

# US 2009 lodging report



# Introduction



Dear Colleagues,

We are pleased to present the 2009 edition of Ernst & Young's *US Lodging Report*. In this year's report, we review the performance of lodging markets and segments throughout the US. As important, we focus on the global events and trends of the past year that are likely to affect the hospitality industry in 2009 and beyond. These include the turbulent global economy and financial markets, an emphasis on cost control, an increased focus on green technology and the increasing role of technology to promote the brand, generate customer demand and improve the bottom line.

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Ernst & Young's Hospitality Services professionals provide developers, lenders, owners and operators with an array of advisory services. Please feel free to contact us if we may be of service.

Sincerely,

A handwritten signature in black ink that reads "Michael Fishbin".

Michael Fishbin  
National Director  
Hospitality & Leisure  
Ernst & Young LLP

# US 2009 lodging report

1	<b>Top 10 thoughts</b>
11	<b>Global and US overview</b>
12	Global perspectives
14	US industry overview
21	<b>Chain segments</b>
35	<b>Market overviews</b>
36	Atlanta
40	Boston
44	Chicago
48	Dallas
52	Fort Lauderdale
56	Hawaii
62	Las Vegas
68	Los Angeles
74	Manhattan
80	Miami
84	New Orleans
88	Orlando
92	Philadelphia
96	Phoenix
100	San Diego
104	San Francisco
110	Washington, D.C.
115	<b>Hospitality contacts</b>





## Top 10 thoughts



# 1 Credit crunch: capital waiting on the sidelines

The credit crunch, which began in the US in mid-2007, has gradually turned into a global economic crisis. While the US and many European governments are considering alternative restructuring options for their financial systems, the hospitality industry is being significantly impacted by the economic slowdown and lack of capital.

The scarcity of capital has frozen the transaction market and is delaying new lodging supply. Many lenders are waiting on the sidelines or extending loans only to high-quality, cash-flowing properties in strong markets, albeit at comparatively higher interest rates, stricter loan covenants, lower loan-to-value ratios and increased debt-service coverage ratios relative to the financing terms of the real estate boom between 2004 and 2007. As an example, some lenders' interest rates for mezzanine loans are as high as 20.0%. The majority of private equity and sovereign wealth funds, which were once viewed as alternative sources of capital, are waiting for further declines in asset prices or are investing domestically in debt instruments rather than buying assets.

Given the reduction in liquidity in the market, revised downward RevPAR expectations, a virtually non-existent transaction market and the perceived risk premium, there is a wide gap between sellers' and buyers' expectations. This difference has resulted in fewer assets changing hands in the

short-term. Hotel values are anticipated to erode as capitalization rates increase, with public real estate investment trust (REIT) stocks possibly indicating what lies ahead for devaluation in the private sector. If fundamentals continue to deteriorate, many highly levered hotels could find it difficult to meet their debt service obligations, resulting in some lenders facing the risk of balloon defaults on construction and interim loans. Currently, some lenders are extending a "blanket" moratorium on real estate loans to financially troubled borrowers.

It is difficult to predict when the financial markets will rebound, although

**"Almost 60.0% of the investors polled are defining themselves as net buyers to take advantage of fire-sale prices of commercial real estate."**

the potential settling of the first commercial real estate bankruptcy cases through the first half of 2009 may provide a good indication of bottom pricing. However, what appears certain is that cash-rich opportunistic investors will be hunting for hotel deals at discounted or distressed prices as late buyers during the previous lodging cycle, who may no longer have the wherewithal to hold onto their assets, may be forced to sell or inject additional

equity from third-party investors. According to Ernst & Young and Globest. Com's "Reality Check Survey" of nearly 3,000 companies concerning the credit crisis, conducted in October 2008, "almost 60.0% of the investors polled are defining themselves as net buyers to take advantage of fire-sale prices of commercial real estate." In this new ownership cycle, private equity and institutional investors – sovereign wealth and endowment funds – along with traditional commercial banks, are likely to be the prime sources of capital for hotel investors following the collapse of the majority of large investment

banks. Numerous private equity firms have raised an estimated US\$400 billion for distressed debt investments, which will most likely encounter a new era of stringent underwriting standards requiring thorough financial due diligence with the assistance of independent subject matter experts and trusted advisors.

# 2

## Enterprise excellence: focus on cost containment and the bottom line

As market conditions weaken, hotel owners and operators are concentrating on improving efficiencies, productivity and cost savings in both capital and operating costs at the corporate and property level. Owners are increasingly concentrating on overhead cost reduction, asset utilization yields, operations, construction-cost efficiencies and limited capital improvements. Branding has also become a major focus for hotel owners and operators, resulting in increased marketing and procurement effectiveness, particularly among brand conglomerates that leverage their extensive network of owned and/or managed (or franchised) properties.


Increasing the efficiency and integration of the corporate office structure is essential to controlling expenses. Aligning the corporate accounting department with property-level accounting can eliminate the chance of duplicating efforts. Technology has come to the forefront, with companies using document management and other management systems. Additionally, business functions, such as legal, purchasing and accounts payable, are increasingly being outsourced to third parties.

Efficiency can be improved by allowing the owner and operator to work more closely together, effectively bridging the gap between the two parties. Value can be added by thinking about revenue management, driving ancillary revenue in areas such as audio/visual, parking

and leasing, redeveloping existing space, repositioning to better serve the market and analyzing property-level budgets and forecasts. The relaxation of certain brand standards is also anticipated, with a strong emphasis on flexible service levels to support each hotel operation in consideration of local market demands.

As a result of the uncertain economic conditions and the decrease in demand forecast for the next year, owners are acting quickly to increase profitability at the asset level. Current labor agreements limit the opportunities to reduce payroll costs, so owners will require more creative measures to reduce operational expenses. Some of the areas in which they are achieving the most return on their investment are implementing energy efficiency programs, outsourcing business functions and monitoring capital expenditures. Growth in asset management services and operational advisory is expected in 2009 as hotel owners approach asset managers to align hotel operations with the current stage of the investment cycle. More and more often, management companies are seeking independent reviews that shed light on industry best practices from both an asset management and corporate management strategy perspective.





## 3 Technology: leveraging brand name and the internet

As the industry enters a period of economic slowdown, both branded and independent hotels will be utilizing the most up-to-date technology to capture reservations directly through their own distribution channels. At the same time, hotel owners have begun to acknowledge the impact of third-party, web-based distribution channels.

The wealth of information available to consumers makes it easier for them to research prospective hotels before booking. According to the *2008 National Leisure Travel Monitor*, which summarizes a survey of 2,100 US leisure travelers, among leisure travelers who have used internet travel or hotel websites to make a hotel reservation, approximately three-quarters have booked a hotel or resort online – a significantly higher proportion than noted in 2007.<sup>1</sup> As a result, independent hotels may have a greater opportunity to capture their share of the online market; their performance will be the true test of the equalizing power of the web during this downturn. In this regard, moving forward, so-called search engines such as Sidestep and Kayak may streamline the relationship between hotels and potential guests since these channels operate on advertisement-based models that eliminate the need for the commission-based models of third-party wholesale travel websites.

Consumers are also using word-of-mouth recommendations to make travel decisions. Such recommendations are circulating in a virtual medium, through

the use of blogs, social networking sites and travel websites like TripAdvisor, Yapta, Travel Muse and Concierge. The user-generated content is important to travelers and has a strong influence on booking decisions. Before booking a hotel stay, potential guests use these online sources to research what others have to say about their stay, in terms of both the level of service and the accommodations. According to a Google study, 33.0% of travel website readers changed their travel plans based on these reviews. Hotel owners are therefore implementing strategies to manage their online reputations and, ultimately, maintain their brand integrity.

At this turbulent time for the hotel industry, companies are leveraging their brand names and technology to differentiate themselves. Brand presence in the virtual space will likely become an increasingly important decision-making factor for hotel owners when selecting lodging operators for their projects.

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<sup>1</sup> 2008 National Leisure Travel Monitor, The Ypartnership/Yankelovich, Inc.

# 4

## Hospitality mixed-use: subject to adjustment

In the past, many hotel development sites were developed by underwriting projects with residential components supported by the then-burgeoning residential market. However, with investors' market confidence waning and credit conditions tightening, there was a shift from this trend as several hotel and condominium mixed-use developments were put on hold at the end of 2008. In the current economic environment, the emerging limited-service "lifestyle" brands may offer alternatives aligned with developments containing office and rental apartments, which better suit the changing market fundamentals. Limited-service lifestyle brands are expected to be more prevalent in the next two to three years due to their offering a less-costly hotel product alternative.

Recently, hotels have received growing attention as an instrument of urban redevelopment since they provide 24-hour activity to an area in conjunction with residential and commercial uses, particularly retail. Moreover, a hotel's opening celebrations and marketing campaigns can increase a district's exposure to the media, as was demonstrated by the L.A. Live and Dallas Victory developments, both anchored by hotels. A hotel component adds multiple benefits, providing the strength of its brand to the other components, as well as providing support amenities. Revenue streams benefit as the hotel caters to users of all asset types, and some costs, such as common area maintenance,

can be shared across components. Similarly, hotels can play significant roles in the redevelopment or restoration of a landmark.

In resort developments, frequently supported by second-home residential sales as well as hotel and recreational component revenue, second-home condominium sales have declined. This has resulted in the reworking of facilities programming. In order to identify market-supported uses, the various second-home alternative uses (such as condominium-hotels, fractionals and timeshares) should be matched separately to market fundamentals and then combined to model shared revenues and expenses. For many developments, the condominium-hotel component will be scaled back because of the structure's

meetings. Fractional ownership has a mixed outlook: it could be a trendsetter, given the value proposition of limited versus whole ownership, though high-priced fractions may see a weakening as both developers and buyers have difficulty in obtaining financing. Similarly, at its lower price point, timeshare product may be attractive to buyers. But the continued debt securitization challenges of developers may decrease the attractiveness of financing packages offered to end-users and therefore reduce timeshare's inclusion in mixed-use developments in the short term.

Given the current economic conditions, 2009 is anticipated to be a challenging year for residential sales, which may cause a reconfiguration of mixed-use developments currently in the planning

Recently, hotels have received growing attention as an instrument of urban redevelopment.

legal and operating challenges. This strategy was integrated into the St. Regis Bal Harbour, where condominium-hotel units amount to 16.0% of total guestroom inventory, providing a cash injection for the development while giving the hotel operator a dedicated inventory for booking groups and

process. Projects that better align uses or phase developments with current market fundamentals, however, may provide developers with previously unconsidered options.

# 5

## Financing: planning loan restructuring and modifications in a structured finance setting

According to the Mortgage Bankers Association (MBA), US\$16 billion of loans pooled into commercial mortgage-backed securities (CMBS) has matured in 2008 and another US\$19 billion will in 2009.<sup>2</sup> The market to refinance them, however, has essentially been eliminated, bringing concerns as to how these loans will be repaid. Given the current economic conditions, a significant number of loan modifications are anticipated in 2009.

Historically, most loan originators were balance-sheet lenders, which resulted in the alignment of expectations and interests of the special servicers and loan originators. As a result of CMBS and the introduction of AAA bondholders, junior bondholders, B-note holders and mezzanine lenders, however, special servicers are faced with the difficult, if not impossible, task of satisfying the desires of all interested parties when deciding how to proceed with loan modification. The special servicers' main responsibility is to manage loans in accordance with the servicing standard, "which requires administration and servicing of loans without giving preference or deference to other serviced loans, and with a view of ensuring timely loan payments and otherwise maximizing recovery amounts to bondholders taken as a collective whole."<sup>3</sup>

Due to the various positions in the priority of payments, some bondholders may be risk-averse while other bondholders (in a different position) may prefer a loan restructuring that



entails increased risk. Therefore, one party may prefer the special servicer to liquidate the asset while another party may prefer the special servicer to lower the interest rate or extend the term, all of which are options the special servicer has access to. However, special servicers are faced with an illiquid market – which may make foreclosure liquidations less feasible – as well as weak commercial real estate (CRE) fundamentals – which may mitigate the effectiveness of providing temporary relief to the borrower in the form of a lower interest rate or an increased amortization period.

Given the decreasing occupancy levels, decelerating average daily rate (ADR) growth and growing number of mortgage delinquencies in the CRE market, special servicers are likely to have a significant role in the future of the CRE market. Therefore, a complete understanding of the role of servicers with regard to the investor's specific position is considered to be a requisite for success during these turbulent times.

2 Rob Noeldechen, "Time for a Workout," *Global Real Estate Newsline*, Spring 2008.

3 Andrew Day, "Servicing With a Smile," *Morgan Stanley Global CMBS*, 17 November 2008.

# 6

## Globalization and decoupling: growth beyond the current economic cycle

During the past decade, one of the most prominent international economic developments has been globalization. However, more recently, and as turmoil has erupted in many financial markets, the term “decoupling” has come to the fore, referring to divergences in economic performance among regions. Although it has become clear that no region or industry is completely immune to the present financial crisis, it is anticipated that regions that have recently achieved above-average growth, such as Asia-Pacific, the Middle East and North Africa (MENA) and Latin America, may also exhibit stronger lodging fundamentals during the current slowdown. In particular, countries with large and rapidly growing domestic economies and population, combined with a relative scarcity of quality hotel inventory, present the best opportunities for hotel developers. This is evidenced by the development pipelines of major international hotel operators in these regions.

With three of the four fastest-growing destinations in the world, Asia-Pacific remains the international hotspot for global hotel developers. As of September 2008, Intercontinental Hotel Group (IHG) had 177 new properties in the regional pipeline<sup>4</sup> while Marriott International has plans to open 75 properties by 2012.<sup>5</sup> International operators are focusing their expansion primarily on upscale brands

in the hope of capturing demand from a growing wealthy domestic base and international, brand-sensitive travelers whereas local brands (and a few international players through joint venture agreements) are expected to stay focused on the budget segment catering to a growing middle-class base.<sup>6</sup>

In MENA, the increasing demand and lack of supply in recent years, especially in the United Arab Emirates (UAE), have captured the attention of many international hotel brands. Pending a recovery in global tourism, IHG views the next few years as an era of growth and diversification,<sup>7</sup> mainly in the UAE and Saudi Arabia, with a sustained focus on the company’s mid-scale Holiday Inn and Express brands. Marriott had 23 properties in the pipeline across the Middle East as of December 2008,<sup>8</sup> and Hilton Hotels had a development pipeline of 17 properties across MENA.<sup>9</sup> While the region has an established, traditional four- and five-star market, the branded budget market may present stronger opportunities, as may Islamic or Sharia-compliant hotels tailoring their services to Muslim visitors. Local brands that apply no-alcohol policies and respond to this regional trend include Shaza, Tamani and Flora.

Operators and investors see similar prospects for Latin America. Mid-scale,

business-oriented products are the fastest growing and the most needed as regional businesses join the global economy. Demand for mid-scale products can be seen in Courtyard by Marriott’s strong growth over the past five years,<sup>10</sup> as well as Hilton Hotels’ expansion plans around its Hilton Garden Inn and Hampton Inn brands.<sup>11</sup> Brazil is anticipated to be the main focus of expansion given its growing economy and exposure to the international travel market. Mexico and Central America are expected to continue to grow their stock of business-oriented hotels and mixed-use hotel communities, benefitting from their proximity to the US, baby-boomer demographics and a growing younger middle-class.

However well the tourism sector has held up in 2008, forecasts suggest that the situation will deteriorate over the next six to nine months.<sup>12</sup> This will provide challenges, but could also provide opportunities across geographies for lodging developments and increased competition among tourism destinations to tap into an increasingly diversified traveler base. Based on the strong growth of regional travel and an expanding middle-class population, markets such as China, India, Vietnam and Brazil are anticipated to be at the forefront of future growth.

4 IHG in Asia Pacific, Intercontinental Hotel Group, 30 September 2008.

5 Dominic Whiting, “Smiles turn to frowns as hoteliers face downturn,” Reuters, 17 October 2008.

6 Jason Leow, “Hoteliers Look to China – A Bright Spot Remains as Travel Business Wanes in Some Places,” *The Wall Street Journal*, 17 October 2008.

7 Tom Rowntree, Vice President, Sales & Marketing, Middle East & Africa, Intercontinental Hotel Group.

8 Nina Varghese, “Dubai hotels report 85% occupancy rate,” 30 December 2008, [www.zaywa.com](http://www.zaywa.com) accessed on 16 January 2008.

9 “Hilton launches innovative Middle East incentive program for conference and events bookers,” [www.zaywa.com](http://www.zaywa.com), accessed on 4 November 2008.

10 “The Latin American hotel sector – A dormant giant,” *Meridia Capital*, March 2008.

11 “Hilton Hotels Corporation Announces Major Expansion Plans to Quadruple its Caribbean and Latin America Portfolio,” *Business Wire*, 8 September 2008.

12 “UNTWO Sees Negative Growth for Tourism in 2009”, World Tourism Organization, 2 December 2008.

# 7

## Green building: going mainstream

Now a niche trend within the hotel industry, the recent green movement can be explained by the concerted efforts of various players, including governments, hotel companies, developers and investors, who realize the benefits of building green developments. Governments are requiring federal agencies to occupy green buildings and mandating that their employees travel green. Governments are also creating green tourism campaigns and environmental certifications for local hospitality businesses while offering tax credits and capital allowances for energy-saving equipment and privately constructed green buildings. Furthermore, some governments are requiring reduced carbon emissions and are poised to penalize buildings with large carbon footprints, putting yet greater emphasis on both green renovations and new development.

Initially created for office buildings, LEED (Leadership in Energy and Environmental Design) building certification has gained prominence across real estate commercial uses, including 415 hotel projects that have achieved or registered for certification. Originally predominant in high-end, mixed-use hotel projects, LEED certification can now be found in projects across price points and product types. The United States Green Building Council and the American Hotel and Lodging Association are planning to release a dedicated certification for hotel projects in late 2009, which may help ease concerns among certain developers regarding

the applicability of LEED standards to hospitality projects. However, the creation of green standards for day-to-day hotel operations is still lacking, providing an opportunistic scenario for lodging companies to market themselves as being green without adopting green practices holistically throughout their organizations.

Hotel companies are designing new brand features that are aligned with the perceived growing demand for green products. New brands offer a whole suite of environmentally friendly hotel services although current market conditions are likely to slow down their introduction into the hotel industry. These new brands offer not only hotels with LEED-certified design, but green services, such as organic meals and eco-friendly shuttle service to and from airports by hybrid cars. These hotels aim to minimize energy use and waste by providing amenities such as shampoo and soap dispensers rather than bottles that create excess trash, as well as by recycling water and eliminating packaging.

In the finance arena, professionals have developed various investment vehicles specifically for green real estate. Private investors can now invest in green real estate funds, such as JP Morgan's US\$500 million Green Urban Renaissance Fund.<sup>13</sup> Developers of LEED- or Energy Star-certified projects can participate in green lending programs and receive longer payback periods, higher loan-to-value ratios or preferred review terms, in comparison to the terms they would normally receive on financing



of non-green buildings.<sup>14</sup> To support these innovations in green real estate finance, in October 2008, the Green Building Finance Consortium released the Sustainable Property Due Diligence Process, aimed at developing valuation and underwriting frameworks to project more accurately the financial returns from green properties.<sup>15</sup> Furthermore, the Clinton Climate Initiative is lending US\$5 billion to renovate existing structures to energy-efficient standards.

As green programs mature, energy efficiency becomes the norm and consumers of hospitality services demand more green products, companies that successfully integrate environmentally friendly practices across all their business activities should have a higher potential to achieve an even greater competitive advantage.

13 Leanne Tobias, "Green Real Estate Finance Going Mainstream," *Urban Land Green*, Spring 2008.

14 Ibid.

15 Green Building Finance Consortium, <http://www.greenbuildingfc.com/Home/Announcements.aspx>, accessed on 23 October 2008.

# 8

## Fair value: what does it mean?

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 157 (FAS 157), *Fair Value Measurements*, which establishes a framework for measuring and disclosing the fair value of assets (and liabilities) under US Generally Accepted Accounting Principles (GAAP).<sup>16</sup> FAS 157 does not expand the use of fair value in GAAP, but instead provides a single definition of fair value to increase consistency, comparability and transparency of fair value measurements. As the credit crisis continues to grow and real estate declines affect other asset classes (with hotels and retail likely to be significantly affected), the principles of FAS 157 will play an increasingly important role in hotel valuation.

Although the FASB had previously defined fair value and concluded that it was relevant to users of financial statements, there was limited guidance in applying the concept of fair value for financial reporting purposes. FAS 157 clarifies that fair value is an exit price – that is, the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. FAS 157 does not prescribe the use of any one valuation method. While in some cases, a single valuation technique will be appropriate, multiple valuation techniques (e.g., sales comparison, income and/or cost approaches) may be appropriate in other cases. The valuation technique(s) to be used should be consistent with those that market participants would use in

determining fair value in a hypothetical sale at the measurement date. However, FAS 157 does include specific guidance on the inputs to be utilized within a valuation technique(s), providing that a fair value measurement should maximize the use of observable inputs and minimize the use of unobservable inputs. This will likely require additional documentation and support as to the inputs and methodology used in arriving at the fair value estimate. In addition, FAS 157 requires additional disclosures regarding the use of fair value measurements, including information to enable users to assess the inputs used to develop these measurements. Revisiting the process used to measure fair value and documenting the fair value estimates is anticipated to be extensive for owners this year. This process is likely to be even more challenging in the current market due to the decrease in observable inputs on which to base fair value estimates. With limited transactions taking place, capturing such inputs as applicable comparable sales, appropriate market capitalization rates and relevant market revenue and expense change rates, can be difficult. Those limited transactions that are occurring may not be representative of fair value, as they may not be at arm's length or, in certain instances, may represent "distressed sales," but obtaining the evidence to demonstrate that fact can be challenging.

Given the lack of observable inputs, the application of the FAS 157 definition of fair value as an "exit

price" will require a greater degree of judgment from management as to appropriate valuation assumptions based on historical experience and future anticipated performance. In order to ensure that fair value measurements hold up to scrutiny, owners may look to utilize third-party professionals. However, the use of third-party specialists does not alleviate management's ultimate responsibility for the fair value measurements (and related disclosures) reported in the entity's financial statements. Management will need to understand and appropriately challenge the assumptions and processes used by third-party professionals. In situations where relevant observable data does not exist, management may need to use internal assumptions about future cash flows and required rates of return. However, these assumptions need to be consistent with assumptions that market participants would use to price the asset in a current transaction.

The clarifications made by the FASB regarding the concepts of a fair value measurement may result in changes to certain existing practices. In addition, the effort to appropriately support, document and disclose various input assumptions is likely to be substantial, particularly with increasing impairments. In the current environment, investors are requiring additional clarity on fair value measurements, thereby increasing the importance of transparent disclosures.

<sup>16</sup> "Original Pronouncements (As Amended): Statement of Financial Accounting Standards No. 157: Fair Value Measurements," Financial Accounting Standards Board, Issued September 2006, p. 2.

# 9

## Alternative vacation products: value isn't everything

During economic slowdowns, Americans have traditionally continued to travel for vacation though their trips typically become shorter, closer to home or less expensive. In this context, the value proposition of alternative lodging options, such as timeshare and cruise products, becomes increasingly attractive for leisure travelers due to their all-inclusive nature, the ability to lock in pricing and overall lower costs for packages. However, the current economic crisis appears to be affecting these sectors in a more severe manner than in previous periods of distress (e.g., post-9/11), when they earned the "recession-proof" label.

Timeshare is marketed and sold as a prepaid vacation, generally in one-week increments. It is thus perceived as an alternative to lodging accommodations, rather than a competitor of other forms of second-home ownership, due to its lower price point. The ability to lock in the cost of future vacations makes it appealing to many budget-conscious travelers, which may help explain the interval sales increases following 9/11. While the prepurchase aspect of timeshare has historically protected the industry from volatile fluctuations in pricing, the influx of highly discounted resale inventory, as well as the impact of other resort products (such as fractional ownership) may negatively impact price and the absorption of newly constructed inventory. In addition, developers are facing growing difficulty in securitizing



the loans provided to timeshare buyers, historically a significant source of interest arbitrage income. This is likely to reduce the ability to provide attractive terms for approximately 40.0% of developers in the industry offering financing to complete purchases.<sup>17</sup>

Cruises have also traditionally maintained robust demand levels during times of economic insecurity. All-inclusive cruises allow vacationers to book packaged deals and thus maintain control of travel budgets. Cruise lines were able to pass fuel price increases (upwards of 75.0% year-over-year for some companies<sup>18</sup>) on to consumers through fuel surcharges to post profit increases through the third quarter of 2008. However, the landscape may be less benign looking forward, as the strengthening US dollar and falling fuel prices are not anticipated to provide sufficient cushion to offset increased competition from new cruise ship supply as well as anticipated declines in new bookings.<sup>19</sup> To counter the lower revenues that are forecast, shorter and more affordable routes requiring low-cost or no air travel at all are anticipated from ports of call. Cruise lines such as Carnival and Celebrity, for example, are foregoing their Mediterranean and Australian itineraries, respectively, while increasing operations from their Miami and Baltimore homeports.

Together with all-inclusive resorts, prepurchased timeshares and all-inclusive cruises should become increasingly attractive for vacationers in 2009, due to their high value proposition. However, supply-side risks will require a thorough understanding of industry and local market fundamentals among investors in these asset classes.

17 2007 Annual Fractional Interest Report, NorthCourse, 8th edition, 2007.

18 "Carnival PLC – 3rd Quarter Results," PR Newswire, 18 September 2008.

19 "Royal Caribbean's Third Quarter Profit Raises 4 Percent," Associated Press, 28 October 2008.

# 10

## Obama's stimulus package: impact on the lodging industry

President Barack Obama has announced a significant economic stimulus plan intended to create jobs, implement tax breaks for businesses, improve infrastructure and stabilize the economy. Similar to the US\$168 billion stimulus package passed in February 2008 that emphasized tax rebates, President Obama's package, which totals US\$825 billion, features US\$275 billion in tax relief for businesses and individuals, investments in alternative energy initiatives, infrastructure (although not as much as anticipated) and aid to state governments.<sup>20</sup> A key component of the proposed plan is to create or preserve approximately three to four million jobs through 2011,<sup>21</sup> as the unemployment rate increased to 7.2% in December 2008, the highest level in approximately 16 years. Further, according to President Obama, unemployment could reach "double digits" without government action.

The proposed economic stimulus plan is anticipated to have positive short-term and long-term impacts on the US lodging industry, as the industry would benefit from increased consumer spending and corporate profits as well as improved transportation infrastructure and access. The plan aims to offset decreases in consumer spending by creating jobs and increasing disposable income, and would likely increase corporate

sales and profits, particularly in the construction and manufacturing sectors. Infrastructure investments will have a positive impact on the US lodging industry, as improvements made to the nation's transportation infrastructure would improve access to major tourist destinations and stimulate additional domestic/international travel over the long term.



20 Naftali Bendavid, Elizabeth Williamson and Sudeep Reddy, "Stimulus Package Unveiled," *The Wall Street Journal*, 19 January 2009.

21 Peter Nicholas, "Obama Expands Size of Stimulus Plan," *The Los Angeles Times*, 20 December 2008.



## Global and US overview

# Global perspectives

Despite declines in occupancy across most major regions in the world, operating performance remains positive as hoteliers continue to focus actively on revenues, so RevPAR increases have outpaced the previous year's results. Although a portion of the decline in occupancy can be attributed to the cyclical nature of the industry and additions to supply, the global economic weakness, as well as the uncertainty in energy and other commodities markets,<sup>22</sup> are anticipated to have a negative impact on the industry's growth in 2009.

For 2009, the Middle East and Africa are expected to see a decline in lodging fundamentals as world economic growth has waned and oil prices have retreated from their peak. The Middle East and Africa, however, are the only markets to have experienced growth in occupancy for year-to-date November 2008. In spite of a slight fall in occupancy, Dubai achieved the highest RevPAR in the Middle East

and Africa region at US\$239. Eight of the 10 major markets in the Middle East and Africa achieved RevPAR growth in excess of 20% year-to-date November, with Beirut and Abu Dhabi earning the highest at 51.1% and 10.4%, respectively. Contrary to other global markets, the Middle East and Africa were favorably impacted by the increase in oil prices, which improved disposable income, increased intraregional travel and enabled local investors to continue to fund massive infrastructure and tourism-related developments. However, challenges such as shortages of construction materials and rises in labor costs due to the building boom, as well as a reduction in travel, have recently caused a slowdown in real estate investment and development, and are likely to further curtail development activity in 2009.

The South American lodging market achieved the second highest RevPAR growth by region (behind Northern

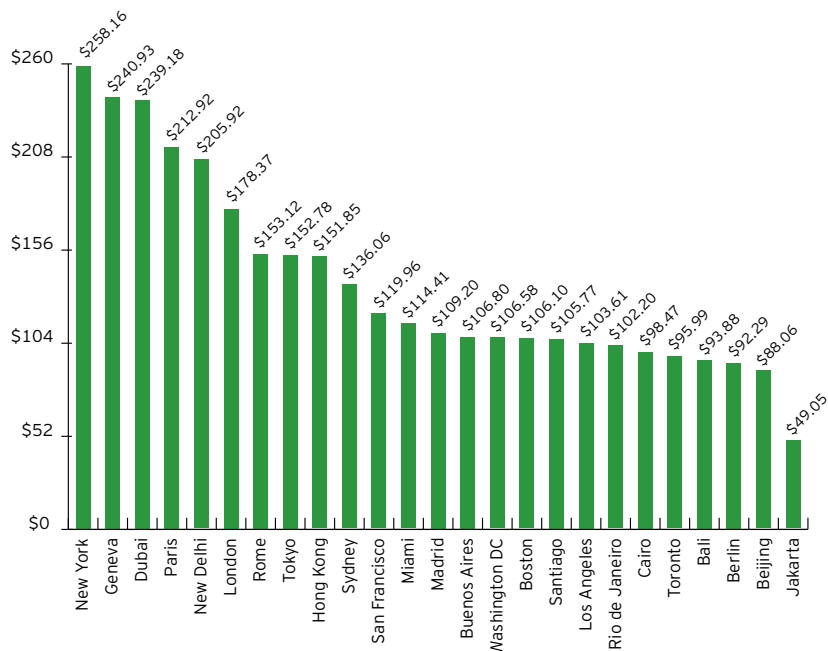
Africa) for year-to-date November 2008, primarily due to an increase in international arrivals and intraregional travel. Year-to-date November 2008, Buenos Aires earned the highest RevPAR in the region at US\$107, while Santiago and Rio de Janeiro achieved RevPAR of US\$106 and US\$102, respectively. The combination of greater regional travel, stronger tourism infrastructure and lower costs of leisure activities has initiated a transformation similar to that of Asia, where new developments are targeting luxury travelers rather than the typical backpacker.<sup>23</sup> Additionally, the foreign policies of the governments of Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Surinam, Uruguay and Venezuela have enabled their citizens to travel among them without passports, contributing to the rise in regional tourism. Brazil has so far been the focus of new hotel developments with 59% of South America's total pipeline.

22 "Global financial crisis 2008: decline in short-term but recovery by 2010," *Euromonitor International*, 16 October 2008.

23 "South America - The Next Big Thing?," *eTurboNews*, 30 September 2008.

## Year-to-date November 2008 RevPAR performance by market (USD)

Source: Smith Travel Research  
Monthly Lodging Review



However, estimates of total new hotel supply continue to be adjusted downward as lending conditions continue to deteriorate. Despite indicators that may suggest stronger operating fundamentals than those of previous years, the South American lodging market lags in RevPAR levels compared with other major global markets.

Overall, the European lodging market continues to achieve consistent RevPARs due to a combination of leisure demand for historical and cultural destinations, corporate demand generators and intraregional demand.<sup>24</sup> London is still the focus of hotel supply and renovations in preparation for the 2012 summer Olympics. Eastern Europe also experienced increased hotel supply until October 2008 with top-end brands establishing themselves in high-spending capital cities.<sup>25</sup> However, Europe has been affected by the global economic

slowdown, and lodging fundamentals in 2009 are anticipated to correlate with those of the global markets. As of November 2008, Geneva was the market leader in the European region with a RevPAR of US\$241. Of the major markets in Europe, Geneva also achieved the highest RevPAR growth at 21.0%.

The Asia-Pacific lodging market, consisting of Asia, Australia and various islands in the Pacific, achieved significant gains compared with 2007. Specifically, China experienced growth due to the added demand for the 2008 Beijing Olympics. Other regional sporting events, such as the East Asian Games (Hong Kong), Commonwealth Games (New Delhi) and the Youth Olympics (Singapore), are expected to support hotel development in those markets in 2009 and 2010. However, sustained occupancy and absorption of large sporting events remain a concern for

the region.<sup>26</sup> In China and India, lodging fundamentals have been supported by the introduction of low-cost carriers, an increase in middle-class income and the establishment of gaming destinations, which fuel intraregional travel. Within the Asia-Pacific region, New Delhi achieved the highest RevPAR (US\$206), while Bali and Jakarta lead in RevPAR growth of 36.5% and 19.3%, respectively. However, in spite of strong operating fundamentals in a few markets, the global economic slowdown is likely to have a negative impact on the hotel industry in much of the Asia-Pacific region in 2009.

In 2009, the global lodging industry is anticipated to face strong headwinds, with declining lodging demand and increased lodging supply. These factors will force the hotel industry to reduce costs and focus on the bottom line. While the scale of the downturn remains uncertain, a global rebound is not expected until 2010.

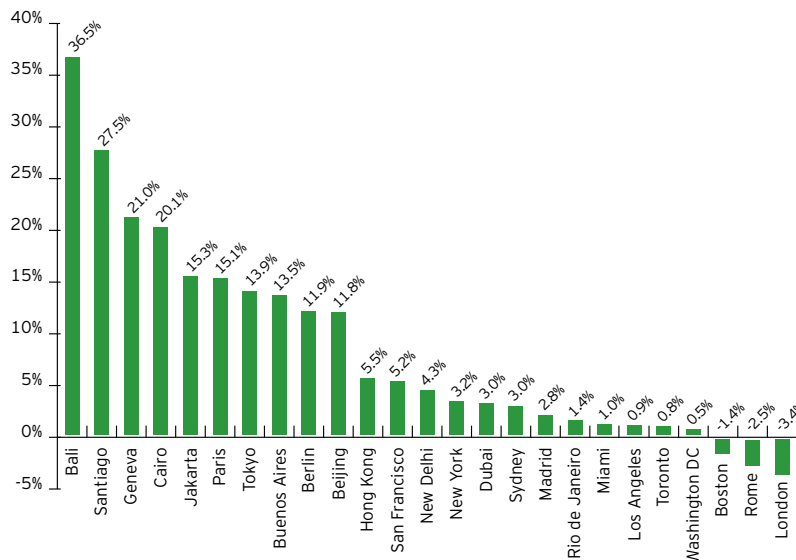
24 *Tourism Highlights: 2008 Edition*, World Tourism Organization, 27 September 2008.

25 "Boutiques enter the mainstream," CNBC European Business, September 2008.

26 "Beijing hotel rates, revenue spike during 2008 Olympic Games," Smith Travel Research Global, 27 August 2008.

### Year-to-date November 2008 RevPAR percent change by market

Source: Smith Travel Research  
Monthly Lodging Review



# US industry overview



With one of the worst financial crises hitting the United States since the Great Depression, the US lodging industry faced several key challenges in 2008, resulting in declines in demand and occupancy and slower growth in average daily room rate and RevPAR.

Business travel in particular was affected in 2008 as declining profits and rising travel costs forced many companies to tighten expense budgets, shorten lengths of stay or cancel meetings altogether. In September 2008, the number of individuals who purchased first-class or business-class airline tickets declined 8.0% compared with September 2007, and this decline is anticipated to continue through 2009.<sup>27</sup> Overall, the Travel Industry Association (TIA) anticipates business travel volume to decline 3.7% in 2008 and 2.7% in 2009.<sup>28</sup>

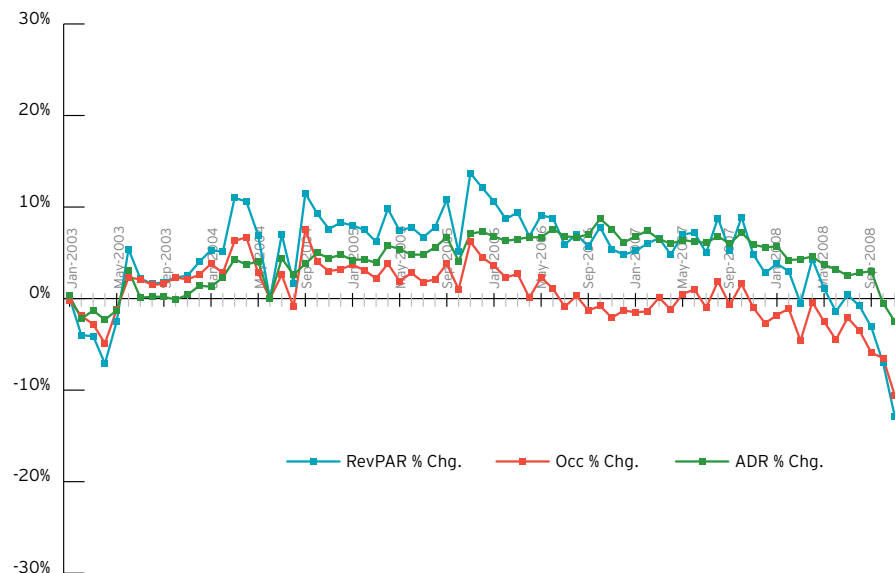
27 Christopher Hinton, "Airlines See Big Declines in Business Travelers; Further Losses Could Lead Carriers to Cut Prices," *Chicago Tribune*, 24 November 2008.

28 "Leisure Travel Stable, Business Travel Down," *Travel Industry Association*, 30 October 2008.

## US lodging market change in monthly occupancy, ADR, RevPAR performance

January 2003–November 2008

Source: Smith Travel Research  
Monthly Lodging Review



Similarly, leisure travel declined in 2008, as fuel prices reached record highs and significant job cuts across industries and uncertainty about the economy eroded real personal income and consumer spending. The drop in the leisure sector, however, was not as pronounced as it was in the business sector. According to TIA, leisure travel volume is expected to decrease 0.2% in 2008, and a modest 1.3% in 2009.<sup>29</sup>

Although international travel was strong in 2008, the weakening of the global economy and the recent gain in the value of the US dollar against major global currencies is likely to result in moderation of inbound travel to the US in 2009. The Department of Commerce estimates that in 2009, international and overseas arrivals will decline 1.6% and 3.0%, respectively.<sup>30</sup> However,

these declines may be offset with the acceptance of new countries into the US's Visa Waiver program, which would enable nationals of certain countries to stay in the US for 90 days or fewer for tourism or business purposes without visas. As of 17 November 2008, nationals of the Czech Republic, Estonia, Latvia, Lithuania, Hungary, the Republic of Korea and the Slovak Republic were granted these privileges, provided they possess a biometric passport and register online through the Electronic System for Travel Authorization.<sup>31</sup>

As a result of declines in both business and leisure travel, occupancy levels decreased in 2008 and are anticipated to continue decreasing in 2009, particularly as new supply comes online in the midst of falling demand and a softening economy. Over the next two years, supply

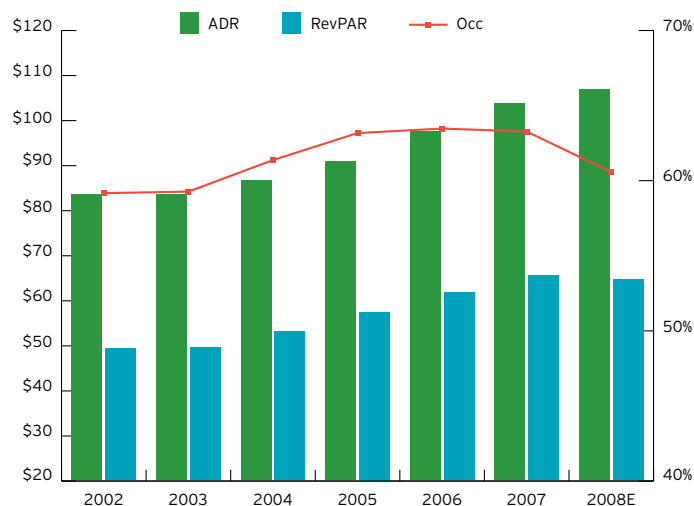
will increase 6.2%, adding approximately 275,000 rooms to the lodging market.<sup>32</sup>

The lodging industry has also experienced slow ADR growth, as declining demand growth in both the business and leisure sectors has made it difficult for US hoteliers to raise room rates. Many US hoteliers, in fact, have had to heavily discount room rates and/or offer promotional packages to offset declines in occupancy. Based on year-to-date November 2008 data from Smith Travel Research, overall occupancy is estimated to decrease by 2.7 percentage points to 60.5%, with ADR increasing 3.0% to US\$107, resulting in a RevPAR decrease of 1.4% to reach US\$65.

29 Christopher Hinton, "Airlines See Big Declines in Business Travelers; Further Losses Could Lead Carriers to Cut Prices," *Chicago Tribune*, 24 November 2008.  
 30 Ibid.  
 31 [http://travel.state.gov/visa/temp/without/without\\_1990.html#](http://travel.state.gov/visa/temp/without/without_1990.html#) accessed on 25 November 2008.  
 32 Hotel Horizons, National Edition, PKF Hospitality Research, Third Quarter 2008.

### US lodging market occupancy, ADR, RevPAR performance 2002-2008E (USD)

Source: Smith Travel Research  
 Monthly Lodging Review



## RevPAR trends by market segment

Unlike 2007's robust RevPAR figures, year-end 2008 RevPAR levels are anticipated to decline in all segments. By year-end 2008, the luxury segment is expected to experience the greatest decline in RevPAR of 5.5% primarily as disposable income decreases given the slowdown in the economy. Unlike historical economic downturns, the

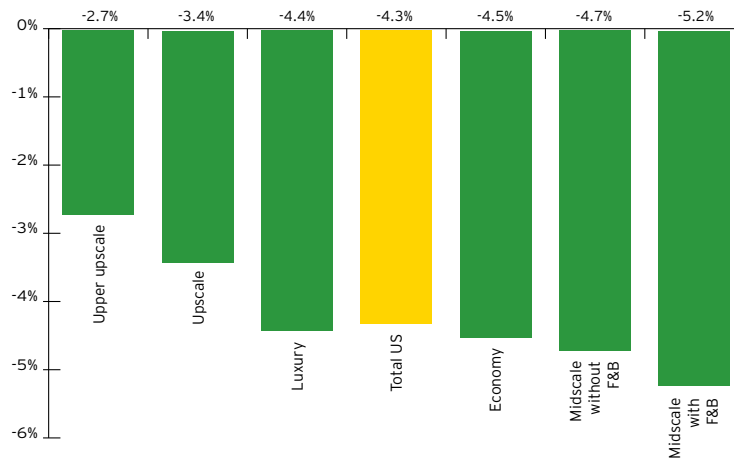
luxury segment has not been insulated from RevPAR declines in 2008. Luxury travelers to destination markets, such as high-end ski, beach and golf resorts, are reducing travel and spending. Additionally, luxury travelers are downgrading to upper upscale and upscale chain scales. Also, the economy segment is anticipated to experience

the second greatest decline in RevPAR of 3.1% due to the heightened price sensitivity of guests in this segment.

Furthermore, the upscale segment is anticipated to be the most affected segment in 2008 due to heavy reliance on business travel, resulting in a RevPAR decrease of 0.8% for year end 2008.

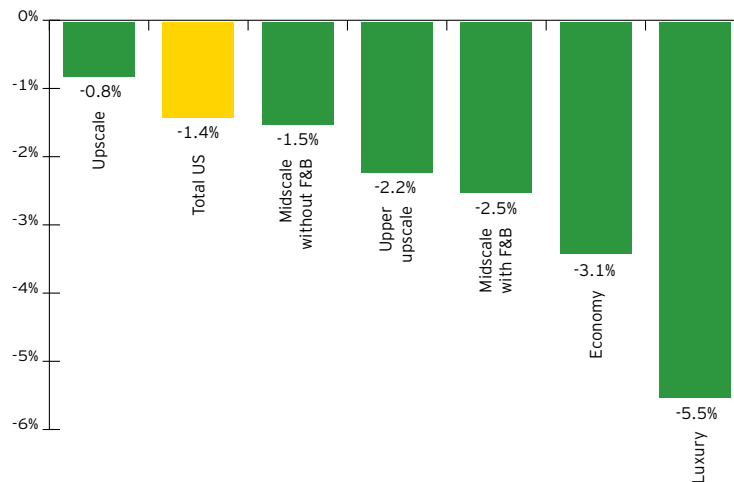
### Occupancy performance by segment 2008E

Source: Smith Travel Research  
Monthly Lodging Review



### RevPAR percent change by segment 2008E

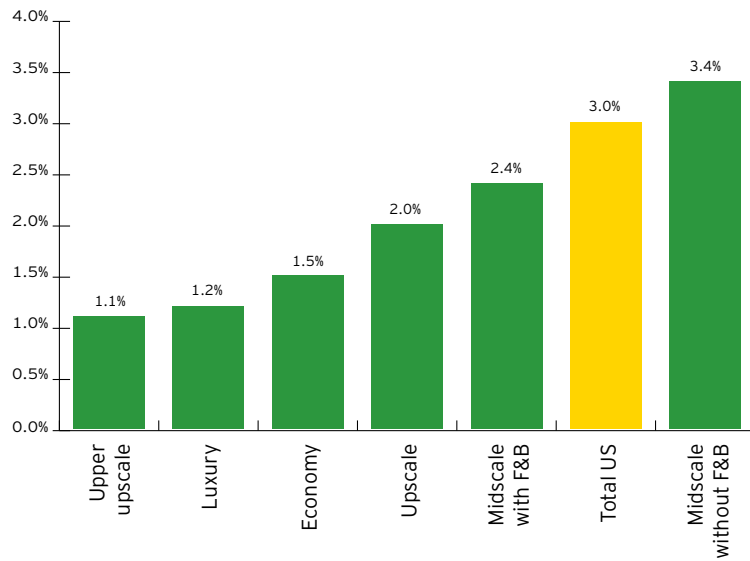
Source: Smith Travel Research  
Monthly Lodging Review





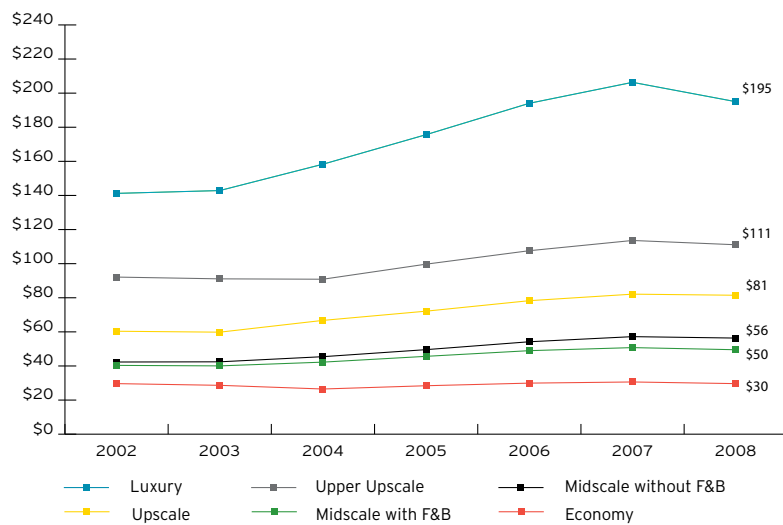
**ADR percent change by segment 2008E**

Source: Smith Travel Research  
Monthly Lodging Review



**RevPAR trend by chainscale 2000-2008E (USD)**

Source: Smith Travel Research  
Monthly Lodging Review



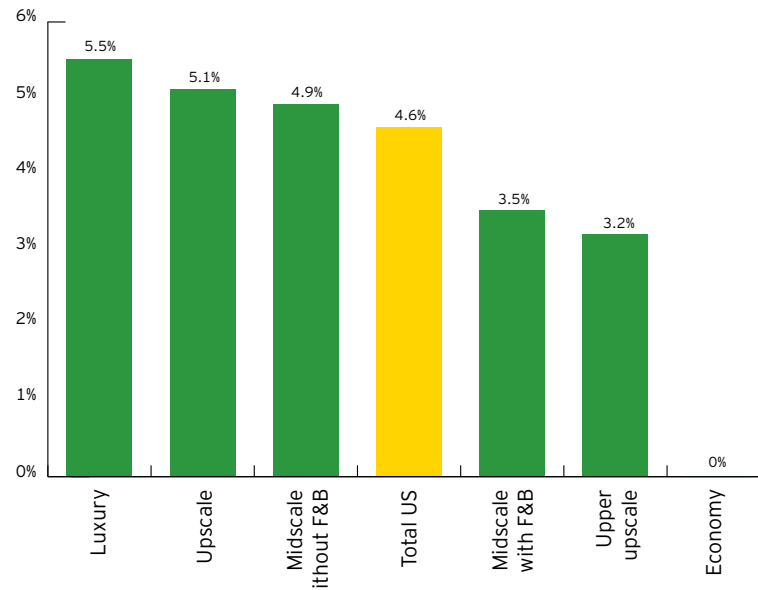
## RevPAR compound annual growth rate by market segmentation

The luxury and upscale segments demonstrated the most significant compound annual growth rates between 2002 and estimated year-end 2008, at 5.9% and 5.1%, respectively. To the contrary, the economy segment

experienced no growth from 2002 to estimated year-end 2008. Overall, the US market is projected to achieve 4.6% compound annual growth for RevPAR between 2002 and estimated year-end 2008.

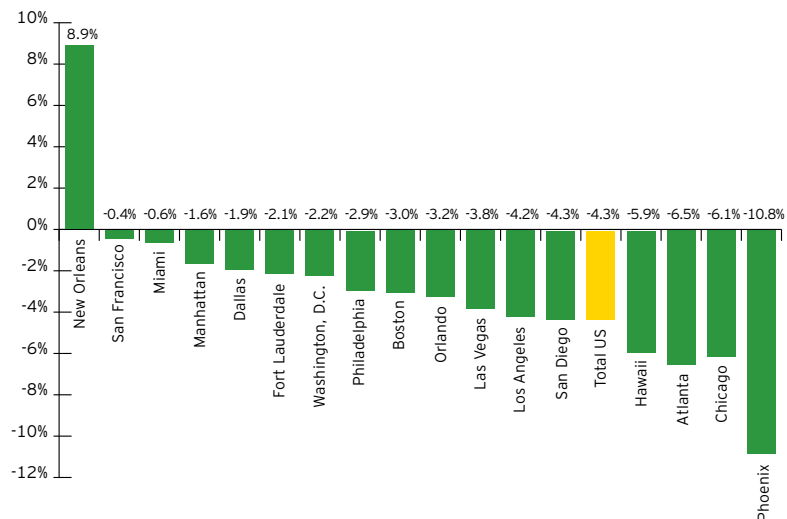
### RevPAR compound annual growth rate (%) 2000-2008E

Source: Smith Travel Research  
Monthly Lodging Review



### 2008E occupancy percentage change by market

Source: Smith Travel Research  
Monthly Lodging Review



## RevPAR trends by top performing markets

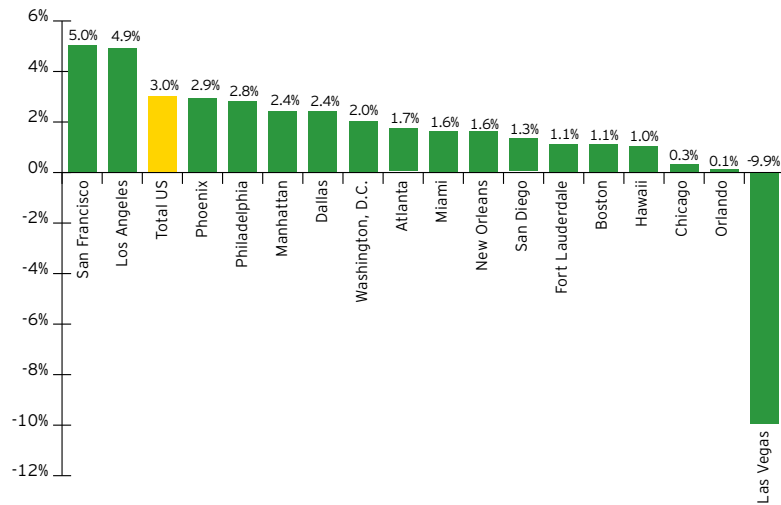
Based on year-to-date November 2008 data from Smith Travel Research, Manhattan is anticipated to lead the major markets in terms of performance, with RevPAR of US\$257, followed by Hawaii and Philadelphia with RevPARs

of US\$143 and US\$124, respectively. In terms of RevPAR percentage increases, New Orleans and San Francisco are projected to lead the markets with the most significant gains at 10.6% and 5.1%, respectively. RevPAR gains in New

Orleans are attributed to continuing rebounds post-Hurricane Katrina while those in San Francisco are attributed to a record-breaking convention season, an increase in international travel and the growing technology sector.

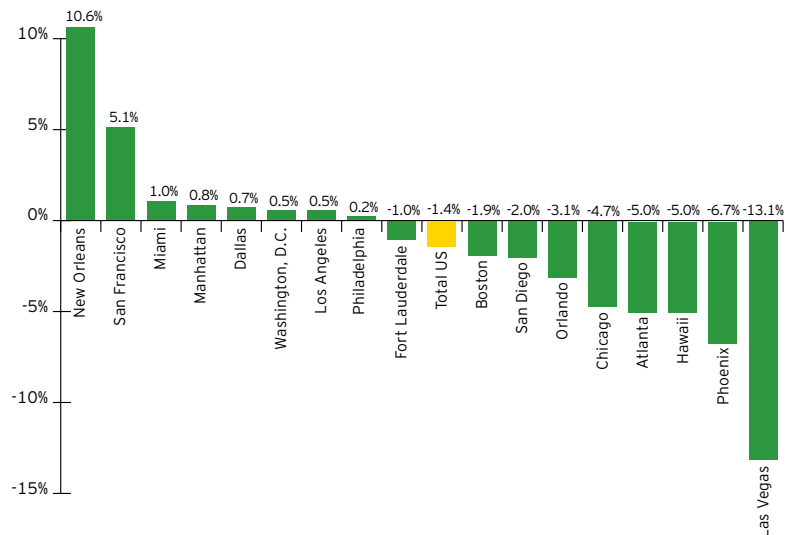
### 2008E ADR percentage change by market

Source: Smith Travel Research  
Monthly Lodging Review



### 2008E RevPAR percentage change by market

Source: Smith Travel Research  
Monthly Lodging Review



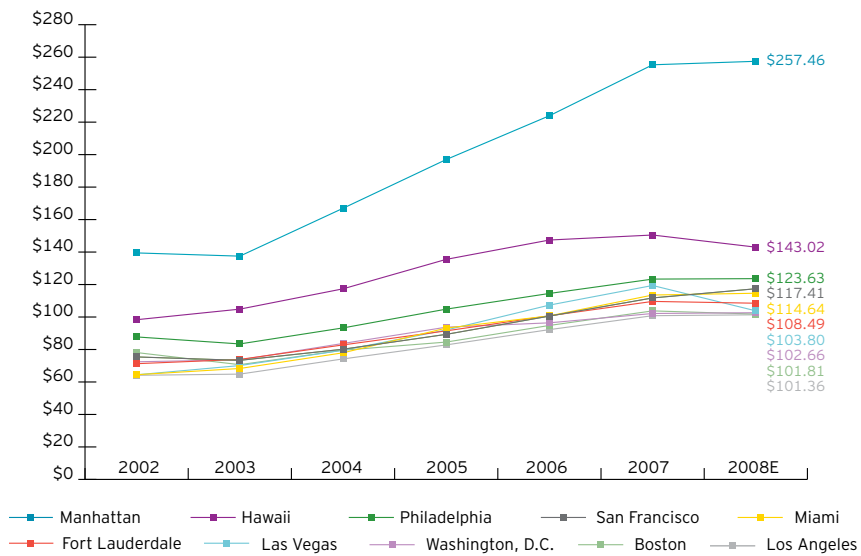
# RevPAR compound annual growth rate by top performing markets

All the major markets covered in this report have experienced increases in RevPAR since 2002. Between 2002 and estimated year-end 2008, Manhattan experienced the most significant

compounded annual growth at 10.8%. Other top performing markets include Miami at 10.1%, Las Vegas at 8.3%, Los Angeles at 7.9% and San Francisco at 7.7%.

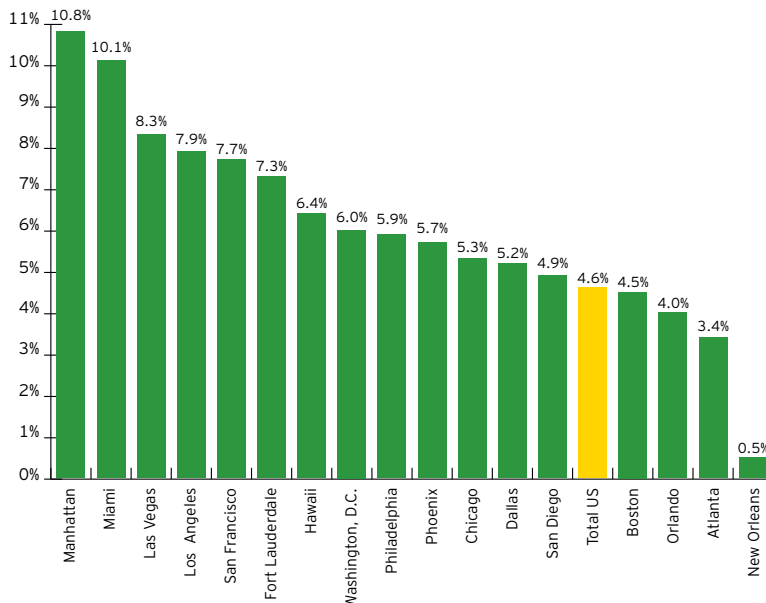
## RevPAR trend for top markets 2002-2008E (USD)

Source: Smith Travel Research Monthly Lodging Review



## RevPAR compound annual growth rate (%) 2000-2008E

Source: Smith Travel Research Monthly Lodging Review





## Chain segments

# Luxury

Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decline 3.1 percentage points to 67.9% in 2008, with ADR increasing 1.2% to US\$287. The result is a RevPAR of approximately US\$195, representing a decrease of 5.5% versus 2007. The projected 5.5% decrease of RevPAR in 2008 is estimated to be lower than it was during the most recent downturn in the lodging sector in 2001 and 2002, when RevPAR decreased approximately 14.2% and 5.1%, respectively, in those years.

The trend in RevPAR growth is commensurate with trends in consumer confidence: the Conference Board Consumer Confidence Index declined from 99.5 to 59.8 from September 2007 to September 2008. Despite the fall in consumer confidence, however,

the number of high net-worth individuals has risen. This has resulted in only minor RevPAR decreases in the luxury segment as compared with those of other chain segments. According to the 2008 Worldwide Wealth Report, in 2007, the number of high net-worth individuals (those who owned at least US\$1 million in liquid investable assets) was estimated at 10.1 million on a global basis, an increase of 6.0% as compared with 2006.<sup>33</sup> The wealth accumulated by high net-worth individuals is expected to continue increasing approximately 6.8% annually through 2012. This growing affluence is likely to help buffer, but not entirely protect, the luxury segment from the effects of the current financial turmoil. It should also be noted that the turmoil of the financial market has negatively affected this segment as demand from financial services firms,

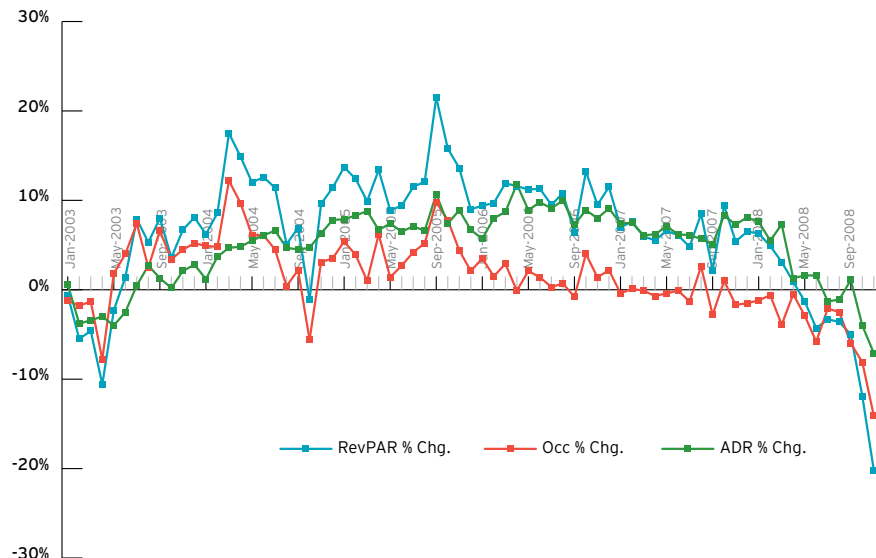
as well as general business travel, has softened since the third quarter.

According to Smith Travel Research's *U.S. Hotel Pipeline Report* for October 2008, the luxury segment has 94,898 rooms, representing 2% of the total lodging supply in the United States.<sup>34</sup> October 2008 Smith Travel Research data shows 7,570 luxury rooms under construction and a total of 14,596 rooms in the active pipeline.<sup>35</sup> Despite the shrinking economy, several new US and international luxury brands are anticipated to enter or expand their footprint in the US lodging market, including Baccarat, SLS, Armani, Shangri-La and Trump Hotels. In view of the increased competition, coupled with a weak economy, it is becoming ever more important for luxury hotels to differentiate themselves. Amenities that a few years ago were unique are now commonplace,

33 World Wealth Report 2008, Merrill Lynch and Caggemini, June 2008.  
 34 "Smith Travel Research reports U.S. Hotel Pipeline October 2008," Hospitality Net, 14 November 2008  
 35 Ibid.

## Luxury lodging market change in monthly occupancy, ADR, RevPAR performance January 2003-November 2008

Source: Smith Travel Research Monthly Lodging Review



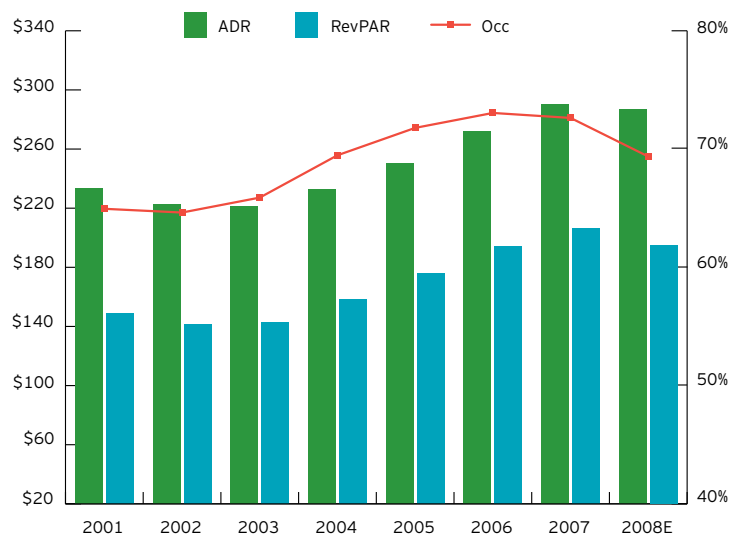


such as flat screen televisions, now present in 81% of luxury hotels recently surveyed by the American Hotel and Lodging Association.<sup>36</sup> One emerging trend in luxury hotels is the display of high-end art in the hotel's public spaces. This can be seen in the Gramercy Park Hotel in New York, for example, and the Wynn Las Vegas, which boast a collection of museum-quality work. Other hotels provide unique services and offerings as a means to distinguish themselves, including specialized butler service and room service for pets.

36 "World's Decadent Hotel Amenities," *Forbes*, August 2008.

**Luxury lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2001-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Upper upscale

Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decrease 2.4 percentage points to 68.9% in 2008, while ADR is expected to increase approximately 1.1% to US\$161, resulting in a 2.2% decline in RevPAR to approximately US\$111 as compared to 2007.



According to Smith Travel Research's *U.S. Hotel Pipeline Report* for October 2008, the upper upscale segment has 568,074 rooms, representing 12.2% of the total lodging supply in the United States.<sup>37</sup> The segment is anticipated to be negatively impacted by the current financial crisis, which will result in the need to become more operationally and financially efficient. The Advito 2009 Industry Forecast<sup>38</sup>, a white paper published by Advito, a travel industry consulting firm, as of October 2008 projects a rise of approximately 13.0% in

business travel expenses in 2009. This, coupled with the economic slowdown, is likely to induce companies to permit only essential travel. According to a survey conducted by the Association of Corporate Travel Executives,<sup>39</sup> 61.0% of survey respondents believe travel costs will outweigh trip value in 2009. Furthermore, approximately 36.0% of respondents said they would travel more, 33.0% said they would travel about the same amount and 31.0% said

they would travel less in 2009, thus indicating limited business travel growth in the near future.<sup>40</sup>

Additionally, the potential reduction in business expenditures could threaten the upper upscale segment with losing business travelers to lower-priced segments. The segment has already felt a steady increase in group attrition rates, with a greater number of cancellations as the day of reservation approaches. Furthermore, according to industry

37 "Smith Travel Research Reports U.S. Hotel Pipeline for October 2008," Hospitality Net, 14 November 2008.

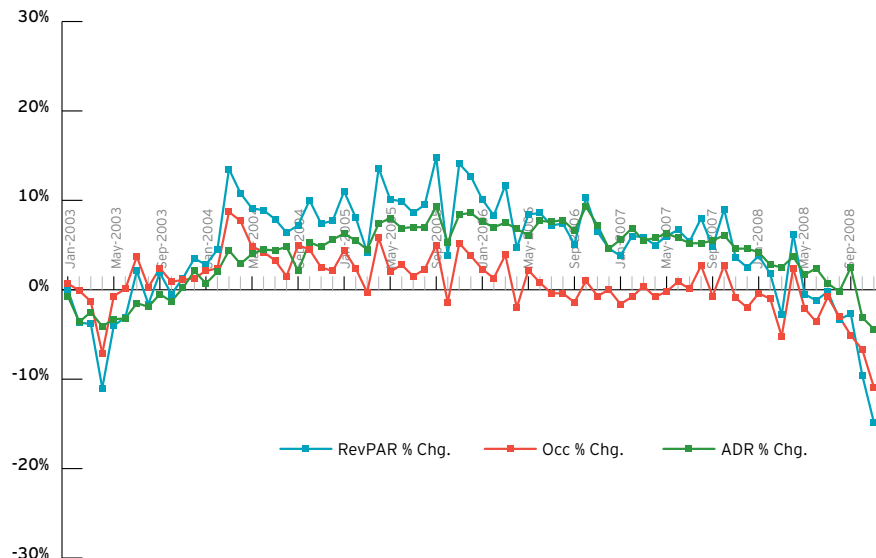
38 "Advito Forecasts 13% Hike in U.S. Travel Budgets," *Business Travel News*, 2 October 2008.

39 "Significant Cutbacks Forecast," *Business Travel Information and Magazine*, October 2008.

40 George Dooley, "ACTE Says: Don't Count on Business to Increase Travel Spending," *Travel Agent Central*, 7 October 2008.

### Upper upscale lodging market change in monthly occupancy, ADR, RevPAR performance January 2003-November 2008

Source: Smith Travel Research  
Monthly Lodging Review



interviews, as businesses cut back their travel budgets, the segment is seeing a drop in guest spend on food. Some hotels are witnessing cutbacks in lunches and coffee breaks, coupled with groups opting for shorter time periods and less expensive menu items.

Although the upper upscale segment could benefit from travelers downgrading from the luxury segment, this mitigating factor is likely to have only a limited impact because of the smaller relative size of the luxury segment.

Given the upper upscale segment's reliance on the business traveler, it is becoming increasingly important for hotels in this segment to expand and adopt certain marketing initiatives to mitigate a decline in corporate and group demand. Hotel operators are shifting marketing budgets from print and internet

advertising to direct marketing efforts. According to the March 2008 Marketing Sherpa Special Report, a survey published by Sherpa, a marketing research firm, only 4.0% of surveyed respondents noted plans to raise current print advertising levels. Additionally, spending for online advertising is projected to decrease 26.0% in 2009. Hotels are typically more likely to heighten direct marketing efforts over brand or image advertising during an economic downturn as it appears to be both cost-effective and efficient. Direct marketing efforts allow hotels to create offers tailored to individual corporate clients, which encourages loyalty and a return on their marketing investment.

According to travel management company Carlson Wagonlit Travel, corporate clients overall "should expect to see rate increases of 2.0% to 3.0% but with more [bargaining] leverage in

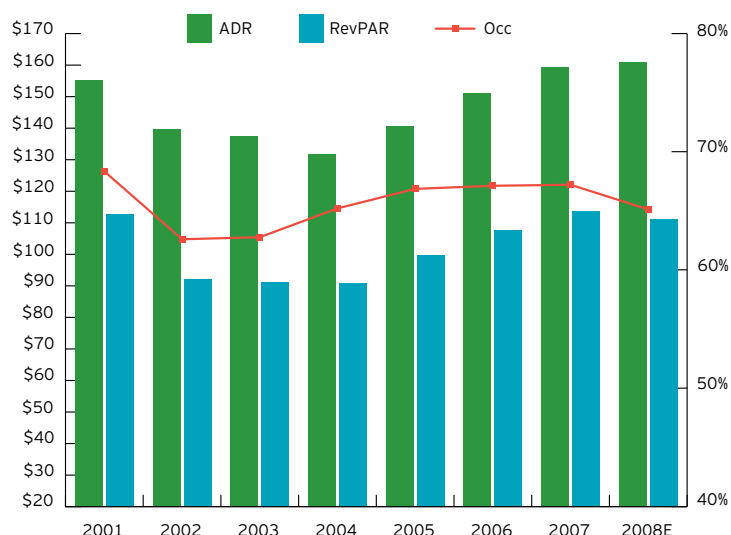
2009 negotiations compared to recent years."<sup>41</sup> In markets with low occupancy rates, corporate clients should be able to negotiate lower rates. To enhance the effectiveness of direct marketing, some hotel companies are developing marketing databases to store client preferences and to track the efficacy of various marketing campaigns. While these practices are applicable to all segments, they are particularly relevant to the upper upscale segment in view of the anxiety over the potential loss of corporate demand in the future.

In 2009, the economic crisis is likely to have a negative impact on the upper upscale segment as a direct result of the projected reduction in business travel spending. Occupancy is anticipated to decline due to the expected increase in lodging supply while ADR is anticipated to remain relatively steady.

41 "CWT Predicts Airfares to Soar, Room rates to Grow Modestly in 2009," Travel Management, 11 September 2009.

**Upper upscale lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2001-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



# Upscale

Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decrease 1.9 percentage points to 67.5% in 2008, with ADR increasing 2.0% to US\$121, resulting in a RevPAR of approximately US\$81, a decline of 0.8% versus 2007.

Smith Travel Research's US Hotel Pipeline Report for October 2008 indicates 450,412 rooms in the upscale segment, representing 9.7% of the total lodging supply in the US.<sup>42</sup> The upscale segment is anticipated to experience the largest relative increase in new supply as a percentage of existing supply among the six chain scale segments. Smith Travel Research indicates that approximately 51,400 upscale rooms were under construction as of October 2008,

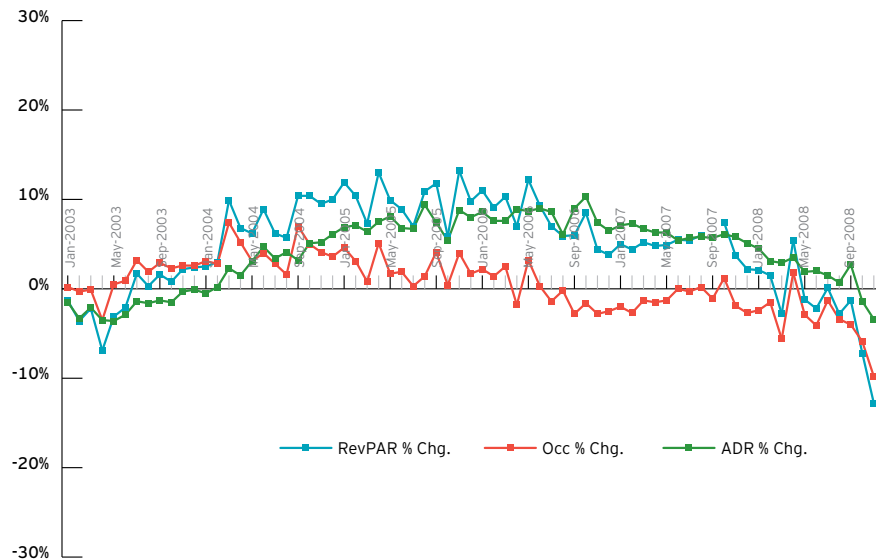


42 "Smith Travel Research Reports U.S. Hotel Pipeline for October 2008," Hospitality Net, 14 November 2008.

## Upscale lodging market change in monthly occupancy, ADR, RevPAR performance

January 2003–November 2008

Source: Smith Travel Research  
Monthly Lodging Review



representing approximately 11.4% of existing upscale room supply. Furthermore, for the same period, approximately 157,300 upscale rooms were under construction, in final planning or in planning phases, representing approximately 34.9% of the existing upscale room supply. This outpaces the second fastest-growing segment, midscale without food and beverage, with 23.2% of the existing room supply. However, in light of the recent contraction in the availability of credit, additions to the upscale segment supply are expected to slow in the short term as projects are postponed or cancelled.

The significant growth in supply can be partially attributed to the introduction of 12 new upscale lodging brands

since February 2005.<sup>43</sup> Many of these brands are targeting “Gen X” and “Next Gen” travelers, who spend more on leisure and travel than do previous generations,<sup>44</sup> by offering amenities tailored to their needs. A majority of the amenities are focused on state-of-the-art technology, including hotel-wide high-speed wireless internet, flat-screen televisions in the guestrooms and flat-screen desktop computers in the bar or lounge. Other updated offerings aimed at Gen X and Next-Gen include convenience-oriented amenities such as grab-and-go food outlets and 24-hour fitness centers. Many new brands are also implementing green initiatives since many travel managers now ask for details of environmental friendliness

in their requests for proposals. The relative development costs for such initiatives have dropped.

In 2009, the economic crisis is expected to have a negative impact on the upscale segment due to decreases in leisure and business travel spending. The significant additions to supply will add further pressure on operating performance going forward. Although some of this forecast may be mitigated by travelers downgrading from the upper upscale segment, both ADR and occupancy are likely to endure declining growth rates relative to 2008.

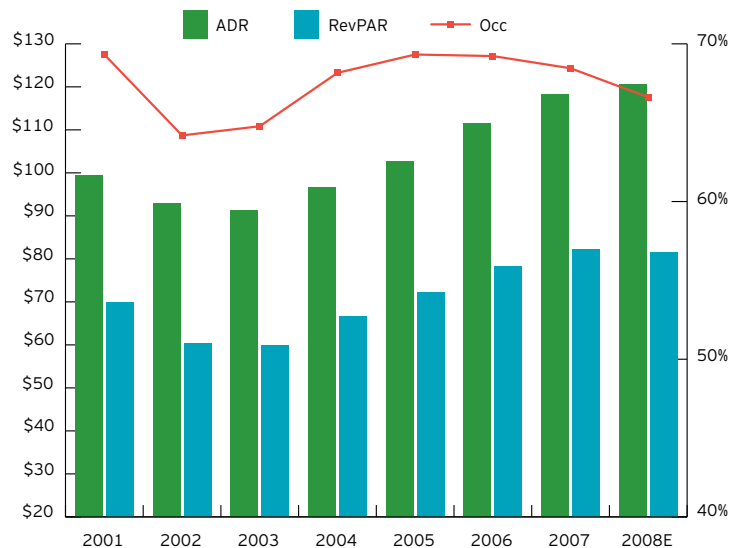
43 “New Hotel Brands Target Next-Gen Business Travelers,” *Travel Management*, April 2008.

44 Eric Knapp, “Generation X and the Hotel Industry: How Hotel Brands are Changing,” June 2005, [http://www.brandchannel.com/images/papers/76\\_Hotels.pdf](http://www.brandchannel.com/images/papers/76_Hotels.pdf) accessed on 19 October 2008.

### Upscale lodging market occupancy, ADR, RevPAR performance (USD)

2001-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Midscale with food and beverage

Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decrease 3.1 percentage points to 56.0% in 2008, with ADR increasing 2.4% to US\$88, resulting in a RevPAR decrease of 2.5% to approximately US\$50 versus 2007.

According to Smith Travel Research's US Hotel Pipeline Report for October 2008, the midscale with food and beverage segment has 515,194 rooms, representing 11.1% of the total lodging supply in the United States.<sup>45</sup> Data from Smith Travel Research shows the segment with 9,626 rooms under construction and 32,242 rooms in the total active pipeline as of October 2008.

This represents an 11.6% decline in the number of rooms under construction as compared with October 2007.

Many brands are reinventing and upgrading their food and beverage offerings to stay competitive. The new restaurant concepts are designed for easy operation, so they are suitable for new construction or renovated properties. For example, one lodging brand has developed a concept in which the food and beverage outlet can adapt functionality throughout the day. It can convert from a coffee bar with breakfast service to a grab-and-go casual dining outlet to a wine bar. In addition, many brands have recognized the value of a

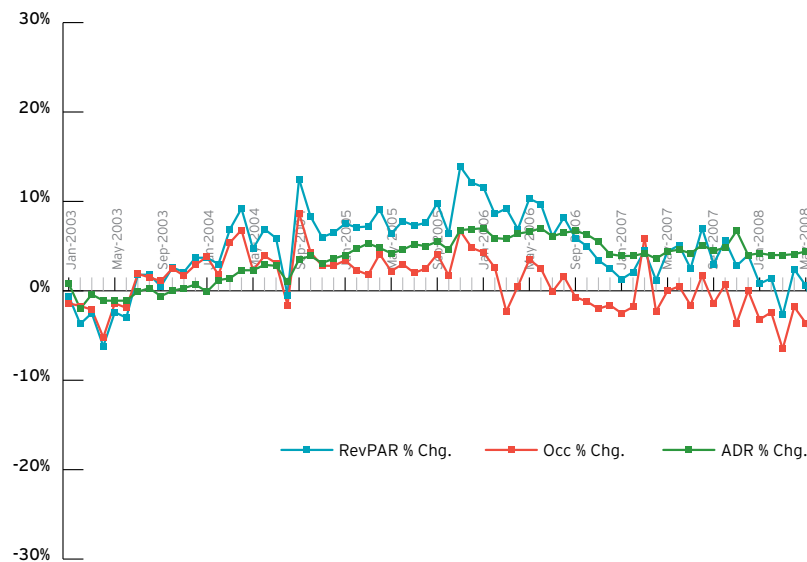


45 "Smith Travel Research Reports U.S. Hotel Pipeline for October 2008," Hospitality Net, 14 November 2008.

### Midscale with food and beverage lodging market change in monthly occupancy, ADR, RevPAR performance

January 2003-November 2008

Source: Smith Travel Research  
Monthly Lodging Review





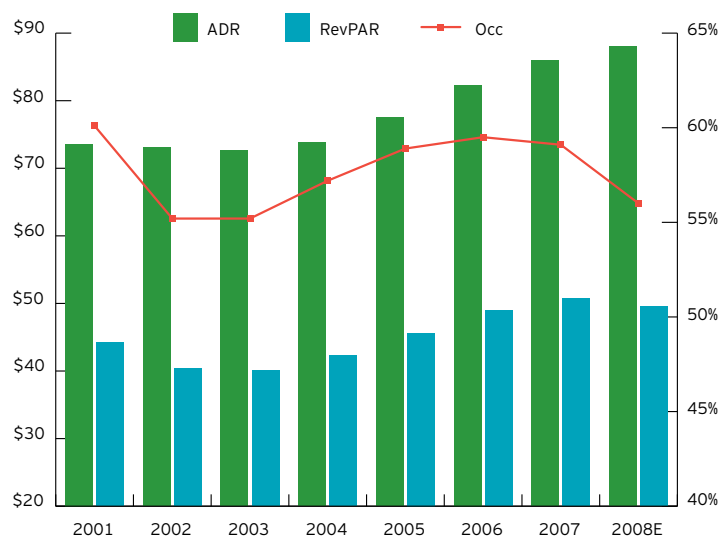
small 24-hour food market within the hotel and are incorporating this concept into their properties.<sup>46</sup>

For 2009, the midscale with food and beverage segment is expected to be negatively affected by the economic crisis. Although some travelers may downgrade to this segment, it is projected that occupancy will decline while ADR will remain more stable, resulting in an overall decrease in RevPAR.

46 Tony Dela Cruz, "Midscale Hotel Brands Fine-Tune F&B," *Lodging Hospitality*, 1 May 2008.

**Midscale with food and beverage lodging market occupancy, ADR, RevPAR performance (USD) 2001-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Midscale without food and beverage

Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decrease 3.0 percentage points to 62.5% in 2008, with ADR increasing 3.4% to US\$90, resulting in a RevPAR of approximately US\$56, a decline of 1.5% versus 2007.

According to Smith Travel Research's *U.S. Hotel Pipeline Report* for October 2008, the midscale without food and beverage segment has 767,624 rooms, representing 16.5% of the total lodging supply in the US.<sup>47</sup> As of October 2008, this segment had 57,420 rooms under construction, while the total active pipeline numbered 178,136 rooms.<sup>48</sup> The development pipeline comprises approximately 26.5% of total supply. However, it is likely that projects will be subject to further delays or even cancellations given the difficulty in securing financing and the sluggish economic conditions. Holiday Inn Express



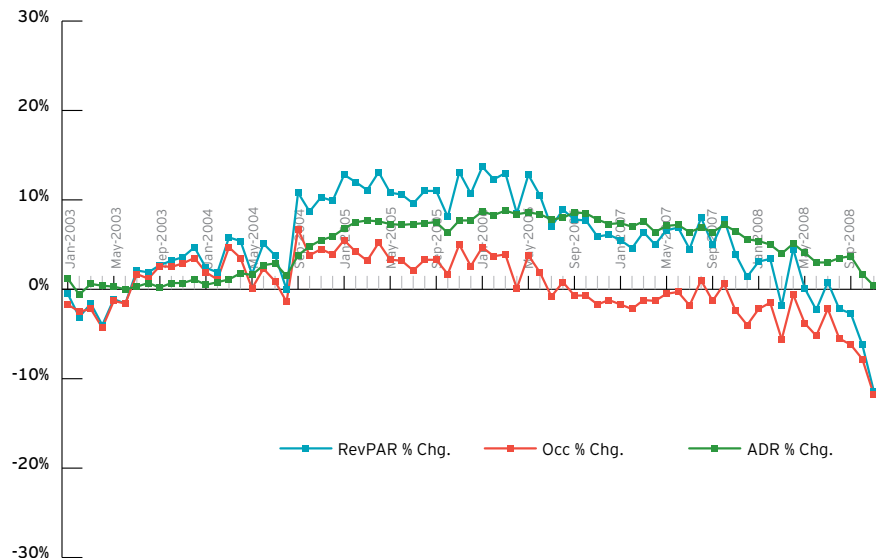
47 "Smith Travel Research Reports U.S. Hotel Pipeline for October 2008," Hospitality Net, 14 November 2008.

48 Ibid.

### Midscale without food and beverage lodging market change in monthly occupancy, ADR, RevPAR performance

January 2003-November 2008

Source: Smith Travel Research  
Monthly Lodging Review





and Hampton Inn, which are included in the segment, are both rapidly expanding as the two fastest-growing brands with more than 450 Hampton Inns and more than 656 Holiday Inn Expresses in the pipeline for the US.<sup>49</sup>

As corporate travel budgets are reduced, business travelers are expected to downgrade from the more highly rated chain scale segments to the midscale segments. Midscale lodgings can be more attractive to the business traveler in part because they tend to include complimentary business services, such as internet access. As corporations curb their travel spending and that spending comes under greater scrutiny, these practices figure into a firm's choice of hotels. Amenities like complimentary internet service and breakfast are viewed as a value driver by travelers and will assist hotels in becoming more competitive.

Although a greater number of corporate travelers are expected to stay at midscale without food and beverage properties, this segment is at risk due to its heavy dependence on middle-income leisure travelers. These travelers are the ones most affected by the economic crisis because their spending habits are more susceptible to declining home values, rising unemployment and the well-being of the general economy. Furthermore, the segment is vulnerable to reductions in airline capacity as corporate mid-level business travelers are forced to curtail business travel.

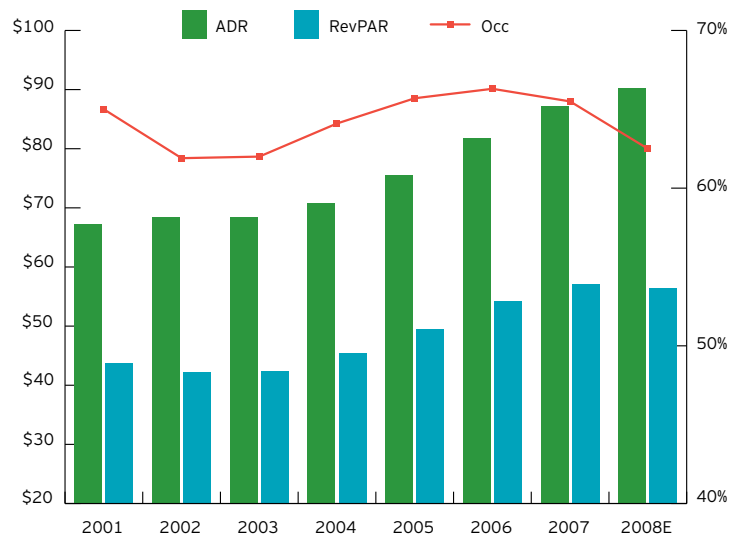
In 2009, the midscale without food and beverage segment is anticipated to experience a decline in RevPAR as occupancy decreases and ADR remains flat. However, the fall in RevPAR for the segment will be moderate as compared with the other lodging segments.

49 "Buyers Optimistic on '09 Hotel Rate Weakness," The Transnational, May 2008; "Holiday Inn Express Fact Sheet," Development.ihg.com accessed on 29 October 2008.

**Midscale without food and beverage lodging market occupancy, ADR, RevPAR performance (USD)**

2001-2008E

Source: Smith Travel Research  
Monthly Lodging Review



# Economy

According to Smith Travel Research year-to-date November, the economy segment had the greatest year-over-year decline in RevPAR relative to the other chain segments. Based on year-to-date November data from Smith Travel Research, occupancy is estimated to decrease 2.4 percentage points to 54.5% in 2008, with ADR increasing 1.5% to US\$54, resulting in a RevPAR of approximately US\$30, a decline of 2.8% versus 2007.

Smith Travel Research's *U.S. Hotel Pipeline Report* for October 2008 reports that the economy segment has 758,417

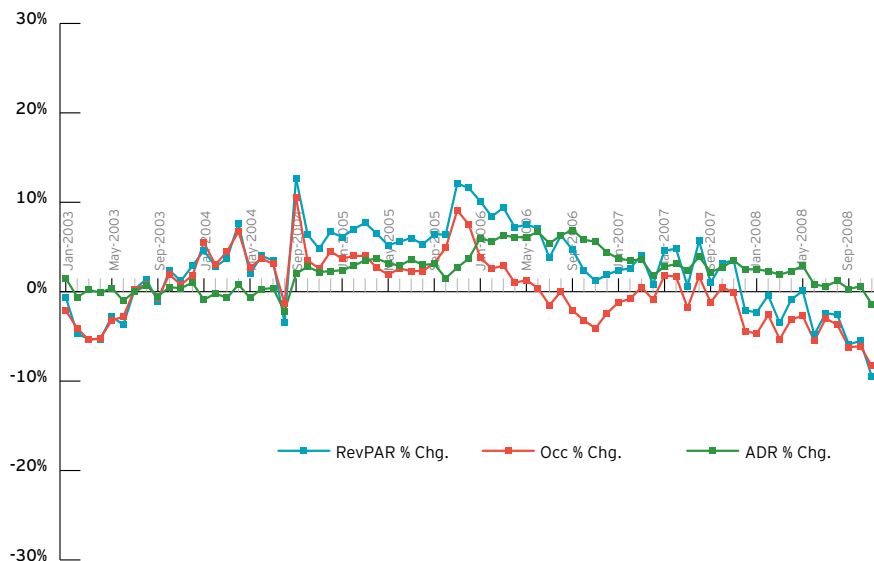
rooms, representing 16.3% of the total lodging supply in the United States.<sup>50</sup> October 2008 Smith Travel Research data shows 11,200 economy rooms under construction and a total of 26,570 rooms in the active pipeline. In an effort to become more competitive, several economy brands, such as Red Roof Inn and Motel 6, have introduced new hotel prototypes. These next-generation hotels include modern guestrooms, spacious lobbies and enhanced in-room technologies such as flat screen televisions. They also emphasize more luxurious bathroom fixtures and amenities, such as granite countertops,



50 "STR Reports U.S. Hotel Pipeline for October 2008." HospitalityNet.org. 14 November 2008.

## Economy lodging market change in monthly occupancy, ADR, RevPAR performance January 2003-November 2008

Source: Smith Travel Research Monthly Lodging Review





walk-in showers and upgraded vanity areas that are typically more common in more highly rated segments.<sup>51</sup>

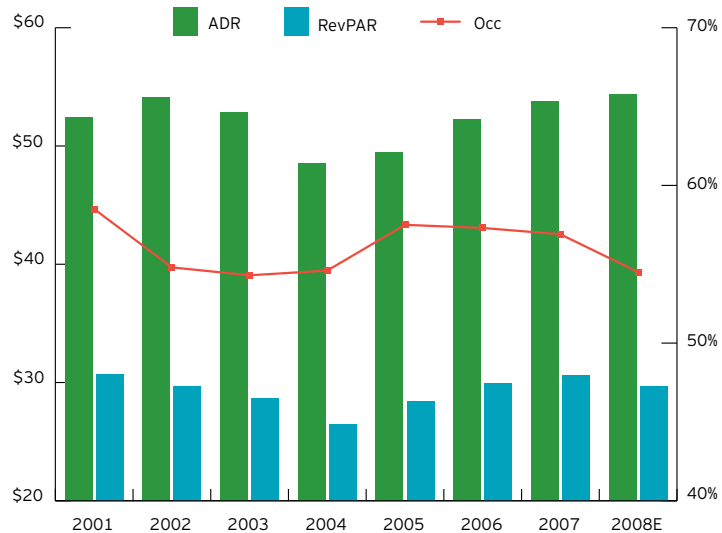
The current slowdown will have a significant effect on leisure travelers. Since the economy segment caters primarily to those travelers, it is expected to experience moderate decreases in occupancy and RevPAR and relatively flat ADR growth throughout 2009.

51 "Sleek Design, High-Tech Conveniences and Value: Red Roof Inns Unveils New Face of Economy Lodging," Red Roof Inn Press Release, May 2008; "Motel 6 Reinvents the Economy Lodging Segment with 'Phoenix' Prototype," Motel 6 Press Release, 11 March 2008.

**Economy lodging market  
occupancy, ADR, RevPAR  
performance (USD)**

2001-2008E

Source: Smith Travel Research  
Monthly Lodging Review







## Market overviews

# Atlanta

## Introduction

The Atlanta lodging market is anticipated to experience its first RevPAR decline since 2003, due to moderate decreases in occupancy with limited growth in ADR. Based on year-to-date November data from Smith Travel Research, it is estimated that the Atlanta lodging market will achieve RevPAR of US\$54 in 2008, a decrease of 5.0% from the previous year. ADR is anticipated to increase a slight 1.7% to US\$91, while occupancy is expected to decrease 4.1 percentage points to 59.1%.



## Hot topics

### Visitation: Hartsfield-Jackson International Airport continues to lead in volume

Atlanta's Hartsfield-Jackson International Airport continues to lead the country in terms of passenger movement, with an estimated 89.4 million passenger arrivals and departures in 2007. Passenger movement in 2008 remained positive, as the latest year-to-date information available as of September 2008 indicated a 1.1% increase relative to 2007, with forecasts expecting marginal growth by year's end.<sup>52</sup> Despite a year in which cash-strapped airlines are substantially decreasing capacity by cutting routes, Atlanta's Hartsfield has only had a slight (3.2%) decrease in capacity – well below the 10.3% nationwide decrease year-to-date – as Atlanta benefits from its airline hubs (Delta and AirTran), central location and large number of Fortune 500 companies.<sup>53</sup> Looking forward, Atlanta should continue to maintain its position as the country's busiest airport, especially in light of

Delta's merger with Minneapolis-based Northwest Airlines, whose hub will now be Atlanta. Furthermore, Atlanta is one of the more accessible destinations in the US, especially for larger groups and convention demand that may be slightly more price-sensitive in a recessionary environment. However, the continued slump in the office market, which experienced further vacancy increases of approximately 2.0% in Atlanta during the third quarter of 2008, may further limit the air arrivals that remain dependent on corporate travel.<sup>54</sup>

### New supply downtown: the emergence of luxury and lifestyle brands

While Atlanta welcomed two W Hotels in 2008, the city is poised to see additional luxury and lifestyle-oriented hotels in 2009 with the anticipated completions of the W Buckhead and W Downtown, Rosewood's The Mansion on Peachtree and Kimpton's Hotel Palomar, in addition to a Loews hotel and St. Regis Hotel

expected in late 2009/early 2010. Until recently, branded luxury hotels were scarce in Atlanta; however, certain submarkets, such as the midtown and Buckhead submarkets, have become increasingly trendy. Furthermore, the "Streets of Buckhead," a US\$1.5 billion mixed-use retail and lifestyle-oriented community whose first phase of retail shops is anticipated to open in late 2009, is anticipated to attract travelers to the downtown district.<sup>55</sup>

### Pipeline standstill: developers wait for more visibility on the market

While numerous lodging projects have managed to secure financing and continue development, many hotels in the pipeline have stalled in light of deteriorating financial conditions in the US credit market – especially given the high barriers to entry in downtown Atlanta. Furthermore, residential developments in downtown Atlanta, particularly those affiliated with larger, mixed-use hotels and retail components,

52 Hartsfield-Jackson Atlanta International Airport, Department of Aviation, <http://www.atlanta-airport.com/> accessed on 10 October 2008.

53 "Airline Schedule Changes at 300 US Airports," *USA Today*, <http://www.usatoday.com/travel/flights/airline-capacity-map.htm> accessed on 10 November 2008.

54 *Market View: Atlanta Office Report*, CB Richard Ellis, Third Quarter 2008.

55 "Premium Luxury Brands Choose The Streets of Buckhead for Global Expansion," *Business Wire*, 25 September 2008.



have had their construction plans put on hold, including at least 650 rooms associated with prominent, luxury hotel operators. Meanwhile, numerous hotel developments on the perimeter, predominantly limited-service and upscale hotels, have likewise been put on hold, and some districts have instituted hotel-development moratoriums, as supply and demand statistics point toward an overbuilt market. While a few of these projects may eventually be built, the elimination of some of the new supply pipeline should allow for the market to react better to recessionary pressures and avoid further supply saturation.

**Convention activity: slower bookings expected through 2009**

As the fourth-largest convention center in the US, with more than 1.4 million square feet, the Georgia World Congress Center, along with the Georgia Dome and other smaller venues with convention facilities, are the bloodline of Atlanta's visitation and lodging market. Following

a strong convention year in 2007, which experienced large-scale events such as the National College Athletic Association (NCAA) Final Four Basketball tournament that attracted a total of 963,000 room nights, convention booking activity as of midyear 2008 had declined approximately 5.0%, as large-scale events moved to competitive destinations.<sup>56</sup>

The Atlanta Convention and Visitors Bureau expects additional declines in 2009, as the booking pace decreases based on the cyclical nature of larger conventions. The recessionary environment may also limit corporate travel and events.

**Leisure visitation: introducing new cultural activities and expanding old ones**

Atlanta completed the Georgia Aquarium expansion and the World of Coke museum in 2007, and the city continues to promote new leisure-based cultural activities. Atlanta is scheduled to open the National Museum of

Patriotism in November 2008, which will complement Millennium Gate, recently completed in July 2008.<sup>57</sup> Furthermore, numerous limited-time art exhibitions should continue to attract visitors, including the Titanic Aquatic exhibit at the Georgia Aquarium, the King Tut Great Pharaohs exhibit at the Atlanta Civic Center (November 2008 to May 2009) and the First Emperor of China exhibit (November 2008 to April 2009). The latter two are expected to attract up to 1.5 million visitors total during their stays in Atlanta.<sup>58</sup>

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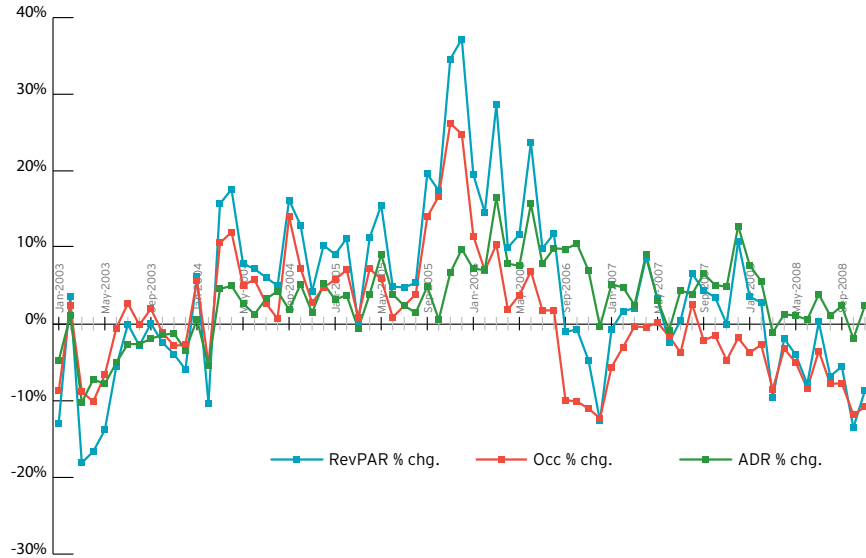
56 Atlanta Convention and Visitors Bureau, <http://www.atlanta.net/> accessed on 1 October 2008.

57 Ibid.

58 Ibid.

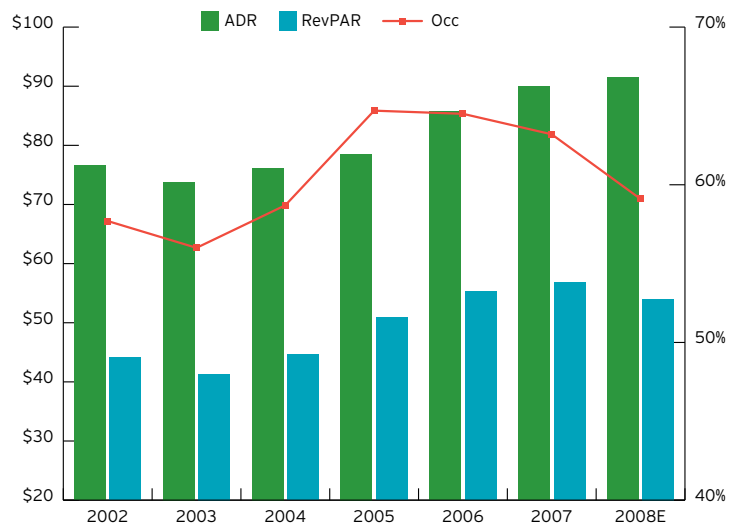
**Atlanta lodging market change  
in monthly occupancy, ADR,  
RevPAR performance**  
January 2003-November 2008E

Source: Smith Travel Research  
Monthly Lodging Review



**Atlanta lodging market  
occupancy, ADR, RevPAR  
performance (USD)**  
2002-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

As one of the larger economic hubs of the southeastern United States, it's not surprising that Atlanta is not immune to the recent economic troubles plaguing the country. The evidence is a continued slump in the city's office sector and limited growth in convention and leisure demand, which have resulted in an overall decrease in occupancy and limited room growth through 2008. While the time it will take for Atlanta to experience RevPAR growth remains unknown, 2009 is expected to be a year in which continued passenger-arrival growth at Atlanta's international airport, coupled with the opening of new, boutique luxury supply and subsequent commercial developments and leisure activities, are expected



to continue to marginally offset any further declines associated with the economy. Furthermore, corporate mergers such as Delta/Northwest, the continued presence of multinational

conglomerates such as Coca-Cola and AT&T and new entrants and expansions such as Rubbermaid are anticipated to drive Atlanta's economy and lodging growth in the midterm.

## Supply additions

Based on year-to-date September 2008 data from Smith Travel Research, the existing hotel supply in Atlanta is approximately 92,100 rooms. The following chart summarizes selected major supply changes:

Property	Submarket	Units	Scheduled opening date	Developer/owner
W Hotel Atlanta Downtown	Downtown, Atlanta, Ga.	237	January 2009	Barry Real Estate Cos.
St. Regis Hotel & Residences @ Two Buckhead Plaza	Buckhead, Atlanta, Ga.	150	March 2009	Rabun Rasche Rector & Reese Architects
Kimpton Hotel Palomar	Midtown, Atlanta, Ga.	304	May 2009	Kim King Associates LLC, Kimpton Hotels & Restaurant Group LLC, Atlanta's Gulch Ventures LLC
Loews Atlanta	Midtown, Atlanta, Ga.	414	April 2010	Daniel Corporation
Marriott Hotel Airport	Hartsville-Jackson International Airport, Atlanta, Ga.	403	May 2010	City of College Park
The Grand Bohemian Atlanta	Perimeter, Atlanta, Ga.	254	June 2010	The Kessler Enterprise, Inc.
InterContinental Atlanta Midtown	Midtown, Atlanta, Ga.	225	December 2011	Shailendra Group LLC
Hilton Atlanta Buckhead	Buckhead, Atlanta, Ga.	300	January 2012	Sandcastle Resorts and Hotels
Mandarin Oriental	Midtown, Atlanta, Ga.	200	2012	Tivoli Properties Inc.

Source: Smith Travel Research

# Boston

## Introduction

Boston is anticipated to experience decreasing RevPAR performance in 2008, driven by decreases in occupancy levels and flat ADR compared to 2007. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 2.1 percentage points to 66.4% in 2008, with ADR increasing 0.1% to US\$152 – resulting in a RevPAR of approximately US\$102, a decrease of 1.6% from 2007.



## Hot topics

### Hotel fundamentals: softening occupancy

Occupancy decreased slightly in 2008 and is expected to continue declining through 2009 due to a slowing economy, increasing unemployment levels, decreasing visitation and additions in room supply.

Population growth slowed to 1.7% in 2007 compared with annual growth of 2.6% from 1990 to 2000, while unemployment levels increased 0.8 percentage points to 5.2% in August 2008 relative to the same period in 2007. Additionally, visitors to Boston decreased, as indicated by Logan International Airport's 5.5% decline in passenger volume year-to-date August 2008 relative to year-to-date August 2007.

While room nights generated from citywide conventions for 2009 are flat in comparison with the same period in 2008, room bookings specifically for the first quarter of 2009 lag the 2008 pace by 56.3%, according to the Greater Boston Convention & Visitors

Bureau. The expected local economic slowdown, driven by the national downturn, should be partially mitigated by the growth of national and worldwide demand for the state's technology-based products and knowledge-based services, including medical devices and life sciences. These industries have helped maintain relatively strong office-market fundamentals despite some recently observed weakness.<sup>59</sup>

### Commercial real estate development: strong despite economic downturn

The Boston Redevelopment Authority reports a total of 60 new commercial and residential projects, worth approximately US\$4 billion, currently under construction, with an additional 250 projects in planning.<sup>60</sup> Major commercial developments planned include office expansions for the life sciences, the medical device sector and the university sector. Specifically, the medical research industry is anticipated to expand its footprint in the Boston area

with a US\$1 billion, 10-year plan to boost Massachusetts' position in life sciences, signed by Governor Deval Patrick in June 2008.<sup>61</sup> As a result, biopharmaceutical company EMD Serono is expected to undergo a US\$50 million expansion of its Billerica facility in northwest Boston,<sup>62</sup> while Siemens Healthcare Diagnostics opened a US\$100 million expansion in Walpole and Covidien Limited is planning an expansion to a 115,000-square-foot building near its corporate headquarters in Mansfield.<sup>63</sup> Despite the expansion plans announced for the near future, the office market is expected to slow due to the softening economy. According to Cushman & Wakefield, Boston's third-quarter 2008 Central Business District Office weighted-average gross rental rate for Class A buildings decreased 24.9% to US\$51 per square foot from midyear 2008, while overall vacancy was 7.0%, an uptick of 0.4 percentage points from midyear 2008. Cushman & Wakefield anticipates asking-rent to be flat in 2008, while vacancy is expected to increase.

59 "Spring 2008 Press Release," The New England Economic Partnership, <http://www.neepecon.org/Press.htm> accessed on 9 October 2008.

60 Scott Van Voorhis, "Building Booms in Boston; 60 Projects Worth US\$4 Billion Going Up," *Boston Herald*, 15 June 2008.

61 Office of the Governor of Massachusetts, <http://www.mass.gov> accessed on 9 October 2008.

62 "EMD Serono Announces Planned Investment of US\$50 Million in Research Center in Massachusetts," *Obesity, Fitness & Wellness Week*, 3 May 2008.

63 Todd Wallack, "Three Firms Planning to Expand in State," *The Boston Globe*, 2 September 2008, and Life Saving Industry Takes a Bow, [nreionline.com](http://nreionline.com), 1 December 2008.



Boston is also experiencing growing demand for new university and hospital facilities. Six million square feet of new dormitories, laboratories and classrooms had been planned, including expansions at Boston College, Suffolk University, Northeastern University and Harvard University.<sup>64</sup> However, the downturn in the financial markets has impacted university endowments. Universities, including Harvard, MIT and Boston University, have announced cost-cutting measures to offset endowment losses. Northeastern University has put on hold its plans for a multimillion-dollar dormitory.

### **New developments post-Big Dig: Fan Pier and Russia Wharf**

The Big Dig, a US\$21.9 billion public transportation infrastructure project, was finally completed in December 2007 after 16 years.<sup>65</sup> Now, one of the most prominent developments in Boston is the US\$3 billion, 21-acre Fan Pier developed in Boston Harbor by Fallon Company. The project includes nine buildings and

encompasses 3 million square feet of first-class office space, luxury residential apartments, a five-star hotel, retail and a six-acre marina.<sup>66</sup> Fan Pier's office tower is scheduled for completion by early 2010, while the development timeline for the remainder of the project has not yet been released (as of January 2009).<sup>67</sup> Additionally, the US\$300 million Russia Wharf, being developed by Boston Properties, is anticipated to include a 32-story, 942,000-square-foot redeveloped tower in downtown Boston and is scheduled for completion in 2011.<sup>68</sup> The project consists primarily of office space, but also includes a 300-room hotel, 50 residential lofts and 27,000 square feet of ground-floor retail space. The improved infrastructure and corporate and leisure developments should increase Boston's attractiveness to visitors.

### **Lifestyle hotels: anticipated new openings**

According to Smith Travel Research, Boston experienced approximately a

3.0% increase in room supply through year-to-date September 2008 versus the same period in 2007, resulting in a total inventory of approximately 50,100 rooms. As of September 2008, approximately 898 additional rooms were under construction, while more than 4,000 rooms were in various planning stages. Lifestyle hotels with a focus on service and design continue to be popular in the Boston lodging market, as evidenced by the recent opening of the 148-room Mandarin Oriental, the 136-room loft Hotel and the 123-room element Hotel. Other lifestyle hotels anticipated to open in 2009 include the 235-room W Hotel in the theater district and the 115-room Ames Hotel (a redevelopment of the historical Byzantine and Romanesque-style office tower built in 1889). The popularity of lifestyle hotels in the Boston market reflects the continued growth in worldwide demand for personalized service and unique design elements.

64 Todd Wallack, "Three Firms Planning to Expand in State," *The Boston Globe*, 2 September 2008.

65 Massachusetts Turnpike Authority, <http://www.masspike.com/bigdig/updates/timeline.html> accessed on 9 October 2008.

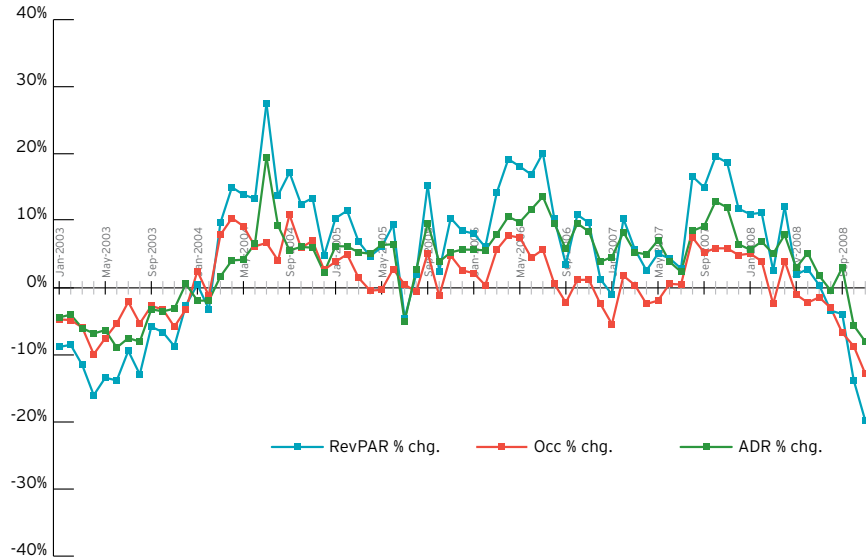
66 The Fallon Company, [www.fanpierboston.com](http://www.fanpierboston.com) accessed on 20 October 2008; and Paul Fournier, "Construction of US\$3 Billion Fan Pier Development Begins on Boston Waterfront," *New England Construction*, 9 October 2007.

67 "Fan Pier: Much Ado about Something," *Boston Daily*, 26 September 2007.

68 Thomas C. Palmer, "Firm in Talks for Russia Wharf Tower," *The Boston Globe*, 28 September 2007; Boston Redevelopment Authority, "Russia Wharf Project Receives BRA Board Approval," *City of Boston Press Release*, 13 May 2004.

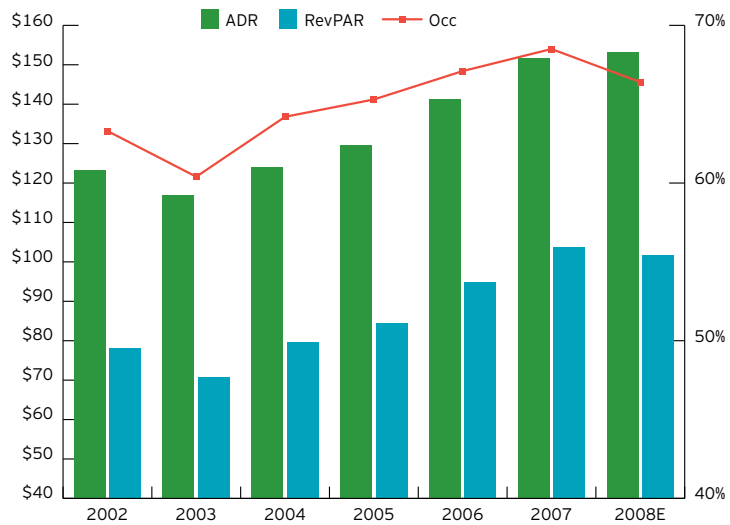
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January 2003-November 2008

Source: Smith Travel Research  
Monthly Lodging Review



**Boston lodging market  
occupancy, ADR, RevPAR  
performance (USD)**  
2002-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Lodging demand has been supported by the completion of the Big Dig surface restoration and the opening of the waterfront Rose Fitzgerald Kennedy Greenway Parks. Several large-scale real estate developments (including hotels) are anticipated to be completed in the next 12 to 24 months. The Fan Pier project and Russia Wharf development

project will energize the waterfront and downtown areas. However, the recent credit-market events may complicate completion of some projects scheduled to open through 2010. In the short term, occupancy and, potentially, ADR in 2009 will continue to struggle given the increase in rooms supply.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
The Ames Hotel	Downtown, Boston, Mass.	115	May 2009	O'Callaghan Hotels
Unnamed hotel, mixed-use	South Station, Boston, Mass.	200	June 2009	Gerald D. Hines Interests
W Hotel Boston	Theater District, Boston, Mass.	235	August 2009	Sawyer Enterprises
Residence Inn Boston Northeastern University	Fenway-Kenmore, Boston, Mass.	186	June 2010	Northeastern University
Waterside Place Condotel	South Boston/Waterfront, Boston, Mass.	300	June 2010	Core Development Group LLC
Unnamed hotel	Downtown Crossing, Boston, Mass.	250	August 2010	The Gale Company (Boston)
Unnamed hotel	Columbus Center, Boston, Mass.	192	June 2011	Winn Development
Homewood Suites Boston Fenway Park	Fenway-Kenmore, Boston, Mass.	100	July 2011	Boston Red Sox
Congress Street Hotel	South Boston/Waterfront, Boston, Mass.	505	TBD	Madison Properties
Fan Pier Hotel	South Boston/Waterfront, Boston, Mass.	150	TBD	Fallon Company
Hard Rock Hotel Boston	Beacon Hill, Boston, Mass.	Not available	Not available	Seminole Hard Rock Cafe International Corp. Headquarters

Source: Smith Travel Research

# Chicago

## Introduction

The Chicago lodging market experienced a slowdown in 2008 largely due to a decline in business and leisure travel. This downward trend is projected to continue through 2009. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 4.2 percentage points to 63.5% in 2008 while ADR is expected to increase 0.3% to US\$130, resulting in a RevPAR of approximately US\$83 – a decrease of 4.7% from 2007.



## Hot topics

### Chicago economy: taking a major hit

As with other cities throughout the US, Chicago's economy faced numerous challenges in 2008, including rising unemployment rates, a significant budget shortfall and increased home foreclosures. Unemployment rates in Chicago reached 7.4% in October, representing a 1.9 percentage point increase over the previous year.<sup>69</sup> The city's financial sector in particular suffered a major hit, as approximately 8,900 jobs were lost between January and September 2008 before the banking meltdown – representing 2.2% of local financial services positions. According to Moody's Economy, Chicago's unemployment rate may climb to 8.4% in 2009 as worsening economic conditions may cause the city to lose a net of 43,000 jobs.<sup>70</sup> The city's US\$469 million budget shortfall

that arose from decreasing city tax revenues in 2008 will likely contribute to these losses.<sup>71</sup> According to Chicago Mayor Richard Daley, Chicago will lay off approximately 929 city workers in order to bridge the budget gap in 2009.<sup>72</sup> The situation, however, may be mitigated by the Chicago City Council's recent approval of the leasing of Chicago's metered parking system to a private operator for more than US\$1.1 billion.<sup>73</sup> To date, the council has already approved a US\$2.5 billion lease of Midway Airport, which is anticipated to close by early 2009, and a US\$2 billion lease of the Chicago Skyway.<sup>74</sup> Chicago also experienced a significant rise in home foreclosures in 2008. According to Woodstock Institute, home foreclosures in Chicago will likely increase approximately 40.0% to more than 53,000 homes in foreclosure.<sup>75</sup>

### O'Hare International and Midway Airport: declines in flights and passenger traffic

Amid rising fuel costs and a slowing economy, Chicago's two major airports – O'Hare International and Midway Airport – experienced significant declines in passenger traffic and capacity between January and September 2008. Passenger traffic and capacity declined 7.0% and 4.0%, respectively, at O'Hare, while at Midway they declined 9.0% and 13.0%, respectively. The city is projecting that both passenger traffic and capacity will continue this downward trend through 2009 and decline 3.0% each, although this estimate may prove to be too optimistic. In 2009, expenses at O'Hare and Midway are anticipated to increase 9.0% and 5.0%, respectively – a burden that will have to be shouldered by airlines in the form of higher landing fees. These higher fees will potentially

69 Illinois Department of Employment Security, <http://lmi.ides.state.il.us/laus/ratecity.htm> accessed on 1 December 2008.

70 John Pletz, "No Relief Until 2010; Widespread Recession is Poised to Rock Virtually Every Segment of Local Economy," *Chicago Business*, 20 October 2008.

71 Hal Dardick, "Daley Budget Includes Rosier View of Economy: \$6 Billion Spending Plan Heads to City Council," *Chicago Tribune*, 14 November 2008.

72 Fran Spielman, "Chicago: the City That Won't Work; Mayor Says Business Leaders Expect Blizzard of Layoffs and That's Just the Beginning," *Chicago Sun-Times*, 13 November 2008.

73 "Chicago Aldermen Approve \$1.1 Billion Parking Meter Lease to Help Weather Economy," Associated Press, 4 December 2008.

74 Deanna Bellandi, "Chicago to Get Almost \$1.2 Billion in Meter Lease," *The Associated Press*, 2 December 2008.

75 Becky Yerak, "Chicago Foreclosures Projected to Rise 40% for 2008," *Chicago Tribune*, 4 December 2008.



force airlines to continue to reduce flights, depressing passenger traffic even more.<sup>76</sup> Additionally, increasing costs for airlines may further delay O'Hare's planned expansion. In the early 2000s, airlines agreed to finance the first phase of the expansion project; but they have not yet agreed to finance the final phase, which has been estimated to cost approximately US\$5 billion.<sup>77</sup> The expansion project would add new runways and terminals to O'Hare, which would significantly reduce delays at the airport as well as increase passenger and visitor capacity to the city.

#### **Lodging demand: business demand decreasing, but convention demand remains strong**

Although the Chicago office market remained strong in 2008 – with vacancy rates decreasing to 10.7% during the third quarter and lease rates increasing to US\$33 – hoteliers in downtown Chicago are reporting a noticeable

decline in demand by business travelers, who, along with trade show visitors, account for approximately 80.0% of hotel bookings in this submarket.<sup>78</sup> This decline can be attributed to tighter corporate expense budgets, higher airfares and a slowing economy, all of which are forcing companies to shorten their lengths of stay or cancel meetings altogether in order to reduce costs. Average spending on functions has also declined, due to lower expenditures on items such as food and beverage.<sup>79</sup> This trend is anticipated to continue as the national and local economies remain soft. Despite the decline in corporate demand, however, convention-related hotel bookings are projected to rise from 2007 levels over the next two years, according to the Chicago Convention and Tourism Bureau (CCTB).<sup>80</sup> Attendance numbers for 2009 have not yet been released by the CCTB, but are anticipated to be stronger than 2008 due to the

cyclical nature of the industry. As of November 2008, hotel reservations for 2009's trade shows were 3.0% greater than total bookings for 2008.<sup>81</sup>

#### **Hotel occupancy: supply outpaces demand**

Although lodging demand in Chicago is expected to increase modestly during the next few years, new supply should outpace demand, providing yet another challenge for Chicago hotels and their occupancy rates. Between 2009 and 2011, approximately 7,200 rooms will potentially be added to the Chicago market, representing a 19.8% increase in supply. Demand, however, as measured by room nights is only anticipated to increase 9.8%.<sup>82</sup>

#### **Olympic dreams: Chicago a top-four finalist**

Selected as one of four cities to host the 2016 Summer Olympics, Chicago will vie for the coveted position against Tokyo,

76 John Pletz, "Airport Expenses Climb," *Chicago Business*, 27 October 2008.

77 Michael Tarm, "Airline Industry Woes Threaten O'Hare Expansion," Associated Press, 9 August 2008.

78 Bob Tita, "Local hotels brace for downturn," *Chicago Business*, 31 March 2008.

79 Alby Gallun, "Travel cuts to hit downtown hotels," *Chicago Business*, 13 October 2008.

80 Kathy Bergen, "Hotels Feeling Chill in Tourism: High Fares, Economic Woes Deter Travelers," *Chicago Tribune*, 2 July 2008.

81 Bob Tita, "Travel Tears; Corporate Cuts Foreshadow Gloom for Hotels, Conventions," *Chicago Business*, 17 November 2008.

82 Alby Gallun, "Hotel Occupancy to Drop," *Chicago Business*, 18 August 2008.

Madrid and Rio de Janeiro through 2 October 2009.<sup>83</sup> According to a study conducted by the University of Illinois at Urbana-Champaign in 2006, a 2016 Chicago Olympiad could produce an estimated US\$5 billion in economic activity for the city and generate

about 81,000 jobs.<sup>84</sup> Furthermore, the Olympic spotlight could improve the city's transportation infrastructure, parks, athletic facilities and housing, as it did in Beijing. It could also provide Chicago international exposure, opening doors for the city to lure international

visitors long after the games are over. Hotels in the Chicago area have begun to sign contracts committing them to reserve 85.0% of their rooms for the Olympics, should Chicago be chosen as the host city.<sup>85</sup>

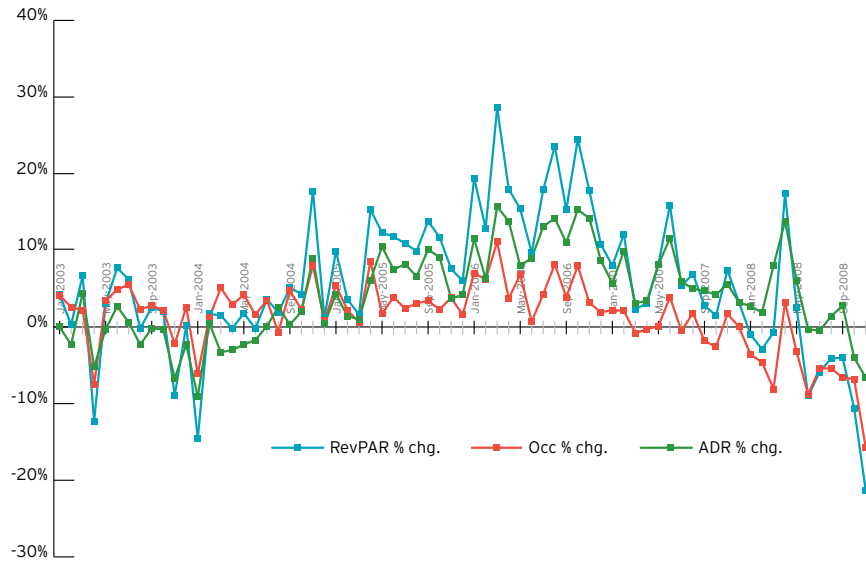
83 "Chicago's Olympic Potential," *Chicago Tribune*, 1 September 2008.

84 Gregory Meyer, "What Would Olympics Really Bring Chicago," *Chicago Business*, 9 October 2006.

85 "Chicago Area Hotels Commit Rooms to 2016 Games," Associated Press, 17 August 2008.

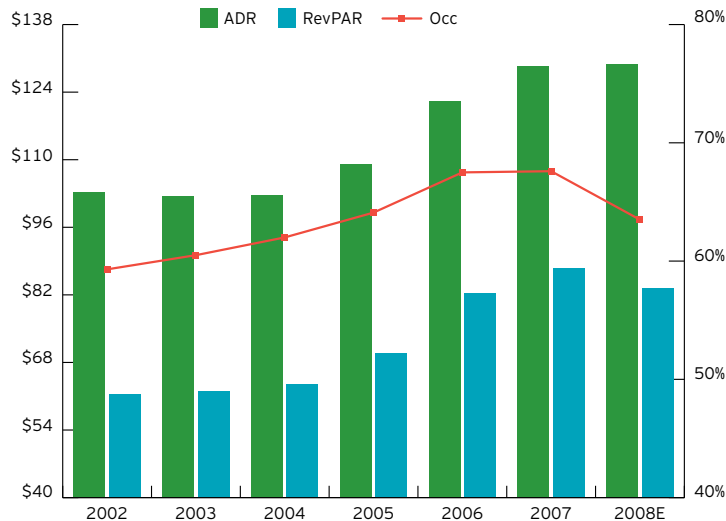
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2002-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Chicago will likely experience a slowdown in lodging fundamentals in 2009 as a result of lower hotel demand from business and leisure travelers, coupled with significant increases in supply. A strong convention season, however, is expected to help support the market.



## Supply additions

Based on year-to-date September 2008 data from Smith Travel Research, the existing hotel supply in Chicago is estimated at 104,266. The following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
Hotel Felix	Chicago, Ill.	225	January 2009	Oxford Capital Partners
Elysian Hotel & Residences	Chicago, Ill.	188	April 2009	Elysian Development Group LLC
Doubletree Hotel Chicago The Wit	Chicago, Ill.	298	May 2009	ECD Company Inc.
aloft Hotel Bolingbrook	Bolingbrook, Ill.	155	July 2009	LTD Management Co.
Four Points by Sheraton Chicago O'Hare	Chicago, Ill.	287	July 2009	Unknown
Staybridge Suites Des Plaines	Des Plaines, Ill.	176	August 2009	The Harp Group
element Chicago O'Hare Airport	Chicago, Ill.	320	October 2009	Starwood Hotels and Resorts Worldwide
Staybridge Suites Chicago	Chicago, Ill.	200	October 2009	Dellisart Lodging LLC
Hyatt Place Warrenville	Warrenville, Ill.	123	November 2009	Corporex Development Services
Hyatt Summerfield Suites Warrenville	Warrenville, Ill.	123	November 2009	Corporex Development Services
Hyatt Place Northbrook	Northbrook, Ill.	145	March 2010	EAG Capital Holdings
Shangri-La Chicago	Chicago, Ill.	222	May 2010	Teng & Associates
aloft Hotel Chicago City Center	Chicago, Ill.	274	July 2011	Friedman Properties Ltd
Mandarin Oriental Chicago	Chicago, Ill.	250	December 2011	Solomon Cordwell Buenz & Assoc. Inc.
Hyatt Regency McCormick Place Addition	Chicago, Ill.	594	TBD	Thompson Ventulett Stainback & Associates
Conrad Hotel Rosemont	Rosemont, Ill.	255	TBD	Not Available

Source: Smith Travel Research

# Dallas



## Introduction

The Dallas lodging market has experienced steady lodging fundamentals in 2008. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 1.1 percentage points to 59.2% in 2008. ADR is projected to remain relatively stable at US\$94, resulting in a RevPAR of approximately US\$56 – an increase of 0.7% from 2007.

## Hot topics

### Convention hotel: controversial project in the works

The city of Dallas acquired an eight-acre, US\$42 million tract of land for the construction of a publicly owned convention hotel. The proposed hotel would be attached to the existing convention center, with an overall cost of approximately US\$500 million. Marriott and Omni have both submitted proposals to operate the 1,000 room hotel and 100,000-square-foot conference space. Despite the benefits that a convention hotel may bring in the form of strengthening convention bookings, the project is encountering opposition as local hoteliers fear cannibalization of existing lodging demand. Meanwhile, there are 200 definite meeting and convention bookings scheduled for 2009 and an additional tentative 298 events, as reported by the Convention and Visitors Bureau (CVB). In 2007, the CVB reported a total of 603 meetings and conventions. With an active convention calendar, Dallas is currently the only top-20 domestic convention-market destination lacking a dedicated

convention-center hotel. Nearby Fort Worth's US\$213 million, privately owned convention hotel was inaugurated in December 2008, and it is expected to pose additional competition to the Dallas convention market.<sup>86</sup>

### Dallas entertainment: new leisure venues are underway

A reviving sports, cultural and art scene is anticipated to provide further visibility to the Dallas metropolitan area and boost leisure demand. The Dallas Center for the Performing Arts in the downtown Dallas Arts District comprises the Margot and Bill Winspear Opera House, the Dee and Charles Wyly Theatre, the Annette Strauss Artist Square and the Performance Park, and is scheduled to open in October 2009. This multivenue facility, located adjacent to the existing Morton H. Meyerson Symphony Center, will comprise centers for music, opera, theatre and dance.

The US\$1.1 billion new Dallas Cowboys stadium in Arlington, scheduled to open in 2009, has already booked a number of high-visibility events, including the

2010 NBA All-Star Game, the 2011 Super Bowl and the 2014 NCAA Men's Basketball Final Four, keeping pace with owner Jerry Jones' vision of a multiuse stadium. The 80,000-seat facility could be expanded to 100,000 seats during major events.

### Office demand: downtown Dallas benefits from lack of a supply pipeline

Office demand in the Dallas-Fort Worth area closed the third quarter of 2008 slightly above the same period in 2007. The most recent data available from Cushman & Wakefield suggests that net office leasing in the Commercial Business District (CBD) improved significantly in the third quarter of 2008, at 2.7 million square feet of space versus 1.0 million square feet for the first and second quarters combined.<sup>87</sup> The CBD has an inventory of nearly 29 million square feet of space, no new inventory in the pipeline and vacancy rates at 26.5% throughout the third quarter of 2008. This rate compares favorably to an overall vacancy of 30.3% at the end of 2007. Declining

<sup>86</sup> Sam Merten. "Dallas Convention Center Hotel's Murky Future," *Dallas Observer*, 25 September 2008.

<sup>87</sup> "Market Beat: Dallas Office Report," Cushman & Wakefield, Second and Third Quarters 2008.



office vacancy levels are a positive trend in the CBD and bode well for hotels situated in the immediate vicinity; however, office demand in the overall Dallas metropolitan area is expected to slow in 2009, in the midst of corporate retraction.

#### **Corporations relocate to Dallas: increase in temporary lodging**

Dallas offers several competitive advantages that typically push its name into the short list of companies looking to relocate: low business costs; central US location and airport hub; fourth-largest metropolitan area in the US; and home to 25 Fortune 500 companies.<sup>88</sup> Two major relocations are underway in 2008 – AT&T and Research in Motion (RIM). RIM, maker of the BlackBerry, is anticipated to relocate more than 1,000 people, while AT&T is expected to relocate 700 employees from its corporate headquarters. In 2009, additional relocations to downtown Dallas include Tenet Healthcare, Clark Consulting and a regional office of Capital One. Corporate

relocations may generate temporary lodging demand while employees search for housing and increase the local business base generating out-of-town business for local hotels.

#### **Airport trends: turbulent times**

Corporate revisions of travel policies, lower demand from leisure travelers, fare increases and uncertainty about the future of fuel costs have all converged to cause airlines to reduce seat inventory. A recent study by USA Today predicts that the Dallas-Fort Worth (DFW) and Love Field Airports will experience an estimated decrease of 9.3% and 4.3%, respectively, in seating capacity as of the end of 2008. American Airlines and American Eagle will be eliminating 42 flights, while KLM is cutting back on a recently added schedule from DFW to Amsterdam – from seven to five flights per week.<sup>89</sup> Other airlines are reportedly following the same trends. Less passengers translates to lower revenue from passenger facility charges, parking fees and food and retail concessions,

impacting the airports' operating budget and capital projects.<sup>90</sup> Dallas lodging demand may be adversely affected by reduced airline seat inventory.

In addition, Love Field Airport, owned by the City of Dallas and primarily occupied by Southwest Airlines, has a six-year, US\$500-US\$600 million terminal modernization project in the works, scheduled for completion in 2014. The project will be partially financed through lease revenue bonds, with the first bond issuance taking place in September 2009.<sup>91</sup> With more than 50 limited and full-service hotels located within five miles of Love Field Airport, lodging demand is anticipated to experience positive fundamentals in the long term.

#### **Public transportation: new developments by 2013**

Despite high construction costs, Dallas is one of several cities in the west and southwest, including Phoenix, Salt Lake City and Denver, investing in a rail system. Dallas-Fort Worth Airport will

88 Sheryl Kean, "Businesses Want to Be in Big D Location," *The Dallas Morning News*, 16 April 2008.

89 "KLM to Cut Back DFW Flights to save Money," *The Fort Worth Star Telegram*, 8 August 2008.

90 "Years of Growth Over for Many US Airports," Associated Press, 11 August 2008.

91 "Dallas Forming New Entity to Issue US\$300M for Love Field," *The Bond Buyer*, 25 June 2008.

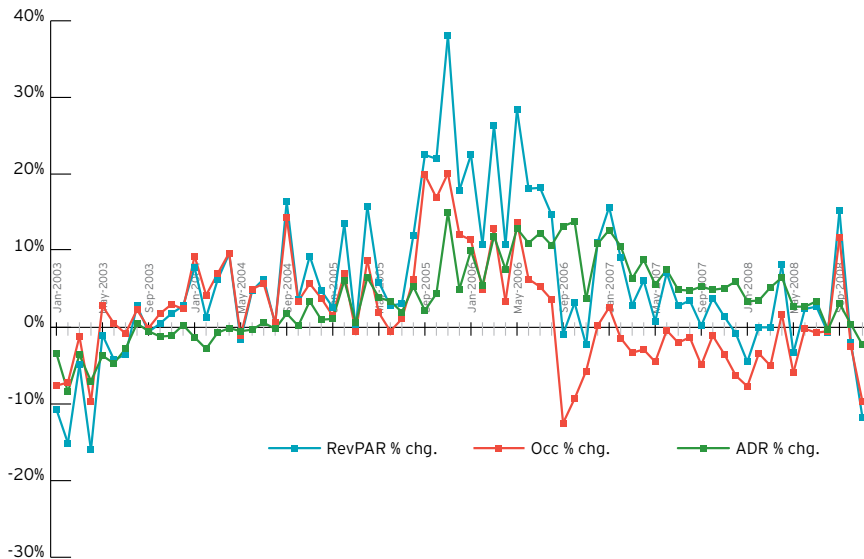
be connected to the Dallas Area Rapid Transit (DART) Authority's new rail line to downtown and east Dallas, via Irving. A second rail line connecting west Dallas to DFW airport and the DART is being planned by the Fort Worth Transit Authority. A new rail line, known as the Green Line, which crosses the western

part of Dallas's Love Field Airport, is also anticipated to be connected to the DART by bus service. DART currently operates 45 miles of rail network; the planned expansion would bring its total area of coverage to 91 miles by 2013. Finally, the City of Dallas long-term plan for Love Field Airport includes the

construction of a rail system to substitute most shuttle buses. At a macro level, the expansion and modernization of the city's transportation system should have a positive impact on the city's ability to continue to attract corporate relocations and convention business, resulting in increased hotel demand.

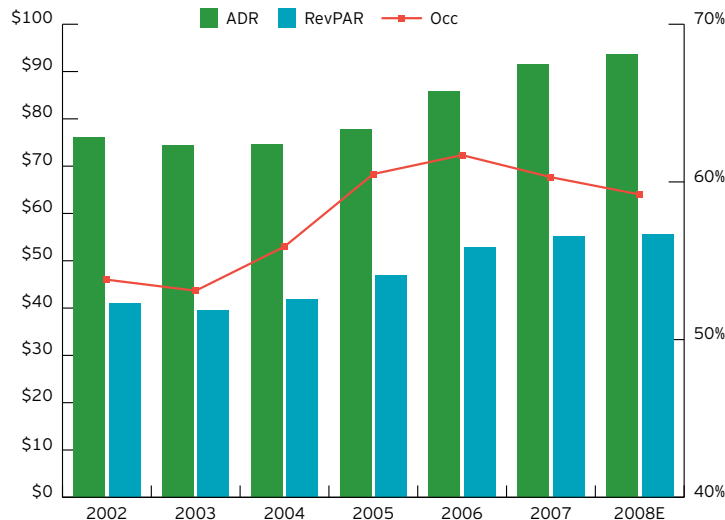
**Dallas lodging market change in monthly occupancy, ADR, RevPAR performance**  
**January 2003-November 2008**

Source: Smith Travel Research  
 Monthly Lodging Review



**Dallas lodging market occupancy, ADR, RevPAR performance (USD)**  
**2002-2008E**

Source: Smith Travel Research  
 Monthly Lodging Review



## Key takeaways

Despite a nationwide economic slowdown, Dallas continues to bolster strong convention center activity, as confirmed by the City of Dallas' dedicated efforts to build a new convention hotel. The city also commands a strong business segment, as substantiated by the continued interest in the downtown area by companies looking to relocate to Dallas, as well as a declining office vacancy rate downtown. The city is further investing in the expansion and modernization of its rail transit lines, which bodes well for its continued success in attracting corporate relocations and convention business. Finally, current economic conditions, which had a negative impact on airline seating capacity, may pose a small setback for short-term future lodging demand growth.



## Supply additions

Based on year-to-date September 2008 data by Smith Travel Research, the following chart summarizes selected major supply changes from 2009 through 2010. It should be noted that construction on the Mandarin Oriental, Westin and Crowne Plaza hotels has been delayed due to the economic slowdown.

Property	Location	Units	Scheduled opening date	Developer/owner
Renaissance	Plano, Texas	276	November 2010	Jackson-Shaw Co.
Mandarin Oriental	Victory Park, Texas	139	On Hold	Hillwood Development
Westin	McKinney, Texas	211	On Hold	City of McKinney
Crowne Plaza	Frisco, Texas	141	On Hold	Atlantic Hotels Group
Downtown Convention Hotel	Dallas, Texas	1,000	Not available	City of Dallas

Source: Smith Travel Research and Dallas Convention and Visitors Bureau

# Fort Lauderdale

## Introduction

The increasing cost of living in South Florida, given the past years' rising costs of real estate and insurance, continues to deter business expansion in the short term for Fort Lauderdale. However, infrastructure expansion plans, continued international interest, an extended period of minimal tropical storm activity and stronger efforts marketed to drive-to markets are anticipated to enhance Fort Lauderdale's overall visibility. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 1.4 percentage points to 64.7% in 2008, with an ADR increase of 1.1% to US\$168, resulting in a RevPAR of approximately US\$108 – an decrease of 1.0% over 2007.



## Hot topics

### Convention center hotel a long time coming

After a 20 year effort to develop a convention hotel, Hilton Hotels was awarded the management contract for the 1,000-room upscale hotel adjoining the Broward County Convention Center. The property, slated for a mid-2011 opening, is expected to be the host hotel for the estimated 280 annual events that have historically relied upon as many as 50 different hotels throughout the county.<sup>92</sup> While news of the long-awaited hotel has generated increased interest on the part of meeting planners, project financing continues to be a concern, casting doubt upon the scheduled opening date.

### Visitation: a greater global presence

Broward County officials estimate approximately 11 million visitors in 2008, an increase of 2.8% from the prior year.<sup>93</sup> The Convention and Visitor's Bureau (CVB) attributed the rise to the weakness of the dollar in 2008, further driving international visitation from Europe and Canada. For the first half of 2008, domestic visitation decreased by 1.2% while international visitors increased 8.2%, resulting in a net gain of 3.0%.<sup>94</sup> Fort Lauderdale has traditionally been able to mitigate domestic declines with a strong international presence, as evidenced by a projected 4.0% rise in hotel-tax revenue in 2008, aided by the weak dollar and new international air service to Fort Lauderdale-Hollywood

International Airport (FLL).<sup>95</sup> Nevertheless, the economic slowdown is threatening domestic tourism-driven revenue, as Fort Lauderdale is a popular driving destination and easily accessible via lower-priced airlines. Canada continues to be the primary international feeder market for Fort Lauderdale, and is expected to account for more than 30.0% of total visitation to the city in 2008 – more than the top three Latin American feeder markets combined.

### Port Everglades and FLL ... together at last?

Broward County remains optimistic about the proposed US\$1.4 billion transportation project connecting Port Everglades to FLL, which is expected to boost tourism and alleviate traffic

92 Scott Wyman, "Hilton favored for hotel at port. 27-story convention center complex beats out Marriott," *South Florida Sun-Sentinel*, 2 November 2007.

93 Terry Sheridan, "Weak dollar should strengthen surge in international visitors," *Broward Daily Business Review*, 14 January 2008.

94 Scott Andron, "Can Florida economy take a double whammy?" *The Miami Herald*, 19 October 2008.

95 Ibid.



from congested thoroughfares.<sup>96</sup> The project, as currently envisioned, includes an automated People Mover beginning at the airport and eventually extending to Port Everglades. Port Everglades remains a premier international port, due both to its growing containerized-cargo business and to Royal Caribbean Cruise Line making it the home port for two new vessels. The ships accommodate 5,400 passengers each, with the first one scheduled to set sail in late 2009 and the second in 2010. In addition, access to Fort Lauderdale continues to be complemented by the choice of Miami International Airport as an alternate port of entry for Fort Lauderdale-bound tourists, enhancing access to the area despite the reported reductions at FLL by the major airlines. With United Airlines

ceasing operations in FLL and carriers such as American, Delta and Continental expected to reduce more flights, total availability is estimated to decline 10.0%. The short-term outlook remains mixed, as the anticipated increases in cruise traffic and planned infrastructure enhancements are not projected to completely offset the reduction in air arrivals.

#### **New lodging enhances destination positioning**

Fort Lauderdale continues to position itself as an upscale destination. More than one year after its opening in early 2007, the St. Regis was reflagged to a Ritz-Carlton, following a lawsuit over a contractual dispute between Starwood and the developer. Blackstone and Hilton Hotels announced the development of Bahia Mar as a combination Waldorf-

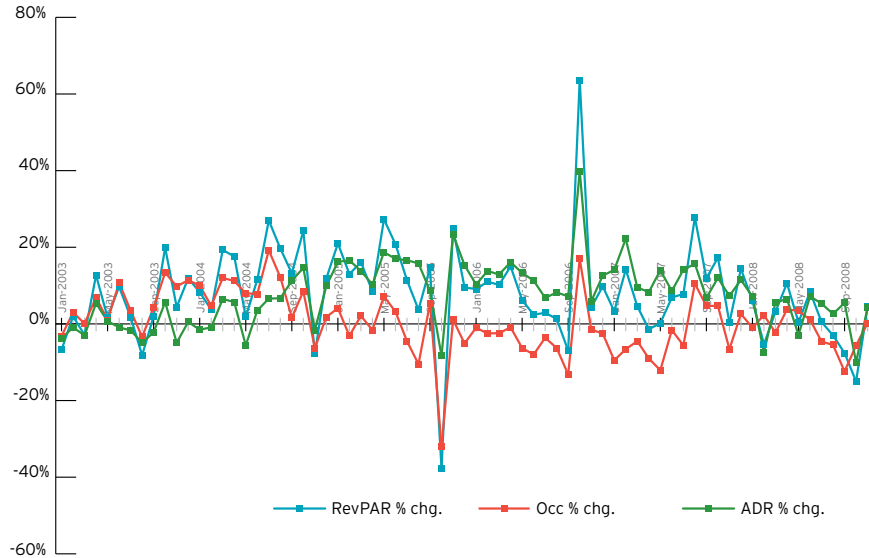
Astoria and Hilton, while the Sheraton Yankee Trader Hotel, a long-time landmark in Fort Lauderdale, is scheduled to reopen in early 2009 as the 433-room Westin Beach Resort. The W and Trump International Hotels are well underway to open in 2009, though some skepticism remains – they both feature condominium-hotel components, and this asset class faces many problems in light of operating and marketing complexities and the volatile real estate market. In an effort to mitigate the dependency on hotel-driven businesses, campaigns such as Spa Chic and Dine Out Fort Lauderdale try to attract local demand during the slow season by showcasing top spas and restaurants with reduced prices from October to December.

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<sup>96</sup> Todd Wright, "Airport-seaport transit plan alive; a new elevated system between the airport and Port Everglades could boost tourism in Broward and ease traffic on local roads," *The Miami Herald*, 7 January 2008.

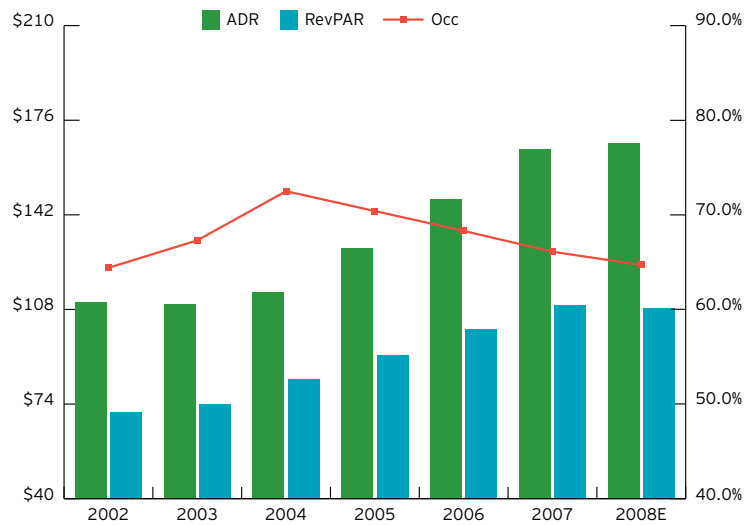
**Fort Lauderdale lodging market  
change in monthly occupancy,  
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Source: Smith Travel Research  
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**Fort Lauderdale lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2002-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Economic pressure, concern about real estate market conditions and airlift reductions are anticipated to continue in 2009 in Fort Lauderdale. Nevertheless, the city continues to position itself as a more upscale destination, as evidenced by the recent arrival of upscale and luxury brands. The increase in supply anticipated in 2009, however, will create significant pressure on the lodging market, which may be impacted despite continued efforts to attract international travelers, convention attendees and Florida residents.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2010.

Property	Location	Units	Scheduled opening date	Developer/owner
W Hotel & Residences	Fort Lauderdale, Fla.	346	January 2009	Sable Resorts
Westin Beach Resort (Formerly Sheraton Yankee Trader)	Fort Lauderdale, Fla.	433	January 2009	Starwood Capital Group Global, LLC
Trump International Hotel & Tower	Fort Lauderdale Beach, Fla.	298	April 2009	Stillman Organization LTD
Crowne Plaza	Fort Lauderdale, Fla.	150	June 2009	Sanjaynumar Patel
Waldorf-Astoria	Fort Lauderdale, Fla.	TBD	TBD	Blackstone
Hilton	Fort Lauderdale, Fla.	TBD	TBD	Blackstone

Source: Smith Travel Research, company websites

# Hawaii

## Introduction

The Hawaii lodging market experienced negative lodging fundamentals in 2008 due to the general economic downturn and a weak performance during the traditionally high summer season. Japanese tourists and visitors from the US West Coast have historically been two large sources of visitors to Hawaii, but decreases in their numbers have worsened Hawaii's lodging problems. Combined with a reduction in the number of airlines that offer travel to Hawaii, the islands have seen a significant decrease in tourism activity. Based on year-to-date November data from Smith Travel Research, overall occupancy is anticipated to decrease 4.5 percentage points to 70.8% in 2008, with ADR increasing by 1.0% to US\$202 – resulting in a RevPAR decrease of 5.0% to US\$143.

## Hot topics

### Hawaii: declining economic growth

Hawaii's economy continued to decline through the third quarter of 2008, largely due to worsening national economic conditions and the lack of visitor industry activity in the state. The unemployment rate in Hawaii was 3.7% as of October 2008, an increase of 1.1 percentage points compared with the prior year. Furthermore, the number of bankruptcy filings increased by approximately 33.7% through July 2008, resulting in decreasing wealth and declining lodging demand. However, despite the economic slowdown, the military remains a significant contributor to the Hawaiian economy, and military spending as of late 2008 increased approximately 8.4% from the same period in the prior year.<sup>97</sup>

### Room rates: strong lodging market despite room discounts

With higher airfares and reductions in flight capacity, hotels in Hawaii have offered bargain room rates and incentives in order to attract tourists to the island. Several hotels have offered discounted rates for 30% to 40% of their rooms, where in the same period last year they discounted only 15% to 20%.<sup>98</sup> Total visitor spending, excluding visitors by ship, decreased 8.5% through year-to-date October 2008 compared with the same period in 2007, largely due to declines in room rates.<sup>99</sup> In an effort to maintain occupancy levels, hotel operators are decreasing their ADRs to attract visitors – year-to-date November 2008 occupancy declined to 4.1 percentage points to 71.3% from 75.4% for the same period in 2007, according to Smith Travel Research. While performance in the US lodging market



has slowed relative to 2007, Hawaii's lodging market compares favorably to other US markets, ranking second in ADR and RevPAR behind New York.

### Airline failures: ATA Airlines, Aloha Airlines

Aloha Airlines and ATA Airlines ceased operations and cancelled all current and future flights in March and April 2008, respectively. Unable to absorb the high cost of fuel, both airlines declared bankruptcy. Combined, the two airlines accounted for 15% of the passenger seats available between Hawaii and the mainland. ATA ended service to four mainland cities, and Aloha, the island's second largest carrier, discontinued service to six mainland cities. Hawaiian Airlines and Mesa Air Group each announced plans to add planes and flights on routes within Hawaii to help make up for the loss of the bankrupt

97 Hawaii State Department of Business, Economic Development & Tourism, *Quarterly Statistical & Economic Report, 4th Quarter 2008*, <http://www.hawaii.gov/dbedt/info/economic/> accessed on 15 October 2008.

98 Candace Jackson, "Travel slumping, hotel deals jumping; As airline prices rise and occupancy falls, resorts woo bargain-hunting vacationers," *The Charlotte Observer*, 7 September 2008.

99 Hawaii State Department of Business, Economic Development & Tourism, "Month Visitor Statistics," October 2008, <http://hawaii.gov/dbedt/info/visitor-stats/tourism/> accessed on 12 November 2008.



airlines.<sup>100</sup> Largely due to the collapse of ATA and Aloha, Hawaii has experienced a 30.1% reduction in capacity, the largest decrease in flight capacity in the nation. Compared with figures from 2007, November schedules this year indicate a 28.2% total reduction in capacity at Honolulu Oahu International Airport, Hawaii's largest airport by total number of seats. This is the largest loss among major US airports.<sup>101</sup>

### **Cruise lines: a declining industry in Hawaii**

Two major events negatively impacted the Hawaiian cruise industry in 2008. Norwegian Cruise Lines (NCL) ended its four-year effort to dominate the cruise industry in Hawaii, transferring its 2,224-passenger *Pride of Hawaii* to Europe and its 2,002-passenger *Pride of Aloha* to Star Cruises, NCL's Asia-based sister company.<sup>102</sup> The US and international cruise ship industry struggled in 2008,

with the total number of visitors arriving in Hawaii by cruise ship decreasing 21.8% to 82,000 (year-to-date October 2008).<sup>103</sup> In addition, the redefining of a maritime law by US Customs and Border Protection would require ships to spend at least half of each cruise itinerary in ports outside the US and at least 48 hours at each stop. This would significantly increase the duration of cruises, including cruises to Hawaii, due to extended foreign port call requirements. As many tourists are accustomed to cruise durations of three to five days, this rule change would adversely affect the vacation plans of many cruise travelers, disrupting the nation's cruise industry and jeopardizing future economic plans for cruise facilities.<sup>104</sup>

### **Origin of visitors: international and domestic travelers**

Overall visitor arrivals in Hawaii in 2008 totaled 5.7 million through year-to-date October 2008, a 9.7% decrease from October 2007 and the lowest level since 2001. Year-end 2008 projections indicate that Hawaii will see a 6.7% decrease in visitor arrivals and a 6.4% decrease in visitor expenditures in 2008. Projections for 2009 are more positive, indicating a 0.8% decrease in visitor arrivals and a 2.9% increase in visitor expenditures due to the decline in crude oil prices, steady federal and military spending and overall growth in construction.<sup>105</sup> As of mid-September 2008, domestic arrivals have been down 19.5%. Due to rising airfares, Hawaii has experienced a significant decrease in visitors flying in from the US West Coast, historically a strong source of visitors. International arrivals have declined

100 "Hawaiian Air boosts service after rivals collapse," Associated Press, 4 April 2008.

101 "Airline schedule changes at 300 U.S. airports," *USA Today*.

102 "NCL yanks another cruise ship from Hawaii," *USA Today*, 19 September 2008.

103 Hawaii State Department of Business, Economic Development & Tourism, "Month Visitor Statistics," <http://hawaii.gov/dbedt/info/visitor-stats/tourism/> accessed on 15 November 2008.

104 "Proposed rule change would hurt US cruise vacationers, ports, and cities," *States News Service*, 23 January 2008.

105 "New Hawaii economic forecasts see brighter future," Associated Press, 18 August 2008.

13.9% as of mid-September 2008.<sup>106</sup> But despite the decrease in arrivals and the strengthening dollar, Japan and Canada continue to be the two largest sources of foreign visitors to the island. As of October 2008, approximately 977,000 visitors arrived from Japan and 270,000 visitors arrived from Canada, representing a 9.0% decrease and 7.7% increase, respectively, through year-to-date October 2008 compared with the same period in 2007. Although visitation from Japan has decreased in 2008, Japanese visitors continue to spend the most per capita on a daily basis – US\$281 per person, an increase of 5.9% from the same time period in 2007.<sup>107</sup>

#### **Visa waiver program: more South Korean and Chinese visitors**

Japanese visitors are foregoing Hawaii in favor of new, lower-cost destinations, such as Taiwan. With a decrease in Japanese visitors this year, Hawaiian officials are positioning the island to capture more visitation from China and South Korea.<sup>108</sup> President Bush signed a law in 2007 that allows more countries to qualify for visa waivers, and tourism officials are optimistic that South Korea will qualify for a visa-waiver after the implementation of an enhanced exit program for foreign nationals scheduled to come online in mid-2009. Furthermore, a recently signed agreement with China now allows US companies to actively market travel between the US and China. Although Chinese visitors planning to enter the

US are required to apply for a visa, the new agreement eliminates restrictions on leisure travel, allows Chinese tourists to travel freely and increases Hawaii's ability to bring more Chinese visitors to the islands.<sup>109</sup>

#### **Convention center bookings stable for now**

Spurred by the bankruptcy of two major airlines and rising energy prices, the increased cost of air travel has taken a toll on convention visitor traffic to Hawaii. However, the Hawaii Tourism Authority does not see a trend toward large groups canceling their bookings. Furthermore, bookings have continued as Hawaii attracts business planned for the short term. For example, groups from Sun Microsystems and Best Western scheduled conventions at the Hawaii Convention Center in October 2008,<sup>110</sup> which drew 2,900 participants and generated approximately 23,300 room nights for Oahu Island's hotels. Information from the Hawaii Convention Center reported stable bookings for 2008. Year-end 2007 figures show that 39 bookings represented a total of 91,215 delegates and were responsible for approximately 540,000 room nights on Oahu Island. As of November 2008, 41 bookings have been reserved, which represent 80,968 delegates and 433,253 room nights on Oahu Island. Based on year-to-date 2008 figures, it is anticipated that the convention market's performance will remain unchanged in 2008 compared with the prior year.



106 David Brudney, "Notes on Hawaii on the Back of an Airline Boarding Pass," *Hotel Online: Ideas & Trends*, September 2008.

107 "Monthly Visitor Statistics," Hawaii State Department of Business, Economic Development & Tourism, <http://hawaii.gov/dbedt/info/visitor-stats/tourism/> accessed on 29 October 2008.

108 "As fewer Japanese visit, Hawaii officials look to China and South Korea for tourists," Associated Press, 5 March 2008.

109 Marsha Weinart, Hawaii, State Tourism Liaison.

110 "Church cancels Hawaii meeting, citing airfares," Associated Press, 10 September 2008.



### **New development: Disney's Hawaii project breaks ground**

Walt Disney Parks and Resorts' first development in Hawaii, scheduled to open in 2011, began construction in November 2008. Disney's planned family destination resort is located at the Ko Olina Resort & Marina development on the western side of Oahu and is planned to include 350 hotel rooms and 480 Disney Vacation Club timeshare villas.<sup>111</sup> The US\$800 million project's plans include a pool and water play area, an 18,000-square-foot spa, a wedding lawn, an 8,000-square-foot convention center, a children's club and two restaurants. The development is expected to create 1,000 jobs in Hawaii.<sup>112</sup>

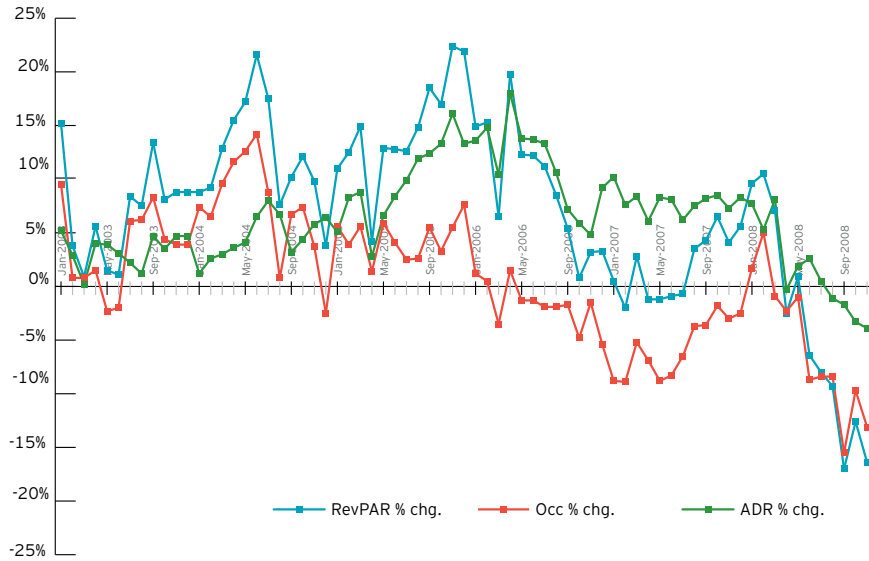
### **Hawaii Superferry resumes inter-island service**

In April 2008, the Alakai, Hawaii Superferry's first ferry, resumed service. The 350-foot long ferry, which travels between Oahu and Maui, can accommodate up to 800 passengers and approximately 200 subcompact cars. Its average load per trip is anticipated to be about 400 passengers and 100 vehicles of mixed sizes (motorcycles, cars, trucks and buses).<sup>113</sup> Although Hawaii Superferry has delayed the introduction of a second ship to a more suitable economic climate,<sup>114</sup> the firm reached a significant 125,000-passenger milestone in August,<sup>115</sup> indicating strong demand for this ferry service as an alternative to air travel for inter-island travel.

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- 111 "News: Disney's Hawaii project begins with ground blessing," [http://www.thrillnetwork.com/stories\\_view.php/2355/disneys\\_hawaii\\_project\\_begins\\_ground\\_blessing.html](http://www.thrillnetwork.com/stories_view.php/2355/disneys_hawaii_project_begins_ground_blessing.html) accessed on 24 November 2008.
- 112 "Disney breaks ground at Hawaii resort," *Pacific Business News*, 20 November 2008.
- 113 "Fact Sheet," Hawaii Superferry, <http://www.hawaiisuperferry.com/about-us/media-resources/default.html> accessed on 25 November 2008.
- 114 "Hawaii Superferry Postpones Introduction of Second Ship," Hawaii Superferry, 28 October 2008, <http://www.hawaiisuperferry.com/about-us/newsroom/press/2008/postpone-second-ship.html> accessed on 25 November 2008.
- 115 "Hawaii Superferry Reaches 125,000th Passenger Milestone," Hawaii Superferry, 19 August 2008, <http://www.hawaiisuperferry.com/about-us/newsroom/press/2008/125k-passenger.html> accessed on 25 November 2008.

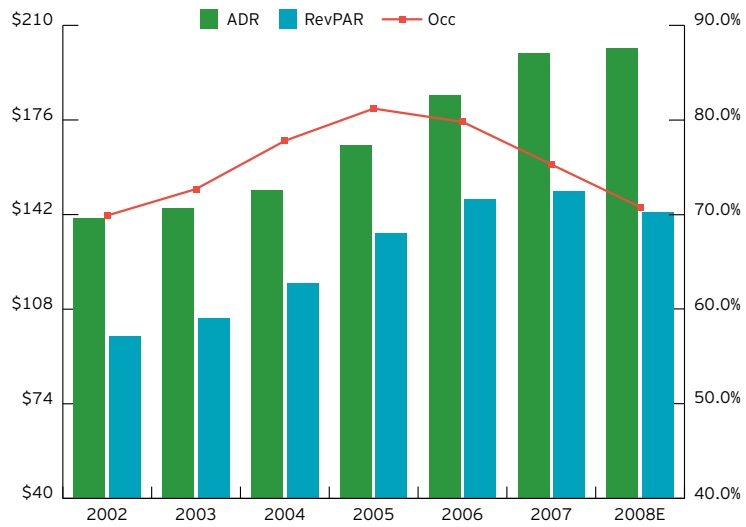
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Source: Smith Travel Research  
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**Hawaii lodging market occupancy, ADR, RevPAR performance (USD)**  
**2002-2008E**

Source: Smith Travel Research  
 Monthly Lodging Review



## Key takeaways

In 2008, the Hawaii lodging market showed signs of decline, reflected in the decrease of visitor arrivals and their expenditures in 2008. Due to the shutdown of Aloha Airlines and ATA Airlines, coupled with the departure of two domestic cruise ships from Hawaii, the outlook for 2009 shows a slight decrease in visitor arrivals, which is anticipated to result in weakening occupancy, ADR and RevPAR growth.<sup>116</sup>

116 "Slower But Continued Economic Growth Predicted in Current State Forecast," Department of Business, Economic Development and Tourism, 22 August 2008.



## Supply additions

Based on year-to-date September 2008 data from Smith Travel Research, the existing hotel supply is approximately 56,050 rooms. The following chart summarizes selected major supply changes.

Property	Location	Units	Scheduled opening date	Developer/owner
Trump International Hotel & Tower Waikiki Beach Walk	Honolulu, Hawaii	460	November 2009	Irongate Capital Partners
Baccarat Resort Wailea	Wailea, Hawaii	193	TBD 2010	Kobayashi Development Group/ Starwood Capital Group
Disney Resort @ Ko Olina	Kapolei-Oahu, Hawaii	400	June 2011	Walt Disney Parks & Resorts / Disney Vacation Club
Sea Mountain @ Punaluu	Punaluu, Hawaii	300	June 2015	Ocean Futures Society
Kona Kai Ola (mixed-use development)	Hilo, Hawaii	400	Not Available	Jacoby Development Inc.
Palamanui (mixed-use development)	Kailua Kona - Hawaii, Hawaii	120	Not Available	Keauhou Kona Construction LP
Keaau Village Inn	Keaau-Hawaii, Hawaii	60	Not Available	Bob Saunders
Oahu (mixed-use development)	Honolulu, Hawaii	TBD	Not Available	Jacoby Development Inc.
Grand Ko Olina Resort Hotel & Spa	Kapolei-Oahu, Hawaii	TBD	Not Available	Marriot Vacation Club International
Honua Kai Resort	Lahaina-Maui, Hawaii	TBD	Not Available	Intrawest Corp.
Laie Inn Hotel	Laie, Hawaii	226	Not Available	Hawaii Reserves Inc.
Waikoloa Village (mixed-use development)	Waikoloa, Hawaii	200	Not Available	Passco Companies LLC

Source: Smith Travel Research

# Las Vegas

## Introduction

Las Vegas experienced a significant slowdown in 2008, as lodging fundamentals, visitation and convention attendance have all declined. The credit crunch and economic conditions have slowed the transaction market and caused the cancellation or delays of some prominent projects, including Boyd Gaming's Echelon project, Elad Group's Las Vegas Plaza and a portion of MGM Mirage/Dubai World's CityCenter development in addition to others. Further, as Las Vegas lodging demand decreased in 2008, supply continued to increase with the opening of the 3,066-room Palazzo, 599-room Palms Place, 1,282-room Trump Las Vegas and the 2,034-room Encore by Wynn. Based on year-to-date November data from Las Vegas Convention and Visitors Authority ("LVCVA"), occupancy is anticipated to decrease 3.5 percentage points to 86.9% in 2008, with ADR decreasing 9.9% to US\$119, resulting in a 13.1% RevPAR decrease to US\$104 compared to 2007.



## Hot topics

### Credit crunch causes cancellation of numerous projects

The economic slowdown and difficult credit market conditions impacted the Las Vegas lodging market in 2008. No major real estate transactions occurred along the Las Vegas Strip in 2008, and multiple projects have been canceled or delayed, including Echelon, Las Vegas Plaza, Cosmopolitan Las Vegas and Crown Las Vegas. Further, in January 2009, MGM Mirage/Dubai World announced that they would delay and revise a portion of the US\$9.1 billion CityCenter development. Opening of the Harmon Hotel at CityCenter will be delayed by one year to the end of 2010 and will not include the original 200 condominium units. Instead, the Harmon Hotel will feature 400 rooms and be half as tall as its originally planned 47 stories.<sup>117</sup> Additionally, in January 2009, Harrah's Entertainment announced the delay of the new Octavius Tower at Caesars Palace. The

expansion, which is close to completion and includes over 600 rooms, was scheduled to open in the summer of 2009; however, the company does not anticipate opening the new tower until tourism demand rebounds in Las Vegas.<sup>118</sup>

### Las Vegas visitation: local vs. international

Despite increased international visitation as a result of the weak US dollar, overall year-to-date October 2008 Las Vegas visitor volume decreased 3.2%.<sup>119</sup> Drive-in visitation to Las Vegas decreased in 2008, as record gas prices caused average daily auto traffic on Interstate 15 (the main thoroughfare connecting Southern California to Las Vegas) at the California/Nevada border to decrease 5.8% through year-to-date October 2008.<sup>120</sup> Decreases in drive-in visitation can have a significant negative impact, as Southern California comprises approximately 25.0% of Las Vegas' visitors.

Las Vegas is expected to benefit from Nevada's tourism marketing campaign in China. Nevada is the first US state to promote tourism in China by organizing a marketing campaign. According to the Nevada Tourism Bureau, approximately 90.0% of mainland Chinese tourists who travel to the United States have visited Las Vegas. However, Asian visitation to Las Vegas has been negatively impacted in recent years by the rapid development and increased popularity of Macau. In addition to its efforts to promote visitation from China, the LVCVA launched a new international brand-marketing strategy program in July. The LVCVA's goal is to increase the number of international visitors to comprise 15.0% of Las Vegas' projected 43 million annual visitors by 2010 (international visitors comprised approximately 12.0% of Las Vegas' 39 million visitors in 2007).<sup>121</sup>

117 Howard Stutz, "Condominium Component Canceled at the MGM Mirage Harmon Hotel in the CityCenter Development," Las Vegas Review, 8 January 2009.

118 "Caesars Delays Expansion as Tourism Tumbles," MSNBC, 13 January 2009.

119 "2008 Las Vegas Year-to-Date Executive Summary," Las Vegas Convention and Visitors Authority, [www.lvcva.com](http://www.lvcva.com) accessed on 20 December 2008.

120 Ibid.

121 "Las Vegas Introduces New International Brand Strategy," Reuters, [www.reuters.com/article/pressRelease/idUS133390+13-Jun-2008+PRN20080613](http://www.reuters.com/article/pressRelease/idUS133390+13-Jun-2008+PRN20080613) accessed 1 October 2008.



### Lodging performance: continued declines

Hotel operators discounted rooms and increased marketing efforts in 2008 in an attempt to maintain occupancy levels and offset the effects of the economic slowdown, increased gas prices and increased airfares. According to the LVCVA, the average daily room rate for Las Vegas hotels decreased 8.1% in November 2008 and 9.5% year-to-date November 2008 to approximately US\$121. Occupancy levels decreased 7.7% in November 2008 and 3.9% through November 2008 to 87.1%. In addition, a significant increase in group cancellations in 2008 and 2009 has placed downward pressure on room rates, as operators have attempted to fill those mid-week rooms with the free independent traveler, casino and wholesale segments at lower rates.

### Airlift trends: airline reductions

Las Vegas airport passenger levels and airlift are anticipated to decrease in the short term. Passenger levels at McCarran International Airport decreased 6.4% year-to-date October 2008. Las Vegas airlift was expected to continue to decrease through December 2008, as major US airlines such as US Airways, Continental, Delta and Northwest reduce flights to Las Vegas due to increased fuel costs. As a result, direct flights to Las Vegas are expected to decrease between 5.0% and 8.0% in 2008.<sup>122</sup> US Airways, the second-largest carrier to Las Vegas (behind Southwest), decreased its air capacity to Las Vegas by approximately 25.0% (120,000 seats) in October 2008 compared with October 2007, and Continental, Delta and Northwest are anticipated to have similar capacity reductions. According to the LVCVA, approximately half of Las Vegas visitors

arrive by air, while air arrivals account for about 80.0% of hotel stays. Experts anticipate that Las Vegas will need to bring in an additional 2.8 million visitors to fill the added rooms opening through 2009. With the reductions in airline capacity, it is likely the increased fares will lead to lower guest spending and hotel rates, as operators must keep prices low to subsidize the cost of a visitor's trip.<sup>123</sup>

Although McCarran International Airport has experienced airlift reductions in 2008, the Clark County Department of Aviation has plans to spend approximately US\$3.5 billion through 2013 to enhance the capacity and condition of the present McCarran International Airport facilities. Nine new gates were completed in October 2008 and an additional US\$1.8 billion terminal (terminal 3) with 14 gates is projected

122 Joseph Greff, "Wynn Resorts: Lowering LV Estimates; Price Target to \$109; Maintain Overweight," JP Morgan Chase, 26 June 2008.

123 Deena Beasley, "Airline cuts squeeze Las Vegas resorts," *USA Today*, www.usatoday.com accessed on 19 September 2008.

to be completed in 2012. Following expansion, officials at McCarran International Airport estimate that the facility's maximum long-term sustainable capacity will be roughly 53 million passengers, an increase of approximately 5 million from 2007 levels.<sup>124</sup>

### **Convention market: decrease in conventions held and attendance**

Las Vegas convention facilities have the most convention space in the US at 22.6 million square feet (followed by Orlando at 7.6 million square feet) and it is the only market in the US to feature three major convention venues of more than 1 million square feet each – including the Las Vegas Convention Center, Mandalay Bay Convention Center and Sands Expo and Convention Center. While tradeshow performance was strong, the convention market slowed through year-to-date September 2008, as convention attendance and the number of conventions held decreased 3.9% and 4.2%, respectively. August and September were particularly weak months for convention attendance: respectively, attendance decreased 22.3% and 10.0% year-over-year.<sup>125</sup>

The US\$890 million renovation schedule for the Las Vegas Convention Center is being reconsidered due to a slowdown in the convention and tourism industry. Officials announced that the project will be broken into three phases, beginning with renovations on existing buildings. This move is expected to save money on financing and delay the completion date of the overall project beyond the original estimate of 2011.<sup>126</sup> Further, Las Vegas



124 Mishak and Richard N. Velotta, "Vegas tourism drop dims need for airport expansion, airlines say," <http://www.scrippsnews.com/node/34823> accessed on 19 September 2008.

125 "2008 Las Vegas Year-to-Date Executive Summary," Las Vegas Convention and Visitors Authority, [www.lvcva.com](http://www.lvcva.com) accessed on 29 December 2008.

126 Benjamin Spillman, "Las Vegas convention and visitors authority rethinks the \$890 million renovation of the Las Vegas Convention Center," Hotel Online, [http://www.hotel-online.com/News/PR2008\\_3rd/Aug08\\_Vegas CC.html](http://www.hotel-online.com/News/PR2008_3rd/Aug08_Vegas%20CC.html) accessed on 19 September 2008.



Sands announced plans in April to spend approximately US\$680 million to replace the Sands Expo and Convention Center by 2010; however, the project has been delayed as a result of the credit crunch and capital requirements.<sup>127</sup> In addition, Wynn Resorts announced plans for a 1.8-million-square-foot convention center and 5,200 rooms to be built on the golf course located behind the Wynn Las Vegas; however, a timeline for the Wynn golf course redevelopment is yet to be determined.<sup>128</sup>

#### **Supply additions: if you build it, will they come?**

Las Vegas lodging supply is expected to increase by 26,433 rooms (from 132,947 rooms to 159,380 rooms) between 2008 and 2010, representing a compound annual growth rate of 6.2%.<sup>129</sup> This growth is 1.6 percentage points greater than the 37-year (1970 through 2007) average of 4.6%. Historically, Las Vegas has proven to be an atypical market in which new supply stimulates new demand, as demand increased 4.9% annually during the 37-year period. However, given the current state of the US and global economies, the new properties slated to open in 2009 may have difficulty generating the incremental Las Vegas visitation achieved in prior years. Further, approximately 90.0% of new supply planned for the Las Vegas Strip is anticipated to target the luxury market, resulting in significantly increased competition in this segment.

127 Benjamin Spillman, "Owners of The Venetian and Palazzo Resorts Spending \$680 million to Replace the Sands Convention and Expo Center," Hotel Online, [http://www.hotel-online.com/News/PR2008\\_2nd/May08\\_WynnCC.html](http://www.hotel-online.com/News/PR2008_2nd/May08_WynnCC.html) accessed on 19 September 2008.

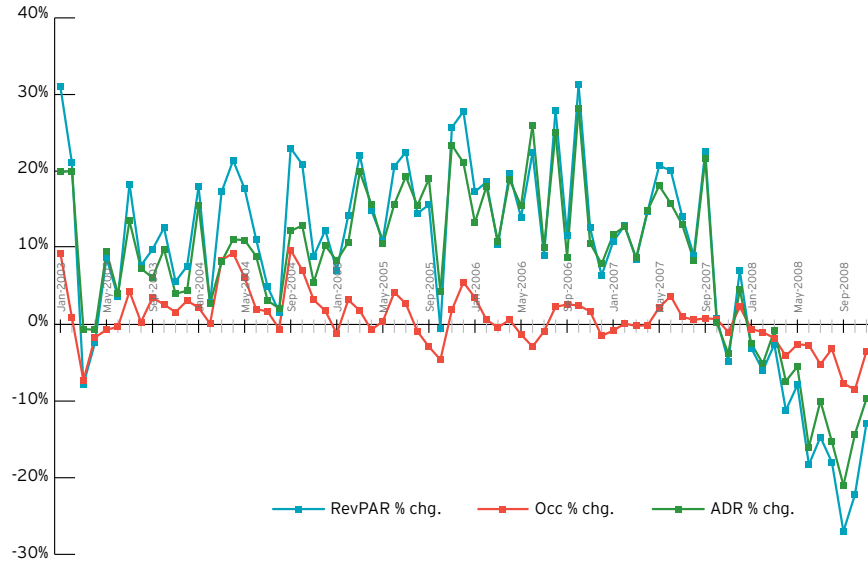
128 Benjamin Spillman, "Steve Wynn Contemplating Another Use for the Plush Golf Course Located Behind Wynn Las Vegas," Hotel Online, [http://www.hotel-online.com/News/PR2008\\_2nd/Apr08\\_SandsCenter.html](http://www.hotel-online.com/News/PR2008_2nd/Apr08_SandsCenter.html) accessed on 17 November 2008.

129 "Hotel/Casino Development - Construction Bulletin," Las Vegas Convention and Visitors Authority, [www.lvcva.com](http://www.lvcva.com) accessed on 17 November 2008.

**Las Vegas lodging market change in monthly occupancy, ADR, RevPAR performance**

January 2003–November 2008

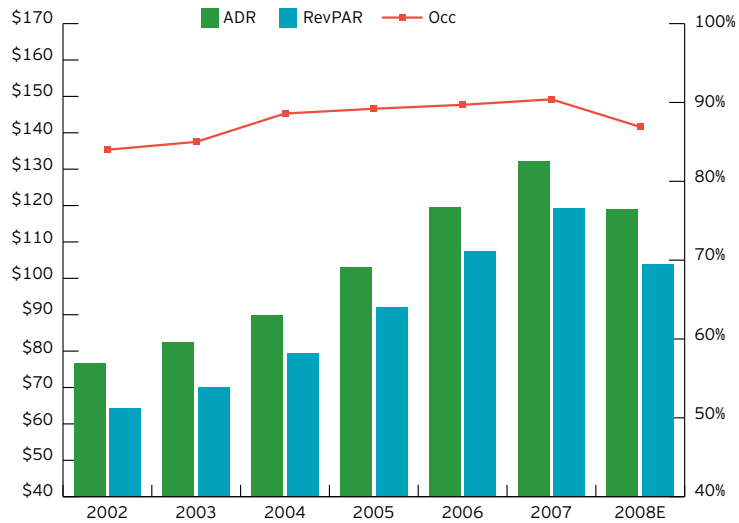
Source: Smith Travel Research  
Monthly Lodging Review, Las Vegas  
Convention and Visitors Authority



**Las Vegas lodging market occupancy, ADR, RevPAR performance (USD)**

2002–2008E

Source: Smith Travel Research  
Monthly Lodging Review, Las Vegas  
Convention and Visitors Authority



## Key takeaways

Las Vegas experienced significant decreases in lodging demand and airlift in 2008 along with significant increases in lodging supply, resulting in a rapid deterioration of lodging fundamentals. Further, numerous prominent Las Vegas developments have been delayed/ canceled as a result of the economic slowdown and credit crunch. Given decreasing lodging fundamentals and economic conditions, major Las Vegas gaming operators are now focusing on preserving cash flows, decreasing debt and complying with debt covenants.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
M Resort, Spa and Casino	Las Vegas, Nev.	390	March 2009	M Holdings LLC
Hard Rock (expansion and redevelopment)	Las Vegas, Nev.	875	September 2009	Hard Rock Hotel
ARIA Resort & Casino/ Project City Center	Las Vegas, Nev.	4,004	November 2009	MGM Mirage/Dubai World
Mandarin Oriental Hotel (CityCenter)	Las Vegas, Nev.	400	November 2009	MGM Mirage/Dubai World
Vdara Condo Hotel (CityCenter)	Las Vegas, Nev.	1,543	November 2009	MGM Mirage/Dubai World
Fontainebleau Las Vegas	Las Vegas, Nev.	3,889	Late 2009	Turnberry Construction/ Development Co.
Cosmopolitan Resort & Casino	Las Vegas, Nev.	2,998	2010	Deutsche Bank
Caesars Palace (expansion)	Las Vegas, Nev.	665	TBD	Caesars Entertainment/ Harrah's
Harmon Hotel (CityCenter)	Las Vegas, Nev.	400	Late 2010	MGM Mirage/Dubai World

Source: Las Vegas Convention and Visitors Authority, Smith Travel Research

# Los Angeles

## Introduction

As the fifth largest hospitality market in the US, Los Angeles has been partially insulated from the current economic slowdown. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 3.2 percentage points to 73.3% in 2008, with ADR increasing 4.9% to US\$138, yielding a RevPAR of approximately US\$101, an increase of 0.5% from 2007. Strong fundamentals in the market have been supported by tourism and development initiatives focused on revitalizing interest with the local market and repositioning it to become a preferred destination for both convention and leisure activity.



## Hot topics

### National economic softening impacts the local economy

The US economic slowdown has adversely impacted several key aspects of the Los Angeles economy in 2008, including the office market, port activity and the entertainment sector. As a result of the downsizing and layoffs that occurred in the local financial services and banking sectors, office vacancy rates increased by 1.5 percentage points through September 2008 while asking rates decreased 4.2%.<sup>130</sup> Similarly, the Port of Los Angeles, which accounts for approximately 45.0% of the nation's seaborne trade, experienced a 10.0% decline in overall volume as of November 2008, resulting in US\$55.5 million in economic losses.<sup>131</sup> The credit crunch impacted Los Angeles' entertainment

industry in 2008, as banks and hedge funds significantly decreased the availability of movie financing, putting projects at major film production studios at risk. The decreased financing availability forced studios (e.g., Paramount Studios) to reduce their annual feature schedule to 20 films per year, a 23.0% decrease from 2007 levels. In addition, the Screen Actors Guild initiated a strike authorization vote following the unsuccessful negotiations to renew the contract that expired 30 June 2008, which could result in an economic impact similar to the approximately US\$3 billion loss experienced during the Writers Guild of America strike in early 2008.<sup>132</sup>

### Hollywood and Beverly Hills development: revitalization initiated

The lodging market in the Hollywood Entertainment District (HED) currently operates as one of Los Angeles' leading sectors, achieving an ADR growth rate that is 207.0% greater than that of Los Angeles County as a whole.<sup>133</sup> In an effort to maintain this trend and revitalize the area, both city officials and private developers have initiated modernization and development efforts. Upcoming projects scheduled to begin construction by fall 2009 include The Boulevard 6200, the Camden Development, Vine Luxury Apartments, W Hotel & Residences and the Jefferson at Hollywood. Upon completion, these properties will feature approximately

130 Michael Washington, *Greater Los Angeles Office Report*, CB Richard Ellis, 3rd Quarter 2008.

131 Kristopher Hanson, "Unsold cars pile up at the Port," *Tribune Regional News*, 20 November 2008; "Port of Los Angeles Adopts 2008-2009 Fiscal Year Budget," The Port of Los Angeles: Americas Port Press Release, 5 June 2008.

132 Michael Stroud, "Economic turmoil takes its toll on Hollywood," Reuters, 13 November 2008; "Corporate News: SAG to Seek Strike Authorization," Associated Press, 24 November 2008; Aislinn Simpson, "Hollywood stars to vote on strike action," *The Daily Telegraph*, 24 November 2008.

133 Hollywood Entertainment District, <http://www.hollywoodbid.org/vPage.aspx?ID=29> accessed on 22 September 2008.



305 new rooms, 2,100 residential units and approximately 500,000 square feet of "Class-A" office space. The economic impact of these developments is expected to account for more than 4% of Los Angeles County occupancy tax revenue.<sup>134</sup>

Due to the passing of Measure H by local Los Angeles residents on 2 December 2008, Beverly Hills is anticipated to experience similar revitalization efforts. The owner of the Beverly Hilton Hotel, Oasis West Realty, has proposed a US\$500 million long-term redevelopment plan which would include the construction of the west coast's first Waldorf-Astoria.<sup>135</sup>

#### **Downtown development: LA Live and Grand Avenue developments anticipated to reignite interest within Downtown LA**

The downtown Los Angeles market is experiencing a significant increase in new development activity, positioning the market as a convention and tourist destination. The Anschutz Entertainment Group is currently developing LA Live, a US\$2.5 billion mixed-use development expected to be completed by 2010 and to feature an 878-room JW Marriott and a 124-room Ritz-Carlton.<sup>136</sup> In addition to the hotel component, the project will include entertainment and sports venues, such as the recently completed 7,000-seat Nokia Theater.<sup>137</sup> The US\$3 billion Grand Avenue project, led by the Related Companies, is another significant development, slated to open

in the downtown Los Angeles market by 2011. The Grand Avenue project plans to feature 2,600 residential units, 450,000 square feet of retail space, a 295-room Mandarin Oriental hotel and 266 branded condominium units.<sup>138</sup> Although the Grand Avenue project has experienced a series of delays related to project financing, the Honua Group, a Korean investment firm, invested US\$100 million in October 2008.<sup>139</sup> But as a result of the economic slowdown and frequent project delays, the completion date has yet to be determined.<sup>140</sup>

#### **Local propositions: measures focus on infrastructure modernization**

In July 2008, Measure R was passed in Los Angeles County to create funding for new transportation projects.<sup>141</sup> Over a 30-year period, the measure is

134 Christine Safriet, "Economic Impact Update," Economics Research Associates, 12 February 2008.

135 Martha Groves, "A Waldorf in Beverly Hills is a step closer," *Los Angeles Times*, 1 May 2008.

136 "The Ritz-Carlton Hotel and JW Marriott Hotel," LA Live, <http://www.lalive.com/content.php?section=hotels&page=hotels> accessed on 16 November 2008.

137 Morris Newman, "Why Not All Investors Are California Dreamin'," *National Real Estate Investor*, 1 September 2008.

138 Anna Scott, "Grand Avenue Groundbreaking Delayed," *Los Angeles Downtown News*, 19 September 2008.

139 Cara DiMassa, "Korean firm invests in Grand Avenue project," *Los Angeles Times*, 15 October 2008.

140 Cara DiMassa, "Penalty set if L.A. Grand Ave project is delayed more," *Los Angeles Times*, 29 July 2008.

141 "What is measure R?" Metropolitan Transportation Authority, <http://www.metro.net/measure/default.asp> accessed on 19 November 2008.

projected to generate approximately US\$40 billion that will be allocated toward congestion relief projects. Proposed infrastructure development projects include the expansion of the local subway and light rail system, as well as freeway improvements.<sup>142</sup> In addition, in November 2008, Proposition 1A, a measure focused on modernizing the California tram system, was passed.<sup>143</sup> The proposition approved the issuance of US\$9.9 billion of general obligation bonds which will be used as a down payment for the development of a high speed train connecting northern and southern California by 2030.<sup>144</sup> These infrastructure measures are expected to help Los Angeles address its long-term public transportation needs, resulting in additional visitation from nearby drive-in markets.

**Travel and tourism: China presents new opportunities for LA in a softening market**

The Los Angeles County market achieved record visitation in the fiscal year ended 30 June 2008, with 25.9 million overnight travelers accounting for more than US\$14 billion in local spending.<sup>145</sup> Despite the recent economic slowdown, 1.2 million cruise ship patrons docked in the port of Los Angeles, providing an additional US\$58 million in sales from local goods.

Since 9/11, the US has experienced a decline of more than 46 million overseas travelers, amounting to approximately US\$140 billion in lost revenue.<sup>146</sup> The department of commerce has signed a memorandum of understanding with China to encourage increased travel to the US by making it easier for tour groups to attain travel visas. As the fastest growing tourism sector in the world, Chinese visitation is anticipated to reach approximately 600,000 visitors by 2011.<sup>147</sup> With the average Chinese visitor spending approximately US\$6,000 per visit, Chinese visitors are projected to spend approximately US\$3.6 billion annually when visiting the US by 2011.<sup>148</sup>

**Local transportation: new renovation plan is proposed for LAX amid weakening patronage**

Los Angeles is anticipated to experience a decrease in airlift in 2008 as a result of increased fuel costs and decreased demand. Several airlines, including Cathay Pacific, Air India, Aer Lingus and Malaysia Airlines, were estimated to have eliminated approximately 163,000 passenger seats annually to Los Angeles International Airport (LAX) by year end 2008.<sup>149</sup> Further, LAX experienced a 7.3% decline in international and domestic travelers in September 2008 (compared with September 2007) and is



142 Dan Abendschein, "Measure R would give boost to transit within Los Angeles County," *San Gabriel Valley Tribune*, 12 October 2008.

143 Debra Bowen, "California General Election - Proposition 1A - Safe, Reliable High-Speed Train Bond Act," <http://vote.sos.ca.gov> accessed on 19 November 2008.

144 Lisa Vorderbrueggen, "SPENDING SPREE," *Contra Costa Times*, 9 November 2008; Melanie Turner, "Pacheco Route picked for high-speed train," *Sacramento Business Journal*, 10 July 2008.

145 "Tourism - LA's 2nd Largest Industry," The Los Angeles Convention and Visitors Bureau, <http://www.discoverlosangeles.com/los-angeles-page.php?pageid=285&tid=2090> accessed on 23 September 2008.

146 Sam Farr, "Extensions of Remarks - Travel Promotion Act Of 2008," Congressional Record 154.

147 "TIA Welcomes First Chinese Tour Group to the United States Under New Government Agreement," TIA, <http://tia.usdm.net/pressmedia/pressrec.asp?Item=902> accessed on 22 September 2008.

148 Ben Baeder, "Travel pact to bring surge in Chinese tourists," *McClatchy-Tribune Regional News*, 21 September 2008.

149 Rick Orlov, "LAX looking for new revenue airport: Freezing job positions among ideas," *Los Angeles Daily News*, 7 August 2008.



projected to experience a 13.4% decrease in passenger count in 2008.<sup>150</sup> While passenger volume is anticipated to decline in the short term, Los Angeles County is planning to increase international passenger capacity in the long term. In November 2008, LAX officials unveiled the proposed plan for an expansion and modernization of the Tom Bradley International Terminal. Scheduled to be completed by 2013, the approximately US\$5.5 billion plan proposes the development of a cross-field taxiway, reconstruction of two concourses, new gates to accommodate large commercial aircrafts (such as the Airbus A-380) and a new central hall offering shopping, restaurants and lounges.

#### **National Football League (NFL) stadium proposed for Los Angeles**

Several sites have been proposed for the location of a new professional football stadium in Los Angeles, including Carson and the City of Industry.<sup>151</sup> Ed Roski and Majestic Realty proposed to develop a stadium in the City of Industry that, if built, would offer 75,000 seats, 8,000 club seats, 175 suites, 40,000 square feet of attraction space, 60,000 square feet of retail and restaurant space and a medical center.<sup>152</sup> While members of the Majestic Realty group anticipate completing the project within two

years of its start, the timeline is largely dependent on the developer's ability to attract an NFL team and secure financing.<sup>153</sup> If built by the anticipated 2011 date, the stadium will stand as a potential venue for the 2016 Super Bowl game, which the NFL estimates will generate approximately US\$400 million for the local economy.<sup>154</sup>

#### **Lodging transactions: LA books the largest lodging transaction in 2008**

The Los Angeles County lodging market has performed well relative to other major US markets. Los Angeles had the largest hotel transaction in the US in 2008 with the sale of the Hyatt Regency Century Plaza for US\$366.5 million, or US\$504,821 per room.<sup>155</sup> The second- and third-largest lodging sales in the LA market were the sale of the Langham Huntington Hotel & Spa (former Ritz-Carlton) for US\$165 million, or US\$434,211 per room, and the Sheraton Gateway for US\$95 million, or US\$118,454 per room.

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150 Dan Weikel, "Upgrades at LAX face new hurdles; Officials say tighter borrowing costs, drop in traffic threaten revenue but won't halt crucial improvements," *Los Angeles Times*, 5 November 2008.

151 Roger Vincent, "Landfill in Carson to be Cleaned for Development," *Los Angeles Times*, 4 August 2006.

152 "Cutting-edge-design," Los Angeles Stadium, <http://www.losangelesfootballstadium.com/stadium> accessed on 22 September 2008.

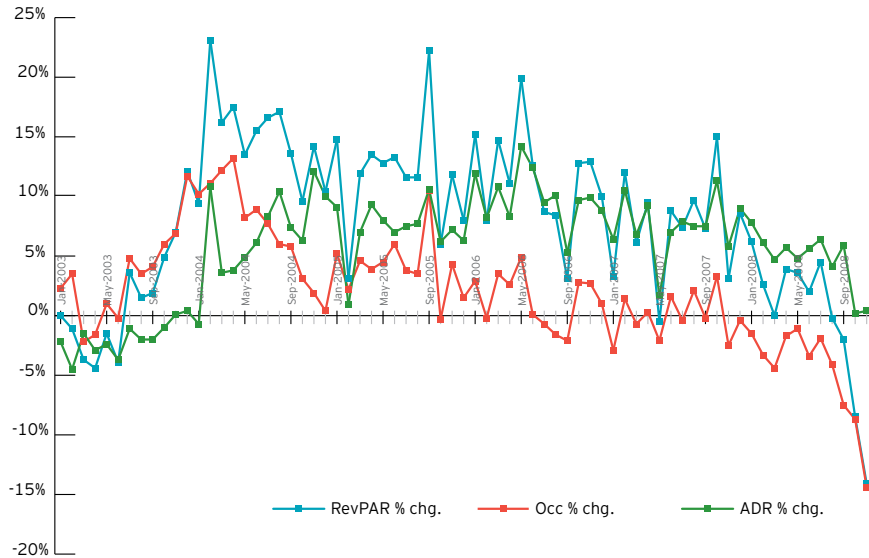
153 "Los Angeles to play in next season," LAlist, [www.lalist.com](http://www.lalist.com) accessed on 22 September 2008.

154 Sam Farmer, "BETWEEN THE LINES; Team or not, L.A. has a shot at 2016 Super Bowl," *Los Angeles Times*, 9 November 2008.

155 Lee Murphy, "Hotel REITs sell assets, strengthen portfolios," *National Real Estate Investor*, 1 September 2008.

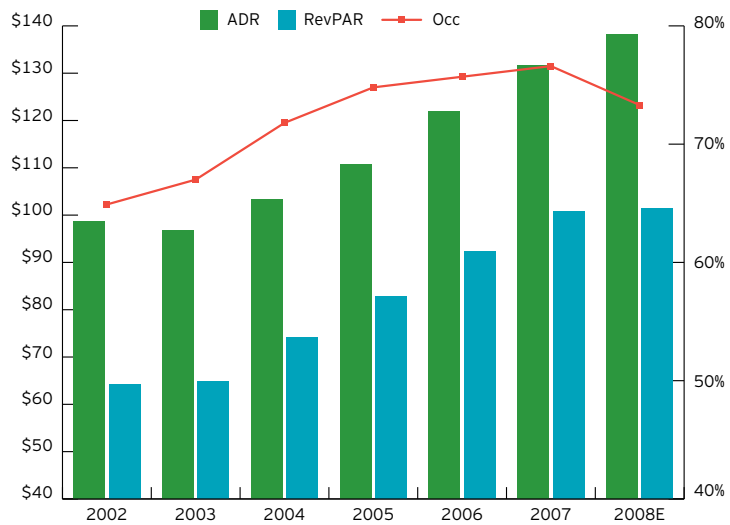
**Los Angeles lodging market  
change in monthly occupancy,  
ADR, RevPAR performance  
January 2003-November 2008**

Source: Smith Travel Research  
Monthly Lodging Review



**Los Angeles lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2002-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

As the US continues to experience the effects of an economic slowdown, the Los Angeles lodging market is anticipated to outperform other major markets in RevPAR. The LA market has strong hotel-development growth throughout Hollywood, Beverly Hills and Downtown along with infrastructure modernization and a possible NFL stadium. With an increase in demand generators and continuing room-rate growth, the LA market is poised to outperform the US in RevPAR growth.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
Miyako Hybrid Hotel	Long Beach, Calif.	209	April 2009	Kintetsu Enterprises
Hotel Esterel	Long Beach, Calif.	160	June 2009	The D'Orsay International Partners LLC
W Hollywood Hotel & Residences	Hollywood, Calif.	305	November 2009	Gatehouse Capital Corp.
Avalon @ South Bay	Long Beach, Calif.	300	June 2010	Hopkins Real Estate Group
JW Marriott & Ritz-Carlton	Los Angeles, Calif.	1,000	December 2010	Anschutz Entertainment Group
Waldorf=Astoria	Beverly Hills, Calif.	120	February 2011	Oasis West Realty, LLC
Metropolis	Los Angeles, Calif.	480	Not available	IDS Real Estate Group
Hyatt Place Glendale	Los Angeles, Calif.	172	Not available	Komar Investments
Columbia Square	Los Angeles, Calif.	125	Not available	Molasky Pacific
Mandarin Oriental LA	Los Angeles, Calif.	275	TBD	The Related Companies

Source: Smith Travel Research

# Manhattan

## Introduction

The Manhattan lodging market continued to be resilient through most of 2008 as other major markets throughout the US softened. Based on data from Smith Travel Research, Manhattan remains the top-performing market in the United States, achieving RevPAR of US\$258 through year-to-date November 2008. This represents an 80% premium over Hawaii, the nation's second-strongest market in terms of RevPAR. In spite of the recent economic slowdown, the Manhattan lodging market strengthened in 2008, albeit at a significantly more moderate pace than in previous years. Manhattan hotel operators, however, have indicated a further slowdown in demand for the remainder of the year, with an increased number of cancellations. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 1.4 percentage points to 84.1% in 2008, with ADR increasing a moderate 2.4% to US\$306. This results in RevPAR of approximately US\$257, an increase of 0.8% versus 2007.

## Hot topics

### Office market: weakening fundamentals' effect on business travel

Wall Street, which accounted for 36.0% of the total wages earned in 2007, is anticipated to face a challenging future, as it is estimated that more than 100,000 jobs in the financial sector will be lost in the next 12 to 24 months.<sup>156</sup> Due to economic conditions, office vacancy rates throughout Manhattan are rising, potentially indicating the beginning of a downturn in the office sector.<sup>157</sup> According to CB Richard Ellis, office vacancy in Manhattan, the largest office market in the US, increased to 5.8% in September 2008 from 4.7% in September 2007, while rental rates have begun to decline.<sup>158</sup> Furthermore,

upwards of 16 million square feet of office space in nearly 70 buildings was listed as available as of the beginning of December 2008, according to Colliers ABR, nearly twice the available space as a year ago.<sup>159</sup> While New York City's economy has diversified to reduce its dependence on Wall Street since the prior economic decline in 2002 – through the growth of industries including manufacturing, tourism, fashion, film, healthcare, media and bioscience – the decline in employment in the financial sector is expected to result in a decrease in the amount of business travel to Manhattan.



### Lodging fundamentals: slowdown anticipated in 2009

While economic indicators for Manhattan are softening and office fundamentals are weakening, the lodging market remained strong through the third quarter of 2008. According to data from Smith Travel Research, Manhattan's RevPAR was up 3.2% through year-to-date November 2008 versus the same period in 2007, and Manhattan's lodging market continues to outperform other major US lodging markets in terms of RevPAR. However, area hotel operators indicate that lodging demand is beginning to slow: hotels are beginning to experience decreased occupancy and increased cancellations. Meanwhile, corporations are instituting stricter

156 Paul Bubny, "Financial Markets Produce Differing Office Forecasts," *www.GlobeSt.com*, 9 October 2008.

157 Ibid.

158 Raymond Wong, "United States National Office Vacancy Index: Third Quarter 2008," CB Richard Ellis, October 2008.

159 Alex Tarquinio, "Manhattan Awash in Open Office Space," *The New York Times*, 3 December 2008.



travel guidelines and are seeking more significant discounts for 2009 negotiated room contracts, both of which could be major issues for the Manhattan lodging market. The threat of room rate negotiations is being accentuated by an anticipated decrease in corporate travel to Manhattan due to the recent Wall Street turmoil. These potential losses in future revenue are causing some hotel owners to postpone renovations, while the concern surrounding supply additions in 2009 is palpable. In an effort to prepare New York City for a downturn in the hotel market, some have called for increasing the city's hotel tax rate. Currently, taxes paid on a hotel room amount to 14.5%, making Manhattan one of the highest-taxed lodging markets

in the US. Proponents of the increase say that a one-point increase would generate approximately US\$70 million in additional revenue for the city on an annual basis, while opponents feel that the increase could lead to a loss of more than US\$530 million in sales and more than 3,700 jobs.<sup>160</sup>

#### **Hotel development pipeline remains robust**

While demand weakens, supply remains robust with approximately 144 new hotels, or 17,700 new rooms, in the development pipeline, according to Smith Travel Research. Of these, approximately 8,600 rooms (or 49.0%) are currently under construction, with another 633 rooms in the final stages of planning. With

approximately 65,800 existing rooms, the total pipeline represents a potential 26.9% increase to Manhattan's current lodging supply by 2012.<sup>161</sup> It should be noted that while historically fewer than 50.0% of hotels in the planning and preplanning stages actually come to fruition,<sup>162</sup> this share is anticipated to be even lower given the current lending and economic environments. According to CB Richard Ellis, most hotel projects in the development pipeline but not yet under construction are subject to delays or cancellations due to lack of available financing.<sup>163</sup> The current market has resulted in delays of several high-end hotel projects in the early stages of development, including the 206-room Shangri-La, with a now unknown

160 Charles V. Bagli, "Troubles for New York Hotels," *The New York Times*, 18 October 2008.

161 "Lodging Supply Report - Manhattan," Smith Travel Research, 25 September 2008.

162 Jack B. Corgel, Ph.D. and Robert C Baker, "The Hotel Supply Conundrum," *PKF Hospitality Research Whitepaper Series*, Volume 1, Issue 1, March 2007.

163 Terry Pristin, "Grand Plans for Manhattan Hotels Are Stalling," *The New York Times*, 28 October 2008.

completion date, and the 128-room Nobu Hotel and Residences in Lower Manhattan, delayed until fall 2010 at the earliest.

Manhattan has historically proven to be a market in which new supply induces demand. Even with anticipated delays and cancellations in the pipeline, Manhattan's hotel supply is projected to continue to increase at a relatively fast pace in comparison to the rest of the nation, particularly in the limited-service segment. Given the significant increase in supply and the current economic environment, supply additions will likely moderate ADR and occupancy growth during the next couple of years.

**Major development projects: continued progress should have long-term effects**

Even in the current economic climate, several large-scale development projects, located throughout Manhattan, are underway, particularly on Manhattan's west side. Of particular note is the expansion and renovation of the Javits Convention Center. While Javits is the 18th-largest convention facility in the US in terms of capacity, it ranks first in national convention attendance, and its renovation will result in an estimated 100,000 lost hotel-room nights per year. The US\$1 billion project will last several years but will address maintenance issues and add approximately 60,000 square feet of exhibition space.<sup>164</sup> Several new hotels are in the planning stages surrounding the center.

In addition, the New York City Metropolitan Transit Authority officially approved a bid from The Related

Companies and Goldman Sachs to develop the 26-acre Hudson Rail Yards, located between West 30th and West 33rd Streets and between 10th and 12th Avenues. The plan includes 5.3 million square feet of residential space (of which approximately 20.0% is to be designated as affordable housing), 3.6 million square feet of office space, 566,000 square feet of retail space, a luxury hotel and a school, as well as public space and green areas. While the first phases of the development are not anticipated to be completed until 2014 at the earliest, the Hudson Rail Yards should further create opportunities for Manhattan's lodging market in the long term.

In Lower Manhattan, the redevelopment of the World Trade Center site continues to face delays and budget overruns. In October 2008, The Port Authority of New York and New Jersey announced that most of the targeted completion dates for the development were deemed aggressive and delays were expected.<sup>165</sup> At this point the transportation hub is expected to be completed by mid-2014, the memorial by mid- to late-2011, the museum by mid-2013 and the Freedom Tower by late 2013. Once completed, each of these developments should further increase lodging demand throughout the city in the long term.

**Hotel compression demand plays an increasingly important role**

As average room rates increased by approximately 60.0% between 2002 and 2007, and as hotel occupancy frequently approaches sold-out levels in Manhattan, many travelers have increasingly utilized lodging options in



164 Charles V. Bagli, "Plan to Expand Javits Center Is Revived, Less Ambitiously," *The New York Times*, 3 September 2008.  
165 Chris Ward, "World Trade Center Report: A Roadmap Forward," The Port Authority of New York and New Jersey, 2 October 2008.



the outer boroughs and New Jersey. These markets have been benefiting from the compression demand from Manhattan, with many areas experiencing significant interest from both small developers and major brands. According to Lodging Econometrics, 55 hotels are presently in various stages of development throughout New York City's four outer boroughs and Hudson County (New Jersey). Starwood Hotels and Resorts, for instance, has plans to develop hotels in Brooklyn and Queens, while a 225-room W Hotel in Hoboken (New Jersey) is scheduled to open in February 2009.<sup>166</sup> Officials in Queens recently converted a refurbished subway car into a tourist bureau, and the Queens Economic Development Corporation started a tourism website.<sup>167</sup> Meanwhile, Forest City Ratner was scheduled to break ground in December 2008 on a US\$4 billion development at the Atlantic Yards in Brooklyn; however, the project is now scheduled to break ground sometime in 2009.<sup>168</sup> The planned development includes a US\$950-million arena, several thousand residential apartments and a significant amount of office space.<sup>169</sup> While these perimeter lodging markets benefit from expanding Manhattan lodging demand, they may also be the first to suffer from adverse effects of a softening hotel sector.

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166 Carlyn Kolker and Oliver Staley, "I'll take Manhattan... from Hoboken or Brooklyn or Queens," *Bloomberg News*, 26 July 2008.

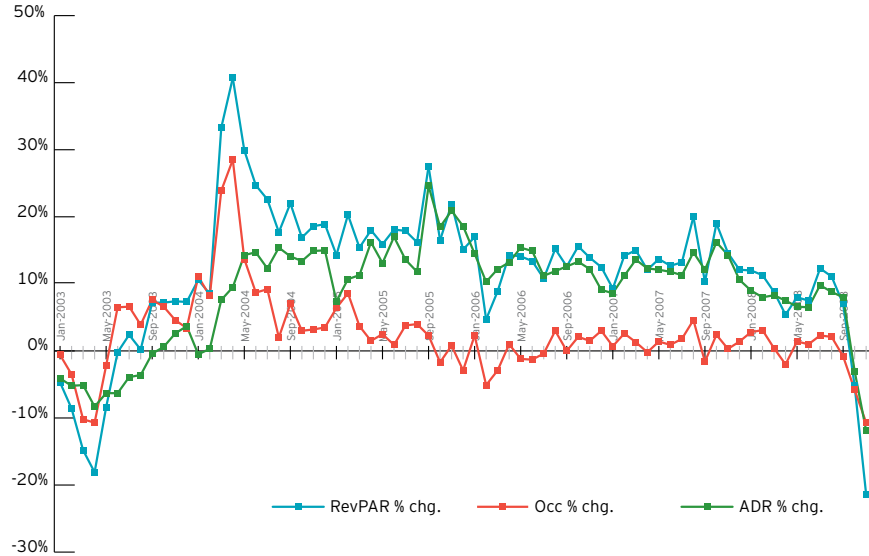
167 Ibid.

168 "Barclays Affirms Steadfast Commitment to Arena in Brooklyn and 2009 Groundbreaking," [www.atlanticyards.com](http://www.atlanticyards.com).

169 Charles V. Bagli, "Brooklyn Arena Builder Plans to Break Ground in December After Delay," *The New York Times*, 10 September 2008.

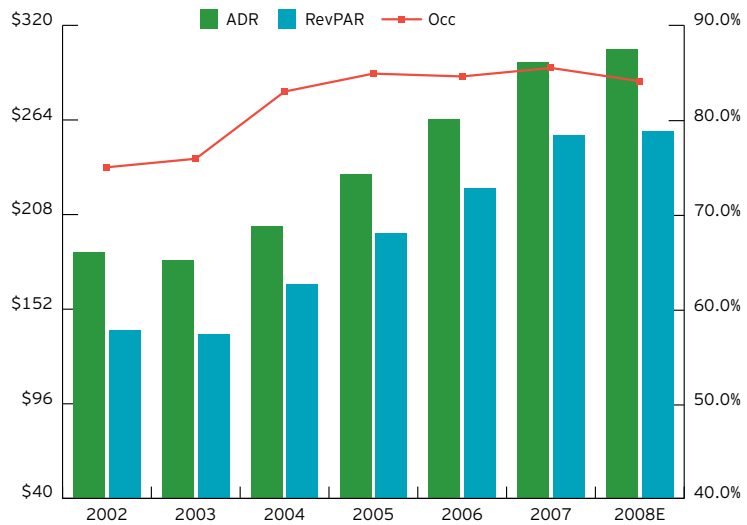
**Manhattan lodging market  
change in monthly occupancy,  
ADR, RevPAR performance  
January 2003-November 2008**

Source: Smith Travel Research  
Monthly Lodging Review



**Manhattan lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2002-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

While strong demand for hotels in Manhattan is likely to persist, the unfolding recession, weakening office market, citywide job losses and reductions in corporate travel and negotiated rates, as well as an increase in hotel supply, are anticipated to result in weakening occupancy for year-end 2008 and 2009. ADR will experience a significant slowdown as well, but it is expected to be less affected than occupancy. Continued plans for several large-scale developments

in Manhattan should further strengthen the Manhattan lodging market in the long term. In addition, there is a large pipeline of new hotels in various stages of development in New York's outer boroughs and in New Jersey. While these markets provide less expensive lodging options than their Manhattan counterparts, they may be the first to experience RevPAR decreases during periods of lessened lodging demand.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
The Pierre	New York, NY	201	January 2009	795 Fifth Avenue Corporation
Thompson Smyth Tribeca	New York, NY	120	February 2009	Thompson Hotels
Andaz Hotel 75 Wall Street	New York, NY	251	May 2009	Hakimian Organization
Trump SoHo Hotel Condominium New York	New York, NY	413	June 2009	The Trump Organization
Gansevoort Park Hotel	New York, NY	225	October 2009	Gansevoort Hotel LLC
W Hotel NYC Downtown	New York, NY	217	October 2009	The Moinian Group
Mondrian Soho	New York, NY	270	November 2009	Cape Advisors, Inc.
Sheraton Tribeca New York	New York, NY	361	November 2009	McSam Hotel LLC
Andaz Hotel 5th Avenue	New York, NY	144	December 2009	Global Hyatt Corporation
Cassa Hotel & Residences	New York, NY	166	February 2010	Extell Diamond Tower LLC
Nobu Hotel & Residences New York	New York, NY	128	October 2010	Swig Equities
Viceroy New York	New York, NY	168	December 2010	Tribeca Associates
InterContinental Times Square	New York, NY	611	July 2011	InterContinental Hotels & Resorts/Tishman Realty & Construction
Four Seasons Downtown	New York, NY	175	March 2011	Silverstein Development Corp.
21 Hotel	New York, NY	150	TBD (on hold)	Orient-Express Hotels, Ltd.
Shangri-La New York	New York, NY	206	Not available	RFR Realty LLC

Source: Smith Travel Research, HVS, Lodging Econometrics

# Miami

## Introduction

The lodging market in Miami rapidly changed in 2008, as current supply stabilized and a new wave of development opened at a time of economic uncertainty. Despite a relatively inactive hurricane season in Miami, occupancy and room rates fell in the latter half of 2008 compared with the same period in 2007, following years of significant growth. Based on year-to-date November 2008 data from Smith Travel Research, occupancy is estimated to decrease 0.4 percentage points to 71.6% in 2008, with ADR increasing 1.6% to US\$160. The resulting RevPAR of US\$115 is an increase of 1.0% to the prior year.



## Hot topics

### **New supply: ready for new doors to open**

After several continuous years of supply reductions, more than 4,500 rooms are scheduled to open in 2008 following new construction or renovations, including the 334-room Gansevoort South Hotel, the 335-room Miami Mondrian, the 1,035-room Fontainebleau Resort & Towers, and the 124-room Regent Bal Harbour, among others.<sup>170</sup> The market has been optimistic about Miami's ability to absorb the new supply, citing the strength of the last six years, as greater-Miami occupancy increased approximately ten percentage points to 72%, according to Smith Travel Research. The positive occupancy performance is partly attributed to a 15.0% decrease in supply from August 2003 to August 2008, due to hotel closings, condominium conversions and closings for renovations. Despite this significant reduction in supply, demand decreased by a marginal 0.8%.<sup>171</sup> Given the current

demand outlook, the supply additions are anticipated to place downward pressure on occupancy in 2009.

### **Brickell and Downtown: poised to induce or reduce?**

As both the Brickell and Downtown office markets showed overall negative absorption and heightened vacancy rates through the third quarter of 2008, the new upper-uptscale/luxury lodging supply in the Brickell corridor and Downtown may have difficulty achieving anticipated market penetration.<sup>172</sup> In a submarket that is primarily driven by corporate demand, the influx of supply – including the 411-room EPIC, a Kimpton Hotel, and the 129-room Viceroy Icon Brickell – may put downward pressure on the area's occupancy, as the Downtown area has limited ability to induce leisure demand. Although these hotels may attract more leisure business upon completion of the proposed "Seven-Mile Promenade" and the new Florida Marlins Stadium, the ramp-up period, especially

for room rates in 2009, may be challenged. Other planned Brickell and Downtown hotels include the JW Marriott Met-Marquis in 2010 and Flagstone's Island Garden development.

### **Visitation: can foreign visitors carry Miami in 2009?**

Market representatives credit Miami's international appeal (46.7% of total visitors are international, the highest rate of any US destination), with the city's ability to endure the national decline in domestic travel demand in 2008 without itself experiencing a significant decline in overall visitation. Through September 2008, Miami International Airport (MIA) experienced a year-over-year increase of 4.1% in total international passengers while experiencing a decrease in domestic travel of 1.5%. The number of overnight visitors to Miami-Dade County through June increased 3%, to approximately 6.4 million, and this was driven by an 8.2% increase in international visitors,

170 "New Hotel - Motel Product Miami-Dade County," Greater Miami Convention and Visitors Bureau, <http://www.miamianandbeaches.com/Index.asp> accessed on 15 September 2008.

171 "Lodging Supply Report - Miami-Hialeah, FL", Smith Travel Research, 25 September 2008.

172 "MarketView Miami Office," CB Richard Ellis, Third Quarter 2008.



which offset a 1.2% decrease in domestic visitation.<sup>173</sup> However, as the US dollar regains strength, the European recession deepens and Latin American economic growth slows, 2009 may bring fewer international visitors. It remains unclear whether an increase in foreign travel can continue to offset the decrease in domestic arrivals.<sup>174</sup>

#### **Condominiums and condominium-hotels: difficult times ahead**

During the recent real estate boom, Miami experienced strong RevPAR growth, declining office vacancies and rampant condominium sales. While more than 70.0% of the 17,000 condominiums constructed between 2003 and November 2008 were closed on by buyers, there are another 6,000 or so still in the pipeline, and some projects currently at or near completion are experiencing cancellation rates well over 50.0%.<sup>175</sup> The combination of the turbulent economic times, investors fleeing the deflating condo

market and the unique, untested asset class of condominium-hotels are presenting legal, financial and marketing challenges for Miami developers. While condominium-hotels became a popular financing technique earlier in the decade, the majority of projects remained under construction until 2008 and 2009. While recently opened condominium-hotels face a multitude of legal and operating challenges, new projects face buyers less than eager to close on their units. Several condominium-hotels in South Florida were deflagged as frustrated owners and management companies rethink their involvement. Clearly, if buyers don't close, closing the financing gap will be a significant challenge.

#### **Infrastructure: positively positioned for 2009**

After numerous construction delays, cost overruns and negative publicity about flight delays, significant progress has been made, resulting in a more positive image for MIA. The capital

improvement plan for the airport is rapidly progressing toward completion in 2011. Project components currently under construction include a new runway; 17 new cargo buildings comprising a total of 2.7 million square feet; portions of North Terminal, Concourse H and other components of the existing terminal; and new concessions, including restaurants, gift shops and other amenities. The most recent improvement includes the opening of a new US\$1.1-billion-dollar South Terminal, with 27 gates and an adjoining cruise ship bus depot.<sup>176</sup> As MIA reinvents itself as a comfortable, streamlined operation, airport officials hope that more major airlines will use the airport as a hub for international flights, increasing capacity to the area. Additionally, the Port of Miami is anticipated to experience higher levels of traffic due to the rerouting of various cruise ships from European to US ports, such as Miami, as cruise lines aim to reduce travel expenses for passengers.

173 Greater Miami Convention and Visitors Bureau, Planning and Research Department, <http://www.miamiandbeaches.com/Index.asp> accessed on 15 November 2008.

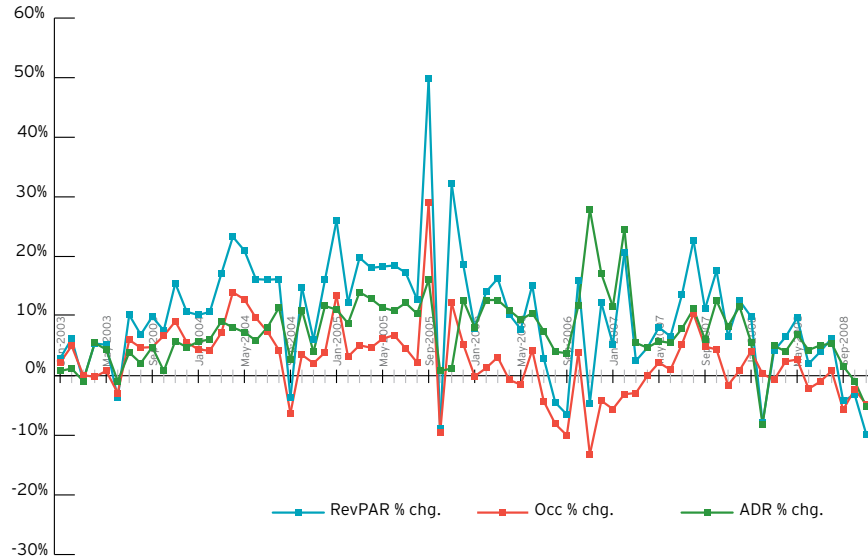
174 Doreen Hemlock, "Weak dollar, easy airline access make South Florida popular with foreign tourists," *South Florida Sun Sentinel*, 12 October 2008.

175 Matthew Haggman, "Test ahead for downtown condo market," *Miami Herald*, 21 November 2008.

176 "Facts at a Glance," Miami International Airport, [http://www.miami-airport.com/html/fact\\_at\\_a\\_glance.html](http://www.miami-airport.com/html/fact_at_a_glance.html) accessed on 20 October 2008.

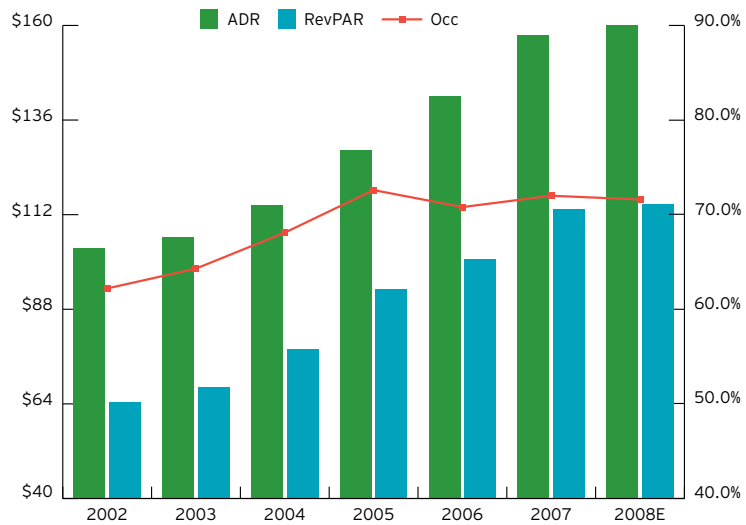
**Miami lodging market change  
in monthly occupancy, ADR,  
RevPAR performance**  
January 2003-November 2008

Source: Smith Travel Research  
Monthly Lodging Review



**Miami lodging market  
occupancy, ADR, RevPAR  
performance (USD)**  
2002-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Although thought to be somewhat protected from oscillations in the US economy given its balanced mix of demand, Miami is not immune to the recent global economic crisis. MIA should continue to be an important component in international travel as Miami expands its positioning as the business center for Latin America. Occupancy in 2009 may decrease with domestic demand softening and a proliferation of new supply, while average daily rates are anticipated to decrease marginally given the continued occupancy declines.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/Owner
EPIC, a Kimpton Hotel	Downtown Miami, Fla.	411	January 2009	Lionstone Hotels & Resorts
W South Beach Hotel & Residences	Miami Beach, Fla.	511	March 2009	Tri Star Capital/Related Companies
JW Marriott Miami Met-Marquis	Downtown Miami, Fla.	396	2010	MDM Development Group/MetLife
Viceroy Icon Brickell	Brickell, Fla.	129	2009	The Related Group of Florida
St. Regis Resort & Residences Bal Harbour	Bal Harbour, Fla.	219	December 2010	The Related Group of Florida
Upper Upscale Hotel Island Gardens	Watson Island, Fla.	345	2011	Flagstone Property Group
Shangri-La Hotel Island Gardens	Watson Island, Fla.	153	2011	Flagstone Property Group

Source: Greater Miami Convention and Visitors Bureau; Smith Travel Research

# New Orleans

## Introduction

The lodging industry in New Orleans experienced strong growth, attributed to the continued recovery post-Hurricane Katrina and the overall improving image of New Orleans. The effects of Katrina and current economic conditions continue to impact the New Orleans market, with the total area employment and population totals reaching only 86% of pre-Katrina numbers.<sup>177</sup> The casino industry in New Orleans, however, has not been severely affected by the national economic conditions, and gaming experts anticipate that the slight decrease in casino profits is only short term.<sup>178</sup> Based on year-to-date November data from Smith Travel Research, occupancy is projected to increase 5.1 percentage points to 62.5% in 2008, with ADR increasing 1.6% to US\$118. The resulting RevPAR of approximately US\$74 represents an increase of 10.6% over 2007.



## Hot topics

### Citywide convention market: strong activity expected in 2009

The New Orleans convention market in 2009 is expected to have one of its strongest years post-Katrina. Bookings at the Ernest N. Morial Convention Center have been increasing since 2005 by a compounded annual growth rate of 31.4%, as of October 2008, with 2008 being the highest year in convention bookings at the Center since before 2002. Bookings are projected to achieve pre-Katrina levels by 2009.<sup>179</sup> Major conventions held in late 2008 and early 2009 included the Prospect 1, the largest international contemporary art event ever hosted in the United States, and the Professional Convention Management Association conference, which many expect will sway several of the 3,000 meeting planners and decision-makers in attendance toward

bringing future events to New Orleans.<sup>180</sup> Additionally, the Roosevelt Hotel (formerly the Fairmont Hotel), which closed after Katrina, is scheduled to re-open as a Waldorf-Astoria in mid-2009, featuring 500 rooms and approximately 40,000 square feet of meeting space – reinforcing the positive image of New Orleans as a convention site.

### Tourism marketing: new initiatives to attract additional visitors

Following the effects of Hurricane Katrina, and more recently Hurricanes Gustav and Ike, significant efforts have been made to revitalize the New Orleans tourism industry. In October 2008, the New Orleans Convention and Visitors Bureau (CVB) organized a large initiative in London – the largest international feeder market pre-Katrina, with approximately 105,000 visitors in

2005, according to the CVB – by hosting a New Orleans Saints football game in London and a Jazz Festival similar to the annual Jazzfest in New Orleans. The success of this event prompted the CVB to plan comparable events in France, Germany, Japan and Asia-Pacific for 2009. In the US, the CVB has invested the US\$8 million grant received in 2007 and 2008 from the Community Development Block Grant to rebrand New Orleans and to increase sales efforts, and is returning to traditional forms of tourism marketing in 2009, through avenues such as trade shows and attending special events.

### Downtown office market: will occupancy remain strong?

The downtown New Orleans office market remained strong in 2008, attributed to limited inventory post-Katrina and

177 "Uno Metropolitan Report: Economic Forecast Through 2009," Targeted News Service, 29 May 2008.

178 Alan Sayre, "Casinos feeling economic pinch," *Charleston Gazette*, 21 May 2008.

179 "2009 Strategic Leisure Marketing Plan," New Orleans Tourism Marketing Corporation, <http://www.neworleansonline.com/> accessed on 24 October 2008.

180 *Hospitality Industry Report, 3rd Quarter 2008*, New Orleans Convention and Visitors Bureau, 17 July 2008.



increasing demand from new business and returning tenants. The vacancy rate as of July 2008 in the downtown office market was approximately 9.0% for Class A buildings, the same rate as 2007, and 14% for Class B buildings.<sup>181</sup> Vacancy rates are at the lowest since the late 1990s, with the exception of the second quarter of 2006. However, total Class A office space inventory has been reduced from 9.2 million square feet to 8.7 million square feet post-Katrina, while the downtown Class B inventory has been reduced from 2 million square feet to 1.3 million square feet post-Katrina. The closing of 1450 Poydras, a 492,000-square-foot Class A office building near the Superdome, accounted for the largest reduction in Class A office space and may either be redeveloped as part of the Superdome or reopened as Class A office space. The redevelopment

and closing, respectively, of the 121,000-square-foot 800 Common Building and the 429,000-square-foot 225 Baronne Building account for approximately 72.0% of the reduction in Class B office space. The oil industry, long noted as a driver of extended-stay demand, is anticipated to fluctuate with declining oil prices, and this may have a slight negative impact on lodging demand by reducing the number of visitors to the area. However, the lodging market is expected to be positively influenced by the strong office market.

#### **New Orleans airlift: bringing them back to the Big Easy**

Economic conditions and the rising fuel costs during the first half of the year prevented airlift from reaching pre-Katrina levels at the New Orleans Louis Armstrong International Airport (MSY)

in 2008. ExpressJet, for example, halted operations from MSY in September 2008 because of rising fuel costs, cancelling a total of 10 flights per day. However, given that arrivals to MSY increased 12.6% in 2008 to 5.6 million passengers, the CVB is currently working with airport officials to adequately align anticipated demand with projected airlift.<sup>182</sup> According to Boyd International, an airline consulting firm, MSY is the third-fastest-growing airport in the United States, with total passenger numbers expected to reach or exceed pre-Katrina levels by 2014.<sup>183</sup> Recent route additions to MSY include JetBlue's flight from Boston and Southwest's flight from Denver, which will increase the city's ability to meet the expected demand from these two strong medical and technology convention and annual festival source markets.

181 "Despite Slowdown, New Orleans Office Space Remains in Tight Supply Post-Katrina," NAI Global, 1 October 2008, [http://blogs.naiglobal.com/nai\\_global/2008/10/despite-slowdown.html](http://blogs.naiglobal.com/nai_global/2008/10/despite-slowdown.html) accessed on 15 October 2008.

182 "Summary of Enplaned Passengers by Airline - August 2008," New Orleans Louis Armstrong International Airport, <http://www.flymsy.com/> accessed on 15 October 2008.

183 "Armstrong International Airport Third Fastest Growing Airport in US," New Orleans Louis Armstrong International Airport, 14 October 2008, <http://www.flymsy.com/> accessed on 16 October 2008.



## Key takeaways

As recovery and reconstruction efforts from recent natural disasters continue in New Orleans, the lodging industry also continues to progress. Economic conditions have recently slowed the recovery for the New Orleans lodging market; however, limited-service hotels are continuing to strengthen the market, as they are expected to accommodate visitors taking part in reconstruction-related projects. In addition, lodging fundamentals in New Orleans in 2009 are anticipated to be positively affected by convention demand and a strong office market, aided by the CVB's marketing initiatives to highlight New Orleans as an attractive destination to major source markets domestically and abroad.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2010.

Property	Location	Units	Scheduled opening date	Developer/owner
La Quinta Inn & Suites Boutte	Boutte, La.	55	March 2009	Victor Guillory Construction
Residence Inn	Covington, La.	126	July 2009	HMS Architects
Hyatt Place	Covington, La.	127	November 2009	Jackies International
Trump International Hotel & Tower New Orleans	New Orleans, La.	250	June 2010	Poydras Property Holdings LLC

Source: Smith Travel Research

# Orlando

## Introduction

Orlando is projected for 2008 to experience its first RevPAR decline since 2003, as hotels observe decreases in occupancy and little growth in ADR. Based on year-to-date November data from Smith Travel Research, it is estimated that Orlando will experience a RevPAR of US\$70 in 2008, a decrease of 2.1% from the previous year. This decline is driven by a decrease in market occupancy, which is anticipated to decrease 2.2 percentage points to 65.8% while ADR is projected to increase a modest 0.1% to US\$106 compared to 2007.

## Hot topics

### **New supply: lodging brands “up the ante” with new properties and renovations**

With lodging demand and room rates increasing from 2003 to 2007, many developers in recent years were preparing to “get in on the action” in Orlando. Several properties are anticipated to open in 2009, including a Hilton Hotels trio (two Hilton properties and one Waldorf-Astoria property) that will add approximately 2,900 rooms to the market. After years of planning, the Peabody Orlando started construction of a 750-guestroom tower and renovations to the main hotel, which are both anticipated to open in 2010; the Hyatt Grand Cypress is also anticipated to complete renovations and possible expansion by 2010. While only in the planning phase, it appears likely that the Four Seasons Resort located on Walt Disney World’s grounds will be developed – although an opening is not scheduled for before 2011. Overall,

the anticipated increases in supply in 2009 and 2010 may further increase occupancy pressures in the market, thereby causing downward pressure on room rates.

### **Convention activity: softening attendance**

Attendance at the Orange County Convention Center (OCCC) decreased approximately 8.4% year-to-date July 2008 compared with the same period the previous year. With a declining economy, convention demand may remain soft throughout 2008 and into 2009. The International Builders’ Show, a mainstay at the OCCC for the past four years, announced a move to Las Vegas in 2009 with an estimated 105,000 vendors and participants.<sup>184</sup> To reduce the impact of softening OCCC attendance, larger hotels have focused on in-house groups to maintain performance levels. Looking forward, the combination of increasing room supply,



declining OCCC demand and increasing price sensitivity of groups may negatively impact the performance of the local lodging supply in 2009.

### **Visitation: will increases in international demand continue in 2009?**

As in 2007, the weakness of the US dollar relative to the Euro through the first half of 2008 made Orlando, and the United States as a whole, an attractive destination for foreign tourists. According to the Orlando/Orange County Convention and Visitors Bureau, international visitors accounted for 5.8% of visitation in 2007, and their numbers have been increasing at a compound annual growth rate of 5.4% since 2003. International passenger traffic at the Orlando International Airport increased by 21.2% for year-to-date September 2008 compared with the same period the previous year. As a result, air capacity was added on new-to-market airlines and

184 Beth Kasab, “Could be couple of lean years at convention center,” *Orlando Sentinel*, 18 January 2008.



existing carriers.<sup>185</sup> Given the marginal 1.8% compound annual rate growth in domestic visitation since 2003 and the weakened US economy, international visitation could represent the best growth opportunity for the market. However, this may not materialize, due to a strengthened US dollar and Europe entering an economic recession.

### **Condominium-hotels: carving out a niche**

Condominium-hotels, in a period of five years, had gone from general obscurity to a concept with tens of thousands of units recently planned in Orlando. Yet, since the credit crisis in 2007, both the demand for and supply of condominium-hotels decreased rapidly due to the complexities of the asset class and deflating residential market. Projects in late planning or construction face the prospect of buyers not closing on their units, potentially throwing project financing back to the drawing board in a market with little credit and lower

residential pricing. Although many lodging operators welcome much of the proposed new supply being placed on hold, those developments that have opened offer a value proposition and a competitive impact to dedicated hotel facilities. Condominium-hotels, with larger units and often two- and three-bedroom layouts, are offering room rates that leisure travelers, especially larger family groups, find more economically attractive than competing room rates at dedicated full-service hotels. As a result, condominium-hotels (and similarly positioned vacation rentals) may gain traction within the leisure-accommodation market and pressure traditional hotels – especially lower-priced full-service and limited-service hotels – for market share.

### **Orlando's theme parks: economic conditions pressure attendance**

Despite high fuel prices over the summer and the weakened economy, the debut of several rides, attractions and water

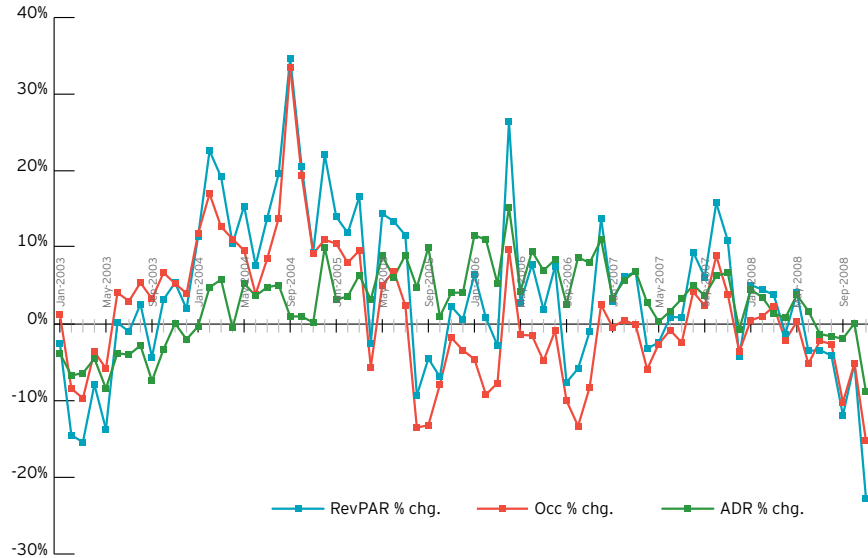
parks during 2008 is expected to have helped to maintain a healthy interest in Orlando. In efforts to capture more revenue per visitor, several theme parks marketed “all-inclusive” packages, which consist of tickets, meals and other items, during 2008. The outlook for 2009, however, is not as positive. Disney warned in November of a possible sharp drop in theme park attendance in early 2009, and it plans to utilize discounts to bolster attendance figures.<sup>186</sup> As the weakened economy causes families to scale back or eliminate travel for 2009, Orlando's theme parks will likely offer more packages and discounts to increase interest and maintain attendance levels. Ultimately, lower theme park attendance, or high attendance subsidized through incentives, may impact the lodging market's performance and ability to maximize rate yields during both low and high seasons.

185 Jason Garcia and Scott Powers, “Foreign flights pick up slack,” *Orlando Sentinel*, 4 August 2008.

186 Peter Sanders, “Disney Net Slumps as Slump Hits Home – With Consumers Spending Less, a Tough Year Looms With Discounts Planned for Theme Parks,” *The Wall Street Journal*, 7 November 2008.

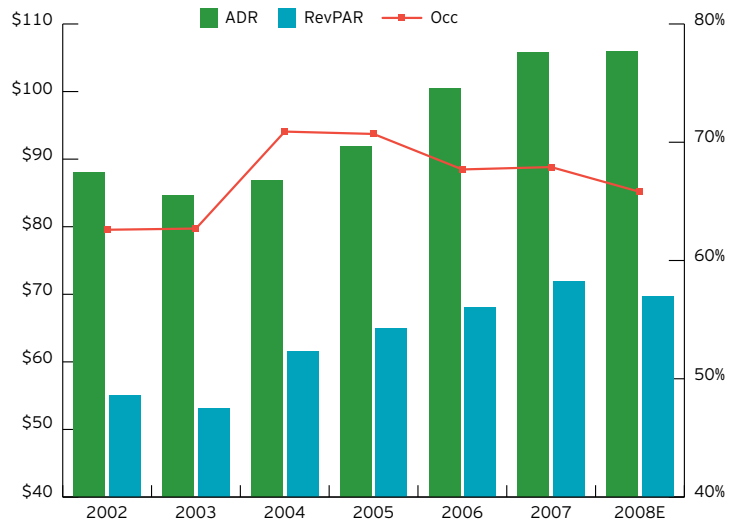
**Orlando lodging market change in monthly occupancy, ADR, RevPAR performance**  
**January 2003–November 2008**

Source: Smith Travel Research  
 Monthly Lodging Review



**Orlando lodging market occupancy, ADR, RevPAR performance (USD)**  
**2002–2008E**

Source: Smith Travel Research  
 Monthly Lodging Review



## Key takeaways

In 2009, lodging demand in Orlando is expected to soften due to a weak economy. Beyond the weakened economy, lodging demand will likely experience negative pressure from a decrease in convention-center activity, a decline in theme park attendance and increased competition from condominium hotels. The influx of approximately 2,900 rooms in the second half of the year, in addition to softening demand, may pressure lodging operators to reduce average daily rates in an effort to maintain occupancy levels and RevPAR.



## Supply additions

Based on year-to-date September 2008 data, the existing hotel supply is approximately 114,000 rooms. The following chart summarizes selected major supply changes.

Property	Location	Units	Scheduled opening date	Developer/owner
Hilton Convention Center	International/ Universal Drive, Orlando, Fla.	1,400	August 2009	Hilton Hotels, Apollo Real Estate Advisors, RIDA Development Corp.
Waldorf=Astoria Bonnet Creek	Lake Buena Vista, Orlando, Fla.	498	October 2009	Brooksville Development Corp., GEM Realty Capital
Hilton Bonnet Creek	Lake Buena Vista, Orlando, Fla.	1,000	October 2009	Brooksville Development Corp., GEM Realty Capital
Wyndham Bonnet Creek	Lake Buena Vista, Orlando, Fla.	400	1st quarter 2010	Buena Vista Corp.
Peabody Orlando (addition)	International/ Universal Drive, Orlando, Fla.	750	4th quarter 2010	Peabody Hotel Group
Four Seasons Walt Disney	Lake Buena Vista/ Walt Disney, Orlando, Fla.	400	2011+	Four Seasons Resorts

Source: Smith Travel Research

# Philadelphia

## Introduction

Although the overall US lodging performance has weakened in 2008, Philadelphia's RevPAR has remained relatively flat, with ADR growth offsetting declines in occupancy. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 2.1 percentage points to 71.3% in 2008, with ADR increasing 2.8% to US\$173; the resulting RevPAR of approximately US\$124 reflects modest growth of 0.2% compared to 2007.



## Hot topic

### Lodging performance: decreased hotel demand

Hotel occupancy rates in Philadelphia experienced gains over the last several years with a historic high in 2005. However, in 2008, rates decreased for the first time since 2003. Demand decreased 3.4% through year-to-date September 2008 versus the same period in the prior year as airport traffic remained stagnant at Philadelphia International Airport (PHL) through the first eight months of the year.<sup>187</sup> The decreases can be attributed not only to the softening economy but also to fewer and smaller groups at the Pennsylvania Convention Center and reductions in flight schedules to PHL.<sup>188</sup>

### Demand generators: promising convention market and entertainment industry

In the mid- to long term, area hotel demand should be positively impacted

by several city initiatives, including the expansion of the Pennsylvania Convention Center, the development of a new entertainment complex in South Philadelphia and the potential move of Foxwoods Casino into the city. The US\$700 million, 376,000-square-foot expansion of the Pennsylvania Convention Center in Center City is expected to surpass its budget by US\$90 million due to increasing construction costs.<sup>189</sup> According to the Philadelphia Convention & Visitors Bureau, the expansion, which is scheduled to open by 2011 and result in a total of 1 million square feet of saleable space, has stimulated growth, including plans for an additional 2,500 hotel rooms to open by 2013.<sup>190</sup>

In September 2008, the Philadelphia City Council and casino investors agreed to a proposed move of Foxwoods Casino from South Philadelphia to Center City.

The move could increase lodging demand and improve the city's economy, as similar gaming establishments have in other cities in Pennsylvania – including Pittsburgh, Erie and Bethlehem<sup>191</sup> – although no estimated completion date has been released.

In addition, Comcast-Spectator, a Philadelphia-based sports-entertainment and arena-management firm, has partnered with the Cordish Company, a Baltimore-based real estate-development firm, to develop Philly Live!, a multimillion dollar entertainment complex in South Philadelphia.<sup>192</sup> The project, which will be located adjacent to the Wachovia Center, plans to include retail, dining, music venues, a movie theater and a potentially 300-room hotel.<sup>193</sup> The development's construction costs and completion dates were not released as of January 2009.

187 Greg Robb, "Bullish on Philadelphia; New Mayor Wants to Reverse Population Outflow," *Marketwatch*, 4 July 2008.

188 Ibid.

189 "US\$700 Million Expansion of the Philadelphia Convention Center is on the Horizon with Demolition Underway. Construction Community Gears up for Next Wave of Downtown Work," *Mid-Atlantic Construction*, 1 October 2007 and [www.paconvention.com/exp/expstats.asp](http://www.paconvention.com/exp/expstats.asp) accessed on 21 October 2008.

190 "Convention Center Expansion Spurs New Developments and Renovations," Philadelphia Convention & Visitors Bureau, September 2008.

191 Katharine Q. Seelye, "Economic Picture is Mixed in Pennsylvania," *The New York Times*, 8 March 2008.

192 Ed Moran, "Flyers – Luukko to Unveil Early Plans for Complex," *The Philadelphia Daily News*, 22 January 2008.

193 "Destination Retail, Dining and Entertainment District in South Philadelphia," <http://philadelphia.about.com> accessed on 21 October 2008.



### **Philadelphia economy: a strong and diverse mix of industries**

Philadelphia continues to reinvent itself from its past as a manufacturing city, with city government efforts to expand the sciences, venture capital, financial services and entertainment production industries. The “Select Greater Philadelphia” initiative has attracted 29 companies to the region in the last two and a half years.<sup>194</sup> In addition, venture-capital investing in 2007 reached a six-year high in the Philadelphia area, at US\$661.8 million.<sup>195</sup> The city has had discussions with Toronto-based TD Bank Financial Group to move the headquarters of its US branch into the city.<sup>196</sup> The Comcast Center, a 1.3-million-square-foot office building which opened in June 2008 as Philadelphia’s tallest tower, is anticipated to become the tallest green office building in the nation once it achieves LEED certification. The US\$850

million project is owned by a joint venture of Commerz Leasing und Immobilien and Liberty Property Trust.<sup>197</sup> Furthermore, Pennsylvania committed US\$75 million in tax credits to film and television productions agreeing to spend at least 60% of their total production cost in Pennsylvania.<sup>198</sup> As of December 2007, US\$28.9 million of the US\$75 million available has been committed statewide.

According to Cushman & Wakefield, Philadelphia’s Central Business District weighted average gross rental rate for class A office buildings increased 1.51% to US\$28 per square foot in the third quarter of 2008, while overall vacancy was 10.0%, an increase of 0.5 percentage points from midyear 2008. According to Cushman & Wakefield’s fourth-quarter Philadelphia market beat report, 2009 office rental rates will decrease slightly due to the economic contraction and a moderate increase

in vacancies. The office market’s resilience and the city’s diversification of industries will likely result in more stable business-traveler demand, partially mitigating the economic downturn’s effects on lodging.

### **Lodging pipeline: continued investment in hotel development**

A number of renovations and new developments in the hotel sector are occurring in Philadelphia. Recent renovations include a US\$11.5 million restaurant and spa upgrade to the Four Seasons Hotel Philadelphia and a US\$26 million soft goods, lobby and ballroom renovation at the Ritz-Carlton Philadelphia, both completed in 2008. Planned hotel openings include a number of lifestyle hotels in the luxury and upper upscale segments, such as Le Méridien, the Kimpton Palomar and the W hotels.<sup>199</sup>

194 Crissa Shoemaker Debree, “Gamesa is a Worldwide Force,” *Bucks County Courier Times*, 17 January 2008.

195 “Big Year for Venture Capital,” *Philadelphia Inquirer*, 21 January 2008.

196 Jeff Blumenthal, “Region seeks to score TD,” *Philadelphia Business Journal*, 4 April 2007.

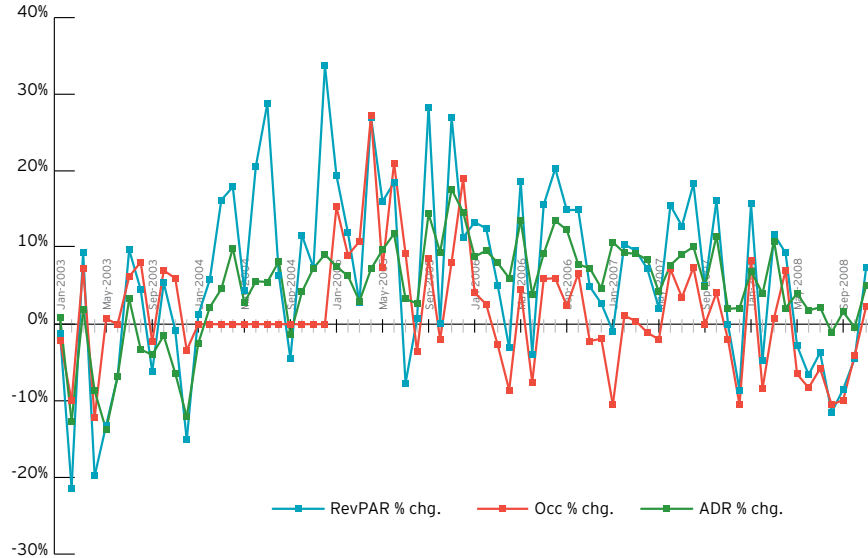
197 “Comcast Center Claims Its Place Atop the Philadelphia Skyline; Nation’s Tallest Sustainable Skyscraper Rises 975 Feet into the Clouds,” *Business Wire*, 6 June 2008.

198 “Philadelphia Region Will See US\$68 Million Investment from Filmmakers Due to Film Tax Credit Program, Governor Rendell Says,” Pennsylvania Office of the Governor, 21 December 2007.

199 “One of the First Grand Hotels Meets One of the Country’s Finest Cities,” *Business Wire*, 30 October 2008.

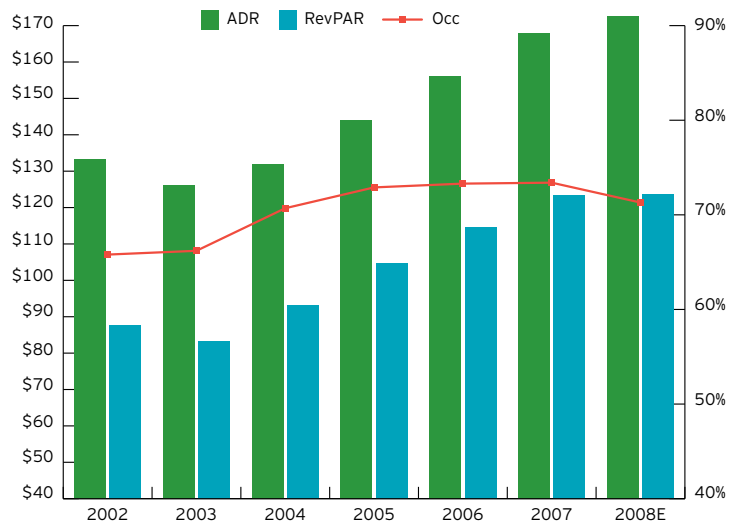
**Philadelphia lodging market  
change in monthly occupancy,  
ADR, RevPAR performance  
January 2003-November 2008**

Source: Smith Travel Research  
Monthly Lodging Review



**Philadelphia lodging market  
Occupancy, ADR, RevPAR  
performance (USD)  
2002-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Philadelphia's long-term lodging demand is supported by efforts to expand the sciences, venture capital, financial services, and film and television production industries. A plan by US Airways to begin daily nonstop service between Philadelphia and Beijing was postponed in mid-2008 due to fuel price hikes, but may be reconsidered in 2010. In the longer term, Philadelphia's hotel demand will potentially be sustained by the expansion of the Pennsylvania Convention Center, the development of a new entertainment complex in South Philadelphia and the potential move of Foxwoods Casino into the city. However, in the short term, occupancy and ADR are anticipated to lag historical levels.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
Le Méridien Philadelphia	Center City, Philadelphia, Pa.	202	June 2009	Development Services Group
Hotel Palomar Rittenhouse Square	Center City, Philadelphia, Pa.	235	November 2009	Kimpton Hotel and Restaurant Group, Inc.
W Hotel & Residences Philadelphia	Center City, Philadelphia, Pa.	250	December 2009	Starwood Hotels and Resorts Worldwide, Inc.
Luxury Collection Stamper Square	Center City, Philadelphia, Pa.	150	January 2011	MF Stein Corp.
Inter-Continental Philadelphia	Center City, Philadelphia, Pa.	268	June 2011	Grasso Holdings

Source: Smith Travel Research, Philadelphia Convention & Visitors Bureau, company websites and contacts

# Phoenix

## Introduction

In 2008, the Phoenix metropolitan area experienced a decrease in RevPAR despite hosting the NFL Super Bowl. Phoenix's lodging market experienced a decrease in occupancy and an increase in ADR in 2008, resulting in an overall decrease in RevPAR. New convention space, national sporting events and the light rail system's opening are anticipated to fuel economic growth in the area. Based on year-to-date November data from Smith Travel Research, it is estimated that overall occupancy will decrease by 7.2 percentage points to 59.7%, with ADR increasing 2.9% to US\$124 – resulting in a RevPAR decrease of 6.7% to US\$75.<sup>200</sup>

## Hot topics

### NBA All-Star Game: sporting events drive future demand

Phoenix will host the 2009 NBA All-Star Game at the US Airways Center in February 2009. Phoenix city officials estimate 125,000 to 150,000 attendees, generating an economic impact of US\$80 million, similar to the non-gaming revenues that the 2007 Las Vegas host generated for the city.<sup>201</sup> Other sporting events that attract significant out-of-state attendees in the Phoenix Metro Valley include the Fiesta Bowl, Insight Bowl, FBR Open golf tournament and spring training baseball games. In addition, University of Phoenix will host the NCAA men's basketball tournament west regional games in late March 2009. Phoenix is also bidding to host college basketball's Final Four games in 2012, hoping to utilize the full University of Phoenix's stadium with 80,000 seats. The Super Bowl week of festivities generated a record US\$501

million in direct and indirect spending by visiting fans and organizations.<sup>202</sup> In 2009, the Cactus League will grow from 12 to 14 teams, adding the Los Angeles Dodgers and the Cleveland Indians. By 2010, it could be 15, up dramatically from 6 in 1993 and equal to Florida's Grapefruit League.<sup>203</sup>

### Convention space: becoming a top convention market

New convention center space in Phoenix is expected to be a significant source of visitation growth for Phoenix in 2009. In continuation with Phase 1 of the Phoenix Convention Center's 2006 expansion (which also included the West Building with 400,000 square feet of additional meeting space), Phase 2 of the expansion was completed in January 2009. The US\$600 million expansion will feature a total of approximately 2 million square feet of convention space, a light rail station, underground exhibit hall and



50,000 square feet of newly renovated meeting-room space.<sup>204</sup> Furthermore, the convention center anticipates generating an economic impact of US\$350 million in 2009 and US\$500 million in 2013.<sup>205</sup> The convention center has scheduled major events for 2009. Phoenix has been chosen to host the National Rifle Association's annual convention in 2009, an event expected to attract up to 65,000 people.<sup>206</sup>

With approximately 3,500 rooms in the downtown Phoenix area, new supply additions help alleviate the shortage of downtown lodging. The Downtown Sheraton opened in September 2008, which marks a significant milestone for the downtown area. The Sheraton adds 1,000 hotel rooms and 80,000 square feet of meeting space, including a 30,000-square-foot ballroom and a 15,000-square-foot junior ballroom. The hotel currently offers the most rooms

200 *MarketView: Phoenix Report*, CB Richard Ellis, 3rd Quarter 2008.

201 Jahna Berry, "Big All-Star Impact No Slam Dunk," *The Arizona Republic*, 12 November 2008.

202 "Economic Impact Study: Phoenix Scores Big with Super Bowl XLII," Knowledge@W.P. Carey, 23 April 2008.

203 Debbie Arrington, "Cactus League experiences population boom," *The Sacramento Bee*, 22 March 2008.

204 Scott Blair and Tom McClure, "Features; Southwest Contractor 2006 Top Projects Arizona," *Southwest Contractor*, 1 June 2007.

205 "Fact Sheet," Phoenix Convention Center, <http://www.ci.phoenix.az.us/CIVPLAZA/PhoenixConventionCenterFactSheet.pdf> accessed on 10 November 2008.

206 "Phoenix Will Host NRA's 2009 Convention," KVOA Tucson Channel 4 News, 25 February 2006.



of any hotel in Arizona and is the first downtown hotel built since 1976.<sup>207</sup>

In addition, a resort and convention center is planned in East Mesa at the former General Motors proving ground site with at least 1,250 rooms and 200,000 square feet of convention space. The space will be created by Gaylord Hotels in partnership with DMB Associates.<sup>208</sup> Along with the resort, other features include retail stores operated by Westcor and a championship golf course. The project will cost an estimated US\$1 billion and is expected to break ground in summer 2009.

#### **Light rail: linking downtown**

Construction of the 20-mile initial light rail line that links midtown and downtown Phoenix with Sky Harbor Airport and downtown Tempe was completed in December 2008.<sup>209</sup> The initial light rail line's north end begins at Phoenix Spectrum Mall and continues along

Camelback Road to the east and south through midtown and downtown Phoenix. In the heart of downtown at Central Avenue and Washington Street, the route turns east to Sky Harbor Airport, to Arizona State University and then terminates in West Mesa. The 28 stations of the initial line link three communities and also link the Main Campus of Arizona State University with its downtown Phoenix campus.

#### **Major developments: long-term lodging driver**

"cbd101," a mixed-use development in Glendale, is set to begin construction in 2009. The development will include 2.6 million square feet of office space and will be situated on 77 acres of land. The project will comprise a 40-story mixed-use tower, three stand-alone hotels, 850 midrise residential units and an organic farm. The project is being developed by the Bidwill family, the owners of the

Arizona Cardinals. During the 10-year build-out, the project is estimated to generate 23,000 jobs and to have an annual economic impact of US\$2.6 billion.<sup>210</sup> The Glendale City Council has approved the development, and Phase I is scheduled to be completed in the fall of 2010.<sup>211</sup> Phase I will include a hotel, an office building, a parking structure, residential units and an organic farm.

One Scottsdale is a retail and residential community development in North Scottsdale. It will include 1.8 million square feet of retail, dining and class A office space, 400 resort and boutique hotel rooms and 1,100 mixed-use residential units. The community is being developed by DMB in partnership with Macerich. Macerich will develop and operate the retail portion of the community and operate under the Wescor name.

207 Jahna Berry, "Construction Tops Out at New Hotel," *The Arizona Republic*, 15 August 2007.

208 "Gaylord Entertainment Plans Resort and Convention Hotel in Mesa, AZ," *Hotel News Resource*, 4 September 2008.

209 "Light Rail Update," Valley Metro, Summer 2007, <http://www.valleymetro.org/> accessed on 5 February 2009.

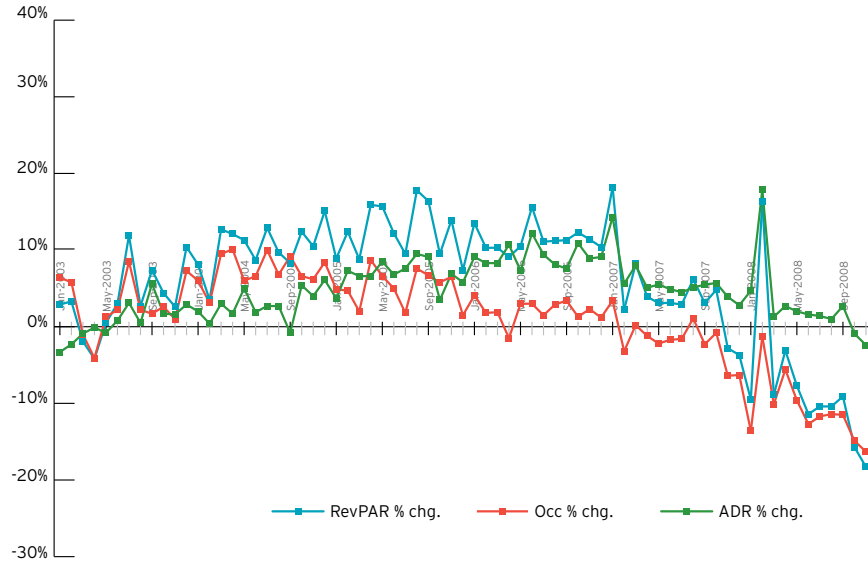
210 Scott Wong, "Bidwill project could generate \$2.6 bil a year, report says," *The Arizona Republic*, 15 December 2007.

211 Carrie Watters, "Council backs Bidwill project proximate Loop 101," *The Arizona Republic*, 9 April 2008.

**Phoenix lodging market change in monthly occupancy, ADR, RevPAR performance**

January 2003-November 2008

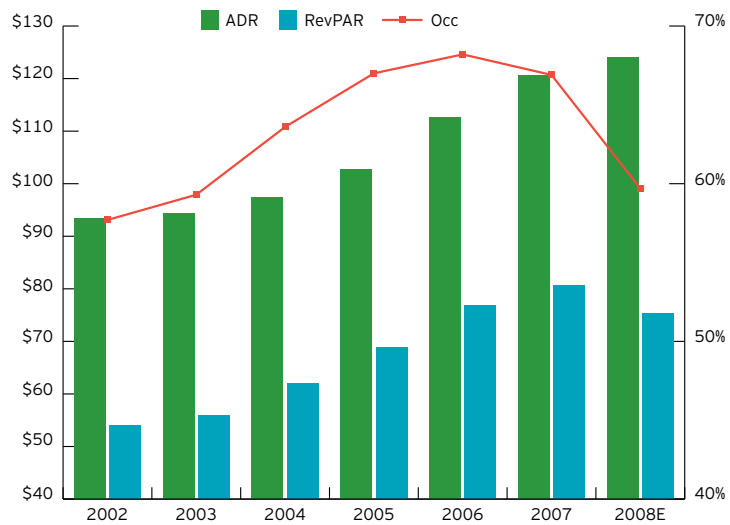
Source: Smith Travel Research  
Monthly Lodging Review



**Phoenix lodging market occupancy, ADR, RevPAR performance (USD)**

2002-2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

Despite demand generators such as the Phoenix Convention Center, the 2009 NBA All-Star Game, light rail and scheduled national venues planned through the high-season, Phoenix's

lodging-industry performance is anticipated to decline in 2009. The Phoenix lodging industry's dependence on the winter tourism season is expected to be further impacted by fallout from the

financial crisis. In addition to the state of the national economy, these costs may limit the number of business travelers to Phoenix through 2009.

## Supply additions

Based on year-to-date September 2008 data from Smith Travel Research, the existing hotel supply is 54,717 rooms. The following chart summarizes selected major supply changes.

Property	Location	Units	Scheduled opening date	Developer/Owner
Residence Inn	Phoenix, Ariz.	208	January 2009	Finvarb Hospitality
Hilton Phoenix Chandler	Chandler, Ariz.	197	March 2009	Western International
Hilton Garden Inn	Phoenix, Ariz.	192	January 2009	Equus Development
Aloft Hotel	Phoenix, Ariz.	143	September 2009	Starwood Hotels
Courtyard by Marriott	Chandler, Ariz.	140	November 2009	White Lodging Services
Aloft Hotel Tempe	Tempe, Ariz.	139	April 2009	Triyar Hospitality Scottsdale
Hyatt Place Gilbert	Gilbert, Ariz.	127	March 2009	Adelson Fijan Properties
Hyatt Place at Mesa Riverview	Mesa, Ariz.	127	April 2009	Wolff Urban Development
Homewood Suites Phoenix	Phoenix, Ariz.	125	January 2009	Cotton Center Hospitality
Value Place Phoenix	Phoenix, Ariz.	121	April 2009	Value Place, LLC
Aloft Hotel Glendale	Glendale, Ariz.	120	December 2009	Glendale 13.5 LLC
Legacy Suites Hotel	Gilbert, Ariz.	107	June 2009	Structures Inc.
Hampton Inn Suites	Gilbert, Ariz.	96	July 2009	Paramount Investor Group
Legacy Suites Tolleson	Phoenix, Ariz.	540	June 2009	Inland Empire Builders
eSuites Hotel Phoenix	Phoenix, Ariz.	224	July 2009	Phoenix E Suites LLC
Hampton Inn Suites Chandler	Chandler, Ariz.	153	October 2009	DLR Group
Homewood Suites Tempe	Tempe, Ariz.	140	August 2009	Huntington Hospitality Group
Homewood Suites Chandler	Chandler, Ariz.	136	October 2009	DLR Group
Springhill Suites oeni-Mesa East	Mesa, Ariz.	134	May 2009	Khangura Developments
Hyatt Summerfield Suites	Avondale, Ariz.	127	November 2009	EDGE Construction Group
Cambria Suites Scottsdale	Scottsdale, Ariz.	125	September 2009	ZMC Hotels
Staybridge Suites	Goodyear, Ariz.	121	September 2009	InterContinental Hotels Group
Radisson Glendale	Glendale, Ariz.	120	June 2009	Glendale 13.5 LLC
Courtyard by Marriott Phx/Mesa	Mesa, Ariz.	114	April 2009	Hansji Hotels Inc
Residence Inn	Mesa, Ariz.	135	December 2009	VJ Crimson LLC

Source: Smith Travel Research

# San Diego

## Introduction

The San Diego lodging market showed mixed results in 2008. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 3.1 percentage points to 69.8% in 2008 compared to 2007. However, due to the strong convention center performance, increased military spending and strong drive-in visitation, ADR is expected to increase 1.3% to US\$141, resulting in a RevPAR decline of 2.0% to US\$99.

## Hot topics

### San Diego not immune to economic slowdown

The US economic slowdown negatively impacted many aspects of the San Diego economy in 2008, including unemployment, commercial and residential home values and corporate profits. The San Diego unemployment rate was 6.4% as of September 2008, an increase of 1.6 percentage points from the prior year, while the number of businesses filing for bankruptcy increased by approximately 85.0% through July 2008.<sup>212</sup> Further, San Diego office vacancy increased 1.1% to 17.1%<sup>213</sup> during third quarter 2008 at the same time that home values decreased by approximately 17% through August 2008<sup>214</sup> – resulting in decreased wealth and decreased lodging demand. However, despite the economic slowdown, the military and defense industry remains a significant contributor to the San Diego economy and accounts for approximately 27.0% of all jobs in the county.

Government spending on military and defense in San Diego County increased approximately 7.0% to US\$15.5 billion in 2008. Further, defense spending is anticipated to increase in the coming years, making San Diego County the largest recipient of government military spending in the nation.<sup>215</sup>

### Lodging supply on the rise

While San Diego experienced a 3.1 percentage point decrease in occupancy through year-to-date November 2008, much of the decrease can be attributed to increased lodging supply. Lodging supply in San Diego County increased 2.6% to 55,266 rooms during the same time period. According to Smith Travel Research, supply should increase an additional 4.6% to 57,784 by the end of 2009.<sup>216</sup> Although lodging supply experienced a significant increase in 2008, credit market conditions have caused the cancellation or delay of significant lodging developments,



including the cancellation of the 2,000-room Gaylord Entertainment resort with 400,000 square feet of proposed convention space. Lodging developments in San Diego may continue to experience cancellations or delays in 2009 unless credit-market conditions improve.

In addition to area hotels' rising vacancy rates, the San Diego office market is experiencing a similar trend.

### "San Diego – The Road to Happiness"

The San Diego tourism industry has historically performed well in difficult economic times due to a strong drive-in market. While San Diego visitation decreased approximately 1.1% through year-to-date September 2008, total visitor spending increased approximately 2.8%. Tourism officials expect to attract vacationers through a new US\$1.75 million marketing initiative with the slogan "San Diego – The Road to Happiness."

212 Zach Fox, "Downturn has led to surge in business bankruptcies in San Diego County," *North County Times*, 3 August 2008.

213 "MarketView: San Diego Office," CB Richard Ellis, Third Quarter 2008. [www.cbre.com/research](http://www.cbre.com/research) accessed on 24 November 2008.

214 Case-Shiller Home Price Index, S&P. August 2008, <http://www2.standardandpoors.com> accessed on 29 October 2008.

215 Dean Calbreath, "Military Seen As Stabilizing Economic Force in County," *The San Diego Union-Tribune*, 20 August 2008.

216 Smith Travel Research, 25 September 2008.



The campaign will focus largely on the major drive-in feeder markets of Los Angeles, Orange and San Bernardino counties, as well as Phoenix and Las Vegas<sup>217</sup> – approximately 70.0% of San Diego visitors originate from these markets. In addition, San Diego officials are attempting to target more local tourists by promoting “staycations.” San Diego may also be in a position to benefit from travelers trading down from Hawaiian or overseas vacations and opting for a less expensive San Diego vacation.<sup>218</sup>

San Diego is planning a marketing campaign to attract more international visitors. Approximately 4.1% of San Diego’s overnight visitors were from international locations in 2007, and San Diego is currently the 10th-most-visited city in the US by international travelers. The San Diego Convention & Visitors Bureau is planning a US\$19 million international marketing campaign in

2009, funded through a new 2.0% fee added to hotel-room bills. In addition, San Diego officials are working with Los Angeles tour operators to include San Diego on their itineraries. Los Angeles ranks second among US cities receiving the most international visitors.<sup>219</sup>

#### **San Diego: not the sky to happiness, for some airlines**

Many major airlines, including Southwest, ExpressJet, United Airlines and American Airlines, decreased airlift to and from San Diego as a result of the economic slowdown and increased operating costs. As a result, San Diego International Airport is projected to experience an 8.6% decrease in seat capacity in the fourth quarter of 2008 compared with the same period in 2007.<sup>220</sup> Although many major airlines are decreasing flight capacity to San Diego in the short term, airport officials are planning a US\$700 million expansion project that is scheduled to

begin construction in early 2009. The expansion plans include the construction of 10 additional gates, a 5,000-space parking structure, a jet parking lot and a variety of road improvements surrounding the airport.<sup>221</sup> The new infrastructure of the airport will benefit San Diego in the long term, sustaining additional visitors to the area.

#### **Convention business blossoms in economic fall**

The San Diego convention market experienced an increase in performance during fiscal year 2008 (ended 30 June 2008), as the San Diego Convention Center hosted 234 events with total attendance of 996,226, an increase of 14 events and 12,520 attendees from fiscal year 2007. Further, convention attendees spent approximately US\$751.8 million at area hotels, restaurants, shops and local attractions, an increase of approximately 15.0% from the prior fiscal year.<sup>222</sup> While the

217 Penni Crabtree, “Local tourism more fizzle than fireworks - Officials hope freebies, ads can save summer,” *San Diego Union-Tribune*, 1 August 2008.

218 “Revised 2008 Forecast,” San Diego County Visitors Bureau, [www.sandiego.org](http://www.sandiego.org) accessed on 15 October 2008.

219 Connie Lewis, “Foreign Travelers to San Diego Drop 1 percent,” *San Diego Business Journal*, 9 June 2008.

220 Penni Crabtree, “U.S. carriers to slash their domestic capacity,” *San Diego Union-Tribune*, 15 June 2008.

221 Mike Allen, “Board Clears Lindbergh Field Plans for Takeoff,” *San Diego Business Journal*, 12 May 2008.

222 Penni Crabtree, “Record impact for convention site in fiscal '08,” *San Diego Union-Tribune*, 12 September 2008.

San Diego Convention Center's performance is anticipated to decline in fiscal year 2009, the decrease is expected to be partially mitigated by the fact that most conferences are booked three to five years in advance. San Diego Convention Center is projected to

host 978,805 attendees and generate spending of US\$648.1 million during fiscal year 2009.<sup>223</sup> Additionally, in August 2008, San Diego hosted the American Society of Association Executives & The Center for Association Leadership (ASAE). ASAE officials

estimate that 20.0% of executives attending the convention will book their own meetings sometime over the next five years, providing approximately US\$1 billion in future meeting and convention business.<sup>224</sup>

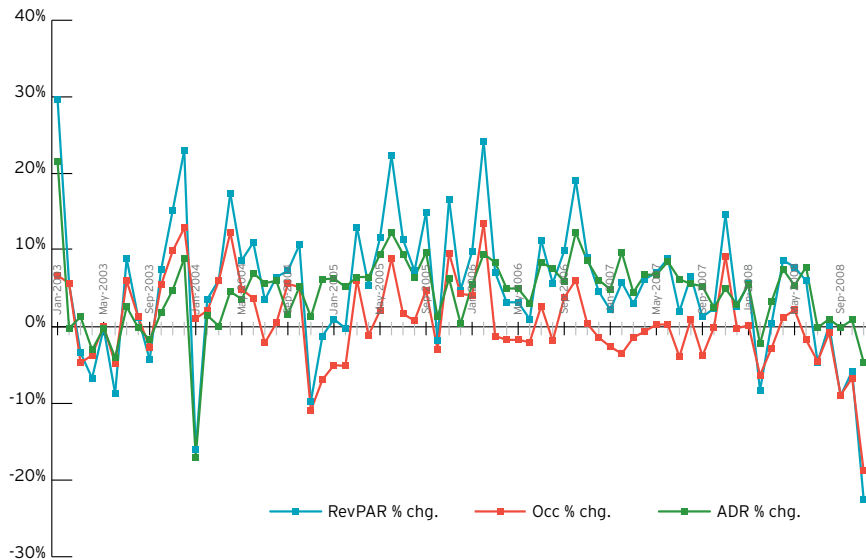
223 Penni Crabtree, "Record impact for convention site in fiscal '08," *San Diego Union-Tribune*, 12 September 2008.

224 Penni Crabtree, "San Diego to host Super Bowl of convention meeting trade," *San Diego Union-Tribune*, 16 August 2008.

### San Diego lodging market change in monthly occupancy, ADR, RevPAR performance

January 2003–November 2008

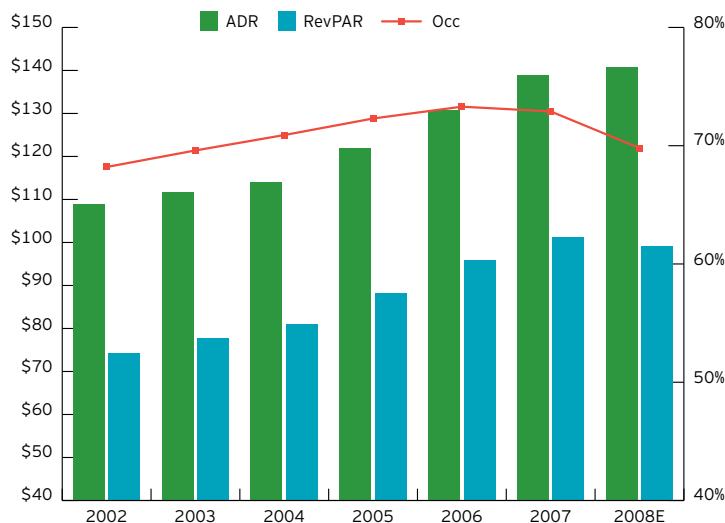
Source: Smith Travel Research  
Monthly Lodging Review



### San Diego lodging market occupancy, ADR, RevPAR performance (USD)

2002–2008E

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

San Diego hotels experienced flat RevPAR growth through September 2008, with increased ADRs and decreased occupancy levels. While San Diego has benefited from increased military spending, strong convention business and strong drive-in visitation, the lodging industry is anticipated to be negatively impacted in 2009 by the economic slowdown, decreased airlift and significant increases to lodging supply.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2011.

Property	Location	Units	Scheduled opening date	Developer/owner
Holiday Inn	Oceanside, Calif.	101	March 2009	Shiva Management Corporation
Best Western San Diego	San Diego, Calif.	99	May 2009	Otay Hospitality
Westin La Jolla Commons	La Jolla, Calif.	327	June 2009	Makar Properties
Marriott Hotel	Escondido, Calif.	196	Fall 2009	C.W. Clark Inc.
Hilton San Diego Convention Center	San Diego, Calif.	1,190	2009	Clarion, Portman Holdings and Phelps Program Management
Hampton Inn and Suites	Poway, Calif.	108	2009	Ocean Park Hotels Development Office
Hotel Indigo	San Diego, Calif.	210	2009	Intercontinental Hotels Group PLC
Best Western Bay Marina Hotel	National City, Calif.	173	2009	Not available
Candlewood Suites Hotel - Escondido	Escondido, Calif.	76	2009	Pacifica Companies
Residence Inn - Gaslamp	San Diego, Calif.	185	2009	Franklin Croft Hospitality LLC
Westin Oceanside Hotel	Oceanside, Calif.	289	Spring 2010	S.D. Malkin Properties and Interstate Hotels & Resorts
InterContinental	San Diego, Calif.	550	2010	Manchester Development
Nickelodeon Family Resort Hotel	San Diego, Calif.	650	2010	McMillin Companies
Marriott Renaissance Hotel	San Diego, Calif.	369	2010	Not available

Source: Smith Travel Research, San Diego & San Diego County Visitors Bureau

# San Francisco

## Introduction

San Francisco continued to experience strong lodging fundamentals in 2008, largely due to a record-breaking convention season, strong international visitation and a growing technology sector. The city is anticipated to experience the second highest RevPAR increase in 2008 of all markets covered in this report, just behind New Orleans. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 0.3 percentage points to 74.9% in 2008, with ADR increasing 5.0% to US\$156; the resulting RevPAR of approximately US\$117 is an increase of 5.1% over 2007.

## Hot topics

### San Francisco economy: impacted by US downturn, but faring better than others

As with other major US cities, San Francisco has been negatively impacted by the US economic downturn, as its unemployment rate rose and housing prices fell in 2008. However, San Francisco continues to lead the pack as one of California's strongest economies, primarily due to strong tourism and biotech sectors. According to the Employment Development Department, the unemployment rate in the San Francisco-San Mateo-Redwood City metropolitan statistical area was 5.6% as of October 2008, representing an increase of 1.6 percentage points from October 2007.<sup>225</sup> California as a whole, however, had an unemployment rate of 8.2%. Like many other cities, San Francisco also saw its home prices

decline significantly. During the fourth quarter of 2008, housing prices in the city declined 29.5% compared with the same period a year ago.<sup>226</sup> A recent study conducted by Beacon Economics estimates that in Marin, San Mateo and San Francisco counties, home prices will decline 25.0% from their peak through the first quarter of 2010.<sup>227</sup>

### New building codes: San Francisco goes green

San Francisco Mayor Gavin Newsom passed a number of stringent green building-code laws in August 2008, making San Francisco the most environmentally progressive city in the US. These laws – which will require new and renovated private-sector buildings to meet LEED Gold standards by 2012 – will apply to most buildings in the city, including “residential projects of all sizes, new commercial buildings over



a certain size, and renovations of large commercial spaces.”<sup>228</sup> Based upon a study conducted by the US Green Building Council, green commercial buildings, on average, save 30.0% more energy, have 90.0% less waste and experience a 9.0% decrease in operating costs compared with standard buildings.<sup>229</sup> For hotels, these benefits may be even more pronounced, as they are particularly resource-intensive. However, a recent study conducted by the Office of Economic Analysis reported that the new measure may cost the city between US\$30 million and US\$700 million a year, as it could lead to higher rents and cause businesses to locate elsewhere. Other experts have argued the report is inaccurate and have predicted that the new rules would not be financially burdensome on builders, but rather cost-effective.

225 “Silicon Valley Unemployment Rate Grows Even as Jobs Increase,” *Silicon Valley/San Jose Business Journal*, 21 November 2008.

226 Peter Hong, “Home Prices Keep Plunging. LA Sees Some of the Sharpest Declines,” *Los Angeles Times*, 25 November 2008.

227 Tom Abate, “SF Seen As Surviving Downturn,” *San Francisco Chronicle*, 21 October 2008.

228 Wyatt Buchanan, “Newsom Signs Strict Green Building Codes Into Law,” *SF Gate*, 5 August 2008.

229 “Green Hotels Have Greater Value, PKF Says,” *Hospitality.net*, 24 September 2008.



### **San Francisco tourism: tourism funds get a boost**

In an effort to maintain the competitiveness of San Francisco's tourism industry, the city's Board of Supervisors has created a Tourism Improvement District (TID). The TID will assess tourist hotels 0.75% to 1.50% on gross revenues over the next 15 years, beginning 1 January 2009. In 2009 alone, the TID will generate an estimated US\$27 million, US\$9 million of which would be for upgrading the Moscone Center and US\$18 million would be for marketing and promoting the city. This US\$18 million marketing budget is a significant increase from the Convention and Visitor Bureau's current fund of US\$8.2 million and is anticipated to better position San Francisco to compete against other popular tourist destinations, such as San Diego and Los Angeles. Currently,

tourism is San Francisco's number-one industry, generating about US\$8 billion each year.<sup>230</sup>

### **Convention activity: a flat, but strong, convention year ahead**

2008 was a record-breaking convention year for San Francisco, with more than 1.6 million room nights booked – a 19% increase from 2007. And the San Francisco Convention and Visitor's Bureau (SFCVB) predicts 2009 to be as strong. As of August 2008, 1.1 million room nights have been booked for the 2009 season, but this number is expected to increase significantly, as a number of citywide and "self-contained" events have yet to be booked for 2009. Oracle is anticipated to be among the most significant San Francisco conventions in 2009. Oracle generated approximately US\$71 million and attracted more than 45,000 attendees in 2008.

### **Office market weakens while biotech flourishes**

Approximately 595,000 square feet of available office space, representing 1.0% of the total market, entered the San Francisco office sector during the third quarter of 2008 with the collapse of numerous financial firms, thereby increasing vacancies and placing downward pressure on lease rates. During the third quarter of 2008, vacancy in the San Francisco downtown market increased to 10.4%, representing a 2.0% increase year-to-date, while lease rates declined to US\$41.41, representing a 3.4% decrease from the second quarter of 2008.<sup>231</sup> Such an event may likely affect demand for lodging in 2009, as it may affect business travel to the city. Biotech office and R&D space, however, continued to perform well in the Bay Area, largely due to the strength of the technology

230 Sarah Duxbury, "S.F. Hotels to Boost City's Tourism Funds," *San Francisco Business Times*, 22 October 2008.

231 *San Francisco Office MarketView*, CB Richard Ellis, 3rd Quarter 2008.

sector. The technology sector has been a significant driver for employment growth in San Francisco and Marin Counties despite the broader US economic slowdown. Between February 2007 and February 2008, the region added 19,000 jobs, a 1.9% increase, surpassing all other metro areas in California.<sup>232</sup> Over the next two years, developers plan to construct an additional 2.3 million square feet of biotech and R&D space in order to meet the increasing needs of a maturing Bay Area biotech community.<sup>233</sup> This is anticipated to positively affect the lodging industry, as a strong biotech industry would increase business and corporate travel in the R&D and biotech sector.

**Visitation: passenger traffic rising, but airport expansions on hold**

Despite a slowing economy, passenger traffic at San Francisco International Airport (SFO) is projected to increase 9.1% in 2008 and an additional 5.7% in 2009. The increase in passenger volume can primarily be attributed to strong international travel from Europe, Asia and Australia and aggressive expansion plans by low-fare domestic airlines, including Jetblue Airways Corp., Southwest Airlines Co. and Virgin

232 T.S. Mills-Faraudo, "Tech, Biotech, Media Are Adding Hundreds of Jobs," *San Francisco Business Times*, 11 April 2008.

233 Ron Leuty, "Building Boom Meets Maturing Biotech's Needs," *San Francisco Business Times*, 29 August 2008.





America Inc.<sup>234</sup> Between January and August 2008, SFO attracted 3.2 million international visitors, representing a 4.4% increase from the same period last year. Over the next few years, San Francisco is expecting a significant increase in Chinese visitors due to an agreement signed in December 2007 between China and the US aimed at facilitating group leisure travel from China to the US. While San Francisco attracts approximately 100,000 Chinese visitors annually, this number is anticipated to double to 200,000 by 2011, according to the SFCVB.<sup>235</sup> Though beneficial for the San Francisco economy, the increase in visitation and passenger traffic may soon create problems for SFO, as rising fuel costs and a slowing economy have forced the airport recently to postpone plans for new runways. Currently, SFO operates at approximately 80.0% capacity and may soon reach its full capacity if the economy rebounds.<sup>236</sup>

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234 Eric Young, "SFO Rides High On International Travel," *San Francisco Business Times*, 15 February 2008

235 Anne Makovec, "Chinese Tourists Expected to Flood Bay Area," *ABC Local News*, 28 June 2008.

236 Steve Ginsberg, "Economy Puts Bay Area Airports in Holding Pattern," *San Francisco Business Times*, 15 August 2008.



## Key takeaways

San Francisco has continued to experience healthy lodging fundamentals in 2008 – though at a slower growth rate – due to a strong tourism industry coupled with limited supply. However, with declines in the overall economy, it is anticipated that business travel, and consequently lodging demand, will be negatively affected in the short term.



## Supply additions

Based on year-to-date September 2008 data from Smith Travel Research, the existing hotel supply in San Francisco is estimated at approximately 51,128 rooms. The following chart summarizes selected major supply changes.

Property	Location	Units	Scheduled opening date	Developer/owner
Hyatt Place San Francisco Airport	South San Francisco, Calif.	159	April 2010	TBD

Source: Smith Travel Research

# Washington, D.C.

## Introduction

During 2008, lodging performance in Washington, D.C., was characterized by growth in ADR and declines in occupancy. Based on year-to-date November data from Smith Travel Research, occupancy is anticipated to decrease 1.5 percentage point to 67.0% in 2008, with ADR increasing 2.0% to US\$152; the resulting RevPAR of US\$103 represents an increase of 0.5% from 2007.

## Hot topics

### The capital city: positive effects on lodging

The current state of the US economy will likely have a negative effect on the performance of the Washington, D.C., lodging market in 2009. However, the downturn may be mitigated by certain factors inherent to the capital city's tourism market. The recent administration changes are anticipated to support government-related visitation to the Washington, D.C., market. As the country focuses on Washington, D.C., for the inauguration of a new president, lodging performance should be positively influenced during the short period surrounding the inauguration and related events in January. The last inauguration occurred in January 2005, when demand increased 5.1% versus the prior year; however, 2004 was also an election year for the House of Representatives and the Senate, which further increased lodging demand in 2004. In the five previous election cycles, annual occupancy increases averaged 2.9 percentage points above the previous year's level.

The Washington, D.C., market is further supported by the government per diem rates for overnight accommodations, which are expected to range from US\$165 to US\$233 during fiscal year 2009 (October 2008 to September 2009), up from a 2008 range of US\$154 to US\$201.<sup>237</sup> The per diem rate in Washington, D.C., is among the highest of the major US markets and may provide some insulation from the struggling national economy. Although leisure travel by domestic visitors to the capital may be reduced by factors such as increasing airfare prices and decreasing consumer spending in 2009, the city does offer an attractive destination for many US travelers. By being a drive-to destination from many Northeast population centers and offering a high number of free attractions, Washington, D.C., is a high-value destination compared with other national and international locations.



### International visitation: foreign visitation anticipated to rise

While domestic visitation may decrease, international visitation to the capital is projected to remain flat or marginally increase in 2009 and 2010, depending on changes in the value of the dollar relative to other currencies. With the current state of the economy, visitation to the Washington, D.C., market is projected to decline by an estimated 1.9% in 2009, to 15.7 million visitors, due to declines in domestic tourism. The projected decrease in domestic visitation is partially attributed to a projected slow convention year, due to tightening corporate budgets and the rotating schedules of annual conventions that in 2009 will not take place in Washington, D.C.. Approximately 8% of visitors to the capital are international – approximately 1.2 million in 2007. This annual visitation is expected to increase slightly each year until 2011, when international visitors are projected to reach approximately 1.3 million, returning to pre-9/11 levels. However, the fluctuation in international currencies and the

237 "Domestic Per Diem Rates," US General Services Administration, [www.gsa.gov](http://www.gsa.gov) accessed on 16 October 2008.



US dollar may influence international visitation. Recently expanded air links to feeder markets in Asia, Europe, the Middle East and South America are anticipated to support an increase in international visitation. New routes include United Airlines service from Beijing, Rome and Rio de Janeiro; Qatar Airways service from Doha; and Copa Airlines service from Panama City.<sup>238</sup>

**Cultural attractions: positive impact on domestic visitation**

The recent renovation of the National Museum of American History (a Smithsonian Institution museum), the opening of the Capitol Visitor Center and the Abraham Lincoln Bicentennial Birthday celebration are three cultural demand generators that may have a positive effect on tourism to Washington, D.C., in 2009. The 42-year-old National Museum of American History, with an anticipated attendance of 3 to 4 million visitors per year, re-opened in November 2008 after a major renovation and the

addition of a Star-Spangled Banner exhibit.<sup>239</sup> Opened on 2 December 2008, the Capitol Visitor Center is located below the US Capitol and includes auditoriums, exhibit space, and a TV and radio studio, along with several dining outlets and retail shops.<sup>240</sup> Lastly, the Abraham Lincoln Bicentennial birthday celebration will run through the first half of 2009.<sup>241</sup> The event includes several dedication ceremonies, receptions and exhibits around the city and has a projected attendance of 4 million visitors.<sup>242</sup> These cultural attractions are expected to mitigate declining domestic visitation trends.

**Waterfront redevelopment: increasing tourism in the long term**

Waterfront redevelopment in Washington, D.C., is active, with two major redevelopments under way: the National Harbor mixed-use development and the revitalization of the Anacostia waterfront. The National Harbor project, a US\$2.1 billion development

located along the Potomac River in Prince George's County, Md., began construction in 2005 and includes retail, residential and lodging projects, as well as a marina and several piers. The 2,000-room Gaylord National Resort and Convention Center – the principal lodging development in the National Harbor project – opened in April 2008, representing a large portion of the total lodging supply increase in Washington, D.C., in 2008. The second development, the US\$10 billion revitalization of the Anacostia waterfront located in the Southwest area of Washington, D.C., includes several mixed-use projects and the new Washington Nationals baseball stadium – the first LEED-certified baseball stadium in the country. The redevelopment plan for the entire area includes 3 million square feet of office space, approximately 500 residential units, 20 miles of riverside trails, and 23 acres of new parkland.<sup>243</sup>

238 "Washington, D.C.'s 2007 Visitor Statistics," [www.washington.org](http://www.washington.org) accessed on 16 October 2008.

239 "Cultural Tourism Projected Attendance," [www.washington.org](http://www.washington.org) accessed on 16 October 2008.

240 "The Capitol Visitor Center," [www.aoc.gov](http://www.aoc.gov) accessed on 5 February 2009.

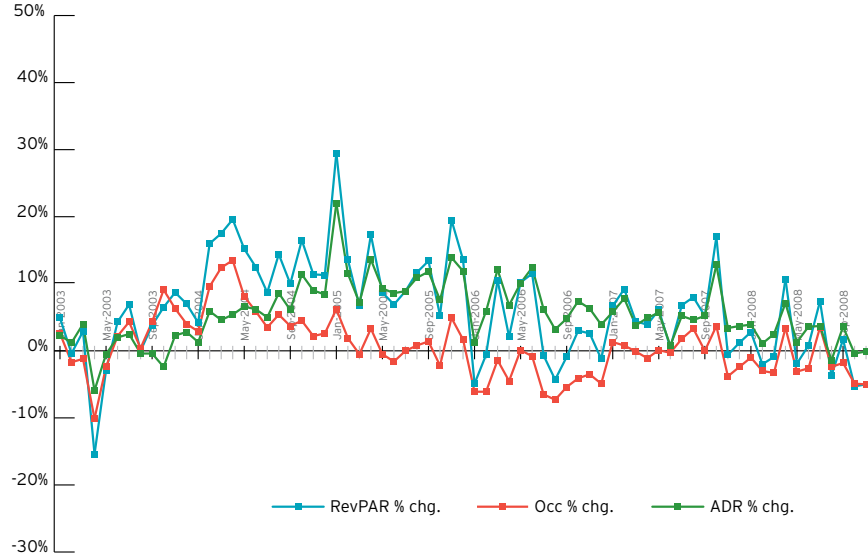
241 "Lincoln Bicentennial," [www.lincolnbicentennial.gov](http://www.lincolnbicentennial.gov) accessed on 16 October 2008.

242 Ibid.

243 Rachel Cooper, "Anacostia Waterfront: Washington, D.C.'s Biggest Revitalization Project," [www.about.com](http://www.about.com) accessed on 16 October 2008.

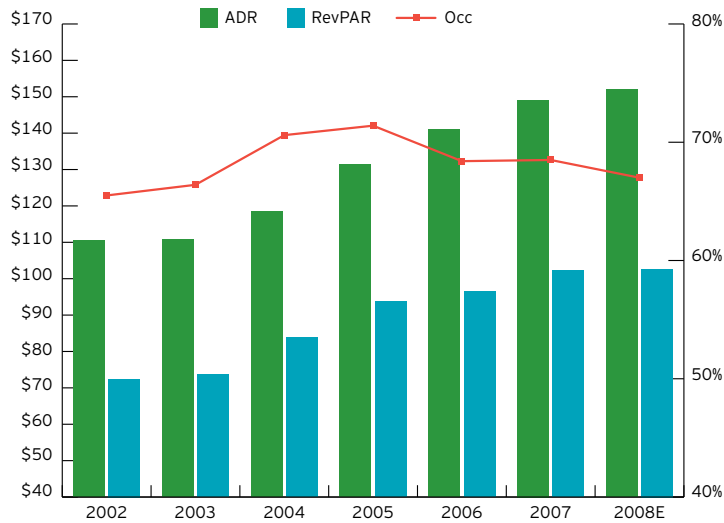
**Washington, D.C. lodging market  
change in monthly occupancy,  
ADR, RevPAR performance  
January 2003-November 2008**

Source: Smith Travel Research  
Monthly Lodging Review



**Washington, D.C. lodging market  
occupancy, ADR, RevPAR  
performance (USD)  
2002-2008E**

Source: Smith Travel Research  
Monthly Lodging Review



## Key takeaways

The Washington, D.C., lodging market in 2009 will be challenged by declining economic conditions and declining domestic visitation. However, changes in both the administration and cultural tourism attractions may partially mitigate the negative effects on lodging performance in the coming year. Additionally, the continued market support from the government per diem rates for hotels will help support the city's lodging market. In the medium term, progress on waterfront redevelopments in the Washington, D.C., metro area should have a positive effect on the market.



## Supply additions

Based on year-to-date September 2008 data, the following chart summarizes selected major supply changes from 2009 through 2012.

Property	Location	Units	Scheduled opening date	Developer/owner
Hyatt Place Dulles Station	Herndon, Va.	151	January 2009	OTO Development
Sheraton Herndon Dulles Station Hotel	Herndon, Va.	184	February 2009	OTO Development LLC
aloft Washington National Harbor	Oxon Hill, Md.	190	April 2009	National Harbor Development LLC
Sheraton Dulles North	Sterling, Va.	179	August 2009	NBJ Architecture
Sheraton Dulles South	Chantilly, Va.	249	September 2009	Suffolk Construction Company, Inc.
Marriott Bethesda North & Conference Center (addition)	North Bethesda, Md.	225	September 2009	Marriott International
Salamander Resort & Spa	Middleburg, Va.	168	January 2010	Salamander Hospitality LLC
Marriott Marquis Hotel Convention Center	Washington, D.C.	1,150	January 2012	Tishman Urban Development Corporation

Source: Smith Travel Research





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