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MARKET REPORT

How the Right Asset Management Firm Helps Optimize Hotel Investments

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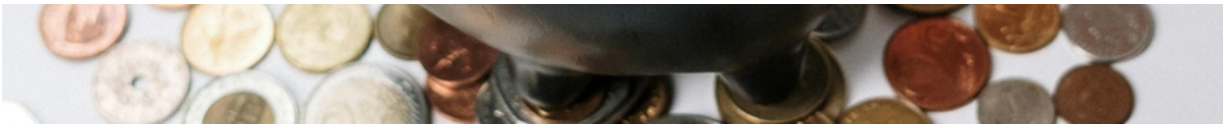
Partnering with an asset management firm can help maximize investor returns and property values. Asset management is particularly important in the current environment where macroeconomic conditions are in constant flux, geopolitical issues continue to intensify, and domestic monetary policy has considerable implications. The following article outlines how the right hotel asset management firm will help optimize the return on your hotel investment.

When implemented effectively, partnering with the right asset management firm can help maximize investor returns and real estate property values. Asset management is particularly important in this post-pandemic environment where macroeconomic conditions are in constant flux, geopolitical issues continue to intensify, and domestic monetary policy has considerable implications for real estate wealth management.

These factors present both challenges and opportunities; however, without the proper analysis and expert tactics of skilled asset managers, risk becomes more difficult to anticipate and opportunities more challenging to harness.

The following article outlines how choosing the right asset management firm, and more specifically, the right hotel asset management firm, will help optimize the return on your hotel real estate investment.





But First, What Is an Asset Management Firm, and What Are Its Obligations to Ownership?

Asset management is first and foremost about protecting the interests and maximizing the investment of an owner's real estate holdings. Asset managers are responsible for implementing the strategic direction of the asset, including its financial performance, risk management, and condition oversight. The most competent asset management firms work to ensure the long-term prosperity of the investment through efficient operations and income growth.

Asset managers in the real estate sector have a long list of responsibilities. A few of these might include tenant and lease management; property performance analytics and reporting; property maintenance coordination; risk mitigation; strategic development; portfolio management; environmental, social, and governmental oversight; and financial management.

Asset managers are generally not responsible for the day-to-day operations of an asset like a hotel manager or multi-family property manager might be. Asset managers instead confirm that the contractual obligations of the day-to-day operator are being met; ensure that the property is running effectively from labor, customer, and property perspectives; and, most importantly, represent the owner's interests and vision.

How Does a Hotel-Specific Asset Manager Differ from a General Asset Manager?

The objectives of hotel-specific asset managers and general real estate asset managers are aligned in that both aim to maximize the benefits of an investor's real estate holdings, both have real estate expertise, and both understand how the current economic climate affects portfolio management. However, hotel-specific asset management is highly nuanced and requires a greater knowledge of the lodging industry and asset performance itself.

A hotel asset manager will home in on the following specific items:

Hospitality Industry Trends – A hotel-specific asset manager will understand the greater hospitality trends happening in the market, like integration of artificial intelligence (AI) as part of the guest experience, technological advancement in revenue management, and franchise contract terms and obligations. Other asset managers might have more generalized knowledge and recommendations without specific industry context.

Revenue Management – Although a day-to-day operator of a hotel or resort implements daily average rate management, an asset manager designs the strategic plan for a hotel's revenue management through an in-depth analysis of market trends and demand cycles. This is executed with a complex variety of actions, including monitoring the competitive landscape, implementing dynamic pricing functions, and pivoting marketing and distribution channel management to optimize revenue per available room (RevPAR) levels.

Market Analysis and Investment Strategies – Because hotel asset managers act as representatives of the hotel owners, their understanding of the hotel real estate investment market is paramount to maximizing investor returns. They look for all opportunities to maximize performance, including capital expenditure planning, often in conjunction with brand requirements; operational efficiency, specifically from labor and energy perspectives; in-depth review of third-party contracts for compliance and adherence to terms; and asset repositioning strategies, including branding options, amenity offerings, and/or vendor enhancements.

Risk Management – The mitigation of risk in hotel investments is a never-ending task. Asset managers conduct risk analyses from economic, physical, environmental, and operational perspectives. Given the nature of the business, contingency and emergency planning is reviewed frequently to ensure the safety of guests and employees.

Operations and Cost Management – Hotels are highly complex real estate investments, and without prudent operational and cost management oversight, operators can overlook important decisions. Asset managers work in conjunction with operators to develop hiring, retention, and compensation plans; design cost-reduction goals; and set appropriate staffing and training plans. On the owner's behalf, asset managers analyze capital expenditure requests to approve or deny them, examine their validity, consider the most optimal time to implement the improvements, and more. An asset manager will also work with the owner, operator, and brand to negotiate the terms and conditions of any upcoming property improvement plan (PIP) required by the brand (if a branded hotel) or work with the owner and appropriate designers and procurement companies (if unbranded).

Guest Satisfaction and Loyalty – Hotel asset managers have a unique understanding of guest expectations and how to meet or exceed them. They work closely with brand representatives to ensure that the brand and owner are maximizing the benefits of their contractual relationship to enhance the guest experience and guest retention. Asset managers will work with operators to develop marketing plans, create staff training programs, add amenity and facility programing, and enhance product quality to improve the guest experience.

These are just some examples of the industry-specific expertise and knowledge that differentiate hotel asset managers from those with broader market experience. These differentiators allow these firms to be better positioned to effectively manage and maximize the value of the investment on behalf of the owner. Next, we will look at identifiable ways a hotel-specific asset management company can optimize investment results.

Identifiable Ways a Hotel-Specific Asset Management Company Can Optimize Investment Results

One of the biggest advantages of hiring a hotel-specific asset management company is its ability to review and analyze complex third-party agreements, particularly franchise and hotel management agreements. Negotiating these agreements requires in-depth market expertise, effective communication among a variety of stakeholders, and strategic planning. Hotel asset managers must first understand the objectives of the owner. For example, what are the owner's financial goals? What is the owner's desired involvement in the asset's operations? How will the investment be positioned from a chain scale perspective, and what capital outlay needs to be made?

Hotel asset managers can leverage their expertise to evaluate components such as fee structures, contract duration, areas of protection, performance thresholds, incentive structures, preferred vendor requirements, and indemnity clauses. These professionals can help evaluate differences between providers and negotiate incentives like key money and performance termination clauses. We note that most asset managers will also recommend consulting an attorney specializing in contract negotiations for reviews and recommendations.

Working with the hotel's operator and owner, hotel-specific asset managers analyze an abundance of key performance indicators that a more generalized non-hotel asset manager might not consider. The most common indicators are occupancy, average daily rate, and RevPAR, which gauge demand levels, pricing fluctuations, and overall revenue performance, respectively. More specialized performance barometers include the following:

- Gross operating profit (GOP) represents the profit realized before fixed costs are deducted. This is important because revenue and expenses above the GOP line require granular cost management and potentially offer the greatest opportunity for performance optimization.
- Penetration rate or market penetration index (MPI) measures the performance of the subject hotel in comparison to its competitive set. This is critical to understand, as many management-contract incentive structures are tied to this indicator. Selecting the wrong competitive set can swing MPI metrics in vastly different directions, with potentially costly repercussions.
- Employee productivity is another key indicator asset managers analyze, focusing on whether onsite labor is efficient and maximally productive. Asset managers will review the time it takes housekeeping to clean a guestroom, evaluate staffing levels within various departments based on peak usage times, and identify training needs to increase nimbleness across departments.
- Guest service scores and net promoter scores are also important indicators analyzed by hotel managers, franchisors, and asset managers. Certain aspects of guest service scores are better managed by the day-to-day operator of the hotel; however, items relating to the physical wear and tear of the building or brand shortfalls are better controlled from an asset-management perspective because they involve direct coordination with ownership and/or the franchisor.
- The final key performance indicator for hotel asset managers to consider is the cost of sales, or the cost incurred to generate the hotel's revenue. These costs might include marketing expenses, distribution channel charges, and/or travel agent and third-party sales commissions. Careful review of these expenses, maximizing the obligations of the brand (if applicable), and vendor management are crucial to monitoring and managing the cost of sales.

Complexities within the highly nuanced hotel real estate sector require the attention to detail that only a hotel-specific asset management company can provide. However, even within the hotel industry, the expertise of one firm may not align with the strategic vision or financial goals for your specific investment.

When selecting an asset management firm, remember that it is imperative to enter a professional relationship with a firm you trust and that intimately understands your investment objectives. The best firms will have a high level of financial acumen, will work with you to develop a customized approach to asset management, and will keep you informed on the general health of your investment from both macro and micro perspectives.

Hotels are highly complicated investments that enter into daily leases, unlike other types of commercial real estate. The management of this type of multi-faceted property requires oversight from highly skilled industry professionals who can leverage their experience and market positioning to help owners realize operational success. The right hotel asset management firm will have a strong reputation in the market and will demonstrate a commitment to your success through trustworthy, proactive, and responsive communication.

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