

Hornes' Lodging Properties **Best Western - Lehi Motel Case**

Wade Sewell took a deep breath. As the new director of operations for Hornes' Lodging Properties, he had a lot of responsibility. Mr. Horne had called him early that morning and asked him to go with him to look at some property in Lehi, just off the freeway, as a possible site for a motel. Mr. Horne had already spoken with the owners of the property about forming a partnership to develop a motel on the site. The owners had considered developing a motel on the property, but had no experience in the industry. Mr. Horne offered to build and manage the motel, using his expertise and financial clout to finance and develop the project. The property owners would contribute the land to the partnership. The proposed motel would be affiliated with the Best Western chain and would be a limited-service, 59 room facility in the luxury-budget category with good highway visibility. It would most likely contain a Jacuzzi and small meeting room. Exhibit A shows a map of the area and proposed motel site.

Horne Lodging Properties owned and operated several hotels and motels in the intermountain region and based on years of experience in the lodging industry, Mr. Horne felt that Lehi was an excellent possibility as a site for a small motel. Wade Sewell's job was to gather market and financial data to help determine if Mr. Horne's hunch was correct. As he contemplated the job ahead, several questions ran through his mind. First, would the market research and financial analysis bear out the need for a motel in Lehi — enough of a need for them to go ahead with this investment? Mr. Horne expected a fairly high cash-on-cash return on investment—at least a 15% average over a five year investment period.

To answer these questions Wade would have to estimate several pieces of information. What kind of occupancy could they expect? What rate could they charge? The company was leaning toward the Best Western franchise based on previous research and analysis in which they had compared several factors including a cost analysis and the reservation contribution expected from each franchise.. Based on his experience in the lodging industry, Doug Horne knew that an affiliation with a nationally-known chain had a much higher success rate than an independent hotel did. Best Western had a high rate of reservation contribution which meant that the franchise would be working for them to get customers. That meant less sales and advertising effort on their part. The cost structure was also desirable. Franchise fees were reasonable, as were the initial start-up fees (see Table 1). Exhibit A-2 shows a comparison of franchise chains in this class of motel. Wade was fairly certain as to which chain the company would use, but the bigger question remained—should they even build a motel in Lehi?

Table 1: Costs for Best Western Chain

Name of Chain	Initial Fee	Royalty Fee	Ad/Mktg Fee	Reservation Fee
Best Western International	\$33,000 for 100 rooms, plus \$100 per additional room up to 400	\$25,003 for 100 rooms, plus 62 cents per room per day for 101 to 150 rooms, 61 cents per room for 151 to 400 rooms	\$3,262 for 100 rooms, plus \$16 per room for 101 to 400 rooms	\$0.35 per room per day for first year, then based on number of room nights booked via res center in previous year

The National Lodging Industry and Market Trends

The lodging industry in the U.S. had shown strong gains in the 1993-1994 year, breaking out of the 1990-91 recession. The recovery and previous slump are best understood from the beginning of the cycle in the early 1980's when the supply of new rooms began to increase at an accelerating pace.

The construction boom was fueled by four major factors. First, franchises created new products for developers to build. The 1980's saw the introduction of a market segmentation strategy in guest rooms. Commercial accounts, business travelers, and tourists could choose between hard budgets, regular budgets, limited service, lower/middle, upper/middle, all suites, and extended stay. The new selection of rooms was primarily provided by new construction, which led to an over-built market. Second, lenders had capital to lend for the development of these new concepts in the hotel industry. Third, capital was readily available as a result of flourishing equity markets, the entry of savings and loans in commercial lending, and lower bank cash reserve requirements. Finally, the economy was expanding.

Room demand did not keep up with the rapid increase in supply. When the economy began to slow down and room demand dropped, many new facilities were already partially built and new units continued entering the market. A surplus was building and the industry was set to topple. The hotel industry was not alone; most other real estate sectors had expanded beyond the supply-demand equilibrium as well.

The expansion in the early eighties resulted in a downturn in the late eighties and early nineties. The database of *Trends in the Hotel Industry USA edition 1992(Trends)* indicates that, based on taxable income, the industry did not make money from 1985 to 1990. These were difficult times in the real estate market.

The difficult times, however, caused hotel managers to tighten operating procedures and improve their operating margins. *Trends* reports that payroll and related costs had declined from 40% of total revenue in 1975 to 34% in 1989. Cost cutting measures assisted in attaining higher operating margins for all types of hotels and thus continued to bolster profitability through 1994. The two most profitable categories of hotels were the limited-service properties and the all-suite hotels without food and beverage facilities.

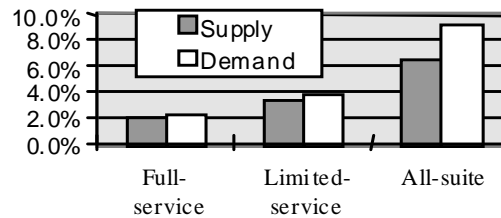
The 1994 market conditions were generally upbeat. Room demand in the market seemed to be outpacing supply growth in the lodging industry. As can be noted in Table 2, 1992 and 1993 showed much improvement over 1990 and 1991 when supply growth exceeded that of demand. These trends coincide closely with the downturn of the national economy in 1991.

Table 2: U.S. Growth in Room Supply vs. Demand¹

	Supply	Demand
1989	3.5%	4.9%
1990	3.4%	2.1%
1991	2.5%	0.6%
1992	1.3%	4.0%
1993	1.0%	4.0%

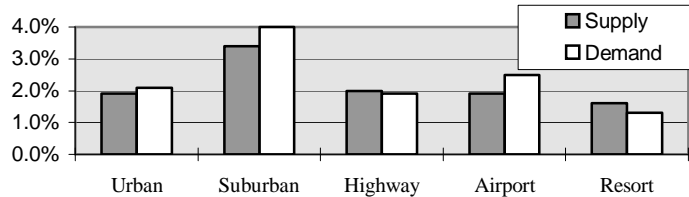
When the room rate supply and demand figures are compounded into annual growth rates and broken down by type of hotel and location, the numbers are even more telling (see Figures 1- 2).

Figure 1: Compound Annual Growth in Room SUPPLY VS. DEMAND BY TYPE OF HOTEL - U.S. 1988 to 1993



SOURCE: *The Host*, Arthur Andersen, Annual Report 1993

Figure 2: Compound Annual Growth in Room SUPPLY VS. DEMAND BY LOCATION U.S. 1988 to 1993



SOURCE: *The Host*, Arthur Andersen, Annual Report 1993.

In conjunction with the reversal of supply and demand trends, occupancy figures for 1993 were improved over 1992 and previous years. Preliminary figures for the U.S. show an occupancy of 62.4 percent in 1993 (see Table 3). Whereas occupancy had gained ground in 1993, rates did not keep pace with inflation. Table 4 shows the average daily room rates by hotel type for 1992 and 1993. The room rate increase from 1992 to 1993 was \$1.34, a gain of only 1.02 percent.

¹ *The Host Report*, Arthur Andersen Real Estate Services Group, 1993.

Table 3: U.S. Average Occupancy Levels²

Type	1992	1993
U.S. Total	60.6%	62.4%
Full-Service	61.9%	63.4%
Limited-Service	61.7%	62.0%
All-suite	69.8%	72.7%

Table 4: U.S. Average Daily Room Rate³

Type	1992	1993
U.S. Total	\$60.07	\$61.41
Full-Service	\$74.58	\$75.85
Limited-Service	\$44.45	\$45.51
All-suite	\$78.64	\$80.44

Occupancy levels fluctuate dramatically throughout the year reaching their peaks in the summer months and reaching their lows in the winter months. Fluctuations can vary as much as 20% from 60% occupancy in the winter to well over 80% occupancy in the summer months.

Occupancy is expected to rise very slightly from 1995-1997. The U.S. average daily rates are forecast to increase over time rising from around \$63.37 in 1994 to over \$70.00 by 1997.

Additional forecast information is summarized below in Table 5.

Table 5: U.S. Lodging Forecast

	1994	1995	1996	1997
Total Receipts	68,663	73,470	78,948	85,001
% change	6.5%	7.0%	7.5%	7.7%
Room revenue per available room	14,902	15,787	16,792	17,909
% change	5.2%	5.9%	6.4%	6.7%
Room supply	3,161	3,195	3,226	3,257
% change	1.1%	1.1%	1.0%	1.0%
Room starts	48,663	42,679	44,180	47,917
% change	50.6%	-12.3%	3.5%	8.5%
Room completions	33,461	46,475	43,757	43,983
% change	-12.2%	38.9%	-5.8%	0.5%

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Chain-affiliated vs. Independent Hotels

Market data comparing the performance and financials of chain-affiliated properties versus independent properties show that the chain-affiliated properties outperformed the independents in terms of capturing room nights (average occupancy) and controlling costs (expenses).

Independent properties, however, generated substantially higher average daily room rates than the chain affiliates. Chain-affiliated properties reported higher profit margins than independent properties. Table 6 summarizes comparative information:

Table 6: Chain-affiliated motels vs. Independent motels

² ibid

³ ibid

	Chain-Affiliated	Independent
Income as % of sales before fixed costs	39.6%	28.0
Overall labor costs per occupied room	\$14.32	\$21.00
Operating revenues as % of sales	70.8%	66.0%
Average pre-tax income per room	\$1,954	(\$267)

Utah County Lodging Market

The lodging market along the Wasatch Front primarily consists of the Utah County, Salt Lake County, and the Davis/Weber County. The proposed subject property is located in Lehi on Interstate 15, which belongs to the Utah County sub-market. The Utah County Lodging Market could be further broken down into two sub-markets, the I-15 corridor and Provo. The Provo market will often impact the I-15 market when the Provo motels are full and consequently will send overflow to the surrounding areas. In addition, the Utah County Lodging Market also benefits from overflow from Salt Lake County. The Utah County market consists of a balanced mix between budget to economy motels and upper-end moderate-rate properties. The I-15 corridor is almost completely limited to service budget to mid-rate motels.

Lodging demand in Utah County comes from business travelers, tourists, and en route travelers. Convention business is minimal in Lehi. Business travelers maintain a base occupancy during the winter months that are less popular among tourists. Tourism dominates the summer months. Harsh weather conditions have produced high occupancy and room rates at times along I-15 as truckers and travelers seek shelter. The Monthly Occupancy Trend shows that August typically has the highest occupancy (90.7% in 1993 and 89.9% in 1992). The summer months are the most popular among leisure vacationers visiting nearby attractions, or traveling through the area. The low occupancy months of 1993 and 1992 were in December at 47.8% and 45.8% respectively.

Room rates are also seasonal in Utah County. The Average Daily Rate (ADR) in 1993 ranged from a low of \$42.63 in December to a high of \$51.34 in August. The ADR in 1992 ranged from \$43.62 in May to \$49.83 in August. The average annual room rate rose from \$46.16 in 1992 to \$47.27 in 1993, a 2.4% increase.

Demand Generators

Demand generators in the subject neighborhood are those institutions, industries, and facilities that will have the most significant impact on the occupancy and average daily rate of the proposed facility. These generators were determined by survey of the competitive properties, local competitors, travel councils and businesses in the area.

The following summarizes the findings of the demand generator survey:

1. Interstate Travel
2. Tourism
3. Salt lake City and Provo Overflow
4. Business Travel & Other

Interstate Travel. With the subject property being located along a major interstate freeway, the most important source of demand for lodging services will consist of en route traffic on Interstate 15. En route traffic is made up of leisure and commercial travelers passing through Utah County without it being a destination. A large portion of travelers prefer lodging at a freeway location rather than venturing into town and leaving the freeway. These travelers typically arrive late and are anxious to be back on the road early. Unlike most motels in Utah County, the subject property would have direct freeway access and visibility. None of the Provo lodging facilities have good visibility from I-15, and only Mountain Springs in Springville and the Comfort Inn in Payson have good freeway visibility.

Traffic is expected to continue to grow through the next decade. Information regarding traffic flows was obtained from the Utah Department of Transportation, which collects information using automatic traffic recorders located at various points throughout the state. Below, Table 7 summarizes the total traffic count at I-15 and Main Street since 1987.

Table 7: Traffic count Lehi Main St. and I-15

Location	1987	1989	1991	1993	Annual Growth Rate
I-15 South of Interchange	42,440	51,910	54,405	62,545	6.67%
I-15 North of Interchange	41,520	44,910	49,945	57,315	5.52%
Main St. West of Interchange	7,725	7,910	5,965	8,250	1.10%
Main St. East of Interchange	8,325	8,520	9,965	10,005	3.11%

Traffic is expected to continue to grow as the interchange is built up. A Subway fast-food outlet was built in 1993 at the northeast corner of Main Street and 850 East. Walker Oil purchased 1.75 acres for the development of a gas station and Wendy’s restaurant at the southeast corner of the intersection. The service station will not have diesel fuel to service trucks, nor will it cater to truck drivers.

The only sizable truck stop with a motel in Utah County is located in Springville at the Mountain Springs Truck Stop and Motel. Although no travel plaza is planned for the interchange in Lehi, the subject’s location near the freeway may be convenient for a limited number of truckers.

McDonald’s was also negotiating for property at the southwest corner of 850 East Main Street. The presence of McDonalds would most likely draw additional traffic from the freeway and provide additional exposure to the subject.

Tourism. Tourism is a significant industry generating lodging demand. Rural Utah Tourism, a study conducted by several state agencies and completed in 1992 concluded that the total spending by out-of-state travelers was \$2.90 billion in 1991. There were 14.0 million out-of-state visitors, supporting tourism related employment for 61,200 people, or 8.2% of the total

workforce. The total state and local taxes reportedly generated by tourism spending equaled \$214 million. The estimated tourism related employment in the Mountainland Region, which includes Utah, Summit, and Wasatch Counties, grew at an annual rate of 5.39% from 1980 to 1990, according to the tourism report.

Utah County, and specifically Lehi and American Fork, are not popular tourist destinations. However, general tourism in the region increases inter-regional travel, bringing tourists to the area. Several attractions in the area include BYU, Utah Lake, Timpanogos Cave, and Sundance Ski Resort. The following visitor counts show mixed growth at these destinations.

Table 8: Utah County Visitor Counts

	1991	1992	1993
Timpanogos Cave	104,745	120,995	93,261
Skier Visits—Sundance	65,446	50,014	67,729
Utah Lake State Park	216,085	274,408	394,189
Utah County Visitor Center	n/a	18,960	22,523

Timpanogos Cave visitations reported a sharp decline in 1993 due to budget cutbacks that shortened the season by closing October through May, rather than November through April. Nonetheless, tourism is not expected to suffer because the visitors during May and October were typically from local elementary schools.

The Utah Office of Planning and Budget forecasts growth rates of several tourism indicators to the year 2000, in the publication, Rural Utah Tourism. The forecasts are summarized below:

National Park Area Visits	3.52%
Temple Square Visits	4.56%
Real Room Rents (\$1990)	3.16%
Skier Visits	2.63%

Salt Lake and Provo Overflow. High occupancy rates in Salt Lake and Provo create overflow occupancy to nearby areas. Guests wishing to stay in Salt Lake County must often find lodging in Utah County. In addition, during high occupancy periods, Provo City will refer guests to nearby motels in Springville and Payson as well as Salt Lake County. The months in which Provo or Salt Lake experience occupancy over 80% will most likely result in overflow to the subject property. When Salt Lake or Provo occupancy exceed 80% for a month, many nights are fully occupied, and the good quality, economy franchise properties are filled first. According to Susan Bowen at the South Jordan Sleep Inn, many motels are turning guests away and referring them to Utah County when occupancy is high in Salt Lake. Table 9 gives a summary of occupancy rates for Salt Lake and Provo which indicates the months that will likely result in overflow business to Lehi.

Table 9: Monthly Occupancy Rates

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Provo	58.1	67.3	82.6	77.4	64.3	87.9	83.5	91.4	72.7	68.2	57.4	50.5
SLC	73.4	86.7	91.1	86.0	78.7	84.1	86.5	91.5	80.6	73.1	60.0	64.6

The bolded months, based on 1993 occupancy rates, indicate those months where the subject property will likely have increased demand. May is typically a low month in Utah as the ski season is ending and summer tourism has not yet begun. In addition, BYU ends its regular school year at the end of April, reducing traffic through Provo in May.

Business Travel & Other. To ascertain the amount of economic impact on Utah County from corporate and business travel, the Lehi and American Fork Chambers of Commerce were contacted as well as the Utah County, Orem and Provo Economic Development Agencies.

The lack of existing lodging facilities in the immediate area limits the ability of communities like Lehi and American Fork to sponsor festival and related activities. The Lehi rodeo brings visitors from outside the area. However, these guests are forced to stay in Salt Lake or Provo.

Various existing local businesses require travel to the area by mechanics, sales people, buyers, or guardsmen, including Lehi Block, A.P. Green, and the Army National Guard in Lehi and American Fork. Many other small businesses in the area indicated a need for adequate lodging in the area between Provo and Sandy. The proposed Micron facility will certainly add to the auditors, staff, executives and consultants visiting the area.

Group travel is another factor. Although few tour groups are expected to patronize the subject property, groups for sporting events will require some lodging in the area. American Fork, Lehi, and Pleasant Grove High Schools often sponsor students from out of town that require lodging. Currently, there are no lodging facilities in the area that can accommodate the demand generated by the schools in the area north of Provo. Additionally, many people have contacted the Chamber of Commerce looking for lodging in Lehi for family reunions or to visit family and friends.

General Risks and Benefits

Demand for hotel properties is driven by the relative risk/return profile of this real estate class. Potential disadvantages of a hotel investment are competency of management, long start-up periods, food and beverage risks, rapid functional obsolescence, susceptibility to external obsolescence and illiquidity.

On the micro level, many motels constructed in the 1950's were forced out of business by the changeover from the U.S. highways to modern interstates. The deterioration of downtown areas is another risk. Uncontrollable factors such as these are a constant risk for lodging facilities. In most cases external obsolescence cannot be cured and the impacted property experiences an immediate drop in value.

On the other hand, announcements like the addition of the Micron plant to Lehi can enhance property values for this type of investment. Other positive aspects of hostelry investments include favorable tax treatment from short depreciation periods. After income from a lodging facility reaches the break-even point, profits tend to increase rapidly. A large portion of hostelry expenses are fixed, meaning they do not vary with occupancy. Thus profits increase rapidly with increased occupancy.

Summary of Demand Analysis

Demand for the proposed motel is expected to come from interstate business and leisure travelers, tourism, over-flow from Salt Lake and Provo and local business. Growth in room demand has been estimated at about four to five percent per year from 1988 to 1993. The *Room Night Demand Quantification* taken from the Smith Travel Research (STR) Trend Report from September 9, 1994 indicates that the total room demanded among the Utah County competitors for 1993 was 248,252, or 71.9 percent of the supply. Total room demand competitive to the subject is expected to reach 310,718 room nights in 1998. See the Table 10 below:

Table 10: Room Demand Growth – Utah County (weighted)

Year	Growth Rate	Room Nights
1993	--	248,252
1994	3.0%	255,699
1995	6.0%	271,041
1996	6.0%	287,303
1997	5.0%	301,668
1998	3.0%	310,718

Supply and Competition

The proposed subject property does not have any direct competitors in the North Utah County area. The primary competitors are considered the most direct competition due to their proximity and freeway location. The Sleep Inn and Hampton Inn are located about 14 miles to the north. The next closest freeway property located in Utah County are those at the south University Avenue exit and the Mountain Springs Motel, located 15 to 20 miles to the south. The Holiday Inn Express (Spanish Fork) and Comfort Inn (Payson) are located about 23 and 27 miles south of the subject. The Mountain Springs Motel, Comfort Inn and Holiday Inn Express are considered secondary competition because they will compete with the subject for overflow guests, and I-15 travelers looking for lodging somewhere in Utah County. Other Utah County competition is made up primarily of Provo motels/hotels. The subject will compete indirectly with the Provo facilities for all types of travelers. For example, if more Provo hotels are built, less overflow will go to Lehi. Occupancy and ADR estimates for the market were extrapolated from data in the STR report and surveys of the property. Most of the motels in competition with the subject are affiliated with national franchises and compete in the economy to mid-rate motel categories. Exhibit B summarizes information regarding primary and secondary competition of the area's lodging facilities.

Supply Growth

Supply growth is estimated by analyzing past activity and researching current plans for development. It is typical that only some proposed motels will actually be developed. Likewise, other lodging facilities may be built which are not currently planned.

Recent Developments. Supply growth over the past six years has been minimal in Utah County, with most of the Interstate 15 growth focused in southern Salt Lake County. Table 9 tracks the

supply growth of competitive properties up to 1995. When a project opened mid-year, the rooms are pro-rated based on the opening date.

Table 11: Trade Area (Utah County and S. SLC) Supply Growth - # of Room Additions

	Pre 1989	1989	1990	1991	1992	1993	1994	1995	Total
Courtyard, Sandy								60	60
Super 8, S. Jordan							5	57	62
Holiday Inn, Sp Fork							24	24	48
Sleep Inn, S. Jordan					51	17			68
Hampton, Sandy				131					131
Mtn.Springs, Springville	62								62
Comfort Inn, Payson	62								62
Other Utah County	1,451				30	42			1,523
TOTAL ADDITIONS	-	0	0	131	81	59	29	141	-
TOTAL COMPETITION	1,575	1,575	1,575	1,706	1,787	1,846	1,875	2,016	2,016
YEAR OVER % GROWTH	-	-	0%	8.3%	4.7%	3.3%	1.6%	10.9%	-
Average Annual Compound Growth Rate	4.8%								

Proposed Development. As noted above, new hotel development accelerated in 1995, with various projects rumored, particularly in southern Salt Lake County. Lehi City indicated that a land owner directly east of the subject across I-15 discussed a hotel use. However, no plans had been presented to the city by mid 1995. All information gathered on proposed developments were gathered from city and county planners as well as motel operators who were questions about plans for future expansion. No construction was underway in Utah County in late 1994 when the subject's proposed development would take place.

Below are summarized the proposed developments by year in Utah County.

- 1994 62 unit Super 8, South Jordan
- 1995 59 unit subject property, Lehi
60 unit Courtyard, Sandy
- 1996 50 unit Convention hotel, Orem
- 1997 40 unit Courtyard/Hampton in Provo or Orem
- 1998 no units planned for development

Occupancy Rates

Occupancy is determined by correlating current supply and demand on a weighted basis. Future growth rates are then applied to each of the base figures to arrive at future levels of supply and

demand. The following table summarizes the analysis and presents the occupancy estimates for the Utah County market for the years from 1993 to 1998, based on supply and demand trends.

Table 12: Market Occupancy Projections (weighted)

Year	Supply	Demand	Occupancy
1993	345,108	248,252	71.93%
1994	367,738	255,699	69.53%
1995	411,538	271,041	65.86%
1996	429,788	287,303	66.85%
1997	444,388	301,668	67.88%
1998	444,388	310,718	69.92%

It should be noted that there is some risk associated with the location of the subject property in an area that is untested. However, given the success of highway properties in the mountain region, the subject property will likely have full name and location recognition after a penetration period. Exhibit B contains a summary of the occupancy rates of the competition.

The data indicate that the properties to the north of Provo, at 106th South in Sandy and South Jordan, surpass the motels to the south of Provo. Salt Lake in general has higher occupancy than Provo, and there is higher traffic volume to the north of Provo than to the south. In addition to the property-by-property analysis, regional surveys and results for occupancy are presented below:

Table 13: Occupancy by Regional Surveys

Regions and Source	1992	1993
State of Utah—Rocky Mtn. Lodging Report	70.3%	71.9%
Mountain States, Limited Service Hotels— <i>Host Report</i>	66.4%	71.6%
Utah County—STR	67.5%	69.7%
Provo—Rocky Mtn. Lodging Report	n/a	69.2%
Salt Lake City—Rocky Mtn. Lodging Report	74.1%	77.3%
Utah County—Utah County Travel Council	63.3%	66.2%
U.S., Limited Service Properties— <i>Host Report</i>	63.6%	63.3%

Most regions indicate an increase in 1993 over 1992 occupancy rates. Year-to-date data for 1994 show that occupancy is continuing to increase. The data from the broad surveys above include properties that may be inferior or superior to the proposed subject motel.

Average Daily Rates

Regional averages were gathered to find a typical average daily rate throughout the area. The following table gives a summary of the typical rates in the area.

Table 14: Average Daily Rate by Regional Surveys

Regions and Source	1992	1993
State of Utah—Rocky Mtn. Lodging Report	\$57.37	\$58.52

Mountain States, Limited Service Hotels— <i>Host Report</i>	\$50.76	\$50.74
Utah County—STR	\$46.16	\$47.27
Provo—Rocky Mtn. Lodging Report	n/a	\$47.79
Utah County—Utah County Travel Council	\$45.79	\$52.36
U.S., Limited Service Properties— <i>Host Report</i>	\$45.06	\$45.93

In determining an appropriate ADR, it is also helpful to estimate average rates among competitors. Table 15 presents the estimated ADR's of the competition, however, adjustments should be made to each property to reflect the condition and quality of the property, as well as the amenities offered. See additional information for competitors in Exhibit B.

Table 15: Average Daily Rates

Property	# of Rooms	Rack Rates	ADR
Sleep Inn, S. Jordan	68	\$50-60	\$43.00
Hampton Inn, Sandy	131	\$63-69	\$55.00
Mtn Springs, Springville	62	\$34-47	\$40.00
Comfort Inn, Payson	62	\$55-69	\$48.00
Holiday Inn, Sp Fork	48	\$50-55	\$46.00
Other Utah County		\$34-40	\$34.00
Weighted Avg.	371		\$47.96

The comparable properties in the Utah County sub-market have an average rate of \$47.96 before making adjustments. According to the Rocky Mountain Lodging Report, room rates for the first eight months of 1994 were up to \$49.59 from \$47.58, a 4.23% increase.

The average daily rate is expected to grow at a rate of 4.0 percent annually through 1999. This rate is based on an analysis of the CPI, the Lodging Price Index, and the ADR growth over past years. Room rates, however, grew at an average annual growth rate of 6.1% from 1989 to 1993. Most new lodging facilities price below the competition initially in order to penetrate the market more rapidly and build-up occupancy. The proposed motel would come on line early in 1995. Additionally, national survey information shows that the normal range of room rates for a luxury-budget hotel range from \$40-\$60, and Best Western chain franchises have an average rate of \$57 with a standard deviation of 14 and a range of \$43-71 nationally.

Financial Analysis and Cost Data

Information taken from a land appraisal estimated a land value for the property of \$500,000. The total cost to build the motel, not including land was \$2,073,938. This equates to \$35,151 per room and \$68.00 per square foot. See Exhibit C for a cost breakdown.

The table below shows the summary of data from the previous sale of comparable motels in the area.

Table 16: Motel Sales - Summary

	Sale 1	Sale 2	Sale 3	Sale 4	Sale 5
Location	Riverdale	Layton	Provo	Moab	SLC
Sales Date	12/91	08/89	06/93	01/90	01/90
Sales Price	\$1,925,000	\$2,450,000	\$1,900,000	\$1,725,000	\$3,300,000
No. of Rooms	110	100	78	56	99
Room Revenue Multiplier	1.83	3.11	2.49	2.94	3.14
Price Per Room	\$17,500	\$24,500	\$24,359	\$30,804	\$33,333
Adjusted Price Per Room*	\$33,600	\$33,810	\$35,384	\$40,661	\$44,000
Overall Rate	14.00%	14.16%	12.94%	11.92%	12.72%

*Adjusted for market conditions, location, age & condition, and amenities

The room revenue multiplier is one of the most relevant income parameters because it isolates the income attributed to the motel rooms only. It is calculated by dividing the sales price by the projected rooms revenue. The multipliers towards the upper end represent fully stabilized properties with good operating histories. The lower multipliers represent bank-owned properties which had marginal operating histories or location limitations.

Exhibit D shows the estimated expenses for the first year of operation, based on the experience of the other properties managed by Horne's Lodging Properties. Revenues come primarily from room rentals (96.43% of total revenues) which is calculated by multiplying the number of rooms by 365 days, multiplied by the occupancy rate, multiplied by the average daily rate. However, a small amount is generated from telephone and other charges (3.57% of total revenues).

Depreciation occurs at different rates for different assets. For example, the building, though it may last longer, might be depreciated over 15 - 25 years (assume 18 years). The furniture, fixtures and equipment (FFE) will depreciate much faster and is usually replaced within 5-7 years. Those expenses not tied to the percentage of revenue will probably grow at the rate of inflation, about 3%. Property taxes and fire insurance tend to grow at about 5% per year.

It was also indicated that a construction loan would have to be secured before the permanent financing to build the proposed motel. Construction loans typically were quoted at 2% above prime and the project would be built within six months of beginning construction. Once the building was complete and final inspection passed, local lending institutions indicated that properties similar in nature to the subject's could obtain a long term mortgage with a fixed interest rate of 10.5 percent on a 25-year amortization compounded monthly with a 10-year call and a maximum loan-to-value ratio of 80 percent. Refer to Exhibit E for market data for mid September, 1994.

Armed with the market research and financial data he had compiled, Wade was ready to go to work. He hoped he could validate Mr. Horne's idea to build a motel at the site in Lehi.*

* Market research, facts and figures included in this case were taken from feasibility studies and appraisals provided by Horne's Lodging Properties

Proforma Cash Flow to Equity

EXHIBIT A-2

Comparison of Various Franchise Fees for Luxury/Budget Motel Class

Name of Chain	Initial Fee	Royalty Fee	Ad/Mktg Fee	Reservation Fee
Best Western International	\$33,000 for 100 rooms, plus \$100 per additional room up to 400	\$25,003 for 100 rooms, plus 62 cents per room per day for 101 to 150 rooms, 61 cents per room for 151 to 400 rooms	\$3,262 for 100 rooms, plus \$16 per room for 101 to 400 rooms	\$0.35 per room per day for first year, then based on number of room nights booked via res center in previous year
Comfort Inn and Suites	\$300 per room or \$45,000 (min.); Suites: \$300 per unit or \$50,000 (min.)	5.25% of gross rooms revenue; Suites: 5%	2.1% of gross rooms revenue	1.75% of gross rooms revenue
Econo Lodge	\$250 per room or \$25,000 (min.)	4% of gross rooms revenue	3.5% of gross rooms revenue	Combined with marketing fee
Hilton Garden Inns	\$250 per room for first 100; \$150 per room thereafter	5% of gross rooms revenue	1% of gross rooms revenue	1.7% of gross rooms revenue
Holiday Inn Express	\$500 per room or \$35,000 (min.)	5% of gross rooms revenue	2% of gross rooms revenue	1% of gross rooms revenue
Days Inns of America	\$350 per room or \$35,000 (min.) plus \$100/room res. entry charge	6.5% of gross rooms revenue	Included in royalty fee	2.3% of gross rooms revenue
Super 8 Motels	\$20,000 to 120 rooms; then \$167 per additional room	5% of gross rooms revenue	3% of gross rooms revenue	Included in ad/marketing fee
Travelodge	\$350 per room or \$35,000 (min.)	4.5% of gross rooms revenue plus 10 cents/room/month	4% of gross rooms revenue plus 5-10 cents/room/day	Included in ad/marketing fee
Fairfield Inn/Suites by Marriott	\$375 per room or \$25,000-\$40,000 (min.)	4-4.5% of gross rooms revenue	2.5% of gross rooms revenue	1% of gross rooms revenue, plus \$2.45 per confirmed reservation
Hampton Inn	\$450 per room or \$45,000 (min.)	4% of gross rooms revenue	4% of gross rooms revenue	N/A

Source: *Lodging Hospitality*. December 1997

Proforma Cash Flow to Equity

EXHIBIT B

Summary of Competitor Data

Summary of Area Lodging Facilities

Name	Location	Class	Amenities
Primary Competition			
Sleep Inn	S. Jordan	Budget/Economy	Jacuzzi, conference room
Hampton Inn	Sandy	Mid-rate	Swimming pool, Jacuzzi, conference room
Secondary Competition			
Mountain Springs	Springville	Budget	Swimming pool, Jacuzzi
Comfort Inn	Payson	Economy/mid-rate	Meeting rooms, indoor pool, sauna, exercise room, coffee shop
Holiday Inn Express	Sp. Fork	Economy	Small meeting room

Market Occupancy and Average Daily Rate Summary

Property	# of Rooms	Occupancy Range	Estimated Occupancy	Room Rates	ADR
Sleep Inn	68	80-85%	83.0%	\$50-60	\$43.00
Hampton Inn	131	84-90%	88.0%	\$63-69	\$55.00
Mtn Springs	62	70-75%	72.0%	\$34-47	\$40.00
Comfort Inn	62	54-56%	55.0%	\$55-69	\$48.00
Holiday Inn	48	60-65%	62.0%	\$50-55	\$46.00

EXHIBIT C

Best Western Lehi Motel Cost Breakdown

Description	Cost	Per room	Per Sq. Ft.
Land (183,000 square feet)	\$ 500,000	\$ 8,475	\$ 2.73
Building	\$ 1,847,138	\$ 31,307	\$ 60.57
Jacuzzi/pool	\$ 36,800	\$ 624	N/A
Furniture, Fixtures & Equip	\$ 190,000	\$ 3,220	N/A
Total Building Costs	\$ 2,073,938	\$ 35,151	\$ 68.00
Total Project Cost	\$ 2,573,938	\$ 43,626	\$ 14.00
Room Count		59	
Area (sq. ft.)			30,497

Proforma Cash Flow to Equity

EXHIBIT D

Best Western Motel Estimated Expenses - Year 1

Operational Expenses	
Rooms**	\$ 220,000
Telephone	\$ 15,000
Admin & General	\$ 60,000
Franchise Fees	\$ 29,000
Advertising	\$ 30,000
Utilities	\$ 25,000
Maintenance	\$ 30,000
Total Oper. Expenses	\$ 409,000
Other Expenses	
Depreciation	See case
Interest	See case
Fire Insurance	\$ 2,000
Management Fees	\$ 22,000
Property Tax	\$ 15,000

*The following items are based on a % of revenues per year:

Franchise Fee = 4%

Management Fees = 3%

Capital Acquisitions = 2.9% (depreciated over 10 years)

**Rooms expense includes such expenses as maids, front desk, laundry, bell man, meeting room, payroll, cleaning supplies, shuttle bus, continental breakfast

Proforma Cash Flow to Equity

EXHIBIT E

Market Data for week of September 10, 1994

	This week	Last week	Last year
Federal Funds Rate	4.70%	4.74%	3.03%
Discount Rate	4.00%	4.00%	3.00%
Prime Rate	7.75%	7.75%	6.00%
Corporate Bond - Baa rating	8.97%	8.88%	7.26%
90 day T-bill	4.72%	4.68%	3.03%
1 year T-note	5.72%	5.62%	3.32%
10 year T-bond	7.44%	7.33%	5.28%
30 year T-bond	7.70%	7.61%	5.98%
Residential Mortgage Rate	8.66%	8.51%	6.96%
Commercial Mortgage Rate	10.5%	N/A	N/A
S & P 500 Index	474.06	467.55	448.20