Weighing Up the Options: Franchise, Management Agreement, or Third-Party Operator?

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Choosing a hotel operating model is a major decision and one size certainly doesn't fit all. **Hala Matar Choufany**, president of **HVS Middle East and Africa**, has the insights that hotel owners need to make their evaluations and selections, with a view to optimizing returns.

Hotel management is complex, with the value of the property highly dependent on the operating performance of the asset and the achievable earnings before interest, taxes, depreciation and amortization (EBITDA) levels. As such, evaluating the most suitable hotel operating model for a hotel investment is crucial to ensure that the owner's return is optimized. There is no single model that fits all; hotel owners should therefore investigate, evaluate, negotiate and assess, to find the most suitable operating model and brand that will allow them to successfully operate in the ever-changing hospitality market.

Changing Market Dynamics

A recent HVS survey on global operators in the Middle East revealed that 84 percent of branded hotels operate under management agreements, 11 percent under franchise agreements and 5 percent as leased properties. However, franchise agreements are rising, accounting for 20 percent of new signings, and this trend is set to continue. Mature markets, such as the US and Europe, see a higher prevalence of franchise models – 70 percent and 40 percent respectively – compared to 25 percent in Africa and 20 percent in the Middle East.

Given these trends, there's much to be gained from analyzing how franchise agreements and management contracts work in detail, and the emerging role of third-party operators.

Franchise Agreements: On The Rise

Franchise agreements have gained traction in mature markets like the US and Europe, and are steadily increasing in popularity in the Middle East. By 2025, they are expected to account for 25 percent of hotel agreements in the region. This growth reflects owners' confidence in their ability to control costs and enhance asset value, particularly in emerging or secondary markets. Operators also benefit by expanding their brand presence, while reducing financial risks.

Franchise agreements typically last 10-15 years, with franchisors retaining termination rights if brand standards are not met. Owners gain access to brand recognition, marketing resources and operational support. However, these benefits come at a cost: franchise fees rank among the highest operating expenses after payroll. These fees usually include an upfront payment and ongoing charges for using the brand's name and marketing and reservation systems.

When choosing a franchise affiliation, brand attributes and the structure of franchise fees are critical considerations. While franchise agreements allow owners greater operational control, they must maintain brand standards, often necessitating experienced management teams or the hiring of third-party operators.

Hotel Management Agreements: Balancing Risk and Reward

Management contracts dominate in the Middle East, historically favored by owners and operators alike. The GCC region has seen substantial growth in upscale and luxury hotels under management agreements, with increasing

Summary

Choosing the right hotel operating model (franchise, management agreement, or third-party operator) depends on owner goals, market conditions, and property characteristics. Franchises offer brand support but require strict standards. Management agreements, common in the Middle East, balance risk and reward. Third-party operators provide flexibility and cost efficiency. Owners must evaluate options to maximize returns as market dynamics shift.

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interest in midscale and economy brands over the past five years.

These agreements have evolved to balance risk and reward between owners and operators. As owners become more sophisticated, employing asset managers and consultants, they negotiate terms that offer flexibility and control. Key changes in modern management agreements include:

1. Shorter contract terms – contracts are becoming shorter, with options to transition to franchise models. This offers owners increased flexibility and control over their properties.
2. Evolving tiered fee structures – base and incentive fees are structured to align operator incentives with achieving performance benchmarks, such as adjusted gross operating profit (AGOP) and net operating profit (NOP). Incentive fees are expected to increase for operators who achieve strong AGOP levels, while base fees have been steadily declining.
3. Enhanced budget approvals and performance tests – owners now have greater influence over budget approvals. Stricter performance tests ensure that operators remain accountable and meet predefined thresholds.
4. Diminished area of protection (AOP) – the significance of AOP clauses has lessened, with owners focusing more on shorter terms and fees linked to profitability metrics.
5. Stronger exit strategies and termination rights – owners place greater emphasis on exit strategies, leading to stricter and more enforceable performance test thresholds. This provides added security in cases of underperformance.
6. Key money contributions – operators are increasingly offering upfront financial incentives, especially for strategic assets in prime locations, as part of their bid to secure management agreements. These developments reflect a growing demand from hotel owners for better control mechanisms, flexible exit options and greater alignment of operator incentives with property performance.

Third-Party Or White-Label Operators: Welcome flexibility

Already well established in North America and rapidly growing in Europe, third-party operators are gaining traction in the Middle East, Asia-Pacific and Africa. These operators manage hotels on behalf of owners, operating as independent properties or under franchise agreements. Their appeal lies in their flexibility, competitive fee structures and shorter contract terms compared to branded operators.

Third-party agreements typically involve lower base and incentive fees, shorter initial terms (5-10 years), and more flexible exit options, such as termination at will. They are especially suitable for independent hotels or franchised properties, where owners lack operational expertise.

The key advantages of third-party operators are:

- flexibility – unlike branded operators, third party firms adapt more easily to owners' specific needs and property characteristics
- owner influence – owners retain greater control over operations, while benefiting from professional management
- portfolio management – for owners with multi-brand portfolios, a single third party operator simplifies reporting and performance comparisons
- value addition – flexible management agreements enhance the property's marketability.

Strategic evaluation required

Choosing the right operating model – franchise, management agreement or third-party operator – will largely come down to three key factors: what the owner's goals are; the market conditions; and the characteristics of the property. Franchise agreements offer brand support and operational control, but require adherence to strict standards. Management agreements provide a comprehensive operational framework, but may need adjustments for modern ownership demands. Third-party operators combine operational flexibility with professional expertise, making them especially suitable for independent or franchised properties. As the hospitality landscape evolves, hotel owners must strategically evaluate their options to maximize returns and adapt to market dynamics.

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www.hospitalitynewsmag.com*, features essential market insights, analysis and guidance from experts in the field, in addition to special reports on the latest concepts and interviews with top international names in the sector. Widely regarded as a must read, the magazine has built a solid reputation as a reference for hospitality professionals in the Middle East and beyond. Daily news bulletins can be found* ***online****.*

About Hala Matar Choufany

Hala is an experienced Regional President and Managing Partner, an industry expert, and is recognized as one of the most influential leaders in the hospitality industry, notably in the Middle East and Africa region.

Hala has advised on more than 5,000 hospitality and mixed-use projects in the last 20 years across Europe, the Middle East, Africa and Asia. She has advised clients in areas such as Valuations, Acquisitions, Asset Management, Strategic investments and development, Contract Negotiations, and general Real Estate Strategic Advisory.

Hala has authored more than 50 publications and speaks frequently at investment and hospitality related conferences on a range of topics including asset valuation, investments, management issues and women leadership.

In addition to being a Board Member of HVS Global, Hala sits on the Boards of Harvard Business School Club of the GCC, Hotel Investment Advisory Board, and is regularly invited to Boards as a subject matter expert in the industry. Hala is frequently invited to discuss hotel and tourism trends on major news channel including Alarabiya, Bloomberg, Abu Dhabi TV, Forbes, Breaking Travel News and CNN.

Hala is also a member of the International Society of Hospitality Consultants (ISHC).

Hala completed Executive Education at Harvard Business School. She also holds an MBA in Finance and Strategy from IMHI (Essec- Cornell) University, Paris, France and a BA in Hospitality Management from Notre Dame University, Lebanon. Hala is fluent in English, French and Arabic.

Born in Beirut, Hala lived and worked in several cities across Europe, Asia and Middle East and is a mother of three.

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