AN EXPLORATION OF THE ROLE OF THE CONSTRUCT OF CONTROL IN EXPANSION STRATEGY OF HOTEL CHAINS: A MULTIPLE-CASE STUDY

Ines GHORBAL-BLAL

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Michael D. Olsen, Chair
Devi R. Gnyawali
Suzanne K. Murrmann
Richard R. Perdue

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An Exploration of the Role of the construct of Control in Expansion Strategy of Hotel Chains: A Multiple-Case study

Ines GHORBAL-BLAL

(ABSTRACT)

Multinational hotel chains pursue extensive expansion strategy via unit growth as a competitive strategy despite the presently limited knowledge on the full implications of such a strategy on long-term performance. Since theory suggests that structure intervenes in the success of a strategy, this work proposes to investigate the relationship between expansion strategy and structure in the hospitality industry. Within this rationale, this work addresses one overarching question: How do structure and strategy relate?

The purpose of this study is to explore the management of expansion strategy in the hotel industry from the perspective of control. In other words, it proposes to examine the interaction between strategy and structure using the control approach as presented in the literature of organizational theory. Works on risk and risk management, research on control, and studies of expansion in the hotel industry constitute the three domains of the literature review. This integration illustrates that the management of risk in expansion strategy is intertwined with control.

For this study, two research steps were undertaken: a panel of experts and four case studies. Three out of the four studied companies are publicly traded and managed more than one brand in distinct segments. Case B, a privately owned company, is smaller and manages a single brand.
The question “How does control intervene in the management of risk in expansion strategy?” was the operationalization of the overarching question of strategy and structure. The answers to this question are summarized in a framework and four propositions. These propositions are: P1: The alignment with brand standards and the alignment of the Return On Invested Capital (ROIC) expectations are the operationalizations of the relationship between strategy and structure. P2: The degree of alignment with the brand standards affects the magnitude of loss through the bonding and monitoring costs. P3: The degree of alignment of the ROIC of the chain affects both the probability and the magnitude of loss. P4: The degree of alignment of the ROIC of the other party affects both the magnitude and the probability of loss.

The contribution of this work to academia is threefold. First, this work provides a detailed, theories-driven documentation about how expansion strategies are conducted in the international hotel context. Second, this research integrates three different fields of research (i.e.: strategy, finance, and OT) and directs to multiple new research tracks in both fields of strategic management and organization theory. Third, the notion of alignment is key to both OT and strategy research and has been the subject of extensive research. This study offers a new approach to measure the alignment between strategy and structure. From a managerial standpoint, this research offers guidance for the comprehension of the determinants of risk in the expansion strategy for international hotel chains.

DEDICATION

Dédiée à mon Pépé et à Amayma Hbiba, pour l'inspiration qu'ils apportent à ma vie

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Chapter 1: Introduction

Expansion strategy via unit-growth is *the* generic strategy that publicly traded multinational hotel chains have pursued for decades and continue to engage in today. They have pursued growth through franchises, management contracts, leases, and full or partial equity involvement. As a consequence, some multinational hotel chains presently count several thousands of units (almost 3,000 for Marriott International and Hilton Hotels and 4,000 for Accor S.A.). Despite the presently limited knowledge on the long-term implications of such a strategy on performance, growth remains the predominant strategy. It is imperative that we further explore the implication of this strategy on long-term performance within the hospitality industry.

More precisely, it is time to explore the role structure plays in expansion strategy within the hospitality industry. Refining our comprehension of the relationship between structure and expansion strategy would be a step towards understanding the impact of expansion strategy on long-term performance. Within this rationale, this work proposes an examination of the interaction between strategy and structure using the control approach as presented in the organizational theory literature. In particular, the purpose of this study is to explore the management of risk in expansion strategy within the hotel industry from the control perspective.

From a control perspective, the management of expansion strategy is the strategic management of a new unit's introduction into the company network. Particularly, it is the strategic management of the transaction between the hotel chain and the unit selected for growth. This transaction requires the management of risk to ensure that the control in place is consistent with the features of the new hotel unit. Therefore, the management of expansion strategy is related to the management of control costs, which, in turn, affects the management of risk.

By and large, this work addresses the following overarching question: How do structure and strategy relate? Drawing from research in strategic management, finance, and organization theory, this work raises the following questions in order to better understand the effect of expansion strategy on long-term performance:

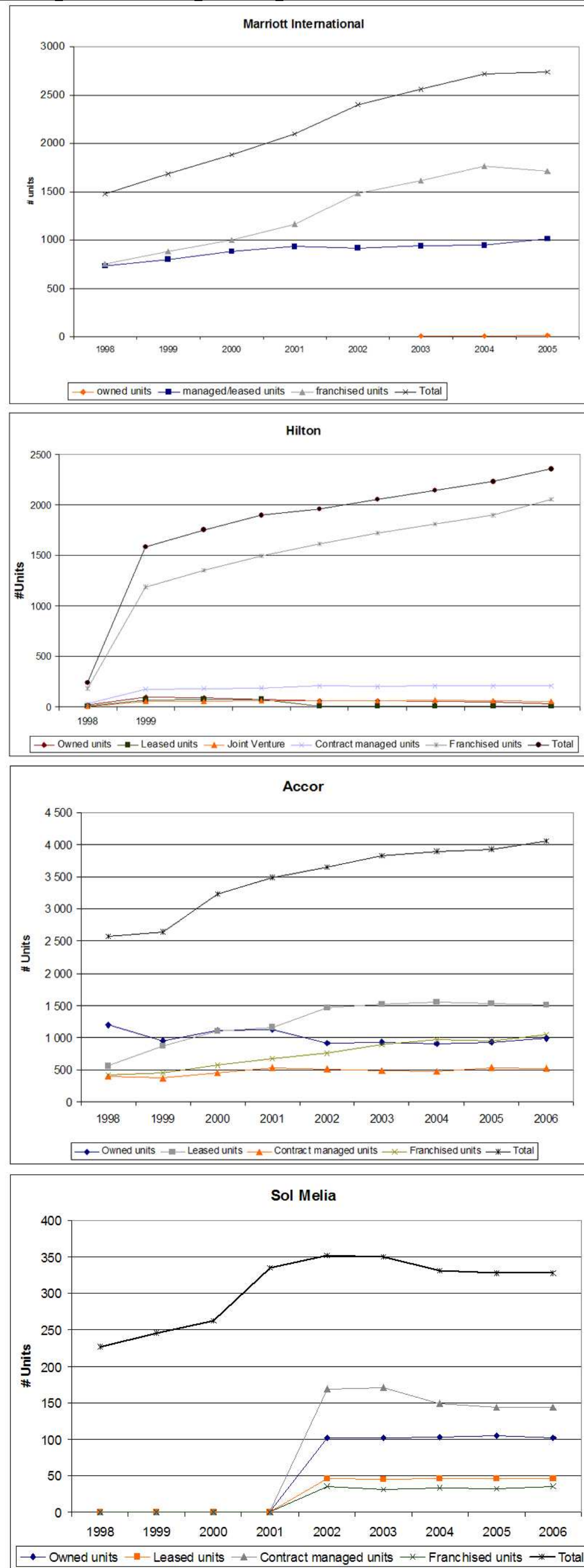
- Is control a structural variable in the management of expansion strategy?
- How does control intervene in the management of risk in expansion strategy?
- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion strategy context?
- What is the role of control costs in the management of risk for expansion strategy?

- How do the features of the hotel unit affect the management of risk in expansion strategy?

EXPANSION AS A GENERIC STRATEGY: THE HOTEL INDUSTRY CASE

Growth is a critical aspect of the hotel industry (Littlejohn & Roper, 1992; Olsen & Merna, 1992; Olsen et al. 1998, Zhao, 1994). In fact, unit growth is the most widely relied upon strategy in the hotel industry. Hotel firm report on unit growth every year from their inception. Marriott International, for instance, in its 2005 financial report declares the opening of "*134 properties totaling 21,611 rooms, across (their) brands in 2005*" (…) and having "*more than 70,000 rooms under construction, awaiting conversion or approved for development in (their) development pipeline, and (they) expect to add approximately 25,000 hotel rooms to (their) system in 2006*." (Marriott International Financial Statements, Year Ended 2005: 31-32). More concretely, during the last seven years (between 1998 and 2005), Marriott International's network has expanded by 85%, Hilton's has been multiplied by 8, Accor's has grown by 58 % and Sol Melia's augmented by 44% (Please refer to Appendix A and Figure 1 for further details). These four international hotel chains are only an example of the expansion that characterizes the hotel industry. Growth reports and projections are common to every hotel chain's financial statements and reflect the criticality of unit growth in the industry.

Figure 1 Total Hotel Units per Chain per expansion mode-1998 to 2005-



GROWTH OPTIONS IN THE EXECUTION OF EXPANSION STRATEGY

International hotel chains have relied on a range of growth options during their execution of expansion strategy. Commonly used growth options are: franchises, management contracts, leases, rentals, and full or partial equity participations. Marriott International, for instance, owns and leases less than 1% of its units, operates 37% under management contract, and franchises 62% of its network (Figure 1 and Appendix A). These growth options are common to every international hotel chain however one feature distinguishes itself among major international hotel chains: the maintenance of a mix in growth options at the network level.

The mix of growth options in the network of international hotel chains is a unique and observable disparity among hotel chains. Indeed, while all international hotel chains employ different growth options during the execution of expansion strategy, a particular mix in these growth options also characterizes them. As reflected in Figure 1, Marriott maintains a proportion of 6-3-1 with 60% franchises, 30% management contract and the residual for owned units. Hilton relies on a larger franchise base with an average of 80% of franchised units, 10% under management contract, between 2 and 3 % under a joint venture, and less than 3% of owned units. The two European firms operate on a larger owned or leased base. Accor, for instance, leases and owns between 50 and 60% of its units, and franchises a fourth of its network. SolMelia presents a similar mix with a greater emphasis on management contract and less on leases (Appendix A). Why do firms work on maintaining a specific mix of growth options? What are the implications of this mix on the structure of the chain? How does this structure affect performance? And most importantly, what is the link between structure and the management of expansion strategy? These are the inductive questions initiating this research effort.

GROWTH OPTIONS AND CONTROL

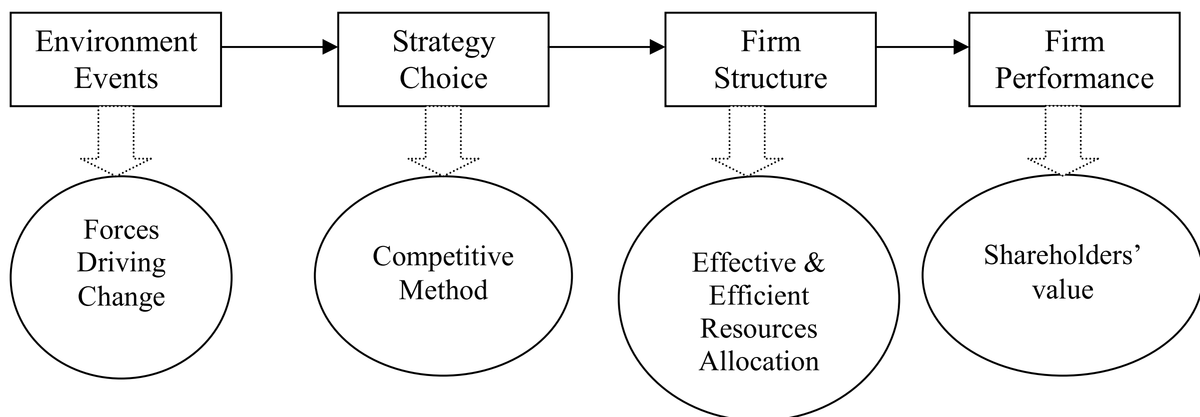
Research literature in management and organization theory related to the mix of growth option points to the criticality of control mechanisms in the execution of expansion strategy. Whether applied to the fast food industry (Bradach, 1992), cosmetics industry (Cliquet and Croizan, 2002), or retail business (Lafonataine, 1992; Yin and Zajac, 2004) the specific role of control can be observed. More precisely, key variables in organization theory and strategic management such as price, authority or trust can be viewed as specific examples of control

mechanisms (Bradach & Eccles, 1989). Overall, these research streams recognize that each growth option is associated with a set of imperatives and mechanisms for control. Therefore, the focus of this study is the exploration of control as a structural dimension that relates strategy to structure.

THE STRATEGY-STRUCTURE ALIGNMENT

Fundamental principles of strategic management assert that performance is likely to be produced in a sustainable manner, if the strategic choice is aligned with forces driving change in the environment. Equally, the same strategic choice should be aligned with the resources and capabilities of a company in order to create a sustained level of return (Venkatraman, 1990). This principle contending that aligning strategy and its context has significant positive implications for performance is referred to as contingency, consistency, alignment (Bourgeois 1996), fit (Yin and Zajac, 2004), or co-alignment (Bourgeois 1996; Olsen et al. 1998) in theoretical research.

Figure 2 Co-alignment principle



In essence, the co-alignment principle (Figure 2) suggests that if firms accomplish the alignment of environmental events, strategy choice, and firm structure, "*the financial results desired by owners and investors have a much better chance of being achieved*" (Olsen et al. 1998: 2). Figure 2 illustrates the four founding constructs of the, above named, co-alignment principle, as well as the sub-constructs utilized in strategic management. First, the "*environment events*" overarching construct embraces: the forces driving change, shaping the environment, modeling threats, and opportunities for a firm. Second, "*strategy choice*" corresponds to the intended strategy (Mintzberg, 1987) or choice of competitive methods. "*Competitive methods in*

the hospitality industry are made up of portfolios of products and services designed to bring the unique resources and capabilities of the firm together in order to achieve advantage in the marketplace" (Olsen et al. 1998: 2-3). Third, "*Firm Structure*" encompasses the effective and efficient allocation of resources within a firm. Key to the co-alignment model (and in accordance with the Resource-Based-View in strategic management) structure should interact with strategic choice in a fashion that builds a sustainable competitive advantage. In other words, the resource allocation structure in place needs to efficiently and effectively support the implementation of competitive methods. Finally, the sub-construct "*firm performance*" corresponds to shareholders value, which corresponds to the financial expectations of owners and investors.

Of interest in this work is the question of whether the alignment of expansion strategy with company structure (as the introduction of a growth option within the existing hotel network) allows for the facilitation of long- term performance (Figure 2). In this case, an existing hotel network of hotels constitutes the structure of a firm and the introduction of a growth option represents the expansion strategy.

The fit between the selection of unit growth and its execution is the substitute for the alignment between choice and structure in the context of hotel expansion. In other words, to reduce the number of asset des-investment (which reflects under performance rather than long-term performance, Rappaport, 2006), prevent the downgrading of financial ratings, and create a positive stream of cash flow, the modal choice selected should be aligned with the allocation of resources currently in place. More importantly, the structure needs to allow the achievement of the initial growth objectives (effective) as well as present dynamics that allow the achievement of these objectives (efficient). Simply stated, to achieve performance, the structure should allow for the execution of strategic choices. This work departs from a simple question: How does such an alignment occur? Little evidence is available with that regard; therefore, this work proposes to examine control and understand the interaction between structure and strategy.

CONTROL AS INDICATOR OF ALIGNMENT

The proposition of this study is as follows: each growth option can be perceived as a particular set of agreements, or transactions, between the firm and a selected hotel unit. Each of these new transactions is associated with a specific setting of control ensuring the execution of operations. Control is perceived to interact with the management of risk to affect long-term

performance. In the case of ownership, for instance, new hierarchies and internal control systems are enforced when it is selected as growth option. Similarly, contractual agreements between hotel owners and hotel chains control leasing or franchising relationships. Control could, reasonably, be used as an indicator of the alignment between strategy and structure. More importantly, control is put forward as a key construct in the relationship between strategy and structure. It is suggested that control guides the process of strategy implementation through its role in the management of risk. This research builds on existing research pointing to control in expansion strategy, and explores the role of control in the management of risk in expansion strategy.

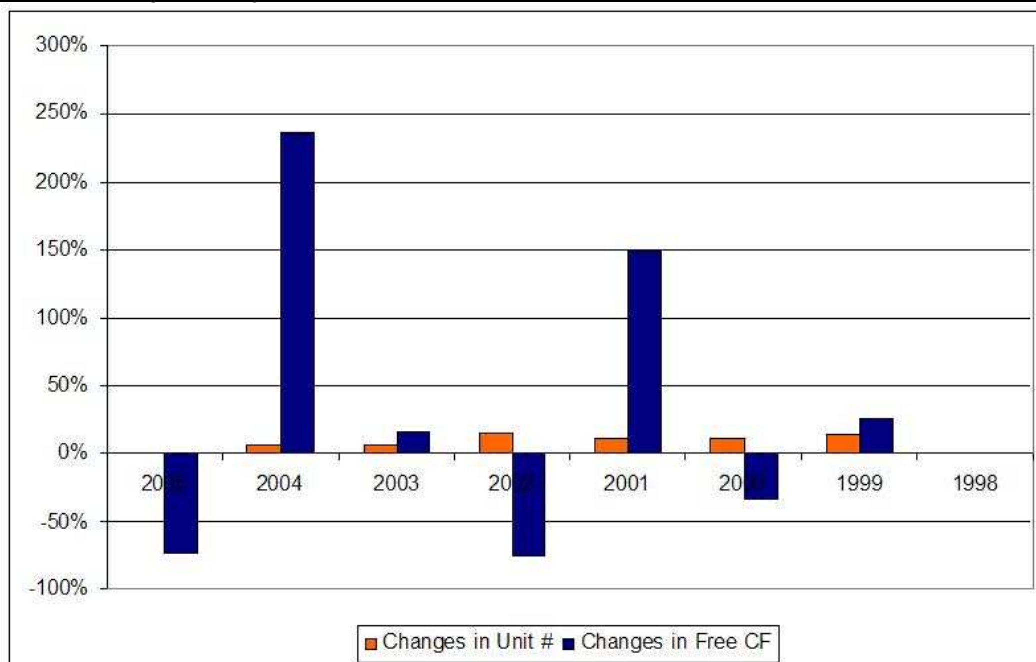
According to seminal research linking management, structure, and performance, the presence of different forms of control simultaneously creates particular dynamics. These dynamics support the performance of a company. The work of Bradach (1992) on plural forms, or the mix of growth options, constitutes the first effort to explain the role of the structure of mix of growth options on performance. Bradach (1992) found that plural forms were put in place by fast food restaurants to meet four managerial challenges: 1. uniformity, 2. local responsiveness, 3. system wide adaptation, and 4. unit growth. Simply, this study revealed that these organizations attempt to control operations and processes in order to maintain their performance. Bradach noted that fast food restaurants were found to rely on a set of growth options in order to gain control over a particular set of resources and capabilities at both the unit and network level. It is this control over the resources and capabilities that allowed these firms using the plural form to perform better. The contribution of this research effort is in examining the management of risk as related to expansion strategy through control.

Research in Organizational Theory (OT) has presented different and sometimes conflicting views, and hypotheses regarding to the role of structure and firm performance. The Transaction Cost Theory (TCT) and Agency Theory (AT) are the founding theories in OT relating structure and performance. TCT perspective opposed market and hierarchy in the examination of determinants of economic performance (Coase, 1937; Mahoney, 1992). As for AT, it approached the challenges related to structural dynamics through the examination of the link between the unit and headquarters (Eisenhardt, 1989). Research in OT has indicated a connection between the role of size, technology, processes, integration, and coordination in the relationship between strategy and structure. While all these suggestions might appear divergent and conflicting, there is one

common point relating them: the centrality of control in the management process. In essence, the imperatives of control inevitably come out in the examination of the relationship between strategy and structure. In sum, while research from different streams of management and economics point towards control as a structural element in expansion strategy management, little is known about the subject.

The question of the contribution (or lack of contribution) of unit growth on performance is daunting to hospitality decision makers and is likely to continue in the future. Studies of the industry life cycle reveal that the hotel industry has entered the maturity stage (Olsen et al. 1998, Taylor, 2002). This new phase in the industry will involve increased competition among actors in the hospitality industry. Market shares, enhanced financial performance, value creation and process within organizations will be core elements in the future of hospitality management. Regarding expansion decisions, pressures on the selection of an appropriate long-term performing unit will be increasing. Global private capital rationing, governmental capital rationing, regional influences, growing influence of capital markets, and new pressures for publicly traded firms will build further strains on expansion decisions for the hotel industry. Additionally, the management of risk in hotel expansion strategy is likely to become crucial. In sum, international hotel chains will have to better comprehend and control the effects of expansion on long-term performance to succeed.

Figure 3 Percentage change in number of units and Free Cash flow. Marriott 1999-2006



As long as des-investment and flag changing are common practices in the sector (Appendix A), the question of the effects of growth on long-term performance remains open. Marriott, for instance, after gradually acquiring 99% of the ownership of Ritz-Carlton in 1998, sold this same participation to Cendant Ramada International Hotels & Resorts in September 15, 2004. Similarly, Hilton Hotels gradually withdrew its investments in hotels, and thus dividing by three its total number of owned units (from 96 at the beginning of 1999 to 30 on January 2006). Why would large firms such as Marriott or Hilton invest in new units to withdraw these same investments a couple of years later? Are such processes enhancing long-term performance?

Despite being a critical and common investment decision in the hotel industry, unit growth does not seem to translate into uniform performance for hotel chains. Free cash flow for each of the firm, presented as example in this introduction, is not as steady through the years as unit expansion. Marriott International, for instance, has increased its hotel network by 84% between 1998 and 2005 while, over the same period its free cash flow has decreased by 48%. Specifically, in 2004, while maintaining unit growth at 6 % Marriott multiplied its free cash flow by almost 2.5. Three years earlier the same company despite increasing its number of units by 15% has recorded a loss in free cash flow of 76% from 2001 (Figure 3) Obviously exogenous events such as industry demand should not be ignored in these free cash flow fluctuations. Nevertheless, it is clear that the relationship between unit growth and cash flow performance is neither linear nor direct. There can be no doubt about the relationship between unit growth and performance since hotel units are operating sources for the cash flows within hospitality organizations. Research literature points to organizational structure as a key to strategy, thus the question: How do structure and expansion strategy relate?

PROBLEM STATEMENT

Growth is a generic strategy utilized by publicly traded international hotel chains and its long-term performance implications are as of yet unknown.

The achievement of long-term performance is critical to business success in a competitive environment. Literature in strategic management and organizational theory suggests that the alignment of a strategic choice with a supporting firm structure is key to the success of a company. Simply stated, long-term performance is achieved not only through the alignment of a strategic investment with the requirements of the environment but also with a fit between strategy

and the existing structure. Simply, according to theory, an investment will generate long-term performance if it is supported by an efficient and effective resource allocation process within its organizational structure.

The significance of this structural alignment is even more important for large hotel chains in which networks might reach upwards 4,000 units. In these large networks, each investment has to be managed carefully to ensure the success of the organization. Unfortunately, little, if nothing, is known about the structural elements that ensure a sustainable performance in the expansion of hotel chains. Therefore, how do structure and strategy relate? Practically, how can the managers of a hotel chain achieve the alignment of their strategic investment with the structure of their firms? And more importantly, how can managers ensure the adequate compensation of the risk related to their strategic investment? These questions present the orientation of this research.

PURPOSE OF STUDY

Hotel chains have extensively relied on expansion strategy to respond to the growth imperative of their industry (Olsen et al. 1998). As a consequence, their unit network is comprised of a mix of fully or partially owned, leased, operated under management contracts or franchised hotels. The focus of the study is on the strategic role of control in the management of risk involved with expansion strategy. This work suggests using control as a structural variable in the examination of the efficient and effective allocation of resources supporting the execution of expansion strategy. Theoretically, this study proposes to provide an understanding of the interaction between structure and expansion strategy using the control perspective as presented in the organizational theory literature.

STUDY QUESTIONS

How do structure and strategy relate? This is the driving question in this research effort. This subject is examined from a control perspective and in the context of expansion strategy used by international hotel chains. Particularly, the management of risk, a key determinant in expansion strategy success, is studied in relation to organizational features and control costs. In essence, this work puts forward control as a structural dimension linking the management of risk and organizational features and seeks to address the following research questions:

- Is control a structural variable in the management of expansion strategy?
- How does control intervene in the management of risk in expansion strategy?
- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion context?
- What is the role of control costs in the management of risk for expansion strategy?
- How do the features of the hotel unit affect the management of risk in expansion strategy?

Ten study questions, listed below, were developed to direct the examination of the above overarching research issues. These study questions are constructed around the three main areas where control intervenes in the strategic management of expansion namely expansion selection and control stake, cost and control advantages, and the management of risk.

Expansion selection and control stakes

1. Do hotel chains assess possible control advantage(s) and disadvantage(s) when selecting a particular growth option? If yes, what are they?
2. Are these advantages and disadvantages different from one growth option to another? If so, how do they differ?
3. Why and how does the introduction of the new unit modify the control in place in the chain?
4. How is the modification of control, through the introduction of a new unit, assessed?

Costs and control advantages

5. Are there costs associated with the identified control advantages and disadvantages?
6. Are these costs estimated when selecting a growth option?
7. Is there a relationship between these cost estimates and the amount of resources committed in the selected growth option?
8. Are resources committed when modifying the control in place to the new unit?
9. Why are these resources committed?

The management of risk

10. How does the assessment of control advantages and disadvantages intervene in expansion strategy risk assessment?

RESEARCH DESIGN

Case studies were employed for this exploratory work. Due to the nature of the study questions, along with the lack of industry contextual variable, the case study as data collection method appeared as most appropriate. A case study was conducted in four hotel chains to explore the relationship between strategy and structure in the expansion of hotel chains. Particularly, interviews and administrative documents were gathered to explore the interaction between strategy and structure in the hotel expansion setting.

The data collection process was composed of three stages. In the first step, a list of interview questions was developed and submitted to a panel of experts for validation. Once the final list of interview question was approved, a pilot case study was undertaken. Finally, three case studies were conducted.

STUDY CONTRIBUTION

The central theoretical contribution of this study lies with the introduction of control in the examination of the relationship between strategy and structure. Control is related to the management of risk and thus, offers a dynamic and more realistic, view to the possible alignment between strategy and structure. As such, it is believed that control could allow a more flexible approach to the research linking strategy and structure in strategic management. More importantly, this study presents the opportunity to refine our understanding of the intricate between strategy, structure, and performance of an organization.

In addition, the integration of three different fields of research within one study effort also constitutes a contribution.

Furthermore, this work provides a scientific investigation of a commonly relied upon strategy in the hotel industry. Little can be found in either the academic or managerial literature on how developers manage their expansion. This work provides a detailed, theories-driven

documentation about how expansion strategies are conducted in the international hotel context. Simply put, this research enhances our contextual knowledge of expansion strategy.

From a managerial standpoint, this study examines the details of expansion management through essential issues such as control costs and the management of risk. Such an exploration carries the potential of examining a widely relied upon strategy in the hospitality industry which implications on performance are still challenging for practitioners. In essence, this work offers measures for the alignment between expansion strategy and structure in the context of international hotel chains. These measures enhance the knowledge on risk and its management in the field of strategy.

SUMMARY

Publicly traded multinational hotel chains pursue extensive expansion via unit-growth as a competitive strategy despite the presently limited knowledge on the full implications of such strategy on long-term performance. Since theory suggests that structure intervenes in the success of strategy, this work proposes to explore the relationship between expansion strategy and structure in the hospitality industry.

The purpose of this study is to explore the strategic management of expansion in the hotel industry from the perspective of control. From this perspective, the strategic management of expansion is the strategic management of the transaction between the hotel chain and the hotel unit selected for unit growth. Consequently, a control perspective proposes that the strategic management of expansion is related to the management of control costs, which in turn affect the management of risk in expansions. These relationships will be examined in this research effort.

Variables related to control are derived from the literature review for the examination of the relationship between strategy and structure in the expansion setting of hotel chains. These variables were used as a guideline for the data collection process framing a theory-driven study. Case study research methodology was employed to collect evidence.

The interaction between strategy and structure has been a daunting question in both the strategy and organizational theory field. Similarly, the question of expansion strategy management is a key question in the hospitality industry. This study puts forward an innovative way to examine the issue of structure in relation to strategy for the benefit of hospitality research and management practices.

CHAPTER 2: LITERATURE REVIEW

INTRODUCTION

The achievement of long-term performance is critical to business success in a competitive environment. The capacity to achieve sustainable performance has been indicated as the most distinctive feature in strategy literature (Rappaport, 2006; Porter, 1996, Hamel and Prahalad, 1990). Within this same field, long-term performance is often defined as the firm's capacity to provide its stockholders with a sustained level of return. In practice, however, this sustainability in a firm's financial performance has been narrowly approximated by a more simplistic measure: growth. Growth has been so predominant as to become an environmental imperative, a key success measure for managers, and a pre-requisite for investors.

Expansion and long-term performance

Surprisingly, this widespread practice is relied upon while little, if nothing, is known about the positive impact of unit expansion on the long-term performance of firms. Latest examinations on the real impact of growth regarding firm performance and its value creation capacity does little to enhance our confidence with respect to the positive long-term impacts of growth (Chathoth and Olsen, 2007; Zook et al. 2000; Zook and Rogers, 2001). Zook et al. (2000) examined the performance of 1,854 companies between 1988-1998 and noted: "*that revenue growth alone has little or no impact on shareholder value. In fact, companies that grew revenues were more likely to destroy value than create it!*" (2000: 3). In a more recent research effort in the U.S. restaurant industry, Chathoth and Olsen (2007) empirically studied the ability of growth to "*really help a firm add value, and thereby benefit its stockholders in the long run*" (2007: 68). The result of the linear regression model relating sales growth with return on equity and growth potential with free cash flow per share is clear: "*growth strategies do not help explain a significant amount of variance in firm performance.*" (2007: 78).

Growth and risk

Ignoring the nature of the growth-performance relationship can have negative effects on firms. As mentioned earlier, the pursuit of growth strategies can lead to short- term returns or even weak performance. Particularly, the latest examination of the financial characteristics of

restaurants and risk (Borde, 1998) uncover the fact that growth "*could increase risk"* (1998: 69). In other words, pursuing growth could destroy an organization's capacity to achieve long-term performance as it potentially creates a risky financial structure. Borde (1998) empirically examined the contribution of selected financial measures in the variance of risk for restaurants and concludes that "*aggressive and rapid growth could increase risk by straining a firm's human resources and its ability to develop efficient controls and an effective internal structure*" (1998:69). He further advises executives to "*carefully manage (*growth*) while developing an internal structure that is capable of coping with that growth while maintaining control of the firm's operations*". This last assertion implies that the relationship between growth and performance is more complicated that it first appears. Simply stated, Brode implicitly assumes that the management of expansion strategy, and not just expansion strategy itself, determines performance, which suggests that the relationship between growth and performance is not direct. How can growth be strategically managed to have a positive effect on performance? How can growth be managed to constrain risk and generate a sustained performance? In order to be able to answer to these fundamental strategic questions, we should first better understand how growth and performance relate to the management of risk.

Summary

The achievement of long-term performance is critical to business success in a competitive environment. In strategy theory, long-term performance refers to the firm's capacity to provide its stockholders with a sustained level of return. In practice, growth is used as a narrow approximation. As a consequence, growth is pursued in the hotel industry (as in any other sector) as an option to generate performance while little, if nothing, is known about the positive or negative impact of growth on long-term performance. On the contrary, recent research in strategic management reveals that growth not only has little to do with long-term performance, but that it can also increases risk. These last advancements can reasonably lead us to assume that the path from growth to performance is much more complicated than a simple linear progression. More importantly, strategy literature identifies the concept of risk as a critical element in this relationship. The key strategic question, which is left unanswered in previous research, is how can risk be better managed in relation to growth?

Under the overarching research question, which focuses on the relationship between structure and strategy, four main fields are examined in this literature review: finance, strategy, organization theory, and behavioral management research. First, risk and its management are studied in the financial, strategic, and decisional literature. Second, the literature related to the concept of control is reviewed. In particular, the propositions of the Agency Theory and the Transaction Cost Theory on the determinants of control are examined. The last section of this chapter introduces the four propositions emerging from the review synthesis and proposes a model integrating the management of risk and control in a hospitality expansion setting.

RISK

Financial perspective of risk

In finance, risk is approached as a bi-dimensional construct that is composed of a systematic risk portion and an unsystematic risk part. The addition of the two previously mentioned risk components constitutes total risk (Brealey and Myers, 2000; Winfrey and Budd, 1997). The perspective of total risk as a combination of systematic and unsystematic risk is derived from a fundamental theory in finance the Capital Asset Pricing Model (CAPM). The CAPM relates risk with return. In essence, systematic risk and unsystematic risk are "*standard measures of risk for stock market return data*" (Miller and Bromiley, 1990). In this section, the financial definition of risk and its associated measurement is described. Then, the derived financial perspective on the management of risk is briefly presented.

- *Risk, Return, and Probabilities*

Financial theorists differentiate among different types of risk. They distinguish among the market risk, the project risk, the portfolio risk, the default risk, the financial risk, and the business risk, to mention only a few (Brealey and Myers, 2000). Nevertheless, risk is always summarized through the variance or standard deviation of the "*spread of all possible outcomes*" (Brealey and Myers, 2000: 163). In finance, risk is associated with uncertainty. Uncertainty, in turn, is the extent to which an outcome happening is improbable. Thus, the financial representation of risk is that of "*all possible outcomes and the probability of each*" (Brealey and Myers, 2000: 163). It is important to note that one key element differentiates finance from other management theories (stock) return is the outcome under consideration. Simply stated, financial theorists define risk in

relation to return. Based on the statistical assumption of normality of event distribution, financial theorists represent risk as the variance of all possible outcomes of an event. The mathematical formula for market risk is thus expressed as follows:

$$\sigma^2 (r_m) = 1/(N-1) \sum_{t=1} (\tilde{r}_{mt} - r_m)^2$$ where,

σ^2 : Variance

r_m : is the actual market return,

$\tilde{r}_{mt}$: market return in period t,

r_m : mean of values of $\tilde{r}_m$

Derived from the representation of risk described earlier, the theory of finance has developed varieties of concepts related to risk. The most common one is the approach to risk as composed of a systematic (also called market or undiversifiable risk) portion and an unsystematic part (often referred to as unique, specific, residual or diversifiable risk).

✓ *Unsystematic risk:* It is the risk that "*stems from the fact that many of the perils that surround an individual company are peculiar to that company*" (Brealey and Myers, 2000:167). It corresponds to the uncertainty stemming from the firm's management decisions. The variance in an individual firm's net cash flow is a standard measure for unsystematic risk (Winfrey and Budd, 1997). Other accounting and financial measures of income streams, such as ROE (Return on Equity) and ROA (Return on Assets), are used in standard deviation computations (Miller and Bromiley, 1990).

✓ *Systematic risk*: Systematic risk "*stems from the fact that there are other economywide perils which threaten all businesses*" (ibid: 169). Simply stated, general economic or market conditions are associated with systematic risk (Winfrey and Budd, 1997) and are assumed to affect all companies. Changes in the interest rates or in the price of raw material are examples of a source of systematic risk. The latter is often measured with the beta (β), a measure of covariance between the returns of a firm and the return of a selected portfolio. Mathematically, the β formula is as follows:

$$\beta = \sigma_{im} / \sigma^2_m$$ where,

σ_{im}: covariance between stock i's return and the market return

σ^2_m: variance of market return

- *The management of risk: Financial perspective*

As far as the management of risk is concerned, financial theorists assume that market risk, or rather systematic risk cannot be reduced but can only be hedged. In other words, investors can only protect themselves from the fluctuations associated with market risk by compensation through financial management tools (Froot et al, 1993). As for the unsystematic risk, its management is rarely examined (Winfrey and Budd, 1997). The reason for the focus of finance on the systematic risk component is that finance assumes that the unsystematic portion can be eliminated. Finance researchers defines unsystematic risk as the "*risk that can be eliminated by diversification*" (Brealey and Myers, 2000:1073) as opposed to systematic risk that is viewed as "*risk that cannot be diversified away*" (ibid: 1068). Simply stated, the financial perspective assumes that an investor can eliminate the unsystematic risk through diversification and thus, the latter is considered to be less of an issue.

Risk is perceived in finance from the investor perspective and is defined in relation to return as suggested in the CAPM. Brealy and Myers' conclusion on risk leaves no place for ambiguity about this relationship as they state "*risk in an investment means that future returns are unpredictable*" (Brealey and Myers, 2000:179). Risk and return are intertwined in finance since high risk is assumed to be related to high returns and vice-versa (Bettis and Mahajan, 1985; Winfrey and Budd, 1997). Consequently, financial investment decisions are made based on the relationship between risk and return that shapes the financial approach to the management of risk.

- *Summary*

In finance, risk is approached from the position of the investor and is defined as the "*spread of all possible outcomes*" (Brealy and Myers, 2000). Moreover, (total) risk is assumed to be comprised of a systematic and an unsystematic risk portion. On one hand, the systematic risk refers to the overall business threats affecting all businesses. On the other hand, the unsystematic risk labels the risk related to the firm. As for the financial perspective of the management of risk, it is based on three fundamentals. First, based on the nature of the systematic and unsystematic risk, only the systematic risk matters since the unsystematic is eliminated through portfolio diversification. Second, the systematic risk cannot be reduced, but instead can only be protected against by financial processes such as hedging. Third, risk is considered as being positively

correlated with return therefore, financial investment decisions are driven by the relationship between risk and return.

Strategic perspective of risk

The strategic perspective of risk differs from the financial approach on two points (Winfrey and Budd, 1997). First, the positive correlation between risk and return is not perceived to exist in the strategic view of risk (Ruefli, 1990). Second, strategists and financial theorists differ on their stances on the type of risk to manage and where to place their focus (Winfrey and Budd, 1997).

- *Risk-return paradox?*

As mentioned above, the relationship between risk and return is at the heart of financial theory. The idea is simple in that higher risk yields higher return, while lower risk should be compensated by lower returns. Findings in strategic management appear to indicate the possibility of a negative relationship when such a relationship is found to exist.

Several research efforts in strategy observed a negative relationship between risk and return (Bowman, 1980; Fiegenbaum and Thomas, 1986; Lubatkin and Chatterjee, 1991; Wiseman and Bromiley, 1991) and are thoroughly reviewed by Winfrey and Budd (1997). In light of how these findings contradict the fundaments of finance, Ruefli (1990) examines the measures used for the concept of risk. He argues that the use of mean-variance to measure the relationship between risk and return explains the divergence of finance and strategy findings on risk and return. Simply, he argues that the use of mean-variance to measure the relationship between risk and return in the strategic context leads to an unverifiable relationship. Further examination of the measures of risk in strategic management points to the lack of validity in the construct and the need to refine the research with this regard (Timothy et al. 1999). Both studies reviewing the measures of risk in strategic management draw a common conclusion. This conclusion is that in order to be able to verify the relationship between risk and return, the concept of risk needs to be measured with tools based on the premises of strategy. Simply put, risk definition calls for a refinement in the field of strategic management (Miller and Reuer, 1996; Ruefli, 1990; Timothy et al. 1999). This refinement should be in accordance with strategic management fundamentals, rather than financial principles.

Also, other studies in the field of strategy suggest that there might be no relationship between risk and return (Jemison, 1987). In an innovative approach to performance, Jeminson studied risk

and return as performance dimensions in the strategic management context. His conclusions on the banking industry are that "*different strategies were found to be associated with differences in risk but not in return*" (ibid: 1087). This study introduces a key idea in relation to risk and return in strategic management, which is that risk could be managed independently from return (Bromiley, 1991). From a theoretical perspective, this study suggests "*risk and return may be tapping two different dimensions of performance*" (Jemison, 1987:1087).

Whether negative or non-related, the relationship between risk and return as components of firm performance is central to strategic management. The above discussions might reflect confusion with regard to risk and return in the strategy literature. Nevertheless, these findings are converging towards an essential idea that risk, in a strategic context, relates to return in a more complex manner than the one suggested in finance. This observation raises a rather naïve, but fundamental, question: why would we continue to use a financial definition to risk in our examination of strategic questions? Finance is based on a set of assumptions that differ from strategy. It is thus, logical that financial approaches to risk reveal shortcomings when applied to a strategy context. Then, if strategy and finance diverge on their assumptions and approaches to returns we should apply a definition of risk that applies to strategy questions.

This study seeks to maintain theoretical fundamentals of strategy while examining the concept of risk. It is hoped that such an effort would contribute to the development of a theoretically sound definition of risk in strategy.

As mentioned earlier, strategy diverges from finance by assuming that the management of unsystematic risk affects returns (firms performance). Strategy assumes that the role of managers is proactive with regard to the environment and its uncertainties. Thus, it focuses on the actions of managers to explain the determinants of returns. In essence, based on the fundaments of strategy, the relationship between risk and return is actually the interaction between *the management of risk* and return. In an effort to maintain coherency with the fundamentals of strategy, this research effort is based on the assertion that the construct of "risk" in strategic management needs to be re-defined to "the management of risk " when examining the relationship between risk and return. The strategic and financial divergence about risk and its return relationship is rooted in the fundamental theoretical difference between strategy and financial management. While finance focuses on the investor perspective, strategy perceives the relationship between risk and return from the management's perspective. These divergent

perspectives of the concept of risk impart different assumptions on the relationship between risk and return. Strategy has a voluntaristic view of organizations (Astley and Van de Ven, 1983), while finance a more deterministic approach to companies. Therefore, strategy takes into account managerial intervention in the relationship between risk and return through the management of the specific risk of the firm. This managerial intervention is referred to as the management of risk and reflects the distinctive feature that separates strategy from finance: the voluntaristic approach to firm performance.

- *The management of risk: Strategic Perspective*

In total contradiction with the assertions made by finance theorists, empirical studies in the field of strategic management suggest that systematic risk can be reduced. In an examination of the relationship between corporate diversification and shareholder value, Lubatking and Chatterjee (1991) found that "*firms which diversify by emphasizing common core technologies show on average lower levels of systematic risk, regardless of market conditions*" (ibid, 1991: 266). This finding suggests that strategically derived competitive advantages can actually constrain systematic risk (Barton, 1988). The fact that strategic decisions can also have an impact on the systematic risk constitutes an important contribution to our knowledge of risk, as Lubatking and Chatterjee (1991: 268) conclude:

> "*The systematic risk findings are important because they suggest that corporations can achieve a reduction in risk which stockholders cannot achieve on their own. (...) Management actions may alter the underlying risk profiles (...). In instances of corporate diversification, therefore, general market risk appears to have an uncontrollable and a controllable component*".

Simply stated, the strategic view of risk considers that market risk can be reduced through the implementation of competitive advantage dictated by strategies. In agreement with the Rumelt (1991) research and the Schumpeterian view (Jacobson, 1992), which as justification to the strategic view, this above quote on risk in strategic management suggests that managerial actions (competitive-advantage) do have an impact on the environment. Lubatking and Chatterjee's (1991) conclusion, however, introduces the new element of the decisions of managers through competitive advantage investments, which allows a control option that constrains market risk. In complete agreement with the strategy assumption that firm returns are actually determined by

managerial decisions and actions, Lubatking and Chatterjee (1991) suggest that components of systematic risk can also be reduced, or even controlled.

Consequently, drawing from a voluntaristic view of management, strategists suggest that both the unsystematic and systematic risk can be constrained. This assertion is based on the view that risk is reduced when uncertainty impacts are managed or controlled for. The actions of an organization can be influenced or controlled for (Chatterjee et al. 1999; Winfrey and Budd, 1997) through strategic management. Similarly, market conditions can be influenced or controlled (Lubatking and Chatterjee, 1991) through strategic investments. From a theory construction perspective, this indicates that risk and its management in strategy are associated with control. Therefore, a strategy-sound definition of risk should include the construct of control.

- *Summary*

Findings on the relationship between risk and return in strategy increasingly contradict the financial fundamentals relating risk to return. These findings raise construct validity issues for a strategic construct of risk as financially derived measures are applied in strategy research. The question of the validity of finance measures in strategy research is even more critical as finance and strategy are based on divergent assumptions. Strategy relies on a voluntaristic view of organizations while finance views businesses from a more deterministic perspective. Simply, strategists suggest that the returns of a firm are determined by managerial decisions and actions. As a result, the interaction between risk and return becomes more complex in a strategic context as the management of risk, and not risk itself, is assumed to affect return. Assuming the voluntaristic perspective in which the returns of a firm are actually driven by managerial decisions equates to acknowledging the capacity of management to control for risk. From a theory construction perspective, the above indicates that risk and its management in strategy need to be examined along with control.

This study seeks to maintain the theoretical fundaments of strategy in the approach to the risk concept. It is hoped that such an effort would contribute to the development of a theoretically sound definition of risk in strategy. It is proposed that risk should be approached as the management of risk in a strategic context. In order to build a more theoretical base for this research, the behavioral decision perspective of risk is examined in the next section.

Behavioral decision perspective of risk

The integration of a behavioral perspective on the management of risk is key at this stage. This field provides us with the managerial approach to risk, an element that is missing from the financial theory and lacked integration in the strategic one (Miller and Reuer, 1996). In the following section, the main behavioral directions in relation to the management of risk are presented, integrated to strategy and contrasted against the financial approach.

- *The management of risk*

The discrepancy between the conceptualization of risk in the financial theoretical literature and in behavioral practices pointed out by March and Shapira in 1987 is increasingly discussed in the field of management (Forliani, 2002 Palmer and Wiseman, 1999) and strategic management (Miller and Bromiley, 1990). This divergence stirred investigations on the interaction between risk and return (Jemison, 1987), risk behaviors (Forlani, 2002), the refinement of risk measurements (Miller and Bromiley, 1990) and on the overall definition of risk in management. Observing this discrepancy seems to open new horizons for knowledge building around the management of risk in the strategic context.

Behavioral decision theory brings in a key element with regard to the management of risk. Both the financial and the strategic perspective neglected this management element. This element is based on the managerial practical perspective to risk. While financial theory identifies risk as the variance of the probability distribution of possible outcomes, behavioral research suggests that, in practice, managers associate risk with only the negative outcomes (March and Shapira, 1987: 1407):

> "*From the former perspective, a risky choice is one with a wide range of possible outcomes. From the latter perspective, a risky choice is one that contains a threat of a very poor outcome*".

Finance theorists have been discussing the use of semi-variance measures of risk to better tap this construct. Behavioral decision theory, define risk as the "*probability of loss and magnitude of loss*" (Forliani, 2002: 125). Thus, while finance theory suggests that risk is the distribution of the probability of all losses and all gains, and is often mentioned as possible outcomes (March and Simon, 1958; Jiron, 2002), managerial behavior advocates the probability and the magnitude of only one possible outcome the loss.

- *Downside risk*

Downside risk is used to refer to the managerial perception of risk (Miller and Leiblein, 1996; Miller and Reuer, 1996). In their thorough integration of behavioral decision, finance, and management theories, Miller and Reuer (1996) provide support for the relevance of the concept of downside risk. Although no clear definition is presented, the authors suggest that downside risk is the "*understanding of risk as performance below expectations*" (1996:674). This nuance is essential to the understanding of the management of risk as it introduces the idea that managers perceive risk in relation to target performance or a certain set of expectations set by the organization. Expanding uppon the managerial perception of risk, recent research (Forliani, 2002; MacNamara and Bromiley, 1999, Miller and Reuer, 1996) agrees on the following two dimensions of risk:

- ✓ Probability of loss
- ✓ The magnitude of the loss

Additionally, March and Shapira (1987) observed that managers had a different perception of risk as they "*believe, (...) that they can manage the odds, that what appears to a probabilistic process can usually be controlled*" (ibid: 1414). In other words, it seems that managers focus on the above two dimensions of risk, because they believe, as society suggests, that they can "*control fate*" (ibid: 1413). As a consequence, the attention managers pay to downside risk, is not due to their incapacity to perceive the probability distribution of outcomes, but rather, is due to their intent to control the outcome. March and Shapira argue that this is the primary reason for managers to insist on the distinction between risk and gambling. Simply, managers "*believe that risks can be reduced by using skills to control the dangers. (...) Partly by securing new information, partly by attacking the problem with different perspectives*" (ibid: 1410). Finally, March and Shapira observed that managers looked for "*risk controlling strategies*" (ibid: 1411) before making a decision.

The above inference on the management of risk from the behavioral decision theory shares the voluntaristic assumption with the strategic management approach. Moreover, these findings also point to control as a key construct in the practices of the management of risk. As pointed out by March and Shapira, managers tackled the management of risk through risk controlling strategies, since they relate risk to control. Once again, risk is managed in relation to control. But what is the role of control in the strategic management of risk? How do control relate to the

management of risk? What are the components of the risk controlling strategies? Answering these questions could, ultimately, enhance our knowledge on the relationship between risk and return in strategy.

Behavioral literature also contains valuable debates on the determinants of decisions related to risk that could guide us through the above questions. For this purpose, the determinants of risk decisions in the behavioral literature are examined in the following section.

- *Determinants of risk-related decisions*

Literature in organization behavior suggests that risk approaches, attitudes, and behaviors are determined by the personality or moods of managers (Atkinson, 1964; Hastorf and Isen, 1982), and other personal characteristics such as age or experience (March and Shapira, 1987). However, this approach has been critized for not taking into account a determinant element, namely the decision-taking context (MacCrimmon and Wehrung, 1986; Shapira, 1986; March and Shapira, 1987). From a strategic perspective, management should be examined in its context. It is for this reason that the forthcoming review will only focus on research related to attitudes to risk within a context. Within this focus, the predominant approach to integrate the context in risk-taking decisions has been the Prospect Theory.

Prospect Theory:

Traditionally, prospect theory (Kaheneman and Tversky, 1979) has been used in organizational theory to explain the risk behavior of managers in relation to context. The prospect theory predicts that managers in the domain of loss will demonstrate risk-seeking behaviors, while those in the domain of gain will have risk-averse behaviors. The theory has been investigated (Bowman, 1980), tested, (Fiegenbaum and Thomas, 1988) and prevailed in the risk-taking literature. However converging conflicting research is raising questions (Miller and Bromiley, 1990; Forliani, 2002) and calling for a refinement of the prospect theory as a predictor of risk behaviors. Among the suggested refinements is the introduction of control in the examination of the management of risk. The latest suggestions to understand risk-seeking behaviors propose "*perceived outcome control, or the degree of influence an individual perceives having over an action's future outcomes*" as a moderator effect between decision domain and risk taking (Forliani, 2002: 126). In other words, behavioral theorists suggest that control relates to

risk through the notion of perceived outcome control. Forliani (2002) found empirical support for the role of perceived outcome control on risk-taking decisions. In his model, he suggests that:

> "*When all the alternatives in a decision maker's consideration set have a low probability of loss, magnitude of loss becomes the dominant element of risk. In this case where positive outcomes are virtually assured, there is little need for control. (...) However, when the alternatives in a consideration set have high probability of loss, making it the dominant element of risk, perceived outcome control has leverage to function*." (2002:126).

Simply, Forliani (2002) suggests that decision-makers will examine a certain set of considerations in the management of risk. Upon this examination, decision makers will focus on either the probability of loss or magnitude of loss as a dominant element of risk. This research brings the first insight into a possible relationship between control and the management of risk. Nevertheless, a key strategic question left unanswered is what are the components of the decision-maker's consideration set? Or, what are the elements that once assessed, determine whether the probability or magnitude of loss is the dominant element of risk?

While Forliani's research contributes in enhancing our knowledge on the management of risk, it falls short in explaining the determinants of managerial perceived outcome control. The author indicates that these findings are coherent with managerial rationality, but does not raise the question of the absence of knowledge on how managers build their perception of control. In essence, the role of the concept of control in the management of risk is revealed but left misunderstood.

- *Summary*

The behavioral decision perspective of risk introduces key elements in the comprehension of the management of risk. First, it establishes that management approaches risk not as the spread of all possible outcomes, but rather as composed of a probability and magnitude of loss. Managers appear to distinguish risk as a "*probabilistic process* (that) *can usually be controlled*" (March and Shapira, 1987: 1414). This view is in agreement with the voluntaristic strategic perspective and contrasts with the financial approach. Second, probability and magnitude of loss are dimensions of risk and determine contingency relationship in the management of risk. In other words, it appears that probability and magnitude of loss relate to control in the management of risk by

decision-makers. Third, this research stream points to control as a determinant concept in the management of risk. Behavioral literature allows the first integration of control and the management of risk. Nevertheless, a key strategic question is left unaswered: What elements determine whether the probability or magnitude of loss is the dominant element of risk?

The management of risk and Strategy management

Explaining differences among performances of organizations is the purpose of strategy research (Ginsberg and Venkatraman, 1985). Fundamental principles of strategic management assert that performance is likely to be produced in a sustainable manner if the strategic choice is aligned with the forces driving changes in the environment. Equally, the same strategic choice should be aligned with the structure of the firm in order to create a sustained level of performance (Venkatraman, 1990). This principle contending that aligning strategy and its context has significant positive implications for performance is referred to as contingency, consistency, alignment (Bourgeois 1996), fit (Venkatraman and Camillus, 1984; Venkatraman, 1989; Yin and Zajac, 2004), or co-alignment (Bourgeois 1996; Olsen et al. 1998) in theoretical research. In essence, the co-alignment principle suggests that if firms accomplish the alignment of environmental events, strategy choice, and firm structure, then "*the financial results desired by owners and investors have a much better chance of being achieved*" (Olsen et al. 1998: 2). Thus, if the alignment of strategy choice (i.e.: unit growth) and firm structure is achieved, a sustained level of return can be accomplished.

Subsequent to the contingency approach, another paradigm emerged in strategy and organizational theory the Strategy-Structure-Performance (SSP) paradigm (Galunic and Eisenhardt, 1994). Based on the contingency assumption of fit between an organization and its environment, the SSP focuses on the interaction between strategy and structure as a determinant of performance. The particularity of the SSP paradigm is that it approaches the concept of structure in a less static fashion than the contingency perspective (Galunic and Eisenhardt, 1994). The SSP paradigm perceives organizational structure as containing a static aspect (organizational form), formal processes (administrative systems), informal patterns (personal interaction and social networks), values, and norms. This approach is broader and less rigid than approaching structure as a mere organizational design. Furthermore, the SSP approach focuses on the impact of the contingency of strategy and structure as a key element of organizational survival and success. This contrasts with the market, or environmental selection of successful companies (Van

de Ven and Drazin, 1985) and introduces a more voluntaristic view to organizational performance.

Conclusion

Risk and the management of risk have been examined through three different lenses: the financial, the strategic and the behavioral. The integration of these three fields reveals that the management of risk is related to probabilities and variance (finance) but that only the magnitude and probability of loss are taken into consideration in the practices of the management of risk. Furthermore, this synthesis effort reveals that strategic management and finance diverge in their theoretical assumptions in relation to the interaction between risk and return. Simply stated, strategic management and finance differ on their focus and the possible effects of the management of risk. Finally, the integration of behavioral work with the strategic approach and the management of risk points to the concept of control in relation to risk. But most importantly, the integration of finance, strategy, and decision behavior theory raises issues that are left unanswered.

First, the concept of risk in a strategic context is still to be further defined as insights are provided in managerial research. For the sake of coherence with the voluntaristic approach in strategy, it clearly appears that a strategic perspective to risk cannot be approached as the variance of probability distributions of possible outcomes. However, risk needs to be approached as the management of risk and also incorporate nuances such as downside risk and odds control. The integration of strategy and behavior literature reveals the centrality of control in the process of the management of risk. Control bridges the field of strategy and organizational behavior through the notion of risk. Little is still known about the role of control in the management of risk. New orientations on risk research put forward the construct of perceived outcome control as a moderator between the loss-gain domain and risk behavior of managers. Nevertheless, the question remains as to how decision-makers estimate their control over a perceived outcome. Or simply, how do managers assess for the downside risk?

Second, the process of the management of risk in strategy calls for further research. If the management of risk determines firm performance, how can managers improve it? If control is central to the determinants of risk, how does it intervene in the process of management of risk? What controlling strategies are used in the management of growth? How are these controlling

strategies related to the management of risk of expansion strategy? These are key strategic questions that are left unanswered.

In an effort to work towards the comprehension of the above questions the concept of control will be examined in the following section. Understanding the concept of risk and its determinants can provide valuable leads to answering the proposed research question.

CONTROL

Giglioni and Bedian's (1974) literature review on control in the management field reveals the early interest of researchers in the control construct. Their review tracks the construct of control back to Taylor's, Emerson's, and Fayol's "*scientific management*" in the early 1900's. Describing the evolution of the early management control theory, the authors mention three fundamentals in the management of control. First, control is, by nature, *dichotomous* with both "*the achievement of effective control over subordinates though the direction of their activities*" and "*the evaluation of the desired outcome of an activity and the making of corrections when necessary*" (Giglioni and Bedian's, 1974: 293). Second, the authors note the close association between management control and financial control in management practices. Finally, the authors acknowledge the importance of control in the management practice. These three fundamentals are persistently observed in the subsequent major publications on control in Organization Theory (OT).

Control in Organizational Theory

In order to gain insight into the construct of control in organizational research, predominant control definitions are examined. Table.1, chronologically lists definitions of control that are presented in most cited organizational works on control. This review of definitions allows the tracing of the construct formation of control and the determination of its main constituents in organization studies.

Table 1 Control in Organizational Theory: a chronology of definitions

Definition	***References***
• "That *function* which coordinates all of the other functions and in addition supervises their work"	Church, 1914: 28
• "Verifying whether everything occurs in conformity with the plan adopted, the instructions issued and principles established."	Fayol, 1949: 107
• "Control is seen as a *process* which brings about adherence to a goal or target through the exercise of power or authority."	Etzoni, 1965 Cray, 1984:86
• "Control can also mean to direct. Precisely defined control refers solely to the *task* of ensuring that activities are producing the desired results"	Reeves & Woodward, 1970: 38

Definition	*References*
• "Control is essentially concerned with regulating the activities within an organization so that they are in accord with the expectations established in policies, plans, and targets"	Child, 1973:
• "The fundamental purpose for management control systems is to help management accomplish an organization's objectives by providing a formalized framework for (1) the identification of pertinent control variables, (2) the development of good short-term plans, (3) the recording of the degree of actual fulfillment of short-term plans along the set of control variables, and (4) the diagnosis of deviations.	Lorange & Morton, 1974: 42
• The process of monitoring, evaluating, and providing feedback.	Dornbusch & Scott, 1975 Ouchi, 1978:174
• "In organizational evaluation, there are only two kinds of phenomena which can be monitored or counted; these are <u>behavior</u> and <u>outputs</u> which result from behavior."	Ouchi, 1978:174
• "Three modes of control (market, bureaucratic, and clan) along each of two dimensions: the informational requirements necessary to operate each control type, and the social underpinnings to operate each control type". • Control view through 2 questions: "what are the mechanisms through which an organization can be managed so that it moves towards its objectives? How can the design of these mechanisms be improved and what are the limits of each basic design?"	Ouchi, 1979: 837, 833
• "Operating and strategic parts need to be separated and that the strategic part requires access to an internal incentive and control apparatus."	Williamson, 1983:355
• Output control: "the performance reporting system whereby foreign subsidiaries submit a variety of data to the parents are perhaps the most visible control systems" • Behavior control: "when MNC assigns parent company managers to the key management positions of a foreign subsidiary. This is consistent with the concept of behavior control. (…) • Both represent cybernetic control processes"	Egelhoff, 1984:74
• "Control (…) encompasses any process in which a person (or group of persons, or organizations of persons) determines or intentionally affects what another person, group, or organization will do".	Baliga & Jaeger, 1984: 26

Definition	***References***
• "Control is operationalized in terms of behavior vs. outcome based reward structures".	Eisenhardt, 1985: 143
• "Control is a cybernetic, regulatory process that directs or constraints an iterative activity to some standards or purpose."	Green & Welsh, 1988:291
• "Control refers to the process by which one entity influences, to varying degrees, the behavior and output of another entity through the use of power , authority, and a wide range of bureaucratic, cultural and informal mechanisms."	Geringer & Hebert, 1989:236
• "Internal control mechanisms are designed to bring the interests of managers and shareholders into congruence. (…) The market for corporate control provides an external control mechanism whereby the shareholders' interests can be served in the event of the breakdown of the internal control mechanism."	Walsh & Seward, 1990: 423 & 435
• Two control processes (TCT) "Hierarchical control consists in explicitly telling employees what to do, and in observing their behavior to ascertain that they are following orders". "Cultural control (…) employees need not to be monitored, and they do not have to be given specific answers to specific problems: they only need to be inculcated with the goals and philosophies of the organization."	Hennart, 1991:81-82
• "Any process in which a firm determines or intentionally affects what others will do. Note that this definition of *control* includes more than an active exercise of power or authority. (…) Thus, not only how an exchange is to be governed, but also **if** the exchange is to take place should be viewed as a control decision."	Sohn, 1994:296
• "Regulatory process by which the elements of a system are made more predictable through the establishment of standards in the pursuit of some desired objective or state"	Leifer & Mills, 1996:117 Das & Teng, 1998: 493 Das & Teng, 2001:258
• "The governance structure of the alliance, or the choice between equity and non-equity alliance in our case, should be used to control the level of total risk." (*Relational and performance risk*)	Das & Teng, 1996: 839
• "In addition, control mechanisms and level of control are two other important concepts".	Das & Teng, 1998: 493

Definition	*References*
• "The purpose of control is to cause behaviours and outcomes to conform to existing goals/strategies/objectives. As such, its purpose is convergence-reducing the gap between planned and expected behaviours and outcomes."	Birnbirg, 1998:427
• "A coordinating mechanism based on asymmetric relations of power and domination which conflicting instrumental interests and demands are the overriding contextual considerations"	Reed, 2001: 201

The first particular of control is that it has an impact on all levels of an organization. This inherent aspect of control supports the use of control as a structural dimension in strategic management. The process or task of control bridges different organizational levels from individuals (Ouchi, 1979), to systems, groups (Baliga and Jaeger, 1984), organizations (Egelhoff, 1984), or general "entities" (Geringer and Herbert, 1989), all of which explains that control is examined in a wide range of areas in social sciences from organizational behavior to organization sciences. Control has been examined between managers and shareholders (Walsh and Seward, 1990), managers and employees (Hennart, 1991), foreign subsidiaries and parent companies (Egelhoff, 1984). The intervention of control in all organizational levels indicates the possibility of its use as a structural dimension in strategic management.

The second distinctive feature of control is its importance in management practices. Early inductive works on management (Taylor, 1906; Church, 1914; Fayol, 1949) pointed to control as a determinant task in management activities. In these early studies, control is a coordination process (Church, 1914), whereby managers ensure that actions are performed according to the "*principles established*" (Fayol, 1949). The construct of control is further refined to include the dimensions of regulation (Child, 1973), organization (Lorange and Morton, 1974), monitoring, and evaluating (Ouchi, 1978). These incremental contributions lead to a definition of control as a cybernetic process (Green and Welsh, 1988) and include the earlier discussed dichotomous nature of control.

A parallel with the notion of downside risk emerges at this stage with the role of control as being pivotal in the management of risk. As earlier mentioned in the section on risk, downside risk is the "*understanding of risk as performance below expectations*" (Miller and Reuer, 1996: 674). Control, in its simplest form, is a cybernetic process that ensures actions to be performed according to principles. In alignment with March and Shapira's findings (1987), managers

perceive the management of risk as the development of control strategies for actions to meet the financial objectives of the firm. This again supports the idea that the management of risk and control are intertwined. However, one central strategic question remained unanswered: If control is perceived as a cybernetic process, how can mangers determine what then should be tested, measured and reported on? What are the criteria that should be used to determine the control variables in an organization? According to Ouchi (1978), the premises for control are phenomena that can be "*monitored or counted*". Ouchi suggests that two kinds of phenomena can be controlled for: the *output* or the *behavior*. The definitions often remain vague in relation to what should be controlled as research definitions allude to objectives, planned results or desired results. These premises for control, introduced by organization theory (Ouchi, 1979; Thompson, 1967), constitute a major insight into the construct.

While control variables remain vague, the phenomena's separation suggested by Ouchi has inspired researchers to consider control systems to make the distinction between behavior and output. Egelhoff (1984) discusses "*performance reporting systems*" between foreign subsidiaries and their parent firm; Eisenhardt (1985) suggests reward structures to control for both behavior and outcome. Geringer and Herbert (1989) put forward "*Power, authority, and a wide range of bureaucratic, cultural and informal mechanisms*". Hennart (1991) discusses the hierarchical and the cultural control, and Reed (2001) sees power and domination as key controlling processes. In essence, after attempting to define what should be controlled for, processes for how to control are the second research focus.

Eisenhradt (1985) examined the determinants of control and considered them as an organizational design variable. The author integrates the Organizational Theory and Agency Theory literature to identify the determinant of control contingencies. Eisenhardt concludes that, from a theory development perspective, "*the results suggest that the combined organizational and economic perspective yields a more complete view of control than either alone*" (Eisenhardt, 1985: 146). This first integration effort on the concept of control and management opens encouraging perspective for further integrative work.

Two dominant views in organization theory relate control and management and also offer a potential for approaching control with strategic assumptions: the Agency Theory and the Transaction-Cost-Theory. In order to gain insights into the determinant of control, control in Agency Theory and Transaction-Cost-Theory is first examined in the following section. The

purpose of this examination is to uncover the organizational features that determine control in management.

- *Summary*

Organizational theory conveys three main insights into control. First, the construct of control taps all organizational levels, which supports its use for relating the strategic management and structure constructs. Second, control, as a cybernetic process appears central in management practices and presents several parallels. These parallels are evident in the idea of downside risk that emerged in the risk section. Finally, organization theorists suggest that two kinds of phenomena can be controlled for: the output and the behavior.

Control in the Agency Theory (AT)

Control is central to the organizational economics approach of Agency Theory. Agency contracts are, in fact, agreements aimed at controlling relationships. The purpose of such control is to assure the convergence of interest of the parties bound by the contract (Jensen and Meckling, 1976). AT explores the dyad formed by the principal and the agent, along with the enforcement of contracts within it. In an agency relationship, the principal is the party that delegates work to another, the agent. Therefore, the AT attempts to solve two main problems. First, it tries to resolve the conflicts in the principle and agent's goals. Second, the AT also tries to solve the problem of management costs in relation to the verification by the principal of the acts of the agent (Eisenhardt, 1989). Agency theorists argue that a principal has two options to ensure that the actions of the agent are convergent with hers. On option is to observe her behavior (process), while the other is to check her performance. In other words, the principle can either control for the processing of the agent or her final outcome. This is parallel to the measurable control elements and processes suggested in organizational control (Ouchi, 1979, Eisenhardt, 1985, 1989). Early work by Ouchi suggests that two kinds of phenomena can be controlled for: the *output* or the *behavior*" because they offer the possibility to be either "*monitored or counted*". It is interesting to note that literature in organizational control does not separate outcome control from behavior control. This nuance is not pointed out in the research on risk-taking behavior and is, thus, a refinement that the AT introduces.

Agency Theory offers insights into the determinants of control modes. Integrating the literature on organizational theory and AT on control, Eisenhardt points to three determinants of control (Eisenhardt, 1985, 1989):

- ✓ Task programmability
- ✓ Information systems
- ✓ Outcome Uncertainty

- *Task programmability*

Task programmability stems from organization theory literature (Ouchi, 1979; Thompson, 1967; Galbraith, 1973, 1978, 1979) and refers to the knowledge about a given task or process.

> "*If tasks can be programmed, then behaviors are explicitly defined and readily measured. Therefore, control is accomplished by performance evaluation of behavior. (...) Now consider outcomes. If the goals can clearly be stated, then outcomes can be measured and performance evaluations of outcomes is the appropriate control strategy*". (Eisenhardt, 1985: 135).

In other words, when the knowledge of managers of the characteristics of a task is high, they can program it and plan for its details. Practically, more programmability means more information about the behavior of the agent. In the case where little is known about the behavior of the agent (low programmability), high behavior measurement costs will have been incurred, and outcome control will be selected. On the other hand, if there is high programmability of the task, then behavior measurement costs will be minimal and behavior control implemented.

- *Information Systems*

As very early suggested by Lawrence and Lorsh (1967), Galbraith (1973), and other information processing approaches (Daft and Lengel, 1986; Ginsberg and Venkatramn, 1985; Gnyawali and Stewart, 2003), information systems play a key role in managing relationships within an organization. The key role of information resides in its relationship with the environmental uncertainty (Galbraith, 1973), external risk, as well as, task programmability (Eisenhardt, 1985), the risk of the task. Departing from the AT assumption that information is a commodity, outcome and behavior control will depend upon the information available and the prices to pay for it (budgeting system costs, inter-organizational reports). Thus, in agency theory, information systems are viewed as serving either a behavior measurement or an outcome

measurement purpose. Further, the type of measurement is based on the degree of task measurability.

- *Outcome Uncertainty*

Finally, Eisenhardt (1985) introduces outcome uncertainty to control. In agreement with agency theory's assumptions, she considers uncertainty as random effects from the external environment. AT operationalization of outcomes are as follows:

Outcome = f (employee behavior) + random effect

It is this latter, random effect that is associated with uncertainty. Agency theorists suggest that uncertainty in external events surrounding the contract is likely to raise the cost of outcome control. Coming back to the above function, an increase in uncertainty augments the random effect element, which in turn, increases the cost of output control. The cost of behavior control is not necessarily affected. In the case of very high costs for outcome control, Agency theorists propose that the improvement of information systems can reduce the overall agency costs. Similarly, if the information system in place cannot be improved at reasonable costs, the effect of uncertainty on output control costs will be at its higher level.

Integrating OT and AT literature on control has pointed out the determinants of control strategies (Eisenhardt, 1985). However, an important constraint on the conclusions of Eisenhardt has yet to be discussed the role of measurement costs in predicting control strategies. In the examination of sales stores in a commercial area, Eisenhardt found that task characteristics contributed relatively more explanatory power than do measurement systems characteristics. But these findings present limited generalizability as budgeting and other monitoring systems, components of the model, could not be observed in the selected sample. Therefore, at this stage, we can assume the predictive power of the determinants of control put forward by Eisenhardt, but remain cautious on the explanatory power of each. Simply put, the study of Eisenhardt falls short in assessing the agency costs related to task programmability, information systems, and outcome uncertainty as determinants of control. A question left unanswered is What is the role of agency costs in the construct of control?

Interestingly, economic relationships have also been addressed by another economic stream in OT, namely, the Transaction Cost Theory (TCT). According to the TCT, uncertainty stems from the nature of the transaction itself and the external setting. TCT shares common assumptions with AT, examines similar relationships, and is also concerned with control.

Therefore, it appeared important to examine this approach for organizational determinants of control.

Control in the Transaction Cost Theory (TCT)

Developing on the seminal work of Coase (1937), the ideas labeled as Transaction-Cost-Theory (TCT) propose that firms are created because there is a profit in making a transaction internally when compared to making it on the market. The profit is the economic rent that a firm can gain from a transaction. This rent is contingent upon the firm's capacity to reduce integration costs. TCT perceives integration as related to the: "*degree (*at which) *transaction-specific (nonmarketable) expenses* (are) *incurred*." (Williamson, 1979: 239). Williamson (1985) further developed this fundamental idea and advanced transaction uncertainty, asset specificity, and frequency as the three dimensions that rule whether a transaction should take place in the market or within the firm. The determinant costs allowing the discrimination between the firm (hierarchy) and market (price) are named transaction costs.

Control is present in TCT through the two transaction options: make or buy (Williamson, 1985). Researchers in TCT's stream argue there are two main and exclusive control mechanisms: hierarchy and price. Hierarchy can be assimilated to behavior-based (salaries) while markets are outcome based (Eisenhardt, 1989). Indeed, a hierarchical control process focuses on the observation of the employee's behavior and on a salary-base remuneration. On the other hand, the market control process focuses on the outcome of the economic exchange and thus is an outcome based control process. As a result, control is the benefit extracted from integration obtained from resource commitments (Anderson and Gatignon, 1986; Erramilli and Rao, 1993). In essence, in deciding to make or buy, managers are making a trade-off between control and resource commitment.

The TCT approach to the choice between integration (ownership) and contract (market) is based on a simple postulate, which states that low integration (market transaction) is preferable until proven otherwise (Anderson and Gatignon, 1986). In other words, TCT is based on a "*default hypothesis*" (ibid: 22) that contractual agreements are preferable unless three main elements are affected. The main elements that determine whether a firm should integrate the transaction rather than maintaining it under contractual agreements are as follows: frequency, asset specificity and uncertainty.

- *Frequency*

TCT postulates that if a contractual agreement evolves into a relationship where exchanges increase in frequency, integration could become a preferred option. Integration would be preferred over market transaction if the cost of resources committed augments until it to outsets integration costs. Frequency refers to the frequency of a buyer-supplier transaction. Simply, if the number of exchange increases to considerably augment transaction costs, integration should be considered. This particular feature of transaction contracts "*refers strictly to buyer activity in the market*" (Williamson, 1979: 247). Williamson (1979) put forward the transaction types based on the frequency type (occasional or recurrent) and the investment characteristics (nonspecific, mixed, and idiosyncratic). Each one of these transactions is specific to the buyer-supplier relationship (ibid).

- *Asset Specificity*

According to the transaction-cost approach, asset specificity, or transaction-specific assets, is a key determinant of market failure (Erramilli and Rao, 1993; Williamson, 1986). Transactions cost theorists define transaction-specific assets as "*nonredeployable physical and human investments that are specialized and unique to the task*" (Erramilli and Rao, 1993: 21). Several examples are often provided, such a professional know-how or skills in the service industry. TCT postulates that a transaction ought to be maintained contractual until the transaction-specific asset becomes valuable to the firm. Simply stated, if the asset is highly specific to the transaction and becomes hard to replace, its related resource commitment will offset the integration costs. As a result integration is then, preferable.

Transaction economists consider asset specificity as a key determinant feature in explaining the nature of contracts engaged by a firm (Riordan and Williamson, 1985; Williamson, 1996). Specifically, asset specificity is viewed as the principal factor that is responsible for transaction cost differences among transactions. The idea is that the more specific, the assets are involved in the transaction, the higher the transaction-incurred costs and also the higher the likelihood for firms to integrate the transaction. According to Williamson (1983 b: 522), "*costs that are highly specific to a transaction have two attributes: they are incurred in advance of the contemplated exchange; and their value in alternative use, or by alternative users is greatly reduced*". Consequently, Williamson (1983b and 1996) lists four forms of asset specificity: site specificity,

physical asset specificity, human asset specificity, and dedicated assets specificity. First, site specificity is "*where successive stations are located in a cheek-by-jowl relation to each other as to economize on inventory and transportation expenses*" (1983 b: 526). The site specificity form is assumed to reflect ex-ante decisions to minimize inventory and transportation costs (Joskow, 1988). Second, physical asset specificity refers to investments made by one of the parties that involves design characteristics specific to the transaction and which have lower values in alternative uses (Joskow, 1988; Williamson, 1983b). Simply it is the commitment of resources by one party to the transaction. This commitment is regarded as asset specificity if it cannot be easily transferred or used in another setting. Third, human asset specificity is the investment in relationship-specific human capital. In other words, it is the allocation of human resources to the tasks that are specific to the transaction. In their thorough literature review on empirical research in TCE, Boerner and Macher (2002) list different research examining the human capital specific asset. They mention research on the specificity of developing automotive components for a vehicle assembler; on working relationships between a salesperson and her organization; the specificity of communication between product designer and engineer; or individual rock band member replacement and music quality assessment; and the wife in a household, and the use of prenuptial contracts. Finally, dedicated asset specificity refers to general investments by a supplier that would not otherwise be made. The difference between asset and dedicated asset is the value of that asset outside the transaction. In the case of dedicated assets, if the contract were terminated prematurely, it would leave the supplier with significant excess capacity and the capacity of transfer would be lower than for a non-dedicated specific asset.

Asset specificity is a key determinant in the make-or-buy choice as it has a direct effect on the costs related to the transaction. From a strategic standpoint, it is also critical as it bridges external environmental conditions (nature of the contract) to resource commitment. Asset specificity is particularly interesting in the strategy implementation questions as it involves external variables, structural determinants, and resource commitment. It is, therefore, not surprising to read research in strategic management integrating asset specificity with competitive advantage (Balakrishnan and Fox, 19993). Balakrishnan and Fox relate finance (capital structure) with asset specificity for their role in forming a competitive advantage for the firm.

- *Uncertainty*

This dimension relates to the uncertainty surrounding a particular transaction or "*unanticipated changes in circumstances surrounding an exchange*" (Noordewier et al. 1990). TCT is concerned with how the "*governance of transactions is affected by increasing the degree of uncertainty"* (Williamson, 1979: 234). Transaction-cost theorists predict that if the uncertainty related to the transaction decreases (due to industry maturity for instance), then the benefit of integrating that same transaction decreases. Simply stated, if the transaction is well defined, known, and its outcome predictable, then there is little benefit in integrating it within the firm. This first type of uncertainty is labeled the internal uncertainty. It is also referred to as behavior-related uncertainty, an uncertainty dimension that is still under-examined in social research (Boerner and Macher, 2002). Using the AT and OT vocabulary, internal uncertainty is nothing more than the programmability level of the transaction, which is a determinant of the control applied in an organization. Indeed, TCT assumes internal uncertainty to exist "*when the firm cannot accurately assess its agents' performance by objective, readily available output measures*" (ibid: 15). Additionally, TCT distinguishes between external uncertainties related to the volatility of the environment and refers to them as external uncertainties (Anderson and Gatigan, 1986). This is what AT refer to as, outcome uncertainty, a determinant of control.

Transaction theorists assert that uncertainty needs to be examined in conjunction with asset specificity (Boerner and Macher, 2002), as the effect of uncertainty can be almost null in the absence of asset specificity. Simply put, asset specificity leverages the impact of mal-adaptation hazards on a transaction.

TCT has been extensively applied in research on expansion choices and vertical integration (Anderson and Gatignon, 1986; Erramilli and Rao, 1993). Transaction theorists argue that the make-or-buy choice is in fact a decision about the degree of control and the resources committed in a transaction. Simply put, decision makers will assess the degree of control in a transaction in regard to the resources committed to gain the control. Again, this points to the criticality of transaction approach from a strategic standpoint.

In addition to the other elements already discussed, it important to note that transaction costs determinants of control are developed in the buyer-supplier relationship and, thus, cannot be easily reported to all transactions and situations. As a result, frequency refers strictly to the buyer-supplier relationship and cannot be applied in non-vertically integrative expansion strategy.

Nevertheless, the two remaining elements, namely, asset specificity and uncertainty are not necessarily restricted to the relationship between a buyer and supplier and can be applied in other settings. Moreover, the convergence of the ideas of uncertainties between AT and TCT is proof of the integration potential between the two perspectives.

- *Summary*

The AT and TCT provide two major insights to the construct of control in the management of risk. First, the AT suggests that three organizational features can determine the degree of required control in a contract: task programmability, information systems, and outcome uncertainty. Second, the TCT introduces the perspective of relating control to resources commitment.

More particularly, AT and TCT offer solid integration possibilities, summarized in Table 2, as they share common assumptions and present overlaps in their approaches to control and its determinants. Both perspectives share the limited (or bound) rationality and opportunistic assumption on human behavior. As for their determinants of control, they are listed in Table 2 and will be further discussed in the following section.

Table 2 Three contributions to the determinants of control

AT: Agency Theory	TCT: Transaction Costs Theory
• Information systems • Outcome Uncertainty • Task programmability • Agency costs	• Frequency • Asset specificity • Internal & external uncertainty • Transaction costs
Assumptions • Limited rationality • Opportunistic behavior	

Control-related costs

- *Agency Costs*

The integration of *agency costs* in the approach to control is the second refinement introduced by Agency Theory. Agency costs are a sum of costs paid by the principal and the agent to ensure the convergence of the actions of the agent with the interests of the principal. Since agency contracts are essentially control relationships, agency costs are merely costs related to control. Agency costs are incurred whether the principal decides to observe behavior of the agent or to monitor his/her performance. The fathers of the AT, Jensen and Meckling (1976:6) define agency costs "*as the sum of:*

1. *The monitoring expenditures by the principal*
2. *The bonding expenditures by the agent*
3. *The residual loss*"

Monitoring expenditures are costs incurred by the principal to ensure that agent is performing and processing according to the principal's interest. The AT assumes that monitoring efforts and costs can limit but not eliminate all agency costs. According to Jensen and Meckling monitoring costs "*include efforts on the part of the principal to 'control' the behavior of the agent"*. Monitoring methods include auditing, formal control systems, budget restriction, and incentive compensation systems. Relating to the previous section on AT, monitoring costs require specific information systems based on behavior measurements. Agency theorists predict that monitoring costs are minimal in the context of high task programmability and outcome measurement. Consequently, monitoring costs are likely to increase when task programmability is low.

Bonding expenditures, on the other hand, are incurred by the agent for the reduction of agency conflicts. Bonding costs are considered as a facilitator of the agency relationship, thus reducing its costs. Simply put, bonding costs are insurance for the principal that the agent will perform within the principal's interest. In this case, bonding costs are meant to decrease the probability of the loss element of risk for the principal.

Finally, the residual loss is the opportunity cost resulting from the agency relationship and is borne by the principal. In other words, the residual loss relates to the cost, for the principal, of the divergence in the behavior and actions of the agent. The notion of residual loss is very similar to the financial principle of opportunity cost. This cost is important in investment decisions as it

reflects the cost of the "lost opportunity" of choosing a project rather than another conflicting one.

In essence, the agency contract, a set of control variables, is employed as an answer to a risk-sharing problem. If agency problems occur because different parties have convergent views on goals and behaviors, the contrac, is put in place to reduce the divergence in the opinion of the parties. In other words, control variables are employed to reduce agency costs or the divergence of interests and performance. Agency theorists argue that the higher the divergence of the interests of the parties, the higher the agency costs will be. In other words, if the interests of the two parties diverge, the principal will have to commit to higher monitoring costs, and bear higher opportunity costs. Agency theorists suggest two main agency issues: moral hazard and free-rider behaviors. The first relates to the judgment error in the selection of the agent, while the second refers to the agent using the contract to her own benefit with no respect of its binding terms. The higher these problems, the higher the control-related costs incurred by each party.

Agency costs offer a way to measure the risk related to the agency relationship based on coherent and consistent assumptions about information and organizations. Eisenhardt (1985) suggests that agency costs are affected by the costs of information systems. However, she falls short in assessing the predictive role of these costs since the sample she used (small retail stores) did not allow for the measurement of such effects. Consequently, the role of the costs of information systems in control and the management of risk is still left unknown.

- *Transaction Costs*

Benefits, trade-offs, and determinants of control under the TCT cannot be considered separately from transaction costs (Emeralli and Rao, 1993). Economists define a transaction cost as the expenditure (both pecuniary and non) incurred by making an economic exchange. Coase (1937), the first contributor to this theory, discusses three components for a transaction cost:

1. The cost of information search,
2. The bargaining cost, and
3. Policing and enforcement costs, or integration costs.

The determinants of transaction costs are rather intuitive. The two first transaction costs refer to the costs of collecting information that would allow for decision-making. They are based on a shared assumption between AT and TCT that perceive information as a purchasable

commodity. Similarly, the higher the estimated bargaining cost in an economic setting, the higher will be the resources to be committed.

Integration costs have been covered in the previous section. Levels of frequency, asset specificity, and uncertainty related to a transaction determine integration costs. Integration costs relate to the costs incurred when operation units are owned. In this case, significant internal organization and bureaucratic costs (legal, administrative, and operating related costs) are incurred (Davidson and McFetridge, 1985; Erramilli and Rao, 1993). Therefore, integration costs can be viewed as the supplementary agency costs incurred by the shift from market transaction to hierarchy. Transaction theorists argue that integration costs can be given up if control is gained from the transaction's change in nature.

A father of the modern TCT, Williamson (1983b) also discusses a particular association between resource commitment and asset specificity--transaction hostages. The idea is that asset specificity has the effect of placing contracting parties in a bilateral dependency relationship, thus "*credible commitments*" would support hostages in the exchange. The notion of credible commitment is similar to the concept of bonding cost introduced by Jensen and Meckling. Specifically, Williamson points to the dual role of "credible commitments", or hostage resources as having "*both ex ante (screening) and ex post (bonding effects, the ex post contract execution consequences are of principal interest* " (Williamson, 1983b: 521). Simply put, bonding costs or credible commitment play an important role in shaping the nature of the transaction as they correspond to financial investments made by a party as a commitment in the transaction.

In conclusion, both agency and transaction costs present strong relationships with control. In the case of agency, control is a tool for the management of agency problems. In transaction costs, control is a potential benefit to be gained from investing in a transaction. While each perspective departs from similar hypotheses, AT and TCT propositions on control seem to complement each other. In the following section, transaction and agency approaches to control are integrated.

- *Control-related costs and the management of risk*

One element emerges from the above section on AT, TCT, and their respective costs and that idea is that control carries a cost. More particularly, each form of control presented in the organizational and behavioral literature comes with a cost. The behavior control, predominant in

the AT, requires monitoring costs. Output control, predominant in TCT, is obtained with the allocation of contract costs or output contract costs.

Founding propositions in the AT depart from the assumption that the principal will observe the behavior of the agent to ensure the convergence of their interests. When behavior control is not possible, the principal is then assumed to bind the agent to measures of performance. As mentioned in the previous section, monitoring costs are efforts on the part of the principal to control the behavior of the agent (Jensen and Meckling, 1976). Therefore, founding propositions in AT are formulated on behavior control and its attached monitoring costs. Agency theorists propose that behavior control is in place in contracts (or organizations) when monitoring costs are low.

Similarly, TCT is founded on the output control (contracts) and their related output control costs (contract costs). As earlier mentioned, TCT is grounded in a "*default hypothesis*" that a contract is the best solution until proven otherwise. This assumption simply states that the contract best accommodates for transaction costs until changes occur in the nature of the exchange involved. According to transaction theorists, output control is employed when output control are low. Once the nature of the exchange evolves to a more asset-specific or uncertain one, output control costs can increase and become higher than monitoring costs. In this case, behavior control (hierarchy in TCT terms) becomes an option. In sum, the AT and TCT propose a similar postulate the cheapest form of control is to be chosen. The determinants of control costs, are however, not similar in the AT and TCT.

AT suggests that task programmability, information systems for control measurement, and outcome uncertainty determine control costs and also control practices. TCT, however, suggests that transaction frequency, asset specificity, and uncertainties (internal and external) determine the contract costs, in turn, control practices. While those assertions might appear contradictory, a closer examination reveals that they actually complement each other. First, outcome uncertainty in AT taps the same idea that the TCT external uncertainty does. Second, task programmability, corresponds to the TCT internal uncertainty. As for information systems, they are very similar to the information search costs in TCT, but in a different stage of the relationship development. Asset specificity and transaction frequency are the only concepts that do not echo in the agency perspective on contracts. Based on the listed similarities and shared assumptions between the AT and TCT, asset specificity and transaction frequency will be maintained rather than excluded.

Below is a summary of the fundamental relationships found in the reviewed literature. These propositions relate organizational features, organizational control, and costs related to control.

- Task programmability: corresponds to the degree of information that the principal has concerning the agent's actions.
    - The lower the programmability, the less the principal knows about the behavior of the agent, the higher the monitoring costs, the higher the likelihood for output control reliance.
    - The higher the programmability, the more the principal knows about the behavior of the agent, the lower the monitoring cots, the higher the likelihood for behavior control.
- Outcome uncertainty: the degree of the assurance of the principal that the agent will deliver a certain output or outcome. The degree of outcome uncertainty does affect the cost of outcome control, but does not affect behavior control (Eisenhardt, 1985).
    - The higher the uncertainty about the outcomes of the contract, the higher the resources required to control for the outcome, the higher the likelihood for behavior control
    - The lower the uncertainty about the outcomes of the contract, the lower the resources to be committed to control the agent's output, the higher the likelihood for output control
- Transaction frequency: the number of times during a defined period of time that the transaction takes place. This determinant of control-related costs is specific to the supplier-buyer relationship and does not hold in other relationships.
    - The higher the transaction frequency, the higher the transaction costs, the higher the likelihood for transaction costs to outweigh integration costs, the higher the likelihood for behavior control.
    - The lower the transaction frequency, the lower the transaction costs, the higher the likelihood for transaction costs to be less than integration costs, the higher the likelihood for contract (output) control.
- Asset specificity: refers to the uniqueness of the asset involved in the transaction. The more specific to the principal's activities, the more specific is the asset.
    - The higher the asset specificity, the higher the resources committed in its transaction, the higher the transaction's costs, the higher the likelihood for behavior control (integration).

    - The lower the asset specificity, the lower the resources committed in its transaction, the lower the transaction's costs, the higher the likelihood for contracts and output control to be maintained.
- Information systems: refers to the control measurements in place in the organization. Information systems can either be behavior-based or measurement based.
    - The higher the reliance on behavior-based measurement systems, the higher the chances for the principal to have information about the agent's behavior, the higher the likelihood for behavior control to be in place.
    - The higher the reliance on outcome-based measurement systems, the higher the chances for the principal to have information about the outcome's certainty, the higher the likelihood for outcome-based control.

Summary

Organizational theory conveys three main insights into control and sets the stage for a control perspective. First, the construct of control impacts all organizational levels. Second, control, presents several parallels with downside risk. Finally, organization theorists suggest that two kinds of phenomena can be controlled: the output and the behavior.

Agency theorists propose task programmability, information systems, and outcome uncertainty as determinants of control in a transaction. Transaction theorists relate control to resource commitments and introduce asset specificity, frequency, and uncertainty aspects as determinants of control. Since both perspectives share the limited (or bound) rationality and opportunistic assumption on human behavior, their propositions present integration potential.

Additionally, both AT and TCT share a concept in common which is that costs related control. Simply, control is managed in relation to its inherent costs. These control costs are examined in relation to the phenomena to be controlled for (the output and the behavior) and their coherency with the determinants of control (task programmability, information systems, outcome uncertainty, asset specificity, and frequency).

EXPANSION STRATEGY: GROWTH OPTIONS FOR MULTINATIONAL HOTEL CHAINS

This research effort goal is to enhance our comprehension of the relationship between strategy and structure through the introduction of a control prospect. The control perspective has revealed that the management of risk and control are closely related. The examination of risk through the lenses of finance, strategy, and behavioral literature reveals that risk in strategy cannot be detached from the management of risk, which in turn, is intertwined with control. Therefore, control has also been reviewed in the first part of this chapter to explore its determinants. The purpose of such exploration is to determine the variables that would allow connecting control and the management of risk. Due to the exploratory nature of this work, an inductive effort is to be conducted in order to reveal such connections. It is thus suggested to conduct a contextual research in order to better define the boundaries of the explored relationships. Therefore, in this section, risk and control are examined in a contextual setting, namely, expansion strategy in the hotel industry.

Contextual research

International hotel chains employ six main options when managing their expansion strategy: full ownership, joint venture, lease, rental, franchise, and management contract (Chathoth and Olsen, 2007; Erramilli, Agarwal, and Dev, 2002; Zhao, 1994; Zhao and Olsen, 1997). The trend today among publicly traded multinational hotel chains is to decrease the proportion of fully or partially owned units (or equity options) and focus on the remaining, non-equity, four options. Non-equity growth options are suitable to consumer-services business models (i.e.: hotels and restaurants) when compared to professional service firms (Erramilli, 1990). The non-equity growth option's suitability with the hotel business model explains their widespread applications. In practice, a regional distinction has to be made, as lease, rental, and management contract options are predominant in Europe, whereas franchise prevails in North American's expansions (Jones Lang LaSalle 2001 and 2005 survey).

It is common in the strategic literature to group the six growth options named above into two main categories (Dunning, 1988; Erramilli et al., 2002): equity and non-equity options. Full ownership and Joint Venture (JV) are the two equity participation expansion modes employed by multinational hotel chains in their expansion strategy. As for the remaining four options, they are

the non-equity options and are essentially contractual modes (Dunning, 1988). For the sake of coherence with this grouping practice, the following section examines strategic growth options based on the equity vs. non-equity distinction.

A parallel with the previous sections on risk and control is important to make at this time. The distinction between equity and non-equity expansion modes is important as it reflects the degree of "credible commitments" or the importance of the transaction hostages invested by the hotel chain in its expansion option. Transaction theorists perceive "credible commitments" as the key strategic decision in a transaction as it will affect transaction costs and determine market failure. From the AT perspective, the equity participation of the hotel chain represents the bonding costs and affects the control-related costs incurred by the contract. Therefore, equity participation aspects will be considered as bonding costs from hereafter.

Non- Equity participation

Research related to entry modes in the hotel and restaurant industry reveals that the important question for "*many service firms desirous of entering foreign markets, (...) an important question is not how to choose between different equity and non-equity modes but how to choose between different non-equity modes of organizing their operations in the foreign markets*" (Erramilli et al., 2002: 224). As mentioned above, multinational hotel chains employ four non-equity growth options in the implementation of their expansion strategy. These options are presented in the following section, along with their relationship with risk, while control is briefly introduced.

Rentals and Leases

A leasing contract binds a real-estate owner (the lessor) to a tenant (the lessee). Under a leasing contract, the lessor gives the lessee the right to occupy the real estate in exchange of a determined payment and the respect of a code of conduct described in the contract. The terms real estate (in this particular case, hotels) "renting" and "leasing agreements" are often used interchangeably. The detailed legal distinction between these two types of contracts is beyond the scope of this study. For the sake of simplicity, we will only point out the fundamental difference between these two options, which is that a leasing agreement covers a fixed pre-determined period during which any change to the contract can only be made with both parties' agreement. On the other hand, a renting agreement does not fix both parties over a long-term period. It is for their stability that lease contracts, and not rent contracts, are predominantly used in the hotel

industry practice. Since lease contracts are the predominant growth option in the industry, the following discussion will focus on leases agreements.

- *Parties involved*

The lessor is the real-estate owner, or the legal entity that owns the title of the lodging property. This entity can be a person, a corporation, or an institution. The main works in lease contract valuations point towards diversification as the main benefit provided by leases to real-estate owners (Peterson & Singh, 2003; Corgel & deRoos, 1997). In terms of the lessor's risk exposure, these works point to the lessee's credit risk as the lessor's most common concern in lease agreements. With the focus of this study being on the perspective of the international hotel chain, the study of the risk carried by the lessor will not be further developed.

In the context of the multinational hotel chain lease contracts, the hotel chain is the lessee or tenant of the hotel owners present in its network. Ambrose et al. (2002) simply summarizes the relationship between the lessee and lessor as follows: "*Leasing separates property ownership from property use where the lessor receives lease payment and the residual property value while the lessee receives the use of the property over the lease term*".

Investing in lease as a growth option defers from the equity participation option as the chain does not own the property. From the hotel chain perspective, this difference favors its capital requirements, since the rental option does not involve purchase capital collection. However, in terms of operation, most of the risk related to managing the lodging property is carried by the international hotel chain. The residual value of the property and the lease payments are obviously to the benefits of the lessor. Rent payments are pivotal in the leasing contracts as they directly affect each party's risk. Rent details (amount and related provisions) are key controlling tools in the lease contract and are becoming more and more complex.

- *Key provisions in lease contracts*

Rent is the most critical clause in lease contract negotiation. However, there are complementary areas that are critical in the determination of a lease contract in the hotel industry (Rowland, 2000). Following the rent provisions in a lease contract, indexation clauses, options to renew or terminate, options to purchase, upward only adjusted rent, contingent use of the asset, and leasing incentives are the most critical negotiation elements. In the case of the lease option, each one of the six areas can have an impact on risk determination in the case of lease options

(Rushmore, 2002; Andrew, 2007). Particularly, from the hotel chain perspective, rent, indexation clause, and leasing incentives will affect the form of organizational control. In regard to options to renew or terminate, options to purchase, options to upward adjustments of rent, option of contingent use of the asset, they will affect the uncertainty aspect of the relationship.

- *Growth option, control, and the management of risk: Leases*

In this growth option, the transaction relates the hotel chain with the hotel owner on a leasing contract. From the AT perspective, the lessor is the principal and the lessee is the agent. In other words, in a lease contract the hotel chain is the agent and the hotel owner the principal. Thus it is the hotel owner that will deploy efforts to control for the hotel chain's behavior or performance. This research is focused on the hotel chain's the management of risk efforts and will, thus, examine the control-related issues in a leasing contract from the agent's perspective.

Rent is the pivotal tool used by the hotel owner to control for the hotel chain's performance and behavior. The simplest form of lease contract is where the rent payment is fixed over the contractual usage period of the property. Under a fixed lease agreement, the tenant agrees to pay a fixed amount of cash flow on a pre-defined time basis over the lease agreement length. In this case, the lessor is exposed to the lessee's credit risk and also to inflation. As for the hotel chain, it is under the pressure of generating enough cash flow to cover the lease payments. Therefore, internally, the hotel chain's control imperatives are similar to those faced by the lessor when owning the unit. Nevertheless, the nature of leases has an effect on the relationship between the hotel chain and the hotel unit. Therefore, the examination of the lease characteristics can introduce nuances in the control relationships between the hotel chain and the owner of the new unit. A central characteristic of lease contracts is the rent. The practice of lease agreement, especially in Europe (Jones LangLasalle, 2005), has lead to the creation of more complex rent clauses. Complexity in rent clauses ranges from a periodic adjustment of the payment using external indexes such as CPI, real-estate market prices, or internal measures of profitability such as net profit or EBITDA. According to the last industry survey (Jones LangLasalle, 2005), three rent forms are presently applied to the European hotel lease contracts: the fixed, the semi-variables, and the fully variable rent leases.

- The fixed rent lease, while predominant in the lease agreements, is less and less practiced in the industry. Less than one third of the contracts examined were based on a fix-rent.

- On the contrary, the semi-variable is becoming the predominant rent practice (over 60% of contracts). Under a semi-variable structure, the hotel company pays a lower fixed rent, complemented by a performance-related payment. The most common indices of performance are usually the Gross revenues or an agreed upon level of performance.
- As for fully variable rents, they remain the exception, representing approximately 5 % of the examined contracts. These types of agreements provide for a variable rent payment by the lessee based on performance indices such as Gross Revenues.

Through the TCT lenses, the above forms of contract lease affect the asset specificity of the transaction. The lower the fixed component of the rent correlates to the asset specificity level being higher in relation to the transaction. Particularly, the variability component of the rent is a credible commitment by the hotel chain into the transaction. This hostage situation is likely to increase integration costs for the hotel chain. In relation to organizational control, the indexation of the agent's remuneration on performance measures reflects the introduction of a performance type of organizational control. From the hotel chain's standpoint, this imposes a constraint on the internal existing control structure. Simply, if the transaction is based on output control, the hotel chain will have to allocate resources into output control measurement tools.

Similarly, and in accordance with transaction theorists postulates, asset specificity needs to be examined in conjunction with uncertainty. Therefore, the rent clauses need to be examined in conjunction with key provisions list above and not yet discussed.

Finally, under the lease agreement, the hotel chain is the agent. Consequently, it does not incur monitoring costs on its relationship with the hotel owner. However, the hotel chain needs to invest in information search costs, bargaining costs and, most importantly, bonding costs. Thus, it is likely for a hotel chain to incur ex-ante costs related to the screening of the new hotel unit, but also ex post costs through the commitment of resources in the relationship. This commitment of resources can take the form of equity participation in the lease or other investments that increase the asset specificity aspect of the transaction.

Management Contracts

Despite their widespread use (Erramilli et al. 2002), hotel management contracts are not extensively covered in academic work. To the best of our knowledge, currently, six academic works on management agreements have been conducted. Eyster (1988) pioneered the research on this widely employed growth option in the "*Negotiation and Administration of hotel and restaurant management contract*". Later, he published an article in 1997 updating his 1980s findings. Two other Cornell Hotel and Restaurant Administration Quarterly articles have treated the subject (Johnson, 1999, and Shindler, 1997). Finally, two articles (Armistead, 2004; Beals & Denton, 2005) have been lately published in the Journal of Retail & Leisure Property. Due to this limited academic literature, the following review will also include practitioners' publications such as the Jones Lang LaSalle hotels 2001 and 2005 hotel survey.

In this section, hotel management contracts are defined, the parties involved are presented, and the agreement's particularities presented.

- *Definition*

A hotel management contract, or management agreement, is a written agreement biding a hotel owner and a hotel operator. Through a management contract, a hotel owner (principal) employs the operator as an agent (employee) to take full responsibility of the management and operation of the property.

> "*As an agent, the operator pays, in the name of the owner, all operating expenses from the cash flow generated from the property, retains management fees, and remits the remaining cash flow, if any, to the owner. The owner supplies the lodging property, including any land, building, furniture, fixtures, equipment, and working capital, and assumes full legal and financial responsibility for the project.*" (Eyster, 1988: 4).

In essence, the hotel owner hires the operator to run her property in exchange for a management fee. Therefore in a management contract-based transaction, the hotel chain is the agent and the hotel unit's owner the principal. Similar to the lease relationships, the controlling efforts will mostly be on the hotel unit's owner, while the hotel chain will incur probable bonding costs and ex ante efforts.

Parties involved

The operator is "*a chain operating company or an independent operating company, whose function is the professional management of a hotel property*" (Eyster,1988: 4.) In a management contract, the operator has the *exclusive* rights to manage the property. The operator can either be a chain or an independent operating company. According to Eyster's work, an international trademark and reservation system are the distinguishing elements between a chain operating company and an independent operating company. In this study, the focus is on chain operating companies, particularly those operating at the multinational level. In a management contract, the operator provides her expertise in operating a lodging unit and access to her reservation systems. In his exploratory work on management agreements, Eyster (1988:7) lists twelve main elements that are generally, provided by the operator. These twelve elements detail the operating and management duties of the operator on the property:

1. Human resources: "to select, employ, terminate, supervise, direct, train, and assign all employees of the owner engaged in the operation of the property".
2. Pricing and revenues: "the operator agrees (…) to establish all price and rate schedules and to collect all receipts for all services or income of any nature from the operation" Eyster (1988:7).
3. Accounting, budgeting and reporting systems have to be maintained on the owner's behalf
4. Legal representation: maintaining and obtaining licenses on owner's behalf.
5. Negotiate service contracts
6. Purchasing: Purchase of material required for the operation of the property
7. Plan and prepare for advertising
8. Preparation of annual budgets
9. "To make or cause to be made all necessary repairs, replacements, and improvements
10. Comply with the law" Eyster (1988:7).
11. Provide access to the reservation system

The other part is the owner, the legal entity that owns the title to the property. The entity can be an individual (proprietor, partnership) or an institution (commercial bank, savings bank, pension fund, real-estate investment trust –REIT-). Under a management contract, the owner is responsible for liabilities and debts related to the duties of the contract and passes on his

management rights to the operator. As earlier mentioned, the owner provides the operator with the premises and working capital required, as well as, her rights of inference on the operations. Eyster (1988) has identified nine major owner's contractual obligations:

1. Supply of adequate assets and funds
2. Maintenance of working capital flow at a minimum level
3. Grant the operator the exclusive operational right to act in her name
4. Agreement of non-interference
5. Assumption of employees' reasonability
6. "Carry minimum fire, general liability, workers' compensation, employer's liability, and bonding insurance and to hold operator harmless for any loss sustained, irrespective and regardless of any negligence on the part of the operator"
7. Payment of management and incentives fee to operator as a compensation
8. Payment of Operator's head quarter's charges at pro-rata
9. Right of first refusal: "to give the operator the right of first refusal or the right of first offer to purchase the property if the owner sells the property during the term of the contract."

In essence, the management contract leaves control over the operations in the hands of the hotel chain.

- *Distinctive Features*

Three contract provisions characterize the nature of a management contract: the owner is restricted from inferring in the property's operation, the owner pays all operating and financing expenses, the operator does not take any responsibility, except for fraud or gross negligence. (Eyster, 1988).

The three characteristics of a management contract mentioned above shape a very a specific relationship where the owner bears a considerable amount of risk. Indeed, the owner bears all financial risk related to the project since he/she is required to pay operating and financing expenses. The operator manages the operating risk while the owner has no right of interference. The human resource management best illustrates this agreement where the owner pays employees' salaries but is required to limit his/her interference in their operations. In essence, the owner has no control over the operational risk of the project, while bearing all financial risk. In

this case, international hotel chains achieve to maintain both the probability and magnitude of loss to a minimum.

- *Control in management contracts*

The special nature of the employment agreement between a hotel owner and an operator under a management contract shapes a specific relationship where the power balance between the two parties is determinant (Armistead, 2004; Beals & Denton, 2005; Johnson, 1999; and Eyster, 1997). Five management contract provisions have been determined as critical in the literature (Beals & Denton, 2005; Eyster, 1988):

- Contract term length and renewal options,
- Fees and fees structure,
- Operator loan and equity contribution,
- Termination provisions including performance provisions
- Budgeting and spending limitations

Contract term length and renewal options, as well as, termination provisions affect the level of uncertainty of hotel chains about the future of the transaction. Thus these two provisions reflect the transaction-related degree of uncertainty. However, the fees and fee structure, along with the budgeting and spending limitations, control for the agent's behavior and/or performance. Finally, the operator loan and equity contribution are clearly a bonding costs (or credible commitments) of the hotel chain to the transaction.

Fees and most particularly, fee structures determine the behavior of the hotel chain, the agent in the contract. The degree to which the fee structure will be based on outcome will determine the organizational control that the hotel chain will have to institute. Simply, if the fee structure is based on outcome or performance measures, the hotel chains will have to commit to a control based on performance. Similarly, if the fee structure is based on behavior control, the hotel chain is most likely to implement behavior-based control and incur monitoring costs. According to AT, the higher the reliance on outcome-based control is, the higher the effect of uncertainty on controlling costs. Similarly, strict budgeting and spending limitations aim at quantitative control for the hotel chain's behavior. As for termination provisions based on performance provisions, they are clearly implemented to control for the hotel chain's performance. It is thus suspected that

under a management control, resources will have to be committed in both output and behavior control.

Franchises

International hotel chains have extensively relied on franchise options for their expansion strategy starting from the late 1970's (Littlejohn & Roper, 1992; Olsen & Merna, 1992; Olsen et al. 1998). Franchising offers a flexible growth option for international hotel chains in a capital scarce environment as it can be based on either no equity participation from the international hotel chain or a minor involvement level (Zhao, 1994; Zhao & Olsen, 1997). The international franchise association defines a franchise as

> "*Business model created by someone or a team of people, called the franchisor, that grants the right to someone (the franchisee) to sell the business model's proven or well-recognized goods or services under a pre-defined set of terms and conditions, also known as a "system*".

In other words, it is a business agreement, whereby one party (the franchisor) grants the right to another party (the franchisee) to use her product, trade name, or business format under specific conditions.

There are three main types of franchises: the product franchise, the trade name franchise and the business format franchise. The first, product franchise, is restricted to the right to sell a specific product, while, the second, the trade name franchise, is the right of using a specified licensed trade name. Finally, the business format franchise is based on both a brand identity and standard of production or sale. The following discussion is related to the latter franchise option, as business format is the predominant option in the franchise research and in the hotel industry. In the following section, the parties involved in a franchise agreement are presented. Then, the key provisions in franchise contracts are briefly discussed, as will, control in the context of franchise then to be examined.

- *Parties involved*

Contrary to the lease contract, under the franchise option, the hotel chain is the principal and the agent, the hotel operator (can either be the owner or mere operator).

Franchisor: is the entrepreneur or the legal entity that has developed and owns a particular concept. Major hotel chains such as Marriott or Hilton rely on franchising for their expansion

strategy. Under a franchise agreement, the franchisor provides the brand identity (i.e.: name, logo), the method and standards to be followed in the production or preparation of specified items. The franchisor is also bound by the franchise agreement to provide the franchisee with assistance along with the organizational and technical skills needed to efficiently manage the business. Consequently, the franchisor is liable for the development of a system that ensures the standardization and uniformization of the product and service in different environments.

Franchisee: is the independent operator, entrepreneur, or the legal entity that purchases the right to use a specified business model for a fixed period of time. The franchisee also enjoys the franchisor's know-how and technical support. In turn, the franchisee is bound to respect the franchise's standards and methods, as well as, the product and service quality set by the agreement. Finally, the franchisee is liable for a set of payments to the franchisor. These payments include the initial fees, royalty fees, reservation fees, and advertising or marketing fees.

- *Key provisions in franchise contracts*

✓ Franchisee fees: As above mentioned, franchise fees in a standard franchise agreement are comprise of an initial fee, a royalty fee, reservation fee, and advertising or marketing fees. The initial fee is the fee paid to obtain the franchise rights. It is an upfront payment, usually required upon contract signature. This fee is either a fixed pre-determined amount, or computed on a room-basis. As for royalty fees, they cover the continuing services provided by the franchisor. Common practice in the lodging industry is to base the royalty fee as a percentage of room revenues. The reservation fees are specific to the lodging industry and are meant to cover the franchisor's reservation systems' costs. Each hotel chain offers a particular basis for reservation fees computations. These can vary from a fixed amount, to a semi-fixed, to a variable one based on the number of reservations made through the system. Finally, the advertising and marketing efforts fees are meant to cover the franchisor's centralized efforts to promote and develop the brand name.

In addition to the franchise fees details, which directly affect cash flows of parties, the term, advertising efforts, operating details, training, and competition clause are the five key provisions in a franchise agreement.

✓ Franchise term: refers to the duration of the contract. Generally, a provision of renewal is also negotiated along with the franchise term. The length of the contract has an impact on the estimated returns derived from the agreement, thus, on the risk estimate of both parties.

✓ Advertising: this provision refers to the efforts of the franchisor to promote and develop the brand. It is often a source of frictions between the two parties, as they have divergent interests. On the one hand, the franchisor is inclined to invest in the international development of its brand name for further extension, while, on the other hand, the franchisee would benefit from the local promotional and advertising efforts to increase its revenues.

✓ Training: this provision details the training obligations of the franchisor towards the franchisee as part of its technical support. Equally, for the sake of uniformity and quality standards maintenance, the franchisor can often require special training for future franchisees. This provision is often a source of tension, as it requires efforts and involvement of each party, for the other's benefits.

✓ Competition clause: the latter provision restrains the franchisee from operating a competing unit in a specified geographical area. This restriction can even bind the franchisee to non-competition even after the end of the franchise term. Obviously, this provision is meant to restrain franchisees from using their know-how and new acquired competences in developing the franchisor's competing businesses.

In the following section, control issues are examined from the standpoint of the hotel chain (franchisor).

- *Franchise and control*

Research on franchising has proposed, researched, and contrasted two main approaches to explain the determinants of the choice between franchise and ownership: the resource scarcity thesis (Carney and Gedajlovic, 1991; Lafontaine and Kaufmann, 1994; Vazquez, 2005) and the agency theory (Ackerberg and Botticini, 2002; Lafontaine, 1992).

The resource scarcity view extends early works on franchise proposing that franchising is related to the firm's life-cycle (Oxenfelt and Kelly, 1968) to assert "*it is the lack of financial and managerial resources which is imputed as the cause for the high reliance upon franchising in a firm's early development*" (Carney and Gedajlovic, 1991: 608). Simply, this perspective builds on the life-cycle approach and proposes that young firms franchise because they are pressured by a

lack of critical resources, while larger and older firms will own their units. In other words, life-cycle defenders predict that younger firms are more likely to franchise their units to deal with the resource scarcity they face. This perspective has been revised when Lafontaine and Kaufmann (1994) raised a simple, but fundamental, question of Why did old and large firms, with capital, present a large proportion of franchised units? Agency theorists suggest that AT provides better explanations as to why firms chose franchising over ownership. AT hypothesizes that franchising decisions were driven by the need to reduce agency problems and costs. Simply, the contractual relationship relating the franchisor (principal) and the franchisee (agent) releases agency challenges inherent to the employer-employee relationship. Agency theorists, thus predict that firms will chose to franchise, rather than own, in order to reduce the agency costs related to controlling a specific relationship. In sum, the AT perspective proposes that agency imperatives, stemming from control requirements, determine a firm's decision to franchise its unit rather than own it.

Carney and Gedajlovic (1991) examined and contrasted each perspective in a strategic context. They conclude that both perspectives contain the explanation for the franchise-ownership decision as,

> "*Firms choose franchising as a means of achieving faster levels of growth by delimiting their resource constraints. However, where agency problems associated with franchising are strong, administrative efficiency considerations reduce the potential of growth through franchising. In other words, administrative efficiency mediates the franchise for growth relationship*" (ibid: 619).

Simply, administrative efficiency cost, or control-related cost, is a key, mediating variable in the franchise-ownership expansion decision. This contribution does bring insight into the question of why do firms choose franchising over unit ownership. Nevertheless, this integration work falls short in relating administrative efficiency costs to another key element in expansion decisions: the management of risk. Suggesting that control-related costs are mediating the expansion choice relates to proposing that administrative efficiency costs relate to the management of risk, since risk is in the core of expansion decisions. The authors, Carney and Gedajlovi, pointed to the fact that franchise systems are a way to adapt to market changes, but missed the view that risk is a key construct for strategic adaptation to environmental changes.

Latest research in the economic field seems to indicate control as a key element in the strategic decision for franchise. Lafontaine and Shaw (2005) have conducted a longitudinal analysis on almost 5,000 U.S. and Canadian franchisors from 1980 to 1997 and observed that firms worked on maintaining a stable level of owned units, determined by brand name. First, this research confirms the life-cycle perspective's low predictability power. Lafontaine and Shaw observed that franchisors "*with eight or more years of experience and at least 15 outlets maintain a constant percentage of company-owned outlets*" (ibid: 146). Second, a brand name is introduced in the franchise-ownership decision as the researchers observed a distinctive behavior between high and low brand name companies. Third, this research sheds light on the role of administrative efficiency costs in expansion processes. Lafontaine and Shaw observe "*franchisors with high brand name value target high rates of company ownership*" (ibid: 148) as they need to manage higher risks of franchisees' free ride. In other words, the administrative efficiency costs are higher for strong brand name firms as one type of agency problem, free ride, becomes predominant. When the free ride possibility is high, the "*franchisor need to exert more managerial control, and they do so by owning and operating a larger percentage of their outlets*" (ibid: 148). This research strengthens the need for relating control with risk for an enhanced comprehension of expansion strategy. More specifically, it is important, at this stage, to take the risk-control interaction in expansion strategy a step further. It seems that the costs related to control play an important role in the management of risk for expansion strategy. These control costs are related to parties' mal-adaptations such as moral hazards. Further developing our understanding of the determinant elements in expansion processes is a milestone towards the comprehension of performance in expansion strategy.

- *Growth option, control, and the management of risk: Franchise*

In this section, franchising is integrated in the literature review compiled so far in this second chapter. In other words, key determinants and features of a franchise contract are examined in the context of TCT, as management of risk and control are examined in the context of AT. Once again, the focus will be on the hotel chain's perspective.

First, the initial fee is a commitment in the transaction by the agent to the principal. Therefore, it is a bonding cost or resource commitment by the hotel operator to the hotel chain. The higher the initial fee is, the higher is the hotel chain will be secured against moral hazard and

hotel operator's opportunistic behavior. Second, the royalty fees, which are commonly a percentage of room revenues in the hotel industry, are one of the principal's sources of revenues. Using the TCT terms, royalty fees are transaction rents gained by the hotel chain. This rent is contingent upon the agent's sales performance. Third, the advertising and marketing fees allow for the coverage of the principal's investments incurred for the maintenance of the brand name.

As principal, the hotel chain will invest in controlling systems. The purpose of such systems will be to either control for the operator behavior or her performance. Monitoring costs will thus include managers' supervision of the franchisee's unit (Bradach, 1992) and formal behavior measures, such as benchmarks, across franchised units (ibid). Output control measurement costs will include the resources allocated to the control of the performance of the franchisee.

Equity participation

Distinguishing between equity and non-equity involvement for growth options is important in a strategic management context (Erramilli, Agarwal, and Dev, 2002, Contractor and Kundu, 1998). Exploratory research in the international hotel industry has revealed that "*the degree of environmental analysis* (i.e.: country risk, location) *conducted by respondent lodging firms was a function of the total investment they were required to put into their foreign lodging project*" (Zhao and Olsen, 1997: 86). Simply put, whether an international firm has equity involvement in the selected growth option will determine its organizational efforts and commitments. While the trend is oriented towards an increasing pressure on hotel chains to invest greater sums in their foreign operations (Zhao and Olsen, 1997), their commitment remains correlated with the level of equity involved in a growth option. This is consistent with transaction theorists' assertion related to the impact of asset specificity, resource commitment, and transaction exchange hostage. According to the TCT, the higher the resources are that are committed into a transaction, the higher the asset specificity aspect will be. Furthermore, along with the above parameters the higher the transaction costs are likely to be, along with the higher the impact of uncertainty on the transaction will be.

- *Equity participation and control*

> "*When comparing entry modes, the only generalization that could be made with reasonable certainty is that wholly owned operations allow the firm more control than do other arrangements*" (Erramilli and Rao, 1993: 20).

In the multinational hotel chain environment, full ownership and limited ownership (joint ventures) are the only two growth options involving the hotel chain's equity. This financial participation has an impact on the share of risk carried by the expansion firm and not only shapes its efforts and commitments, but also its control levels (Erramilli and Rao, 1993). Under the (full) ownership growth option, the international chain fully owns the hotel and fully controls its operations. The risk related to the operations of the lodging unit is fully carried by the hotel chain. Since no other party is involved in the direction of the investment, contractual costs such as bonding, information search and bargaining costs are not considered at the hotel chain-hotel unit transaction level. Rather, management will be concerned with monitoring and enforcement costs related to integration. In this case, control and agency relationships are observed in the employer-employee relationship.

Joint venture is also an equity participation of the hotel chain's corporate head, but this participation in the lodging property's unit remains limited. In this case, the international hotel chain and the JV partner proportionally share the risk. From a TCT perspective, joint venture is a hybrid form where resources are committed and hold the parties hostages in the transaction.

Summary

International hotel chains employ six main growth options when implementing their expansion strategy: full ownership, joint venture, lease, rental, franchise, and management contract. Under the full ownership and the joint venture options, hotel chains have higher degrees of "credible commitments" as the hotel chain commits equity into the transaction. According to the AT and TCT, this specific commitment sets the stage for particular control requirements. Cases of leases, management contracts, and franchises with equity participations are examples of enhanced commitments and higher asset specificity in the transaction.

Under the lease and the management control options, hotel chains are the agents while hotel owners' are the principal. According to both the AT and TCT this also sets for particular control requirements. In the lease option, rent is pivotal, as its nature determines the tool controlling the relationship. Similarly, in the management contract, management fees and fees' structure as well as budgeting and spending limitations are key control means.

Finally, in a franchise agreement, the situation is reversed. In this case, the hotel chain is the principal that will control for an agent, the franchisee. When franchise is the selected growth option, the initial fee, royalty fees, and advertising and marketing fees are the three main controlling elements.

THEORETICAL DEVELOPMENT

The management of risk and Control relationships in international hotel expansion strategy: a model

Under the encompassing research question involving structure and strategy relationship, four main fields have been examined in this literature review: finance, strategy, organization theory, and decision research.

First, risk has been studied in the fields of finance and strategic management. This first stage revealed a misfit of the finance-based risk definition in a strategic context along with a lack of strategy-specific definition of risk. Drawing from strategic management findings on risk and return, this review suggests that for the understanding of the relationship between risk and return in a strategic context, *the management of risk*, rather than *risk* should be studied. The decisional literature has, then, been explored on the question of the management of risk. Two components emerged from this section of the literature review: the elements of risk and control. Elements of risk represent the managerial conceptualization of risk in their decision-making process. These elements are the *magnitude and the probability of loss*. In other words, works on decision theory reveal that risk is managed based on the assessment of the magnitude of loss in a project and the probability of loss. Furthermore, these elements of risk appear to be intertwined with the concept of control.

The second section of this literature review is, therefore, based on the examination of the concept of control. In this section, areas in the organizational theory examining control have been identified and discussed. More specifically, the agency theory and transaction cost perspective appeared to offer propositions on the determinants of control. Both the AT and TCT relate control to control-related costs. Additionally, both theories focus on two main types of control: the behavior and the performance control. A third type, social control, is often cited thoug, its determinants are still unclear. Control-related costs are proposed to affect the control method practiced in an organization. Particularly, task programmability, information systems, transaction frequency, asset specificity, and outcome uncertainty are revealed as the organizational features defining the control-related costs incurred by an organization. These control-related costs are suggested to predict whether behavior or output control should be put in place.

This work proposes integrating control and the management of risk and to also examine this combination in a key strategic choice--expansion. The rationale behind such a suggestion is further explained. First, the management of risk emerges, from the strategy literature, as essential to the relationship between risk and return. Thus, the management of risk could, reasonably be considered as fundamental in determining a strategy's success. Second, from a strategic perspective, control appears essential to both the strategy-structure relationship and the management of risk. By relying on the management of risk and control as founding constructs, this approach acknowledges the voluntaristic nature of strategy. Consequently, examining the role of control in the management of expansion strategy risks could reasonably enhance our comprehension of the role of structure in strategy.

Within this overarching direction, this effort proposes a model relating the nature of the growth option, organizational control, control-related costs, and their determination of dominant risk elements. More particularly, it is proposed that decision-makers appraise the nature of the growth option against the organizational control in place to assess the sum of costs involved in the expansion. These option costs estimates will determine whether the probability or magnitude of loss will dominate the choice's risk. As discussed in the literature review, decision theory predicts that the dominance of either risk element will, in turn, affect the actual expansion decision and ultimately the strategy's success.

Four overall propositions emerge from the literature review pointing to elements for studying the strategy-structure question through the control construct. These propositions, predict the sum of organizational control-related costs to determine whether the magnitude or probability of loss is the dominant risk element. These constructs and their related propositions are graphically illustrated in Figure 4.

Propositions

P1: Control costs incurred by the transaction result from the interaction of organizational features of the hotel unit with the organizational control of the hotel chain.

P2: The higher the control costs involved in the transaction, the more likely the magnitude of loss will be the dominant element of risk.

P3: Other control costs have a moderating effect on the relationship between control costs of the transaction and the risk elements.

P4: Other control costs will vary with the nature of the growth option adopted (lease, management contract, franchising).

P1: *Control costs incurred by the transaction result from the interaction of organizational features of the hotel unit with the organizational control of the hotel chain.*

This proposition follows from the AT and TCT argument that organizational features (asset specificity, task programmability, information systems, and outcome uncertainty) are determinants of control. Furthermore, this proposition integrates the TCT and AT views that organizational features are determinants of control on the basis of their effect on control costs (either transaction or agency costs). Simply, organizational control is the moderating variable between organizational features and control costs. P1 also integrates the notion that control is managed to reduce costs a common element with the management of risk in expansion strategy.

Four sub-propositions have been derived from this first proposition and are discussed hereafter. Based on the synthesis conducted in the second chapter, four organizational variables determine the level of agency and transaction costs: asset specificity, task programmability, information system-base, and outcome uncertainty. The following sub-propositions are the result of the synthesis of both Eisenhardt's (1985) work and the present integrating effort. They are summarized in Figure 5.

P1.1: *When at least one type of asset specificity is high and behavior control is in place, control costs are likely to be low.*

This is based on the TCT argument that the higher the asset specificity in a transaction, the higher the criticality of the asset for the chain, which leads to the higher the output control (or transaction) costs. Simply, if the contract concerns a highly specific asset, output control costs are likely to outweigh monitoring costs. In essence, a highly specific asset is best handled in a behavior control setting.

As summarized in Table 2, three main types of asset specificity have been derived from the TCT literature and applied to the context: site specificity, physical specificity, and human specificity.

P1.2: *When the degree of task programmability is high and behavior control is in place, control costs are likely to be low*.

This proposition follows the AT and TCT argument that task programmability determines the level of output control costs. More programmability is equivalent to more certainty about the transaction. Similarly, less programmability implies less certainty about the other party's behavior and higher monitoring costs.

P1.3: *When the information system between the principal and the agent is behavior based and behavior control is in place, control costs are likely to be low*.

This is based on the agency argument that each control type (behavior and output) needs to be supported by an information system. If the information system reports performance measures, it is more suitable to outcome control. Similarly, behavior control is more efficient (less costly) if it is supported by a behavior based information system.

P1.4: *The higher the outcome uncertainty in a behavior control organization, the more likely control costs are to remain unaffected*.

AT and TCT suggest that when outcome uncertainty increases, the cost of controlling for that outcome increases (Eisenhardt, 1985). Therefore, if behavior control is in place, and thus monitoring costs incurred, an increase in outcome uncertainty is unlikely to affect control costs. However, if output control is in place and outcome uncertainty increases, control costs are likely to rise.

P2: *The higher the control costs involved in the transaction, the more likely it is that the magnitude of loss will be the dominant element of risk.*

P2': *The lower the control costs involved in the transaction, the more likely it is that the probability of loss will be the dominant element of risk.*

These propositions follow the decision theory argument that one element of risk is likely to dominate in a strategic decision-making setting. The lower the control costs related to a hotel unit, the more likely it is that the likelihood of loss will be the dominant concern. Equally, the higher the control costs related to a new unit, the more likely it is that the amounts involved will be the hotel chain's central concern.

The dominance of either risk element is, in turn, likely to determine the risk-related decision. From a strategic perspective on the risk –return relationship, the risk decision is likely to, in turn, affect firm performance.

P3: *Other control costs have a moderating effect on the relationship between the control costs of the transaction and the risk elements*.

This proposition stresses the view, which is shared by both the AT and TCT, that control efficiency is based on agency and transaction costs management. Building on P1, P2 suggests that the overall control costs related to a hotel unit-hotel chain transaction is composed of control costs as defined in P1 and other control costs.

Two elements in the literature support adding other control-related costs as criterion variables for the above mentioned relationship between the hotel unit organizational features and the elements of risk. First, the theoretical development of both the TCT and AT is based on the determination of either transaction or agency cost reduction. Therefore, not only monitoring and output control costs, but also other control costs related to the transaction should be examined. Second, the decision-theory findings on the management of risk relate control to magnitudes or sums estimates. Thus, all sums or costs estimated for an expansion contract have to be integrated (Figure 5).

According to the TCT perspective, there are ex-ante and post contract costs incurred by a transaction. Similarly, the AT argues that monitoring costs are comprised of a portion of a contract's agency costs. Additionally, with regard to the subject of the management of risk, decision theory suggests that costs other than monitoring costs should be considered. Four main categories of other control costs have emerged from this chapter's integrative literature review: residual loss estimate, information search costs, bargaining costs, and bonding costs. These four costs are referred to as the other control costs and are suggested to have a moderating effect on the relationship between control costs and the elements of risk. The moderating effect of other control costs are summarized in the following sub-propositions:

P3.1: *When the residual losses are high, and control costs are high, the likelihood that the magnitude of loss will be the dominant element of risk will be high.*

P3.2: *When the information search costs are high and control costs are high, the likelihood that the magnitude of loss will be the dominant element of risk will be high.*

P3.3: *When bargaining costs are high and control costs are high, the likelihood that the magnitude of loss will be the dominant element of risk will be high.*

P3.4: *When the bonding costs are high, and control costs are high, the likelihood that the magnitude of loss will be the dominant element of risk will be high.*

P4: *Other control costs will vary with the nature of the growth option adopted (lease, management contract, franchising).*

The presence of one type of other control costs will vary from one growth option to another. In the leases and management contract cases where the hotel chain is the agent, the residual loss estimate is likely to be nonexistent in the hotel chain's estimates of risk. Similarly, the bonding costs are likely to be important elements in the hotel chain's estimates of risk. Oppositely, in the case of franchise agreements where the hotel chain is the principal, residual loss estimates are likely to be an important element in the hotel chain's estimates of risk.

Specifically, the variation will depend on whether the hotel chain is the agent or the principal in the relationship. Both leases and management contracts are growth options where the hotel chain is the agent. Oppositely, under a franchising option, the hotel chain is the principal. The following four propositions are derived from P4 to reflect each situation:

P4.1: *In the case of lease agreement (and management contract),the residual loss estimate is likely to not exist in the hotel chain's estimates of risk.*

P4.2: *In the case of a management contract, the residual loss estimate is likely to have no effect on the magnitude of the loss element of risk.*

P4.3: *The lower the bonding costs in a lease agreement (and management contract), the more likely it is that the probability of loss will be the dominant element of risk.*

P4.4: *The higher the bonding costs in a lease agreement (and management contract), the more likely it is that the magnitude of loss will be the dominant element of risk.*

Figure 4 Summary of constructs

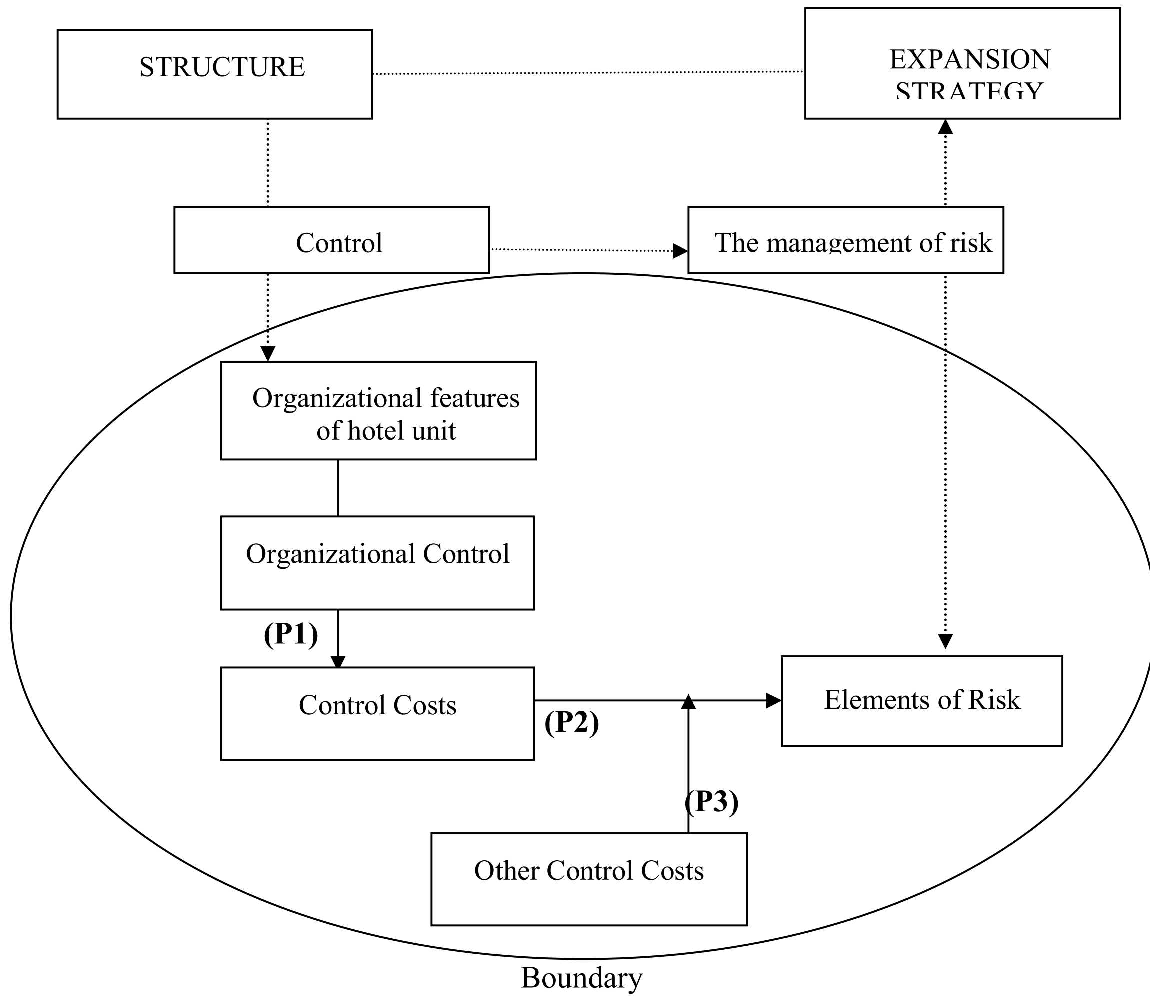
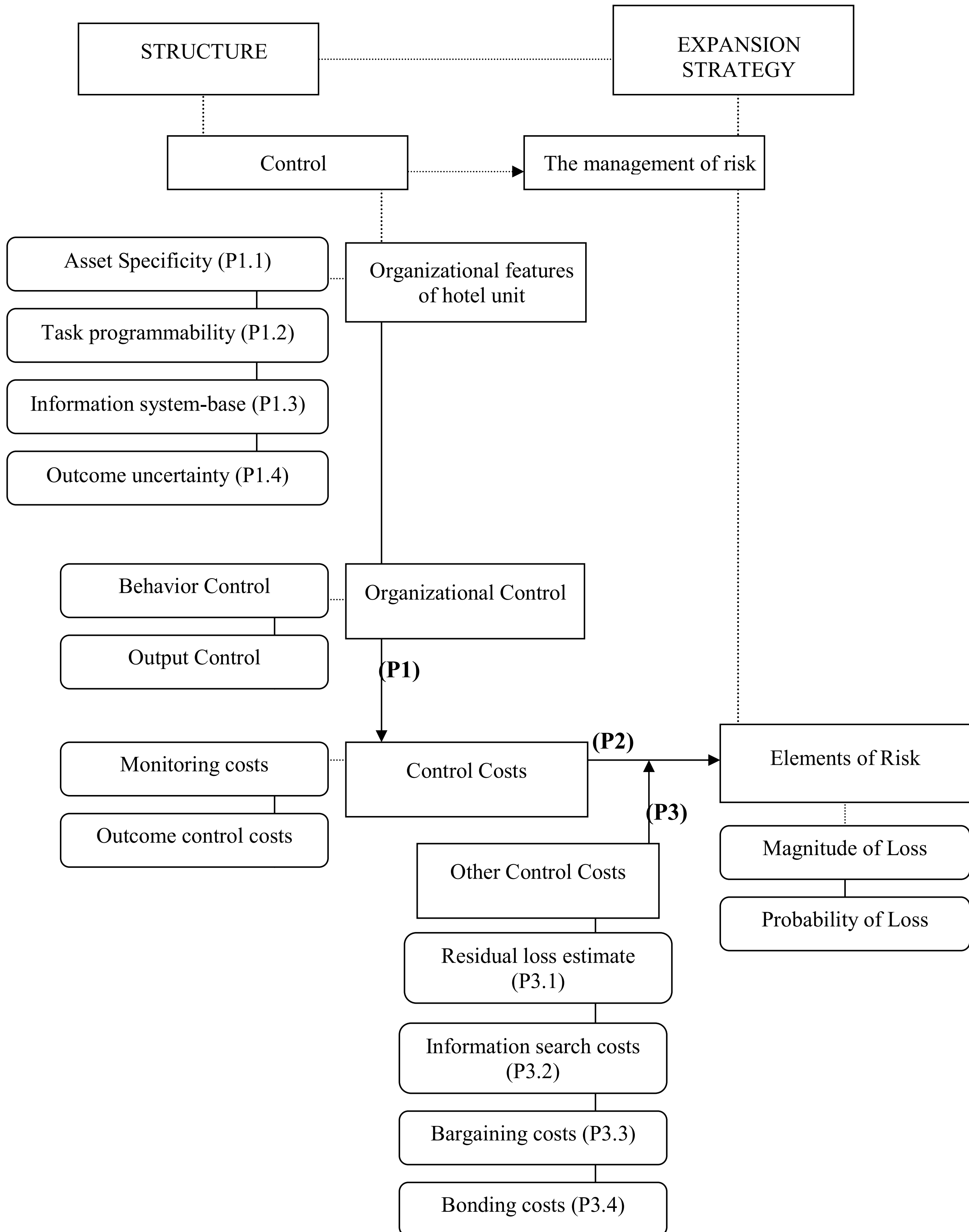


Figure 5 Summary of constructs and Variables



Consequently, the four propositions mentioned earlier put forward a new examination of the strategy-structure relationship through the perspective of control. From this approach, control interacts with the management of risk in expansion strategy. In essence, it is suggested that control criteria based on control-related costs intervene in risk decisions. According to the strategic perspective of the risk-return combination, the intervention in the risk decision is likely to ultimately affect long-term performance.

SUMMARY

This chapter is organized around three main sections. An integrative section where risk and control were examined from three different perspectives composes the first. The second contains a part reviewing the hotel industry expansion context. The third is a synthesis section presenting the theoretical model and its four guiding propositions.

Integrating the financial, strategic, and behavioral fields reveals that the management of risk is related to probabilities and variance but that only the *magnitude and probability of loss* are taken into consideration in *the management of risk* practices. Moreover, this synthesis effort reveals that a strategic approach of risk needs to incorporate nuances such as downside risk and odds control. Finally, the integration of behavioral work to the strategic approach to the management of risk points to the concept of *control* in relation to risk. In essence, this literature review reveals that control bridges the field of strategy and organizational behavior through the notion of the management of risk.

The organization theorists approach to control can be summarized as follow:

- There are two kinds of phenomena that can be controlled for: *the output and the behavior* (OT)
- The determinants of output or behavior control are *asset specificity, task programmability, information systems, and outcome uncertainty* (AT and TCT).
- Control is managed in relation to its inherent costs (AT and TCT). These *control costs* are examined in relation to the phenomena to be controlled for and their coherency with the determinants of control.

Examining the expansion context of the hospitality industry reveals that international hotel chains apply six main growth options when managing their expansion strategy: full ownership, joint venture, lease, rental, franchise, and management contract. In the lease option, rent is a

pivotal as its nature determines the tool controlling the relationship between the hotel chain and hotel owners. Similarly, in the management contract, management fees and fees' structure as well as budgeting and spending limitations, are key control means. When franchise is the selected growth option, the initial fee, royalty fees, and advertising and marketing fees are the three main controlling elements. Finally, based on the TCT assumptions, ownership and joint ventures are mere examples of transactions where commitment is increased to modify the control requirements.

The purpose of this study is to explore the relationship between expansion strategy and structure in the hotel industry from the perspective of control. From a control perspective, expansion's strategic management is related to the management of control costs, which in turn, affect the management of risk in expansions. These relationships are detailed in Table 3 and synthesized the four main propositions.

Table 3 Summary of Research Propositions

Risk elements	Control Variables	Control costs	Working Relationships
Probability of loss			• The lower the control costs involved in the transaction, the more likely the probability of loss will be the dominant element of risk.
	Degree of asset specificity: • Degree of site specificity • Degree of physical specificity • Degree of human specificity	Monitoring costs vs. output control costs	• When at least one type of asset specificity is high and behavior control is in place, control costs are likely to be low.
	Degree of task programmability:	Monitoring costs vs. output control costs	• When the degree of task programmability is high and behavior control in place, control costs are likely to be low.
	Information system base: • Behavior base • Output base	Monitoring costs vs. output control costs	• When the information system between the principal and the agent is behavior based and behavior control is in place, control costs are likely to be low.
	Degree of outcome uncertainty	Monitoring costs vs. output control costs	• The higher the outcome uncertainty in a behavior control organization, the more likely control costs to remain unaffected.
		Other control costs: • Residual loss estimate • Information search costs • Bargaining costs • Bonding costs	• The lower the other control costs, the more likely probability of loss to be become the dominant element of risk.
Magnitude of loss			• The higher the control costs involved in the transaction, the more likely the magnitude of loss will be the dominant element of risk.
	Degree of asset specificity: • Degree of site specificity • Degree of physical specificity • Degree of human specificity	Monitoring costs vs. output control costs	• When at least one type of asset specificity is high and output control is in place, control costs are likely to be high

Risk elements	**Control Variables**	**Control costs**	**Working Relationships**
Magnitude of loss	Degree of task programmability:	Monitoring costs vs. output control costs	• When the degree of task programmability is high and output control in place, control costs are likely to be high
	Information system base: • Behavior base • Output base	Monitoring costs vs. output control costs	• When the information system between the principal and the agent is output based and behavior control is in place, control costs are likely to be high
	Degree of outcome uncertainty	Monitoring costs vs. output control costs	• The higher outcome uncertainty in an outcome control organization, the more likely control costs will increase
		Other control costs: • Residual loss estimate • Information search costs • Bargaining costs • Bonding costs	• The higher the other control costs, the more likely the probability of loss will be reduced and the magnitude of loss will become the dominant element of risk.

CHAPTER 3: METHODOLOGY

INTRODUCTION

The structure of this section is derived from Yin's (2002) work on case study research and adapted to the investigation on hand. Specifically, this chapter applies the four founding elements for case study research as described by Yin (2002). In the first section, conditions of the research method selection are evaluated against present research questions. This assessment provides support for the choice of the case study approach as the research method for this study. Second, the research steps are specified. In particular, the details of the panel of experts, the pilot case study, and the interviews are presented in the second section of this chapter. Third, Yin's directives for the case studies design are reviewed and applied to the present effort. Fourth, the development of the test instruments is delineated. In this step, applicable sources of evidence are listed, and the data collection method is detailed. Finally, the protocol employed for data management and method analysis is explained.

RESEARCH METHOD: CASE STUDY REQUIREMENTS

The objective of this first section is to assess the selected research method against the inquiry on hand. According to Yin (2002), the determinants of research method selection are as follows: the type of research question, the control of behavioral events requirements, and the research question degree of focus on contemporary events. In order to confirm that a case study is indeed the research method corresponding to the research question on hand, the research questions are detailed and assessed against Yin's three conditions for research method selection.

Research Questions

In an effort to enhance our comprehension of the strategy-structure relationship in strategic management, this work explores the relationships between the management of risk and organizational aspects in expansion strategy. Particularly, this work proposes control as a structural dimension linking the management of risk and strategy. Therefore, this effort's purpose is to explore the role of control in the management of risk in expansion strategy. In particular, this research addresses the following questions:

- Is control a structural variable in the management of expansion strategy?
- How does control intervene in the management of risk in expansion strategy?
- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion context?
- What is the role of control costs in the management of risk for expansion strategy?
- How do the features of the hotel unit affect the management of risk in expansion strategy?

The fundamentals of research designs and methodology are that the research question drives the research strategy. In this work, the research questions are exploratory and focus on examining the interaction of structure with strategy in the hospitality industry international context. In other words, the research questions are of the "what" and "how" variety (Yin, 2002; Whetten, 1989). In order to examine the structure and strategy interaction phenomena, there is no need for control of behavioral control in the experimentation process. To the contrary, the management of risk and its interaction with control is a phenomenon that only occurs in a contextual setting.

To summarize, the present research is of an exploratory type and, as a result, does not require behavior of control and, most importantly examines a contextual phenomenon. The, before mentioned, three conditions predetermine the need for case study as the research method. The existence of these intrinsic conditions supports conducting a case study as the data collection method.

RESEARCH STEPS

For this study, three main research steps were undertaken: the panel of experts, the pilot case study, and the three actual case studies. These steps were applied, essentially, to maintain the construct validity of the research. First, a list of interview questions was developed and presented for assessment to experts in the field of hotel development. Next, both the interview content and procedure were tested in a pilot case study. Finally, a final list of questions was determined and used to interview hotel development managers.

Panel of experts

The purpose of this first step was to verify the construct validity of the contextual measures. These measures have been inferred from the literature review and developed by the researcher. In order to strengthen the construct validity of the developed measures, the questions were submitted to a panel of experts.

- *Participants*

Twelve experts were contacted for this step. Six provided complete answers to the panel questions and one person has provided an overall comment. Out of the six persons participating in this electronic panel, three were academics and three were practitioners. All of the six persons were specialized in development aspect of the hotel industry. Profiles of these seven participants are listed in Table 4. All three academics had a strong record in research and teaching in the field of hotel development. The expertise of two participants was in financing hotel development. One participant's area of expertise was related to a specific segment of the industry (budget hotels). Finally, one participant had an expertise in economics and its applications to the hotel industry. Two of the three practitioners were heads of development in a hotel chain. The first hotel chain was publicly traded and the development efforts were worldwide. The second was a smaller private hotel chain, whose activity was mainly European. Finally, the third practitioner represented the architecture and infrastructure design aspect of the development activity.

Table 4 Panel of experts: Profiles

Academics	
Expert # 1	PhD; teaching and research in hotel development, financing and asset management
Expert # 2	Teaching and research fields are economics and hotel development
Expert # 3	PhD; research focus on the ownership reform of the hotel industry in China and investment of budget hotels
Expert # 4	Teaching and research fields are finance and real estate management in the hotel industry
Practitioners	
Expert # 5	Director of development of a large publicly traded international hotel chain
Expert # 6	Development manager of a private European hotel chain
Expert # 7	Chairman of an international design-consulting firm. Specializes in architecture, resort design and development

- *Procedure*

The panel of expert was conducted electronically. Each expert received an Excel file with a list of questions to validate (screenshots of the documents are provided in Appendix B). The document contained ten sub-sections corresponding to the ten constructs under examination (i.e.: Asset specificity, site specificity, physical asset specificity, human asset specificity, task programmability, information-base systems, control-related costs, outcome uncertainty, other control costs, and risk elements). Within each of the ten sections, the questions developed by the researcher beforehand were presented for rating. The experts were asked to rate how favorable he or she was with using this question to examine construct X. For instance, the six questions that were created for asset specificity was listed under construct A. Beneath each question, the expert had to select his or her answer from a multiple choice list. In this case, the expert was asked: "How favorable are you with using this question to examine construct A?" The expert could then choose from a multiple-choice list with the following five possible answers: strongly favorable, somewhat favorable, undecided, somewhat unfavorable, and strongly unfavorable.

Once the Excel sheet was returned to the researcher, the answers were coded. As follow:

+2 Strongly favorable
+1 Somewhat favorable
u Undecided
-1 Somewhat unfavorable
-2 Strongly unfavorable

For each question, a total score was computed. This step allowed determining which questions were strongly supported by the panel from those that were not.

Once this first stage completed, it appeared that one expert presented very different answers. Therefore, he was contacted for an in-depth discussion of his results. The purpose of this step was to ensure that the issues of construct validity related to the questions were fully understood by the researcher. Finally, the selection of the final questions to include in the interview was conducted on a construct-by construct basis.

- *Results*

Table 5 contains the scored results for each question. The questions that are crossed in the table are those that were eliminated after the examination of the results of the panel of experts. The elimination decision was a result of both the score and the comments provided by the experts in their answers.

Question 1 is the first question that was eliminated. There were two reasons for this elimination: the question had one of the lowest score in this set and the experts commented on the vagueness and sensitivity of this question. Indeed, the experts suggested that the reasons for signing a contract in the hotel development vary, are mainly related to financial incentives, and are opportunity-driven. They suspect that the development team would be uncomfortable with this question.

Table 5 Panel of experts: Results

Construct A. Asset specificity	***Definition:* Asset specificity refers to the degree of uniqueness of an asset to a contract. In other words, an asset that is highly specific to a contract is difficult to transfer or use in another contract.**								
	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
~~**Question 1:** What were the reasons for signing with this particular hotel unit?~~	-2	2	2	2	2	1	-2	1	**3**
Question 2a: Would you say that the profile of the hotel unit is consistent with the one of the hotel chain?	2	1	2	5	1	1	2	4	**9**
Question 2b: If yes, in what regard?	2	1	2	5	2	-1	2	3	**8**
Question 3: Is the level of your pre-opening commitment (both in terms of efforts and money) comparable to other contracts you have signed lately?	1	1	1	3	2	1	1	4	**7**
Question 4a: Did you need to make special arrangements (i.e.: addition of special clauses to the standard contract, increase in financial participation) or spend more time for this particular hotel unit?	-2	2	1	1	1	2	1	4	**5**
~~**Question 4b:** If yes, what were these arrangements?~~	-2	2	1	1	1	1	-1	1	**2**

Construct B. Site Specificity	***Definition:* Site specificity is when the location of the hotel unit provides an advantage to the hotel chain.**								
	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 5a: Is the hotel location interesting for your hotel chain?	-2	2	1	1	2	1		3	**4**
Question 5b: If yes, in what regard?	2	1	1	4	2	1	2	5	**9**
~~**Question 6:** Would there be any cost reduction advantages gained with this new unit?~~		2	1	3	1	1	1	3	**6**

Construct C. Physical asset specificity	***Definition:* Level of investment made by one of the parties in a contract that involves construction and tangible alteration. Modifying the architecture of a hotel unit to adhere to the requirements of the hotel chain increases the physical specificity of the hotel unit to the contract.**								
	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 7a: Would you say that this hotel's general infrastructure (architecture, design, furniture and equipment) required further investment before its opening under your banner	2	1	0	3	2	2	-1	3	**6**
Question 7b: What is (was) your approximate estimate of this investment?	2	1	0	3	2		-1	1	**4**

Question	#1	#2	#3	Total 1	#4	#5	#6	Total 2	TOTAL
Question 8a: Would you say that this hotel required further investment in operation and marketing activities before its opening under your banner?	2	1	1	4	1	1	0	2	**6**
~~**Question 8b:** What's your estimate of this investment?~~	2	1	1	4	1	2	0		**4**

Construct D. ***Human asset specificity***	***Definition**: The level of investment in the human resources which are specific to the contract.*

	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 9a: Who are the persons involved in the project?	1	1	-1	1	0	-1	2	1	**2**
Question 9b: How many other projects are (or were) these persons working on?	1	1	-1	1	0	0	2	2	**3**
Question 10: What is the role of these persons in the project?	1	2	-1	2	0	1	2	3	**5**
Question 11a: Did the contract require particular investment in human resources?	1	2	-1	2	2	0	2	4	**6**
Question 11b: If yes, what was this investment?	1	2	-1	2	2	1	0	3	**5**

CONSTRUCT E. ***Task Programmability***	***Definition:** Task programmability refers to the capacity to plan for the details of a contract. When the components of a contract and their measures are determined, the contract is considered to present a high level of programmability.*

	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 12: Could you please, briefly describe your obligations to the hotel unit representative?	1	2	-2	1	1	1	-1	1	**2**
Question 13: Could you please, briefly describe the obligations of the hotel unit representative?	1	2	-2	1	1	1	-1	1	**2**
Question 14: Which obligation of the hotel unit representative is the most important to the success of the contract?	2	2	-2	2	2	1	1	4	**6**
Question 15a: Is it your first contract with the other party?	1	1	1	3	1	1	2	4	**7**
Question 15b: If no, what other contracts have involved the other party?	1	1	1	3	1	1	1	3	**6**
~~**Question 16:** Do you consider these past transactions successful?~~	1	2	0	3	1	0	2	3	**6**
Question 17: Is it your first investment in the hotel's area?	1	2	1	4	1	1	2	4	**8**
Question 18: What information were you looking for prior to the signature?	2	2	-2	2	2	2		4	**6**

CONSTRUCT F. Information-base systems	***Definition**: The information system is the set of communication procedures in place in the transaction. In this research context, the system is based on information related to either behavior or performance.*

-	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 19a: How often does the representative of the hotel unit visit the hotel?	2	2	-2	2	0	-1	2	1	**3**
Question 19b: What's the purpose of these visits?	2	2	-2	2	1	-1	2	2	**4**
Question 20: What information does the representative of the hotel unit use in the assessment of your compensation?	2	1	-2	1	2	1	2	5	**6**
Question 21a: What information are you required to transmit to the representative of the hotel unit?	2	2	-2	2	2	1	2	5	**7**
Question 21b: What other information is exchanged?	2	2	-2	2	1	1	1	3	**5**
Question 21c: By what means?	2	1	-2	1	0	1	2	3	**4**
Question 22: What targets do you need to meet for your compensation?	2	2	-1	3	2	2	0	4	**7**
Question 23a: How often do you visit the hotel unit?	2	1	-1	2	1	-1	2	2	**4**
Question 23b: What's the purpose of these visits?	2	2	-1	3	2	-1	2	3	**6**
Question 24: How do you distinguish a "good" hotel unit performance from a "bad" performance?	2	0	-2	0	2	1	2	5	**5**
Question 25a: What information is the hotel representative required to transmit to you?	2	2	-1	3	2	1	2	5	**8**
Question 25b: What other information is exchanged?	2	2	-1	3	1	1	2	4	**7**
Question 25c: By what means?	2	1	-2	1	0	1	2	3	**4**
Question 26a: Do you impose targets or standards on the hotel representative?	2	2	2	6	2	1	2	5	**11**
Question 26b: If yes, what are these targets?	2	2		4	2	1	0	3	**7**

CONSTRUCT G. Control-Related Cost	***Definition**: Control-related costs are expenses incurred by the party of a contract who is delegating a task to another party. These costs are paid by the delegating party to control for either the behavior (process) or the performance (output) of the other party*

	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 27a: Do you have a reporting system in place?	-2	2	-2	-2	2	1	2	5	**3**
Question 27b: If yes, what are the system's outputs?	1	2	2	5	2	1	2	5	**10**
Question 28a: When was the system put in place?	0	1	-1	0	2	1	2	5	**5**

Question	#1	#2	#3	Total 1	#4	#5	#6	Total 2	TOTAL
Question 28b: Were there further investments made in the system since its origination?	0	2	-1	1	2	-2	2	2	**3**
Question 28c: Are there any further investments planned in the reporting system?	1	2	-1	2	2	-1	1	2	**4**
Question 29a: Who is in charge of monitoring the unit's activity?	1	1	-1	1		1	2	3	**4**
~~**Question 29b: What is the person(s) salary(ies)?**~~	-2	0	-2	-4	1	-1	-2	-2	**-6**
Question 30: Did the chain invest in systems supporting this person's activity (Information Systems and Reporting Systems)?	1	1	1	3	1	1	1	3	**6**
Question 31a: How many times, in a year, do you meet with the hotel unit representative?	-2	2	-1	-1	1	1	2	4	**3**
~~**Question 31b: How long do these meetings last?**~~	-2	0	-2	-4	-1	-1	2	0	**-4**

CONSTRUCT H. ***Outcome uncertainty***	***Definition**: Outcome uncertainty corresponds to the unanticipated changes in circumstances surrounding a contract. The purpose of this section is to assess the level of outcome uncertainty within a particular contract.*								
	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 32: Would you say that the project's overall estimates are accurate within what % of accuracy (ie: ±10%)?	2	2	1	5	2	1	1	4	**9**
Question 33: How would you rate the political stability of the hotel location on a 1-5 scale, where 1= very unstable and 5= very stable?	2	2	1	5	2	1	2	5	**10**
Question 34: How would you rate the quality of goods & services available in the location on a 1-5 scale, where 1= very poor and 5= very good?	2	2	-1	3	2	1	2	5	**8**
Question 35: How would you rate the level of taxation in the unit's location on a 1-5 scale, where 1= very low, 5= very high?	2	2	1	5	2	-1	2	3	**8**
Question 36: Would you say that the project's sales estimates are accurate within what % of accuracy (ie: ±10%)?	-2	2	2	2	2	1	2	5	**7**
Question 37: How would you rate the stability of the hotel location's local currency on a 1-5 scale, where 1= very unstable and 5= very stable?	2	2	2	6	2	2	2	6	**12**
Question 38: Would you say that the project's cost estimates are accurate within what % of accuracy (ie:	2	1	1	4		1	2	3	**7**

±10%)?									
Question 39a: How would you describe the infrastructure in the local destination?	2	2	2	6	2	1	2	5	**11**
Question 39b: Is this infrastructure sufficient for the support of your chain's goods and services standards?	2	2	2	6	2	0	2	4	**10**
Question 40: How confident are you about the other party's successful contribution to the contract? (1. Very confident, 2. confident, 3. somehow confident, 4. Somehow unconfident, 5. Unconfident, 6. Very unconfident)	2	2	-1	3	2	1	2	5	**8**
Question 41: Are you concerned about the possibility for the hotel unit representative to misuse your name for his/her own benefit at your disadvantage?	2	1	-1	2	0	-1	2	1	**1**

CONSTRUCT I. Other Control Costs	***Definition**: All other expenses incurred by the parties involved in a transaction to ensure the convergence of their actions and interests. These costs include pre-payments or other proofs of commitment, expenses for information search, and bargaining cost*								
-	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 42a: Was an opportunity cost estimated by your financial team?	1	2	2	5	2	1	0	3	**8**
Question 42b: If yes, what was the amount?	0	2	1	3	2	-1	-1	0	**3**
Question 42c: If yes, what assumptions were used for this specific estimate?	1	2	1	4	2	-1	0	1	**5**
Question 43: Could you please, describe the process that your chain has been through until the final signature with the other party?	1		0	1	1	1	1	3	**4**
~~**Question 44a:** How many persons were involved in the implementation of the project~~?	-2	1	-2	-3	0	-1	1	0	**-3**
Question 44b: How many times did they travel to the location?	-2	1	-2	-3	0	1	1	2	**-1**
Question 45: How long did the negotiation process last (from first contract daft to final signature)?	2	2	-2	2	0	1	1	2	**4**
~~**Question 46:** How many persons worked on creating the final contract?~~	-2	1	-2	-3	0	-1	1	0	**-3**
Question 47: How many revisions to the contract were made?	0	2	-2	0	1	1	2	4	**4**
Question 48: What clauses were conceded?	-2	2	2	2	2	-1	-1	0	**2**

CONSTRUCT J. ***Risk Elements***	***Definition**: When making a decision, managers assess two elements of risk: the probability of the loss and the magnitude of the loss.* • ***Probability of the loss: is the estimate of the threat of a very poor outcome*** • ***The magnitude of the loss: is the estimate of the amount of money that could possibly be lost in the decision***

	#1	#2	#3	Total 1	#4	#5	#6	Total 2	**TOTAL**
Question 49: What are the chances for this new contract to be successful (on a 0-10 scale: 0 being no chance; and 10 very certain that this deal will be successful)?	2	0	0	2	2	0	1	3	**5**
Question 50: If the deal was to be cancelled, what would be your estimate of the loss involved?	2	2	1	5	2	1	-1	2	**7**
~~**Question 51a:** Overall, what's your estimate of the deal?~~	-2		-2	-4	1	1	1	3	**-1**
Question 51b: What is the deal worth to your company?	1	1	1	3	2	1	-1	2	**5**

Question 4.b was also eliminated for its very low score. It was suggested that it was redundant with question 4.a.

Questions 5a and 5b were merged as a result of the panel of experts. Indeed, Question 5b scored very high (a total of 9, with no negative score). Therefore, question 5 a and 5b were merged in one question: "In what regard is the hotel location interesting for your hotel chain?"

Question 6 was excluded from the final list of interview questions. However, since it presents the support of the experts, it was integrated as a direction for expansion in the interview process. This direction in the interview procedure was put in place to ensure the maintenance of chain of evidence (Yin, 2002). In other words, next to question 5, a note on expansion was mentioned for the interviewer.

Question 8 b. was eliminated from the list of questions. Its low score and the comments of the panel showed that this question is redundant with question 7 b.

Questions 11a and 11b merged into one open-ended question. It is important to mention that the relatively low scores of the construct of human asset specificity were not related to the lack of construct validity. Rather, the low rating on this construct was due to the fact that the experts believed that the question of human resources was less relevant to the development business than the others are.

Questions 19a and 19b were maintained despite their low score. The reason for that is that these questions were derived from the literature on control. Indeed, these questions were predominant in research related to control. Since the research questions were built around the construct of control, it seems necessary to maintain any question that permitted to observe and estimate variables related to control.

Question 29b. was eliminated for its very low score. Additionally, the convergence of the opinion of the six experts on that specific point supported the decision for eliminating the question. Similarly, the same reasons supported the elimination of questions 31b. The high scores of the questions related to construct H of outcome uncertainty seemed to indicate that question of outcome uncertainty is essential in hotel development activities. This note has been considered during later stages of data collection and analysis. Question 41 has a low score in comparison to the rest of the questions related to construct H. Nevertheless, it was maintained in the interview question list. Question 41 was inspired from the literature on franchising where it is very often employed. Thus it was suspected that the low score on this question was not related to its lack of

construct validity but rather to its contextual aspect. This point was confirmed during the in-depth interview with one of the experts.

Questions 44a and 46 were eliminated for their redundancy with Question 9a. Indeed, it did appear in the analysis that these questions were redundant with question 9a and that they could be covered under the construct of Human Asset specificity.

Finally Question 51a was judged too sensitive by the panel of experts. Therefore it was eliminated from the interview questions.

Once this step of the data collection completed, a final list of interview question and an interview procedure was put together. (The document that resulted from this procedure is presented in Appendix C).

Pilot case study

Prior to the three actual case studies, a pilot test was conducted. As suggested by Yin (2002), the purpose of the pilot was to test and refine the interview procedure and its content. The pilot also served to test the collection and data management method selected. The process allowed a minor refinement of the wording and comprehensibility of the questions. Additionally, specific attention was given to the accuracy of the link between the propositions and the data collected. Upon completion of the pilot study, the final list of interview questions was determined. This list is reviewed in the following section.

Since the refinements made after the pilot were minor, the results from the pilot were integrated in the final results of this study.

Interviews

This step in the data collection was the most important in this research. Focused and semi-structured interviews were conducted. Representative from the development departments in the selected hotel chains were interviewed in a one hour to one hour and a half semi-structured setting regarding all variables (Please refer to Appendix C for the entire questionnaire). These interviews were conducted over the phone. Each interview was taped and transcribed after hand.

Initial emails were exchanged between the researcher and the potential interviewees. The purpose of the research was explained at this stage and arrangements were made to conduct the interviews. Data were collected over a four-month period. Each interview opened with an explanation of the research and an assurance of confidentiality. The confidentiality aspect was sensitive in this research as development managers were often careful about the information they were sharing with this regard.

The interviews were composed of three parts. First, the interviewee was asked a general question about her role within the company[1]. Second, the researcher asked about the expansion plans of the hotel chain[2]. Third, the interview procedure was explained. The procedure consisted of asking the respondent about the last contracts they have signed. Next, these contracts were contrasted all through the interview questions. The full interview procedure is available in Appendix C.

The series of developed interview questions is presented in the next section. In order to maintain the linkage between the propositions and the data, several questions were annotated with leads for the interviewer. These comments on elements to expand on were developed to support the chain of evidence that was developed during the design stage (Yin, 2004). Simply, below several questions, the interviewer was reminded about the contextual measures and constructs she was investigating. This process was put in place during the design stage and refined during the pilot test.

CASE STUDY: THE DESIGN

This research is a theory-driven exploratory effort. Four initial propositions were put forward from the literature review to answer the question of how structure relates to expansion strategy. Essentially, these four propositions explained how, from a literature perspective, organizational control features and the management of risk relate when firms follow an expansion strategy.

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[1] Could you briefly describe your role (responsibilities and duties) within the company?
[2] What are your targets in terms of expansion? Which type of contract do you sign to meet your development plans?

Propositions

P1: Control costs incurred by the transaction result from the interaction of organizational features of the hotel unit with the organizational control of the hotel chain.

P2: The higher the control costs involved in the transaction, the more likely the magnitude of loss will be the dominant element of risk.

P3: Other control costs have a moderating effect on the relationship between control costs of the transaction and the risk elements.

P4: Other control costs will vary with the nature of the growth option adopted (lease, management contract, franchising).

Unit of analysis

The unit of analysis refers to the type of object whose variable characteristic is of interest in the scientific process. It refers to the type of unit a researcher uses when measuring (Neuman, 2003), and thus, determines how the researcher measures variables. In this case, the type of object whose variable characteristic is of interest is the *transaction between the hotel chain and the hotel unit selected as a strategic growth option*.

Consequently the proposed relationships are not supposed to hold outside transactions other than those relating a hotel chain and a hotel unit introduced in the network for expansion purposes. The generalization and replication of the present work should consider this analytic limitation.

Data and propositions: Relationship

This section explains the process relied upon to relate the measures with the constructs of interest. Due to the exploratory nature of this research and the lack of contextual measures for the examined constructs, a particular approach was undertaken. This approach consisted of three main steps:

- ✓ First, existing measures in previous research were examined. The purpose of this first step was to determine the variables that could apply to the present research. For this purpose, each construct, and its related variable(s), were listed in the first two columns of Table 6. Then, the measures that had previously been used in research were summarized in the third

column of this same table. This procedure allowed the comprehension of the dimensions of each construct and their relationship with their related contextual measures.

✓ In parallel, possible operationalizations for the context of the hospitality industry expansion strategy were presented in Table 7.

✓ Finally, the results of these two steps were contrasted and the resulting contextual measures were listed in Table 7. For each contextual measure, a data collection method was suggested in the last column of the same table.

Table 6 Review of empirical measures used in research3

Variable/Construct[4]	Dimensions	Measure(s) used
Asset Specificity	Site specificity	• Physical proximity between contracting parties • Idiosyncratic investments • Product complexity • Inter-firm co-specialization • Spatial or temporal proximity
	Human capital specificity	Commitment for the specific relationship • Specificity of working relationship between a salesperson and her organization • Specificity of the wife to the household and the use of prenuptial contracts • Specificity of individual rock and band members to critic's assessments of music quality
	Physical Assets	• Developing automotive components for a vehicle assembler
Task programmability	Description of task involved	• Proportion of selling task in sales job • Categories of services offered to customers • Categories of customer efforts • Time spent by each selling person with customer • Length of training period
Information-system base	Behavior measurement	• Personal observation of the agent's work • Formal quantitative behavior measures: comparison of budget • Behavior rewards: pay plans in which pay is salary or hourly rate
	Performance measurement	Objective measures of results (rather than methods used to achieve results) • Salespersons' commissions • Performance reporting systems
Organizational control	Behavior	• Behavior-based reward structures • Assignment of parent company managers to key

[3] These measures are derived from Boerner and Macher's (2002) literature review
[4] This column contains both constructs and variables. Subsequent tables extracted from Table 7 better refine this generic labeling.

Variable/Construct	Dimensions	Measure(s) used
		management positions of the foreign subsidiary: number of top five jobs in the subsidiary that are held by nationals from the country where headquarters is located
	Outcome	• Outcome-based reward structures • Frequency with which various types of financial, manufacturing, and marketing information were received by the head office from the subsidiary (weekly, monthly quarterly, annually)
Variable/Construct	**Dimensions**	**Measure(s) used**
Control-related costs	Monitoring costs Outcome control costs	The cost of observation: depends upon the cost of the measurement system. Size is an important factor in the determination of administration burden • Number of stores in the store chain & dichotomous ownership variable (private vs. public corporation)
Outcome Uncertainty	Industry uncertainty Outcome distribution	• Number of competitors • Demand uncertainty • Technological uncertainty • Supplier uncertainty • Failure rate per time period • Volatility
The elements of risk	Probability of loss	• Probability of loss with the introduction of new product(s): brand likelihood of failure (1- stated likelihood of success)
	Magnitude of loss	• Capital requirement: Capital required to build the production capacity needed to produce the chosen new product(s)

There are two overarching constructs in this research: control and management of risk. The construct of control is, in turn, composed of three main sub-constructs namely, organizational features, organizational control, control costs, and other control costs. As for the management of risk it is essentially composed of the sub-construct of the elements of risk. Figure 6 presents the relationship between the two overarching constructs and the sub-constructs.

The following section presents the interview questions used to observe these constructs and sub-constructs.

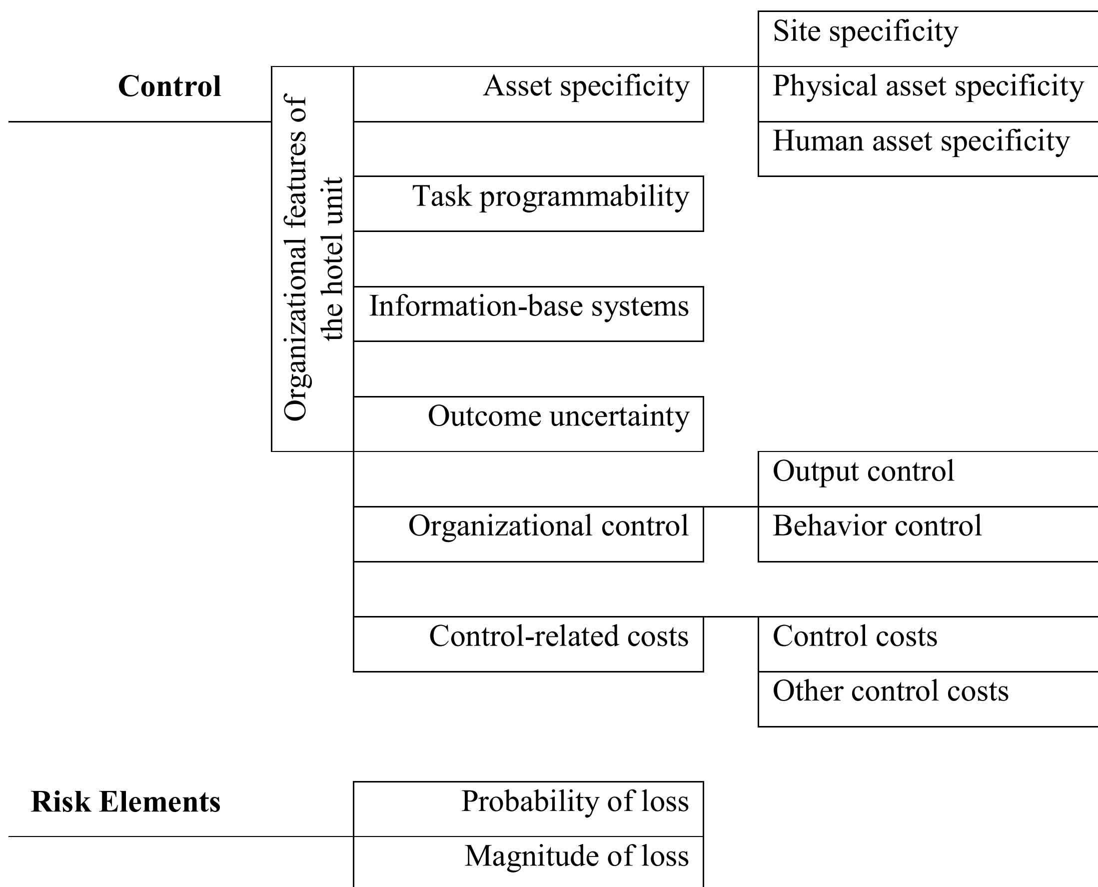


Figure 6 The constructs and their relationship.

- *The construct of Control*

The first part of the model (Figures 5 and 6) is related to the overarching construct of control. As determined in the literature review, the construct of control is revealed in three aspects when approached from the structural perspective: the organizational features, the organizational control, and the control costs. Each one of these three aspects of control was suggested to play a role in the management of risk in expansion strategy.

The first dimension of control appears in the organizational feature of the hotel unit. Four organizational features were revealed as important and considered as determinants of control (Figure 5):

Asset specificity,
Task programmability,
Information-system base, and
Outcome uncertainty.

- *The organizational feature of the hotel unit*

1. Asset Specificity

Asset specificity has been predominantly examined in terms of human capital specificity or site specificity (Table 6). In either case, the focus of the examination was on the impact of these structural determinants on the costs of doing business (Boerner and Macher, 2002). Previous efforts revealed that these determinants vary from a transaction type to another and thus, are highly contextual (Table 6). For instance, the geographical distance, or the physical proximity, between contracting parties, measured site specificity. Similarly, spatial or temporal proximity groups measured the geographical and temporal dimensions of site specificity.

Human specificity has also been measured in different settings ranging from salespersons and their organizations, wives and their household, rock members and music quality. In every case, the measures attempted to reflect the specialization or specificity of key human resources in a transaction. Transaction theorists suggest that a high level of investments for a specific transaction is an indication for asset specificity. Two following questions are suggested to determine the contextual measure(s): *Would this investment have been made in another transaction; and what use can the asset have outside of the examined transaction*?

There are no measures, to date, for asset specificity in the hotel industry. Therefore, measures have been developed for each of its aspect. Prior to the data collection process, it was suspected that a contextual research in the hotel industry should include further nuances for the site specificity aspect of transactions (Zhao, 1994; Zhao and Olsen, 1997). Indeed, in the context of the hotel industry, asset specificity cannot be limited to just the distance between the hotel chain's headquarters and the hotel unit, but should instead take into account the centrality of location for the hotel business. Simply put, site specificity is pivotal in the hotel industry, as it not only affects costs but also revenues. This fundamental aspect of the hotel business had to be reflected in this measure. Similarly, human capital specificity also needed to be researched along the physical asset specificity. The site specificity variable had to include aspects of the locational advantage (Zhao, 1994; Zhao and Olsen, 1997) sought by the hotel chain when investing in a specific hotel unit. Particularly the consistency of the hotel unit's profile with the hotel chain offer had to be considered. Similarly, the physical asset dimension had to be examined in the context and include infrastructure investments in the hotel unit made for its introduction into the chain. These findings in the literature were also confirmed by the results from the panel of experts.

Asset specificity represents the incremental benefits gained from the transaction as opposed to without the transaction. In essence, an asset that is highly specific to a contract is difficult to transfer or use in another contract. In this study, it is defined as the degree of uniqueness of an asset to a contract. In the context of hotel chains, site specificity is when the location of the hotel unit provides an advantage to the hotel chain. Physical specificity is related to the hotel infrastructure (Roberts and Shea, 1996) and its related investments. In this research, it is defined as the level of investment made by one of the parties in a contract that involves construction and tangible alteration. Modifying the architecture of a hotel unit to adhere to the requirements of the hotel chain increases the physical specificity of an asset. As for human specificity, it refers to the level of investment in human resources that are specific to the contract.

The third column of Table 7 lists suggested contextual measures for each dimension of asset specificity. These measures were then transformed into the following interview questions.

Site specificity:

Question 1. In what regard was the profile of the hotel unit consistent with the portfolio of the hotel chain? (*Expand on the degree of asset specificity*)

Question 2. Do your pre-opening commitments (both in terms of efforts and money), across the different contract types?

Question 3. Did you need to make special arrangements (i.e.: modification of the chain standard requirements, increase in financial participation) or spend more time for this particular hotel unit? (*Expand on contract length and renewal options*.)

Physical asset specificity:

Question 4. Can you please tell me the key criteria you relied upon in choosing the location?

Question 5. Did you invest in the hotel's general infrastructure (architecture, design, furniture and equipment) before its opening under your banner? (*Expand on the level of the investment).*

Question 6. Did you invest in operation and marketing activities before the opening of the hotel under your banner? (*Expand on the level of the investment).*

Human Asset specificity:

Now, I would like to ask you about the mobilization of the human resources capabilities:

Question 7. First**,** how important is the human resource capability (at the corporate level) in the decision to sign?

Question 8. Did the contract require particular investment in HR? (*Expand on the level and details of investment.)*

Question 9. What is the role of the persons involved in the project?

2. Task programmability

Task programmability is determined by both the nature and description of the task involved in the transaction. In previous research the construct has been observed through agency relationship between a company and its salespersons (Table 6). In this specific case, the measures of task programmability are based on the proportion of selling tasks in the sales job. This proportion has been derived from the number and complexity of the service categories offered to customers, time spent with customers, or length of training period (Eisenhardt, 1985).

Obviously none of these measures mentioned in Table 6 could be applied in the international hotel expansion setting. Therefore, contextual measures for task programmability were

developed. In this study, task programmability was defined as the capacity to plan for the details of a contract. When the components of a contract and their measures are determined, the contract is considered to present high level of programmability. As stated earlier, there are two main dimensions to task programmability--the transaction dominant task and the information aspect. Below is the extract of the interview related to task programmability:

Let's discuss the capacity to plan for the details of the contract:

Question 10. Was this your first contract in the hotel's area?

Question 11. Was this your first contract with the other party (hotel developer/owner or franchisee? (*Expand: if no: what other contracts? Can you tell me if you consider those past contracts as successful? If yes, what information did you look for prior to signature?)*.

Question 12. Do you differentiate the obligations of the hotel owner or developer among the four contracts?

3. Information-base system

The idea of control in a transaction is simple in that the principal has two ways of ensuring that the agent's actions converge with her interests: measuring her output or observing her behavior in the process of concern. The former is labeled output control, the latter, behavior control. Each one of these control types is best served with its corresponding information and measurement systems. Performance or output measurement has been observed through the presence of commissions in the agent's salaries, or other objective measures of agent's results. The reliance on the personal observations, budget comparison or behavior rewards has been used as an indicator for behavior measurements. In essence, when the subject of control measurements is the "what", it is a performance measurement. Similarly, when the control measurement subject is the "how", it is a behavior measurement.

Interview questions have been developed to collect data related to the information base used in the transaction. Other sources of evidence were organizational documents such as reporting outputs or clauses in the contract related to the type of information to be transferred.

The contextual measures that were derived from previous research were listed in Table 7. Particularly, a monitoring effort could be measured by the number of visits to the agent by the principal (or hotel chain's headquarters' manager). Another measure, adapted from previous research would be the information used for the agent's compensation.

In this study, information-base system was defined as the set of communication procedures in place in a transaction. The system is based on information related to either behavior or performance. The following section of the interview addresses the sub-construct:

The following questions relate to the information system in place in the contract:

Question 20. Did the targets or standards you impose on the hotel owner, or developer, differ across the four contracts?

Question 21. What type of information is the hotel owner or developer required to transmit to you and how is it related to his compensation?

Question 22. What information are **you** required to transmit to the hotel owner or developer? And how is it related to your compensation? (*Expand: Is it used for the assessment of the compensation? What information is used to assess compensation?*

Question 23. What other information is exchanged? *(EXPAND on the means used and form (formal or informal).*

4. Outcome uncertainty

There are several dimensions of uncertainty, and therefore, different ways in which it has been measured (Table 6). As Boerner and Macher (2002) discuss in their literature review, the measurement of outcome uncertainty is *"concerned with exploring the hazards of maladaptation, empirical findings that relate uncertainty to organizational form are mixed, partly because of the multitude of uncertainty types examined*" (Boerner and Macher, 2002: 8).

In this study, outcome uncertainty was defined as the unanticipated changes in circumstances surrounding a contract. The purpose of the questions in this section was thus, to assess the level of outcome uncertainty within a particular contract. Contextual measures are listed in Table 7 and include sources of uncertainty surrounding the transaction in an international expansion hospitality context. These measures are the result of a synthesis between research efforts in TCT, AT, and those in the hospitality industry. These measures were transformed into the below interview questions.

The following two sections relate to your assessment of the outcome uncertainty of each of the (applicable number) contracts:

Question 24. If you were to give a level of accuracy of the contract's overall estimates, what would it be (ie: ±10%)? (*Expand: Is this accuracy different from one contract to another? What is the breakdown of estimates: RevPar, occ or costs).*

Question 25. On a 1-5 scale, how would you rate the political stability of the hotel location, where 1= very unstable and 5= very stable?

Question 26. On a 1-5 scale, how would you rate the quality of goods & services available in the location where 1= very poor and 5= very good? (*Expand: concern on the quality of the P&S provided in the hotel)*

Question 27. On a 1-5 scale, how would you rate the level of taxation in the unit's location, where 1= very low, 5= very high?

Question 28. On a 1-5 scale, how would you rate the stability of the hotel location's local currency where 1= very unstable and 5= very stable?

Question 29. How would you describe the infrastructure in the local destination?

Question 30. Is this infrastructure sufficient for the support of your chain's goods and services standards?

Question 31. How confident are you about the other party's successful contribution to the contract? (1. Very confident, 2. confident, 3. somehow confident, 4. Somehow unconfident, 5. Unconfident, 6. Very unconfident)

Question 32. Are you concerned about the possibility for the hotel unit representative to misuse your name for his/her own benefit at your disadvantage?

- *Organizational control*

Measures of behavior and output control as initially introduced by Ouchi (1977) have been developed around two axes--the reward system approach (Eisenhardt, 1985) and job assignments in the case of multinational organizations (Martinez and Jarillo, 1991). These measures are summarized in Table 6.

Outcome control has also often been measured through the frequency in which specific information were communicated to the principal. Egelhoff (1988) inspired Chung et al (2000), who relied on marketing information (total sales revenue, sales revenue by product line, sales to specific accounts, total selling expenses, components of selling expenses, selling expense by product line). They also examined manufacturing control through the following: total manufacturing expense, components of manufacturing expense, cost of specific raw materials, units of output by product, manufacturing variances from standard cost, and quality control data. Lastly, financial control was examined through the following parameters: subsidiary total profit, subsidiary profit by product line, inventory levels, account receivable turnover. In the present hospitality setting, the information type would be gathered through the examination of the contracts (Table 7).

The following questions, in conjunction with those on information system-base, were used to collect data on organizational control:

Question 13. How do you make sure that a franchisee will deliver?

Question 14. Do you control the hotel owner or developer? How? (*Make sure franchisee is covered.*)

Question 15. Could you please, briefly describe the main steps in the negotiation of a contract from first contact to signature?

Question 16. When does your first payment occur? (*For each contract!)*

Question 17. When are the corporate fees paid?

Question 18. Did it happen that your corporate fees were not paid?

Question 19. How do you recover them in that particular case?

- *Control Costs*

According to the AT and TCT, there are two types of control costs--the monitoring and the outcome control cost. Monitoring cost is the price for controlling an agent's behavior, while the output control cost is the price for measuring the agent's performance. These costs are supposed to be highly correlated with the cost of measurement systems. Additionally, research in AT point to the size of a firm as an important factor in the determination of administration burden. Eisenhardt (1985) measured outcome control costs using a dichotomous ownership variable (private vs. public corporation). However, as Eisenhardt acknowledges, her study suffered from a lack of control costs measures. More specifically, her sample did not allow for the measurement of control costs.

In order to allow control costs to be measured, contextual measures had to be developed for this research. These measures are listed in Table 7. Monitoring cost was measured using the time allocated by the hotel chain to the monitoring of the hotel unit's activity. This measure was triangulated with the count of the number of persons allocated to the monitoring task and investment in quantitative behavior information systems. Similarly, output control costs were assessed through the amount of investment in performance reporting systems or number of official meetings involving both parties. Control related costs are defined here as the expenses incurred by the party of a contract who is delegating a task to another party. These costs are paid by the delegating party to control for either the behavior (process) or the performance (output) of the other party. This data was collected through the following section of the interview:

Now, I would like us to discuss control related costs:

Question 33. Do you have a reporting system in place? (*Expand on outputs.)*

Question 34. Did the contract require further investments in the reporting system? (*Expand on date of creation and evolution of the system.)*

Question 35. Who is in charge of monitoring the unit's activity? (*Expand on role (meetings), and degree of specialization of the person.)*

Question 36. Did the chain invest in systems supporting this person's activity (Information systems and reporting systems)?

- *Other Control Costs*

This construct integrates, for the first time, agency and transaction costs. Therefore, there is no operationalization of additional costs integrating agency and transaction costs in the hospitality industry. Based on the literature review conducted in the previous chapter, evidence related to additional costs could be collected from the each growth option's contract. Thus, bonding costs should be reflected in the equity and loan contribution clauses (Table 7) for the management and lease contracts. Advertising clauses and training clauses specificity could provide indications of the level of additional costs in a franchise contract.

Literature on franchising, is more developed than the one on management contracts or leasing, and suggests a particular franchise cost related to the free rider potential. This risk is usually covered by the competition clause, which attempts to restrict the free rider potential. Consequently, measures for the residual loss estimate, information search costs, and bargaining costs were left for development. Table 7 lists contextual measures that have been developed for this exploratory study. These contextual measures serve as a development basis for the questionnaire.

Other control costs relate to pre-contract costs that often would be considered as a sunk cost. Thus, they would constitute estimates for time and effort spent to investigate about the other party (information search costs), negotiating (bargaining costs), and showing commitment into the transaction (bonding costs). Contextual measures are suggested in Table 7 and used for the questionnaire development.

In this study, other control costs were defined as all other expenses incurred by the parties involved in a transaction to ensure the convergence of their actions and interests. These costs include pre-payments or other proofs of commitment, expenses for information search, and bargaining costs. The following questions were developed for the construct of other control costs:

Question 37. Was an opportunity cost estimated by your financial team? (*Expand on the estimate and the assumptions used for the estimate.)*

Question 38. When you think of the process that your chain has been through until the final signature, does it differ across the four contracts? (*Expand on length and revisions on the contract.)*

Furthermore, data related to other control costs appeared in the interview answers related to control costs, growth option selection, and task programmability. This aspect is further developed in the data analysis section of this chapter.

- *The construct of Elements of Risk*

Decisional management research pointed to two elements of risks in managerial practices-- the probability and the magnitude of loss. In a decision theory context, Forlani (2002) submitted respondent groups to scenarios settings for the measurement of the elements of risk. He asked respondents to assess the probability of loss related to the introduction of one new product, and then to several ones into an existing product line. The magnitude of loss was operationalized through the capital requirement incurred by the production of the same product.

In this study, the elements of risk were defined as the two components that are assessed by managers when making a decision. Thus the first element was the probability of loss, or the estimate of the threat of a very poor outcome. Second element was the magnitude of the loss and is the estimate of the amount of money that could possibly be lost. Practically, this aspect was sensitive in the development context of the study. Obviously, as suggested by one of the experts in the panel, development managers could not reasonably answer that they believed that the negotiated contract could fail. Therefore the initial questions were refined after the first interview and the following were used.

The following interview questions addressed the elements of risk:

Question 39. What types of risk do you attempt to manage? (*Expand on the most important.)*

Question 40. How does this risk differ across contracts types (franchise, management agreement, etc…)?

Question 41. When negotiating a deal, are you more concerned with the likelihood of a poor outcome or the amount of money that could possibly be lost? Please explain.

TEST INSTRUMENT DEVELOPMENT, VALIDITY, AND RELIABILITY

Triangulation

Two main sources of information were relied upon for the data collection process. The first source was a series of interviews with pre-determined participants in the organization. The second were organization documents such as franchise contract agreements, press releases, annual reports, information-system documentation and other information related to the expansion project under examination that were made available. For construct validity purposes, multiple sources of evidence were used. The summary of sources of information for the present research variables is listed in Table 7.

- *Interviews*

Semi-structured interviews were conducted with managers involved in the process of selecting, negotiating, and supporting the implementation of expansion strategy. A series of interview questions was developed based on the contextual measures listed in Table 7. These questions were relied upon to structure the interviews. This structure in the interview process was introduced in an effort to enhance the study's reliability. In international hotel chains such managers are part of the "development" department or development team. These managers are often in charge of the examination of the feasibility of a growth option. Generally, the expansion strategy involves the financial officer, operation officer, and the chain's CEO. The decision-making team might differ from one company to another based on its size or culture; therefore, criteria for interviewee selection were determined as follow.

Interviewee's criteria: To be interviewed the person needed to be involved, in practice, in the expansion process. To determine such involvement, the potential interviewee's tasks and responsibilities were first verified. Questions were asked at the beginning of the questionnaire to ensure this aspect. A pre-requisite for such a profile was that the interviewee was part of the corporate team in the international hotel chain.

Table 7 Data collection method: Summary

Constructs	Sub-Constructs	Variables	Contextual Measures	Data Collection Method
Option's organizational features	Asset Specificity	1. Site specificity	Locational advantage The reasons for selecting the site The location is consistent with the chain's hotel offer Destination attractiveness for the chain Destination corresponds to strategy coverage Hotel segment affiliation Hotel Market share Hotel reputation Synergy sought The hotel unit is a landmark in the chain's image or in one of its brands Sources of logistic cost reductions (i.e.: central purchasing unit)	Interview Interview Interview Interview Interview Annual report Interview Interview Interview Interview Interview
		2. Physical asset specificity	From an architectural and design standpoint: level of investment made in hotel unit Hotel infrastructure: level of investment Investment reduction through exiting amenities (minimum upgrading) Level of investment for the alignment of the unit's marketing and operation activities with the chain	Chain's documents Development department & Interview Interview
		3. Human asset specificity	Investment needs in human capital to include the unit into the chain Particular HR allocation due to the unit's nature or location	Interview Annual reports/website

Constructs	Sub-Constructs	Variables	Contextual Measures	Data Collection Method
Option's organizational features	Task Programmability	Predominant task	Obligations to the principal Task delegated by the principal to the agent Nature of the transaction Processes covered by the contract Procedures in place Uses of manual of operations	Enforced contracts analysis Interview Administrative documents
		Information level about the agent	Prior transactions with the agent Prior investments in the location Information gathered about the other party	Interview Interview Interview
	Information system base	Behavior – based information system (Monitoring)	Number of principal's visits to the agent for control Information used for agent's compensation Information used in the agent-principal communication Reliance on monitoring vs. performance targets	Contracts Interview Organization's documents
		Output – based information systems (impersonal evaluations)	Reliance on monitoring vs. performance targets Information used for agent's compensation Information used in the agent-principal communication	Contracts Contracts Interview
	Control-related costs	Monitoring measurement Costs	Time allocated to the monitoring of the unit's activity Persons allocated to the monitoring of the unit's activity Salary level of the person responsible for monitoring Availability of monitoring person Investments in quantitative behavior measurement	Interview
		Outcome measurement costs	Investment in performance reporting systems Investment in information systems Number of official meetings involving agent and principal	Interview
	Outcome uncertainty	Volume uncertainty	Level of confidence about demand forecast Level of political stability in the unit's location Quality of goods & services Taxes in the unit's location	Interview Interview Company Website

Constructs	Sub-Constructs	Variables	Contextual Measures	Data Collection Method
Option's organizational features		Revenue forecast	Level of confidence about price forecast Level of political stability Level of exchange rate stability	Interview Interview Company website
		Cost forecast	Level of confidence about cost estimates Level of political stability Quality of goods & services Availability of standard-supporting goods and services	Interview Company website
		Uncertainty about other party's behavior	Estimate of moral hazard in the relationship Estimate of free rider's threat in the relationship	Interview Interview
		Project uncertainty	Discount rate applied to the forecasts Manager's estimate of the project's success dependency on external factors	Interview Administrative documents
Organizational Control	Behavior	Informal qualitative behavior measures	Part of behavior control and supervision in principal's tasks	Interview Administrative document
		Formal quantitative behavior measures	Agent's evaluation scheme Budgeting and spending limitations Quantitative behavior measurement Agent's compensation basis	Interview Administrative document
	Output	Formal quantitative output/performance measures	Agent's evaluation scheme Performance provisions in contract Fees & Fee structure Compensation basis	Contractual documents
Other control costs	Residual loss estimate	Principal's opportunity costs	Amount estimated for the opportunity costs	Interview Project's estimate
	Information search costs	Means-end (specific to destination) Moral hazard reduction	Costs related to information collection about the property, the other party, and property external environment (political situation, economic situation) Time dedicated to the project Number of persons working on the project	Administrative documents & Interview

Constructs	Sub-Constructs	Variables	Contextual Measures	Data Collection Method
Other control costs	Bargaining costs	Negotiation costs	Legal costs incurred Estimated costs related to conceded clauses Number of negotiation rounds Number of contract modifications Time incurred between first contact and contract signature	Interview
	Bonding costs	Agent's financial commitment	Equity participation Amount of loans Pre-payment Amount engaged by the agent, that would not be engaged for another transaction	Interview and company website
Risk Elements	Magnitude of loss	Amount of money that could be lost if actual outcomes turn out worse than expected	Capital required to introduce the new unit in the network	Interview
	Probability of loss	Assessment of the project's likelihood of failure [1-P(Success)]	Decision makers' estimate of the project's likelihood of failure	Interview

- *Administrative documents*

Administrative documents related to expansion strategy and legal contracts for each growth option were used as a second source of evidence. These documents include documentation of communication between the two parties, project development documents, and other documents related to the growth option and its introduction in the chain. In addition, when made available, contracts related to the transaction were used as a third source of information.

This data triangulation aimed at enhancing the research's construct and content validity. This procedure was also used in TCT, AT, and control literature. That previous use enhances the confidence in the process. For instance, in their assessment of measurements for uncertainty in TCT research, Boerner and Macher (2002) argued that "*usually employed by economists, the examination of actual contracts represent an excellent data source for historical and empirical (Transaction Cost Economics) TCE-related research*" (ibid: 10). The authors listed the examination of contract terms such as price, royalty rates, franchise fees, take-or-pay provisions, price adjustment benefits, and dispute resolution mechanisms.

Therefore administrative documents were used as sources of evidence for data triangulation. Documentations and contracts were used for a more objective measurement of the examined constructs. It is believed that they are a good complement to a semi-structured interview. Obviously, the use of these last two sources of information depended on the participating hotel chain's willingness to share information. When possible, press releases and information of the chain's website was retrieved.

Table 8 presents a summary of the directions followed to analyze the documents that were presented. This procedure for the operationalization of the construct was developed prior to the field research.

Table 8 Specific construct operationalization by growth options

	Growth Option	**Contract clauses**	**Construct operationalization**
Asset specificity	Lease	Option to purchase	• The presence of option to purchase in the lease is an indicator for increased degree of asset specificity
Outcome uncertainty	Leases and management contract	Contract length and renewal option	• The higher the contract length the lower the uncertainty • The presence of a renewal option decreases the uncertainty
	Franchise	Contract term and renewal option	• The higher the contract length the lower the uncertainty

			• The presence of a renewal option decreases the uncertainty • High contract terms and renewal options are indicators of behavior control efforts.
Control	Management Contract Agent's evaluation scheme	Fees & Fess structure Termination provision including performance provision Budgeting and spending limitations	• Degree of reliance on performance indicators (i.e.: % GOP rather than % revenues) • The presence of a degree provision is an indicator of outcome control • The stricter the termination terms, the higher the presence of outcome control • The nature of budgeting and spending limitation is an indicator of behavior control in the relationship
	Lease Rent nature: • Fixed • Semi-variable • Variable	Indexation clauses Upward only adjusted rent Contingent on asset use clause Leasing incentives	• The higher the portion of variability in the rent, the higher the presence of output control • A fixed lease reflects behavior control
	Franchise Agent's evaluation scheme	Franchise fee	• The structure of the franchise fee is an indicator of the organizational control in place
Bonding Costs	Leases and management contract	Operator loan & equity contribution	• The higher the loan and contribution, the higher the bonding costs
	Franchise	Advertising clause Training clause	• The higher the commitment into advertising and training, the higher the bonding costs
Free rider potential	Franchise	Competition clause	• The stricter the competition clause (ie. large geographical perimeter, and long duration) the lower the free rider potential

Sample

According to Stake (1994:243), case selection in qualitative research is "*a sampling problem. The cases will be selected to represent some population of cases. (...) In the beginning, phenomena are given; the cases are opportunities to study the phenomena*". Therefore, he simply suggests that the researchers in case study should lean towards "*those cases that seem to offer opportunity to learn*."

Chain selection criteria: Chains selected for this multiple case study presented the following characteristics:

- More than 60% of its revenues are generated from the hotel business.
- The chain must have property in more than three countries to be considered as a multinational hotel chain.
- The chain is presently implementing an expansion strategy. In other words, the company is presently involved in prospecting, negotiating, and opening new units under one of its brands. These units' results will then be part of the chain's consolidated annual financial reports.
- Size being a critical control variable in organization theory research, it has been used as a control variable in the selection of the case study. Size is defined in this study as the number of hotel unit operated, owned or franchised by the international hotel chain. Case C presents the largest network of hotels, followed by the pilot, and Case A. As for Case B, it has the smaller size and is the only privately owned company.

International hotel chains have been selected for two reasons. First, international and not national hotel chains were selected for practical reasons. Making this choice increased the size of the population to investigate on. Second, by selecting a sample of international chains, the noise related to national effect was hoped to be minimized. Simply put, if two national chains were to be compared, the effect of the national context on the observed relationships would be even more difficult to assess in a qualitative research. It is this last research obstacle that was hoped to be avoided by the selection of international hotel chains.

External Validity

"*Case study can usefully be seen as a small step toward grand generalization*" (Stake, 1994: 238).

Yin (2002) suggests the use of theory in single-case studies and replication logic in multiple case studies for the enhancement of external validity. The present research is directed by theory as propositions were derived from existing literature review. Not only were propositions derived to guide the study, but the sub-propositions as well. This is due to the AT and TCT development, two fundamental underpinnings in this research. Additionally, the reliance on multiple case studies strengthens the external validity potential of this research.

As mentioned above, the unit of analysis is the transaction between the hotel chain and the hotel unit selected as a strategic growth option. This specification of the unit of analysis sets the research boundaries and the analytic limitation for further replication. Simply stated, this research's observations and conclusions could reasonably be generalized to other transactions relating a hotel chain and a hotel unit selected as a strategic growth option. This study is guided by two well-established theories, the AT and TCT, both of which strengthen its theoretical basis. This solid theoretical grounding enhances external validity. In other words, future generalization of this study's results and observations could reasonably be considered despite the limited generalizability of the adopted research method.

Construct and Content validity

The issue of construct validity is related to the insurance that the sources of data, or operational information collected, do indeed represent the construct or phenomena under examination. Four tools were relied upon for construct validity insurance: a panel of experts confirmation of contextual measures, multiple sources of evidence, constant link between theory and evidence, and key interviewees revision of draft case study reports.

The purpose of applying these four tools above was to develop a sufficiently operational set of measures that would take into account the practical constraints related to the present research work. In this case, construct validity is jeopardized by the lack of existing contextual measures for the examined constructs and relationships. To overcome this issue, contextual measures were rigorously inferred from previous research efforts. Additionally, when applicable several measures for each construct were developed for the interview questions. Moreover, when it was

possible, in-depth focused interviews were completed during the design stages. It is believed that the reliance on these four steps would allow the introduction of an "objectivity" element in the data collection process. To further enhance confidence in the measures used, a panel of experts was asked to evaluate the questions prepared for the interviews. This panel of experts was composed of both practitioners and academic specialized in the hotel industry. Finally, key interviewees were asked to review the draft case study reports. This process aimed at reducing subjectivity aspects that might have been introduced by the researcher.

The central methodological issue related to conducting case studies is the one of content validity. Three preventive measures were applied to enhance the content validity of this research: the use of multiple case studies, the reliance upon multiple sources of evidence, and the maintenance of a chain of evidence (Yin, 2004). Additionally, the interview questions helped structure the interview. Furthermore, organizational documents were inspected. These documents included (when accessibility allowed it) the following: legal contracts encompassing the transaction, budgeting, reporting documents, communication documents between the hotel chain and the hotel unit, financial forecasts conducted during the development stage, and any other document related to the transaction. These multiple sources of evidence were used for data triangulation. Finally, links between the available literature and evidence collected from the field was conducted on a regular basis.

Reliability

The question of whether or not the same results would be obtained through replication of the study is fundamental in the case study research method. To enhance the reliability of this study, four measures were applied: a case study protocol was developed, a case study database was created, interview questions did structure the interviews, and a detailed data management process was put in place prior to the first contact with the field.

DATA MANAGEMENT AND METHOD OF ANALYSIS

Data reduction

According to Miles and Huberman (1994) data reduction is the first step in the analysis of qualitative data. The process of data reduction also referred to as the "*ladder of abstraction*" (Miles and Hubmeran 1994) consists of four main actions: condense, cluster, sort, and link

overtime. These four steps have been followed for the analysis of the data collected. This process is illustrated hereafter in figure 7. The first three steps, namely condensing, clustering, and sorting were applied to each case study separately; then the individual-case findings were contrasted against each others to identify a more general pattern.

First, a transcript of each interview was written shortly after each interview. Then, the text obtained was analyzed. This research is theory-driven and the model developed in Chapter 2 was followed to condense the data. Therefore, terms were identified by construct, and manually highlighted in the text. During this step, the dimensions of each construct were identified.

Second, the clustering consisted of copying the dimensions of each construct in a matrix. (Appendix D is the collection of matrices obtained from each case study.) Therefore a 3x12 matrix was obtained for each case study. Each matrix presented the 3 interviewees and their answers for the 12 constructs and respective sub-constructs.

Table 9 Matrix for the data reduction by interviewee, by case

Case C	
Interviewee 1 *Director of Development*	***Expansion mode:***
Interviewee 2 *Senior VP of development*	***Expansion mode:***
Interviewee 3 *Regional Director of development*	***Expansion mode:***

Organizational features of hotel unit	
	Asset specificity
Interviewee 1	✓
Interviewee 2	✓
Interviewee 3	✓

	Organizational features of hotel unit		
Case C	*Task programmability*	*Information system-base*	*Outcome uncertainty*
Interviewee 1	✓	•	•
Interviewee 2	✓	✓	•
Interviewee 3	•	•	✓)

	Organizational Control	
Case C	*Behavior Control*	*Output Control*
Interviewee 1		•

Interviewee 2		
Interviewee 3	•	•

	Control Costs	
Case C	*Monitoring costs*	*Outcome Control Costs*
Interviewee 1		
Interviewee 2	•	
Interviewee 3	•	

	Other Control Costs			
Case C	*Residual loss estimate*	*Information search costs*	*Bargaining costs*	*Bonding costs*
Interviewee 1	•	•	•	•
Interviewee 2	• ”	•		•
Interviewee 3	•	•	•	•

	Elements of Risk	
Case C	*Magnitude of loss*	*Probability of loss*
Interviewee 1	•	•
Interviewee 2	•	•
Interviewee 3	•	•

Third, this data display by matrix allowed the identification of dominant dimensions and trends within each construct. This step consisted of relating "*categories to subcategories along the lines of their properties and dimensions*" (Strauss and Corbin, 1998). Particularly, the emerging themes within each construct and sub-construct were compared against the propositions developed at the end of Chapter 2. The purpose of such comparison was to maintain the chain of evidence and to maintain the construct validity of the research. Similarly, the triangulation of the sources of evidence was conducted during this same step of data analysis. This procedure is often referred to as "*axial coding*" (Strauss and Corbin, 1998:124).Appendix E contains all four matrices obtained from each case study).

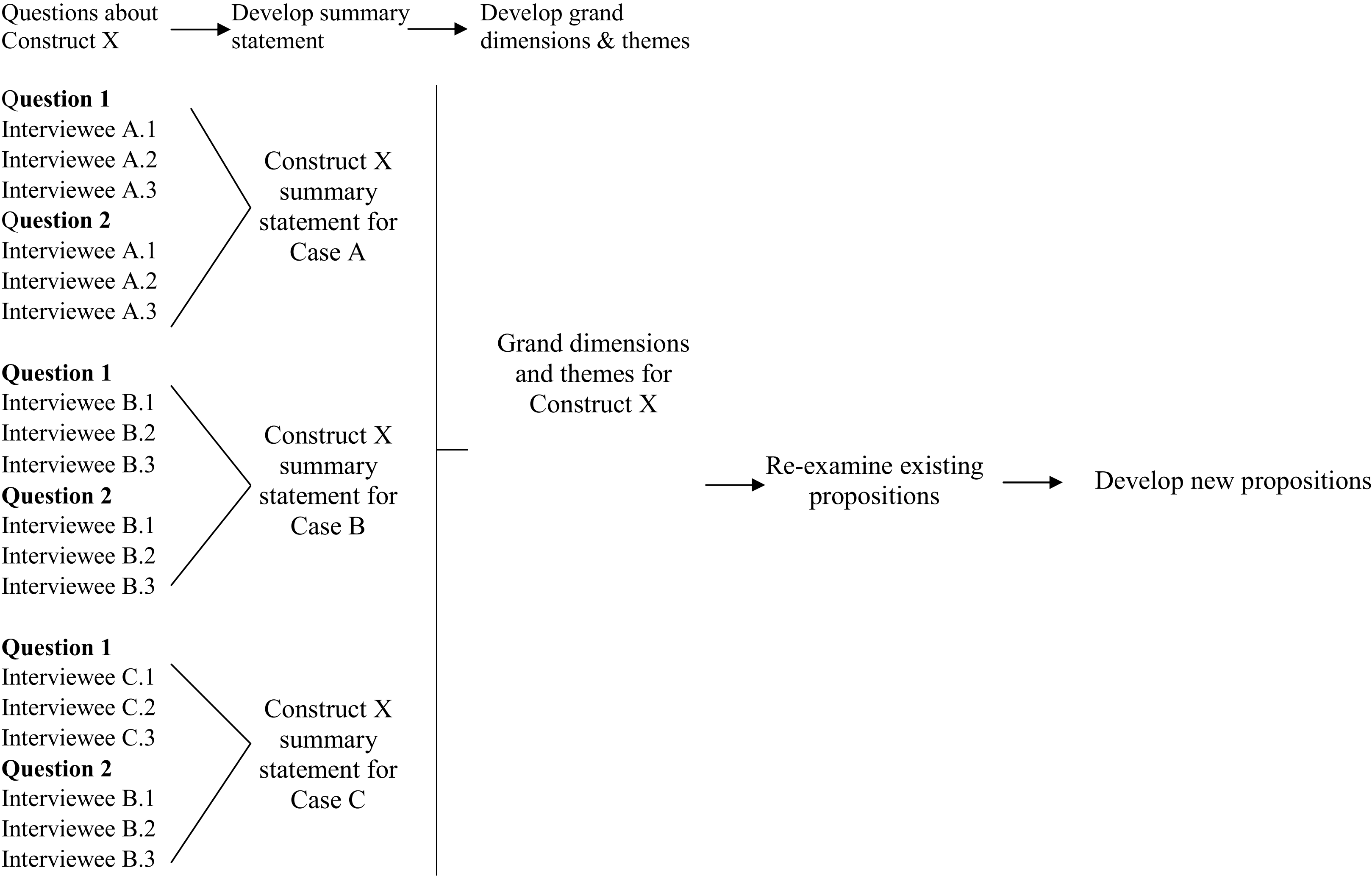
Finally, the "*deep structure*" (ibid) and the framework were developed from comparing the sorted data from each case study.

Data display

"*The visual format that presents information systematically, so the use can draw valid conclusions and take needed actions*" (Miles and Huberman, 1994: 91).

Matrices were built to systematically present the information collected through the interviews and in the documents collected. These matrices were built at the second step of the analysis of data and used in the following two steps. The process of developing the variables, propositions, and the new model are very similar to the one used by Schmelzer (1992) in her examination of the strategy implementation in restaurants. This process is presented in the following Figure (7).

Figure 7 Flow chart showing the process of developing variable description, propositions, and new framework



Verifications and conclusions

This research made comparisons and drew conclusions. The conclusions were drawn at the case study level and comparisons were made across interviewees and case studies. Results from these verifications are presented in Chapter 4. Conclusions drawn on the constructs of control and the elements of risk are summarized in Chapters 5. Based on these conclusions, propositions and additional suggestions are made in Chapter 5 on the relationship between expansion strategies and structure in the hotel industry.

SUMMARY

This chapter presents an overview of the research method that was adopted for this research. Further, the methodology section covers the assessment of the case study method as a research method, the research design, the data collection preparation, and the case study reporting.

CHAPTER 4: RESULTS

INTRODUCTION

Under the overarching question of how strategy and structure relate, five research questions guided this work:

- Is control a structural variable in the management of expansion strategy?
- How does control intervene in the management of risk in expansion strategy?
- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion strategy context?
- What is the role of control costs in the management of risk for expansion strategy?
- How do the features of the hotel unit affect the management of risk in expansion strategy?

Based on these five research questions, the methodology presented in chapter 3 was developed. The methodology and the constructs investigated were, in turn, the result of the literature review conducted in Chapter 2. This chapter presents the synthesis of the results obtained from this research. In particular, this chapter introduces the results for the constructs of control and elements of risk within each case study. Four main sections representing the four cases studied constitute this chapter.

Confidentiality was a major concern for the interviewees in the hotel chains of this study. Very strict confidentiality agreements were signed between the researcher and the hotel chain contacts restricting the information to be displayed. Following the demand of the participants, the information provided about the hotel chain was aggregated so that the company could not be recognized. Nevertheless, the details on the process of the implementation of expansion strategies and on the constructs of control and elements of risk were maintained.

The four companies constituting the cases of this study fulfilled the sampling requirements described in Chapter 3. In other words, each company had more than 60% of its revenues generated from the hotel business. Additionally, each chain operated properties in more than three countries. Furthermore, each chain was in the process of implementing an expansion strategy during the study. However, the steps of data collection revealed that each chain approached its expansion strategy differently. These discrepancies are discussed hereafter

separately for each case. Size, a control variable, is also discussed in the presentation of the individual case study.

Three persons were interviewed within each company. In each case, the first contact was the development director, who then directed the researcher towards members of his development team. The two other interviewees were regional development directors who participated in the regional efforts of development.

Three out of the studied companies are publicly traded and managed more than one brand in distinct segments. Case B, a privately owned company, is smaller and manages a single brand. In the case of publicly traded companies, documents that could not be provided from the contact person were retrieved from the chain website for data triangulation. The contact person of the privately owned company provided most of the documents required for triangulation purposes. The first company contacted was used as a pilot for this research.

In an effort to guide the reader through this chapter, Table 10, below, recapitulates the main terms that are employed in this study. These terms were dictated by the research questions once the review of the literature was conducted.

Table 10 Glossary of terms as employed in this study

	Definition in this study
Asset specificity	The degree of uniqueness of an asset to a contract. There are three types of asset specificity: site specificity, physical specificity, and human asset specificity.
Bargaining costs	Costs related to the negotiation of the transaction.
Bonding costs	The agent incurs bonding expenditures for the reduction of agency conflicts. Bonding costs are considered as a facilitator of the agency relationship, thus reducing its costs.
Control costs	The expenses incurred by a party in a transaction to control for either the behavior (process) or the performance (output) of the other party.
Developer	A position in the hotel chain. The developer is generally part of a development team, whose responsibility is to expand the network of the chain through new contracts.
Elements of risk	The two components that are assessed by managers when making a decision. The probability of loss and the magnitude of the loss are the two elements of risk.
Growth option	The expansion mode available for the execution of the expansion strategy. Commonly used growth options in the hotel industry are: franchises, management contracts, leases, rentals, and full or partial equity participations.
Human asset specificity	The level of investment in human resources specific to the contract.

Information-base system	The set of communication procedures in place in a transaction.
Magnitude of loss	One of the two elements of risk, it is the estimate of the amount of money that could possibly be lost.
Monitoring costs	Monitoring costs are the costs attached to behavior control. Monitoring methods include auditing, formal control systems, budget restriction, and incentive compensation systems.
Other control costs	All other expenses incurred by the parties involved in a transaction to ensure the convergence of their actions and interests. Thus, they would constitute estimates for time and effort spent to investigate about the other party (information search costs), negotiating (bargaining costs), and showing commitment into the transaction (bonding costs).
Outcome uncertainty	The unanticipated changes in circumstances surrounding a contract.
Physical specificity	The level of investment made by one of the parties in a contract that involves construction and tangible alteration. Modifying the architecture of a hotel unit to adhere to the requirements of the hotel chain increases the physical specificity of an asset.
Probability of loss	One of the two elements of risk, it is the estimate of the threat of a very poor outcome.
Site specificity	The advantages provided by the location of the hotel unit to the hotel chain.
Structure	The network of hotels making up a hotel chain.
Task programmability	The capacity to plan for the details of a contract.
Transaction	(Borrowed from the Transaction Cost Theory.) It is the interaction between the hotel chain and any representative from the hotel unit for a business purpose. The interviewees often referred to it to as the "*contract*", or the "*deal*".

PILOT CASE

The pilot company is a multi-brand, publicly owned international hotel chain. It presents a very large network in comparison to other players in the industry. Its publicly quoted targets are of an additional 1,000 hotels (which corresponds to almost 50% increase) in the next 10 years. According to the interviews and based on the documents collected for this research, management agreements and franchises were the two growth options relied upon for meeting these expansion targets. The company did not project to expand through leases or any form of equity participation. The development efforts of this company were oriented towards two main goals: first, maintain the stream of fees over the length of the contract and second, extend the size of the system. As one of the managers interviewed said, the company's focus was on the "*expansion of (*their*) brands*". All three persons perceived the development of the chain as the implementation in "*strategic markets*".

Organizational features

Asset specificity

In accordance with previous research in hospitality management (Zhao, 1994; Zhao and Olsen, 1997), the results of the interviews revealed that the profile of the destination was the most important element in determining the asset specificity of the hotel unit. By profile of destination, the respondents intended the characteristics of the tourism destination where the hotel unit was located. More specifically, the respondents emphasized on the "*potential of the destination*" and perceived it as an important element in the selection of the hotel unit.

When the questions on asset specificity were asked (please refer to Chapter 3), the characteristics of the location were always mentioned first in the answers. This indicated a strong relationship between asset specificity of the hotel unit and the location. Respondents mentioned the room supply in the destination, estimates of room demand, degree of competitiveness, uniqueness of the location, and the potential of growth for the hotel market at the destination. Appendix D details the dimensions forming the potential of a destination extracted from the interviews.

Overall, the interviews revealed that in the current hotel industry situation, the degree of compliance of the hotel offer with the brand determines its degree of asset specificity. As one of the interviewees summarized it: "*deals are consistent, they have to be to our brand*." This consistency was based on two main axes: the degree of correspondence with the customer base and the degree of brand competitiveness in the destination. According to one interviewee, a flagship unit represented the highest level of asset specificity for hotel chains.

Site specificity:

Site specificity, one type of asset specificity, was highly inter-related with the specificity of the destination. The interviewees systematically mentioned the characteristics of the location first when answering the questions on site specificity.

When asked to expand on the specific characteristics of the site, the interviewees listed selection criteria such as hotel in a capital city, proximity to economic activity, or hotel in industrial or commercial center. Most importantly, they made a clear distinction between two main determinants of site specificity: resort or city site. According to the respondents, the

specificity of the site was related to the degree of compliance of the hotel site with one of these two main segments of the hotel product.

Physical asset specificity:

The second type of asset specificity, namely physical asset specificity, also presented two dimensions. It appeared that the degree of physical asset specificity was determined by first, the degree of compliance of the hotel infrastructure with the brand norms and second, by the degree of advancement of the infrastructure of the project. In other words, development directors perceived two aspects of the infrastructure of the hotel as important in their development decision and efforts. First, they examined the coherence between the infrastructure (architecture, design, building attributes, room size, number and size of restaurants, and other service outlets in the hotel) and the brand standards and norms of the chain. This consistency ensured that the infrastructure of the hotel would efficiently support the future operations of the hotel chain. As one of the respondents said, developers examine the "*efficiency of the design*" of the hotel. Second, the respondents also referred to the stage of advancement of the infrastructure of the hotel. Developers distinguished between a hotel at project stage, and a conversion of an existing one. According to the interviewees, the degree of advancement of a hotel unit constituted an important element in assessing the degree of consistency of the hotel unit with their chain.

The interviews also revealed that the degree of advancement of the hotel was a criteria used by developers to assess the degree of control they have over the contract. According to the developers, intervening in the early stage of construction increases their control over the end product. Ultimately, this intervention can increase the insurance of having a hotel that corresponds to the standards of the chain. The notion of having control over the internal determinants of a contract was referred to, in Chapter 2, as task programmability. This indicated a bridge between asset specificity and task programmability. This last result is further discussed in the section on task programmability and in Chapter 5.

Human asset specificity:

The mobilization of human capital in the efforts of hotel developments appeared to be a complex effort of coordination. The developers benefited from a set of support skills from the head offices. This support consisted of a financial, operational, and legal support. At the same

time, developers had to coordinate with the operational team and the "*technical team*" during the pre-opening stages of the project. Finally, developers had to take into consideration the availability of human resource capabilities in their selection of the hotel unit. This is without mentioning the planning effort of the development head to train and support his development team. The profile of a developer presents a "*difficult combination*" that required several distinct skills.

Therefore developers had to coordinate between the different functions of the head office and the teams on site. The operations and technical teams were the main groups on site. The operational team was in charge of managing the hotel once opened. They intervened in the pre-opening stages. The technical team was responsible of aligning the infrastructure of the hotel with the brand standards and norms.

The above-mentioned elements related to the mobilization of human resources were support elements that were managed at the chain level. Two dimensions of human asset specificity were relevant to the unit of analysis: time and the operation competencies available in the location. Timing between the signature of the contract and the opening of the hotel composed the degree of human asset specificity in hotel development. The interviewees mentioned the available training period in the location and its relationship with the deployed human efforts. When the time available until the opening is short, the investment in human asset was more important (in terms of number of manager-expatriates on site and number of team members on site). The availability of operation competencies in the location of the hotel emphasized the influence of timing on the degree of human asset specificity. In turn, this revealed that human asset specificity was related to the cost of monitoring (number of manager-expatriates on site and number of team members on site) and thus to the costs of control. This aspect is also discussed in the section on control costs and explored in Chapter 5.

Task programmability

The second sub-construct forming organizational features is task programmability. The interviews of the pilot case revealed four determinants of the degree of task programmability. First, the existence of past and present experiences of the chain in the destination increased the degree of task programmability. Second, the level of experience of the other party (i.e.: the hotel owner or developer) with the market in the destination augmented the degree of task programmability. Third, the level of experience of the other party (i.e.: the hotel owner or developer) with the operations of a hotel added to the degree of task programmability. Particularly, developers referred to the capacity of the hotel owner or developer to operate according to the standards of the brand. And finally, a shared comprehension of the terms of the contract between the chain and the other party (i.e.: the hotel owner or developer) raised the degree of task programmability.

These four dimensions were synthesized into two main categories: the first was the existence of a known third party in the market and the second was the presence of another operating hotel in the destination. In the first dimension, the third party could be the hotel owner or a developer or a third party that introduced the owner or developer to the hotel chain. As one of the respondents described them: "*partners with shared interests and past transactions*". This first dimension encompasses the above listed determinants two to four. As for the presence of another operating hotel unit in the destination, it ensured a better knowledge of the market and thus a higher capacity for planning the details of the contract. This represents the first determinant presented in the previous paragraph.

The answers to the questions on task programmability revealed links with other constructs. In relation to control, and as suggested by the literature on TCT and AT (please refer to Chapter 2), task programmability had an impact on control costs. Particularly, the absence of a known third party or an existing unit required the instruction of an independent market study, or an in-depth feasibility study, a higher number of on-site visits, more thorough due-diligence fulfillment, or a higher participation in the pre-opening stages. Simply put, the low level of task programmability (due to the absence of a known third party or operating unit in the destination) increased the monitoring costs.

Similarly, and also in relation to control, asset specificity appeared to be related to task programmability. As mentioned earlier, the stage of advancement of the hotel infrastructure

allowed a more accurate programmability of the contract. In other words, a contract that is still at the project stage presents a higher degree of programmability. The existence or absence of partner or operating units in the location emphasized the degree of programmability related to the contract. In an extreme case, for instance, if a contract was to be a conversion and it was the first contact of the chain with the destination, the degree of task programmability would be very low. As a result, the monitoring costs would be at their highest.

Outcome uncertainty

For the interviewees, the outcome of a development process is a hotel that corresponds to the brand standards. Simply put, the outcome is a hotel that sells at the expected level and provides the expected returns. As one of the developer said, their responsibility is to ensure: "*quality of the end product*".

The interviews revealed three variables affecting outcome uncertainty of the transaction. The first is the degree of application of brand standards, the second is the financing capacity of the owner or developer, and third, is the comprehension of the dynamics of the market. In other words, if the contract presents factors that might jeopardize the application of brand standards (i.e.: "*the owner's own agenda*", political instability that might affect the ownership status, economic development of the country), or if the owner misled the chain on his financing capacity, or if the developers failed to accurately assess the market, the degree of outcome uncertainty is increased.

In an effort to manage this outcome uncertainty, and in accordance with the contingency approach to uncertainty (Galbraith, 1974), developers gathered data on "*comparable hotels and locations*". However, when timing was an issue in the destination, the respondents tended to allow for "*unexpected delays*" into their planning.

Information system-base

The information system-base in the pilot case essentially served a behavior measurement process. The data collected revealed that the chain relied upon a large electronic information system relating the different functions within the organization. Furthermore, the information system in place allowed the sharing of information between the organization and its external partners. The type of the information that was transmitted in the network was mainly process

oriented. The financial and accounting information reported in the system constituted the only performance-based information. The accounting reporting system was used to monitor the performance on a day-to-day basis.

In addition to the electronic information system, meetings and other formal and informal means of communication were also in place. Guest comments, quality audit teams, and mystery guests were the other bases of information collection. The interviewees insisted on the role of maintaining communication with the hotel owner and or developer. According to them, regular meetings and communication with the other party were essential for the success of the transaction. This supported the result that the information system-base in place in the company served a behavior measurement process.

Organizational Control

Control type

The data revealed that the objects of control, both the performance and the behavioral ones, are explicitly mentioned in the contract. The legal document relating the two parties clearly lists the milestones of behavior control and the outputs of performance control. The objects of behavior control are brand standard, description of procedure of operation, due diligence, hotel architectural plans and hotel engineering plans, or legal ownership documents. The measures of performance for the output control are mostly financial figures and include occupancy, ADR (Average Daily Rate), RevPar (Revenue Per Available Room), GOP (Gross Operating Profit), GOP percentage, and departmental profit. Finally, the measures of quality of operations include a mix of output and process based information. These indicators comprise guest comments, quality audit teams, mystery guests, or feedback from team members.

Overall, control in the development process consisted of a selection process rather than a control of the transaction itself. The respondents viewed the objective of the control task as one of brand protection. Finally, it appeared that the higher the financial level and involvement of the chain in the transaction, the larger the number of persons involved in the selection process.

The data revealed four features of behavior control in the implementation of expansion strategies by the pilot case. First, behavior control was predominant during the pre-opening stage. Second, during that same stage the technical and operation teams monitored the process. Third, constant communication and on-site visits maintained behavior control. Finally, this same

control was supported by a "*good comprehension*" between the chain developer and the hotel owner.

During the pre-opening stage a "*raft of information*" was exchanged between the hotel owner and the representatives of the chain. During this step of the implementation of expansion strategy, the hotel chain worked on ensuring that the brand standards were put in place. The operation and technical team was in charge of monitoring the design, the construction, and employee training. This was achieved through constant monitoring and presence on site. Additionally, when possible, the regional offices also supported this monitoring effort. The head office participated through the legal team efforts in supporting the development of the project. As one of the respondents stated, the chain verifies what owners "*do physically with the hotel*". These procedures supported the presence of a behavior type of control.

As for output control, it was observed in the description of the operating rather than the development or pre-opening stage. The only component of output control during the development stage was for the respondents. The development director, especially the regional ones, had an incentive related to the number of deals signed. This indicated a control oriented towards performance rather than process.
When the hotel is operating, output control prevails as a control mechanism. The hotel operators are then responsible for specific performance outputs that are transmitted through the reporting system. Similarly, for the transactions between the hotel chain and the hotel owner, the control shifts to more performance-based control mechanisms.

Control costs

Monitoring costs did obviously prevail during the pre-opening stage where the behavior control was pre-dominant. Equally, more outcome control costs were incurred during the operating stage where performance control was in place.

The salaries and the number of persons in charge of controlling the process mostly determine the monitoring costs. In this case, there were two to three persons at the headquarter level supporting the process. These persons were mostly highly specialized (i.e.: lawyers, engineers, and other "*consultant type*" positions). The operations and support team included an average of fifteen to sixteen specialized persons. The number of visits and the level of effort of

the support team increased as opening approached. Additionally, one person was usually appointed on a full-time basis for the monitoring of the pre-opening and operations of the hotel. The regional director of operations was responsible for monitoring the person in charge in the hotel unit. The initial technical fee paid by the hotel owner and developer often covered monitoring costs.

Three variables determined the monitoring costs: the accessibility of the hotel, the degree of compliance with the brand, and the required human resources during the pre-opening and the opening stages. The number of visits to the hotel unit and the time spent on a specific project appeared as the two main drivers for monitoring costs. These two main indicators of control costs increased if the hotel was located in a remote area. In this case, the number of hotel visits per time period decreased, thus increasing the monitoring costs for one specific unit. Similarly, the number of visits and the monitoring efforts increased when obstacles to the compliance of the hotel operations with the brand arose. Finally, and as discussed in the section on human asset specificity, when the availability of the human resources in the location was limited, monitoring costs tended to increase.

The investment in the infrastructure of the information system and the bonuses paid to regional managers and general managers constituted the two main components of outcome control costs. In particular, the investment in the reporting and information system, its on-going maintenance, and the quality reporting system make-up most of the outcome control costs.

Other control costs

The interview revealed that the development team computed no financial opportunity cost. It was suspected that this cost was computed by the financial team. Rather, the residual loss estimates were assessed in terms of sales cannibalization. In other words, the residual loss was regarded in terms of the impact of the new hotel on other hotels in the location.

The information search costs increased as task programmability decreased. Information search costs consisted of on-site visits and background checks. On-site visits of the hotel unit composed the largest part and effort of the information search costs. Due diligence and owner background check constituted the remaining portion of information search costs. Moreover, when possible, the chain commissioned an independent market study. The hotel owner or developer

often paid this market study. Otherwise, the chain relied upon available information on the Internet, and contracted third party specialists on a contract basis. One of the respondents indicated that the chain tended to hire "*previous consultants of consultancy offices*" in an effort to reduce information search costs.

The bargaining costs differed from one region to another. These same bargaining costs, indeed, depended on the level of competitiveness in the geographical market. One respondent compared the competitiveness and attractiveness of major capital city markets such as London or Paris in comparison to other less attractive markets. In essence, it appeared that the bargaining costs were related to the nature and quality of room supply available in comparison to the number of brand operators in the market. The legal costs related to the negotiation of the contract appeared minimal in comparison to the costs related to the competitiveness of a market. Additionally, it seemed that the development team did not consider legal negotiation of the contract as a main cost because the head office was accountable for these fees.

Since the financial commitment was maintained at minimum, as the chain *"position (...) is usually a dry position and we're not putting cash or equity of any form into the dea*l", the bargaining costs as described by the TCT were almost inexistent. However, a bonding cost specific to the hotel chain development appeared in the interviews. The shared responsibility of the brand standards, by the operator, the developer, and/or the franchisee constituted a strong bonding cost in the context of hotel chain expansion. This is consistent with the literature on hotel chain expansion modes (Dev 2007). Simply put, the operator was maintained "*hostage*" (Williamson, 1974) through this shared responsibility of the brand standards. Additionally, it appeared that the degree of asset specificity of the hotel unit was a determinant of the level of bonding costs. In other words, the higher the compliance of the hotel unit with the demand of the customer base and the degree of brand competitiveness, the higher the bonding costs involved by the hotel chain in the transaction.

Elements of risk

Respondents expressed that their main concern was the image of the brand that would be delivered in the hotel unit. As one of the developers stated, his main concern was that "*Image, and that the property will be delivered and per our image worldwide and to our standards and specifications*".

Magnitude of loss

The magnitude of loss appeared to be the main concern during the first stage of development, namely during the negotiation of the deal. According to the interviewees, the financial magnitude and financial implications had to be determined at the negotiation stage. During that same stage, the concern would be over the assessment of the magnitude of the deal in order to best estimate the adequacy of the financial profile of the hotel owner or developer. The information search costs were therefore perceived as important in reducing the magnitude of loss. Once that portion of risk was estimated, the focus was then on controlling for its probability to happen.

When asked to expand on other sources of risk and their magnitude, respondents mentioned the impact of damage in one hotel on the whole brand network. The example of a food poisoning in one hotel unit and its impact on the sales of the rest of the units of the brand was put forward by one of the respondents. According to him, the higher the control over the operations, the lower the magnitude of risk of brand damage is. He stated that in the case of management, the chain could "*do something about it*".

Probability of loss

Once the amount of the deal was estimated, the main aspect of risk that remained under the responsibility of the deal is the probability of loss. The magnitude of loss was under the responsibility of the hotel owner or developer and the operator was mainly concerned with the variability in the hotel sales. Therefore, the operator concentrated their efforts on controlling for elements that might affect the probability of loss. Among these elements, the interviewees mentioned the risk of abuse and damage to brand reputation, the performance of the hotel business, and the destinations.

Finally, it appeared that task programmability was the most important element in assessing for the probability of risk. As an illustration, when asked about the probability of loss, one respondent answered: "*I guess that is why we went many steps ahead by asking for everything in place before we signed*".

In addition to the examination of the above constructs, results contrasting the growth options employed by the hotel chain were observed. The results of this comparison are presented in the following sub-section.

Distinction among growth options

Asset specificity

In relation to asset specificity, the degree of physical asset specificity was said to be less of a concern in a franchise than in a management contract. Since the hotel chain has the responsibility of managing the unit, the degree of physical asset specificity was regarded as more important. Similarly, human asset specificity was more important to the hotel chain in the case of a management contact when the chain operated the unit. In the case of a franchise, the availability of operational and the managerial competences in the destination were the priority.

Information system-base

In a franchise contract, the information is focused on sales as an indicator of performance. These indicators included revenues and occupancy measures. In a management contract further "*costs of profitability*" are added examined and exchanged between the hotel operator and the hotel owner.

Outcome uncertainty

The financial strength of the owner/developer was mentioned as the most important source of outcome uncertainty in a management contract. In a franchise contract, the application of the brand standards was considered as the main source of outcome uncertainty.

Control type

As suspected, behavior control is more present in a franchise agreement. The behavior control was observed in the use of the examination of the franchisee business plan and operational projections. "*We want to really meet and understand the key staff that they are proposing*". One of the respondents summarized the types of control over prospective franchisees as follow: we are looking for the "*right skills and right infrastructure*". The franchisee on the other hand employs a control based on outputs.

In a management contract, the General Manager and the regional offices were responsible for the outcome of the operations. The reliance on bonus compensation schemes for these managers reflected a control based on performance. As mentioned earlier, the focus of the control in a management contract was the financial output of the owner/developer. As a consequence, due diligence was more thorough in the case of a management contract.

Other control costs

Despite the lack of financial commitment by the operator, bonding costs appeared to be higher in a franchise agreement. In this case, the chain accepts to share the responsibility of the brand standards. This shared responsibility constituted a bonding cost, which was perceived to be higher in the case of a franchise.

CASE A

Case A is a publicly traded international hotel chain operating multiple brands covering more than four segments of the hotel industry. During the data collection process, the company was in the midst of its international expansion. While the Pilot Case reflected a firm with an international expansion launched several years ago, Case A represented a chain that was implementing a considerable enlargement of its international presence and entering new markets. Simply put, Case A had managed to establish its brands in existing markets and was aiming at entering new markets and enhancing its international presence.

The head of development, a regional director of development, and a headquarter-based director of development were interviewed in this first case study. The head of development is the highest person in the hierarchy, followed by the headquarter-based director and the regional director of development. The two directors of development report directly to the head of development.

The expansion strategy was constructed around three main axes: first, expansion as an operating company, second, reliance on target markets by brand type for a defined time range, and third it entrance in each country through its capital cities.

Management contracts were the predominant growth option signed by the developers of Case A. According to all three interviewees and the documents collected, Case A offered management contracts a flexible response to the demand of hotel owners of the target region. As one of the interviewees said "*It is an operator market here*. (…) *There are so many projects chasing too few operators* (in the target region)". Each of the three persons interviewed stressed the flexibility of the company in the negotiation and establishment of management contracts. According to the managers interviewed, the management contract allowed the application of flexibility in the contract that was not possible with the other growth options. In addition, contract management was presented as the most adequate option to enter a new region where the company had a limited presence. Finally, management contracts were perceived as the best option to conceal the chain's growth target within the time allocated to meet those plans. As one of the interviewees summarized it: (Management contracts are signed) "*to grow the numbers* (….) and *we are not in those countries by lease. (…) Lease is much more difficult and time consuming*".

Lease was the second growth option in the network of the chain in terms of number of rooms. However, leases were limited to established markets (i.e.: capital cities in Western Europe) and were not signed in most of the new target regions. As one of the managers mentioned, "*leases offer a way of not using your capital (...) to grow your brand and lock in good locations*". According to the interviewees, the markets sought for the new expansion plans were not adequate for the establishment of a lease. In particular, leases did not permit the delivery of the required rate of return expected from developers investing in those volatile markets.

Franchise was the third growth option relied upon by the chain in its international deployment. The company had limited its franchise expansion to master franchise agreements in the established markets (i.e.: capital cities in Western Europe). Two reasons were presented for this choice. First, the lack of available possible partners in the target regions limited the possibility of franchise in the new markets. As one of the interviewees stated "*there are no management teams* (in the region)". The poor quality of existing hotels and the limited knowledge of hotel operations in the region were not a favorable context for the development through franchise. Second, master franchises (or the signature for several franchised hotels with one operator) and not individual franchises provided a rate of return that was more coherent with the chain's expected returns.

Finally, other forms of growth options involving equity and financial participation of the firm were rarely signed. As stated by one of the interviewees, "*equity is very rare. Strategic equity maybe*". Equity participation was labeled "*strategic*" because it was employed in cases of entrance in an attractive market or had the possibility of a sale-and-lease-back. Therefore, equity participation was viewed as an "*exception*" in the development scenery. These exceptions included purchases for a sale-and-leaseback, or "*some projects where (*the firm*) might have given a loan to a project, a subordinated loan, or might have gone into small equity, or sometimes just to penetrate a growing market*".

In sum, the chain was targeting a growing region and responding to the local demand by offering flexible management contracts.

Organizational features

Asset specificity

Every hotel or hotel deal was assessed against a set of criteria that are described in this section. This set of criteria formed the determinants of asset specificity and served specific objectives. It appeared that asset specificity ensured a high room rate at early stages of operations, the long-term commercial potential of the hotel unit, and the promotion of a brand to owners.

First, a high level of asset specificity meant the capacity to open quickly and be the first mover in a market to the interviewed developers. The early implementation in a growing market combined with a long-term commercial potential "*demonstrate that (*the Chain*) can operate across the country, and will get more properties*". In essence, the case study investigation revealed that developers seek a high level of asset specificity to align the return expected from a hotel unit and the return expected from the hotel developer.

The pre-opening commitments emerged as a pivotal element in the transactions described. While described by the interviewees as a non-bonding activity, the pre-opening commitments appeared to be central in relating several constructs of interest. During this stage, the owner was responsible for a pre-opening budget; nonetheless, it seemed that the pre-opening commitment was important in the chain's expansion strategy. Pre-opening commitments were essentially made up of marketing and operation efforts. In other words, the hotel chain's efforts during the pre-opening stage were on preparing the operating processes and marketing the hotel. These efforts were estimated and accounted for in the pre-opening fees charged to the hotel owner. Billing these efforts to the hotel owner seemed to reduce their centrality in the expansion effort. However, having the hotel owner pay for the fees does not undermine the centrality of these efforts in the implementation of the expansion strategy. The level of pre-opening commitments was determined by the classification of the market of the hotel, the availability of specific human assets, and the timing of the project. Whether the hotel was in a city (primary market) or a resort destination (secondary market) determined the length of the pre-opening commitment. The following statement about a resort hotel reflects these findings: "*So for sure, the pre-opening phase will not only start, but it will start earlier than it would start for a city hotel*". Similarly, the length of the pre-opening stage also affected the availability and duration of the mobilization of specialized human assets. Simply put, the pre-opening commitments constitute the critical path of

the success of the transaction. In addition, the pre-opening commitments present a bridge between the constructs of asset specificity and task programmability. Finally, the level of pre-opening commitments is the discriminating element between growth options.

Site specificity

"*A good location? Depends for which brand*". As reflected in this reported statement, site specificity was first considered in terms of the alignment between a market and an existing brand from the chain's portfolio. Simply put, asset specificity was defined in terms of brand positioning. It appeared that the first step of alignment between the hotel deal and the strategy was the selection of a market that corresponded to an existing brand. This is the reason why site and physical asset specificity were the two components that were secured before the signature of any hotel contract. "*It's an element of the contract, otherwise, we wouldn't sign the contract*" answered one of the developers. Verifying that the hotel features were those required by on of the brands and imposed by the environment in the destination was key to a successful transaction.

In terms of the components of site specificity, the research revealed that the destination (often referred to as the market) and the site were the two dimensions of site specificity. Elements of the destination that were assessed were the hotel size, the local market coverage, and the existence of primary destinations that can feed secondary ones. This examination was often conducted at the country level, as the stage of industrialization of the economy was the main concern for developers. As for the site of the hotel, or future hotel, it was assessed for its location in the area or the market. In their study of a potential hotel unit, developers examined the possible commercial synergies between the prospected unit and existing hotels in other markets of the region.

Physical asset specificity

Rooms, hotel, and plot sizes, along with the general layout of a hotel were the dimensions of physical asset specificity. These dimensions were assessed against the specification of the brand standard when selecting a hotel for addition to the chain's network.

Due to the centrality of this specificity in the success of the expansion strategy, it constituted a key element in the negotiation and in the final contract sealing the transaction. The stakes related to physical asset specificity were to first, ensure that the hotel infrastructure would align with the

standards of the brand, and second, to ensure the delivery of the end product in a timely manner. Thus a highly specific hotel unit would be the one that is built and presents the essential standards of the brand to be implemented.

Human asset specificity

Human asset specificity was of concern for the pre-opening and operating stages of a transaction. Except for the profile of a developer, which is highly specific, no other special skill was required at the development level. At the pre-opening and operating stage, the level of experience and knowledge about the destination defined the specificity of the human asset. The number of managers with experience of the destination could, thus, be the measure for the requirements and investments related to this specificity in human skills. The central person in this specificity was the general manager of the hotel unit. His role was to align the operations of the hotel unit with the market through the monitoring of the activities.

Task programmability

As mentioned earlier, the time and effort dedicated to the pre-opening stage increased the task programmability of the transaction. Thus, the nature of the project (whether it was a new construction, a conversion project or an asset management) affected the level of task programmability. The data collection process uncovered two orientations for task programmability. Hotel chains were concerned with the planning for two aspects: the relationship with the owner and the forecasting of profits. In this planning effort, two scoring sheets were employed: one that assessed the deal and another where the cooperation with a local consultant as scored.

The main concerns about the owner were either that he might default financially or that he might interfere in the operations of the hotel. To assess each of these concerns, developers stressed the due-diligence efforts for background checks, the investment in the human relationship to “get to know” the owner, and assurance that the owner has an understanding of the components of the hotel operations. In other words, the operator placed a behavior control on the owner. As for the forecasting of profits, it emerged that allying with an owner with an existing unit in the same market, conducting a market study, and the relying on internal knowledge were

the three main efforts conducted internally to support the achievement of the required return. In explaining his confidence about a new project, a developer said "*It's a new construction project with very reliable partners who have done a lot of development on that site*". Simply put, it appeared that knowledge of the operations in the region of the new hotel were key to task programmability.

The construct of task programmability appeared to be related to three other constructs: control, outcome uncertainty, and information-base system. Controlling processes, such as committing in the design and the layout were related to task programmability. As reported from one interview "*If you can influence early on the concept and everything else, then it makes the job much easier down the road*". Outcome uncertainty is the level of threats from the external environment that will influence task programmability. The forecasting of future profits is an illustration of this finding. In their efforts to enter new markets, the developers were concerned about the factors influencing the future sales of the hotel. These concerns were related to both internal and external factors. Internal factors were related to the internal competencies for predicting the future. The following statement illustrates this point: "*You need to have the vision of thinking, especially in (*the region*), of imagining how this site will be, or how popular the site will be in let's say 5 years, 10 years, 15 years*". As for external factors, they were related to those events and decisions that were outside of the control of the hotel chain, and that are discussed below in the outcome uncertainty section.

Outcome uncertainty

As discussed above, the main component of outcome uncertainty is related to the sales of the hotel rooms. As one of the respondent said: "*The difficulties* (of the discussed contract) *are related to the destination, the marketing for the destination*." With this regard, the difficulty is in the estimate of the sales generated from the tourist destination itself that made up outcome uncertainty for the contract.

Outcome uncertainty can thus be observed in the difficulty of forecasting occupancies and rates, in predicting drastic changes in the region that will affect sales, and estimating the timing of the opening. These challenges are related to external factors such as the commitment of the government of the region to build the required infrastructures or the political stability of the region.

Information system-base

In accordance with these levels of internal and external uncertainties, behavior-based information systems were observed. Both the transmission of the information between the hotel chain and the owners and internally were mostly informal and process oriented. In the first stages (initial contact and before signature), most of the information was exchanged in an informal way through telephone conversations, emails, and meetings. During sub-sequent stages, the contract was the most formal piece of information but did not constitute the most important pat of the information in the transactions.

Overall, the information system is heavily documented. Below is a listing of the most important information exchange points between the hotel chain and the owner:

- Personal meetings with the hotel owner/developer
- Site visit
- Summary proposal
- Space plan to further discuss the concept
- Technical services agreements
- Documents exchanged between the technical team and the project managers/architects
- Emails and other correspondence to achieve the construction of the hotel
- Draft of contract
- Final contract

This list of information reports on the behavior orientation of the control and information system between the chain and the owners.

At the internal level, the information was also based on behavior, but the reliance on output performance measures was more present. During the operations of the hotel, for instance, the reliance on financial reporting systems was predominant, indicating an output-oriented information system. Equally, developers were due to report the advances of their work on a formal system, reflecting the focus on output rather than processes.

Organizational Control

Control type

The control types in the organization were consistent with the information system observed in the documents and discussed during the interviews. There were two main

transactions in strategy expansion: the transaction with the hotel owner, and the transaction between the developers and their superiors.

First the focus of control in the relationship with the owner, as mentioned earlier, was on the profile of the owner, on the construction, and on the pre-opening commitments. First, the owner's check was conducted through internal due-diligence process. Then, the control of the owner's behavior occurred during the construction stage. Also, a heavy involvement of the chain's representative and through a "*permanent and informal contact with the owner*" maintained the control over the process. It was mentioned that the higher the influence of the developer on the owner during the preparatory stages, the lower the efforts of the technical teams after the signature of the contract. This is an indication of the reliance on behavior control.

Second, the focus of the internal control is a mix of output and behavior control. The behavior control was present in the human resources policy. The following statement summarizes the evidences collected in this regard: "*There are only two ways to enter our company either through our hotel school or through acquisition*". Similarly, the existence of a project approval process reflects the presence of behavior control. Besides these process-oriented mechanisms, an output system was also in place. The targets applied to developers, the performance objectives on the operating team, and the budgets imposed on the rest of the staff are indicators of goal-oriented control.

The performance measures employed were the following:

- RevPar
- Occupancy
- GOP
- Customer satisfaction scores

These measures were controlled on monthly, accumulated basis, and forecasted basis. They were also compared against the market, previous years, and budget.

Control costs

The predominance of the behavior type of control led to the prevalence of monitoring over outcome control costs. The cost of the reporting system and the salaries of the persons responsible for the outcomes of the reporting system constituted the outcome control costs.

The monitoring costs were, on the contrary, more present. Before the signature, monitoring costs included the salaries and expenses of the development and technical teams. After signature, the monitoring costs were related to the efforts of the operations, the technical, and the development teams. Although the technical fees were the owner's responsibility, the hotel chain had to work on respecting the allocated fee. On average, the teams monitored thirty to fifty hotels a year; every hotel required a minimum of twenty visits. In the case of contracts where the owner's opinion diverged with the chain's requirements, this total number could be doubled. Overall the monitoring costs consisted of:

- Time spent by the technical team to apply the standard layout
- Management fees to cover the monitoring during the operations
- Legal control by legal team at headquarter and a clerk in the region.
- Budget meetings and discussions
- Regional controller, financial controller (approximately15 to 20 hotels/region)

Other control costs

In the case of Case A, the information search costs constituted the center of the other control costs. This was due to the novelty of most of the markets in which it was entering during the data collection process. Most of the target markets and regions were not only new to the chain, but were also not established travel markets. The level of uncertainty of the profit forecasts was high–as detailed above- inducing high information search costs. These information search costs includes market study costs, which were almost inexistent in established markets. Additionally, the fees of the local consultant who also had the role of facilitator in the relationship with the owner where also added to the development efforts. However, two out of the three interviewees pointed to the fact that these costs were minimized by the high number of hotel owners prospecting for operators in those same regions. This last element almost eliminated the bargaining costs. Similarly, residual loss estimates were seldom considered.

However, the high outcome uncertainty level in these markets increased the level of bonding costs. Despite the fact that management contracts did not bind the operator financially, other intangible bonding elements were incurred. The sources of bonding costs included the shared responsibility of the brand. In the case of Case A, who was launching its international expansion, this element was even more critical. Additionally, since reputation of the brand among

owners was key to the success of the expansion, the chain refrained from legally perusing owners for default of payment. According to the interviewees, having a lawsuit pending against a hotel owner has a negative impact of the brand image. Therefore, the chain seldom sued owners for default of payment. Not to mention the threat of cancellations, when the "*name is out and the PR machine is already working the hotel*". Also, the cancellation of technical fees in "*favor of getting the contract*" constituted an indirect bonding cost. Finally, the length of the pre-opening procedures affected the time targets of the chain and also constituted bonding costs.

Elements of risk

The following statement best summarized risk related to development activities: "*we are concerned with how much we could loose financially and in terms of credibility*".

Magnitude of loss

The above statement sums up a finding related to risk in the hotel expansion context. The magnitude of loss is not only financial but also commercial. In other words, when estimating the amplitude of the loss related to a deal, developers consider the amount of money that could be lost but also the impact on the commercial power of the brands.

The financial impact included the guarantees signed in certain clauses of a management contract but also the bonding costs that are listed in the above section.

Probability of loss

Two concerns were listed under this element of risk. First, there was the probability of losing the contract, second, the probability of not achieving the forecasted sales. As one of the interviewees responded, the first concern was essentially to "*Sign a contract that doesn't materialize*" or "(It is) *the risk is that we spend too much time on projects that don't yield and that's the hardest thing to juggle at the moment*." Having a contract that does not materialize would not only delay the entry of the brand on the market when the chain focused on "*act quickly and be on the market early*", but also incur unnecessary costs. As for the second concern in terms of probability, it was related to the outcome uncertainty related to the project. In essence, the second concern was on not achieving the forecasted returns. At the center of these concerns was the probability of not delivering the return promised to the owner.

Distinction among growth options:

Risk and risk elements in the hotel expansion context appeared higher in leases than in any other growth option. Since Case A did not plan to offer a full acquisition as a growth option, leases emerged as the most risky growth option. The commitment of the chain in a hotel through a lease was considered as riskier than equity participation for four reasons. First, the chain had a greater brand exposure in a lease than in equity participation. Therefore, the commitment to the hotel unit was greater in the case of a lease. Second, there was no possibility of sharing the operating responsibilities in the case of a lease. And finally, the lack of flexibility and high requirements of a lease prevented the firm from employing it in emerging markets where the speed of entry at speed to market was key.

Lease was listed as the growth option that required most of the information search, pre-opening, and programmability efforts. Overall, the respondents pointed to the need to carefully manage the outcome uncertainty related to a contract in the case of a lease. This point was even more important in leases where the operator was responsible for insurance, maintenance, and repairs. In sum, the lease required a focus on both the magnitude and the probability of loss.

In the case of a "*straight*" or "*dry*" management contract, the focus was mostly on the probability of loss. However, when clauses such as guarantees, thresholds, or subordination on fees were included, the magnitude of loss was considered. Probability of risk emerged as the most important concern in these cases.

CASE B

Case B is a private company that manages one brand. According to the interviewees, the expansion focus was on maintaining the consistency of the units with the brand. Case B had been through large expansion efforts during the last ten years and intended to conduct a more focused approach for its future expansion. In terms of size, Case B had the least number of hotels in its network. For comparison, the pilot case and case C had approximately 30 times more hotels than Case B.

Management contracts represented approximately 98% of the chain's entire network and were the preferred growth option for expansion. In general, the company offered a classic format of management contract comprising a basic fee and incentive fees. However, in rare instances it did sign management contracts with Gross Operating Profit (GOP) guarantee. Under the latter form of contract, Case B would engage in providing the hotel owner with a minimum GOP.

Company B did not intend to expand through franchising. As for leases and equity participation, they were sometimes employed for expansion. Leases and equity participation were signed in a few very specific instances, where the market conditions pressured such a choice. As one of the respondents described it, "*We would prefer a management contract but it is not always possible. In certain areas you have to accept a lease or you have to provide certain equity in order to retain the contract or in order to get to the contract*." Simply put, Case B as a service provider, had to adapt its offer to the market demands and conditions by offering a lease or certain equity participation.

Most of the leases in Case B had two components: a fixed fee and a percentage of the hotel Net Operating Profit (NOP) or GOP. Based on these contracts, the operator (Case B) had to pay the owner a fixed rent for the use of the property and a percentage of the operating profit. As for equity participation, it was seldom examined on a hotel basis. It would be considered for a group of hotels rather than for one individual unit.

Organizational features

Asset specificity

In company B, the level of asset specificity was determined by the consistency of the hotel with the strategy of the chain. A hotel was considered specific to the chain when it helped enhance its brand image. The synthesis of the data collection process revealed that the consistency of the strategy of brand image was based on 3 main axes:

1. Iconic hotels
2. Regular stream of profit
3. Uniformity with brand standards

In order for a new hotel to support the brand image of the chain, it had to be aligned with the three above named axes. First, the hotel had to be located in a city or resort area that could support its position as a "*trophy hotel*". Second, the hotel had to support the effort of maintaining a regular stream of profits. There were two possible ways to ensure this objective: open in a year-round location or in proximity to a hotel that had the opposite seasonality pattern. Additionally, the growth option selected for the hotel unit had to coherently support this effort of regularity in the financial streams. Finally, the new hotel unit had to present features that were consistent with the brand standards. These features could be either present in the infrastructure, or expected to be achieved through the relationship with the other party in the contract. In essence, as one of the interviewees said in describing a last deal: "*In this case, the partnership was right, the contract was right, and the location was right*".

Site specificity

Respondents provided an exhaustive list describing the components of site specificity. (Please refer to Appendices D and E). Among the features of location listed, the interviewees mentioned: the market potential for the target customer market, the level of tourism attractiveness, the regional potential for further development, the changes in the dynamics of the region or city, and the geographical location vis-à-vis other destinations.

Two main grand themes emerged from these components: first, the commercial potential of the location and second, the alignment of the features of the site with the strategic axes. In other words, a site was examined in terms of its market potential for the brand, the degree of exposure offered by the location to the brand, and the sales complementarities with other nearby units.

These three elements constituted the components to estimate the commercial potential of the hotel. In addition, the features of the location of the hotel were assessed against the three axes mentioned (i.e.: iconic hotel, regular stream of profit, uniformity with brand standards). Thus, the existence of another hotel in the region with a complementary seasonal pattern was to support the second axis of maintaining a regular stream of profits. As for the image of the hotel in the region (historically and presently) it came to support the first and the third axes.

In essence, the degree of site specificity was determined by the commercial potential of the location and the alignment of the features of the site with the three strategic axes of the chain.

Physical asset specificity

The respondents distinguished two physical aspects: the infrastructure of both the location and the hotel unit. In terms of infrastructure of the location, hotel development managers were concerned with the accessibility of the hotel. In assessing the physical asset specificity, the interviewees integrated the accessibility and infrastructure of the whole location. This indicated the lack of dissociation between a hotel and its site location. The respondents tended to mention both the location and the hotel itself in answering the questions on physical asset specificity.

The level of commitment in the hotel was perceived in relation to the time and effort spent during the pre-opening stages and operating stages. Although not explicitly mentioned, these commitments were considered in terms of monitoring efforts to be deployed in a specific hotel. This level of commitment was determined by two main conditions. First, the level of experience of the owner with the chain and its operations affected the level of commitment by the chain. When the hotel owner was already operating hotels with the chain, the latter did not have to commit at unusual levels to the pre-opening and operating stages. Second, the intensity and duration of pre-opening efforts varied with the stages of development of the project. Simply put, when the hotel was at the project stage, the pre-opening commitments were low and spread over time. Equally, when the hotel was at a takeover or conversion stage, the pre-opening commitments were concentrated in one short period of time.

This observation on pre-opening commitments indicated a series of links between the experience of the owner, the level of asset specificity, and the degree of task programmability. (This element is further discussed in the section on task programmability and in Chapter 5.)

It appeared that the degree of physical asset specificity was determined by the number and extent of modifications to be made for operational efficiency. Thus, the larger the number and the extent of modifications, the higher the degree of physical asset specificity. Moreover, the degree of physical asset specificity increased with the length of the collaboration during the pre-opening stage. The longer the time spent with the hotel owner during the pre-opening stages, the more likely the degree of physical asset specificity has of being high. Finally, it appeared that the degree of physical asset specificity differed for each type of growth option. This was probably related to the length of the pre-opening stage and modifications to be made under each growth option.

Human asset specificity

The level of specificity of a contract with the chain in terms of human resources was approached in terms of costs related to the mobilization and planning for staffing needed. The higher the number of people required for a specific hotel, the higher the degree of human asset specificity. Equally, the longer the planning for staffing took, the higher the degree of human asset specificity in that specific contract.

The local availability of qualified staff, the number of projects opened in the same region, and the stage of development of the hotel were the three elements determining the level of human asset specificities. When the chain was entering a new country, where the local knowledge in hotel operations was low, the degree of human asset specificity of this particular hotel was likely to be high. This degree of human asset specificity was likely to increase if the hotel was at the development rather than at the conversion stage.

Finally, it was stated that the specificity in human assets differed with the type of contract. In other words, the degree of human asset specificity varied from one growth option to another. In a management contract for instance, where the recruitment and the training is the operator's burden, the level of human asset specificity was likely to be higher than in a franchise.

Task programmability

Previous experiences and the involvement in the pre-opening process emerged from the answers on task programmability. In essence, if the chain had already operated with the hotel

owner or in the region and had the possibility to participate in the pre-opening process, the capacity to plan for the future transactions (in this case the operations of a hotel) was higher.

Previous experiences with the hotel owner or developer increased the capacity to plan for the details of the operations, or the level of task programmability. As one of the respondents said in relation to the hotel owner "*He knows how we function*". Not only did previous experience enhance the capacity to plan, but it also decreased the requirements for monitoring and efforts for aligning the hotel with the brand. Additionally, previous experience with the hotel owner or developer allowed assessment of his financial capacity. Therefore, past experiences with the hotel owner decreased the information search costs, the monitoring costs, and reduced the possibility of outcome uncertainty.

The existence of at least one previous or planned hotel in the region increased the level of task programmability. The planning for the human resources element was the most important element considered in this case. In a broader sense, if the chain had already operated in the region or had been prospecting the region for another unit, it was very likely that this process increased the level of task programmability of the next hotel. For instance, the chain had signed for the management of a hotel in a region where it already had one hotel under development. Thus, the chain could use its knowledge of the region to plan for its need in human resources and other resources required for the management of the hotel.

The involvement of the chain during the early stages of development of the hotel constituted the second determinant of task programmability. As one of the respondents mentioned, when the chain is involved from the renovation stages the hotel deal became "*Very structured, we know at which point in time we will start, we know at which stage we have to be there*." This implication could be limited to the participation of the future General Manager (GM) of the hotel in the renovation stages.

In answering the questions on task programmability, the element of "*trust*" was often recurrent. While the role of trust varied from one growth option to another, its relationship to task programmability was consistent across the answers. Trusting the other party after past successful experiences increased the level of task programmability and thus decreased the monitoring costs and the level of outcome uncertainty. Trust also allowed the transfer of the level of task programmability to another transaction that has been introduced by a known and trusted partner.

Having trust in the relationship was perceived to be most important in the case of the management contract in comparison to a lease or an equity growth option.

Outcome uncertainty

According to the respondents, the accuracy of the estimates of the amount of fees to be earned determined the certainty of the outcome. The fees to be earned were perceived as determined by two factors: the coherence of return expectations and the time and effort devoted in estimating the amount of fees to be earned. In other words, the coherence of the return expectations and the effort devoted to estimating the amount of fees to be earned determined the level of outcome uncertainty in a hotel deal.

For the outcome uncertainty to be reduced, the respondent believed that the future demand for the hotel should be carefully assessed. More importantly, the key to the estimating of the outcome of the contract was the coherence of the return expectations. In particular, the coherence (or alignment) appeared to be important between the hotel's commercial potential, the selected growth option, and the expected return on the property. If any of these components was overlooked, the level of outcome uncertainty increased. For instance, if the level of expected GOP did not correspond to the type of hotel operated (in terms of segment and products offered), it was likely that the level of outcome uncertainty was to increase. In the case of a management contract, the alignment between the outcome estimates and the return expectations could be enhanced with the owner's understanding of the components of a management contract.

Time and efforts spent in estimating the future stream of fees from a specific hotel also appeared to determine the level of outcome uncertainty of a contract. Essentially, the time available to the chain, the effort allocated to the financial planning, and the role of the person who determines the figures affected outcome uncertainty. As one of the respondents said in response to the determinants of the outcome uncertainty: "*it depends (...) on the amount of time, the number of resources, (....) and who ran the figures*". Since time and effort had an impact on outcome uncertainty, it appeared that other tools were employed to assess the expected returns of a hotel contract. Among others, it was observed that city comparison was often employed in assessing the uncertainty of a deal. In explaining the assessment of the level of uncertainty of a hotel transaction to the researcher, each respondent compared a city to another to illustrate his/her process of estimate. In addition to city comparison, the stability of the country where the hotel is

located was also used as a proxy for the assessment of the volatility of the expected returns. Finally, the respondents pointed to the financial participation (bonding costs) of the other party as a third proxy for the assessment of the uncertainty related to the expected returns of the hotel.

Information system-base

The respondents made a clear distinction between the internal information systems (between the headquarters, the regional offices, and the hotel units) and the external information channels between the chain and the other parties (hotel owner and developer). The latter were essentially behavior-based, while the former relied more on performance-based information.

Communication with the owner was predominantly behavior based. When asked about the information system used to communicate with the owner, one respondent said, "*we meet on a very regular basis. (...) We have a very open communication (...) be it on the phone, on personal meetings, planned or non-planned*". As for the critical information exchanged, respondents mentioned the profiles of the GM and the pre-opening budget as the most important information presented to the owner at the development stage. From the perspective of the chain, the bank loan documents of the owner, the feasibility study, the FF&E listings, and the hotel master plan constituted the information provided by the owner to the chain. These indicated the focus on the process rather than on the outcome of the information that was exchanged between the chain of Case B and the hotel owners.

Internally however, the reporting system, the intranet, and income performance were more prevalent. Process-based information systems were in place such as the "*constant contact*" with the GM of the unit, performance based information was cited in relation to internal communication.

Organizational Control

Control type

The respondents clearly distinguished three stages when answering the questions on control. They differentiate the prospecting period ("*prior to signature*"), the pre-opening or developing phase, and the operating stage.

During the prospecting period, the owner was controlled on his financial situation, previous hotel operations, and his reinvestment propensity. The focus of this step was the insurance that the hotel owner had the financial capacity to sustain the operations of the hotel.

This point was discussed above in relation to organizational features and task programmability in particular. During this first step, the information was based on processes and thus the control was essentially behavior oriented.

During the developing and pre-opening phase, the stage of development of the hotel determined the degree of possible behavior control. In describing the control mechanisms in a hotel project, one of the respondents stated: "(*the hotel is*) *under development, so we have the ability to put in all our brand standards*". As discussed earlier in the section on task programmability, it appeared that the participation in the development stages of the hotel increased the reliance on behavior control. Additionally, the monitoring effort of the technical team was predominant at that stage (i.e.: site visits, plan approval, close contact with future GM, study of owner's strategy plan, pre-opening budget, and monitoring of the opening).

Finally, during the operating stage, the chain controlled the quality of the operations and ensured that the owner did not intervene. In either case, for the control of its internal employees or the hotel owner, the reliance was on behavior control. Indicators of behavior control were the insistence of the respondents to develop a "*close relationship*", an "*open communication*", or "*trust*" with the hotel owner. Internally, the performance of the hotel was examined in terms of "*people management*" and "*quality*", two process oriented control mechanisms.

Output control was found in two relationships: in the control of the chain by the owner in a management contract and in the hierarchical control within the chain. In a management contract, the hotel owner had specific expectations with regard to return and thus controlled for the performance of the chain in the hotel. In particular, the owner had specific sales and GOP targets (determined in the budget). Thus, in a management contract, the owner had little say in the process but exerted his power on the output. Simply put, in a management contract the operating chain handled the behavior control. As for the output control, the owner directed it. The fees and the investments in FF& E were the two most important performance measured in a management contract. In terms of behavior, the operator in turn was focused on the management of people and the quality of operations.

The second setting for output control was internal. As previously discussed in the section on information-base systems, output was controlled internally at the unit level. In particular, the GM of the hotel was liable for fees to the regional director, who was in charge of reporting to the

headquarters. The reporting system produced financial outputs such as the month-end results, the departmental revenues, the occupancy rates, ratios, and budgeted fees. This information served the forecasting, planning, and budgeting purposes and indicates the reliance on output control internally.

Consequently, it was observed that behavior control was the predominant form of control in the relationship between the chain and the hotel owner. Within the internal mechanisms of the chain, both behavior and output control were in place. As one of the respondents summarized it: "*In fact, one might say that the quality, the performance, and the people management in a hotel are the three major components of an open hotel*". Thus, two out of the three elements are process oriented, indicating the dominance of behavior type of control. Nevertheless, the chain considered the GM as neither a "*glorified guest-relation manager*" nor an "*administrator*", but rather as an entrepreneur. This revealed that the responsibility of the GM was increasing and strengthening the output control mechanisms in the internal operations.

Control costs

Technical fees represented most of the monitoring costs related to the prospecting and development fees in a management contract. The cost of the development team was not mentioned as it was fully integrated in the headquarters' expenses. The technical fees were covered during the pre-opening stage and were computed as a fixed fee per room. The technical fees were made up of site visits, plan examination, and development control. On average, the development team monitored fifteen contracts a year. The pre-opening fees were made up of the salaries and expenses of the GM and other officers in place, the marketing representative, and other costs related to the pre-opening team. The latter was often composed of expatriate managers whose role is to ensure the implementation of brand standards.

The GM or regional manager's expenses constituted the costs of behavior control during the operating period of the hotel. On average, there were five persons regionally in charge of monitoring the performance of a group of hotels.

The synthesis of the collected data revealed that the monitoring costs were likely to be higher when the market is unknown. This point was also revealed in the questions on task programmability. Similarly, the questions on control confirmed that monitoring costs were likely to be higher when the local knowledge of hotel operations was limited.

With regard to outcome control, it was revealed that the cost of the owner control on the operator was mainly legal. In fact, most of the components of performance control were covered in the contract. Thus, the outcome control costs consisted of the legal costs related to drafting the contract. In Case B, most of the contracts were drafted internally. When specific cases arose, a lawyer was commissioned on a case basis.

The investment in the reporting system and its maintenance constituted the cost of controlling for the performance of the hotel unit.

Other control costs

Residual loss estimate:

The estimates of residual loss were seldom considered. The assessment of the opportunity cost as defined by financial theory was not employed. Rather, the notion of residual loss appeared to be considered in relation to competing brands. The interviewees perceived the opportunity cost in terms of competition in a specific market. The reasoning is in terms of presence or absence from a strategic market and the possible opportunity of entering this same market. This possible residual loss was factored in the decision to sign but was not accurately estimated.

Information search costs:

Two types of information were related to the management of the expansion strategy: the owner and the location. In other words, in the decision of implementation of the expansion, development managers were required to collect information on the owner (due diligence or owner's check) and the location (for demand and revenue estimates). Thus there were two main types of information search costs: the costs of due diligence and owner's check and the cost of data collection on the location. The cost of due diligence was sometimes left to the owner who was responsible for commissioning a third party. The examination of the financial situation, the owner's track records and visits to the other operations constituted the cost of the owner's check. The owner sometimes carried the cost of data collection about the location, but this was less often.

The information search costs were reduced when there was a common third party in the negotiated deal and when the "*reputation*" of the region as a tourism destination was established.

Bargaining costs:

The legal process constituted the first main components of the bargaining costs. According to the interviewees, the legal process took on average six to eight months. However "*typically, the longer it drags on, the less likely that it's going to have actually serious prospects*". In other words, the higher the bargaining costs, the less likely a contract is to be pursued.

The synthesis of the data collected revealed that the bargaining costs were very closely related to the level of competitiveness of the market. When the hotel chain attempted to enter highly competitive markets (the examples of Paris or London were provided), it was likely that the bargaining costs were to be higher.

Bonding costs:

Bonding costs in a contract were likely to increase with the existence of other contracts with the hotel owner, or when the owner's priority clause was concealed, or when the responsibilities for meeting the settled targets were not shared.

When the chain was signing a management contract with a hotel owner with whom it had already had operating contracts, the bonding costs were higher. The presence of other hotels increases the dependency of the operator on one hotel owner, which corresponded to an increase the bonding costs of the transaction. Similarly, the concession of the owner's priority constituted an increase in bonding costs. Finally, when the hotel owner agreed to share the responsibility of a mitigated performance, bonding cost was likely to be decreased.

Elements of risk

Magnitude of loss

The respondents distinguished between the two elements of risk but named them the "*financial risk*" and the "*brand risk*", respectively. The financial risk was presented as related to the amount of estimate, the "*that's actually a number*", and constituted the magnitude of loss related to a decision.

The growth option type determined the magnitude of loss. Therefore, full equity participations or leases were considered as the growth options where the magnitude of loss was of most concern. The management contract was considered as the growth option where the magnitude of loss was less of a concern.

Finally, it was observed that when the location of a hotel was highly visible to the targeted customers, the magnitude of loss was considered to be higher. In other words, if the hotel (under any type of contract) was located in a highly visible location, the magnitude of loss would become key in the management of risk related to the transaction.

Probability of loss

The second type of risk presented the other determined element of risk. When discussing brand risk, one of the interviewees said "*the minute you start deviating from the standards and quality in one hotel*" the chain incurs the brand risk. Thus brand risk was actually referring to the probability of loss associated with a deal. The probability of loss was considered as important but difficult to assess. As one of the respondents summarizes it: "*image is more difficult to estimate and equally, if not more, important*".

The probability of loss was examined in conjunction with the magnitude of loss. Particularly, when describing their examination of risk, the interviewees mentioned that their focus on the probability of loss increased as the magnitude increased. Additionally, the probability of loss appeared to be related to the financial viability of the partner. If the selected partner was not financially viable, the brand perception and image could be harmed as the operations in the hotel deviated from the brand standards. Thus, limiting the information search costs, the behavior control costs or the bonding costs appeared to increase the volatility of the expected returns and thus the probability of loss.

These results on the management of risk in the hotel expansion context are coherent with research on management but deviate from the financial body of knowledge. Thus, both magnitude and probability of loss were considered together in the estimates of the risk in a transaction as suggested by both research on management and finance. However, the way managers estimate each element of risk (magnitude and probability) differed from one contract to another.

In essence, the dual aspect of risk was confirmed in the answers to the interview questions. Both aspects were highly related and considered in conjunction to each other. While the magnitude of loss appeared as the highest concern for the respondents, the probability was also considered as key. However, since the determinants and the estimates of the probability of loss were more difficult to assess, it was considered after the magnitude of loss.

Finally, it was observed that in a management contract, the probability of loss made up the risk. As for a lease or equity contract, the magnitude of loss was the first concern as the obligation on the amount due was more present. One of the respondents resumed this obligation by stating: "*if you can't pay your lease, the owner of the building won't ask where the money is coming from. We have to deliver the rent*".

Distinction among growth options

Case B relied on management contracts for its expansion strategy. Therefore, only management contracts were signed at the time the interviews were conducted. This had made it difficult to contrast the different types of growth options. The last interviewee, however, was negotiating both leases and management contracts. For that reason, the results reported below are essentially derived from the last interview.

Asset specificity

The fact that the hotel was located in a targeted market (or strategic market) was present in both management and lease contracts. It was the main variable constituting the construct of asset specificity. Simply, when the hotel was located in a strategic market, its degree of asset specificity had passed the threshold of acceptability in the process of decision-making. Then, if the physical attributes (i.e.: architecture, design, size of rooms, nature of other services) of the hotel unit presented consistency with the brand standards, the degree of asset specificity of the hotel increased. In other words, the higher the number of physical attributes that corresponded to the brand standards, the higher the degree of asset specificity from the base level determined by the location.

Next, the higher the level of asset specificity, the more likely the hotel chain was to consider other growth options than management contracts. In these cases, the negotiating power of the hotel chain was decreased and had to adapt to the demands to the hotel owners and developers. As the last interviewee clearly stated when explaining the choice of a lease: "*The (lease) contract in itself was required in order to have the hotel*". In sum, the level of pre-commitment was related to the degree of site specificity and, to a certain extent, physical asset specificity.

Finally, human asset specificity was examined from the angle of planning and implementation. It wasn't taken into consideration as a determinant factor in the decision to sign for the hotel, in neither management nor lease contracts. There was no particular distinction between managements and lease contracts in terms of human asset specificity. In both cases, the hotel chain was required to operate the hotel and was thus in charge of planning for the staffing requirements.

Information system-base

The basis of the information system did not significantly vary from a management contract to a lease contract. In both cases, the process of information exchange was maintained informal and based on a previously agreed upon contract. The frequency of contacts between the hotel chain and the owner in a lease was lower than in a management contract. Finally, the clauses on physical (i.e.: building) alteration and responsibilities were what distinguished a lease from a management contract.

Outcome uncertainty

The level of outcome uncertainty was the same for leases and management contracts. According to the interviewees, an increase in the commitment did not necessarily mean a change in the acceptable level of outcome uncertainty. A little nuance was however observed: the level of outcome uncertainty was less of a concern in a management contract where both the hotel chain and the hotel owner shared the performance responsibility.

Control type

The types of control employed during different stages of the hotel were described above. The interviewees distinguished between the stronger obligations of the lease payment in comparison to the fees reception. The nature of the compensation for the hotel chain affected the control types involved in each contract. In the management contract, the remuneration of the hotel chain was its management and incentive fees. Lease, on the other hand, was very similar to the ownership of the property, where the remuneration of the chain was based on what was left after the payment of the rent. The nature of these payments affected the relationship between the hotel chain and the owner. Therefore, the control between the hotel chain and the owner was

different in each contract. Simply, in a lease contract, output control by the owner was the dominant type of control. In a management contract, output control was also essentially employed, but some degrees of behavior control were also found.

Other control costs

The lease payment (or the rent) constituted a bonding cost for the hotel chain. This bonding cost was determined by the degree of site specificity of the hotel location. In a management contract, the bonding costs were based on the strength of the bond between the hotel chain and the hotel owner. In describing the downside of management contracts, the interviewee said: "*If the relationship goes sour in a management contract, it has much more of an implication in terms of operations compared to a lease contract*". Therefore, in a management contract, bonding costs existed for both the hotel chain and the owner. In contrast, in a lease, the bonding costs were higher for the hotel operator and the owner.

According to one of the interviewees, signing several management contracts with one hotel owner constituted a source of risk. This indicated that bonding costs determined the level of risk in a management contract.

Finally, in terms of risk and determinants of risk, the interviewees stressed the importance of non-intervention of the owner in a management contract. According to them, the most important concern in a management contract was ensuring that the owner would not intervene in the daily operations of the hotel.

CASE C

Case C is the largest of the four chains examined in this study. It is the largest in terms of international presence, or number of rooms, of hotels, and brands offered. Together with the Pilot Case study, Case C is a major publicly traded organization in the hotel industry. The Pilot and Case C, however, do compete in different segments of the industry. Contrary to Case A, Case C has been a large player in the international arena for several years now and it is focusing on sustaining its expansion. Case C already has one of the largest networks. During this study, the company was planning on further expanding with an increase of 20 to 25% of its network within a 4 year-period.

One element emerged from the data collection process on Case C. The presence and integration of a financial approach to the implementation of expansion prevailed in the data collected. The determinants and components of the expansion strategy were very much articulated and integrated with the financial imperatives. Moreover, the reliance on business plan layout to formulate and implement the chain's expansion strategy appeared to support this approach to expansion.

At the corporate level, all growth options were considered. However, Case C, like all the players of the industry, has focused its expansion on operating activities rather than real estate profits. Simply put, the expansion strategy in Case C did not include extensive extension through ownership. Rather, management contracts were the most commonly offered growth option.

According to the interviewees, the choice of growth option was based on value creation criteria. "*Depending on the country, depending on the product, the product positioning, we may have different approaches*". In practice, Case C worked on selecting the growth option that permitted the alignment between the market demand of a brand and the request of the owner. In essence, the growth option offer was considered against return expectations of both the owner and the hotel chain. The return expectation of the hotel chain was in turn assessed against the market potential of one brand of the portfolio. As one of the interviewee summarized it each growth option "*has a special profile for value creation and return profile*" and they attempted to align this profile with the market conditions.

Expansion via franchising was considered in Western established markets. The main reason for this choice was because established markets insured both a stable stream of room

revenues and the presence of franchisees with hotel operation knowledge. To cite one of the interviewees, franchises required "*reliable partners*" with hotel operation experience that could ensure a "*good adherence to the product*". This reliability was mostly observed in economically established Western markets "*where good professionals exist, where there are hotel professionals*".

The price of the lease ("*if the market leases are affordable*") and whether the lease proposed by the owner was fixed or variable, were the two determinants of the decision to lease within Chain C. According to the interviewees, the price of the lease was related to the economic life cycle along with the situation of the real estate market at a given point in time. Also, according to the persons interviewed, the conjuncture at the time of the data collection was favorable to hotel chains. Hotel chain C appeared to adjust to the first determinant (price of the lease) with the length of the contract. As for the alignment with the structure of the lease (variable or fixed), it was achieved with the selection of the brand from the chain's portfolio. "*We will consider leases or company owned hotels in the regions where we have good visibility and a sustainable situation or stabilized political and economic situation. Then the differentiation will be brand by brand".*

Full equity participation (or full ownership) was seldom considered. Rather, minority participation with a long-term management contract was employed. Only Case A made the same use of this growth option. Out of the three persons interviewed for Case C, two mentioned relying on minority participation as a growth option. The decision of whether to participate in a project through equity was decided at the corporate level and communicated to the development team through the strategic business plans. The list of countries where equity participation could be considered as a growth option was presented in these strategic plans and put together at the corporate level.

According to the interviewees, one of the advantages of the minority participation is that the Chain had "*a say*" in the project and can, thus, leverage its influence through its minority participation. But ultimately, the purpose of equity participation was to initiate a larger scale of development in a target region. Or as one of the interviewees answered: "*If you take the risk (*equity involvement) *it may open the door for larger markets".* In essence, the decision to invest equity in a project was examined with regard to the expected return on invested capital. In

practice, this translated in that "*equity participation is considered especially in segments where returns are higher*".

Most of the deals signed by the interviewees in a given period were management contracts. According to the developers, management contracts were about brand management. Or as one of them said "*if you convince the owners that you are the right brand, you will have more customers*". Simply, management contracts were perceived as a mean to develop the brand exposure through the increase of the chain's network.

Organizational features

Asset specificity

Two main themes emerged from the data collection process with regard to asset specificity in the case of hotel chain C. First, a hotel that offered a forecasted return on invested capital (ROIC) or the "*earning capacity of the project*" corresponding to the strategic plans of the chain was considered as highly specific. (ROIC is obtained by dividing the total amount gained from a transaction by the total amount invested in the same transaction.) In addition, the asset specificity of a hotel unit for chain C was higher if the hotel permitted the alignment of both the chain and the partner's expectations for the hotel.

Within this approach to asset specificity, other types of specificities (site, physical, human asset) are dimensions contributing to the overall asset specificity of the deal. Simply, the site, the physical asset, and the human asset specificity are dimensions of the alignment between the ROIC and the chain's strategic plans.

Site specificity

The ROIC estimates for a specific project included the forecasts, the future cash flows generated from operations, the value of the property appreciation (in the case of equity), and the ROIC over the life cycle of the investment or the timing of the project. Data analysis revealed that these variables determined the asset specificity of the hotel unit to the chain.

In particular, the potential of the travel market in the country was perceived to have an impact on the stability of the future cash flows. The destination attractiveness and the existence of several travel markets within one country were assessed for their impact on the future streams of cash flows. Similarly, the location was examined for its impact on the potential profits of the hotel unit. In essence, the potential of the travel market in the country and the destination

determined the degree of site specificity. Within this approach to asset specificity of a hotel deal, site specificity permitted the achievement of the ROIC of the strategic plan. To paraphrase one of the interviewees, the site was examined in terms of the "*return available for the risk taken*". Therefore, a risk-return profile in a location that corresponded to the one targeted by the chain represented a high degree of site specificity.

Physical asset specificity

Data reduction process revealed that physical asset specificity was the factor that allowed the hotel chain to respond to the demand in the selected market. While the interviewees referred to the brand as the "*product*", the physical infrastructure of the hotel did constitute a fundamental component of that same product. The brand was actually the bundle of products and services offered to the market to achieve the targeted returns. As a result the brand guided the level of standardization of the product offered. The physical aspects such as the number of rooms, the features in the rooms, the number of restaurants and meeting rooms, constituted key elements of the product. These physical elements constituted the offer of the chain to the selected market.

The technical assistance has emerged as the process allowing the realization of the physical aspects related to the product. The technical assistance was used as means of control to ensure that the end product presented the physical features to respond to the targeted market. In addition to the need for collaboration during the technical assistance stage, the ability to construct on time and within budget were also important determinants of the specificity of the physical aspect. First the ability to construct on time ensured the entry of the product at the announced time. Second, the respect of the budget limited the cost incurred for the construction. These two imperatives constituted a first step towards the achievement of the required ROIC.

Human asset specificity

The interviews and the data reduction process revealed that human asset specificity in the case of hotel expansion strategy was found in both the internal and the external transactions of Case C. Internally, the requirement of a unique profile for the team involved in development reflected a high degree of human asset specificity. Externally, the need for a specific profile for the partner in the transaction also revealed a need for a high level of human asset specificity.

First, internally, the required team included developers, operation members, and technical staff. The development task required a complex set of skills that was said to be difficult to find. Operations were the essential core competency of the chain. Not only was the operations staff operating the hotel, but also its experience and knowledge was valuable for the establishment of the forecast for the hotel unit. Finally, the technical team had to be knowledgeable about construction but also about hotel operations. The cooperation between these three teams appeared essential to the success of a hotel transaction. Therefore, the data revealed that training was essential to the success of a hotel deal.

One of the interviewees, distinguished between two types of developers: "*we have on the one hand the franchise and the management contract and on the other hand the lease and the ownership*". The first set of developers required a more commercially oriented set of skills. As for the second type of developer, he had to be more of the "*buyer type*" whose financial skills had to prevail.

Second, the interviewed developers mentioned the difficulty of mobilizing expatriates for specific countries as a key difficulty encountered in the case of human asset specificity. To illustrate, one of the interviewees mentioned about his region: "*it can be complicated to hire the staff who is prepared to go there, who will be able to live in the country and do a good job*".

Finally, externally, the hotel chain needed a specific profile for its partner in a hotel transaction. One of the interviewees has summarized it as follow: "*One of the key factors is to make sure that the owner is really confident that C has the hotel expertise the know-how and is really designing a project which is acceptable for the country. Second, make sure that the owner (...) will comply with the provisions, not only the financial ones, but all the provisions of the contract*. (…) *And that the owner will not interfere in the day-to-day management*". In essence, a partner with the required financial and technical capacity and with common past experiences increased the level of human asset specificity of the transaction. In the case of a management contract, the non-inference of the owner in the hotel daily operations of the hotel was another dimension of the external human asset specificity.

Pre-opening commitments

The overall investments for the pre-opening efforts were made at the corporate level. Most of this investment was dedicated to the promotion of the brand. Pre-opening commitments varied

with the brand, the location, and were also a distinguishing element among growth options. In other words, pre-opening commitments varied with the growth option but also with the degree of asset specificity of the hotel unit. In particular, the higher the asset specificity, the lower the pre-opening commitments. The equity participation required longer and higher pre-opening efforts, followed by management contracts, then leases. Franchising was the growth option that required the least pre-opening efforts. The standards and procedure documents attached to a franchise allowed the reduction of the chain's direct involvement in the pre-opening efforts. In addition, the data reduction process revealed that the lower the pre-opening commitment, the lower the monitoring costs for a specific hotel.

Task programmability

Four components of a hotel transaction were essential to plan for. In particular, the developers of the hotel chain had to be able to forecast for a. the room rates, b. the occupancy, c. the food and beverage (F&B) revenues, and c. the operating costs. According to the interviewees, these were the four critical outcomes to plan for. These four elements were, therefore, examined in both the strategic plan at the corporate level and the business plan of the hotel unit. At the corporate level these forecasts were made by brand and by country. The forecasts at the unit level were an extension of these corporate estimates.

The daily operations of the hotel constituted the supporting tasks to achieve the required room rate, occupancy, F&B revenues, and operating costs. In addition, the due diligence of the prospecting developer and the effort of the sales and marketing team further support the achievement of the corporate goals. These supporting activities not also supported the implementation of the expansion efforts but also allowed for the planning of the future tasks to perform.

Task programmability was therefore affected by the rigor of the due diligence conducted by the development team. The examination of the market performance, the sources of financing, and the capabilities of the future partners were presented as the key elements permitting task programmability. In other words, the better the assessment of the specificity level of the asset (through its site, physical, and human asset specificity), the higher the level of task programmability.

Outcome uncertainty

Variables that reduce the capacity for task programmability were presented as the dimensions of outcome uncertainty. In other words, any variable or possible event that could prevent or adversely affect the forecasts on market performance, the sources of financing, and the capabilities of the future partners were listed as sources of outcome uncertainty for the transaction. In particular, the interviewees listed the stability of the events in the country (either economic, legal, or political) and the likelihood of improvement in the infrastructure of the destination as the two main events that could affect the outcome uncertainty of the deal.

It was revealed that the level of outcome uncertainty increased in non-established markets, where the demand was increasing due to the economic boom of the region. This uncertainty was related to the difficulty of forecasting the pattern of evolution of the economic development of the region.

Information system-base

The chain's intranet, emails, and telephones were the three most relied upon information systems. Both the emails and telephones were used either internally or externally to monitor the evolution of a project. Simply put, behavior rather than outcome control information systems were employed for the expansion efforts. According to one of the interviewees "*80% of the job is done by emails*" and the documents exchanged were "*mostly technical documents, rather than legal*". These documents consisted of drawings, plans, and technical service agreements. The contract bounding the hotel chain and its partner was the pivotal legal document of the transaction. In sum, process was the key focus of the information system.

The intranet allowed the reporting for outcomes, but the process control prevailed in the elements to report for in the process. The chain had "*2 electronic databases: one for the management contract and franchise contracts and another for projects where C has a financial commitment.*" In other words, in a more formal information system, the distinction was made between those growth options requiring equity and those that did not. The process, nevertheless , remains the center of the information system, reflecting the presence of a behavior-based information system.

Beside the information exchanged between the hotel chain and its partner (a hotel owner or an investor), the information search in a new market was also discussed. These information search costs are further discussed in the information search costs section below.

Organizational Control

Control type

In alignment with the prevalence of behavior-based information system, behavior control appeared as the predominant form of control in Case C's expansion strategy. Behavior control was present in both the external transactions (with the chain's partners) and in the internal transactions (developers with the rest of the chain's members). First, in the external transactions, the focus was on the partner's profile and his relationship with the developers, which are indicators of behavior-based control. Second, in the internal transactions, the centrality of the assistance provided by the monitoring team, the reliance on an analysis grid, and the implementation of policies indicated the use of behavior rather than output control in the organization. Again, the fact that equity investment, and not outcomes, was the distinction among databases reflected the focus on processes rather than outcomes. As one of the respondent mentioned "*there are two databases: one for the management contracts and franchise contracts and another for projects where C has a financial commitment*". Finally, the distinction among growth options was not based on the outcome, but rather on the process. In describing the monitoring process of a new unit, one of the interviewees said: "*it depends, if it's a project with investment, we are or I am with my team following the project at an early stage. When it is a management or a franchise, we are really checking at later stages, unless it is a specific project*". Therefore, behavior control was the predominant type of control in the expansion efforts of case C.

Output control did not prevail, but was nonetheless employed in the expansion strategy of Case C. The data reduction process revealed that because of geographic dispersion of Case C, control tended to shift from behavior to a more output oriented type of control. In particular, when new units were located in less accessible regions, output control tended to be more relied upon. In addition, it emerged that output control permitted the company to store and analyze information, which was in turn used to improve its processes. As one of the interviewees mentioned, performance measures were analyzed and the conclusions were presented on a regular basis to the chain's developers. Simply put, output control also served learning purposes for the organization.

Revenues, operating and maintenance costs were the three results controlled for in the expansion efforts of the chain. The monthly and yearly figures were used to assess the firm's

performance. Planned and actual data were compared "*We look at what we have planned in terms of costs and in terms of results initially when we have validated the project. We compare what was planned with what has happened*." The comparison served not only control but also learning purposes. The results of the analysis were used to review the expansion and the strategy plans developed at the corporate level.

Finally, management contracts presented a distinctive feature in comparison to the other growth options. The legal obligation of the hotel chain to prepare a budget and report its performance to the hotel owner enforced the use of output control in the transaction. Other types of outcomes prevailed in management contracts. Capital reserves for expenditures and renovation (Capex) and provisions for working capital were also mentioned as central elements for control. These were intermediary outcomes, but were nonetheless considered as performance measures by the interviewees.

Overall, the interviewees perceived the control of a joint venture partner as the most important but also most difficult type of control. This control tended to be even more complicated if the association was planned to last and the other partner was not from the hotel business. This last observation reveals that the higher the degree of human asset specificity, the lower the need for control and especially behavior control.

Control costs

The reliance on behavior rather than on output type of control leads to the dominance of monitoring costs over other types of control costs. The cost of the information system reporting on the information within the network constituted most of the costs related to outcome control. Monitoring costs, on the other hand, were accounted for in the expansion efforts.

In particular, the costs of monitoring related to a new hotel unit were assessed against the expected revenues in the estimates of a deal's ROIC. In other words, monitoring costs were factored in the earning forecasts of a hotel. The monitoring costs included the travel expenses (in the least accessible regions, these were billed to the owner in the case of a management contract), the number of persons required on site (on average 2 to 4 persons), the training requirements of the location, the number of expatriates needed in the hotel, and the monthly meeting to monitor the advances as well as the operations.

Monitoring costs varied across growth options. As mentioned earlier, in the case of a management contract, most of the monitoring costs are billed to the owner. Thus, the technical efforts to control for the construction were included in the technical fees. Equally, the commercial and operational efforts were included in the pre-opening budget paid by the owner. And finally, in the case of a non-accessible destination, the owner paid the travel expenses. However, no compensation was accounted for the extra time dedicated by the support team to one project at the expense of another. Simply put, the monitoring costs related to the reduced efficiency of the technical team were not factored in. In joint venture agreements, additional monitoring costs were observed. In most joint ventures, the interviewees mentioned the need for appointing a person to monitor the relationship with the partner and ensure the enforcement of the chain's rights in the partnership.

In a more theoretical perspective, it emerged that when the task programmability was high, behavior control was possible at minimum monitoring costs. In this case, outcomes are clearly defined and overall control costs are maintained minimum. Also, it was observed that the higher the asset specificity, the lower the monitoring costs. Finally, outcome control could support the learning process of the chain, increase the chances of successful transactions, and in turn reduce the overall monitoring costs.

Other control costs

Like in the other chains examined, the estimates of the residual loss were not factored in the development efforts of Chain C. The three persons interviewed appeared skeptical with regard to the notion and admitted not considering this element. As one of the interviewees summarized it "*No, we know that there is an impact. (...) We are much more pragmatic, and we don't want to spend more money in a study that will not really bring us much*". In essence, the developers interviewed in Case C doubted the possibility of computing such a loss and did not consider it a priority. When such a loss was considered, it was from a commercial perspective. In other words, when developers were prospecting for a hotel they examined its potential impact on the sales of nearby hotels. Overall, what developers were concerned about was mostly the "*capacity of absorption of the market*".

Information search costs were found to be higher in joint ventures than in a management contract. In essence, the higher the risk involved (in terms of magnitude of loss), the higher the

information search costs. This increase was the consequence of longer and more in-depth investigations about the potential partner. In the case of leases and franchises, information search costs were limited to a track record of the future partner from a maintenance and operating perspective. The data reduction process revealed that the level of information search costs tended to be reduced with the experience of the development team. Due diligence processes constituted the most important part of the information search costs. Therefore, the deeper the due diligence, the higher the information-search costs. More in depth due diligence was required in the case of a joint venture, which mostly corresponded to the entrance in a new market. Very often, case C appointed one person in the new market to collect the information or had special contacts with their country's embassy in the region.

The analysis of case C revealed a relationship between bargaining and bonding costs in the hotel chain's expansion strategy. First, bonding costs were mainly constituted of the fund introduced in a joint venture and the investment made in previous contracts with the same partner. Future possible projects with the partner also appeared to constitute bonding costs. Simply put, bonding costs were not just the money invested in the partnership but also any past or future transaction that was or would be signed with the same partner. This was even more important since Case C signed joint ventures attached to multiple long-term management contracts. Second, bargaining costs appeared to be reduced when the hotel chain entered a deal with a partner with experience and knowledge of hotel operations. In other words, the more experience of hotel operations the partner had, the lower the bargaining costs for Case C. Simply, the partner knew about the steps of the relationship through his past experience, and Case C had to disburse less efforts in bargaining. This revealed a relationship between bargaining and bonding costs.

Elements of risk

The following statement, which was made by one the interviewees, resumes the approach to risk of Case C: "*Risk is related to the level of stabilization of the political, financial, and legal environment*". This statement reflects the focus of developers on the dominance of probability of loss as a risk element in expansion strategy. The fact that the interviewees focused their attention on degrees of stability, or likelihood of unfortunate events to happen reflects the dominance of the probability of loss rather than its magnitude as a risk element.

More than the magnitude of loss, the next element that was factored in Case C's management of risk is the variable of time. Within their value creation approach to expansion, developers at Case C viewed time as an important element to factor in when estimating the risk related with a growth option. In essence, payback was also examined to assess for the risk related to a new hotel transaction. One of the interviewees explained: "*You make sure that return will take more time, but you will never lose at the end of the day*". In other words, this last of interviews revealed that the magnitude of loss could be examined in conjunction with the life cycle of the transaction. In this case, the probability of loss becomes the likelihood of any unfortunate event that could affect both the operations and the timing of the investment.

The knowledge of the market and the destination allowed estimating the amount involved in the transaction. The developers of Case C considered this future amount as the magnitude of loss. And like with all three other cases, more than the financial impact of the expansion strategy, the impact on the brand was listed as the most important element considered in the assessment of the amount that could be lost in a transaction.

Distinction among growth options

In practice, these risk elements were estimated first at a country level. Thus, when a country scored high on both the magnitude and the probability of loss, a management contract would be preferred. When the situation of the country was stable, or the probability of loss lower, guarantee levels were added. When both the magnitude and the probability of loss were low, leases were offered. Joint ventures were more difficult to classify in these dimensions because they constituted a more proactive or dynamic approach to expansion. The primary goal of joint ventures was not to manage risk in the destination, but rather to take advantage of a favorable environment. In these cases, timing was considered as a third variable in the investment decision and both the probability and the magnitude were estimated with a timing variable attached to it.

SUMMARY

This Chapter reports the results from the case study research. For each case study, a brief descriptive introduction is presented, and then the results per construct are detailed. The complete synthesis of this work is detailed in the following chapter.

CHAPTER 5: FRAMEWORK__

INTRODUCTION

Each of the four chains formulated its expansion strategy in a particular way. For the pilot case, the customer was at the center of its expansion strategy. In the case of the pilot, expansion was viewed in terms of the network of customers and market share. Case A formulated its expansion strategy in function of market competition. In particular, the expansion strategy of Case A was to be the first mover in the fast expanding targeted markets. Case B focused on the maintenance of consistency across its network. And finally, the expansion strategy of Case C was formulated in terms of ROIC. In sum, the goals of the expansion strategy can be resumed for the pilot case as the market share; for Case A, the timing of entrance; for Case B, the attainment of a regular stream of profit; and for Case C, the alignment of the ROIC requirements of the chain and the hotel owners. Each one of these formulations of the expansion strategy reflected a specific stage of development of the hotel chains.

This chapter is an inductive synthesis of the results presented in the previous section. The findings are assembled by construct and used to extract a framework relating expansion strategy and structure from the perspective of control. Finally, propositions derived from this same framework and relating expansion strategy and structure are proposed at the end of the chapter.

ORGANIZATIONAL FEATURES

Asset specificity

The expansion strategy of the chain defined the asset specificity of a transaction. The higher the adherence of a transaction with the objectives of the expansion strategy, the higher the level of asset specificity was. In the pilot, the expansion strategy was customer oriented, Case A pursued a first mover expansion strategy, Case B focused on the development of its brand, and Case C chose projects with internal returns that aligned both the chain's and investor's targets. For Case C, a hotel that offered a forecasted return on invested capital (ROIC), or an "*earning capacity of the project*" corresponding to the strategic plans of the chain was considered as a highly specific asset. Thus, the hotel transaction that was perceived as highly specific was the one that appeared to best respond to the imperatives of the expansion strategy. In essence, the assets

that allowed the implementation of the expansion strategy of the chain were perceived as highly specific.

Asset specificity served three purposes in the expansion strategy. In particular, asset specificity was the insurance of high room rates at early stages of the operations, the long-term commercial potential of the hotel unit, and the promotion of a brand to hotel owners.

As suggested by the economic theory presented in Chapter 2, the three types of asset specificity were present in the transactions negotiated by the interviewed hotel developers. The results from Case C best illustrate the relationship between the different types of asset specificity, strategy, and the hotel chain performance. First, the destination of a hotel (site specificity) was perceived to have an impact on the success of the expansion strategy through the stability of the future cash flows. Similarly, the location was examined for its impact on the potential of profits of the hotel unit. In essence, the site was examined in terms of the "*return available (*in that site*) for the risk taken*". Second, the achievement of physical asset specificity within time and budget constituted the fundaments for the ROIC of a transaction. Third, the investment in human assets reflected the allocation of competences required for the execution of the transaction.

- Variables of the construct of asset specificity:

The following variables of the construct of asset specificity were uncovered by the research:

- *The degree of compliance of the hotel offer with the brand*: The higher the number of elements that are common between the hotel unit and the brand standards, the higher the degree of asset specificity of the considered hotel unit.
    - → *Elements of the brand standards*: room size, number and size of restaurants, building attributes, architecture and design, and other service outlets in a hotel unit.
    - → The customer base defined the elements of brand standards.
- *The degree of alignment with the owner's expectations of return*. The closer the expectations of return both the hotel chain and the hotel owner for a hotel unit, the higher the degree of asset specificity. The asset specificity of a hotel unit was higher if the hotel permitted the alignment of both the chain and the partner's expectations for the hotel.

- *The degree of site specificity*: The higher the level of site specificity, the higher the level of asset specificity of the transaction. Site specificity is one mean to achieve a high level of asset specificity as it is the fundamental element for the implementation of expansion strategy. In particular, a specific site means that the selected hotel would permit the positioning of the brand in its target market. "*A good location? Depends for which brand*".

  In the context of hotel expansion, it is the most important type of asset specificity and is bi-dimensional:

  → *The specificity of the tourism destination*: the attributes of the tourism destination where the hotel is located. The determinants of the specificity of the tourism destination are

  - The attractiveness of the destination to the customer base of one of the brands
  - The degree of brand competitiveness in the destination: The lower the level of competitiveness (estimates of rooms demand vs. the number of rooms offered in the destination) the higher the degree of asset specificity of the considered hotel unit.

    → *Competitiveness in the destination* is a measured with: the number of rooms offered in the destination, estimates of room demand, the degree of competitiveness, uniqueness of the location, and the potential of growth for the hotel market at the destination.

  → *Site specificity*: the location of the hotel unit within the tourism destination. The determinants of the specificity of the location are

  - Whether the hotel is in a city or resort location
  - Hotel size
  - Proximity to economic activity
  - Existence of commercial synergies with other nearby units
  - Degree of exposure of the brand to the customer base ("*Trophy hotels*")

- *The degree of physical asset specificity*: the higher the level of physical asset specificity, the higher the degree of asset specificity of a transaction. Once the selected site presents a corresponding level of site specificity, the physical asset specificity is considered. Physical

asset specificity allowed the hotel chain to respond to the demand on the selected market. Thus, the higher the number of common physical features between the considered hotel and the brand standards, the higher the level of physical asset specificity.

→ The physical attributes dictated by the brand standards included: the hotel or plot size, room size, number and size of restaurants, and other service outlets in the hotel, architecture, design and building attributes.

In the context of hotel expansion, physical site specificity was often developed jointly with the other party. Therefore, two management imperatives were attached to physical asset specificity: the ability to construct on time and achieve the specificity within the budget. These two imperatives constituted a first step towards the achievement of the required ROIC.

→ The ability to construct on time ensured the entry of the product in the announced time

→ The realization of the construction within budget limited the cost incurred

→ The technical assistance (in management contracts and franchises) is the control process allowing the realization of the physical aspects related to the product

- *The degree of human asset specificity*: the higher the level of investment in human resources capabilities for a transaction, the higher the level of asset specificity in the transaction. This type of asset specificity is key for the pre-opening and operating stages of a transaction. The determinants of human asset specificity are:

→ The level of experience of the chain in operations in the destination

→ The knowledge of operations in the destination available in the chain

The number of projects opened in the same region and the number of managers with experience of the destination were extracted as a measure for the degree of human asset specificity. In addition, interviewees perceived that human asset specificity was affected by:

→ Availability of operation competencies in the destination

→ Time available before opening the hotel unit

Thus, the higher the number of people (with experience and knowledge) required for a specific hotel, the higher the degree of human asset specificity. Equally, the longer the planning for staffing took, the higher the degree of human asset specificity in that specific contract.

In the context of hotel expansion strategy, the requirement of a specific profile for the partner in the transaction also revealed a need for a high level of human asset specificity. In this case, the determinants of human asset specificity are:

→ The level of hotel expertise of the partner

→ The partner's willingness and capacity to comply with all the provisions of the contract.

→ In the case of a management contract, the non-inference of the owner in the daily operations of the hotel was key.

Task programmability

In the context of the expansion strategy, hotel chains were concerned with the planning of two aspects: the relationship with the owner and the forecast of profits. To assess each of these concerns, developers stressed:

→ The due-diligence efforts for background checks to assess the level of human asset specificity

→ The capacity to forecast: 1. the room rates, 2. the occupancy, 3. food and beverage (F&B) revenues, and 4. the operating costs

Variables affecting Task Programmability:

- *The better the assessment of the specificity level of the asset* (through its site, physical, and human asset specificity), *the higher the level of task programmability*. Task programmability included the examination of:

  → the market performance,

  → the capabilities of the future partners

- *The chain experience of the destination*: when the hotel chain has at least one experience in the destination of the transaction, it enhanced its capacity to plan for the transaction.
- *The existence of a known third party in the market*: When the chain had contacts with a known third party in the destination, the level of task programmability was perceived to be higher.

- *The level of experience of the other party with the market in the destination*: when the other party has experience of hotel operations in the destination, the chain's capacity to plan was enhanced. This constituted a link between human asset specificity and task programmability.
- *A shared comprehension of the terms of the contract between the chain and the other party*: when the other party understood the terms of the contract, the degree of task programmability was raised.

Link with other constructs:

- As suggested by the literature review, task programmability is related to control costs. The absence of each of the above listed variables increased the monitoring costs.
- Equally, past experiences with the hotel owner decreased the information search costs, the monitoring costs, and reduced the possibility of outcome uncertainty.
- The planning for the human resources element was the most important element considered in this case.
- Controlling processes, such as committing in the design and the layout were related to task programmability.
- "*Trust*" and task programmability. Trust also allowed the transfer of the level of task programmability to another transaction that has been introduced by a known and trusted partner. Having trust in the relationship was perceived to be most important in the case of the management contract in comparison to a lease or an equity growth option.

Outcome uncertainty

Variables that reduce the capacity for task programmability were presented as the dimensions of outcome uncertainty. In other words, any variable or possible event that could prevent or adversely affect the forecasts of profits and the level of human asset specificity of the future partners were listed as sources of outcome uncertainty for the transaction.

Forms of outcome uncertainty:

Outcome uncertainty can be observed in the difficulties in:

→ Forecasting occupancies and rates,

→ Predicting drastic changes in the region that will affect sales,

→ Estimating the timing of the opening.

Time and efforts spent in estimating the future stream of fees from a specific hotel also appeared to determine the level of outcome uncertainty of a contract. By and large, the estimated information search costs and the level of bonding costs affect the level of task programmability, which in turn will affect the perceived outcome uncertainty.

Information system-base

The information system-base in the examined cases served, essentially, as a behavior measurement process. At the heart of this behavior-based information system is the informal communication and a "*constant contact*" with the participants in the transactions. These participants include key internal positions such as the hotel GM (General Manager) and the other party. The most common information system was informal and behavior orientated as it consisted of discussions of the milestones for the development process.

The internal information systems (between the headquarters, the regional offices, and the hotel units) were essentially behavior-based, while the external information channels between the chain and the other parties relied more on performance-based information.

Overall the information system, both external and internal to the organization, was heavily documented. In the relationship with the other party, the contract was the most formal piece of information but did not constitute the most important part of the information in the transactions. The documents related to the asset specificity of the transactions were key elements of the information-system. At the internal level, the information was also based on behavior, but the reliance on output performance measures was more present.

All firms, with the exception of the smallest chain of the sample, Case B, relied on a large electronic platform for the exchange of information within the organization and with external partners (i.e.: hotel owners, franchisees). The regular financial and accounting information reported in the system constituted the only performance-based information. The cross-comparison of the four cases revealed that the greater the network and the geographical dispersion of the chain, the higher its reliance on its intranet as an information system. This is in accordance with the premises of AT, discussed in chapter 2, in relation to control and its attached control costs.

In Case C, it was reported that the chain had "*2 electronic databases: one for the management contract and franchise contracts and another for projects where C has a financial commitment*." This indicated that behavior-based information systems were used, but that the level of control efforts (monitoring costs) was higher in growth options with financial commitment.

ORGANIZATIONAL CONTROL

In alignment with the above findings on information-base systems, behavior control was present in both the external transactions (with the chain's partners) and in the internal transactions (developers with the rest of the chain's members). Also, and in accordance with the premises of AT and TCT presented in chapter 2, the case studies revealed that the smaller the chain, the higher the reliance on behavior control. Equally, the data reduction process revealed that because of geographic dispersion of Case C, control tended to shift from behavior to a more output oriented type of control.

The data reduction process revealed that the type of control varied with the stage of development of the transaction. This fact was also confirmed when contrasting the growth options on the four case studies. Both the type and level of control varied with the stage of the development. "*It depends, if it's a project with investment, we are or I am with my team following the project at an early stage. When it is a management or a franchise, we are really checking at later stages, unless it is a specific project*".

- *During the pre-opening stage behavior control was predominant*. During this phase, constant monitoring of the other party prevailed. The purpose was to ensure a high level of asset specificity of the asset integrated in the network. The only component of output control during the development stage was the incentive of developers (related to the number of deals signed).
- *During the operating stage, output control prevailed as a control mechanism*. Once the hotel is opened, control shifts to more performance-based control mechanisms for both externally and internally.

Components of behavior control

The legal document relating the two parties (the contract) clearly lists the milestones of behavior control and the outputs of performance control. The objects of behavior control are:

- → Brand standard,
- → Description of procedure of operation,
- → Due diligence,
- → Hotel architectural plans and hotel engineering plans,
- → Legal ownership documents.

Tools of behavior control

The following means for the exertion of behavior control were found:

- → Human resources policies: recruitment and policies for internal promotion
- → Hierarchical approval process of projects
- → Analysis grid for project selection
- → Assistance of the technical team to the project

Components of output control

The measures of performance for the output control are mostly financial figures and include:

- → Occupancy,
- → ADR (Average Daily Rate),
- → RevPar (Revenue Per Available Room),
- → GOP (Gross Operating Profit),
- → GOP percentage, GOP targets
- → Budgets
- → Departmental profit
- → Fees and the investments in FF& E (in the case of a management contract)

Tools of performance control

The following means for the exertion of performance control were found:

- → Performance-related incentives. The compensation of the developers was based on the number of transactions signed. Equally, the management fee in the case of a management contract constituted a performance-related incentive.

→ Comparisons: Year-to-year, or planned vs. actual, and other comparisons of performance components was a tool of performance control. "*We look at what we have planned in terms of costs and in terms of results initially when we have validated the project. We compare what was planned with what has happened*." (Case C)

Finally, the measures of quality of operations include a mix of output and process based information. These indicators comprise:

→ Guest comments,

→ Quality audit teams,

→ Mystery guests, or

→ Feedback from team members

→ Customer satisfaction scores

Uses of Organizational Control

- *Behavior control served the increase in the degree of asset specificity.* The processes in place where found to direct the elements of the transaction that could be controlled for, namely physical and human asset specificity. In a broader sense, behavior control served the maintenance of brand standards through the controllable elements of asset specificity.
- *Output control allowed the integration of the return expectations in the expansion efforts*. Revenues and operating and maintenance costs were the three results controlled for in the expansion efforts of the chain. In other words, the determinants of the ROIC of the transaction were integrated through output control.
- *Output control was used to improve the process related to expansion strategy*. It emerged in Case C that output control permitted the company to store and analyze of information, which was used to improve its processes. Simply put, output control also served learning purposes for the organization.

CONTROL COSTS

The reliance on the behavior rather than on the output type of control led to the dominance of monitoring costs over other types of control costs. The cost of the information system reporting on the information within the network constituted most of the costs related to outcome control. Also in line with the results on organizational control, monitoring costs did prevail during the pre-opening stage where the behavior control was pre-dominant. Equally, more outcome control costs were incurred during the operating stage where performance control was in place.

Below are the observed relationships related to control costs:

- *When the level of task programmability was high, behavior control was possible at minimum monitoring costs*. In the case of high level of task programmability, outcomes are clearly defined and overall control costs are maintained minimum.
- *Monitoring costs were likely to be higher when the local knowledge of hotel operations was limited*. Therefore, there seemed to be a negative correlation between the level of experience and knowledge about hotel operations in a destination and monitoring costs.
- *The higher the asset specificity, the lower the monitoring costs*. When the level of asset specificity was high in a transaction, monitoring costs remained low.
- *Outcome control costs indirectly reduced the overall monitoring costs at the chain level*. Since outcome control could support the learning process of the chain, it increased the chances of selecting a highly specific asset, and in turn reduced the overall monitoring costs.

Dimensions of the monitoring costs

Results from Case C revealed that the costs of monitoring related to a new hotel unit were factored in the earnings forecasts of a hotel to determine the ROIC of the transaction. Monitoring costs were made-up of:

→ The salaries

→ The number of persons in charge of monitoring the process (number of expatriates required on site, and persons mobilized in the headquarter). During the pre-opening stages, this includes the development, technical, and operating team. As

for the operating stage, the regional director and the GM of the hotel unit are the persons in charge of monitoring the process.

→ The number of visits (x travel expenses x number of persons required on site)

→ Time spent by the monitoring team on a specific transaction (number of meetings)

→ Training requirements of the location

In the case of a management contract and franchise, the initial technical fees (usually a fixed fee per room) paid by the hotel owner and the franchisee, respectively, often covered monitoring costs. Also, in the case of a management contract, management fees covered the monitoring fees (salaries and number of expatriates in the hotel unit).

Variables affecting monitoring costs

The following variables were found determining the monitoring costs:

→ The accessibility of the hotel,

→ The level of asset specificity: it affected the number of visits to the hotel unit and the time spent on a specific transaction.

Dimensions of the outcome control costs

Outcome control costs were made-up of:

→ Investment in the infrastructure of the information system

→ The bonuses paid to regional managers and general managers

OTHER CONTROL COSTS

Residual loss estimates

- *There was no estimate for the residual loss*. When considered, the residual loss was assessed in terms of sales cannibalization. Overall, what developers were concerned about the "*capacity of absorption of the market*". This being a feature of asset specificity, it revealed that when considered, an opportunity cost was estimated in the assessment of the degree of asset specificity of the transaction.

Information search costs

- *There is a negative correlation between information search costs and task programmability*. In the case of Case A, the information search costs constituted the center of the other control costs. This was due to the novelty of most of the market in which it was entering.
- *Monitoring costs were likely to be higher when the local knowledge of hotel operations was limited*. Therefore, there seemed to be a common purpose served by the information search costs and monitoring costs.
- The level of information search costs tended to be reduced with the experience of the development team.

Types of the information search costs

Two types of information search costs were identified:

→ Information search costs related to the destination (assessment of the site specificity). On-site visits constituted this first type of information search cost

→ Information search costs related to the owner (assessment of the human asset specificity) were made-up of background checks

When possible, the Pilot and Case B commissioned third party specialists on a contract basis.

In the case of a management contract or franchise, the hotel owner and the franchisee often paid for this market study. Otherwise, the chain relied upon available information on the Internet (cost of information). Case A tended to hire "*previous consultants of consultancy offices*" in an effort to reduce information search costs.

Bargaining costs

- *The bargaining power of hotel chains determined both the bargaining and information-search costs*. The high number of hotel owners prospecting for operators in comparison to the chain offer in the destinations minimized both information search costs and bargaining costs.
- *The bargaining costs were contingent upon the destination of the hotel*. Bargaining costs, indeed, depended on the level of competitiveness in the tourism destination of the hotel. The higher the level of competitiveness of a destination, the higher the bargaining costs for hotel chains.

- *The higher the level of human asset specificity of the other party, the lower the bargaining costs*. In particular, the more experience of hotel operations the partner had, the higher the level of task programmability, the lower the bargaining costs in the transaction. Simply, the partner knew about the steps of the relationship through his past experience, and Case C had to disburse less effort in bargaining.

Bonding costs

- *Despite the non-financial participation in a management contract, there were bonding costs attached to this same growth option*.
  - → The shared responsibility of the brand standards, by the operator, the developer, and/or the franchisee constituted a strong bonding cost in the context of hotel chain expansion. The operator was maintained "*hostage*" (Williamson, 1974) through this shared responsibility of the brand standards.
  - → In the case of Case A, who was launching its international expansion, this element was even more critical.
  - → The higher the degree of asset specificity, the higher the bonding costs involved by the hotel chain in the transaction. In accordance with the TCT premises presented in Chapter 2, the compliance of the hotel unit with the demand of the customer base and the degree of brand competitiveness constituted a bonding cost.
  - → The cancellation of technical fees in "*favor of getting the contract*" constituted an indirect bonding cost.
  - → The length of the pre-opening procedures affected the time targets of the chain and also constituted bonding costs.

Bonding costs were likely to increase with:

- → The financial commitment of the hotel chain in the transaction
- → The existence of other contracts with the hotel owner, or
- → The conciliation of the owner's priority clause, or
- → The non-division of the responsibilities for meeting the settled targets with the other party.

- *There was a relationship between bargaining and bonding costs.* On the one hand, having several contracts with the other party increased the bonding costs. On the other hand, having several contracts with the other party reduced the bargaining costs.

ELEMENTS OF RISK

As suggested by the literature reviewed in chapter 2, the dual aspect of risk was confirmed by the case studies. The probability of loss was considered in conjunction with the magnitude of loss in the management of risk in expansion strategy. In particular, the focus on the probability of loss increased with the level of perceived magnitude.

While the magnitude of loss was first mentioned as the highest concern for the respondents, the probability also appeared key. The determinants and the estimates of the probability of loss being, by nature, more difficult to assess, developers considered the probability of loss after the magnitude of loss.

In line with Bradach's findings in the restaurant industry (1992), this research revealed that uniformity in the network was a key element of the expansion strategy for hotel chains. This requirement for uniformity was reflected in the brand standards and image: "*Image, and that the property will be delivered as per our image worldwide and to our standards and specifications*" (Pilot Case). As a consequence, maintaining this uniformity was the central element of control and risk management in the expansion strategy of hotel chains.

The dominance of either element of risk was a function of the stage of the development process. The magnitude of loss was the main concern during the negotiation of the deal. During that same stage, the concern would be about the assessment of the magnitude of the deal in order to best define the level of human asset specificity required for the other party. Once that portion of risk was estimated, the focus was then on controlling for its probability to happen. This dominance of either element of risk was observed in the all of the cases except Case C.

Case C presented a particular approach to the management of risk. First, for developers in Case C, "*Risk is related to the level of stabilization of the political, financial, and legal environment*" (Case C). Thus, for Case C, outcome uncertainty, namely the degree of stability, or likelihood of unfortunate events to happen were the main focus. This reflected the dominance of the probability of loss rather than its magnitude as a risk element in their expansion efforts.

Second, more than the magnitude of loss, the next element that was factored into Case C's management of risk was the variable of time. "*You make sure that return will take more time, but you will never lose at the end of the day*". Simply, the magnitude of loss was examined in conjunction with the life cycle of the transaction. In sum, for Case C, the probability of loss became the likelihood of any unfortunate event that could affect both the operations and the timing of the investment.

Magnitude of loss

- The respondents distinguished between the two elements of risk but named them the "*financial risk*" and the "*brand risk*", respectively (Case B). The financial risk was the amount of the estimates, "*that's actually a number*", and constituted the magnitude of loss related to a transaction.
- The financial impact included the guarantees signed in certain clauses of a management contract but also the bonding costs.
- *The magnitude of loss is not only financial but also commercial*. Risk related to development activities was summarized as follows: "*we are concerned with how much we could lose financially and in terms of credibility*" (Case A)
    - → *Visibility of the location to the segment of targeted customers increased the magnitude of loss*. When the hotel (even a management contract) was located in a highly visible location, the magnitude of loss would become key in the management of risk related to the transaction.

- *The information search costs reduced the magnitude of loss*. The information search costs were paid during the negotiation stage to estimate the level of human asset specificity required for the other party. They were paid to control for future losses. Equally, the knowledge of the destination allowed estimating the amount involved in the transaction. This future amount was considered as the magnitude of loss.

Probability of loss

- Probability of loss was often associated with brand risk. The "*the minute you start deviating from the standards and quality in one hotel*" (Case B) the chain incurred brand risk. This notion of deviation reflected the likelihood of variance related to the probability element of risk.
- Two concerns of development were listed under this element of risk:
  - → The probability of losing the contract, or "*Sign a contract that doesn't materialize*" (Case A). A contract that would not materialize would not only affect the timing of the expansion but also incur unnecessary costs.
  - → The probability of not achieving the forecasted sales or "*the risk is that we spend too much time on projects that don't yield and that's the hardest thing to juggle at the moment.*" (Case A). At the center of these concerns was the probability of not delivering the returns targeted by the chain and those promised to the other party.
- Variables affecting the probability of loss:
  - → The probability of loss was related to the human asset specificity of the other party. In particular, the financial viability of the partner was a key determinant of the probability of loss in a transaction.
  - → Reducing the information search costs, the behavior control costs or the bonding costs increased the volatility of the expected returns and thus the probability of loss.
  - → Task programmability was the most important element in assessing for the probability of risk. "*I guess that is why we went many steps ahead by asking for everything in place before we signed*" (Pilot Case)

DISTINCTION AMONG GROWTH OPTIONS

The four growth options presented in the literature review section were confirmed by the data collection. However, the four examined chains did not rely on direct full ownership (without creation of subsidiary) for the examined expansion strategy. Management contracts, on the contrary, were the most commonly relied on growth option. Equity participation was used in

Cases A, B, and C. In these instances, the chain formed a joint venture with an investor. Within this joint venture, the hotel chains were both partners and operators of the future hotel units. Sometimes, the hotel chain franchised the operations of the hotels of the joint venture to an established hotel operator. The former case was considered in this study as a management contract. The latter was examined as a franchise. In essence, the distinction was whether the hotel chain operated the hotel or not. Finally, Cases A, B, and C also offered leases. Leases could either be fixed or variable. Leases were accepted in established destinations with a high level of competitiveness.

Case C, the largest chain of all four investigated, presented the following profile of expansion. First, the risk elements were estimated at a country level. Thus, when a country scored high on both the magnitude and the probability, a management contract would be preferred. When the situation of the country was stable, or the probability of loss lower, guarantee levels were added. When both the magnitude and the probability of loss were low, leases were offered. Joint ventures were more difficult to classify in these dimensions because they constituted a more proactive or dynamic approach to expansion. The primary goal of joint ventures was not to manage risk in the destination, but rather to take advantage of a favorable environment. In these cases, timing was considered as a third variable in the investment decision and both the probability and the magnitude were estimated with a timing variable attached to it.

In sum, the elements of risk determined the choice of the growth option. When both elements were estimated to be high, management contracts were selected. The lower the probability of loss compared to this initial situation (both elements being high), the higher the chances for the chain to offer equity participation. In a contract were both the magnitude and the probability of loss were lower than the initial situation, leases would be pursued. Finally, the offering of joint venture is tight to both the elements of risk and timing of the investment.

In practice, when the magnitude of loss was under the responsibility of the hotel owner (like in a management contract), the operator was mainly concerned with the variability in the hotel sales. Therefore, the operators concentrated their efforts on controlling for elements that might affect the probability of loss.

Below is a list of distinctive features that were found by growth options.

Management contracts

- The degree of physical asset specificity was said to be less of a concern in a franchise than in a management contract. Since the hotel chain has the responsibility of managing the unit, the degree of physical asset specificity was regarded as more important.
- Human asset specificity was more important to the hotel chain in the case of a management contact when the chain operated the unit.
- The level of outcome uncertainty was less of a concern in a management contract where both the hotel chain and the hotel owner shared the performance responsibility.
- General Manager and the regional offices were responsible for the outcome of the operations. The reliance on bonus compensation schemes for these managers reflected a control based on performance.
- The owner paid most of the monitoring costs through the technical fees and the pre-opening budget.
- *The management contract separated the process from the output control between the chain and the owner*. The chain handled the behavior control. The owner had little say in the process but exerted his power on the output.
  - → The (management and incentive) fees, the provisions for working capital, and the investments in FF& E were the three most important performance indicators measured in a management contract.
  - → The operator, in turn, focused on the management of people and the quality of operations.
- The most important concern in a management contract was the control for the probability of the intervention of the owner in the daily operations of the hotel.
- The probability of loss is the dominant element of risk

Leases

- Risk and risk elements in the hotel expansion context appeared higher in leases than in any other growth option. The commitment of the chain in a hotel through a lease was considered as riskier than equity participation for four reasons:
  - → Greater brand exposure in a lease than in equity participation.

→ No possibility of sharing the operating responsibilities in the case of a lease. And finally, the lack of flexibility and high requirements of a lease prevented the firm from employing it in emerging markets where the speed of move was key.

- The magnitude of loss was the dominant element of risk.

Equity participation

- The control of a joint venture partner was the most important but also most difficult type of control. This control tended to be even more affected by:
  → The length of the association
  → The lack of hotel operating experience of the other partner
- Additional monitoring costs were related to equity participation: a person was appointed to monitor the relationship with the partner and ensure the enforcement of the chain's rights in the partnership.
- The higher the risk involved (in terms of magnitude of loss), the higher the information search costs.
- The magnitude of loss was the dominant element of risk.

Franchise

- In the case of a franchise, the availability of operational and the managerial competences in the destination were the priority.

FRAMEWORK

The relationship between strategy and structure is fundamental to both research on strategic management and organization theory. In fact, both bodies of knowledge indicate that this relationship has an impact on the long-term performance of an organization. Within this rationale, this work addresses one overarching question: how do structure and strategy relate? Drawing from research in strategic management, finance, and organization theory, this study examines the link between expansion strategy and structure in the international hotel industry

context through the perspective of the construct of control. In particular, this research effort raised the following questions:

- Is control a structural variable in the management of expansion strategy?
- How does control intervene in the management of risk in expansion strategy?
- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion strategy context?
- What is the role of control costs in the management of risk for expansion strategy?
- How do the features of the hotel unit affect the management of risk in expansion strategy?

In line with the above research questions, ten further research questions that are presented in Chapter 1 directed this study.

Expansion selection and control stakes

1. Do hotel chains assess possible control advantage(s) and disadvantage(s) when selecting a particular growth option? If yes, what are they?
2. Are these advantages and disadvantages different from one growth option to another? If so, how do they differ?
3. Why and how does the introduction of the new unit modify the control in place in the chain?
4. How is the modification of control, through the introduction of a new unit, assessed?

Costs and control advantages

5. Are there costs associated with the identified control advantages and disadvantages?
6. Are these costs estimated when selecting a growth option?
7. Is there a relationship between these cost estimates and the amount of resources committed in the selected growth option?
8. Are resources committed when modifying the control in place to the new unit?
9. Why are these resources committed?

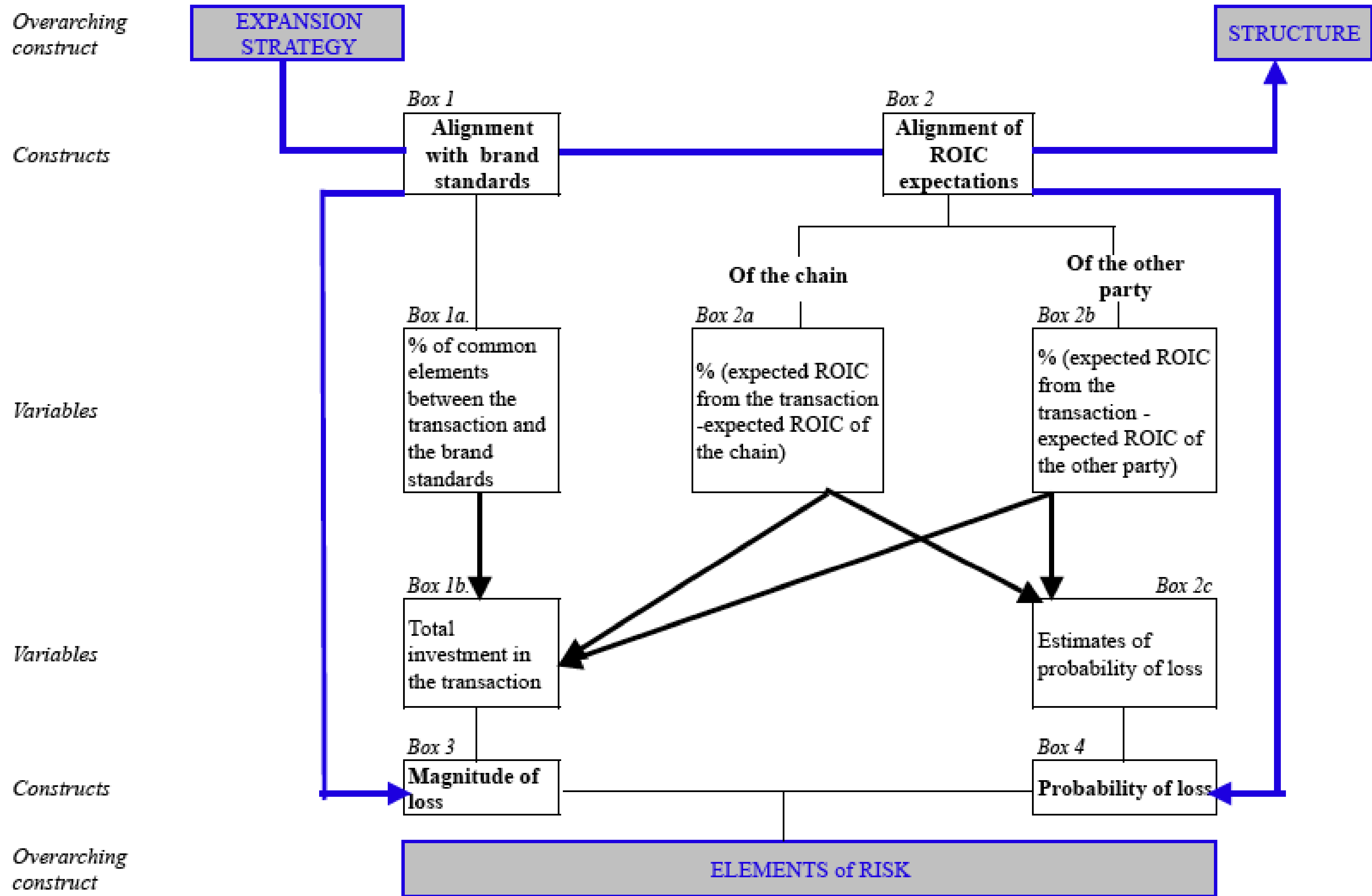
The management of risk

10. How does the assessment of control advantages and disadvantages intervene in expansion strategy risk assessment?

Guided by these questions, this research led to the framework presented in this section. Figure 8, hereafter, is a graphical representation of this framework. In particular, to the first research question, "is control a structural variable in the management of expansion strategy", the multiple-case study research confirmed the proposition of exploring the relationship between strategy and structure from the perspective of control. Three findings support this conclusion. First, the inductive data reduction effort not only uncovered relationships between constructs, but also revealed variables for these constructs. Second, the two main constructs that were derived from the data analysis are in line with the existing theory on long-term performance in strategic management. In particular, alignment of the hotel offers with the brand standards and alignment of ROIC expectations are coherent with the fundaments of finance and strategy implementation. Finally, the links between the elements of risk and the expansion strategy-structure relationships are consistent with the literature review on control in the management of risk.

In chapter 6, the findings of this research are further contrasted with the literature. Before discussing these points, this section presents the details of the framework that emerged from the data analysis process.

Figure 8 The relationship between expansion strategy and structure of hotel chains from the perspective of control



As illustrated in Figure 8, structure is the result of expansion strategy. In other words, the network of the hotel chain is the consequence of its expansion strategy. The network of the chain is, in fact, the result of both the alignment of the transaction with the brand standards (Box1) and the alignment of ROIC expectations (Box 2). These degrees of alignment are, in turn, defined by the expansion strategy of the chain. Figure 9 presents these constructs and their respective variables.

- *Alignment of the transaction with the brand standards* = (number of common elements between the transaction and the brand standards)/ number of elements listed by the brand standards. (Box 1a.)

In practice, the list of elements of the transaction is compared against the elements listed by the brand standards, and then the number of common elements recorded. The list of elements of the brand standards is detailed in the legal contract sealing the transactions. Traditionally, the section of a management contract labeled "operating standards" serves this purpose.

Figure 9, that is discussed below, reflects that the elements listed by the brand standards are common with the variables constituting the construct of asset specificity. This further supported the relevance of the perspective of the construct of control.

There are two types of Alignment of ROIC expectations: the first is the alignment with the ROIC of the chain (Box 2a.) and the second is the alignment of the ROIC expectations of the other party (Box 2b.).

- *Alignment of ROIC of the chain* = (The ROIC expected from the transaction – the ROIC set by the chain) / the ROIC set by the chain. (Box 2a.)

The first element of this computation is the estimated ROIC of the transaction (e.g.: the expected return on invested capital from a newly formed joint venture with attached management contracts). The second is the ROIC standard or target set by the chain for its expansion efforts. For the three publicly traded chains, these ROIC requirements were aligned with those of its stockholders.

- *Alignment of the ROIC of the other party* = (The ROIC expected from the transaction – the ROIC expected by the other party) / the ROIC expected from the transaction. Here, the requirement is to have the other party (either the hotel owner, the partner in the joint

venture, or the franchisee) to align his/her expectations of ROIC with those estimated by the chain. (Box 2b.)

The bottom of Figure 8 reveals that determining the degree of alignment of the transaction with the brand standards (Box 1) determines the total investment of the transaction. This total amount of money constitutes the magnitude of loss (Box 3), one of the two elements of risk. In parallel, the degree of alignment of both ROIC expectations (Box 2) permits the estimates of the probability of loss (Box 4), the second element of risk as defined by management theory.

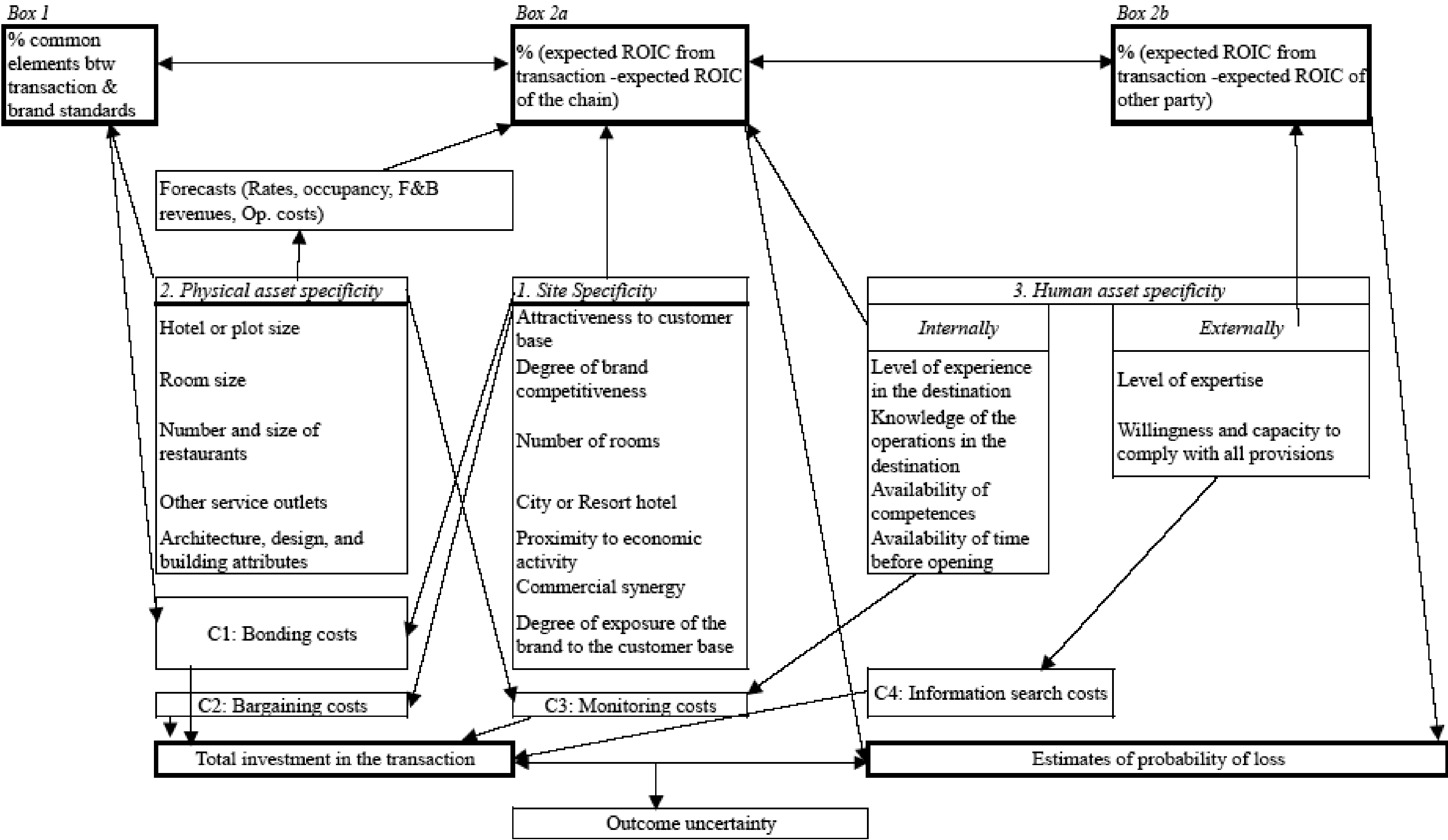
At this stage, the question that is left unanswered is: which minimum level of alignment is, then, required to positively affect the success of the expansion strategy? This minimum, or rather, optimum level of alignment is determined by a series of iterative analyses of the links between:

- ✓ The alignment with the brand standards
- ✓ The alignment of ROIC expectations,
- ✓ The magnitude of risk, and
- ✓ The elements of risk.

Figure 9 illustrates the components of the iterative analyses that determine the optimum level of alignment. This analysis details the interaction between the components of control and the variables intervening in the management of expansion strategy.

The central component is the construct of asset specificity introduced by the perspective of the construct of control. Specifically, the construct of site specificity emerged as central in the relationship between expansion strategy and structure in the context of international hotel chains. This finding is, again, consistent with research in the hospitality industry, which further support the consistency of the results.

Figure 9 The interaction of variables in the relationship between expansion strategy and structure from the perspective of control



The components of physical asset specificity (2.) are, in fact, the elements outlining the brand standards. Thus, the level of physical asset specificity (2.) determined the degree of alignment of the transaction with the brand standards (Box 1). In particular, if the size of the hotel (or plot in the case of a project), the size of the rooms, the number and size of the restaurants, the number and nature of the service outlets in the hotel (e.g.: SPA, shops, etc...), the architecture and design attributes correspond to those set by the brand standards, then the degree of alignment with the brand standards (Box 1) is likely to be high. Moreover, the estimates of the components of the physical asset specificity were factored in the computations of the magnitude of loss. Finally, the degree of alignment with the brand standards (Box 1) determined the level of monitoring efforts (C3) required by the hotel chain in the transaction. Thus the lower the degree of alignment of the transaction with the brand standards, the higher the level of monitoring costs required. Equally, according to the TCT, the higher the degree of alignment with the brand standards (Box 1), the higher the bonding costs (C1) of the transaction are. These bonding costs were part of the magnitude of loss of the transaction.

The strict adherence to the brand standards is more important for brands of lower segments of the market (e.g.: budget hotels). For these brands, standardization is a key element of the expansion strategy. In these cases, the elements of the transaction had to strictly adhere to those set by the brand standards. For the brands operating in higher ends of the market, the components of the transaction had to correspond to those of the brand within a certain bracket.

Next, the determinants of the degree of alignment with the ROIC of the chain (Box 2a) are threefold. The first determinant of the degree of alignment with the ROIC of the chain is the forecast derived from components of the physical asset specificity (2.) of the transaction. In particular, the hotel size, the size of the rooms, the number and size of the restaurants, the number and nature of the service outlets in the hotel (e.g.: SPA, shops, etc...), the architecture and design attributes are the premises for the forecast of the room rates, the occupancy, the F&B revenues, and the operating costs. These forecasts were factored in for the computation of the ROIC expected from the transaction.

The second determinant of the degree of alignment with the ROIC of the chain is the degree of site specificity (1.) of the transaction. In fact, computation of the ROIC expected from the transaction was refined based on the components of site specificity, namely:

- ✓ The level of attractiveness of the destination of the hotel to the customer base,

- ✓ The degree of brand competitiveness in the destination,
- ✓ The number of rooms in the hotel,
- ✓ Whether the hotel was a resort or a city hotel,
- ✓ The potential commercial synergy, and
- ✓ The degree of exposure of the brand to the customer base

The third determinant of the degree of alignment with the ROIC of the chain is the degree of internal human asset (3.) specificity. The expected ROIC from the transaction was further refined with the analysis of the components of human asset specificity. In other words, the level of experience of the destination of the chain, its knowledge of the operations in the destination, the availability of those competences in the destination, and the availability of time before opening were all factored in the estimates of the expected ROIC from the transaction. In fact, all these four determinants of human asset specificity lead to the projections of monitoring costs related to the transaction. These costs were in turn factored in the ROIC. Moreover, the analysis of these determinants allowed estimating for the timing, or the life cycle of the investment in the transaction.

As a result, a low degree of alignment of ROIC of the chain would suggest a low ROIC for the transaction compared to the one set by the chain. Ultimately, this low degree of alignment would result in a high probability of loss for the transaction.

The alignment of ROIC of the other party (Box 2b) was determined by the degree of external human asset specificity (3.). The level of expertise of the other party and his/her willingness and capacity to comply with all the provisions of the legal contracts confirmed or disconfirmed the alignment of the ROIC. In other words, the higher the level of expertise about hotel operations of the other party, the higher the alignment of ROIC of the other party would be. Equally, the higher the willingness and (financial) capacity of the other party to comply with all provisions, the higher the alignment of the ROIC of the other party would be.

In the case where these first assessments of alignment of ROIC of the other party were low, information search costs (C4) were incurred and factored in the magnitude of loss for the transaction. In turn, the lower the degree of alignment of ROIC of the other party, the higher the magnitude of loss would be.

To recapitulate on the relationship between strategy and structure from the perspective of the construct of control:

- The degree of alignment with the brand standards is determined by the components of physical asset specificity. A high degree of alignment with the brand standards leads to high bonding costs and low monitoring costs. Both bonding and monitoring costs are elements of the magnitude of loss.
- The degree of alignment of the ROIC of the chain is a function of both the level of site specificity and the forecasts derived from the components of physical asset specificity. A high degree of alignment of the ROIC of the chain reduces the probability of loss of the transaction.
- A high level of internal human asset specificity in the transaction increases the degree of alignment of the ROIC of the chain. In this instance, a low level of monitoring costs is to be invested, which reduces the magnitude of loss of the transaction.
- A high level of alignment of the ROIC of the other party is a consequence of a high degree of external human asset specificity.
- A high degree of alignment of the ROIC of the other party not only reduces the probability of loss related to the transaction, but also diminishes the magnitude of loss through the reduction of the information-search costs.

At this stage, two parts of the magnitude of loss are still left to discuss: the bonding and the bargaining costs. As mentioned earlier, bonding costs are a function of the degree of alignment with the brand standards. Bonding costs are also a consequence of the degree of site and human asset specificity. Overall, the TCT suggests that the higher the level of asset specificity, the higher the bonding costs for the hotel chain in the transaction.

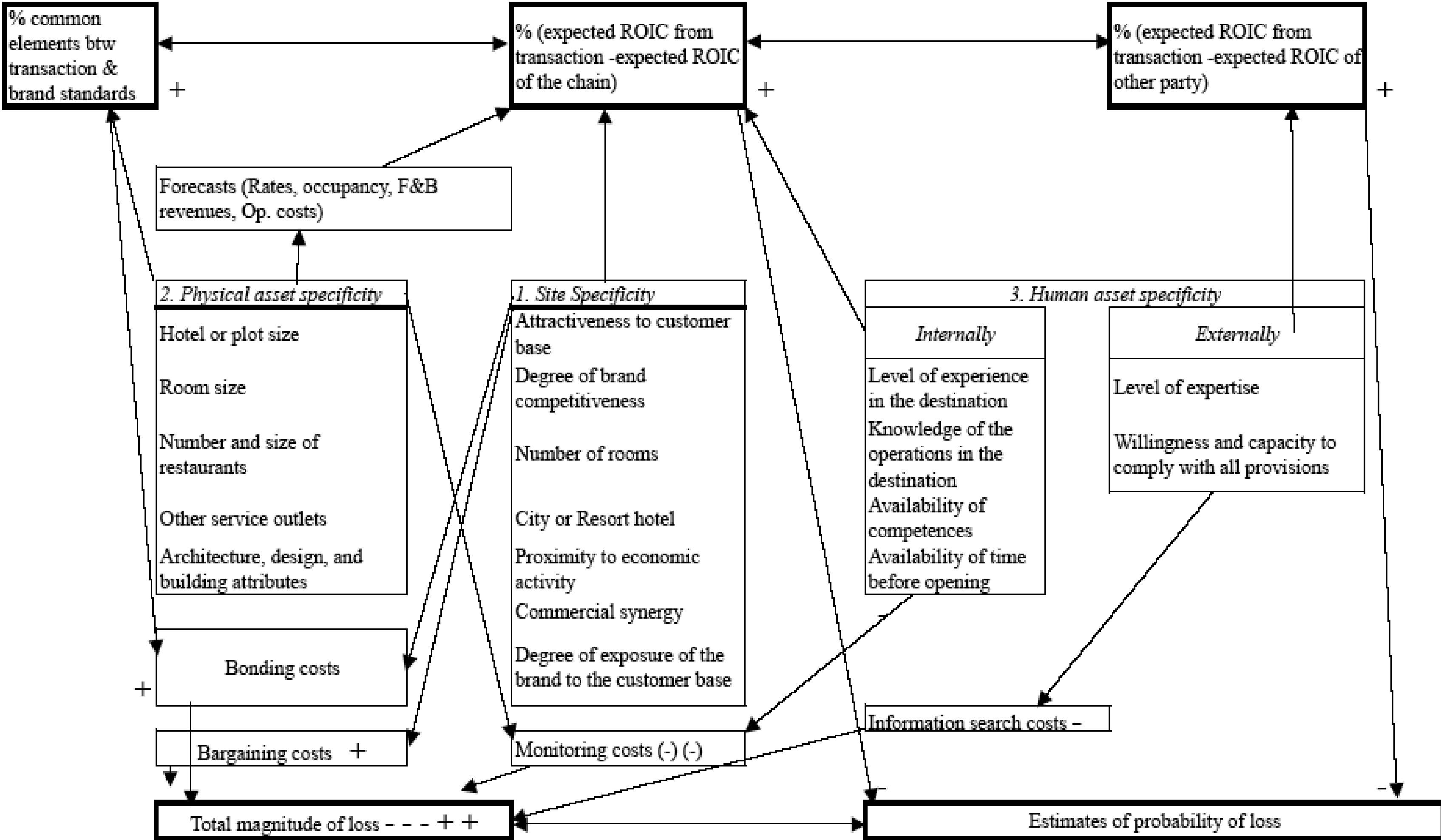
The bargaining costs, however, appeared to be essentially derived from one aspect of site specificity. Simply, the data analysis revealed that when the site of the transaction was highly specific to a hotel chain, its bargaining costs increased.

Figure 10 shows an example of transaction where all three types of alignments are high. The positive signs (+) near the constructs show a positive degree of alignment. Equally, positive and negative (-) signs are drawn next to the different components of the magnitude and

probability of loss. In this case, a negative sign in the box indicates an increase (+) or a decrease in the amount invested.

What this example illustrates, is that when all three alignments are high, the magnitude of loss is likely to be low (3 – and only 2 +). And, in this same case, the probability of loss is also likely to be low.

Figure 10 The interaction of variables in the relationship between expansion strategy and structure from the perspective of control: An example



PROPOSITIONS

In essence, four propositions have been extracted from this research effort. These propositions are presented hereunder. In addition, the uncovered variables and measures are listed to not only put forward variables for future research, but also to allow for possibilities of falsifiability of these relationships.

P1: The alignment with brand standards and the alignment of the ROIC expectations are the operationalizations of the relationship between strategy and structure.

Measures

- *Alignment of the transaction with the brand standards* = (number of common elements between the transaction and the brand standards)/ number of elements listed by the brand standards.
- *Alignment of ROIC of the chain* = (The ROIC expected from the transaction – the ROIC set by the chain) / the ROIC set by the chain.
- *Alignment of the ROIC of the other party* = (The ROIC expected from the transaction – the ROIC expected by the other party) / the ROIC expected from the transaction.

P2: The degree of alignment with the brand standards affects the magnitude of loss through the bonding and monitoring costs.

Measures

The components of brand standards are defined by the elements of physical asset specificity, namely:

- ✓ The size of the hotel (or plot in the case of a project),
- ✓ The size of the rooms,
- ✓ The number and size of the restaurants,
- ✓ The number and nature of the service outlets in the hotel (e.g.: SPA, shops, etc.),
- ✓ The architecture and design attributes

Bonding costs were likely to increase in the case of:

- ✓ Absence of shared responsibility of the brand standards with the other party
- ✓ Early stages of international expansion
- ✓ High degree of asset specificity

- ✓ Cancellation of technical fees
- ✓ Duration of the pre-opening procedures
- ✓ Financial commitment of the hotel chain in the transaction
- ✓ Existence of other contracts with the hotel owner
- ✓ Conciliation of the owner's priority clause
- ✓ Non-division of the responsibilities for meeting the settled targets with the other party.

Monitoring costs include:

- ✓ The salaries
- ✓ The number of persons in charge of monitoring the process
  - Number of expatriates required on site,
  - Number of persons mobilized in the headquarter
- ✓ The number of visits (x travel expenses x number of persons required on site)
- ✓ Time spent by the monitoring team on a specific transaction
- ✓ Investments in training requirements of the location

P3: The degree of alignment of the ROIC of the chain affects both the probability and the magnitude of loss.

<u>Measures</u>

The components of ROIC expectations from the transaction are the forecasts of:

- ✓ Room rates,
- ✓ Occupancy,
- ✓ F&B revenues,
- ✓ Operating costs

These forecasts are contingent upon the components of site specificity, namely:

- ✓ Level of attractiveness of the destination of the hotel to the customer base,
- ✓ Degree of brand competitiveness in the destination,
- ✓ Number of rooms in the hotel,
- ✓ Resort vs. city hotel,
- ✓ Potential commercial synergy
- ✓ Degree of exposure of the brand to the customer base

And the elements of physical asset specificity, namely:

- ✓ The size of the hotel (or plot in the case of a project),
- ✓ The size of the rooms,

- ✓ The number and size of the restaurants,
- ✓ The number and nature of the service outlets in the hotel (e.g.: SPA, shops, etc...),
- ✓ The architecture and design attributes

<u>Measures</u>

The degree of alignment of the ROIC is a function of internal human asset specificity or:

- ✓ The chain's level of experience of the destination
- ✓ The chain's knowledge of operations in the destination,
- ✓ The availability of the required hotel operation competences in the destination
- ✓ The availability of time before opening

These components of internal human asset specificity determined the required monitoring costs (a constituent of the magnitude of loss), namely:

- ✓ The salaries
- ✓ The number of persons in charge of monitoring the process
    - Number of expatriates required on site,
    - Number of persons mobilized in the headquarter
- ✓ The number of visits (x travel expenses x number of persons required on site)
- ✓ Time spent by the monitoring team on a specific transaction
- ✓ Investments in training requirements of the location

P4: The degree of alignment of the ROIC of the other party affects both the magnitude and the probability of loss.

<u>Measures</u>

The degree of alignment of the ROIC is a function of external human asset specificity or:

- ✓ The other party's level of expertise in hotel operations
- ✓ The other party's willingness and financial capacity to comply with all the provisions of the legal contracts

The level of human asset specificity determines the required information-search costs (a constituent of the magnitude of loss), namely:

- ✓ On-site visits to gather information on the destination.
- ✓ Investments in background checks of the other party

CONCLUSION

Coming back to the initial research directions mentioned throughout this work, the answer to whether control is a structural variable in the management of expansion strategy, the question is no. Control is not a variable, but a construct intervening in the management of expansion strategy. And, control costs, products of control, are an important variable in the management of expansion strategy. In fact, control costs are key in the management of expansion strategy since they are the bridging elements between expansion strategy, structure, and the elements of risk.

To resume, the answers to the research questions in light of these results are synthesized below:

- Is control a structural variable in the management of expansion strategy?

✓ No, control is a construct intervening in the management of expansion strategy. Bacharach (1989) defined constructs as "*approximated units (…), which by their nature cannot be observed directly (e.g. centralization, satisfaction, or culture)*". In addition, he defined variables as "*observed units", which are operationalized empirically by measurement*". In the study on hand, control was a construct, present across the examined relationships, but not directly observed. Control costs, on the other hand, were the measurements of control that were observed and measured. Consequently, based on these definitions of constructs and variables, it has been concluded that control was a construct not a variable in the study on hand

- How does control intervene in the management of risk in expansion strategy?

✓ Control intervenes through control costs in the management of risk in expansion strategy. Figure 8 details the relationship observed between control costs and elements of risk in the management of expansion strategy.

- Is it possible to operationalize the relationship between structure and strategy using control as surrogate for the expansion strategy context?

✓ Yes, the uncovered variables for the construct of control support this answer. The construct of control offers tools for operationalizing the relationship between strategy and structure for hotel chains. P1 (The alignment with brand standards and the alignment of the ROIC expectations are the operationalizations of the relationship between strategy and structure.) is extracted from approaching the question through the lenses of control. This first

proposition clearly reveals that control can be used to operationalize the relationship between structure and strategy for the expansion strategy context. In addition, this research uncovered the two main constructs that operationalized this relationship.

- What is the role of control costs in the management of risk for expansion strategy?

✓ Figure 8 and the extracted propositions provide details for this answer. In particular P2 (The degree of alignment with the brand standards affects the magnitude of loss through the bonding and monitoring costs) resumes the answer to this question.

- How do the features of the hotel unit affect the management of risk in expansion strategy?

✓ As illustrated in Figure 8, and detailed in figure 9, hotel features affect the management of risk in expansion strategy as they determine both the degree of alignment with brand standards and the alignment of ROIC expectations. Of importance is the construct of asset specificity, which is provided by the TCT. The construct of asset specificity, or the features of the hotel unit, is at the center of the framework on developed from this research on the management of risk in expansion strategy.

As far as the ten sub- research questions that guided this research are concerned, below is a summary of the findings of this research.

Expansion selection and control stakes

1. Do hotel chains assess possible control advantage(s) and disadvantage(s) when selecting a particular growth option? If yes, what are they?
2. Are these advantages and disadvantages different from one growth option to another? If so, how do they differ?

The results of this research reveal that hotel chains do assess two elements when selecting a particular growth option: the alignment with brand standards (Box1) and the alignment of ROIC expectations (Box2). Theses two elements of analysis are directly related to control and risk through control costs and their organizational determinants (Figure 9).

3. Why and how does the introduction of the new unit modify the control in place in the chain?
4. How is the modification of control, through the introduction of a new unit, assessed?

Little has been found with regard to these two questions in the results of this study. It is suspected that the size of the hotel chain might be an intervening variable in this question. Further research is suggested in Chapter 6 with regard to these two sub-research questions.

Costs and control advantages

5. Are there costs associated with the identified control advantages and disadvantages?
6. Are these costs estimated when selecting a growth option?
7. Is there a relationship between these cost estimates and the amount of resources committed in the selected growth option?
8. Are resources committed when modifying the control in place to the new unit?
9. Why are these resources committed?

The management of risk

10. How does the assessment of control advantages and disadvantages intervene in expansion strategy risk assessment?

As mentioned throughout these last two chapters, control costs are the key variables in the relationship between structure and expansion strategy in the hotel industry. Figure 9 details these relationships. Finally, Figure 9 also details the role of control advantages and disadvantages, through control costs in the assessment of the risk in expansion strategy.

CHAPTER 6: CONCLUSIONS & DISCUSSIONS

INTRODUCTION

Two sets of propositions have been developed during this research endeavor. The first is the result of a deductive effort, pre-data collection, and the second has been derived after data collection and analysis. Table 11 opposes these two sets of propositions to support the brief introductory comparison.

The first proposition has been refined after the case study analysis as measures for control costs have been uncovered during the research. In fact, control costs have been factored in the relationships between the constructs (please refer to the measures under each proposition in Chapter 5).

Table 11 Propositions of pre-data collection vs. research propositions

Proposition from the pre-data collection	Research Propositions
P1: Control costs incurred by the transaction result from the interaction of organizational features of the hotel unit with the organizational control of the hotel chain.	P1: The alignment with brand standards and the alignment of the ROIC expectations are the operationalizations of the relationship between strategy and structure.
P2: The higher the control costs involved in the transaction, the more likely the magnitude of loss will be the dominant element of risk.	P2: The degree of alignment with the brand standards affects the magnitude of loss through the bonding and monitoring costs.
P3: Other control costs have a moderating effect on the relationship between control costs of the transaction and the risk elements.	P3: The degree of alignment of the ROIC of the chain affects the probability of loss.
P4: Other control costs will vary with the nature of the growth option adopted (lease, management contract, franchising).	P4: The degree of alignment of the ROIC of the chain affects the magnitude of loss.

Equally, organizational features, which appeared to be essentially made up of asset specificity, have been integrated into the relationship through the measures. In other words, the constructs, per-se, have been eliminated from the propositions but the variables that they have helped uncover were maintained. Overall, the constructs of control costs and

organizational features have provided the guidelines for the data collection and examination, but were not kept as constructs in the final propositions.

The second and the third propositions were overly simplistic as it appeared that the relationship between control costs and elements of risk was less linear that it appeared after the first deductive process. The research propositions that were derived from the overall research effort, along with their measures, best illustrate this point.

Finally, the impact of the growth option is discussed separately as it appeared to be a mean for adapting the magnitude and the probability of loss of a situation to the risk profile of the organization. The first section details the link between the framework and the growth options. Finally, this chapter concludes with summary of the contribution of the research, and suggestions for future research.

DISCUSSION

Growth options and the management of risk in expansion strategy

The results of this research on risk support the behavioral decision approach rather than the financial view on risk presented in the literature review. In other words, managers of hotel expansion approach risk in terms of probability and magnitude of loss and not as the spread of all possible outcomes. Thus, and as suggested by the literature, hotel developers viewed the management of risk as contingent upon the probability and the magnitude of risk related to a contract. In sum, in accordance with the voluntaristic approach of strategy, hotel developers did not consider risk as the variance of probability distributions of possible outcomes. Rather, they approached risk and its management through its main elements, namely probability and magnitude of loss, and incorporated nuances such as downside risk and odd controls.

In line with this approach to risk, hotel developers employed growth options to align with the risk profile of a contract. In order to best illustrate how growth options are integrated into the framework a more managerial oriented version of the framework has been created. This version is illustrated below in Figure 11.

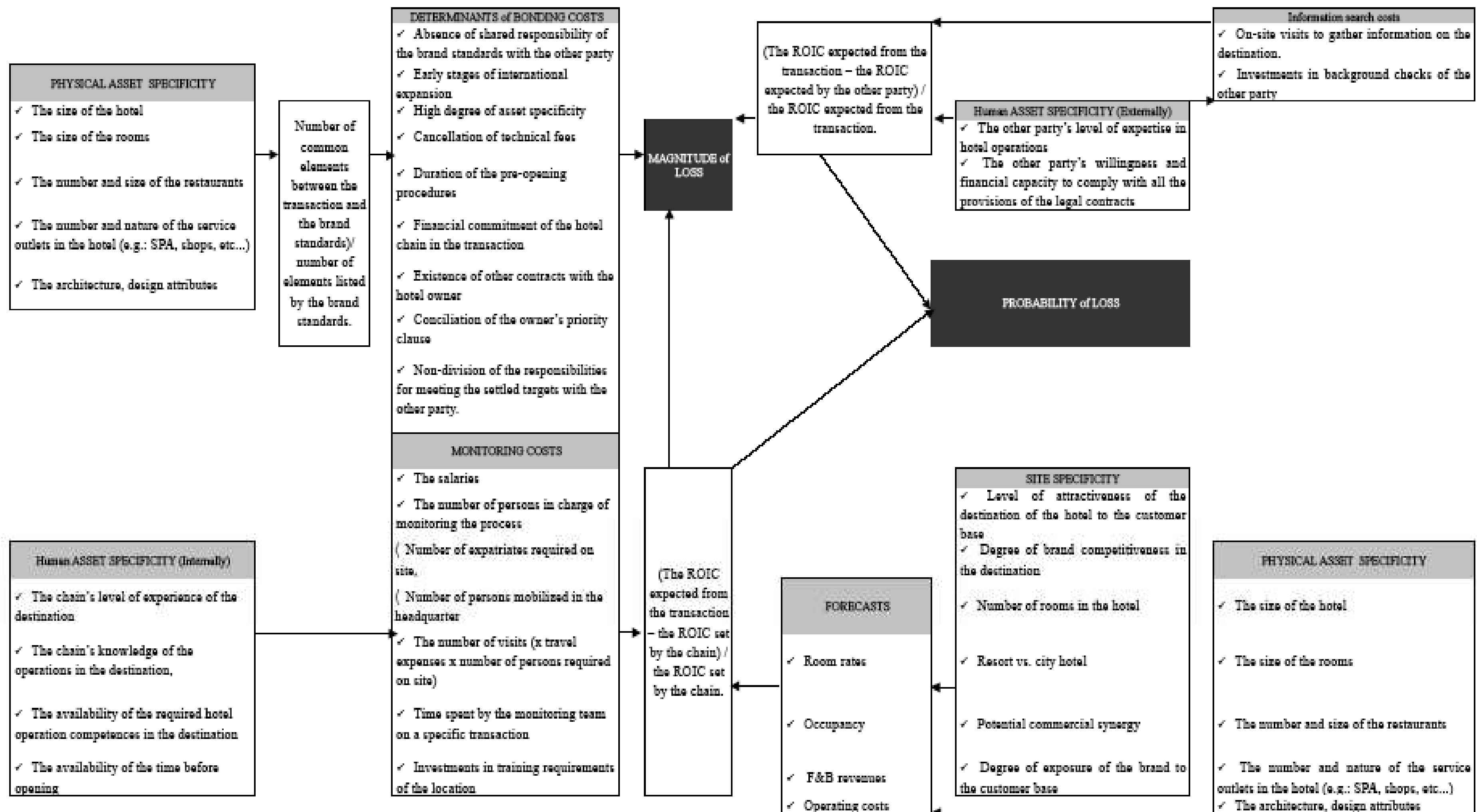
The risk-return trade-off in the selection of a growth option:

The premise for the integration of the growth option within the framework is derived from the fundaments of finance. As mentioned in Chapter 2, finance theory asserts that the higher the risk in an investment, the higher the return from that same investment is likely to be. In parallel, this study revealed that when the alignment in terms of brand standards and ROIC expectations is high, the probability of loss is likely to be low and the magnitude of loss is likely to be moderate.

In other words, when both types of alignment are high, the probability of losing in the transaction is likely to be low. Since finance suggests that it's a high risk situation that ensures return, managers can increase the amount invested in the transaction (magnitude of risk) to ensure a higher return. In these instances where the probability of risk is low, the magnitude of risk could be increased to enhance the possibilities of return.

Growth options are the tools that allow managers to take the optimum position in terms of probability or magnitude of loss. The following discussion illustrates this statement on a growth option basis. All the examples explained hereunder are related to a situation where both alignments (brand standards and ROIC) are high. As already mentioned, in this situation the probability of loss is likely to be low and the magnitude of loss moderate.

Figure 11 Measures of the determinants of the elements of risk



- *Management contracts*

The particular feature of the management contract is that the hotel chain does not pay most of the monitoring costs. The monitoring costs for both the achievement of the alignment with the brand standards and the ROIC expectations are the responsibility of the owner. First, the technical fees cover the monitoring costs for the alignment with the brand standards. Second, the owner, through the payroll of the hotel, also pays the monitoring costs for the achievement of the ROIC expectations. What this implies is that the magnitude of loss is likely to further decrease in the case of a management contract. The managers are thus faced with a low magnitude and probability of loss. According to the financial theory, the expected return in this situation should therefore be minimum. Therefore, in order to increase the return of the transaction, a financial investment, or a guarantee provision could be considered in these instances. The equity participation in such a transaction would increase the risk through the magnitude of loss and thus enhance the possible return to be gained from the transaction. This would be an optimum position for the chain in the transaction. Similarly, if the transaction already presents a high level of magnitude of costs (e.g.: if the bonding costs are high), no equity participation should be considered.

In essence, a "*dry*" or "*basic*" management contract is best suited for transactions where both the probability and the magnitude of loss are high. The lower the magnitude of loss, the more is the need for equity participation, or a guarantee option, in order to meet the optimum risk-return trade-off. If equity participation cannot be considered, then a lease is also an option.

- *Leases*

In light of the above illustration of the management contract, leases appear as an optimum choice for a transaction where the probability of loss is low, and where the magnitude of loss could be increased. In fact, by its nature, the lease differs from the management contract by a higher magnitude of loss. In the case of a lease, the magnitude of loss is a dominant element of risk, thus if the probability of loss is low, it is likely that the return from the transaction to be higher. Because of the dominance of the magnitude of loss in a lease, any transaction that might put further burden on the magnitude of loss could jeopardize the transaction.

In sum, leases are optimum in transactions where the both the probability and the magnitude of loss are minimum. In fact, by the dominance of the magnitude of loss in a lease, selecting this option permits the increase of the risk of the transaction and thus increases the chances of a higher return. Leases are optimum in transactions where the magnitude of loss is very low. In cases where the magnitude of loss is intermediate, equity participation could be considered.

- *Equity participation*

Similarly, equity participation increases the magnitude of loss. In fact, according to the TCT, equity involvement is a bonding cost. Simply put, in the case of equity participation, the lower the probability of loss, the higher the investment that could be made in the transaction.
According to the framework, equity participation should be considered in transactions where the probability of loss is low, and the magnitude of loss moderate. The equity participation would then permit the chain to position itself in an optimum risk-return situation.

- *Franchises*

Franchises could constitute the optimum growth option in transactions where the probability of loss is high, but the magnitude of loss minimum. However, in a franchise, the availability of operational and the managerial competences in the destination are the priority and the most important component of both the magnitude and the probability of loss. Thus, in transactions where there are available competences in the destination, both elements of risks are decreased and the chain could consider further investment with the franchisee to fully take advantage of the situation.

In conclusion, each growth option could allow the chain to optimize its position within the examined transaction. Figure 12 illustrates how a growth option could be selected to best take into account the elements of risk of a transaction in hospitality expansion. It is hoped that this first attempt to adapt the growth option to the strategy-structure relationship would help developers in their expansion efforts and prevent hotel chains from taking unnecessary risks.

Figure 12 Optimum growth option according to the elements of risk of a transaction

	Low probability of loss	*High probability of loss*	
High Magnitude of loss	Management contracts with guarantees Management contracts with equity participation	"*Dry*" management contract	*High Magnitude of loss*
Low Magnitude of loss	Leases	Franchise	*Low Magnitude of loss*
	Low probability of loss	*High probability of loss*	

CONTRIBUTION OF THE RESEARCH

The first contribution of this work is the scientific investigation of a commonly relied upon strategy in the hotel industry. Little can be found in either the academic or managerial literature on how developers manage their expansion. This work provides a detailed, theories-driven documentation about how expansion strategies are conducted in the international hotel context. Both academics and managers could benefit from this documentation. The findings of this research could be employed for the development of a scorecard, or evaluation grid that could guide developers in their efforts. Simply put, this research enhances our contextual knowledge of expansion strategy. As for the academic contribution of this work, it lies in its integrative efforts. Multiple research directions within fields of OT or strategy, such as learning organizations, or expansion could be derived from this work. The main research orientations that could be driven by the results of this work are discussed below in the chapter.

In addition to providing a scientific documentation as to how international hotel chains manager their expansion, this work contributes to the body of knowledge with its integration of three different fields within one study. This research is, therefore, an example of how theoretical knowledge from the fields of finance and OT could contribute to the enhancement of research in strategy. It is also a clear example of the vast possibilities that could emerge from the integration of established bodies of knowledge. Indeed, this research not only uncovers measures of alignment between strategy and structure (i.e.: alignment with brand standards measures and

alignment with ROIC expectations) but also reveals future research possibilities for the field of strategy. In particular, the contribution of this study to the research on strategy is twofold:

First, it offers refinements to the definition of risk from the perspective of strategy. As pointed out in Chapter 2, the definition of risk in strategy suffers from a lack of construct validity. As demonstrated in Chapter 2, the body of knowledge of strategy suffers from a lack of consistency in its approach to risk as it borrowed its definition of risk from the field of finance. This research contributes to this lack by suggesting approaching risk from the behavior management of risk. In other words, as proven through this research, the operationalization of risk from its two elements (probability and magnitude of loss) not only offers a more consistent definition of risk to strategy, but also enhances the comprehension of expansion strategy.

Second, it constitutes a proof for the benefits of integration for the field of strategic management. It is the integration effort that allowed the discovery of variables such as control costs or constituents of asset specificity. Similarly, it is the theoretical integration of the three fields that permitted to link these variables in the context of expansion strategy (these links are presented in the theoretical framework in Chapter 5). In essence, this research revealed bridges between the fields of finance, management, and strategy through the determinants of control.

Form a methodological standpoint, this study is an encouragement for further exploratory efforts in the development of knowledge in strategic management. The multiple-case study investigation that combines both a deductive and an inductive effort reinforces the validity of the findings of the integration and appears as a valid tool for our understanding of strategy.

Moreover, this study offers a new approach to measure the alignment between strategy and structure. The notion of alignment is key to both OT and strategy research and has been the subject of extensive research. This work not only suggests an innovative contextual measure for alignment, but also offers links with organizational performance. In sum, this work proposes the examination of the strategy-structure through a new angle. This new approach, ultimately, provides tools to measure the alignment of a hotel deal with the strategy. In essence, the findings of this research enhance our comprehension of the components of value creation in hotel chains. But most importantly, this work provides another evidence for the relevance of the co-alignment approach in the research on strategy. The inductive effort applied to this research provides further support for the co-alignment model (Olsen et al. 1998) and directs towards further research for its full investigation.

Finally, the findings of this work could be employed for teaching purposes. In particular, the managerial framework presented in this chapter (Figure 11) could be relied upon for pedagogical purposes in a strategy course. Students could study the components of the framework and examine the effect of each of them on the risk taken. Simply put, this framework could be relied upon for illustrating the role of value drivers in the strategic decision making process.

Managerial contribution

Expansion is at the heart of strategic management in the hotel industry. But not only is expansion widely employed, it is also required to be the main driver of performance for hotel chains. However, the question of the contribution (or lack of contribution) of unit growth on performance is still not fully investigated. The four examined cases were undertaking major expansion efforts during the data collection. This study offers guidance for the comprehension of the determinants of risk in the expansion strategy of international hotel chains.

The managerial framework that is discussed in this chapter (Figure 11) could be used to build a development grid analysis that not only permits the estimation of the risk-return trade-off offered by a transaction but also allows the selection of an optimum growth option. In other words, this framework could be employed as a “development scorecard” where all essential value drivers are listed for analysis. Figure 11 synthesizes the determinants of risk in development for hotel chains. In sum, the framework could be employed as an analysis tool that can support the decision making process. This is the next step of future research.

In alignment with the risk-return paradigm of finance, this work offers new leads for the implementation of hotel development. Simply put, the findings of this research encourage the adaptation of an optimum growth option for each expansion situation. These results might help senior hotel developers challenge the cautious approach to development that consists in offering pure management contracts. Indeed, depending on the risk profile of a contract, other growth options might be more appropriate than a management contract in order to maximize the returns on a transaction. This work reveals that higher returns could be extracted in certain situation with the employment of other growth options.

LIMITATIONS

This study is based on a new model using newly developed interview questions. Despite the efforts made to ensure the quality of these instruments, replication would be the best means to further sustain both validity and reliability.

Overall, the limitations of this research endeavor are inherent to the qualitative research and to case studies in particular. First, this study was carried out in international hotel chains. Therefore, the uncovered measures are highly contextual, which limit their generalization to expansion strategy within the hospitality industry. Also, the number of hotel chains available in the field could not make up a statistically acceptable sample size. As a consequence, this research suffers from a lack of quantitative measures. This shortage in quantitative measures makes it difficult to assess which are the most important relationships and which are simply specific to the four particular cases studies. Despite these limitations, using case studies permitted the discovery of the measures presented in chapters 4 and 5.

The data collection process in the field also constituted limitations to the study. The case study protocol had to be accommodated with the constraints of the field. In particular, the interviewees set the timing of the interviews at their best convenience. As a result, it wasn't possible to conduct each case study separately. This might have allowed for interferences between the results of the case studies. To prevent this overlap between cases, prior to the data reduction process and analysis, rigorous reliance on field notes and application of the case study protocol was followed. In addition, the analysis was conducted on a case-by-case basis once all the interviews were completed and all documents gathered for one chain.

Also, part of the constraints of the field was the pressure for confidentiality about the subject of development. This issue made it difficult to examine certain questions with more depth. In every case, interviewees were very cautious about delivering financial figures. In particular, no developer was willing to provide details about the amount of the technical fee, or the marketing budget for one hotel or any other performance element. To overcome this constraint, basis for computations rather than the figures were asked for. For instances, developers were asked how they did compute the technical fee, but not about how they actually charged the owner.

Finally, a theoretical limitation is present in this study and is related to the initial perspective chosen for the work. This research suggests that the relationship between strategy and structure should be examined through the lenses of control. This proposition contributed to the research findings but also to its limitations. This approach made it difficult to contrast and suggest other contradictory theories with the one related to control. This can be a direction for future research.

FUTURE RESEARCH

First of all, quantitative tests of the framework are required. Historical measures of the components of the framework could be collected and linear regression conducted on the determinants of the elements of risk. If these tests are conducted at the transaction level, the issue of the limited sample is eliminated and quantitative research could be conducted to validate this framework. Of value for future research would be not only the quantitative test of the framework, but also the investigation and test of the optimum growth option relationship discussed above. These are the two main directions dictated by this research. In addition, the following investigation paths are also suggested.

Performance of expansion strategy

Surprisingly, expansion strategy is a widespread practice in the hotel industry while little, if nothing, is known about the positive impact of unit expansion on the long-term performance of organizations. In Chapter 2, latest examinations on the real impact of growth regarding firm performance and its value creation capacity were presented. In essence, it appeared that this research decreased our confidence with respect to the positive long-term impacts of growth (Chathoth and Olsen, 2007; Zook et al. 2000; Zook and Rogers, 2001). But revisiting these statements in light of the findings of this study revealed new research directions.

First, when Zook et al. (2000) examined the performance of 1,854 companies between 1988-1998 and noted: "*that revenue growth alone has little or no impact on shareholder value. In fact, companies that grew revenues were more likely to destroy value than create it!*" (2000: 3). But the flaw here is that he examined revenues and not ROIC. Based on the findings of this study,

value creation should be examined from the ROIC of the transaction and not for the revenues generated from it.

Equally, Chathoth and Olsen (2007) applied a linear regression model relating sales growth with return on equity and growth potential with free cash flow per share. Their conclusions were that "*growth strategies do not help explain a significant amount of variance in firm performance.*" (2007: 78). It would be interesting to examine the result of a linear regression model relating ROIC from a transaction with return on equity and expected ROIC with free cash flow per share. Overall, the research efforts on long-term performance of expansion strategy could employ ROIC per transaction as a variable.

Management of risk in expansion theory

In the proposed framework, the question of brand risk is integrated in both the elements of risk and bonding costs. However, since brand appears as key in the management of expansion strategy, its role on long-term performance of hotel chains should be further investigated. In particular, different levels of brand strength could be integrated in the quantitative tests of the relationships of the framework. Simply put, the role of brand in the management of risk in expansion strategy could be the subject of future research.

The four chains investigated in this research focused on different growth options for their expansion efforts. While all of the four chains primarily offered management contracts, their offer on the other growth options varied. The Pilot Case, for instance, tries to reduce its equity offer and did not offer leases. Cases A and C, on the other hand did offer leases and equity participation despite their different approaches to expansion. At this stage a question is left unanswered: Why, in a same market, would two similar chains offer different growth options? In particular, is the risk profile of the managers of a chain a determinant in the final selection of a growth option? Future research could examine the influence of the risk profile of managers on the proposed framework.

Finally, the cross-cases comparison revealed that control in Case C, the largest hotel chain of the sample, is shifting from a behavior-base control to a more output-base control. This link between size of the structure and control enforced in the organization in the strategic context could also be further researched.

In order to limit the effects of size[5] on the observed relationship between strategy and structure, the four case studies were chosen with different sizes. As a result, the findings of this investigation are common to four international hotel chains that present drastically different sizes. In other words, this study aimed at maintaining size as a control variable.

Despite this effort in reducing the effects of size on the relationship between strategy and structure, the development stage of the brands, an organizational phenomenon related to size was still observed. As briefly discussed in the introduction of Chapter 5, each case study approached its expansion strategy from a different angle. This angle was related to the stage of development of the brands in the portfolio of the hotel chain. In other words, the expansion strategy did depend on the development stage of the brands that were managed by the firm. Simply put, despite maintaining size as a control variable, its effects emerged in other aspects of the expansion strategy.

Since size is a key variable in research on OT and strategy, it is recommended that future research could further explore the implications of size and development stage in expansion strategy of hotel chains. For instance, future efforts could be oriented towards examining the effect of the development stage of brands on risk in the managed expansion transactions. It is suspected that the development stage could have a moderating effect on the propositions of the present work.

Expansion and Organizational Theory

The hotel industry environment is symptomatic of a non-transparent market where a common or previous contact is often the most important source of information. This highlights the role of information and agency issues in the hotel business. The centrality of task programmability and information search costs in the proposed framework indicates that information is essential in the expansion of hotel chains. For instance, the existence of previous or planned hotels in a targeted destination increases the level of task programmability through its impact on the planning for the human resources element. In a broader sense, when the chain has already operated in the destination or has been prospecting the region for another unit, it is very likely that this would affect the risk elements of a transaction. Simply put, the contextual

[5] In this study, size is defined as the total number of hotels in the network of the hotel chain.

knowledge and competencies available in the chain appear to have an impact on the performance of the expansion strategy.

The proposed framework could benefit from further integration from the work on organizational learning. In particular, the findings related to the transfer of knowledge and its link to performance could be further integrated to this work. Guidelines to further define the suggested measures could be offered. Equally, this research could be a support for future research on the strategic role of knowledge in organizations.

For instance, the study revealed that the central person in the transfer of knowledge was the general manager of the hotel unit. His role is to align the operations of the hotel unit with the market through the monitoring of the activities. Work on learning organization could help better define the knowledge and competences that could be developed. It could also help refine the measures of the costs related to human asset specificity and its impact on risk in a transaction.

In line with the link between control and learning in the organization, future research could further examine the link between the control-base system and the learning processes in an organization. The example of the learning process in Case C could guide further integration efforts in research. Case C uses the information collected to control its transactions for learning purposes. In fact, the information collected through its information systems is studied for learning purposes. The impact of this process on the cost of learning and the strategic contribution of learning could constitute a future direction for research.

Also in accordance with this suggested research directions, two sub-research questions were left partially unanswered and call for further investigation. In particular, the questions of why and how does the introduction of the new unit modify the control in place in the chain? And how is the modification of control, through the introduction of a new unit, assessed? These two sub-questions for research did not receive full answers. Subsequent research could examine the post-implications of expansion strategy on the structure of a hotel chain.

In line with this suggestion, research from OT on stewarding could also enhance our comprehension of the determinants of performance in expansion strategy. This research reveals that, in the hotel industry, human relationships are essential to maintain control over a transaction. In fact, developers explained that the legal contracts present a safeguard, but do not cover for all the types of risks incurred through the transaction. Thus contracts are completed by behavior control, or trust in the relationship. These mechanisms allowed increasing task

programmability, reducing uncertainty, and decreasing other control costs such as information-search costs and bargaining costs. "*The contract is as good as implemented*". In particular "*trust*" is often presented a means of control in a transaction. Future research could examine the determinants, the costs, and the impact of trust on long-term performance of hotel chains.

SUMMARY

This study is an exploratory investigation of how strategy and structure relate in the hotel industry context. The relationship between expansion strategy and structure in four international hotel chains has been investigated from the perspective of the construct of control.

A refined framework describing the link between expansion strategy, hotel chain structure, and elements of risk resulted from the analysis of the data in this study. The framework not only synthesizes how strategy and structure relate in the management of risk, but also provides measures for the proposed relationships. In addition, the use of the framework as an analysis tool for growth option selection is discussed in this chapter.

By and large, the contribution of this study is in the documentation of the development process of expansion strategy in the hotel industry. In addition, the results of this work could be used as a decision-making tool in the hotel expansion context. Finally, the integrative effort conducted in this research directs towards multiple new tracks for future research in both the fields of strategic management and organization theory.

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APPENDICES

APPENDIX A : PLURAL MIXES IN FOUR INTERNATIONAL HOTEL CHAINS (1998-2005)

Marriott	2005			2004			2003			2002			2001			2000			1999			1998	
	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units
Host Mariott																							112
Owned/leased	0.6%	17	183%	0.2%	6	-25%	0.3%	8	-33%	0.5%	12											15%	220
Contract mgmt	37%	1017	7%	35%	947	1%	37%	937	2%	38%	916	-2%	44%	931	6%	47%	882	10%	48%	803	58%	34%	509
Franchised	62%	1707	-3%	65%	1765	9%	63%	1612	9%	61%	1482	27%	56%	1168	17%	53%	998	13%	52%	883	18%	51%	749
Total	100%	2741	1%	100%	2718	6%	100%	2557	6%	100%	2410	15%	100%	2099	12%	100%	1880	12%	100%	1686	14%	100%	1478

Hilton	2005			2004			2003			2002			2001			2000			1999			1998	
	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units
Owned	1.3%	30	-0,4	2.2%	50	-0,09	2.6%	55	-0,13	3.1%	63	-0,03	3.3%	65	-16.7%	4.1%	78	-8.2%	4.9%	85	-11.5%	6.1%	96
Leased	0.3%	6	-14%	0.3%	7	0%	0.3%	7	0%	0.3%	7	-0,22	0.5%	9	-87.7%	3.9%	73	-1.4%	4.2%	74	7.2%	4.4%	69
Joint Venture	2.3%	54	-17%	2.9%	65	-3%	3.1%	67	3%	3.2%	65	0%	3.3%	65	6.6%	3.2%	61	8.9%	3.2%	56	-3.4%	3.7%	58
Contract mgmt	8.9%	210	2%	9.2%	206	0%	9.6%	206	2%	9.8%	201	-4%	10.7%	210	10%	10.1%	191	3%	10.6%	185	5%	11.2%	177
Franchised	87.3%	2'054	8%	85.3%	1900	5%	84.4%	1'808	5%	83.7%	1'721	7%	82.2%	1'612	8%	78.7%	1'492	10%	77.2%	1'352	14%	74.8%	1'186
Total	1	2'354	0,06	100%	2'228	0,04	100%	2'143	0,04	100%	2'057	0,05	100%	1'961	0,03	100%	1'895	0,08	100%	1'752	0,1	100%	1'586

Accor	2005			2004			2003			2002			2001			2000			1999			1998	
	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units
Owned	0,24	984	0,06	0,24	927	0,03	0,23	902	-0,03	0,24	928	0,01	0,25	921	-18.4%	0,32	1129	1.7%	0,34	1'110	17.0%	0,36	949
Leased	0,37	1'510	-1%	0,39	1526	-2%	0,4	1'553	2%	0,4	1'520	0,04	0,4	1'465	26.7%	0,33	1156	5.1%	0,34	1'100	26.3%	33%	871
Contract mgmt	13%	524	-2%	14%	535	13%	12%	475	-2%	13%	484	-5%	14%	512	-4%	15%	531	16%	14%	456	24%	14%	368
Franchised	26%	1'047	10%	24%	949	-2%	25%	964	7%	23%	897	19%	21%	752	12%	19%	672	18%	18%	568	24%	17%	458

Total	100%	4'065	3%	100%	3'937	1%	100%	3'894	2%	100%	3'829	5%	100%	3'650	5%	100%	3'488	8%	100%	3'234	22%	100%	2'646

	Sol Melìa																						
	2005			2004			2003			2002			2001			2000			1999			1998	
	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chage	Mix	Units	Chge	Mix	Units	Chge	Mix	Units	Chge	Mix	Units
Owned	0,31	102	-0,03	0,32	105	0,02	0,31	103	0,01	0,29	102	-0,01	0,29	102	N/A	0.0%		N/A	0.0%		N/A	0.0%	
Leased	0,14	46	0%	0,14	46	-1%	0,14	46	2%	0,13	46	-0,01	0,13	46	N/A	0.0%		N/A!	0.0%		N/A	0.0%	
Contract mgmt	44%	144	0%	44%	144	-3%	45%	149	-13%	49%	172	2%	48%	169	N/A	0.0%		N/A	0.0%		N/A	0.0%	
Franchised	11%	36	10%	10%	33	-1%	10%	33	5%	9%	32	-11%	10%	35	N/A	0.0%		N/A	0.0%		N/A	0.0%	
Total	100%	328	0%	100%	328	-1%	100%	331	-5%	100%	350	-1%	100%	352	5%	0%	335	28%	0%	262	7%	0%	246

APPENDIX B : SNAPSHOT OF THE ELECTRONIC FILE SENT TO THE PANEL OF EXPERTS

The Purpose of the panel : validate 51 questions that will be used for interviewing hotel chains' development teams on their latest expansion decisions.

Topic: The questions relate to a contract between a hotel chain and a specific hotel unit of this chain's network.
The contract can either be a franchise, a management contract, a lease, or a joint venture.

Structure: There are 51 questions covering 10 constructs (construct A to construct J)
- Each of the 10 constructs is defined
- Following the definition, questions created to examine the construct are presented for rating

Instructions: The entire process is **electronic**.
1. Click on the rating question (*i.e.: How favorable are you with using this question to examine construct X?*) to reveal the multiple choice list icon.
2. Click on the icon in the right of the cell to reveal the multiple choice list.
3. Click on your answer in the list.
4. Proceed to the next question.
5. Save the document.
6. Email it back.

Construct A. Asset specificity	***Definition:** Asset specificity refers to the degree of uniqueness of an asset to a contract. In other words, an asset that is highly specific to a contract is difficult to transfer or use in another contract.*
Question 1: What were the reasons for signing with this particular hotel unit?	
	Strongly favorable
Question 2a: Would you say that the profile of the hotel unit is consistent with the one of the hotel chain?	
	Somewhat favorable
Question 2b: If yes, in what regard?	
	Strongly favorable
Question 3: Is the level of your pre-opening commitment (both in terms of efforts and money) comparable to other contracts you have signed lately?	
	Strongly favorable
Question 4a: Did you need to make special arrangements (i.e.: addition of special clauses to the standard contract, increase in financial participation) or spend more time for this particular hotel u	
	Somewhat favorable
Question 4b: If yes, what were these arrangements?	
	Somewhat favorable
Comments on the above questions related to Construct A:	

There are three types of asset specificity:
- Site Specificity (Construct B)
- Physical asset specificity (Construct C)
- Human asset specificity (Construct D)

Construct B. Site Specificity	***Definition:**Site specificity is when the location of the hotel unit provides an advantage to the hotel chain.*
Question 5a: Is the hotel location interesting for your hotel chain?	
	Strongly favorable
Question 5b: If yes, in what regard?	
	Strongly favorable
Question 6: Would there be any cost reduction advantages gained with this new unit?	
	Somewhat favorable
Comments on the above questions related to Construct B:	

APPENDIX C : INTERVIEW PROCEDURE AND QUESTIONS

Interview procedure and questions

Setting for the interview:

After introduction, the interviewer will review the purpose of the research project.

Purpose of research project: Study how international hotel chains manage risk in the context of their expansion strategies. It is hoped to uncover elements that would support managers in this task.

The person being interviewed will be asked some general questions about her role within the company, the development efforts of the company, as well as a series of specific questions about the latest negotiated contracts.

It will be further explained that the interviews are being recorded, but that all of the contents of the recordings will be kept ***confidential.***

General questions:

- May I ask you to briefly describe your role (responsibilities and duties) within the company?

Development: The following questions are related to your chain's development effort.

- What are your targets in terms of expansion?
- I have listed here four types of contracts that are most common to the hotel industry. Can you tell me which one do you sign to meet your development plans?

___ Franchise
___ Management Contracts
___ Leases
___ Contracts requiring equity participation (ownership, Joint Ventures…)
If other: ____________

As we go through the process, might it be possible for me to ask you for the documents you might mention?
HERE EXPAND (frequency, time, etc…)

Explain the interview structure:
When was the last (name applicable) that you have signed?

Management contract: __________________________

Franchise: _________________________________

Lease: ___________________________________

Equity involvement contract: _______________________

HERE EXPAND
The following questions relate to **each** of these last contracts:

Interview questions:

	In the case of the Franchise contract	In the case of the Management Contract	In the case of the Lease	In the case of the contract involving Equity participation
1: In what regard was the profile of the hotel unit consistent with the portfolio of the hotel chain?				
2: When you think of your pre-opening commitments, do they differ (both in terms of efforts and money), across the different contract types?				
3: Did you need to make special arrangements (i.e.: modification of the chain standard requirements, increase in financial participation) or spend more time for this particular hotel unit? *EXPAND on contract length and renewal options.*				
4: Can you please tell me the key criteria you relied upon in choosing the location?				
5: Did you invest in the hotel's general infrastructure (architecture, design, furniture and equipment) before its opening under your banner? *EXPAND on the level of the investment.*				

6: Did you invest in operation and marketing activities before the opening of the hotel under your banner? *EXPAND on the level of the investment.*				
Now, I would like to ask you about the mobilization of the human resources capabilities:				
7: First**,** how important is the human Resource capability (at the corporate level) in the decision to sign?				
8: Did the contract require particular investment in human resources? *EXPAND on the level and details of investment.*				
9: What is the role of the persons involved in the project?				
Let's discuss the capacity to plan for the details of the contract:				
10: Was this your first contract in the hotel's area?				
11: Was this your first contract with the other party? *EXPAND: if no: what other contracts? Can you tell me if you consider those past contracts as successful?* *If yes, what information did you look for prior to signature?*				
12: Do you differentiate the obligations of the hotel unit representative among the four				

contracts?				
The following questions relate to the information system in place in the contract:				
13. When you think of the targets or standards you impose on the hotel representative, did they differ across the four contracts?				
14. What type of information is the hotel representative required to transmit to you?				
15. What information are **you** required to transmit to the representative of the hotel unit? *EXPAND: Is it used for the assessment of the compensation? What information is used to assess compensation?*				
17. What other information is exchanged? *EXPAND on the means used and form (formal or informal).*				
Now, I would like us to discuss control related costs:				
18. Do you have a reporting system in place? *EXPAND on outputs.*				
19. Did the contract require further investments in the reporting system? *EXPAND on date of creation and evolution of the system.*				
20. Who is in charge of monitoring the unit's activity?				

EXPAND on role (meetings), and degree of specialization of the person.				
21. Did the chain invest in systems supporting this person's activity (Information systems and reporting systems)?				
22. Was an opportunity cost estimated by your financial team? *EXPAND on the estimate and the assumptions used for the estimate.*				
23. When you think of the process that your chain has been through until the final signature, does it differ across the four contracts? *EXPAND on length and revisions on the contract.*				
The following two sections relate to your assessment of the outcome uncertainty of each of the four contracts:				
24. Would you say that each contract overall estimates were accurate within what % of accuracy (ie: ±10%)? *EXPAND on breakdown of estimates: RevPar, occ or costs.*				
25. How would you rate the political stability of the hotel location on a 1-5 scale, where 1= very unstable and 5= very stable?				
26. How would you rate the quality of goods & services				

available in the location on a 1-5 scale, where 1= very poor and 5= very good?				
27. How would you rate the level of taxation in the unit's location on a 1-5 scale, where 1= very low, 5= very high?				
28. How would you rate the stability of the hotel location's local currency on a 1-5 scale, where 1= very unstable and 5= very stable?				
29. How would you describe the infrastructure in the local destination?				
30. Is this infrastructure sufficient for the support of your chain's goods and services standards?				
31. How confident are you about the other party's successful contribution to the contract? (1. Very confident, 2. confident, 3. somehow confident, 4. Somehow unconfident, 5. Unconfident, 6. Very unconfident)				
32. Are you concerned about the possibility for the hotel unit representative to misuse your name for his/her own benefit at your disadvantage?				
Risk elements:				
33. If the deal were to be				

cancelled, how would each contract differ in terms of the loss involved? *EXPAND on elements of the loss and amount of loss.*				
34. Do you differentiate among the potential threats posed by each contract to your company?				
35. When you think of the risk involved in each of the four contracts, which element is most important to you: the probability of loss or the magnitude of the loss?				

Documents:
Letter of intent
Standard requirements sent to a prospecting hotel owner
Memorandum of understanding
Contract (for each type) that they would be willing to share
Any document related to the project's estimates (P&L, external feasibility studies, etc…).

Might it be possible to contact another person within your department for a similar interview?

THANK YOU!

Follow-up: a summary of this interview will be sent for your review. If you could please examine it to ensure that your comments have not be distorted.

APPENDIX D: DATA REDUCTION MATRICES: SUMMARY BY INTERVIEWEE, BY CASE

Pilot Case	
Interviewee 1	***Expansion mode:*** 2 models are used in this company: management contract and franchising (With presently 60% of the agreements being management contracts). The company is perceived as a "*management company or as a branding company*". It has two main objectives: 1. Maintain a stream of fees over the length of the contract and 2. Extend the size of the system.
Interviewee 2	***Expansion mode:*** development is based on management agreements and franchise license in "*strategic markets*". Do not sign leases, do not take equity stakes.
Interviewee 3	***Expansion mode:*** management agreements and franchise in "strategic markets". Do not take equity stake. Development is "*expansion of our brands*".

	Organizational features of hotel unit
Pilot Case	*Asset specificity*
Interviewee 1	• The location and the hotel correspond to a list of criteria ("right profile of location and the right access"): ✓Capital cities ✓Seat of governments ✓Industrial or commercial centers ✓ Resort location ✓Access ✓Proximity to business district, city center, transportation. ✓Development of the system • Location: "site suitability" ✓ The changing characteristics of location HIGH • Physical aspects: ✓Building attributes ✓Building compliance with the brand standards ✓Size of the hotel (!) ✓No money participation HIGH but no financial commitment. • Pre-opening commitments: ✓ Degree of sophistication and competitiveness in the local market. ✓Changes in incentive fees ✓Support to the hotel owner and developer. But on a consultancy basis. LOW → Fee structure is related to the level of competition in the market. → Fee structure: standing assignment, incentive fee, and priority return. • Compliance of the hotel with the brand. • Human asset specificity: ✓Team of consultant: operations, finance, and lawyers. *HIGH, but paid by owner.* *Lower for franchise than mgmt contract.*

	→ Asset specificity is defined in terms of brand: customer and system perspective.
Interviewee P.2	• The degree of advancement of the project: whether it is an existing project or a conversion affects the asset specificity. • The location is part of the strategic market as defined by the company: the strategic market is "where we saw the greatest potential for growth" for the company. ✓ Supply level of the market ✓ Presence of other management companies in the market ✓ Potential of the market, or demand generators ✓ Strength of the destination (RevPar, occupancy rates, GOP, and EBITDA of existing hotels in the destination): "prominent city-centers, good accessibility, good visibility". ✓ Business area ✓ Exhibition or conference facility. • Opportunity to enter a strategic market: potential of the unit from a commercial standpoint • Physical aspects: Brand standards requirements are met: ✓ Number of restaurants, ✓ Bars ✓ Ballrooms ✓ Meeting facilities ✓ SPA ✓ Room surface ✓ Bathroom standard requirements ✓ Correspond to the demand for the location (alignment of the structure with the segment) ✓ Brand systems and automatic infrastructure, ✓ Security infrastructure: means of escape, fire alarms, etc… • Pre-opening commitments: ✓ The history of deal imposed timing issues on the pre-opening stage. ✓ The support team is growing: development offices and directors of development, support teams, brand support teams. • Human asset specificity: ✓ Lack of specialized staff (in emerging market) is becoming problematic: implication in hotel school settlement. ✓ The investment in the support and development team is structured along with the expansion. → "*Make sure that the opportunity matches what our strategy is*". Distinction: The concern over the outcome uncertainty differs whether it is a franchise or a management contract. The physical infrastructure (efficiency of design) is less of a concern in a franchise than when it is operated by the company.
Interviewee P.3	• Consistency of the asset is defined in relation to brand "our deals, are consistent, they have to be, to our brand." "When you do grow by management or franchise, you are always thinking of strategic locations where you are missing". • Certain elements or "icons" are in place in the hotel unit (these requirements vary from one brand to another): ✓ Meeting rooms ✓ Executive floor

	✓Checking desk ✓Executive lounge ✓Minimum room surface in square meters ✓Amenities in the bathroom ✓Amenities in the hotel correspond to the chain standards • Location: ✓Uniqueness of the location ✓Geographic dispersion of the unit compared to the rest of the network: "Presence for a chain equally all over the world". ✓LT future potential of the market location ✓First step and most important in the development process ✓Accessibility ✓Future development in the location ✓Current demand ✓International market situation • Pre-opening commitments: Vary widely ✓Construction issues: mainly delays (in turn delays the first installments). ✓Contractual issues These commitments are relates to the location and the availability of the supplies+ regulation[6] • Potential of a destination: ✓Potential is defined for the chain: at each country level: examine branded and non-branded hotels ✓Growth of the destination: hotel rooms built, occupancy, availability, demand. ✓Country indicator: development of the economic situation, increase of political stability and incentives, increase in foreign investment in the country/region ✓Potential for brand flagship → Flagship unit is the highest level of asset specificity for hotel chains. • Infrastructure: ✓Number of rooms ✓Category of the hotel ✓Type and number of facilities ✓Parking space ✓Number of restaurant ✓Amenities within the rooms • HR: ✓The key HR resource: the developer: as the job requires a large set of specific competences+ constraints (young and travel) or "difficult combinations". ✓Difficult to schedule for the number of developer that would be needed, as the exact number of projects is hard to predict ✓Long training required: 1 to 3 years. Average of 2 years before becoming independent developer. Related to the examined franchise contract ✓Distance and travel time: long distance and accessibility decreased the number of monitored hotels during a period of time

[6] The pre-opening commitments do not "lock" the party in the transaction as suggested by the TCT, rather they are obstacles or delays to the implementation of the standards and operating rules in the hotel unit. The operator will get paid for that extra-effort, but it will require more coordination and planning efforts.

	✓Distance and accessibility: Same issue for operation team Related to the examined management contract ✓Distance and travel time ✓Training period is an important variable ✓Number of expatriates in the hotel unit. This depends on the training period available and the level of training of the HR in the location

Organizational features of hotel unit			
Pilot Case	*Task programmability*	*Information system-base*	*Outcome uncertainty*
Interviewee P.1	• Existence of another operation in the market. • Existence of a familiar third party in the market. "*Because they are known to us, we're comfortable with them*". • Experience of the owner/developer with the market • Experience of the owner/developer with operating a hotel. • Assessment of the owner/developer to operate according to brand standards. • Instruct to commission an independent market study. • Determine market data • Produce feasibility study. • Identification of "pros and cons" of a location. • Look-up information on the Internet. • Conduct in-house analysis. • On-site visits • Request of due-diligence fulfillment. • Check background • Reliance on third party specialists to do due-diligence. • Programmability is difficult in terms of	• Reliance on OnQ as a IS platform. • The information transmitted varies with the type of contract: ✓Franchise: focus on sales ✓Mgmt: add the operating costs, or "costs of profitability" The accounting methods are used here as IS. • On-going investment. • Meetings with owners on a regular basis + informal meetings. • Accounting system for day-to-day performance.	• Comprehension of the historical performance of the market for assessment of uncertainty+ impact of future factors: ✓New supply ✓Changes in economic situation • Data on comparable hotels and locations • The management contract: low on political stability, low on quality of local goods & services, local currency is an issue if the business is based on local demand. • Concerns for the application of brand standards. The concern is higher in franchise contracts. • HIGH concern for name mis-use. Distinction: Due diligence might be more in depth for management contract.

	cost of building and opening a hotel + timing estimates.		
Interviewee P.2	• Previous transactions signed with the hotel developer or the intermediary. • Work with existing partners: i.e.: development and investment company. • Common known intermediaries. • Participation in the pre-opening steps. • Operating capacities of the franchisee. • Work with partners for the development. *→Partners with shared interests and past transactions.*	• Informal + meetings with hotel owners, developers and operators.	• The financing capacity of the hotel owner/developer • Changes of ownership for the hotel owner/ developer (related to political stability) • Reasons for the hotel developer/owner entrance in the deal with the chain. ("*The owner's own agenda*").
Interviewee P.3	• Who the owner is: what does he do? Will he deliver? • Funding structure • Financial situation • Administrative situation: i.e.: building permit, the architect, the building plans. • Due diligence • Ensure that the other party understands the terms and nature of the contract. • Cash flow streams are defined in the contract and are usually under standard clauses. • Number of hotels already owned	• Documents supporting the owner/developer structure and situation. • Performance reports • Guest comments • Quality audit teams • Mystery shoppers • IT reporting system	Outcome uncertainty is affected by • Timing • Quality of the end product Accuracy of estimate is affected by • Country whether it is a developed or under-developed region. However, when it is in under-developed country you tend to take into account unexpected delays. The examined franchise • 90% certainty in estimate • 5 on political stability • Quality of goods and service: good but expensive • Very stable currency • Confident about other

	• Number of persons representing the other party (i.e.: company headed by more than one person increases the difficulty to program for the task).		party: has other hotels in the location The examined management contract • 60% certainty in estimate • 4 on political stability • High taxation • Quality of goods and service: lower but cheaper • Lower taxation • Unstable currency, but most of the business in not in local currency • Other party: Large company headed by 2 persons. This is a concern.

<table>
<tr><td></td><td colspan="2">Organizational Control</td></tr>
<tr><td>Pilot Case</td><td>Behavior Control</td><td>Output Control</td></tr>
<tr><td>Interviewee P.1</td><td>• Approval process during the renovation or building
• # of visits increase as opening approaches
• Technical team (a fee is leveraged) of around 15 to 16 specialized persons. Legal team
• Operation & support teams
• Feasibility and investment analysis team: control of the development team and provides independent opinion.
• Meetings with owners on a regular basis+ informal meetings
• Obligations in terms of: brand standards, property, and property maintenance. “What they do physically with the hotel”.
• Regional offices monitor: customer standards and customer experiences

Distinction: Less involvement in franchise contracts.

• Elements of concern for franchisee selection: “right sills and infrastructure”.

→ Here the control is based on brand standard adherence: the objective is to control for the process. Brand protection.</td><td>• Outputs of reporting system: essentially accounting figures “full accounts”.
• The information transmitted varies with the type of contract:
✓ Franchise: focus on sales (revenues and occupancy)
✓ Mgmt: add the operating costs, or “costs of profitability” The accounting methods are used here as IS.
• Information is also available for franchisees (performance focus).
• Regional offices control: hotel financial performance. Comparison of budgeted and real performance.</td></tr>
<tr><td colspan="3">Development control process:
Developer proposes deal → legal council→ senior operator → president of operations → brand approval → technical team → back to development: End Phase 1
Developer → CEO and CFO (→ finance and investment committee for exceptional deals) → final OK.</td></tr>
<tr><td>Interviewee P.2</td><td>• Quality audit (throughout the year)
• Operation team is involved in the approval process.</td><td>•</td></tr>
</table>

<table>
<tr><td></td><td>• Go through the franchisee business plan and operational projections and future structure (“we want to really meet and understand the key staff that they are proposing”).
• Ensure the presence of full structure + personnel.
• Full support training (franchisee).
• In the US: UFOS.
• Management contract: ensure a common comprehension with the hotel owner/developer.
• Operating abilities of the franchisee.</td><td></td></tr>
<tr><td colspan="3"><u>Development control process:</u></td></tr>
<tr><td>Interviewee P.3</td><td>• Most of the control conducted by the technical and operation team is behavior: always required to be on-site to monitor.
Franchise:
• Adherence to brand standards: quality control
Management agreement:
• Quality teams for on-site visit
• Bonuses on the GM are based on quality standards

• Guest comments
• Quality audit teams
• Mystery shoppers
• Feedback from team members
“So we are pretty much aware of what is happening”.</td><td>• Due diligence by a third party.
• Guest complaints examination
• Feedback from the loyalty program members
• Performance reports
Franchise:
• Less outcome control, the focus is on behavior control and the maintenance of the quality of the brand.
Management agreement:
• GM bonuses are equally based on performance measures
• Financial reports:
✓ Occupancy,
✓ ADR, RevPar,
✓ GOP, and
✓ GOP percentage
✓ Departmental profit</td></tr>
</table>

	Control Costs	
Pilot Case	*Monitoring costs*	*Outcome Control Costs*
Interviewee P.1	• 1 or 2 persons dedicated to new hotels: based in the headquarter • # of visits increase as opening approaches • Last year, the technical team supervised 30 hotels. • Legal team • High-skill people (lawyers, engineers, "consultant type" positions). • Operation & support teams: traditionally 1 year before opening, it is a full-time commitment. • Feasibility and investment analysis team • Number of meetings depends on the hotel performance. • Regional offices are dedicated to monitor the hotel performance. <u>Distinction</u>: Less involvement in franchise contracts. → Monitoring costs are pre-dominant. However a fee is leveraged to cover them.	• Price of the investment in the reporting and OnQ system. + on-going maintenance. • Regional offices are dedicated to control the hotel performance. •
Interviewee P.2	• By project, an average of 4: 1 developer in the HQ + regional director + analyst and legal team member in the HQ. • Support team: internal tax advisors, insurance advisor, treasury advisor. • Operational support: VP of operations per area + team. • External legal advise is hired on a country basis. • Management contract: GM and VP of operations • Franchise: directors of franchise + brand support team.	• Management contract: GM and VP of operations • Reporting system. • Franchise: directors of franchise + brand support team.
Interviewee P.3	• Technical team: accessibility and distance from HQ increases the	• Reporting system ✓Financial reporting system: almost

	monitoring costs • Monitoring costs related to brand standards are low when the other party adheres to them. • Monitoring cost for the operation and technical team: number of hotel visits per week. • Monitoring costs: number of expatriates needed on the site for the pre-opening and early opening stages.	daily ✓ IT system ✓ Previous-year budget ✓ GM reports performance compared to budget ✓ Quality reporting system: Guest comments, loyal customer feedback, results from audit quality.

	Other Control Costs			
Pilot Case	*Residual loss estimate*	*Information search costs*	*Bargaining costs*	*Bonding costs*
Interviewee P.1	• Value the contract: NPV formula, • Discount rate varies based on market economics.	• Commission an independent market study. • Determine market data • Produce feasibility study. • On-site visits • Due-diligence form + documents → Information search costs are at the expenses of the hotel developer. • Internet and other accessible information (free). • Internal analysis (previously consultant employees). • Third party specialists Distinction: Due diligence might be more in depth for management contract.	• Legal team costs (a fee is leveraged for the developer/owner) HIGH but not at the expense of the chain.	• Maintained at minimum: "*our position (...) is usually a dry position and we're not putting cash or equity of any form into the deal*".
Interviewee P.2	•	•	•	• More focus on the owner/developer commitment to the deal.
Interviewee P.3	• Estimates of the impact on the sales of other hotels in the location.	• Due diligence by a third party. Third party in each region or country.	• Legal team cost. But included in the corporate overhead costs.	•

<table>
<tr><th></th><th colspan="2">Elements of Risk</th></tr>
<tr><th>Pilot Case</th><th>Magnitude of loss</th><th>Probability of loss</th></tr>
<tr><td>Interviewee P.1</td><td>• Example of magnitude of loss: food poisoning outbreak and its impact on the brand.

<u>Distinction</u>: More of concern in a management contract that in a franchise contract. However, in a management contract, the chain has the capacity to “do something about it”.</td><td>• Concerns in relation to the application of the brand standards.
• Risk of abuse and damage to brand reputation.

<u>Distinction</u>: the risk is higher for a franchise than management contract.</td></tr>
<tr><td colspan="3"><u>Note</u>: The higher the control over the operations the lower the risk for brand damages.</td></tr>
<tr><td>Interviewee P.2</td><td>•</td><td>• Performance of the hotel business and the destinations where the chain is present.</td></tr>
<tr><td colspan="3">• “The key is on market risk”: including political and economic risk.
• Franchise: operating ability</td></tr>
<tr><td>Interviewee P.3</td><td>• Assessment of the required financing: Examine the financing capabilities of the owner or developer.</td><td>• Looked for in: questionnaires, due diligence, market study, and examination of financing. Task programmability</td></tr>
<tr><td colspan="3">“Image and that the property will be delivered and per our image worldwide and to our standards and specifications”.
→The probability of loss is the most dominant concern and is related to the growth option nature. Since the amount is estimated and is the responsibility of the developer/owner, the main aspect of risk that the operator has to manage is the probability of loss; but first the estimate of the deal has to be determined, so that it is properly covered by the owner financial structure. → Behavior control systems are in place: “I guess that is why we went many steps ahead by asking for everything in place before we signed”.</td></tr>
</table>

Case A	

Interviewee	
Interviewee 1 *Head of development*	***Expansion mode:*** In order of frequency: 1. Management agreements (particularly this year) 2. Leases, 3. Franchise, and 4. Other structures involving equity. Franchise contracts are not the focus since the company operates as a master franchise provider. → Expansion as an operating company. Focus on the competency of the company: hotel management and operations. Development stage: The brand names are still to be developed internationally.
Interviewee 2 *Regional development manager*	***Expansion mode:*** Reliance on target markets (countries and regions) by brand within a time range. Only rely on management contracts to adapt to the region's circumstances There "*are no management teams here*" is the reason for not franchising. Only option sign with an international management team if present in the region. + Demand is for operators "*so many projects chasing too few operators*". Lease: the market is risky and volatile and developers expect a higher return than elsewhere. So the lease does not allow the delivery of such high returns. Determinant: return expectations of the developers in the region. "*Equity is very rare. Strategic equity maybe*". Not relied upon for the same reasons that apply to a franchise or lease and again → can respond to the demand with a management contract.
Interviewee 3 *Manager Business Development*	***Expansion mode:*** In the region of responsibility the focus is on the offer of management contract. Franchise is sometimes considered, but lease and joint venture is not considered in the region supervised. However, several types of contracts are offered: • Pure management contract • Management contract with a capped guarantee • Management contract with a threshold on the operating fees The expansion first aims at a presence of the chain in capital cities of the region. The reasons provided for this choice are: • The limited presence of the company in the region (new entrance of the market) • The demand from developers and owners in the region is for management contract • The flexibility of the management contract compared to other contracts (in terms of elements that can be negotiated) • The quality of hotel and management available in the region is not favorable for franchise • Size of the system of franchises offered is limited • The higher risk related to leases

Organizational features of hotel unit	
Asset specificity	
Interviewee 1	• The equity participation is one way to enter a new market or "*penetrate a growing market*"; It is an opportunity that is taken.

	"*It helps us to be the first one to get into a country, the first one raise the bar so high, which makes the entry barriers for other competitors strong*". • The new market can either be a new country or a new segment (i.e.: new area in a European city through an airport connected project). • The first criteria mentioned in the potential of the market. • Franchise contracts are in groups rather than on individual units: the chain sells the franchise to a master franchisee that then operates the hotel units. • The goal is to maintain a repeat business with other hotel management companies through the franchise contracts. • Franchise contracts are conducted in market where the brands are already established. • First criteria mentioned: an established operator is the master franchisee. • Leases: a good compromise to insure the location and not provide the funding. "*a way of not using your capital (…) to grow your brand and lock in good locations*". • A way to respond to the offer of hotel developers/owners. • The leases are offered for "*brand enhancing*" markets or locations. • The leases are offered in markets where the demand is stabilized with a required return corresponding to a stable market. • First criteria mentioned: stable markets permitting exposure. • Lease requires more commitment in time and effort. • Management contracts: a way to expand in a market or country after the penetration with JV and leases. "*To grow the numbers*". • The demand for management contracts is an indicator of the brand strength. • First criteria: the location in the area, in the market. • The destination: ✓ Affluent area in a city ✓ Size of the market respective to the region ✓ Local market coverage • The location: ✓ "*Brand driven*": a "*good location? Depends for which brand*". ✓ Demand ✓ Yield possibly offered to the hotel owner/developer: assessment of the rate, occupancy. ✓ The potential for brand enhancement. • Physical asset specificity is ensured through the signature of contracts that are still at the project stage. • Pre-opening commitments: Distinction between franchise and management contract, lease, or equity. • Franchise contract clauses are less flexible than the other types of contracts. • Pre-opening commitments vary from one country to other, mostly due to the legislation requirements and practices. • HR asset specificity:

	✓Related to behavior control: training programs ✓Required number of managers in a new operating unit. ✓HR asset specificity is also related to the time available before opening ✓HR asset specificity is related to the nature of the project: new construction, conversion, and asset management. More mixed team for first 2 types. ✓Operation team ✓Brand and concept team ✓Technical team ✓Development team • Time available before opening is a recurrent theme in the discussion on asset specificity.
Interviewee 2	• Asset specificity: ✓Located in a strategic city (first reason) ✓Placed in a good location ✓At development stage7 but far forward (allows early opening) ✓Allows early and first entry in a market before other competing brands ✓Early opening "demonstrate that you can operate across the country, you'll get more properties": Brand presence and expansion ground (respond to the large demand in the market" ✓Ensure high rates at early stages ✓Degree of competition presence in that market vs. the chain's presence • Location specificity: ✓Economical boom in the city ✓There is wealth in the city ✓Large population ✓Center district, heart of the economic boom. • Physical asset specificity: ✓Size of the hotel did not correspond to all standards of the chain ✓Exterior design mis-matched what is usually designed by the chain ✓Room sizes are ok ✓General layout ok ✓Still some development required and could be involved. ✓Plot size if the hotel is not built yet. • Pre-opening commitments ✓Commitment in the design and layout. "*if you can influence early on the concept and everything else, then it makes the job much easier down the road*". ✓Influence in the design to reduce the efforts of the technical team • Other investments (operations, marketing): ✓PR at the development stage before opening. ✓Marketing when the opening date approaches • HR asset specificity: ✓Timing (before opening) is a determinant variable for HR efforts ✓Included in the contract ✓Normal process: contract signature, design process, built process, then 6months

[7] Important because it guarantees that the operator has a saying in the infrastructure, but the drawback is timing.

	before opening HR.
Interviewee 3	• Asset specificity: ✓The growth option (in this case management contracts) allows meeting the company's growth target in a timely manner. "*We are not in those countries by lease. (…) Lease is much more difficult and time consuming and so on*". ✓Length of negotiation and timing required by the development team ✓The company has a brand in its portfolio that corresponds to the market context ✓Classification of the market (primary, secondary) ✓Resort or city hotel ✓Commercial potential in the future ("*the traffic, the transport systems (…) that will be built*") • Location specificity: ✓Commercial leverage from other units is possible ✓Possible synergy in terms of destination commercial potential (primary markets aliment secondary markets) ✓Ranking of the city or destination in the country in terms of size (the indicators vary with the development level of the country): • Population size • Economic indices ✓Ranking of the market of the destination within the country (primary is a city, resort is secondary). In the region, the capital is main market and the other cities are thus secondary ✓By country approach: taking into account the stage of development of the country • Physical asset specificity: ✓ Corresponds to the standards of the firm (room size is listed first, design second) ✓The stage of the construction: whether it is an existing hotel or a site ✓Agreement on the physical specificity before signature "*It's an element of the contract, otherwise, we wouldn't sign the contract*" • Pre-opening commitments: ✓The owner/developer is in charge of the pre-opening fees ✓Mobilize operating knowledge of the market on site ✓Mobilize operating experience of the market on site ✓Timing is based on the hotel location being a resort or a city destination. "*So for sure, the pre-opening phase will not only start, but it will start earlier than it would start for a city hotel*". ✓PR and marketing efforts to be initialized ✓2 objectives for the commercial effort: market the destination and market the hotel ✓Technical fees charged to the owner. A rule of thumb is applied for the computation of the technical fees. In weakly served destinations, the travel expenses are added to the technical fees. (Number of flight connections is factored in). • Other investments: ✓Depends on the type of management contract that was agreed upon ✓The entrance in a market is subordinated to the existence of another hotel in a higher ranked market. In other words, the chain will only enter a secondary market after having opened an operation in the primary market of the country

	→ The market (location or destination) affects the timing of the pre-opening (start time and length). The financial aspect of the pre-opening is less of a concern unless there is a divergence between the actual pre-opening costs and the fees charged to the developer • HR asset specificity: ✓GM is listed first. The requirement: a person with experience of the country or the market ✓The GM is an expatriate in these new regions ✓Operating team ✓Technical team 2 concerns: • The availability of key HR skills • The compensation through technical fees

Organizational features of hotel unit			
Case A	*Task programmability*	*Information system-base*	*Outcome uncertainty*
Interviewee 1	• Existing units operating in the same market. "*New construction project with very reliable partners who have done a lot of development on that site*" • Is affected by the nature of the project (new construction, conversion, and asset management) • Background check • Market study for non established markets • Reliance on internal knowledge (*intellectual capital*). • Site approval • Affected by the political stability of the region • Scoring sheet used • Increases in a lease with the existence of a FRI clause.	• Background check of the other party (sometimes at the expenses of the chain). • Financial performance are transmitted through the reporting system ✓RevPar index ✓P&L	• Behavior control is employed to counter outcome uncertainty. • Leases: the costs of maintenance Distinction: • More accurate estimates in a franchise: "*just a certain percentage of top-line and you are less sensitive to the changes*". • Most difficult: lease: "*you are responsible for the entire P&L*". • Equity is also difficult. • Management contract: reasonable estimate of uncertainty. • Follows the higher risk-higher return mechanic.
Interviewee 2	• First contract with the developer • Brought in, rejected; then re-examined after on site visit. • Owner's readiness to understanding • Assess during the development stage, the capacity to remain "*off-hands*". • Degree of training of the other party with the industry and the type of contract.	• No other party • Internal due-diligence ✓Registration documents for the land ✓Titles, etc… • Written form: heavily documented • Documents in chronological order: ✓Personal meetings with the hotel owner/developer ✓Summary proposal ✓Space plan to further discuss the concept ✓Technical services agreements ✓Documents exchanged between the technical team and the project managers/architects ✓Emails and other correspondence to	• Timing estimates of opening • Collaboration of the hotel owner • Very low in the region, as it is expanding rapidly. The revenues are higher than forecasted for. • Experience of the team is relied upon to assess the outcome uncertainty of the deal or hotel performance • The difficulty is related to the volatility of the region. • Labor costs are low • Expectations of payment by the local customers is high • As an operator the stability of the exchange rate is of a concern in case of large devaluations or fluctuations in the exchange rate

		achieve the construction of the hotel • First stages it is verbal information and agreements during meetings	
Interviewee 3	• Cooperate with a consultant specialized in the market • The consultant is located in the country • Contact with private investors, who are prospective hotel owners • Individual check on the hotel owner/developer (Internet) • The results will be contingent upon the development of the infrastructure in the region. The operation is related to whether the authorities will deliver the promised infrastructure on time. • In these countries (in the stage of development) the programmability is more difficult. "*You need to have the vision of thinking, especially in (*the region*), of imagining how this site will be, or how popular the site will be in let's say 5 years, 10 years, 15 years*."	• For information about the region and the other party: contract with a local consultant • The consultant is the facilitator of the transaction (hired by the owner to select an operator) • One visit on site before the start of the negotiation • Emails, telephone, conference calls during the negotiation process • Final meeting for signature is made in person • Reliance on informal means of communication between the owner and within the firm • A tracking or reporting system is in place for developers to report the advances of their work	• The development of the infrastructure of the region • The demand for the region by travelers "*The difficulties* (of the discussed contract) *are related to the destination, the marketing for the destination*." → The forecast of the demand for the hotel (occupancy and rates) is the key component of outcome uncertainty (especially in new tourist regions)

	Organizational Control	
Case A	*Behavior Control*	*Output Control*
Interviewee 1	• HR policy is a strong indicator of behavior control. "*Only 2 ways to enter our company is either through our hotel school or through acquisition*". • A formal process is in place for signing-off new contracts (includes 4 persons: brand manager, development officer, CFO, and CEO). • Project approval process or milestones for pre-opening stages for contracts in which the firm operates. • On-site direct monitoring (technical and other members of development) • Franchise: ✓Restrictions on the use of the brand name • Pre-dominant in franchise contract enforcement: ✓Compliance with brand standards ✓Control for the reservation system ✓Annual audit of a franchisee	• Leases: ✓Penalties in the contract (timeliness and performance targets) during the operations ✓Full-repair-and insurance clause • Franchise: Include milestones in the behavior control elements ✓Brand standards: signage, construction, design. • Management contract type ✓"*Straight*", ✓with a "*threshold*", ✓subordinated fees, ✓with guarantees • Top-line performance measures: ✓RevPar ✓Occupancy ✓GOP ✓Monthly basis ✓Accumulated basis ✓Forecasted basis ✓Performance against the market ✓Against previous years ✓Against budget • Customer satisfaction scores
Interviewee 2	• Involvement in the development process to influence the layout of the hotel.	• HR staffing by the operator is dealt within the contract. • Targets for the developers (constitute the basis for incentives portion of income) • On the GM of operating hotels (revenues and cost) • Taxes are incorporated in the contract • Contract clauses for the owner performance and obligations
Interviewee 3	• The control for the construction is also maintained through a close collaboration with the technical team of the hotel owner • Permanent and informal contact with the developer and his team members • Developers report on their leads, the stages of negotiation, the timing of the signature.	• The outcome of the hotel construction is a key performance outcome that is controlled for by the developer • Summary of proposal • Daft of contract • Final contract • Reporting system with monthly output • Revenue management outputs

	Control Costs	
Case A	*Monitoring costs*	*Outcome Control Costs*
Interviewee 1	• Approximately 30-50 hotels/year are monitored by the development team and other supporting teams. • Average number of visits by the hotel chain (mainly technical and operations tams): minimum 20 site visits sometimes double for technical team. • Technical and operation team control through monitoring " *They need to be physically there*". • Costs of franchise contract enforcement: mostly on site visits ✓Cost of monitoring compliance with brand standards ✓Cost of controlling for the reservation system ✓Cost of annual audit by external party • Regional directors and GM with the reliance on business plans as a control tool (3 years range and LT) • Regional director supervises approx. 15 to 20 hotels/region.	• Override costs of losing a signed contract by including "*wash-out*" in the forecast. • Reporting system
Interviewee 2	• The support and pre-opening commitment of the technical team. • Time spent by the technical team to get the layout "right" • Before signature: development team • Signature-opening: technical, operations (incl. pre-opening team), and liaison with other party through development team. • Technical services coverage before opening (not systematic) • Opening: operations • Management fees cover the monitoring during the operations. • Legal control by legal team in HQ and a clerk in the region. • Operation regional director to monitor the performance of operating hotels.	• Reporting system to the head quarter (advanced Access database)
Interviewee 3	• Meetings and close collaboration (time required from the chain's members) allocated to the control of the process of construction planning • Concentration of efforts during the	• The regional development manager + one technical member (i.e.: architect or engineer) are in charge of the hotel final output in terms of construction • Regional controller (to date,

	construction stage (technical team) and pre-opening (operating team) • Budget meetings and discussions • Regional controller, financial controller	overviews less than 20 hotels) • Revenue manager • Head of operations for budget setting

	Other Control Costs			
Case A	*Residual loss estimate*	*Information search costs*	*Bargaining costs*	*Bonding costs*
Interviewee 1	• Seldom taken into consideration, at lease in a rational manner. • ROI considerations are taken into account.	• Market study costs: very low, almost inexistent in established markets. • In less established markets, it varies with: ✓Degree of background check ✓Market studies ✓Political stability ✓Utilities ✓Government • Low if internal competencies and experience is available in the chain. • Lease is the contract that requires more information search	• Vary from one country to another. • Lower for franchises (more rigid clauses) • Higher for leases more than management contracts	• The shared responsibility of the brand. It is especially important in franchises: especially when the deal is signed and the franchisee does not deliver. • No litigations for recovery is advised • Bonding costs are at their highest in leases (more than equity) → Important finding
Interviewee 2	• Only considered in terms of competition taking over a "target" hotel or location- missed opportunity. • Following a lead, spending effort, and have it cancelled.	• Low because of the structure of the market: the demand comes to the chain	• Low if the owner is perceived as a good partner	• Waiving the technical services fees "*in favor of getting the contract*". • Contract signature, and threat of cancellation: "*the name is out, the PR machine is already working the hotel…*"

Interviewee 3	• Not taken into consideration	• Collaboration with a local consultant	• In the discussed example: 6 months involving the development manager, and 1 person from the technical team and the legal team. • The process can take between 6 months up to 1year and a half	• In case of clauses of guarantee to the owner • Length of the process constitutes a bonding cost

	Elements of Risk	
Case A	*Magnitude of loss*	*Probability of loss*
Interviewee P.1	• Most of the concern: "*how much we could loose: credibility and financially*".	
Types of risk: opportunity cost, financial risk, type of leasing. Risk of wrong party selection. Risk of wrong judgment that "*will destroy all the good things you did with the brand*". Risk of delays Risk of not opening → Risk of not achieving the announced expansion		
Interviewee P.2	•	• Probability of losing the contract is at heart of the risk managed.
• "*The risk is that we spend too much time on projects that don't yield and that's the hardest thing to juggle at the moment*." • "*Sign a contract that doesn't materialize*". • Mis-evaluation of the **demand** for the hotel unit. • Timing: act quickly and be on the market early.		
Interviewee P.3	• Relevant when there are guarantees involved • The magnitude would the compensation that the chain would have to offer	• Related to the forecast of the demand • Default of the hotel owner/developer
"*The forecast especially if there is a guarantee involved*, *or if there is some kind of financial involvement from our side*". Delivering the return promised to the owner Risk of not "occurring" because of financial problems and so on.		

Case B	

Interviewee P.1 *Head of Development*	***Expansion mode:*** Management contract is the main focus (98% approx. of the network. In rare instances, signature of management contract with GOP guarantee. Leads come at the regional and corporate level.
Interviewee P.2 *Director of development*	***Expansion mode:*** Expansion focus is on maintaining the consistency of the units with the brand. Management contract is the selected growth option for expansion.
Interviewee P.3 Regional VP	***Expansion mode:*** The preference is for management contract and this growth option constitutes most of the regional network. However, since the hotel demand in that specific region is for both leases and management contracts, both are signed. Leases with 2 components: a fixed and a % of NOP or GOP. Equity participation is examined but not at an individual hotel basis. "*We would prefer a management contract but it is not always possible. In certain areas you have to accept a lease or you have to provide certain equity in order to retain the contract or in order to get to the contract.*"

Organizational features of hotel unit	
	Asset specificity
Interviewee P.1	• Location: ✓Market with potential ✓Presence of ✓other chains operating in the same segment prospecting ✓market for the targeted customer segment ✓market potential to cater for meetings & incentives • Physical aspects: ✓The hotel is under development, increases the potential of coherence with the brand standards • Pre-opening commitments: ✓ Reduced by the fact that the owner had already worked with the chain on previous contracts → • Human asset specificity: ✓Local availability of the qualified staff ✓Cost of the required staff for managing the hotel unit. ✓Cost and planning for cost of the HR required ✓Responsibility of the regional offices
Interviewee P.2	• Asset specificity: ✓Existence of another hotel in the same city: synergies sought. ✓The history of the building and its image • Location: ✓ Part of the development targets for that region. ✓City center ✓Well-established destination

	✓Coherent with the brand offer ✓Presence of the target customer segment (arrival patterns) ✓Potential of the demand for the destination ✓Economics of the region were positive ✓The degree of competitiveness and other brands' presence. ✓Stability of the country • Infrastructure: ✓International accessibility ✓National accessibility • Physical: ✓Extension and renovation stage of an old hotel. ✓The hotel infrastructure corresponds to the brand segment ✓Style of the hotel needs to be coherent with the brand segment ✓Room size, within the differences between cities and countries. • Pre-opening commitments: ✓The construction stage can take longer than expected, based on the different legal steps that the owner has to ensure (building permits, etc….) ✓Technical team from the day of the signature • Human asset specificity: ✓Local availability of the qualified staff ✓Cost of the hiring and training staff locally ✓Varies with the number of projects opened in the same region
Interviewee P.3	Privileged markets, or strategic locations identified by the chain in the region. The transactions that were signed were related to hotels located in one of these markets. In Western Europe, they "*were looking for trophy hotels, iconic hotels*" to enhance the brand image. • Asset specificity[8]: ✓Hotels that enhanced the brand image ✓Ideally with dual seasonality, or with a hotel presenting a complementary seasonality in the same region ✓The chain has been attempting to enter the location for several years ✓Coherence with the standards of the brand "*In this case, the partnership was right, the contract was right, and the location was right*". • Location: ✓Strategic location ✓Proximity to large cities, economic centers ✓The brand was represented in the resort segment in the region, the hotel allowed the completion of the offer with a city location ✓With a lot of potential for further development (regional level) ✓In a central district of a European capital ✓Infrastructure available in the location ✓The positioning of the country as a destination in the segment of the hotel ✓Propensity of the market to grow ✓Changes in the dynamics of the region/city

[8] The degree of asset specificity is related to the brand power of negotiation. Small companies have to assert their brands, so they would accept a higher commitment in the relationship (TCT).

	✓Geographical location vis-à-vis other destinations (Gateway cities). • Infrastructure: ✓New building ✓High architectural and design standards ✓Newly renovated ✓Corresponds to the standards of the segment of the brand ✓Minor modifications to be made for operation efficiency Distinction: Management contract and lease: ✓The responsibility of infrastructure alterations • Pre-opening commitments: ✓Higher when the timing between signature and opening is shorter ✓Level of renovation of the building ✓Age of structure and refurbishment required ✓The pre-opening commitments were discussed with the other party to decrease their expectations for the first season ✓Accept to operate and wait for addition of upgrades to be done after the first season. • HR: ✓The mobilization of highly skilled HR is higher when the timing between signature and opening is shorter ✓The mobilization includes technical, operations, PR, and Sales and Marketing. ✓ The stage of development (renovation) determines the time until opening and the planning time for HR efforts

Organizational features of hotel unit			
Case B	*Task programmability*	*Information system-base*	*Outcome uncertainty*
Interviewee P.1	• Existence of previous contracts with the owner. "*He knows how we function*." • Existence of previous operation in the city of the hotel (allows for the programmability of HR element). • Confidence in the financial capacity of the owner. • "*Trust*" in the owner • Operations programmability is the responsibility of the regional offices. • Related to the information search efforts (due diligence)	• Meetings with the owner and site visits. • Reporting with the regional offices.	• Based on the effort spent on the financial planning (if it is done by the hotel chain or the developer). "*The amount of time, the number of resources*" "*Who ran the figures*" • Time available to prepare the forecast affects the outcome uncertainty.
Interviewee P.2	• Previous contracts in the city • Previous or planned contracts in the region • Previous contracts with the hotel owner/developer • Check for financial background • Check for solidity of the partner	• Meetings with the owner and site visits. • Reporting with the regional offices. • Site visits and site evaluation • Documents for financial check: ✓Loan bank documents ✓Building permit ✓Interior sketches ✓Master plan ✓Feasibility study ✓Projected costs ✓FF&E listing To the owner: ✓GM profiles ✓Pre-opening budget	• Estimates of the amount of fees to be earned • Mainly based on the assessment of future demand. • City comparison is often used in the assessment of uncertainty • Stability of the country
Interviewee P.3	• The chain has been involved in the process from the renovation stage: "*Very structured, we know at which point in time we will start, we know at which stage we*	• Formal and informal meetings: "*we meet on a very regular basis*. (…) *We have a very open communication*". (…) *Be it on the phone, on personal meetings,*	Outcome uncertainty is affected by: • The consistency between the type of contract signed and the return expectations • The degree of understanding of the

	have to be there". • The operation team (essentially the GM) is integrated in early stages of development to allow for planning • Commonly known third party: Owners and developers who have signed with the chain. • Possibility of having a close an open relationship with the owning company (especially in a management contract).	*planned or non-planned*." • Intranet • Reporting system • Meeting and informal communication essentially	components of a management contract by the owner. • In a management contract: The level of understanding of the standards and culture of the chain. • The alignment between the GOP expectations and the type of product/hotel operated. • Outcome uncertainty is related to bonding costs involved by both parties in the transaction.

	Organizational Control	
Case B	*Behavior Control*	*Output Control*
Interviewee P.1	• The stage of development of the hotel determines the degree of possible behavior control. The hotel is "under development, so we have the ability to put in all our brand standards". • "*Trust*" in the owner • Technical team • Focus on control of the operations ✓Control for quality of operations ✓Ensure that the owner does not intervene • Owner: the control of the owner, ✓Financial situation ✓Previous operations ✓Re-investment propensity	• Outputs of the new reporting system[9]: ✓P&L ✓Month-end results ✓Revenues ✓Costs ✓All accounts at the unit level Purposes: ✓Forecasting ✓Re-forecasting ✓Planning ✓Budgeting With the owner: ✓Fees computations ✓Investments in FF&E • Targets imposed by the owner: based on a minimum level of fees. • The targets vary with the country and the region.
Development control process:		
Interviewee P.2	• Technical team: site visits, plan approval • Regional offices monitor the performance of the hotel unit • Control on owner: ✓Strategy plan ✓Interviews ✓Pre-opening budget ✓Monitor the opening and "*critical path*". ✓Feasibility study exam ✓Secure financing ✓Advance working capital ✓Building permits • Site visits and site evaluation (corporate or regional team) • GM is in charge of controlling for the quality of the product offered with client and with the relationship with the owner.	• Outputs of the new reporting system: ✓Occupancy ✓% Revenues ✓F&B revenues ✓Ratios ✓Budgeted fees
Development control process:		

[9] This is for internal control of the unit performance rather than to control for the owner.

Interviewee P.3	• Marketing plan is designed during the pre-opening stage. • Very close relationship (through constant communication) is maintained. • The relationship allowed the reduction in the pre-opening commitments by the operator. • With the GM: in charge very early of the marketing plan of the unit. • In a management contract: The development of a shared understanding of the culture of the chain and the components of the contract. ✓The "hands-off" required position by the owning company ✓The chain is the unique responsible for HR and other operating decisions. • The owner is informed about the management decisions and policies • The owner monitors the process • The outputs for the development system: ✓Progress on projects • Performance indicators that are examined by the regional office: ✓People management ✓Quality • Close contact is maintained with the GM of the hotel unit.	• The owning company expects specific returns from the property ✓Sales and marketing targets ✓Sales and marketing efforts ✓GOP forecast for the property • The owner controls by output while monitoring the process. • The outputs of the reporting system: ✓Financial ✓Sales ✓Forecasts ✓Real vs. budget • Performance indicators that are examined by the regional office: ✓Sales ✓Costs ✓Total Revenues ✓Operating ratios
• Elements examined by the regional officer on an operating hotel: "*in fact, one might say that the quality, the performance, and the people management in a hotel are the 3 major components of an open hotel*". → 2 out of three are behavior control. • The GM is not a "*glorified guest-relation manger*", he is a manager with the entrepreneur aspect: indicates the increased responsibility of the GM and the emergence of the performance focus.		

	Control Costs	
Case B	*Monitoring costs*	*Outcome Control Costs*
Interviewee P.1	• Technical team site visits • Technical team plan exam • Operation and sales when the market is unknown • On average the development effort (all regions included): 15 contracts/year. • Could be shared with other partners when existing. • The GM and the financial controller for the operating units. • Pre-opening teams for the pre-opening stage • Expatriate managers to ensure the implementation of brand standards.	• Investments in reporting system at the corporate level. ✓Financial reporting system • The components to control for in the relationship with the owner are contained in the contract.
Interviewee P.2	• Technical team efforts to monitor the construction or renovation efforts. • On average 2-3 people depending on the effort and knowledge needed on a specific unit. • Mainly covered by the technical fees, or the first installment after the signature. • Regional offices monitor the performance of the hotel unit: approx. 5 people • Activity of the hotel unit is monitored by the GM or the regional operation manager.	• The control of the process with the owner is secured in the contract. • Most of contracts are drafted internally, but also commission a lawyer depending on the contract. • Reporting system from units to corporate • Monitored by CFO • Owner will audit the monthly report of the operations • Investments in the communication between elements of the company.

Interviewee P.3	• Technical team, technical fees are covered during the pre-opening stage, computed as a fixed fee per room. • Sales and marketing people to support the GM with the marketing plan • Regional VP+ assistant • GM on site • The owning company and the chain maintain a constant and "*close relationship*". • Formal and informal meetings: "*we meet on a very regular basis*. (…) *We have a very open communication*". (…) *Be it on the phone, on personal meetings, planned or non-planned*." • Pre-opening assistantship increases the likelihood that the product will correspond to the standards of the brand.	• Reporting system ✓ Financial and accounting elements ✓ Persons in charge of the reporting system (regional VP and GM) ✓ Intranet base

	Other Control Costs			
Case B	*Residual loss estimate*	*Information search costs*	*Bargaining costs*	*Bonding costs*
Interviewee P.1	• Implied in relation to the presence in a location where other brands are represented.	• Due diligence: ✓Financial situation ✓Track record ✓Previous operations visit • Information about the location • Visit of the location • Require the owner to commission a third party.	• Legal • Process takes on average 6 to 8 months. "*Typically, the longer it drags on, the less likely that is going to have actually serious prospects*".	• The owner/developer signed for several units in different countries. • Owner priority[10] • Targets of minimum fees differ with the level of competitiveness of the market and the potential of revenue of the location.
Interviewee P.2	• Not considered	• Commission a third party for owner's check and due diligence.		
Interviewee P.3	• In terms of non presence in strategic markets	• Reduced if there is a common party. • Reduced by "reputation" in the region.	• Correlated with the competitiveness of the market. Depends on the potential and commercial capacity of the destination	• When obligations to meet the expected GOP are shared. For instance, in a management contract, the performance of the GOP was contingent upon the owner's addition of new rooms.

[10] Whereby the operator agrees to stand aside on incentive fees to the extent that he doesn't reach certain performance targets. The fees are deferred to the years where the targets are met. Mentioned also in the pilot-interview1-.

<table>
<tr><td></td><td colspan="2">Elements of Risk</td></tr>
<tr><td>Case B</td><td>Magnitude of loss</td><td>Probability of loss</td></tr>
<tr><td colspan="3"></td></tr>
<tr><td>Interviewee P.1</td><td>• Financial impact in terms of lost fees is straightforward
• Financial impact in terms of brand image is more difficult to estimate and equally if not more important.
• The visibility and importance of the location to the segment and the perception of the brand increase the magnitude of the loss.

→ Highest concern</td><td>• Examined in conjunction with the magnitude.
• Probability of loss comes as a second consideration based on the magnitude of the possible loss.
• Increase the focus on the probability as the magnitude increases.</td></tr>
<tr><td colspan="3">• The risk is related to the brand and its positioning with the selection of the contract. “Making sure that each development project enhances our brand as opposed to weaken it.”
• Brand perception and image also through the selection of a healthy partner.</td></tr>
<tr><td>Interviewee P.2</td><td>• Highest concern
• Losing one contract would mean losing the possibility of signing further deals with the same owner. This in turn increases the required resources for behavior control.</td><td>• “It’s a damage than you can control for fairly easily”.</td></tr>
<tr><td colspan="3">• <u>Note</u>: city comparison is used in the assessment of risk (often mentioned in other interviews)
• Risk of mis-evaluation of the relationship with the owner.
• Risk of not being able to communicate with the owner anymore (behavior control loss)
• Risk of not having enough resources to maintain the relationship with the owner.
• Risk of having the owner intervening in the operations of the hotel (lose control on the operations and thus on the delivery of the brand).</td></tr>
<tr><td>Interviewee P.3</td><td>• The “financial risk” is very much similar to the magnitude of loss. It is the notion of amount estimate. “That’s actually a plain number”.</td><td>• Brand risk: “the minute you start deviating” from the standards and quality in one hotel”.</td></tr>
<tr><td colspan="3">• 2 types of risk:
✓Financial risk: “depends on the type of contract you have”
✓Brand risk: “if quality or performance falls below a certain level, you are harming your brand name.”
• Distinction: In a management contract the risk is essentially brand risk. In a lease or equity contract, the financial risk is the first concern: the obligation on the amount is more present “if you can’t pay your lease, the owner of the building won’t ask where the money is coming from. We have to deliver the rent”.</td></tr>
</table>

Case C	

Interviewee 1 *Director of Development*	***Expansion mode:*** At the corporate level all growth options are considered. Start with the brand in the middle-segment and decide to go up or down the market segments based on the country conditions Franchise: in the Western established markets Need to find reliable partners, for a good adherence to the product Sale of a certain number of owned units, focus on operating profits and activities Leases: "*if the market leases are affordable*". Depends of the real estate market conditions. The length of the lease contract varies whether it is a fixed or variable lease (longer for variable leases) Equity participation is essentially done through minority participation A brand approach to expansion efforts Equity participation allows the firm to have a "*say*" in the project, it leverages the power of the chain in the project. Equity participation means that you have to develop the project. Consider the potential of the country and the access provided by a location "*if you take the risk it may open the door of larger markets*" Management contract is based on brand management: "*if you convince the owners that you are the right brand, you will have more customers*". Each growth option has a special profile for value creation and return profile.
Interviewee 2 *Senior VP of development*	***Expansion mode:*** Respond to the market with the brands The signature of one growth option over another depends on what is offered by the owner "*Depending on the country, depending on the product, the product positioning, we may have different approaches*". In the region supervised, the corporate decision is to expand through management contracts and management contracts with minority participation. Rental is considered on a case-by-case basis, if the opportunity comes up. General rules about growth options: Franchise "*where there exists good professionals, where there are hotel professionals*". "*We will consider leases or company owned hotels in the regions where we have good visibility and a sustainable situation or a stabilized political and economic situation. Then the differentiation will be brand by brand.*" The criterion of Return on Invested Capital is examined first. Therefore equity participation is considered especially in segments where the returns are higher.

Interviewee 3 *Regional Director of development*	***Expansion mode:*** Based on the profile of the country Development strategy in the country "*both from a brand point of view and also for an investment-commercial structure point of view*". Most of the deals signed are management contracts Limited franchises Forms of investments "*either 100% investment (by the chain), or we take let's say 20 to 25% minority equity with a long-term management contract in the place*". The purpose of the equity participation is for further development

Organizational features of hotel unit	
Asset specificity	
Interviewee 1	• Brand: fit between the brand and the operations requirements related to the market entered • Fit with the strategy and business plan • Timing estimates, the ROIC over the life-cycle of the investment • Property track record • CF generated from the operations in the future, estimated value of the property appreciation (in the case of equity participation) and the current result of the hotel • Location: ✓Country: financial conditions ✓Country: stability ✓Correspond to the plans laid out in the strategy and business plan ✓Possibilities of expansion within the country in number of brands and number of rooms ✓The strategic aspects related to the market: the return available for the risk taken ✓The risk taken is related to the size of the market ✓Timing for entrance in a market varies with the brand. The reason is that the cost of development differs for each brand or segment of the market. This in turn, affects the ROIC ✓Potential of the market ✓Demographics ✓Competition: the dynamic of the market ✓Possibility for site location within the market considering the dynamics of the country ✓Trade-off between volume and quality ✓Visibility ✓Easy access ✓Attractiveness to the people ✓Strong primary market close by ✓Convenient for travelers • Physical aspects: ✓The technical assistance ✓Related to the level of standardization of the product (the brand) ✓Features of the room ✓Number of restaurants ✓Meeting rooms, presence and features ✓Way to adapt to the demand on the market

	• Pre-opening commitments: ✓ Minimum for franchise. Has to remain such since the future CF (fees) are minimum to cover for the invested capital need further time "to convince the owner that your brand is the right one" ✓ Longer for management contract: the owner is most of the time an investor so need to convince him that both "*the brand and the management team is going to optimize, or to extract the maximum value from the property*" ✓ More room for flexibility in a management contract ✓ Leases: "*is mainly the question of agreeing on the financial terms*". Commitment increases if the lease is variable rather than fixed ✓ More related to the legislation of the country. ✓ Ownership: longer process because you have be involved in the purchase of the land, in the development of the property ✓ Investments at the corporate level in the promotion of the brand ✓ Pre-opening budget for the pre-opening period; varies with the brand • Human asset specificity: ✓ Distinction between two types of developers: "*we have on the one hand the franchise and the management contract and on the other hand the lease and the ownership*". The first are sellers, the others are more buyers with a good understanding of figures ✓ Team effort: finding the right team to launch and run the unit ✓ Various expertise are required at the same time: operations to decide on the physical infrastructure of the building, on the site location. ✓ Operations concentrate the core skill and the knowledge required. Relied upon for the forecasts, for the site location, and any other step of the development effort. ✓ Technical for the facilities design ✓ Marketing to decide on the product ✓ Legal especially in JV agreements
Interviewee 2	• Asset specificity: ✓ "*Earning capacity of the project*" for both the chain and the owner ✓ Location is the most important aspect ✓ Quality of development ✓ Type of development ✓ Specifications of the development ✓ Align the development with the brand ✓ "*Product matches the brand criteria we have*": product location, and financial ✓ A project that aligns the chain and the partner's expectations of return ✓ Offers the growth option that corresponds to the strategy the chain has for a particular country • Location: ✓ Suitable for a hotel: "*we will, as an operator, we will be able to drive adequate business into that hotel for it to make sense.*" ✓ Location with high demand generators • Infrastructure: ✓ Affects the forecasts for the unit • Physical: ✓ Ability to construct on time and budget is key • Pre-opening commitments: ✓ Nothing in particular for the concerned region

	✓6 to 12 months duration ✓Varies with the size of the hotel, the brand, the "*specific needs of the location*" ✓Depends on which stage of the project does the chain enter. If the hotel is already in the construction phase, more compromises will be made on the infrastructure and the brand standards • Human asset specificity: ✓Lack of experienced and knowledgeable developers ✓Developer requires a complex set of skills that is often difficult to find ✓For operations: the demand for operation workers is booming in the region, reducing the pool available of people
Interviewee 3	• Asset specificity: ✓A project, therefore it will be built according to the standards ✓Consistent with the strategy of the chain. Strategy is developed for the country (based on the macro-economic factors and the knowledge of the hotel market in the country) • Physical: ✓Size of the hotel (determinant of the return on invested capital): enough revenues generated in comparison to the costs incurred (monitoring costs in the case of management contract) • Human asset specificity: ✓The financial capacity of the owner or partner ✓Technical capacity of the owner ✓Past experiences with the partner ✓Knowledge about hotel operations and real estate ✓Mobilization of expatriates for specific countries or regions of the world "*to hire the staff who is prepared to go there, who will be able to live in the country and do a good job*". ✓Training requirements ✓"*One of the key factors is to make sure that the owner is really confident that C has the hotel expertise the know-how and is really designing a project which is acceptable for the country*". ✓"*Second, make sure that the owner (...) will comply with the provisions, not only the financial ones, but all the provisions of the contract*". ✓"(…) *And that the owner will not interfere in the day-to-day management*" • Infrastructure: ✓The travel time required to reach the hotel (monitoring costs) • Pre-opening commitments: ✓Monitoring efforts: send expatriate on site ✓Marketing and operations ✓Marketing efforts is related with the commercial situation of the destination • Location: ✓ The land: zoning of the hotel ✓The profile of the travelers constituting the demand for the location

Organizational features of hotel unit			
Case C	*Task programmability*	*Information system-base*	*Outcome uncertainty*
Interviewee 1	• Development of a strategic plan at the corporate level by brand (define the number of hotels by brand for each country) • Derive a business plan by brand and by country • Due diligence ✓Reputation ✓"*Has money to do the job*" ✓Positive track record with previous partners	• Mostly rely on intranet • One person is in charge in new countries of collecting the information • Country's embassy in the region	• Infrastructure in the destination • Stability of the events in the country
Interviewee 2	Project for ✓Room rates ✓The occupancy of the hotel ✓The F&B revenues ✓Operating costs	• Previous contracts with the investment partners • Documents ✓Letter of interest ✓Legal contracts ✓Technical services agreements •	• Build the hotel on time and budget • Especially in the region where the demand is very high due to a strong economic development • Level of room rate growth • Infrastructure improvement
Interviewee 3	• Previous contracts and projects with the owner or partner	• Mostly technical documents rather than legal • 80% of the job is done by emails • Documents ✓Drawings ✓Plans • Internal network for investigation on the owner • "*2 electronic databases: one for the management contract and franchise contracts and another for projects where C has a financial commitment.*"	Outcome uncertainty is affected by: • The lack of due diligence by the prospecting developer: ✓Comparing the performance in the country with other locations ✓The market analysis ✓The location ✓The sources of financing of the project (funding of the overall project and the working capital)

	Organizational Control	
Case C	*Behavior Control*	*Output Control*
Interviewee 1	• Of the development team: "*it depends, if it's a project with investment, we are or I am with my team following the project at an early stage. When it is a management or a franchise, we are really checking at later stages, unless it is a specific project*" and at a larger scale. • Marketing and legal team check at early stages of the management contract or franchise negotiation	• The head of development controls for successful signature of the deal: the hotel opens and is positioned well ✓ Because of geographic dispersion, the shift moves from behavior to output control • Output control: ✓ "We look at what we have planned in terms of costs and in terms of results initially when we have validated the project. We compare what was planned with what has happened." ✓ Feedback to the development team to develop the knowledge ✓ Used to review the expansion strategy: aligning growth option with the market and the destination • Capex on renovation. Conflicting element especially if the owner is not receiving the expected return
Control of the other party in case of a JV is the most difficult and important: length of the association and the difference in competencies (not from the hotel business).		
Interviewee 2	• "*We have to be aligned in our ROI requirements from the assets*." • Controlling system for developers ✓ Approval committee for the JV ✓ Detailed database intranet	
Interviewee 3	• The profile of the hotel owner • Technical assistance contract (costs are paid by the owner) • Analysis grid of the chain • Sales policy (reported to the owner) • HR policies • *2 electronic databases: one for the management contract and franchise contracts and another for projects where C has a financial commitment*	• Reports generated from an operating unit (presented to the owner and the hierarchy in the chain) • Legal requirements from the contract to provide for the reports • Budget for the operating unit • Maintenance costs • Provisions for working capital asked from the owner

	Control Costs	
Case C	*Monitoring costs*	*Outcome Control Costs*
Interviewee 1		
Interviewee 2	• There are additional monitoring costs related to the JV: need to appoint a person to work with the JV partner and maintain the relationship and build the project together • 2 to 4 people per project (commercial and technical side) • The intranet system for reporting on the development process	
Interviewee 3	• Assessed in comparison with the expected revenues to determine the ROI of the unit • Economies of scales are assessed against the monitoring costs for a region or country • Travel expenses and travel time is considered for the monitoring costs • Technical aspect: 1 expert (number of projects per person in a given period of time): approx. 10 projects at the same time • Training requirements for the country or selected region • The number of expatriates will depend on the size of the hotel and the brand • Monthly meetings with developers	

	Other Control Costs			
Case C	*Residual loss estimate*	*Information search costs*	*Bargaining costs*	*Bonding costs*
Interviewee 1	• "*No, we know that there is an impact. (…) we are much more pragmatic, and we don't want to spend more money in a study that will not really bring us much*"	• More in depth due diligence for JV contracts compared to management contracts	• The level of agreement between the partners on the return of the project reduce the bargaining costs	• In the case of equity participation, there are considered in the estimates of the possible return from the participation • Bonding costs decrease the bargaining costs
Interviewee 2	• In terms of demand potential and potential of the segment aimed for "*the capacity of absorption of the market*"	• Due diligence on the site itself		• Previous contracts involving investments with the same partner
Interviewee 3	• Not considered	• Reduced with the experience of the development team	• Reduced when the partner has the experience and the knowledge of hotel operations	• Equity participation • Future projects with the same owner

<table>
<tr><td></td><td colspan="2">Elements of Risk</td></tr>
<tr><td>Case C</td><td>Magnitude of loss</td><td>Probability of loss</td></tr>
<tr><td colspan="3"></td></tr>
<tr><td>Interviewee 1</td><td>• The knowledge of the market and the destination allows this estimate</td><td>• First driver and is determined by the degree of stability of the country in its political, financial and legal environment.</td></tr>
<tr><td colspan="3">• Risk is related to the level of stabilization of the political, financial, and legal environment.
• When a country scores high on both the magnitude and the probability, a management contract will be preferred and the guarantee levels will depend on the stability of the country.
• Time is factored in to reach the expected return. “You make sure that return will take more time, but you will never lose at the end of the day”.
• Payback considerations have to be factored in</td></tr>
<tr><td>Interviewee 2</td><td>• Rather than the financial impact, it is more the impact on the brand that is of a concern</td><td>• Managed with experience of the hotel environment</td></tr>
<tr><td>Interviewee 3</td><td>• Ability to obtain good rates for the project</td><td>• Focus of attention
• Probability of adverse events in terms of operations
• Level of room rate growth
• Infrastructure improvement in the destination
• Probability of non-occurrence of unfortunate events</td></tr>
<tr><td colspan="3">• There are two main imperatives composing the risk in development: on time and on budget
• In this case, the concern is more over the probability of affecting either the timing or the budget
Control elements: due diligence, proposition check list, team in place, and various elements of the deal are factored in</td></tr>
</table>

APPENDIX E: DATA REDUCTION MATRICES: GENERAL SUMMARY BY CASE

Pilot Case	**Organizational features of hotel unit**
	Asset specificity

Expansion mode: The development is based on management agreements and franchise license in "*strategic markets*".
The company focuses on the "*expansion of our brands"*
2 main objectives: 1. Maintain a stream of fees over the length of the contract and 2. Extend the size of the system.

Dimensions	Grand themes
Site specificity: • The location ✓Capital cities ✓Seat of governments ✓Industrial or commercial centers ✓ Resort location ✓Access ✓Proximity to business district, city center, transportation. ✓Development of the system ✓The changing characteristics of location • Potential of a destination: ✓At country level ✓Growth of the destination ✓Degree of sophistication and competitiveness in the local market. ✓Changes in incentive fees ✓Room supply level of the market ✓Presence of other management companies in the market ✓Potential of the market, or demand generators ✓Exhibition or conference facility. ✓Uniqueness of the location ✓Completes the "Presence for a chain equally all over the world". ✓LT future potential of the market location ✓Accessibility ✓Current demand ✓International market situation Physical asset specificity ✓Building attributes ✓Building compliance with the brand standards ✓Size of the hotel (!) ✓Meeting rooms	• Destination profile is the most important element in determining the asset specificity of the hotel unit. "*When you do grow by management or franchise, you are always thinking of strategic locations where you are missing*". • Asset specificity of the hotel unit and the location of the unit are highly inter-related. • The degree of physical asset specificity is determined by its degree of compliance with the brand norms. • The degree of advancement of the project: whether it is an existing project or a conversion affects its asset specificity.

✓Executive floor ✓Checking desk ✓Executive lounge ✓Minimum room surface in square meters ✓Amenities in the bathroom ✓Amenities in the hotel correspond to the chain standards ✓Number of restaurants, ✓Bars ✓Ballrooms ✓Meeting facilities ✓SPA ✓Room surface ✓Bathroom standard requirements ✓Correspond to the demand for the location (alignment of the structure with the segment) ✓Brand systems and automatic infrastructure, ✓Security infrastructure: means of escape, fire alarms, etc… ✓Number of rooms ✓Category of the hotel ✓Type and number of facilities ✓Parking space ✓Number of restaurant ✓Amenities within the rooms ✓Advancement of project <u>Human asset specificity</u> Team of consultant: operations, finance, and lawyers. ✓Lack of specialized staff ✓The investment in the support and development team is structured along with the expansion. ✓The developer: "difficult combinations" for the profile ✓Difficult to schedule for the number of developer that would be needed, as the exact number of projects is hard to predict ✓Long training required: 1 to 3 years. Average of 2 years before becoming independent ✓Training period	*<u>Distinction</u>*: The physical infrastructure (efficiency of design) is less of a concern in a franchise than when it is operated by the company. • Timing affects HR asset specificity: The training period available and the level of training of the HR in the location will determine the number of expatriates in the hotel unit; thus the cost of HR for a specific contract. • When the chain operates the unit the above point is the most important. • In the case of a franchise, the availability of operational and managerial competences in the destination are the priority. → The degree of compliance of the hotel offer with the brand determines the degree of asset specificity. "*Our deals, are consistent, they have to be, to our brand.*"/ "*site suitability*" • The compliance is on 2 axes: ✓Degree of correspondence with the customer base ✓ The degree of brand competitiveness in the destination → Flagship unit is the highest level of asset specificity for hotel chains.

Organizational features of hotel unit		
Task programmability	*Information system-base*	*Outcome uncertainty*
• Grand themes: ✓Past and present experiences in the market increase the degree of task programmability. ✓Level of experience of the other party with the market location and/or hotel operations. ✓In a management contract, the financial situation of the owner/developer is key to task programmability. ✓A shared comprehension of the terms of the contract with the specificity of the hotel business. • Dimensions: ✓Existence of a familiar third party in the market. *"Partners with shared interests and past transactions".* ✓Existence of another operation/unit in the market. • Link with Control and control costs: ✓Assessment of the owner/developer to operate according to brand standards. ✓Instruct to commission an independent market study ✓Produce feasibility study ✓Information search: identity, funding structure, and administrative situation ✓On-site visits ✓Request of due-diligence fulfillment. ✓Check background ✓Participation in the pre-opening steps. ✓Check of operating capacities of the franchisee. • Other links: Programmability affects the cost of building and opening the hotel. Programmability affects timing estimates. Number of persons representing the other party increases the difficulty to program for the task.	• Grand themes: ✓Large IS platform allows the sharing of information within the organization and with external players. ✓The information transmitted varies with the type of contract ✓Regular communication (formal and informal meetings) is maintained ✓Meetings with owners on a regular basis + informal meetings. ✓The accounting system is used for the monitoring of day-to-day performance. • Dimensions: ✓Franchise: focus on sales ✓Mgmt: add the operating costs, or "*costs of profitability*" ✓Documents supporting the owner/developer structure and situation ✓Performance reports ✓Guest comments ✓Quality audit teams ✓Mystery shoppers	• Grand themes: ✓Outcome is "*Quality of the end product*". ✓The degree of application of brand standards determines the degree of outcome uncertainty. The financing capacity of the owner/developer determines the degree of outcome uncertainty. ✓The degree of comprehension of the historical performance of the market and the impact of future factors determines the degree of outcome uncertainty. • Dimensions: ✓Changes of ownership for the hotel owner/ developer (related to political stability) ✓Reasons for the hotel developer/owner entrance in the deal with the chain. ("*The owner's own agenda*"). ✓Timing affects the degree of uncertainty ✓Country whether it is a developed or under-developed region. • Link with other constructs: ✓Data on comparable hotels and locations are collected to decrease the level of uncertainty. ✓When it is in under-developed country you tend to take into account unexpected delays. Distinction among types of contracts: ✓Due diligence might be more in depth for management contract. ✓The concern for the application of brand standards is higher in franchise contracts.

	Organizational Control	
Pilot Case	*Behavior Control*	*Output Control*
	• Grand themes: ✓Behavior control is predominant during the pre-opening stage ✓Behavior control is ensured by the technical/support and operation team ✓Behavior control is maintained through constant communication and on-site visits. ✓Behavior control is put in place through the creation of a "*good comprehension*" with the hotel owner/developer. • Dimensions: ✓Behavior control is conducted by the operation and technical team during the renovation or building stage. ✓Obligations in terms of: brand standards, property, and property maintenance. "*What they (*owners and developers*) do physically with the hotel*". ✓The number of visits (level of behavior control) increases as opening approaches ✓Legal team ✓Regional offices supporting the monitoring effort. ✓Behavior control is present through training of the employees in the location. Distinction among types of contracts: ✓ In franchise contracts: less involvement in the physical design ✓Go through the franchisee business plan and operational projections and future structure ("*we want to really meet and understand the key staff that they are proposing*"). ✓Elements controlled for in franchisee selection: "*right sills and infrastructure*". → Behavior control is more present in a franchise agreement.	• Grand themes: ✓Output control is more present in the operating stage. ✓The outputs are transmitted via the reporting system and electronic platforms ✓At the development stage, output control is in place for developers (compensation on the number of deals signed). ✓The outputs to be controlled for are mentioned in the contract and relied upon during the behavior control process. • Dimensions: ✓Outputs of reporting system: essentially accounting figures "*full accounts*". ✓Regional offices control: hotel financial performance: Comparison of budgeted and real performance. ✓Financial outputs controlled for: Occupancy, ADR, RevPar, GOP, and GOP percentage, Departmental profit. ✓The output of the development team is checked against the analysis of the feasibility and investment analysis team. ✓Quality audit (throughout the year): guest comments, quality audit teams, and mystery shoppers, feedback from team members ✓Output requirements are defined in the standards (internal or external regulation such as UFOS in the U.S.) Distinction among types of contracts: The information transmitted varies with the type of contract: ✓Franchise: focus on sales (revenues and occupancy) ✓Mgmt: add the operating costs, or "costs of profitability". ✓In a franchise agreement the hotel operator is responsible to the franchisee for output: Output control by the franchisee. ✓In a management contract, the General Manager and regional offices are responsible for the outcome of the operations. (bonus compensation scheme). → In a management contract, the focus is on the control of the owner/developer financial output.

- Grand themes: CONTROL:
  - ✓ In development, control consists of a selection process rather than a control of the transaction itself.
  - ✓ The control is based on the adherence to brand standards: the objective is to control for the process. The focus of on control is on brand protection.
  - ✓ The control in development is higher when equity is involved.
  - ✓ There is a control process in place involving different functions of the organization (senior developers, legal department, operations, brand managers, financial department, and technical department)

- Dimensions:
  - ✓ Senior managers are involved when equity is required: there is a finance and investment committee for exceptional deals.

	Control Costs	
Pilot Case	*Monitoring costs*	*Outcome Control Costs*
• Grand themes: ✓Monitoring costs are pre-dominant. However, these costs are recovered by an early installment (before the opening) ✓Monitoring costs vary with the accessibility of the hotel location. ✓Monitoring cost vary with the degree of compliance of the other party to the brand standards. ✓Number of expatriates needed on the site for the pre-opening and early opening stages affects monitoring costs ✓The level of the monitoring costs is related to the brand level. • Dimensions: ✓In HQ: 2-3 persons (1 HQ developer, analyst, and sometimes legal team member) ✓Technical team (Operation & support teams): Approximately 15 to 16 specialized persons. ✓Operation & support teams: traditionally 1 year before opening, it is a full-time commitment. ✓Support team: internal tax advisors, insurance advisor, treasury advisor ✓Operational support: VP of operations per area + team. ✓Last year, the technical team supervised 30 hotels. ✓The number of visits (monitoring costs) increase as opening approaches ✓Monitoring cost for the operation and technical team: number of hotel visits per time period. ✓High-skill people (lawyers, engineers, "consultant type" positions). ✓Feasibility and investment analysis team ✓Number of meetings depends on the hotel performance. ✓When it is a new location, local legal advisor is hired ✓		• Grand themes: ✓The cost of investment in IS determines a large portion of the control costs ✓The bonuses paid to regional managers and GM make-up the remaining portion of control costs. • Dimensions: ✓ Price of the investment in the reporting and the IS. ✓ On-going maintenance of the IS ✓Regional offices compensation on hotel performance. ✓GM compensation ✓Reporting system. ✓Quality reporting system • Distinction among types of contracts: ✓The IS system includes less elements of reporting for a franchise than for a management contract.

• <u>Link with other constructs:</u> ✓There is a relationship between the level of HR asset specificity and monitoring costs: the higher the level of HR specificity, the lower the monitoring costs. ✓The higher the task programmability, the lower the monitoring costs. • <u>Distinction among types of contracts:</u> ✓Franchise: directors of franchise + brand support team ✓Management contract: GM and VP of operations	

	Other Control Costs		
Residual loss estimate	*Information search costs*	*Bargaining costs*	*Bonding costs*
• Grand Themes: ✓The residual loss estimates are assessed in terms of sales on other hotels in the location. • Dimensions: ✓Estimates of the impact on the sales of other hotels in the location. ✓Value the contract: NPV formula ✓Discount rate varies based on market economics.	• Grand Themes: ✓The owner/developer is responsible for the information search costs ✓On-site visits are part of the information search process. • Dimensions: ✓Commission an independent market study (often paid by the other party) ✓Produce feasibility study. ✓Use of free information: Internet and other accessible information. ✓Third party specialists on a contract basis ✓Hire previous employees of consultants for internal analysis ✓Due diligence • Link with Control construct: ✓Both parties produce feasibility studies (control construct) ✓Due-diligence form + other documents (control construct) • Distinction among types of contracts: Due diligence might be more in depth for management contract. Due diligence by a third party. Third party in each region or country.	• Grand Themes: ✓The bargaining costs are high but not at the expense of the chain. ✓Bargaining costs are correlated with the degree of competitiveness of the market. • Dimensions: ✓Legal team costs (a fee is leveraged for the developer/owner) ✓Visits and meetings with the owner/developer are included in the fees. ✓Regional offices negotiate the deals	• Grand Themes: ✓Financial commitment is maintained at minimum: "*our position (...) is usually a dry position and we're not putting cash or equity of any form into the deal*". ✓The degree of asset specificity is the determinant of the level of bonding cost. ✓The shared responsibility of the brand standards constitutes an indirect bonding cost for the hotel operator. • Dimensions: ✓ Bonding costs in a franchise agreement are higher because of the shared responsibility of the brand standards.

	Elements of Risk	
Pilot Case	*Magnitude of loss*	*Probability of loss*
	• Grand Themes: ✓Magnitude of loss is more of concern in a management contract that in a franchise contract. ✓The magnitude of loss is important during the negotiation of the deal (first the estimate of the deal has to be determined, so that it is properly covered by the owner financial structure). • Dimensions: ✓Example: food poisoning outbreak and its impact on the brand. ✓ "The key is on market risk": including political and economic risk. • Link with Control construct: ✓The higher the control over the operations the lower the magnitude of risk of brand damages. The chain has the capacity to "*do something about it*". ✓Information search cost is important in reducing the magnitude of loss. • Distinction among types of contracts: ✓Franchise: operating ability is the main concern or source of risk ✓Management agreement: The financing capabilities of the owner or developer determine the magnitude of loss.	• Grand Themes: ✓The main source of risk is the variability of the sales. ✓The amount is estimated and is the responsibility of the developer/owner, therefore the main aspect of risk that the operator has to manage is the probability of loss ✓Concerns in relation to the application of the brand standards ✓Risk of abuse and damage to brand reputation ✓Performance of the hotel business and the destinations where the chain is present. • Link with other construct: ✓The probability of loss is "managed" in the checking stage: when questionnaires, due diligence, market study, and financing are examined. Therefore, task programmability is related to the probability of loss. "*I guess that is why we went many steps ahead by asking for everything in place before we signed*". • Distinction among types of contracts: ✓The risk is higher for a franchise than management contract.
	• Grand Themes: RISK: ✓Main concern for development managers: The image of the brand that will be delivered in the hotel unit. "*Image and that the property will be delivered and per our image worldwide and to our standards and specifications*".	

Case A
Stage of development: The brand names are established in the existing market and the chain aims for a larger international development. Strategic choices: • Expansion as an operating company • Reliance on target markets (countries and regions) by brand within a time range • Establish presence in capital cities first ***Expansion mode:*** In order of frequency: 1. Management agreement (particularly this year) 2. Lease 3. Franchise 4. Other structures involving equity The reasons provided for this choice are: • The demand from developers and owners in the targeted regions is for management contract • The limited presence of the company in the region (stage of development of the chain) • The flexibility of the management contract compared to other contracts • The opportunity to expand in a market or country after the penetration with JV and leases • Permits meeting the company's growth target in a timely manner. • The markets chased are volatile, which increases the expectations of developers in terms of return. Leases do not allow the delivery of the required levels of return • Lease constitutes a good compromise to insure the location without providing the funding • Lease is offered in markets where the demand is stable and exposure possible • The quality of hotel and management available in the region is not favorable for franchise There • Size of the system of franchises offered is limited (reliance on master franchise providers) • Franchise contracts are employed in markets where the brands are already established

Organizational features of hotel unit	
Asset specificity	
Dimensions	Grand themes
Asset specificity: ✓Located in a strategic city or primary market ✓Placed in a good location ✓Commercial potential in the future ("*the traffic, the transport systems (...) that will be built*") ✓Allows early and first entry in a market before other competing brands ✓Early opening ✓Ensure high rates at early stages ✓Length of negotiation and timing required by the development team ✓Yield possibly offered to the hotel owner/developer: assessment of the rate, occupancy	• Grand themes: ✓A high degree of asset specificity ensures a high rate at early stages of operations ✓A high degree of asset specificity ensures the long term commercial potential of the unit ✓A high degree of asset specificity ensures the promotion of the brand to the developers and owners ✓High asset specificity ensures the alignment between return expected from the operations of the hotel and the return expected from the hotel owner or developer

<u>Site specificity</u>: • The destination ✓The company has a brand in its portfolio that corresponds to the market context ✓Size of the market respective to the region ✓Local market coverage ✓Possible synergy in terms of destination commercial potential ✓Ranking of the city or destination in the country in terms of size: • Population size • Economic indices ✓By country approach: taking into account the stage of development of the country • The location/the site ✓The location in the area, in the market ✓Economical boom in the city ✓Large population ✓Center district, heart of the economic boom <u>Physical asset specificity</u> ✓Physical asset specificity is ensured through the signature of contracts that are still at the project stage ✓Room size, size of the facilities ✓General layout: external and interior ✓Amount of development required and could be involved. Timing is the key concern ✓Plot size if the hotel is not built yet ✓The stage of the construction: whether it is an existing hotel or a site ✓Agreement on the physical specificity before signature. <u>Human asset specificity</u> ✓Required number of managers in a new operating unit ✓HR asset specificity is related to the time available before opening ✓HR asset specificity is related to the nature of the project: new construction, conversion, and asset management. ✓GM is listed first. The GM is an expatriate in these new regions ✓Included in the contract ✓Related to behavior control: training programs • Pre-opening commitments: ✓Pre-opening commitments vary with the country's legislation requirements and practices ✓The owner/developer is in charge of the pre-opening fees	✓Site specificity is defined in terms of a brand ✓Site and physical asset specificity are pre-requisites to signature ✓The operating experience of the destination is the determinant of the level of human asset specificity ✓The human asset specificity of a contract is determined by the required number of managers in a new hotel ✓Pre-opening commitments are related to the time available before opening • <u>Dimensions:</u> ✓The location of the hotel site in a target market of one of the brands determines the level of asset specificity ✓ The timing related to the project determines the level of asset specificity ✓Synergies in terms of site specificity are related to the number of hotels promoted through the marketing of one destination ✓The destination and the site determine are the two dimensions for site specificity ✓The destination is assessed against economic indicators and commercial synergies at the country level ✓Room size, hotel size, plot size, and the general layout are the dimensions of physical asset specificity ✓Monitoring of the technical and marketing efforts are the dimensions of the pre-opening commitments ✓Marketing and operations efforts constitute the pre-opening commitments ✓The classification of the market of the hotel, the availability of specific human asset, and the timing determine the level of pre-opening commitments • <u>Link with other constructs:</u> ✓Degree of physical asset specificity and timing may conflict in determining the level of asset

✓Mobilize operating knowledge and experience of the market on site ✓Timing is based on the hotel location being a resort or a city destination. ✓2 objectives for the commercial effort: market the destination and market the hotel • Other investments: ✓PR and marketing at the development stage before opening. ✓The entrance in a market is subordinated to the existence of another hotel in a higher ranked market 2 concerns: ✓The availability of key HR skills ✓The compensation through technical fees	specificity. ✓The management of human asset is included in the contract through procedures. ✓Human asset specificity is related to task programmability through time planning ✓The higher the pre-opening commitments, the higher the degree of task programmability *Distinction*: ✓Distinction between growth options in the pre-opening commitment level

Organizational features of hotel unit		
Task programmability	*Information system-base*	*Outcome uncertainty*
• Grand themes: ✓Is affected by the nature of the project 2 elements to plan for ✓The relationship with the owner ✓The forecast of profit • Dimensions: ✓ 2 tools employed: Scoring sheet and cooperate with a consultant specialized in the market ✓Owner with existing units operating in the same market ✓Market study for non established markets ✓Reliance on internal knowledge (intellectual capital) ✓Affected by the political stability of the region ✓Background check ✓Owner's readiness to understanding ✓Assess during the development stage, the capacity to remain "*off-hands*" ✓Degree of training of the other party with the industry and the type of contract • Link with Control and control costs: ✓On site visits for assessment ✓Commitment in the design and layout ✓Related to the information base system • Distinction: ✓Increases in a lease with the existence of a FRI (Full Repaying and Insuring) clause.	• Grand themes: ✓First stages it is verbal information and agreements during meetings ✓For the deal and internally • Dimensions: ✓Financial performance transmitted through the reporting system: RevPar index, P&L ✓Reliance on informal means of communication between the owner and within the firm ✓For information about the region and the other party: contract with a local consultant ✓Written form: heavily documented ✓A tracking or reporting system is in place for developers to report the advances of their work	• Grand themes: ✓Timing (estimate of opening) ✓Outcome uncertainty is mainly related to the destination rather than the unit itself • Dimensions: ✓Large devaluations or fluctuations in the exchange rate is a concern ✓The forecast of the demand for the hotel (occupancy and rates) composes outcome uncertainty • Link with other constructs: ✓Behavior control is employed to counter outcome uncertainty ✓The dimensions to task programmability and outcome uncertainty are common Distinction among types of contracts: ✓Leases: the costs of maintenance is an added uncertainty ✓Management contract: reasonable estimate of uncertainty required ✓More accurate sales estimates are required in a franchise: "*just a certain percentage of top-line and you are less sensitive to the changes*". ✓Lease is the most difficult in terms of outcome uncertainty: "*you are responsible for the entire P&L*". ✓Equity is also difficult

	Organizational Control	
Case A	*Behavior Control*	*Output Control*

Behavior Control	Output Control
• <u>Grand themes:</u> ✓2 transactions of concern ✓The higher the influence on the owner, the lower the efforts of the technical team • <u>Dimensions:</u> ✓HR policy based on behavior control ✓The existence of a formal process is in place for signing-off new contracts ✓On-site direct monitoring (technical and other members of development) ✓Involvement in the development process to influence the layout of the hotel ✓Developers report on their leads, the stages of negotiation, the timing of the signature • Internal due-diligence ✓Registration documents for the land ✓Titles, etc… • <u>Distinction</u>: ✓Franchise: Restrictions on the use of the brand name • Pre-dominant in franchise contract enforcement: ✓Compliance with brand standards ✓Control for the reservation system ✓Annual audit of a franchisee	• <u>Grand themes:</u> 2 catgories of outputs are controlled for ✓The performance measure of the hotel unit ✓The hotel as a final product presented by the developer • <u>Dimensions:</u> ✓Outputs include top-line performance measures: ✓On the GM of operating hotels ✓Contract clauses for the owner performance and obligations ✓Targets for the developers (constitute the basis for incentives portion of income) ✓The outcome of the hotel construction is a key performance outcome that is controlled for by the developer <u>Distinction among types of contracts</u>: • Leases: ✓Penalties in the contract (timeliness and performance targets) during the operations ✓Full-repair-and insurance clause • Franchise: Include milestones in the behavior control elements ✓Brand standards: signage, construction, design. • Management contract type ✓"*Straight*", ✓With a "*threshold*", ✓Subordinated fees, ✓With guarantees

	Control Costs	
Case A	*Monitoring costs*	*Outcome Control Costs*
	• Grand themes: There are 2 phases ✓ Before signature: development, technical, brand and concept team. Development is in charge of liaison ✓ After signature: operations join in, and start to take over the liaison task ✓ Technical fees charged to the owner. A rule of thumb is applied for the computation of the technical fees. In weakly served destinations, the travel expenses are added to the technical fees. (Number of flight connections is factored in). ✓ Pre-opening fees are charged to the owners ✓ Concentration of efforts during the construction stage (technical team) and pre-opening (operating team) • Dimensions: ✓ Approximately 30-50 hotels/year are monitored ✓ Average number of visits by the hotel chain (mainly technical and operations teams): minimum 20 site visits sometimes double for technical team. ✓ Technical and operation team control through monitoring ✓ Regional directors and GM with the reliance on business plans as a control tool (3 years range and LT) • Distinction among types of contracts: ✓ Franchise: Costs of franchise contract enforcement: mostly on site visits • Cost of monitoring compliance with brand standards • Cost of controlling for the reservation system • Cost of annual audit by external party	• Grand themes: ✓ The reporting system ✓ The persons responsible of the outcomes of the reporting system • Dimensions: ✓ Override costs of losing a signed contract by including "*wash-out*" in the forecast ✓ Reporting system to the head quarter (advanced Access database) ✓ The regional development manager + one technical member (i.e.: architect or engineer) are in charge of the hotel final output in terms of construction ✓ Regional controller ✓ Revenue manager ✓ Head of operations for budget setting

	Other Control Costs		
Residual loss estimate	*Information search costs*	*Bargaining costs*	*Bonding costs*
• Grand Themes: ✓ Seldom taken into consideration • Dimensions: ✓ ROI considerations are taken into account ✓ Only considered in terms of competition taking over a “target” hotel or location-missed opportunity ✓ Following a lead, spending effort, and have it cancelled	• Grand Themes: ✓ The nature of the market affects the level of information search costs • Dimensions: ✓ Market study costs ✓ In less established markets, it varies with: • Degree of background check • Market studies • Political stability • Utilities • Government ✓ Low if internal competencies and experience is available in the chain ✓ Fees of a local consultant • Distinction among types of contracts: ✓ Lease is the contract that requires more information search	• Grand Themes: ✓ Vary from one country to another • Dimensions: ✓ Low if the owner is perceived as a good partner • Distinction among types of contracts: ✓ Lower for franchises (more rigid clauses) ✓ Higher for leases more than management contracts	• Grand Themes: ✓ Intangible elements compose the bonding costs • Dimensions: ✓ The shared responsibility of the brand ✓ No litigations for recovery is advised (possible) ✓ Waiving the technical services fees Contract signature, and threat of cancellation ✓ Length of the process constitutes a bonding cost • Distinction among types of contracts: ✓ In case of clauses of guarantee to the owner ✓ Bonding costs are at their highest in leases (more than equity)

	Elements of Risk	
Case A	*Magnitude of loss*	*Probability of loss*

• Grand Themes: ✓The magnitude would the compensation that the chain would have to offer ✓Commercial and financial ✓Relevant when there are guarantees involved • Link with Control construct: ✓The link with financial (measurable) bonding costs	• Grand Themes: 2 main losses are mentioned ✓The probability of losing the contract ✓Related to the forecast of the demand • Dimensions: ✓"Wrong" party selection ✓"Wrong" judgment that "*will destroy all the good things you did with the brand*" ✓Delays ✓Not opening ✓Default of the hotel owner/developer ✓Not achieving the announced expansion ✓Not delivering the return promised to the owner • Distinction among types of contracts: ✓The type of leasing and its clauses

Case B	
Expansion mode: • Expansion focus is on maintaining the consistency of the units with the brand. • Management contract is the main focus (98% approx. of the network). • In rare instances, signature of management contract with GOP guarantee. • Leases are singed in few specific instances: "*We would prefer a management contract but it is not always possible. In certain areas you have to accept a lease or you have to provide certain equity in order to retain the contract or in order to get to the contract.*" • Leases with 2 components: a fixed and a % of NOP or GOP. • Equity participation is examined but not at an individual hotel basis.	

Organizational features of hotel unit	
Asset specificity	
Dimensions	Grand themes
Asset specificity: Privileged markets, or strategic locations identified by the chain in the region. In Western Europe, they "*were looking for trophy hotels, iconic hotels*" to enhance the brand image. ✓Ideally with dual seasonality, or with a hotel presenting a complementary seasonality in the same region ✓The chain has been attempting to enter the location for several years ✓Coherence with the standards of the brand "*In this case, the partnership was right, the contract was right, and the location was right*". Site specificity: • Existence of another hotel in the same city: synergies sought. • The history of the building and its image • Location: ✓Market potential for the target customer segment ✓The degree of competitiveness and other brands' presence. ✓Stability (political and economical) of the country and region ✓Level of tourism attractiveness of the location ✓Proximity to or in large cities, economic centers ✓The brand was represented in the resort segment in the region, the hotel allowed the completion of the offer with a city location ✓Regional potential for further development ✓Suitable infrastructure available in the location ✓The positioning of the country as a destination in the segment of the hotel ✓Changes in the dynamics of the region/city	Asset specificity: Asset specificity is determined by the consistency of the hotel with the strategy of the chain. Enhancing brand image the strategy and was based on 3 main axes: 4. Iconic hotels 5. Even stream of profit 6. Consistency with brand standards Site specificity: The existence of another hotel supports axis 2 of the strategy. As for the image of the hotel, it corresponds to axes 1 and 3. Location was assessed against: ✓Market potential for the brand segment ✓Possibility of exposure of the 2 main segments of the chain: city and resort ✓Complementarily with another unit

<table>
<tr><td>✓ Geographical location vis-à-vis other destinations (Gateway cities).</td><td></td></tr>
<tr><td>• Infrastructure:
✓ International accessibility
✓ National accessibility</td><td>The accessibility of the hotel is the component of the location infrastructure that is assessed.</td></tr>
<tr><td>• Pre-opening commitments:
✓ Reduced by the fact that the owner had already worked with the chain on previous contracts
✓ The construction stage can take longer than expected, based on the different legal steps that the owner has to ensure (building permits, etc...)
✓ Higher when the timing between signature and opening is shorter
✓ Level of renovation of the building
✓ Age of structure and refurbishment required
✓ The pre-opening commitments were discussed with the other party to decrease their expectations for the first season</td><td>The level of pre-opening commits are determined by:
✓ Experience of the owner with the chain and its operations
✓ Its duration varies with the stage of development of the project
✓ Its intensity varies with the timing between signature and opening</td></tr>
<tr><td><u>Physical asset specificity</u>
✓ The hotel is under development, increases the potential of coherence with the brand standards
✓ Extension and renovation stage of an old hotel
✓ The hotel infrastructure corresponds to the brand segment
✓ Room size, within the differences between cities and countries.
✓ Minor modifications to be made for operation efficiency
<u>Distinction: Management contract and lease</u>:
✓ The responsibility of infrastructure alterations</td><td>The degree of physical asset specificity increases with the length of the collaboration during the pre-opening stage.

The degree of physical asset specificity is determined by the number and extent of modification to be made for operation efficiency.

The degree of physical asset specificity differs for each type of growth option.</td></tr>
<tr><td><u>Human asset specificity</u>
✓ Local availability of the qualified staff
✓ Cost and planning for the HR required
✓ Varies with the number of projects opened in the same region
✓ The mobilization of highly skilled HR is higher when the timing between signature and opening is shorter
✓ The mobilization includes technical, operations, PR, and Sales and Marketing.
✓ The stage of development (renovation) determines the time until opening and the planning time for HR efforts</td><td>Costs related to HR and the planning efforts constitute the human asset specificity of a contract.
This specificity differs for each growth option.
Human asset specificity varies with:
✓ Local availability of the qualified staff
✓ The number of projects opened in the same region
✓ The stage of development (renovation) determines the time until opening and the planning time for HR efforts</td></tr>
</table>

Organizational features of hotel unit		
Task programmability	*Information system-base*	*Outcome uncertainty*
• Grand themes: ✓ Existence of previous contracts with the owner. "*He knows how we function*." ✓ Existence of previous or planned operation in the city of the hotel ✓ The financial capacity of the owner. ✓ The chain has been involved in the process from the renovation stage: "*Very structured, we know at which point in time we will start, we know at which stage we have to be there".* • Dimensions: ✓ Existence of previous contracts in the region enhanced the programmability of HR element ✓ "*Trust*" in the owner (reasons varies with growth option type) ✓ The operation team (essentially the GM) is integrated in early stages of development to allow for planning. ✓ Commonly known third party: Owners and developers who have signed with the chain. ✓ Possibility of having a close and open relationship with the owning company (especially in a management contract). • Link with Control and control costs: ✓ Related to the information search costs: due diligence ✓ Operations programmability is the responsibility of the regional offices. ✓ "*Trust*" in the owner to reduce control costs.	• Grand themes: ✓ Meeting and informal communication essentially ✓ Reporting with the regional offices ✓ Varies if its internal or with the owner • Dimensions: ✓ Meetings with the owner ✓ Site visits ✓ Site evaluation ✓ Intranet ✓ Reporting system • Documents for financial check: ✓ Loan bank documents ✓ Building permit ✓ Interior sketches ✓ Master plan ✓ Feasibility study ✓ Projected costs ✓ FF&E listing To the owner: ✓ GM profiles ✓ Pre-opening budget ✓ Formal and informal meetings: "*we meet on a very regular basis*. (…) *We have a very open communication*". (…) *Be it on the phone, on personal meetings, planned or non-planned*."	• Grand themes: ✓ Certainty related to the estimates of the amount of fees to be earned. These estimates are mainly based on the assessment of future demand. ✓ The consistency between the type of growth option and the return expectations ✓ Based on the effort spent on the financial planning (if it is done by the hotel chain or the developer). "*The amount of time, the number of resources*" "*Who ran the figures*" • Dimensions: ✓ The degree of understanding of the components of a management contract by the owner ✓ The alignment between the GOP expectations and the type of product/hotel operated. ✓ Time available to prepare the forecast affects the outcome uncertainty ✓ City comparison is often used in the assessment of uncertainty ✓ Stability of the country is included in the assessment • Link with other constructs: ✓ Outcome uncertainty is related to bonding costs involved by both parties in the transaction. Distinction among types of contracts: ✓ In a management contract: The level of understanding of the standards and culture of the chain.

<table>
<tr><td>Case B</td><td colspan="2">Organizational Control</td></tr>
<tr><td colspan="2">Behavior Control</td><td>Output Control</td></tr>
<tr><td colspan="2">

• <u>Grand themes:</u>

✓ During the operations 2 elements are controlled for:
▪ The quality of operations
▪ Insurance that the owner does not intervene
✓ Prior to signature, the owner is controlled on:
▪ Financial situation
▪ Previous operations
▪ Re-investment propensity

✓ The stage of development of the hotel determines the degree of possible behavior control. The hotel is "*under development, so we have the ability to put in all our brand standards*".

✓ Very close relationship (through constant communication) is maintained.

✓ Formal and informal meetings: "*we meet on a very regular basis. (...) We have a very open communication". (...) Be it on the phone, on personal meetings, planned or non-planned.*"

• <u>Dimensions:</u>
✓ "*Trust*" in the owner
✓ Monitoring of the technical team: site visits, plan approval
✓ Regional offices monitor the performance of the hotel unit
✓ Close contact is maintained with the GM of the hotel unit
✓ Control on owner:
▪ Strategy plan
▪ Interviews
▪ Pre-opening budget
▪ Monitor the opening and "*critical path*".
▪ Feasibility study exam
▪ Secure financing
▪ Advance working capital
▪ Building permits
✓ The owner is informed about the

</td><td>

• <u>Grand themes:</u>

✓ The owning company expects specific returns from the property
✓ The owner controls by output
✓ The owner impose targets imposed based on a minimum level of fees:
▪ Sales and marketing targets
▪ GOP forecast for the property

✓ Output control is observed internally and in the control of the operator by the owner.

• <u>Dimensions:</u>

✓ Outputs of the new reporting system:
▪ P&L
▪ Month-end results
▪ Revenues
▪ Departmental Revenues
▪ Costs
▪ Occupancy
▪ Ratios
▪ Budgeted fees

✓ Purposes:
▪ Forecasting
▪ Re-forecasting
▪ Planning
▪ Budgeting
✓ With the owner:
▪ Fees computations
▪ Investments in FF&E

✓ The targets vary with the country and the region.

<u>Distinction among types of contracts</u>:
✓ Management contract: The owner controls by output. His monitoring efforts are very limited.

</td></tr>
</table>

<table>
<tr><td>management decisions and policies
✓The owner monitors the process
✓Performance indicators that are examined by the regional office:
▪ People management
▪ Quality

• <u>Link with other constructs:</u>
✓The relationship allowed the reduction in the pre-opening commitments by the operator: thus a reduction of financial bonding costs.

<u>Distinction among types of contracts</u>:
✓ In a management contract: The development of a shared understanding of the culture of the chain and the components of the contract.
▪ The “hands-off” required position by the owning company
▪ The chain is the unique responsible for HR and other operating decisions.</td><td></td></tr>
<tr><td colspan="2">• <u>Grand themes: CONTROL:</u>
✓Behavior control is the pre-dominant form of control between the hotel chain and the hotel owner/developer. Behavior control is observed in the reliance on “close relationship”, or “close communication” or maintaining a relationship of “trust”. These types of control are process oriented rather than output oriented, thus indicating the reliance on behavior control.
✓Internally, the elements examined by the regional officer on an operating hotel: “in fact, one might say that the quality, the performance, and the people management in a hotel are the 3 major components of an open hotel”. Two out of three elements are process oriented, and thus indicate a predominant reliance on behavior control.
✓However, in this chain, GM is neither a “glorified guest-relation manger”, nor an “administrator”. He is believed to be a manager with the entrepreneur aspect. This indicates the increased responsibility of the GM and the emergence of the performance focus in the control tool employed internally.
✓Behavior control is in place by the operator for the owner. As for output control, it is in place internally and by the owner for the operator’s performance.</td></tr>
</table>

Case B	Control Costs
Monitoring costs	*Outcome Control Costs*
• <u>Grand themes:</u> ✓ Technical fees are covered during the pre-opening stage, computed as a fixed fee per room. ✓ The GM or the regional operation manager monitors the activities of the hotel unit. • <u>Dimensions:</u> ✓ Technical team site visits ✓ Technical team plan exam ✓ Operation and sales when the market is unknown ✓ On average the development effort (all regions included): 15 contracts/year. ✓ Could be shared with other partners when existing. ✓ The GM and the financial controller for the operating units. ✓ Pre-opening teams for the pre-opening stage ✓ Expatriate managers to ensure the implementation of brand standards ✓ Regional offices monitor the performance of the hotel unit: approx. 5 people • <u>Link with other constructs:</u> ✓ Pre-opening assistantship increases the likelihood that the product will correspond to the standards of the brand. ✓ Monitoring costs are likely to be higher when the market is unknown ✓ Monitoring costs are likely to be higher when the local knowledge of hotel operations is limited	• <u>Grand themes:</u> ✓ The components to control for in the relationship with the owner are covered in the contract. ✓ Most of contracts are drafted internally, but also commission a lawyer depending on the contract. ✓ Investments in reporting system at the corporate level. • <u>Dimensions:</u> ✓ Reporting system ▪ Financial and accounting elements ▪ Persons in charge of the reporting system (regional VP and GM) ▪ Intranet base

Case B	Other Control Costs		
Residual loss estimate	*Information search costs*	*Bargaining costs*	*Bonding costs*
• Grand Themes: ✓The residual loss is not directly estimated. ✓When considered, it is estimated in relation to competing brands • Dimensions: ✓Implied in relation to the presence in a location where other brands are represented. ✓In terms of non presence in strategic markets	• Grand Themes: ✓ Commission of a third party for owner's check and due diligence. ✓Information about the location ✓Information search costs is reduced if: ▪ There is a common party ▪ Reduced by the "reputation" in the region • Dimensions: • Due diligence: ▪ Financial situation ▪ Track record ▪ Previous operations visit ✓Visit of the location ✓Require the owner to commission a third party.	• Grand Themes: ✓Legal process constitutes most of the bargaining costs. ✓Correlated with the competitiveness of the market. Depends on the potential and commercial capacity of the destination • Dimensions: ✓Legal process takes on average 6 to 8 months. "*Typically, the longer it drags on, the less likely that is going to have actually serious prospects*".	• Grand Themes: ✓Existing contracts signed with the owner/developer increase bonding costs ✓Owner's priority increase bonding costs ✓The higher the level of competitiveness of the market the higher the bonding costs ✓Bonding costs decrease if the obligations to meet performance targets are shared[11]. • Dimensions: ✓In a management contract: obligations to meet the expected GOP.

[11] For instance, in a management contract, the performance of the GOP was contingent upon the owner's addition of new rooms.

<table>
<tr><td>Case B</td><td>Elements of Risk</td></tr>
<tr><td>Magnitude of loss</td><td>Probability of loss</td></tr>
<tr><td>• <u>Grand Themes</u>:

✓The “financial risk”, related to the amount estimate, is very much similar to the notion of magnitude of loss. “That’s actually a plain number”.

✓The magnitude of loss varies with the type of contract signed.
✓The visibility of the location to the segment increases the magnitude of the loss.

• <u>Dimensions</u>:
✓Assess in terms of lost fees
✓Financial impact in terms of brand

• <u>Link with Control construct:</u>
✓Losing one contract would mean losing the possibility of signing further deals with the same owner. This, in turn increases the required resources for behavior control, information search costs, and bonding costs.</td><td>• <u>Grand Themes</u>:
✓The brand risk is associated with the probability of loss.
(Brand risk: “the minute you start deviating from the standards and quality in one hotel” the chain incurs the brand risk.

✓Examined in conjunction with the magnitude: Increase the focus on the probability as the magnitude increases.

• <u>Dimensions</u>:
✓The risk is related to the brand and the coherence of the contract with the brand positioning: “Making sure that each development project enhances our brand as opposed to weaken it.”
✓Brand perception and image also through the selection of a financially viable partner.
✓Mis-evaluation of the relationship with the owner (limited information search costs)
✓Difficulty of communication with the owner (behavior control loss)
✓Lack of resources to maintain the relationship with the owner (limited bonding costs)

→ Most difficult to assess: “image is more difficult to estimate and equally if not more important”.</td></tr>
<tr><td colspan="2">• <u>Grand Themes</u>: RISK:
✓The dual aspect of risk is confirmed in the answers
✓Both aspects are examined in conjunction as they are considered as highly related.
✓The magnitude of loss appears as the highest concern
✓The probability, while more important is difficulty to estimate and is thus, considered second.

• <u>Note</u>: city comparison is used in the assessment of risk (often mentioned in other interviews)

<u>Distinction among types of contracts</u>: In a management contract the risk is essentially the probability of loss. In a lease or equity contract, the magnitude of loss is the first concern: the obligation on the amount is more present “if you can’t pay your lease, the owner of the building won’t ask where the money is coming from. We have to deliver the rent”.</td></tr>
</table>

Case C
Expansion mode: • At the corporate level all growth options are considered. Each growth option has a special profile for value creation and return profile Respond to the market with the brands • Franchise: Western established markets Need to find reliable partners, for a good adherence to the product • Leases: Depends of the real estate market conditions. The length of the lease contract varies whether it is a fixed or variable lease (longer for variable leases) • Equity participation is essentially done through minority participation A brand approach to expansion efforts Equity participation allows the firm to have a "*say*" in the project, it leverages the power of the chain in the project The purpose of the equity participation is for further development The criterion of Return on Invested Capital is examined first. Therefore equity participation is considered especially in segments where the returns are higher. Consider the potential of the country and the access provided by a location • Management contract is based on brand management: "*if you convince the owners that you are the right brand, you will have more customers*". Most of the deals signed are management contracts

Organizational features of hotel unit	
Asset specificity	
Dimensions	Grand themes
Asset specificity: ✓Timing estimates, the ROIC over the life-cycle of the investment. Property track record. CF generated from the operations in the future, estimated value of the property appreciation (in the case of equity participation) and the current result of the hotel ✓Fit with the strategy and business plan ✓Offers the growth option that corresponds to the strategy the chain has for a particular country ✓Brand: fit between the brand and the operations requirements related to the market entered ✓ "*Product matches the brand criteria we have*": product location, and financial ✓Specifications of the development (type, quality)	Asset specificity: • Grand Themes: ✓The ROIC of the hotel correspond to the strategic plans ✓Alignment of the chain's and the partners' expectation in the asset • Dimensions: ✓Consistent with the strategy of the chain.
Site specificity: • Destination: ✓Country: financial conditions and stability ✓Possibilities of expansion within the country in number of brands and number of rooms	Site specificity: • Grand Themes: ✓The destination and the location are the two main dimensions of site specificity

✓The strategic aspects related to the market: the return available for the risk taken ✓Potential of the market ✓Timing for entrance in a market varies with the brand The reason is that the cost of development differs for each brand or segment of the market. This in turn, affects the ROIC • Location: ✓Location is the most important aspect ✓Competition: the dynamic of the market ✓Possibility for site location within the market considering the dynamics of the country ✓Trade-off between volume and quality ✓Visibility ✓Attractiveness to the people: Easy access, Convenient for travelers ✓Location with high demand generators (Strong primary market close by) ✓Suitable for a hotel: "*we will, as an operator, we will be able to drive adequate business into that hotel for it to make sense*." ✓Affects the forecasts for the unit ✓The travel time required to reach the hotel (monitoring costs) ✓The profile of the travelers constituting the demand for the location	✓The degree of specificity was determined by its coherence with the risk-return profile sought by the firm • Dimensions: ✓The potential of the travel market in the country and the destination constitute the degree of site specificity ✓The travel market in the country affects the stability of the future cash flow ✓The location affects the potential profits of the hotel unit
<u>Physical asset specificity</u> ✓Related to the level of standardization of the product ✓Features of the room ✓Number of restaurants ✓Meeting rooms, presence and features ✓Way to adapt to the demand on the market ✓The technical assistance ✓A project, therefore it will be built according to the standards ✓Ability to construct on time and budget is key ✓Size of the hotel (determinant of the return on invested capital): enough revenues generated in comparison to the costs incurred (monitoring costs in the case of management contract)	<u>Physical asset specificity</u>: • Grand Themes: ✓The physical aspect of the hotel is a way to adapt to the demand on the market ✓The technical assistance is a key tool to achieve physical asset specificity ✓The ability to construct on time and budget is a key determinant of physical asset specificity
<u>Human asset specificity</u> ✓Team effort: finding the right team to launch and run the unit ✓Various expertise is required at the same time: operations to decide on the physical infrastructure of the building, on the site location ✓Developer requires a complex set of skills that is	<u>Human asset specificity</u>: • Grand Themes: ✓Human asset specificity is relevant in

often difficult to find ✓Distinction between two types of developers ✓Operations concentrate the core skill and the knowledge required. Relied upon for the forecasts, for the site location, and any other step of the development effort. ✓For operations: the demand for operation workers is booming in the region, reducing the pool available of people ✓Technical for the facilities design ✓Marketing to decide on the product ✓Legal especially in JV agreements ✓Mobilization of expatriates for specific countries or regions of the world ✓Training requirement ✓The financial capacity of the owner or partner ✓Technical capacity of the owner ✓Past experiences with the partner ✓Knowledge about hotel operations and real estate	both the internal and the external transactions • Dimensions: ✓Internally, human asset specificity is related to the skills required for the achievement of the expansion plans ✓Externally, human asset specificity is the alignment between the hotel chain targets and the profile of the partner
• Pre-opening commitments: ✓ Investments at the corporate level in the promotion of the brand ✓Pre-opening budget for the pre-opening period (6 to 12 months duration) ✓Varies with the size of the hotel, the brand ✓Depends on which stage of the project does the chain enter. If the hotel is already in the construction phase, more compromises will be made on the infrastructure and the brand standards ✓Monitoring efforts: send expatriate on site ✓Marketing efforts is related with the commercial situation of the destination Distinction among types of contracts: ✓Minimum for franchise. Has to remain such since the future CF (fees) are minimum to cover for the invested capital need further time "*to convince the owner that your brand is the right one*" ✓Longer for management contract: the owner is most of the time an investor so need to convince him that both "*the brand and the management team is going to optimize, or to extract the maximum value from the property*" ✓More room for flexibility in a management contract ✓Leases: "*is mainly the question of agreeing on the financial terms*". Commitment increases if the lease is variable rather than fixed ✓Ownership: longer process because you have be involved in the purchase of the land, in the development of the property	Pre-opening commitments: • Grand Themes: ✓Pre-opening commitments varied with each growth option • Dimensions: ✓The longer is the ownership, then management contract, than lease, and finally franchise • Link with other constructs: ✓The longer the duration of the pre-opening efforts, the higher the monitoring costs

Organizational features of hotel unit		
Task programmability	*Information system-base*	*Outcome uncertainty*
• Grand themes: ✓Task programmability was laid out in the strategic plan at the corporate level by brand • Due diligence by the prospecting developer: ✓Comparing the performance in the country with other locations ✓The market analysis ✓The location ✓The sources of financing of the project ✓Positive track record with previous partners ✓Previous contracts and projects with the owner or partner • Dimensions: Project for ✓Room rates ✓The occupancy of the hotel ✓The F&B revenues ✓Operating costs	• Grand themes: ✓Intranet system and telephone are the means of information employed ✓Mostly technical document, rather than legal, are exchanged ✓One person is in charge in new countries of collecting the information ✓Previous contracts with the investment partners • Dimensions: ✓Internal network for investigation on the owner • Documents ✓Drawings ✓Plans ✓Letter of interest ✓Legal contracts ✓Technical services agreements	• Grand themes: Outcome uncertainty is affected by: ✓Stability of the events in the country ✓Infrastructure improvement in the destination • Dimensions: ✓Especially in the region where the demand is very high due to a strong economic development ✓Level of room rate growth • Link with other constructs: ✓Build the hotel on time and budget (site specificity) ✓Link between task programmability and outcome uncertainty

<table>
<tr><th>Case C</th><th colspan="2">Organizational Control</th></tr>
<tr><td colspan="2">Behavior Control</td><td>Output Control</td></tr>
<tr><td colspan="2">• <u>Grand themes:</u>

✓Behavior control is the predominant form of control employed in both the internal and external transactions

• <u>Dimensions:</u>
✓The profile of the hotel owner
✓Technical assistance contract (costs are paid by the owner)
✓Analysis grid of the chain
✓Sales policy (reported to the owner)
✓HR policies

• <u>Link with other constructs:</u>
✓The higher the human asset specificity with regard to the partner, the lower the monitoring costs

<u>Distinction among types of contracts</u>:
✓Behavior control of the partner by the development team varied with the growth option and the scale of the project.
✓Marketing and legal team check at early stages of the management contract or franchise negotiation</td><td>• <u>Grand themes:</u>

✓Because of geographic dispersion, the shift moves from behavior to output control
✓Outputs that are controlled for are the profits, and maintenance expenses
✓Findings from output control develop the learning curve

• <u>Dimensions:</u> of Output control:
✓Planned vs. actual
✓Feedback to the development team to develop the knowledge
✓Used to review the expansion strategy: aligning growth option with the market and the destination
✓Capex on renovation. Conflicting element especially if the owner is not receiving the expected return
✓Outputs for the development team are: the hotel opening and is correct positioning

<u>Distinction among types of contracts</u>:
✓Reports generated from an operating unit (presented to the owner and the hierarchy in the chain)
✓Legal requirements from the contract to provide for the reports
✓Budget for the operating unit
✓Maintenance costs
✓Provisions for working capital asked from the owner</td></tr>
<tr><td colspan="3">• <u>Grand themes: CONTROL:</u>
✓Control of the other party in case of a JV is the most difficult and important: length of the association and the difference in competencies (not from the hotel business)</td></tr>
</table>

<table>
<tr><td>Case C</td><td colspan="2">Control Costs</td></tr>
<tr><td colspan="2">Monitoring costs</td><td>Outcome Control Costs</td></tr>
<tr><td colspan="2">• <u>Grand themes:</u>
✓Monitoring costs are assessed in comparison with the expected revenues to determine the ROI of the unit
✓Economies of scales are assessed against the monitoring costs for a region or country
✓Travel expenses and travel time is considered for the monitoring costs

• <u>Dimensions:</u>
✓2 to 4 people per project (commercial and technical side)
• Controlling system for developers
✓Approval committee for the JV
✓Detailed database intranet
✓Technical aspect: 1 expert (number of projects per person in a given period of time): approx. 10 projects at the same time
✓Training requirements for the country or selected region
✓The number of expatriates will depend on the size of the hotel and the brand
✓Monthly meetings with developers

• <u>Link with other constructs:</u>
✓There are additional monitoring costs related to the JV: need to appoint a person to work with the JV partner and maintain the relationship and build the project together</td><td>• <u>Grand themes:</u>

✓The intranet system for reporting on the development process</td></tr>
</table>

Case C	Other Control Costs		
Residual loss estimate	*Information search costs*	*Bargaining costs*	*Bonding costs*
• Grand Themes: ✓Residual loss estimate is not considered ✓When considered, it is from a commercial perspective • Dimensions: ✓In terms of demand potential and potential of the segment aimed for	• Grand Themes: ✓Higher in JV ✓Higher when risk-return profile is higher ✓Reduced with the experience of the development team • Dimensions: Due diligence on the site itself ✓More in depth due diligence for JV contracts compared to management contracts ✓One person is in charge in new countries of collecting the information ✓Country's embassy in the region	• Grand Themes: ✓Reduced when the partner has the experience and the knowledge of hotel operations • Dimensions: ✓Previous contracts with the partner decrease the bargaining costs	• Grand Themes: ✓Equity participation ✓ In the case of equity participation, there are considered in the estimates of the possible return from the participation • Dimensions: ✓Previous contracts involving investments with the same partner ✓Future projects with the same owner

Case C	Elements of Risk
Magnitude of loss	*Probability of loss*
• Grand Themes: ✓The knowledge of the market and the destination allows this estimate ✓Rather than the financial impact, it is more the impact on the brand that is of a concern • Dimensions: ✓Ability to obtain good rates for the project	• Grand Themes: ✓First driver and is determined by the degree of stability of the country in its political, financial and legal environment ✓Managed with experience of the hotel environment ✓Probability of non-occurrence of unfortunate events (Infrastructure improvement in the destination) • Dimensions: ✓Probability of adverse events in terms of operations ✓Level of room rate growth