



HVS STUDY

Preferred Hotels & Resorts

SUBMITTED TO:

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Executive Summary

HVS was retained by Preferred Hotels & Resorts (“PHR”) to evaluate a sample of its affiliated hotels in the context of the North American lodging market. We selected the seventeen PHR properties that entered the PHR program in 2015 to quantify the effect of joining PHR. We reviewed the hotels’ performance over the period from 2016 through 2018. We herein present our findings for the last three years of data for the selected hotels.

EXECUTIVE SUMMARY - PHR HOTEL PERFORMANCE

	2016	2017	2018	Percent Change
Preferred Hotels & Resorts Properties				
Occupancy	69.8 %	70.3 %	69.5 %	(0.5) %
Change	(3.2) %	0.7 %	(1.1) %	
Occupancy Penetration	93.6	97.3	94.1	0.5 %
Average Rate	\$229.03	\$236.41	\$249.62	9.0 %
Change	2.6 %	3.2 %	5.6 %	
Average Rate Penetration	96.4	100.2	105.3	9.3 %
RevPAR	\$159.94	\$166.19	\$173.46	8.5 %
Change	(0.7) %	3.9 %	4.4 %	
RevPAR Penetration	90.2	97.5	99.1	9.8 %

The selected set of hotels shows a major improvement over the three-year period. Both RevPAR and ADR increased by 8.5% and 9.0%, respectively, but more importantly, the ADR and RevPAR penetration figures experienced nearly 10% increases over the three years. ADR penetration exceeded the market average after two full years with PHR, and RevPAR penetration approached the market average by the third year. The benefit of affiliating with PHR is shown in the penetration- and percentage-change figures. We note that occupancy remained relatively flat during the period shown; however, this was in line with the Peer Properties, major markets, and national statistics for occupancy.

Methodology and Scope of Work

In developing this study, we have relied on information provided by STR Analytics, which assembled occupancy, average rate, and RevPAR data, in aggregate, for the following:

- A group of 17 PHR-affiliated hotels in North America
- All hotels identified as competitors by the PHR-affiliated hotels (“Peer Properties”)
- All hotels in the 25 major markets in the U.S., as defined by STR
- All hotels in the U.S.

We have also relied on our internal database of information that was prepared for the *2018 U.S. Hotel Franchise Fee Guide*, published by HVS.

Preferred Hotels & Resorts

Preferred Hotels & Resorts (“PHR”) is a global hospitality company based in Newport Beach, California. PHR encompasses four- and five-star, full-service hotels and resorts, predominantly classified as luxury hotels and including iconic properties. It is classified as a “soft” brand, essentially comprising individual hotels that operate under the PHR umbrella. Like traditional hotel brands, soft brands provide affiliates with reservation systems and connectivity, sales support, and other marketing and operational support systems, such as a frequent guest program. Soft brands require that affiliated properties meet defined quality operational standards, but typically do not mandate specific facility, design, or operational criteria. As a result, hotels affiliated with soft brands usually maintain a distinct identity and offer an array of facilities, amenities, and services as appropriate to the location and market.

The services and support that PHR provides to its affiliated hotels include reservation management systems, integrated marketing and communications, the I Prefer loyalty program, sales support, representation at trade shows and events, quality assurance, and group purchasing.

The Peer Properties

For the purposes of this study, the Peer Properties were aggregated using the individual hotels’ STAR competitive sets. These properties are selected at the property level by ownership/management and must fulfill the minimum STR reporting requirements. HVS staff members evaluate STAR competitive sets on a regular basis in the course of our appraisal and consulting work. These sets are compiled at the discretion of the property representatives that often have motivations for presenting their hotels against specific comparables to reach incentive or compensation thresholds; however, on average, HVS finds that the majority of comparable sets represent an adequate snapshot of the market and subject property performance. We also note that providing this data in aggregate

form diminishes any bias within the individual comparable STAR reports. The following table sets forth the profile of the hotels that comprise the Peer Properties, based on chain scale, as defined by STR.

Overall Performance Review

FIGURE 1 PROFILE OF THE PEER PROPERTIES, BY CHAIN SCALE

Chain Scale	Number of Properties		Number of Rooms	
	Total	Percent of Total	Total	Percent of Total
Luxury	36	36.4 %	7,064	33.5 %
Upper Upscale	50	50.5	11,604	55.0
Upscale	12	12.1	2,333	11.1
Upper Midscale	1	1.0	101	0.5
Total	99	100.0 %	21,102	100.0 %

Most of the Peer Properties are classified as luxury or upper-upscale hotels by STR; together, these classifications account for 87% of the hotels and 89% of the guestroom inventory. Peer Properties in the luxury segment include hotels affiliated with Four Seasons, Hyatt, Marriott, Omni, and Loews, as well as numerous iconic hotels and resorts. The predominance of luxury and upper-upscale properties within the peer set reflects the overall quality of the hotels affiliated with PHR. Approximately 13% of properties are classified as upscale and upper-midscale, and many of these properties are located in secondary markets.

The following table sets forth the profile of the hotels that comprise the Peer Properties based on brand or hotel company. We were provided with the aggregate data grouped by parent company, rather than a detailed list of individual hotels.

FIGURE 2 PROFILE OF THE PEER PROPERTIES

Brand	Number of Properties		Number of Rooms	
	Total	Percent of Total	Total	Percent of Total
Marriott International	26	55.3 %	5,969	51.2 %
Hilton Inc.	11	23.4	3,350	28.8
InterContinental Hotels Group	4	8.5	936	8.0
Hyatt	6	12.8	1,396	12.0
Total	47	47.5 %	11,651	54.4 %
Other Brand*	13	21.7 %	3,084	26.5 %
Total Branded	60	60.6 %	14,735	68.8 %
Independent	39	39.4 %	6,686	57.4 %
Total Competitive Sample	99	100.0 %	21,421	100.0 %

* "Other brand" includes Rosewood, Loews, Wyndham Hotels and Resorts, Omni, and other boutique-style brands.

Note: STR does not specifically track affiliations with Leading Hotels of the World, World Hotels, Small Luxury Hotels or other soft brands.

A majority of the Peer Properties are affiliated with a brand; in aggregate, 60.6% of the hotels and 68.8% of the guestroom inventory are affiliated with a hotel chain. Moreover, slightly under half (47.5%) of the hotels and approximately 55% of the room inventory operate under Marriott, Hilton, InterContinental Hotels Group, and Hyatt brands. Over 20% of the hotels are affiliated with smaller brand such as Omni, Loews, and Rosewood.

Approximately 39% of the hotels are classified as “independent.” This category includes hotels that may be affiliated with other soft brands, such as Leading Hotels of the World, WorldHotels, and Small Luxury Hotels of the World, as well as properties that operate independent of any affiliation. As STR Analytics does not currently track all soft-brand affiliations, it is not possible to further subdivide this category based on the data we received.

The first category, which includes the larger brands, is generally viewed as the one with the strongest brands in the U.S. in terms of market presence and room-night delivery. Each brand is characterized by a well-recognized market image, wide geographic distribution, a strong reservation system, well-established sales and marketing functions, and a popular frequent guest program. Based on these attributes, properties affiliated with these brands are generally considered less vulnerable to macro-economic fluctuations, although individual properties can have significantly different experiences depending on property- and market-specific circumstances. The predominance of these brands among the Peer Properties suggests that, in aggregate, the PHR properties have had to operate in a highly competitive market.

Overview of the U.S. Lodging Industry through and after the Recession

The onset of the recession in December 2007 first became evident in lodging trends in the spring of 2008 and accelerated in the fall of 2008, as both corporate and consumer spending fell substantially in the wake of the financial crisis. The U.S. lodging market recovered quickly from the downturn. After years of steady occupancy and average rate growth, many markets across the United States are stabilizing as new supply continues to enter, and demand growth slows.

For the purposes of this study, we have focused on the recent data. From 2016 through 2018, occupancy remained relatively flat, and average rate (ADR) grew at over 2%. This stable occupancy trend, coupled with ADR growth, resulted in a national RevPAR of \$81.19 in 2018. However, the revenue per available room (RevPAR) has reached record highs in many markets across the country. The national occupancy and ADR growth rates have slowed in recent years, as supply growth has become more prevalent in markets across the country. Most analysts agree the national lodging market is approaching its peak.

STR Analytics Data

STR Analytics has compiled performance data for the hotels that are affiliated with PHR, as well as for the hotels identified as Peer Properties. Data for the 25 major lodging markets in the U.S. and for the overall U.S. lodging industry were also provided. The statistics include occupancy, ADR, and RevPAR, which is calculated by multiplying occupancy by ADR and provides an indication of how well rooms revenue is being maximized. The data were provided to us in aggregate form, as set forth in the following table.

STABLE REVPAR GROWTH: 2016–2018

The PHR properties that entered the system in 2015 were evaluated for their change in RevPAR penetration over the three-year period following their affiliation with PHR. We compared the aggregate of these hotels' RevPAR to the industry averages, on a national level, the top 25 markets, and the Peer Properties for these hotels. The performance of the PHR hotels outpaced the 25 major markets' and overall U.S. lodging industry's in both occupancy and ADR during the period shown.

The PHR hotels recorded strong, positive trends in both the amount and the pace of RevPAR growth. The RevPAR of the PHR hotels remained lower than that of the Peer Properties during the illustrated period. However, the RevPAR of the PHR properties grew by 3.9% in 2017 and 4.4% in 2018, while the Peer Properties experienced negative growth in RevPAR in 2017 and less than 3% growth in 2018. The overall RevPAR penetration levels achieved by the PHR hotels grew in 2017 and eventually neared 100% in 2018. The total RevPAR increase during the three-year period shown is highest for the PHR properties.

Overall, there was an upward trend in performance after the selected hotels became affiliated with PHR, relative to the performance of the larger set and the Peer Properties.

FIGURE 3 PERFORMANCE

	2016	2017	2018	Percent Change
Preferred Hotels & Resorts Properties				
Occupancy	69.8 %	70.3 %	69.5 %	(0.5) %
Change	(3.2) %	0.7 %	(1.1) %	
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Change	(0.7) %	3.9 %	4.4 %	
RevPAR Penetration	90.2	97.5	99.1	9.8 %
Aggregate Peer Properties				
Occupancy	74.6 %	72.3 %	73.9 %	(1.0) %
Change	(1.2) %	(3.1) %	2.2 %	
Average Rate	237.57	235.92	236.98	(0.3) %
Change	0.4 %	(0.7) %	0.4 %	
RevPAR	177.24	170.53	175.06	(1.2) %
Change	(0.9) %	(3.8) %	2.7 %	
U.S. Major Markets				
Occupancy	62.9 %	63.7 %	62.6 %	(0.5) %
Change	0.3 %	1.3 %	(1.7)	
Average Rate	\$145.66	\$149.42	\$152.52	4.7 %
Change	1.4 %	2.6 %	2.1 %	
RevPAR Change	\$102.45	\$108.47	\$110.97	8.3 %
Change	8.4 %	5.9 %	2.3 %	
Total U.S. Lodging Industry				
Occupancy	52.8 %	54.0 %	54.1 %	2.5 %
Change	(0.4) %	2.3 %	0.2 %	
Average Rate	\$119.22	\$122.05	\$124.28	4.2 %
Change	2.6 %	2.4 %	1.8 %	
RevPAR Change	\$74.28	\$78.67	\$81.19	9.3 %
Change	8.1 %	5.9 %	3.2 %	

Source: STR Analytics

The selected set of hotels shows a major improvement over the three-year period. Both RevPAR and ADR increased by 8.5% and 9.0%, respectively, but more importantly, the ADR and RevPAR penetration figures experienced nearly 10% increases over the three years. Average penetration exceeded the market average after two full years with PHR, and RevPAR penetration approached the market average by the third year. The benefit of affiliating with PHR is shown in the penetration- and percentage-change figures. We note that occupancy remained relatively flat during the period shown; however, this was in line with the Peer Properties, major markets, and national statistics for occupancy.

Cost-Benefit Consideration

The cost of membership in a hotel brand is also an important consideration. To evaluate the costs associated with a PHR affiliation in the context of the Peer Properties, we reviewed the database prepared for the *2018 U.S. Hotel Franchise Fee Guide*.

Based on a pro-forma forecast of income and expense for a typical full-service hotel, we have calculated the royalty fees and the aggregate marketing, advertising, sales, miscellaneous, and initial fees for the hotel brands that comprise a significant portion of the Peer Properties. The same calculations have been made for PHR hotels using the average for Preferred Hotels & Resorts. This methodology is consistent with that employed in the preparation of HVS's *2018 Hotel Franchise Fee Guide*. The following chart presents the results of these calculations.

FIGURE 4 AVERAGE AFFILIATION COSTS AT MAJOR HOTEL COMPANIES AND PREFERRED HOTELS & RESORTS

Affiliation	Percent of Gross Rooms Revenue (Brand Average)					
	Royalty Fee	Marketing Fee	Loyalty Fee	Sales Fees	Misc. Fees	Initial Fees
Hyatt	5.1%	1.2%	1.6%	1.5%	2.1%	0.1%
Marriott	5.4%	1.5%	1.7%	1.9%	1.1%	0.1%
Hilton	5.4%	1.9%	2.1%	2.2%	1.2%	0.1%
IHG	5.1%	1.5%	1.8%	3.0%	1.8%	0.1%
Preferred Hotels & Resorts	0.4%	0.1%	0.1%	0.8%	0.0%	0.0%

Based on the pro-forma forecast, the average annual fees payable by hotels that operate under a PHR affiliation equate to 1.4% of rooms revenue. By comparison, the average of the major hotel companies' franchise fees reviewed in the above chart require significantly higher fees, both as a dollar amount per room and as a percentage of rooms revenue. According to representatives of PHR, sales fees are

assessed only on those reservations that pass through the PHR central reservations system.

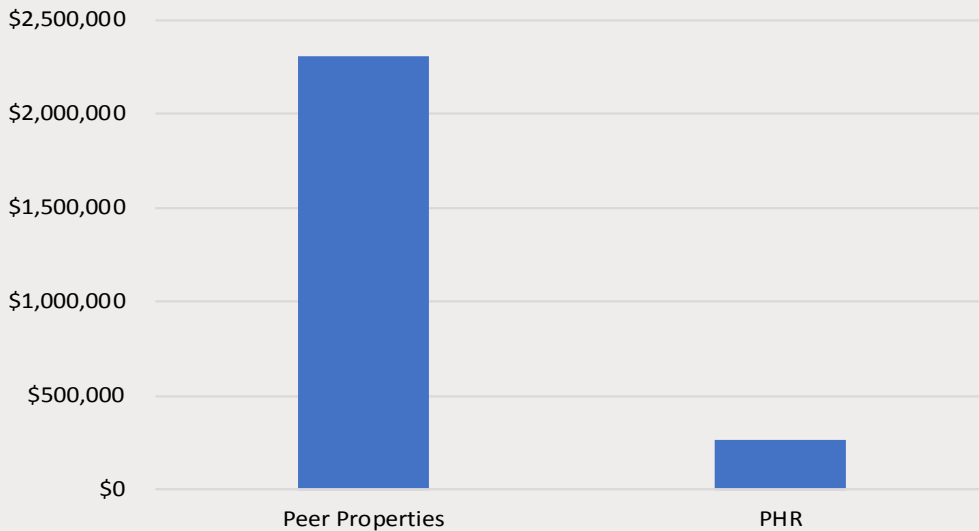
The following chart summarizes the range and average fee structure indicated by the data used for the *2018 Hotel Franchise Fee Guide*.

FIGURE 5 AFFILIATION COSTS, AS A PERCENTAGE OF TOTAL ROOMS REVENUE

	Royalty Fees to Rooms Revenue	Sales Fees to Rooms Revenue	Marketing Fees to Rooms Revenue	Loyalty Fees to Rooms Revenue	Misc. Fees to Rooms Revenue	Initial Fees to Rooms Revenue	Total
Luxury & Upper-Upscale Brands <i>Average</i>	4.1% - 6.9% 5.3%	0.2% - 3.3% 1.9%	0.0% - 3.3% 1.9%	1.0% - 2.5% 1.9%	0.0% - 4.8% 0.9%	0.0% - 0.1% 0.1%	12.0%
Upscale Brands <i>Average</i>	2.6% - 6.0% 5.1%	0.3% - 4.0% 2.0%	0.8% - 2.5% 1.6%	0.0% - 2.5% 1.6%	0.1% - 3.0% 1.3%	0.1% - 0.2% 0.1%	11.7%
Preferred Hotels & Resorts	0.4%	0.8%	0.1%	0.1%	0.0%	0.0%	1.4%

For the PHR hotels, the total marketing and sales fees equate to 0.9%, while the loyalty fees equal 0.1% of rooms revenue; these levels are below the average indicated for the other brands. Particularly, the difference in the royalty fee is striking. The royalty fee of 0.4% of total rooms revenue is substantially lower than the royalty fees payable under the other brands, which range from 2.6% to 6.0%. Additionally, most brands require miscellaneous fees related to technology support, training programs, national and regional annual conferences, and so on; however, PHR charges no such fees to the affiliated hotels.

FIGURE 6 FRANCHISE COSTS COMPARISON



*The Chart assumes 300-property with average RevPAR in 2018

For the purposes of illustration, using the 2018 RevPAR for both the PHR hotels' average (\$173.46) and Peer Properties' average (\$175.06), the total franchise cost for a 300-room hotel would be \$266,000 (rounded) per year for a PHR hotel, as compared to \$2,307,000 (rounded) per year for a Peer Property (12% franchise cost). While this substantial difference is not universal across all properties, as these figures are presented in averages, the average franchise cost for a national brand is over nine times the affiliation cost of PHR hotels.

We hereby certify that we have no undisclosed interest in the subject of this study, and our employment and compensation are not contingent upon our findings and conclusions.