Choosing a location
What you need to know

The key principles to choosing a profitable location

Benchmarking KPI's for your hotel business

Developed markets or emerging markets

Assessing opportunities

What generates demand

One of the most challenging aspects of hotel investment is the selection of the most favourable and profitable site for your investment. Taking into account that a successful hotel needs to achieve at least a 65-75% year round occupancy, a winning location must provide the opportunities to fill rooms in both the weekends and the slower weekdays in Winter.

It may be enticing to consider building next to a major highway or a tourism site but in order to achieve this kind of occupancy there is a range of determinants that require consideration. These include public service infrastructure, road accessibility, corporate and leisure demand initiators, adjacent hotel stock and the consequential demand along with the economic outlook for travel development in the community.

The hotel market in EMEA has experienced significant growth in occupancy and average daily rates over the years and despite a recent softening in the market due to supply increases and reduced growth, hotel investment remains an option for attractive returns.

The key principles to choosing a profitable hotel location

Demand generators are the most important consideration to selecting a successful hotel location

If demand generators move away from a hotel, the product left behind becomes obsolete. Demand generators can be categorized into long term **corporate demand generators** and **leisure demand generators.**

Long term corporate demand generators

The corporate sector is vital to ensuring reliable and constant demand for hotel rooms. Business travel takes place during the week where salespeople, suppliers and clients often seek accommodation close to their corporate offices or meeting locations.

It is also important to consider the current and future competition in a particular geographical area, a market can go from performing well to oversupply in a short space of time.

Leisure demand generators

Leisure demand generators come into play when the location is within the vicinity of tourism sites, shopping malls, theatres and restaurants. These attractions ensure demand remains high not just on the weekends but also during weekdays.

Other factors to consider include proximity to public service infrastructure such as airports and train stations, major arterial routes, conference centres, universities and hospitals.

Sustainable occupancy rate

To achieve a sustainable occupancy rate you will need strong corporate demand that provides consistent annual revenue streams. The leisure sector represents only 50% of the demand in a robust hotel market so a conservative approach is advised. You should be relying on this segment to generate occupancy during summer months and weekends.

Tip: As part of your due diligence, you have to dig down and understand who is going to generate room demand for your hotel.

Put yourself in the customer's shoes – would you stay here?

Poll the market's demand generators – by just walking into a company in the immediate area you can reveal a lot about it, ask them 'Would your people stay in this location?' Hotel operators need to focus on building or acquiring in the midst of the right demand generators for the hotel in question.

How to achieve 65-75% year round occupancy

Consistent and reliable demand from the corporate sector on a year round basis coupled with a sturdy supply of leisure customers to fill in summer, shoulder and off-season leisure weekends.

Determining existing demand

A developer should not fall into the trap of expecting to create demand for rooms when building a hotel; Hotels service existing demand they do not create it.

When you are determining market demand in the desired location, you should interact with local businesses and ascertain the level of business they generate. Summarise existing tourist attractions based on the number of visits they attract and assess the results of your competitor set. If overall demand is subdued then the success of a new hotel may be restrained.

The right benchmarking KPI's for your hotel business

Average rate index (ARI)

This measures an individual hotels' average daily rate (ADR) result versus the ADR in the competitive set or market

$$= \frac{\textbf{Hotel ADR}}{\textbf{Market ADR}}$$

Market penetration index (MPI)

This index tells you what occupancy your property has achieved in relation to the market occupancy

$$= \frac{\textbf{Hotel occupancy}}{\textbf{Comp set occupancy}}$$

Fair market share

This is an indicator of your hotel's overall performance compared to your competitor set in your market

$$= \frac{\textbf{Total number of rooms}}{\textbf{Total number of rooms in your competitor set}}$$

Actual share

This differs slightly from Fair Market Share in that this is what you have actually achieved – the amount of rooms actually sold rather than the percentage of the total market.

$$= \frac{\textbf{Your number of rooms sold}}{\textbf{Total number of rooms sold}}$$

If your hotel is not achieving fair market share, has a low ADR compared to the market or poor market penetration you may need to consider refurbishing to ensure your hotel matches the standards and offerings of your competitor set. Undertake organized research of your competitor's facilities to understand where discrepancies exist.

Research, research and more research!

Investing in a hotel location involves different considerations than it did a decade ago. Brand loyalty now plays a major part in the customer's decision about which hotel to frequent. Certain considerations do not change; this includes access, visibility, an area's growth potential, proximity to complementary retail and a ready supply of potential customers. However, the difference between a good site and a great one often depends on the intangibles.

Research into intangibles should include factors such as:

- Soil condition
- Is the site ready for construction
- Does its foundations support the buildings weight load
- Is the site ready for development permit approval

A great site is one that is flat, zoned and does not need a lot work; construction workers can start building and avoid having to wait for approvals and pay carrying costs.

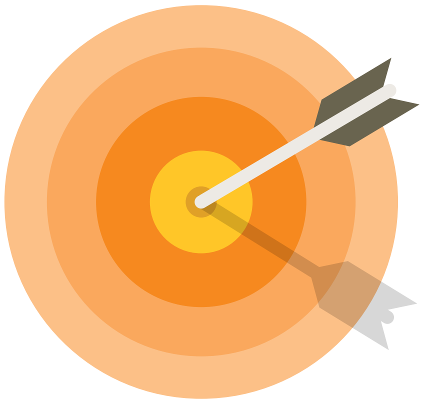
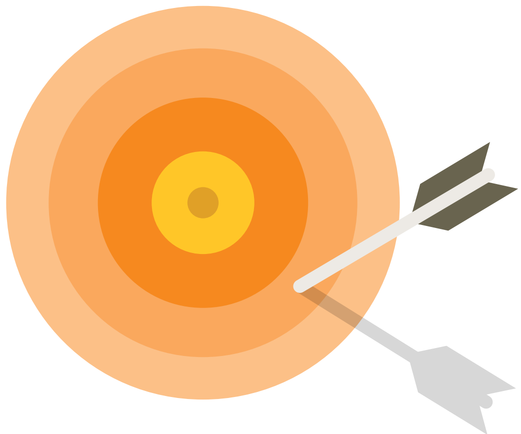
There is a wealth of information located at the city council. You will find everything you need to know about current projects and whether they are pending or approved, helping you to avoid a hotel with empty rooms due to oversupply.

Rule of thumb: start with the market first, if you do not believe you can fill Monday to Thursday night at a strong rate then you should consider your options.

Feasibility studies – meeting the needs of your target audience

Consider hiring professional expertise for a detailed analysis of the location. A feasibility study will ascertain the economic feasibility and suitability of a location for your hotel investment. Experts can provide ideal decision basis for the development, financing or operation of a hotel project. Services can include site and market analysis, assessment of the general suitability of the location and market for a hotel and return on investment calculations. Remember, a feasibility can provide insight you may not have considered and as a result, assist in avoiding a less than ideal scenario. Conversely, a feasibility study can provide reassurance, instill confidence in potential investors and lenders.

Choosing your market
developed or emerging?

Factors	Developed markets	Emerging markets
	 Primary markets such as Berlin, Paris, Dubai and secondary markets such as Cologne and Taupo	 Tertiary markets-communities of less than 20,000 people
Size and depth of demand generators	Long term occupancy rates are buoyed by a greater diversity and quantity of demand generators	Constraints on the occupancy rates and ADR due to a smaller number and less diversified demand generators
Supply factors	Finding optimal sites where no development is taking place could be challenging	Greater availability but more caution and due diligence is required to ensure sites are suitable for purpose
Barriers to entry	High due to expensive land and construction costs	Low due to more affordable land
Project risk	Supply and demand inequity leading to oversupply	Considered higher risk due to demand generator constraints

Leased land
beware of the drawbacks

You may have found the site that fits your development needs however the desired site is either not for sale or is available at a price point outside of your development budget. While purchasing the land may not be an option, leasing the land may work to your advantage directing financial resources towards construction.

The development of a ground lease is a negotiated process that should reflect the needs and expectations of the participants as well as market conditions. Below are some drawbacks that you need to be aware of before embarking on this course of action:

Constrained cost savings in secondary markets

Land is more affordable in these markets and therefore leasing the land would not necessary reduce capital costs.

Access to finance

Banks do not look favorably at hotel investments built on leased land. This has the possibility of causing complexities further down the line when you want to sell.

Return on investment

Increasing land values mean access to capital gains; this in turn generates incremental value in the future. Hotels built on leased land will not have access to the capital gains associated with land values.

Market conditions

A fixed rental ground lease is not responsive to current market activity. Should the business go through a decline the fixed payment becomes a proportionally increased liability to the development.

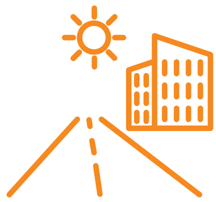
Start-up period

The hotel will have a startup period until it reaches a level of financial stabilization. If the ground lease does not allow for the initial financial constraints, it may not reach stabilization within the required period.

Assessing opportunities in certain markets

How do you decide which is the better option – a hotel near a major arterial route in a smaller market or a city hotel in a large market?

The answer to this depends on financial resources and the type of hotel planned. Trying to make a project work in the wrong site is a common mistake made by developers.

	Primary market City location	**Tertiary market** Highway location
		
Demand generators	City locations generally provide better access to both corporate and leisure demand generators	Provides good visibility potentially leading to high occupancy. Winter months could put pressure on the occupancy rates if traffic falls
Costs	Hotel operators are now competing with commercial developers so construction and land costs tend to be excessive in CBD locations	Land costs are more affordable leading on to lower construction costs
Occupancy and average daily rate (ADR)	Supply and demand are important factors in a large market. If the balance becomes unstable with supply exceeding demand this can negatively impact occupancy and average rates	In general the ADR would be lower however in high peak demand the large markets will contribute to an increase in the ADR
Site selection	With a strong pipeline of planned hotels in the major cities it can be difficult to source optimal sites	Greater availability but more caution and due diligence is required to ensure sites are suitable for purpose

Considerations for the future location selection

Due to the strong growth of the hotel sector specifically in recent years, there is an increased need from hotel investors to understand how guests select hotels and what the decision-making factors are that prevail. The hotel industry is very dynamic, incorporating properties that fit specific market needs. This includes economy, mid-range, luxury, boutique and lifestyle hotels aimed at specific target markets.

While the corporate and leisure demand generators will most likely remain similar in the near future, improved technology and construction methods have made it more economical to build and operate a hotel compared to a decade ago.

Now more than ever optimal locations in primary and secondary markets are already developed. This has led to investors looking for opportunities in the smaller communities and towns where viable site options are available to meet an investor's needs. Ultimately providing high occupancy and average daily rates and attractive returns.

Choice Hotels: optimal locations through in-depth research and expert knowledge from our broker and economic development teams

Choice Hotels conducts extensive due diligence when reviewing and selecting hotel sites for its hotel portfolio. It conducts a rigorous market prioritization summary that includes a detailed review of each market's population, share of rooms and Choice hotels in that market along with the performance of those properties. Choice then draws upon its specialized expertise including ratings from our sales, franchise services and development managers, assigns an overall value to each market and creates a market priority list.

Its development managers then work with brokers and economic development teams to determine the most optimal opportunities available for franchisees. While the Choice Hotels' market opportunity evaluation process does not eliminate the need for you to undertake your own due diligence supporting project viability, it does minimize the risk of developers spending time and effort in markets where development opportunities are limited.

Choice Hotels EMEA is one of the largest franchisors in the region with more than 380 properties currently open or under development. The Choice family of hotel brands has over 7,100 hotels worldwide and provides business and leisure travellers with a range of boutique, high quality mid-scale, and economy accommodation options.

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