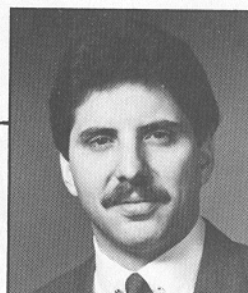


# RUSHMORE AND ARASI



**D**eveloping a new hotel or motel typically requires a feasibility study to verify market demand and to prove the project is economically viable. Selecting the right firm to perform this study is an important decision which can affect the ultimate success of the venture.

Most of the feasibility studies made for lodging facilities are prepared either by accounting firms or real estate consulting organizations. Some firms are highly qualified, producing well-researched and documented conclusions. Others tend to turn out cookie-cutter-type studies with little originality and too many boiler-plate findings. To assist in selecting a feasibility firm, we have developed the following checklist of questions to ask and things to consider.

The term feasibility study as used by most firms is a misnomer. Their reports are merely market studies with financial projections which do not consider whether the bottom-line net income is adequate to support the total project cost. As a result, many studies which they conclude are "market feasible," in that a reasonable occupancy level is anticipated, fail to generate sufficient profit to support debt service based on total project cost. This obvious shortcoming is solved by the firms which have the expertise to estimate construction and development expenses and relate these costs to economic value. A true feasibility study, therefore, proves that the economic value is greater than the total project cost.

Most lending institutions and investors ultimately require a true feasibility study, where in addition to justifying the market demand and financial

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## SELECTING THE FIRM TO PREPARE YOUR FEASIBILITY STUDY

forecast, the project financing, development costs and economic value are thoroughly documented. Those firms which offer an MAI-certified appraisal included within their market studies have the most complete and up-to-date package. Since nearly every lender needs an MAI appraisal to justify a loan-to-value ratio, the combined market study and appraisal saves the developer time, money and the duplication of professional effort.

### Qualifying the personnel

No matter how noted a firm might be, it is the individuals employed by the firm who listen to your ideas and concepts, visit the site, conduct the fieldwork, research the demand, evaluate competition and come to a conclusion as to feasibility. When selecting a firm to make your study, the final product will be no better than the persons who do the work — particularly the individual who conducts the on-site research. With this in mind:

Ask to meet and interview the person who will perform the fieldwork and any supervisor assisting in formulating and/or reviewing the final conclusion. Get a copy of their resumes. Since a hotel is a highly specialized business venture, each individual should have the following minimum qualifications:

- a. Degree from an accredited

- hotel management school;
- b. Actual operating experience in the hospitality industry;
- c. Post-graduate courses in real estate principles and practices, real estate appraisal and real estate finance;
- d. Experience in evaluating a wide range of different types of lodging facilities, both proposed and existing.

Since the lodging industry is constantly changing, only the true specialists who concentrate all their efforts within this field are the best suited to make these highly complex market studies and appraisals. Generalists who devote time to other types of real estate have difficulty staying current with industry data, statistics and trends. True experts publish widely in professional journals and are active lecturers.

### Evaluate the final product

Before retaining a firm to perform a feasibility study, ask for a sample report to evaluate its content, approach to the problem and comprehensiveness. You should compare studies from several different firms in order to properly judge quality and completeness. Some of the areas of consideration include:

- Does the study document every number and conclusion with a logical rationale, or are recommendations seemingly pulled out of thin air?
- Are forecasts of income and expenses made in accordance with the uniform system of accounts for hotels? Do they contain a complete accounting of all normal expenses, including management fees, property taxes, insurance and reserve for replacement? Are they made in inflated dollars?
- Is the construction cost and

*continued*

financing requirements quantified?

- Does the study support occupancy and average rate estimates by citing actual operating data from nearby competitive hostelrys?
- Hotel feasibility studies are often distributed to potential investors and lenders throughout the world. Descriptions of the site, proposed improvements, neighborhood and competition should be highly descriptive and augmented with a variety of graphics and photographs.
- Is the study a cookie-cutter-type report, or does it contain unique approaches that set it apart from the ordinary mass-produced varieties? Areas that demonstrate specialized competence include:
  - a. Breakeven analysis
  - b. Use of full supporting schedules
  - c. Mortgage interest rate regression evaluations
  - d. 10-year IRR analysis of debt, equity and total property components
  - e. Spatial allocations on a square footage basis
  - f. Usage of RGI and RAI indicators.

Once a firm has been selected based on the quality of personnel and the final project, you should ask for a written proposal that outlines the scope of the assignment, fees and timing. It is best to have the study completed in a series of steps or stages which allows for periodic reviews to determine whether an adequate level of feasibility exists to continue onward with further research. In most instances, a qualified hotel consultant should be able to ascertain an unfeasible project within approximately five days after starting fieldwork. A full feasibility study should take approximately 30 to 45 days to complete. A firm that can produce a finished report in

significantly less time is apt to be boiler-plate much of the findings and conclusions. Always set firm completion deadlines.

Fees for feasibility work depends on the scope and nature of the assignment. Always ask for an all-inclusive fee which includes professional and computer time, report production costs and miscellaneous expenses such as telephone, postage and photo copying. It is best, however, to reimburse out-of-pocket travel expenses based on actual receipted invoices rather than a lump-sum estimate. Beware of firms that bill travel expenses at a rate (10-20 percent) higher than their actual cost. Also, expect to pay a sizable retainer fee before work commences.

You must also determine what are the normal limiting conditions. Many accounting firms will not allow their reports to be used in any form of public or private offerings. This can seriously impair the usability of the study.

Above all, you should feel comfortable with the people performing your feasibility study, particularly the ones who do the actual fieldwork and analysis. Beware of firms that isolate or limit your interaction with any of the personnel working on the study. Starting with your first meeting through every meeting thereafter, *all* members involved with the project should be in attendance. This personal interaction is necessary in order for everyone to gain a first-hand flavor for your concepts and ideas and to share the team's combined knowledge, experience and insights.

A well-prepared hotel feasibility study and appraisal can cost from \$15,000 to \$50,000, depending on the scope of the assignment. This expense is generally well worth the price if the findings and recommendations are accurate and well-founded. By looking beyond a firm's prestige and concentration on the abilities of the actual personnel performing your study, the criteria set forth in this column will greatly assist in selecting the right firm to prepare your feasibility study.

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