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Planning is the first step in capital spending

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While few large projects ever go 100% to plan, common pitfalls can be avoided with proper planning, due diligence and effort.

Highlights

- 2014 expenditures will likely reflect a significant increase above 2013 levels.
- Spending smart is a good mantra, concentrating on areas that will yield a positive ROI.
- Think strategically about the contingency.



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Capital spending has increased significantly in recent years, and 2014 is shaping up to continue this trend.

Revenue per available room continues to recover; hotel valuations are on the rise; furniture-fixtures-and-equipment reserve balances are more robust than they have been in years; and in many markets, new or repositioned competition is back in the mix supporting the need for reinvestment.

Recent industry studies suggest capital expenditure spending in 2013 for United States hotels was estimated at \$5.6 billion, marking a nearly 10% increase over 2012 and more than a 100% increase over 2010 levels. In short, the industry is playing catch up. If our asset management portfolio is any indication of broader industry trends, 2014 expenditures will likely reflect a significant increase above 2013 levels. In light of increased capital spending, we are reminded of the importance of planning and offer some key considerations for hotel owners to ensure successful execution of capital plans with a focus on enhancing investment returns.

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- **Unless money is no object, you can't do everything.** Developing a detailed project scope (and budget) is critical to successful CapEx project execution. This exercise invariably will include difficult decisions about what to (and what not to) include in a project. By design, this effort will prioritize projects by investment return, while identifying risks early in the process. Understanding that it is unlikely that 100% of the items on your list will be addressed in a project is critical and can help avoid "owner's remorse" and overspending at the end of a project.
- **Focus dollars on high-impact areas.** Spending smart is a good mantra, concentrating on areas that will yield a positive return on investment. Balance spending requirements outlined by the brand with what is relevant in the market that also supports revenue growth.
- **Assemble the "right" project team (for the right fees).** The project manager, designer (architect, if needed) and purchasing agent are the most critical team members, and there is no shortage of talent specializing in our industry. Key to this process is finding firms with experience in similar hotels (and working with similar budgets). Experience has shown us that careful selection and competitively bidding of team members can result in significant (more than \$2 million in 24 months alone) in savings to our clients from original estimates.

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- **If applicable, identify the role of the brand.** In some of our renovation projects, divisions of the major brands have been engaged for key project team roles (design, procurement, etc). We partner with brand representatives early on to ensure they are aware of our milestone dates and to allow sufficient time for reviews. Treat brands as you would any other member of the project team, requiring qualifications and a competitive bid offer to ensure pricing is in line with value delivered.
- **Planning takes longer than you think.** Depending on the scope of your renovation, many of the items (FF&E) might be coming from overseas, arriving to the U.S. by ship. Paying more for air freight makes little sense (unless absolutely necessary) and should be avoided by putting forth additional effort during the planning and scheduling phases of work. Significant savings might be realized through working with a logistics specialist to ensure the most cost-effective routing of goods, but time is money, so planning ahead is crucial.
- **Have a contingency plan.** For some owners, spending every last penny of a budget is a solid business decision. For others, leaving funds unspent at the end might be the sign of a successful project. Think strategically about the contingency, including development of wish list items that can be added to the scope should funds be available.
- **Identify and plan for operational costs.** Examples can include additional housekeeping and engineering department hours for rooms coming out and going back into service, replacement of operating supplies and amenities, and even increased utility expenses if otherwise unoccupied floors are active for construction. While a management team should not be given carte blanche on its budget during a renovation, it is important to note that these expenses are real and will be incurred. Similarly, during the planning phase, we have worked to identify project elements that might result in ongoing labor savings post-renovation. We not only are managing to a capital budget, but also to future operational plans.
- **Timing is everything.** Unlike other forms of commercial real estate, the hotel business is operationally intensive. Work must be planned and phased to ensure minimal displacement of revenue and as little guest impact as possible.
- **Modify your capital plan.** When funds get tight, it is always easy to defer something and say "that can come out of the reserve or contingency." It is critical that these items be captured in the hotel's capital plan, including any cyclical replacements that might need to be re-timed after a renovation.

Execution of a successful capital project requires the elements above from the pre-planning, execution, operational-impact and post-renovation phases. While few large projects ever go 100% to plan, with proper planning, due diligence and effort, common pitfalls can be avoided.

Andrew Leber brings more than 12 years of hospitality consulting, operations and asset management experience to CHM. Mr. Leber is responsible for creating value through asset management of a diverse portfolio of assets, including full-service, convention-oriented and select-service hotels, representing a wide range of brands and geographic markets. He brings subject matter expertise in the planning and execution of major-scale renovations, as well as implementing strategic operational initiatives for enhancing value.

Larry Trabulsi brings more than 15 years of consulting and asset management experience and four years of hotel operations experience to CHM. Mr. Trabulsi has been involved in a number of land uses, including hotels, resorts, restaurants, golf courses, marinas and other recreational assets. His clients have ranged from private operators, developers, and equity firms to public entities, such as convention and visitors bureaus, the National Park Service, the United States Forest Service and branches of the U.S. Department of Defense. Mr. Trabulsi currently serves on an asset management team for a hotel portfolio of 12 hotels with a total value of approximately \$2 billion.

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