HVS

Comparing Same Hotel Across Five Regions

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I always wondered how a hotel would operate financially if it were located in different parts of the world. To demonstrate these differences and show the impact on the net income, I developed the following side-by-side comparison of the revenue and expense for a proposed 200-room Marriott type hotel, assuming it was located in the following five regions: China, Europe, India, South America and the U.S.

Let's assume the projected occupancy and average rate are the same in each market, which will produce identical rooms revenue. The rest of the revenue and expense items will be projected by my local HVS partners based on how this Marriott hotel would be designed and operated in that particular region. For example, in India, a Marriott hotel would typically have significantly more food, beverage and banquet outlets thereby generating more food and beverage revenue than a Marriott hotel in the U.S.

Click here to download the detailed chart of revenue and expense showing the side-by-side comparison for the five regions as of the Marriott's fourth year of operation.

Base on the financial statements set forth, it is apparent there are many similarities and differences in the mode of operation and the resulting impact on revenues and expenses for hotels in various parts of the world. Let's take a closer look.

Rooms Revenue
The underlying assumption for all five markets is the subject property is a 200-room Marriott hotel in its fourth year of operation in 2014. The occupancy is 71% and the average rate is $250, which produces rooms revenue of $12,958,000.

Food and Beverage Revenue
India shows the highest food & beverage revenue of $9,517,000 compared to the lowest, with China at $6,312,000. Indian hotels typically have extensive food and beverage outlets — usually several restaurants and extensive banquet rooms. Some of the best restaurants in India are located in hotels. The large Indian weddings are often held in hotel banquet rooms. Travelers also appreciate dining in a hotel since driving in the large cities can be challenging and time consuming. Hotels in China also attract banquet business, but their restaurants don't cater to as many locals as Indian hotels. The European Marriott is second to India in food & beverage revenue with a volume of $7,390,000. Locals in Europe will often frequent hotel restaurants and utilize their banquet facilities. South American and U.S. hotels derive similar levels of f&b revenue.

Telephone Revenue
India and South America show the highest telephone revenue with a volume of $630,000 and $466,000 respectively. India hotels derive significant revenue from Internet charges, which are very expensive in this region. The U.S. telephone revenue is $96,000 and Europe is a low $22,000. China does not separately account for telephone revenue but puts it in Other Income.

Rentals and Other Income
South America and the U.S. have the highest rentals and other Income at $932,000 and $829,000 respectively. China is the lowest at $371,000.

Spa Revenue
India's spa revenue is the highest at $950,000. Upscale Indian hotels typically have extensive spa facilities that cater to both hotel guests and the local community. Spa revenue for China, Europe and the U.S. ranged from $241,000 to $413,000. South America does not show spa revenue because hotels of this size typically have very

Summary

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small spas and the income is insignificant.

Garage Revenue

A hotel in China typically has garage revenue and for this property it was estimated at $307,000. The other regions did not specifically include garage revenue, but it could be included in other income.

Total Revenue

The resulting total revenue ranges from $24,560,000 for India down to $20,361,000 for China. Europe, South America and the U.S. are similar at approximately $21,000,000.

Rooms Department Expense

Major financial operating differences among the different regions become apparent when the rooms department expense percentage is compared. India has the lowest at 10.4% and Europe is the highest at 30%. China, South America and the U.S. are similar at around 22%. India's extremely low labor cost is the primary reason why the rooms department expense is so low. Indian hotels appear overstaffed, and usually provide a high level of service. However, wages are extremely low there, which results in a highly profitable department. Europe's labor costs are very high. Unions, government regulations, vacations and benefits, high cost of health care and social security contribute to staffing costs and a high rooms department expense.

Food and Beverage Department Expense

Again, India with its low labor cost has a f&b departmental expense ratio of 45.5%. The other regions of the world are fairly consistent with a cost ranging from 64% in China to 68.6% in the U.S. It appears Europe's higher f&b volume helps control the expense ratio at 67.8%. Food & beverage labor is not as large of a component of the f&b department as it is in the rooms department.

Telephone Expense

In all areas of the world, the telephone department makes a small profit except the U.S., where it loses money. This can be attributed to the low telephone revenue in the U.S.

Spa Expense

India has the lowest spa expense at 40.8%, with China at 55.9% and Europe and the U.S. at 76.1% and 73.4% respectively. Again, these differences are typical labor cost related.

Garage Expense

Good profit is made in the garage of China hotels with an expense ratio of 25.4%.

Administrative and General

South America has the highest administrative and general cost at $11,940 per room. Europe is the next most expensive at $8,975 per room, followed by the U.S. at $8,120. Comparatively, India is not as low as might be expected, operating at $7,130 per room. Administrative and general expenses are not as labor intensive as rooms and f&b, so India's labor advantage does not show up as much in this expense item.

Marketing

The U.S. has the highest marketing expense at $6,090 per room, followed by South America at $5,430. India is at the lowest at $3,020. The competitive environment in the U.S. is particularly difficult and requires higher expenditures in marketing.

Brand Marketing Fee

India hotels typically charge a separate marketing fee for chain-affiliated hotels.

Property Operations and Maintenance

India pays the most for property operations and maintenance: $4,955 per room. This can be attributed to the high cost of replacement equipment parts and the wear and tear of operating a hotel in India. The property operations and maintenance in the other areas of the world are similar: around $3,500 per room.

Energy Costs

India has the highest energy costs at $9,665, followed by China at $6,885 and Europe at $3,925 per room. South America and the U.S. are similar at approximately $2,700 per room.

Income Before Fixed Charges

With its high f&b coupled with very low departmental expenses, the proposed Marriott in India generated income before fixed charges of $12,528,000, which was 51% of total revenue. The other four markets had a fairly tight range of IBFC of $8,014,000 for Europe and up to $8,788,000 for the U.S. These profit ratios are about 40%.

Management Fees
The base management fee for all the markets was 3% of total revenue except for China and India, which was 2.5%. China is a particularly attractive market for international hotel companies who compete aggressively to obtain management contracts.

Property Taxes
The U.S. pays the most in property taxes: $540,000. China is next at $433,000, followed by Europe at $424,000. India is next at $252,000, followed by South America at only $110,000. Note that South America also pays a turnover tax of $844,000 and a bank credits & debits tax of $211,000, making it much more expensive than the other regions from a total tax perspective.

Insurance
Insurance ranges from a low of $66,000 in South America to $209,000 in the U.S.

Reserve for Replacement
All the markets utilized a 4% of total revenue reserve for replacement except the U.S., which used 5%.

The following are several additional expenses that are deducted by typical buyers of hotels in the regions where they operate. As appraisers, it is important to reflect the actions of typical buyers and sellers and include these expenses in the revenue and expense statement if they are customary deductions used by market participants. For example in China, it is normal for buyers to deduct a business tax. This type of tax is normally deducted in other regions of the world.

Business Tax
An additional tax normally deducted in China, which amounted to $1,117,000 or 5.5% of total revenue.

Incentive Management Fee
Additional fees paid to hotel management companies are usually based on a percentage of net income. Marriott typically has an incentive management fee, which is traditionally deducted for valuation purposes in other areas of the world. However, as described previously, in the U.S., incentive management fee is usually subordinated to debt service and is usually loaded into the equity yield and not specifically deducted during the appraisal process. Occasionally, it may be helpful to include incentive management fees for appraisals in the U.S., which is also proper methodology. Outside the U.S., the incentive management fee ranges from 2.7% of total revenue in South America to 3.9% in India.

Turnover Tax and Bank Credits and Debits Tax
As previously described, hotel appraisers in South America also deduct a turnover tax and a bank credit & debits tax.

Net Income
The resulting income for these five regions is as follows:
China: $5,086,000
Europe: $5,272,000
India: $9,602,000
South America: $4,904,000
U.S.: $6,351,000

India leads the list showing a net income of $9,602,000, which is significantly higher than the other regions. South America is the lowest at $4,904,000. Even if you deduct an incentive management fee for the U.S., it would still be the second highest at $6,351,000. At least from a profit point of view, these results show why India has been getting so much attention from hotel companies looking to do business there. On the other hand, even with the growth of Brazil, South America is not as active in new development compared to India, the U.S. and China.

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About Steve Rushmore

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