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Growth Opportunities for Three Star Hotels in Split and Dubrovnik

RIT Senior Project

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Hospitality and Tourism Management

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Increasingly competitive, with constant implementation of the new technologies and adaptation to a changing consumer need and wants, the hotel world today is transforming in a rapid change. The mid-priced hotel category was category concerned only with the basic offer and service. The mid-scale hotels of tomorrow, which are still focused on the basics, will need to differentiate. The right example is 'Tru' by Hilton. It is a mid-priced property developed to fill a massive void in the midscale category in the U.S. and Canada. By focusing on technology and different design, this mid-scale property was already called a game-changer in the mid-priced market. It is a hotel created to attract a broad range of travelers with quality accommodation and at an affordable price. Mid-priced hotels today must be aware that the quality doesn't mean luxury. Quality of the accommodation and service is the standard for the whole industry today, including the mid-market as well..

Purpose of this research is to analyze the existing mid-range (3 star) hotel supply in Dubrovnik and Split, especially in terms of amenities and facilities; as well as capacity and price in order to identify potential areas for growth and also to meet challenge of increasing competition from private accommodation.

Hotel Industry Growth

Due to the rapidly changing needs and preferences of the customers, the lodging industry is like a living organism that constantly follows and adapts to new trends on the market. The market environment is affected by the political, economic, social and technological factors making the whole business and operations even more complex.

For ownership and management, globalization allowed the development of hotel networks – “international private chains and unions between different states” (Vasadze, 2016, p.6), as

well as implementation of new and improved information technology and the possibility of high personalization of service. (Vasadze, Akhalaia, 2016).

Since the economic crisis in 2009 the annual number of the overnights in hotels in the world is increasing.....For two days Tourism Statistics official page is down, they provide statistics for the whole world but the server is down....Hopefully they will recover it till Tuesday, so that I can enter the reliable data for the whole world.

The annual number of overnight hotel stays rise from 2,35 billion in 2007 to 3,26 billion in 2018 in Europe (Schmid, 2020). United Nation World Tourism Organization published that compared to 2017, in 2018 increase of the international arrivals in Europe was 43 million - which is significant number that will continue to rise according to the predictions. According to their data European region is the most visited region in the world.

Current Challenges

The development of technology created a new platform for travelers and introduced different possibilities but also created many challenges for the hotel industry including increased competition from private accommodation renters. In 2018 Airbnb platform was recognized as a major threat for the hotel industry which will revolutionize the whole lodging industry. (Gerdeman, 2018).

The results of the research in 2015 showed that 42% of travelers in the U.S. who used Airbnb stopped booking hotels for future stays, and remained fully loyal to private a private accommodations (Stanley, 2015). This study on 4 000 U.S. travelers that have used Airbnb found that price was the main factor for using it and over 90% of customers were highly satisfied with it. According to a study by Zervas et. al. (2017) in Texas, the hotels most affected by competition from Airbnb were budget and mid-price hotels while the luxury

segment had a less significant difference. They estimated that entry of Airbnb to their market had negative impact on lower end local hotel room revenue. The reason behind it is because of the similarity of the stay – casual stay and attractiveness of option for travelers on a budget. Their research was done by segmenting hotels by price category and analysis year – over-year changes and impact of the Airbnb. The results support their hypothesis that Airbnb is directly negatively affecting lower end hotels revenue. As well, they argue that their research can be applicable in any destination where Airbnb is providing their services. They also found that the amenities and the quality of the private properties were similar or even better in some cases than the hotel; as well the prices were lower compared with staying in the hotel. It creates new pressure for mid-price hotels to constantly improve amenities and services in order to stay competitive on the market.

In early 2020 the outbreak of COVID – 19 - the greatest global crisis of the century – stopped the whole world which will permanently shift our economies, industries, lives and perceptions. Although the pandemic is slowly being put under the control the transformation of the travel and hospitality industry is inevitable. This could be a great opportunity for the mid – price hotels because many business travelers who were staying in higher priced hotels now will be settling down to the mid-priced properties (Philip, 2020). As well it is highlighted that customers of luxury upscale properties are mostly foreigners, so that hotels will be in loss. The potential for growth of the mid-scale properties in crisis like this according to them will be an increase number of the domestic travelers that will be staying in the mid-priced hotels (Philip, 2020).

Defining Mid Market

Type of the hotel is directly related to the level of the service they provide, facility, price, and complexity of the operations in the business. (W.G. Kim, M. Cho, R. Brymer, 2013).

The World Tourism Organization developed a couple of differentiation criteria – frameworks to classify hotels around the world. The midscale segment could be considered a flexible category, but the classification is based on the number of beds, number of stars given by local authorities, and price relative to the local markets and different national criteria. In Europe, mid-price properties are usually categorized as three-star hotels which are often hotels with up to 400 rooms (WTO, 2004).

Since there is no standardized method for determining the classification of the hotel - the hotel star rating system is usually determined by government agencies, but it mostly depends on the country to country. Hotel price classification in Europe is mostly determined by standards, quality of service and price. Hotel Star Union is an association in which providers harmonized hotel classification with the same standards, procedures, and requirements for classification in Europe.

According to Hotel Star Union organization, the mid-price or three-star hotels should provide:

- Reception service open 14 hours minimum
- 24 hours availability by phone and bilingual staff
- Reception area surrounded by lounge space
- Luggage service, laundry and ironing provided on demand
- Medium – size restaurants that provide breakfast included in the price
- Parking, fitness center and swimming pool are often available
- Room service is not provided in most of the properties

Regarding the amenities in the rooms, it is stated that each room should provide:

- a mini-bar
- telephone
- TV
- hair-dryer
- an adequate place to lay aside clothes
- regular amenities such as bed and nightstand (Hotel Star Union, 2019)

In Croatia, hotel properties are categorized based on mandatory requirements set by The Ministry of Tourism regarding the arrangement, equipment, devices, services, and maintenance (Narodne Novine , 2016). In addition to the basic conditions accommodations standards that hotels are required to follow regarding the categorization of the mid-priced properties, in order to receive a 3-star designation, the minimum area of the hotel room needs to be larger than 17,5 m² for the basic double room. Three star hotels must provide an elevator (if higher than three floors) and a room telephone with direct access to a public telephone network, TV with remote control, and air-conditioned dining. (Pravilnik Narodne Novine no.8)

Trends in Mid Market Hotels

Customer increased free time and the possibility of better management of it, created a few trends worldwide as well. Urbanization and globalization contributed to a higher number of corporate travelers which require basic hotel amenities at an affordable price which creates enormous opportunities for mid range hotels. (Hotel Business, 2019). Profound changes are taking place in the style of leisure. The hotel business is increasingly investing in a particular sector of the market. Some of them specialize in low and middle-income transit passenger services and many hotels select business tourism as their target segment. “ (Vasadze, Akhalaia, 2016). Concentration on a particular segment and recognizing the parts and potentials of the market that can be served is a crucial part of developing the business today.

When it comes to congress tourism, it must be emphasized the importance of the development in that direction for the mid-price segment to increase the interest and profitability. The growth in popularity of workshops, off - company education, or team building activities should be taken into consideration because the main characteristic of congress tourism is that it takes place throughout all year. It is interesting how mid-priced hotel properties in Dubrovnik and Split aren't focused on the MICE segment because by developing this hospitality sector mid-priced hotels in Dubrovnik would create competitive advantage and strengthen their positions on the market. Mid-priced properties by improving their food quality and investing in their venues for wedding and banquet events could attract potential offseason customers which would prolong their season. Three-star hotels are a good replacement for five-star hotels considering that the venues will be used only for one day. Many Indian mid-priced hotels are shifting their businesses into events hosting to expand the future of mid-priced hotels beyond the hotels' basic service (Russel, 2018). Changes in the market required changes in the way of doing the business, which created new standards for the whole industry. Once air – conditioning in the room was a luxury but now is the basic amenity in all hotel types. Due to extreme competitiveness, mid-priced hotels are implementing changes to stay competitive on the market. The case study conducted in Ghana revealed how two of their three-star hotels are creating a competitive advantage in the market. By developing highly innovative processes of marketing and increasing the online presence these two hotels build their successful image on the market. By that said, they suggest to the mid – price market that they should avoid mistake of focusing too much on interior design. Regarding the developing highly innovative process of marketing they highlighted importance of online presence with accurate and informative data to attract potential customers. Hotels must encourage positive communication and engage in aggressive online and offline marketing strategies to compete with the private accommodation properties.

Interestingly, a study related to the size and type of the hotel revealed the finding that property up to 400 to 500 rooms turned out the most profitable size of the hotel (Withiam, 2000). As well, it is noted when the number of rooms was over 500, the profitability started to decrease. The research conducted on 27 hotels in Tunisia showed the relationship between hotel size and financial performance. Many factors listed in the research affect the profitability of the hotel but when it comes to size category the recommended optimal size of the hotel (excluding resorts), should be the maximum of 500 rooms. The reason behind it is because hotels with a higher number of rooms will benefit from high occupancy and sales revenue but they will be confronted with lower profitability and lower efficiency. (Aissa, Goaid, 2016). The research conducted by consultants Price Waterhouse Coopers in Dubai analyzed the profitability of the mid-market hotels with luxury hotels and the results of the analysis showed that despite the high land price, similar to Dubrovnik, there is a profit opportunity for both high end luxury properties and mid-price hotel types (Pwc, 2015). According to the research the main reasons behind the profitability of the mid-scale properties on premium locations are high occupancy and significantly lower operating costs compared with luxury properties

Overview of Hotel Industry in Dalmatia

The development of the hotels in Croatia has developed in accordance with the increased tourist demand; most of the hotels were build along the Adriatic coast from Istria all the way to Dubrovnik – Neretva County. Hotel industry in Croatia is one of the bases of tourist offer directly connected to the economic development of the whole country. Croatian tourist income was 18% of GDP which was one of the highest ratios in Europe in 2016 (Croatian Chamber of Commerce, 2016). After the war for the independence of Croatia in 1990s, the

recovery of the whole country, economy and tourism took years. The years of the recovery finally reached the peak when 16,3 million arrivals and 91,3 millions of overnight in 2016 its been recorded, which was the highest recorded number by that time (Ministry of tourism Croatia, 2017)

Dalmatia is the largest tourist region in Croatia with three major tourist destinations – Zadar, Split and Dubrovnik. From high luxury upscale hotels to motels, camps and variety of private accommodations this region offers accommodation for any type of the travelers.

Dubrovnik

Dubrovnik as the most famous tourist destination in Croatia has a long tradition in tourism mostly because of its unique architecture. The confirmation of development potential has are visible in the statistics where in 2007 the city of Dubrovnik had 1.6 million overnight stays while in 2017 the number increased to 3.4 million (Croatian Chamber of Commerce, 2017). High-end hotel facilities and private accommodations are the predominant accommodation offer. Among the overall number of the accommodations properties 58% of the market are private accommodations while hotel properties occupy 35% (Croatian Chamber of Commerce, 2017).

Dubrovnik's existing hotel supply is a mostly high luxury segment where the targeted market is the one with higher income - similar to Dubai, where 49% of hotels are luxury 5 and 4 star hotels. In Dubrovnik the proportion is even higher – 54% (26 hotels) of the current properties are luxury upscale hotels and 40% (19 hotels) the mid-scale properties (Dubrovnik Tourist Board, 2020). From the overall number of overnights in 2007, 75 percent of tourists was accommodated in the hotels, while 10, 5 percent of tourists were in the private accommodations. From the overall number of overnights in 2017, 53 percent of tourists were

accommodated in the hotels, while 34 percent of tourists were in the private accommodations (Tourist Board of Dubrovnik, 2020).

Split

Split was considered for many years as a transit destination but in the last ten years the city of Split achieved record tourist results. The statistics show that in 2007, the city of Split recorded 407, 301 overnights, while in 2017 the number increased to 2.1 million (Tourist Board of Split, 2017).

In Split private accommodations occupy 68,5% of the lodging market while hotel properties are only 11,21% (Tourist Board of Split, 2017). Most dominant hotel supplies in Split are upscale hotels (4 star hotels) with 61% (21 hotels) from the overall hotel supply. Mid-priced hotel are second major supplier with 29% (10 hotels) from the overall number. Luxury hotels (5 star hotels) are just 5 % (2 hotels) of the market and one hotel that is classified as two star hotel 2% of the market (Tourist Board of Split, 2020).

-Waiting for the data of Tourist Board of Split about the exact percentage of overnights in private accommodations and hotels in 2007 and 2017

By analyzing the data collected from two different mid-priced markets in Dubrovnik and Split, the purpose of this research - to identify potential areas for growth and to meet challenges of increasing competition from private accommodations in two different cities - will be supported.

METHOD

The online observation of hotel websites, analysis of existing data from local authorities and email inquiries to hotel management were used to collect detailed information about existing three star hotels, including:

- Location (Dubrovnik, Split)
- Ownership (International chain, Domestic chain, Independent)
- Seasonal length
- Size (number of room and beds)
- Room category based on the number of beds (small - up to 160 beds, medium - up to 380 beds and large category beyond 380 beds)
- Price (peak double room in July per night, 25th - 26th)
- Category based on the relative price of the room (low, medium, high)
- Availability of pool (yes/no)
- Availability of wellness (yes/no)
- Availability of room service (yes/no)
- Conference space capacity (number of attendees)
- Availability of conference amenities
- Age of the hotel (year opened)
- Age category (historic, mid century, new)
- Year of most recent renovation
- Location type (airport hotel, city center hotel, island hotel, suburban hotel)

The qualitative approach was primarily used while collecting the data for the analysis and all information was based on the 2019 calendar year, summer season.

RESULTS

Data was gathered for 19 hotels in Dubrovnik and 10 hotels in Split where 18 pieces of data were collected for each hotel. The results showed a significant difference between the mid-market hospitality offers in two tourist destinations in Croatia. This research differentiated hotel individually but at the same time it differentiated two Croatian mid-price markets in the city of Dubrovnik and the city of Split.

Relative size of mid – market segment

The data showed that there is a big difference in hotel supply in the city of Dubrovnik and Split. In the city of Dubrovnik there are much more luxury (5star) and mid-priced (3 star) properties compared to Split, where most of the hotels were upscale properties (4 star).

The results of the analysis showed that 40 percent (19 properties) of in the city of Dubrovnik are 3 star hotels. Upscale – four star properties are 23 percent (11 hotels); Luxury – five star hotels are taking 31 percent (15 hotels); 4 percent (2 hotels) of the overall market are categorized as two star hotels.

The results analysis of Split hotel chain showed that 29 percent (10 hotels) are mid-market properties. Upscale – four star properties are 61 percent (21 hotels); Luxury – five star hotels are taking 5 percent (2 hotels) of the overall market and the last one are 2 star hotels 2 percent (1 hotel).

Ownership structure

Most of the properties in both of the cities are managed by independent owners.

It is interesting that in the city of Dubrovnik 57 percent (11 hotels) of 3 star properties are managed by independent owners, usually family owned hotels. Domestic chains own 42 percent (8 hotels) while international chains own 5 percent (1 hotel).

Even more interesting results were from the city of Split, where all 10 mid-priced hotels, are owned by independent owners.

Seasonal length

Most hotels in Dubrovnik operate seasonally, while most hotels in Split operate all year.

The opening date for most of the mid-priced hotel properties in Dubrovnik was March and closing was November 57 percent (11 hotels). Following were hotels that operate all year 15,7 percent (3 hotels). From May to September only 10,5 percent (2 hotels). An additional 15 percent (3 hotels) operate on shorter seasonal basis. The data for one hotel was not available. However, most of the mid-price hotels in the city of Split are open all year 80% (8 hotels). One hotel is working from February till December. Information was not available for one hotel.

Capacity

In both cities most of the hotels were categorized as small hotels.

In the city of Dubrovnik most of the hotels were categorized as a small hotels 57,8 percent (11 hotels); medium hotel occupied 26,3 percent (5 hotels) of the market while as large hotels were categorized as 15,7 percent (3 hotels).

In the city of Split all of the hotels were categorized as small hotels 100 percent (10 hotels).

Relative price

The difference between the markets is clearly visible in the price of the rooms. There were no high price hotels in Split, while in Dubrovnik most of the hotels were categorized as medium and high.

In the city of Dubrovnik the results showed that as medium price properties are 36 percent (7 hotels) of the hotels and the same percentage is for the low price properties 36 percent (7 hotels). The rest of the properties was marked as a high price hotels 28 percent (5 hotels).

Most of the 3 star hotel properties in the city of Split were categorized as low price 80 percent (8 hotels) and the rest of the properties were medium price 20 percent (2 hotels). There were no 3 star hotels with relatively high price.

Amenities

From the data collected it is evident that mid-priced hotels in Dubrovnik provide much more amenities than the ones in Split.

Among mid-priced properties in Dubrovnik, about half, or 52 percent (10 hotels) have available pool for the guest while the rest of the properties 48 percent (9 hotels) is not providing the pool. Room service is about as equally divided as pool. Regarding the room service in Dubrovnik mid-market, 48 percent (9 hotels) provide room service while the rest 52 percent (10 hotels) is offering room service. The wellness service in the city of Dubrovnik for the mid-priced market is providing 57 percent (11 hotels) and the rest 43 percent (8 hotels) is not providing it.

In the city of Split 90 percent (9 hotels) does not have the pool, while only 10 percent (1 hotel) offers pool.

In the city of Split 40 percent (4 hotels) are providing the room service, while 60 percent (6 hotels) does not provide it. In the city of Split 20 percent (2 hotels) is providing the wellness service while 80 percent (8 hotels) is not providing it.

Conference space capacity

In the city of Dubrovnik, less than half of the hotels provide conference space, while in the city of Split only two hotels are offering it.

From overall number of 19 mid- priced hotels in Dubrovnik 57,8 percent (11 hotels) of the properties do not provide any conference space. Three hotels provide small capacity space (50 people); one hotel provide medium capacity space (160 people); four hotels provide large capacity space (200-260 people)

Three star hotels in Dubrovnik are providing basic conference equipment along with the space (Hotel Vis, Hotel Komodor, Hotel Splendid and Hotel Ivka).

In the city of Split only 20 percent (2 hotels) provide small conference space (80 people) and the rest 80 percent (8 hotels) is not providing it.

Conference space for 30 people provide 10 percent (1 hotel); 10 percent (1 hotel) provides conference space for 80 people. Only one hotel provides basic conference equipment.

Hotel age and condition

In the city of Dubrovnik, there are fewer new hotels and an equal number of historic and midcentury hotels, but recent renovation had almost half of the properties. In the city of Split half of the hotels are the new ones and there is equal number of mid-century and historic hotels. The reason behind the lower renovation percentage in the city of Split could probably be because of the high number of new hotels.

In Dubrovnik, the current 3 star hotel stock is about equally divided among historic, midcentury and new property. As historic properties were 31,5 percent (6 hotels); as mid – century properties were 36,8 percent (7 hotels) and the remaining were 26,3 percent (5 hotels) of properties which were marked as new. Recent renovation in the city of Dubrovnik had 47 percent (9 hotels) of the properties, while 10 percent (2 hotels) were renovated in the late 90's. The information of the latest renovation was not available for 21 percent (4 hotels) of the properties. The rest of 26 percent (5 hotels) were new building, so the renovation was not necessary.

In the city of Split 49 percent (4 hotels) were categorized as new hotels, while 10 percent (1 hotels) as mid-century property and 10 percent (1 hotel) as a historic. For the rest of the properties 40 percent (4 hotels) the data was not available. Recent renovation in the city of Split was done on two of the hotels, one that is categorized as historic and one that is categorized as new.

Location type

Most of the mid-price hotels in Dubrovnik were categorized as suburban hotels, while in the city of Split there were more city center hotels. Given the context that city of Dubrovnik is a small city, especially when compared to Split where city center is much broader.

As a suburban properties was categorized 84 percent (16 hotels); 10 percent (2 hotels) were categorized as island hotels; percent (1 hotel) was categorized as airport hotel.

In the city of Split mid-priced hotels were mostly situated in the suburban as well 60 percent (6 hotels), while the rest 40 percent (4 hotels) were situated in the city centre.

DISCUSSION

Limitations

The limitations of this research were a small amount of the unavailable data, particularly regarding dates of renovation of existing properties. Although some the required data was not available online, it was collected through the online communication with the property managers, but didn't provide the required data. So, the limitation of this research is the missing data that affected the percentage result in specific categories, but from all of the listed categories neither category has significant percentage of missing data.

Both Dubrovnik and Split hotel market is dominated by high luxury hotels where the absence of more quality and trendy three-star hotels creates the opportunity for the further development of the mid-priced market. As already said, quality doesn't necessarily mean luxury. Future development perspective is clearly visible based on the increasing number of arrival in both of the cities, but the rise of Airbnb and favoring the private accommodations among travelers created an enormous competition challenge. Private accommodations, upscale and luxury segments have been driving the local hospitality sector but by recognizing the potential in further increasing demand for the mid-priced hotels, the quality offer development of the whole destination could close the gap on the hotel market. The maturity of the destination by offering diversified quality hotel supply should be highlighted to create sustainable tourism, especially now when the world economic crisis will affect the tourism as a whole, traveler's income, and decisions. The absence of international hotel chains and brands of mid-priced properties in both of the cities could be seen as the opportunity for foreign developers to enter the market. Most of the hotels in both markets are family-owned properties that are categorized as three star hotels but based on the amenities and higher

prices, especially in Dubrovnik market, it could be said that these properties are branching out to boutique style. It, even more, complicates and questions the star rating system, which clearly is losing its relevance by time. Unlike to Split, clear seasonality of tourism of the city of Dubrovnik is visible in the opening and closing date of the hotels - because generally from November and the end of the March city depends only on the business and events tourism - which is the obvious limitation for the local hotel market. Lack of conference spaces in the mid-priced hotels in Dubrovnik and Split is another limitation of the offer; congress, wedding and banquet events are obviously not in the focus in the city of Split based on the data collected. By investing in meeting and banquet spaces, especially hotels in Split which are operating mostly all year, the hotels could use the opportunity for further development in that segment and prolong the season. The capacity of the hotels differs in both markets as well, which is a clear indicator of the potential in both markets. Interestingly, the city of Split is much bigger than the city of Dubrovnik where the price of the land is much higher, but in the city of Split properties are smaller and newer, while the ones in Dubrovnik are larger and older. The condition of the mid-priced hotels in Split is better than the ones in Dubrovnik and the price of the ones in Split is lower. The reason behind it is probably the demand on the market and a higher price of the land in Dubrovnik. As well, in Dubrovnik mid-priced properties provide more amenities than the ones in Split. By investing in more amenities the properties in Split could upgrade their quality of the offer and experience and attract more potential guests.

To understand the complexity of the mid-priced hotel industry in different market structures, it is necessary to monitor and understand the development of tourism trends and consumer needs and expectations - which leads to the analysis of tourism markets and competition.

Bearing this in mind, the major transition from the economics of services, to the economics of

experiences should be the key approach for the mid-priced market, while positioning themselves against the private accommodation competitors.

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Appendix:

Dubrovnik Hotel Supply			
	5 star	15 hotels	31%
	4 star	11 hotels	23%
	3 star	19 hotels	40%
	2 star	2 hostels	4%
TOTAL		47 hotels	

Split Hotel Supply			
	5 star	2 hotels	5%
	4 star	21 hotels	61%
	3 star	10 hotels	29%
	2 star	1 hostels	2%
TOTAL		34 hotels	