

# Advice on hotel, motel investment

by Carlton Smith  
for the Tundra Times

During the '70s in Alaska, millions were spent on new hotel and motel construction.

Several older hotels were re-sold to new owners, and it seemed logical that hotel properties might be an excellent investment.

Statewide, numerous companies chose to get involved in tourism in this way and made substantial investments, taking on significant debt to become involved in the industry. Some of the same companies engaged management firms to run their hotels by contract, which added to operating costs in addition to debt service.

Today, some of the same properties and their owners are faced with either heavy annual losses or marginally profitable properties that have no longer term prospects for developing good returns for shareholders.

A critical question becomes how to turn this situation around so owners can either look at making major changes for their operations or evaluate selling these properties and obtaining the highest possible value on sale.

There are five key steps to properly assess the value and marketability of a hotel property.

Let's take a look at each of the five segments and how a company might approach them.

•**Property Condition.** In this part of the process, a hotel property should be examined thoroughly by a professional engineer qualified to spot potential structural, plumbing, electrical or code problems that might interfere with the sale of the property.

Taken together, a report by such an individual can be used as a disclosure to a prospective buyer identifying that

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a thorough review of the property had been completed by a professional inspector.

•**Financial Statements.** The financial statements of the operation are, next to the quality of management, the most important information contributing to a successful sale.

Actual (not estimated) income and expense figures for at least the current and past two years of operation will provide a prospective purchaser with complete information from which to make a decision to purchase.

In fact, the story of a hotel's or motel's true operating health is told here, and the care taken in the preparation and review of these data will determine how seriously the purchase of a property is considered by a prospective buyer.

•**Current hotel management.** When a property is evaluated for sale, the management of the hotel — the skills and day-to-day oversight of the operation should have real value to the new owner because the management of the operation actually secures the cash-flow of the hotel and gives it real money-making potential season to season.

If the management team of the hotel is to go with the purchase of the property, that group of professionals should be very involved with the sale process and might actually have some financial incentives to assist in the sale.

•**Other options besides outright sale.** There can often be other uses to a hotel



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property through conversion if an owner decides to maintain ownership but improve the financial viability of a property. Some of these options might include converting the property to an apartment building, condominium or office building.

These types of conversion proposals, however, each require a review of what are called "civil" requirements of the local municipality or the state and include specific rules for such features as parking, zoning classifications, fire code rules and construction standards for different uses.

Also, one conversion cost can involve higher cash requirements than another, and return the same or less cash once conversion is complete. Other conversions can take place rather inexpensively and offer a much higher rate of return to the owners once the conversion is complete.

Of course, projected income statements will be required to be developed for each of the proposed changes in building use. You may

wish to employ a third party professional accounting firm to assist in preparing the pro-forma statements on all proposed options so that the data can be evaluated in a consistent way.

•**Review of the marketing elements for a property.** The overall benefits for a prospective owner of a hotel property are usually found in a complete marketing prospectus which, depending on the scale of the project, may be prepared by an investment banking firm, or a real estate brokerage firm.

The contents of this package will include summary information including: complete property description, engineering reports, pro-forma income statements, a complete outline of management functions and successes and detail on financing terms if offered by the seller.

Again, the most critical part of this package for evaluation, next to the management of the property is the accountant's pro-forma income statements. They hold the facts that are critical to evaluating how the investment will perform in the future.

In the end, for a seller of a hotel property, the goal will be to negotiate the highest value for the property and therefore preserve value for its present owners.

The hotel investors of the '90s will be looking to sellers to provide this kind of information. In order to be successful, the sellers of hotel properties in the '90s will be able to present their properties to a wider group of potential investors if this type of preparation is done prior to offering a hotel for sale.

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