

## The Truth Behind Hotel Feasibility Studies

Over the years hotel consultants have been blamed for hotel feasibility studies that seem to have missed their mark and came to conclusions that did not seem to reflect reality. As a consultant and appraiser who has worked on thousands of my own studies and have reviewed hundreds of studies prepared by others, I have found that in many instances users of these studies have unrealistic expectations as to what the results actually mean and how external influences can skew the a study's findings. This article was written to clear up some of the misconceptions concerning hotel feasibility studies.

Hotel feasibility studies are used to determine whether a proposed hotel will be economically viable when it becomes operational. It typically consists of a market study which measures the local supply and demand of existing and proposed hotel facilities. This analysis results in a projection of occupancy and average rate for the subject property. The next step is a forecast of income and expense showing the hotel's profit potential going into the future. The last step is determining the hotel's economic value based on the projected profit and the cost of capital. If the hotel's economic value is greater than its total development cost then the hotel is feasibility. If on the other hand the hotel development cost is more than its economic value, the hotel is not economically viable.

A hotel feasibility study is typically prepared at some point prior to the commencement of construction. If it takes two years of development time to build the hotel plus another two to three years for it to reach a stabilized operating level after opening, that means there is a 4 to 5 year period of time between the completion of the feasibility study and point in time where a comparison is made between the projections contained in the study and what actually happens. To criticize a hotel consultant for not knowing exactly what is going to happen five years from now is clearly an unfounded expectation. Let me provide you some examples of how unrealistic it is to look for a high level of accuracy in making these long-term hotel projections. Do you think that anyone has an accurate projection of what the Dow Jones Average will be five years from now? How about one year from now? How about tomorrow? Do you have any idea of what your house will be worth two years from now? Can you accurately predict the weather in your home town 20 days from now? The answer to all these questions is that you can project, you can estimate and you can guess- but the looking into the future is always subject to unforeseen events that can render your projection incorrect. Did you anticipate the events of 9/11 that radically changed travel and the hotel business in New York City? Did you anticipate the financial meltdown in 2008 which caused the stock market and housing values to decline? Did weather forecasters predict that hurricane Irene would dump record levels of rain in Vermont? These events were unanticipated and therefore any projection of hotel feasibility prior to these events would have to be re-evaluated with a new set of economic factors.

Users of hotel feasibility studies need to understand that the accuracy of the findings start to deteriorate the day the study is issued. Depending on the magnitude of the events that impact any of a number of factors contained in the study, the validity of the study degrades. Some of the major factors that will render a hotel feasibility study obsolete is- a significant economic change such as what was described above and unexpected increase in new hotel supply that was not anticipated as of the date of the study. The bottom line is that hotel markets, the economy, travel trends and so forth are constantly evolving and hotel feasibility studies are not static, long-term predictions but merely an estimate of the future based only on the facts existing today.

Hotel feasibility studies should be continuously updated throughout the development process. We recommend an update be made at least every six months and even more often if there is an unanticipated event that might affect the study's projections and recommendations.

HVS has been on the cutting edge in developing software for performing hotel feasibility studies and appraisals. We have just released Hotel Valuation Software version 3.0. If you send me an e-mail and mentioned you read my Lodging Hospitality column, I will tell you how to obtain a copy at a 50% discount. [srushmore@hvs.com](mailto:srushmore@hvs.com)