



August 29, 2022

Mr. Brian Froelich  
Senior Planner  
City of Capitola  
420 Capitola Ave.  
Capitola, CA 95010

**Re: Monarch Cove Inn Feasibility Analysis**

Dear Mr. Froelich:

Kosmont & Associates, Inc. doing business as Kosmont Companies (“Consultant” or “Kosmont”) is pleased to present our findings relative to the California Coastal Commission request for a feasibility analysis of future hospitality use for the historic Monarch Cove Inn, an 11-room hotel (“Property”) on 1.4-acres owned by the Blodgett family (“Owner”), and located at 620 El Salto Drive in Capitola (“City”).

**BACKGROUND**

In 2020, the City initiated a zoning change for the subject Property from Commercial to R-1. As part of the Local Coastal Plan review, the California Coastal Commission (“CCC”) requested an independent 3<sup>rd</sup> party study to assess the feasibility of the Property to continue as a visitor serving facility. The main house was built in 1886 and has undergone extensive renovations, but overall amenities are lacking compared to competitive facilities limiting achievable room rates.

Due to its small size of 11 rooms and regulations limiting special events (i.e., weddings), the Property has been unable to generate sufficient net operating income to cover the annual debt service. CCC wants to know if there are any modifications that can be made to allow the Property to operate profitably (e.g., additional rooms, restaurant, special event facilities).

To address CCC concerns, the City retained Kosmont Companies to provide an independent assessment of the hotel operations and the financial feasibility of adding new facilities to the Property.

Consultant toured the Property and met with Owner to understand operating challenges, and see the historic financial performance records. Consultant worked with City staff to understand the terms of the existing Conditional Use Permit.



## Hotel Description

The 620 El Salto Drive Property is located at the end of a narrow cul-de-sac street. It was developed as a single family estate in the late 1890's with the construction of a ~4,000 SF main house. The family also owned most of the property along El Salto Drive. Over the years many parcels were sold to other individuals who built single family homes.

In 1991, the family converted the property into a visitor serving facility called the Monarch Cove Inn. While primarily a hospitality facility, the major source of revenue was outdoor weddings and special events prior to CUP restrictions, generating over \$250,000 per year in operating income that often exceeded the hotel room revenue.

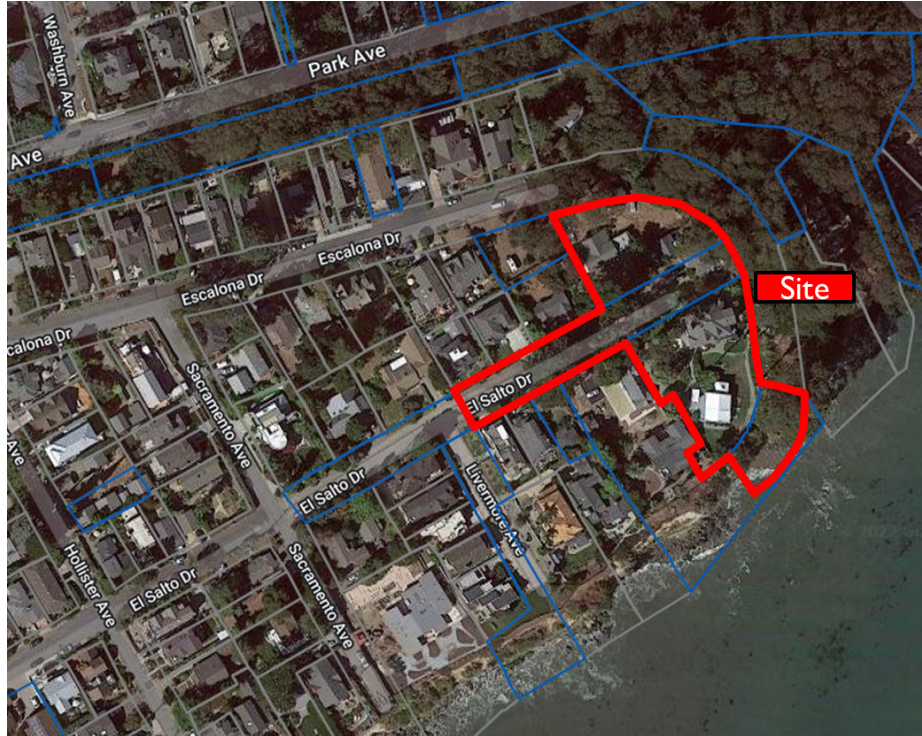
The Property is surrounded by single family residences to the north and west and the Pacific Ocean on the south. In the 1880's the property was surrounded by a 60 foot wide Escalona Drive right of way connecting to Grand Ave. The majority of Grand Avenue has been eroded away and right of way is now a pedestrian path.

The Property is comprised of 4 parcels. In the 1989 General Plan, the City designated three parcels as Visitor Serving (V-S) with the fourth parcel 036-143-36 zoned Parks and Open Space (P/OS).

Due to adjacent neighbor complaints about noise and parking on city streets, the lodging has been operates under a Conditional Use Permit since 2001, that restricts special events to no more than two per week and six per month. Events during the week (M-F) are limited to 40 people and during weekends they are limited to 75 people, which negatively impacts revenue from wedding substantially.

Another factor that has restricted guest attendance is parking. The subject Property currently has approximately a dozen parking spaces on site. Guests used to be able to park on offsite lots and drives that were privately owned. As those parcels were sold and developed, parking became an problem for the community. Property now must arrange for offsite parking and shuttle systems to bring guests at significant cost.

### Subject Property





## Hotel Operations

Kosmont gathered hotel market data for the Santa Cruz/Capitola submarket from Smith Travel Research (STR) to understand the competitive hotel market room rates and occupancy rates for the time frame pre-Covid up to the current year.

The Property has extraordinary maintenance needs with an acre of gardens and three Victorian buildings requiring a full time handyman and full time gardener. Engineering assessments have also identified the need for a new foundation and a seismic retrofit that would cost approximately \$800,000.

Table 1 shows that despite increasing hotel operating revenues, expenses have climbed faster resulting in lower net operating income and cash flow during the past 8 years.

**Table 1**

	Monarch Cove Inn Financial Performance								
	2014	2015	2016	2017	2018	2019	2020	2021	
Occupancy Rate	47%	72%	78%	81%	79%	64%	55%	82%	
Average Daily Rate	\$ 193	\$ 178	\$ 176	\$ 171	\$ 178	\$ 200	\$ 173	\$ 193	
Room Revenue (net of TOT)	\$ 364,000	\$ 516,000	\$ 552,000	\$ 557,000	\$ 564,000	\$ 515,000	\$ 382,000	\$ 634,000	
Other Revenue	82,000	97,000	54,000	46,000	58,000	42,000	14,000	29,000	
Total Revenue	\$ 446,000	\$ 613,000	\$ 606,000	\$ 603,000	\$ 622,000	\$ 557,000	\$ 396,000	\$ 663,000	
Operating Costs	\$ 317,000	\$ 355,100	\$ 433,000	\$ 463,200	\$ 463,000	\$ 387,000	\$ 357,400	\$ 523,400	
Net Operating Income	\$ 129,000	\$ 257,900	\$ 173,000	\$ 139,800	\$ 159,000	\$ 170,000	\$ 38,600	\$ 139,600	
Return on Investment /1	3.2%	6.4%	4.3%	3.5%	4.0%	4.3%	1.0%	3.5%	
Less: Debt Service /2	\$ 114,000	\$ 125,900	\$ 105,000	\$ 128,800	\$ 105,000	\$ 123,000	\$ 116,000	\$ 105,000	
Net Cash Flow	\$ 15,000	\$ 132,000	\$ 68,000	\$ 11,000	\$ 54,000	\$ 47,000	\$ (77,400)	\$ 34,600	
Source: Monarch Cove Inn									
/1 \$4 million estimated debt and equity investment									
/2 Excludes deferred interest on \$2 million loan									

As shown above, the Monarch Cove Inn has struggled for years to achieve breakeven operations, despite high room rates and strong occupancy. Wedding and other event revenues have continued their significant decline. With a return on investment of less than 4%, Owner is not able to invest in long term improvements needed to maintain a hospitality use.

## Hotel Market

The Santa Cruz / Capitola hotel market contains over 3,000 hotel rooms plus over one hundred nearby camping spaces at New Brighton State Beach and over 60 RV camp sites at Seacliff State Beach Campground.

The potential loss of 11 rooms at Monarch Cove represents less than 0.3% of the dedicated hospitality inventory, *not counting* the hundreds of single family homes renting rooms via Airbnb.com and similar websites.

Table 2 illustrates the major hotel properties in Santa Cruz/Capitola that have been historically surveyed by STR as to room rates and occupancy.

**Table 2**

Competitive Set Hotel Properties in Capitola and Santa Cruz						
Miles from Site	Property Name	Property Address	City	Hotel Class	Rooms	Year Built / Renovated
0.7	Quality Inn & Suites Capitola By The Sea	822 Bay Ave	Capitola	Midscale	55	1980
1.2	Best Western Plus	1435 41st Ave	Capitola	Upper Midscale	58	2000
1.2	Fairfield Inn & Suites Santa Cruz Capitola	1255 41st Ave	Capitola	Upper Midscale	84	2011
1.9	Seacliff Inn Aptos, Tapestry Collection	7500 Old Dominion Ct	Aptos	Upscale	148	1980
4.1	Best Western Plus All Suites Inn	500 Ocean St	Santa Cruz	Upper Midscale	77	1989 / 2022
4.1	Comfort Inn Beach Boardwalk Area	314 Riverside Ave	Santa Cruz	Upper Midscale	28	1996
4.1	Hyatt Place Santa Cruz	407 Broadway	Santa Cruz	Upscale	106	2017
4.2	Autograph Collection Hotel Paradox	611 Ocean St	Santa Cruz	Upper Upscale	170	1969 / 2012
4.3	Holiday Inn Express & Suites Santa Cruz	1410 Ocean St	Santa Cruz	Upper Midscale	100	2009
4.3	Quality Inn Santa Cruz	1101 Ocean St	Santa Cruz	Midscale	42	1972
4.4	Comfort Inn Santa Cruz	110 Plymouth St	Santa Cruz	Upper Midscale	62	1970
4.4	Best Western Inn Santa Cruz	126 Plymouth St	Santa Cruz	Midscale	28	1983
4.4	Hampton Inn Santa Cruz	1505 Ocean St	Santa Cruz	Upper Midscale	46	2000

Source: STR



Market area hotel performance metrics, based on the hotel competitive set identified above, are summarized in the Table 3 below. The data shows that Monarch Cove Inn Property achieved higher room rates (\$193) and occupancy rates(82.2%) than the competitive hotels in 2021.

**Table 3**

Market Hotel Performance: 2014 - 2021							
Year	Avg. Occupancy	ADR	Supply of Room Nights	Demand for Room Nights	Change in Occupied Room Nights	RevPAR	Change in RevPAR
2014	65.8%	\$140.27	328,135	215,790		\$92.25	
2015	70.2%	\$153.69	328,135	230,197	6.7%	\$107.82	16.9%
2016	70.2%	\$160.08	328,135	230,225	0.0%	\$112.31	4.2%
2017	70.6%	\$161.19	344,353	243,264	5.7%	\$113.87	1.4%
2018	74.3%	\$165.26	366,825	272,543	12.0%	\$122.78	7.8%
2019	74.6%	\$165.73	366,825	273,776	0.5%	\$123.69	0.7%
2020	51.8%	\$141.22	366,491	189,670	-30.7%	\$73.09	-40.9%
2021	64.2%	\$175.91	366,460	235,319	24.1%	\$112.96	54.6%
2022*	68.5%	\$157.44				\$107.77	

Source: Costar / STR

Significant seasonality is highlighted by the Capitola/Santa Cruz market's monthly performance data over the past year as summarized below:

Monthly Hotel Performance: Previous 12-month Period			
Month	Avg. Occupancy	ADR	RevPAR
Jun 21	73.8%	\$207.45	\$153.14
Jul 21	81.5%	\$243.12	\$198.20
Aug 21	71.9%	\$224.87	\$161.61
Sep 21	67.9%	\$208.10	\$141.31
Oct 21	66.1%	\$169.49	\$111.96
Nov 21	65.1%	\$146.87	\$95.58
Dec 21	57.8%	\$129.16	\$74.70
Jan 22	55.9%	\$118.70	\$66.34
Feb 22	66.9%	\$139.95	\$93.66
Mar 22	70.6%	\$148.90	\$105.14
Apr 22	78.3%	\$186.05	\$145.70
May 22	70.7%	\$180.89	\$127.86
Average	68.9%	\$175.30	\$122.93

Source: Costar / STR



### **Limiting Conditions per Conditional Use Permit (“CUP”)**

The various operational constraints imposed by the CUP have had a dramatic impact on the feasibility of continued hospitality operations at the Property.

1. Maximum of two weddings per week and six per month
2. Maximum of 40 guests allowed Monday thru Thursday
3. Maximum of 75 guests will be allowed Friday thru Sunday
4. All events must occur prior to 6:00 pm
5. No event parking may take place in residential neighborhood. City allows remote parking if a shuttle is provided
6. A security guard is required on site during all events

With 80% of weddings occurring between May and October, the limit of 6 weddings per month impacts revenue substantially, eliminating 2-3 weekend event days during peak months (according to Brides.com). The most significant constraint is the limitation of 75 guests on weekends, as pre-pandemic wedding parties averaged 130 guests (theknot.com). The financial data shown above clearly demonstrates the dramatic decline in non-hotel room revenue, a trend that continues today.

### **Feasibility of New Development**

One potential option to improve operating revenues would be an expansion of hotel rooms or addition of restaurant/bar area. In 2014, the Owner Robert Blodgett applied to the City for an expansion of the facility into a 41-room hotel complex that would retain the historic Victorian Inn, demolish and replace the two cottages and garage area with a subterranean garage for 56 cars and two new hotel buildings with 32 guest rooms, meeting rooms and kitchen facilities. The Owner prepared a full Environmental Impact Report, but the Project application was withdrawn by the Owner due to massive community opposition.

With current resident sentiment opposed to hospitality uses, no changes to the commercial uses allowed on the Property can be expected to be approved by the City.

### **Finding**

Kosmont’s analysis of the Monarch Cove Inn Property shows the hospitality operations yield an inadequate return on investment of less than 4% to justify operations as a hospitality venue. Given the long term capital investment required, continued hotel use of the property is not financially feasible.

#### *Disclaimer:*

*The analyses, projections, assumptions presented herein are for illustrative purposes and are not a guarantee of actual and/or future results. Actual results may differ from those expressed in this analysis, as results are difficult to predict as a function of market conditions, natural disasters, pandemics, significant economic impacts, legislation and administrative actions.*