Hotel Recovery in 2011 and Beyond?

The U.S. is emerging from one of the worst economic downturns in its history. As demand accelerates, the lodging sector is entering a strong recovery period. Sidelined investors debating their timing would do well to heed Warren Buffett, "….be fearful when others are greedy and be greedy only when others are fearful." In other words - If an investor waits to invest when everyone else is…it's probably too late. Investors making new acquisitions now can benefit from the rising asset values and the recovering capital markets.

During the period of 1990 to 2009, hotels averaged a total return of 8.4%. According to the National Council of Real Estate Investment Fiduciaries, this is the highest return among all property sectors. While the industry isn't at boom, indicators point to recovery for the hotel market.

Historically, hotel revenues have correlated with gross domestic product. GDP increased 3.1% in the fourth quarter last year and increase another 1.8% in the first quarter 2011. The Fed is forecasting 3.4 to 3.9% continued growth for the year. Specific to the hotel industry, Smith Travel Research (STR) is forecasting continued growth in terms of occupancy. Last year's total occupancy was reported to be 57.6%. STR predicts 58.5% for 2011 and 59.5% in 2012.

Revenue growth will come from a relatively equal contribution of increases in occupancy and ADR. A hotel lease is short and allows for room rates to be adjusted quickly as room demand continues to climb. PKF-Hospitality Research is forecasting that the average hotel in the U.S. will be able to increase their total revenue by 6.8% for the year. The key will be controlling costs. It is also important to note that hotel supply is declining - according to Lodging Econometrics' 2011 U.S. Real Estate Trends Outlook Report, new projects are at a low, not seen since 2004 and will remain that way into 2012.

For the balance of this year, investors should look to bank-owned and note purchases to obtain hotel assets at a significant discount. If a hotel asset can be purchased for 20-30% discount to replacement cost, it's better to buy than to build. Banks are struggling to move underperforming assets off their balance sheets. Most sales in the economy sector are bank driven and selling at a discount to the former debt. In many cases there is financing available from the selling bank. Note purchases (loan to own) are also a viable option, but only for the sophisticated buyer. There are many hidden traps to purchasing a note to eventually own the asset. In either case, investors are encouraged to take advantage of the benefit of counsel. A strong franchisor like Vantage and seasoned broker can guide you successfully through the process.

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