



HOTEL LIFE EXPECTANCY

You're driving down a street and you notice two hotels. Both appear neat, clean and orderly. One has exterior corridors, a flat roof that reveals the air-conditioning fan units, an out-of-date Tudor-style brick exterior, a plain, square swimming pool, and a small guestroom converted to a fitness room. The other has interior corridors, a front desk providing entrance security, a mansard roof that conceals the air-conditioning equipment, art deco exterior decor, a free-form swimming pool with water falls and slide, and a well-designed health club.

It shouldn't surprise you that the modern hotel captures more than its fair share of occupancy and operates at a higher a.d.r. than the older property. Revenue loss stemming from out-of-date appearance and inferior facilities is functional obsolescence. Hotel appraisers recognize that obsolescence reduces income potential and value.

The life cycle of most hotels is characterized by rapid growth in occupancy and net income during the first five to 10 years. Then a hotel stabilizes, and net income remains fairly level from eight to 15 years after opening.

“Hoteliers may be able to do something about functional obsolescence. But external obsolescence—the social and economic context of a hotel—is beyond a hotelier's control.”

After that, net income begins to decline as the property nears the end of its economic life and its income-generating capability decreases.

Studies show that a hotel's economic life averages about 40 years, but the standard deviation is, believe it or not, 20 years. That means the risk of hotel investing is related to not knowing whether the economic benefits will last up to 60 years or end in 20.

Various factors affect the economic life of a lodging facility. Functional obsolescence can be key to hotel value decline.

In the above example, it's likely that the first hotel is 15 years old and in its decline, while the second is brand-new. It's also possible that both hotels are 15 years old, but the second just underwent a major renovation.

Functional obsolescence is curable. Most hotels have a continuous program of furniture replacement and decor updating to keep functional obsolescence in check during a facility's initial years. But the first hotel hasn't undergone the massive renovation generally required between the 15th and 20th years.

Thousands of older hotels are in the declining phase of their life cycles. Those with good locations and sound structures are prime candidates for the type of massive overhaul that will add years to their life. Others will eventually lose their national affiliation, deteriorate in appearance and go out of business.

External obsolescence is a loss in income and value resulting from outside factors. Examples include population shifts and declining neighborhoods, changes in traffic patterns, economic adversity among local businesses and hotel room oversupply. Unlike functional obsolescence, external obsolescence is generally incurable because a hotel owner has no control over it.

Taking the broader view, several new developments are likely to reduce the use of lodging in the long run.

Video communication is apt to have a devastating effect on commercial hotels. The ability to sit in one's office and conduct meetings, both verbally and visually, with others throughout the world will eliminate many trips. Even educational and training programs can run through this medium.

In addition, faster transportation, such as suborbital flights, will make every point throughout the world a one-day turnaround. I predict that in less than 20 years, business people will be able to board a plane in New York, reach Tokyo in two hours, hold a three-hour meeting and return the same day. That eliminates the need for hotel accommodations.

On the flip side, technology will give people more time to travel, greatly benefiting lodging facilities geared toward the leisure traveler. **LH**

STEPHEN RUSHMORE, MAI, CHA, IS PRESIDENT OF HOSPITALITY VALUATION SERVICES OF MINEOLA, NY; SAN FRANCISCO AND LONDON. THE FIRM IS THE LARGEST ORGANIZATION SPECIALIZING IN THE VALUATION OF HOTELS AND MOTELS.