HOTELS

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What Owners Want

Owners have never felt freer to mix and match management to opportunities—whether that means a major flag, no flag, a new name, a soft brand or a concept of their own.

Additional Web-exclusive content:
Companies to watch in Asia; new strategies in Spain; and the private equity story in the United States.

By Mary Scoviak, Contributing Editor

Track records for hotel companies still matter. So do relationships. But in this era of customization, nearly every decision to flag—or not to flag—starts with clean-slate thinking. There is no sure thing.

Giving owners what they want starts and ends with the numbers. "Owners always want performance, which trumps all the other elements," says S. Kirk Kinsell, InterContinental Hotel Group's senior vice president, chief development officer, The Americas. But owners see the decision as to which company can deliver the "best" performance varying from market to market. That fact is broadening the list of contenders and opening up growth avenues for hard brands, soft brands, membership concepts and independents alike. "You have to look at each location on a case by case basis. If there are local demand generators that you can influence readily on your own, the brand contribution becomes less important," says Teresa Matsui Sanders, president, InnWorks, Roseville, Minnesota, which has 13 America's Best Value Inns, four Wyndham Worldwide franchises and an independent. Matsui Sanders sees value in the marketing and channel support brands can bring. However, she says owners are carefully weighing the expected benefits against the direct costs of fees and royalties as well as "forced" operating costs and revenue reductions from brand mandates.

"To the extent my fee payments provide the kind of support I want and need in terms of revenue generation, quality standards and technology initiatives, I am happy to send my checks to the brand," Matsui Sanders says. "But, if I get the feeling that my fees are being used to pay for empire building or for a private plane to take people on vacation, it does not matter how much concrete value I am getting. I am still paying for something that does not benefit me. There is a great deal of anger and resentment among hotel owners for some of the traditional franchise brands."

Matsui Sanders says some of the disenchantment centers on brands that have strayed from their value proposition and consumer message. "That simply is not a healthy business model, especially when owners are locked into long-term agreements where termination comes at a financially unpalatable price," she adds. Reflagging is another key issue for owners. An independent hotel with US$1 million in revenue will have to weigh to what extent spending up to US$100,000 in annual fees to rebrand will improve performance.

Owners who share Matsui Sanders' views are building the numbers for franchisors who are more flexible and collaborative as well as for short-term membership concepts such as those offered by Best Western International and America's Best Value Inn, Vantage Hospitality's Chagrin Falls, Ohio-based membership brand that added 101 new properties in the first half of 2006. "It is about educating owners, not mandating to them," says Patrick Mullinix, America's Best Value Inn's national sales and development manager.

Even owners who have realized the full benefits of a big-brand portfolio are shopping around. They are taking a closer look at the average RevPAR index for the various brands nationally, brand contribution to revenue, national and regional sales, promotion and training support and the extent of input they will have in the decision-making process regarding their hotel. "Owners want far more involvement in decisions pertaining to physical standards and to the overall marketing program," says Laurence Geller, president and CEO, Strategic Hotels & Resorts, Chicago. That view is being reflected in management contracts with a more "consultative approach" and a more detailed approval process.

Accountability continues to be the buzzword among owners. Michael Nigitsch, president and CEO of Ishin Hotels Group, Tokyo, sees owners asking brands for "significantly enhanced" brand management and distribution; more focus on people management and people development; more transparent corporate cost structures and charging mechanisms; and enhanced technology/design/equipment and development support. He also predicts owners will shift management contracts toward shorter terms with lower fixed fees and more creative bonus fees. "Owners will be asking brands for more commitment to build business and organizational infrastructure in the respective local market," Nigitsch adds.

What Brands Offer Now

Brands are responding with "new dialogue pieces" that answer these concerns. "It is about how much brands will align with the owner's interest at the unit level, about how much the brand will mimic the owner's priorities, and about how much the brand can work with the owner's goals for hold periods and investment windows," Kinsell says. In the field, that can translate to investing alongside owners or reducing fee structures for new concept launches such as IHG's Hotel Indigo or providing front-end funding for new programs such as the rollout of the Breakfast Bar for Holiday Inn Express or Candl0ewood Suites' new bedding program, then allowing franchises to pay back corporate over two years with their capital expenditure funds. More attention to the bottom line is keeping some big players brand loyal.

Philadelphia-based Hersha Hospitality Trust will open

The Gist

• Owners have more management options than ever. Decisions on branding—or not branding—are market specific.

• Lesser known brands are getting a second look, especially the young or underpenetrated brands offered by the giants—Starwood's aloft, IHG's Hotel Indigo, Marriott's revitalized Renaissance. Start-up brands will need both corporate resources and adequate capital to get noticed.

• Big is not always best. Independence is back in vogue, especially among boutiques and resorts that market through the "soft brands" of major reservations/

three Residence Inns, one Homewood Suites and one urban Hampton Inn from Boston to Washington, D.C., this year because "these are our tried and true brands." "Do chains really deliver enough bang for the buck in terms of return for reservation services and marketing fees? Yes, most do—though the impact varies widely among the various brands and families of brands," says Jay H. Shah, Hersha's CEO.

marketing companies. Owners also like specialists—from Six Senses and Amanresorts to Joie de Vivre, Kimpton Hotel & Restaurant Group and Hoteles Silken.

• More participation by private equity players is shortening turnaround times. Savvy owners want more of a voice in issues ranging from personnel choices and succession planning to how their sales and marketing fees are being used to benefit their hotels.

Owner support programs are evolving along with owners' needs. One major area in which owners are demanding—and receiving—support from their management companies and franchisors is in human resources. "Asia Pacific's owners count on hotel operators to provide talented and capable human resources and related development and training programs—especially in light of the fact that many of the high growth markets such as China and India are struggling to provide enough qualified labor for the increasing number of job opportunities," says Paul Kirwin, president, Carlson Hotels Asia Pacific. In these markets, Kirwin says training has emerged as "an incredibly important part of hotel management."

The clear trend is toward personalization. "Each owner has different needs, different circumstances. Brands have to work closely with franchisees to develop financial and operational incentives that address their needs," says Dean Savas, senior vice president, Accor North America. Franchisees will see a new generation of initiatives such as Accor's Owner Orientation Program and General Managers Program that take owners and managers through the process step by step. Accor, like most major brands, is reaching out to a growing market of minority business leaders with its Ambassador Program—an offer that gives potential minority franchisees first-hand experience in learning about daily operations. Chains also are exhibiting new-found flexibility in meeting their owners' needs.

Not every new owner needs hand-holding. "The next generation of owners will be successful entrepreneurs from other industries. There will be those who have a proven track record in owning and operating service-oriented businesses and/or those who are real estate developers experienced in working with land, approval processes, construction and finance," says Mike Muir, senior vice president, Microtel Inns & Systems, US Franchise Systems. But that does not mean new franchisees will not be looking for help. Brands such as Microtel are bridging that gap by negotiating upfront initial franchise fees "if our franchisee is willing to use that money to benefit their hotel performance by hiring a management company to operate the hotel for the first two years of operation," Muir adds.

Technology is among the top issues on owners' priority lists. "Owners want to know how we are going to use technology to reduce costs," says Bill Fortier, senior vice president, franchise development, Hilton Hotels Corp. Chains are responding with everything from check-in machines and check-in via the Internet to more cost-effective and more marketable in-room business and entertainment offers. One of the biggest pushes still centers on distribution. "A key performance enhancer is taming the Internet. Higher yields from the electronic distribution system on all fronts is very impactful for owners' results," adds William Heaney, vice president, brand development, Red Lion Hotels.

Owners also want help harnessing development and construction costs. "We continue to work through different value engineering concepts," Fortier says. "The brand's focus is on having a building that meets its standards. But, there are things brands can do. We did away with the multistory atrium in our Embassy Suites as part of new design that saves land, energy and design costs."

Companies such as Taj Hotels, Resorts and Palaces, Mumbai, are using corporate leverage to bring down development and construction costs. They are standardizing suppliers, looking for ways to use materials used in quantities that earn better volume discounts and centralizing logistics. Development of localized vendors and sourcing of local alternatives to international materials also makes a substantial difference toward reduction of costs, says Rajshree Bakshi, director of sales—special initiatives & marketing information system for Taj's parent, Indian Hotels Co. Ltd.

Something Totally Different

Depending on an owner's goals, bigger is not always better. What constitutes strength in numbers for some means over-saturation to others. A brand's ability to differentiate itself is becoming a key issue in brand choice.

That preference is fueling growth not only for the giants' brand launches such as Hotel Indigo and Starwood's aloft or for rejuvenated flags within brand families such Marriott's Renaissance and Hilton's Doubletree, but also for breakout regional brands and niche players as well. Local expertise is a big selling point for players such as San Francisco-based Joie de Vivre. And why not? While many San Francisco/Silicon Valley hotels watched RevPAR tumble 35% from 2001 to 2004, Joie de Vivre's RevPAR index climbed from 103 to 121 for same store hotels. Numbers like these are one reason Joie de Vivre is bracing for the addition of 10 properties to its existing 38-hotel portfolio within two years. "What satisfies owners and lenders is the trust they are working with someone who made it through an historic downturn. Because of our track record, we have been able to be even more aggressive in terms of what we're asking for from a compensation standpoint," says Chip Conley, founder and CEO, Joie de Vivre Hospitality.

Dubai-based Jumeirah has been able to leverage its expertise as a Middle Eastern luxury operator to build a growth platform that already has planted flags in London and New York City and soon will add its first Asia Pacific hotel in Shanghai. "Some owners may want a 'fresh' brand, but most are keen to work with experienced management brands that consistently deliver 'fresh' experiences," says Gerald Lawless, Jumeirah's CEO. Based on his negotiations, Lawless says owners want a management company "to add value to their investment in a variety ways." That means not only delivering a commercial performance that meets the owner's objectives, but also increasing the value of the asset.

Personalization helps to sell growing brands, Lawless says. “Owners no longer want management companies to deliver ‘cookie-cutter’ management techniques. They want to associates themselves with cutting-edge, innovative, idea-driven organization,” he adds.

New owners with different kinds of objectives and different hold periods are shaking up the brand landscape. In Europe/Middle East/Africa, investment from real estate companies recently listed on the Alternative Investment Market is fueling growth for seasoned mid-size players with operational expertise and in-depth market knowledge. Aggressive and growth-oriented, these companies are opening up new kinds of expansion opportunity. “We believe these companies are willing to take greater risks than many of the institutional funds and financial banks. They are more willing to accept management contracts as opposed to leases,” says Jean-Gabriel Peres, president and CEO, Zurich-based Mövenpick Hotels & Resorts.

Young, start-up brands can make their move in this market, but they will have to bring more than a good idea to the table. “The choice of brand remains largely dependent on the individual property. New, specialist brands are welcome, provided they have adequate distribution. Newer brands and brands with capital such as Six Senses and Toga Hospitality’s Medina are benefiting already,” says David Gibson, CEO, Jones Lang LaSalle Hotels Asia Pacific.

Owners such as Nigitsch will need a lot of convincing. “New ‘global’ brands will have little economic value for local owners. More investment, research and marketing dollars will flow into creating the owner’s own brand platforms, as we did with the launch of the ‘b hotels.’ Established or newly forged, all brands have to demonstrate the capability to produce sustainable economic value in terms of asset, financial, team and customer performance,” he adds.

Fortier shares owners’ cautious approach to prototypes and new brands. While brands need to keep changing to remain in line with—if not ahead of—consumer demand, there are risks for owners who move to the cutting edge.

“New is always fun and will attract consumers with a ‘let’s try that’ attitude. Will the customer get what he or she wants and be willing to pay for that over the long run? That is the question,” Fortier says. He also points out that new brands “can be very expensive to build and operate.” Owners need to be certain brands can demonstrate demand sufficient to carry the concept as it builds toward critical mass.

Independent Minded

Economics is one reason for the explosive growth of soft brands, says Paul McManus, president and CEO, The Leading Hotels of the World. “Owners are looking at remaining independent or at a soft brand because of the value proposition,” McManus says. “Those with a strong established name of their own enhance their brand image and benefit from global sales, marketing and distribution services at a fraction of the cost of a franchise fee.”

Soft brands also offer the lure of an a la carte service menu. Like guests, owners have the option of paying for what they want most. “The history of franchising in the United States has created a love-hate relationship between owners and brands.

Owners were held captive by brands' global distribution systems and, as a result, were required to enroll in long-term agreements without the promise of production," says Tom Griffiths, vice president, WORLDHOTELS, The Americas.

The Internet has leveled the playing field sufficiently to make independent status feasible in a globally competitive marketplace. "Luxury customers tend to up-sell themselves to higher room categories," McManus says. That has meant an increase in ADR from US$386 in 2004 to US$433 in the third quarter of 2006. Soft brands are taking on one of owners' key issues—the cost of supporting loyalty programs—with new initiatives such as Leading's Leaders Club, which are self-supporting. Members pay a joining fee to offset operational costs; benefits are delivered through partnerships with luxury goods and services providers.

Performance like this is earning soft brands consideration among the new wave of private equity investors, many of whom are mixing hard and soft branded properties in their growing portfolios.

"What is most interesting about the new investors is the operations strategy—or lack thereof—behind their acquisitions. These investors simply identify luxury properties which they determine to be underperforming and/or undervalued and have turnaround potential. These are pure real estate plays. In three to five years, they will be transformed into profit centers and sold again," McManus says. That does not leave much time for a management company to ramp up its returns.

Both McManus and Griffiths point to the growing appeal of soft brands for one-of-a-kind approaches such as those launched by owner/managers such as Grace Leo-Andrieu, Gordon Campbell Gray and Sir Rocco Forte, as well as niche boutique hotel operators around the world. "The investor groups and funds looking at boutique hotels seem to be smaller players who are not interested in big, high-risk projects that do not deliver the same return on investment as a successful niche product," Griffiths says. "I see the next generation of hotel owners as young, non-traditional operators who place a premium on the guest experience. The products they create will reflect personal taste, regional diversity and a commitment to the 'experience.' They will be aimed at consumers who avoid traditional hotel services."

The Stats

Asset managers are becoming a way of life for owners. What will they be looking for from the general manager?

• Doris Parker-Grossman, Jones Lang LaSalle Hotels, Chicago: “On the revenue side, asset managers are paying particular attention to rate growth and yield management systems to ensure money is not being left on the table. More attention is paid to the food and beverage and spa operations—and their contribution to the bottom line. The majority of Last Room Available accounts are being eliminated. On the expense side, union activity is being followed closely—regardless of whether the hotel is unionized—as union negotiations and agreed terms will impact labor costs. Energy costs will be tracked more closely. Amenity creep is being monitored as many amenities have hidden operating costs attached. Dinosaurs need not apply. Operators and owners have little patience for GMs who are not technologically savvy.”

• Philippe Bijaoui, HVS International, Madrid: “In Spain, more and more lease agreements have variable components linked to revenues and even sometimes to gross operating profit. Some performance tests are not really applicable, taking into account the European laws that forbid the exchange of information between hotels. So, asset managers should try to find other ways to measure performance.”

• David Gibson, Jones Lang LaSalle Hotels, Sydney: “Hotels are seeing a material portion of their sales and marketing budget going toward group marketing services (i.e. funding of head office sales and marketing efforts.) Asset managers should question how these funds are being used to the benefit of their hotel. They also should look at e-channels and how they are charged for by the operators. Routing of reservations through operator-controlled channels is illegal in many countries. Succession planning will be a key focus, especially as labor markets tighten and new hotels open at a rapid rate—particularly across China and India. In maturing markets, many owners will be looking forward to predict when the current will cycle and when they should sell out. Operators must keep owners aware of upcoming threats to supply.”