Research into European hotel market shows number of franchises is overestimated

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Research by law firm Field Fisher Waterhouse LLP into the hotel industry has shown that only between three and four per cent of hotels in Europe are part of a franchise, far lower than previous estimates.

The research found that there are approximately 200,000 hotels in Europe but only a small proportion of these are franchised. Previous reports had only looked at franchises of major hotel chains, overestimating the number at closer to 30 per cent.

The research further found that franchising as a business model is not as successful in Europe as it is in the United States and Australia. Comparing the scale of the franchise industry in Europe to the US and Australia it was seen that whilst the turnover from franchising in Europe is estimated to be only two per cent of GDP, in the USA it is nearer six and in Australia it reaches ten per cent. This differential suggests that franchising is not realising its full potential in Europe.

Estimates that placed the number of franchised hotels in Europe at between 25 and 30 per cent were completely unrealistic.

The research showed that brands such as Best Western and Choice who offer a 'franchise light' model have been more successful in Europe than traditional US franchisors that have a strict list of mandatory brand standards. Best Western topped the league table of European franchise brands with 1,300 hotels, followed by French brands Accor and Louvre with 750 and 600 respectively. Choice and Intercontinental with 500 franchised hotels each are also relatively successful while major global brands such as Marriott and Starwood have less than 100 franchised hotels in Europe, traditionally focussing their efforts on management agreements. Some regional markets such as the UK, Germany and Spain continue to be mainly lease driven with the likes of Premier Inn, Travelodge, NH and Barcelo showing almost no franchised properties. Other players at the five star end of the market are unwilling to consider franchising as a business model. Hyatt, Fairmont and Four Seasons do not franchise in Europe. The reason often given is that it is more difficult to maintain quality standards in five star properties operated under a franchise model.

The main difference between a franchise and a management approach is that the franchisee will itself operate the hotel based on a manual and certain training provided by the franchisor. This can lead to lower standards of service unless the franchisee is a very experienced operator. If the hotel is operated under a management agreement the brand owner will control and supervise the operation of the hotel and prepare the budget therefore preventing a drop in standards. The control over the budget also gives the manager more say in the level of investment. Franchisees can be more reluctant to invest in new brand features.

On the other hand, franchising is a straight-forward and low-cost strategy for brands that want to expand internationally and there are sectors such as pizza delivery and tuition where the franchise business model is thriving.

It has been suggested that one of the reasons for the limited success of franchising in Europe is the unusually large amount of legal regulation and complexity. There are eight EU countries with franchise laws generally requiring franchisors to provide a technical disclosure document comparable to an investment prospectus to franchisees. In this document the risks and costs of buying a franchise have to be made plain. This could put potential investors off. On the other hand, it is interesting to note that hotel franchising has been very successful in France, reaching similar figures to those achieved in the US and Australia. France is one of the eight European countries with a franchise disclosure law, yet it has a huge franchise market for budget brands such as Ibis, Campanile and Formule 1 driven by the likes of Accor and Louvre. This suggests that franchise regulation is not the main reason that is stifling growth.

Another important factor is the level of control that Franchisors seek to exercise. Generally hoteliers are independent entrepreneurs and do not like to be told how to run their hotels. This is where there is a particular opportunity for the ‘franchise light’ model. This is a franchise model where brand standards are scaled back to a list of 20-30 must have features to open membership of the brand to a broader audience. For example German based Worldhotels have recently created a franchise light product that seeks to appeal to this market. Pioneers in the US have added additional features designed to tempt hoteliers to try the brand. For example Vantage Hospitality offer a 12-month rolling contract so the franchisee can leave the system at short notice if they do not feel that the brand is adding value.

It is expected that we will see more franchise light offers in Europe soon.

Franchising can be a very cost effective way for hotel brands to put flags on maps. Many European owners dislike management agreements which do not guarantee a minimum revenue in the same way as a lease. In a franchise model the franchisee will take the lease from the owner and enter into a franchise agreement with the brand so this satisfies the lease driven owner base. For potential franchisees it gives their hotels access to the added reach that the marketing expertise and loyalty programmes of big brands can bring. In some cases room rates can also be increased significantly by adding a major brand. This is not guaranteed however. As increasing numbers of guests look for value options, we are also seeing the franchising model used more and more at the budget end of the spectrum where it is easier to replicate the customer experience.