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Hospitality forecast remains cloudy but hotel business is in a superior position

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As Labor Day weekend comes to an end, we must say goodbye to the carefree summer days we all treasure. Like many others, I enjoyed the sun, surf and sand with family and friends while putting the challenges of the hotel business in the rearview mirror and focusing on future opportunities.

Recently, when my daughter resisted my request to get up for school, I reminded her that summer vacation was over and both of us needed to get ready for the day. Begrudgingly, she peeled herself out of bed and began preparing for her first day of first grade with simultaneous nervousness and excitement. Coincidently, I drove to work that same day feeling positive about the future, yet apprehensive about the remainder of 2011.

The hotel industry continues its long road back from historic revenue per available room (RevPar) drops and net operating losses (NOI) in 2009. As you may recall, according to Smith Travel Research (STR), RevPar dropped 16.9% in 2009, improved over 10% in 2010 and continued to trend positive through July 2011. Similar to other industry recoveries, occupancy improved first and was eventually followed by average daily rate (ADR) as room demand improved. That said, in July of this year STR reported over 105,000 room nights sold nationwide, both a new record and a 3.6% increase over July 2010.

Although STR reported a record July, no one was in the mood to celebrate as macro-economic indicators at home and abroad deteriorated causing significant stock losses and talk of a second recession, or "double dip" as July turned to August. As a result, hotel analysts now fear companies will start pulling back on business travel causing RevPar to decrease in the last quarter of 2011 and into 2012. If those fears materialize, hotel owners face the prospect of RevPar decreases and diminishing profits through the end of this year and into 2012. Obviously, this is unwelcome news to owners and operators eager to reap the economic rewards of three consecutive years of RevPar improvement.

The possibility of a prolonged, or "double dip" recession would impair both hotel values and transaction activity. According to STR Analytics, hotel transactions were up over 80% through July 2011 as compared to July 2010. During that time period, RevPar and NOI increased, investment capital was deployed and debt re-entered the marketplace allowing buyers to underwrite leveraged internal rates of return.

The buyers responsible for fueling transaction activity and increasing values are real estate investment trusts (REITS) and private hotel companies, along with their institutional equity partners. Moving forward, public REITS impaired by declining stock prices will face liquidity issues, while lenders could resist participating in hotel deals. Without REITS buying hotels, sellers may not find suitable partners willing or able to purchase hotels.

The uncertainty of the economic outlook continues to blur hospitality forecasting. The cyclical nature of the business continues to test the resolve of owner/operators, lenders and capital partners. As in all real estate investments, when to buy, how long to hold and when to sell is tantamount to meeting or exceeding return on investment hurdles. Based upon prices paid for hotel through July 2011, it appears many sellers successfully weathered the recession and sold at a beneficial time.

Although the industry continues to show improvement over the dark days of 2009, it appears hotels owners are not out of the woods yet. In the foreseeable future, hotel owners could be facing diminishing NOI, reduced values and lender issues including defaults and maturities. Investors armed with capital would be in position to fill the void left by REITS and buy into a market demanding higher capitalization rates and lower values.

When we look at the fall of 2008, and compare it to the fall of 2011, we recognize the economic forecast is cloudy but we believe the hotel business is in a superior position and that the fundamentals remain strong. Although cyclical, and at times volatile, our experience proves that making hotel investments in good locations, controlling costs, delivering world-class customer service and exceptional price value generates above average investment returns. When approached properly, the hotel business is neither a "day at the beach" nor a gut wrenching first day of school - it probably falls somewhere in the middle.

David Roedel is partner at Roedel Companies, LLC. As a partner at Roedel Companies, he is accountable for meeting or exceeding the companies' annual and three year strategic plans. Specifically, he is responsible for real estate development including hotel acquisitions and development and implementing a marketing and public relations strategy which supports its growth and revenue goals.