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Diamonds: A Hotel's Best Friend?

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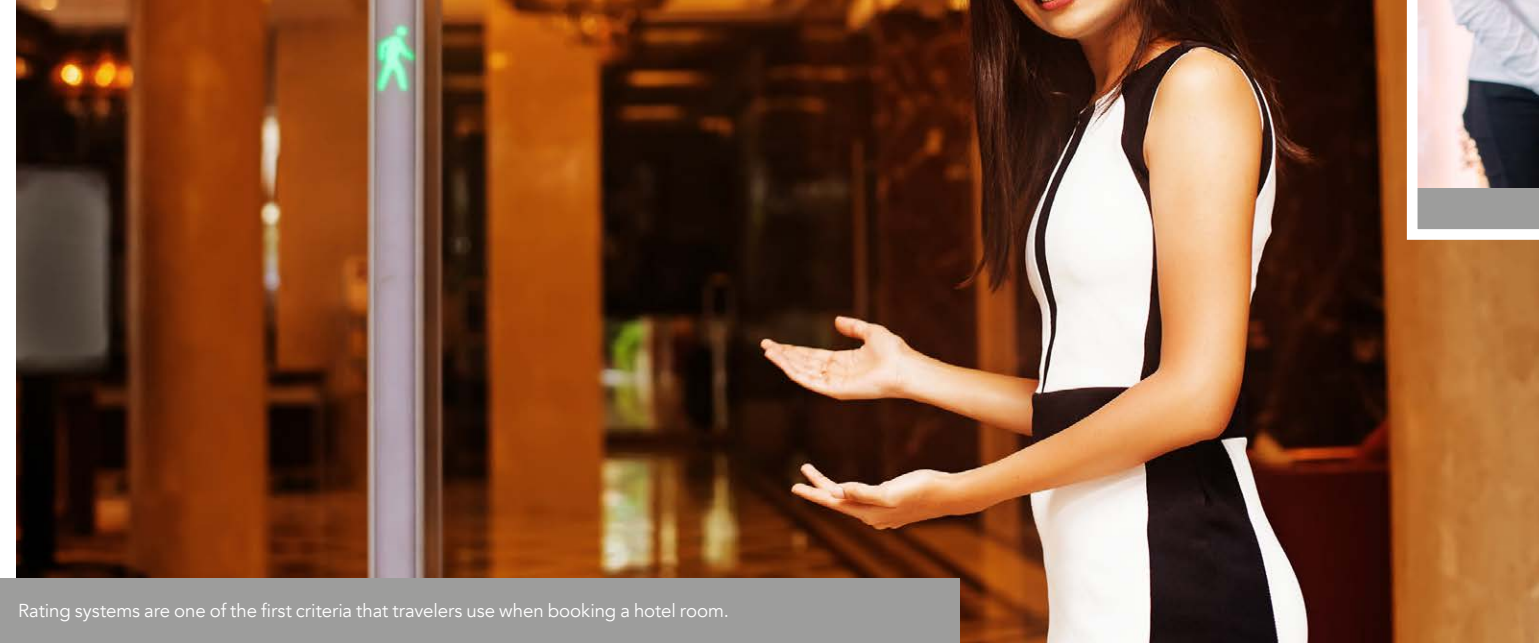
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DIAMONDS:

A hotel's best friend?



Rating systems are one of the first criteria that travelers use when booking a hotel room.



The criteria used by the Diamond rating scheme are famously exacting and specific.

HOTELS ARE EXPERIENCING GROWING THREATS FROM ALTERNATIVE FORMS OF ACCOMMODATION SUCH AS AIRBNB, AND THUS, THE SEARCH FOR POTENTIAL ANTECEDENTS OF HOTEL PERFORMANCE HAS BECOME EVEN MORE CRUCIAL.

Independent rating systems are common in many industries but possibly not as important as they are in the hospitality industry, covering both restaurants (with their world renowned Michelin stars) and hotels. In the US, the leading rating organization is the AAA (American Automobile Association) with their Diamond rating scheme. Many studies have looked at the impact of the Diamond rating on the performance of a particular hotel, but this study by Rosen College of Hospitality Management researchers Dr. Michael Nalley, Dr. Jeong-Yeol Park and Dr. Diego Bufquin, takes a different perspective, looking at how a change in the Diamond rating affects hotel performance.

Since 1902, the AAA (American Automobile Association) has been covertly visiting hotels across the United States and assessing them against a range of criteria. Those that meet these strict standards are awarded an appropriate Diamond rating on a 1-5 scale. Just as crucially, a hotel with a Diamond rating will risk losing some or all of it if, on the annual inspection, they are considered by the AAA's professionally trained inspectors to have let standards fall.

There have been many studies into the impact of rating systems on hotel performance which support the correlation between respected rating and performance. However, in this current study, Dr. Michael Nalley, Dr. Jeong-

Yeol Park and Dr. Diego Bufquin from Rosen College of Hospitality Management, have chosen to apply their research expertise to the less obvious question of how the simple fact of a change in rating, whether positive or negative, might affect the key performance indicators (KPI) common in this industry.

In particular, they ask whether that change is maintained over the longer term and how this new understanding can impact hotel management strategy and investment decision making.

HOTELS TODAY

The study is particularly relevant in the current environment as the industry is facing the threat of competition from internet-enabled



newcomers such as Airbnb. Similarly, with the advent of social media, both positive and negative customer experiences can be widely shared across the market in a way that wasn't previously possible. Unfortunately, as many businesses have found to their cost, customers are more likely to post feedback on a bad experience than they are on a positive one.

Previous studies have generally identified that rating systems are one of the first criteria that travelers use when booking a hotel room. In fact, the four most important variables on overall per-room performance are room quality, positive regional review, hotel regional reputation and regional room star rating.

Recognition by a well-respected independent body such as the AAA becomes more significant in these circumstances, providing an impartial recommendation and reference for the guest lodging decision.

THE DIAMOND RATING SCHEME

The criteria used by the Diamond rating scheme are famously exacting and specific. Take room service, for example: A five Diamond property is required to offer

room service 24/7, while a four Diamond property only has to offer room service for breakfast, lunch and dinner. Or consider the bathroom specifications: A shower base in a three Diamond property must have a base of not less than nine square feet, whereas the four Diamond property shower base must be no less than 12 square feet.

With such a clearly defined set of criteria, customers have a good idea of what they will find and experience when they book a hotel room. They can also be confident that the properties will be inspected at least annually, so a Diamond rating is always current.

HOTEL PERFORMANCE

A Diamond rating, therefore, has value for the customers' purchase decision and, consequently, the number of Diamonds the hotel is awarded is likely to be linked to the hotel's KPIs.

The KPIs that are typically used to assess hotel performance are:

- Occupancy – percentage of available rooms occupied
- ADR – average daily rate
- RevPAR – revenue per available room

Each of these tells us something different about the hotel performance. For any hotel, the number of rooms it has available for occupancy is fixed (at least in the short to medium term): A hotel with more rooms available for occupancy has less rooms booked and so is likely to be under performing. Average daily rate puts a marker on the price customers are willing to pay and RevPAR captures the value per room and assists in measuring the overall success of the hotel.

Each of these KPIs has a corresponding "index" which allows performance in this area to be compared to the hotel's main competitors to determine if the hotel is obtaining its "fair share" of the market. So KPIs and KPI indexes are both used to assess hotel performance.

ALL CHANGE

But what about a change of rating? How can the impact of that change be assessed? The researchers from Rosen College were keen to find out.

Firstly, AAA provided its own data detailing properties that had Diamond rating changes

THE AAA DESCRIPTION OF THE FIVE LEVELS

- ◆ Budget-oriented, offering basic comfort and hospitality
- ◆◆ Affordable, with modestly enhanced facilities, décor and amenities
- ◆◆◆ Distinguished, multifaceted with enhanced physical attributes, amenities and guest comforts
- ◆◆◆◆ Refined, stylish with upscale physical attributes, extensive amenities and a high degree of hospitality, service and attention to detail
- ◆◆◆◆◆ Ultimate luxury, sophistication and comfort with extraordinary physical attributes, meticulous personalized service, extensive amenities and impeccable standards of excellence

within a recent 10-year period (2006-2016). Nalley, Park and Bufquin were also able to access indexed performance data from 5,073 properties from Smith Travel Research.

After rejecting properties with missing KPI data, the researchers ended up with 1,824 properties that had experienced a change in rating; 499 of these had gained a diamond rating and 1,325 had lost a diamond rating. For each of these properties, they had both KPI data and KPI indexes so they could assess hotel performance and compare it to competitors.

The researchers hypothesized that, one year after the rating change, hotels with an increase in Diamond rating would have significantly higher KPIs and KPI indexes compared to hotels which lost a Diamond.

On examining the data, Nalley, Park and Bufquin found it supported their ideas: The hotels which had gained a Diamond had higher KPIs than those which had lost one. When the team looked at the KPI indexes (hotel performance relative to competitors) this was also the case with one exception: In the occupancy rate index there was no significant difference between the performance of hotels which had gained a Diamond versus those which had lost one. In the short term, they concluded, an increased rating boosted overall room rate performance.

However, they reasoned that the increased Diamond rating and resultant improved KPIs would be related to improvements in service, amenities and facilities. Would the investment needed for improvements continue over time?

In the long term, they suggested, improvements in KPIs and KPI indexes related to Diamond ratings would plateau out. In effect, there would be a significant improvement early on but, while the KPIs and KPI indexes would



The Diamond rating criteria even cover the size of the shower base.

continue to improve, the impact of this would decrease over time.

Further detailed analysis of the data supported this hypothesis. Those hotels which had increased their Diamond rating had higher KPIs and KPI indexes over the long term compared to those hotels which had lost a Diamond rating. As expected, however, the improvements tended to drop off around five years after the increase in rating.

PUSHING FORWARD

Perhaps we should not be surprised that properties that gained Diamond ratings experienced improved KPI outcomes over properties that lost ratings – it feels intuitive. But this research from Nalley, Park and Bufquin,

particularly the emphasis on the short lifespan of the benefits, has important implications for the hotel industry.

It is reasonable to suggest that the improved individual and market performances of hotels with an increased rating could be driven by the accompanying advantages and benefits perceived by the guests. An increase in the Diamond rating suggests an increase in the quality, sophistication, guest comfort, accommodation, style, service, hospitality, physical attributes, amenities and attention to detail that the guest desires and is willing to pay for. The Diamond rating is, therefore, an important factor in hotel performance.

This suggests that hotel brands and individual properties may need to reconsider their investment strategies. One-off investment purely to achieve an increased rating runs the risk of losing that rating if customer experience standards are found to be fading. Hotel management could instead apply a more informed and dynamic strategy of continuous investment to ensure the rating is maintained. It seems, after all, that Diamonds (at least from the AAA) are a hotel's best friend!

IT IS REASONABLE TO SUGGEST THAT THE IMPROVED INDIVIDUAL AND MARKET PERFORMANCES OF HOTELS COULD BE DRIVEN BY THE ADVANTAGES AND BENEFITS PERCEIVED BY THE GUESTS IN THE HOTEL DIAMOND RATING SCALE.

RESEARCHERS IN FOCUS

RESEARCH OBJECTIVES

Dr. Nalley, Dr. Park and Dr. Bufquin have examined the effect a change in Diamond rating has on hotel performance.

REFERENCES

Key Paper

Nalley, M.E., Park, J.-Y., Bufquin, D. (2018). An investigation of AAA diamond rating changes on hotel performance. *International Journal of Hospitality Management*. Available at: <https://doi.org/10.1016/j.ijhm.2018.07.016>

Background Info

American Automobile Association, 2017. AAA Diamond Rating System Fact Sheet. Retrieved from: <http://newsroom.aaa.com/Diamond-ratings/>.

PERSONAL RESPONSE

Why do you think customers are so swayed by rating systems?

Rating systems provide the customer with an authentic measure to gauge the product that they are going to buy, to ensure that it aligns with their specific wants, needs and desires. Whether this is provided by an industry organization or online by user generated content (UGC).

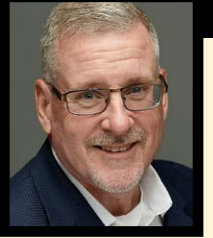
And what makes a good one?

Consistency in accurately representing the product for the customer experience and standards that represent the guest preferences and key concerns.



According to the researchers, investment should be ongoing to ensure standards are upheld.

Dr. Michael Nalley



Dr. Nalley is a hospitality executive with over 30 years of experience in hospitality education, training and operations management. He is a customer service and training expert experienced in global brand program development, implementation and analysis. He has worked with six hotel brands in operational and corporate level positions.

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Dr. Park has conducted multiple research studies that have examined potential travelers' purchase behavior at online travel agencies, restaurant customers' behavior, and demand analysis for hospitality industries. Currently, he teaches Hospitality Industry Financial Accounting and Research Methods in Hospitality and Tourism.

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Dr. Diego Bufquin



Dr. Bufquin has a multicultural background that has led him to live and work in a variety of countries. In the hospitality industry, Dr. Bufquin has had the opportunity to work at several hotels and restaurants. His research mostly focuses on the areas of consumer and organizational behavior.

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