HVS NYU Investment Conference Takeaways

November 11, 2021 / By Rod Clough

The **NYU Investment Conference** arrived five months late this year, but it was worth the wait. The event attracted over 1,000 registered participants eager to hear from a stellar lineup of the global industry's top leaders and influencers, and it kicked off in a bustling Times Square on the same day U.S. airports reopened to fully vaccinated international travelers. The **Marriott Marquis** did an expert job of handling the event, including top-notch service, food, beverages, and cleanliness. The attendees, all required to be fully vaccinated, were treated to a fantastic program arranged by **Dorothy Jennings** and her planning committee.

Diversity, Equity, and Inclusion Take Center Stage

A highlight of the event were the panels and conversations centered on diversity, equity, and inclusion. Speakers agreed that greater efforts must be made to attract minorities, particularly Black students, for hotel-related degree programs at universities and colleges. Intensified efforts are needed to encourage minority students, particularly Black students, to pursue hotel-related careers (e.g., hotel operation, hotel development/ownership, lending institutions, and real estate investments). A provided example of this working is the partnership between **NYU** and **Howard University** to create a program that is attractive and encourages Black students to pursue hotel-related professional degrees.

Necessity for Fast HR Innovation is Critical, Especially in Light of Quickly Returning Demand

As more and more positions go unfilled, and as the number of people leaving the industry daily continues to exceed those joining, quick innovation is required not only to stop the outflow but also to reestablish the hospitality sector as a top choice for employment. While higher wages and/or expanded benefits should help, more will be needed to compete with the likes of **Amazon**, which offers signing bonuses and much more flexible schedules, among other aspects. Hospitality companies that can make quicker hiring decisions, initiate daily payroll, and roll out other innovations will find themselves better staffed and capable of taking advantage of the industry's rebound. Those that don't will find themselves unable to reopen entire room inventories, food outlets, and banquet and event capacities.

Management companies are looking forward to the ramp-up of international work visas for hotel staff, and the importance of this factor was underscored at the conference. The industry has long thrived on an internationally diverse workforce, and this is a key aspect to solving the current staffing dilemma.

ADRs & Occupancy Are Rebounding Faster than Expected

Average ADRs in the United States bounced back to 2019 levels this summer, and by the fall of 2022, many global CEOs expected to see brand average RevPAR levels back to where they were prior to the pandemic. Accelerating the ADR recovery is the emergence of higher inflation. In deflated dollars, the 2019 RevPAR may not return for another three to four years, and with cost pressures heightened factored in, the higher rates won't likely translate into considerably stronger NOI levels.

Occupancy's comeback has been positively influenced by longer lengths of stay, as more and more people combine business and leisure (colloquially known as the "bleisure" segment). The pandemic has given us the opportunity to slow down and contemplate what is truly important, including our career paths and work-life balance, and accounting for personal time and recharging time. Lifestyle hotels (particularly in the upscale,

Summary

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upper-upscale, and luxury tiers) must continue to evolve in order to fill the niche of experiential travel for people who place importance on these aspects. This can also include hotel stays or public-area hotel use from residents in the local neighborhood that need a place to work, visit, and/or socialize outside of their home office/residence. More people being in a home environment 24/7 is opening up new hotel demand sources from this nearby resident group.

The strengthening of resort markets, highway markets, and suburban markets is expected to continue to outweigh any lagging recovery in the central business districts. The robust extended-stay sector is also helping to offset the more challenged property types.

What remains to be seen is how the bundling or unbundling of amenities and related charges translates into revenue growth. What works for a midrate-level property may not work as successfully for a luxury-class hotel.

Cap Rates Expected to Stay Low

As I presented in my Statistically Speaking session, cap rates are at new lows for the limited- and select-service sectors, about 1.0 to 1.5 points below, on average, of what would be normal levels for these property types. With more and more investors chasing quality deals in this space, and the still-low cost of capital available, these low rates should remain in place through the near term. The consensus was that these low interest rates won't be around for long; however, at present, this is a seller's market.

Currently, the alternative asset classes of office and retail don't look as favorable as they may have in prior downturns (though apartments and industrial space are still popular sectors). The rise of Amazon and the decline of storefront retail, as well as the movement toward more flexible work-from-home job designs and the related need for less traditional office space, have put pressure on these alternatives as commercial real estate investments. Equity returns are now in the 12%–16% (mid-teens) range for assets that may have previously been in the low 20% range.

Next Year Should Bring Strong Transaction Volume

The fire sale of hotel assets due to the pandemic never materialized, as equity infusions, PPP funding, and loan modifications stepped in instead. While distressed asset activity may increase in 2022, the recovering economy, accelerating group bookings, and return of international travel will likely dissipate any tidal wave before it reaches shore.

For non-distressed assets, the consensus was that 2022 would most certainly be an active year, maybe even a banner year, for hotel transactions. Private equity funds looking at the hospitality sector have low return thresholds at present, which is positively affecting pricing, particularly in light of inflationary cost pressures on the pro forma. CMBS debt is becoming more readily available. Moreover, international investor interest is high, as the United States is seen as an economically and politically stable country, especially compared to the global alternatives.

In Closing

Another concern raised for investors is the increased wear and tear on the physical hotel asset related to the increase in leisure demand. Higher PIP and capital investments are likely coming, well beyond a typical reserve requirement, and should be factored into pricing decisions by buyers.

With inflation growth not currently dissipating, buyers should also pay closer attention to the exit scenarios, particularly if this is just three or five years down the road. Factors to analyze include the potential cost of capital at that time, the renovation requirements, and the effects of labor and cost inflation on the bottom line. Accordingly, management companies will need to get increasingly creative when coming up with cost-saving solutions that can be implemented without a decline in the customer experience.

The industry has many challenges ahead, but it was evident that we are among a group of exceptional leaders and talent that will overcome these with hard work, collaboration, and innovation. It remains exciting to be part of this group of leading organizations helping the industry thrive.

*Many thanks to **Emil Iskandar**, **Glenn Skolnick**, **Chelsey Leffet**, **Patricia Shih**, **Robert Fitzpatrick**, and **Cole Masler** for their contributions to this article.*

About Rod Clough

As President of HVS Americas, Rod oversees strategy execution for HVS throughout its 40 Americas locations. Rod's tenure with HVS spans over 25 years, during which time he has played an important role in growing the company from a few locations across the Americas to 40. In a typical year, Rod's group consults on over 2,500 existing or proposed hotels and resorts, and in 2021, he oversaw the 568-hotel Extended Stay America appraisal portfolio. In 2003, Rod founded the firm's sister appraisal division, U.S. Hotel Appraisals, which completes roughly 1,000 hotel appraisals annually. Rod is a founding owner/partner of HVS Mexico-Latin America, and he re-launched the firm's U.S. Brokerage and Capital Markets division in 2018. Rod is a Designated Member of the Appraisal Institute (MAI) and a licensed real estate broker. Furthermore, Rod is proudly Latino and gay, and his firm is welcoming of all races and colors, sexual orientations, ages, genders, and gender identities. Once associates join HVS, they tend to stay due to the extraordinary culture Rod has inspired, a culture defined by the ideals of balance, connectivity, efficiency, collaboration, honesty, integrity, kindness, and excellence, among others. Rod resides in northern Colorado where he and his husband Jeff are raising their daughter, Rory.