

INVESTMENT TODAY



WHO NEEDS AN ASSET MANAGER?

The lodging buzzword of the 1990s must be *asset management*. Many hotel companies are offering it. Most hotel owners probably need it. But very few people really know what it is.

In general terms, hotel asset management is the service of assisting hotel owners in realizing their investment goals. Asset managers act as an owner's agent or representative to insure that a hotel is acquired for a reasonable price; is then operated properly during the period of ownership; and is ultimately disposed of at an appropriate time and price. Asset management can either be provided by an in-house hotel group as is found at a number of major hotel investors or it can be contracted for from third-party hotel asset managers.

Asset management in the hotel industry is a fairly recent phenomenon. Prior to the mid 1980s, hotel owners generally did not use this type of service. Why now? The answer is simple: Hotel ownership has become extremely complicated and sophisticated. To invest successfully in hotels, you must understand the intricacies of concepts such as yield management, call accounting, TQM, central reservations, reserve for replacement and owner's priority. Most passive hotel investors, particularly financial institutions, simply do not possess this comprehensive level of ownership competence.

So what are you paying a hotel management company to do? Good question. In an ideal world, your management company should provide most of the services that asset managers do. It has become very evident, however, that the motivations of many hotel management companies are not always the same as those of hotel owners.

For example, most management companies derive a significant amount of their fee as a percentage of revenue, rather than net income. This structure creates an incentive to maximize revenue by increasing expenditures such as the level of service, marketing and property improvements. Net income suffers as the management company collects an inflated management fee and the owner faces huge deficits. A skilled hotel asset manager will closely monitor this type of situation and work out an economic balance between the parties.

What are some of the skills needed to provide comprehensive hotel asset management services? Hotel management experience is an important prerequisite, but asset managers need actual

hotel ownership experience as well. The asset manager must think like an owner to fully appreciate concepts such as downsizing, deferring maintenance, disputing property tax assessments, prepackaged bankruptcies and increasing profitability through growth in market share. These concepts, while alien to many hotel companies, are essential for ownership survival in difficult markets.

The combination of operational and ownership expertise can be difficult to find. In addition, be on the lookout for potential conflicts of interest. For example, hotel management companies acting as asset managers seem to be overly critical as they angle for a shot as managers. Investment bankers and hotel brokers acting as asset managers seem to always be looking for a buyer to collect a huge transaction fee. Accounting firms seem to always be looking to expand their role by offering added services such as audits, valuations and expensive consulting.

Over the past several years, I have evaluated a number of hotel asset managers and found that large insurance companies appear to offer both the operational and ownership expertise without the potential for a conflict of interest. For example, Thomas Engel of Equitable Real Estate Investment Management's Hospitality Asset Management Group and Allen Ostroff of the Prudential Property Company supervise the ownership and operation of a number of hotels owned by their parent company as well as third parties. Because their organizations are so huge, they can call upon a wide range of in-house experts such as acquisition specialists, engineers, attorneys, auditors, property tax reps and disposition experts. In addition, since they have supervised a number of hotel companies over the years, they thoroughly understand each operator's unique strengths and weaknesses. This level of skill and experience is obviously an essential element of successful hotel ownership.

Unless you are an owner-operator, you probably need the services of a hotel asset manager. Try to structure a fee based on the property's market value, so the asset manager has an ownership type of incentive to maximize long-term revenue and minimize long-term expenses while at the same time enhancing the value of the hotel. **LH**

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