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Opinions

Sealing the deal in 2020

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An off-market transaction could be a good choice for landing your next deal in 2020.

By Nick Plasencia

To better navigate a marketplace brimming with both quality assets and active capital, buyers and sellers are more frequently considering off-market transactions to secure deals. While the traditional process offers clear benefits to all parties, off-market discussions present strategic advantages by establishing a more personal bidding atmosphere. Conventional marketing practices oftentimes appear most prudent, but this may not always be the case in 2020's increasingly crowded transaction market.

A streamlined approach

Off-market transactions are discrete by nature, allowing sellers to explore top pricing potential without risking a visible failure should the offering, be it a single property, resort or portfolio, not ultimately trade. In off-market transactions, sellers and their advisors are oftentimes able to guide to higher values without fear of alienating a large potential buyer pool. If a deal is not consummated, ownership still reserves the right to take an asset to a broader market without the overhang of a failed prior process or buyer fears of unrealistic pricing expectations.

This more confidential strategy also minimizes the potential stress endured by operational staff and ownership during a transaction period. A full-fledged sale process can raise concerns among property staff about job security, while frequent property tours and diligence requests can become taxing for the operating team's senior managers. If operators aren't preoccupied with outside scrutiny, they are able to focus on their duties, while ownership benefits from fewer confidentiality agreement negotiations and less frequent transaction correspondence. The off-market approach can often allow operators and owners to focus on what they do best: maximize the operating performance of the asset.

Making a splash

It should come as no surprise that for many of the above reasons, a growing number of today's most qualified buyers and sellers have come to prefer off-market transactions to the traditional broad marketing process. Large institutions, real estate investment trusts, private equity firms and high-net-worth individuals are accustomed to spending time and resources underwriting deals only to find themselves outbid by groups offering a higher purchase price, but sometimes with less direct access to funds and a lower certainty of closure.

The most qualified buyers are frequently hesitant to fully engage with a transaction unless they believe there is a legitimate chance for them to come out on top. Buyers may be willing to wait for a rebound opportunity if deals don't pan out with the selected bidder, but this typically is not a preferred strategy. Off-market arrangements incentivize the most qualified bidders to dig in aggressively from the outset.

The psychology of buying and selling

Exclusivity of the potential deal can also induce a pricing premium in an off-market transaction. Investors may be more willing to "pay up" if they are aware of an exclusive opportunity to acquire an asset without widespread competition. Off-market bidders may also be more likely to buy in to upside potential opportunities and convince themselves to be more aggressive on pricing, lest the opportunity pass them by and someone else capitalize on it. Sellers often stand to capture an exclusivity premium in the purchase price derived from aggressive underwriting.

Lastly, off-market transactions are not reserved specifically for hotly-contested assets and can also benefit assets with challenges or sellers with limited resources or time. By taking an asset with a reduced buyer pool off-market, sellers can focus their available resources on the most reliable bidders without courting nonessential buyers and "tire kickers." Assets that are suffering from unique physical challenges, are located in tertiary markets, or are saddled with unattractive debt or management encumbrances oftentimes have limited buyer pools. These assets may be better served by a more direct, targeted marketing effort than a traditional broad offering process.

Sticking to tradition

It would be a mistake to gloss over the positives of keeping your transactions on the market, as not every asset benefits from a discreet marketing strategy. On-market offerings allow for a wide range of interested parties to pursue an asset, usually resulting in competitive bidding.

For example, an investor traditionally focused on premium-branded, select-service hotels may not make the short list as a buyer for an off-market offering of an independent boutique hotel. However, if that group's investment criteria has recently changed, or they have a strategic or emotional tie to a market that the seller and investment advisor are unaware of, they will undoubtedly benefit from exposure to the asset in a widely marketed process.

Additionally, while keeping assets off the marketplace may help owners in some circumstances, the simple laws of supply and demand typically prove effective in generating competitive pricing pressure. Quality listings have a scarcity value and are in high demand. A full marketing campaign can escalate competition, often leading to multiple rounds of bidding. In some situations, in addition to maxing out their prices, interested potential purchasers have even demonstrated a willingness to offer non-refundable deposits at the execution of a purchase and sale agreement in order to secure a competitive fully marketed deal.

Staying flexible

The lodging investment landscape is set to be competitive throughout 2020, but sellers who are strategic in their disposition processes have a lot to gain from offering quality investment opportunities to a market eager to deploy capital. Be flexible in your approach, think critically about the most advantageous marketing method for each asset, and don’t be afraid to shake things up with the assistance of your trusted investment advisors.

Nick Plasencia is a vice president with The Plasencia Group and specializes in the disposition of full-service, premium select-service, boutique and resort properties, both in single-asset and portfolio transactions. He has personally transacted several hundred million dollars of lodging assets across all regions of the United States, and has advised clients ranging from privately held owner-operators and high-net-worth individuals, to management companies, private equity funds and REITs.