



WHERE STYLE MEETS PROFIT
THE EVOLUTION OF **LIFESTYLE**
SELECT-SERVICE HOTELS

WATG

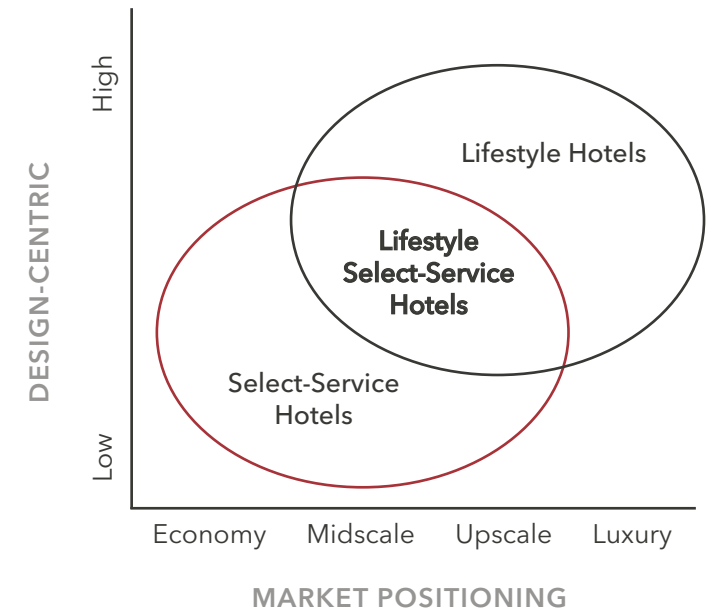
2020

INTRODUCTION

Select-service hotels have long proved their ability to withstand economic downturns and sustain higher profit margins compared to their full-service counterparts. With casual F&B options and moderate meeting spaces, select-service hotels are designed with space efficiency and a lean labor model in mind. As such, they have been the darlings of developers and owners, and are expected to be among the first hospitality segments to recover post-COVID-19.

On the other hand, lifestyle hotel concepts have shaken up the luxury sector, and cost-sensitive concepts are now making inroads into the select-service space. To remain relevant, traditional select-service hotel brands have been racing to refresh and update in recent years, while more contemporary select-service brands continue to be introduced. These 'lifestyle' qualities, which place more emphasis on design and localization, connect with modern travelers and local communities alike. While the 'lifestyle' premium is hard to measure, these design-driven hotels undeniably drive higher revenue.

What happens to a hotel that straddles both lifestyle and select-service categories? In this paper, WATG Strategy explores this intersection and demonstrates that this breed of hotels, when differentiated by design and driven by efficiency, is at once stylish and lucrative.



This piece was compiled by WATG Strategy. We offer clients market research-led pre-development advice, programming and financial feasibility to help simplify the complexities of hospitality development. We work seamlessly with our design studios to create award-winning destinations that maximize economic performance.

FINANCIAL BENEFITS OF SELECT-SERVICE HOTELS

As hotels begin their long journey of post-pandemic recuperation, operational efficiency mastered by select-service hotels is more critical than ever. Investors and developers will continue to turn to this category for the following reasons:

ROOMS-FOCUSED

Select-service hotels focus on the most profitable business line in a hotel - the rooms department. The average rooms departmental profit margin is 73 percent in the U.S. in 2019, which far exceeds the average food & beverage (F&B) departmental profit margin of 29 percent, largely due to the labor-intensive nature of F&B operations. In addition, given their efficiency, select-service hotels' profit margins fall on the higher end of this range.

EFFICIENT AND LOWER-RISK LABOR MODEL

The hotel business is labor-intensive, and labor cost increases have consistently outpaced revenue growth in recent years. In 2019, hotel labor cost in North America amounted to 35 percent of total revenue, and labor cost increased 2.8 percent, outstripping total revenue growth of 0.9 percent. Select-service hotels' staffing levels are generally 40-50 percent of those at full-service hotels, and can effectively 'flex' labor by having lean teams that promote cross-staffing, especially during non-peak times.

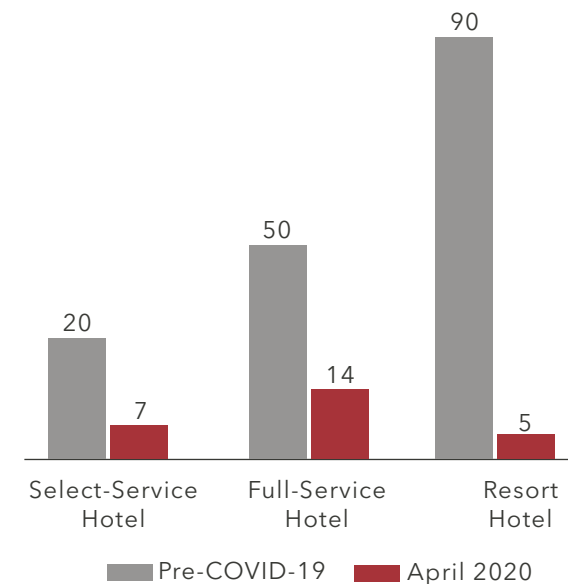
For example, front desk agents at Marriott's Aloft hotels are known as Lifestyle Guest Experience Specialists, and they are empowered to take on a wide range of roles, such as concierge and shuttle driver. Another example is citizenM hotels, who address their employees as 'Ambassadors', avoiding formal uniforms and routine job functions. All citizenM employees work across functions, making the job less monotonous and more enriching.



Source: HotStats

STAFFING LEVEL FOR AVERAGE HOTEL

Number of Employees



Source: Hotel Effectiveness

FINANCIAL BENEFITS OF SELECT-SERVICE HOTELS

CONSTRUCTION COST AND TIME SAVINGS

Select-service hotels are attractive investments given their lower development cost. According to HVS' U.S. Hotel Development Cost Survey 2018-19, total cost to build ground-up select-service hotels average \$290k per key, with a median of \$196k per key. In contrast, the average full-service hotel costs \$397k per key to build, with a median of \$314k per key.

In addition, select-service hotels are the most suitable candidates for modular construction given a manageable number of room types. Also known as prefabricated construction, this method can deliver projects up to 20 to 50 percent faster than traditional methods, according to a McKinsey study. Even though modular construction is not yet mainstream or fully established in North America, numerous hotel developers are testing the waters. Concord and citizenM are among its pioneers in the U.S.; citizenM New York Bowery Hotel is currently the world's tallest modular hotel, and Concord's proposed AC Nomad in New York City, if constructed, will claim the world record. As long as global supply chain disruptions can be mitigated, modular construction could prove to be advantageous for a wider group.

RECESSIONARY RESILIENCE

Over 70 percent of investors are bullish on select-service hotels and believe they enhance portfolio returns, according to a 2019 JLL survey. Indeed, select-service hotels have demonstrated that they experience less severe revenue and profit declines during economic recessions. As current trends show, the COVID-19 downturn will be no exception.

It is no surprise that more select-service hotels, with a nimbler operating model, are able to stay open than their full-service counterparts during the pandemic. On its Q1 2020 earnings call, Hyatt shared that in the Americas, while 62 percent of its full-service hotels temporarily shuttered, only 19 percent of its select-service hotels were closed. Additionally, select-service hotels can break even on a Net Income level at a 40 percent occupancy, compared to a 50 percent occupancy hurdle for full-service hotels, according to STR.



Source: Apple Hospitality REIT Investor Presentation

FINANCIAL BENEFITS OF LIFESTYLE HOTELS

Likewise, lifestyle hotels of all service levels have displayed superior financial performance compared to more traditional and standardized hotels.

FLEXIBLE RATE CEILING

Whereas a traditional select-service hotel (i.e. Hampton Inn by Hilton) is typically priced below a full-service hotel (i.e. Hilton) in the same market, a lifestyle select-service brand (i.e. Canopy or Curio Collection by Hilton) is not constrained by the fixed pricing hierarchy. This higher degree of pricing elasticity allows lifestyle brands to charge higher ADR particularly on peak nights, which translates into stronger profit for the hotel. Lifestyle boutique hotels' RevPAR premium is approximately 40 percent over the average U.S. Upper Upscale hotels, according to the 2019 Boutique Hotel Report.

ADDITIONAL REVENUE STREAM FROM LOCALS

By attracting locals with inviting all-day cafes, coffee shops, bars, and communal lobbies, lifestyle hotels are well-integrated into their communities and bring in an additional source of revenue. Hilton Canopy, for example, positions itself as the 'Street Lamp' of the neighborhood, with an emphasis on exterior lighting as well as visible and accessible F&B outlets that draw in local workers and residents.

HIGHER NET REVENUE THROUGH DIRECT BOOKING

Perhaps because of their distinct appeal, lifestyle hotels have demonstrated the ability to garner more reservations from direct channels instead of third parties, which lead to higher net revenues. For example, Marriott's reservation channels generate 80 percent of total bookings for AC hotels, but only 71 percent for Courtyard and 66 percent for Fairfield Inns. Direct bookings help hotels to avoid hefty guest acquisition fees, which can amount to 15 to 25 percent of revenue, according to Kalibri Labs.

SOCIAL MEDIA POWER

Design-driven hotels with photo-worthy spaces are best able to capitalize on social media's advertising power and reduce marketing spend, as travelers follow word-of-mouth advice. Over 97 percent of millennials share photos on social media while traveling, and 75 percent of them post photos to social networks at least once per day, according to Site Minder. This doesn't just apply to younger generations, however; social media usage is as high as 78 percent for Gen X and 48 percent for Baby Boomers.



BRAND STRATEGIES

The lucrative nature of lifestyle select-service hotels has raised standards and brought new players to the sector, making it fiercely competitive. Major players, in turn, are evolving their strategies to stay ahead.

SHIFTING TOWARDS LIFESTYLE

New hotel brands have continued to emerge with one commonality: they are targeting the modern traveler who is expecting localized experiences even from international hotel chains whose brand standards may prescribe the look and feel for thousands of hotels globally.

While this is the case for all hotel segments, new additions to the select-service sector have been the most prolific in recent years, as select-service projects accounted for 70 percent of total U.S. construction pipeline at the end of 2019. This trend forces the industry to localize rather than institutionalize, and the importance of authentic brands that build connections will be heightened post-COVID-19.

CASTING A WIDER NET

To further complicate the competitive landscape, dual-branded (and even triple-branded) hotels are on the rise, where two or more brands coexist in the same

building. Guests can experience the amenities of multiple hotel brands within the same or even different hotel families. Developers are enthusiastic about dual-branded hotels because of diversified revenues from multiple guest segments, improved operating margins (from sharing selected staff and back of house areas), lower combined development costs (compared to building two separate hotels), and stronger Area of Protection in blocking out multiple competitive brands from entering the market.

Select-service brands are primary targets for dual branding. While numerous brand combinations have been conceived, the most common groupings typically involve a select-service hotel a) in tandem with another select-service hotel of a different character, b) an extended stay hotel, or c) a full-service hotel.

BLURRING THE LINES BETWEEN TRADITIONAL AND LIFESTYLE

Terminating a brand is costly due to existing franchise agreements. Therefore, rather than retiring outdated brands, hotel groups continue to revive their traditional brands to keep them relevant. In 2018, Hilton modernized the exterior and interior design for its more than three-decade old Hampton Inn brand, including enlarging windows by 25 percent

while shrinking the rooms and reducing the number of suites to entice developers. In the same year, Marriott contemporized not just the interior and exterior of its classic select-service brands, but also their logos. The latest prototypes of the reborn classics are so enhanced that they too are adopting a 'lifestyle' appeal, blurring the distinctions between traditional and lifestyle brands.

From a design perspective, while select-service brands offer developers the option of selecting 'off-the-shelf' design packages, having customized and localized design is becoming essential for the market leaders.

PROLIFERATION WITHOUT DILUTION

Brand proliferation has created confusion for consumers and owners alike and has played a role in the elevated pipeline. However, some hotel brands are not looking to be in every market. According to Marriott's Development team, the Moxy brand is only going into hand-picked urban-core locations to ensure no two Moxy hotels are alike. As the result, Marriott only has 32 Moxy hotels in its North America pipeline as of year-end 2019. As the hotel industry braces itself for a period of reprioritization, whether a hotel brand and property can withstand the test of time will be influenced by a key factor: design.

BRAND STRATEGIES

WATG CASE STUDY: ARCHITECTURE AND LANDSCAPE

Residence Inn Glendale | Los Angeles County, California

Status: Under Construction

Located in downtown Glendale near the Americana at Brand retail park and the historic Alex Theater, the Residence Inn is a project by R.D. Olson Development and R.D. Olson Construction. A pedestrian paseo will connect the new hotel to the existing movie theater complex, capitalizing on the urban and walkable location that invites guests to explore the city on foot. The hotel draws in guests and locals through arched entryways into a double height lobby, and the indoor & outdoor city-corner street seating evokes the feeling of the neighborhood breakfast room.

The building's architecture draws inspiration from the Spanish Colonial Revival style to complement the aesthetics of the nearby historic YMCA structure, and yet is contemporized to fit the modern developments of the city and demands of the traveler. A selection of guestroom types features Juliet balconies with large slider windows, providing guests with a view of classic Glendale California.

"The Residence Inn fits comfortably into the intersection of E. Wilson and N. Louise and extends the fabric of the downtown and pedestrian experience."

- Greg Villegas, Vice President, Director of Construction + Full Services, WATG



Residence Inn Glendale California

DESIGN CHARACTERISTICS

During a profit-stagnating phase of the market cycle, thoughtful and distinguished design details are important for a select-service hotel to stand out in the crowded market. Below are some key design trends that define today's lifestyle select-service hotel.

LOBBY AND COMMUNAL SPACES

The hotel lobby is going through a metamorphosis. The transactional nature of the check-in experience is being replaced by a much more fluid and conversational one, thanks in large part to the prevalence of self-check-in technology via mobile and kiosks. Ian Schrager's Public Hotel in New York City, which is designed to compete with select-service hotels, removed the front desk altogether. This trend may be accelerated post-COVID-19 as touchless and hygienic methods are being prioritized and operators look for ways to reduce labor cost.

Likewise, certain design trends pre-COVID-19 are also likely to be boosted, such as the use of double-height ceilings to make the lobby feel fresh and airy, biophilic design to evoke a sense of well-being, and blurring of indoor and outdoor boundaries to connect to nature. These design traits which were once associated mostly with high-end full-service hotels are now common features in lifestyle select-service hotels.



Moxy San Diego - Check-In at the Bar

FOOD AND BEVERAGE

Food and beverage are being shifted forward to greet guests when they first enter the hotel. Instead of formal three-meal restaurants, select-service hotels are delivering casual and convenient dining experiences, as well as lively bar spaces, that appeal to hotel guests and locals (alcohol generates a higher profit margin than food). Made possible by a wealth of F&B options in high-density locations, as well as food delivery services, these light and beverage-focused operations can be profitable even in high-cost urban environments:

- **All-day 'Grab-and-Go' markets:** Lobby cafés ensure guests can grab a bite no matter what time they arrive or depart. Increasingly, these markets offer gourmet options that incorporate and showcase local flavors. An

example is Caption by Hyatt, which partnered with Danny Meyer's Union Square Hospitality Group and created its F&B program that is a 'vibrant mash-up' between café, market and bar.

- **Multipurpose and beverage-focused:** Marriott's Moxy hotels take cross-staffing to the next level by combining the bar and front desk in selected new builds. At the Moxy San Diego, guests check in at the bar by bartenders and receive a complimentary welcome cocktail.
- **Chameleon Spaces:** Another example is Marriott's AC Hotels which serve European-style complimentary breakfast in the AC Kitchen; later in the day, the space is transformed to host coffee service, wine and cheese tastings, nightly beverage rituals and other special events.

LOCAL CONNECTION

When the first chain-hotels were born, consistency was celebrated, and travelers took comfort in a hotel where they knew exactly what to expect no matter where they were. Today, however, travelers are sponges for new discoveries and seek unexpected delights at every corner. From lobby ambience to guestroom artwork, select-service hotels too can be the ambassadors of their surroundings and act as organic members of the community. Marriott's AC Hotels, for example, display museum quality artifacts that are unique to their locations, and Hyatt's Joie de Vivre is also known to reflect their vibrant neighborhoods.

DESIGN CHARACTERISTICS

WIMBERLY INTERIORS CASE STUDY: INTERIOR DESIGN

Hotel 50 Bowery, Joie de Vivre by Hyatt,
New York City

Status: Built

Hotel 50 Bowery is a 229-room boutique hotel that opened in 2017 in the Chinatown neighborhood of New York City. As the first Joie de Vivre property in New York, Hotel 50 Bowery captures the spirit of change on one of the city's oldest streets. The design was inspired by warehouses synonymous with the Bowery, with subtle Asian undertones celebrating the old and new influences of its local surroundings.

Past meets the present in the reclaimed wood reception desk set resting on contemporary poured concrete, while a Corten steel screen to the rear evokes a Chinese landscape painting. Atmospheric hallways are punctuated by subtle lanterns and large, bold works of art from Beijing-based graffiti artist, Dake Wong. Light-filled guest rooms feature industrial materials, original artwork, and signature hand-plastered headboards, with a hint of Asian chinaware in the blue and white color scheme. The Crown, a rooftop bar and lounge occupies the 21st floor where the urban eclecticism design continues, taking advantage of the expansive views of Lower Manhattan and Brooklyn across the water.

"The light fixtures in the hotel lobby give a nod to the incense cones that hang from the ceilings of temples omnipresent throughout Asia (especially the Man Mo Temple in Hong Kong), but also play off the fact that Chinatown remains a haven for lighting showrooms. The concept for the guestrooms at Hotel 50 Bowery is an homage to the neighborhood itself - it is a study on blending customs. The room follows the harmonic philosophy of Feng Shui through the mixture of the elements: Wood, Fire, Earth, Metal and Water."

- Margarita Velez-Mantovani, Associate Project Manager, Wimberly Interiors



Hotel 50 Bowery, New York City

DESIGN CHARACTERISTICS

WATG CASE STUDY: ARCHITECTURE AND LANDSCAPE

Canopy by Hilton | Sacramento, California

Status: In Planning

Located in downtown Sacramento, the Hilton Canopy hotel comprises of 265 hotel rooms, as well as 55 luxury residential apartments on the top floors. On the ground floor, a corner bar and café open up to the sidewalk to maximize street activity and invite pedestrians into the building. An outdoor terrace, function spaces and a pool are located on the third floor. On the rooftop, an amenity deck, covered lawn and a bar are planned. This vibrant mixed-use building will activate the city block and transform the street corner into a new destination for Sacramento.

The building will be framed by a vertical expression that extends from the podium to the roof. The columns serve to accentuate the corner of the building, while a light metal canopy - a fun interpretation of the brand name - will crown the building and provide shade on the roof terrace.

WATG is working closely with ownership to optimize the building's efficiency and overall user experience. The goal is to maximize revenue-generating spaces while ensuring guest and staff flow is streamlined, views are optimized and the overall product is simultaneously iconic and timeless.

"Our client's commitment to the future success of downtown Sacramento provides vibrant direction and inspiration to the design team. The developer Eva Hill appreciates great design and challenges the team to seek the very best solutions to provide exquisite design, efficiency for its future operations, and an outstanding experience for the guests, the residents and the employees. It paves the way for WATG in creating an urban destination that stands out in the ever-changing city canvas."

- Mark Yoshizaki, Senior Vice President, Architecture, WATG



Canopy by Hilton Sacramento

DESIGN CHARACTERISTICS

GUEST ROOMS

Lifestyle select-service hotels are all about the delicate balance of delivering a premium experience while maintaining cost efficiency. Therefore, they focus on what guests need in the guestrooms, and eliminate everything else.

Added: Space-Saving Features

Peg walls, under-bed storage, open wardrobe, lofted beds, bunk beds, and multi-use furniture that can be discreetly stowed when not in use

Eliminated: Space-Consuming and High-Touch Features

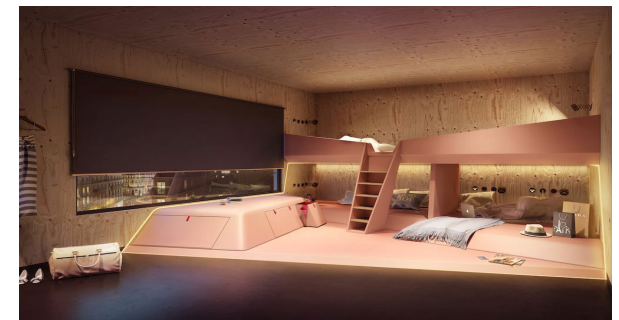
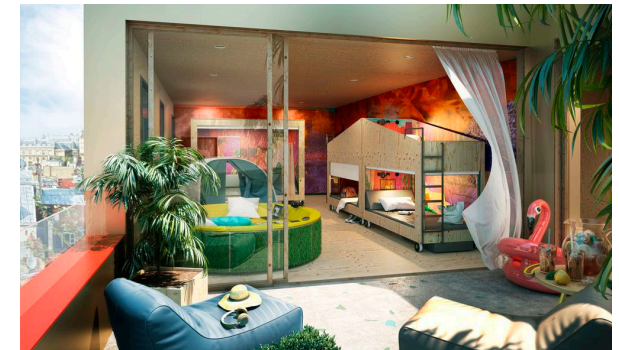
Coffee machine, closed closet, dresser, mini bar, telephone

- **Cozy Guest Rooms:** With multipurpose common spaces come the inevitable shrinkage of hotel guest rooms, particularly in urban locations. Minimizing room sizes is also embraced by developers as it translates into development cost and ongoing maintenance cost savings, as well as higher overall hotel value in maximizing key count. Marriott's Moxy is an example of a micro-hotel, with guest rooms averaging just 183 square feet – about half of the U.S. average of 325 square feet.

Similarly, Hilton's Motto's average room size is 163 square feet. The Pod Hotels push the limit even further, with rooms that are as small as 90 square feet in the Pod 39 New York City hotel.

- **Multisensory Sleep Experience:** A deluxe sleep experience is no longer exclusive to high-end hotels. Lifestyle select-service hotels are now offering sumptuous beds, along with customized touches such as fresher air, controllable sound, and personalized lighting. Hilton pampers its Canopy guests who sleep under a canopy on a Serta mattress with a special foam topper; the beds come with Cool Balance Technology for optimized temperature control. CitizenM is known for its wall-to-wall, two-meter squared mattresses, which are topped with Italian linen and duck-feather pillows. Black-out blinds provide darkness, and thick modular-constructed walls provide quietude, both indulgences in 18- to 24-hour urban settings.
- **Spacious Shower:** Even as hotel room sizes are shrinking, the showers are not. Hilton Canopy guest bathrooms have large walk-in showers, built-in benches, and generous counter spaces. A number of lifestyle brands such as the Moxy may even place the sink outside of the bathroom to ensure a spacious shower, a feature well received by guests.

- **Communal Guestroom Spaces:** Studio Commons by Marriott's Element Hotels and Open Houses by Accor's Jo & Joe are among examples of the concept of shared living room, kitchen and dining spaces that connect to guest rooms or sleeping areas. Guests who travel with a large family or in groups, such as reunions and wedding parties, now have an option to spend time together during the day without having to resort to Airbnb or alternative lodging venues.



Open House by Accor's Jo & Joe

NEXT-GENERATION LIFESTYLE HUBS

Lifestyle select-service hotels may have a competitive edge but by no means a bullet-proof model. Lower barrier-to-entry and over supply in the select-service category are obvious sources of pressure on existing hotels. The bigger challenge is perhaps an inherent tension: during the development stage, the costly design-driven hotel product must be affordable for the developer. During the operating stage, hotels are tempting guests to spend more with minimized guest room and staff; at the same time, they still need to ensure that guests leave satisfied and eager to return.

Maintaining a balance between efficiency and high perception of value will be key as lifestyle select-service hotels navigate toward a new and more evolved normal in the post-pandemic world. Innovations that go beyond touchless technology, such as robotics and artificial intelligence, may be an important leap. Unlike luxury hotels where guests still may expect high-touch service, select-service hotels can lean more heavily on technology and robots to take on repetitive or tedious tasks, thereby freeing staff to provide guests with better service.

In recent years, we are witnessing the emergence of a new breed of wellness, co-working and co-living social clubs. The younger generations, in particular, are opening their minds (and wallets) to these integrated and inspirational communities for their professional, personal and family lives. The next generation of the lifestyle select-service hotel, then, could progress alongside its users and become more than a place to sleep for a few nights. It can become multi-faceted work-play-stay hub while continuing to deliver superior value for its owners and heartfelt hospitality for its guests.



Lido House Autograph Collection, Newport Beach California, a WATG project



WATG STRATEGY

BESPOKE ANALYSIS AND INSIGHTS

While WATG is world-renowned for our design services, we are also committed to being a full service hospitality real estate advisor to our clients. We recognize that a project's success is measured not only by how it looks, but by how it performs. Our advisory team, WATG Strategy, ground every project in economic realities through detailed market research, industry trend monitoring, concept visioning and competitive positioning. What distinguishes us from the other consulting firms is our collaborative approach with our design team; we work in conjunction with the master planners and architects to identify solutions and maximize the potential for our clients. This consulting expertise is unique within design firms, and allows us at a very early stage to effectively position the asset, resulting in the optimum opportunity for economic success.

Understanding the branded residence model, and its application within specific markets, is a complex undertaking and requires sensitive planning. WATG's Strategy team has vast experience in the sector, undertaking due diligence for developers and operators around the world. The team's extensive database of supply and market performance allows us to equip developers with recommendations which optimize the financial viability of a given scheme.

WATG is in a unique position to share insights that will help position your development for success in an increasingly crowded and competitive marketplace. We're not just looking at current supply and demand trends, but also how they might change in the future. WATG's Strategy team will actively guide the early stages of project planning, through:

- Local market benchmarking
- International benchmarking and success stories
- Assessment of market demand to identify source markets, consumer preferences and to position the project relative to local, regional, state and international trends
- Area programming based on the supply and demand characteristics of the competitive market, in isolation from or collaboration with the design team
- Identify potential hotel companies that may be appropriate for the development, based on the geography, market demand and brand recognition
- Develop a financial appraisal to evaluate key returns metrics
- Identify, recommend and facilitate introductions to prospective development partners, operating companies, public relations firms, project managers and / or legal counsel at the appropriate time and integrate them into the process

Disclaimer: This report is based on an industry-wide database assembled by WATG from an independent research effort, general knowledge of the industry, and consultation with representatives at numerous hospitality firms. This report is for general informative purposes only, and no warranty or representation is made by WATG regarding the accuracy of the data. Unless required by law, you shall not provide this report without WATG's prior written consent, which WATG may at its discretion withhold or grant subject to conditions. Possession of this Report does not carry with it the right to commercially reproduce, publish, sell, hire, lend, redistribute, abstract, excerpt or summarise this Report or to use the name of WATG in any manner without first obtaining the prior written consent of WATG.

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