

# Appendix 2

## Market Study

### I. Conclusions/Executive Summary

#### Introduction

As part of Phase I of the Governors Island Planning and Pre-Development Services Program, Robert Charles Lesser & Co., LLC (RCLCo) has completed a market study of a wide variety of land uses that are now being considered for Governors Island. These include:

1. Conference, Retreat and Training Center Facilities
2. Hotel and Lodging
3. Spa and Wellness Facilities
4. Parks, Recreation and Sports Facilities
5. Marina
6. Educational and Non-Profit Facilities Theater and the Arts
7. Restaurants, Banquet Space, Retail and Office

In order to assess the depth and character of demand for these uses at Governors Island, RCLCo has undertaken a number of tasks and utilized a variety of information gathering techniques. Our analysis of each land use has included each of the following components:

- An analysis of market demand conditions, specifically research of the economic, demographic, tourism and development trends in the New York metropolitan region, New York City and Lower Manhattan;
- National market trends for each land use;
- Regional and local competitive supply analysis;

- Targeted interviews with key decision makers and interested parties for particular land uses (a list of those interviewed is near the end of this section);
- Statistical demand analyses (where appropriate); and,
- An assessment of the conceptual “fit” on the Island and the development constraints.

A summary of our findings is provided in the sections below. More detailed discussion of the market conditions for specific land uses are provided in the following sections. This report is subject to the Critical Assumptions and General Limiting Conditions below.

#### Market Strengths and Challenges

The character and location of the Island has created a powerful dynamic: the combination of a special, unique place with incredible access to one of the world’s largest and most attractive markets. The Island offers business leaders, visionaries and educators a place of retreat and reflection from the driving economic engine of Manhattan. The Island also gives New Yorkers another great public green space that is minutes from their homes or places of work. Finally, the Island will be a tremendous draw for visitors who want the best of all worlds – natural serenity, historic charm and access to the urban excitement of New York City.

Overall, Governors Island represents a truly unique redevelopment opportunity, and will be embraced by the development community with significant enthusiasm. The opportunity to develop on a site with this level of access that also offers such wonderful natural amenities is unparalleled. The

key to realizing this market potential, however, will be creating a plan that leverages the site’s existing competitive advantages, creates a vibrant combination of land uses and effectively addresses the challenges associated with the Island’s physical constraints. While the challenges are not overwhelming, they are substantial enough to limit demand for a variety of uses if left unaddressed.

The redevelopment efforts will be able to leverage Governors Island’s natural beauty, waterfront, views and historic character in order to attract significant market demand and development interest for a variety of land uses. New York City has struggled through a period of economic decline, beginning with a national economic recession and exacerbated by the shock of 9/11. Yet, the affect of this economic decline on demand for new projects on Governors Island should not be overstated, as Manhattan will continue to be a global economic powerhouse. Further, the extent to which jobs have dispersed throughout the region in search of geographical redundancy will not dramatically affect demand for uses at a regional destination like Governors Island, especially since corporate headquarters are often still located in Manhattan or closer-in office cores. The changing character of Lower Manhattan, with a greater vitality and diversity as it moves away from just a concentration of jobs to a place where people live, work, visit and play, is a related, positive trend.

However, significant challenges to the redevelopment effort do exist. Governors Island is an island, and that brings with it a number of physical challenges, especially related to the efficiency and quality of transportation to, from and on the Island. The relative harshness of

weather conditions is another concern. Further, the requirements that restrict certain uses, in particular permanent residential, and encourage the use of historic buildings are positive for many reasons, but also create challenges that need to be overcome.

### **Market Strengths**

**Access to One of the World's Most Attractive Markets.** New York City is the economic, cultural and social center for a region of 9.5 million jobs and 20.6 million people. It is a true global city. Governors Island's location at the southern tip of Manhattan provides tremendous access to this marketplace. The Island can be reached in an eight minute ferry ride from Lower Manhattan and Brooklyn, and regional ferry access could be provided from New Jersey and JFK Airport. The Battery Maritime Building (BMB), the ferry launch site from Lower Manhattan, located adjacent to the Staten Island Ferry, is easily accessible via subway and car.

**Lower Manhattan diversification.** Lower Manhattan is likely the most prominent gateway to the Island. While Lower Manhattan is still recovering from the economic shock of 9/11 and a national recession, it is also becoming a more diverse, lively place. This includes a wider variety of companies located in Lower Manhattan, which gives the daytime population a greater diversity and reduces future concerns about economic over-dependency on one industry; increased 24-hour vitality, primarily due to the 5,200 residential units added since 1995 (with an additional 1,800 planned by 2007); and increased tourist traffic, which will only increase once the 9/11 Memorial is completed and becomes a "must see" tourism destination.

**Waterfront revival.** The redevelopment of Governors Island should be viewed as part of a larger revitalization of the waterfront in Lower Manhattan and Brooklyn. In particular, the planned, 63-acre Brooklyn Bridge Park and, across the East River, the expansion of East River Park south to Battery Park will create an impressive concentration of active and passive park space. These additional waterfront recreational activities may be more competition for park space at Governors Island; however, more likely bringing the waterfront back to the people of New York will create renewed interest, and therefore all the projects will benefit.

**The mystery of Governors Island.** For nearly all New Yorkers, Governors Island is a mystery – a visible, high profile island off the tip of Manhattan that very few New Yorkers have ever visited or even know much about. This sense of mystery will drive significant interest in the Island, and drive traffic from both New Yorkers and visitors who want a unique day on the Island, as well as corporations who want to use the Island as a place for a strategy meeting or a marketing event.

**The beauty of "getting away."** The Island's strongest competitive advantage may be its natural beauty and college campus feel. It is a place that can be used for a serene retreat or quiet reflection, in sharp contrast to the hustle and bustle of Manhattan just to the north. It is also a place that will potentially offer the type of natural beauty that makes just being there an event. An important part of this serene environment and natural beauty are the views – back to Manhattan, to the Statue of Liberty and Ellis Island, among others – and the waterfront.

**Historic character.** The north part of the Island includes approximately 1.5 million square feet of historic buildings, as well as two sites – Fort Jay and Castle Williams – under the control of the National Park Service (NPS). The history of the Island is yet another reason why New Yorkers and tourists will want to visit the Island. Even more so, the historic buildings help create the character of the Island. Having authentic, architecturally unique buildings is a proven market commodity, especially in the banquet and hospitality sectors.

### **Market Challenges**

**Economic decline and the road to recovery.** New York City was shaken by the events of 9/11 and the national recession, and from 2000 to 2003 the City lost approximately 200,000 jobs. Approximately 25,000 of these job losses were in the finance, insurance and real estate (FIRE) sectors in Lower Manhattan. These job losses include the movement of some or all of the operations of major firms in order to create geographical redundancy. The overall impact of the recent economic should not be overstated. The Manhattan market will obviously continue to be a powerful one for uses driven by corporate uses, and a period of economic recovery will likely replace a number of the net losses in jobs. Also, many of the job losses have been in mid-level jobs with many of the headquarters functions remaining in Manhattan. Finally, Governors Island will be a regional destination for corporate uses, so the dispersal of jobs throughout the region is not necessarily a reduction in demand for uses at Governors Island.

**Making transportation convenient and special.** The location of Governors Island is geographically

accessible to a large market, but it still is an island with no direct transportation routes. A ferry is certainly an acceptable transportation mode, and rationally may even be preferred to automobiles on congested roadways. However, the challenge will be to provide the level of service that will be required by the wide variety of consumers that will use the Island on a daily basis. Many users will require convenience, and that means relatively short lead times, extended hours and redundancy. Many users will also require that the transportation to the Island match the experience on it – e.g., a unique, special experience. This includes the point of embarkment, such as the Battery Maritime Building, which currently offers a very poor experience for visitors.

Controlling for the weather. The weather on Governors Island can be relatively quite harsh, especially during the Autumn and Winter months. The wind conditions are of a particular concern, especially on the west side of the Island. The chance for tough weather conditions will certainly affect the depth of demand for certain uses at specific times of the year, although primarily indoor uses can continue to some extent. It is important the land plan attempts to block wind as much as possible, so that interior parts of the Island are more pleasant. Even more critically, uses on the Island that will operate during the harsh weather periods must have transportation options on the Island that can get people comfortably to and from the access/ departure and the various buildings on the Island.

The use of historic buildings. Historic buildings can be a very strong market advantage, as discussed above. However, they also present several challenges associated with rehabilitation

and adaptive reuse. For example, often, reusing historic structures can be more expensive than new construction, which then requires a competitive positioning that may not be possible or is more risky. It is also often the case that historic buildings do not often meet the size specification of many modern uses, which can result in the inefficient use of space and/or the need to construct new buildings in addition to the historic rehabilitation.

The lack of permanent residents. The redevelopment of Governors Island must be completed in accordance with the guidelines set when the land was transferred from the federal government to the City and the State of New York. This includes a prohibition of permanent residential uses in order to ensure the Island remains a public place. However, the lack of a supply of permanent residents does create some market challenges, in particular limiting the 24-hour, year-long population on the Island that would support other uses – in particular retail and restaurants.

### Land Use Opportunities

The strength of the opportunity for specific land uses on Governors Island is based upon three factors: market support, conceptual fit on the Island, and the expected market and development constraints. These factors are defined as:

- Market support – The projected demand and supply conditions for the land uses in the defined market area.
- Conceptual fit – The extent to which the land use “fits” on the Island, based upon both the objective -- requirements of the land transfer agreement -- and the subjective – the initial sense of what the Island can become based

upon review of past studies, discussions with key stakeholders and the consulting team’s preliminary work on conceptual designs for the Island.

- Development constraints – The extent to which market perceptions or physical characteristics constrain demand for land uses on Governors Island. This will include issues of transportation and susceptibility to poor weather conditions.

Exhibits I-1 to I-3 demonstrate in a matrix format how we believe each of the land uses relates to the above factors.

Hospitality uses represent a strong market opportunity on Governors Island, although the strength of that opportunity varies among the type of the use. We have found that a strong opportunity exists for the development of a high-end executive conference center hotel. A conference center hotel on Governors Island has the potential to capture market share at the top niche of demand due to its unique competitive advantages: a location off the southern tip of Lower Manhattan that also offers the ability to “get away” to a serene, campus-like environment. The quality of the built environment must match the quality of the place, including both the character of historic, architecturally significant buildings and modern units and amenities. There will also be opportunities to create synergies with other uses on the Island, such as passive and active recreational amenities, historic places such as Fort Jay and Castle William, and other educational and learning resources, as well as spa facilities for weekend traffic.

Certainly, the Manhattan employment base will drive demand for weekday conferencing, typically in peaks of Monday to Wednesday and Thursday to Friday and in groups of 45 to 75 persons. There may even be an opportunity to reach an agreement with one or more large users for dedicated blocks of space; dedicated space significantly lowers risk due to guaranteed occupancy, and therefore greatly enhances the marketability of the project to sources of equity and financing. Given the natural and built amenities that will potentially be on the Island, the conference center hotel can also compete for leisure demand on the weekends.

There are certainly challenges associated with conference center hotel operation on the Island that must be overcome or mitigated, such as transportation to the Island, traveling around the Island (in particular from the point of arrival and departure to the conference center facilities) during periods of inclement or harsh weather periods, and mixing public access with a semi-private retreat. However, these constraints are moderated by the fact that conference center attendees are more likely to spend more organized time on the Island and in the conference center facilities, and will travel in larger groups.

The optimal size for a conference center hotel will be 300 rooms with approximately 40,000 square feet of meeting space. Conference center hotels work most profitably when selling complete meeting packages (CMPs), which includes the cost of a room, meals, audio/video, presentation and meeting supplies, etc. The average CMP for a conference center at Governors Island should fall in the \$350 to \$400 range, with peak CMPs averaging in the \$400 to \$450 range.

There will be a strong opportunity to develop one or more hotels over the life of the redevelopment project. The Manhattan hotel market has rebounded after a few down years following 9/11. Occupancies have returned to near 85% in recent months, and while average daily rates (ADRs) are still in recovery after a significant decline since 2001 due to hotels buying occupancies with lower room rates, these should improve quickly in response to the tighter room supply. Assuming rather conservative growth rate in demand, there will be significant numbers of new hotel rooms demanded over the next three to five years; however, there is relatively little supply in the development pipeline. Thus, we expect there to be significant market opportunities for new hotel development in Manhattan looking forward.

Lower Manhattan is a relatively small hotel submarket, historically known only for business hotels serving the financial district. However, that is changing, as the environment in Lower Manhattan is gaining momentum, as more homes, restaurants, hotels and park activities draw locals and visitors below Houston Street. Hotels such as Ritz Carlton Battery Park and the Millennium Hilton are now attracting significant weekend leisure traffic. Lower Manhattan should be able to capture much greater than its fair share of excess demand; as of now, approximately 50% of Manhattan planned new supply is in the downtown area.

Boutique hotels are a growth segment within the hotel sector, and we believe that this concept is a better fit with the Island than other types of hotels. Boutique hotels are smaller, and can be better oriented towards the strengths of Governors Island – natural beauty, seclusion – and away from its challenges – transportation, lack of a critical mass of

development – because boutique hotel customers are more likely than other types of hotel guests to buy into a retreat concept. Certainly, transporting hotel guests is more of a challenge than with conference center guests, because hotel guests will more likely act as individuals, and therefore transportation will need to be available in shorter lead times and at longer hours. Transportation from the point of arrival to the hotel will be critically important during harsh winter months.

We envision the concept for a boutique hotel on Governors Island is the “urban getaway” – a small, luxury hotel that provides the appropriate level of services and can offer easy access back to Manhattan, but more critically can also offer the natural and built beauty of Governors Island. We are also assuming that complimentary uses, in particular a spa, will be available to guests of the boutique hotel. A typical boutique hotel will have 100 rooms, and the projected ADR will be \$350 to \$450. We have concluded that one boutique hotel is supportable in the near term, with a second supportable in the two to five years following.

There is less of an opportunity for a luxury hotel at Governors Island. The market support for a luxury hotel in the Manhattan market is strong given growth in total demand. The proven success of the Ritz Carlton Battery Park shows that, given the right environment, Lower Manhattan can attract this market segment. However, Governors Island may be a more difficult fit than would be a boutique hotel. We believe the luxury hotel consumer may be less likely than boutique hotel guests to leave the critical mass of activity in Manhattan. Luxury hotel guests will also be less likely to accept inconveniences associated with the transportation to and from

Manhattan (or points elsewhere). In the mid- to long-term, once Governors Island is established as a destination and a critical mass of complimentary uses have been developed on the Island, a moderate opportunity may exist to develop a 250 to 300-room luxury hotel.

There is a limited opportunity to develop a Full Service Hotel or Limited Service Hotel at Governors Island. The market support in Manhattan for these types of hotel are also strong, especially limited service hotels as they have filled a gap as a lower-cost alternative. However, they do not fit well into the concept of the Island, and the market constraints for these types of hotels are a particular concern. Typically, these two hotel concepts cater to more price-sensitive, convenience-oriented guests, such as business travelers. These types of guests would be particularly sensitive to the relative lack of activity and services on the Island, as well as any inconveniences or constraints on transportation. These types of hotels would allow for a greater range of price points on the Island, but providing heavily discounted rooms will likely cause market confusion and dilute the experience of the much more expensive boutique hotels.

A high-end spa will represent a strong opportunity on Governors Island, primarily as an amenity to the conference center and boutique hotel(s). The concept of the spa fits perfectly into the overall theme of the Island as an urban getaway. There are, however, a number of different types of spas, of which we studied market feasibility for the following: destination and wellness, resort, and day.

A destination and wellness spa sells strictly programmed, extended stay packages focused

around issues of health and wellness. These types of spas tend to have recognizable brands, such as Canyon Ranch and Golden Door, and these brands are often not easily transferable to new locations. The market opportunity for this type of spa is limited, as market demand represents a relatively small niche of consumers that is apparently declining (or not growing as fast as other spa market segments). Constraints are limited, primarily because guest are more likely to travel only once to the Island over a several day period and will likely spend much of their time in organized events within the facility; however, for this same reason, the concept does not really fit on the Island, as it will do little to help populate the Island and will more likely create a secluded, private facility.

Resort and day spas tend to focus more on pampering than on strict programming. Resort spas provide overnight stays, and therefore cater more to weekend getaways where guests are utilizing the spa as well enjoying other activities in and outside the resort. Day spas typically offer treatments over the course of one or two hours. Both of these concepts have good market support in the local and regional market. Overall, the resort spa concept fits better on the Island and has somewhat less constraints than the day spa. Customers on a weekend getaway will likely be able to plan around inconveniences associated with transportation, although transportation within the Island will be critical in harsher weather periods. Day spa customer will have less flexibility, as appointments need to be met and the customer is only willing to commit a few hours to the trip (meaning a missed ferry and a long wait could create significant annoyance).

We believe the resort spa concept is the most supportable concept on the Island, with a modification that weekend rooms at the conference center hotel and boutique hotel rooms are substituted for rooms directly tied to the facility. The resort will be not one facility or campus, but the entire Island. The conference hotel and boutique hotel(s) can sell packages to the spa, or vice versa; the details of that relationship will need to be negotiated, but should not be a strong impediment. We recommend that the spa on Governors Island will have between 8 and 12 treatment rooms, with the average price of \$130 to \$150 per hour. We project that approximately 80% of the demand for spa treatments will be derived from hotel guests on the Island, with a higher percentage of day spa traffic in the weekday.

There is very strong opportunity to provide park space, recreational facilities and water-based activities on the Island. Park space and recreational facilities are necessary urban elements that are rarely oversupplied, and our analyses have found that significant pent-up demand and trip potential does exist from within in the local market area. The park space should include large tracts of passive open space (for picnics, sunbathing and events), extraordinary landscaping, and walking and biking trails. This public-oriented land use fits very well conceptually on Governors Island, and can act as the centerpiece and defining characteristic of the Island. Transportation concerns will be rather limited for park space; although there will be peak days on the summer weekends, the travel will typically be spread throughout the day. Weather is a concern, only in that it will make the park space unusable for much of a three to five month period.

We have also found significant market depth for a variety of recreational facilities, including baseball, softball and soccer fields; tennis courts; basketball courts; golf driving range; swimming pools; and an ice hockey rink. There is significant pent-up demand for league and instructional facilities throughout New York City. The market success of the 1.7 million square foot Chelsea Piers recreational complex is particularly relevant given its nearby location. This complex attracts over 4 million visitors a year, and many of the facilities, while technically open to the public for a significant fee, are often booked well in advance by leagues and instructional activities. Chelsea Piers attracts approximately 20% of its traffic from outside of Manhattan, despite the fact that it is not very accessible. There is a proposal to expand operations onto Pier 57, in particular cultural space for galleries and dance recitals, a 30,000 square-foot swim center, and a 100,000 square-foot tennis center, all of which are significant voids in the current marketplace. The Pier 57 proposal would certainly work as well on Governors Island, although we believe Governors Island could also support a larger facility due to extensive pent-up demand in the marketplace.

The Island needs to effectively address the waterfront. Where appropriate, given conditions of the current, water activities such as kayaking and sailing launches could prove to be very successful. We also have found there to be a very strong opportunity to develop a marina on the Island. The number of slips and moorings in the greater New York City are well below the potential number of boat owners, based upon our demand analysis. The market is certainly undersupplied today, as the marinas we surveyed are almost all 100%

occupied. The concept of a marina certainly fits on the Island, although a safe harbor will likely need to be constructed.

A marina at Governors Island should be approximately 200 to 250 slips, with about 20% of the slips used for transient traffic and the remainder used as seasonal rentals. We do not expect that the marina will be used during harsher weather months, and thus seasonal rental slips make most sense. Creating a year-round marina would require upland facilities, which are often very unattractive and most likely would not fit into the land plan for the Island. Transient slips fill a particular market void, and are attractive in that provide another access point for visitors to Governors Island. Seasonal slips should be rented at \$120 per foot of boat.

There are mixed opportunities to develop office, retail and restaurant space on the Island. Stand-alone office space that requires users to commute to and from the Island every day is not a feasible use, as the overall market demand is still recovering and the inconvenience for workers represents too significant of a constraint. There may be some limited office demand from uses already on the island that need some office presence, such as GIPEC, but in the grand scheme this amount of space should not be significant. Stand-alone retail space that must attract convenience and comparison goods retail traffic to the Island also has very limited support, for obvious reasons of access and visibility.

We have projected that there is an opportunity to develop some significant supportive retail and restaurant space – uses that support visitors that have come to the Island for other reasons -- on the

Island. The market depth depends on our analysis of the population generated by other uses, and the constraints are low because the target population is already on the Island. Over the life of the project, we project that approximately 20,000 square feet of restaurant space and 16,000 square feet of retail space can be supported on the Island. The restaurant space will offer a wide variety of food options and price points, from parkside food stands to fast casual restaurants and mid-class sit down restaurants. The retail space will be a mixture of convenience and specialty shops.

We also believe that a moderate to strong opportunity does exist to develop one or more destination restaurants on the Island. Each restaurant will be approximately 8,000 square feet (200 seats), with an average price per check (per person) of \$100 and sales of well over \$1,000 per square foot. A destination restaurant is unlike other restaurants in that customers view the restaurant experience as a trip unto itself.

The transportation to the Island is still a constraint, as convenient service must be offered for customers to be able to make their reservations, and given the recommended price point at this type restaurant, the customer will be extremely discerning and sensitive to the quality of the overall experience. Providing transportation to and within the Island will be particularly important during the harsher weather months, although we have already accounted for the fact that demand will be lower during this period. Transportation could actually be transformed from a constraint to an amenity if the ferry ride is made an exciting part of the Governors Island experience, such as extended trips around the Island for better views and a high-end lounge

area on the ferry for those customers waiting to leave the dock. This experience will also require that the point of embarkment, most likely the BMB, and disembarkment reflect the level of quality at the restaurant.

The conceptual fit for this type of restaurant is strong, given the location, unique character and potential views the Island can provide. The market depth is also strong, given the Island's proximity to the vast New York City market; however, overall market support is only moderate due to the fact that these types of restaurants are driven less by overall market depth, but more by the quality of the brand or concept of the particular restaurant. Thus, attracting the "right" restaurant(s) that can establish itself as a destination is not a very easy task. Preliminary discussions with several prominent restaurateurs and investors suggest, however, that the unique opportunity at Governors Island will generate significant initial interest from the marketplace.

Banquet and event space represents a very strong market opportunity; in fact, several prominent catering companies have already expressed strong interest in hold events on the Island. Unique spaces in exciting locations drive the demand for high-end banqueting facilities, and there is likely no more unique and exciting place in New York City than Governors Island, with the great open spaces, historic and charming buildings, and incredible views. Our research indicates that pent-up demand is especially strong for unique banquet facilities that can seat 1,000 persons or more. Further, banquet space is not only a good fit on the Island, but is supportive of other uses, specifically the hotels. Much like with other uses, transportation

will be a constraint, but only a moderate one given that banquet visitors are more likely to enter and exit the Island at set times. Outdoor events will be constrained by the weather, but likely not much more than for any other location in the region.

Depending on which of the existing buildings are selected as most appropriate, we believe the market could support both 500-seat and 1,000-seat facilities on the Island. Across New York, locations whose primary business is not the rental of its space, such as the New York Public Library, Grand Central Terminal, Ellis Island, The Metropolitan Museum, and the Museum of Natural History, charge large fees for the use of their space. For example, the Metropolitan Museum charges \$30,000 just to gain access to the space, then requires payment for its own security, housekeeping, and other personnel. Ellis Island charges \$12,000 to \$18,000 for use of its vast hall and reception landing, and guests to Ellis Island must also pay Circle Line boats for private service to and from the island at a cost of \$7,500 per boat. Governors Island should be able to achieve pricing at or near the top of the market.

Educational facilities are not necessarily market-driven uses, in that typically these decisions are made based upon available funding and long-term growth plans. For many years there has been significant interest in a Governors Island location among various educational institutions, including New York Harbor School, CUNY summer school and auxiliary campus use, and a proposal for a nanotechnology research center. Educational uses on Island directly fit with one of the key mandates for the Island. While transportation to the Island will present some constraints, coordinating the ferry schedule and the start/ stop times of the educational

uses can help mitigate these constraints.

We have identified several educational uses, other than those already proposed, that would fit well on the Island:

- A Governors Island Institute, a colloquium of thinkers and leaders who will live part-time on the Island and work, teach and interact;
- A specialty education component, such as the Culinary Institute of America, which teaches professional and continuing education courses to a wide urban market; and,
- An environmental education center, which would provide an ecological learning environment for visitors to the Island.

We have also discovered, in a preliminary sense, a moderate opportunity to provide student housing on the Island. There is a housing crunch around universities and colleges in New York City. According to our estimates, there are approximately 175,000 full-time students in Manhattan and Brooklyn colleges and universities, but only 31,500 on-campus housing units. That is a gap of approximately 143,500 students that will demand housing in some form (including living at home with parents or family).

Student housing is a good fit for the Island, in particular because it allows the Island to attract a resident population without providing permanent housing. Yet, there are also significant constraints, in particular the need to provide transportation for a significant number of residents. This will require long operating hours, short lead time and dependable redundancy. The harsh weather on the Island at certain months will also be a market constraint. Indeed, given these conditions, we

do not expect the Island location to appeal to the broader student market. However, we do believe that it will be very attractive to a niche of the student population, as well as younger professors and researchers, especially if there are synergies with on-Island educational activities such as the Governors Island Institute or a top-notch research center. Even a 0.5% capture of the off-campus student market would equal 720 students. We have assumed for the purposes of further analysis that 500 student beds could be developed in the first or second phase of development, with future supply depending on the extent of proven demand.

As a center for the arts and culture, demand is likely strong for additional performance arts and theater uses in the broader market area. These types of uses are constantly struggling to find a home in New York City, and they certainly would fit within concept of the Island. Further, the Island’s natural beauty and historic structures offer a unique location for the performance arts. Constraints are high for larger theaters that have set schedules of daily shows, in particular because of the concerns over transportation and access.

The constraints are lower for festivals and special events on the Island, as demand would more likely be spread over a period of time. Very large events will be more difficult to accommodate, as they will require special transportation and logistics planning, although for a single event it certainly is possible. Constraints aside, there will be strong demand for a variety of different type of events on Island -- such as public displays of art, corporate product rollouts, or weekend long music festivals -- due to its natural beauty, large open spaces and access to a large market area.

### Summary of Market Findings

Governors Island represents a truly unique development opportunity – a 150-acre redevelopment site just off the tip of one of the most attractive markets in the world that offers the best of all worlds: access and seclusion, economic vitality and quiet retreat, urbanity and natural beauty, and modern amenities and living history. The strongest market positioning of Governors Island is as an “urban getaway”, with a focus on public access, hospitality, education, arts and the creation of ideas.

Based upon our market analysis, we have found that the following land uses are supportable on Governors Island, organized by strength of the opportunity:

Strong	Moderate	Limited - Long Term
Conference Center Hotel	Boutique Hotel 2	Luxury Hotel
Boutique Hotel 1	Destination Restaurant(s)	
Spa	Student Housing	
Public Park	Theater	
Marina		
Recreational Facilities		
Banquet Facilities		
Supportive Retail/ Restaurant		
Educational Facilities		

The Island will also be an excellent location for special events of a variety of types and sizes.

The key land use drivers are the public park, the conference center and hotels, and the destination restaurant(s). However, there are tremendous synergies among all the uses. For example, the spa is a critical amenity for the hospitality uses, and the hotel rooms on the Island will provide the majority of demand for the spa. The banquet facilities and hotels will also have an important, symbiotic relationship. The educational facilities are important as their own uses, but also create an environment of learning, thought and ideas that create potential synergies with the conference center hotel.

Part of our analysis involves a preliminary estimate of the annual population to the Island. For the purposes of this analysis, we have assumed the following uses on the Island:

- 300-Room Conference Center Hotel
- Two 100-Room Boutique Hotels
- Two 200-Seat Destination Restaurants
- 500-Seat and 1,000-Seat Banquet Facilities
- Spa with 12 Treatment Rooms
- 500-Student Full-Time Educational Facility (e.g., Harbor School)
- 450-Student Specialty Educational Facility (e.g., Culinary Institute)
- 50-Fellow Governors Island Institute
- 500-Bed Student Housing Complex
- 80-Acre Park
- 225-Slip Marina

Assuming just these land uses, we project that the Island could have an annual population of 4.37 million, at an average of 12,000 people per day if all land uses were programmed at their maximum

and the park demand was met (See Exhibit I-4). Not surprisingly, the population will be much greater on the weekend (average of 17,500 per day) than on the weekday (7,800). Also, not surprisingly, the peak season is the Summer (35,200 average daily visitors on the weekend/16,400 on the weekday), with the Spring (18,800/7,800), Autumn (11,300/4,900), and Winter (4,800/2,100) are less busy. Weather will clearly be a significant factor on the Island.

The key constraint for most of the uses we studied was transportation to the Island, and within, the island. The daily population estimates will clearly place much greater pressure in the Summer months, with more sporadic demand in the harsher weather months. A transportation plan must be devised that can gear up for the heavy demand periods, but also scale down to the low demand periods without completely diluting the quality of the service. Further, a number of uses will require that the transportation options run extended hours and offer frequent trips.

**List of Interviewees**

**Conference Centers**

<b>Name</b>	<b>Company/Category</b>
Jeff Burns	Dolce International
Felix Cacciato	Dolce International
Steve Sackman	ARAMARK Harrison
Jack Kealey	ARAMARK Harrison
Jeff Farina	Benchmark Hospitality
C.A. Anderson	Intercontinental Hotels & Resorts
Thomas Lorenzo	Hilton International
David Keys	Hilton International
Eva Wasserman	Hilton International

Denise Adam	Helms Briscoe Meeting Planners
Claude Vargo	PKF Consulting IACC Contractor
Brandon Dolci	NY Society of Assoc. Executives
Lesly Rehaut	NY Meeting Planners Int'l Meeting Planners
Leo Renahan	Cornell University School of Hotel Admin.

**Marinas**

<b>Name</b>	<b>Company/Category</b>
Stan Johnson	Marinas International Marina Investor/Developer
Bill Anderson	Westrec International Marina Investor/Developer
Mari Lou Livingood	Nat'l Marine Manuf, Ass'n Marine Industry Association
David White	New York Sea Grant Research Organization
Michael Vanderford	US Fish and Wildlife Admin Boating Infrastruc. Grants
Queene Foster	NY Yacht Club
Scott Seisler	Surfside3 Marina Developer/Operator
Gus Savaros	NY Found. for Safe Boating Boating Association
N/A	Comm. Boating – Boston Boating Association
N/A	Comm. Bting. – Providence Boating Association
Tim Keogh	Marina Management, Inc. Marina Operator/Investor

**Hotels**

<b>Name</b>	<b>Company/Title</b>
Kate Hearth	Ritz Carlton Battery Park Director Sales / Marketing
Jimmy Santostefano	Millenium Hilton Director Sales / Marketing
Mike Milligan	Embassy Suites Director Sales / Marketing
Teresa Chen	SoHo Grand/Tribeca Grand Director Sales / Marketing
N/A	Wall Street Inn Sales and Marketing
N/A	Kitano Hotel Sales and Marketing
Susan Lee Bishop	Four Seasons Catering Sales Manager
N/A	Hudson Hotel Sales and Marketing
N/A	Mandarin Oriental Sales and Marketing
N/A	Sherry Netherland Sales and Marketing
N/A	Sheraton Hotel Sales and Marketing

**Spas**

<b>Name</b>	<b>Company/Title</b>
Suzanne Ng	Mandarin Oriental Spa Director
Laura Anne Pelliccio	Plaza Spa Assistant Director
Thomas Olsen	Doral Forrestal Spa Director of Operations
Gary Milner	Canyon Ranch Director of Development
Dean Gitter	Emerson Inn President, founder
Rachel Caldwell	Golden Door Spa Director

Verna Wormley	4 Seasons Spa (Philad.) Spa Director	<b>Education Name</b> Sue Cussen	<b>Company/Title</b> Culinary Institute of America Continuing Education Director of Marketing
Rae Pinchuk	Greenhouse Day Spa Spa Director		
N/A	Mirbeau Inn Marketing		
Kim Matheson	NRI Spa Consultants Director	Nathalie Fischer	Culinary Institute of America Director, New Media
Lynn Curry	NRI Spa Consultants Director		
Margie Ruddick	Landscape Architecture Spa Developer/Planner	<b>Restaurants Name</b> Mary Dearborn	<b>Company/Title</b> Restaurant Associates Director Catering
Mary Tabacchi Hospitality	Cornell School of Professor, Spas	Tim Bartley	Charlie Palmer Group COO
Bjorn Hanson	Price Waterhouse Coopers Director, Spa Group	Joanne de Santos	Tavern on the Green Director of Sales
<b>Recreation and Parks Name</b>	<b>Company/Title</b>	David Swinghamer	Danny Meyers Group CFO
Dana Thayer	Chelsea Piers Director of Marketing	Michael Whiteman	Whiteman Baum Consulting Consultant to Restaurants
Dan Biederman	Bryant Park Director	Scott Stamford	River Café Director
Ron Lieberman	NYC Parks Budget Off, – Concessions	Drew Nierporent	Myriad Group President
Ed Feldman	NYC Parks Budget Office – Permits		
Joshua Laird	NYC Parks Director of Planning	<b>Banquets Name</b> Mike Warren	<b>Company/Title</b> Chelsea Piers, Pier 60 Director
N/A (Multiple)	NYC Parks Permit Offices	Sean Driscoll	Glorious Food Director
N/A	Central Park Conservancy Marketing	Carl Dean Hedin	Abigail Kirsch Manager
		Liz Neumark	Great Performances Director, President
		Jennifer Kozlowski	Aramark/ Ellis Island Manager

### Critical Assumptions

The conclusions and recommendations presented in this report were reached based on our analysis of the information available to us from our own sources and from the client as of the date of this report. We assume that the information is correct, complete and reliable.

Our conclusions and recommendations are based on certain assumptions about the future performance of the global, national, and/or local economy, as well as that of the real estate market and on other factors similarly outside either our control or that of the client. To the best of our ability we analyzed trends and information available to us in drawing these conclusions and making the appropriate recommendations. However, due to the very fluid and dynamic nature of the economy and the real estate markets, it is critical to continually monitor the economy and the market, and to revisit the aforementioned conclusions and recommendations periodically to ensure that they stand the test of time.

We assume that in the future the economy and the real estate markets will grow at a stable and moderate rate. Often this assumption is made due to budget limitations that prevent us from delving deeper and/or more frequently into the economic forecast or the forecast of the real estate markets. History tells us that this stable and moderate rate growth pattern is not likely to occur over extended periods of time. The economy is quite cyclical, and the real estate markets are typically very sensitive to these cycles. Our analysis does not take into account the potential negative impact that major economic “shocks” could have on the national and/

or the local economy, and the residual impact on the real estate market and the competitive environment. We are currently in the midst of an economic recovery, the timing, depth and duration of which is unknown.

Additionally, we assume that economic, employment and household growth will occur more or less in accordance with current expectations, as will other forecasts of trends and demographic and economic patterns. Along these lines, we are not taking into account any major shifts in the level of consumer confidence; in the cost of development and construction; in tax laws (i.e., stable property and income tax rates, deductibility of mortgage interest, etc.); or, in the availability and/or cost of capital and mortgage financing for real estate developers, owners, and buyers. Should any of the above change, there is good reason to believe that this analysis should be updated, and the conclusions and recommendations summarized herein be accordingly reviewed (and possibly revised).

We also assume that competitive projects will be developed as planned (active and future), and that real estate demand will be met with a reasonable stream of supply offerings. Finally, we assume that major public works projects occur and are completed as planned.

### **General Limiting Conditions**

Every reasonable effort has been made to insure that the data contained in this study reflect the most accurate and timely information possible and it is believed to be reliable. This study is based on estimates, assumptions and other information developed by RCLCo from its independent research

effort, general knowledge of the industry and consultations with the Client and its representatives. No responsibility is assumed for inaccuracies in reporting by the Client, its agent and representatives or any other data source used in preparing or presenting this study. This report is based on information that was current as of June 2004, and RCLCo has not undertaken any update of its research effort since such date.

Our report may contain prospective financial information, estimates or opinions that represent our view of reasonable expectations at a particular point in time, but such information, estimates or opinions are not offered as predictions or as assurances that a particular level of income or profit will be achieved, that events will occur or that a particular price will be offered or accepted. Actual results achieved during the period covered by our prospective financial analysis may vary from those described in our report and the variations may be material. Therefore, no warranty or representation is made by RCLCo that any of the projected values or results contained in this study will actually be achieved.

Possession of this study does not carry with it the right of publication thereof or to use the name of "Robert Charles Lesser & Co." or "RCLCo" in any manner without first obtaining the prior written consent of RCLCo. No abstracting, excerpting or summarization of this study may be made without first obtaining the prior written consent of RCLCo. This report is not to be used in conjunction with any public or private offering of securities or other similar purpose where it may be relied upon to any degree by any person other than the Client without first obtaining the prior written consent of RCLCo. This study may not be used for any purpose other than

that for which it is prepared or for which prior written consent has first been obtained from RCLCo.

## II. Socioeconomic Trends & Tourism

### Summary

Governors Island will not create change, but will be an integral part in solidifying current shifts in Lower Manhattan and Brooklyn. The economic shock of September 11th, exacerbated by a national economic recession that hit the financial sector especially hard, has led to significant job loss in New York City, and Lower Manhattan in particular. Partially in result, the New York City economy is currently undergoing an economic restructuring, and the growing diversity of firms in Lower Manhattan may make future localized recessions less likely, as well as change the character of the local employment base. Most firms that had a presence in Lower Manhattan before 9/11 continue to have a presence there today. Even when significant operations have moved elsewhere, these firms have typically stayed in the region, and often headquarters operations have stayed in Manhattan. Governors Island will have incredible access to this vast corporate marketplace.

Lower Manhattan is diversifying beyond the economic restructuring. New residential units are creating a more residential feel, which is driving more supportive retail and services. In great part because of the draw of Ground Zero, tourist traffic has also increased significantly. Lower Manhattan is transforming from a more staid, corporate place to a true 24-hour neighborhood. Waterfront revitalization in Manhattan and Brooklyn is giving this burgeoning population another outlet for engaging and enjoying the neighborhood.

Governors Island will certainly feed off the adjacent vibrant neighborhoods in Manhattan and Brooklyn; even more so, it will add another critical dimension to these neighborhoods that will enhance change and growth.

### Economic Growth Trends

The New York metropolitan region is a global economic center and in particular is a world leader in finance and professional services. New York City is the unquestioned economic center of this region with an estimated 3.5 million jobs in 2004, or 37% of the region's 9.5 million jobs (Exhibit II-1). The City has also shown to be more vulnerable to national and localized economic shocks, and the most recent economic downturn has been no different.

Between 2000 and 2003 New York City had a net loss of 195,000 jobs; during the same period, the region lost approximately 243,000 jobs, meaning that the City accounted for 80% of the region's job losses. Thus, the regional economy as a whole has fared better than New York City, with suburban areas in the region showing only moderate job losses, and in some cases even job growth, over the same period. As an example, between February 2001 and February 2003, New York City lost an estimated 110,000 jobs while the New York counties of Suffolk, Nassau, Westchester, Rockland, Dutchess and Putnam actually gained 47,000 jobs. Over most of this period, the northern New Jersey suburbs continued to lose jobs, but a slower rate than the region. The same trend has been observed in the Connecticut suburbs of New York City (Exhibits II-1 through II-4).

Some economists have suggested the New York City economy was operating "above capacity" during the 1990s, and the recent period of economic decline was due in part to a return to "normalcy." It has also been widely argued that New York City's economic concentration in financial services made it especially recession-sensitive, and that the more diversified local economies in the remainder of the region helped these areas weather the national recession in a much better fashion. Concentrations in pharmaceuticals, telecommunications, biotechnology and healthcare are all prevalent in the surrounding employment cores, creating what may be a more balanced overall economy. No doubt, these areas would not be what they are without their historical relationship to New York City's humming economic engine, but they are now better able to insulate themselves from the economic shocks that hit Manhattan's highly concentrated economy especially hard.

The nation's general economic contraction certainly affected New York City particularly hard, owing to the fact that Manhattan's economic engine is largely in the business of selling services – financial, in particular – to other companies, many of which were in decline by early 2001. However, the impact of the terrorist attacks of September 11th, 2001 had an additional negative impact upon the New York City economy that was "clear, unambiguous, and independent of the national recession. The economic downturn in the City was sharper than could have been anticipated from just the general economic recession."

Thus, the downtown area had to deal with a double hit – a national recession that would naturally affect

its key industry even harder, and the localized effects of the catastrophic events of 9/11. In 2003, the downtown area had roughly 281,000 jobs, 181,000 of which were in professional service jobs. Approximately 90,000 of these jobs were either in securities, commodities or banking. Since 2001 the job losses in Lower Manhattan, especially in the finance, insurance and real estate (FIRE) sector, have been relatively severe. Lower Manhattan lost approximately 25,000 FIRE jobs from 2000 to 2003, which accounts for 20% of the jobs in this critical sector (Exhibits II-5 and II-8).

These FIRE jobs are critical because they are some of the strongest export jobs of the regional economy. According to economists a typical FIRE job generates two additional Full Time Equivalent (FTE) jobs in the New York City economy; a FIRE job loss equates to two additional FTE job losses. FIRE jobs are also the highest paying, with average salaries more than double those of professional services. Combined with the physical and psychological destruction of 9/11, these job losses were – and continue to be – significant not only to the economic health of Lower Manhattan, but also Manhattan and New York City in general.

Certainly, not all is doom and gloom, and there has not been a widespread flight from the City. For example, many of Lower Manhattan's hardest-hit firms, the tenants of the World Trade Center, have decided to maintain a local presence and wait for recovery -- of the 185 businesses that were either damaged or destroyed 9/11, 91 remain downtown and 71 have moved to Midtown, while 12 have moved to New Jersey and only 10 have moved out of region altogether.

There has been movement within Manhattan that has generally shifted the amount of occupied space instead of creating widespread vacancies. In fact, Class A office vacancies in Manhattan have stabilized and started to recover in the past few months, currently standing at relatively respectable 10.6% in June 2004, after reaching a height of just 11.3% by the end of 2002 (Exhibit II-12). Certainly, the extent to which firms are occupying space inefficiently, and the impact of the loss in the World Trade Center inventory, have suppressed vacancy rates. Still, trends suggest vacancy rates will continue to fall, especially as a significant numbers of firms grow back into their sublease space, thus pushing those tenants back onto the market.

The slower job loss in the suburban areas relative to the City and Lower Manhattan is due in part to the transfer of jobs out of the City into suburban locations. A number of Manhattan firms are operating more efficiently by maintaining the necessary Manhattan presence with a smaller operation consisting primarily of top-tier executives and brokers while shifting back-office operations outside of Manhattan. Efficiency is not the only factor; geographic redundancy is also an important decision factor for firms as well as a national security issue. Following the terrorist attacks of 2001 and the power grid failures of 2003, the federal government strongly suggested that Manhattan's concentrated financial services sector accelerate the decentralization process in order to maintain operational redundancy in the case of a catastrophic event.

In the case of firms such as Lehman Brothers, the geographical diversification has meant a shift within New York City, rather than out of it. However, for

other firms, the geographical dispersion was much more significant. JP Morgan Chase and Goldman Sachs have secured facilities in New Jersey. Morgan Stanley bought the former Texaco World Headquarters building in Westchester and has planned to move 2,200 jobs there. New York Life is also planning to move 1,000 jobs to Westchester, and Bank of New York is planning on expanding its operations and move jobs into Syracuse, NY. Citigroup is keeping a significant concentration of its operations in Queens, but is also moving 1,600 technology jobs to a new campus in Warren, New Jersey.

Many companies have realized, however, that remaining competitive means retaining their headquarters – and their highest-paid executives – in Manhattan. Goldman Sachs continues to rent 600,000 SF of office space in New Jersey while building a new headquarters building in Manhattan, shifting at least some workers into the regional economy but keeping its top-tier employees in New York City. TIAA-CREF is in the process of divesting more than 500,000 SF of office space in Manhattan, but is maintaining its headquarters in New York City while moving “back office” operations elsewhere.

In short, the jobs that New York City is losing might not be coming back, but the jobs that it is keeping are indeed the crown jewels of the regional economy. This is a trend that was occurring before 9/11, but was certainly exacerbated by the terrorist attacks. According to 2000 estimates, New York City was projected to lose approximately 4,000 jobs annually in “back office” jobs by 2010, but more than make up for that loss in “upper-tier” legal, management and business and financial operations sectors. The city is projected to gain

jobs in healthcare, pharmaceuticals, education and other sectors that have helped the regional economy weather the recent economic downturn. For example, Pfizer, Inc., a major pharmaceutical firm, has recently located in Manhattan.

In the face of structural economic shifts, Lower Manhattan is rapidly diversifying its commercial tenant base and demographic character. Among the perspicacious entities to seize upon Lower Manhattan's relatively high vacancy rates are education, healthcare, nonprofit, legal and arts/design firms. New York University's Berkeley Center recently committed to 20,000 square feet, and the Claremont Children's school leased 100,000 square feet. Publishing companies Hachette Filipacchi Media, Inc. and Newsweek are also shopping for space downtown.

According to Jones Lang LaSalle, tenants can secure Class A space downtown for \$33.85 per square foot, a 20% discount to Midtown. Sublease space, which composes 35% of the Lower Manhattan market, is an additional 20% off that price. While discounts in price and high vacancies suggest that the downtown market is still very soft and most likely several years from a significant rebirth, it has allowed the downtown market to absorb nontraditional tenants, diversify its economic base and approach a less single-sector sensitive economic base.

With the national and regional economy beginning to show signs of life as of 2Q 2004, the projected near-term health of the New York City economy still is a mixed bag. As of June 2004, we have seen moderate job gains in New Jersey, Connecticut, and Long Island. Yet, in New York City employment has

yet to respond to an improving national economy by adding net new jobs. In a recent survey, while 32% of companies nationwide are planning to hire workers, that number is only 20% for New York City companies, with 10% planning additional job cuts. Still, overall the pace of economic decline has slowed, a sign that the hemorrhaging has stopped and the New York City economy will soon begin the process of growth and rebuilding.

The most important conclusion is that the New York regional economy is still the home to a large number of Fortune 1000 companies, many of which will continue to maintain some presence – and more often than not the headquarters operation – in New York City. Even if the operations of these firms move outside of the City, a critical mass will remain, ensuring not only economic relevance, but a continued place as the economic center of the region.

### **Demographic Context**

New York City is the most populated city in the United States, with an estimated 8.1 million people and 3.1 million households in 2004. From 2004 to 2009, approximately 5,500 new households will be added each year. Certainly this is an impressive level of projected growth, although it is a pace slightly less than the region as a whole. The region's households are projected to grow at an average annual rate of 0.5% from 2004 to 2009, while the City will grow at an annual rate of 0.2% (Exhibit II-13). The City's share of regional households will drop from 42.6% in 1990 to 39.8% in 2004.

Although the City is a place of tremendous wealth, its household population is more evenly distributed with regards to annual income than the region as a whole. Approximately 57% of New York City households have an income of less than \$50,000, while roughly 17% have an income of \$100,000 or more. Approximately 25% of the regions' households have an income of \$100,000 or more. The City's average income is \$64,000 and its median income is \$41,800, compared to \$80,800 and \$56,700, respectively, in the region as a whole. Still, given the size of the City of the depth of market is outstanding -- there are approximately 500,000 households in the City with an income of \$100,000 or more, and 140,000 households with an income of \$200,000 or more (Exhibits II-13 through II-17).

Since 1975, New York City's boroughs have been broken down into smaller legal jurisdictions called Community Districts (CDs). The CDs allow us to analyze 2000 demographic and land use data for smaller, more proximate market areas in New York City. Some of the more relevant data reveals the following (Exhibits II-18 through II-27):

- Manhattan CD 1, the area located south of Canal Street, had approximately 16,000 households, and this area has a significant concentration of wealth -- 39% of these households had an income of over \$100,000, with 24% of households with an income of \$150,000 or over. Roughly 60% of these households were non-family households, while only 17% of the households were families with children under 18 years of age.
- Manhattan CD 2 and CD 3, south of 13th Street, had approximately 120,000 households in 2000. CD2, the western half of this area, had a higher concentration of higher

income households – approximately 23% of households with an income of \$100,000 or over, versus 10% in CD3. Approximately 70% of the CD 3 households had an income under \$50,000. CD 2 also had a much higher percentage of non-family households (72%), while CD 3 also had a relatively high percentage of these households (53%) but also had a higher share of families with children, especially single parents.

- Approximately 90,000 households lived in Brooklyn CDs 2 and 6, directly across from Governors Island. These market areas provide a mix of lower, middle and upper-income households, as well as a mix of families and non-family households. An additional 39,000 households lived in Brooklyn CD 7, with a high concentration of households with an income of \$50,000 or under.
- A huge market area – nearly 400,000 households -- resided in Manhattan CDs 4, 5, 6, 7 and 8. There is a strong concentration of higher-income and non-family households. Manhattan CDs 9, 10, 11 and 12 held 200,000 more households, although this market area is more income constrained.

The 2000 data is a snapshot in time; however, demographic change is occurring throughout New York City, in particular in Lower Manhattan as new residential units are added to the inventory. While some office space is absorbing new types of tenants, other office space is being converted into residential uses. The 412g Residential Conversion program implemented in 1995 in concert with Liberty Bonds issued after September 11th have helped create over 5,200 residential units (both new and conversion) since 1995, with 2,360 of

those units built after September 11th, 2001 (Exhibit II-28). When the remaining Liberty Bond projects are selected, it is expected that Lower Manhattan will be home to over 7,000 additional units. Current occupancy rate of units stands at 95%.

New residents in Lower Manhattan tend to be wealthy, with an average household income of \$138,853, a median age of 35, and 59% of the population between 20 and 49. The late 1990s rebirth of the Lower East Side and Tribeca brought additional young professionals into Lower Manhattan, and a similar rebirth is taking place today in the Meatpacking District, now a location for trendy bars and fashionable hotels. In all, the portions of Manhattan most proximate to Governors Island are gaining high-income households, and have become entertainment and recreational destinations. More traditional retail growth is slowly following, with consumer-driven retail such as Borders Books and Chipotle securing space downtown. Overall, Lower Manhattan appears to be diversifying its economic base while bringing new residential and retail online in areas previously dominated by office, suggesting the growth of another 24/7 neighborhood in New York City.

Meanwhile, a similar vibrancy surrounds the Brooklyn CDs proximate to the Buttermilk Channel, the 400-yard strip of water that separates Governors Island from Brooklyn. Carroll Gardens, Brooklyn Heights, Cobble Hill and Atlantic Avenue all experienced dramatic upstream transformations in the late 1990s, gaining new populations of young professionals and the accompanying trendy bars and restaurants. In fact, Brooklyn CD2 has more households earning over \$125,000 than Manhattan CD3. Finally, the proposed Brooklyn Bridge Park

promises to revitalize the waterfront north of Governors Island, creating a regional recreational destination that will create a wonderful amenity for residents and place at least this portion of Brooklyn near the top of the list of “must-see” destinations in New York City.

## **Tourism Trends**

Tourism is a vital component of New York City's economy. Visitor spending directly contributes to entertainment, hotel and leisure industries, and to city, state and federal tax revenues. Jobs are created from every tourist dollar spent and significant secondary or induced spending results from tourism activities. New York City counted 138,000 employees that serviced the tourism industry in 2002. The wages and salaries generated by these industry jobs was \$4.1 billion, spurring further expenditures by these employees and therefore creating a secondary economic impact fueled by tourism. Otherwise stated, every tourism dollar spent in New York City generated an additional \$0.47 in secondary spending in 2002.

In 2002, the most recent year for which tourism data has been analyzed and made available, the total economic impact of tourism was estimated to be \$21 billion. Approximately \$14 billion of this was direct expenditure, 61% of which went to food and lodging, and the remaining \$6.6 billion was secondary spending from the employees supported by the tourism industry. Yet, total economic impact still is awaiting a full recovery -- in 2000, New York's peak tourism year, the total economic impact of tourism was \$25 billion. Though the total numbers of tourist have increased by 2003, these are from gains in domestic travelers who, on the whole,

spend less time and less money than international travelers (Exhibits II-30 and II-31).

The strong global and national economy that closed out the 1990's led to New York's peak tourism years in 1999 and 2000. More than 36 million visitors came to New York in each of these years, and Manhattan's hotel average daily hotel room rates were at an all-time high of \$223. However, the national economic recession and September 11th forced major declines in the tourism sector. The city lost 1 million visitors in 2001 from its 2000 volume, and only recovered a small portion of those in 2002. Last year witnessed a jump in visitor numbers by 2 million people to a high 37.2 million visitors (Exhibits II-29A and II-29B).

International visitors, however, have not returned, and these visitors from abroad are fewer in proportionate and absolute terms. This segment represented 19% of visitors to New York in 1999, and now represents only 14% on a larger base. Major contributing factors to this decline are the political unrest caused by US actions and policies abroad, restrictions on foreigners entering the US following 9/11 and a general worldwide recession. Growth, therefore, has been especially high in the domestic sector, which has surpassed its own 1999 levels by 3.1 million visitors in 2003 (Exhibits II-29A and II-29B).

Tourist behavior following September 11th leads analysts to believe that the drop in visitor volume in the subsequent 12 months was dictated by a respect for mourners more than a long lasting fear of travel or of security levels in New York. For almost exactly one year following the attacks, tourism dropped off, particularly in Lower

Manhattan. The Statue of Liberty was closed for security concerns, causing a decline in visitor numbers from almost 5 million to half that number. Occupancy levels in Lower Manhattan hotels dropped by 5% and would have fallen further were it not for the rebuilding happening in Ground Zero and relocation of residents. During the year following the attacks, the scales flipped in the balance of tourists that claimed to visit for vacation/leisure and those who came to visit friends and family.

After one year, tourists began to return, and the boost in 4th quarter numbers and holiday travel caused the modest recovery in 2002 annual numbers. The subsequent strength of the domestic tourist market in 2003, a 7.6% growth from 2002 numbers, signals a return of confidence and, many assert, a high level of interest from US nationals to pay their respects at Ground Zero. Curiosity in the rebuilding efforts is expected to continue to draw tourists and local visitors to the market. One indication of this trend has been the almost full occupancy achieved by the Millennium Hilton hotel on Saturday nights over the past year. The hotel offers views directly onto the Ground Zero site across the street.

Changes in tourism volume correspond with a similar recovery of the hotel industry in 2003 and the first quarter of 2004, although occupancy rates have recovered before average daily rate (ADR) and revenues, as hotels have continued to buy high occupancies with lower room rates. Following 9/11, a double hit to hotel occupancy and ADR in Manhattan hotels caused revenue per available room (REVPAR) to drop by 21.7%. Manhattan's hotels showed positive occupancy growth of 0.9% in 2003 for the first time since the attacks. First

quarter results for 2004 demonstrate positive growth in ADR as well for the first time since the attacks, signaling a quick response to the market's increased occupancy rates.

Further characteristics of travelers to New York City include (Exhibits II-30 through II-32):

- The bulk of visitors (76%) to New York are leisure visitors. The domestic leisure traveler typically comes to New York for a special event (30%), to visit friends or relatives (28%), for a getaway weekend (15%), a vacation (14%) or personal/other reasons (13%).
- The vast majority of leisure visitors spend one to three nights during a visit, although 22% spend four nights to a week and 3% spend more than a week. Average expenditures per day for the leisure traveler are \$150. The typical leisure traveler spends money fairly evenly across food, entertainment, shopping and transportation, and a smaller amount (15%) on lodging. Only 44% of domestic leisure travelers stay overnight.
- Most domestic leisure tourists attend a cultural event on their visits to New York. 32% go to the theater or a concert, 18% visit museums and another 18% visit historic sites, which likely includes Ground Zero.
- Business travelers, representing a purported 24% of visitors, are more likely to stay overnight than are leisure travelers -- approximately 3.3 million, or 55% of business travelers, stayed overnight in 2002. Business travelers spend \$228 per day typically, and apply the majority towards hotel expenses, with the next most important categories being transportation, then food. Of all traveler types,

domestic business travelers who stay in a hotel spend the most amount of money on a daily basis, \$275.

- Finally, international travelers spend more money per trip, \$1,080, than any domestic visitors, business or leisure. International visitors spent \$5.5 billion in 2002, while domestic visitors spent \$8.6 billion, or \$285 per trip.
- International tourists typically spend more time in New York per trip, which helps account for the higher expense -- 39% spend 1 to 3 days, 35% up to a week and 23% spend longer than eight days.
- While in New York, shopping and dining are the most popular activities for international visitors, while approximately half sightsee and visit historic places.

In a 2003 survey conducted by the Downtown Alliance, visitors' top destinations in their visits to Lower Manhattan were Ground Zero (66%), South Street Seaport (53%), Ellis Island and Statue of Liberty (45%), Historic Battery Park (33%), Century 21 discount shopping store (26%), St. Paul's Chapel/WTC Memorial (26%), the Staten Island Ferry (23%) and Trinity Church (16%). Visitors were equally distributed among international visitors (32%), the local region (36%) and the rest of the US (33%). The average household income of these visitors was \$77,800, well above the national average of \$58,208 (Exhibit II-33).

The typical number of visitors to Lower Manhattan is between eight and ten million, with four to five million visitors attending Ellis Island and Statue of Liberty. This represents a 23% capture for Lower

Manhattan of all visitors to New York. Recent reports have estimated that Ground Zero now attracts six to seven million people annually.

Ground Zero will have a lasting effect on the number and type of visitors to Lower Manhattan during the rebuilding period and beyond. The nature of the event struck a chord with the community-minded character of New Yorkers. The level of the public's interest in the design selection process surprised the Lower Manhattan Development Corporation, which altered its strategy to host town meetings in every borough and public forums for discussion at multiple steps along the way. Residents of New York and New Jersey will remain vested in the building and the area's redevelopment for many years. People care more than ever about the shape and environment of Lower Manhattan, an aspect that will likely have a ripple effect on community-level improvements.

The redevelopment of the waterfront is another factor that will contribute to the increase in visitors to Lower Manhattan. Battery Park and the Hudson River Park have already drawn pedestrians, bikers, joggers, kayakers, parents and their children to the edges of the water. More than 32,000 New Yorkers used the kayaks in downtown during the summer of 2003, and festivals and concerts happen frequently along the Piers of the Hudson River and lawns in Battery Park. The East River Park Development, currently in planning, will open the eastern edges to recreational and communal activities on the water, providing a further reason for New Yorkers to explore their waterfront. Governors Island will be in the sight line of all visitors to these destinations and able to capture a large portion of them.

Existing and improved destinations in Brooklyn will also have an effect on the number of visitors in the area of Governors Island. The Brooklyn Museum of Art, Brooklyn Botanical Gardens and Brooklyn Academy of Music are all major attractions. There is potential for the Brooklyn Nets to draw weekly traffic to the area during the season and for special events. Similarly the Brooklyn Piers may draw traffic to the portion of Brooklyn proximate to Governors Island as the proposed Cruise Ship Terminal comes on line. The proposed Brooklyn Bridge Park promises to revitalize the waterfront north of Governors Island, creating a regional recreational destination that will place at least this portion of Brooklyn near the top of the list of "must-see" destinations in New York City.

### III. Conference Center

#### Summary

We have found that there is a strong market opportunity for a high-end executive center at Governors Island. Certainly, the Manhattan employment base will drive demand for weekday conferencing, typically in peaks of Monday to Wednesday and Thursday to Friday and in groups of 45 to 75 persons. There may even be an opportunity to reach an agreement with one or more large users for dedicated blocks of space; dedicated space significantly lowers risk due to guaranteed occupancy, and therefore greatly enhances the marketability of the project to sources of equity and financing. Given the natural and built amenities that will potentially be on the Island, we believe that the conference center hotel can also compete for leisure demand on the weekends at rates higher than normal for executive conference centers.

Through our research and analysis efforts, we have found that the optimal size for a conference center on Governors Island ranges from 250 to 350 rooms, with 30,000 to 40,000 square feet of meeting space. Individual guest rooms can range from 350 to 450 square feet, and the amount of meeting space per room ranges from 100 to 125 square feet; the lower end of the range would be more appropriate if a larger leisure market for hotel rooms than is typically found in many other conference center hotels was achievable at Governors Island.

According to our initial interviews, a complete meeting package (CMP) of between \$350 and \$450 during peak season would likely be required to justify a new hotel conference center. The operators

we interviewed felt that Governors Island should be able to command a price premium above the top of the market due to its unique history, character and location adjacent to Lower Manhattan. The premium will include not only higher peak CMPs, but also less discounting on the weekend and off-seasons. The average CMP for a conference center at Governors Island should fall in the \$350 to \$400 range, with peak CMPs averaging in the \$400 to \$450 range.

While a minimum occupancy rate of 50% to 60% is required by most operators, the site's competitive advantages will likely allow for a higher occupancy rate due to increased market share from proximate employers, its role as one of only two true residential conference centers in or near Manhattan and more demand than is typical from leisure/weekend travel. The center may also be able to guarantee more space through the ability to sell dedicated space to prominent Manhattan firms or institutions. Our demand analysis suggests that an occupancy rate of approximately 80% is achievable.

The conference center must offer modern units and amenities, including guest and meeting rooms built with the business user in mind (including the appropriate technologies), excellent food service and other project amenities such as a fitness center and recreational areas. Utilizing architecturally significant buildings is not only important in order to fulfill the historic preservation mandate for the development of the Island, but also will contribute the quality and uniqueness of the overall experience for the end user. There will also be opportunities to create synergies with other uses on the Island, such as passive and active recreational amenities,

historic places such as Fort Jay and Castle William and other educational and learning resources.

A conference center on Governors Island would benefit from a premier amenity package. Conference center operators have indicated that while some level of golf would be an intriguing addition to the project, its inclusion is not necessary to the success of a site with so many other strengths. We do recommend examining the potential for a chip-and-putt course or at the very least a waterfront driving range. It will be important for the conference center to provide a fitness center and take advantage of the potential for excellent walking/strolling trails. To the extent possible, the provision of an all-season swimming pool and all-season tennis courts should be explored, as their inclusion on-site would make the site even more competitive. Conference center operators we interviewed have indicated that in lieu of golf, some level of spa amenity would provide an additional draw to help backfill weekend occupancy. There are certainly challenges associated with conference center hotel operation on the Island that must be overcome or mitigated, such as transportation to the Island, inclement weather and mixing public access with a semi-private retreat. The consulting team will be working on these challenges in the coming months, and in some cases there will be an opportunity to turn a challenge into a strength – such as selling the ferry experience as a positive rather than a transportation constraint.

## Introduction and Definitions

In the hospitality industry, conference centers have carved out a competitive niche distinct from hotels that provide gathering spaces. With strict standards set by the International Association of Conference Centers (IACC), conference centers are best defined by the following characteristics:

1. A majority of space dedicated only to conferences and meetings.
2. Conference rooms available around the clock.
3. Tables with hard writing surfaces and upholstered armchairs that keep occupants comfortable during long sessions.
4. Food and beverage specifically designed to accommodate conference groups (i.e. buffet meals, healthy alternatives, continuous refreshment breaks and group-specific dining areas).
5. Lighting, acoustics and wall surfaces all designed for the special needs of conference business.
6. Electrical, AV and telephone outlets sufficient for conference needs.
7. Specialized generalists - personnel that are dedicated to working closely with meeting planners and participants.

Conference centers are typically divided into four categories: resort, executive, corporate, and university.

- Resort conference centers are typically located alongside a golf course or body of water, and they market their amenities to a target market that seeks recreation and leisure alongside a modicum of gathering and meeting space.

- Executive conference centers are geared more toward business decision-makers who demand top-flight meeting and gathering space and who may not have time or desire to involve themselves in an extensive outdoor amenity package. Guest rooms must be of a high quality, with a particular focus on functionality.
- Corporate conference centers, or day centers, serve dual purposes. Much of the space is dedicated to one or more large firms with consistent conference and meeting space needs. However, excess space is available to the broader marketplace. Corporate conference centers typically do not have guest rooms
- University centers are spaces affiliated with a college or university. When space is not used for university purposes, the center is marketed for external meetings. The availability at these centers must accommodate the academic year, and university-related functions almost always receive priority. The amenity packages are typically less robust than privately operated centers.

Conference centers cater primarily to the business community, providing boardrooms and guest rooms and designing their amenity packages to the special needs of business travelers. This is an important distinction from hotels that have meeting space, which cater primarily to leisure traffic but may have the space necessary to hold large events such as conventions, weddings or bar/bat mitzvahs. Conference centers, because they book groups of 40 to 70 participants months in advance, have a more predictable income stream than leisure or meeting hotels. They also have more predictable transportation constraints, as conference-goers

tend to stay put for days at a time while leisure hotel travelers tend to desire maximum mobility from their hotel.

Unlike meeting hotels, which sell room nights and meeting space, conference centers sell complete meeting packages (CMPs), which include the cost of a room, meals, audio/video, conference space, continuous refreshment breaks, presentation and meeting supplies, etc. Conference centers seek to maintain an 80%/20% business traffic to leisure traffic occupancy mix, with the vast majority of business traffic composed of overnight meetings. Conference centers largely differentiate their marketing and advertising from meeting hotels, choosing to leverage their excellent meeting facilities and meeting planner services as their competitive advantage, in addition to location and recreational amenities.

A breakdown of national and local data on the conference center industry is provided in Exhibits III-1 through III-7. The national market is nearly evenly split among these four center types. For the purposes of further discussion, we will focus on resort and executive conference centers. These two centers represent the strongest fit for Governors Island based upon our preliminary analysis and our discussions with conference center operators.

A typical conference center provides between 100 to 150 square feet of dedicated meeting space per guest room. Centers can range from 50 guest rooms to over 300, and can offer as little as 10,000 square feet of meeting space to upwards of 40,000 square feet. The optimal size of a center for management purposes is between 250 and 350 guest rooms and 30,000 to 40,000 square feet of meeting space. Guest rooms and meeting

rooms should offer the modern amenities that corporate users require, such as high-speed internet access. Increasingly, conference center operators offer dedicated meeting planners and staff as standard operating procedure, further differentiating themselves from hotels, which may offer concierge and support services rather than de facto meeting planners.

### Industry Overview & Critical Success Factors

Conversations with New York City meeting planners as well as a review of the industry literature confirms that conference centers are now the destination of choice for business meetings, whose attendees often demand top-flight meeting space free from distractions, rather than converted ballroom space with meandering tourists nearby. Additionally, firms tend to choose conference center destinations based on:

- Price: For training/sales meetings, the primary driver is price point and amenities. These “lower-tier” meetings can take place anywhere large numbers of participants can be accommodated at the lowest price with a modicum of amenities.
- Location: For executive meetings, the primary driver is proximity to the firm headquarters or central business districts. The quality of the actual meeting space, as well as its convenience to firm headquarters, is of crucial importance, as busy executives have little time for extraneous travel and demand top-flight meeting rooms for their gatherings.
- Amenities: For selected meetings, such as executive or “reward” retreats, offering excellent recreational opportunities, an exciting

and unique location and access to luxurious services and amenities.

According to conference center operators, recent cost-cutting measures prevalent in New York City firms have influenced the following recent market trends with respect to conference centers.

- Meeting planners and conference center operators confirm that meetings have become shorter and more efficient, usually lasting two to three days, resulting in Sunday through Wednesday and Wednesday through Friday occupancy peaks for conference centers.
- Demand for conference center services is typically regional in nature. Executive conference centers tend to locate no further than 45 minutes from a major airport, and resort conference centers draw demand from a maximum of three hours from the location of a firm headquarters, either by air or by land.
- During economic downturns, executive conference centers continue to maintain or exceed target occupancy, while the other categories of centers tend to see declines in both CMP and occupancy.
- Golf and other time-intensive recreation, once a required component of many conferences, are now waning in popularity, especially as conference schedules demand maximum productivity and a younger generation of workers is less inclined to play even a 9-hole executive course. In fact, conference centers today support their golf course operations primarily by selling club memberships in the local residential community, rather than via usage fees from conference-goers.
- Corporate conference centers, which typically

maintain 80% of their space for in-house meetings, are increasingly being managed by or sold to conference center operators. This is due to cost-cutting measures at the firm level, as well as the need to reap efficiency gains leveraged by conference center operators, which can book and retain conferences to fill dead space with greater ease than companies can. Merrill Lynch, for example, now has private conference center operators managing operations and sales at three of its New York/New Jersey area conference centers.

- Conference centers differ in their weekly and seasonal peaks. Executive conference centers are typically full on weekdays and relatively empty on weekends, with seasonal peaks occurring between April and November, with winter lulls and another lull in August. Resort conference centers can usually achieve slightly higher weekend occupancy due to their ability to draw amenity-seeking leisure traffic. However, their seasonal fluctuations are usually more severe than Executive centers, and some even close altogether during the winter.

Critical to the success of a conference center is the identification and retention of a repeat client base. In the case of resort conference centers such as The Sagamore, dedicated New York City clients book space year after year, and weekend traffic consists of repeat customers attracted to the nearby summer horseracing season in Saratoga Springs. Without a wintertime draw to this summertime resort, The Sagamore goes dark through much of the winter. In the case of Doral Arrowwood, 60% of their space is permanently reserved by Pfizer, Inc. (Pfizer Learning Center, or PLC). This inflates

their occupancy levels and CMP rates slightly, but also ensures that Arrowwood, which is located 45 minutes from Manhattan, maintains consistent occupancy year-round. Dolce International manages numerous New York City properties year-round by retaining over 120 dedicated New York City clients.

### Competitive Market Analysis

We believe that the Competitive Market Area (CMA), the area containing properties with which the subject site will compete, includes the New York Primary Metropolitan Statistical Area (PMSA), Fairfield County in Connecticut and the New Jersey Counties of Bergen, Hudson, Essex, Passaic, Union and Morris. A conference center on Governors Island will also compete with Princeton-based conference centers such as Doral Forrestall and Chauncey Conference Center, although these centers draw a majority of their clientele from the pharmaceutical firms of Princeton, NJ, and may not directly compete with the subject site for Manhattan clients. Exhibits III-9 through III-16 provide data on the competitive marketplace.

Of the IACC-approved conference centers that claim to serve the New York City metropolitan area, RCLCo identified twenty-one (21) centers in the CMA. Only one of these centers, the Millennium Broadway, lies within New York City. Through site visits and interviews with center staff and management companies, we conducted a thorough assessment of these 21 centers with regard to market capture, CMP rates, occupancy, capacity and amenity packages. We have also conducted a competitive evaluation of these centers with respect to their competitive positioning vis-à-vis a potential conference center on Governors Island.

Harrison Conference Center at Glen Cove and Dolce Tarrytown House are highly comparable conference centers within the CMA. Both centers have utilized buildings of historical and architectural significance to create a campus-like learning environment targeted to top-level executives from the New York City and regional markets. Glen Cove offers 196 guest rooms, while Tarrytown house offers 212, and the centers offer 25,000 and 30,000 square feet of meeting space, respectively. Both centers cite occupancies of around 85% during the week, with Glen Cove averaging 15% occupancy on the weekends, and Tarrytown House faring slightly better, at 30% on average. Neither center offers golf on-site, though they both provide fitness centers, tennis courts and swimming pools. Tarrytown House charges a base \$279 CMP and \$169 CMP for peak and off-peak seasons, respectively, while Glen Cove charges a similar amount \$259 for peak season CMP. While sales managers advertise these CMP rates, it should be noted that they are base prices that do not include peak premiums or upgrades. For example, peak scheduling, including open bar service, and/or serviced rather than buffet meals can significantly impact the CMP rate. A full-service CMP for a typical upper-tier client, such as those found in Manhattan's financial services sectors, can reach the high \$300s or low \$400s, once the aforementioned premiums are included.

Doral Arrowwood is a much more modern center with an adjacent 9-hole executive golf course. Arrowwood has a proprietary relationship with Pfizer, Inc. to house and service the Pfizer Learning Center, dedicated conference and training space that guarantees a certain amount of occupancy year round. Besides Pfizer, the center caters primarily to corporate clients from New York City, Fairfield

County, CT and northern New Jersey, with 20% of its demand emanating from beyond these regions. Because the center courts weekend leisure traffic, Arrowwood is as large as some hotels, offering 374 guest rooms and 30,000 square feet of meeting space, and charges \$416 CMP and \$280 CMP during peak and off-peak seasons, respectively.

The IBM Palisades conference center is also a newer, modern building located in a pastoral setting, offering guest access to an 18-hole golf course, tennis, a fitness center and proximity to the historic town of Piermont-on-Hudson. Branded as a technology-rich environment, IBM Palisades caters to a tech-savvy corporate clientele desiring meeting space in a serene atmosphere within driving distance of Manhattan. This site is also able to command CMP rates of \$380 to \$410 during peak season, and \$299 during off-peak season. According to sales staff, IBM Palisades maintains a conservative average annual weekday occupancy of 60%, with an estimate of weekend occupancy of 20%. It offers 206 rooms and 48,000 square feet of dedicated meeting space in 43 meeting rooms.

Edith Macy Conference Center, located in Briarcliff Manor, NY, is smaller than its peers, offering 86 rooms and only 14,000 square feet of meeting space. They maintain excellent weekday occupancy rates of 70% but weekend occupancy can be as low as 10%. Edith Macy does not offer golf, but instead markets its "team building activities", which have waxed and waned in popularity over the years. When we interviewed the sales staff at Edith Macy, they quoted a range of \$200 to \$225 for off-peak CMP, but did not disclose peak rates, which we assume to be in the high \$200s to low \$300s.

The Millennium Broadway commands peak CMP rates of \$259 to \$355, lower than rates of centers that provide the type of environment similar to that potentially provided at the subject site. Even though the Millennium Broadway meets IACC criteria, we feel that its attempt to cross-market its rooms to both transient and conference guests may undercut its attempt to secure top-of-the-market CMP rates, as executive conference-goers prefer secluded environments during weekday meetings. In addition, it appears that the Millennium Broadway is absorbing a fair share of “training” and “sales” meetings, which typically garner lower CMP rates than executive-level meetings. We therefore feel that while Millennium Broadway is located in Manhattan and IACC-approved, it is not representative of the occupancy mix or attainable CMP we expect the subject site to absorb and achieve.

In summary, executive conference centers in the New York metropolitan area run profitably by targeting executive-level conference attendees from the numerous headquarters and firms located in the Hartford to New Brunswick region, with a focus on the Manhattan market. This clientele supports peak-season CMPs in the high \$300s to low \$400s at conference centers that provide top-flight technology alongside serene, peaceful environments for learning and decision-making and market their excellent meeting space/facilities in addition to a wealth of recreational amenities.

Conversations with conference center operators in the CMA suggest that the subject site has a significant competitive advantage over existing centers in that it can provide a serene, campus-like environment – highly desired by conference-goers

– without necessitating lengthy travel through congested roads into Westchester or Connecticut. Additionally, the ability to hold a meeting or session in a serene setting, less than 1,000 yards from Manhattan, with views of the Statue of Liberty in the background, should carry significant cachet in the marketplace.

Finally, with only one other residential conference center located in Manhattan, and one we feel caters to a middle- rather than upper-tier clientele, we believe that the existing demonstrated demand for conferencing facilities may be somewhat muted due to the capture of demand by less-optimal meeting locations such as luxury meeting hotels and day centers. We feel that the addition of a conference center at the subject site could catalyze additional demand by providing the region’s most highly-desired atmosphere at a hitherto unprecedented level of convenience.

### **Target Market**

Through surveys of IACC-approved conference center operators and sales directors at conference centers located in New York, Connecticut and New Jersey, we feel that the subject site’s Primary Market Area (PMA), the area from which it will draw the vast majority of its occupancy, stretches from Hartford, Connecticut to just north of Princeton New Jersey. Because the subject site is one of national and even international significance, we believe that the site has the potential to garner a limited amount of occupancy from a national and even international base of conference goers. Finally, we believe that a conference center located at the subject site also has the potential to capture a higher-than-normal share of weekend leisure traffic due to its proximity

to the tourism nodes of New York City in general, and Lower Manhattan in particular.

We feel that executives, CEOs and upper level management located in Manhattan and its immediate surrounding employment cores are the most appropriate target market for the subject site. Firms tend to hold executive and some training meetings in locations that are convenient to their national or global headquarters, minimizing the opportunity cost of time for their most valuable employees. Approximately 15% of the Fortune 1000 have headquarter locations within the region between Hartford, CT and New Brunswick, NJ, with the heaviest concentrations by zip code occurring in Midtown and Lower Manhattan. Approximately 18% of Fortune 500 firms have headquarters located in this band, and 30% of the Fortune 100 firms are located in this region.

Most importantly, the subject site is located minutes from Manhattan, a market that conference center operators have agreed is underserved with respect to true conference centers and which boasts an extraordinary concentration of national and global firm headquarters. Governors Island is also within a 90-minute drive from firm headquarters in Northern New Jersey and Eastern Connecticut, and it is located within 45 minutes of three major international airports, La Guardia International, JFK International and Newark International. We believe that current New York City based conference attendees would appreciate the convenience of a near-Manhattan location combined with the feeling of “getting away” in an idyllic, campus-like environment ideal for a learning, thinking and decision-making.

Employment loss in Manhattan should not have an overly significant effect on demand for a conference center on Governors Island. Recent employment losses are due to a variety of factors, most of which are not permanent. Further, as mentioned in the economic analysis before, many firms are choosing to maintain their headquarters – and therefore executive employment – in Manhattan, making the subject site an outstandingly convenient and desirable alternative to the long and congested drives outside the city limits to reach a comparable environment such as Glen Cove or Tarrytown House. Even if operations have moved elsewhere in the region, the corporate clientele most likely is still within an acceptable travel distance of Governors Island.

Given the apparent migration of some middle-level and/or “back office” employees beyond the city limits, as described in the earlier section, we do not feel that the subject site should market itself as a “training” conference center. Furthermore, despite the potential for a robust amenity package at the subject site, we feel that the mid-Atlantic region climate may preclude maximum year-round occupancy should the subject site be developed as a true “resort” conference center. Finally, because of contraction in the day or “corporate” conference center industry – as evidenced by the change in operation of the Merrill Lynch centers in the area, we do not feel that a “corporate” or “day” orientation is the optimal target marketing for a conference center on the subject site.

Based upon interviews with conference center operators in the PMA, we feel that a typical meeting would consist of executive groups ranging in size from 40 to 75 persons with an average stay of

three nights. We feel that this market will make primary use of both medium-sized meeting spaces of up to 2,000 square feet and smaller breakout rooms of 100 to 400 square feet. There may be an occasional need for a larger hall, perhaps as large as 4,000 to 6,000 square feet, in addition to the requisite dining, lounging and recreational amenities. The target market will emerge primarily from Lower Manhattan and Midtown companies, with ancillary demand emerging from companies located in Northern New Jersey, Westchester County, NY and Fairfield County, CT.

The Island should also be able to attract weekend and leisure traffic to the conference center facility, given its unique characteristics and natural beauties. However, attracting this market segment will also likely require some harder amenities, such as a spa facility, that can be sold as a package.

### **Demand Analysis**

Our demand analysis, provided in Exhibit III-17, confirms that demand does exist for a conference center facility at Governors Island. The demand model calculates existing demand conditions in the region based upon the expected performance of the existing competitive supply. We have then applied a capture rate for Governors Island – 7.5% for the weekday market, and 10% for the weekend traffic – based upon our assessment of the competitiveness of the Island as a location. Clearly, we believe the Island can capture more than its fair share of demand from within the competitive market set.

We have also factored in additional demand that will be generated by the unique opportunity at Governors Island. This includes demand that

originates from outside of the market currently being served by the competitive market, as we do believe that Governors Island will be able to reach more of a national and global market than the typical competitive center. This factor also includes business demand that remained internal, but is tempted to outsource meeting needs because of the attractive opportunity at the Island. This would include some pre-booked space by large firms. We do believe the increase in demand will be larger (on a percentage basis) for weekend travel, as the center is able to compete with luxury hotels and resorts for leisure traffic with which a typical center does not normally compete.

Our demand analysis shows that there is adequate support for a 300-room center. Average occupancy will reach 80%, which is very high for conference centers. Weekday occupancy will hover near 89%, and we expect that weekend occupancy can reach 69% -- certainly a unique situation for the conference center marketplace, but one, once again, that we feel is achievable given the unique attributes of the Island.

## IV. Hotel

### Summary

The Manhattan hotel market was significantly weakened by the economic shock of September 11th combined with a national economic recession. From 2001 to 2003, the hotel occupancy rates stayed relatively healthy (around 75%), but this occupancy was bought by lower room rates, as the average daily rate (ADR) in the Manhattan hotel market dropped from \$224 in 2000 to \$183 in 2003. The combination of drops in occupancy and ADR resulted in a very strong drop in REVPAR, from \$187 in 2000 to \$138 in 2003, including a 21.7% drop just from 2000 to 2001.

However, the market has rebounded significantly in the past six months. New York occupancy rates through April 2004 have increased to 77.5% compared to 66.5% for the same period in 2003; occupancies in recent months have increased above 80%. ADRs have shown more modest increases in the past year, although the ADR through April 2004 is still 11.3% below 2001 numbers for the same period. However, the stemming of ADR declines with increased occupancies is a very good sign for the near and mid-term health of the New York City hotel market.

Lower Manhattan is a relatively small hotel submarket, generally known only for business hotels serving the financial district. Yet, that is changing, and we believe the leisure market will become more and more prominent over the next decade. The Lower Manhattan neighborhood is gaining momentum, as more homes, restaurants, hotels and park activities draw locals and visitors below

Houston Street. The September 11th Memorial should further establish Lower Manhattan as a destination for local, national and global visitors. The Ritz Carlton Battery Park and several full-service and limited-service hotels, such as the Millennium Hilton, are already attracting strong weekend leisure traffic into Lower Manhattan. Boutique hotels in the Tribeca, SoHo and Village neighborhoods have also been very successful in attracting high-end leisure travelers.

We have projected that there will be significant excess hotel demand in Lower Manhattan from 2004 to 2010. Taking into account current known supply, we estimate that as many as 4,400 new hotel rooms can be supported in Lower Manhattan by 2010. This is due to overall growth in the size of the Manhattan market, as well as an increasing share of new growth that will be captured in Lower Manhattan. Currently, approximately 43% of the planned new hotel rooms in Manhattan will locate in Lower Manhattan – approximately 1,970 new rooms by 2010 (excluding any hotel rooms developed on the World Trade Center site).

Given the projected future demand-supply conditions, we believe there will be a strong opportunity to develop one or more hotels on Governors Island over the life of the redevelopment project. Governors Island offers a unique, attractive environment that will be incredibly desirable to a niche of the hotel consumer market. In particular, we project that two 100-room boutique hotels can be supported on the Island by 2010.

Boutique hotels are a growth segment within the Manhattan hotel market, and we believe that this concept is a better fit with the Island than other

types of hotels. Boutique hotels are smaller, and can be better oriented towards the strengths of Governors Island – natural beauty, seclusion – and away from its challenges – transportation, lack of a critical mass of development – because boutique hotel customers are more likely than other types of hotel guests to buy into a retreat concept. We envision an “urban getaway” concept for a boutique hotel on Governors Island – a small, luxury hotel that provides the appropriate level of services and can offer easy access back to Manhattan, but more critically can also offer the natural and built beauty of Governors Island. We are also assuming that complimentary uses, in particular a spa, will be available to guest of the boutique hotel. The projected ADR at a boutique hotel on Governors Island will be \$350 to \$450 (2004 dollars).

We believe there is a more limited opportunity to deliver a luxury hotel on Governors Island. The market support for a luxury hotel in the Manhattan market is strong given growth in total demand, although this will continue to represent a market niche. The proven success of the Ritz Carlton Battery Park shows that, given the right environment, Lower Manhattan can attract this market segment. However, Governors Island may be a more difficult fit for this market segment, as the luxury hotel consumer may be less likely than boutique hotel guests to leave the critical mass of activity in Manhattan and accept inconveniences associated with the transportation to and from Manhattan (or points elsewhere). Our demand analysis found some support, but not enough of a demand to justify the construction of a new hotel. In the mid- to long-term, once Governors Island is established as a destination and a critical mass of complimentary uses have been developed, a

moderate opportunity may exist to develop a 250 to 300-room luxury hotel, if the an operator with an established brand can be attracted to the site.

There is a limited opportunity to develop a full-service or limited-service hotel at Governors Island. The market support in Manhattan for these types of hotel are also strong, especially limited-service hotels as they have filled a gap as a lower-cost alternative. However, typically, these two hotel concepts cater to more price-sensitive, convenience-oriented guests, such as business travelers. These types of guests would be particularly sensitive to the relative lack of activity and services on the Island, as well as any inconveniences or constraints on transportation. These types of hotels would allow for a greater range of price points on the Island, but providing heavily discounted rooms will likely cause market confusion and dilute the experience of the much more expensive boutique hotels. It is also unlikely that a hotel priced competitive with other full-service or limited-service hotels could support the expected construction costs on the Island.

## Market Overview

The New York City and Manhattan hotel market enjoyed an unprecedented period of health in the mid and late 1990s. The hotel room occupancy rate in the Manhattan hotel market was above 80% from 1996 to 2000, and average daily rate (ADR) and revenues per available room (REVPAR) increased by double digits each year from 1996 to 1998. The growth in ADR in the Manhattan market began to slow in the late 1990s, but remained at a still healthy 5%-7% increase each year until 2001. For the year 2000, which represented the peak of this period,

the Manhattan ADR had hit \$224 and the REVPAR stood at \$187 (Exhibit IV-2).

In 2001, the hotel market experienced a sharp dive in occupancy and ADR. September 11th had a serious impact on business and tourist demand in late 2001 and early 2002; the shocks of 9/11 were exacerbated and prolonged by a further slowdown in business and leisure travel due to a national and regional economic recession. From 2001 to 2003, the hotel occupancy rate hovered around 75%. While historically, and relative to other markets, these occupancy levels are still healthy, they were bought by reducing room rates. The ADR in the Manhattan hotel market dropped from \$224 in 2000 to \$183 in 2003. The combination of drops in occupancy and ADR resulted in a very strong drop in REVPAR, from \$187 in 2000 to \$138 in 2003, including a 21.7% drop just from 2000 to 2001 (Exhibit IV-2).

Recent data suggests that the hotel market in New York City has rebounded, with an increase in occupancy to 77.5% (through April 2004), compared to 66.5% for the same period in 2003. The New York City ADR also showed significant increase to \$185 through April 2004 from \$179 for the same period the year before – an increase of 3.5%. The increase in ADR is modest, and the ADR through April 2004 is still 11.3% below 2001 numbers for the same period. However, the stemming of ADR declines with increased occupancies is a very good sign for the near-term health of the New York City hotel market (Exhibit IV-1). HVS International has projected an even more robust recovery for the Manhattan hotel market, with a projected occupancy in 2004 of 81%, and a projected ADR of \$193, an increase of 6% from the 2003 data (Exhibit IV-2).

## Lower Manhattan Hotel Trends

Lower Manhattan is a neighborhood gaining momentum, as more homes, restaurants, hotels and recreational activities draw locals and visitors below Houston Street. SoHo's gentrification and the infusion of restaurants and nightclubs in the Lower East Side and Tribeca are all positive catalytic trends. Redevelopment efforts and a shifting focus towards the waterfront have begun to change the misperceptions about the isolation and staleness of Lower Manhattan. Finally, Ground Zero (and the eventual 9/11 memorial) is an anchor of Lower Manhattan's redevelopment efforts, and is expected to create a very important destination for local, national and global visitors to New York. The traffic driver of Ground Zero will be compliment and leverage the established tourist destinations of the Statue of Liberty and Ellis Island, which typically attracted between four and five million visitors (out of the eight and ten million visitors to Lower Manhattan in total) before 9/11.

Midtown is Manhattan's largest hotel submarket, with 47,350 rooms, or 73% of the total Manhattan market. In sharp contrast, Lower Manhattan, defined as the area south of Houston Street, has only 5% of Manhattan's hotels, or 3,240 rooms. Yet, Lower Manhattan has generally outperformed the Midtown submarkets. In 1998, the REVPAR in Lower Manhattan in 1998 was \$192, with an increase to \$220 by 2000. This is compared to a 2000 REVPAR of \$182 and \$216 in Midtown West and Midtown East, respectively. Further, while Lower Manhattan experienced a sharp decline in performance – REVPAR dropped 22.7% from 2000 to 2003 – this drop was less than in the Midtown markets – the REVPAR in Midtown West dropped

24.1% over this period, and Midtown East declined by 28.2% (Exhibits IV-4A and IV-4B).

The strong performance of Lower Manhattan has been due in great part to the smaller inventory, combined with a large, captive source of demand from downtown employment. The room supply below Houston Street is expected to grow dramatically with the addition of more than 2,000 rooms by 2008 -- a 73% increase in hotel supply over the submarket's existing 3,240 rooms. Obviously, the increase in inventory will require that the submarket is able to attract a larger, and also more diverse (business vs. leisure), market.

### Trends by Hotel Type

First-class hotels are the most common hotel in the Manhattan market, with 41% of all hotel rooms, followed by limited-service hotels with 28% of the supply, luxury hotels with 19% and boutique hotels with 13%. Not surprisingly, the luxury hotel segment (2003 ADR of \$303) has achieved the highest ADR positioning, followed by boutique (\$215), first class (\$186) and limited service (\$122). In general, the limited service and first class segments have enjoyed the strongest occupancies, followed by luxury and then boutique (Exhibits IV-4C and IV-4D).

The boutique hotel segment was the strongest growth segment in Manhattan in terms of performance during the late 1990s. From 1998 to 2000, ADR and REVPAR for the boutique hotel segment increased 22% and 40% respectively, well in excess of the growth in other segments -- luxury (13% growth in ADR, 14% growth in REVPAR), first class (10%, 13%) and limited service (13%, 12%). This growth is likely due to the introduction

of destination boutique hotels, which offered a level of luxury that could command a higher ADR and occupancy rate, as well as changes in consumer preferences towards more unique hotel experiences and market-wide growth in room rates that allowed smaller hotels to aggressively push rates and still maintain the position as a price alternative to many luxury and first class hotels.

While the boutique, luxury and first class segments all experienced similar declines (approximately 25%) in REVPAR from 2000 to 2003, the boutique hotel has been the first segment to post positive REVPAR growth in 2002 and 2003, although only 0.9% and 1.4% for these two years. The boutique segment was hit harder initially (with a 27% drop in REVPAR from 2000 to 2001) than other segments, but has shown a greater ability to rebound than the other segments. The boutique segment is also the only segment to achieve overall positive REVPAR growth from 1998 to 2003, albeit a modest 4.3% growth over this period -- a testament to the relatively low base in 1998, the growth from 1998 to 2003, and the modest growth since 2001. The limited-service segment experienced the sharpest REVPAR drop from 2000 to 2003 (31%) and 1998 to 2003 (23%), and luxury hotels performed slightly better than first-class hotels over these two periods. Hotels that are able to offer a unique experience are most often more resilient during downturns, which accounts for some of the relative resiliency in the boutique and luxury segments (Exhibits IV-4c and IV-4D).

The boutique hotel segment is the fastest growing segment in terms of new supply, having increased its share of the Manhattan market from 8% to 13% from 1998 to 2003. Over this time period 33% of

the new hotel rooms delivered were in boutique hotels (Exhibits IV-4c and IV-4D).

### Competitive Market Analysis

Exhibits IV-5 through IV-12 provide data on selected hotel properties in Manhattan, with a particular focus on the Lower Manhattan submarket.

We collected and analyzed performance data on five major downtown hotels: Ritz Battery Park (298 rooms, Millennium Hilton (383), Marriott Financial Center (499), Holiday Inn Wall Street (227) and Embassy Suites (463). Data reporting for the remaining four begins in May 2002, when the Embassy Suites reopened after the attacks. The Hilton Millennium, situated directly across the street from Ground Zero, reopened in May 2003 and began reporting in the same month. The renovated Marriott Financial Center and the new Ritz Carlton Battery Park both opened in January 2002 (Exhibits IV-5a through IV-5C).

This group of Lower Manhattan hotels has outperformed the Manhattan market as a whole. In 2003, ADR for the downtown hotels was \$201 versus Manhattan's \$183, and the REVPAR was \$147 versus \$138. The recent data presents strong evidence of the rebound of the hotel market in Lower Manhattan. From May 2002 to 2003, the average occupancy stayed the same (76%), but the ADR increased 17% (from \$201 to \$235) and the REVPAR increased 16% (\$153 to \$178). From May 2003 to May 2004, the rebound was even clearer, with a significant increase in occupancy (from 67% to 78%), along with a 9% increase in ADR (\$196 to \$213) and a very strong 27% increase in REVPAR (\$130 to \$166) (Exhibits IV-5a and IV-5B).

The selected downtown hotels are clearly driven by weekday travel, which is primarily business-oriented. The REVPAR of this group of hotels was approximately 20% above the weekly average on Tuesday and Wednesday, 5% above on Monday and Thursday, 5% below on Saturday, 15% below on Friday, and 30% below on Sunday. The relative decline in REVPAR on Friday and Saturday has more to do with reduced room rates than sharp drops in occupancy. The group of hotels enjoyed an 83% occupancy on Saturday and 75% occupancy on Friday, although the ADR for both nights was roughly \$185, from a weekly average of \$209 (Exhibits IV-5a and IV-5B).

This secondary data was confirmed by our review of asking room rates and interviews with hotel managers. Exhibits IV-8 and IV-9 provide the data and graphical displays of asking rates of a select number of the most relevant hotel properties in Manhattan. The eight surveyed hotels in the downtown area reduced asking room rates an average of 15% from weekday to weekend. This includes a 22% weekend discount at the Ritz Carlton Battery Park, a 29% weekend discount at the Millennium Hilton, and a 16% discount at the Marriott New York Financial Center.

The performance of downtown hotels on the weekend must be placed in the proper context.

First, merely looking at percentage discount can be misleading, since the absolute room rate relative to other options should also be considered. For example, the Ritz Carlton Battery Park does significantly discount its weekend rates, but in absolute terms, its asking weekend rates are still among the highest in Manhattan.

Second, lower asking room rates are buying occupancy; an unhealthy leisure market would struggle with both pricing and occupancy. The strong occupancies with the discounted room rates proves that the issue is not an inherent problem with getting leisure visitors downtown, but more to do with adjusting room rates to reflect the fact that leisure visitors will naturally pay less than business travelers in this market.

Third, downtown is not alone. Even those submarkets that are commonly perceived as stronger tourist destinations significantly discount on the weekends. For example, the Ritz Carlton Central Park discounts its standard rooms 9% on the weekends, The Mandarin Oriental and Four Seasons in Midtown also discount weekend rooms 12% and 11%, respectively.

It must also be noted that even those hotels that do not publish discounted room rates on the weekends likely still do provide deals. Often hotels will not publish discounts farther in advance, and will use shorter-term tactics, such as releasing deals to discount web sites, in order to fill weekend vacancies. Presumably this allows hotels to maintain rack rates during event weekends such as the Marathon, Fashion Week or the upcoming Republican Convention.

### **Luxury Hotels**

The Ritz Carlton Battery Park, as the only 5-star/5-diamond hotel south of 56th Street, has performed extremely well, with reported occupancy in the high 90%'s year round. Weekday asking room rates range from \$500 to \$660, with suites ranging from \$750 to \$1,150. As discussed above, there is a

weekend discount, with asking room rates ranging from \$400 to \$500, although there is no discount for the suite units.

The Battery Park property is discounted heavily relative to the Central Park Ritz – a 17% and 28% discount on the weekday, and a 29% to 40% discount on the weekend. The Ritz Carlton Battery Park is also priced below other notable ultra luxury hotels in Midtown, such as the Mandarin Oriental (\$745 average asking room rate on weekday, \$659 on weekend), Trump International (\$675, \$675), Four Seasons (\$625, \$555) and the Carlyle Hotel (\$663, \$663).

The Ritz Carlton Battery Park has shown the ability to attract a diverse target market. According to the property manager, roughly half of the demand comes from leisure/tourist traffic. The property offers excellent amenities and services in-line with Ritz brand. The Ritz is the destination building at the tip of Battery Park, with unrivalled views of NY Harbor from the 14th floor bar and the majority of guestrooms. The property does offer 12,000 square feet of meeting space, a business center and a small fitness area. The three-room spa at the Ritz Battery Park is a strong amenity, especially for the tourist traffic, although this spa is smaller, more affordable, and not as prestigious a brand as the La Prairie spa at the Ritz Carlton Central Park.

In order to achieve top-of-the-market room rates, luxury hotels must target the top niche of the market. This means that these hotels must offer more than a guest room, but also must provide a true experience. Luxury hotels must therefore offer an exceptional level of service and strong amenities. This includes luxurious and modern rooms, quality

meeting and event space, a restaurant and lobby bar, a fitness center, spa services (ranging from massages to relationships with nearby full-service spas and salons and actual spas on site) and concierge and business services. Location in the “heart of things” is also a critical selling point, especially for the larger Midtown luxury hotels. Their location, amenities and services allow luxury hotels market equally well to the top end of business and leisure markets.

### Full and Limited-Service Hotels

Full-service and limited-service hotels offer a price point below the luxury hotels, although room rates are often still quite strong. Even so, these types of hotels tend to target more convenience and price-oriented customers, in particular business travelers, than luxury hotels. Full-service hotels (referred to as first-class hotels in the data analysis above) offer more amenities and services than limited-service hotels.

There are several examples of full-service hotels in the downtown area, in particular the Millennium Hilton and Marriott New York Financial Center. The Millennium Hilton offers room rates ranging from \$2999 to \$399 on the weekday and \$199 to \$299 on the weekend. The Marriott is priced somewhat higher, from \$329 to \$369 on the weekday and \$214 to \$369 on the weekend. The Millennium has enjoyed strong occupancy, with an estimated 92% occupancy rate over the past year. The weekday traffic is geared almost wholly (90%) to business travel, with the weekend demand almost wholly driven by tourist traffic. These hotels offer smaller fitness and spa amenities than is typically found in luxury hotels.

The Millennium Hilton and Marriott New York Financial Center also offer a small amount of meeting space – 3,500 square feet in Millennium and 10,500 square feet in the Marriott. The Midtown submarket has several full-service hotels with the larger amounts of meeting spaces. For example, the New York Hilton Towers has 2,000 guestrooms and 151,000 square feet of space available for corporate and private rental. The Millennium Broadway Hotel, the only IACC-accredited conference center in Manhattan, offers 110,000 square feet of meeting space and only 763 rooms. The Sheraton Hotel, with 1,700 guestrooms, has 55,000 square feet of conference and meeting rooms. All three have small fitness facilities but no in-hotel spa rooms, and are priced midweek from \$212 to \$304. The demand for the meeting space in these hotels, in contrast to strictly business-oriented conference center hotels, is more evenly split between social events/tour groups and business conferences.

The Waldorf Astoria is another large conference center hotel, and it also markets its rooms and meeting space evenly to business and leisure travel market with its meeting space. The hotel is widely known as the only hotel in Manhattan appropriate for hosting non-corporate large events on the basis of design and layout of the public space. Its ballrooms handle large daytime meetings and private evening galas and receptions unlike the corporate environments of the other hotels. The Waldorf has 1,425 rooms and 60,000 square feet of meeting space. It also has a small fitness center and a 3,000 square foot spa with four treatment rooms and rack rates just above \$300.

### Limited Service Hotels

Limited-service hotels offer few amenities, and instead target consumers more interested in a convenient location and a relatively more affordable pricing. In the downtown area, examples of limited-service hotels include the large Embassy Suites (463 rooms) and Holiday Inn Wall Street (227) hotels, as well as the smaller independent Cosmopolitan (103) and Manhattan Seaport Suites (56) hotels. Standard rack rates for these hotels fall in the \$219 to \$239 range, however the Cosmopolitan is much more affordable and the Embassy Suites is priced at \$399 (due to the larger rooms that allow for doubling up, as well as excellent views).

Of the five limited-service hotels in Manhattan surveyed in this analysis, only the Embassy Suites provides any meeting space. It has 13,000 square feet of meeting space, including five theaters and a host of small meeting rooms that are regularly booked for at least one meeting per day. None of the limited-service hotels we surveyed in the downtown area have spa or fitness facilities, but they all publicize nearby clubs available for use. Many limited-service hotels have more trouble attracting a leisure weekend market, although significant weekend discounting does allow these hotels to attract a more price-sensitive visitor. The Embassy Suites does not discount prices on weekends but believes that its free buffet breakfasts is an additional incentive for the leisure market that would otherwise pay \$60 at a midtown hotel for the same. Rooms are large in the Embassy Suites, once again allowing for room rate sharing, and the views are outstanding, which further helps attract leisure visitors.

## Boutique Hotels

Boutique hotels are typically smaller hotels (although hotels such as the Hudson can be quite large) offering a creative, design-intensive orientation for consumers that want a distinctive hotel experience. Much of the value of the boutique hotel experience is derived from the unusual and lively public spaces in the lobby, restaurants and bars rather than luxurious rooms. The W Hotels and Ian Schrager hotels refer to their lobbies as Living Rooms and furnish them with coffee table books, board games and wireless Internet connections. Boutique hotels are typically priced below luxury hotels, but are priced competitively with upscale full-service hotels. Yet, these hotels are often able to better target the leisure market, and thus often are able to maintain, or even increase, room rates on the weekends.

Boutique hotels are a destination attraction and are certainly a growth segment in the Manhattan hotel market. Currently, only one boutique hotel is located in the downtown area, the Wall Street Inn, although seven boutique hotels are located south of 14th Street, including the newest and trendiest one, the Gansevoort Hotel in the Meatpacking District. The 46-room Wall Street Inn in the financial district is a recently renovated hotel in the traditional style and with no amenities. Asking room rates average \$249 on weekdays, when business travelers constitute 95% of the clients, and \$199 on the weekends.

The Wall Street does not generally compete with the boutique hotel concepts that have become destinations in soon-to-be discovered neighborhoods such as the Tribeca Grand and

the Gansevoort Hotel in the meatpacking district. Asking room rates for the Tribeca/SoHo/Village boutique hotels range from \$309 to \$599 on the weekday and weekend. These, along with the new Gansevoort Hotel, are the highest positioned boutique hotel properties in Manhattan. The W Hotels and the SoHo and Tribeca Grands, like the Wall Street Inn, target a business market, albeit a younger one in general, and given their destination qualities are more adept at attracting a high-end leisure market.

Amenities in high-end boutique hotels are secondary to the design concept and are provided according to the hotel's space and desired market positioning. Tradeoffs between meeting space, public lounges, restaurants, fitness centers and spas have allowed for few standard amenities across this segment. In particular, meeting space is typically very flexible for both social and corporate events.

- The SoHo Grand, seeking to address the needs of its majority business clientele better, recently expired the lease of one of its trendy restaurants to convert it to meeting space. The 393-room hotel now has 3,900 square feet of meeting space and a growing base of corporate clients based in midtown and downtown.
- Its sister hotel, the Tribeca Grand, which caters to the film industry and has a large theater for screenings, converts its open lounges and public space into meeting rooms and reception areas on a nightly basis.
- The new Gansevoort hotel in the meatpacking district is another boutique hotel that is bridging the corporate and social clientele with flexible event space and bars that are very

exclusive.

- The 1,000-room Hudson Hotel – a rather unique large hotel that embraces the boutique concept -- has the most meeting space of all boutique hotels, with 18,000 square feet and an exclusive caterer that handles regular corporate and social events.
- The W Hotels are Starwood Hotel's boutique hotel brand that is targeted to a young, professional clientele. The Union Square and Lexington Avenue W Hotels have 7,000 and 8,800 square feet of meeting space, respectively.

Spas are a recent addition to the boutique hotel amenity offering. Typically left to the luxury hotels in midtown, boutique hotels are beginning to find and acquire the space to add fitness centers, treatment rooms and wellness centers to their offering. The Hudson Hotel will soon introduce a three-story, 20,000 square foot spa adjacent to the hotel, and the W Hotel at Lexington is currently building a Bliss Spa where in its former 10,000 square foot Away spa space. At the furthest end of the spectrum, the 208-room DreamNY hotel, currently under construction, will be an urban wellness retreat with a Deepak Chopra-branded spa and Ayurvedic healing center, as well as modern restaurants and lounges designed by David LaChapelle and David Rockwell.

Boutique hotels are a growth segment in this market, although the total rooms in this segment are not very large. Seven boutique hotels are located below 20th street, while only one of them is located in the downtown financial district neighborhood. Combined, they supply a little more than 1,000 rooms to Manhattan. Two new boutique

hotels will appear in downtown by 2005, the 83-room Downtown and the 340-room Ian Schrager Hudson Center Hotel. These hotels, and the Ritz Battery Park, whose majority of rooms have full Harbor views, are contributing to the waterfront revitalization that began with the creation of Battery Park City and has most recently been captured in the Hudson River Park redevelopment.

### **Demand Analysis**

Exhibit IV-13 provides our statistical analysis of the demand and supply conditions in the Lower Manhattan submarket. The model projects demand and supply conditions for the Manhattan and Lower Manhattan markets from 2004 to 2010, and estimates the excess hotel room demand that will be captured by particular hotel types, and then by Governors Island.

We have assumed that Manhattan hotel demand will experience a relatively sharp increase over the next few years as it recovers from the recent period of stagnation, with more historically appropriate growth rates (2.5%) in the years following. From 1998 to 2003, Lower Manhattan constituted a growing percentage of the proven Manhattan room night demand – from 3.4% to 5%. We project that this growth will continue, and that the Lower Manhattan market will constitute as much as 11.5% of the total Manhattan market by 2010, primarily by capturing a very strong share (25% to 50%) of the net new hotel room night demand.

Based upon current estimates, we expect the Lower Manhattan market to grow by 1,970 hotel rooms by 2010, not including any new hotel rooms at a World Trade Center Hotel. This represents a more than

60% increase in the hotel room supply in Lower Manhattan; this submarket has 43% of the planned hotel rooms in all of Manhattan. Yet, despite this increase in hotel rooms, we expect demand to outpace supply.

We have assumed that a 75% occupancy rate across the Lower Manhattan submarket is an appropriate demand-supply balance in this market (in other markets, market-wide occupancy rates of 65% are considered healthy). Where demand is in excess of 75% of supply, unmet demand is expected to drive new hotel development. By 2010, we expect that over 4,400 net new hotel rooms, above and beyond the planned development, could be supported in Lower Manhattan.

The luxury, five-star hotel market should capture 15% of net new Lower Manhattan demand from 2004 to 2010, after capturing a similar share of net new hotel supply in Manhattan from 1998 to 2003. The luxury hotel market will continue to represent a market niche. We expect Governors Island to initially be able to capture 10% of the available luxury hotel demand, with the capture rate increasing to 20% by 2010 as the Island develops a critical mass of complimentary land uses (including extraordinary public spaces). According to our estimates, by 2010 only 132 rooms will be supported on Governors Island. The Island will be very attractive to a share of the luxury market that wants to experience the unique environment of Governors Island. However, 132 rooms generally is not a large enough room count to justify construction of a new luxury hotel. The Island will likely find it difficult to attract a larger share of the luxury hotel market, as these consumers will tend to want to locate in an area with a more critical

mass of amenities and services and may balk at the inconveniences (even if minor) of transporting to and from the Island. The commitment of an operator with an established brand could increase and/or accelerate demand, although in general we believe that the Island will be a difficult site for luxury hotel operators given the market challenges.

We project that the full-service hotel market will capture 30% of Lower Manhattan net new demand from 2004 to 2010, a similar capture of the growth in supply from 1998 to 2003. Governors Island will only capture 5% to 10% of the net new Lower Manhattan demand. The full-service hotel segment is more driven by convenience and price than by the uniqueness or quality of the experience of the hotel stay, and therefore the transportation issues and lack of critical mass of services on the Island will be barrier to attracting this market demand. The business traveler is especially important to demand for this hotel type, and we believe that the Island is more attractive to leisure visitors seeking an experience rather than convenience and access. Given these market conditions, by 2010 we estimate that the Island will only support 132 full-service hotel rooms; certainly, this is not a large enough inventory to support the construction of a new full-service hotel.

Limited-service hotel demand will confront similar market challenges as full-service hotels, but even more so given that limited-service hotel consumers will be even more driven by convenience and price. We are assuming that it will be very difficult to offer a lower-priced hotel alternative on the Island given the expected costs of rehabilitation, redevelopment or new development on the Island. Thus, a limited-service hotel would likely need to be priced well

above existing competitive limited-service hotels, without providing the convenience and access the market desires. Although we did not provide the calculations for limited-service demand in our demand model, we project that approximately 25% of net new Lower Manhattan demand from 2004 to 2010 will be in this market segment. Given the market constraints, Governors Island will only be able to capture a very small share of this demand.

We project that boutique hotels will capture 30% of the Lower Manhattan demand. Currently, boutique hotels represent 12.5% of the Manhattan supply, but it has been a growth segment, and from 1998 to 2003 represented 33% of net new Manhattan supply. We believe that Governors Island can capture 10% to 20% of Lower Manhattan boutique hotel demand, which will allow the Island to capture approximately 127 rooms by 2007 and 264 by 2010. A typical boutique hotel is 75 to 125 rooms, so two boutique hotels can be supported on the Island over the next six years. Governors Island will be very attractive to consumers who want a unique, boutique hotel experience. An established concept or brand for the hotel would make the chances for initial success much more likely, although the unique attributes and beauty of the Island will be the real draw.

## V. Spa

### Summary

The spa industry has grown into a multi-billion dollar business nationally since the late 1990's. In 2001, spas in the US grossed \$10.7 billion, a 114% increase since 1999. The number of spa visits grew 71% from 1999 to 2001, when almost 156 million visits were recorded.

An analysis of the competitive marketplace confirms that demand is strong for a variety of spa types in the New York area. A destination and wellness spa sells strictly programmed, extended stay packages focused around issues of health and wellness. Destination spas, such as Canyon Ranch in Lenox, Massachusetts, are proven successes, and draw significantly from the New York market. The market opportunity for this type of spa at Governors Island is somewhat limited, as it targets a relatively small niche of consumers.

Resort and day spas tend to focus more on pampering than on strict programming, and these types of spas can attract a broader market. Resort spas provide overnight stays, and therefore cater more to weekend getaways where guests are utilizing the spa as well enjoying other activities in and outside the resort. Day spas typically offer treatments over the course of one or two hours. Spas are also a proven amenity in luxury and upscale boutique hotels, and are now being used as a centerpiece for marketing to the top niche of affluent leisure visitors

A high-end spa developed in conjunction with conference center and boutique hotel rooms

represents the strongest opportunity on Governors Island. The concept of the spa fits perfectly into the overall theme of the Island as an urban getaway. The spa will be able to market itself as a resort spa, not only because of the spa facilities, but also because of the natural and developed amenities on the entirety of the Island. The conference hotel and boutique hotel(s) can sell packages to the spa, or vice versa, which will allow both the spa and hotels to reach a broader market audience than they would separately.

We recommend that the spa on Governors Island have between 8 and 12 treatment rooms, with an average price of \$130 to \$150 per hour. We project that approximately 80% of the demand for spa treatments will be derived from hotel guests on the Island, with a higher percentage of day spa traffic on the weekday. Typical hotel or resort spas in the New York region attract 30% to 50% of total demand from the local market. However, given the transportation constraints associated with the Island, we do expect that Governors Island will have a harder time attracting a larger share of local, day spa consumers, and will need to rely more on visitors already staying on the Island.

The spa will see a lull in demand during winter months, as harsh weather limits the desirability of the Island. The spa could be at full capacity on the weekend, and between 46% and 56% occupied during the weekday. A 12-room spa could achieve an average annual occupancy of 66%, but should enjoy occupancy rates above 70% for all but the winter months.

## Spa Definitions

The concept of a spa is not monolithic, and spas vary significantly by concept. The different concepts, or spa types, are described below (and in Exhibit V-2):

- **Medical spas:** The newest type of spa to emerge, these spas provide an out-of-hospital medical environment for clients that want to pursue plastic surgery and other medical enhancements. Licensed doctors, aestheticians and massage therapists are on staff at these spas to create a pampering and healing environment.
- **Destination spas:** These spas often focus on regimented wellness concepts. Typical stays are one-week or more, and the spa offers programmatic elements for diet, exercise, or other health-intensive programs. Meals, hotel and activities are usually included in a package. The more strictly regimented activities are usually combined with pampering body and facial treatments. The environments of destination spas range from simple outdoor retreat (Golden Door in Escondido California) to high-end, sprawling campuses (Canyon Ranch in Lenox, Mass.).
- **Resort spas:** These spas are vacation getaways that offer luxury hotel accommodations and a wide range of activities, including high-end restaurants, spa treatments, fitness activities and other amenities, such as golf. Resort spas can be weekend retreats within a few hours drive from a major urban market or larger-scale resorts, such as the original resort spas located in California, Colorado and Arizona. Resort spas are typically larger than day or hotel spas,

and typical visitor stays range from two to four days.

- **Hotel Spas:** Many high-end hotels are now offering in-house spa services. These services range from a house-call service or a partnership with a nearby spa to an in-hotel spa facility. Typically, demand from hotel guests is not consistent enough to allow hotels to operate spas completely dedicated for hotel use, and therefore larger hotel spas also rely on outside day spa demand. Hotel spas can vary greatly in size, with hotel spas we have surveyed ranging from 2 to 14 treatment rooms and 1,000 to 35,000 square feet.
- **Day Spas:** The most common spa type, day spas, offer nail, massage and facial services to a transient market. In 2001, day spas accounted for 75% of the spas in the US and 68% of the visits to spas. Unattached to a hotel, day spas rely on local traffic (or partnering agreements with nearby hotels) and product sales, which can account for as much as 65% of a day spa's revenues.

## Market Overview

The spa industry has grown to a multi-billion dollar business nationally since the late 1990's. In 2001, the latest year for which we have total expenditure data, spas in the US grossed \$10.7 billion, a 114% increase since 1999. The number of spa visits grew 71% from 1999 to 2001, when almost 156 million visits were recorded.

Demographically, the average spa consumer has a household income of \$72,000 and is 41 years old, although 42% of spa-goers are younger than 35 years. Approximately 55% of spa goers are college-

educated, and 82% consider their health good or excellent. Across the US population, a survey by the International Spa Association estimates that 26% of women and 16% of men are likely to visit a spa within one year; spa use data suggests that approximately 71% of current spa-goers are women.

The spa is a leisure activity, and not surprisingly, occupancy at all kinds of spas is highest on weekends. Much as many hotels offer discounts on weekends to attract the leisure market, spas often offer lower rates and package deals during the week. According to spa directors, spas can sustain their business with occupancy as low as 40% during the weekdays, as long as weekend volume approaches 100% occupancy (with the help of flexible worker hours).

Still, getting that 40% can sometimes be a challenge, especially at resort spas, and thus discounting and package deals are common. The Spa at Norwich Inn offers an 11% discount on its midweek pricing and the Emerson Inn offers certain packages for Monday through Thursday use only. Larger vacation resorts try to bridge the gap between midweek and weekend occupancy rates by targeting vacationing retirees or seasonal golf and ski visitors for multi-day vacations. Day spas, which offer treatments that can last from one-half hour to a whole day and draw from a local market, are less susceptible to weekday lulls, although the preferred day spa time slots continue to be on the weekend.

Day spas, resort spas and hotel spas all rely to some degree on local, day spa traffic in order to maintain occupancies. Day traffic typically consists of discerning clients make frequent visits. Quality of

service causes more repeat visitors than does brand or location, according to leisure industry analysts, although brand can often become synonymous with quality of service.

Operators at several resort spas we surveyed in the New York region have indicated that only 35% of overnight guests use the spa, and that often more than 50% of spa demand is from local sources. This is especially true during the weekday, when overnight visits are more limited. Full-service hotel spas certainly also rely on outside traffic; only 15% of hotel guests, on average, will use the spa facilities in a luxury or boutique hotel. In particular, the business traveler that drives hotel demand does not provide a consistent demand for the spa facilities given issues of timing (both lack of time for the traveler and the misfit between the availability of spa rooms and the typical businessperson schedule) and the appropriateness of the service as a business expense. Although meeting planners are tending to book corporate retreats that incorporate spa activities more than in the past, it is still a relatively small share of overall business hotel stays. Still, hotels with spas are active with deals and packaging in order to sell the rooms and the spa. For example, the Four Seasons' Urban Spa package includes accommodations and two treatments for \$895 versus the room's regular price of \$725, saving the guest more than \$40 on treatment costs.

A well-defined or unique spa experience will draw clients from a wider market than a standard spa of the same type. A general finding from a survey of spa-goers is that spa selection is made on the basis of 1) quality of service and products, 2) price and 3) uniqueness or attractiveness of location -- in that

order. However, local day spa-goers will still heavily weigh the convenience of a location, especially if traveling for just a single treatment or service. The local market will travel further for two or more treatments or, in special situations, if the concept and/or level of service are very well differentiated from more convenient options.

Resort spas tend to attract from a regional market, and larger or well-known resorts with access to an airport do draw from a national market. Very high-end resort spas compete with spas as far as Asia and Central America. A new type of vacation resort spa is emerging that offers a holistic experience in packages that include meals, luxury accommodations, fitness activities, spa treatments and classes such as meditation and yoga. This holistic spa concept combines the structure of the destination spa with the more relaxed services of a resort spa. It is a trend that is becoming widely accepted in "exotic" locations as Mandarin Oriental, Hilton, Amman and other leading resort developers introduce them in beach and island settings.

The "wellness" concept incorporates a new range of services and products that target very specific health, relaxation, fitness, beauty and spiritual interests. The destination wellness concept certainly has found a devoted market niche, but the strictly regimented programs of many wellness spas do not generally appeal to the broader marketplace. It is a difficult market to expand. Destination spas have also found that branding is difficult, in particular due to the difficulties of establishing a consistent level of quality and service across multiple properties. The most popular orientation appear to be those day or resort spas that offer pampering services, either by themselves for a few

hours on one day or as part of a larger amenity package for weekend getaways.

Canyon Ranch, a very well known brand of destination spas, has responded to the market and operational challenges associated with expansion by following a strategy that will create wellness centers in conjunction with residential developments. Following its last development of a luxury resort spa in the Queen Mary 2 cruise ship, Canyon Ranch is pursuing the wellness center as a real estate amenity rather than as a health destination, with its first planned community in Miami.

Overall, to find market support in an increasingly competitive environment, spa operators seek to differentiate themselves from their competition with regards to several factors: higher quality treatment methods; unique concepts in the form of interior design and programming; or striking settings.

### **Competitive Supply**

We surveyed a number of resorts in the New York region, including destination and resort spas, as well as New York City hotel spas and day spas. The location and key information for these spas is provided in Exhibits V-3 through V-5, with more detailed case studies of selected spas in Exhibit V-6.

### **Destination and Resort Spas**

We identified seven relevant and potentially competitive destination and resort spas in the New York region (three hour driving distance from New York City): Emerson Inn in Woodstock, NY;

The Doral Forrestal in Princeton, NJ; The Spa at Norwich Inn in Norwich, CT; New Age Health Spa in Neversink, NY; Copperhood Inn in Shandaken, NY; Mirbeau Inn in Skaneateles, NY; and, Canyon Ranch in Lenox, Massachusetts. The highlights of the destination and resort spa competitive market are discussed below.

Canyon Ranch, in Lenox, Massachusetts, is a well-known destination spa with a heavily programmed orientation and a minimum stay of four days. This spa offers 126 guest rooms, 100,000 square feet of spa, fitness and wellness facilities, all surrounded by 120 acres in an idyllic setting. Average daily rates for the entire year range from \$590 to \$710 (an average of \$650), although demand, and therefore average rates, are quite seasonal. The average summer rate is \$820, with fall and spring average daily rates at \$615, and average winter rates at \$555. The daily rate includes accommodations, three gourmet meals, access to fitness classes and facilities, a personal health assessment and a \$300 to \$500 credit towards spa services. The primary target market is individuals or small groups of friends/relatives, although Canyon Ranch also can service larger corporate and social groups of between 10 and 60 people.

The Emerson Inn is a luxury resort with only 24 guest rooms and eight treatment rooms in its 15,000 square foot spa. The Inn is located in historic Woodstock, New York, with access to hiking trails in the Catskills and small-town New England activities. It is designed with Old World themes that offer African, Persian, West Indies Colonial and Victorian guest rooms in a Ralph Waldo Emerson-inspired 19th century inn. The restaurants and lounges focus on highest quality wine and gourmet meals.

Non-suite hotel rates, including breakfast, are \$539 for weekday pricing and \$724 for weekend prices, jumping to over \$1,000 for the limited number of suites. A one-hour massage costs \$100, although package deals reduce this rate to approximately \$77 per hour. On occasion, the spa will do group/conference business, especially social events such as weddings in the summer, and they do maintain a relationship with the Longyear Conference Center. However, the small Inn is largely dedicated to the weekend getaway market from New York, just two hours away. Local day traffic does constitute more than 50% of the overall spa demand.

The Doral Forrestal Inn in Princeton, NJ is a resort conference center that primarily serves executive business conferences and meetings; however, the Inn also attracts weekend travelers by marketing the spa and outdoor recreation activities. The Inn has 290 guest rooms, 35,000 square feet of business-oriented meeting space and a 15,000 square foot spa, which is expanding from six to nine treatment rooms based on high levels of demand. Conference attendees also provide a decent stream of weekday demand for the spa. Weekend demand is attracted through room and spa packages, where the cost of the room includes two spa treatments per day (in addition to three gourmet meals). Much like with the Emerson Inn, local spa traffic at the Inn constitutes more than 50% of the spa traffic. Spa prices at the Doral are \$70 per hour and rooms typically cost \$285 during the week.

### **Full-Service Hotel Spas**

Luxury and boutique hotels are more commonly providing spa services as an additional amenity. Of the 29 mid- to high-end hotels that we surveyed

in the New York competitive market, we found the following:

- Six hotels have a full-service, luxury spa, with five to fourteen treatment rooms, that serves both the hotel and local day spa traffic in order to sustain its comparably large operations.
- Seven hotels have one to four treatment rooms in a small, dedicated spa facility that serves more as an amenity to the hotel's full-service offering than as a revenue center. Small spas typically adjoin a fitness room and range from high-end design to health club atmosphere.
- Sixteen hotels did not have a spa or fitness center, but most had formal or informal relationships with nearby spas.

Hotel spas in New York City are reaching very high levels of design and pricing in their attempts to attract high-margin niche markets. The Mandarin Oriental hotel has beautiful 35th floor panoramic views from its Japanese-designed treatment rooms and tea lounges in the new Time Warner building at the foot of Central Park. Massages cost \$280 per hour, and day packages provide treatments and lunch for an equivalent of \$160 to \$220 per hour. The spa could support four more treatment rooms above its existing eight rooms, yet keeps supply restricted to retain an environment of exclusivity. The Mandarin Oriental hotel has 256 rooms and a rack rate of \$659 for standard rooms. Yet, the majority of the spa clientele are local visitors, many of whom come for an \$885 day package, which includes use of the pool and fitness facilities.

The Peninsula Hotel's 35,000 square foot fitness center and spa is a long-time success story in New

York hotels. It boasts a large though undisclosed membership of midtown professionals and Upper East and West side residents, which supports the majority of its business. The spa's 14 treatment rooms are booked four weeks in advance typically. Rack rates for the hotel's 239 rooms are \$650, comparable to the Mandarin, but an hour massage is only \$150.

Other luxury hotels, such as the Four Seasons, Plaza Hotel, Ritz Carlton Battery Park and Trump International, have in-hotel spas ranging in size from 5,000 to 8,000 square feet. Treatments range in price from \$120 to \$175 per hour. Between 50% and 80% of the demand for these spas is driven by hotel traffic, with the exception of the Trump International, whose spa is dedicated to guests.

Boutique hotels, the fastest growing hotel segment in Manhattan, are also beginning to focus efforts on the spa business, which they traditionally left to the domain of luxury hotels. In early 2004, Starwood Hotels bought the highly successful London-based Bliss day spa and product line, and it now will introduce Bliss Spas in all of its W Hotels, beginning with the W Hotel at Lexington Avenue, replacing the hotel's less glamorous 10,000 square foot Away spa. Pricing is not yet available for these treatments, Bliss treatments in their two Manhattan day spas cost \$100 for an hour massage. The Bliss brand is targeted to a young, urban market that has proven its willingness to spend on both treatments and products, more than 60% of its revenues. Bliss products were formerly offered exclusively at the boutique SoHo Grand and Tribeca Grand Hotels in downtown Manhattan.

Another boutique hotel that is entering the spa and wellness retreat business is Ian Schrager's Hudson Hotel. The hotel has announced plans to build a three-story wellness center adjacent to the 1,000-room hotel. The center will offer yoga classes, basketball courts, a full-service spa, swimming pool and other relaxation amenities. The hotel is a high-end destination, whose special weekend packages often include guaranteed admission to one of its three bars.

Leading boutique hotels have not offered spas or fitness centers in the past and little is known of the traffic that emanates from the hotel versus local daytime traffic. In the past, trendy boutique hotels were very successful at creating destination restaurants and lounges that became lasting destinations for New Yorkers as well as hotel visitors. Many boutique hotel developers are betting that the same trend will occur with day spa traffic, in order to supplement hotel-driven demand.

### **The Role of Brands**

The spa industry is a fragmented and locally driven one. Some brands have emerged over the years as leaders in a certain segment of the spa business, however, due to the service nature of the business, few have achieved true economies of scale or derived a business expansion model that could be replicated. Customers certainly show brand loyalty, but often that loyalty is to a particular location rather than true brand. Spa operators have indicated that branding of multiple properties is difficult, in great part because of the difficulties associated with maintaining a consistent level of quality across multiple properties. This is especially the case with destination and resort spas.

The Golden Door destination spa has worked hard to protect its brand despite its acquisition by Wyndham Hotels. The original spa, in Escondido California, is known as a sanctuary for wellness, beauty and health during a \$6,500 all-inclusive week. The spa's 39 rooms bring in \$11.7 million in revenues annually, yet the concept and brand has been difficult to support in other environments. For example, the Telluride Peaks Golden Door spa proved to be too seasonal to retain high-quality service providers, and the Wyndham Anatole hotel in Dallas could offer only sporadic demand from the conference-center market, forcing the hotel company to resist naming the spa a Golden Door spa.

Day spa brands, such as Bliss or Elizabeth Arden, have been somewhat more successful establishing a brand identity. Yet, attracting a brand is not a requirement for success, or a guarantee either. Brand identity may get initial traffic in the door, but return spa goers – the critical market segment to serve – will most likely choose the spa that provides the highest level of quality and service, regardless of brand.

### **Market Analysis and Demand**

In order to determine the market support, we completed two statistically driven demand models. Exhibit V-7 calculates the depth of demand for day spa traffic. Exhibit V-8 incorporates demand from other sources, in particular conference center and boutique hotel rooms, and calculates the supportable number of treatment rooms and expected occupancy by time of the year.

Day spa traffic to Governors Island will draw

from the local residential markets of Manhattan and Brooklyn, as well as a certain percentage of additional demand— such as persons living outside of the defined market areas and local tourists/visitors. Assuming a high-end spa concept that is competitive with spas such as the Peninsula, Bliss and Hudson Hotel spas, we defined our primary market areas as all of Midtown and Lower Manhattan and the Western districts of Brooklyn (as defined by community districts).

Based upon ISPA surveys, we have estimated that 11% of women and 7% of men will visit a day spa. The key breakdown of spa visitors is between those visitors that will visit a spa just once a year, and those that will visit multiple times – we have estimated multiple visitors will visit an average of six times per year, based upon interviews with industry experts. We have estimated that 30% of women will be frequent spa visitors, and only 10% of men. We have applied these factors to the population in households with a household income of \$75,000 and over for all the selected market areas.

Residents of Manhattan’s Lower Manhattan – Manhattan Community Districts (CDs) 1 through 3 – and of the nearest Brooklyn neighborhoods – Brooklyn CDs 2 and 6 -- will have a higher propensity to go to a day spa on Governors Island. Yet, the Lower Manhattan market will only contribute 18% of total demand potential, with an additional 10.5% from the closest Brooklyn neighborhoods. This is because the relatively low populations (either in total, or the population that meets the income requirements) in these areas relative to other parts of Manhattan. For example, despite lower capture rates in these areas, Manhattan CDs 4 through 8 will constitute approximately 27% of the demand

potential at Governors Island.

We also have estimated that 17% of day spa demand will originate from outside of the defined market areas – either persons living outside these areas or visitors to New York. For all sources of demand, Governors Island will capture a higher percentage of one-time visitors versus frequent visitors. The assumption is that frequent visitors will seek a spa that is more convenient, and thus transportation constraints to Governors Island will present a stronger market barrier. One-time visitors are more likely to travel to Governors Island for the unique experience or out of curiosity.

In total, we approximate that 7,200 day spa visitors a year would potentially visit a spa at Governors Island. Nearly 69% of this demand will be from one-time spa visitors. In Exhibit V-8, this day spa demand was distributed by season, based upon RCLCo judgment that was informed by interviews with industry experts. We also factored in demand from conference center boutique hotel demand. Based upon our competitive market analysis, we have assumed that 10% of conference center and 20% of boutique hotel demand on the weekday will demand spa treatment. On the weekend, these propensities increase to 35% for conference center guests and 25% of boutique hotel guests. Weekend guests are more likely to use the spa because these guests are more likely to be attracted by the spa as part of an overall amenity package (including the natural environment and historic structures on the Island). Weekend guests are also more likely to purchase package deals that include (or provide discounts for) spa treatment.

Assuming a conference center hotel and two 100-room boutique hotels, we project that as many as 12 treatment rooms can be supported on the Island, although a smaller 8-room spa would enjoy strong occupancies and therefore be a less risky development proposition. For example, an 8-room spa would enjoy an annual occupancy of 73%, and occupancy will drop to 66% for a 12-room spa. We expect that the spa will be completely full on the weekend throughout much of the year, with the exception being the winter during which we expect harsher weather conditions to limit overall demand.

For the 12-room spa option, approximately 19% of demand will originate from local (or visitors to other parts of New York) day spa demand. The percent of day spa traffic will be higher during the weekday (26%) versus the weekend (15%). This ratio of on-Island hotel traffic to day spa traffic is at the upper end of the competitive market; typical spas attract 30% to 50% of total demand from the local market. However, given the transportation constraints associated with the Island, we do expect that Governors Island will have a harder time attracting a larger share of local, day spa consumers, and will need to rely more on visitors already staying on the Island.

## VI. Parks and Recreation

### Summary

A park on Governors Island would serve the needs of its neighboring community districts in Manhattan that severely lack active and passive recreational space by national, and even citywide, standards. Park space and recreational facilities are necessary urban elements that are rarely oversupplied. Beginning in 1857, when Central Park was commissioned to Frederick Law Olmsted and Calvert Vaux, parks and playgrounds started to work their way into the public agenda. Cities across America recognized the restorative capacities of open space for people living in growing cities, as well as the need for the public to have widespread and active use of these lands. Cities created public vehicles for the design and maintenance of parks and began to establish standards by which urban planners could envision the future development of cities.

There is very strong opportunity to provide park space and recreational facilities on Governors Island. Our analyses have found that significant pent-up demand and trip potential does exist from within in the local market area – including both residents and visitors. The park space should include large tracts of passive open space (for picnics, sunbathing and events), extraordinary landscaping and walking and biking trails.

We have also found significant market depth for a variety of recreational facilities, potentially including baseball, softball and soccer fields; tennis courts; basketball courts; golf driving range; swimming pools; and an ice hockey rink. There is significant

pent-up demand for league and instructional facilities throughout New York City. The market success of the 1.7 million square foot Chelsea Piers recreational complex is particularly relevant given its nearby location, and similar transportation and access constraints. This complex attracts over 4 million visitors a year, and many of the facilities, while technically open to the public for a significant fee, are often booked well in advance by leagues and instructional activities. Chelsea Piers attracts approximately 20% of its traffic from outside of Manhattan, despite the fact that it is not very accessible.

There is a proposal to expand operations onto Pier 57, in particular cultural space for galleries and dance recitals, a 30,000 square-foot swim center, and a 100,000 square-foot tennis center, all of which are significant voids in the current marketplace. The Pier 57 proposal would certainly work as well on Governors Island, although we believe Governors Island could also support a larger facility due to extensive pent-up demand in the marketplace.

### Parks and Facilities Assessment in Manhattan and Brooklyn

Though fixed ratios were widely considered unfeasible by city leaders and planners, the National Park Service established benchmark guidelines in 1943 that encouraged cities of more than one million people to provide ten acres per 3,000 people or 300 people to an acre. New York City shares 28,700 acres of park space in 1,700 parks among eight million residents, a ratio of 279 people per park acre. Compared to Minneapolis, the leading city in terms of acreage, design and usability of an extensive network of park systems, pathways,

beaches, recreation centers and playgrounds, New York's ratios pale. In Minneapolis in 2000, there were 60 people per park acre.

Data on the existing park and recreational facilities in Manhattan and Brooklyn are provided in Exhibits VI-1 through VI-6. Approximately 18% of Manhattan's total acreage is park space, compared to 9% in Brooklyn. These two boroughs have the highest ratio of residents to parkland of all boroughs, at 574 residents per acre for Manhattan and 547 residents per acre for Brooklyn. By comparison, Queens has 309 residents per park acre, the Bronx has 192 and Staten Island has 61.

The Citywide park system contains 14 miles of beach, 950 playgrounds, 800 athletic fields, 563 tennis courts, 63 indoor and outdoor swimming pools, 13 golf courses and six ice rinks. In Manhattan, there are 133 basketball courts, 104 baseball fields, 101 tennis courts and 16 recreation centers. When national benchmarks set forth by the National Parks and Recreation Association (NPR) are applied to New York, there is significant unmet demand for recreational facilities. Central Park, Randall's Island, Fort Washington Park and Riverside Park offer the largest concentrations of recreational amenities. Central Park is in Midtown Manhattan, and these other large parks are on the northern end of Manhattan in Community Districts 9, 11 and 12.

In Lower Manhattan, both active and passive park space is scarce. The area's 292,000 residents have a very high ratio of population to park acre of 1,738. Community District 1 does not have any recreational centers or facilities, although it does have the second largest park in the area, the 23-acre Battery

Park. Community District 2 has one baseball field in James J Walker Park and a handful of basketball courts. Community District 3's East River Park offers the most recreational amenities, and size, of any parks in the three districts. It provides eith baseball fields, 12 tennis courts and soccer, football and cricket fields, as well as a waterfront promenade in its 58 acres.

Brooklyn residents along the waterfront have a great deal more passive space per person than their Lower Manhattan neighbors. The three Community Districts in Brooklyn that border the waterfront nearest to Governors Island, Districts 2, 6 and 7, have a total of 725 park acres, 526 of which are in Prospect Park. With 323,000 residents in these Districts, this results in a ratio of 445 residents per park acre. The beautifully designed Prospect Park was considered by Olmsted and Vaux to be the designers' superior version of Central Park, and provides the same range of activities available in Central Park: soccer, tennis, football, volleyball, horseback riding, running trials, baseball and skating. After Prospect Park, Fort Greene (30 acres) in Community District 2 and Sunset Park in Community District 7 are the largest. Once the Brooklyn Bridge Park, currently 3.4 acres, is expanded, the Districts will have almost 800 acres of public parkland.

Based upon our interviews with City parks officials and private recreational facilities managers, as well as studies performed by advocacy and economic development groups, we have identified the following key factors of success for active and passive space.

- Reasonable ratios for people to park acre for Manhattan range from 300 to 800;

- Well-allocated pushcart vendors are a larger revenue generator than high-end restaurants;
- Active space should be designed around either instructional or occasional use;
- New Yorkers are willing to travel for recreational facilities; and,
- New Yorkers have stronger opinions regarding acceptable conditions for sitting areas, playgrounds and passive recreation space than they do on active recreational space.

As shown in Exhibit VI-8, the New Yorkers for Parks organization rates three parks in the Lower Manhattan area as "A" level parks of the 195 parks surveyed for acceptability of conditions across New York City. These are City Hall, Battery Park and Washington Market Park, all located in Community District 1. The survey ranks parks on the basis of the conditions of its overall environment, sitting areas, pathways, passive recreation space, active recreation space, playgrounds, bathrooms and drinking fountains. Parks were not penalized in the scoring if they did not have one or more of these factors, such as recreational space, hence these parks' ability to earn high scores from the assessment. Brooklyn's highest ranked park was Columbus Park in Community District 2. Overall, the assessment found that the elements that were most neglected, or least maintained, among the 195 parks were active recreational facilities, drinking fountains and bathrooms.

## Waterfront Development

Park space on Governors Island must be considered within the context of major public investment in the waterfront and surrounding parks.

- The Brooklyn Bridge Park, a planned 63-acre park on Piers 1,2,3 and 5, will extend along 1.3 miles of shoreline. Early plans for the park include public art, open space, bike and pedestrian paths, and an indoor recreation complex for swimming, ice-skating and other sports. The Brooklyn Bridge Development Corporation has received a commitment of \$85 million for the park's design and construction.
- Across the East River from the Brooklyn Bridge Park, the East River Park redevelopment plans will extend the existing park south to Battery Park and will redevelop the entire shoreline with active and passive recreational uses. Initial designs for the park include a very innovative floating skating rink, beach and hydroponic garden. The East River Park development forms part of Mayor Bloomberg's \$10 billion waterfront redevelopment initiative, which also includes an underground rail link from Lower Manhattan to JFK airport and an opening of major arteries in downtown along West Street and Fulton Street. The architecture and planning firms, Richard Rodgers and SHoP have been selected to lead the design.
- Piers 6 through 12 in Red Hook, Brooklyn, the Red Hook Marine Terminal, are a third major area of redevelopment focus in the Harbor. These functioning piers have shrunk in port activity over the last century, receiving less than 1% of the Port Authority of New York New Jersey's total shipping volume. Almost all

(94%) of the goods received are transferred back across the Harbor to western transport hubs, making them more expensive to operate than other piers in the Harbor. Consensus across city and community groups is that the 120 acres encompassed in these piers should be redeveloped to enhance the historical and commercial nature of the maritime terminal. The first major advancement in this redevelopment is the recent partnership agreement reached between New York City and the Carnival Cruise Line for the redevelopment of Pier 7 as the Queen Mary's cruise ship terminal.

## The Economics of Park Development

Active and passive open space on Governors Island will likely need to be financed by a mixture of public dollars, private recreational institutions and dedicated trusts. Achieving financial break-even for park and recreational space is understandably difficult, even in private ventures. A detailed look at the revenue sources for New York City Parks is provided in Exhibit VI-7.

Ongoing operations of New York City's public parks are marginally supported by several revenues sources, in particular concessions, concert revenues and permit fees. There are approximately 600 concessions businesses throughout the five boroughs that cover a gamut of services. These businesses include pushcart food vendors, magazine vendors, souvenir stalls, golf courses and high-end restaurants. In 2003, concessions revenues to the City were \$62 million across the Parks' five boroughs, compared to the agency's \$250 million costs.

Pushcarts are the highest-producing revenue generators for the City. Fee structures and lease conditions for these vary in the controlled NYC Parks environment, unlike the open-use permit system employed by the City for its street vendors. Kiosk and pushcart vendors pay an individually agreed upon price to operate in a specific location within a park. The City sets prices for food and other items, and charges rents according to the value of the real estate. The rent varies widely -- one vendor in a small park in the Bronx may pay \$100 per year for an operating license while another that sells in front of the Metropolitan Museum in Manhattan pays \$300,000 per year.

Park usage, both daily and during special events, drives demand for concessions. The volume of park usage is difficult to measure. Central Park's 840 acres attract an estimated 250,000 visitors on any given weekend day; in 1982, it was estimated that Central Park attracted 14.2 million visitors. Prospect Park in Brooklyn is likely the second largest park attraction in the City; a 1987 estimate has annual visitation at 4.4 million. On a smaller scale, the successful 6-acre Bryant Park typically attracts 3,000 visitors during weekday lunch hours.

Large events obviously attract significant numbers of visitors. A free Dave Matthews concert in 2003 in Central Park's Great Lawn reached capacity with 80,000 people. Two free concerts in the North Meadow, which were tracked with less precision, brought an estimated 750,000 people (for Garth Brooks) and 900,000 attendees (for Paul Simon).

Destination restaurants on public parkland do drive traffic, but according to City Parks planners, are not significant revenue generators. Manhattan's

three destination restaurants within city parkland are Tavern on the Green in Central Park, the Boathouse in Central Park, and the Battery Garden Café in Battery Park. Fees are structured on a percentage rent basis, ranging from 3.5% to 20%, usually with an upfront payment towards that figure.

In Central Park, Tavern on the Green and the Boathouse restaurants, though very different concepts and business models, both typically pay \$1 million to the City for the license to operate on city parkland. Tavern on the Green is the highest grossing restaurant in New York with \$36 million in revenues in 2003. Based on a 3.5% of sales rent schedule, the park received \$1.3 million in revenues from the restaurant in 2003. The Boathouse in Central Park earned approximately \$11 million in revenues in 2003 and paid 15% of that, or \$1.65 million, to Parks. The percentage of revenues, and the upfront payments required, increases over time.

Other restaurant concessions include the Heliport in Flushing Meadows, Queens, which pays 9% of gross receipts for its park license, and, in Battery Park, the recently renovated Battery Park Café. The Café overlooks the Harbor and is expecting \$5 million in revenues for 2004. At this time, we do not know how that translates to concessions revenues for the City.

Merely looking at the direct economic returns of park space misses the point; the social capital and indirect economic value created by parks must be considered. New Yorkers find great meaning in their parks and have put tremendous public and non-profit resources towards their successful implementation and design. As one example, the very successful Hudson River Park Trust

redevelopment of five miles along the western waterfront – at a cost of roughly five million dollars -- is one of the latest examples of private initiative to improve the standards of living through open and recreational space. As another example, Bryant Park, the only park to receive a perfect score in 2003 by the nonprofit advocacy group New Yorkers for Parks, was a complete turnaround of a 6-acre urban park on 42nd street at the core of the city. Redeveloped 20 years ago with financing from a specially created Business Improvement District that took \$0.11 additional taxes per square foot from the seven million square feet of commercial tenants overlooking the park, the initiative turned the park into a neighborhood amenity and helped reduce crime in the area. Bryant Park recently achieved an operating surplus and reduced these taxes from its neighboring commercial tenants from a total \$950,000 to \$750,000. The park operates on a \$3 million annual budget and is entirely sustained by taxes and revenues from restaurant leases and special events sponsorship.

The indirect value of parks is difficult to measure, although their effect on real estate values and subsequent development is measured and real. Following the renovation of Bryant Park, rents increased by as much as 40% in surrounding commercial properties, and occupancy rates jumped up by 60%, according to brokers in the area. In Worcester, Massachusetts, a study measuring the impact of four parks in the early 1980's "found that a house within 20 feet of a park was worth about \$2,675 more than a similar house 2,000 feet away from the park. It was also noted that after 2,000 feet the impact is negligible." Frederick Law Olmsted performed the original economic impact analysis of parks. Ten years following

Central Park's completion in the late 1800's, taxes on property values from residences surrounding the park increased by \$54 million. Neighborhoods all over the world witness safer streets, cleaner environments and higher property values when a well-used and maintained park is nearby.

### **Chelsea Piers Case Study**

To further understand the value of recreational facilities to New Yorkers, we looked at the Chelsea Piers Sports Complex, a remarkably comparable property given its location on Manhattan's waterfront (Exhibit VI-9). The piers on the western edge of the city were a formerly desolate area with little traffic until Chelsea Piers created a destination recreational facility. The complex currently attracts four million visitors a year, more than the Statue of Liberty, Madison Square Garden and Yankee Stadium.

Built on two redeveloped piers on the Hudson River, the complex operates 1.7 million square feet of space that is designed specifically for at least 16 different types of sports use and multiple social and commercial pursuits. The majority of visitors and members are from Manhattan, however 11% come from Brooklyn, 5% from other parts of New York and 4% from New Jersey. Brooklyn residents are most interested in ice hockey and roller hockey, constituting 15% and 21% of the users of these facilities. Most Brooklyn members live in the wealthier districts of the borough and drive to Chelsea Piers.

The complex relies on repeat users, whether through the private gym membership, lessons and camp for any number of sports, or leagues that

schedule regular games. All facilities are open to the public for a price premium, although availability is limited for anything other than the basketball courts, skate park/roller rink and fitness facilities. Soccer, basketball and ice and roller hockey leagues attract 15,500 players each year. Fees for the leagues range from \$150 to \$475 for the season or \$450 to \$1,900 per year, depending on the sport and frequency of play.

Membership to the Health Club's fitness facilities costs approximately \$2,000 per year, with a day pass costing \$50. Chelsea Piers earns more revenues with a reduced membership and higher fees than it did with a lower-fee revenue model. Membership dropped from 8,000 to 5,500 as a result of price increases since Chelsea Piers opened. Golf driving range users have also shown a willingness to pay a premium for the facilities. The lowest tier of golf membership is priced at \$325, and only allows players to call for reservations within 48 hours of a desired tee time. The highest \$4,200 annual membership allows players to reserve 60 days in advance, guaranteeing tee times, and also includes four lessons.

Chelsea Piers also operates a 22,000 square-foot event space, Pier 60, which is run by the exclusive caterer Abigail Kirsch. The space has become the most profitable activity to date for the complex, but only became feasible once transportation barriers were addressed. Buses and taxi drop-offs were given ample space to maneuver within the pier's parking area, making event planners and guests more comfortable with their options for arrival and departure.

Overall, transportation has improved to the complex since it opened in 1997. Two bus lines access the waterfront, when before, they ended the line two long avenues inland at 9th Street. Bus travel is used by only 15% of the members, whereas the majority (39%) drives. Other members arrive by taxi (17%), subway (15%), or by walking, skating or biking (14%). Still, Chelsea Piers does not enjoy tremendous access, and thus users must trade-off some convenience of access for the opportunity to use facilities that are truly unique in the Manhattan market.

Chelsea Piers rents the piers from the Hudson River Park Trust. The complex is not always profitable and has retained financial assistance from the City, though the degree and terms need to be studied further. The Chelsea Piers corporation is making a bid for Pier 57 to the south of the complex. If successful, it will expand its activities to include cultural space for galleries and dance recitals, a 30,000 square-foot swim center, and a 100,000 square-foot tennis center. Tennis and swimming, according to managers at the Piers, are a large recreational market void.

## **Demand Analyses**

In order to provide some sense of depth to the demand for park and recreational amenities at Governors Island, we completed statistical demand analyses of visits to passive park space (Exhibit VI-10) and need for recreational facilities (Exhibit VI-11).

Exhibit VI-10 estimates the likely number of visits that a large park could achieve on Governors Island (outside of large events). Demand potential was

determined for a number of nearby Community Districts (CDs), in Manhattan CDs 1 through 12 and Brooklyn CDs 2, 6, 7 and 10, 11, 12 and 14. Based upon a 1997 study of park usage, we estimated the average number of park visits per month for each of the seasons. We then applied a capture rate for the proposed Governors Island park space, based upon proximity of the particular CD to Governors Island, competitive park spaces and taking into account transportation concerns associated with the Island (including the expectation that ferry access will be provided at a cost to visitors).

We have estimated that approximately 2.9 million persons would potentially visit a large park on Governors Island each year. Approximately 58% of this demand will come from the surrounding neighborhoods, with an additional 12% from residential areas outside of the defined market areas. Approximately 30% of total demand, or 867,000 visitors, will originate from visitors to New York City and Lower Manhattan.

Approximately 68% of demand will occur on the weekends. Summer months will represent the most active part of the year, with 1.7 million of the total 2.9 million visits. A summer weekend day could attract an average of 28,800 visitors a day, with spring weekend days (13,500) and summer weekdays (11,600) representing the next busiest times of the year.

Exhibit VI-11 calculated the demand potential for a variety of recreational uses. This demand was based upon NPRA thumb rules for the amount of facilities that should be provided in urban areas.

These thumb rules are:

- A softball/baseball diamond, and Little League baseball field for every 1,500 persons;
- A soccer field for every 4,000 persons;
- A basketball court for every 3,000 persons;
- A tennis court for every 1,500 persons;
- A golf driving range for every 25,000 persons;
- A swimming pool for every 1,000 persons; and,
- An ice hockey rink for every 50,000 persons.

Given the significant population in relatively close proximity to Governors Island and the scarcity of existing recreational facilities in many neighborhoods, we have found that there is very strong demand for multiple units of the variety of recreational facilities listed above. This is true even when assuming rather conservative capture rates for Governors Island. Based upon our demand analysis, a very large recreational complex could be supported on Governors Island.

## VII. Marina

### Summary

The Island needs to effectively address the waterfront. Where appropriate, given conditions of the current, water activities such as kayaking and sailing launches could prove to be very successful. We also have found there to be a very strong opportunity to develop a marina on the Island. The number of slips and moorings in the greater New York City are well below the potential number of boat owners, based upon our demand analysis. The market is certainly undersupplied today, as the marinas we surveyed are almost all 100% occupied. The concept of a marina certainly fits on the Island, although a safe harbor will likely need to be constructed.

A marina at Governors Island should be approximately 200 to 250 slips, with about 20% of the slips used for transient traffic and the remainder used as seasonal rentals. We do not expect that the marina will be used during harsher weather months, and thus seasonal rental slips make most sense. Creating a year-round marina would require upland facilities, which are often very unattractive and most likely would not fit into the land plan for the Island. Transient slips fill a particular market void, and are attractive in that provide another access point for visitors to Governors Island. Seasonal slips should be rented at \$120 per foot of boat.

The subject site should seek to minimize the travel time to Governors Island and maximize the potential convenience of the site to the areas defined as the competitive market area (CMA). Dedicated shuttle boats that leave every 15 minutes from locations

throughout the CMA may be necessary to ensure that boat owners feel they have “instant” access to their prized possessions, even though they will be unable to travel to their boats by land. The marina operation should utilize Wi-Fi technology and GPS in order to make it as convenient as possible for transient boaters to reserve slips and navigate to the marina.

### Industry Overview and Critical Success Factors

Marinas consist of two primary land uses – waterfront and upland development. Waterfront property contains boat-docking systems, such as slips, docks and moorings. Upland development contains related and supporting activities such as office, supporting retail and boat servicing/fueling operations. Because waterfront development is heavily regulated by the Clean Water Act and the US Army Corps of Engineers, it is a development type with very high barriers to entry.

Construction and expansion of waterfront development is therefore a very difficult venture, even for sophisticated development ventures with deep pockets. Within the past two decades, Goldman Sachs attempted to enter the marina development industry, but found quickly that the lag times between financing and lease-up to be inconsistent with typically accepted timeframes and rates of return. Their subsequent exit from the field has left just a few major institutional investors in the United States, the most notable of which are Westrec and Marinas International.

Successful marinas typically meet the following criteria:

- Access to target demographics is key. According to the National Association of Marine Manufacturers (NAMM), the typical boater is 45 years of age or older, is married and has a household income of at least \$80,000. Boaters tend to live where they boat – this minimizes travel time to the marina on precious weekend mornings – and marinas typically locate no further than a one-hour drive from a the target demographic.
- Upland development can either make or break a marina. Successful marinas provide fuel, boat and motor repair, pumpout and haulout and sundry retail where seasonal or year-round boaters are prevalent. In some cases, more robust packages can include boat dealerships, business services, dry cleaning/laundry, fitness centers and restaurants. Where transient boaters are prevalent, a marina should cater to their distinct desires for privacy, resort-like amenities, upscale retail and fine dining. Full-service marinas in either category can charge higher rates and maintain full-occupancy more readily than limited-service marinas.
- Marinas must provide and maintain safe harbor for docked boats, whether in wet slips or in moorings. While the cost of breakwaters and/or other water calming mechanisms may be costly, boat owners are typically very averse to rough waters in harbor, which can cause significant damage to boats should they knock together. A component of this has to do

with currents and tides, and a component has to do with the nature and frequency of waterborne traffic in the adjoining waterways.

### Overall Market Trends

The boat-building industry nationwide is booming. The NMMA estimates that marine manufacturers increased production levels an average of 17% during the second quarter of 2004, and 92% of marine manufacturers are looking to expand production, either through increased employment or through capital investment. Boat sales nationwide have shown steady growth for over a decade, growing from 10.78 million registered boats nationwide in 1989 to 12.85 million in 2003, a growth rate of 1.26% per annum.

The health of the boating industry is evidenced in New York, currently the 6th leading state with respect to boat registrations according to the NMMA. From 1997 to 2003, boat registrations in the state increased from 512,430 to 532,672, showing steady growth even through the recent recession due to strong sales in used boats while sales of new boats declined somewhat. According to the New York State Department of Parks, Recreation, and Historic Preservation, and shown in Exhibit IV – 1, growth in New York boat ownership is expected to continue to rise at a rate faster than New York population growth for the next 15 to 20 years.

Within New York City itself, boat registrations have grown 11% since 1996, from 23,755 to 26,403, a rate of 1.52% per annum. While in absolute numbers the largest gains were in boats 16' to 25' in length, the fastest-growing classes of boats

were, in order, the 40' to 65' and 26' to 39' classes, which grew by 29% and 26% over the period, respectively. Interviews with marina owners in New York City confirm that these registration trends have resulted in a surge of demand for boat slips that accommodate boats 26' and longer, and especially for boats 40' and longer.

The New York City slip capacity has not grown in tandem with demand. Because of the aforementioned strict barriers to construction and expansion, area marinas have not been able to expand their operations to accommodate the increasing number of boats in the city. Additionally, marina owners affiliated with boat dealerships contend that limited slip availability in the city has actually stymied demand for boats. Finally, some marinas have actually been taken offline as residential developers acquired and developed the upland areas for condominiums or luxury apartments. In short, the marina slip market has not kept pace with the market for boats in New York City.

According to marina operators in New York City, boaters have had to look southward to New Jersey or eastward to Long Island to locate slips to accommodate their boats. Marinas in New Jersey such as Liberty Landing, within a 10-minute ferry from Lower Manhattan, have recently added significant slip capacity to handle spillover demand from New York City. The same is true of Lincoln Harbor in New Jersey, which accommodates a large number of New York City boaters unable to find slips in New York City. As dredging and waterway issues plague New York City harbors seeking expansion, competing marinas in other waterways should continue to successfully attract and retain clientele

intent on slipping their boats within 45 minutes of Manhattan.

Many marinas incorporate boat dealerships into their operating model. Chelsea Piers Surfside3, for example, is a primary SeaRay dealer. In some marina financial models, boat sales can in some years account for up to 50% of total revenues. Preliminary conversations with marina investors indicate that boat manufacturers would be eager to establish a sales location at a potential marina on Governors Island.

### Subject Site Analysis

The subject site has an outstanding location, situated at the intersection of New York Harbor's heavily-frequented Hudson River, East River and Long Island Sound waterways. It provides access equal to or better than that provided by Liberty Landing and Lincoln Harbor, though it is not accessible by car or proximate to residential development. The site, accessible only by boat, has long been associated with maritime activity, and may be seen as increasingly desirable for boaters in conjunction with other development on the Island as well as the emergence of the Cruise Ship industry across the Buttermilk Channel in Brooklyn.

Like all New York City area marinas, the waters surrounding Governors Island may pose some challenges to creating and sustaining safe harbor. Marina owners surveyed indicate that wave heights surrounding Governors Island can reach averages of three to five feet, and the constant wind on the west side of the island is well-documented. Two implications for the subject site influence slip

construction and slip demand. First, marina owners in the area indicate that boaters who navigate the waters around Governors Island typically drive powerboats longer than 30' – smaller and/or windpowered boats are subject to difficult navigation and capsize. Second, the natural waves and wake-generated waves (from large boats such as NY Water Taxi and the Staten Island Ferry) make the provision of safe harbor more difficult. Maintaining heavily-impacted breakwaters in order to protect expensive boats can be a cost-heavy endeavor, and even Surfside3 owners cite heavy waves and wakes as competitive disadvantages to calmer waters in New Jersey. Of course, should the subject site accommodate a share of transient boaters and limit or eliminate wet winter storage, these concerns become a moot point.

Finally, with the potential for recreational, restaurant, hospitality and other uses being considered for development on Governors Island, the subject site presents the opportunity to generate upland development to optimally-suit the target boater. In particular, the resort-type amenities associated with boutique hotels and top-flight conference centers would mesh very nicely with the needs of transient boaters, who are currently grossly underserved in the New York City market. High-end, larger, transient boat-users who boat for travel and tourism would frequent high-end restaurants, spa facilities, recreational amenities and even retail – uses that might also complement other contemplated uses on Governors Island. According to marina investment experts at Marinas International, who have been investigating the New York marina market for many years, the site might attract as much as 25% of its slip capacity from transient boaters.

## Supply Analysis

Local market data and national industry experts agree that boaters typically slip where they live. Boaters have a desire to access their boats within no more than a one-hour travel time, and ideally no more than a 45-minute travel time. In most cases, boaters drive from their homes to the marina. However, in the case of New York City, interviews with marina operators confirm that many boaters take public transportation to shuttle-boat launch points that take them quickly to their marina of choice in Brooklyn, Staten Island or New Jersey.

Based upon our research, the Primary Market Area (PMA) for the subject site includes all of Manhattan, Brooklyn Community Districts 2, 6, 7, and 10, Staten Island and the counties of Hudson and Bergen in New Jersey. The Secondary Market Area (SMA) is less geographically defined, but will draw on the population of transient boaters who frequent the mid-Atlantic harbors, typically from Maine to Maryland. Based upon research in the local market, Connecticut, Long Island and Westchester Counties provide an entirely different marina experience, thrive upon boaters who live in these communities, and do not fall into the marina PMA for the subject site. Furthermore, CMA for the subject site consists of the East River, Hudson River below Spuyten Duyvil, City Island, northern portions of Staten Island, Sheepshead Bay, Bay Ridge and the counties of Hudson and Bergen in New Jersey.

Area marinas are operating at or near full-capacity, with waiting lists at almost every marina in the CMA and slips renewed year-to-year in over 85% of the marinas surveyed. In most local cases, new and used boat sales are contingent upon

securing slippage at the sales or nearby marinas, underscoring the tight supply of slips. A summary of relevant market data surrounding marinas in the CMA and PMA is given in Exhibits VI – 4 through VI – 7.

In general, seasonal slip rates can range from \$75 to \$140 per foot, depending on the boat length, while wet winter storage can range from \$25 to \$50 per foot. Though marinas in City Island, such as Ever's Marina, are typically cheaper than other locales, many of these are in the process of raising their rates to meet market pricing. Marinas surveyed indicated that most new demand was originating from boats longer than 40'. Dry rack storage is relatively under-developed in the market area, most likely due to the fact that the PMA is over-supplied with respect to winter storage facilities. Fueling stations are limited in the area, owing to the difficulty of constructing and maintaining underground storage tanks (USTs). Finally, existing marinas, because they cater primarily to residential boaters rather than luxury tourists, have not yet seized on the opportunity to capture and/or draw demand from transient boaters eager to visit New York City by boat.

While CMA marinas are at capacity, numerous marinas in New York City have been recently closed and sold to residential developers. This trend is especially prevalent in City Island, a unique maritime community in The Bronx. Meanwhile, existing marina operators, eager to capitalize on boat sales trends of these expensive and large boats, have been unable to expand their marinas due to restrictions on additional dredging. Citing unmet demand, Surfside3 at Chelsea Piers and the 79th Street Boat Basin, along with several other

marinas, are attempting to expand or even double the number of slips they offer, especially for boats longer than 40’.

Strict environmental regulations and dredging guidelines have prevented any expansion efforts thus far, and in part give cause for the continued success of new marina development and expansion in New Jersey, Long Island and along the Hudson River north of New York City. For example, Liberty Landing, which lies directly across the Hudson River from Lower Manhattan, recently added 200 slips and continues to operate at or near full occupancy for the summer season.

In fact, most marinas in the area are operating near or at full occupancy, and many marina operators have long waiting lists for available slips. New Yorkers who own boats are slipping their boats in New Jersey, Westchester County, and Long Island, in part due to the lack of availability of slips in New York City. According to some experts, potential boaters in slip-constrained environs may even be putting off boat-buying decisions because of the scarce availability of convenient slips, a condition which is assumed by industry experts to be taking place in New York City.

### **Demand Analysis**

Boat ownership has historically been related to household wealth, household income and general macroeconomic trends. As marine loans typically require household income of \$80,000 or greater, this facet becomes especially important for demand for smaller boats, or those less than 24’ in length. Since larger boats, or those greater than 24’

in length, can cost anywhere from \$250,000 to more than \$1 million, plus dockage, maintenance, licensing and other fees, demand for these boats is less subject to macroeconomic fluctuations, because owners of this class of boat tend to be more insulated from year-to-year economic shocks.

Demand for boating and slips is expected by the New York State Department of Parks and Recreation to outpace population growth in New York City over the next ten to twenty years. Industry data confirms that sales of larger boats will continue to be strong nationwide. Conversations with boat dealers in New York City confirm that this trend is prevalent in the local market area, as well. Limited slip availability has muted boat demand in the area somewhat, but anecdotal evidence indicates strong expressed interest in slips that can accommodate boats over 40’.

Based upon the above, although we did not complete a statistical demand analysis for a marina, there appears to be ample demand for a marina on Governors Island.

## **VIII. Commercial, Retail and Restaurant/Banquet**

### **Summary**

Governors Island does not make market sense as a conventional office or retail location, given concerns over accessibility and visibility. However, there are strong opportunities to develop commercial space that either is a true destination or is supportable by existing traffic to the Island. There is likely no more unique and exciting place in New York City than Governors Island, with the great open spaces, historic and charming buildings and incredible views. Therefore, selling the Island as a destination will be a natural fit.

Along these lines, we believe there is strong market support on the Island for several banqueting and event spaces, and one or more destination restaurants. Traffic to other uses on the Island will also support approximately 20,000 square feet of Island-serving restaurant space and 16,000 square feet of specialty retail. There is likely also a small opportunity to develop office space for users already on the Island for other reasons.

This development should be clustered together in order to create a critical mass of activity. This is particularly important for the restaurant uses; the mixture of destination and Island-serving restaurants will create a multitude of culinary options at different price points. To every extent possible, the development of retail and restaurant space should leverage obvious synergies with other planned uses. For example, the banquet facilities and restaurants should have at least informal agreements with the

conference center and hotels on the Island, so that all Island amenities are fully utilized and market potential is fully realized.

Another synergistic opportunity may be the opening of one or more restaurants in conjunction with a culinary institute. The five restaurants at the Culinary Institute of America in Hyde Park, located two hours north of Manhattan, draw tourists, wedding parties and adult education participants whose courses include a meal at one of the five for every day of instruction. The restaurants are booked every weekend and reach 60% to 75% occupancy during the week. They are also operated on very low budgets, serviced at no labor cost by the full-time students of the school. If pursued in conjunction with culinary courses on the Island, restaurants of this form would provide a natural and affordable synergy.

### **Banquet and Event Space**

Based on our primary research, including discussions with event planners and catering companies in this market, we believe that the opportunity for event and banquet space on the Island is strong. GIPEC has already received unsolicited interest from firms very interested using the open spaces and historic buildings for large and small events. Four particular market needs emerged from our interviews with operators:

- Unique, beautiful location for all types of events;
- Outdoor space for spring and summertime events;
- Banquet space that can seat 1,000 people or more; and

- High-end restaurant or banquet spaces for private events of 25 to 40 people.

Unique spaces in exciting locations certainly drive the demand for high-end banqueting facilities, and there is likely no more unique and exciting place in New York City than Governors Island, with the great open spaces, historic and charming buildings and incredible views. While we discovered that a particular market void exists for larger banqueting facilities, as well as more intimate settings, demand will be strong for a broad range of banquet facilities.

Success of banquet facilities on the Island will depend on execution and operation of those spaces. We recommend that the island consider an arrangement with an exclusive operator that will provide redevelopment capital, manage the development process, equip the facilities and ensure a seamless experience for their clients. Although the financial implications of an exclusive agreement with a caterer versus running the facility as a non-exclusive facility needs to be further tested before a final decision can be made, an exclusive agreement does seem to limit overall risk while making it more likely that the layout and design of the banquet facilities are in line with market demand (since caterers would be most adept at identifying market needs and shifting consumer preferences).

One of the most important issues to resolve for the existing venues in unusual locations is transportation, and Governors Island will be no different. Ferries (or alternative modes) must be convenient and of a quality that meets the expectation of high-end banquet planners and guests.

### **Banquet Market Trends**

Corporate functions, non-profit fundraising events and special social events (weddings, bar/bat mitzvahs, etc.) drive the high-end banquet business. Corporate business is the largest segment of demand for most caterers, constituting between 65% and 80% of the revenue-generating activity of most firms. A very large portion of this corporate segment is non-profit fundraising events. Given the breadth of options for size and scope of events – they can range from a 30-person private dinner to a 2,000-person unseated gala – a wide variety of flexible spaces are required to meet market demand (Exhibit VIII-1).

Banquet spaces often operate under exclusive agreements with catering companies. As part of these exclusive agreements, caterers will often commit capital to the development, rehabilitation and or maintenance of the facility in order to specific spaces in order to secure a good location for their patrons' events and to capture the additional business that is drawn to the building or space itself. Other agreements may simply be a long-term lease, or an upfront reservation for specific dates throughout the year. In these cases, GIPEC (or a third party investor) would likely be fully responsible for the development of the banquet space. The negative aspect of an exclusive agreement is the opportunity cost of having fewer points of sale to the public through multiple catering companies and fewer events to produce revenues.

## Competitive Banquet Supply

Unique spaces certainly drive traffic and can charge a premium. Across New York, locations whose primary business is not the rental of its space, such as the New York Public Library, Grand Central Terminal, Ellis Island, The Metropolitan Museum and the Museum of Natural History, are known to charge very large fees for the use of their space alone. The Metropolitan Museum charges \$30,000 just to gain access to the space, then requires payment for its own security, housekeeping and other personnel.

The Ellis Island Museum hosts approximately 50 events every year for large corporate and non-profit clients – up to 2,000 people for a single event. Although a stunning location and historic building, the hall suffers challenges of both availability and accessibility that curtail its success as a banquet hall. All events must be set up after the museum closes at 6:45 pm, leaving little chance for decorations. Transportation is another significant market barrier. The Circle Line ferry is expensive for a private event, and the perceived barriers of being unable to return to mainland are troubling for some users.

Ellis Island charges \$15,000 to \$18,000 for use of its vast hall and reception landing. Guests to Ellis Island must also pay Circle Line boats for private service to and from the island at a cost of \$7,500 per boat. Thursday nights are Ellis' biggest nights; the hall is closed for event business in the winter months. Aramark Corporation has the exclusive arrangement with the Island to service the museum restaurant and cater the events, often through its high-end partner, Great Performances (Exhibit VIII-2).

There are a number of full-time banquet facilities in the area, although according to industry experts there is pent-up demand for high-quality spaces. The Abigail Kirsch catering company is the exclusive operator of the 22,000 square foot Pier 60 event space at Chelsea Piers. The relationship has been in place since the complex opened, and is one of several exclusive venues where the caterer operates. Others include the Tappan Hill mansion in Tarrytown, the New York Botanical Gardens and the Abigail Kirsch yacht, which seats 150 people. Pier 60 is the most profitable business arm of the Chelsea Piers complex. Transportation and access issues had to be addressed before the public was comfortable making the journey to the West side where taxis are scarce and the West Side highway divides the waterfront from the livelier parts of the city. Once buses, limos, and taxis were given ample access and parking in the complex, occupancy of the hall reached high levels.

The space is a standard, large space with carpeting and movable walls that can be utilized for corporate events and weekend weddings. It hosts an average of three events per weekend and multiple corporate events per week. Daytime meetings are less common, though feasible in the space. The center's main attraction is its views to the Hudson River at the end of the pier. Furthermore, it is one of a few places in Manhattan that can seat 1,000 people for dinner. Without food costs, the 22,000 square foot space rents for \$45,000 per day. Total costs for a weekend night at Pier 60 ranges from \$190 to \$260 per person. This is at the top of the market for full-time banquet and event facilities; Ellis Island does garner a higher positioning, but has the luxury of only having the fill a limited number of dates (Exhibit VIII-2).

The Waldorf Astoria is widely considered the only hotel in Manhattan whose 60,000 square feet of ballroom/meeting space is appropriate for large, high-end social events. The New York Hilton and Towers, Sheraton Hotel and Millennium Broadway also have large meeting spaces, but also have a much more conservative decoration and cater to a strong corporate market. The market for larger social events is captive for the Waldorf, whose hotel rooms and location in Midtown offer a traditional and easy setting for events. The general understanding is that the service and quality have declined with little competition in the market.

Luxury hotels such as the Four Seasons and Ritz Carlton Battery Park have 10,000 and 12,000 square feet of meeting space, respectively. These spaces can accommodate medium-sized social events (200 to 500 people), and will be competitive with similarly sized venues on Governors Island. They typically charge \$100 to \$150 per person, based upon a three to four hour event.

## Demand Conditions for Banquet Facilities

Exhibit VIII-3 provides a quantification of expected traffic to medium-sized (500 person) and larger (1,000 person) banquet facilities on Governors Island. In order to do so, we have estimated the average number of events per day, the average space usage rate and the average percentage of capacity that is used when the space is rented. These estimates are based upon our interviews with operators in this market. Generally, space usage rates will be greater on weekends than on weekdays, although weekdays do allow for more events per day due to the business-oriented breakfast event. We are assuming a significant

lull in demand during the winter months, in part because this tends to be a lower season for the industry as a whole, but to a greater extent because of the market challenges associated with the particularly harsh weather on the Island during the winter months.

In total, we have estimated that a 500-person banquet space will attract approximately 166,000 persons each year, about 97,000 (58%) of which will fall on the weekends. A 1,000-person facility is projected to attract approximately 386,000 persons each year, 260,000 (67%) of which will be on the weekends. These figures do not include larger events on the Island, or events geared solely towards outdoor spaces.

### **Destination Restaurants**

The success or failure of a destination restaurant is very difficult to predict, as this restaurant type does not rely on traditional factors such as access, visibility or location near a concentration of complimentary land uses. Instead, these restaurants are only a success when they have become a true destination – because of the quality of the food, the uniqueness of the concept or location, or a combination of both. We believe that Governors can support one or more destination restaurants, given the Island’s natural beauty, historic structures, mystery and uniqueness and the extraordinary views. The key will be attracting the restaurant operators that can leverage the existing resources with a concept and design that will excite the marketplace.

We do expect that there will be lulls in demand, especially during the weekday (due to the

inefficiency of the location for business lunches) and the winter months. Even with these expected down periods, we have found that revenues at a 200-seat destination restaurant could approach \$1,600 per square foot. Guidelines for restaurant construction and development in New York City indicate that sales per square foot should be \$800 at a minimum. Successful restaurants such as Tavern on the Green, the highest grossing restaurant in the city with \$36 million in revenues in 2003, reaches sales above \$1,500 per square foot on an estimated square footage of 22,000 square feet.

Even though a destination restaurant is a destination, and therefore consumers are more likely to accept a more inconvenient trip, transportation and access will still be critical. Ferry service must be available in short lead times, as consumers arrive at various times throughout the day. The ferry service must also match the quality of the restaurant experience. If the ferry ride can be made a part of the experience, with a short trip around Governors Island combined with on-board bar service and restaurant check-in, the ferry ride may actually be viewed as an amenity.

### **Destination Restaurant Market Conditions**

Most restaurant traffic is driven by basic retail concepts – visibility, accessibility, concentration of complimentary uses, etc. However, destination restaurants create their own traffic through a combination of very high quality of food and service, and the uniqueness of the concept (including, at times, the presence of a celebrity chef) and/or location. Exhibits VIII-4 and VIII-5 provide relevant data on several destination restaurants in the New York area.

The average check per person at high-end destination restaurants ranges from \$100 to \$150. The market tends to be a mixture of “once-a-year” customers seeking a special experience, executive business lunches or dinners and smaller corporate and social group events. The group demand typically contributes 35% to 50% of demand, and as mentioned above, we found during our interviews that there is apparently significant pent-up demand for spaces that can accommodate this market.

The River Café in Brooklyn is a good example of a destination restaurant. The River cafe has not encountered difficulties with getting customers to its remote location. The restaurant has been a waterfront success for almost thirty years and reaches capacity every weekend night, seating more than 220 people three days a week. At an average \$100 per meal per person and an estimated 75% occupancy during the week, the restaurant achieves approximately \$7 million in sales each year, or \$1,300 per square foot.

One restaurant to watch carefully is the Battery Garden Café, at the tip of Battery Park City. The former chef of the Pierre Hotel in Midtown recently reopened the café as an upscale restaurant, with views of the Hudson in a modern open-air setting. Functioning as a concession in the New York Parks Department, the restaurant is estimated to have revenues of \$5 million on approximately 150 seats. In order to be successful, the restaurant will need to establish itself as a destination, due to its location on a very beautiful but quiet corner of the park.

Successful restaurateurs in New York have pursued a strategy of concentrating restaurants in order to create a destination. Danny Meyer’s Union Square

Hospitality Group, which has been responsible for the successful launch of the Gramercy Tavern, Union Square Café, Tabla, 11 Madison and recently Blue Smoke, has pursued the restaurant row strategy in the Union Square and Flatiron district. Choosing to anchor the 14th street to 23rd street area around Broadway with highest-quality restaurants, each one with a different flavor and décor, the group has established a destination of the area itself, attracting other chefs such as Bobby Flay to the region as well.

### **Demand Conditions for Destination Restaurants**

It is very difficult to quantify the demand for destination restaurants; in New York, the demand for a unique restaurant experience is deep, and market failures are typically due to the lack of traction for the concept rather than weakening demand. In Exhibit VIII-6, we have attempted to test the feasibility of a destination restaurant given certain assumptions about demand during certain days of the week and months of the year.

Destination restaurants will generally have between four and six seatings per day. We have assumed that a destination restaurant could achieve an average check per person of \$100 for dinner and \$50 for lunch. We have also assumed that there will be demand lulls on most weekdays, in particular due to the relatively inconvenient location for business lunches, and during the winter, when harsher weather conditions make the Island a less attractive destination. Approximately 64% of demand will be on weekday or weekend nights. Weekend days will comprise 21% of the demand versus only 15% of demand on weekday days. Approximately 40% of the demand will originate in the three summer

months, in sharp contrast to the winter months, which will contribute only 10% of total demand.

Even with these expected down periods, we project a 200-seat, 8,000 square foot destination restaurant on the Island could achieve sales of approximately \$12.8 million, or \$1,599 per square foot. This level of sales is comparable to other destination restaurants we researched, and is well above the \$800 to \$900 per square foot threshold for the development of new restaurant space.

### **Retail and Office**

While both the retail and office markets are improving in Manhattan in general, and Lower Manhattan in particular, such uses require a critical mass of complimentary uses, households, jobs and/or visitors. These uses also have to be highly accessible and visible. Clearly, the Island is not an appropriate location for stand-alone office or retail uses.

However, the Island will obviously generate a significant number of visitors – to stay for a few hours, the day, or one or more days in one of the hotels that will likely be developed on the Island. Exhibit VIII-7 quantifies the amount of potential restaurant and retail space that can be supported by traffic to the Island.

Assuming all the uses listed are developed on the Island, we project that approximately 19,500 square feet of restaurant space and 16,250 square feet of retail space can be supported on Governors Island. The restaurant space will offer a wide variety of food options and price points, from park-side food stands to fast casual restaurants and mid-class sit down

restaurants. The retail space will be a mixture of convenience and specialty shops. Although we did not quantify local-serving office demand, a small amount of office space is likely supportable, in particular serving users already with a presence on the Island.

## IX. Education

### Summary

There are excellent opportunities for educational uses on Governors Island. Not only does the Island itself already possess a campus-like environment reminiscent of a New England college campus, but its location just minutes from Manhattan combined with its serene, peaceful setting provides a unique opportunity to create a quality learning environment that is both secluded yet connected.

Based on the unsolicited interest from numerous educational groups, we know the appropriateness of the island for learning activities is strong. We have considered wide range of educational activities to ascertain their potential impact upon total visitor traffic to Governors Island and understand the potential connections and synergies with other proposed uses. These uses range from educational opportunities for public school children in New York City to first-class teaching facilities for premier educational institutions. They are public sector and private sector, and they cover all ages and activities.

The proposals received to date by GIPEC are the New York Harbor School, The City University of New York (CUNY) summer school and auxiliary campus use, and a proposal for a nanotechnology research center. To this list, we have added the “Governors Island Institute”, a colloquium of thinkers and leaders who will interact, live, work and teach on the Island; a specialty education component, such as the Culinary Institute of America, which teaches professional and continuing education courses to a wide urban market; and an environmental education center, which would provide an ecological learning

environment for visitors to the Island. Finally, student dorms have been considered as a possibility for temporary housing, given the shortage of dorms in New York City.

### Public Schools – Harbor School and CUNY

The Harbor School and CUNY would be able to provide their students – New York City residents – with a unique campus setting for their programs. Demand and feasibility for the programs is determined at the school level and would not represent a financial obligation on the part of GIPEC. Synergies are high among the other uses planned for the Island, with the most intense impact of a school being the constant and steady stream of people to the Island during the week.

New York Harbor School provides a hands-on curriculum for inner-city children in conjunction with the South Street Seaport Museum, The Waterkeeper Alliance and The NYC Department of Education, among other organizations. It is a new program designed for high-school teens who do not have access to outdoor learning opportunities and whose public education options are among the lowest-ranked in the city. The school has already taught its first class of students and is looking for a home where it can more easily develop its unconventional curriculum, which teaches kids through activities such as sailing and boatbuilding. The proposal identifies buildings 310, 315 and 330, constituting 22,000 square feet, as the optimal locations for its Phase 1 rollout for 250 students. Long-term plans include buildings 324 and 333 to teach 500 students and house a certain portion of them in a total of 46,500 square feet.

CUNY has also identified Governors Island’s historic buildings and campus setting for specific potential uses. However, any further investigation of the opportunity would need to follow a City-mandated process that determines the school’s expansion plans. School representatives attest that educational facilities are in short supply for all institutions in the city. Original interest from a higher education institution came from New York University in the late 1990’s, but was dropped when it decided to expand into the East Village. CUNY proposes a campus on the Island that will focus on a specialized form of study such as marine biology or art and drama. It will also enable the institution to do teacher training and summer school for kids during the summer.

The traffic and population impact of a university campus on the Island would be tremendous and needs to be considered in the context of its impact on the non-public sector uses on the Island. Next steps will likely involve the input from selected anchor tenants such as a conference center and destination restaurants.

### Governors Island Institute

Though still unformed, the concept of a forum for academics and world leaders has emerged and remained a point of great interest among contributors to the Governors Island development. The Governors Island Institute would become an important place of learning and convening, unique in the world much like Davos or the Aspen Institute. It would help root the identity of Governors Island in a global, high-level concept and associate the Island with leadership in the minds of New Yorkers and people around the world.

The Institute has several resources to provide the foundation of the thinking behind it: Wall Street, the United Nations and the numerous first class colleges and universities nearby. The Institute will need to be developed by a consortium of leaders in one of these or another similar area, and should be very specifically structured around the needs and goals of that thought industry in order to retain the clearest possible sense of purpose and identity.

The officers' homes around the courtyard in Nolan Park and the comfortable setting of the academic halls provide an ideal platform for the development, sharing and assessing of ideas. Just as the Xerox Parc Lab in Palo Alto is designed to foster creativity, with sofas and desks mixed together and white board covering every wall, the protected yet luxurious Island environment can do the same. Institutional models need to be studied and designed according to the desired level of interaction. There are ample resources to accommodate an Institute of high-level participants without too much conversion of the existing historic buildings. It is an interesting option to explore and one that is synergistic with the other uses on the Island.

### **Environmental Education**

Environmental education has emerged as an area of interest for the educational efforts considered for the island, particularly marine ecology and maritime history. Passive park space at the southern end of the Island will become an important part of the Island's character and will also be one of the few large spaces in New York that offers access to the water from the coastline. It can become a place

where children can experience nature beyond Central and Prospect Parks.

Both CUNY and the Harbor School have strong environmental components to their proposed curricula. CUNY has proposed a marine-focused campus on the island that would gather experts, visiting scholars and students from all CUNY and other schools to the Island to focus on marine biology and ecology studies. The New York Harbor School, together with the US Army Corps of Engineers, has proposed building a hydraulic model of New York Harbor, much like San Francisco's Bay model that attracted 250,000 visitors in 2003. The Harbor School's learning methods are very focused on helping children understand physics, math, ecology and geology through the practical application of techniques in the outside world. It has focused on the Governors Island opportunity for the indoor, outdoor and water-based resources available.

Another idea proposes an environmental learning center that combines functioning wind turbines and solar panels with interactive and educational exhibits on hydraulic power, maritime travel and design and marine ecology. The Island's unique location and access to water, unobstructed sunshine and wind make it an ideal setting for an interactive environmental learning center. Technologies for renewable energies can be demonstrated and used to help support the Island's electricity needs, which are significant if any further development is pursued. This type of center would create a hands-on learning environment and laboratory for renewable energy and sustainability in the Harbor while feeding clean energy to the remainder of the Island.

### **Specialty Schools**

The specialty school option, like all continuing education programs at universities, provides a broad market of people with access to educational opportunities after they have finished school. This is usually a professional market that is willing to pay very high prices per hour of instruction when compared against a full-time program. It is a good market and re-use of resources for many educational institutions. Specialty education courses that should be explored for Governors Island are sailing, cooking, arts and acting and any number of possibilities.

We have profiled the Culinary Institute of America here to better understand how this entity might use and interact with Governors Island and its accompanying resources/amenities. A detailed description of this organizations and its potential use is given below, and should be used as a guide to understanding how the Island might serve the needs of a yet-to-be identified educational institutional partner.

### **Culinary Institute of America – an in-depth study**

Culinary institutes represent an interesting opportunity for the Island's educational use. These schools apparently operate at high margins, covering costs with tuition, whether designed for a corporate, professional, or individual structure. In our analysis of culinary institutes, we have identified a strong market opportunity for the continuing education course offering. This concept is a one-day to two-week cooking course that is targeted to amateur chefs and backed by renowned institutions such as Cordon Bleu or the Culinary Institute

of America. The continuing education market represents the “low-hanging fruit” of the culinary market, an easily targeted and untapped market of non-professional cooks that is willing to pay for specialized courses. Once kitchen and specially designed classroom space is built, the facilities are easily expanded to draw on a larger market. Ancillary uses for the instructional kitchen facilities would include demonstrations by celebrity chefs, film leasing of the facilities for commercials and special events by restaurants and professional chef associations. The Culinary Institute of America’s Napa Valley location, as an example, does three food demonstrations per day, attracting San Francisco residents and visitors to the wine region for numerous events.

The bulk of continuing education courses are one to two day courses, offered on the weekends. They are typically structured as learning retreats for high-income markets, and include a full day of coursework in the school kitchens and a meal in a leading restaurant associated with the school. The synergies for these educational retreats and the Island’s intended hotels and recreational uses, including spas, a marina and restaurants, are very high.

The Culinary Institute of America has expressed interest in offering its Continuing Education courses on Governors Island. The CIA is based in Hyde Park, New York, in a converted monastery on the Hudson River, and has a second campus in Napa Valley, located in a picturesque, converted vineyard. Students service five upscale restaurants at the Hyde Park campus. It is the only culinary institution that offers a four-year Bachelor’s degree alongside its professional training courses, custom

programs for institutional operations and continuing education classes. The CIA has just begun a certification program in 2004 that hopes to set industry standards among employer institutions and to differentiate its offerings from other less serious cooking schools, which number more than 500 in the US. The CIA’s management has put great efforts towards this in hopes of strengthening its presence and leadership around the world.

The success of the Institute’s continuing education courses has far exceeded capacity of the kitchen space. The school’s week long, intensive “Boot Camp” courses sell out weeks in advance, as do the weekend adult education courses, which are only offered in the spring and fall. Boot camp classes can accommodate 16 students and cost \$1,800 per week. The weekend courses have 30 kitchens at their disposal and bring 450 people per day to the campus. Marketing is minimal due to the full occupancy of the school’s kitchens throughout the year and each day of the week.

Twelve rooms on campus are reserved for continuing education students, however, most stay in a Bed and Breakfast or less expensive hotels in the area. The courses attract individuals from nearby metropolitan regions in Boston and New York, and far-reaching states such as California and Texas. The New York City market, in particular, is a very large source for the continuing education courses. The school is convinced that a large, untapped market of food enthusiasts would be well served by weekend and full week courses in Manhattan. The food enthusiast is a non-professional cook who would like to spend the time and money with high-rated professional chefs to improve their at-home skills.

A second and larger market opportunity should be explored with the Culinary Institute or another culinary program of equal caliber. Ongoing professional chef training is the bulk of the culinary institute business and includes semester-long courses and certification classes. Dedicated chefs use vacation time and spend \$850 per week plus hotel expenses, often not reimbursed by their employers, to improve their skills in certification courses. Corporations are another professional source that is actively targeted by the CIA. Custom courses are designed for companies such as Aramark, the US Navy and Marriott Hotels, to train chefs and line professionals in specific techniques used by the company. Custom courses are scheduled around the standards school use of kitchens and sometimes in the corporations’ locations, and are very profitable for the Institute. The school is actively building its relationships with outside corporations to strengthen the custom arm of its business.

### **Market Opportunity**

More than 10,000 students attend the school every year. The CIA teaches 2,200 full-time students at a time on its campus, with 42 kitchens dedicated the main program. Ongoing professional education certificate and other courses attract 50 to 150 students per week and range in price from \$850 to \$1,800. The continuing education program receives 450 food enthusiast trainees each of the 14 Saturdays that it is open, for a total of 6,300. These students pay \$160 per day and \$250 for a two-day course, usually opting to stay at a nice hotel and eat two dinners at the school’s leading restaurants.

Initial interest from the CIA in Governors Island is centered on the Continuing Education program for

its proximity to the city and its separation from the school's more academic and professional programs. Some concern of cannibalization of the custom programs for corporations has been raised. The size of the continuing education market, and its ability to pay for capital improvements, including kitchen build outs, to the existing buildings on the Island, are uncertain. At this point, the school would be very comfortable renting kitchens for the use of its instruction.

What is very clear from early conversations is that the pricing and capacity of the continuing education is missing the New York City potential. Pricing is too high for local Hyde Park and surrounding residents at \$160/day, however, the school feels it could charge much more for New Yorkers. Students are typically 45 years or older and earn well above \$150,000. The demographic is surprisingly skewed 60%-40% male-female.

Though further analysis into cooking class demand is needed, our early understanding is that approximately 10 to 15 kitchens and at least one demonstration kitchen with a theater and studio-ready capabilities would be a strong market use on the Island. For standard classes, 150 to 200 students would be expected daily. Special events could draw 300 at a time. If a more intensive program that caters to corporate or ongoing professional use is pursued, dorm rooms would also be a key and profitable component to the offering.

An overview of CIA courses at the Hyde Park Campus is shown in Exhibit IX-1.

### **Student Housing**

There is a great lack of housing for students in New York City. Currently, there are approximately 35,000 dorm-room beds for New York's 233,000 full and part time students in Manhattan and Brooklyn (See Exhibit IX-2). This translates to a student renter population in the two boroughs of almost 200,000 people. A very small 1% capture of that demand would yield 2,000 renters annually at very sustainable rental rates given the price points in Lower Manhattan today.

The student dorm option faces challenges for being the only residential activity on the Island. Other than overnight hotel guests and conference center attendees, it could be an isolated living experience for nine months. We have assessed the transportation concerns of getting to and from the Island regularly and consider them a concern for most college-age students. We would need to measure the depth of demand for a graduate student population who would prefer quieter environment of the Island to ease of access. If demand is found, student dorms present a very feasible opportunity to bring a steady and paying population to the Island.

### **Next Steps**

The need for Governors Island to be a self-sustaining entity dictates that the educational uses be developed in conjunction with private sector initiatives. The opportunities and development requirements are unique for each educational initiative – from sailing and environmental education to world leadership – and cannot be assessed with any particular goals in mind. As we

interview potential partnering institutions, the strengths and challenges associated with any one of these efforts will become clearer.

