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Destination Hotels operates resort locations, such as in Vail, Colo., top, while Commune is largely in cities, including New York.

Hotels Ramp Up Mergers

Deal activity picks up in the sector as owners look to push back against rivals such as Airbnb

By Craig Karmin and Dana Mattioli

Hotel companies are ramping up their merger activity, hoping a broader reach will help them regain ground lost to upstart home-rental companies and online travel agents.

Commune Hotels & Resorts and Destination Hotels are the latest hospitality companies to merge. The two privately held firms on Friday announced they completed a deal to create the largest independent operator of boutique hotels—properties that focus on design and often appeal to a younger crowd.

The combined company has 92 hotels in seven countries and $2 billion in property-management revenue.

In a cross-border transaction last month, French lodging giant **Accor** SA agreed to acquire **FRHI Holdings** Ltd., the Toronto-based parent company of Fairmont, Raffles and Swissotel brands. The deal valued the company at more than $3 billion.

Driving much of the deal activity is the negotiating power that comes with mass scale, which could be the most effective way for hotel operators to fend off rising competition from tech-oriented companies that have been eating into hotel profits over the past decade, analysts say.

Online travel agents like Expedia Inc. and Priceline Group Inc.'s Booking.com account for about 17% of U.S. hotel book-

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ings, according to a study from research firm Phocuswright. These booking channels charge fees of about 12% to 25% of room revenue, and the brands boasting the largest room inventory extract the most favorable terms.

Among other recent deals, privately-held Carlson is exploring strategic alternatives, including a possible sale or merger, for its hotel company with about 174,000 hotel rooms and the Radisson brand, said people briefed on the matter.

In one of the largest transactions ever for the industry, Marriott International Inc. in November agreed to pay $12.2 billion to acquire Starwood Hotels & Resorts Worldwide Inc. The deal would create the world's largest hotel company with more than one million rooms and 30 brands.

Much of the industry also is feeling the effects of home-rental company Airbnb Inc., which will account for 5.4% of total U.S. room supply in 2016, up from 3.6% last year, according to an estimate from Goldman Sachs Group Inc. Only five hotel operators have a market share greater than 5%, Goldman said.

Marriott Chief Executive Arne Sorenson referred to home-rental companies and Google Inc., which offers hotel reviews and panoramic views of properties from its site, on an analyst call when the merger was announced.

"We became more convinced that strategically we could drive better value and compete better by being bigger," he said.

Bigger hotel operators have greater brand recognition, expanded loyalty programs and more robust marketing budgets, analysts said. At a time when most major hotel companies own few of the properties they manage or franchise, those attributes make a brand more attractive to owners.

Part of the hotel merger momentum also might be tied to the business cycle. After years when hotels were able to charge more for their rooms and to grow revenue rapidly, the hotel business cycle is slowing from weaker global economic growth and new supply coming on in the U.S.

"Companies that are finding it hard to grow organically are starting to look to grow through acquisition," Destination Hotels President Jamie Sabatier said in an interview Friday.

Other operators view deals as a way to plug holes in a brand portfolio. Accor picked up three luxury brands in its acquisition of FRHI, boosting to 35% from 20% of its hotel management revenue derived from high-end hotels, the company said.

Hospitality deals worldwide totaled $58.9 billion last year, the industry's strongest since 2007, according to Dealogic. But that consisted mostly of many smaller deals and represented a tiny fraction of the trillions of dollars in overall deal activity.

Overall mergers-and-acquisition activity has been muted so far this year after reaching an all-time record in 2015. There have been $114.2 billion in deal announcements to date, down 33% from the same period last year, according to data provider Dealogic.

Some hotel experts think the Marriott deal, which caught the market by surprise after earlier indications from the company that it wasn't interested in a major transaction, has motivated boards to look more aggressively at takeover prospects.

"The Starwood-Marriott transaction created momentum," said Phil Zrihen, a managing director specializing in the hospitality sector for investment bank Houlihan Lokey Inc.