TRANSFORMING WYNDHAM

La Quinta deal moves quality needle; revived rooms growth Ballotti’s next step.
WHERE INVESTORS, INNOVATION, AND THE HOTEL INDUSTRY CONNECT
Geoff Ballotti is called a stand up, accessible leader. Good thing, as he has to convince a franchise community to step up its game to help bring the world’s biggest franchisor upmarket. Its recent acquisition of La Quinta marks a good move in that direction.

With the democratization of the Internet, owners can more easily choose to brand or go it on their own. How are the options and sentiments evolving?

What will be investor sentiment at ALIS 2019? Mandarin Oriental’s James Riley on the record Thorny wage issues in U.S.

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When the hotel industry gathers in January for ALIS, how will hotel investors view the road ahead? For the past several years as we started the New Year, investor sentiment has been positive but tinged with some caution. The Great Recession ended in June 2009, and typical economic growth cycles averaged about six years, according to statistics from the U.S. National Bureau of Economic Research.

For any hotel industry veteran, the positive performance has seemingly lasted too long, but on the other hand nothing has pointed to its end. This positive yet cautious mood has been articulated by the ALIS themes: “Where’s the Peak?” in 2016, “Please Stand By…” in 2017, and “Dealing with the New Normal” in 2018.

As the 2019 ALIS conference developed, overall investor sentiment has sounded similar to recent years. There is nothing to suggest the end is coming to this up-cycle, but history suggests that sooner or later things will turn.

Will it be today, tomorrow or beyond? To foresee what may be on the horizon, BHN connected with a handful of leading hotel investment executives. We interviewed them about the coming year and if they expect to do more or fewer deals, and whether it will be more single assets or portfolio deals. To round out the story, we asked about their preference of gateway versus non-gateway markets.

DEAL ACTIVITY
Setting the stage for what looks to be a decent year ahead, Gilda Perez-Alvarado of JLL Hotels & Hospitality Group says liquidity in 2019 is expected to remain strong, underpinned by activity across gateway markets, the resort sector and portfolios of select-service assets. “General sentiment in the industry is optimistic as we head to year-end 2018 due to continual strength in fundamentals, occupancy reaching an all-time high and global tourism trends that support increased travel to the U.S.,” she says.

Also expressing positive views about 2019, Nala Holmes of Pyramid Hotel Group, Boston, is optimistic that more sellers will come to market to recycle capital, while deal volume will continue to be dependent on quality of product on the market.

“With the recent pullback in hotel REIT stocks, the ability to be acquisitive, at least in the near term, becomes more difficult.”

— Krissy Gathright
and owners wanting or needing to sell instead of refinance, which was more prevalent over the past 12 to 18 months. “Demand is still strong for hotel assets, so expect overall deal climate to remain competitive,” Holmes says.

Transaction volume has been steadily increasing, according to Krissy Gathright of Apple Hospitality REIT, Richmond, Virginia. “Barring any significant changes in current market dynamics, we anticipate that trend will continue, and the industry will see more transactions in 2019 as compared to 2018, and we see ourselves as likely participants,” she says.

Lynne Roberts of Aimbridge Hospitality believes hotel trading activity for 2019 will surpass 2018. She is “expecting favorable U.S. economic indicators to be sustained over the next 12 months: an abundance of debt/leverage, GDP growth coupled with low unemployment rates, and a steady, albeit slower, hotel RevPAR growth as additions to supply curtail.”

WHO WILL BE ACTIVE, AND WHY?
As the most active player, private equity is a net buyer, having acquired approximately US$10 billion worth of hotels in the U.S. as of YTD Q3 2018, while disposing of a little less than US$7 billion, according to Perez-Alvarado, who expects this trend to continue in 2019 with liquidity provided from domestic and foreign investors.

Through Q3 2018, REITs have been net sellers, disposing of US$845,000 more of assets than what they have acquired (US$2 billion). Nonetheless, in 2019 Perez-Alvarado anticipates REITs will be net buyers.

“The buyer group’s positive stock performance, including the fact that hotel REITs have outperformed all other REIT product types and the S&P index, provides a good backdrop for increased activity in 2019,” she says. “Some of the larger owners of select-service hotels are expected to dispose of portfolios acquired earlier this cycle, which is expected to lead to several billion dollars’ worth of transactions in the select-service sector.”

As the REIT contributor here, Gathright adds, “With the recent pullback in hotel REIT stocks, the ability to be acquisitive, at least in the near term, becomes more difficult. However, as Gilda (Perez-Alvarado) noted, there is a lot of capacity to buy across the hotel REIT sector… Fueled in part by continued strength in the debt markets, we have also seen an uptick in interest for select-service assets, which could help to facilitate selective dispositions in 2019.”

Roberts expects M&A activity, including portfolio trades, will dominate next year. “International in-bound firms and family offices based in Asia and Europe are expected to expand in pursuit of tax-advantaged investing into U.S. hotel real estate,” she says, adding that the risk-return on the hotel front of investing is attracting new investors into the space.

GATEWAY OR NON-GATEWAY?
When it comes to geographic focus, Gathright says Apple Hospitality REIT will continue to seek acquisition opportunities in urban and high-end suburban markets that present attractive upside potential and provide a wide variety of demand generators and guest amenities.

Mary Beth Cutshall of HVMG and Amara Capital adds, “Historically, we’ve acquired assets in both gateway and non-gateway markets. We’re opportunistic buyers and have also had success in secondary markets.”

Touching on the benefits of diversification, Pyramid’s Holmes says while they operate in gateways, representation in secondary Midwest and Southeast markets remain part of the strategy. “With the existing competitive landscape of more buyers than sellers, we’ve seen capital partners spread a wider net, expanding efforts from top-tier gateway cities to the top 25-50 travel markets,” she says.

Contributed by Burba Hotel Network

“General sentiment in the industry is optimistic as we head to year-end 2018 due to continual strength in fundamentals, occupancy reaching an all-time high and global tourism trends that support increased travel to the U.S.” — Gilda Perez-Alvarado
James Riley, group chief executive of Mandarin Oriental Hotel Group since April 2016, is not one to mince words. In fact, he calls himself somewhat cynical when it comes to things like industry giant’s overzealous pipeline boasts. But the former senior financial executive with Mandarin’s Hong Kong-based parent company Jardine Matheson Group has also developed quite a passion for the hotel business and enormous respect for the dedication of his colleagues. “If anything, I’ve grown even more in love with what Mandarin and, in particular, my Mandarin colleagues do and are able to deliver, which I find very special,” he says.

That said, Mandarin and Riley have a lot of work ahead and more to prove as the company has not opened a new hotel since September 2015 (it reflagged a Caribbean property as Mandarin Oriental, Canouan in July 2018) and is still recovering from the unfortunate fire at its London property in early June of this year, days before it was set to reopen after a top-to-bottom, 18-month refurbishment. MOHG’s intention, Riley says, is to realistically (no aggrandizing here) grow the brand over the next five years at a preferred average pace of three to four openings a year, predominantly via management contracts. Mandarin has 31 hotels open – seven with residences – in 21 countries and a current pipeline, give or take, of 19 hotels with 12 residences. Its about to open three hotels (Dubai, Doha, Beijing) in early 2019 and has a rush openings set for 2021.

Riley would love to increase the portfolio in the United States, especially California, and while he says they have looked closely at the available Belmond portfolio, quite frankly there is no serious intent to get more aggressive with an acquisition or to create a second brand.

In the meantime, Riley says 2018 has been a relatively strong performance year due to improved trading in Hong Kong and he is encouraged by, among other things, the fact that the London hotel will come back online next year.

TAKE ON LUXURY
Riley, who doesn’t wear suits and sports an atypical Mandarin-style beard, has much to say about the evolution of luxury hotelkeeping. “Today, you will find if you go into Mandarins, there are people with tattoos and ear piercings beginning to emerge in those areas where one wants a slightly more edgy, slightly more character-full delivery of service,” he says in reference to how the company is far from tone deaf about how lifestyle is impacting the luxury hotel business model.

“My approach and mindset is to set a tone, use words and allow people to interpret and take a judgment, because again, whereas things are relaxed and chill in certain locations, it’s probably still right to say that at the Mandarin Oriental Hyde Park in London, formality and elegance remains the order of the day, and a greater degree of formality is what guests would like, and expect there,” he adds.

Riley thinks that luxury is increasingly leisure oriented and the days of luxury hotels for non-senior corporate
While James Riley says Mandarin has looked closely at the Belmond portfolio, there is no serious intent to get more aggressive with an acquisition or to create a second brand.

Mandarin’s most recent move: reflagging a Caribbean property as Mandarin Oriental, Canouan in July 2018.

executive are long gone. “Corporate executives will stay in Conrads and Marriotts and Hiltons, which are really for corporate road warriors who want their points. The corporate leaders will increasingly be asking of themselves, ‘Why are we putting our executives up in accommodation that’s vastly smarter than they live in at home?’”

Therefore, Riley believes luxury hotels need to have a significant leisure component as well as a group component, where one’s delivering a special experience, rather than relying just on regular corporate travelers.

Because luxury’s becoming increasing leisure focused means that it will become increasingly relaxed, according to Riley, and that means that luxury hotels do need to adjust their offering. “It means that the historic formality of what I would call Alpine or Mid-European hotel schools needs to gradually change.

“It’s important to remember the courtesies and formalities, which is something that I think one forgets at one’s peril, but at the same time, what guests are really looking for is an empathetic experience – one where they really feel they engage with colleagues and appreciate that,” he says.

Looking ahead, Riley points to one particular challenge of how to initiate a differentiated technology platform that best enables interaction with guests and among colleagues. “Technology is an enabler, but also a restrainer,” he says. “Being able to implement technology effectively and to make sure that people can effectively communicate, talk to each other, interact, and enable guests to engage as they increasingly want to, in a multitude of ways that you create, is an important part of the experience.”

The reality, Riley believes, is to keep up with the expectations of guests and “not suddenly burst on the scene with some amazing new idea which will, generally speaking, be a bit of a gimmick rather than a real value creator.”

Spoken like a leader with a firm grasp on reality.

By Jeff Weinstein, editor in chief
Running a prosperous hotel is no easy task. The costs are innumerable, and delivering bottom-line profit for owners each month is a grind.

One of the most difficult of these expenses to manage is payroll — and maybe at no time in the U.S. has it been more onerous. According to the U.S. Department of Labor, unemployment held steady in October at 3.7% with employers adding 250,000 jobs. Conspicuously, hourly wages posted the strongest gain in nearly a decade, climbing 3.1% from a year ago. (Wages haven’t exceeded 3% year-over-year growth since April 2009.) The evidence is clear: The tight labor market is forcing employers to raise wages to attract and keep talent.

In no industry is this more evident than hospitality, where it can take hundreds of employees to operate a full-service hotel. Of that, about a quarter are room attendants. It’s high stakes on both sides — employees and owners — and the union strikes impacting Marriott hotels that began in October in San Francisco and spread elsewhere aimed a spotlight on wages and proved how dire a work stoppage can be on operational efficiency, not to mention the interruption of guest experience and service.

Yet the hospitality industry remains a shining star in America’s job market. It is one of the biggest drivers of employment in the U.S.: In the past 12 months, the hospitality sector has added 254,000 new jobs, ranking fifth of any industry and just behind manufacturing.

But low unemployment and wage growth are conspiring to create a huge war on talent at every level of the hotel industry. It’s being compounded by competition from other industries, namely retail, where big-box retailers like Walmart and Target have raised minimum wages and promised future increases.

While wage growth and low unemployment are propitious for the American worker, the tandem can be grievous for owners and operators of hotels focused on maintaining and driving healthy profit margins. This is exposed in recent data from HotStats, a global provider of profit-and-loss data benchmarking for the hospitality industry. First, the good: On a rolling 12-month basis for upper-scale full-service hotels in the U.S., all key top-line measures are up: occupancy up 0.6%; average daily rate up 2%; and revenue per available room up 2.8%.

Though top-line numbers remain strong on a national scale, albeit leveling off as the cycle matures, expenses continue to rise and needle hoteliers.

According to HotStats data, room expenses on a per-occupied-room basis are up more than 2% from January to September, 2018. In September alone, room expenses were up 4.7% over the same time last year to US$12.09. Room expenses include such items and services as linen, complimentary amenities, laundry and dry cleaning, operating supplies and other operating supplies.

Things are not much better on the payroll side. Rooms labor costs on a per-occupied-room basis were up 3.5% from January to September 2018, to US$37.66, and up 3.4% on a rolling 12-month basis to US$36.86.

In New York City, a union town, total payroll expenses are higher and growing, up 4.6% on a per-available-room basis this year to September. By comparison, San Francisco total payroll is up 2.4% in the same time period.

The data portend rocky times for the hotel industry into 2019. The combination of dwindling RevPAR growth and increasing wage pressure is detrimental to profit margins and an obstacle to EBITDA growth.

On average, hotels normally budget 3% expense growth per year, but in an environment of RevPAR and TRevPAR growth not matching or exceeding that, hoteliers could be in for a rude 2019. How well they handle expense control will prove how fulsome or slight their bottom lines become.

Contributed by David Eisen, director of hotel intelligence, HotStats
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DirectTV Hospitality
RE-POSITION for GROWTH

By Jeff Weinstein, editor in chief
Confidence is on the rise at Wyndham Hotels & Resorts — not just among the executive team, but with franchisees who feel pretty good about its direction. That includes an ongoing system cleanup to improve the reputation of some 20 economy and mid-market brands, and taking the company further upmarket with acquisitions such as its May close on the US$1.95 billion La Quinta brand.

That same month, the Parsippany, New Jersey-based company became the world’s biggest pure-play hotel company when it split from the timeshare business, now called Wyndham Destinations.

Moving forward franchisees, say the focus needs to shift to further enhancement of the loyalty program and improving technology platforms, which some say still suffer from some hiccups. At the same time, analysts say they want to see improvements in system growth, which for Q3 2018 saw a net gain of 3%, and they ponder when the next bolt-on acquisition may come for the company, which has more than 9,000 properties and over 798,000 rooms.

“I feel pretty good. I am more confident than before,” says Janak Patel, a North Carolina-based Wyndham franchisee who owns and operates with his wife four Days Inn and invests in multiple other Wyndham properties. “I like the way the company has come to this level, and I wouldn’t mind reinvesting in Wyndham again.”

SunTrust Robinson Humphrey analyst C. Patrick Scholes also thinks Wyndham is making progress, citing market share gains among its economy brands during Q3. In the next breath, however, he says the biggest challenge and opportunity is the need to more aggressively grow the system, along with further integrating La Quinta. “Ideally, they will get Wyndham customers to cross over to La Quinta and vice versa,” Scholes says.

Owners also seem to like the leadership of President and CEO Geoff Ballotti, who has a growing reputation as a stand-up leader who will own his mistakes, as well as be available to the franchise community.

“He is, without a doubt, one of the most accessible and humble CEOs in the hotel industry today,” says Harshil Patel of Champion Hotels, a Wyndham owner based in Oklahoma City, Oklahoma, who would not answer direct questions about Wyndham’s strengths and weaknesses as a franchisor. “When Wyndham announced the purchase of La Quinta, Geoff stood in front of a whole room of concerned La Quinta franchisees and gave out his cellphone number so that anyone could reach out to him directly. It was a clear representation of who he is.”

Ballotti says the split creating a hotel franchise company in May has given him and his team even more focus and flexibility. “We are able to do deals at higher multiples than we were looking at before. It has us entirely focused on being an asset-light, fee-based business that is driving consistent earnings and cash flow growth,” he says.

**JOBS AT HAND**

For the Harvard University-educated Ballotti, who has held multiple positions at Wyndham, including president and CEO of Wyndham Exchange & Rentals — who also was president, North America, at Starwood Hotels &
Resorts Worldwide — stabilizing the system and opening a path to greater domestic rooms growth is chief among his near-term goals.

He says Wyndham is opening more rooms than ever domestically on a gross basis. “Where we’re most encouraged right now is the progress we’re making internationally, where our room growth declined in the first quarter and second quarter based on the work we’re doing with our master franchises,” he said during the Q3 earnings call. “But when you look at what happened in the third quarter, with 6,000 rooms of positive international growth, we’re really excited about that growth and where we’re seeing it overseas.”

He cited China direct business growing, with a pipeline up 16%. The Ramada brand, in particular, has seen strong growth there — all coming through direct franchise sales. “We have over 40,000 direct franchise rooms in that country. We are seeing strong growth in Southeast Asia and in a solid pipeline in Europe,” he says. “I would like to see it stronger and in Latin America, as well.”

In fact, emerging markets like China — where Wyndham has grown in a short time to 1,400 hotels split among eight brands and developed a 100-strong Shanghai office — is probably the company’s biggest opportunity to continue to grow. “Our ability to add new brands into the China market is really strong… We’re now selling franchises directly and we’re managing. One of my favorite managed hotels is the Wyndham Grand Xian.”

Wyndham is increasingly managing, with upward of 500 hotels system-wide. “Internationally, we probably have about 100 managed that fit in the upper-upsacle market. We like to manage,” Ballotti says.

Outside China, Ballotti says Southeast Asian markets like Vietnam and Indonesia have been the company’s fastest-growing market over the past three years, and continue to be so. He also points to Latin America, where the company acquired Argentina’s Fen Hotels and its 70-plus properties about 18 months ago and is now selling Wyndham brands across the region; he notes that the company just crossed 3,000 rooms in India.

Domestically, in addition to its most recent acquisition brands of La Quinta and AmericInn, Wyndham’s soft brand, Trademark, added 60 hotels this year to go with 50-some hotels in Europe. Another 70 Trademarks are in the pipeline, according to Ballotti. La Quinta’s pipeline stood at approximately 24,000 rooms at the end of Q3 and guidance suggests it will grow at a 2% to 4% clip in the near term.

On the M&A front, Ballotti wants bolt-ons of at least similar quality to La Quinta and AmericInn, as well as brands that have domestic and international growth stories. Having averaged an acquisition about every 18 months over the past 30 years, he says...
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that expectation should remain the same with organic growth leading the way forward.

TRANSFORMATIONAL LA QUINTA

The May close of the La Quinta deal dramatically expands Wyndham’s presence in the mid-scale space and gives the company, in general, a lift outside of the economy segment. “Now we are at 40% of the nation’s mid-scale rooms and have an ability to continue to grow that brand both domestically and internationally,” Ballotti notes.

What makes the deal transformational is that it more than doubles the company’s associates (close to 16,000) and gives even more heft to its managed portfolio. “They have an exceptionally strong team, and we’ve been able to maintain their Irving, Texas, office. It has really bolstered our franchise sales, our franchise development, our architecture design and production resources,” Ballotti says. “We’re learning how to be a better, new construction company... We have 35 La Quintas in the ground right now under construction.” He adds, “We want to be the leading provider of select-serve lodging on both the franchise and the managed front and we’re now managing over 400 select-serve operations.”

Because so many Wyndham franchisees also have La Quintas, Ballotti and his team learned they needed a stronger distribution platform and a larger loyalty program to drive more business direct. “In the first quarter of next year, when we combine La Quinta Returns with Wyndham Rewards, we’re creating something very powerful for those owners,” he adds.

On top of that, La Quinta owners will move from a legacy central reservation system to Wyndham’s cloud-based platform, which will drive down their cost of distribution, lower online transaction fees and provide more direct business, according to Ballotti.

From a growth perspective, Ballotti says by the end of Q2 2018 Wyndham signed 20 new La Quinta agreements and reignited construction deals. “The great thing about their pipeline is 90% of it is new construction and their prototype is a killer in its category in terms of it’s cost efficiency for developers,” he says, adding that data suggests more than 30% of U.S. markets today do not have La Quintas.

Internationally, there are no more than a dozen La Quintas, and Ballotti says brand President Raj Trivedi is focused on Mexico and South America, including Argentina, Uruguay, Bolivia and Peru. In Europe the first prospects should come from Spain,
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Portugal and Germany. Asia will start selling the brand when the timing is right, Ballotti adds, but for now the company is just introducing the Tryp by Wyndham, Wyndham Garden and Wingate brands.

**FLIGHT TO QUALITY**
Among the other stated goals of Wyndham has been working with the franchise community to better enforce brand standards. Domestically, over the past three years Wyndham has trimmed some 80,000 to 90,000 sub-standard rooms and has been especially focused on the bottom 20% of its portfolio with more deliberate and diligent inspections, which Ballotti says has the endorsement of the various franchise advisory councils.

Probably one of Wyndham’s most successful brand improvement programs has been with its largest brand, Super 8, which launched a new guest room design a few years ago. A new FF&E standard has become a requirement, and Ballotti says those who have been through the process are running a higher RevPAR index and achieving their monthly share.

The next priority, he says, is Days Inn, where the advisory board is standing firmly behind a new guest room design for some 1,800 hotels.

“I feel good about doing this for Days Inn because they look at the cost concern and the quality, as well as review our clientele,” says franchisee Janak Patel. “They understand that as a smaller economy hotel how owner-operators are concerned.”

Patel says the new scheme is a boost for how Wyndham is going to play its role during an inevitable down cycle, as well as during an upmarket.

“The position for this economy brand is well-centered. Geoff Ballotti will not just improve the quality, but he will look at what can be done to market this. And based on the marketing, what kind of resources and tools they will provide to benefit the operators, the franchisees and the GMs.”

In addition to more aggressive PIPs, the “by Wyndham” tag is going on all brands. Across the brands, franchisees will have three years to install new signage, and Ballotti believes the move will translate into more than a half-billion additional impressions.

“It will have a big lift in terms of the awareness for Wyndham and, most importantly, Wyndham Rewards,” he says. “Since April, our digital folks have seen an increase in searches by over 50% for all of our brands given that they’re now cross-referenced and searched 6 million times a year.”

As for individual franchisees upset about another PIP, Ballotti says it is offset by the leadership of the brand councils that support the changes.

“The biggest issue for us is driving engagement with franchisees — getting them to believe in us and becoming more engaged,” Ballotti says. “Our engagement levels have consistently risen in each of the last three years that we’ve surveyed them.”

**BIGGER PICTURE**
When considering macro-economic factors and their potential impact on the business, Ballotti says the group is not seeing anything that would suggest potential bigger issues. “We’re seeing economy and midscale brands out perform the rest of the industry,” he says. “We’re incredibly confident when it comes to consumer confidence. We saw a great summer season. With 80% of our business is leisure — it’s the spot that’s been outshining for the last several years — you’d think given consumer confidence we’ll continue to outpace that.”

In terms of supply, Ballotti again points to the economy and midscale segments, where he says it has continued to run well below demand. “We don’t foresee any change,” he adds. “People are still traveling and we are really optimistic about the year.”

Even with interest rates and construction costs rising, Ballotti paints a positive picture. “The ability to find financing for the suburban properties that franchisees are constructing has really not changed,” he says. “Construction costs have picked up a little bit. But this is a very compelling and resilient business model from a return of investment standpoint… Efficiency and the return on building a strong category killer is where financing will be readily available. GOP will be higher than in luxury and upper-upscale.”
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To BRAND, or not to BRAND

How the explosion of affiliation options is changing the hotel landscape.

Contributed by Megan Rowe

I
n the past decade, hotel owners have faced a barrage of new brands, new choices for independent hotels seeking the shelter of a larger organization, and newly defined segments. For an owner or investor, it can be daunting. Go with a traditional brand? Sign on with a consortium? Fly solo? Bet on a not-quite-proven soft brand?

Figuring out which model aligns best with a property is not simple, although the end game seems pretty straightforward. “We look at what is going to maximize the value of the real estate,” says Ramsey Mankarious, CEO of London-based Cedar Capital Partners. Cedar’s holdings include high-profile luxury independent hotels and brand-managed properties.

Independents dominate in Europe, in large part because the existing inventory often doesn’t fit well into brands’ standards. Because of that, soft brands and consortia are appealing options for many owners. But with bigger properties, “banks want to see a professional international brand running the hotel, which is what they are used to,” Mankarious says.

Branding is making inroads in Europe, particularly France, Spain and the U.K., says Philippe Doizelet, managing partner at Horwath HTL in France. The shift started when companies like IHG and AccorHotels moved from ownership toward franchising, and was nudged along by the rise of OTAs.

Soft brands are especially well-suited to the current environment. “All those hotels that have capitalized on some lifestyle flair now have the guarantee offered by a brand name and strong distribution,” Doizelet says. “You end up being endorsed by a major group, but you don’t have to develop based on a very rigid concept.”

Jay Shah, CEO of Philadelphia-based REIT Hersha Hospitality Trust, looks at four factors when deciding which model fits best: the ability to create real brand equity, market conditions, location and size. He thinks soft brands make sense for many owners.

“It allows the guest to enjoy the independent experience with a certain quality assurance, and it allows them to participate in the loyalty programs, which remain a driver,” Shah says. “Owners, in turn, get the comfort of knowing there are some traditional hard-brand drivers in place.”

Shah adds, “As an independent, you will have more costs around marketing, branding and sales; with a soft brand some of that will be supported by the brand. You have to decide whether the amount you pay for that will drive incremental EBITDA.”

Going it alone is not an option for many owners who lack the expertise and staff
Hersha Hospitality Trust affiliated its newly opened Cadillac Hotel & Beach Club in Miami Beach with Marriott International’s Autograph Collection.
to survive against better-equipped competition. “You have to be better, more focused and more effective in your sales and marketing to make up for what the brands do,” says John Hamilton, senior vice president of development at Pyramid Hotel Group, a Boston-based asset and property management company.

In parts of Asia Pacific, where a building boom has stretched the capacity of architects, interior designers, engineers and other experts, “appointing a major brand with a good technical services team can be of great assistance,” says Robert MacIntosh, executive director at CBRE Hotels Asia Pacific. Developers are turning to franchise agreements and management agreements to tap their specialized services, he adds.

Yet another factor to settle before committing to any kind of brand: exit strategy. “It’s very important to consider your holding pattern for the asset. How long are you going to hold it? If it’s short-term, there is a premium when selling an unencumbered asset. The pool of potential investors is significantly larger,” says Andrea Grigg, executive vice president of JLL. Buyers want flexibility in determining a hotel’s future, and a long-term contract limits options.

**RULES OF THUMB**

“If you are in a very dynamic market, like a city center, or if the hotel is well-located and has some flair in décor, you can be successful as an independent — no question,” Doizelet says. It would be difficult for a hotel of less than 50 rooms to get the benefit of affiliation, he adds.

Shah says when an independent operator can offer a unique experience, pricing power might exceed that of a similar branded hotel. “So you might outperform on the top line without additional costs on the bottom line,” he says. But, Shah adds, operators need to have their own capabilities in e-commerce, revenue management, marketing and sales.

As a rule, says Craig Mason, executive vice president of CHMWarnick, a hotel asset management and advisory firm, “the smaller the hotel and better the location, the more you can lean heavily on being independent or soft-branded. A larger hotel in a weaker location may need the support of a brand to help fill the rooms, relying heavily on loyalty programs.”

Location — not flag — arguably is the primary driver of demand, Mason adds. “A well-located hotel next to a major demand generator has a unique advantage. If the hotel is not large — less than 250 rooms — the demand generator located nearby may be enough to fill the hotel, and there is no reason to pay the fees for a soft or hard brand.”

Loyalty is perhaps the most compelling reason to line up with a chain. But “the point-collecting mentality in Asia is nowhere what it is in North America,” says Eric Levy, managing director of Tourism Solutions International in Singapore. But he also thinks it will catch up eventually.

Some hotels demand a brand: Suburban, airport and roadside hotels and those with significant meeting facilities rely heavily on chain affiliation. Lenders and institutional investors typically also prefer brands. And not everyone wants a unique experience. “Customers still love standards,” Doizelet says. “Especially when they are traveling for business, they’re not keen to go on an adventure. What they’re looking for is convenience.”

Hotels in secondary or emerging markets benefit from a brand as well, Mankarious argues. “People visiting those markets don’t know them that well, so they put a lot of emphasis on feeling comfortable — and that means choosing a brand,” he says.

Asian destinations are ripe for branding as they open up to more international travelers, MacIntosh notes, and “brand recognition may be difficult for an independent to achieve unless offering a unique product.”

Is brand affiliation a plus during an economic downturn? “During downturns there is a sense of safety with a brand-managed property,” Grigg says. Mason agrees. Even soft brands, he

“As an independent, you will have more costs around marketing, branding and sales; with a soft brand some of that will be supported by the brand. You have to decide whether the amount you pay for that will drive incremental EBITDA.”

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says, offer a safety net because of the reservation system and loyalty program supporting the asset. But Shah suspects that while branded hotels might do marginally better in a downturn, independents would recover more quickly.

But brand can’t make a silk purse from a sow’s ear, Levy says. “Some properties just don’t have the facilities, the location, or whatever attribute is required to be competitive, and a brand is not a panacea.”

Mason says owners sometimes look to brands and managers as advisers, “which can be a slippery slope,” he notes. Bringing in a third party early in the process to help navigate development and negotiate the branding/management decision is a way to avoid surprises.

“We tell clients, ‘Don’t fall in love with a brand when you are developing a product,’” Grigg agrees. “Make sure you do your homework and request information. You need to understand that you can have the brands compete for your business.”

WHAT’S DOWN THE ROAD?
The greater availability of affiliation choices for owners opens up opportunity for global expansion among the major players, especially in markets with many independents and new development. But there’s a downside to all those bulky product lineups.

“The reality is that there is brand bleed across many of the current brands within the large hotel companies, potentially diluting demand for their core brands in a market.”

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“The reality is that there is brand bleed across many of the current brands within the large hotel companies, potentially diluting demand for their core brands in a market.”

— Craig Mason, CHMWarnick

brands within the large hotel companies, potentially diluting demand for their core brands in a market,” Mason says. “I think this, as well as the high cost to be affiliated with a brand, is driving more owners to consider the independent model and the flexibility it represents.”

One casualty of brand proliferation might be some consortia. All those soft, boutique or lifestyle brands theoretically are chasing many of the same properties that are aligned with traditional soft brands. Laurence Geller, chairman of Geller Capital Partners, a Chicago-based luxury hotel investment and management firm, suggests consortia may be best suited to making deals with one chain or another. He also predicts that more operators with small groups of branded independent hotels will join with industry giants, mainly to leverage scale in technology and distribution.

BRAND OVERKILL?
The explosion in hotel brands has been breathtaking: Between 2006 and 2018, U.S. parent companies created 72 new brands, and each month it seems the big players unveil yet another product. Hotel research analyst Stephen Hennis, president of Hotelogy, calls the phenomenon “the need to fill shelf space.” In other words, the dominant companies want to have a product that suits a broad range of hotel owners and guests.

“It gives them more of a basis to compete,” he says. “It helps get people to go to their website to book instead of using an OTA. If they’re on Marriott.com, and they see the brands they typically stay at aren’t available, they might try an Autograph Collection or a Moxy, even if they don’t know what the product is.”

On the developer side, Hennis says, companies are betting on the strength of a big company to carry an untested brand. But owners of existing hotels face potential impact issues from the upstart brands, which he calls “ankle biters.”

For example, travelers on Hilton’s reservations site might be looking for a Hampton by Hilton, but see that a less expensive Tru by Hilton is right next door, and will still net them Hilton Honors points. He says that kind of scenario might come into play more frequently if there is an economic downturn and travelers trade down.

The other risk is brand fatigue among consumers, but John Hamilton, senior vice president of development at Pyramid Hotel Group, sees that as a self-resolving problem. “The main reason there is confusion is that most of these brands haven’t been around long enough to develop their own distinct personality,” he says. “Over time, there should be more separation, as people stay in these properties and become more familiar with them… And there is definitely a trend, especially among younger consumers, to have a wide variety of offerings to satisfy individual tastes and needs.”
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an entrepreneur by disposition,” says Philip Bates, CEO of Bode Hotels. Bates, whose background is in private equity, was running a real estate tech venture with his brother when the idea for Bode was born; the entity includes a real estate company with a few other investors in the properties, and a management company. Bode, whose 4-star hotels average 100 rooms in a combination of new-builds and conversions, opened its first property, in Nashville, Tennessee, in November with a very focused target market in mind: groups. Rooms connect around common areas with kitchens and living rooms, and a central hub or gathering space offers F&B that morphs from morning to night. Chattanooga, Tennessee, opens in February, and after that are three California properties: Palm Springs, breaking ground next year; Indian Wells; and Orange County. HOTELS’ Investment Outlook talks to Bates about his approach and ambitions.

HOTELS’ Investment Outlook: How did you decide on the first locations?

PHILIP BATES: The Bode brand is built entirely around what we call group lifestyle travel. That is, people traveling in parties of three or more. You see multi-generational families. You see a lot of friends traveling, colleagues traveling, bachelor-bachelorette groups traveling.

When you look at markets like Palm Springs and Nashville, it is just full of group travel. We wanted to start there and we wanted to go into markets that were relatively far from each other, so that we could have a broader presence. Then once we put our anchor in those cities, we wanted to expand pretty close to them.

HIO: How will Bode accommodate groups?

PB: (When people are) traveling with their friends, they want to be in a lifestyle or a boutique hotel, in a setting where they can interact and enhance private spaces to an ambitious growth plan.
their experience with whoever they’re traveling… In a normal hotel you either have to hang out in the lobby and then just call it a night, or if you’re in a hostel-type situation, you’re in hotel rooms but you’re really a little bit cramped. As it comes to conversions, we’ve converted more condo-like buildings.

HIO: It’s more about what people are doing when they’re staying at the hotel versus, for instance, extended-stay.
PB: That’s right.

HIO: How did you conceive the idea?
PB: This is almost exclusively how we travel. This is how I travel with my friends. My wife and I went on five or six trips like this just last year… Frankly, it’s how the whole Bode team travels whenever we go to a new location. We’re all staying together.

HIO: What is Bode trying to improve on?
PB: We said, ‘OK, if there’s the whole spectrum of your best Airbnb to your best hotel, what are the elements from each of those that we can pull and begin to lay the foundation of Bode?’ Then from there, we want to pioneer out to where no one has really gone before and start customizing spaces for these people and really observing how groups interact out of Bode. Then iterating and customizing spaces to enhance that experience of our guests… When you’re traveling with your friends, you’re talking, you’re laughing, you’re usually doing things that are a little bit more leisurely, so you’re wanting to hang out in the lobby. When you get multiple groups like that into one area, whether it’s our bar or it’s our common areas, you just see the energy level of the property rise rapidly. It becomes a much more engaging and social scene. I think it’s really enticing. We observed that as a base layer, just only having had folks stay at our place for just a few weeks really. We’re hoping to build on that, and learn.

HIO: How big do you want to get in, say, three to five years?
PB: We think this is perhaps the most underserved area of hospitality, and so we’re on a trajectory to be 20 or 30 locations in that time frame. Whether that’s open or in various stages of development is a different conversation. But we think Europe and places abroad are really ripe for this kind of product, and in fact we have folks on the team that have experience in overseas markets for that reason. But I think for us right now we’re really wanting to lay a solid foundation for a long-term brand here in the States. But overseas, there’s definitely opportunity there that we would be looking at. Probably in three to four years.

HIO: Is your long-term play to join a larger company?
PB: It’s a little early to tell. I think our main focus right now is really on building a reputable brand. That’s just what we’re focused on and where that ends up taking us, we’ll see.

By Barbara Bohn, managing editor
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CREATE AN ‘ARMY’ TO GROW CULTURE

When the U.S. unemployment rate is at an all-time low of 3.7%, employees can pick and choose where they work and won’t give pause to leave one employer for another opportunity. Employee retention is a costly battle faced by every organization.

According to the U.S. Bureau of National Affairs, US$11 billion is lost annually due to employee turnover. If organizations don’t improve and brand their culture, the inevitable costs include (but are not limited to) the following:

- Recruiting and training new associates
- Productivity due to potential lost engagement among current team members and coverage for vacancies
- Service recovery

Company culture is the character of a company. It is their story to tell. Employees need a motive beyond the systematic paycheck to help them choose to stay. Whether it is mentorship, training and development, recognition and even work/life balance, businesses must address these areas of need to compete and thrive. When a company is not engaging with its associates, the consequences are dear. According to Gallup, only 37% of engaged employees are looking for jobs or watching for opportunities versus 73% of actively disengaged employees.

Culture can be used to retain employees as well attract new talent. Company culture is a key deciding factor for millennials, the largest generation in the workforce, when choosing an employer. According to the Association for Talent Development, millennials want to be recognized as individuals and to be “sold on a company through its values and culture.”

How do hotels create a culture that attracts and retains employees? That’s the US$11 billion question.

A strong culture needs a team of strong spokespeople. Ownership cannot spread the message alone. Here are some steps to take to help create an effective culture:

- Recruit within your own organization, constantly, looking for your “army” of culture diplomats. This committee should meet regularly and their goals should support those of your culture story. For example, if community outreach is important, have your culture committee identify what organizations they will support throughout the year and how line level associates can get involved.
- Onboard training should focus not only on policy but also the benefits of the company culture and mission. This gets new hires excited about your culture and keeps it alive each time a training takes place.
- Share stories of successful associates who have been rewarded for service, loyalty and cultural model behavior. Celebrating associate successes and important milestones brings your entire team together – even if just for a few moments. It creates a connection.
- Develop an award for those who best support your culture story. Make it an annual award that is a great honor to receive (and that other associates want to achieve) and get all associates involved in the nomination process.

Culture is your brand; it is your identity. Have the people who believe in it most and do it best, share your story.

Contributed by Justin Jabara, vice of development and acquisitions, Meyer Jabara Hotels, Danbury, Connecticut
Extended-stay hotels in the U.S. have achieved compound annual growth rates of 4.8% in total operating revenue and 6.3% gross operating profits from 2010 to 2017, according to recent research from CBRE. The firm forecasts demand for U.S. hotels in this segment to increase by about 2% each year through 2022.

At the same time, CBRE’s 2017 data shows that U.S. extended-stay occupancy reached over 80%. By comparison, STR clocked total U.S. occupancy at 65.9%. The numbers show the promising longevity of the segment.

While it’s clear why extended-stay hotels are gaining attention from developers and owners — after all, this segment’s revenue did not suffer as much as the overall lodging industry during the depths of the recession in 2009, according to CBRE — the definition and operating model of a true extended-stay hotel might not be as apparent.

Many hoteliers might think of an extended-stay hotel as comprising rooms with kitchens. While kitchens are an essential part of the model, it’s more important to look at the property’s average length of stay.

This segment caters to guests in transition: people who are relocating, experiencing disaster-related events, traveling for work for an extensive period or simply trying to get back on their feet. These guests typically stay five to seven days on average, with a large percentage staying for 30 or more days.

This extended length of stay leads to a vastly different operating model than a typical transient hotel, allowing for controlled costs and greater return on investment. For instance, wages are one of the biggest line items for hotels, and extended-stay cuts that need in half. Because of the stretched length of stay, there is simply no need to staff as a transient hotel would. For a 100-room hotel, an extended-stay property would need about 10 to 12 total employees. Those employees can also be cross-trained to complete tasks. The front-desk associate will not be checking in guests at the same pace as his or her counterpart at a traditional hotel. A washer and dryer can be housed behind the front-desk area, and that team member can work on laundry when not needed at the desk. Likewise, housekeeping staff is light as rooms aren’t turned on a daily basis. That leads to less of a need to spend dollars on water consumption and washing linens.

Additionally, extended-stay guests use the kitchens in their rooms. Therefore, they don’t expect the hotel to provide a complimentary breakfast. A true extended-stay hotel might provide a plastic-wrapped muffin and coffee in the morning. The offering costs about 55 cents per occupied room, a fraction of the expenditure required at a typical select-service hotel that provides breakfast.

While the operating model allows for fewer expenses, developers can find great ROI when it comes to construction costs, too. True extended-stay hotels can cost 15% to 20% less to build than typical select-service projects due to their lack of public space.

Contributed by Stephen Miller, managing director, real estate development, Extended Stay America, Dallas
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