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New England Hotel Realty and Lodging Econometrics Hotel Construction Pipeline

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In our Q4 report to the lodging industry, New England Hotel Realty (NEHR) and its research division, Lodging Econometrics, stated that the U.S. Hotel Construction Pipeline totaled 5,358 projects with 686,516 guestrooms at the end of 2008. This represents a 9% decline in the number of projects and a 13% decline in the number of rooms from the cyclical peak in Q2 2008. The pipeline is declining at an accelerated pace, having lost nearly 100,000 rooms over the past two quarters. This downward trend is expected to continue through 2010.

With the realization that the national economic and banking crises are going to be with us a bit longer, consumer and business sentiment has dampened. Guestroom demand has turned negative, resulting in declines in occupancy and RevPar, and putting considerable pressure on room rates. This is causing many developers to retreat to the sidelines to wait for a bottoming in economic conditions and a thaw in the lending environment. As a result, project cancellations and postponements are at trend-line highs, while new project announcements are significantly below previously set cyclical peaks.

New openings in Q4 2008 exceeded expectations, with 367 hotels/43,845 guestrooms coming online, the highest quarterly total since Q2 1999. This brings 2008's total new openings to 1,330 hotels/153,411 guestrooms, a gross growth rate of 3.2%. New construction projects are coming out of the pipeline at an accelerating pace, as there is less pressure on the availability and cost of building materials and labor crews, leading developers to complete projects on schedule or even ahead of schedule.

New openings are expected to reach a cyclical high in the next two years, as projects that were able to secure financing before lending closed down come online. The speed with which under construction projects are moving to completion has ramped up now that logistical pressures have eased. As a result, NEHR and LE have adjusted their forecast higher, as it is now likely that new openings will be greater than initially expected. Our revised forecast for 2009 now calls for 1,431 hotels/165,927 rooms to open, a gross growth rate of 3.4%. In 2010, an additional 1,370 hotels/160,885 rooms will come online, a gross growth rate of 3.2%. Net growth rates will end approximately .2% lower after hotel closings and other removals from current supply are compiled. Our forecast for new hotel openings is based on current development trends as of the end of Q4 2008. The forecast does not account for other unforeseen changes in economic or lodging operating fundamentals that would alter these trends going forward.

New England Hotel Construction Pipeline

At the end of 2008, New England's Hotel Construction Pipeline consisted of 162 projects with 20,259 guestrooms (Chart 1). This accounts for about 3% of total projects and 3% of total guestrooms in the national pipeline. Compared to the end of 2007, there are 3 fewer projects and

470 fewer rooms in the New England Pipeline. NEHR forecasts that 32 hotels with 3,520 new guestrooms will open in '09 for a gross growth rate of 1.6%, which is prior to any removals of hotel rooms from the current census of open and operating hotels. For '10, NEHR forecasts that 26 hotels with 2,284 new guestrooms will open in New England. Given the high number of projects scheduled to start construction in the next 12 months and in early planning, the supply side forecast for 2011 and beyond is correspondingly significant. However, given the current economic climate and associated financing issues, some of these projects are likely to be delayed or postponed.

The forecast for individual states in New England reveals more details. Forecasted new hotel openings in New England for '09 and '10 combined show the largest growth, as you might expect, in the region's two most populous states, Conn. and Mass. 15 new hotel openings with 1,687 new rooms are expected in Conn., while 16 new hotels and 1,585 new rooms are anticipated in Mass. During the same period, Maine and N.H. are expected to have 11 new hotels each, with 1,171 and 969 new rooms, respectively.

What does it mean for the region? It means that over the next 24 months or so, there will be a relatively modest supply increase in New England. Some existing properties will feel the effect of new supply more than others, depending on each specific location.

New England Lodging Transactions and Values

The number of lodging transactions and corresponding values in New England had seen a steady increase from 2003 through 2006. However, at the end of 2007, there were 8 fewer transactions and the average price per room had declined almost \$14,000 compared to 2006. (Chart 2)

In 2008, the decline continued, with the number of transactions falling to 53 and the average price per room settling in at just over \$60,000 - almost half of the 2007 average price per room.

Because of the economy, slowing demand and the scarcity of financing for hotel deals greater than \$15 million, many investors went to the sidelines temporarily, especially in the third and fourth quarter of 2008.

However, over the past 30 days or so, new equity groups with significant capital resources have started to form and are looking for hotels and owners interested in pruning their portfolios. We expect this trend to continue into 2009. With any luck, when we write this article in 2010, we will be discussing healthier transaction volumes.

Some larger significant transactions that occurred in 2008 were: the Residence Inn, Marlborough, Mass. at \$180,357 per room; SpringHill Suites, West Warwick, R.I. at \$103,670 per room; Hampton Inn & Suites, Westford, Mass. at \$138,636 per room; and the Doubletree Hotel, Norwalk, Conn. at \$109,434 per room.

New England Hotel Realty is the highest volume hospitality real estate advisory and brokerage firm in the Northeast, providing acquisition, disposition, consulting and market research services to the lodging real estate and lending industries. Since 1977, the NEHR team has provided quality investment opportunities and seller representation in hundreds of hotel transactions. We are frequently called upon as advisors to assist in the analysis of a client's lodging investments.

About this month's author:

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NEHR provides acquisition, disposition, consulting, and market research services to the lodging real

estate industry since 1977. NEHR is highly skilled in the sale of lender-owned and distressed hotels. Ford is responsible for overseeing and directing the company's brokerage department, working with new clients, and servicing the disposition and acquisition needs of existing clients. He specializes in the sale of full and limited service hotels and portfolio sales.

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