

# Re-Purposing of Hotel Assets — What Does it Entail?

The UAE hotel sector has been increasingly overestimating the market demand over the past few years and as such has been suffering from an oversupply of hotel keys.

The Covid-19 pandemic has nothing but accelerated the deterioration of market conditions which was expected regardless of the virus, only a bit later. For the market to reach equilibrium and recover from the decline in hotel rates and occupancies, it is no secret that future supply should be carefully studied. Repurposing of hotel assets to better address the actual current and future demand has also been a major topic of discussion among industry experts.

We at Grant Thornton UAE have been part of these discussions and are hereby summarising our views on the repurposing of hotel assets to residential or long-stay properties.



## Steady Cash Flows

The pandemic has put immense pressure on hotels to maintain the desired level of liquidity. For hotel owners looking for steady cash flow in turbulent times, converting their asset into a residential building would be a good option to decrease volatility. Besides, the UAE hospitality market is highly seasonal given the hot summer months and pleasant winter, which is not the case with residential properties that are generally not affected by seasonality.



## Lower Operating Costs

A major portion of hotels fixed operating costs pertains to annual maintenance contracts in line with the requirements of local authorities such as the Dubai Municipality and Dubai Civil Defense. Since residential buildings are not bound by such requirements, fixed operating costs tend to be lower by 15% – 20% in residential properties than they are in hotels.



## Longer Renovation Cycles

It is recommended that hotel assets undergo major renovations every 10 years, failing which would affect the hotel's performance. Residential properties renovation cycle is much longer, and performance is not as dependent upon such works as it is in hotels.

## Reduced Risk Exposure

It comes as no surprise that hotels invest in third party internal audit and mystery shopping services. Hotels face the risk of fraud and other forms of revenue and inventory leakage. Besides, the higher the number of parties involved in a business, the higher the risk, whatever that may be. Residential businesses offer minimal exposure to risk given the reduced number of parties involved, in addition to the restricted payment methods generally accepted.





## Lower Return on Investment

The saying “the higher the risk, the greater the return” holds true. Although residential buildings offer steady income and cash flow, the return on capital is certainly much lower than what hotels offer. The high amounts invested in hotels development may therefore not be offset by the returns of a residential business.

## Opportunity Cost

While the prospects for a rosy near future of hospitality still look slim, the rapid rollout of the COVID-19 vaccine is expected to expedite the recovery of the sector, especially after travel restrictions ease up and people restore confidence in travel. The UAE will also benefit from the Expo 2021 that is fast approaching and expected to attract regional and international visitors. Hotel owners converting their properties into residential buildings may not be able to capitalise.

## Re-Modelling Costs

Converting hotels into residential buildings may require significant re-modelling costs, legal costs and assets disposal costs which should be considered when making such a decision.

It is evident that several factors affect the viability and potential success of repurposing a hotel into a residential or long-stay property. From re-modeling and operating costs to long term prospects and associated risks, comparing both operating models is essential before any decision is taken. Should the owner decide to proceed with repurposing their hotel, a detailed project plan should be prepared with the relevant specialists.



Grant Thornton UAE aims to provide you with updates regarding the latest developments in the Hospitality industry within the country.

For more details with respect to this article or queries on other Hospitality issues, please contact the Hospitality Industry Lead, whose details are given below.



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