected from 477 general managers of units operated and located across the UK, from the same budget hotel chain.

The managers who participated in the qualitative study generally supported the research model and research hypotheses developed. The key finding from the secondary data set was that there is no direct influence from service quality on profitability. This data set further revealed that profitability is positively influenced by sales growth, as a consequence of customer retention, and negatively influenced by premium price.

For the quantitative data set, exploratory factor analysis (EFA) supported the two dimensions of service quality (physical service quality, and staff behaviour and attitude). For the managing demand and capacity scale, (EFA) indicates a four factor solution. Looking at the scale reliabilities, the results approved the two dimensional scale of service quality, while the managing demand and capacity scale showed poor values for all dimensions extracted except the first dimension (controlling guest’s usage).

The findings from the quantitative data set (General Manager’s Perspective) confirmed the indirect impact of service quality on profitability. The findings from the general managers’ data set suggest that that service quality improves profitability through the customer behavioural response direction, which implies satisfying the current customers and retaining them as well as attracting new customers and guests in order to improve market share and revenues. All analyses undertaken in this study concluded that service quality has an indirect and positive impact on profitability in the UK budget hotel sector through customer response. Theoretical and empirical contributions were made based on the results of this study.
Table of Contents

| Title Page | I |
| Abstract | II |
| Table of Contents | III |
| List of Tables | IX |
| List of Figures | XII |
| Acknowledgement | XIV |

Chapter 1 Introduction ................................................................. 1
  1.1 Background of the Study .................................................... 2
  1.2 Purpose of the Study ........................................................... 3
  1.3 Objectives of the Study ....................................................... 3
  1.4 Structure of the Study ....................................................... 4

Chapter 2 The UK Budget Hotel Sector ........................................ 7
  2.1 Introduction ........................................................................ 8
  2.2 Definition of a Hotel .......................................................... 8
  2.3 Classifications of Hotels .................................................... 9
    2.3.1 Quality of Facilities and Services ................................ 10
    2.3.2 Target Market ............................................................. 10
    2.3.3 Ownership and Affiliation .......................................... 10
    2.3.4 Comparative Statistics .............................................. 11
    2.3.5 Level of Service ....................................................... 11
      2.3.5.1 Limited-Service .................................................. 11
      2.3.5.2 Extended-Stay .................................................... 11
      2.3.5.3 Full-Service ....................................................... 12
  2.4 The UK Hotel Industry ................................................... 12
    2.4.1 The Supply of the UK Hotel Industry ......................... 14
    2.4.2 The Demand of the UK Hotel Industry ....................... 16
  2.5 Definition of a Budget Hotel ............................................. 18
  2.6 Characteristics of Budget Hotels ...................................... 20
  2.7 The UK Budget Hotel Sector ........................................... 25
### Chapter 6 Methodology

- 6.1 Introduction ......................................................... 182
- 6.2 Objectives of the Study ........................................ 182
- 6.3 Research Philosophy ............................................. 182
- 6.4 Research Philosophy Adopted ............................. 185
- 6.5 Types of Research Design ........................................ 186
  - 6.5.1 Exploratory Study ........................................... 186
  - 6.5.2 Descriptive Research ..................................... 187
  - 6.5.3 Hypotheses Testing Study ............................... 187
- 6.6 Research Design Selected ...................................... 188
- 6.7 Preliminary Study .................................................. 191
  - 6.7.1 Objectives of the Preliminary Study ................. 191
  - 6.7.2 Sample of the Preliminary Study ...................... 192
  - 6.7.3 Data Analysis of the Preliminary Study ............ 192
  - 6.7.4 Findings of the Preliminary Study (Part Two) ...... 193
- 6.8 Timeline of the Main Study .................................... 195
- 6.9 Measurements of Variables .................................... 201
  - 6.9.1 Study 1 (Hotel Performance Data) ................. 201
  - 6.9.2 Study 2 (General Managers' Perspective) ........ 202
  - 6.9.3 Pilot Study of the Research Instrument .......... 210
- 6.10 Sampling Procedures ........................................... 211
  - 6.10.1 Sample Population ....................................... 211
  - 6.10.2 Sample Selection ......................................... 211
- 6.11 Data Analysis Techniques ..................................... 212
  - 6.11.1 Validity and Reliability of the Measures .......... 212
    - 6.11.1.1 Validity ............................................... 212
    - 6.11.1.2 Reliability .......................................... 216
  - 6.11.2 Testing of the Research Model ....................... 217
- 6.12 Conclusions ....................................................... 218

### Chapter 7 Findings of Study 1 (Hotel Performance Data)

- 7.1 Introduction ......................................................... 222
- 7.2 Nature and Description of Data ............................. 222
- 7.3 Correlation Analysis ............................................. 229
Chapter 8 Findings of Study 2 (General Managers’ Perspective) ........................................... 247
8.1 Introduction ..................................................................................................................... 248
8.2 Characteristics of the Sample .......................................................................................... 248
  8.2.1 Characteristics of the Hotels ................................................................................ 249
    8.2.1.1 Location ................................................................................................... 249
    8.2.1.2 Years of Operations ................................................................................. 250
    8.2.1.3 Number of Rooms ................................................................................... 250
    8.2.1.4 Revenue Segmentation ............................................................................ 251
  8.2.2 Demographic Characteristics of the Respondents ............................................... 252
    8.2.2.1 Gender .................................................................................................... 252
    8.2.2.2 Age ........................................................................................................... 252
    8.2.2.3 Education ................................................................................................. 253
    8.2.2.4 Years of Experience in This Hotel .......................................................... 254
    8.2.2.5 Job Title ................................................................................................... 254
    8.2.2.6 Years of Experience at this position ........................................................ 255
8.3 Descriptive Analysis ........................................................................................................ 256
  8.3.1 Brand Awareness ................................................................................................. 256
  8.3.2 Service Quality .................................................................................................... 257
  8.3.3 Customer Satisfaction .......................................................................................... 257
  8.3.4 Customer Retention ............................................................................................. 258
  8.3.5 Premium Price ..................................................................................................... 258
  8.3.6 Business Performance ......................................................................................... 259
  8.3.7 Managing Demand and Capacity ........................................................................ 261
8.4 Normality of the Data ...................................................................................................... 262
8.5 Construct Validity of the Scales (Exploratory Factor Analysis) ..................................... 264
  8.5.1 The Service Quality Scale ................................................................................ 264
  8.5.2 The Demand and Capacity Management Scale ................................................... 266
8.6 Reliability of the Scales ................................................................................................... 270
  8.6.1 The Service Quality Scale ................................................................................ 271
# List of Tables

<table>
<thead>
<tr>
<th>Table</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.1</td>
<td>Number of VAT-Based Enterprises Engaged In the Hotel Operation</td>
</tr>
<tr>
<td>2.2</td>
<td>Number of Hotels and Rooms by Locations in the UK</td>
</tr>
<tr>
<td>2.3</td>
<td>The UK Hotel Market Revenue</td>
</tr>
<tr>
<td>2.4</td>
<td>The UK Hotel Market Statistics, 2001-2006</td>
</tr>
<tr>
<td>2.5</td>
<td>Branded Budget Hotels in UK</td>
</tr>
<tr>
<td>2.6</td>
<td>Branded Budget Hotel Supply in UK (2001-2007)</td>
</tr>
<tr>
<td>2.7</td>
<td>The UK Budget Hotel Market Statistics, 2005-2007</td>
</tr>
<tr>
<td>3.1</td>
<td>Differences between Service and Physical Goods</td>
</tr>
<tr>
<td>3.2</td>
<td>Models of Service Quality</td>
</tr>
<tr>
<td>4.1</td>
<td>Profitability Ratios</td>
</tr>
<tr>
<td>4.2</td>
<td>Investment Ratios</td>
</tr>
<tr>
<td>4.3</td>
<td>Activity Ratios</td>
</tr>
<tr>
<td>4.4</td>
<td>Liquidity Ratios</td>
</tr>
<tr>
<td>4.5</td>
<td>Leverage Ratios</td>
</tr>
<tr>
<td>4.6</td>
<td>Performance Measurement System in the Service Industry (PMSS)</td>
</tr>
<tr>
<td>4.7</td>
<td>Developments and Changes of PMSs</td>
</tr>
<tr>
<td>4.8</td>
<td>Financial Measures in the Hotel Industry</td>
</tr>
<tr>
<td>4.9</td>
<td>Operational Performance Indicators in the Hospitality Industry (Rooms Dep)</td>
</tr>
<tr>
<td>4.10</td>
<td>Other Ratios in the Hospitality Industry</td>
</tr>
<tr>
<td>4.11</td>
<td>Operational Performance Indicators in the Hospitality Industry (Restaurant and Food and Beverage Dep)</td>
</tr>
<tr>
<td>4.12</td>
<td>Performance Measures in Restaurants</td>
</tr>
<tr>
<td>4.13</td>
<td>Ratios used in the Uniform System Accounts for the Lodging Industry</td>
</tr>
<tr>
<td>5.1</td>
<td>Summary of Empirical Studies</td>
</tr>
<tr>
<td>6.1</td>
<td>Research Philosophies Comparison</td>
</tr>
<tr>
<td>6.2</td>
<td>Research Design Features</td>
</tr>
<tr>
<td>6.3</td>
<td>Advantages and Disadvantages of Cross-Sectional and Longitudinal Design</td>
</tr>
<tr>
<td>6.4</td>
<td>Timeline of the Main Studies (Study One + Study Two)</td>
</tr>
<tr>
<td>6.5</td>
<td>Guidelines for Identifying Significant Factor Loadings based on Sample Size</td>
</tr>
<tr>
<td>Section</td>
<td>Title</td>
</tr>
<tr>
<td>---------</td>
<td>-----------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>7.1</td>
<td>Example of the Balanced Scorecard System of Unit X</td>
</tr>
<tr>
<td>7.2</td>
<td>Values of Skewness and Kurtosis for Study 1</td>
</tr>
<tr>
<td>7.3</td>
<td>Correlation Matrix of Variables for Study 1</td>
</tr>
<tr>
<td>7.4</td>
<td>Assumptions of Multiple Regressions for Study 1</td>
</tr>
<tr>
<td>7.5</td>
<td>OLS Regression Analysis: Predicting Customer Retention</td>
</tr>
<tr>
<td>7.6</td>
<td>OLS Regression Analysis: Predicting Premium Price</td>
</tr>
<tr>
<td>7.7</td>
<td>OLS Regression Analysis: Predicting Sales Growth</td>
</tr>
<tr>
<td>7.8</td>
<td>OLS Regression Analysis: Predicting Profit Growth</td>
</tr>
<tr>
<td>7.9</td>
<td>OLS Regression Analysis: Predicting Premium Price</td>
</tr>
<tr>
<td>7.10</td>
<td>OLS Regression Analysis: Predicting Sales Growth</td>
</tr>
<tr>
<td>7.11</td>
<td>OLS Regression Analysis: Predicting Profit Growth</td>
</tr>
<tr>
<td>7.12</td>
<td>OLS Regression Analysis: Predicting Profit Growth</td>
</tr>
<tr>
<td>7.13</td>
<td>Summary of Hypotheses Testing for Study 1</td>
</tr>
<tr>
<td>8.1</td>
<td>Evaluation of Brand Awareness</td>
</tr>
<tr>
<td>8.2</td>
<td>Evaluation of Service Quality</td>
</tr>
<tr>
<td>8.3</td>
<td>Evaluation of Customer Satisfaction</td>
</tr>
<tr>
<td>8.4</td>
<td>Evaluation of Customer Retention</td>
</tr>
<tr>
<td>8.5</td>
<td>Evaluation of Premium Price</td>
</tr>
<tr>
<td>8.6</td>
<td>Evaluation of Business Performance Indicators</td>
</tr>
<tr>
<td>8.7</td>
<td>Evaluation of Managing Demand and Capacity</td>
</tr>
<tr>
<td>8.8</td>
<td>Values of Skewness and Kurtosis for Study 2</td>
</tr>
<tr>
<td>8.9</td>
<td>Correlation Matrix of the Service Quality Scale</td>
</tr>
<tr>
<td>8.10</td>
<td>VARIMAX-Rotated Component Analysis Factor Matrix for the Service Quality Scale</td>
</tr>
<tr>
<td>8.11</td>
<td>Correlation Matrix of the Demand and Capacity Management Scale</td>
</tr>
<tr>
<td>8.12</td>
<td>Varimax-Rotated Component Analysis Factor Matrix for the Demand and Capacity Management Scale</td>
</tr>
<tr>
<td>8.13</td>
<td>Reliability of the Service Quality Scale</td>
</tr>
<tr>
<td>8.14</td>
<td>Reliability of the Demand and Capacity Management Scale</td>
</tr>
<tr>
<td>8.15</td>
<td>Correlation Matrix of Variables for Study 2</td>
</tr>
<tr>
<td>8.16</td>
<td>OLS Regression Model: Predicting Profitability</td>
</tr>
<tr>
<td>8.17</td>
<td>OLS Regression Model: Predicting Customer Satisfaction</td>
</tr>
<tr>
<td>8.18</td>
<td>OLS Regression Model: Predicating Premium Price</td>
</tr>
<tr>
<td>8.19</td>
<td>OLS Regression Model: Predicting Customer Retention</td>
</tr>
</tbody>
</table>
### List of Figures

<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>Structure of the Study</td>
<td>5</td>
</tr>
<tr>
<td>2.1</td>
<td>Critical Factors and Characteristics of Budget Hotels</td>
<td>22</td>
</tr>
<tr>
<td>2.2</td>
<td>Total Rooms Revenue from Budget Hotels for the Period (2000-2006)</td>
<td>32</td>
</tr>
<tr>
<td>2.3</td>
<td>Customer Segmentation in the UK Budget Hotel Sector</td>
<td>33</td>
</tr>
<tr>
<td>3.1</td>
<td>Quality Definitions Continuum</td>
<td>48</td>
</tr>
<tr>
<td>3.2</td>
<td>Service Characteristics</td>
<td>51</td>
</tr>
<tr>
<td>3.3</td>
<td>The Gronroos's Model</td>
<td>57</td>
</tr>
<tr>
<td>3.4</td>
<td>The Gab Model</td>
<td>62</td>
</tr>
<tr>
<td>3.5</td>
<td>The Three-Component Model</td>
<td>66</td>
</tr>
<tr>
<td>3.6</td>
<td>The Multilevel Model of Service Quality</td>
<td>67</td>
</tr>
<tr>
<td>3.7</td>
<td>The Hierarchical Model of Service Quality</td>
<td>68</td>
</tr>
<tr>
<td>3.8</td>
<td>The Internal Service Quality Model</td>
<td>70</td>
</tr>
<tr>
<td>3.9</td>
<td>A Multilevel Model of Service Quality in the Hospitality Industry</td>
<td>89</td>
</tr>
<tr>
<td>4.1</td>
<td>How to Improve ROCE</td>
<td>106</td>
</tr>
<tr>
<td>4.2</td>
<td>The Balanced Scorecard (BSC)</td>
<td>114</td>
</tr>
<tr>
<td>4.3</td>
<td>The SMART System</td>
<td>119</td>
</tr>
<tr>
<td>4.4</td>
<td>The Performance Prism</td>
<td>123</td>
</tr>
<tr>
<td>5.1</td>
<td>The Conceptual Framework</td>
<td>169</td>
</tr>
<tr>
<td>6.1</td>
<td>Overview of the Study Process</td>
<td>219</td>
</tr>
<tr>
<td>7.1</td>
<td>The Simplified Research Model for Study 1</td>
<td>227</td>
</tr>
<tr>
<td>7.2</td>
<td>Normal P-P Plot of Regression Standard of Residual of Dependent Variable for Study 1</td>
<td>232</td>
</tr>
<tr>
<td>7.3</td>
<td>Scatter Plot of Regression Standardised Residual for Study 1</td>
<td>232</td>
</tr>
<tr>
<td>7.4</td>
<td>The Simplified Research Model: Testing Hypothesis 1A</td>
<td>234</td>
</tr>
<tr>
<td>7.5</td>
<td>The Simplified Research Model: Testing Hypothesis 1B</td>
<td>235</td>
</tr>
<tr>
<td>7.6</td>
<td>The Simplified Research Model: Testing Hypothesis 1C</td>
<td>236</td>
</tr>
<tr>
<td>7.7</td>
<td>The Simplified Research Model: Testing Hypothesis 1D</td>
<td>237</td>
</tr>
<tr>
<td>7.8</td>
<td>The Simplified Research Model: Testing Hypothesis 2A</td>
<td>238</td>
</tr>
<tr>
<td>7.9</td>
<td>The Simplified Research Model: Testing Hypothesis 2B</td>
<td>239</td>
</tr>
<tr>
<td>7.10</td>
<td>The Simplified Research Model: Testing Hypothesis 3</td>
<td>240</td>
</tr>
<tr>
<td>7.11</td>
<td>The Simplified Research Model: Testing Hypothesis 4</td>
<td>241</td>
</tr>
</tbody>
</table>
7.12 Final Model with Significant Paths for Study 1 ................................................. 242
8.1 Location of Hotels ................................................................................................ 249
8.2 Years of Operations ............................................................................................. 250
8.3 Number of Rooms ................................................................................................ 251
8.4 Customer Segments ............................................................................................. 251
8.5 Gender .................................................................................................................. 252
8.6 Age Groups .......................................................................................................... 253
8.7 Level of Education ............................................................................................... 253
8.8 Years of Experience in this Hotel ......................................................................... 254
8.9 Job Title ................................................................................................................. 255
8.10 Number of Years at this Position ......................................................................... 255
8.11 Scree Plot Analyses for the Service Quality Scale ............................................. 265
8.12 Scree Plot Analyses for the Demand and Capacity Management Scale ............. 268
8.13 Normal P-P Plot of Regression Standardized Residual of Dependent Variable for
Study 2 ...................................................................................................................... 277
8.14 Scatter Plot of Regression Standardised Residual for Study 2 ............................ 278
8.15 The Research Model: Testing Hypothesis 1 ....................................................... 280
8.16 The Research Model: Testing Hypothesis 2 ....................................................... 281
8.17 The Research Model: Testing Hypothesis 3 ....................................................... 282
8.18 The Research Model: Testing Hypothesis 4 ....................................................... 283
8.19 The Research Model: Testing Hypothesis 5 ....................................................... 284
8.20 The Research Model: Testing Hypothesis 6 ....................................................... 285
8.21 The Research Model: Testing Hypothesis 7 ....................................................... 286
8.22 The Research Model: Testing Hypothesis 8 ....................................................... 287
8.23 The Research Model: Testing Hypothesis 9 ....................................................... 288
8.24 The Research Model: Testing Hypothesis 10 ..................................................... 289
8.25 The Research Model: Testing Hypothesis 11 ..................................................... 292
8.26 Post Hoc Analysis Model .................................................................................... 294
8.27 Final Model with Significant Paths for Study 2 ................................................ 299
9.1 The Relationship between Service Quality and Profitability ............................. 311
Acknowledgement

First of all, I would like to thank my supervisors Prof. Andrew Lockwood and Dr. Yuksel Ekinci so much for their invaluable support, guidance and patience over the last few years. My meetings with them were always constructive as they helped me find solutions for the problems and tricky I faced. Without their contributions and supervision, I could not have produced and completed this thesis. Simply, they were vital to my progress. Each one of them, in his way, was supportive and sympathetic. Together, they did very well from that first day.

I also wish to thank the anonymous company that gave me access to their invaluable data base and allowed me the opportunity to distribute my questionnaire to undertake my study. The coordinator there was particularly helpful during all stages of the study. I am grateful for her understanding and patience with my continuous questions and needs. I would like to extend my gratitude to all staff at the School of Management and the University for their friendship and providing useful and professional assistance. Furthermore, I give my thanks and regards to all friends and colleagues I met at the University of Surrey, especially to Arkam, Marwan, Amar, Krystin, Khalid, Sameer, AbdelHadi, Mohammad, and Rania for their honest advice and emotional encouragement whenever I needed it.

I acknowledge my sponsor Al-Hussein Bin Talal University in Jordan for giving me a scholarship. They have always been willing to generously provide all needful support to facilitate my task as a student in the UK. And a special thank you to all the staff at the academic research deanship for their prompt help.

To my best friends in Jordan, Ra’fat, Taher, Zaydon, Shaheer, and Moheeb thank you for asking about me all the time. Finally, I would like to take this opportunity to thank my parents and family for their love and moral support. I thank them for their endless caring, concern and questions. I thank them for tracking and sharing my happy and frustrated moments during my Ph.D. They did everything they could to enable me to finish my studies peacefully and smoothly. Indeed and forever, thank you from my heart, and I promise to be with you soon.
Chapter 1

Introduction
1.1 Background of the Study

In recent decades, the world has witnessed a great deal of interest and widespread growth in the hotel industry. As a result, this industry now plays a major role in the social and economic growth for any country. For example, this industry is highly labour intensive and employs a huge number of people in both full and part-time careers. More precisely, the hospitality industry in total employs over 1.8 million people in the UK. At the hotel unit level, there are around 307,000 people working in approximately 12,000 hotels. Therefore, the workforce in hotels represents around 17% of the total number of people working in the hospitality industry (National Statistics, 2005).

The hotel industry is experiencing intense competition and becoming a truly international/global industry. This complex business environment forces managements to engage in quality improvement programs in order to surmount the risks and threats they face (Hasan and Kerr, 2003). Therefore, the term ‘quality’ has emerged as one of the most important elements for achieving competitive advantage within service oriented firms. A number of authors support the view that achieving higher product and service quality leads to improved business performance (e.g. the service profit chain by Reichheld and Sasser, 1990). Accordingly, extensive efforts have been carried out by academics and practitioners to better understand and explain this concept and to explore its relationship with customer behaviour and business performance (Cook and Verma, 2002; Zeithaml and Bitner, 2003).

The subjects of quality and its impact on business performance have therefore received extensive attention by researchers and experts investigating this relationship. For instance, the Profit Impact of Marketing Strategy (PIMS) project investigated the impact of quality, market share, productivity, price and other elements on financial performance (Buzzel and Gale, 1987, 2004; Brennan, Baines and Gareau, 2003; Buzzell, 2004). In addition, Hardie (1998) looked at 43 case studies, experiments, opinion surveys and
correlation studies in order to analyze the effect of quality management on business performance.

Marketing and strategic disciplines have provided a theoretical framework for the link between quality programs and business performance (Deming, 1983, 1986; Garvin, 1988; Shapiro, 1983; Bolton and Drew, 1991; Heskett, Sasser and Schlesinger, 1997). The aim of these theoretical models was to explain the relationship between quality and business performance. The key finding in these theoretical endeavours was to propose that improving quality of services and goods will improve business performance. However, the relationship between service quality and profitability remains open for debate, as the theoretical link between the two is considered neither straightforward nor simple. Moreover, no single researcher has covered this relationship completely (Zeithaml, 2000). Consequently, the main aim of this study is to contribute further to the body of knowledge on this topic in specific relation to the budget hotel sector.

1.2 Purpose of the Study
This study aims to examine the relationship between service quality and profitability in the UK budget hotel sector. Recently, the budget hotel sector is considered one of the largest and fastest-growing segments within the UK hospitality industry (Brotherton, 2004). The number of UK Budget hotels in 1992 was 193, with 7326 rooms (Deloitte & Touche, 2003). In 2006, this sector had 70000 rooms operating in a wide range of locations and markets, and in 2007, 15000 more were added for a total of 85000 rooms. Deloitte & Touche reported that the budget hotel sector in the UK valued more than £3 billion pounds (Key Note-Top Markets; Travel and Tourism, 2007; TRI, 2007). In the next few years, key players in the market will add 23000 additional rooms. As a result, this budget sector of hotels will compete with mid and upper sectors.

Hence, this study aims to contribute to existing knowledge by testing the hypothetical relationship between service quality and profitability performance in the UK budget hotel sector.

1.3 Objectives of the Study
(1) To develop a conceptual framework which captures the relationship between service quality and profitability in the UK budget hotel sector.
(2) To examine empirically the relationship between service quality and profitability in the UK budget hotel sector.

(3) To determine what variation, if any, exists in the nature and direction of this relationship among different data sets collected from different sources.

(4) To determine which outcome of service quality makes the greatest contribution to budget hotel profits.

1.4 Structure of the Study
This thesis consists of nine chapters as indicated in Figure 1.1
Chapter two provides a discussion about the UK hotel industry in general and budget sector in particular. To do so, this chapter reviews the definition of a hotel and the common classifications of hotels, then provides some information about the UK hotel industry in general in terms of supply, demand and performance. Finally, chapter two introduces some facts concerning the definition and characteristics of the budget hotel sector, followed by displaying the main characteristics and economic background of the budget hotel sector in UK. This chapter also shows new strategies and trends occurred in the budget hotel sector in UK.
Chapter three reviews the following issues related to service quality: definitions of quality, definitions of service, characteristics of service, definitions of the service quality concept, dimensions of the service quality construct, models or schools of service quality thought, service quality measurements and techniques, quality of service in the hospitality industry and outcomes of service quality.

Chapter four reviews the relevant literature concerning the theory of business performance measurement systems. Therefore, this chapter discusses definitions of business performance measurement, the common types of business performance systems and developments in these systems over the last decades, measurements of financial performance and PMSs in the hospitality industry. Moreover, this chapter reports the first part of the preliminary study conducted with hoteliers.

Chapter five explores the debate over empirical studies concerning the topic investigated, in order to find the research question and develop the research model. Accordingly, this chapter starts by presenting the research question, then displays the conceptual framework developed, followed by definitions of variables. Finally, this chapter generates and justifies the research hypotheses.

Chapter six explains and discusses methodological issues required for conducting the research. This chapter covers different topics; types of research paradigms and designs, the research methods selected, results of the preliminary study, measurement of variables in the two studies, sampling procedures and finally the data analysis technique used.

Chapters seven and eight focus on the data analysis for study 1 (Hotel Performance Data) obtained from the budget hotel chain plus study 2 (General Managers’ Perceptions) collected by the researcher from the same chain, i.e. secondary and primary data. Chapter seven analyzes data obtained for study one, while chapter eight considers and analyzes data for study two, collected from general managers by using a questionnaire.

Chapter nine reviews and summarizes findings obtained from the preceding data analysis chapters to draw a broad conclusion for the study. Furthermore, this chapter provides theoretical and empirical implications, and suggests directions for future research.
Chapter 2

The UK Budget Hotel Sector
Chapter 2

The UK Budget Hotel Sector

2.1 Introduction

In order to discuss the main concepts, characteristics and trends in the budget hotel sector, this chapter aims to explain the main concepts and trends within both the UK hotel industry in general and the budget hotel sector in particular. Section two defines the hotel establishment. Section three classifies common hotels. Section four gives a snapshot of the UK hotel industry, including both the supply and demand side, as well as some economic trends. Sections five and six define the budget hotel establishment and introduce the common operational characteristics of budget hotels. Section seven gives historical background about budget hotels in the UK and describes the supply and demand sides of the sector in the UK. Section eight sheds lights on the recent trends and developments in the UK budget hotel sector. Finally, section nine concludes this chapter.

2.2 Definition of a Hotel

The hotel industry is a part of the hospitality industry. The hospitality industry encompasses different activities and purposes, including lodging, catering and entertainment (Dittmer, 2002). Although the hospitality industry is comprised of other establishments besides hotels, such as restaurants, pubs, clubs, entertainment venues, and transport, the hotel industry represents a key segment of the hospitality industry.

Accommodation/hotel establishments came into existence around 12,000 years ago due to the need for trade and travel. After the creation of money as a common bartering unit, the development of transport infrastructure, and an expansion of real opportunities for people to travel, the need for a lodging industry increased rapidly (Lattin, 1998; Jones, 2002; Jones and Lockwood, 1989). A few centuries later, the rapid growth of demand for travel by business and leisure travellers, coupled with further development of technological innovations and the enhanced wealth of individuals, increased international demand for short-term accommodation. As a result, different products and services appeared within
the industry, such as hotels, motels, inns, motor hotels, bed-and-breakfasts, resorts, time-share properties, etc.

Given this brief historical background, a hotel can be defined as "an establishment whose primary business is providing lodging facilities for the general public, and which furnishes one or more of the following services: food and beverage service, room attendant (housekeeping) service, concierge, bell and door attendant service (sometimes called uniformed service), laundry or dry cleaning, and use of furniture and fixtures" (Kasavana and Brooks, 1998 p.5). Moreover, the context of a hotel is defined by Dittmer (2002, p. 205) as "an establishment that charges fees for providing furnished sleeping accommodation to persons who are temporarily away from home or who consider these accommodations their temporary or permanent home".

According to the above definitions of a hotel, it can be assumed that the hotel is a profit-driven organization which provides temporary accommodation services for the public with some additional and optional services. Moreover, the term "hotel" represents the general term for any accommodation or lodging service.

2.3 Classifications of Hotels

Classifying hotels into different groups creates some advantages for all parties in the industry. Firstly, it establishes a uniform system which can be used to compare service and product quality among hotels. Secondly, it informs travellers about the range and type of hotels available, which leads to the promotion and marketing of hotels. Thirdly, it protects consumers by ensuring that a hotel meets the minimum standards in terms of accommodation, facilities and services for each class or grade. Finally, such classification helps to control the general quality of the industry (Gee, 1994).

Stutts (2001) outlines that hotels vary widely, which may complicate this 'mission' for travellers, owners, investors and managers. To put it more simply, assigning a hotel to a particular category is not easy, and each hotel can potentially be allocated to several alternative classifications (Kasavana and Brooks, 1998). In this regard also, Barrows and Powers (2009) claim that hotels can be grouped into different classifications at the same time. However, they offer several classifications for hotels based on different criteria such
as price, function, location, market segment and distinctiveness of style or offerings. The following sub-sections show these classifications briefly.

2.3.1 Quality of Facilities and Services
This classification of hotels identifies to what extent a hotel adopts certain standards with respect to different aspects such as management, public areas, exterior, guest room security, fire protection, housekeeping and maintenance, room decor and ambiance, and bathrooms. The most popular system of classification is the diamond rating system, developed by the American Automobile Association (AAA) in 1907, which ranks any hotel by evaluating the quality of the services and facilities implemented in that hotel. This rating system contains five levels or stars; a hotel with one star adopts lower standards than a hotel with two stars and so on (Stutts, 2001). There are other rating schemes in common use, such as the AA in the UK.

2.3.2 Target Market
According to this classification, Barrows and Powers (2009) classify hotels according to the guests’ needs and purposes of visiting the hotel, such as airport hotels, resorts, bed and breakfast, casino and conference centres, health spas and vacation ownership (timeshare). Hence, the purpose of visiting the hotel can be used to classify it. For example, business guests are more likely to visit budget and/or conference hotels than leisure travellers are.

2.3.3 Ownership and Affiliation
This classification differentiates hotels according to the ownership of the hotel. In the lodging industry, there are two common approaches. On the one hand, there is the independent hotel approach, which means that the owner of the hotel is also the operator and does not have a relationship with other properties. Thus, in this structure of ownership, the owner of the hotel carries out all procedures – marketing, standards, financial obligations and so on. On the other hand, there is the chain hotel approach, in which a hotel has an arrangement with the company that owns the brand name. In other words, the hotel has to obey the company’s regulations, standards and procedures. Additionally, this form of ownership (chain hotel) includes two ways of managing the hotel: management contracts and franchising (Kasavana and Brooks, 1998).
2.3.4 Comparative Statistics

Managers and experts use this classification in order to understand particular facts about individual properties versus the industry as a whole, in terms of number of rooms, room rates and geographical locations. In other words, this classification gives a snapshot of the industry (Stutts, 2001). As a result, this classification can be used to make statistical comparisons of hotels, either at the unit level or the aggregate level of the industry, for different periods such as yearly, monthly, weekly or daily. Moreover, some operational indicators (e.g. average daily rate, occupancy and costs) can be used in this classification.

2.3.5 Level of Service

This classification categorizes hotels according to the level of service provided for guests. However, it is worth saying that this classification of hotels also depends on prices charged. In other words, prices of accommodation can determine the level of service provided. Accordingly, this classification divides establishments in the lodging industry into three different levels.

2.3.5.1 Limited-Service

This class of hotels deals extensively with price-sensitive business or leisure travellers with an average length of stay in the region of one or two nights. Accordingly, limited-service hotels offer limited services for guests. Food and beverages are not always available or limited to complimentary breakfast only; similarly, restaurants, meeting rooms, bell service, and parking service may be limited or absent in such establishments (Stutts, 2001). Hotels located in this class can be called limited-service hotels, budget hotels or economy hotels (Barrows and Powers, 2009). Because the budget hotel sector represents the main sample in the current research, the definition and characteristics of such hotels will be discussed later in more detail.

2.3.5.2 Extended-Stay

This segment of hotels is designed for business and leisure guests who need more than an overnight visit. Hotels within this level provide guests with the typical facilities and amenities of apartment-style living (e.g. facilities for preparing meals in the room). In other words, extended-stay hotels accommodate guests with most of the comfort facilities of their own homes. Therefore, such hotels may not offer all services available in luxury
hotels, including business centres, premium guest room amenities, spas, retail outlets, 24-hour restaurants, etc. (Stutts, 2001).

2.3.5.3 Full-Service
This class of hotels provides guests with a wide variety of services, facilities and amenities (Barrows and Powers, 2009). Accordingly, food and beverage choices in this class are wider than in any of the previous hotel classifications; business centre facilities, parking, meeting rooms, room service, recreational activities, banquette facilities and full room service (24 hours) are all available. Guests in these hotels are generally not sensitive to price.

To conclude, the lodging industry has several classification systems. According to these systems, hotels are varied based on different standards such as quality of facilities, purpose of visiting, location, price and level of service. However, each single hotel or lodging establishment can be grouped into several classifications. These classifications can help customers in evaluating and choosing hotels. Moreover, such classifications can help operators in their benchmarking, marketing and promotional activities.

2.4 The UK Hotel Industry
There is no doubt that the UK hotel industry is considered a mature and important industry within the global hotel market for several reasons including the fact that a number of key international hotel brands are owned by British groups (e.g. Intercontinental Hotel Group) and that some British brands exist overseas. In other words, the British market includes both international and domestic chains. Accordingly, the UK hotel industry is an important competitor in the international hotel market. Furthermore, the UK hotel industry includes all classes of hotels as shown previously (Key Note-Hotels, 2005). In this respect, Imrie and Fyall (2001) divided the total UK hotel market into five major segments: (1) independently owned and operated hotels, (2) small company owned and operated hotels, (3) corporately owned and operated branded hotels, (4) franchised hotels operating highly branded hotels in medium and upscale market levels and, (5) hotels participating in marketing consortia. Imrie and Fyall (2001) mention that these five segments are comprised of hotels with different levels of service including low, budget, mid-market, upscale and luxury hotels.
However, Imrie and Fyall (2001) claimed that the corporately owned hotels (e.g. Hilton, Holiday Inn, Forte, Premier Inn, etc) which focus mainly on the budget and upscale market levels are succeeding because hotels in this segment have a well-focused strategic direction, clear branding, well developed sales and marketing forces, economies of scale, a high degree of flexibility and a rapid response to changing market conditions.

Similarly to other hotel markets in the world, hotels in the UK serve two main kinds of clients: corporate (business travellers) and consumer (leisure travellers). The first market forms the larger portion, which has different activities including conferences, meetings, exhibitions, trade fairs, corporate events, outdoor events and business travel for attending meetings or events. The second sector (consumer clients) is smaller. Leisure travellers use hotels for recreational purposes and holidays, or to break up a long journey (Key Note-Hotels, 2006).

Like other hotel industries in the world, British bodies engaged in the hotel industry, including the Automobile Association (AA) and the Royal Automobile Club (RAC), adopted a single system for assessing establishments within the industry in 2005. Hence, all hotels in the UK market are assessed and awarded between one and five stars (the more stars awarded, the more facilities and the higher the level of service). All operators that do not participate in this assessment process will be excluded from promotional activities at domestic and international events.

The UK hotel market is divided into two geographical groups: first, London, which represents an international destination for a large number of passengers visiting the UK for national and international events, conferences and exhibits, etc. Thus, London as a capital is enjoying the high demand of the overall industry. For example, the average RevPAR for hotels in London is typically 50% higher than other location in Britain. Furthermore, provincial hotels, which comprise hotels located in all other cities and towns across the country, target leisure guests (Mintel, 2006).

In order to explore the status of the UK hotel industry, the Key Note Consult Company (2007) describes the internal and external environment of the overall UK hotel industry in terms of strengths, weaknesses, opportunities and threats. The strengths of the UK hotel industry are attributed to the following points: promising international and domestic
tourism, promotional support from other parties in the country (e.g. VisitBritain), the
large variety of accommodations available at different prices, the well-known
international and local brands, the internet booking system, and the significant
development of the budget hotel sector. On the other hand, some weaknesses diminish the
industry such as the oversupply of UK hotels and the high competition in the mid-market
hotel sector with less differentiated service. However, the UK hotel industry should gain
benefits from opportunities available in the market, such as the significant number of
non-hotel users who might simply be attracted, the new regulations against air travel that
could increase domestic breaks and finally the Olympics event in 2012, which could
increase the occupancy of hotels, especially those located around London.

In terms of ownership, the movement of hotels away from the property-owning sector and
towards more flexible methods of management forms the most important trend in the UK
hotel industry for the period between 2001 and 2006, and it will continue to be the most
important trend in the coming years. In other words, the last years witnessed a trend
towards a separation between the ownership and operation of hotels. Different equity
groups such as banks and real estate firms are now involved in this new trend of
ownership, freeing operators to deal with marketing, management and branding.
According to this new trend, banks or other fund entities own the building of the hotel
while operators own the hotel brand within the building. For instance, Intercontinental
Hotels Group sold-off £1 billion of its assets to Lehman Brothers, GIC Real Estate and
Realstar Asset Management. As a result of this shifting of ownership, popular and strong
brands in the market have emerged, focusing on offering broad, new services (BHA,
2005; Mintel, 2006; Key Note, Hotels, 2007).

Having shown the importance of UK hotel industry as well as some of its main issues, the
following sub-sections will briefly discuss the supply and demand sides of the UK hotel
industry over the last years.

2.4.1 The Supply of the UK Hotel Industry

Phillips (1997) states that understanding the forces of supply and demand in any hotel
industry is necessary to obtain competitive advantages for operators. To do so, different
published indicators and statistics can be used to measure the supply and demand sides of
the hotel industry. In this regard, Phillips (1997) mentions that the supply side can be
measured by specific indicators, such as unit numbers and room stock available in the
market. On the other hand, the demand side can be measured by another set of indicators including; revenues, occupancy percentages, room rates and room nights sold. Statistical data for such indicators can be obtained from several sources and consultant companies to track the supply, demand and performance of hotels in the UK.

Although the registration of hotels in the UK is not compulsory, several publications have attempted to determine the number of hotels in the UK. Therefore, it is difficult to find the exact number of hotels operating in the UK (Phillips, 1997; Allin, 1999). However, this study will adopt figures published by one market research company (Key Note). Table 2.1 displays the number of VAT-Enterprises engaged in hotel operation between 1990 and 2007 in the UK.

Table 2.1 Number of VAT-Based Enterprises Engaged in Hotel Operation

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Hotels</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>14410</td>
</tr>
<tr>
<td>1995</td>
<td>12005</td>
</tr>
<tr>
<td>1997</td>
<td>10,935</td>
</tr>
<tr>
<td>1999</td>
<td>10425</td>
</tr>
<tr>
<td>2001</td>
<td>9580</td>
</tr>
<tr>
<td>2002</td>
<td>9215</td>
</tr>
<tr>
<td>2003</td>
<td>9535</td>
</tr>
<tr>
<td>2004</td>
<td>9030</td>
</tr>
<tr>
<td>2005</td>
<td>9110</td>
</tr>
<tr>
<td>2006</td>
<td>8925</td>
</tr>
<tr>
<td>2007</td>
<td>8810</td>
</tr>
</tbody>
</table>

Source: Key Note-Hotels (2007, p: 15)

Table 2.1 indicates a significant decrease in the number of establishments in the UK over the last 15 years. To be more precise, the decrease between 1990 and 2000 was very steep while the decrease was very minor since 2002. More than 6000 businesses have left the market due to national and international forces.

Several reports and sources explain the reasons for the underperformance of the UK hotel industry. For example, in a report published by Key Note (2007), foot-and-mouth disease,
the downturn in international travel, the high level of competition among hotels, the events of September 11th 2001 and the war in Iraq all negatively affected the UK hotel industry. As a result, the number of establishments interested in hotel operation has fallen by more than a third (38%) between 1990 and 2007.

Another important part of the supply side, Table 2.2 displays the room number in UK.

<table>
<thead>
<tr>
<th>Location</th>
<th>Number of Hotels</th>
<th>Number of Rooms</th>
</tr>
</thead>
<tbody>
<tr>
<td>England</td>
<td>12520</td>
<td>337,203</td>
</tr>
<tr>
<td>Scotland</td>
<td>1269</td>
<td>41,557</td>
</tr>
<tr>
<td>Wales</td>
<td>689</td>
<td>14,690</td>
</tr>
<tr>
<td>North Ireland</td>
<td>131</td>
<td>6,075</td>
</tr>
<tr>
<td>Total</td>
<td>14609</td>
<td>439,525</td>
</tr>
</tbody>
</table>

Source: BHA, UK Hotel Industry (2005, p: 15)

The above table reveals that England has the vast majority of rooms offered in the UK hotel industry. In other words, approximately 85% of rooms are located in England hotels due to England’s importance as a popular destination for business and leisure travellers, while hotels in other parts in the country account for less than 15% of rooms. This can be explained by the small numbers of hotels in those areas as well as the small size of those hotels.

2.4.2 The Demand of the UK Hotel Industry

Although the events of 9/11 in 2001 and the London bombings in 2005 had a negative impact on the demand side of the UK hotel industry in terms of sales and occupancy rates, the market research company “Mintel” discovered some other factors which diminished demand in the UK including high competition from American hotels in the UK market (e.g. Holiday Inn, Ramada, etc), environmental disasters (foot and mouth disease) and the exchange rates for the US Dollar and British Pound. These factors all had a negative impact on UK tourism revenues in the last few years. However, the UK hotel market is now showing good progress toward recovery because travellers are becoming less sensitive to international incidents as the years pass. Therefore, the figures for revenue and occupancy rates in the UK market have improved gradually, especially in 2006.
As mentioned in the previous section, the demand side of the hotel industry can be assessed by using several indicators. For example, revenues generated can be used as an indicator of the demand side of the UK hotel industry. Table 2.3 displays the total revenue of UK hotels from 2002 to 2006.

Table 2.3: The UK Hotel Market Revenue

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenues (£m)</th>
<th>% change year-on-year</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>10,859</td>
<td>-</td>
</tr>
<tr>
<td>2003</td>
<td>11,462</td>
<td>5.6</td>
</tr>
<tr>
<td>2004</td>
<td>12,295</td>
<td>7.3</td>
</tr>
<tr>
<td>2005</td>
<td>13,176</td>
<td>7.2</td>
</tr>
<tr>
<td>2006</td>
<td>14,000</td>
<td>6.3</td>
</tr>
</tbody>
</table>

Source: Key Note, Hotels (2007, p:10)

As shown in Table 2.3, the UK hotel market has been progressing well since 2002 in terms of sales and revenue generated. An excellent growth rate was achieved in 2006, bringing the total turnover to £14 billion for the first time. Figures in the above table indicate that the hotel industry in the UK is expanding positively year after year. In a report published by Key Note addressing UK hotel industry performance, several factors were introduced to explain this improvement in sales and revenue such as higher occupancy rates, the increased availability of room stock in the market through the establishment of new hotels, the higher prices charged in the market in the last few years since some operators upgraded their properties and moved up to 4 and 5 star hotels and positive and stable economic events and environment (Key Note, 2007).

Moreover, demand in the UK hotel market can be assessed by some other valuable indicators such as occupancy rates, average room rate and room RevPAR to give a more comprehensive picture of the hotel market as shown in Table 2.4

Table 2.4: The UK Hotel Market Statistics, 2001-2006

<table>
<thead>
<tr>
<th>Indicator</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006 (est)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Occupancy rate (%)</td>
<td>71.8</td>
<td>72.2</td>
<td>71.7</td>
<td>73.1</td>
<td>72.5</td>
<td>73.2</td>
</tr>
<tr>
<td>Average room rate (£)</td>
<td>70.05</td>
<td>68.38</td>
<td>67.86</td>
<td>73.63</td>
<td>76.45</td>
<td>79.50</td>
</tr>
<tr>
<td>Room RevPAR (£)</td>
<td>50.32</td>
<td>49.36</td>
<td>48.66</td>
<td>53.83</td>
<td>55.45</td>
<td>58.75</td>
</tr>
</tbody>
</table>

Source: Mintel, 2006 (Online Report)
Figures in the above table reveal that the room occupancy percentages varied between 2001 and 2006 with slight positive and negative movements. The above table clearly shows that the occupancy rate in 2005 was lower than the rate in 2004 due to the terrorist attacks that occurred in 2005 and negatively influenced the hotels’ occupancy by reducing number of foreigners to visit the UK. However, occupancy percentage in 2006 was higher than the rate in 2001, which means that the market as a whole is recovering. Similarly, the figures for average room rates (room revenue/ rooms sold) and Room RevPAR (total hotel income to available rooms) have risen from around £70.05 in 2001 to £79.50 in 2006 for the average room rate while RevPAR was increased from £50 in 2001 to £58 in 2006. Accordingly, the UK hotel market has recovered quickly and remarkably, and 2006 marked a golden year for the UK hotel industry in terms of all business performance indicators.

Thus, the UK hotel industry has been suffering from the negative impacts of national and international events, such as the impacts of 9/11 and the outbreak of foot and mouth disease, but the hotel industry as a whole is now showing positive trends. To put it another way, total hotel revenues have grown considerably since 2001 and have now reached a total of £14.2 billion a year, up from £10 billion at the start of the decade. In addition, recent figures have shown positive trends for hotels including occupancy rates and RevPAR.

2.5 Definition of a Budget Hotel

Before defining such an enterprise, it is worth noting that a budget hotel establishment can have several names such as a budget hotel, a limited-service hotel and an economy lodging (Senior and Morphew, 1990; Brotherton, 2004). Though this type of hotel has had a significant impact on the hospitality industry in the last decades, there is not yet a universal and comprehensive definition of the “budget hotel” in the literature. In other words, the literature has introduced different definitions, and each definition has a different focus and different characteristics. In this sense, Fiorentino (1995) argues that there is a lack of agreement among the existing definitions of the budget hotel concept, and therefore it is difficult to produce a single definition. Instead, there are several slightly different definitions for the budget hotel model.
D. Zeglat 2008

Chapter 2

The UK Budget Hotel Sector

Quest (1983), for example, describes a budget hotel as the new generation of the hospitality industry and focuses on offering limited facilities and no-frills services. Lee (1984) mentions that budget hotels offer a clean, simple room, with a telephone and television, but without room service, banquets, health clubs or other amenities. In the same journal, Bale (1984) defines a budget hotel as “a rooms-only operation, with room rates 25 to 50 percent lower than those of mid-range hotels and offering 150 rooms or fewer” (Bale, 1984, p. 12). Roper and Carmouche (1989, p. 25) describe budget hotels as “a variety of accommodation types offering rooms at proportionately lower tariff rates than the industry norms and whose facilities and services often differ both in extent and type from those defined as common to traditional full-service hotels”. In addition, Gilbert and Arnold (1989, p. 70) define this class of hotels as one that “simplifies the hotel product to give the guest a good quality core product at a reasonable price”.

Gilbert and Lockwood (1990, p.21) indicate that this kind of hotel means “a limited service lodging establishment offering the benefit of good value for money in standardised modern accommodation; quality is as good as three or four star hotels and rates cheaper, 25-30% cheaper, than average market area rates”. Senior and Morphew (1990, p. 6) refer to a budget hotel as “a 30-bedroom sleeping block located next to a roadside restaurant, or to a 300-bedroom high-rise city centre hotel, or even to a pub with bedroom extension”. Justus (1991) states that budget hotel refers to an establishment offering just the basic services and therefore no other facilities are provided (e.g. fitness centres, meeting-room facilities, food and beverage facilities, etc). As a broader and newer perspective, Fiorentino (1995, p. 461) declares that the budget hotel “is a brand new purpose-designed product concept in the hospitality industry which relies heavily on three factors; brand product concept, value for money and service consistency”. In the same perspective, Imrie and Fyall (2001) refer to the budget hotel entity as a place providing lodge service for customers with a good value for their money through charging low room rates and transparent pricing, i.e. fixed room rates are charged. In a very recent paper, Hinton (2008) refers to this class of hotels as “a hotel operation offering nightly room rental with added services beyond a continental breakfast, a meeting room, and perhaps a limited exercise facility” (Hinton, 2008, p. 47).

Based on the preceding definitions published in the literature, the budget hotel is a difficult and vague concept since it can have several aspects of services. In this regard,
Brotherton (2004) admitted that there is a difficulty in establishing a comprehensive definition of budget hotels, as can be seen in his comment "A budget hotel is not easy to define" (Brotherton, 2004, p.946). Moreover, Roper and Carmouche commented about the definition of a budget hotel "there is a lack of definitional consensus over what the product actually is" (Roper and Carmouche, 1989, p. 25).

For this reason, Fiorentino (1995) reviewed definitions that had emerged in the literature and concluded that budget hotel definitions have developed and evolved chronologically in two phases; the first phase lasted until the 1980s and defined budget hotels according to their low prices and cost strategies. This phase of definition such as Lee (1984) and Bale (1984) consider budget hotels as a very simple model of accommodation that relies on the low cost of land, construction and operation. Therefore, such hotels achieve higher economies of scale and profit. On the other hand, definitions during the second phase had the low cost-price strategy and switched to the non-price based competition strategy, offering more services without being costly and remaining a good value for the money spent (e.g. Fiorentino, 1995; Imrie and Fyall, 2001; Hinton, 2008).

To conclude, definitions of the budget hotel concept have evolved to comprise several strategies, characteristics and levels of services. This complicates the budget hotel model. Accordingly, budget hotel establishments can have several ranges and types of services. Roper and Carmouche (1989) support this view and claim that budget hotel establishments are not the same and therefore budget hotel establishments have taken on different names. For this reason, this sector has several operators offering similar provisions but with different tariff structures and facilities. In order to solve this confusion of the budget hotel concept, Roper and Carmouche (1989) suggest a system of classifications to categorise budget hotels into three different segments: lower, middle and upper budget.

2.6 Characteristics of Budget Hotels
As shown in the previous section, it is difficult to define the budget hotel concept. However, budget hotels do have common attributes and characteristics as suggested by Senior and Morphew (1990) who argue that budget hotels have broad similarities among them and share some common characteristics. In this respect, the literature identifies some generic operational characterises of budget hotels. For instance, at early stage of the
budget hotel literature, Lee (1984) discussed and summarized the main characteristics of budget hotels into a few points: (1) low construction and operating costs, (2) simple design, (3) highway locations with some exceptions in town centres and airports, (4) live-in managers plus desk clerks, (5) small size ranged between 50 and 150 guest rooms.

In a modern perspective, Brotherton (2004) provides several operational characteristics of the budget hotel concept including: (1) strongly branded product, (2) extensive geographical coverage of hotels, i.e. a broad network of hotels, (3) easily and accessible locations, (4) centralized reservation system, (5) standardized unit construction and layout of guest bedrooms, (6) fixed room rates with some discounts offered promotionally only, (7) limited service, (8) high value-for-money.

To confirm the importance of these characteristics in the budget hotel sector, Brotherton (2004) tested these characteristics by adding some extra operational and strategic factors that might help budget hotels to achieve operational success at the unit level rather than at the corporate or brand level. As a result of this factor development stage, a list of 36 items representing the most critical success factors for budget hotels was created. The findings of Brotherton’s survey indicated that there are seven dimensions that form the most critical factors for budget hotels as shown in Figure 2.1.
Figure 2.1 Critical Factors and Characteristics of Budget Hotels

Figure 2.1 indicates that there are seven dimensions essential to the budget hotel concept. Therefore these factors can help to budget hotels gain successful performance. Brotherton (2004) claims that these factors are very similar to the eight generic characteristics introduced before (shown on the previous page). According to Brotherton’s findings, these factors and characteristics are generic. However, budget hotels should not adopt all of these factors together since the budget hotel market is heterogeneous, and not all budget hotels operate at the same stage of the market/product life cycle.

In their review of budget hotels, Johnson and Clifton (1996) refer to a budget hotel as a hotel that offers rooms at low tariffs, with facilities and services that don’t match the usual situation found in any traditional hotel. They summarized the budget hotel characteristics into a few points: (1) simple mode of operations and atmosphere, (2) low and competitive room rates, (3) low construction and operation costs, (4) good-quality accommodation with good value for the money, (5) generally located in urban areas near
major road networks with easy access for customers. According to these characteristics, the budget hotel segment is considered an alternative repackaging option for the low cost accommodation properties offering low prices but systematic services after stripping out many of the services offered in conventional hotels in easy access locations. Budget hotels focus on two kinds of customers: business travellers who dominate the bedroom sales in this sector because they prefer to exploit the high standards of budget hotels rather than use a local independent hotel or guest house. On the other hand, leisure travellers normally don’t tend to stay in the hotel for the whole duration of their visit.

Senior and Morphew (1990) introduce another set of characteristics in order to define the common attributes among budget hotels including: (1) low tariff structure, (2) minimum range of facilities, (3) limited services, (4) strategic location of units near major motorway networks, (5) modern constructions. To explain further, Senior and Morphew (1990) claimed that a budget hotel should charge up to 50% lower than other 3-star hotels located in the same area. Budget hotels should also provide basic but comfortable rooms for guests. Budget hotels should employ the minimum number of staff, which means limited services. Budget hotels would be located mostly alongside major highways, while the larger units might be located in city and town centres. Finally, budget hotels should use and exploit modern methods for design and construction. As a result of these characteristics, a budget hotel can be established with good standards and only a low investment required compared to other level of hotels.

In his review of strategies for branded budget hotels, Fiorentino (1995) identified two levels of characteristics. The first level refers to the key characteristics available in these types of businesses including: (1) branded product concept, (2) value for money, (3) consistent service and product while the second level of attributes and characteristics help to reinforce and improve they key characteristics such as (1) standardization of service encounters, (2) accessible, easy-to-find and people-intensive flow locations e.g. main roads, airports, busy city centres, (3) nearby facilities (4) center reservation systems, (5) customer partnership in the service encounter. As a result of these sub-attributes, a budget hotel will improve its brand name, increase the value it offers for its customers’ money and offer a consistent service.
Drawing from Hinton’s (2008) study addressing factors that influence the purchaser’s willingness to buy a limited-service hotel in the US market, some desirable and contemporary characteristics of budget hotels can be identified including: (1) franchise affiliation, (2) attractive designs for the exterior corridor and overall building, (3) acceptable room size, (4) lower construction costs, (5) highway and metropolitan city locations.

In his comment about the customers’ needs and perceptions of budget hotels, Patrick Dempsey, the managing director of Premier Inn notes that customers in this sector are looking mainly for value for money with a clean and consistent product because they are fed up with going to hotels without knowing what level of service they are going to get. In contrast, budget hotels have consistent standards and services and offer a good value for the money. Therefore, customers have a clear view of prices, standards and policy in budget hotels (Caterer & Hotelkeeper, 2007).

Another description of budget hotels characteristics by “Mintel” shows similar characteristics, such as: (1) standardised design and appearance, (2) systematised services, (3) no-frills facilities in general with some exceptions, (4) basic but modern rooms and usually en-suite facilities, (5) no food provided, (6) room rates that can vary according to location, (7) business customers form the main customer segmentation while leisure and short break tourists served as well, especially in the weekends (Mintel, 2007).

Having shown the characteristics of budget hotels mentioned in the literature by different authors and sources, it is worth saying that no sources provide empirical validation for these characteristics from either the customer’s or the provider’s perspective, except Brotherton (2004) who did a survey in the UK budget hotel sector. As a result of his study, it is possible to match characteristics introduced in the literature with those that really exist. In addition, characteristics introduced by authors between the 1980 and 1990 (e.g. Lee, 1984) were limited and reflected an old, simple budget hotel model. Akin to definitions developed in that period, the early wave of characteristics focused only on the low cost and tariff model without addressing the brand, value and quality concepts in this sector. However, recent characteristics introduced in the literature indicate that budget hotels have expanded their model to offer more facilities and services beyond those which used to be offered in such businesses. In addition, the locations of budget hotels in recent
years have increasingly included city centres and metropolitan areas, rather than only highway roads (e.g. Fiorentino, 1995; Brotherton, 2004; Hinton, 2008).

The former paragraphs in this section show that there is an indirect debate between authors about the exact number of generic characteristics of budget hotels. In another sense, there is an agreement about the generic characteristics of budget hotels, such as low tariffs, low costs and consistent, simple services. However, new characteristics and concepts of budget hotels have emerged, including quality, value and brand as key factors. Hence, it can be assumed that characteristics of budget hotels have changed and developed, which in turn has led to a change in the strategies for success in this sector.

To conclude, budget hotels differ from other traditional hotels in terms of tariffs, bundles of services, level of facilities, and location. In order to show the operational characteristics of budget hotels, the points below indicate their main features.

- Clean, comfortable room.
- Branded network of hotels.
- Consistency and standardized services.
- Lower tariffs than charged for similar accommodation in similar areas.
- Modern designs and construction.
- Low construction and operation costs.
- Reduced facilities and services while providing sufficient staff and comfortable equipment.
- Target mostly business and leisure travellers.
- Easily accessible locations.
- Catering is usually provided by an adjacent food operation.
- Fixed and transparent price.

2.7 The UK Budget Hotel Sector

In the 1970s, some major hotels in UK could not cope with the high construction and upgrade expenses that occurred in response to increasing demand by customers. As a result, those operators had to raise their tariffs beyond their customers’ ability to pay. In the mean time, a quite large number of small hotels in the UK could not keep their properties up to their customers’ expectation. Therefore, small operators found
themselves unable to provide a consistent, high level of services. This lead them to leave the market as their hotels were unable to offer good, consistent products and services at low tariffs. This status of the market forced several government organisations to encourage hoteliers in the UK to simulate the French hotel industry experience by offering budget hotels in the UK (Roper and Carmouche, 1989; Senior and Morphew, 1990).

Until 1985, British hoteliers were not keen on adopting and offering low priced accommodations. In contrast, overseas operators anticipated the need for accommodation services at budget prices in the UK. For example, a French chain (Ibis) recognised the need for low tariff accommodations, and therefore opened the first budget unit in 1985 at London Heathrow Airport. Sometime later in the same year, a few budget hotels were created in different parts in the country by chains such as Travelodge. Owing to the increase in business and short-break domestic travellers, as well as increasing operation costs, the budget hotel concept has been adopted quickly in the UK market (Gilbert and Lockwood, 1990). That is, the main motivation behind the budget hotel appearance in the UK was to offer accommodations at more attractive rates than existing full service hotels with minimum facilities (Callan and Lefebce, 1997). In addition, hoteliers in the UK responded directly to the business and leisure travellers’ need for accommodations on a limited budget (Harris, 2001).

Budget hotels have been developed as an equivalent market to that of low cost airlines which have made a major impact on tourism in Europe and in the UK in particular. It is noteworthy that the development of the budget sector was also influenced by motel chains in the USA. For example, Travelodge brought from the US market into the UK market (Key Note-Top Markets; Travel and Tourism, 2007). Budget hotel establishments in the UK focused initially on roadside and suburban locations. More recently, this class of hotels became well represented in London and the majority of the city centres across the country, to target different kinds of travellers and families.

As a result of the spread of this sector in the UK, the budget hotel sector now has several levels of hotels within the same market located in different areas across the country, including London, motorways, city centres, town centres and airports. Harris (2001) describes, in his paper about factors influencing the growth of budget hotels in USA and
France, the growth of this sector in the UK as a consistent and significant growth. In addition, he states that the growth of the UK sector was accelerated and dominated by two brands (Travel Inn and Travelodge) through exploiting landbanks located next to their restaurants, i.e. bedroom products were added to their branded food and beverage outlets. However, new brands of budget hotels have entered the market such as Express by Holiday Inn, Days Inn, etc.

As a result of the new players in the sector, budget hotels vary according to the services and facilities offered which leads to the division of budget hotels into several tiers. This tier structure was developed to reduce overlap among budget hotels in terms of tariff and services and to serve as a guide for customers (Senior and Morphew, 1990). In this sense, Roper and Carmouche (1989) developed a framework for categorizing the budget hotel sector into more homogeneous segmentations including (1) new-system budget hotels which rely on low construction costs, simplified operational systems, small-sized units, low tariff rates, no discount policy, no additional profit outlets and no product differentiation policy. The most popular brand in this segment is Formula 1. (2) Traditional budget hotels form the most popular segment in the sector. Hotels in this segment provide accommodations adjacent to food and beverage outlets, offer discounts, make additional profit areas available (e.g. conference), make public areas available, offer flexible and standardized services and products. This segment has very well known brands such as Premier Inn and Travelodge (3) This segment contains upper-tier budget hotels which developed due to the development and expansion of products in home markets such as Accor and Express by Holiday Inn. Hotels in this upper segment offer discounts, provide minimum public areas and some additional profit areas (e.g. conference, banquette leisure) to make their tariff perceived as highly value added.

Having shown the historical development of this sector in the UK, it is worth discussing the growth of this sector over the last decades. In this sense, the budget hotel sector has rapidly become one of the fastest growing sectors in the UK hospitality industry. The budget hotel sector has been one of the greatest success stories in the UK hospitality industry over the last 10-15 years, and continues to be so (Brotherton, 2004, p. 944). The growth of this sector covers two sides: the supply side as well as the demand side. Experts and consultant companies predicted this growth well in advance. For example, Deloitte & Touche (2000) expected more than new 500 units to be available in the market by 2000.
Fortunately, the number of units offered at that time was behind this expectation. To put it another way, the number of units available in 2002 was 933 (Deloitte & Touche, 2003), and then this number grew to 1171 units in 2007 (TRI, 2007). Due to the growth of this sector, operators from other classes are planning to enter the budget hotel sector. For instance, the luxury brand "Rezidor group" is planning to enter the budget hotel sector through opening a colourful and very happy budget hotel to overcome shortcomings in the market (Sharkey, 2008a). According to Kurt Ritter, the chief executive and president of the group, "Rivals' offerings are boring and depressing".

In terms of the contribution of this sector to the total UK hotel industry, significant results were achieved. For example, the UK budget hotel sector accounts for nearly 9% of value and 13.6% of capacity of the overall UK hotel market (Mintel, 2007). According to Melvin Gold, a consultant in the UK hotel industry, the share of the budget sector will be doubled in the next two decades to arrive at 26.8% of the total UK hotel industry (Kuhn, 2007). However, some other resources such the Business Development Research Consultants (BDRC) announced that the share of the budget hotel sector within the domestic hotel market in the UK was around 35.8% in 2007 (Sharkey, 2008b).

After displaying the historical background, growth and importance of the UK budget hotels sector and its contribution to the total UK hotel market, the next sub-sections will shed more light on the supply and demand sides of the UK budget hotel sector.

2.7.1 The Supply of the UK Budget Hotel Sector

Reports about the budget hotel sector in UK indicate that this sector is considered one of the largest and fastest-growing segments within the UK hospitality industry (Brotherton, 2004). To put it another way, the number of UK Budget hotels in 1992 was 193, with 7326 rooms total (Deloitte & Touche, 2003). In 2006, this sector had 70000 rooms operating in a wide range of locations and markets, and in 2007, 15000 more rooms were added to yield 85000 rooms in total. Deloitte & Touche noted that the budget hotel sector in the UK was valued at more than £3 billion in 2006 (Key Note-Top Markets; Travel and Tourism, 2007; TRI, 2007). In the next few years, the key players in the market will add 23000 additional rooms. Table 2.5 shows figures regarding the number of units and rooms available in the branded budget hotel sector in the UK in 2007.
The above table shows that the budget hotel sector has doubled its room stock comparing to figures announced ten years ago. Moreover, Table 2.5 indicates that the Premier Inn and Travelodge hotels dominate the UK budget hotel sector in terms of number of units and rooms, providing 38.2% and 22.6% of the market respectively. Together, Premier Inn and Travelodge represents 60% of the total sector supply. To put it more simply, a small number of franchises of budget hotels operate the majority of units within the country. However, other brands are operating in the market such as Etap from Accor, Yotel and Easyhotel, etc.
The budget hotels listed in Table 2.5 can not be classified into the same levels as discussed before. In other words, because of changes that have happened in this sector in the last decade, budget hotels in UK are categorised into different classes. In a survey done by Deloitte & Touche (2003), operators in the budget hotel sector categorised their hotels into three groups and segments: the upper-tier segment which includes budget hotels providing more services and facilities than others. This sub-segment comprises hotels located at one end of the sector’s scale (e.g. Express by Holiday Inn) while the mid-tier segment offers some services and amenities but not as much as the upper-tier (e.g. Travelodge and Premier Inn) and finally the lower-tier segment which provides very basic services, such as Formula 1 (Deloitte & Touche, 2003).

In order to support the figures appearing in Table 2.5, the Table below indicates that positive changes have occurred in the UK budget hotel sector. For example, the number of budget hotels has increased by 43% since 2001 and now stands at 1171. Moreover, the average size of hotels has increased 14% to arrive at 73 rooms per hotel (Mintel, 2007). To make it easy to track changes in this sector in the last few years, Table 2.6 shows changes for UK branded budget hotels in 2005 and 2006.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Hotels</th>
<th>Average Number of Rooms</th>
<th>Number of Budget Hotel Rooms</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>818</td>
<td>64</td>
<td>52,452</td>
</tr>
<tr>
<td>2002</td>
<td>933</td>
<td>61</td>
<td>57,022</td>
</tr>
<tr>
<td>2003</td>
<td>979</td>
<td>64</td>
<td>63,043</td>
</tr>
<tr>
<td>2004</td>
<td>1,066</td>
<td>65</td>
<td>69,276</td>
</tr>
<tr>
<td>2005 (est)</td>
<td>1,104</td>
<td>69</td>
<td>75,794</td>
</tr>
<tr>
<td>2006 (est)</td>
<td>1,137</td>
<td>71</td>
<td>80,972</td>
</tr>
<tr>
<td>2007 (est)</td>
<td>1,117</td>
<td>73</td>
<td>85,665</td>
</tr>
</tbody>
</table>

Source: Mintel, Budget Hotels (2007, p: 33 and 34)

According to Table 2.6, it is worth saying that the development of this sector refers to a positive trend for all indicators of the supply side over the last few years. Moreover, the number of rooms has grown rapidly, nearly doubling the number of rooms that is now available in the market (Mintel, 2007). However, the TRI consultant team announces that
the budget hotel sector is not mature yet and will have more expansion in the coming years for several reasons (TRI, 2007):

1. Investors and lenders are interested in this sector due to its strong brands and the simplicity of its business model in terms of location, cost, strong cash flow and continuous growth in asset value.
2. Contemporary construction techniques have a positive impact on time and cost savings.
3. A remarkable number of leisure customers are still not tapped into this sector.

2.7.2 Demand for the UK Budget Hotel Sector

Having shown the significant growth of the supply side of the budget hotel sector in the UK, the current section aims to illustrate the demand side of the budget sector to provide more details about its performance. Before doing so, it is necessary to explain the reason for the huge demand achieved in this sector in the last few years. Deloitte & Touche (2004) announced that the growth of internet usage as a booking tool, the recovery of the London market, an increase in marketing activities and an increase in brand distribution have all improved the demand for this sector. On the other hand, TRI (2007) attributed the strong demand for this sector to other factors: strong supply and distribution of this sector led to the creation of an expectation of availability and an awareness of the sector in customers' minds, low costs, a consistent value for the money spent, accommodation services relevant to the customers' needs and, finally, the online distribution system (TRI, 2007). Accordingly, the internet revolution and the offering of consistent, branded hotels encouraged customers to patronize this sector and in turn increased the demand.

As mentioned in section 2.4.1, although they provide limited interpretation for changes in supply and demand patterns, Phillips (1997) states that the discussion of the demand side should cover indicators including revenues, occupancy percentages, room rates and room nights sold. To start with revenues generated, budget hotels in the UK have witnessed a massive improvement in sales and revenues over the last ten years. As a result, the business performance of hotels within this sector experienced a similar gain. To put it another way, total rooms revenue which forms the vast majority of sales and revenue in this sector has broken the £1 billion barrier for the first time since 2000. Figure 2.2 shows total rooms revenue for budget hotels over the last seven years.
Figure 2.2 Total Rooms Revenue from Budget Hotels for the Period (2000-2006)

Figure 2.1 shows that total rooms revenue exceeded the £1 billion barrier in 2006. Since 2000, revenues have increased by nearly 50% to over £1 billion in the year 2007. In addition, it is expected by some industry consultants that sales value will increase additionally. Mintel, for instance, as a market research company declared that revenues generated from the budget hotel sector in the UK will arrive at approximately £1.5 billion in 2012 (Mintel, 2007). On the other hand, the other indicators of demand such as occupancy percentages, average room rates and RevPAR revealed improvements, as shown on Table 2.7.

Table 2.7 The UK Budget Hotel Market Statistics, 2005-2007

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>% Change 2005-07</th>
</tr>
</thead>
<tbody>
<tr>
<td>Room Occupancy %</td>
<td>71.07</td>
<td>72.81</td>
<td>72.73</td>
<td>+1.66</td>
</tr>
<tr>
<td>Average room rate £</td>
<td>47.14</td>
<td>48.35</td>
<td>49.98</td>
<td>+6</td>
</tr>
<tr>
<td>RevPAR £</td>
<td>33.50</td>
<td>35.21</td>
<td>36.35</td>
<td>+8</td>
</tr>
</tbody>
</table>

Source: Mintel, Budget Hotels (2007, p: 34; 35)

Table 2.7 reveals that the overall trend for demand in the UK budget sector has been going in a positive direction. In contrast to the overall UK hotel industry, occupancy percentages in the UK budget hotel sector did not change substantially as happened in the
overall UK hotel industry as shown on Table 2.4. In other words, the growth rates for the three indicators show a positive direction for budget hotels in the UK. Therefore, it can be assumed that this sector is outperforming the total UK hotel industry.

According to the positive indicators and performance of the UK budget hotel sector, this sector has moved toward maturity. In other words, this sector is now enjoying high occupancy rates and a wide range of geographical coverage remote from the sector's roadside origins. TRI consulting group (2007) states that the budget hotel sector achieved occupancy results slightly higher than the UK full services hotels in 2006 which implies a strong competition between budget hotels and the total UK hotel industry.

In terms of the customers using this sector, business travellers form the main group of users for this sector in the UK. Thus, business travellers have been a significant factor in the success of the budget hotel sector, according to room nights made by business travellers. This segment of customers generated 57 million room nights in budget hotels in 2006 (Key Note, 2007). Figure 2.3 shows the percentages of different kinds of customers and guests who used this sector of hotels in the UK in 2004.

![Figure 2.3 Customer Segmentation in the UK Budget Hotel Sector](image)

**Source:** Deloitte & Touche, Budget Hotel Survey (2004, p: 8)

Although the former figure shows the importance of business travellers comparing to other customer segments in the UK budget hotel sector, Figure 2.3 also indicates that the budget hotels serve quite a good proportion of leisure customers and guests visiting for
tourist and entertainment reasons. According to TRI consulting group (2007), the leisure travel segment has increased its engagement and contribution to the budget sector through increasing the number of users as well as the number of room nights sold from 2006 until now. Hence, this growth of leisure travellers is a positive sign for the budget sector.

In contrast to the percentages displayed in Figure 2.3, the latest statistics regarding customers using budget hotels indicate something different. For instance, the leader among budget hotel chains in the UK, “Premier Inn,” recently announced that 55% of its sales came from leisure travellers while only 45% of sales came from business travellers (Allen, 2008). However, operators in this sector believe that the decline of travel expenses has encouraged companies to use budget hotels instead of full-service hotels. According to Alan Parker, the chief executive of Whitbread, “Companies are trading down in terms of travel expenses. They have found that they do not need to pay £150 per night when (an employee) can stay in Premier Inn for £50” (Blitz, 2007).

In light of the discussions in the previous two sections (supply and demand), the significant growth and expansion of the budget hotel sector in the UK has been demonstrated. The discussions of the supply and demand sides of the UK budget hotel sector highlight the positive growth of this sector in terms of the number of units and rooms opened in the last few years. In addition, sales, revenues and other operational figures such as occupancy rates indicate that this sector is giving good returns to owners and shareholders. As shown earlier, the revenues of the UK budget hotels increased by nearly 50% between 2000 and 2006, to reach £1 billion GBP. According to experts, the budget hotel sector is going to grow further and further in the next few years.

2.8 New Dynamic Trends and Issues in the UK Budget Hotel Sector

Having introduced the common characteristics as well as supply and demand sides of the budget hotel sector in the UK, this section aims to discuss the changes and developments that have occurred in the budget sector as a reaction to the challenges that emerged over the last 10-15 years. As a result of these challenges, operators had to change the main strategies adopted previously in the sector. Intense competition and growth in this sector forced the operators of budget hotels in the UK to change their original strategies to attain a competitive advantage in the market. This idea to modify the current characteristics and develop new strategies was required by the academic and industry community.
In early 1990s, Senior and Morphew opened the debate over new strategies for success in this sector. They stated that budget hotels should change their old competitive strategies (e.g. low price) and suggested operators rely increasingly on service quality as stated in their comment "Long term commercial success will not be achieved on price-cutting or product augmentation strategies, but could be achieved on providing service quality" (Senior and Morphew, 1990, p. 8). Thus, early in the last decade, operators were advised to change their strategies and move from a short-term to a long term perspective. Besides the service quality recommendation, Senior and Morphew (1990) also suggested that operators adopt a differentiation strategy to differentiate one brand name from all other competitors in the marketplace. In addition, Senior and Morphew recommended operators focus on smaller market segments, instead of serving the whole market, and modify their service packages to meet their customer segmentation strategy.

Similarly to Senior and Morphew, the differentiation strategy was recommended also by Fiorentino (1995) who claimed that budget hotels should differentiate themselves from others, stay away from competition through building and gain a strong brand name in the market. Fiorentino (1995) suggested another strategy to overcome competition and new economic and environmental changes happening in the world (e.g. globalization and changes in consumer behaviour) through adopting several strategies, such as mergers, acquisitions, franchising, joint ventures and strategic alliances in order to overcome challenges.

Currently, the budget hotel sector in the UK is facing some challenges including high competition, market saturation, economic slowdown and uncertainty, continuation of new entrants into the market, limited and similar product and service range across brands, increasing customer expectations and, finally, the availability of funds from different financial institutions (Deloitte & Touche, 2002; 2003, TRI, 2007; Mintel, 2007). Considering these challenges within the UK budget hotel sector, operators have to compete more effectively in the market through changing their old strategies in order to survive. The following paragraphs discuss some of these strategies emerging in the sector.

First, the product modification and differentiation strategy: the growth and high competition within the UK budget hotel sector have forced many operators in the sector
to modify their products and services. Thus, the low price strategy alone is not valid any more due to high competition. Hoteliers have to change their products and services. Accordingly, the product modification strategy has emerged as a new trend in the sector. For example, the amenity creep concept has become the priority for several budget hotels in the UK market to meet the needs of their longer-stay visitors and business travellers by adding more facilities and services such as aircondition, sky TV, internet connections and direct-dial telephones, etc (Deloitte & Touche, 2002; 2003).

This strategy suggests that some operators need to modify services and products offered in their hotels through adding some extra or unusual facilities and services in order to survive and compete in the market. According to Delloitte & Touche (2002), some operators have changed their services, such as Express by Holiday Inn “Today, at one end of the scale, there are Sleep Inn and Express by Holiday Inn, offering, for example, air conditioning, bar facilities and satellite television” (Delloitte & Touche, 2002, p.15).

Harris (2001) also supported this view and stated that budget hotels should improve and expand their products and services to respond to new customers’ needs and competition. As a result of this reaction, the upper economy segment emerged as a key segment in the UK budget hotel sector. Clearly, this sub-sector added new essential amenities and services (e.g. satellite TV, Plasma screens, electronic locks on all bedrooms doors, ensuite bathrooms, and wireless internet access) at a price below the mid-market and full-service hotels.

This strategy of upgrading and modifying services was adopted by some operators in the sector to gain more market share, instead of using only the low-price strategy, as said by Danny Thompson, the franchise development manager of Sleep Inn:

“Price is still of maximum importance, but increasingly there are niches developing within the sector to include lower, middle and superior budget products. It seems inevitable, as the customers become more demanding that some of the basic hotels will need to upgrade their offering or lose market share” (Deloitte & Touche, 2002, p. 17).

However, this strategy was not fully adopted by all the operators in this sector. In their budget hotel survey about product modifications, Deloitte & Touche (2002) found that
some budget hotels did not change and do not have any intention of modifying their services.

Although Brotherton (2004) recommends budget hotels to adopt this strategy (adding additional services and facilities) to achieve operational and brand success, he said that this approach may be risky since it is easily copied by competitors and may diminish returns. However, Brotherton claims that budget hoteliers can use the concept of quality and value to differentiate their offers from others and achieve a greater competitive advantage. Thus, Brotherton (2004) emphasizes the role of service quality in achieving a better competitive advantage for budget hotels.

According to these changes, it was claimed that due to the modification of offers and services in the budget hotel sector, it can no longer be called budget sector. Instead, the upper class hotels should be called full-service hotels. Fiorentino (1995) predicts that budget hotels of the future will be focusing mainly on the middle and lower classifications while the upper scale of budget hotels will be engaged in full-service three-star hotels and therefore will not be called budget hotel. However, some players in the budget hotel sector do not worry about these segmentations as long as their customers are satisfied. For example, Michael Brooker, the managing director of the Hoxton hotel, commented about this debate, "Are we premium budget or limited service? I don't know and I don't care. Our customers are happy. It's not important to them" (TRI, 2007, p.5).

Also due to this strategy, a luxury budget hotel product emerged recently in the UK that includes new services and products such as an air-conditioned room, double sofa beds, pull-down-desks, WI-FI internet access, flat-screen plasma TVs, power showers, etc. Prices in this sub-sector are higher than traditional budget hotels, but still lower than full service hotels. Some operators in this sub-segment can be called "boutique, budget or lifestyle brands". Operators in this new segment of the budget hotel sector comprise different brand names such as Yotel, Nitenite, The Big Sleep and Base2stay. Some operators in this segment brought ideas for their new budget hotel products from other industries. For instance, Simon Woodroffe, the founder of Yotel, translated the concept of a luxury airline into a capsule-style hotel. Operators claim that their hotels provide low-cost and luxury accommodations (Webster, 2006).
In this respect, Churchill (2006) attributes this emerging wave of stylish budget hotels to the fact that customers and guests requested more facilities be provided by normal budget operators (e.g. Travelodge) and found offers and services in the upper tier (e.g. Express by Holiday Inn) too ordinary, but they can't afford prices charged in four and five-star hotels. Thus, the new operators (e.g. Yotel, Base2stay) are aiming to create more services and value for customers at affordable prices. However, the hotel consultant Melvin Gold claims that despite this new trend, operators can't move far beyond the sector's fundamentals of convenient locations and pricing options (Churchill, 2006). In this respect also, Chetwynd (2008) asserts that the business model of the budget hotel sector is based on the no frills principle and should not go too far beyond this principle. Otherwise, the budget hotel will lose its low-cost characteristics.

Within this strategy, operators have adopted several different offers. Travelodge, for instance, is now offering a new service by providing five smells on customers' pillows and sheets including sea, freshly cut grass, baby powder, and home-baked apple pie. This idea was first launched in five locations of Travelodge hotels. The company said that this service could remind guests of their comfortable memories (Meikle, 2008).

Considering these changes in the products and services offering, budget hotels are no longer cheap hotels. In this regard, Sharkey (2008b) reports that getting a room from Premier Inn in London's King Cross Station, for instance, costs around £100 a night. She claims that people may use a budget hotel in order to save money, but this assumption doesn't mean that prices in the budget hotel sector should be close to the bottom end of the market. Thus, budget hotels have now changed from simple models to newly attractive models in terms of design, features and services.

Second, the brand strength strategy: operators in the UK budget sector believe that increasing the competition, segmentation, usage and awareness of budget hotels forced them to establish strong, well-known brands to avoid these threats and to isolate them from other competitors (Deloitte & Touche, 2002). In other words, building a strong brand has emerged as a significant strategy for the success of the budget hotel sector. According to Grant Hearn, the CEO of Travelodge, budget hoteliers are retailers and not owners of hotels, and therefore they have to strengthen their brands. Thus, brand strength
became one of the valuable tools used by players in the budget hotel sector to overcome competition (TRI, 2007).

In this sense, Stanley and McCaskey (1999) claim that the winners in the budget hotel sector will be those who can build the strongest brands through improving and reinforcing the value-for-money and differentiation strategies. In addition, they identify the quality of service concept as a key tool for building and reinforcing the brand and value position.

Similar tools are suggested by Delloitte & Touche (2002) to improve the brand of budget hotels. Deloitte & Touches found that several factors and methods can lead to brand strength in the budget hotel sector including value for money, consistency, central reservation system, restaurant offering and competitive pricing. However, the value for money and service consistency were the most important factors in achieving brand strength from the operators’ perspective.

McCaskey and Symes, (2004) in their paper about Travel Inn’s satisfaction programme (now called Premier Inn), describe the UK budget hotel sector as being in a period of exponential growth and maturity. In this sense, they claim that the best strategy at this stage of the product/service lifecycle should be associated with the unique brand and differentiation strategies which will in turn lead to strong brand loyalty. To do so, the Travel Inn Company launched a special programme called “100% satisfaction guarantee or your money back” in 2001 to differentiate their brand from their competitors’ and to sustain their position as a leader in the market. The marketing implication for this brand strength strategy was to reduce the risk element of the purchase decision for new customers and increase the long-term loyalty of the current customers.

Third, the franchising strategy: in their review of the growth of international hotel chains in Europe, Slattery, Gamse and Roper (2008) claim that since 2000 the affiliation structure of the hotel industry in Europe has changed from brands owning and leasing hotels to management contracts and franchise methods. They attribute these changes to three reasons. First, hotel chains that owned and leased their hotels especially in the UK were more likely to face higher risks and lower returns on their investments than chains involved in management contracts and franchise methods. Second, the new players in the hotel industry such as real estate funds and private equity funds use more sophisticated
risk and return criteria. Third, the huge expansion of the hotel market in Europe in terms
of both size and demand made it impossible for hotel owners to fund this expansion with
only their internal equity resources. Parallel to the whole market in Europe, the
franchising strategy has emerged as a significant tool for funding and managing the
budget hotel sector in the UK as suggested before by Fiorentino (1995).

According to Lawrence Alexander, the chief executive officer of easyhotel, the franchise
strategy has emerged as a vital tool for expanding this sector as mentioned in his
comment, "I think there is a huge opportunity for the budget sector to franchise. Not only
is service limited for the customer, but it is also limited involvement from the owner" (TRI, 2007, p.15). In addition, Danny Thompson, the franchise development manager of
Sleep Inn supported using this strategy in the UK budget hotel sector as shown in his
comment "We believe that franchising will become more important in the sector as key
brands, including our own Sleep Inn superior product, strive to achieve nation-wide
distribution even more quickly" (Delloitte & Touche, 2002, P. 17.)

Fourth, location and coverage: the budget hotel sector has recently witnessed some other
changes in terms of the locations and coverage of units. Initially, the budget hotel concept
was created to operate mainly on the roadside networks. However, the new trend of
budget hotels has been a change to attract other locations including the capital and central
cities more widely than before. To be more precise, the budget hotel sector in the UK has
changed its strategy in terms of location and coverage to be in more different locations
rather than concentrating only on motorway areas. Hence, the budget hotel concept is
now trying to serve the whole market by offering affordable budget hotels. According to
Grant Hearn, the chief executive of Travelodge, "We've moved away from the road
network- it now presents only 5% of our portfolio- and are developing city-centre and
urban locations" (Caterer & Hotelkeeper, 2007, p.9).

In an article about the growth of budget hotels in London, Chesshyre (2008) attributes the
growth of budget hotels in the capital and other city centres in the UK to the fact that
operators of budget hotels need to attract more and different kinds of customers. In
addition, travellers who use cheap flights need to have cheap accommodations in city
centre locations. In this sense also, Hearn told the Caterer & Hotelkeeper magazine
"While 60% of the UK population stay away from home every year, only 30% stay in
hotels. We're trying to increase the share of the pie and grow the size of the overall pie” (Caterer & Hotelkeeper, 2007).

British budget hotels have therefore moved their interest to the capital. In this sense, Alan Parker, the Whitbread's chief executive, says: “The capital is an important focus for Premier Inn. There is a growing need for high quality, affordable accommodation. Our further pipeline will position us as the largest hotel chain in London with at least 8,500 rooms before the Olympics in 2012” (Walsh, 2008, p. 45). In his comment about the new trends in budget hotel locations, Parsons also says that budget hotels look better now than ever before and can be found in more appealing places (Sharkey, 2008b). As a result of this trend, the average size of hotels has grown to around 70 rooms instead of 20-40 rooms, and having 400-500 rooms in the London area become normal (McCaskey and Symes, 2004).

Moreover, the UK budget sector has recently shown new trends for international markets. In other words, the key players in the UK budget hotel sector are moving internationally. For instance, Travelodge is planning to open 100 hotels in Spain by 2020. Moreover, Premier Inn has entered the Middle Eastern market after opening a budget hotel (308-room) in the Dubai market (Blitz, 2007).

2.9 Conclusions

Discussions introduced in this chapter revealed that the UK hotel industry had been suffering from threats, such as fear of terrorism, foot-and-mouth disease, the downturn in international travel and the high level of competition among hotels. All of these threats forced numerous hotels to close down. However, the discussion concerning the supply and demand of the overall UK hotel industry indicates a recovery for the industry since 2004 until the present. The UK hotel industry is considered a mature and important industry within the global market. A number of the major international hotel brands are owned by British groups and companies. Furthermore, the UK hotel industry includes all classifications of hotels such as low, budget, mid-market, upscale and luxury hotels.

In terms of the UK budget hotel sector, this chapter showed that the sector has experienced a rapid growth in the number of units and rooms. Currently, the UK budget hotel sector is one of the fastest growing sectors in the UK. This class of hotels represents a popular sector within the UK hotel industry, due to its favourable characteristics.
This chapter displayed several definitions of the budget hotel concept introduced in the literature. Discussion included in this chapter revealed that there is no single definition of the budget hotel. However, the relevant literature indicates that definitions of budget hotels have developed over the last decades. In other words, the old definitions of budget hotels focused on the low price and cost features of budget hotels, while the contemporary definitions focus more on the services and facilities offered in such an establishment at a high level of quality and value for customers. In addition, the discussion introduced in this chapter regarding the characteristics of budget hotels revealed that there is a debate between authors about the exact number of generic characteristics of budget hotels. The literature included in this chapter implies that the characteristics of budget hotels have developed over the last decades.

Moreover, this chapter highlighted the superior performance of the budget hotel sector in the UK in the last ten years. However, experts are predicting even more positive performance by this sector in the next few years. This chapter explored the dynamic new strategies and trends that have occurred in this sector in the last decade. In this sense, it can be assumed that the budget hotels in the UK currently rely on some contemporary strategies including product modification and differentiation, brand strengths and identity, franchising and wider coverage and locations of units. The discussion in this chapter shows that the concepts of service quality and value form the main tool for achieving brand strength and differentiation strategies for hotels in this sector.

According to the new trends, budget hotels in the UK have extended their models to do something beyond the low-cost model originally brought from the low cost airline model. In other words, the budget hotel sector in the UK relies on service quality and value for money, a branded chain management approach, product modification and brand strength strategies to compete in the market. However, this chapter found that although the concept of service quality has emerged since 1990 as a key tool for success in this sector, the literature did not give enough attention to this concept in the budget hotel sector.

Despite this growth, the academic literature did not give this sector sufficient analysis to understand its strategies. This lack of attention by the academic community was made clear through the small number of papers published about this sector as claimed by
Brotherton (2004) "Given the vibrancy and growth in this sector of the UK hotel industry, on which relatively limited research has been conducted" (Brotherton, 2004, p. 944).
Chapter 3

The Theory of Service Quality
3.1 Introduction
The term of quality has been developed according to the belief that customer service is a key requirement for gaining competitive differentiation strategy. Customers have become more willing to change and shift their loyalties and choices between companies. As a result, quality policy has emerged as a fundamental tool for an organization to differentiate itself over its competitors (Harrington and Akehurst, 2000). The huge (and still growing) importance of service sector in the world leads to increased need for quality improvements in this sector. As a result, quality of service is widely discussed, and it is considered in the literature as a critical competitive strategy (Rust and Oliver, 1994; Morgan and Piercy, 1996).

According to this importance of the quality and service concepts, the main objective of this chapter is to review key issues in the service quality literature. Thus, this chapter reviews definitions of quality, characteristics of service, dimensions of service quality, models of service quality, service quality measurements and quality of service in the hospitality industry, in order to understand the link between quality and profitability.

3.2 Definitions of Quality
Differing perspectives and viewpoints were developed in the literature to explain and define the term of quality. As a result, several and different meanings and definitions of this concept were introduced in the literature. This confusion leads to make it hard to decide which definition is the best and valid. In other words, each definition has different focus and perspective.

As a simple and single definition of quality, Crosby (1979) refers to the quality concept as a conformance to requirements. In other words, quality means consistency to a previously set of specifications and requirements. Crosby claims that each product should meet these specifications. However, such definition is really simple and ignores other
aspects or elements of quality such as acceptance and perceptions of customers in the market.

In order to overcome limited and narrow definition of quality, Deming (1984) classifies quality definitions into three different groups. The first definition group, quality of design/redesign, relates to how well a company can produce an item, according to information gathered from customers and market research. The second group, quality of conformance, indicates how well a company and its suppliers can meet their customer's specifications and requirements in order to satisfy them. Finally, the third group, quality of performance, refers to how well the firm's products work in the market.

As a broader perspective of defining quality, Garvin (1984) reorganized quality definitions used by researchers into five different groups: (1) Transcendent quality, (2) Manufacturing quality, (3) Product-based quality, (4) User-based quality, and (5) Value based quality.

For the first perspective, (transcendent quality) refers to the overall and innate excellence of a product, or the ability to produce uncompromising standards. Obviously, this perspective makes quality something difficult to define precisely. The second perspective (manufacturing-based quality) indicates conformance to design requirements and design specifications, which in turn leads to the lowest defect rates. Clearly, such definitions are involved in engineering and manufacturing practices. However, the third perspective (product-based quality) refers to the number of required and desired attributes and characteristics in products. For this group quality is a measurable and computable variable. As a unique perspective, the fourth perspective of definition (user-based quality) implies the achievement and fulfilment of individual users' needs and wants, which in turn leads to their greatest satisfaction. Thus, this definition of quality illustrates and evaluates quality as a subjective item. The final perspective (value-based quality) indicates that quality means the product's fitness for use at an acceptable and suitable price, in other words, the degree to which it is 'excellent' and worthy at an acceptable cost and price. The final perspective of definition is considered an extension of the user-based quality definition.
Instead of offering a new definition of quality, Forker (1991) acknowledges the user-based quality perspective as discussed by Garvin and claims that this definition forms the best definition. Forker (1991) states that the support for this perspective based on the fact that fulfilling and satisfying the customers' needs form the ultimate judge of quality. In the meantime, even if a product conforms to specifications defined by managers and engineers, it may not reflect customers' needs.

On the other hand, Hardie (1998) in his effort to illustrate the theoretical and empirical models of the link between quality and business performance, he categorises different definitions introduced in the literature into five groups of definitions shown below;

1. Conformance to requirements: indicates how the product or service will match production standards and conditions.
2. Fitness for use: shows if the product or service will do the intended job or function.
3. Meeting customers' expectations: displays how much the product or service will meet the current expectations of customers.
4. Exceeding customers' expectations: illuminates how the product or service will go beyond the current customer expectations.
5. Superiority to competitors: how the product or service will match and overcome competitors' products.

It is obvious from the above definitions classified by Hardie (1998) that quality can be grouped into two main groups, on the one hand, the first group focuses on the manufacturing perspective (including the first and second definitions) and can be measured by the company inspection tools, on the other hand, the second group of definitions (including the third, fourth and fifth definitions) relays on the customers' judgements and assessment of quality. Thus, measuring quality according to Hardie can be conducted internally and externally, objectively and subjectively.

One of the new definitions of quality emerged in the literature; Kasper, Helsdingen, and Gabbott (2006) consider and emphasize the idea that quality means value. According to their perspective, defining quality relays on the comparison between the customers' perception of price s/he paid and what benefit obtained. In other words, this perspective
indicates that customer evaluates quality based on the differences between the customer’s investments in acquiring or using a product and benefits perceived (Kasper et al., 2006). Thus, quality, within this definition implies a ratio between what customers get and what price s/he paid.

In order to categorise definition of quality, Seawright and Young (1996) addressed the issues of variation in quality definitions by developing a continuum which gradually combined different definitions. To put it more simply, this graphical framework categorises quality definitions into five groups according to two criteria: the first sorts definitions based on the internal or external scope of quality, while the second arranges these definitions from objective to subjective in their evaluation of quality. Figure 3.1 shows the quality definitions continuum.

![Figure 3.1 Quality Definitions Continuum](image)

**Source:** Seawright and Young (1996, p: 112)

Figure 3.1 shows that different quality definitions can be extracted from five different perspectives. In other words, the continuum shows how each group of quality definitions can sequentially affect the next one. This framework arranges the groups of definitions starting from internal perspectives and progressing to the external perspectives. This classification shows how these groups of definitions work consecutively and also that each group contributes to jointly achieve a competitive advantage. In other words, when any item is produced to good specifications and conditions (manufacturing-based quality) it will have favourable characteristics and attributes (product-based quality). Then, it will meet customer’s needs (user-based quality) and satisfy them at a suitable price (value-based quality). As a result, a company with high quality items will likely increase its
market share and profits (strategic quality). Thus, the appropriate operations are the essential procedures to accomplish a high level of external outcome.

In light of preceding discussion in this section, it seems that introducing one single definition of quality is not possible. In other words, the discussion in this section indicates inconsistency and diversity for defining the quality concept. As a result, it can be concluded and confirmed that there is no universal and comprehensive definition of quality that can be used in all businesses and settings. In this regard, Reeves and Bednar (1994) argue that quality concept is a vague concept which includes different meanings and interpretations. For this reason, it is better to use and consider several definitions of quality as shown above (e.g. Deming, 1984; Garvin, 1984; Hardie, 1998) instead of relaying on one definition only.

3.3 Definitions of Service

The majority of industries use services to distinguish their products or offers from other competitors such as; offering free delivery, a telephone helpline, a guarantee, or other unique aspects or services. As a result, service is becoming the dynamic force in instigating competitive advantage for a company (Hoffman and Bateson, 1997). Accordingly, the world is witnessing a significant movement toward using and offering services besides the core product. Accordingly, the service sector has a massive role and contribution to the world economy. Moreover, it can be understood that services can have different aspects and forms, therefore, involve in a wide range of settings and activities. In this regard, several and different classifications have been developed to understand this diversity of services. Dorothy (1996), for instance, classified services into different groups in order to understand the scope of such phenomenon as shown below (Fitzsimmons and Fitzsimmons, 2001):

(1) Business Services: includes consulting, finance and banking services.
(2) Trade service: comprises retailing, maintenance and repair services.
(3) Infrastructure services: embraces communication and transportation services.
(4) Social/personal services: involves in hotel, restaurant and health care services.
(5) Public administration: contains education, security and government services.
According to the previous groups, the service concept involves and participates in diverse industries and markets, connected with different groups of customers and clients. This diversity can lead to different definitions of the service concept, which can be classified into two approaches (Lovelock and Wright, 2001). On one hand, the first approach defines the service construct as a performance that one party can offer to another party. The nature of this service is intangible and it does not relate to the ownership of anything (Lovelock, Vandermerwe and Lewis, 1999). Naturally, this approach considers the service concept as a process which links the producer of the physical component of the service with the users, without ownership in some cases. This definition shows the service concept as a means to deliver service from the producer to the user.

On the other hand, the second approach defines service as economic activities that produce intangible products and benefits for customers at specific times and places, such as education, entertainment, food and accommodations. Clearly, the second approach considers the service concept as actions and movements which generate new advantages for the customer, not only as delivery of an immediate service.

According to the above definitions, it can be concluded that services form intangible benefits and outcomes offered, produced and transformed from one part to another part without having the opportunity to own it. Moreover, the two definitions highlight the idea that services mean and imply intangible benefits produced and consumed during the interaction between the service provider and customer in a specific time and place.

### 3.4 Characteristics of Service

Having shown the definition or main idea of services, it is worth displaying the main characteristics of services. In this regard, the marketing literature indicates that service characteristics or attributes play an important role in the service literature. In addition, these attributes can make key distinctions between goods and services as separate entities (Oberio and Hales, 1990). Figure 3.2 displays four characteristics of services:
The above figure implies that services have four characteristics; however, other scholars introduce five main characteristics as described below:

First, intangibility: this attribute implies that a service cannot be seen, tasted, felt, heard or smelled before purchasing, such as travelling by airplane. In other words, a customer before using or buying a service, she or he will not have any idea in mind about this service (Kotler et al., 2003). As a result, Palmer (2001) claim that according to the intangible feature and lack of physical signal of service products, a customer will face uncertain situations that in turn influence his or her experience and impression. To reduce the feeling of uncertainty, the company should use the tangible component of a service to give positive information and confidence, i.e. tangible elements present signals of the quality of the intangible service.

Second, inseparability: such characteristic means that a service is created and consumed simultaneously. In this regard, Oberio and Hales (1990) states that services, unlike physical goods, are produced and consumed at the same time. According to this feature, customers and suppliers of a service must come together in the same place and time to realise the benefit. Obviously, such a characteristic of service products implies that all people concerned in the service process represent an important part of the transaction. Moreover, this characteristic implies that service products cannot be stored or prepared before being ordered by the customer.
Third, variability (heterogeneity): the current feature of services refers to the notion that service quality varies and fluctuates because the product depends on a simultaneous and unique interaction between provider and consumer. Kotler et al (2003) note that there are different reasons for why service variability exists including; production and consumption happen in the same time, unstable and changeable demand for service products by the customer makes it impossible to control the quality of the service setting and finally the supplier’s skills, mood and attitude during delivery of the service differ from transaction to transaction and from time to time.

Forth, perishability: this feature means that a service cannot be stored before ordering because of the nature of service. In other words, any company providing a service will find problems controlling the variation in demand for its services. For example, the lack of stable demand leads to unstable sales and profits, e.g. empty airline seats, empty train seats and so on (Oberio and Hales, 1990; Fitzsimmons and Fitzsimmons, 2001). Finally, ownership: Such characteristic implies the inability to own or to have a service. To put it more simply, in service business, the customer pays for the right to use the benefits without any transferring of the ownership from the supplier to the buyer such as using of a car park (Palmer, 2001).

According to the former characteristics, services will have special and unique characteristics making them different from goods, which in turn have their own measurements and concepts. In order to show the differences between services and goods, Table 3.1 summarises the main differences between services and physical products.
Table 3.1 Differences between Service and Physical goods

<table>
<thead>
<tr>
<th>Physical good attributes</th>
<th>Service attributes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tangible</td>
<td>Intangible</td>
</tr>
<tr>
<td>Homogenous</td>
<td>Heterogeneous</td>
</tr>
<tr>
<td>Production and distribution separated from</td>
<td>Production, distribution and consumption</td>
</tr>
<tr>
<td>consumption</td>
<td>simultaneous from consumption</td>
</tr>
<tr>
<td>Represents a thing</td>
<td>Represents an activity or process</td>
</tr>
<tr>
<td>Core value produced in factory</td>
<td>Core value produced in buyer-seller interactions</td>
</tr>
<tr>
<td>Customers do not normally participate in the</td>
<td>Customers participate in production process</td>
</tr>
<tr>
<td>production process</td>
<td></td>
</tr>
<tr>
<td>Can be stored</td>
<td>Cannot be stored</td>
</tr>
<tr>
<td>Transfer of ownership</td>
<td>No transfer of ownership</td>
</tr>
</tbody>
</table>

Source: Gronroos (2000, p: 47)

As displayed above, there are some clear differences between services and goods. The tangible nature of goods represents the most significant and first criterion. On the other hand, service implies process and interactions between two parts without transferring of ownership. However, products mean moving the ownership without even participating in the production process. As a result of these differences, dealing with services becomes more complex than goods. Accordingly, perceiving and evaluating service quality will be harder since it depends on intangible factors and elements occurred during and after the interaction between the service provider and a customer. In other words, the human interaction plays a critical role in determining the customers' perceptions of service quality delivered. The next sections discuss the nature and mechanism of customers' perceptions and evaluations of quality in the service sector.

3.5 Definitions of Service Quality

The service quality concept is considered by scholars a difficult construct to define, conceptualize and measure. In other words, the distinguishing characteristics of service quality make it hard for researchers, providers and customers to define, measure and deliver service quality. Accordingly, definitions of such construct are still not well developed (Ghobadian et al., 1994). In this sense, Parasuraman et al (1985) reviewed the literature on quality theory and found that it is difficult to define service quality like
traditional goods. Therefore, they defined service quality as a form of perceptions resulting from a comparison of customers' expectations with their perceptions of actual service performance (Parasurman, Zeithaml and Berry, 1985). Clearly, such a definition of service quality implies the disconfirmation paradigm, i.e. how well will customers' experiences of the service consumption and outcome meet their expectations (Gronroos, 2000).

In order to define the service quality concept, two approaches or methods have emerged. On one hand, the first approach forms the foundation of most ongoing definitions in the literature; this approach uses the disconfirmation paradigm developed by Oliver (1980) which defines service quality as "the degree and direction of discrepancy between consumers' perceptions and expectations" (Parasurman, Zeithaml and Berry, 1988, p. 17) and "the extent to which perceived service delivery matches up to these initial expectations" (Palmer, 2001, p.208). McDonald and Payne (2006) supported this approach through defining service quality as "the ability of the service organization to meet or exceed customer expectations" (McDonald and Payne, 2006, p. 231). Thus, such approach of defining service quality refers to service quality as to what extent customers' perceptions of service delivery meet their expectations (Palmer, 2008).

On the other hand, the second approach defines service quality as an attitude toward the firm, accumulated by customers from a number of successful and unsuccessful service experiences (Bateson, 1995), that is, service quality defined as "a global judgement, or attitude, relating to the superiority of the service" (Parasuraman et al., 1988, p. 16). Similarly, quality of service is defined as "an attitude formed by a long term, overall evaluation of a firm's performance" (Hoffman and Bateson, 1997, p. 324).

According to the above definitions, the literature on the definition of service quality refers to this concept as an attitude or overall judgement resulting from the comparisons between the customer's expectations and perceptions of actual service offered and performed by a company (Robinson, 1999;). To date, papers published in this area are still using and referring to the Parasuraman et al.'s (1988) definition of service quality to define such construct (e.g. Akabab, 2006; Ueltschy, Laroche, Eggert and Bindl, 2007; Carrillat, Jaramillo and Mulki, 2007; Ladhari and Morales, 2008; Vinagre and Neves, 2008).
Thus, it is obvious from the literature that definitions of the service quality concept concentrate and use the comparison between customers’ expectations and perceptions of the way that the service has been performed and delivered (Parasuraman et al., 1985, 1988, 1994; Gronroos, 1984; Coulthard, 2004). More interestingly, such definitions refer to perceived service quality as an aggregate judgement developed by the customer over time and over a number of transactions. To conclude, the following key points summarize the service quality concept;

- Service quality is a long-term and overall evaluation of service performance.
- Customer’s expectations play a significant role and effect on perceived service quality.
- Evaluating service quality depends on the interaction between the customer and the service provider.
- Service quality evaluation occurs before and after the service delivery process.
- Quality of service definition is related to process, manner and interaction as well as the outcome of service evaluation.

3.6 Models of Service Quality

The research on the service quality concept as a different construct from product quality has initiated and improved since 1980. As a result, several models of service quality have emerged to conceptualize service quality (Brogowicz, Delene and Lyth, 1990; Gronroos, 1989). However, the conceptual models of service quality are still in the developing stage (Brady and Cronin, 2001). The main objective for service quality models is to outline factors affecting service quality in the organization, to overcome quality problems and to provide a framework for improving quality programs (Ghobadian, Speller. and Jones, 1994).

Service quality models have been developed within two schools of thought. Researchers in these two schools have tried to explain and conceptualize service quality through developing new dimensions or integrating the current dimensions of service quality. However, theories and models of service quality are categorised into two schools of thought: the Nordic European School and the North American School (Ekinci, Riley and Fife-Schaw, 1998; Karatepe, Yavas and Babakus, 2005). No consensus has yet been developed to consider the appropriate approach of perceived service quality, what
customers are looking for and what they evaluate (Cronin and Taylor, 1992; Caro and Carcía, 2007).

3.6.1 The Nordic School of Thought
Researchers in this school state that a customer’s perception of quality of service is based on a number of components or dimensions. In other words, explaining service quality within this school is based not only on the process of service quality delivery but also on the outcome and image aspects of service quality (Kang and James, 2004). Thus, this school adopts several attributes and dimensions of service quality (i.e. three dimensions) in order to illustrate and predict the customer’s perception of service quality. Gronroos’s model can be considered one of the original models in this school of thought.

3.6.1.1 Gronroos’s Model
Gronroos (1984) developed this model in order to provide a clear picture of how customers perceive and assess service quality, and to determine in what way service quality can be influenced. The Gronroos’s model is based on the idea that perceived service quality is the result of the consumer’s comparison between his/her expectations and perception (the outcome of the evaluation process). In other words, when the perceived service is compared with the expected service, a customer formulates his/her judgement of overall service quality. Moreover, this model proposes that the overall evaluation and perception of service quality depends on three dimensions: technical quality, functional quality and image. The image dimension in turn answers two questions: what a customer gets from the service company and how a customer gets this service. Thus, Gronroos’s model tries to understand what customers in a service setting are looking for and how they evaluate it. As a result, the service provider will be able to control, affect and manage the customer’s evaluation in the desired direction (Gronroos, 1989). Figure 3.3 illustrates the Gronroos model of perceiving service quality.
Perceived service quality in this model results from three dimensions of quality; technical, functional and image (Gronroos, 2000):

- Technical quality or outcome dimension: this means what the consumer gets as a result of his/her interactions with a service firm. Thus, this dimension represents the physical outcome of the service delivered to customers, e.g. a room or a bed provided for a guest in a hotel.
- Functional quality or the process-related dimension: this dimension reflects how the customer gets the service, and how he/she experiences the production and consumption process, i.e. the way the outcome of the service is delivered to the customer. Therefore, this dimension focuses on employees' performance and their buyer-seller interactions with customer, i.e. this dimension indicates the psychological aspect of the service delivered, e.g. the staff's behaviour in a bank, hotel or restaurant.
Image: which implies the result of the customer's recognition and perception of the technical and functional quality dimensions. Hence, the firm's image, which represents one of the quality dimensions, will certainly affect the customer's perceived service quality. In addition to the technical and functional dimensions, corporate image can be influenced by other variables such as price, external communications, physical location, the appearance of the site and the competence and behaviour of service provider's employee(s) (Ghobadian et al., 1994).

Gronroos (1984) noted that the corporate image dimension can be used as a filter. To put it more simply, if the service provider has a good image in the customer's mind, small mistakes in technical and functional quality will be forgiven by customers. If the number of mistakes increases, the corporate image will be damaged. Also, if the corporate image is negative in the customer mind, any mistake will have a huge impact on the customer.

Clearly, the first two dimensions of service quality (technical and functional) can be measured in different ways. Technical quality can be quantified objectively according to its material content. On the other hand, functional quality can be measured subjectively (Kandampully, 2002).

Gronroos (1984) indicates that successful service companies have to recognise that functional dimension is more important than technical dimension of quality. In other words, such a model supposes that improving the functional quality dimension will have a powerful and critical effect on the customer's perception, because improving functional quality (buyer-seller interaction) will have significant value for customers and a competitive advantage for the service provider at the same time (Gronroos, 1989, 2000). This discussion doesn't mean that technical quality isn't important. The service company has to deliver an acceptable level in this dimension, i.e. the physical aspect of service quality should be good enough to be translated into a good level of functional quality. If technical quality fails, total perceived quality will fail as well. On the other hand, good technical quality alone does not secure a high level of service quality perception or achieve a competitive edge, because competitors deliver similar technical outcomes or can create a similar solution quickly. Hence, a company should focus on its functional (process-related) quality to overcome and differentiate itself from the competition.
Kang and James (2004) acknowledge the Gronroos's model since it provides a wide illustration of service quality perception through including the main dimensions of service quality. In other words, the technical quality dimension explains service quality after the service is performed while the functional quality dimension explains service quality during delivery of the service. Thus, such a model involves all dimensions of service quality construct.

To conclude, Gronroos's model shows functional quality as the most important dimension of service quality. Secondly, corporate image dimension is more dependent on functional dimension and word-of-mouth communication. Finally, corporate image can compensate the shortcomings problems in both temporary and overall technical quality dimension.

3.6.1.2 Lehtinen and Lehtinen Model
Also in the Nordic European school of thought, Lehtinen and Lehtinen (1991) developed another model to explain how customers perceive service quality. The authors of this model state two approaches to understand and conceptualize service quality: the first approach is three-dimensional whereas the second is two-dimensional.

The first approach in Lehtinen and Lehtinen's model focuses on the elements of the service production process, i.e. all factors related to service quality phenomena in an organization. It indicates three dimensions of service quality: (1) Physical quality, (2) Interactive quality, and (3) Corporate image.

Physical quality (1) refers to facilities and materials of the service. These elements are classified in this model into two components: the physical product component, which implies goods delivered to customers during the interaction between customer and provider (e.g. food in a restaurant), and the physical support component which aims to facilitate producing the service for customers. In other words, physical support represents a framework where the service can be easier to produce and deliver.

The physical support component is further divided in this model into two categories: the environment and the instrument. The first category is comprised of the interior,
decorations and layout of a service production outlet, whereas the second includes tools needed for producing and delivering the service, e.g. plates, forks, etc.

Interactive quality (2) refers to the interaction between the customer and the interactive elements of the service company. Interactive quality could include interactive person(s) and interactive equipment. Accordingly, producing a service can be done by using a contact person (interactive person) or by physical equipment (interactive equipment). Moreover, interaction can also be between customers themselves.

Corporate image (3) refers to how current and potential customers observe the company’s profile. Therefore, this dimension of quality is developed through the historical relationship between the customer and the service company. However, a corporate image dimension is the only one of the quality dimensions that can actually be created before having any contact or experience with company. Moreover, word-of-mouth recommendation has a great influence on corporate image.

Unlike the first two dimensions of service quality (physical and interactive quality), developing the corporate image dimension happens cumulatively, continually and intangibly, i.e. the third dimension can’t be improved quickly by sudden efforts such as renovation and can’t be affected by a customer’s momentary feeling.

The second approach in Lehtinen and Lehtinen’s model (two-dimensional, as mentioned earlier) focuses on the service quality process and its output. This is similar to the first approach, with a more comprehensive view of the service quality construct, i.e. the two dimensional approach represents a higher level or more abstract way of modelling service quality. The two dimensions in this model are related to Gronroos's model: process quality and output quality.

Process quality represents the consumer’s judgement of his/her interaction with the service provider’s process, i.e. how a customer assesses his/her participation and interaction experience during the service production process. Therefore, the process quality dimension depends on the fit between the customer’s participation style and the contact person’s style (i.e. the manner of participation by the contact person in the service organization), or how the customer has been fit into the service process. Obviously, the
degree of participation will vary from transaction to transaction, e.g. a customer dealing with an automatic bank’s teller will have heavier participation in service process than a customer dealing with the filling of their tank in petrol station by an employee.

Output quality implies the customer’s evaluation of the service process result, which can be either tangible or intangible. Therefore, evaluating output quality is a difficult task for both the service provider and the consumer. Unlike the process quality dimension, this dimension can be measured not only by customers but by any person around them; in other words, output quality can be evaluated by anyone regardless of participation in the service process. Thus, output quality represents a result of the service process.

3.6.1.3 Criticisms of the Nordic European School
Scholars within Nordic European School have made great contributions and influence on service quality literature through developing a model that explains how service quality can be perceived by customers. In other words, the contribution of this school appears through its ability to produce and clarify the main determinants and dimensions of the service quality construct. However, some criticisms have been emerged for this school. First, this school didn’t offer sufficient empirical justifications of its service quality dimensions. In other words, the Nordic European School focuses on the conceptualization issues of service quality, without offering strong evidence to support its validity (Ekinci, 2002; 2008). Second, the Gronroos model didn’t give sufficient details about what kind of customer’s expectations should be used and measured (Ekinci et al., 1998). Third, this school didn’t explain how to measure technical and functional quality (Ghobadian et al., 1993; Seth, Deshmukh and Vrat, 2005).

3.6.2 The North American School of Thought
This school of thought is based on the SERVQUAL model, which proposes that service quality perception is based on multiple dimensions evaluated by the consumer to form his/her expectations and perceptions of service quality (disconfirmation model). As a result, the SERVQUAL scale has emerged in the literature as the most popular instrument for measuring service quality in different industry settings. Later modifications of the SERVQUAL scale have been developed by scholars in order to surmount the limitations and criticism of the original version (Parasuraman et al., 1985, 1988: Parasurman, Zeithaml and Berry, 1991).
3.6.2.1 The SERVQUAL Model

Parasuraman et al (1985) developed a gap model after doing exploratory qualitative research in different groups of service organizations. According to this model, service quality is defined as the difference between consumer expectations and the perceptions of the service provided. In other words, the model considers service quality as a gap between the customers’ expectations and perceptions of the service performed. Therefore, the SERVQUAL model measures service quality by deducting customers’ perceptions of performance score (P) from their expectations score (E) in order to measure the level of service quality perception (Q=P-E) (Parasuraman et al., 1985; Zeithaml, Berry and Parasuraman, 1988). Figure 3.4 illustrate the Gap model.

**Figure 3.4 The Gap Model**

![Figure 3.4 The Gap Model](image)

**Source:** Parasuraman et al (1985, p: 44)
The key contribution of the SERVQUAL model to the service literature concerns the supposition that perceived service quality is represented by four gaps. To put it more simply, customer perception of service quality (the service quality gap) is affected by four gaps that occur in the service provider side. Therefore, customers’ perception of service quality represents the fifth gap in the SERVQUAL model, while the four provider gaps represent the antecedents for the service quality gap.

Figure 3.4 above illustrates the Gap model. It can be seen that customers’ expectations are affected by factors such as word of mouth, personal needs and past experience. In addition, the figure shows that the central gap in the SERVQUAL model is the customer gap, i.e. the gap between what customers expect and what they perceive. According to this model, customers’ perceptions of service quality (customer gap) are influenced by the four provider gaps; all five are described below (Zeithaml and Bitner, 2003):

**Gap 1: The difference between consumers’ expectations and management perception**
This gap refers to the degree to which management in the service company doesn’t know what its customers expect. The responsibility for this gap lies not only with managers but all employees in the company. This gap results from several potential reasons, such as inadequate market research or orientation, lack of upward communication, insufficient relationship focus and inadequate service recovery program. As a result of the first gap, the whole company will fail to understand what customers expect, and then take wrong decisions and strategies.

**Gap 2: The difference between management perception and service quality specification**
The second gap implies the degree to which a company doesn’t provide the right service quality designs and standards. This gap reflects the inability of a company to translate management’s perception of customers’ expectations into service quality specifications or standards. This gap can result from deferent reasons, such as considering customers’ expectations unrealistic, poor service design, absence of customer-defined standards and inappropriate physical evidence and servicescape.
Gap 3: The difference between service quality specifications and service delivery
Such gap reflects the inconsistency between customer-driven service standards or specifications and the actual performance of services delivered by a company's staff. Therefore, such gap implies delivering services that are not compatible with customer specifications which reveal the real customer expectations, i.e. not delivering the service to the customers' standards. This kind of gap involves people in company such as managers, front-line employees, and support staff who failed to perform and deliver service to the customer-driven standards. This gap appears as deficiencies in human resource policies, failure to match supply and demand, customers not fulfilling rules, problems with service intermediates, etc.

Gap 4: The difference between service delivery and external communications
The current gap reveals the incompatibility between the employees' performance to deliver services and the service promises made by a company. To put it another way, such gaps occur when a company fails to achieve the service promises announced via external media. Obviously, any company has different means to transfer its promises to the audience, such as advertising, promotion and sales force. The possible reasons for differences between the actual and promised service can include lack of integrated marketing communications, inadequate coordination between operations and marketing activities, ineffective management of customer expectations, overpromising and inadequate horizontal communications.

Gap 5: The difference between customers' expectations and perceptions
According to the SERVQUAL model, this gap represents the customers' evaluations of service quality (service quality gap). This gap is a function of the four provider gaps. In other words, the magnitude and direction of the providers' gaps will have an impact on the customer gap. As discussed above, the present model indicates that the fifth gap is central to the service quality construct. Therefore, management should control and close the four provider gaps in order to improve the customer's perception of service quality. This model shows how the identified four shortages, or gaps, can influence the service quality perceptions and evaluations by customers.
3.6.2.2 Criticisms of the North American School of Thought

The SERVQUAL model has emerged as a diagnostic tool for discovering service quality deficiencies. In other words, this model can be used by a company to identify gaps or factors that can be improved and that will affect service quality perception from the customers' viewpoint. Discovering these gaps will lead to adoption of corrective marketing programs. Moreover, this school of thought empirically approved five dimensions as a determinant of service quality (Ghobadian et al., 1994; Brogowicz et al., 1990).

On the other hand, this school of thought has been criticized by scholars because it is focusing on the functional or operational service quality dimension, i.e. the North American School focuses more on the functional aspects of service delivery processes between provider and consumer than on the service technical quality dimension (Kang and James, 2004; Mangold and Babakus, 1991). Later, in section 3.8.1, it will be discussed how the SERVQUAL instrument has been extensively criticised in terms of validity and reliability. In other words, this theory is still problematic for modelling and measuring service quality.

3.7 Other Models of Service Quality

Rust and Oliver (1994) introduced the three-component model of service quality to examine how a firm can measure service quality. This model includes three dimensions of service quality: service product (service features and specifications), service delivery (service performance process) and service environment. The main contribution of this model is introducing the third dimension which has an effect on the interaction between employee and customer. Figure 3.5 shows the three-component model of service quality.
The above figure shows service environment as a new dimension in a service quality construct. This conceptualization model supposes that the service environment dimension will affect the customer's perception of service quality, as well as the technical and the functional dimensions. Moreover, the service environment dimension comprises two another sub-dimensions: the internal environment, which focuses on the organizational culture and philosophy of the service provider (items such as market orientation, internal marketing and employees' support and reward system), and the external environment, which focuses on the physical atmosphere of service (servicescape).

Dabholkar, Thorpe and Rentz (1996) developed a multilevel model of service quality particularly for the retail industry which provides a mix of merchandise and service products. Unlike the pure service setting, service quality in such business can be perceived in different ways. Therefore, the developers of this model suggest that the customer's perception of service quality will be influenced by the complex relationship between customers and retailers, i.e. more interactions and more retail choices lead to the introduction of new dimensions for evaluating service quality by customers. Consequently, the multilevel model contains additional dimensions to capture service quality in a retail setting. Figure 3.6 shows the multilevel model.
Figure 3.6 indicates that this model has a hierarchical structure of dimensions for perceiving quality of service. In other words, such a conceptualization model includes three levels of service quality. The first level is the overall retail service quality which captures the common meaning of all dimensions and sub-dimensions in business. The second level includes five main dimensions of service quality, while the third is comprised of six sub-dimensions. Therefore, this model can help to determine which aspect of retail service quality has deficiencies and problems.

Brady and Cronin (2001) introduced another hierarchical model to explain how customers perceive service quality. The developers reviewed and examined all the previous models and related themes. As a result, their model depends on two models of service quality. Namely, this model adopts both the Rust and Oliver (1994) and Dabholkar et al (1996) models. Therefore, this model joins the previous two models together. Consequently, the current model has main dimensions and sub-dimensions. Thus, such model illustrates service quality as a multiple level construct. In other words, customers firstly evaluate the service quality at the sub-dimensions level then they form their perceptions at the primary dimensions level. Finally, customers develop their perception at the overall service quality level according to the previous three dimensions. Figure 3.7 shows the hierarchical model.
Figure 3.7 The Hierarchical Model of Service Quality

The above figure indicates multiple levels of service quality. The first level is the sub-dimension level which includes nine factors. The second level of this model is the primary dimensions which includes three factors. The third level represents the overall perception of service quality. Thus, the combinations of the sub-dimensions produce and reflect the perception of the key dimensions which in turn form the overall perception of service quality.

Additionally, there are some theoretical efforts by other researchers reported in the literature in terms of conceptualization of the service quality concept in different service settings. The Haywood-Farmer (1988) introduced model relies on user-based definitions of service quality, i.e. meeting customers’ expectations. This attribute model of service quality is based on the idea that service companies are diverse according to different elements such as labour intensity, level of service customisation, etc. Therefore, this model urges management to adopt an appropriate mix of the three basic service quality attributes: physical facilities, people’s behaviour, and professional judgement from the provider’s staff. Moreover, this model provides other factors within each attribute of service quality.

Source: Brady and Cronin (1996, p: 37)
Another hierarchical model of service quality was proposed by Philip and Hazlett (1997). They suggest that service quality incorporates three dimensions. Firstly, the pivotal dimension represents the main variable that affects the consumer’s selection of a service company, which in turn will affect the customer’s satisfaction; in other words, this dimension is the end product, or what the customer wants to get from the service encounter. Secondly, the core dimension implies the mixture of people, processes, and organizational structure that a customer should contact and/or negotiate. Thirdly, the peripheral dimension reflects extra attributes performed or designed to make the consumer delighted by his experience with a service company. Thus, the model shows the pivotal dimension as an output of service quality while core and peripheral dimensions together form inputs to service quality.

Mattsson (1992) introduced a value-based model of service quality that is quite unlike the previous models. In other words, this model explains service quality through comparing the perceived ideal standard (value) against the consumer’s experience, i.e., the model applies value instead of the consumer’s expectation. 18 items are defined for measuring value from the customer’s viewpoint. Thus, the value-based model aims to use a new standard in service quality measuring.

Due to the employees’ roles and importance, internal marketing as well as external service quality is developed as a critical topic in marketing literature. Frost and Kumar (2000) developed a special model for measuring internal service quality from the employees’ viewpoint. In other words, the model measures the service quality dimensions among the internal customers (front-line staff) and internal suppliers (back-office staff). Obviously, such model is based on the five dimensions of the Gap model (Parasuraman et al., 1985, 1988). Precisely, the internal model of service quality includes three internal gaps in any service organization. Figure 3.8 displays the internal service quality model.
Figure 3.8 The Internal Service Quality Model

![Diagram of the Internal Service Quality Model]

Source: Frost and Kumar (2000, p: 366)

The above figure indicates that internal gap (1) represents the inconsistency between the internal suppliers' perceptions and the internal customers' expectations. Internal gap (2) is the inconsistency between the service quality specifications and the actual service delivered. Internal gap (3) focuses on front-line staff, i.e. this is similar to gap 5 in the Gap model by Parasuraman et al (1985). Moreover, the above figure shows that perceived internal service quality (gap (3) is linked to internal gap (1) and internal gap (2).

Recently, new models of e-service quality have been developed as a result of the interest in Internet marketing and the growth of electronic commerce. Many researchers have participated in developing a conceptual model of e-service quality. Santos (2003) for example developed a model for understanding the consumer's evaluations of service quality in electronic businesses, i.e. exploring the dimensions of e-service quality. His qualitative research revealed two groups of dimensions. The first group contains incubative dimensions which include ease of use, appearance, linkage, structure, layout and content, i.e. factors that can be developed before launch of a website. The second group has active dimensions which consist of reliability, efficiency, support, communication, security and incentives, i.e. factors that apply consistently throughout the period that a website is working.
To conclude, understanding how customers perceive service quality is considered a difficult and unresolved topic because of its multidimensional nature. In other words, there is no consensus has yet been developed in terms of a generic operational definition of service quality, dimensions that constitute service quality or which conceptual model is more proper than the others to explain how customers perceive quality of service.

Thus, models of service quality complicated the mission to answer how service quality can be defined, conceptualized and measured. The previous discussions presented in the former sections indicate that quality of service is a multidimensional construct. For this reason, the academic community have tried to confirm the exact number and nature of the service quality dimensions in different and several service settings and contexts. Unfortunately, the outcomes of these efforts gave mixed results. To date, there has been no clear agreement in the service literature on the generic and exact number of dimensions of service quality. In order to give a simple view about efforts undertaken for conceptualizing the service quality construct, Table 3.2 summarises the main points of the previous models of service quality.

<table>
<thead>
<tr>
<th>Author</th>
<th>Dimensions</th>
<th>Application</th>
<th>Empirical Support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gronroos, 1984</td>
<td>Three dimensions (technical, functional and image).</td>
<td>Wide range of service organizations</td>
<td>Yes</td>
</tr>
<tr>
<td>Lehtinen and Lehtinen, 1991</td>
<td>Three dimensions (physical, interactive and corporate image).</td>
<td>Restaurants</td>
<td>Yes</td>
</tr>
<tr>
<td>Parasuraman et al., 1985</td>
<td>Five dimensions (reliability, responsiveness, tangible, assurance and empathy).</td>
<td>Wide range of service organizations</td>
<td>Yes</td>
</tr>
<tr>
<td>Rust and Oliver, 1994</td>
<td>Three dimensions (service product, service delivery and service environment).</td>
<td></td>
<td>No</td>
</tr>
<tr>
<td>Dabholkar et al., 1996</td>
<td>Five main dimensions (physical aspects, reliability, personal interaction, problem solving and policy).</td>
<td>Retail industry</td>
<td>Yes</td>
</tr>
</tbody>
</table>
According to Table 3.2, models of service quality can be grouped into two groups. On one hand, the first group of models concentrates on developing additional dimensions of the service quality construct rather than dimensions developed by Parasuraman et al (1988); Gronroos (1984); Lehtinen and Lehtinen (1991). These models introduced new dimensions of service quality in different service industries (e.g. Rust and Oliver, 1994; Haywood-Farmer, 1988; Philip and Hazlett 1997). On the other hand, the second group focuses on the multidimensional structure of service quality, i.e. developing several dimensions and sub-dimensions of the service quality construct (e.g. Dabholkar et al., 1996; Brady and Cronin, 2001).

3.8 Measuring Service Quality
3.8.1 The SERVQUAL Scale
Parasuraman et al (1985; 1988) developed the SERVQUAL scale based on the gap model as an instrument for measuring customers’ perceptions of service quality. The developers of this scale, after doing exploratory research, introduced ten dimensions representing

Source: Developed by researcher
general attributes of service quality. Basically, such dimensions are considered in the literature as determinants of service quality. As a result of the initial qualitative research, the ten dimensions for a service quality construct emerged: reliability, responsiveness, competence, access, courtesy, communication, credibility, security, understanding (knowing the customers) and tangibles. These dimensions represent the key factors or elements which can be used by customers to evaluate service quality.

Then, the SERVQUAL scale’s developers generated a pool of items for the ten dimensions of service quality. Each item was recast into two groups of statements: the first group of statements measures customers’ expectations about firms in general, while the second measures customers’ perceptions of service provided by a specific service company. At the same time, half of the statements were worded positively while the rest were worded negatively, for methodological requirements. Hence, the ten dimensions resulted from qualitative research used as a foundation for developing the SERVQUAL instrument.

Later, the SERVQUAL scale developers observed some overlapping across items generated from the above ten dimensions of service quality. In other words, some dimensions reflect the same meaning and represent the same criteria when measuring service quality. This overlapping forced the developers to do new empirical research in order to refine and improve their scale. For that reason, Parasurman et al (1988) undertook several stages and approaches of data collection, samples and statistical analysis in order to provide and refine the final dimensions of service quality. The final set of service quality dimensions includes just five dimensions; reliability, responsiveness, tangibles, assurance and empathy (Fitzsimmons and Fitzsimmons, 2006).

Clearly, both the gap model theory and the above five dimensions of service quality were used to form the SERVQUAL instrument. The valid and reliable version of the SERVQUAL tool (1988) is based on five dimensions; and four to five items are used to measure each dimension. Thus, the SERVQUAL scale includes 22 items for measuring customers’ expectations of service quality which apply to excellent firms within a particular industry. Another 22 items are included for measuring customers’ perceptions of actual service quality, which apply to a specific firm under study.
According to the SERVQUAL scale, the results for each dimension of customers' expectations and customers' perceptions are compared to estimate the gap in scores between the two components. As a result of this comparison, a firm's level of service quality assessment can be defined, e.g. the larger the gap, the lower the service quality evaluation, whilst the lower the gap, the larger the evaluation (Hoffman and Bateson, 1997). To sum up, the SERVQUAL scale for measuring service quality illustrates the extent to which service performance in each of the five dimensions matches the level of performance that consumers thought a service provider should provide.

The SERVQUAL instrument offers some favourable applications and advantages as shown below (Parasuraman et al., 1988; Coulthard, 2004):

1. Can be employed across different sorts of service companies.
2. Provides valuable data about customers' perception of service quality through capturing the key dimensions of the service quality concept. That is, the scale offers a comprehensive framework of five service quality dimensions.
3. Can be used regularly to follow trends in customers' assessment of service quality.
4. Provides an assessment of service quality for each dimension as well as an overall assessment. In other words the scale displays the relative importance of the five dimensions.
5. Allows a company to classify its customers into several segments, according to their individual degrees of perceiving service quality.

Parasuraman et al (1985; 1988) claim that the five dimensions used in the SERVQUAL scale represent and offer generic instrument and dimensions for measuring service quality in a broad range of services. Over the last years, the SERVQUAL instrument has been used widely and extensively for measuring service quality in different contexts and industries such as banking, healthcare, hotels, restaurants, retail chains, communication, real estate, higher education, etc. In addition, the SERVQUAL instrument has been used extensively in several cultures and countries including: the USA, UK, China, Honk Kong, Greece, and so many other countries. Accordingly, the SERVQUAL scale has been replicated and appreciated in the service quality literature in the last decades by academics and industry people (Buttle, 1996).
In contrast to Parasuraman et al’s (1985; 1988) finding and argument, researchers rejected any generalization of dimensions for the service quality construct and, therefore, for the SERVQUAL scale. For instance, Chowdhary and Prakash (2007) concluded from their study which aimed to determine the importance of dimensions of service quality, that there is no simple generalization of dimensions of service quality can be found. This rejection of generalization is attributed to the fact that the importance of dimensions of service quality vary across services and even within same services and countries.

Accordingly, several researchers questioned using the SERVQUAL scale as a generic and simple measure of service quality in different industries and settings, therefore, researchers asked for developing alternative industry-specific measures of service quality (Babakus and Boller, 1992; Dabholkar et al., 1996; Van Dyke, Prybutok and Kappelman, 1999; Akbaba, 2006). In this regard, Ladhari (2008) reviewed several industry-specific scales used to measure service quality published in the literature taken from two data bases. Ladhari (2008) aimed to explore conceptual and empirical issues can be considered by researchers for developing industry-specific measures of service quality such as; number of dimensions, scores calculation methods, number of items. He concluded that industry-specific scales are varied according to the country, culture and industry characteristics. Thus, such variances of industries and cultures reinforce the notion and need for developing and using the industry-specific scales rather than having only one generic scale as supposed by Parasuraman et al (1985; 1988). Therefore, section 3.9 will shed more light on the service quality measurements developed and used in the hospitality industry in particular.

3.8.1.1 Criticisms of the SERVQUAL Scale
While the SERVQUAL scale has been used extensively by scholars for measuring service quality, some critical criticisms emerged by different researchers and scholars (Brown, Churchill and Peter, 1993). In other words, the literature shows some fundamental criticisms and shortages in this scale. These criticisms can be organized into two groups: theoretical criticisms and operational criticisms.

3.8.1.1.1 Theoretical Criticisms
Several critical faults and deficiencies have been identified in the original version of SERVQUAL scale. The first problem focuses on the disconfirmation paradigm: the
SERVQUAL approach to measuring service quality is based on disconfirmation, which is adopted in customer satisfaction literature. Thus, the developers of this scale mixed two different and distinct constructs (Buttle, 1996; Cronin and Taylor, 1992; Coulthard, 2004).

The second problem is the gap model which is still debated by researchers. To put it more simply, there is no significant evidence demonstrating the validity of this model in terms of explaining service quality from the customers’ perspective. Furthermore, some researchers feel that expectation scores do not provide any additional information beyond that already obtained from the perception component of service quality. Therefore, some researchers recommend using just the perception component of the SERVQUAL scale in measuring service quality; this is the basis for the SERVPERF scale (Cronin and Taylor, 1992; Babakus and Boller, 1992; Carman, 1990; Teas, 1993; Brown et al., 1993).

Moreover, customers’ expectations of service quality may be formed during and after the service consumption process, i.e. such expectations may not exist before the service consumption and interaction. Thus, expectation components of the SERVQUAL battery don’t represent a good standard for evaluation of a service experience (Buttle, 1996). Furthermore, expectation items may lead to a social desirability response bias. In other words, asking about customers’ expectations will motivate respondents to have higher expectations, which in turn will increase the gap score between perceptions and expectations (Babakus and Inhofe, 1991). Boulding, Stealin and Zeithaml (1993) also claim that customers’ expectations can be updated over the time during and after service delivery due to service encounters and the communication effect. As a result, customers’ evaluation of service quality will be affected and changed from time to time. Thus, customers’ expectations represent a questionable component in measuring service quality.

The third problem of the SERVQUAL scale is focusing on process orientation rather than service outcome in measuring the service quality. That is, the scale pays too much attention to behavioural interaction aspects of service quality rather than the result of the interaction processes between the service provider and the consumer. Therefore, the SERVQUAL scale doesn’t represent a precise evaluation of service quality (Kang and James, 2004; Mangold and Babakus, 1991).
Finally, the five dimensions presented by Parasuraman et al (1985) don’t represent all components of the service quality construct, i.e. they are not generic across all service settings. Some studies found more than five dimensions while others found less (Buttle, 1996; Asubonteng, McCleary and Swan, 1996; Ekinci and Riley, 1998). As a result, Babakus and Boller (1992) conclude that the number of service quality dimensions depends on the nature of the service company under investigation. Therefore, the literature about service quality conceptualization includes several different dimensions of service quality.

3.8.1.1.2 Operational Criticisms

Some operational criticisms of the SERVQUAL scale have also been discussed in the literature. First of all, Parasuraman et al (1988) define the customers’ expectation component of the SERVQUAL scale as what they believe a service provider should offer rather than would offer, i.e. customers’ expectations imply customers’ desires and wants. Thus, the definition of expectations by Parasuraman et al (1988) refers to an ideal standard of performance by the service provider. Clearly, such a component of the SERVQUAL scale is not clear, and is in fact vague for respondents in terms of meanings and interpretations. In other words, customers’ interpretations of ‘expectation’ will vary because determining the ideal level of a service is problematic for customers (Teas, 1993; Ekinci and Riley, 1998). Thus, such scale of measuring service quality will suffer from a lack of discriminate validity (Buttle, 1996).

Second, the SERVQUAL scale’s items are not able to capture all aspects for each dimension of the service quality construct. Using just four or five items for each dimension is insufficient to capture either the variance within or the context specific meaning of each dimension (Buttle, 1996).

Third, according to the fact that service context is provided to the consumer over several encounters, this scale is criticised because it doesn’t take into account the affect of the ‘moment of truth’ in customers’ evaluation of service quality. In other words, the SERVQUAL scale’s items consider service quality as a global construct and ignore that service quality assessment is directly affected by particular incidents, i.e. service quality evaluations vary from one moment of truth to another.
Fourth, the polarity feature of this scale causes comprehensive errors and more reading time for respondents. To put it more simply, since the SERVQUAL scale includes several positively worded statements and several negatively worded statements in order to avoid bias by respondents, the methodology causes confused and time-consuming reading with lack of understanding and eventual errors for the reader. Moreover, Babakus and Boller (1992) indicate that using positive and negative statements in the same instrument will lead to data quality problems and decrease both dimensionality and validity of the instrument.

Fifth, the Likert scale in this instrument has been criticised in the literature for reasons such as interpretation problems of the scale midpoint by respondents according to their poor knowledge or experience of the items, i.e. the mid-point will be selected by respondents to imply either a neutral or a don’t know response (Smith, 1995). Moreover, the seven-point rating scale will lead to overuse of the ends of the scale by respondents, due to the lack of verbal labelling for the points from two to six (Lewis, 1993). In addition, Anderson (1992) criticises use of a normal scale such as Likert because this kind of scaling is ineffective to investigate interdependences among the dimensions of the service quality construct. These problems indicate the inability of the SERVQUAL scale to reflect the proper and real consumers’ expectations and perceptions of service quality.

Sixth, two sets of items asking about customers’ expectations and perceptions lead to respondents getting bored or confused by unnecessarily repetitive questions. Hence, the double administration of items creates a problem in measuring service quality (Buttle, 1996; Hoffman and Bateson, 1997). Carman (1990) indicates that asking a reader to answer two sets of items at a single time is impractical. Seventh, the variance extracted represents a measurement of the scale reliability. The variance extracted in the first version of the SERVQUAL scale is 67.9 percent, which is insufficient. As a result, the reliability of this scale is problematic (Buttle, 1996). Finally, Hoffman and Bateson (1997) assert that the SERVQUAL scale doesn’t measure customers’ satisfaction, which has a significant effect on their behavioural intention. This deficiency affects the predictive power of the scale, i.e. the instrument fails to forecast the customers’ ability and intention to purchase again.
3.8.1.1. 3 Revisions of the SERVQUAL Scale

According to the theoretical and operational criticisms discussed in the previous two sections, Parasuraman and his team revised the original version of the SERVQUAL scale twice. In the first revision, Parasuraman et al (1991) retested the original SERVQUAL scale in a sample of 300 customers. Parasuraman et al. computed means, standard deviations and reliability coefficients for the five SERVQUAL dimensions used in the survey. Parasuraman et al (1991) recognised that the mean score for the expectation items were above 6 on a 7-point scale ranging from “Strongly Disagree” to Strongly Agree”. Developers of the scale declared that these high mean scores were not anticipated because items were intended to measure the normative expectations. In other words, the expectation items included in the original SERVQUAL measure the “Should” terminology which leads to unrealistic expectation scores. As a result, the scale’s team changed the wording of the expectation items to measure what customers would expect from companies delivering excellent service. Consequently, the instruction part of the expectation items was modified, while no changes were made to the perception items except minor wording changes to keep them parallel to the revised expectation part.

Parasuraman et al., (1991) also changed at the first revision the negative wording for 16 items to positive wording for several reasons. Firstly, respondents might have been confused by this negative wording since higher standard deviations were received for the negative items of expectations than for the positive items of expectations. Secondly, respondents felt that the negative items were difficult. Thirdly, reliability scores for the two dimensions (responsiveness and empathy) were very low because they contained many negatively worded items. For this reason, negatively worded items were given a positive wording in the final questionnaire. As a final change on the refined SERVQUAL, two items were replaced and new items were added to the tangible and assurance dimensions instead of the two original items to more fully capture and measure the dimensions.

In the second revision, the SERVQUAL team refined the scale again in order to address criticisms. In this second revision of the SERVQUAL scale, Parasuraman et al (1994) expanded the conceptualization of expectations. In other words, the modified scale measures two kind of expectations: the desired service which refers to what extent customers believe that the company should provide and the adequacy service which refers...
to the minimum level of service customers are willing to accept. The gap between the two levels of expectations form the zone of tolerance. Accordingly, Parasuraman et al. in the second attempt to revise the SERVQUAL instrument computed the discrepancy between perceived service and desired service (measure of service superiority) and also computed the discrepancy between perceived service and adequate service (measure of service adequacy).

The second revision of the SERVQUAL scale formulates three alternative rating scales including: first, the three column format which has three separate scales for desired, adequate and perceived service and therefore scores are computed for service superiority gap and service adequacy gap. Second, the two column format which has only two scales and asks respondents to rate their perceptions of service performance against their desired and adequate service levels. Third, a one format scale which generates direct ratings of the service superiority and service adequacy gaps. Therefore, the same battery of the SERVQUAL items is repeated to measure service superiority and adequacy separately.

In this modified version of the SERVQUAL scale, several minor changes were undertaken also such as: using 9-point scale instead of 7-point scale to provide a wider range of choices for ratings to capture two different expectation levels, revising three of the 22-items to reduce redundancies and improve clarity. Then, this modified version was retested through two stages. As a result of these tests, more modifications were made for the final version of the scale including reducing the number of items from 22 to 21, adding a “no opinion” option to the rating scale, reducing the directions paragraph and, finally, sharpening the definitions of desired and adequate service.

3.8.2 The SERVPERF Scale

This scale was developed by Cronin and Taylor (1992) to measure service quality as an alternative approach for measuring this construct. According to their method of measuring service quality, a performance-based measure of service quality represents a more valid and reliable method to measure service quality. Therefore, they developed the SERVPERF scale which measures only the performance perceptions data. Such a scale assumes that measuring the respondents' expectations is not necessary and leads to theoretical and operational problems as displayed in the former sections. In their classic paper, Cronin and Taylor (1992) proved empirically that SERVQUAL is not an adequate
approach for measuring service quality by obtaining a higher explanatory power of variations in service quality by using SERVPERF than could be obtained using SERVQUAL. Cronin and Taylor (1994) reconfirmed the adequacy of the SERVPERF scale for measuring and conceptualizing service quality after doing another empirical study to respond to Parasuraman et al's (1994) criticisms of SERVPERF.

A sufficient number of papers in the literature adopted the SERVPERF scale for different types of services and in many countries (e.g. Quester and Romaniuk, 1997; Lee, Lee and Yoo, 2000; Brady, Cronin and Brand, 2002; Zhou, 2004). Moreover, other researchers improved Cronin and Taylor's (1992) original scale such as Brady et al (2002) who replicated, extended and confirmed the superiority of the SERVPERF instrument as a more appropriate method for measuring service quality.

After introducing and explaining the advantages of the SERVPERF scale in the former sections, the literature has witnessed an interesting debate about whether SERVPERF will outperform SERVQUAL to measure and predict service quality or vice versa. The literature provides mixed results regarding the predictive adequacy of SERVQUAL and SERVPERF to measure service quality. To solve this debate, Carrillat et al (2007) performed a rigorous meta-analysis study using 17 years of empirical service quality studies. The result of this meta-analysis indicates that both of the SERVQUAL and SERVPERF form a valid measure of service quality. However, Carrillat et al found that SERVPERF is stronger than SERVQUAL in predicting the service quality constructs by getting higher correlation coefficients. Their findings also indicate that any modifications to the context of the study will increase the predictive power of the SERVQUAL scale while no changes occurred to the SERVPERF scale. Carrillat et al (2007) asked to end this debate after using this rigorous meta-analysis since both of the scales give similar results.

Accordingly, it seems that the two popular scales (SERVQUAL and SERVPERF) are valid for measuring service quality. As suggested before, researchers are invited to close this area of debate. Therefore, efforts should be directed toward answering other questions such as developing industry-specific measures (e.g. hotels, restaurants, etc) as will be discussed in the next section.
3.9 Measurements and Dimensions of Service Quality in the Hospitality Industry

Although Zeithaml, Parasuraman and Berry (1990) claimed that the SERVQUAL scale is a generic and reliable scale for measuring service quality across different services regardless of the nature of the organization being studied, huge efforts have been undertaken to test the reliability of using this generic scale in the hospitality industry. Owing to the unique characteristics of the hospitality industry (e.g. imprecise standards and fluctuating demand), more customization of the popular service quality measurements were needed to fit the hospitality industry (Fick and Ritchie, 1991; Saleh and Ryan, 1991; Mei, Dean and White, 1999; Ekinci, 2001). As a result, researchers have carried out a long debate about modelling service quality in the hospitality industry.

In response to this debate, a huge number of studies using different methods for measuring the service quality concept were introduced into the literature about service quality measurements in the hospitality industry introduced a huge number of studies used different methods for measuring the service quality concept. The main objective of these studies was to provide a valid technique for measuring the quality of service in the hospitality industry through introducing a unique conceptualization and operationalization of such a concept. However, the outcomes of these studies provided mixed results and mixed solutions to understanding the dimensional structure of service quality (Akbaba, 2006).

Measurements of service quality in the hospitality industry vary according to several factors including the research methods, which can be qualitative or quantitative paradigms, and the research techniques. On the one hand, qualitative methods were used to measure and understand service quality in this industry. For instance, Lockwood (1994) used the Critical Incident Technique (CIT) which was developed initially by Flanagan (1954) to obtain success and failure observations from respondents in the hospitality industry in order to discover and resolve existing practical problems. On the other hand, quantitative methods were used more extensively to measure service quality from different perspectives such as employees, managers, consumers and guests. Obviously, the SERVQUAL scale and its modifications are the most popular instrument in the second approach (Zeglat, Ekinci and Lockwood, 2008).
Since the aim of this section is to highlight the most important measurements of service quality emerged in the hospitality industry, the following paragraphs display, in a chronological order, some studies conducted for measuring service quality in the hospitality industry.

Oberio and Hales (1990) investigate how consumers of conference hotels perceive service quality and what dimensions of service quality should be measured. Interviews with some UK hotel managers were conducted to identify attributes of service quality specific to the conference hotel business, in order to gain valid dimensions and measurement. Initially, 54 attributes were developed. These attributes were organized into four main groups: facilities, catering, pricing and activities. After a consumer survey, 23 attributes were considered as the most important from the consumers' viewpoints. Oberio and Hales (1990) then classified the 23 dimensions into two groups: the functional group (12 attributes) and the technical group (11 attributes). Thus, Oberio and Hales developed a specific instrument for measuring service quality in conference hotels. Moreover, results showed that the functional attributes of service quality had a greater contribution to the overall quality of service in such hotels.

Knutson et al (1990) developed a new instrument called LODGESERV to measure service quality in the lodging industry by replicating the five dimensions of SERVQUAL (reliability, assurance, tangibility, responsiveness, and empathy). Initially, 36 statements were developed in order to capture the customers' expectations of the five dimensions of service quality in the accommodations industry. Knutson et al (1990) then processed these items into several testing and refinement methods in order to provide a valid and reliable instrument for measuring customers' expectations. As a result, a new instrument including 26-items to measure the customers' expectations of service quality in a hotel experience was developed. Knutson et al claimed that the LODGESERV scale presents a consistent, valid instrument to measure service quality in the hotel industry, through defining the most important dimensions from the customers' standpoint.

Saleh and Ryan (1991), after reviewing studies about service quality in the hospitality industry, noted that the majority of these studies focused on the tangible dimensions of service quality. To introduce new dimensions suitable for the industry, a 33-item questionnaire, with three sections of expectations, perceptions and demographic
information, was distributed in a good four-star hotel. Their empirical research demonstrated five new dimensions of service quality different from the SERVQUAL dimensions, to measure the customers’ perceptions of service quality in hotels. The five new dimensions (conviviality, tangibles, reassurance, avoidance of sarcasm and empathy) have emerged as critical dimensions for measuring service quality from the customers’ viewpoint in the industry.

Akan (1995) investigated which dimensions contributed to service quality perceptions for customers in hotels in Turkey. In his work, Akan aimed to know whether quality dimensions developed by Parasuraman et al (1985; 1988) included in the SERVQUAL scale could be applied to an international environment, and what other dimensions identified by customers could be added to the service quality concept. To do so, a modified version of SERVQUAL was applied to measure service quality and identify the level of importance of each dimension for users in four- and five-star hotels in Turkey. Results indicated seven new dimensions of service quality that users of Turkish hotels expect to receive including courtesy and competence of the personnel, communication and transactions, tangibles, knowing and understanding the customer, accuracy and speed of service, solutions to problems and, finally, accuracy of hotel reservations. Akan concluded that SERVQUAL is a valuable tool, but it is not generic. Hence, additional modifications for both for the specific service situation and for the environmental context should be undertaken.

Webster and Hung (1994) introduced a new version of SERVQUAL to measure service quality in hotels by modifying the original scale into a new easy-to-use questionnaire. Authors claim that their adapted questionnaire is valid, reliable and practicable and that the wording of the scale is suitable for the hotel setting. Webster and Hung used several of the dimensions of service quality considered the most relevant to the hotel industry, including tangibles, reliability, communication, responsiveness, security, courtesy, understanding and access. Although the developers of the scale claim that their scale was valid, some technical problems can be attributed to this scale such as the lack of a sufficient number of items to measure each dimension. However, this scale contributed to the debate over service quality in hotels by showing the importance of some dimensions of service quality in hotels such as tangibility and reliability of service.
In the restaurant setting, Stevens, Knutson and Patton (1995) developed a new instrument for measuring service quality called "DINSERVE" by using a modified version of the SERVQUAL scale which would apply to such a business. A questionnaire with 29 items measuring the five dimensions was distributed in the US. The results revealed that the new scale showed high reliability for measuring service quality.

Ekinci et al (1998) investigated the suitability of the two dimensional model and the Gap model for measuring service quality in hotels. Researchers distributed a new (38 item) instrument in two seaside Turkish resorts. The results showed that the five-factor structure of the SERVQUAL scale was inappropriate. Therefore, researchers modified their first instrument to develop a revised (16-item) scale based on the two factor model (tangible and intangible items). The factor analysis showed acceptable results. In other words, the two factor model was more appropriate for measuring service quality in this industry. The Nordic European School provided a reliable and valid model for measuring service quality. Ekinci suggested further exploratory research of the dimensions of the Nordic European School to develop an instrument with practical value for the hotel setting.

Another key paper was published by Mei et al (1999) who explored the unique dimensions of service quality in the hotel industry. Mei et al extended and modified the original version of the SERVQUAL scale. As a result, a new scale with 27 items called HOLSERV was developed. This instrument included changes to some items and the deletion of others from the SERVQUAL scale, in order to make it suitable for a hotel setting. 1,000 questionnaires were sent to five mid-luxury hotels in Australia. Results of the study found that service quality is represented by three dimensions in the hospitality industry, including employees' behaviour and appearance, tangibles and reliability. In terms of the relative importance of these dimensions, the employees dimension was the best predictor of overall service quality. The findings also show that the one-column format questionnaire represents a valid, but much shorter, way to survey customers.
Unlike other approaches used in the original SERVQUAL scale, Caruana, Ewing and Ramaseshan (2000) used the three-column format developed by Parasuraman et al (1994) to determine its validity for measuring service quality in hotels. The findings of their study did not support the suitability of the two types of expectations (desired and adequate service) suggested by Parasuraman et al (1994) since respondents could not distinguish the differences between the two types. However, results revealed that the perception component was the most important component in measuring service quality.

In terms of the dimensions of service quality, the results of the factor analysis produced only three dimensions instead of five, namely reliability and tangibility while the remaining three dimensions loaded into only one factor measuring the intangible features of service quality.

Based on his work in 1998, Ekinci (2001) developed a new 15 item instrument for measuring service quality in the hospitality industry, after selecting generic dimensions of service quality by reviewing previous empirical and conceptual studies related to quality of service in lodging literature. More precisely, Ekinci nominated six dimensions as evaluative dimensions in hotels as they were the most frequently quoted dimensions. As a result of using two rigorous methodologies of validity procedures, three dimensions were found to be generic for such a business (physical quality/ output quality, staff behaviour and attitude, and timeliness).

Nadiri and Hussain (2005) used the SERVPERF scale to measure service quality in hotels in northern Cyprus from the perspective of European tourists. The authors of this study claim that using the SERVPERF scale is one of the best methods to measure service quality because it provides a diagnostic tool regarding the level of service performance from the customer’s perspective. Findings of the exploratory analysis supported Ekinci’s (2001) findings. In other words, Nadiri and Hussain’s findings reject the five dimensional structure of SERVPERF. Instead, findings indicate that the two dimensional model (tangible and intangible) developed by the Nordic European school fits the service quality concept in the hotel industry.

New dimensions of service quality were claimed by Akbaba (2006). More precisely, Akbaba used a modified version of the SERVQUAL scale to measure service quality in business hotels in Turkey. The motivation for his study was to explore whether this new
segment of hotels in this international environment could help to find additional dimensions for measuring service quality in hotels rather than the five dimensions included in the original SERVQUAL scale. The results of his study produced five new dimensions, including tangibles, adequacy in service supply, understanding and caring, assurance, and convenience. Thus, some of these dimensions were different from SERVQUAL. Moreover, findings revealed that convenience was the most important dimension for business travellers. Akbaba recommended modifying the SERVQUAL scale for specific service segments and for cultural context.

As a modern approach for measuring service quality in hotels, Wilkins, Merrilees and Herington (2007) developed an approach for measuring service quality in the hotel industry through building a hierarchical structure for measuring service quality. This new approach investigates the structure and antecedents of the concept in the hotel industry. Wilkins et al., (2007) conducted a qualitative study to generate items that could be used to measure the performance of service quality in five star hotels. As a result, a set of 63 items was gained from this stage. Then, these items were grouped into several dimensions using exploratory and confirmatory factor analysis. Findings indicated that there are only three main dimensions of service quality in hotels, including physical product, service experience and quality of food and beverage. In addition, results showed that there another level of dimensions that exists in the hotel setting that can be used for fully measuring service quality i.e. sub-dimension or sub-factor. For example, the physical product dimension encompasses another three sub-dimensions, such as stylish comfort, room quality and added extras such as valet parking.

Hsieh, Lin, and Lin (2008) used another approach for measuring service quality in hot spring hotels in Taiwan. Based on the five dimensions of service quality developed by Parasuraman et al (1988), a special questionnaire was developed in this study to produce evaluation criteria of service quality more suitable for this type of hotels. Hsieh et al claim that the process of evaluating quality of service requires an evaluation framework. Accordingly, this study used a new approach called analysis network process (ANP) to build an evaluation framework of service quality in hot spring hotels in Taiwan. The procedure of (ANP) is a bit complicated and requires sequential phases for grouping and gathering items. However, (ANP) helps to find the relative weights of the five dimensions of service quality and the weights for all items corresponding to these dimensions. To be
more precise, the findings of this study ranged dimensions (from highest to the lowest): assurance, reliability, responsiveness, tangibles and empathy. As a result, using this approach will allow management to identify directions for future improvements in service quality through defining strengths and weaknesses.

As can be seen in the above studies, the literature of service quality measurements in the hospitality industry can be divided into two groups. The first group measured service quality by using the SERVQUAL or SERVPERF scales with or without some modifications (Knutson et al., 1990; Saleh and Ryan, 1991; Akan, 1995; Mei et al, 1999; Webster and Hung, 1994; Ekinci et al, 1998; Caruana, et al., 2000; Nadiri and Hussain, 2005; Akbaba, 2006). The second group includes studies measured service quality using different methodologies (Oberio and Hales, 1990; Lockwood, 1994; Ekinci, 2001; Wilkins et al, 2007; Hsieh et al, 2008). Unfortunately, these studies couldn't confirm the suitability of the popular scales (e.g. SERVQUAL) because of mixed results. Moreover, these studies could not find a generic set of dimensions for measuring service quality in the hospitality industry.

However, it is worth noting that the latest development and application of service quality measurements in the hospitality industry indicates that such a concept can be split into two levels of dimensions, primary and secondary dimensions (factors and sub-factors), as shown in Wilkins et al’s (2007) modelling of service quality. This multidimensional and hierarchical modelling of service quality was first introduced by Brady and Cronin (2001) in a different industry and then applied to the hospitality industry by Wilkins et al (2007). In his review, Ekinci (2008) shows that service quality as a multidimensional construct and can be grouped, in the hospitality setting, into primary and secondary dimensions i.e. the hierarchical structure as shown below in Figure 3.9.
According to the above figure, the primary service dimensions include output quality and interactive quality, while the secondary dimensions are physical quality, product quality, staff behaviour and responsiveness. In addition, several attributes are used to measure each secondary dimension.

To conclude, the findings of the previous studies could not confirm the dimensions of service quality in the hospitality industry and which scale and method is the best. Comparing the number of dimensions in studies of service quality in the hospitality industry is not easy due to the wide variety of results. Hence, it is hard to define one set of dimensions for measuring service quality in the hospitality industry. In this regard, Albacete-Saez, Fuentes-Fuentes and Liorens-Mountes (2007) state that measuring service quality in the hospitality industry is difficult, and no agreement has been developed yet;
"No consensus exists on evaluation and measurement of service quality dimensions in the hospitality industry" Albacete-Saez et al., (2007, p. 49).

However, the majority of studies of the hospitality industry nominated the tangible (physical) and staff behaviour (intangible) as the most important and common dimensions for measuring service quality. In other words, most of the empirical studies discussed previously show those two dimensions as common factors in the hospitality industry. In this respect, Ekinci (2001) claimed that the validity of the two dimensional model (technical quality and functional quality) offered by the Nordic European School was more generic than any other service quality model. Moreover, Brady and Cronin (2001) suggest that service quality should be measured with fewer dimensions than were suggested by the North American School. Ekinci, Prokopaki and Cobanoglu (2003) also found that perception and measurement of service quality could be obtained by two global dimensions: tangibles and intangibles. For the other dimensions, Ekinci et al (2003) claim that the four SERVQUAL dimensions, assurance, reliability, empathy and responsiveness, could be loaded into a single dimension called intangibles, while the tangibles dimension remained distinct.

In light of the preceding discussion, the current study will use the scale developed by Ekinci (2001; 2008) for measuring service quality for several reasons. First, the scale was developed after investigating all the dimensions of service quality that had emerged in the hospitality literature. Second, this scale measured both the processes and outcomes of the service quality construct (tangible and intangible). Third, the scale matches the Gronroos and Lehtinen's models of service quality which have been confirmed previously as valid models of service quality in the hospitality industry (e.g. Nadiri and Hussain, 2005). Finally, the scale’s validity and reliability were confirmed using rigorous statistical procedures.

3.10 Consequences of Service Quality
Several outcomes or consequences of service quality have been introduced and discussed in the literature. Studies interested in the outcomes of quality, such as financial results, have been pioneered by Schoeffler, Buzzel and Heany (1974) through the Profit Impact of Marketing Strategy (PIMS). This project aims to gather quantitative information
regarding the relationship between business performance and certain marketing activities, such as quality, price, advertising, and promotion expenditures, research and development expenditures, etc. Moreover, researchers from past decades have conducted different studies to explore and confirm the outcomes of service quality. As a result, different consequences of service quality have appeared in the literature.

Accordingly, the present section focuses on benefits and outcomes obtained by achieving an acceptable and high level of service quality. In other words, the following points illustrate outcomes and consequences of the service quality concept.

3.10.1 Customer Satisfaction

The customer satisfaction concept has been defined and measured widely in the literature, which in turn leads to complicate understanding the construct without developing a generic definition. However, Oliver (1981) reviewed definitions of customer satisfaction developed in the job satisfaction literature and consumer behaviour discipline. Consequently, Oliver (1997) summarised definitions of in one concept compatible with previous theoretical and empirical results, as “the consumer's fulfilment response. It's a judgement that a product or service feature, or the product or service itself, provides a pleasure level of consumption-related fulfilment, includes levels of under- or overfulfillment” (Oliver, 1997, p. 13). Zeithaml and Bitner (2003) also introduced other feelings related to satisfaction, such as contentment, pleasure, happiness, delight and relief. Moreover, customer satisfaction was defined as “a short-term emotional reaction to a specific service performance (Lovelock and Wright, 2001, p. 78).

Accordingly, customer satisfaction can be described as an emotional and affective construct, i.e. an affect-laden evaluative response developed after a consumption process. In other words, this concept means how much the consumer likes or dislikes the products or service after using them.

However, it is necessary to mention two key issues underlying this concept. First, customer satisfaction occurs at the transaction level. In this regard, previous studies indicate that customer satisfaction is an affective construct that occurs at the transaction level (e.g. Kotler et al., 2003; Zeithaml and Bitner, 2003; Dabholkar, Shepherd and Thorpe, 2000).
Second, the customer satisfaction concept is based on the disconfirmation paradigm theory which was introduced by Oliver (1981). To state this in a simpler way, the disconfirmation paradigm theory means that if performance matches expectations, the customer is satisfied. If performance falls short of customer expectations, the customer is dissatisfied. If performance exceeds expectations, the customer is delighted. Thus, such theory refers to the size and direction of the performance experience and the person's initial expectations. In other words, this theory states that consumers form their satisfaction as a result of a subjective comparison between expectations and perceptions, i.e. the level of satisfaction is determined according to the size and direction of disconfirmation. Thus, the expectancy-disconfirmation model confirms the idea that customer satisfaction is a direct function of subjective confirmation.

As a broader model of the disconfirmation paradigm theory, Churchill and Surprenant (1982) introduce four constructs of the disconfirmation paradigm phenomena including; expectations (i.e. the anticipated performance), actual product performance, disconfirmation (which forms an intervening variable in the satisfaction process) and finally satisfaction (which represents an outcome of the comparison between the real rewards, benefits and costs of purchase and expectations). On the other hand, Oliver (1981) introduces another four components of the comprehensive satisfaction construct; expectations (which means the affect-belief component), disconfirmation (which refers to the difference between pre- and post-performance judgement), satisfaction (implies an emotional response following disconfirmation experience) and attitude (indicates a person's affective orientation toward an objective).

Having shown definition and theory underlying the customer satisfaction concept, it is worth discussing briefly the differences between the service quality and customer satisfaction concepts since they relay on the disconfirmation paradigm theory i.e. differences between expectations and perceptions of performance. In this regard, several researchers debated this area of research and confirmed that the two concepts are distinct concepts. For instance, Parasuraman et al (1988) indicate that the customer satisfaction construct is related to a specific transaction level while the service quality concept is a global judgement or attitude toward service. Furthermore, although both service quality and customer satisfaction constructs are based on the disconfirmation paradigm, consumers' expectations in service quality literature imply what he/she thinks that a
service provider should offer, whereas consumers' expectations in customer satisfaction literature refer to what he/she thinks is likely to happen through a specific transaction. Moreover, Oh (1999) summaries the differences between the expectancy-disconfirmation models (customer satisfaction) and the gap model (service quality) in a few points; the expectancy-disconfirmation model explains the consumption process while the SERVQUAL model explains and describes just the service quality perceptions. In addition, the former model measures disconfirmation directly, i.e. subjectively, whereas the SERVQUAL model does that indirectly, i.e. arithmetically.

3.10.2 Behavioural Response
As another outcome of service quality, the marketing literature considers the behavioural response as an outcome, indicator and assessment of service quality delivered or performed. In other words, a customer's behavioural responses form a signal whether customers will be retained or will switch to another service provider. Therefore, this outcome of service quality is considered as an indicator for customer defection rate (Zeithaml, Berry and Parasuraman, 1996). Moreover, researchers describe this outcome of service quality as defence activities which aim to retain the current customers rather than capturing new customers. As a result of the customers' behavioural state, any company can improve its profits (Rust and Zahorik 1993, 2002; Zeithaml, 2000).

Several dimensions of the behavioural responses concept emerged in the literature. However, Zeithaml et al (1996) reviewed the potential facts and dimensions of the behavioural responses construct, and introduced five main dimensions: loyalty to company (loyalty), propensity to switch (switch), willingness to pay more (pay more), external response to problem (switching to other provider and complaining to other customers) and internal response to problem (complain to the company's employees). This classification of dimensions provides a wide and comprehensive view of the behavioural intention and response construct. In other words, these five dimensions incorporate all dimensions used in the literature for defining and measuring this concept.

3.10.3 Productivity
Obviously, this concept refers to the relationship between outputs and inputs that have been used in the operation system in any organization. Hence, this concept is used to manage production efficiency in a manufacturing context. Clearly, this meaning of
productivity, which developed and emerged in the manufacturing or industrial setting, focuses on the results of operations and elements to produce and create the results. Thus, such a traditional definition of this concept aims to measure how much the company doing well in terms of exploiting and transforming inputs to quantifiable outputs (Schroeder, 1985; Gronroos and Ojasalo, 2004; Yeoman, Ingold and Peters, 1996).

On the other hand, this concept is defined in the service sector literature as "how well a service provider uses resources to create output in the form of acceptable perceived quality and value for customers" (Gronroos, 2000, p:208). Obviously, such a definition has a different nature and function from the tradition definition of manufacturing productivity which focused just on the relationship between output and input. To put it more simply, customers in a service context have great influence on determining and measuring the level of productivity. Moreover, production and consumption in service are simultaneous, which in turn leads to an inability to standardize and calculate inputs and outputs. Therefore, productivity measurements in service industry should provide information about how a given input affects customers' perceptions of service quality, and the ability of an organization to create profits, i.e. there is a complicated relationship between quality, profits and productivity.

Obviously, traditional concepts and measurement of goods productivity cannot be easily adopted and used in service organizations for several reason: the characteristics of service (intangibility, perishability, heterogeneity and simultaneity), inability to standardize inputs and outputs (which in turn complicates the ability to relate objectively a given amount of inputs to a given amount of outputs due to the unique requirements for each transaction), the significant influence of customers on the production and delivery process (i.e. the service system forms an open system), the difficulties of selecting a suitable unit of measurement, the lack of constant relationships between input and output (i.e. customers perceive facilities in service settings differently), the difficulties of replacing labour with equipment, and no constant assumption of quality (Jones and Lockwood, 1989; Witt and Witt, 1989; Yeoman et al., 1996; Gronroos, 2000; Sigala, Jones, Lockwood and Airey, 2005).
3.11 Conclusions

Although the quality concept was developed first in the manufacturing industry, huge efforts have been undertaken in the service sector in the last few decades to understand and implement it in that sector as well. The quality movement was adopted in the service sector as a central theme in terms of satisfying customers and surmounting high competition. As a result, the literature on the subject has developed rapidly in parallel with the increasing contribution of this sector to the economy. As mentioned in this chapter, the literature shows the service quality construct as a complicated phenomenon according to the unstable state of service quality definitions, as well as the diversity of dimensions, frameworks and measurements of service quality.

The major concern of the literature reported in this chapter was to present and identify a valid and comprehensive model of service quality, which can be used to illustrate how service quality can be assessed by customers and others. Several different models were developed by different authors. Each model introduces a different set of dimensions of service quality. For example, the Nordic European Model developed three dimensions of service quality: technical quality, functional quality and image; the North American Model developed five dimensions of service quality: tangibles, reliability, responsiveness, assurance and empathy. Other models introduced and recommended other dimensions. Rust and Oliver (1994), for example, developed another model that includes three dimensions of service quality: technical quality, functional quality and the physical environment. As a result, each model adopts a different point of view in terms of explaining the service quality concept leading to mixed results.

Thus, understanding how customers perceive service quality is an unresolved topic according to its multidimensional nature. In other words, no consensus has yet been developed in terms of what dimensions form service quality or which model is more proper than others to explain how customers judge quality of service. As a result, measuring service quality is still problematic in terms of both theoretical and operational issues. Although the multi dimensional instrument (SERVQUAL) has been adopted in the literature as the main tool for measuring quality of service in service organizations, some critical issues have emerged as deficiencies in the instrument. Several modifications have been made by different researchers to overcome these limitations in the SERVQUAL scale, in order to provide a reliable, valid and generic instrument for measuring service
quality. The key modification and recommendation in the literature was to use the perception of service quality performance only for measuring the construct, (Cronin and Taylor 1992). Moreover, this chapter highlighted the debate between SERVQUAL and its alternative approach SERVPERF.

Discussions introduced in this chapter show that the debate over the service quality concept is focused on two main areas. On one hand, the first area aimed to discern whether disinformation theory or service performance is more suitable and adequate for measuring service quality, i.e. SERVQUAL versus SERVPERF. In this regard, Carrillat et al (2007) after doing a meta-analysis asked to stop searching this area since both models and scales are adequate to measure service quality. On the other hand, the second area aimed to identify the generic dimensions of service quality to develop a reliable scale. To date, the service quality literature has produced mixed results regarding the generic dimensions of service quality across different industries. Due to this inconsistency, scholars have been asked to produce industry-specific scales for measuring service quality in different industries.

More importantly, this chapter shows that huge efforts have been given to conceptualizing and measuring service quality in the hospitality industry. The main objective behind these studies was to develop a set of generic dimensions and specific scales for measuring service quality in this industry in particular. Quite a large number of empirical studies modified and tested the generic scales such as SERVQUAL and SERVPERF. Moreover, some of these studies introduced industry-specific scales such as LODGSERV, HOLSERV, and DINlRERVE. Unfortunately, the hospitality literature failed to agree about the perfect modelling and the exact number of dimensions of service quality in this industry.

However, some studies (e.g. Oberio and Hales, 1990; Ekinci, 1998; Nadiri and Hussain, 2005) demonstrated that the two-dimensional model developed in the Nordic European school of thought is more suitable for conceptualizing and measuring service quality in the hospitality industry. This model seems more generic than the SERVQUAL model. Therefore, it may be more suitable for measuring service quality in the hospitality industry. Accordingly, the scale developed by Ekinci (2001); Ekinci et al (2008) will be
used in this study for measuring service quality in the budget hotel sector by adopting only two generic dimensions: physical quality and staff behaviour and attitude.
Chapter 4

Business Performance Measurement
4.1 Introduction
Performance measurement system (PMS) is one of the most important topic and technique discussed in the field of business management. The fields of accounting, business strategy, operations management, marketing, and organisational behaviour have all discussed and contributed to this topic at length (Neely, 1999; Marr and Schuima, 2003). The importance of this topic emerged from the assumption that performance measurement system is an essential tool that enables a company to achieve and control its desired objectives. In addition, such tool allows managers to balance the tensions between growth versus control, short-term performance versus long-term performance, and opportunities versus threats (Simons, 2000).

Due to the importance of this topic, the purpose of this chapter is to review the relevant literature concerning the theory of business performance measurement system, in order to select suitable measures for the current research. To do that, section two reviews definitions of performance measurement systems, while section three discusses types or methods of performance measurement systems. According to methods of the performance measurement systems outlined in section three, the following sub-sections review the financial and integrated (balanced) performance measurement systems developed and emerged in the literature. Section four then reviews financial and operational measures used in the hospitality industry, while section five discusses performance measurement systems developed and used in the hospitality context. Section six displays results obtained from the first part of the preliminary study conducted with hoteliers. Finally, section seven draws a conclusion for the chapter.

4.2 Definition of Performance Measurement Systems
Before defining the performance measurement system (PMS) concept, it is worth discussing its components. First, the literature defines the term “performance” as the ability of an entity, such as a person, group or organization, to make results in relation to specific and determined
objectives (Laitnen, 2002; Lebas and Euske, 2004). In addition, performance is an actual work or output produced by a specific unit or entity. To put it another way, the performance concept refers to the measurable achievements produced (Harbour, 1997; Phillips, Davies and Moutinho, 1999). Second, the term "measurement" indicates the ability and processes used to quantify and control specific activities and events (Morgan, 2004).

As key authors of this area, Neely, Gregory, and Platts (1995) define the performance measurement concept as "a process of quantifying the efficiency and effectiveness of actions" (Neely et al., 1995, p. 80). On the other hand, Neely, Gregory, and Platts, (2005, p; 1229) refer to the performance measurement system (PMS) as "the set of metrics used to quantify both efficiency and effectiveness." Literature defines measures as metrics used to quantify and compute an action's efficiency and effectiveness (Bourne and Neely, 2003).

The definition of PMS introduced by Neely's et al (2005) shows that efficiency and effectiveness act as an important part of the performance measurement system concept. Although this definition of PMS is popular, simple, and straightforward, the diversity of the PMS definitions introduced by different disciplines (e.g. strategy, operations, finance, accounting, human resources management, etc.) complicated the understanding of this concept. In this regard, Franco-Santos, Kennerley, Micheli, Martinez, Mason, Marr, Gray, and Neely (2007) claim that there is no agreement in terms of producing a single definition of the PMS concept; accordingly, any research in this area will be with a limited generalisability and comparability. To solve this confusion and simplify the complexity of the PMS definition, Franco-Santos et al (2007) reviewed several definitions introduced in the literature by different contributors who represented various research disciplines.

Resulting from their analysis of PMS definitions, Franco-Santos et al (2007) confirmed the diversity of the concept as well as the lack of consensus, since each definition provides a different perspective and characteristic of PMS. However, they categorised the various definitions of PMS into three main themes and perspectives. First, the operations perspective, which implies that a PMS uses a set of metrics to quantify efficiency and effectiveness as introduced by Neely et al (1995; 2005). Second, the strategic perspective, which refers to the PMS as a tool to cascade performance metrics down to achieve the
strategies and objectives of a company and also to align processes with strategic goals and objectives (e.g. Ittner et al., 2003); and third, the accounting perspective, which considers the PMS as a tool for the planning and budgeting of performance and results as suggested by Otley (1999).

According to these three perspectives, the PMS concept implies a sophisticated tool that offers useful information, implications, and needful functions. In this regard, Shank (1989) mention that PMS can be involved in policies and actions in order to harmonize activities and to transfer information supporting the entire business management strategy. Nanni, Dixion, and Vollman (1992) also indicate that a PMS is comprised of systematic activities conducted to ensure the successful implementation of strategies and plans in an organization. In other words, a performance measurement system provides a tool to clarify how well a company is doing, in terms of processes, actions, and strategies, in order to achieve its objectives. Moreover, Morgan (2004) considers the PMS a strategic tool with a wide variety of metrics used by management to monitor and guide a company toward successful desirable objectives and goals. Lohman, Fortuin, and Wouters (2005) state that PMS aims to support the implantation of strategies.

Based on the above discussion of the literature, a performance measurement system’s definitions, functions, and benefits play interesting and different roles in the short and long-term of an organisation. In addition, the literature shows that a PMS serves as a tool for monitoring and controlling performance as well as achieving strategic control and performance.

In order to help researchers and users of performance measurement systems to identify the main roles and tasks of the PMS, Franco-Santos et al (2007) summarised these functions into five main areas. The first area is that of measuring business performance, specifically, monitoring the progress of performance achieved. The second area involves in introducing and deploying strategic management philosophies into a company by developing, formulating, and implementing strategies and providing alignment between processes and objectives. The third area involves facilitating communications within the company as well as with parties outside of the company (i.e. internal and external communications), and benchmarking with different criteria. The fourth area involves influencing behaviour through deciding and monitoring rewards and compensations and
the fifth area is learning and continuous improvement function, which is accomplished by conducting feedback processes in order to improve future performance.

To conclude, definitions and functions of the PMS concept imply that this concept is not easy and offers several benefits. Moreover, the previous discussion in this section revealed that the PMS concept involves in different areas and functions within any organisation. However, the two key functions of this concept are measuring and monitoring the progress of performance and achieving strategic objectives.

In terms of using PMSs, Phillips, et al (1999) claim that determining how to measure business performance is not an easy task for two reasons: difficulties in finding definitions for performance, competitiveness, effectiveness, and other related concepts, and also due to difficulties in finding measures and metrics for such concepts. As a result, there is a little agreement about which business performance measurement system is the best one to implement. Owing to this difficulty and the complexity of the PMS literature, several and different methods, perspectives, and models have been developed in order to enable organizations to measure and manage their performance effectively, as will be shown in the next sections.

4.3 Types of Performance Measurement Systems

In order to know the main streams of PMSs emerged in the relevant literature, Ghalayini and Noble (1996) categorized the literature of PMSs into two waves. The first wave started in the 1880s and lasted until 1980; which was based on using traditional accounting measures, while the second wave, which started in the late of 1980s, was a response to the changes of the global markets and to the limitations of the first method. In the second wave and method of PMS, companies began focusing on new dimensions and measures, such as quality, time, and flexibility to evaluate their business performance.

A similar argument was introduced by Neely (1999), who claimed that the criticisms of the traditional financial measures raised in the mid-1980s forced practitioners to go to more integrated methods of measuring performance. Consequently, academics and practitioners started asking for revolution in the PMS arena during the period between the late 1980s and early 1990s. In this regard, Olve, Roy and Wetter (1999) grouped PMSs into two groups; the first group adopts historical financial measures of performance.
extracted from accounting and financial sources, whilst the second group includes qualitative measures of performance besides the financial measures, such as the balanced scorecard system (BSC). Burgess, Ong, and Shaw (2007) also developed a similar classification of performance measurement systems. They categorised methods of PMSs into two groups; the first group includes traditional accounting measures, while the second group comprises contemporary integrated systems that combine financial with non-financial measures.

In light of the preceding discussion, performance measurement systems have evolved from using accounting and financial measures only to using more sophisticated and balanced methods (financial and non-financial) for measuring performance. The two broad methods that have been developed and used within the PMS concept include financial measurements and integrated performance measurement systems. The following sub-sections will discuss these two methods for measuring business performance.

### 4.3.1 Financial Performance Measurement

Otley (2004) considers financial performance is the ultimate objective and outcome for any organisation, since any business should deliver perceived value in exchange for money invested in the business by its owners and shareholders. Financial performance measures offer valuable information about the condition and status of a business in financial terms. According to Keown, Martin, Petty, and Scott (2008), one of the best ways to measure financial performance is to use financial ratios or metrics. Such ratios should reflect standardised accounting data in order to allow managers and financial analysts to identify the weaknesses and strengths of a company’s performance. This accounting data includes the Profit and Loss Account (Income Statement), the Balance Sheet Statement, and the Cash Flow Statement (Mills and Robertson, 2000; Wheelen and Hunger 2004; Ward, 1989).

Although the roots of using financial ratio analysis can be traced to the last half of the nineteenth century (Horrigan, 1968), Atrill (2003) argue that this kind of performance measurement provides a useful view of the financial situation and condition of a business by expressing the relation of one figure appearing in financial statements to other figures. Brigham and Houston (2004) highlight the ability of the financial ratio analysis technique to compare the firm’s performance with other firms in the same industry and to anticipate
trends in the firm’s financial position over time in order to help management to identify deficiencies and take actions to improve performance. Ratio analysis can be used also from an investor’s standpoint to predict how well the company will perform in the future in terms of generating profits; thus, these ratios can be used by shareholders as an external analysis tool.

Thus, the financial ratio analysis measures and evaluates a firm’s performance to determine if the firm’s financial situation has changed from one period to another period. Moreover, it can be sued to measure and evaluate a firm’s performance versus other companies in the same industry. In this regard, Keown et al (2008) state that financial ratios are used by financial managers and other parties within and outside of their organisations, including investors, lenders, suppliers, employees, and customers. On one hand, people within the company can use such ratios to identify the firm’s performance and take corrective actions, evaluate employees’ performance, and decide on the incentive plans, as well as to compare financial results among different departments. On the other hand, financial ratios can assist people from outside the company; for example, lenders use such ratios to decide whether or not to make a loan for a company. Investors also can use the results of these ratios to decide whether or not to invest in a company.

After showing the importance and benefits of using the ratio analysis technique for measuring the financial performance of a company, these ratios can be categorized into several groups in order to make inferences about a company’s financial situation and position. For this reason, the following sub-sections display the common financial ratios emerged in the literature;

4.3 1.1 Profitability Ratios
Profitability ratios measure the effectiveness of a firm in generating profits (Mclaney, 2000) In addition, the profitability ratios show how well the management utilized the capital employed in the company to generate profits (Thompson, 2001). To put it more simply, profitability ratios can show and determine how well the money (capital) invested in the business is being used. However, these ratios ignore how the business is funded but focus on how well the business makes profit (Thompson, 1997). Measuring profitability can be done by using the ratios shown in Table 4.1.
Table 4.1 Profitability Ratios

<table>
<thead>
<tr>
<th>Ratio</th>
<th>Equation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1- Gross profit margin</td>
<td>( GPM = \frac{Sales - Cost\ of\ sales}{Sales} \times 100 )</td>
<td>Indicates the total profit margin available to cover administrative and other expenses beyond cost of goods sold.</td>
</tr>
<tr>
<td>2- Net profit margin</td>
<td>( NPM = \frac{Net\ income}{Sales} \times 100 )</td>
<td>Indicates how much profit the firm was able to generate after all expenses.</td>
</tr>
<tr>
<td>3- Return of capital employed</td>
<td>( ROCE = \frac{Net\ income}{capital\ employed} \times 100 )</td>
<td>Indicates the earning power of all capital invested to generate profits.</td>
</tr>
<tr>
<td>4- Return on equity</td>
<td>( ROE = \frac{Net\ income/shareholder\ equity}{100} )</td>
<td>Indicates the earning power of equity to generate profits.</td>
</tr>
</tbody>
</table>


As shown in Table 4.1, profitability ratios have four measures. The first two measures (GOP) and (NPM) use sales generated to determine the company’s ability to generate profit. On the other hand, (ROCE) and ROE) use the capital employed or shareholder equity only, to determine the company profitability. According to those two perspectives of measuring profitability, business profitability could be improved through one of two approaches or scenarios, as shown in Figure 4.1.
The first option focuses on increasing sale revenues while reducing the direct cost of selling, such as advertising, as well as reducing administration overhead, such as salaries, wages, etc. The second option focuses on reducing the amount of capital invested in the company through increasing the exploitation of existing fixed assets in the company and decreasing dependence on working capital, as well as reducing long-term funding and stock and increasing short-term funds.
4.3.1.2 Investment Ratios

Investment ratios evaluate business performance from the viewpoint of shareholders and investors that purchased or intend to buy shares in a firm, in order to get regular income in the form of dividends and share price increases (Adams, 1997). Investment ratios include different measures as shown in Table 4.2.

Table 4.2 Investment Ratios

<table>
<thead>
<tr>
<th>Ratio</th>
<th>Equation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-Earnings per share</td>
<td>EPS=Net income/ Number of ordinary shares</td>
<td>Indicates after tax profits generated for each share in a company.</td>
</tr>
<tr>
<td>2-Operating cash flow per share</td>
<td>OCF=Operating cash flow- preference dividends/ Number of ordinary shares</td>
<td>Indicates the ability of a company to pay profits before tax and interest for each share.</td>
</tr>
<tr>
<td>3-Dividend per share</td>
<td>DPS=Dividends announced during the period/ number of shares</td>
<td>Indicates profits actually paid for a shareholder from holding shares in a company.</td>
</tr>
<tr>
<td>4-Dividend payout ratio</td>
<td>DPR=Dividends announced for the year/ Earnings for the year available for dividends*100%</td>
<td>Indicates proportions or percentage of earnings that a company pays out to shareholders.</td>
</tr>
<tr>
<td>5-Dividend cover ratio</td>
<td>DCR=Earnings for the year available for dividend/ Dividend announced for the year</td>
<td>Indicates the ability or comfort ability of organization to pay dividend for shareholders.</td>
</tr>
</tbody>
</table>

Source: Atrill (2003, p: 70-75)

As shown above, five indicators are included for helping current and potential investors assess the ability of a company to pay gross and net profits from their shares or investment. That is, these indicators focus on identifying how much each share generates
profit. Moreover, these measures show to what extent the company prefers to distribute and pay profits to shareholders rather than reserving profit.

4.3.1.3 Activity Ratios (Assets Management Ratios)

Activity ratios are known also as efficiency ratios because they measure how efficient the firm is in managing its assets. Therefore, activity ratios aim to know if the total amount of each type of asset, as reported on the financial statements, seems acceptable, too high, or too low (Brigham and Houston, 2004). This group of ratios includes different measures as shown in Table 4.3.

### Table 4.3 Activity Ratios

<table>
<thead>
<tr>
<th>Ratio</th>
<th>Equation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-Fixed assets turnover</td>
<td>( \text{FAT} = \frac{\text{Sales}}{\text{Net fixed assets}} )</td>
<td>Indicates how effectively the firm used its fixed assets such as equipment and plant to generate sales.</td>
</tr>
<tr>
<td>2-Total assets turnover</td>
<td>( \text{TAT} = \frac{\text{Sales}}{\text{Total assets}} )</td>
<td>Indicates how effectively the firm exploited all assets to generate sales.</td>
</tr>
<tr>
<td>3-Days sales outstanding</td>
<td>( \text{DSO} = \frac{\text{Receivables}}{\frac{\text{Annual sales}}{360}} )</td>
<td>Indicates the average length of time that a firm should wait after making sales before receiving cash.</td>
</tr>
<tr>
<td>4-Inventory turnover</td>
<td>( \text{IT} = \frac{\text{Sales}}{\text{Inventories}} )</td>
<td>Indicates the number of trips that finished goods took each year.</td>
</tr>
</tbody>
</table>

Source: Brigham and Houston (2004, p: 79-81)

As shown, activity ratios have four measures. These ratios indicate the ability of a company to utilize its assets to generate profits. Therefore, FAT and TAT investigate the company’s efficiency to generate profits from its assets. DSO indicates the number of days that sales remain in credit before the funds are collected. Moreover, this group of ratios shows how much time goods stay in the company as inventory.

4.3.1.4 Liquidity Ratios

Liquidity ratios are used to evaluate a firm’s ability to pay off its debts as they come due over the next year, through quickly converting its assets to cash without very much reducing the asset’s price. In other words, liquidity ratios show the relationship between
the firm’s cash and other current assets (Brigham and Houston, 2004). Thus, they measure a firm’s ability to exchange assets for cash, quickly and at low cost, in order to pay its short-term obligations (Brealey, Myers and Marcus, 2001). This group has three ratios as shown in Table 4.4.

Table 4.4 Liquidity Ratios

<table>
<thead>
<tr>
<th>Ratios</th>
<th>Equation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-Current ratio</td>
<td>CR=Current assets/Current liabilities</td>
<td>Indicates a firm ability to cover its current liabilities through converting current assets to cash in the near future (one year’s time).</td>
</tr>
<tr>
<td>2-Quick or Acid-test ratio</td>
<td>QR=Quick assets(current assets- inventories)/ current liabilities</td>
<td>Indicates a firm ability to pay its current liabilities through its current assets excluding inventories.</td>
</tr>
<tr>
<td>3-Defensive interval ratio</td>
<td>DIR=Quick assets- Daily cash expenses</td>
<td>Indicates the number of days that quick assets cover and meet normal cash expenditures.</td>
</tr>
</tbody>
</table>


Clearly, each measure has different elements. For example, CR uses current assets in the company whereas QR excludes inventories since such elements are hard to quickly convert to cash. Therefore, QR is a quick ratio of liquidity. Similar to the first two measures, DIR indicates how many days the company needs to pay off its daily expenditures from its quick assets.

4.3.1.5 Leverage Ratios

Leverage ratios focus on determining the proportion of owners’ contributions to a business. Namely, this group of ratios measures the extent to which the firm is using long term debt in a company capital structure (Brigham and Houston, 2004). Additionally, leverage ratios provide an indication of the long-term solvency of the firm using long term debt. This group includes ratios shown in Table 4.5.
Table 4.5 Leverage Ratios

<table>
<thead>
<tr>
<th>Ratios</th>
<th>Equation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-Total debt to assets</td>
<td>TDA=Total debt (current liabilities + long term debt)/ Total assets * 100</td>
<td>Indicates the extent to which borrowed funds have been used to finance the company’s assets.</td>
</tr>
<tr>
<td>2.Total debt to equity</td>
<td>TDE=Total debt (current liabilities + long term debt)/Total equity * 100</td>
<td>Indicates the funds provided by creditors versus the funds provided by owners.</td>
</tr>
<tr>
<td>3-Interest coverage</td>
<td>IC=Earning before interest and taxes/Interest expense</td>
<td>Indicates the ability of the company to meet its annual interest obligation.</td>
</tr>
</tbody>
</table>


As shown in Table 4.5, the solvency ratios show to what extent the company used long-term debt in its capital structure. Three measures are categorised in this group. The first two ratios (TDA and TDE) show to what extent the company used long-term debt and equity for funding its business. IC investigates the ability of the company to serve and pay its annual long-term interest.

4.3.1.6 Limitations and Enhancements of Financial Performance Measurements

The financial performance measures discussed in the previous sections have been used extensively to evaluate and measure the financial performance of companies. Although such ratios provide a yardstick that can judge how close a company is to its declared and predetermined objectives (Morgan, 2004), the literature shows limitations and problems for using the financial performance perspective for measuring and judging performance. For example, if a company is experiencing seasonal business conditions, the variations and fluctuations of such conditions will influence the results of these ratios. In addition, accounting practices and procedures may vary among companies and industries, which leads to differences in computed ratios. Moreover, such ratios can mislead managers and
analysts when unusual transactions or events occur (Keown et al., 2008; Ross et al., 2008).

In this regard also, Ghalayinin and Noble (1996) reviewed the most common limitations of using financial measures for measuring business performance only; they found that such ratios use lagging metrics that are not related to corporate strategy and are unable to quantify improvement efforts (e.g. time reduction, customer satisfaction). These lagging metrics are inflexible and expensive; they contradict continuous improvements; and they do not meet and reflect the customers' requirements. In addition, Ghalayinin and Noble (1996) claim that reducing costs and increasing profits does not necessarily mean always that the operation and management of a company is efficient and perfect.

In his review for developments and trends of PMSs, Philips (1999) appreciated using traditional financial measures, such as return on investment (ROI), for measuring performance. However, Philips mentioned that these kinds of measures offer a narrow focus and explanation, and consequently encourage managers to focus on the short run of expenses. As mentioned in Phillips' review, Fisher (1995) introduced three main reasons for using and adopting non-financial measures as performance measures instead of using financial measures only. First, financial measures tend to be backward-looking and offer results about functions within the organisation rather than cross functions. Second, an unstable and uncertain environment makes it difficult to identify the outcomes of drivers that lead to competitive advantages. Third, such non-financial measures represent a very important element of organisations' philosophies and improvements such as total quality management. In this regard also, Phillips (2007) asserted the idea that the success of any organisation and business may go beyond achieving short-term financial results, especially in a complex business environment.

In order to overcome deficiencies and criticisms of the financial measures displayed in this sub-section, literature suggested two solutions for measuring the business performance of a company (Phillips and Louvieris, 2005; Phillips, 1999). The first solution asks for enhancing the accounting and financial measures employed and used by managers to improve the management control and decision-making process. In this respect, some improvements have been made for the financial measurement such as developing the economic value added approach (EVA) (Neely, Marr, Roos, Pike, and Gupta, 2003). On the other hand, the second solution for overcoming limitations of the
financial performance perspective suggests using more qualitative and non-financial measures and supplementing them to the financial measures in a more comprehensive framework, as will be discussed in the next sub-sections.

As a technique suggested within the first solution, Economic Value Added (EVA) was developed to focus on shareholder value or the wealth of shareholders and costs of capitals for evaluating the financial performance of a company. Such a performance measurement approach was developed by Stern Stewart & Company (a consulting company). After calculating the EVA value, the financial performance of a company can be easily assessed. Stewart (1991) claim that the EVA approach can be used for several reasons, namely: as a financial decision-making tool; for setting goals, evaluating performance, and determining bonuses; for communicating with investors, and for capital budgeting. The EVA approach can be calculated as shown in the following equation:

\[
\text{EVA} = \text{Cash-based operating profits (after-tax operating income)} - \text{capital used} \times \text{average cost of capital}
\]

This equation indicates that operating costs should reduce revenues, and costs of capital should be used to generate profits in the business. Thus, EVA considers all costs (cost of debt and equity) used in the business in order to evaluate and assess performance (Aggarwal, 2001). As a result, EVA investigates whether or not the operating costs of the capital have been achieved. To understand the result of such an approach, if the value is positive, that means the company creates shareholder wealth. In contrast, if the value is negative, that implies the company is reducing the shareholders' wealth.

4.3.2 Integrated Performance Measurement Systems

According to the former limitations of the financial performance perspective, the balanced PMSs combining non-financial measures with financial measures were suggested to overcome the previous limitations of the financial measures and to gain an overall view of the company's performance (Ghalayinin and Noble, 1996). In other words, PMSs were advised to be more balanced through integrating financial and non-financial measures into a single system (Bergin-Seers and Jago, 2007). Thus, the dissatisfaction of the traditional performance measures forced management to use
financial, non-financial, internal, and external measures in order to have a balanced and multi-dimensional view of performance (Mills, Wilcox, Neely and Platts, 2000). Besides the former criticisms of the traditional performance measures discussed in the former sub-section, Neely (1999) offered seven reasons to justify merging and adopting the integrated business performance systems. These seven reasons are as follows: the changing nature of work (i.e. process automation), increasing competition, specific improvement initiatives such as Total Quality Management; national and international awards; the ever-changing organizational roles (e.g. the role of the financial department has moved from providing financial reports to providing necessary information for running the business); changing the external demands and regulations; and finally, the power of information technology.

To conclude, according to limitations of financial measures and changes of the internal and external environment, the literature shows a revolution in the last 20 years of using integrated systems and frameworks for measuring performance. The main objective of these frameworks has been to help organizations to identify a set of measures that reflect their objectives and assess their performance (Kennerley and Neely, 2004). To shed more light on this approach, the next sub-sections display the most common and popular systems developed in the literature.

4.3.2.1 The Balanced Scorecard System (BSC)

It was claimed by Kaplan and Norton (1992) that an effective business performance measurement system should have balanced measures combining the financial and non-financial perspectives together in a single model to offer a more strategic and comprehensive view of performance. The findings of a research project that studied 12 leading companies confirmed that no single measure can provide a clear view of business performance as well as reaching targets. Accordingly, Kaplan and Norton (1992) introduced the balanced scorecard system as a PMS (Kaplan and Norton, 1992; 1993). Thus, the term “balanced scorecard” implies measuring and monitoring performance by using financial and non-financial measures, and leading and lagging measures to cover the long-term and short-term objectives (Denton and Whilte, 2000). Figure 4.2 shows the components of the balanced scorecard system.
Figure 4.2 The Balanced Scorecard (BSC)

Source: Kaplan and Norton (1992, p: 72)

Figure 4.2 indicates that the BSC system comprises a set of performance perspectives to provide a comprehensive insight of performance. Thus, the BSC system measures financial performance in conjunction with other performance perspectives, including, customers' needs and satisfaction, organisational innovations, and finally, the internal business process. According to Kaplan and Norton (1996), users of the BSC system do not need to use only short-term financial measures to measure and evaluate the company's performance. Conversely, the BSC supplements the financial measures with other criteria to measure performance from three alternative perspectives as shown in Figure 4.2. As a result, the BSC system lets users track their financial results and at the same time, monitor and check the progress of other intangible assets.

However, Brignall (2002) rejected the comprehensive view in the BSC system and claimed that such a system measures only three perspectives and stakeholders: shareholders (financial performance), customers (customer relations), and employees (internal and learning perspective). According to Brignall (2002), the BSC does not take into consideration other important perspectives including environmental and social matters (Brignall, 2002).
Ghalayini and Noble (1996) mention two main advantages of the BSC system. First, it offers one management report summarising the disparate elements of a company’s competitive strategy. Second, it prevents sub-optimization by asking managers to consider all operational measures at the same time. Sanger (1998) acknowledges using the BSC system. In this regard, he states that the BSC system recognises the weaknesses of traditional measurement systems, which focus only on the financial measures that offer back-forward perspective and evaluation. Moreover, Sanger attributes the success and spread of the BSC system to the appropriateness and quality of measures used in this system.

Brander Brown and McDonnell (1995) state that this system has two vital advantages: first, it provides information from different aspects of the organisations; second, it minimizes the overloading and overlapping of information by identifying a specific number of measures. Atkinson and Brander Brown (2001) also describe this system as a valuable tool that balances the relationships and trade-offs between different measures and aspects of performance in order to link the operational aspects of performance with the organisation’s strategy and objectives.

Amaratunga, Baldry, and Sarshar (2001) review the key features of the BSC system and issues needed to use and implement this system. According to their analysis, Amaratunga et al (2001) announce that the BSC system has been used widely and successfully as a management framework for measuring performance since it assesses performance by taking a balanced view across a wide range of performance perspectives. In the same regard, Norrekilt (2000) acknowledges the integration of the financial and non-financial measures in a single measurement system. As a result, Norrekilt claim that the BSC includes measures four outcomes and drivers of performance linked together in order to provide a feed-forward control system. However, Norrekilt (2000) states that the BSC offers problematic assumptions concerning the causal relationships between the four dimensions proposed in the system, which may lead to faulty and unrealistic positive performance.

In their review of the measures, steps, and software required to use the BSC, Gautreau and Kleiner (2001) identified some other shortcomings of the BSC, such as the difficulty
to quantify, decide, and establish the measures required to measure performance, especially the non-financial measures and dimensions, which in turn leads to several and complex systems. Moreover, a huge amount of time and resources are needed to keep the BSC system updated and effective. In addition, it is difficult and time-consuming to implement the BSC system.

Although Letza (1996) offered rich explanations, cases, and examples for how to implement and use the BSC system, Letza identified some limitations of the BSC framework and therefore warned practitioners and users of some common mistakes and limitations. These included measuring the wrong things due to the numerous and detailed performance measures; difficulty for measuring all activities of the organisation; and finally, the possibility to have conflict between senior managers after removing all functional lines of authority among them. Phillips (1999) also introduced other limitations of the BSC system including: difficulty in identifying vital measures that will lead to success; difficulty in sharing and communicating the BSC system to all levels within the same organisation; and finally, the BSC system was mainly developed to maximise the shareholder value over others (i.e., the system ignores the needs of other stakeholders).

Furthermore, Hundson, Smart and Bourne (2001) state that the BSC system suffers from the lack of integration among all levels within the organisation, and also between top and operational levels of measures, which makes the achievement of the strategy problematic. Neely et al (1995) also questioned why the BSC system does not have indicators about what competitors are doing (i.e., absence of competitiveness dimensions and indicators).

According to all criticisms of the original modelling and mechanism of the BSC system, Kaplan and Norton conducted two waves of improvements in the BSC system. The first wave of improvements involves using and creating strategy maps to identify the critical perspectives and measures and show the causal relationships among them. According to Kaplan and Norton (2000), such strategy maps can provide a visual representation of a company’s critical objectives and relationships between those objectives that drive the company’s performance. In other words, strategy maps provide visual frameworks that insert the different dimensions and aspects of the balanced scorecard into a cause-and-effect chain. For this reason, Kaplan and Norton developed a template that companies from various industries can use.
In this respect, Phillips (2007) claim that the key improvement of the BSC system was the replacement of the simple causal relationships between perspectives with identified cause-and-effect relationships. In contrast, Neely et al (2003) refute this idea and argue that although the strategy maps use the same logic of the BSC system, they provide a new and different visualisation of the four perspectives.

In the second wave of improvements, Kaplan and Norton (2001) claimed that the BSC system introduced in 1992 had evolved over the last ten years from a pure performance measurement to an organizing framework to assure and achieve successful implementations of a strategy. They refer to their model as a strategy-focused system, and they suggested five common principles to make the BSC system a strategy-focused system: first, translate the strategy to operational terms; second, align the organisation to the strategy; third, make strategy everyone's job; fourth, make strategy a continual process; and finally, mobilise leadership for change.

Although the former five suggestions were not discussed and implemented widely in the literature, Kaplan and Norton (2001) claim that the BSC system became an important tool for transforming the company's mission and strategy into detailed goals and measures covering a wide range of performance perspectives. In this regard, the BSC approach identifies a set of goals and objectives for an organisation and then develops measures to track the progress of achievements and the implementations of those goals and objectives. Hence, the BSC system has moved from a radical performance measurement system to a system for managing and controlling strategy implantation (i.e., a strategic management tool) (Hepworth, 1998; Evans, 2005).

To conclude, the BSC is a key performance measurement system that integrates the financial with the non-financial measures of performance. Although academics and practitioners have appreciated such a system, some limitations have emerged, especially in identifying the critical measures that should be used and the difficulties for understanding the relationships between perspectives within this system. However, the recent implementations of the BSC system imply that it is not only a performance measurement system, but also it is a strategic system aligning departmental goals with the company's overall strategy. According to the changes and developments of the BSC,
Phillips and Louvieris (2005) state that this system has developed to perform two roles: strategic and operational controls. As a result, the BSC approach became a performance managerial tool that helps organisations to monitor their performance and link objectives and measures to strategies. In a recent paper in which Phillips (2007) reviewed the latest trends of the BSC system practices and functions, he appreciated the strategic control function of the balanced scorecard system suggested by Kaplan and Norton (2001) (the strategy-focused organisation model).

It is worth noting that several industries and countries have implemented this system in particular, apart from other systems and frameworks. In this respect, a survey conducted by the American Institute of Public Accountants and Maisel in 2001 indicated that 43 percent of the members were using and adopting the system. Evans (2005) attributed the popularity of this system to its inherent advantages and to the intense marketing efforts and promotion of this system.

4.3.2.2 The Strategic Measurement Analysis and Reporting Technique (SMART)
This system, which is also called the performance pyramid system, was developed by Cross and Lynch after doing surveys of senior managers in the manufacturing industry (Cross and Lynch, 1988). The developers of this system recognized the limitations of the traditional financial measures. The main purpose of this model is to link an organization’s overall strategy with its operations in order to sustain success. This system translates the vision and strategy into objectives for lower levels in the organization and transmits measures of business performance upward through the organization. Figure 4.3 shows the SMART system.
As shown in Figure 4.3 above, the SMART system divides a company into four levels. First, there is the corporate management level, which represents the uppermost level of the organization. At this level, the management formulates the vision – the corporate strategy for the company. Second, at the business unit level, the management translates the company’s vision into long-term market goals (e.g. growth and market penetration) and short-term financial goals (e.g. positive cash flow and profitability). At the third, which is the business operating system level (BOS), the strategic point for linking each department’s performance with the overall strategy and performance of the business is determined. Measurements at this level focus on the entire operating system, not just on a single department. At this level, management translates the previous objectives into tangible, key measures that represent performance drivers such as customer satisfaction, flexibility, and productivity. Finally, the fourth is the department level, which converts and translates the previous key measures into more explicit operational measures for each department, such as quality, delivery, cycle time, and cost. Thus, the objective for each function or department is to support the business operating system through increasing quality, improving delivery, reducing cycle time, and cutting costs.
As argued by Cross and Lynch (1988), achieving objectives for all levels leads to reaching the strategic objective or vision of the organization as a whole. To do so, each level has suitable objectives based on and resulting from the level above it. On the other hand, each level has special measures based on the performance of the level below it. Thus, this system of measuring business performance has a two-way communication feature built in. The first way focuses on spreading the objectives from the top down, while the second focuses on decompressing measures from the bottom up.

Ghalayinin and Noble (1996) noted that the measures used in this system form the keys to achieve higher-level results and successful implementation of the company strategy and vision. Likewise, Neely, Mills, Platts, Richards, Gregory, Bourne, and Kennerly (2000) appreciated this system due to its valuable and favourable features, including, distinguishing between measures interested in external parties (e.g. customer satisfaction, quality, and delivery) and measures interested in the internal business (e.g. productivity, cycle times waste).

Despite its attempt to link the corporate objectives of an organisation with its operational performance measures, the SMART system doesn't provide clear discussion to identify key measures for the operational measures i.e. what measures are needed to measure quality, cycle time, and so on. In addition, this system did not conceive of the concept of continuous improvement (Ghalayini and Noble, 1996). In their review of performance practices in the SME, Hundson et al (2001) also mentioned that one of the main weaknesses of the SMART system is that it does not specify in any detail how to select measures or what process is required for developing measures. Laitinen (2002) also claimed that the SMART system did not provide sufficient discussion and justification for its choices of measures, and that the relationships between measures at the same level were not sufficient. However, Laitinen considered the hierarchical structure between levels and factors to be logical.

4.3.2.3 Performance Measurement System in the Service Industry (PMSSI)

According to the characteristics of companies in the service industry, Fitzgerald, Johnston, Brignall, Silvestro, and Voss (1991) developed a special system for the service context after examining a wide range of case studies in order to explore how managers in the UK service companies measured their business performance. Fitzgerald et al (1991)
claimed that the dimensions and measures selected in this model reflect the nature and characteristics of the service industry. Table 4.6 displays this system.

Table 4.6 Performance Measurement System in the Service Industry (PMSSI)

<table>
<thead>
<tr>
<th>Dimensions of performance</th>
<th>Types of measures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Results</td>
<td></td>
</tr>
<tr>
<td>1-Competitiveness</td>
<td>-Relative market share and position</td>
</tr>
<tr>
<td></td>
<td>-Sales growth</td>
</tr>
<tr>
<td></td>
<td>-Measures of customer base</td>
</tr>
<tr>
<td>2-Financial performance</td>
<td>-Profitability</td>
</tr>
<tr>
<td></td>
<td>-Liquidity</td>
</tr>
<tr>
<td></td>
<td>-Capital structure</td>
</tr>
<tr>
<td>Determinants</td>
<td></td>
</tr>
<tr>
<td>3-Quality of service</td>
<td>-Reliability, responsiveness, aesthetics, appearance,</td>
</tr>
<tr>
<td></td>
<td>cleanliness, tidiness, comfort, friendliness, communication,</td>
</tr>
<tr>
<td></td>
<td>courtesy, competence, access, availability, and security</td>
</tr>
<tr>
<td>4-Flexibility</td>
<td>-Volume flexibility</td>
</tr>
<tr>
<td></td>
<td>-Delivery speed flexibility</td>
</tr>
<tr>
<td></td>
<td>Specification flexibility</td>
</tr>
<tr>
<td>5-Resource utilization</td>
<td>-Productivity</td>
</tr>
<tr>
<td></td>
<td>-Efficiency</td>
</tr>
<tr>
<td>6-Innovation</td>
<td>-Performance of the innovation process</td>
</tr>
<tr>
<td></td>
<td>-Performance of individual innovations</td>
</tr>
</tbody>
</table>


As shown in the above table, this system links financial and non-financial measures, as well as qualitative and quantitative measures, in order to implement, control, and develop performance in a service organization. The system categorizes the six dimensions into two groups: results dimensions, which include factors that reflect the success of the chosen strategy (such as competitiveness performance and financial performance), and determinant dimensions, which contain factors affecting overall performance, such as quality of service, flexibility, resource utilization, and innovation.
Neely et al (2000) acknowledge this classification of measures, which can help to determine the lagging indicators (results dimensions) and leading indicators (determinant dimensions). In this sense also, Atkinson and Brander Brown (2001) described this system as a tool that integrates the accounting models with some relevant and useful operations management concepts and models. This model provides a combined and balanced range of performance measures (financial and non-financial) compatible with service industry style. In addition, this system provides a feed-forward and feedback control by including results and determinant dimensions of performance.

Mills et al (2000) also appreciated classifying dimensions and measures of performance into determinants and results, and stated that this system can give an early indication about future business performance as well as it can record what happened in the past. However, Hudson et al (2001) criticised this system, as it does not have any discussion or measures about customers or human resources as dimensions of performance in the service sector. Accordingly, this system is not able to offer a real and truly balanced view of performance. Laitinen (2002) also criticised the PMSSI since it does not offer enough argument regarding the theoretical basis for the dimensions chosen and the causal relationship between the two categories of dimensions of performance.

4.3.2.4 The Performance Prism

Neely, Adams, and Crowe (2001) developed the Performance Prism system as shown in Figure 4.4 as an effort to respond to the limitations inherent in the existing performance measurement systems. According to Kennerley and Neely (2004), this system combines the existing PMSs into one single framework and builds its methodology on their individual strengths. The main idea behind this system is that it gives more attention to the stakeholders of the company and encourages managers to answer critical questions from different perspectives. Neely et al (2001) claim that the Performance Prism system forms the second generation of the integrated performance measurement systems since this system motivates managers to think about the linkages between perspectives and measures of performance. Although the relevant literature did not widely discuss this feature of the Performance Prism system, Neely et al (2003) confirmed the idea by saying that this system was located in the second generation of PMSs since it adopts the concept of success and failure maps which can help management to identify and map important and critical points and objectives of an organisation.
According to the above Figure, the framework of this system includes five interrelated sides and perspectives. Neely (2002) states that integrating these five perspectives will ensure the comprehensive and integrated framework of an organisation’s business performance. The first facet refers to the stakeholder satisfaction. Neely et al (2001) claim that this perspective is broader and more comprehensive than the balanced scorecard’s view of stakeholders. In other words, the Performance Prism includes more stakeholders, such as investors, customers, employees, regulators, and suppliers, since those parties can contribute and affect the performance and success of an organisation. In contrast, the balanced scorecard system deals with investors and customers only. The second perspective focuses on strategies since this facet can let an organisation achieve and deliver value to its stakeholders. The answer to the question raised by this perspective lies in determining what strategies an organisation has to put in place to satisfy and achieve the stakeholders’ needs.

The third facet aims to know what process is needed to allow strategies to be delivered. The fourth facet in the Performance Prism framework is capabilities. Neely et al (2001) argue that this level of performance is new and important, which implies the combination of people, practices, technology, and infrastructure all working together in order to accomplish the organisation’s business processes. The key determination and question that should be made at this level is what capabilities are needed to operate processes.
Finally, the fifth perspective of this system is the stakeholders' contributions (i.e., the two-way relationship between stakeholders and the organisation). The developers of this system claim this perspective forms a new perspective in the PMS filed. For instance, on one hand, the employees wait for salary and recognition. On the other hand, the organisation needs its employees to contribute to the business by offering ideas and suggestions, and to remain loyal to the company.

Neely et al (2001) claim that previous measurement frameworks, according to their literature survey, did not recognise the relationship between the organisation and its stakeholders. For this reason, Neely et al (2001) consider the measurement of this relationship to be a unique feature of the Performance Prism. Moreover, Neely (2002) argue that this system has internal and external, and financial and non-financial measures, which helps to gain an efficient and balanced performance system. Moreover, Kennerley and Neely (2004) state that answering the five questions in this system can demonstrate the creation of stakeholder value and give a comprehensive and integrated overview of the company's performance since this system includes additional levels of detail for each facet. According to Neely et al (2001), several companies employed the Performance Prism system, such as, DHL, House of Fraser and other firms.

Carpinetti et al (2008) acknowledge the wide range of stakeholders included in this system, such as, employees, suppliers, regulators and communities. They note that addressing stakeholders' requirements and needs in this system leads to strategic directions of an organization's performance. However, Tangen (2005) claim that although this system has some strengths, including relying on the company's strategy first before proceeding to the measures selection stage and incorporating some new stakeholders (e.g., employees, suppliers, etc.) for measuring performance never measured before, this system did not offer sufficient discussion and explanation for how performance measures can be realised.

4.3.2.5 Other Integrated Performance Measurement Systems and Issues
Having shown the key and popular PMSs in the former sections, the current section aims to present briefly some other models and frameworks introduced in the literature for measuring business performance. For instance, Keegan, Eiler, and Jones (1989), developed an integrated and balanced PMS combining financial and non-financial
measures. This system, which is called the performance measurement matrix, classifies measures into cost or non-cost, and external or internal measures. Neely et al (1995) claim that this system is simple and flexible, but it does not accommodate all attributes of measures that are considered to be necessary.

In addition, Azzone, Masella, and Bertelè (1991) argue that the time dimension of performance forms a key source for gaining excellence and competitive advantage for organisations. Accordingly, Azzone et al proposed a framework in a matrix form consistent with time-based principles. Azzone et al (1991) claim that this framework of performance measurement is consistent with the strategic objectives of a company. As a different focus, the literature shows another system called the Skandia Navigator. Skandia (a Swedish financial services company) developed this system as a model for measuring the intellectual capital of an organisation. The unique characteristic of this model is that it gives a significant effort to measure a company’s intangible assets to measure the real value of the company rather than focusing on the traditional financial dimensions. Thus, the Skandia Navigator measures business performance by maintaining an index or list of financial and non-financial metrics for several areas, including financial capital, intellectual capital, human capital, structural capital, customer capital, organisational capital, innovation capital, and process capital (Edvinsson, 1997; Chen, Zhe and Xie., 2004; Bose, 2004; Marr, Schiuma and Neely, 2004).

As a novel, original, and contemporary framework, Khan and Wibisono (2008) developed a PMS that combines three different approaches (Knowledge Based, Gap Analysis, and Analytic Hierarchy Process). This system is called the hybrid knowledge-based performance measurement system (KBPMS). Khan and Wibisono claim that the KBPMS helps companies in the improvement and decision-making processes and to make the PMS consistent and practical for implementations. The KBPMS comprises five levels of business performance, namely business perspective, customer perspective, manufacturing competitive priorities perspective, internal process perspective, and finally, resource and method availability perspective. Each level of performance includes several dimensions. For example, the business perspective level has two dimensions: financial performance and market share. Obviously, the first two levels (business perspective and customer perspective) imply strategic performance, while the remaining levels form operational perspectives of performance.
To give more details about the KBPMS, on one hand, the GAP analysis method in this PMS measures the differences between the desirable and actual performance within each performance dimension of the five performance levels (i.e. GAP analysis identifies problems and deficiencies of all performance areas). On the other hand, the Knowledge Based (KB) and Analytic Hierarchy Process (AHP) methodologies is used to determine which one of the performance problems identified in the GAP process stage should be in priority of improvement. As a result, such a system gives ranks for priority of improvements in performance. In other words, the KBPMS identifies problems existing in different performance levels and areas, and offers prioritised recommendations for improvement.

Laitinen (2002) developed another PMS measure of business performance by using financial and non-financial factors and dimensions. The proposed system, which is called the integrated performance measurement system (IPMS), tracks the use of resources, from the point of resources allocated to the point when the results of the allocation are realized as revenues. Thus, such a system demonstrates and explains the causal relationships between factors. To do so, the IPMS uses seven financial and non-financial indicators grouped into internal and external factors. Laitinen (2002) claim that different types of organizations could apply the IPMS, irrespective of the company’s size, because it includes common factors and dimensions that are compatible with different companies, industries, and environments. Finally, Laitinen argue that the IPMS provides a well-grounded causal relationship by using a balanced model of related factors and dimensions.

The literature of PMS offered also some others frameworks, such as Brown’s (1996) input, processes, the outputs and outcomes system, Dixon’s et al (1990) performance measurement system questionnaire, Ghalayini, Noble and Crowe’s (1997) the integrated dynamic performance measurement framework, Neely, Richards, Mills, Platts and Bourne’s (1997) the Cambridge performance measurement process “the performance measure record sheet”, the European Foundation for Quality Management’s (EFQM), Business Excellence Model, and the Malcolm Baldridge Quality Award. However, Kennerley and Neely (2004) claim that the last three models were not designed primarily as performance measurement frameworks, but they tried to address some areas of
performance not discussed by the balanced scorecard framework. Therefore, the current section is not going to discuss these models due to the limited space of this chapter and for the need to cover some other issues in the PMS literature.

The preceding discussions in this section show that the literature has introduced several frameworks and systems for measuring business performance. In this sense, systems adopted a wide range of measures and dimensions and offered different mechanisms and explanations for the causal relationships among components. Unfortunately, such systems have common weaknesses and problems as shown in this chapter in terms of offering clear and sufficient explanations for the linkages between dimensions and perspectives of performance. In this regard, Laitinen (2002) claim that PMSs displayed in the literature are useful; however, they have two main problems. First, the majority of systems suffer from the need to offer a well-grounded justification for factors and measures chosen and selected. Second, most systems and models do not provide a logical foundation for the relationships between all of these factors to ensure consistency and successful implementation. As outlined by Neely et al (2005) in their review of the existing PMSs, the area of the PMS is complex; therefore, introducing a single unifying framework seems to be unrealistic. Accordingly, researchers have moved to focus and produce processes for designing, using, and implementing performance measurement systems rather than developing new frameworks.

In this area in particular, the literature shows debate in terms of how to identify, implement, and use the performance measurement measures and systems. This stream of research called the process of performance measurement system design. As outlined by Neely et al (2000), the process for using and implementing the balanced systems is still not well understood, nor has it been completely operationalized, as can be seen in their comment: “There have been numerous attempts to document performance measurement system design processes, nearly all of which end up as rather open-ended and vague statements” (Neely et al., 2000, p. 1127).

As a result, several scholars have tried to establish and offer a generic guideline of such process to design, implement, and put into practice such performance measurement systems. Accordingly, instead of developing new integrated performance measurement systems, researchers have tried to introduce guidelines and processes for designing and
implementing performance measurement systems. In this sense, some efforts emerged such as the criteria introduced by Wisner and Fawcett (1991). They developed nine processes or steps for performance measurement system design: (1) define the firms' mission statements, (2) identify the firms' strategic objectives, (3) develop an understanding of each functional area's role in achieving the strategic objectives, (4) develop a performance measure for each functional area, (5) communicate strategic goals to lower levels and establish more specific measures at each level, (6) assure consistency with strategic objectives among the performance measures at each level, (7) assure the compatibility of all performance measures in all functional areas, (8) use results to define competitive positions and problem areas, and (9) periodically re-evaluate the appropriateness of the current PMS to the current competitive environment. Keegan et al (1989) also recommended fewer and simpler steps, namely: (1) to define the strategic objectives of the company and translate them into divisional goals and individual actions, (2) to decide what to measure, (3) to instil the PMS into the management's thinking. In this regard also, Neely et al (2005 and 2000) reviewed the processes of performance system design introduced and developed by other researchers such as Kaplan and Norton (1993), who developed eight-step processes.

Based on other works in the relevant literature, Franco-Santos et al (2007) summarised the steps and processes of designing and implementing a PMS in five stages: (1) selection and design of measures, (2) collection and manipulation of data, (3) information provision and interpretation, (4) performance evaluation and rewarding, (5) system revision and conducting feedback. However, Franco-Santos et al (2007) claim that without implementing the first three steps, it would be impossible for any company to have a BPM system.

In this respect also, Bourne, Mills; Wilcox, Neely and Platts (2000), claim that most of the balanced performance frameworks (e.g. Kaplan and Norton, 1992; Cross and Lynch, 1988; Fitzgerald et al., 1992) focused mainly on the early stages of development i.e. conceptual models without explaining how to implement and use the performance systems. Accordingly, Bourne et al (2000) suggested a framework helps to give better understanding for the other stages of implementing and using performance measurement systems. The proposed formwork includes three sequence phases and processes to use a performance measurement system; first, decide on and designs the necessary performance
measures; second, implement the performance measures; and finally, use the performance measures. Three UK manufacturing companies tested the proposed framework over a period of two years. The results of the longitudinal study recommend adding another phase called the continuous updating and reviewing of measures and targets in order to align the performance measurement system with a company's strategy.

The recommendation introduced by Bourne et al (2000) was supported by Anderson and McAdam (2004), who declared that processes for designing performance measurement systems should consider and adopt more dynamic methods in order to accommodate the evolving changes in the market. More recently, Burgess et al (2007) contributed to this area of debate, according to the findings of the literature review. More precisely, they found that no single design of PMS would suit all organisations and settings; for this reason, users of PMSs should adapt and update their PMSs according to changes that occur in the internal and external business environment.

According to the above discussion introduced by Bourne et al (2000), Bititci and Turner (2000), Anderson and McAdam (2004), and Burgess et al (2007), it is obvious that the business performance system design should be more flexible and should incorporate the continuous reviewing and updating function to assure successful implantations of performance systems.

Kennerley and Neely (2005) argue that although the literature has identified the need to develop and design dynamic performance measurement systems in order to cope with and reflect changes in the internal and external environment, there is a limited amount of preliminary literature concerning how to develop a dynamic performance measurement system and what factors or changes affect this evolutionary process as can be seen in their comment:

"These streams of work result in new research problems being identified – namely how to develop dynamic rather than static measurement systems" (Neely, 2005, p. 1272).

In other words, Kennerley and Neely (2005) claim that there is no empirical investigation of how to make dynamic performance measurement systems in practice. To answer this
gap in the literature, Kennerley and Neely (2005) developed a model with some factors that affect the evolution of performance measurement systems. According to this model, organisations have to consider some key capabilities, including effective processes, appropriate skills and human resources, appropriate culture, and flexible systems. To put it more simply, organisations must demonstrate and consider these capabilities in order to manage the evolution of performance measurement systems effectively.

In a recent paper, Olsen, Zhou, Lee, and Padunchwit (2007) claim that the relevant literature offers a good understanding of the conceptual issues of how to design balanced PMSs. However, the literature shows weak and insufficient research in terms of how to improve and evolve the existing PMSs. They argue that there is a gap between the normative design of a PMS (i.e. how to design a PMS) and the evolution and continuous improvement of a balanced PMS. Based on their case study, they found that the design of a PMS represents a complex and evolutionary process.

To conclude, this section shows that the PMS literature introduced several and different balanced models for measuring business performance in different industries and settings by different authors. Obviously, these systems suggested various measures, dimensions, and logics for the relationship among measures, dimensions, and levels with an organization. However, it seems that developing a generic and single system suitable for all settings covering the common limitations is not possible. For this reason, the literature has turned its attention and concern to another area of research – the process of designing performance measurement systems. Unfortunately, few efforts have emerged and been developed to answer and cover these processes. Recent processes suggest developing dynamic performance measurement systems by conducting regular review of measures used and whole systems. Discussion in this section reveals that there is more work needed to build a dynamic performance measurement system to keep alliance between measures and strategy and internal and external changes.

4.3.2.6 Trends and Developments of Performance Measurement Systems

The previous sections indicate that the literature of PMS has been going through several phases of developments and improvements. However, such discussions make it difficult to identify and track steps and changes that have occurred in the PMS literature in the last
few decades. For this reason, this section aims to summarise and track changes and developments of the PMS literature.

In his review of the evolution of the PMS's literature, Neely (2005) summarised the developments and trends of this area into five phases: he called the first phase "the problem identification." This phase criticized and discussed the limitations of the financial and accounting methods. As presented previously in this chapter, the limitations of the traditional financial accounting measures were the main topic and debate in this phase, which lasted until the 1980s. The second phase, which had begun by the early 1990s, focused on offering potential solutions through developing balanced measurement systems (e.g., the BSC, SMART, determinate, and results model, etc.) in order to overcome limitations and problems outlined in the first phase.

Although the second phase has made significant development and contribution to the PMS literature, such models and frameworks were criticised by scholars and practitioners, as was discussed previously in this chapter. For instance, Ghalayini and Noble (1996) claim that PMSs that emerged in the late 1990s were limited for several reasons. Their focus was on monitoring performance rather than continuous improvement; they did not provide any mechanism for identifying which objectives should be achieved in a specific time; they were not dynamic in nature since they did not revise critical areas and measures of performance; they were not forward-thinking, as they did not compromise predicting techniques; and finally, most systems that exist do not emphasize the importance of time as a critical performance measure.

The third phase, known as "methods of application," was involved in offering processes, methods, and ways to apply and populate the proposed frameworks developed in the second phase. According to this phase, several contributions emerged through suggesting different and several processes, rules, and regulations for designing PMS as introduced previously in this chapter. Researchers in this phase tried to introduce processes for designing, using, and implementing PMSs rather than developing new frameworks (Neely et al., 2005). It is worth stating that this phase continued throughout the late 1990s until 2000.

The fourth phase, known as "the empirical investigation phase," was interested in offering rigorous analysis of the existing frameworks developed specially for the BSC
system. The aim of this phase was to prove and investigate the theatrical validity of the existing frameworks and methodologies. Based on this phase, a new phase and stream of research emerged in the PMS literature (the fifth phase) known as “the theoretical validation phase.”

To offer a different perspective of classification and to focus on the integrated (balanced) performance systems only, Neely et al (2003) reviewed the developments of the balanced system introduced over the last decades and summarised these developments into three waves of generations. The first generation of PMSs combined the non-financial measure with financial measures such as the Balanced Scorecard System. Although performance measurement systems in this wave made a significant contribution to the literature, they did not provide enough explanation for the linkages between different performance measures within these systems.

The second generation of PMSs tried to overcome the limitations of the first wave by using the strategy and success maps as suggested by Kaplan and Norton (2000). Finally, the third generation of the PMS indicated that the system should have three criteria in order to address and fulfil the characteristics of the third generation of PMSs. First, models should reflect the static as well as dynamic realities of organisations; second, information produced should offer right, rich, and rigorous details about the organisation, especially the intangible drivers of performance; and finally, models should be practical and aligned with all processes in the organisation in order to take action.

In order to support this view, Neely (2005) claim that developing a dynamic PMS was one of the most important goals for future research in the PMS literature. Accordingly, Neely (2005) urged scholars to examine the area of enhancing the flexibility of performance measurement systems in order to cope with and overcome organisational changes and updates.

In order to summarise and show all changes that have occurred in the PMS literature to date, Marchand and Raymond (2008) tracked changes and evolutions of the PMS field based on a four-period temporal scale. Details introduced by Marchand and Raymond (2008) captured developments and changes of PMSs according to several focuses as shown in Table 4.7.
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Definition of performance</td>
<td>Pure financial definition</td>
<td>Pure financial definition and some new operational performance definitions</td>
<td>Performance definition based on a company’s strategic objectives in relation to expectations of stakeholders</td>
<td>Performance definition based on the society’s (more stakeholders) judgement of the value/cost ratio and the company’s strategic objectives</td>
</tr>
<tr>
<td>Dimensions of performance</td>
<td>Financial measures (profitability, liquidity, etc)</td>
<td>Operational measures of performance with the financial measures</td>
<td>Several aspects of performance including financial performance, managerial performance (e.g. employees, clients, innovations, processes, learning) and finally manufacturing dimensions (e.g. flexibility, quality, productivity, etc)</td>
<td></td>
</tr>
<tr>
<td>Architectural form or logic</td>
<td>Vertical (i.e. organisational functions and levels)</td>
<td>Vertical and somewhat horizontal (intra- and inter-organisational processes)</td>
<td>Vertical, horizontal and balanced (i.e. integrating both vertical and horizontal logics)</td>
<td></td>
</tr>
<tr>
<td>----------------------------</td>
<td>--------------------------------------------------</td>
<td>-----------------------------------------------</td>
<td>---------------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Organisational role of PMS</td>
<td>Performance measurement and control tool.</td>
<td></td>
<td>A supporting tool for decision-making, continuous improvement, strategy</td>
<td>diffusion and development, managerial development, operations-strategy alignment.</td>
</tr>
</tbody>
</table>

Source: Marchand and Raymond (2008, p: 666-667)
Table 4.7 offers a visual and chronological explanation of changes and developments that have occurred in the PMS literature over the last decades based on different focuses and criteria, including definitions of performance, dimensions of performance, architecture and logic of performance measurement frameworks, and roles and output of performance measurement systems. The previous table shows changes on a four-period temporal scale (before 1980; 1980-1989; 1990-1999; and 2000-present). As a result of their review and summary of changes, Marchand and Raymond (2008) state that PMSs have evolved and been enriched to move from simply measuring performance to being a supportive tool for decision-making.

However, Marchand and Raymond (2008) found that the literature shows few and limited research on the application of information systems’ (IS) theories and models in PMSs. In this respect, they claim that the IS perspective can provide useful ways and methods for researching the field of PMSs, including development, implementation, and evaluation of PMSs in terms of output (e.g., scope, form, and quality) and socio-technical attributes (e.g. user-friendliness, accessibility, and security). Accordingly, Marchand and Raymond (2008) recommend more investigation and implementation in this area in order to gain a better understanding of PMS practices and to support those practices.

4.4 Financial and Operational Measures in the Hospitality Industry
Discussion introduced in section 4.3.1 shows some generic financial measures developed for measuring the performance of a company. Obviously, this approach implies using different ratios such as the profitability ratio, the liquidity ratio, the leverage ratio, etc. The hospitality industry has extensively utilized the ratio analysis approach, which is based on calculating the relationship between figures derived from different accounting statements. Banker, Potter, and Srinivasan (2005), for instance, mention that financial measures can be used in the hospitality industry to reflect the effectiveness of current and former activities.

Lockwood (2008), however, gives three reasons why these generic financial measures may have limited value and contribution when it comes to understanding financial performance in the hospitality industry. First, most financial results are aggregate data and don’t provide enough details about performance; second, the value of money is not constant within a country due to inflation; third, many hospitality enterprises are
expanding internationally, and therefore, results should be converted into a common currency using the current exchange rates. Unfortunately, exchange rates are changeable over time and do not reflect the real local economic conditions. Accordingly, the hospitality industry is advised to use other industry-specific indicators to measure performance rather than using the generic financial measures alone.

In this regard, the literature introduced several different industry-specific indicators and ratios for measuring financial and operational performance in the hospitality industry. The following tables show some of the common financial and operational measures adopted and used in the hotel industry.

Table 4.8 Financial Measures in the Hotel Industry

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Meaning</th>
<th>Equation</th>
</tr>
</thead>
<tbody>
<tr>
<td>TREVPAR</td>
<td>Total revenue per available room</td>
<td>Total revenue divided by number of rooms available at the hotel</td>
</tr>
<tr>
<td>COSTPAR</td>
<td>Operating cost per available room</td>
<td>All day-to-day expenses divided by number of rooms available</td>
</tr>
<tr>
<td>AVGRATE</td>
<td>Average room rate for a hotel</td>
<td>Total revenues divided by number of occupied rooms</td>
</tr>
<tr>
<td>OCCRATE</td>
<td>Occupancy rate for a hotel</td>
<td>Number of occupied rooms divided by number of available rooms</td>
</tr>
</tbody>
</table>

Source: Banker et al (2005, p: 399)

Table 4.8 reflects the operational and financial performance of hotels using various measures. TREVPAR, for example, emerged as one of the common indicators for measuring profitability in the hotel industry. However, it is worth noting that TREVPAR mentioned by Banker et al (2005) in the above table implies not just revenues generated from rooms, but it also includes all sales generated from all profit centres in the hotel, such as the restaurant, food and beverage concessions, the spa, and so on. Jagels (2007) distinguishes between operations of the rooms department and food and beverage department in the hospitality industry. Therefore, he displays separate measures for determining financial and operational performance in the two different departments. Table 4.9 displays measures related to the rooms department.
Table 4.9 Operational Performance Indicators in the Hospitality Industry (Rooms Dep)

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Equation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average room rate</td>
<td>Room revenue / rooms occupied</td>
</tr>
<tr>
<td>Occupancy rate</td>
<td>Rooms occupied / rooms available</td>
</tr>
<tr>
<td>Double room occupancy rate</td>
<td>Rooms doubled occupied (number of rooms occupied by more than one guest) / rooms occupied or Room guests / room occupied</td>
</tr>
<tr>
<td>RevPAR</td>
<td>Total room revenue / rooms available or Occupancy percentage x average room rate</td>
</tr>
</tbody>
</table>

Source: Jagels (2007, p: 171-174)

The average daily rate as displayed in Table 4.9 refers to the mean or average price charged for all hotel rooms sold in a specific period. In addition, the above Table shows two methods for calculating the double occupancy. The first method shows percentage of rooms occupied by more than one guest out of all rooms occupied, while the second method refers to average guests for all rooms occupied. Jagels (2007) states that double occupancy in as many rooms as possible is desirable for all hotels in order to increase usage of facilities and services offered in the hotel. The above Table indicates also that average room rate and occupancy percentage form key factors and elements for calculating the RevPAR ratio. Jagels (2007) asserts that hoteliers use RevPAR to measure the financial performance of the rooms department since it gives wider feedback about performance rather than using the single average room rate or occupancy percentages ratios.

In addition to ratios displayed in Table 4.9, Abbott and Lewry (2001) suggest using other ratios that can give more insights about customers and guests rather than merely about the hotel performance, such as average daily spend per guest and average stay per guest as shown in Table 4.10.
Table 4.10 Other Ratios in the Hospitality Industry

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Equation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average daily spend per guest</td>
<td>Total guest bills / total guests</td>
</tr>
<tr>
<td>Average stay per guest</td>
<td>Total rooms night / total guests</td>
</tr>
</tbody>
</table>

Source: Abboott and Lewry (2001, p: 179-180)

Ratios displayed in the above Table reveal valuable information about guests’ consumer behaviour during their hotel stay. On one hand, finding the average amount of money spent by guests helps hoteliers to know which guest segment is more profitable and thus worth attracting. On the other hand, calculating the average stay per guest helps operators decide which facilities to offer guests according to their length of stay and needs. After showing the most common measures in the hotel industry in particular, Table 4.11 displays ratios used in the food and beverage department.

Table 4.11 Operational Performance Indicators in the Hospitality Industry
(Restaurants and Food and Beverage Dep)

<table>
<thead>
<tr>
<th>Indicators</th>
<th>Equation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales per server</td>
<td>Meal sales revenue/number of servers</td>
</tr>
<tr>
<td>Guests per server</td>
<td>Number of guests served / number of servers</td>
</tr>
<tr>
<td>Seat turnover</td>
<td>Number of guests served / number of seats</td>
</tr>
<tr>
<td>Revenue per available seats</td>
<td>Sales revenue / number of seats</td>
</tr>
</tbody>
</table>


Ratios displayed in Table 4.11 measure the profitability and productivity of servers or employees offering the service. In other words, the first two indicators (sales and guests per server) inform how much money is generated and how many guests are served by each single employee or server. However, the third and fourth indicators (seat turnover and revenue per available seats) could lead to the customers’ perceptions of price charged or quality of food. Jagels (2007) and Coltman and Jagels (2001) recommend that hoteliers calculate and analyse these indicators. The relevant literature introduces other measures and ratios that restaurants and food and beverage departments can use. For example, Harris (1999) displays some ratios that have different purposes and give different indications as shown in Table 4.12.
Table 4.12 Performance Measures in Restaurants

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Equation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average food spend</td>
<td>Food revenues / number of covers</td>
</tr>
<tr>
<td>Average beverage spend</td>
<td>Beverage revenues / number of covers</td>
</tr>
<tr>
<td>Food cost percentage</td>
<td>Cost of food sold / food revenues</td>
</tr>
<tr>
<td>Beverage cost percentage</td>
<td>Cost of beverage sold / beverage revenues</td>
</tr>
</tbody>
</table>

Source: Harris (1999, p: 45-46)

After reviewing the most common measures, Adams (2006) classified ratios and measures developed in the hospitality industry into two groups. The first group combines ratios and measures related to the sales activities, while the second group includes measures lead and focus on cost reduction as shown on Table 4.13.
Table 4.13 Ratios Used in the Uniform System Accounts for the Lodging Industry

<table>
<thead>
<tr>
<th>Sales-related ratios</th>
<th>Cost-related ratios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Room occupancy percentage</td>
<td>Labour costs in relation to costs</td>
</tr>
<tr>
<td>Double room occupancy percentage</td>
<td>Laundry costs in relation to sales</td>
</tr>
<tr>
<td>Bed occupancy percentage</td>
<td>Servicing costs per room</td>
</tr>
<tr>
<td>Maximum rooms revenue</td>
<td>Cost per available room (CostPAR)</td>
</tr>
<tr>
<td>Average room rate per room occupied</td>
<td></td>
</tr>
<tr>
<td>Average room rate per guest</td>
<td></td>
</tr>
<tr>
<td>Room sales per front desk clerk</td>
<td></td>
</tr>
<tr>
<td>Total average spend of each guest</td>
<td></td>
</tr>
<tr>
<td>Revenue per available room (RevPAR)</td>
<td></td>
</tr>
<tr>
<td>Sales-mix ratio</td>
<td></td>
</tr>
<tr>
<td>Yield percentage</td>
<td></td>
</tr>
<tr>
<td>Number of room service per employee</td>
<td></td>
</tr>
</tbody>
</table>

**Food and beverage operations**

<table>
<thead>
<tr>
<th>Restaurant occupancy by meal or day</th>
<th>Wages in relation to sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average spend per cover</td>
<td>Material costs in relation to sales</td>
</tr>
<tr>
<td>Sales revenue per employee</td>
<td>Stock turnover</td>
</tr>
<tr>
<td>Percentage of beverage to food revenue</td>
<td>Stock days</td>
</tr>
<tr>
<td>Percentage of food/beverage to rooms</td>
<td>Expenses in relation to sales</td>
</tr>
<tr>
<td>revenue</td>
<td></td>
</tr>
<tr>
<td>Seat turnover</td>
<td></td>
</tr>
</tbody>
</table>

Source: Adams (2006, p: 188)

All ratios mentioned in Table 4.13 measure the financial and operational performance of hotels. However, Adams (2006) refers to RevPAR and yield percentage as the most significant set of statistics and measures in the hospitality industry, since the first ratio evaluates the earning power of rooms available for sale and the usage of the accommodation letting space in the hotel, while the second ratio “yield rate” can lead to evaluating the pricing policy used in a hotel. In this regard also, Harris (1999) claim that the RevPAR ratio can overcome limitations of using other ratios such as average room rate and occupancy percentage. According to Harris (1999), achieving high occupancy
does not mean good performance if this occupancy is achieved by low average room rate, and vice versa.

Moreover, Harris (1999) states that the yield ratio offers a comprehensive indication about the percentage of actual business achieved comparing to potential revenue calculated in advance on the basis of 100% room occupancy or whatever the occupancy is. The yield ratio can be determined by dividing actual room revenues by maximum potential room revenues. Although Harris (1999) claim that the RevPAR and yield ratios form the most important and sensitive ratios in the hospitality industry, literature shows that there are some other important measures such as the occupancy rate, which represents a basic and important indicator about the room capacity utilizations. In this regard, Bardi (2007) acknowledges using the occupancy ratio, since it reveals the success and effectiveness of the hotel’s staff to attract customers and guests, and because it can determine the potential gross income for any hotel establishment.

Besides limitations and deficiencies attributed to the financial and accounting measures mentioned previously in the generic financial measures, some authors highlight some other problems and disadvantages of financial and operational measures used and developed in the hospitality industry. Adams (2006), for example, argue that using these ratios might confuse users due to several and multiple advices, equations, and methods for calculating such measures. In other words, choosing, defining, and calculating these measures depend primarily on personal judgement.

Wassenaar and Stafford (1991) also criticised the traditional economic indicators used in the hospitality industry, including average occupancy and average room rates, for several reasons: first, these two rates are not always available for all destinations or properties; second, ratios are normally collected by surveys, which cannot represent the whole industry; third, some operators do not reveal their true rates and results. According to these criticisms, Wassenaar and Stafford (1991) introduced an alternative indicator called the Lodging Index, which disclose average nightly revenue earned for each room, vacant or occupied, within a given city or region during a specific period. Obviously, Wassenaar and Stafford’s index is similar to the RevPAR ratio, but the lodging index is useful for local travel destinations and can be derived from two resources including transient occupancy tax information and occupancy and room rates statistics. Moreover,
Wassenaar and Stafford claim that the Lodging Index can be used to double-check the occupancy and average room rates information obtained by surveys.

Jeffery and Barden (2000), on the other hand, consider the hotel occupancy ratio as a valuable and acceptable method for measuring hotel performance because such occupancy data can be used in the process of marketing strategy. However, despite this power of the occupancy rate, Jeffery and Barden refused the fact that such a rate forms a comprehensive indicator of profitability, since high occupancy gained by price discount policy can reduce average room rates. Accordingly, Jeffery and Barden confirm the suitability and validity of RevPAR as a profitability indicator of hotels.

Conversely, Slattery (2002) questioned the reliability of RevPAR as a measure of a hotel’s profitability. To put it more simply, Slattery argue that this ratio is problematic and flawed due to mistaken practices undertaken by hoteliers for calculating elements of RevPAR, including room nights available, room nights sold, rooms occupancy, and turnover. Moreover, Slattery criticized the insufficient disclosure of such ratio and excluding it from the external auditing processes. Because of these practices, Slattery claims that RevPAR gives inflated results without really improving cash flow.

Brown and Dev (1999) also criticized the common ratios used in the hospitality industry, such as average daily rate and RevPAR, since these two ratios do not take into account other revenues generated from the food and beverage department and other departments. Accordingly, Brown and Dev (1999) suggested using the financial measures of total sales, gross operating profit (GOP), and other financial ratios although these ratios are influenced by price level differences among cities and locations.

Regardless of the previous limitations and the weakness of the financial and operational metrics developed in the hospitality industry, the vast majority of researchers and hoteliers still use these ratios to measure the financial and operational performance of hotels. Smith (2008), for instance, is still using the average daily rate, RevPAR, and occupancy metrics as a promoter of the hotel industry performance in the USA.

It is worth noting that measures and ratios displayed in this section can be calculated on a daily, weekly, monthly, or even a yearly basis. However, it is important to measure some
of these measures daily such as occupancy rate since weekly or monthly ratios do not mean that the rate was the same for every night of the week or month. Moreover, results of these indicators can show the directions of performance over time.

Jagels (2007) mentions four methods for interpreting results obtained from the former metrics. Obviously, Jagels asked for comparing results with different criteria, including: the industry averages, external competitive figures, previous periods, and finally, comparing results with predetermined budgetary standards. Because of doing so, hoteliers will be able to evaluate the financial, operational, and economic conditions of their enterprises. However, Adams (2006) declares that setting standard targets of performance is problematic, especially in the hospitality industry, since the environment is changeable and conditions of the market do not stay the same. Moreover, most of the standards are based on the best performance rather than average performance.

The above comparisons imply and refer to the benchmarking concept. Although the hospitality industry has used this concept extensively, this section is going to mention the main idea of this topic briefly. The literature shows different and several classifications of benchmarking. In this regard, Phillips and Appiah-ADU (1998) review different categorises of benchmarking developed and discussed in the literature, such as customer benchmarking, competitor benchmarking, and core benchmarking by Jennings and Westfall (1992); strategic, operational, and management benchmarking by Camp (1992); and internal, competitive, and functional benchmarking by Yasin and Zimmer (1995).

According to the different classifications and types shown above, benchmarking indeed comprises different classifications and types. As a result, such concepts can have different definitions, methods, and reference points. However, Lockwood (2008) refers to benchmarking as a systematic process of evaluating the business’s performance or other key focus points (e.g. process, strategy, and management practice) against different reference points such as same unit over time, other units, regions, competitors, sector, industry, national, and even international. Thus, hoteliers will be able to define where the business is going and determine gaps in performance with reference points identified.

After displaying the common measures and indicators developed and used in the hospitality industry for measuring financial and operational performance, it can be
concluded that the hospitality industry has developed its own specific measures that suit its establishments. Although the literature has introduced several limitations, the RevPAR, occupancy, and ADR ratios represent common and useful measures for performance in the hospitality industry. Thus, it is worth reviewing in the next section the hospitality literature concerning the performance measurement systems that incorporate the financial and operational measures with other non-financial measures in order to attain strategic and operational control as shown in the next section.

4.5 Performance Measurement Systems in the Hospitality Industry

Having shown the huge amount of academic attention and latest trends in the PMS concept in the generic literature, it is worth discussing research and development of this topic in the hospitality literature. In this regard, Haktanir and Harris (2005) claim that few researchers in the hospitality literature have turned their attentions to this topic. Teare (1996) also found that business performance has emerged as a key theme in the hospitality literature along with other themes, such as customers and service improvement, operations and the curriculum, and strategy and development. Specifically, Tear (1996) reviewed papers on the use of the balanced scorecard in hotels; it is surprising that he does not view business performance as an area that emerges from his analysis of publications between 1989 and 1994. Thus, in 1995, attention began to be given to this important area in the hospitality literature.

Since that time, the hospitality literature has discussed this area either directly through finding several papers dealing with this topic mainly or considering this area as a part of a broader study with a direct focuses elsewhere. For example, Brander Brown and McDonnell (1995) discussed the issues of using the balanced scorecard system in the hospitality industry in the UK. After addressing the limitations of the traditional financial measures, they appreciate using non-quantitative performance measures in the USA hotel industry besides the traditional accounting measures such as guest satisfaction and employee attitudes. However, Brander Brown and McDonnell (1995) claim that the hotel industry is still not using the relevant measures, and they questioned the appropriateness and effectiveness of the current measures to the hotel industry’s characteristics. To overcome these concerns and problems, they recommended hoteliers to use the balanced scorecard system developed by Kaplan and Norton (1992). They also recommended
hoteliers change measures of performance among units, and then review and update these measures on a regular basis.

Hepworth (1998) also reviewed the literature on the balanced scorecard published in the hospitality area. He concluded that limited application of the balanced scorecard concept has been undertaken in the hospitality industry in the UK in particular; however, he acknowledged the success of the implementation of this approach across several industries in the USA. On the other hand, Harris and Mongiello (2001) recognised and appreciated moving from narrow and limited profit-centric approaches to balanced performance systems. In order to know what perspectives of performance most managers focus on, they surveyed hotel general managers in chain-affiliated European properties. Findings of their study indicate three key dimensions or perspectives of performance, including human resources, operations, and the customer.

Phillips (1999) suggested a contingency system for the hotel industry in particular to overcome shortcomings in previous models that did not capture the relevant performance aspects required for characteristics of the hospitality industry. Phillips tried to solve the common problem of previous systems by developing a model that focuses not only on individual techniques but also on processes for evaluating and monitoring the business performance of hotels. In his conceptual paper, Phillips explained how this model works to achieve the desired competitive advantage. To put it more simply, the Phillips’s hotel performance model determines how well a hotel measures its inputs and processes, environmental characteristics, strategic orientation, outputs, markets, and outcomes to achieve the competitive advantage.

In another study that tackled the impact of strategic planning on business performance in the hotel industry, Phillips et al (1999) used a new methodology called the neural network analysis approach to investigate the impact of the strategic planning interactive on business performance. Results indicate that the degree of sophistication and thoroughness of the strategic planning processes and practices have a positive impact on the hotel’s performance; however, Phillips et al found that formality and rigidity of the strategic planning process serve to hinder the overall performance of hotels.
In order to explore factors that will improve a hotel’s performance, Gray, Matear, and Matheson (2000) surveyed 1000 service companies in New Zealand in order to understand the relationship between the characteristics of a hotel and its business performance. For the purpose of the study, Gray et al isolated the results of twenty-one hospitality companies that participated in the survey from the larger sample approached in order to compare results between the two groups. The results indicated that there were few performance differences between the two groups. More importantly, those results revealed that top performing firms are those that conduct market-oriented practices and deal with powerful suppliers. Accordingly, Gray et al (2000) recommended that operators in the hospitality industry enhance their market orientation practices to cope with future market turbulence and have closer relationships with customers. They also encourage hoteliers to innovate and develop new service development processes to be more oriented for customers.

Brander Brown and Atkinson (2001) reviewed advantages and disadvantages of the traditional budgeting system, which was based on the comparison between actual financial results and budgets (predetermined results). They found that this approach is inefficient and ineffective and has some limitations, including it required too much time and several revisions, it encouraged managers and users to parochial behaviour, it reinforced barriers between different departments, and hindered flexibility within the organisations. Because of these problems, and based on suggestions and improvements noted in the literature, Brander Brown and Atkinson (2001) proposed a new budgeting system. This system incorporated alternative dynamic techniques and practices such as frequent and regular forecasts with a wide and balanced range of performance indicators. They claim that indicators in this system measure the future performance and the current and short-term results achieved.

Phillips and Louvieris (2005) conducted a case study approach in order to determine and explore performance measures used in a sample of 10 small and medium best practices organisations in the hospitality, tourism, and leisure industries. To do so, a theoretical framework derived from the balanced scorecard approach was used in the study. Their results indicated four key concepts that compromise performance measurement systems in these organisations; however, these four concepts were slightly different from the original four perspectives introduced by Kaplan and Norton. In other words, these four
perspectives were budgetary control, customer relationship management, strategic management, and collaboration on both the inside and the outside of the business, in order to archive innovation and learning. Phillips and Louvieris proposed a template for the balanced scorecard system that can help hoteliers to identify some critical success factors and key performance indicators.

In a recent paper, Cruz (2007) examined business performance measurements used in an international hotel industry. Cruz found that old and traditional techniques such as “budgetary practices” – which are based on the comparison between actual and budget financial results – form a popular tool for measuring performance in the hospitality context. However, findings revealed that operators besides the old budgeting system added new and flexible techniques of performance measurement called the rolling forecasting (RF) technique, which focuses on predicting and forecasting a set of variables such as the occupancy rate, the average room price, the gross operating profit of each unit, the cost of energy and personnel, and so on. The main objective for this new technique is to improve the forward-looking practices at the group level and to encourage the local managers to expect actions needed in order to respond more quickly to future changes in the marketplace. Cruz (2007) claim that such forecasting practices introduced in his paper expand the understanding of the contemporary performance measurement systems.

To explore the current status and practices of PMS in the UK hotel industry, Atkinson and Brander Brown (2001) reviewed the key PMSs developed and the recent developments and trends of measurements in the hotel setting in the UK. Their empirical study, which was based on a hybrid methodology (extensive survey and in-depth interviews with hoteliers), revealed that British hotels are monitoring and measuring their financial performance dimensions (profitability, turnover, and cost control) in significant detail while the non-financial dimensions (such as service quality and customer satisfaction) received little attention. These findings indicate that measurement systems used by hoteliers in the UK are narrow in that they neglect the other dynamic dimensions of performance such as innovation and flexibility.

As a contemporary perspective of PMSs in the hospitality industry, Evans (2005) refers to the BSC framework as a tool for strategic implementation. In this sense, Evans argued
that balanced performance measurement systems have emerged not just to measure the success of any organisation but also to offer a road map and to tell managers how a strategic vision can be realised and achieved "strategic implementation tool". After surveying three- and four-star hotels in the Northeast of England, the findings revealed that hospitality literature has limited details about using the BSC as a strategic implantation tool in the hospitality industry. However, results indicated that hotels in the research sample used a wide variety of measures that represented and covered the four perspectives of the BSC system, which means that measures in this industry are not focusing only on the financial perspective. Thus, results imply that hoteliers are aware about the BSC approach. In addition, results show that larger chains are more oriented to measure their performance using formal methods (i.e. using several measures of performance).

As a more contemporary perspective or function of the BSC system, Phillips (2007) referred to BSC as a strategic control tool that could help in ensuring that strategies adopted are changed according to environmental changes, invalid planning, and new opportunities and threats. Phillips (2007) conducted a longitudinal case study approach over three years in a major hotel company in the UK in order to understand and highlight the theoretical and practical aspects of adopting the BSC as a strategic control tool. He found that using the strategy-focused organisation model as developed by Kaplan and Norton (2001) helps to improve the practices of the successful balanced scorecard system, achieve strategic thinking, determine how to achieve strategic goals, and when to change the strategy. Accordingly, Phillips indicate that using the BSC system alone is not enough to achieve organisational success; consequently, it will lead hoteliers to focus on planning and the results of strategies without giving enough attention to changing strategies. However, Phillips (2007) asked to replicate his study in richer case studies by using multiple methodologies to gain a deeper understanding of the strategic control function of the BSC system in the hotel industry.

Bergin-Seers and Jago (2007) tried to explore the key performance measures and methods used in small motels in Australia. They claimed that understanding measurement activities in successful firms would help to get a better understanding of good performance management. They found that successful motels use a balanced method for measuring performance (i.e., a balance of financial and non-financial measures).
However, results found that key measures depend on the strategy adopted in each motel. In other words, if a motel adopts a development strategy, sales growth and percentages of new and current customers will be the key measures, while if the strategy adopted is a maintenance strategy, the customer satisfaction and average room rate will be the most important measures.

According to their review of PMSs in the hospitality area, Gomes, Yasin, and Lisboa (2007) claim that systems used and adopted in the hospitality industry are not well integrated and incorporated. In this respect, they found that measurement systems are categorised into two platforms; the first platform implies the measure-specific perspective, which uses individual performance measures to evaluate the operational performance such as operational efficiency and employees' productivity. On the other hand, the second platform refers to the organisational-wide or system-wide management perspective, which measures the critical organisational performance dimensions such as competitive positions of the organisation in the marketplace. They concluded that the former two platforms are measuring and dealing with two different levels of performance separately (i.e. operational and organizational performance).

To overcome this limitation of the current approaches, Gomes et al (2007) developed a performance system called the service operational effectiveness (SOE), which integrates and incorporates the two levels or platforms of performance systems into a single model. To do so, the suggested system measures the key dimensions of performance in the hospitality industry including services availability, quality, and efficiency. In their paper, Gomes et al offered a road map for effective implications and adaptation of the SOE system in the hospitality industry.

However, this system is still at the theoretical and development stage. In addition, authors of this system did not prove the contribution power of the three dimensions suggested in the model to measure the performance in the hospitality industry. Moreover, the proposed system did not offer or introduce measures that can be used to measure the three dimensions.

Israeli, Barkan, and Fleishman (2006) argued that although the relevant literature referred to the balanced scorecard system as the most popular system for measuring performance,
the performance measurement concept is multi-faceted, and there is still no agreement for adopting a single performance measurement system. In an effort to dispel this confusion, they conducted a survey to identify the most important indicators for measuring a hotel’s performance from the hotel managers’ perspective by exploring their perception of a list of financial and non-financial measures. The main finding of their study confirmed their assumption and revealed that hotel managers do not have a clear understanding of the most important and suitable indicators in this industry. In other words, ratings for hotel managers’ perceptions indicate that all performance measures are highly important and highly unimportant at the same time. Thus, hotel managers show a lack of obvious direction and philosophy towards performance systems.

Having displayed some parts of the performance measurement system discussed in the hospitality literature, it became clear that the hospitality industry had made good progress and improvements in terms of using and adopting the integrated (balanced) performance measurement systems, such as the BSC system, as a tool for measuring performance. In other words, several studies and cases displayed in this section have discussed, utilized, and demonstrated the balanced measurement systems as a valuable measurement tool (e.g. Brander Brown and McDonnell, 1995; Hepworth, 1998; Harris and Mongiello, 2001; Phillips and Louvieris, 2005; Evans, 2005; Phillips, 2007).

However, Cruz (2007) claimed that using and implementing the new systems and techniques developed in the generic literature instead of the traditional tools has not achieved completely yet in the hotel industry as can be seen in his comment: “it appears that a widespread use of these new PM tools has not occurred in the hospitality industry” (Cruz, 2007. p. 576). In this regard, some authors claim that using the traditional financial and budgeting measures of performance, which focus on the historical activities and short-term perspectives, are still dominating the business performance practices in the hotel industry setting (e.g. Cruz, 2007; Brander Brown and Atkinson, 2001; Atkinson and Brander Brown, 2001).

Discussions in this section show two main streams of research concerning PMSs in the hospitality industry; on one hand, the first stream of research focuses on introducing new techniques and models of measuring performance such as Cruz (2007), who emphasized and recommended using the rolling forecasting technique (RF); Gomes et al (2007), who
developed a PMS called the service operational effectiveness (SOE), which integrates two levels or platforms of performance into a single model; Phillips (1999), who developed a contingency system for the hotel industry specifically to solve problems in previous models that didn’t highlight the aspects of performance in the hospitality industry. On the other hand, the second stream of research tries to discuss the use and implementation of the existing balanced performance models (e.g. the BSC system) developed in the generic PMS’s literature (e.g. Hepworth, 1998; Phillips and Louvieris, 2005; Evans, 2005; Phillips, 2007). Within this stream of research, few researchers tried to follow and test the latest trends and developments that occurred in the generic PMS literature, such as, Phillips (2007), who tried to use the BSC as a strategic control tool based on the Kaplan and Norton’s (2001) model.

To conclude, although the hospitality industry showed some progress in terms of using the balanced (integrated) systems, discussing and addressing the latest trends of the BSC system as shown by Phillips (2007) and Evans (2005), moreover, though the hospitality literature highlights the need to revise measures and systems of performance to offer dynamic and flexible systems as suggested earlier by Brander Brown and McDonnell (1995) and Brander Brown and Atkinson (2001), it seems that the hospitality industry is still lagging behind the generic literature in terms of fully implementing the latest trends that have occurred in the PMS arena: such as developing more dynamic performance measurement systems. Thus, the findings of this section indicate that the hospitality literature has limited details and implementations for the latest trends developed in the generic PMS literature and more works are needed.

4.6 Findings of the Preliminary Study (Part One)
The preliminary study was undertaken at an early stage of the current study in order to achieve two objectives; first, to explore hoteliers’ perspective on and understanding of the performance and profitability concept and what measures are used for profitability in the hotel industry; second, to test the adequacy and suitability of the proposed research framework to the hotel industry. According to these two different objectives, the discussion and presentation of the findings from this preliminary study are divided into two parts. Part one deals with the first objective, which is introduced and discussed in this chapter, while part two, which deals with the second objective after introducing details
and procedures for doing this preliminary study (e.g. the sample, timeline, data analysis) is introduced and discussed in the methodology chapter (Chapter 6).

For the first part of the preliminary study, the researcher asked interviewees about their level of understanding and definition of the profitability concept. The researcher also asked interviewees during the interview about what measures they perceive are used for measuring profitability in the hotel industry and what elements constitute the profitability concept in this industry as shown on Appendix 1.

Thus, interviewees were invited to answer the following questions:

How would you define the profitability of a hotel from your point of view? How would you measure it? and what are the resources or activities which contribute to profitability in your hotel?

As shown in the data analysis and discussion introduced in Appendix 3, interviewees appreciated using the profitability measures and results of a hotel as an important indicator of the overall performance. According to interviewees, profitability is one of the most important factors that help hotels compete in the market. In this regard also, profitability gives a good indication about the professionalism and effectiveness of the management and staff of a hotel. Moreover, high profitability will lead to improvement in other aspects of performance by expanding or adding new profit centres, investing more in safety and refurbishment, research and development, and training staff.

In terms of definition of profitability, all interviewees declared that profitability means revenues or income remained after covering all costs and expenses of running a hotel. In other words, hoteliers prefer to define profitability as to what extent a hotel is generating revenues after covering all costs and expenses. However, only one interviewee expanded this definition and understanding of profitability. Specifically, the third interviewee defined profitability as the ability of a hotel to generate revenues from the capital used and invested in the hotel while other participants of the preliminary did not refer to the capital employed in their definitions of profitability.
In terms of measures used for determining profitability, all respondents mentioned that they use gross operating profit (GOP) as a key and popular ratio for measuring the profitability of hotels. For resources of calculating measures of profitability, interviewees noted that they use the common financial statements (e.g. profit and loss account and balance sheet) for calculating profitability measures. Thus, such results imply that hoteliers use similar resources for building measures. Finally, results indicated that the hoteliers interviewed use several outlets for generating profits and revenues; however, the room and food and beverage departments are the most important for achieving profits in hotels. (For more details and discussions of the preliminary study, please go to Appendix 3.)

To conclude, part one of the preliminary study reveals the following results:

1. The definition of profitability is the same amongst hoteliers, which is based on the ability of a hotel to generate revenues or income after covering all costs and expenses.

2. Hoteliers' definition of a hotel's profitability is simple since it relies mainly on the hotel's ability to generate net income from sales rather than evaluating the hotel's ability to exploit and utilise capital or assets or even equity invested to generate revenues.

3. Although it represents a simple measure of profitability, hoteliers use GOP as a common ratio for measuring profitability in the hotel industry.

4. Achieving profitability refers to good performance of a hotel and brings several benefits for hotels, such as more investment in the improvement of service features, staff, R&D, and so on.

5. Rooms and food and beverage revenues account for the majority of a hotel's revenues.

According to the above results, hoteliers have a clear and consistent definition of profitability as previously introduced in the literature. In other words, hoteliers refer to profitability as the ability of an organisation to generate profit and sales as introduced by
Mclaney (2000). Although one interviewee expanded the definition of profitability, hoteliers have a simple understanding of the profitability concept. In other words, hoteliers focused on the amount of revenues generated to evaluate hotel profitability without linking this amount of revenues to other factors or elements such as capital used or assets as introduced in the literature by authors such as Thompson (2001). Accordingly, measures used in the industry are simple. Moreover, hoteliers use profitability measures and results as a key indicator of the overall hotel industry. Clearly, this result is consistent with the results of the literature review, which revealed that financial measures dominate measures of business performance in the hotel industry (e.g. Cruz, 2007; Brander Brown and Atkinson, 2001; Atkinson and Brander Brown, 2001).

Although most of interviewees mentioned that the GOP ratio forms a popular measure of profitability, the present study is going to use the ROCE ratio as a measurement of profitability. This is because the GOP ratio does not offer a broad definition and measurement of profitability, whereas the ROCE ratio measures profitability not only as a profit margin generated from sales but also in relation to the amount of capital used and invested. This ratio (ROCE) was used in a wide range of studies in the generic and hospitality literature. In this regard, Adams (2006) claimed that this ratio is one of the most widely used ratios for measuring profitability in the hotel industry. Moreover, this study is going to use the RevPAR ratio since it forms a key measure of profitability in the financial and operational measures in the hospitality industry as discussed before in this chapter. To summarize, this study will use two measures of profitability (ROCE and RevPAR) after explaining the meaning and definitions of these measures to ensure the correct understanding of these measures.

4.7 Conclusions
This chapter discussed the subject of performance measurement systems in the generic literature and in the hospitality industry. Discussions in this chapter showed that finding a single definition of PMS is not an easy task since this concept has been discussed widely in different areas and disciplines. Accordingly, a PMS plays several roles and functions in any organisation. The literature on this topic shows two main categorises or methods for measuring performance; the first one focuses on the financial perspective of performance only and introduces several measures or ratios (e.g. profitability ratios, liquidity ratios, etc.), while the second method focuses on measuring the balanced performance in order
to overcome the limitations of using the financial perspective only. In this respect, the literature develops several and different systems and frameworks such as the Balanced Scorecard system, the SMART system, the results and determinants model, the Performance Prism, and the performance measurement matrix, etc.

Although the literature developed useful frameworks and systems for measuring the balanced performance in the last 20 years, unfortunately, such systems showed some weaknesses and limitations in terms of offering justifications for factors or measures used, and also insufficient explanations for the linkages between dimensions or perspectives of performance. Accordingly, researchers have moved their attention from building new systems to explaining the processes and steps for designing, implementing, and using performance measurement systems. In this respect, the literature shows some suggestions and contributions in terms of how to implement PMSs as introduced by Wisner and Fawcett (1991); Keegan et al (1989); and Franco-Santos et al (2007).

Recently, the literature indicates that the design and implementation of PMSs should include dynamic processes in order to overcome the constantly changing internal and external environments (Bourne et al., 2000; Bititci and Turner, 2000; Anderson and McAdam, 2004; Kennerley and Neely, 2005). In other words, the designing of PMSs should be a more dynamic, flexible and should include the continuous reviewing and updating process for measures to assure successful implementations of performance measurement systems.

As introduced by Neely (2005), the PMS literature has been going through several developments, changes, and generations; the first generation of PMS literature combines the non-financial measure with financial measures such as the Balanced Scorecard System. Within this generation, scholars were interested in finding and developing suitable measures and dimensions of performance. On the other hand, the second generation of PMS tried to overcome the limitations of the first by using the strategy and success maps to put these systems in practice. In other words, researchers within this generation were interested in improving the causal relationships between dimensions and perspectives of performance. Finally, the third generation of PMS indicates that systems should reflect the dynamic realities of organisations and markets. More recently and as a very new development and suggestion in the literature, Marchand and Raymond (2008)
asked to apply, utilise and expand the information system’s (IS) theories and models in the PMS concept.

Although the generic literature of the integrated measurement system shows huge developments and changes, the hospitality literature revealed that financial and operational measures still dominate practices of PMSs. However, the hospitality industry has shown a good number of cases that implemented the integrated performance systems such as the BSC system (e.g. Hepworth, 1998; Phillips and Louvieris, 2005; Evans, 2005; Phillips, 2007). In addition, some papers in the hospitality literature discussed the newest and latest trends introduced in the generic PMS literature. For example, Phillips (2007) used and referred to the BSC system as a strategic and dynamic tool and tested a model of it in the hospitality industry. Moreover, other authors have asked for dynamic measures of performance by revising and updating measures in regular bases according to changes as suggested by Brander Brown and Atkinson (1995) and Brander Brown and Atkinson (2001). Moreover, Cruz (2007) asked hoteliers to use the new and contemporary trend of the rolling forecasts technique to face the competitive nature of the hotel industry.

In other words, the hospitality industry showed significant changes and movements towards using the balanced (integrated) systems and also discussed the contemporary issues and developments in this area as introduced by Phillips (2007). However, the hospitality industry is still lagging behind the generic literature in terms of implementing and adopting the latest trends occurring in the generic PMS literature. Thus, findings of this chapter revealed that the hospitality literature has not yet discussed and implemented the latest trends in the generic PMS’s literature and there is more work required to develop more dynamic systems.

According to the objective of the current study, the present research will adopt only the financial performance measures to quantify and evaluate budget hotel’s abilities to generate profits. To put it more simply, this study will use the financial indicators in order to assess the financial performance of hotels, which represents the ultimate objective for any organization. In this regard, Otley (2004) states that financial performance and achieving profits form the major objective of a business organisation. To do so, the profitability ratios are considered to be the most suitable measures.
Discussion in this chapter showed also that profitability can be measured by the generic profitability ratios and some other specific measures developed in the hospitality industry. Accordingly, the present study is going to use two measures; one from the generic literature and another one from the hospitality industry: (ROCE and RevPAR). Doing so will help managers to be better able to determine the financial performance of their portfolio of hotels.
Chapter 5

The Research Model
Chapter 5

The Research Model

5.1 Introduction
The previous discussion (chapters 2 and 3) provides a broad theoretical overview of service quality and business performance concepts, identifying a lack of consensus in opinions, definitions and measurements. Therefore, the generation of further empirical evidence and support serves as a rational justification for this study, with the development of a conceptual framework to explain the relationship between service quality and profitability in the UK budget hotel sector. Additionally, this review of empirical studies will help to discover gaps in the literature, to generate the research questions/problems which form the motivation for the study. Therefore, section two of this chapter identifies the research question that has emerged and been extracted from previous studies. Section three develops the research model used to explain the relationship between variables. Section four provides definitions for variables and constructs appearing in the research model. Section five generates and discusses research hypotheses to be examined in later chapters. Finally, section six draws conclusions.

5.2 The Research Question
It is argued in the literature that the pursuit of quality is incompatible with supernormal profits, through imposing a high level of costs resulting from the demand for different and expensive sets of actions (Phillips, Change and Buzzell, 1983). In contrast, evidence exists which suggests that this apparent incompatibility of quality and costs is an unfounded assumption (Wheelwright, 1981; Smith, 1980). In other words, some authors support the notion that quality has emerged as a fundamental competitive strategy for organizational success (Zeithaml and Bitner, 2003). Quality is considered one of the key methods to attain a differential market position and achieve higher revenues and profits (Hall, 1980; Porter, 1980; Parasuraman et al., 1988; Harrington and Akehurst, 1996).
Previous empirical studies have investigated the relationship between quality improvements and profitability by adopting both direct and indirect perspectives on the assumed relationship. Some of these studies indicated that quality has a positive relationship with business performance, which could be measured by profitability ratios such as ROI or ROE (Schoeffler et al., 1974; Phillips et al., 1983; Nelson, Rust, Zahorik, Rose, Batalden and Siemanski, 1992; Garuana and Pit, 1997; Hendricks and Singhal, 1997; Zhang, 2000; Kimes, 2001; Raju and Lonial, 2002; Duncan and Elliott, 2002; Hasan and Kerr, 2003). Conversely, some studies have indicated that the nature of the relationship between the two is negative, or weak, i.e. increasing quality of service may decrease the profitability of firms in the short term (Harrington and Akehurst, 1996; Sterman, Repenning and Kofman, 1997; Adam, 1994; Claver, Tari and Pereira, 2006). Table 5.1, shown on the next few pages, summarises some of the empirical studies published in the related fields.
### Table 5.1 Summary of Empirical Studies Investigate the Relationship between Quality and Business Performance

<table>
<thead>
<tr>
<th>Study</th>
<th>Country</th>
<th>Sample</th>
<th>Independent Variable(s)</th>
<th>Dependent Variable(s)</th>
<th>Main Finding</th>
<th>Statistical Test</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Schoeffler et al (1974)</td>
<td>USA</td>
<td>57 corporations which include 620 diverse businesses.</td>
<td>37 variables; product quality, market share, R&amp;D expenses, marketing expenditures, investment intensive, etc.</td>
<td>Profit performance: (ROI).</td>
<td>(+) association between product quality and profits.</td>
<td>Simple regression</td>
<td>Direct relationship.</td>
</tr>
<tr>
<td>Study</td>
<td>Country</td>
<td>Sample</td>
<td>Independent Variable(s)</td>
<td>Dependent Variable(s)</td>
<td>Main Finding</td>
<td>Statistical Test</td>
<td>Perspective</td>
</tr>
<tr>
<td>------------------------------</td>
<td>---------</td>
<td>--------------------------</td>
<td>--------------------------</td>
<td>-----------------------</td>
<td>-------------------------------------------</td>
<td>---------------------------------------</td>
<td>--------------</td>
</tr>
<tr>
<td>Forker (1996)</td>
<td>USA</td>
<td>Furniture Industry (65 firms)</td>
<td>Product Quality</td>
<td>Business Performance (ROI; ROA, Sales growth; market share).</td>
<td>(+) positive association especially for quality design and product improvement dimensions.</td>
<td>Stepwise Regression</td>
<td>Direct</td>
</tr>
<tr>
<td>Hendricks and Singhal (1997)</td>
<td></td>
<td>400 firms won awards for TQM implementation</td>
<td>TQM</td>
<td>Operating Performance;</td>
<td>(+) association.</td>
<td>Descriptive analysis for longitudinal data (10 years).</td>
<td>Direct</td>
</tr>
</tbody>
</table>

162
### Chapter 5
#### The Research Model

<table>
<thead>
<tr>
<th>Study</th>
<th>Country</th>
<th>Sample</th>
<th>Independent Variable(s)</th>
<th>Dependent Variable(s)</th>
<th>Main Finding</th>
<th>Statistical Test</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chapman, Murray and Mellor (1997)</td>
<td>Australia</td>
<td>75 companies from different industries e.g. mining, agriculture, fishing, etc.</td>
<td>Quality management</td>
<td>Financial performance</td>
<td>(+) moderate strength of the association</td>
<td>Correlation</td>
<td>Direct</td>
</tr>
<tr>
<td>Loveman (1998)</td>
<td>USA</td>
<td>450 branches for a retail Bank</td>
<td>Internal service quality, staff loyalty and satisfaction</td>
<td>Profitability</td>
<td>(+) association</td>
<td>Simple regression analysis for panel data</td>
<td>Indirect perspective</td>
</tr>
<tr>
<td>Chang and Chen (1998)</td>
<td>Korea</td>
<td>Retail stock brokerage firms</td>
<td>Market orientation and service quality</td>
<td>Profitability</td>
<td>(+) association between quality and profitability. Quality positively mediate market orientation and profitability</td>
<td>Multiple regression</td>
<td>Direct</td>
</tr>
<tr>
<td>Anderson and Sohal (1999)</td>
<td>Australia</td>
<td>62 small business</td>
<td>Quality management practices</td>
<td>Organizational performance</td>
<td>(+) positive impact</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Direct</td>
</tr>
</tbody>
</table>
### Chapter 5

**The Research Model**

<table>
<thead>
<tr>
<th>Study</th>
<th>Country</th>
<th>Sample</th>
<th>Independent Variable(s)</th>
<th>Dependent Variable(s)</th>
<th>Main Finding</th>
<th>Statistical Test</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Terziovski and Samson (1999)</td>
<td>Australia and New Zealand</td>
<td>Manufacturing companies</td>
<td>Quality management practices</td>
<td>Organizational performance</td>
<td>Significant differences of impact among industries and different size companies</td>
<td>MANOVA and MANCOVA to test group differences</td>
<td>Direct</td>
</tr>
<tr>
<td>Kunst and Lemmink (2000)</td>
<td>UK, Spain and Netherlands</td>
<td>Hospitals sector</td>
<td>Quality management</td>
<td>Business performance</td>
<td>Limited positive impact on business performance</td>
<td>Regression analysis</td>
<td>Direct</td>
</tr>
<tr>
<td>Kimes (2001)</td>
<td>USA and Canada.</td>
<td>1135 Holiday Inn franchise properties</td>
<td>Product quality.</td>
<td>Profitability; RevPAR.</td>
<td>(+) association.</td>
<td>Variance analysis (6 month interval for 3 years).</td>
<td>Direct</td>
</tr>
<tr>
<td>Agus and Sagir (2001)</td>
<td>Malaysia</td>
<td>Manufacturing companies</td>
<td>Total quality management</td>
<td>Finical performance</td>
<td>(+) positive association</td>
<td>Structural equation modelling (SEM)</td>
<td>Indirect通过 competitive advantage variable</td>
</tr>
<tr>
<td>Raju and Lonial (2002)</td>
<td>USA</td>
<td>175 hospitals.</td>
<td>Service quality and service marketing.</td>
<td>Financial performance; NP, CF, ROI.</td>
<td>(+) indirect impact of service quality on FP via SM.</td>
<td>Structural equation modelling.</td>
<td>Indirect perspective.</td>
</tr>
<tr>
<td>Study</td>
<td>Country</td>
<td>Sample</td>
<td>Independent Variable(s)</td>
<td>Dependent Variable(s)</td>
<td>Main Finding</td>
<td>Statistical Test</td>
<td>Perspective</td>
</tr>
<tr>
<td>-----------------------</td>
<td>------------</td>
<td>---------------------------------</td>
<td>------------------------------------------------</td>
<td>---------------------------------------------</td>
<td>--------------------------------------</td>
<td>------------------------------------------</td>
<td>-------------</td>
</tr>
<tr>
<td>Duncan and Elliott</td>
<td>Australia</td>
<td>14 financial institutions.</td>
<td>Service quality.</td>
<td>Financial performance; (ROA)</td>
<td>(+) association.</td>
<td>Structural equation modelling.</td>
<td>Direct</td>
</tr>
<tr>
<td>Cook and Verma</td>
<td>Honk Kong</td>
<td>28 bank branches</td>
<td>Quality management system and service quality</td>
<td>Performance</td>
<td>(+) positive impact of service quality on performance</td>
<td>Stepwise regression</td>
<td>Direct</td>
</tr>
<tr>
<td>(2002)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hasan and Kerr</td>
<td>Australia</td>
<td>109 service organizations.</td>
<td>TQM</td>
<td>Organizational performance; financial and non financial performance.</td>
<td>(+) association.</td>
<td>Multiple regressions.</td>
<td>Direct</td>
</tr>
<tr>
<td>Kaynak (2003)</td>
<td>USA</td>
<td>382 firms from different industries</td>
<td>Total quality management practices</td>
<td>Business performance</td>
<td>(+) impact</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Direct</td>
</tr>
<tr>
<td>Weech-Maldonado et al</td>
<td>USA</td>
<td>Nursing homes companies</td>
<td>Quality of care (outcomes quality, process quality, registered nursing staff)</td>
<td>Financial performance</td>
<td>(+) impact through lowering costs of care and increasing revenues</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Indirect</td>
</tr>
<tr>
<td>(2003)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>perspective.</td>
</tr>
</tbody>
</table>

Chapter 5
The Research Model
<table>
<thead>
<tr>
<th>Study</th>
<th>Country</th>
<th>Sample</th>
<th>Independent Variable(s)</th>
<th>Dependent Variable(s)</th>
<th>Main Finding</th>
<th>Statistical Test</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Daskalopoulou and Petr (2005)</td>
<td>Greece</td>
<td>Electrical goods stores</td>
<td>Functional dimension of quality</td>
<td>Business performance (sales)</td>
<td>(+) positive association</td>
<td>Structural equation modelling (SEM)</td>
<td>Direct</td>
</tr>
<tr>
<td>Lee and Hwan (2005)</td>
<td>Taiwan</td>
<td>Bank industry</td>
<td>Service Quality</td>
<td>Profitability</td>
<td>(+) impact Via customer satisfaction</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Indirect through customer satisfaction</td>
</tr>
<tr>
<td>Gillean, Shaha, Sampanes and Mullins (2006)</td>
<td>USA</td>
<td>18 Hospitals</td>
<td>Quality</td>
<td>Profitability</td>
<td>(+) association for some indicators of quality including; timely and appropriate intervention and timely and complete documentation</td>
<td>Correlation</td>
<td>Direct perspective</td>
</tr>
<tr>
<td>Claver et al (2006)</td>
<td>Spain</td>
<td>11 Three- and four-star hotels</td>
<td>Quality system</td>
<td>Business performance: sales, sales growth, market share, market share growth and financial performance</td>
<td>(+) low positive impact on financial performance but stronger impact on the other indicators of performance</td>
<td>Qualitative (Interviews with general managers)</td>
<td>Direct</td>
</tr>
<tr>
<td>Study</td>
<td>Country</td>
<td>Sample</td>
<td>Independent Variable(s)</td>
<td>Dependent Variable(s)</td>
<td>Main Finding</td>
<td>Statistical Test</td>
<td>Perspective</td>
</tr>
<tr>
<td>-----------------------</td>
<td>----------</td>
<td>---------------------</td>
<td>----------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------</td>
<td>----------------------------------</td>
<td>-----------------------------</td>
</tr>
<tr>
<td>Yoo and Park (2007)</td>
<td>Korea</td>
<td>129 Hotels</td>
<td>Service quality</td>
<td>Financial performance; room occupancy and repeated reservation as a surrogate of hotel's financial performance.</td>
<td>(+) positive impact through customer satisfaction</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Indirect via customer satisfaction</td>
</tr>
<tr>
<td>Macinati (2008)</td>
<td>Italy</td>
<td>148 Hospitals</td>
<td>Quality management system</td>
<td>Organizational performance which includes; financial, operational and subjective and objective outcomes (e.g. stakeholder and patient satisfaction)</td>
<td>Weak significant relationship between quality management and financial performance</td>
<td>Canonical correlation</td>
<td>Direct</td>
</tr>
<tr>
<td>Yee, Yeung and Cheng (2008)</td>
<td>Hong Kong</td>
<td>223 small service shops</td>
<td>employee satisfaction, service quality and customer satisfaction</td>
<td>Firm's profitability</td>
<td>(+) positive impact of service quality on profitability through customer satisfaction</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Indirect</td>
</tr>
</tbody>
</table>
### Chapter 5
*The Research Model*

<table>
<thead>
<tr>
<th>Study</th>
<th>Country</th>
<th>Sample</th>
<th>Independent Variable(s)</th>
<th>Dependent Variable(s)</th>
<th>Main Finding</th>
<th>Statistical Test</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Marinova, Ye and Singh (2008)</td>
<td>USA</td>
<td>30 Non-profit hospitals</td>
<td>Quality and productivity orientation</td>
<td>Business performance; unit revenues, customer satisfaction and unit efficiency</td>
<td>Negative and insignificant direct impact on unit revenue and customer satisfaction but positive and significant impact found after including the front line impact</td>
<td>Structural Equation Modelling (SEM)</td>
<td>Indirect</td>
</tr>
</tbody>
</table>
The majority of the empirical studies considered in Table 5.1 reveal and confirm a positive relationship between quality improvement and business performance. However, most of these studies adopted the direct perspective for testing the service quality-profitability relationship. Moreover, most of these studies used the quality construct rather than service quality construct. In addition, the majority of the previous studies that discussed this topic by using the indirect perspective were carried out in different industries and settings (e.g., finance, healthcare and retail, etc). All of these characteristics of the literature in this area lead to complicate the view regarding the impact of service quality on profitability in the budget hotels setting. As a result; it can be claimed that there is a lack of complete consensus about this topic in the hospitality industry. For example, Zeithaml (2000) reviews the literature concerning the relationship between service quality and profitability in order to verify the correspondence and finds that there is still a debate in the literature in terms of the direction and nature of the relationship between service quality and profitability. In this regard also, Babakus, Bienstock and Scotter (2004) found in their literature review that despite nearly two decades of research on quality improvements efforts, the relationships between customer perceptions of quality and financial outcomes are still debated and not clear.

Accordingly, this research aims to answer the following questions:

- What is the relationship between service quality and profitability in the UK budget hotel sector?
- Is it a positive or negative relationship?
- Is it a direct or indirect relationship?
- If indirect, what variables mediate and moderate the relationships between the two variables?

5.3 The Research Model

Figure 5.1 displays a graphical representation of the conceptual model which guides this research.
As shown above, the research model suggests that service quality has a positive relationship with profitability through some mediating (intervening) variables. In other words, the research model links service quality and profitability by including some mediating and moderating variables involved in this relationship.

Firstly, revenue expansion which resulted from customers' perceptions of service quality leads to more sales and shares in the market. In other words, service quality manifests as an improvement of overall customer satisfaction and perception. The second outcome implies that better service quality allows the company to charge higher prices than its competitors for similar services and benefits. Finally, the last outcome of service quality attempts to increase productivity by reducing unnecessary efforts and errors in time, labour and material (Rust et al., 1995, 2002, 2004; Raju and Lonial, 2002).

Thus, quality of service represents a critical factor for business profitability, due to its marketing and operational implications and outcomes. Variables shown in the conceptual framework, such as customer satisfaction and retention, market share, premium price and productivity, are interrelated and present the outcomes of service quality improvements. To sum up, the relationship between service quality and profitability is considered to be a complex and multidirectional relationship.
5.4 Definitions of Variables

5.4.1 Service Quality
Quality of service defined as “customers' perceptions of how well a service meets or exceeds their expectations” (Dibb, Simkin, Pride and Ferrel, 2006, p. 386). Such definition implies an attitude or overall judgement resulting from comparison between customers’ expectations and their perceptions of actual service offered by a company (Parasuraman et al., 1988; Robinson, 1999).

5.4.2 Customer Satisfaction
Customer satisfaction implies an emotional and affective construct that occurs at the transaction level for customers and users of services and products. Hence, customer satisfaction depends on customers’ possession and/or use of a specific service or product (Rust and Oliver, 1994). In this sense, the literature refers to customer satisfaction as the customer's judgement of product or service experiences. Simply, when any product or service meets or matches the customer’s needs and expectations, satisfaction will be claimed by customers. On the other hand, if customers did not get their expectations and needs, emotional dissatisfaction will emerge (Zeithaml and Bitner, 2003; Olorunniwo, Hsu and Udo, 2006).

5.4.3 Customer Retention
The concept of customer retention implies the behavioural dimension of loyalty (Ranaweera, 2003). In other words, refers to the likelihood that customers will stay with a specific supplier without going anywhere else. Therefore, customer retention can be measured according to the behavioural based criteria (Aspinall, Nancarrow and Stone, 2001). Ranaweera (2003) refers to this construct as meaning to what extent the customer is going to leave a specific service provider at different times, or to recommend it for others. Other researchers indicate that customer retention implies the absolute number of customers and their relative purchases, percentage share of spending and purchasing (volume or value) for a specific period, compared to the customer defection rate (Ahmad and Buttle, 2001). In addition, Harrison and Ansell (2002) indicate that some events or dimensions of customer retention can help in explaining this concept, such as the ability of customers to switch to other competitors versus the ability to purchase additional products from the same company.
5.4.4 Premium Price

In general, the price concept is defined as "the amount of money charged for a good[s] or service" (Kotler et al., 2003, p. 445). Clearly, such a definition refers to the objective price, i.e. the actual price of a product. Price studies in literature classified the price construct into two groups: objective price, as mentioned in the former definition, and perceived price which means the fairness and awareness of price as encoded by the consumer (Zeithaml, 1988). Perceived price can be measured by asking customers about their perception of the overall price paid for specific product or service, i.e. the extent to which they considered the price very low or very high (Oh, 1999). On the other hand, premium price implies the extent to which the price paid by customers is considered higher than average prices in the market. As a result, a premium price offers an economic profit for organization during a specific transaction (Rao and Bergen, 1992).

5.4.5 Business Performance Indicators

5.4.5.1 Market Share

This concept can be defined as "the proportion of actual sales volume or value within [a] defined market" (McDonald, 2002, p. 415). Therefore, Buzzell and Gale (1987) introduce three approaches for defining market share of any organization: (1) absolute market share, (2) market-share rank (3) relative market share.

The first approach makes comparison between sales for a specific company and total sales of its served market, i.e. sales of all companies that offer, head-to-head, their products or services. The second approach ranks companies according to their absolute market share in a specific industry (e.g. if a company has a market-share rank of number one, that means this company is a leader with seventy percent of the market). The third approach compares the absolute share for a specific company to its single largest competitor, or to the three largest competitors in its market.

5.4.5.2 Profitability

Profitability can be measured by using the ratio analysis technique. The profitability ratio group includes several metrics as shown below. (Ross et al., 2002; Gallinger and Poe, 1995; Jagels and Coltman, 2004; Atrill, 2003; Stutts, 2001):

- Gross Profit Margin (GPM):
  \[ \text{Gross profit / Sales} \times 100\% \]
The Research Model

- **Net Profit Margin (NPM):**
  Net income / Sales * 100%

- **Return on Capital Employed (ROCE):**
  Net income before interest and tax / Capital employed * 100%

- **Return on equity (ROE):**
  Net income after interest and tax / Common equity * 100%

5.4.5.3 Productivity

Disagreement on defining productivity leads to difficulties in creating consensus for its measurement in the service setting. In other words, the literature shows diverse definitions, concepts and measurements for productivity in the service context and in general. Each one of these definitions and measurements has special perspective and value, and reflects a different aspect of productivity (Sigala et al., 2005). The literature concerning measurement of productivity in a service setting includes two groups or categories of classifications (Gronroos, 2000; Gronroos and Ojasalo, 2004; Sasse and Harwood-Richardson, 1996; Jones and Lockwood, 1989; Ojasalo, 1999; Ball, Johnson and Slattery, 1986; Brown and Dev, 1999; Jones, Howcroft and Drake, 1997). The first group of classifications includes three kinds of measurements:

1. Financial measurements focus on financial factors related to both inputs and outputs, such as revenues, sales, costs of labour, operating costs, resources, value added and profits.
2. Physical measurements focus on physical aspects related to both inputs and outputs, such as number of customers served, number of rooms cleaned, number of covers, number of working hours, number of rooms occupied, etc.
3. Combined measurements use both of financial and non-financial (physical) aspects, such as revenues versus number of employees or customers, etc.

On the other hand, the second group of classifications is comprised of two kinds of measurements for evaluating service productivity. The first measurement within this group measures total productivity; in other words, it takes into account all factors involved in the production process and operations. As a result, this category calculates revenues as well as...
costs for all elements and factors in the organization, such as labour, material, capital, energy, etc.

The second measurement in this group is partial productivity, which focuses only on one aspect or factor of the inputs, such as labour productivity, material productivity, etc. To that end, partial productivity is interested only in some elements, related to staff or employees for example. Therefore, this type of productivity measurement compares between all outputs and one element of input such as labour costs (payroll), number of employees, number of working hours, and so on. Thus, the partial productivity measurement approach focuses on a specific element among the inputs.

As mentioned above, different measures or metrics for measuring productivity have been developed in the service industry. To put it another way, too many approaches, levels and equations for measuring service productivity have been developed, with different perspectives and scopes of measurement. Therefore, no final solution has been developed for measuring service productivity that can be considered more valid than other equations (Gronroos, 2000). In addition, different combinations of numbers and types of inputs and outputs lead to a huge number of productivity metrics which in turn complicates the situation (Sigala et al., 2005). The literature shows huge ratios (inputs and outputs) for measuring productivity in hotels. For example, Sigala et al (2005, p: 71) review inputs and outputs used and developed in the literature for measuring productivity.

Developing a measurement of productivity requires a series of actions and decisions: firstly, defining the level and unit of analysis (partial versus total productivity approach), secondly, identifying appropriate elements for inputs and outputs (financial, physical and combined measures), and finally, using the appropriate methods for measuring the relationship between outputs and inputs (ratio analysis, multi-factor ratios and regression analysis). Thus, the previous discussion considered fundamental and important procedures for selecting and adopting a productivity measurement.

5.4.6 Managing Demand
The literature indicates and provides special techniques for managing demand, such as demand management strategies and intelligence enhancement strategies, e.g. using a reservation system, analyzing the historical trends of demand and pre-marking the calendar
for special events (Shemwell and Cronin, 1994). The aim of these activities is to manage the demand in order to match and fit the capacity of the company, and to modify capacity to fit demand in different situations, i.e. a company should adopt different procedures to manage the fluctuations of demand when demand exceeds capacity or when capacity exceeds demand. Thus, there are two solutions for managing the fluctuations of demand: controlling the level of demand, or adjusting the level of capacity to meet demand variations (Lovelock and Write, 2002).

The first solution aims to managing demand to match capacity by using a set of techniques focused on modifying four dimensions of the services marketing-mix: price, product elements, place and time of delivery, and education. In other words, these four dimensions represent the techniques used for managing demand under different conditions in the service sector.

The second solution attempts to adjust the level of capacity to match demand by using different sets of techniques known as a chase demand strategy. Unlike the approach of managing demand, this method aims to stretch and align capacity to match the current demand as much as possible, rather than trying to shift the current demand to match the inflexible capacity. To put it more simply, during periods of peak demand the company tries to expand capacity, while in periods of slack demand the company tries to minimize its capacity (Zeithaml and Bitner, 2003). Obviously, modifying capacity focuses on the dimensions of time, labour, equipment and facilities.

5.5 Development of Hypotheses

The Link between Service Quality and Customer Satisfaction

Service quality implies the difference between the customers' expectations and their perceptions of service performance, whereas customer satisfaction is considered a short-term emotional reaction to a specific service performance, i.e. the evaluation of the specific transaction that follows a purchase event (Lovelock and Wright, 2002). The literature indicates that perceived high levels of service quality lead to an effective response in the form of customers' satisfaction. In other words, perceived high levels of service quality induce a psychological state called customer satisfaction. Therefore, customer satisfaction represents an outcome or direct function of the customers' perceptions of service quality (Churchill and Surprenant, 1982; Anderson, Fornell and Lehmann, 1994; Fornell, Johnson, Anderson, Cha
and Bryant, 1996; Cronin, Brady and Hult, 2000; Dabholkar et al., 2000; Brady and Robertson, 2001; Kang, Okamoto and Donovan, 2004; Choi, Lee, Kim and Lee, 2005; Olorunniwo et al., 2006; Cronzález, Comesaña and Brea, 2007), leading to the first hypothesis:

H1- There is a positive impact of service quality on customer satisfaction.

The Link between Customer Satisfaction and Customer Retention
Achieving a high level of customer satisfaction can bring some offensive and defensive advantages at the micro level, such as: increased customer loyalty/retention, reduced price elasticity (more tolerance of increases in price), insulation of current customers from other competitors’ campaigns, reduced costs from attracting new customers (by positive word of mouth), reduced costs of future transactions, an enhanced reputation for the company and minimized likelihood of customers switching to another brand in the case of quality falter. Thus, customer satisfaction helps to bring behavioural advantages for the individual business (Fornel, 1992; Anderson et al., 1994; Anderson, Fornell and Mazvancheryi, 2004). The literature indicates that customer satisfaction acts as an antecedent factor for customer retention and loyalty, i.e. customer satisfaction mediates the relationship between service quality and customer retention (Churchill and Surprenant, 1982; Rust and Zahorik, 1993; Danaher and Rust, 1996; Olsen, 2002; Anderson and Sullivan, 1993; Oliver, 1980; Mittal and Kamakura, 2001; Taylor and Baker, 1994; Cronzález et al., 2007).

H2-There is a positive impact of customer satisfaction on customer retention.

The Link between Customer Satisfaction and Productivity
As mentioned above, customer (dis)satisfaction brings behavioural and economic (dis)benefits, therefore, the relationship between customer satisfaction and productivity is positive through helping a company to use fewer resources handling returns, rework, warranties and complaint management. As a result, customer satisfaction can reduce costs which in turn lead to improved productivity. For example, Reichheld and Sasser (1990) mention that satisfying customers and reducing defects leads to increased productivity through lower costs of future transactions and attracting new customers.
On the other hand, it is conversely argued that increasing customer satisfaction increases costs which in turn reduce productivity. Anderson, Fornell and Rust (1997) find a negative relationship between customer satisfaction and productivity in the service setting (airlines, hotels, restaurant, etc.) and a positive association in the goods sector. Thus, there is evidence that improving customer satisfaction and productivity in the service sector is an important challenge; however, the present research will adopt the theoretical view and propose that customer satisfaction is positively related to productivity.

H3- There is a positive impact of customer satisfaction on productivity.

The Link between Customer Retention and Market Share

Retaining the current customer is an important policy for a company, delivering beneficial advantages such as increasing revenues, reducing the marketing costs of acquiring new customers, reducing problems and questions, and becoming more accustomed to the company's products (Bateson, 1995). In addition, customers who have a long term relationship with a firm are more likely to purchase additional services than are new customers, and also to spread favourable word-of-mouth (Zeithaml et al., 1996) and this leads to increased market share and revenues (Rust et al., 1995). The literature indicates that customer retention results from customer satisfaction; therefore customer satisfaction represents a central issue in the financial impact of service quality (Rust and Zahorik, 1993; Lariviére, 2008).

H4-There is a positive impact of customer retention on market share.

The Link between Market Share and Profitability

Increasing market share may return financial benefits for a company for a number of reasons, such as economies of scale from some aspects of the operation (e.g. procurement, manufacturing, marketing, R&D, etc.). In addition, higher market share may lead to greater bargaining power in the market between customers and suppliers (Aaker, 1995). Thus, a high market share proportion will lead to reduced costs over time, which in turn should be translated into higher profits (Buzzell and Gale, 1987). Although there is some inconsistency in the literature about the direction of such a relationship, researchers have found positive relationships between market share and profitability, i.e. companies with high market share.
tend to have higher earnings (Schoeffler et al., 1974; Szymanski et al., 1993; Buzzell and Gale, 1987; Larivière, 2008).

H5-There is a positive impact of market share on profitability.

The Link between Service Quality, Premium Price and Profitability

It is argued by different researchers that price can be used like other cues (value, brand name and store name) as an indicator of quality evaluation by consumers (Zeithaml, 1988; Dodds, Monroe and Grewal, 1991; Rao and Bergen, 1992; Lichtenstein and Burton, 1989). The current research is not interested in such a relationship; instead, the focus is on the relationship between quality of service and charging premium price.

The literature indicates that premium price can be used as an indicator of perceived high quality, or in other words that offering high levels of quality allows a company to charge higher prices. Theoretically, producing high quality gives a company the option to charge premium prices over competitors due to superior quality performance, and further higher premium prices will be translated into higher bottom line profits (Garvin, 1988; Shapiro, 1983; Phillips et al., 1983; Buzzell and Gale, 1987; Rust et al., 1994; Zeithaml, 2000; Kimes. 2001). Moreover, charging premium prices allows a company to invest more than its competitors in R&D and in new products, to obtain higher perceived quality and market share in the future. Unfortunately, premium price may undermine the market share position of the company.

H6 -There is a positive impact of service quality on premium price.
H7-Thers is a negative impact of premium price on market share.
H8-Thers is a positive impact of premium price on profitability.

The Link between Service Quality, Productivity and Profitability

Theoretically, improving quality will lead to increased productivity through reducing defects and wastage, as well as improving worker productivity which could lead to a reduced workforce while holding output constant (Garvin, 1984; Rust et al., 2002). However, in the service sector the management of quality cannot easily be separated from the management of productivity (Filiatrault et al., 1996), therefore, quality improvement must embrace both productivity and profitability at the same time (Gummesson, 1998).
The literature indicates that a positive relationship exists between quality and productivity for several reasons, such as reducing unnecessary work and reducing defects in the quality of materials, equipments, tools and other processes (Fuller, 1985; Leonard and Sasser, 1982; Hayes and Clarks, 1986; Garvin, 1983; Shetty, 1986; Krafick, 1988; McCracken and Kaynak, 1996; Larson and Sinha, 1995; Harkey and Varciu, 1992).

Unfortunately, the fluctuation of demand, in the service industry in general and the hotel industry in particular, is a huge problem which in turn presents a major challenge for both productivity and stability. Thus, the hotel industry epitomizes the challenge of achieving equilibrium between demand and capacity when demand is highly elastic and unstable (Lovelock and Wirtz, 2004; Zeithaml and Bitner, 2003). As a result, demand management should play a significant role in the relationship between quality of service and productivity. Balancing and managing the fluctuation of demand can bring favourable results for providers as well as customers. In other words, quality of service has a positive impact on productivity only when management has the ability to manage the demand fluctuations.

On one hand, when demand patterns are understood and managed (demand equal to supply or capacity), higher quality achieved leads to increased productivity as well as reduced cost. On the other hand, when the demand exceeds the capacity (high level of demand), workers will be overworked (increasing the probability of errors and delays), higher costs of labour and material will occur, staff will be pushed beyond their abilities to deliver consistent outcomes, and customers will be dissatisfied with service quality – which will in turn decrease profits. Low levels of demand will lead the company to suffer from underutilisation of resources and disappointing of current customers, which in turn will lead to decreased productivity (Harkey and Varciu, 1992; Lovelock and Wirtz, 2004; Zeithaml and Bitner, 2003). Thus, the relationship between service quality and productivity will be positively related only when the company can manage and control patterns of demand for their services capacity.

To do that, management should adopt techniques and procedures to manage and match the fluctuations of demand. These techniques, such as the demand management strategies, intelligence enhancement strategies, and supply management strategies, can cause the demand to fit the capacity of the company in different situations (Shemwell and Cronin, 1994; Zeithaml and Bitner, 2003; Lovelock and Wirtz, 2004; Lovelock et al., 1999).
H9- Managing the fluctuations of demand moderates the positive relationship between quality of service and productivity.

H10- There is a positive impact of productivity on profitability.

5.6 Conclusions
After discussing empirical studies in the investigated topic, this chapter identified some important questions in this relationship, which will be answered in the next chapters. This study seeks to determine what the relationship is between service quality and profitability in the UK budget hotel sector, and how this relationship works.

To do so, this chapter depicted and presented how service quality is related to profitability in a framework that supposes service quality has several consequences and benefits. Some of these benefits are intangible, such as customer satisfaction and retention, which help to increase the hotel's market share and profits, whilst some are tangible, such as decreased waste and costs as well as increased prices charged. However, all of these benefits should align between service quality and business performance. Finally, this chapter developed the research hypotheses required to explain how variables in the research model are related to each other and why, i.e. it created justifications for linkages in the research model.
6.1 Introduction
This chapter presents and discusses a number of methodological issues required for this research. Section two outlines the research objectives. Section three provides basic background about research philosophy, followed by discussion of the research philosophy adopted in section four. Section five gives a brief description of the possible types of research design. Section six justifies the research design selected and used in this research. Section seven discusses objectives, sample, and data analysis of the preliminary study and introduces findings and conclusions of the preliminary study (part two). Section nine discusses measurements used for variables in the first study (Hotel Performance Data) and second study (General Managers' Perspective) followed by changes undertaken for the questionnaire after the pilot testing. Section ten covers the sampling procedures. Section eleven outlines and explains the appropriate statistical analysis techniques used in this study. Finally, section twelve extracts conclusions from this chapter.

6.2 Objectives of the Study
(1) To develop a conceptual framework which captures the relationship between service quality and profitability in the UK budget hotel sector.
(2) To examine empirically the relationship between service quality and profitability in the UK budget hotel sector.
(3) To determine what variation, if any, there is in the nature and direction of this relationship among different data sets collected from different sources.
(4) To determine which outcome of service quality makes the greatest contribution to UK budget hotel profits.

6.3 Research Philosophy
Understanding the research philosophy is very useful for deciding which research design is going to work and why (Easterby-Smith, Thorpe and Lowe, 1999). The literature shows a few different philosophies or paradigms for conducting studies in business and management science. As a result, different names and classifications developed, such as positivism, phenomenology, pragmatism, interpretivism, realism, etc. (Saunders, Lewis
and Thornhill, 2003). Hence, the literature provides sufficient discussion regarding these different philosophies in order to outline elements and differences between them in terms of ontology (the reality is being investigated), epistemology (relationship between reality and researcher) and methodology (techniques will be used by researcher) (Healy and Perry, 2000).

Positivism assumes that the researcher makes an objective analysis and interpretation for the data collected (Saunders et al., 2003). In other words, such research philosophy supposes that researchers deal with issues objectively without influencing the real problem being studied. Furthermore, this philosophy supposes that the end product gained by this method can be law-like generalisations, similar to the results obtained by physical and natural scientists. In addition, this philosophy requires highly structured methodology, quantifiable observations and statistical analysis (Remenyi, Williams, Money and Swartz, 2005). Thus, researchers in such a paradigm separate themselves from the world they investigate.

In contrast to the first philosophy, phenomenology or interpretivism have a different view for developing knowledge, focusing on a subjective and descriptive model to deal with complicated situations rather than an objective, tangible or mathematical model (Remenyi et al., 2005). Such philosophies argue that the social world of business and management science is too complex to be treated as a physical science. To put it another way, any rich explanation and insight for complex management studies in the social world will be lost if its complexity is reduced to a series of law-like generalizations. In addition, this school of thought considers each business situation unique, with different and particular circumstances. Besides the complexity and uniqueness of the world, this school of thought considers and takes account of the changing state of business organisation as well as different interpretations by people. So, this methodology is not a suitable method for generalisation (Saunders et al., 2003).

Similar to the first philosophy, pragmatism (realism) asserts that reality does exist. In addition, this methodology supports the objective nature of science, i.e. the researcher is independent from what is being studied. However, this philosophy also believes that individuality will affect how people perceive the world, i.e. research is subjective. In addition, this school declares that large-scale social forces affect how and what people
perceive even if they are not aware of such factors and forces. Therefore, this school of thought brings multiple explanations and interpretations for science (Saunders et al., 2003).

Guba and Lincoln (1994) introduce different classifications of research diagrams. The first one is the positivism paradigm, which is totally sure about reality and indicates that findings are true. Experiments/surveys (quantitative methods) should be used in this paradigm which is objectivist in nature.

The second paradigm is critical theory, which believes that reality is shaped and developed by social, economic, ethical, and political values, crystallised over time i.e. reality has an historical structure. This philosophy makes assumptions about reality subjectively (value-dependent and not value free). Critical thinking therefore adopts specific methodologies including dialogic/dialectical methods, i.e. researchers change the social world within which participants live.

Thirdly, constructivism focuses on subjectively understanding multiple and specific constructed realities such as ideologies and values constructed by people to create findings. The researcher in such a subjectivist analysis should be a passionate participant within the world being investigated.

The final paradigm, realism, is the most popular for many qualitative studies. This paradigm believes that reality is real but it is still imperfectly apprehensible. Therefore, findings in realism may be true (i.e. it is a modified objectivist type of analysis). The most common methods in realism are case studies and convergent interviewing. In addition, triangulation can be used in this philosophy, by using qualitative and some quantitative methods. Hence, realism makes a link between positivism and the subjectivist paradigms.

Table 6.1 displays the main characteristic of the most common research philosophies and makes comparisons between them according to some criteria.
Table 6.1 Research Philosophies Comparison

<table>
<thead>
<tr>
<th>Feature</th>
<th>Positivism</th>
<th>Phenomenology</th>
<th>Pragmatism</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independence</td>
<td>Researcher is independent</td>
<td>Researcher is part of the study</td>
<td>Researcher is both independent and part of the study</td>
</tr>
<tr>
<td>Value-freedom (what &amp; how to study)</td>
<td>Objective criteria</td>
<td>Subjective criteria</td>
<td>Objective and subjective criteria.</td>
</tr>
<tr>
<td>Identify causality</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Deductive/inductive</td>
<td>Deductive</td>
<td>Inductive</td>
<td>Both</td>
</tr>
<tr>
<td>Operationalisation</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Reductionism</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Generalisation</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Cross-sectional analysis</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Sample size</td>
<td>Large</td>
<td>Small</td>
<td>Both</td>
</tr>
<tr>
<td>Measurement</td>
<td>Quantitative</td>
<td>Qualitative</td>
<td>Both</td>
</tr>
</tbody>
</table>

As we can see from the table, each one of the paradigms has different and distinct characteristics. However, it is clear that the pragmatism methodology combines features from both objectivist and subjectivist schools of thought to provide a new trend in research philosophy disciplines. In other words, the pragmatism philosophy forms a continuum of research philosophies since no one research model is better than another.

6.4 Research Philosophy Adopted

Owing to its particular aim and objectives, this research selected the positivism model as a research philosophy and approach. Although the pragmatism (realism) philosophy criteria are also suitable to the research objectives, some features of the pragmatism model makes it a less than perfect approach to deal with this topic. Positivism will be adopted for the following reasons: independence of researcher in this study, formulation of hypotheses is appropriate, exploration of relationships and causality between variables in a specific industry is required, and finally generalization is desired for the budget hotel sector.
6.5 Types of Research Design

Research design implies a guideline and framework for researchers. In other words, research design provides an outline for the research processes and elements. The choice of research design depends on the research nature, its purposes, and the questions and hypotheses developed. That is, determining the suitable research design should rely on the former elements. Research methods textbooks provide different categories and classification of research designs for researchers and scholars. Although each research design has distinctive characteristics, there are overlaps and confusion among them. The sections below discuss and explain briefly the most common types of research design (Aaker, Kumar and Day, 2001, 2004; Hakim, 2000; Yin, 2003).

6.5.1 Exploratory Study

This kind of research design aims to define and provide insight and understanding of a specific phenomenon or concept. Moreover, this research can be adopted to examine the problem more precisely, and to gain further information before confirming findings by using another type of research, e.g. breaking a broad and vague problem into smaller sub-problem statements. Thus, exploratory research could be used when the problem area is little known, in order to increase familiarity with the area. Exploratory research therefore focuses on research questions rather than specific hypotheses or actual measurement. Hence, flexibility, loosely structured information, small sample size, and an evolutionary approach are the main characteristics of exploratory research design (Malhotra and Birks, 2003; Churchill and Brown, 2004).

While it is preferred to conduct the exploratory research using qualitative techniques, some researchers employ quantitative techniques. For example, when the study aims to examine additional connections between several questions and hypotheses that had not been investigated before, the quantitative technique could be used. According to the exploratory research’s purposes, methods for collecting data in this type of study will vary to include different approaches, such as literature search, expert surveys, pilot surveys, secondary data, individual in-depth interviews, focus groups, and instructed observations (Yin, 2003; Sekaran, 2003).
6.5.2 Descriptive Study
Unlike the previous research design, this kind of research design aims to describe specific phenomena. In other words, such research tries to describe the characteristics of some variables under study in a specific situation (Sekaran, 2003). The variety of applications of descriptive research leads to its extensive use in the literature. For instance, it can be used to describe the characteristics of a specific group, to estimate the percentage of a specific population having a certain type of behaviour, to count the frequency of events, to determine the perception of specific goods or service, and so on.

6.5.3 Hypotheses Testing Study
This kind of research design aims to explain the nature of relationship or association between two or more variables, i.e. to explore relationships between variables by testing a set of hypotheses. Hence, the main goal of this research design is to explain variance in the dependent variable through one or more independent and mediating variables. As a result of using this research design, a researcher will be able to explore if there is any relationship between independent and dependent variables.

This research design should be formal, pre-planned and structured, with a large sample size, and the information needed should be quite clear. Some notes emerge from these characteristics. Firstly, such a design aims to measure associations in a specific phenomenon in a consistent and universal way. Secondly, the results developed using this type of research can be generalized to represent larger populations. Finally, methods that can be used in this research type include several techniques, such as surveys, secondary data, database and so on. Table 6.2 Summaries key features of the above research design strategies.
Table 6.2 Research Design Features

<table>
<thead>
<tr>
<th>Research design</th>
<th>When to use</th>
<th>Research question</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exploratory research</td>
<td>When the problem area is little known and not familiar. When researcher seeking knowledge in a contemporary and complex phenomenon.</td>
<td>What? Why?</td>
</tr>
<tr>
<td>Descriptive research</td>
<td>When the characteristics of some variables under study in a specific situation are not known.</td>
<td>How many? How much?</td>
</tr>
<tr>
<td>Hypothesis testing</td>
<td>When the researcher is interested in investigating the linkage between variables.</td>
<td>What? Who? How?</td>
</tr>
</tbody>
</table>

Source: Developed by researcher

As shown above, these research designs are different from each other in terms of the reasons for their use and the research questions that need to be answered. As a result, the differences between these types of research designs require the use of different procedures and methods for each. In other words, methods and techniques suitable for collecting data in the exploratory design may not be suitable or possible for conducting hypothesis testing, and vice versa.

6.6 Research Design Selected

The most important criterion for deciding the type of research design is the research question. Therefore, the present research uses hypotheses testing design to investigate the nature and degree of association between service quality and profitability in the UK budget hotel sector, i.e. what is the impact of service quality on profitability? Using the hypothesis testing design helps to explore the relationships between all variables included in the conceptual framework (positive, negative or nonexistent in this hotel sector). Moreover, the hypothesis research design selected in this study will determine the strength of association between various outcomes of service quality and profitability, in order to know which outcome or direction has more contribution and impact on profitability. Thus, the hypothesis research design was chosen for this study after excluding exploratory and descriptive designs which were not suitable according to the current research questions and objectives.
Although the required data is hard to collect, the present research could get access to one of the leading budget hotel chains in the UK, which has 477 hotels across the country. The main reason for choosing and conducting this research in a particular budget hotel chain can be summarised in these points:

- Investigating the service quality-profitability relationship in hotels that operate within the same segment and offer consistent standards (i.e. the same specifications) leads to a homogenous sample for analysis. As a result, additional and irrelevant variables in the analysis will be avoided and excluded (Harrington and Akehurst, 2000).

- In addition, the budget hotel market includes and serves the main customers in the hotel industry market, i.e. business and leisure travellers as well as local and foreigner guests (Jones, 2002). Therefore, the budget hotel setting provides an excellent opportunity for gaining wide and comprehensive perspectives and feedback about the industry.

- Moreover, units within this budget hotel chain are located in different places, such as London, various city centres, the motorway network, urban areas, and airports across the UK. Obviously, such a budget hotel company provides a national and comprehensive coverage of the budget market.

- Finally, this study got access and permission from the management of this budget hotel chain to obtain secondary data and to collect and distribute questionnaires in order to test the conceptual framework.

After selecting the research design, the next question is to decide which technique should be used for collecting data, i.e. a cross-sectional study or a longitudinal study. On the one hand, the cross-sectional approach represents the most popular research design in the literature. Unfortunately, such an approach doesn't offer deep penetration into the research problem. This design naturally provides a snapshot of the variables at a single point of time, and the sample in this approach should typically be selected to comprehensively represent the population. Therefore, this design of research is also
named by researchers as a sample survey (Churchill and Brown, 2004; Malhotra and Birks, 2003).

On the other hand, the longitudinal approach represents a more sophisticated technique for investigating relationships between variables at different points of time. Such an approach focuses on a fixed sample of elements, in order to measure variables by the same methods over time. In other words, the sample, measurements and variables in this approach remain constant, to provide an in-depth view of the research problem and track all changes taking place over the observed time period (Bernhardt, Donthu and Kennett, 2000). Some advantages and disadvantages of both techniques are summarised in Table 6.3.

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Cross-sectional design</th>
<th>Longitudinal design</th>
</tr>
</thead>
<tbody>
<tr>
<td>Detecting change</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Large amount of data</td>
<td></td>
<td>+</td>
</tr>
<tr>
<td>collection</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accuracy</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Representative sample</td>
<td>+</td>
<td>-</td>
</tr>
<tr>
<td>Response bias</td>
<td>+</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: Malhotra and Birks (2003, p: 86)

The present research will use both of these techniques to estimate and test the conceptual framework and to overcome the disadvantages and deficiencies of either one alone. The longitudinal approach will use secondary data provided by the same budget hotel chain (Hotel Performance Data). The cross-sectional approach will be conducted using a questionnaire developed for managers in the budget hotel chain (General Managers' Perspective).

At early stage of the current study as shown in chapter four, a preliminary qualitative study was conducted through interviewing managers of hotels in order to explore and validate the conceptual framework from the hoteliers’ perspective and to explore their understanding of performance and profitability and measures used and adopted in the
hotel industry. Thus, these interviews aimed to test whether the current framework can be used in the hotel industry, as determined from the hoteliers' viewpoints according to their experience. Thus, the study adopted qualitative methods to reinforce the research model.

To justify the usage of both qualitative and quantitative approaches in this research, Salomon (1991) mentions that such a link provides a systematic and analytic understanding about interactions between variables in a complex environment. Additionally, Rossman and Wilson (1984) display some advantages for such a method: confirmation and corroboration of each other, provision of richer detail and analysis, and creation of new lines of thinking. Furthermore, Green, Caracelli and Graham (1989) suggest that using both qualitative and quantitative methodologies leads to expanded breadth and scope of the study. Finally, Sieber (1973) proposes that using qualitative data during research design will support the quantitative data through improving the conceptual development and instrumentation.

6.7 Preliminary Study

6.7.1 Objectives of the Preliminary Study

This preliminary study aimed to explore the hoteliers' perceptions of the profitability concept and the current measures used in the hotel industry. Another purpose of the preliminary study was to test the suitability of the proposed research model from the industry players' points of view. Thus, this study has two objectives. As mentioned previously in chapter four, the discussion and results of this preliminary study was divided into two parts. The first part of the preliminary study addressed the hoteliers' understanding of profitability in the hotel industry and what measures were used, while the second part of the preliminary study discussed the adequacy of the hypothesized research model and the link between service quality and profitability.

Thus, the interview schedule includes two parts. Part one deals with profitability concepts and measures, whilst part two addresses the link between service quality and profitability in the hotel industry and how quality of service affects profitability as shown in one of the interview transcripts (Please see Appendix 1). Before displaying the findings of the second part of the preliminary study, the following sub-sections discuss some issues related for conducting this preliminary study.
6.7.2 Sample of the Preliminary Study

Several financial managers of five-star hotels in Jordan were approached to conduct the interviews. Phone calls were made with the potential interviewees before going to Jordan to give them a brief description about the study and the objectives of the interviews. Another wave of phone calls and personal contacts was conducted when the researcher arrived in Jordan. The potential interviewees were selected randomly from a list of hotels operated in Jordan and developed by the Jordan Hotel Association. Financial managers preferred to be interviewed due to their knowledge and expertise in the area of measures and definitions of profitability and their ability to evaluate the financial impact of service quality in their hotels. Four financial managers agreed to participate in the interviews, and appointments were made with them to do the interviews in the period between 29th of March and 25th of April 2006. Interviewees held senior positions in the financial departments of their hotel chains, as shown in the sample below:

- Mr Abed Aziz Salhab, Director of Finance, Sheraton Amman
- Mr Abd Al.-Barghouthi, Regional Financial Controller, Radisson SAS Jordan
- Issam Salem, Assistant Finance & Business Support Manager, Intercontinental-Jordan
- Mr Ehab Abu Osba’a, Assistant Financial Manager, Le Royal-Amman

All interviewees agreed to be tape-recorded except for one, who preferred that the researcher wrote notes instead. The open-ended, semi-structured interview approach was used to give the interviewees the freedom to answer and to bring some preliminary issues as shown in the interview transcript in Appendix 1. The duration of the interviews was between 30 and 40 minutes, and all of the interviews were carried out face-to-face and occurred in the interviewees’ offices. A short introduction by the researcher was given to provide some information about the study in order to better facilitate the interviews. Interviews were conducted in the Arabic language since this language is the first language in Jordan. However, the raw data of the interviews was translated accurately into the English language.

6.7.3 Data Analysis of the Preliminary Study

As suggested by Miles and Huberman (1994) and Dey (1993), at the beginning of the data analysis stage of the preliminary study, the researcher compiled all the data collected
from the interviewees in the form of tape recordings and handwritten notes. This raw data was converted to English in the form of intelligible and clear documents and transcripts (Please see one example of transcripts in Appendix 1). Later, the researcher reviewed all transcripts in order to develop a list of codes to categorise, combine, and differentiate themes and topics that emerged in the data. Thus, these codes (labels or tags) were developed to organize, assign, and allocate themes and sub-themes dealing with similar meanings and implications. Appendix 2 displays the list of codes and sub-codes developed in the preliminary study and what each code means.

The researcher then started linking responses regarding each code from all participants in order to determine where information and answers agreed and disagreed among participants. To do so, respondents' answers for each code were summarised to explore the patterns of answers (Appendix 3 displays this stage of data analysis and discussion). In other words, the researcher integrated the responses and discussions of each code across all interviewees to get the findings and formulate conclusions. The researcher then compared the findings of the preliminary study with the findings of the literature review undertaken previously by the researcher.

6.7.4 Findings of the Preliminary Study (Part Two)

In this part, interviewees were invited to think about what factors affect profitability in the hotel industry; they were also invited to think about the relationship between service quality and profitability in the hotel industry, and what benefits and impact of service quality there are in this industry. Thus, part two of the preliminary study aimed to get a deeper understanding and to confirm the theoretical and empirical results reviewed by the researcher.

The interviewees were invited to answer the following four open-ended questions:

Q.2 According to your opinion, what factors affect the hotel's profitability?

Q.3 What is the nature of the relationship between service quality and profitability in the hotel industry?
Q.4 What are the financial benefits or outcomes of service quality activities in the hotel industry?

Q.5 In my conceptual framework, there are three paths or directions for the relationships between high levels of service quality and profitability as shown below. Which one would you support, and with which do you agree?

- Charging premium price
- Customer emphasis (increasing revenues)
- Operations emphasis (increasing productivity)

The data analysis of the second part of the preliminary study produced some useful findings and results, as shown below. (For more details and discussions of the preliminary study, please see Appendix 3).

(1) Service quality was one of the most significant and often-cited internal factors that affect the hotel's profitability. However, interviewees highlighted some other factors as well, such as the bundle of services offered, staff behaviour, location, and brand familiarity of the hotel.

(2) Political situations and stability represent the most important external factors that affect profitability.

(3) Service quality is positively related with profitability in the hotel industry.

(4) The positive relationship between service quality and profitability in the hotel industry is not clear in terms of the strength (strong or weak relationship) and mechanism of the effect and link (direct or indirect relationship).

(5) Satisfying the current customers and increasing their response and relationship with a particular brand was the most important outcome or benefit of service quality.

(6) The proposed research model in the current study was almost compatible with hoteliers' opinions and answers. In other words, hoteliers agreed with most of the relationships and connections introduced between variables included in the proposed
research model except for the relationship between service quality and productivity. This particular link (between service quality and productivity) was debated by the interviewees, and no confirmation has emerged since interviewees were not sure whether service quality could improve productivity or not. Some participants said that service quality would improve productivity since service quality doesn’t mean more costs and activities, while other respondents said that this relationship is negative, since superior service quality requested by customers requires higher expenses and greater cost of materials.

To conclude, the findings that emerged in the second part of the preliminary study indicate that service quality forms a significant factor and determinant of a hotel’s profitability. This result is consistent with results introduced in the literature by Buzzel (2004) and Buzzel and Gale (1987). Moreover, the research model developed and displayed in chapter 5 was confirmed and supported in the preliminary study in all aspects other than one link (or path), which was debated. In other words, interviewees approved and appreciated relationships between variables included in the research model except the link between service quality and productivity. Accordingly, although that one link is still not fully supported and confirmed, the researcher decided to use the research model as displayed in chapter 5 for the main study without making any changes.

6.8 Timeline of the Main Study
At early stages of the present study, in June 2006 in particular, the researcher, and his supervisors, made direct contact with one CEO of a leading budget hotel chain in the UK. The objectives and significance of the current study were introduced to the CEO. This budget hotel chain was targeted in particular due to its promising performance, popularity in the market, wide distribution across the country and, more importantly, because the University of Surrey has a long-standing relationship with this budget hotel chain. It was assured by the researcher that the results of the study will be shared with the budget hotel company supporting this study. A few weeks later the top management gave the researcher permission to access the company’s Balanced Scorecard Database. On July 2006, the budget hotel chain selected a contact person. His position was the Brand Excellence Manager of the chain.
According to the above introduction, Table 6.4 below summarizes the steps and activities undertaken by the researcher to conduct the current study from the early stages until the data analysis stage as follows:

<table>
<thead>
<tr>
<th>Step</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Initial contact</td>
<td>June 2006</td>
</tr>
<tr>
<td>Getting permission from the top management and identifying a contact person</td>
<td>July 2006</td>
</tr>
<tr>
<td>Introducing the study objectives and data required to the contact person.</td>
<td>August 2006</td>
</tr>
<tr>
<td>Getting the company Balanced Scorecard Data (Study One)</td>
<td>September 2006</td>
</tr>
<tr>
<td>Reorganizing the Balanced Scorecard Data into new Excel files (Study One)</td>
<td>October 2006</td>
</tr>
<tr>
<td>Analyzing the Balanced Scorecard data (Study One)</td>
<td>November 2006 - January 2007</td>
</tr>
<tr>
<td>Pilot testing of the questionnaire (Study Two)</td>
<td>February 2007</td>
</tr>
<tr>
<td>Distributing the questionnaire by Panorama online system, email and post (Study Two)</td>
<td>February - April 2007</td>
</tr>
<tr>
<td>Reminder of the survey (Study Two)</td>
<td>May 2007</td>
</tr>
<tr>
<td>Data entry stage (Study Two)</td>
<td>May 2007</td>
</tr>
<tr>
<td>Analyzing the second study data</td>
<td>June - August 2007</td>
</tr>
</tbody>
</table>

According to the above table, on the first of August 2006, the researcher had a meeting with the contact person at the company headquarters. A list of broad questions developed before the meeting served as ground to build on and opened the door for other questions. The general questions in the meeting focused on the quality system adopted in the hotel chain, how they measure their service quality, how they measure their customers' satisfaction, how they measure their financial performance, how often they do this, since when have they been measuring such variables, how many customers they survey, what is the level of data available (monthly, quarterly or yearly level) and for how long they have been using the Balanced Scorecard System. Before the discussion of all these points, the researcher introduced the objectives of the present study in more detail and showed the
contact person all the procedures needed for the current study, such as the timeframe of the study, research model and all variables and measures needed. The contact person seemed impressed and interested in the research topic.

At this meeting, the contact person provided some relevant documents about the Balanced Scorecard System in terms of what variables and measures are used in this system. Accordingly, the researcher tried to compare the measures and data available already in the company’s system with the variables and measures needed for the current research. In addition, the contact person showed the researcher the computerized version of the Balanced Scorecard System and explained how it worked. In other words, the contact person displayed samples of the Balanced Scorecard System data, such as the brand standards they use, guest recommendation/satisfaction surveys they collect and some financial and operational indicators, to the researcher (More description about the Balanced Scorecard System will be introduced in chapter 7).

This discussion with the contact person identified those variables already available in the system and how the company measures them. At the end of the meeting, the contact person promised to provide all data required and to communicate with any department in the chain to facilitate the study. This meeting lasted for around two hours at the contact person’s office.

The outcome of this meeting indicated that the budget hotel chain collects the Balanced Scorecard Data on a monthly basis for nearly 200 units but not for all the units owned and operated by the hotel chain. Moreover, data gathered by the company covers the period from March 2005 until that time. However, the researcher had to wait until the end of the month to get the most recent data. The researcher recognised that the data in the Balanced Scorecard System was collected using the company’s own measures which were different from measures explored in the literature and intended to be used by the researcher. Moreover, not all variables included in the research model were measured and included in the Balanced Scorecard System, especially labour productivity, price perceptions, and customer satisfaction.

Therefore, the researcher decided to conduct another study to collect another set of data using the researcher's measures to cover the whole research model developed. In other
words, the researcher decided to collect the Balanced Scorecard Data available until that time from the company’s records (study one) as well as collect another subjective set of data (study two) gathered by the researcher himself to overcome problems and shortcomings that occurred in study one. Hence, study two will conduct a survey to measure and test the research model from manager’s perspective through distributing a questionnaire to all general managers of units in the chain, not only units that were included in the Balanced Scorecard System in study one.

To start the first study, the researcher had another meeting with the contact person on the 15th of August 2006 to give a list of variables needed to conduct the first study and to sign a confidentially agreement. The researcher required all data available since March 2005 until that moment at monthly and unit levels for the following variables in the company’s system:

- The aggregated brand compliance score for each unit.
- Profit growth of each unit.
- Sales growth of each unit.
- Guest recommendation for each unit as a proxy of measuring customer and guest retention.

As shown on the previous table, the first wave of the Balanced Scorecard Data was sent on the 29th of September 2006 by e-mail from the contact person to the researcher. At the end of October 2006, more data was sent to complete the data set covering the 20-month period from March 2005 until October 2006. Several Excel files were attached to the emails, including list of units with scores for variables or measures as requested (chapter 7 explains the data in the Balanced Scorecard System).

The data sent was at monthly level base for each unit, i.e. scores were reported for each unit over several months for several variables. In addition, the attached files included some theoretical background about the Balanced Scorecard System in terms of objectives, definitions of each dimension and aspect of performance measured in the system as will be discussed in the next chapter.
After getting the original data files in the researcher's computer, several e-mails and phone calls were made thereafter between the researcher and the contact person and the financial team in the budget hotel company to answer some questions raised when the original data files were transformed from the original compact micro files into normal Excel files. Such discussion aimed to elucidating how scores for variables or measures have been calculated. For example, some missing scores for the sales growth and profit growth were found. The contact person and the financial team of the budget hotel explained why these problems (Chapter 7 covers such problems) were in the data set. In order to use the data obtained from the company, the researcher had to transform data from the original micro Excel files into new Excel files, to do so, the researcher had to rearrange and reorganise the flow of the scores of variables from a horizontal view to a vertical view in order to use this data set in statistical software packages. This stage took a long time to ensure that the data was correctly rearranged. To put it more simply, the original files of data arranged the variables vertically for each unit, while scores for these variables were arranged horizontally over months (Chapter 7 displays sample of the layout and structure of the Balanced Scorecard System). Thus, the researcher had to make these changes to the data layout and structure in order to use the data in the statistical software packages. After finishing the rearrangement stage, the researcher started analyzing the data by using the suitable statistical software as will be discussed in the next chapter.

For study two, as shown on Table 6.4, the researcher conducted a pilot testing of the questionnaire designed with the contact person and 10 other general managers in the chain. Some changes have been made according to the respondents' suggestions, especially regarding the number and length of some questions in the questionnaire.

After approximately two weeks and before starting the survey for the second study, the contact person sent a note to all general managers of units by using their internal communication system to inform them about the survey and to encourage them to participate. After this stage, the researcher started distributing the questionnaire to all units in the budget hotel chain using different approaches to ensure a high response rate. First, the researcher used an online system called Panorama to design the questionnaire and send it to all respondents. After designing an electronic version of the questionnaire, a link to the questionnaire was sent to the email addresses of all general managers. The
list of email addresses was provided by the contact person. Unfortunately, the response rate was very poor (around 25 questionnaires), due to technical problems. In other words, general managers could not answer the questionnaire because the internet policy adopted by the hotel chain restricted any internet browsing, meaning that general managers were not allowed to open the link and fill out the questionnaire, i.e. it only allowed for general managers to check their corporate e-mails. Thus, as a second method, the researcher resent the questionnaire as an attached file to all the general managers who could not participate in the first wave of the survey. To do so, the researcher attached a protected word file copy of the questionnaire to prevent respondents making any changes to the wording of the questionnaire. However, respondents were only allowed to put their answers on the questionnaire by clicking their answers in boxes to suit their opinions. Respondents were asked to send the completed questionnaire back by e-mail to the researcher’s email address. Unfortunately, this second approach also did not provide enough respondents. Only 47 questionnaires were sent back by email from managers.

Third, on the first of March 2006, the researcher resent the questionnaire by post to the remaining general managers who did not participate in the two previous waves of the survey. To ensure a higher response rate, a prepaid envelope was enclosed with each letter. The researcher put codes on all questionnaires to be able to identify who retuned the questionnaire and who did not. A few weeks later, the researcher sent a reminder by post for all general managers who did not answer with a new prepaid envelope. This third method collected around 135 questionnaires. At this stage, the researcher decided to stop the survey because the response rate was statistically acceptable according to assumptions of multiple regression (Hair et al, 2006). The next stage involved analyzing the data as will be displayed in chapter 8.

To conclude, two main studies were undertaken to complete this research. In study one, the researcher collected objective and secondary data gathered and designed by the company, while in study two the researcher collected subjective data designed by the researcher.
6.9 Measurement of Variables

6.9.1 Study 1 (Hotel Performance Data)

As mentioned in the previous section, this study obtained data from secondary sources (company records) in order to measure the variables in the conceptual framework. Data available from the company’s records measures the following variables: service quality, customer retention, premium price, sales growth and profitability. To explain further, the sections below provide brief descriptions about the indicators and measures used by the company for measuring variables in the research model.

- **Service Quality**
  Service quality measured in this budget hotel company using an internal auditing approach, conducted by the general manager of each unit and an auditing team in the headquarters of the hotel chain. Such auditing process is called a brand compliance assessment. In other words, this process clarifies to what extent certain specific standards and features in different areas of the hotel are followed. To do that, the general managers and the auditing team use a checklist that covers different standards, features and areas in the hotel, including guests’ experiences in terms of different standards (e.g. pre-arrival booking, first impression of the team, first impression of reception, check-in, the route to the room, great service, night reception, breakfast, etc.), reception operation, and housekeeping standards.

- **Customer Retention**
  This variable was measured by asking customers and guests about their likelihood to recommend the hotel for others. Five-point numerical rating scale (from Definitely will not/Definitely will) was used to ask guests about their intention to recommend this hotel brand to others.

- **Sales Growth**
  This rate measures the sales growth rate by dividing sales achieved of each month by sales gained in the same month last year.
• **Profit Growth**

Percentage of return on capital employed (ROCE) growth was used by the company for measuring the profitability of each unit throughout the chain. Growth rate implies the change in results comparing to the same period in the previous year.

• **Premium Price**

The price charged per room in each unit was used to measure this variable. Obviously, there are variations and differences in terms of room rate between units and over time, such as weekend and weekday or summer and winter rates. For example, units located in London will have room rates higher than those in suburban locations, and the weekday room rate for a room is more expensive than the weekend rate. To overcome this problem and to gain a comprehensive view of room rates for each unit separately, an average room rate was used for measuring this variable for each unit in the chain.

6.9.2 **Study 2 (General Managers’ Perspective)**

Data collected in the second study is considered a primary source of data since it was gathered by a questionnaire developed and distributed by the researcher. The questionnaire measures all variables in the conceptual framework from the management’s perspective, including service quality, customer satisfaction, customer retention, premium price, market share, profitability, productivity, and managing demand and capacity (Please see Appendix 4).

For the service performance variables, including quality of service, customer satisfaction, customer retention and price perception, the general manager’s perspective was used to evaluate performance in these variables according to their interaction with customers and guests and their knowledge of customers’ perceptions, assessments and needs.

Although most of the service studies have used customers as a primary source of data, there is a sufficient number of empirical studies that have indicated that service provider’s perceptions are highly correlated with those of customers, not only in their overall assessment of service quality, but also in their evaluations of the firm’s service performance climate, practices and procedures e.g. how much managers emphasized service and how well managers run the service (e.g. Schneider, Parkington and Buxton, 1980; Schneider and Bowen, 1985; Dunlap, Tornow and Wiley, 1991; Reynierse and
Harker, 1992). In other words, a high degree of consistency has been found between providers' self-reports of customer's perceptions and customers' actual perceptions of service performance. In this respect, Mangold and Babakus (1991) emphasize that service providers can be superior to customers as a source of service quality data since service employees have a back stage view, allowing them to get more details of the service performance than customers who have front stage perspective only. In other words, provider's perspective enables companies to identify and predict activities and problems that go unnoticed by customers.

Accordingly, the appropriateness of the service provider's perspective (top management or employees) was discussed and proven in the literature as a valuable tool for evaluating service performance. Several papers provide justification for the appropriateness of such methods. For instance, service providers can understand the customers' service needs and the firm's ability to deliver that service (Schneider et al., 1980). Moreover, Schneider and Bowen, (1985) say that the service providers approach provides accurate customer satisfaction data as it appears to be quite sensitive as to how their customers are treated. Sergeant and Frenkel (2000) also appreciate the appropriateness of such an approach since service providers (customer-contact employees) are the face of any organisation and their interaction with customers is considered a part of the service. Therefore, they can affect the customers' perception and satisfaction. In addition, the employees who provide the services offer many significant insights about the processes, shortfalls and problems of the service performance since they are, in a way, internal customers of the service company (Parasurman, Zeithaml and Berry, 1990). Boshoff and Mels (1995) state that the service provider approach is considered a valid method to evaluate service performance and recognise challenges facing customers because service results from the human interaction between customers and service providers. Finally, Berry, Parasuraman and Zeithaml (1994) summarise some benefits of measuring service quality and performance from the provider perspective into two points. First, a service provider's experience can reveal what problems occur in the service system, why they happen, and how to overcome them. Second, a service provider is able to predict when the system is going to be down.

Tsang and Que (2000) used the management perspective (respondents ranged from general managers to supervisors) to measure service quality provided in the Chinese hotel
market, in order to compare it with customers’ expectations and perceptions of service quality. They found some discrepancies between customers’ perceptions of actual service delivered and managers’ perceptions, which were higher. However, they found that managers have a reasonably good understanding of guests’ expectations. They concluded that management’s perception and evaluation of service quality delivery is a useful tool to use in identifying the service problems and service failure points in the hotel industry. Tsang and Que recommended that managers carry out this analysis regularly, interacting with guests to experience real service delivery in order to gain a better understanding of guests’ perceptions since knowing guests’ expectations is not enough to perform service at the desired level.

In light of the previous discussions, it can be accepted that service providers, whether they are top management or a customer contact employee, have a valid perspective which is a useful source of service performance information. Thus, such an approach can be used for service performance assessment rather than merely asking the customers themselves, especially if it is not possible to contact the customers directly.

Indeed, service providers’ assessments of service delivery have been used extensively and effectively in previous research such as; (Schneider et al., 1980; Schneider and Bowen, 1985; Bashoff and Mels, 1995; Bashoff and Tait, 1996; Goodale and Koerner, 1997; Sergeant and Franker, 2000; Malhotra and Mukherjee, 2003; Malhorta and Mukherjee, 2004). In the same time, a huge number of former studies used top management’s perspective to successfully evaluate service delivered to customers such as (Harrington and Akehurst, 1996; Chang and Chen, 1998; Tsang and Qu, 2000; Raju and Lonial, 2002; Lee and Hwan, 2005; Daskalopoulou and Petrou, 2005; Yoo and Park, 2007; Ueno, 2008).

Although management tends to perceive its service performance as being more successful than customers perceive it to be, the literature measured service quality performance from a managerial perspective instead of a customer perspective because the managers’ perceptions can directly affect the design, development and delivery of the service (Tsang and Qu, 2000). Moreover, Nel and Pitt (1993) argue that managers can have a reasonably good understanding of customer needs and expectations. Knust and Lemink (2000) also used the managers’ perceptions for measuring service quality and service performance
instead of customers’ perceptions since this perspective represents a reliable proxy of customers’ actual perception.

Accordingly, the general manager’s perspective instead of customers and guests was used for measuring and evaluating performance of service quality, customer satisfaction, customer retention and premium price by asking general managers of each unit in the budget hotel chain.

On the other hand, for the business performance variables, the literature indicates two approaches for measuring business performance in general and financial performance in particular, either the objective approach (absolute values) or the subjective approach (management’s judgement of performance). Access to performance data at the hotel unit level, like any private company, is restricted. In other words, owners try not to expose their business financial data. Aggregate performance data can be provided by some data bases (e.g. Data Stream, Amadeus, etc.) and some consulting and auditing companies (e.g. Deloitte & Touche, TRI, PKF, etc.), but unfortunately this level of data can’t explain variations in performance between individual hotels. Since objective measurement at the hotel unit level is not available or possible as an option for measuring financial performance, the subjective approach should be used to measure the hotel’s performance and profitability. The subjective approach reflects the manager’s own assessment of some business indicators of the organization, in relation to competitors in the industry, i.e. it is a self-reported measure of performance.

This approach has been supported and justified in the literature for measuring business performance. Dess and Robinson (1984) and Pearce, Robinson and Robinson (1987) found a positive correlation between objective and subjective measurements of performance. In other words, researchers confirmed the validity and reliability of the subjective approach for measuring performance, when problems are encountered in obtaining objective accounting performance data. As a result, previous studies used this methodology extensively for measuring the relationship between different variables (e.g. market orientation, quality improvements, strategic decisions, etc.) and business performance.
Therefore, the hotel’s profitability and assorted performance other variables (e.g. market share, productivity and managing demand) measured in study two using the subjective approach, through developing special questions in the questionnaire to measure these variables from the managers’ viewpoints. In other words, the business performance variables will be measured in the second study by using a subjective approach which relies on management’s perception of the hotel’s performance in relation to similar competitors in the industry, assessed over the past three years using a seven-point Likert scale. Responses will be ranged on the seven point scale from much worse than competitors to much better than competitors (Sin et al., 2005). Obviously, such numerous rating points will increase the possibility of responses to be clustered around the mean i.e. the increased spread of responses will produce more variation between hotels in terms of performance indicators. The sections below show the measures used in the questionnaire for measuring variables in the research model.

*Service Quality*

Therefore, this study will adopt the two dimensions (physical quality and staff behaviour) of service quality which emerged in the three-dimension scale developed and refined by Ekinci (2001); Ekinci et al (2008). To put it more simply, eight items related to service quality performance were used to measure the service provider’s perception of service quality performance according to a five-point Likert scale. Items 1, 2, 3, and 4 measure the physical quality dimension, while items 5, 6, 7 and 8 measure the staff behaviour and attitude dimension. Below is a sample of one item from the service quality scale.

<table>
<thead>
<tr>
<th>Service Features</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our decor is well co-ordinated.</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
<td>□</td>
</tr>
</tbody>
</table>

*Customer Satisfaction*

According to the definitions from the previous chapter, the present research will measure the customers’ satisfaction by adopting the emotional items used in the hospitality setting introduced by Baker and Compton (2000). In other words, customer satisfaction items (emotion-based) measure the emotional state of customers by using a five-point
numerical rating scale. These items are: very dissatisfied/very satisfied, very displeased/very pleased, and very unfavourable/very favourable. Thus, the service provider will be asked about these items to measure the satisfaction of guests as shown in the sample below:

*Overall, how would you rate the guests’ overall experiences with your hotel? Please indicate your opinion on the following scales by clicking a suitable number for you.*

<table>
<thead>
<tr>
<th>Very Dissatisfied</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Very Satisfied</th>
</tr>
</thead>
</table>

- **Customer Retention**

The present research used the definition of customer retention introduced by Ranaweera (2003). Therefore, two items were used, with a five-point numerical rating scale. In other words, these items ask the service provider about the likelihood of their customers and guests to use and retain to the hotel brand again and to recommend it to others, as shown in the sample below:

*Overall, how likely is that the guests will return to this hotel? Please indicate your opinion on the following scale by clicking a suitable number for you.*

<table>
<thead>
<tr>
<th>Extremely Unlikely</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Extremely Likely</th>
</tr>
</thead>
</table>

- **Premium Price**

One item with a five-point numerical rating scale was used to ask the service provider about how guests rate the price they paid for accommodation in this hotel, as compared to other similar hotels:

*Overall, how would you rate the guests’ perceptions of the price paid for accommodation in your hotel compared to similar hotels? Please indicate your opinion on the following scale by clicking a suitable number for you.*

<table>
<thead>
<tr>
<th>Lower Than Similar Hotels</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Higher Than Similar Hotels</th>
</tr>
</thead>
</table>

- **Market Share**

The actual market share for a hotel means the percentage of total rooms occupied in a specific hotel compared to the total number of occupied rooms in the competitive market (Stutts, 2001). Obviously, this approach to measuring the market share for a
hotel is compatible with the first approach of defining and measuring the market share variable mentioned in an earlier chapter.

Thus, each hotel’s manager has to evaluate his market share (rooms sold or occupied) against other similar hotels in the same area for the last three years as shown in the following question:

![Financial Performance Indicators](image)

- **Profitability**
As mentioned previously, the business profitability dimension measured using the profitability ratio analysis. To that end, each hotel’s manager will evaluate the hotel’s profitability using two measures, the return on capital employed ratio (ROCE) and the RevPAR, in relation to similar hotels in the same area, in the last three years, as shown below:

![Financial Performance Indicators](image)

- **Productivity**
The present research adopted labour productivity, which is considered a partial approach for measuring productivity, as mentioned earlier in chapter five. In addition, this study used the occupancy rate for measuring the hotel productivity and
operational performance of a hotel which represents a physical measurement of productivity as mentioned earlier in chapter five. Even though the labour productivity ratio has some limitations, the present research will use it for measuring service productivity because it focuses on the one factor that represents the majority of total costs in service organizations in general and in the hospitality industry in particular (Ball et al., 1986; Coltman, 1989; Anderson et al., 1997; Sigala et al., 2005).

Thus, the present approach used the labour productivity and occupancy rate for measuring productivity. That is, each hotel’s manager will evaluate labour productivity and occupancy in the hotel in relation to other similar hotels in the same area for the last three years, as shown below:

<table>
<thead>
<tr>
<th><strong>Financial Performance Indicators</strong></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
</tr>
</thead>
<tbody>
<tr>
<td>How would you rate your hotel’s labour productivity*** in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- **Managing Demand**

As mentioned in chapter five, there are two solutions for managing the fluctuation of demand. Items for measuring the first solution (managing demand to match capacity) were extracted from the dimensions that can be applied in the hotel industry; therefore, just three dimensions used. To be more precise, the price dimension was measured by items one and four, a modified product elements dimension was measured by item number two, and the education and communication dimension was measured by items three and five. The fourth dimension (place and time of delivery) is difficult to adapt to the hotel industry.

On the other hand, items for measuring the second solution, adjusting the level of capacity to match demand, was measured through three dimensions; time, labour, equipment and facilities. The time dimension was measured by items eight and ten,
labour was measured by items six and nine, while facilities equipment was measured by item seven. The item below represents a sample of the scale used;

<table>
<thead>
<tr>
<th>Managing Demand &amp; Capacity</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>In this hotel, we charge full prices during peak periods i.e. no discounts.</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

6.8.3 Pilot Study of the Research Instrument

The pilot study was undertaken with general managers in the same budget hotel company. An electronic copy of the questionnaire was sent out by e-mail to 10 managers within a two week time period. A covering letter asked managers to complete the questionnaire and send it back to the researcher’s e-mail address. At the same time, respondents were asked to give their comments and recommendations in terms of clarity of questions, language and layout of the questionnaire, and give more ideas and suggestions. A reminder e-mail was sent after the first week. A response rate of 90% usable questionnaires was achieved. Points raised and modifications recommended by general managers were used to improve the structure of the questionnaire and the clarity of questions, including the following:

- One sentence was added in the introduction to inform the reader that the study was approved and supported by the management of the budget hotel company, in order to improve the response rate.
- The introduction set a deadline date for completing the survey.
- One more option was added to the location group in Part I Q.1. The new option is “countryside” because some respondents didn’t find any answer suitable for them.
- The numbers of years of operation in Part I Q.2 was changed from 1-3 years to 0-3 years, as some hotels have been operated for less than a year.
- Items in Part I Q.5, which measure brand familiarity, were summarised into one item that measures to what extent the brand name of this particular hotel is popular from the guest’s perspective, because respondents gave similar ratings or answers for all
three original items measuring brand familiarity, i.e. managers could not differentiate between the three items measuring brand familiarity.

- The first item in part II Q.1 was changed from “Our decor is beautifully co-ordinated with great attention to detail” to “Our decor is well co-ordinated”; the rest of this item “with great attention to detail” was deleted because it made managers confused.

- The word “staff” part II Q.1 was changed to “our team member” since this phrasing is very commonly used in the internal auditing system.

- In Part II Q.2, one item for measuring customer satisfaction was used instead of 3 for measuring this variable or construct. Most of the general managers put similar rates for all three items. In other words, managers didn’t differentiate between the items and gave the same scaling for each.

- In part III Q.1, occupancy rate was added as a measurement of productivity in addition to using the labour productivity item. The reason was that managers did not differentiate too much between indicators of profitability, market share and labour productivity.

- Changing the word “repeated customers” to “repeat customers” in Part III Q.2+3.

- Some items in part III Q.4 were changed and reworded because they were not easily understood. Moreover, managers asked for examples for some items.

- One age group in part IV Q.2 was changed from 25-34 to 20-34, as some managers are younger than 25 years old.

6.10 Sampling Procedures

6.10.1 Sample Population

The population of the present research was all hotels owned and operated by one budget hotel chain in the UK. This hotel chain has over 300 units across the country. Thus, the sample frame for this research includes all hotels at the unit level operating under the brand name of a specific budget hotel chain in UK.

6.10.2 Sample Selection

On one hand, data collected for the first study (Hotel Performance Data) covers the period from March of 2005 until October of 2006 for the selected budget hotel chain, i.e. 20 months time. In other words, this data set includes data for different points of time for various variables, i.e. it is panel data. This information was gathered and developed by the chain each month at the unit level for 182 units throughout the UK.
The second study (General Managers’ Perspective) surveyed all units operating in the same budget hotel chain. Intended respondents in this study were the general managers of each unit. A covering letter and self-administered questionnaire were distributed by e-mail and post (with a pre-paid return postage envelope) to the general managers for each unit.

6.11 Data Analysis Techniques

The data analysis for this research was undertaken using the following techniques:

6.11.1 Validity and Reliability of the Measures

Using alternative scales influences the quality and goodness of data collected. Therefore, it’s important to assure that the scales developed and used measure variables accurately and correctly (Sekaran, 2003). Literature introduces different tests for validity and reliability:

6.11.1.1 Validity

Validity aims to examine whether the items used in the research instrument are tapping and reflecting the concept itself or something else (Sekaran, 2003). Hence, validity means the degree to which the construct is measured and captured (McDaniel and Gates, 2006). Literature provides different ways of establishing validity as shown below:

Content Validity

This type of validity measures to what extent the scale used is adequate and represents the concept. To put it differently, content validity is considered as a function of how well the proposed dimensions and elements of the concept have been delineated and targeted by the scale, i.e. the more items are used for measuring the concept, the higher the content validity of the scale (Sekaran, 2003). In this sense, content validity informs about the representativeness or sampling adequacy of the instrument for measuring the concept (McDaniel and Gates, 2006). The main advantage of measuring content validity is that researchers can make sure the scale covers the most crucial aspects and characteristics of the construct being measured. To ensure that researcher will achieve valid content, a systematic process of item collection from the relevant literature should be followed, to gain the maximum number of possible items.
Thus, the initial set of items should to be large, to make sure the refined set of items still covers the concept (Churchill and Brown, 2004).

Face validity is the technique for achieving content validity. Establishing face validity can be performed by asking other people or experts about the scale developed. Simply, those people and experts evaluate and judge whether the scale captures the concept that is the focus of attention. Face validity considered an essential step of scale purification. Therefore, this technique is useful for newly established scales, to make sure that the developed scale measures and reflects the content of the concept investigated (Bryman and Bill, 2003). Unfortunately, face validity does have some criticisms and weaknesses; it depends only on the judgement, agreement and subjective evaluation of the researcher. However, revisions and frequent discussion can enhance the outcome of face validity (McDaniel and Gates, 2006).

**Criterion-Related Validity**

This test of validity has a different purpose and implication. Criterion validity aims to make sure that the scale used identifies the differences between subjects based on some criterion, e.g. the characteristics and behaviour of individuals. The literature provides two techniques for running this validity test: concurrent validity and predictive validity (Sekaran, 2003). Concurrent validity helps to decide whether the research sample is different in terms of some criterion known before running the analysis. In other words, the score obtained from the sample should be different among the subjects, as expected before running the data analysis. In contrast, predictive validity is interested in identifying differences between subjects in the sample according to some future criterion instead of the contemporary criterion.

**Construct Validity**

This type of validity shows how well results obtained from using a specific scale match theories (Sekaran, 2003). In other words, construct validity is an assessment of how well the research instrument measures the concept as it is supposed to be measured. Thus, items used in the research instrument should measure the whole range of the construct (Churchill and Brown, 2004). To admit
that the instrument has construct validity, the scale should measure and underline specific dimensions in question, and not some other dimensions, thereby providing a better understanding of the theoretical foundations underlying the measures.

This type of validity can be established by using two methods: convergent validity and discriminate validity. On the one hand, convergent validity means achieving high correlation scores between two scales measuring the same concept, i.e. high correlation between two different measures of the same construct. On the other hand, discriminate validity assumes that measures for two different concepts are not highly correlated with each other, i.e. there should be weak correlation between scales measuring different constructs. To demonstrate discriminate validity, the measures for the two different concepts or constructs should be at least marginally relevant to the situation, e.g. job satisfaction and job commitment.

After reviewing different types of validity, statistical books provide rich discussions about techniques for measuring and achieving validity, one of which is factor analysis. This is the most popular technique since it helps to confirm a number of dimensions that have been developed or defined for the concept. Thus, factor analysis forms a special technique of construct validity. The literature introduces two popular types of factor analysis technique: exploratory perspective (EFA) and confirmatory perspective (CFA). The first should be used at early stages of a study to define how many dimensions are needed for the construct, while the second can be used at the end of the research to confirm results or findings.

To run a factor analysis test, a researcher should follow the following stages and steps (Hair, Black, Babin, Anderson and Tatham, 2006; Tabachnick and Fidel, 2007):

- Identify the objective of the analysis, researcher has to choose between the data summarization objective, which aims to range items from the most detailed level to the most generalised level (grouping individual items into groups or dimensions), versus the data reduction objective, which attempts to
identify representative items within a large number of items, in order to create a new set much smaller than the original set of items.

- Select unit of analysis. Researcher has to choose the unit for analysis, which can be either items or respondents, in order to select a suitable technique. For example, if factor analysis aims to explore the correlation between items, *R factor analysis* should be applied.

- Check the suitability of data for analysis in terms of sample size. The researcher will not be able to run a factor analysis for a sample of fewer than 50 observations. However, statistical books suggest using 100 or more cases to ensure a sufficient analysis.

- Estimate the data matrix and check the suitability of data in terms of overall measures of inter-correlation. The researcher must insure that the data available provides a sufficient correlation matrix, i.e. there must be strong inter-correlation among the items. To do so, researcher should achieve the following criteria;
  1. The correlation matrix of the items should have coefficients greater than .30.
  2. Kaiser-Meyer-Olkin (KMO) test of sampling adequacy should be more than .60.
  3. Bartlett’s test of sphericity, which investigates the presence of correlation among items, should be significant (p<.05).

- Estimate the unrotated factor matrix of loadings, after choosing a suitable model for factor extraction (component factor versus common factor). In other words, this stage calculates the correlation between each item and all factors immerged in the matrix. Note that statistical books determine the significance level of correlation based on sample size.

Table 6.5 outlines the significant levels required based on sample size. As a result of this stage, the researcher will be able to identify a number of factors underlying the constructs, using different criteria including eigenvalues greater than 1.0, previous study findings, research objectives, percentage of variance, and scree test findings.
Table 6.5 Guidelines for Identifying Significant Factor Loadings based on Sample Size

<table>
<thead>
<tr>
<th>Factor loading</th>
<th>Sample size needed for significance</th>
</tr>
</thead>
<tbody>
<tr>
<td>.30</td>
<td>350</td>
</tr>
<tr>
<td>.35</td>
<td>250</td>
</tr>
<tr>
<td>.40</td>
<td>200</td>
</tr>
<tr>
<td>.45</td>
<td>150</td>
</tr>
<tr>
<td>.50</td>
<td>120</td>
</tr>
<tr>
<td>.55</td>
<td>100</td>
</tr>
<tr>
<td>.60</td>
<td>85</td>
</tr>
<tr>
<td>.65</td>
<td>70</td>
</tr>
<tr>
<td>.70</td>
<td>60</td>
</tr>
<tr>
<td>.75</td>
<td>50</td>
</tr>
</tbody>
</table>


- Rotate factors in order to regroup all items which achieved acceptable significant levels into factors that emerged from the unrotated matrix above. In other words, this stage shows which items related or loaded into the first factor, which items loaded into the second factor, and so on. In some cases, the researcher needs to repeat this process after deleting some items, in order to get a simpler and more theoretical meaning of factor analysis solutions.
- Label the factors when acceptable factor solutions have been obtained for all items. By this is step, the researcher gives meaning to the patterns of factor loadings, through giving names or labels to factors. The researcher should give accurate names that really reflect the factor implications and contents.

6.11.1.2 Reliability

This test identifies to what extent the scale developed is free from random error (Pallant, 2005). Therefore, such technique aims to provide a scale with consistent results across time, occasions, respondents, and even across items in the research instrument. In other words, this analysis tries to maintain stability and consistency of the scale (Sekaran, 2003, Churchill and Brown, 2004).
Research reliability has two features, stability and consistency. In terms of scale stability, two techniques have been developed: test-retest reliability and parallel-form reliability. Test-retest reliability is based on correlation between two sets of responses obtained at two different points of time from the same respondents. A reliable scale should have high correlations (.80 or more) between the two sets. To test parallel-form reliability, the scale can be assessed by calculating the correlation between two sets of scales measuring the same construct. To state it differently, this type of scale stability implies getting high correlation between two similar scales, in terms of items and response formats, with changes in wording and order of items and questions.

Scale consistency has two different techniques: inter-item (i.e. internal) consistency reliability, and split-half reliability. The most common technique used in the literature to assess the scale's reliability and stability is use of the Cronbach Alpha Statistic (Churchill, 1979; Peter, 1979; Pallant, 2005), which identifies to what extent items hang together as one set (Sekaran, 2003). Low Cronbach Alpha values mean that items don't capture the same construct, but high values of Cronbach Alpha indicate that items very well measure and reflect the construct. Ideally, Cronbach Alpha should be over .70 to produce a reliable scale (Cronbach, 1951), and any scale with Cronbach Alpha less than this standard should be eliminated. Finally, consistency of the scale can also be assessed through splitting the instrument into two halves; high correlation should be gained from the scores of the two halves of the scale to support a claim of its stability (Churchill, 1979; Sekaran, 2003).

6.11.2 Testing of the Research Model
For study 1 and 2, Correlation Analysis and Multiple Regression Analysis were used to test the nature of the relationship among variables and the impact between the variables. On the one hand, correlation analysis aims to determine the strength of association between variables (Churchill and Brown, 2004). On the other hand, the rationale for using the multiple regression analysis technique rose from the fact that this technique can be used when the research is interested in exploring the impact on a single dependent variable from several independent and mediating variables. As a result, the researcher will be able to predict and explain the dependent variable. In other words, this technique aims to predict variations in the dependent variable in response to the changes in a number of independent variables (Cohen, Cohen, West and Aiken, 2003; Field, 2005;
Methodology

Gujarati, 2003; Hair et al., 2006). However, this study will not ignore simple regression which aims only to investigate the nature of the relationship between one independent and one dependent variable (Churchill and Brown, 2004).

6.12 Conclusions

This chapter discussed some methodological steps required for running and conducting this study. At the beginning of this chapter, after displaying the research objectives, possible and potential research philosophies were discussed and compared against each other. According to the research aim and objectives, the positivism philosophy was selected.

Afterward, the proper research design for this research was selected after discussion of different options and alternatives. This study selected hypothesis testing rather than other designs introduced in the related literature. As another aspect of the research design, this study selected both longitudinal and cross sectional data collection methods. Therefore, this chapter identified what sources would be used for the research, i.e. both the hotel chain records and questionnaires.

This chapter also displayed the main findings of the preliminary study (part two) undertaken with hoteliers. Findings of the preliminary study confirmed the importance of service quality as a significant determinant of hotels’ profitability as well as the suitability of the research model developed in chapter 5 to the hotel industry. In other words, findings of the preliminary study (part two) approved findings of the literature concerning the link between service quality and profitability.

In addition, this chapter explained the measurements to be used for all variables in the two studies (Hotel Performance Data and General Managers’ Perspectives). Moreover, the methodology chapter highlighted sampling issues. Hence, this study targeted all units operating in a specific leading budget hotel chain in the UK. Finally, this chapter outlined what statistical techniques would be used. For scale purification purposes, this study selected only face validity and construct validity (EFA), plus inter-item consistency for reliability because measurement validity is often tested by construct validity and also Cronbach Alpha is considered a perfectly adequate index of scale reliability. Thus, the study used only two types of validity test and one of reliability, since it aims to test the
relationship between quality of service and profitability rather than developing or improving scales already developed and accepted in the literature. Hence, this study selected multiple regression analysis to test the relationships between all variables shown in the research model. Figure 6.1 summarises the process undertaken for doing the research.

As shown in the former figure, the study started with research model development, through revising theoretical and empirical studies related to this topic. Then, a qualitative study was undertaken as a preliminary study for testing the research model from the perspective of a small sample of financial managers. Next, the research model was be tested using two sets of data. The first data set was actual hotel performance data obtained from a leading budget hotel chain in UK covering 182 units. The second data set was
collected by distributing questionnaires to the general managers of 477 units in the same budget hotel chain. Finally, conclusions will be developed from data analysis of the two data sets, and the theoretical and empirical contributions of findings will be highlighted.
Chapter 7

Findings of Study 1

Hotel Performance Data
7.1 Introduction
This chapter deals with secondary data gathered and obtained from a leading budget hotel chain in the UK. To do so, section two describes the data obtained in terms of the nature of the data and how it was originally collected, the period covered by this data set, its suitability for analysis, and the normality of the data. Section three estimates initial strength and association between variables, using the correlation technique. Section four tests assumptions required for running multiple regression analysis. Section five runs the regression analysis in order to test the hypotheses developed. Section six discusses the findings of analysis while Section seven draws a conclusion.

7.2 Nature and Description of the Data
Data in this study was obtained from the Balanced Scorecard System used in the budget hotel chain. The main objective of this system, according to the company’s records, is to achieve high organisational performance. This system will let the top management of the hotel chain know how to take care of its people, whether their guests and customers had a great experience or not, if they intend to come back again and, finally, if investors are happy with the profits achieved. Thus, critical performance information is available every month for all units participating in this system.

The performance information in the Balanced Scorecard System is collected from all units in the chain every month. After doing so every month, all results are stored in the central Balanced Scorecard System in the hotel chain headquarters. Hence, this system adopted in the hotel chain provides an analytical tool to evaluate and track the performance of specific indicators every month for all sites participated.

This Balanced Scorecard System collects performance information regarding several aspects of performance, including both financial and non-financial indicators. To explain more, this system includes different measures regarding three major dimensions of performance including staff, guests and, finally, investors. These three major dimensions
are measured separately from one another. As a result, each dimension of performance will have a different score. A cumulative score is available for each dimension of performance at the end of the financial year, or up to last month. However, the Balanced Scorecard system also gives one single score derived from all dimensions of performance for each unit at monthly or yearly intervals i.e. one aggregate score is given for all scores of dimensions for each unit, and this score varies from 0% to 100%. Table 7.1 displays an example of the Balanced Scorecard System.

Table 7.1 Example of the Balanced Scorecard System for Unit X

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Measure</th>
<th>March</th>
<th>April</th>
<th>May</th>
<th>June</th>
<th>July</th>
<th>Aug</th>
<th>Sep</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
<th>Jan</th>
<th>Feb</th>
<th>Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>People</td>
<td>Team turnover</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Guests</td>
<td>Brand complian-c</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Guest recommen-dation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investors</td>
<td>Sales growth</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit growth</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Score</td>
<td>Total Score</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

As displayed in Table 7.1, the first month of the system is March every year. The above table shows the key three dimensions of performance measured in the system at the unit level. Points and sub-points below discuss the system.
1) **People:** this dimension of performance includes data about staff and employees working in each unit. This score in this dimension measures the staff's turnover. The score of this dimension refers to number of leavers (excluding fixed term contracts, retirement, deaths) as a percentage of total staff. The score is calculated every month by the general manager of each unit and sent to the central Balanced Scorecard System. The score for this dimension is grouped into three colours to give visual feedback about each unit. The colour green will be used if the score was less than the unit target, which means positive performance. The colour amber will be used if the score was higher than the unit target but still lower than the last year's score, which means acceptable performance. Finally, the colour red will be used if the score was higher than both the unit target and the last year's score which indicates very negative performance.

2) **Guests:** this dimension of performance has two parts. The first part measures service quality standards adopted in each unit using the evaluations of general managers of units and an auditing team. The second part measures the guests' desire to retain the same hotel and recommend it to others. Discussions below explain how this dimension of performance measured for these two sub-dimensions and how data is collected.

a) **Brand compliance:** this sub-dimension of performance refers to the extent to which some specific standards have been adopted in each unit. Thus, the brand compliance checks standards and features in different areas in the unit. The general manager of each unit, with support from the auditing team, evaluates the guest experience in the following elements:

- Pre-arriving booking.
- Arrival.
- First impression of team.
- First impression of reception.
- Check-in.
- Route to room.
- Great service.
- Night receptionist.
- Good night room.
- Breakfast.
Moreover, the general manager of each unit evaluates the operating standards performed in the unit. These standards relate to three areas: first, reception standards which focus on issues in the reception area such as payment, refunds, lost properties and so on, second, housekeeping standards which measure to what extent the areas are quiet and calm and not annoying to guests (in addition, the housekeeping standards monitor whether or not items were used safely and without waste by staff), third, extraordinary management which measures to what extent the management of each unit adopts the best practices policy such as to what extent staff are committed to standards and features, to what extent staff are well-trained, to what extent management can fix errors and mistakes in services and properties.

Scores in this sub-dimension (brand compliance) range from 0% to 100%. Moreover, scores are divided into three categories and colours: the colour green will be used if the total score of this sub-dimension was over 82.5%, which means good performance; the colour amber will be reported if the total score was larger than 80% but less than 82.5%; and the colour red will appear in the system if the total score was 79.9% or less, which indicates weak results.

b) **Guest recommendation:** each hotel unit distributes questionnaires monthly for guests before they leave the hotel. The questionnaires are then sent to the headquarters at the end of each month. This survey asks guests about their overall satisfaction and intention to retain the hotel brand and to recommend it to others.

However, it is worth noting that data obtained from the company’s system in this sub-dimension refer to the percentage of customers who are definitely going to recommend the brand name of the hotel chain to others. Scores are divided into three colours: green if the score was more than 42%, which means good performance; amber if the score was more than 35% but less than 42%; and the colour red will appear if the score was less than 35%.

3) **Investor:** this dimension measures the financial performance of all the units in the chain. This dimension has two sub-dimensions:
a) **Sales growth:** this sub-dimension measures the sales growth rate by calculating the sales achieved during each month in relation to sales achieved during the same month last year. The colour green will be used if the score was higher than the unit target, which means positive and promising performance; The colour amber will be reported if the score was less than the unit target but higher than the last year score which means satisfactory performance; and finally the colour red will appear if the score was less than the unit target and the last year score, which indicates very poor and negative performance.

b) **Profit growth:** this rate is used to measure financial performance by using the Return on Capital Employed ratio (ROCE). Clearly, the profit growth rate in this sub-dimension is produced by comparing the profit achieved during each month to the profit achieved in the same month last year. Similar to other measures in this system, scores are coloured to give a visual indicator of performance for all units. The colour green will be used if the score was more than the unit target; the colour amber will be reported if the score was less than the unit target but higher than the last year score, which indicates satisfactory performance; and the colour red will appear if the score was less than the unit target and last year’s score, which indicates very poor performance.

After explaining the nature of the Balanced Scorecard System and how the data was originally collected and organised in this system, the remainder of this section describes how the data was used for analysis in study one. This set of data covered 182 units over a 20 month time period from 2005 until 2006. As a result, this format of data from a panel data method, i.e. several time series for several cross sections (units) for different variables.

Balanced Scorecard Data available from the company measures some variables appearing in the research model. In other words, the available panel data doesn’t measure or cover all variables included in the research model. Therefore, Figure 7.1 displays a new simplified model developed in order to measure the relationship between service quality and profitability according to the data available in Study One (Hotel performance data).
The above figure displays a graphical representation for the indirect relationship between service quality and profitability similar to the original conceptual framework developed before. This simplified model suggests that service quality has a positive and indirect relationship with budget hotels’ profitability via two major simultaneous links. On the one hand, revenue expansion resulted from customers’ perceptions of service quality which led to more sales and a larger share of the market. On the other hand, revenue expansion resulted from higher prices, which in turn led to more profits.

To measure variables in the simplified research model by using the panel data available, service quality was measured by using the brand compliances data, customer retention measured by using the guest recommendation data, profitability measured by using the profit growth rate, market share measured by using the sales growth rate, and finally premium price measured by using the average room rate announced for each unit in 2005 and 2006.

Before starting the data analysis stage, some problems emerged from the data cleaning and organizing stages. There is one variable measured using two different methods in 2005 and 2006; customer retention was measured in 2005 by calculating the number of complaints divided by the number of rooms sold. In contrast, customer retention was measured in 2006 by calculating the number of customers who are planning to retain to same brand and recommend it to others. In other words, different methods were used for measuring the same variable which in turn led to different meanings and results for the same variable. Furthermore, scores (observations) for profit and sales growth variables were almost missing in 2005, since these measures require the previous year results.
Therefore, only data gathered in 2006 was used for testing the simplified conceptual framework in study one.

In early stages of the data analysis, different panel data analysis techniques were used, including pooled regression, random effects modelling and fixed effects modelling. These were conducted using different software packages suitable for panel data analysis, such as Stata, Pcgive, E-views, etc. Unfortunately, significant results were not obtained. The reason for this problem is attributed to the short time series available in the panel data, i.e. only eight time series were available for each unit or location in 2006 after excluding the data for 2005. However, significant panel data analysis requires 15 time series at least. To solve this problem, the mean value for each time series was calculated for each variable, for each unit or hotel, i.e. the average value was calculated for each variable across the eight months. As a result, a cross section data set was developed, created from the panel data, to overcome the previous problems. The SPSS software was used to test the simplified research model and the hypotheses formulated for linkages between variables, using the multiple regression analysis.

However, before running the analysis for the hypotheses testing, outliers were detected and removed by using the Boxplot charts for each variable. After this stage, numerical techniques or indicators of normality were tested; for example skewness and kurtosis show acceptable results as shown in Table 7.2. In other words, all of the figures below fall inside the range from -1 to +1 (Hair et al., 2006, p. 40).

<table>
<thead>
<tr>
<th>Variable</th>
<th>Skewness</th>
<th>Kurtosis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service quality</td>
<td>-.039</td>
<td>-.429</td>
</tr>
<tr>
<td>Customer retention</td>
<td>-.037</td>
<td>.016</td>
</tr>
<tr>
<td>Premium price</td>
<td>.936</td>
<td>.128</td>
</tr>
<tr>
<td>Sales growth</td>
<td>-.120</td>
<td>-.211</td>
</tr>
<tr>
<td>Profit growth</td>
<td>.171</td>
<td>-.320</td>
</tr>
</tbody>
</table>
7.3 Correlation Analysis

This analysis aims to measure the extent to which two variables are linearly associated. In other words, the correlation analysis implies to what extent the scatter graph of the relationship between two variables fits a straight line (Miles and Shevlin, 2001). However, the correlation coefficient (r) measures the strength of the association between each pair of variables: small correlation (r) = 0.10, medium correlation (r) = 0.30, large correlation (r) = 0.50 (Cohen, 1988). Table 7.3 displays the correlation matrix of variables.

<table>
<thead>
<tr>
<th>Variable</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Service quality</td>
<td></td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Customer retention</td>
<td>0.21**</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Premium price</td>
<td>0.24**</td>
<td>0.03</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Sales growth</td>
<td>0.09</td>
<td>0.17*</td>
<td>0.12</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>5. Profit growth</td>
<td>-0.04</td>
<td>0.12</td>
<td>-0.21*</td>
<td>0.59**</td>
<td>1</td>
</tr>
</tbody>
</table>

* Pearson correlation coefficients significant at the 0.05 level (2-tailed).
** Pearson correlation coefficients significant at the 0.01 level (2-tailed).

As shown in the above matrix, it can be easily recognised that the relationship between service quality and profitability was negative and not significant (r=-.04). As a result, it can be assumed that the relationship between service quality and profitability is indirect, and mediated by other variables as depicted in the research model. In order to track the indirect relationship, the correlation matrix indicated a positive and significant association between service quality and both customer retention (r=.21) and premium price (r=.24). However, premium price had a negative and significant correlation with profit growth which means premium prices charged in this hotel chain do not improve profits (r=-.21). Finally, it can be seen from the correlation matrix that sales growth was positively and significantly related to customer retention (r=.17) and with profit growth (r=.59).
7.4 Assumptions of Multiple Regressions

Before running the regression analysis, some assumptions must be assessed and checked, such as sample size, outliers, multicollinearity, and normality of residuals for dependent variables, as described in the following sections (Hair et al., 2006; Tabachnick and Fidel, 2007)

7.4.1 Sample Size

This assumption identifies how many cases are required for running a significant multiple regression analysis. Deciding the number of cases required depends on different criteria, including number of independent variables, Alpha level, and expected effect sizes (Tabachnick and Fidell, 2007). The literature suggests the minimum ratio of cases to independent variables should not fall below 5 to 1, i.e. five cases are needed for each independent variable. However, the larger sample size, the more generalisable are the regression results. Therefore, the most desirable size of sample is 15 to 20 cases for each independent variable. To solve this confusion, literature provides a very popular rule of thumb for testing the multiple regressions. This rule of thumb is \( N \geq 104 + m \) (where \( m \) is the number of independent variables). In this study, sample size was 182 which provide acceptable sample size for such analysis.

7.4.2 Absence of Outliers

At an early stage of analysis, this study deleted some outliers for variables to assure normal distribution of responses. Boxplot diagrams were used to identify extreme cases or points located out of range (i.e. very low and very high scores) which should be deleted. However, statistical books explained more sophisticated methods for exploring and dealing with outliers before running a multiple regression analysis. Tabachnick and Fidell (2007) identify the outlier as a case that has a residual of more than +3.3 or less than -3.3. Fortunately, standardised residual for cases in this research varied from -2.4 to +3.6 which means that data doesn’t have serious outliers. For other techniques aiming to explore outliers, Mahalanobis distance and Cook’s distance can be used. For the first test (Mahalanobis), a critical chi-square value suitable at this Alpha level of .001 should be equal to or less than 18.46. In this data set, there was no need to delete any cases since none exceeds this limit of chi-square. The second technique (Cook’s Distance) values should be less than 1. Fortunately, all cases have scores with less than 1 Cook’s distance value, in fact the maximum values varied between .000 and .084. Thus, it can be assumed
that available data doesn’t have serious outliers and can be considered eligible to run a multiple regression analysis.

7.4.3 Absence of Multicollinearity
Regression analysis attempts to avoid multicollinearity, i.e. two or more independent variables that are highly correlated and predicting each other (Hair et al., 2006). In other words, multicollinearity occurs when one independent variable has a perfect correlation coefficient \((r= 1)\) with another independent variable. Such a problem will affect the estimation and explanation. To put it another way, multicollinearity causes shared variances between independent variables, and reduces the unique variances for each one, which in turn leads to decreased predication power for the independent variables.

Three methods have been produced to assess and diagnose multicollinearity between independent variables. Firstly, the correlation matrix can be used as the simplest way to discover multicollinearity between independent variables. Coefficient correlation values of .90 or more imply multicollinearity. Secondly, the tolerance test forms another means for detecting multicollinearity. This technique measures the variance of a selected independent variable not explained by another independent variable. Therefore, the tolerance score should always be higher than .10 which means no collinearity. Thirdly and finally, the Variance Inflation Factor (VIF) provides the last way for assessing multicollinearity among independent variables. This test is an inverse method of Tolerance analysis. Thus, VIF should be low to confirm no collinearity, i.e. the value should be less than 10.

For this data set, the correlation matrix provides positive results. To put it another way, the correlations between all independent variables were lower than .90. In other words, results emerged from the correlation matrix supported the assumption that there is no multicollinearity effect between independent variables.

For the other techniques, Variance Inflation Factor (VIF) also indicates that there are no multicollinearity threats or problems. In other words, VIF values calculated for all independent variables were below the cut-off of 10 as suggested. In addition, tolerance values indicate that there is no serious multicollinearity between independent variables,
because the tolerance values for all independent variables were well above .10. Accordingly, there is no need to worry about multicollinearity for this data set.

7.4.4 Normality and Homoscedasticity Residuals
In regression models, assumptions of normality for dependent variables can be checked by using a normality probability plot of the regression standardised residuals (i.e. the differences between obtained and predicted scores of each dependent variable). As can be recognised in Figure 7.2, the residual of the dependent variable is normally distributed about the predicted dependent variable scores. To put it more simply, the residual points of the dependent variable are somehow having a straight-line relationship with predicted dependent variable scores (Tabachnick and Fidell, 2007).

Figure 7.2 Normal P-P Plot of Regression Standard of Residual of Dependent Variable

Figure 7.3 Scatter Plot of Regression Standardised Residual for Study 1
Figure 7.3 indicates acceptable homoscedasticity of the independent variable since the residual is rectangularly distributed. In other words, the scatter plot above shows that most of the scores are concentrated in the centre of the chart, i.e. there are no curves and no side higher than another side.

To conclude, all assumptions of regression were investigated and did not provide any violations that would affect the quality and reliability of results. Table 7.4 below summarises outcomes and results of all assumptions required for running the multiple regression analysis. There is no need to do any modification or purification more for the data available.

<table>
<thead>
<tr>
<th>Assumption</th>
<th>Test</th>
<th>Critical value</th>
<th>Actual value</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sample size</td>
<td>N ≥ 104 + m</td>
<td>108</td>
<td>182</td>
<td>Accepted</td>
</tr>
<tr>
<td>Outliers</td>
<td>Standard residual</td>
<td>-3.3 to +3.3</td>
<td>-2.4 to 3.6</td>
<td>Partially accepted</td>
</tr>
<tr>
<td>Mahal Distance</td>
<td>≤ 18.467</td>
<td>.267 to 11.873</td>
<td>Accepted</td>
<td></td>
</tr>
<tr>
<td>Cook's Distance</td>
<td>Less than 1</td>
<td>.00 to .084</td>
<td>Accepted</td>
<td></td>
</tr>
<tr>
<td>Multicollinearity</td>
<td>Tolerance</td>
<td>More than .10</td>
<td>--------------</td>
<td>Accepted</td>
</tr>
<tr>
<td>VIF</td>
<td>Less than 10</td>
<td>---------------</td>
<td>Accepted</td>
<td></td>
</tr>
<tr>
<td>Normality of residuals</td>
<td>Normal P-P plot</td>
<td>---------------</td>
<td>Accepted</td>
<td></td>
</tr>
<tr>
<td>Homoscedasticity of residuals</td>
<td>Scatter plot</td>
<td>---------------</td>
<td>Accepted</td>
<td></td>
</tr>
</tbody>
</table>

In term of overall model fitting, the results of multiple regression analysis indicate that independent and mediator variables explain and predict 35% of variances in the dependent variable (profit growth). To put it another way, 35% of the variance of the
overall profitability of hotels in the research sample is attributed to the independent and mediating impact included in the simplified research model. The $R^2$ value was low but still acceptable and significant ($p < .00$) especially for this sample size and the number of variables that emerged in the simplified research model.

### 7.5 Hypotheses Testing

The research hypotheses developed will be tested using Ordinal Leasing Square (OLS) regression analysis.

*The Impact of Service Quality on Customer Retention.* Figure 7.4 shows the graphical representation of hypothesis 1A.

**Figure 7.4 The Simplified Research Model: Testing Hypothesis 1A**

H1A There is a positive impact of service quality on customer retention.

**Table 7.5 OLS Regression Analysis: Predicting Customer Retention**

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service Quality</td>
<td>.21</td>
<td>2.90</td>
<td>.00</td>
<td>$F$ value $R^2$ p value</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>8.42 .05 .00</td>
</tr>
</tbody>
</table>

As displayed in Table 7.5, the beta value ($β: .21$) shows a positive and significant impact of service quality on customer retention. $R^2$ indicates the prediction and explanation power of service quality on customer retention which was .05. Finally, the p value is used to show whether service quality is making a significant impact on customer retention; if
the p value is less than .05, then the X variable is making a significant impact on the Y variable. As shown in the above table, the p value (.00) was less than .05. Therefore, this hypothesis is accepted.

The Impact of Service Quality on Premium Price. Figure 7.5 shows the graphical representation of hypothesis 1B.

**Figure 7.5 The Simplified Research Model: Testing Hypothesis 1B**

![Simplified Research Model](image)

H 1B: There is a positive impact of service quality on premium price.

**Table 7.6 OLS Regression Analysis: Predicting Premium Price**

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service Quality</td>
<td>.24</td>
<td>3.23</td>
<td>.00</td>
<td>10.44, .06, .00</td>
</tr>
</tbody>
</table>

As displayed in Table 7.6, beta value shows a significant effect of service quality on premium price (β: .24; p < .05). The R² value was poor (0.06); however, the hypothesis is accepted.
Findings of Study 1 (Hotel Performance Data)

The Impact of Service Quality on Sales Growth. Figure 7.6 shows the graphical representation of hypothesis 1C.

**Figure 7.6 The Simplified Research Model: Testing Hypothesis 1C**

H1C: There is a positive impact of service quality on sales growth.

**Table 7.7 OLS Regression Analysis: Predicting Sales Growth**

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service Quality</td>
<td>.09</td>
<td>1.08</td>
<td>.28</td>
<td>1.16 .01 .28</td>
</tr>
</tbody>
</table>

As displayed in Table 7.7, the beta value shows a positive but not significant impact of service quality on sales growth (β: .09; p > .05). The $R^2$ was .01. Therefore, this hypothesis is rejected.
The Impact of Service Quality on Profit Growth. Figure 7.7 shows the graphical representation of hypothesis 1D.

Figure 7.7 The Simplified Research Model: Testing Hypothesis 1D

H1D: There is a positive impact of service quality on profit growth.

Table 7.8 OLS Regression Analysis: Predicting Profit Growth

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service Quality</td>
<td>-.04</td>
<td>-.47</td>
<td>.64</td>
<td>.22</td>
</tr>
</tbody>
</table>

As displayed in Table 7.8, the beta value shows a negative and not significant influence of service quality on profit growth (β: -.04; p > .05). The $R^2$ was .00. According to this result, this hypothesis is rejected.
The Impact of Customer Retention on Premium Price. Figure 7.8 shows the graphical representation of hypothesis 2A.

Figure 7.8 The Simplified Research Model: Testing Hypothesis 2A

H2A: There is a positive impact of customer retention on premium price.

Table 7.9 OLS Regression Analysis: Predicting Premium Price

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Retention</td>
<td>.03</td>
<td>.43</td>
<td>.67</td>
<td>F value</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>R²</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>p value</td>
</tr>
</tbody>
</table>

As displayed in Table 7.9, the beta value shows a positive but not significant impact of customer retention on premium price (β: .03; p > .05). The R² was poor (.00). Hence, this hypothesis is rejected.
The Impact of Customer Retention on Sales Growth. Figure 7.9 shows the graphical representation of hypothesis 2B.

H2B: There is a positive impact of customer retention on sales growth.

As displayed in Table 7.10, the beta value shows a positive and significant impact of customer retention on sales growth ($\beta: .17; p < .05$). The $R^2$ was low (0.03); however, the hypothesis is accepted.
Findings of Study I (Hotel Performance Data)

The Impact of Service Premium Price on Profit Growth. Figure 7.10 shows the graphical representation of hypothesis 3.

**Figure 7.10 The Simplified Research Model: Testing Hypothesis 3**

H3: There is a positive impact of premium price on profit growth.

| Table 7 11 OLS Regression Analysis: Predicting Profit Growth |
|---------------------------------|----------------|-------------|----------------|
| Independent Variable | Standardised Coefficients ($\beta$) | t-value | p value |
| Premium Price | -0.21 | -2.56 | 0.01 |

<table>
<thead>
<tr>
<th>Overall Model Fit Statistics</th>
<th>F value</th>
<th>$R^2$</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>6.56</td>
<td>0.04</td>
<td>0.01</td>
</tr>
</tbody>
</table>

As displayed in Table 7.11, the beta value shows a negative and significant impact of premium price on profit growth ($\beta$: -21: $p < 0.05$). The $R^2$ was low as well (.04). According to the negative impact of the two variables, the hypothesis is rejected.
The Impact of Service Sales Growth on Profit Growth. Figure 7.11 shows the graphical representation of hypothesis 4.

**Figure 7.11 The Simplified Research Model: Testing Hypothesis 4**

![Diagram showing the research model with relationships between Service Quality, Premium Price, Customer Retention, Sales Growth, and Profit Growth marked as H1a, H1b, H2a, H2b, H3, H1c, H4, and their respective impacts (+).]

H4: There is a positive impact of sales growth on profit growth.

**Table 7.12 OLS Regression Analysis: Predicting Profit Growth**

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales Growth</td>
<td>.52</td>
<td>6.95</td>
<td>.00</td>
<td>48.33</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>.27</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>.00</td>
</tr>
</tbody>
</table>

As displayed in Table 7.12, the beta value shows a positive and significant impact of sales growth on profit growth (β: .52; p < .05). The R² was fairly good (.27). Hence, this hypothesis is accepted.
7.6 Discussion of Findings (Study 1)
The main finding of the first study supports the idea that service quality has an indirect impact on profitability. Hence, the empirical results of study 1 confirm that, as proposed before in the research model, there is no direct impact of service quality on profitability in the UK budget hotel sector but mediated by other variables including customer retention and market share.

Because the direct link was not significant and was rejected, the analysis was used to test relationships among variables by using serial sets of linear regression models between each two variables.

As reported in the hypotheses testing section, only four hypotheses out of seven were supported and accepted in this data set. In other words, many linkages hypothesized to be significant in the research model proved not to be statistically significant in this data set. However, there are positive and significant relationships between service quality, customer retention, sales growth and profit growth. To present it easily, Figure 7.12 highlights only the significant results obtained from study 1, while table 7.13 summarises all hypotheses tested in study 1.

**Figure 7.12 Final Model with Significant Paths for Study 1**

![Diagram](image-url)
Table 7.13 Summary of Hypotheses Testing for Study I

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Beta Value</th>
<th>P Value</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1A: There is a positive impact of service quality on customer retention.</td>
<td>.21</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H1B: There is a positive impact of service quality on premium price.</td>
<td>.24</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H1C: There is a positive impact of service quality on sales growth.</td>
<td>.09</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H1D: There is a positive impact of service quality on profit growth.</td>
<td>-.04</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H2A: There is a positive impact of customer retention on premium price.</td>
<td>.03</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H2B: There is a positive impact of customer retention on sales growth.</td>
<td>.17</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H3: There is a positive impact of premium price on profit growth.</td>
<td>-.21</td>
<td>P &lt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H4: There is a positive impact of sales growth on profit growth.</td>
<td>.52</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
</tbody>
</table>

Above Table and Figure show that only four hypotheses out of eight were supported and accepted in this data set. Results for H1A show that higher service quality has a direct positive influence on customer retention. This result is compatible with previous empirical evidence indicating that service quality has a positive and direct impact on different measures of behavioural intentions, including willing to return, to recommend to others, and to stay even if prices increased (Cronin and Taylor, 1992; Boulding et al., 1993; Zeithaml et al., 1996; Ennew and Binks, 1996; Danaher and Rust, 1996; Dabholkar et al., 2000; Cronin et al., 2000; Baker and Crompton, 2000; Tomas, Scott and Crompton, 2002; Choi, Cho, Lee, Lee and Kim, 2004). However, these previous studies suggested that service quality will have a stronger impact on customer behaviour through customer satisfaction i.e., the mediating impact of customer satisfaction on the relationship between service quality and customer retention is significant because service
quality refers to the evaluation of the service whereas customer satisfaction acts as a function of service quality.

Looking next at the result of H1B, it can be claimed that higher service quality has a positive impact on premium price i.e. higher service quality leads to prices higher than others. As discussed in the research model, theoretically, offering superior service quality provides the company several benefits and advantages such as the option to charge premium prices over competitors due to its quality. This finding is compatible with other findings and arguments made by Phillips et al (1983); Zeithaml (2000); Kimes (2001). Clearly, values obtained for H1B can be considered weak, which supports findings by Gerstner (1985) who reviewed the literature concerning the link between quality and price and concluded that the quality-price relationship is weak in general and is product-specific.

The results of H1C confirm that higher service quality does not have a positive impact on sales growth, which acts as one aspect or indicator of business performance. These results mean that increasing service quality will not lead directly to increased performance. Instead, the impact of service quality goes through sequential steps of interactions, including appraisal of service quality, affective response (customer satisfaction) and behavioural state. The result of this hypothesis is consistent with other studies which found that service quality does not improve business performance directly but needs more processes (Bagozzi et al., 1992; Babakus et al., 2004).

As in H1C, the findings for H1D indicate that higher service quality does not have a positive impact on profit growth. The results of H1D support the research model which supposed that service quality would have an indirect positive impact on profitability via other intervening variables such as the revenues mechanism and production/operational mechanism (Rust et al., 1995, 2002; Hardie, 1998; Lai and Cheng, 2005). These results do not follow those of previous studies which found a positive impact of service quality on profitability in different industries (Nelson et al., 1992; Kimes, 2001).

Service quality does not have a direct impact on business performance indicators such as sales growth and profit growth because cognitive and affective processes exist in this relationship. In other words, linking service quality directly to business performance
measures, while ignoring that lag effect of service quality, does not correctly represent that relationship. Efforts of service quality in the service sector are dealing with tangible as well as intangible aspects of quality and will not yield immediate financial gains (Rust et al., 1995; Babakus et al., 2004).

The results of H2B prove that higher customer retention as a result of high service quality will lead to higher sales and a larger market share by retaining a higher percentage of existing customers, attracting more customers through positive word of mouth and increasing the usage rates of existing customers. This result parallels findings by other studies supporting the indirect financial benefits and consequences of service quality (Rust and Zahorik, 1993; Anderson et al., 1994; Danaher and Rust, 1996).

For H3, there is a negative impact of premium price on profit growth; in other words, the higher the price, the less the profit growth. This result is not consistent with all theories suggesting that higher prices will increase margins as an outcome of high quality of services. However, Phillips et al (1983) indicates that the quality, price and profitability relationship is not clear and varies according to industry. One explanation for this result could be that the premium price will have a negative impact on occupancy rates, decreasing profits. Moreover, charging a premium price may require high costs and expenses to achieve high levels of service quality, leading to decreased margins and profits.

Finally, results for H4 indicate that higher sales growth will have a positive impact on profit growth. This result supports all previous hypotheses on the indirect behavioural and financial outcomes of service quality on profitability. Hence, this result is consistent with all studies discussing the link between market share and profitability (Schoeffler et al., 1974; Szymanski et al., 1993; Buzzell and Gale, 1987).

The beta and $R^2$ values for the accepted hypotheses were low compared to some previous studies, except the link between sales growth and profit growth. This weak relationship between the variables could be explained by a lag in the variables or because previous studies were conducted in different settings and industries. In other words, service quality might not have a strong direct impact on customer retention and, in turn, on sales growth because such effects take some time to manifest. Thus, the lag effect can diminish the
strength of the linkages among service quality, customer retention and sales growth. However, the results obtained in study 1 are still much higher than results from other studies such as an informative study by Babakus et al (2004) who found a very low $R^2$ value (.08%) for the impact of service quality, retention on store performance. However, this explanation does not apply to the impact of service quality on premium price since the budget hotel sector uses the low price policy; this is supported by Gerstner's findings (1985) that the impact of quality on price is varied across products and services and is weak in general.

7.7 Conclusions
The key contribution of this study emerges from the fact that the indirect impact of service quality on profit growth was supported and proved. The data analysis undertaken in this chapter indicates that the influence of service quality on sales growth and, in turn, profit growth was mediated by customer retention. Also, the analysis identifies the positive impact of sales growth on profit growth, whereas premium price had a negative impact in the budget hotel industry.

Thus, findings from the analysis in this chapter indicate that efforts aiming to improve service quality will have a positive impact on bottom line profits. This effect was achieved, however, through customer retention and hence sales growth. Maintaining contact with existing customers over time will therefore be important. A small concern arising from this chapter was that although high service quality will allow a hotel to charge a premium price, service quality improvements did not help budget hotels to improve profits because of the price sensitivity issue.
Chapter 8

Findings of Study 2
General Managers’ Perspective
Findings of Study 2 (General Managers' Perspective)

Chapter 8

Findings of Study 2
General Managers' Perspective

8.1 Introduction
This chapter aims to explain the relationship between service quality and profitability according to the general managers' perceptions. Suitable statistical techniques will be used, including descriptive analysis, validity, reliability, regression and correlation analysis to explore relationships between the variables. Section two starts with the demographic information of the hotels as well as a demographic profile of the respondents who participated in the survey. Section three provides a descriptive analysis for the items, and displays the normality statistics for the data which follows in section four. Section five runs an exploratory factor analysis for the service quality scale and the developed scales for managing demand and capacity. Section six measures the reliability of the scales. Section seven conducts a correlation for the data collected. Section eight tests the assumptions of the multiple regressions analysis before running the multiple regressions analysis in section nine in order to test hypotheses. Section ten retests the research model by using Post Hoc procedures. Section eleven reviews findings of the analysis. Section twelve gives conclusions for study 2.

8.2 Characteristics of the Sample
This section displays demographic information and characteristics of the respondents participated in this study. A questionnaire was sent to (477) general managers using online and post data collection methods. Total of (208) questionnaires were returned which means that the response rate was 43%. Four questionnaires were excluded due to missing answers and inconsistent responses. The following sections present the demographics of the hotels and the respondents who took part in the survey.
8.2.1 Characteristics of the Hotels

8.2.1.1 Location

This subsection shows the distribution of sample based on hotel locations. Figure 8.1 displays the location of hotels.

![Figure 8.1 Location of Hotels](image)

As shown in the above figure, the majority of hotels are located in the provincial town centre (25%) and in rural/countryside areas (20%). This result supports the fact that budget hotels are mostly located in provincial, rural and motorway areas for cost cutting reasons.
8.2.1.2 Years of Operation

Figure 8.2 illustrates years of hotels' operation.

![Figure 8.2 Years of Operations](image)

From the above figure, it can be observed that most hotels that participated in the survey had been working and operating in the market for 10 years or more (53%). In addition, a good proportion of the hotel (22%) had been operating between 4 and 6 years. Clearly, a small number of hotels (6%) had been operating less than 3 years.

8.2.1.3 Numbers of Rooms

Figure 8.3 indicates the number of rooms in hotels surveyed.
From Figure 8.3 it can be seen that the vast majority of hotels in the sample had between 26 and 100 rooms. A very small segment of the hotels in the sample located in the other classifications. Obviously, this result is supported with data available about the company.

8.2.1.4 Revenue Segmentation

Figure 8.4 illustrates revenue generated from different customer segments according to purpose of use.
According to Figure 8.4, the business traveller segment generates the biggest portion (67%) of the hotel revenues. Leisure travellers take the second rank (30%) in generating revenues for the hotels in the sample. Other segments and service generate just (3%) from the total revenues earned.

8.2.2 Demographic Characteristics of Respondents
The following subsections show briefly some demographic details about respondents who filled the questionnaires.

8.2.2.1 Gender
Figure 8.5 demonstrates the gender distribution of the sample.

As can be recognised from the above figure, the percentage of female respondents (69%) in the sample is higher than the male subjects (31%).

8.2.2.2 Age
Figure 8.6 reports the age grouping of the sample.
As shown in Figure 8.6, the majority of the respondents (54%) are between 20 and 34 years old. In addition, 25% of the respondents were in the second age group (35-44). A relatively small number of the respondents were assigned to the 56 years and more age group. The reason for such a high number of young people in the industry is attributed to the age of the budget hotels, which are still young in the UK. Moreover, the rapid growth of this industry forced hotels to attract young people to work in the industry.

8.2.2.3 Education

Figure 8.7 shows percentages of education level for individuals in the sample.
Findings of Study 2 (General Managers' Perspective)

College diploma/ professional qualifications got the highest percentage (53%) among subjects. This result agrees with the fact that people in the hospitality industry are not highly educated. However, a reasonable percentage of subjects (14%) and (11%) were categorized as highly educated staff, i.e. undergraduate and postgraduate degrees.

8.2.2.4 Years of Experience in this Hotel

Figure 8.8 shows years of experience in this hotel.

As shown above, (38%) of the subjects have 3 to 5 years experience at their current hotel. This result supports the previous result in the age subsection. In other words, the majority of the respondents in this budget hotel chain are young. However, (3%) of general managers are located in the final group (16 years and over) which confirms the fact that most managers and staff are still young in this hotel sector in general and in this hotel chain in particular.

8.2.2.5 Job Title

The current part of this analysis outlines the job titles for subjects taking part in the survey.
Figure 8.9 shows that (77%) of the respondents are general managers. The rest of respondents (23%) occupied different positions and different job titles (e.g. reception manager, food and beverage manager, and holding manager) due to delegation and empowerment policies and practices adopted in the industry. Clearly, the high percentage of general managers in the sample implies accurate and useful information for the research purpose.

8.2.2.6 Years of Experience at this Position

Figure 8.10 displays years of experience at this position for respondents.
Although the largest portion of respondents (30%) reported working at this position in the hotel industry for 3 to 5 years, the sample is fairly evenly distributed over other year groups. Consequently, the individuals surveyed in this sample can provide a valid and complete picture about the budget hotel sector in terms of facts, events and trends.

8.3 Descriptive Analysis
This section seeks to measure the respondents' perceptions and evaluations of variables and constructs investigated in the study. To do so, the next paragraphs show the mean and standard deviation values for all constructs, according to the order of questions in the questionnaire. All constructs were measured using a 5-point scale, except those items used for measuring business performance which had a 7-point scale. Therefore, items in general will have negative perception and evaluation if their mean scores are less than 3. If the mean scores are more than 3 and less than 3.5, the items will have a moderate assessment. Finally, the items will perceived more positively if their mean scores are greater than 3.5.

8.3.1 Brand Awareness
Table 8.1 below reports the mean and standard deviation for respondents' evaluations of guests' awareness of the hotel brand name.

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>How would you rate your guests' awareness of the hotel's brand name?</td>
<td>4.04</td>
<td>.72</td>
</tr>
</tbody>
</table>

From the above table, it can be understood that general managers thought that guests using this budget hotel chain were very aware of the hotel’s brand name, with a high mean score of 4.04 (SD=.72). In other words, respondents indicated that their guests were able to recall and recognise the hotel’s brand name among other competitor hotels' brand names. Basically, this result confirms that this hotel in particular has a strong and well known brand name from its customers' point of view.
8.3.2 Service Quality

Table 8.2 below summarises respondents’ perceptions of the two dimensions of service quality and their items.

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Physical Service Quality</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our decor is well co-ordinated.</td>
<td>3.81</td>
<td>.93</td>
</tr>
<tr>
<td>Our hotel has visually attractive rooms.</td>
<td>4.06</td>
<td>.92</td>
</tr>
<tr>
<td>Our hotel is tidy.</td>
<td>4.58</td>
<td>.62</td>
</tr>
<tr>
<td>Our hotel is clean.</td>
<td>4.65</td>
<td>.56</td>
</tr>
<tr>
<td><strong>Staff Behaviour and Attitude</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our team members anticipate the guests’ needs.</td>
<td>4.07</td>
<td>.73</td>
</tr>
<tr>
<td>Our team members are competent and display effortless expertise when serving the guests.</td>
<td>4.25</td>
<td>.70</td>
</tr>
<tr>
<td>Our team members listen carefully to the guests.</td>
<td>4.28</td>
<td>.71</td>
</tr>
<tr>
<td>Our team members are helpful and friendly.</td>
<td>4.51</td>
<td>.66</td>
</tr>
</tbody>
</table>

From the above table, it can be observed that the mean values for service quality items ranged between 3.81 and 4.65 with standard deviations between 0.56 and 0.93. The cleanliness of the hotel had the highest score at a mean of 4.65 (SD=0.56) on a five point scale. On the other hand, the coordination or organization of the hotel furniture and facilities had the lowest score at a mean of 3.81 (SD=0.93). In addition, it can be seen that the mean value for staff behaviour dimension, 4.28 (SD=.623) is slightly higher than that of physical quality dimension 4.27 (SD=.58).

8.3.3 Customer Satisfaction

This section explores to what extent respondents believe their customers and guests were satisfied at the overall level. Table 8.3 shows the mean and standard deviation values:
Table 8.3 Evaluation of Customer Satisfaction

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall, how would you rate the guests’ overall experiences with your hotel?</td>
<td>4.05</td>
<td>.56</td>
</tr>
</tbody>
</table>

The mean value of 4.05 (SD=.56) implies that respondents think overall satisfaction for customers and guests is fairly high.

### 8.3.4 Customer Retention

As mentioned in the methodology chapter, customer retention variable is measured using two items. Hence, Table 8.4 includes a calculated composite mean and standard deviation.

Table 8.4 Evaluation of Customer Retention

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall, how likely is that the guests will recommend this hotel to others?</td>
<td>4.00</td>
<td>.59</td>
</tr>
<tr>
<td>Overall, how likely is that the guests will return to this hotel?</td>
<td>4.17</td>
<td>.60</td>
</tr>
<tr>
<td>Overall customer retention scale</td>
<td>4.08</td>
<td>.55</td>
</tr>
</tbody>
</table>

It can be seen that both items for measuring customer retention were rated highly (positively). On the one hand, the intention for guests to return to this hotel got a higher value with a mean of 4.17 (SD=.60) than the intention to recommend this hotel to others (4.00 with SD=.59). On the other hand, the overall rating of this variable was also relatively high with a mean value of 4.08 (SD=.55). This result implies that respondents assume customers and guests are loyal, and will both return and give favourable words about this hotel.

### 8.3.5 Premium Price

Table 8.5 below summarises the mean and standard deviation of the premium price perceived upon customers and guests from the general managers’ perspective.
From Table 8.5, it can be recognised that the mean value and standard deviation for the customers' perceptions of price paid for their accommodation was moderate, with a mean score of 3.32 (SD=.92) on a five-point scale of 1 to 5, where 1=lower than similar hotels and 5=higher than similar hotels. In other words, respondents believe that customers and guests did not pay a high or premium price for their accommodation compared to similar hotels in the same area and within the same hotel segment or classification.

8.3.6 Business Performance
Table 8.6 below displays the mean and standard deviation values for different indicators of business performance for the hotels. The items used for measuring business performance indicators were rated using a 7-point scale. Rating 1 indicates that the hotel is performing much worse than similar hotels, and rating 7 that it is performing much better than similar hotels from the general managers' perceptions.
<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>How would you rate your hotel's labour productivity in the last 3 years against similar hotels in the same area?</td>
<td>5.24</td>
<td>1.14</td>
</tr>
<tr>
<td>How would you rate your hotel's revenue per available room (REVPAR) in the last 3 years against similar hotels in the same area?</td>
<td>5.30</td>
<td>1.13</td>
</tr>
<tr>
<td>How would you rate your hotel's profitability measured by return on capital invested (ROCE) in the last 3 years against similar hotels in the same area?</td>
<td>5.31</td>
<td>1.20</td>
</tr>
<tr>
<td>How would you rate your hotel's occupancy in the last 3 years against similar hotels in the same area?</td>
<td>5.39</td>
<td>1.25</td>
</tr>
<tr>
<td>How would you rate your hotel's market share in the last 3 years against similar hotels in the same area?</td>
<td>5.40</td>
<td>1.27</td>
</tr>
<tr>
<td><strong>Overall business performance scale</strong></td>
<td>5.32</td>
<td>1.02</td>
</tr>
</tbody>
</table>

From the above table, it can be observed that the mean values for business performance indicators ranged between 5.24 and 5.40 with standard deviations between 1.13 and 1.27. The market share of the hotels had the highest score at a mean of 5.40 (SD=1.27), while labour productivity of the hotel was rated lowest with a mean of 5.24 (SD=1.14). Available performance data about this chain indicates that it has a very big market share which supports the questionnaire results. Moreover, this result confirms that labour productivity is low in the hospitality industry. The overall rating of business performance indicators was good with a mean of 5.32 (SD=1.02).
8.3.7 Managing Demand and Capacity

This section presents the mean and standard deviation values for subjects’ scores for the managing demand and capacity scale. Table 8.7 summarises the values. It can be noticed that the mean values ranged between 1.62 and 4.46 with standard deviations between 0.82 and 1.47. No discount policy (charging the full price) was the highest rated item with a mean of 4.46 (SD=0.93) on a scale of 1 to 5, where 1=strongly disagree and 5=strongly agree. On the other hand, renting of equipment at peak times was rated lowest score, with a mean of 1.62 (SD=0.82).

Table 8.7 Evaluation of Managing Demand and Capacity

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>In this hotel, we rent equipment at times of peak demand, e.g. we rent LCD projectors for business travellers.</td>
<td>1.62</td>
<td>.82</td>
</tr>
<tr>
<td>In this hotel, we offer discounts during slow periods.</td>
<td>2.34</td>
<td>1.33</td>
</tr>
<tr>
<td>In this hotel, we modify the service offering in the slow seasons to attract new market segments, e.g. we rent rooms for film, advertisement or report producers.</td>
<td>2.35</td>
<td>1.21</td>
</tr>
<tr>
<td>In this hotel, we hire part-time employees during peak demand.</td>
<td>2.70</td>
<td>1.34</td>
</tr>
<tr>
<td>In this hotel, we increase advertisements during slow periods.</td>
<td>2.89</td>
<td>1.19</td>
</tr>
<tr>
<td>In this hotel, we reduce hours of operation during off-peak periods.</td>
<td>2.89</td>
<td>1.47</td>
</tr>
<tr>
<td>In this hotel, we communicate with guests to inform them about times of peak and slow demand.</td>
<td>3.19</td>
<td>1.21</td>
</tr>
<tr>
<td>In this hotel, we train employees in the periods of slow demand.</td>
<td>3.38</td>
<td>1.12</td>
</tr>
<tr>
<td>In this hotel, we work overtime at times of peak demand</td>
<td>3.59</td>
<td>1.22</td>
</tr>
<tr>
<td>In this hotel, we charge full prices during peak periods i.e. no discounts.</td>
<td>4.46</td>
<td>.93</td>
</tr>
</tbody>
</table>
8.4 Normality of the Data

Due to the nature of the constructs being investigated and measured in this study, scores obtained and presented in the descriptive analysis were normally distributed with positive direction for curves. In other words, the data gathered is located in the centre in general but to some extent oriented toward the positive side. However, some outliers were deleted using the Boxplot figures to improve distribution of data. Values of skewness and kurtosis (measures used to describe the shape of distribution) presented in Table 8.8 below demonstrate that the data collected is normally distributed, since most of the figures fall inside the range of -1 to +1 (Hair et al., 2006, p. 40).
As shown in Table 8.8, the majority of the values were between -1 and +1 except three items even after deleting some outliers but researcher couldn’t do any more deleting for cases. Thus, the data gathered can be considered normally distributed after removing outliers. To put it another way, skewness values, which indicate the symmetry of distribution, and kurtosis values, which refer to the peakedness of distribution, did not exceed normal levels (Pallant, 2005).
8.5 Construct Validity of the Scales (Exploratory Factor Analysis)

The factor analysis technique (construct validity) is considered the best solution to purify any scale. In other words, to identify the number of dimensions underlying any construct, a factor analysis should be used. The factor analysis technique may add new dimensions or reduce them, through grouping intercorrelated items into distinct sets of factors (Churchill, 1979). As a result of using this technique, the researcher will be able to understand the building blocks of the constructs and explore interrelationships among a large number of dimensions (Hair et al., 2006). The sections below will undertake factor analysis for the service quality scale and managing demand and capacity scales.

8.5.1 The Service Quality Scale

As mentioned, this analysis tries to determine the structure of constructs. Therefore, this section aims to underline the dimensions that compose the service quality construct, to determine whether the two dimensions of the service quality scale developed by Ekinci (2001) properly capture it. Although the literature has extensively and deeply developed and discussed the service quality scale's reliability and validity issues, this section will reassess that validity by exploratory factor analysis because Ekinci's scale traditionally uses the customers' perspective of service quality to measure the service quality construct. In contrast, this study uses the general managers' perspectives of service quality.

A correlation matrix for the items is displayed in Table 8.9 to show the suitability of the data for factor analysis.

Table 8.9 Correlation Matrix of the Service Quality Scale

<table>
<thead>
<tr>
<th>Statement</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Decoration</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Cleanness</td>
<td>.31</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Tidiness</td>
<td>.27</td>
<td>.71</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Attractiveness</td>
<td>.48</td>
<td>.43</td>
<td>.40</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Effortlessness</td>
<td>.17</td>
<td>.42</td>
<td>.32</td>
<td>.33</td>
<td>.68</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Anticipation</td>
<td>.08</td>
<td>.33</td>
<td>.22</td>
<td>.21</td>
<td>.68</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Helpfulness</td>
<td>.12</td>
<td>.51</td>
<td>.35</td>
<td>.31</td>
<td>.70</td>
<td>.68</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>8. Carefulness</td>
<td>.11</td>
<td>.41</td>
<td>.29</td>
<td>.25</td>
<td>.67</td>
<td>.67</td>
<td>.80</td>
<td>1.00</td>
</tr>
</tbody>
</table>

According to the matrix, all coefficient values are over .30; therefore, there is no need to delete any item in order to improve the suitability of the data for factor analysis. In addition,
the Kaiser-Meyer-Olkin (KMO) value was .82 which indicates that the data are acceptable for factor analysis. Finally, the value of Bartlett’s Test of Sphericity was significant at .00. Thus, all tests for assessing the adequacy of data for factor analysis were acceptable.

In order to determine how many factors should be extracted the Eigenvalue test and the Scree Plot analysis displayed in Figure 8.11 are used. In other words, the figure identifies how many factors underlie the service quality construct. The Eigenvalue test indicates that two factors can be extracted to capture the service quality variable, since the first two components achieved acceptable Eigenvalue scores, i.e. values greater than 1 (3.99 and 1.55), to explain 49.5% and 19.3% of the variances respectively.

![Figure 8.11 Scree Plot Analyses for the Service Quality Scale](image)

The following part of the factor analysis regrouped items into the two dimensions (factors) extracted and identified in the previous tests. In other words, the objective of this process is to explore and interpret the association between each item and each factor. Therefore, VARIMAX rotation is used as displayed in Table 8.10.
Table 8.10 VARIMAX-Rotated Component Analysis Factor Matrix for the Service Quality Scale

<table>
<thead>
<tr>
<th>Statement</th>
<th>Component</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Factor (1)</td>
<td>Factor (2)</td>
</tr>
<tr>
<td><strong>Staff Behaviour &amp; Attitude</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Carefulness</td>
<td>.88</td>
<td></td>
</tr>
<tr>
<td>2. Helpfulness</td>
<td>.88</td>
<td></td>
</tr>
<tr>
<td>3. Anticipation</td>
<td>.85</td>
<td></td>
</tr>
<tr>
<td>4. Effortlessness</td>
<td>.82</td>
<td></td>
</tr>
<tr>
<td><strong>Physical Service Quality</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Attractiveness</td>
<td>.75</td>
<td></td>
</tr>
<tr>
<td>6. Tidiness</td>
<td>.74</td>
<td></td>
</tr>
<tr>
<td>7. Decoration</td>
<td>.72</td>
<td></td>
</tr>
<tr>
<td>8. Cleanness</td>
<td>.72</td>
<td></td>
</tr>
</tbody>
</table>

Variance extracted by the two factors is 68.9%. The first factor explains (staff behaviour & attitude) 49.5% of variances and the second factor (physical service quality) explains 19.3% of variances.

As can be seen from Table 8.10, factor loadings indicate a high level of association between items and the two derived factors. As mentioned in the methodology chapter, the significant value for loading in this study is .40 or greater, according to the research sample size; in fact, all items have more than a .70 loading level. Thus, it is confirmed that service quality has two components or factors. The first factor (staff behaviour and attitude) explains 49.5% of variances. The second factor (physical aspect of service quality) explains 19.3% of variances. To conclude, this two dimensional scale explains 68.9% of variance.

8.5.2 The Demand and Capacity Management Scale

In order to underline the dimensions of this construct, a component factor analysis will be undertaken, since the literature hasn’t yet developed any scale for it. In other words, there is no scale in the service literature for measuring the ability of a service firm to manage demand and capacity. Therefore, this research developed a scale for such measurement, with 10 items. This study proposed 3 dimensions for managing demand and another 3 dimensions for managing capacity, i.e. 6 dimensions in total. However, the factor analysis below will check the dimensionality of the construct in order to validate the developed scale. A correlation matrix for the 10 items will be presented in Table 8.11 to show the suitability of the data.
### Findings of Study 2 (General Managers' Perspective)

#### Table 8.11 Correlation Matrix of the Demand and Capacity Management Scale

<table>
<thead>
<tr>
<th>Statement</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Charge full prices</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Modify services</td>
<td>-0.06</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Increase AD</td>
<td>0.06</td>
<td>0.38</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Offer discounts</td>
<td>-0.20</td>
<td>0.48</td>
<td>0.33</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Communications</td>
<td>-0.02</td>
<td>0.23</td>
<td>0.30</td>
<td>0.29</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Part-time staff</td>
<td>0.05</td>
<td>0.06</td>
<td>0.14</td>
<td>0.11</td>
<td>0.12</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Rent equipments</td>
<td>-0.01</td>
<td>0.25</td>
<td>0.23</td>
<td>0.31</td>
<td>0.15</td>
<td>0.27</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Work Overtime</td>
<td>-0.04</td>
<td>-0.07</td>
<td>0.11</td>
<td>0.04</td>
<td>0.07</td>
<td>0.08</td>
<td>0.03</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. Train employees</td>
<td>0.02</td>
<td>0.15</td>
<td>0.14</td>
<td>0.12</td>
<td>0.19</td>
<td>0.18</td>
<td>0.15</td>
<td>0.22</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>10. Reduce hours</td>
<td>0.00</td>
<td>-0.00</td>
<td>0.01</td>
<td>0.03</td>
<td>0.11</td>
<td>-0.01</td>
<td>0.08</td>
<td>0.10</td>
<td>0.18</td>
<td>1.000</td>
</tr>
</tbody>
</table>
As shown, the data correlation matrix shows weak correlation between items, especially for items 2 and 8, i.e. most of the coefficients in the matrix are less than .30. However, the Kaiser-Meyer-Olkin (KMO) test shows an acceptable value of .69 which means that the data is adequate for running a factor analysis. Also, the value of Bartlett’s Test of Sphericity was significant at .00. Thus, two tests required for assessing the adequacy of data for factorability indicated that it was acceptable and significant.

In order to determine how many factors should be extracted, the Eigenvalue test and the Scree Plot analysis displayed in Figure 8.12 show how many factors underlie this construct. After performing the Eigenvalue test, four factors can be extracted to capture the managing demand and capacity variable, because the first four component’s Eigenvalues were over 1 (2.43, 1.33, 1.11 and 1.00) explaining 24.3 %, 13.3 %, 11.1 % and 10 % of the variances respectively.

Figure 8.12 below shows how many dimensions or factors should be extracted. The line starts straightening at the third factor, which means three factors should be extracted; however, the number of factors with minimum Eigenvalues of 1 is four, which implies that the factor analysis extraction should stop after the fourth factor. The four factor solution will be used instead of the three factor solution.

Figure 8.12 Scree Plot Analyses for the Demand and Capacity Management Scale
The following part of the factor analysis aims to regroup items into the four dimensions (factors) extracted and identified. The objective of this process is to explore and interpret associations between each item and each factor. To do so, VARIMAX rotation is used as displayed in Table 8.12.

### Table 8.12 VARIMAX-Rotated Component Analysis Factor Matrix for the Demand and Capacity Management Scale

<table>
<thead>
<tr>
<th>Statement</th>
<th>Component</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Factor (1)</td>
</tr>
<tr>
<td><strong>Controlling guest’s usage</strong></td>
<td></td>
</tr>
<tr>
<td>1. Modify services</td>
<td>.787</td>
</tr>
<tr>
<td>2. Offer discounts</td>
<td>.711</td>
</tr>
<tr>
<td>3. Increase advertisement</td>
<td>.670</td>
</tr>
<tr>
<td>4. Communications</td>
<td>.571</td>
</tr>
<tr>
<td><strong>Scheduling workforce</strong></td>
<td></td>
</tr>
<tr>
<td>5. Reduce hours</td>
<td>.664</td>
</tr>
<tr>
<td>6. Work overtime</td>
<td>.649</td>
</tr>
<tr>
<td>7. Train employees</td>
<td>.632</td>
</tr>
<tr>
<td><strong>Outsourcing activities</strong></td>
<td></td>
</tr>
<tr>
<td>8. Part-time staff</td>
<td></td>
</tr>
<tr>
<td>9. Rent equipments</td>
<td></td>
</tr>
<tr>
<td><strong>Pricing</strong></td>
<td></td>
</tr>
<tr>
<td>10. Charge full prices</td>
<td></td>
</tr>
</tbody>
</table>

Variance extracted by the four factors is 58.7%. The first factor explains 24.3% of variances; the second factor explains 13.3% of variances; the third factor explains 11.1% of variances and the fourth factor explains 10% of variances.

As can be seen in Table 8.12, factor loadings indicate a high level of association between the items and the four derived factors. As mentioned before in the methodology chapter, the significant value for loading in this study is .40 or greater, based on the research sample size. The actual item loading values vary between .571 and .930. Therefore, managing demand and capacity’s items will be grouped as follows:

The first factor explains 24.3% of the variances. These items represent the ability of the hotel to attract and encourage guests and customers to visit and use the hotel in peak and slow periods, through using different techniques such as giving discounts, increasing advertisements, increasing direct contact with guests, and modifying the nature of services for
new or different users. This factor forms the first dimension of managing demand and capacity, and will be called controlling guest’s usage.

The second factor comprises different items that explain 13.3% of the variances. These items imply the ability of the hotel to manage working hours for staff in peak and slow periods through adopting several techniques, for instance asking staff to work overtime, reducing the operations hours and training employees during the slow times. Therefore, this factor implies the second dimension of managing demand and capacity and will be called workforce scheduling.

The third factor explains 11.1% of variances. These two items refer to outsourcing policy or strategy. In other words, the combined items refer to the ability of the hotel to get capacity from outside the company. Item 6 deals with hiring part-time staff, item 7 with renting equipment from others. Therefore, this factor implies the third dimension of managing demand and capacity and will be renamed outsourcing activities.

Finally, the fourth factor consists of only one item that explains 10% of variances. This item pertains to the pricing policy of charging higher prices during peak times. So, this factor acts the fourth dimension of managing demand and capacity and will be called price policy.

To sum up, the total variance explained by the four factors (dimensions) is 58.7%.

8.6 Reliability of the Scales
A reliability test should considered one of the essential tests for purifying the scale after identifying dimensions of the construct. Basically, reliability of the scale refers to the degree of consistency among several items. A reliable scale means that the items are highly intercorrelated and measure the same thing (Hair et al., 2006). As a result, the objective of running the analysis is to ensure that the scale has low error and to provide an indication of consistency across time and across different items of the scale (Sekaran, 2003). As mentioned before, this study is going to use the Cronbach Alpha for assessing internal consistency of the scale.
8.6.1 The Service Quality Scale

Having identified the two dimensions of service quality (physical service quality and staff behaviour and attitude), this section aims to check the reliability of the two service quality scales. Table 8.13 displays the Cronbach Alpha Coefficients and item to total correlations.

<table>
<thead>
<tr>
<th>No</th>
<th>Item</th>
<th>Cronbach Alpha</th>
<th>Item to total correlation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Our decor is well co-ordinated.</td>
<td>.71</td>
<td>.44</td>
</tr>
<tr>
<td>2</td>
<td>Our hotel is clean.</td>
<td></td>
<td>.56</td>
</tr>
<tr>
<td>3</td>
<td>Our hotel is tidy.</td>
<td></td>
<td>.54</td>
</tr>
<tr>
<td>4</td>
<td>Our hotel has visually attractive rooms.</td>
<td></td>
<td>.55</td>
</tr>
<tr>
<td></td>
<td><strong>Physical Service Quality</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>Our team members are competent and display effortless expertise when serving the guests.</td>
<td></td>
<td>.76</td>
</tr>
<tr>
<td>6</td>
<td>Our team members anticipate the guests' needs.</td>
<td></td>
<td>.75</td>
</tr>
<tr>
<td>7</td>
<td>Our team members are helpful and friendly.</td>
<td></td>
<td>.82</td>
</tr>
<tr>
<td>8</td>
<td>Our team members listen carefully to the guests.</td>
<td></td>
<td>.80</td>
</tr>
<tr>
<td></td>
<td><strong>Staff Behaviour and Attitude</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

It can be seen from the above table that the internal consistency of the two service quality scales is acceptable, i.e. the Cronbach Alpha values for the two scales exceeds the recommended criterion (Alpha = .70). In addition, item to total correlations exceed .50. Therefore, it is confirmed that this scale is reliable for measuring service quality.

8.6.2 The Demand and Capacity Management Scale

Table 8.14 displays Cronbach Alpha scores and item to total correlations for the three dimensions of the demand and capacity management scale.
Table 8.14 Reliability of the Demand and Capacity Management Scale

<table>
<thead>
<tr>
<th>No</th>
<th>Item</th>
<th>Cronbach Alpha</th>
<th>Item to total correlation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>In this hotel, we modify the service offering in the slow seasons to attract new market segments, e.g. we rent rooms for film, advertisement or report producers.</td>
<td>.67</td>
<td>.50</td>
</tr>
<tr>
<td>2</td>
<td>In this hotel, we offer discounts during slow periods</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>In this hotel, we increase advertisements during slow periods.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>In this hotel, we communicate with guests to inform them about times of peak and slow demand.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Outsourcing activities</strong></td>
<td>.39</td>
<td>.27</td>
</tr>
<tr>
<td>5</td>
<td>In this hotel, we hire part-time employees during peak demand.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>In this hotel, we rent equipment at time of peak demand e.g. we rent LCD projector for business travellers.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>In this hotel, we reduce hours of operation during off-peak periods.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>In this hotel, we work overtime at times of peak demand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>In this hotel, we train employees in the periods of slow demand.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>In this hotel, we charge full prices during peak periods i.e. no discounts.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 8.14 summarises reliability results for the items related to managing demand and capacity. For the first dimension (controlling guest’s usage), the Cronbach Alpha was .67, which was less than the recommended level (.70). However, the scale for the first dimension is still considered reliable for several reasons. The actual score of Cronbach Alpha was close to the recommend score (.70). Item to item correlation values were over .30. Deleting items would not improve the scale reliability, i.e. the maximum Alpha is obtained with this set of items. In the exploratory level of scaling, internal consistency can be achieved at a Cronbach Alpha value of .60. Finally, the Cronbach Alpha value is influenced by the number of items, i.e. a small number of items leads to a low Cronbach score.

In terms of reliability for the second dimension (outsourcing activities), results show a very weak and negative reliability result (.39). In addition, the third dimension (scheduling workforce) got a very low score. Therefore, the current research will drop these two dimensions and will not use their items in the final scale, because they had very low coefficients. To put it more simply, the items used to measure the second and third dimensions are not reliable for that purpose. Finally, this study will drop the pricing policy.
dimension, because it is not possible to test reliability with only one item loaded from the factor analysis stage.

To conclude, the measuring demand and capacity construct will be measured only by using the items related to the first dimension (2, 4, 3 and 5), i.e. only the items considered reliable at this level of Cronbach Alpha. The items for measuring the other dimensions will be excluded from the final scale.

According to the validity and readability results of the management demand and capacity scale, it is found that this scale is valid but not reliable except in the first dimension. The exploratory factor analysis recommended four factors for the managing demand and capacity scale, but the scale may have proven unreliable in the other dimensions because the consistency of the answers was poor, since not all managers of units adopt and use these techniques and practices for managing demand and capacity in their units. This justification for the contradictory results would imply that the scale really does not capture perfectly the practices for managing demand and capacity in the hotel industry.

8.7 Correlation Analysis

The correlation analysis measures how well the independent variables go with or are related to the dependent variable. Thus, this analysis provides a brief indication of the direction and strength of relationships between variables. The result values of this analysis vary from -1 to +1, where a correlation of +1 indicates an excellent positive association between variables, and a correlation of -1 indicates an excellent negative relationship. A correlation of .00 means there is no relationship at all (Wright, 2002). Although such analysis does not imply causation, it will be used in this study to give preliminary results about the relationships between variables in the research model. The correlation matrix calculated in Table 8.15 reports the direction of relationship, size (strength), and significant level of association between independent, mediate, moderate and dependent variables that emerged and were discussed earlier in the research model chapter.

Correlation analysis was undertaken for the general manager’s sample only to check if there were any differences of results compared to the whole sample (general managers and other managers). Similar results obtained in terms of strength and directions of association between variables. Thus, the following correlation matrix shows results obtained from the whole sample (general managers and other managers).
## Chapter 8

Findings of Study 2 (General Managers’ Perspective)

### Table 8.15 Correlation Matrix of Variables for Study 2

<table>
<thead>
<tr>
<th>Variable</th>
<th>Scale Mean</th>
<th>S.D.</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ1-Physical Quality</td>
<td>4.27</td>
<td>.59</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SQ2-Staff Attitude</td>
<td>4.28</td>
<td>.62</td>
<td>.40**</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall CS</td>
<td>4.08</td>
<td>.49</td>
<td>.25**</td>
<td>.20**</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall CR</td>
<td>4.12</td>
<td>.50</td>
<td>.19**</td>
<td>.12</td>
<td>.47**</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premium Price</td>
<td>3.34</td>
<td>.90</td>
<td>.05</td>
<td>.03</td>
<td>.22**</td>
<td>.10</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Productivity (Occupancy)</td>
<td>5.46</td>
<td>1.17</td>
<td>.05</td>
<td>.08</td>
<td>.12</td>
<td>.11</td>
<td>.08</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Productivity (Labour Productivity)</td>
<td>5.25</td>
<td>1.10</td>
<td>.05</td>
<td>.19**</td>
<td>.06</td>
<td>-.01</td>
<td>.00</td>
<td>.48**</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Market share</td>
<td>5.47</td>
<td>1.19</td>
<td>.18*</td>
<td>.10</td>
<td>.15*</td>
<td>.17*</td>
<td>.16*</td>
<td>.77**</td>
<td>.43**</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profitability (ROCE)</td>
<td>5.37</td>
<td>1.13</td>
<td>.09</td>
<td>.04</td>
<td>.02</td>
<td>-.01</td>
<td>.06</td>
<td>.58**</td>
<td>.63**</td>
<td>.61**</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profitability (REVPAR)</td>
<td>5.33</td>
<td>1.08</td>
<td>.08</td>
<td>-.01</td>
<td>.11</td>
<td>.10</td>
<td>.07</td>
<td>.81**</td>
<td>.50**</td>
<td>.73**</td>
<td>.66**</td>
<td></td>
</tr>
</tbody>
</table>

* Pearson correlation coefficients significant at the 0.05 level (2-tailed).

** Pearson correlation coefficients significant at the 0.01 level (2-tailed).
Findings of Study 2 (General Managers' Perspective)

From Table 8.15 can be seen the relationship between service quality and profitability. The correlation matrix shows a positive and very weak relationship between the two dimensions of service quality and all indicators of profitability, including return on capital employed (ROCE) and revenue per available room. To put it simply, the Pearson Correlation Coefficients for the links between the first dimension of service quality (Physical quality) and both indicators of profitability (ROCE and REVPAR), respectively, were .09 and .08. On the other hand, the second dimension of service quality (Staff behaviour and attitude) was positively and negatively correlated with both measures of profitability (r = .04 and r = -.01, respectively) with a p value that was not significant. Therefore, it was found, as supposed in the research model, that service quality doesn’t have a direct relationship with the financial business performance of hotels.

It is also anticipated that the indirect outcomes of service quality lead to positive correlation between customer retention and market share. That is, positive and significant correlation obtained between customer retention and market share (r = .17). However, a small value of Pearson correlation may occur due to the fact that some other factors can influence the market share of hotels, as measured by number of rooms sold in a specific market and time. So, this link will be explained and justified later in the regression analysis.

As expected from the research model, market share was positively correlated with both indicators of financial business performance, ROCE and REVPAR (r = .61, r = .73). There is no doubt that market share forms an input for profitability indicators.

From Table 8.15, it was surprising to see that both dimensions of service quality had very weak and not significant correlations with premium price (r = .05; r = .03, p > .05). In addition, the correlation matrix indicates very poor and not significant correlation between premium price and both indicators of profitability (respectively r = .06 and r = .07, p > .05).

Regarding the link between service quality and productivity, two different results obtained to explain this link. On one hand, the first dimension of service quality was not correlated with occupancy and labour productivity as indicators of hotels' productivity (r = .05). On the other hand, the second dimension of service quality (Staff behaviour and attitude) was not correlated with occupancy (r = .08) but was significantly correlated with labour productivity.
Findings of Study 2 (General Managers’ Perspective)

Hence, this result supported the argument made in the research model discussion that improving and delivering a high level of service quality will improve labour productivity, through doing the right thing the first time which in turn will lead to reduced time and waste, etc.

8.8 Assumptions of Multiple Regressions

Before displaying the regression analysis results, this section will present some assumptions required to run this analysis.

8.8.1 Sample Size

The sample size obtained in this research was 208 observations or cases, while the number of independent variables was 6 variables. So, the research sample exceeded the popular rule of thumb, i.e. 208 ≥ 104+6.

8.8.2 Absence of Outliers

After the data entry stage, outliers were observed and removed for some variables by using Boxplot diagrams in order to identify extreme points that located out of range (very low and very high scores). As mentioned in chapter 7, Tabachnick and Fidell (2007) suggest that the outliers are all cases which have residuals beyond +3.3 and -3.3, i.e. residuals should be between these two limits. The standardised residual for the measured variables varied from -2.70 to 2.15, which means that the data do not have any outliers. In terms of Mahalanobis distance and Cook’s distance techniques, results show for the first test (Mahalanobis) a few cases as outliers. To explain more, the critical chi-square value suitable at this Alpha level of .001 is 22.458, but three cases were found that exceeded this value (case Ids: 20, 73 and 196). Therefore, these cases were deleted from further analysis. On the other hand, in the second technique (Cook’s Distance), values should be less than 1. Fortunately, all cases have scores less than 1, i.e. the maximum Cook’s distance value was .063. Thus, it can be confirmed that data collected doesn’t have outliers and is eligible to run a multiple regression analysis.

8.8.3 Absence of Multicollinearity

Three methods can be used to assess and diagnose multicollinearity between independent variables. For the first technique, correlations between all independent variables were less than .90. Therefore, the correlation matrix supports the assumption that there is no
multicollinearity effect between the independent variables. Labour productivity, occupancy, and market share did show high correlations, but all coefficients were less than .90; therefore, all variables were retained in the model at this stage.

The Variance Inflation Factor (VIF) value was calculated for all independent variables. All values were below the cut-off value of 10; the highest values were 2.77 and 2.74, for variables measuring the operational performance items market share and occupancy. The tolerance values also supported the idea that no serious multicollinearity existed between independent variables; in other words, all calculated tolerance values were well above .10. However, the market share and occupancy values, as expected were so low (.36 and .37) compared to other independent values (since they have similar inputs) that in the end the occupancy variable was excluded as an indicator for productivity. The model includes another indicator for measuring productivity, i.e. labour productivity.

8.8.4 Normality of Residuals

Figure 8.13 shows the residual of the dependent variable (profitability).

Figure 8-13 Normal P-P Plot of Regression Standardized Residual of Dependent Variable for Study 2

The residual points of the dependent variable have to some extent a straight-line relationship with predicted dependent variable scores. Thus, the variance of the residuals around the
predicted dependent variable scores is nearly the same for all predicted scores (Tabachnick and Fidell, 2007).

8.8.5 Homoscedasticity of Residuals

The homoscedasticity assumption implies that the standard deviations of errors in predicting are approximately equal for all predicted dependent variable scores (Tabachnick and Fidell, 2007, p. 127). Figure 8.14 indicates that there is no problem with heteroscedasticity (i.e. unequal variances) since the residual is rectangularly distributed. In other words, the scatter plot in the figure shows that most of the scores are concentrated in the centre of the chart near the 0 point, i.e. no curves and no side higher than another side.

Figure 8.14 Scatter Plot of Regression Standardised Residual for Study 2

![Scatter Plot of Regression Standardised Residual for Study 2](image)

After checking and passing the assumptions required for running multiple regression analysis, the overall model fitting and linkages (paths) between variables will be discussed in the next section. In other words, none of the assumptions of multiple regression leads to diminished results since no violations of the assumptions were recorded.
8.9 Hypotheses Testing

Regression analysis can predict the contribution power of each independent variable on the dependent variable, to show the relative importance and contribution of each independent variable to the overall prediction (Hair et al., 2006; Tabachnick and Fidell, 2007). Therefore, multiple regression analysis can provide explanations for sophisticated and complex interrelationships between independent and dependent variables (Pallant, 2005).

For the overall model fitting, results of multiple regression analysis indicate that independent and mediate variables explain and predict 56% of the variance of the dependent variable (profitability). To put it another way, 56% of the variance of overall profitability of hotels in the research sample is accounted to the independent and mediator variables included in the research model. The $R^2$ value was quite high, acceptable and significant ($p < .00$) according to criteria established by Hair et al (2006) which suggest that the minimum and desirable $R^2$ for this model at this sample size and at this number of independent variables is 12% (Hair et al., 2006, p: 195).

The developed research hypotheses will be tested using Ordinal Least Square (OLS) regression analysis. The general managers' perceptions and assessments of their hotels' performance, in terms of service quality, customer satisfaction, customer retention, market share, profitability, labour productivity, premium price charged, and managing demand and capacity, will be used to test these hypotheses.

The Impact of Service Quality on Profitability. Figure 8.15 shows the graphical representation of hypothesis 1.
H1 0: There is no positive impact of service quality on profitability.
H1 A: There is a positive impact of service quality on profitability.

This proposition aims to investigate whether service quality has an impact on profitability. Table 8.16 summarises the finding of the regression model.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>.08</td>
<td>1.06</td>
<td>.29</td>
<td>.69</td>
</tr>
<tr>
<td>SQ: Staff Behaviour</td>
<td>.02</td>
<td>.24</td>
<td>.81</td>
<td>.01</td>
</tr>
</tbody>
</table>

From Table 8.16, it is clear that the two dimensions of service quality had no direct impact on hotels’ profitability. The $R^2$ value for the two dimensions was so low (.01) it did not explain any significant portion of the hotels’ profitability. The table shows that the two dimensions of service quality did not make a significant contribution to predicting the hotels profitability ($p > .05$). Therefore, findings support the Null Hypothesis.
The Impact of Service Quality on Customer Satisfaction. Figure 8.16 shows the graphical representation of hypothesis 2.

**H2 0:** There is no positive impact of service quality on customer satisfaction.

**H2 A:** There is a positive impact of service quality on customer satisfaction.

According to discussion introduced in the research model chapter, it was supposed that customer satisfaction acts as an outcome or result of achieving a high level of service quality. Table 8.17 displays results of the impact of service quality on customer satisfaction.

### Table 8.17 OLS Regression Model: Predicting Customer Satisfaction

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>.30</td>
<td>4.46</td>
<td>.00</td>
<td></td>
</tr>
<tr>
<td>SQ: Staff Behaviour</td>
<td>.21</td>
<td>3.14</td>
<td>.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>F value: 18.99, R²: .16, p value: .00</td>
</tr>
</tbody>
</table>
It can be seen that the two dimensions of service quality do act as antecedents of customer satisfaction. Moreover, the $R^2$ score obtained (.16) infers that variances of customer satisfaction are explained by those two dimensions. Finally, service quality dimensions made a significant impact on customer satisfaction ($p < .05$). Thus, results reject the Null Hypothesis.

The Impact of Service Quality on Premium Price. Figure 8.17 shows the graphical representation of hypothesis 3.

**Figure 8.17 The Research Model: Testing Hypothesis 3**

H3 0: There is no positive impact of service quality on premium price.
H3 A: There is a positive impact of service quality on premium price.

The conceptual framework illustrates the link between service quality and profitability through the mediating impact of premium price. To state this in a simpler way, achieving and offering high levels of service quality allows the hotel to charge prices higher than its competitors for the same service. This in turn will lead to more profit. Table 8.18 outlines results for this regression model.
Findings from Table 8.18 provide unexpected results. In other words, according to the OLS regression analysis above, the two dimensions of service quality did not make a significant impact on premium price, since the beta scores obtained were so low (.04 and .01). In addition, the R$^2$ (.00) implies that those two dimensions did not explain any variances of premium price. Finally, service quality did not make a statistically significant contribution to premium price (p > .05). According to the above findings, the Null Hypothesis is accepted.

The Impact of Customer Satisfaction on Customer Retention. Figure 8.18 shows the graphical representation of hypothesis 4.

**Figure 8.18 The Research Model: Testing Hypothesis 4**

H4 0: There is no positive impact of customer satisfaction on customer retention.
H4 A: There is a positive impact of customer satisfaction on customer retention.

This hypothesis tries to track the indirect impact and outcomes of service quality. Therefore, Table 8.19 displays results for the impact of customer satisfaction and customer retention.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p-value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Satisfaction</td>
<td>.48</td>
<td>7.55</td>
<td>.00</td>
<td>56.99</td>
</tr>
</tbody>
</table>

The above table indicates that customer satisfaction is a positive and significant predictor of customer retention, which implies the likelihood of customers and guests to return or recommend to others, since the Beta value was a little bit high (.48). The $R^2$ score obtained (.23) indicates that variances of customer retention behaviour are explained and attributed to satisfying customers. Finally, customer satisfaction found to have a significant impact and contribution to predicting customer retention ($p < .05$). Hence, the Null Hypothesis is rejected.

The Impact of Customer Satisfaction on Productivity. Figure 8.19 shows the graphical representation of hypothesis 5.
H5 0: There is no positive impact of customer satisfaction on labour productivity.
H5 A: There is a positive impact of customer satisfaction on labour productivity.

According to the interrelationships supposed between variables mediate the indirect relationship between service quality and profitability, it was assumed that improving customer satisfaction would help to improve the hotels’ productivity, as measured by labour productivity, through outcomes gained from the state of customer satisfaction. Table 8.20 shows findings of the regression model.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Satisfaction</td>
<td>0.06</td>
<td>0.83</td>
<td>0.41</td>
<td>F value</td>
</tr>
</tbody>
</table>

It can be seen that customer satisfaction did not make a significant impact on hotels’ labour productivity; the low beta score (0.07) implies this poor relationship, in addition to the R² value (0.00). Results obtained rejected the impact of customer satisfaction on hotel labour productivity. Accordingly, the Null Hypothesis is accepted.

The Impact of Customer Retention on Market Share. Figure 8.20 shows the graphical representation of hypothesis 6.

Figure 8.20 The Research Model: Testing Hypothesis 6
Findings of Study 2 (General Managers’ Perspective)

H6 0: There is no positive impact of customer retention on market share.
H6 A: There is a positive impact of customer retention on market share.

Retaining current customers can bring favourable outcomes for hotels. Therefore, this hypothesis supposes that retaining customers will lead to improving and increasing the market share as measured by number of rooms sold comparing others in the market. Table 8.21 presents outputs of regression model.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Retention</td>
<td>.17</td>
<td>2.44</td>
<td>.02</td>
<td>5.94 (.03 .02)</td>
</tr>
</tbody>
</table>

The above table shows that customer retention had a positive impact on a hotel’s market share (β: .17). The $R^2 (.03)$ implies that customer retention did not explain enough portions of variances of the market share. However, the Alternate Hypothesis is accepted, since customer satisfaction made a significant impact on hotels’ market share ($p < .05$).

*The Impact of Market Share on Profitability. Figure 8.21 shows the graphical representation of hypothesis 7.*

**Figure 8.21 The Research Model: Testing Hypothesis 7**

```
Service Quality → Customer Satisfaction → Customer Retention → Market Share → Profitability
```

- H2 (+): Service Quality
- H3 (+): Customer Satisfaction
- H4 (+): Customer Retention
- H5 (+): Productivity
- H6 (+): Market Share
- H7 (+): Profitability
- H8 (-): Premium Price
- H9 (+): H1 (+)
- H10 (+): MD&C
- H11 (+): H2 (+)
H7 0: There is no positive impact of market share on profitability.
H7 A: There is a positive impact of market share on profitability.

As depicted in the research model, market share helps the hotels in the sample to improve profitability. Table 8.22 shows the regressions model results of the impact of market share on profitability.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Share</td>
<td>.61</td>
<td>10.65</td>
<td>.00</td>
<td>113.35</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>.38</td>
</tr>
</tbody>
</table>

The above table provides strong support that market share had a strong impact on hotels’ profitability. In other words, the beta value was very high (.61). The $R^2$ values were also high (.38). Hence, the Null hypothesis is rejected according to the above results which show that market share made a significant effect on hotels profitability ($p < .05$).

The Impact of Premium Price on Market Share. Figure 8.22 shows the graphical representation of hypothesis 8.
H8 0: There is no negative impact of premium price on market share.
H8 A: There is a negative impact of premium price on market share.

It was supposed in the research model that premium prices would negatively impact the market share (room sales), i.e. higher prices lead to fewer sales. Tables 8.23 answers and explores the supposed negative impact of premium price on market share.

Table 8.23 OLS Regression Model: Predicting Market Share

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premium Price</td>
<td>.16</td>
<td>2.30</td>
<td>.02</td>
<td>5.28</td>
</tr>
</tbody>
</table>

Table 8.23 shows no negative impact of premium price on market share. In contrast, the results above indicate that premium price is a positive and significant predictor of market share (β.16), although the R² value was poor (.03). The Alternate Hypothesis is rejected.

The Impact of Premium Price on Profitability. Figure 8.23 shows the graphical representation of hypothesis 9.

Figure 8.23 The Hypothesis on the Model: Testing Hypothesis 9
H9 0: There is no positive impact of premium price on profitability.
H9 A: There is a positive impact of premium price on profitability.

The purpose for charging premium price is to improve and increase profits through increasing margins. This hypothesis addresses the relationship between premium price and hotels’ profitability as displayed in Table 8.24.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premium Price</td>
<td>.07</td>
<td>.93</td>
<td>.35</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>F value</td>
</tr>
<tr>
<td>.87</td>
</tr>
</tbody>
</table>

The above table provided unexpected results; premium price had a weak and not significant effect on hotels’ profitability. In other words, the beta score was very low (.07). Also the R² value was quite poor (.01). Thus, the premium price did not make a significant contribution to predict the hotels profitability (p > .05). Thus, the Null Hypothesis is accepted.

The Impact of Managing Demand and Capacity. Figure 8.24 shows the graphical representation of hypothesis 10.

**Figure 8.24 The Research Model: Testing Hypothesis 10**
H10 0: There is no positive moderation impact of managing demand and capacity on the relationship between service quality and labour productivity.

H10 A: There is a positive moderation impact of managing demand and capacity on the relationship between service quality and labour productivity.

In this hypothesis, it was assumed that managing demand and capacity positively moderates the relationship between service quality and labour productivity. In other words, this moderation effect helps quality of service to make a positive influence on labour productivity.

Before running the analysis, it is necessary to define the meaning and function of the moderator variable as well as the main characteristics of such variables. Basically, the moderator variable implies a variable which can modify the relationship between two other variables, either by changing the form (direction) or strength of the relationship between the independent and the criterion variable (Sharma, Durand and Gure-Arie, 1981). Accordingly, moderator variables are classified into two different types: variables influencing the strength of the relationship and variables changing the form of the relationship from positive to negative or vice versa.

However, the literature introduces specific procedures to determine whether or not the moderator variable makes significant effects (Hair et al., 2006; Cohen et al., 2003):

1. Examine the unmoderated relationship, i.e. the linear and simple relationship, between independent and dependent variables, in this case service quality and labour productivity.

2. Examine the moderated relationship through including the moderator variable in the original simple equation, i.e. including the managing demand and capacity scale.

3. Assess the changes of the $R^2$ value in the final equation or estimation. If the change of $R^2$ obtained from the variables is significant, a significant moderation effect exists. Tables 8.25 and 8.26 display all results obtained from the single equations (only independent and dependent variables) and the combined equation (moderator variable included).
Table 8.25 OLS Regression Model: Predicting Labour Productivity

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>.03</td>
<td>.38</td>
<td>.71</td>
</tr>
<tr>
<td>SQ: Staff Behaviour</td>
<td>.21</td>
<td>2.96</td>
<td>.00</td>
</tr>
<tr>
<td>Controlling guest’s usage</td>
<td>-.20</td>
<td>-2.86</td>
<td>.01</td>
</tr>
</tbody>
</table>

Overall Model Fit Statistics

<table>
<thead>
<tr>
<th>F value</th>
<th>R²</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.50</td>
<td>.08</td>
<td>.00</td>
</tr>
</tbody>
</table>

Table 8.25 presents unexpected results in terms of the unmoderated impact of service quality dimensions on labour productivity. To be more precise, the first dimension of service quality (physical quality) had a positive but not significant impact on labour productivity (β: .03, p > .05). On the other hand, the second dimension of service quality (staff behaviour and attitude) had a positive and significant impact on labour productivity (β: .21, p < .05) which is logic. Finally, the construct managing demand and capacity (controlling guest’s usage) had a negative and significant impact on labour productivity (β: -.20, p < .05). The R² value for the overall model was low but significant (.08, P < .05).

Table 2.26 OLS Regression Model: Predicting Labour Productivity

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>-.14</td>
<td>-.63</td>
<td>.53</td>
</tr>
<tr>
<td>SQ: Staff Behaviour</td>
<td>.30</td>
<td>1.23</td>
<td>.22</td>
</tr>
<tr>
<td>Controlling guest’s usage</td>
<td>-.47</td>
<td>-.61</td>
<td>.54</td>
</tr>
<tr>
<td>Physical Quality X Controlling guest’s usage</td>
<td>.54</td>
<td>.80</td>
<td>.42</td>
</tr>
<tr>
<td>Staff Behaviour X Controlling guest’s usage</td>
<td>-.25</td>
<td>-.39</td>
<td>.69</td>
</tr>
</tbody>
</table>

Overall Model Fit Statistics

<table>
<thead>
<tr>
<th>F value</th>
<th>R²</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.42</td>
<td>.09</td>
<td>.01</td>
</tr>
</tbody>
</table>
As can be seen in Table 2.26, the moderated impact of managing demand and capacity (controlling guest's usage) provides a not significant impact on labour productivity for all independent variables, without making significant changes of the $R^2$ value. In other words, the interaction model displayed in Table 2.26 gave a not significant impact on labour productivity.

Thus, including managing demand and capacity (controlling guest's usage) as a moderator variable will not be considered a moderator variable because it did not make significant changes in the $R^2$ value of the whole model as suggested by Hair et al (2006). Thus, the Null Hypothesis is accepted.

*The Impact of Productivity on Profitability. Figure 8.25 shows the graphical representation of hypothesis 11.*

**Figure 8.25 The Research Model: Testing Hypothesis 11**

H11 0: There is no positive impact of labour productivity on profitability.
H11 A: There is a positive impact of labour productivity on profitability.

Finally, the research model supposes that improving the hotels' labour productivity will lead to more profit. Table 8.27 displays results for testing this hypothesis.
Table 8.27 provides strong support to the Alternate Hypothesis. In other words, labour productivity had a significant impact on hotels profitability due to the high beta score (.63). The $R^2$ value was also high (.40). Accordingly, labour productivity made a significant contribution to hotels profitability ($p < .05$) which implies rejecting the Null Hypothesis.

8.10 Post Hoc Analysis

It can be easily recognised from the data analysis that market share and labour productivity form critical predictors and antecedents of profitability, i.e. they produce significant beta and $R^2$ values. Therefore, post hoc analysis will be used to confirm and validate the importance of market share and labour productivity, in terms of their impact on profitability. To do so, the research model was reshaped as shown in Figure 8.26, using the same general managers’ perspective data to check whether market share and labour productivity really mediate the relationship between antecedents (premium price, service quality, customer satisfaction and customer retention) and the dependent variable (profitability) in the budget hotel sector.
As seen in Figure 8.26, market share and productivity have a mediating role for the impact of the antecedent variables on profitability. Regression analysis will be conducted assuming that market share and labour productivity mediate the effects on profitability of premium price, service quality, customer satisfaction and customer retention. Baron and Kenny’s criteria (1986) will be used to confirm the mediating impact of market share and labour productivity actually exists. Firstly, the impact of antecedents on consequences should be significant. Then, the impact of antecedents on the mediator variables should be determined. Finally, the impact of antecedent and mediator variables together on the dependent variable should be significant as well. Table 8.28 examines the impact of antecedents on the dependent variable.
Table 8.28- OLS Regression Model: Predicting Profitability

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>.07</td>
<td>.89</td>
<td>.37</td>
</tr>
<tr>
<td>SQ: Staff Behaviour and Attitude</td>
<td>.01</td>
<td>.12</td>
<td>.90</td>
</tr>
<tr>
<td>Customer Satisfaction</td>
<td>-.05</td>
<td>-.58</td>
<td>.56</td>
</tr>
<tr>
<td>Customer Retention</td>
<td>-.02</td>
<td>-.28</td>
<td>.78</td>
</tr>
<tr>
<td>Premium Price</td>
<td>.08</td>
<td>1.04</td>
<td>.30</td>
</tr>
</tbody>
</table>

Overall Model Fit Statistics

<table>
<thead>
<tr>
<th>F value</th>
<th>R²</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>.41</td>
<td>.01</td>
<td>.84</td>
</tr>
</tbody>
</table>

As can be easily recognised from the table, all independent variables had positive and negative but not significant impact on the dependent variable (profitability), i.e. p values were higher than .05 with very poor $R^2$ scores for all variables. Therefore, this model failed to meet the first criterion defined by Baron and Kenny's. In addition, the overall confidence level obtained of this model was higher than .05.

The second criterion of Baron and Kenny (1986) implies that antecedents should have a significant impact on the mediator variables. Table 8.29 shows the regression results of the antecedent's impact on mediator variables (Market share and labour productivity).

Table 8.29- OLS Regression Model: Predicting Market Share

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>.13</td>
<td>1.72</td>
<td>.08</td>
</tr>
<tr>
<td>SQ: Staff Behaviour and Attitude</td>
<td>.01</td>
<td>.17</td>
<td>.87</td>
</tr>
<tr>
<td>Customer Satisfaction</td>
<td>-.02</td>
<td>-.27</td>
<td>.79</td>
</tr>
<tr>
<td>Customer Retention</td>
<td>.14</td>
<td>1.70</td>
<td>.09</td>
</tr>
<tr>
<td>Premium Price</td>
<td>.13</td>
<td>1.71</td>
<td>.09</td>
</tr>
</tbody>
</table>

Overall Model Fit Statistics

<table>
<thead>
<tr>
<th>F value</th>
<th>R²</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.35</td>
<td>.06</td>
<td>.04</td>
</tr>
</tbody>
</table>
As displayed in Table 8.29, results show a not significant impact of all independent variables (physical quality, staff behaviour and attitude, customer satisfaction, customer retention and premium price) on the first mediator variable (Market Share), i.e. p values were not significant for all independent variables. However, the overall model got a significant level of confidence p < .05.

Table 8.30 shows the impact of the same antecedent variables on the second mediator variable (Labour productivity).

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (B)</th>
<th>t-value</th>
<th>p value</th>
<th>F value</th>
<th>R²</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>-.02</td>
<td>-.21</td>
<td>.84</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SQ: Staff Behaviour and Attitude</td>
<td>.17</td>
<td>2.22</td>
<td>.03</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer Satisfaction</td>
<td>.01</td>
<td>.08</td>
<td>.93</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer Retention</td>
<td>-.03</td>
<td>-.41</td>
<td>.68</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premium Price</td>
<td>.00</td>
<td>-.00</td>
<td>.10</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

As displayed in Table 8.30, results show a not significant impact for all independent variables except staff behaviour and attitude on the mediator variable (Labour Productivity), i.e. p > .05. Thus, this model failed to fulfil the second Baron and Kenny condition and criterion. The next table shows results concerning the third criterion of Baron and Kenny, which tests the impact of independent on the dependent variable after controlling the effect of the mediator variables. In other words, independent variables should have less or not significant impact while the mediator variables should have significant impact on the consequence variables.
Table 8.31- OLS Regression Model: Predicting Profitability

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Standardised Coefficients (β)</th>
<th>t-value</th>
<th>p value</th>
<th>Overall Model Fit Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>SQ: Physical Quality</td>
<td>-.00</td>
<td>-.06</td>
<td>.95</td>
<td></td>
</tr>
<tr>
<td>SQ: Staff Behaviour and Attitude</td>
<td>-.04</td>
<td>-.82</td>
<td>.41</td>
<td></td>
</tr>
<tr>
<td>Customer Satisfaction</td>
<td>-.05</td>
<td>-.82</td>
<td>.42</td>
<td></td>
</tr>
<tr>
<td>Customer Retention</td>
<td>-.07</td>
<td>-1.28</td>
<td>.20</td>
<td></td>
</tr>
<tr>
<td>Premium Price</td>
<td>.03</td>
<td>.53</td>
<td>.59</td>
<td></td>
</tr>
<tr>
<td>Market Share</td>
<td>.44</td>
<td>7.61</td>
<td>.00</td>
<td></td>
</tr>
<tr>
<td>Labour Productivity</td>
<td>.46</td>
<td>8.12</td>
<td>.00</td>
<td>31.85</td>
</tr>
</tbody>
</table>

The result as shown in Table 8.31 was that independent variables did not have significant impact on dependent variables. In contrast, mediator variables (market share and labour productivity) did have significant impact, which means this regression model passed the third criterion of Baron and Kenny’s method.

According to post hoc analysis which supposed that market share and labour productivity fully mediate the impact of antecedents on profitability, the results obtained did not fulfil Baron and Kenny’s criteria. Only the third criterion passed the assumptions of Baron and Kenny, while the first and second conditions did not pass the criteria. As a result, this study will ignore results that emerged from the post hoc method because the results are questionable and problematic, and are not fully understood and justified. In other words, the results of the post hoc analysis are not reliable and statistically not significant.

However, passing one condition of Baron and Kenny’s criteria means that the mediating impact of market share and labour productivity partially exists and forms a good start for further research. Moreover, the results of post hoc analysis supported the results obtained previously in this chapter which tested the original research model, supposing that service quality relates to profitability through a set of consequential variables.
8.10 Discussion of Findings (Study 2)

The results of validity and reliability tests used in this study will be reviewed in this section before discussing the results of the model testing and path analysis between variables. To start with, the service quality scale used in study 2 passed the validity and reliability criteria. For the validity test, the Exploratory Factor Analysis (EFA) confirmed the two dimensions of service quality (physical service quality and staff behaviour and attitude) introduced and recommended by Ekinci (2001). For the reliability test, the two dimensional scale of service quality was found to be reliable since the Cronbach Alpha scores exceeded .70. Hence, there was no need to delete any item from the Ekinci’s scale used to improve the reliability results.

For the managing demand and capacity scale, the Exploratory Factor Analysis (EFA) did not indicate the same six dimensions of the demand and capacity management scale introduced before (price, modify product element, education and communication, time, labour and facilities and equipment). Instead, the EFA introduced four different solutions for this scale: controlling guest’s usage, outsourcing activities, schedule workforce and pricing. EFA reduced the number of dimensions to four factors from six. As a result of this analysis, the new factor solution introduced different aspects of the managing demand and capacity construct. However, three of the four scales failed to achieve acceptable levels of reliability; there were very low Cronbach Alpha values for all dimensions except for controlling guest’s usage. Thus, the purification processes for the scale dropped the three dimensions and kept only the first dimension (controlling guest’s usage) for measuring the managing demand and capacity construct because the results of reliability test were poor for the other three dimensions (outsourcing activities, scheduling workforce and pricing).

Going next to the direct impact of service quality on profitability, study 2 indicates positive but not significant impact for the two dimensions of service quality (physical quality and staff behaviour and attitude) on profitability ($b: .08$ and $.04$; $R^2: .01$ and $.00$; $P > .05$). Therefore, the study two found not significant scores for the direct impact of service quality on profitability.

Similar to the first study (the hotel performance data), the direct analysis was rejected in the second study and therefore turned out to run a simpler testing of sequential relationships between each two variables in the research model. To summarise the findings that emerged in study 2, Figure 8.27 highlights only the significant results obtained;
According to Figure 8.27, many linkages between variables that had been proposed to be significant were found to be not significant in study 2. As displayed in the figure, only six hypotheses out of 11 were significant in study 2. However, data analysis found support for only five hypotheses because of the impact of premium price which, although proposed in the research model to have a negative impact on market share, had a positive impact instead. Thus, the data analysis for the research model in study 2 found that half of the linkages (paths) in the research model are not statistically significant. Table 8.32 summarises findings obtained in study two.
### Table 8.32 Summary of Hypotheses Testing for Study 2

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Beta Value</th>
<th>P value</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1 A There is a positive impact of service quality on profitability.</td>
<td>.08 + .02</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H2 A There is a positive impact of service quality on customer satisfaction.</td>
<td>.30 + .21</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H3 A There is a positive impact of service quality on premium price.</td>
<td>.04 + .01</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H4 A There is a positive impact of customer satisfaction on customer retention.</td>
<td>.48</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H5 A There is a positive impact of customer satisfaction on labour productivity.</td>
<td>.06</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H6 A There is a positive impact of customer retention on market share.</td>
<td>.17</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H7 A There is a positive impact of market share on profitability.</td>
<td>.61</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
<tr>
<td>H8 A There is a negative impact of premium price on market share.</td>
<td>.16</td>
<td>P &lt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H9 A There is a positive impact of premium price on profitability.</td>
<td>.07</td>
<td>P &gt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H10 A There is a positive moderation impact of managing demand and capacity on the relationship between service quality and labour productivity.</td>
<td>No Significant Interaction</td>
<td>P &lt; .05</td>
<td>Rejected</td>
</tr>
<tr>
<td>H11 A There is a positive impact of labour productivity on profitability.</td>
<td>.63</td>
<td>P &lt; .05</td>
<td>Accepted</td>
</tr>
</tbody>
</table>

Starting with the first hypothesis, H1A indicates that the two dimensions of service quality do not have significant impact on profitability. These findings mean that higher service quality does not lead to a positive impact on profitability. As mentioned in the research model, this
result supports the research model which supposed that service quality will have indirect positive impact on profitability indirectly via other intervening variables such as the revenues mechanism and production/operational mechanism (Rust et al., 1995, 2002; Hardie, 1998; Lai and Cheng, 2005; Larivièreme, 2008). However, the results of this hypothesis are not consistent with other studies which found a positive direct impact of service quality on profitability.

H2A finds positive impact of the two dimensions of service quality on customer satisfaction. This study is completely consistent with the key studies in the literature indicating that customer satisfaction forms an important consequence of service quality (Anderson et al., 1994; Brady and Robertson, 2001; Cronin et al., 2000; Dabholkar et al., 2000; Olorunniwo et al., 2006; Cronzález et al., 2007).

For the third hypothesis (H3A) there is positive but not significant impact of the two dimensions of service quality on premium price. Thus, improved service quality in this budget hotel doesn't help this chain to charge prices higher than its competitors in the market. This result contradicts theories supporting the positive impact and consequences of service quality on prices (Phillips et al., 1983; Buzzell and Gale, 1987; Rust et al., 1995; Zeithaml, 2000; Kimes, 2001).

The results of H4A imply that the higher customer satisfaction will be translated into higher customer retention. This result supports the theoretical and empirical findings that indicate that customer satisfaction has a positive influence on customer retention measured by likelihood to recommend to others and return again to this budget hotel chain. Thus, the results of H4A are consistent with earlier studies by Oliver (1980); Churchill and Surprenant (1982); Anderson and Sullivan (1993); Mittal and Kamakura (2001); Olsen (2002) and Cronzález et al (2007).

According to the results from H5A, customer satisfaction has a positive but not significant impact on labour productivity. The results of this hypothesis show that customer satisfaction does not have a significant positive impact on labour productivity, which means that satisfying customers will not be translated to more customers served by the available number of staff. So, the assumption of customer satisfaction having positive impact on labour productivity was rejected in this study. However, the result of this hypothesis supports
findings by Anderson et al (1997) who did not find positive significant impact of customer satisfaction on productivity in the service industry in particular because customer satisfaction in such industries is more dependent on customization strategy which requires more costly materials and adding more features and service personnel.

H6A suggests that there is a positive impact of customer retention on market share. In other words, higher customer retention will lead to more market share and sales in the market. These results are in complete agreement with theoretical and empirical investigations into the link between customer intentions and market share (Rust et al., 1995, 2002).

In terms of the impact of market share on profitability, H7A shows a positive impact. In other words, more market share and sales will improve profitability. Earlier studies interested in this link by Schoeffler et al (1974); Szymanski et al (1993); Buzzell and Gale (1987) found similar results. Furthermore, Phillips et al (1983) supposed and found that the market position of the company will lead to improved profits via two options: on one hand, higher market share will lead to reduced costs required, leading to more profits; on the other hand, market share improves profitability through market power and economies of scale.

For the link between premium price and market share, the result obtained in H8A rejects the proposition that higher prices diminish the market position of the company. Thus, the fact that premium prices will have positive impact on market share is true in this budget hotel setting. This result is supported by previous findings by Phillips et al (1983) that proved that the higher prices gained from higher quality apparently do not decrease market penetration and position. Thus, rejecting H8A refutes the inverse relationship between prices and market share as suggested by theories developed in the economy and niche models.

For the impact of premium price on profitability, H9A indicates positive but not significant impact. This result disagrees with theories that higher prices as an outcome of high quality of services will lead to increased profit margins. However, Phillips et al (1983) indicate that the quality, price and profitability relationship is not clear and varies according to industry. The One explanation for this result could be that a premium price would have a negative impact on occupancy rates which in turn would decrease profits. Moreover, charging a premium price may require high costs and expenses to achieve high levels of service quality, leading to decreased margins and profits.
In terms of the link between quality and productivity—and before discussing H10A—the data analysis in study 2 explores the positive and significant impact of the second dimension of service quality (staff behaviour and attitude) on labour productivity before including the impact of the managing demand and capacity construct. For the first dimension of service quality (physical service quality), the results did not show a significant impact on labour productivity. It is not surprising that physical attributes of quality do not improve labour productivity in the budget hotel sector in particular, but it may help in other hotel classifications such as luxury hotels since they have more technological facilities and equipment that can help to reduce costs while increasing the number of customers served and reducing wait time and so on. Facilities and different material aspects of service quality in a different class of hotels may help to enhance labour productivity. Moreover, it is not surprising that staff behaviour and attitudes, rather than physical quality, have a positive impact on labour productivity.

Result for the impact of the second dimensions of service quality dimension (staff behaviour and attitude) on productivity is consistent with other findings in the literature. For example, Weech-Maldonado et al (2003) found significant negative impact of quality programs on resident and patient costs and process related. Higher service quality will lead to lower costs and fewer processes through increased productivity caused by decreasing the number of defects and eliminating wastes.

In terms of the moderating impact of managing demand and capacity, H10A indicates that managing demand and capacity does not moderate positively the impact of service quality on profitability. This result reveals that managing demand and capacity failed to change the relationship between service quality and labour productivity positively and significantly. In other words, according to general managers' assessments, all activities used to manage demand and capacity did not make any significant improvements in the relationship between service quality and labour productivity. A significant change of the $R^2$ value is required to prove the moderation impact and effect (Hair et al., 2006), but in this case the $R^2$ value only changed from .08 to .09.

Finally, for the link between productivity and profitability, H11A reveals positive and strong impact of labour productivity on profitability. Thus, more labour productivity leads to more
profits, which is supported by Phillips et al (1983) and Anderson et al (1997) who found positive association between reduced costs and profitability.

8.12 Conclusions
This chapter describes all procedures undertaken to explore the relationship between service quality and profitability from the general managers' perspective. First, this chapter describes the characteristics of hotels and demographic information of respondents who participated in this study; responses were to some extent compatible with facts and trends occurring in the UK budget hotel sector. Then, tests used to check validity and reliability for the service quality and demand and capacity management scales are introduced. The exploratory factor analysis (EFA) technique was used as a tool for analysing the construct validity. The EFA indicated and confirmed the two factors as supposed and confirmed by Ekinci (2001). For the managing demand and capacity scale, the EFA indicated four factor solutions instead of six.

The consistent reliability was used to check the scale's reliability. The Cronbach Alpha value indicated that the internal consistency of the two service quality scales is acceptable and exceeds .70. In contrast, the managing demand and capacity scale showed very poor values for all dimensions except controlling guest's usage. Therefore, all of the other dimensions were dropped as a measurement of demand and capacity management.

Finally, in terms of impact and association between variables in the research model, results indicated that general managers support the indirect positive impact of service quality on profitability. In this sense, this study explored how service quality can be transformed into profit through causal paths from the general managers' perceptions. The findings of study 2 identified which path in the conceptual framework helps to improve and increase profitability in the UK budget hotel sector. As a result of the data analysis, general managers think that customer' perceptions of service quality (customer behavioural response) represents the major predictor of profitability in this hotel sector.
Chapter 9

Conclusions and Recommendations
Chapter 9

Conclusions and Recommendations

9.1 Introduction
This chapter reviews and summarises the results of the data analysis in chapters 7 and 8. Section two redisplays the aim and objectives of the study. Section three summarises the findings emerging from the two data analysis chapters. Section four highlights the theoretical implications of the results, while section five emphasizes the practical implications that can be used and adopted by practitioners and experts in the budget hotel industry. Section six identifies some limitations of the study. Finally, section seven proposes some areas and directions for future research.

9.2 Aim and Objectives of the Study
The purpose of this study is to extend the existing knowledge on the hypothesised relationship between service quality and profitability in the budget hotel sector. This relationship is tested in the UK budget hotel sector in particular. To do so, this study has the following objectives:

(1) To develop a conceptual framework that captures the relationship between service quality and profitability in the UK budget hotel sector;
(2) To examine empirically the relationship between service quality and profitability in the UK budget hotel sector;
(3) To determine what variation, if any, there is in the nature and direction of this relationship between different data sets collected from different sources; and
(4) To determine which outcome of service quality makes the greatest contribution to the UK budget hotel profits.

9.3 Summary of Findings
Before displaying the empirical findings of this study, it is worth re-presenting briefly once again the latest trends and strategies used and adopted in the budget hotel sector, previously introduced in the literature review part of this study. In this regard, the literature recognized a shift in strategies from the basic and traditional strategies, which focused mainly on the low cost and tariff, offering simple and consistent service
strategies towards new and dynamic strategies and characteristics. Several reasons and factors have forced operators of budget hotels to adopt these changes and developments such as high competition, market saturation, economic slowdown and uncertainty, continuation of new entrants into the market, limited and similar product and service range across brands, and increasing customer expectations. In other words, these factors and elements have forced budget hoteliers to change their thinking and upgrade their strategies.

Thus, budget hotels are now relying on new dynamic strategies, including product modification and differentiation, brand strength and identity, franchising, and wider coverage of units, with keeping services and offers simple and consistent. As a result, the service quality concept and value for money have emerged as one of the significant and valuable tools for achieving the new strategies and changes. In other words, the new dynamic trend within the budget hotel concept and model is using service quality and value as a tool to strengthen and differentiate brands and offers from other competitors in the same sector.

The findings of the literature in this study showed that the majority of players in the budget hotel sector have adopted the new dynamic strategies and moved away from the traditional concept of budget hotels to the new and contemporary strategies and solutions. In this regard, the recent development of the budget hotel concept implies that budget hoteliers have started to enhance their quality of service and offering to achieve more brand strength and identity among other competitors in the same sector as well as achieving more value for money.

According to the new trends and strategies emerging in the budget hotel sector highlighted above, it seems that enhancing service quality really exists and works in the budget hotel sector concept as proved and confirmed in the findings of this study (as shown in chapters 7 and 8). Thus, this study has confirmed the validity of the service quality concept as a critical and successful strategy for achieving profitability in the budget hotel sector.

In this regard, the main finding of this study confirmed and proved a positive and indirect relationship between quality of service and profitability in the UK budget hotel sector by
using two sets of data (the hotel performance data and general managers' perspective data). However, as assumed in the research model, the results obtained from the two data sets revealed that there is no significant direct influence of service quality on profitability. Hence, the key finding of the research model supports the assumption that service quality has an indirect positive impact on profitability through some intervening and mediation variables.

As shown in the data analysis chapter, sequential regression models were used for the two data sets to assess the direction of paths between all variables involved in this relationship. The results of this path analysis identified the relationship between each set of variables in the research model. More importantly, results emerged that can lead to the discovery of how service quality lead to profits through some intervening variables which act as outcomes and consequences of service quality.

In this sense, the data analysis of the two data sets found that service quality influences customer satisfaction positively and significantly more than other variables, i.e., customer satisfaction was the strongest and most significant outcome of service quality. The regression analysis results in the first study indicated positive impact of service quality on customer retention which forms a proxy of customer satisfaction ($\beta = .21$, $p < .05$). This was reinforced by the second study which provided nearly similar results in terms of the impact of the two dimensions of service quality on customer satisfaction ($\beta = .30$ and $.21$ respectively, $p < .05$).

For the other consequences of service quality, the first study indicated that quality of service had a positive significant impact on prices ($\beta = .24$, $p < .05$), i.e., higher service quality will lead to higher prices charged. In contrast, results in the second study showed that service quality did not have a significant impact on price ($\beta = .04$ and $.01$, $p > .05$). The conflicting results are attributed to using different measurements of service quality and prices in the two studies: objective quality features against perceived service quality and actual prices charged for rooms against perceptions of room rates. As mentioned in the discussion sections in chapters 7 and 8, the relationship between quality and price is weak and influenced by the product and service under investigation.
In terms of the impact of premium price on profitability, the two sets of data (studies 1 and 2) had conflicting results. The first study found significant negative impact on profitability (-21, p < .05) while the second study gained positive but not significant impact (.07, p > .05). Basically, this competing result in the two studies together means that prices charged in this hotel group did not help in improving either profit growth or annual profits but actually decreased them. Phillips et al (1983) declare in their classic study of a large number of companies from different industries that the direct link between quality-price-profitability is not well supported, and the literature has little evidence for sequences between variables.

However, it is noteworthy that this study was undertaken in one UK budget hotel chain, which means that this class of hotels does not and should not charge high prices for their high standards of service quality. High prices adopted in this kind of hotel sector do not help to improve either profit growth or annual profits for an important reason: this class of hotels is considered a very competitive market and uses price as a crucial tool for attracting and keeping customers. Therefore, any premium price policy adopted will affect negatively the demand for rooms and sales, which in turn leads to decreased profits. So, it was not surprising for this hotel sector that the data analysis did not support the assumption that higher service quality enables charging higher prices compared to competitors which would increase profits.

Furthermore, the analysis of the general managers' data in study 2 indicates that, for this hotel chain, any increase in price would not have a negative influence on market share (room sales) but would have a positive impact instead. The regression analysis result found positive and significant impact for hypothesis H8A (β= .16, p < .05). Such a result means that satisfied and loyal customers are willing to stay more and come again even if the prices increased, at least to some extent.

Finally, results in the second study failed to support a positive moderator impact of managing demand and capacity on the relationship between service quality and labour productivity. In other words, the change in R^2 values after including the moderator variable was not significant. However, analysis in the second study found strong positive and significant impact of labour productivity on profitability (β= .63, p < .05).
In a budget hotel establishment, management is more likely to use the minimum amount and quality of physical inputs such as decor, equipment, facilities, etc. Thus, any budget hotel will not use the physical dimension of service quality to improve its labour productivity. Instead, the second dimension of service quality (staff behaviour and attitude) will be used in this class of hotels to make significant improvements in labour productivity.

In terms of the overall model fitting the test results, the findings in the first study indicated that independent and mediator variables explain and predict 35% of the variance of the dependent variable (profit growth). On the other hand, 56% of the variance of the overall profitability of hotels in the second study was explained by the independent and mediator variables included in the research model. Therefore, the $R^2$ value was acceptable, significant and higher than in other key papers published in this area. However, it is necessary to comment on the degree of strength of associations between variables in the research model. The data analysis from the two data sets indicates that the $R^2$ values for paths between variables were not high because of reasons introduced by Adam (1994): first, $R^2$ values in the management literature in general are much higher in cases of attitude studies than in operating and financial studies; second, many items besides quality affect operating and financial performance; and third, $R^2$ values for cross-sectional studies are generally much lower than for longitudinal studies. Hence, it is positive to have statistically significant results for a good number of paths in the research model even though the $R^2$ values were not as high as desired.

Before integrating and presenting the results obtained from studies 1 and 2 as shown on Figure 9.1, it is worth summarising the results of the data analysis chapters in a few points:

- Customer satisfaction and behavioural response form the strongest consequences of service quality in terms of the impact on profitability in the budget hotel sector.

- Premium price in the budget hotel sector does not help to increase profitability even though satisfied and loyal customers will pay premium price to some extent.
The impact of service quality on labour productivity is not moderated positively by managing the demand and capacity, but labour productivity is positively influenced by staff behaviour and attitudes of staff.

Figure 9.1 The Relationship between Service Quality and Profitability

As illustrated in figure 9.1, service quality improved profitability in this sector of hotels through improving the customer behavioural response (customer direction) more than any other direction. In other words, service quality improves profitability through increasing revenues gained from satisfying and retaining the current customers and also attracting more customers, which in turn leads to improved revenues and profits. Clearly, such findings validate Bagozzi’s (1992) attitude theory and framework which suggests that customer satisfaction will determine the customer’s future behaviour. As a result, satisfied customers will increase their patronage through buying more and attracting more customers which will lead to more revenues.

On the other hand, service quality activities failed to help this class of hotels to charge higher prices than other competitors. As a result, the prices charged in this market of
hotels did not help to improve profits and sometimes had a negative impact due its negative impact on occupancy. Finally, although labour productivity (operation direction) improves profits, service quality after managing the demand did not work positively to improve labour productivity.

The first objective of this study was to develop a conceptual framework that illustrates the relationship between service quality and profitability in the UK budget hotel sector. To do so, a model was created with linkages between variables and including a discussion to show the direction between variables and explain why.

The study's second objective, which was examining empirically the relationship between quality of service and profitability in the UK budget hotel sector, was also met. This study collected two sets of data from a leading budget hotel company located and operating in the UK. Obviously, the data collected covers different points in time and different perspectives and represents a large number of hotels and units across the UK.

This study successfully completed the third objective which was to determine whether there are any differences in the nature and direction of the relationship between service quality and profitability among the two data sets obtained. The results that emerged from the two data sets did not show differences after comparing and integrating them into one model to determine if findings are similar to each other or not. Comparison between the two results indicates that both data sets revealed positive and indirect impact of service quality and profitability with nearly similar strength of this impact.

Finally, this study satisfied the fourth objective which was to identify which outcome of service quality improves and contributes the most to profitability in the budget hotel industry. Results of regression analysis found strong support for the customer behavioural direction in terms of the impact on profitability. In other words, customer satisfaction forms the most useful tool for improving profitability in this hotel sector.

In light of former discussions, it can be claimed that all objectives required to answer the research question in this study have been met. Thus, the current study answered empirically the main research question: what is the relationship between service quality and profitability in the UK budget hotel industry?
9.4. Theoretical Implications

Having summarised the results that emerged from the two data sets in the former section, this section will display some theoretical implications and contribution of the present study. First, despite a long-term interest in investigating the relationship between service quality and profitability, there is still a debate concerning the exact nature and direction of the relationship between these two concepts. Accordingly, this study answered and contributed to this debate and supported the theoretical and classic assumptions developed by Heskett et al. (1997) who claim that service quality has a positive impact on profitability. In other words, this study tested and confirmed the well-known theory-based model called “the service profit chain,” which illustrates and depicts the associations and connections between the service quality and profitability of a business i.e. this study offered a strong support for the theoretical background concerning the link between service quality and profitability.

Second, although the key finding of the present study – which reveals that service quality has a positive impact on profitability – is compatible with previous empirical studies conducted and introduced in the literature (e.g. Schoeffler et al., 1974; Phillips et al., 1983; Kimes, 2000; Hasan and Kerr, 2003; Claver et al., 2006; Yee et al., 2008; Lariviére, 2008), the current study moved beyond this scope of investigation and expanded the understanding and modelling of the relationship between quality of service and profitability through the development of a comprehensive framework. As shown in the research model earlier, this study argued that the link between quality of service and profitability is indirect and complex; this was accomplished by including some mediating variables that had never been tested together in this hotel sector in particular. Thus, the current study extends the understanding of the service quality-profitability relationship in the hotel industry in general and in the budget hotel sector in particular.

In order to show the contribution of this study within the relevant literature, three streams of research in this area have emerged. The first stream links service quality with profitability directly (e.g. Schoeffler et al., 1974; Nelson et al., 1992; Harrington and Akehurst, 1996; Kimes, 2001; Hasan and Kerr, 2003; Claver et al., 2006; Macinati, 2008). The second stream tests the relationship between service quality and profitability by using simple indirect perspectives, achieved by including the customer satisfaction and behavioural response variables only (e.g. Babakus et al., 2004; Anderson et al., 2004; Al-
Conclusions and Recommendations

Hawari, 2005, Yoo and Park, 2007; Yee et al., 2008). Finally, the third stream of research integrates more marketing and operational variables than the variables included in the second stream; these variable include customer satisfaction, retention and loyalty, price, value, costs and productivity for testing the relationship between service quality and profitability (e.g. Phillips et al., 1983; Heskett et al., 1997; Hardie, 1998; Loveman, 1998; Rust et al., 1995; Anderson et al., 1997; Raju and Lonial, 2002; Rust et al., 2004; Larivière, 2008). Obviously, the present study belongs to the third stream, which represents a more sophisticated perspective for testing the relationship between service quality profitability in the budget hotel sector.

To highlight the theoretical contribution of this study, few studies have examined the service quality-profitability relationship in the hospitality industry by using and integrating the relevant intervening variables as introduced in the third stream of research. The majority of studies in the hospitality literature tested the link between quality of service and profitability either by using the direct perspective (first stream) (e.g. Kimes, 2001; Harrington and Akehurst, 1996) or simple indirect perspective as shown in the second stream (e.g. Yoo and Park, 2007). Accordingly, the main contribution of this research is based on investigating the relationship between service quality and profitability in the budget hotel sector by including more relevant variables as suggested and introduced in the third stream, which implies the service profit chain theory developed by Heskett et al (1997). Thus, the findings of this study give strong credibility to both the theoretical assumption (e.g. service profit chain) and the empirical findings.

Fourth, the present study supports the existing literature and the arguments that discussed the best strategy or path needed to enhance and maximise the impact of service quality on profitability in the service sector. To put it another way, the findings of this study revealed that revenue expansion gained from customer satisfaction and retention is the most significant route to take for improving profitability rather than cost reduction efforts (increasing productivity) or increasing price. Obviously, such a finding is compatible with assumptions made by Rust et al (1995; 2002), who claimed that service organisations rely on customer satisfaction strategy rather than on cost reduction strategy to improve profitability. Thus, this study contributes to the service literature by confirming and validating the indirect impact of service quality on profitability through customer satisfaction and behavioural responses. Compatible with other theoretical assumptions,
Reichheld and Sasser (1990) state that customer satisfaction has a stronger impact on the company’s profit than it has on other variables such as scale, market share, costs, and many other factors usually associated with the competitive advantage of a company.

Fifth, the current study tests the service quality-profitability relationship by using two sets of data never before used together in the budget hotel sector; the first set of data was objective and longitudinal, and obtained from the company’s sources, while the second data set was subjective and collected from general managers at the hotel units in the same budget hotel chain in order to provide comprehensive insight on this topic in the hospitality industry.

Sixth, this study opened the discussion on managing and measuring the demand and capacity practices in the budget hotel sector in particular, and the findings of this study found poor understanding and measurement of the demand and capacity concept in that sector. This study also developed a scale for measuring such practices in the budget hotel sector. However, statistical results for the reliability and validity of scales for measuring such practices were weak, which implies that the academic and practitioner communities did not give enough attention to this area in general, and to this sector in particular. Finally, besides the above theoretical contributions, this study confirmed the suitability of the two-dimensional scale (functional and technical) for measuring service quality from the general managers’ perspective in the budget hotel sector. Accordingly, this study also supported the theoretical and empirical findings discussed in the literature that confirm the possibility and validity of using the Nordic European school of thought developed by Gronroos (1984) for measuring and understanding service quality in the budget hotel sector.

To conclude, this study contributes to the ongoing debates on whether service quality will have a positive influence on profitability in the budget hotel sector and, if so, whether the impact of service quality on financial performance will be direct or indirect. More interestingly, this study integrates theoretical links suggested in the literature (e.g. service profit chain) by linking service quality, customer satisfaction, behavioural intentions, price, and productivity to profitability. Testing the research model by using two sets of data (longitudinal and cross-sectional data) provides a comprehensive chain of effects. Such integration of linkages conducted in the present study as shown in the research
model represents the most significant contribution to the service sector in general and the hospitality literature in particular. Accordingly, the evidence gained from this study will support, reinforce, and contribute to the understanding of this topic in the hospitality literature.

9.5 Practical Implications
The findings of the present study provide interesting managerial and practical implications for the budget hotel sector in general and for the budget hotel company under investigation in particular. At the budget hotel sector level, the current study revealed that higher service quality would lead to greater customer satisfaction, retention, and market share revenues, which in turn will lead to greater profitability. Given the potential benefits and outcomes of service quality, hoteliers in this sector should focus on and use service quality as an important long-term strategy for achieving better financial performance.

More precisely, this study found that customer satisfaction direction has the strongest impact on profitability rather than other directions including premium price and productivity. Accordingly, hoteliers should know that offering service quality would yield a positive impact on their customers’ feelings and behaviours, which would result in improvement in the hotel’s profitability. Thus, managers in the budget hotel sector have to recognise and improve the role and contribution of customer satisfaction to profitability in budget hotels. To do so, managers in this sector have to understand the needs and requirements of customers in order to satisfy them. The present study urges hoteliers in this sector to thoroughly understand this construct and give it more attention and investment in order to manage it in a profitable way. Both hotel managers and staff should be able to predict and respond quickly to their customers’ and guests’ needs as well as market trends in order to successfully track changes in those customers’ needs.

Moreover, managers in this sector should create programs or systems for tracking and receiving complaints from customers and guests in order to reduce the number of future complaints and failures. Managers in this sector are also are required to adopt programmes for service recovery in order to keep their customers and guests satisfied. As a result, customers will stay attracted to this sector and will freely spread positive and favourable recommendations to others about this sector. Moreover, in order to improve
the satisfaction of customers and guests, hoteliers in this sector need to get continuous feedback, suggestions, and solutions from their guests and customers.

Since the results of this study conclude that satisfying customers and increasing their behavioural responses (including the intention to retain and make recommendations to others) represents the most significant outcomes of service quality to improve profitability, managers in this sector should know that this impact on profitability occurs through three internal routes. These routes include increasing the number of current customers and guests; attracting new customers through word of mouth; and finally, by increasing the usage or visitation rate of existing customers and guests.

However, managers should know how to manage and improve these three routes effectively and separately. For instance, to increase the number of current customers and guests and their usage and visits, hoteliers should improve and focus on customers' perceptions and experiences of service quality, and use more promotional or loyalty programmes. Clearly, such loyalty programs (e.g. points rewarded to loyal buying customers that are exchanged for complimentary accommodation or services) will build long-term relationships with the existing customer base. On the other hand, in order to increase the number of new customers and guests, hoteliers need to boost their advertising campaigns highlighting the competitive advantages of budget hotels, including consistent service quality, reasonable price, and high value. Such campaigns should lead to attracting new segments of customers that may never have used this sector previously.

Thus, managers in this sector are advised to manage these three outcomes of service quality within the customer satisfaction direction separately. Once that has been accomplished, managers will be able to know at the brand level how many sales they made from their current and existing customers, how many incremental sales were gained from new customers, and how many customers and guests switched to this sector. Thus, hoteliers will be able to identify which route is more profitable and easily achieved and improved.

As outlined earlier in this study, the new trend within the budget hotel sector indicates that many budget hotels are now committing to using service quality as a contemporary
strategy for achieving more brand strength and identity; hence, it is essential for budget hotels to measure their customers and guests' perceptions of service quality in comparison with competitors in the same sector. In other words, asking customers and guests about their perceptions of service quality delivered in a specific hotel in relation to competitors as a comparison standard. This results in powerful information for decision makers at the brand level of budget hotels. As suggested by Babakus et al (2004), measuring service quality according to what competitors are doing should generate useful suggestions and solutions for improvement and changes. Doing so will allow some budget hotels to proceed with some changes and innovations to go beyond their competitors by identifying new trends and unique requirements in the market. Obviously, such comparison will increase practices of the product modification strategy adopted in this sector as discussed previously.

The findings of this study revealed also that staff behaviour and attitude account for a significant contribution and influence on the customers' and guests' satisfaction. This result implies that the budget hotel sector represents a direct contact service setting like other classes of hotels. For this reason, managers in this sector need to focus their efforts and attention on training as well as satisfying their staff in order to enhance service quality delivered, since staffs play an important role in enhancing the operational performance of hotels.

The results of this study indicate also that price charged in this sector does not have a positive significant impact on profitability since the profit margin in this sector is low. Accordingly, managers need to reconsider their pricing policy (room rates) by developing more dynamic price schemes or adopting the revenue management practices in the budget hotel sector. As a result, hoteliers need to reconsider or modify the fixed or transparent price policy adopted in the budget hotel concept in order to maximise the financial benefits of service quality. Accordingly, budget hoteliers need to test whether charging different prices to different customer segments is applicable and possible. Budget hoteliers may also need to charge different prices for leisure travellers in order to attract them to this sector.

Proving the positive and indirect impact of service quality on profitability encourages managers to link and match data available about customers' perceptions of service quality
and satisfaction with their accounting data on a regular basis. Having made this connection, managers will be able to document and track the financial impact of service quality in performance, and thus they will be able to justify to shareholders and owners any expenses required for further improvement in service quality features and attributes in this sector.

Having shown the importance of the service quality on profitability in this sector, it is worth saying that this importance does not mean that hoteliers in the budget sector should improve quality of service at any cost. In contrast, managers should know that there is a limit to spending, and exceeding this limit will diminish returns and profits. In line with that, hoteliers should not exceed customers' expectations and needs by enhancing their service quality.

The findings of this study indicate that improving profitability through service quality is a long-term process and needs several and sequential phases of impacts and effects; therefore, managers should be patient to evaluate and recognise the financial impact of service quality. The impact of such programmes takes a long time to be recognised; managers must understand this, otherwise they will draw the wrong conclusion and take incorrect and hasty actions. It is also important for hoteliers to know that this relationship is influenced by other factors (economic conditions, location, staff training, and advertising) that can change or diminish the financial impact of service quality. Hence, management should consider these additional factors when tackling and explaining this relationship.

However, the positive impact of service quality on profitability in this study means that budget hotels should keep focusing on service quality improvements. Thus, budget hotels should keep this as a top priority and strategy in this competitive environment. Because the relationship between service quality and profitability is a complex, indirect, and long-term relationship, management must be prepared to wait for the gains from investments in service quality.

In terms of practical implications for the budget hotel chain under investigation, the findings of this study reveal that the first dimension of service quality (physical quality) was attributed lower positive perceptions or importance compared to the second
dimension of quality (staff behaviour and attitude). Nevertheless, the findings of this study indicate that this tangible and physical aspect of service quality has a stronger impact and a greater contribution and influence on customer satisfaction than the second dimension (staff behaviour and attitude). Thus, this budget hotel chain is required and advised to pay more attention to improving the tangible aspect of service quality to enhance their guests' satisfaction and perception of that service quality. In other words, some reasonable efforts and investments are needed to reveal the tangible aspect of service quality, such as replacing, adding or refurbishing some of the physical features of the budget hotel chain in guest rooms and other areas. Given the potential outcomes of making these improvements, the service quality in this budget hotel chain will meet customers' expectations and may exceed offers of other competitors in the same sector.

The findings of this study also reveal that business travellers account for the majority of the customer segmentation. For this reason, this budget hotel chain should consider adding some extra facilities beyond the meeting rooms they currently offer in some of their units, such as, adding modern communication and visual equipments and tools. As another aspect of services offered, this budget hotel chain is advised to offer free wireless access to the Internet in all guest rooms, since the budget hotel company is currently charging their guests for using this service. Doing so can help the company gain more business and sales especially from business travellers. In this regard, the marketing company, Mintel (2007), found in their review of budget hotels in UK that the Wi-Fi service now is a common feature and service in the budget hotel sector.

For this hotel chain in particular, the results do not show a significant association between quality of service, price, and profitability. Accordingly, this hotel chain needs to develop and adopt a more flexible pricing policy by gaining a greater understanding of customers' perceptions and responses to the average prices charged in the chain. In this sense, the management of this hotel chain needs to understand their guests' perceptions of prices in order to charge suitable and fair prices that will retain their customers as well as achieve a profitable margin of turnover. Although the budget hotel in the present study charges different prices for rooms located in different locations across the country, as well as different prices for weekday and weekend stays, revenue management and more flexible prices are needed to charge prices that are compatible with high quality and consistent
customer service quality delivered and perceived by their guests as shown previously in this study.

Although the present study assured the need for developing and using more dynamic performance measurement systems in order to face competition and changes within the hotel industry, the balanced scorecard system adopted and used in the study under investigation represents a basic, static, and inflexible performance measurement system. In other words, the discussion in chapter 4 highlighted the need for and urged the adoption of more highly dynamic systems for measuring performance within the hotel industry. Thus, the budget hotel chain under investigation and hoteliers in the entire market should adopt contemporary models, practices, and processes for measuring performance. For example, Cruz (2007) suggested using rolling forecasts to increase the planning activities performed by managers in the hotel industry. Another alternative perspective and suggestion by Phillips (2007) highlights the need to use and implement the balanced scorecard system as a strategic control tool to achieve more positive and successful outcomes. Thus, the hotel chain under investigation needs to upgrade the performance measurement system it currently uses, which is based on using three colours (red, amber and green) as indicators of achievement for targets and performance in several areas.

Moreover, the current practices used and adopted in the budget hotel chain under investigation imply that the results and outcomes of their balanced scorecard system is used and reviewed by top management only; therefore, it is important and useful for the budget hotel chain to inform and disseminate the results and outcomes of the BSC system concerning the link between service quality and profitability not only to top management, but also to all other levels as well, in order to get their support, feedback, and suggestions for improvement. In other words, saving and storing the balanced scorecard data centrally, as is currently done, without publishing results to other levels or units in the budget hotel chain, may prevent a better understanding of outcomes and results and potential improvements of performance. On the other hand, sharing the results can help top management and users of this system to develop better measures and strategies for improving the hotel's profitability; doing so will also make it easier to review these measures on a continuous basis in response to changes in the real market. Accordingly, this budget hotel chain is advised to use its internal network on a frequent basis to share
and update results and ideas with staff. In this respect, Phillips and Louvieris (2005), in their effort to build a suitable balanced scorecard system for enterprises in the hospitality and tourism industry, they emphasised that staff should share and approve the performance measures that the hotel formulates and uses.

Finally, the current practices of measuring service quality in this budget hotel chain are somehow simple and basic since they are based on using a checklist reviewed and filled out by an auditing team and general managers of each unit. However, the latest trend of measuring service quality in the hotel industry involves a hierarchical concept as introduced before in the literature review of this study by Wilkins et al (2007). Therefore, this company and the whole hospitality industry are encouraged to implement this contemporary and comprehensive approach for measuring service quality in their establishments.

9.6 Limitations of the Study
Although the current study highlights some justifications, advantages and contributions of the methodology used and the results found, some limitations were beyond the scope of the current study which may affect the strength of the findings. Points presented below discuss some limitations raised and suggestions for future research.

First, although the research sample in this study is considered acceptable for statistical criteria, because it focuses primarily on one sector within the hotel industry, i.e., a single firm or single case, this case may not represent the overall industry. Hence, this study recommends future research to retest this relationship in different hotel sectors, including the five-star hotels. Moreover, this study was undertaken only in the UK; future research should be done in different countries to test whether cultural differences will modify the results.

The second limitation of the study comes from addressing only the service provider’s perspective for evaluating customers’ perceptions. Accordingly, this study advises future research to evaluate service quality performance and the other variables from the customers’ perspectives by using guest-reported quality perceptions.

Third, this study used multiple regression analysis for testing the impact of service quality on profitability. However, Structural Equation Modelling (SEM) serves to test the total
direct and indirect impact of variables in the research model simultaneously, measuring the fit of the entire model and between variables (Baron and Kenny, 1986). This study did not use SEM according to its complexity in terms of usage and assumptions required to run such analysis. So, future research is recommended to test a similar research model by using SEM.

Finally, due to the literature available, the research objectives and the time frame, the scale used for measuring demand and capacity in this study was not well developed and purified for measuring and capturing the variables in this hotel sector. In other words, the factor analysis and reliability tests indicated poor results for the use of the scale for measuring the budget hotel's ability to manage demand and capacity. Accordingly, future research is encouraged to pay more attention to understanding the managing demand and capacity activities in the budget hotel sector in particular in order to develop a valid and reliable scale. To do so, more qualitative and quantitative efforts are needed and required for the scale's improvement.

9.7 Directions for Future Research
Service quality and business performance measurement models are the focus of considerable attention in academic and practitioner communities. Service quality models, as well as business performance measurement systems, make significant contributions to the management of hospitality firms in general and hotels in particular. However, the relationship between service quality and profitability is still not clearly understood. Although this thesis has addressed this issue by introducing and testing a conceptual model and the hypothesized relationships between variables, future research needs to be subjected to experimental testing methods.

For the contribution of this research to be realized, it is essential that the measurement systems and models used to be relevant and appropriate for the environment and strategies of hotel firms. Given the dynamic and rapidly changing environment in which most hotel firms compete, it is important that hotel firms effectively manage their businesses performance measurement systems so that the company's decisions are based on the information that is relevant to the issues of current importance. Hence, future researches have to develop, improve and use dynamic performance measurement systems that are more relevant to the industry's environment and cases.
Conclusions and Recommendations

The service quality literature asserts that perceived quality is generic but empirical tests of the current service quality models have produced inconsistent results regarding the validity of the generic nature of service quality dimensions in the hospitality industry. To date, studies have failed to determine the exact nature and number of dimensions that are applicable to all hospitality firms in general and hotels particularly. It seems that a two-dimensional model of service quality – physical quality and interaction quality – is most suited to measuring service quality in the hospitality industry. However, future research on the relationship between service quality and profitability should address this issue in the budget hotel sector specifically.

Furthermore, because firms in the hospitality industry are highly fragmented and service-oriented, testing the relationship between service quality and profitability may require including different and new variables such as branding. Researchers and future studies should consider including more potential variables in order to expand the understanding of the relationship between these two concepts across various hotel sectors.

Finally, some specific questions that need to be answered are: What dimensions and aspects of service quality are most important for customer retention? Where should companies invest in service quality to have the greatest impact on customer satisfaction, customer retention, and financial outcomes? How can existing customers be identified and segmented in terms of profitability? How can potential customers be identified in terms of profitability?

To conclude, this study has spent proper efforts on the relationship between service quality and profitability in the UK budget hotel sector. This study found support for the theoretical and empirical evidence in terms of antecedents and consequences of service quality construct in the budget hotel sector. This study addressed the critical factors involved in this relationship. Based on the two sets of findings, the results support the indirect positive impact of service quality on profitability. Hence, the financial profitability of hotels in general and the budget hotel sector in particular is a function of the service quality policy and its marketing outcomes. Thus, the current study illustrates how service quality can be transformed into profit through a chain of impacts between some variables.
In this sense, this study identified which path or direction in the conceptual framework leads to improved and increased profitability in the budget hotel sector in particular. More interestingly, the data analysis confirmed that customer satisfaction and its consequences (customer behavioural response) represent the major path or direction to improve profitability in this hotel sector. So, hotels and other service organizations should pay more attention to this activity, as well as the interrelationships between the other variables involved, in order to improve the financial outcome of service quality on performance.
References


References


D.Zeglat 2008

References


Cooper, R., Kaplan, R., Maisel, L., and Oehm, R. (1992) Implementing Activity-Based Management: Moving From Analysis to Action, Montvale, NJ: IMA.


Dey, I. (1993) Qualitative Data Analysis, First Published, Routledge, USA.


D.Zeglat 2008

References


Guba, E. and Lincoln, Y. (1994) "Competing Paradigms in Qualitative Research", in Denzin, N. and Lincoln, Y. (ED), Handbook of Qualitative Research, Sage Publication, USA.
References


References


Key Note; (2006) *Hotels*, Edited by Philippa Drewer, 21st Ed, Hampton: Key Note Ltd.


References


References


D. Zeglat 2008

**References**


References


Appendices
Appendix 1

A Sample of Interview

Name: Mr Abed Aziz Salhab
Position: Director of Finance/ Sheraton Amman
Number of years of experience: 10
Date of interview: 29/03/2006

Q.1 How would you define profitability of a hotel from your point of view and how you measure it?

According to the profit and lost statement perspective, the meaning of profitability is revenues minus expenses. From my viewpoint as a financial manager, the hotel’s profitability is generating revenues as much as I can as well as managing and controlling costs in order to get more profits for my hotel.

To explain more, the highest profits in general or the highest gross operating profit (GOP) I get, the highest departmental profitability I get in my hotel. As a result of achieving profits, the hotel will get some advantages as following:

- Provides an indicator for a good performance for the organization at all.
- Provides a valid indicator of the effective and professionalism of the financial department.
- Increase the bonus amount for the executive committee.
- Increase the awards and returns for the shareholder.
- Increase the ability to pay the management fees.
- Increase the value of stocks.
- Increase the continuity of the company (hotel) i.e. higher profits, higher reserves which in turn lead to expand the hotel’s operations, innovation and satisfy employees through paying good compensation and rewards.

Generating more revenues is a basic and a fundamental tool for improving the hotel’s profitability. As a result of getting more profits, the company will increase the ability to compete in the marketplace which is going more complex every day. To increase the hotel’s revenues and
profitability, the management has to do three options; firstly, expand and create new generating centres or new outlets such as opening new restaurants and offering new services. Secondly, raise the average daily rates for rooms. Finally, increase the occupancy rate in the hotel.

To do so in the high competition marketplace (the previous three options), a management should provide professional service team, customer loyalty programs, new and high quality services, good brand name (how can I differentiate my self over others). In other words, to improve the revenues and profits the management should provide an excellent service in order to get loyal customers and high occupancy rate.

All activities in the hotel are not enough to improve the hotel’s profitability unless a hotel provides a high quality and amazing service. Thus, the guest when stay in the hotel shouldn’t feel paying money to get a good service (financial transaction). The new concept of services in hotel is not just accommodation and paying fees for this service. On contrast, the guest should feel and live a cosy atmosphere and friendly transaction with staff to let the guest feel that he/she in his/her home. In other words, the guest should have a human transaction not financial transaction for getting these services in a hotel. When a hotel management can do so, we can differentiate ourselves from competitors and others in services offered to the customers and guests.

In the same time, a management should motivate its staff to serve guest and customers extensively because the hotel industry depends comprehensively on offering some services such as; (rooms, food and beverage, gym, business centres, etc). Namely, the most important factor in performing and offering these services in the industry as well as other service industries such as banks and health care focused on the human activities and communications between customers and employees.

Q.2 According to your opinion, what factors affect the hotel’s profitability?
There are two groups of factors affecting the hotel’s profitability; external factor and internal factors. Besides different factors such as; number of competitors, number of properties, regulations, events at the country level and seasonality, the political factor represents the most important external factor affect profitability. For example, what is going in Iraq and west bank have a major influence on what’s going in Jordan. Moreover, the bomb attacks occurred in November last year destroyed and cancelled some events in the country. To be more precisely, right now the hotel sector still suffering from this attack and in our hotel in particular approximately (20%) to (30%) of the occupancy percentage has been lost.
Thus, the hotel industry will be related to the political and environmental factors because such industry depends on visitors, passengers, foreigner businessmen and embassies more than local people. On the other hand, the internal factors have numerous influences on the hotels' profitability such as; the average room rate, kind and variety of services, sales team efforts, staff motivation, job satisfaction, strategies created and adopted by management and hotel’s brand name. In other words, hotels with well-know brand name will have more business in the marketplace.

Q.3 What is the nature of relationship between service quality and profitability in the hotel industry?
Basically, service quality has a positive and direct impact on hotel’s profitability. Unfortunately, I’m not sure about what percentage or the extent to which these concepts are related or correlated to each other. In other words, the influence of service quality on the hotel’s profitability is exist but without any measurement or percentage of this effect. Anyway, the impact of service quality on profitability is high in this industry.

Q.4 What are the financial benefits or outcomes of service quality activities in the hotel industry?
As mentioned above, service quality helps the hotel to let its customers and guests loyal to this particular hotel, encourage them to repeat their experiences with this hotel, attract new customers and guests through the recommendations of the current guests, improve the hotel’s reputation in the market place. As a result of these advantages, a hotel will have more business and operations in the future.

To explain the mechanism for that, achieving high level of service quality and satisfying the guests’ needs act the most important reasons for retaining and paying for a hotel. Clearly, the pure service (accommodation, food and beverage, etc) in hotels represents the main source for generating revenues and profits. According to the offering of this service, a hotel will generate revenues and profits. Obviously, offering more reliable and excellent services will bring more revenues and profits for the hotel. Thus, the higher service quality, the more revenues and profitability a hotel can get and vice versa.

Q.5 In my conceptual framework, there are three paths or directions for the relationships between high levels of service quality and profitability as following;
1. Charging Premium price
2. Customer emphasise (increasing revenues)
3. Operations emphasis (increasing productivity)
First of all, offering and achieving high level of service quality surely will enable a hotel to charge a premium price over competitors and other organization working in the same market place. This benefit of the service quality helps a hotel to get more revenues without affecting its market share (occupancy rate).

Secondly, there is no doubt that good and high level of service quality will satisfy guests and customers which in turn will increase the hotel’s occupancy. As a result of the high occupancy, a hotel will get more margins and profits. I believe that this direction is the most important and profitable direction of the relationship between service quality and profitability in the hotel industry. To put it more simply, high level of service quality is what all guests and customers are looking for; otherwise a hotel will loose its business.

Finally, high level of service quality doesn’t mean high or low cots (inputs). Yes if you need high standard of service you have to spend more but not to spend too much. By this meant, when you spend for improving service quality you have to spend rationally and reasonably not seeking for spending without objective. In the hotel organization, the financial controller plays a significant role to minimize and control expenses not just cut expenses in order to offer services at acceptable expenses and prices. Therefore, in my opinion I think that service quality has a positive affect and correlation with productivity because service quality doesn’t mean at all increase expenses or inputs especially when you have a loyal and satisfied staff.

Briefly from this conceptual framework, the direct and the fast impact of service quality is the premium price. On contrast, at the long term perspective, the customer emphasis (customer satisfaction direction) has the most powerful and profitable impact on a hotel’s profitability.

In fact, your conceptual framework is compatible 100% with a five star luxury hotel offers an excellent service. For example, the Four Seasons hotel in Amman has all dimensions you have included in your model. In other words, this hotel offers unbelievable service quality and charge the highest room rate in the market. Despite the average room is quite expensive comparing other hotels, the occupancy rate for this hotel is the best in the market with high annual profits.

In summary, the main tool for achieving good financial position is offering an excellent and high level of service. To do that, you have to differentiate yourself from others by adopting and practicing high quality of service standards.
### Appendix 2

**List of Codes**

<table>
<thead>
<tr>
<th>No</th>
<th>Code</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Def/Prof</td>
<td>Definition and meaning of profitability.</td>
</tr>
<tr>
<td>2</td>
<td>Ben/Prof</td>
<td>Benefits and advantages of profitability.</td>
</tr>
<tr>
<td>3</td>
<td>Res/Prof</td>
<td>Resources of profitability.</td>
</tr>
<tr>
<td>4</td>
<td>Det/Prof</td>
<td>Determinants of profitability.</td>
</tr>
<tr>
<td>5</td>
<td>Det/Prof-Ex</td>
<td>External determinants of profitability.</td>
</tr>
<tr>
<td>6</td>
<td>Det/Prof-In</td>
<td>Internal determinants of profitability.</td>
</tr>
<tr>
<td>7</td>
<td>Nat/Rel</td>
<td>Nature of relationship between service quality and profitability.</td>
</tr>
<tr>
<td>8</td>
<td>Ben/Ser</td>
<td>Benefits and outcomes of service quality.</td>
</tr>
<tr>
<td>9</td>
<td>Rel/SerPro-Pp</td>
<td>Relationship between service quality and profitability through premium price.</td>
</tr>
<tr>
<td>10</td>
<td>Rel/SerPro-Ce</td>
<td>Relationship between service quality and profitability through customer emphasis.</td>
</tr>
<tr>
<td>11</td>
<td>Rel/SerPro-Pro</td>
<td>Relationship between service quality and profitability through productivity.</td>
</tr>
</tbody>
</table>
Appendix 3

Data Discussion and Analysis

**Def/Prof**

This code refers to definitions and perceptions of profitability concept from the interviews' perspectives. The first participant mentions that profitability concept implies or means "revenues minus expenses". From this quotation, the profitability concept calculates all costs and expenses related to sales in order to produce the net profit. Therefore, high revenues lead to high profitability. According to this view, finding out profitability is based on the profit and lost account.

In addition, the second participant highlights that revenues earned in a specific financial period which usually one year, indicate and determinate the rate of profitability. To gauge this rate, costs and expenses should be taken. The most popular indicator for measuring profitability in the hotel industry is the gross profit margin (GPM). Using such indicator, allows a company to evaluate its ability to generate profits as well as benchmarking its performance with other companies in the industry.

The third participant shows profitability as "how much income or turnover generated from the capital invested retained after paying all costs and expenses". Clearly, such definition of profitability has the same interpretation. Thus, the profitability concept refers and means how much a hotel get after covering all costs and expenses. Moreover, hoteliers, consider the gross operating profit (GOP) one of the most powerful indicator and metrics for measuring hotel's profitability. Finally, the fourth informant says that profitability is how much and how long you able to stay in the market after paying and covering costs and expenses. To conclude, profitability definitions from all participants highlight two components; revenues and costs.

**Ben/Prof**

This code implies benefits and advantages of achieving high profits. Only the first interviewee mentions these advantages. Clearly, high percentage of profitability proves the hotel's efficiency and effectively, increases the potential dividend, reward for shareholders, increases the ability of a hotel management to open new outlets or expand them, improve the continuity of the hotel in the marketplace, etc. Thus, improving the hotel's profitability brings financial and non-financial benefits for hotel. (Please see appendix 2).
This code illustrates what hotels' activities and resources contribute and generate revenues and profits for hotels. The first participant reveals three strategies for increasing profitability; expanding or creating new outlets, raising the room rates and increasing the occupancy rate. Obviously, these strategies need different set of actions. For example, raising the room rate conflict with the increasing the occupancy rate strategy. Therefore, a hotel management should make balance between all of these strategies. In addition, the first participant declares the key resources for generating profits in the hotel setting such as; rooms, food and beverage, business centres and gym centre. In addition to rooms and food and beverage revenues, the third participant states other resources such as; shops rental and parking revenues. Thus, rooms and food and beverage still act the core service in the hotel industry.

This code illustrates what factors can affect the hotel’s performance in general and profitability in particular. The literature refers to this factor as determinants of performance and profitability. Obviously, these determinants divided by the interviewees into two groups as following;

The external determinants include factors located in the external environment. The first participant displays some factors; political events, number of competitors, regulations, seasonality and events at country level. This participant emphasizes the importance of the political situations. In other words, the political situation has the major impact on hotel’s profitability. For instance bomb attacks and terror threats cause declining in percentages of occupancy. Moreover, the second participant underlines the political events and security situation as a critical factor affecting profitability. The reason for that, any customer or guest will not go to insecure destinations. In contrast, customers, guest, travellers and businessmen need safe and secure atmosphere. Another external factor mentions by this participant, the nature of activities and economic state in the country. To put it more simply, developed and manufacturing countries have more opportunities more than developing countries for attracting customers, visitors and businessmen. Moreover, the third participant emphasizes the importance of the political situation as well in term of determining the hotel’s performance and profitability. Finally, the forth interviewee mentions that this factor (political situation) has the massive impact in thus industry.
Dislike external determinants, internal factors located in the hotel's environment and control. Therefore, such factors have a direct and fast effect on the hotel's ability to generate revenues and profits. The first participant cites some factors such as; service quality, bundle of service offered, average room rate, sales team efforts, staff motivation, job satisfaction and brand name awareness and familiarity by customers. Furthermore, the second participant highlights some different factors such as; location, quality of service supplied, price. In addition, the third participant mentions the same elements like service quality, price of services and brand name familiarity and popularity. As previously stated, positive brand name of the hotel plays a significant role for attracting customers and guests. In other words, hotels with well known, positive and popular brand name help to achieve and attract more business. Finally, the fourth participant highlights some dimensions (service quality, variety of services, staff behaviour) but he gives too much attention for brand name according to its influence upon customers and guests.

This code shows the nature and the direction of relationship between service quality and profitability. The first respondent assures that service quality movement and activities have a positive and direct impact on the hotel's profitability. By this is meant, offering high standards of quality of service will definitely increase profits without any explanation for the significant between these two variables. The second participant confirms the positive relationship between service quality and profitability in such industry as well as other industries. Furthermore, this respondent supposes that delivering poor service quality will diminish and decline profits. Moreover, the third participant briefly states that quality of service has a positive and indirect relationship between service quality and profitability. That is, offering high level of service quality will helps gradually a hotel to increase its profits. Finally, the fourth informant admits that service quality has a positive and direct relationship with the hotel's profitability. As mentioned above, the relationship between service quality and profitability in the hotel industry is compatible with the literature.

Such code displays benefits or outcomes of achieving and supplying high level of service quality. The first respondent stresses the importance of service quality to retain and attract new customers for a particular hotel. As a result, good quality for services in particular hotel will improve customer satisfaction and loyalty as well as reputation of this hotel. Thus, this particular hotel will have more business and revenues. The second participant shows customer satisfaction as the most and the first financial outcomes of offering high service quality. Due to customer satisfaction, the market share
of a particular hotel will be increased. As a result, revenues will be developed at semi-fixed level of costs. Thus, the hotel's profitability ratio will be improved. To put it more simply, high standards of service quality leads customers and guests to justify what they pay for and let them feeling satisfy i.e. higher service quality, higher customer satisfaction, higher revenues and market share, higher profitability. According to this respondent, the customer satisfaction as a result of good service quality will improve 100% the hotel's profitability. The third participant confirms that hotels use service quality to improve profits through customer satisfaction and retention. According to his view, this is the logic theory of the relationship between service quality and profitability in the hotel industry. Finally, the fourth informant mention just for customer loyalty as a key outcome of service quality. In addition, loyal customer can expand the hotel's market share through spreading good reputation about a particular hotel.

- **Rel/SerPro-Pp**
  This code explains the relationship between service quality and profitability through premium price. The first respondent assures that offering high and consistent level of service quality allows a hotel to charge prices more than competitors in the market. The benefit of charging higher prices is increasing revenues and margins without affecting the current market share. In addition, this respondent says that premium price is a first and fast outcomes and benefits of high service quality policy and movements. The second participant has no consideration for such relationship through premium price. The third participant agrees strongly that offering high service quality lead to charge prices more than others. In addition, the third participant justifies charging premium prices in this sentences "Due to maintenance and improvement expenses in order to supply excellent service quality, a hotel can charge premium prices". According to high level of service quality, customers and guests will still dealing with a particular hotel even when you raise or charge high prices. In other words, high standards of service quality help to have good relationship with customers and customers without negative reaction for prices. To charge premium prices, a hotel management has to investigate all current and potential segments in the market to select a suitable and profitable segment. Finally, the last participant confirms this direction. As mentioned above form all respondents, premium price links and leads to get more profits after offering high service quality.

- **Rel/SerPro-Ce**
  This code examines the relationship between service quality and profitability through customer emphasis i.e. increasing customer satisfaction and customer retention. Obviously, this relationship means and focuses on the link between the hotel and its customers and guests. The first interviewee has the same opinion that good and high service quality means and leads to satisfy customers and
guests. As a result of that, repeated customers and guests will attract new customers. In other words, satisfied customers will increase the market share, margins and profits. The second respondent considers this direction of the relationship is the most powerful and logical direction. Thus, satisfied customers bring regular and more revenues for hotels. Additionally, the third participant considers this direction as the upmost goals for any hotel. Lastly, the fourth interviewee declares that customer satisfaction direction has 80% in term of the influence of service quality on profitability. As previously mentioned, this direction in such industry is valid, applicable and compatible to the literature.

Rel/SerPro-Pro
This code discusses the link between service quality and profitability through productivity. The first participant mentions that offering high level of service quality doesn’t mean more inputs or costs. Offering high level of service quality requires more attention and expenses but not paying too much without consideration. Thus, a hotel can offer good and high service quality at acceptable and rational level of inputs such as material or labour. On contrast, the second precipitant supposes that offering high service quality requests more and high expenses and materials because customers are looking for superior service. Thus, service quality according to the second interviewee has a negative relationship with productivity because customers will pay high and premium prices. The third participant says that each hotel should be able to provide a consistent service quality without delay or mistakes. As a result of that, resources and inputs should be exploited properly. In other words, offering high level of service quality means managing all elements and outputs economically in order to improve productivity. Thus, according to the third participant, service quality has a positive relationship with productivity. Finally, the fourth informant agrees with this direction as long as a hotel able to mange its demand and capacity. Clearly, such relationship between service quality and profitability through productivity has two views or options; positive and negative.
Dear Sir/Madam,

I am a PhD student in the School of Management at the University of Surrey. I'm investigating the relationship between the quality of service and profitability of hotels in the UK budget hotel sector. My research will contribute to the understanding of the link between service quality and financial performance in the hotel industry.

It should take you only a small amount of time to complete this questionnaire. Your response and participation form a critical part of the success of my research. I would be very grateful if you could complete and return this questionnaire using the prepaid envelope enclosed. I would like to reassure you that your response will be kept strictly confidential and will only be used for the purposes of this academic research.

Kindly regards.

Dia Zeglat
PhD researcher
School of Management
University of Surrey
Guildford, Surrey
UK
GU2 7XH
Part I. About your Hotel’s Characteristics

**Direction:** This part is designed to obtain information about your hotel. Please answer the questions below by placing a mark (X) in the appropriate option.

1. How would you categorize the location of your hotel?
   - [ ] London
   - [ ] Other city centre
   - [ ] Provincial town centre
   - [ ] Roadside
   - [ ] Airport

2. How many years has your hotel been in operation?
   - [ ] 1-3
   - [ ] 4-6
   - [ ] 7-9
   - [ ] 10 and above

3. How many rooms are there in your hotel?
   - [ ] 1-25
   - [ ] 26-50
   - [ ] 51-100
   - [ ] 101-150
   - [ ] 151-200
   - [ ] 201 and over

4. Please estimate the percentage of revenues generated on average over the last three years from the following customer segments?

<table>
<thead>
<tr>
<th>Segment</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business travellers</td>
<td></td>
</tr>
<tr>
<td>Leisure travellers</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100%</td>
</tr>
</tbody>
</table>

5. How would you rate your guests’ feelings about your hotel’s brand name?

   - [ ] Very Unfamiliar
   - [ ] Very Inexperienced
   - [ ] Not knowledgeable at all
   - [ ] Very Familiar
   - [ ] Very Experienced
   - [ ] Very Knowledgeable

383
Part II: About your Hotel’s Service

Q.1 Direction: The statements presented below refer to your perception of *service quality performance and guests’ experiences* in your hotel. After each statement, there are five numbers from (1) to (5). Please circle the number that best describes your opinion. The higher the number means the more you agree with the statement. The lower the number means the more you disagree with the statement. If you feel your agreement is between these two extremes, please pick any number from within the scale.

<table>
<thead>
<tr>
<th>Service Features</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our decor is beautifully co-ordinated with great attention to detail.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our hotel is clean.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our hotel is tidy.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our hotel has visually attractive rooms</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our staff are competent and display effortless expertise when serving to the guests</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our staff anticipate the guests’ needs.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our staff are helpful and friendly.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Our staff carefully listen to the guests</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.2 Overall, how would you rate the guests’ experiences with your hotel? Please indicate your opinion on the following scales by circling a suitable number for you.

<table>
<thead>
<tr>
<th>Very Dissatisfied</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Very Satisfied</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Very Displeased</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>Very Pleased</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Very Negative</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>Very Positive</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

384
Q.3 Overall, how likely is that the guests will return to this hotel? Please indicate your opinion on the following scale by circling a suitable number for you.

<table>
<thead>
<tr>
<th>Extremely Unlikely</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Extremely Likely</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.4 Overall, how likely is that the guests will recommend this hotel to others? Please indicate your opinion on the following scale by circling a suitable number for you.

<table>
<thead>
<tr>
<th>Extremely Unlikely</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Extremely Likely</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.5 Overall, how would you rate the guests' perceptions of the price paid for accommodation in your hotel compared to similar hotels? Please indicate your opinion on the following scale by circling a suitable number for you.

<table>
<thead>
<tr>
<th>Lower Than Similar Hotels</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Higher Than Similar Hotels</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Q.1 **Direction:** The following questions aim to compare the financial performance of your hotel on average over the last three years *against other competitor hotels of similar category* in your area. To do that, please circle the number that best describes your assessment of your hotel’s performance. Rating (1) indicates *much worse than similar hotels* and rating (7) indicates *much better than similar hotels*. If you feel your agreement is between these two extremes, please pick any number from within the scale.

<table>
<thead>
<tr>
<th>Financial Performance Indicators</th>
<th>Much Worse</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th>Much Better</th>
</tr>
</thead>
<tbody>
<tr>
<td>How would you rate your hotel’s revenue per available room (REVPAR)* in the last 3 years <em>against</em> similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>* (REVPAR indicates revenues generated from available rooms).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s profitability measured by return on capital invested (ROCE) ** in the last 3 years <em>against</em> similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>** (ROCE indicates revenues generated from all capital employed)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s market share*** in the last 3 years <em>against</em> similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>*** (Market share refers to the proportion of actual rooms sold in the marketplace)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s labour productivity**** in the last 3 years <em>against</em> similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>**** (Labour productivity refers to the percentage of revenues to payroll expenses)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.2 Please estimate the average percentage of repeated customers who visited this hotel since 2003: %

Q.3 Please estimate the percentage of your hotel’s revenue generated from the repeated customers who visited this hotel since 2003: %
**Q.4 Direction:** This section looks at the hotel’s ability to manage different patterns and fluctuations in demand and its capacity. To do that, please circle the number which indicates the extent to which you agree with the statement. Rating (1) means you *Strongly Disagree* with the statement and (5) means you *Strongly Agree*. If you feel your agreement is between these two extremes, please pick any number from within the scale.

<table>
<thead>
<tr>
<th>Managing Demand &amp; Capacity</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>In this hotel, we charge full prices during peak periods.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we modify the service offering in the slow seasons to attract new market segments e.g. rent rooms for family market segment.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we increase promotions during slow periods.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we charge lower prices during slow periods</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we communicate with guests to let them know the times of peak demand.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we hire part-time employees during peak demand</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we rent or share equipment at times of peak demand</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we request overtime work at times of peak demand</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we train employees in the periods of slow demand to enable them to do a variety of tasks.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>In this hotel, we schedule downtime during off-peak periods</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
</tbody>
</table>
Part IV. About You

Direction: This part is designed to get information about you. Please answer the questions below by ticking (X) in the appropriate option.

Q.1 Are you?

☐ Female ☐ Male

Q.2 Please indicate your age group.

☐ 25-34 ☐ 35-44

☐ 45-55 ☐ 56 and over

Q.3 What is your educational level?

☐ Secondary school

☐ College Diploma / Professional qualifications

☐ Undergraduate degree

☐ Postgraduate degree

Q.4 How many years have you been working in this hotel?

☐ Less than one year ☐ 1 to 2 years

☐ 3 to 5 years ☐ 6 to 10 years

☐ 11 to 15 years ☐ 16 and over

Q.5 Please print your job title?

Q.6 How many years have you been working at this level in the industry?

☐ Less than one year ☐ 1 to 2 years

☐ 3 to 5 years ☐ 6 to 10 years

☐ 11 to 15 years ☐ 16 to 20 years

Thank you for your contribution to this research
Dear Sir/ Madam,

I am a PhD student in the School of Management at the University of Surrey. I’m investigating the relationship between the quality of service and profitability of hotels in the UK. My research will contribute to the understanding of the link between service quality and financial performance in the UK budget hotel sector, the results of which will be shared with Hotel Company supporting this study. The University of Surrey has a long-standing relationship with your company, and I have already been working with XXXX. I am now asking for your support in completing this short questionnaire.

It should take you only a small amount of time to complete the questionnaire. Your response and participation form a critical part of the success of my research. I would be very grateful if you could complete and return this questionnaire via email to me at: D.Zeglat@surrey.ac.uk. I would like to reassure you that your response will be kept strictly confidential and will only be used for the purposes of this academic research. I understand that this is a busy time of year for you, but I would be grateful if you could return the questionnaire by the 31 of March, 2007.

Kind regards.

Dia Zeglat
PhD researcher
School of Management
University of Surrey
Guildford, Surrey
UK
GU2 7XH
Part 1. About your Hotel’s Characteristics

Direction: This part is designed to obtain information about your hotel. Please answer the questions below by placing a mark (X) in the appropriate option.

Q.1 How would you categorize the location of your hotel?
- [ ] London
- [ ] Motorway
- [ ] Other city centre
- [ ] Airport
- [ ] Provincial town centre
- [ ] Rural/countryside
- [ ] Other

Q.2 How many years has your hotel been in operation?
- [ ] 1-3
- [ ] 7-9
- [ ] 4-6
- [ ] 10 and above

Q.3 How many rooms are there in your hotel?
- [ ] 1-25
- [ ] 101-150
- [ ] 26-50
- [ ] 151-200
- [ ] 51-100
- [ ] 201 and over

Q.4 Please estimate the percentage of revenues generated on average over the last three years from the following customer segments?

<table>
<thead>
<tr>
<th>Segment</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business travellers</td>
<td></td>
</tr>
<tr>
<td>Leisure travellers</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100%</td>
</tr>
</tbody>
</table>

Q.5 How would you rate your guests’ awareness of the hotel’s brand name?

- [1] Not at all aware
- [2] 1
- [3] 2
- [4] 3
- [5] 4
- [6] Very aware
- [7] 5
Part II: About your Hotel’s Service

Q.1 Direction: The statements presented below refer to your perception of service quality performance and guests’ experiences in your hotel. There are five numbers from (1) to (5). The higher the number means the more you agree with the statement. The lower the number means the more you disagree with the statement. If you feel your agreement is between these two extremes, please pick any answer from within the scale.

<table>
<thead>
<tr>
<th>Service Features</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our decor is well co-ordinated.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our hotel is clean.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our hotel is tidy.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our hotel has visually attractive rooms.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our team members are competent and display effortless expertise when serving the guests.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our team members anticipate the guests’ needs.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our team members are helpful and friendly.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Our team members listen carefully to the guests.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

Q.2 Overall, how would you rate the guests’ overall experiences with your hotel? Please indicate your opinion on the following scales by clicking a suitable number for you.

Very Dissatisfied 1  2  3  4  5  Very Satisfied

Q.3 Overall, how likely is that the guests will return to this hotel? Please indicate your opinion on the following scale by clicking a suitable number for you.

Extremely Unlikely 1  2  3  4  5  Extremely Likely
Q.4 Overall, how likely is that the guests will recommend this hotel to others? Please indicate your opinion on the following scale by clicking a suitable number for you.

Extremely Unlikely 1 2 3 4 5 Extremely Likely

Q.5 Overall, how would you rate the guests’ perceptions of the price paid for accommodation in your hotel compared to similar hotels? Please indicate your opinion on the following scale by clicking a suitable number for you.

Lower Than Similar Hotels 1 2 3 4 5 Higher Than Similar Hotels

Part III. About your Hotel’s Performance

Q.1 Direction: The following questions aim to compare the financial performance of your hotel on average over the last three years against other competitor hotels of similar category in your area. Rating (1) indicates much worse than similar hotels and rating (7) indicates much better than similar hotels. If you feel your agreement is between these two extremes, please pick any answer from within the scale. To do that, please click the answer that best describes your assessment of your hotel’s performance If you have not been at your hotel since 2003, please give your best estimate
<table>
<thead>
<tr>
<th>Financial Performance Indicators</th>
<th>Much Worse</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>Much Better</th>
</tr>
</thead>
<tbody>
<tr>
<td>How would you rate your hotel’s occupancy* in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>*(Occupancy rate refers to percentage of rooms sold to rooms available at a given period).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s revenue per available room (REVPAR) ** in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>**(REVPAR shows revenues generated from available room).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s market share*** in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>*** (Market share refers to the proportion of actual rooms sold in the marketplace).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s labour productivity**** in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>**** (Labour productivity refers to the percentage of revenues to payroll expenses).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>How would you rate your hotel’s profitability measured by Return on Capital Employed (ROCE) ***** in the last 3 years against similar hotels in the same area?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>***** (ROCE indicates revenues generated from all capital employed).</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q.2 Please estimate the average percentage of repeat customers who visited this hotel since 2001: %.

Q.3 Please estimate the percentage of your hotel’s revenue generated from the repeat customers who visited this hotel since 2003 %.

Q.4 Direction: This question looks at the hotel’s ability to manage different patterns and fluctuations in demand and its capacity. To do that, please click the answer which indicates the extent to which you agree with the statement. Rating (1) means you Strongly Disagree with the statement and (5) means you Strongly Agree. If you feel your agreement is between these two extremes, please pick any answer from within the scale;
<table>
<thead>
<tr>
<th>Managing Demand &amp; Capacity</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neither Agree nor Disagree</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>In this hotel, we charge full prices during peak periods i.e. no discounts.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we modify the service offering in the slow seasons to attract new market segments e.g. we rent rooms for film, advertisement or report producers.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we increase advertisements during slow periods.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we offer discounts during slow periods</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we communicate with guests to inform them about times of peak and slow demand.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we hire part-time employees during peak demand</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we rent equipment at time of peak demand e.g. we rent LCD projector for business travellers.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we work overtime at times of peak demand</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we train employees in the periods of slow demand.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>In this hotel, we reduce hours of operation during off-peak periods.</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>
Part IV. About You

Direction: This part is designed to get information about you. Please answer the questions below by ticking (X) in the appropriate option.

Q.1 Are you?
☐ Female ☐ Male

Q.2 Please indicate your age group.
☐ 20-34 ☐ 35-44
☐ 45-55 ☐ 56 and over

Q.3 What is your highest educational level?
☐ Secondary school
☐ College Diploma / Professional qualifications
☐ Undergraduate degree
☐ Postgraduate degree

Q.4 How many years have you been working in this hotel?
☐ Less than one year ☐ 1 to 2 years
☐ 3 to 5 years ☐ 6 to 10 years
☐ 11 to 15 years ☐ 16 and over

Q.5 Please print your job title:

Q.6 How many years have you been working at this level in the industry?
☐ Less than one year ☐ 1 to 2 years
☐ 3 to 5 years ☐ 6 to 10 years
☐ 11 to 15 years ☐ 16 to 20 years

Thank you for your contribution to this research