

**HOTEL PROPERTY DEVELOPMENT:  
A FRAMEWORK FOR SUCCESSFUL DEVELOPMENTS**

by

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## **PREFACE**

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This dissertation, *Hotel Property Development: A Framework For Successful Developments*, is the result of my passion to develop and construct hotels, and was born from a desire to understand the full scope of hotel property development.

Working in the hotel development and construction industry, I often contemplated the reasons why some hotels were successful, whilst others branded failures. No single comprehensive answer was available in published literature nor did industry professionals provide an encapsulating explanation.

This lack of understanding motivated my research in hotel property development, and established an interest in a field not yet extensively explored or published.

All commercial and public organisations, to be successful, should comply with a mix of critical success factors that is unique to their environments. Similarly, hotel developments should subscribe to a mix of critical success factors, which are incorporated during the development process.

A hotel business consists of two distinct components – the tangible (building, furniture, fittings and equipment) and intangible parts (service orientated business). It could be taken for granted, for a hotel development to be successful, that all tangible and intangible critical success factors should be incorporated during development in a specific mix and manner.

The question is what are the tangible and intangible critical success factors, how should these factors be combined, and at what stages in the development process should the factors be combined?

It became clear to comprehensively understand and explain the full scope of hotel property development, that all aggregate components representing the whole entity of hotel development had to be analysed and combined in a single document.

In an attempt to answer these questions, the critical success factors for hotel property development are established as a secondary dissertation objective, and subsequently combined in a hotel property development framework that forms the primary objective of the study.

The dissertation literature review identifies the critical success factors for hotel development in the process of answering the following questions:

- What is a hotel and hotel business?
- What are the constituent parts a hotel business?
- What is hotel property development?
- What is included in the scope of hotel property development?

The primary objective of the study, the empirical study, explains how the hotel development framework was established and validated.

Hotel Property Development: A Framework For Successful Developments consists of five basic and interrelated components:

- **Section A – Introduction**, explains the prerequisites for a Masters Degree dissertation as defined by the University of Pretoria.
- **Section B – Literature review**, establishes the basis on which the third component section C is founded.
- **Section C – Empirical study**, explains the development and validation process of the proposed hotel property development framework.
- **Section D – Conclusion**, draws the study together and closes with recommendations.
- **Section E – Addendums and Bibliography**.

In an effort to orientate the readers and unambiguously explain the hotel property development body of knowledge (dissertation literature review: section B), a dissertation component guide or ‘road map’ is included at the outset of each chapter to highlight the text covered in the subsequent section. It should be noted that this is not the hotel property development framework, but merely a visual guide.

The dissertation literature review (section B) starts by explaining the principles of a hotel business in chapter 3. The tourism industry, the next chapter (chapter 4), briefly explains the important basis (motivator) tourism forms for hotel and hotel development businesses.

In chapter 5, the dissertation steers towards property development in general and more specifically to hotel property development.

Chapter 6 introduces the concept of strategic management and the application of this in hotel property development.

Hotel property development feasibility studies guide the decision whether to develop or not. The feasibility study process is illustrated in chapter 7.

In the feasibility study explanation, the market analysis and financial feasibility are briefly covered. As imperative components of the feasibility process, the hotel market analysis and financial feasibility processes are comprehensively explained in chapter 8 and 9.

Chapter 10 deals with risk management of hotel developments, followed by chapter 11, which explains financing of hotel property developments.

A wide variety of project consultants could be appointment, depending on the experience of the project initiator or client. The selection of a competent development team is dealt with in chapter 12. After the appointment of a project team, the design phase commences.

Chapter 13 contains the design, documentation and implementation phase of a hotel development, forming yet another very important step to any successful developments.

The literature review concludes with a brief discussion of the construction phase in hotel property development.

## **ACKNOWLEDGEMENTS**

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It is with great appreciation that I acknowledge the contribution to my current career, of three hotel development professionals, who unknowingly served as my mentors to establish and guide my passion for hotel developments. Firstly, Mr. Rod Oosthuizen of SIP Project Managers, appointed me to my very first hotel project where I was introduced to the variety of nuances which distinguishes hotel property development from most other types of property development. The second person is Mr. Jeff Forrer, Development Director of Global Resorts and Casinos, who taught me how to conquer obstacles by energetically tackling it head-on, with an absolute determination to succeed. Finally, Mr. Dean Murphy of Mirage Leisure and Development, who from humble beginnings, working for a building contractor on a hotel project, was subsequently appointed as a hotel development director and today is one of the most formidable global hotel developers. His ambition, aspiration and achievement will remain to serve as a tangible example, reinforcing that I could also achieve the same.

Also, I would like to thank my wife Rhelda, for her support and motivation in completing my Masters of Science studies; Professor Chris Cloete, my study leader; William Carr and Thomas Hilberath of Six Continents Hotels; Peter Neeb of MLC Quantity Surveyors; Keith Randall, Development Director of Southern Sun Hotels and Resorts, James McGee, Development Director of Sun International, Marlien Lourens of Grant Thornton Kessel Feinstein Tourism, Hospitality and Leisure Specialists, for the support, guidance and information.

Finally, I give praise to Lord Jesus, who entrusted me with talents that I could apply.

## ABSTRACT

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Title of the dissertation: Hotel Property Development: A Framework For Successful Developments.

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Although there are similarities between hotel and other commercial property developments in terms of land, structures and services, it is important when developing hotels to understand that they have unique characteristics. These unique characteristics are that hotels require specific management expertise, are usually a “single-use” property, whose primary revenue is generated from a service-based industry, and has a market value that is directly related to its ability to generate future net income.

The essence of successful hotel property developments lies in understanding these unique characteristics, as illustrated in the dissertation literature review. In addition, the dissertation identifies various critical success factors for hotel development which in turn is incorporated into a hotel property development framework, establishing a practical ‘road map’ for successful hotel developments.

The literature review incorporates a wide range of hotel topics, such as the principles of a hotel business, fundamentals of the tourism industry as a motivator for hotel development, property development in general, hotel property development, strategic hotel management, hotel property development feasibility studies, hotel market analysis, financial feasibility, risk management of hotel developments, financing of hotel property developments, the project team and consultants, the design phases, and finally the construction phase.

The dissertation empirical study tests the validity of the hotel property development framework, by presenting it to and questioning hotel development professionals in intensive direct interviews.

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**Section A**

**INTRODUCTION**

## **1 Introduction**

### **1.1 Research Motivation**

Although there are similarities between hotel and other commercial property developments, the hotel development process have unique and very specific characteristics.

From extensive involvement, reading and researching property development over the last twenty years, various property development processes were observed. What clearly transpired in practice, from reading and research was the total absence of a hotel development framework.

The total absence of a hotel development framework, served as motivation to establishing a comprehensive and definitive hotel property development framework, which included critical success factors and components for hotel developments.

### **1.2 Dissertation Hypothesis**

*“Does the hotel property development frameworks, proposed in this dissertation called **Hotel Property Development: A Framework For Successful Developments**, establish a practical and comprehensive property development framework for developing successful hotels?”*

### **1.3 Dissertation Objectives**

The dissertation objectives were categorised as either primary or secondary objectives. The secondary objective established a body of knowledge from which the primary objective drew factors and components.

The secondary objective was to establish the critical success factors for hotel development, which were identified by addressing the following questions:

- What is a hotel and hotel business?
- What are the constituent parts a hotel business?
- What is hotel property development?
- What is included in the scope of hotel property development?
- What are the criteria for a successful hotel development?

The primary objective of the study was to test the validity of the hotel property development framework.

### **1.4 Literature Review**

The dissertation research originally commenced with internet search engines, such as [www.yahoo.com](http://www.yahoo.com) and [www.google.com](http://www.google.com), resulting in several referrals (internet links) to professional organisations. These professional hotel development organisations' websites contains a wealth of information, direction and research possibilities. Unfortunately, but understandably, commercial organisations are reluctant to furnish any information of substance, unless you are willing to contract their services. However, some of the more reputable hotel development consultants publish regular newsletters, either on the internet,

fax or mail. Examples of these consultants are HVS International (HVS International Web Page), Jones Lang LaSalle Hotels (Jones Lang LaSalle Hotels Web Page) and DTZ Consultants (DTZ Consultants Web Page). In addition to regular newsletters, some hotel development consultants' webpages contain valuable information. Examples of these are Andersen Consulting (Andersen Consulting Web Page), Arthur Andersen Real Estate Services (Andersen Consulting Web Page), BDO Hospitality (BDO Hospitality Web Page), Driver Jonas Consulting (Driver Jonas Consulting Web Page), Hotel Online (Hotel Online Web Page), Hotel Consulting International (Hotel Consulting International Web Page), Global Hospitality Resources (Global Hospitality Resources Web Page), to name a few.

Large volumes of general information pertaining to some form of hotel development were found on the webpages of international newsmagazines, newspapers and television channels. Examples of these are The Economist (The Economist Web Page), News Week (News Week Web Page), Washington Post (Washington Post Web Page), Online Newspapers (Online Newspapers Web Page), CNN (CNN Web Page) and BBC Online (BBC Online Web Page).

Internet bookshops, such as [www.amazon.com](http://www.amazon.com) and [www.blackwells.co.uk](http://www.blackwells.co.uk) or professional institutes, such as Urban Land Institute (Urban Land Institute Web Page) and The Appraisal Institute (USA) (The Appraisal Institute Web Page) revealed valuable hotel development textbooks.

In addition to these hotel development textbooks, a vast number of supplementary textbooks were scanned for relevant information. Topics covered were marketing, marketing planning, hotel management, strategic management, tourism, tourism distribution, property development, franchising, feasibility studies, project management, architecture and designs.

Another valuable source of hotel related information, though few articles directly addressed hotel development, were online academic journals. These journals are accessed either directly by paying an annual subscription fee or through a university library or other libraries.

### 1.5 Dissertation Framework

Hotel Property Development: A Framework For Successful Developments consists of five basic and interrelated components:

- **Section A – Introduction**, explains the prerequisites for a Masters Degree dissertation as defined by the University of Pretoria.
- **Section B – Literature review**, establishes the basis on which the third component section C is founded.
- **Section C – Empirical study**, explains the development and validation process of the proposed hotel property development framework.
- **Section D – Conclusion**, draws the study together and closes with recommendations.
- **Section E – Addendums and Bibliography**.

## 1.6 Delimitation

The present study covers the full scope of hotel property development.

The concept **Hotel Development** is often used generically, referring to either **Hotel Property Development** or **Hotel Business Development**, if not both simultaneously. Hotel business development should not be confused with hotel property development, as there is a clear distinction between the two concepts.

Hotel business development applies to the full spectrum of hotel business, whether strategic or day-to-day operations, expanding the organisation's market exposure. Hotel business expansion could be achieved through a wide variety of actions e.g. organisational mergers, existing hotel property purchases, marketing, hotel facility renovations, hotel extensions and new-builds, marketing, branding and business repositioning.

When expanding a hotel business through facilities renovation, extensions or new-builds, organisations venture into hotel property development.

Even though hotel business development and hotel property development are two separate entities, they often function consecutively as interconnected requirements in the full spectrum of hotel development. The full spectrum of hotel development would start with strategic business management on the one side and end with the final handing over of a newly built hotel to the operator, on the other hand.

## 1.7 Empirical Study Methodology

The empirical study research, specifically pertaining to hotel property development in southern Africa by South African hotel operators and hotel property developers, is limited to only a few prominent organisations. Due to this fact, the number of primary data sources was limited to key personnel within these few prominent hotel operator and hotel property developer organisations.

The empirical study methodology could broadly be categorised as content analysis type study (Mouton, 2001), wherein secondary textual data was analysed.

Research was conducted by means of intensive interviews with key hotel development managers / directors of the few prominent hotel operators and hotel property developers in South Africa. The interviews were conducted on a personal (face-to-face) basis, and the questions asked were extracted from the respective hotel development frameworks (refer to section 'C' and addendums 'F' & 'G').

## 1.8 Empirical Study Results

The primary objective of the dissertation and empirical study was to establish whether the hotel development framework defined in section 'C', is a true reflection of the structured and sequential process, and that hotel operators and hotel property developers should follow to develop successful new hotel developments.

All hotel operators and hotel property developers interviewed, agreed that the hotel development frameworks are both correct and a crucial tool in the process of developing a successful hotel.

## **1.9 Conclusion**

Given the rapid global tourism expansion it is surprising how limited the availability of relevant hotel development text and expertise is.

This dissertation, called Hotel Property Development: A Framework For Successful Developments, contributes to the serious lack of hotel development text in two ways. The first major contribution is the literature review that culminates substantial hotel development information into a single document. The second contribution is the hotel development frameworks for both hotel operators and developers, which defines the crucial route and junctures to developing successful hotels.

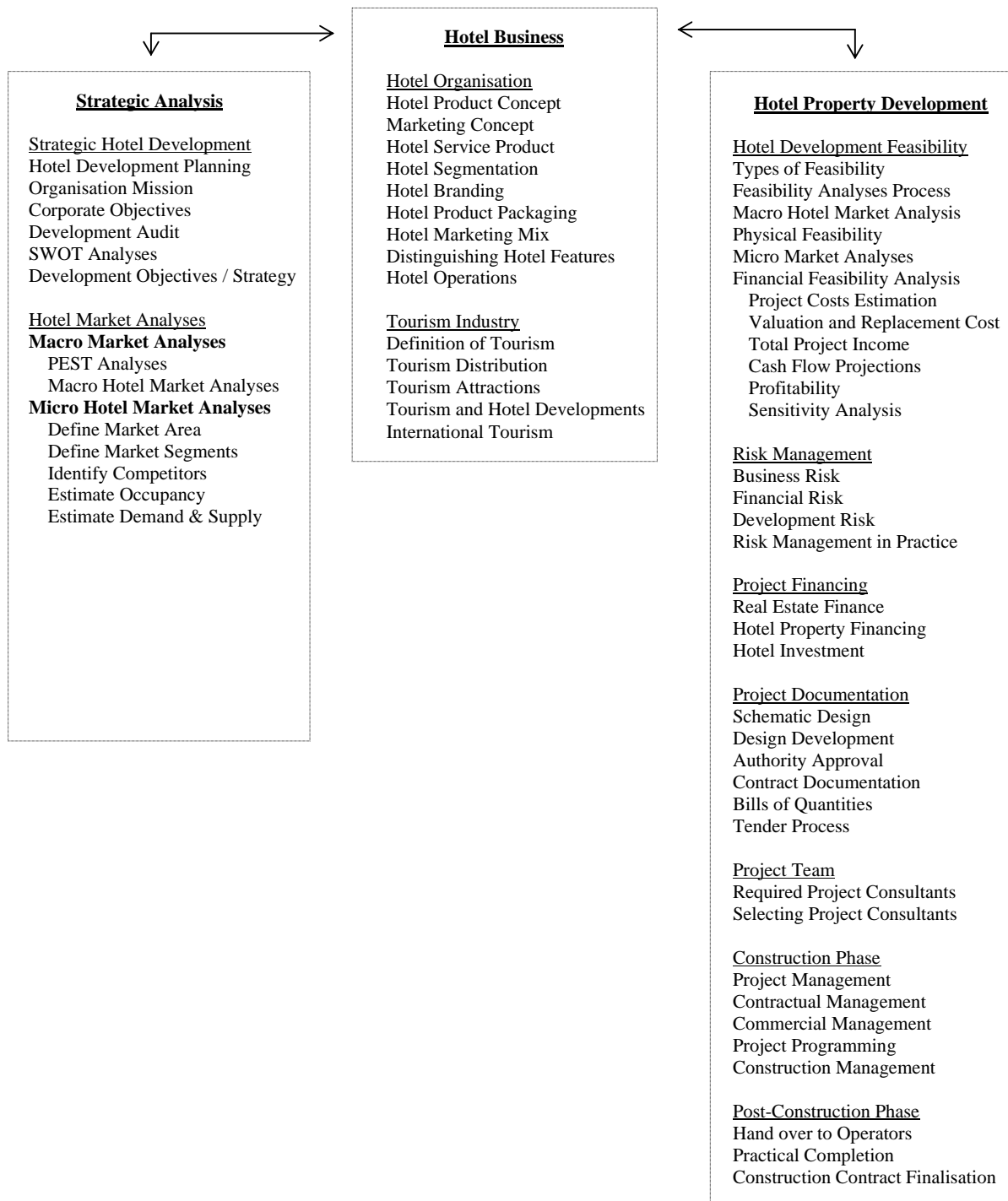
Based on the fact that the dissertation hypothesis was proved to be true, it is recommended that the content of this dissertation, i.e. the literature review and hotel development framework, be seriously considered as a guiding tool when new hotels are developed.



**Section B:**

**LITERATURE REVIEW**

## **Chapter 2: Introduction to Hotel Development**



## **2 Introduction to Hotel Development**

*“During the last few decades the hotel industry has changed beyond all recognition. There are greater opportunities than ever to succeed and, of course, to fail. Market expansion has been associated with an ever more discerning consumer, who has come to expect that hotel facilities and services reach a minimum standard of comfort and convenience.”* (Ransley and Ingram, 2000: xxii)

To meet the needs of the discerning hotel guests when developing hotel properties, explain Ransley and Ingram (2000), a wide range of experts must be consulted to determine how the property might be developed and what the costs might be. Such capital investments are expensive in terms of time, effort and money. The consequences of getting it wrong could affect the business adversely. After all, development projects are not undertaken every day.

Many participants in the hotel industry consider hotels to be highly complex real estate projects that involve great risk and often consume far too much time, energy, and capital. Great uncertainty, an extensive and ever-shifting array of market segments, and high expectations on the part of the parties involved, frequently make hotel development more challenging and exciting than other kinds of real estate development.

It is imperative to understand that a hotel is in fact an unusual type of business formula that combines a form of real estate with an ongoing service-orientated business. A hotel development is both a real estate venture and the creation of a new business establishment. The successful developer will understand this essential ‘**duality**’ of a hotel as both real estate and business. (Baltin et al, 1999)

Property development [and for that matter hotel property development], according to Wurtzbach and Miles (1995: 630), is a process starting with an idea or a concept that is brought to successful fruition in bricks and mortar (space) with associated services. It is a complex process requiring the co-ordinated expertise of many professionals. On the investment side, sources of financing must be attracted by the promise of sharing the cash flow generated by development in a manner that properly balances risk and return. The physical construction of the project requires co-ordination among architects, engineers and contractors. The public sector, especially local government, must approve the legality of the development in terms of zoning and building codes to name a few. Ultimately and most importantly, the user’s (the hotel guest) needs must be satisfied. This requires the developer to identify a market segment in which sufficient effective market demand will exist for the type of space to be created.

Real estate development takes place in an extremely dynamic world, which forms the essence of the development game with risks and rewards to developers, related players, neighbours of the properties and government.

Property development is a very cyclical activity (Kennedy, 1999: 18). As an example the North American economic boom in the early 1970s led to a vast new property supply exceeding mid-1970s new demand. Following the cycle of over development during the early and mid 1970s, little new space was contracted in the late 1970s causing rents to rise drastically, laying fertile grounds for the next upsurge in development. In the 1980s commercial space (office, hotel, retail, and industrial) increased by nearly 6 percent annually, which far exceeded demand growth leading to another financial crisis and a sharp

decline in new development. The last decade similarly experienced a cyclical trend with speculative developments towards the end of the 1990s, resulting in a substantial number of bankruptcies due to the Asian financial crisis causing a decline in market rental rates and investor confidence.

Kennedy (1999) further describes the hotel market as one of the most volatile construction markets, which swings widely with the ups and downs of its cycle. Over the 1993-1997 period, the very healthy and extended [USA] economic expansion encouraged an upsurge in leisure and business travel which led to an aggressive expansion in hotel development, whilst Wall Street provided new and lucrative sources of capital for hotel development. During the summer of 1998, however, the turmoil in international financial markets (fallout from the Asian financial crisis) led to a capital flight to safety and temporarily dried up sources of funding for commercial property development. This capital crunch hit the hotel industry even more severely than many of its sister sectors because of the hotel market's weakening fundamentals. Signs of overbuilding that began to appear in the core measures of hotel market performance.

An analysis performed by Andersen Hospitality Real Estate Consultants (Graham, 2001) of 25 regional hotels in the United Kingdom over a 20-year period, encompassing two periods of recession (1981 and 1993) and two periods of peak performance (1990 and 1998), indicate sustained real growth in profitability. Trading profits are shown to have increased between 2.9 and 3.5 percent in real terms over the 20-year period, however short-term volatility in earnings performance is evident.

Not only do economic trends and cycles impact on a country's hotel market stability, but also political, technological, socio-economic and other uncontrollable factors. As an example, the tourism and hotel industries are key foreign currency earners for Egypt, but there is a danger that the industries could be severely harmed by terrorism, as occurred after the Luxor massacre in November 1997. (Sixty-two German tourists were savagely gunned down, the survivors killed with knives and the killers then danced on top of their victims' bodies). This attack affected tourism in many parts of Egypt and sparked off a price war just as the sector was attempting to double hotel capacity, according to Butter (1997).

Following the tragic terrorist attacks in the U.S.A. on 11 September 2001, Jones Lang LaSalle Hotel Consultants reported that the USA and world economy was likely to slip into a bona fide recession. *"The question for hotel real estate investors is what this will do to hotel markets and investment performance? The global hotel market will be profoundly affected by the recent terrorist attacks as safety concerns, cost cutting and waning consumer confidence impact travel. The extent of the impact is difficult to assess at this point and will be largely dependent on the ultimate resolution of the conflict, including the length of the impending military action."* (The Impact of the September 11, ..., 2001: 2).

The factors affecting the macro economic environment has a direct but delayed impact on the hotel industry and business environments, which then influence hotel revenues and profitability. Consequently business fundamentals become unbalanced and negatively affect the feasibility of hotel developments. Smith Travel Research (STR) reported that the USA hotel occupancy rates declined in 1998 for the first time since 1991. Nearly half of the markets surveyed by STR saw a drop in occupancy during 1998, and further declines are expected during 1999 (Smith and Lesure, 2000). The market is likely to recover by mid to late 2002, assuming no further major economic shocks occur (The Impact of the September 11 ..., 2001). When occupancies begin to decline, average daily revenue (ADR) and

revenue per available room (RevPAR), two key measures of market performance for the hotel industry, become endangered. Once ADR and RevPAR begin to fall, hotels typically lower room rates in an attempt to recover lost revenue but more often than not, this has a negative effect on profitability, making the market less attractive to investors.

As the world economy enters the next phase in the business cycle, new hotel proposals will require feasibility studies to measure market demand and to prove that projects are economically viable. In order to avoid the problems of overbuilding, these new studies should focus on one major question (Turkel, 2000):

- Is there a market for this hotel in this location? And if so,
  - Where is that market, how large is it?
  - What are its needs?
  - How is it currently being served?
  - What share can be captured?

Turkel (2000) further recommends, that in order to make feasibility studies more realistic, a fresh look at the methodology needs to be considered, including the following important issues:

- Occupancy and average daily rate projections should reflect the real volatility in the marketplace.
- There should be a genuine analysis of the tradeoffs inherent in the yield management decisions as they pertain to both market penetration and revenue maximisation.
- There should be a serious analysis of the relative profitability of the food and beverage outlets beyond the misleading departmental profit margins provided by the Uniform System of Accounts.
- The feasibility study analysis should enable owners to decide whether to manage, lease or franchise the food outlets.

One of the major findings in the global research report, "Hospitality 2000: The Capital" by Andersen Hospitality Consultants, was that while location remains the most important factor affecting investment and lending decisions, intangible assets such as brand and human capital are gaining ground on tangible assets as an important key to hotel property valuations in the new economy. The hotel industry has always been a house divided, because companies act as both real estate owners and managers of enterprises, seeking capital to support both the property and operational sides of the business. At the same time, management must allocate capital between physical assets (the hotels they own and operate) and intangible assets (customers, the brands they own, the people they employ, the technology they use and the alliances they form) (Cline, 2001).

The main product of the real estate industry is space over time, which comes in different forms such as an apartment on a six-month lease, a beach resort time-share unit for two weeks a year, a department store in a regional shopping mall on a 30-year lease or a motel room off the interstate highway rented for one night. *"In order to have maximum value to its users, most space comes with services, i.e. utilities, maintenance, security, and someone in charge to collect the money and see that what needs doing gets done - property management, in other words."* (Wurtzbaach and Miles, 1995: 313)

Although there are similarities between hotels and other commercial properties in terms of land and buildings, hotels have particular characteristics such as normally being "single-use" properties (i.e. having little or no alternative use), requiring specific management expertise, and with a value that is directly related to their ability to generate future net income.

*"A hotel is an establishment that provides transient lodging for the public and often meals and entertainment. Factors affecting the success or failures of a hotel development vary according to its primary function"* (Pyhrr et al, 1989: 871). This and the frequent turnover of guests (often daily) mean that hotels require more constant management than most other category of space. Hotel management includes food service and entertainment as well as the typical property management functions. The lease period is very short and to be successful, management must find tenants (guests) for spaces vacated daily, stressing the importance of hotel marketing (Wurtz bach and Miles, 1995).

Hotels and tourism development are often criticised that they can destroy the attractiveness of a sensitive location. This must be balanced against the extensive economic benefits derived from tourism. Care should be taken to carefully select sites for development, which can provide the means for financing conservation. Hotels are often developed from restored historic buildings and are used as catalysts in attracting reinvestment into depressed urban and rural areas. Mindful of the need to regularly attract visitors, most designs must carefully respond to their environmental settings whether this is to blend into the landscape or to make a dramatic statement in otherwise bland surroundings (Lawson, 1997).

The above actual events and factors relating to real estate are only a few examples in a complex and dynamic environment that make up hotel property development. With this introductory illustration of the complexities involved in hotel development, the absolute necessity for a development strategy is reinforced. A real estate development strategy can only provide added value if it is orientated towards the same goals and the same objectives as those of other functional areas in the company. Companies that are successful from the point of business management, consider real estate to be a strategic asset and base the management of their real estate on an ongoing review of its relation to the company's business units and strategic plan. The ongoing review includes the periodic analysis of the company's needs in terms of alternative real estate solutions, an ongoing comparison of expenses and the detailed preparation of annual budgets and of periodic financial information.

## **2.1 Hotel Development Framework**

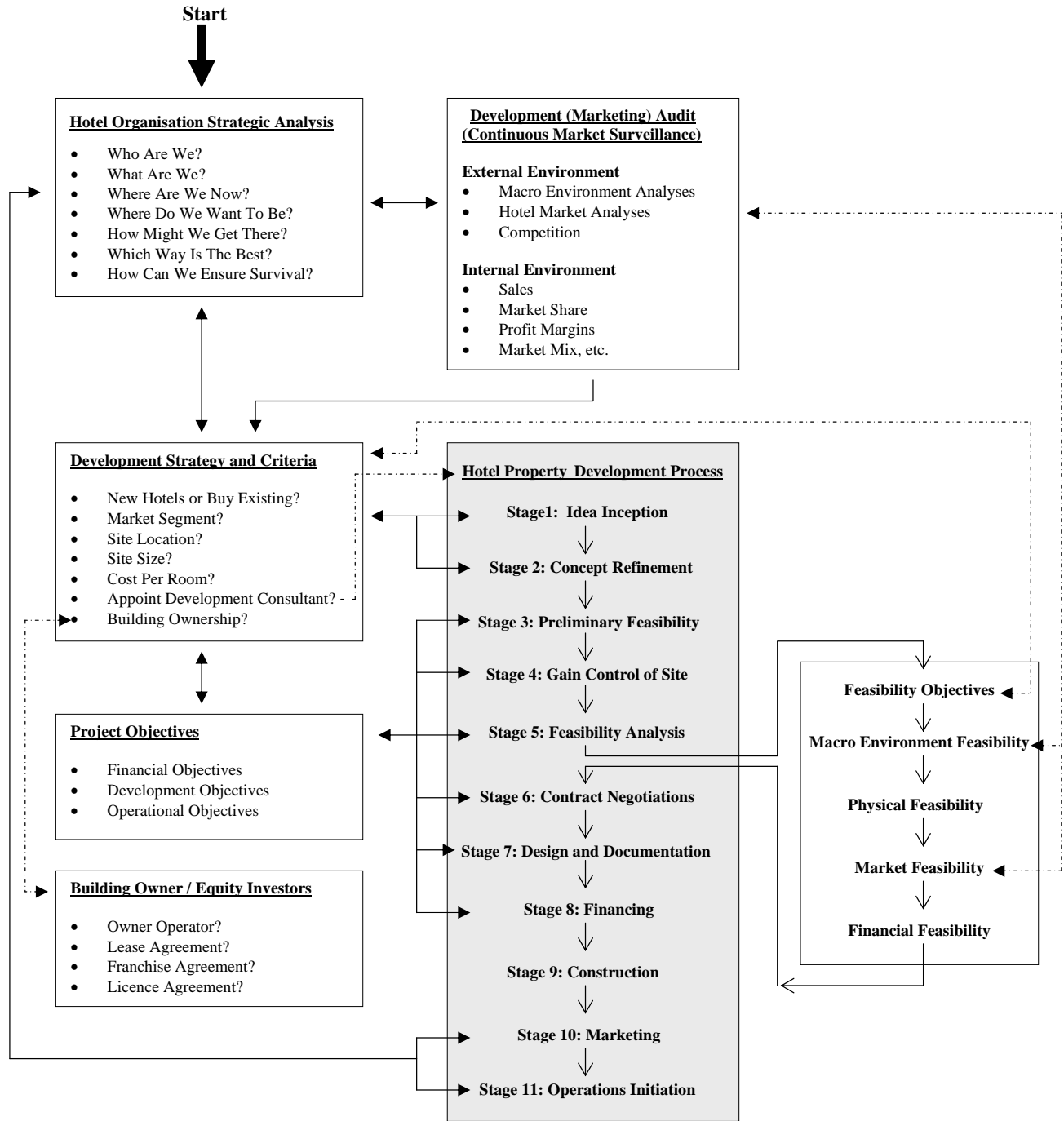
In an effort to mould this dissertation into a practical hotel development guide, the aggregate hotel development components are ultimately assembled into a single hotel property development framework, which forms the 'road map' for developing successful hotels.

As a brief introduction to the empirical study contained in section C, the two hotel property development framework scenarios are illustrated in the following.

The first development framework, exhibited in illustration 2.1(a) [Hotel Development Framework for a Hotel Operator], includes the suggested developments steps and requirements to be complied with by a hotel organisation or operator.

**Illustration 2.1(a): Hotel Development Framework for a Hotel Operator**

(Source: Culmination of views in the literature review)



The second hotel development framework explains the approach suggested for a hotel property developer, hotel development consultant, landowner or even an equity investor interested in developing a hotel. This framework exhibited in illustration 2.1(b): Hotel Development Framework for a Hotel Property Developer.

**Illustration 2.1(b): Hotel Development Framework for a Hotel Property Developer**

(Source: Culmination of all the text in the literature review)





## 2.2 Requirements for Successful Hotel Developments

To achieve success in hotel development, it is imperative for a hotel developer or hotel operator to establish a wide, but specific range of factors.

Success requirements according to Lawson (1997: 1) could generally be grouped under the following five headings:

- *Marketing*: an increasing and unsatisfied demand for accommodation stemming from the tourism, recreation and business attractions of a locality.
- *Economics*: the state of the economy and financial inducements or constraints, which may favour or restrict investment.
- *Location*: availability of appropriate sites with adequate infra-structural services and opportunities for development.
- *Enterprise*: correct interpretation of requirements and entrepreneurial organisation of the necessary finance and expertise to successfully implement a project.
- *Planning and design*: careful planning and design of facilities to create an attractive hotel which will satisfy the marketing, functional and financial criteria.

According to Cloete (1998: 116) success factors for property developments, which are relatively controllable even if only in the sense that the developer is able to choose between alternatives, are:

- Type and quality of property
- Factors regarding location
- Price, interest and costs
- Time and advertising.

There are also a number of other factors which an investor has less or no control over:

- International, national and local economic, political and social factors
- National and local government regulations (legislation, town planning and building regulations)
- Short- and long-term business confidence

Baltin and Cole (1995: 36) caution against designers who often incorrectly do what their clients think is correct, rather than what will attract the hotel guest. The successfully targeted development will focus on the market objectives it is supposed to achieve. “A targeted design begins not with colour swatches, but with an analysis of all the information bearing on the hotel's market position, which includes the following”:

- Competition.
- Available market.
- Targeted market segment, by purpose of visit.
- Guest profiles using psychographics
- Budgetary considerations.
- Consideration of potential amenities, facilities configuration and aesthetics.
- Management configuration and goals.
- Brand standards, strengths and constraints.
- Marketing and distribution capabilities.

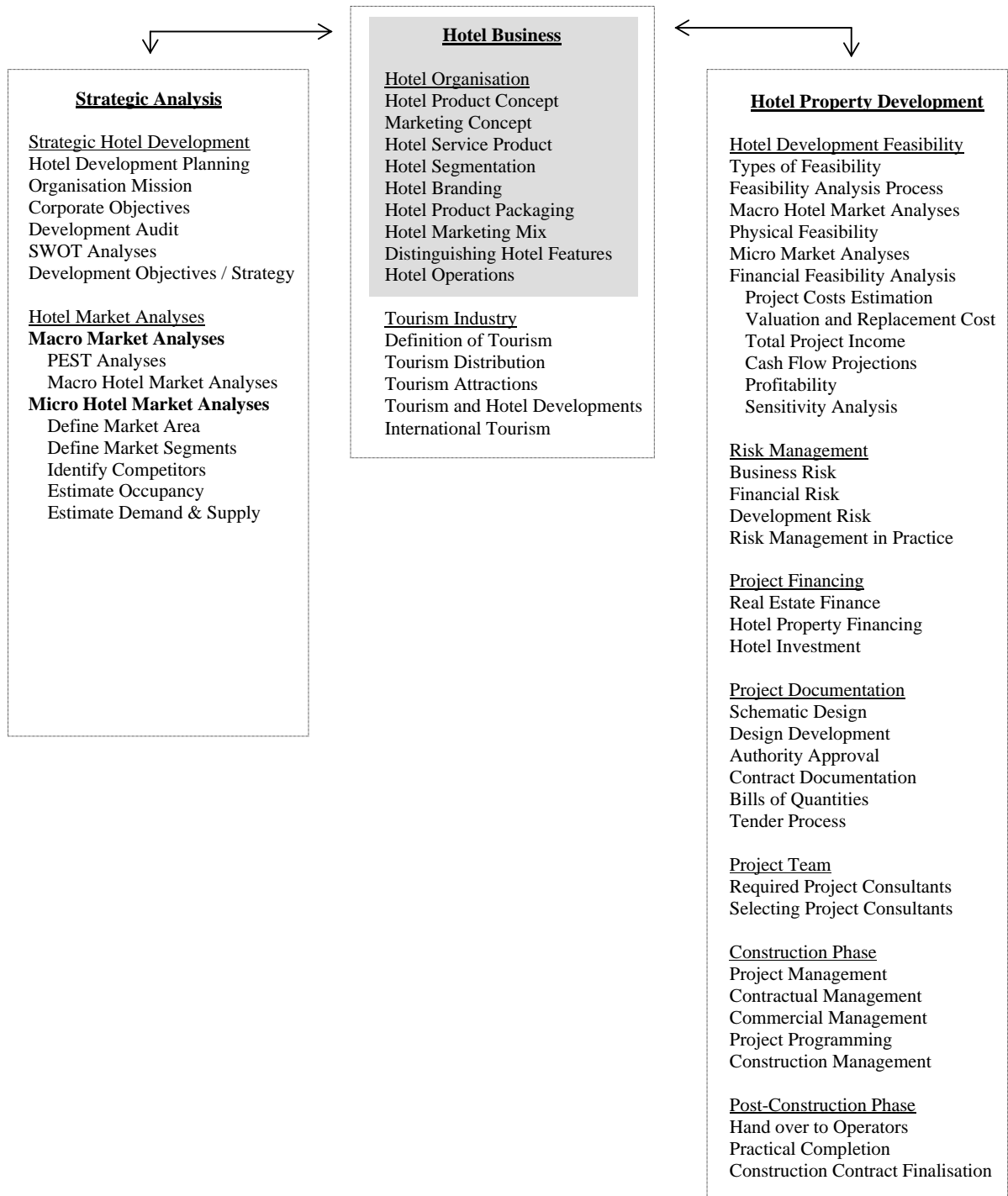
Targeted design requires as much data as possible about the potential guest, using both guest questionnaires and interviews with the hotel sales, food and beverage, housekeeping and management staff. The manager, market consultant, designer and owner can then collaborate on a focused design that will include not only decor, but also facilities configuration, pricing, amenities and marketing strategy (Baltin & Cole, 1995).

Cloete (1998: 118) summarises the various requirements for successful property development as:

- A sufficient demand for the product at a price that justifies investment.
- The identification of a cost structure that will ensure the optimum net profit.
- The architect's ability to design the product that will meet the demands of the cost structure and also ensure maximum demand.
- The development of the project in an area with a good location.
- The developer's ability to:
  - control the erection costs,
  - finance the project economically,
  - manage the development effectively,
  - lease or sell the property effectively.

## Chapter 3:

## Hotel Business

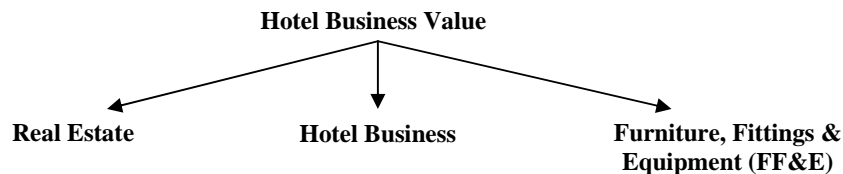


### 3 Hotel Business

The question might be asked, what the relevance of hotel and tourism management theory is to hotel property development? Belfrage (2001) answers this by explaining that the value of a hotel lies in three components, i.e. real estate, hotel business, and furniture, fittings and equipment (FF&E).

**Figure 3(a): Hotel Value Components**

(Source: Visual interpretation of Belfrage's (2000), above explanation)



Belfrage (2000: 278) further explains: *“Obviously, anyone with or without hotel experience could locate a site and construct a hotel. The creation of going concern value, however, includes selecting the appropriate affiliation, management team, marketing plan services, and even employee attitudes. How often has, a patron [hotel guest] selected an alternative property because of disorganisation, uncleanliness, or an unfriendly employee attitude? These situations can be detrimental to property value (i.e. occupancy and rate) despite payment by the ownership of franchise and management fees.”*

The above views of Belfrage emphasise the importance of hotel and tourism management theory as the body that houses the essence, definition and direction for successful hotel property development. Hence, the aim of this section is to extract from hotel and tourism management, theory relevant to hotel property development. These extracted components are then elaborated on, in an effort to illustrate the practical application within the hotel property development context.

#### 3.1 Service Product

The commonly used word ‘product’ is in reality a complex concept that needs careful definition.

*“A product is anything that can be offered to a market for attention, acquisition, use, or consumption that might satisfy a want or need. It includes physical objects, services, persons, places, organisations, and ideas.”* (Kotler et al, 1999: 14)

Many well-established definitions are primarily concerned with manufactured goods. The rise of service industries (including tourism) in recent years has led to the development of other definitions designed to modify the idea of a product to reflect the complexity of industries in which the definition of product also includes services, in addition to manufactured good. There is now a general recognition that in many service industries the product is actually a combination of tangible goods and intangible services (Swarbrooke, 1999).

McDonald and Payne (1998: 10) define a service as: “... *an activity which has some element of intangibility associated with it. It involves some interaction with customers or property in their possession, and does not result in a transfer of ownership. A change of conditions may occur and provision of the service may or may not be closely associated with a physical product.*”

Kotler’s product categorisation is cited by McDonald and Payne’s (1998: 8), as:

1. A pure tangible product, such as sugar, coal or tea.
2. A tangible product with accompanying services such as commissioning, training and maintenance.
3. A service with accompanying minor goods, e.g. property [real estate] service.
4. A pure service, where one buys expertise such as psycho analysis

Kotler et al (1999: 42) stresses the importance that a service product has four distinct characteristics, which are intangibility, inseparability, variability and perishability.

### Intangibility

Unlike physical products, services cannot be seen, tasted, felt, heard, or smelled before they are purchased. Prior to boarding an airplane, airline passengers have nothing but an airline ticket and the promise of safe delivery to their destination. Members of a hotel sales force do not sell a room, instead they sell the right to use a room for a specific period of time. When hotel guests checkout, they retain nothing but a receipt as evidence to show that they actually stayed at the hotel. Someone who purchases a service may go away empty-handed, but they have memories that can be shared with others.

Buyers look for tangible evidence that will provide information and confidence about the service to reduce uncertainty caused by services’ intangibility, as an example the exterior of a restaurant is the first thing that an arriving guest sees. The condition of the grounds and the overall cleanliness of the restaurant provide cues as to how well the restaurant is run. Various tangibles provide signals as to the quality of the intangible service.

### Inseparability

Both the service provider and the customer must be present for the transaction to occur. Customer-contact employees are part of the product, as is the example with the food in a restaurant that may be outstanding, but if the service person has a poor attitude or provides inattentive service, customers will be disappointed and reprioritise the dissatisfactory restaurant experience.

Service inseparability also means that customers are part of the product. A couple may have chosen a restaurant because it is quiet and romantic, but if a group of loud conventioners is seated in the same room, the couple will be disappointed.

### Variability

Services are highly variable. Their quality depends on who provides them and when and where they are provided. There are several causes of service variability, such as services which are produced and consumed simultaneously, limiting quality control. The high

degree of contact between the service provider and the guest means that product consistency depends on the service provider's skills and performance at the time of the exchange. A guest can receive mediocre service the one day and excellent service the next day from the same person. With regards to mediocre service, the service provider may not have felt well or perhaps experienced an emotional problem.

### Perishability

Services cannot be stored. A 100-room hotel that on a particular night only sells 60 rooms, cannot store the 40 unsold rooms and sell 140 rooms the next night. The revenue lost from not selling the unsold 40 rooms is gone forever. Restaurants are also starting to charge a fee to customers who do not show up for a reservation. If services are to maximise revenue, they must manage capacity and demand since they cannot carry forward unsold inventory.

### **3.2 Marketing Concept**

Modern organisations are influenced and function amidst a complex network of external and internal environments. To be successful the aim of organisations should be to match its capabilities with the needs of customers in order to achieve the objectives of both parties.

In keeping with the hotel property development success requirements defined before, McDonald and Payne (1998: 4) explain that marketing should be a matching process, synchronising all possible factors that influence business. The organisation has to develop strengths, either from the nature of the services it offers or from the way it exploits these services, in order to provide customer satisfaction.

It is not possible to be equally competent at providing all services for all types of customers. An essential part of this matching process is to identify those groups of customers whose needs are most compatible with the organisation's strengths and future ambitions.

The matching process is further complicated in that it takes place in a business environment which is never stable for any length of time. External factors continue to have a major impact on the company's attempts to succeed. For example, new competitors might enter the business market, existing ones may develop a better service, government legislation may change and as a result alter the trading conditions, new technology may be developed which weakens a businesses current skills base.

One of the biggest areas of misunderstanding about marketing is that it is mainly concerned with customer wants. Many people, even people in marketing have a naive concept of customers and see them as people, or organisations, who can be manipulated into wanting things that they do not really need.

Business is not that simple and customers are not prepared to act without consideration of suppliers' requests. This is clearly evident from the high number of new products and services that fail to make any impact in the marketplace.

### 3.3 Hotel Service Product

Powers (1996: 215) describes the hotel service product as a bundle of features and benefits. The service product and offering has three elements, i.e. a core benefit, an essential facilitating service and a competitive supporting service.

#### 3.3.1 Core Benefit

The core benefit is the generic function the service product provides the guest. For the operation it is “the reason for being in the market.” This could be a night’s lodging, entertainment, relaxation, nourishing and a social experience.

#### 3.3.2 Facilitating Services

Facilitating services are services that are absolutely essential to the operation. If the facilitating services are lacking, delivery of the core benefits are impossible. In a hotel for instance, the absence of a front desk or housekeeping would make the hotel’s operation impossible. In a restaurant, a kitchen provides a facilitating service. Without it the operation would shut down.

#### 3.3.3 Supporting Services

Supporting services are not essential to providing the core benefit, but they are essential to marketing the operation. Supporting services are used to differentiate the operation from its competitors. For instance a restaurant is not a necessary component of a hotel, but could be used to differentiate one property from another. One of the most powerful supporting services in lodging is reservation service.

The key to the successful operation of a hotel according to Crowne Plaza Hotels and Resorts (Crowne Plaza Standards Manual, 2000), is providing an experience that truly satisfies the guest. To accomplish this, the hotel or resort’s management and staff must focus on the guest’s perspective of what is important and deliver on the guest’s expectations. The customer’s viewpoint includes elements from reservations through check-out, such as reservations, advance deposits, arrivals, kerbside / door service, valet parking, front desk registration, background music, bell service, telecommunications, voice mail and messaging, telephone sets, gift shop, complimentary tea & coffee, complimentary news paper, guestrooms, guest bathroom amenities, in-room dining, laundry services, housekeeping, lost & found, security, maintenance, primary restaurants, secondary restaurants, lounge, bars, pool, sports activities and fitness centre.

This explains the relevance and necessity for comprehensive hotel knowledge, as an imperative foundation and starting point for successful hotel property development.

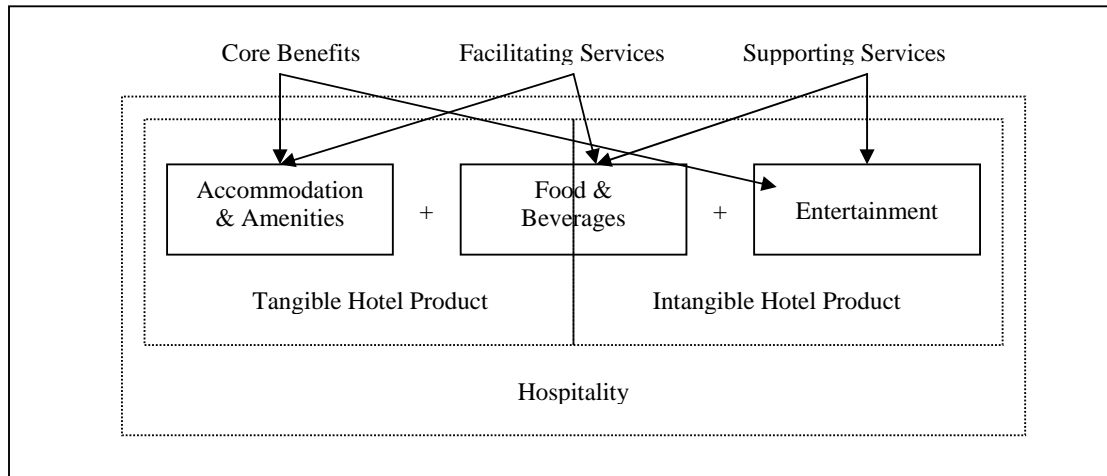
### 3.4 Hotel Segmentation

Segmentation involves a three-step process (Kotler et al., 1999). The first step in this process is **market segmentation**, dividing a market into distinct groups of buyers who might require separate products and/or marketing mixes. The company identifies different ways to segment the market and develops profiles of the resulting market segments.

One of the most frequently used methods for segmenting a market has been demographic segmentation, which consists of dividing the market into groups based on demographic variables such as age, gender, family lifecycle, income, occupation, education, religion, race and nationality. One reason for the popularity of this method is that the consumer's needs, wants and usage rates ranges closely with demographic variables. Another is that demographic variables are easier to measure than most other types of variables. Other variables, for example geographic, geodemographic, psychographic and behaviourist variables, can be used to segment markets.

**Figure 3.3 (a): The Hotel (Product) Concept.**

(Source: A visual illustration of the previous text by Powers, 1996)



Geodemographic segmentation is based on the grouping of people's similar demographic and geographic characteristics, for example the world's most frequent users of scheduled airlines reside in specific and identifiable areas such as the Urban Gold Coast in the United States of America.

The second step in the segmentation process is **market targeting**, which is the evaluation of each segment's attractiveness and selecting one or more of the market segments. Marketers identify the segments and then look for the segments that would be the most profitable in the long term for the organisation.

The third step is **market positioning**, comprising the development of a competitive position and an appropriate marketing mix for a product. Once a company has chosen its target market segments, it must decide what positions to occupy in those segments. The positioning task consists of three steps, i.e. identifying a set of possible competitive advantages on which to build a position, selecting the right competitive advantages and effective communication, and delivering the chosen position to a carefully selected target market.

Hotel developers should consider the target market that the hotel expects to serve. The target market will serve as a guide for planning the physical structure and amenities in the hotel, which are derived from guest profiles, the hotel's location, budget and brand status (Baltin & Cole, 1995). It is suggested that consultations with experienced designers and architects will yield feasible concepts on how to achieve an overall look that would appeal to the target market while keeping within the development budget.



Hotel organisations approach market segmentation similar to the above explanation by Kotler et al. McDonald and Payne (1998: 81) categorises segmentation as falling under the two broad headings of **customer characteristics** and **customer responses**. In other words, who are our customers and why do they behave as they do?

### 3.4.1 Customer Characteristics

- *Demographics*: Characteristics including sex, age, family size, etc.
- *Socio-economic*: Characteristics such as income levels, education, social class and ethnic origins.
- *Psychographics*: Characteristics defining people's behaviour, lifestyles, customers' attitudes, underlying personality types, motivations and aspirations.
- *Geography*: Characteristics identifying local and regional tourism trends, or population density, climate-related factors and the availability of communications media. For the service company operating on a global scale, geographical segmentation might carry with it a whole package of other considerations such as culture, religion and degree of industrialisation.

### 3.4.2 Customer Responses

The segmentation characteristics in this category are more likely to explain what guests buy, why they buy and where they prefer to stay.

- *Benefit*: The reason people buy a service is to acquire a benefit.
- *Usage*: By focusing on the usage patterns of particular guests, the hotel company can identify ways to reinforce relationships with existing guests who are frequent users. Also the information could be used to devise strategies for converting less frequent or first time users.
- *Promotional response*: This considers how customers respond to various types of promotional activity, such as, for example, advertising, exhibitions, in-store displays, sales promotions, and direct mail.
- *Loyalty*: Customers can be characterised by their degree of loyalty, being hardcore loyals, soft-core loyals, shifting loyals or switchers.
- *Service*: This approach is based on considering the service environment that accompanies the hotel service product.

### 3.4.3 Hotel Market Segments

Singh and Raymond (2000) reviewed the USA lodging industry from the beginning of the century to the current period and found that the industry has not only grown in size, but has been transformed from a relatively homogenous industry (primarily "full-service" hotels comprising small guestrooms and diningrooms) to a heterogeneous one (consisting of motels, all-suite hotels, limited-service hotels, conference centres and full-service hotels).

One factor driving the lodging industry's development, according to Singh and Raymond (2000), was the financing organisations' attraction to specific hotel types (products), which became popular from time to time. In the 1950s the development of the motor-inns or motels was introduced, in the 1960s franchising was the popular development vehicle (predominantly associated with highway properties) resulting in substantial amounts of capital sought for developing highway hotels, and during the period of suburban growth

(the 1960s and 1970s) airport and suburban hotels gained popularity, with city centre locations falling from favour. Later, as the market became more segmented, hotel financing was used for a variety of different hotel products.

Pannel Kerr Forster Consultants' (PKF) distinguishing criteria for different types of hotels, which are commonly used to categorise target markets, are cited by Singh and Raymond (2000: 40). (Refer to table 3.4.3 (a)).

**Table 3.4.3 (a) Hotel Market Segments**

(Source: Singh & Raymond, 2000: 40, illustrating PKF Consultants' distinguishing criteria of different types of hotels)

<b>Distinguishing criteria of different types of hotels</b>				
<b><u>Price</u></b>	<b><u>Function</u></b>	<b><u>Location</u></b>	<b><u>Market Served</u></b>	<b><u>Distinctiveness of style or offerings</u></b>
<b>Budget or economy</b> Rooms-only; little public space with no food and beverage	<b>Convention</b> Large; 500 or more guestrooms; extensive public space and meeting space	<b>Downtown</b> High-rise structures; attached parking; wide mix of facilities and amenities	<b>Executive-conference centre</b> Secluded settings; fewer than 300 rooms, small meeting rooms audio- visual facilities and variety of recreation facilities	<b>All-suite</b> Larger-than-normal guestrooms; living and sitting areas separate; minimum public space; facilities equipped for extended stay (e.g., kitchenette)
<b>Middle-market</b> Range of facilities and amenities	<b>Commercial</b> Functional guestrooms, ample work area, small meeting and conference rooms, limited recreation facilities	<b>Suburban</b> Low- to mid-rise structures; parking, meeting and banquet facilities	<b>Health spa</b> Catering to market looking for specific need, such as weight loss or hedonistic experience, staff consists of a variety of trained professionals such as dieticians, therapists, and counsellors	<b>Historic conversion</b> Well-known historic buildings and landmarks renovated or converted to hotels
<b>Luxury</b> Upscale decor and furnishings, concierge service, high-quality public space, higher-than-average employee-to-guest-room ratio		<b>Highway</b> Low-rise structures; surface parking, exterior corridors, outdoor pools  <b>Airport</b> Adjacent or attached to airports	<b>Resort</b> Emphasis on recreation, extensive food and beverage, banquet settings are picturesque	<b>Mixed-use hotels</b> Mixed-use developments consisting of hotels, retail, and other attractions.

*Note:* Many types of hotels can be defined by more than one classification scheme.

### 3.4.4 Hotel Product Repositioning

Repositioning refers to finding new markets or market segments. An example is the repositioning of some Asian-Pacific resort hotels, from their previous focus on sun-seeking-all-family holiday business, to a guest mix including the 'young' retired market. Choy (1998) confirms that the shift away from resort destinations offering sun, sand and sea, also reflects the aging of the population in industrialised countries and the trend toward special-interest travel. As the population of industrialised countries continues to age, mature travellers will seek alternative travel experiences in line with their interests.

Another aspect of repositioning is dealing with new competitors, when a hotel changes its target market. Consequently, the hotel's repositioning analysis needs to take into account, not only the needs and preferences of the added market segment, but also the competitive advantages of the competition to those segments. The new offering must include competitive points of difference that will give the hotel operation an advantage, and not just a duplication of market patterns.

### 3.5 Hotel Branding

#### 3.5.1 Branding Concept

Kotler et al (1999: 284) defines a brand: "... as a name, term, sign, symbol, or design or combination of them intended to identify the goods or services of one seller or group of sellers and to differentiate them from those of competitors." Brand names and logos or trademarks encourage people to buy the particular product because for customers they represent familiarity and safety.

According to Powers (1996: 220): "... branding is seen as a product characteristic because the brand is associated in the consumer's mind with the product it represents." Brand imaging is partly the result of advertising, but ultimately it is the consumer's experience of the product that determines the brand's success.

*"At the one end of the branding concept is the simple idea that a brand constitutes a name, a logo, a symbol, identity or a trademark, and at the other end of the spectrum is the complex idea that a brand embodies all that the business stands for. In its most complex form, the brand is the hallmark of quality a promise or an assurance to the buyer a set of associations or expectations, a perception, an icon, or an image that triggers a propensity on the part of the customer to purchase the brand's product. As such the brand becomes a symbol that connects the company or its products with the customer in a relationship and presents the entire 'product personality' "* (Prasad & Dev, 2000: 23).

Kandampully and Suhartanto (2000) write that 'image' could influence customers' minds through the combined effects of advertising, public relations, physical image, word-of-mouth, and their actual experiences with the goods and services. Customers' experience with the products and services is considered to be the most important factor that influences their minds in regard to image.

*"Studies of hotel brand loyalty in the free independent traveller's market, found hotel image to be an important factor and to maintain a relatively high score rating among loyal customers. Image is positively associated with customer satisfaction and customer*

*preference (a dimension of customer loyalty) in luxury hotels” (Kandampully & Suhartanto, 2000: 349).*

Globally, hotel operators use brands to segment markets and to diversify between their service product offerings. An example is Six Continents Hotels’ Inter-Continental Hotel brand being used in the upper-scale (1<sup>st</sup> class) market segment and Holiday Inn Hotel’s brand used in the more price sensitive mid-scale segment.

Brands also help with the introduction of new hotel products. When Holiday Inn decided to enter the limited-service lodging market, the name Holiday Inn Express for its ‘new’ product drew on the reputation built up over many years on the Holiday Inn name.

Branding in practice starts with a brand definition statement. Crowne Plaza Hotels & Resorts established the following worldwide brand positioning statement:

*“For the upscale business traveller, Crowne Plaza is the smart choice - because Crowne Plaza offers upscale services and amenities that are better designed for relevance and value, without extravagance in rate or facilities.” (Crowne Plaza Standards Manual, 2000: 3)*

The brand positioning statement underpins the design of the hotel’s service product, the physical product, and all communications between the brand and its customers. It is manifested in what the brand is, what it does, and how we talk about it.

Rendering the branding concept more tangible, Crowne Plaza Hotels and Resorts go further by communicating a personified brand statement (Crowne Plaza Standards Manual, 2000: 4):

*”You can imagine Crowne Plaza as a person, she is a genuine, trustworthy person, well presented and intelligent, but open minded and down-to-earth. She is always welcoming, and will do whatever she can, to help and to support the people she meets.”*

### **3.5.2 Brand Equity**

*“Today, brand equity is too important to the success of a hotel property to simply be estimated or considered as “goodwill”, it must be calculated.” (Schultz, 2001: 1)*

Schultz (2001) explains that property prices commonly revolve around the tangible elements of the facility or facilities. Those typically include such things as number of rooms, desirability of location, quality of the furnishings, state of repair, taxes, alternative sources for income and current debt. This is then factored against strategic fit within the organisation, available management resources and capital requirements to come up with a price acceptable to the buyer and seller. Current purchase prices could also be reviewed for relevant properties in the same or similar markets to give both the buyer and seller some view of what a realistic price might be. While there is a degree of brand equity assessment involved in the process, in the hotel business this intangible value has often not been well understood or validated.

Further to this, Schultz (2001) writes that a hotel’s brand equity could be defined as the intangible value of a hotel, meaning the management’s operational experience, employees and training, marketing and communication skills, intellectual property in the form of

operating programs, and reservations systems all have traditionally been measured in terms of cost and output.

*“The problem has always been that this intangible value, the hotel’s brand image, has traditionally been measured in terms of attitudes, feelings and associations among customers. All attitudinal measures are valid but all are extremely difficult to quantify, particularly financially. Currently there are tools that can relate these elusive consumer factors into definable, verifiable income flows that can be of tremendous benefit to the hotel owner or manager” (Schultz, 2000: 1).*

In addition to the problem with intangible value, Schultz (2001: 1) stresses a key ingredient in understanding a hotel property’s value, which is: “ ... *to understand what is called its ‘brand momentum’. This is a summary measure of the hotel’s historical income flows that have been generated over the past three to five years. This income data is then plotted on a graph and a trend line drawn indicating the brand momentum. In this graph, historical hotel income will be plotted on a monthly basis for a period of a few years, e.g. three or more. In the monthly data peaks and valleys will indicate seasonality, economic conditions, conventions, etc. The key element, however, is the trend line indicating whether hotel income, and therefore value, is increasing or declining.*”

### **3.6 Hotel Product Packaging**

Packaging is easy to understand in the case of manufactured goods but what does it mean in the context of the hotel product? Swarbrooke (1999: 43) writes that the answer depends on the definition of packaging:

*“For goods it is the external wrapping that is designed to make the product attractive to potential purchasers. Packaging is also used to make it easier for customers to pick up, transport and use goods.”*

Packaging could include the following elements in relation to the hotel product (Swarbrooke, 1999):

- Providing information and directional signage to help visitors find the hotel.
- Attractive entrances to attract passing trade.
- Combining the attraction to a hotel with other facilities and services to make it more attractive or accessible.
- Selling the product by making it part of the package offered by another organisation with its own client base such as a tour operator or coach company.

### **3.7 Hotel Marketing Mix**

McDonald and Payne (1998: 17) simplify the marketing mix concept, describing it as the: “...*‘flexible coupling’ between the supplier [hotel operator] and customer [guest] facilitating the matching process.*”

Traditionally the marketing mix was said to consist of four elements only, namely (McDonald & Payne, 1998):

- a) *Product*: The product or service being offered.
- b) *Price*: The price or fees charged and the terms associated with its sale.

- c) *Promotion*: The communications programme associated with marketing the product or service.
- d) *Place*: The distribution and logistics involved in making the product/service available.

The four elements of the marketing mix are also referred to as the 4Ps of marketing, which is obvious from the above. One could say the marketing mix is like a recipe, a blending of ingredients to achieve the delivery of planned goods and services and to make the offer of the product known to consumers. Of primary importance to hotel property development is the mix elements **product, place** and **price** as they house the origin, essence and feasibility of hotel property developments. What is contained within these mix elements are the hotel concept, design, specifications, development parameters and characteristics, as defined in the hotel business and marketing plans.

It should be noted that within each of the four 'Ps' is included a number of sub-elements pertinent to that heading. Further to this, in recent years some academics and professionals felt that the original marketing mix concept was insufficient. The original concept was expanded to include the additional marketing mix elements, *customer service, people and processes* (McDonald & Payne, 1998).

### 3.7.1 Tangible Hotel Product

It is argued by Powers (1996: 211) that: “ ... *if the service product is an experience, then clearly, the environment in which it takes place is a key part of the product.*” The physical (tangible) setting is a representation of the experience on offer, and the perception of the tangible product is shaped to a large extent by things that consumers can comprehend with their five senses. Guests take an appearance of luxury or crisp efficiency in an operation as representing the reality they are experiencing. The reverse is also true, as most people will recall entering a disorderly restaurant or a worn and frayed hotel lobby.

Powers (1996) further distinguishes between the exterior and interior, tangible hotel product experience:

The *hotel exterior* serves as the initial attraction and first impression of the hotel. The visual appearance of the operation needs to be a strong element in the hotel [property] development decision, and if a hotel has been designed successfully, the guest should be able to tell what is happening inside the building simply by viewing its exterior. The physical structure should reflect the intangible service elements that are part of the total product offering. The building's exterior design and the external landscaping must complement the image intended. Clean parking lots imply an efficient operation, and could be extended to reflect the cleanliness of the kitchen.

The *hotel interior* gives the lasting impression, the environment in which service is rendered. This physical support or service delivery system could analogously be referred to as the stage setting. To create the desired impression about the nature of the service product, the interior design should achieve certain desired effects called the atmospherics. The hotel's interior atmosphere has been defined as the conscious designing of space to create certain effects on guests. “*More specifically, atmospherics is the effort to design buying environments to produce specific emotional effects on the guests that enhance his purchase probability*” (Powers, 1996: 213).

Atmospherics go beyond mere visual appearance and is used to impact four of the five human senses (Powers, 1996):

- *Sight.* Designers create a visual effect with colour, brightness or dimness, size and shape.
- *Sound.* Music says a great deal to the guests about where they are and how they are supposed to feel.
- *Smell.* No-smoking rooms offer an odour-free environment to the hotel guest, and some restaurants arrange to pipe the smell of baking bread into guest areas.
- *Touch.* Luxurious linen napkins and tablecloths are the hallmark of the white-tablecloth restaurant. Extra-thick bath towels and deep-pile carpets support the feel of luxury in an elegant hotel.

Decor is clearly the dominant theme in the message an operation's atmosphere sends to the guests. Other measures to support that effort are also used, which could include uniforms, tabletop appointments and graphics.

Finally, Swarbrooke (1999: 39) associates characteristics such as features, brand name, quality, styling and packaging with the tangible product.

### **3.7.2 Hotel Place**

Place in the hotel marketing mix covers a number of related topics. Some of these are property location, site decisions, distribution of the product (that is making the product conveniently available in many places) and place-related factors such as logistics.

#### **3.7.2.1 Hotel Place Spectrum**

In order to establish a competitive advantage, hotel operators often introduce new and innovative hotel products to the market. These new hotel products, including all types of different properties, would then target specific market segments in an exercise to expand their guest base.

The spectrum of hotel properties, as a facilitating service (refer to section 3.2) to the core hotel product, is wide and often subjective. For clarity in this regard, Lawson's (1996: 77) categorisation of hotel developments is included as a generic grouping. This would include the following types of hotel properties:

- Suburban hotels
- City centre and downtown hotels
- Budget hotels
- Resort development
- Beach resort hotels
- Marinas
- Health resorts and spas
- Rural resorts and country hotels
- Mountain resorts
- Themed resorts
- All-suite hotels
- Condominium, time-share and residential developments.

In addition to the above categories of hotel properties, a wide variety of other lodging facilities exist (Lawson, 1996):

- Motels, motor hotels and motor courts
- Boarding houses, guesthouses, pension and pension de famille
- Bed and breakfast accommodation and hotels-garnis
- Holiday villages
- Condominiums
- Individual villas, apartments, suites and cottages.

Hotel properties could be categorised in accordance with their various characteristics as previously defined in section 3.4.3 and table 3.4.3(a). From all the sources consulted for this text, it could safely be accepted that the most frequently used dimension for categorisation is price. At one end of the hotel development price spectrum is the hard-budget hotel and at the other end the first class or upper scale hotel.

Cahill and Mitroka (1992) place the hard-budget hotel at the price sensitive budget end of the market, featuring small guestrooms, including bathrooms, which contain cost-effective built-in furnishings. These hotels are designed with minimal public space and contain no restaurant, lounge or meeting space. Near the middle of the segmentation spectrum is the extended-stay hotel. This type of hotel is designed to serve hotel guests who stay for five or more consecutive nights. Examples of extended stay hotels are Residence Inns by Marriott, Homewood Suites and Staybridge by Six Continents Hotels. At the opposite end of the spectrum is the luxury hotel and destination resort with expansive recreational facilities, meeting facilities and public space. Throughout the spectrum there are many other unique and physically distinct hotel products or property types.

Yet more categorisation should be noted. Powers (1996: 229) draws a distinction between full service and limited service operations. In turn, each of these service categories could be divided by price, location and specific use.

Powers (1996) is of the opinion that the basic full-service property is gradually being displaced by limited-service concepts that offer little or no food service and few of the traditional hotel services such as a bell staff. Fairfield Inns, Courtyard by Marriott, Hampton Inns and Holiday Inn Express are well-known brands in this group.

For an example of how a hotel organisation would position its various brands in different market segments, refer to table 3.7.2.1 (a), Six-Continent Hotels & Resorts hotel segmentation spectrum:



**Table 3.7.2.1 (a): Six Continents Hotels Brand and Market Segmentation**

(Source: Six Continents Hotels Product Segmentation, 2001)

Mid-Scale (Limited Service)		Mid-Scale (Full Service)	Upscale (Full Service)	Upper-Scale (1 <sup>st</sup> Class) (Full Service)
Without F&B	With F&B			
<b>Holiday Inn Express</b> (Leisure & Business Traveller)	<b>Holiday Inn Garden Court</b> (Leisure & Business Traveller)	<b>Holiday Inn Select</b> (Business Traveller)	<b>Crown Plaza</b> (Leisure & Business Traveller)	<b>Inter-Continental</b> (Business & Leisure Traveller)
		<b>Holiday Inn SunSpree Resorts</b> (Leisure Traveller)	<b>Staybridge Suites</b> (Extended Stay)	
		<b>Holiday Inn</b> (Leisure & Business Traveller)		
		<b>Holiday Inn Family Suite Resorts</b> (Leisure Traveller)		

### 3.7.2.2 Hotel Location

The prime consideration in choice of a hotel, remains location. This fact was confirmed in a survey by Omni Hotels Corporation, in which location was rated first by 56.8% of guests who responded, price was next with 17.6%, service followed with 12.7% and facilities were fourth with 9.9% (Golden, 1994).

The Travel Weekly magazine included an article, (Hotel safety, location, clean rooms are women's..., 1993: 13), in which the importance of hotel property location is discussed. The article explains: "We see the market-product-location balance too often overlooked by owners, managers, and even designers who become entranced with style details." Three factors: market, physical plant and location should be analysed and balanced by the owner or developer when planning a new hotel.

Specific factors pertaining to hotel site locations are comprehensively discussed in section 8.9 and 8.10.

### 3.7.2.3 Hotel Grading

A brief overview of hotel grading is included in this section, serving as additional and supporting information to broaden the spectrum of relevant hotel property development information.

In most countries a 'hotel' is defined as: "...a public establishment offering travellers and temporary visitors, against payment, two basic services: accommodation and meals" (Lawson, 1997: 1).

Lawson (1997) further clarifies that the precise definition of what constitutes a hotel and conditions for hotel registration and grading are set out in more than one hundred classification systems world-wide. These classifications are operated by governmental or representative agencies, vary both in the range of categories and method of designation (letters, figures, stars, crowns and other symbols), and may be compulsory or voluntary.

“Since 1962 the World Tourism Organisation (WTO) has sought to develop a universally accepted hotel rating system. Similar proposals have been considered by the International Hotel Association (IHA) and the Confederation of National Hotel and Restaurant Associations (HOTREC) of the European Union has devised an alternative system using symbols to represent the facilities without classification. In 1995 there were over 100 classification systems in operation, the majority based on the World Tourism Organisation model, but customised to suit local conditions” (Lawson, 1997: 5).

Section 6.5, Hotel Grading and Standards, provides a more comprehensive discussion of hotel grading systems.

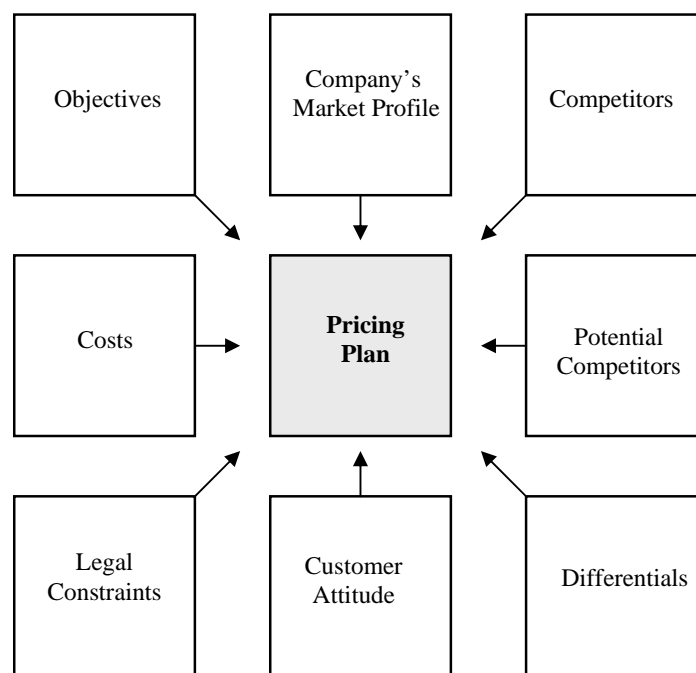
### 3.7.3 Hotel Price (Rates and Costs)

Price represents value to the customer and is a means to recapture costs and earn an operational profit. Price and demand interact, each affecting the level of the other. As price increases, demand generally declines, but this relationship depends on the price sensitivity of the customer. Price sensitivity exists in some relevant range and is not the same at all price levels. Price is also affected by supply, being higher for scarce goods. A third price determinant is the intense competition in the hospitality industry, offering alternative choices to the consumer (Powers, 1996).

“The fastest and most effective way for an organisation to achieve maximum profit is to get its price right. Given the importance of price in generating revenues and profits for a company, the pricing approach used by service firms in price setting has been relatively unsophisticated” (Tung et al, 1997: 53). It was found (Tung et al, 1997), that cost-orientated pricing was the most popular approach used, but although this method offers some advantages, the simplistic nature of cost-orientated pricing is not effective in a complex and competitive business world. As consumers have become more sophisticated and demanding, it is imperative that service firms adapt to this changing environment when setting prices.

#### Illustration 3.7.3 (a): Factors Affecting Price

(Source: McDonald and Payne, 1998: 178)



There are several pricing approaches covered in service-product literature, but Tung et al (1997) is of the opinion that only the following has general practical application:

- a) Traditional cost-orientated approach.
- b) Traditional competitive-orientated approach.
- c) Extended cost-orientated approach.
- d) Differentiation premium approach.
- e) Client-driven approach.
- f) Bundle pricing approach.
- g) Multi-step synthetic pricing approach.

*Cost-orientated pricing and Competitive-orientated pricing approaches* are the two traditionally dominant pricing approaches in the service industry. A cost-orientated pricing approach sets a service price based on all the costs plus a desirable profit margin. It is usually based on full cost, but it can also be a contribution and incremental basis. For competitive-orientated pricing approach, the price is set to meet the market competitive situation. The simplistic nature of these two pricing approaches provides the advantage of a useful and quick pricing method. On the other hand, the simplicity of these two pricing approaches also causes them to lose their effectiveness, as the business world becomes more dynamic and complex. In general, a competitive-orientated service pricing approach provides no guidance on how much higher or lower than a competitor's price a service provider should set its price.

*Extended cost-orientated pricing approach* includes the traditional cost-orientated pricing factors of fixed costs, variable costs and the firm's profit goals, along with the factors that make up the extended model. These factors are:

- essentiality (the extent to which the purchase of the service is postponable),
- durability,
- value added, and
- the percentage of performance capacity.

*Differentiation premium pricing approach* incorporates the firm's pricing strategy, recognising the ability to differentiate the firm's competitive advantages from those of competitors. The differentiation premium comes from an availability premium, reputation testability premium, commitment incentive premium and price sensitivity premium.

*Client-driven pricing approach* is a model based entirely on clients' response to price, namely the quantity of service used and the number of clients gained or lost. The major advantages of this model are consideration of the relationship between market share (demand) and price, and maximising short-term and long-term profit. The major disadvantage of his model is that it is built on the economic assumption of static equilibrium along with zero marginal cost and constant/or linear consumption.

*Bundle pricing approach.* Broadly defined, bundling is the practice of marketing two or more products or services in a single package for a special price. The rationales for service bundling are the cost structure consists of a high degree of cost sharing and a high ratio of fixed cost to variable cost, and the demand for a firm's services is generally interdependent. The advantage of pure bundling is its ability to reduce effective buyer heterogeneity, while the advantage of unbundled sales is its ability to collect a high price. Mixed bundling can make use of both of these advantages by selling the bundle to a group buyers with

accordingly reduced effective heterogeneity, while charging high mark-ups to those on the fringes of the taste distribution who are mainly interested in only one of the two goods.

*Multi-step synthetic pricing approach.* Compared with the other service pricing approaches, the proposed pricing approach considers simultaneously the crucial aspects of service pricing:

- market competitiveness;
- internal cost-profit structure;
- bundling and unbundling services pricing;
- service characteristics premium;
- price standard limits;
- client-orientated price/demand sensitivity; and
- client-orientated profit maximisation.

### 3.7.3.1 Determining Hotel Rates

Lane and Dupre (1996) explain that the unit for sale in a hotel is a room night and for a restaurant a cover or a meal. The supply of rooms or restaurant seats is fixed, but on the other side of the equation demand fluctuates. Filling up all of your hotel rooms or restaurant seats, at the highest rate possible without turning anyone away, would mean you have a perfect match between supply and demand.

The measure of how much of a hotel's supply [rooms] is sold, is called the occupancy percentage. The number of rooms available for sale in a hotel may be less than the total in the hotel. If a room is under repair it is 'not available' (can not be sold) and thus would not be included when calculating an occupancy percentage. Including these 'not available' rooms in the measure of revenue, the RevPAR concept is used (RevPAR = Revenue Per Available Room).

Determining room rates involves the assessment of capital-intensive businesses with a high fixed-cost structure. Room rate calculations are typically set in the context of a property life of 30 years or more.

The following simple example illustrates the calculation: A hotel with 60 rooms sold, of its 100 rooms available for sales on a given night, is 60 percent occupied. The measure of what price the supply is sold for, is the average daily rate per room sold. Since not every customer pays the same rate, an average is used. If 30 of the 60 rooms in the above example were sold for \$100.00 and the other 30 were sold for \$120.00, the total revenue for the evening would be \$6,600.00. The average daily rate would be \$6,600/60 or \$110.00. A variation of this statistic is to consider the average rate per available room. This previous statistic illustrates an average of all rooms in the hotel, whether they were sold or not. A room that was not sold contributes zero dollars. In the above example, 30 rooms were sold for \$100.00, 30 rooms were sold for \$120.00, and forty rooms were not sold. Thus the average rate per available room is  $((30 \times \$120) + (30 \times \$100) + (40 \times \$0))/100 = \$66.00$ .

Typically, the breakeven occupancy for a hotel or the occupancy needed for revenues to match expenses, will be approximately 65 percent. The typical average daily rate has a wide variance depending on the type and location of a given hotel. Occupancy and average daily rate are probably the two statistics used most frequently by hotel managers.

The comparable measures of occupancy rate and average daily rate for a restaurant are number of turns or turnover and average amount (money value) of the invoices (checks). The number of turns is the number of sittings in a given meal period (breakfast, lunch, or dinner) that a restaurant seat provides. The average number depends very much on the type of restaurant service. A quick service family-style restaurant might have four turns per meal period, where a gourmet restaurant would likely not have more than two turns. The average invoice (check) or price per cover served is also dependent on the style of restaurant and the location.

In summary, the calculations for these important hospitality measures are:

- Occupancy Percentage = Total no. of Rooms Sold / Total no. of Rooms Available for Sale.
- Average Daily Rate per Room Sold = Total Revenue / Total Number of Rooms Sold.
- Average Rate per Available Room = Total Revenue / Number of Rooms Available for Sale.
- Number of Turns or Turnover = Number of Persons or Covers Served / Number of Seats in the Restaurant.
- Average Check = Total Revenue / Number of Persons or Covers Served.

All of these statistics can be calculated for different time frames. They can be calculated on a daily, weekly, monthly or yearly basis. Even the “average daily rate,” despite its name, can be considered annually, for example.

Projected room rates for a new property, according to Powers (1996), must be reviewed as part of the feasibility study to determine, at the very least, whether the estimated costs are covered by an adequate margin. Compared to newly proposed hotel properties, existing properties can adjust rates more realistically in accordance with other revenue generating options in the hotel. Other opportunities for good profit performance could be food and beverage, outdoor recreation, convenience shopping and commercial rentals. In conclusion, Powers (1996) asserts that there is no question that the room rate is the principal factor, along with occupancy levels, for determining revenue and profitability.

### **3.7.3.2 Demand and Competition**

When the market for rooms in a town begins to expand, new hotels will typically be more expensive (higher room rates). This is true, not only because the investment cost of new construction is higher than the capital cost of existing properties, but also because many guests will pay more to use a new facility. As new facilities enter the market, occupancies in older properties tend to drop as a result of business lost to the new properties. The drop in older properties’ occupancies are often offset by the higher rates for new hotels, resulting in limited occupancy losses (Swarbrooke, 1999).

### **3.7.3.3 Room Rate Range (Lane and Dupre, 1996)**

Hotel room rates vary widely according to the country, economic climate, geographical area and market segment it serves.

Properties in the limited-service and economy segments generally have only one or two room types and charge the same basic rate for each type, with additional charges for each

additional person in the room. There are sometimes exceptions to this “one size fits all” approach for suites or large family rooms.

Luxury, upscale and to a lesser degree mid-priced properties generally have a number of room types which range in price. The practice of having a minimum of three rates, preferably five, gives front-office staff and reservationists an opportunity to “sell up.” The object is to have several levels of rooms and rates, each differentiated from the other by physical features, i.e. size, in-room facilities, location, view, higher floors and so forth.

Very few rooms are sold at “rack rate”, the hotel’s equivalent of list price. The reasons for discounting rooms seem to cover almost every contingency, except for the traveller who does not know enough to ask for a special deal.

Every hotel market is in a local market and should respond to business conditions in its local market. Special discount rates are generally a function of demand in a particular geographic market. The obvious driving force for widespread price discounting in hotel lodging in recent years is overcapacity and heightened competition.

### **3.7.3.4 Yield Management**

Yield management in hotels, is defined by Lee-Ross and Johns (1997: 66) as a: “...*procedure that attempts to maximise profits by using information about buying behaviour and sales to formulate pricing and inventory controls.*” Hotels use historic purchasing behaviour and compare current demand with forecasts for the future. In theory, this allows sales opportunities to be identified. A balance may then be achieved between supply and demand through constant small adjustments of price (because the room price will affect demand). The procedure considers how different room types are allocated to demand and pricing deals with the optimum prices to charge in different situations. In other words, yield management considers when to restrict availability in order to maximise return and when to sell rooms cheaply.

Yield management suits hotels where the hotel market demand is unstable, where the capacity is fixed or where the market is segmented.

Powers (1996: 246) explains that hotel yield management is a system intended to maximise revenue by adjusting hotel rates for a given time period of demand for accommodation, in that time period. For example in very high demand periods, few, if any, discounts are given. In low periods, on the other hand, special rate categories are opened to attract the price-sensitive market segments

The optimum yield would be achieved when every room in a hotel is rented every day at the posted rack rate. In hotel lodging [as is true for most all service products] there is no means of storing unused rooms or services not sold or utilised. Today’s vacant room has no value tomorrow and so there is pressure to sell the room at a discount. The question arises, however, as to when to discount and what the appropriate discount is. Yield management has been designed to rent as many rooms as possible while generating the maximum rate possible at a given level of demand. The object is to use the hotel’s capacity in the best (most profitable) way possible (Powers, 1996).

### 3.7.3.5 Life-Cycle Costing

Life cycle costing is particularly important in hotels, where the asset value is based on the profitability of the operation rather than bricks and mortar. (Ransley and Ingram, 2000)

Ransley and Ingram (2000: 150) define life cycle costing as: “...a technique used to examine the capital, operating and maintenance costs and revenues of an asset.”

*“The use of life cycle costing in hotel development is highly relevant. After all, the design decisions taken at the early stages of a project can have a significant long-term effect on the running costs and operational efficiency of the completed facility. Quantity surveyors use life cycle costing to identify design options that deliver the best value over the time scale defined by the client. The distinguishing feature of a life cycle costing study is the use of discounted cash flow techniques to bring together income and expenditure streams in a comparable form, even though the cash flows for different options might occur at different times”* (Ransley & Ingram, 2000: 150).

It could be demonstrated by using life cycle costing, that a greater initial investment such as more expensive floor finishes could be beneficial to long-term financial returns. Current expenditure on running costs and staff will, in occupied buildings over time, exceed the initial capital expenditure by many times as they reduce repair and replacement costs over the life of the hotel.

The benefits of life cycle costing for hotels include:

- Proper understanding of the long-term consequences of design decisions
- Capacity to design in order to minimise long-term operating costs
- Ability to consider the design in accordance with the client’s own investment criteria.

### 3.8 Distinguishing Features of the Hotel Business

In an attempt to understand what distinguishes the hospitality business from others, Lane and Dupre (1996: 37) suggest that one should consider the following:

- Hotels are in operation 24 hours a day, 365 days per year. This creates some unusual operational issues, for example, closing for repairs is not possible as it is in other businesses.
- The official end to the day (for administration only) is generally sometime in the early hours of the morning. Also, because of the unlimited hours and the public access to a hotel, hotel staff must fulfil the difficult dual role of hospitable innkeeper. The hotel personnel must also be security officers to insure that invited guests feel welcome and that uninvited guests do not present security problems.
- There are many peaks and valleys in operating a hotel business. Not only are there seasonal fluctuations (e.g. high, low and shoulder season, which is a time of moderate business between the high and low periods at a resort) but there are also weekly fluctuations (e.g., weekday versus weekend business at a centre city hotel), and daily fluctuations (e.g. extensive business during meal periods in restaurants or many guests showering at the same time in the morning).

- The hospitality business is primarily a service business that serves guests who are away from home. Of all the operational costs that a hotel or restaurant manager must monitor and manage the largest is labour. Even when compared to other kinds of service business, hospitality employs a higher than average ratio of employees compared to sales.
- Starting a hotel business is capital intensive (a substantial amount of money is required to get into the business) and therefore high barriers to entry exist. While restaurants are less capital intensive, they usually still require the purchase or lease of substantial pieces of equipment.

### 3.8.1 Hotel Features Shared with Other Businesses

Although the hotel business does have some distinguishing features, in many senses it is much like other businesses, for example repeat business is critical to success. Many hotel companies have followed the airline and other industries' example by creating frequent guest programs, recognising that keeping current guests happy is more cost effective than generating new customers (Lane & Dupre, 1996).

### 3.8.2 The Major Players

The largest chains, as opposed to independent operations, control a substantial and growing portion of the hotel and restaurant business. In addition to this ownership distinction, Lane and Dupre (1996: 42) disseminate the following regarding a hotel chain. *“A chain, quite simply, is two or more operations open under the same name. A chain is distinguished from an independent, which is a stand-alone property. Some chains are structured in such a way that all of the units are owned by one parent company. This would be a corporate-owned chain. Others are franchised, and this means that a parent company or franchisor gives an individual, or franchisee, the right to open a unit for a set of fees described in a franchise agreement.”*

World-wide, according to Lane and Dupre (1996), the largest hotel chains are dominated by the American chains. The top three chains – i.e. Hotel Franchise Systems, Holiday Inn Worldwide (lately renamed to Six Continents Hotels) and Best Western International, and 15 of the top 25 have their headquarters in the United States. The largest European chains are Accor - a French company that ranks fourth globally, Forte Plc. [Plc = public limited company] - a British company that ranks ninth globally, Club Méditerranée - a French company ranking 13<sup>th</sup> globally and Hilton International - a British company that ranks 15<sup>th</sup> globally. The largest Eastern European company is Poland's Orbis, which is ranked 52<sup>nd</sup>. The largest Asian companies are New World / Renaissance, based in Hong Kong and is ranked 16<sup>th</sup>, and Prince Hotels ranked 22<sup>nd</sup> is a Japanese company. The largest Australian company is Southern Pacific Hotels Corporation ranking 40<sup>th</sup> and finally the largest African company is Sun International ranking 78<sup>th</sup>.

## 3.9 Hotel Operations

The following section draws mainly from Lane and Dupre (1996: 188 – 210):

There are two common divisions in hotel operations: the front-of-house and the back-of-house. The back-of-house is also sometimes referred to as the heart of the hotel. What the customer experiences, the front-of-house (public areas), includes the lobby and related services, the dining areas and sometimes a health club or recreational facilities. The back-



of-house includes support services, such as the kitchens, reservations and office support for the front desk, housekeeping, human resources, sales and marketing, accounting, security, and maintenance and engineering.

The hotel lobby is the first contact and experience a guest has with a hotel. However the fairly quiet and tranquil atmosphere in the lobby and other public areas, stand in sharp contrast to the active and busy back-of-house components of a hotel. Not every establishment will be structured in the same way. For example, a bed-and-breakfast would most likely have many departmental functions performed by the same person. The person who checks you in, may carry your baggage, serve tea, take reservations and balance the books at the end of the evening. On the other hand, a mega resort may have many departments each responsible for the many aspects of running the resort. Regardless of size, there is a series of key functions performed in all lodging operations.

Some departments generate revenue for the hotel (revenue centres) and others incur expenses (cost centres). Revenue centres include the front office, telephone (if surcharges are added to guests' bills), restaurant outlets and laundry (if that service is available). Health clubs, golf courses, retail stores and parking are also areas in a hotel where revenues can be generated. Other departments, such as marketing, accounting and maintenance typically do not contribute to income. These departments, which are cost centres, provide support services to enhance the overall operation and to ensure guest satisfaction within the hotel.

### **3.9.1 Rooms Division**

The rooms division of a hotel usually consists of the front office, reservations, telephone, uniformed services and housekeeping.

#### **3.9.1.1 Front Office**

The front office is the first department with which the guest has contact. Front desk clerks perform three critical functions at check-in: (i) they offer a warm reception by greeting guests and making them feel welcome, (ii) they register the guests, by having the guests sign in and presenting a form of payment, usually by leaving an imprint of a credit card, (iii) and they assign rooms to guests, giving them a room key or key card. If all goes smoothly, the process can take minutes, or even less if the guest checks in electronically. However, the hotel business is a service business and has elements that cannot be controlled.

At checkout time, the customer traditionally settles the account (bill) at the front desk. The guest account itemises all room, food, phone, and miscellaneous charges. Many establishments today have installed computer programs that allow the guest to review the bill on the television screen in the room. If the guest agrees that the bill is correct, he / she can give authorisation to charge the total amount to his / her credit card used at registration, simply by following the directions on the screen. Guests can then leave the key or key card in the room, and depart from the hotel without making a stop at the front desk. The latest technological advancement in use is in-room printers, where the guest can review the bill on the television screen, print a receipt using the in-room printer, and depart. This is commonly known as express checkout. Where this option is unavailable, or the guest would like to change the method of payment or question part of the account, a visit to the front desk can settle these issues. The front desk staff then performs a cashiering function. The

reception part of the front desk and the checkout or cashiering functions are generally in two separate places. In small hotels, both functions would be performed by the same person.

Because a front office services guests 24 hours a day, there are typically three shifts of staff involved, and at least two managers, a day manager and a night manager. During the course of a guest's stay, it is the front office that is the front line in terms of handling guest complaints or requests, providing information about the hotel and the surrounding community, and the sending and receiving of guest mail.

#### 3.9.1.2 Reservations

The reservations department, though often considered to be back-of-house, has a very important front-of-house function. It is often the first contact that a guest has with a hotel, and therefore serves an important public relations and sales function. The reservations agents are the sales force for individual reservations and their interaction with a guest can influence whether that guest chooses the hotel again. Many major hotel companies have a toll-free number to call for reservations. This kind of reservations service is not physically located in the hotel at all, but in a separate reservations centre which functions as an independent office.

#### 3.9.1.3 Telephone Service

The telephone system in a hotel operation is commonly referred to as the PABX, and is the telephone exchange that connects calls coming into and going out of the hotel, to and from different departments and guestrooms. It also serves as the exchange for all internal hotel phone calls. The PABX is not really a department within a hotel, but it is a revenue-generating centre that contributes smaller amounts to profits. Though the amounts are relatively smaller than rooms or food and beverage, it is nonetheless important.

Other services related to the phone system, which offer potential additional revenue, are increasingly being added to the list of guest amenities. Many rooms now have facsimile machines, voice mail, and modem connections for computers. Cellular phones are also being made available for use by guests staying in the hotel. Some convention hotels even offer conference call service with video connections, teleconferencing, which allows guests to see and hear via video screens, their business associates in other parts of the world.

#### 3.9.1.4 Uniformed Services

There is no mistaking a doorperson, traditionally called a doorman, at an upscale hotel. He / she usually has a distinguishing hat and uniform, a whistle, and an air of ownership of the hotel entrance. He / she helps co-ordinate some of the other members of a hotel's uniformed service, i.e. the shuttle bus driver, the valet parking attendants who park guests' cars and bell persons, led by a bell captain, who transport luggage to and from guestrooms and provide other assistance as needed while guests check in and out. Members of the bell staff can also function as salespersons by explaining the features of the property and by answering guests' questions.

The concierge desk, usually located in the main lobby, is also part of uniformed services and provides information ranging from restaurant options to theatre tickets. The concierge may also assist guests in more unusual predicaments.

Not all hotels have uniformed service, and more often this service is unique to the more expensive hotels where the guest expects to find a doorman and a concierge. Some upscale hotels even have what is called a concierge floor, which is a floor of the hotel with its own concierge staff, dedicated to the comfort of the guests on that floor. These concierge floors usually charge a premium price.

#### 3.9.1.5 Housekeeping

The housekeeping department performs the cleaning function of the hotel, in the guestrooms, public spaces and back-of-house. The housekeeping department is also responsible for additional items such as an ironing board, cribs and extra towels, which the guests might request. They also attend to dry cleaning and guest laundry, if the hotel offers that service. Hotel laundry such as sheets, towels, and uniforms may be done at the on-site laundry facilities or sent to an outside contractor.

The daily tasks of a housekeeper are mainly determined by the room status. Housekeepers are generally assigned a quota of rooms for a given shift. A separate crew cleans public spaces late at night when the hotel is less busy. Housekeepers must pay close attention to detail with respect to cleaning and at the same time respect the guests' privacy.

### **3.9.2 Sales and Marketing**

A hotel's sales and marketing department must perform a series of functions that maximises customer satisfaction and simultaneously maximises revenues.

Most marketing departments have a sales force and each member of the sales team is usually assigned a special type of market, for example, corporate, international or association sales. The type of customer the hotel attracts dictates these market segments. It is important that the marketing department has a keen understanding of the profile of its customer base and the corresponding needs and wants of each category of customers.

A hotel may choose to use advertising as a means of marketing, either through mass media (such as television, an advertisement in the travel section of a newspaper, or a radio campaign), or direct mail. Using direct mail means that the hotel isolates a specific audience and sends out customised mailing. A hotel may send an invitation for a complimentary visit to travel agents in the geographic areas most likely to send them business. Direct mail pieces, such as colour brochures and rate cards, are usually the primary marketing pieces to attract individual (as opposed to group) guests' bookings.

Public relations is another facet of the marketing department. Unlike advertising, media attention generated by public relations is not paid for directly. Advertising, by contrast, is paid for, and what is printed is completely controlled by the hotel. Public relations news articles are the words of an independent writer who may be assisted by a press release from the hotel. Public relations efforts are intended to generate goodwill. Some efforts are managed and well planned by the marketing department.

### **3.9.3 Human Resources**

The human resource department provides support for all employees of the hotel, as recruiter, ombudsperson, record keeper, trainer, benefits provider, manager, coach, and

sounding board. In these capacities, the human resources department is responsible for a diverse set of functions:

- *The employment process*: recruiting, selecting, orienting and training new employees, and terminating employment of staff that are not meeting expectations.
- *Record keeping*: keeping track of employees' personal information, payroll records, compensation structure and benefits.
- *Relocation*: assisting in the geographic relocation of employees. In the hotel business, particularly in chain organisations, promotion is often tied to relocation.
- *Employee relations*: assuring a comfortable work environment, responding to the needs of employees as if they were internal customers, also called internal marketing.
- *Serving as a sounding board*: playing a mediating role if conflict arises between an employee and a fellow employee or a supervisor.
- *Discipline*: notifying and implementing disciplinary action against inappropriate behaviour by employees.

### **3.9.4 Food and Beverage**

The function of the food and beverage department can best be described by following the route within the hotel that food and drink travel from preparation to consumption. Foodservice planning starts with a menu, either for a restaurant operation, room service, employee cafeteria, or a catered function. Once the raw ingredients are determined (based on the menu) the food and beverage is then purchased, received, stored, issued, produced, and served.

The next steps, production and service vary greatly, depending on the size and complexity of the meal offerings at a particular hotel. An economy hotel, for example, would probably have no food and beverage offerings at all, but might be located near a stand-alone restaurant, often a fast food or family restaurant chain. The number of possible restaurants, banquet facilities, room service, and employee cafeterias are linked to the size and type of hotel. A luxury hotel might have an informal restaurant, a fine dining choice, 24-hour room service and afternoon tea service. A large convention property might have several restaurant choices, including a fast food or take-away option, a speciality restaurant and a 24-hour coffee shop in addition to banquet facilities.

Restaurants in hotels are not always managed by the hotel and are sometimes leased by the hotel to the restaurant operator.

In addition to restaurants, most hotels also provide a beverage service through some type of cocktail lounge or public bar. These areas are generally under the jurisdiction of a beverage manager and are operated separately from the restaurants. A service bar provides a drink service to restaurant guests, and minibars are offered in guestrooms with a selection of alcoholic, non-alcoholic beverages and snacks.

### **3.9.5 Accounting**

This department's functions include recording, classifying, summarising and reporting financial information. Recording information involves accounting of the day-to-day operational events such as issuing payroll checks or receiving guests' payments. Since the hotel business operates on a 24-hour basis, the end of the accounting day is generally some time in the early morning hours. It is then that the night auditor, the person who balances

the books for the hotel, accounts for all money from the previous day's transactions. Among the night auditor's duties are reviewing the posting of charges to guests' folios (statements of the guests' account) from various points of sale within the hotel, such as a restaurant or health club. The night auditor also reconciles the cash register transactions with actual cash deposits. A night auditor may also serve a dual role as a front desk clerk for the overnight shift.

### **3.9.6 Security**

The security division of the hotel is responsible for the physical safety of guests and employees, as well as security of the hotel's property, including both the outside (grounds, gates and parking lots) and inside (public spaces, stairwells, corridors, elevators and guestrooms). This division is also responsible for taking preventative measures with respect to fire, accidents, pilferage and burglaries. When things go wrong, for example, an emergency medical situation or theft of guest property, the security department should assist. The security staff usually has police and emergency medical training.

### **3.9.7 Maintenance and Engineering**

All the physical systems of the hotel, such as heating, plumbing, ventilation, air-conditioning, electricity, and water and steam distribution, literally converge on the inside of the building. All of these systems are the responsibility of the maintenance and engineering department. In addition to these physical systems, the maintenance department manages all other building and FF&E (furniture, fitting and equipment) components.

On a daily basis, the engineers and maintenance personnel respond to work orders to fix what is broken and undertake routine inspections to keep everything functioning properly. Work orders could range from repairing a leaking tap to securing a loose carpet. The skills of carpenters, plumbers, painters, electricians or engineers might be needed. On an ongoing basis, the department must do preventative maintenance on the capital equipment of the hotel. Such work might involve, for example, changing the expendable parts of machinery.

### **3.10 External Factors Influencing the Hotel Industry**

The hotel and tourism industry is susceptible to extreme demand fluctuations owing to a wide range of uncontrollable external factors, such as political unrest, terrorism, natural disasters, accidents and epidemics. The following are examples of the factors that have disrupted and impacted on the hotel and tourism industries recently:

Referring to two factors affecting U.S.A outbound travel market, Swarts (2001: 24) attempts to illustrate the wide range of travel market influences and adversities. *"With roadblocks ranging from the European Mad Cow scare to a volatile Middle East, it's no surprise that U.S.A. travellers would choose to stay close to home this summer."*

The Israeli-Palestinian conflict of the past year [2000 to 2001], says Buckholtz (2001: ?), has cut deeply into the region's tourism infrastructure. *"Travellers, who once dreamed of stepping onto hallowed cultural and religious ground, now get an armchair view during nightly news broadcasts."*

Following the 11 September 2001 terrorist attacks on the World Trade Centre Buildings and other locations, travellers have been cut off from many more Middle Eastern

destinations. Some trips have been deemed unwise, leaving popular sites throughout Arab and Muslim countries deserted.

A PricewaterhouseCoopers report (Attacks to Dampen Hotel Construction, 2001), was of the opinion that the air attacks on the World Trade Centre and the Pentagon and subsequent drop-off in U.S. travel will dampen new hotel construction, resulting in 6% of projects set to finish in the next two years, to be cancelled or delayed. The assessment was in line with earlier observations by hotel analysts and financiers who stated that many lenders have adopted a wait-and-see stance towards new projects until the travel situation becomes clearer. PricewaterhouseCoopers also lowered its previous forecast for new room construction this year, following a travel drop-off that resulted in hotel vacancies of 80% during the two weeks following the attacks.

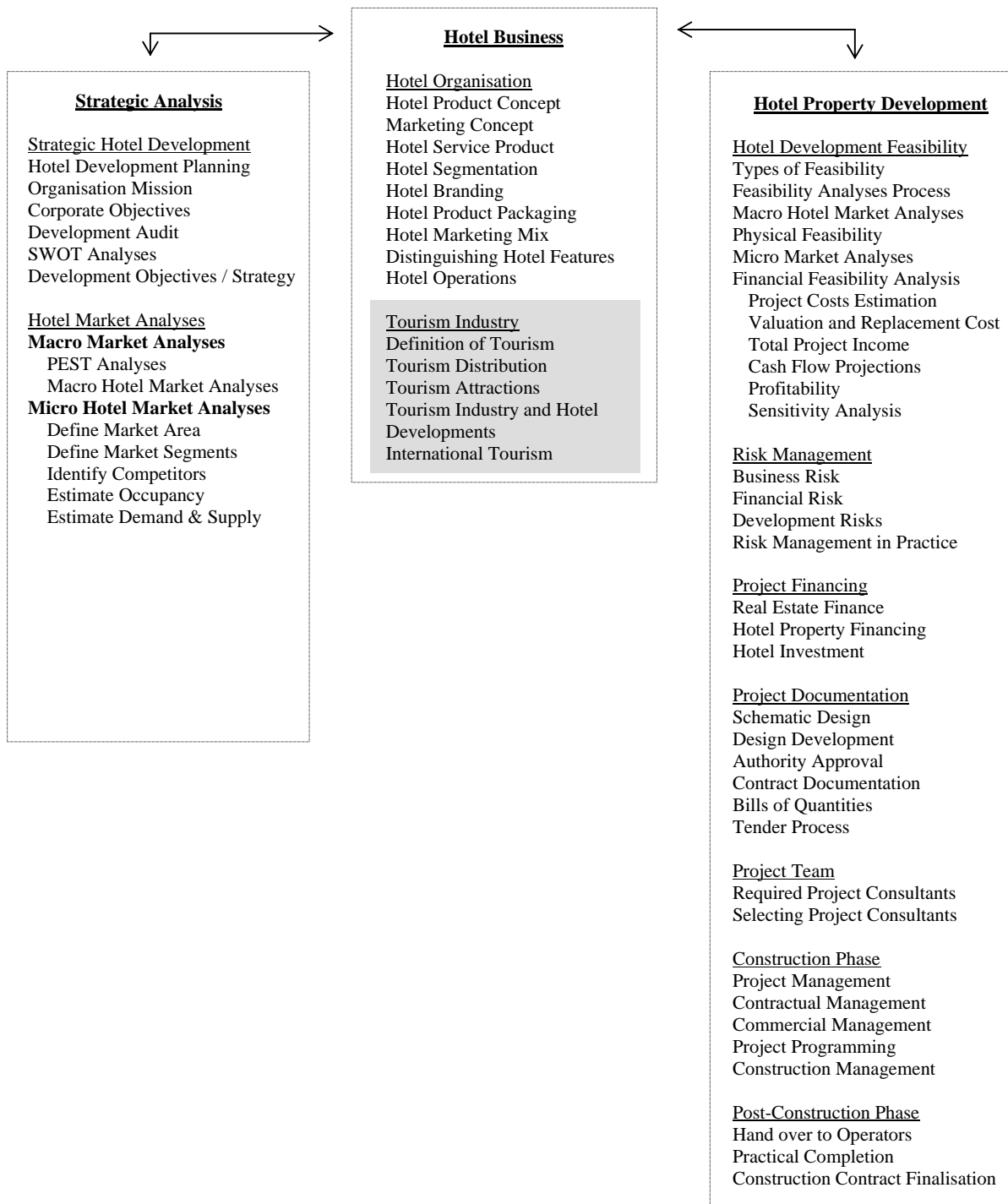
Instability in Zimbabwe and the high level of crime in SA are causing concern. The Businessday (South Africa) reported that owing to the Zimbabwean political crisis, the overall number of foreign visitors to South Africa declined in 2000 for the first time in 15 years, but good growth prospects are foreseen for the tourism industry if external factors can be negated (Breaking down barriers to international visitors, 2001).

The World Tourism Organisation forecasts that Africa should be able to triple the size of its tourism industry by 2020 if proper efforts are made to ensure the safety and security of visitors. The report also highlights the negative effects of attacks on tourists and health scares. (Luhrman and Peressolova, 2001)

These reported incidents and factors are only a small number of possibilities that negatively influence the hotel and travel industry, which could have serious repercussions on hotel development feasibility.

**Chapter 4:**

**Tourism Industry**



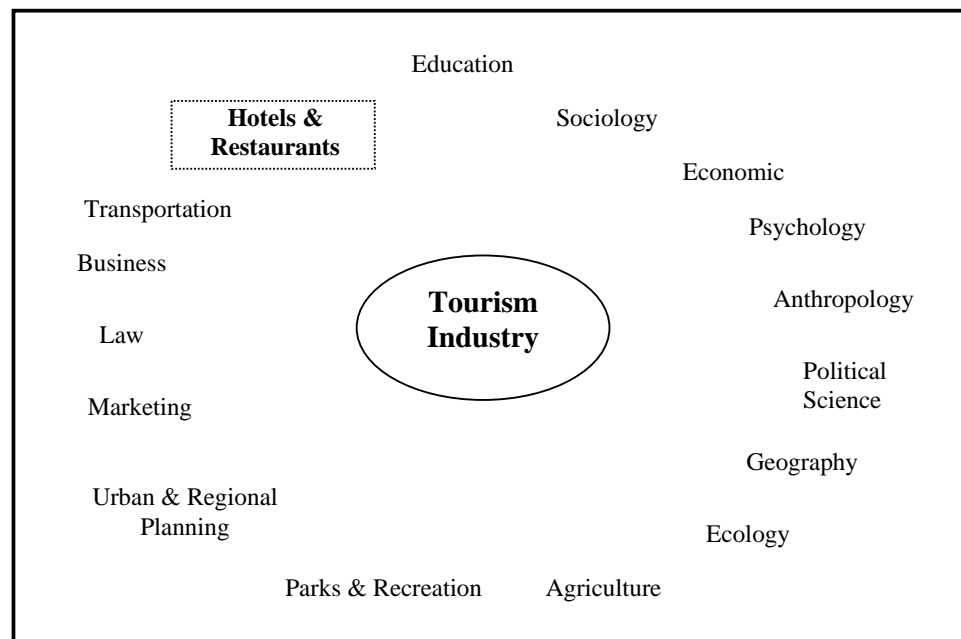
## 4 Tourism Industry

### 4.1 Definitions of Tourism

*“Tourism can be thought of as a whole range of individuals, businesses, organisations and places that combine in some way to deliver a travel experience. Tourism is a multidimensional, multifaceted activity, which touches many lives and many different economic activities”* Cooper et al (1998: 8), as illustrated in diagram 4.1(a).

#### **Diagram 4.1 (a) Tourism Industry Elements**

(Source: Adaptation of Cooper et al (1998: 4)



Cooper et al (1998) further divides tourism into two primary categories, a demand-side and a supply-side:

#### **4.1.1 Demand-Side Definitions of Tourism**

*“Demand-side definitions have evolved by firstly attempting to encapsulate the idea of tourism into ‘conceptual’ definitions and secondly through the development of ‘technical’ definitions for measurement and legal purposes.*

*From a conceptual point of view, we can think of tourism as the activities of persons travelling to and staying in places outside their usual environment for not more than one consecutive year for leisure, business and other purposes”* (Cooper et al, 1998: 8).

Technically the tourism definition conveys the essential nature of tourism, i.e.:

- Tourism arises out of a movement of people to, and their stay in, various places, or destinations.



- There are two elements in tourism, i.e. the journey to the destination and the stay (including activities) at the destination.
- The journey and stay take place outside the usual environment or normal place of residence and work so that tourism gives rise to activities that are distinct from the resident and working populations of the places through which they travel and stay.
- The movement to destinations is temporary and short term in character, and the intention is to return within a few days, weeks or months.
- Destinations are visited for purposes other than taking up permanent residence or employment in the places visited.

#### 4.1.2 Supply-Side Definitions of Tourism

*“As with demand-side definitions there are two basic approaches to defining the tourism sector for the supply-side, the conceptual and the technical approaches. From a conceptual point of view the tourist industry consists of all those firms, organisations and facilities intending to serve the specific needs and wants of tourists.”*

*A major problem concerning technical supply-side definitions is the fact that there is a spectrum of tourism businesses, which are one the one side wholly serving tourists to the other side those who also serve local residents and other markets. One approach to the problem is to classify businesses into two types” (Cooper et al, 1998: 9):*

- Type 1: Businesses that would not be able to survive without tourism.
- Type 2: Businesses that could survive without tourism, but in a diminished form.

#### 4.2 Tourism Distribution

Lubbe (2000: 7) explains that the: *“... travel distribution systems link the suppliers of travel products and services to the end customers. This system of distribution can be described as a predominantly linear chain of distribution because it follows the traditional pattern from the supplier to the wholesaler and/or retailer and finally to the customer. The number of channel levels may vary from simple and direct marketing where the supplier sells directly to the customer, this is called direct distribution, to complex distribution systems involving several layers of channel members such as retail travel agents, tour wholesalers/operators and speciality which is called indirect distribution.”*

The travel suppliers' role, Lubbe (2000) further explains, is to provide travel and transport related services to consumers. Owing to the fact that the tourism product is to a large extent intangible, customers rely on the distribution of information. This information is stored on global distribution systems (GDSs) such as Amadeus, Galileo, Sabre and Worldspan, and it is disseminated to the consumer via the travel intermediaries who are linked to these GDSs. Traditionally the GDS has been the main tool used by the travel industry to distribute information about air travel and other products such as package holidays, hotel accommodation and car hire.

Travel intermediaries can be divided into wholesalers and retailers. Tour wholesalers buy different components of the tourism product from suppliers and create packages, consisting of transportation, accommodation and sightseeing, which are sold via the travel agent to the consumer. In essence, the dominant sales channel for the airline and tour operating companies has traditionally been the travel agents.

Four components could be identified in the tourism distribution system, namely suppliers (or producers or principals), global distribution systems, travel intermediaries, and customers or clients. *“Suppliers may be broadly defined as any producer or principal who has products or services to sell. Global distribution systems (GDSs) and central reservation systems (CRSs) distribute reservation and information services to sales outlets around the world. Intermediaries may be described as any third party or organisation between the producer and consumer that facilitates purchases, the transfer of the service to the buyer as well as sales revenue to the product. Customers may be defined as people who have the need for, want and are able and willing to buy a product or service”* (Lubbe, 2000: 10).

In table 4.2(a) each of the components referred to above are broken down into sub-components, and a description of each provided.

**Table 4.2 (a): Components of the Tourism Distribution System**

(Source: Lubbe, 2000: 11)

Suppliers	Description
Transportation providers	A group travel mode offered by a common carrier, for example airlines, car-rental companies, coaches, trains and ships.
Ancillary transportation services	Airports and terminals
Food service	Eating and drinking places such as restaurants, which include fast food outlets and coffee shops; travel food services which include hotels, motels, roadside food outlets, airlines, ships and trains; vending machines; contract institutional food services such as catering companies.
Resorts	Winter (skiing). Summer (sea).
Accommodation	Sleeping accommodation, which may range from hotels of an international standard, bed and breakfast establishments to condominiums and self-catering apartments and camping grounds.
Recreational activities	This relates to the action and activities of people engaging in constructive and personally pleasurable use of leisure time and may include passive or active participation in individual or group sports, cultural functions, natural and human history appreciation, non-formal education and sightseeing.
Entertainment	Live entertainment shows
Festivals and events	This includes sporting events, cultural festivals and exhibitions such as the Rugby World Cup, Olympic Games and world fairs.

Distributors	Description
GDS / CRS	<p>The terms GDS and central reservation systems (CRS) are often used interchangeably, hence we need to make a brief distinction. A GDS is a system used by travel agents to book airline seats and accommodation for their customers and which connect several CRSs. A CRS is mainly a travel suppliers' own computerised reservation system.</p> <p>GDSs were formed from alliances of several CRSs, each of which had its own airline backer. Their original formation was to some extent influenced by intra-airline relationships as well as the technical architecture of each airline's CRS. Once formed, there was a period of some consolidation and shakeout, after which four main GDSs emerged: Amadeus, Galileo, Sabre and Worldspan.</p>

Intermediaries	Description
Retail travel agent	A middleman selling the travel industry's individual parts or a combination of the parts to the consumer. Acting on behalf of the client, making arrangements with suppliers of travel (airlines, hotels, tour operators) and receiving a commission from the suppliers
Tour wholesaler	A middleman, who may be a business or person, puts together a tour and all its components and sells the tour through his or her own company, through retail outlets and/or through approved retail travel agencies.
Speciality channeller	A middleman who represents either buyers or sellers, receiving either a commission or a salary from his or her employer. He / she generally specialises in meeting specific travel needs by putting together a package on behalf of a client or on behalf of a tourism supplier, tour wholesaler or retail travel agent. Speciality channellers include incentive travel planners, convention planners and hotel sales representative firms.
GSA	A general sales agent (GSA) is the exclusive representative of a principal for a given area. The principal may be a supplier of an off-line airline, a car-rental company or a hotel that does not have its own sales office in the area. A general sales agent may also be a representative for government tourism bureaux and other destination organisations that want to develop a market in the area where the agent is located.

Customers	Description
Leisure travellers	Individuals or groups of tourists who travel for the purposes of recreation and pleasure
Business travellers	Individual travellers who travel specifically for business purposes or who travel as a result of business incentives. This would include travel for the purposes of conferences and meetings.

### 4.3 Tourism Attractions

*“Attractions are arguably the most important component in the tourism system. They are the main motivators for tourist trips and are the core of the tourism product. Without attractions there would be no need for other tourism services. Indeed tourism as such would not exist if it were not for attractions” (Swarbrooke, 1999: 4).*

Swarbrooke (1999: 3) explains what a visitor attraction is by quoting the Walsh-Heron and Stevens (1990) definition. *“A visitor attraction is a feature in an area that is a place, venue or focus of activities and does the following things”:*

- *Sets out to attract visitors/day visitors from resident or tourist populations, and is managed accordingly.*
- *Provides a fun and pleasurable experience and an enjoyable way for customers to spend their leisure time.*
- *Is developed to realise this potential.*
- *Is managed as an attraction, providing satisfaction to its customers.*
- *Provides an appropriate level of facilities and services to meet and cater to the demands, needs, and interests of its visitors.*
- *May or may not charge an admission [fee] for entry.*

Attractions, in general, tend to be single units or individual sites that motivate large numbers of people to travel for a limited leisure time some distance from their home, to clearly defined and accessible small-scale geographical areas. This definition excludes uncontrollable and unmanageable phenomena such as sunshine or snow, etc. (climate or weather), which are sometimes incorrectly described as attractions, according to Swarbrooke (2000).

Swarbrooke (2000) asserts that attractions are entities, which are managed and delimited, and could be categorised into four main types:

- Features within the natural environment.
- Man-made buildings, structures and sites that were designed for a purpose other than attracting visitors, such as religious worship, but which now attract substantial numbers of visitors who use them as leisure amenities.
- Man-made buildings, structures and sites that are designed to attract visitors and are purpose-built to accommodate their needs, such as theme parks.
- Special events.

Table 4.3 (a) illustrates the variety of different types of attractions within these four categories.

#### **4.3.1 Attractions and Destinations**

*“Attractions are generally single units, individual sites or very small, easily delimited geographical areas based on a single key feature. Destinations are larger areas that include a number of individual attractions together with the support services required by tourists. There is a strong link between the two and it is usually the existence of a major attraction that tends to stimulate the development of destinations whether the attraction is a beach, a religious shrine or a theme park. Once the destination is growing other secondary attractions often spring up to exploit the market”* (Swarbrooke, 2000: 7).

#### **4.3.2 Attractions, Support Services and Facilities**

*“The idea that attractions are distinctly different from support services and tourism facilities like hotels, restaurants and the transport system is clearly an over-simplification for two main reasons. First, many attractions are increasingly developing services such as catering and accommodation on-site to increase their income. Secondly, some support services and tourism facilities are attractions in their own right. Many famous restaurants attract people to travel hundreds of miles to visit them. There are numerous hotels that function as attractions such as the Gleneagles in Scotland which is a Mecca for golfers, while some modes of transport such as Concorde and the Orient Express also meet our definition of an attraction”* (Swarbrooke, 2000: 7).

#### **4.3.3 Attractions and Activities**

*“As far as activities are concerned, attractions are a resource that provides the raw material on which the activity depends. For example, sunbathing makes use of beaches, sailors use marinas and music fans visit folk festivals.*

*Some attractions are a resource for a number of different activities, some of which may be conflicting, in which case they will need to be managed to reconcile the needs of the users*

*with the conservation of the resource. There are many examples of this including the use of rivers and reservoirs by anglers and powerboat enthusiasts. This illustration also shows the conflicts that can exist between the use of attractions for leisure and their use for other purposes such as water supply and conservation” (Swarbrooke, 2000: 7).*

**Table 4.3 (a): The Four Categories of Attractions**

(Source: Swarbrooke, 1999: 5)

<b>Natural</b>	<b>Man-made but not originally designed primarily to attract visitors</b>	<b>Man-made and purpose-built to attract tourists</b>	<b>Special events</b>
Beaches	Cathedrals and churches	Amusement parks Theme parks	Sporting events
Caves	Stately homes and historic houses	Open air museums	Arts festivals Markets and fairs
Rock faces	Archaeological sites and ancient monuments	Heritage centres	Traditional customs and folklore events
Rivers and lakes	Historic gardens Industrial archaeology sites Steam railways Reservoirs	Country parks	Historical anniversaries Religious events
Forests		Marinas	
Wildlife: Flora and fauna		Exhibition centres	
		Garden centres	
		Craft centres	
		Factory tours and shops	
		Working farms open to the public	
		Safari parks	
		Entertainment complexes	
		Casinos	
		Health spas	
		Leisure centres	
		Picnic sites	
		Museums and galleries	
		Leisure retail complexes	
		Waterfront developments	

#### 4.4 Tourism Industry and Hotel Development

*“In the context of the tourism sector in general, accommodation rarely has a place and rationale in its own right”* Cooper et al (1998: 314). It is rare for a tourist to select to stay in a hotel for the sake of staying in that specific hotel. The choice of accommodation is made because it provides a supporting service for the main reason that brought the visitor to the destination, whether it is for business or leisure. Some guests may choose to stay at specific destination resorts because of the accommodation experience that such hotels provide, hence proving that some resort hotels may indeed fall outside this generalisation.

Accommodation is a necessary component in the development of tourism within any destination that seeks to serve visitors other than day-trippers (Cooper et al, 1998). An accommodation facility's quality and range could reflect and influence the mix of visitors to a destination. To meet the destination's strategic tourism development objectives, an appropriate accommodation balance must be reached, which could prove to be quite challenging. Accommodation is usually seen as part of the overall tourism infrastructure, without which tourists will not visit the location.

Accommodation, according to Lawson (1997: 1), plays an integral but varied role as part of the wider tourism product. He states that: *“Hotels are not the only types of accommodation used by tourists, travellers and temporary visitors. In Europe some 75 per cent of all domestic tourists (people travelling or taking vacations in their own countries) stay with friends and relatives, use camp or caravan sites or rent houses and apartments. In many resort areas a high proportion of visitors own second homes, condominium or time-shared properties.”*

#### 4.5 International Tourism

World tourism has grown exponentially over the last 50 years, as is illustrated in table 4.5 (a) below. The total number of travellers increased from 25,30 million in 1950 to 656.90 million in 1999, representing a growth of approximately 450% or 25 times over the last 50 years.

The increase during the 1990s only, was approximately 200 million travellers.

Note, as illustrated in table 4.5 (a), the change in travellers to “other destinations”, including Asia, Middle East and Africa.

World Tourism Organisation's (WTO) group secretary-general, Francesco Frangialli remarked (Global tourism still on the rise, 2001): *“Despite all the conflicts we've had in the world over the past 50 years, there has never been one year that experienced a decline in tourism. During the first eight months of 2001, global tourism was on track for an increase of 2.5% to 3.0%. Barring widespread new developments, it predicted growth this year should come in at a 1.5% to 2.0% growth rate. Last year [2000], the industry grew by 7.4% and generated US\$475.8 billion, excluding airfares. The WTO noted that during the Gulf War, international air passengers declined from 280 million in 1990 to 266 million in 1991. But tourist arrivals crept up by 1.2% and receipts increased by 2.1%.”*

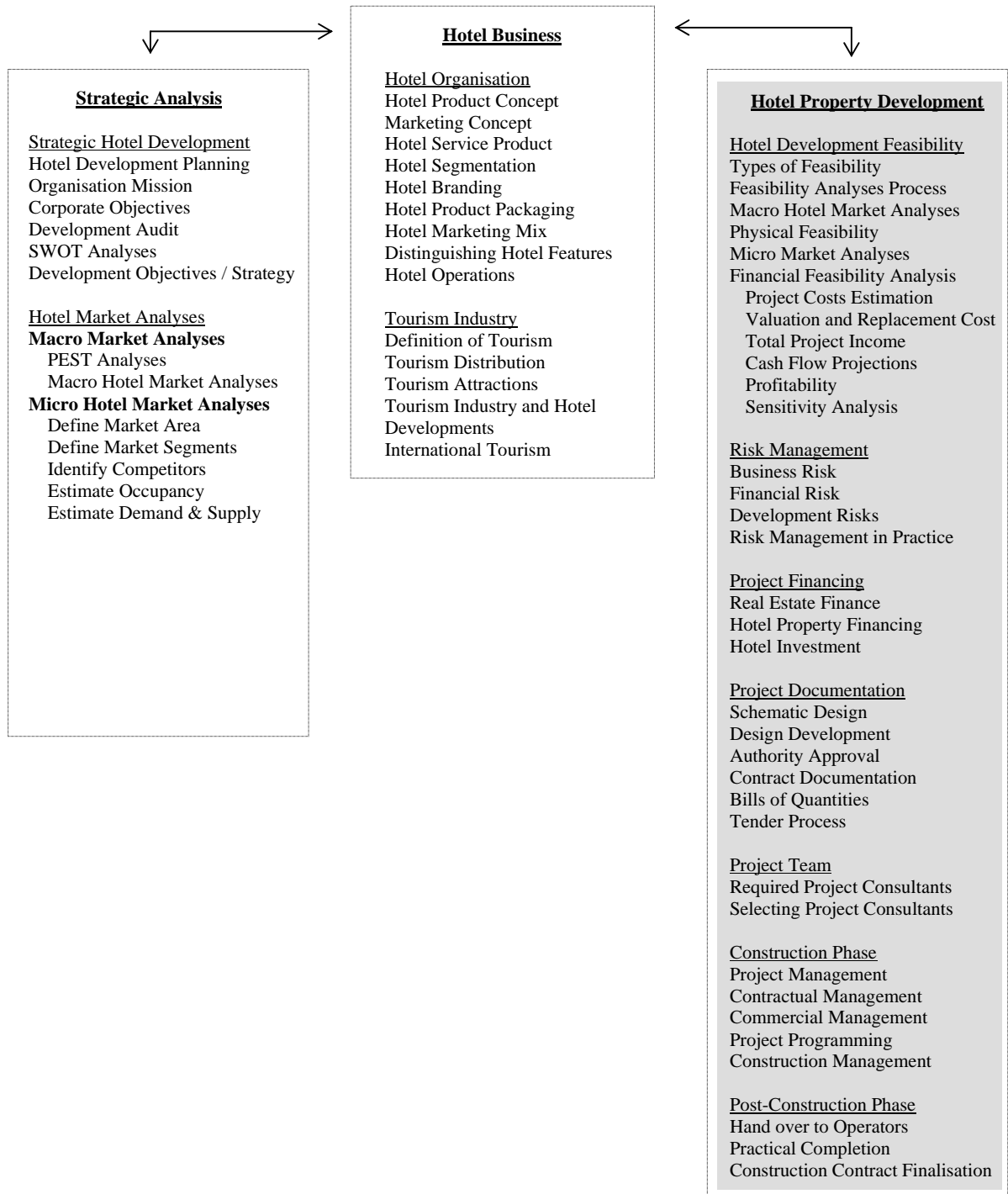
**Table 4.5 (a): World's Top Tourism Destinations by International Tourist Arrivals**

(Source: World Tourism Organisation (WTO): Tourism Highlights 2000)

Rank	1950	Share World	1970	Share World	1990	Share World	1999*	Share World
1	United States	71%	Italy	43%	France	38%	France	35%
2	Canada		Canada		United States		Spain	
3	Italy		France		Spain		United States	
4	France		Spain		Italy		Italy	
5	Switzerland		United States		Hungary		China	
6	Ireland	17%	Austria	22%	Austria	19%	United Kingdom	15%
7	Austria		Germany		China		Mexico	
8	Spain		Switzerland		Mexico		Canada	
9	Germany		Yugoslavia		Germany		Poland	
10	United Kingdom		United Kingdom		Canada		Austria	
11	Norway	9%	Hungary	10%	Switzerland	10%	Germany	11%
12	Argentina		Czechoslovakia		United Kingdom		Russian Fed.	
13	Mexico		Belgium		Greece		Czech Rep.	
14	Netherlands		Bulgaria		Portugal		Hungary	
15	Denmark		Romania		Malaysia		Portugal	
16	Others	3%	Others	25%	Others	33%	Others	39%
Total		25.3 million		165.8 million		458.2 million		656.9 million

## Chapter 5:

## Hotel Property Development





## 5 Hotel Property Development

*“Property development is the process directed at the increase in value of an existing property (undeveloped or developed) by the application of resources (material human and capital)” (Cloete, 1998: 109)*

Further to this definition, Cloete (1998) construes that property development could therefore be regarded as:

- An active form of investment which is not limited to erection of buildings.
- Activities such as the performing of necessary survey work to create building lots.
- The establishment of associated infrastructure, such as the construction of streets, water facilities, sewers, electrical lines.
- The creation of space, in which to play, live, work, and build.
- The redevelopment of existing buildings as well as the erection of new ones.
- It may even include the rezoning of properties.

Wurtzebach and Miles (1995) outline four common development situations, each presenting the developer with different development possibilities. These situations are:

- *A site looking for a use:* This is perhaps the most common situation, where a landowner wants to develop his or her land, or an investor buys land, without first deciding on a particular development plan.
- *A use looking for a site:* The second situation is where the developer identifies a need in a certain area for a specific kind of constructed space for which the most appropriate site must be found.
- *Capital looking for an investment opportunity:* In this third situation an investor has cash money that needs to be invested.
- *An existing development:* The fourth situation is where an existing structure may be converted to a new use or be redeveloped.

*“Although all four situations are common in practice, the second alternative is the most efficient way to turn ideas into reality. The site looking for a use is in some sense putting the cart before the horse. Capital looking for an investment should involve looking at all investment opportunities, not just property development” (Wurtzebach, 1995: 630).*

The idea for a hotel project could originate from many quarters (Baltin, 1999). Generally, one or more of the following parties initiates the development program: an equity investor, investment group, institutional investor, or investment fund; a property owner recognising a development opportunity; a developer that is seeking an opportunity, interested in expanding its real estate portfolio, or needing a cash-producing investment; a developer needing a hotel as a component of a mixed-use development; a hotel development or management company seeking to expand its product into new markets; a local non-profit, tax exempt development corporation; a public or quasi-public agency (such as a redevelopment authority, a planning department, a development corporation, or a tourism authority); citizens advisory committee, or special community task force; a special interest group, organisation of local businesses, or merchants association; or the owner/developer of a sports or entertainment facility.

The development process can be defined as the act of bringing an idea or a concept to successful fruition in bricks and mortar (space) with associated services. It is a complex process requiring the co-ordinated expertise of many professionals. On the investment side, sources of financing must be attracted by the promise of sharing the cash flow generated by development in a manner that properly balances risk and return. The physical construction of the project requires co-ordination among architects, engineers, and contractors. The public sector, especially local government, must approve the legality of the development in terms of zoning, building codes, and so on. Ultimately and most importantly, user needs must be satisfied. This requires the developer to identify a market segment in which sufficient market demand will exist for the type of space to be created.

The development process for a lodging facility, as explained by Baltin (1999: 29): “...is complicated and requires a great deal of planning and co-ordination. The developer plays multiple roles, being a visionary, an entrepreneur, a risk taker, co-ordinator of the various disciplines involved, and ultimate decision maker. The developer is the arbitrator between the hotel project concept and the realities of the marketplace.”

Baltin (1999) explains when selecting the disciplines for developing a hotel, the developer should compile a team that will attend to the nuts and bolts [intricate detail] of planning and implementation. The developer must thoroughly understand the development process, know when to seek professional advice and be able to bring experts in various disciplines into an effective, integrated development team.

The development of a hotel takes many months and sometimes years. It should be market driven, based on the principle that hotels meet the development objectives of investors and owners by providing the type and quality of products and services that the market desires. The development process, therefore, links the investor/owner, the developer and the operator with the public to be served.

“Great uncertainty, an extensive and ever-shifting array of market segments and high expectations on the part of the parties involved frequently make hotel development more challenging and exciting than other kinds of real estate development. A hotel development is both a real estate venture and the creation of a new business establishment. The successful developer will understand this essential duality of a hotel as both real estate and business” (Baltin, 1999: 29).

### **5.1 Property Development Process**

“The development process of hotels - regardless of the hotel’s type, size, location, or market orientation - comprises of five distinct and generally sequential phases (Baltin, 1999: 30)”:

- 1) Development planning
- 2) Assembly of the development team
- 3) Feasibility analysis
- 4) Project implementation
- 5) Initial marketing and operations.

Inter-Continental Hotels defines the following five key development phases for their hotel developments (Inter-Continental Hotel Architectural and Engineering Specifications, 1996):

- Phase 1: Design concept
- Phase 2: Design development
- Phase 3: Contract documentation
- Phase 4: Construction period
- Phase 5: Post-construction period.

Wurtzebach and Miles (1995) explain that the real property [real estate] development process consists of eight stages. Their view is that the flow of activities through the stages represents a typical sequence in real property development. Although this sequence is not followed in all cases, it does provide a very useful framework for analysing the process and it also creates a structure for evaluating individual projects.

The Wurtzebach's eight-stage property development model includes the following stages (Wurtzebach, 1995: 652):

- 1) Idea / Inception
- 2) Idea refinement
- 3) Feasibility
- 4) Contract negotiations
- 5) Commitment point
- 6) Construction
- 7) Initiation of operations
- 8) Asset management over time.

In the same vein as Wurtzebach, Cloete (1998: 111) describes property development as having a number of specific stages. The Cloete property development process consists of the following stages:

- 1) Idea
- 2) Preliminary feasibility
- 3) Gaining control of the site
- 4) Feasibility analysis and design
- 5) Financing
- 6) Construction
- 7) Marketing
- 8) Leasing
- 9) Sale of the project.

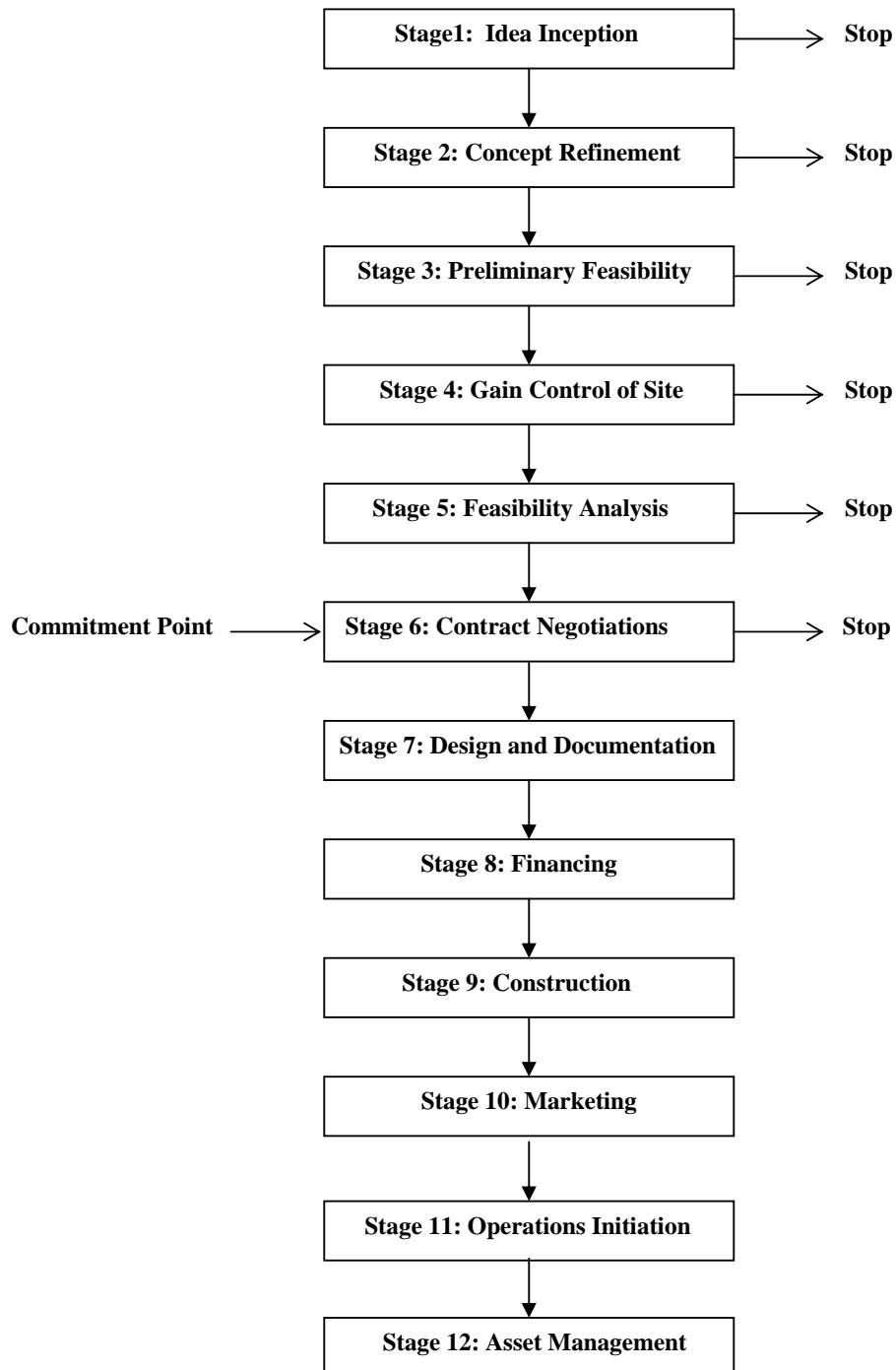
One could gather from the above, that quite a few different approaches and viewpoints of property development exist. A hotel organisation would, as an example, as part of their expansion plan, not start at the very beginning with an idea. They would have a clear direction, objectives and parameters within which opportunities are sought, which is a good example of a concept looking for a site. Contrary to the clear hotel concept and objectives, generally the development concept would start from the idea stage. Quite often the idea for a hotel development starts as part of a multi-use development scheme, e.g. large regional shopping centres, commercial areas and resorts.

The point being made is that one should be cognisant of the fact that the development process is not rigid but rather a flexible process that could be adapted to a required situation.

### 5.1.1 Hotel Property Development Process

Although the characteristics and requirements for hotel property development differ in many respects from other types of real property [real estate], there are also great similarities. In light of this fact and with the aim to develop a generic hotel property development process, the Wurtzebach and Miles, and Cloete property development models, referred to before, are combined in figure 5.1.1(a):

**Figure 5.1.1 (a): Hotel Property Development Process**



### **Stage 1: Idea / Concept Inception**

Mostly all property development processes begin with an idea. The ideas are usually visualisations of a particular type of hotel or resort project. Many of the more successful hotel developers are quite good at visualising what types of facilities are needed and where they should be located. Generating ideas is the most creative aspect of the real estate industry, and by reading, looking, listening, and thinking, the developer finds new combinations of place, built space and services to satisfy tomorrow's consumers' needs (Wurtzebach and Miles, 1995).

Successful hotel development requires a comprehensive understanding of the hotel industry, markets, trends, etc. which is then combined with thorough knowledge of the development process from stage 1 through to stage 12. The developer would consider the possible guest market segment, geographical market area, location, hotel size, hotel brand, services, infrastructure and possible sources of financing, to name a few requirements. Along with the developer's thorough understanding of the development process, it should also be ensured that the development is market driven, based on the principle that the hotel meets the development objectives of investors and owners by providing the type and quality of products and services that the market desires.

Most hotel organisations have expansion [growth] objectives, which normally are very clear development parameters and concepts of what property types, locations, market segments, etc. they are pursuing.

*Important to note here, as illustrated in figure 5.1.1(a), is that the developer can still decide to quit at each of the first six stages without major financial loss.*

### **Stage 2: Concept Refinement**

From stage 1, after being scrutinised and evaluated, the development idea becomes a development concept where it is again refined and tested in stage 2.

Firstly, the developer must find a specific area. The site must be checked to see that zoning is appropriate or that appropriate rezoning is possible. Furthermore, there must be access to appropriate transportation arteries, and required municipal services must be available. Also, the previous considerations given to possible guest market segment, geographical market area, location, hotel size, hotel brand, hotel design, image, services, infrastructure, etc. would now be thoroughly investigated and refined resulting in a detailed concept.

From a hotel operator's point of view, Inter-Continental Hotels (Inter-Continental Hotels Architectural and Engineering Specifications, 1996) defines the first task in the development process as deciding, in conceptual terms, how the finished product might look and what market it might serve. This usually entails communication between the developer and a designer to draw up plans and concept drawings. For larger organisations, this might be part of an overall development strategy and brand management, and will take in issues of asset management.

Adding more detail to this stage, Baltin (1999) explains that the developer should achieve the following tasks:

- Establish financial, development, and operational objectives.
- Identify the major development issues.
- Formulate a development concept, and
- Hire a professional financial and development adviser and establish a timetable (development programme) to guide the durations allowed for the feasibility analyses, anticipated design phases, commercial and contract documentation, construction phase and all pre-opening activities.

*“Seasoned real estate professionals allocate a generous amount of time and resources for this phase. The objectives established and the plans made at this time will serve as a framework by which they could measure the subsequent progress and success of the development process. In some cases, too little effort goes into the concept-planning phase, due to restricted budgets, time constraints and a strong desire to get started. But the result of cutting corners here is likely to be a hotel that performs poorly.*

*The first question a developer needs to answer is: ‘Why are we developing this property?’ The reasons can range from pure economics to pure emotion - the lure of having a world-class place of one’s own in which to entertain or be entertained. There are many strategic reasons for developing a hotel. Once having identified a compelling reason (vision) for a hotel’s development, the developer must proceed to validate the vision” (Baltin, 1999: 30).*

For most hotel projects, it is important to obtain the services of a professional financial and development adviser during the development-planning phase. On complex projects, having such an adviser on board early is particularly important. The responsibilities of the adviser at this stage depend somewhat on the sophistication and hotel development experience of the project initiator.

Also during the concept refinement stage, the developer will begin to look for general contractors who are available to do work in the area. Potential permanent and construction lenders will be approached to ascertain their general interest in providing loans. A check of possible sources of equity capital will be made, and the tax ramifications of alternative financing structures will be considered.

The concept refinement stage is critical to the developer and requires the exercise of careful judgement about whether to go ahead, to rework the idea, or to abandon it and start over. This preliminary planning phase is complete when the development objectives are set, a real-world awareness of the major opportunities and constraints facing the project is defined, an initial development concept completed, professional financial and development advisers are hard at work, and a timetable for the feasibility analysis is set, the developer’s idea has taken on a location and a physical form, and has finally been tested for physical, legal, and financial feasibility.

### **Stage 3: Preliminary Feasibility**

At this stage the developer will perform a rough cost and income analysis.

The market segment being targeted will determine the range and specification of guest facilities, and ultimately the related construction, furniture and finishing requirements. This information together with additional estimates such as professional fees, land cost, local authority fees, etc. will then be used to determine the rough development cost figure. On the income side the developer should determine the average room rate and average annual

occupancy being achieved in similar markets, market areas, market segments, etc. by competitor hotels. From this the developer will devise a rough estimate of the revenue stream that the project will generate. Subtracting the cost of providing the necessary guest facilities and ongoing services, from the estimated revenues, the developer obtains a projected net operating income (NOI).

From this income stream, a very rough project value can be established, based on current market capitalisation rates.

The developer will go through this relatively inexpensive process many times, and only when these rough estimates meet the development objectives should the developer move on to the next stage of the development process.

Also at this stage the developer will prepare schematic architectural layouts and determine some aspects of physical feasibility. The developer will arrange for soil tests to determine the load-bearing capacity of the ground, examine the grade and configuration of the site, and consider any other unique physical characteristics. The developer's architect determines whether the general type and size of the envisioned project can be placed on the site. The building must be put on the land without compromising the overall visual impression of the site or the functioning of the constructed space for the proposed tenant. Appearance and function are important not only to marketability and operations, but also to the developer's relationship with his ever-present partner, government, on all its levels and in all its forms.

#### **Stage 4: Gaining Control of the Site**

It is quite important that the developer gains control ('tie-up') of the site, but not necessarily purchasing it at this early stage in the development process. At this stage the developer would be reluctant to commit large sums of money to a piece of land that may not end up being developed. However, doing extensive planning prior to gaining control of the site, can leave the developer in a disadvantageous negotiating position with the landowner. Consequently, the objective at this time may be to arrange for an option on the land, a long-term lease or possibly a low down payment with no personal liability. The site will then be available when needed and premature investment will be minimised.

#### **Stage 5: Feasibility Analysis**

The formal feasibility study commences in stage five, the pre-commitment stage of the development process. Once control of the site has been obtained, a more detailed feasibility study can be undertaken. How detailed the feasibility study is, depends on the project and the developer.

A complete feasibility study will analyse the legal, site, market and financial aspects of the proposed development, to name a few aspects. Legal analysis will tell the developer how much and what kind of space can legally be developed. Site analysis will provide information such as the ability of the soil to support structures and any special problems for construction. Varying degrees of market research are possible to answering questions about the size and type of facility to be developed, which in essence will be based on regional and local economics, tourism and relevant market data. Preliminary drawings will be made, trading off an aesthetic market appeal against the cost of the particular project. From the preliminary drawings, more refined construction cost estimates will be made.

Also part of the feasibility study is a clear statement of all the aspects to be addressed with local and regional authorities. This would include not only required building permits but also all possible local and regional authority fees assuring that all the public services (water, sewerage, etc.) will be available for the project.

What constitutes an acceptable or unacceptable project, at this point, depends on the objectives of the developer and the ability of the project to satisfy them. This means that the same result from a feasibility study may lead one developer to consider the project acceptable while another finds it unacceptable. One cannot say that a proposed project is acceptable without considering the specific developer.

If these more detailed feasibility analyses indicate that the project does not meet the set objectives, the project should be abandoned at this point as the developer now starts paying significant amounts of money to the architect and other consultants for preliminary drawings, market study, feasibility analysis, engineering, etc.

### **Stage 6: Contract Negotiations**

The contract stage is the point at which written agreements are entered into with all the key participants in the project. On the financial side, a permanent loan commitment will usually be obtained. The permanent lender, relying on the developer's feasibility study as well as on its own analysis and appraisal of the site and project, grants a loan on the premise that the project is built according to plans and specifications. The developer will then take the permanent loan commitment to a potential construction lender. After convincing the construction lender that the project is likely to be completed on time according to plans and specifications, the developer obtains a construction loan, to be funded in stages as the project is built.

After securing the permanent and construction loans, an operator should be appointed, should the developer choose not to take on the responsibility of operating the hotel. Operational contracts could comprise various forms of which franchising, joint ventures and management contracts are the most prevalent. Hotel operators such as Holiday Inn or Sheraton often develop their own hotel properties, and are then referred to as owner-operated hotels (Ransley & Ingram, 2000).

The developer must at this point also start communicating with building contractors, who have extensive hotel construction experience. It should be decided whether the construction contract will be negotiated on a one-to-one basis or if the contract will be awarded through a tender process, which includes all interested pre-qualified general contractors. Other questions that should be answered are whether the architect will supervise the construction process or should a project manager be appointed? What type of construction contract will be used and the details of the agreement between the client and the contractor?

When the hotel facility includes any leasable areas, e.g. convenience shop, memorabilia and souvenir shops, stationary shops, bars and restaurants, the developer should consider what the hotel operator's operational strategy is. Will they outsource these facilities or operate and manage the facilities in-house? This fact is important because the developer should at this stage attempt to pre-lease these areas, should the operator not take responsibility for these facilities, and further it is necessary so that the marketing function can continue without interruption.



A decision on financing the equity must be made. Should a money partner be brought in to share development risks? Should the project be sold in advance to long-term equity investors? What particular investment vehicle would be most advantageous, considering the tax shelter possibilities as well as the risks involved in the particular development?

Finally, before proceeding to the next step the developer comes to the big decision. The commitment point is the culmination point of all information obtained from stages one through five, and is the point of principal decision by the developer – do we proceed or not?

### **Stage 7: Design and Documentation**

Before detailed design commences, a development budget should be drawn up as an essential aid to achieving objectives successfully by maintaining project cash control and preventing budget overruns. Exceeding the budget could result in a failure to complete the project or cannot not meeting the set developer, investors and operator objectives. If the hotel is not completed or commence operations on schedule, extra interest costs and lost rental income could impinge on profitability. If any of the parties involved in construction are confronted with financial difficulties, the project could be held up by legal proceedings.

Time control should also be well established by scheduling the work of the different parties on the project in a critical path method. This process allows the decision-maker (project manager) to identify and focus on the critical path [sequential critical programme activities], directing resources to those activities, which if delayed, will delay the final completion of the project.

The concept and schematic designs done in the earlier stages are now developed into detailed and formal working drawings. Detail design starts with a process called design development, which is a fluid and flexible process in which all operational requirements, aesthetics, local authority requirements, image, brand identity, ergonomics, etc. are all coordinated into a practical, optimal and appealing environment. As soon as the developer and operator approve areas of design, those facilities would then be submitted to a detailed design process. The detailed designs are finalised in working drawings, which are issued to and used by the building contractor to construct the hotel.

At the same time and in conjunction with the design process, the contractual documentation processes are also started. Contractual documentation includes a wide range of items, such as general specifications, quantity takes-offs resulting in the bill of quantities, tender documentation and building contract only to name a few.

The general contractor is usually selected and appointed during this stage. The contractor should be selected with care, whether it is by negotiation or a tender process. The contractor should be financially sound, have a good track record in projects similar to the one planned, and be credit worthy.

### **Stage 8: Financing**

During the feasibility analysis and design phase, preliminary discussions are started with construction and permanent lenders. Once the plans are completed and the project has been determined to be feasible, financing negotiations will be finalised. First, permanent financing will be arranged, after which the construction financing is sought. The

construction lender will want to see a firm commitment from a reputable permanent lender before considering a request for construction financing. Any difference between the construction loan amount and the cost of the project represents the required equity investment in the development of the project, and will normally have to be provided upfront.

### **Stage 9: Construction**

During this period the facility is built and the developer's previous limited financial exposure changes to large amounts being paid out. As a consequence of the large amounts of money being spent, the developer seeks to reduce the construction time during which he experiences maximum financial exposure.

Periodically during construction, the subcontractors submit payment certificates (payment requests) for their costs to the general contractor, who again submits the total value of work performed to date to the developer for payment. The developer adds all other relevant costs e.g. consultant fees, insurance, financing interest, marketing expenses, etc. to the direct construction costs and sends a draw request to the short-term lender. The short-term lender when satisfied with the request for money, places funds in the developer's bank account, after which the contractor, subcontractors and other parties are paid.

Before payment will be made to the contractor, the constructed work for which money is being requested will be inspected and certified by the architect. This procedure makes sure that the work has been done according to plans and specifications, thereby protecting the lender. Furthermore, if the building contract does not require the contractor to furnish a performance guarantee before commencing the work, a portion of the payments due to the contractor and the subcontractors (perhaps 10 percent) will be withheld. This practice, known as retention, is intended to protect the lender (and developer) against incomplete or defective work. The retained sums are paid to the contractor after the architect certifies that the project has been completed in accordance with the plans and specifications.

The project manager, hotel marketing / operations representatives and financial officer, all members of the development team, work closely together during this stage. The project manager must be sure that the project is being built according to plans, specifications and on time. The hotel marketing and operations representatives must see to it that the targeted guest markets are informed of the new hotel being developed, operating staff is trained in advance, facilities are functioning and that the hotel opens on time.

### **Stage 10: Marketing**

Marketing at this stage comprises of major marketing campaigns, with the aim of communicating and building awareness within the target markets, of the new hotel, the facilities it offers, what brand it is and when it is due to open.

Marketing a new or improved hotel usually starts at an early stage (concept stage) of the development process, with light media coverage only. As soon as the developer commits to constructing the facility, all possible opportunities falling within the parameters of the marketing plan, are used to create awareness.

The ultimate success of a hotel development project depends on its marketability. Generating cash as early as possible is critical to the success of a project because the entire

construction period is one of cash outflows. Often developers underestimate or simply fail to consider the cash necessary to operate the property after construction is completed and before the project is producing enough revenue to cover costs. Some projects require years to reach a breakeven point, and many projects ultimately fail during this period.

### **Stage 11: Initiation of Operations**

At this stage all construction work is being completed and operating personnel are brought on the scene. Pre-opening advertising and promotion takes place, utilities are connected, operating equipment is commissioned, municipal requirements such as inspections and certificates of occupancy are satisfied.

The commissioning of equipment is followed by the initiation of hotel operations, which is referred to as the 'soft opening' phase, during which all personnel, systems, equipment and facilities are applied as during normal operating conditions. The aim of the 'soft opening' phase is to highlight any possible problems that may arise when operating, whilst giving management the opportunity to rectify the problems before the actual opening.

As a promotional exercise the hotel operator usually invites influential people, contacts, media and marketing / distribution intermediaries to use the hotel facilities for a day or two on a no-charge complimentary basis.

On the financial side, the permanent loan is finalised and the construction loan paid off. Unless the developer is keeping the property as an investment, long-term equity interests take over from the developer (based on a presale contract or a sale after completion).

### **Stage 12: Asset Management**

Asset management includes all facets of maintaining, releasing and repositioning of real estate assets in the marketplace over its economic life. To do this well at best of times, is a challenge. In today's overbuilt markets, the capacity for quality asset management may be the critical ingredient in financing and initially leasing any new development.

*"Hospitality [hotel] properties are generally high-value, capital-intensive assets that require concentrated management in order to generate adequate returns on the capital employed. To achieve this objective, the investor must finance and develop a product at reasonable cost that meets market needs. The investor must then maximise revenue and profit from the investment by ensuring the property is effectively marketed, efficiently operated and that adequate capital is reinvested in the product to maintain its competitive position"* (Ransley & Ingram, 2000: 38).

One of the most important concepts to understand in hotel asset management is that the value of the hotel comprises two components, namely an asset (real estate) component and a business (or operating) component. "Historically, the hospitality industry has tended to focus on one or the other - usually depending on whether one's background was in real estate or in hotel operations. Today, however, it is essential that an asset manager understands both the asset and business components to optimally manage and maximise the performance of a hotel investment" (Raleigh & Roginsky, 1999: 95).

### Asset (Real Estate) Component

An asset manager needs to be concerned with:

- The age and condition of a property
- The cost to maintain and/or refurbish the property
- Barriers to competition
- Existing and potential functional obsolescence issues
- Regulatory issue.

*“Functional obsolescence, meaning the need to replace or upgrade a capital item due to changing needs rather than the actual physical deterioration of an asset, represents a major challenge for many hotels today. From rewiring older hotels to keep pace with customer expectations for services (for example, additional telephone lines in guestrooms) to updating group meeting-space layouts to fit the needs of today’s meeting planners, many hotels are dealing with major functional and potentially costly alterations to correct obsolescence issues”* (Raleigh & Roginsky, 1999: 96).

### Business (Operating) Component

Here an asset manager needs to think about the same issues that would be important in evaluating any type of business. He/she needs to evaluate the revenue performance of a hotel, including the hotel’s business mix, the seasonality of the business and rate and occupancy performance.

The business performance review and evaluation should also include a review of other financial barometers. It might include a review of fixed versus variable costs (or operating leverage), such as departmental costs per guest, or per occupied unit ratio analysis and other comparative performance ratios (compared to the previous year or comparable property).

#### **5.1.2 Hotel Property Redevelopment Process**

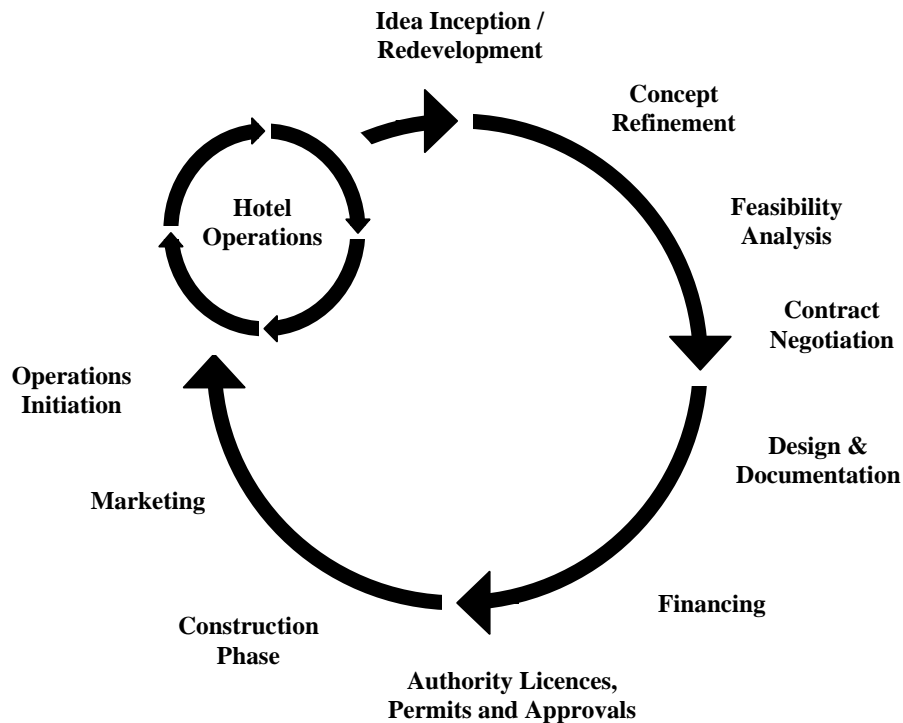
The hotel development process (section 5.1.1) mainly focuses on new [proposed] developments and does not address hotel redevelopment (refurbishment, renovations and extensions), which forms a large and significant part of hotel property development.

The stages included in the property redevelopment process are similar to that of the new hotel development process. The basic difference between the ‘newly-built’ [proposed] property development process and the redevelopment process is that the latter is a continuous process that is repeated at regular intervals owing to interior changes, renovations and extensions.

Once a development is complete and functioning, the effectiveness of the operation needs to be reviewed periodically, to establish whether the organisational objectives and customer requirements are met. This process gives rise to the property redevelopment / improvement cycle (Refer to the illustrated in figure 5.1.2(a)).

**Figure 5.1.2(a): Hotel Redevelopment Process**

(Source: An adaptation of The Project Cycle (Echavarren, 2001: 4))



## 5.2 Strategic Hotel Property Development

Management could be categorised in three levels, i.e. executive (strategic management, long term), business (business management, medium term) and functional (daily operational management, short term). At each of these different levels of management, objectives are set and strategies defined to achieve the objectives. Objectives at the executive level are usually defined in financial terms, i.e. ROI, net profit, share values, etc. To achieve the executive objectives, strategies at the executive level are formulated through a process of strategic analysis, guided by the organisation's mission. At the next level, the business level, the executive strategies become the business level objectives to be achieved in the medium term through the business level strategies. The business strategies are formulated through a process of market analysis. Similarly, the business level strategies become the functional level objectives to be achieved through functional strategies. In summary, strategies could be seen as the vehicle to achieving the targeted objectives. (Pearce & Robinson, 1994)

The starting point of all major business decisions should be the organisation's mission statement with its associated goals. The mission of an organisation should articulate the vision and give a sense of direction (Brookes, 1999).

From the hotel organisation's mission, objectives and strategies, the hotel development department should develop its own specific task orientated mission statement, objectives, strategies and control procedures.

Should a hotel development not be executed by a hotel organisation, the developer should have a thorough understanding of possible future hotel operator's strategic context, hence the necessity for early alliance with a hotel operator or hotel development consultant in the development process is strongly advised.

Ransley and Ingram, (2000) advise that those concerned with preparing a development strategy need to know where the business is going, to develop a sound knowledge of the product / brand, and to be aware of the characteristics of the customer profiles. The objectives should be clearly articulated at the beginning of a plan as part of a strategic vision and mission. In some instances the plan can be for the corporate entity as a whole, in other cases it may be that there is an individual plan for each project (which could then be consolidated into the corporate plan).

An analytical and questioning approach to strategic planning allows management to put together its game plan for the business in order to identify the resources needed, and deploy them successfully to obtain a favourable commercial position. Development plans are important to hotel organisations and can have a significant effect on the future success of the business.

To establish a sound property development plan for either an organisation business unit or a specific project, extensive planning and consideration should be given to various strategic issues such as development strategy, project objectives and strategies and development criteria to name a few.

### **5.2.1 Hotel Development Strategy**

A development strategy is a statement of how an organisation intends to reach its growth objectives, and in the hotel industry this often means the construction of new units. Clear criteria need to be set for the hotel building, facilities and other considerations, such as the site. Development considerations would include the site size, cost per room and total development costs, and some general guidelines that could help with the rapid appraisal of potential new projects. Finally, a set of locational criteria should be developed to assist in ensuring that the hotel is constructed in suitable contexts. This shows how a clear development strategy can assist in the proliferation of a hotel brand.

There are very few organisations today that do not have a development strategy which details where they are at present, where they would like to be within a realistic time frame and defining how they will bridge the gap between these two. It is perhaps self-evident but the preparation of a development strategy requires an honest and analytical approach to the business, and depends on the 'vision' of the building blocks required to achieve the mission. The resources required to become 'the largest branded hotel chain in Europe' might be very different to those required to 'prepare the company for a public share offering in four years' time'. It is important to clearly identify the resources needed, and at the same time build in an element of flexibility to take into account the possibility of unexpected changes in circumstances. (Ransley & Ingram, 2000)

The development strategy will define and analyse in considerable detail the following internal and external questions:

*Internal:*

- What are the objectives of the organisation and its shareholders and stakeholders?
- What are the brands, products or services being supplied and how might they be described?
- Where are the strengths and weaknesses in the organisation?
- What are the opportunities and threats for the brand?
- What is the pricing policy and how does it relate to price sensitivity in the marketplace?

*External:*

- Who is the competition and what is known about them and their strategies?
- How can a competitive advantage be obtained?
- Who are our customers? What is known about them and their characteristics or buying habits? Are these characteristics likely to change and if so how and why?
- Are there external influences that are likely to affect the 'marketplace', including political, environmental, economic or legislative issues?

An example of the objectives defined in a hotel group's development plan is the following by Trust House Forte's Post House Hotels, United Kingdom (Ransley & Ingram, 2000: 26):

- Expand the group by adding three new hotels a year for a five-year period
- Take the brand ultimately into Europe from a strong UK positioning
- Become the preferred hotel group of choice for the business and leisure traveller operating in the mid-price market
- Maintain value for money
- Sustain brand loyalty and increase market share
- Provide an above average return on investment
- Develop an economic model for the evaluation of opportunities.

Finally, branding is an increasingly popular method of marketing and developing hotels because it communicates a consistent and understandable message to the potential guest.

### **5.2.2 Hotel Development Criteria**

All the elements that might affect the development of the hotel product and the owner's requirements should be considered. During the 1980s, the Trust House Forte's Post House chain, after extensive research, formulated a development plan and a strategy for future business expansion. The development plan included criteria for the hotel, site and other considerations: (Ransley & Ingram, 2000)

#### **Hotel Criteria**

1. Demand had to emanate predominantly from the corporate organisations in the locality, but there should also be potential demand for underpinning the weekend/leisure periods, from local social functions (including weddings, anniversaries) and for small meetings.
2. Hotels had to be built where there is demand for a preferred minimum of 120 rooms, with a maximum size of 180 rooms.
3. Every bedroom had to have a bathroom, and rooms would be 24 to 26 square metres in size.

4. All hotels had to have two catering outlets, a function room, several boardrooms and a swimming pool.
5. There had to be only one central kitchen, with a capacity to service all outlets in the unit.
6. Staffing levels had to be in the order of 0.6 to 0.7 staff per bedroom.
7. There had to be ample car parking spaces, on average 1.2 spaces per bedroom to allow for guest and staff requirements.

#### **Site Criteria**

1. Minimum of 0,46 hectares, and preferably no more than 0,78 hectares.
2. Flat or only gently sloping land.
3. Visible (from major trunk roads or motorways) and easily accessible, without the construction of major access roads.
4. Hotels near motorways had to ideally be located close to a full motorway junction allowing access and exit in both directions.
5. Services and utilities (electricity, gas, water, and sewage) needed to be close to the site and provided at minimum cost. If the cost of providing these services were abnormal then it would mean that either there had to be compensating cost reductions elsewhere or that a premium on the tariff had to be obtained.
6. Attractive, without electricity pylons or other visible intrusions or defects, and away from major intrusions of noise (i.e. not adjacent to a railway line or in a flight path) and obnoxious smells.
7. Maximum cost of £160 000 per hectare.
8. Available on a freehold or long lease basis only.
9. Well-drained land at the site.
10. Pleasant or attractive views an advantage.

#### **Other Criteria**

1. There had to be no difficulty in obtaining planning permission and there should preferably already be outline planning permission for hotel use within the Local Government Structure Plan.
2. The hotel development had to be realisable within a realistic time frame, ideally two to three years.
3. Local authority support for the development.
4. No serious objections from local residents or community groups.
5. If there were financial inducements or grants for the project these were seen as advantageous and would be pursued.
6. No foreseeable major changes that had to negatively impact the site or its major demand factors (these could be changes to the road and infrastructure network, or changes to the demand profiles).
7. The financial feasibility forecast had to show a high probability of 15 percent cash on cash return on investment in a stabilised year.
8. Properties had to be 100 percent owned by the company (Trust House Forte), and management and joint venture agreements had not been considered (there was no franchise or licence product at that time).
9. Signage, external to the building and from local access roads would be necessary.



Ransley and Ingram (2000: 34) further explain that the rationale behind the above criteria was mainly economically and commercially driven, and these were factors that directly affected the feasibility and viability of a proposed Post House hotel. This case demonstrates the relationship between site size and the final cost per room. Sites of less than 0.78 hectares require a high-rise structure that would drive up comparative development costs. Further, it was more in keeping with the brand to develop in semi-rural locations where space was not a problem. The size was also evaluated in 'staff cost' terms, as hotels of that brand have a similar management structure whether 100 or 175 rooms in size (below 100 rooms it was difficult to support the structure and over that a more specialised management was required).

Although market research was undertaken to assess the demand profile and strength for each specific Post House site, this is not a precise science when it comes to hotels. During the lead-time of building a hotel, with a typical period of thirty months from the time of commitment to a project to opening for trade, the demand and supply factors can change. The reputation of the brand and pricing policies can also affect business volume levels. Therefore, much of the research was directly focused on identifying risk factors and working on ways to reduce and limit risk exposure.

Most hotels in good locations that market to business travellers might expect reasonably high levels of demand in midweek (Monday to Thursday) outside of holiday periods. If the hotel achieves full occupancy for these nights, that statistically still only provides a room occupancy of about 38 per cent over the week, far short of the 65 per cent that is generally recognised as necessary to achieve adequate levels of profitability for most newly constructed hotels. Accordingly, such hotels must generate weekend demand from other market segments. In resort locations the equation is slightly different, but the general principles are the same. A hotel might experience peaks in the months of May to September, and the shoulder (off peak) months March, April, October and November. There may be little or no demand in the winter months. The planning of resort hotels requires the developer to forecast demand for each potential market segment and the effects upon revenue and profit.

In the case of Post House hotels, it was also found that a lack of support from local authority planners could make the process costly, time-consuming and uncertain.

Having defined the criteria for the Post House hotels, it was then possible to look at the geographic locations for the hotels and the economic generators of demand. The following were typical parameters for location choices that were used in appraising sites:

- Major cities with a population in excess of 150 000 inhabitants
- Airport locations that dealt with at least 4 million passengers per year.
- Major employers in the locality, not in traditional heavy industries but in sectors that generated demand for hotel accommodation.
- Local attractions within a maximum of a 40-kilometer radius that could be promoted so as to attract weekend stays at the hotel.
- Other weekend demand generators such as universities or public schools were seen as a bonus, as were major sporting venues.
- Passing trade from the motorway/trunk road should be composed of a large proportion of distance traffic as opposed to local commuting traffic.
- No other group hotel in the city that might compete with the new development.

This illustrates how closely development strategy and brand management go together and, for the most part, hotel constructions in the UK have been successful. However, there have also been mistakes. For example, when Novotel first entered the UK market, it tried to replicate the standard French product in locations in the UK, and hotels were built in the north of England with outdoor swimming pools that could only be used for a few weeks of the year. When Post House decided to enter the German market, they kept the name, which in German means 'post office'. A 'Post Office Hotel' sent out conflicting messages and caused confusion as to the nature of the brand.

### 5.2.3 Project Objectives and Strategies

Arthur Andersen Real Estate Services highlights in their Corporate Finance Quarterly Report for Europe 2001, that from experience the most common downfalls when developing a project are: (Echavarren, 2001)

- Lack of vision and objectives for the project: the project arises on impulse and its strategy and objectives are not clearly defined.
- Unrealistic objectives: estimated savings or expected returns are not calculated properly.
- Inadequate project specifications, requirements not calculated, areas undefined

The development planning of a property starts with setting overall objectives. The central problem with many unsuccessful hotels is that the inexperienced party's original inspiration is never solidified with sound business planning. Some developers and investors attempt a project without considering their level of commitment, their ability to finance the project, or their expectations of financial gain. Developers building a hotel in a mixed-use development often fail to make these critical assessments. Developers that perceive an overriding need for a hotel often ignore good planning practices.

Answering the following initial questions will aid the development team in its effort to establish a property's development objectives (Baltin et al, 1999: 30):

***“Financial Objectives:** Is long-term value appreciation an objective? Is the creation of an operating entity an objective? Are development profits being sought? What are the priorities of the developer regarding these goals? How much equity the development partners can invest? Can the developer obtain financing for a project of this magnitude? What return on investment will be acceptable to the developers and the potential financial partners? How much time, money and resources can be committed by all parties involved?*

***Development Objectives:** Does the site present development constraints? Development opportunities? Is the site free of toxic contamination? Are the surrounding land uses (existing and proposed) compatible with a hotel? Who will serve as the developer? How familiar is the developer with the hotel development process? Is making a special statement an objective (through distinctive design, for example)? Will government policies encourage or discourage development of the site? Are appropriate public financing incentives available? How will the public react to the proposed development? How long will the necessary approval processes take?*

**Operational Objectives:** *What type of hotel management will be best - franchise, affiliate, or owner/manager? Can the owner/developer manage the hotel, or will the services of a professional hotel operator be required? What level of owner/developer involvement in the hotel is desirable or even possible?"*

These objectives must fit with real-world conditions. Thus, initial planning has to identify any conditions and activities that could have positive or negative impacts on the hotel's development. Important data must be assembled at this early stage and consultations initiated with experts and potential participants (public agency officials, lenders, developers, syndicates, bankers, hotel operators, and architects). Failure to do so will limit the developer's chances of putting together a development program that is economically feasible. The developer must obtain the answers to some detailed questions on development issues.

### **5.3 Requirements for Successful Hotel Property Development**

Due to the fact that the requirements for successful hotel property development specifically applies to this section named Hotel Property Development, the important factors for achieving success in hotel property development are repeated (refer to section 2).

It is imperative for a hotel developer or hotel organisation that wants to develop a hotel, to establish an overarching comprehension of a wide, but specific range of hotel operational and development factors. Success requirements according to Lawson (1995: 1) could generally be grouped under the following five headings:

- *Marketing:* an increasing and unsatisfied demand for accommodation stemming from the tourism, recreation and business attractions of a locality.
- *Economics:* the state of the economy and financial inducements or constraints, which may favour or restrict investment.
- *Location:* availability of appropriate sites with adequate infra-structural services and opportunities for development.
- *Enterprise:* correct interpretation of requirements and entrepreneurial organisation of the necessary finance and expertise to successfully implement a project.
- *Planning and design:* careful planning and design of facilities to create an attractive hotel that will satisfy the marketing, functional and financial criteria.

According to Cloete (1998: 116) the success factors for property developments are relatively controllable even if only in the sense that the developer is able to choose between alternatives, which are:

- Type and quality of property
- Factors regarding location
- Price, interest and costs
- Time
- Advertising.

There are also a number of other factors over which an investor has less or no control:

- International, national and local economic, political and social factors
- National and local government regulations (legislation, town planning and building regulations)
- Short- and long-term business confidence.

Baltin and Cole (1995: 36) define project specific success requirements when cautioning designers who, often incorrectly, do what their clients think is right, rather than what will attract the ultimate client (hotel guest). The successfully targeted development will focus on the market objectives it's supposed to achieve.

A targeted design begins not with colour swatches, but with an analysis of all the information bearing on the hotel's market position, which includes the following:

- Competition
- Available market
- Targeted market segment, by purpose of visit
- Guest profiles using psychographics
- Budgetary considerations
- Consideration of potential amenities, facilities configuration and aesthetics
- Management configuration and goals
- Brand standards, strengths and constraints
- Marketing and distribution capabilities.

Targeted design requires as much data as possible about the potential guest, using both guest questionnaires and interviews with the hotel sales, food and beverage, housekeeping and management staff. The manager, market consultant, designer and owner can then collaborate on a focused design that will include not only decor, but also facilities configuration, pricing, amenities and marketing strategy.

From a hotel operator/developer's point-of-view, Sun International defines their hotel development success criteria as (Mc Gee, 2002):

- Location
- Accessibility (For guests, staff and suppliers)
- Flexibility of design (Combination of room types, e.g. suites, king size, double-double and interconnecting)
- Efficiency of design
- Marketing
- Branding
- Staffing (Skills, training and experience)
- Standards (Education, implementation and consistency of standards)
- Government requirements (Taxes, duties, crime, policies, etc).

Cloete (1998: 118) summarises the various requirements for successful property development as:

- A sufficient demand for the product at a price that justifies investment
- The identification of a cost structure that will ensure the optimum net profit

- The architect's ability to design the product that will meet the demands of the cost structure and also ensure maximum demand
- The development of the project in an area with a good location
- The developer's ability to:
  - control the erection costs,
  - finance the project economically,
  - manage the development effectively,
  - lease or sell the property effectively.

## 5.4 Scope of Hotels

In Baltin et al's (1999: 21) hotel types overview, it is expressed that in general, hotel development has followed paths taken by other types of commercial real estate developments. In the United States during the first half of the 20th century, most hotel development occurred in those city centre (downtown areas) where most office and retail development was also taking place. Then new highways, particularly interstate highway systems and major expressways that wound through and around major cities, sparked the development of suburban areas. Demand for hotel rooms accompanied the outward movement of offices, stores and people.

Hotel products geared toward highway locations and other suburban sites, differed significantly in character from city centre hotels, which were typically high-rise, primarily because less expensive land allowed for low-rise construction. In addition, suburban hotels and motels provided extensive parking because their guests generally arrived by automobile.

Beginning in the 1970s, hotel product segmentation was carried to great lengths as developers and operators attempted to define their potential markets more narrowly and to develop facilities targeted at those markets.

### 5.4.1 Tourist Accommodation Types

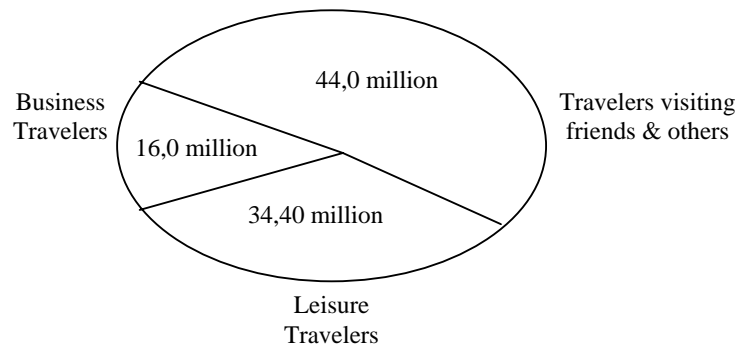
Hotels are not the only types of accommodation used by tourists, travellers and temporary visitors. Lawson (1997: 1) states that in: *"...Europe some 75 per cent of all domestic tourists (people travelling or taking vacations in their own countries) stay with friends and relatives, use camp or caravan sites or rent houses and apartments. In many resort areas a high proportion of visitors own second homes, condominium or time-shared properties."*

Business travellers and foreign tourists represent a significant part of hotel usage in the United Kingdom, as illustrated in figure 5.4.1 (a).

Lawson (1997: 1) further explains that: *"The distinction between serviced hotels and rented accommodation is increasingly blurred. In many budget hotels and lodges the restaurant is operated independently from the accommodation, and bed and breakfast establishments restrict meal service and most resorts offer the option of self-catering or serviced rooms."*

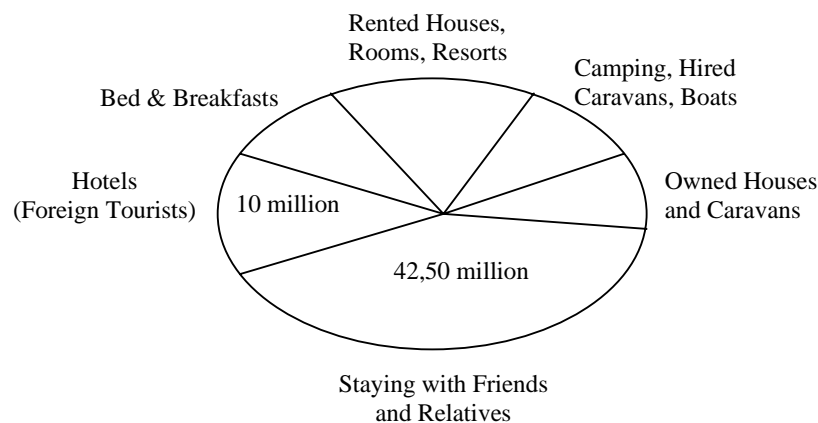
**Figure 5.4.1 (a): United Kingdom Domestic Tourists 1992: Visiting by Purpose**

(Source: Lawson, 1997: 2)



**Figure 5.4.1 (b): United Kingdom Domestic Tourists 1992: Accommodation Used**

(Source: Lawson, 1997: 2)



### 5.4.2 Hotel Definition and Categories

*“In most countries a ‘hotel’ is defined as a public establishment offering travellers and temporary visitors, against payment, two basic services accommodation and meals. The precise definition of what constitutes a hotel and conditions for hotel registration and grading are set out in more than one hundred classification systems worldwide operated by governmental or representative agencies” (Lawson, 1997: 1).*

The words ‘resort’ and ‘hotel’ are quite often used interchangeably, but this is incorrect. It is also used widely and diversely and often means different things to different people. For some, an entire city (such as Aspen, Naples or Brisbane) is a resort, and for others a resort is a second-home golf course community, a hotel on the beach or a ski facility.

To clarify this matter, Schwanke (1997) lists three primary characteristics of resorts:

- Resorts are real estate developments that have been planned and developed, and are currently operated by a private business enterprise.
- Resorts offer proximity and easy access to significant natural, scenic, recreational, and or cultural amenities that make them attractive places to visit.

- Resorts include lodging accommodation, timeshare ownership, and / or residences used largely by tourists, vacationers, weekend travellers, seasonal residents, and / or owners or users of second homes.

Circumstances under which resorts are operated also vary, for example resort hotels may be operated under exclusive contract to one or more tour operator, or they may restrict food service to residents and remain open only during the holiday season. Resorts may also include many different types of accommodation such as guestrooms, suites, self-catering units and supplementary apartments using the hotel services.

The World Tourism Organisation groups accommodation into two main groups (Lawson, 1997):

- Hotels and similar establishments, and
- Supplementary accommodation

**Similar establishments** could broadly be defined and categorised in the following groups:

#### 5.4.2.1 Motels, Motor Hotels and Motor Courts

Motel accommodation is located and arranged to serve the particular needs of the motorist traveller and ranges from the simple court or lodge to more elaborate motor hotels offering extensive conference and banqueting facilities. In most countries, motels are ranked with hotel accommodation and are subject to the same standards. Specific legislation has been introduced for motel requirements in six countries. For example, in France there are three categories classified by location, standards of rooms and fittings and collective amenities. Motel facilities in Turkey require the provision of a service station.

#### 5.4.2.2 Boarding Houses, Guesthouses and Pension de Famille

This type of accommodation generally involves the use of domestic-type property which may be shared with the resident family. Facilities and meals are limited for the use of resident guests, and standards in a number of countries are subject to regulation. Sophisticated facilities for paying guests may be provided in stately houses and chateaux.

#### 5.4.2.3 Bed & Breakfast and Hotels-Garnis

Facilities offering bed and breakfast services range from converted hotels to shared domestic properties. Services are generally limited and many facilities operate only during the tourist season.

**Supplementary accommodation** ranges from camping and caravan sites to rented and owned properties, and could broadly be grouped as:

#### 5.4.2.4 Holiday Villages

Holiday villages are centres of accommodation, usually planned as self-contained resorts, with extensive opportunities for sport and recreation in an attractive natural or created setting. The accommodation is typically in multiple small-scale units clustered around recreational focuses or dispersed in landscaped grounds. Self-catering or serviced options,

including a choice of restaurants, are normally offered with a high ratio of family units, each providing a convertible living room, bedroom(s), bathroom / shower and kitchen.

Commercial holiday villages (holiday centres, camps and clubs) are usually large (600 to 1200 or more bed capacity) with a density of about 150-200 beds/hectare (60-80 beds/acre). Design emphasis may be given to sport and contact with nature (Club Méditerranée, Club Robinson), to enclosed subtropical leisure pools (Center Parcs) or entertainment attractions (Butlins, Pontins).

Specific regulations may apply, as in Spain where holiday villages are classified into three categories according to the amenities and services provided. In France, regulatory standards apply to commercial holiday villages and to social holiday centres like those of the Association Villages Vacances Familiales (VVF).

Village style accommodation may also feature in large integrated resorts and marina developments, in pavilion hotels and as part of resort hotel complexes.

#### 5.4.2.5 Condominiums

Condominium development involves joint ownership of a complex. The condominium owner purchases and has full benefit of a unit (guestroom, suite, apartment, villa) while also sharing in the costs common to the whole complex. The latter usually includes property taxes, maintenance of the premises, upkeep of grounds, roads and recreational facilities and the provision of services such as security, management and letting.

The condominium has many advantages over leased property, enabling the owners to enjoy extensive recreational facilities which are exclusive to the complex. Mortgages are generally available, with tax benefits of property ownership, and capital invested can appreciate with rising values, particularly in prime locations.

Condominiums are often used in multiple developments to generate capital and to provide accommodation back-up for other hotel and convention centre projects. Various schemes have been devised to widen opportunities for investment including single, joint or multiple ownership, sale and leaseback for letting, timesharing and property exchange arrangements.

#### 5.4.2.6 Individual Villas, Apartments, Suites, Cottages

Much of the recent investment in resorts has been in privately furnished villas and apartments for owner occupation and / or letting. Land allocations, financial loans and credits are often available for appropriate development which will contribute to capital costs of resort infrastructure and public amenities. In many European countries, notably France, there are incentives for conversion of redundant farm buildings and cottages to provide self-catering tourist accommodation.

Residential accommodation is subject to the general law relating to housing and public health. Specific legislation for rental apartments has been introduced in several countries. Regulations generally cover such aspects as the capacity, furniture, fittings, amenities, services and sanitation and may include classification based on location, size and furnishings.

Individual investment in rooms and suites may also be provided in aparthotel and marina developments.



The demand for second residences for weekends, holidays, letting and retirement has led to extensive conversion of traditional properties (cottages, farm buildings, mills) as well as large scale real estate development in areas of scenic and climatic attraction (as in Florida, the Mediterranean and European Alps).

#### 5.4.3 Hotel Categories (Industry Segments)

Cahill and Mitroka (1992: 380) oversimplify hotel categories by stating that : *“At one end of the hotel development spectrum is the hard-budget hotel. Near the middle of the segmentation spectrum is the extended-stay hotel. At the opposite end of the spectrum is the luxury, destination resort with expansive recreational facilities, meeting facilities, and public space.”*

From the statement by Cahill and Mitroka, and others, it would appear that many hotel specialists have developed their own unique hotel categories, and no generic or agreed format exists. However, from the plethora of opinions, common categorisations such as those by Lawson (1997: 20), Lane and Dupre (1996: 32), Baltin et al (1999: 22), Ransley and Ingram (2000: 199) and Schwanke (1997: 37) are more frequently used by hotel professionals.

The two principal methods of classifying hotels are by location and by market served. (Baltin et al, 1999: 21):

- **“Location:** *The primary locational distinction is downtown (city centre) hotel versus suburban hotel. Other frequently used categories include airport hotels (hotels located on airport grounds or near airports) and highway hotels, (hotels not in city limits and not in what generally is considered a suburban location). Classifiers sometimes include “resort” as a locational category, but more often the term “resort” in resort hotel refers to the facility’s amenities (on site or nearby) rather than its location. Resort hotels can be located almost anywhere. However, the vast majorities are found in either waterfront or mountain locations.*
- **Market Served:** *Categorisations of hotels on the basis of the niche or segment of the market they target have evolved. It is probably more accurate to describe hotels on the basis of markets served rather than by distinctions between locations, which have become somewhat blurred due to urban sprawl.”*

Two hotel classification schemes based on **market served** are presented in table 5.4.3(a) and table 5.4.3(b). The generic classification in table 5.4.3(a) developed by PKF Hotel Consultants (Baltin et al, 1999: 22), sorts hotels according to five criteria, i.e. price, function, location, special market served, and distinctiveness of style or offering. Similarly and as an example, Six Continents Hotels identifies segments (refer to table 5.4.3 (b)) within which they place their separate hotel products, i.e. mid-scale, up-scale and upper-scale. According to Hilberath (2001), the global trend to classify hotels into price segments is the contemporary replacement of the grading system, discussed in section 5.5 (Hotel Grading and Standards). Most international hotel media communication and promotions also support this trend.

**Table 5.4.3(a): Types of Hotels by Development Criteria**

(Source: Baltin et al, 1999: 21)

<b>Distinguishing criteria of different types of hotels</b>				
<u>Price</u>	<u>Function</u>	<u>Location</u>	<u>Market Served</u>	<u>Distinctiveness of Style or Offerings</u>
<b>Budget or economy</b> Rooms only, little public space, no food and beverage	<b>Convention</b> Large, 500 or more guestrooms, extensive public space and meeting space	<b>Downtown</b> High-rise structures, attached parking; wide mix of facilities and amenities	<b>Executive-Conference Centre</b> Secluded settings, fewer than 300 rooms, small meeting rooms audio-visual facilities and variety of recreation facilities	<b>All-Suite</b> Larger than normal guestrooms, living and sitting areas separate, minimum public space, facilities equipped for extended stay (e.g. kitchenette)
<b>Middle-market</b> Range of facilities and amenities	<b>Commercial</b> Functional guestrooms, ample work area small meeting and conference rooms, limited recreation facilities	<b>Suburban</b> Low- to mid-rise structures, parking meeting and banquet facilities	<b>Health spa</b> Catering to market looking for specific need, such as weight loss or hedonistic experience, staff consists of a variety of trained professionals such as dieticians, therapists, and counsellors	<b>Historic Conversion</b> Well-known historic buildings and landmarks renovated or converted to hotels
<b>Luxury</b> Upscale decor and furnishings concierge service, high-quality public space, higher-than-average employee-to-guest-room ratio		<b>Highway</b> Low-rise structures, outside parking exterior corridors have outdoor pods  <b>Airport</b> Adjacent or attached to airports, efficient	<b>Resort</b> Emphasis on recreation, extensive food and beverage and banquet settings are picturesque	<b>Mixed-use hotels</b> Mixed-use developments consisting of hotels, retail, and other attractions.

**Table 5.4.3(b): Six Continents Hotels Brand and Market Segmentation**

(Source: Six Continents Hotels Product Segmentation, 2001)

<b>Mid-Scale (Limited Service)</b>		<b>Mid-Scale (Full Service)</b>	<b>Upscale (Full Service)</b>	<b>Upper-Scale (1<sup>st</sup> Class) (Full Service)</b>
<b>Without F&amp;B</b>	<b>With F&amp;B</b>			
<b>Holiday Inn Express</b> (Leisure & Business Traveller)	<b>Holiday Inn Garden Court</b> (Leisure & Business Traveller)	<b>Holiday Inn Select</b> (Business Traveller)	<b>Crown Plaza</b> (Leisure & Business Traveller)	<b>Inter-Continental</b> (Business & Leisure Traveller)
		<b>Holiday Inn SunSpree Resorts</b> (Leisure Traveller)	<b>Staybridge Suites</b> (Extended Stay)	
		<b>Holiday Inn</b> (Leisure & Business Traveller)		
		<b>Holiday Inn Family Suite Resorts</b> (Leisure Traveller)		

Lawson (1997: 21) in the same vein suggests two main categorising parameters. Firstly he uses *identification* of the hotels by their locations, standards of quality, operation as a chain or independently, and extent of specialisation.

**Table 5.4.3(c): Hotel Identification**

(Source: Lawson, 1997: 38)

Identified by	Examples	Characteristics
<b>Location</b>	City centre, Provincial town Resort, Country house Airport, Motel	Business travel, urban visitors Vacation and conference users Transient and staging needs
<b>Quality</b>	Official or voluntary grading systems denoted by 1 to 5 stars, crowns, diamonds, etc.  Company tiering or sub-branding of products to serve differentiated markets.	Standards of space, facilities and services appropriate for hotels of that grade  Budget, mid-markets and luxury hotels distinguished by brand names, specific design features and range of services offered
<b>Operation</b>	Large hotel companies operating as a chain or group of company-owned, managed or franchised properties  Individual hotels which may be fully independent or associated with a marketing consortium	Similar standards of quality, facilities and services. Branding is usually adopted to provide a recognizable and consistent product at a common national tariff  Emphasis is often placed on the distinctive character of the hotel and personal service
<b>Specialisation</b>	Hotels offering particular facilities and services, e.g.:  Resort hotels  Convention hotels  Spa hotels  Casino hotels	  Orientated around resort and leisure attractions  Including extensive facilities for meetings and conventions  Providing medical, paramedical, fitness and convalescence services  With gaming rooms, spectacular entertainment and public facilities

Secondly, Lawson (1997: 20) uses *size* as a parameter along which hotels are categorised (refer table 5.4.3(d)). *“The stock of hotel accommodation in most developed countries is characterised by a high proportion of small family-run hotels, inns and guesthouses. New hotels are generally in the mid- to large size range to justify commercial investment and group operation. The optimum for efficient staffing is usually round 200 rooms (120 rooms for budget / mid-tariff hotels) while larger units can provide savings in property operation and advantages in marketing. In prime locations (city centres, resort prominence) the high cost of site acquisition with usually dictate the minimum size and grade to achieve a viable cost/room ratio.”*

**Table 5.4.3(d) Characteristics of Various Sizes of Hotel**

(Source: Lawson, 1997: 23)

Size Range	Characteristics
Fewer than 25 rooms	Typical guesthouses, farmhouse and cottage conversions, small private hotels and traditional inns and lodges. Usually family run and individually owned. This form of small-scale dispersed tourism development is actively encouraged in many rural tourist areas
50 - 80 rooms	Includes the smaller independent hotels, country houses and luxury conversions of stately houses, Paradors (Spain). Hotels of this size are large enough to employ a separate manager and may be operated independently or as part of a company or marketing consortium
80 - 120 rooms	Most new budget hotels, inns, lodges and motels are in this size range providing standard rooms with an independent restaurant. Depending on location, the development may include a small outdoor swimming pool and children's play area
120 - 200 rooms	New provincial hotels in Europe tend to be in this size range. The number of rooms allows for better utilisation of space and facilities — which usually include some business meeting/private function rooms, a separate coffee shop and restaurant and health-fitness centre
150 - 250 rooms	Luxury hotels in resorts and spas. Hotels of this size can retain a personal service while offering a wide range of exclusive facilities (private beach, golf-course, speciality restaurants, remedial treatments)
200 - 300 rooms	Typical size for resort hotels supporting more extensive dining areas, lounges and recreational facilities. This size is also representative of mid-scale city centre hotels and many airport hotels
300 - 500 rooms	High-grade hotels in city centre, downtown and prime resort locations. Invariably these provide more than one restaurant, a health - fitness club including an indoor pool and extensive business facilities. This size is also necessary to support more extensive convention facilities
300 - 800 rooms	Most integrated resorts, holiday centres and club complexes have a large capacity to support extensive recreational and entertainment facilities and marketing costs
800 - 1000+ rooms	Mega city centre hotels where economies-of-scale can allow spectacular designs and cost savings in construction and operation. This includes the larger convention hotels and casino hotels

Lane and Dupre (1996) are of the opinion that perhaps the most important characteristic that separates one type of hotel from another is *price*. They further express that *location* and *specific type* are other important characteristics.

The various hotel categories are comprehensively summarised by Lane and Dupre (1996: 32) in the following:

#### Defined by Price

- Luxury/Upscale
- Boutique
- Upscale Commercial
- Midscale Commercial
- Budget/Economy

Location Specific

- Airport
- Motor Hotel/Motel
- Downtown
- Suburban
- Boatels

Defined by Room Configuration

- All-Suites
- Extended Stay
- Residential
- Capsule Hotels
- Bed & Breakfast
- Youth/Elder Hostel
- Private Clubs

Convention Related Conference Centres and Convention Flotels (Floating Hotels)

Lodging with Entertainment Components

- Casino Hotels
- Destination Resorts
- Mega Resorts
- Urban Resorts
- Resorts
- Theme Parks
- Spas
- Cruise Ships
- River Boats

In summary, as is evident from the various citations, hotels could be categorised in many segments within various parameters. Thus, hotel categorisation could be defined as a multi-dimensional process wherein different parameters are applied, resulting in a specific hotel having various category characteristics. Taking a small economy airport hotel as a case in point, which is defined by location, price and size.

## 5.4.4 Hotel Types

Various hotel types, as clarified in section 5.4.3, could be categorised by different parameters and in various segments. The following descriptions taken from Lawson (1997: 39), Baltin et al (1999: 22) and, Lane and Dupre (1996: 166) aim to elaborate and explain the different characteristics of specific types of hotels:

### 5.4.4.1 Convention Hotels

The downtown (city centre) convention hotel generally contains 400 to 500 rooms and considerable banquet and meeting space. In many cases, convention hotels are physically connected with or adjacent to large convention centres. They usually contain several food and beverage outlets in different styles and price ranges. Many also include substantial amounts of retail space.

Convention hotels also have large lobbies to handle the check-in and check-out functions that occur in a concentrated period at the beginning and end of every convention. It is common for up to 10 percent of the guestrooms to be suites. Guests use the living rooms of the suites as hospitality rooms, or the hotel turns them into meeting spaces for small groups. Wishing to overcome the perception that they cater solely for large groups, some convention hotels designate specific space for small group meetings or conferences.

In addition, many convention hotels have set aside concierge floors. For a premium price, these concierge floors typically offer controlled access, separate check-in and check-out areas, a lobby or lounge area, extra in-room amenities, complimentary daily newspapers, and continental breakfasts. Often, their concierge services are separate from the normal concierge services of the hotel.

Figure 5.4.4(a) provides a profile of the operating characteristics of convention hotels.

Descriptions of three representative convention hotels are:

- *New York Hilton*: This hotel contains 2042 rooms and suites, including 237 rooms and suites in the Tower (concierge section). It has 47 meeting rooms, the largest of which will seat nearly 3000 persons for banquets, and a separate exhibition space of approximately 7500 square metres.
- *The Sheraton Chicago Hotel and Tower*: This has 1200 guestrooms, of which 96 are in the Towers (concierge section). The hotel also includes 36 meeting rooms, the largest of which can accommodate more than 3000 persons for banquets, and a 3250 square metres exhibition hall. The facility also contains newsstands, gift shops, and business service centres.
- *Century Plaza Hotel and Tower*: Located in Los Angeles, this is a 750-room hotel with an additional 320 rooms provided in the adjacent Century Plaza Tower. The hotel has 16 meeting rooms, the largest of which will seat nearly 2000 for banquets, and a large shopping arcade. It is adjacent to a large and well-known shopping centre that offers numerous speciality shops and theatres. Hotel amenities include two heated outdoor pools, a whirlpool, and two fully equipped fitness centres.

**Table 5.4.4(a): USA Hotel Type Profiles, 1994**

(Source: Baltin et al, 1999: 25)

Average Size, Occupancy and Room Rates			
Hotel Type	Average Number of Rooms	Average Occupancy	Average Daily Room Rate (US\$)
Convention Hotel	1142	70.0%	\$ 103.86
Commercial Hotels	251	66.5%	\$ 68.66
Luxury Hotels	323	65.5%	\$ 196.62
Economy Hotels	108	65.5%	\$ 44.80
All-Suite Hotels	186	74.4%	\$ 74.87
Conference Centres	248	62.1%	\$ 79.33

Revenue Categories (Percentage of Revenue)						
Hotel Type	Rooms	Rental and Others	Food	Beverage	Telephone	Other Operated Departments
Convention Hotel	58.0%	1.8%	22.5%	5.9%	2.5%	9.3%
Commercial Hotels	61.5%	0.8%	25.7%	7.0%	2.6%	2.4%
Luxury Hotels	55.4%	3.1%	24.8%	7.1%	2.7%	6.9%
Economy Hotels	95.8%	0.7%	0.0%	0.0%	2.4%	1.1%
All-Suite Hotels	86.4%	1.2%	5.5%	1.6%	2.9%	2.4%
Conference Centres	42.9%	1.7%	30.3%	7.2%	1.8%	16.1%

Expense Categories (Percentage of Total Expenses)									
Hotel Type	Rooms	Food & Beverage	Telephone	Other Operational Depart	Maintenance	Energy	Marketing	Admin & General	Operating Profit *
Convention Hotel	17.3%	23.0%	1.4%	2.4%	5.9%	3.9%	6.9%	9.0%	30.2%
Commercial Hotels	16.3%	26.0%	1.6%	1.7%	5.2%	5.2%	8.6%	9.8%	25.6%
Luxury Hotels	17.2%	28.9%	1.8%	5.3%	5.9%	3.6%	6.9%	9.4%	21.1%
Economy Hotels	21.6%	0.0%	1.6%	0.5%	6.1%	5.9%	7.3%	9.2%	47.8%
All-Suite Hotels	22.3%	5.9%	1.4%	1.8%	5.1%	4.5%	9.8%	8.8%	40.4%
Conference Centres	10.1%	26.9%	1.8%	8.8%	5.2%	4.8%	7.9%	8.8%	26.3%

\* Profit Before Fixed Charges

#### 5.4.4.2 Commercial Hotels

Commercial hotels are generally considerably smaller. They offer from 100 to 500 guestrooms. While meetings may represent an important part of their business, the groups that are served generally are smaller than those using convention hotels. Compared to convention hotels, most commercial hotels provide less public space and a limited number of food and beverage outlets.

Figure 5.4.4(a) provides a profile of operating characteristics. Two examples of typical commercial hotels are the following:

- *Le Meridien Boston Hotel*: This hotel contains 326 guestrooms, including 22 suites. It has one formal restaurant open for lunch and dinner and a cafe that remains open throughout the day. In total it houses eight meeting rooms, the largest of which can seat 220 people for banquets. An indoor swimming pool and health club and a gift shop are the major amenities.
- *Holiday Inn Cincinnati North*: This hotel contains 408 guestrooms, six meeting rooms totalling approximately 500 square metres, a 140-seat restaurant, and a cocktail lounge

in a number of two- to four-storey structures. A recreation area offers an indoor swimming pool, whirlpools, and game rooms.

#### 5.4.4.3 Luxury Hotels

Luxury hotels tend to be located in large metropolitan areas, places visited frequently by persons who will pay a premium price of accommodation. Most have fewer than 300 rooms, and the few larger luxury hotels tend to cater more for corporate travellers and overseas visitors. High-quality furnishings, amenities and services distinguish these hotels. Many house superior restaurants, although this is not a requirement. Their high ratio of employees to guestrooms affects the economics of operations. Although luxury hotels may accommodate some meeting and banquet business, they do so generally only for very small groups.

As shown in figure 5.4.4(a), the operating profile for luxury hotels (defined as hotels achieving average rates for 1993 in excess of \$200) differs significantly from the profile for convention hotels. Two examples follow:

- *Four Seasons Hotel*: This New York City hotel with 367 rooms, including 58 suites, is atypical of most luxury facilities in that it occupies 52 floors. Guestroom amenities include mini-bars, two-line speakerphones, safes, terrycloth bathrobes, superior furnishings and 23 guestrooms/suites have terraces. Although the hotel has 13 meeting and function rooms, the largest measures only 150 square metres. A restaurant seating 64, a cocktail lounge seating 80, a fitness centre and spa, and a business centre are among the amenities.
- *Lowell Hotel*: By contrast, New York's Lowell Hotel contains only 90 rooms and 62 suites. Its restaurant, a leased facility, is a landmark New York steakhouse. The Lowell also has a small tearoom for guests. Each suite is elegantly appointed and contains an extensive array of amenities.

#### 5.4.4.4 Economy Hotels

Appearing at the lower end of the price segment spectrum (opposite luxury and 1<sup>st</sup> class) are the economy hotels, which go by many names, including budget, hard budget, limited service, and economy. They are a response to the emergence of more value conscious travellers in the late 1970s and 1980s. With inflation heating up, many businesses became concerned about travel expenditures and began to control them much more carefully. At the same time, while tourist travel expanded rapidly, much of the growth came from a more price-sensitive portion of the market.

The economy hotel offers limited services and average room rates significantly below prevailing market rates, typically 20 to 50 percent below the rates of full-service facilities in the same area. These facilities usually do not have restaurants or banquet space, recreational facilities, or many other amenities found in more traditional hotels.

The economy hotels were built along highways outside metropolitan areas, on relatively inexpensive land. They have since moved into suburban areas, airports, and, in some cases even city centres (downtowns). The original economy properties were one- and two-story structures with exterior corridors, consisting of 50 to 150 rooms. Motel 6 was the first budget hotel. It began operations in 1963 with, as the name implies, a room rate of \$6 a



night. Showers, but no bathtubs, were offered. Guests paid extra to use the television sets and telephones were not available in the guestrooms.

The economy segment has expanded greatly. In the USA during the 1970s, half a dozen chains operated fewer than 200 hotels. Today, more than 40 chains operate over 9200 budget properties. The segment has diversified as well, and now offers at least three separate tiers of product:

- *Upper Tier:* Hotels at the high end of the budget segment offer more upscale furnishings and decor, and generally charge rates much closer to market area averages. These hotels are generally larger, usually over 100 rooms. While the guestrooms are small, the level of quality is often much closer to that of commercial hotels.
- *Middle Tier:* Mid-economy hotels generally have 60 to 125 fully furnished rooms, and charge rates that are usually 25 to 40 percent below market. Their corridors can be either external or internal.
- *Lower Tier:* Economy hotels at the lower end have room rates that are about 50 percent below market. They generally have 50 to 125 sparsely fitted rooms (bare necessity amenities) and exterior corridors.

Economy properties operate at generally higher occupancy levels than do full-service hotels, and, as shown in table 5.4.4(a) achieve income ratios that are significantly higher. Their higher profits are the consequence of lower staff requirements and the lack of food and beverage facilities, which generally operate at fairly low profit margins.

#### **5.4.4.5 Boutique Hotel**

In an article by Jones Lang LaSalle (Focus on Boutique Hotels, 2000), the author explains that boutique hotels as we recognise them today, began appearing in the early 1980s. The popularity of boutique hotels can be traced to numerous factors. Firstly, the individualistic character of boutique hotels appealed to seasoned and sophisticated travellers who did not want to stay at “just another hotel.” Indeed, the pains which boutique hoteliers took to incorporate local elements into a property’s concept served as an antidote for cookie-cutter (repetitive and similar) hotel rooms. Secondly, while many boutique hotels today command top dollar because of their high profile and strong demand, boutique hotels in the early years were often frequented by value-conscious leisure and independent business travellers. Since the first boutique hotels did not have outlays for expensive meeting facilities and enjoyed savings by not paying for branding-related fees, they were able to pass along these savings to their guests.

The two preceding factors were instrumental to the entry of boutique hotels as a separate segment of the lodging industry. However, a third factor, the advent of the information technology age, is believed to be the most significant in terms of the continued success of the boutique hotel segment today. The latest shift in the consumer paradigm towards an Internet-based, multimedia-intensive, instant-access-to-information model has given rise to a culture that prizes innovation and distinct identity. By offering stylish, personality-orientated, customised amenities as well as an intimate, well thought out, technology-orientated product boutique hotels have become mainstream choices for travellers in the dot-com age. Our society has become focused on personalisation, from the way we order our hamburgers to the amenities in our car. The boutique hotel product rides the wave of the same trend.

Presently, a boutique hotel encompasses the following characteristics, among others: small, urban location, non-branded and showcasing stylish architecture and interior design. In addition to these traits, boutique hotels are notorious for having their own “personality” or “identity,” and for providing high levels of customised service and guest amenities. Such hotel properties surpass the now standard amenity set of toiletry kit, coffeemaker, hairdryer, iron and ironing board by providing whimsical offerings that might include companion gold-fish, pillow menus, compact disc libraries, compact disc players, stereos, complimentary cappuccino bars, ginseng sodas in the mini-bar and a Rubik’s Cube

#### **5.4.4.6 All-Suite Hotel**

All-suite hotels came into existence as a separate category in the 1970s. Their guest spaces are larger than normal (usually containing more than 45 square metres) and have a living area separate from the bedroom. Some all-suite facilities offer nearly full-size kitchen areas, some offer a small compact food preparation area (often called a pullman kitchen), and others offer no kitchen at all.

The all-suite hotel was developed to meet the needs of business travellers who spend a lot of time on the road and long stay guests like corporate personnel who are relocating or consultants who are on a project that will last some time. Many leisure travellers, especially families, also find these facilities desirable.

This product category varies widely from property to property. Still, all-suite hotels generally take one of three basic forms:

- *Urban:* Urban all-suite hotels are usually mid- to high-rise structures containing 200 to 300 suites, a size generally considered small enough to retain a residential atmosphere and large enough to provide the desired level of service.
- *Suburban:* Usually found in areas containing a concentration of office buildings, such as edge cities or built-up highway corridors. Suburban all-suite hotels generally have four to eight storeys.
- *Residential:* In contrast, residential all-suite hotels usually occupy two-storey structures. They resemble apartment complexes more closely than they resemble hotels. Their guest spaces are large, with separate living and sleeping areas, full kitchens, exterior entrances, and a variety of amenities. Residential all-suite facilities usually attract guests who stay longer and, because of the higher occupancies and smaller staffing needs, attributable to low guest turnover, they frequently are more profitable than regular hotels.

All-suite facilities have achieved occupancy levels well above average for the hotel industry. In most cases, they command significant rate premiums. Their operating profile is shown in table 5.4.4(a). Despite good performance, all-suite facilities constitute a relatively small proportion of the total number of rooms in the United States (approximately 4 percent).

#### **5.4.4.7 Airport Hotels**

Special situations arise near airports (and ferry-ports) where transfers are likely to require overnight or day accommodation. Other markets include aircrew and airport staff in addition to the needs of other tourism developments around the airport. Airport hotels also provide a convenient meeting place for international representatives and most offer extensive conference facilities.

Disadvantages may arise from the lack of character in the surroundings, height restrictions, noise disturbance and isolation from other amenities. To counter this, new airport hotels are increasingly designed with distinctive styling to serve as landmarks and may be in atrium form using impressions of light and transparency to contrast the restrictions of travel. In developing airports, hotels may be directly linked by walkways to the terminal buildings. For other locations, transport to and from the terminals must be provided but the hotel may offer extended parking.

#### **5.4.4.8 City Centre (Downtown) Hotels**

In Europe, city locations are the most prestigious locations and are usually limited and subject to stringent town planning controls. In these situations most hotel development arises from the conversion of other buildings and the refurbishment and complementary enlargement of existing hotels to maximise the advantages of their location and character.

Conversion and refurbishment generally applies to medium size hotels (150-350 guestrooms) offering a distinctive individual character and personal service. Plot ratio and height restrictions generally limit the construction of hotels to five to ten storeys but there are many notable exceptions.

Elsewhere, new city hotels tend to be large and impressive, featuring amongst the most prominent buildings in downtown districts. To gain advantages in marketing as well as economies of scale in high-rise construction, hotels commonly have 300-600 rooms and sometimes more.

With some reservations, for example reasons of safety, there are virtually no limitations on height. Many of the new urban hotels are over twenty-five storeys tall. The Westin Stamford in Raffles City, Singapore, at seventy-one storeys is the tallest hotel in Asia. The Peachtree Plaza in Atlanta (1200 rooms) is seventy storeys tall and at fifty-six storeys the Island Shangri-La (565 rooms) is the tallest hotel on Hong Kong Island.

Urban redevelopment programmes are usually done on a large scale to attract the levels of investment and appreciation of land and property values required for regeneration. Hotels often feature as part of comprehensive schemes, combined with office buildings, shopping malls, convention centres, exhibition and trade centres and serviced apartments. The hotel accommodation may occupy only upper floors as part of a vertical complex but must be served by exclusive elevators or escalators from a distinctive lobby or reception at street level. The main lobby providing front desk and lounge services may be located at the hotel floor levels. Separate goods and service access is required as well as appropriate control, temporary storage and transportation to the 'back-of-house' areas. In drawing up leasing arrangements for the building, the areas, equipment and engineering services provided for hotel use, need to be clearly defined.

#### 5.4.4.9 Suburban Hotels

Suburban hotels cater for diverse markets (transient, business, conference and local visitors). Normally, the lobbies and public areas need not be extensive unless there is a local market demand for quality restaurant and function rooms. Leisure facilities can provide a marketing advantage (particularly for weekend promotions) and may attract local club memberships.

The development of hotels in suburban areas has been accelerated by:

- High land costs and taxes affecting inner city and town development
- Development restrictions in sensitive city areas
- Traffic congestion in towns and trends towards more pedestrian traffic
- Decentralisation of offices and perimeter location of new industries.

Suburban developments generally permit more convenient access and parking, more space for amenity and leisure and larger room sizes without cost penalty. The hotel location may be advantageously associated with other new commercial properties, including business and research parks and institutions such as hospitals and universities, trade centres and airports.

Standard twin rooms are generally required with a proportion of alternative double bed studio rooms. Corridors may be off-centre to provide rooms in two sizes and specific blocks of ground floor rooms may be designed for easy conversion into syndicate rooms for business use. Car parking ratios of 1.25 spaces per room are usually provided.

New suburban hotels mostly fall into two tiers of standards:

- *Main company hotels*, with superior accommodation, conference facilities, business and leisure centres (including enclosed swimming pool and choice of restaurants).
- *Motor and courtyard-style hotels*, offering less sophistication with a simpler style of building. The facilities generally include one or more small meeting rooms, a fitness room and a café-restaurant open to non-residents.

Suburban developments also include:

- *Individual older hotels or converted houses*, usually set in their own grounds, which require refurbishment and / or appropriate extension.

#### 5.4.4.10 Resort Hotels

As mentioned before, the word “resort” is used widely and diversely and often means different things to different people. Owing to this confusion Schwanke (1997: 4) defined parameters by which a resort property or facility could be characterised:

- Resorts are real estate developments that have been developed and planned and are currently operated by a private business enterprise.
- Resorts offer proximity and easy access to significant natural, scenic, recreational, and/or cultural amenities that make them attractive places to visit.
- Resorts include lodging accommodation, timeshare ownerships, and/or residences used largely by tourists, vacationers, weekend travellers, seasonal residents, and/or owners or users of second homes.

Resorts can be categorised along three major dimensions: by their proximity to their primary markets, by their setting and primary amenities, and by their mix of residential and lodging products. Resorts can also be classified by their quality, pricing structure, and overall appeal to different income groups. Based on price segmentation there are budget resorts, mid-priced resorts, and luxury resorts as well as a host of products in between.

Resort hotels are by far the most common type of resort property. The accommodation in these facilities ranges from very modest facilities, such as tent cabins, to luxury resort suites with all the comforts of home and more.

The difference between a resort hotel and a traditional commercial hotel can be described in terms of the guests' purpose in staying at the facility. The guest at a resort hotel typically visits for relaxation or recreation, whereas the guest at the commercial hotel typically visits to satisfy a need for convenience. Increasingly, however, resort hotels are catering to commercial guests, especially conferencees during off-season periods, while traditional hotels are catering to leisure travellers, particularly during weekends and holiday periods. (Schwanke, 1997)

Resort hotels and other resort lodging facilities generally differ dramatically from most commercial hotels in terms of their setting and level of amenities. Whereas a typical commercial hotel is set on a fairly small site in a city centre or along a suburban highway, a resort hotel or lodge is often located on a fairly large site away from unrelated commercial activity and highways. Room accommodation in resort hotels is often carefully positioned within attractive settings, frequently offering exceptional views of and/or access to the natural surroundings.

Traditional hotel amenities are typically limited to an exercise room, a small pool, and the concierge's ability to arrange off-site activities. Resort hotels and lodges often include extensive on-site amenities, including large swimming pools, tennis courts, boating and water sport facilities, equestrian facilities, gardens and landscaped courtyards, golf courses, and a wide range of other amenities, including the hotel's own ski slopes. Golf, in particular accounts for the success of resorts in attracting business meetings, an increasingly important source of revenue. Resort hotels are often set within larger resort communities, allowing them to offer access to a range of amenities included in the community, such as beaches, parks, amusement facilities, retail services, etc.

Further to the above categorisation and explanation, Schwanke (1997: 8) broadly classifies resorts into two categories:

- *Resort Hotel*: They are large and often self-sufficient hotel properties that include major on-site amenities such as tennis courts, golf course (s), large swimming pools, retail operations, and numerous restaurants.
- *Other Resort Lodging Facilities*: These are smaller hotels that do not include major amenities but are located near off-site amenities and attractions.

Examples of different types of resort hotels, to name a few, are:

#### Beach Resort Hotels

Most resort hotels are based on the leisure attractions of water both as a visual setting and recreational amenity. The hotel sites may front beaches, lagoons or lakes directly or provide elevated views with convenient access to the waterfront activities. To protect the environment and other views, hotels may be integrated into the environment with appropriate landscaping, built into cliffs and amongst rocky outcrops to reduce the outline, or stepped down slopes screened by planted terraces or kept below the height of indigenous trees.

While the views and setting of the sea or lake are critical, much of the recreational activity is normally focused in the grounds of the hotel itself. The location and landscaping of swimming pools may be used to create an interest for rooms and restaurants separated from the beach. In larger hotels, compensatory views may be provided through the development of associated golf courses and other outdoor sporting interests.

Generally, beach resorts offer a range of attractions for family vacations, but high-grade hotels may specifically target markets seeking more sophisticated requirements.

#### Health Resort Hotels

Development of health resort hotels derives from the therapeutic benefits of local mineral springs and other related forms of treatment. Traditional spa resorts are well established, particularly in Europe and Japan, and have experienced a resurgence in demand arising from a combination of several factors, such as increasing concerns over stress, diet, health and fitness, ageing populations and, in some countries health insurance reimbursement of treatment costs.

Modern spa hotels cater for a variety of needs and include wide-ranging provision for individual and family recreation. In existing resorts many hotels have undergone extensive refurbishment installing the latest sophisticated equipment. New hotels may also be located in or near traditional spa towns or be individually developed to provide self-contained health and fitness centres.

Depending on location, spa hotels may place emphasis on intensive sport and fitness programmes, health and beauty rejuvenation, treatment of rheumatoid and other conditions, stress relief and body toning (relaxation and revitalisation), or dietary and weight loss regimes. Set programmes may extend over days, 1-2 weeks or longer. The quality and range of restaurant and lounge facilities are important. Although spa usage is mainly non-seasonal, provision should be made for special events, entertainment, competitions, exhibitions and festivals.

#### Rural Resort Hotels

Inland resort hotels are more difficult to market than those offering beach, lake or mountain attractions. Hotels in rural surroundings, isolated from business and local users, need to create their own individual amenities. In many cases extensive grounds for golf courses, tennis, equestrian and/or fishing will surround the property. More exotic sports may be

offered (hot air ballooning, war games, archery, river rafting, rock climbing) and professional instruction programmes included.

Country hotels are usually combined with club facilities for wider marketing, and invariably provide banquet halls, meeting rooms for executive conferences and functions. Indoor swimming pools, health and fitness facilities (including spa equipment), squash courts and tennis/badminton halls are usually included.

The quality standards of high-grade country hotels are similar to those for beach resorts. Many of the hotels are converted from historic buildings to provide unique character. Others may be integrated with the larger scale development of property for lease or sale under management agreements.

### Ski Resort Hotels

Ski resort hotels and mountain lodges are planned to serve the markets for winter sports. They are located in areas of high altitude having access to mountain slopes suitable for skiing. Most of the traditional resorts in Europe are found near original mountain villages at altitudes of 1200-1500 metres although some of the new resorts are at 1500-2000 metres. This higher altitude allows longer skiing seasons but being above the tree line, is less attractive for dual summer use. As a rule a minimum of four months' snow cover is necessary for national marketing. The potential of an area for skiing depends also on the gradients of the mountain slopes (average 25-35% with short sections up to 60%), the vertical drop for downhill ski slopes (1000-1500 metres for national standards), tree cover and terrain and orientation avoiding long exposure to sun (melting) and wind.

### Themed Resort Hotels

Themed resort hotels cover a wide range of developments, such as those:

- Associated with themed leisure parks, entertainment complexes (Euro-Disney)
- Offering specific attractions (Safari/Game Lodges, Desert Resort)
- Providing 'atmosphere' and experiences (historical/archaeological restorations).

In each case the hotel complex is designed to complement and extend the experience of the situation and emphasis is given to sensitive interpretation of the environmental setting. Where appropriate, historic and otherwise unique buildings and features may be incorporated into the development as a means of securing their conservation.

The range of facilities and standards of accommodation depends on the particular attraction and its market appeal. As an example, hotels associated with leisure parks cater for families, whilst safari lodges and ranches are designed for reasonably comfortable escapism.

### Casino Resorts Hotels

Specialist casino hotels tend to be concentrated into specific resorts (Reno, Las Vegas, Atlantic City, Sun City) or located in tourist destinations having access to large affluent markets such as the Caribbean. In addition to hotel residents (average stay four days) many resort hotels attract large numbers of day visitors.

Casino hotels in resort locations are generally large (500 rooms plus) with glittery signage and ornate interiors to create an air of excitement and fantasy. Most provide extensive amenities including multiple-choice restaurants and bars, health clubs, convention facilities and entertainment ranging from cabaret/piano bars to sophisticated nightclubs.

#### **5.4.4.11 Conference Centres**

While many hotels market themselves as conference centres, truly dedicated conference centres are designed to provide a setting free of distractions for executive and professional meetings. Usually located in rural areas or in suburban office communities near major metropolitan areas, they combine meeting and conference facilities with lodging in a way that can accommodate groups in a self-contained learning environment.

Conference centres usually contain 200 to 400 guestrooms and a large number of dedicated conference and meeting rooms. They provide a carefully designed and more or less isolated learning environment, with comfortable seating, suitable lighting, audiovisual equipment, conference support services, and living and recreational facilities to occupy the hours when conferences are not in session. The food offered is typically of a sufficient quality and variety to make leaving the facility even for an occasional meal, unnecessary. These centres offer recreational facilities that are more extensive than those in traditional hotels. In many, if not most cases, occupancy by transient guests is a relatively small part of the operations.

### **5.5 Hotel Grading and Standards**

The precise definition of what constitutes a hotel and conditions for hotel grading are set out in more than one hundred classification systems worldwide operated by governmental or representative agencies. National systems of classification vary both in the range of categories and method of designation (letters, figures, stars, crowns and other symbols) and may be compulsory or voluntary. (Lawson, 1997)

Since 1962 the World Tourism Organisation (WTO) has sought to develop a universally accepted hotel rating system. Similar proposals have been considered by the International Hotel Association (IHA). The Confederation of National Hotel and Restaurant Associations (HOTREC) of the European Union has devised an alternative system using symbols to represent the facilities without classification. In 1995 there were over 100 classification systems in operation, the majority based on the WTO model but customised to suit local conditions.

Cooper et al (1998: 326) says: *“In common with all areas of tourism, the accommodation sector in any one location is a product of local and global forces representing historical, political, economic, socio-cultural and technological factors. The interplay of these environmental determinants is the main cause of the sector’s heterogeneity. Comparison, therefore, becomes difficult between sub-sectors within accommodation and between operations in different countries and regions of the world.”*

There are few meaningful frameworks or criteria that can compare the physical product attributes and ambience of, for example, Ashford Castle in Ireland with its traditional focus and landed aristocracy, with the ultra-modern Ritz Carlton in Singapore situated in the heart of that urbanised city-state. Both offer excellence within their own location and context but their physical product is completely different.



There is a difference in focus between classification and grading (Cooper et al, 1996):

*“Classification may be defined as the assignment of hotels to a **categorical rating** according to type of property, facilities, and amenities offered. This is the traditional focus of most schemes.”*

*“Grading in contrast emphasises **quality dimensions**. In practice, most commercially operated accommodation operations concentrate on classification, with quality as an add-on which does not impact upon the star rating of an establishment.”*

The purposes of accommodation classification are varied, and include:

- Standardisation to establish a system of uniform service and product quality that helps to create an orderly travel market distribution system for buyers and sellers
- Marketing to advise travellers on the range and types of accommodation available within a destination as a means of promoting the destination and encouraging healthy competition in the market place
- Consumer protection to ensure that accommodation meets minimum standards of accommodation, facilities, and service within classification and grade definitions
- Revenue generation to provide revenue from licensing, the sale of guidebooks and so forth
- Control to provide a system for controlling general industry quality, and
- Investment incentive to give operators incentive to up-grade their facilities and services in order to meet grading/classification criteria.

Accommodation classification is not without problems. One major problem relates to the subjectivity of judgement involved in assessing many key aspects of both the tangible and intangible elements of the accommodation experience, such as personal service or the quality of products. Consequently many classification schemes concentrate primarily on the physical and quantifiable attributes of operations, determining level of grade on the basis of the following features (Lawson, 1997):

- Room size
- Room facilities, especially whether en-suite or not, and
- Availability of services, such as laundry, room service, 24-hour reception.

However, this is commonly done without any attempt to assess the quality of such provision or the consistency of its delivery. Other problems with classification schemes include:

- Political pressures to offer classification and grading towards the top end of the spectrum to most hotels, thus creating a top-heavy structure
- The cost of administering and operating a comprehensive classification assessment scheme, especially where subjective, intangible dimensions are to be included
- Industry objections to state-imposed compulsory schemes, and
- The tendency of classification schemes to encourage standardisation rather than individual excellence within hotels.

Lawson (1997: 5) states the grading systems fall broadly into the following two groups:

- Official classifications: Standards set by governmental agencies, usually the Ministry of Tourism or Regional Tourist Board. It could also be as a compulsory requirement for registration or licensing or as a voluntary scheme.
- Independent ratings: Hotels inspected and assessed by associations (such as hotel or automobile associations) or commercial bodies.

Grading criteria include:

- Local infrastructure: Fundamental requirements such as pure water supply, sanitation, ceramic tiles that are generally assumed, may need to be specified in developing countries.
- Overall quality: Some properties, whilst lacking certain amenities, may have outstanding features, such as its history, location or character.
- Factual basis: Tangible factors (space, facilities, amenities, services provided), and qualitative aspects (performance, personal service) that involve subjective judgements, tend to be more variable.
- Location and market needs: Guest requirements differ, country standards may differ, etc.
- Maintenance: Hotel quality depends on standards of cleanliness, upkeep and maintenance that can impair comfort and safety, but may be difficult to monitor.

***Refer to addendum 'A', for a comprehensive list of the 'Minimum Hotel Standards' as defined by the World Tourism Organisation.***

## **5.6 Hotel Property Ownership and Management**

Once the decision to develop a new (or acquire an existing) hotel has been made, selecting how the property is to be operated on a day-to day basis and who will carry out that function are two of the most important considerations for the developer, owner or asset manager. Ransley and Ingram (2000: 41) advise that the “...*operator selection decision should be based on a clear understanding of the investors' objectives, particularly in terms of their risk and reward expectation. This will determine the structure under which the property is to be operated and the key terms and conditions required to meet the investors' objectives. For example, if the hotel development manager (decision maker) is working for an owner-operator hotel organisation, the selection of the operator for the asset/property is likely to be limited to the brands owned by them (the owner-operator hotel organisation). Other types of investors, however, such as large financial institutions, may be seeking a low-risk, long-term investment that would require a very different structure from that required by an investor seeking a shorter-term capital gain but willing to accept some risk on their income profile.*”

Ownership and management of hotels reflect the growing complexity of business formats within the private sector generally. Over the last 40 years, hotel organisational mode(s) have become considerably diverse across regional and international markets. (Lashley & Morrison, 2000)

In light of the hotel operating modes' diversity, the views of Baltin et al (1999: 61), Cooper et al (1996: 316), Ingram and Ransley (2000: 37), Lane and Dupre (1996: 357), Lashley and Morrison (2000: 170) and Lawson (1996: 30) are combined to yield the following five principal structures under which a hotel property could be operated:

1. Owner and Operator
2. Lease Contract
3. Management Contracts
4. Franchises Contract
5. Consortia and Referral Groups.

Lashley and Morrison (2000: 171) briefly explain where the different hotel organisational models started. *“Modern, business format hotel franchising has its origins in America, where, in 1954, Holiday Inn launched its franchising system. However, the earliest example of any form of franchising in the hotel industry probably occurred in 1907, when Cesar Ritz granted permission for his name to be attached to hotels in New York, Boston, Montreal, Lisbon and Barcelona. Hotel organisations with established brand names and market reputations use franchising as a relatively low risk method to expand their chain system.*

*One distinctive feature of hotel franchises is the frequency with which these might be allied to a management contract arrangement. Indeed, the first hotel management contract granted by the Puerto Rican government to Conrad Hilton in 1948 also involved the property trading as the Caribe Hilton and thus it is also the first management contract / business format franchise arrangement. Here the owner contracts with the franchisor or a third party management firm to undertake the day-to-day operation of the franchised property. It is important to be aware of this situation as frequently those arrangements which are reported as management contracts also involve a franchise arrangement.”*

Fundamentally (Lashley & Morrison, 2000), the existence of business format franchising (and indeed, management contracting) is a recognition that capital intensive assets and knowledge-based assets can be separated. The franchisee undertakes the necessary investment in the capital assets (i.e. the hotel building, equipment, furnishing and fittings) and then enters into a franchise agreement to access the value-adding services of the franchisor. These take the form of a brand name and reputation which facilitates the market positioning of the property, plus additional services such as operating procedures and controls, marketing, and referral and reservation systems. In this way the franchise enables the hotel owner to enhance the return from the investment made in the capital assets. For the franchisor it is particularly attractive as a means of supporting international expansion where equity based strategies are frequently perceived as a high-risk foreign market entry mode.

The international hotel firm has a choice of organisational mode(s) it can use to support its growth and development. In addition to franchising they could choose another form of non-equity alliance, the management contract (which is often used in combination with a franchise arrangement). Both represent an alternative to equity-based arrangements such as full ownership (i.e. full equity) and partial ownership arrangements (i.e. joint ventures). The selection process as to which modal form provides the optimum choice requires consideration of both firm and country-specific factors. Of particular interest here are those factors which are conducive to supporting a franchising strategy.

Lawson (1997: 30) supports the view of Lashley and Morrison (2000), and explains that separating hotel property ownership from the trading business, enables the hotel company to expand at a faster rate and run more hotels than it could finance from its own resources. The acquisition of existing hotels may be funded in part by the purchase and simultaneous sale and leaseback of the property or site. The method of releasing capital assets (land, property, etc.) is also used to reduce the company borrowings and is particularly important in times of low growth in property values.

Although family-owned and individual hotels running on an independent basis comprise the global majority of units, there is a continuing move towards company-affiliated hotels. Small independent hotels are often under-capitalised, limited in scope for expansion and have difficulty in financing marketing and facility improvements. Whilst most family-run hotels are owned and operated on an individual basis, many company hotels have an increasingly complex ownership structure, as illustrated in table 5.6(a).

### 5.6.1 Hotel Owner-Operator

Under this structure the entity owning the asset also directly controls and manages the business. Until the 1950s, this was the most common structure in the hotel industry, and in Europe still remains the dominant structural form. However, in the increasingly competitive marketplace individual owner/operators are finding it more difficult to generate adequate returns on capital employed. One way owners are seeking to improve returns is through affiliation to a marketing consortium. This enables them to retain ownership of the asset and day-to-day control of the business, yet gives them access to a reservations system to generate greater revenue (Lane & Dupre, 1996).

When the owner chooses to manage a hotel property personally, it typically is called an **O and O**, which stands for **owned and operated**. Smaller properties are more typically O and Os than are larger properties.

**Table 5.6(a): Types of Hotel Ownership**

(Source: Lawson, 1997: 30)

Hotel Ownership / Operating Structures	Examples
Land Owner or Ground Lessor	Development of leasehold sites Sale and leaseback of freehold Joint venture schemes with landowner
Hotel Developer or Sub-Lessor	Development of property and sale to an institution, investment group or unit owner
Hotel Lessee	Leasing of property by hotel company or hotel investment group
Franchisee	Investment in franchised hotel property by an individual or company. Master franchise rights may be obtained for a country or region
Hotel Management or Operator	Operation by hotel management company under contract agreement

Typically the owner would hire a general manager and other key managers on an independent basis, meaning that they are not part of a management company. The relationship with each hired member would be that of employer and employee. This allows professionals to oversee the day-to-day operational decisions, but it is not the same kind of turnkey approach (where everything is taken care of) that a management company provides. In the employer/ employee scenario, owners still have important operational decisions to make, e.g. must keep close control over finances and must manage the strategic direction of the property.

The biggest advantage of being an owner-manager is complete freedom in running the operation. The self-managed property also saves the cost of the management fees that otherwise would be paid to the management companies. Owners with hotel experience or desiring to be entrepreneurs, are likely candidates for owner-managers (owner-operator).

### **5.6.2 Lease Contract**

With the lease contract operational mode, the physical hotel property is owned by one party, the owner, who receives rent from another party, the tenant. The tenant operates the business for a period of time in the expectation that the profits from the business will exceed the rent paid. The lease is normally long term (typically fifteen to twenty years plus tenants' options to extend) with the property owner receiving a fixed rent. This is usually subject to periodic review, sometimes to a pre-set criterion (for example, an inflation index) and sometimes to open market terms (which would usually require an industry expert to gather evidence and provide advice as to prevailing market rental levels for a property of that type in that location). This type of structure is preferred by institutional investors/owners (such as pension funds and insurance companies) as it provides a secure long-term return on their investment. However, the hotel business is cyclical making it difficult for a tenant to meet a fixed rental commitment in years when trading is poor and profits from the business are low. Nevertheless, this structure remains in use, especially in continental Europe where large institutions still dominate the property investment market. However, in recent years property owners have begun to understand better the cyclical nature of the hospitality industry and some now accept a turnover base rent subject to a minimum guarantee. This enables the property owner to maintain a secure income stream while benefiting from higher income in strong trading years. At the same time, the impact of a poor trading year on the tenant is partially offset by a lower rent.

### **5.6.3 Hotel Management Contract**

A hotel management contract is a term commonly used in the industry describing both the organisational mode and legal contract. The legal contract is an agreement entered into by the owner of a hotel property and an operator offering management expertise. The management contract as an organisational mode comes into existence when the owner/developer decides to hire an outside specialist manager to operate his/her existing or newly developed hotel. One of the leading experts on management contracts, James J. Eyster, defines the agreement this way: (Lane and Dupre, 1996)

*“A management contract is a written agreement between the owner and the operator of a hotel or motor inn, by which the owner employs the operator as an agent to assume full responsibility, operating and managing the property. As an agent, the operator pays, in the name of the owner, all operating expenses from the cash flow generated from the property, retains management fees, and remits the remaining cash flow, if any, to the owner. The*

*owner supplies the lodging property, including any land, building, furniture, fixtures, equipment, and working capital, and assumes full legal and financial responsibility for the property.”*

To start with, the hotel owner/developer should decide whether or not an independent hotel operator would be required. Should the owner/developer have little or no management experience, particularly if it is a larger property, a management contract would immediately introduce professional expertise to hotel. The advantages of hiring a management company include access to expertise and systems, and limits management problems for the owner in terms of the day-to-day operations. Another major advantage could be when the owner/developer is negotiating financing from a lender, a management contract with a reputable company may greatly improve the chances of obtaining financing.

Some of reasons for the fast growth of management contracts over the last 40-years are:

- **Increasing costs of land:** Because land has become more expensive, hotel companies rather enter into management contracts as opposed to property ownership.
- **The increasing costs of building construction and mortgage interest:** Ownership investment in large-size properties has become more prohibitive to hotel companies.
- **Hotel companies could manage more properties, more quickly, than they could own them.** It is quicker to only appoint and train a hotel’s management team than it is to buy an existing hotel and then appoint and train the management team. Hotel companies widened their investment base by increasing the number of guestrooms managed through rapid penetration of new markets, and improving earnings per share of stock.

Despite the economic recessions of the mid-1970s and the overbuilding of the 1980s, the lodging industry nevertheless has continued to favour the management contract as its preferred form of operating mode. This was especially true for new hotels/motels larger than 100 rooms, which were the more expensive properties to build. In the USA, by the late 1980s as many as 20 large chain operator companies (with nearly 700 properties under management contracts) and 60 smaller independent operator companies (with some 950 hotels and motor inns) were identified. By the mid 1990s the numbers grew even larger.

### 5.6.3.1 The Typical Management Contract

Because most management contracts agree on matters of concern to a specific property owner and a particular management company, it would be misleading to say that a generic management contract applies to the hotel industry. Practice and custom have established an industry provision norm, which is most likely to be included in most management contracts. Accordingly, Lane and Dupre (1996) caution against oversimplifying of what is a complex process for both owners and management companies in the hotel world.

Key contract provisions that a hotel owner, developer, manager or operator should be familiar with are explored briefly in the following:

#### Agreement and General Purposes

The owner and operator should be identified as parties to the agreement and state concisely their respective goals and expectations. Note that the terms operator, manager and management company can be used interchangeably.

### Operator's Duties and Authority of the Manager

This provision, sometimes referred to as the "owner's hands-off" provision, not only serves to prevent owner interference with the day-to-day management, but also specifies in detail the scope of managerial discretion and authority to be exercised exclusively by the operator/ manager as the sole agent of the owner.

### Annual Operating Budget

Customarily, a yearly budget is prepared by the operator, and submitted to the owner for his approval at least 60 days prior to the start of the fiscal year. A typical budget might include the following:

- An estimated profit and loss statement (income statement)
- Proposals for any expenditure for furnishings, revisions, rebuilding, replacements, additions or improvements
- Payroll and other operating expenses.

### Working Capital, Funding, and Banking

Working capital, the excess of current assets over current liabilities, is supplied by the owner. For example, the contract may state that the working capital amount may not be less than \$15,000. In essence, working capital is what the manager needs for the operation and maintenance of the hotel. It includes cash, marketable securities, notes receivable, accounts receivable, inventory, and prepaid expenses. All of these may be used for revenue producing activities, or acquiring fixed assets (such as new buildings) and for paying obligations (such as salaries and taxes).

### Management Fees

A management fee is the cost to the owner of using a management company to operate the property. This is a very important provision of the contract, for it spells out how the operator will be paid for services provided. Fees can be paid monthly, quarterly, annually, or at some other set interval. Management fees can be calculated in many different ways. The following presents some of the methods, which could also be used in combination:

- **A fixed fee:** This means that the management company will be paid the same fixed amount whether the hotel makes a profit or not.
- **A fixed fee plus a percentage of profit:** In this fee structure, the management company is paid a set amount, plus a percentage of the profits as an incentive.
- **A fixed fee or a percentage of profit, whichever is greater:** In this scenario, the percentage of profit amount would be what is paid to the operator if performance is strong, and the fixed fee is what is paid if performance is weak.
- **Pure profit and loss:** In this fee structure, the fate of the management company is tied completely to profits. If no profits are made, no management fee is paid. This is not a common fee structure.

### Accounting

According to this provision, the management will provide the owner with periodic accounting statements. These could be on a monthly, quarterly, or annual basis. These statements are necessary for the management team to maintain adequate operational control. In addition to the balance sheet, income statement, and statement of cash flows, specific management reports detailing ratios would be included.

### Term of Agreement and Termination Fees

The length of the contract term and any termination fees are of prime concern to both the owner and the management company. This section of the contract spells out the length of notice that is required should either party decide to terminate the agreement, as well as any termination fees. Typically, an owner wants the contract length to be as short as is mutually acceptable, and the operator wants it to be as long as is mutually acceptable. A shorter contract gives an owner greater flexibility. A longer contract gives an operator more security.

### Cost of Repairs, Replacements, Maintenance, and Capital Improvements

This provision requires the owner's prior approval of any expenditure that is not provided for in the annual budget and that is necessary to keep the property and equipment of the hotel in good operating condition. Most management contracts do identify what is included under the headings of repairs, maintenance, furniture, fixtures and equipment. Capital improvements involve any revisions, alterations or rebuilding of the hotel structure, the cost of which is not charged to normal repairs and maintenance. Such costs also require prior approval of the owner.

### Insurance

In most management contracts, either the owner provides or the operator purchases at the owner's expense, public and employer's liability, workmen's compensation, fire, property damage, business interruption and other such customary insurance as needed for the protection of the interests of the owner and/or operator.

### Real and Personal Property Taxes

Some contracts include the taxes that the management company must pay (that is property taxes, sales taxes, social security taxes, etc.). Other contracts do not include a tax provision, in which case the owner, not the management company would be responsible for paying the taxes.

### Damage, Destruction, or Condemnation of the Property

This type of provision provides that if all or part of the hotel is damaged or destroyed by fire, casualty or other cause, the owner will make repairs and/or replacements within a reasonable time period after the damage has occurred. If the owner fails to do so, the manager may typically terminate the contract, and the owner will pay the termination fee. The contract may also include government action, for example a contract may state that if all or part of a hotel is condemned by government action and as a result can no longer be operated in accordance with the manager's standards, the contract may be terminated with



payment of the termination fee to the manager. Remember that the management company often has an international reputation to uphold.

#### Default or Termination Rights

Many management contracts contain extensive provisions covering the variety of circumstances under which the owner and operator may terminate a contract. These provisions typically speak to:

- Default by the manager, and the consequent remedies available to the owner.
- Default by the owner, and the consequent remedies available to the manager.

In either case, default means failure to abide by any material part of the agreement. The prescribed remedy is contract termination and payment of fees and other sums of money due to either party. This provision was noted by members of the International Council of Hotel-Motel Management Companies as one of the two most compelling ones. The second was management fees. This is because when and how a contract might end, is very important to both parties.

#### Indemnity

Most management contracts indemnify the respective parties for various losses and liabilities that are specifically enumerated. Indemnify is another way of stating that a party is insured against loss or damage. Thus the owner is said to “hold harmless” the manager from certain losses while the manager likewise is said to “hold harmless” the owner from certain losses.

#### Transferability

This provision (customarily identified in most management contracts under the heading “successors and assigns”), refers to the owner’s right to sell, transfer, lease or sublease the hotel, subject to the manager’s right of first refusal. The right of first refusal means that the owner cannot sell or lease the property without the prior written consent of the manager.

#### Notices and Miscellaneous

This provision covers not only communications between the parties to the contract, but also other matters such as the following:

- Manager’s right to engage in competitive hotel operations elsewhere, provided such operations are not located within a certain distance, for example five kilometres from the owner’s hotel.
- If any provision of the existing management contract is determined to be legally invalid or unenforceable, the remainder of the contract shall continue in full force and effect
- Agreement that nothing in the existing contract shall be construed as making the owner and manager joint ventures or partners in the hotel operation.

### 5.6.3.2 Management Contract Comparative Analysis

In addition to reviewing the terms of a potential management contract, including the fee structure, an owner must evaluate the skill set of the management company itself. When comparing one management company to another, an owner should ask a set of questions that can lead to the best selection. Some of the key questions to ask in such an evaluation are:

- Does the management company have a successful track record and a reputation that can be trusted?
- Does the company have experience with properties of similar type and size, and in the same market conditions?
- Does the management company have any experience operating other types of franchises?
- Does the operating company have a proven ability to generate profit?
- Will the operating company be responsive to your goals and objectives?
- Can the company deliver marketing and sales expertise to generate revenues?
- Do you have confidence that you will receive timely and meaningful reports from the management company?

### 5.6.3.3 Hotel Management Contract Trends

In the world of hotel management contracts, two parties have always sat on opposite sides of the bargaining table. Both parties work together to profit from the revenues derived from the real estate asset; the owner, at the one end, in addition to taking the financial risk of building or acquiring a hotel, offers a fee to the manager, who sits at the other end and supplies operational expertise and manages the business. (De la Cruz, 2000)

De la Cruz (2000: ?) further says: *“Of course, virtually no industry expert today believes the hotel business can be simplified to such a degree. The days of Hilton, Hyatt or Marriott managing only for a fee and being left alone by the owner for 20 years at a time are long past. Management-for-fee deals, for the most part, have been replaced by complex incentive structures. Contracts have been thickened by stipulations yet shortened in duration. Owners no longer take all of the financial risk; management companies are expected to take some equity in the properties they manage.”*

Hotel management specialists have had to contend with and adapt to recent broad market trends, such as brand consolidation, shifts in the hotel owner base because of the emergence of real estate investment trusts (REITs), the virtual evaporation of capital in North America and the lodging market booms and busts, respectively, in Europe and Asia. All of these have resulted with each passing quarter, in a constantly shifting environment in which management contracts are crafted.

Regardless of these external forces, it is the contract itself that remains the central issue for owners and managers. *“Bill Marriott, chairman of Washington-based Marriott International, the world’s largest hotel management company with a portfolio of 759 managed properties, says contracts have evolved to the point where there is a much greater sense of partnership between owners and managers. Most management companies work on incentive fees, where their compensation varies in accordance with the performance of the hotel’s bottom line. Marriott said: ‘We have to work harder to make money for the owners, and they work harder to make us work for them’ ”* (De la Cruz, 2000:?).

Jones Lang LaSalle Hotels (Management Agreement Trends Worldwide, 2001) reported that the global hotel management trend is fundamentally shifting towards providing a better balance of risk and reward. Attempts have been made to align operator and owner's interests through the increased use of sliding incentive fees and performance clauses. The new balance of risk and reward in management agreements is likely to further open the hotel investment market to institutional investors, who have been absent as significant owners for most of the nineties in many countries.

On a regional basis, the following trends were noted (Management Agreement Trends Worldwide, 2001):

- Operators in the Asia Pacific region are subject to the most competitive pressures when negotiating management agreements followed by American operators.
- The initial term of management agreements on average has decreased over the period, except in Europe, where it has increased.
- The granting of options to renew the term of management agreements is common, but the term of the option is decreasing. Whereas once the operators tended to have the sole right to exercise options, there is a trend towards owners having the right.
- Operator fees tended to increase over the last three years. This trend has applied to both base and incentive fees in all regions other than Asia Pacific. Whilst many agreements still utilise a fixed percentage of Gross Operating Profit (GOP) as an incentive fee, increasingly there are variations on this formulae, such as sliding scales, which provide greater returns to the operator as the hotel improves its performance.
- To provide greater flexibility and the possibility to enhance the asset's value on sale, there is an increasing trend towards providing termination without cause and the right to terminate the agreement on sale of the property. In most cases, these provisions are available only with a compensation payment made to the operator.
- There is a strong trend towards financial performance criteria, with failure to achieve a specified benchmark resulting in an opportunity for termination of the management agreement.
- The majority of management agreements provide for a specific FF&E contribution and, although more Asia Pacific contracts provide for a FF&E reserve, they generally require a lower contribution.

#### **5.6.4 Hotel Franchising**

The franchising decision is independent from whether or not a hotel owner/developer agrees to enter into a management contract. For example, suppose you have selected Richfield Management as your management company, you could in addition consider a franchise with agreement with Hyatt Hotels. It is common that the same operating company offers a hotel owner both a management contract and a franchise, for instance, entering into a management contract with Marriott and a franchise with Marriott. These should still be thought of as two very different kinds of agreements, providing two very different kinds of services, even though the legal paperwork may be combined. It is possible, and happens, for example that Westin Hotels could manage a Hilton Hotels franchise. (Lane & Dupre, 1996)

If you choose to enter into a franchise agreement, as the owner of the hotel, you would be the franchisee. The parent company from which you would obtain the rights of the franchise, such as Marriott or Hilton, is the franchisor. The agreement between the

franchisee and the franchisor is known as a franchise agreement. Franchising is a business opportunity, in which a franchisor grants the rights, trademarks, and service ideas to a franchisee, for local distribution or the hotel service. In return, the franchisor receives a payment or royalty. Note that the franchise agreement does not provide the day-to-day management services that a management contract does. A separate management contract is necessary to ensure those provisions.

What does franchising offer when the owner of the hotel enters into a franchise agreement with Four Seasons Hotels, for example? Four Seasons, as the franchisor, would grant the hotel property the right to bear the Four Seasons name, to use its logos and trademarks, to put up a Four Seasons sign, and to have the property listed in the Four Seasons reservations system. The entire business concept of Four Seasons, the marketing strategy, operating manuals and standards, quality controls and continued assistance and guidance would become the hotel's to use in exchange for paying Four Seasons a franchise fee.

Hotel owners should be aware, when entering into a franchise agreement, that one redeems a large amount of operational and management independence, because entering into a franchise agreement means meeting the specifications set out by the franchisor, not one's own. There are also costs associated with a franchise agreement that must be weighed against the benefits.

These franchise affiliations are, as commonly referred to, 'flags' that provide a brand name, a supporting reservation system, and other services to hotel owners. Since the early 1980s most hotels have been developed with a specific franchise or group of similar franchises in mind. Even if a hotel is built as an independent or is currently 'unflagged', the developer will probably replicate a successful franchise property which he / she have encountered or visited.

It is important to note that each new hotel developed subject to a franchise affiliation, is normally built following specific construction and design standards. The franchise agreement signed by a hotel developer often gives the franchisor the right to review and approve building design and construction. The franchisor may go so far as to reserve the right to approve the franchisee's architect and general contractor. As a result, most hotel franchisors' products are similar in terms of construction quality, facilities, layout, furnishings and design.

Consider the following advantages and disadvantages for the franchisee, or similarly for the franchisor (Lane & Dupre, 1996):

#### **5.6.4.1 Franchisee Advantages**

- The franchisee enjoys the benefit of an established product or service having consumer acceptance and therefore does not need to contribute to traditional start-up costs such as developing a market presence. Franchisor companies such as Sheraton Hotels, Hilton Hotels and Holiday Inns spend a sizeable portion of their advertising budget on national campaigns to keep the public aware of their hotels. These costs are charged to and recovered from the franchisees as an advertising fee based on the gross revenues of a franchised unit. The brand name recognition, or the fact that customers have heard of the chain and have an image associated with the chain, is a key advantage to the franchisee. Moreover, a franchisee saves time, effort, and expense that would have been

required in building a reputation, if the hotel is an individual (non-franchised) property, thus enabling his franchise unit to maintain its competitive edge.

- A second advantage to the franchisee is the availability of managerial and technical assistance provided by the franchisor. Depending on the policy of a specific franchisor, the range of assistance available may, or may not, include managerial training, site selection, layout and design, furniture, fixtures and equipment purchasing, inventory control and promotional plans for the grand opening.
- Another advantage to the franchisee is the franchisor's ignorance of quality control standards. This is important not only to assure a consistent customer image but also to maintain employee pride in the workplace.
- In many instances, franchisees benefit financially from the franchisor's advice and guidance on inventory management, thus avoiding waste and spoilage of perishables, and unprofitable storage of low demand items. Franchisees also benefit from purchasing economies of scale, as the chain as a single unit, can negotiate better rates for commodities such as soap and towels, as well as credit card fees and phone charges.
- Carefully designed procedures of a franchised system minimise the financial risks for the franchisee and therefore tend to increase, but not to guarantee, the likelihood of generous franchise earnings.
- Substantial business is often referred to individual hotels via a central reservations system and chain directories, the cost of which is shared by all units in the chain. This makes the marketing budgets of individual units go much further.

#### **5.6.4.2 Franchisee Disadvantages**

- Apart from substantial franchise fees and regular royalties from franchisees, the initial upfront financial obligation when entering into a franchise agreement could also be large. Regular payment of fees also consumes profits that a hotel could make as an independent property.
- Franchisees may be required to provide certain additional amenities and facilities such as swimming pools and/or 24-hour front desk service, in order to comply with the franchisor's standards. These and other service costs borne by a franchisee may ultimately be higher than expected, hence may severely diminish the franchisee's expectations of a satisfactory return on the investment.
- Territorial rights of the franchisor may overlap those of a franchisee, and limit the revenue that the franchisee might otherwise expect to realise. Many of the larger hotel chains, for example, previously granted franchises that prohibited the franchisor from making any other franchise agreements within a specified geographical area. This was designed to protect a franchisee from having the franchisor grant another franchisee the right to operate another unit in the immediate neighbourhood. In recent years, however, segmentation of hotel markets has resulted in the creation of different hotel brands with separate corporate identities. When such new brands have granted franchises, they have often disregarded the territorial restrictions agreed to by the parent company and its franchisees. Thus, such original franchisees are hurt by competition from another franchisee, in essence from the same company, being permitted to locate within territory originally designated exclusively for the parent company franchisee.
- With respect to a franchisee's desire to transfer or terminate the franchise, these actions are generally covered by the terms of the agreement. An uncooperative franchisor may withhold approval of such a transaction if for any reason the franchisor believes the franchisee to have violated any provision of the franchise agreement.

#### **5.6.4.3 Franchisor Advantages**

- Franchising is a vehicle to growth for a franchise organisation and its members have a vested ownership interest. Franchisors regard business expansion through a franchising network as the most attractive means of achieving rapid growth without the necessity of having to inject large sums of their own money or of incurring substantial debt through borrowing from financing companies. Thus, the franchisee's investment in a particular franchise enables the franchisor to share the heavy burden of a rapidly growing hotel or restaurant empire, while at the same time allowing the franchisor valuable time for evaluating market opportunities in a wide variety of competitive environments.
- Some franchisors are adamant that a large company relocated manager may be less enthusiastic, compared to managers of franchised hotels. Franchised hotel managers are usually residents of the local community. The personal investment of the franchisee-manager motivates him to work hard in pursuit of financial success.

#### **5.6.4.4 Franchisor Disadvantages**

- The idea of using the franchisee's money to keep a franchisor's business expansion plan afloat is not without its drawbacks. In the first place, overseeing a quickly expanding chain of hotel franchisees is always a formidable challenge. If less desirable franchisees are allowed to enter the system, it reflects badly on the whole organisation.
- In addition, there can be no guarantee that a franchisee will not discover that he/she would be able to do just as well (if not better) by operating the business without the franchisor. After the franchise agreement expires, the franchisee may not renew the agreement.
- Though the supply of prospective franchisee applicants may appear to be inexhaustible, some franchisors report a dearth of applicants whose experience, financial backing, and motivational drive are sufficiently persuasive to warrant taking a chance on their ability to become successful franchise operators.

#### **5.6.4.5 Typical Franchise Agreement**

The components of a franchise agreement are directly related to the kinds of fees that are charged. In exchange for each type of fee, the franchisor agrees to provide certain benefits. The various types of fees are made up of the initial costs, which are covered in a one-time fee, and a series of ongoing fees that are paid as long as the agreement is in place. These ongoing fees include a royalty fee, advertising or marketing fees, reservations fees, training fees, frequent traveller program fees and other miscellaneous fees.

##### Initial Fee

The initial cost or initial fee is only paid once, i.e. at the commencement of the franchise agreement. The initial fee for a hotel franchise is typically a fixed amount plus an additional charge depending on the number of rooms within a hotel. The fee is submitted with the application for the franchise. In exchange for the fee, the franchisee receives a review of the application, a site review, evaluation of the construction plans and visits during construction. Initial costs may also be incurred for signage and computer software and hardware necessary to interface with the organisation. If any application for a franchise is denied, the initial fee is returned in total, less a 5 to 10 percent for review costs.

If it is an existing hotel applying to be a franchisee, or is changing from previous to a new franchise, the property is known as a conversion.

### Continuing Fees

The balance of the fees is known as continuing or ongoing fees, and consists of the following:

**Royalty Fee:** A royalty fee is the fee paid as compensation for the use of the chain's name, trademarks, logos and goodwill. This fee is calculated to generate a profit for the franchisor. Royalty fees are generally calculated as a percentage of rooms' revenue and range from approximately 3 percent to 6 percent.

**Advertising or Marketing Fee:** The franchisor collects the marketing fees from all franchisees to use for various kinds of regional, national or international advertising that benefit multiple members, and also includes the costs for publication and distribution of a chain directory. This fee is either calculated as a percentage of rooms revenue (ranging from approximately 1 to 3 percent), or a fixed amount per available room. The income generated from this fee is used for specific purposes and does not generate a profit for the franchisor. In general, the same is true for the balance of the fees listed.

**Reservations Fee:** The reservations fee is used to support the costs associated with the operation of the central reservation system. These include office expenses, telephone and computer expenses, and the salaries of reservations personnel. As with the marketing fees, the fees generated for reservations are applied directly to the specified use and do not generate profits for the franchisor. The reservations fees may be calculated the same way as marketing fees, a fixed percentage of rooms revenue or based on a fixed cost for each reservation sent through the central system. If the fee is calculated as a fixed cost, it would then typically be \$4 to \$6 per reservation in the USA.

**Frequent Traveller Fees:** For franchisors maintaining a frequent guest program, a fee is assessed to cover the costs of administering the process. This fee is based upon the benefit generated to a specific hotel by its frequent guests. It is calculated as a percentage of what each guest spends (ranging from approximately 5 to 7 percent), or as a fixed amount per room occupied. On a fixed basis, the amount is typically \$3 to \$10 per guestroom in the USA.

**Other Miscellaneous Fees:** Sometimes a franchisor offers other specific services and products for a fee. These services could include training programs, assistance in purchasing, computer equipment rentals, or assistance in opening a property. These fees are designed to cover the costs of the services provided and generally represent minimal profit (if any).

A practical example of a franchise agreement is that of Sleep Inns, a brand of Choice Hotels. This franchisor, which is an economy chain, charges five types of fees (Lane & Dupre, 1996: 370):

1. **Initial Fees:** (One time only) \$300 per room or \$40 000 minimum payable upon application.
2. **Royalty:** A monthly assessment of 4% of gross room revenue.
3. **Marketing:** A monthly assessment of 1.3% of gross room revenue, plus \$0.28 per room per day.

4. **Reservations:** A monthly assessment of 1.75 % of gross room revenues. This includes software support and communication fees.
5. **Other:** A nominal fee for pre-opening materials and training services package, invoiced 60 to 90 days prior to system entry. There are also support charges for signs and reservation send/receive terminals, which may be purchased or leased.

#### 5.6.4.6 Franchise Comparative Analysis

The owner of a hotel is left with the question of whether to enter into a franchise agreement or not, based on the advantages and disadvantages as well as the costs associated with the benefits. If the owner does decide to enter into a franchise agreement, he/she should first determine the kind of franchise more appropriate for the specific hotel. If it is a first-class hotel with extensive amenities and facilities it will be inappropriate to join a budget chain. Following the category selection, a fee comparison between different franchisors in the appropriate category should be performed, as exhibited in table 5.6.4.7 (a) for first-class or upscale hotels.

Finally, a hotel owner should also decide if the operating philosophy (strategic context) of the franchisor is compatible with the subject hotel's. The following is a list of considerations, before deciding on a franchisor:

- Since risk is inevitably involved in any form of investment, a potential franchisee needs to evaluate not only the franchisor's performance record but also his/her own personal experience, business skills, and aptitude for successful franchise operation. In other words, a thorough self-evaluation is important before undertaking the risk of investing in a franchise.
- Undertake comparison-shopping of other franchisees in the same or related line of business to obtain their comments on the downside as well as the upside of their franchise experience.
- Study very carefully the initial package of information that you receive from the prospective franchisor and compare the terms with those of other franchisors.
- Before signing a franchise agreement, obtain competent legal advice as to:
  - what you are legally bound to do or not do under the franchise contract,
  - what requirements of federal, state or local laws you must observe,
  - what personal liabilities you are obligated to meet, e.g. financial, tax, or licence liabilities.

#### 5.6.4.7 Franchise Trends

The best franchise companies no longer limit their activities to neat advertising slogans, a good-looking logo for signage, and a reservations system. Swig (2001) explains that the best franchisors provide multi-tasking tools to provide dynamic support for any hotel operator.

Some might argue that there are too many franchise companies, as consumers are seemingly hard pressed to keep up with all of the brand names and products. Between the common varieties of limited service, mid-scale with or without food and beverage, plus the all-suite categories both extended stay and otherwise, there is certainly opportunity for consumer confusion.



Positioning and geographic coverage are still critical elements in choosing a franchise company. A brand's positioning and product offerings should also fit the target demand generators of an owner's site.

Traditionally, an owner joined a franchise organisation for the following business reasons:

- Reservations system.
- Promotional services.
- Assistance in development planning and opening.
- Operational aids, including manuals, job descriptions and quality assurance.

These and other basics are the same today, except that the franchise companies have taken these elements and expanded their availability and effectiveness. Technology will play a dominant role in current and future franchise changes.

Where technology ten years ago was focused on evolving property management systems and global distribution systems (GDS), today's purchasing is done on the internet, training is completed via CD ROM, and data is collected and collated to be shifted over data lines connecting franchisee, management company, and the individual hotel unit.

Current property management systems now include yield management tools, guest history databases, two-way interfaces to central reservations and accounting programs rendering the "night audit" process practically obsolete.

The process of product distribution is also changing radically. Although reservations over the internet are still below 3% of total bookings, internet requests for information may be impacting as many as 20% of hotel stays. Brands must have web friendly programs and a website available through any portal and any internet service provider plus links from city, state, region, or destination locator. Brands, which have not gone beyond a GDS and telephone reservations format, are in the distribution dark ages.

Even with the new technological distribution revolution, the same basic brand strength qualification criteria still exist:

- Percentage of room night contribution
- Strengths in specific market segments, e.g. business versus leisure, travel agents versus direct consumers
- Database and market research capabilities
- Yield management capabilities
- Mirror image inventory or inventory update capability
- Frequent Guest Program.

**Table 5.6.4.7(a): Summary of Chain Franchise Fees for First-Class Hotels (United States of America, 1994)**

(Source: Lane &amp; Dupre, 1996: 371)

Chain Name	Total Royalty Costs (US\$)	Total Other Cost* (US\$)	1994 Total 10-Year Cost (US\$)	1994 Cost as a % of Total Room Revenue
Clarion	2,866,409	2,736,661	5,603,073	5.8
Doubletree	2,880,814	3,390,949	6,271,763	6.5
Doubletree Club	2,880,814	3,450,949	6,331,763	6.6
Doubletree Suites	2,880,814	3,390,949	6,271,763	6.5
Embassy Suites	3,814,085	3,630,983	7,472,068	7.8
Guest Quarters Suites	2,880,814	3,390,949	6,271,763	6.5
Hawthorne Suites	3,841,085	2,520,678	6,361,763	6.6
Hilton Garden Inn	4,801,356	3,520,103	8,321,459	8.7
Hilton Inn	4,801,356	3,559,832	7,361,188	7.7
Hilton Suites	4,801,356	3,520,103	8,321,459	8.7
Holiday Inn Crowne Plaza	4,801,356	3,741,174	8,542,530	8.9
Homewood Suites	3,841,085	3,984,785	7,825,870	8.1
Marriott	7,487,115	2,024,553	9,511,667	9.9
Omni	2,880,814	3,410,949	6,291,763	6.6
Preferred Hotels**	390,000	1,040,235	1,430,235	1.5
Radisson	3,841,085	4,754,852	8,595,937	9.0
Residence Inn	4,622,359	2,997,377	7,619,736	7.9
Sheraton Inn	4,801,356	2,890,258	7,691,614	8.0
Sheraton Suites	5,761,627	2,792,599	8,554,226	8.9
Westin	4,801,356	3,644,306	8,445,662	8.8

\* Total Other Cost includes initial costs, and costs for reservations, marketing, frequent traveller programs, and miscellaneous.

\*\* Preferred Hotels is an affiliation. Note dramatic difference relative to chains.

Calculation Assumptions for Chain Franchise Fees for First-Class Hotels: Table 5.6.3.6 (a)	
Number of Rooms	300 Rooms
Average Room Rate (Year One)	\$ 95.00
Room Rate Growth	5% per year
Occupancy:	
Year 1	60%
Year2	70%
Year 3 to10	75%
Projection Period:	10 years
Total Room Nights	799,350
Total Rooms Revenue During 10-year Projection Period:	\$96,027,117
Total Food and Beverage Revenue During 10-year Projection Period:	\$57,616,270
Number of Reservations from Franchisor:	15% of occupied rooms
Percentage of Rooms Occupied by Frequent Travellers	8% of occupied rooms
Percentage of Rooms Occupied by Third Party Reservation Travellers	5% of occupied rooms
Average Length of Stay	Two nights

The more advanced questions relate to internet marketing opportunities with the links to online travel agents or alternative distribution channels. Additionally, GDS marketing tactics, which utilise various advertising or hotel screen positioning activities and inventory presentation through inside availability, are also now critical competitive components.

Marketing has become more technologically targeted through improved information gathering, the use of GDS, and internet messaging. Data can now be requested and delivered instantaneously, which makes program implementation far more efficient and effective with better reaction time and relatively instant impact.

### **5.6.5 Hotel Consortia and Referral Groups**

Lane and Dupre (1996) say, an alternative affiliation approach a hotel owner has, in contrast to being an owner-operator, leasing, management contract or franchising, is a referral group or a consortium. This type of affiliation offers many of the same advantages as a franchise, but typically is less expensive and less restrictive. Because of reduced cost, reduced restrictions and effortlessness to terminate an affiliation, the agreements are much less complex in nature than franchise agreements or management contracts.

*“The key distinction between a member of an affiliation and a member of a franchise is in how the hotel property is named. All members of a chain of hotels with franchised units will have the same name, such as Radisson Hotels or Four Seasons Hotels. On the other hand, all members of Best Western Hotels, which is the largest and best-known referral group, will have an unique/independent name, such as Pacific Inn and Conference Centre in White Hock, British Columbia, Canada. The Best Western logo will be prominently displayed next to the hotel’s unique name.*

*Referral groups typically group together properties that share common attributes and meet minimum criteria. For example, Relais Hotels, whose properties are primarily in Europe is a group of relatively small properties (less than 100 rooms). These hotels typically come with old-world charm, often formerly having been castles, convents and other historic sites” (Lane and Dupre, 1996: 373).*

Unlike franchises, referral groups are structured as non-profit associations. They aim to match the fee income to the expenses incurred in providing benefits for members. The governance of the referral group rests primarily in the hands of its members, although it employs full-time employees in a central office.

The duration (term) obligation as a member of a referral group is much shorter than that for a franchise agreement. Typically the relationship lasts for one year and is renewed on an annual basis. Furthermore, there are typically no penalty fees if you decide to leave the group.

Consortia or referral groups are appropriate for owners who want to maintain the hotel’s unique name and a great degree of independence in management. Such hotel owners would find the advantages of consortia and referral groups quite attractive, offering a central reservations system, national or international advertising coverage, purchasing economies, no franchise fees and no long-term commitment required.

#### **5.6.5.1 Typical Affiliation Agreement**

An affiliation agreement, similar to franchising, contains rules and regulations that regulate the members. Typically regulations will cover the following topics (Lane & Dupre: 1996):

- Governance of the organisation
- Signs and advertising

- Use of the reservations system
- Membership duration and fees associated
- Appearance of the lobby and front office
- Guestrooms and bathrooms
- Maintenance of buildings, grounds and public areas
- Use of logo items
- Violations and sanctions, should a member not perform according to regulations
- Procedures for terminating membership.

Though the properties in an affiliation may look physically very different, all member hotels within a particular country or group of countries are bound to the same standards. The aim is that all of the properties in a consortia or referral group should have the same minimum quality standards.

The fee payments required by consortia and referral group consist of an initial fee and ongoing fees. Best Western, as an example, charges the following types of fees (Lane & Dupre, 1996: 375):

#### Entrance Fee (One time fee, with application)

An **affiliation fee** starting at a minimum of \$20,000 (20 rooms or less) is payable, and an additional \$100 for each additional room thereafter. Also an **evaluation fee** of \$4,000 (non-refundable) is payable.

#### Annual Dues

A **base fee** of \$1,163.00 for 20 rooms, plus an additional \$39.10 per room for 21 to 50 rooms, which reduces to \$15.20 per room for 51 to 400 rooms is payable.

#### Membership Fee

A **membership fee** of \$0.72 per room per day for the first 25 rooms, plus, \$0.67 per room per day for 26 to 50 rooms is payable. A reduced fee of \$0.60 per room per day is paid for 51 to 100 rooms.

#### Reservation Fee

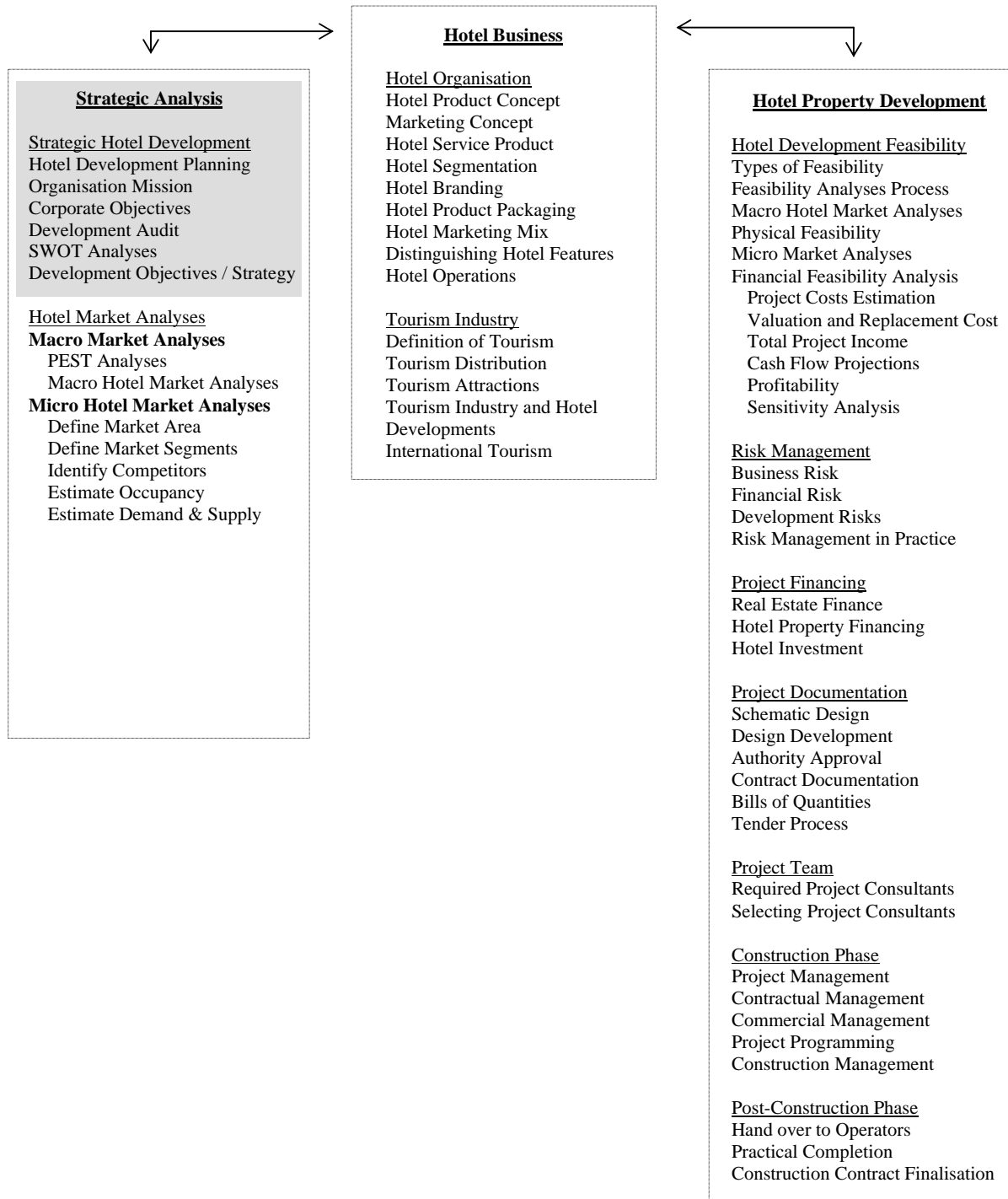
For the first 12 months after reservation activation, a new property will be charged \$0.33 per room per day as a reservation fee. After 12 months, the reservation fee is based on the number of rooms booked through the reservations system.

#### Special Assessment Fee

A special assessment fee is charged for the analysis and investigation of a specific project, e.g. a special investigation into a new reservation system for the affiliation group.

**Chapter 6:**

**Strategic Hotel Development Planning**



## **6 Strategic Hotel Development**

At the outset, the rationale behind the inclusion of this section called Strategic Hotel Development needs to be explained.

Hotel organisations quite often have an in-house development division, managing future hotel expansion and other development related issues such as franchising, market segmentation, management contracts, market valuations, identifying market expansion, to name a few. For these employees or consultants dedicating their daily effort to hotel development, it is imperative to understand the strategic context of the subject organisation.

In addition to an in-house hotel development division, many property developers either specialise in hotel property development or would at least consider developing a hotel at some stage in their endeavours. Hence the strategic characteristics of possible hotel operators need to be understood, before a developer considers targeting a specific hotel market or type of hotel development. For these and many more reasons as will glean from this section, Strategic Hotel Development Planning is an important inclusion.

### **6.1 Strategic Management**

Strategic management is the set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company's objectives. It involves long-term, future-orientated, complex decision-making processes, requiring executive management involvement and considerable resources. (Pearce and Robinson, 1995)

In addition to an organisation's internal environment, challenges are posed by the immediate and remote external environment. The immediate external environment includes competitors, suppliers, increasingly scarce resources, government agencies with their ever more numerous regulations, and customers whose preferences often shift inexplicably. The remote external environment comprises economic and social conditions, political priorities, and technological developments, all of which must be anticipated, monitored, assessed and incorporated into the executive management's decision making. However, executive management often is compelled to subordinate the demands of the firm's internal activities and external environment to the multiple and often inconsistent requirements of its stakeholders, i.e. the owners, top managers, employees, communities, customers and country.

Strategic management focuses on the belief that a firm's mission can be best achieved through a systematic and comprehensive assessment of both its internal capabilities and its external environment. Subsequent evaluation of the firm's opportunities leads, in turn, to the choice of long-term objectives and grand strategies, and ultimately to annual objectives and operating strategies, which must be implemented, monitored and controlled.

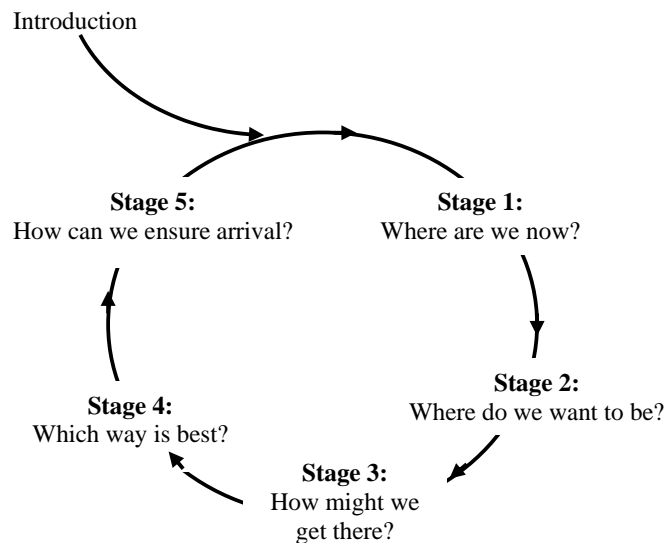
Pearce and Robinson (1995) explain that strategic management involves the planning, directing, organising, and controlling of a company's strategy-related decisions and actions. By strategy, it is meant the large-scale, future-orientated plans for interacting with the competitive environment to achieve company objectives. Although that plan does not precisely detail all future deployments (of people, finances and material), it does provide a framework for managerial decisions.

Strategic management shares the essence of the marketing concept, as described by McDonald and Payne (1998: 4), in that it is also a matching process whereby the organisation's capabilities are matched with the needs of the customer in order to achieve the objectives of both parties. Since very few companies can be equally competent at providing a service for all types of customers, an essential part of this matching process is to identify those groups of customers whose needs are most compatible with the organisation's strengths and future ambitions. It must be recognised that the limitations imposed by an organisation's resources and the unique make-up of its management skills, make it impossible to take advantage of all market opportunities. Companies who fail to grasp this fundamental point that lies at the heart of strategy formulation, are courting commercial disaster.

In summary, Wilson and Gilligan (1999: 6) explain that the strategic management process concerns the need to make decisions. Managers need to know *what* decisions should be made and *how* they should be made. Wilson and Gilligan's sequence of strategic management stages, as illustrated in figure 6.1(a), reflects a problem-solving routine in which the five main components of the strategic management process are identified.

**Figure 6.1(a): The Five Stage Strategic Management Process**

(Source: Wilson & Gilligan, 1999: 6)



**Stage 1** raises the question of where the organisation is now in terms of its competitive position, product range, market share, financial position and overall effectiveness. In addressing this question we are seeking to establish a base line from which we can move forward.

**Stage 2** is concerned with where the organisation should go in the future, which requires the specification of ends (or objectives) to be achieved. While top management in the organisation will have some discretion over the choice of ends, this is constrained by various vested interests.

**Stage 3** deals with the question of how desired ends might be achieved, which begs the question of how alternative means to ends might be identified. This strategy formulation stage requires creative inputs, which cannot be reduced to mechanical procedures.

*Stage 4* focuses on the evaluation of alternative means by which the most preferred (or 'best') alternative might be selected. The need to choose may be due to alternatives being mutually exclusive (i.e. all attempting to achieve the same end) or a consequence of limited resources (which means that a rationing mechanism must be invoked).

*Stage 5* covers the implementation of the chosen means, and the monitoring of its performance in order that any corrective actions might be taken to ensure that the desired results are achieved. Since circumstances both within the organisation and in its environment are unlikely to stay constant while a strategy is being pursued, it is necessary to adapt to accommodate such changes.

## **6.2 Strategic Hotel Development Planning**

Owing to a lack of relevant strategic [hotel] property development text, this section establishes a strategic development planning process, by drawing an analogy between strategic hotel property development and strategic marketing management, marketing plans and generic strategy formulation.

To achieve this end, cited strategic marketing planning text is altered to fit the strategic hotel development theme. Thus, in the following text, some words relating to strategic marketing planning was replaced by relevant hotel development vocabulary. This process merely alters the focus of the cited text from marketing to hotel development, and at no stage changes the gist or meaning of the information.

McDonald (2000: 28) is of the opinion that managers would agree that a sensible way to manage the sales and marketing function is to find a systematic way of identifying a range of options, then choosing one or more of them, which have been scheduled and cost out to determine what has to be done to achieve the objectives. From this it could be deduced that marketing planning is simply a logical sequence of activities leading to the setting of marketing objectives and the formulation of plans for achieving them.

Pearce and Robinson (1995: 3) identify nine critical tasks in the strategy development process:

1. Formulate the company's mission, including broad statements about its purpose, philosophy and goals
2. Develop a company profile that reflects its internal conditions and capabilities
3. Assess the company's external environment, including both the competitive and general contextual factors
4. Analyse the company's options by matching its resources with the external environment
5. Identify the most desirable options by evaluating each option in light of the company's mission
6. Select a set of long-term objectives and grand strategies that will achieve the most desirable options
7. Develop annual objectives and short-term strategies that are compatible with the selected set of long-term objectives and grand strategies
8. Implement the strategic choices by means of budgeted resource allocations in which the matching of tasks, people, structures, technologies, and reward systems are emphasised
9. Evaluate the success of the strategic process as input for future decision-making.

For the purpose of including sufficient detail into a strategic plan to be of any practical use, it is advisable to keep the forecasting period down to three years if possible, since beyond



this period, detail of any kind is likely to become pointless. There can certainly be scenarios for five to ten years, but not a plan in the sense intended for ordinary marketing plans. (McDonald, 2000)

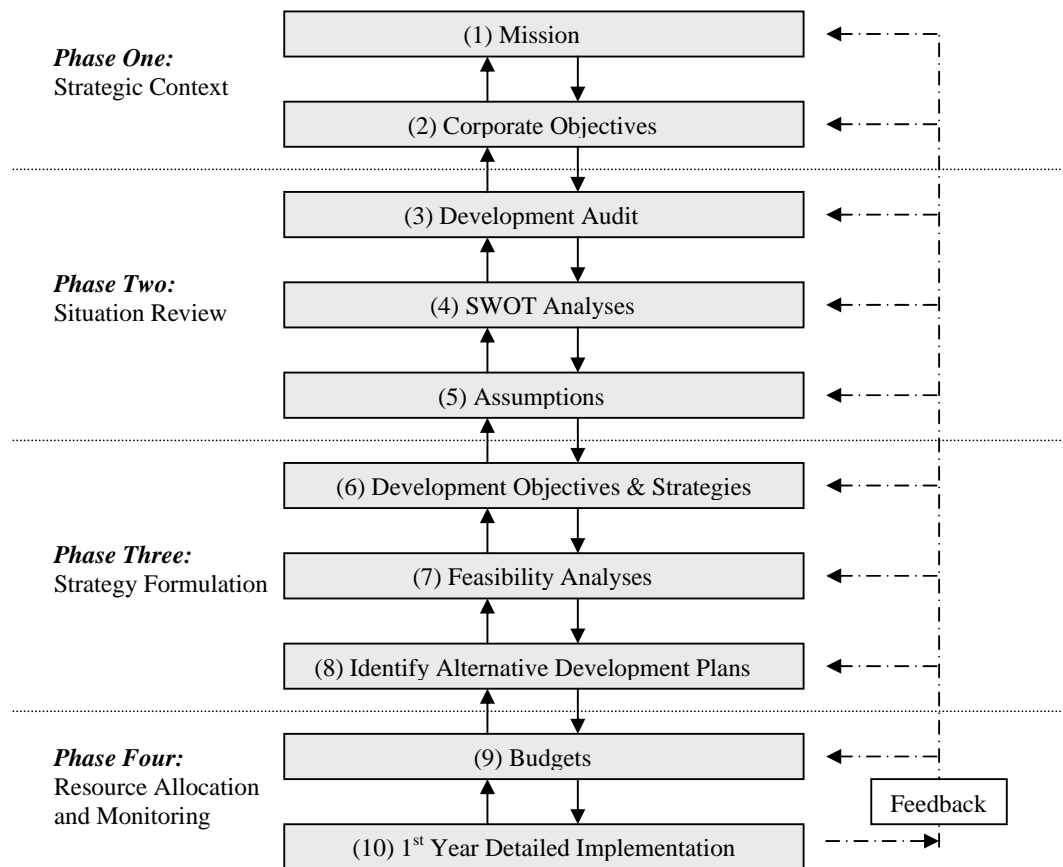
Similar to the information presented before, development planning could be defined as a logical sequence and series of activities leading to the setting of development objectives and formulating plans to achieve them. Strategic Hotel Development Planning Process, the sequential process, is illustrated in figure 6.2 (a).

Conceptually, this process is very simple and primarily involves defining the organisation’s strategic context, a situation review, the formulation of strategies, allocation of resources and finally monitoring the process.

In light of the text above and in accordance with Pearce and Robinsons’ (1995) view of the organisation external environment (section 6.1), there can be little doubt, that property development planning is essential when we consider the increasingly hostile and complex environment in which companies operate. Hundreds of external and internal factors interact in a complex way to affect the ability to achieve profitable sales.

**Figure 6.2(a): Strategic Hotel Development Planning**

(Source: An adaptation of The Marketing Planning Process, McDonald, 2000: 40)



It is important that managers should have some understanding of how all these strategic development planning variables interact, resulting in rational business decisions, irrespective of how important intuition or experience is as a contributory factors in this process of rationality.

In previous decades when business life was less volatile and complex than it is today, hotel organisations were able to survive and sometimes prosper without paying very much attention to development planning. During periods of recession there is often an increased interest in planning and how it can help organisations deal with economic downturn.

Strategic planning needs to permeate all parts of the organisation. A strategy is a company's game plan and reflects a company's awareness of how, when, and where it should compete, against whom it should compete and for what purposes it should compete.

Strategic development planning is more than a cognitive process, because inherently there are implications that can impact on all parts of the business, from the boardroom down.

Finally, the interrelationship between strategic marketing planning and strategic property development planning should be highlighted. Firstly, a property development organisation's strategic development plan is in essence its strategic marketing plan, owing to the fact that its product is property development. In a hotel organisation, the strategic development plan forms a primary component of the strategic marketing plan, directing the company's future expansion, re-development, etc. of its product range. Also when formulating the development plan, it will draw primarily from and fall within the parameters of the organisation's marketing and general strategic plans.

The various components of a strategic hotel development planning process (figure 7.2(a), steps 1 to 10) are briefly explained hereafter.

### **6.3 Organisation Mission: (Step 1)**

*"All companies should have a sense of mission..."*, surmise McDonald and Payne (1998: 37). *"By defining an organisation's mission into a brief, highly personal and meaningful statement, it gives the various stakeholders in an organisation a clear purpose and sense of direction."*

The mission statement is an important device that can provide an understanding for staff working in different parts of the organisation, assisting them to pull together and uphold the corporate values and philosophy. However, it is essential that the mission statement is communicated clearly to all stakeholders and is perceived to be both relevant and realistic. Unless these requirements are met, the mission statement is unlikely to have any real impact on the organisation.

Pearce and Robinson (1995: 14) suggest that the: *"... mission of a company is the unique purpose that sets it apart from other companies of its type and identifies the scope of its operations. In short, the mission describes the company's product, market, and technological areas of emphasis in a way that reflects the values and priorities of the strategic decision makers."*

An example of an international hotel organisation's mission statement is Inter-Continental Hotels': (Six Continents Hotels and Resorts Web Page, 2001)

*"We aim to be the leading global hotel owner/operator/franchisor in the upscale market, satisfying guests at a profit by delivering the highest levels of guest satisfaction, the best cash flows and asset value growth for owners, and to be the employer of choice for our people."*

In table 6.3(a) a comprehensive mission statement is developed for a property development consultancy, specialising in hotel and leisure projects. This mission statement follows the guidelines set out by McDonald and Payne (1998: 56) and McDonald (2000: 41).

**Table 6.3 (a): Hotel Property Development Consultancy's Mission Statement**

(Source: Venter, 2001: 3)

***"We realise your hotel and leisure real estate visions"***

We are a real estate consultancy providing hotel and leisure project excellence, expertise, solutions and peace of mind.

**Our competitive advantage is a function of our,**

- Aim to be the best the market requires
- Comprehensive experience of real estate, construction and hotel operations
- Proud track record and ability to realise our client's hotel and leisure requirements
- Management information systems to remain competitive and achieve market related professional results
- Vigorously upholding our client relationships
- Family of experts who together form the soul and character of the organisation
- Cohesive, open, warm and friendly organisation culture
- Employee pride through education, training, authority and recognition of performance.

**Our business is,**

- Hotel and Leisure Property Development
- Hotel and Leisure Project Management
- Hotel and Leisure Construction Management

**In future we aim to,**

- Annually expand our business by double the expected market average.
- Be recognised as the preferred real estate facilitator.
- Achieve expected profit margins.

### 6.4 Corporate Objectives: (Step 2)

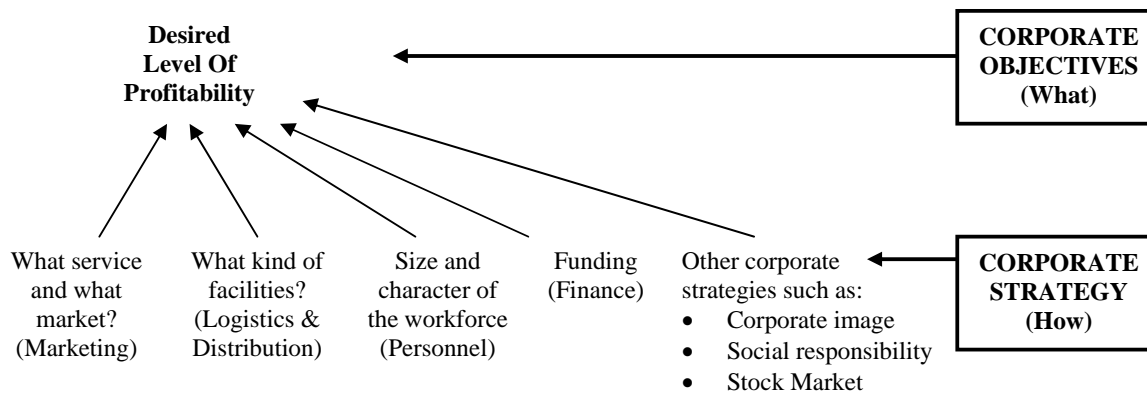
The purpose of corporate objectives is for the stakeholders to measure the success of the mission. McDonald and Payne (1998: 37) remark in light of this: “...*the only true objective of a company is what is stated as being the principal purpose for its existence. In most commercial organisations this is expressed in terms of profit, since profit is the one universally accepted criterion by which efficiency can be evaluated. It is profit which provides the means of satisfying shareholders and owners alike, and it is also profit which provides the motivation to reinvest in the business to make it grow. For non-profit-making organisations such as government departments or charities, objectives such as economic efficiency, funds raised or projects completed might be more realistic measures of performance.*”

From this, it follows that stated desires such as to ‘expand market share’, ‘increase sales’ or ‘improve productivity’ are not objectives, but are actually strategies at a corporate level, since they are the means by which the company will achieve its profit objectives. (McDonald and Payne, 1998)

Some typical corporate objectives and strategies for a commercial organisation are shown in figure 6.4(a). From this, it is clear that at the next level down in the organisation, i.e. at the functional level, ‘what services and what markets’ becomes the marketing objectives. In turn, the marketing strategies for meeting these, such as using advertising or personal selling, become departmental objectives for those particular parts of the business.

**Figure 6.4(a): Relationship between Corporate Objectives and Strategies**

(Source: McDonald and Payne, 1998: 39)



Viewed in this way, the whole organisation is a hierarchical chain of inter-linking objectives and strategies.

From this hierarchical interconnection, it should be understood that individual components or levels within organisations, whether it be a strategic business unit (SBU), organisation function (e.g. marketing, financial, operations, etc.) or department (e.g. property development, food and beverage, etc.) should develop their own objectives and strategies from higher level strategies.

The specific objectives and subsequent strategies of a property development department in a larger organisational environment would flow from the company’s grand strategies. The formulation of objectives is influenced by the development department’s perception of their

responsibilities, as well as by the restrictions the environment places on their behaviour. (Lawson, 1996)

Further to the development department’s objectives, individual projects also have specific objectives. The project objectives will be an extrapolation of the subject higher level, i.e. development department’s and executive/grand objectives. Specific project objectives are discussed in section 6.8.

**6.5 Development Audit: (Step 3)**

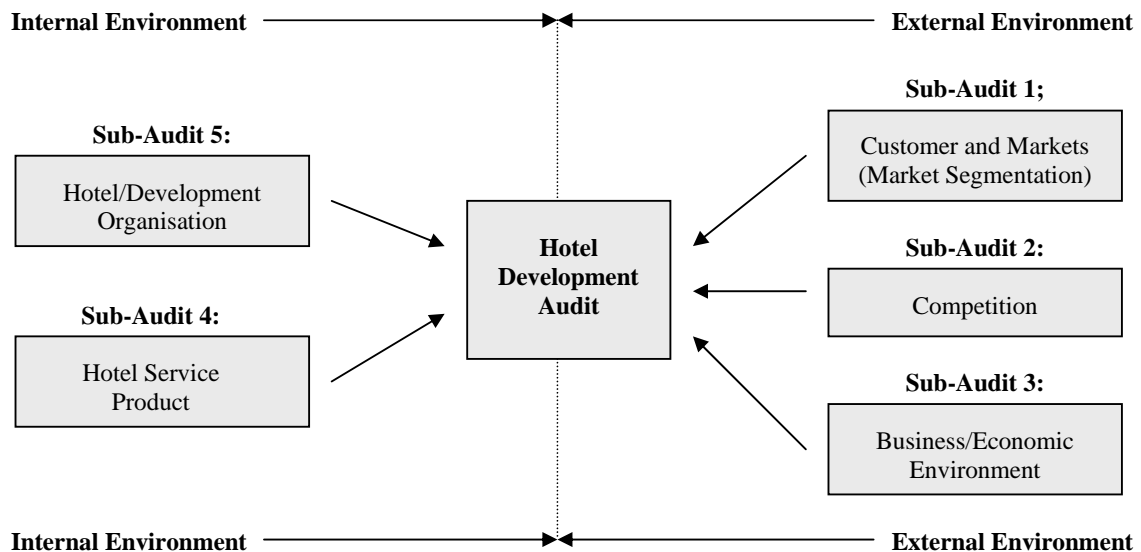
“A [development] audit provides the means for the organisation to understand how it relates to the environment in which it operates. It also enables internal strengths and weaknesses to be identified in terms of how they match external opportunities and threats. The [development] audit should be a systematic, critical and unbiased review and appraisal of the company’s [development] operations. Thus, it provides management with the information to select a position in its particular environment based on known facts. In short, it provides the answer to the question: Where is the company now? “ (McDonald & Payne, 1998: 78).

The development audit is a process in which data is collected from external sources. It is concerned with the business and economic environment, together with market and competitor analysis. Not only is the current situation analysed, but also future trends and their significance are considered. Internal sources provide additional information and help to identify the company’s strengths and weaknesses.

Note that the development audit itself is not a development plan. By carrying out an audit on a regular basis, e.g. once a year (rather than just at those times when things go wrong), management is more prepared for future occurrences. This means that, instead of responding to symptoms, managers address the root causes of organisational problems.

**Figure 6.5(a): Constituent Parts of the Development Audit**

(Source: McDonald and Payne, 1998: 80)



The development audit can be visualised as a set of five interrelating sub-audits, which focus on different aspects of the business, as shown in figure 6.5(a).

“Any company carrying out an audit will be faced with two kinds of variables. Firstly, there are variables over which the company has no direct control. These usually take the form of what can be described as environmental, market and competitive variables. Secondly, there are variables over which the company has complete control, i.e. the operational variables” (McDonald, 2000: 43).

The *external audit* starts with an examination of the general economy, after which it establishes the health and growth of the markets served by the company.

**Table 6.5.1(a): Development Audit Checklist**

(Source: McDonald, 2000: 45)

**EXTERNAL (opportunities and threats)**

**Business and Economic Environment**

<i>Economic</i>	Inflation, unemployment, energy, price, volatility, materials availability, etc.
<i>Political/fiscal/legal</i>	Nationalisation, union legislation, taxation, duty increases, regulatory constraints (e.g. labelling, product quality, packaging, trade practices, advertising, pricing, etc.)
<i>Social/cultural</i>	Education, immigration, emigration, religion, environment, population distribution and dynamics (e.g. age distribution, regional distribution, etc.), changes in consumer life style, etc.
<i>Technological</i>	Aspects of product and/or production technology which could profoundly affect the economics of the industry (e.g. new technology, cost savings, materials, components, equipment, machinery, methods and systems, availability of substitutes. etc.)
<i>Intra-company</i>	Capital investment, closures, strikes, etc.

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**The Market**

<i>Total market</i>	Size, growth, and trends (value, volume). <i>Customers/consumers:</i> changing demographics, psychographics and purchasing behaviour.
<i>Market characteristics, developments and trends</i>	<i>Products:</i> principal products bought; end-use of products; product characteristics (weights, measures, sizes, physical characteristics, packaging, accessories, associated products, etc.). <i>Prices:</i> price levels and range; terms and conditions of sale; normal trade practices; official regulations, etc. <i>Physical distribution:</i> principal method of physical distribution. <i>Channels:</i> principal channels; purchasing patterns (e.g. types of product bought, prices paid, etc.); purchasing ability; geographical location; stocks; turnover; profits; needs; tastes; attitudes; decision-makers, bases of purchasing decision; etc. <i>Communication:</i> principal methods of communication, e.g. sales force, advertising, direct response, exhibitions, public relations, etc. <i>Industry practices:</i> e.g. trade associations, government bodies, historical attitudes, inter-firm comparisons; etc.

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**Competition**

<i>Industry structure</i>	Make-up of companies in the industry, major market standing/reputation; extent of excess capacity; production capability; distribution capability; marketing methods; competitive arrangements; extent of diversification into other areas by major companies in the industry; new entrants; mergers; acquisitions; bankruptcies; significant aspects; international links; key strengths and weaknesses.
<i>Industry profitability</i>	Financial and non-financial barriers to entry; industry profitability and the relative performance of individual companies; structure of operating costs; investment; effect on return on investment of changes in price; volume; cost of investment; source of industry profits; etc.

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**Table 6.5.1(a): Development Audit Checklist (Continued)****INTERNAL (strengths and weaknesses)****Own Company**

Sales (total, by geographical location, by industrial type, by customer, by product)

Market shares

Profit margins

Marketing procedures

Marketing organisation

Sales/marketing control data

Marketing mix variables as follows:

- |                              |                     |
|------------------------------|---------------------|
| • Market research            | Samples             |
| • Product development        | Exhibitions         |
| • Product range              | Selling             |
| • Product quality            | Sales aids          |
| • Unit of sale               | Point of sale       |
| • Stock levels               | Advertising         |
| • Distribution               | Sales promotion     |
| • Dealer support             | Public relations    |
| • Pricing, discounts, credit | After-sales service |
| • Packaging                  | Training            |
- 

**Operations and Resources**

*Development objective* Are the development objectives clearly stated and consistent with marketing and corporate objectives?

*Development strategy* What is the strategy for achieving the stated objectives? Are sufficient resources available to achieve these objectives? Are the available resources sufficient and optimally allocated?

*Structure* Are the development responsibilities and authorities clearly structured along functional, product, end-user, and territorial lines?

*Information system* Is the marketing intelligence system producing accurate, sufficient and timely information about developments in the marketplace? Is information gathered being used effectively in making marketing decisions?

*Planning system* Is the marketing planning system well conceived and effective?

*Control system* Do control mechanisms and procedures exist within the group to ensure planned objectives are achieved, e.g. meeting overall objectives, etc.?

*Functional efficiency* Are internal communications within the group effective?

*Inter-functional efficiency* Are there any problems between marketing and other corporate functions? Is the question of centralised versus decentralised marketing an issue in the company?

*Profitability analysis* Is the profitability performance monitored by product, served markets, etc., to assess where the best profits and biggest costs of the operation are located?

*Cost-effectiveness analysis* Do any current marketing activities seem to have excess costs?

Are these valid or could they be reduced?

---

The purpose of the *internal audit* is to assess the organisation's resources as they relate to the environment and the resources of competitors.

Table 6.5.1(a) is a checklist of the areas that should be investigated as part of the development audit.

Each one of these headings should be examined with a view to isolating those factors that are considered critical to the company's performance. Initially, the auditor's task is to screen the enormous amount of information and data for validity and relevance. Some data and information will have to be reorganised into a more easily usable form, and judgement

will have to be applied to decide what further data and information is necessary for a proper definition of the problem.

#### **6.6 SWOT Analysis: (Step 4)**

It could be said that the previous stage, the development audit, provides all the pieces of a jig-saw puzzle, and then the SWOT analysis takes these pieces and tries to make a picture that makes sense, writes McDonald and Payne (1998: 108). A SWOT analysis is a summary of the audit under the headings, internal strengths and weaknesses as they relate to external opportunities and threats.

McDonald (2000: 48) is of the opinion that SWOT analyses should be conducted for each segment that is considered to be important in the company's future. *"These SWOT analyses should, if possible, contain just a few paragraphs of commentary focusing on key factors only. They should highlight internal differential strengths and weaknesses vis-à-vis competitors and key external opportunities and threats. They should be interesting to read, contain concise statements, include only relevant and important data, and give greater emphasis to creative analysis."*

#### **6.7 Assumptions: (Step 5)**

The previous section elaborated on the need for fact-finding and data gathering as the foundation upon which the development plan is built. However it is impossible to start with the facts without also starting out with some assumptions. Assumptions are certain key determinants of success in all companies about which assumptions have to be made before the planning process can proceed. (McDonald, 2000)

McDonald and Payne (1998: 113) define assumptions *"...as the basis for objective and strategy setting. Facts and assumptions can become blurred at times, to the extent that one can be mistaken for the other, and it is important to distinguish between them."*

It is important to state assumptions explicitly. By making them explicit, it becomes possible to check and monitor assumptions to be certain that they are, and remain valid, and if not, to develop contingency plans to deal with them.

The purpose of the key assumption steps is to identify explicitly those factors, which will be critical to the success or failure of the strategic development planning process. Key assumptions need to be considered in terms of how they impact on the organisation as a whole and on each market segment. Since they are an estimate of the future operating conditions of the development plan, they may influence not only its formulation, but also its implementation.

Key assumptions might include:

- Inflation rates
- Growth of the economy
- Changes in political/legislative framework
- Interest rates
- Demographic predictions.



In order to be systematic, it can be useful to list key assumptions under a number of general headings such as:

- The general economy
- The hotel 'industry' sector under consideration
- The company's markets
- Competitors
- Internal organisational factors
- Technological and other developments.

When they are identified, it is important to consider their implications for the development plan. This can remove potential sources of disagreement between managers involved in the planning process and can also indicate where contingency plans might need to be developed, should an assumption prove not to be true.

### **6.8 Development Objectives and Strategies: (Step 6)**

Kindly refer to the following where development objectives and strategies are extensively discussed:

- Section 5.2.1
- Section 5.2.2
- Section 5.2.3
- Section 6.4

To recap, an objective is the set target to be achieved and a strategy is the plan of how to achieve the objectives. There can be objectives and strategies at all levels in the organisation.

### **6.9 Financial Feasibility Analyses: (Steps 7)**

Having completed the major planning task, says McDonald and Payne (1998), it is normal at this stage to employ judgement, similar experience, field tests, etc. to test the feasibility of the objectives and strategies in terms of market share, sales, costs and profits.

The purpose of estimating the expected results by means of feasibility analyses is to determine whether the development strategies will actually deliver the desired results. Once the development objectives and strategies have been decided on for the various development options, the financial implications of introducing them need to be evaluated. This will require a detailed review of (McDonald & Payne, 1998: 136):

- Development Costs
- Projected Sales Revenues
- Operational Costs
- Projected Return on Investment, etc.

This analysis should show that the chosen approach would indeed deliver the anticipated financial contribution to achieve the required targets. If it does not, then the development strategies will need to be re-examined in order to establish how they could be redeveloped to achieve the expected results.

*“In times of economic uncertainty, it can be useful to calculate three sets of analyses. These would reflect the estimated results based upon the most pessimistic interpretation of all the salient factors, the most likely result and those facts based on the most optimistic levels of demands. In this way, it becomes possible to identify the possible spread of expected results and, in that sense, have a feel for the potential ‘margin of error’ surrounding the most likely result”* (McDonald & Payne, 1998: 136).

Refer to section 7 for an exhaustive explanation of hotel property development feasibility.

#### **6.10 Identify Alternative Development Plans: (Step 8)**

*“Even if the original objectives and strategies do produce the expected results, it is still important to ascertain if a more effective approach could lead to even better results”* (McDonald & Payne, 1998: 136).

It is at this stage that plans should be formulated to cover anticipated lower or higher levels of demand.

Contingency plans should also be considered at this stage of the development planning process, in response to the impact of different sets of assumptions made earlier. It will not be possible to develop plans for every eventuality, but it is advisable to consider at least the following (McDonald & Payne, 1998: 137):

- A *defensive contingency plan* which takes into account the possibility that the assumptions surrounding the development audit were unduly optimistic and thus responds to threats that might materialise
- An *offensive contingency plan*, which is really the converse of the defensive contingency plan and seeks to take advantage of opportunities, should they occur.

#### **6.11 The Budget: (Step 9)**

The various strategies in a strategic development plan would normally be converted in to financial estimates. These estimates would then become the various development budgets.

Most often, as advised by McDonald and Payne (1998: 141), there would not only be a budget for the medium term (e.g. full three years of the strategic development plan), but also a very detailed budget for the first year of the plan (i.e. one-year development /operational plan).

It will be obvious from all of this that the setting of budgets becomes not only much easier, but the resulting budgets are more likely to be realistic and related to what the whole company wants to achieve, rather than just one functional department.

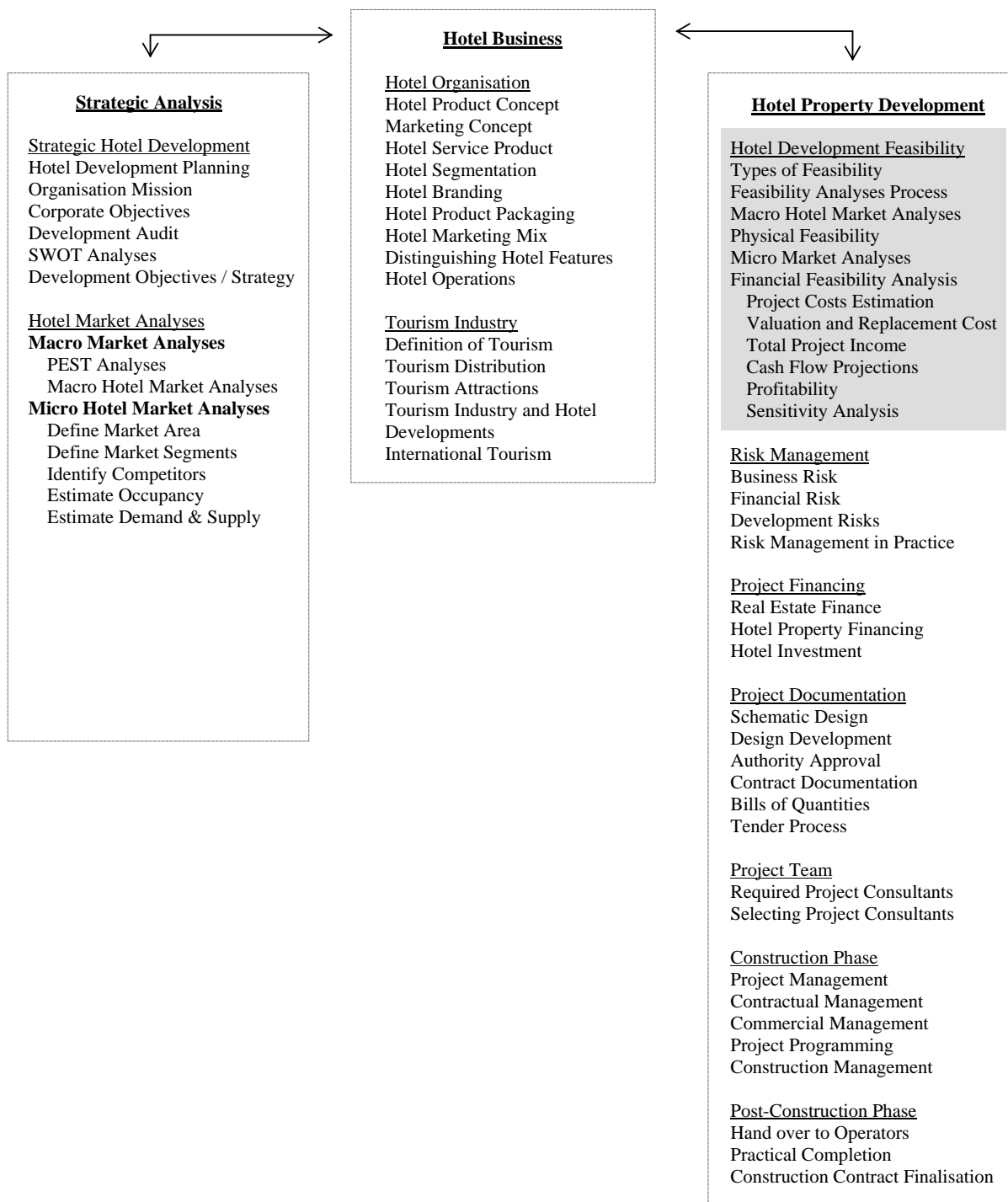
#### **6.12 First Year’s Detailed Implementation Programme: (Step 10)**

Once agreement has been reached regarding budgets, those responsible for the development of the first year implementation programme of the development plan can then proceed to develop details of tasks to be completed, together with responsibilities and timings.

In a one-year tactical plan, the general development strategies would be developed into specific sub-objectives, each supported by more detailed strategy and action statements.

**Chapter 7:**

**Hotel Property Development Feasibility**



## **7 Hotel Property Development Feasibility**

### **7.1 Introduction to Feasibility Analysis**

Cloete (1995: 90) recommends that before property development is undertaken, it is necessary to do an analysis to evaluate the chances of successfully executing the development. This analysis, called the feasibility study or viability analysis, involves the comparison of the cost benefit relationships of alternatives over specific time periods.

Further to the above recommendation, Cloete (1995: 91) cites Downs' definition of a feasibility study, being any analysis aimed at determining whether a proposed development on a particular site can be successfully executed. This definition begs the question, what does "successfully executed development" actually mean? In answer to this question, it is submitted that a development is successful, when from the viewpoint of the developer it satisfies the developer's objectives, whatever that maybe. Of course, a development may be unsuccessful from the developer's point of view (for example, it may not result in a desired profit) but it may nevertheless be successful from another point of view (for example, it may provide a facility which satisfies a need of the community).

Ransley and Ingram (2000: 58) explain that no standard definition exists for feasibility studies, even though it is well-known and used by development professionals and understood to some extent by others.

Cloete (1995: 91), includes Graaskamp's generic definition of what a feasibility is:

*"A real estate project is 'feasible' when the real estate analyst determines that there is a reasonable likelihood of satisfying explicit objectives when a selected course of action is tested for fit to a context of specific constraints and limited resources."*

From this feasibility definition by Graaskamp, Cloete deduces a number of critical implications:

- The "objectives" are specific to the client. Feasibility is unique to the individual developer and his specific objectives and resources.
- Use of the term "likelihood" explicitly recognises that a feasibility study involves consideration of future events that are of necessity probable in nature. The impact of future events must be considered, whether it is done by sophisticated analysis of probability or by "gut feel."
- The concept of "satisfying" refers to satisfaction of the objectives of the developer.
- The "selected course of action" refers to the unique nature of the proposed development. This implies that a feasibility study is specific to a particular proposal on a specific site and at a specific time.
- "Tested for fit to a context of constraints and limited resources" means that the proposed course of action must be compared to its context, to determine whether there are any incompatibilities with the applicable physical, economic and political characteristics of both the environment of the proposed development and the developer himself.

The purpose of a feasibility study is to provide an objective, independent analysis of a development opportunity (or an acquisition opportunity, in the case of an existing property) and sufficient information for the client (and others involved in the project) to make a decision as to whether the project should proceed and, if so, in what form. At the request of the client, and given the units of measurement (for example, rates of return on project cost and on equity), the consultant can reach a conclusion as to the feasibility. However, in practice the feasibility conclusion should be made by the client, based on the evidence presented in the feasibility study plus other external factors such as political pressures and economic climate to name only two.

What a feasibility study for a hotel property should do (provided it is positive) is to give support to a hotel development proposal. A study can only conclude that a project is feasible if the measurement of feasibility is predetermined, which will vary according to who makes the decision. A definitive conclusion can therefore be reached from one viewpoint (for example, the projected income streams are at an acceptable level according to specific criteria), while the project may not be considered feasible from another viewpoint (for example, because the projected net foreign exchange earnings of the proposed property are insufficient to compensate for environmental drawbacks). (Ransley & Ingram, 2000)

The level of risk involved in the decision to proceed, varies according to the nature of the project, the reliability of the database, the team's ability to control future events and conditions, and the expected level of financial gain and commitment.

The "proceed" decision rests on a set of assumptions, analyses, and expectations. It requires an accurate assessment of current and future economic and market conditions, a hotel development plan and hotel business strategy that insulate the project from conditions outside the developer's control, a management group committed to maintaining the quality of the investment, and a feasibility study that is pragmatic, timely, and responsive to all potential influences on the hotel's performance.

In his marketing feasibility diagram, as illustrated in table 7.1 (a), Lawson (1996: 109) includes several dimensions and considerations a feasibility analysis should include.

In general terms, says Ransley and Ingram (2000: 60), it is possible to categorise the reasons why feasibility studies are commissioned into five primary groups:

- To support an application for finance
- To support an application for planning permission
- To attract potential operators
- To define optimum land use
- To define a concept.

Further to the primary categories, most feasibility studies will also have one or more secondary purposes, which could include:

- To provide marketing information
- To identify market opportunities
- To analyse specific operational aspects, for example local labour laws
- To identify potential sources of development finance.

**Table 7.1(a): Hotel (Property) Development Feasibility**

(Source: An adaptation of Organisation of Market Feasibility Studies by Lawson, 1995: 109)

<b>Hotel Feasibility Stages</b>	<b>Marketing &amp; Operations</b>	<b>Economic &amp; Financial Analysis</b>	<b>Location &amp; Development</b>
↓ <b>Organisational Identity &amp; Policies</b> ↓	<b>Market Definition</b> <ul style="list-style-type: none"> <li>• Target market</li> <li>• Market characteristics</li> <li>• Viability</li> <li>• Potential growth</li> </ul>	<b>Investment Sourcing</b> <ul style="list-style-type: none"> <li>• Economic climate</li> <li>• Trends</li> <li>• Price: earnings ratios</li> <li>• Source of financing</li> <li>• Conditions of financing</li> </ul>	<b>Location Identification</b> <ul style="list-style-type: none"> <li>• National and regional patterns of development</li> <li>• Optimum location for development</li> </ul>
↓ <b>Areas</b> ↓	<b>Local Data Analysis</b> <ul style="list-style-type: none"> <li>• Catchment areas</li> <li>• Socio-economic trends</li> <li>• Business activities</li> <li>• Tourism demands</li> </ul>	<b>Funding Considerations</b> <ul style="list-style-type: none"> <li>• Development incentives</li> <li>• Location incentives</li> <li>• Location benefits</li> </ul>	<b>Potential Areas Survey</b> <ul style="list-style-type: none"> <li>• Location advantages</li> <li>• Planning conditions</li> <li>• Traffic transportation</li> <li>• Future developments</li> </ul>
↓ <b>Sites</b> ↓	<b>Competition Assessment</b> <ul style="list-style-type: none"> <li>• Location</li> <li>• Main markets</li> <li>• Advantages</li> <li>• Weaknesses</li> </ul>	<b>Labour Availability</b> <ul style="list-style-type: none"> <li>• Employment in area</li> <li>• Wage rates</li> <li>• Services available</li> </ul>	<b>Site Requirements</b> <ul style="list-style-type: none"> <li>• Area</li> <li>• Access</li> <li>• Car parking</li> <li>• Infrastructure</li> </ul>
↓ <b>Plans</b> ↓	<b>Demand Analysis</b> <ul style="list-style-type: none"> <li>• Segmented categories</li> <li>• Projection over period</li> <li>• Sensitivity to change</li> </ul>	<b>Operating Forecast</b> <ul style="list-style-type: none"> <li>• Business mix</li> <li>• Average room rate</li> <li>• Occupancy levels</li> </ul>	<b>Building Needs</b> <ul style="list-style-type: none"> <li>• Number</li> <li>• Type of rooms</li> <li>• Range of facilities</li> <li>• Net and gross areas</li> </ul>
↓ <b>Feasibility</b>	<b>Operating Needs</b> <ul style="list-style-type: none"> <li>• Organisation</li> <li>• Contract arrangements</li> <li>• Staff requirements</li> <li>• Procedures</li> </ul>	<b>Investment Feasibility</b> <ul style="list-style-type: none"> <li>• Construction cost model</li> <li>• Budgets</li> <li>• Revenues</li> <li>• Costs</li> <li>• Profit &amp; loss forecast</li> <li>• Sensitivity analysis</li> </ul>	<b>Initial Planning</b> <ul style="list-style-type: none"> <li>• Client's brief defining hotel style</li> <li>• Facility programming</li> <li>• Schematic plans</li> <li>• Options for development</li> </ul>

Any feasibility study is a perishable product. The future can never be predicted with guaranteed accuracy and although the consultant will bring his or her experience into the equation when doing so, and will conscientiously research all the factors which might impact on future projections, unforeseen events can and will happen. Such things might be the unexpected closure of a major employer and generator of room demand (perhaps because the firm has been taken over and operations moved elsewhere), or a natural

disaster, such as an earthquake, which may destroy half the existing hospitality stock in a moment.

The findings of a hotel feasibility study should therefore be subject to examination at regular intervals, to assess the impact of any changes in the bases and conditions of the recommendations and projections that have been built up on those factors.

As the world economy enters the next phase in the business cycle, new hotel proposals will require feasibility studies to measure market demand and to prove that projects are economically viable. In order to avoid the problems of overbuilding, these new studies should focus on one major question: Turkel (2000)

- Is there a market for this hotel at this location?
- If so, where is that market and how large is it?
- What are its needs?
- How is it currently being served?
- What share can be captured?

Turkel (2000) further recommends, in order to make feasibility studies more realistic, a fresh look at the methodology needs to be taken, including the following important issues:

- Occupancy and average daily rate projections should reflect the real volatility in the marketplace.
- There should be a genuine analysis of the tradeoffs inherent in the yield management decisions as they pertain to both market penetration and revenue maximisation.
- There should be a serious analysis of the relative profitability of the food and beverage outlets beyond the misleading departmental profit margins provided by the Uniform System of Accounts.
- The feasibility study analysis should enable owners to decide whether to manage, lease or franchise the food outlets.

When comparing various definitions of the “feasibility study” concept, a number of common elements stand out (Cloete, 1995):

- A clear definition of the developer’s objectives is needed to determine the success of a potential development.
- A feasibility study is aimed at the future and is based on subjective judgements of probable future events.
- Since many variables are involved in projections, there usually is not only one optimal solution, but rather a number of possibilities, each with its own probabilities and risks.
- A possible development should not only comply with the developer’s objectives, but must also take into consideration the restrictions placed on it by the external environment. A feasibility study therefore shows the same characteristics as those of problem-solving in general: an attempt is made to match the determining elements of (i) the context in which the problem arises and (ii) the suggested solution.
- Suggested development is furthermore restricted by the resources (financial, time and other resources) available to the investor. An optimal development from other points of view is therefore not necessarily feasible within the restrictions of a specific developer.



- Although certain types of developments have common characteristics, a feasibility study is eventually only applicable to a specific project, carried out at a specific time and in a specific context.

Finally, from Cloete (1995: 90) and, Pearce and Robinson (1995: 4) it is obvious that the strategic management and property feasibility analysis processes share the following similar dimensions:

- Require top-management involvement and decisions
- Organisation and developer's objectives should be met, for property development to be rendered successful
- Require large amounts of the firm's resources
- Often affect the firm's long-term prosperity
- Is future orientated
- No single optimal solution normally exists
- Limited by the resources available
- Should conform to the external constraints.

## 7.2 Types of Feasibility Analysis Reports

Pyhrr et al (1989: 40) is of the opinion that a "complete" feasibility study might include seven types of studies, any one of which could be the analyst's total assignment in a particular situation.

1. *Strategy study*: Determination of investment and development objectives, policies, plans, and decision criteria.
2. *Legal study*: Analysis of the various legal and political constraints, and problems that may affect the project, including forms of organisation, title, zoning, building codes, etc.
3. *Compatibility study*: The compatibility of the project to surrounding land uses, city or county master plans, public policies, and environmental standards.
4. *Market analysis*: Macro-economic studies, including regional analysis, economic base and neighbourhood or related aggregate data reviews.
5. *Merchandising study*: Consumer surveys, analysis of competitive properties, sales and marketing evaluation, strategy, price, absorption rate studies and the like.
6. *Architectural and engineering study*: Determination of alternative land use plans, structure, and design alternatives, soil analysis, utility availability, etc.
7. *Financial-economic study*: Cash flow forecasts, tax and tax shelter planning, rate-of-return analysis, analysis of financing alternatives, holding-period analysis, and so on.

As can be seen, the nature and extent of the feasibility study is determined by the nature and extent of the problems that need to be solved. It also is determined by the sophistication of the decision maker who perceives the problems, the size of the project and the budget available for such study.

In light of the wealth of possibilities, it is necessary to define the concept being used and the nature of the study being done when using the term "feasibility study." Seldom does a developer, investor or analyst perform a complete feasibility study as defined here, wherein investment analysis is actually a subset of the feasibility analysis.

### 7.3 Comparing Property Development Feasibility and Property Appraisal Analysis

According to Rushmore and Baum (2001: 25): “...each time a hotel is bought, sold, developed, financed, refinanced, syndicated, or assessed, parties to the transaction may require some type of market study and valuation to indicate its future financial performance. Over the years the lodging industry has used a variety of terms to describe the process of forecasting the revenue and expenses of a property and estimating its market value. These studies may be called feasibility studies, market studies, market studies with financial projections, market demand studies, economic studies, economic feasibility studies, appraisals, valuations, economic valuations, economic market studies and appraisals, or market studies and valuations.”

It would seem from this statement by Rushmore and Baum that property development feasibility analyses and property appraisals/valuations are referred to as one and the same concept.

Comparing citations before by Ransley and Ingram, Cloete, Downs, Graaskamp and the above statement by Rusmore and Baum, it could be surmised that although property feasibility and appraisal/valuation studies share vast mutual areas or aggregate components for analyses, they are not one and the same thing.

Property feasibility studies are directed more towards evaluating possible successful execution of a proposed property development, comparing the cost benefit relationships of alternatives over a future period of time, using the developer’s objective as a benchmark. Feasibility analyses generally presume a development situation in which the following exist (Pyhrr et al, 1989: 39):

- A site or building is searching for a user.
- A user is searching for a site and certain improvements.
- An investor is looking for a means to participate in either of the situations mentioned above.

This stands in contrast to property appraisals/valuations, which are geared towards establishing a market value for a property (existing or proposed) or a hotel business as an example, at a specific moment in time. Appraisals/valuations are performed for a number of reasons (Rushmore and Baum, 2001: 30):

- To develop an opinion of market value or investment value for potential hotel purchasers
- To estimate market value or investment value for potential hotel sellers
- To interest lenders in providing project financing
- To attract investors for equity syndications
- To resolve property tax disputes
- To establish value for bankruptcy and/or foreclosure (liquidation sale)
- To value property for condemnation proceedings
- To determine if a proposed hotel will be economically feasible
- To determine if present management is maximising the value of the property
- To quantify the value of property expansion or renovation.

#### **7.4 Similarities between Strategic Hotel Development Planning and Feasibility Analyses**

From the previous strategic hotel development planning section (section 6.2) and the following feasibility analyses text, it is clear that these two processes share components/analyses which could be used interchangeably. For example the development audit (section 6.5) contains all the elements required for the feasibility study's market analyses.

The differences between the strategic hotel development planning and the feasibility analysis processes are in the focus of the processes, as explained in the following:

*Strategic hotel development planning* is the set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company's objectives. It involves long-term, future-orientated, complex decision-making processes, requiring executive management involvement and considerable resources. (Pearce and Robinson, 1995)

*Feasibility analyses* are undertaken to analyse and evaluate the chances of successfully executing a specific subject development, and involves the comparison of the cost benefit relationships of alternatives over specific time periods. (Cloete, 1995)

Owing to the overlapping of some of the mentioned analyses/components, it could be a major benefit and timesaver to the feasibility analyser, should a strategic hotel development plan be in place.

#### **7.5 Feasibility Analyses Process**

Various approaches to feasibility studies exist, depending on the purpose for which the study is undertaken. The approaches differ mainly according to the emphasis placed on different components. (Cloete, 1995)

Although Ransley and Ingram (2001: 68) previously stated that there is no such thing as a standard feasibility study, they feel that the experience of professional consultants shows that there are common elements in any study. The demands of a specific study, and the commissioning client(s), will dictate the degree to which any element is covered and the manner in which it is investigated and reported, but none can readily be omitted. Common hotel development feasibility elements are:

- a) Evaluation of the proposed site for the property, e.g. its position and general description, topology and topography, soil considerations, access to utilities and infrastructure, outlook and overlooks, environmental considerations, sun and shade patterns, prevailing winds, and its general suitability for the proposed project, plus ownership of the site and access alongside, planning permissions and restrictions relating to the site and the surrounding areas. (For some of these criteria, input from other professionals such as civil engineers will be required.)
- b) Transportation and accessibility, relating to the general and specific location, both currently and in the light of planned/potential future changes.
- c) Location of the site relative to any competitors, and to existing and future demand generators (for example, business districts, conference centres) and tourist attractions.

- d) Assessment of the economic and social climate of the area in which the project is to be located, to identify future economic and tourism development and whether there are likely to be future fiscal or social constraints that could influence occupancy rates.
- e) Market evaluation. Where pioneering projects cannot benefit from local market demand trends, the consultant should then look elsewhere for data to support projections. (This could include an evaluation of similar, but non-competitive, units in other locations.)
- f) Sources and characteristics of demand, existing and potential, for rooms, food and beverage, conference, leisure and other facilities, plus drivers of that demand, and relevant internal and external influences.
- g) Evaluation of competitive situation and planned additions, and identification of market opportunities and advantage for this project.
- h) Future demand and likely market share/demand potential.
- i) Evaluation of design concept and recommended facilities.
- j) Projected operating statement's estimates of room occupancy, average daily rate, food, beverages, telephone, room hire, leisure and other revenues, and the associated fixed and variable operating costs.
- k) Cash flow projections and investment appraisal - estimates of fixed property costs, funding structures, loan terms and application of various appraisal methods including net present value, IRR and payback. A valuation of the project may also be included.

Ransley and Ingram further advise (2000: 68), before commencing with a hotel property development feasibility study, there are two principles of paramount importance to which any hotel feasibility study must adhere in order for it to be valid:

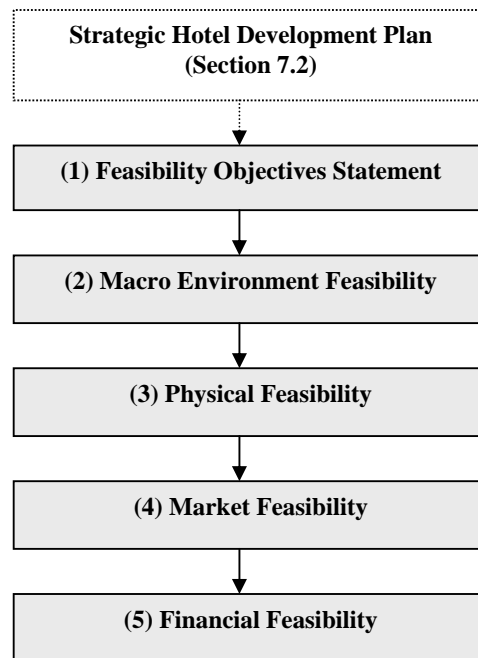
- **The contents of the study must be current, relevant and focused.** Everything contained therein must have some impact upon the proposed hospitality operation, or must be instrumental in assisting the reader in making a decision based upon that study. General background information on a country or area is therefore relevant where the reader may be unfamiliar with such information. However, even then the skill of the consultant lies not so much in what he or she puts into a study, but in what he or she leaves out.
- **The work of the team undertaking the feasibility study must begin with an assessment of the suitability of the site for development.** Much time and effort can be wasted in assessing the local market and other relevant aspects if it has not been established from the outset that the site will be suitable at the time the property is in operation, for some type of hospitality [hotel] development. That location is of vital importance to a hospitality [hotel] operation and cannot be ignored when carrying out a feasibility study.

### 7.5.1 Hotel Property Feasibility Framework

The feasibility process views of Baltin et al, Rushmore and Baum, Ransley and Ingram, and Cloete are combined in figure 7.5.1(a). This hotel property development feasibility process forms the framework for the following feasibility analyses text, elaborating and exploring the aggregate hotel property development feasibility components.

**Figure 7.5.1(a): Hotel Property Development Feasibility Process**

(Source: A visual conclusion of relevant text by Baltin et al (1999), Rushmore and Baum (2001), Ransley and Ingram (2000), and Cloete( 1998))

**7.5.2 Hotel Property Feasibility Analysis Components**

Before elaborating on the individual feasibility analysis components, it is prudent to explain the rationale behind the chosen definition and sequence of the feasibility components.

In some feasibility process frameworks, distinction is drawn between the concepts of market analyses and marketability analyses. From property development textbooks and marketing subject literature, it would seem that a confusing range of definitions exist of the concepts **market analyses** and **marketability analyses**. As an example, Pyhrr et al (1989: 408) is of the opinion that marketability analyses deal with a particular property's marketability, i.e.: "...the ability to generate an income stream, which will satisfy the investor's financial objectives over a projected ownership cycle." Market analyses on the other hand, says Pyhrr et al (1989), may be the final objective of the market research effort, or it may be an intermediate step necessary to generate information for the marketability study.

Pyhrr et al (1989) further explains that in this distinction it is not clear where the market analyses end and the marketability analyses begin. However, the confusion can be eliminated if one thinks of the market and marketability analysis as a continuum, in which the market analysis represents the macro-environment study and the marketability analysis the micro-environment study.

This definition of Pyhrr et al (1989) stands in contrast to Wurtzbaach and Miles (1994: 248) as real estate authors, and marketing text authors such as McDonald (2001) McDonald and Payne (1998), Kotler et al (1999), and Stanton et al (1991). Not only do the marketing authors rarely, if at all, use the concept of marketability, but rather use the terms market,

marketability and marketing as integrated components of a single concept, with differentiation only as nouns or verbs.

The essence of what Pyhrr et al (1989) explains in the above, i.e. the external macro- and micro-environment analyses, forms part of the market analysis or market audit, which in turn forms an integral part of the marketing planning process and the wider marketing concept. Refer to table 6.5(a), wherein McDonald defines the primary two variables of a market audit.

In support of the other marketing authors, Kotler et al (1999: 104) recognises that a company's business environment consists of the outside actors and forces that affect a company's ability to develop and maintain successful transactions with its target customers. The business environment is made up of a micro-environment and a macro-environment. The micro-environment consists of actors and forces close to the company that can affect its ability to serve its customers, the company itself, marketing channel firms, customer markets, and the public at large. The macro-environment consists of the larger societal forces that affect the entire micro-environment, demographic, economic, natural, technological, political, competitor, and cultural forces.

Cooper et al (1999: 32) also says that all tourism and hospitality companies operate within a business environment consisting of many factors that the feasibility analyst should consider. Some of these factors are external to the company and thus largely out of management's control. Other factors are within a company and generally controllable by management. These micro- and macro-environmental factors are interrelated. For example, the relationship between a company and its intermediaries (micro-environmental) is affected by interest rates, an economic factor (macro-environmental).

The *micro-environment* consists of those factors that are within the immediate business environment of the company, and they can be controlled and influenced to some extent by the company. An example is the relationship between a company and its intermediaries. On the other hand, the *macro-environment* consists of the societal/global factors that affect a hotel company. These factors affect the buying behaviour of consumers, the hotel product offering and the company's marketing activity. This external business environment consists of demographic, political/legal, economic, geographical, socio-cultural, technological and natural factors. These factors are subject to continual change and the task of the hotel company is to adapt to these ever-changing forces. A company can, for instance, adapt to technological changes (by installing the latest computer software, for example). Some of these forces bring opportunities, such as a growing international tourism market; some of them bring threats to a company, such as social factors (high levels of crime in a region may deter international tourists). These factors are, however, largely out of the marketer's control.

George (2001: 36) adds a further dimension to the macro-environmental factors when categorising the macro-environmental factors that affect tourism and hospitality [hotel] companies, on four levels:

- At a *local* or destination level, for example, the population size of the provinces/states affect operations.
- On a *national* scale, for example, the income levels of South African households are a significant factor for all the tourism and hospitality companies operating in the country.

- At a *regional* level, for instance, political unrest in a neighbouring country could affect tourism demand at a national level.
- On a *global* or international scale, an economic recession in Asia, for example, could affect tourism and hospitality companies throughout southern Africa.

In addition to the macro-environment analysis a distinction needs to be drawn between domestic and international business. Taggart and McDermott (1993: 34) regard the environment of international business as the sum total of all the external forces working upon the firm as it goes about its affairs in foreign and domestic markets. The environment is often subdivided into two overlapping parts, the *operating environment* and the *remote environment*. The operating environment of the firm is, effectively, the industry within which it operates and includes factors such as labour markets, creditors, customers and competitors. As well as these factors influencing the firm, the operating environment is often, in turn, affected by the strategic decisions of individual firms. The remote environment includes all the factors which influence the firm but whose source is so remote that the strategic decisions and actions of even the largest firm have no noticeable effect on them. This category includes economic, financial, political, legal, cultural and technological factors.

Taggart and McDermott (1993) further explain that the environment can also be classified in another way, i.e. in terms of domestic, foreign and international spheres of impact. The domestic environment is clearly the most familiar to managers and consists of those uncontrollable external forces that affect the firm in its home market. However, it should be remembered that some of these factors (e.g. the cost of capital, export restrictions, etc.) could also have a significant effect on international operations. The foreign environment can be taken as those factors which operate in those other countries within which a multinational company (MNC) operates. Generally, the factors are the same, but they can have widely differing impacts compared the home-country situation. It is the scale of these differences that make any form of environmental forecasting such a difficult proposition for the MNC. Finally, the international environment is conceptualised as the interaction between domestic and foreign factors, and is thus very diverse indeed.

To conclude and in order to follow a clear unambiguous feasibility framework, for the remainder of this text, the marketing/development audit (table 6.5(a)) will form the basis of the hotel property feasibility analysis framework.

Subsequent to defining the strategic context and feasibility objectives in the hotel property development feasibility process (table 7.2(a)), the macro-environment feasibility is performed, followed by the physical, market and financial feasibilities. The reason for this priority order, i.e. macro-environment before physical, market and financial feasibilities, is because development initiatives seldom occur in poor macro-environmental conditions. Hence organisations would first consider the macro-environment of a proposed development, before considering any further actions.

Why the physical feasibility precedes the market feasibility is based on Rushmore and Baum's (2001: 29) advice that quite often considerable time is wasted when the market feasibility is performed before the physical feasibility, only to find that the location/site does not meet the requirements for the type of hotel development in mind.

Finally, all the preceding feasibility information culminates in the financial feasibility.

## 7.6 Strategic Context and Feasibility Objectives Brief (Step 1)

*“Establishing a complete and clear definition of the feasibility assignment is the first phase in all hotel feasibility studies and valuations. A clear definition is needed because a person cannot determine how to get somewhere until he or she has a specific destination. An analyst must understand the client’s needs before beginning data collection and analysis”* (Rushmore & Baum, 2001: 29).

The feasibility analyst, according to Wurtzebach and Miles (1994: 678), should begin by clearly stating the objectives of the organisation for which the feasibility is performed. These will be the dominant objectives in the study. However, the analyst needs to consider all the other stakeholders or participants as well. If the objectives of the stakeholders or other participants are not met, the project will most likely not go forward and will be less likely to succeed in the future.

Cloete (1995: 97) stresses that the objectives of the developer are of the utmost importance, as the feasibility of a project is evaluated by the extent to which these objectives are met.

Further to stressing the importance of the developer’s objectives, Cloete (1995) defines two main types of objectives:

- 1) **Economic objectives:** Optimising the use of resources in maximising the return on funds invested. The maximising of the return and the skill in being able to employ the optimum amount of capital in the development will result in a financially feasible development. The investment of capital in property provides a hedge against the erosion of the capital through inflation, but the primary objective is still the generation of an income stream.
- 2) **Social or other objectives:** The objective of governmental institutions is normally the improvement or optimisation of services.

From Rushmore and Baum, Wurtzebach and Miles, and Cloete’s opinions of what the starting point of a feasibility analysis should be, and previous sections pertaining to the subject hotel organisations’ strategic context, it could be postulated that the strategic context and feasibility objectives statement, step 1 of the feasibility process, should include the following important components:

- Organisational strategic context (refer to sections 6.2 and 6)
- Hotel operational objectives and parameters (refer to section 3.10, 5.3, 5.4 and 5.5)
- Development objectives and parameters (refer to section 5.2.1, 5.2.2 and 5.2.3)
- Economic objectives (refer to Cloete above)
- Social objectives (refer to Cloete above)

These departure objectives are imperative in directing the feasibility analysis and ultimately measure the feasibility results’ successes.



## **7.7 Macro-Environment Feasibility Analysis (Step 2)**

A tool available to the feasibility analyst to analyse the current macro environmental feasibility, is a PEST analysis, which is an analysis involving the examination of the external macro-environmental forces that may affect a company (George, 2001: 62). PEST stands for political, economic, socio-cultural, and technological forces.

### **7.7.1 Political Factors**

The direction and stability of political factors is a major consideration for feasibility analysts. Political factors define the legal and regulatory parameters within which firms must operate. Political constraints are placed on firms through fair-trade decisions, antitrust laws, tax programs, minimum wage legislation, pollution and pricing policies and many other actions aimed at protecting employees, consumers, the general public and the environment. Since such laws and regulations are most commonly restrictive, they tend to reduce the potential profits of firms. However, some political actions are designed to benefit and protect firms. Such actions include patent laws, government subsidies, and product research grants. Thus, political factors may either limit or benefit the firms they influence. For example, when Ethiopian Airlines was formed in 1945, it received assistance from TWA and the Ethiopian government. This support made Ethiopian Airlines one of the most successful members of the African air transport industry. The airline pioneered the hub concept in Africa and arranged its schedules to provide easy connections between many of the continent's countries, as well as between Africa and points in Europe, the Middle East and Asia. Without the political support of the Ethiopian government, it would have been impossible for the airline to operate. (Pearce & Robinson, 1994)

The feasibility analyst should focus on the political environment in the market(s) in which the company operates or hopes to operate. In some cases there may be political unrest and instability in current or proposed operating countries, which could affect the company.

As an example, according to George (2001: 319), South Africa will continue to become more politically acceptable as an international tourist destination. However, politics in Africa are very turbulent and can affect tourism and hospitality marketers' planning almost instantaneously. A civil war in a neighbouring country can affect the industry in South Africa.

It is likely that political instability in the region will constrain the development of tourism in various southern African countries.

While the economic and financial environments are of critical importance to the multi national companies (MNC), most international business activities are also influenced by the political environment. Taggart and McDermott (1993: 38) advise that almost from the beginning of multinational business operations, MNCs have been regarded as threats to national sovereignty, and while the zenith of this outlook probably occurred in the 1970s, it is still alive and flourishing in the 1990s. Naturally, different political ideologies will be reflected in different economic systems, with the People's Republic of China and the USA being at opposite ends of the spectrum. While the number of centrally planned economies has shrunk rapidly following the massive political changes in Eastern Europe, a new factor may be the rise of the fundamentalist Moslem approach to state management of the political and economic environments. Another facet of the political environment that has come to the fore in recent years has been the involvement of governments in different areas of business. For example, in virtually every industrialised country, the government controls

the postal services and the railways. During the 1980s, however, there has been a boom in privatisation, particularly in telecommunications, energy, steel and shipbuilding. Finally, the force of nationalism can never be ignored. While this was relatively dormant during the period 1975 to 1985, it has become a very potent factor in Europe, with a significant number of former Soviet client-states regaining sovereignty. Perhaps as a result, nationalism has also raised its profile within the European Community affecting, for example, Catalonia, Brittany, Belgium (Flemings and Walloons), Scotland and the Basque Country.

The principal concept used by international businessmen in appraising the political environment is known as political risk. This expresses itself through government-inspired events and actions that impact on the international companies working within a particular state. Weekly and Aggarwal (1987) define political risk as:

*'The risk of loss of assets, earning power, or managerial control due to events or actions that are politically based or politically motivated'.*

The immediate association of political risk is with developing countries, in terms of nationalisation and expropriation of assets, but it is also present in industrialised countries, as the following examples may demonstrate (Taggart and McDermott, 1993: 39):

- The election of conservative Prime Minister Thatcher in the United Kingdom in 1979
- The election of socialist President Mitterrand in France in 1981
- The accession of Portugal and Spain to the EC in 1986
- The reunification of Germany in 1990
- The great mass of political decisions by member states upon which the whole concept of the Single European Market (1992) rests
- The disintegration of the Soviet Union.

Perhaps the most difficult political risk assessment the MNC must make is when it contemplates its initial entry into a particular country. Taggart and McDermott (1993: 39) cite Daniels and Radebaugh's simple checklist for the primary appraisal:

- What is the political structure of the country?
- Under what type of economic system does the country operate?
- Is my industry in the public or private sector?
- If it is in the public sector, does the government also allow private competition in that sector?
- If it is in the private sector, is there any tendency to move it towards public ownership?
- Does the government view foreign capital as being in competition or in partnership with public or local private enterprises?
- In what ways does the government control the nature and extent of private enterprise?
- How much of a contribution is the private sector expected to make in helping the government formulate overall economic objectives?

If the situation is especially complex, or if the new foreign investment is very large, most MNCs would move beyond such a simple assessment and call on the assistance of specialist political risk assessment consultants, most of whom have had extensive previous experience working with or within government or international bodies like the UN or the World Bank.

Cooper et al (1999: 63) confirms that politics affect travel propensities, and consequently hotel development, in a variety of ways. For example, the degree of government involvement in promoting and providing facilities for tourism depends upon the political complexion of the government. Governments that support the free market try to create an environment in which tourism industries can flourish, rather than the administration being directly involved in tourism itself. Socialist administrations, on the other hand, encourage the involvement of the government in tourism and, through 'social tourism', often provide opportunities for the 'disadvantaged' to participate in tourism.

Governments in times of economic problems may control levels of propensity for travel overseas by limiting the amount of foreign currency that can be taken out of a country or demanding a monetary bond to be left in the country while the resident is overseas. Government restrictions on travel also include visa and passport controls as well as taxes on travel. Generally, however, these controls are not totally effective and, of course, they can be evaded.

We can also identify inadvertent political influences, for example, a government with an economy suffering high inflation may find that inbound travel is discouraged by the travel fraternity. In a more general sense, unstable political regimes (where civil disorder or war is prevalent) may forbid non-essential travel, and inbound tourism will be adversely affected.

According to Taggart and McDermott (1993: 40), the international legal environment within which multi national companies (MNCs) have to conduct operations could be regarded as a subset of the political environment, as the two are completely intertwined. Unfortunately for MNCs, they do not work within a single, unified international legal environment; on the contrary, an MNC faces a different legal context in every country within which it operates. These codes are usually put in place by governments in an attempt to control the amount, rate and impact of both outward and inward investment.

This large number of factors included could conveniently be classified as follows: (Taggart & McDermott, 1993: 40)

- *Industrial intellectual property rights:* This includes all aspects of trade names, trade secrets, copyrights and patents. As business has become progressively internationalised, so MNCs and their home governments have brought pressure to bear [particularly, but not solely] on developing countries to bring regulations into line with those of the industrialised countries.
- *Trade obstacles:* These include tariffs and quotas which are usually clearly laid down by regulations, and other less well-defined factors. A good example here is product labelling where the requirements are not only legal, but also culture-bound. For instance, foreign companies trading in France must produce all labels, warranties, instructions, etc. in French.
- *Product liability:* This has been a boom area for the legal profession in many industrialised countries in the last ten years, though this is hardly surprising when the long list of product manufacturing problems is considered. The pharmaceutical industry could be quoted as a case in point, although the most spectacularly disastrous example must be the Bhopal incident. In 1984, an explosion occurred at Union Carbide's plant at Bhopal in India, as a result of which poisonous emissions killed over 2,000 people. As a result, not only were Indian regulations tightened, but there was a wave of environmental legislation throughout the industrialised world.

- *Monopoly and restrictive trades practices:* This type of legislation is common throughout the developed world. U.S.A. regulations are regarded as tightest, followed by Germany. However, unlike other areas of legislation, there is a move towards uniformity here, with the European Community taking the lead in the approach to the Single European Market.
- *Home-country legislation:* This includes all legislation passed in a particular country to regulate the activities of MNCs based in that country while operating overseas. The best-known example is the U.S.A. Foreign Corrupt Practices Act which was passed following a number of highly publicised bribery cases in the 1970s involving American multinationals. It forbids US firms to give bribes or any other questionable payments anywhere in the world as these are regarded as ethically repugnant and bad for the international reputation of American business.

Many more examples of either macro- or micro-environmental political factors should be considered, as the following would indicate:

- Local, provincial and national authority policies
- Land use regulations (zoning)
- Building regulations
- Rent control
- Taxation legislation
- Labour legislation
- Health and food regulations, etc.

### **7.7.2 Economic Factors**

Economic factors concern the nature and direction of the economy in which a firm operates. Further to this statement Pearce and Robinson (1994: 64) say that because consumption patterns are affected by the relative affluence of various market segments, in its strategic planning each firm must consider economic trends in the segments that affect its industry. On both the national and international level, it must consider the general availability of credit, the level of disposable income, and the propensity of people to spend. Prime interest rates, inflation rates, and trends in the growth of the gross national product are other economic factors to be considered.

Until recently, the potential impact of international economic forces appeared to be severely restricted and was largely discounted. However, the emergence of new international power brokers has changed the focus of economic environmental forecasting. Among the most prominent of these power brokers are the European Economic Community (EEC, or Common Market), the Organisation of Petroleum Exporting Countries (OPEC), and coalitions of developing countries.

Taggart and McDermott (1993: 34) suggest that in the great majority of cases, economic factors are the most influential subset that the international manager has to consider in his analysis of the remote environment. In every nation and region in the world, the constant interplay of the factors of production (land, labour and capital) impact on the activity of all firms, both domestic and multinational. The importance of this interplay would be immediately obvious, for example, to the manager who visited Kowloon, Kuala Lumpur and Ho Chi Minh City on the same business trip. These basic factors of production are put together in different ways in different countries to affect the production, distribution and consumption of those goods and services that satisfy human wants and needs.

Critical as they are in the domestic context, economic parameters are even more significant in dealing with international markets, because the multi-national companies (MNC) manager is trying to evaluate many and varied national and regional economies. These are likely to exhibit a number of different themes, including the following:

- Differing rates of economic growth
- Improving or deteriorating balances of payment
- Various fiscal approaches, with governments increasing or decreasing the levels of spending and taxation
- A wide spectrum of monetary policies, where monetary stability and the increase or decrease in money supply are strategic elements in any government's armoury
- Whether price levels are showing inflationary or deflationary trends, and therefore whether price and wage controls may be enforced or relaxed
- The stage a country is at in the never-stationary business cycle, i.e. boom, depressions, recession, recovery, and back to prosperity again.

Thus it could be argued that these factors are even more important in international markets than they are at home. In taking business activities overseas, the MNC faces the problem of assessing and understanding many economies whose characteristics are likely to prove highly divergent. This point is immediately clear when we classify countries into economic types:

- The industrial market economies, primarily the developed nations of the Organisation for Economic Co-operation and Development (OECD). These are the major trading nations.
- The oil-exporting nations, which are also massive exporters of petro-dollars.
- Developing countries including industrialising countries like Brazil, Argentina, Hong Kong, Singapore and Taiwan.
- The newly independent nations of the former Comecon bloc, which are attempting to move rapidly from centrally planned to market economies.

In pursuing his economic analysis of international markets, the MNC manager has to remember that while the decisions and actions of his own firm are most unlikely to have an appreciable impact on the remote environment, the overall effect of all multinational activity is likely to be significant. There is a final list of economic indicators which the individual MNC is likely to scrutinise carefully before entering a market. These economic indicators include:

- The gross national product (GNP), GNP per capita, the rate of private (as opposed to public/governmental) investment
- The level of personal consumption (especially that made out of discretionary income), variations in unit labour costs
- The distribution of incomes as measured by total disposable income per household or disposable income per capita.

A society's level of economic development, says Cooper et al (1999: 66), is a major determinant of the magnitude of tourist demand because the economy influences so many critical and interrelated factors. One approach is to consider a simple division of world economies into the affluent 'North', where the countries are major generators and recipients

of both international and domestic tourism, and the poorer 'South'. In the latter, some countries are becoming generators of international tourism but mostly tourism is domestic, often supplemented by an inbound international flow of tourists. In fact, the economic development of nations can be divided into a number of phases, as detailed in table 7.7.2(a).

**Table 7.7.2(a): Economic Development and Tourism**

(Source: Cooper et al, 1999: 67)

<b>Economic stage</b>	<b>Some characteristics</b>	<b>Examples</b>
<b>Traditional society</b> Long-established land-owning aristocracy, traditional customs, majority employed in agriculture. Very low output per capita, impossible to improve without changing system. Poor health levels, high poverty levels.	<b>The undeveloped world</b> Economic and social conditions deny most forms of tourism except perhaps domestic VFR.	Parts of Africa, parts of southern Asia.
<b>Preconditions for take-off</b> Innovation of ideas from outside the system. Leaders recognise the desirability of change.	<b>The developing world</b> From the take-off stage, economic and social conditions allow increasing amounts of domestic tourism (mainly VFR).	Parts of South and Central America; parts of the Middle East, Asia and Africa.
<b>Take-off</b> Leaders in favour of change gain power and alter production methods and economic structure. Manufacturing and services expand.	International tourism is also possible in the drive to maturity. Inbound tourism is often encouraged as a foreign exchange earner.	
<b>Drive to maturity</b> Industrialisation continues in all economic sectors with a switch from heavy manufacturing to sophisticated and diversified products.		Mexico; parts of South America.
<b>High mass consumption</b> Economy now at full potential, producing large numbers of consumer goods and services. New emphasis on satisfying cultural needs.	<b>The developed world</b> Major generators of international and domestic tourism.	North America; Western Europe; Japan; Australia; New Zealand.

As a society moves towards the high mass consumption stage, a number of important processes occur. The balance of employment changes from work in the primary sector (agriculture, fishing, forestry) to work in the secondary sector (manufacturing goods) and the tertiary sector (services such as tourism). As this process unfolds, an affluent society usually emerges and the percentage of the population who are economically active increases from less than a third in the developing world to half or more in the high mass consumption stage. With progression to maturity, discretionary incomes increase and create demands for consumer goods and leisure pursuits such as tourism.

Other developments are closely linked to the changing nature of employment. The population is healthier and has time for recreation and tourism. Improving educational

standards and media channels, boost awareness of tourism opportunities, and transportation and mobility rise in line with these changes. Institutions respond to this increased demand by developing a range of leisure products and services. These developments occur in conjunction with each other until, at the high mass consumption stage, all the economic indicators encourage high levels of travel propensity. Clearly, tourism is a result of industrialisation and, quite simply, the more highly developed an economy, the greater the levels of tourist demand.

As more countries reach the drive to maturity or high mass consumption stage, so the volume of trade and foreign investment increases and business travel develops. Business travel is sensitive to economic activity, and although it could be argued that increasingly sophisticated communication systems might render business travel unnecessary, there is no evidence of this to date. Indeed, the very development of global markets and the constant need for face-to-face contact should ensure a continuing demand for business travel.

### **7.7.3 Socio-Cultural Factors**

To determine whether a development will be successful or not, the feasibility study takes all the relevant factors into account in order to establish whether the socio-cultural climate is favourable for the active and effective implementation of the development.

According to Pearce and Robinson (1994: 66) the social-cultural factors are the beliefs, values, attitudes, opinions and lifestyles of persons in the firm's external environment, as developed from cultural, ecological, demographic, religious, educational and ethnic conditioning. As social attitudes change, so too does the demand for various types of clothing, books, leisure activities and so on. Like other forces in the remote external environment, social forces are dynamic, with constant change resulting from the efforts of individuals to satisfy their desires and needs by controlling and adapting to environmental factors.

One of the most profound social changes in recent years has been the entry of large numbers of women into the labour market. This has not only affected the hiring and compensation policies and the resource capabilities of their employers, but it has also created or greatly expanded the demand for a wide range of products and services necessitated by their absence from the home. Firms that anticipated or reacted quickly to this social change offered such products and services as convenience foods, microwave ovens and day-care centres.

A second profound social change has been the accelerating interest of consumers and employees in quality-of-life issues. Evidence of this change is seen in recent employment contract negotiations. In addition to the traditional demand for increased salaries, workers demand such benefits as sabbaticals, flexible hours or four-day workweeks, lump-sum vacation plans and opportunities for advanced training.

A third profound social change has been the shift in the age distribution of the population. Changing social values and a growing acceptance of improved birth control methods are expected to raise the mean age of the U.S.A. population, which was 27.9 in 1970, to 34.9 by the end of the 20th century. This trend will have an increasingly unfavourable impact on most producers of predominantly youth-orientated goods and will necessitate a shift in their long-range marketing strategies. Producers of hair- and skin-care preparations already have begun to adjust their research and development to reflect anticipated changes in demand.

A consequence of the changing age distribution of the population has been a sharp increase in the demands made by a growing number of senior citizens. Constrained by fixed incomes, these citizens have demanded that arbitrary and rigid policies on retirement age be modified and have successfully lobbied for tax exemptions and increases in social security benefits. Such changes have significantly altered the opportunity-risk equations of many firms, often to the benefit of firms that anticipated the changes.

Socio-cultural forces are major influences in the marketing activities of tourism and hospitality companies. The marketing planner should assess such factors as:

- Changes in lifestyles and fashions, perhaps towards healthy eating and fitness
- Changes in family patterns away from traditional families of four towards single parent families
- Demographic shifts towards an ageing population
- Changes in types of holidays from package holidays to independent holidays
- The market's interest in eco-tourism. There might be a trend towards environmentally friendly destinations, hotels and restaurants.

Cooper et al (1999: 64) says that the levels of population growth, its development, distribution and density affect travel propensity, and consequently hotel development. Population growth and development can be closely linked to the stages of economic growth of a society by considering the demographic transition where population growth and development is seen in terms of four connected phases:

The **high stationary phase**: This corresponds to many undeveloped countries with high birth and death rates keeping the population at a fluctuating, but low level

The **early expanding phase**: Here high birth rates continue but there is a fall in death rates owing to improved health, sanitation and social stability. This leads to a population expansion characterised by young large families. Countries in this phase are often unable to provide for their growing populations and are gradually becoming poorer. Clearly tourism is a luxury that cannot be afforded although some nations are developing an inbound tourism industry to earn foreign exchange.

The **late expanding phase**: In this phase a fall in the birth rate is rooted in the growth of an industrial society and birth control technology. Most developing countries fit into the early expanding and late expanding phases. A transition to the late expanding phase parallels the drive to maturity.

The **low stationary phase**: This phase corresponds to the high mass consumption stage of economic development. Here birth and death rates have stabilised at a low level.

Population density has a less important influence on travel propensity than has the distribution of population between urban and rural areas. Densely populated rural nations may have low travel propensities owing to the level of economic development and the simple fact that the population is mainly dependent upon subsistence agriculture and has neither the time nor the income to devote to tourism. In contrast, densely populated urban areas normally indicate a developed economy with consumer purchasing power, giving rise to high travel propensity and the urge to escape from the urban environment.



The distribution of population within a nation also affects patterns, rather than high levels, of tourist demand. Where population is concentrated into one part of the country, tourism demand is distorted. This asymmetrical distribution of population is well illustrated in the U.S.A. where two-thirds of the population live in the eastern third of the country. The consequent east to west pattern of tourist focus (and permanent migrants) has placed pressure on the recreation and tourist resources of the western states.

Social changes since the Second World War in the developed world have changed travel demand patterns. Most of these countries are experiencing a slowing of the birth rate, with some having projections of population decline. This, combined with extensions in life expectancy, has created an ageing population.

The older generation in the 'third age' or 'grey panther' group is often made up of those who did not pay into pension schemes and consequently whose pension and benefits barely keep up with inflation. These groups and the unemployed are likely to adapt their lifestyle to basic activities and seek cheap travel activities. Other better off older people are able to travel outside the main season and offer the ideal target market for season extension.

Socio-cultural factors can be regarded as the sum total of attitudes, beliefs and lifestyles, say Taggart and McDermott (1993: 41). Thus the international manager must be aware of attitudes towards material culture, work and achievement, time, change, authority, family, decision-making and risk. Since this description includes a vast number of intangible factors, it should come as no surprise that the cultural environment of international business gives multinational company (MNC) managers so many problems. As host countries have come to resent the 'cultural imperialism' of so many MNCs, so these companies have come to realise, particularly in the last ten years, the critical importance of this area. Culture is all-pervasive, and represents a dilemma for both operating and strategic management. It is a truism of strategic management that any strategy which runs counter to the corporate culture is certain to fail. The same is true of an international strategy which runs counter to a national or regional culture, but the results of failure will become apparent even more quickly. The broad prescription for MNC managers is to avoid insensitivity toward, or ignorance of, the aspects of local culture which will have the greatest influence on commercial success in any particular country. This requires a high level of cultural awareness and a sufficient degree of cultural empathy, e.g. at the operational level, it demands a significant level of cultural training for expatriate managers before a new posting.

The question of language is crucial and arouses great sensitivity in many countries. While there is a trend toward the acceptance of English as the universal business language, MNC managers should be aware that such a presumption causes great offence in, for example, France. Non-verbal communication also has its pitfalls, with different elements having different intrinsic meanings, which could include the use of eye contact, touching, personal appearance, relative position between people having a discussion, bodily postures, distance apart, and non-verbal aspects of speech like accents and tones.

Host-country religion also has a fundamental part to play, with each major religion having an impact on the overall attitude to business. The so-called 'Protestant work ethic' is a noticeable feature of Christianity. However, not only is this rather obviously shared by Roman Catholics, but it also finds a resonance in Confucianism. MNCs operating in Islamic countries have to be keenly aware that Moslems pray at five specific times during the day, and that there must be no requirement to work during these intervals. The concept

of the (extremely) extended family is important to Hindus, and includes support of all family members in the business world. Thus MNC managers have to be extra sensitive to the problems of pay, promotion, discipline and dismissal. Buddhists lay little stress on material wealth, and so are much less susceptible to western methods of motivating the workforce. Animism is probably the oldest religion and is widespread in Africa and Latin America. The Animist puts all problems down to the action of evil spirits which must be exorcised, and this can cause some odd situations for the expatriate production manager who has to cope with the Animist response to defective quality, machine breakdowns, and industrial accidents.

Taggart and McDermott (1993: 43) give a useful checklist for the MNC managers as an aid to coping with international differences in culture:

- Be culturally prepared: forewarned is forearmed
- Learn the local language and its non-verbal elements
- Mix with host nationals, including socially
- Be creative and experimental without fear of failure
- Be culturally sensitive, do not stereotype or criticise
- Recognise complexities in the host culture
- Perceive yourself as a culture bearer and ambassador
- Be patient, understanding and accepting of your hosts
- Be most realistic in your expectations
- Accept the challenge of intercultural experiences.

Translating social change into forecasts of business effects is a difficult process, at best. Nevertheless, informed estimates of the impact of such alterations as geographic shifts in populations and changing work values, ethical standards and religious orientation can only help a strategising firm in its attempts to prosper.

#### **7.7.4 Technological Factors**

The fourth set of factors in the remote environment, says Pearce and Robinson (1994: 67), involves technological change. To avoid obsolescence and promote innovation, a firm must be aware of technological changes that might influence its industry. Creative technological adaptations can suggest possibilities for new products, improvements in existing products or in manufacturing and marketing techniques.

A technological breakthrough can have a sudden and dramatic effect on a firm's environment. It may spawn sophisticated new markets and products or significantly shorten the anticipated life of a manufacturing facility. Thus, all firms, and most particularly those in turbulent growth industries, must strive for an understanding both of the existing technological advances and the probable future advances that can affect their products and services. This quasi science of attempting to foresee advancements and estimate their impact on an organisation's operations, is known as technological forecasting.

Technological forecasting can help protect and improve the profitability of firms in growing industries. It alerts strategic managers to both impending challenges and promising opportunities.

The key to beneficial forecasting of technological advancement lies in accurately predicting future technological capabilities and their probable impacts. A comprehensive analysis of

the effect of technological change involves study of the expected impact of new technologies on the remote environment, on the competitive business situation, and on the business-society interface.

Cooper et al (1999: 77), asserts that there is no doubt that technology has been a major enabling factor in terms of converting suppressed demand into effective demand. This is particularly the case in terms of transport technology where the development of the jet engine in the late 1950s gave aircraft both speed and range and stimulated the variety of tourism products available in the international market to meet the demand for international travel. Developments in aircraft technology have continued but so has the level of refinement and access to the motorcar.

Similarly, the development of information technology is a critical enabling factor in terms of tourism demand. Generally, technology acts to increase access to tourism by lowering the cost or by making the product more accessible. Examples here include developments in 'recreational technology' such as windsurfers, durable outdoor clothing, heli-skiing and heli-hiking, and off-road recreational vehicles.

On the international front, according to Taggart and McDermott (1993: 43), technology is a critical aspect of MNC operations, and represents the single most important competitive advantage an international firm can possess. Not only does a suitable technological development within the MNC help domestic operations (as it would in any domestic firm), but the MNC can internationalise the advantage throughout its network of subsidiaries at very little extra cost. This is an increasingly important factor as the cost of technological advancement increases with each passing year. Technological changes lead to new products and new processes, and MNCs are highly effective at transforming this innovation into additional profits. In fact, it could be argued that innovation is the key to MNC success, the element that differentiates the MNC from its single-country domestic competition.

## **7.8 Macro Hotel Market Analyses**

*The following sections, 7.8.1, 7.8.2 and 7.8.3 draw primarily from Rushmore and Baum (2001), hence only where other authors' text is included will the quotation or citation be highlighted.*

These sections include a considerable amount of U.S.A macro tourism/travel/hotel market statistics, serving to illustrate the wide range of information required for a comprehensive and valid feasibility study, and are not intended to focus this text on the U.S.A market only.

Please note, because the following statistics pertain to the U.S.A, their standard/units for measurement are used, e.g. miles, feet and inches, as opposed to the metric system.

### **7.8.1 Macro Demand for Transient Accommodation**

Much of the macro data relating to travel in general and hotel demand in particular is compiled by government and industry organisations. This type of data can be divided into four categories based on its ability to reflect trends in hotel demand.

*Category 1* consists of information pertaining to the actual use of commercial accommodation. This data relates to the number of travellers actually using hotels and is a direct measure of lodging demand. They most clearly indicate the current status of the hotel

industry because the data requires little interpretation. Examples of category 1 data would include a survey of the number of travellers using hotel accommodation during their trips and quantification of the occupied hotel rooms within a specific macro market over a certain period of time.

**Category 2** information pertains to travel that may entail the use of commercial accommodation. This type of data does not directly reflect demand for transient accommodation, but rather, provides a basis for drawing inferences that could lead to supportable estimates. Examples of category 2 data include information on the amount of airline travel, attendance at recreational attractions and the number of travellers in general.

**Category 3** data indicates the general condition of the national economy and describes the broad demographic trends that can indirectly impact on the use of commercial accommodation. Like category 2 data, this type of data does not directly reflect the demand for commercial accommodation, and only indirect inferences can be drawn. Examples of category 3 data include statistics on population growth and disposable income and various types of economic trend indicators. (*Refer to sections 7.7.2(Macro economic factors) and 7.7.3 (Macro socio-cultural factors)*)

**Category 4** information details specific characteristics of transient travel demand (i.e. reasons for travel, types of accommodation selected, length of stay, and size of party). This data is used to evaluate the relative competitiveness of various types of hotels within a specific market.

The best type of data for quantifying hotel demand, evaluating historic trends and formulating projections, is category 1 data. This type of data can be obtained nationally from government administered sources charged with the task of tracking travel data of all sorts. On a regional or micro level, most analysts/appraisers develop their own information on the specific market areas surrounding their subject properties and then augment their findings with competitive data provided by private researchers/consultants, such as Smith Travel Research. Category 2 data is also readily available nationally but is sometimes difficult to obtain on the micro level.

Category 3 data covering most micro markets is available from many sources. Appraisers/analysts often use this type of data as a basis for forecasting future trends in hotel demand once a base level has been quantified through primary research techniques. Category 4 data is available on a macro basis, but micro market data can sometimes be obtained from public sources.

#### **7.8.1.1 Total Trips and Person Trips**

The primary unit of travel demand used by the U.S. Travel Data Centre is the “trip.” Each trip unit represents the number of times a member or members of a household travel to a place at least 100 miles from home, one way, and then return. A “person-trip” is a unit of measure that accounts for the number of persons on a trip. If three persons from a household go together on one trip, their travel is counted as one trip and three person-trips. Therefore, the average party size can be calculated by dividing the number of trips by the number of person-trips. This type of category 2 data, for the period 1987 to 1997 is illustrated in table 7.8.1.1(a).

**Table 7.8.1.1(a): Person Trips and Party Size Statistics**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 79)

Year	Total Trips (Millions)	Percent Change	Person-Trips (Millions)	Percent Change	Party Size (People)
1987	567.3	-	893.5	-	1.58
1988	584.9	3.1%	924.5	3.5%	1.58
1989	592.2	1.2	945.2	2.2	1.60
1990	589.4	(0.5)	956.0	1.1	1.62
1991	592.4	0.5	980.1	2.5	1.65
1992	650.7	9.8	1,063.0	8.5	1.63
1993	648.2	(0.4)	1,057.5	(0.5)	1.63
1994	665.3	2.6	1,139.1	7.7	1.71
1995	669.7	0.7	1,172.6	2.9	1.75
1996	682.8	2.0	1,161.2	(1.0)	1.70
1997	715.9	4.8	1,256.1	8.2	1.75
<b>Annual Compounded Percent Change</b>					
1987 - 1997		2.4%		3.5%	
1990 - 1997		2.8		4.0	

Between 1987 and 1997, the number of trips increased at an average annual compounded percentage rate of 2.4%. This growth rate accelerated slightly to 2.8% between 1990 and 1997. The strongest rate of expansion was recorded in 1992, when trips increased by 9.8%, while 1997 also saw an above-average rate of expansion equal to 4.8%. As for person-trips, this indicator increased at an average annual compounded percentage rate of 3.5% between 1987 and 1997. The rate of growth accelerated again between 1990 and 1997, when travel volume increased at an average compounded rate of 4.0% per year. Since mid-1992 the national economy has been expanding, driving stronger rates of growth for the decade than have been recognised over the long term. Most industry experts tend to consider an annual growth rate of 2% a reasonable benchmark for evaluating projected demand growth for a given market. Whenever an analyst uses a higher demand growth rate, it must be recognised that such an estimate exceeds long-term national averages. Thus, the applied growth rate should be justified by favourable local economic and demographic data.

Table 7.8.1.1(a) also illustrates the trends in increasing party size, where the average number of household members per trip has grown from 1.58 in 1987 to 1.75 in 1997. This dynamic resulted in rapid growth among person-trips relative to trips. Just as the rate of travel has increased since 1987, the size of travelling parties has also expanded.

### 7.8.1.2 Purpose of Trip

The U.S. Travel Data Centre also reports total travel demand as categorised by the purpose of each trip. Table 7.8.1.2(a) shows trends in trip volume for four separate categories of travel, including business, pleasure, vacation, and weekend trips. Total trip volume is presented again for context. Because a given trip may have multiple purposes, the total of the four travel categories exceeds the number of total trips.

Between 1982 and 1997, business trips increased at an average annual compounded percentage rate of 3.7%. Between 1990 and 1997, the rate of growth decelerated to 1.8% per year, while the year-to-year changes demonstrated significant volatility. Business travel volume decreased in 1990, 1991, 1993, 1994, and 1996. These declines were offset, however, by strong gains in 1992, 1995, and 1997.

Unlike the trends noted in business travel, pleasure travel volume accelerated in the 1990s. Whereas the rate of growth between 1982 and 1997 equated to 2.8%, the growth rate between 1990 and 1997 equated to 3.0%. Like business trips, the number of pleasure trips surged in 1992. The number of pleasure trips declined in 1995 but grew consistently over the historical period.

**Table 7.8.1.2(a): National Travel Volume Segmented by Purpose of Trip**

(Source: U.S Travel Data Centre as reproduced by Rushmore and Baum, 2001: 80)

Year	Business Trips (Million)	Percent Change	Pleasure Trips (Million)	Percent Change	Vacation Trips (Million)	Percent Change	Weekend Trips (Million)	Percent Change	Total Trips (Million)	Percent Change
1982	119.7	-	291.2	-	-	-	-	-	479.0	-
1983	121.7	1.7	291.0	(0.1)	-	-	-	-	482.2	0.7
1984	134.5	10.5	275.0	(5.5)	-	-	-	-	470.9	(2.3)
1985	156.6	16.4	301.2	9.5	-	-	-	-	497.8	5.7
1986	164.4	5.0	325.3	8.0	-	-	-	-	528.0	6.1
1987	185.0	12.5	348.6	7.2	285.0	-	-	-	567.3	7.4
1988	182.8	(1.2)	356.7	2.3	308.4	8.2	-	-	584.9	3.1
1989	199.3	9.0	358.3	0.4	324.4	5.2	-	-	592.2	1.2
1990	182.8	(8.3)	361.1	0.8	328.7	1.3	263.7	-	589.4	(0.5)
1991	176.9	(3.2)	364.3	0.9	327.7	(0.3)	299.8	13.7	592.4	0.5
1992	210.8	19.2	411.7	13.0	352.8	7.7	340.3	13.5	650.7	9.8
1993	210.4	(0.2)	413.4	0.4	352.2	(0.2)	330.0	(3.0)	648.2	(0.4)
1994	193.2	(8.2)	434.3	5.1	343.4	(2.5)	315.2	(4.5)	665.3	2.6
1995	207.8	7.6	413.0	(4.9)	349.7	1.8	317.5	0.7	669.7	0.7
1996	192.8	(7.2)	432.5	4.7	375.5	7.4	332.4	4.7	682.8	2.0
1997	207.4	7.6	443.2	2.5	388.6	3.5	353.5	6.3	715.9	4.8
<b>Annual Compounded Percentage Change</b>										
1982 - 1997		3.7		2.8		-		-		2.7
1987 - 1997		1.1		2.4		3.1		-		2.4
1990 - 1997		1.8		3.0		2.4		4.3		2.8

Vacation trip data is only available for the years between 1987 and 1997. Over this period the number of vacation trips increased at an average annual compounded percentage rate of 3.1% (the rate of growth decelerated slightly to 2.4% between 1990 and 1997). Data for weekend trips is only available for the years between 1990 and 1997, but they showed that weekend trips increased at an average annual compounded percentage rate of 4.3% over this period. The stronger rate of growth in weekend trips in recent years is tied to a national trend towards more frequent, yet shorter, vacations. Instead of taking extended vacations, Americans are taking more three-day weekends. Destination resorts near metropolitan centres have benefited from this change and commonly offer mini-vacations and weekend packages to capitalise on it.

Overall, these historical trends indicate that gains in pleasure-related trips (including vacations and weekend trips) outpaced gains in business trips, although trends for each variety of travel have been positive.

### 7.8.1.3 Hotel Trips

Table 7.8.1.3(a) explains the historical trip volume statistics for travellers using hotels and motels during the years 1982 to 1997. These statistics, however, pertain only to trips involving hotel and motel usage. Because these statistics do not account for the trip's duration, the data does not necessarily correlate to hotel room nights occupied.

Between 1982 and 1997 trips involving hotel/motel stays increased at an average annual compounded percentage rate of 3.6%. The rate of growth, however, slowed to 2.0% between 1990 and 1997. Offsetting declines in 1994, 1995, and 1997, hotel/motel trips surged in 1992 and 1996.

Again, the number of hotel/motel trips does not necessarily correlate to hotel room nights occupied. In 1997 the number of hotel/motel trips declined slightly, by 0.1%, although the number of occupied room nights rose that year owing to an increase in the average length of stay. Smith Travel Research (STR), the leading independent research firm serving the U.S.A. hotel industry, estimated the gain in 1997 occupied room nights to be roughly 3.0%. More extensive data provided by STR will be detailed later in this text.

**Table 7.8.1.3(a): Trips Involving Motel/Hotel Usage**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 82)

Year	Hotel/Motel Trips (Millions)	Percent Change	Year	Hotel/Motel Trips (Millions)	Percent Change
1982	197.2	-	1992	325.8	11.9%
1983	206.3	4.6%	1993	329.5	1.1
1984	215.3	4.4	1994	318.5	(3.3)
1985	224.2	4.1	1995	316.4	(0.7)
1986	247.9	10.6	1996	334.0	5.6
1987	282.1	13.8	1997	333.6	(0.1)
1988	273.3	(3.1)	<b>Annual Compounded Percent Change</b>		
1989	290.5	6.3	1982 - 1997		3.6%
1990	291.0	0.2	1990 - 1997		2.0
1991	291.1	0.0			

Additional characteristics associated with hotel/motel trips identified by the U.S. Travel Data Centre are:

- 79% of travellers had one overnight destination; the remaining 21% had multiple destinations
- 66% of trips involved travellers arriving by car, truck, or recreational vehicle (RV); 31% arrived by air
- 54% of the trips involved only one household member; 28% of the trips involved two household members
- 54% of the trips were pleasure-related; business was identified as the main purpose of 42% of the trips
- 53% of the trips were described as a vacation
- The average length of the hotel/motel stay was 3.4 nights
- 51% of the trips involved overnight weekend travel
- For 24% of the trips, a travel agent was consulted; 20% of the trips were booked through a travel agent
- A car was rented for 22% of the trips
- 19% of the trips included a child
- The average round-trip distance was 1159 miles.

### 7.8.1.4 Characteristics of Trips

The U.S. Travel Data Centre also compiles category 4 data on trip characteristics. Table 7.8.1.4(a) shows the typical characteristics of different types of trips based on the trip's purpose and the traveller's age. Note that each of the categories is analysed based on person-trips, with the exception of the hotel category.

**Table 7.8.1.4(a): Person-Trip Characteristics – 1997, USA**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 83)

Total	Total	Busi ness	Pleasure	Vaca tion	Weekend	Hotel	Age Distribution			
							<18	18 - 34	35 - 54	55+
Base (millions)	1,256.1	275.5	862.4	751.8	656.0	333.6	214.4	361.0	431.3	249.4
<b>Type of Lodging</b>										
Hotel or motel	45%	64%	39%	46%	47%	100%	40%	44%	51%	42%
Friends', relatives' homes	34	16	40	38	40	8	41	40	27	35
Camper, trailer, or RV	4	2	5	5	5	*	5	4	3	5
Owned cabin or condo	3	1	4	4	3		2	2	2	5
Rented cabin or condo	3	3	3	5	3	1	5	3	3	3
Other	5	3	4	5	5	1	3	5	5	5
No overnight stay	11	14	10	5	0	0	11	8	13	13
Average friends/ relatives (nights)	3.9	3.6	3.8	4.4	2.6	4.2	3.8	3.6	3.4	4.6
Average hotel /motel (nights)	3.5	3.4	3.5	3.8	2.5	3.4	3.4	3.4	3.3	3.9
<b>Main Purpose of Trip</b>										
Pleasure travel (net)	71%	0%	100%	89%	78%	54%	83%	73%	62%	70%
Visit friends/relatives	36	0	51	41	41	17	44	39	27	37
Entertainment	24	0	34	33	25	28	26	22	24	24
Outdoor recreation	11	0	15	15	12	8	13	11	11	9
Business travel (net)	23	100	0	9	16	42	11	22	31	22
Business (unspecified)	14	60	0	1	7	30	4	14	21	12
Convention, seminar, meeting	2	9	0	1	2	4	1	2	3	3
Combined business/pleasure	7	30	0	7	7	8	6	6	8	6
Personal business	*	1	0	*	0	*	*	*	*	1
Other	6	0	0	2	6	4	6	5	7	8
Vacation travel	60%	24%	75%	100%	66%	53%	69%	64%	53	57%
Overnight weekend travel	52%	36%	58%	58%	100%	51%	57%	56%	52%	43%
Friday night	8	7	8	8	N/A	9	8	8	8	7
Saturday night	10	7	11	10	N/A	10	11	10	11	8
Both Friday and Saturday nights	34	22	39	40	N/A	32	37	38	33	28
<b>Round-Trip Distance</b>										
200—299 miles	22%	18%	22%	18%	23%	15%	22%	19%	22%	21%
300—399 miles	15	14	16	15	18	12	18	16	15	14
400—599 miles	18	17	19	18	21	16	20	20	16	17
600—999 miles	14	15	14	15	14	16	12	14	16	13
1,000—1,999 miles	14	16	13	15	12	17	15	14	13	14
2,000milesormore	12	15	10	13	8	17	9	11	12	15
Outside U.S.	5	5	6	6	4	7	3	5	5	6
Average round-trip distance (miles)	939	1,084	872	992	802	1159	825	932	950	1,004



**Table 7.8.1.4(a): Person-Trip Characteristics – 1997, USA (Continued)**

(Source: Rushmore and Baum, 2001: 84)

Total	Total	Busi- ness	Pleasure	Vaca- tion	Weekend	Hotel	Age Distribution			
							<18	18 - 34	35 - 54	55+
Base (millions)	1,256.1	275.5	862.4	751.8	656.0	333.6	214.4	361.0	431.3	249.4
<b>Primary Mode of Transportation</b>										
Auto/truck/RV/rental car	79%	65%	84%	80%	85%	66%	89%	79%	75%	78%
Airplane	18	33	13	17	13	31	9	17	23	18
Bus	1	1	1	1	1	2	1	2	1	2
Train	1	*	1	1	1	1	1	1	1	1
Other	1	*	1	1	*	*	*	1	1	2
<b>Trip Duration</b>										
No nights	12%	14%	10%	5%	0%	0%	11%	8%	13%	13%
One night	16	19	15	12	18	19	15	17	16	15
2 or 3 nights	39	36	41	40	58	43	38	42	40	33
4 to 9 nights	27	25	27	34	24	30	29	27	25	29
10 nights or more	7	6	7	9	0	8	7	6	6	10
Average duration (excludes 0 nights)	4.1	3.9	4.1	4.7	2.6	4.1	4.0	3.9	3.8	5.1
Average duration (includes 0 nights)	3.7	3.3	3.7	4.4	N/A	N/A	3.6	3.5	3.3	4.4
<b>Number of Destinations</b>										
No overnight destinations	12%	13%	10%	5%	0%	0%	11%	8%	13%	13%
One destination	75	72	77	79	91	79	75	81	74	70
Two destinations	9	8	9	10	7	14	10	8	9	10
Three or more destinations	4	6	4	6	2	7	4	3	4	7
Average number of nights per destination	3.2	3.0	3.0	3.4	2.3	2.9	3.1	3.0	2.9	3.6
<b>Census Region of Destination</b>										
South Atlantic	19%	20%	20%	21%	18%	21%	19%	20%	22%	17%
Pacific	13	15	13	14	14	14	14	13	13	13
East North Central	13	13	13	12	14	12	14	14	14	12
West South Central	11	12	10	9	11	10	12	12	10	10
Mountain	11	11	10	11	10	12	10	9	0	12
Mid-Atlantic	9	9	10	9	10	8	8	11	8	10
West North Central	8	7	8	7	8	6	9	7	7	8
East South Central	7	6	7	6	7	6	7	6	6	8
New England	4	3	4	4	4	4	3	4	4	4
Outside U.S.	5	5	5	7	4	7	3	5	5	6
<b>Number of Household Members on Trip</b>										
One **	53%	71%	45%	46%	48%	54%	2%	43%	34%	38%
Two	28	17	31	30	30	28	12	26	32	55
Three	11	7	13	13	12	10	33	16	19	6
Four	6	3	8	8	8	6	37	12	11	1
Five or more	2	2	3	3	2	2	16	3	4	*
Average	1.8	1.5	1.9	1.9	1.9	1.8	3.5	2.1	2.2	1.7
Child from household on trip	21%	12%	25%	24%	23%	19%	100%	28%	35%	4%
*Less than 0.5%										
** Includes those who travel alone or with someone from outside the household										

Weekend and pleasure travellers tend to cover the shortest distances in the course of their trips. Business and vacation travellers generally cover longer distances, and such trips are more likely to require the use of a hotel. In addition, older travellers are more likely to travel farther than younger travellers. The average round-trip distances ranged from a low

of 802 miles among weekend travellers to a high of 1,159 miles among travellers using a hotel.

In terms of the mode of transportation, each category of traveller is most likely to arrive via a car, truck, recreational vehicle (RV), or rental car. However, weekend and pleasure travellers and travellers younger than 18 are more likely than other travellers to use these modes of transportation. Air travel is most common for business travellers, travellers requiring a hotel, and travellers between the ages 35 and 54.

Travellers older than 55 posted the longest average trip length, with an average stay (excluding trips that require no overnight stay) of 5.1 nights. Vacationers posted a similarly high average trip length of 4.7 nights. Weekend travellers, who reported an average trip length of 2.6 nights, posted the lowest indication. Travellers using hotels and motels reported an average trip duration of 4.1 nights, equal to the average for all trips. As for the number of destinations per trip, vacationers, travellers using hotels, and travellers older than 55 were most likely to have multiple destinations.

Business travellers are the most likely to require a hotel or motel during their trips. Whereas 45% of all trips required hotels or motels in 1997, 64% of business trips required hotels or motels. Vacationers, weekend travellers and travellers between ages 35 and 54 also used hotels and motels more often than average in 1997. The average length of the hotel stay equated to 3.4 nights in 1997, with the duration of the stays exceeding this average for pleasure travellers, vacationers, and travellers aged 55 and older.

As for the purpose of travel, 71% of all travellers reported that their trip was for pleasure, whereas 23% of all travellers reported a business purpose. In contrast, of all those travellers who used hotel facilities on their trip, 54% had a pleasure-related purpose, while 42% had a business-related purpose. Otherwise, travellers aged 35 to 54 were more likely than other age groups to have a business-related trip.

Of all trips surveyed, 60% included a vacation component. Categories for which this average was exceeded included pleasure travellers, vacationers, weekend travellers and travellers under the age of 18 as well as travellers between ages 18 and 34. Overnight weekend travel was identified as a component of 52% of all trips, where an above average indication was noted in the following categories: pleasure, vacation, weekend, travellers under the age of 18, and travellers between ages 18 and 34.

Every category surveyed, identified the South Atlantic as the most common region of destination, with vacationers, travellers using hotels, and travellers aged 35 to 54 noting particularly high visitation to the South Atlantic. Business travellers reported the highest ratio of total travel to the Pacific region.

In terms of the number of household members on the trip, 53% of all trips involved a single member of the household, while the ratio for business travel was 71%. The average number of household members for all trips was 1.8, with business-related trips reporting an average of 1.5 household members per trip. Trips involving a traveller under age 18, reported an average of 3.5 household members, whereas trips involving a traveller aged 55 or older reported an average of 1.7 household members. A child was included in 21% of all trips, while 19% of trips involving hotel facilities included a child.

### 7.8.1.5 Travel Trends by Gender

The U.S. Travel Data Centre also analysed travel characteristics as differentiated by gender. Table 7.8.1.5(a) identifies the results of this survey.

Differences in travel trends among males and females have narrowed significantly in recent years. As of 1997, the greatest disparities were realised in the share of business- and vacation-related person-trips. Less than 10 percentage points differentiated all other categories.

**Table 7.8.1.5(a) Comparison of Travel Characteristics by Gender – 1997**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 85)

Characteristic	% of Person-Trips		
	Men	Women	Difference
Business trips	28%	17%	11 points
One person from household	37	28	9
Midweek travel	21	15	6
Hotel/motel use	48	43	s
Rental car use	15	10	5
Consulted travel agent	15	11	4
Travel by air	19	16	3
Vacation	55	65	(10)
Visiting friends/relatives	32	40	(8)
Child on trip	33	40	(7)
Overnight weekend	49	55	(6)

### 7.8.1.6 Month of Travel

Table 7.8.1.6(a) identifies month of travel statistics for 1996 and 1997. As indicated, travel is generally more concentrated in summer months (Northern Hemisphere). July and August represent peak national travel times. Travel volume declines significantly in January and February, but is generally consistent throughout the remainder of the year.

**Table 7.8.1.6(a) Month of Travel 1996 and 1997**

(Source: U.S. Travel Data as reproduced by Rushmore and Baum, 2001: 87)

Month	1996	1997
January	6%	7%
February	6	6
March	8	8
April	9	8
May	9	8
June	9	8
July	10	11
August	9	10
September	9	9
October	9	9
November	7	8
December	9	8
Total	100%	100%

### 7.8.1.7 Payroll Employment

Another way to gauge hotel-motel demand is to look at the number of people employed in the hotel-motel industry. Table 7.8.1.7(a) identifies the total number of people employed in the nation's hotels and other lodging facilities between 1972 and 1998.

Between 1972 and 1998, employment levels in hotels and other lodging facilities increased at an average annual compounded percentage rate of 3.1%. The strongest rate of growth over this historical period was realised in the 1980s, when hotel employment increased at an average annual compounded percentage rate of 7.2%. Hotel supply increased dramatically throughout the 1980s, and a recession in the early 1990s contributed to the significantly slower rate of hotel employment growth between 1990 and 1998. As indicated, hotel employment levels declined in 1991 and 1992. Since 1992, hotel employment growth has stayed relatively consistent, between 1.2% and 2.8% per year.

**Table 7.8.1.7(a): U.S.A. Employment – Hotels and Other Lodging Places**

(Source: Bureau of Labour Statistics as reproduced by Rushmore and Baum, 2001: 88)

Year	Total Hotel Employment (Thousands)	Percent Change	Year	Total Hotel Employment (Thousands)	Percent Change
1972	813.1	-	1988	1 540.1	5.2%
1973	854.2	5.1%	1989	1 595.8	3.6
1974	877.7	2.8	1990	1 631.1	2.2
1975	898.4	2.4	1991	1 589.4	(2.6)
1976	929.4	3.5	1992	1 576.4	(0.8)
1977	956.1	2.9	1993	1 595.7	1.2
1978	988.0	3.3	1994	1 630.9	2.2
1979	1 059.8	7.3	1995	1 630.9	2.3
1980	1 075.8	1.5	1996	1 715.0	2.8
1981	1 118.7	4.0	1997	1 745.7	1.8
1982	1 132.9	13	1998	1 775.8	1.7
1983	1 171.5	3.4	<b>Annual Compounded Percent Change</b>		
1984	1 262.8	7.8	1972 - 1998		3.1%
1985	1 331.3	5.4	1972 - 1980		3.6
1986	1 377.8	3.5	1980 - 1990		7.2
1987	1 464.2	6.3	1990 - 1998		0.9

### 7.8.1.8 Modes of Transportation

Other useful category 2 data includes statistics relating to the usage of different modes of transportation. When evaluating trends in lodging industry demand, data about air and car travel are most relevant. Table 7.8.1.8(a) sets forth the volume of American air and car travel between 1982 and 1997.

Between 1982 and 1997, air travel volume increased at an average annual compounded percentage rate of 3.8%. However, this growth rate decelerated to 2.0% annually between 1990 and 1997. Growth trends for air travel have been volatile, particularly in the 1990s. Air travel volume surged by roughly 28% in 1992, then plummeted in 1994. Car travel volume has increased more consistently. Between 1982 and 1997, car travel increased at an average annual compounded percentage rate of 2.5%, accelerating to a 3.1% growth rate between 1990 and 1997.

The data in Table 7.8.1.8(a) was gathered by the U.S. Travel Data Centre and based on travel surveys. Additional information on airline passenger traffic is published by the Air

Transport Association and based on actual airline usage. Table 7.8.1.8(b) shows airline travel statistics, including revenue passengers enplaned (i.e., boarding an aeroplane) and the number of miles flown, between 1980 and 1998.

**Table 7.8.1.8(a): National Travel Volume Segmented by Mode of Transportation**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 89)

Year	Air Travel (Millions)	Percent Change	Automobile Travel (Millions)	Percent Change
1982	91.2	-	366.5	-
1983	112.0	22.8%	349.2	(4.7)%
1984	114.5	2.2	335.8	(3.8)
1985	135.4	18.3	331.6	(1.3)
1986	138.2	2.1	357.6	7.8
1987	154.9	12.1	382.4	6.9
1988	149.0	(3.8)	416.7	9.0
1989	149.0	0.0	423.0	1.5
1990	139.7	(6.2)	426.7	0.9
1991	130.6	(6.5)	437.5	2.5
1992	166.7	27.6	455.6	4.1
1993	169.0	1.4	455.8	0.0
1994	135.8	(19.6)	502.7	10.3
1995	147.9	8.9	500.1	(0.5)
1996	145.4	(1.7)	511.9	2.4
1997	160.5	10.4	530.1	3.6
<b>Annual Compounded Percent Change</b>				
1982 - 1997		3.8%		2.5%
1990 - 1997		2.0		3.1

**Table 7.8.1.8(b): Airline Passenger Traffic**

(Source: Air Transport Association as reproduced by Rushmore and Baum, 2001: 90)

Year	Revenue Passengers Enplaned (Thousands)	Percent Change	Revenue Passenger Miles (Thousands)	Percent Change
1980	296,903	-	255,192,114	-
1981	285,976	(3.7)%	248,887,801	(2.5)%
1982	294,102	2.8	259,643,870	4.3
1983	318,638	8.3	281,829,148	8.5
1984	344,683	8.2	305,115,855	8.3
1985	382,022	10.8	336,403,021	10.3
1986	418,946	9.7	366,545,855	9.0
1987	447,678	6.9	404,471,484	10.3
1988	454,614	1.5	423,301,559	4.7
1989	453,692	(0.2)	432,714,309	2.2
1990	465,560	2.6	457,926,286	5.8
1991	452,301	(2.8)	447,954,829	(2.2)
1992	475,108	5.0	478,553,708	6.8
1993	488,520	2.8	489,648,421	2.3
1994	528,848	8.3	519,381,688	6.1
1995	547,773	3.6	540,656,211	4.1
1996	581,234	6.1	578,663,005	7.0
1997	599,131	3.1	605,573,543	4.7
1998	614,168	2.5	619,455,758	2.3
<b>Annual Compounded Percent Change</b>				
1980 - 1998		4.1%		5.1%
1990 - 1998		3.5		3.8

Between 1980 and 1998, the total number of passengers enplaned increased at an average annual compounded percentage rate of 4.1%. This rate of growth decelerated slightly to

3.5% between 1990 and 1998. Over the historical period, passenger volume decreased only in 1981, 1989, and 1991.

Between 1980 and 1998, passenger miles increased at an average annual compounded percentage rate of 5.1%, with the rate of growth decelerating to 3.8% between 1990 and 1998. The rates of growth for passenger miles have historically exceeded the rates of growth for passenger volume, indicating that the average distance travelled has also increased. This dynamic represents a positive trend for the hotel industry, as longer trips are more likely to require hotel stays.

An analysis of statistics on various modes of travel shows the relative importance of each. The automobile is by far the predominant means of transportation within the United States. It is also the primary means by which guests access lodging facilities. Air travel is second in importance, followed by bus and rail.

Table 7.8.1.8 (c) summarises the historical growth rates indicated in the preceding text, where such growth rates were indicated by the U.S. Travel Data Centre findings. The growth rates generally indicate stronger expansion rates over the longer historical period, with decelerating growth indicated in the 1990s. These trends are chiefly a result of the early 1990s economic recession.

**Table 7.8.1.8(c): Rates of Growth among Types of Travel**

(Source: U.S. Travel Data Centre as reproduced by Rushmore and Baum, 2001: 91)

Category	Annual Compounded Percentage Change 1982 - 1997	Annual Compounded Percentage Change 1990 - 1997
Business	3.7%	1.8%
Pleasure	2.8	3.0
Vacation	-	0.4
Weekend	-	4.3
Air	4.1	3.5
Automobile	5.1	3.8
Hotel	3.6	2.0

### 7.8.1.9 International Travel

Because travel is becoming more global, pertinent statistics pertain to visitors to the United States from foreign countries. Table 7.8.1.9(a) identifies historical trends in visitation from Mexico, Canada, and other countries between 1980 and 1997.

Between 1980 and 1997, travel to the United States from Mexico increased at an average annual compounded percentage rate of 5.8%, decelerating to 2.2% between 1990 and 1997. Travel to the United States from Canada increased at an average annual compounded percentage rate of 1.7% between 1980 and 1997, but receded at an average annual rate of 1.9% between 1990 and 1997. Significant declines were noted between 1993 and 1995, when the value of the Canadian dollar weakened relative to the American dollar. Among other countries growth has remained strong and consistent historically, with an average annual percentage growth rate of 7.1%. Overall, arrivals in the United States from foreign countries increased at an average annual compounded percentage rate of 4.6% between 1980 and 1997, with the rate of growth decelerating to 2.8% between 1990 and 1997.

**Table 7.8.1.9(a): International Travel to the United States of America**

(Source: U.S. Travel &amp; Tourism Administration as reproduced by Rushmore and Baum, 2001: 92)

Year	Mexican (Million)	Percent Change	Canadian (Million)	Percent Change	Other (Million)	Percent Change	Total (Million)	Percent Change
1980	3.2	-	11.4	-	7.6	-	22.2	-
1981	3.8	18.8%	10.9	(4.4)%	8.8	15.8%	23.5	5.9%
1982	2.6	(31.6)	10.4	(4.6)	8.5	(3.4)	21.5	(8.5)
1983	1.8	(30.8)	12.0	15.4	7.7	(9.4)	21.5	0.0
1984	2.3	27.8	11.0	(8.3)	13.6	76.6	26.9	25.1
1985	2.5	8.7	10.9	(0.9)	12.0	(11.8)	25.4	(5.6)
1986	5.6	124.0	10.9	0.0	9.5	(20.8)	26.0	2.4
1987	6.7	19.6	12.4	13.8	10.3	8.4	29.4	13.1
1988	7.8	16.4	13.8	11.3	12.5	21.4	34.1	16.0
1989	7.2	(7.7)	15.3	10.9	14.1	12.8	36.6	7.3
1990	7.2	0.0	17.3	13.1	15.0	6.4	39.5	7.9
1991	7.7	6.9	19.1	10.4	16.1	7.3	42.9	8.6
1992	8.3	7.8	18.6	(2.6)	17.7	9.9	44.6	4.0
1993	9.8	18.1	17.3	(7.0)	18.7	5.6	45.8	2.7
1994	11.3	15.3	15.0	(13.3)	19.2	2.7	45.5	(0.7)
1995	9.6	(15.0)	13.7	(8.7)	20.2	5.2	43.5	(4.4)
1996	8.5	(11.5)	15.3	11.7	22.7	12.4	46.5	6.9
1997	8.4	(1.2)	15.1	(13)	24.3	7.0	47.8	2.8
<b>Annual Compounded Percent Change</b>								
1980 - 1997		5.8%		1.7%		7.1%		4.6%
1990 - 1997		2.2%		(1.9)		7.1		2.8

The U.S. Department of Commerce provides an alternate measure of travel to the United States from foreign countries, which includes both the number of total visitors and total expenditures (i.e., total amount spent while visiting) between 1989 and 1998. The data are presented in Table 7.8.1.9(b)

**Table 7.8.1.9(b): International Travel to the United States of America**

(Source: Department of Commerce as reproduced by Rushmore and Baum, 2001: 92)

Year	Visitors (Millions)	Percent Change	Expenditures (Millions)	Percent Change
1989	36.4	-	46.9	-
1990	39.4	8.2%	58.3	24.3%
1991	42.7	8.4	64.2	10.1
1992	47.3	10.8	71.4	11.2
1993	47.3	(3.2)	74.4	4.2
1994	44.8	(2.2)	75.4	1.3
1995	43.3	(3.3)	82.3	9.2
1996	46.5	7.4	90.2	9.6
1997	47.8	2.8	94.2	4.4
1998 (projected)	46.4	(2.9)	91.3	(3.1)
<b>Annual Compounded Percent Change</b>				
1989 - 1998		2.7%		7.7%

Between 1989 and projected year-end 1998, international visitation to the United States increased at an average annual compounded percentage rate of 2.7%, while total expenditures increased at a rate of 7.7% per year over the same period.

Foreign travel to the United States represents an important source of national lodging demand because such travel usually requires the use of a hotel or motel. Historically, foreign travel to the United States has benefited key gateway and resort cities such as

Boston, Washington, D.C., Orlando, Miami, Houston, Los Angeles, San Francisco and Honolulu. Note that trends in foreign travel are commonly tied to trends in the strength of the American dollar. Periods in which the American dollar is weak, tend to attract higher-than-usual levels of foreign travel, and often motivate domestic travellers to remain within the country rather than travel abroad. A strong American dollar has the opposite effect.

Statistics illustrating travel from the United States may also be pertinent in certain analyses. Table 7.8.1.9(c) sets forth historical trends in this variety of travel between 1985 and 1997.

**Table 7.8.1.9(c): International Travel from the United States of America**

(Source: U.S. Travel & Tourism Administration as reproduced by Rushmore and Baum, 2001: 93)

Year	To Mexico (Millions)	Percent Change	To Canada (Millions)	Percent Change	Overseas (Millions)	Percent Change	Total (Millions)	Percent Change
1985	10.5	-	12.1	-	12.7	-	35.3	-
1986	11.5	13.0%	13.0	16.5%	12.0	(5.5)%	37.6	6.5%
1987	13.0	13.0	13.3	(5.7)	13.6	13.3	39.9	6.1
1988	13.4	3.1	13.3	0.0	14.4	5.9	41.1	3.0
1989	14.2	6.0	12.2	(8.3)	14.8	2.8	41.2	0.2
1990	16.4	15.5	12.3	0.8	16.0	8.1	44.7	8.5
1991	15.0	(8.5)	12.0	(2.4)	14.5	(9.4)	41.5	(7.2)
1992	16.1	7.3	11.8	(1.7)	16.0	10.3	43.9	5.8
1993	15.3	(5.0)	12.0	1.7	17.2	7.5	44.5	1.4
1994	15.8	3.3	12.5	4.2	18.1	5.2	46.4	4.3
1995	15.8	0.0	12.9	3.2	18.7	3.3	47.4	2.2
1996	13.4	(15.2)	12.9	0.0	19.8	5.9	46.1	(2.7)
1997	17.7	32.1	13.4	3.9	21.6	9.1	52.7	14.3
<b>Annual Compounded Percent Change</b>								
1985 - 1997		4.4%		0.9%		4.5%		3.4%
1990 - 1997		1.1		1.2		4.4		2.4

American travel to Mexico increased at an average annual percentage rate of 4.4% between 1985 and 1997, decelerating to 1.1% between 1990 and 1997. A substantial decline was noted in 1996 as a result of political and financial instability in Mexico, although travel levels recovered in 1997, exceeding 1995 levels. Rates of growth in travel to Canada have remained relatively consistent historically remaining in the range of 1.0% per year, while travel to other foreign countries has increased more sharply. Between 1985 and 1997, overseas travel increased at an average annual compounded percentage rate of 4.5%, slowing only slightly to 4.4% per year between 1990 and 1997. Overall, travel to foreign countries increased at an average annual compounded percentage rate of 3.4% between 1985 and 1997, slowing to 2.4% between 1990 and 1997.

#### 7.8.1.10 Macro Demand by Market Segment

The preceding discussion of the macro demand for lodging facilities focuses on the overall market without regard to specific types of travellers. Since most hotels are orientated towards one or more market segments, however, the major components of the travel market must be identified. Most macro data is divided into three primary market segments: business travellers, meeting and group travellers, and pleasure or leisure travellers. Each segment has its own historic growth trends and demographic characteristics.



#### **7.8.1.10.1 Business Travel**

Often identified as “commercial” demand, business travel is the lifeblood of most lodging markets in the United States. Not only does the business travel segment represent the largest volume of room night demand, but is also, on the whole, the least price sensitive. A business-orientated hotel will generally achieve higher average room rates than will a comparable facility catering to meeting and group travellers.

The demographics of the business traveller are particularly interesting in evaluating the relative competitiveness of the various lodging facilities that attempt to attract this market segment. As illustrated in table 7.8.1.2(a), statistics provided by the U.S. Travel Data Centre indicate that the number of business trips increased at an average annual compounded percentage rate of 3.7% between 1982 and 1997, slowing to 1.8% between 1990 and 1997. Note that business trips, as defined by the U.S. Travel Data Centre, include trips for conventions and other business meetings. Although specific travel characteristics associated with business travel in 1997 were also set forth earlier in this text, some pertinent statistics are summarised as follows:

- 60% of business trips consisted of “general business,” while 9% of business trips consisted of a convention, seminar, or meeting.
- 71% of business trips involved only one household member.
- 64% of business trips required use of a hotel or motel.
- The average length of a business trip was 3.3 nights.
- 36% of business trips included an overnight weekend stay.
- Overall, 30% of business trips were combined with a pleasure-related purpose.

Certain types of businesses tend to generate more hotel room night demand than others. Whereas non-profit organisations tend to have a limited impact on lodging demand, firms involved in wholesale trade tend to generate the largest amount of hotel demand. The finance, insurance and real estate (FIRE) sector also tends to generate a strong share of business travel.

#### **7.8.1.10.2 Meeting and Group Travel**

Meeting and group demand is an important market segment for full-service hotels with meeting and banquet space. This segment is usually subdivided into three categories of meetings: corporate, convention, and association. Each has somewhat different characteristics and hotel requirements.

Corporate meetings are often organised by businesses and serve specific commercial needs. Conventions are large gatherings that can serve both business and social interests. Association meetings tend to be smaller than conventions and are commonly structured as business or educational functions.

**Table 7.8.1.10.2(a): Meeting and Group Attendance**

(Source: 1998 Meetings Market Report conducted by Plog Research for *Meetings & Conventions* magazine, as reproduced by Rushmore and Baum, 2001: 95)

Year	Avg. Annual Corporate Percent (Millions)	Percent Change	Avg. Annual Convention Percent (Millions)	Percent Change	Avg. Annual Associations (Millions)	Percent Change	Avg. Annual Total (Millions)	Percentage Change
1974	24.3	-	11.6	-	4.1	-	40.0	-
1977	46.3	24.0%	9.0	(8.1)%	11.2	39.8%	66.5	18.5%
1979	39.2	(8.0)	8.0	(5.7)	14.0	11.8	61.2	(4.1)
1981	42.3	3.9	9.5	9.0	13.0	(3.6)	64.8	2.9
1983	36.8	(6.7)	12.1	12.9	14.4	5.2	63.3	(1.2)
1985	39.8	4.0	13.5	5.6	18.2	12.4	71.5	6.3
1987	47.3	9.0	10.7	(11.0)	16.3	(5.4)	74.3	1.9
1989	58.4	11.1	13.6	12.7	21.7	15.4	93.7	12.3
1991	49.6	(7.8)	8.6	(20.5)	22.6	2.1	80.8	(7.1)
1993	55.1	5.4	10.7	11.5	18.7	(9.0)	84.5	2.3
1995	49.3	(5.4)	13.0	10.2	15.1	(10.1)	77.4	(4.3)
1997	49.9	0.6	11.7	(5.1)	17.9	8.9	79.5	1.3
<b>Annual Compounded Percent Change</b>								
1974 - 1997		3.2%		0.0%		6.6%		3.0%
1991 - 1997		0.1		5.3		3.8		(0.3)

**Table 7.8.1.10.2(b): Number of Meetings**

(Source: 1998 Meetings Market Report conducted by Plog Research for *Meetings & Conventions* magazine, as reproduced by Rushmore and Baum, 2001: 96)

Year	Avg. Annual Corporate Percent (Thousand)	Percent Change	Avg. Annual Convention Percent (Thousand)	Percent Change	Avg. Annual Associations (Thousand)	Percent Change	Avg. Annual Total (Thousand)	Percentage Change
1987	807.2	-	12.7	-	181.7	-	1,001.6	-
1989	866.8	3.6%	12.6	(0.4)%	186.6	13%	1,066.0	3.2 %
1991	8.6.2	(3.6)	10.2	(10.0)	215.0	7.3	1,031.4	(1.6)
1993	801.3	(0.3)	11.8	7.6	206.5	(2.0)	1,019.6	(0.6)
1995	797.1	(0.3)	10.9	(3.9)	175.6	(7.8)	983.6	(1.8)
1997	783.9	(0.8)	11.3	1.8	189.5	3.9	984.7	0,1
<b>Annual Compounded Percent Change</b>								
1987—1997		(0.3)%		(1.2)%		0.4°/a		(0.2)%

Between 1974 and 1997, total meeting and group attendance increased at an average annual compounded percentage rate of 3.0%, although attendance of this sort decreased at a rate of 0.3% between 1991 and 1997. Between 1974 and 1997, association attendance increased at the strongest rate, growing at an average annual compounded percentage rate of 6.6%, although this variety of visitation declined significantly between 1991 and 1997, pacing the overall decline throughout the 1990s. In contrast, convention visitation was essentially flat between 1974 and 1997 but increased at an average annual compounded percentage rate of 5.3% between 1991 and 1997.

Of the three sources of meeting and group attendance, the corporate segment accounts for the largest total share. This segment posted an average annual compounded percentage growth rate of 3.2% between 1974 and 1997 but remained flat between 1991 and 1997.

The 1998 Meetings Market Report also addresses the number of meetings held by each segment of meeting and group demand. Table 7.8.1.10.2(b) identifies these statistics, biennially, from 1987 to 1997.

**Table 7.8.1.10.2(c): Total Expenditure-Meetings and Groups**

(Source: 1998 Meetings Market Report conducted by Plog Research for *Meetings & Conventions* magazine, as reproduced by Rushmore and Baum, 2001: 97)

Year	Avg. Annual Corporate Percent (\$ Billions)	Percent Change	Avg. Annual Convention Percent (Billions)	Percent Change	Avg. Annual Associations (Billions)	Percent Change	Avg. Annual Total (Billions)	Percentage Change
1987	\$7.1	-	\$11.8	-	\$10.0	-	\$28.9	-
1989	9.7	16.9%	15.0	12.7%	14.9	22.1%	39.6	17.1%
1991	8.7	(5.3)	11.0	(14.4)	15.3	1.3	35.0	(6.0)
1993	10.6	10.4	15.5	18.7	14.3	(3.3)	40.4	7.4
1995	8.6	(9.9)	16.8	4.1	12.0	(8.4)	37.4	(3.8)
1997	10.8	12.1	16.7	(0.3)	14.3	9.2	41.8	5.7
<b>Annual Compounded Percent Change</b>								
1987 - 1997				4.3%	3.5%	3.6%	3.8%	

Between 1987 and 1997, the total number of meetings and conventions decreased at an average annual compounded percentage rate of 0.3%, with a moderate gain in association meetings offset by a decline in the number of corporate meetings and conventions. The number of conventions and association meetings grew between 1995 and 1997, with growth rates equal to 1.8% and 3.9%, respectively. Corporate meetings, on the other hand, decreased by 0.8%. The number of corporate meetings has declined consistently since 1989, due to corporate downsizing and cuts in corporate travel budgets. Although the decline through 1991 was significant, decreases in corporate meetings since that time have been comparatively small.

Another important measure of meeting and group activity pertains to total meeting expenditures. Table 7.8.1.10.2(d) sets forth these statistics biennially between 1987 and 1997.

Between 1987 and 1997, total meeting and group expenditures rose at an average annual compounded percentage rate of 3.8%, with strong gains noted in each of the three segments. Corporate meeting expenditures rose at the strongest rate, with a 4.3% growth rate. Growth in convention and association spending equalled 3.5% and 3.6%, respectively. Whereas the preceding trends in attendance and the number of meetings indicate a mix of positive and negative trends, the comparatively steady increase in spending across the three segments is a positive indicator.

**Table 7.8.1.10.2(d): Types of Facilities at which Meetings Were Held – 1997**

(Source: 1998 Meetings Market Report conducted by Plog Research for *Meetings & Conventions* magazine, as reproduced by Rushmore and Baum, 2001: 97)

Facility Type	Corporate Meetings	Conventions	Association Meetings
Downtown Hotels	61%	56%	60%
Suburban Hotels	44	21	36
Resort Hotels	35	21	33
Convention Centres	33	20	N/A
Airport Hotels	24	11	26
Golf Resorts	20	10	14
Suite Hotels	19	12	13
Residential Conference Centres	12	2	10

Table 7.8.1.10.2(d) specifies the frequency with which certain venues hosted corporate meetings, conventions, and association meetings. Downtown hotels hosted the majority of all three varieties of meeting and group demand. Sixty-one percent of those surveyed indicated that they had attended a corporate meeting at a downtown hotel; 56% indicated that they had attended a convention at a downtown hotel, and 60% indicated that they had attended an association meeting at a downtown hotel. Suburban hotels, usually unpopular as convention sites, most commonly hosted corporate and association meetings. Resort hotels reflected a relatively balanced level of popularity among the three varieties of meeting and group demand.

Again, corporate meetings represent the largest of the three meeting and group segments. Table 7.8.1.10.2(e) describes this segment in greater detail. Flog Research's survey indicates that training seminars represent the most common variety of corporate meetings (aside from "other"), followed by sales meetings and management meetings. New product introductions generally feature the largest attendance, with an average of 129. Group incentive trips feature the second-largest average attendance at 102. Individual incentive trips reported the longest duration, with stays of 4.7 days, followed by group incentive trips at 4.4 days. The 1998 Meetings Market Report also indicates that, on average, it takes six months to plan corporate meetings.

**Table 7.8.1.10.2(e): Corporate Meetings Characteristics**

(Source: 1998 Meetings Market Report conducted by Flog Research for *Meetings & Conventions* magazine, as reproduced by Rushmore and Baum, 2001: 98)

	Average No. of Meetings/Year	Average Attendance	Average Duration (in Days)
Sales Meetings	6.2	63	2.8
Management Meetings	5.0	39	2.6
Training Seminars	7.4	58	2.6
Professional/Technical Meetings	4.5	63	2.7
New Product Introductions	4.1	129	2.5
Individual Incentive Trips	3.9	66	4.7
Group Incentive Trips	3.2	102	4.4
Stockholder Meetings	1.8	35	2.1
Other Meetings	12.4	95	2.6

Among the remaining meeting and group segments, association meetings tend to host about 100 people, comparable to the attendance of corporate meetings. Conventions, on the other hand, generally attract an average of 1,000 people. While lead-planning time for associations is only slightly longer than that of corporate meetings, conventions often take years to plan.

The average meeting and convention size and the time required to plan them can be important considerations for a hotel appraiser. In valuing a hotel orientated toward the convention market, an appraiser should note the amount and size of the facility's meeting space. Doing so will help the appraiser determine whether or not the space suits an area's meeting demand. For example, if the market is composed mostly of corporate meetings, the meeting rooms should be relatively small and contain appropriate audiovisual and computer equipment. A convention market, on the other hand, requires facilities that can accommodate large groups and exhibit space.

The lead time for different types of meetings is particularly important for hotels under development, if major conventions are planned and hotels and meeting accommodation is

selected three years in advance, any new hotel scheduled to open within this period should be pre-marketed so that convention planners will consider it. As a hotel's meeting capacity increases, so must its marketing efforts prior to opening. A well-planned convention hotel will typically start its marketing program before construction begins.

### **7.8.1.10.3 Leisure Travel**

Most of the sources for data on leisure travel were introduced earlier in this chapter. Visitation counts that the National Parks Service compiles, are also significant. Between 1980 and 1998, national park visitation increased at an average annual compounded percentage rate of 1.5%, with a comparable growth rate of 1.4% noted between 1990 and 1998. With the exception of Sequoia National Park, each of the parks identified in the table posted stronger growth rates than that realised for all parks between 1980 and 1998. Between 1990 and 1998, visitation to Yellowstone National Park grew slightly below the national average, while visitation to Sequoia National Park receded.

Because each of the primary market segments displays specific characteristics that can affect the selection and use of a particular lodging facility, it helps to make a side-by-side comparison of typical traveller characteristics for the market's commercial, meeting and group, and leisure segments. Table 7.8.1.10.3(a) provides such a comparison.

Peak travel periods for commercial and leisure travellers are usually negatively correlated. Therefore, a hotel able to attract both of these segments is likely to have a smoother year-round occupancy pattern than a property largely dependent on one segment. The same analogy applies to weekly travel peaks for these two market segments.

The average length of stay affects many operational aspects of a hotel property. A hotel with a shorter average stay requires more front desk personnel, luggage carriers, and accounting staff because more people will be checking in and out over the course of a week. More cleaning staff may also be needed because maids can generally clean the room of a stay-over guest in less time than it takes to prepare a room for a new occupant. Operating costs increase with the number of checkouts.

An extended-stay property that attracts guests who stay longer than seven days, solves the problem of the weekend occupancy drop-off, which occurs when commercial travellers go home for the weekend. In this situation, longer stays actually increase the potential stabilised occupancy. From a layout point of view, however, a hotel with a longer average length of stay, such as a resort, often requires larger closets and more clothing storage areas to accommodate a greater amount of luggage.

Double occupancy refers to the average number of guests per room. Leisure demand, which includes many travelling families, has a double occupancy rate ranging from 1.7 to 2.5 people per room. Commercial demand, typically composed of individual travellers, produces a double occupancy rate of 1.0 to 1.3 people per room. Many hotels are able to charge higher room rates for additional guests in a room, which tends to increase a property's overall average rate.

When it comes to room layout, a hotel with a high double occupancy rate requires more beds per room. A family-orientated resort should have at least two double beds in each room to accommodate its high double occupancy. On the other hand, a commercial-orientated property can offer a large number of rooms furnished with single, king-sized

beds. Properties with high double occupancies usually require larger closets, two vanity sinks, and larger rooms.

**Table 7.8.1.10.3(a): Typical Traveller Characteristics**

(Source: HVS International, as reproduced by Rushmore and Baum, 2001: 101)

	Commercial Travellers	Meeting and Group Travellers	Leisure Travellers
Peak travel periods	Fall, winter	Fall, winter, spring, and summer	North - summer and spring South - winter, spring
Weekly peaks	Mon. – Thurs.	Sun. - Thurs.	Variable
Average length of stay	Highway: 1 - 2 nights. Downtown: 2 - 3 nights.	3 - 5 nights.	Highway: 1 night. Resort: 3 - 5 nights. 1.2 - 1.4 ppl/room
Double occupancy	1 - 1.3 ppl/room	High ADR conventions: 1.7 - 2.5 ppl/room Low ADR conventions: 1.3 - 1.7 ppl/room	
Use of food facilities			
Breakfast	50 - 70%	60 - 80%*	75 - 80%**
Lunch	10 - 20	50 - 80*	10 - 50**
Dinner	30 - 50	40 - 80*	30 - 50**
Use of beverage facilities	20 - 60%	30 - 75%	30 - 75%
Degree of price sensitivity	Low	Medium	Medium - high
Special requirements	Entertainment Quiet rooms Desks with good lighting Convenient parking	Adequate function and exhibit space Active sales organisation Large closets	Recreational facilities Large guestrooms Guest laundry
* Depends on the amount of banquet service			
** Depends on the meal plan (American or European)			

The use of food and beverage facilities is higher for meeting and group travellers than other market segments since many groups incorporate banquets and other forms of food service into their function schedules.

### 7.8.2 Macro Supply of Transient Accommodation

It has traditionally been difficult to determine the macro supply for transient lodging accommodation within the United States because there was no uniform, long-term census that annually quantified the number of hotel units. One of the problems relates to definition. What constitutes a lodging facility? Should properties such as rooming houses, residential hotels, dormitories, camps, seasonal resorts, and motels with fewer than 10 units be included? The U.S. Bureau of Census has information dating back to 1939, but the definition of a lodging facility used at that time included many properties that would not be considered competitive lodgings today.

Today the hotel data-consulting firm Smith Travel Research (STR) addresses the problem of quantifying the supply of hotel and motel rooms in the United States. STR tracks the number of lodging units currently operating in the United States and compiles occupancy, average room rate, and other operational statistics about thousands of hotels and motels throughout the nation. This information is then published in composite form and made available to subscribers of *Lodging Outlook* magazine.

### 7.8.2.1 Occupancy, Average Rate and RevPAR Data

Table 7.8.2.1(a) identifies historical and projected trends in supply, demand, and occupancy for the United States, based on data provided by STR, as well as HVS International. Between 1970 and 1998, the number of hotel rooms in the United States increased at an average annual compounded percentage rate of 2.4%. Between 1990 and 1998, the rate of growth equated to 1.8% per year. Recession in the early 1990s, and oversupply throughout the industry, slowed growth to a low of 0.3% in 1993. As the industry stabilised, the environment for additional gains in supply improved. Gains of 3.5% and 3.9% were noted in 1997 and 1998, respectively.

**Table 7.8.2.1(a): Supply, Demand and Occupancy – U.S.A. Lodging Industry**

(Source: Smith Travel Research and HVS International, as reproduced by Rushmore and Baum, 2001: 149)

Year	Net Rooms Added (Thousands)	Rooms Available Supply (Thousands)	Percent Change	Demand (Thousands)	Percent Change	Occupancy	Percent Change
1970	-	1,911	-	1,364	-	71.4%	-
1971	59	1,970	3.1%	1,375	0.8%	69.8	(22)%
1972	83	2,053	4.2	1,448	5.3	70.5	1.1
1973	109	2,162	5.3	1,526	5.4	70.6	0.1
1974	138	2,300	6.4	1,482	(2.9)	64.4	(8.7)
1975	60	2,360	2.6	1,512	2.0	64.1	(0.6)
1976	21	1,281	0.9	1,577	4.3	66.2	3.4
1977	24	2,405	1.0	1,627	3.2	67.7	2.1
1978	27	2,432	1.1	1,694	4.1	69.7	3.0
1979	34	2,466	1.4	1,783	5.3	72.3	3.8
1980	19	2,485	0.8	1,766	(1.0)	71.1	(1.7)
1981	38	2,523	1.5	1,723	(2.4)	68.3	(3.9)
1982	17	2,540	0.7	1,703	(1.2)	67.0	(1.8)
1983	31	2,571	1.2	1,667	(2.1)	64.8	(3.3)
1984	38	2,609	1.5	1,682	0.9	64.5	(0.6)
1985	73	2,682	2.8	1,704	1.3	63.5	(1.4)
1986	89	2,771	3.3	1,743	2.3	62.9	(1.0)
1987	94	2,865	3.4	1,814	4.1	63.3	0.7
1988	112	2,977	3.9	1,891	4.2	63.5	0.3
1989	101	3,078	3.4	1,983	4.9	64.4	1.4
1990	99	3,177	3.2	2,022	2.0	63.6	(1.2)
1991	45	3,222	1.4	1,993	(1.4)	61.9	(2.8)
1992	24	3,246	0.7	2,035	2.1	62.7	1.4
1993	11	3,257	0.3	2,071	1.8	63.6	1.4
1994	34	3,291	1.0	2,133	3.0	64.8	1.9
1995	43	3,334	1.3	2,172	1.8	65.1	0.5
1996	77	3,411	2.3	2,220	2.2	65.1	(0.1)
1997	118	3,529	3.5	2,275	2.5	64.5	(0.9)
1998	139	3,668	3.9	2,346	3.1	64.0	(0.8)
1999*	128	3,796	3.5	2,409	2.7	63.5	(0.8)
2000*	114	3,910	3.0	2,472	2.6	63.2	(0.4)
2001*	102	4,012	2.6	2,533	2.5	63.1	(0.1)
2002*	92	4,104	2.3	2,592	2.3	63.2	0.0
<b>Annual Compounded Percent Change</b>							
1970 - 1998			2.4%		2.0%		(0.4)%
1990 - 1998			1.8		1.9		0.1
1998 - 2002			2.8		2.5		(0.3)
* Projected							

Demand growth was outpaced by supply growth between 1970 and 1998, driving the national occupancy rate down from 71.4% in 1970 to 64.0% in 1998. The national occupancy rate has generally remained in the 60 - 65% range since 1983. The strongest national occupancy rate noted on the chart, 72.3%, was recorded in 1979. The lowest national occupancy rate, 61.9%, was recorded in 1991.

**Table 7.8.2.1(b): Average Rate, Occupancy Rate and RevPAR – U.S. Lodging Industry**

(Source: Smith Travel Research, Bureau of Labour Statistics, and HVS International, as reproduced by Rushmore and Baum, 2001: 150)

Year	Average Room Rate (US\$)	Percent Change	Consumer Price Index	Percent Change	Hotel Occupancy	Revenue Per Room (RevPAR) (US\$)	Percent Change
1973	17.36	-	44.4	-	70.6%	\$12.25	-
1974	18.68	7.6%	49.3	11.0%	64.4	12.04	(1.8)%
1975	20.04	7.3	53.8	9.1	64.1	12.84	6.7
1976	21.68	8.2	56.9	5.8	66.2	14.36	11.8
1977	23.44	8.1	60.6	6.5	67.7	15.86	10.4
1978	26.72	14.0	65.2	7.6	69.7	18.61	17.4
1979	31.27	17.0	72.6	11.3	72.3	22.61	21.5
1980	36.03	15.2	82.4	13.5	71.1	25.61	13.3
1981	39.64	10.0	90.9	10.3	68.3	27.07	5.7
1982	42.04	6.1	96.5	6.2	67.0	28.19	4.1
1983	44.21	5.2	99.6	3.2	64.8	28.67	1.7
1984	47.27	6.9	103.9	4.3	64.5	30.47	6.3
1985	49.45	4.6	107.6	3.6	63.5	31.42	3.1
1986	51.04	3.2	109.6	1.9	62.9	32.10	2.2
1987	53.12	4.1	113.6	3.6	63.3	33.63	4.8
1988	54.98	3.5	118.3	4.1	63.5	34.92	3.8
1989	56.84	3.4	124.0	4.8	64.4	36.62	4.9
1990	58.68	3.2	130.7	5.4	63.6	37.35	2.0
1991	58.78	0.2	136.2	4.2	61.9	36.36	(2.6)
1992	59.61	1.4	140.3	3.0	62.7	37.37	2.8
1993	61.27	2.8	144.5	3.0	63.6	38.96	4.2
1994	63.54	3.7	148.2	2.6	64.8	41.18	5.7
1995	66.65	4.9	152.4	2.8	65.1	43.42	5.4
1996	70.93	6.4	156.9	3.0	65.1	46.16	6.3
1997	75.31	6.2	160.5	2.3	64.5	48.55	5.2
1998	78.62	4.4	163.0	1.6	64.0	50.28	3.6
1999**	81.76	4.0	166.3	2.0	63.5	51.89	2.0
2000**	84.70	3.6	170.4	2.5	63.2	53.55	2.5
2001**	87.41	3.2	175.2	2.8	63.1	55.19	2.8
<b>Annual Compounded Percent Change</b>							
1973 - 1998		6.2%		5.3%			5.8%
1990 - 1998		3.7		2.8			3.8
1998 - 2001		3.6		2.4			3.1
* Consumer Price Index for Urban Consumers, base period is 1982—1984							
** Projected							

STR also records average rate and RevPAR trends for the nation. Table 7.8.2.1(b) identifies historical and projected trends in national average rate, occupancy rate, and RevPAR. RevPAR equates to revenue per available room and is calculated as the product of occupancy and average rate. Because it accounts for both occupancy and average rate together, this figure provides the best overall measure of revenue-generating results for a single property or group of hotels. For example, a hotel operating at a 55% occupancy rate with a room rate of \$65 has a RevPAR of \$35.75 (55% x \$65). This hotel is generating



more rooms revenue than a hotel with a 70% occupancy rate and a room rate of \$50, which has a RevPAR of \$35 (70% x \$50). Table 7.8.2.1(b) also sets forth the CPI-U (Consumer Price Index for Urban Consumers). A comparison of national average rate growth trends with the CPI-U is meaningful.

Between 1973 and 1998, the national average rate increased at an average annual compounded percentage rate of 6.2%, slowing to 3.7% between 1990 and 1998. In both cases, hotel average rate growth has exceeded the rate of gain in the CPI-U. In 1998, the national average rate increased by 4.4%, compared to the 1.6% gain in the CPI-U. RevPAR growth has also outpaced the rate of change in the CPI-U. The rate of change in hotel expenses conforms with that of the CPI-U, and the fact that average rate gains (and therefore hotel revenues) have increased at a superior pace is positive from the viewpoint of overall profit margins.

Table 7.8.2.1(c) sets forth supply levels for each of the 50 states and Washington, D.C., as of year-end 1989 and 1994, and as of September 30, 1999. As of 1999, the states with the largest quantity of hotel rooms (In descending order) were California, Florida, and Texas. Between 1994 and 1999, the highest rates of supply growth were noted in Mississippi, Minnesota and Nevada.

**Table 7.8.2.1(c): Lodging Industry Census by State**

(Source: Smith’s Travel Research, as reproduced by Rushmore and Baum, 2001: 151)

State	No. of Properties			Percent Change		No. of Rooms			Percent Change	
	1989	1994	1999*	1989 to 1994	1994 to 1999	1989	1994	1999*	1989 to 1994	1994 to 1999
Alabama	412	464	610	12.6%	31.5%	41,694	44,449	54,569	6.6%	22.8%
Alaska	148	153	168	3.4	9.8	11,636	12,235	14,326	5.1	17.1
Arizona	621	660	857	6.3	29.8	68,599	71,530	91,701	4.3	28.2
Arkansas	357	397	466	11.2	17.4	28,557	31,304	35,883	9.6	14.6
California	3,608	3,796	3,991	5.2	5.1	360,213	381,403	402,726	5.9	5.6
Colorado	743	764	934	2.8	22.3	68,640	70,551	87,436	2.8	23.9
Connecticut	238	246	260	3.4	5.7	24,522	25,164	28,174	2.6	12.0
Delaware	116	119	131	2.6	10.1	8,498	9,116	10,253	7.3	12.5
Florida	2,353	2,451	2,768	4.2	12.9	292,788	316,052	358,136	7.9	13.3
Georgia	878	976	1,356	11.2	38.9	103,705	110,958	142,276	7.0	28.2
Hawaii	309	315	313	1.9	(0.6)	66,455	69,270	69,240	4.2	(0.0)
Idaho	166	189	220	13.9	16.4	13,194	14,737	17,579	11.7	19.3
Illinois	812	900	1,096	10.8	21.8	103,837	111,387	130,388	7.3	17.1
Indiana	435	484	663	11.3	37.0	47,608	51,170	64,889	7.5	26.8
Iowa	371	425	516	14.6	21.4	28,167	31,183	37,463	10.7	20.1
Kansas	319	334	398	4.7	19.2	24,731	25,463	30,753	3.0	20.8
Kentucky	345	391	507	13.3	29.7	34,559	37,344	45,653	8.1	22.2
Louisiana	326	331	438	1.5	32.3	49,201	47,976	58,615	(2.5)	22.2
Maine	314	320	326	1.9	1.9	19,956	20,753	21,396	4.0	3.1
Maryland	426	423	469	(0.7)	10.9	46,931	48,332	53,191	3.0	10.1
Massachusetts	563	567	599	0.7	5.6	57,607	58,817	64,373	2.1	9.4
Michigan	802	830	974	3.5	17.3	76,726	78,558	90,556	2.4	15.3
Minnesota	504	561	697	11.3	24.2	44,608	42,802	58,119	(4.0)	35.8
Mississippi	256	297	417	16.0	40.4	26,165	29,636	43,083	133	45.4
Missouri	563	653	821	16.0	25.7	63,123	71,242	85,435	12.9	19.9
Montana	259	280	316	8.1	12.9	17,052	18,454	21,228	8.2	15.0
Nebraska	288	307	368	6.6	19.9	18,798	20,221	24,156	7.6	19.5
Nevada	469	487	551	3.8	13.1	105,881	132,371	171,300	25.0	29.4
New Hampshire	221	221	231	0.0	4.5	15,482	15,564	16,697	0.5	7.3
New Jersey	484	496	537	2.5	8.3	62,174	65,055	71,168	4.6	9.4
New Mexico	351	402	493	14.5	22.6	27,446	31,183	38,484	13.6	23.4
New York	1,127	1,151	1,219	2.1	5.9	138,256	142,608	150,284	3.1	5.4
North Carolina	1,125	1,168	1,457	3.8	24.7	95,354	98,570	125,129	3.4	26.9
North Dakota	121	139	155	14.9	11.5	9,748	10,817	12,039	11.0	11.3

**Table 7.8.2.1(c): Lodging Industry Census by State (Continued)**

State	No. of Properties			Percent Change		No. of Rooms			Percent Change	
	1989	1994	1999*	1989 to 1994	1994 to 1999	1989	1994	1999*	1989 to 1994	1994 to 1999
Ohio	790	854	1,092	8.1	27.9	87,679	91,825	112,422	4.7	22.4
Oklahoma	356	375	448	5.3	19.5	35,044	36,127	40,658	3.1	12.5
Oregon	525	574	665	9.3	15.9	38,926	42,373	51,563	8.9	21.7
Pennsylvania	774	833	970	7.6	16.4	83,545	89,081	103,404	6.6	16.1
Rhode Island	61	65	69	6.6	6.2	5,721	6,313	6,736	10.3	6.7
South Carolina	636	682	845	7.2	23.9	66,293	69,662	82,964	5.1	19.1
South Dakota	219	260	292	18.7	12.3	12,777	15,077	17,326	18.0	14.9
Tennessee	780	878	1,104	12.6	25.7	79,784	86,467	104,860	8.4	21.3
Texas	1,671	1,742	2,395	4.2	37.5	205,823	210,252	269,443	2.2	28.2
Utah	364	372	454	2.2	22.0	28,243	29,174	36,850	3.3	26.3
Vermont	198	200	203	1.0	1.5	13,632	14,093	14,491	3.4	2.8
Virginia	842	878	1,023	4.3	16.5	96,221	101,628	114,110	5.6	12.3
Washington	583	642	745	10.1	16.0	49,214	54,816	66,113	11.4	20.6
Washington, D.C.	103	98	103	(4.9)	5.1	24,446	23,820	24,799	(2.6)	4.1
West Virginia	170	180	217	5.9	20.6	17,118	18,036	21,222	5.4	17.7
Wisconsin	667	720	834	7.9	15.8	50,138	54,255	63,481	8.2	17.0
Wyoming	250	258	272	3.2	5.4	17,951	18,466	19,539	2.9	5.8
Total U.S.	29419	31308	37053	6.4%	18.3%	3114466	3,307,740	3,876,679	6.2%	17.2%

\* 1999 data are as of the 12 months ending September; all other data are year-end

STR also sorts lodging industry census data by hotel location, i.e., urban, suburban, airport, highway, and resort. Table 7.8.2.1(d) shows these census data. In terms of the number of rooms, suburban supply increased most dramatically between 1994 and 1999, while the resort sector recorded the smallest increase in inventory. Table 7.8.2.1(e) shows the share of total supply contributed by each of the various location types. The suburbs account for the largest single share, at 34%.

**Table 7.8.2.1(d): Lodging Industry Census by Location**

(Rushmore and Baum, 2001: 152)

State	No. of properties			Percentage Change		No. of Rooms			Percent Change	
	1989	1994	1999*	1989 to 1994	1994 to 1998	1989	1994	1999	1989 to 1994	1994 to 1999
Urban	2,843	2,887	3,472	1.5%	20.3%	520,875	531,019	609,160	1.9%	14.7%
Suburban	9,749	10,690	13,506	9.7	26.3	968,361	1,053,187	1,304,085	8.8	23.8
Airport	1,738	1,937	2,392	11.4	23.5	277,679	296,959	341,916	6.9	15.1
Highway	12,989	13,638	15,404	5.0	12.9	948,977	1,001,744	1,142,255	5.6	14.0
Resort	2,100	2,156	2,279	2.7	5.7	398,574	430,231	479,263	7.9	11.4
Total U.S.	29,419	31,308	37,053	6.4%	18.3%	3,114,466	3,313,140	3,876,679	6.4%	17.0%

**Tale 7.8.2.1(e): Hotel Locations (1999 Rooms Count)**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 152)

Location	Percent of Total
Urban	16%
Suburban	34
Airport	9
Highway	29
Resort	12

**Table 7.8.2.1(f): Lodging Industry Census by Property Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 153)

Type	No. of Properties			No. of Rooms			Percent Change		
	1989	1994	1999*	1989 to 1994	1994 to 1999	1989	1994	1989 to 1994	1994 to 1999
Gaming	153	173	206	13.1%	19.1%	85,837	104,203	21.4%	38.0%
Convention	140	147	156	5.0	6.1	117,699	122,824	4.4	2.8
Conference Centre	107	115	122	7.5	6.1	25,002	27,231	8.9	42
All suites	1,343	1,601	2,810	19.2	75.5	169,750	207,979	22.5	68.8
Hotel	27,675	29,272	33,781	5.8	15.4	2,716,558	2,851,390	5.0	132
Total U.S.	29,418	31,308	37,075	6.4%	18.4%	3,114,846	3,313,627	6.4%	17.0%

\* 1999 data are as of the 12 months ending September; all other data are year-end

STR also sorts lodging industry census data by property type, i.e., gaming, convention, conference centre, all-suites, and standard hotels. Table 7.8.2.1(f) shows this data. In terms of the number of rooms, the number of all-suites hotels increased by 68.8%, while gaming hotels increased by 38.0%. Only minor increases in convention and conference centre hotels were noted. Table 7.8.2.1(g) shows the share of total supply contributed by each property type.

**Table 7.8.2.1(g): Share of Total Supply Contributed by Hotel Types (1999-Room Count)**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 153)

Type	Percent of Total
Gaming	4%
Convention	3
Conference Centre	1
All suites	9
Hotel	83

Table 7.8.2.1(h) sets forth occupancy levels for each of the 50 states and Washington, D.C., for 1989, 1994, and the 12 months ending September 30, 1999. In 1999, the highest occupancy rates were recorded by Nevada, Rhode Island, and New York. The lowest occupancy rates were recorded by Wyoming, South Dakota, and Arkansas. Between 1994 and 1999, the strongest rates of occupancy gain were realised by Maine, Connecticut, and Vermont.

Table 7.8.2.1(k) sets forth occupancy rate levels by location type. Urban hotels posted the strongest occupancy rate in 1999; the urban location was the only one to realise a gain in occupancy between 1994 and 1999.

Table 7.8.2.1(m) sets forth occupancy rate levels by property type. Gaming hotels posted the highest occupancy level in 1999, although this sector's occupancy levels actually declined between 1994 and 1999. Between 1994 and 1999, occupancy rates increased for both the convention and conference centre sectors.

Table 7.8.2.1(n) sets forth average rate levels for each of the 50 states in the nation, as well as for the District of Columbia, for 1989, 1994, and the 12 months ending September 30, 1999. In 1999, the highest average rate levels were recorded by New York, Hawaii, Massachusetts, and Washington, D.C. The lowest average rate levels were recorded in North Dakota, Oklahoma, and Arkansas. Between 1994 and 1999, the strongest rates of average rate gain were realized by New York, Connecticut, and Delaware.

**Table 7.8.2.1(h): Hotel Occupancy Levels by State**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 154)

State	Occupancy Level			Percent Change	
	1989	1994	1999*	1989 to 1994	1994 to 1999
Alabama	61.2%	63.4%	57.4%	3.6%	(9.5)%
Alaska	70.5	65.1	63.1	(7.7)	(3.1)
Arizona	65.2	67.6	60.9	3.7	(9.9)
Arkansas	55.8	59.8	55.6	7.2	(7.0)
California	68.7	63.2	68.4	(8.0)	8.2
Colorado	55.6	63.6	60.4	14.4	(5.0)
Connecticut	60.4	60.8	66.5	0.7	9.4
Delaware	59.7	61.9	66.2	3.7	6.9
Florida	68.3	64.4	66.5	(5.7)	3.3
Georgia	60.5	66.6	61.6	10.1	(7.5)
Hawaii	78.5	75.5	71.7	(3.8)	(5.0)
Idaho	63.7	64.1	60.5	0.6	(5.6)
Illinois	64.1	65.4	64.8	2.0	(0.9)
Indiana	61.5	62.9	57.0	2.3	(9.4)
Iowa	59.6	60.1	58.7	0.8	(2.3)
Kansas	61.1	65.2	59.9	6.7	(8.1)
Kentucky	61.7	63.0	57.8	2.1	(8.3)
Louisiana	61.0	70.0	65.7	14.8	(6.1)
Maine	63.4	56.3	62.6	(11.2)	11.2
Maryland	62.1	63.2	67.0	1.8	6.0
Massachusetts	61.9	62.8	67.9	1.5	8.1
Michigan	58.8	61.9	61.5	5.3	(0.6)
Minnesota	61.5	64.5	62.1	62.1	(3.7)
Mississippi	59.4	67.4	58.9	13.5	(12.6)
Missouri	60.4	60.4	58.6	2.6	(5.5)
Montana	60.7	60.6	57.8	(0.2)	(4.6)
Nebraska	60.4	65.1	59.7	7.8	(8.3)
Nevada	76.1	79.6	75.7	4.6	(4.9)
New Hampshire	56.1	56.0	60.1	(0.2)	7.3
New Jersey	63.6	65.7	67.9	3.3	3.3
New Mexico	59.1	68.9	59.4	16.6	(13.8)
New York	68.8	66.7	71.1	(3.1)	6.6
North Carolina	60.2	63.5	59.4	5.5	(6.5)
North Dakota	65.2	57.6	57.4	(11.7)	(0.3)
Ohio	62.9	62.3	59.1	(1.0)	(5.1)
Oklahoma	54.4	56.2	56.2	3.3	0.0
Oregon	68.8	63.4	57.3	(7.8)	(9.6)
Pennsylvania	64.9	63.5	63.0	(2.2)	(0.8)
Rhode Island	65.7	63.4	72.2	(3.5)	13.9
South Carolina	65.1	64.3	60.5	(1.2)	(5.9)
South Dakota	54.3	55.4	55.4	2.0	0.0
Tennessee	60.4	64.2	58.3	6.3	(9.2)
Texas	59.9	64.9	61.3	8.3	(5.5)
Utah	62.8	68.3	57.6	8.8	(15.7)
Vermont	64.4	56.3	61.3	(12.6)	8.9
Virginia	63.7	63.6	62.9	(0.2)	(1.1)
Washington	68.9	65.2	63.2	(5.4)	(3.1)
Washington, D.C.	71.0	67.1	70.7	(5.5)	5.4
West Virginia	63.3	67.9	58.6	7.3	(13.7)
Wisconsin	60.5	60.5	57.6	0.0	(4.8)
Wyoming	54.6	55.2	53.9	1.1	(2.4)
Total U.S.	64.4%	64.8%	N/A	0.6%	N/A

\* 1999 data are for the 12 months ending September.

Table 7.8.2.1(p) sets forth average rate levels by location type. Resorts and urban hotels posted the strongest average rate levels in 1999. Urban hotels experienced the strongest rate of average rate growth between 1994 and 1999.

**Table 7.8.2.1(k): Hotel Occupancy Levels by Location Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 155)

Location	Occupancy Rate			Percent Change	
	1989	1994	1999*	1989 - 1994	1994 - 1999
Urban	65.3%	67.7%	68.0%	3.7%	0.4%
Suburban	63.1	65.9	64.1	4.4	(2.7)
Airport	67.4	69.2	67.1	2.7	(3.0)
Highway	63.1	62.8	60.2	(0.5)	(4.1)
Resort	68.9	67.6	67.4	(1.9)	(0.3)

\* 1999 data are for the 12 months ending September.

**Table 7.8.2.1(m): Hotel Occupancy Levels by Property Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 155)

Type	Occupancy Rate			Percent Change	
	1989	1994	1999*	1989 - 1994	1994 - 1999
Gaming	85.7%	86.0%	81.8%	0.4%	(4.9)%
Convention	70.8	71.3	72.8	0.7	2.1
Conference Centre	62.9	67.7	68.0	7.6	0.4
All suites	69.3	73.7	70.5	6.3	(4.3)
Hotel	63.8	64.9	63.3	1.7	(2.5)

\* 1999 data are for the 12 months ending September.

Table 7.8.2.1(q) sets forth average rate levels by property type. Convention and conference centre hotels posted the highest average rate levels in 1999. These sectors also recorded the strongest rate of average rate growth between 1994 and 1999.

Table 7.8.2.1(r) sets forth RevPAR levels for each of the 50 states and Washington, D.C., for 1989, 1994, and the 12 months ending September 30, 1999. In 1999, New York, Hawaii, and Massachusetts, as well as Washington, D.C recorded the highest RevPAR levels. The lowest RevPAR levels were recorded by North Dakota, Oklahoma, and Arkansas. Between 1994 and 1999, the strongest rates of RevPAR gain were realized by Connecticut, New York, and Rhode Island.

Table 7.8.2.1(s) sets forth RevPAR levels by location type. Resorts and urban hotels posted the strongest RevPAR levels in 1999 and the strongest rates of RevPAR growth between 1994 and 1999.

Table 7.8.2.1(t) sets forth RevPAR levels by property type. Convention and conference center hotels posted the highest RevPAR levels in 1999 as well as the strongest rates of RevPAR growth between 1994 and 1999.

**Table 7.8.2.1(n): Hotel Average Room Rate by State**

(Rushmore and Baum, 2001: 156)

State	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Alabama	\$40.19	\$45.12	\$54.17	12.3%	20.1%
Alaska	69.94	89.91	96.94	28.6	7.8
Arizona	56.69	69.44	84.81	22.5	22.1
Arkansas	36.65	42.06	52.33	14.8	24.4
California	62.29	69.44	92.17	11.5	32.7
Colorado	55.31	71.15	87.12	28.6	22.4
Connecticut	61.17	62.03	86.79	1.4	39.9
Delaware	53.25	52.15	71.87	(2.1)	37.8
Florida	59.58	66.86	85.76	12.2	28.3
Georgia	47.71	55.51	69.68	16.3	25.5
Hawaii	98.30	104.05	129.38	5.8	24.3
Idaho	40.09	51.33	61.10	28.0	19.0
Illinois	61.71	69.06	91.07	11.9	31.9
Indiana	44.75	51.24	63.42	14.5	23.8
Iowa	40.30	45.15	54.70	12.0	21.2
Kansas	39.13	45.16	56.31	15.4	24.7
Kentucky	41.65	46.70	57.44	12.1	23.0
Louisiana	55.93	68.19	85.38	21.9	25.2
Maine	56.07	59.74	71.12	6.5	19.0
Maryland	58.22	62.24	80.58	6.9	29.5
Massachusetts	78.97	83.11	111.23	5.2	33.8
Michigan	51.64	55.40	69.53	7.3	25.5
Minnesota	47.54	58.47	70.69	23.0	20.9
Mississippi	37.05	46.37	54.39	25.2	17.3
Missouri	47.57	54.33	64.86	14.2	19.4
Montana	36.93	46.69	53.88	26.4	15.4
Nebraska	37.43	43.59	54.18	16.5	24.3
Nevada	48.32	56.90	78.30	17.8	37.6
New Hampshire	61.28	60.74	74.14	(0.9)	22.1
New Jersey	79.08	70.90	93.39	(10.3)	31.7
New Mexico	41.37	53.53	58.96	29.4	10.1
New York	87.77	95.23	134.41	8.5	41.1
North Carolina	42.58	47.65	61.29	11.9	28.6
North Dakota	36.53	39.94	44.69	9.3	11.9
Ohio	46.79	53.16	66.19	13.6	24.5
Oklahoma	38.10	43.58	51.74	14.4	18.7
Oregon	45.65	56.54	68.57	23.9	21.3
Pennsylvania	56.74	63.14	80.71	11.3	27.8
Rhode Island	77.23	76.09	100.01	(1.5)	31.4
South Carolina	47.89	55.27	65.99	15.4	19.4
South Dakota	37.21	45.04	54.67	21.0	21.4
Tennessee	45.60	52.37	62.97	14.8	20.2
Texas	46.59	56.64	69.98	21.6	23.6
Utah	45.22	57.54	69.14	27.2	20.2
Vermont	65.38	73.18	82.86	11.9	13.2
Virginia	53.88	59.34	75.01	10.1	26.4
Washington	49.83	62.05	77.83	24.5	25.4
Washington, D.C	101.12	113.01	138.73	11.8	22.8
West Virginia	41.65	46.50	56.41	11.6	21.3
Wisconsin	46.21	54.48	63.20	17.9	16.0
Wyoming	39.57	50.96	62.10	28.8	21.9
Total U.S.	\$51.23	\$57.78	N/A	11.8%	N/A

**Table 7.8.2.1(p): Hotel Average Room Rate by Location Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 157)

Location	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Urban	\$79.91	\$91.73	\$121.08	14.8%	32.0%
Suburban	54.50	61.04	76.16	12.0	24.8
Airport	56.73	60.96	78.33	7.5	28.5
Highway	42.29	47.19	59.23	11.6	25.5
Resort	87.24	97.96	125.89	12.3	28.5

\* 1999 data are for the 12 months ending September.

**Table 7.8.2.1(q): Hotel Average Room Rate by Property Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 157)

Type	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Gaming	\$64.71	\$60.36	\$74.65	(6.7)%	23.7%
Convention	103.93	110.75	148.87	6.6	34.4
Conference Centre	84.07	106.49	148.41	26.7	39.4
All suites	79.41	86.83	94.98	9.3	9.4
Hotel	55.82	63.47	81.29	13.7	28.1

\* 1999 data are for the 12 months ending September.

**Table 7.8.2.1(r): Hotel RevPAR by State**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 158)

Type	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Alabama	\$24.60	\$28.61	\$31.09	16.3%	8.7%
Alaska	49.31	58.53	61.17	18.7	4.5
Arizona	36.96	46.94	51.65	27.0	10.0
Arkansas	20.45	25.15	29.10	23.0	15.7
California	42.79	43.89	63.04	2.6	43.7
Colorado	30.75	45.25	52.62	47.1	16.3
Connecticut	36.95	37.71	57.72	2.1	53.0
Delaware	31.79	32.28	47.58	1.5	47.4
Florida	40.69	43.06	57.03	5.8	32.5
Georgia	28.86	36.97	42.92	28.1	16.1
Hawaii	77.17	78.56	92.77	1.8	18.1
Idaho	25.54	32.90	36.97	28.8	12.3
Illinois	39.56	45.17	59.01	14.2	30.7
Indiana	27.52	32.23	36.15	17.1	12.2
Iowa	24.02	27.14	32.11	13.0	18.3
Kansas	23.91	29.44	33.73	23.2	14.6
Kentucky	25.70	29.42	33.20	14.5	12.8
Louisiana	34.12	47.73	56.09	39.9	17.5
Maine	35.55	33.63	44.52	(5.4)	32.4
Maryland	36.15	39.34	53.99	8.8	37.3
Massachusetts	48.88	52.19	75.53	6.8	44.7
Michigan	30.36	34.29	42.76	12.9	24.7
Minnesota	29.24	37.71	43.90	29.0	16.4
Mississippi	22.01	31.25	32.04	42.0	2.5
Missouri	28.73	33.68	38.01	17.2	12.8
Montana	22.42	28.29	31.14	26.2	10.1
Nebraska	22.61	28.38	32.35	25.5	14.0
Nevada	36.77	45.29	59.27	23.2	30.9
New Hampshire	34.38	34.01	44.56	(1.1)	31.0
New Jersey	50.29	46.58	63.41	(7.4)	36.1

**Table 7.8.2.1(r): Hotel RevPAR by State (Continued)**

Type	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
New Mexico	24.45	36.88	35.02	50.8	(5.0)
New York	60.39	63.52	95.57	52	50.5
North Carolina	25.63	30.26	36.41	18.0	20.3
North Dakota	23.82	23.01	25.65	(3.4)	11.5
Ohio	29.43	33.12	39.12	12.5	18.1
Oklahoma	20.73	24.49	29.08	18.2	18.7
Oregon	31.41	35.85	39.29	14.1	9.6
Pennsylvania	36.82	40.09	50.85	8.9	26.8
Rhode Island	50.74	48.24	72.21	(4.9)	49.7
South Carolina	31.18	35.54	39.92	14.0	12.3
South Dakota	20.21	24.95	30.29	23.5	21.4
Tennessee	27.54	33.62	36.71	22.1	9.2
Texas	27.91	36.76	42.90	31.7	16.7
Utah	28.40	39.30	39.82	38.4	13
Vermont	42.10	41.20	50.79	(2.1)	23.3
Virginia	34.32	37.74	47.18	10.0	25.0
Washington	34.33	40.46	49.19	17.8	21.6
Washington, D.C.	71.80	75.83	98.08	5.6	29.3
West Virginia	26.36	31.57	33.06	19.8	4.7
Wisconsin	27.96	32.96	36.40	17.9	10.4
Wyoming	21.61	28.13	33.47	30.2	19.0
Total U.S.	\$36.62	\$41.18	N/Av	12.5%	N/A

\* 1999 data are for the 12 months ending September.

**Table 7.8.2.1(s): Hotel RevPAR by Location Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 159)

Location	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Urban	\$52.18	\$62.10	\$82.33	19.0%	32.6%
Suburban	34.39	40.23	48.82	17.0	21.4
Airport	38.24	42.18	52.56	10.3	24.6
Highway	26.68	29.64	35.66	11.1	20.3
Resort	60.11	66.22	84.85	102	28.1

\* 1999 data are for the 12 months ending September.

**Table 7.8.2.1(t): Hotel RevPAR by Property Type**

(Source: Smith Travel Research, as reproduced by Rushmore and Baum, 2001: 159)

Type	Average Room Rate			Percent Change	
	1989	1994	1999	1989 to 1994	1994 to 1999
Gaming	\$55.46	\$51.91	\$61.06	(6.4)%	17.6%
Convention	73.58	78.96	108.38	7.3	37.2
Conference Centre	52.88	72.09	100.92	36.3	40.0
All suites	55.03	63.99	66.96	16.3	4.6
Hotel	35.61	41.19	51.46	15.7	24.9

\* 1999 data are for the 12 months ending September.



### 7.8.3 Macro Travel Price Data

Macro travel data pertaining to the price of hotel accommodation are also important to hotel feasibility analysts. Since a hotel's rooms revenue is calculated by multiplying the number of occupied rooms (demand) by the price of each occupied room, trends in macro hotel room rates can be a factor in forecasting future changes.

Each year the Travel Industry Association of America compiles data pertaining to the Travel Price Index (TPI) for various components of the travel industry, such as transportation costs, airfares, lodging costs, and food and beverage costs. These indices are similar to the Consumer Price Index (CPI) in that they show annual price increases caused by inflation and other factors. Table 7.8.3(a) shows the travel price Indices for various travel components as well as the overall TPI.

**Table 7.8.3(a): Travel Price Index**

(Source: Travel Industry of America, as reproduced by Rushmore and Baum, 2001: 102)

Year	Transportation	% Change	Airline Fares	% Change	Lodging	% Change	Food & Beverage	% Change	Recreation Services	% Change	Total TPI	% Change
1988	99.8	-	124.2	-	132.9	-	122.2	-	131.1	-	119.7	-
1989	107.3	7.5%	131.6	6.0%	138.4	4.1%	127.8	4.6%	135.4	3.3%	125.7	5.0%
1990	121.4	13.1	148.4	12.8	152.5	10.2	133.8	4.7	143.2	5.8	136.0	8.2
1991	123.4	1.6	155.0	4.4	174.5	14.4	138.8	3.7	150.6	5.2	144.8	6.5
1992	123.3	(0.1)	155.2	0.1	184.2	5.6	141.7	2.1	155.8	3.5	148.9	2.8
1993	132.3	7.3	178.7	15.1	189.4	2.8	144.3	1.8	160.8	3.2	154.0	3.4
1994	135.5	2.4	185.0	3.5	195.5	3.2	146.8	1.7	166.8	3.7	157.7	2.4
1995	138.0	1.8	189.7	2.5	203.1	3.9	150.2	2.3	172.0	3.1	162.1	2.8
1996	142.8	3.5	192.5	1.5	213.7	5.2	154.0	2.5	178.1	3.5	168.1	3.7
1997	145.6	2.0	199.2	3.5	224.1	4.9	158.5	2.9	183.8	3.2	173.7	3.3
1998	140.2	(3.7)	205.3	3.1	234.5	4.6	162.6	2.6	189.0	2.8	177.1	2.0
<b>Annual Compounded Percent Change</b>												
1988 - 1998		3.5%		5.2%		5.8%		2.9%		3.7%		4.0%

Between 1988 and 1998, the total TPI increased at an average annual compounded percentage rate of 4.0%. A significant share of this growth was recorded between 1988 and 1991. In more recent years, the TPI has increased at levels below 4.0% per year. The most rapid rate of growth among the various TPI categories occurred in lodging, which grew at an average annual compounded percentage rate of 5.8% between 1988 and 1998. Unlike the overall TPI, lodging has experienced strong price increases in recent years. That is largely due to the fact that the general health of the national lodging industry allowed for strong gains in hotel pricing relative to the overall TPI, and, as noted in table 7.8.3(b), the CPI. Airline fares are the only other TPI category where price increases exceeded those realised for the overall TPI. Table 7.8.3(b) illustrates historical trends in the lodging TPI and the overall TPI in relation to the CPI for all urban consumers (CPI-U), between 1979 and 1998.

Gains in the lodging TPI have historically outpaced gains in both the overall TPI and the CPI-U. A comparable premium in the rate of gain in lodging prices versus the overall TPI and the CPI-U is apparent for both periods of analysis, 1979 to 1998, and 1990 to 1998. Thus, whereas the average annual compounded percentage rate of lodging TPI gain decelerated to 5.5% between 1990 and 1998 (down from 6.9% between 1979 and 1998), the real gain relative to general inflation remained significant throughout the 1990s.

**Table 7.8.3(b): Travel Price Index vs. Consumer Patrice Index**

(Source: Travel Industry Association of America, as reproduced by Rushmore and Baum, 2001: 103)

Year	Lodging TPI	% Change	Total TPI	% Change	CPI-U*	% Change
1979	66.4	-	69.3	-	72.6%	-
1980	75.8	14.2%	81.2	17.2%	82.4	13.5%
1981	84.5	11.5	90.4	11.3	90.9	10.3
1982	94.2	11.5	95.5	5.6	96.5	6.2
1983	99.0	5.1	98.9	3.6	99.6	3.2
1984	106.8	7.9	103.6	4.8	103.9	4.3
1985	114.2	6.9	108.4	4.6	107.6	3.6
1986	118.4	3.7	109.0	0.6	109.6	1.9
1987	125.7	6.2	114.9	5.4	113.6	3.6
1988	132.9	5.7	119.7	4.2	118.3	4.1
1989	138.4	4.1	125.7	5.0	124.0	4.8
1990	152.5	10.2	136.0	8.2	130.7	5.4
1991	174.5	14.1	144.8	6.5	136.2	4.2
1992	184.2	5.6	148.9	2.8	140.3	3.0
1993	189.4	2.8	154.0	3.4	144.5	3.0
1994	195.5	3.2	157.7	2.4	148.2	2.6
1995	203.1	3.9	162.1	2.8	152.4	2.8
1996	213.7	5.2	168.1	3.7	156.9	3.0
1997	224.1	4.9	173.7	3.3	160.5	2.3
1998	234.5	4.6	177.1	2.0	163.0	1.6
<b>Annual Compounded Percent Change</b>						
1979 - 1998		6.9%		5.1%		4.3%
1990 - 1998		5.5		3.4		2.8
* Consumer Price Index for Urban Consumers, base period is 1982-1984						

The preceding trends indicate that gains in hotel room rates are not totally tied to changes in the CPI (they can also be market-driven). For example, when hotel demand is strong and the market is under supplied, occupancy levels will increase and room rates should show impressive gains. When hotel supply exceeds demand, occupancy levels will fall and hotel room rates will either level off or start to decline. The trends indicated in table 7.8.3(b) support these observations. National lodging markets became substantially overbuilt by the early 1990s, and as hotel operators sacrificed average rates to retain viable occupancy levels, the rate of gain in the lodging TPI slowed. Between 1993 and 1995, the rate of gain ranged from 2.8% to 3.9%. As the lodging industry's recovery progressed in more recent years, the environment for average rate recovery also improved.

### 7.8.3.1 Future Changes in Hotel Macro Demand

If the past is an indication of the future, continuous changes in the transportation industry could significantly affect the characteristics of an average trip. Supersonic transport may prove to be as revolutionary as the jet plane, allowing travellers to make international trips in a single day. More expensive gasoline could reduce the mobility of the average vacation traveller, while greater use of mass transportation and the possible rebirth of rail service might prompt travellers to bypass highway facilities altogether. More sophisticated telecommunication systems may someday make in-person business meetings and conferences obsolete.

Future macro travel projections should also reflect potentially positive factors. In the past decade companies have given their employees more fringe benefits, including longer vacations. Some firms have even implemented a four-day workweek. Although these trends

do not necessarily mean increased travel, they do add to the time that families can spend away from home.

A growing number of senior citizens with better retirement incomes and a desire to travel could also generate additional lodging demand. Increased foreign travel to the United States and a more travel-orientated society in general, could mean more business for the lodging industry.

### 7.8.4 Supplementary Macro Hotel Development Indicators and Trends

In addition to the macro hotel demand and supply analyses, a few more macro trends and cycles that could influence hotel development, are included. This section does not aim to be an exhaustive explanation of all possible economic trends that could influence hotel development, but rather serves as an introduction and reminder of the many factors that need to be considered when feasibility analysts perform a feasibility study.

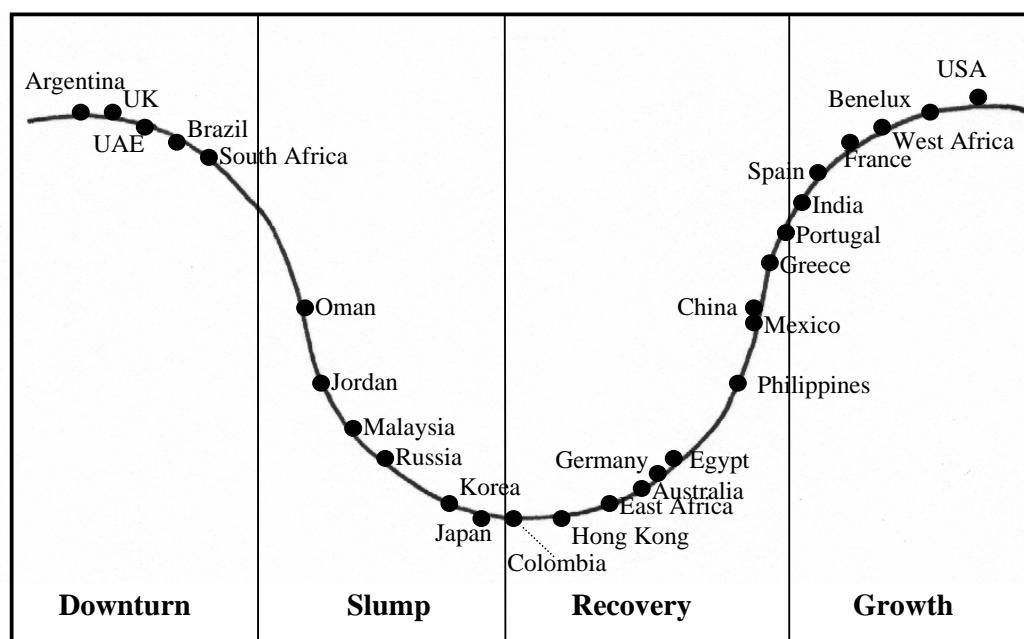
Today’s business climate is both complex and uncertain. *“Contemporary management thinking suggests that in this climate, managers must manage for the future, not the past. To accomplish this challenging objective, a successful manager must use all the tools available to him or her to scan the business environment in order to identify the forces driving change in that environment”* (Choia et al, 1999: 59).

Scanning the business environment demands from managers the ability to use effective cognitive and perceptual skills to predict change. Using these skills, managers can be expected to identify emerging patterns in their business domain that will provide opportunity to add value to the firm. One tool useful for this purpose is scanning the business environment for emerging economic patterns or trends unfolding in the broader economic climate in which the firm is functioning.

#### 7.8.4.1 Global Hotel Investment Cycle

**Table 7.8.4.1(a): Global Hotel Investment Cycle**

(Source: Global Investment Cycle, 2001)



International hotel developers, operators and franchisers direct their hotel expansion programmes in accordance with global investment cycle research.

Table 7.8.4.1(a) summarises the findings of global investment research, placing the various countries in one of four economic phases, i.e. downturn, slump, recovery or growth phase.

#### **7.8.4.2 Hotel Industry Cycle**

The hospitality cycle comprises five characteristic periods (Baltin et al, 1999: 71):

##### **1. Growth**

During the growth period, occupancy levels and average room rates increase, usually by more than inflation. Hotels generate strong cash flows. Capital markets jump on the bandwagon with equity capital and loans for new development. Market values for hotel properties increase.

##### **2. Peak**

During the peak period, occupancy levels and room rates continue to be strong. Cash flows remain high. Equity and debt capital continues to be available. Market values continue to rise, but at a slower rate, before stabilising. Everyone is happy.

##### **3. Decline**

The decline period is led by a downward trend in occupancy. Room rates grow at or below the rate of inflation. Cash flows stabilise or decrease slightly. As investors sense risks rising, they require higher returns and begin to look for other investments. Decreasing cash flows and investors' demands for higher rates of return push market values downward.

##### **4. Gutter**

During the gutter period, occupancy levels, room rates, and cash flows reach rock bottom. As the competition becomes fierce, the market becomes a buyer's market. Perceiving the risks to be extremely high, investors look for even higher returns. Financing is not available, and values bottom out—often at below-replacement costs.

##### **5. Resuscitation**

At this stage, occupancy levels and room rates begin to rebound. Over-leveraged players have vanished and bankruptcies have removed some rooms from the market, at least for a time. The survivors start making profits again. Equity investors come out of hiding and begin to lower their return requirements. Lenders cautiously lend money. Market values start slowly to improve.

And, the cycle begins all over again.

Choi et al (1999: 159) refer to Baltin et al's (1999) above mentioned industry cycle as "the hotel business cycle", which is "...a type of fluctuation found in the aggregate economic activity of nations that organise their work mainly in business enterprises. A cycle consists of expansions occurring at about the same time in many economic activities, followed by similarly general recessions, contractions, and revivals which merge into the expansion phase of the next cycle. This sequence of changes is recurrent but not periodic, the duration of business cycles vary from more than one year to ten or 12 years and they are not divisible into shorter cycles of similar character with amplitudes approximating their own."

The business cycle typically consists of an interlude of prosperity rising into boom, peaking out, sliding into recession, recovering and launching into a new phase of prosperity. A turning point occurs when a time series that has been rising begins to fall, or vice versa. Although the length and breadth of its phases have differed widely from one cycle to another, this general pattern has repeated itself with little variation.

Choi (1999: 160) researched the cyclical trend of the U.S.A. hotel industry over a 28-year period (from 1966 to 1993), which resulted in the following findings:

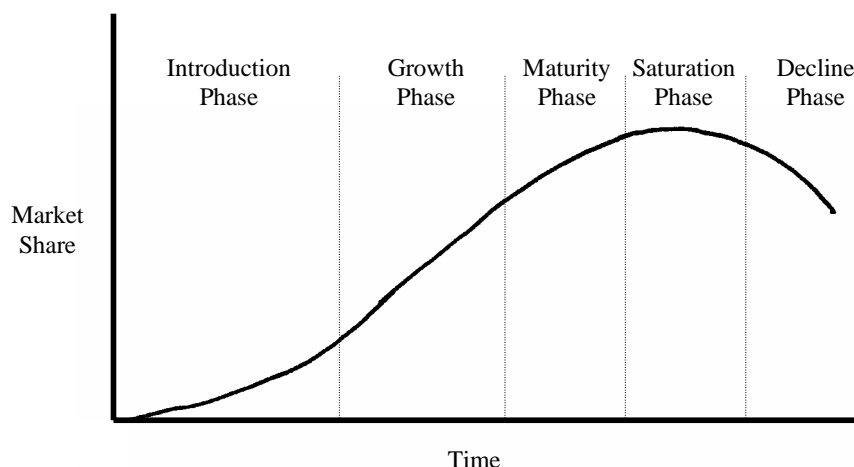
- During this period the U.S.A. hotel industry demonstrated three cycles (peak to peak or trough to trough).
- The industry peaked in 1967, 1973, 1980, 1989, and troughed in 1969, 1974, 1982, and 1991. The mean duration of the hotel industry cycle is 7.3 years, calculated either by peak-to-peak or trough-to-trough.
- The hotel industry declined sharply after it reached the peaks.
- The mean duration for the contraction is about two years (1.7 years) and the mean duration for the expansion is about six years (5.7 years).
- The hotel industry cycle was reformed with the hotel industry growth cycle based on year-over-year growth rate.
- The hotel industry experienced high growth (boom) every four or five years.
- The average expansion period is about three years and the average contraction period is about two years.
- The hotel industry led the general business cycle peaks by about 0.75 years on average and also led at troughs in the general business cycle by roughly 0.5 years.
- The results of this study provide useful guideposts for taking every possible advantage of the cycle study for the practitioners and researchers in the hotel industry.

#### 7.8.4.3 Hotel Product Life cycle

A key marketing diagnostic tool, which is extremely useful for the purpose of determining appropriate marketing objectives and strategies for the service product of an organisation, is life cycle analysis. (McDonald & Payne, 1998)

**Figure 7.8.4.3(a): Product Life cycle Curve**

(Source: McDonald & Payne, 1998: 104)



A product life cycle curve is characterised by five different phases:

- *Introduction:* Here, there is a slow growth in sales as the new service struggles to get known and accepted.
- *Growth:* If the service is successful, its sales take off as repeat purchases are made and customers become aware of it. Not all new services survive long enough to reach this phase. Moreover, the growth potential attracts other companies into this field and so competition also increases.
- *Maturity:* Since all markets are finite, the rapid growth rate of the earlier phase begins to slow down.
- *Saturation:* The rate of sales growth eventually levels out. Generally, there are too many firms competing for too little business at this stage. As a result, price wars may break out and there are casualties, or tactical withdrawals, among the competitive companies.
- *Decline:* Finally, the market itself falls into decline.

These phases in the life cycle concept suggest that if a product or service is introduced to the market successfully, then the momentum of buying will increase over time. Consumers will try the product or service and will then often repeat their purchase decision. They will also pass on information about the product to others who, in turn, will test the product. However, the market will eventually reach its peak. As the market matures, there are many firms in the market place and price wars are common as competition develops for market share. Eventually, some firms will be forced out of the market, with the most competitive ones surviving. The market will gradually decline as alternative products are offered and fashions change. The market may be sustained for a small volume, with few producers, though this will often be difficult as economies of scale can be lost.

As an example, the characteristics of a mature market are that it is one populated by established companies that are expert operators and marketers with substantial financial resources. Fast food is a good example of a mature industry, one in which corporate giants compete against each other in a mass market. The responses which maturity dictates to marketers in a mature market are repositioning against other segments, altering some or all of the marketing mix, or a combination of both.

#### **7.8.4.4 Hotel Property Life Cycles**

Hotel buildings, facilities, operating equipment, furniture, etc. has an economic lifetime, during which it would be regarded as optimal to use, as long as it complies with the hotel quality standards. When it does not comply with standards, it is replaced or revitalised. These economic life spans are determined by either accounting procedure or practical utilisation.

Powers (1996: 231) explains that hotels are assets with a long economic life, commonly 30 or 40 years or more. Requiring large amounts of capital to build hotels, it is often not feasible for a style change to suite the life cycle or fashion trend. Nevertheless fashions in decor do affect hotel restaurants in much the same way they do any other restaurant. Hotel public spaces (lobbies, banquet rooms, and the like) are also subject to aging in appearance and periodically require major refurbishing.

#### 7.8.4.5 Resort Life Cycle

Lundtorp and Wanhill (2001) refer to Butler's Resort Life cycletheory, which defines a life cyclefor a destination resort. The five stages in Butler's theory are the following:

A few tourists, simple facilities, unspoiled nature, and undisturbed local communities, characterise the first stage called **exploration**. In the next stage, **involvement**, the local community is engaged in tourism. Facilities and infrastructure are built, tourism associations are created, and the market is defined, which, in turn, increases the speed of tourism development. In the **development** stage, the destination is well defined. Attractions have been developed, promotional campaigns raise awareness and the novelty of the location is gradually falling away with the steady increase in tourist numbers. In the **consolidation** stage, the volume of tourists is still growing, but at a declining rate. The destination is now heavily marketed and tourism is very essential for the local economy, with an identifiable business district. Finally, at the fifth stage, **stagnation**, the highest number of tourists is achieved. The resort is no longer fashionable and there are evidently problems with environment, culture and the changes in the local structure of industry. At this stage the destination has two options, **Decline or Rejuvenation**.

#### 7.8.4.6 Hotel, Travel and Tourism Trends

Accommodation or lodging is, by a long way, the largest and ubiquitous sub-sector within the tourism economy, according to Cooper et al (1999: 131). Hotels are the most significant and visible sub-sector within the accommodation and lodging sectors. From this it would be evident that the opposite, being the foundation and direction that tourism gives to a successful hotel organisation or industry, is imperative to a feasibility analyst.

Since the Second World War there has been rapid growth worldwide in international tourism (Cooper, 1999). After the war, increasing proportions of the populations of the industrialised nations were in possession of both the time (in the form of paid leave from employment) and the money (owing to increased disposable incomes) to engage in international travel. Supply to meet this increased demand for leisure tourism in particular was developed mainly in the form of the standard, mass package tour. This was made possible by the arrival of the jet aircraft in 1958, and by cheap oil. Further, international travel was boosted by a substantial increase in business travel.

Over this period, international tourism has shown itself on a worldwide scale to be robust, showing resilience against such factors as terrorism and political unrest in many parts of the world, worldwide economic recession and fluctuating exchange rates. Generally, at times of economic growth, demand for travel has increased. On the other hand, during times of recession, demand has either remained constant or soon recovered. This global experience of almost uninterrupted growth is not, though, equally shared by all destinations. For example, tourists tend to stay away from destinations that they rightly or wrongly perceive to be unsafe (this has clearly affected tourism to the Middle East and North Africa). Other destinations might suffer because they are simply no longer fashionable.

Industrialised and developing countries have become aware of the potential of incoming tourism as an invisible export to support the current account of their balance of payments. In the 1990s, tourism accounted for up to 10% of world trade in goods and services, and can be considered to be one of the world's top three industries, along with oil and motor vehicles. Every day, well over one million people take an international trip.

## **Indicators of Tourism Demand**

### Travel Propensity

One of the most useful indicators of effective demand in any particular population is travel propensity. This measure simply considers the penetration of tourism trips in a population (Cooper, 1999).

There are two forms of travel propensity:

1. **Net travel propensity** refers to the percentage of the population that takes at least one tourism trip in a given period of time. In other words it is a measure of the penetration of travel among 'individuals' in the population. The suppressed and no demand components will therefore ensure that net travel propensity never approaches 100% and a figure of 70% or 80% is likely to be the maximum for developed Western economies.
2. **Gross travel propensity** gives the total number of tourism trips taken as a percentage of the population. This is a measure of the penetration of 'trips', not individual travellers. Clearly then, as second and third holidays increase in importance, so gross travel propensity becomes more relevant. Gross travel propensity can exceed 100% and often approaches 200% in some Western European countries where those participating in tourism may take more than one trip away from home per annum.

### Demand Schedules

In economic terms, a demand schedule refers to the quantities of a product that an individual wishes to purchase at different prices at a given point in time. Generally, the form of this relationship between price and quantity purchased is an inverse one, i.e. the higher the price of the product, the lower is the demand, and the lower the price, the greater is the demand.

### Patterns of Demand: The Regional Dimension

Regional tourism has to be viewed in the context of a greatly changing total, and so even a constant share represents substantial growth.

Cooper et al (1999) confirm that Europe and, to a lesser extent, the Americas have for some time dominated the international travel scene in terms of numbers of arrivals and receipts. More specifically, it is Western Europe and North America that have given rise to a high level of geographical concentration of movement. In 1990, Europe accounted for well over half of all international tourist arrivals, with the European Community (EC) alone hosting 40% of the total.

A number of factors can be identified which could explain Europe's leading position (Cooper et al, 1999: 51):

- Large segments of the population receive relatively high incomes, resulting in high levels of disposable income
- Paid leave from work is normal in European countries
- High proportions of the populations of, for example, Germany, France and the UK attach very high priority to the annual foreign holiday and are reluctant to let it go even in times of recession



- There is a wealth of both artificial and natural attractions
- Demand for foreign travel is satisfied by a large tourist industry and the necessary infrastructure
- International travel need not involve great distances, owing to the number of relatively small countries.

A number of these factors are equally applicable to North America. However, the sheer size of the USA and Canada means that the majority of their populations prefer to take domestic trips. Nevertheless, there are substantial numbers of North Americans who do engage in foreign travel each year, not merely within their own continent but also in long-haul trips.

The shares of Europe and the Americas have fluctuated somewhat over the years, with some evidence of a decline in terms of both numbers of arrivals and tourism receipts. The clearest trend though has been the emergence of countries in the East Asia and Pacific (EAP) region as both receivers and generators of international tourism. The EAP share of arrivals worldwide was only 1% in 1960, but grew to 3% in 1970, 7% in 1980 and 11% in 1990. The increasing share is of an expanding market. This represents remarkable growth in a highly competitive environment. Examples of countries in the EAP which have been part of this success are Hong Kong, Singapore, Thailand, Australia, Korea and Indonesia.

The shares of international tourism of Africa, the Middle East and South Asia have throughout the period 1950 to 1990 been small, though with a high level of fluctuation. As regions, they are not able to compete with Europe, the Americas and the EAP either in terms of generating or receiving large numbers of international tourists. The reasons for this are mainly economic. Destination countries within these regions can compete for specific markets from the major generating countries. Many, though, have been vulnerable to the effects of unrest and war, not necessarily in their own countries but near enough for them to be perceived as dangerous places to visit. In general, their incoming international tourism has suffered when business conditions have been depressed in the traditional tourism generating countries.

#### Patterns of Demand: Seasonality

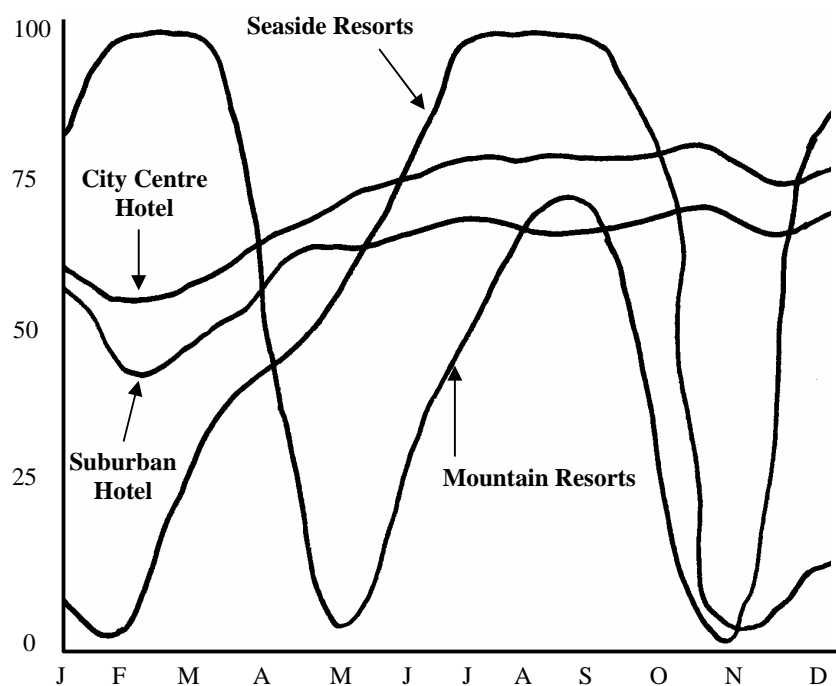
“We know that within most patterns of demand in tourism, there are regular fluctuations due solely to the time of year. This phenomenon is called seasonality. It is often the result of changes in climate over the calendar year. Thus a destination that is essentially attractive because of its beaches and hot summers is likely to have a highly seasonal demand. The same applies to demand for holidays at a ski resort that has snow for only part of the year. There are also other influencing factors, such as the timing of school and work holidays, or regular special events held at a destination.” (Cooper et al, 1999) This phenomenon is illustrated in figures 7.8.4.6(a) & (b).

Cooper et al (1999) further explains, that as tourism is a service industry, it is not possible to stockpile the product, i.e. a hotel room that is unsold on a particular night, an unsold seat on a flight or an unsold theatre ticket all have an economic value of zero. Seasonality of demand therefore causes major problems for the tourist industry. It can result in only seasonal employment for employees, and the under-use or even closing down of facilities at certain times of the year. It can also result in an over-stretching by some destinations and businesses at times of peak activity, to compensate for low demand in the off-season. This leads to overcrowding, over bookings, high prices and ultimately to customer dissatisfaction and a worsening reputation.

Various approaches exist to reduce responses to seasonality. Typically they involve attempts to create or shift demand to the shoulder or trough months, either through setting price differentials or through the introduction or enhancement of all-year facilities. Marketing may be targeted at groups that have the time and resources to travel at any time of the year, notably the elderly.

**Figure 7.8.4.6(a): Hotel Type Demand Level Comparison (Northern Hemisphere)**

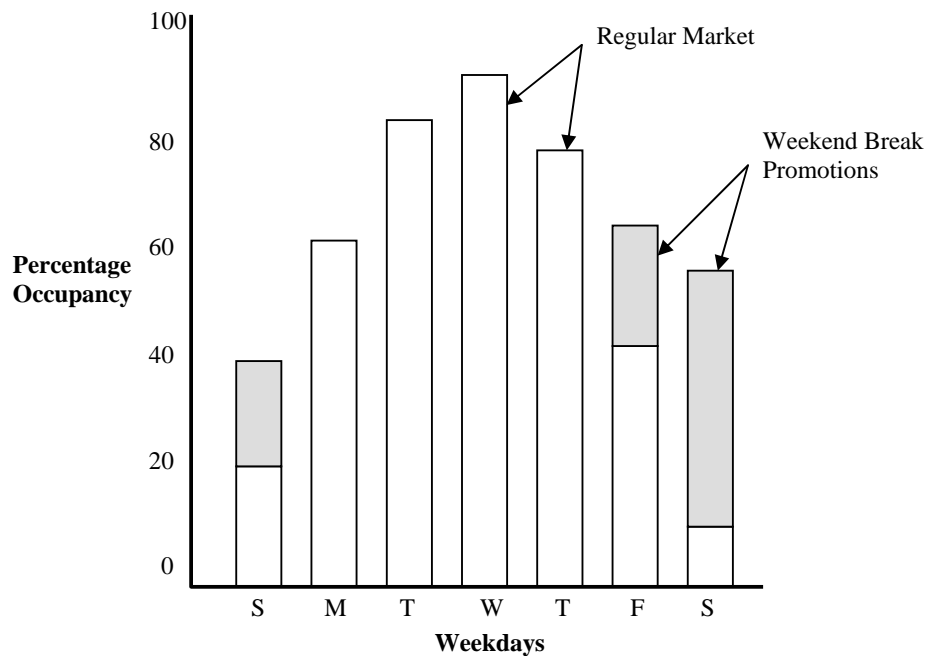
(Source: Lawson, 1997: 104)



In an analysis of monthly demand data, note is often taken of the number of days in the month. Even with identical daily demand in January and February, one would expect their monthly demand figures to differ by about 10%. There can be substantially different levels in demand for the tourism product on different days of the same week, depending on the precise business or activity involved (refer figure 7.8.4.6(b)). Hotels often experience differences in room bookings at weekends compared to weekdays. This is particularly the case where a hotel is able to fill with businesspeople during the week at high rates, and achieves at best only reasonable occupancy at weekends through special offers. In some parts of the world, Sundays are often 'dead' nights for large city-centre hotels. Attractions or recreation sites often attract more visitors during weekends than on weekdays.

**Figure 7.8.4.6(b): Typical Weekdays/Weekend Hotel Demand Fluctuation**

(Source: Lawson, 1997: 104)



#### 7.8.4.7 Urban Trends Analyses

Successful real estate investors understand the process of growth and decline in urban areas (Pyhrr et al, 1989: 373). They are aware of the many relationships between the growth and development of the urban area and the demand for various types of space, the basic product of the real estate industry. Knowledge of an urban area and its development processes provides a baseline for forming overall impressions of the area as a foundation for further research into investment potential. Certainly, population growth creates the need for additional housing and increases in office employment create the need for more office space. The same logic applies to space for industrial, retail, entertainment, lodging, and other types of real estate activity.

Investors should be aware of the impact of the legal, political, and sociological dimensions of an urban area on the demand for and the ability to provide space. For example, if increasing office employment is fuelling urban growth and many of these employees are young, well educated and affluent, the demand for particular housing types may increase much more rapidly than has historically been the case. The ability of the real estate industry to provide an adequate supply of types of space is related not only to the availability of land but also to the attitudes of the formal and informal power structures of the community towards growth and real estate development, and to the legal environment with respect to land use controls. Thus, the real estate investor must be attuned not only to the macro-development of the community but also to the many other factors that effectively shape the balance between the supply of and the demand for particular types of space.

For urban analysis the investor also needs to understand land use patterns within the area. Are there patterns of land use that indicate where various types of housing will likely be built in the future? Are there patterns in the location of hotel space, office space, shopping

space, and industrial space? If so, do these patterns satisfy space user and consumer demands, and are these patterns likely to continue? Why?

Specific urban trends that should be considered are:

#### Urban Economic Analysis

Changes in the economics of an urban area are directly related to the need for space of all types. Economic growth creates a demand for new office and industrial space for new employees to work in, homes for them to live in, and other types of space in which they can shop and be entertained. Associated with different types of employment are varying levels of income and expenditures by the employers and employees.

#### Urban Demographic Analysis

Demographics is the study of a population. The study begins with the compilation of the most reliable and current data available. Although much data is available through the various countries' bureaus of census, many independent research organisations also provide useful information. As used in real estate analysis, demographics is the study of the particular population characteristics considered important to the demand for particular types of space. Demographic analysis provides richer insights than a purely economic analysis by examining the size and composition of the population and the impact of economic change on these variables.

The urban demographic analysis should include population projections reflecting the population's assumed birth rate, death rate, levels of migration and immigration, household composition, mean population age, etc.

#### **7.8.4.8 Real Estate Cycles**

Similar to the hotel industry cycle, the property real estate market also has specific business cycles with four clearly identifiable phases, i.e. **overbuilding, adjustment, stabilisation and development**. As a result of overbuilding, demand begins to decline, absorption slows and rents weaken further, just as building peaks. Overbuilding is a consequence of prosperity that cannot last forever, precedes and then coincides with recession. The real estate market then continues to decline, occupancy diminishes further and rent concessions become widespread. New building is decidedly slowed during periods of recession and depression. This is followed by stabilisation, a period in which demand begins to increase despite declining construction, thus making inroads into the excess supply. This coincides with the depths of recession or depression and is the real estate equivalent of recovery. The last stage is development. As prosperity returns to the rest of the economy, occupancy is high, rents are rising, and absorption levels are high. Demand accelerates and new construction is needed to meet the increased demand. (Downs, 1991)

As an example, the building industry in South Africa shows unique characteristics that should be considered when making investment decisions about property developments. Building escalation costs, shortages of materials, skilled labour and professional expertise can have a severely negative effect on the financial merit of a property development.

#### 7.8.4.9 Inflation Cycles

Pyhrr et al (1989: 451) advises that the impact of inflation and real estate cycles should be an explicit consideration in the investor's analysis of specific properties, as well as the entire investment portfolio. The investor must learn to understand inflation and the cyclical factors that influence the value of investments, and the events that cause those factors to change. If the investor cannot develop such an understanding, his or her perceptions of the risks and returns involved are likely to be influenced greatly by incorrect reports in the media, i.e. the daily newspaper headlines, the opinions of the six o'clock newscasters, and other highly subjective and short-sighted analyses. As a result, the investor is more likely to follow the crowd and buy and sell properties at precisely the wrong times.

The key to understanding how inflation and cyclical activity affect investment returns and risks, is to understand how these macro-economic variables interact to change the microeconomic real estate variables, namely:

- Property values
- Rental income
- Vacancies and credit losses
- Operating expenses
- Debt-equity financing alternatives, amounts and terms
- The investor's required rate of return on investments
- The overall market capitalisation rate.

An understanding of interactions between macro-variables and micro-variables includes knowledge of macro-variability sources, linkages to micro-variables and sensitivity of each micro-variable to changes in each macro-variable. The knowledgeable investor can estimate values of these micro-variables over time using conventional discounted-cash-flow analysis, sensitivity analysis and risk analysis techniques. Thus, the investor can make investment decisions that will maximise returns relative to risk over time (i.e., maximise wealth). Furthermore, if estimates are made for a wide variety of real estate investments, as well as for non-real estate assets, the investor can begin to develop a strategy for shifting the portfolio to take advantage of cyclical developments.

It is Pyhrr et al's (1989) belief that economic history repeats itself. Rapid inflation and volatile real estate conditions are frequent in many countries. High rates of inflation were characteristic of more than 20 percent of this century. Falling business activity has been almost as frequent, occurring in more than 15 percent of the period since the mid-nineteenth century. Although history never repeats itself exactly, most real estate and business factors have shown consistent patterns for centuries. The serious real estate investor should study these patterns and consult others who have experienced many years of real estate inflation cycles. The first step towards understanding the impact of inflation on future real estate returns and risks is to understand its history.

#### 7.8.4.10 Other Cycles

There are, according to Pyhrr et al (1989: 490), a few more types of real estate cycles that may directly or indirectly affect investors' returns and risks:

- *Construction Cycle*: When money is plentiful and interest rates are low, builders build to satisfy the lean demand from the period of limited construction.

- *Mortgage Money Cycle*: The mortgage cycle is highly correlated with the business and construction cycle. During the contraction phase of the business cycle, federal/central bank reserve monetary controls almost always include credit controls in addition to tightening the money supply, which places upward pressure on interest rates. The opposite of the cycle would have an expanding effect owing to relaxation of monetary controls.
- *Neighbourhood Cycles*: Each neighbourhood has its own specific land use life cycle that affects real estate activities.
- *Property Specific Cycles*: Different types of properties are subject to different demand and supply relationships. As a result each city has a unique set of property-specific cycles in apartments, hotels, office buildings, retail and shopping centres, industrial buildings, etc.
- *Seasonal Cycles*: The timing of real estate transactions, with respect to the month or season, significantly affects the property's marketability, selling price, and terms of purchase and sale.
- *Property, Ownership and Investor Life Cycles*: Pyhrr et al (1989) conceptualises property life cycle as a eight stage pyramid that encompasses the entire development and holding period, from the inception stage through the demise and abandonment of the project at the end of its useful economic cycle.
- *Popularity Cycles*: Also referred to as the bandwagon or herd cycle, the popularity cycle typically occurs during boom-and-bust periods of real estate activity and is stimulated by the news media. If an investor is currently successful in a particular type of property, location or field, many others are attracted until the market becomes glutted. After a while those who cannot compete successfully, fall out of the market.
- *Social Change Cycles*: A real estate investor must continually analyse the basic social and cultural changes occurring in society and the possible implication on the changing real estate needs, returns and risks.

### 7.9 Physical Feasibility (Step 3)

Cloete (1998: 123) defines a physical feasibility study as an analysis of the suitability of the site for suggested development. It therefore is a match between the unique requirements of the proposed development and the unique characteristics of the specific site.

The physical feasibility study is limited to a site analysis of essential factors. The content of the study, according to Cloete (1998: 123 and 1995: 103) could be described under three headings, i.e. site characteristics, site location and environmental factors.

Contrary to Cloete and Pyhrr's approach, wherein the physical feasibility (including legal characteristics) is an independent analysis, Wurtzebach and Miles (1995: 681) include site analysis as part of the market study. These different approaches highlight a further important distinction that should be drawn between *physical site* feasibility and *locational* feasibility.

In contrast to the physical site analysis/feasibility as defined before by Cloete, the locational feasibility forms an integral part of the market analysis/feasibility. Raleigh and Roginsky (1999: 140) include the following definition of a locational evaluation in their explanation of current market analysis techniques:

*"A site evaluation includes an analysis of the location in terms of access, visibility, neighbourhood ambience, and proximity to lodging demand generators, as well as*

*competitive advantages and disadvantages of the property relative to the locations of existing and proposed competition.”*

In support of Raleigh and Roginsky, Ransley and Ingram (2000: 33), stipulate a few locational considerations for hotel feasibility:

- Population of the surrounding areas
- Major employers in the locality
- Tourism demand generator in the vicinity
- Passing trade
- Competition, etc.

A further ambiguity in the explanation of the physical feasibility study, is Pyhrr et al (1989: 430) and Cloete's (1995: 103) inclusion of a site's legal characteristics, which stands in contrast to Cloete (1998: 124) wherein a site's legal considerations form part of the political factors, which in turn is a subcomponent of socio-economic environment (macro-environment).

In light of the different physical feasibility structure opinions, and Ransley and Ingram's (1999: 68) statement that there is no single or uniform feasibility process, the following principles will be applied to all subsequent feasibility text:

- Cloete's (1995: 103) definition and explanation of physical feasibility, including legal consideration which directly apply to the site, will form the basis for the physical feasibility process, and
- Distinction will be drawn between location and locational characteristics. The distinction will be between factors that are directly associated with the site (location characteristics) and factors that influence the success of the business activities on the site (locational characteristics). Locational characteristics will be included in the market feasibility analysis and the location characteristics in the physical feasibility analysis.

## **7.9.1 Site Characteristics**

### **7.9.1.1 Site Description**

The site description must include the following:

- A statutory description of the property
- Site plan with form, size, measurements, servitudes, orientation, street fronts
- The local regulations applicable to the premises (zoning, coverage, height restriction, density, floor space ratio and building regulations).

### **7.9.1.2 Services**

The availability and adequacy of those services that are essential to the proposed development must be examined:

- Electricity
- Water
- Sewerage
- Stormwater removal, as well as

- Environmental services such as:
  - Refuse removal
  - Delivery of post
  - Fire brigade, and
  - Police services, must also be examined.

#### **7.9.1.3 Underground Factors**

Ground tests can determine the feasibility of a project. The plant life and nearby existing buildings should be observed, field trips, geological surveys and if possible, ground tests, should be undertaken to determine the foundation tests, while the height of the water table must be taken into consideration when basement levels are planned.

#### **7.9.1.4 Topography**

The topographical level of the site has important design and cost implications for the planned project. Information on the slope, contour lines, view and visual form must be gathered.

#### **7.9.1.5 Vegetation**

The distribution of the natural vegetation must be known in order to conserve it and to plant new plants for landscaping purposes.

### **7.9.2 Location Characteristics**

Two classes of location characteristics can be discerned:

#### **7.9.2.1 Accessibility**

- Method of transportation - hotels must be easily accessible, whether on foot, by car or public transport.
- Physical access - access points, traffic flow and pedestrian crossings determine the ease with which guests can reach their hotel.
- Travel anxiety refers partly to safety and ease of physical access and partly to attitudes created by the access zone.
- Travel costs, expressed in money or time.

The importance of access can be summarised as follows: the demand for premises in an urban area reflects the extent to which businesses or households are dependent on or can benefit from access. Access determines the rent or price that will be paid for premises with the required access qualities.

#### **7.9.2.2 Exposure of Site and Hotel Facilities**

Exposure refers to the visual impressions made by sight lines as well as by the accumulative impression created by the environment when the property is approached.



### **7.9.3 Environmental Factors**

#### **7.9.3.1 Climate**

The climate (macro as well as micro) of a specific site determines the orientation of buildings, the placing and size of windows, building materials and vegetation.

#### **7.9.3.2 Uses of Adjacent and Proximate Land**

Current and future uses of properties nearby or next to a residential areas are often of crucial importance to the success of the scheme. Disturbing factors such as pollution, noise and a state of disrepair have a negative effect on the marketability of the property.

#### **7.9.3.3 Environmental Impact of the Proposed Development**

Criticism is often levied that hotels and tourism development can destroy the attractiveness of a sensitive location. This must be balanced against the extensive economic benefits derived from tourism. Mindful of the need to constantly attract discriminating visitors, most designs carefully respond to their environmental settings whether this is to blend into the landscape or to make a dramatic statement in otherwise bland surroundings. (Lawson, 1996)

Determine the environmental impact of the proposed development. In certain cases (for example, ecologically sensitive areas) a formal and systematic environmental assessment may be required by law.

In addition to Cloete's generic physical feasibility explanation, addendum 'C' contains a "Hotel Feasibility, Appraisal, Valuation or Market Study Data Collection Checklist", which is an expanded checklist containing elements for a hotel development's physical feasibility study.

### **7.10 Market Feasibility Analysis (Step 4)**

A market analysis, according to Cloete (1998: 126), is the study of the supply and demand in the area studied with a view to determining whether a specific type of property is marketable.

The ultimate goal of the market study is to inform the hotel developer or operator of the effective demand for the hotel product at realistic price levels. This information lays the basis for the development decision (proceed or abort), and how much could be spent on the various cost components of the development.

Cloete (1998) further explains that a market analysis is done to identify the market for a specific product and is therefore aimed mainly at the future. Since each property is unique to a greater or lesser degree, and since it is furthermore easy to collect an almost endless amount of data that shows a relationship with the property market, a sensible decision must be made regarding the market parameters most relevant to the specific analysis.

Raleigh and Roginsky (1999: 137) express that a hotel market study should contain the following important sections:

- Introduction
- Area Review
- Lodging Supply and Demand Analyses
- Recommended Facilities (Proposed hotels only)
- Subject Property Penetration Analysis
- Financial Projections of the Subject Property

The above only serves as a very brief introduction. Owing to the extent and vast text constituting hotel market feasibility studies, a dedicated section (section 9) is included.

### **7.11 Financial Feasibility Analysis (Step 5)**

The last phase of the feasibility study determines whether the project, which conforms to physical, socio-economic and marketing norms and restrictions, will also comply with the developer's financial requirements. (Cloete, 1998)

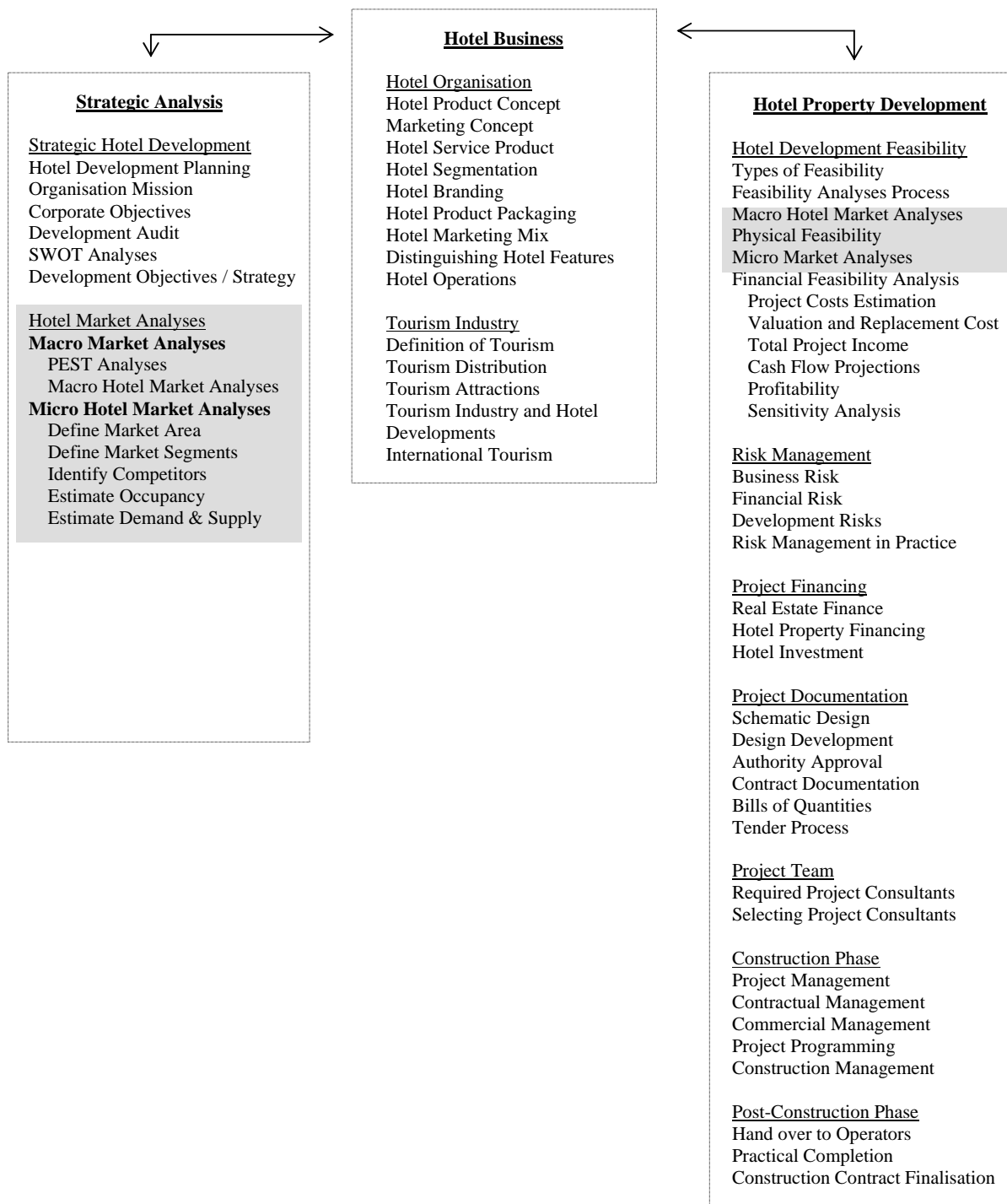
The financial feasibility study consists of five steps (Cloete, 1998: 128):

1. Estimate the total project cost
2. Estimate the total project income
3. A cash-flow projection for the investment period
4. Estimate the profitability of the project and compare the profitability with the investor's objective
5. Estimate the risks involved in the project (e.g. by doing a sensitivity analysis).

Similar to the section 7.9 (market feasibility) the above financial feasibility text only serves as a very brief introduction. Owing to the extent and vast text constituting hotel financial feasibility studies, a dedicated section (section 9) is included.

**Chapter 8:**

**Hotel Market Analyses**



## **8 Hotel Market Analyses**

### **8.1 Introduction to Hotel Market Studies**

Hotel consultants are regularly engaged by hotel owners, managers, developers and investors to conduct market studies for existing or proposed hotels. The goal of a hotel market study, according to Raleigh and Roginsky (1999:137) is to estimate the projected performance of an existing or proposed hotel. The projections are then relied upon to make development and/or investment decisions that often involve vast sums of money.

The question is asked whether anyone has a truly reliable crystal ball, to predict the future? The answer is obviously no. Nevertheless, hotel market studies will remain a necessary and essential component of any hotel investment. However, in order for hotel owners, managers, and investors to maximise the benefits of hotel market studies, there must be a clear understanding of what market studies do (and don't do), as well as the methodology and analytical techniques involved.

Rushmore and Baum (2001:77) advise that in performing hotel market feasibility studies, analysts are primarily interested in the micro, rather than the macro aspects of demand (refer to section 8.8). Micro demand for transient accommodation refers to the demand within a limited geographic area such as a town or city. By quantifying the micro demand into measurable units such as room nights, half of the supply and demand equation is known. Macro demand is much broader in scope and takes into account national and international travel patterns. Although macro demand receives only limited attention in most appraisal reports, it is an important consideration because it often foreshadows changes in travel trends for micro areas. Long-term macro supply trends often affect local hotels significantly, particularly with respect to hotel size, layout, design, chain affiliation, financial structure, and type of management. An understanding of the micro supply is needed to predict the relative competitiveness of area properties and to estimate the subject property's probable market share.

Owing to the dynamic nature of the lodging (hotel) industry and individual hotel markets, hotel market studies can be a useful analytical tool from the early stages of a hotel's development throughout its economic life. Too often a consultant is asked for a "quick and dirty" or "desktop" opinion that is subsequently perceived as a complete study when instead it is only an initial "gut" opinion. (Raleigh and Roginsky, 1999)

Rushmore and Baum (2001:25) state that each time a hotel is bought, sold, developed, financed, refinanced, syndicated or assessed, parties to the transaction may require some type of market study and valuation to indicate its future financial performance. Over the years the lodging industry has used a variety of terms to describe the process of forecasting the revenue and expenses of a property and estimating its market value. These studies may be called feasibility studies, market studies, market studies with financial projections, market demand studies, economic studies, economic feasibility studies, appraisals, valuations, economic valuations, economic market studies and appraisals, or market studies and valuations.

Although the studies identified by these names will generally produce similar findings, in this text the term *market study* will be used.

While the basic sections of hotel market studies are similar to the parts of any real estate analysis, the management intensiveness and financial complexities of hotel operations require a market analyst with proven experience in the hotel industry. Overall, a professional market study for a hotel investment represents the unbiased opinions and recommendations of an expert. As such, a market study mitigates the risk for both owners and investors because it forces a third, independent party to evaluate the potential of various hotel investment strategies. (Raleigh and Roginsky, 1999)

The following parties can benefit from the projections, conclusions and recommendations contained in hotel market studies:

### **Hotel Developers**

In the development process, a market study offers performance projections for a proposed hotel based on an analysis of the performance of existing competition, new supply additions, and current and projected lodging demand trends. Owing to the niche-specific nature of the hotel industry, a thorough analysis will include facilities recommendations for the proposed hotel including the type of lodging product (e.g., limited-service, full-service, extended-stay), a recommended guest-room inventory and the ancillary facilities/amenities that are expected to optimise performance. The proposed hotel's performance projections contained in the market study enable the developer to evaluate the economic feasibility of the proposed development. In addition, the Facilities Recommendations section of a market study can assist the developer in refining the architect's facilities program for a proposed development. The cash flow projections and returns forecast for a proposed hotel are often compared to the financial forecasts of alternative real estate developments at the same site to determine the highest and best use of a particular site and development.

### **Hotel Owners and/or Managers**

During the economic life of a hotel, a market study provides the owner or manager with projections that can be used to determine the viability of various investment and/or operational strategies related to the property. A market study evaluates the potential return on investments such as renovations, or managerial strategies such as yield management. Moreover, the projections presented in the market study may be used to help negotiate management or franchise contracts. Similarly, a market study is often a means of resolving a dispute between an owner and management-company, or a method of evaluating the performance of a management company.

### **Hotel Investors/Debt Partners**

A hotel market study provides a commercial lender with an unbiased assessment of a potential hotel investment. Often commercial lenders are not as familiar with local market conditions and/or the managerial aspects of a hotel operation as a qualified and experienced hotel consultant. In such cases, the consultant's report and follow-up discussions become a critical factor in the lender's risk analysis of a loan. Similarly, the cash flow projections in a market study may be used by a potential equity investor to determine the value of a hotel via a discounted cash flow analysis.

The basic supply and demand paradigm, which serves as the basis for a hotel market study, is well-known throughout the lodging industry. However, as hotel investments have

become increasingly complex, so have the analytical skills required of hotel analysts in completing engagements.

## **8.2 Hotel Market Study Framework**

If completed with adequate due diligence, a hotel market study can be an extremely useful tool in assessing the risk associated with a lodging investment. Adequate due diligence includes primary and secondary research, quantitative analyses and qualitative analyses. While the basic supply and demand paradigm of a hotel market analysis is generally understood, the complexity of today's hotel markets and investments often requires the application of more advanced analytical methodology. Each section of a hotel market study can be considered in terms of more thorough research and analytical techniques.

A well-documented market study typically, as defined by Raleigh and Roginsky (1999:138) contains the following seven sections:

1. Introduction
2. Area Review
3. Site/Neighbourhood Evaluation
4. Lodging Supply and Demand Analysis
5. Recommended Facilities (Proposed hotels only)
6. Subject Property Penetration Analysis
7. Financial Projections of the Subject Property

In Rushmore and Baum's definition (2001:25), a hotel market study is a six-step process:

1. Evaluate the hotel's site and locational characteristics
2. Quantify lodging demand
3. Evaluate competitive lodging supply
4. Measure property-specific characteristics (for an existing hotel)
5. Forecast revenue and expenses
6. Estimate market value.

## **8.3 Performing a Hotel Market Study**

Based on the hotel market study framework, explanations and definitions by Rushmore and Baum, and Raleigh and Roginsky, the following market study process and components are suggested.

- Introduction and Assignment Definition
- Macro Hotel Market Review
- Locational Analysis
- Micro Hotel Market Supply and Demand Analyses
- Proposed Hotel and Facilities Suitability Recommendations.

***Note: The following text in sections 8.4 to 8.7 is a close reproduction of Rushmore and Baum (2001: 104-145). The reason for this extensive quotation or reproduction is due to the technical and concise nature of the text, contained in their book.***

## 8.4 Market Study Assignment Introduction and Definition

The introduction of a hotel market study states the purpose of the engagement and any critical assumptions made by the third-party expert. Critical assumptions often include the development or renovation cost associated with a project, the opening or completion date of the hotel and the chain affiliation of the property. The more precisely the assumptions are stated, the more useful the study becomes for the reader. Of particular concern is the assumed chain affiliation of a property (hotel chain affiliations are not interchangeable and the assumption of a generic chain affiliation should be avoided). The revenue and expenses impact of one chain versus another varies significantly from market to market.

The market analyst/appraiser must define the assignment. Some questions that should be considered when defining a hotel market study and valuation assignment are:

- Where is the property located?
- Is the hotel existing or proposed?
- What facilities constitute the property (if it is existing)?
- What is the date of value?
- What is the purpose of the study?
- What property rights are to be appraised?
- Is there any excess land?
- Who will operate the hotel?
- What is the financial structure - debt and equity?

The answers to these questions are generally provided by the property owner or client and form the basis for defining the assignment.

Once the assignment has been defined, the analyst/appraiser begins to collect data. The collection process starts by determining exactly what type of data is required to complete the assignment. A data collection checklist is often employed to ensure that no essential information is overlooked (refer to addendum 'C'). The analysts must then determine where to look for each type of data. Typical data sources include:

- Information provided by the property owner or client
- Primary market research conducted in the field by the analyst
- Secondary research of in-house data and other secondary sources.

The data collection process should be thorough, accurate and all-inclusive. The results of the market study and valuation are only as accurate as the data collected.

## 8.5 Macro Hotel Market Review

The purpose of an area review is to identify and evaluate the economic factors and indices that influence hotel room night demand in the local market area. Relevant factors often include trends in office space absorption, convention centre events and delegate attendance, tourism counts, airport passenger statistics, etc.

Too often, however, this secondary research information is either outdated or of little relevance. For example, the date a community was founded, the breakdown of a community's population by age group, or the type of soil upon which the city rests has little or no bearing on the overall goal of the hotel market study. In addition to providing relevant

economic data, consultants must provide timely statistics. The information published by the local Chamber of Commerce is typically outdated, hence current trends (airport passenger statistics, tourism counts, etc.) must be researched by contacting the entity directly. In addition to providing timely data, this type of primary research often allows the researcher the opportunity to learn about potential or proposed changes to the economic catalysts of an area (i.e., an expansion of the airport or renovation of a tourist attraction).

For an extensive explanation of these macro hotel analyses factors, pertaining to macro hotel (transient) accommodation, refer to section 7.8.

### 8.6 Locational Analysis

Referring to section 7.9, you are reminded of the distinction drawn between location and locational characteristics. The distinction is between factors that are directly associated with the site (location characteristics) and factors that influence the success of the business activities on the site (locational characteristics).

A locational evaluation includes an analysis of the location in terms of visibility, neighbourhood ambience and proximity to lodging demand generators, as well as competitive advantages and disadvantages of the property relative to the locations of existing and proposed competition.

The location of a hotel must be appropriate to serve the needs of the intended market and satisfy a number of requirements, as illustrated by Lawson in table 8.6(a). The time-distance relationship is usually critical in determining the catchment area for hotel restaurants and other hotel amenities, in terms of travel convenience. This is illustrated in table 8.6(b).

**Table 8.6(a): Hotel Locational Requirements**

(Source: Lawson, 1997:108)

Key Factors	Considerations
Trading Advantage	Proximity to key attractions (beach frontage, recreational interests, fashionable shopping areas, etc)
Aspects	Vantage position (views of river, historic buildings, parks, recreational activities, etc)
Convenience	Time-distance, access, relationship to major highways and junctions, visibility, signing, etc.
Surroundings	Suitability of environment (attractive surroundings, quality of other buildings in vicinity, valuation of area, etc.)
Space	Land area for cost-efficient planning, design, car parking and recreational requirements.



**Table 8.6(b): Major and Complementary Hotel Markets**

(Source: Lawson, 1997:108)

Location	Major Markets (a)	Complementary Markets (b)
Resorts	Vacation tourists Recreationists	Incentive travel. Conventions. Special events. Out of season training
Towns/cities	Business travellers Conferences and meetings	Long and short vacations. Weekend packages. Exhibitions
Suburban	Business travellers Transient visitors	Visitors to locality. Social functions. Recreation clubs
Terminals	Passenger transfers Airline crews, etc.	Business meetings. Training sessions. Recreation clubs
Country houses	Business visitors Recreationists	Recreation clubs. Social events. Health and fitness treatments
<i>Notes:</i> (a) Typical characteristics. (b) Programmed to balance demand. May require higher investment in space and facilities and should be checked for feasibility.		

As an example, the importance of a hotel's locational decision, according to Kempinski Hotels, could be gathered from a security survey performed by them. The results show that security in a hotel's vicinity or location is the most important criteria for businesswomen in selecting a hotel for business travel.

The 150 women surveyed at the firm's deluxe properties in Dallas, Los Angeles, Montreal, Toronto and San Francisco indicated that a hotel's location was next on their list of importance, followed by clean rooms and reasonable cost.

### 8.7 Micro Hotel Demand Analysis

In preparing a hotel market study and appraisal, accurate quantification of micro demand is essential. The room night is the unit of measurement commonly employed.

A *room night* is defined as one transient room occupied by one or more persons for one night. For example, a business traveller who stays at a motel for three nights accounts for three room nights. A family that uses one room for three nights also generates three room nights. If this family had occupied two guestrooms during their stay, the demand generated would have been six room nights.

The total number of room nights within a defined market area represents the total potential demand, which can be measured daily, weekly, monthly, or yearly, depending on local travel patterns.

The total demand for transient accommodation within a micro market is primarily quantified by using the *build-up approach* based on an *analysis of lodging activity*. Supporting this is the *secondary build-up approach* based on an *analysis of demand generators*.

To apply the build-up approach based on an analysis of lodging activity, an area's transient room night demand is estimated by totalling the rooms actually occupied in local hotels. Through interviews with hotel operators, owners, and other knowledgeable individuals, occupancy levels for individual lodging operations and area occupancy trends can be established. The percentage of occupancy for each property times the available number of rooms is multiplied by 365 days to produce the total number of room nights actually

occupied each year. The area's total room night lodging demand can be quantified by combining the estimated number of occupied hotel rooms for each property and adding a factor for latent demand.

The build-up approach based on an analysis of demand generators, involves interviews and statistical sampling market research. Lodging demand is estimated by totalling the room nights generated from sources of transient visitation. Drawing from a sample of major transient generators located within a defined market area, interviews and surveys are conducted to determine the amount of demand each source attracts during a specified period. When this data is combined with other survey information such as facility preferences, price sensitivity, the nature of the demand, travel patterns, the analysis of demand generators provides both support and amplification for the findings derived from the analysis of lodging activity.

Analysts use a combination of the two procedures to save time and the effort of researching. In practice, an overall area demand is first established by analysing lodging activity. Then selective interviews are conducted at one or more major generators of visitation to verify the transient demand and establish traveller characteristics. By defining not only the quantity of transient demand but also its lodging characteristics, the analyst has enough data to develop a micro demand projection. Because each market area is unique, the analytic approach often must often be adjusted to account for particular demand characteristics.

### **8.7.1 Build-Up Approach Based on an Analysis of Lodging Activity**

The build-up approach is based on an analysis of lodging activity, which is performed in eight steps.

1. Define the primary market area.
2. Define the area's primary market segments.
3. Identify all primary and secondary competitive lodging facilities in the market area and determine their individual room counts and competitive weighting factors.
4. Estimate the percentage of occupancy for each competitive hotel or motel annually and determine the percentage relationship between each market segment and the entire market.
5. Quantify the accommodated room night demand by multiplying each property's room count by its annual occupancy and then by the 365 days in a year. Each property's total accommodated room night demand is then allocated to the primary market segments (i.e., commercial, meeting and group, and leisure) within the market area.
6. Estimate fair share, market share, and penetration factors for each of the competitors.
7. Estimate latent demand, which includes both unaccommodated and induced demand.
8. Quantify the area's total room night demand.

### 8.7.1.1 Define Primary Market Area

The first step in analysing lodging activity is to define the subject's market area. The market area for a lodging facility is the geographical region where the sources of transient demand (visitation) and the competitive supply are located. To delineate the boundaries of a market area, four factors must be considered:

1. Travel time between the source of visitation and the subject property
2. Methods of travel commonly used
3. Sources of transient visitation
4. Location of competitive lodging facilities.

Travel time is generally a better measure of distance than kilometres/miles because highways, road conditions and travel patterns differ. Most people are willing to travel up to 20 minutes to get from a source of visitation to their lodging accommodation. If most of visitors' travel time is spent on high-speed, interstate highways, the market area will be larger than if the route to the subject facility is along busy downtown streets.

The 20-minute market area radius is a rule of thumb that is usually appropriate for suburban areas. In rural regions the travel time radius can be significantly increased, sometimes to as much as four hours. Central business districts usually have a much shorter travel time radius of five to 10 minutes.

The transportation used also affects travel time. For example, a convenient rapid transit system can increase the market area by shortening the time needed to reach the subject property. Airport properties that depend on a shuttle bus service should consider visitors' waiting time. These hotels should be located no more than 10 minutes from the airport to allow for a 20-minute round trip.

The analyst should locate the subject property on a detailed road map and indicate points that could be reached within 20 minutes of travel time. Connecting these points creates an irregular circle, which represents the boundaries of the initial market area. To determine the actual shape of the final market area, certain adjustments must be made to show the influence of competition and other demand characteristics.

Before any modifications are made, however, all potential sources of transient visitation within the initial market area should be identified and located on the map. Any attraction that draws out-of-town travellers who require commercial lodging facilities, is a source of transient visitation. A representative list of visitation sources and the methods used to quantify their micro demand are presented later in this section.

After the initial market area has been determined, all competitive hotels should be located on the map and their positions with respect to the subject property and sources of visitation should be noted. Travellers tend to stay at the lodging facility closest to their destination, assuming the property meets certain requirements. If a comparable hotel is located between a source of demand and the property being analysed, the competitive facility may attract patrons (guests) first and the subject hotel will receive the overflow. Care must be taken to evaluate the competition's drawing power because travellers will bypass one facility for another if it better suits their needs and budgets. The location of competitive properties between the property being appraised and the attraction generating business can decrease

the size of the initial market area and may even eliminate some sources of visitation from consideration.

Local travel patterns and popular routes are important factors to consider when evaluating the competition. Travellers usually prefer to travel familiar routes and are not inclined to venture into unfamiliar areas. If the customary route to a source of demand happens to bypass the subject property, its potential for capturing that market is greatly reduced. The location of one or more comparable lodging facilities along the route, also decreases the subject property's drawing power. Traffic counts, origination and destination studies prepared by state and local agencies can help pinpoint popular routes and identify area travel patterns. By plotting this information on the map showing the initial market area, appropriate adjustments can be made to the boundaries indicated. The resulting enclosure is the final market area and contains the sources of transient visitation available to the subject property.

### **8.7.1.2 Define Market Segments**

Once the market area has been outlined, the analyser should determine the primary segments of transient demand using local hotels. The three market segments found in most areas are commercial, meeting and group, and leisure. Other market segments that are sometimes considered include extended-stay, government, airline crews, sports teams, military, truck drivers and cruise ships.

Market segmentation is useful because individual market segments exhibit unique characteristics relating to future growth potential, seasonal aspects of demand, average length of stay, rates of double occupancy, facility requirements, price sensitivity and other factors. Once the room night demand has been quantified by market segment and the individual characteristics of each segment have been defined, the future demand for transient accommodation can be more accurately forecast by making separate projections for each market segment. Some unique characteristics of the major market segments are described below.

*Refer to addendum 'B' – Characteristics of Hotel Market Segments, for extensive statistics and characteristics of the various guest profiles.*

#### **8.7.1.2.1 Commercial Segment**

The commercial market segment is composed of individual business people visiting the various firms within a market area. Commercial demand is strongest Monday through Thursday nights, declining significantly on Friday and Saturday and increasing somewhat on Sunday (also refer to section 7.8.6.4, in this regard). A typical stay ranges from one to three days and the rate of double occupancy is low at 1.2 to 1.3 persons per room. Commercial demand is relatively constant throughout the year, with some drop-off in late December and during other holiday periods. Individual business travellers are not overly price-sensitive and usually use a hotel's food, beverage and recreational facilities. Commercial travellers usually represent a desirable and lucrative market segment for hotels because such guests provide a consistent demand at room rates approaching the upper limit for the area.

#### **8.7.1.2.2 Meeting and Group Segment**

The meeting and group market includes individuals attending meetings, seminars, trade association shows and similar gatherings for 10 or more people. Peak convention demand typically occurs in the spring and fall. Because many people take summer vacations, the summer months are the slowest period for this market segment (winter demand varies) (also refer to section 7.8.6.4, in this regard). The average stay for typical meeting and group travellers ranges from three to five days. Most commercial groups hold meetings Monday through Thursday, but associations and social groups sometimes meet on weekends. Commercial groups tend to have a low double occupancy of 1.3 to 1.5 persons per room, while social groups are likely to have somewhat higher double occupancy rates ranging from 1.5 to 1.9 persons per room. Hotels and motels often profit from meeting and group patronage. Although room rates are sometimes discounted for large groups, hotels benefit from the use of meeting space and the inclusion of in-house banquets and cocktail receptions.

#### **8.7.1.2.3 Leisure Segment**

The leisure segment consists of individuals and families spending time in the area or passing through en route to other destinations. Their purposes for travel may include sightseeing, recreation, relaxation, visiting friends and relatives, or other non-business activities. Leisure demand is strongest Friday through Saturday nights and all week during holiday periods and summer months. These peak periods of demand are negatively correlated with commercial visitation patterns, demonstrating the stabilising effect on occupancy produced by capturing weekend and summer tourist travel (also refer to section 7.8.6.4, in this regard). The typical length of stay for the leisure traveller ranges from one to four days, depending on the destination and the purpose of travel. The rate of double occupancy is often high - 1.8 to 2.5 people per room. Leisure travellers constitute the most price-sensitive segment of the lodging market. Many prefer low-rise accommodation with adjacent parking. Vacationers typically demand extensive recreational facilities and amenities. Highway accessibility and distance to vacation-related attractions are important considerations for vacationers choosing a location.

#### **8.7.1.3 Identify Primary and Secondary Competition, Room Counts and Competitive Weighting Factors**

The primary and secondary competitive lodging facilities located within a market area are part of the overall lodging supply, which can be defined as all transient accommodation catering to overnight visitors. Transient accommodation includes hotels, motels, conference centres, bed and breakfasts, rooming houses, health spas, and other facilities. Although all transient lodging facilities operating in the same market area compete with one another to some extent, only those that are considered primary or secondary competition are included in the lodging analysis.

Hotels that are similar to the subject property (in terms of their class and facilities) and that appeals to the same type of transient visitor are considered primary competitive lodging facilities. Secondary competition consists of lodging facilities that would not normally attract the same type of transient visitor but become competitive because of special circumstances.

Determining which hotels represent primary or secondary competition and which provide no competition at all, is largely subjective. Relative competitiveness can be evaluated by looking at area demand and identifying the different types of accommodation that transient visitors are selecting. Alternatively, competitive supply can be examined to identify accommodation that is similar to the subject in their market orientation (i.e., facilities, class, image, location and other characteristics).

Demand generator interviews can provide information about the types of accommodation market area travellers are using. The responses to interview questions should allow the analyst to pinpoint which lodging facilities are competitive with each other and why.

To evaluate the similarities of facilities and the market orientation of the hotels that make up the lodging supply, an analyst may visit each property and judge its competitiveness using specific criteria. The following questions could be used to judge whether a lodging facility represents primary or secondary competition or does not compete with the subject property at all.

- Does the hotel occupy a similar location? Is it within 20 travel minutes of the demand generators? Is it identified with a specialised location such as an airport, convention centre, downtown area or resort?
- Is the hotel similar in terms of the types of facilities offered? Specialised types of hotels include convention, resort, suite, residence, conference centre, casino and health spa.
- Does the hotel offer similar amenities? Amenities may include restaurants, lounges, meeting rooms, pools (indoor or outdoor), health spas, tennis courts, and golf courses.
- Is the hotel similar in class, i.e. quality and price? Classes of lodging facilities include luxury, first-class, standard/mid-rate, economy/budget and hard budget.
- Is the hotel similar in image? Image refers to the hotel's brand name, local reputation, management expertise and unique characteristics.

Area hotels can be considered *primary competition* if they are similar to the subject property with respect to many of these criteria, particularly those related to types of facilities, class and image. *Secondary competition* would include hotels that are similar in location-related characteristics but meet few of the other criteria, particularly class and image. Secondary properties are considered competitive because they occasionally attract the same market or travellers that the subject property and other primary competitors do.

When all primarily competitive hotels are sold out, travellers desiring this type of accommodation must settle for a secondarily competitive property. If, for example, a traveller wanted an upscale, first-class hotel, a budget property would be the secondary alternative. A budget traveller who found all the economy properties filled, might have to patronise a first-class facility.

A secondary competitor is sometimes in demand because it has a particularly good location. A secondary property adjacent to a demand generator may do good business in inclement weather when people want to stay at the first hotel they see.

Generally a secondary hotel is not as competitive as a primary property is. To reflect this lesser degree of competitiveness, an analyst will assign a weighting factor to a secondary property, which reduces the hotel's room count. For example, a 100-room, secondary hotel that is considered to be 25% competitive with the subject property is assumed to have an effective room count of only 25 rooms. This assumption not only reduces the existing

supply of competitive hotel rooms, it also lowers the area's current room night demand. If the analyst determines that more than one hotel can be considered secondarily competitive, then all of the secondary properties are typically combined into a single hotel using a weighted-average calculation in the market analysis.

Usually a few hotels in the market area offer no competition to the subject property and are therefore not considered in the analysis of lodging activity. These properties are often so dissimilar to the subject property that any crossover of demand would be highly unlikely. Most travellers would probably defer their trip if they were unable to obtain accommodation in either the primary or secondary competitive properties.

To quantify hotel room night demand using the build-up approach based on lodging activity, it is necessary to determine the room counts of all competitive hotels. This information can be obtained directly from the properties or from various lodging directories. The room counts of any hotels that opened during the 12-month base year must be adjusted based on estimates of occupancy and market segmentation. For example, a 124-room hotel that opened within the base year period, which extended from January 1 to December 31, would be calculated in the following manner: Say, for example the hotel only operated for six months of the base year period, its historic average room count (HARC) is 62 rooms ( $50\% \times 124 = 62$ ).

The *historic average room count* is the hotel's room count multiplied by the percentage of the base year that the property is actually open. In addition to weighting the impact of new hotels on the market, the HARC can also be used to adjust the room counts of seasonal properties that close for a portion of the year and existing hotels that add new rooms during the base year.

#### **8.7.1.4 Estimate Occupancy and Determine Market Segmentation**

The key ingredient in the build-up approach based on an analysis of lodging activity is the occupancy estimate for each of the primary and secondary competitive hotels in the market area. The estimate of competitive occupancies should cover a full, 12-month period. Ideally this period, which is called the *base year*, will closely precede the first year projected in the supply and demand analysis.

When collecting occupancy and average room rate data, the analyst should be aware of several factors that could skew the data and cause errors in the analysis. For example, occupancy is calculated as the number of rooms occupied over a period of time divided by the number of rooms available. The analyst should first understand how the hotel defines "rooms." Generally, a room is synonymous with the term *hotel unit*, which is the smallest accommodation that can be rented to a guest. Each unit must have a full bath and its own entrance to a public hallway or to the exterior. Some hotel units are composed of two rooms, but since such a unit may have only one entrance or one bath, it would be impossible to rent it to two unrelated parties. If, on the other hand, each room has its own bath and entrance and the connection between the two rooms can be locked, then each room could be considered a separate unit.

The second factor to be examined in gathering occupancy data is how the hotel handles complimentary rooms. Most hotels have a small percentage of rooms that are provided on a complimentary basis to hotel guests. Since these rooms do not generate rooms revenue, they are sometimes omitted from the hotel's occupancy calculation. However, they do

represent a form of hotel utilisation and should be included in the calculations when the lodging activity approach is used to quantify hotel room night demand. The analyst should therefore always ask for the percentage of occupancy that includes complimentary rooms. The inclusion of complimentary rooms also affects the calculation of average room rate, which will be discussed later.

The need to divide the market's overall room night demand into individual market segments has already been discussed. In applying the lodging activity approach, market segmentation is determined by interviewing competitive management about the percentage relationship of each market segment to the whole market. This information is usually not considered confidential and should be easily obtained from each of the hotels. The analyst must define the market segments in detail before asking about percentage relationships so the interviewee will understand and employ the same basis in allocating the hotel's occupied rooms. The percentages should total 100% when all segments are considered.

### 8.7.1.5 Quantify Accommodated Room Night Demand

The current accommodated room night demand for each market segment is calculated separately for each competitive hotel using the following equation:

$$\begin{aligned} &\text{Historic average room count} \\ &\times (\text{multiply by}) \text{ occupancy} \\ &\times (\text{multiply by}) \text{ market segmentation} \\ &\times (\text{multiply by}) 365 = \text{Total accommodated room night demand} \end{aligned}$$

The number of occupied rooms per market segment for all of the competitive hotels in the market area is then combined to yield the area's current accommodated room night demand. The accommodated room night demand represents the actual number of competitive rooms occupied during the base year. Table 8.6.1.5(a) shows the estimated accommodated room night demand divided by market segment.

**Table 8.6.1.5(a): Accommodated Room Night Demand**

(Source: Rushmore and Baum, 2001:120)

Hotel	HARC	Occu-pancy	Market Segment			Market Segmentation		
			Com-mercial	Meeting and Group	Lei-sure	Com-mercial	Meeting and Group	Leisure
Embassy Suites	200	78%	80%	5%	15%	45,552	2,847	8,541
Hilton	275	72	40	50	10	28,908	6,135	7,227
Radisson Hotel	250	68	45	40	15	27,923	24,820	9,308
Holiday Inn	175	73	55	25	20	25,646	11,657	9,326
Courtyard	62	65	75	5	20	11,032	735	2,942
Ramada Inn	150	66	65	20	15	23,488	7,227	5,420
Island Inn	135	62	60	30	10	18,330	9,165	3,055
Quality Inn	175	78	50	10	40	24,911	4,982	19,929
Days Inn	120	74	70	5	25	22,688	1,621	8,103
Secondary competition	420	75	64	14	22	73,820	16,148	25,376
Accommodated room night demand						302,298	115,337	99,227
Percent of total						58%	22%	19%



### **8.7.1.6 Fair Share, Market Share and Penetration Factors**

Each competitive hotel's historical performance may be judged by comparing the respective occupancy rates. A statistical measure of each hotel's performance is called the *penetration factor*, which relates a specific hotel's performance (both overall and by segment) to that of the market at large. The penetration factor calculation is based on each hotel's fair share, which simply equates to a given property's room count divided by the market-wide room count. The fair share percentage functions as the denominator in all penetration factor calculations, whereas market share is the numerator. Market share represents that portion of demand actually accommodated by a particular property (either overall or by segment), divided by market-wide demand. Market share divided by fair share results in a penetration factor.

### **8.7.1.7 Estimate Latent Demand**

The area's current accommodated room night demand is based on actual occupancies and accounts for only those hotel rooms that guests have used. It does not consider other types of demand that may have been present in the market but, for one reason or another, have not been accommodated by the current supply of lodging facilities. This additional demand is called *latent demand* and is composed of both unaccommodated demand and induced demand.

#### **8.7.1.7.1 Unaccommodated Demand**

Unaccommodated demand represents transient travellers who seek accommodation within a market area but, because all local lodging facilities are full, must defer their trips, settle for less desirable accommodation, or stay outside the market area.

Since this type of demand is not actually accommodated by the area's lodging facilities, it is not included in the room nights quantified in the previous steps of the lodging activity approach.

Unaccommodated demand is actually a form of excess demand that develops as a result of the hotel business's cyclical nature. For example, in markets dominated by commercial demand, area occupancy levels Monday through Thursday often approach 100%, indicating that many travellers are not being accommodated locally. Many resort market areas also sell out during peak vacation periods, thereby generating unaccommodated room night demand. Because hotels cannot expand or contract in response to cyclical lodging demand, unaccommodated transient visitation is normal in many market areas.

In quantifying the current hotel room night demand, unaccommodated demand only becomes a factor when the number of competitive rooms in the market increases. As the supply of hotel rooms increases, more of the previously unaccommodated demand will be accommodated during periods of peak visitation. Since these uncounted room nights will help offset the impact of new rooms entering the market, it is important to quantify the number of unaccommodated travellers trying to use lodging facilities in the area.

Quantifying the room nights that are not being accommodated in a market is difficult and requires experience and good judgment. The following list outlines factors that should be considered when deriving this type of estimate:

- *The nature of the demand:* Is the area demand cyclical and concentrated at certain times (e.g. Monday through Thursday, vacation periods, special events)?
- *Area occupancy:* Considering the nature of the area's transient demand, are most of the local lodging facilities operating at stabilised levels of occupancy? For example, in a typical, commercially orientated market where lodging demand is high Monday through Thursday and drops considerably over the weekend, one might expect that a strong stabilised level of occupancy would be approximately 70%. Under these circumstances an area-wide occupancy of 78% could produce a significant amount of unaccommodated demand. If most of the area's hotels are operating at 60% occupancy, however, the amount of the unaccommodated demand will probably be negligible.
- *Fill nights:* How many fill nights are area hotels experiencing? In conducting competitive interviews the analyst should try to determine the number of nights area hotels are actually filled to capacity. Once this number has been established, the number of turn-away room nights can be quantified. Sometimes hotels with centralised reservation systems keep monthly denial reports, which show the number of people who called to make reservations at a specific hotel but were denied because the property was booked. Occasionally individual hotels also track the number of walk-ins turned away on days when the hotel is fully booked.
- *Alternative accommodation:* If it appears that a sizeable amount of unaccommodated demand exists in an area, the analyst might want to conduct interviews at alternative accommodation to identify the sources of their demand and to determine if any of the customers would choose other facilities if they were available. Alternative accommodation might include lodging facilities outside the market area or hotels within the area that are considered less desirable.

In most instances data on fill nights and turn-away frequency is not available. Analysts should try to obtain as much information as possible, but they must be prepared to estimate unaccommodated room night demand without a strong factual basis. The analyst's experience plays an important role in quantifying unaccommodated demand. By observing numerous market areas that have experienced cycles of building, declining occupancies, and recovery, analysts can develop an appropriate estimate of unaccommodated demand.

Unaccommodated demand is estimated as a percentage of the accommodated demand for each market segment. The range for unaccommodated demand typically extends from 0% to 30% of accommodated demand. The high end of this range would be appropriate for exceptionally strong markets where nearly every hotel is experiencing high levels of occupancy, many fill nights and a large amount of turn-away demand. In strong hotel markets 5% to 10% is a reasonable level of unaccommodated demand. Since unaccommodated demand is difficult to quantify, a conservative estimate is usually warranted.

Unaccommodated demand is brought into the market analysis as accommodated demand when there are sufficient new rooms available to absorb this form of latent demand. Care must be taken to ensure that the amount of unaccommodated demand converted into accommodated demand is justified by the number of new rooms opening in the market. The capacity (new rooms) available to convert unaccommodated demand into accommodated demand is called the *accommodatable latent demand*.

#### **8.7.1.7.2 Induced Demand**

Induced demand is the second type of latent demand. It represents the additional room nights that will be attracted to the market area. Induced demand may be created by specific circumstances such as:

- *The opening of new hotels that offer new amenities, including extensive meeting and group space and specialised recreational amenities such as golf courses, ski slopes, or a health spa:* These hotels are expected to attract a new market segment that does not currently seek accommodation in the subject's market area. For example, if a new hotel with a 60,000-square-foot exhibit hall opens in a market that does not have a similar facility, this hotel will probably attract into the area groups that had previously selected hotels elsewhere.
- *The aggressive marketing efforts of individual properties:* Some major hotel chains have been able to bring new room nights into the market by aggressively marketing the properties they operate. Convention-orientated lodging chains frequently are able to move convention groups around to various hotels within their systems, thereby creating induced demand for any new hotels they operate.
- *The opening of a new major demand generator such as a convention centre, commercial enterprise, retail complex, transportation facility or recreational attraction:* The development of Disney World is an example of an induced demand generator. Airport expansions commonly induce new demand, particularly if the facility develops as a major hub for many airlines.

Because induced demand can be traced to one or more specific factors, quantifying these additional room nights is somewhat easier than estimating unaccommodated demand. The procedure used is similar to the build-up approach based on an analysis of demand generators. The analyst evaluates each generator of induced demand to determine the number of room nights that will be attracted to the market area. Induced demand may either enter the market all at once or gradually.

Induced demand is occasionally factored into the market on a temporary basis. Examples of this scenario involve one-time or cyclical events hosted by a given lodging market, such as the Olympics and the Super Bowl. Movie crews in town for extended shoots are another common example of temporary induced demand. In such cases, analysts must factor the associated demand levels in and out of the projections at the appropriate times. Unaccommodated demand and induced demand combined, equal the total latent demand for the market area.

#### **8.7.1.8 Quantify Total Room Night Demand**

Totalling the area's existing and potential room night demand is the last step in the build-up approach based on an analysis of lodging activity. This demand includes both accommodated and latent demand, which have been identified in the preceding steps.

## 8.7.2 Build-up Approach Based on an Analysis of Demand Generators

In markets with few demand generators, it is sometimes appropriate to quantify the existing hotel room night demand by interviewing demand generators. As markets become more complex and the number of generators increases, it becomes more difficult to identify all of the demand generators and conduct an accurate survey. Most markets are too complex to rely solely on this approach, so the analysis of lodging activity is usually emphasised and selective demand generator interviews are used to determine the characteristics of the transient demand.

The build-up approach based on an analysis of demand generators is typically performed in three steps:

1. Identify generators of transient visitation.
2. Interview or survey selected demand generators and identify the characteristics of the demand.
3. Quantify room night demand.

Each step in the analysis of demand generators is discussed in the following sections.

### 8.7.2.1 Identify Generators of Transient Visitation

The generators of transient visitation are identified when the final market area is defined. There may be many sources of transient visitation and efforts should be made to compile a complete list. The following methods can be used to identify generators of hotel demand:

1. *Interview local hotel and motel managers to determine the sources of their occupancy.* Ask for a percentage breakdown on the types of customers (i.e., commercial, convention, leisure) and try to learn the names of firms or groups that use the facility regularly.
2. *Obtain a directory of local businesses and identify those with regional or national operations that are likely to attract out-of-town customers, suppliers, vendors or company representatives.*
3. *Obtain statistics pertaining to area visitation from the local convention and visitors bureau.* Request a list of recent conventions and meetings that used local hotels. Determine if the primary market area has any popular tourist or vacation attractions. Visitor counts and projections can be helpful if their reliability can be verified.
4. *Visit car rental agencies, especially those at local airports, to determine which firms regularly rent cars.* This information will indicate which area businesses attract out-of-town visitors. These agencies can also supply information about which hotels are popular among their clients.
5. *Drive around the area looking for concentrations of out-of-state cars in industrial parks, office complexes, government centres, regional hospitals and other facilities.* Parking lots at local hotels also contain many market indicators. Do most of the cars belong to out-of-state or in-state residents? Do they belong to businessmen travelling alone (clean and neat) or families on vacation (with luggage, games and roadmaps)? A late-night parking lot count can indicate a highway motel's occupancy, assuming one vehicle per room. Even more important, a parking lot count can indicate the relative competitiveness of area hotels if all are surveyed on the same night. One night's count is not necessarily indicative of annual occupancy, so additional factors should also be considered.

6. *Interview chamber of commerce officials, visitor information centre employees, taxi drivers, gas (petrol filling) station operators and restaurant managers.* They can help identify potential sources of transient visitation. The local building department can also provide information on proposed projects and changes in highway patterns.

Identifying the prime demand generators within a market area is relatively simple. When the survey is completed, the list will probably contain one or more of the following:

- Businesses, i.e. office buildings, industrial parks, research facilities and manufacturing plants
- Government centres
- Airports
- Convention centres and conference facilities
- Colleges and universities
- Tourist attractions
- Vacation and recreation areas
- Parks and scenic areas
- Hospitals
- Sports attractions
- Casinos
- Military bases
- Trade and professional associations
- Convenient highway stopping points
- Regional shopping centres
- Special events, state fairs and parades.

For market areas with many demand generators, the list should rank the sources in order of their estimated potential to generate demand. Prime sources with the greatest ability to attract out-of-town visitors should be researched first so that the analyst can conduct a thorough analysis.

#### **8.7.2.2 Interview or Survey Selected Demand Generators**

Quantifying the total demand into measurable units, i.e. room nights, is the most important step in the survey process. By estimating the number of room nights attributable to each generator of visitation in the subject market area, the total micro demand can be determined.

In addition to quantifying total demand, the analyst's survey should outline the general characteristics of the travellers who make up the potential market. The following list indicates factors that can help define the demand and may be useful in designing a proposed hotel:

##### **8.7.2.2.1 Demand Factors**

- Number of nights per stay
- Number of people per room
- Periods of use during the year

- Definition of seasonality
  - Fluctuations in use during the year
  - Fluctuations in use during the month
  - Fluctuations in use during the week
- Price willing to pay
- Food, beverage, entertainment and telephone usage.

#### 8.7.2.2.2 Design Factors

- Number of people per guestroom
  - Space requirements
  - Bed requirements
  - Bathroom requirements
  - Closet and storage requirements
- Use of guestrooms for purposes other than sleeping (i.e. meetings, entertainment, interviewing or displays)
  - Space requirements
  - Furniture and layout
  - Lighting and decor
- Restaurant and lounge facilities
  - Space requirements
  - Decor, menu and price
  - Kitchen equipment
  - Staffing
- Meeting and banquet facilities
  - Space requirements
  - Types of configuration
  - Special equipment
- Methods of travel
  - Parking requirements
  - Entrance, loading and baggage requirements
- Recreational facilities.

The list of demand generators must be analysed in order to select market-surveying techniques that will be most effective in quantifying potential demand and defining specific traveller characteristics. Research techniques may include personal and telephone interviews, questionnaires, and the use of available data and surveys.

Regardless of the techniques chosen, it is most important to locate and question the individuals most knowledgeable on the subject. For a hotel demand study, these people are typically those who make hotel reservations, e.g. secretaries, executive transfer departments, travel departments, personnel and recruitment departments, convention and visitors' bureau placement departments, tour operators and travel agents, airline flight service and customer relations departments, and college alumni and athletic offices. (The people who actually book reservations for out-of-town visitors are called *bookers*). Purchasing agents and buyers, executives, receptionists, college admissions officers and park rangers who greet out-of-town visitors might also be questioned. Security departments, convention and visitors' bureau registration and research departments and hospital admission departments that control visitation data are other good sources. (People who see and come into contact with out-of-town visitors are called *seers*).

Personal interviews produce the most reliable data, but they are usually time consuming. In areas with many sources of visitation, personal interviews can be limited to those with the greatest potential for generating room nights. A checklist of essential items to cover should be devised and interview time should be limited to five or 10 minutes. Use appointments only if an initial drop-in visit produces no results.

Key questions typically asked during an interview include:

- How many out-of-town visitors do you average each week, month, or year?
- What is the purpose of the visitation?
- How long do the visitors stay?
- Are the visitors visiting any other demand sources in the area?
- Where are the visitors staying now?
- What rates are they willing to pay?

Once these questions are answered, more detailed questions should be asked to identify some of the market's characteristics. The interviewer should always ask if any other people in the organisation have contact with visitors. The interviewer should also specify the interview's purpose, because the more information the interviewer is willing to provide, the more information the interviewer will receive.

Telephone interviews are less time-consuming but rarely produce the same quality of data. Less important demand sources can be interviewed over the phone and later seen personally if greater potential is discovered.

Questionnaires, on the other hand, are useful for mass surveys when hundreds of identifiable demand generators are involved. A short, simple form that can be completed in less than five minutes usually yields the best results. It is important to contact the person best suited to answer the questions when using this type of survey. A brief letter explaining the survey's purpose should accompany each questionnaire. A greater response will be obtained if someone who is well-known in the community signs the letter. A self-addressed, stamped envelope for returning replies must be enclosed.

Occasionally, various groups and municipal agencies compile data pertaining to local transient demand. These data are usually part of larger studies conducted in connection with urban renewal or redevelopment projects, proposed convention centres and master development plans. Organisations that may perform such market surveys include chambers of commerce, convention bureaus, municipal planning departments, redevelopment agencies, financial institutions and utility companies. Data obtained from these sources should be verified. If the information is usable it can serve as a starting point for defining the local transient market.

All major generators of transient visitation should be surveyed with a personal or telephone interview or a mailed questionnaire. In market areas with many secondary generators of visitation, however, these techniques may not be practical. Time restraints and the inability to identify smaller generators often require some form of sampling.

### **8.7.2.3 Quantify Room Night Demand**

Sampling is a market research procedure in which conclusions about a large population are drawn from a thorough analysis of a representative portion of the population. Properly applied, sampling can yield more accurate results than complete surveys can because more time can be devoted to correct interviewing and data collection techniques.

Selecting the unit of comparison that best reflects the total market is the key to proper sampling. Counting room nights per square metre of office space is one frequently used measure for determining potential commercial traveller demand. Interviewing a representative sample of office space users and estimating how many out-of-town visitors are received over a given period can be used to develop a unit of comparison. The number of visitor room nights is divided by the total square meters of office space within the sample. Multiplying this factor by the amount of office space within the market area produces an indication of the potential commercial demand. If necessary, adjustments can be made to avoid double counting of travellers visiting more than one firm.

Other units of comparison that may reflect transient visitation include population, employment, university enrolment, hospital beds, traffic counts, retail sales and convention attendance. Many books have been written about correct sampling and market research procedures. Although every market area requires a somewhat specialised approach, three basic rules should be followed.

1. The sample must be representative of the total market.
2. Data and information from the sample must be factual and unbiased.
3. The units of comparison applied should reflect market behaviour.

Analysing demand generators provides an estimate of the total number of room nights available in the market area as well as specific information about the demand's characteristics. The total potential demand must be divided among all the competitive lodging facilities before the market capture rate for the subject property can be estimated.

### **8.7.3 Forecasting Room Night Demand**

By analysing lodging activity and/or demand generators, the analyst has quantified the total room night demand in the current market. This existing demand consists of either accommodated demand or latent demand, or both. Latent demand consists of unaccommodated demand and induced demand.

Because a market study and valuation requires the appraiser to look into the future, the existing room night demand must be forecast over the projection period. Future hotel demand will increase, decrease or remain level. The direction and rate of change is estimated by analysing various economic and demographic indicators.

An excellent context for future demand growth projections may be provided by historical demand growth trends for the lodging market in question. Demand projections are based on the analysis of economic and demographic data gathered during fieldwork. Forecasts depend on how well economic and demographic data reflect changes in hotel room night demand. Data that mirrors future trends in transient visitation is given greater weight in the appraiser's analysis than those that do not. Since changes in hotel demand are often tied to specific types of visitation, individual market segments (such as commercial, meeting and



group and leisure) are analysed. Table 8.6.3(a) illustrates the three primary market segments and the types of data that feasibly could change hotel room night demand. Other market segments, such as extended stay demand, have profiles or characters that align with one of the three primary segments.

Commercial hotel demand is greatly influenced by trends that relate to business activity, such as office space absorption, employment, new businesses moving into the area and airport enplanements. Population growth is not a strong indicator of changes in commercial demand, but it usually sets the lower limit for potential growth in commercial visitation. For example, if an area's population is expected to grow at an annual compounded rate of 1.5%, it is likely that commercial hotel demand will grow by at least the same rate. Other indicators may justify using a higher rate.

There are fewer indicators of meeting and group demand, and many of them provide only an indirect basis for projecting trends in hotel demand. Convention centre activity, particularly that which generates visitation from outside the area, is probably the best indicator of meeting and group demand. The commercial activity reflected in employment trends and office and industrial space absorption indirectly indicates meeting and group demand, because many meetings result from business activity. Meeting and group demand is also created through the sales efforts of individual hotels. This type of induced demand was discussed in a previous section of the text.

Few indicators of leisure demand are available. However, visitor statistics, especially in resort areas, do indicate leisure demand trends. Attendance data for area tourist attractions is also useful.

Changes in hotel demand are projected by market segment for periods ranging from three to 10 years. In forecasting lodging demand, it is wise to keep the projection period as short as possible. The annual compounded percentage of change should reflect the most probable trend in hotel room night demand. Many hotel market studies and valuations seem to project continuous growth in lodging demand, but demand trends do not have to be positive, nor does growth have to increase by the same percentage each year.

The forecast direction and rate of change in hotel room night demand are applied to both accommodated and unaccommodated demand components, which tend to move in tandem with one another.

Changes in induced demand are not usually related to projected changes in the accommodated and unaccommodated components of demand. Rather, induced demand depends on the latent demand characteristics exhibited by the specific demand generator. For example, if a large convention hotel is expected to open in a market enabling the area to attract major groups that previously could not be accommodated, the growth and ultimate size of this induced demand will reflect the hotel operator's marketing ability as well as the hotel's capacity to handle these groups. Depending on the convention hotel's size, the additional demand will usually be expected to increase over a period of time and then stabilise as the hotel approaches its capacity. Although growth in induced demand does not usually depend on growth in an area's convention demand, the surrounding meeting and group market should be considered when quantifying induced demand.

**Table 8.7.3(a): Data Reflecting Changes in Demand**

(Source: Rushmore and Baum, 2001:140)

Commercial	Meeting & Group	Leisure
Total employment by category	Convention centre patronage	Tourist visitation
Office space	Total employment by category	Highway traffic counts
absorption	Airport enplanements	Visitor counts at attractions
inventory	Air cargo data	Employment by category
under development	Tourist visitation	Restaurant Activity Index (RAI)
vacancy rate	Retail sales	Restaurant Growth Index (RGI)
Retail space	Visitor counts at attractions	
absorption	Office space	
inventory	absorption	
under development	inventory	
vacancy rate	under development	
Industrial space	vacancy rate	
absorption	Retail space	
inventory	absorption	
under development	inventory	
vacancy rate	under development	
New businesses entering area	vacancy rate	
Highway traffic counts	Industrial space	
Airport enplanements	absorption	
Air cargo data	inventory	
Commercial building permits	under development	
Housing starts	vacancy rate	
Assessed values	New businesses entering area	
Population		
Retail sales		
Effective buying income		
Personal income		

### 8.8 Micro Hotel Supply Analysis

Another term for the micro supply of hotels and motels is competition. A previous section (section 5.4.4) described how to classify lodging accommodation by the type of facilities offered (e.g. commercial, convention, resort, suite, extended-stay), the class (e.g. luxury, first-class, mid-rate, economy) and the location (e.g. highway, downtown, airport, resort.). Compiling this information on all the hotels within the local market area allows an analyst to identify the primary and secondary competition and evaluate the relative competitiveness of each property. These tasks are fundamental to the build-up approach based on the analysis of lodging activity.

The hotel market analyst's next step is to determine the future guestroom supply considering both the addition of new properties into the market and the removal of existing rooms. From this information the total room nights available can be projected. The accommodatable latent demand and the total usable latent demand are then calculated to project annual area-wide occupancy.

The last step in the market analysis phase of the market study/appraisal is to evaluate the relative competitiveness of all hotels within the market area. This evaluation will form a basis for projecting the future market share of the subject property. Once the market share has been determined, the number of room nights captured and the resulting projected occupancy can be calculated.

### 8.8.1 Total Guestroom Supply

The total guestroom supply consists of the existing market area hotels (primary and secondary competition), which were previously identified in the build-up approach based on an analysis of lodging activity, plus any facilities under construction and proposed projects likely to be completed. Information on the room counts of existing hotels and those under construction is fairly simple to obtain.

Most proposed hotels are never developed, so it is sometimes difficult to pinpoint projects that could feasibly be completed. Local building departments, development agencies, chambers of commerce, hotel associations, newspapers, Hotel and Lodging Association development reports, developers, hotel managers, real estate brokers, lenders and other analysts/appraisers all provide useful information about proposed hotels.

Determining whether or not the project will ultimately be developed is the key to evaluating a proposed hotel. The following list of criteria can help answer this question:

- Does the developer have all necessary zoning approvals, building permits and licences? These approvals must be obtained before construction can begin. A project planned for a jurisdiction with restrictive development policies has less chance of reaching the development stage.
- Is the project financing in place? The entire financing package, including both debt and equity capital, must be fully committed and implemented before a proposed hotel is considered definite. Hotel financing has always been difficult to secure and most of the projects that are discontinued during the development process fail because they lack some form of financing.
- Does the project have a franchise and/or management company commitment (contractually obligated)? Sophisticated lenders generally require a franchise affiliation and an experienced operator before agreeing to finance a project. In markets where appropriate identification is unavailable, the development probability is reduced.
- Does the developer have a history of successful hotel projects? Most first-time developers fail to complete their contemplated hotel projects, and lenders are often reluctant to finance inexperienced hotel developers.
- What is the current supply and demand situation in the local hotel market? If the lodging market is overbuilt or suffering from decreased demand, proposed hotel projects are generally reconsidered and either postponed or terminated. An analyst should investigate the competitive environment several years into the future to determine the probable impact of definite additions to supply over the projection period. Should the anticipated area-wide occupancy drop below an acceptable level, it becomes more likely that some of the proposed hotel projects will be withdrawn.
- What is the hotel financing market's current condition? Over the past 40 years, the availability of hotel financing has followed a cyclical trend. Since few hotel projects are developed without some form of financing, a downward trend in the availability of debt and/or equity money will usually curtail many proposed projects.

Using these criteria, the analyst evaluates each proposed hotel within the market area and determines whether the project should be considered a definite addition to the future lodging supply or disregarded as unlikely to be built. A third alternative would be to assign

a probability factor to the project based on its chance of being developed. Using the criteria set forth above, the project can be considered a future addition to the competitive supply, but its room count would be weighted to reflect its development probability. For example, assume that a 200-room hotel is planned for a site within a given market area. Based on the preceding development criteria and discussions with the building department and developer, the analyst estimates that there is a 50% chance that this project will be built. When projecting the competitive supply, the appraiser would include this project but apply a 50% probability factor and consider it a 100-room hotel rather than a 200-room hotel.

The total guestroom supply is estimated for each projection year by totalling the existing supply of hotel rooms. Actual room counts are used for those hotels that are considered primary competition, and appropriately weighted room counts are used for properties considered secondarily competitive. To this existing supply are added any new rooms currently under construction and rooms in proposed hotels that are likely to be completed. If a hotel that is under construction or proposed is expected to open at some point during one of the projection years, its room count is weighted for that year based on the ratio of 12 minus the month opened divided by 12. If a hotel will be removed from the market during the projection period, its room count is deducted after it is appropriately weighted for the number of rooms available.

The total room nights available is quantified by multiplying the total guestroom supply for each projection year by 365.

### **8.8.2 Total Accommodatable Latent Demand**

If the appraiser projects any type of latent demand, a calculation should be made to determine what portion of the latent demand can be accommodated by the new additions to the guestroom supply. Accommodatable latent demand is calculated for each projection year by multiplying the number of new hotel rooms that have opened since the base year by 365. This calculation indicates the number of new rooms available per year, which is then multiplied by the estimated area-wide occupancy for that year. The portion of the latent demand that cannot be accommodated by the new rooms entering the market, is known as the unaccommodatable latent demand and is calculated as follows:

$$\text{Latent demand} - \text{accommodatable latent demand} = \text{unaccommodatable latent demand}$$

Since the supply of hotel rooms is insufficient to accommodate the unaccommodatable latent demand, the unaccommodatable latent demand must be deducted from the previously calculated total demand to produce an accurate estimate of occupancy and total usable demand. The unaccommodatable latent demand is allocated to each market segment based on the percentage relationship between each segment's latent demand and the market's total latent demand.

### **8.8.3 Total Usable Latent Demand**

The total usable latent demand for any given projection year is either the total latent demand or the total accommodatable latent demand, whichever is less.

The projected market-wide occupancy provides an indication of the future health of the local lodging market and a rough estimate of occupancy for any proposed lodging facility.

When projected area-wide occupancies are anticipated to fall below 55% to 60%, the normal breakeven point for hotels, the health of the local lodging market could be jeopardised. In these situations the average hotel within a market is unable to generate sufficient cash flow to meet debt service, so competition often intensifies and hotels reduce their rates to hold onto their market share. If the market does not recover within a short time, owners run out of reserves and hotels are taken back by lending institutions. These situations can sometimes be avoided by carefully considering the economic impact on both existing lodging facilities and any proposed hotels before recommending that a new hotel be developed in a seriously overbuilt market.

A rough estimate of occupancy can be developed for a proposed hotel using the following rules of thumb:

- A new hotel entering the market should achieve an occupancy rate in Year 1 that is 5% to 15% below the market-wide occupancy level.
- In its second year of operation a new hotel should achieve an occupancy rate that is approximately equal to the market-wide level.
- In Year 3 a new hotel should achieve an occupancy rate approximately 5% to 15% higher than the market-wide level.

As with all general rules, there are many exceptions, but this procedure provides a basis for a quick-go or no-go decision before proceeding to the next step in the analysis.

#### **8.8.4 Allocate Area Demand to All Competitive Hotels**

Once the relationship between supply and demand has been quantified with the estimate of market-wide occupancy, all of the competitive hotels are evaluated to quantify their relative competitiveness. Evaluating each hotel's competitive characteristics helps the appraiser to fit any new properties into the market and calculate how much of the room night demand each hotel is likely to attract.

The percentage of the market captured by an individual lodging facility is called its *market share*. The market shares of all competing properties, including the subject, should total 100% for each market segment.

The allocation of the area's total room night demand among the lodging facilities in the area can be accomplished through analysing customer preference items or penetration factors. Just as the two build-up approaches for quantifying an area's demand analyse the actual generators of transient visitation and the demand indicated by all lodging activity, the two approaches for allocating the total demand to individual properties, concentrate on the nature of the visitation and the characteristics of the lodging activity. Owing to the similarities in these methodologies, demand allocation based on an analysis of customer preference items is generally used in conjunction with the build-up approach based on an analysis of demand generators, while demand allocation based on an analysis of penetration factors is usually applied in conjunction with the build-up approach based on an analysis of lodging activity.

### 8.8.4.1 Demand Allocation Based on an Analysis of Customer Preference Items

Demand allocation based on an analysis of customer preference items generally begins after the build-up approach based on an analysis of demand generators has been completed. Once the final market area is defined and the sources of transient visitation are identified, surveyed and quantified, the procedure can be applied.

First, the area's competing lodging facilities must be identified by type and class. As described previously, hotels can be categorised by type (commercial, convention, resort, etc.) and each type can be further divided into classes (luxury, standard, economy). Interviews with area hotel managers and a review of published room rate information can facilitate categorisation.

Second is to allocate the demand that each source of visitation has generated among the subject property and the other area hotels. The allocation should be based on the demand's characteristics and on the supply's relative competitiveness. This allocation is based on customer preference items.

Choosing a hotel is actually a complex procedure. Several customer preference items influence the selection of a particular lodging facility. Hotel and motel patrons can be grouped into three categories based on the primary purpose of their trips.

1. Commercial, i.e. business travel, either alone or in groups of fewer than five.
2. Convention, i.e. gathering for groups, meetings, lectures, seminars or trade shows.
3. Leisure, i.e. recreation, sightseeing, or visiting friends and relatives.

A further breakdown of each group reveals customers' reactions to room rates; economy accommodation will appeal to highly rate-conscious travellers; standard rates draw moderately rate-conscious customers; and individuals indifferent to cost will probably choose luxury lodgings.

Combining the three customer categories with the three rate reactions produces nine types of guests (e.g. commercial-economy rate, convention-standard rate, leisure-luxury rate.) Each customer preference item represents a specific characteristic guests consider in choosing one hotel over another. Six of the most prominent customer preference items are shown in table 8.8.4.1(a).

**Table 8.8.4.1(a): Customer Preferences and Considerations**

(Source: Rushmore and Baum, 2001:198)

Item	Consideration
Price	Economic
Travel distance	Time, convenience
Quality of facilities	Comfort, status, atmosphere
Amenities	Comfort, status, recreation, convenience, atmosphere
Management	Comfort, atmosphere
Image	Status

Ranking the six customer preference items in order of importance establishes a basis for predicting how guests will choose among several lodging facilities in a particular market area. Table 8.8.4.1(b) ranks the preference items listed above.

**Table 8.8.4.1(b): Customer Preferences Items by Market Segments**

(Source: Rushmore and Baum, 2001:198)

	<b>Economy</b>	<b>Standard</b>	<b>Luxury</b>
<b>Commercial</b>			
Most important	1 Price	Travel time	Image
	2 Travel time	Quality	Quality
	3 Quality	Price	Management
	4 Management	Image	Travel time
	5 Amenities	Management	Amenities
Least important	6 Image	Amenities	Price
<b>Meeting &amp; Group</b>			
Most important	1 Price	Amenities	Image
	2 Amenities	Quality	Amenities
	3 Quality	Price	Quality
	4 Management	Image	Management
	5 Travel time	Management	Travel time
Least important	6 Image	Travel time	Price
<b>Leisure</b>			
Most important	1 Price	Amenities	Image
	2 Amenities	Quality	Amenities
	3 Quality	Price	Quality
	4 Management	Image	Management
	5 Travel time	Management	Travel time
Least important	6 Image	Travel time	Price

For example, an economy-minded commercial traveller will drive farther (more travel time) to stay at a hotel that offers favourable prices. This same traveller will probably select a property with good-quality facilities over a lower-quality hotel with more amenities. A standard-rate leisure traveller on the other hand places primary emphasis on a hotel's amenities and price, regarding travel time as less important.

A market share distribution can be constructed by carefully analysing the preferences and characteristics of the typical transient traveller visiting the market area and matching these selection criteria with the competitive hotel supply. Each competitive property should receive a portion of the overall market share, and the size of the portion will depend on the property's relative competitiveness and its ability to attract a particular type of traveller. The sum of all the allocated market shares for each generator of demand should equal 100%.

The number of room nights captured by an individual property can be calculated by multiplying each generator's percentage market share allocated to the hotel by the total number of room nights quantified in the build-up approach based on an analysis of demand generators. The total of all allocated room nights from all generators of demand is divided by the property's room count (multiplied by 365) to produce the estimate of occupancy.

The following example illustrates how customer preference information can be used to allocate the room nights generated by a source of visitation among the subject property and all competing lodging facilities. Table 8.8.4.1(b) illustrates the importance of various hotel characteristics to different market segments.

<b>Example</b>
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The subject property is a proposed nationally franchised commercial motor hotel offering typical amenities at standard rates. Three competing lodging facilities lie within the market area. Competition A is a luxury-rate nationally franchised commercial hotel with high-quality facilities and a reputable image. Competition B is a standard-rate nationally franchised, commercial motel with good-quality facilities. Competition C is an economy-rate independent commercial motel with fair facilities.

A prominent national manufacturing company's home office generates transient visitation within the market area. Based on a survey of various department heads an estimate of the firm's out-of-town visitation is developed as shown in table 8.8.4.1(c).

**Table 8.8.4.1(c): Estimate Out-of-Town Visitation**

(Source: Rushmore and Baum, 2001:200)

Type of Visitor	Typical Rate Preference	Estimated Total Yearly Room Nights	Facilities Currently Used
Corporate Executives	Luxury	3,700	Competition A
Middle Management	Standard	5,000	Competition B
Visiting Sales Representatives	Standard and Economy	7,500	Competition B and C

The property being analysed will be built approximately eight travel minutes away from this source of visitation. The other properties are also nearby. Competition A is 15 minutes from the source of visitation, Competition B is 12 minutes away and Competition C is 10 minutes away.

In allocating the room nights generated by this source of visitation the analyst assumes that most corporate executives will continue to travel the extra seven minutes to stay at Competition A because it offers the best image and quality. Some may use the new facility if Competition A is full or inclement weather or some other factor makes a closer location more desirable. The allocation of room nights based on customer preference items for this market segment is shown in table 8.8.4.1(d).

**Table 8.8.4.1(d): Allocation of Room Nights For Corporate Executives**

(Source: Rushmore and Baum, 2001:200)

Lodging Facility	Estimated Market Share	Room Nights
New property	5.0%	185
Competition A	94.0%	3,478
Competition B	1.0%	37
Competition C	0%	0

Middle-management visitors will choose either the new property or Competition B. Because the property being appraised will be newer and four minutes closer, it may capture a sizeable portion of this market. Competition B may respond by upgrading its facilities and/or lowering its rates. If differences in travel time are minimal, the quality of the facilities, price, image and management could be deciding factors. The allocation of room nights for this market segment is shown in table 8.8.4.1(e).



**Table 8.8.4.1(e): Allocation of Room Nights for Middle Management**

(Source: Rushmore and Baum, 2001:200)

Lodging Facility	Estimated Market Share	Room Nights
New property	65.0%	3,250
Competition A	1.0%	50
Competition B	29.0%	1,450
Competition C	5.0%	250

Economy-minded visiting salespeople will probably drive the extra two minutes to take advantage of the low rate offered by Competition C. Standard-rate salespeople, like the middle-management visitors, must choose between the new property and Competition B. The allocation of room nights for this market segment is shown in table 8.8.4.1(f).

**Table 8.8.4.1(f): Allocation of Room Nights for Visiting Sales Representatives**

(Source: Rushmore and Baum, 2001:201)

Lodging Facility	Estimated Market Share	Room Nights
New property	30.0%	2,250
Competition A	1.0%	75
Competition B	24.0%	1,800
Competition C	45.0%	3,375

Table 8.8.4.1(g) indicates that the total demand from this particular source of visitation allocated to the appraised property, is 5,685 room nights: 185 room nights for corporate executives, 3,250 for middle management, and 2,250 for visiting salespeople. If the subject has 150 guest units, the 5,685 room nights would equate to approximately 10% of occupancy.

**Table 9.8.4.1(g): Total Demand to Subject from Manufacturing Company**

(Source: Rushmore and Baum, 2001:201)

Company Staff	Room Nights to Subject Property
Corporate executives	185
Middle management	3,250
Visiting sales representatives	<u>2,250</u>
Total	5,685

Quantifying the total demand generated by all sources of visitation and allocating the room nights between the subject and competing properties is accomplished using the procedure described below. The result is an estimate of occupancy, calculated as the total number of room nights allocated to the appraised property divided by the property's total available rooms per year.

$$\frac{\text{Total number of room nights}}{\text{Number of rooms} \times 365} = \text{Estimated occupancy}$$

**End of Section 8.7.4.1 Example**

### 8.8.4.2 Demand Allocation Based on an Analysis of Penetration Factors

Demand allocation based on an analysis of penetration factors is usually employed in conjunction with the build-up approach based on an analysis of lodging activity. The approach assumes that the accommodated room night demand for each competitive hotel has been determined and allocated among the appropriate market segments. To calculate new market shares for area hotels when another lodging facility is added to the market, a rating factor known as the *penetration factor* is used.

Penetration factors show how well each property in the market area competes for a particular market segment. The penetration factor is calculated by dividing a given hotel's market share by its fair share. *Market share* represents that portion of total demand accommodated by a given property. *Fair share* represents that portion of total supply accounted for by the same property. A 100-room hotel in a 1000-room market has a fair share of 10%. If that same hotel accommodates 12% of the market's total demand, then its penetration factor is 120% (12% / 10%). In other words, this hotel attracts 120% of its fair share of the market's demand. When a new hotel enters the market, the projection of future penetration factors is somewhat complicated and requires the use of a market share adjuster.

<b>Example</b>
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Assume that the local market consists of three competitive lodging facilities with a total of 675 rooms. Hotel A has 300 rooms, therefore its fair share equates to 44.44% (300/675). Market research indicates that, over the past 12 months, Hotel A has operated at 80% occupancy, of which 50% of its total accommodated demand comes from the commercial segment of the market. The number of accommodated room nights per year in the commercial segment for Hotel A is calculated as follows:

$$300 \text{ rooms} \times 365 \text{ days} \times 0.80 \times 0.50 = 43,800 \text{ commercial room nights}$$

After doing similar calculations for the other hotels in the market, i.e. Hotels B and C, the total level of commercial demand is estimated at 83,836 room nights. As such, Hotel A's commercial segment market share equates to 52.24% (43,800/83,836). With known fair share and market share ratios, Hotel A's commercial segment penetration factor can be calculated as follows:

$$\frac{52.24\%}{44.44\%} = 118\%$$

Commercial segment penetration factors for each of the hotels in the competitive market are presented in table 8.8.4.2(a).

The penetration factors show that Hotel C is somewhat more competitive than Hotel A in the commercial segment, and that both Hotel A and Hotel C are significantly more competitive than Hotel B. As noted Hotel A's fair share equates to 44.44%. If it were to capture its fair share of the commercial market it would receive 44.44% of the demand and have a penetration factor of 100%. Hotel C is the most competitive property for commercial demand, with a penetration factor of 126%. However it has only 125 rooms, so it captures 23.27% of the commercial market which is the smallest share noted among the three competitors.

**Table 8.8.4.2(a): Penetration Factors**

(Source: Rushmore and Baum, 2001:203)

Hotel	Number of Rooms	Percent Yearly Occupancy	Commercial Demand	Room Nights Per Year	Market Share	Fair Share	Penetration Factor
A	300	80%	50%	43,800	52.24%	44.44%	118%
B	250	75	30	20,531	24.49	37.04	66
C	<u>125</u>	95	45	<u>19,505</u>	<u>23.27</u>	<u>18.52</u>	126
Total	675			83,836	100.00%	100.00%	

Now assume that Hotel D enters the market adding 200 rooms to the total supply. Market research and analysis of its location, amenities management, and other competitive characteristics indicate that Hotel D will be more competitive than Hotel B for commercial demand, but somewhat less competitive than Hotel A. The penetration factor for Hotel D should fall somewhere between 66% and 118%, but probably closer to 118%. It is also anticipated that Hotel D will become increasingly competitive during its first two years of operation. Therefore, based on market research and the analyst's judgement, the penetration factor for Hotel D is estimated to be 97% in Year 1 and 105% in Year 2.

Because this new property has entered the market, the commercial demand must be reallocated among four hotels and the market shares and commercial room nights captured must be recalculated. In this process note that penetration factors of the existing hotels are expected to remain stable and our projections also assume that the level of demand in the market remains fixed table 8.8.4.2(b) illustrates this procedure.

**Table 8.8.4.2(b): Demand, Market Share and Capture Rate**

(Source: Rushmore and Baum, 2001:204)

Hotel	Number of Rooms	Commercial Penetration Factor	Commercial Fair Share	Market Share Adjuster	Market Share	Room Nights Captured
<i>Year 1</i>						
A	300	118%	34.29%	40.3%	40.6%	34,022
B	250	66	28.57	18.9	19.0	15,948
C	125	126	14.29	17.9	18.1	15,150
D	<u>200</u>	97	<u>22.86</u>	<u>22.2</u>	<u>22.3</u>	<u>18,716</u>
Total	875		100.00%	99.3%	100.0%	83,836
<i>Year 2</i>						
A	300	118%	34.29%	40.3%	39.8%	33,407
B	250	66	28.57	18.9	18.7	15,659
C	125	126	14.29	17.9	17.7	14,876
D	<u>200</u>	105	<u>22.86</u>	<u>24.0</u>	<u>23.7</u>	<u>19,893</u>
Total	875		100.00%	101.1%	100.0%	83,836

The fair share of each property is multiplied by its projected penetration factor to yield the market share adjuster. Each property's market share adjuster is then divided by the total of all the market share adjusters, rendering a revised market share. The market share adjuster re-establishes the market share factors for each property which is necessary due to the projected opening of the new hotel. Note that Hotel A's market share declines from the historical level of 52.24% shown in table 8.8.4.2(a) to 40.6% in table 8.8.4.2(b). The decline is chiefly a function of the hotel's decreased fair share. When the market expanded by 200 rooms, Hotel A's fair share declined from 44.44% to 34.29%. Because the new

hotel is expected to increase its penetration in the second projection year, Hotel A's market share declines further that year, falling to 39.8%

The opening of Hotel D is not expected to increase the actual number of commercial room nights accommodated within the market area so the current demand of 83 836 must be reallocated among the four hotels.

Key to this example is the use of a market share adjuster in the calculation of a property's market share. This unique factor allows an analyst to compare many competitive aspects of a lodging establishment regardless of the property's room count or changes in the overall supply of accommodation. The example assumes that the relative competitiveness of the original three hotels remains constant while the new hotel becomes more competitive. This is generally experienced by established lodging facilities operating at stabilised penetration levels. If market research indicates that any of these properties is becoming more or less competitive however, its penetration factor can be modified upward or downward.

The example illustrates demand allocation based on an analysis of penetration factors for the commercial market segment. The same procedure could be used to allocate meeting and group demand, leisure demand or any other quantifiable source of visitation within the market area. The ultimate result is a total room night estimate for the subject property, which can be converted into a projection of occupancy by dividing the total projected room nights by the number of available room nights. The results are shown in table 8.8.4.2(c).

In practice analysts generally use a combination of customer preference items and penetration factors to allocate room night demand among competitive lodging facilities. Both approaches call for judgements on a wide variety of competitive factors. Experience in hotel operations and analysis can prove invaluable in determining the most probable sequence of events

**Table 8.8.4.2(c): Hotel D – Projected Room Nights**

(Source: Rushmore and Baum, 2001:205)

	<b>Year 1</b>	<b>Year 2</b>
Commercial	18,716	19,893
Meeting & Group	26,270	27,560
Leisure	<u>9,420</u>	<u>10,185</u>
Total	54,406	57,638
Available Room Nights: 200x365	73,000	73,000
Projected occupancy	74.5	79.0

**End of Section 8.8.4.2 Example**

### 8.8.5 Room Nights Captured

The projected room nights captured by any hotel can be calculated by multiplying the hotel's market share percentage by the total room night demand for the corresponding segment. This process is repeated for each market segment and the results are totalled to yield the number of room nights captured.

### **8.8.6 Stabilised Occupancy**

When projecting a property's room nights captured and occupancy rates into the future, the assumptions of continued growth and no new additions to the competitive supply will ultimately produce unreasonably high capture and occupancy levels. As a result, appraisers use the concept of a stabilised occupancy.

A property's stabilised occupancy level reflects the anticipated level of occupancy over the remaining economic life of the property, given any or all periods of build-up, plateau and decline in its life cycle. The concept of stabilised occupancy excludes from consideration any abnormal relationship between supply and demand as well as any transitory or nonrecurring conditions, whether favourable or unfavourable, that may result in unusually high or low levels of occupancy. Although it is common for a hotel to operate at occupancies above its stabilised level, it is equally possible that new competition and temporary downturns in the economy could force actual occupancy below stabilised occupancy.

Projections become more uncertain the farther into the future they are made. The use of a single stabilised occupancy rate produces the same results as a forecast that attempts to reflect the inevitable upward and downward occupancy cycles that any typical lodging facility experiences. Furthermore, discounting future economic benefits tends to smooth out the cycle, providing additional support for using a stabilised level of occupancy.

For new hotels a two- to five-year build-up in occupancy is generally factored into the projection. Few hotels stabilise in their initial year of operation. Since the initial years tend to generate operating losses, the build-up period must be included in the projection to illustrate the actual start-up cash requirements.

Several factors influence the selection of a stabilised level of occupancy. The following list identifies some key considerations:

#### **Market-Specific Considerations**

- Market area demand trends
- Composition of local demand
- Supply and competitive trends
- Historic occupancy cycles

#### **Property-Specific Considerations**

- Location-specific factors
- Competitiveness
- Age
- Management and image
- Obsolescence

The best indicator to analyse when determining a stabilised level of occupancy is probably the nature of the local hotel demand. Different types of travellers have different travel patterns (i.e. days of travel, length of stay and seasonality), so the mix of visitors within a given market will influence the area's overall occupancy level.

For example, assume a market has a strong business base, which generates a significant room night demand Monday through Thursday nights. However, the local area has no leisure attractions, so few people use local hotels and motels on Friday and Saturday nights. Some commercial demand is experienced Sunday night as business travellers try to get a head start on Monday's activities. Because of this occupancy pattern, the maximum market-wide occupancy would be approximately 67%, assuming near sell-outs every Monday through Thursday. Table 8.8.6(a) illustrates how this maximum occupancy level has been established.

**Table 8.8.6(a): Maximum Occupancy**

(Source: Rushmore and Baum, 2001:224)

Day	Percentage of Occupancy
Monday	80%
Tuesday	85
Wednesday	90
Thursday	80
Friday	30
Saturday	45
Sunday	60
Weekly average	67%

Considering market conditions and the nature of the existing lodging demand, a stabilised occupancy rate higher than 67% could not be justified unless the property has competitive or physical attributes that enable it to capture more than its fair share of weekday demand as well as the existing weekend demand.

The historic occupancy cycles experienced in the market area, also indicate where the stabilised occupancy rate should fall. Table 8.8.6(b) shows the 20-year occupancy cycle of three different hypothetical cities.

**Table 8.8.6(b): 20-Year Occupancy History**

(Source: Rushmore and Baum, 2001:225)

Year	City A	City B	City C
1	71.0%	72.0%	57.0%
2	66.0	74.0	68.0
3	63.0	76.0	62.0
4	69.0	75.0	56.0
5	60.0	69.0	50.0
6	61.0	68.0	47.0
7	63.0	69.0	49.0
8	66.0	70.0	51.0
9	64.0	69.0	46.0
10	66.0	64.0	57.0
11	68.0	71.0	59.0
12	69.0	71.0	61.0
13	72.0	77.0	63.0
14	72.0	78.0	60.0
15	69.0	76.0	63.0
16	66.0	72.0	62.0
17	59.0	68.0	61.0
18	65.0	68.0	60.0
19	69.0	70.0	57.0
20	70.0	69.0	60.0
Average	66.4%	71.3%	57.5%
Standard deviation	3.8	3.6	5.8

Statistical data relating to the 20-year occupancy cycles are shown in table 8.8.6(c). The stabilised occupancy for each of these cities should approximate the average occupancy, which is generally the midpoint between the highest and lowest occupancy levels recorded during the 20-year period.

**Table 8.8.6(c): 20-Year Occupancy Cycles**

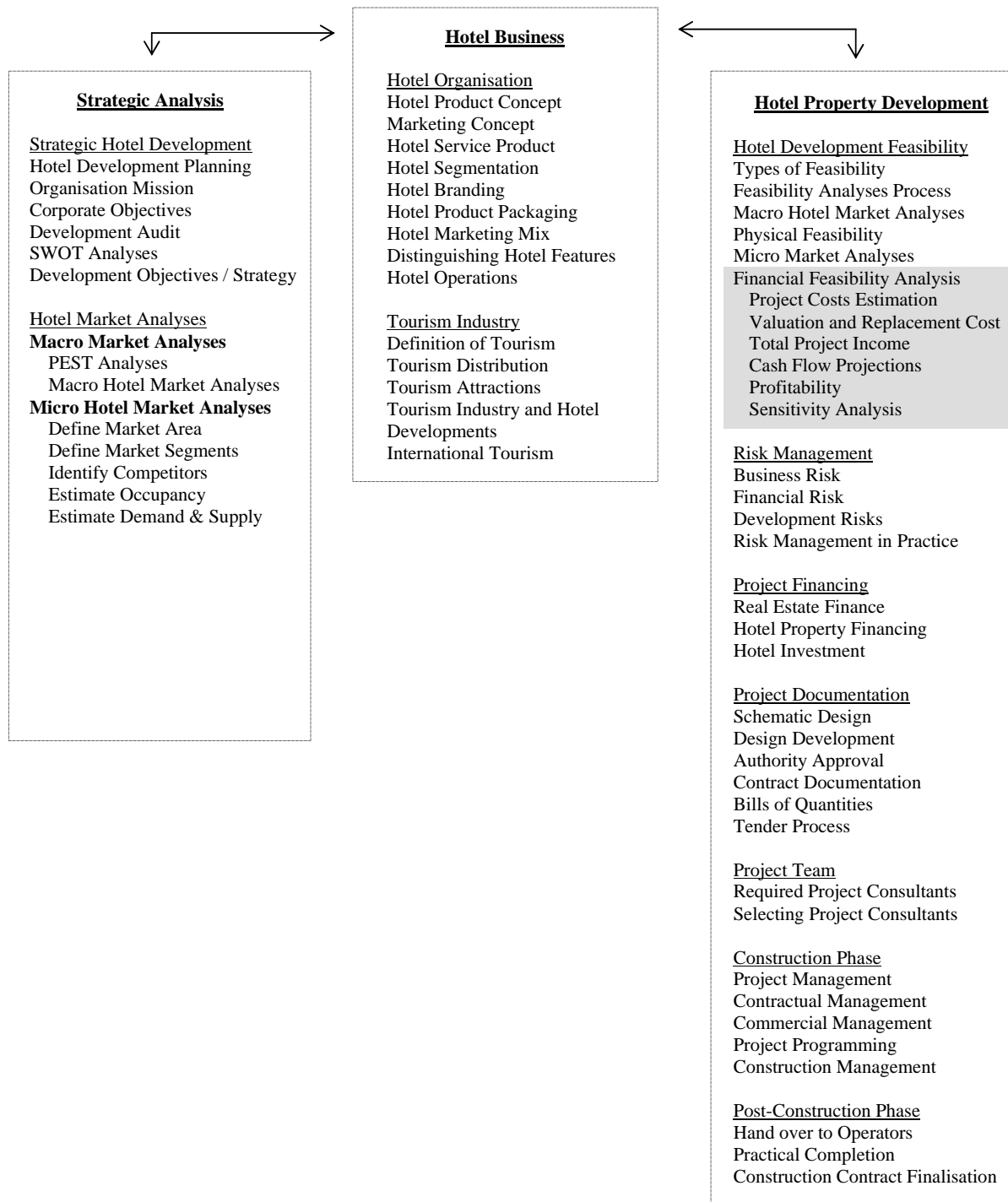
(Source: Rushmore and Baum, 2001:225)

<b>Year</b>	<b>City A</b>	<b>City B</b>	<b>City C</b>
Average occupancy	65.5%	71.3%	57.0%
Highest occupancy	72.0	78.0	68.0
Lowest occupancy	59.0	64.0	46.0
Difference	13.0 pts.	14.0 pts.	22.0 pts.
Standard deviation	3.8	3.6	5.8

### **8.8.7 Proposed Hotel and Facilities Suitability Recommendation**

The suitability recommendation of the hotel and amenities, typically only appears in engagements involving proposed hotels or rehabilitations of existing buildings. This section identifies the facilities, amenities and services that are expected to enable the property to optimise its overall performance. To make these kinds of recommendations, the consultant needs to understand the facilities currently in the market, the desires of potential demand generators, the physical constraints of the site and the specifics of its location.

## Chapter 9: Hotel Development Financial Feasibility





## **9 Hotel Development Financial Feasibility**

### **9.1 Introduction to Financial Feasibility**

The last phase of the feasibility study, according to Cloete (1996:5), is to determine whether a proposed project is expected to satisfy the financial requirements of the developer. He says: "*Whereas the [feasibility] analysis up to this stage had as objective to determine whether a proposed project is 'feasible', i.e., whether it can be done in practice, the financial feasibility can more accurately be described as a viability study, i.e., to analyse whether the proposed project is 'capable of maintaining life'.*" To support this clarification, Cloete (1996:5) quotes Eagar's distinction in this regard: "*A feasibility confirms the possibility, and a viability measures the performance capacity.*"

The purpose of the viability study (Cloete, 1996:5), is to determine whether the proposed project will satisfy the financial criteria of the parties involved. It could be seen in accounting terms as a budget of expected future yield, e.g. the developer's profit or construction turnover, the professional consultants' fees, the leasing or selling agents' commission and the investor's return on his/her investment. Similarly, the local and other authorities, the potential tenants and political and environmental pressure groups all have concerns which need to be addressed.

Pyhrr et al (1989:30), further to Cloete (1996) above, highlights an additional distinction between investment analysis and feasibility analysis, i.e.: "*Investment analysis, as we define it, deals with the return-risk relationship associated with **existing projects**. Feasibility analysis generally considers the return-risk relationship in the development and construction of **new projects**. Both entail far more than financial analysis of a project, generally involving market, marketability, legal, and physical analyses.*"

Pyhrr et al (1989:38) draws yet another distinction between the two concepts, by stating that investment analyses have traditionally focused on financial aspects of real estate investment, whereas feasibility analyses concentrate on the non-financial elements, e.g. marketing, physical, legal, political and social elements.

In essence, from the above, the term financial feasibility and investment analysis has the same meaning. Hence for the remainder of this text, the term financial feasibility will be used, encapsulating investment analysis for proposed hotel property developments, and will feasibility and viability be used interchangeably.

### **9.2 Different Types of Financial Feasibility Reports**

The following types of financial feasibility reports can be distinguished: (Cloete, 1996:6)

- a) Estimate of current building cost (capital cost) only (usually based on either the rate per square metre or elemental methods)
- b) Same as (a) above, but escalated to tender date (estimated building cost at tender date) or to date of practical completion (estimated final building cost)
- c) Estimate of escalated final building cost with only the estimated cost of professional fees added
- d) Estimate of total capital outlay
- e) Replacement valuation (for insurance purposes, etc.).

The financial feasibility may also be performed to establish any one of a number of other variables in the equation, for example:

- Price that may be paid for a parcel of land at a given required yield
- Room rate to achieve a required yield
- Optimum contract period (with reference to the size of the project)
- Optimum construction cost (again with reference to the size and specification of the development).

### 9.3 Structure of the Financial Feasibility Study

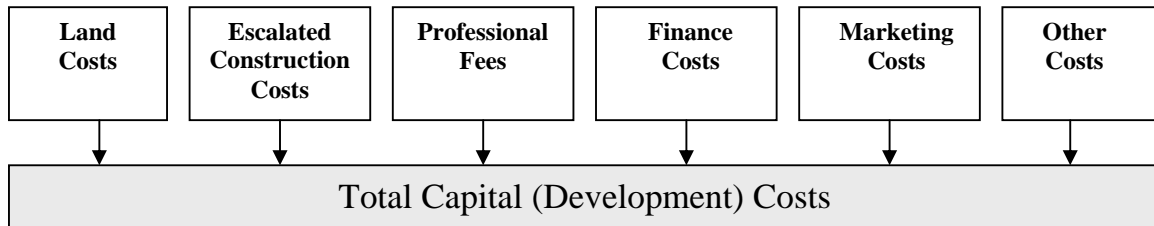
The financial feasibility study consists of five steps (Cloete, 1996:7):

1. Estimate the **total capital outlay** of the project
2. Estimate the **total net project income**
3. Do a **cash flow projection** for the development period
4. Estimate the **profitability** of the project and compare to the investor's objectives
5. Do a **risk analysis** on the proposed project.

The process, structure and components of a financial feasibility study are illustrated in the following:

#### Illustration 9.3(a): Components of the Total Capital Cost

(Source: An adaptation of Cloete, 1996:8)



### 9.4 Capital Cost (Development Cost or Total Capital Outlay of the Project)

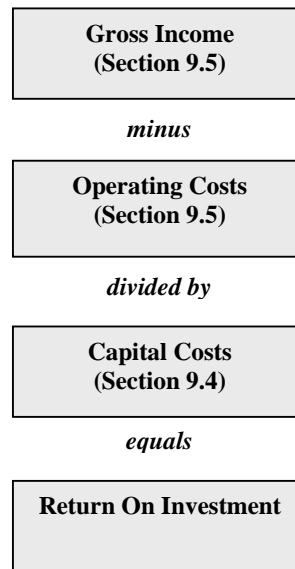
Comparing the development costs of hotel building projects are complicated, because of the wide variations in facility requirements and standards of sophistication as well as differences in the siting and design of the buildings. Local prices are also affected by the extent of competition, rates of inflation in the region and exchange rates (Lawson, 1997)

A project's capital (development) cost consist of the following elements (Cloete, 1996: 8):

- Land Costs
- Building Costs
- Professional Fees and Disbursements
- Finance Costs
- Marketing Costs
- Sundry Costs.

**Illustration 9.3(b): Feasibility Components and Return on Investment Calculation**

(Source: Cloete, 1996:8)



Cahill and Mitroka (1992) distinguish between the following hotel development cost categories:

- Hard construction costs
- Furniture, fixtures, and equipment
- Pre-opening and working capital
- Financing fees
- Miscellaneous soft costs/developer fees
- Reserves and contingencies.

Inter-Continental Hotels separates each of the principal development elements in the hotel project development, planning, building, supply and hand-over process in the following categories (Inter-Continental Hotel Architectural and Engineering Specifications, 1996):

- Land
- Construction
- Furniture, Fixtures and Equipment (FF&E)
- Technical Services and Other Professional Fees
- Other Fees
- Financing Costs
- Organisation and Development Costs
- Pre-Opening Expenses
- Working Capital
- Contingency.

Capital investment, describe Lawson (1997), is the costs of constructing and fitting out the hotel together with the associated fees and expenses. The outlay also includes provision for initial working capital and the payment of interest during the construction period.

Table 9.4(a) illustrates the approximate percentages of development costs in which (a) represents a prime area with land costs of 15% and interest rates of around 12% with a two-year building and fitting out period, and (b) being the more typical of underdeveloped land with higher infrastructure costs. Land purchase varies from 5 to 20%, the higher value applying to city centre and motel developments.

The general building construction cost usually represents between 50 and 60% of the total. Furniture fixtures and equipment (FF&E) may be estimated as a percentage (25 - 30%) added to building cost or based on model schemes. This covers items which may be client supplied. Examples of these are loose furniture, furnishings, back-of-house equipment (food service, laundry), front office equipment and inventories (linen, uniforms, china, glassware, silverware, utensils, stationery supplies, printing, etc.). More specialised equipment is usually leased. Financing costs and interests depend on the time taken for construction, phased payments for the work and interest rate charged on loans. Agreements may provide for interest to be deferred during the initial year (Lawson, 1997).

**Table 9.4(a): Overall Development Costs**

(Source: Lawson, 1997: 129)

Development Item	Range (a) - (b)%	Coverage
Land purchase	15 - 5	Leasing or sale and leaseback alternatives.
Site works, infrastructure	1.5 - 4	Utilities, roads, surface parking, landscaping.
Building construction	50 - 55	See breakdown of costs.
Special systems	1 - 1.5	Telephone, fire safety, audio-visual systems.
Furniture, furnishings, equipment	14 - 16	See below, includes purchasing costs.
Professional/legal fees	4 - 6	Architecture, engineering, interior design, specialist.
Pre-opening expenses	1.5 - 2.5	Cleaning, recruitment, training.
Working capital	1 - 1	Initial supplies.
Financing costs + interest	11 - 8	Fees, interest during construction, taxes, insurance.
Miscellaneous contingencies	1 - 1	
	<u>100 - 100</u>	

Mc Gee (2002) explained that the development cost of a hotel project should include the cost of **all** the elements required to operate a hotel. At a given point in time, subsequent to establishing an operational hotel, the development cost ends and permanent operational management (revenues, expenses and costs) commences.

Development cost estimates are often calculated by either the cost per room or cost per square metre of built-up-area approach (Lawson, 1997):

The cost per room approach indicates the median cost per room for the specific hotel type (e.g. budget, mid-scale or 1<sup>st</sup> class hotel) and is calculated by multiplying the number of room by the estimated cost per room. The gross area per room is assumed but the conditions such as location, size, height, type and grade of hotel need to be qualified. Cost per room indices is useful in making comparisons between several types of projects and over a range of timescales.

Costs based on built areas are more accurate and can take account of the actual facilities specified, the building design and the gross areas required. Unit costs can be projected to forecast future prices, using building cost and tender price indices, and can more accurately represent regional variations.

Assessment of financial viability is carried out at an early stage to determine the likely return on the investment. As a rough preliminary indicator the ratio of investment cost per room : room rate = 1000:1 is sometimes used, but this does not allow for changes in interest rates, occupancies, food and beverage income and other variables. For example, should a hotel's development cost per room equal US\$ 1,000,000 then the room rate should be set at approximately US\$ 1,000.

From the above explanations by Cloete, Cahill and Mitroka, Mc Gee, Inter-Continental Hotels and Lawson, the following components of the total hotel development cost are defined and illustrated sections 9.4.1 to 7.4.7:

- Land Costs
- Construction Costs
- Furniture, Fixtures and Equipment (FF&E) Costs
- Professional Fees and Disbursements
- Financing Costs
- Pre-Opening Expenses
- Working Capital
- Sundry Costs.

*Refer to addendum 'E', wherein the above categories are elaborated on, listing subcategories of relevant hotel development cost items.*

#### **9.4.1 Land Costs**

The total cost of land is made up of (Cloete, 1996):

- Market value
- Transfer costs
- Soil tests
- Bulk service charges
- Interim tax on land or improvements.

#### **9.4.2 Construction Costs**

##### **9.4.2.1 Estimated Current Construction Cost**

*“One of the best sources available for [hotel] construction cost estimation is actual development cost of comparable properties. In a perfect world, a hotel feasibility analyst would obtain actual construction cost data on a hotel identical in every way to the subject property. This ‘perfect comp’ [comparison property] would be located next door to the subject hotel and the construction would have been completed within the last week. In the real world, such a perfect comp is seldom encountered” (Cahill & Mitroka, 1992: 380).*

Unfortunately, (Cahill & Mitroka, 1992) unlike comparable cost data for single-family homes or office buildings, comparable hotel construction costs are difficult to obtain. This is especially the case for analysts who do not specialise in hotel development and accordingly do not maintain large databases of development cost information. In addition to this, the number of similar hotels located in any one market area is limited and no two hotels are exactly identical in construction quality, layout and design.

Included in the estimation of current building cost are (Cloete, 1996):

- Basic building elements, influenced by design and aesthetic specifications
- Special items, such as partitioning, air-conditioning, ventilation, escalators, hoists, boilers, heating reticulation, smoke extraction, kitchen and bar equipment, refrigeration equipment, laundry equipment, flagpoles, signage, etc.
- Siteworks for example paving, roadwork, electrical- and water- reticulation, stormwater drainage and soil drainage, boundary walls, etc.
- Preliminaries
- Contingencies, for design and detail development on site.

The estimate is usually based on an estimate of on a US\$/m<sup>2</sup> basis or an elemental analysis.

If the elemental method of estimating building cost is employed, the following should be noted (Cloete, 1996: 9):

- The basic items of the different functional entities are usually kept separate, for example parking garages or areas, restaurants, convenience shops, front offices, back-of-house areas such as the kitchens and laundry, to name a few.
- The estimate is measured by separating the different functional entities into component or sub-component.
- The individual components and sub-components costs are expressed as a rate per unit, a building rate per m<sup>2</sup> and a percentage of building cost. This facilitates comparison with other building developments and highlights possible over-expenditure and/or measuring and pricing errors.

In all cases it is important that the specifications used for estimating the building cost are clearly identified.

Neeb (2002) explains, from a quantity surveyor's point of view, the type of measurement (construction cost estimation) performed depends not only on the availability of information at the time of performing an estimate, but also on the requirements of the client/developer. It would not be possible to perform a comprehensive quantities measurement and cost estimation of the proposed facility if only limited or concept information is available.

#### **9.4.2.2 Construction Cost Escalation**

Escalation of building costs comprises both pre-tender escalation and post-tender escalation.

**Pre-tender escalation:** *“Comprises allowance in tender price from date of feasibility report to anticipated tender date. Apply the tender price index predictions or a percentage per month compounded, obtained from a reliable authority...”* and,

**Post tender escalation:** “The escalation during the building period is usually calculated by applying the BIAC Contract Price Adjustment Provisions (Haylett formula)” (Cloete, 1996: 10).

### 9.4.2.3 Hotel Construction Cost Drivers

Table 9.4.2.3(a) illustrates the range of costs for typical UK hotel developments, according to Ransley and Ingram (2000). The broad range of costs detailed in Table 8.1 is determined by a range of factors including; the range of facilities provided, sizes of bedrooms and quality of finish among others. These factors are termed ‘cost drivers’. Cost drivers can be specific to a type of building, a client or a procurement strategy. Consideration of a project’s cost drivers is particularly important at the earliest stages of a feasibility study, when the client and project team have the greatest freedom to opt for site or design alternatives.

**Table 9.4.2.3: Indicative Costs of Hotel Developments in the United Kingdom (1999)**

(Source: Ransley and Ingram, 2000: 140)

Indicative All-in Estimating Rates	Average Gross Floor Area per Room (m <sup>2</sup> )	Cost, building only (£/m <sup>2</sup> - gifa)*	Cost, building only (£/000s/bedroom)
Luxury city-centre hotel multi-storey, conference and wet leisure facilities	70—130	1500—1850	130—195
Business town centre/provincial hotel 4 - 6 storeys, conference and wet leisure facilities	70—100	1100—1300	90—130
Mid-range provincial hotel 2 - 3 storeys, conference and leisure facilities	50—60	1100—1350	55—80
2 - 3 storeys, bedroom extension	33—40	800—1200	25—45
City-centre aparthotel 4 - 7 storeys, apartments with self-catering facilities	50—60	850—1150	45—70
Budget city-centre hotel (new build) 4 - 6 storeys, dining and bar facilities	35—45	900—1050	33—45
Budget city-centre hotel (office conversion) 4 - 6 storeys, excluding dining facilities	32—38	700—1150	22—45
Budget roadside hotel 2 - 3-storey lodge, excluding dining facilities	28—35	850—950	26—33

Note: 1) Costs are for mid-range schemes for chain or affiliate hotels in outer London, with prices current in July 1999, assuming competitive tendering. Indicative costs include furniture, fittings and equipment, but exclude costs of drainage, external works, and any necessary site preparation and demolitions. Costs of professional fees and VAT are also excluded.

2) \*gifa – gross internal floor area.

The figures set out in table 9.4.2.3(a) provide indicative costs and require adjustment to account for the characteristics of specific projects.

The following eleven cost drivers are particularly significant in determining overall cost levels (Ransley & Ingram, 2000: 141):

- Site conditions and characteristics
- Building plan, layout and massing
- Quality levels
- Building services installations
- Furniture, fittings and equipment (FF&E) expenditure
- Leisure facilities
- Extent of external works
- Requirements of local and statutory authorities
- Unforeseen work and changes to client requirements
- Speed of construction
- Location.

These and other cost drivers should be carefully considered by the QS to ensure that appropriate allowances are made in the budget estimates and that the proposed capital investment will provide the required rate of return.

#### **9.4.3 Furniture, Fittings and Equipment (FF&E) (Including Soft Operating Equipment (SOE))**

This includes goods needed to furnish the hotel rooms, public areas, kitchen, etc, such as (Lane & Dupre, 1996: 253):

- Silverware (cutlery, decanters, etc.)
- Crockery
- Glassware
- Linen
- Furniture
- Case goods
- Bedding
- Pictures and mirrors
- TVs, and radios
- Lamps
- Pianos
- Kitchen pots, pans and food containers, etc.

#### **9.4.4 Professional Fees and Disbursements**

##### **9.4.4.1 Professional Fees**

In this section, allowances for the various professional fee calculations based on the recommended fee scales of the various professional consultants, are included in your feasibility study.

Cloete (1996) cautions against overlapping or duplication of professional fees, such as the architect charging fees for interior design services when an interior specialist in fact prepares the design.



Often on large developments, a project manager or project coordinator is appointed to control the overall management, coordination and expenditure of the project. A fee should be allowed for when a project manager is appointed.

#### 9.4.4.2 Disbursements

Disbursements is the name for costs such as typing and duplicating, printing of plans, travelling and subsistence, and should be allowed for in the feasibility analysis. It is normal to allow 0,5% of the escalated building cost for this, excluding travelling and subsistence (Cloete, 1996: 12).

#### 9.4.5 Financing Costs

Financing costs include items such as:

- Mortgage registration cost
- Mortgage raising fee
- Cost of capital and/or interim interest on mortgage. This allowance is to cover the finance fee and the interim cost of capital during the construction period calculated according to a cash flow prepared for the project.

#### 9.4.6 Pre-Opening Expenses

Pre-opening expenses include items such as:

- Marketing and promotion costs
- Operational staff training and initiation
- Leasing commissions, only applicable where retail or convenience shops are let through an agent.

#### 9.4.7 Sundry Costs

- a) **Sundry legal fees** are for legal fees paid in respect of agreements to name one.
- b) **Plan scrutiny fee** is a fee paid to, and calculated in accordance with the requirements of the relevant local authority for approval of building plans.
- c) **Stamp duty on lease agreements.** Usually the stamp duty is paid by the tenant but in many cases, especially where a major anchor tenant is involved, the cost is shared equally by the tenant and the landlord (Cloete, 1996: 13).
- d) **Development and promotion fee.** If applicable this can range between 1 and 5% of the escalated building costs.
- e) **Non-recoverable tenant requirements.** This item is for additions and changes made for tenant requirements not allowed for in the hotel building specification.
- f) **Contingencies.** Allow 0.25% to 0.50% of the total estimated capital costs for any unforeseen expenditure. This should not be confused with the building contingency (Cloete, 1996: 14).
- g) **Interim income** is the net income, if any, which is generated before the opening date of the entire hotel facility.
- h) **Other sundry costs,** includes any other items that may be applicable.

## 9.5 Total Net Projected Income (Forecasting Hotel Revenues and Expenses)

*The following text (section 9.5) is a close reproduction of Rushmore and Baum (2001: 239 to 307).*

With regards to estimating hotel revenues and expenses, it should be understood that hotels are unique forms of real estate with many unusual characteristics, including intensive use of labour, cost-of-goods-sold expense categories and a retail product identity. Special knowledge and data are required to estimate a hotel's future income (Rushmore & Baum, 2001: 239).

### 9.5.1 Existing Facility vs. Proposed Facility

Valuing an existing hotel generally requires less fieldwork than a proposed facility. In the case of an existing hotel, the appraiser first reviews the local supply and demand situation and projects the subject's future revenue. Then, using the property's operating ratios obtained from previous years' financial statements, various expense categories are estimated. These estimates should be compared to the operating results of similar properties (if available) or to national averages, and any differences should be resolved. Discrepancies may occur for several reasons, including (Rushmore & Baum, 2001: 239):

- *Unusual Property Characteristics:* Some hotels are more expensive to operate than others. For example, beachfront hotels have higher maintenance costs; properties in the Northeast United States pay more for energy; commercial hotels have more credit card commissions, and airport hotels incur shuttle bus expenses.
- *Assumed competent management:* Projected expenses reflect competent management, while the actual management may be better than, equal to, or less capable than normal.
- *Different levels of occupancy and average rate:* When comparing expense ratios for two properties, the appraiser must ascertain that they operate at similar occupancy levels and have similar average rates. Lodging facilities generally experience more efficient operations as their rates and occupancies increase.

The historical operating results and future expectations should blend into the final income and expense estimate for an existing hostel.

Assembling sufficient market information and comparable data for a proposed facility requires more research. A market analysis should help to accumulate enough information to formulate estimates of occupancy and average rate. Once these two factors have been established, rooms revenue and other income sources may be computed.

Owing to the fact that a proposed hotel has no operating history on which to base an expense projection, the feasibility analyst must either obtain data from existing comparable properties or use national averages. Statistics from either of these sources can be processed to project income and expenses for the proposed subject property.

### 9.5.2 Uniform System of Accounts for Hotels

The data in most hotel financial statements is arranged in accordance with the Uniform System of Accounts for the Lodging Industry (USALI). The USALI provides a simple formula for classifying the accounts used by hotels of all types and sizes. The system's universality allows analysts to compare individual properties or groups of properties that have similar characteristics.

A complete set of financial statements for a hotel or motel should include a balance sheet, a statement of income and expenses, a statement of changes in financial position and any disclosures needed to comply with accepted accounting principles. The analyst is primarily interested in the data contained in the statement of income and expenses.

The following list is extracted from the *Uniform System of Accounts for the Lodging Industry* (1998), published by the Educational Institute of the American Hotel and Motel Association, Florida, USA. It shows how various hotel activities are classified in income and expense statements (Rushmore and Baum, 2001: 241):

#### **Operating Departments**

- Rooms
- Food
- Beverage
- Telephone
- Garage, parking lot
- Guest laundry
- Golf course
- Golf pro shop
- Tennis, racquet club
- Tennis pro shop
- Health club
- Swimming pool, cabanas, baths
- Other operated departments
- Rentals and other income

#### **Undistributed Operating Expenses**

- Administrative and general expenses
- Human resources
- Information systems
- Security
- Transportation
- Marketing
- Guest entertainment
- Franchise fee
- Property operation and maintenance
- Energy costs

#### **House Profit**

- Management fee

**Total Income Before Fixed Charges**

- Rent, property taxes, and insurance
- Interest expense
- Depreciation and amortisation

**Income Before Income Taxes**

- Income taxes

**Net Income**

The total income after expenses for each major revenue-producing department is listed separately. If there are other departments with revenues and expenditures, they too are enumerated. The expenses incurred by undistributed overhead departments and capital expenses are then listed. The entries are totalled to determine the property's income before taxes. Then state and federal income taxes are deducted to arrive at the property's net income.

Because this format does not address the specific needs of the analyst, who must capitalise income after property taxes and insurance (before interest, depreciation and amortisation), a slightly modified system is required to indicate:

**Total Income Before Fixed Charges**

- Property taxes
- Insurance
- Reserve for replacement

**Income Before Debt Service**

Under the USALI, salaries and wages are allocated to individual departments and expense categories as follows:

***Rooms***

- Assistant managers
- Front office
- Housekeeping
- Service (doorman, front)
- House officers and watchmen

***Food***

- Food preparation
- Food service

***Beverage***

- Beverage service

***Administrative and general***

- Manager's office
- Accounting office
- Data processing
- Front office bookkeeping
- Night auditors
- Credit office
- Timekeepers

- Receiving clerks
- Employment office
- Employees' locker attendants

#### ***Marketing***

- Sales department
- Advertising
- Merchandising
- Public relations and publicity
- Research

#### ***Guest entertainment***

- Manager
- Entertainment director
- Stagehands

#### ***Property operation, maintenance, and energy costs***

- Chief engineer and assistant
- Engineers
- Painters and paperhangers
- Radio and television repair
- Grounds and landscape
- Office and storeroom

### **9.5.3 Forecasting Revenue and Expense**

*Note: Refer to addendum 'D' for a case study that demonstrates the forecasting of a hotel's rooms revenue and expenses.*

The forecast of revenue and expense begins by converting the occupancy and average rate projections into an estimate of rooms revenue. Using data collected in the market and industry statistics, the analyst then develops a forecast of other revenue items such as food, beverage, telephone and other income as well as normal hotel operating expenses. Combining all this information produces a highly documented forecast of revenue and expenses, which becomes a key component in estimating market value and evaluating the economics of the investment.

#### **9.5.3.1 Rooms Revenue Defined**

The primary components of rooms revenue (occupancy and average room rate) have been discussed in section 7.8 and 8.7. A projection of rooms revenue is derived using the following formula:

$$\text{Occupancy} \times \text{average room rate} \times \text{room count} \times 365 = \text{Rooms revenue}$$

#### **9.5.3.2 Fixed and Variable Component Approach to Forecasting**

Before projecting individual items of hotel revenue and expense, analysts must understand the fixed and variable component approach to forecasting. This approach produces one of the most accurate models of a hotel's financial performance. It forms the basis for many

computerised hotel forecasting programs utilised by hotel appraisal firms, hotel companies, investors, lenders and developers.

#### 9.5.3.2.1 Theoretical Basis

The fixed and variable component approach is based on the premise that hotel revenue and expenses have one component that is fixed and another that varies directly with occupancy and the use of the facility. A projection can therefore be made by examining a known level of revenue or expense and calculating the portion that is fixed and the portion that is variable. Then the fixed component is held at a constant level, while the variable component is adjusted to reflect the percentage change between the projected occupancy and facility utilisation and the actual occupancy and facility utilisation that produced the known revenue or expense. This process is demonstrated in the following example.

<b>Example</b>
----------------

A 200-room commercial hotel operated last year with an occupancy of 70%, an average room rate of \$104.33, and a rooms department expense of \$1,226,000 or 23% of rooms revenue. A projection for this year indicates that the subject's occupancy is expected to fall to 61% because several new hotels will open in the area during the year. This year's rooms department expense can be calculated using the following procedure:

First, last year's rooms department expense is expressed in this year's dollars by applying a 3% inflation rate.

$$\mathbf{\$1,226,000 \times 1.03 = \$1,263,000 \text{ (rounded)}}$$

The analyst has determined that 60% of the rooms expense is typically fixed and the remaining 40% varies with occupancy. Thus, fixed and variable components of this year's rooms expense are estimated as follows:

$$\begin{aligned} \mathbf{\text{Fixed:}} \quad & \mathbf{0.60 \times \$1,263,000 = \$758,000 \text{ (rounded)}} \\ \mathbf{\text{Variable:}} \quad & \mathbf{0.40 \times \$1,263,000 = \$505,000 \text{ (rounded)}} \end{aligned}$$

Next the variable component is adjusted for the decline in occupancy from 70% to 61%. The percentage decline in occupancy (occupancy adjustment) is calculated by dividing the projected occupancy by the known occupancy.

$$\mathbf{0.61 \div 0.70 = 0.8714}$$

Multiplying the occupancy adjustment by the variable component yields the adjusted variable component.

$$\mathbf{0.8714 \times \$505,000 = \$440,000 \text{ (rounded)}}$$

Finally, the fixed component and the adjusted variable component are combined to produce the estimated rooms department expense at 61% occupancy.

<b>Fixed component</b>	\$ 758,000
<b>Adjusted variable component</b>	<u>440,000</u>
<b>Projected rooms department expense</b>	\$1,198,000

Assuming the hotel's average rate remains \$104.33 during the first projection year, the hotel's rooms departmental expense ratio will increase from 23.0% to 25.8%.

The fixed component of rooms expense represents items such as front desk salaries and the cost of cleaning public areas that must be maintained regardless if the hotel is operating at zero or full occupancy. The variable component is made up of items such as maids' salaries and guest supplies, which vary directly with the level of occupancy.

<b>End of Section 9.5.3.2.1 Example</b>
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### **9.5.3.2.2 Application of the Approach**

The process of forecasting hotel revenue and expenses by the fixed and variable component approach is accomplished in the nine steps outlined below.

#### **Step 1: Obtain Comparable Financial Statements**

All revenue and expense items are projected based on information found in the financial statements of the subject and/or comparable hotels. If the subject property is an existing hotel, then its past operating performance is generally used to establish future projections. For proposed hotels the analyst must rely on the operating results of hotels considered comparable to the subject property.

Obtaining operating information on hotels is relatively simple for firms that regularly appraise existing lodging facilities, but for those who only perform this type of assignment occasionally, comparable financial data can be more difficult to obtain.

The key to selecting financial data for use in projecting hotel income and expenses is to rely on only recent financial statements from properties that are truly comparable to the subject. Hotel facilities vary in many respects, including differences attributable to location, size, facilities, class, management, occupancy and average room rate. Each of these factors can impact on a hotel's financial operating results. When a number of financial statements are available, the following financial comparable selection procedure indicates the order in which factors should be considered to eliminate statements of hotels that are less similar to the subject:

- Average room rate (class)
- Facilities
- Room count
- Management (image & service)
- Occupancy
- Geographic location.

When evaluating several financial statements, the feasibility analyst should first look for income and expense data from hotels that are similar to the subject property in terms of average room rate. A hotel's class or rate structure directly impacts on both income and expense ratios, particularly fixed expenses that are measured on a per-available-room basis. Generally, hotel-operating data should not be compared unless the properties are either in the same class or not more than one class removed. Most hotels can be categorised in one of the following room rate classifications: luxury, first-class, mid-rate, economy (budget), or sub-budget (also refer to section 5.4).

After the analyst has accumulated financial statements from other properties with similar room rates, attention is focused on hotels with comparable facilities to those of the subject property. Hotels can be classified by the types of facilities they offer (e.g., commercial, convention, resort, conference, health spa, suite or extended stay). Within these broad classifications financial comparability can be further refined by matching properties with similar physical components. The facility's age and condition should also be considered. Financial comparability can be enhanced by using the financial statements of properties with similar facilities, particularly if these facilities generate large amounts of revenue (food and beverage) or operating expenses (golf courses).

Room count is the next consideration in the financial comparable selection order. The financial data used in projecting income and expense is generally more reliable when it comes from comparable properties that are similar in size to the subject property. In assessing comparability, size can be defined broadly. A small hotel might be defined as one with 0 to 150 rooms. A mid-sized property would have between 150 and 300 rooms, and properties of 300 to 1,000 rooms would be considered large. A mega-property would have 1,000 rooms or more. These categories can overlap, so size must be evaluated on a case-by-case basis.

When a hotel's future management is known, it is often appropriate to use the financial operating ratios exhibited by other properties managed by this particular operator as a basis for forecasting income and expense. Although more weight should be given to the previous considerations in the financial comparable selection order (i.e., average room rate, facilities, and rooms count), the obvious strengths and weaknesses of the contemplated management should be factored into the analysis, particularly if the property is subject to a long-term management contract.

Occupancy is one of the least important considerations in the evaluation of comparability. When the fixed and variable income and expense forecasting model is used, differences in occupancy levels between the comparable and the subject property are automatically adjusted. Nevertheless, analysts should avoid using financial data from hotels that exhibit widely divergent occupancies.

Geographic considerations are generally given minimal weight in selecting comparable financial data. Most hotel operating expenses are not dependent on the property's geographic location. However, two specific expense categories, i.e. energy cost and property taxes, are strongly affected by local factors. Also, data from markets with unusually high labour costs should not be compared to properties that are not similarly affected.

Analysts should recognise that the financial comparable selection order provides a quick method for identifying financial data that may be comparable to the subject property. In



certain situations it may be appropriate to use data that does not fall within the process described as long as the desired effect, i.e. a proper base for projecting income and expense, is ultimately obtained.

### **Step 2: Adjust comparable financial statements**

Comparable financial statements must usually be adjusted or modified to reflect the subject property's unique characteristics. These adjustments may include changing the average room rate, modifying the income and expense ratios and altering the fixed charges. These changes are made to create a one-year financial statement that uses the subject property's first-year average room rate (expressed in current dollars prior to any initial year discounts) and the income and expense ratios that represent the occupancy level that the comparable experiences. This profit and loss statement is called the base (or comparable base) and will form a foundation for calculating fixed and variable component relationships.

Comparing hotels is never a precise exercise, hence adjustments must be made to individual categories of income and expense to bring the compared hotels' actual operating results closer to the expectations for the subject.

Comparable financial data are adjusted in two stages. In stage 1, the comparable operating data for a particular income or expense category are projected for the subject property using an appropriate unit of comparison. This produces a general estimate of each income and expense category. In stage 2, each of the subject's projected revenue and expense categories is refined by factoring the property's unique physical, operational and location-specific attributes into the final projection.

When projecting income and expense using comparable financial data, it is first necessary to break down the comparable income and expense statement into specific units of comparison. For hotels, these units of comparison include:

- Percentage of Total Revenue
- Percentage of Rooms Revenue
- Percentage of Food and Beverage Revenue
- Dollars per available room
- Dollars per occupied room

Applying units of comparison puts the financial data on a common basis so that the comparable's operating results can be analysed and projected for the subject. A given unit of comparison may be better suited to some revenue and expense categories than others. Certain units are more applicable because of specific volume relationships, which cause individual revenue and expense categories to react differently to changes in a hotel's occupancy, average room rate and food and beverage volume. If, for example, a revenue or expense category varies in relation to changing occupancy levels or average room rates, the appropriate unit of comparison would be the percentage of rooms revenue or total revenue. If the category is primarily fixed, then greater emphasis should be placed on the dollars per available room unit of comparison. A category that is food and beverage sensitive would be expressed as a percentage of food and beverage revenue.

Table 9.5.3.2.2(a) shows the primary units of comparison applied in projecting each category of hotel income and expense from a comparable financial statement.

**Table 9.5.3.2.2(a): Units of Comparison Applied**

(Source: Rushmore and Baum, 2001: 253)

Unit of Comparison	Sensitivity Factors	Used to Project the Following Income and Expense Categories
Percentage of total revenue	Occupancy Average room rate Food & beverage revenue	Administrative and general Management fee Marketing Property operation and maintenance
Percentage of rooms revenue	Occupancy Average room rate	Food revenue Telephone revenue Other income Rooms expense
Percentage of food and beverage revenue	Food & beverage revenue	Food and beverage expense
Dollars per available room	Fixed categories	Administrative and general Marketing Property operation and maintenance Energy Insurance Property taxes
Dollars per occupied room	Occupancy	Food revenue Beverage revenue Telephone revenue Other income Rooms expense Energy

Each of the five units of comparison in the first column is sensitive to the various factors shown in the second column. For example, the percentage of total revenue is sensitive to a hotel's occupancy, average room rate, and food and beverage revenue. The last column shows which income and expense categories are best projected by a specific unit of comparison. Since most items of income and expense have both a fixed component and a variable component, it is some times appropriate to use more than one unit of comparison.

Once a projection for a category of income and expense is made, using the units of comparison described, it is often necessary to fine-tune the projection to account for the physical, operational and location-specific differences between the comparable and subject property. Primary differences that should be adjusted include:

- Differences in average room rate, particularly if the subject property is in a higher or lower class (e.g., economy, mid-rate, first, luxury) than the comparable
- Substantial differences in size (room count)
- Differences in food and beverage volume, particularly if one property has significantly more or less beverage or banquet revenue
- Location-specific differences, which generally affect energy costs and property tax expenses.

Since fixed and variable analysis adjusts for differences in occupancy between the comparable and the subject property, no specific adjustment is needed to account for a variance in occupancy at this point in the projection process.

When fine-tuned adjustments are required to account for differences between properties, the unit of comparison used in the projection is adjusted either upward or downward in the manner described in the following:

***Percentage of Total Revenue:*** Adjusting the percentage of total revenue unit of comparison upward for an expense item causes the dollar amount of that expense to increase. When the comparable has an average room rate that is higher than the rate of the subject property, its operating expense ratios based on a percentage of total revenue tend to be lower. If such an unadjusted percentage were to be applied to the subject property, it would be understated. Therefore, the unit of comparison should be fine-tuned upward.

It is difficult to determine how to adjust the percentage of total revenue based on the property's size. In general, if the comparable is slightly larger than the subject property, its operating expense ratios, which utilise a percentage of total revenue, tend to be lower because some of the fixed expenses (such as payroll) can be spread out over a greater amount of revenue. This advantage ends at the point when added costs must be incurred to handle the additional rooms. For example, a single general manager might operate a 100-room hotel efficiently. That same individual could probably handle an additional 75 rooms, which would decrease the management payroll expressed as a percentage of total revenue. Once the room count exceeds 175, however, it may be necessary to hire an assistant manager to take over some of the operational responsibilities. This extra expense quickly increases the expense ratio.

When the comparable has more food and beverage revenue than the subject property does, its operating expense ratios, based on a percentage of total revenue, tend to be lower and should be fine-tuned upward when projecting expenses for the subject property.

***Percentage of Rooms Revenue:*** The fine-tuned adjustments for this unit of comparison are the same as those just described for the percentage of total revenue.

***Percentage of Food and Beverage Revenue:*** This unit of comparison is used primarily to project food and beverage department expenses. As the volume of food and beverage increases, the food and beverage expense ratio usually decreases. If the comparable has more food and beverage revenue than the subject property does, its food and beverage expense ratio would be lower and should be adjusted upward to project the subject's food and beverage department expenses. An even greater upward adjustment is needed if the comparable has a considerable amount of beverage or banquet business, which tends to operate at a greater profit margin.

***Dollars Per Available Room:*** Adjusting the dollars per available room unit of comparison upward for an expense item causes the dollar amount of that expense to increase.

When the comparable has an average room rate that is higher than the subject property's rate, it is likely to be providing a superior level of service. This would likely increase the cost of operations on a per-available-room basis. In this instance the unit of comparison used to project expenses for the subject property should be adjusted downward.

The preceding discussion of an efficient room count also applies to the dollars per available room unit of comparison. If the comparable has a room count that is less efficient than the subject's, its operating expenses expressed on a per-available-room basis could be

overstated and may have to be adjusted downward when making a projection for the subject property.

If the comparable has a greater amount of food and beverage revenue than the subject property does, its operating expenses will probably be higher when expressed on a per-available-room basis. In this case the unit of comparison used to project expenses for the subject property should be adjusted downward.

***Dollars Per Occupied Room:*** Since the occupancy level used for the subject property's base profit and loss statement will be the same as the occupancy of the comparable, the adjustments made to this unit of comparison should be identical to those used for the dollars per available room.

### **Step 3: Revise the Base**

The base revenue and expense categories must be revised to reflect current dollars for each forecast year and the anticipated rate fluctuations resulting from other, non-financial variables (general inflation).

Step 3 is intended to adjust the comparable operating data that make up the subject property's base so that it will reflect forecast costs stated in the current dollars anticipated for each particular year. To compute the fixed and variable operating data and forecast relationships for each projected year, an assumed rate (or rates) of inflation should be applied to each operating category.

Each revenue and expense category can be affected by different factors that increase or decrease associated costs. For example, future changes in the average room rate are largely influenced by local supply and demand conditions, which may modify general inflation assumptions. Energy costs are usually tied to fuel prices, which often fluctuate erratically. Changes in property taxes are often correlated to changes in the local tax base, which means that the rate assumption may be negative in an area experiencing rapid new development. Labour costs can change radically if a new union contract is implemented.

The analyst should look at each revenue and expense category and project an individualised assumption that reflects the market's current view of pricing for the components within the stated category or the category as a whole. Often it is appropriate to apply a single inflation factor to all categories of revenue and expense data, particularly for the years projected after the property reaches a stabilised level of occupancy. This assumes that all other cost-influencing variables remain stable.

### **Step 4: Estimate Fixed and Variable Percentages For Each Revenue and Expense Category**

Fixed and variable percentages are estimated for each revenue and expense category. Table 9.5.3.2.2(b) shows typical ranges of fixed and variable percentages and the index used to measure the amount of variable change.

These fixed and variable percentages were developed from a regression analysis that evaluated hundreds of financial statements to determine which portion of each revenue and expense category was fixed and which was variable.

The index of variability refers to the factor that controls the movement of the variable component. For example, the variable component of food revenue moves in response to occupancy changes. Beverage revenue seems to be tied directly to food revenue. Food and beverage expense levels depend largely on changes in food and beverage revenue. The variable components of undistributed operating expenses and all fixed expenses seem to move in relation to total revenue.

**Table 9.5.3.2.2(b): Fixed and Variable Percentages**

(Source: Rushmore and Baum, 2001: 247)

Revenue and Expense Category	Percent Fixed	Percent Variable	Index of Variability
<b>Revenues</b>			
Rooms	N/A	N/A	N/A
Food	10 - 50%	50 - 90%	Occupancy
Beverage	0 - 30	70 - 100	Food revenue
Telephone	10 - 40	60 - 90	Occupancy
Other Income	30 - 60	40 - 70	Occupancy
<b>Departmental Expenses</b>			
Rooms	50 - 70%	30 - 50%	Occupancy
Food	35 - 60	40 - 65	Food revenue
Beverage	35 - 60	40 - 65	Beverage revenue
Telephone	55 - 75	25 - 45	Telephone revenue
Other income	40 - 60	40 - 60	Other income
<b>Undistributed Operating Expenses</b>			
Administrative and general	65 - 85%	15 - 35%	Total revenue
Transportation	65 - 90	10 - 35	Occupancy
Human resources	80 - 95	5 - 20	Total revenue
Information systems	80 - 100	0 - 20	Total revenue
Security	65 - 90	10 - 35	Occupancy
Marketing	65 - 85	15 - 35	Total revenue
Franchise fee	0	100	Rooms revenue
Property operation & maintenance	55 - 75	25 - 45	Total revenue
Energy (utilities)	80 - 95	5 - 20	Total revenue
<b>Fixed Expenses</b>			
Management fee	0%	100%	Total revenue
Property taxes	100	0	Total revenue
Insurance	100	0	Total revenue
Reserve for replacement	0	100	Total revenue

### **Step 5:**

Each individual line item in a hotel's financial statement is projected separately using the fixed and variable calculations. The fixed component is estimated by multiplying the appropriate fixed percentage by the base revenue or expense line item for the corresponding projection year. The variable component is estimated in steps 6 through 8.

### **Step 6:**

Variable components are assumed to vary directly with the index of variability established in step 4. The amount of variable change is quantified by dividing the appropriate projected index of variability by the index of variability for the base. For example, assume that the projected occupancy percentage for the subject property in Year 1 is 62%. The occupancy of the base is 73%. Dividing the projected occupancy by the base occupancy results in the following variable percentage change:

$$\frac{\text{Projected occupancy}}{\text{Base occupancy}} = \frac{0.62}{0.73} = 0.849 \text{ or } 84.9\%$$

Basically, this calculation shows that, as of that projected year, the subject's occupancy is estimated to be 84.9% of the occupancy percentage found in the comparable base data.

#### **Step 7:**

The unadjusted variable component is calculated by multiplying the appropriate base revenue or expense item for the projected year by the variable percentage estimated in step 4. Note that the total of the fixed and variable percentages for each line item must equal 100%.

#### **Step 8:**

The unadjusted variable component must now be adjusted for variability in the index by multiplying the results of step 7 by the variable percentage change calculated in step 6. The product is known as the *adjusted variable component*.

#### **Step 9:**

The forecast for the revenue or expense category is the total of the fixed component calculated in step 5 and the adjusted variable component calculated in step 8.

### **9.6 Capital Expenditure (CapEx)**

This section called capital expenditure (also commonly referred to as CapEx) is included merely to highlight the meaning of the term, why it is important to understand it and to clarify the differences between capital expenditure and capital cost (development cost).

Mellen et al (2000: 1) cites the definition of capital expenditure as defined in The Appraisal Institute's (USA) Dictionary for Real Estate Appraisal as: "*Investments of cash or the creation of liability to acquire or improve an asset, e.g., land, buildings, building additions, site improvements, machinery, equipment; as distinguished from cash outflows for expense items that are normally considered part of the current period's operations.*"

From this definition it could be accepted that capital expenditure is similar to capital cost (development cost, discussed in section 9.4.2), but does not include costs such as marketing and pre-opening expenses, which form part of a project's development cost.

The International Society of Hotel Consultants (ISHC) in their CapEx 2000 study, extends the definition of the Appraisal Institute, to include (Mellen, 2000: 2):

*" the cost of replacing worn out furniture, fixtures and equipment, as well as the costs of:*

- *updating design and decor*
- *curing functional and economic obsolescence, thereby extending both the physical and economic life of the asset*
- *complying with franchisors' brand requirements*
- *technological improvements*
- *product change to meet market demands*
- *adhering to government regulatory requirements*

- *replacing all short and long lived building components due to wear and tear.*

*Accordingly, for the purpose of this study, CapEx represents the amount of money actually spent by a hotel owner to undertake all of the foregoing, as well as the replacement of furniture, fixtures and equipment (“FF&E”) components in an existing hotel. Reserves, on the other hand, represent the amount of money set aside (in some form or fashion) for the future undertaking of the above, which includes renovations and refurbishments to a hotel, as well as replacement of FF&E.”*

## **9.7 Cash Flow Projections**

*“Financial considerations begin with a calendar of events determining outlays and receipts and thus the span of time for which specified amounts of money are utilised. A bar chart indicating the timing and duration of all the major activities is very useful” (Cloete, 1996: 17).*

In the explanation of the basic financial feasibility model (BFFM), Pyhrr et (1989: 170) highlights several disadvantages, such as that, it analyses the project’s cash flows for only one year, ignoring future revenues and expenses, and does not incorporate present-value analysis, does not explicitly consider equity build-up through loan amortisation, price inflation, start-up or transactions costs, nor can it deal effectively with the erratic nature of net operating income (NOI) and hence the “riskiness” of the project.

To solve all the shortcomings of the basic financial feasibility model, a discounted-cash-flow (DCF) model needs to be applied (Pyhrr et al, 1989).

*“[Financial] return is typically analysed within an accounting framework that focuses on the source and timing of cash flows. The expected residual cash flow generated by income-producing real estate comes in two parts. First are the annual cash flows to be received throughout the holding period. Second are the capital appreciation or proceeds from sale or disposal of the real estate” (Wurtzebach and Miles, 1995: 555).*

Wurtzebach and Miles (1995) further elaborate that the discounted cash flow (DCF) model brings together, in a straightforward accounting framework, all the factors that affect the return from a real estate investment. All expected cash flows are reduced to a single figure, the present value. The cash flows for a hotel include all cash inflows such as room-, restaurant and bar-, and other amenity revenues and ultimately the proceeds of sale. It also includes all cash outflows, such as operating expenses, taxes, and debt service. The present value figure represents the value today of the residual equity claim to future cash flows adjusted for both the time value of money and the risk associated with the expected cash flows. The net present value (NPV) is the difference between the present value of the expected inflows and the cost of the project. If the NPV is positive, the investment meets the investor’s requirements.

Estimates of operating cash flows reflect the analyst’s knowledge of existing market conditions and market trends that are crucial to a successful investment analysis. After the operating cash flow is performed, claims of the lender (debt service) and the government (income tax liability, if any) in calculating the after-tax residual cash flow should be included. The real estate analyst must consider the investor’s marginal tax rate, after-tax required rate of return or discount rate, expected investment horizon or holding period and the expected sales price at the end of the holding period.

Cloete (1996) distinguishes between two types of cash flows for real estate developments:

- Construction cash flow
- Income and expenditure cash flow.

### **9.8 Income Tax**

*“If applicable, the effects of income tax on the return of the project and its cash flow may be illustrated. It is useful to provide the developer with a five-year projection of the effects of income tax”* (Cloete, 1996: 19).

Cloete (1996) highlights the fact that the Receiver of Revenue will allow capital incentive allowances as well as wear and tear tax incentives and deductions.

### **9.9 Measures of Return**

*“The success of a development is measured by the extent to which the investor’s objectives are met. These objectives may be in terms of maximising yield, beating inflation, the service of a public need, etc. The decision-making process is based on the results of comparing the results of information analysis with the success criteria of the developer”* (Cloete, 1996: 20).

Financial yield can be measured in a number of ways (Cloete, 1996: 21):

- **Initial Return**

Properties are often sold on an initial rate of return (e.g. 10%) which is the first year’s net income divided by the capital outlay.

- **Payback Method**

This is simply the capital outlay divided by the average net income to determine the duration it will take to get the investor’s capital back. The time value of money is not taken into account.

- **Return On Investment (ROI)**

ROI is the actual net income in each year divided by the total capital outlay. The average return is the average ROI over a period of 20 years, for example.

- **Net Present Value (NPV)**

NPV is the net income discounted back at the required rate of return. Should the NPV exceed the actual capital outlay a profit is made. This method takes into account the time value of money, at a fixed discounting rate, which is not always the case in practice.

- **Internal Rate of Return (IRR)**

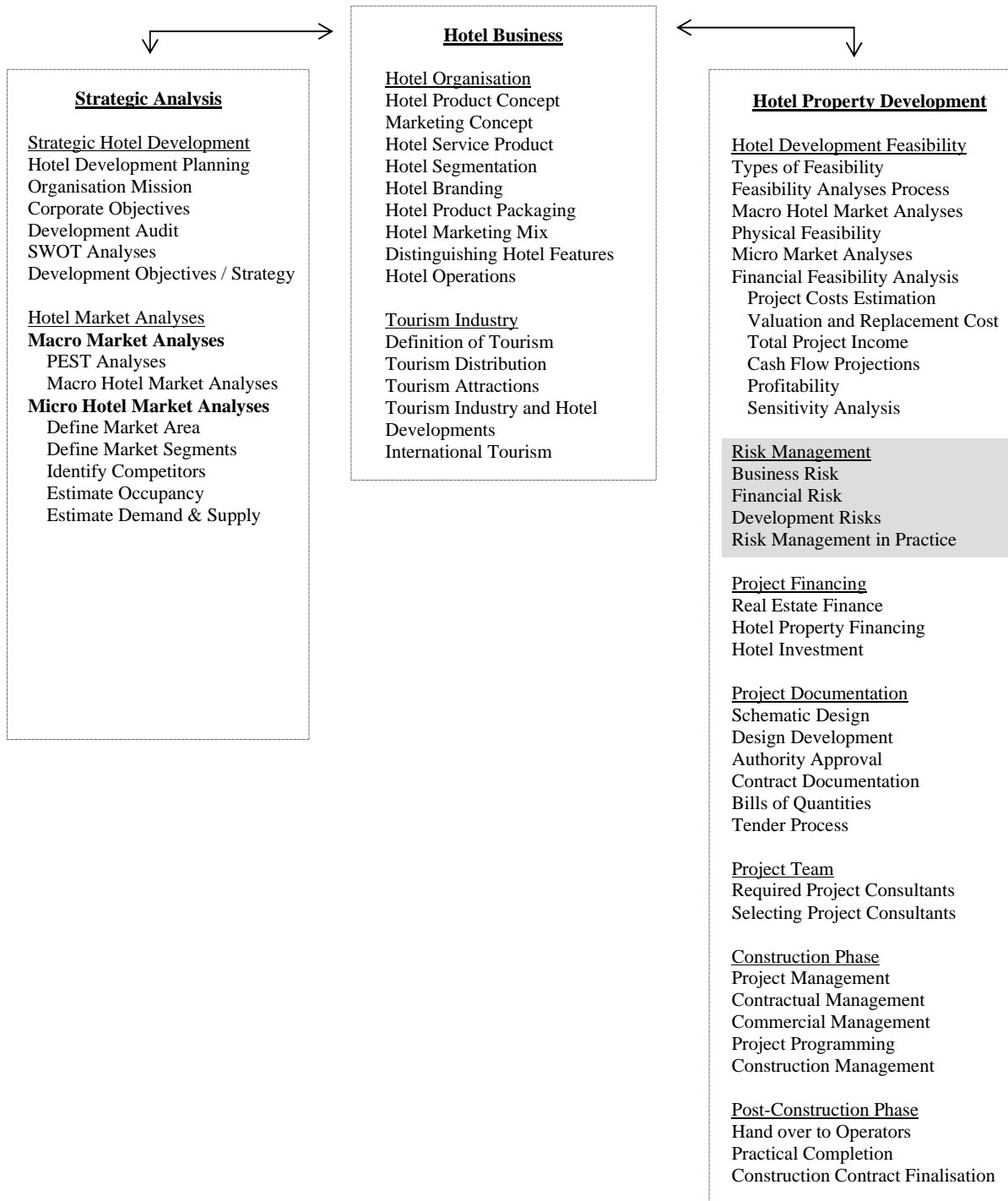
The IRR is that interest rate that will render the NPV of the total net cash flow of a project (including the development cash flow) equal to zero.



*“An acceptable percentage of IRR will vary from investor to investor depending on their investment criteria, but should be in excess of the rate of interest for long-term Government stock – the rationale being that Government stock is blue-chip whereas the property development is exposed to risk which should be discounted by 1 to 2% (or more, depending on the perceived risk of the development). The IRR method is particularly useful in ranking alternative investment opportunities with different economic lifespans. It is not possible to calculate the IRR if the land value is not known and a residual land value calculation is usually called for” (Cloete, 1996: 21).*

**Chapter 10:**

**Risk Management**



## 10 Risk Management

### 10.1 Introduction to Risk Management

*“Risk management is a process used by the project teams to reduce the impact of risks on the outcome of a project, through the identification, appraisal and management of potential risk events throughout the life of the project”* (Ransley and Ingram, 2000: 138).

Ransley and Ingram (2001) make it clear that construction projects potentially involve a high degree of risk exposure, which is due to the one-off nature of many schemes, their long development programmes and the uncertainties that are often associated with on-site construction operations. Risk management techniques should be adopted, which could potentially make a significant contribution to the successful delivery of projects. These techniques enable the project team to reduce the impact of risks, improve the overall management of a project and be more certain of achieving the client’s objectives.

Under a formal risk management process, risks are identified, then an assessment is made of the cost, time and quality consequences of a risk occurring, and finally where appropriate, mitigating actions are identified.

The principal benefits of risk management are (Ransley and Ingram, 2001: 148):

- Greater certainty of project outcomes
- Improved control of risks through pre-planning and early remedial action
- Encouragement of ‘right first time’ thinking through pre-planning of responses to risk events
- Allocation of responsibility for risk mitigation to the party best placed to manage the risk
- Implementation of cost-effective risk mitigation measures
- Effective control of the contingency sum.

Risk management is a team-based process, utilising the knowledge and experience of the whole project team to manage the client’s exposure to risk. The principal stages in the process are (Ransley and Ingram, 2001: 149):

- 1) **Information gathering:** Understanding the project and setting the scope of the risk management process.
- 2) **Identifying risks:** Risks are identified by questionnaire, interview or by brainstorming. The identified risks are entered into a formal risk register and prioritised. The most significant risks are selected for further analysis and active management.
- 3) **Analysing risks:** Risks are analysed to calculate risk allowances for their time and cost consequences. There is a wide range of techniques available to the Quantity Surveyor, which varies in complexity, transparency and reliance on proprietary computer software (IT) applications.

- 4) **Managing risks:** Management concerned with risks must be identified. The options available to the project team to manage risk are:
- *Avoidance:* Changing the project to prevent the risk occurring
  - *Reduction:* Altering the design, specification or working method to minimise the impact of the risk, should it occur
  - *Transfer:* Reallocating risks to other parties, through insurance or through the terms of a building contract
  - *Acceptance:* Continuing management of risks without any pre-emptive action
  - *Reviewing the register:* A review is important to monitor progress on risk mitigation measures and to update the risk register to account for new risks, expired risks and changing assessments of existing risks.

## 10.2 Risk Prevention

The occurrence of perceived risks frequently impact on the outcome of major projects and are not always provided for at the outset. Effort should be made at the beginning of a project to identify possible major risks and a strategy should be agreed to deal with them.

The client or developer can lead the risk prevention process by (Ransley and Ingram, 2001: 163):

- Establishing a clear and concise brief
- Appointing experienced advisers
- Accepting objective advice even when unwelcome
- Accepting realistic targets
- Accepting a shared responsibility for time, cost and quality control
- Making timely decisions and sticking with them
- Insisting on value rather than lower price
- Applying a systematic approach to the analysis and management of risk.

## 10.3 Types of Risk

Wurtzebach and Miles (1995) define the several types of real estate investment risk as:

- Purchasing power risk
- Business (and related market) risk
- Financial risk
- Liquidity risk.

Hospitality projects are particularly sensitive to time and cost overruns, as well as poor quality finishes consequences. Some of the significant areas of risk in major building projects of lengthy duration include (Ransley and Ingram, 2001: 162):

- Statutory regulations (approvals and licences)
- Funding/fiscal arrangements
- Inflation and exchange rates
- Budgeting and estimating data
- Adequacy of design
- Site conditions, climate, access and familiarity

- Market conditions (labour, materials, company)
- Scope of project.

In addition to the listed risks, Echavarren (2001) elaborates on risks associated with a real estate project.

### **10.3.1 Inflationary Risks**

Most investors agree that their money will buy less in the future than today, hence the first form of risk that they want to be compensated for is likely to be for inflation eroding. There is also a risk that future rates of inflation may be underestimated (Wurtzebach and Miles, 1995).

### **10.3.2 Financial Risk**

Financial risk is the potential inability of a project's NOI (net operating income) to cover the required debt service. Such an event is more likely to occur when a high proportion of the purchase price is financed with debt. The less debt used in the capital structure, the lower the financial risk.

Lenders could offer a variety of variable rate mortgages that could also affect financial risk. If market interest rates rise, the debt service associated with many non-fixed-rate mortgages will also rise. As the debt service rises, the NOI may not be sufficient to cover the increase. Such projects financed with non-fixed-rate mortgages may expose the borrower to greater financial risk (Wurtzebach and Miles, 1995).

A hotel investment may be separated into the land, building shell, interior assets and operating systems. To limit investment risk for a developer or hotel operator, the land and building shell may be (Lawson, 1997: 36):

- Separately owned as part of a mixed development of shops, offices etc., and leased to a hotel company
- Sold to a property company or financial institution under a leaseback arrangement
- Assessed on a rental basis as part of company policy to provide financial control over its property assets
- Operated through a management contract arrangement by a separate hotel company.

Lawson (1997) further notes that various other financing arrangements may also be adopted to reduce initial investment outlays, defer capital repayments or raise additional cash:

- Rental or hire purchase of equipment and furnishings
- Loan negotiation and restructuring, including repayment of interim and short-term finance (see sections 1.4.6 and 1.4.7)
- Increase in company equity through stock market flotation or cash calls on investors.

### 10.3.3 Business Risk

The possibility that the investment's cash flows will not be sufficient to justify the investment, represents the degree of business risk associated with the investment.

Business risk is determined by (Wurztebach, 1995: 557):

- 1) Type of project
- 2) The project or business' management, and
- 3) The particular market in which it is located.

### 10.3.4 Liquidity Risk

*“An investor would ideally want to be able to sell quickly and with out substantially discounting the price below fair market value. The liquidity risk associated with a particular investment is the risk that a quick sale will not be possible or that a significant price reduction will be required to achieve a quick sale”* (Wurtzebach and Miles, 1995: 558).

Real estate is generally considered an illiquid asset, not easily convertible to cash without discounting the price. Consequently, the liquidity risk is high for real estate investments.

### 10.3.5 Project Development Risk

*“Based on our experience of the review of real estate projects, the most common risks of [property development] are as follows”* (Echavarren, 2001: 4):

#### 10.3.5.1 Basic Definitions

- Lack of vision and objectives in the project: the project arises on impulse and its strategy and objectives are not clearly defined
- Unrealistic objectives: estimated savings or expected returns are not calculated properly
- Inadequate project specifications, requirements not calculated, areas undefined.

#### 10.3.5.2 Feasibility and Design

- Insufficient market analysis
- Inadequate design for the objectives pursued
- Design prevails over functionality and feasibility.

#### 10.3.5.3 Licences and Permits

- Conflict of interests with local authorities
- Sluggish, inadequately planned administration
- Management of zoning and urban development aspects not based on adequate procedures.
- Official formalities based mainly on good relations with municipal councils.

#### **10.3.5.4 Contracts**

- Insufficient breakdown of project units
- Incomplete documentation of contracts
- Inadequate contractual provision for future disputes
- Contracts awarded mainly on the basis of prices without taking into account the quality or experience of the contractor.

#### **10.3.5.5 Construction**

- Inadequate or unrealistic estimates of cost and/or deadlines
- Inadequate planning of the project
- Insufficient communication structure with internal personnel and/or contractors
- Lack of procedures
- Lack of involvement of future users and managers.

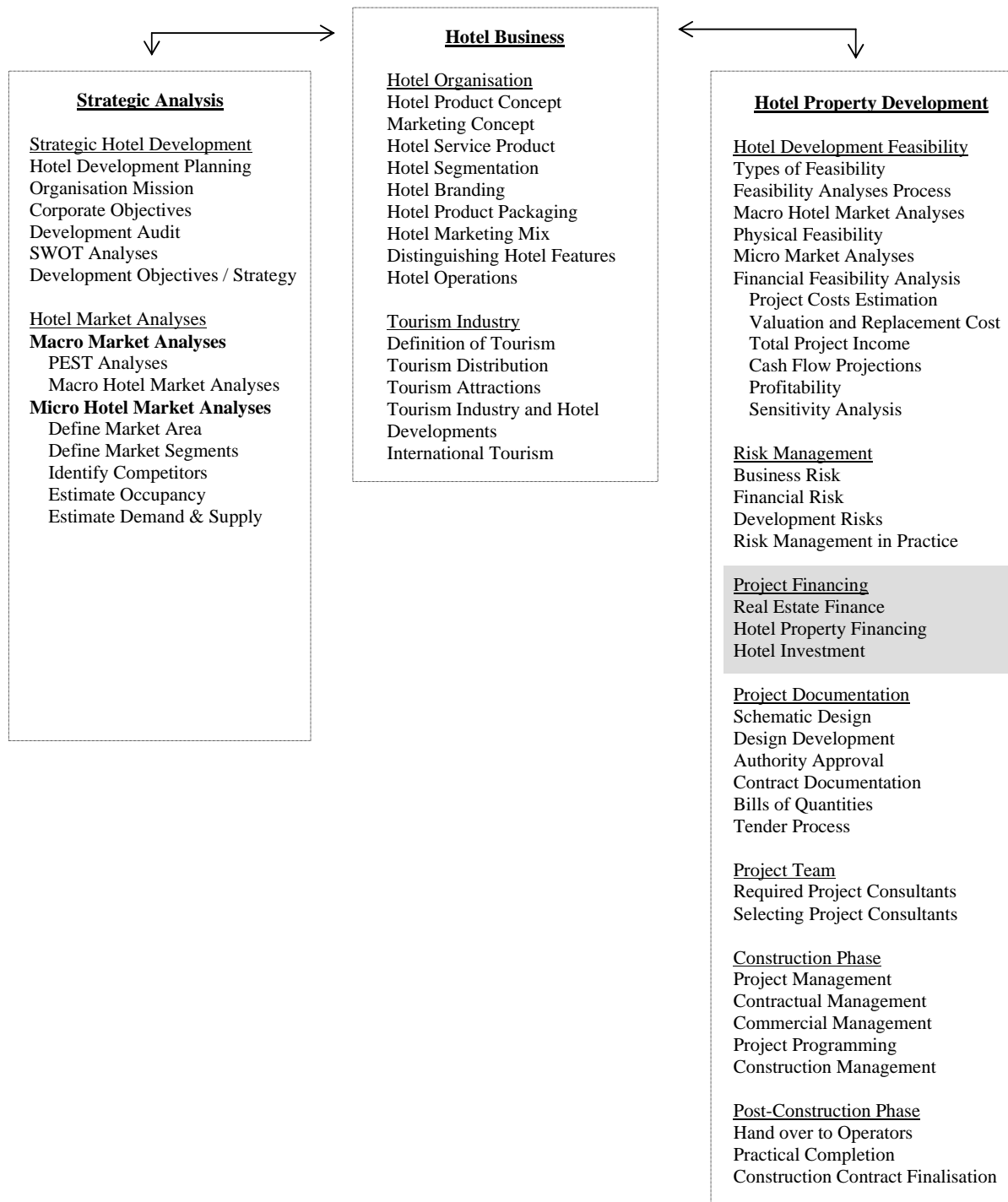
#### **10.3.5.6 Rental / Sale / Occupancy**

- Non-existent marketing plan
- Inadequate occupancy planning
- Failure to consider the final internal or external customer.

In short, the performance of any real estate project implies the assumption of a series of risks that will have a significant impact on the success or failure of the project.

A systematic, objective and independent review of a project and of its handling by the organisation is essential in order to minimize the risks of the project, increase its value and ensure its economic success.

## Chapter 11: Financing Hotel Developments





## **11 Financing Hotel Developments**

Obtaining financing for developing a hotel property calls for creativity, tenacity, and flexibility. Not only do hotel developers and operators aggressively compete for a constantly changing pool of funds (both equity and debt), but they also have to deal with increasingly complex terms and conditions for the use of those funds.

*“During the relatively stable decades of the 1960s and 1970s [in the USA], real estate financing remained an orderly, standardized process for matching developers with investors and lenders. Inflation and interest rates fluctuated only slightly. The one wish developers had, was for a speedier process. During the late 1970s and early 1980s, real estate financing, stimulated by tax incentives and high inflation rates, increasingly involved financial institutions becoming equity or quasi-equity partners. These institutions sought both income and equity participation. Income participation included sharing in the effective gross revenue, net operating income, cash flow after debt service, or income above a base income. Equity participation included sharing in the proceeds of the sale or refinancing, or sharing in the tax benefits” (Baltin et al, 1999: 55).*

However, in stringent economic times the supply of commercial real estate (including hotels) outweigh the demand and financial institutions become quite reluctant to finance hotel property due to the additional risks involved. Distressed hotels can be purchased at a fraction of their replacement cost. Consequently there is no incentive to build new hotels, and financing for hotel construction ceases. By the time the economy recovers, most of the distressed hotels are sold off and the prices of hotels begin to stabilise.

The financing of lodging properties bears little resemblance to office, industrial, or residential projects. Lodging properties, which rely on the success of their operational business, are often viewed as high-risk investments with tremendous upside potential. Lenders, therefore, tend to limit their attention to projects that are well conceived and well located, and that involve experienced developers and operating companies.

### **11.1 Sources of Hotel Development Funds**

Funding hotel property development could be achieved through a range of approaches. The traditional sources of funds for a company are (Ransley & Ingram, 2000: 76):

- Retained profits; the reinvestment of profits derived from trading.
- Issue of more shares for cash; this will require an increase in share dividends to be paid even if the dividend remains at the same rate for all investors.
- Long-term borrowing; raising funds through the capital markets in the form of debentures or from institutional loan providers (either of these methods will increase the levels of annual interest to be paid and as a result will raise the gearing of the business).
- Short-term borrowing; this may be available by delaying payments to creditors or by raising the level of overdrafts. However, long-term investments funded from short-term sources are clearly risky and should be avoided.

Expansion in the hotel industry, state Ransley and Ingram (2000), has recently been funded using a range of other mechanisms including real estate investment trusts (REITs) and management contracts. The modern REIT has its origin in the USA and is a real estate mutual fund permitting small investors to participate in large, professionally managed real

estate projects. Real estate investment trust shares provide an effective vehicle for maintaining liquidity.

The growth of USA hotel management companies was extensive during the 1990s. New hotel properties financed by owners with little operational experience, have increased considerably, laying fertile ground for management companies to offer their expertise in running the property. In return for operational expertise, the management company receives a fee based on gross operating profit levels. Contrary to the early days of management contracts where companies seldom obtained shares in a hotel development, it is now not uncommon for them to hold some level of equity investment (shareholding) of the relationship.

Baltin et al (1999: 56) lists five major sources (past and present) of hotel financing in the USA context:

- Life Insurance Companies
- Savings and Loan Associations
- Commercial Banks
- Credit Companies
- REMICs (Real estate mortgage investment conduits)

In addition to Baltin and, Ransley and Ingram, Swarbrooke (1999) distinguishes between direct financial contributions (such as loans and grants) and indirect financial assistance.

Most direct funding comes from the private sector in the form of overdrafts, long/medium/short term loans, commercial mortgages, venture capital, equity, and business expansion schemes. Direct public funding, as an example (not limited to Europe), granted by organisations such as the European Regional Development Fund, European Social Fund, European Investment Bank, European Coal and Steel Community and the European Agricultural and Guidance Funds. Other public sources are international agencies such as the International Bank for Reconstruction and Development (IBRD) and its affiliates, United Nations Development Fund (UNDP) often working in association with the World Tourism Organisation (WTO), Organisation for Economic Cooperation and Development (OECD) mutual aid programmes, European Union (EU) and other regional and national organisations as well as bilateral aid agreements between countries. In addition to the international agencies and bodies, national funding for infrastructure (roads, airports, technical services) could be sourced by means of urban development grants, selective grants for small businesses, and buildings of historic or architectural interest, etc.

Indirect funding by the private sector includes sources such as leasing to reduce capital cost, hire purchases, sale and leaseback arrangements, concessions, franchises and sponsorships. Indirect funding from the public sectors includes provision of land free of charge, tax 'holidays' and tax allowances, provision of costly infra-structure, duty concessions and the supply of labour through educational and training programmes.

## **11.2 Hotel Development Financing Methods**

*“Developers will look in vain for standard methods of financing lodging properties, or for standard financing packages. They do not exist. In fact, financing conditions change almost daily. The ability to analyse, interpret and predict trends in the equity and debt financing markets is essential for success in developing and operating hotels. A project team’s ability*

*to select a proper financing method depends on its experience and on its understanding of the dynamic characteristics of available financing mechanisms. Today, developers and operators commonly turn to specialists in the field of hotel finance for an explication [guidance or explanation] of a project's financing alternatives and a program for obtaining the best financing package” (Baltin et al, 1999: 55).*

Available financing methods can be grouped into three categories, i.e. short to intermediate term debt instruments, long-term debt instruments and equity structures. When a project is characterised by high risk, when permanent financing does not cover the entire development cost, or when sharing equity is not desirable, developers often use short- to intermediate term financing/debt. The most common short to intermediate term debt instruments are (Baltin et al, 1999: 56):

- Construction Loans
- Combined Construction and Term Loans
- Term and Bullet Loans
- Convertible Mortgages
- Land Sale-Leasebacks and Leasehold Loans
- Permanent Loans
- Mortgages with a Kicker
- Wraparound Mortgages
- Other Long-Term Debt Instruments:
  - Seller financing
  - Exchanges
  - Second mortgages
  - Standby mortgages.

On the equity side, three major structures are commonly used to finance hotel development, as highlighted in the following points (Baltin et al, 1999: 57):

- Joint Ventures
- Limited Partnerships
- All-Equity Financing.

### **11.3 Preparing a Loan Package**

All sources of financing for hotels (lenders, parties to limited partnerships and joint ventures, buyers and sellers) require certain documents and reports. Lenders usually require the following documents (Baltin et al, 1999: 59):

- A transmittal letter to the lender from the project team that clearly states the loan amount requested.
- A one-page facts sheet that describes the project, its size, type of ownership and management, operating characteristics, location and design.
- Rendering of the proposed project, a preliminary site plan and general design specifications.
- Formal market study prepared by a nationally recognised hotel consulting firm.
- Cash flow statement that projects the cash available for debt service and identifies the first expected stabilized year of operation.
- Any agreements or letters of understanding with a hotel operating company.

- Any franchise agreement.
- Resumes and financial statements on the project's owners and developers.
- Deed, title policy, or lease agreement for the site.
- All documents (such as legal agreements, other leases, constraints and easements) that affect the site or project.
- Environmental assessment of the site showing that the site is free of soil contaminants, underground storage tanks or possible hazardous materials.
- Any environmental impact statements or reports required for development approval.
- Descriptions and photographs of similar projects developed by the developer and operator.

These documents should be organised and presented in a professionally prepared folder, binder, or booklet. Glossy reports containing mostly superficial information or marketing brochures are materials that lenders do not want/need.

#### **11.4 Evaluating the Financing Package**

Developers, investors, and operators set widely different objectives for their investments and thus use different criteria for deciding whether to become involved in a hotel project. *"The three criteria most commonly used to judge the viability of a hotel project are the internal rate of return (IRR) hurdle rate, debt service coverage, and the size of the loan relative to the value of the project"* (Baltin et al, 1999: 59).

The IRR hurdle rate is the minimum acceptable total return on investment. A developer, investor, or operator will each determine its own IRR hurdle rate. In the USA from the mid-1990s, reports Baltin et al (1999), the pre-tax IRR hurdle rates for equity capital invested, ranged from 12 to 16 percent for freestanding hotels, and from 11 to 20 percent for hotels in mixed-use projects. To determine the IRR, the cash flow should be defined as cash available after all operating expenses, property taxes, insurance, reserves for replacement, and incentive management fees are deducted.

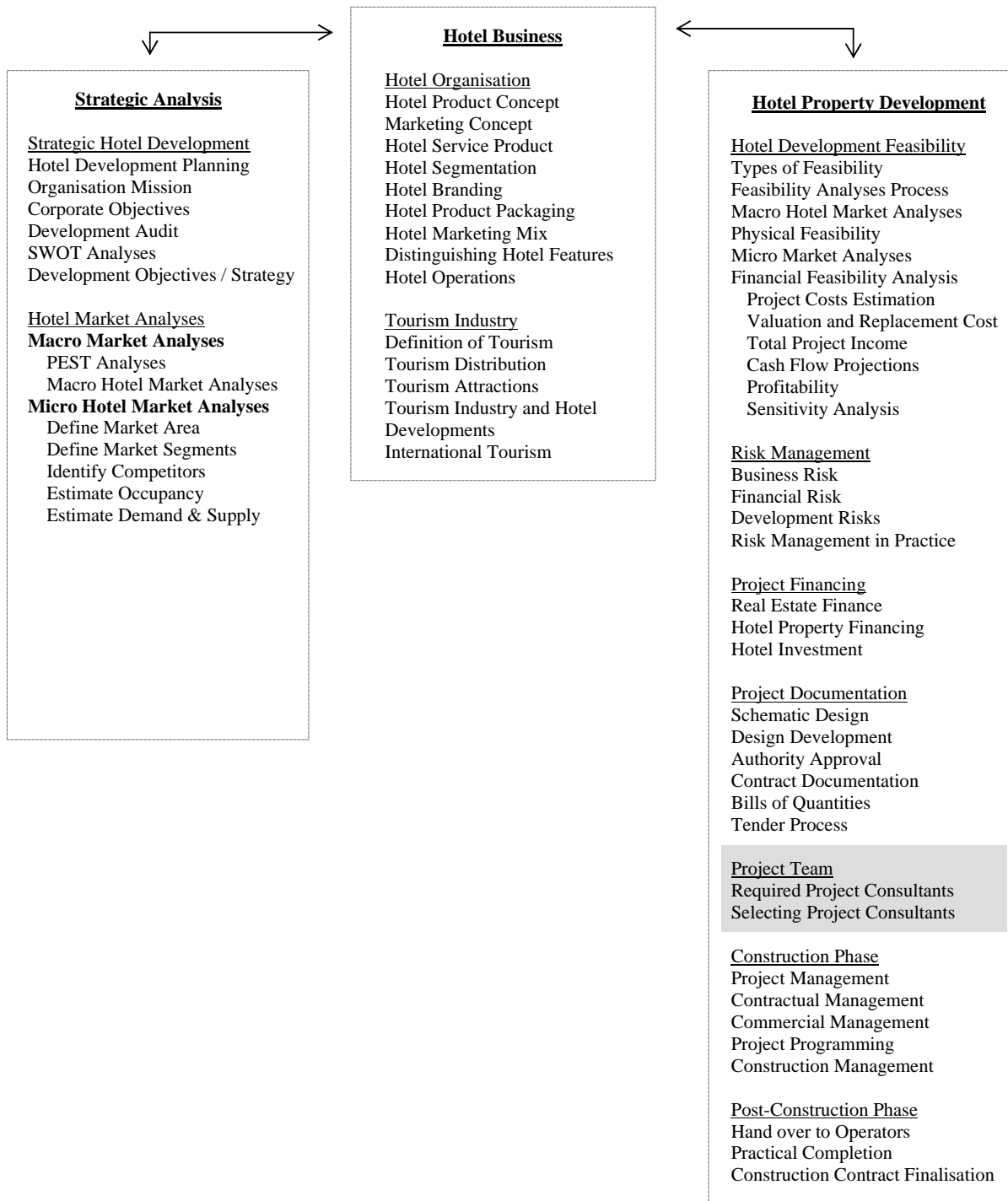
For lenders, explains Baltin et al (1999), debt service coverage generally is viewed as the most appropriate indication of a project's ability to secure debt financing. Lenders typically use the project's first stabilised year of cash flow (the third year for most hotel projects and the fifth year for most resort projects) as a basis. Cash flow in this context means cash available after all operating expenses, property taxes, insurance, and reserves for replacement are deducted. *"Today, acceptable coverage ratios range from 1.1 to 1.8, with most lenders preferring a 1.4 to 1.5 debt coverage. In the opinion of most lenders, hotels present more risk than do office or retail projects, which generally have more stable cash flows. Lenders also look at the size of the loan relative to the project's value. As a rule, lenders cannot make loans that exceed the property's appraised real estate value, lenders want developers to share in the development risk. Therefore, they look at a developer's equity commitment when they evaluate a loan package"* Baltin et al (1999: 60).

Some lenders, developers, and investors use other evaluative criteria that guide them to an expected return on investment, such as cash-on-cash return, the payback period, net present value, or return on equity.

The primary data that analysts require to evaluate a project's return on investment include an estimate of the overall development cost; an estimate of the productive life of the project, or the hypothetical date of a "forced" sale, and income and cash flow projections.

**Chapter 12:**

**The Project Team**



## 12 Project Team

*“Given a hotel property’s dual nature as real estate and a business, a developer should secure the advice of [property development] professionals who are familiar with the lodging industry” (Baltin et al, 1999, 31).*

The development of large-scale hotel or resort projects generally requires a wide range of professional skills and experience, which could be provided by specialists employed by the hotel property developer, hotel group or independent professional consultants (Lawson, 1997).

On the client side, says Baltin et al (1999: 86), a hotel project requires a leader, perhaps even a driver. This person(s)/organisation is usually the developer. *“A principal of a development company might have the vision, energy, and drive to undertake a hotel project. In other cases, the leader could be a principal of an operating company that is developing a project in a prime location on its own or with a local development group. The developer/operator is the client of the project team and any specialty consultants. As such, the developer needs to be represented by a number of key players who will have to commit a significant portion of their time for three to four years to develop the project. The client’s lead representative should be an experienced, development-orientated person. The operator’s representative is typically a vice president of development or a senior member of the technical services department.”*

Baltin et al (1999) explains that on the consultant side, it is imperative to put together a cohesive team in which each member from the beginning of their involvement clearly understands and adheres to his or her responsibilities. The team is usually set up, managed and directed by the client, often with a project manager or a lead consultant in charge. Previously the lead consultant was the architect, but is lately replaced by a project or construction manager. The project management functions include responsibilities such as scheduling, managing and directing the work of the other consultants.

### 12.1 Project Consultants

Normally, explains Baltin et al (1999), a core team of about six professionals are appointed to help guide the overall development process. The appointment usually includes an architect, an interior designer, a market and financial consultant, an attorney or legal consultant, and other consultants depending on the nature of the project.

In addition to these professionals/consultants, Baltin et al (1999: 31) believes that: *“...for most hotel projects, it is important to obtain the services of a professional development adviser during the development-planning phase. On complex projects, having such an adviser on board early is particularly important.”*

Depending on the type of hotel project, location, branding and complexity, most if not all of the following consultants could be appointed (Ransley and Ingram, 2000: 113):

- Architect
- Interior Designer
- Quantity Surveyor or Cost Estimator
- Structural Engineer

- Mechanical and Electrical Services Engineers
- Planning Supervisor
- Planning Consultant
- Landscape Architect
- Historic Building Consultant
- Kitchen Planner and Food Services Consultant
- Traffic Engineer
- Archaeologist
- Botanist
- Project Manager
- Environmental Engineer/Consultant
- Acoustic Engineer
- Procurement Specialist.

Other types of consultants, define Baltin et al (1999: 32), which may be required to work with the core team include:

- Marine Consultant/Engineer
- Government Relations Adviser
- Marketing Consultant
- Management Adviser
- Land Planner
- Soil Engineer
- Fire/Life-Safety Engineer
- Financial Adviser
- Public Finance Adviser
- Appraiser
- Accountant
- Tax adviser.

Many of the professional services overlap and are interdependent. A structured arrangement of main and secondary responsibilities is necessary to ensure (Lawson, 1997):

- Coverage of all requirements without duplication
- Contractual assignment of responsibilities
- Establishment of channels for communication
- Management and coordination to control quality, costs and time.

#### **12.1.1 Hotel Development Consultant (Adviser)**

The responsibilities of a hotel development adviser depend on the project sophistication and hotel development experience of the project initiator.

The duties of this individual or firm include some or all of the following (Baltin et al, 1999: 31):

- Identify other potential members of the development team
- Coordinate the preparation of the development objectives
- Liase with other parties involved in the development process

- Set a timetable for market and feasibility analyses
- Identify similar hotel projects that have been developed and study the lessons to be learned from them
- Establish regular contacts with hotel operators, developers, architects and other professionals in the hotel industry
- Establish the project's credibility within the financial community
- Advise the developer to proceed as quickly or as slowly as the project requires.

The development consultant/adviser cannot have a vested interest in obtaining future work from the project.

### **12.1.2 Architect**

*“The architect interprets, reviews and renders the concepts and specifications set forth by the developer, making sure that the proposed design fits the applicable state and local regulations. The architect usually assumes lead responsibility for the development team and coordinates the efforts of the design team”* (Baltin et al, 1999: 31).

Normally, the architect is responsible for the site planning, architectural design, production of technical drawings and the coordination of the prime consultants on a project. To execute this work effectively, an architectural firm appoints a principal-in-charge. Some firms appoint both a design principal and an administrative principal to oversee the project jointly.

The architect could assist the client when selecting the other members of the project team. All the consultants must understand the complexities of hotel layout, operations, servicing, and design.

### **12.1.3 Interior Designer**

*“The interior designer interprets the developer's concepts, plans and designs the interiors, and supervises their construction and installation. Generally, the architect and designer work together closely”* (Baltin et al, 1999: 31).

The selected interior designer firm for a hotel project is usually a specialist in hospitality design. Their responsibilities would extend from initial space planning to the detailed development of the interior design package, including floor, wall and ceiling finishes, fixed decor furnishings and decorations. The interior designer selects the furniture and fixtures (including the colours and materials) and prepares a specifications book from which the interior design elements can be priced and purchased. They may also be involved in purchasing the furniture and fixtures and overseeing their installation.

### **12.1.4 Landscape Architect**

The landscape architect plays a prominent role in the design of resort hotels and other projects that have large outside areas. He/she is also involved in the design of hardscape paving, furnishings and plantings for a variety of small but important outdoor spaces in urban hotels.

The landscape architect produces detailed drawings and specifications covering hardscape (walls, paving, benches, light fixtures), softscape (plants, shrubs, ground cover), decorative



fountains and fittings, pools, spas, other outdoor recreation facilities and irrigation. It is critical for the landscaping architect to work closely with engineers who are skilled in soil grading, drainage, irrigation, electrical supply and lighting on the design of these elements.

### **12.1.5 Quantity Surveyor**

The role of the quantity surveyor (QS) in hotel construction is to provide cost and procurement advice and cost management at all stages of a building project, from inception to completion. Ransley and Ingram (2000) explain that the QS is particularly concerned with identifying the client's specific requirements and anticipating changes to those requirements or other costly risks, that might affect the viability of an investment. By accurately forecasting and controlling construction costs, by managing the procurement of construction work and through the application of value-adding techniques such as value management, risk management and life cycle costing, quantity surveyors contribute to the optimisation of an investment, meeting the client's objectives and expectations in terms of cost, time and the quality of the development.

In order for the cost consultancy service to be effective, it is essential that the QS works as an integrated member of the project team and that the advice and input provided is positive rather than reactive. Clients benefit from strategic advice, tailored to their particular circumstances, rather than standard solutions.

The services provided by the quantity surveyor on behalf of the client include (Ransley & Ingram, 2000: 135):

- The production of initial estimates
- The development of the cost plan
- Contractor selection
- Contract administration
- Cost and progress reporting
- The agreement of the outturn construction cost of the project.

At the earliest feasibility stage the QS is able to provide an initial estimate, which is essentially budget costings in advance of the completion of detailed design work. These initial estimates are prepared using professional judgement based on costs derived from similar projects, adjusted for location, current price levels, quality levels and other cost drivers affecting the current project. For hotel developments the QS will prepare the initial estimate based on costs related to functional units, such as guestrooms, or costs based on a unit of total floor area. From project inception, the QS will also be able to advise the client on an appropriate procurement strategy and will provide costings and cash flows to support the client's project appraisal.

As a scheme is developed, the QS is able to review the design and produce an increasingly detailed and accurate estimate, known as a cost plan. The cost plan is prepared on the basis of measured quantities of cost-significant components of construction work. The purpose of a cost plan is to ensure that the scheme proposed by the design team is within the client's budget. The cost plan clearly illustrates where expenditure is focused, establishing a clear relationship between specification and cost. In doing so, it highlights areas of disproportionate expenditure and assists, if necessary, in the identification of areas of cost saving. In some instances, when the original budget is exceeded, the client may decide to

approve additional expenditure rather than compromise on quality standards established in the project brief.

The cost plan is a working document, continually reviewed by means of regular cost checks of the design team's proposals. As the design develops, the QS is increasingly able to base the cost plan on quotations from specialist contractors, as well as historic cost information taken from other projects. The accuracy of the cost plan at this stage will typically be within 5 per cent of the eventual contract price. Whilst producing the cost plan, the QS will also advise upon the cost implications of alternative forms of design and construction, and will monitor and report on the cost implications of the design as it develops.

#### **12.1.6 Engineers**

Various kinds of engineers are involved in the design, technical specification and documentation, and detailing of elements/components for a hotel development project. The primary engineering disciplines required are structural, mechanical, electrical and plumbing, and are often performed by a single multidisciplinary engineering firm (Baltin, 1999).

Structural engineers perform the calculations necessary for designing and sizing the foundations, columns, structural walls, floor framing and roof framing. They are involved throughout the design and construction process, coordinating their work with that of the other engineers.

The mechanical, electrical, and plumbing (MEP) engineers size, design and coordinate the layout of various important building elements. Baltin (1999) explains that these engineers must have a thorough understanding of a hotel's operational requirements and be cognisant of utility options in terms of sources, costs and availability. In some cases, engineers must design hotels to be self-sufficient in order to generate their own power, provide their own water through desalinisation or a well. The hotel's facilities and equipment should also be able to process and handle the generated sewage and refuse.

A soil engineer often works in conjunction with an engineering geologist, and is responsible for ascertaining the bearing capacities and properties of the soil and making recommendations to the structural engineer for the design of the building's foundations and superstructure. Investigation by a soil engineer is important in areas prone to seismic activity or having other complex soil conditions.

#### **12.1.7 Kitchen and Laundry Consultant**

Kitchen and laundry consultants work with the operator to create kitchen and laundry layouts that meet the operator's particular food and laundry philosophy and objectives. Food and laundry operations are extensive in large hotels with multiple food and beverage outlets, large banquet facilities and outdoor entertainment areas. Food service can be further complicated when it is offered in remote areas such as pool bars and grills, tennis clubs and other facilities away from the main building.

Kitchen and laundry consultants help design food delivery, preparation and storage areas. They also establish procedures for handling food service trash and garbage. They must coordinate their efforts with the MEP consultants who design the power, drainage and mechanical systems that feed/supply the kitchen and laundry equipment.

### 12.1.8 Market and Financial Consultant

The market and financial consultant is generally hired early on to ascertain how a proposed property might perform. A market consultant evaluates market conditions, determines general development parameters and prepares market projections. On the financial side, the consultant projects revenues and expenses and helps assemble the business plan (Baltin et al, 1999).

### 12.1.9 Legal Consultant

Legal advice, generally, is needed to establish the terms and structure of transactions, and to assist in regulatory matters such as writing contracts, obtaining titles, preparing documents, drawing up the management or franchise contracts, etc.

Legal consultants also deal with real estate tax, corporate and trademark issues.

## 12.2 Consultant Appointment Clarifications

Consultancy or employee appointments require a number of matters to be clarified at the time of engagement, as indicated in table 12.2(a).

**Table 12.2(a): Clarification Matters when Appointing Consultants or Employees**

(Source: Lawson, 1997: 93)

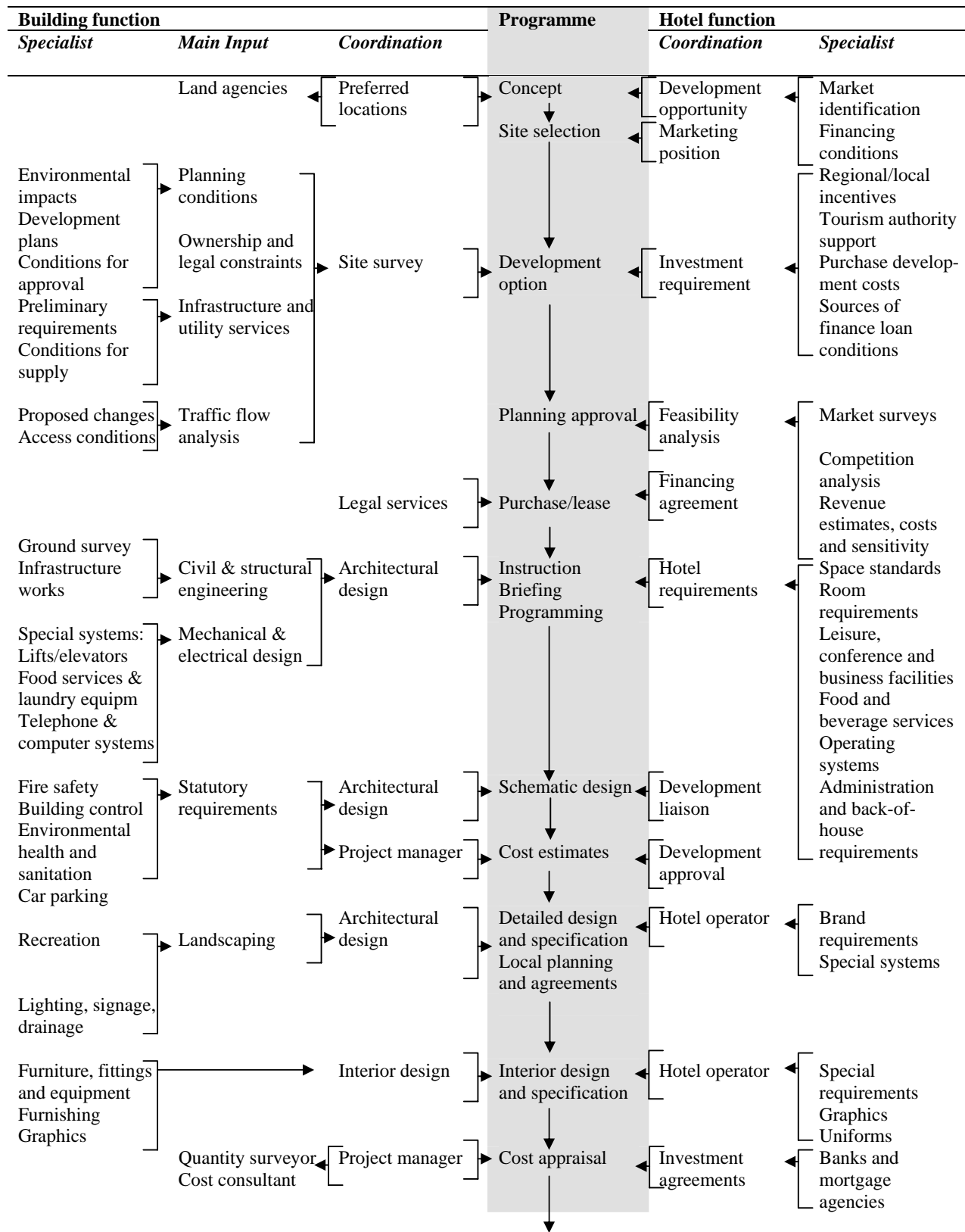
Aspect	Consideration
<b>Selection</b>	Background, experience, resources, local knowledge, reputation, personality, market conditions
<b>Arrangement</b>	Appointment, roles, duties and responsibilities, finance/budget, fee structure, payments
<b>Briefing/programming</b>	Method, meetings, records of decisions, circulation of documents, liaison with developers' representatives
<b>Organisation</b>	Coverage of tasks, resources needed, specific responsibilities, sub-contracting
<b>Timescales</b>	Work phases, key decision stages, critical timescales, work programme

### 12.3 Consultant Inputs

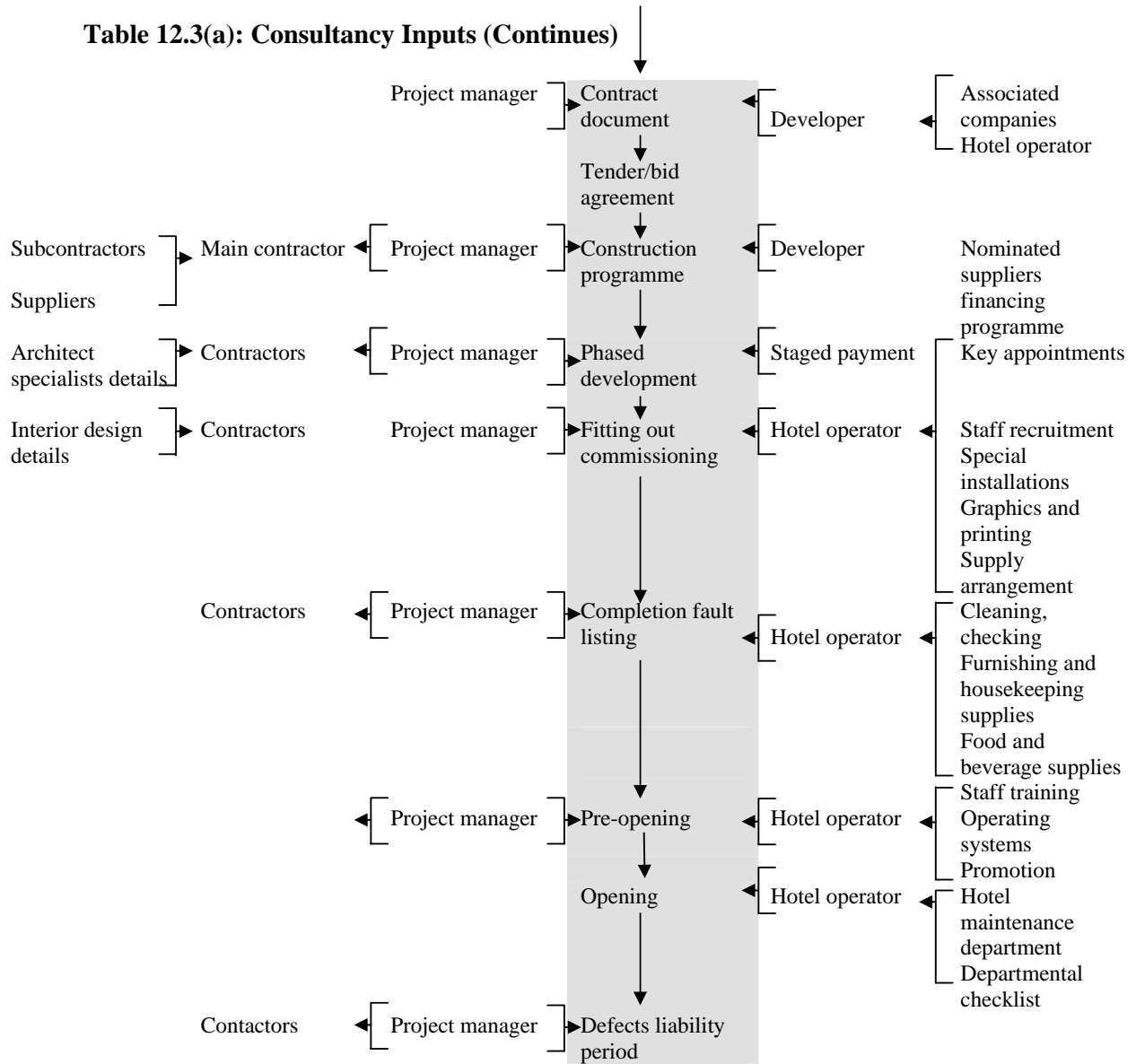
In an effort to explain the intricate relationship of all possible consultants involved in a hotel property development project, Lawson (1997) devised the Consultancy Input Diagram, illustrated in table 12.3(a).

**Table 12.3(a): Consultancy Inputs**

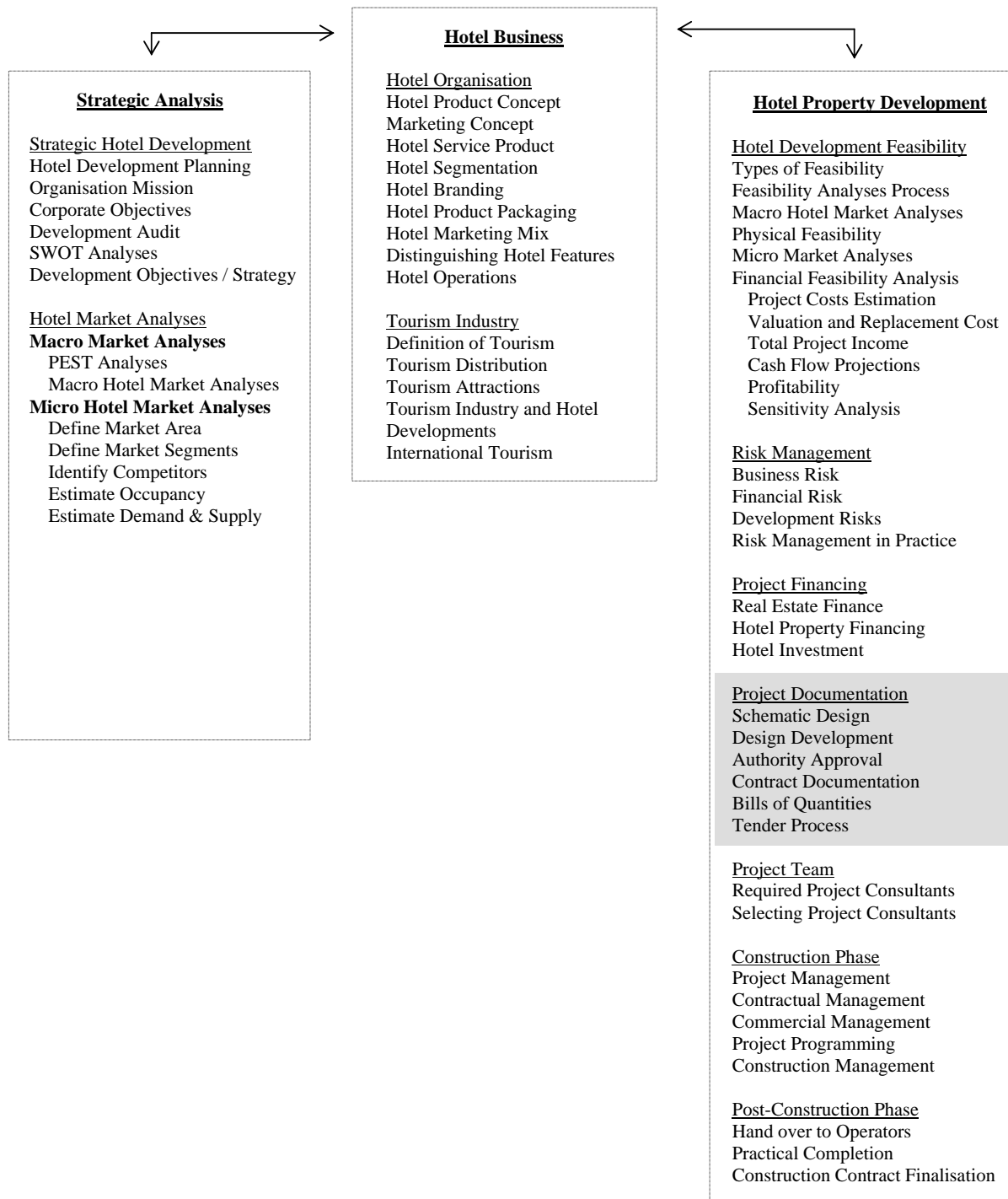
(Source: Lawson, 1997: 94)



**Table 12.3(a): Consultancy Inputs (Continues)**



## **Chapter 13: Hotel Design and Implementation**



### **13 Hotel Design and Implementation**

“[Hotel] design incorporates the planning, drawing and arrangement of properties, and the design process represents the operationalisation of a project from ideas to drawings and reality” (Ransley and Ingram, 2000: 6).

Ransley and Ingram (2000: 3) state that the final hotel product should be designed to meet the needs of the client and satisfy the consumer. *“A balance must be struck between factors such as image, style, operating efficiency and customer comfort, and between aesthetics and practicalities. The external design of hospitality [hotel] properties must be practical and appealing, while internal design aims to make the best use of the space available. The designer is responsible for planning the space available and for filling it with suitable furnishings and fittings, so that the flow of people and materials is facilitated. Design is affected by factors such as company policy, location, budgets and logistics, and a good designer needs to be aware of such considerations. The design of bedroom accommodation requires more attention to tangible factors than food and beverage facilities, where there is more of a requirement to create an environment in which to enjoy a meal experience.”*

Perhaps the most basic difficulty for an inexperienced hotel designer, cites Ransley and Ingram (2000: 3), is learning that hotel operations must earn a profit from the hotel building. A hotel operator is both selling rooms to the public on a daily basis and catering to the guests’ every need, therefore a hotel must provide a total living environment with all the required multi-complex functions and activities, rather than a mere rental space.

Hotel design may be regarded as a sequential process from concept to implementation. In this process the project design brief forms a key document and sets out to define the project objectives and parameters. Design proposals should be evaluated objectively, with special care taken in how the new product should be marketed. Hotel products, similar to any other product, must be carefully packaged so that they appeal to the consumer’s senses and add to their experience (Lawson, 1997).

#### **13.1 Role of the Designer**

The role of the designer in hotel property development is to provide a commercial design service. The design process’s commercial aims should be to maximise the capital investment and financial return of the owners, rather than to satisfy the designer’s artistic talent. Successful designs should please and satisfy the needs of the end user (hotel guest), because guest satisfaction/acceptance and repeat visits to a hotel will greatly assist in achieving the required financial return on the development investment. It is important that the designer and hotel client do not place their personal preferences above those of the customer (Ransley and Ingram, 2000).

Ransley and Ingram (2000: 6) elaborate on the design requirements and state that the responsibility of the designer is to establish a harmonious balance between the following factors:

- Image
- Style
- Operating efficiency
- Customer comfort.

Image and style communicates messages of an organisation, such as brand identity or quality. These intangible design considerations are in addition to the more tangible operational efficiency and customer comfort, commonly referred to as the operational design considerations. A new or adapted design should establish a hotel that can be operated efficiently by the staff and management, and consideration should be given to practical operational issues such as the flow of people, materials or information. An example is the design of a customer interface area such as a bar or reception, which should include space behind the counter for the storage of documents and should be able to accommodate the maximum number of staff required to serve customers at full capacity.

The designer is responsible for the following elements (Ransley & Ingram, 2000: 7)

- Space planning
- Form and colour
- Finishes and durability
- Lighting and audio-visual systems
- Technology.

In essence, the design incorporates all these elements, and the designer acts as the interface between the building form, structure, building services and the operational requirements in order to turn a concept into reality.

In summary, says Baltin et al (1999), a hotel design requires specialised design expertise and involves an array of design specialists that are seldom found on other types of commercial property designs. The project team systematically works through a process by which design concepts are transformed into solid reality, sensitive to the many site and market variables involved. This process involves a myriad of market and operational considerations that must be incorporated into a hotel's design.

### **13.2 The Project Design Brief**

The single most important item for the architect who is about to undertake a hotel project, is the client's project brief (or client's programme as it is often referred to in the USA). The project brief sets out the objectives for the project in clear measurable terms, including such fundamental parameters as the hotel segment being targeted (e.g. budget, 1<sup>st</sup> class, city centre, suburban, convention or resort hotel) and the amenities and services that are to be provided (Baltin et al, 1999).

Ransley and Ingram (2000) also highlight the importance of a project brief and state that it should define a project's objectives and parameters applicable to all the parties concerned, including owners, managers/operators and design team. The project brief should address the following key issues:

- *Objectives of the development:* What is required? (Refer to section 5.2 for an in-depth explanation).
- *Budget:* Spending limits and the required rate of return.
- *Time:* Desired start and finish date to maximise selling opportunities and minimise disruption.
- *Quality:* Standards and durability required from the development.



The client's project brief lists the size requirements for each area of the hotel. It describes the operator's philosophy, criteria and definitions of the levels of service it wishes to provide for the various operations, such as food service, laundry and valet service, housekeeping and staff facilities. (See addendum 'F' for an example of the size requirements in a project brief).

A project brief must include both fundamental matters and the required attributes:

1) Fundamentals

- a) *Objectives*: These should be sorted into priorities, for example costings, marketing, operational and maintenance issues.
- b) *Resources*: Budgets and content, timescale, planned life cycle, operational elements and staffing levels.
- c) *Context*: Scope, relevant legislation, technical facts, nature of site, building fabric and area specifications.
- d) *Planning*: Services, space relationships, function, operational methods and seating capacities.
- e) *Marketing*: Market segment, customer profile, spend per head and duration of stay, service standards, usage and entertainment.

2) Attributes

- a) *Realism*: Realistic in terms of objectives, resources, context, planning and quality.
- b) *Relevance*: Information related to the project only.
- c) *Flexibility*: Be specific enough for decisions to be taken and flexible enough to encourage the exploration of options.
- d) *Operation*: Define the organisation's standards, informed by the client's experiences of the durability of materials and running costs.

*"In defining the project, a tug-of-war can arise between the operator's criteria (its wish list) and the developer's budget or scope. Negotiations and discussions centering on the operational necessity versus the budget impact (additional costs involved and potential income generation) of disputed items normally resolve the differences, and the architect may be asked to help explore various alternatives for particular program items.*

*To work, the project definition must clearly communicate the owner's and operator's requirements, identify any particular constraints or restrictions imposed on the project by other parties, and establish a careful balance among all the complex parameters and factors that together make a hotel. The importance of this fundamental step cannot be overstated: poorly developed or incomplete programs invariably lead to major problems and projects that come in over budget and behind schedule"* (Baltin et al, 1999: 85).

The message conveyed by the project brief should be as clear, concise and briefly stated as possible. The length of the briefing document will be affected by the amount of detail about the constraints that are felt necessary by the developers, as well as the knowledge and ability of those charged with writing it.

The definition and communication of requirements is at the heart of a good brief. The success and value for money of a hotel development project depends on writing a good

brief. This is as crucial to the project as are foundations to a building. Good project briefs are characterised by the following (Ransley & Ingram, 2000: 13):

- *Logical structure:* As with any document, a clear structure aids readability and comprehension.
- *Presentation:* Should always be attractive and well-presented.
- *Consistency:* The brief should express consistent ideas.
- *Progressive:* Define the stages of development and the approval needed at each stage.

The project brief document must be revisited during the various design phases. It should serve as a benchmark, checklist and a tool for documenting and managing the project. It is quite common for some parameters and criteria to change as the project evolves and specific design, market and cost information becomes available. It is important to update and revise the project brief to reflect such changes.

### **13.3 The Components of Hotel Design**

Hotel design incorporates both interior and exterior elements, says Ransley and Ingram (2000).

The exterior presentation of a property includes signs, entrances, canopies, outdoor activities, terraces, patios, lawns and landscaping. It is the exterior presentation that gives the hospitality property a distinctive presence and offers the customer a first hint of what is on offer inside.

The aim of internal design is to optimally utilise the space available in the building, both for front and back-of-house activities. The internal facilities include accommodation, food and beverage areas, reception areas, leisure amenities, storage and services (for example, heating, air conditioning, gas, water, lighting, power and communications). Consideration must be given to the circulation pattern of customers and staff so that minimal disruption/congestion occurs. An important requirement when designing hotels is to ensure that the interior design does not present accident or fire hazards that may affect the safety of guests or other occupants.

The design of a hotel property is also a reflection of the operating standards of the unit and includes factors such as (Ransley & Ingram, 2000: 8):

- Capacity of bedrooms, public areas and food and beverage facilities
- Layouts of table groupings
- Anticipated product and service turnover, flexibility of accommodation and seating
- Method of food and drink service, staffing and support arrangements.

### **13.4 The Purpose of Design**

Effective hotel designs are those that are planned around a number of key criteria (Ransley & Ingram, 2000: 8):

- *Marketing:* Appeal to the target market by projecting the desired image and providing the required price and quality.
- *Ambience:* Create an attractive internal environment and conditions that support a suitable social atmosphere and service style.

- *Operations*: Meet the practical needs of serving guests efficiently and to the required standard.
- *Maintenance*: Fabric can be maintained to suitable standard easily and replacements available (e.g. rare foreign carpet, tiles, toilets).

### 13.5 Factors Affecting Design

A hospitality design concept can be affected by a number of factors (Ransley & Ingram, 2000: 9):

- *Company policy*: Product style, brand, future development strategy
- *Concept*: Objectives, market orientation
- *Location*: Type of premises, surroundings, constraints
- *Function*: Space usage, seating capacity, operational needs
- *Aesthetics*: Style, character, design features
- *Budget*: Investment criteria, payback, financing, resources
- *Business*: Planned life cycle, future changes
- *Logistics*: Critical dates, stages, contractors.

### 13.6 Factors Affecting Space

#### 13.6.1 Hotel Functions

Table 13.6.1(a) identifies relevant hotel functions to be considered for space requirement when designing a hotel.

**Table 13.6.1(a): Hotel Functions**

(Source: Lawson, 1997: 114)

Functions	Operational areas	Considerations
<b>Revenue Earning</b>	Guestrooms, suites	Major source of revenue. Main contributor to gross profits
	Food and beverage services	Usually major source of revenue, but incur high operating costs
	Minor related services	Telephones, business services, hire of meeting rooms, exhibit areas
	Rental charges	Shops, kiosks, representative offices and suites
	Casino, discotheque and entertainment facilities	Management/operating charges and commissions
<b>Cost Contribution</b>	Ancillary, buildings/serviced apartments	Service charges, food and beverage sales
	Club operations, spa facilities	Membership fees, admission charges, charges for individual treatments
	Staff accommodation, staff feeding	Deducted or allowed in setting employee wages/salaries
<b>Non-revenue earning</b>	Car parking	Enclosed parking - high-cost area, may utilise associated public car park
	Public areas - lobbies, lounges, libraries	Usually associated with revenue earning services (food, beverages, promotions)
	General recreation areas	May include charges for equipment, etc., hire and instruction

**Table 13.6.1(a): Hotel Functions (Continued)**

Functions	Operational areas	Considerations
<i>Administrative</i>	Front desk and administration offices	Including interviews and training areas, security and telephone, etc., services usually linked to business centres
<i>Operational support</i>	Food and beverage production and service Housekeeping and laundry Loading dock and storage Staff facilities - changing, dining and rest areas Mechanical and engineering, plant, workshops and stores	Rationalised by centralisation of production Laundry may be contracted out or off-site Location critical (access, noise, disturbance, garbage storage) Linked to staff entrance, supervision, personnel and training areas Plant may be located in basement, roof penthouse or/and intermediary service floors.

### 13.6.2 Variations in Space Requirements

The areas of built space required for hotel functions vary with (Lawson, 1997: 117):

- Hotel company standards
- Grade of hotel
- Specific facilities offered
- Location.

Hotel groups generally lay down space standards as part of their company policy to ensure consistent quality and to characterise their products.

The total area per guestroom will depend on the extent of public facilities offered. These are dictated by location and marketing requirements. The number of rooms compared to the total area is usually critical in ensuring feasibility of investment.

#### **Table 13.6.2(a): Space Considerations**

(Source: Lawson, 1997: 117)

Variations	Effects on space
Grade or standard	Overall space/room increases from 26m <sup>2</sup> (budget) to 76m <sup>2</sup> and over (deluxe hotels) Residential areas represent 80% or more in budget hotels, reducing to 75% in mid-grade and 71% or less in deluxe hotels
Proportion allocated to rooms	US chains tend to offer more generous bed sizes and larger rooms
Product differentiation	Resort hotels generally require larger areas per room
Relative cost of land	Affects the ratio of land: building area, massing and unit building costs Public facilities on multiple floors duplicate lobby and circulation space and require satellite food and beverage services
Specialist facilities	A higher percentage of public space is required for convention hotels, indoor leisure facilities, casinos, etc. The location of ballroom and convention halls (column-free) affects the positioning of guestroom floors
Building design	The proportion of space taken up by circulation and services to rooms varies with the shape and format of guestroom floor plans:

**Table 13.6.2(a): Space Considerations (Continued)**

Variations	Effects on space
	<i>Typical plans Gross factors</i>
	Slab building: central corridor (double loaded) 0.25 - 0.35
	Slab building: side corridor (single loaded) 0.35 - 0.40
	Atrium building, tower building 0.40 - 0.45
	Motels and holiday village resorts (without corridor access) 0.15
Back-of-house	Laundry and other services may be contracted out reducing total areas by 2 - 3%; zoned air-conditioning and other plant may be housed in the associated roof spaces
Basement car parking loading dock	Basement car parking addition to the built area of a high-grade hotel: 1 car space/room + 33% 0.3 car space/room + 11% A basement loading dock can add a further 3% with problems of increased headroom and ramping

### 13.6.3 Preliminary Estimates of Space

Initial allowances for planning may be based on typical areas for hotels of similar grade, as illustrated in table 13.6.3(a).

**Table 13.6.3(a): Size Range of European Hotels, 150 - 350 Rooms <sup>(a)</sup>**

(Source: Lawson, 1997: 118)

Grade	Economy (b)	Moderate	Average	High	Deluxe
Rating	*	**	***	**** (a)	***** (a)
Room area (net)	17.5 (c)	21.7	25.2	30.0 (+5%)	36.0 (+5%)
Gross factor (d)	0.25	0.25	0.30	0.40	0.40
Gross residential area	22	27	33	44	53
Public support areas (e)	5.5	8	12	18	22
Total area/room	27.5	35	45	62	75
Residential % of total	80%	77%	72%	71 %	71 %

**Notes:** Provisional figures rounded. In square metres. Room areas (plus 5% suites).

(a) Typical of European hotels: US comparisons below.

(b) Double bedrooms. Restaurant may be separate provision.

(c) Shower room may be used.

(d) Depends on building format. Allows for room service and greater variety of design for high-grade hotels including part single loaded corridors. Refers to gross internal areas. 0.10 - 0.15 for external access.

(e) Gross areas for non-specialist hotels.

### 13.6.4 American and Large International Hotel Chains

The concept of the compact economy-style hotel has not been widely developed in America (Lawson, 1997). Most USA and international hotel chains adopt larger room sizes to accommodate double or oversized twin beds with a mix of king and queen sized individual beds. The standard 3.65 metre room width is widely used although 4.1 metre or wider rooms may be used in first class and luxury hotels to allow design flexibility.

New USA hotels tend to be larger than those in Europe, permitting some economies-of-scale in public areas, giving a higher overall percentage of residential space per room.

**Table 13.6.4(a): Size Range of USA Hotels, 250 - 500 Rooms**

(Source: Lawson, 1997: 119)

Grade		Budget	Mid-price	First class	Luxury
Rating		**	***	****	*****
				(a)	(a)
Room area (net)	m2	21.9	29.0	32.5 (+5%)	37.2 (+5%)(b)
Gross factor (d)		0.25	0.35	0.40	0.45
Gross residential area	m2	27.9	39.0	47.8	56.6
Public/support areas	m2	7.0	13.0	18.6(c)	22.3
Total area/room	m2 (d)	34.8	52.0	66.4	78.9
Residential % of total		80%	75%	72%	72%

**Notes:** Provisional figures rounded.

(a) Typical range: First class.

(b) Plus nominal 5% suites.

(c) Depends on extent of convention facilities.

(d) Gross areas measured to outside faces of walls.

## 13.7 Design Considerations

### 13.7.1 Sensory Design Responses

*“Design is both functional and sensory. It has visual appeal and emotion through, for example, lighting, richness of colour, texture of furnishings. Mirrors, lighting and sound can transmit excitement and atmosphere in hospitality properties. It is necessary to design a room size and its proportion in relation to the purpose and the number of people who may use it. Public areas, for example, should give sensory clues as to the quality and prices of the services on offer and present a warm and inviting ambience. Warmth or coolness can be created using materials, textures and colours, and variations of light and shade can give the illusion of space and form. The extent and importance of these as design features will depend upon the market that is being targeted. Customers in the luxury market will expect greater aesthetics, and may be more appreciative (and perhaps critical) of items such as antiques and paintings, placed to create an atmosphere of sophisticated elegance”* (Ransley & Ingram, 2000: 10).

### 13.7.2 Aesthetics and Style

*“The atmosphere that can be created by design, including feelings such as calmness, sociability and intimacy, augments customers’ satisfaction with hospitality products and services. Mood can affect the way that an individual responds to an experience and mood can be affected by social and environmental conditions. Hospitality products are often consumed in social conditions, so that an individual might be more aware of others in a half-empty restaurant or bar, than in one which is crowded with people. Paradoxically, some hospitality units are all the more desirable for being crowded, and it is the job of the designer to help to create a balance between size and atmosphere. It is often style that distinguishes a property from those of competitors by branding or product differentiation. Branding style conveys information about product and prices, often through the creation of a theme, for example in McDonald’s or Travelodge. Themes are able to express mood (novelty, escapism), historical period, fashion or ethnic origin. There is also a trend towards cleaner, simpler, less fussy lines, which reflect contemporary lifestyle”* (Ransley & Ingram, 2000: 10).

### 13.7.3 Accommodation Design

Hotel accommodation should be designed with a specific and carefully analysed target market in mind (Ransley & Ingram, 2000). Hotel development analysts should clearly identify factors such as customer profile, price, length of stay, market characteristics (leisure/business) and modes of transport. This market profile will be reflected in the style, quality and service level of the hotel and will affect the configuration and space allocation. After identifying the targeted market profile, the number and type of rooms should be established (e.g. singles, twins, suites), and the space allocated to non-bedroom areas (front and back-of-house).

Because the design process is costly, many multi-unit branded operators such as Holiday Inn, Whitbread and Granada use standard patterns and materials, which saves time and money, and enables equipment, furniture and furnishings to be purchased in bulk. This form of standardisation can also minimise maintenance costs and help to create a corporate brand image (Ransley & Ingram, 2000).

Bedroom furniture is designed and chosen with the following considerations in mind (Ransley & Ingram, 2000: 11):

- *Comfort*: The hardness or softness of the bed is a major source of customer satisfaction - a good night's sleep.
- *Durability*: Beds and furniture must be sturdy enough to stand up to some abuse by guests.
- *Quietness*: Squeaky mattresses are a source of irritation to residents and those in adjoining rooms.
- *Interchangeability*: Able to be exchanged between rooms.
- *Safety*: New beds and furniture must conform to safety standards, and in many countries must be flame/fire resistant.
- *Storage*: Bedroom furniture must be able to be stored if, for example, the room is needed for meeting or seminar purposes.
- *Co-ordination*: A bed needs to be designed in conjunction with the bed covering and valance.
- *Mobility*: Furniture needs to be moved for cleaning and maintenance purposes and may be fitted with glides or castors.

Bedroom finishes include floor (carpet, linoleum, tiles), walls (painted, paper), woodwork, (painted) and ceilings. These elements should be designed to reflect the quality of the establishment and its budget. Room fittings should include electrical and shaver outlets, lighting circuits, and perhaps a control panel for the radio and messaging that may be linked to reception for morning calls. Rooms may also include a telephone, a television, air-conditioning and fire detection (heat or smoke alarms, water sprinklers). Bathroom fixtures include bath, shower, toilet, bidet and washbasin, as well as accessories such as toilet-roll holder, towel rail, shaving mirrors, soap tray and waste bin.

### 13.7.4 Food and Beverage Facilities Design

Contrary to the accommodation product being characterised mainly by tangible factors, the food and beverage facilities rely more on intangible factors to provide customer satisfaction

(Ransley & Ingram, 2000). Food or drink is often consumed with other customers, and satisfaction is subjectively judged by the quality of the product and the service provided.

Many restaurants display food to its best advantage so as to stimulate purchasing and dress their staff attractively in uniforms that are in keeping with the brand or image. Customers may participate in the process of selecting or even cooking food, for example, in carveries, buffets, barbecues or ‘Mongolian’-type restaurants.

Restaurants and bars are designed to accommodate/seat groupings of customers such as families or parties, and some restaurants entertain children in a play area. The type of food service style will, to a certain extent, determine the design and layout of the unit. For example, fast-food restaurants are designed around the systemised flow of people and food-counters, and often feature seats that do not encourage lingering, because the focus is more on volume sales than comfort. Luxury restaurants, on the other hand, charge considerably more for their products and offer more comfortable facilities, which encourage customers to dine at their leisure. Restaurants specialising in foods such as fish, steak, ethnic fare, sushi and pizza are often designed in keeping with the culinary theme.

### 13.8 Hotel Design Process

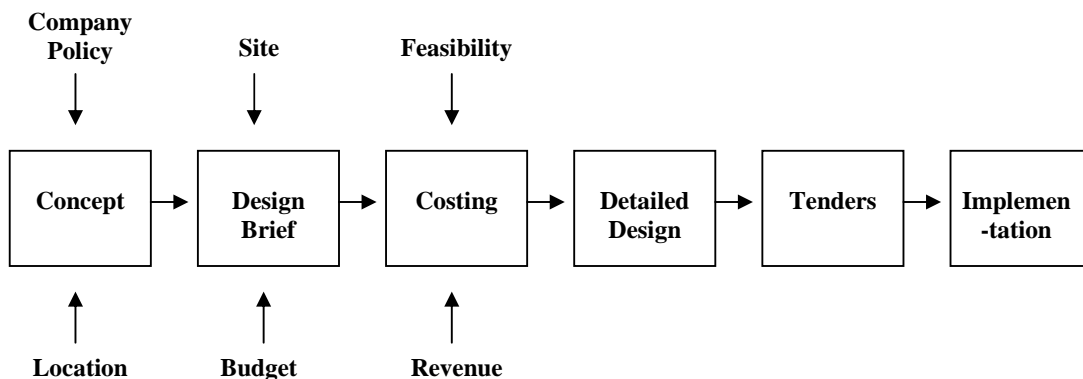
#### 13.8.1 Hotel Design Process Model

*“The design process [refer to illustration 13.7(a)] begins with a desire on the part of the property managers or owners to [establish or] change the tangible product. Initially, there will be some discussion within the organisation about what form this development should take and the approximate resources that might be allocated to fund it. At this stage, a designer would be appointed to explore the idea with the organisation and develop the idea for a new concept. A concept for the development of a hospitality property will be constrained by its location and any company policy on product branding.*

*The next stage is the development of a design brief that will be produced according to the characteristics of the site and within budget guidelines. Subsequently, the design can be costed and feasibility studies carried out as to the effects of the proposed change on revenue, costs and profit. If these meet the needs of the organisation, a detailed set of design specifications may be produced and tenders invited by contractors to implement the design” (Ransley & Ingram, 2000: 8).*

#### Illustration 13.7(a): A Model of the Hotel Design Process.

(Source: Ransley and Ingram, 2000: 9)





Most of the elements contained in illustration 13.7(a) have previously been comprehensively defined in this text. Please refer to sections 5.1.1, 5.2 and 6 for an explanation.

In addition to the concepts referred to in illustration 17.3(a), it is necessary to explain the following:

### **13.8.2 Site Selection**

By the time architects or planners become involved in hotel projects, the client has usually selected the site. Sometimes the developer calls upon an architect or other applicable consultant to assist in the site selection process. These professionals can assess the physical attributes of a site and foresee how various conditions (planning restrictions, environmental considerations, topography, etc.) will influence the design of a hotel. Accessibility (travel modes, distance from airports, etc.), surrounding land uses and other locational criteria should be analysed. Findings can be expressed in a diagram showing the opportunities and constraints of each site (Baltin et al, 1999).

### **13.8.3 Master Planning**

Hotel and resort properties need long-term master plans setting out appropriate land uses, development criteria and phasing, writes Baltin et al (1999: 90). *“Good master plans integrate the various components of the development and establish workable relationships between them. They have a certain degree of flexibility designed into them, allowing the developer to make modifications in a prescribed fashion in response to changes in market demand or economic conditions.”*

Among the key planning issues that should be considered in developing a piece of property for a hotel or resort are the following (Baltin et al, 1999: 90):

- *Land Uses:* Allowed uses should be graphically represented on a land use plan.
- *Densities:* Specifying the amount of actual built-up area that is allowed on a piece of property, density guidelines can be used to restrict the height and bulk of buildings and define spaces between buildings and between different land uses.
- *View Corridors and Open Space:* A key factor in a resort is the spaces between developed parcels. Open-space buffers are necessary, as in the case of a golf course. View corridors opening on prominent features or vistas are essential. The planning for view corridors should take into consideration existing views from developed land and seek to minimise the impacts that the project will have on valued views. Open-space and view restrictions help maintain the character and quality of a resort and ensure that future development phases retain their value.
- *Environmental Sensitivity:* Environmental sensitivity extends beyond sensitivity to the site's natural features and ecology and the development's impact on local and regional natural systems, to include any areas of historic or archaeological interest, as well as the development's impact on indigenous cultures and nearby historic precincts. It is not unusual for governmental agencies to require extensive environmental impact reports. These reports must address a myriad of issues, including impacts on the local culture and economy as well as on the natural environment.

### 13.8.4 Site Design

Baltin et al (1999) explains that when designing a hotel, most architects and planners begin with site design. The graphic analysis of the project brief, applied on the actual site, seeks to determine the best location of the building(s) relative to various physical and other constraints. Vehicular and pedestrian circulation and location/positioning is important, to give the guests a sense of arrival. The location of service entries and separate service drives (if required) and the screening of service areas are other site design factors.

Depending on a hotel or resort property's size and value, the parking area can considerably influence the design approach to the project. On a large site, landscaped parking lots can be located near the hotel. In urban or suburban areas, where land may be limited or expensive, parking structures (above or below ground) may be the best solution. In mixed-use developments, which often include stores, offices, residences and a hotel, parking structures are sized according to the parking requirement for the various components.

### 13.8.5 Hotel Design

The great paradox in hotel design, according to Baltin et al (1999), is that while most hotels are generally the same programmatically, no two are alike. As an example, though oversimplified, it could be said that the majority of hotels in the mid-scale and upscale range contain almost all the same physical spaces, housing similar functions that have the same specific physical relationship to each other. Within this comparability, variables such as site constraints, the number of rooms, operator's requirements and quality differences can help define a hotel and establish its own character.

#### 13.8.5.1 Different Hotel Type Designs

*“Although the urban hotel and the resort hotel are nearly identical programmatically, they present two different design challenges. The typical urban property usually has a limited site area that requires a design focus on concerns such as traffic, access, setbacks and density. The architecture of the hotel, supported by exterior hardscape and interior design, is the hotel's dominant visual statement. The architectural challenge often is to create an icon in the cityscape (within a context of mass, scale, and form)”* (Baltin et al, 1999: 94).

In contrast to this, states Baltin et al (1999), the design challenge presented by a typical resort property is to establish and reinforce a sense of place within a cultural context. The landscape, architecture, and interior design are balanced elements, and the architecture of a resort hotel often forms the background for the landscaping. These elements should blend together to create the desired environment and ambiance.

The casino hotel has come to rival the resort property in terms of design. As with resort hotels, the design goal for most new casino hotels is to create a sense of place set within a themed environment. The recent introduction of entertainment areas in casino hotels has added an additional challenge to the design process and necessitates the inclusion of expert consultants in the design team.

For a hotel architect, the specific design challenges posed by urban mixed-use properties, are to accommodate the hotel's back-of-house requirements and hotel guest's security. In addition to these architectural challenges, the design of structural systems including vertical

transportation systems that can effectively serve multiple land uses, is a major concern in vertical mixed-use projects.

The basic programmatic components of luxury properties are similar to what is provided in other types of hotels. The distinguishing design difference is a high level of finish in luxury hotels.

Dedicated conference centres impose special requirements for the food and beverage areas. The meeting areas and meeting support systems in these facilities are often designed for dedicated use, in contrast to the more flexible arrangements that other hotels prefer.

The spa is another specialised hospitality property. The design parameters for spas vary significantly, depending on the spa's focus which could range from pampering to exercise, and from weight loss to medical evaluation and treatment.

### **13.8.5.2 Hotel Components**

Hotels generally consist of three major components, which are guestrooms, public areas (front-of-house), and administrative and support areas (back-of-house) (Baltin et al, 1999).

Each component presents its own design challenges, for example, guestrooms come in many varieties e.g. kings, double, junior suites, executive suites, presidential suites, villas, to name a few.

Important considerations when designing guestrooms are the associated component such as guest corridors, stairs and elevators and areas supplying guestroom services (such as housekeeping rooms, butlers' pantries, and vending rooms).

#### **13.8.5.2.1 Guestrooms**

*“Almost every hotel design project starts out with a fresh look at the guestrooms. The standard guestroom module becomes the basic building block for the project, whether it is a low-density resort hotel or a high-rise tower. Groupings of guestrooms form the guestroom floor.*

*The designers may have considerable flexibility in locating and interrelating guestrooms and in placing guestroom wings on the site. In projects at the lower end of the quality spectrum or in projects with tight budgets, design flexibility tends to be limited and guestroom wings are kept compact. In five-star [upscale] resort hotels, architects are freer to conceive guestroom wing layouts that might, for example, create courtyards, respond to dramatic views, or reduce the physical scale or mass of the building”* (Baltin et al, 1999: 95).

#### **13.8.5.2.2 Public Areas**

*“The layout of the public areas is usually the most challenging element of a hotel's design”* writes Baltin et al (1999: 95). Public areas should be interrelated with back-of-house areas and also be readily accessible from the main lobby and other public entry points. In high-rise hotels, service ducts and structural columns come down from the guestrooms through the base (or podium) of the building and need to be accommodated in the architectural design to achieve a satisfactory interrelationship between the public area's primary

circulation areas and support spaces. Many public areas (e.g. restaurants, meeting spaces and ballrooms) typically require a higher floor-to-ceiling height than the average guestroom floor. Arranging these large areas in the design, both vertically and horizontally with other hotel components, can be difficult.

The complicated interrelationships between the back-of-house support spaces and the various public areas (such as food and beverage outlets, meeting spaces, pools and health club) require careful analysis and planning. Care should be taken that the public and service staff circulation do not mix, and that guest traffic flow is clearly directed and understood to enable the hotel to meet its standard of service quality.

### **13.8.5.2.3 Administrative and Support Areas**

Back-of-house design is complex. Thorough consideration should be given to important design parameters such as safety and security, the smooth flow of supplies and materials into/through the hotel and the optimal circulation of staff through the hotel. Mechanical plant location is important and should be close to the kitchen, laundry, engineering workshops and maintenance offices (Baltin et al, 1999).

### **13.8.5.3 Special Features and Amenities**

Hotels, whether economy or upper-scale, offer a growing assortment of special features and amenities. These features, ranging from live entertainment to state-of-the-art video conferencing facilities, spas and fitness centres to business support services, all need to be incorporated into the design (Baltin et al, 1999).

Baltin et al (1999) asserts that guestroom layouts and fittings are changing in response to technology advances across a wide range of applications, such as energy-conserving lighting, water-saving bathroom fixtures, HVAC systems that provide more comfort (and are more efficient), personal entertainment centres, and wiring and connections for personal computers and fax machines.

Fitness centres are often included in hotels and resorts. Their designs are evolving in relation to the development of state-of-the-art equipment and the increasing popularity of such innovations as specialised treatment rooms and healthcare products.

A number of hotels provide care for guests' children. The design of hotel childcare facilities and amenities for older children are increasing in popularity, but still leaves room for improvement. Hotel facilities for children take many forms, including playgrounds, children's pools and youth activity centres. Guests accompanied by their teenage children can generate considerable amounts of revenue for a hotel. This type of customer group requires youth-orientated amenities, providing entertainment and opportunities for interaction independent from the parents. Activity centres for teens with video game machines, pool tables and ping-pong tables and big-screen music video amphitheatres are being incorporated into new hotels. Almost every hotel has some retail space, which can range from a small convenience shop in the lobby to extended shopping galleries. The scale and scope of a hotel's retail offering depends greatly on its size, type, location and the potential spending patterns of its guests. Shopping is a major leisure pastime and strategically located retail facilities provide entertainment for hotel guests. Retail space can contribute significantly to the revenue generation of a project, especially with array and frequency of branded outlets in shopping galleries at high-end hotels.

### **13.8.6 The Architectural Design Process**

Baltin et al (1999) defines six primary phases in the architectural design process, which also serve, as a framework for scheduling and coordinating the architectural and engineering work. The process comprises the conceptual design, schematic design, design development, construction document preparation, bidding or negotiation and construction administration phases.

The interior design process also progresses through six phases, namely planning, concept, design development (architectural information), contract documents (working drawings and specifications), bidding and negotiation, and implementation.

With the architectural and interior design processes proceeding simultaneously, careful planning and coordination of the design work is required. Owing to time and cost constraints, these two design phases frequently overlap, placing greater emphasis on the importance of effective coordination of the design team's work.

The following sections explain the phases of the architectural design process (Baltin et al, 1999):

#### **13.8.6.1 Conceptual Design**

During the conceptual design phase, the design team visits the site to collect data on its features, view planes and surrounding areas. This phase begins the design of the building according to approved parameters, which include the project programme and budget. Concept plans (single-line drawings) are prepared, addressing the functional relationships of the project components, and taking into consideration the site features and governmental planning and building requirements. Written descriptions of the building(s), interiors, and landscaping are prepared. Gross building areas by project brief are tabulated and compared with the original project brief.

#### **13.8.6.2 Schematic Design**

Once the client approves the concept, the design team prepares schematic design drawings to illustrate the scale and relationships of the components. In this phase, a definitive project brief is established, building areas are tabulated, the items that will be included in the specifications are outlined and a written description of the aesthetic character of the project is prepared for the use of a cost consultant in establishing the estimated construction costs.

During this phase, the landscape architect, the engineers, the interior designer, the kitchen/laundry and elevator consultants begin their work on the design of the building systems, grounds and interiors.

#### **13.8.6.3 Design Development**

Based on approved schematic design documents, the design team prepares design development documents to further fix and describe the project's form, size and basic materials. All the design consultants prepare drawings and documents that describe their own portion of the work. The documents are scaled to indicate the overall building

configuration in relation to the site and nearby buildings. Preliminary estimates of construction costs are completed.

#### **13.8.6.4 Construction Phase**

Based on approved design documents, the design team prepares detailed construction drawings, specifications and calculations. The team then assists the owner in obtaining bids or negotiated proposals and in awarding and preparing contracts for construction. Finally, the architect and other members of the design team provide administration of the construction contracts. They visit the site during appropriate stages of construction, and observe the construction work for design intent and quality of installation. The design team reviews shop drawings and material samples, and advises the owner. The amount of effort required from the design team during this phase can vary greatly depending on the complexity of the project and the capabilities of the client's development staff.

### **13.9 Project Implementation**

The critical elements to achieving any successful building project are time, cost and quality. Ransley and Ingram (2000) emphasise that these factors are even more important in hospitality projects, which can be complex, especially in major refurbishments where the unit is to remain open and trading.

*“The general perception in the design and construction industry is still that hospitality developments focus on quality in terms of space and decorative standards, and are not sensitive to overall cost. The reality is that hospitality projects are probably more sensitive to capital cost expenditure for their viability than any other form of building”* (Ransley & Ingram, 2000: 15).

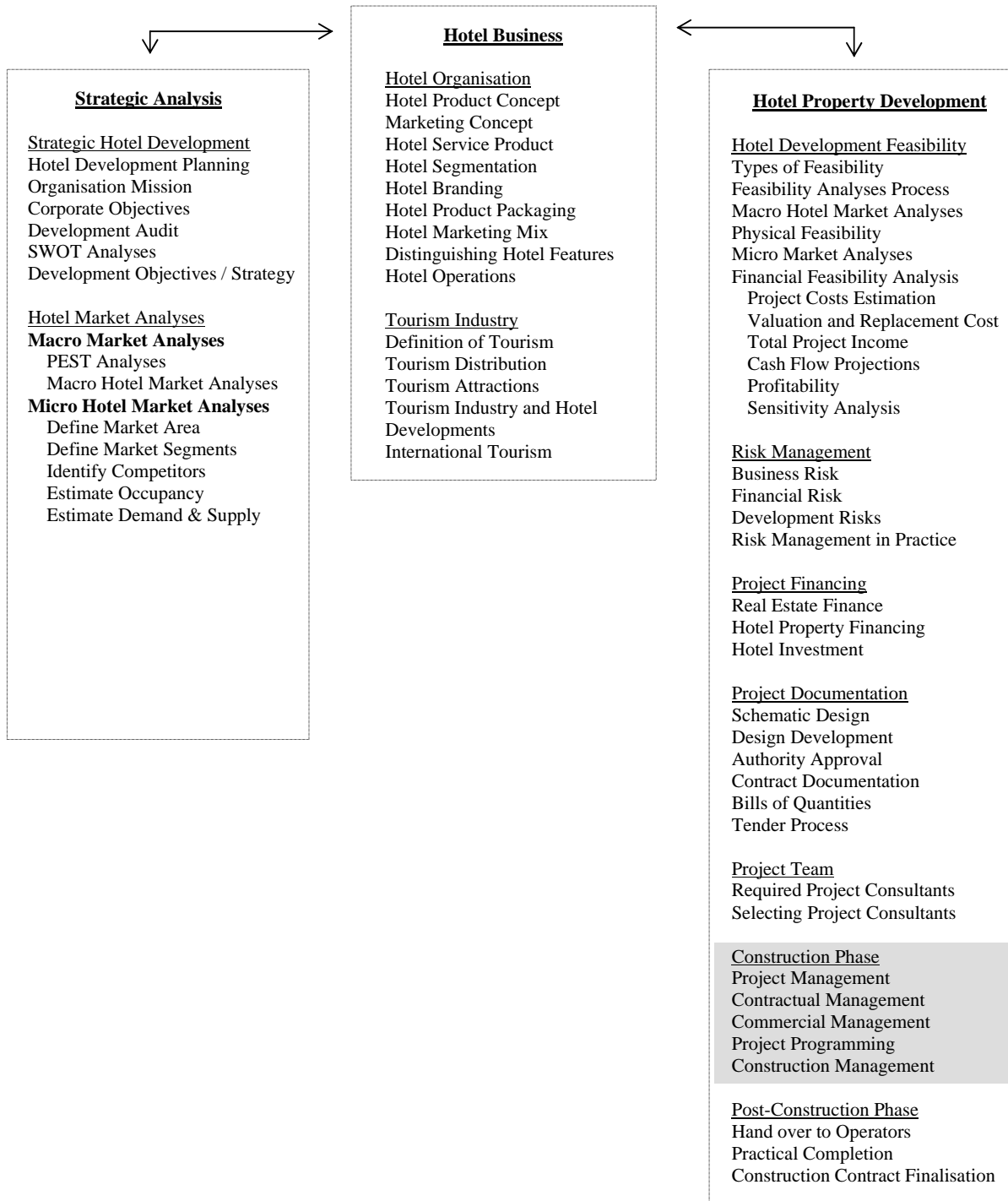
The relation between capital cost and return on investment driven by earnings and profit are direct and measurable. In turn this means that hotels must be planned to be functional, operationally efficient and to operate with minimum maintenance and running costs. In addition to these factors the hotel should be designed to provide guest comfort, appeal and be suited to service a specific market(s). This is equally applicable to budget and luxury hotels, resort or city hotels, branded or individual hotels.

Concerning the balance between project design and cost, Ransley and Ingram (2000: 15) cites that: *“...there is a saying in golf developments that new golf courses are developed by individuals with a passion who end up bankrupt before completion. The projects are then bought by enthusiasts who finish them but cannot get a return on their investment, and sell out to the mainstream operators at a realistic price who then make a handsome profit.*

*Generally, this analogy is applicable to the Western European hotel market, which has matured financially in a dramatic way over the last ten years.”* It is important for hotel development success to shed any emotional traits and develop sophisticated financial systems and controls to manage assets, similar to most major hotel owner companies and financiers.

**Chapter 14:**

**Hotel Construction**



## **14 Hotel Construction**

The purpose of this section is to introduce hotel operators and other hotel specialists to the process of construction, and to consider the client's role in the complex and demanding construction process on site.

*“As a complex mixed-use building type, hotels present significant challenges in both design and construction. Key issues in hotel construction today include the form of the construction contract, construction management and completion schedules, new technologies and post occupancy evaluation”* (Baltin et al (1999:101).

As the client will always be one of the two contractual parties to the building contract, according to Ransley and Ingram (2000), the selection and appointment (procurement) of the building contractor, is one of the key decisions he or she will be making on any project. Consideration of the criteria that influences, such a decision is essential when reviewing the options. It is imperative when making the selection, to accept that there is no perfect or ideal method, but the key is to find the best balance by having clearly defined objectives and priorities. The key considerations are:

- Time
- Cost
- Quality
- Flexibility
- Risk
- Responsibility.

Similar to other industries, social, commercial and technological advances could have an altering effect on the structure and methodology of construction. Construction companies have changed from being producers, to being providers of management and co-ordination service/skills, hence they no longer directly employ a workforce.

*“Consequentially, a number of alternative routes have evolved to facilitate the procurement of building work or construction process, and these fall broadly into two categories:*

- *‘Multipoint accountability’ whereby several individual organisations are separately responsible to the client for design and for construction.*
- *‘Single-point accountability’ whereby a single organisation is responsible to the client for all aspects of design and construction.*

*Whilst there is much ongoing debate about which process serves the client best, the evolution of new skills such as risk management and value management are encouraging greater collaboration between client, designers, managers of the building process and suppliers. Referred to as ‘partnering’, such methods encourage a life cycle approach to the design, construction and usage of the built form”* (Ransley & Ingram, 2000: 161’).

### **14.1 Construction Contract Options**

The form of the construction contract, explains Baltin et al (1999), has much to do with the construction quality, delivery time and cost of the final product. Three forms of construction contracts are used in the international hotel development arena, i.e. design-



award-build, fast track and design/build. Refer to table 14.1(a) for the comparative advantages and disadvantages, for the major parties, of these three construction contract forms.

#### **14.1.1 Design-Award-Build**

The design-award-build contract is the traditional building method. Despite the time it takes to first design and specify the building, design-award-build is still the best overall contracting option (Baltin et al, 1999). This building method puts the emphasis on instituting tight construction management procedures to avoid budget and schedule overruns. It begins with the design effort, establishing clear, complete and concise construction documents. Subsequent to completing the primary contract documentation, a competitive bidding process results in a guaranteed maximum price (GMP) contract, which should provide a high-quality project on time and within budget.

Ransley and Ingram (2000) introduce the construction industry by explaining that the origin of the designer-led contractor management approach (occasionally found today) was during the Industrial Revolution of the nineteenth century. This approach dominated the building process throughout the twentieth century. The appointed designer, or design team, normally with the architect as the lead consultant, having resolved a design solution to satisfy the client briefing requirements, draws up the necessary plans and specifications. Such documentation is then utilised to procure the appointment of the builder to carry out the work, to the instruction of the designer (contract administrator) under the terms of a building contract.

The traditional route strictly compartmentalises design and construction as separate activities. The resultant contractual aspects of this separation in the process are considered by many to be the reason why the construction industry has been dogged with problems. Simply put, the traditional route establishes design, defining the what (design), how and whom (detail and specification), and the builder utilises his or her workforce craft skills (quality) in the best sequential way (programme and time) to efficiently manage the process (time).

#### **14.1.2 Fast Track**

With a fast-track construction contract, the design effort is still underway when construction begins and it continues throughout the building process. Generally, for reasons of economics or availability, major decisions on structure, materials, mechanical systems and vertical circulation elements, are made early and imposed on the preliminary design as finalised (Baltin et al, 1999). As a result of these early decisions, items with long lead times can be ordered before the design is completed, accelerating the delivery duration. However, if items ordered in advance are cancelled or changed, the resultant commercial penalties could be extensive. Project managers (PM) or construction managers (CM) are often appointed to help coordinate the many subcontractors, design professionals and regulatory bodies required on a complex and fast-track hotel project.

An experienced project manager can shorten the construction period considerably, particularly if the PM is familiar with the components, systems or processes used on the project. The PM can be a valuable addition to the project team when fast-track is the construction method. Unless time is especially tight, fast-track is not the best contract option for high quality/finish hotel projects.

**Table 14.1(a): Comparative Advantages and Disadvantages of Construction Contracts**  
 (Source: Baltin et al, 1999: 102)

	Design-Award-Build	Fast-track	Design/Build
<i>For the Client</i>			
<i>Advantages</i>	<ul style="list-style-type: none"> <li>Professional advice on contract and construction quality issues</li> <li>Good industry understanding of how method operates</li> <li>Budgets most accurately resemble actual costs</li> <li>Easier guaranteed maximum price negotiations</li> <li>Clear penalties for cost overruns</li> </ul>	<ul style="list-style-type: none"> <li>Shorter project delivery time</li> <li>Lower project costs</li> <li>Professional advice on contract and construction quality issues</li> <li>Clearly defined sharing of cost overages and underages</li> </ul>	<ul style="list-style-type: none"> <li>Shorter project delivery time</li> <li>Lower project costs</li> <li>Single responsible party</li> <li>Inventive design/construction solutions</li> <li>Reduced project management stress</li> <li>Reduced number of claims</li> <li>Single fee to pay</li> </ul>
<i>Disadvantages</i>	<ul style="list-style-type: none"> <li>Longer start-to-finish time</li> <li>Multiple fees to pay</li> </ul>	<ul style="list-style-type: none"> <li>Project management stress</li> <li>Decision-making responsibilities blurred</li> </ul>	<ul style="list-style-type: none"> <li>No independent professional design advice</li> </ul>
<i>For the Contractor</i>			
<i>Advantages</i>	<ul style="list-style-type: none"> <li>Definitive plans and specifications on which to base bids</li> <li>Role clearly understood by all parties</li> </ul>	<ul style="list-style-type: none"> <li>Difficulty in establishing guaranteed maximum price</li> <li>Early completion bonuses</li> <li>Easier to recommend substitutions</li> </ul>	<ul style="list-style-type: none"> <li>More control over project</li> <li>Minimum risk and uncertainty</li> <li>Improved design</li> <li>Opportunity to increase profits</li> </ul>
<i>Disadvantages</i>	<ul style="list-style-type: none"> <li>Less flexibility for substitution of materials, equipment, and systems</li> <li>Adversarial relationships with design professionals</li> </ul>	<ul style="list-style-type: none"> <li>Coordination failures result in delay</li> <li>Penalties</li> <li>Gaps in insurance coverage</li> </ul>	<ul style="list-style-type: none"> <li>Responsibility for design errors and omissions</li> </ul>
<i>For the Designer</i>			
<i>Advantages</i>	<ul style="list-style-type: none"> <li>Greatest control over design and construction quality</li> <li>Role clearly understood by all parties</li> </ul>	<ul style="list-style-type: none"> <li>More involvement in the field</li> <li>Quick decisions by all parties</li> </ul>	<ul style="list-style-type: none"> <li>More control over project quality</li> <li>Opportunity to increase profits</li> <li>Field experience</li> <li>Greater credibility with clients</li> <li>Reduced number of claims from contractor</li> </ul>
<i>Disadvantages</i>	<ul style="list-style-type: none"> <li>Adversarial relationships with contractors</li> </ul>	<ul style="list-style-type: none"> <li>Decision-making responsibilities blurred</li> <li>Priorities blurred</li> <li>Timeliness more important than quality</li> <li>Coordination stress</li> </ul>	<ul style="list-style-type: none"> <li>Responsibility for errors and omissions of the contractor</li> </ul>

### 14.1.3 Design/Build

*“Design/build has evolved from efforts to reduce the delivery time of projects. It assigns the design and construction responsibilities to a single entity. This approach best serves projects in which the design needs and solutions are known, and the owner is comfortable with the contractor relationship. By using this option, the owner can often do without the services of an independent architect and, as well, without the services of a CM. The contractor is responsible for providing design services and for managing the construction process. Design/build does not function as well when the development objective is an innovative hotel product”* (Baltin et al, 1999: 101).

Baltin et al (1999) further explains that no matter whether the design/build or the fast-track option is chosen, all hotel construction contracts are moving towards negotiated guaranteed maximum prices based on completed plans and specifications. The design/build formula can consistently provide a high-quality hotel on time and within budget, if the developer obeys the following guidelines:

- Deliver complete contract documents before the bidding and construction phase.
- Keep fast-tracking to a minimum. Restrict its use to ordering certain equipment, like transformers and boilers, with long lead times, and then only if the order can be cancelled without significant penalty. Fast-tracking is risky since complete drawings are lacking at the time of contract.
- Base competitive bidding on equivalent quality.
- Make it a policy that no change orders will be accepted unless the owner initiated them.

### 14.2 Client's Role and Function

In a previous section the role and function of the hotel development adviser was defined as any individual providing advice, information or design services. Similarly, explain Ransley and Ingram (2000), a client of the construction industry, could be defined as someone who is responsible for commissioning and paying for building work.

*“Every building project involves at least two separate organisations but, more usually, in a hospitality development a multitude of specialists. For any project to succeed it is essential that the roles of each specialist are clearly defined and understood. Whereas the client can delegate tasks, it is in his or her interest to ensure the different parties understand their role and develop working relationships based on teamwork. Every project belongs to the client and to ensure it is successful he or she must retain control of it. This means considerable demands can be placed on the client organisation or individual and suitable internal resources should be allocated”* (Ransley & Ingram, 2000: 161).

Equally, there should be a single point of contact through whom all information and decisions are channelled. This single point party should clearly define the project objectives resulting in unambiguous communication, which should avoid confusion about instructions. In most hospitality companies the Technical Services or Development Department would normally undertake this role, but in other cases such as for hotel property developers, it would be advisable to appoint an external project manager or client's representative. It is imperative in all cases, that the client's representative should have direct access to the decision-making process, so that he or she could set the inevitable priorities and resolve any conflicting issues.

Ransley and Ingram (2000) further emphasise that once decisions are made they should be adhered to if delays and extra costs are to be avoided. These reasons all highlight the need to consult extensively within the client organisation during the brief compilation stage, thereby avoiding reactive change when works are in hand on site.

In the case of refurbishment projects, consultation with local management is imperative as any building project is disruptive not only to customers, but also to staff, and they will all be happier if they are consulted and kept informed.

Client representatives and advisers should always bear in mind that whilst they assist in proposing and administering the building contractual arrangements, it is the client that is the contractual party and obligated to comply with its conditions, including payment terms.

### **14.3 Management of the Construction Process**

Whether in-house resources or external agents such as a project manager manage a hotel development project, it is imperative that the client's contribution to the project is effectively managed and resourced.

It is imperative for hospitality projects that the briefing document is utilised as a benchmark reference at each stage of the design and construction development. This way, the objectives at the outset of the project can be maintained or change managed, in a deliberate and considered manner (Ransley & Ingram, 2000).

The client should maintain ownership of the project, and to ensure this he or she should follow the main steps of building project success (Ransley & Ingram, 2000: 165):

- Identify objectives
- Establish internal arrangements and resources
- Define priorities and benchmark references
- Establish a project brief
- Appoint advisers
- Liase with users
- Make decisions and accept risks
- Arrange funding
- Utilize appropriate form of contract
- Monitor progress and costs
- Review, analyse and collate post-project data.

The successful realisation of a hotel project begins with a well-organised control system (Baltin et al, 1999). Thus in addition to the main steps of building project success, detailed attention should be given to cost management, which is based upon the timely and prudent allocation of resources. Because of the complexity and financial risk of hotel development, decision makers constantly require updated and clearly understandable information about a project's status.

Effective control systems monitor not only costs but also performance levels. A good control system continually measures expenditures against budgets, and resultantly identifies variances that should alert decision makers to opportunities for corrective action. The first step in establishing an effective control system is to comprehensively plan the work well in advance of construction. Each component of the work must be reduced to a level of tasks

and subtasks that will allow adequate monitoring and control. The project manager should carefully plan the scope and priority of the various construction tasks. This planning should include activities from land acquisition through to post-occupancy evaluation. The work plan should highlight any special needs for labour, materials and equipment that will be utilised at any time during the complete project duration, from planning through to occupancy. Regulatory reviews, inspections and approvals should not be overlooked, as they take time, require resources and are compulsory.

The project programmes (work schedules) are prepared and administered by the project manager, and delineate the time durations for all activities and completion/delivery dates for all parties involved. The project manager must approve any variances in the programmes and is responsible for detecting any changes that could result in cost overruns or savings.

The project manager, according to Baltin et al (1999), also sets forth milestones or benchmarks (measurement points) in the programme. These measurement points are critical performance indicators for the owner and the contractor who uses them in scheduling, budgeting, and resource allocation.

With the work plan, project programme and milestones in place, project budgets can be finalised. Care must be taken to make the budget reasonable, attainable, and it should be based upon the contractually negotiated costs.

*“Constructing a hotel is a dynamic multidimensional event, not a statistical study. For the budget to serve its purpose as a baseline for the cost control system, cost control and cost analysis must be interlocked.”* Reserves and contingency funds are a key element in the control system if the project is large and complex. These reserves and contingencies could as a rule of thumb be 5 percent of budget or 10 percent of material cost, and should reflect the risks and complexities of the project. It should also receive the same level of thought and consideration as every other line item, says Baltin et al (1999:104).

*“The critical path method (CPM) is an increasingly popular tool in hotel project management. A CPM diagram clearly shows each step of the process, the amount of time each step requires, and its dependency upon the completion of other tasks. As the project moves forward, the allocation of performance bonuses or penalties at the completion of the project can be forecast by analysing the early or late start or the early or late finish of each task. CPM quickly resolves many disputes over which party is responsible for project delays and what, if any, penalties should be assessed, without protracted arguments. Successful use of CPM requires regular (at least monthly and preferably weekly) monitoring, evaluation, and maintenance of the CPM diagram”* (Baltin et al (1999: 104).

The completion dates for hotel projects are generally more critical than they are for other types of buildings. Hotels under construction book rooms in advance to guests and groups, and a delayed opening will not only result in loss of revenue, but also a more serious tarnishing of the hotel's reputation among travel agents, corporate groups and affected guests. In addition, staff payroll, training and other fixed pre-opening expenses must be carried through the period between the scheduled and actual opening. In an effort to motivate the parties constructing a hotel project and protect the hotel operator, many construction contracts include liquidated damage and bonus clauses to help ensure that opening dates are met.

Hotel projects involve complex completion schedules, because some key areas must be completed early to permit the installation of furnishings, equipment and training of hotel employees. Hotel construction programmes are generally divided into individual areas with varying handover dates, allowing for areas such as the kitchen, laundry, communications rooms, computer rooms, training room and loading dock to be handed over three months before opening. The guestroom floors and one elevator, reception area and front office are usually handed over approximately six weeks before opening (Baltin et al, 1999).

#### **14.4 Construction Completion and Operator Occupation**

*“Completing a building is always difficult, particularly so in the case of hospitality projects”* (Ransley & Ingram, 2000: 172). In this process several operational/finishing activities have to be coordinated and completed simultaneously with the installations, testing and commissioning of services such as air-conditioning, sound systems, theatrical lighting, computer networks, etc.

Before the operator can take occupation of the hotel site/facilities, practical completion must be achieved, as it is an important contractual milestone, which marks the end of the contractor's possession of the site and hands over the responsibility to the client. This handover should only occur if the building is complete for all practical purposes.

It is rare for a building to be totally complete at handover, hence as mentioned above, one can arrange for areas to be handed over in a phased way. *“Such arrangements, whilst not ideal, can be beneficial to both parties, but they need to be managed carefully. Whether taking full or partial possession of the site, handover requires a schedule of incomplete items, which should be of a minor nature only, must be recorded and arrangements made for the contractor to deal with them within an agreed period. Reasonable access has to be provided for such remedial work to be done whilst the building is operational”* (Ransley & Ingram, 2000: 173).

Operating and maintenance manuals (O&M manuals) of all equipment should be provided to the operator at or shortly after handover/occupation, as well as ‘as-built’ drawings of the building, information on materials and components used, including their care and maintenance.

Prior to handover, the client should have considered the future care and maintenance of the building. This is usually managed by the newly appointed property/maintenance/facilities manager or independently contracted specialist firm. Whichever option is taken, it is important that this arrangement should be in place when the building is handed over.

After handover, the builder remains responsible for latent and patent defects for a specified period of time. This period is known as the ‘defects liability period’, wherein defects should be of a minor nature. Hotels are complex in their service requirements and seldom are afforded any running-in or other trials before accepting its first guests. For this reason it is advisable that a hotel first commences with a soft-opening period before paying guests are accepted. During the soft-opening period hotel guests are invited by the operator to utilise and test the hotel's product offering free of charge, whilst minor adjustments and running-in of services occur.

Upon the expiry of the defects period and satisfactory completion of any remedial work, the building is certified as complete.

**Section C**

**EMPIRICAL STUDY**

## **15 Empirical Study**

### **15.1 Introduction to the Empirical Study**

The aim of the empirical study is to explain, firstly the development and secondly the validation of the hotel property development frameworks.

The dissertation objectives were categorised as either primary or secondary objectives. The secondary objective established the foundation from which the primary objective drew factors and components.

The secondary objective was to establish the critical success factors for hotel development, which were identified by addressing the following questions:

- What is a hotel and hotel business?
- What are the constituent parts a hotel business?
- What is hotel property development?
- What is included in the scope of hotel property development?
- What are the criteria for a successful hotel development?

The primary objective of the study was to test the validity of the hotel property development framework, as defined in the following dissertation hypothesis:

*“Does the hotel property development frameworks, proposed in this dissertation called **Hotel Property Development: A Framework For Successful Developments**, establish a practical and comprehensive property development framework for developing successful hotels?”*

### **15.2 Critical Success Factors For Hotel Developments**

In the literature review answers are provided to the questions posed in 15.1. In addition, from the literature review the following critical success factor for hotel developments were identified:

- Operational strategic direction and market understanding.
- Branding and marketing.
- Operational management and staff – skills, training and experience.
- Operational and construction standards – education, implementation and consistency of standards.
- National and local government regulations – taxes, duties, policies, legislation, town planning and building regulations.
- Site location.
- Accessibility – for guests, staff and suppliers.
- Feasibility – financial, market, physical, macro environment.
- Design efficiency – meeting budget, operational efficiency, and guest satisfaction.
- Development strategic and project objectives.
- Development team – team leader, executive management, key operational staff, consultants, and advisors.
- Contractor – cost, time, quality, experience, resources, capability, and attitude.



### **15.3 Establishing The Hotel Property Development Framework**

As mentioned in the dissertation preface, for all commercial and public organisations to be successful, they should comply with a mix of critical success factors unique to their environments. Similarly, hotel developments should subscribe to a mix of critical success factors, which should be incorporated during the development process.

From this statement the following questions arose:

- What are the tangible and intangible critical success factors for hotel development?
- How should these factors be combined?
- At what stages and junctures in the development process should the factors be introduced?

In addition to identifying the critical success factors for hotel development (listed in 15.2), they had to be combined in a sequence and at specific junctures to form a practical and definitive hotel property development framework.

In solution, two hotel property development frameworks were developed, firstly for hotel operators and secondly for hotel property developers. The Hotel Development Framework for a Hotel Operator is included in illustration 15(a), and the Hotel Development Framework for a Hotel Property Developer in illustration 15(b).

The development frameworks are broadly similar, but slightly adjusted to suit the different development viewpoints of either a hotel operator or a hotel property developer.

### **15.4 Hotel Development Framework Validation Process**

Subsequent to developing the hotel development frameworks, they had to be tested in practice to ascertain their application and validity. To achieve this end, questionnaires (refer to addendums 'F' and 'G') were formulated, to guide hotel operators or hotel property developers through the applicable frameworks, during an interviewing process which aimed to establish whether they agreed with the development frameworks postulated.

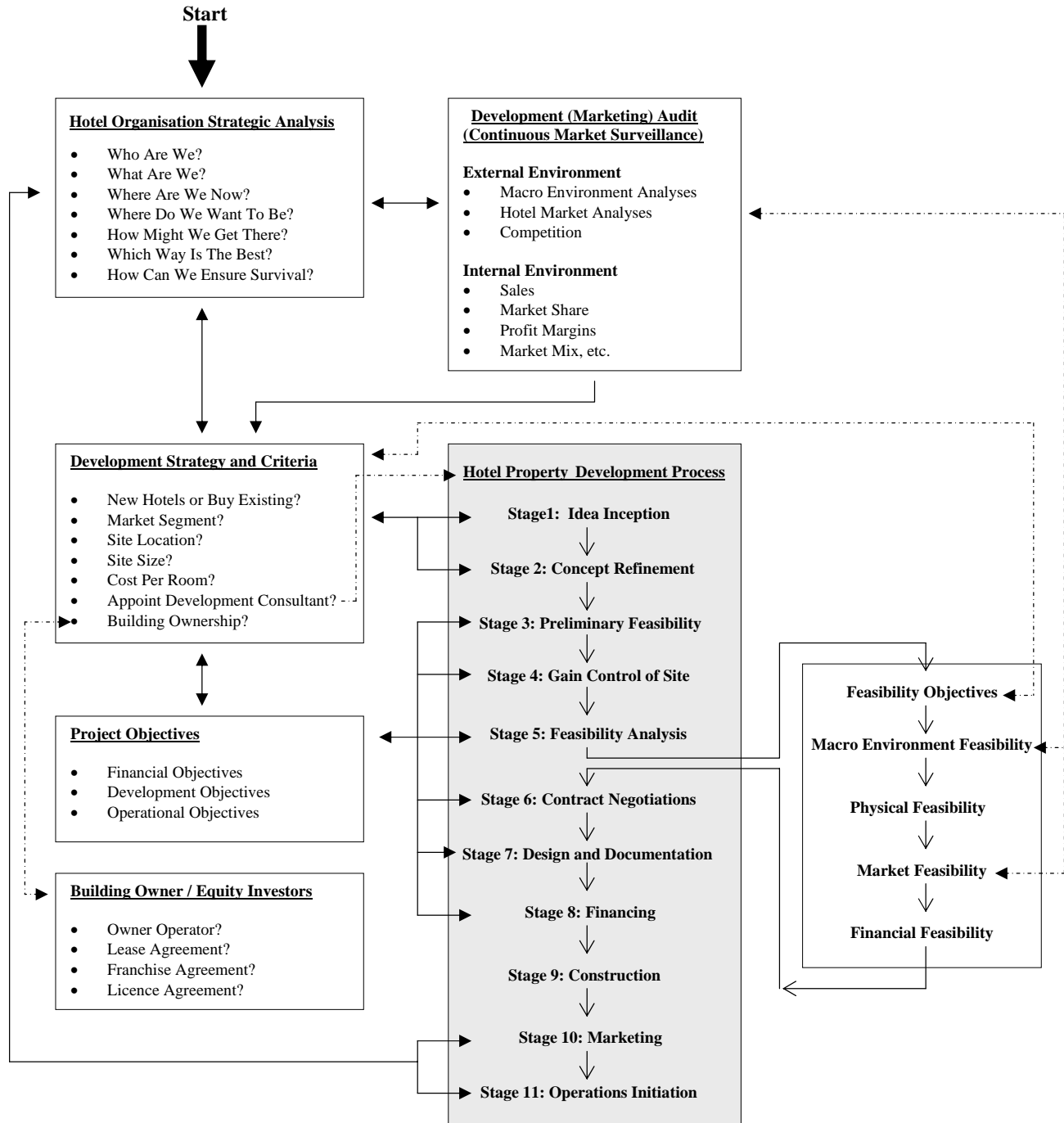
Due to the logistical requirements of intensive interviews, the interviewing candidates were limited to hotel operators and hotel property developers based in the Republic of South Africa, operating or developing properties within the southern African region.

In an effort to focus the empirical study interviews, only prominent hotel operators and developers were selected from:

- Advertisements in leisure magazines
- Advice from travel agencies and tour operators, and
- Guidance received from consultants such as Architects and Quantity Surveyors.

**Illustration 15(a): Hotel Development Framework for a Hotel Operator**

(Source: Culmination of views in the literature review)



**Illustration 15(b): Hotel Development Framework for a Hotel Property Developer**

(Source: Culmination of views in the literature review)



In the southern African region, lodging developments include game lodges, safari accommodation and a variety of outdoor adventure-type developments, in addition to the hotel scope as defined by Lawson (1996: 77):

- Suburban hotels
- City centre and downtown hotels
- Budget hotels
- Resort development
- Beach resort hotels
- Marinas
- Health resorts and spas
- Rural resorts and country hotels
- Mountain resorts
- Themed resorts
- All-suite hotels
- Condominium, time-share and residential developments
- Motels, motor hotels and motor courts
- Boarding houses, guesthouses, pension and pension de famille
- Bed and breakfast accommodation and hotels-garnis
- Holiday villages
- Condominiums
- Individual villas, apartments, suites and cottages.

A number of prominent hotel operators were identified and approached to partake in the dissertation empirical study, but only a few were willing to be interviewed and supply information pertaining to their hotel development process. The hotel operators interviewed were:

- Global Resorts & Casinos, represented by Mr. Jeff Forrer (Development Director)
- Legacy Hotels & Resorts, represented by Mr. Ian Shayler (Group Operations Director)
- Sun International, represented by Mr. James McGee (Manager of Developments)
- Southern Sun Hotels, represented by Mr. Keith Randall (Development Director)

Two hotel property developers were approached, but only one developer could at the time partake and furnish information regarding hotel property development. Due to the fact that only one hotel property developer, Kondotel (represented by Mr. Jan Kruger) was interviewed, the Hotel Development Framework for a Hotel Property Developer was not substantiated. Mr. Jan Kruger however supplied valuable hotel development information, which was included to substantiate the Hotel Development Framework for a Hotel Operator.

It should be noted that all of the hotel development managers contacted were extremely busy and had very little time to be interviewed about topics of lesser importance to their daily responsibilities. The only time most of them could afford was an hour interview, which was all time I had to introduce the dissertation and ask questions. In an effort to introduce the dissertation in advance of the actual interviewing session, I supplied the respective development managers with copies of the treatise, but again due to their limited time no preparation was done.

### **15.5 Empirical Study Research Methodology**

The dissertation research methodology could broadly be categorised as a content analysis type empirical study (Mouton, 2001), wherein secondary textual data was analysed, critical factors identified, which was in turn included in a visual and sequential framework that was validated in practice.

The empirical study research was conducted by means of intensive interviews with key hotel development managers of leading hotel operators and a single hotel property developer. The aim of the interviews was to test the validity of the hypothesis.

These intensive interviews were conducted on a personal (face-to-face) basis and were guided by the respective questionnaires, referred to before, developed as extensions of the Hotel Development Framework for a Hotel Operator and Hotel Development Framework for a Hotel Property Developer.

### **15.6 Research Interviewee Feedback**

In principle, all four hotel operators interviewed, confirmed that the process identified in the Hotel Development Framework for a Hotel Operator is correct and crucial in the process of establishing successful hotel developments.

It however transpired clearly, that the Hotel Development Framework for a Hotel Operator could not be applied in fixed or rigid manner, but would have to be adapted to suite the applicable scenario presented to develop a specific hotel property.

In practise, depending on project requirements and characteristics, some of the framework components are omitted purely because they are not required. An example, according to Shayler (2002) is the construction of the Ports Wood Hotel at Cape Town's Waterfront where hardly any market research was performed. Legacy Hotels & Resorts made the decision to construct the Ports Wood Hotels based on the fact that their adjacent Commodore Hotel's occupancy was averaging at 85%, which justified the construction of an additional hotel in close proximity.

In addition to omitting some stages when required, Randall (2002) and Forrer (2002) advised that some of the individually identified stages of the Hotel Development Framework for a Hotel Operator should be combined into one single step. An example mentioned is the development strategy process and project objectives process, which could be addressed as one stage.

Comment was also made about the depth of detail contained in the Hotel Development Framework for a Hotel Operator. Forrer (2002), Randall (2002) and Shayler (2002) confirmed that in practice, the hotel development process would seldom, if ever, contain the same depth of detail depicted in the hotel development framework.

It is important to highlight, as explained by Forrer (2002) and Randall (2002), that a typical hotel development process within the southern African context, will almost always be driven or initiated from an executive hotel operational point of view, as opposed to a property development perspective. This stands in contrast to USA or European literature included in section 'B' of the dissertation, where specialist hotel property developers often initiate new hotel developments.

**Section D**

**CONCLUSION**

## 16 Conclusion

Five South African hotel development professionals were intensively interviewed, wherein they confirmed that the Hotel Development Framework for a Hotel Operator, as postulated in the dissertation constitutes a practical and valid development framework.

In addition, the development professionals confirmed that the hotel development framework contains essential and critical hotel property development stages and success factors, required for a successful hotel development. Thus, it could be accepted that the dissertation hypothesis defined, is true and relevant.

The dissertation set the task to achieve two objectives – a primary and a secondary objective. The secondary objective established the foundation from which the primary objective drew factors and components.

The secondary objective was to establish the critical success factors for hotel development, which were identified by addressing the following questions:

- What is a hotel and hotel business?
- What are the constituent parts a hotel business?
- What is hotel property development?
- What is included in the scope of hotel property development?
- What are the criteria for a successful hotel development?

The primary objective of the study was to test the validity of the hotel property development framework, which included the following stages and components:

- Strategic analysis
- Development audit
- Development strategy and criteria
- Project objectives
- Hotel property development process, including macro environmental, market, physical and financial feasibility analyses.

Key points identified in researching the distinguishing success factors of hotel development were:

- 1 Hotel business combines three essential components – real estate, hotel operation, and FFE (furniture, fittings and equipment).
- 2 Hotel operation is in essence a service type business with an essential mix of tangible and intangible elements.
- 3 Hotel property development primarily deals with the tangible elements, but cannot successfully achieve its objective without a comprehensive understanding of the intangible service elements.
- 4 Hotel property development comprises 12 sequential phases.
- 5 Strategic hotel development forms an integral part of establishing a successful hotel.
- 6 Clear development criteria and project objectives must be defined and implemented.
- 7 Project feasibility comprises not only the financial considerations, but also macro environmental, physical, and market feasibilities.
- 8 Project financial feasibility comprises five primary considerations.
- 9 Total development cost includes five clearly defined cost categories.

- 10 The project team is critical to establishing a successful hotel, hence selecting the correct member is crucial.
- 11 When appointing a Contractor to execute the work, serious consideration should be given to their capacity, experience, track-record, current work load, and then finally at their tender price, to successfully perform the work.

Hotel development success requirements could be summarised as a combination of marketing, economics, location, enterprise, professional team, planning and design, and construction factors.

### **16.1 Recommendations**

Hotel property development offers ample opportunity for further research. It is recommended that:

- Empirical study interviews should be expanded, locally and internationally, to include at least 20 interviewees.
- The critical success factors for hotel developments be tested in practice.
- An industry barometer for hotel success be established.



**Section E**

**ADDENDUMS**

**Addendum 'A'**

**World Tourism Organisation's Minimum Hotel Standards**

(Source: Lawson, p. 13, 1997)

Amenity Description	1 Star	2 Star	3 Star	4 Star	5 Star
<b>Physical Requirements</b>					
Size	Minimum of 10 rooms				
Entrance	Hotel must have a dedicated / independent entrance		Hotel restaurants must have their own external and internal entrances. Separate service entrance required.		
Staircases	Comply with local authority legal requirements		Separate service staircase		
Construction	Architecture, design, furniture and decoration should be reflecting the local style with a degree of sophistication increasing with categories.				
Furniture, Fittings & Equipment	Moderate cost construction, simple, durable equipment and furniture of standard design		Medium cost construction materials and fittings. Custom made furniture	High cost construction and fittings Custom made equipment and furniture	Top cost construction, fittings equipment and furniture. Individualised decor
Emergency Power Supply	Emergency light sources		Standby generator to supply basic lighting and power up to 24-hours	Standby generator to supply energy for lighting, lifts, water treatment, cooking, refrigeration and heating	
Heating & Cooling	Heating or fan cooling when necessary	1 star + central heating and comfort cooling seasonally available	1 & 2 star + individual heat control in bedrooms. Temperature maintained between 18 and 25 Celsius	1-3 star + individual air conditioning control in all rooms. High quality equipment with very low noise emission	
Elevators Available to Match Room Capacity	Where more than three floor levels	Where more that two floor levels		When more than one floor level	
Service Elevator			Separate from main guest lifts		
In Room Communication	Call bell  One externally connected telephone per floor	Internal telephone only. Telephone available on request	Telephone connected through hotel switch board	Direct dial telephone to other rooms and national calls	Direct dial telephones for national and international calls. Telephone in the bathroom
Public telephones	Telephone available through reception	Telephone booth in the hotel lobby		Soundproof booths in lobby with national and international connections	
			Telephone available near all public rooms		

Amenity Description	1 Star	2 Star	3 Star	4 Star	16 5 Star
<b>Guest Bedroom</b>					
Bedroom Size	Adequate for free movement, comfort and safety. Minimum area in square metres (Excluding bathrooms and lobby)				
Single	8 m2	8 m2	10 m2	12 m2	13 m2
Double	10 m2	10 m2	12 m2	14 m2	16 m2
Triple	12 m2	12 m2	14 m2	16 m2	19 m2
Suites Size				Some suites available or connecting rooms to make temporary suites	Independent suites of various types and connecting rooms
Single bed minimum size	1900mm x 800mm			2000mm x 800mm	
Linen / towels	Bed linen changed with each new occupant, and twice a week		Towels changed with each new occupant and daily Bed linen changed daily		
Room cleaning	Daily			Additional room cleaning on request up to 12h00	24 hours additional room cleaning
Storage	Closet or wardrobe with hangers plus shelves or chest of drawers. Increasing with sophistication depending on category				
Seating	Minimum of one seat per guest		Minimum of one arm chair per guest		
Tables		One bedside table per guest Table in room	Writing / dressing table	Writing / dressing table with drawers	
Lighting	Natural light through windows during day. Artificial light at night adequate for reading. Ceiling light with switches at entrance and bedside. One bedside lamp per guest				
Floor covering	Suitable tiled or covered floors with bedside rugs or carpets where appropriate			Wall to wall carpeting or high quality flooring and floor covering	
In-room entertainment			Radio / central music system controlled by the guest TV available	Colour TV	Colour TV with video channel
Other room facilities	Window coverings to provide privacy and exclude light Waste basket. Ashtray (if not non-smoking rooms) At least one per person Written information on hotel services and procedures providing in one other language Do-not-disturb sign			High quality furnishings Local regulation may require display of tariffs	
		Fire safety instructions Luggage rack			

Amenity Description	1 Star	2 Star	3 Star	4 Star	5 Star
<b>Guest Bedroom (Continued)</b>					
		Mirror other than in the bathroom or at waste bin	Stationery	Mini fridge / mini bar	1-4 star + full length mirror
Soundproofing	Tolerable for day and night stay		Good to tolerable	High standard soundproofing	
Door	Lockable with individual keys or other means		Easily identifiable from outside (from the corridor). Internal security fastening		
<b>Bathrooms</b>					
Availability	Wash-basin with mirror, light, shelf, towels, soap and electric socket marked with voltage	1 star + at least 25% of rooms with private bathrooms	All rooms have private bathrooms		Spacious bathrooms Separate toilets
Size	Adequate for free, comfortable and safe movement				
Standard facilities	Natural or induced ventilation providing at least 3 air changes per hour Hot and running water. Colour coded taps Washbasin with mirror, light, shelf, towels, soap and electrical socket marked with voltage Water closet with toilet paper. Waste bin Shower cabinet or bath with showerhead and curtain or screen		Thermostatically controlled	Bath with showerhead minimum 1600mm long	Chilled drinking water Bath with showerhead minimum 1600mm long. Separate shower cubical
	Minimum of one hand and one bath towel per guest		Bath mats Shampoo provided	Cabinet for personal effects	Shampoo and other toiletries provided Hairdryer, telephone
Shared bathrooms (minimum)	One bathroom per five bedrooms sharing Two on each floor Equipped with shower cubicles or bath tubs, washbasin, mirrors, wc (unless separate) and standard facilities				
Shared water closets (minimum)	One wc per five bedrooms sharing Two on each floor (one for each sex) with washbasin and standard facilities				

Amenity Description	1 Star	2 Star	3 Star	4 Star	5 Star
<b>Public Areas</b>					
Public toilets	Separate for each sex. Normally each should have a minimum of two water closets with toilet paper, washbasins with hot and cold running water, mirror, soap, towels or/and hand dryers and waste bin. Separate cubicle for the disabled equipment with appropriate fittings. Suitably sited near public areas with interiors screened from view. Ventilation with at least 3 air changes per hour				
Corridors	Well lit 24-hours a day by natural and / or artificial light. Adequately ventilated. Free from obstacles or hazards. Suitably signposted with emergency exits clearly indicated.  Carpets, wall to wall carpeting or special floor finishes				
Reception area	Seating and appropriate furniture commensurate to hotel capacity. Well lit. Coffee and / or writing tables. Carpets, wall-to-wall carpeting or special floor finishes. Music / PA system				
Parking	Free access by car. Some reserved parking spaces	Parking space reserved for average number of car-using guests	Parking space reserved for average number of car-using guests	Exclusive parking or garage to accommodate all hotel guests and casual visitors 24-hours a day	4-star plus basic care serving available
Green areas				Some garden areas or terrace with plants	Green area for guests use such as terrace with plants, roof garden, patio or adjoining gardens
<b>Food and beverage, leisure and recreational facilities</b>					
Lounge	Area with lounge seating, music and / or TV service. May also be used for breakfast and reception of guests	Lounge area or sitting room with music and TV service, newspapers and / or magazines	Lounge area or sitting room as before seating at least one third of hotel capacity in combination with reception area	Choice of lounge(s) or sitting room(s) as before, plus service of drinks and refreshments	Choice of lounge(s) or sitting room(s) as before with 24-hour lounge service
Breakfast	As above or by service to room	Provided in hotel or facility in immediate proximity	Restaurant(s) provided within the hotel with adequate seating capacity for breakfast and other meals  Breakfast served 07h00 to 10h00		Breakfast 07h00 to 11h00
Room service	Option of self-catering facilities may be provided Breakfast served in rooms where no breakfast is available		Limited room service may be offered	Breakfast service including newspaper 24-hours beverage and light meal service	24-hours full meal and beverage service

Amenity Description	1 Star	2 Star	3 Star	4 Star	5 Star
<b>Food and beverage, leisure and recreational facilities (Continued)</b>					
Restaurants		Restaurant or cafeteria where meals are served at lunchtime and evening or in immediate proximity to appropriate independent facility	Restaurant or coffee shop where meals are served at lunchtime and evenings. Seating not less than hotel bed capacity	Main restaurant or choice of restaurants serving a variety of meals. Private dining or function rooms available Total seating not less than bed capacity of hotel  High quality food and beverage services	Highest standard of cuisine and service
Bar			Separate bar	Separate bar(s) and cocktail lounge	
Conference facilities				Meeting and conference rooms with appropriate conference facilities	
Cloakrooms			Cloakrooms and toilets near public rooms		
Entertainment				Music and public address system Night club, dancing area or discotheque available in hotel or near proximity	
Recreation				Sauna or swimming pool or health club or combination	Sauna, gymnasium / health club, swimming pool / jet pool
Hairdresser				Hairdresser / beauty salon	
<b>Services</b>					
Reception area	Reception desk manned throughout the day. Night bell Guest luggage handling on request		Permanent reception service. 24-hours check-in		Hall porter, luggage handling and doorman  Paging service / public address system
Medical services	Emergency medical / first aid service			First aid room	
Cashier service	Safety deposit	Credit cards accepted	Currency exchange service	24-hours currency exchange service	Individual safety deposit boxes

Amenity Description	1 Star	2 Star	3 Star	4 Star	5 Star
<b>Services (Continued)</b>					
Postal service	Service to include mail delivery and dispatching of postage stamps and stationery			Dispatch of facsimiles, electronic messaging	Business centre
Tourist and travel service	Local maps available on request	Tourist information available at reception. Booking tickets for local entertainment and cultural events	Tourist information service at reception	Travel agency / tourism service (tourism information, excursions, guiding, insurance, etc.)  Ticket and booking service for transport, hotels, entertainment and cultural events	
Tourist and travel service	Taxi on call			Taxi service  Hotel minibus available if isolated location	Taxi and car rental service Free hotel vehicles for isolated locations
Retail services			Sale of newspapers, books, postcards, tobacco, photographic supplies	Sale of cosmetics and souvenirs	Sale of cosmetics, souvenirs and flowers
Language service	Adequate knowledge by reception staff of one key international language		Working knowledge of two international languages by customer contact staff	Good knowledge of two key international languages by customer contact staff	Good knowledge of two key international languages by management positions and very good knowledge of three such languages by customer contact staff
<b>General Conditions</b>					
	Building, grounds, equipment, fittings and furniture maintained in clean, safe and sound condition, in good working order and free from defects which could impair use Public and guest areas cleaned at least daily, maintained in good decorative order and provided with clean furnishings in good sound condition. Attention given to defects with minimum of delay Full compliance with legal and licensing standards in respect of fire, means of escape and other precautions, hygiene, conditions for places of work and habitation, hotel insurance and other stipulated requirements			Exceptionally clean and in excellent decorative order and condition. Rapid response to any matter requiring attention	



## **Addendum 'B'**

### **Characteristics of Hotel Market Segments**

(Source: Lawson, p. 106, 1997)

Purpose and Main Categories Involved *	Typical Guest Profile **	Hotel Requirements ***
<i>Business</i>		
<b>Individuals</b> Sales representatives Company executives Consultants Government officials (Independent or through travel agent)	1-2 nights, 100% single occupancy 80% men and 20% women Non-seasonal Frequent travellers Price sensitive High average spend 1.3:1	High-grade hotels with good business services and meeting rooms. City centre or convention suburban location. Well-equipped guestrooms with large lounge, work area. 10% suites, room service
<b>Groups</b> Professional seminars Association conventions Sale force meetings Management conference (Independent or through conference organiser)	2-4 nights, 90% single occupancy 75% men and 25% women Weekdays Low mid-season Regular or periodic events Price sensitive Average spend 2.3:1	High-grade hotels with extensive conference and function facilities Well-furnished guestrooms with lounge, work area. 5-10% suites
<b>Management Training Sessions</b> Company orientation programmes (Usually independent)	3-6 nights, 100% single occupancy 65% men and 35% women Weekdays Low season Often part of ongoing programme Price sensitive	Mid-range hotel with good conference facility and seminar rooms. Standard guestrooms with lounge and working area
<b>Contract Business</b> Airline crew Tours Regular visitors	1-2 nights, 60% double occupancy Specific requirements Repeat business Discounted rates	Good standard hotels near airports, tourist areas, hospitals, institutions, universities, research parks
<i>Leisure (Pleasure)</i>		
<b>Mature Couples and Individuals</b> Tours Sightseeing Cultural interests Special promotions Weekend breaks (Independent or via travel agent)  Vacations (Tour organised or independent)	1-3 nights, 25% single occupancy High ratio women Weekdays Mid-season, 2-3 times per year Price sensitive to discount Moderate to high spending  7-10 nights, 20% single occupancy Mid and high season Annual Relative price sensitive Moderate to high spend	Mid-high grade hotels and guesthouses in mainly historic cities and country areas Well-furnished guestrooms  Mid-high grade hotels in attractive resorts and country areas Well-furnished spacious guestrooms with balconies

<b>Purpose and Main Categories Involved *</b>	<b>Typical Guest Profile **</b>	<b>Hotel Requirements ***</b>
<b>Mature Couples and Individuals (continued)</b> Retired Couples and Individuals (Tour organised)	7-14 nights plus 30% plus single occupancy Low-season packages Annual Highly price sensitive Low moderate spend	Mid-grade hotels in quiet resorts with range of amenities Well furnished spacious guestrooms with balconies
<b>Families</b> Vacation. (Tour organised vacations. Independent short stays)	7-14 nights in resorts High season, peak during school holidays One or twice a year Price sensitive Low-moderate spend	Mid-grade hotels in resorts. Holiday clubs Village resorts Guesthouses Self catering houses or flats and camping with rage of recreation and entertainment facilities Well-furnished, large family rooms or a combination of balcony or terrace
<b>Young Professionals</b> Singles and couples Vacations Clubs Associations Winter sports (Independent or tour organised)	6-12 nights, 70% single occupancy Mid-high season: summer and winter Often twice a year Price sensitivity depends on resorts attractions Moderate to high spenders	Mid-grade hotels or shared self-catering in recreation-based mountain or seaside resort, safari parks, etc. Standard rooms in hotels with sociable public facilities
<b>Young Singles</b> Vacation Tours sightseeing Exploration (Independent or tour organised)	1-3 nights when touring 7-14 nights when in resort High –mid season. Annual Highly price sensitive Low spend	Budget hotels, hostels or shared self-catering Basic rooms Shower and shared facilities
<b><i>Transient ****</i></b>		
<b>Couples and Individuals</b> Visits in area Events Stopover (Independent)	1-2 nights Mid-low season Weekends Often periodic Moderately price sensitive Low spend	Mid-grade chain hotels, motels or guesthouses in convenient locations with restaurant
<b>Families</b> Visit in area Stopovers (Independent)	1-2 nights High season Weekends Occasional Price sensitive Limited spend	Budget hotels, motels or guesthouses with large or linked family rooms and play areas for children Mainly bed and breakfast

Purpose and Main Categories Involved *	Typical Guest Profile **	Hotel Requirements ***
<i>Long-Term Residence</i>		
<b>Business</b> Employees in course of relocation Professionals working in area	Several weeks. All year Moderately price sensitive Moderate spend	Suites in hotels and associated self-catering villas and apartments with separate lounge / office area
<b>Pleasure</b> Retired Couples Retired Individuals	Several weeks – semi permanent Moderately price sensitive Low-moderate spend	Mainly self-catering apartments or villas, in condominiums or aparthotels

**Notes:**

- \* Main categories and reasons for visit. Couples include persons sharing rooms with twin beds. Mature couples: independent of children. Individuals include a wide range of ages.
- \*\* General description only with main periods of use. Price sensitivity-influencing choice of hotels but subject to corporate and group discounts. Average spend-total expenditure in hotels. Typical ratio compared with median for hotel guests. Exceptions not included.
- \*\*\* Hotel preferences and main facilities required. Excluding rented houses.
- \*\*\*\* Transient including day visits to friends, relatives, institutions and events. Stopovers in long journeys and at terminals.

## **Addendum 'C'**

### **Hotel Feasibility, Appraisal, Valuation or Market Study Data Collection Checklist**

(Source: Rushmore and Baum, p. 33, 2001)

### **Hotel Feasibility, Appraisal, Valuation or Market Study Data Collection Checklist**

The following checklist, from Rushmore and Baum (p.33, 2001), illustrates the specific types of data that might be accumulated in performing a hotel feasibility, appraisal, market study or valuation. The list is not all-inclusive but does indicate most of the major data hotel feasibility analysts and appraisers use. Some of the data listed may not be appropriate for all studies.

<b>Data Checklist Summary</b>
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#### **Primary Data Sources**

Client-supplied data  
In-house data  
Field data and key contacts

#### **Property-Specific Information**

Land  
Access  
Visibility  
Utilities  
Improvements

- General description and building layout
- Lobby and entrance
- Guest rooms
- Corridors and elevator lobbies
- Food, beverage, and room service facilities
- Housekeeping
- Kitchen
- Meeting and banquet facilities
- Amenities
- Back-of-house layout
- Building systems
  - Vertical transportation systems
  - Heating, ventilation, and air-conditioning (HVAC)
  - Energy management systems

Telephone  
Life safety systems  
Security and exterior lighting  
Miscellaneous

#### **Area-Specific Data**

Neighbourhood  
Assessed value and real estate and personal property taxes  
Zoning/building department  
Planning department  
Highway/transportation department

### **Economic and Demographic Data – Trends**

Chambers of commerce/economic development agencies  
Newspapers  
Demand generators list  
Airport authority  
Convention centre and visitor's bureau  
Car rental agencies  
Competitive hotels  
Rooms, bed, or occupancy tax  
Hotel associations  
Competitive restaurants and lounges  
Liquor licence laws  
Sales of competitive hotels

### **Other Sources of Data and Information**

Commercial real estate firms, boards, etc.  
Local appraisers, counsellors, bankers  
Photographs

<b>Detailed Explanation of Data Types</b>
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### **Primary Data Sources**

#### *Client-Supplied Data*

The client should supply the following types of data:

- Date of market study and valuation (and opening date if hotel is proposed).
- Interest appraised, i.e. fee simple, leasehold, leased fee, other value.
- Purpose of study.
- Balance sheets and profit and loss statements for past three years with supporting schedules. Financial statements should be prepared in accordance with the Uniform System of Accounts for Hotels.
- Development costs, including land, improvements, and furniture, fixtures, and equipment. Cost estimates are particularly important for proposed hotels.
- Monthly occupancy and average rate over two years. This data is most important for hotels with seasonal demand patterns.
- Copies or summaries of all leases, management contracts, franchise agreements, title reports, stock or partnership agreements, etc. Leases include ground, property, furniture, and equipment leases.
- Architectural plans, floor layouts as built, plot plans, survey and legal description. If a hotel is proposed, a detailed estimate of the project's cost is essential.
- Operating budgets and projections. The owner or operator will usually prepare these items.
- Marketing plans. The subject's competitive position and proposed marketing orientation should be evaluated.
- Engineering reports. Reports should show current conditions and any need for capital improvements.

- Capital expenditures over the past three years and capital budget (cost) projections. Past expenditures will indicate the need for future capital expenditures.
- Real and personal property tax bills, assessments of other hotels in the market area, name of legal owner. Assessments of comparable hotels in the market area can be used to verify the fairness of the subject's assessed value or to develop an assessed value if the subject is proposed.
- Past appraisals and market studies. Studying the work of others can save time, but all findings should be verified.
- Purchase price, date, terms, contract, and closing statement for subject property if sold within the past five years. A previous sale price of the subject property can indicate its value.
- Agreement of sale, option, or listing for subject property. Although such data is not strong indicator of value, it can provide useful information.
- Financing documents and mortgage and equity data. Such information forms a basis for developing a capitalisation rate if the data is recent.
- Union contracts. Contracts provide insight into labour rates and work rules. The appraiser should follow up to determine how effectively the unions control productivity.
- Franchise reports concerning occupancy, inspection, and reservations. Hotel franchise companies often provide owners with a wide variety of reports and surveys, including occupancy reports, inspection reports, and reservation reports. An occupancy report compares the occupancy and average rate of the subject with other hotels in the same franchise system; an inspection report records the results of periodic physical inspections made by the franchiser; and a reservation report documents the reservation activity generated by the franchiser's central reservation system. It sometimes includes a denial report, which indicates the number of guests turned away because the hotel was full. All franchise reports should be requested if the subject property is an existing, franchised hotel.
- Meeting planner's brochure and marketing packages. All property-specific descriptive information should be reviewed before starting fieldwork. Data can also be collected during inspection of the property.

### ***In-House Data***

In-house data is gathered before fieldwork begins. Sources of such data are described below.

- Reports on past appraisals performed in the market area. Prior work in the market area forms a base of information that will be updated and refined during fieldwork.
- Personal contacts. Reviewing personal contacts in the market area can help identify individuals who could be helpful in performing the assignment.
- American Hotel and Lodging Association construction report. This monthly report describes proposed hotel projects throughout the United States.
- Publications.
  - Official *Hotel and Resort Guide*, *Hotel Travel Index*, *Red Book*, *AAA Travel Guide*, *Mobil Travel Guide*, *Appraisal Institute Directory of Members*, and *Lodging Data Bank*. Various publications on hotel properties and hotel sales data as well as directories of real estate professionals can be helpful in performing a hotel market study and valuation.
  - *National Real Estate Investor* city data. This is a valuable source of general data on real estate activity in major markets.



- *Sales and Marketing Management* database and *Survey of Buying Power*. These publications are sources of economic and demographic data.
- *Restaurant Business Activity Index (RAI)* and *Restaurant Growth Index (RGI)*. Appraisers should consult these sources for restaurant supply and demand information.
- *FAA terminal forecasts*. These forecasts provide estimates of airline enplanements for most commercial airports in the United States.

### ***Field Data and Key Contacts***

Field data is typically gathered at the subject property and in the surrounding market area. The individuals listed below are primary sources of data and information pertaining to an existing subject property.

- General Manager
- Assistant/Resident Manager
- Director of Marketing
- Director of Sales
- Director of Engineering
- Front Desk Manager
- Controller/Accountant

Key contacts can provide introductions to other general managers and representatives of the local chamber of commerce, convention and visitors bureau, hotel association, etc. Hotel personnel can provide introductions to other data sources in the market area. Key contacts can also provide:

- A definition of primary market area in geographic terms. As a rule of thumb, a hotel market area is the area within 20 driving minutes of the subject property. Defining the market area tells the appraiser where to investigate both supply and demand.
- Demand generator analysis - industry type, location, map. When performing a demand generator analysis, appraisers should identify which attractions create local transient hotel demand, plot them on a map, and investigate major generators within the market area.
- A list of major businesses and industries in the market area. Appraisers should list businesses to quantify commercial and meeting demand and forecast future growth trends.
- Information about major users of the subject property. Listing the primary users of the hotel and determining whether any users receive special, discounted rates is useful for conducting demand interviews.
- Data on major contract business - term, rate, number of room nights. Contract business users such as airline crews typically rent rooms for a specific period of time at a set rate. Appraisers should understand the terms of any significant contract business.
- Competition analysis - competitive hotels, occupancy, average rate, and market segmentation.
- A marketing plan should contain detailed information about all the hotels that compete with the subject. This information is used to quantify area demand and determine the subject's relative competitiveness.
- Information about the mode of arrival and the transportation provided. What modes of transportation do guests use to travel to the subject property? This information shows

the importance of access and visibility and indicates the relative competitiveness of the subject.

- Market segmentation data. Appraisers should determine the types of travellers (e.g., commercial, meeting, leisure) as a percentage of the total usage and note any changes in the percentages that occur over the year. This information can be used to determine the suitability of the improvements and amenities and to project future hotel usage.
- An indication of the average length of stay. How long does the average guest stay at the subject property? Appraisers should identify this information by market segment.
- Specific points of origin - feeder markets. Where do the guests come from? Appraisers should identify this by market segment for both the subject and the market area.
- Details of seasonality - weekly, monthly, by segment. How does usage change over the year? Appraisers should identify this by market segment for both the subject and the market area.
- Quantification of non-accommodated demand by segment. Appraisers should quantify the amount of demand that cannot be accommodated because facilities are filled and identify both the subject property and the market area. This data is important if new supply enters the hotel market.
- Double occupancy percentage. Determining the average number of guests per room for each market segment affects the subject's room rates and usage.
- Indications of rate resistance, by segment. Which market segments display rate resistance and at what rate level does this begin? This information influences future rate increases.
- Rack rate strategy - usage of yield management. What type of yield management, or hotel pricing policy, does the subject use? How does it function? Appraisers should address these questions.
- Percentage of reservations from franchise. Appraisers should ascertain how effective the franchise identification is in generating room reservations. If the subject is proposed, the franchiser can sometimes provide estimates.
- Information about the amount of travel agent commissions. Appraisers should ask how much business is generated from travel agents.
- Information about unions. The number of hotels in the market area that are union operated affects the labour component of operating expenses.

### **Property-Specific Information**

#### ***Land***

- Description of the size, topography, and shape of the land. Data obtained from the plot plan or survey is important for evaluating access and visibility and the site's suitability for new improvements.
- Municipalities. Appraisers should determine the municipality in which the subject is located and identify other municipalities in the market area. This information is needed to research local economic, demographic, and municipal trends.
- Area or acreage. The site area found on the plot plan or survey determines the number of units for a proposed hotel and the amount of excess land for an existing hotel. Land value, which is calculated in the cost approach, is usually based on area.
- Excess land - saleability, highest and best use. If the subject site contains surplus land that could be used for expansion or another use, additional value may be present.
- Plot plan, survey. These documents are sources of land information.
- Frontages. Frontage determines access and visibility.

- Adjoining uses. Appraisers should inventory the land uses surrounding the subject property. Surrounding land uses can enhance or detract from the value of the subject property.
- Grade compared to surrounding roads, uses. Grade level can impact access, visibility, and development costs.
- Contours, slope, drainage. Topography affects development costs.
- Flood hazard insurance. If extra insurance is required, a hotel's fixed expenses increase.
- Soil tests - water table, percolation tests, flood zones, seismic activity, other engineering studies. These considerations can affect a proposed hotel's development costs.
- Air rights, subsurface rights, water rights. Additional rights often enhance a property's value.
- Landscaping. Landscaping can significantly influence a hotel's competitiveness.
- Easements, other restrictions. Restrictions can increase or decrease a property's value.

### *Access*

- North-south roads and east-west roads. Appraisers should list immediate and nearby roads and highways and investigate both the immediate and secondary access for all modes of transportation.
- Modes of transportation. Appraisers should determine how guests reach the subject property and consider that access may be accomplished by more than one mode of transportation.
- Direct access patterns. Appraisers should describe the access to the subject property by the primary modes of transportation and describe adjacent and nearby highways, including the number of lanes, medians, turn restrictions, traffic signals, one-way streets, curb cuts, and limited-access roads.
- Future access. Appraisers should consider how access is likely to change in the future.
- Distance to major facilities. Appraisers should calculate the distance in miles and time to highways and interchanges, airports, mass transportation, convention centres, major demand generators, and competitive lodging facilities.
- Competition. Appraisers should compare the subject's access to that of the competition.

### *Visibility*

- Evaluate visibility from nearby roadways. Appraisers should consider how long the subject is visible to drivers and their ability to exit the highway after the subject becomes visible.
- Visibility from nearby demand generators. Appraisers should see if the subject is visible from any demand generator.
- Visibility from nearby competitive hotels. Appraisers should see if the subject is visible from any competitive hotels.
- Building height and depth. Appraisers should ask how the subject's building height and depth affects visibility.
- Slope of land. Appraisers should know how the topography of the subject parcel affects visibility.
- Obstructions. Appraisers should evaluate all obstructions to visibility, both existing and proposed.
- Signage location, visibility, condition. Appraisers should describe the subject's signage and evaluate its visibility. They should also ask if it could be improved.

- Views from the subject's guest rooms, food and beverage outlets, etc. Appraisers should evaluate visibility during the day and night and consider how it is likely to change in the future.

### *Utilities*

- Location, capacity, and provider  
Appraisers should investigate the availability and cost of these utilities:
  - Electricity: local rates, normal demand charges, quantity discounts, seasonal adjustments
  - Natural gas: local rates, quantity discounts, seasonal adjustments
  - Oil: tank size, local prices, quantity discounts
  - Water: potable, hot and chilled
  - Steam
  - Telephone
  - Sewage
  - Liquefied petroleum gas (LPG), propane
  - Trash removal
  - Storm drainage
- Alternative sources  
If a utility is unavailable, appraisers should consider alternative sources. What will it cost to make it available?

### *Improvements*

The following portion of the checklist is concerned with the subject improvements. During the property inspection, the appraiser focuses on the physical and functional characteristics of the hotel, giving special attention to:

- Age and condition of improvements as well as furniture, fixtures, and equipment
- Immediate and future need for upgrading and renovation
- Physical attributes of the property compared to the competition - appraisers should evaluate the facilities offered and their condition, class, and desirability
- Functionality of the property's layout and design. Appraisers should find out what impact the design has on service, maintenance, labour expenses, and security
- Improvements' effects on future revenues, expenses, and profits.

### *General Description and Building Layout*

- Plans and physical description. Appraisers should obtain all necessary information from the property owner.
- Year opened
- Description and date of expansions and renovations
- Number of structures
- Location of buildings on site
- Number of storeys
- Building configuration - H, L, U, straight
- Total square footage
- Landscaping and sidewalks
- Exterior façade - architectural style, materials, balconies

- Future development plans, including project description and costs
- Current engineering reports
- ADA-compliant and adequate number of ADA-equipped rooms

### ***Lobby and Entrance***

- Porte-cochere
- Valet parking stand
- Shuttle bus pickup and parking area
- Doors - automatic, airlock vestibule, bell stand
- Luggage storage
- Concierge desk
- Restrooms
- Phones - house and public
- Front desk
  - Visibility to incoming guests
  - Elevator visibility
  - Reservation and registration systems
- Location of executive offices
- Lobby - decor, size, ceiling height
- Lobby layout and circulation
- Layout and circulation on other floors

### ***Guest Rooms***

- Total rooms, broken down by type of room so all are accounted for
- Number of connecting rooms
- Walking distance from facilities
- Size, ceiling height, terraces
- Furnishings - when last replaced, typical furniture inventory
- Refurbishment schedule
- Amenities - extra phones, multi-line phones, voicemail, computers, shoeshine, cable TV, VCR, etc.
- Doors - construction material, peephole, type of lock
- Closets - size, type of doors
- Wall material - plaster, drywall, concrete
- Windows - material, operation, glazing
- Sprinklers, smoke detectors, other life safety equipment
- Rooms for the handicapped
- No-smoking rooms
- Bathroom - lighting, amenities
- ADA-equipped facilities

### ***Corridors and Elevator Lobbies***

- Double-, single-loaded
- Interior, exterior
- Direction and width
- Lighting type(s), sufficiency of light level

- Ceiling height
- Wall covering
- Floor covering
- Elevator lobby furnishings
- Ice machine
- Soda and snack machines
- Maid, linen closets
- Life safety systems (smoke, fire, evacuation plan, location cards on all room doors)

### ***Food, Beverage, and Room Service Facilities***

- Seating capacities, meals served, and hours of operation
- Copies of menus
- Decor, theme, style, and quality of furnishings
- Bar
- Back-of-house access from kitchens
- Description of room service facilities
- Separate outside access, visibility of separate entrance
- Access to restrooms
- Entertainment policy
- Point-of-sale accounting system
- Number of meals served (covers) per meal period per outlet
- Average turnover per meal period per outlet
- Average check per meal period per outlet
- Estimate of in-house capture and outside capture per meal period
- Banquet space - square foot area and rental rates

### ***Housekeeping***

- Offices, storage, sorting areas
- Trash chute
- Linen chute
- Exhaust fan
- Washers
  - Manufacturer
  - Model number
  - Quantity
- Dryers
  - Manufacturer
  - Model number
  - Quantity
  - Fuel
  - Guest laundry, contract
- Self-serve guest laundries

### ***Kitchen(s)***

- Location(s)
- Access and distance to receiving and storage areas, food and beverage outlets, meeting rooms
- Description, quality, quantity, configuration, and condition of equipment
- Adequacy of size and layout

### ***Meeting and Banquet Facilities***

- Size, name, and capacities of each meeting room, including floor plan and locations
- Mix and number of breakaway rooms
- Decor
- Entrance, porte-cochere
- Service and public corridors to and from meeting rooms
- Proximity to kitchen
- Adequacy of audiovisual equipment, furniture, and meeting support amenities
- Furniture storage area
- HVAC zone control

### ***Amenities***

- Swimming-pool - shape, indoor or outdoor, type of enclosure, type of heating system
- Tennis courts - lighting
- Golf - number of holes and yards, annual rounds played, fees
- Jogging trails
- Type and inventory of health/exercise equipment - sauna, steam bath, whirlpool, massage, aerobics
- Description of spa
- Game rooms
- Facilities for horseback riding, ice skating, bowling, boating, sailing, fishing, water-skiing, snorkelling, windsurfing, skiing, racquetball, squash, other sports
- Business services - computer, fax, typing, express mail, etc.

### ***Back-of-House Layout***

- Employee entrance, lockers, rest areas, cafeteria, access pattern
- Security - timekeeping, personnel, purchasing offices
- Receiving/loading dock - guest view, lift
- Storerooms
- Engineering - shops, paint, TV locks, carpenter

### ***Building Systems***

- Structural support
- Foundation type
- Framing - steel, pre-cast concrete, reinforced concrete
- Walls - load-bearing, non-load-bearing
- Roof - age, condition, sloped or flat

- Roof material - asphalt shingle, built-up felt and tar, tar and gravel, slate, metal, clay tile
- Parking
  - Number of spaces
  - Indoor or outdoor
  - Valet service
  - Cost to guests
  - Percentage of use by others

### ***Vertical Transportation Systems***

- Passenger elevators
  - Number
  - Floors served
  - Manufacturer
  - Cable or hydraulic
  - Capacity
  - Feet per minute
  - Automatic or manned
  - Control system - mechanical or electrical relays, computerized load system
- Service elevators
  - Number
  - Floors served
  - Manufacturer
  - Cable or hydraulic
  - Capacity
  - Feet per minute
  - Control system - mechanical or electrical relays, computerized load system
- Escalators - number and floors served
- Dumbwaiters/freight lifts - number and floors served
- Stairs

### ***Heating, Ventilation, and Air-Conditioning***

- Type of heating system
  - Hot water, steam, electric
  - Fuel type
  - Two-, three-, or four-pipe, forced-air delivery
  - Simultaneous heating and cooling
- Boilers
  - Manufacturer
  - Model number
  - Age and condition
- Burners
  - Manufacturer
  - Model number
  - Age and condition
- Water heater
  - Manufacturer
  - Model number
  - Size of holding tank



- Age and condition
- Resistance
  - Manufacturer
  - Model or capacity
  - Age and condition
- Heat exchanger
  - Manufacturer
  - Model or capacity
  - Age and condition
- Heat pump
  - Manufacturer
  - Model number
  - Capacity
  - Age and condition
- Type of cooling system
  - Central/chilled water, heat pumps
- Chiller
  - Manufacturer
  - Model or capacity
  - Age and condition
- Cooling tower
  - Manufacturer
  - Model or capacity
  - Age and condition
- Zones
  - Guest rooms, meeting rooms, public space control

#### ***Energy Management Systems***

- Type of system
  - Manufacturer
  - Model number
- Individual thermostats
  - Guest rooms
  - Meeting and public space

#### ***Telephone, Television, Entertainment, Internet***

- Type of system
  - Manufacturer
  - Model number
- Type of call accounting
  - Least cost routing
- Other special functions

#### ***Life Safety Systems***

- Smoke detectors - local or wired
- Heat detectors - local or wired
- Sprinkler system

- Fire extinguisher
- Pull stations
  - Control, communication system
  - Manufacturer and model
- Annunciator panel - location
- Emergency lighting - battery backup
- Exit signage - battery backup
- Fire hoses
  - Fire pump manufacturer
  - Fire pump model
- Standpipes
- Kitchen range hood - CO<sub>2</sub> system/dry system
- Public address system
- Emergency generators and power
  - Manufacturer
  - Model number

### ***Security and Exterior Lighting***

- Electronic surveillance equipment
- Sodium, fluorescent, incandescent, spot, mercury, halogen bulbs
- Building signage

### ***Miscellaneous***

- Presence of asbestos
- Presence of urea-formaldehyde foam insulation
- Building inspection reports
- Health inspection reports
- Underground tanks
- Estimated deferred maintenance
- Estimated functional obsolescence.

### **Area-Specific Data**

#### ***Neighbourhood***

A neighbourhood is a group of complementary land uses that are similarly affected by the operation of the forces that affect property value. The geographic boundaries of the subject's neighbourhood are indicated by land use changes, transportation arteries/ bodies of water, and changes in elevation and topography.

- Neighbourhood characteristics - residential, commercial, retail, or industrial use; rural, suburban, metropolitan, or CBD; age, condition, and economic trends. Appraisers should define the characteristics of the neighbourhood and describe how these characteristics could impact the subject's ability to generate revenues.
- Neighbourhood buildings. Appraisers should make an inventory of the improvements surrounding the subject property and consider the impacts they might have on the subject's revenue-generating ability. Investigating the following factors can help:

- Types of building improvements
- Style, size, density, vacancy levels, rental rates, and trends
- Effective ages and maintenance or condition
- New development and construction
- Competitive facilities, particularly food and beverage
- Immediate generators of visitation
- Adverse conditions such as noise or other nuisances.
- Future trends and potential changes in neighbourhood characteristics. Appraisers should ask what impact these changes will have on the subject property.

#### ***Assessed Value and Real Estate and Personal Property Taxes***

- Estimate of future property taxes for the subject. Appraisers should evaluate local assessing practices and determine which jurisdictions levy real estate and personal property taxes.
- Current assessment of subject. Appraisers should obtain the name, address, and phone number of the assessor and a tax map showing the subject acreage in square feet and length of boundaries. They should also research lot and block number, tax identification number, current assessed value of land, and building and assessment date.
- Basis for assessment - income, cost, sales comparison, change upon sale. Appraisers should consider how the assessed value is calculated for land, improvements, and personal property.
- Date and frequency of assessment, fiscal year
- Five-year and current tax history
- Future trends in equalisation rates, assessed values, and mill rates for the subject's taxing jurisdictions
- Comparable hotel parcel numbers and assessments of land and buildings
- Appraisers should obtain information on how comparable hotels in the area are assessed and determine what the assessed values of comparable hotels for land, improvements, and personal property on a per-room basis.
- Tax abatement
- If the subject property qualifies for or receives any form of tax abatement, the appraiser should ask how it is calculated and what impact it has on property tax liability.
- Special and future assessments
- When an appraiser investigates probable future changes in assessments including any special assessments and tax liabilities, the assessing department can sometimes provide information related to local hotel trends, including:
  - Proposed hotels or hotels under construction
  - Land sales of hotel sites
  - Sales of hotels
  - Rates and occupancies of local hotels
  - Names of hotel owners.

#### ***Zoning/Building Department***

- Jurisdiction covering the subject property and, when appropriate, adjacent jurisdictions
- Names, addresses, and phone numbers of all contacts
- Proposed hotel development in market
  - Names of developers, hotel companies, etc.
  - Estimated completion dates

- Hotels under construction
  - Status of each proposed hotel
  - Description of approval process
- Zoning of subject - historical and current. Appraisers should obtain a zoning map and a copy of zoning regulations and investigate the following:
  - Conforming or nonconforming use of subject property
  - Height restrictions
  - Lot coverage, number of units, size restrictions, floor-area ratio
  - Setback restrictions
  - Parking requirements
  - Sign restrictions
  - Other restrictions
- Moratoriums on building, utilities
- Environmental impact study required for new development
- Zoning of surrounding land uses
- Future of neighbourhood
- Floodplain and seismic areas
- Zoning trends for area
  - Potential/probability of zoning changes
  - Building permits - five-year history, number, and dollar value
- Ability to expand subject property.

#### ***Planning Department***

- Jurisdictions encompassing the subject property and adjacent jurisdictions
- Occupancy and rates of existing hotels
- Proposed hotels, additions, expansions, or renovations
- Master (renewal) plan for development
- Pertinent documents
  - Land use map
  - Economic/demographic studies
  - Transportation studies
- Directions of growth - industrial, commercial, redevelopment
- Availability of public development or redevelopment funds/tax incentives for hotels.

#### ***Highway/Transportation Department***

- Names, addresses, and phone numbers of all contacts
- Origination and destination studies
- Traffic flow/count maps
- Future changes in transportation - road improvements and traffic rerouting roadway changes such as left-turn lanes, lights, curb cuts, medians, turn restrictions, and additional lanes
- Historic and current traffic counts, toll receipts
- Proposed hotels or hotels under construction.

### **Economic and Demographic Data - Trends**

During fieldwork the appraiser/analyst collects economic and demographic data describing the local economy and population. Data from the past 5 to 10 years provides a useful benchmark, but projected data is more useful for predicting future trends. Economic and demographic information is used to forecast changes in lodging demand and food and beverage usage over the projection period. Data an appraiser should collect includes:

- NAIC employment within the local market area
- Population - migration vs. births, peak vs. annual
- Population age distribution
- Income levels and effective buying income
- Retail sales
- Sales at eating and drinking establishments
- Office space occupancy levels, absorption trends
- Major businesses by employment sector, number of employees, ability to generate hotel demand
- Industrial space occupancy levels, absorption trends
- Unemployment trends
- Housing starts
- Building permits - number, dollar value
- Area maps
- Major generators of visitation room/bed tax data
- Visitor statistics, area attractions.

### ***Chambers of Commerce/Economic Development Agencies***

Local chambers of commerce and economic development agencies can often supply much of the economic and demographic data previously described. The following information should be sought:

- Names, addresses, and phone numbers of all contacts
- Area description - growth, economic and population trends, industries, demand generators
- Businesses entering and leaving area
- Area attractions - historical and projected visitation
- Introductions to area officials, hotel associations, etc.
- Occupancy and average rates at existing hotels, area-wide average
- Proposed hotels and hotels under construction
- Miscellaneous economic and demographic data.

### ***Newspapers***

- Advertising/research department
  - Economic and demographic data
- Real estate department
  - Articles on recently announced commercial/hotel projects
  - Stories on recent hotel or land sales.

### *Demand Generators List*

The appraiser should develop a list of market area demand generators.

- Typical hotel demand generators
  - Major companies
  - Office and industrial parks
  - Scenic sites
  - Hospitals - local, regional, or national specialty
  - Military installations
  - Colleges
  - Amusement parks
  - Resort facilities
  - Government offices
  - Residential developments
  - Racetracks
  - Historic events
  - Historic attractions
  - Retail shopping
  - Theatres
  - Museums
  - World's and state fairs
  - Sports stadiums
  - Sporting events
  - Festivals
  - Shows
  - National and state parks
  - Courts of law
  - County seats and state capitals
- Information collected about each generator
  - Description
  - Proximity to subject
  - Type of visitors
  - Visitor counts, admission charges, recent changes
  - Origin of visitors
  - Types of accommodation required
  - Season of visitation
- New generators entering the market.

### *Airport Authority*

If the market benefits from a nearby airport, data related to its usage should be obtained.

- Passenger and cargo traffic - past five years, projected, monthly fluctuations
- FAA terminal forecast of projected enplanements
- Airlines and number of flights
- Physical description of airport
- Airport expansion plans
- Cities served (origination)
- Restrictions on aircraft size, times of usage, number of days closed annually.

### ***Convention Centre and Visitors Bureau***

A convention centre can be a major generator of hotel demand. A visitors bureau often promotes convention centres and area attractions.

- Name, address, and phone number of all contacts
- Physical description of convention centre - size, capacities, age, facilities
- Historic and projected number of conventions and delegates, seasonality
- Average expenditure per conventioner
- Average length of stay, average convention size
- Future calendar, number of future events
- Marketing plan
- Promotion budget - past five years and projected, deficit funding
- Nature and type of events - local, state, regional, national and international
- Visitor statistics
- Hotel association
- Proposed hotels and hotels under construction.

### ***Car Rental Agencies***

- List of major companies renting cars
- Number of cars rented monthly, annually
- Average length of rentals
- Renter's points of origin.

### ***Competitive Hotels***

Such fieldwork is directed toward investigating competitive hotels. The data collected are used to quantify existing lodging demand and evaluate the relative competitiveness of area hotels:

- Name and address of competition
- Name of owner, management company, franchise
- Location and distance from subject and demand generators
- Access and visibility
- Year opened
- Number of rooms
- Various room types (e.g., king, double-double, ADA-equipped, etc.)
- Square footage
- Rates - high, medium, or low
- Type of construction
- Income-producing facilities
  - Names of restaurants, number of seats, types of service, hours of operation
  - Other food and beverage services
  - Banquet and meeting rooms
  - Amenities
- Interior or exterior corridors
- Condition and renovation plans
- Expansion plans

- Layout and functional utility
- Brochure description
- Published rates and special rates
- Occupancy and average rates, existing and historic trends
- Percentage of reservations from central reservation system
- Market segmentation (commercial, meeting, leisure)
- Usage of food and beverage facilities
- Seasonality of demand and usage and number of fill nights
- Major customers
- Frequent travel programs
- Special services provided
- Unionisation of workers
- Proposed hotels and hotels under construction
- Additions and renovations of existing hotels
- Hotels for sale or recently sold in market area
- Photographs of properties.

### ***Rooms, Bed, or Occupancy Tax***

Many jurisdictions impose a rooms tax, which is typically based on a percentage of rooms revenue. Tax data is often available and show revenue trends for the market area as well as for individual properties.

- Definition of taxable properties, change in number of taxable rooms
- Method of tax computation
- Historical taxes per month, past five years, future projections
- Identification of tax by property - occupancy and rate if available
- Historical tax rates and changes in rates.

### ***Hotel Associations***

Some market areas have organized hotel associations, which can provide useful information.

- Name, address, and phone number of all contacts
- List of existing hotels, market segmentation, rates, occupancies
- Total room count - current and historical
- Taxes per room or bed
- Hotels recently withdrawn or added to supply
- Sales transactions involving hotels
- Proposed hotels or hotels under construction.

### ***Competitive Restaurants and Lounges***

The following information is sometimes helpful in analysing the competitiveness of the subject's food and beverage facilities.

- Name and address of competing facility
- Number of seats



- Year opened
- Meals served, days open
- Affiliation
- Name of owner
- Renovation, expansion plans
- Seasonality - weekly, monthly
- Type of menu, service
- Type of patrons - age, income
- Decor/theme
- Entertainment policy
- Average check
- Covers, turnover
- Annual sales
- Reputation
- Location relative to subject property
- Condition.

### ***Liquor License Laws***

The availability of a liquor licence for a proposed hotel and the ability to transfer the liquor licence of an existing hotel can be important considerations.

- Acquisition, time, cost, limitations
- Restrictions
  - Ratio of liquor to food
  - Open to public
  - Required unit of sale
  - Minimum age
- Types of licenses.

### ***Sales of Competitive Hotels***

- Local databases that accumulate information on property transfers
- Hospitality Market Data Exchange - a national clearinghouse of sales transactions involving hotels and motels.

### ***Commercial Real Estate Firms, Boards, Brokers, Developers, and Relocation Services***

- Apartments that accommodate extended-stay demand (less than six months)
- Inventory of commercial, office, industrial, and retail space, historic absorption, and anticipated growth
- New projects, expansions, renovations. Useful data may include developer, location, size (in square feet), opening date, description of major committed tenants, projected occupancy, and tenant mix. Tenant mix by NAIC code and national vs. local company can indicate a hotel's ability to generate room nights.
- Geographic patterns of growth in office, industrial, retail, and residential space
- Source of tenants
- Sales transactions involving hotels
- Proposed hotels or hotels under construction.

***Local Appraisers, Counsellors, Bankers***

- Land and hotel sales
- Occupancy and average rate
- Market segmentation
- Proposed hotels, additions, and expansions
- Economic and demographic data
- Land use, value, and property tax rate trends.

***Photographs***

For a permanent record of site and neighbourhood characteristics, the appraiser may want to include the following photographs:

- Access to and visibility of subject property
- Entrance and sign
- View of subject - four sides
- View from subject - four sides
- Traffic photos - all directions
- Interior photos - lobby, registration, rooms, food and beverage outlets, meeting space, recreational facilities, back-of-house
- Surrounding land uses
- Competitive hotels
- Significant demand generators.

## **Addendum 'D'**

### **Hotel Development Cost Categories and Sub-Categories**

(Source: Hotel Capital Cost Components, 1998)

<b>Ref. No.</b>	<b>DESCRIPTION</b>
<b>1.0</b>	<b>LAND</b>
<b>1.1</b>	<b>Cost of land</b>
<b>1.2</b>	<b>Relocation compensation to tenants</b>
<b>1.3</b>	<b>Other costs</b>
<b>2.0</b>	<b>CONSTRUCTION</b>
<b>2.1</b>	<b>Demolition</b>
	<ul style="list-style-type: none"> <li>• Removal of debris</li> <li>• Salvage for re-use</li> <li>• Safety (shores &amp; supports)</li> <li>• Prevention of nuisance</li> <li>• Making good, protection &amp; preservation generally</li> </ul>
<b>2.2</b>	<b>General excavations and filling</b>
	<ul style="list-style-type: none"> <li>• Site exploration survey</li> <li>• Dealing with existing services</li> <li>• Preservation of backfill</li> <li>• Imported filling</li> <li>• Establishment of datum levels</li> <li>• Prevention of nuisance</li> <li>• Safety</li> <li>• Stopping off and plugging unused drains and pipes</li> <li>• De-watering</li> <li>• Disposal of excavated material.</li> </ul>
<b>2.3</b>	<b>Piling</b>
	<ul style="list-style-type: none"> <li>• Diaphragm walling</li> <li>• Under-pinning</li> </ul>

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<b>2.4</b>	<b>Concrete work</b>	<ul style="list-style-type: none"><li>• Mass concrete</li><li>• Reinforced concrete</li><li>• Pre-cast concrete</li><li>• Formwork</li><li>• Special surface finishes</li><li>• Jointing materials</li><li>• Waterproof membranes</li></ul>
<hr/>		
<b>2.5</b>	<b>Brickwork and blockwork</b>	<ul style="list-style-type: none"><li>• Common, engineering, facing and decorative brickwork</li><li>• Concrete blockwork</li><li>• Mortar, joint sealants, ties and reinforcement</li><li>• Airbricks, copings, sills and lintels</li><li>• DPC's, cavity insulation and fire stopping</li></ul>
<hr/>		
<b>2.6</b>	<b>Stone masonry</b>	<ul style="list-style-type: none"><li>• Natural stonework</li><li>• Cast and reconstructed stonework</li><li>• Mortar, mastics, metal fixings and ties</li></ul>
<hr/>		
<b>2.7</b>	<b>Structural metalwork</b>	
2.7.1	Structural steel	<ul style="list-style-type: none"><li>• Erection, fixings, fire protection, priming and painting</li></ul>
2.7.2	Structural aluminium	<ul style="list-style-type: none"><li>• Fabrication, erection and protection</li></ul>
<hr/>		
<b>2.8</b>	<b>Carpentry</b>	<ul style="list-style-type: none"><li>• Structural and non-structural timber</li><li>• Preservation and flame retardant treatment</li><li>• Plywood, chip board and other boards</li><li>• Wood wool and thermal insulation</li><li>• Pre-fabricated units</li><li>• Mechanical fastenings, adhesives and membranes</li><li>• Timber and metal stud partitioning</li></ul>

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**2.9 Roofing and cladding**

- Asphalt
- Slate, tiles and shingles
- Roofing membranes
- Lead, copper, aluminium and zinc sheeting
- Fixings, flashings, weatherings
- Surface protection

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**2.10 Tanking and waterproofing**

- Mastic asphalt
- Liquid and sheet membranes

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**2.11 Glazing**

- Glass, plate glass and tempered glass
- Obscure and patterned glass
- Decorative glass
- Fixed mirrors
- Fixings

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**2.12 Joinery and ironmongery**

2.12.1 Woodwork

- Natural hard and soft woods
- Grounds
- Decorative wood veneers
- Hardwood boards and sheets
- Mechanical fastenings
- Doors and special doors, seals and drop seals
- Rails, fixed screens and decorative trim
- Curtain and drapery pelmets
- Wainscoting and panelling
- Skirtings, crown mouldings, window boards, linings, etc.
- Bars, counters (including front desk)
- Booth partitions
- Bell captain's desk, cashiers' desks and permanent buffet units
- Work stations in switchboard and telex rooms, business centres, reservation rooms, etc.

- Guest room built-in furniture, closet shelves, drawers, minibar recess and counters
  - Floors
  - Barber and beauty shop cabinet work
  - Staircases
  - Windows and roof lights
  - Service area counters, shelving, notice boards, cork boards etc.
- 2.12.2 Ironmongery & accessories
- Architectural and general
  - Electronic key card system
  - Butts, floor hinges, closers and drop seals
  - Door stops and kick plates
  - Magnetic door holders
  - Decorative hardware
  - Door bells, peepholes, security latches etc.
  - Internal signage
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- 2.13 Non-structural metalwork**
- Ladders, stairs, grilles, windows, doors and roof lights
  - Roller shutters, railings
  - Show cases
  - Toilet partitions
  - Hanging rods, hooks and racks
  - Chutes, etc.
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- 2.14 Finishes**
- 2.14.1 Plasterwork
- Internal wall plasterwork
  - Plaster ceilings on concrete and lath
  - Decorative plasterwork
  - Special preparation to receive wall coverings
- 2.14.2 External rendering
- 2.14.3 Dry linings
- 2.14.4 Internal wall tiling
- Marble, ceramic and mosaics

- 2.14.5 External wall tiling
- Marble, ceramic and mosaics
- 2.14.6 Screeds - dense and lightweight
- 2.14.7 Floorings
- Granolithic, clay tiles, mastic tiles, terrazzo, sheet linoleum, etc.
  - Carpeting
- 2.14.8 Suspended ceilings
- Metal lath (for plaster)
  - Acoustic tile
  - Metal pan
  - Special systems
- 2.14.9 Marble & granite work
- Wainscotes and panelling
  - Counters and trim
  - Bathroom vanitories and thresholds
  - Toilet stalls
  - Other architectural details

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**2.15 Special Fit Out and Finishes**

- 2.15.1 Painting and decorating
- Paints, french and wax polishing, stains, oils, preservatives, wall paper, fabrics, etc.

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**2.16 Plumbing and drainage**

- 2.16.1 Rainwater goods
- Gutters, rainwater heads, pipes and fittings
  - Roof outlets and gratings, guards/outlet grilles
- 2.16.2 Sanitary pipework
- Cast iron, steel and plastic soil and vent pipes and fittings
  - Cast iron, steel and plastic waste pipes and fittings
- 2.16.3 Water services
- Copper, stainless steel and plastic supply pipes, valves and fittings
  - Fire standpipe systems, including fire pump, hose cabinets and hoses
  - Sprinkler systems.
  - Main service connection



- 2.16.4 Gas services
- Gas pipes, valves and fittings
  - Main service connection
- 2.16.5 Appliances
- Sanitary fixtures and fittings, accessories, taps, ball valves, wastes and traps
  - Cisterns, tanks, cylinders, immersion-heaters and pumps
  - Filtration, chlorination and water treatment
  - Other water heaters, boilers, etc.
  - Insulation of pipes, tanks, cisterns and cylinders
  - Domestic kitchen equipment supply installation in suites, apartments, utility areas, etc.
  - Bathroom ironmongery, eg., grab bars, coat hooks, soap dishes, heated towel rails, etc.
  - Shower cubicles, trays, curtain rails, etc.
- 2.16.6 Drainage
- Cast iron pipes, joints and fittings
  - Other pipes, joints and fittings
  - Field drains
  - Inspection covers and step irons
  - Special sewage disposal systems, equipment and piping
  - Main sewer and storm water drain connections
- 2.16.7 Ancillary
- Pipe sleeves, flue pipes and all other special fixing materials
  - Connections to special systems installed by others, e.g., kitchens, laundry, chilled drinking water systems, water coolers, etc., including traps, valves, strainers & accessories not supplied as an integral part of the equipment and required to complete the installation for full operational use

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<b>2.17</b>	<b>Heating, cooling and refrigeration</b>	
2.17.1	Boilers	<ul style="list-style-type: none"><li>• Gas, oil and electric boilers, fuel tanks, storage</li><li>• Steam generators</li><li>• Solar collectors</li><li>• Alternative fuel boilers</li><li>• Primary heat distribution, including traps, pipes and fittings</li></ul>
2.17.2	Heating	<ul style="list-style-type: none"><li>• Steam heating</li><li>• Warm air heating</li><li>• Local heating units</li><li>• Heat recovery</li></ul>
2.17.3	Cooling/refrigeration	<ul style="list-style-type: none"><li>• Central refrigeration plant</li><li>• Primary and secondary cooling distribution, including valves, pipes and fittings</li><li>• Cooling towers</li><li>• Local cooling units</li></ul>

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<b>2.18</b>	<b>Construction - Ventilation and air conditioning systems</b>	
2.18.1	General supply and extract	<ul style="list-style-type: none"><li>• Toilet and bathroom extract</li><li>• Kitchen extract</li><li>• Car park extract</li><li>• Smoke extract and control</li></ul>
2.18.2	Air conditioning	<ul style="list-style-type: none"><li>• Low velocity</li><li>• Other systems</li><li>• Fan coil</li><li>• Floor and wall units</li><li>• Air curtains, etc.</li><li>• Ductwork, filters, fire dampers and reset access</li><li>• Automatic and manual controls</li><li>• Louvres and grilles</li><li>• Laundry and kitchen hoods/ventilated ceilings</li><li>• Drainage piping and fittings</li><li>• Piping and duct insulation</li><li>• Blowers and fans</li></ul>

- Special air conditioning systems for telephone equipment, main computer and lift machine rooms

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**2.19 Electrical systems**

- 2.19.1 Generating plant
- 2.19.2 HV-supply
- 2.19.3 LV-supply
- 2.19.4 LV distribution
- 2.19.5 Other special supplies

- All wiring, conduits, fittings and boxes to all electrical systems including communications
- Lighting fixtures (including

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**2.20 Electrical systems special lighting fixtures**

- Dimmers, stage lighting and spotlights
- Waterproof lights for swimming pools
- External & internal illuminated signs
- External lighting
- Uninterrupted power supply, equipment, material and installations for computer - operations
- Bulbs and tubes for all lighting fixtures (including 10% spare supply for each type and rating)

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**2.21 Communications Systems and Life Safety**

- 2.21.1 Telecommunications

- Telephone trunk lines and equipment
- Switchboard
- Wiring distribution panels
- Instruments
- Demonstration of completed system, including inter-face with billing systems, rooms status and wake-up alarm systems and training

2.21.2	Paging
2.21.3	Public address and sound amplification
2.21.4	Intercom
2.21.5	Simultaneous translation
2.21.6	Radio/TV

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**2.22 Communications Systems and TV sets**

2.22.1	Projection
2.22.2	Built-in projection screens and chalk boards
2.22.3	Advertising display
2.22.4	Clocks
2.22.5	Computer systems
	<ul style="list-style-type: none"><li>• Coordination on conduit layout</li><li>• Automatic fire smothering system</li><li>• Coordination of movement to and placing in final position of main equipment</li><li>• Assistance in making final connections to the distribution system by the suppliers' installers</li><li>• Provision of un-interrupted power supply (UPS)</li></ul>
2.22.6	Access control
2.22.7	Security detection and alarms
2.22.8	Fire detection and alarms
2.22.9	Lightning protection
2.22.10	TV monitors
2.22.11	Building automation

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**2.23 Transport systems**

2.23.1	Lifts	<ul style="list-style-type: none"><li>• Passenger, service and freight lifts</li></ul>
2.23.2	Escalators	
2.23.3	Hoists	
2.23.4	Travelling cradles	

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**2.24 Kitchen and bar equipment**

- Supply, installation and connecting up to gas, electricity, water and drainage services
- Start-up and demonstration at full operating capacity
- Hand-over with all manuals and as-built drawings

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<b>2.25</b>	<b>Refrigeration and freezing equipment</b>	<ul style="list-style-type: none"><li>• Walk-in boxes to kitchen consultant's specifications</li><li>• Condenser water piping, refrigerant tubing, compressors, compressor racks, etc.</li><li>• Cooling tower</li><li>• Insulation</li><li>• Doors, machinery, controls complete, including alarms and warning devices</li><li>• Start-up, monitoring and demonstration at full operating capacity to hotel operations</li></ul>
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<b>2.26</b>	<b>Laundry equipment</b>	<ul style="list-style-type: none"><li>• Linen chute</li><li>• Laundry equipment</li><li>• Dry cleaning equipment</li><li>• Rolling equipment</li><li>• Tables and bins</li><li>• Supply, installation, start-up and demonstration at full operating capacity to hotel operations</li></ul>
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**2.27 Other special equipment**

2.27.1	Fire Extinguishers
2.27.2	Soap dispensing equipment, towel holders, built-in waste bins and/or hand dryers

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**2.28 External works**

2.28.1	General clearing and earthworks
2.28.2	General planting, turfing & trees
2.28.3	Pavings, kerbs & channels
2.28.4	Fencing, walls & gates
2.28.5	Service main trenches & ducts
2.28.6	External fitments, signs, buildings (e.g., beach huts) etc.
2.28.7	Flagpoles
2.28.8	Blinds and canopies

- Adapting and maintenance as necessary of all temporary works, clearing away and making good when no longer required

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2.29	General	<ul style="list-style-type: none"><li>• All preliminary, general and special costs in addition to those included above, for the proper management and execution of the works</li></ul>
2.29.1	Handover	<ul style="list-style-type: none"><li>• All costs relating to programmed phased handover of the site to Hotel operations for occupancy and training</li><li>• Handing over in a clean, functional and secure condition ready for occupation and use as specified</li><li>• Testing, commissioning and demonstration to hotel operations of all MEP systems</li><li>• Provision of all instruction manuals, spares and keys as specified</li></ul>
2.29.2	Miscellaneous	<ul style="list-style-type: none"><li>• Management of the works</li><li>• All expenses of labour employment including safety, health, welfare and insurance</li><li>• Programming of the works</li><li>• Site security</li><li>• Protection of the works</li><li>• Drying out of the works</li><li>• Prevention of nuisance</li><li>• Provision of all plant and equipment</li><li>• Hoardings, barriers</li><li>• Site access</li><li>• Temporary buildings, sanitary and welfare facilities</li><li>• Payment of local rates and charges</li><li>• Water, power, lighting and telephone facilities</li><li>• Site drainage</li><li>• All other preliminary and general costs of the contract works</li></ul>

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<b>2.30</b>	<b>Other construction costs</b>	
2.30.1	Performance bonds, insurance	<ul style="list-style-type: none"> <li>• Hotel company liability insurance</li> <li>• Bonds and other insurance</li> </ul>
2.30.2	Surveys and other hotel company technical costs	<ul style="list-style-type: none"> <li>• Land, building and services</li> <li>• Boring, tests and analysis</li> <li>• Models</li> <li>• Site investigations and reports</li> <li>• Concrete tests</li> </ul>
2.30.3	Miscellaneous fees and expenses	<ul style="list-style-type: none"> <li>• Utility connection fees</li> <li>• Building and other construction permits</li> <li>• Occupancy permits, etc.</li> </ul>
2.30.4	Administrative costs	<ul style="list-style-type: none"> <li>• Fees and related costs of independent construction project manager</li> <li>• Other administrative salary and related costs</li> <li>• Communications - telephones, fax, postage, etc.</li> <li>• Office rent, furniture and equipment</li> <li>• Office supplies</li> <li>• Other miscellaneous expenses.</li> </ul>
2.30.5	Taxes and duties	

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**3.0 FURNITURE, FIXTURES AND EQUIPMENT (FFE)**

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3.1	Linen	<ul style="list-style-type: none"> <li>• Cotton, blends, linen, huck and terry</li> </ul>
3.1.1	Guest bed	
3.1.2	Blankets	
3.1.3	Guest bath	
3.1.4	Table	
3.1.5	Banquet	
3.1.6	Kitchen	
3.1.7	Pool	
3.1.8	Employees	
3.1.9	Health club	

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**3.2 Silver**

- 3.2.1 Flatware - table setting
- 3.2.2 Flatware - other
- 3.2.3 Hollowware

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**3.3 China**

- 3.3.1 Multi-purpose restaurant
- 3.3.2 Specialty restaurant
- 3.3.3 Service plates
- 3.3.4 Ovenware
- 3.3.5 Banquet/room service
- 3.3.6 Special
- 3.3.8 Ashtrays

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**3.4 Glassware**

- 3.4.1 Table/food service
- 3.4.2 Bar
- 3.4.3 Guest room
- 3.4.4 Snack bar

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**3.5 Staff housing**

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**3.6 Guest room/corridor**

- Installation according to design layout where appropriate
- 3.6.1 Case goods
- 3.6.2 Seating
- Chairs and sofas
- 3.6.3 Bedding
- 3.6.4 Balcony furniture
- 3.6.5 Guest room carpets and rugs
- Underlay
- 3.6.6 Curtains etc.
- Drapes, curtain tracks, carriers, hooks and blinds
- 3.6.7 Shower curtains and hooks
- 3.6.8 Bedspreads
- 3.6.9 Lamps
- Bulbs; cords and plugs
- 10% bulb spares



3.6.10	Pictures etc.	<ul style="list-style-type: none"> <li>• Panels, mirrors and other decorative items</li> </ul>
3.6.11	TV/radio sets	<ul style="list-style-type: none"> <li>• Adjustment and demonstration to Hotel operator</li> </ul>
3.6.12	Mini-bars	<ul style="list-style-type: none"> <li>• Adjustment and demonstration to Hotel operator</li> </ul>
3.6.13	Miscellaneous equipment	<ul style="list-style-type: none"> <li>• Coat hangers, rollaway beds, wastebaskets, etc.</li> </ul>
3.6.13	Corridor carpets	<ul style="list-style-type: none"> <li>• Including guest lift hall and service lift lobby</li> </ul>
3.6.14	Pillows and bolsters	
3.6.15	Special decorator's work	
3.6.16	Principal suites	

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**3.7 Public areas**

		<ul style="list-style-type: none"> <li>• Installation according to design layouts where appropriate</li> </ul>
3.7.1	Lobby furniture	<ul style="list-style-type: none"> <li>• Connection and installation of bellman's annunciator equipment in bell captain's desk</li> </ul>
3.7.2	Tables - dining/cocktail	
3.7.3	Seating, moveable - dining/cocktail	
3.7.4	Banquettes	
3.7.5	Stools	
3.7.6	Service stands	<ul style="list-style-type: none"> <li>• Fixed and moveable</li> </ul>
3.7.7	Outdoor furniture	
3.7.8	Banquet tables	
3.7.9	Banquet seating	
3.7.10	Carpets	<ul style="list-style-type: none"> <li>• Rugs</li> <li>• Underlay</li> </ul>
3.7.11	Drapery etc.	<ul style="list-style-type: none"> <li>• Curtains, curtain tracks, carriers, hooks, shades and portable screens</li> </ul>
3.7.12	Mirrors - non-fixed	

3.7.13	Lamps	<ul style="list-style-type: none"><li>• Bulbs, cords and plugs</li><li>• 10% bulb spares of various types</li></ul>
3.7.14	Pictures	<ul style="list-style-type: none"><li>• Picture lights</li></ul>
3.7.15	Moveable equipment	<ul style="list-style-type: none"><li>• Lecterns, blackboards, projectors and portable dance floors</li></ul>
3.7.16	Pianos	
3.7.17	Card tables/chairs	
3.7.18	Casino	<ul style="list-style-type: none"><li>• All furniture and supplies</li></ul>
3.7.19	Special decorator items	
3.7.20	Banquet moveable platform	
3.7.21	Auditorium seating	
3.7.22	Public rest room furniture	<ul style="list-style-type: none"><li>• Equipment</li></ul>
3.7.23	Executive offices furniture and furnishings	
<hr/>		
<b>3.8</b>	<b>Service areas</b>	
3.8.1	Desks, tables, files and office furniture	
3.8.2	Chairs	<ul style="list-style-type: none"><li>• Telephone operators', cashiers' and checkers'</li></ul>
3.8.3	Lamps	<ul style="list-style-type: none"><li>• Bulbs, cords and plugs</li><li>• 10% bulbs spares of different types</li></ul>
3.8.4	Miscellaneous	<ul style="list-style-type: none"><li>• Telephone operators' rest area</li></ul>
3.8.5	Employees facilities	<ul style="list-style-type: none"><li>• Dining room and lounge</li><li>• In-hotel dormitory</li><li>• Training room</li></ul>
3.8.6	Carpet	<ul style="list-style-type: none"><li>• In service area offices, training room and staff rest rooms only</li></ul>

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**3.9 Portable kitchen and bar equipment**

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**3.10 Kitchen and bar utensils**

- 3.10.1 Pots, pans, food containers and bowls - aluminium
- 3.10.2 Pots, pans, food containers and bowls - stainless steel and others (non-aluminium)
- 3.10.3 Cutlery
- 3.10.4 Wire baskets and broilers
  - Dish/glass washing racks
- 3.10.5 Straining implements
- 3.10.6 Scoops, spoons, whips, ladles, measures and moulds
- 3.10.7 Cutters, skewers and openers
- 3.10.8 Kitchen implements - general
- 3.10.9 Kitchen sanitation
- 3.10.10 Bar implements
- 3.10.11 Bakery implements
- 3.10.12 Snack bar implements

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**3.11 Food and beverage service**

- 3.11.1 Room service equipment
- 3.11.2 Chafing dishes, food pans and rechauds
- 3.11.3 Rolling service
- 3.11.4 Coffee service - portable
- 3.11.5 Trays
- 3.11.6 Food specialty items
- 3.11.7 Stainless steel flatware
- 3.11.8 Stainless steel hollowware

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**3.12 Employees food service**

- 3.12.1 Trays
- 3.12.2 Dishware
- 3.12.3 Utensils
- 3.12.4 Glassware

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**3.13 Portable items for laundry**

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**3.14 Housekeeping equipment**

- 3.14.1 Tracks
- 3.14.2 Machines
- 3.14.3 Cleaning equipment (non-mechanical)
- 3.14.4 Miscellaneous

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**3.15 Office equipment and furniture**

- 3.15.1 Safes and cashier's drop boxes
- 3.15.2 Safe Deposit boxes
- 3.15.3 Front desk equipment
- 3.15.4 Typewriters and copy machines
- 3.15.5 Calculators
- 3.15.6 Miscellaneous

---

**3.16 Computers and related electronic business machines**

- Start-up and demonstration to Hotel operations
- 3.16.1 Front office hardware
- 3.16.2 Back office hardware
- 3.16.3 Point of sales hardware
- 3.16.4 Other hardware for management and administrative offices
  - Personal computers and word processors
- 3.16.5 Ancillary equipment for hardware
  - Equipment stands, cabinets and other furniture specifically designed for computer systems
- 3.16.6 Front office software
- 3.16.7 Back office software
- 3.16.8 Other software

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**3.17 Uniforms**

- 3.17.1 Front office
- 3.17.2 Kitchen
- 3.17.3 Housekeeping and Laundry
- 3.17.4 Engineering
- 3.17.5 Waiters and busboys
- 3.17.6 Waitresses
- 3.17.7 Barmen
- 3.17.8 Casino
- 3.17.9 Miscellaneous

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**3.18 Tools**

- 3.18.1 Carpenter
- 3.18.2 Mechanical and plumbing
- 3.18.3 Boiler
- 3.18.4 Electrical/electronic
- 3.18.5 Locksmith
- 3.18.6 Painting
- 3.18.7 Upholstery
- 3.18.8 Garden
- 3.18.9 Millwright and refrigerator mechanic

- 3.18.10 Mason
- 3.18.11 Miscellaneous (water treatment, fire cart etc.)

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**3.19 Lockers**

- Supply, assembly and installation

- 3.19.1 Employees
- 3.19.2 Pool and Health Club

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**3.20 In-house movie system**

- Supply, installation and demonstration to Hotel operations

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**3.21 Barber/beauty**

- 3.21.1 Equipment
- 3.21.2 Furniture

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**3.22 Print shop**

- 3.22.1 Printing equipment
- 3.22.2 Miscellaneous

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**3.23 Motor transport**

- 3.23.1 Executive
- 3.23.2 Guest
- 3.23.3 Employee
- 3.23.4 Stores

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**3.24 Sports and playground equipment and games**

- 3.24.1 Playground equipment
- 3.24.2 Sports and games equipment
  - Tennis and squash court nets, posts, etc.
- 3.24.3 Health Club and Sauna equipment and machines
- 3.24.4 Pool and beach equipment
- 3.24.5 Casino equipment
- 3.24.6 Landscape maintenance equipment

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**3.25 Purchasing costs**

- 3.25.1 Freight and insurance
- 3.25.2 Duties and taxes
- 3.25.3 Replacement stock

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**3.26 Supervision, storage and installation**

- 3.26.1 Labour
- 3.26.2 Site office
  - Secure storage
- 3.26.3 Off-site warehousing

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**3.27 Purchasing fees**

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**4.0 TECHNICAL SERVICES AND OTHER PROFESSIONAL FEES**

- Normal travel and related expenses, and other operating

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**4.1 Operator Fees**

- 4.1.1 Technical Service
- 4.1.2 Specialist services

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**4.2 Design Consultants**

- 4.2.1 Architects
- 4.2.2 MEP Engineers
- 4.2.3 Structural Engineers
- 4.2.4 Interior Designers
- 4.2.5 Quantity Surveyors

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**4.3 Specialist Consultants**

- 4.3.1 Kitchen
- 4.3.2 Laundry
- 4.3.3 Audio-visual
- 4.3.4 Landscape
- 4.3.5 Lighting
- 4.3.6 Acoustics
- 4.3.7 Others

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**5.0 OTHER FEES**

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**6.0 FINANCING COSTS**

<b>7.0</b>	<b>ORGANISATION AND DEVELOPMENT COSTS</b>
<b>7.1</b>	<b>Feasibility studies</b>
<b>7.2</b>	<b>Legal costs</b>
<b>7.3</b>	<b>Miscellaneous</b>
<b>8.0</b>	<b>PRE-OPENING EXPENSES</b>
<b>8.1</b>	<b>Salaries</b>
	<ul style="list-style-type: none"> <li>• Benefits, relocation and housing</li> </ul>
<b>8.2</b>	<b>Special training</b>
	<ul style="list-style-type: none"> <li>• MIS on-site costs for setting up special systems</li> </ul>
<b>8.3</b>	<b>Transportation</b>
<b>8.4</b>	<b>Advertising, marketing and special events</b>
<b>8.5</b>	<b>Expendable operating supplies</b>
8.5.1	Office supplies
	<ul style="list-style-type: none"> <li>• Accounting and personnel forms and other stationery</li> </ul>
8.5.2	Special printing
8.5.3	Food & Beverage service supplies
8.5.3	Kitchen supplies
8.5.4	Menus and related items
8.5.5	Guest convenience supplies
8.5.6	Print shop supplies
8.5.7	Laundry and dry cleaning supplies
8.5.8	Housekeeping supplies
8.5.9	Maintenance supplies
8.5.10	Specialty supplies
8.5.11	Beauty and barber shop supplies
8.5.12	Miscellaneous
<b>8.6</b>	<b>Food</b>
<b>8.7</b>	<b>Beverages</b>
<b>8.8</b>	<b>Engineering department supplies</b>
	<ul style="list-style-type: none"> <li>• Spare parts</li> </ul>
<b>9.0</b>	<b>WORKING CAPITAL</b>
<b>10.0</b>	<b>CONTINGENCY</b>

## **Addendum 'E'**

### **Hotel Project Brief Summary**

(Sources: Baltin et al, 1999: 164, and Ransley and Ingram, 2000: 20)



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- A.1.3 Preliminary operational philosophy

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- A.2.3 Guest facilities
- A.2.4 Service accommodation with support areas
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- A.3.3 General setting
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- A.6.1 Basic flow pattern diagram
- A.6.2 Typical hotel - area relationship plan

**Summary of Areas**

	<b>Square Metres</b>	<b>Square Feet</b>
<b>1.00 to 22.00 Total Project</b>		
1.00 Guest Rooms and Circulation Areas	24,965	268,623
2.00 Public Areas	485	5,218
3.00 Retail	260	2,797
4.00 Front Desk	183	1,970
5.00 Guest Amenities/Recreation	937	10,082
6.00 Food and Beverage Areas	1,162	12,503
7.00 Function Areas	2,777	29,880
8.00 Function Support	1,693	18,218
9.00 Executive Offices	93	1,002
10.00 General Offices	232	2,496
11.00 Accounting Offices	160	1,722
12.00 Food Service Areas	1,417	15,249
13.00 Housekeeping/Laundry	370	3,983
14.00 Maintenance	195	2,099
15.00 Employee Facilities	580	6,240
16.00 Mechanical/Electrical	2,460	26,470
17.00 Receiving and Purchasing	296	3,185
18.00 Circulation	3,100	33,356
19.00 Pool Facility	75	808
20.00 Water Treatment	400	4,304
21.00 Waste Water Treatment	600	6,456
22.00 Landscape Maintenance Facility	<u>114</u>	<u>1,227</u>
<b>Project Total</b>	<b>42,554</b>	<b>457,888</b>

**1.00 Guest Rooms and Circulation Areas**

1.01 Rooms (1 Module = 47.5 square meters)		
185 King Rooms (1 Module)	8,788	94,559
122 Double Rooms (1 Module)	5,795	62,354
20 Parlour Suites (1.5 Modules)	1,425	15,333
21 Executive Suites (2 Modules)	1,995	21,466
2 Presidential Suites (5 Modules)	475	5,111
1 Club Lounge (5 Modules)	<u>237</u>	<u>2,550</u>
<b>Subtotal Guest Rooms</b>	<b>18,715</b>	<b>201,373</b>

	Square Metres	Square Feet
1.02 Corridors	2,500	26,900
1.03 Vertical Transportation	1,400	15,064
1.04 Service	1,350	14,526
1.05 Balconies	<u>1,000</u>	<u>10,760</u>
<b>Subtotal Circulation Area</b>	<b><u>6,250</u></b>	<b><u>67,250</u></b>
<b>Total Guest Rooms and Circulation Area</b>	<b><u>24,965</u></b>	<b><u>268,623</u></b>
<b>2.00 Public Areas</b>		
2.01 Porte-Cochere (Outside)	0	0
2.02 Entry Vestibule	19	205
2.03 Reception Lobby	186	2,000
2.04 Grand Stair	85	915
2.05 Toilets	175	1,883
2.06 Telephone	<u>20</u>	<u>215</u>
<b>Total Public Areas</b>	<b><u>485</u></b>	<b><u>5,218</u></b>
<b>3.00 Retail Space</b>		
3.01 Sundry	50	538
3.02 Gift Shop	50	538
3.03 Logo Shop	80	861
3.04 Travel	20	215
3.05 Beauty Salon at Fitness Centre	<u>60</u>	<u>645</u>
<b>Total Retail Area</b>	<b><u>260</u></b>	<b><u>2,797</u></b>
<b>4.00 Front Desk</b>		
4.01 Registration/Cashier	19	205
4.02 Work Counter	9	97
4.03 Safety Deposit Boxes (SDB)	5	54
4.04 SDB Viewing Area	5	54
4.05 Front Office Manager (Office)	9	97
4.06 Credit Manager	9	97
4.07 Reservations/Telephone Operators	60	645
4.08 Concierge	15	161
4.09 Bell Captain/Baggage Storage	23	248
4.10 Valet Parking	9	97
4.11 Circulation	<u>20</u>	<u>215</u>
<b>Total Front Desk Area</b>	<b><u>183</u></b>	<b><u>1,970</u></b>
<b>5.00 Guest Amenities and Recreation</b>		
5.01 Business Centre	47	506
5.02 Executive Fitness Club	700	7,532
5.03 Pool (Outdoor)	0	0
5.04 Tennis Courts (4) (Outdoor)	0	0
5.05 Squash Courts (2)	190	2,044
5.06 Children's Facility (Outdoor)	<u>0</u>	<u>0</u>
<b>Total Guest Amenities and Recreation Area</b>	<b><u>937</u></b>	<b><u>10,082</u></b>

	<b>Square Metres</b>	<b>Square Feet</b>
<b>6.00 Food and Beverage Areas</b> (Number of Seats)		
6.01 Fine Dining Restaurant		
Dining (80)	250	2,690
Private Dining (14)	37	398
6.02 Three-Meal Restaurant		
Dining (140)	350	3,767
Bar (5)	0	0
Café Terrace (75) (Outside)	0	0
6.03 Lobby Lounge (100)	280	3,012
6.04 Specialty Restaurant		
Dining (64)	170	1,829
Private Dining (36) (3 Rooms)	75	807
6.05 Pool Facilities (Outside)		
Bar (5)	0	0
Covered Dining (35)	0	0
Covered Terrace (20)	<u>0</u>	<u>0</u>
<b>Total Food and Beverage Area</b>	<b>1,162</b>	<b>12,503</b>
<b>7.00 Function Areas</b>		
7.01 Main Ballroom	1,400	15,064
7.02 Junior Ballroom	500	5,380
7.03 Boardroom No. 1	75	807
7.04 Boardroom No. 2	37	398
7.05 Meeting Room No. 1	50	538
7.06 Meeting Room No. 2	80	861
7.07 Meeting Room No. 3	80	861
7.08 Meeting Room No. 4	80	861
7.09 Meeting Room No. 5	95	1,022
7.10 Meeting Room No. 6	95	1,022
7.11 Meeting Room No. 7	95	1,022
7.12 Meeting Room No. 8	95	1,022
7.13 Meeting Room No. 9	<u>95</u>	<u>1,022</u>
<b>Total Function Area</b>	<b>2,777</b>	<b>29,880</b>
<b>8.00 Function Support Areas</b>		
8.01 Pre-function Area	985	10,599
8.02 Grand Stair	100	1,076
8.03 Toilets	325	3,497
8.04 Storage	170	1,829
8.05 Public Phones	50	538
8.06 Audiovisual Storage	19	205
8.07 Banquet Service Manager	19	205
8.08 Control Booth	10	108
8.09 Coatroom	<u>15</u>	<u>161</u>
<b>Total Function Support Area</b>	<b>1,693</b>	<b>18,218</b>

	Square Metres	Square Feet
<b>9.00 Executive Offices</b>		
9.01 General Manager	14	151
9.02 Administrative Assistant	9	97
9.03 Food and Beverage Executive	9	97
9.04 Secretary	9	97
9.05 Rooms Executive	9	97
9.06 Secretary	9	97
9.07 Storage	9	97
9.08 Reception	9	97
9.09 Circulation	<u>16</u>	<u>172</u>
<b>Total Executive Offices Area</b>	<b>93</b>	<b>1,002</b>
<b>10.00 General Offices</b>		
10.01 Catering and Conference Services Director	10	108
10.02 Catering and Conference Service Managers	49	527
10.03 Administrative Assistants	28	301
10.04 Sales and Marketing Director	9	97
10.05 Sales Managers	56	603
10.06 Administrative Assistants	33	355
10.07 Market Research Analysts and Guest History	11	118
10.08 Public Relations	7	75
10.09 Copying, Mail, and Coffee	9	97
10.10 Circulation	<u>20</u>	<u>215</u>
<b>Total General Offices Area</b>	<b>232</b>	<b>2,496</b>
<b>11.00 Accounting Offices</b>		
11.01 Controller	9	97
11.02 Assistant	7	75
11.03 Administrative Assistant	7	75
11.04 General Cashier/Safes	14	151
11.05 Counting Room	16	172
11.06 Clerks	50	538
11.07 Computer Room.	23	248
11.08 Storage, Mail, and Copying	15	161
11.09 Circulation	<u>19</u>	<u>205</u>
<b>Total Accounting Offices Area</b>	<b>160</b>	<b>1,722</b>

	<b>Square Metres</b>	<b>Square Feet</b>
<b>12.00 Food Service Operations</b>		
12.01 Kitchen and Dishware Washing	372	4,003
12.02 Second Kitchen	232	2,496
12.03 Specialty Restaurant Kitchen	232	2,496
12.04 Butcher Shop and Garden Manager	65	699
12.05 Bake Shop, Chocolates, and Pastry Dish-Up	65	699
12.06 Pastry Dish-Up	9	97
12.07 Chef Office	15	161
12.08 Room Service	19	205
12.09 Dry Storage	19	205
12.10 Chemical Storage and Toilets	9	97
12.11 Refrigerated Storage	19	205
12.12 Freezer Storage	19	205
12.13 Liquor Storage	28	301
12.14 Main Service Bar	50	538
12.15 Wines and Beer	9	97
12.16 Soda	9	97
12.17 Steward Office	9	97
12.18 Silver Storage	19	205
12.19 Silver Burnishing	9	97
12.20 China and Glass Storage	<u>9</u>	<u>97</u>
12.21 Function Pantry	<u>200</u>	<u>2,152</u>
<b>Total Food Service Area`</b>	<b>1,417</b>	<b>15,249</b>
<b>13.00 Housekeeping and Laundry Operations</b>		
13.01 Linen Storage	19	205
13.02 Secured Storage	9	97
13.03 Housekeeping Storage	13	140
13.04 Sewing	9	97
13.05 Lost and Found	7	75
13.06 Director (Office)	9	97
13.07 Assistant Manager and Secretary	9	97
13.08 Laundry	165	1,775
13.09 Uniform Issue	19	205
13.10 Mechanical	9	97
13.11 Sorting	19	205
13.12 Detergent Storage	9	97
13.13 Valet	65	699
13.14 Supervisor	<u>9</u>	<u>97</u>
<b>Total Housekeeping and Laundry Area</b>	<b>370</b>	<b>3,983</b>

	Square Metres	Square Feet
<b>14.00 Maintenance Operations</b>		
14.01 Director	9	97
14.02 Assistant	9	97
14.03 Key Room	9	97
14.04 Parts	9	97
14.05 TV Room	9	97
14.06 Paint Shop	19	205
14.07 General	93	1,001
14.08 Yard Storage	<u>38</u>	<u>408</u>
<b>Total Maintenance Area</b>	<b>195</b>	<b>2,099</b>
<b>15.00 Employee Facilities</b>		
15.01 Men's Locker Room	140	1,506
15.02 Women's Locker Room	140	1,506
15.03 Cafeteria	160	1,722
15.04 Training Room	95	1,022
15.05 Restrooms	<u>45</u>	<u>484</u>
<b>Total Employee Facilities Area</b>	<b>580</b>	<b>6,240</b>
<b>16.00 Mechanical and Electrical Equipment</b>		
16.01 Transformer Vault	50	538
16.02 Generator	600	6,456
16.03 Switch Gear	300	3,228
16.04 Panel Room	60	646
16.05 Mechanical	750	8,070
16.06 Boiler	300	3,228
16.07 Telephone, Computer, and PBX	25	269
16.08 Chases	25	269
16.09 Elevator Machine Room	<u>350</u>	<u>3,766</u>
<b>Total Mechanical and Electrical Area</b>	<b>2,460</b>	<b>26,470</b>
<b>17.00 Receiving and Purchasing</b>		
17.01 Truck Dock	40	430
17.02 Compactor	9	97
17.03 Receiving	9	97
17.04 Temporary Storage	19	205
17.05 Refrigerated Garbage	9	97
17.06 Can Wash	5	54
17.07 Dry Wash	5	54
17.08 Security and Fire Control	40	430
17.09 Purchasing	15	161
17.10 Personnel	9	97
17.11 Assistant	40	430
17.12 Waiting	9	97
17.13 Storage	40	430
17.14 Food Washing and Sorting	20	215
17.15 Benefits Office	8	86

	<b>Square Metres</b>	<b>Square Feet</b>
17.16 Nurse	9	97
17.17 Flower Shop	<u>10</u>	<u>108</u>
<b>Total Receiving and Purchasing Area</b>	<b>296</b>	<b>3,185</b>
<hr/>		
<b>18.00 Circulation</b>		
18.01 Public	1,300	13,988
18.02 Back-of-House	<u>1,800</u>	<u>19,368</u>
<b>Total Circulation Area</b>	<b>3,100</b>	<b>33,356</b>
<hr/>		
<b>19.00 Pool Facility</b>		
19.01 Kitchen, Coolers, and Server Station	51	549
19.02 Towel Issue	5	54
19.03 Toilets, Janitor's Closet, and Mechanical	<u>19</u>	<u>205</u>
<b>Total Pool Facility Area</b>	<b>75</b>	<b>808</b>
<hr/>		
<b>20.00 Water Treatment</b>		
20.01 Pump Room	85	915
20.02 Water Storage	<u>315</u>	<u>3,389</u>
<b>Total Water Treatment Area</b>	<b>400</b>	<b>4,304</b>
<hr/>		
<b>21.00 Wastewater Treatment</b>		
21.01 Treatment Equipment	400	4,304
21.02 Wastewater Storage	<u>200</u>	<u>2,152</u>
<b>Total Wastewater Treatment Area</b>	<b>600</b>	<b>6,456</b>
<hr/>		
<b>22.00 Landscape Maintenance Facility</b>		
22.01 Office	11	118
22.02 Secured Locker	14	151
22.03 Secured Locker	9	97
22.04 Uniform Issue Closet	7	75
22.05 Restrooms	5	54
22.06 Bays	58	624
22.07 Circulation	<u>10</u>	<u>108</u>
<b>Total Landscape Maintenance Facility Area</b>	<b>114</b>	<b>1,227</b>



**Addendum 'F'**

**Hotel Operator Questionnaire**

**Section A: Hotel Operator Details**

**1 Organisation Name:**

**2 Interviewee Name:**

**3 Interviewee Position:**

**4 Interview Date:**

**5 Market segments served by hotel organisation:**

**Table 5(a): Segmentation In terms of Price**

<b>Budget (Limited Service)</b>	<b>Mid-Scale (Limited Service)</b>	<b>Mid-Scale (Full Service)</b>	<b>Upscale (Full Service)</b>	<b>Upper-Scale (1<sup>st</sup> Class)</b>

**Table 5(b): Segmentation In terms of Market Served**

<b>Convention</b>	<b>Business</b>	<b>Casino</b>	<b>Leisure</b>	<b>Groups</b>	<b>Game / Safari</b>	<b>Other</b>

**Table 5(c): Segmentation In terms of Location**

<b>City Centre</b>	<b>Suburban</b>	<b>Resort</b>	<b>Rural</b>	<b>Game / Safari</b>	<b>Other</b>

**6 Organisation size, in terms of:**

- a. Annual turnover
- b. Number of rooms available
- c. Average number of rooms per hotel
- d. Number of hotels (in various categories)

## **Section B: Hotel Development Framework Questions**

### **1 Hotel Operator's Strategic Context / Characteristics**

#### **1.1 Mission Statement**

The mission statement is an important device that can provide an understanding for staff working in different parts of the organisation, assisting them to pull together and uphold the corporate values and philosophy. However, it is essential that the mission statement is communicated clearly to all stakeholders and is perceived to be both relevant and realistic. Unless these requirements are met, the mission statement is unlikely to have any real impact on the organisation.

Pearce and Robinson (1995: 14) suggest that the: “... *mission of a company is the unique purpose that sets it apart from other companies of its type and identifies the scope of its operations. In short, the mission describes the company's product, market, and technological areas of emphasis in a way that reflects the values and priorities of the strategic decision makers.*”

An example of an international hotel organisation's mission statement is Inter-Continental Hotels': (Six Continents Hotels and Resorts Web Page, 2001)

*“We aim to be the leading global hotel owner/operator/franchisor in the upscale market, satisfying guests at a profit by delivering the highest levels of guest satisfaction, the best cash flows and asset value growth for owners, and to be the employer of choice for our people.”*

##### **1.1.1 Does your organisation have a clearly defined mission statement?**

##### **1.1.2 Does your organisation define long, medium and short-term corporate objectives?**

##### **1.1.3 Are the following questions clearly answered by your organisation's mission statement, corporate objectives and strategic planning:**

- 1.1.3.1 Who and what are we?
- 1.1.3.2 Where are we now?
- 1.1.3.3 Where do we want to be?
- 1.1.3.4 How might we get there?
- 1.1.3.5 Which way is the best?
- 1.1.3.6 How can we ensure survival?

## **2 Development Audit**

### **2.1 Development Audit Explanation**

*“A [development] audit provides the means for the organisation to understand how it relates to the environment in which it operates. It also enables internal strengths and weaknesses to be identified in terms of how they match external opportunities and threats. The [development] audit should be a systematic, critical and unbiased review and appraisal of the company’s [development] operations. Thus, it provides management with the information to select a position in its particular environment based on known facts. In short, it provides the answer to the question: Where is the company now? “ (McDonald & Payne, 1998: 78).*

### **2.2 Development Audit Questions**

2.2.1 What would you include in your organisations development audit / analysis?

2.2.2 Who are your organisation’s major competitors?

2.2.3 What are your major market segment’s:

a) Size in terms of annual monetary value?

b) Growth potential for 2002 to 2004?

c) Expected future trends?

d) Average room rates?

e) Customer demographics?

2.2.4 What is your market share in your primary market segment?

## **3 Development Strategy**

### **3.1 Development Strategy Explanation**

A development strategy is a statement of how an organisation intends to reach its growth objectives, and in the hotel industry this often means the construction of new units. Development considerations would include the site size, cost per room and total development costs, and some general guidelines that could help with the rapid appraisal of potential new projects. Finally, a set of locational criteria should be developed to assist in ensuring that the hotel is constructed in suitable contexts. This shows how a clear development strategy can assist in the proliferation of a hotel brand (Ransley and Ingram, 2000).

### **3.2 Development Strategy Questions**

- 3.2.1 Are your organisation's development objectives clearly defined?
- 3.2.2 Are your organisation's brands, products or services defined?
- 3.2.3 Are your organisation's strengths and weaknesses identified and understood at executive level?
- 3.2.4 Do you know what the opportunities and threats for your organisation are?
- 3.2.5 Who is the competition and what is known about them and their strategies?
- 3.2.6 How can a competitive advantage be obtained?
- 3.2.7 Who are our customers?
- 3.2.8 Are these characteristics likely to change and if so how and why?
- 3.2.9 Are there external influences that are likely to affect the 'marketplace', including political, environmental, economic or legislative issues?

## **4 Development Criteria**

### **4.1 Development Criteria Explanation**

Development criteria are all the elements that might affect the development of the hotel product (Ransley & Ingram, 2000).

### **4.2 Development Criteria Questions**

- 4.2.1 Does your organisation define specific criteria, to which a possible development should comply?
- 4.2.2 What are the broad categories of criteria?
- 4.2.3 What criteria, as an example, would be included?

## **5 Project Objectives**

### **5.1 Project Objectives Explanation**

Arthur Andersen Real Estate Services highlights in their Corporate Finance Quarterly Report for Europe 2001, that from experience the most common downfalls when developing a project are: (Echavarren, 2001)

- Lack of vision and objectives for the project: the project arises on impulse and its strategy and objectives are not clearly defined.

- Unrealistic objectives: estimated savings or expected returns are not calculated properly.
- Inadequate project specifications, requirements not calculated, areas undefined

## **5.2 Project Objective Questions**

- 5.2.1 When developing a new hotel, does your organisation define specific project objectives?
- 5.2.2 What are the broad categories of project criteria?
- 5.2.3 Name a few examples of project criteria?

## **6 Hotel Property Development Process**

- 6.1 Could you describe or define a typical hotel property development process for your organisation?

## **7 Feasibility Analysis**

- 7.1 What does a typical feasibility analysis of a new hotel development comprise of for your organisation?
- 7.2 What would you include in a physical feasibility analysis?
- 7.3 What would you include in a market feasibility analysis?
- 7.4 What would you include in a financial feasibility analysis?

**Addendum 'G'**

**Hotel Property Developer Questionnaire**

**Section A:** **Hotel Property Developer Details**

- 1 Organisation Name:**
- 2 Interviewee Name:**
- 3 Interviewee Position:**
- 4 Interview Date:**
- 5 Organisation size, in terms of:**
  - a. Annual hotel development turnover?
  - b. Number of hotel rooms developed, during 2001 to 2002?
  - c. Average number of hotel rooms developed annually?
  - d. Number of hotels to date?



## **Section B: Hotel Development Framework Questions**

### **1. Development Audit**

#### **1.1 Development Audit Explanation**

*“A [development] audit provides the means for the organisation to understand how it relates to the environment in which it operates. It also enables internal strengths and weaknesses to be identified in terms of how they match external opportunities and threats. The [development] audit should be a systematic, critical and unbiased review and appraisal of the company’s [development] operations. Thus, it provides management with the information to select a position in its particular environment based on known facts. In short, it provides the answer to the question: Where is the company now? “ (McDonald & Payne, 1998: 78).*

#### **1.2 Development Audit Questions**

- 1.2.1 What would you include in your organisations development audit / analysis for a new hotel development?
- 1.2.2 Who are your organisation’s major competitors?

### **2 Development Strategy**

#### **2.1 Development Strategy Explanation**

A development strategy is a statement of how an organisation intends to reach its growth objectives, and in the hotel industry this often means the construction of new units. Development considerations would include the site size, cost per room and total development costs, and some general guidelines that could help with the rapid appraisal of potential new projects. Finally, a set of locational criteria should be developed to assist in ensuring that the hotel is constructed in suitable contexts. This shows how a clear development strategy can assist in the proliferation of a hotel brand (Ransley and Ingram, 2000).

#### **2.2 Development Strategy Questions**

When you select a possible hotel operator for a new hotel development, do you

- 2.2.1 Clearly defined hotel development objectives?
- 2.2.2 Distinct between different hotel organisation’s brands, products or services?
- 2.2.3 Identify the strengths and weaknesses, and the opportunities and threats of a new development?
- 2.2.4 Who the competition is and what are known about them and their strategies?

- 2.2.5 Know how a new hotel development establishes a competitive advantage?
- 2.2.6 Who the new development's customers are?
- 2.2.7 Identify external influences that might likely affect the 'marketplace', including political, environmental, economic or legislative issues?

### **3 Development Criteria**

#### **3.1 Development Criteria Explanation**

Development criteria are all the elements that might affect the development of the hotel product (Ransley & Ingram, 2000).

#### **3.2 Development Criteria Questions**

- 3.2.1 Does your organisation define specific criteria, to which a possible development should comply?
- 3.2.2 What are the broad categories of criteria?
- 3.2.3 What criteria, as an example, would be included?

### **4 Project Objectives**

#### **4.1 Project Objectives Explanation**

Arthur Andersen Real Estate Services highlights in their Corporate Finance Quarterly Report for Europe 2001, that from experience the most common downfalls when developing a project are: (Echavarren, 2001)

- Lack of vision and objectives for the project: the project arises on impulse and its strategy and objectives are not clearly defined.
- Unrealistic objectives: estimated savings or expected returns are not calculated properly.
- Inadequate project specifications, requirements not calculated, areas undefined

#### **4.2 Project Objective Questions**

- 4.2.1 When developing a new hotel, does your organisation define specific project objectives?
- 4.2.2 What are the broad categories of project criteria?
- 4.2.3 Name a few examples of project criteria?

**5 Hotel Property Development Process**

5.1 Could you describe or define a typical hotel property development process for your organisation?

**6 Feasibility Analysis**

6.1 What does a typical feasibility analysis of a new hotel development comprise of for your organisation?

6.2 What would you include in a physical feasibility analysis?

6.3 What would you include in a market feasibility analysis?

6.4 What would you include in a financial feasibility analysis?

## GLOSSARY OF TERMS

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Term	Definition
<b>Accommodatable Latent Demand</b>	: A portion of latent demand, consisting of induced and unaccommodated room night demand, which does not impact a market area until additional hotel rooms are introduced. The amount of accommodatable latent demand is calculated by multiplying the number of new hotel rooms by 365 days per year and by the local, area wide occupancy rate.
<b>Accounting Rate of Return</b>	: The percentage rate of return earned by a capital investment project.
<b>Actual Market Share</b>	: The percentage share of the total hotel room night demand actually captured by a particular hotel. The actual market share for an individual hotel is calculated by dividing the number of room nights captured by the total number of room nights in the market.
<b>Adjusted Variable Component</b>	: The variable portion of an item of hotel revenue or expense that has already been adjusted by its index of variability.
<b>Architect</b>	: The architect establishes the building design and is often responsible for the detailed design of the fabric of a hotel. Architects are concerned with both the functional and aesthetic issues of building design. Typically, architects are appointed as lead consultants and will contribute to the project brief.
<b>Armoire</b>	: Sideboard with enclosed TV unit.
<b>Area per room</b>	: A useful guide to ensure the efficient use of space within the hotel. This is defined as the gross floor area of the whole building divided by the number of bedrooms.
<b>Asset</b>	: Can represent a building or item of mechanical or electrical plant.
<b>Asset management</b>	: The process by which a property with money value is effectively controlled and managed as a business.
<b>A/V</b>	: Audio/Visual
<b>Average Rate</b>	:
<b>Back of House</b>	: The working areas of a hotel, which are usually not open to guests. The back of the house includes the kitchen, laundry, storage areas, machinery rooms, and shops.
<b>Base Year</b>	: The year that serves as a benchmark for all future projections. The base year is generally the last calendar year completed before fieldwork begins.
<b>Bed Board</b>	: A board that is used in the bed for sleeping on. Provided on request for guests with back trouble.
<b>Bell Service</b>	: The services of carrying bags, storing bags, providing items to the guestroom.
<b>Bill of Quantities</b>	: A pricing document prepared by a quantity surveyor, which may include a detailed description of the type and quantity of the work involved.

Term	Definition
<b>Brands</b>	: Brands are products, services or concepts that can be distinguished from other products, services or concepts in a way that can be easily communicated and marketed. A 'brand name' is the distinctive name used to market the offer.
<b>Brown Field Site</b>	: Development land or site area that is contaminated or requires remedial works before new development or building can occur.
<b>Budget Cost</b>	: The predicted cost as opposed to the actual cost.
<b>Buildability</b>	: Judgement based on experience and practice as to the practicability of a construction method or form.
<b>Combed Percalé</b>	: Measure of thread density in sheeting.
<b>Comp Room</b>	: A room provided free of charge (comp = complimentary).
<b>Commissioning</b>	: Establishing a building as a working operation.
<b>Comparable Base</b>	: A basis for hotel revenue and expense projections developed by adjusting the income and expense statements of comparable hotels. The comparable base is used in the Fixed and Variable Forecasting Model to quantify the fixed and variable components of items of income and expense.
<b>Competitive Index</b>	: A number that reflects the relative competitiveness of a hotel. The competitive index of a hotel is calculated by dividing the number of room nights accommodated within a particular market segment by the property's room count. The result is the number of days per year that a guestroom is actually occupied by a specific type of traveller. By comparing the competitive indexes of several hotels, an appraiser can evaluate the competitiveness of each property.
<b>Concept</b>	: The process of identifying, defining and collecting ideas to create an image for a new business or product.
<b>Development</b>	
<b>Condition Survey</b>	: Inspection and report describing the current state of a building or item of plant.
<b>Construction Manager</b>	: The construction manager is a fee earning professional who is employed to programme and co-ordinate the construction works undertaken. The construction manager selects, supervises and manages the work of specialist trade contractors who are employed to undertake the work.
<b>Contract Rate</b>	: A discounted room rate available to specific high-volume users such as airlines, convention groups and bus tours. Contract rates are negotiated by the user and the hotel, and often apply to a block of rooms that are reserved on an ongoing basis and paid for whether they are used or not. For example, an airline may contract for 35 rooms per night for a full year. Two crews may utilise these rooms in a day, if scheduling permits. The rooms may not be used at all. Depending on the amount and timing of the usage, a contract rate may be heavily discounted and fall significantly below both the average rate and the commercial rate.
<b>Cost of Capital</b>	: The rate of return required by investors in the business.
<b>Crib</b>	: Baby's cot
<b>Credenza</b>	: Sideboard
<b>CRO</b>	: Central Reservations Office
<b>Deadlock,</b>	: A square, non-angled, locking device.
<b>Dead-bolt</b>	

Term	Definition
<b>Debentures</b>	: Fixed interest long-term loans.
<b>Demand Generator</b>	: Anything that creates or attracts hotel room night demand. Examples of demand generators include office parks, convention centres, scenic attractions, shopping malls, regional hospitals, sporting events, universities, military bases, airports, and convenient stopping points along a highway.
<b>Depreciation</b>	: The proportion of the cost of a fixed asset which is to be charged to the profit of the business.
<b>Discount Factor</b>	: The percentage rate of return which represents the opportunity cost of using the funds in different ways.
<b>Discounted cash flow</b>	: The future monetary value of net cash flows expressed in present value terms.
<b>Double loaded corridors</b>	: A corridor providing access to rooms on two sides.
<b>Due diligence</b>	: A systematic process in which concerted attempts are made to unearth every fact that is material to the situation, and that might affect the decision to continue with the venture.
<b>Excess Land</b>	: Contiguous, additional land that is not needed for the successful operation of a hotel. For the land to be considered excess, it must be possible to separate it from the hotel's parcel without adversely affecting the zoning, access, visibility, parking, guest comfort, operational efficiencies, or overall desirability of the hotel.
<b>Executive Desk Set</b>	: Blotter pad & holder, plus accessories.
<b>Expected Monetary Value (EMV)</b>	: A weighted average of the values of the possible outcomes of some action, the weights being the respective probabilities. Facilities management A contract to look after a property, which may cover not just building and plant maintenance and renewal, but also the provision of services such as security, laundry or computer facilities.
<b>Fair Market Share</b>	: A hotel's average percentage share of the total area's room night demand. Fair market share is calculated by dividing a hotel's room count by the total number of competitive rooms in the market. This benchmark is used to determine whether a property is capturing more or less than its appropriate share of total market demand.
<b>F&amp;B</b>	: Food & Beverage – all eating and drinking facilities /services.
<b>Feasibility Study</b>	: A written document prepared in the planning stage of a new development that represents research to justify the costs and benefits of undertaking the project.
<b>FF&amp;E</b>	: Furniture, Fixtures (Fittings) and Equipment.
<b>Fill Nights</b>	: The number of nights that a hotel operates at 100% capacity. The number of fill nights in a market can be used as a basis for quantifying unaccommodated demand.
<b>Fill Pattern</b>	: A specific pattern that reflects when a hotel is operating at capacity. This pattern generally depends on the nature of the demand. For example, strong commercial demand will generally produce fill nights Monday through Thursday, which is the period when commercial travel is most prevalent.

Term	Definition
<b>Footprint</b>	: A statement of the gross area of the building which covers the site at ground floor level, regardless of height or overhangs.
<b>FSM</b>	: Franchise Service Manager
<b>Fully Repairing and Insuring (FRI)</b>	: A leasehold agreement in which the lessee or tenant has full responsibility to keep in good repair both the inside and outside of the leased building.
<b>Green Field Site</b>	: A parcel of land designated for the first time for new development.
<b>GM</b>	: Hotel General Manager
<b>Guestroom</b>	: See <i>hotel unit</i>
<b>Guaranteed All-night</b>	: A reservation where payment is guaranteed, usually by a credit card number or fax letter, and the room is therefore held all night.
<b>Historic Average Room Count</b>	: The effective room count of a hotel that opens or expands during a projection year. For example, a 300-room hotel that opens on July 1 has a historic average room count for that year of 1 50. This factor is useful in projecting room night demand.
<b>Hotel Unit</b>	: The smallest rentable accommodation that provides a guest with a bedroom, a bathroom, and lockable access to a public corridor or the exterior of the facility. A hotel unit is also referred to as a <i>room</i> or a <i>key</i> .
<b>Hurdle Rate</b>	: Target return on capital proposed for capital investment projects that exceed the cost of capital.
<b>HVAC</b>	: Heating, Ventilation and Air-conditioning
<b>IATA</b>	: International Airline Transportation Association
<b>Index of Variability</b>	: The factor that controls the movement of the variable component of an item of income or expense. When forecasting food and beverage departmental expense, for example, the variable portion of the expense depends largely on changes in the property's food and beverage revenue.
<b>Induced Demand</b>	: New hotel room night demand that has been attracted to a market area by a recently created attraction or demand generator. For example, the opening of a large convention hotel will often create induced demand by providing facilities for meetings and groups that might not have been attracted to the market previously.
<b>In-room Dining</b>	: Room Service
<b>Interior Designer</b>	: The interior designer is responsible for the design of the finishes and furniture, fittings and equipment elements of a hotel. The interior designer may, if appointed at an early stage, be involved in the space planning of a hotel.
<b>Internal Rate of Return (IRR)</b>	: A method of assessment of capital projects in which future cash flows are discounted to equal the cost of the project. The rate of interest that is effective in achieving this is the internal rate of return. Where there are several projects being contemplated, the one showing the highest internal rate of return is usually chosen.
<b>Internal Repairing and Insuring (IRI)</b>	: A leasehold agreement in which the tenant agrees to undertake internal repairs.
<b>ISDN</b>	: International Standard Digital Network (digital phone line)
<b>Joint Venture</b>	: An agreement by two parties with different expertise to jointly invest and/or manage a development or facility

Term	Definition
<b>Kerbside/ Doorservice</b>	: An extension of Bell Service that is given to guests as they arrive in their cars. Includes opening of the car door, offering to take bags, and offering valet parking service.
<b>Lead Time</b>	: The time taken in planning or implementing an event until it actually occurs.
<b>Lease Contract</b>	: A form of legal agreement to lease an asset that is owned by one party who receives rent from another party, the tenant. The tenant operates the business for a period of time in the expectation that the profits from the business will exceed the rent paid. The lease is normally long term (typically fifteen to twenty years plus tenants' options to extend) with the property owner receiving a fixed rent.
<b>Life Cycle</b>	: The length of time a whole building or individual part may last, including maintenance required.
<b>Life cycle Costing</b>	: A group of economic appraisal techniques which assess the sum of all relevant capital, operating and maintenance costs and incomes of an asset. All costs and incomes are brought together in a comparable form, allowing for the fact that cash flows occur at different times during an asset's life cycle.
<b>Maintenance</b>	: Replacement or overhaul of a building component, for example windows or items of plant, such as replacing the heating boiler, to ensure that an agreed standard of service is economically achieved.
<b>Management Contract</b>	: An agreement in which a hospitality management company not only offers a licence for the use of its brand name and reservation system but also takes full responsibility for the day-to-day management of the hotel as agent for the owner of the asset.
<b>Market Share Adjuster</b>	: A factor that indicates the relative competitiveness of a hotel and is used to project its market share. The market share adjuster is calculated by multiplying the competitive index of the property by its room count. The hotel's market share is then calculated by dividing the market share adjuster for the property by the total market share adjuster of all the hotels in the market.
<b>Massing</b>	: The aggregation or volume of the components of the building(s), and their relationships to each other.
<b>Mechanical Feasibility Studies</b>	: Mechanical studies are those which a client commissions because it is required by a third party, for example in support of the application for funds, and this is the most common circumstance in which a mechanical study is prepared. Bankers, certainly, are less willing to lend on projects unless such appraisals have been well organized and have been carried out by independent professional organisations.
<b>Monte Carlo Simulation</b>	: A risk analysis procedure based on the calculation of the frequency and mean of the estimated value of a large number of possible inputs and outputs in an investment decision.
<b>Negative Feasibility Study</b>	: One which recommends that a project is not pursued.
<b>Net Present Value</b>	: The current cash value of future discounted net cash flows arising from a project.
<b>Net Rooms Revenue</b>	: The rooms revenue remaining after expenses such as sales tax, rooms tax, and other occupancy taxes are deducted.



Term	Definition
<b>Occupancy Report</b>	: A report prepared each evening by the night auditor which reflects the number of occupied rooms and the percentage of occupancy. This and other revenue information—e.g., the average room rate—is reported to management in the daily occupancy report, which is also referred to as the <i>daily report</i> .
<b>Opportunity Cost</b>	: A term in economics that means the next best alternative that has been foregone. This may represent the time taken or money lost from not choosing a particular option.
<b>Outturn Cost</b>	: The agreed final cost of a development project.
<b>Paid Rooms Occupied</b>	: The total number of rooms sold to paying guests. Most hotels also have a few complimentary rooms, which are given away for promotional reasons. When quantifying area wide demand, the appraiser includes both paid and complimentary rooms.
<b>Payback Method</b>	: A method for discriminating between projects based on how quickly the original cash investment is repaid.
<b>Penetration</b>	: The percentage relationship between the market share of a hotel and its fair share. When a hotel is capturing more than its average market share, the penetration is greater than 100%.
<b>Percentage Phase-in</b>	: An amount of induced demand assumed to enter the market over a period of time. Using the Room Night Analysis program, an appraiser can phase-in a specific percentage of induced demand each year.
<b>PMS</b>	: Property Management System: The main computer system the hotel, handling check-in/out, guest folios, etc.
<b>Planned Preventative Maintenance</b>	: A phased schedule of regular property and equipment maintenance and repairs over time.
<b>Powerdesk</b>	: A brand name for a unique design of desk furniture which contains an integral computer and internet access.
<b>Principal Contractor</b>	: The appointment of a principal contractor is a statutory requirement under the Construction (Design & Management) Regulations 1994. The principal contractor must be involved in the management of the construction work, must be competent and able to allocate adequate resources to the task.
<b>Proactive Feasibility Study Procurement</b>	: One where the client who commissions it requires information to be provided in addition to projections of the return on investment. : Method of obtaining by care and effort the most suitable process or competitively priced element for construction or purchase.
<b>Product Building</b>	: Where the building form is an integral part of a lifestyle product, such as a hotel.
<b>Profit and Loss Projection</b>	: A forecast of income and expense made in accordance with the Uniform System of Accounts for Hotels.
<b>Profit Percentage</b>	: The ratio of dollar profit to total revenue.

Term	Definition
<b>Published Rate</b>	: The room rates listed in hotel directories, advertisements, and rate cards. Generally, the published rate is the hotel's highest room rate. Also referred to as <i>rack rate</i> . This rate is usually quoted as a range (i.e. single room = \$70 - \$ 100) and represents the various rack rates for specific types of accommodation. Published room rates usually set the upper limits of average rates. Average room rates tend to be closer to published rates for single rooms than for double rooms. (Also referred to as the rack rate)
<b>Rack Rate</b>	: An undiscounted room rate generally given to anyone who does not qualify or ask for a special discounted rate. The term is derived from the room rack, a front desk feature that is less common in the computer age. The room rack traditionally contains information about each room's rate, including the highest rate that can be charged for that particular accommodation. When a hotel is expected to be full during a certain period or a guest arrives without a reservation, the rack rate is often the only rate available. The average room rate is always less than the rack rate. (Also referred to as the published rate)
<b>Real Estate Investment Trust (REIT)</b>	: Started in the US, a REIT is an investment vehicle that takes the form of real estate mutual fund permitting small investors to participate in large, professionally managed real estate projects.
<b>Reservation Report</b>	: A report issued by a hotel franchisor which describes the reservation activity generated by the central reservation system. One of the reports typically included in the reservation report is the monthly denial report.
<b>Restaurant Activity Index (RAI)</b>	: An index published by <i>Restaurant Business</i> magazine which measures an area's restaurant sales activity relative to its food store sales and compares this ratio to the national average. The resulting index reflects the market's propensity to eat away from home.
<b>Restaurant Growth Index (RGI)</b>	: An index published by <i>Restaurant Business</i> magazine which shows the relationship between restaurant supply and demand. The RGI is used to determine whether a market can absorb additional restaurants.
<b>RevPAR</b>	: Revenue per Available Room.
<b>Risk Allowance</b>	: A contingency sum that is set aside to fund the cost of construction variations.
<b>Risk Management</b>	: A process used by project teams to reduce the impact of risks on the outcomes of a project, through the formal identification, appraisal and management of potential risk events throughout the life of the project.
<b>Rollaway Bed Room Night</b>	: A transportable bed, which can be moved into or out of a room. : A unit of hotel demand representing one hotel room occupied by one or more people for one night. A family of four occupying a hotel room for one night is considered one room night. That same family of four occupying two hotel rooms for one night is considered two room nights.
<b>Schedule of Condition</b>	: Details the state of the property at the start of a lease, as a standard by which the tenant must hand back the property at the end of the lease period.

Term	Definition
<b>Sensitivity Analysis</b>	: An accounting technique that measures the relationship of cost and volume to profits. If small changes in factors such as volume, selling price, and variable and fixed costs cause a large change in profit, it can be said that profit is sensitive to that factor, and that it is critical to the business.
<b>Snagging List</b>	: The joint identification of a list of faults or problems that need to be rectified before the final payment is made to the contractor(s).
<b>Straight-line Method Depreciation</b>	: This method charges an equal amount of depreciation to each accounting period that benefits from the use of the fixed asset.
<b>SOE (also OS&amp;E)</b>	: Soft Operating Equipment, or Operational Supply (also named Operational Supply and Equipment)
<b>Shoulder Season</b>	: Is a time (period) of moderate business between the high and low periods at a resort
<b>Turnaways</b>	: Inquiries for accommodation at a hotel that is fully occupied. Turnaway demand is important in quantifying unaccommodated demand.
<b>Turnkey Projects</b>	: A development project in which the sole contractor is responsible for design, construction, fitting out and commissioning the building, so that all the client has to do is turn the key and begin trading.
<b>Unaccommodatable Latent Demand</b>	: The portion of latent hotel room night demand that cannot be accommodated in the market area because there are not sufficient new hotel rooms available to absorb it. Unless new hotel rooms are introduced into the market area, latent demand will remain unaccommodatable.
<b>Unaccommodated Demand</b>	: Excess demand for hotel room nights produced by travellers who cannot find lodging accommodation during periods of peak occupancies. Therefore, these individuals must defer their trips, settle for less desirable accommodation, or stay outside the market area. When performing a hotel market study, unaccommodated demand must be quantified to measure the true depth of the market.
<b>Valet Parking</b>	: Where hotel staff park and retrieve guests' vehicles on their behalf.
<b>Value Management</b>	: A process used by project teams to define the objectives of a project and to deliver these economically and quickly.
<b>Voicemail</b>	: An automatic message-taking system incorporated in the hotel's telephone system.
<b>Waiver</b>	: An exception to a particular standard, granted to hotels in exceptional circumstances, and generally with an expiration date imposed.
<b>Walked Room</b>	: Where a guest did not have their reservation honoured. They were instead 'walked' to suitable alternative accommodation, and compensated for the inconvenience. (The compensation being greater in cases where the guest had a Guaranteed All-Night Reservation.)
<b>Walk-ins</b>	: Guests that register at a hotel without a reservation

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Term	Definition
<b>Weighted Average Cost of Capital (WACC)</b>	: Represents the combined cost of the sources of finance utilised by the business.
<b>Yield Management</b>	: A technique that aims to maximize revenue over a cycle of peaks and troughs by adjusting prices to suit market demand.
<b>Zone Split</b>	: The physical division of a property to be refurbished between the parts that are open for business, and those that are to be closed for building work.

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