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Turnaround hinges on RevPAR, bookings increases



H&M/JOHN WALSH

Jim Butler of Jeffer Mangels Butler & Marmaro and Mike Cahill of Hospitality Real Estate Counselors discuss the industry's turnaround at a LIIC roundtable that was held in conjunction with the New York University investment conference.

By John P. Walsh
MANAGING EDITOR

NEW YORK—
Members of the
Lodging Industry
Investment Council,

who participated in two HOTEL & MOTEL MANAGEMENT-sponsored roundtables held in conjunction with the 25th New York University International Hospitality Industry Investment Conference in June, said they believe a turnaround for the lodging industry can be predicted by watching the trends of revenue per available room and advance bookings.

Rich Conti, president and c.o.o. of Boykin Lodging Co., said the first quarter of this year was a tough quarter, and April probably was the worst month in the lodging industry he has ever seen.

"We're hoping by the fourth
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Industry's turnaround

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quarter of this year we start to see year-over-year flatness or year-over-year gains," he said. "That's just a guess at this point, because it is that foggy. You see some small lights of the economy turning on, almost like it was in 1991-'92. The only problem is ... we can't estimate the terrorism factor. We could be like we were in '91-'92, looking for a very robust three to five years. On the other hand, in

'91-'92, because there was no terrorism factor, I don't know that we can re-predict that that same robust event is going to happen."

Jim Merkel, managing director of RockBridge Capital LLC, agreed that April was a difficult month.

"The borrower is telling you, 'We're through the war [and] there's pent-up demand.' But now they're not seeing that come back. You have the slide in April. It was

the war last month. It was Afghanistan six months ago. We don't know what's going to happen in the next few months or six months out. There could be another war. We're finding it hard to pin down what and why to underwrite."

Mike Cahill, president of Hospitality Real Estate Counselors, said there is the potential for real problems in the future.

"Everything's extended longer than we thought it would in terms of the turnaround," Cahill said. "Everyone knows it's going to turn



H&MM/JOHN WALSH

Jeff McKee [left] of GE Franchise Finance and **John Arabia** of Green Street Advisors listen to other members of the LIIC roundtable speak about the state of the lodging industry.

around, but the question is 'how do you underwrite 2003 and 2004?' Obviously, based on some prices people are paying, investors are assuming '04 is going to be an uptick.

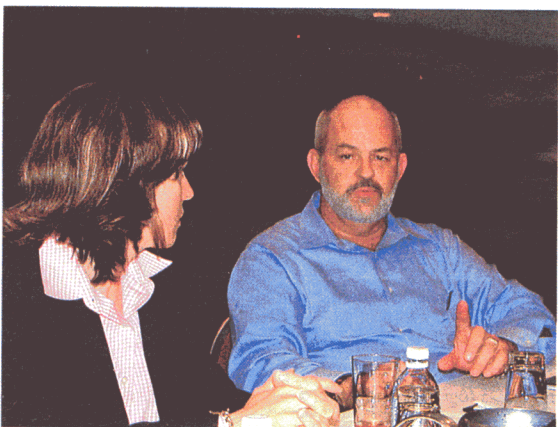
"But what if '04 is a little slow, and they have trouble making debt service, especially on these variable-rate loans? A lot of our clients are being carried by low debt service right now. If we weren't in a low-interest-rate environment, there'd be a lot more trouble out there."

Frank Nardoza, chairman and c.e.o. of REH Capital Partners

Indicating a turnaround

The following are indicators that need to occur to signify that the lodging industry has turned around from the recession, according to Lodging Industry Investment Council members.

- Two consecutive quarters of revenue-per-available-room growth above 2 percent, with evident increases in weekday and weekend demand across the majority of lodging segments.
- When the booking pace for groups exceeds last years, for three or four months.
- Positive growth in corporate profits without increases in unemployment.
- RevPAR demonstrates quarter-over-quarter growth across all segments and this growth coincides with consecutive quarters of positive economic indicators.
- Four positive quarters of gross-domestic-product growth above 3 percent along with improved employment numbers that correlate to the GDP growth.



H&M/JOHN WALSH

Robert Massey of InterContinental Hotels Group, formerly Six Continents Hotels, talks about the company's strategy of distributing rooms inventory via the Internet as Cheryl Boyer of PricewaterhouseCoopers looks on.

LLC, said the industry needs to experience two consecutive quarters of revenue-per-available-room increases of at least 2 percent to 3 percent per quarter to signify a turnaround.

"Then I'll feel we're creating some level of a cushion, and we have some sustained movement, as opposed to the flash in the pan one month we're good, the next

"Saturday night has become the No. 1 occupancy night in New York City. That's unheard of."

— CHERYL BOYER

month we're bad," Nardozza said.

"We're trying to underwrite our deals on the basis of lesser concern about the downturn in the economy today," he said. "We're just trying to make our deals on the buy side. We've been buying foreclosures, and buying at deep discount. ... We're looking at pro-formas and not paying much attention to the trailing 12 [months], particularly in light of the war."

Jim Butler, a partner with the

law firm Jeffer Mangels Butler & Marmaro, said that in early May, some operators reported that they were beginning to see more activity and things were picking up.

"You'll get the increase in RevPAR only when you get the sustained increase in occupancy and the predatory pricing and slashing of hotel rates abates a little," Butler said. "Whether it's one quarter or two quarters or a year, the improvement in RevPAR is going to mean the occupancy has come back, [and] there's enough demand that rates aren't being slashed in a predatory fashion."

Conti said buyers are more sophisticated than they were 10 years ago.

"We bought properties [10 years ago] and said the rising tide will take care of us," he said. "This time around, the sophisticated buyers are looking at opportunities, are finding the markets, tracking the markets and then finding product in those markets. That's

Coming in our August issue:

LIIC members discuss the industry's resiliency, good investments and the impact the Internet has on room distribution.

how you convince the lender and show them it's the market that's going to turn, not that I can do it better than you. That philosophy I don't think can pull up enough of the cash flows that are so depressed today. It's both expertise and market."

Jeff Davis, president of HREC Investment Advisors, said he's seeing a lot of income averaging over a period of time from investors.

"If you look at certain markets, you look at 2000-2001 as an aberration," Davis said. "You have to go back to '97-'98 to get a fair representation of what a market is and average it out. Then at least you're protecting to your down side, and that's what most investors and lenders are underwriting to right now."

Cheryl Boyer, a financial advisor for PricewaterhouseCoopers, said the meetings and group segments held up somewhat last year, but even that segment declined. Boyer said New York is a good example.

"Saturday night has become the No. 1 occupancy night in New

LIIC's mission

The Lodging Industry Investment Council 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.

Co-chairmen for LIIC are Mike Cahill of Denver-based Hospitality Real Estate Counselors and Sean Hennessey of PricewaterhouseCoopers' New York office. Vice chairman is Jim Butler of Jeffer, Mangels, Butler & Marmaro, a Los Angeles-based law firm. LIIC's Web site is www.liic.ws.



York City," she said. "That's unheard of. There's been such a strong shift in demand that the leisure traveler has come in at these low, discounted rates, and they're being drawn into the city. We should be grateful for that, and that's bolstering occupancy. But if you take a look at the rates, if you don't have the business travelers during the mid-week period, it's going to take a while before you can shift that equation."

Boyer said larger companies have learned that maybe they can

get business done with fewer people on the road.

"They're sending fewer people out," she said. "They're scheduling fewer meetings, and the level of travel overall has come down. Part of it is the demand side. If you take a look at some of these major markets, you look at Monday, Tuesday, Wednesday nights, which is when you expect everyone to be full and start to push the rates a little bit, [but] there's not enough demand to push the rates."

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Jim Merkel of RockBridge Capital and Frank Nardozza of REH Capital Partners LLC discuss the financial aspects that are affecting the hotel transactions market.