As Seen In Hotel Business® Green Book 2018

brokers report

What's on the horizon for the transactions market? Joseph Kennedy, president, Crystal Investment Property LLC; Steve Kirby, managing principal, Mumford Company; Peter Nichols, VP/national director, National Hospitality Group, Marcus & Millichap; and Chuck Nester, president, Brown Nester Hospitality Services Inc., shared the details with *Hotel Business.*

—Nicole Carlino

How would you characterize the 2017 transactions market, and what can we expect next year?

Kennedy: The market in 2017 has been extremely robust and we see no signs of deal activity slowing in the Pacific Northwest.

Kirby: In 2017, transactions were typically fewer and smaller across the U.S. The midmarket and select-service sectors were less severely impacted due to continued purchaser demand for those product types. One interesting issue was that transactions were lessened not by lack of buyer demand but by the available supply of hotels on the market.

Next year will likely be similar to this in the first half, while transactions levels should begin picking up later in the year as operators begin the debate of "renovate or trade." As more supply enters the markets and franchisors become more demanding, more sellers will likely choose to exit and trade their asset. Tax reform may indeed open the floodgates to sellers, leading to a significant availability of properties offered for sale.

Nichols: The overall transaction market has improved during the second half of 2017 after a somewhat slow start to the year.

Nester: This year represented a leveling off in all categories. We have seen a good 24 months of strong recovery and stabilized revenues and NOIs. Next year will bring occupancy and RevPARs on a slow decline. The cycle is changing and will be a major factor in values in the oncoming year.

Who has the upper hand heading into 2018: buyers or sellers?

Kennedy: Sellers do, due to very tight supply. However, we aren't seeing buyers overpaying, and both lenders and appraisers are being conservative about overstating value or future projections.

Kirby: Sellers will continue to hold the reins moving into 2018, but that will likely lessen in the later months as debt costs increase and markets begin greater absorption of new supply with limited demand increase.

Nichols: It really depends on the individual market at this point. Strong, well-performing markets continue to hold significant upside, while markets experiencing significant increases in new supply may face some headwinds during the next 12-24 months. That said, the overall market metrics continue to be strong, with balanced supply and demand increases, available capital and low interest rates. Now is an excellent time to enter the market or rebalance a portfolio.

Nester: We did not see a buyers' or sellers' market over the last 24 months. Buyers will have the upper hand, with lenders and appraisers dictating how transactions will be structured. Sellers still will be stubborn, asking above market prices. As owners need to be sellers, prices will begin to come more in line with lenders' views. Too many sellers are waiting for proposed tax changes that, in my opinion, will not affect savings on sale. Capital Gains tax will stay at the 15% market for some time.

What hotel segments do you expect will exhibit the greatest churn?

Kennedy: There is such a broad market for assets across the various classes that we see investors ready to move into almost anything that hits the market. Cash flow and debt service is key, and smaller boutique properties have a more limited appeal.

Kirby: Mid-market and economy segments will always yield the largest number of trades due to the sheer volume of product and buyer demand at this level, but upper-midscale transactions should be more active in the new year.

Nichols: There is typically a higher turnover rate in the smaller select-service assets; however, market specifics also play a key role in the buy/sell/hold decision.

Nester: Mostly midscale and economy because the franchisors are pushing once again for costly design upgrades, and many properties will not be able to afford or finance the upgrade costs, leaving many sellers with the dilemma: how to sell with no flag available on sale or PIPs that will choke the buyer to stay with the existing flag. This will make the sale cash costs and financing too high to have respectable return on investment, thus forcing the prices to decline.

What do you see people coming to buy/invest in?

Kennedy: Upper-midscale, select-service branded properties in good locations.

Kirby: As more of the newer branded products open, many of those products will sell. Investors have an appetite for novel product types that fit into the various niche submarkets. Trading should continue to be active at the lower and midrange product type.

Nichols: Investors, in general, continue to exhibit measured optimism in the marketplace, with capital following market opportunities. Different types of investors are entering a variety of property types based on specific investment and return criteria.

Nester: Buyers will be experienced hoteliers looking for historical revenue streams with no projected new product in their competitive sets. Franchise issues on sale and new flag PIPs will affect all markets, segments.

Words of advice?

Kennedy: Be ready to act quickly. Have financing and franchise relationships in line and be ready to move forward decisively when a property becomes available. Recognize the long-term value of an acquisition; don't lose out over minor negotiation amounts—tripping over dollars to pick up dimes doesn't work in this market.

Kirby: Sell the lesser-branded and noncore assets sooner than later as higher debt cost may erode pricing. Don't be afraid to take the profits and pay the taxes if you can't find a suitable replacement. Opportunities to deploy those gains may be more attractive over the next 18 months.

Nichols: Looking back on 2017, careful, disciplined investors will be the biggest winners; 2018 looks to be a strong year for hotel performance—and as it continues to remain positive, investors will continue to find deals that are accretive to their portfolios.

Nester: Buyers: Stay within your price means. Sellers: Be realistic in your value—would you buy your own property at what you are offering?

Joseph Kennedy
Crystal Investment Property LLC

Steve Kirby, Mumford Company

Peter Nichols. Marcus & Millichap

Chuck Nester, Brown Nester Hospitality Services Inc.