

HOTEL INVESTING REMINDER

Yes, KEY CRITERIA TO CHECK BEFORE YOU BUY INTO THAT HOTEL DEAL

Mark Hollins, buy-to-let hotel room investor, London.

I first wrote about hotel rooms for Property Alerts back in 2008. Since then the hotel investing concept has really caught the imagination. What I said then still holds true though. Read on...

What's the deal? The concept is a simple one. You buy a hotel room, usually in a hotel in a big city or leisure location, in the UK or overseas, for anything from £60,000 to £150,000+. Mortgages are normally available and these deals can usually be done via your SIPP (Self Invested Personal Pension). The hotel markets, lets and manages the room (cleaning etc) and you then share in the revenue from it (or, more often in practice, a share in all of the rooms divided by the number of owners) with the hotel; usually a 50-50 split or similar. Over time, the room may appreciate in value - although, as a relatively new concept, this is largely unproven at this stage.

Start by looking at who is running the hotel and who else is involved. The involvement of a major chain has to be a big plus rather than a single owner set-up and from all sorts of angles; experience, marketing ability, existing client base etc. If there are well-known companies running the attached spa, golf course etc, all the better.

Who's your market? 'Location, location, location' is as important with a hotel as it is with a property that you're buying to let. You need a constant flow of guests which is why most hotels offering these deals are located in busy business and/or leisure locations; cities such as London and York. They need to be accessible, close to airports and motorways as appropriate, and have in-house, on-site and nearby facilities expected by business travellers and holiday-makers; health and fitness spa, golf course etc.

Ideally, you want to see a deal which goes beyond having one single income stream – just business people staying over for an on-site conference, for example. The hotel may cater for business and leisure guests visiting for a variety of reasons; a stopover on the way to an airport; a short break to see the sights; a golfing weekend; attendance at a wedding, conference, exhibition or other event (preferably) at the hotel. When visiting to do your due diligence, assess competing hotels locally as well. Will people stay here - or there?

What's your occupancy rate? This is the key figure when it comes to working out your profit potential. As a rough and ready rule, a hotel will operate at a reasonable profit if it has an occupancy rate of about 60 per cent or more (i.e. six or seven rooms out of 10 will be occupied at any given time). You need to get spreadsheets from the hotel to see what the predicted occupancy rate is. As is often said in financial circles, bear in mind that past performance is no guarantee of future performance – a hotel that has focused mainly on short leisure breaks in the past may do less well during the credit crunch when these may become less popular. It is a good idea to re-work the figures you are given with various

other occupancy rates; 50 per cent, 40 per cent and so on to see if the numbers still add up at these lower rates. If you are investing via a SIPP, bear in mind that income is generated free from tax. If you are using the room yourself for so many nights a year (often part of the deal), take that usage into account as well.

What's the yield? The basic definition of yield is that it's the money you make expressed as a percentage of the investment; so, if you make £10,000 a year from a £100,000 investment, your yield in simple terms is 10 per cent (i.e. £10,000 is 10 per cent of £100,000). Of course, the reality is that if you have borrowed money to invest then the yield will be based on the money you have left after borrowing repayments have been met expressed as a percentage of the actual amount of money you put in. And if you have SIPPed the deal for tax breaks, that too will have a positive impact on yields.

For comparison purposes, the basic yield is used by most people. Clearly, you'll know what you'll be putting in. The variable is the occupancy rate, of course. You'll know what your share of the revenue is but check; where is the, say, 50-50 split made? Do you get 50 per cent of net profit after costs and the hotel's guaranteed sum of money are taken? Look closely at guaranteed yields up in double figures to make sure you are not overpaying at the outset to finance these.

What's the sell-on profit? This is, at the present time when there are limited track records, widely regarded as being the hardest to predict. With most buy-to-let investments, a relatively low yield (say 5 per cent) is often acceptable to investors as the bulk of the money is made from capital appreciation at resale. With hotels, there is greater emphasis on the yield (and the free use of the room to the investor for so many nights of the year). With this being a relatively new concept, there is little to show what capital appreciation might be.

As is often the case, much depends on supply and demand – if the hotel has sold all of its rooms, occupancy rates are, say, 70 per cent and yields are in low double-digits, then there may well be a resale market at more than the original price paid. The hotel itself may offer a buy-back deal. Some deals of this kind give the hotel 'first refusal' on buying back the room if or when it comes to resale. But, bottom line, if an investment is profitable, it's usually possible to find a buyer for it.

UKPA's Hotel Introductions: UK Property Alerts and International Property Alerts can both introduce members to UK and overseas hotel deals that stack up well. Email Iain at iain@ukpropertyalerts.co.uk.

PROPERTY INVESTING IDEA

Yes,
WHY FRACTIONAL OWNERSHIP IS SEEING GROWING DEMAND RIGHT NOW

David Burgess, The Hotel Investment Company.

Fractional ownership has become a 'hot' topic over the past 12 to 18 months. There are many attractions although would-be investors should also be aware of the downsides. Here's our view of this idea...

Get the know-how on fractional ownership. There has been a lot written about fractional ownership and timeshares by property lawyer Peter Esders for Property Alerts in recent months and, as always, he has offered sound and sensible advice. Peter clearly has a wide experience of the various schemes that are on the market. My own understanding of the fundamental difference between fractional and timeshare is that with a fractional purchase you actually own a fraction of the property. Many members will be aware of the same basic idea whereby you can own a part of a racehorse. I have a little experience of this – 5 per cent's worth! There is no way that I could afford full ownership of a racehorse but by buying in a syndicate, this brings the costs down and, as with many property deals, brings many of the same perks as outright owners. I'm not going to try to make any further comparison between owning a fraction of a (losing) racehorse and a property but it does make the point that the concept itself is not a new one.

Fractional or timeshare? As a company - The Hotel Investment Company - we've come relatively late into the fractional property market but have watched with interest over the last 12 to 18 months as the fractional lobby has attracted an increasing amount of column inches in the media. There are obvious comparisons with timeshare which has never really successfully managed to shake off the bad image created by the high-pressure selling tactics that some of the companies involved have employed.

Members will be widely familiar with the age-old stories that have come out of Spain and the Canary Islands etc where holiday-makers have signed up for over-priced timeshare deals that they've then struggled to disentangle themselves from once they get back home. At the same time, however, a balanced look at the surviving timeshare companies shows that this can in fact be a good product and I know a number of people who are perfectly happy with their timeshare purchases. Even so, timeshare generally has a 'dodgy' reputation and fractional ownership is sometimes tarred with the same brush.

Recognise the pros and cons. In the property market, fractional ownership brings the opportunity to own a share in a property that either you would not yourself be able to afford, or even if you could, would not want to own outright. You may wish to diversify your portfolio, investing in different types of property or locations. As indicated, even a part-share of a property brings with it many of the benefits of whole ownership. However, there are, as I see it, number of potential practical problems with fractional ownership.

For example, if you own a property with three others, you each might have different expectations; one might want achieve maxi-

mum rentals, another might want to use it during the peak rental season, and so on. One party might see themselves as the 'main owner' and try to make all the decisions. And then what happens if one party wants to sell and another doesn't? The fact is that, whoever you go in, circumstances change so, before proceeding you need legal advice and a watertight agreement.

What's happening now? Developers who are now bringing fractional properties to the market have looked at the downsides and are starting to put together structures to reduce these. Buyers know what they are buying into and also that there is often an exit strategy built into the deal. Examples I have seen recently include a developer's buy-back option at an agreed stage and also the compulsory sale of the property, again at a fixed time; say, after 10 years of ownership.

The increased interest in fractional is largely due to market conditions with some investors wanting to buy in but being unable to afford a whole unit and, at the same time, developers trying to maintain a decent level of sales. To sell off fractions of a property is, in some cases, a response to not being able to sell the whole property. However, it does raise an issue when it comes to investing, say, £16,000 instead of perhaps £80,000. Just because a purchase is cheaper doesn't make it better. Sure, the lower price will attract more interest but is it a good buy/investment?

Do the usual due diligence. It may be the tempting to perhaps do less checking as either you are not spending as much as you would with a whole property or maybe you are thinking that because other people have bought they'll have effectively done the research and wouldn't be buying in if it wasn't a good deal. Of course, other investors may be smart or not-so-shrewd, assuming that you have done the research so it must be a good buy etc! Again, our advice would be to get proper legal advice at all stages, especially when buying overseas. Just because there aren't taxes to pay in the country you're thinking about buying in, it doesn't mean that you won't have to pay tax here! When looking at any fractional investment we would suggest: be sure about exactly what you are buying; do your research about the calibre of the companies involved, the developers and whoever is managing the resort; assess the exit strategy so that, if you want to sell your fraction, you know there is a built-in process. And, sorry to repeat myself, but get legal advice first!

About David Burgess; David runs The Hotel Investment Company with Jeannie Lumb. You can find out more via David@thehotelinvestmentcompany.com, quoting 'Property Alerts'.