

1-1-1988

## Toward A Better Understanding of the Evolution of Hotel Development: A Discussion of Product-specific Lodging Demand

John A. Camella  
*Laventhol & Horwath*

Follow this and additional works at: <https://digitalcommons.fiu.edu/hospitalityreview>



Part of the [Hospitality Administration and Management Commons](#)

---

### Recommended Citation

Camella, John A. (1988) "Toward A Better Understanding of the Evolution of Hotel Development: A Discussion of Product-specific Lodging Demand," *Hospitality Review*: Vol. 6 : Iss. 2 , Article 2.

Available at: <https://digitalcommons.fiu.edu/hospitalityreview/vol6/iss2/2>

This work is brought to you for free and open access by FIU Digital Commons. It has been accepted for inclusion in *Hospitality Review* by an authorized administrator of FIU Digital Commons. For more information, please contact [dcc@fiu.edu](mailto:dcc@fiu.edu).

---

# Toward A Better Understanding of the Evolution of Hotel Development: A Discussion of Product-specific Lodging Demand

## **Abstract**

In his essay - Toward a Better Understanding of the Evolution of Hotel Development: A Discussion of Product-Specific Lodging Demand - by John A. Carnella, Consultant, Laventhol & Horwath, cpas, New York, Carnella initially describes his piece by stating: “The diversified hotel product in the united states lodging market has Resulted in latent room-night demand, or supply-driven demand resulting from the introduction of a lodging product which caters to a specific set of hotel patrons. The subject has become significant as the lodging market has moved toward segmentation with regard to guest room offerings. The author proposes that latent demand is a tangible, measurable phenomenon best understood in light of the history of the guest room product from its infancy to its present state.”

The article opens with an ephemeral depiction of hotel development in the United States, both pre’ and post World War II. To put it succinctly, the author wants you to know that the advent of the inter-state highway system changed the complexion of the hotel industry in the U.S.

“Two essential ingredients were necessary for the next phase of hotel development in this country. First was the establishment of the magnificently intricate infrastructure which facilitated motor vehicle transportation in and around the then 48 states of the nation,” says Carnella. “The second event ... was the introduction of affordable highway travel.

Carnella goes on to say that the next – big thing – in hotel evolution was the introduction of affordable air travel. “With the airways filled with potential lodging guests, developers moved next to erect a new genre of hotel, the airport hotel,” Carnella advances his picture.

Growth progressed with the arrival of the suburban hotel concept, which wasn’t fueled by developments in transportation, but by changes in people’s living habits, i.e. suburban affiliations as opposed to urban and city population aggregates.

The author explores the distinctions between full-service and limited service lodging operations. “The market of interest with consideration to the extended-stay facility is one dominated by corporate office parks,” Carnella proceeds.

These evolutionary states speak to latent demand, and even further to segmentation of the market. “Latent demand ... is a product-generated phenomenon in which the number of potential hotel guests increases as the direct result of the introduction of a new lodging facility,” Carnella brings his unique insight to the table with regard to the specialization process. The demand is already there; just waiting to be tapped.

In closing, “... there must be a consideration of the unique attributes of a lodging facility relative to its ability to attract guests to a subject market, just as there must be an examination of the property's ability to draw guests from within the subject market,” Carnella proposes.

## **Keywords**

John A. Carnella, Toward a Better Understanding of the Evolution of Hotel Development: A Discussion of Product-Specific Lodging Demand, Latent demand, Specialization, Full-service, Limited-service

# **Toward A Better Understanding of the Evolution of Hotel Development: A Discussion of Product-Specific Lodging Demand**

by  
John A. Carnella  
Consultant  
Laventhol & Horwath, CPAs  
New York

*The diversified hotel product in the United States lodging market has resulted in latent room-night demand, or "supply-driven" demand, resulting from the introduction of a lodging product which caters to a specific set of hotel patrons. The subject has become significant as the lodging market has moved toward segmentation with regard to guest room offerings. The author proposes that latent demand is a tangible, measurable phenomenon best understood in light of the history of the guest room product from its infancy to its present state.*

The tale of the evolution of hotel development in this country has been told countless times. Essentially, the story line reads something like this. Throughout the early part of this century and up through World War II, the major emphasis with regard to most real estate development, hotel development included, took place in what were and what were to be the major urban areas of the United States.

Later, following the conclusion of the war, Americans took to the road. Two essential ingredients were necessary for the next phase of hotel development in this country. First was the establishment of the magnificently intricate infrastructure which facilitated motor vehicle transportation in and around the then 48 states of the nation. The second event which catapulted hotel development into its second stage was the introduction of affordable highway travel. Quite simply, once the network of roads was in place and the majority of families in America had access to a car, the development of roadside lodging facilities was but a logical extension.

Subsequent to this period, in the 1960s, more and more U.S. travelers took to the air. Primarily these airborne individuals were business people whose job responsibilities necessitated frequent and speedy travel. With the airways filled with potential lodging guests, developers moved next to erect a new genre of hotel, the airport hotel.

What happened next in terms of hotel development has more to do with this nation's demographics than its transportation venues. Beginning in the late '60s, American cities experienced a tremendous

out-migration. Urban dwellers were no longer content living among the huge skyscrapers which now composed the nucleus of the modern city. So, off they went to the land of green lawns and station wagons. Concurrent with this residential exodus was the discovery of suburbia by corporate America. Once again, hotel developers were quick to catch on. The result was the creation of a new type of facility, the suburban hotel.

Typically, these hotels were built to suit the needs of the new suburban masses. Most were commercially oriented in terms of their guest focus as well as being extremely well appointed with regard to their level of amenities and guest facilities. These attributes made them particularly attractive to those business entities which had also chosen to exit the costly inner city.

What all of these hotels have in common is a unique success. Their success stems from their ability to provide for the needs of their buying public as that public has progressed through time. Unquestionably, these properties all offered a different product package, but each is successful because it offered the right item, in the right market, at the appropriate time.

### **Product Life Cycle Experiences Transformation**

What happened next in terms of the evolution of hotel development in this country is best explained using a basic business tenet, the idea of the Product Life Cycle. Here, the reader must first accept the idea of the lodging experience as a product. This should not be particularly unfathomable because until recently, most major hotels in this country offered essentially the same lodging product, their location notwithstanding.

In the early 1980s, the lodging product matured. New areas of intense real estate development and hotel development were a part of this, but it seemed there was no great national need to be fulfilled, a fact reinforced by a distinct leveling-off of nationwide hotel occupancies. As many major markets were suffering through bad times as there were those thriving.

Over the past half dozen or so years the hotel product has experienced a tremendous transformation. No longer is it true that "A hotel is a hotel, is a hotel." The answer to stagnant market occupancies has been, unequivocally, product segmentation.

The list of the fastest growing hotel firms proves the point. What was necessary to spur additional demand for guest rooms was the advancement of the hotel product to the next phase of its product life cycle, consequently, the rush to develop properties which appeal to a particular segment of the buying public. The major products which have evolved are all variations of the traditional lodging product, but each is specific in its product offering, whereas the prior focus of hotel development had been more general in its product offering.

### **Implications Exist for Market Study Consulting Firms**

Of particular interest to firms such as Laventhol & Horwath, which specialize in hotel development market study consulting, are

the particular ramifications of this new focus of hotel development. Recently such firms have experienced an increase in their exposure to proposals for hotel developments of the all-suite, extended-stay, and economy lodging variety.

As a direct consequence of this exposure to segmented hotel development offerings, these market study consulting firms are refining and, where necessary, redefining their analysis in such a way as to give credence to the phenomenon of latent demand. It is termed "latent" because it is demand (room-nights) which was formerly unaccommodated in the market, but which is accessed with the advent of the new product offering.

Latent demand is not turnaway demand, a market-generated phenomenon in which the guest flow to a lodging market exceeds the supply of area hotel rooms at some point in time. Latent demand, on the other hand, is a product-generated phenomenon in which the number of potential hotel guests increases as the direct result of the introduction of a new lodging facility.

As logical as this concept may seem to some, it cannot be said that the idea has been embraced by all of those to whom it is relevant, including lenders, equity investors, and market study consultants. Two hotel development case studies will be examined in an effort to lend support to the inclusion of latent demand in arriving at an estimated annual occupancy for a proposed lodging facility. An evolving hotel product has necessitated the recognition of this phenomenon and made it almost commonplace in studies produced by firms involved in such consulting.

Two case histories describe hotels entering an established marketplace, one in which several lodging alternatives existed and one in which its particular lodging product had yet to be introduced. In each case, the new property was highly successful in terms of its occupancy percentage. What is most interesting, however, is that the new hotel's good business fortune did not come at the expense of its competitors, at least not to the degree which would have been expected.

### **Case One: An Economy Lodging Facility**

The first illustration offered is an economy hotel. The market into which this hotel was introduced was a large metropolitan airport. Prior to the subject hotel's entrance, the market contained 1,500 hotel rooms. The upper end of the market consisted of a 400-room facility whose average daily room rate was approximately \$100. There were 750 rooms in the middle of the market, ranging from \$70 to \$80 per night. At the lower end of the market, in terms of average rate, was a 350-room property whose average rate was close to \$50. (This last statistic is a bit misleading in that the hotel had published rates in excess of \$70. The hotel chose to market itself to airline personnel and as a result of winning this segment, which is traditionally heavily discounted, its average rate per occupied room was impacted significantly).

The new economy property was introduced into the market during the last quarter of 1985, with 200 rooms and a published room

rate more than 20 percent below those of its nearest-priced competitor. The hotel's location offers no particular competitive advantage or disadvantage.

The schedule of events was as follows. Market occupancy in 1984 was 79 percent. The beginning of 1985 saw the introduction of the 400-room first-class facility. Market occupancy in this year was 77 percent. The economy hotel entered the market at the close of 1985; its success was phenomenal. Its first year occupancy was nearly 85 percent. Most significant, however, was the hotel's impact on market occupancy, which increased four percentage points to 81 percent for 1986.

What this case offers is an excellent, and not at all inappropriate, example of supply-driven demand; 1985 saw a 36 percent increase in supply and a resultant 33 percent increase in demand. In the following year the number of rooms in the market increased by 13 percent and market demand grew by 19 percent. In microeconomic terms an obvious under-supply existed. However, traditional market study analysis would have precluded such results from any forecast even under the most optimistic scenario. Hindsight allows us to postulate as to the cause of these events and latent demand would seem to be a significant part of any solution.

### **Case Two: An Extended-Stay Facility**

Another lodging product which has arisen as a direct result of the hotel industry's move to product diversification is the extended-stay facility. This product is typically constructed in a manner similar to small townhouse units making use of a cluster arrangement and can be differentiated from its sibling, the all-suite unit, through its almost complete focus on long-term lodging demand, as well as its more residential guest room arrangement.

The market of interest with regard to the extended-stay facility is one dominated by corporate office parks. The city in question is located approximately 90 minutes from a major U.S. urban center; however, much of the surrounding area is rural. There is growth in both the population and employment base. The area has an active commercial airport as well as several small and medium-sized colleges. The lodging market itself is composed of three full-service and three limited-service properties. In 1985 the 400 rooms in the full-service segment had average room rates in the \$50 range and occupancies ranging from 70 to 85 percent. The three limited-service properties, which together had an average annual occupancy of 67 percent and an average rate in the mid-\$40 range, also contributed 400 rooms to the market.

In 1984, two years prior to the introduction of the extended-stay facility, market occupancy was 75 percent. The following year, total room-night demand grew 3 percent and market occupancy went to 77 percent. In 1986 the subject 100-unit property was added to the market. The property operated at 90 percent occupancy through its first year, with an average rate in excess of \$10 above the rest of the market.

Again, the impact on the lodging market in the area was limited. In this case, market occupancy remained at 77 percent. So, in fact,

what had happened was that the market had completely absorbed the additional rooms. This is not to say that some individual properties were not impacted, for in this case they certainly were; this point can be demonstrated through an examination of the subject extended-stay facility's annual occupancy relative to the area-wide occupancy. Nevertheless, the definition of latent demand is predicted on total market room-night demand and is measured by comparing market occupancies before and after the introduction of a new lodging facility.

Undoubtedly, the hotel's developers would contend that what happened had simply to do with their perception of a need. In the latter case, the need was for extended-stay lodging facilities. In the former case, there was a need for hotel rooms of the economy variety. What both situations demonstrate is that there must be a consideration of the unique attributes of a lodging facility relative to its ability to attract guests to a subject market, just as there must be an examination of the property's ability to draw guests from within the subject market.

What this rationale for the inclusion of latent demand in lodging market studies argues is that, in the case of the lodging product which is to be unique in the marketplace, to ignore the phenomenon of latent demand would be to neglect the true intentions of the developer where the intention is to introduce a new and different product into the marketplace, one which, in many cases, is better-suited to satisfy the hotel guest's needs.

Note: At the time of the writing, the author was a consultant with Laventhol & Horwath, New York. Currently he is employed by Balcor Management Services Company, Skokie, Illinois.