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Capital ideas

Think tank shares insights for investors

HMM/JEFF HIGLEY

Lodging Industry Investment Council members C.A. Anderson (left) and Larry Shupnick discuss the flow of money into the hotel industry.

By Jeff Higley
EDITOR-IN-CHIEF

PHOENIX—The glut of capital ready to be invested in hotels as the lodging industry slowly begins to steady itself after more than two years of underperforming is downright scary—but welcome—to some members of the Lodging Industry Investment Council.

The uncertainty about the progress of the recovery was on the minds of LIIC members as they gathered for two HOTEL & MOTEL MANAGEMENT-sponsored roundtables held at The Arizona Biltmore Resort & Spa in conjunction with The Lodging Conference.

The main concern for some LIIC members is a dramatic increase of available asset prices that could cause problems with future valuation processes.

"The scary thing I see is the markets turning, and there's going to be some assets released to the market," said Glyn Aeppel, executive v.p., business development for Le Meridien Americas. "Someone was quoted that there's $4 billion ready to enter the hotel market, so you have the new players that are saying 'Look at my yields. Hotels look good. They've been devastated because of Sept. 11, war, etc. Maybe that's the direction to go.' If you look at all the sophisticated hotel investors, there's a chunk of money

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there. You have sophisticated money, unsophisticated money and a few deals. That is a recipe for disaster."

Mike DeNicola, executive v.p. and chief investment officer for FelCor Lodging Trust, said the investors with money waiting to acquire hotels might be a good thing during the short term for sellers because they could increase prices.

"There's a lot of equity coming to the market that doesn't have a depth of experience in our industry," DeNicola said. "As in past recovery times, those typically come into our industry now, which pushes the pricing a little bit because they're willing to pay maybe more than those who have too much experience. Sometimes knowing too much hurts you in getting a deal done."

Mike Cahill, president of Hospitality Real Estate Counselors and one of LIIC's chairmen, said there's also going to be an opportunity for cash flow to achieve greater levels than people anticipate.

"I don't think you can underwrite honestly where some of the cash flow will be six years from now," Cahill said. "We're still looking at hotels that were doing maybe $5 million cash flow four or five years ago, and now they're doing $2.5 million. ... I guarantee it's going to come back and be even greater. ... Call me a little optimistic, but a lot of people who buy now are going to do very well in 2006 or 2007 when they exit."

HMM/JEFF HIGLEY

Rich Conti of Boykin Lodging discusses current trends in the industry as Mike Cahill (left), Jim Butler and Glyn Aeppel look on.

Many LIIC members said they believe having so much money coming into the lodging industry from nontraditional sources, such as investment funds, is good.

"It creates opportunity for people," DeNicola said. "It's a recognition that our industry has a substantive value beyond just the stuff we went to school for and like being in it. When you see sophisticated investors raising money to come into this industry, it's positive for the industry. The more we can help those investors be successful with our industry, then the more opportunities that creates for all of us."

Some members said the industry veterans must proceed with caution and not be too overzealous when, and if, a buying frenzy occurs.

"It's good for the industry, but there's an opportunity window," said Larry Shupnick, senior v.p. of development and acquisitions for MeriStar Hospitality Corp. "How long will it last, and how long will that reasonable money be available for the hospitality industry before it turns to another form of real-estate?"

Jeff McKee, senior v.p. of hospitality for GE Franchise Finance and a LIIC member, said it's important for the lending community to maintain the high standards that it has followed for the past eight years.

"From where I sit as a lender, there's a lot of equity coming in, but we're only going to look at the experienced hotel people," McKee said. "We don't want a lot of people who don't understand the industry coming in and building whatever they want. From a lending perspective, I won't allow that to happen."

Regardless of lenders' philosophies, many LIIC members said they anticipate a large number of hotel assets changing ownership.

"It's getting to the point where [companies] have seen the cycle come and go and now they're seeing an improvement in the cycle," said C.A. Anderson, senior v.p. of development and acquisitions for Interstate Hotels & Resorts. "If you don't want to be in the hotel business, now is probably a good time to get out. Now, or in the next 18 months, you have one asset and say 'I rode the curve once and now I might be at the bottom again.' There's a lot of that going on."

"We do a lot of work with lenders—not only with special servicers, but lenders who are actually getting quite tired of restructuring," said Rick George, principal with HREC Investment Advisors. "We're going to see a groundswell of significant assets in major markets that are going to become available at discounted prices, based on current numbers. It's going to be a very fun time in the next 12 to 24 months."

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LIIC's mission

The Lodging Industry Investment Council (*www.liic.ws*) is an industry think tank that meets three times annually to discuss hotel finance, development and operations issues. Its 70 members include consultants, lenders, operators, developers, educators and legal professionals.

LIIC
LODGING INDUSTRY INVESTMENT COUNCIL

Co-chairmen for LIIC are Mike Cahill of Hospitality Real Estate Counselors and Sean Hennessey of PricewaterhouseCoopers. Vice chairman is Jim Butler of Jeffer, Mangels, Butler & Marmaro.