Hotel Valuation- Global Perspective

In my previous column (insert date) I showed the development of a projection of revenue, expense and Net Income for five regions of the world- South America, China, Europe, India and United States. These projections were made under the assumption that the hotel would be a 200-room Marriott type hotel with identical REVPARs for each of the five regions.

The resulting income for these five regions is as follows-

China- $5,086,000

Europe- $5,272,000

India- $9,602,000

South America $4,904,000

United States- $6,351,000

India leads the list showing a net income of $9,602,000 which is significantly higher than the other regions. South America is the lowest at $4,904,000. Even if you deduct an incentive management fee for the United States it would still be the second highest at $6,351,000. At least from a profit point of view, these results show why India has been getting some much attention from hotel companies looking to do business there. On the other hand, even with the growth of Brazil, South America is not as active in new development compared to India, United States and China.

Let's take these projections of Net Income and convert them into value estimates based on the valuation parameters utilized in their local regions. Hotel owners, operators, lenders and investors around the globe utilize the income approach for valuing hotels. In most parts of the world, hotel acquisitions are typically financed with mortgage and equity capital which justifies the use of the mortgage equity valuation methodology.

Using these 10-year projections coupled with the mortgage equity parameters utilized in these regions, will produce the value of the proposed Marriott assuming it was located in these areas.

The following table shows the mortgage-equity parameters currently used in each region for valuing a hotel similar to the proposed Marriott.

	South America	China	Europe	India	USA
Loan to Value	55%	55%	65%	60%	70%
Amortization (Years)	10	10	20	10	25
Mort. Term	10	10	10	10	10
Interest	9.0%	7.25%	6.0%	11.5%	7.0%
Terminal	10.0%	8.5%	7.0%	9.0%	11.5%
Transaction Cost	2.0%	1.5%	1.5%	1.0%	2.0%
Equity Yield	18.0%	16.0%	17.0%	18.0%	18.0%
Value ($000)	$41,100	$51,700	$62,600	$86,500	$63,000
Val/Room	$205,000	$259,000	$313,000	$432,000	$315,000
Total Property Yield	14.9%	12.0%	11.6%	16.0%	11.4%
4th Yr. NOI	$4,972	$5,041	$5,280	$9,546	$6,351
NOI %	23.6%	24.9%	24.7%	38.8%	30.1%
Incentive Mgmt Fee	Yes	Yes	Yes	Yes	No

The Loan-to-Value ratio varies from a low of 55% for South America and China, to a high of 70% for the United States. Lenders in the United States tend to offer larger mortgages than other parts of the world.

The Amortization ranges from 10 years for South America, China and India, to 20 years for Europe and 25 years for the United States. Amortization- in years tends to be lower in regions where inflation rates are higher because the lender wants to be paid off quicker because the value of their money is eroding due to inflation.

Interest rates are also tied to inflation. South America has a 9% interest rate and India has 11.5%. Europe has the lowest rate at 6%, with the United States at 7% and China at 7.25%

Terminal Capitalization Rates range from a low of 7.0% for Europe to a high of 11.5% for the United States. These rates tend to project the rate of return environment 10-years from now.

The transaction costs range from 1% in India to 2% in South America and the United States.

The Equity Yields show a fairly tight range from a low of 16% for China to a high of 18% for South America, India and United States.

Using these mortgage equity parameters and the individually projected Net Incomes, produced values that ranged from ($000) a low of $41,100 for South America to a high of $86,500 for India. The United States was second highest with $63,000. China was second lowest with a value of $51,700. Europe was in the middle with a value of $62,600, almost equal to the U.S.

The Total Property Yields (overall discount rate) coupled with the 4th Year NOI tell the relationship between the projection of Income and Expense and the Mortgage Equity Parameters. While the total property yield for India at 16.0% was significantly higher than the other regions, its 4th Year NOI at ($000) $9,546 was sufficiently high to give India the top spot for overall value. The total property yield for South America was the second highest at 14.9%, but coupled with the lowest 4th Year NOI at $4,972, produced the lowest value. The three countries with 10-year amortization had the highest total property yields.

The NOI % shows the Net Operating Income as a percentage of total revenue. India had the highest at 8.8%.

The Incentive Management Fee Line shows that the United States was the only region where the Incentive Management Fee was included in the Equity Yield as opposed to specifically showing the expense in the income and expense statement.

This table illustrates the valuation of a proposed Marriott hotel in five regions of the world using typical mortgage equity parameters at a given point in time. These specific inputs are likely to change and should not be relied upon when valuing a hotel. They demonstrate how a hotel can be valued in different economic environments using the mortgage equity valuation methodology.