

The Entry and Exit of Investors: Hospitality Transactions during the COVID Period

by Yifei Mao

The market turbulence incited by the recent COVID 19 pandemic caused a substantial, albeit brief, disruption in the hospitality and travel industry. Nevertheless, players in the hotel real estate market continued trading during this time. While it's true that a substantial number of owners exited the industry during the pandemic—well over 5,300—nearly as many entered the industry—more than 4,500, according to figures recorded in the CoStar database. Despite the many exits and entrances, the overall distribution of ownership type remained essentially the same in the wake of the pandemic. The preponderance of owners continues to be single firms that hold a single hotel. However, an analysis of the hotel transactions from the COVID period finds one notable change in hotel ownership distribution, due to the interest in the industry by private equity investors. Taking advantage of hotel price weakness early in the pandemic, private equity investors increased their market share from 1 percent to 3 percent, even considering the substantial number of private equity investors that exited the hotel industry.

ABOUT THE AUTHOR



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Although the global hotel and travel industries staged a substantial recovery from the effects of the COVID pandemic, the industry's prospects looked dim indeed when the virus struck in 2019. Many agencies and governments issued travel restrictions, shelter-in-place mandates, and social distancing guidelines in 2020.¹ Moreover, given the initial severity of the illness, many would-be travelers had already decided to stay home. As a result, 2020 was a grim year for the hospitality industry. At that time, Priyadarshini predicted a 17-percent reduction in global revenues for the tourism and hospitality sector compared to 2019, along with tourism and hospitality revenues falling by 9.4 percent in the North America.² According to CNN, up to 80 percent of hotel rooms went unoccupied by mid-2020.³ Using a sample of 5,090 hotel properties in Texas, Yang *et al.* (2003) reported a 10-percent increase in monthly confirmed COVID-19 cases, which led to a 0.522-percent decline in hotel performance.⁴ They further found that higher-end and newer hotels experienced a more severe negative impact than economy hotels.

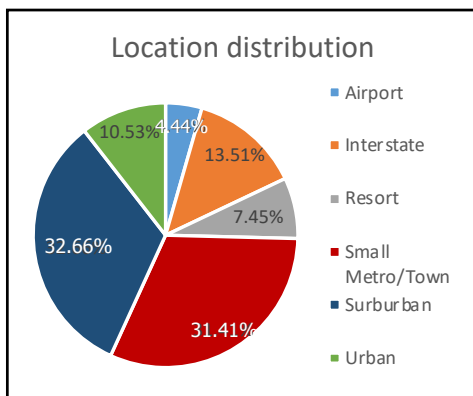
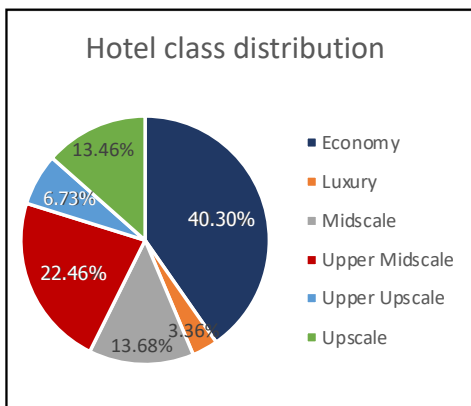
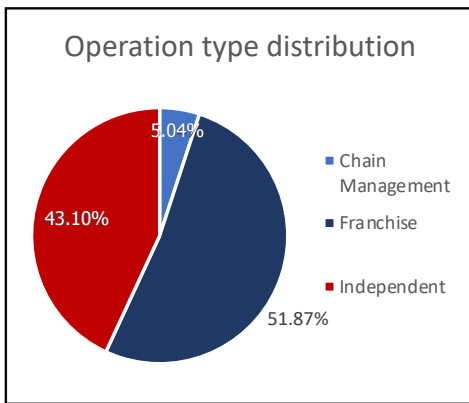
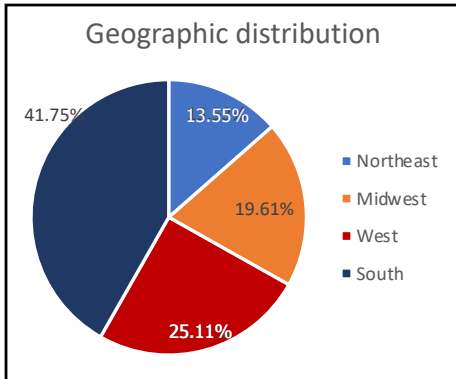
¹ "Coronavirus Closures: Map of Where US States Are Tightening Restrictions," accessed May 30, 2023, <https://www.usatoday.com/storytelling/coronavirus-reopening-america-map/>.

² Ishaani Priyadarshini, "A Survey on Some of the Global Effects of the COVID-19 Pandemic," preprint (In Review, April 7, 2020), <https://doi.org/10.21203/rs.3.rs-20842/v1>.

³ Leah Asmelash Cooper Aaron, "Nearly 80% of Hotel Rooms in the US Are Empty, According to New Data," CNN, April 9, 2020, <https://www.cnn.com/2020/04/08/us/hotel-rooms-industry-coronavirus-trnd/index.html>.

⁴ Yang Yang, Hengyun Li, and Wesley S. Roehl, "COVID-19 Pandemic and Hotel Property Performance," *International Journal of Contemporary Hospitality Management* ahead-of-print, no. ahead-of-print (January 1, 2023), <https://doi.org/10.1108/IJCHM-09-2022-1084>

Hotel distribution by category



Despite the 2020–21 crash in travel activity (or perhaps because of it), hotel real estate transactions continued during the pandemic.⁵ The question that arose for us is whether the nature of hotel ownership would change due to the pandemic. To examine this question, we investigated the ownership of 66,397 hotels using data from the CoStar database.⁶ We constructed our sample by extracting cross-sectional hotel data from 2022, along with transaction data during the pandemic, from 2020 to 2022. Using the transaction data and current owner information, we were able to trace prior ownership before Covid and obtain yearly ownership information.

Considering the significant financial challenges and market dislocations that arose from the pandemic, we anticipated that some individuals or businesses would be compelled (or encouraged) to sell their properties and exit the industry. Consequently, we anticipated a wave of ownership change—along with the possibility of an industry restructuring. Even in the midst of market disruption, for instance, we note an increase in interest within the hotel investment market. Sophisticated institutional investors and high-net-worth sponsors, who possess knowledge of the sector and are experienced in evaluating risks associated with lodging assets, showed a surge in their enthusiasm. There was also the question of whether the pandemic would affect hotel real estate pricing. In that regard, we note that during Q2 and Q3 2020, a half dozen U.S. hotel sale transactions produced market-based evidence of pandemic-induced value erosion.⁷ This appeared to create an opportunity for enhanced returns on investments for buyers.

In the U.S. hotel industry, a hotel owner is typically an individual or institution that is a legal possessor of the hotel property, but often not the operator. In many cases, those who invest in hotels are not involved in daily operational activities. However, hotel owners' expertise in implementing superior strategies regarding segment, brand, operator, and location are critical

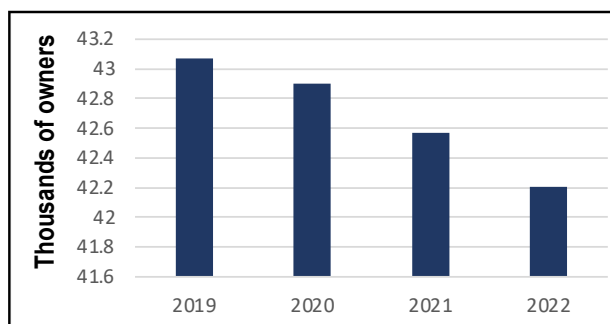
⁵ For example, see: Crocker H. Liu, Adam D. Nowak, and Robert M. White, Jr., *Cornell Hotel Indices: Third Quarter 2023; Higher Interest Rates Hinder Hotel Price Momentum*; October 2023; Cornell Center for Real Estate and Finance and Cornell Center for Hospitality Research; cref.cornell.edu.

⁶ See: CoStar.com

⁷ "COVID-19's Impact on the U.S. Hotel Sale Transaction Market | Boston Hospitality Review," accessed June 3, 2023, <https://www.bu.edu/bhr/2021/03/25/covid-19s-impact-on-the-u-s-hotel-sale-transaction-market/>

EXHIBIT 2

Time trend of number of hotel owners



to hotel units' financial performance.⁸ Therefore, we expected that studying the changes in hotel ownership during the pandemic would help us understand the industry's recovery following the pandemic.

Hotel Distribution

Our investigation focuses on the change in ownership of the 66,397 hotels in the CoStar database. Our analysis extends only to hotels that remained in existence during the entire COVID period. We also examined the hotel distribution over geography, operation type, hotel class, and location (see Exhibit 1). In the year 2019, a preponderance of hotels included in our study are in the south (41.75%) and located in small-town (32.66%) or suburban (31.41%) areas. In terms of hotel class, nearly half of the hotels are economy, followed by upper-midscale (22.46%) and midscale (13.68%). Two major types of operation are franchise (branded hotels managed by owners or third parties), which account for 51.87 percent of the studied hotels, and independent hotels (not associated with brands), representing

⁸ Qu Xiao, John W. O'Neill, and Anna S. Mattila, "The Role of Hotel Owners: The Influence of Corporate Strategies on Hotel Performance," *International Journal of Contemporary Hospitality Management* 24, No. 1 (January 1, 2012): 122–39, <https://doi.org/10.1108/09596111211197836>.

EXHIBIT 3

Ownership frequency table (2019–2022)

| Number of Hotels | 2019 | | 2022 | |
|------------------|------------------|------------|------------------|------------|
| | Number of Owners | Percentage | Number of Owners | Percentage |
| 1 Hotel | 36,696 | 85% | 35,740 | 85% |
| 2 Hotels | 3,698 | 9% | 3,697 | 9% |
| 3 Hotels | 1,098 | 3% | 1,118 | 3% |
| 4 Hotels | 466 | 1% | 476 | 1% |
| 5 Hotels | 262 | 1% | 287 | 1% |
| 5+ Hotels | 854 | 1% | 885 | 1% |

43.10 percent. Chain management (branded hotels managed by those brands) constituted the remaining 5.04 percent of hotels in the survey. We note that the distribution across sectors remains consistent during the pandemic.

Hotel Ownership

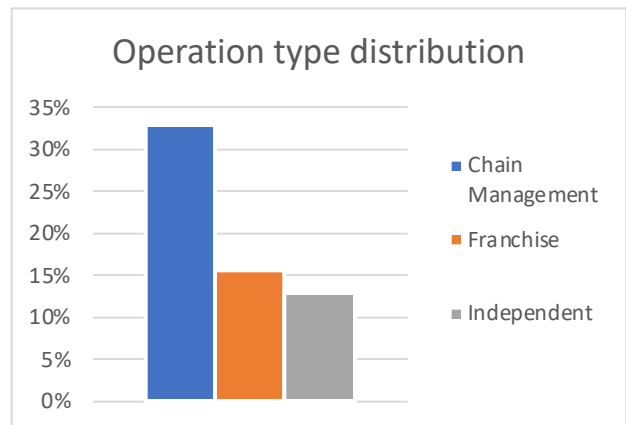
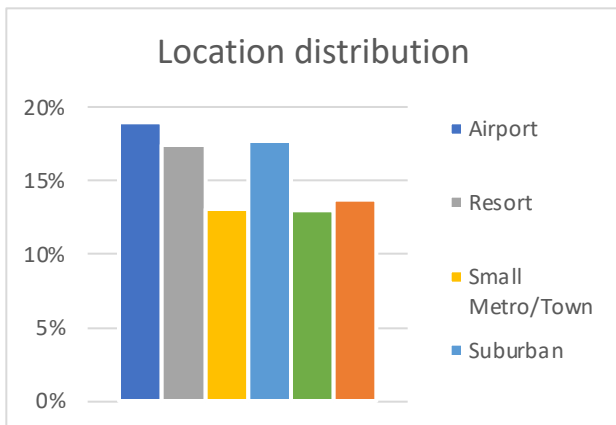
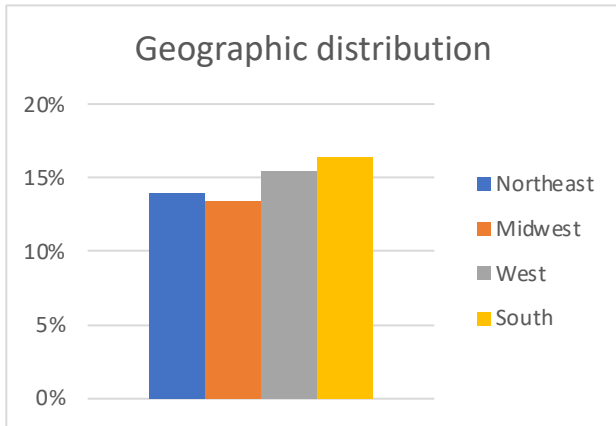
As a point of departure, the number of owners declined during the course of our study, from 43,074 to 42,203, or by 871 (see Exhibit 2). While an owner's exit might normally result in a notable shift in market concentration in many industries, the decentralized structure of hotel ownership has resulted in minimal changes to the Herfindahl-Hirschman Index (HHI).⁹

In particular, more than 85 percent of owners possess only one hotel, while a mere 2 percent of owners own five or more hotels (see Exhibit 3). This suggests that the exit and entry of most owners had a limited impact on the overall market. Indeed, upon comparing the market prior to and after the onset of COVID, we observed no significant changes in the overall ownership distribution.

⁹ A measure of market concentration and competitiveness, the Herfindahl-Hirschman Index (HHI) provides a comparison of the size of companies relative to the size of their industry in which they operate. For example, see: [investopedia.com](https://www.investopedia.com).

EXHIBIT 4

Percentage of hotels with transactions by category



Transaction Distribution

We investigated the distribution of transactions across geography, operation type, hotel class, and location (see Exhibit 4). Notably, we present the transaction distribution weighted by the number of hotels, rather than use unweighted data. This approach considers that sectors with a greater number of hotels are more likely to have transactions. The charts presented here illustrate the distribution of weighted transactions, which can be interpreted as the percentage of hotels that have recorded transactions within each sector.

Scale of Transactions

During the period of 2020 through 2022, there was a total of 11,547 transactions (see Exhibit 5). Out of these, 11,030 hotels (16.61%) had at least one trade. Among the traded hotels, the majority, 10,537 (95.53%), had only one recorded trade. However, 470 hotels (4.26%) recorded two trades, 22 hotels had three trades, and a single hotel had four trades during the pandemic period.

EXHIBIT 5

Time trend of number of transactions

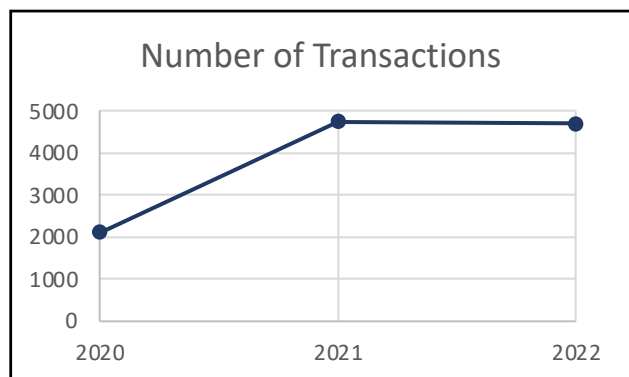


EXHIBIT 6

Time trend of sale price

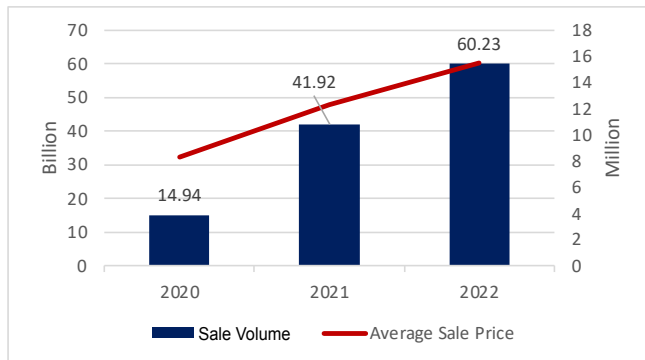


EXHIBIT 7

Time trend of sale price per square foot

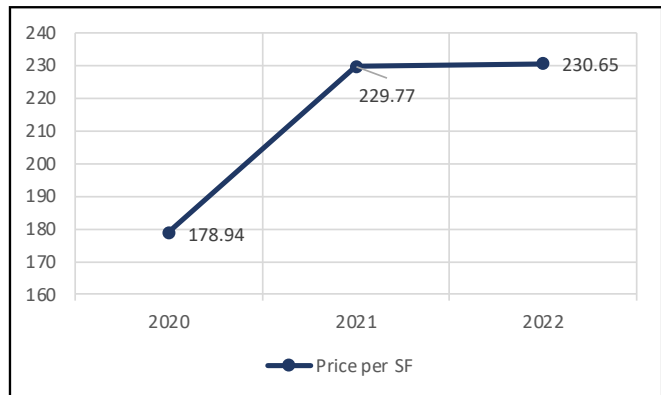


EXHIBIT 8

Transaction frequency

| Number of Transactions | Number of Buyers | Category Percentage |
|------------------------|------------------|---------------------|
| 1 | 5,544 | 84% |
| 2 | 608 | 9% |
| 3 | 178 | 3% |
| 4 | 79 | 1% |
| 5 | 56 | 1% |
| 5+ | 113 | 2% |

In terms of sale prices, the hotel industry witnessed a total trading volume of 117.09 billion USD during the COVID-19 period (see Exhibit 6). This volume showed a continuous increase from 2020 to 2022. Additionally, the average sale price per hotel also experienced an upward trend, rising from 8.33 million USD to 15.54 million USD.

Considering the variation in hotel sizes, we also calculated the price per square foot by weighting the sale price with the size of each hotel (see Exhibit 7). This analysis revealed that the price per square foot exhibited a substantial increase, from around 179 USD to about 230 USD, in the initial year of the pandemic (i.e., 2020). Subsequently, the price per square foot remained relatively stable until the end of the Covid-19 period (that is, 2022).

The Players

In our transaction data, a total of 6,578 different entities bought hotels during the pandemic period (see Exhibit 8). Of these, a majority—5,544, representing 84.28 percent—completed just one transaction, while 608 entities engaged in two transactions and 178 carried out three.

Although we previously noted a decrease of 871 hotel ownership entities post-pandemic, this figure only represents the net change without accounting for the dynamics of market entry and exit. Taking that matter into account, 4,514 buyers entered the hotel industry, while 5,385 existing owners exited the industry when they divested their properties.

Increase in Private Equity

When we classify the hotel industry players by five ownership categories, we find that while the overall distribution of ownership type did not show much

EXHIBIT 9

2019 Distribution by ownership type and market share

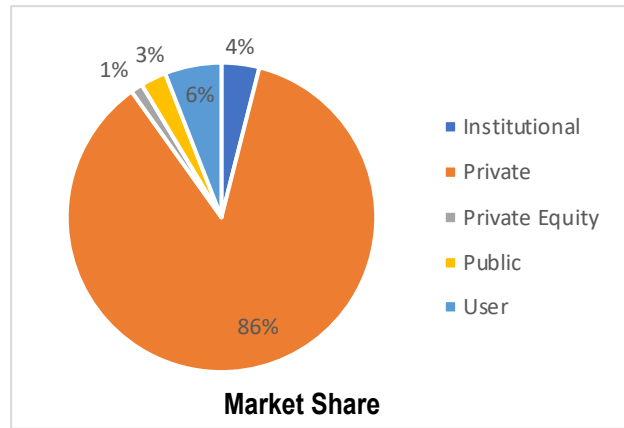
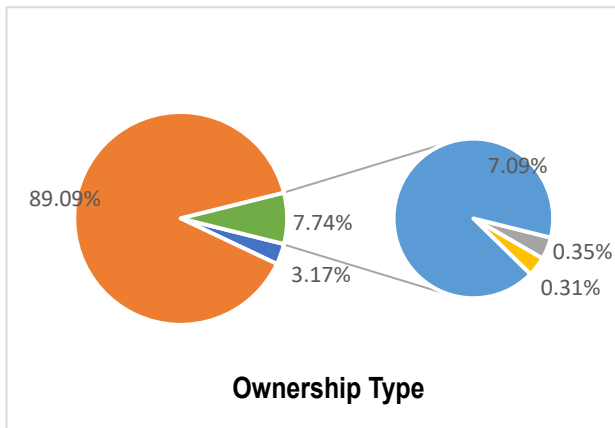
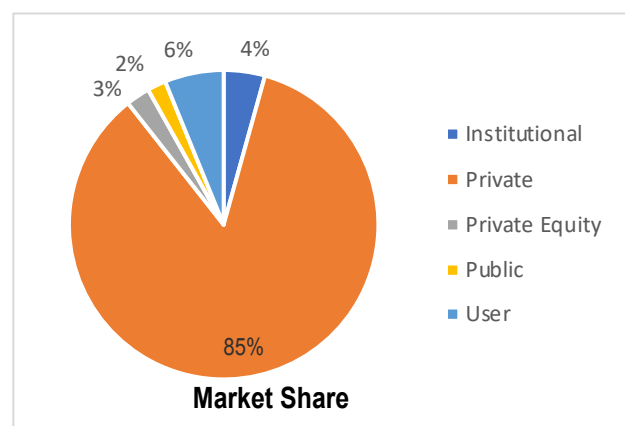
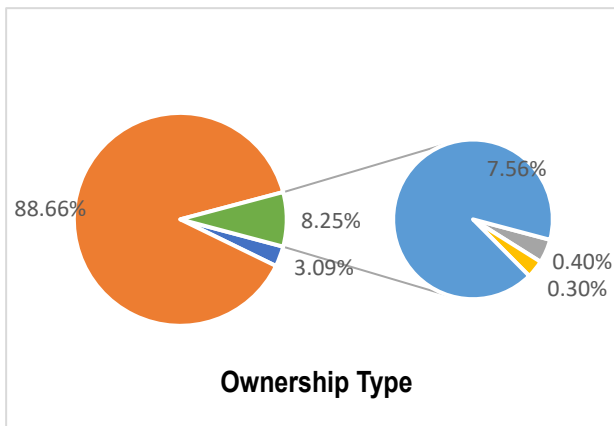


EXHIBIT 10

2022 Distribution by ownership type and market share



change in the wake of COVID, private equity holders saw an opportunity. The five ownership categories are institution, private, user, public, and private equity.¹⁰ The main players both before and after COVID

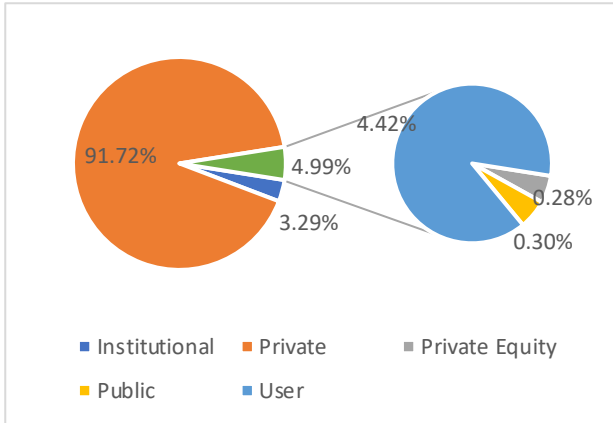
¹⁰ According to Costar’s classification, these five categories of owners are defined as follows: (1) *Institutional entities* are those that manage substantial pools of capital, including banks, insurance companies, pension funds, and sovereign wealth funds, with a primary focus on investment activities to serve their stakeholders’ financial objectives; (2) *Private individuals or entities* include property developers, private REITs, or other private ownership forms, and are characterized by their non-public trading status; (3) The *user category* encompasses a diverse group of end-users such as corporations, educational institutions, governments, and non-profit organizations, which utilize real estate and financial services for their operational requirements rather than for investment purposes; (4) *Public entities* are those that are publicly traded on stock exchanges, including listed investment funds, public REITs, and real estate operating companies, all of which seek to generate returns for their shareholders through various investment strategies; and (5) *Private equity* represents equity funds that are not publicly listed and typically invest in private companies or conduct buyouts, aiming for strategic growth and profitability.

are in the private sector, namely, individuals, private developers, and private equity. Although private equity holders account only for 0.4 percent of the number of owners, they expanded their market share substantially, from 1 percent to 3 percent (compare Exhibit 9 with Exhibit 10).¹¹

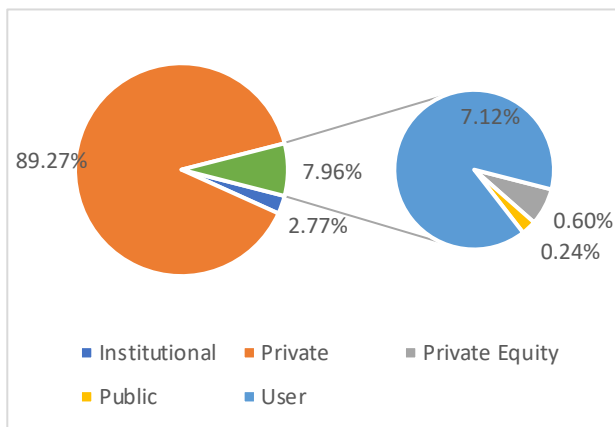
¹¹ The distribution of ownership types is determined by dividing the number of owners of a specific type by the total number of owners. Market share is calculated by dividing the number of properties owned by a certain type of investor by the total number of properties.

EXHIBIT 11

Ownership type of exiting and entering hotel investors, 2019–2022



Exiting Investors



Entering Investors

Indeed, much of the market turbulence involved private sector players exiting and entering the market (90% of transactions). However, as shown in Exhibit 11, the number of newly entering private equity investors is twice that of the exiting private equity holders (0.28% exiting; 0.60% entering).

In sum, our analysis indicates that private equity holders were the largest buyers during the Covid period. These buyers took advantage of the opportunity to acquire hotels at the relatively low prices that prevailed early in the pandemic period. The investors apparently anticipated a recovery in the hospitality sector once the pandemic subsided. Recoveries of this type have occurred in past hotel real estate market dislocations. A similar recovery seems to have occurred for most hotels with the recent pandemic. The findings in this article suggest that the private equity investors viewed the pandemic as an opportunity for long-term investment. ■

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