Recent Trends & Key Considerations in Hotel Valuation

12th Annual Southern California Chief Appraisers Meeting

October 28, 2015

Presented by: Leah Dauer Murphy, HVS Senior Vice President
SUPERIOR RESULTS THROUGH UNRIVALED HOSPITALITY INTELLIGENCE. EVERYWHERE
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• SHARED OWNERSHIP
• SUSTAINABILITY
• PROFESSIONAL SKILLS DEVELOPMENT
KEY CONSIDERATIONS IN HOTEL VALUATION
Key Considerations in Hotel Valuation

- Franchise Agreements
- Capital Improvement Needs
- Hotel Management Company
Key Considerations: Franchise

Franchise is a major driver of revenue and value

- **Customer:**
  - Known product – facilities & services
  - Quality assured
  - Frequent guest programs and points

- **Hotel:**
  - Reservation system
  - Advertising and Marketing support
  - Policies and procedures
Key Considerations: Franchise

Operating Costs

- Royalty Fee: 3.0% to 7.0% of Rooms Revenues
- Program Fees: 1.5% to 4.0% of Rooms Revenues (includes marketing, advertising and reservations)
- Food & Beverage Fees: 2.0% to 7.0% of F&B Revenues
- Frequent Guest Program costs: $2.00 to $5.00 per room per member
Key Considerations: Franchise

Initial Construction Costs

- Brand mandated facilities
- Brand mandated materials and quality standards

Renovation Costs

- Replace soft goods every 6 to 7 years: $6,000 to $8,000/room
- Replace case goods every 12 to 14 years: $6,000 to $8,000/room
- Fully renovate bathrooms after 18 years: $8,000 to $20,000/room

Brand Standards: Services or Amenities

- Minimum 36 inch flat panel televisions
- Wireless internet with a minimum bandwidth
- Life Safety Systems
Key Considerations: Franchise

- Franchise Agreement cannot be transferred to a new owner

- Brand has the right to require potentially significant renovations for a new owner to maintain the affiliation
  - Property Improvement Plan (PIP)

- If the buyer doesn’t maintain the brand, the seller may have to pay liquidated damages
Key Considerations: Capital Improvements

- **Age of Overall Improvements**
  - Increasing number of aging hotels
  - Defensive Capital vs. Repositioning

- **Existing Improvements Could Limit Branding & Redevelopment**
  - Exterior Corridor
  - Life Safety Systems
  - Parking Requirements

- **Brand Mandated Upgrades**
Key Considerations: Management Agreements

- Is agreement Terminable Upon Sale?
  - Not as much an issue with Limited Service hotels
  - More prevalent in Full Service hotels

- Is Hotel Brand Managed?

- What kind of fees?
  - Base Management Fee
  - Incentive Management Fee
HOTEL TRANSACTION TRENDS
U.S. Properties Sold by Transaction Level

Source: HVS/Real Capital Analytics (RCA)
Seven Sales Over $1 Million per Room in 2015

- Bardessono Inn, $1,370,968
- Edition New York, $1,256,410
- Grand Del Mar, San Diego, $1,045,089
- Malibu Beach Inn, $1,700,000
- Waldorf-Astoria, New York, $1,380,042
- Baccarat Hotel, $2,035,398
- Montage Resort & Spa Laguna Beach, $1,451,613

Source: HVS & RCA
### Adjusted Volume Growth Still Substantial

<table>
<thead>
<tr>
<th>Period</th>
<th>Volume</th>
<th>% of Total</th>
<th>% Change</th>
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<tbody>
<tr>
<td><strong>Total Sales Volume ($10M+)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014H</td>
<td>$10,826,000,000</td>
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</tr>
<tr>
<td>2015H</td>
<td>$21,528,000,000</td>
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<td>99%</td>
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<tr>
<td><strong>Total Volume $1M per Room</strong></td>
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<tr>
<td>2014H</td>
<td>$1,482,000,000</td>
<td>14%</td>
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<tr>
<td>2015H</td>
<td>$3,308,000,000</td>
<td>15%</td>
<td>123%</td>
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<td>*<em>Total Adjusted Volume</em></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>2014H</td>
<td>$9,345,000,000</td>
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<tr>
<td>2015H</td>
<td>$18,220,000,000</td>
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<td>95%</td>
</tr>
</tbody>
</table>

*Without $1M per Room Sales

Source: HVS & RCA
2015H Sales by Price per Room ($10M+)

Source: HVS & RCA
Cap Rates Extracted from Sales Relatively Stable

Source: HVS & RCA
Key Takeaways – Hotel Market Conditions

- Ideal conditions for transactions remain – transaction volume and pricing should further exceed 2006 prior peak in 2016.

- Capitalization rates are expected to remain stable despite rising NOI as capital remains available and buyers compete for quality assets.

- Supply is the primary concern in most markets as improving fundamentals are spurring new development.

- Low price of oil, interest rates, and uncertainty in Europe and China remain areas of concern in the near term; however, there are few storm clouds on the horizon in most markets.
QUESTIONS?
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