

Hotels' Hidden Capital

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Abstract


- Capital actually is everywhere.
- Capital formation comes from
 1. Stock Accumulation
 2. Value Flow Enhancement
 3. Option Value Creation
 4. Non-financial Capital
- Uncertainty in our borderless and IT connected world would unavoidably continue in rapid pace.
- Time is a very important alliance (or enemy).
- Flexibility is the key to survive and prosper in new world.
- Adoptability is the tool to cope with fast changing world.
- To form and accumulate capital needs knowledge and know-how apart from network and endowment.

 **Agenda : Hidden Capital**

1. Chilling Trends
2. Capital Ideas
3. Mystery of Capital - Implications
4. Conclusions

 **Chilling Trends for hoteliers**

1. **Uncertainty Economy** – SARS, Terrorism Risks, etc.
Learn to live with volatility – **Flexibility** is the key.
2. **Budget Airlines** – Changing of travel patterns
Growing two tier markets – **Adaptability** is the virtue.
3. **Internet Economy** – Changing buying patterns / economy
more price transparency, diversity vs consistency, short time to the market, Wi-Fi access, ...reduced commission..

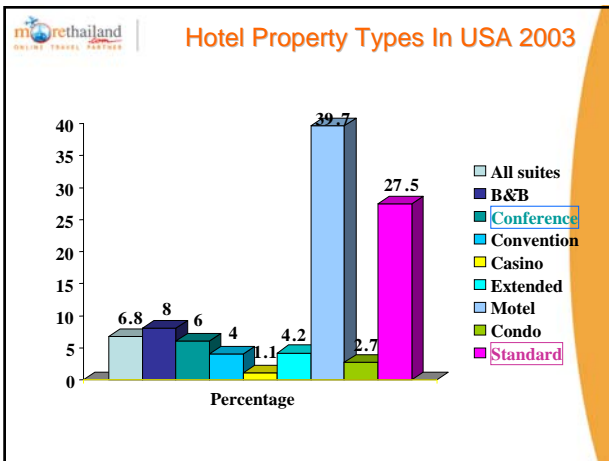
 **Capital Market for Airline**

Top ten airlines by:

Market cap, \$bn	Mar 23rd 2004	Revenue-passenger-kilometres, bn, 2003*	
Southwest Airlines	10.5	American Airlines	153.2
Singapore Airlines	7.6	United Airlines	167.2
Emmy Pacific Airways	6.7	Delta Airlines	152.0
Japan Airlines	6.2	Northwest Airlines	110.2
Lufthansa	6.0	Japan Airlines	164.0†
British Airways	5.2	British Airways	101.1
All Nippon Airways	5.1	Air France	100.2
Qantas Airlines	4.7	Lufthansa	93.0
Ryanair	4.0	Southwest Airlines	77.2
Thai Airway**	2.4	Qantas Airlines	76.9

Sources: FactSet; company statistics

*Airlines with available data only †2002





Who needs capital ? .. Handling Hostile Hotel Environment

All you need is capital to survive and prosper in this ever changing, hostile hotel environment.

- To the owners:
 - Capital Market for Hotelier: Love me or Love me not
 - Hidden Capital coming from wealthy individual with tax + reasons
 - Need knowledge capital rich workers to manage their property.
- To the operators:
 - The Force of Majeure: 'Act of Gods', Terrorist Risk
 - Brand standard eroded
 - Need to 'buy in' block assurance
- To the lenders:
 - Possible work-out or restructuring
 - Nearly all private capital asset needs financing.

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 **Capital Ideas**

What is capital ?

- Resources invest to create new resources.
- Make an investment in and then get a stream of benefits.
- As a accumulation and reproduction process.
- Classification thoughts are as follows:
 - Man-made v.s. national resource
 - Tangible v.s. intangible capital
 - Financial v.s. non- financial capital

 **Capital Ideas**

1. **Stock Approach** – On Balance Sheet
 $Asset = Capital \text{ (or Equity/ Surplus) } + Liability$
2. **Flow Approach** – On Income and Expenditure Statement
 $Financial \text{ Value} = Present \text{ Value of all future cash flow}$
3. **Option Approach** – Off Balance Sheet: Allotment, Time Sharing, Fractional Ownership/Membership ... as functions of Time and Flexibility.
4. **'Non-financial' Approach** -
 Social Capital, Customer/ Relationship Capital, Structural Capital, Human Capital....

1. Balance Sheet Ideas

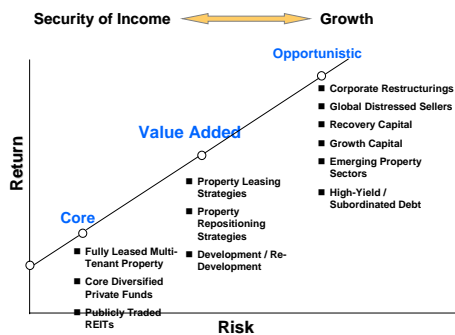
On balance sheet approach :

1. **Debt capital** is, by far, the cheapest additional capital to raise.
2. Fundamental considerations before seeking debt finance
 - 2.1 Business Risk
 - 2.2 The need for financial flexibility
 - 2.3 Risk aversion
 - 2.4 Tax consideration
3. There are four main sources of debt financing
 - 3.1 Bank financing
 - 3.2 Insurance Company
 - 3.3 Securitization – Conduit-loan or single asset.

IMPORTANT – Leverage can be beneficial during good time, but during bad time its **financial distress** can be unbearable.

See more Elgonemy June02

Risk-Return Spectrum of Real Estate (Hotel/resort Property) Investing




Re-capitalize on B/S idea

During ‘bust’ time, all debt restructuring = **‘creative financing’**

1. **‘Hotel debt restructuring’** refers to general reformation cases where the lender has incurred no losses. Steps are
 - 1.1 Reducing interest rate to reflect new mkt fundamental
 - 1.2 Extending the repayment period and
 - 1.3 Granting a grace period...

IMPORTANT – **‘Creative financing’** should be done **before** the foreclosure or during the non-distressed time.

See more Elgonemy June02

 **Re-capitalize on B/S idea**

During 'bust' time, all debt restructuring = **'creative financing'**

2. **'Troubled-debt restructuring'** refers to the cases where the lenders incur losses from the restructuring.

- 2.1 Reduction of the principal or accrued interests.
- 2.2 Loss from Restructuring through acceptance of a transfer of assets whose value is lower than market value
- 2.3 Concessions is loan repayment rest than NPV and
- 2.4 Loss from the debt restructuring.

IMPORTANT – If you are not as big as your lender, then you are likely to lose your ownership !! Bank is normally a senior debt claimer.

See more Elgonemy June02


 **2. Cash Flow Mgt idea**

When hoteliers prefer to maintain control of positive outcome rather than leaving them to chance. **Cash flow management** is a very vital with mixed strategies for cash upfront as follows:

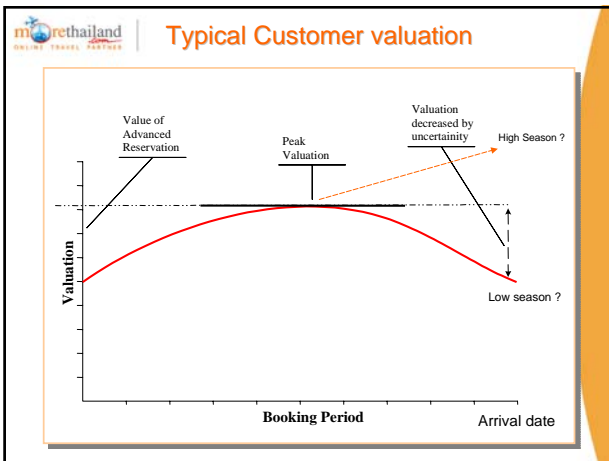
1. **Prepaid voucher or allotment:** Good positive inflow reduce financial distressed and better room inventory management.
2. **Prepaid pricing "value coupons"** for restaurant, spa, fitness:
3. **Price discount coupons** for restaurant...: uses to develop market share. The key is to give this to new customer, not just existing customer.

IMPORTANT – **Time** is becoming an important alliance. **Flexibility** brings you more friends than foes.

See more Elgonemy June02

 **2. Cash Flow and Inventory Mgt- Why advanced sales with discount**

1. **The tourist travelers**, whose demands are more certain with long lead time and therefore cheaper to serve.
2. Increasing the number of **business travelers** increases occupancy rate and increases the expected price that travelers pay.
3. **Bottom line:** Like airlines, hoteliers can have a **mixed customer based**. The use advanced purchase discounts can increase their share of low cost consumer, to reduce the uncertainty in demand and to manage their cash flow and to increase their capital.



3. "Better Option" - Capital

Reasons for hotels to sell allotment, Time Sharing, Fractional Ownership/Membership

- Cost Advantages :
- Management options :
- Risk transfer :
- Transaction cost :
- Asymmetric information:

Off Balance sheet (B/S) adds valued capital to the hotels.

Everything in (hoteliers') life is an option.
Ex: selling a room, allocating allotment, timeshare...

Timeshare as an option

- **Timesharing**
 - A term used to describe the joint ownership of a resort
 - Property by several families. Each family owns a certain period of time.
- **Features & Information**
 - Timesharing began in French Alps in the 1960's
 - Concept immigrated to U.S. in 1970's.
 - By 1998, the fastest growing sector with \$3 billion sales volume with 1.9 million owners.
 - In 2003, Marriott is the biggest time share operators in the world with sale over 1.0 billion USD
 - In Thailand, timeshare had started in Phuket in late 1990's. Now, there are a pocket of timeshares in major tourist attraction.

WARNING – Because the lack of law, regulation and in-depth knowledge, there are plenty of frauds and scams opportunities !!!

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Timeshare and Its principal benefits

- Consumers found it quite attractive due to good experience (87%) and to financial benefit (53%).
- Developers focus on financial goals – property value.
- Hospitality operators can coordinate both sides and achieve their own goals (career/biz development).

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    graph TD
      A["(Real Estate)  
Developers/Hoteliers"] <--> B["Hospitality  
Operators"]
      A <--> C["Consumers"]
      B <--> C
  
```

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4. Non-financial Capital

1 Social Capital refers to the institutions, relationships, and norms that shape the quality and quantity of society's social interactions. **Sources of Social Capital** are:

- Families: the main source and first building block
- Communities: good substitutes for human/physical capital
- Peers and Firms: Trust and common sense of purpose to reduce transaction cost
- Civil society: NGO provides a platform for voices
- Public sector: central to the functioning and welfare
- Ethnicity: share common values/culture for mutual benefit
- Gender : man, woman, gay...

See <http://www.worldbank.org/poverty/scapital/topic/fin1.htm>

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Another Three Types of Capital

- 1. Human capital**
 - Knowledge, skills, and innovativeness of employees as well as company values, culture, and philosophy.
- 2. Structural capital**
 - Capabilities embedded in hardware, software, databases, organizational structure, patents, and trademarks.
- 3. Customer capital**
 - relationships with a company's customers including the intangible loyalty of its customers to the company or a product, based on reputation, purchasing patterns, or the customers' ability to pay.

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Intellectual Capital

Intellectual Capital/ Stage of development	Human capital	Customer capital	Structural capital
Knowledge resources	Tacit knowledge, vision	Experience, knowledge, relations	IT databases, knowledge base, best practices, culture
Innovation resources & processes	Ideas, product concepts, skills	Ideas, product concepts, feedback	Work systems, business processes
Intellectual property	Know-how, trade secrets	Brand identity, reputation	Patents, trademarks, copyrights

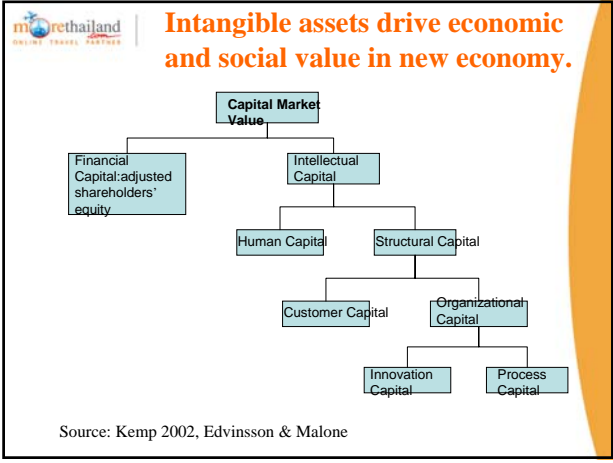
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- ### Agenda : Hidden Capital
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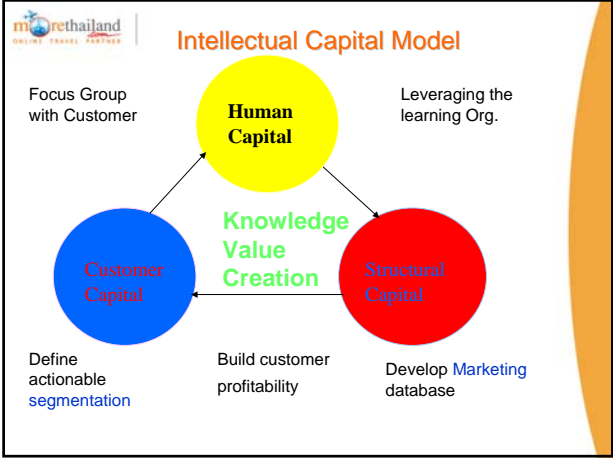
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- ### Hoteliers' organizational capital
- | | | |
|---|------|--|
| <p>Old Ways</p> <ul style="list-style-type: none"> ▪ Rules ▪ Planning ▪ 'Bean counters' ▪ Predictability ▪ Tasks ▪ Budgets ▪ Assets ▪ Make 'long lasting' decisions ▪ Are right most of the time | V.S. | <p>New Ways</p> <ul style="list-style-type: none"> ➢ Flexibility ➢ What ifs ➢ Investors ➢ Uncertainty ➢ Objectives ➢ Resource Flexibility ➢ Knowledge ➢ Accuracy is not needed ➢ Conceptual ➢ Utilise "Team" |
|---|------|--|

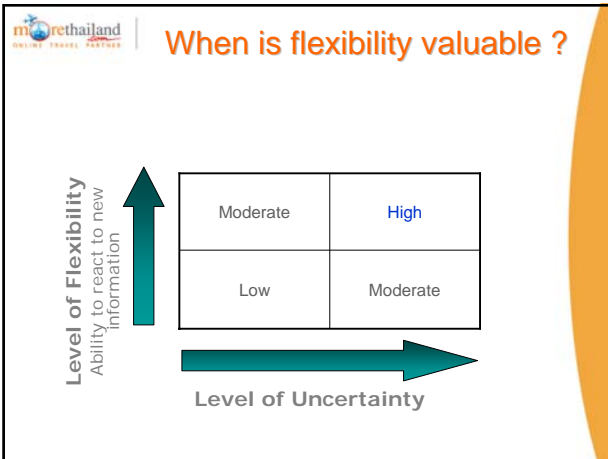
Fin. Value Creation by Risk and Equity Sharing to meet different niche investors n travelers

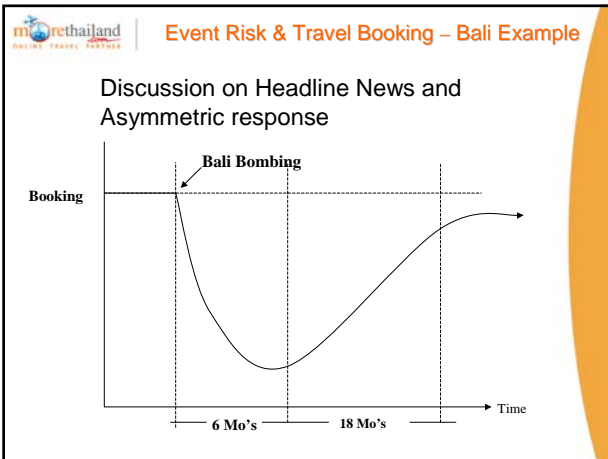
Comparison Between Vacation Ownership Type

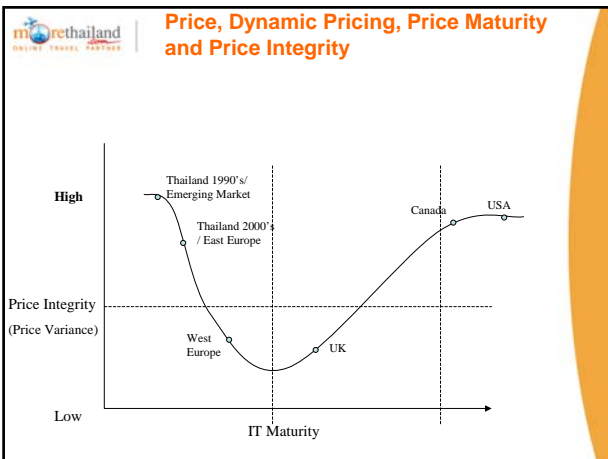
	Condo-Hotel	Apartment	(Non-Brand) Time Sharing	Exclusive Membership Club
Private Resort			✓	✓
Multiple Location	✓	✓		✓
Affordable	✓	✓	✓	✓
No Hassles	✓	✓		✓
Availability				✓
Luxury Amenities	✓		✓	✓
Inventory Liquidity	Low		Medium	Medium
Title - Deed	✓			✓
Securitized Paper	✓		?	✓

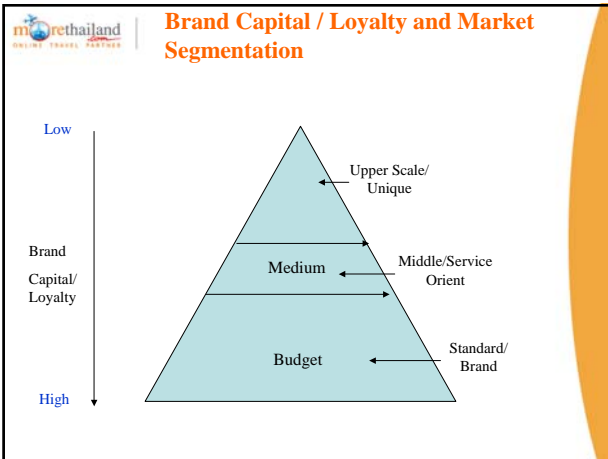






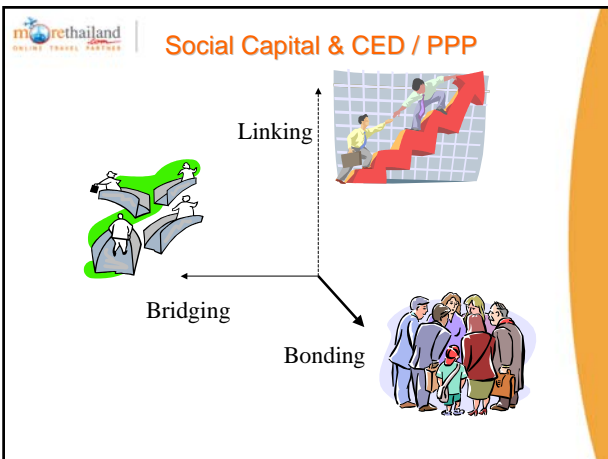






Some Key Insights from Option Thinking

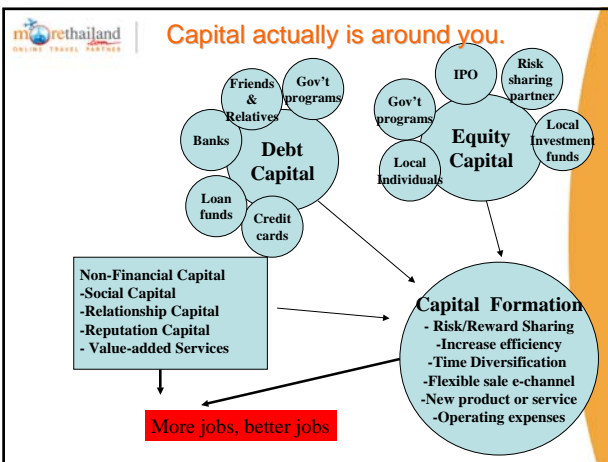
- Don't fixate on the most likely scenario.....*Remain flexible.*
- Sell (or Invest) in stages.....*Each step provides information.*
- Pursue several paths at once.....*Expect failure.*
- Volatility can enhance value when you keep your options open.*
- Growth opportunities and flexibility transform the hoteliers' risk.*



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Dimensions of Social Capital: Implications for Community Building


BRIDGING	
<p>Community change driven by goals of outsiders, often mediated through local bosses</p> <p>-</p> <p>Rich solve problems through financial capital Poor have few options</p>	<p>+</p> <p>Community change driven by community-determined goals and linked to external resources</p> <p>+</p> <p style="text-align: right;">BONDING</p> <p>Community resists change, often groups within the community don't trust each other and do not cooperate</p> <p>-</p>



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Conclusion (1)

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Reference - for further reading

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*Available for free download at www.Pongsak.Hoontrakul.com

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Any comments are welcome
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