



The Financial Impact of Hotel Spas

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The popularity of spa facilities in hotels and resorts has exploded in recent years. For many full-service and resort properties, spas are as much a requirement as restaurants and meeting space. From an operational perspective, the success of a spa does affect a hotel's financial performance, both as an operating department and as a marketing asset. Anecdotally, operators report the addition of an effectively planned spa can improve a property's RevPAR (revenue per available room), allowing the property to sustain its competitive position. The following sets forth some financial statistics from spa operations and considers the economic impact of a spa on a hotel's value.

Spa Operating Performance

Statistical data culled from spa operations in hotels and resorts indicates that spas are not only an expected guest amenity, but can add to the profitability of a hotel or resort. HVS International provides appraisal and consulting services for hotels and resorts around the world. For the purpose of this study, data was collected from spas in hotels located in urban and destination resort areas from coastal California to Orlando, Florida. The spas ranged from 3,500 square feet to 45,000 square feet, with 2 to 43 treatment rooms. Properties for which several years of spa operational performance was available were selected.

The following data (Table 1) includes the composite results from 13 properties containing a total of over 4,600 guestrooms. The initial trend indicated by the data is that while revenue increased during the three years analyzed,

the greatest impact on the departmental profitability is improved operational efficiency. On an aggregate basis, spa revenues increased at a faster pace than expenses, resulting in significant improvements in departmental profitability. The spa comparables indicate an average expense ratio of roundly 74% in 2003, down from an average of roundly 81% in 2005, as a result of greater revenues and good expense control.

For the composite hotel performance illustrated in the preceding chart, hotel RevPAR increased roundly 11% from 2003 to 2004 and 10% from 2004 to 2005, while spa revenue per occupied room increased roundly 21% and 4%, respectively, in the same periods.

As with other hotel operating departments such as food and beverage, spa operations illustrate a wide range of results from hotel to hotel. Factors such as property location, spa design and operating structure, importance of the spa to the hotel's identity, spa size, hotel market position, and competition from other amenities such as golf courses all affect spa revenue potential.

The data from the sample of 13 hotels, which ranged in size from 99 to 1,042 rooms, indicates that spa revenue does not show consistent correlation to any particular property attribute. For some hotels, spa revenue per available room grew faster than RevPAR.

Whether evaluating an existing spa operation or planning for a new facility, an analysis of spa performance is highly

Table 1: Spa Department Trends

Year	Spa Revenue	Percent Change	Revenue per Treatment Room	Revenue per Square Foot	Revenue per Occupied Room	Percent Change	Spa Expenses	Percent Change	Spa Expense Ratio
2003	\$24,764,000	—	\$135,322	\$118.58	\$22.73	—	\$20,084,000	—	81.1 %
2004	32,727,000	32.2 %	178,836	156.71	27.49	20.9 %	24,803,000	23.5 %	75.8
2005	35,435,000	8.3	193,634	169.67	28.54	3.8	26,098,000	5.2	73.7



dependent on the market orientation of the hotel property and the physical and operational attributes of the spa. In our survey, the existing spas averaged 19,300 square feet. Table 2 shows the size distribution of the sample.

Table 2: Spa Square Footage

Property	Spa Square Feet	Number of Treatment Rooms	SF per Treatment Room
A	45,000	27	1,667
B	3,500	8	438
C	27,560	25	1,102
D	20,000	26	769
E	12,000	17	706
F	9,000	9	1,000
G	43,000	15	2,867
H	9,141	6	1,524
I	30,000	18	1,667
J	6,000	2	3,000
K	26,000	43	605
L	10,000	9	1,111
M	10,200	14	729
Average	19,339	17	1,148

The number of treatment rooms does not consistently correspond to spa size. Many of the spas contain relaxation areas and merchandise displays. Several of the spas include large exercise areas that attract local and day users who are not active spa consumers.

Spa Revenue Analysis

Based on the data analyzed, spa revenues are divided into three main categories: spa service revenue, spa retail and other revenue, and spa membership and daily-use revenue. The majority of spa revenue comes from spa services such as massages, facials, nail services, and so forth. Depending on the facility program of the spa, spa service revenue ranged from 48.2% to 93.1% of total spa revenue. All of the spas sampled also included retail revenue from spa merchandise and products. For the properties included in the sample, spa retail revenue contributed 6.4% to 18.5% of total spa revenue. Most of the spas also generate revenue from spa membership and daily-use revenue, which include fees to use the general spa or fitness facilities. Membership and day-use revenue can be substantial depending on the exercise facilities and the hotel or resort’s location relative to a large residential population base. Many hotels and resorts actively promote a local membership program for spa facility use. Typically,

those hotels that include this program offer extensive workout facilities as part of the spa so the spa is an alternative to a local health club. If the hotel or resort has the right facilities and a supportive surrounding residential population, the revenue contribution of a membership program can be substantial.

Because the membership contribution can be a major revenue source for a spa operation, revenue contribution ratios for spas with membership and daily-fee programs were compared to those for spas without such programs. For spas that include spa membership and/or daily-use revenue, these revenues ranged from 1.6% up to 44.5% of total spa revenue, at an average of 13.1%. Spas that include spa membership revenue had spa service revenues ranging from 48.2% to 90.2%, at an average of 75.1%. These spas had spa retail and other revenues ranging from 1.6% to 44.5%, at an average of 11.8%.

Table 3: Averages for Spas with Membership Revenue

Spa Service Revenue as a % of Total Spa Revenue	Spa Retail & Other Revenue as a % of Total Spa Revenue	Spa Membership & Daily Use Revenue as a % of Total Spa Revenue
75.1 %	13.1 %	11.8 %

Spas that do not include membership revenue had spa service revenue ranging from 81.5 to 93.1% of total spa revenue, at an average of 88.7%. In addition, spa retail and other revenue ranged from 6.8% to 18.5%, at an average of 11.9%.

Table 4: Averages for Spas with No Membership Revenue

Spa Service Revenue as a % of Total Spa Revenue	Spa Retail & Other Revenue as a % of Total Spa Revenue
88.7 %	11.9 %

While the revenue composition for the spas varied, the data does not reveal a correlation between overall department profitability and the revenue mix.

Net Operating Income and Feasibility Analysis

A spa can have a number of different impacts on a hotel or resort operation. Depending on the investor’s objective and the market position of the property, a spa can be included to help sustain a property’s RevPAR, and/or to improve its RevPAR and competitive positioning, and/or to



enhance net operating income. Spa facilities do not always contribute significantly to a property's net operating income, but, at the very least, the department should not cause a reduction in overall property profitability. To illustrate the financial impact of a spa department on overall hotel performance, we compared the hypothetical operating statements of a full-service property with a spa to that of a base case scenario without a spa operation, and that of a spa generating a reasonable return on the spa development cost. A return on investment analysis was then performed to demonstrate the potential return on the addition of a spa facility.

Table 5 sets forth three operating statements. The first statement shows the profit and loss data for the base case scenario, a property without a spa. The second statement includes a spa facility where the expense level of the department results in the same net operating income as the base case. The third statement shows a spa with an expense level that provides a net operating income for an acceptable return on the spa's development cost.

All things being equal, the spa, in this hypothetical scenario, has to operate at a modest departmental profitability level (92.9%) for the property to achieve the same overall net operating income as that of the facility without a spa (base case). Increased operational efficiencies would result in positive increases to the net operating income dollars compared to the facility without a spa. This would indicate that running spa departmental expense margins in line with the averages set forth earlier would contribute significantly to the bottom line. But even with the average expense level, the spa department would not generate enough incremental income to warrant its development.

To estimate the incremental income necessary to support the spa development in this hypothetical scenario, a market rate of return was applied to an estimated spa build-out cost. Based on published articles, the cost of building a spa in 2006 dollars is estimated at roundly \$650 per square foot. Assuming an 18,000-square-foot spa, the turnkey development cost would be roundly \$11,700,000.

Table 5: Financial Performance Comparison

	Base Case				Operational Spa Breakeve				Positive Spa ROI				
Number of Rooms:	400				400				400				
Occupancy:	75%				75%				75%				
Average Rate:	\$219.18				\$219.18				\$219.18				
RevPAR:	\$164.38				\$164.38				\$164.38				
Days Open:	365				365				365				
Occupied Rooms:	109,500				109,500				109,500				
REVENUE		% Gross	PAR	POR		% Gross	PAR	POR		%Gross	PAR	POR	
Rooms	\$24,000	52.5	\$60,000	\$219.18	\$24,000	48.7	\$60,000	\$219.18	\$24,000	48.7	\$60,000	\$219.18	
Food	12,500	27.3	31,250	114.16	12,500	25.4	31,250	114.16	12,500	25.4	31,250	114.16	
Beverage	5,000	10.9	12,500	45.66	5,000	10.2	12,500	45.66	5,000	10.2	12,500	45.66	
Telephone	250	0.5	625	2.28	250	0.5	625	2.28	250	0.5	625	2.28	
Spa/Health Club	0	0.0	0	0.00	3,500	7.1	8,750	31.96	3,500	7.1	8,750	31.96	
Other	2,500	5.5	6,250	22.83	2,500	5.1	6,250	22.83	2,500	5.1	6,250	22.83	
Other Income	1,500	3.3	3,750	13.70	1,500	3.0	3,750	13.70	1,500	3.0	3,750	13.70	
Total Revenues	45,750	100.0	114,375	417.81	49,250	100.0	123,125	449.77	49,250	100.0	123,125	449.77	
DEPARTMENTAL EXPENSES *													
Rooms	6,000	25.0	15,000	54.79	6,000	25.0	15,000	54.79	6,000	25.0	15,000	54.79	
Food & Beverage	13,000	74.3	32,500	118.72	13,000	74.3	32,500	118.72	13,000	74.3	32,500	118.72	
Telephone	125	50.1	313	1.14	125	50.0	313	1.14	125	50.1	313	1.14	
Spa/Health Club	0	0.0	0	0.00	3,253	92.9	8,133	29.71	2,461	70.3	6,151	22.47	
Other	1,500	60.0	3,750	13.70	1,500	60.0	3,750	13.70	1,500	60.0	3,750	13.70	
Total	20,625	45.1	51,563	188.36	23,878	48.5	59,695	218.06	23,086	46.9	57,714	210.83	
DEPARTMENTAL INCOME	25,125	54.9	62,812	229.45	25,372	51.5	63,430	231.71	26,164	53.1	65,411	238.94	
UNDISTRIBUTED OPERATING EXPENSES													
Administrative & General	3,500	7.7	8,750	31.96	3,500	7.1	8,750	31.96	3,500	7.1	8,750	31.96	
Marketing	2,800	6.1	7,000	25.57	2,800	5.7	7,000	25.57	2,800	5.7	7,000	25.57	
Prop. Operations & Maint.	2,000	4.4	5,000	18.26	2,000	4.1	5,000	18.26	2,000	4.1	5,000	18.26	
Utilities	1,600	3.5	4,000	14.61	1,600	3.2	4,000	14.61	1,600	3.2	4,000	14.61	
Total	9,900	21.7	24,750	90.41	9,900	20.1	24,750	90.41	9,900	20.1	24,750	90.41	
HOUSE PROFIT	15,225	33.2	38,062	139.04	15,472	31.4	38,680	141.30	16,264	33.0	40,661	148.53	
Management Fee	1,373	3.0	3,431	12.53	1,500	3.0	3,750	13.70	1,478	3.0	3,694	13.49	
INCOME BEFORE FIXED CHARGES	13,852	30.2	34,631	126.51	13,972	28.4	34,930	127.60	14,787	30.0	36,967	135.04	
FIXED EXPENSES													
Property Taxes	1,200	2.6	3,000	10.96	1,200	2.4	3,000	10.96	1,200	2.4	3,000	10.96	
Insurance	600	1.3	1,500	5.48	600	1.2	1,500	5.48	600	1.2	1,500	5.48	
Reserve for Replacement	1,830	4.0	4,575	16.71	1,950	4.0	4,875	17.81	1,830	3.7	4,575	16.71	
Total	3,630	7.9	9,075	33.15	3,750	7.6	9,375	34.25	3,630	7.3	9,075	33.15	
NET INCOME	\$10,222	22.3	\$25,556	\$93.35	\$10,222	20.8	\$25,555	\$93.35	\$11,157	22.7	\$27,892	\$101.89	

*Departmental expenses are expressed as a percentage of departmental revenues.



If the investor required an 8.0% return on that cost, the incremental net operating income resulting from the spa operation would have to be \$936,000.

The total hotel net operating income of the base case in our hypothetical property is \$10,222,000. The incremental spa income would increase the net operating income to \$11,158,000. As illustrated in the preceding chart, the “Positive Spa ROI” shows that the spa department would have to operate at an expense level of 70.3%, slightly below the average expense ratio from 2005, to generate an 8.0% return on the spa investment.

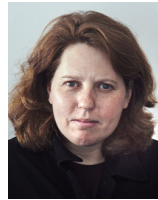
Table 6 shows the assumptions for this analysis.

Table 6: Return on Investment Analysis

Spa Addition	18,000	square feet
Construction Cost per Square Foot	\$650.00	
Estimated Development Cost	\$11,700,000	
Net Operating Income with Spa	\$11,160,000	
Net Operating Income Base Case	10,222,000	
Incremental NOI	938,000	
Capitalization Rate	8%	
Indicated Investment Value	\$11,700,000	

In an actual operating scenario, it could be that the incremental income would be contributed by additional rooms revenue, if the spa enhances the property’s RevPAR. In many scenarios, adding a spa facility to a hotel or resort property can result in a positive impact on a property’s overall operating performance, including higher room rates, occupancy, and more patronage of the food and beverage outlets. Of course other criteria should be considered in the decision such as available space or alternate uses, the hotel’s market mix and area’s residential demographics, a survey of competitive spas, and so forth. A developer should perform an ROI analysis to determine the feasibility of the spa project. At their current profitability trends, spas generally enhance hotel performance, but generating a return on the spa investment will depend on departmental operating efficiencies and RevPAR enhancement.

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