

Managing State-owned Hotels in China: the Challenges and Remedies

Kam Hung, Assistant Professor (Corresponding author)
School of Hotel and Tourism Management
Hong Kong Polytechnic University
Address: Room 705, School of Hotel and Tourism Management,
17 Science Museum Road, TST East, Kowloon, Hong Kong
Phone: (852) 3400 2258
Fax: (852) 2362 9362
Email: hmkam@polyu.edu.hk

Hanqin Zhang, Hong Kong Polytechnic University, [Hong Kong](#)

Chi Fung (Kelvin) Lam, Chinese University of Hong Kong, [Hong Kong](#)

Guo Qiang Yang, Tourism College of Zhejiang, China

Dai Xin Pang, Heilongjiang Agriculture Management Training Center, China

Zhong Wen Chen, Hangzhou Power Real Estate, China

Jing Li, Celebrity City Hotels, China

Fu Ying Yang, Dahua Hotel, China

Lin Quan Yan, HNA Hotel Group, China

Chen Fei Wang, Cangnan Tourism Board, China

Yuan Deng, Hangzhou Qiandao Lake Yanshan Resort Co. Ltd., China

Managing State-owned Hotels in China: the Challenges and Remedies

ABSTRACT

State-owned Hotel (SOH) management is highly controversial given its poor economic performance, state ownership, and unique management structure. The purpose of this paper is to identify the challenges of SOHs and discuss how the SOHs can improve their performance. The results, based on 15 semi-structured interviews with state-owned hotel senior managers and employees, suggest that the SOHs in Hangzhou are encountering various problems in relation to their ownership, human resources, market competition, and management. Suggestions to improve the performance of SOHs in China are offered.

Keywords: State-owned Hotels; China; Ownership; Human Resources; Competition; Management

INTRODUCTION

China has been experiencing tremendous economic growth since implementing an Open Door Policy in 1978. The average growth rate of GDP in China was about 9.31 percent from 1980 to 2010 (National Bureau of Statistic 2011). The tourism and hotel industry was the first to open its market to foreigners and thus is considered a pioneer of economic reform in China (Pine et al., 2000). With the strong support of the government and the favorable business environment, the number of star-rated hotels in China reached 14,237 in 2009; 5,318 were State-owned Hotels

(SOHs), 850 were Collective, 357 were Shareholding Co-operative, 66 were Alliance, 3,135 were Limited Liability, 725 were Limited Liability Share, 2,922 were Private, 345 were Hong Kong, Macau, Taiwan Invested, 229 were Foreign Invested, and 290 were another type of ownership (CNTA, 2010). Although SOHs are the primary type of hotel ownership in China, the majority of them are experiencing either low profit margins or losses (Cai, Zhang, Pearson, & Bai, 2000; Cai, 2004; Mak, 2008). State ownership has been identified as the major cause of such inefficiency given its lack of focus on profit-making and excessive political control over hotel management (Tang et al., 2006; Cai, 2004). Ownership reform has been recommended as an answer to remedy the unprofitability of SOHs (Tang et al., 2006).

Even though ownership reform over the years has reduced the share of SOHs from 59 percent in 2001 (CNTA, 2002) to 38 percent in 2009 (CNTA, 2010), A large number of SOHs and continued inefficiency in operations has led some scholars (e.g., Tang et al., 2006) to conclude that SOHs remain one of the least progressive sectors in China in terms of ownership reform and financial performance. While China's leaders have given priority to the reform of State-owned Enterprises (SOEs), they also insist that large scale SOEs should remain under public ownership and that they will not accept the mass SOE privatization that occurred in many Eastern European countries (Perkins, 1999). Given the unwillingness of the government to engage in full privatization of SOEs and the unprofitability of SOHs, it has become important to identify and remedy the problems plaguing SOHs. Although a number of initiatives have been taken to investigate various aspects of China hotel industry including its most critical issues (Hung, 2012), expatriate hotel managers (Miao, Adler, & Xu, 2011), economy hotel branding (Zhang, Cai, & Kavanaugh, 2008), and multinational hotel image (Huang & Cai, 2010), limited attention has been given to explore the challenges experienced by the SOHs. Such knowledge is

critical for managers to implement corresponding strategies to enhance the efficiency and profitability of SOHs. The purpose of this paper is to identify these challenges based on in-depth interviews with the Chinese hoteliers associated with some SOHs in China and discuss how these challenges may be resolved.

LITERATURE REVIEW

Reforms of State-owned Enterprises (SOEs)

Before 1978, two years after the Cultural Revolution, the only legal form of ownership in China was state ownership (Aivazian et al., 2005). These enterprises were extremely inefficient experiencing only a 0.4% annual growth rate of productivity between 1957 and 1978 (Groves et al., 1994). Managers of SOEs had a limited ability to control product price, set wages, and make employment decisions. Staff of SOEs had high job security due to the “iron-rice-bowl” (i.e., tenure) policy (Lin et al., 1999). The SOEs were mainly financed via interest-free loans from the state. According to Cull and Xu (2003), People’s Bank of China, which is the largest state-owned bank in China, was responsible for 93 percent of all loans made by financial institutions in China.

The reform of SOEs in China began in 1978 (Groves et al., 1994). The first wave of reform promoted a profit retention system in which managers of SOEs took full responsibility for the profits and losses of their enterprise. A target profit was set ex-ante. When SOEs exceeded the profit quota, they got to keep excess profit either at full or at a pre-determined amount (Lin et al., 1999). However, if the target profit was not achieved, the enterprise would have to make up the difference (Lin et al., 1999). Prior to the implementation of this profit retention system, the SOEs were required to remit all profits to the state (Groves et al., 1994). The purpose of this reform was to provide an incentive for SOEs to enhance their performance (Jefferson & Rawski, 1994;

Groves et al., 1994). Although SOEs' productivity increased significantly after the introduction of this scheme (Groves et al., 1994), various problems emerged including: difficulties in identifying appropriate target profit (Aivazian et al., 2005); lack of proper incentive policies for SOE staff (Cauley & Sandler, 1992); and unclear guidelines for evaluating SOEs as well as worker performance (Tang et al, 2006; Mak, 2008).

The second wave of reform was implemented in 1984 and had two main components: Dual Price System and Contract Responsibility System. Under the Dual Price System, SOEs managed sales and purchases in accordance with supply and demand in the market. After fulfilling the quota requirement of the states, SOEs could sell the extra output on the free market (Lau et al., 2000, Roland, 1999, Li, 1999). At the same time, bank loans became the principal sources of external funding (Jefferson & Rawski, 1994). The Contract Responsibility System required managers and relevant parties to agree on pre-determined obligations, such as target profits, amount of profit contributed to the states, and level of productivity in return for less control by the government over the enterprise (Jefferson & Rawski, 1994). Despite these reform strategies, SOEs still suffered losses. In 1993, the total loss of SOEs was 45.3 billion Renminbi (RMB), about 14 times greater than losses in 1985 (Lin et al., 1999).

The third wave of reform was initiated in 1993. The state attempted to sell small and medium SOEs to private companies while keeping the large SOEs (Siqueria et al., 2009; Cauley et al., 1999). This reform also included assigning SOE ownership to the State Asset Supervision and Administration Commission (SASAC). Ideally, the SASAC would be considered owners of the SOEs and the SASAC would motivate the managers and workers by providing them appropriate rewards (Siqueria et al., 2009; Cauley et al., 1999). Before the introduction of the Labor Law in 1995, all SOE employees were tenured because of the "iron-rice-bowl" policy

(Lee, 1990, cited in Cauley & Sandler, 1992). During this third stage of reform, managers had greater autonomy in that they could employ or lay off workers. This power did not exist under the “iron-rice-bowl” system (Hu et al., 2006). Furthermore, state intervention was minimized in an attempt to further develop a modern management system which separated governance and management of SOEs (Hassard et al., 2010).

Problems of SOEs and SOHs

Despite a series of reforms, problems with SOEs are continuously being reported. One key problem is a failure to separate ownership and management (Pine, 2002; Tang et al., 2006). This results in poor monitoring of state assets (Pine & Phillips, 2005; Tang et al., 2006) and a lack of incentives to improve business performance (Tang et al., 2006). Additionally, state investors exercise controlling right to SOEs, and these influences may conflict with the profit maximization of the firms (Tang et al., 2006; Mak, 2008). Because management is not held accountable for performance, there is no motivation for managers or employees to improve business performance (Shirley, 1999). Many SOHs were previously “receiving-style hotels”, first built to provide accommodations for visiting officials from the Communist Party and later to house international officials (Mak, 2008). The most common is the “I-owe-you” payment; basically free accommodations in the hotels with the assumption that the return of this favor will occur at a later time. It was not unusual for officials to occupy hotel rooms for long-term business use, with the restaurants serving as dining rooms for officials, their guests, and their families (Cai, 2004). Guests considered these entitlements but these practices contributed to the poor performances of the SOEs (Cai, 2004). As Heung et al. (2008) point out in a healthy market model, when firms sustain losses they go bankrupt and hence reduce the supply in the market.

However, with monetary support from the state, these under-performing firms stay in the market, which distorts the supply and demand mechanism. These under-performing firms create more competition for existing firms while greater loans and intervention from the state investors is required. As a result, a vicious cycle continues. An additional problem occurred when some government officials built luxury hotels to showcase their achievements without considering market needs (Tang et al., 2006). However, no one is held accountable for the loss of these luxury hotels after the relevant personnel have left their positions.

Scholars generally agree that lack of incentives is one of the major problems in staffing Chinese SOEs (Groves et al., 1994; Lin et al., 1999). Most employees of SOEs are not motivated to produce more than minimum required output because of their fixed remuneration (Groves et al., 1994). Managers cannot discharge inefficient workers due to the “iron-rice-bowl” policy (Lin et al., 1999) and/or turn down the recommended personnel for hiring from some government officials (Yin, 2001). These result in instances of overstaffing problem within the SOEs (Yin, 2001). Consequently, the pension benefits of these redundant workers become a major financial burden for many SOEs (Pine, 2002). Even with the introduction of the Profit Retention System, managers are not motivated to provide incentive schemes for staff because of associated costs and/or wage disparities that would emerge among staff (Groves et al., 1994). Mak (2008) pointed out that the function of remuneration is directed by the Property Department, which lacks information regarding the ability and performance of workers, thus making remuneration criteria both unclear and unfair. This problem exists not only for junior workers but also senior managers and government officials (Tang et al., 2006; Cai, 2004; Cauley & Sandler, 1992).

In conclusion, many scholars have tried to identify the causes of inefficiency in SOEs/SOHs. Although this is not an exhaustive list, the problems of SOEs/SOHs include: lack of job

motivation (Groves et al. 1994; Cauley et al. 1999; Cauley & Sandler, 1992; Lin et al. 1999, Aivazian et al. 2005); failure to separate ownership and management (Omran, 2004; Pine & Phillips, 2005; Tang et al., 2006; Benson & Zhu, 1999; Pine, 2002; Cauley et al, 1999; Siqueria et al., 2009; Pine & Qi, 2004; Perkins, 1999; Cao, 2001; Shirley, 1999; Mak, 2008); nepotism (Cai, 2004; Tang et al., 2006; Mak, 2008; Pine & Qi, 2004; Cao, 2001); short term employment of government officials (Cai, 2004; Tang et al., 2006; Mak, 2008); poor evaluation criteria (Cai, 2004; Tang et al., 2006; Mak, 2008; Cauley & Sandler, 1992); and social objective conflict with profit maximization objective (Omran, 2004; Cull & Xu, 2003; Tang et al., 2006; Boardman & Vining, 1989; Mak 2008; Pine, 2002; Choe & Yin, 2000; Hu et al., 2006; Puterman & Dong, 2000). Since studies of SOEs have been substantial, it would be out of the scope of current study to provide a complete list of them. However, among the aforementioned SOE related articles, only five of them (Cai, 2004; Tang et al., 2006; Shen & Chon, 2007; Heung et al., 2008; and Mak, 2008) investigated SOHs with only one of them published in the form of conference paper (Shen & Chon, 2007).

The conference paper written by Shen and Chon (2007) identified transaction costs of property right as a key determinant prohibiting the reform of SOHs and suggested that privatization, either in full privatization or in the form of shareholder system, is the only solution to the problems of SOHs in China. Tang et al. (2006) examined the corporate governance structure of SOHs in China and identified ownership structures and soft budget constraints as the key problems of SOHs. They pointed out that given that SOHs are financed by state-owned banks, they are obliged to respond to the “orders” sourced from government officials. Cai (2004) investigated both state-owned economy and budget hotels in China based on interviews with hotel operators. Heung et al. (2008) examined state-owned independent hotels and state-owned

franchised hotels and discussed the intentions and reasons of SOHs to join an international franchise operation. Mak (2008) also analyzed problems facing the SOHs. While these studies have contributed to our understanding of SOHs, their samples are focused mainly on management levels or hotel operators, and most of them examined the SOHs issues at a national level with study samples from multiple regions of mainland China. This study is intended to examine the most updated issues concerning the SOHs in a more homogeneous study context, i.e., a single city, with the inclusion of not only managers, but also hotel employees in the study sample. Specifically, this study aims to identify the challenges currently faced by SOHs in the city of Hangzhou, China and discuss how to remedy these problems in connection with local's characteristics. It is expected that the results will enhance our understanding of SOHs and provide some direction in managing such enterprises in China.

RESEARCH METHODS

A qualitative research approach was used in the current study in an attempt to better understand the current problems, and their potential remedies, of SOHs in China. The state-owned hotels in Hangzhou, China were used as examples to understand the difficulties experienced by SOHs. Hangzhou is one of the fastest growing second-tier cities in Mainland China in terms of tourism development. According to CIconulting (2010), 208.6 million international and 41.12 billion domestic travelers visited the city in 2007. The blooming tourism has stimulated rapid growth of the hotel industry with as many as 250 star-rated hotels having been established by the end of 2007. This number continues to grow with a gradual shift of hotel management from the dominance of state-owned hotels in the past to the co-existence of various forms of hotels in the current market. The total revenue of Hangzhou hotels in 2007 was 793.2

million RMB, which was about 22.18 percent above the national average of all hotels and represents and comprised 1.93 percent of the city's total GDP. Since the 80's, international hotel brands such as Shangri-la, Radisson, Sofitel, Howard Johnson, Hyatt, Ramada, Four Seasons, Jumeirah, Amman, Sheraton, Banyan Tree, Crown, Marriott, and Park Hyatt have gradually entered Hangzhou, which has resulted in more fierce competition in the hotel market. In such a competitive market, concerns for the survival and effective management of state-owned hotels have emerged among hotel professionals.

Interviews were conducted in October 2010 with hotel practitioners in five hotels in Hangzhou including Hangzhou Da Hua Hotel, Grand Metropark Hotel, Hangzhou Huajia Shan Resort, ZTG Resort Thousand-Island Lake Hangzhou, and Best Services Hotel. All hotels were state-owned hotels which were chosen based on investigators' personal contacts. The basic information of the five hotels is presented in Table 1. Fifteen face-to-face semi-structured interviews were conducted with various levels of personnel in the hotels to reveal a broader spectrum of analysis (Table 2). The participants include General Managers (3), Assistant General Managers (2), Managers of various departments (4), and other employees (6) of these SOHs (Table 2). Eight participants were males and seven were females. The average age of the participants was 37.3 with 61 recorded as the maximum age and 22 as the minimum age. On average, participants have worked in the industry for 15.9 years with those at management levels having more substantial working experience (24.3 years) than non-managerial participants (3.2 years). Participants at managerial positions also have longer years of service in the current SOH (13.6 years) than other interview subjects (2.5 years).

TABLE 1

TABLE 2

Participants were asked to describe the current conditions of SOHs and identify challenges faced by the hotels in the interviews. Information of various aspects of SOHs such as hotel operation, human resources, market positioning, and other critical issues of SOHs were probed in the interviews. The longest interview was over 45 minutes with the remainder lasting approximately 30 minutes each. The average duration of the interview was about 35 minutes. The lengths of interviews were subjected to the data saturation instead of being determined *a priori*. The interview was conducted at hotel offices where interruptions could be kept to a minimum. Open-ended questions were used to establish a general profile of the interviewees, and the challenges and opportunities faced by SOHs. All interviews except for discussions of sensitive topics were recorded after consent from participants was obtained. When participants requested that conversations not be recorded because of sensitive topics, notes were taken to avoid information loss.

Transcripts were analyzed by two researchers using a grounded theory deductive approach. Grounded theory is used to build a better understanding of the phenomenon which emerges from the interviews and is grounded in the raw data. It strives to help qualitative analysts by: handling masses of raw data; considering alternative meanings of the phenomenon; and elucidating the concepts that are the building blocks of the theory (Patton, 2002). As the current research attempts to generate a holistic understanding of the SOH's phenomenon in China, grounded theory directs and disciplines the methodology in such a way that the results and findings can be

organized into meaningful categories. From this method, key issues, mainly centered on ownership, human resources, market competition, and management emerged from the interview data.

FINDINGS AND DISCUSSION

Ownership of SOHs

Nine participants compared ownership of SOHs with ownership of international hotel brands and suggested that the ownership of international hotels is more clearly defined. In international hotels, management is separated from ownership which results in a clear definition of managers' roles and more efficient operation of hotels. In contrast, Hangzhou SOHs are similar to a product of planned economy. The ownership and management of these state-owned properties are not as clearly divided. There was constant intervention by government entities in hotel operations and management, which resulted in low efficiency, unprofitability, and less of an ability to compete in the hotel market. In the interviews, four (assistant) general managers mentioned that their decision-making abilities are often constrained due to the intervention of government officials. A participant noted: "We have a secretary of communist party directly appointed by the local government to work in our hotel. He oversees any matter relating to the party and has absolute power in influencing hotel major decisions when deemed to be necessary." An additional impediment was a lengthy wait time for approval of their business proposal because of the bureaucratic management structure.

Participants also mentioned that profit-making is not regarded as the most important objective of these SOHs. Due to SOHs' responsibility to the government, priority is often given to providing government officials hospitable services. A general manager commented: "Our

primary mission is to provide high quality hospitality service with high security for government officials and invited guests.” Such prioritization is in conflict with other aims of SOHs including enhancing the SOHs’ asset value and meeting the predetermined profit. These conflicting roles have resulted in inefficient operations and unprofitability.

State ownership has been identified as a root cause of inefficient operation of SOHs (Cai, 2004). Although privatization is a necessary condition for improving corporate governance (Watanabe, 2002), many scholars agree that it is not the only condition (Mak, 2008; Cao, 2001; Watanabe, 2002; Tang et al., 2006). Cao (2001) pointed out that privatization is not simply transferring ownership from state to private hands. Privatization in transitional economies requires establishment of a well-defined property structure both within and outside the business (Cauley & Sandlers, 1992; Cao, 2001; Lin et al., 1999), establishment of an effective management and accounting system (Mak, 2008), and establishment of a competitive market (Lin et al., 1999). In the current study, Best Service Hotel launched a reform of ownership with 40 percent of the share held by the Zhejiang Supply and Marketing Cooperative. The remaining shares were sold through internal purchase. However, a mandatory provision was imposed, which required employees to sell their shares to existing shareholders when they left their positions in the hotel. However, this reform did not improve the hotel’s financial status. In 2010, the Zhejiang Supply and Marketing Cooperative planned to re-purchase employees’ shares. Participants mentioned that ownership reforms are currently being implemented in a number of SOHs in China such as Feng Hotel, Okura Garden Hotel, China World Hotel, LiuHua Hotel Corporation, Aiqun Hotel, BinJiang Hotel, Guangzhou Hotel, JinJiang Hotel, and Crown Plaza Chengdu. More time is needed to evaluate the results of such reforms.

In his discussion of state ownership, Pine (2002, p. 63) stated “The chief problems

occasioned by state ownership are the failure to separate hotel management and ownership and effective monitoring of the state's assets." Almost ten years later, it was found that this phenomenon still exists in the SOHs in Hangzhou and is negatively affecting hotel operations. Therefore, unless there is commitment from the government to reform the ownership/management structure, the inefficiency of most SOHs is likely to continue. To make SOHs more profitable, the ownership should be separated from hotel management thus preventing excessive government intervention on hotel operation and facilitating faster managerial decisions.

The obligation of SOHs to provide hospitality services to visiting government officials has become an operational burden for the SOHs while attempting to fulfill their other obligations, such as meeting the target profit preset by the government. It seems that the "I-owe-you" culture noted by Cai (2004) no longer prevails in the SOHs. However, to charge a regular rate for these reception duties seems to be incompatible with the high operational costs and many inconveniences caused by such activities in regular hotel operation. However, a participant mentioned: "Although we need to meet the preset profit, this is neither our primary mission nor the top criterion for evaluating our performance. Rather, provide high quality hospitality service with high security standards to the government officials are our top priorities." Such a priority highlights the unique nature of SOHs and explains their underperformance in profit-making in comparison with other hotels.

Human resource issues

Human resource is another key issue of SOHs. It was suggested by six participants that most senior employees in SOHs in Hangzhou are not motivated to excel in their jobs due to the secure

“iron-rice-bowl” system. Furthermore, their loyalty to the SOHs seemed to be higher than non-SOH employees despite the lack of job motivation and competition among them. The management style of the SOHs was identified to be more humanized while management in international hotels is more structured and systematic with clearly identified rules and guidelines. One participant commented, “We are together for better or for worse. We do not outperform each other.”

Cheng and Brown (1998) argued that high labor turnover rate is one of the key problems for the hospitality industry. However, this problem was not found among the employees of the SOHs used in this study. All managers from the five hotels suggested that their hotels experience a relatively low labor turnover rate; lower than international hotel brands and the industry average. This may be due to the residual effect of “iron-rice-bowl” policy among senior employees in SOHs and the lack of internal competition among hotel staff.

The reported human resource problem coincides with the previous literature in which “iron-rice-bowl” policy and lack of incentives were identified as the major causes of such problems (e.g., Groves et al., 1994; Lin et al., 1999; Yin, 2001). If the state is to retain its ownership of SOHs while achieving financial excellence, the “iron-rice-bowl” policy ought to be eliminated. Since such a policy is gradually phasing out from the SOHs, it is expected that the adverse effect of this policy will be diminished in later years. Two general managers reported that their employment, promotion and evaluation decisions were influenced by the government compared to other non-SOH in Hangzhou. One of them said: “The authority of general managers at SOHs is limited when making major decisions on different aspects such as purchasing and recruitment. The decisions are determined based on group consensus.” Therefore, the management of SOHs should be given complete control over hiring and wage decisions based on staff qualifications

and performance.

A participant noted: “We have regular staff meetings and social interaction activities organized by the communist party and labor union in the hotel. They aim to uplift employees’ morale and align their spiritual thinking with the communist party.” Some participants appreciate abundant training and internal promotion opportunities in SOHs. Despite such efforts, the lack of drive for excellence among the staff signals the need to tackle the problem with another approach. It is suggested that incentives and competitions should be introduced to SOHs hotels to motivate staff to succeed in their jobs. In a 2005 study of Chinese hotels’ staffs conducted by the China Tourist Hotels Association (CTHA), it was found that Chinese hotel employees are most motivated by money, followed by career development opportunities, public recognition, incentive travel, and others. Since such a study was directed at employees in all hotel sectors, it may not reflect the actual picture of SOHs due to its unique compensation system. A similar study should be conducted in SOHs to understand the factors influencing job motivation.

Market competition

Ten participants mentioned that the current operation mode of SOHs is undesirable for competing with other hotels in the market. Although SOHs are the largest group among all types of hotel companies, their competitive power is limited since they are often operated individually rather than as an aggregated entity. Most SOHs are independent from each other and are in small scales in comparison with international hotel chains. One of the General Managers suggested that changing SOHs from regional management to chain operations would not only avoid direct competition among SOHs, but also elevate the competitive power of SOHs in the market.

Since SOHs in China were established earlier than other hotels, they were the first to choose

their location for hotel construction. Therefore, majority of them possess the best locations in a city. When asking the core competitive advantage of the SOHs, most participants (11) mentioned the premium geographical location of the hotel as their major competitive resources. One participant noted: “We are located at the West Lake, which is the most famous tourist attraction in Hangzhou. Due to our desired location, pleasant environment, high standard of hospitality service and abundant experience in receiving government officials, we are often appointed by the government as a designated hotel for receiving official guests.” Table 1 shows the geographic locations of the five SOHs used in this study. All of them are either in the city center or near popular tourist attractions. Therefore, in their advertisement of SOHs to the leisure travelers, the hotels may highlight such an advantage since location is often regarded as a top criterion when travelers choose a hotel to stay.

Another advantage that SOHs may make use of in increasing their profitability is their rich history in accommodating important political leaders. As Mak (2008) discussed, many SOHs were originally “reception sites” for Chinese government officials and later for international government officials. A “celebrity effect” may be created by advertising this history. For example, Hangzhou Da Hua hotel advertises its history of hosting government meetings and the visits of Chairman Mao Zedong and Prime Minister Zhou Enlai to the hotel on its website (Hangzhou Da Hua hotel, 2011).

Management issues

All participants agreed that international hotel brands have superior management systems and are more experienced than SOHs. Although some widely-regarded management tactics are being applied in the SOHs, their effectiveness is limited due to the rigidity of implementation,

nepotism, and employees' lack of enthusiasm. Although some SOHs have adjusted their management system in response to market needs, these efforts were not fruitful due to certain obstacles faced by the enterprises. For instance, the hotels need to hire many short-term staff to serve customers since many SOH employees are either relatively old or unwilling to comply with the hotel's operational standards. This situation created both management and financial difficulties for SOHs and reduced their competitive power in the market. The root problem of such management difficulty is the inability of SOHs to separate management from ownership (Tang et al., 2006; Pine, 2002). To efficiently manage SOHs, managers should be bestowed with more power in the decision-making and implementation process. In other words, the SOHs may remain state-owned, but their operation and management should not differ significantly from that of privately owned hotels.

Pine (2002) and Lin et al. (1999) point out that because many SOEs/SOHs have certain social objectives such as hosting governmental meetings, invited leaders of other countries, and providing hospitality service to government officials, the government has much incentive to contribute capital to these businesses. But such contributions are incompatible with the market principle. These SOEs/SOHs would not survive with a sudden withdrawal of the state subsidies and protection. The Chinese government would not allow for mass privatization that has occurred in Eastern Europe. Also, the benefits of privatization in these countries have been relatively small (Aivazian et al., 2005). Lin et al. (1998, 1999) suggest that the government should first remove the social objectives of the SOEs/SOHs. When SOEs/SOHs are reporting losses, it is difficult to distinguish whether such losses are caused by bad management decision or because the firms have to fulfill such social objectives. Managers are more likely to attribute losses to the burden placed on them by government policy. Removing the burden of adhering to

government social objectives would mean profit could become a more accurate indicator of managers' performance.

CONCLUSIONS

Using 15 semi-structured in-depth interviews with Hangzhou SOH managers and employees, this paper identifies the problems associated with the SOHs in China and discusses how these problems can be resolved to improve SOH management and operation. Various issues with SOHs have been identified including problems with hotel ownership, human resources issues, market competition, and management difficulties. According to our study, hotel ownership problems such as the unclear division of ownership and management, intervention from government officials, and the valuing of social objectives above private objectives all contribute to the ineffective operation of SOHs. Additional problems include lack of incentives for employees; an inability to effectively compete with international hotel chains; and management issues such as lack of experience among managers. Many scholars have suggested various solutions to these problems including privatization (Shen & Chon, 2007; Mak, 2008; Lin et al., 1999; Cao, 2001), increased competition (Omran, 2004; Majumdar, 1998; Mak, 2008; Lin et al., 1998), franchising (Heung et al., 2008), and corporatization (Shen & Chon, 2007; Aivazian et al., 2005; Hu et al., 2006). Among these suggested solutions, privatization does not fit the political agenda of Chinese leaders (Lin et al., 1999). For competition to be an effective tool in creating incentives, SOH managers must be actually competing with other hotels. This is not currently possible because of the reliance on policy loans or government subsidies. Moreover, there is not much research on the effectiveness of franchising and corporatization of SOHs. Therefore, the question for the SOHs to address should be on how to enhance performance without selling the major government assets.

Although this study focused only on Hangzhou and has limited sample size, it identified several directions in which the SOHs may have the potential to outperform other hotels. First, because of the early development of the SOHs, Hangzhou SOHs are favorably located either at city centers or close to tourist attractions. Since hotel location is a main consideration for customers, this is a huge advantage for SOHs over other hotels. Second, since one of the major social obligations of SOHs are to provide accommodations to government official, many well-known Chinese or foreign government officials have stayed in these SOHs. These histories can create a “celebrity effect”. Rooms in which these government officials stayed can be either used as an exhibition space or designated as premium accommodations. Third, because of the “iron-rice bowl” policy or the desirability for employment in government institutions or some other reasons (a potential area of future research), SOHs have a relatively stable workforce. As high labor turnover rate is prevalent in the hospitality industry, this unstable labor force actually reduces the incentive for hotels to provide training to the workers (Cheng & Brown, 1998; Gonzaga & Maloney, 2003). The stable labor force provides greater incentives to train workers resulting in higher quality and more consistent levels of service. While this study shed some light on the status of SOHs in China, particularly in Hangzhou, further research needs to investigate these same issues in other Chinese cities. Though many problems have been identified in the current as well as past studies, the SOHs in China have the potential to become profitable businesses.

LIMITATIONS

One of the major limitations of this study is the small sample size. Given the resources available, we were only able to conduct 15 semi-structured interviews with 5 state-owned hotels Hangzhou. The sample size was pre-determined based on the willingness of participants prior to

obtaining data. Theoretically, the number of interviews should be determined by data saturation point when further interviews do not contribute any additional information to the investigated topic. Although 15 samples are commonly considered to be reasonable for a qualitative study, future studies should pursue to include more samples based on the aforementioned strategy. Additionally, only hotel managers and employees were included in the study due to the availability of sample. An alternative approach would be to conduct interviews with all stakeholders of SOHs including policy makers, hotel managements, operators, employees, competitors, and customers to portrait a holistic picture of SOHs from different perspectives. Lastly, the level of criticalness of each challenge was not sought in this study. To understand which challenge is the most compelling one, a ranking exercise may be pursued in future research with the use of a panel of experts.

REFERENCES

- Alchian, A. A., & Demsetz, H. (1972). Production, information costs, and economic organization. *The American Economic Review*, 62 (5), 777-795.
- Alchian, A. A., & Demsetz, H. (1973). The property right paradigm. *The Journal of Economic History*, 33 (1), 16-27.
- Benson, J., & Zhu, Y. (1999). Markets, firms and workers in Chinese state-owned enterprises. *Human Resources Management Journal*, 9 (4), 58-74.
- Boardman, A. E., & Vining, A. R. (1989). Ownership and performance in competitive environments: A comparison of the performance of private, mixed, and state-owned enterprises. *Journal of Law & Economics*, 32, 1-33.
- Cai, L. A. (2004). State-owned economy and budget hotels in China – from commodity to brand. *Asia Pacific Journal of Tourism Research*. 9 (1), 29-42.
- Cai, L. A., Zhang, L. L., Pearson, T. E., and Bai, X. C. (2000). Challenges for China's state-run hotels: A marketing perspective. *Journal of Hospitality & Leisure Marketing*, 7(1), 29-46.
- Cao, L. (2001). Chinese privatization: between plan and market. *Law and Contemporary Problems*, 63 (4), 13-16.

Cauley, J., & Sandler, T. (1992). Agency theory and the Chinese enterprise under reform. *China Economic Review*, 3 (1), 39-56.

Cauley, J., Cornes, R., & Sandler, T. (1999) Stakeholder incentives and reforms in China's state-owned enterprises: A common-property theory. *China Economic Review*. 10, 191-206.

CIConsulting (2010). *2010-2015 Hangzhou Hotel Investment Analysis and Forecasting*. Retrieved on May 25, 2012, from the World Wide Web: <http://www.dragonraja.com.cn/20092/12009211571.html>

Cheng, A., & Brown, A. (1998). HRM strategies and labor turnover in the hotel industry: A comparative study of Australia and Singapore. *The International Journal of Human Resource Management*, 9 (1), 136-154.

China National Tourism Administration (CNTA), 1981–2005. *The Yearbook of China Tourism Statistics*. China Tourism Press, Beijing.

China National Tourism Administration (CNTA) (2010). *China Hotel Industry Progress Report 2009*. Beijing: China Tourism Publishing House.

China National Tourism Administration (CNTA) (2002). *China Hotel Industry Progress Report 2001*. Beijing: China Tourism Publishing House.

Choe, C., & Yin X. (2000). Contract management responsibility system and profit incentives in China's state-owned enterprises. *China Economic Review*, 11, 98-112.

Comstock, A., Kish, R. J., & Vasconcellos, G. M. (2003). The post-privatization financial performance of former state-owned enterprises. *Journal of International Financial Market, Institutions & Money*, 13, 19-37.

Cull, R., & Xu, L.C. (2003). Who gets credit? The behavior of bureaucrats and state banks in allocating credit to Chinese state-owned enterprises. *Journal of Development Economics*, 71, 533-559.

Gonzaga, G., & Maloney, W. F. (2003). Labor turnover and labor legislation in Brazil. *Economia*, 4 (1), 165-214.

Groves, T., Hong, Y., McMillian, J., & Naughton, B. (1994). Autonomy and incentives in Chinese state enterprises. *The Quarterly Journal of Economics*, 109 (1), 183-209.

Hangzhou Da Hua Hotel (2011). *Hotel*. Retrieved June 01, 2011 from the World Wide Web: <http://hangzhoudahuahotel.chinahotel.com.cn/index.php?lang=en>.

Hassard, J., Morris, J., Sheehan, J., & Yuxin, X. (2010) China's state-owned enterprises: economic reform and organizational restructuring. *Journal of Organizational Change Management*, 23 (5), 500-516.

- Heung, V. C. S., Zhang, H., & Jiang, C. (2008) International franchising: opportunities for China's state-owned hotels? *International Journal of Hospitality Management*, 27, 368-380.
- Hu, Y., Opper, S., & Wong, S. M. L. (2006). Political economy of labor retrenchment: Evidence based on China's state-owned enterprises. *China Economic Review*, 17, 281-299.
- Huang, J. and Cai, L. A. (2010). Online Image of Multinational Hotel Brands on Different Language Platforms. *Journal of China Tourism Research* 6 (3), 279-295.
- Huang, X., Li, P., & Lotspeich, R. (2010) Economic growth and multi-tasking by state-owned enterprises: an analytic framework and empirical study based on Chinese provincial data. *Economic System*, 34, 160-177.
- Hung, K. (2012). Chinese hotels in the eyes of Chinese hoteliers: The most critical issues. *Asia Pacific Journal of Tourism Research*, DOI:10.1080/10941665.2012.658415
- Jalan, B., (1991). *India's economic crisis: The way ahead*, Oxford University Press, New Delhi.
- Jefferson, G. H., & Rawski, T. G. (1994) Enterprise Reform in Chinese Industry. *Journal of Economic Perspectives* 8 (2), 47-70.
- Kornai, J., (1990). *Vision and reality: Market and state*, Routledge, New York.
- Lau, L. J., Qian, Y., & Roland, G. (2000). Reform without losers: an interpretation of China's dual-track approach to transition. *Journal of Political Economy*, 108 (1), 120-143.
- Lee, K. (1990). The Chinese model of the socialist enterprise: an assessment of its organization and performance. *Journal of Comparative Economics*, 14, 384-400.
- Li, W. (1999). A tale of two reforms. *The RAND Journal of Economics*, 30 (1), 120-136.
- Lin, J. Y., Cai, F., & Li, Z. (1998) Competition, policy burdens, and state-owned enterprise reform. *The American Economic Review*. 88 (2), 422-427.
- Lin, J. Y., Cai, F., & Li, Z. (1999). Fair competition and China's state-owned enterprise reform. *MOCT-MOST*, 9, 61-74.
- Mak, B. (2008). The future of the State-owned hotels in China: Stay or go? *International Journal of Hospitality Management*, 27, 355-267.
- Miao, L., Adler, H., and Xu, X. (2010). A Stakeholder Approach to Expatriate Management: Perceptions of Hotel Expatriate Managers in China. *International Journal of Hospitality Management*, 30 (3), 530-541.
- National Bureau of Statistic (2011). *China GDP Growth Rate*. Retrieved May 25, 2011 from the

World Wide Web: <http://www.tradingeconomics.com/china/gdp-growth>.

Omran, M. (2004). The performance of state-owned enterprises and newly privatized firms: does privatization really matter? *World Development*, 32 (6), 1019-1041.

Patton, M. Q. (2002). *Qualitative Research and Evaluation Methods* (3rd ed.). Thousand Oaks, CA: Sage Publications, Inc.

Perkins, F. (1999). The costs of China's state-owned enterprises. *MOCT-MOST*, 9, 17-33.

Pine, R. (2002). China's hotel industry: serving a massive market. *Cornell Hotel and Restaurant Administration Quarterly*, 43, 61-70.

Pine, R., & Qi, P. (2004). Barriers to hotel chains development in China. *International Journal of Contemporary Hospitality Management*, 16 (1), 37-44.

Pine, R., Zhang, H., & Qi, P., (2000). The challenges and opportunities of franchising in China's hotel industry. *International Journal of Contemporary Hospitality Management*, 12 (5), 300-307.

Putterman, L., & Dong, X.Y. (2000). China's state-owned enterprises: their role, job creation, and efficiency in long-term perspective. *Modern China*, 26, 403-447.

Raiser, M. (1997). How are China's state-owned enterprises doing in the 1990s? Evidence from three interior provinces. *China Economic Review*, 8 (2), 197-216

Roland, G. (1999). Transition and the output fall. *Economics of Transition*, 7 (1), 1-28.

Shen, H., & Chon, K. (2007) Ownership reform of state-owned hotels in China: logic, problems and solutions. *Proceedings of the First Hospitality and Leisure: Business Advances and Applied Research Conference*, 264-268.

Shirley, M. M. (1999). Bureaucrats in business: the roles of privatization versus corporatization in state-owned enterprise. *World Development*, 27 (1), 115-136.

Siqueria, K., Sandler, T., & Cauley, J. (2009) Common agency and state-owned enterprise reform. *China Economic Review*, 20, 208-217.

Tang, F., Xi, Y., Chen, G., & Wang, R. (2006). Ownership, corporate governance, and management in the state-owned hotels in the People's Republic of China. *Cornell Hotel and Restaurant Administration Quarterly*, 47, 182-191.

Wang, X., Xu, L. C., & Zhu, T. (2004) State-owned enterprises going public: The case of China. *Economics of Transition*, 12 (3), 467-487.

Watanabe, M. (2002). Holding company risk in China: a final step of state-owned enterprises reform and an emerging problem of corporate governance. *China Economic Review*, 13, 373-381.

World Bank (1996). From plan to market. *World Development Report 1996*. Washington, D.C.: World Bank.

Yin, X. (2001). A dynamic analysis of overstaff in China's state-owned enterprises. *Journal of Development Economics*, 66, 87-99.

Zhang, J., Cai, L. A., and Kavanaugh, R. R. (2008). Dimensions in Building Brand Experience for Economy Hotels—A Case of Emerging Market. *Journal of China Tourism Research*, 4 (1), 61-77.

TABLE 1: Descriptive Information of the Participating Hotels

<i>Name of the Hotels</i>	<i>Location in Hangzhou</i>	<i>Supervision Division</i>	<i>Star category</i>
Hangzhou Da Hua Hotel	Hangzhou West Lake	Government Office Administration of the Province	4
Grand Metropark Hotel	Hangzhou city center	State-owned Assets Supervision and Administration Commission of the State Council	5
Hangzhou Huajia Shan Resort	Hangzhou West Lake	China's Foreign Affairs Offices under State Council	Unrated, based on 5 stars construction
ZTG Resort Thousand-Island Lake Hangzhou	Hangzhou Qiandaohu sightseeing attractions	China Travel Services Zhejiang	Unrated, based on 5 stars construction
Best Services Hotel	Hangzhou city center	Zhejiang Supply and Marketing Cooperative	3

TABLE 2
DEMOGRAPHICS OF PARTICIPANTS

Participants in the Hotel	Position	Department	Age	Gender	Education	Working Years	Years of Service
#1	Assistant General Manager	N/A	55	Male	Bachelor degree	35	25
#2	General Manager	N/A	45	Male	Bachelor degree	22	12
#3	General Manager	N/A	54	Male	Bachelor degree	30	15
#4	General Manager	N/A	61	Male	Bachelor degree	40	15
#5	Assistant General Manager	N/A	44	Female	Bachelor degree	23	10
#6	Assistant Manger	Executive Office	38	Female	Bachelor degree	19	6
#7	Manager	Sales & Marketing	32	Female	Bachelor degree	13	13
#8	Manager	Sales & Marketing	28	Male	Bachelor degree	7	6
#9	Manager	Engineering	52	Male	Higher diploma	30	20
#10	Receptionist	Front Office	29	Female	Higher diploma	8	8
#11	Bell boy	Front Office	22	Male	High school	2	1
#12	Clerk	Security	27	Male	Bachelor degree	4	2
#13	Clerk	Food & Beverage	26	Female	Bachelor degree	3	2
#14	Clerk	Human Resources	24	Female	Bachelor degree	1	1
#15	Clerk	Executive Office	23	Female	Bachelor degree	1	1

