

Resort Development

*Resorts have been hard hit by
the economic recession.*

AS WITH EVERY real estate asset type, the second-home resort property market is in the midst of a severe downturn. The prospects for a turnaround are not immediate, and even the most optimistic investors feel there may be multiple quarters ahead before an uptick in activity. As a result, resort developers are embarking on strategies to minimize capital while maximizing value.

Today's real estate market conditions for second-home resorts represent a sea-change from the recent past. From 2002 to 2007, second-home sales in the United States doubled over the previous five years. This was due to several factors: cheap capital that made products

more affordable; personal income growth that provided additional net worth; a maturing strong global economy; additional capital available through refinancing by capitalizing on the rapidly rising values of primary homes; growth in baby boomers' discretionary wealth; and supply and demand imbalances due to land constraints. With the exception of land constraints, these factors are gone today. While the amount of prime resort development land is limited—coastal property is still hard to come by, for example, and there is only a limited number of prime ski areas, especially with significantly developable base area property—the sources of capital and of individual wealth creation have all but vanished. The 2009 National Association of Realtors *Investment and Vacation Home Buyers Survey* indicates a 30.8 percent drop in vacation home sales from 2007 to 2008. This is compared to a 13.2 percent drop in primary home sales and a 17.2 percent drop in investment property sales. In addition, prices of vacation homes dropped 23.1 percent in the same period. In higher-end resort markets, the statistical drop in prices has not been significant, but there has been a significant drop in volume.

To preserve the resort development industry, developers will have to work strategically to help define the conditions that will attract investment in this climate.

Early indications show that, due to reduced travel expenses, regional destinations such as New England mountain resorts are weathering the downturn better than their far-flung counterparts, such as Hawaii, which is far away from its major markets. Britons are increasingly “staying home,” according to *Visit Britain*, as they desire more value for their money. This means places like Cornwall or the Lake District are outperforming recent British destinations such as the Algarve, southern Spain, and Cyprus. Resorts are seeing a return to fundamentals wherein success lies in proven locations, association with well-established brands, and easy access—usually less than a three-hour drive from a metropolitan area, less than a one-hour drive from a major hub airport, or less than a three-hour flight for international destinations.

During the previous boom period, buyers preferred investments in products and experiences with socially responsible, philanthropic and environmentally sustainable profiles. This is expected to continue as marketing trends point toward value and well-considered purchasing. This is borne out by the notion that, at any price point, socially responsible and environmentally sustainable products will keep and retain their value. Intangible asset differentiation, especially combined with the inherent ability to acquire distressed properties in today's market,

means such products will continue to attract discerning buyers.

Throughout this downturn, what makes a resort “the best” will not change, but the strategies for achieving success are changing: smaller for-sale products, innovative accommodations, and diverse experiences. In most cases, residential sales are the primary revenue generator for resort communities. Unfortunately for developers, the current market conditions are reducing sales. There are, however, opportunities to overcome this challenge with a firm understanding of where the residential resort world currently stands.

The resort market is flush with resales of commodity developments; that is, generic resort communities built with little regard to quality and site-specific characteristics. These properties have a lower cost basis, meaning they can undercut the prices of new products. Further, lot sales will be exceedingly slow due to these resale bargains. Further compounding the problem, developers are trying to significantly reduce operating costs in an environment where the competition for buyers is intense. Buyers, however, are burdened by the need for cash and low-leverage transactions. Finally, speculative buyers, who once accounted for a significant amount of sales in the second-home resort sector, are all but gone.

LOOKING AHEAD

Looking ahead with the new realities in mind, and trying to determine how people will choose to spend their leisure time and their money, suggests a trend to for-sale products that are smaller and at lower price points. Smaller units act to minimize upfront investment and provide a basis for later phases in which a broader range of products can appeal to a broader range of buyers. Smaller units also reduce ownership costs and maintenance requirements, and give buyers the opportunity to “buy up” into larger, more expensive residences later, providing a foundation for legacy buyers as the resort community evolves.

In addition to smaller products, innovative accommodations serve to bolster the resort’s image, as well as offer opportunities for future uses. Such an approach aims to address current market realities by creating hospitality venues that lower barriers of entry for the developer, minimize infrastructure and other upfront costs, reduce operating costs, establish the community’s character, and focus on service and experience. Despite the fundamental draw of branded hotels, a 2008 survey by *Travel + Leisure* indicated the presence of big brand fatigue—eighteen of the top twenty-five hotels overall were in the “small” category. Travelers are demanding smaller, more distinct properties. Scarcity and intimacy likewise create value in hos-

pitality and second-home resorts. Thus, the need for quality comes to the fore.

For creative developers, starting small does not only mean boutique hotels, but also includes products such as founders' lodges, clubhouse cottages, or high-end tent structures. For example, a founders' lodge might include a main house with living room, dining room, bar, billiards room, and a library to serve as a central gathering area. Surrounding or attached to the main house are individual cabins or cottages for sleeping. Such an arrangement provides accommodations during the initial sales process, and is also an amenity going forward—the rooms can remain in place as guest-rooms, acting as a small high-end hotel, or the suites could be sold as a residence club.

Top resort communities are always leaders in service. This is a bottom-up approach to operations, as the staff becomes ambassadors to create memorable experiences to bring people back. Building upon service, multi-dimensional and experiential amenities create a diversity of activities for a range of users, including especially multi-generational families. With increased access to remote parts of the world, the increasing sophistication of consumers, and a desire for greater content per dollar spent, there has been a decline in popularity of conventional resorts.

Creating a diverse series of activities and places for people to come together

instills satisfaction and pleasure in the resort user and keeps them coming back. It may be easier to get a guest to visit a property just once, but the “best” places in the future will be the economically self-sustainable places where guests want to return. The follow-up visits may be to multiple hotel offerings at a resort (couples hotel versus family hotel) or varied activities via on-site or regional amenities. Further enriching are lifestyle and educational (culinary, language, history) components of the experience, sustained through multiple visits.

Amenities need not be expensive. An amenities arms race is not consistent with concepts of modesty and value. The large upfront costs required to deliver some amenities (such as golf courses) do not necessarily translate to increased value. And, as the cost of operating amenities eventually needs to be passed on to the consumer, sophisticated buyers will look at operating budgets and the likelihood of covering future cost burdens through dues increases or additional fees. Buyers will demand to know that operations can be effective and adequate within existing dues structures.

In resorts as in primary communities, the most popular places are often the least expensive, such as beaches, public parks, walking trails, and protected open spaces. Successful resort communities take advantage of their natural surroundings and the

unique aspects of the land itself. This includes history, culture, and local traditions that attracted people in the first place. Focusing on experiences, with education, environmental, health, cultural, and historical influences, celebrates the context and natural setting and creates truly one-of-a-kind locations that drive value—the collective experience maximizes value.

CONCLUSIONS

To successfully navigate today's downturn, resort developers will need to focus on a few key points: lowering risk by lowering upfront investment in infrastructure, high-rise construction, and operations; increasing and maintaining more flexibility and responsiveness to local conditions and the environment; making projects more adaptable so they can be used in multiple ways and for different purposes in the future; remembering that buyers want to feel good about their investment; and bearing in mind that scarcity and differentiation still drive value, more so now than in the past. Combining concentrations of activity and accommodations forms a density of experiences. Truly unique environments, where the experience is defined by the natural setting creating distinctive places with a strong sense of community, still command premiums.

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