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Strong structures, satisfied spenders: **Trevor Ward** and **David Harper** discuss the how-to's of maximising returns from a hotel investment

Hotels are often seen as a necessary first step in attracting international investment into an under-developed area. Without a decent base to stay, international investors are less likely to come to the country to discuss other business opportunities. In recent years there has been a strong influx of new hotel developments across Africa as inward investment in hospitality property has grown.

The fundamental question is, then, how to ensure that any new hotel being built maximises its potential and adequately rewards the investors.

Ensure the basics are right

Ideally, when first looking at a project you will need to ensure the basics are right.

They include:

- **The right product**

Is it the right product in the right place? There is strong demand for luxury resorts in certain parts of Africa whilst in other areas mid-market business or budget hotels are the optimum type of hotel operation. Creating the right property (including quality, size and ancillary facilities) is one of the most important

steps to ensuring that you can maximise your investment returns.

W Hospitality Group were asked to advise on a new hotel development in West Africa and, because of the nature of the market, they advised incorporating a high proportion of suites into the branded hotel that usually had no suites. This advice was received at an early enough stage to be incorporated into the design. There is therefore no substitute for good professional advice early on. The cost of an initial feasibility study is never wasted.

- **The right brand**

Appointing an international operator to manage a hotel can have a significant impact on the returns you make from your investment. In the initial development phase, this decision will affect an investor's ability to secure funding and also the likely cost of securing it.

Whilst the hotel is trading, international operators can usually improve performance, increasing revenue production, whilst also using their size to generate cost savings, thereby improving the owner's return. In addition, when the hotel is finally sold it can usually attract a higher multiple of earnings if it is internationally branded (and therefore a

higher price).

However, if it is "the wrong brand," or in the "wrong structure," it could have a negative impact on operational earnings potential and the capital value of the asset.

- **Right structure**

If a brand is considered the best option for a hotel then consideration must be made whether to structure the partnership through a lease, a management agreement or through a franchise agreement. The ideal choice will depend upon who the investor is; their long term strategy and the prevailing market conditions.

The devil is definitely in the detail of such arrangements. It is essential that professional advice is taken at this stage. If care is not taken in firstly choosing the most appropriate structure, and then over every clause contained in any agreement, this could have a direct impact on both the income earned and on the price achieved on sale.

Prepare at the outset for the exit

A wise investor plans for the time to sell the hotel from the very beginning. If you know what you want to do in the first instance you can ensure that it is built into



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your planning, as long-term holds have different strategies than medium-term holds or early disposals.

Ensure trading is optimised throughout the holding period

However long you intend to own the hotel it is important that trading should be optimised. Note the use of the word “optimised” – it is deliberately not “maximised,” though of course in many instances these words will be effectively interchangeable. However, in certain circumstances, maximisation of income may be detrimental to long term earnings and/or capital value.

Assuming that the hotel is not being operated by the owner, it usually proves prudent to employ an “asset manager” to liaise with the operating company, to ensure the owner’s interests are uppermost in the manager’s thoughts at all times. The asset manager will review performance, budgets, marketing plans, maintenance schedules and capital investment programs to ensure everything is being done to enhance the owner’s returns.

It is important not to allow basic repairs and maintenance to be neglected.

If the property is not kept in good repair it has an impact on both trading and capital value, and that impact is always greater than the short term savings generated by under-investing in the fabric of the hotel.

Ensure a smooth exit

When disposing of the hotel, an experienced specialist hotel agent will be best placed to secure a quicker sale at the best possible price. The agent must be competent in the specific location, with the type of property and with the type of structure being sold. Generally the best agents will only work on a sole agency basis to ensure they can fully control the disposal process, thereby enhancing the chances of a successful transaction.

It will also be important that the property is marketed to the correct people. There is no point, for example, in advertising a property to international buyers when non-locals cannot own property in that country. In addition, certain types of properties and structures attract certain types of buyers.

There are times when it is best to speak informally to one or two buyers in an off-market scenario to best complete a sale. Your agent will advise on this, on a case-by-case basis.

There is one final point to mention. If advising on hotel transactions over the last fifteen years has taught us nothing else, it is essential that all the due diligence paperwork is collated ahead of going to market. Nothing annoys a keen potential buyer with an interest in a possible transaction more than having to wait for the paperwork to review. It is imperative to the success of a transaction to be able to follow up such interest immediately in order to build the momentum in the transaction so it can be pushed through to a successful conclusion.

Conclusion

In summary, if you are to maximise the returns you receive from your hotel investment, you need to ensure you get the basics right in the first place, ensure that trading is optimised throughout the holding period, and ensure that the best sales price is attained by making the exit as smooth and as professional as possible. **▲**

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