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Exploring the profitability of soft brands

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Myriad options exist when choosing whether to franchise or remain independent and look for marketing support. A cost-benefit analysis is a critical step.

Highlights

- The trick is finding the right approach for each individual asset.
- Taking a hard look at the asset is the first step.
- Determining an ROI for the various options is complicated.

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GLOBAL REPORT—Hotel owners have an increasing amount of options when it comes to finding sponsorship and operating support. The surface-level decision of whether to become part of a franchise or remain independent is only the first step.

Several franchisors—realizing there is a significant amount of travelers who aren't looking for the cookie-cutter experience—in recent years have introduced quasi-brand options, such as Marriott International's Autograph Collection and Choice Hotels International's Ascend Collection.

However, the soft brand strategy has been an option for quite some time. Representation companies like Preferred Hotel Group and Leading Hotels of the World offer sales-and-marketing support for a fraction of the cost of flying a flag.

There are several factors to consider when making these difficult decisions. The trick, experts said, is finding the right approach for each individual asset.

"There is a right approach for each property. Maybe more than one," said Eva Hill, president of Britannia Pacific Properties, which recently deflagged a Palm Beach, Florida, hotel from the Ritz-Carlton system and chose to remain independent as the Eau Palm Beach Resort & Spa. "In certain situations it makes sense to have a brand, and in this particular case, when faced with the fact that we're going to be running the hotel, we decided independent was the best alternative."

The Eau Palm Beach Resort & Spa later joined the Preferred Hotels & Resorts collection.

"What we found appealing about Preferred is the company that they keep," Hill said. "They provide marketing and soft branding for a number of luxurious hotels. They provide the flexibility for hotels with unique selling points to be marketed as well as provide strong standards to minimum levels of service and quality.

"Preferred has expertise in other countries as well, which we thought would be beneficial."

Britannia Pacific is part of a parent company based in the United Kingdom that owns 20 hotels, including three in the U.S. Other than the Eau Palm Beach, Britannia owns and operates an independent luxury boutique that is not part of any collection and also a franchised and branded property.

Weighing options

Taking a hard look at the asset is the first step in determining the right fit, sources said. Location is important. Also key is evaluating the attributes of available brands in the particular segment and determining whether one would complement the asset.

In addition, owners and managers should identify the hotel's target traveler.

"It really does start with the owner and ownership and what their intent is," said Robert Van Ness, executive VP of the Americas at Preferred Hotel Group. "It depends what they want and how much they want to participate (in the operations)."

Van Ness said some owners look at hotels as real estate investments while others want to get their hands dirty and be involved in the hospitality component of the business. He said brands can limit the amount of creativity an owner can have.

"Not everyone wants to be told what to do and instead wants be more involved and more entrepreneurial," he said. "That's someone who might enjoy an affiliation and partnership as opposed to be hard-flagged."

Joining a large hotel franchisor does detract from a property's independence and dilutes creativity, said Philip Truelove, GM of The Greenwich Hotel, actor Robert De Niro's 88-room independent hotel in the Tribeca neighborhood of New York. The Greenwich is part of the Leading Hotels of the World collection.

When The Greenwich opened five years ago, Tribeca wasn't as popular a destination for travelers as it is today. Therefore, introducing an independent hotel to the market would be harder than it would be for a branded property, Truelove said. With a sales-and-marketing background, Truelove said he and De Niro wanted to "introduce our hotel and Tribeca to the whole world."

"We needed a support network to do that; we felt that we needed to put a standard on the hotel and introduce ourselves," he said. "While we certainly considered the other groups, I knew Leading Hotels and we felt it was a good fit. What it has done for us, as well as stamping a seal of approval and setting a certain standard, it also has opened a large sales-and-marketing world."

Data-driven decisions

Savvy hotel owners should use a cost-benefit analysis to determine the right fit for their property. On average, joining a soft brand tends to cost a bit less. Preferred, for example, charges 3.7% of rooms revenue, Van Ness said, while major hotels chains charge anywhere from 4% to 14%, according to HVS's U.S. Hotel Franchise Fee Guide.

However, determining a return on investment for the various options is complicated.

According to data collected by STR Analytics, sister company of Hotel News Now, branded hotels in general report a higher occupancy, while independent hotels garner a higher average daily rate and revenue per available room.

STR Analytics recently evaluated a large sample of data from its HOST Almanac report regarding U.S. hotels (about 180,000 rooms) in the upper-upscale segment and was able to compare certain metrics for branded and independent properties. For the full year 2012, occupancy at the chain-affiliated hotels was 70.7%; ADR was $140.89 and RevPAR was $99.57. The independent sample reported 64.8% occupancy; $171.91 ADR and $111.47 RevPAR.

The chain-affiliated hotels reported spending 7.8% of their operating expense budget on marketing and an additional 3.4% on franchise fees. Independent hotels on average spent 7.1% of their operating expense budget on marketing fees and were able to avoid franchisee fees.

House profit (departmental expenses and operational expenses subtracted from revenue) at the chain-affiliated hotels was 31.9% compared with 30.4% at the independent properties.

STR Analytics' sample size of chain-affiliated hotels (163,262 rooms) was more robust than the independent sample size (22,117 rooms). Also, STR Analytics did not break out independent hotels affiliated with soft brands versus those that weren't.

2012 key metrics: brand vs. independent

	Branded upper upscale	Independent upper upscale
Sample size (# of rooms)	163,262	22,117
Total occupancy	70.7%	64.8%
Average rate	$140.89	$171.91
RevPAR	$99.57	$111.47
Total revenue	$8 billion	$1.4 billion
Revenue per occupied room	$190.76	$273.97
Total departmental expenses	$3.1 billion (38.4%)	$605.7 million (42.6%)
Total operating expenses	$2.4 billion (29.7%)	$383.2 million (27%)
- Marketing	$626.3 million (7.8%)	$100.7 million (7.1%)
- Franchise fees	$273.13 million (3.4%)	$0
House profit	$2.6 billion (31.9%)	$431.8 million (30.4%)

Source: STR Analytics (HOST)

"Independent hotels generally have lower occupancies since they lack the marketing power of brands, but they often compensate with higher ADRs," said Steve Hennis, director at STR Analytics. "However, different management approaches could have an even bigger effect than branding when comparing two hotels."

"Chain properties are really taking a hard look at the ROI (of joining a brand) and determining what else is out there," Van Ness said. "Can I do better running this property as an independent? Owners are having more and more of those types of conversations."

Measuring ROI

When evaluating the ROI of each option, the most obvious measurement is how much demand is being driven through those particular channels.

Britannia's Hill said ownership will measure the value of joining Preferred by way of exposure through sales and booking channels. "And exposure in new markets—geographic as well as customer demographics," she said.

The fact that representation companies have strong ties to other travel associations, such as American Express Travel and Virtuoso, is a positive for sales-and-marketing efforts.

"The most obvious (measurement tool) is to see how many reservations are coming through the system," Truelove said. "We can measure how much traffic comes from their office and their website, especially from different parts of the world. Certainly every year we look at those numbers."

Van Ness said owners ultimately have the option of joining a brand that's going to tell them how to operate their property or—on the other end of the spectrum—just connect to travel agents through a global distribution system and hope to drive enough demand on their own.

Soft brands "fit nicely in the middle," he said. "Ours is much more of a partnership. Our fees are performance based, and our contracts are three to five years in length."