Client Alert

October 2025

Australia: Hotel Valuations – insights into the hotel valuation process

In brief

As lawyers, we have always been intrigued as to the methodology used by hotel valuers. We suspect a great many of our clients are like minded. This newsletter explores this topic and provides valuable insight into the valuation process. A must read for all hotel industry participants particularly those involved in hotel sales and purchases.

Contents

In more detail

Question	Answer
How do you fundamentally approach a hotel valuation?	**Before embarking on the hotel valuation journey, we will go through a process of clarifying a range of matters.** This is both in the interests of providing good service but also to ensure we meet the exacting requirements of our governing bodies and professional standards. Of particular relevance to our undertaking and approach is to clarify the purpose/s of valuation, where the hotel sits in its development lifecycle (i.e. existing or proposed) as well as the ownership and operating structure. The majority of valuations we undertake will either be for loan security or financial reporting purposes. However, we will also undertake valuations for a variety of other purposes. This might range from very specific requirements tailored valuation related advisory work to assist hotel investors/purchasers and existing owners with their decision-making. For many of our clients the scrutiny of an established hotel valuer to help identify matters that are critical to an investment decision is valuable. In many instances, industry participants such as purchasers, owners and operators have identified the importance of a hotel valuer's input when making investment decisions and appreciate the direction. In some instances this might be as straightforward as cost benefit analysis as it relates to asset enhancement through to running development appraisals as well as acquisitions scenario analysis in relation to individual hotels and portfolios. In recent years, the appetite for transaction support services amongst our client base has been growing. An acknowledgment of the hotel valuer's role is the increasing number of former valuers that, while no longer practicing, now have senior positions within a number of highly regarded hotel investment, ownership and management companies.

	Although we undertake valuations of hotel properties that might also be leased or owner operated, the most common assessment type remains that of a hotel that is held subject to a hotel management agreement (HMA). A hotel valuation subject to an HMA is in itself multi-varied. But, fundamentally our role is to assess the operation's future trading potential. This involves a thorough review of historical trading performance, management and owner interviews to establish what an investor/purchaser might reasonably expect the hotel to achieve in terms of net income/EBITDA. With regards to both managed and owner operated hotels, the primary methods of valuation are tend to be by way of a discounted cash flow (DCF) and income capitalisation (and variations thereof). These methods involve the application of market derived investment parameters. The results will of course be cross checked with relevant transactional activity to ensure they make sense and do not run contrary to market and industry expectations. There is a lot to the valuation process and ultimately as a regulated industry the valuer's assumptions, and ultimately opinion of value arrived at, requires careful consideration at all stages.
What is the impact of the Term of a HMA?	**Term is significant.** An HMA is a service agreement whereby a third party hotel manager acts on behalf of an owner. It is important to note that a conventional HMA is not a property interest nor is it a lease arrangement and it will not be registered on title. Rather, an HMA is a contractual arrangement that provides a hotel operator rights and obligations in relation to a hotel's operation and hence a degree of tenure in relation to a property interest. In a market where the possibility of vacant possession of the management will typically be seen by investors as beneficial, the term of an HMA will be critical to value outcome. However, while a short term HMA is perceived as good, the actual benefits in terms of valuation outcome will vary depending on the commercial terms and their perceived favorability (relative to what might be negotiated in the prevailing market). Where a hotel is in its life cycle is also an important consideration. For instance, a new hotel that has yet to establish its trade in an untested market, will benefit from both strong branding and a longer-term commitment from an operator that to some extent is sharing in the uncertainty associated with new development. While typically longer, it is unusual to see an initial term of less than five-years in relation to a new hotel.
How do you assess the value of a hotel operator?	**This is an interesting question, as it depends upon the value to whom.** Is it the value of the hotel operator to an owner or the value of the hotel management arrangements to the operator? In the context of this discussion, I will assume the value of the hotel operator to an owner is what is of most interest. For valuation purposes, the hotel operator is assumed to be reasonably efficient/competent with access to all usual operational

	and distribution systems. However, ordinarily a value to a particular operator is not isolated for its own appraisal. Of course, there may be some instances when there might be a need to assess the value of a hotel operator. Likely a requirement of the hotel operator wishing to understand its own worth rather than an owner requirement. Such an exercise can of course be completed, but is rarely requested.
What value do you attribute to the inherent goodwill due to the location of the property and the previous hotel operators?	**This is a challenging question as the response can go down several paths.** Also, I do not want to provide an overly 'polarising' response. It is important to acknowledge that under an HMA the owner and the hotel operator are working in partnership. A hotel will of course benefit from its location and it might be argued that certain locations will be better suited to some operators. For instance, it may be that a particular operator has a strong track record in city centre operations rather than resort locations. But, it is important to acknowledge that location is a fundamental property characteristic. Its strength (or otherwise) would be reflected within the prospective trading assumptions as well as the investment parameters applied when undertaking a valuation. It is possible to identify and attribute goodwill to an existing operator (and pertinently the associated brand). However, in respect to a previous operator and brand, this would be more challenging. There may be some circumstances where a hotel benefits from its operational and branding legacy. However, this is likely to be perceived by an owner to be outweighed by the commercial benefits of new management. Of course, this is a discussion point that might be contested by established hotel operators. While an onus is placed on the hotel management in terms of operational performance, and under an HMA the owner's involvement can be somewhat passive, their experience as owners is also critical. Active asset management is encouraged. Owning a hotel is not simply a case of having the means to purchase. A commitment to the upkeep and sustaining a Hotel's trade by way of strategic reinvestment is also required. I raise this point as under investment in a hotel asset by an owner can result in a property falling short of brand standards and customer expectations. Overtime this can weigh negatively on both value and perceived goodwill.
How relevant is it that the operator has not previously managed a hotel in Australia or is proposing a brand which is new to Australia?	**From a valuation perspective the existing footprint and the market's familiarity with an operator's brand and reputation is highly relevant.** A track record is also key. It provides reassurances of experience and to some degree will reduce perceived trading uncertainty. New brands and concepts that have yet to be 'road tested' will be perceived as carrying a higher degree of cash flow uncertainty. That said, they can offer an important point of difference in a crowded market. Also, if the operator's wider strategy is to launch or grow a particular brand, it may be possible to negotiate more favorable management terms. Of course, for some these benefits might outweigh the perceived uncertainties surrounding more established brands/concepts. However, through the eyes of a valuer, uncertainty weighs on the outcome and the specifics need careful consideration.

How important is termination on sale or without cause termination?	**In Australia and New Zealand, the ability to acquire a hotel and having the option to change the hotel management is perceived by investors as beneficial.** In simple terms, its availability broadens market appeal and enhances liquidity. However, it is equally important for the operator to secure sufficient tenure to support their own business case and the management commitment they are making. From a valuation perspective, a balanced approach is required. The prospect of securing vacant possession if desired will generally be expressed within an assessment through the application of firmer investment parameters (capitalisation rates and discount rates). Notwithstanding, cash flow stability is also beneficial. So, a valuer will need to consider the aforementioned relative to the appeal of a hotel to operators as well as the terms in place relative to what might otherwise be available. Of course, worth noting that the availability of vacant possession while perceived as beneficial, does not mean termination is inevitable. The decision to terminate is not one that will be taken lightly. A change in management introduces trading uncertainties and disruption that might also weigh on value. Although, not ideal for the hotel operator, it is acknowledged that the availability of vacant possession is an important consideration for an investor/owner. This is evident with termination on sale clauses becoming more commonplace and from time-to-time termination without cause. Of course, important to note that the inclusion of such clauses will ordinarily come at a cost to the owner in the form of a termination fee.
What significance do you give to the effectiveness or otherwise of a performance termination provision?	**While the ability to terminate is inferred by this clause, it is widely agreed that termination on the basis is rare.** Performance based termination clauses are typically based on defined performance hurdles within an HMA. Ordinarily, it is a case of actual performance relative to budget and/or the performance of a hotel by relative to the corresponding performance of an agreed competitive set. Further, when it transpires that the agreed thresholds have not been met, the operator will typically have a right to cure. From a valuation perspective, termination on sale or without cause is more relevant. Also noteworthy, is that the forecast prepared for valuation purposes is intended to represent a reasonable expectation for future trading potential. While historical performance is carefully considered, the contractual ramifications and the potential for performance-related termination is not generally assumed.
How relevant is the base fee/ incentive fee configuration?	**Critical. Especially so for longer agreements that do not facilitate termination.** Again, a balanced approach is required. Management fees are a feature of cash flow performance and hence important to valuation outcome. Of course, on face terms “the lower the better”. However, to secure an appropriate operator requires compromise. It is also

	important that the operator is motivated and incentivised to achieve the best possible results. The quantum is key in respect to both base management fees and incentive management fees. In terms of configuration, both are important in order to drive both positive revenue outcomes as well as effective cost management when doing so.
How important is operator key money?	**Another contentious matter.** Key money is most common in respect to an operator securing a position on a new development. Given the thinness of development margins in respect of proposed hotels, a financial contribution may be positively received by a developer. However, a financial contribution of this type might be at the expense of more favorable terms. Further, such contributions will tend to require repayment in the event of early termination. A valuation concern is that the event that the developer's intention is not to hold the asset, these terms and obligations will ultimately need to be passed to a subsequent owner (and reflected at valuation).
What is the impact of a non disturbance agreement?	**The non-disturbance agreement, supports continuity of trade and therefore cash flow.** However, the relevance of this clause would depend on the specific circumstances.
How do you view a manchise in comparison to a HMA?	**A manchise, being a hybrid of a conventional HMA and a franchise, introduces other considerations such as the owner's own track record in terms of hotel management (or that of a third-party manager).** A HMA is more commonplace and is reflective of the full engagement of the hotel operator. Being a conventional arrangement, this presents less unique characteristics than a manchise. A valuation of a hotel with a manchise in place rather than an HMA would also require careful consideration by a valuer and the valuation implications would be subject to variation in terms of the extent of the terms agreed and the defined responsibilities of the manager/operator and owner.
What is the impact of a split management model where a hotel operator manages the accommodation and an experienced restauranteur manages the F & B?	**This is very much dependent on circumstances and the relative scale of the accommodation and F&B components.** Also, consequential is how the F&B is held. Important considerations from a valuation perspective will be: • How is the F&B integrated within the hotel and does it include C&E. • Is the intention for the F&B to operate independently or remain integrated with the hotel operation (from a customer perspective); • The track record of the F&B operator and how its business complements the hotel (or otherwise); • Is the F&B component to be leased to a third-party by the owner or by the operator and how is the revenue booked; and • Alternatively, if a separate management agreement with an F&B operator is in place, what is the relationship with the hotel

	management company and what are the management fee implications?
What is the impact of a franchise either with owner management or a third party manager (e.g. white label manager)?	**This is very much dependent on the individual parties.** More particularly the benefits of the franchise and the associated fees as well as the experience of the third-party manager. Valuing a hotel that is owner operated and subject to a franchise arrangement is more likely to be reflective of an owner operated hotel (or be notionally adjusted to facilitate comparison with managed hotels). Conversely, an established white label operator might be assessed on a basis that is similar to a managed hotel. Key considerations will be the experience and track record of either owner or white label in terms of management. Also key are key terms along the same lines as an HMA i.e. term and termination rights. A perceived benefit of a franchise arrangement (either direct or with a white label management company) is more favorable terms relative to an HMA. However, this might not always be the case and requires careful consideration.
What are the most material clauses in a HMA that impact valuation (both positively and negatively)?	**Aside from the terms already addressed such as fees, tenure and termination - anything that has the potential to enhance the operational cash flow will impact the valuation positively and vice versa.** I would add that while revenue will receive the most attention, particularly at the time of engaging a manager, it is important that operational costs are considered in equal measure. Ultimately, on the assumption of reasonably efficient management, revenue variations will respond to market conditions. The same can be said of operational expenses. However, there is a higher fixed component. Hence, if revenues are not achieved there may not be a corresponding reduction in costs.
There has been a lot of focus on ESG initiatives in recent years from both owners and operators. Has this factored into hotel valuations yet? If so, how?	**ESG has become an important part of the valuation considerations.** While quantifying can be challenging, it is a consideration of industry participants such as lenders and investors. JLL has prepared separate research in this regard.
Standalone hotels, particularly in the CBD market, are becoming less commonplace in today's market. Does the inclusion of a hotel within a broader mixed use development, as opposed to being a standalone asset, influence its valuation? If so, how?	**There are economies of scale that might be captured from mixed-use development. There will also be complementary uses.** It is still important that a hotel operation stands in its own right within a mixed use scheme and for it to be a 'complimentary' rather than a 'subsidised' use.
We have seen new-builds where property owners have been forced to sell mid-construction due to funding issues. How do	**Restrictive circumstances and especially those that compel divestment within a short period are suboptimal.** Of course the extent of any potential discounting really depends on the specific circumstances.

you value partially completed hotel developments? Can investors expect a big discount in these types of deals?	Under the circumstances described here (and assuming hotel-use remains the perceived highest and best use), a clear pathway to the hotel's opening is required. Immediate questions to be raised would likely revolve around the extent of works that have been completed (or are yet to be completed) the cost to complete, as well as resolving the complexities that may exist in relation to retaining or transitioning between builders/developers/contractors. This would be a topic that would need to be discussed in detail ahead of embarking on as a valuation engagement. I would also envisage the potential need to defer to likes of Baker McKenzie in this regard.

Contact Us

Dora Stilianos
Partner
Dora.Stilianos@bakermckenzie.com

Sebastian Busa
Partner
Sebastian.Busa@bakermckenzie.com

Graeme Dickson
Of Counsel
Graeme.Dickson@bakermckenzie.com

Julian Whiston
Head of Hotels & Hospitality
Australia and New Zealand
Value and Risk at JLL
Julian.Whiston@jll.com