

Chris Tinning & Company

Hotel – Motel Brokers, Auctioneers and Consultants

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The Hotel Marketplace (Country NSW).....

Who knows what price a hotel will sell for?

There are a reasonable number of hotels on the market including Receivership properties, freehold and leasehold hotels. There is a lack of “Blue Ribbon” or “A” class provincial city hotels genuinely offered for sale.

Precious few sales make it difficult to draw comparisons in the market. Discussions with other brokers indicate that whilst there appears to be enquiry for purchasing hotels – there is a lack of purchaser commitment.

Bankers are indicating that they are still interested in financing hotels – although the lending ratios are closer to traditional levels (50 – 60% LVR [loan to value ratio] on Freeholds ... 30% LVR on traditional Leaseholds).

Hotel valuers are indicating a drop in values and indeed this perception is carried through the media (eg. SMH 17-8-09 The pubs with no buyer: hotel values in the cellar <http://business.smh.com.au/business/the-pubs-with-no-buyer-hotel-values-in-the-cellar-20090816-embm.html>)

(<http://business.smh.com.au/business/slump-in-pub-values-pushes-ing-property-fund-to-the-brink-20090830-f40q.html>)



It has been suggested that the record prices seen through 06-07-08 were an anomaly (a bubble in the market) fed by the arrival of “corporate” styled hoteliers who believed that the EBITDAE (earnings before interest, taxation, depreciation, amortisation and exceptional items) calculated by Brokers, Valuers and experts would be achievable for a hotel operator - if not improved by the continued increase in gaming machine revenue. Business rentals were set on these earnings and have since proven (in the majority of cases) to be un-sustainable. No allowance was given for capital expenditure required to minimise the effect of no smoking and other

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compliance issues.

In the early 1990's hotel values fell after rising on the back of card machines profits – unfortunately the popularity to play these machines waned so hotel profits fell – hence the decline in Pub values. Today it is not just the fall in gaming revenue but a number of other factors affecting the hoteliers business.

- The debt burden many hoteliers carry today is well above the 60% LVR. Often external assets such as a home were used as added security. Many loans were initially written as interest only - they are now coming to renewal. Today Banks are now forcing hoteliers to reduce loans to bring them inside the traditional ratios.
- The federal government increases the taxation on alcohol twice a year. The hotelier tries to pass this on to the consumer with price rises that are occurring on an exponential basis. The introduction of the alcopop tax further exasperated this. Each of these increases has furthered the divide between takeaway and on-premise consumption. Woolworths and Coles lead the charge in supplying cost price alcohol for home consumption.
- Hoteliers have become complacent whilst they have enjoyed the profits of poker machines. The traditional hotelier behind the bar has certainly changed – but what makes a good hotelier today?
- Expenses have continued to climb over recent years. The massive increase by Pay T.V providers a good example from \$150 per month to \$1,000 per month! Today there is pressure on staff wages, council rates and electricity to increase sharply.

So where is the good news? Hotels are still one of the best cash businesses. In troubled times hotels generally fair better than most other businesses. Hotels now appeal to a broader cross section of the public. Thinking hoteliers have retained their gaming income.

So where are hotel prices going?

The Freehold Hotel market place has broken into a number of sub-markets with each having their own determinants of price.

These markets can be roughly described as follows:

- a) Hotels without gaming machines
- b) Freehold hotels to \$2.5m with Poker Machine entitlements underpinning the value. (property = asset value NOT business value)
- c) Freehold Hotels to \$4.5m where value is directly related to Business Profitability. (Gaming machine numbers are still important yet price is determined by overall hotel profitability)
- d) Premium freehold properties (generally in excess of \$5m) sought after by corporate style purchasers.

Hotels with no gaming.

Hotels with no gaming machines are a difficult property to sell. The majority of purchases like the added security of PME (poker machine entitlements) – a safety net allowing hoteliers sell PME's should all not go to plan.

Sales for hotels with no gaming are as low as \$100,000 whilst others are on the market at \$1m.

The majority of the sales in hotel with no gaming machines are to "local purchasers". They are people who know and keep in touch with the district or currently live close by.

Hotels with PME's underpinning value.

Potential purchasers today are attempting to minimise the "goodwill value". A purchaser would prefer a hotel with 8 PME's and a profit of \$180,000 for \$1m (18% ROI) – in comparison to a hotel with 3 PME's and a profit of \$200,000 (20% ROI).

The added security of asset base through PME's, land and building is having an effect on the overall value of the property.

Occasionally we are seeing properties appear on the market where asset value is greater than business value. These properties are selling at a reduced or conservative asset value – the purchaser appears to be discounting the asset value.

Freehold Hotels where value is related to business profitability.

Potential purchasers are establishing the business profitability on a conservative basis. Whilst vendors and their brokers attempt to present the business profits in the best light; hotel purchasers are demanding comparison year figures, reviewing each expense at today's actual level and closely monitoring gross profit to sales percentages.

As stated above the purchasers will adopt a more conservative capitalisation rate (ROI) when the "business goodwill" comprises the majority of the purchase price.

Premium Freehold Properties.

There are few hotels that fall into this category. Demand certainly exists for "premium hotel" properties from both the corporate and private purchaser. Currently the corporate purchaser continues to outbid the private purchaser; however the gap has dramatically closed.

Newspaper articles often feature these properties and choose to base the market around the sale results for this style of hotel.

Premium hotels will always attract a top price and often defy the general hotel marketplace.

So what is my hotel worth?

Given that a number of different markets can be identified the selection of a value also becomes more difficult. It is not possible to compare one hotel sale with another without knowing the full circumstances including PME's and profitability. The latent asset value ratio to "business goodwill" is a further variable that needs to be taken into consideration.

Who will buy my hotel?

We continue to be worried by the lack of "new blood" enquiry for the hotel industry.

The majority of affordable hotels (under \$2m) have the largest enquiry coming from the local area. Often these people have little hotel operational knowledge (yet all know an "expert").

There remain a number of experienced hoteliers sitting on the side line waiting for hotel opportunities. The majority pedal the line that they sold at the height of the market and wait for values to return "normal".

Actions and movements continue in the corporate marketplace with a number of mergers, acquisitions and takeovers occurring. Some of the fragile corporate purchasers were taken into receivership.

Leasehold Hotels.

Leasehold Hotels have their own separate marketplace.

There are a number of factors affecting the value of a leasehold hotel; such as Term and Rental. Recent years have seen the "traditional" hotel lease varied with bonded leases, high rent-no premium, 30 yr, 50 yr and even perpetual lease terms.

Assets owned by the tenant vary occasionally and we have seen some lease's where the tenant owns the Poker Machine Entitlements.

Variations from the "traditional" cause confusion in the market and can lead to strange results.

With the tightening of bank lending criteria a number of lease purchasers have had to down grade their expectations. Supply of leasehold properties (particularly CBD Sydney) has increased as pressure is placed on a number of lessee's to reduce their lending exposure and lower debt levels to inside today's new lending parameters. Many of these leasehold properties were freshly created in recent years and have rentals well outside "traditional" levels which are causing them to be rejected by the market.

Latest results show that leasehold properties with rental, lease terms and conditions and terms as expected in the "traditional" leasehold marketplace are far more saleable than properties that are outside expectations.

We hope this has given some guidance into the hotel market place.

During the last 18 months there have been a number of properties placed on the market at levels above their achievable price. The market place is rejecting these properties and in fact damaging the perception of these properties even when a price reduction has occurred.

Genuine vendors need to carefully select the method of sale and the price portrayed to potential purchasers.

Chris Jinning & Company has sold hotels throughout country N.S.W. for the past 30 years. Our knowledge of the market place and its history provides us with great skills in the sale of the property.

If you would like to discuss your hotel then please call Chris, Marie or Nick.