Chicago Hotel Industry Outlook: 2009 – 2012

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July 2009

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Introduction

While the national recession continued into the first half of 2009, the Chicago hotel industry, as with many major cities throughout the United States, continued to experience shrinking demand. Looking to the second half of 2009, some evidence suggests that the recession may be nearing an end and the pace of decline may be moderating in the hotel industry.

This article examines several of the historical trends and future sources of supply and demand that are expected to shape the city of Chicago's hotel industry performance during the next three to four years. Additionally, we present findings from our survey of hotel managers throughout Chicago. Based on this data, HVS developed projections of hotel demand, supply, and performance through 2012.

Economic indicators of the future levels of Chicago's hotel demand provide a mixed outlook for recovery. Crain's Chicago Business reported another leap in Metropolitan Chicago's unemployment rate to 10.7 percent in May of 2009, an increase from the 9.9 percent unemployment rate in April and the 9.3 percent unemployment rate of March[1]. Meanwhile, United Airlines, based in Chicago, plans to reduce capacity further, projecting a 9.5 percent annual decrease in capacity for year-end 2009[2]. On a more positive note, the Chicago Purchasing Managers barometer of business activity rose significantly, from 31.4 in March, to 40.1 in April of 2009; during prior recessionary periods, the economy resumed growth roughly four months after the nadir in the Chicago Purchasing Managers barometer[3].

McCormick Place continues to be a key indicator for the Chicago hotel industry; although some bright spots have occurred, overall attendance at events is down this year. The American Wind Energy Association moved its show from the 2008 location of Houston to Chicago's McCormick Place for the May 2009 show. The event reportedly drew 23,000 total attendees, far exceeding attendance at the 2008 show and projections of attendance for the 2009 show[4]. However, the International Home and Housewares show held in March experienced a 13 percent decline in attendance from the year before, and the National Restaurant Association show experienced a 24 percent decline in attendance over the prior year[5].

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[1] "Chicago metro jobless rate hits 26-year high," Crain's Business Chicago 25 June 2009
[2] "United trims capacity, reports Q1 loss," Crain's Business Chicago 21 April 2009
[3] "Biz barometer shows signs of hope," Crain's Business Chicago 30 April 2009
[4] "Wind power convention shifts to Chicago," Crain's Business Chicago 22 April 2009
[4] "Record attendance at WINDPOWER 2009," 25 June 2009. American Wind Energy Association. <http://www.windpowerexpo.org/2009/>.
[5] "Trade show train wreck," Crain's Business Chicago 01 June 2009

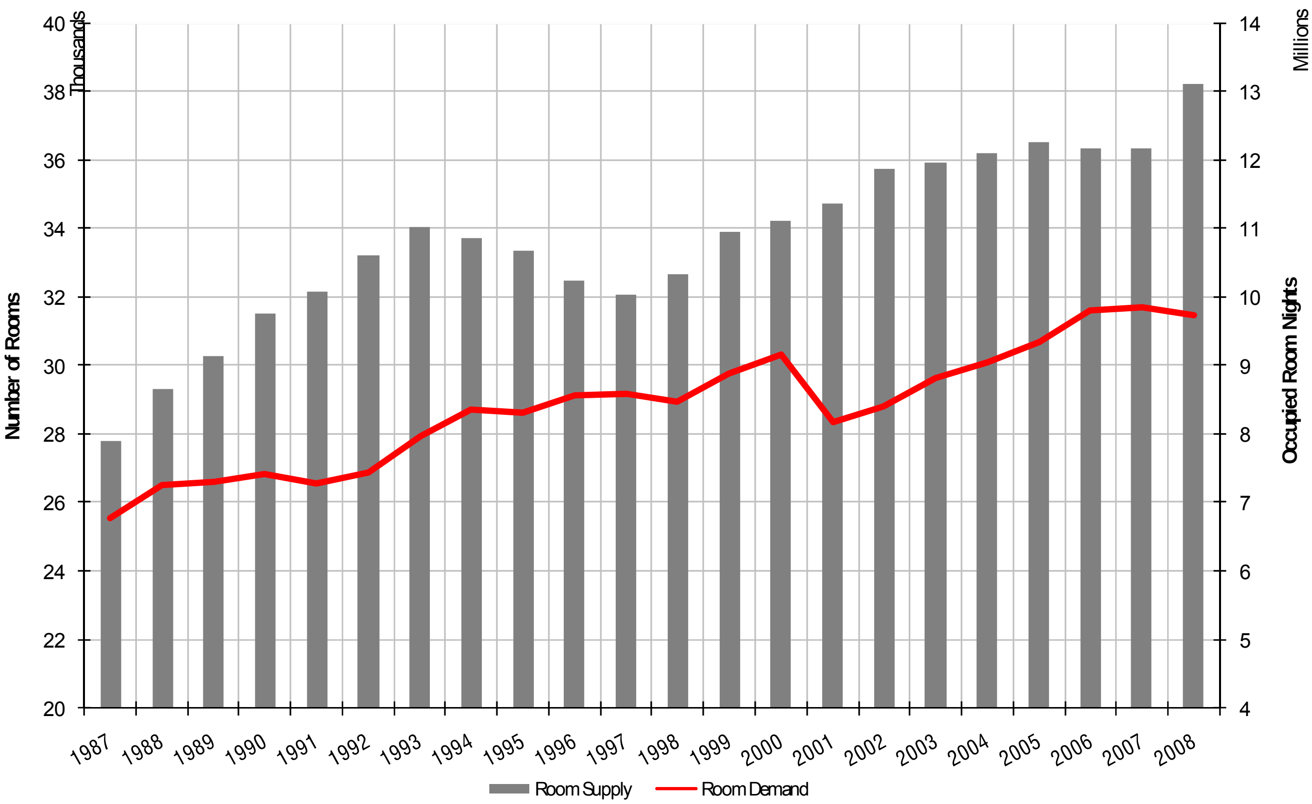
Although the pace of future group bookings at McCormick Place and across the Chicago hotel industry show further deterioration of demand is likely in the group segment through 2009, near-term advance bookings for transient demand in Chicago show an improvement this summer versus last summer. Interviews with hotel managers indicate that the Chicago hotel industry will continue to struggle through 2009. A macroeconomic recovery in Chicago, which the majority of hotel managers expect in mid to late 2010, may lead to growth in hotel demand for 2011 and 2012 that exceeds supply growth. Overall hotel performance is likely to continue to decline year-over-year in the near-term through the end of 2009, but should flatten in 2010, and see growth in 2011 and 2012.

Historical Overview of the Chicago Market

Over the past 22 years, the number of rooms in Chicago has increased by approximately 10,463 units from 1987 through the present, or about 38 percent. Most of this development occurred in two distinct periods of industry expansion. Between year-end 1987 and 1993, the citywide hotel inventory increased by nearly 6,300 rooms, representing a supply increase of approximately 22.6 percent over the six-year period. The hotel room supply decreased by roughly 2,000 rooms between year-end 1993 and 1997. A slower, but longer-lasting, expansion period extended from year-end 1997 through 2005, when the hotel inventory grew by almost 4,500 rooms. Supply declined slightly between year-end 2005 and 2007.

A third cycle of supply growth began when several new hotels opened in 2008, increasing supply by nearly 1,900 rooms in 2008. However, the current economic recession and tightened credit markets are severely limiting the pipeline of new supply expected to take place in the Chicago market during the next several years, as we will discuss later in this article. The following chart sets forth room supply and room demand in the city of Chicago from 1987 through 2008, as reported by Smith Travel Research (STR).

Historical Supply and Demand Trends

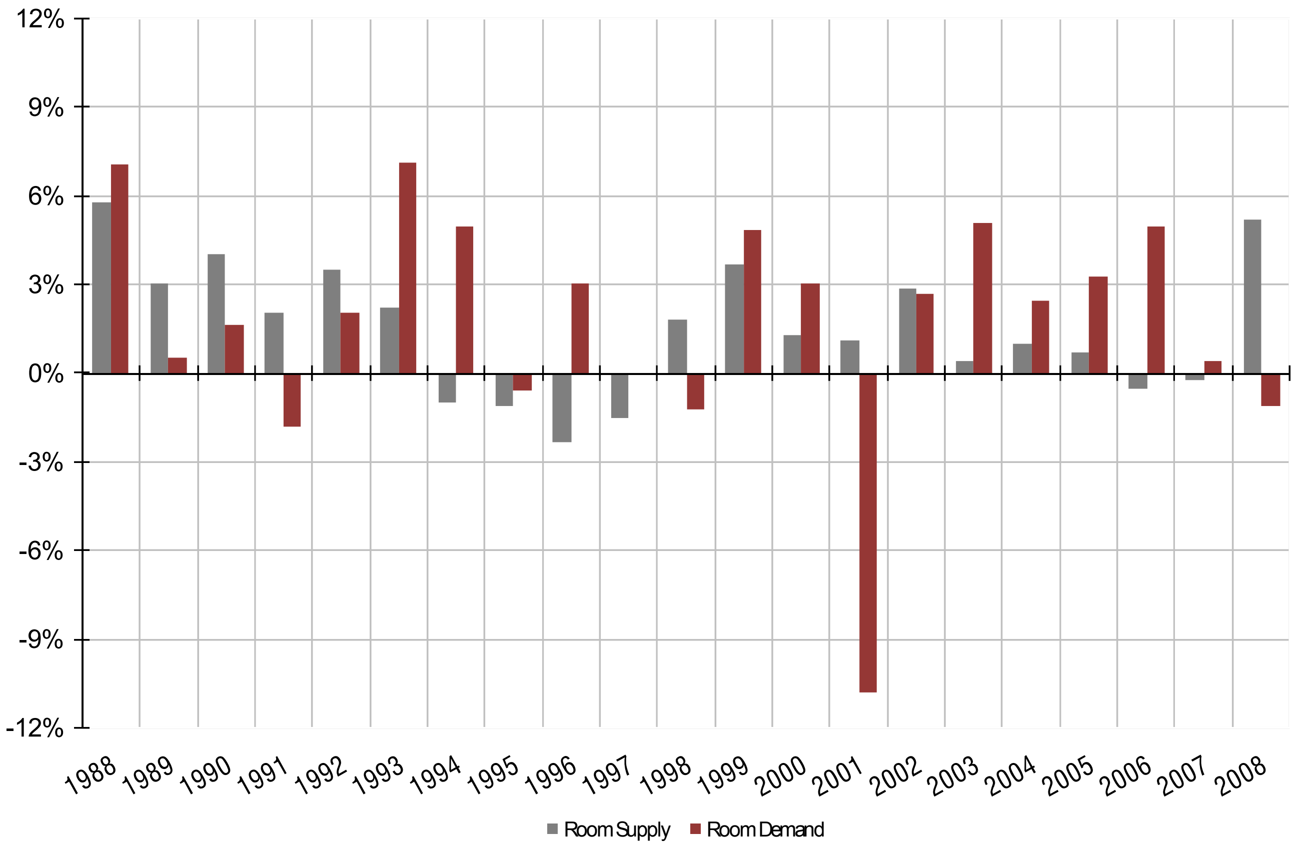


Source: STR

Over the long-term, supply and demand appear to move together, but over short-run periods supply and demand often move in opposite directions. Supply trends are related to the availability and cost of financing as financing is one of the greatest barriers to entry for new hotel development. For example, as interest rates declined throughout the late 1980s and early 1990s, supply grew rapidly. Supply then declined after an upward spike in interest rates in 1993 and 1994 before resuming growth in the late 1990s when interest rates began falling again. As loan-to-value ratios increased and interest rates remained low in the period between 2004 and 2007, an additional wave of projects obtained financing. Eight new hotels opened in 2008. By year-end 2008 there were 38,256 hotel rooms in Chicago, reflecting a significant increase from the 36,381 hotel rooms at year-end of 2007. This new supply growth coincided with a period when demand was actually falling and is partly the result of the relatively inexpensive financing that was available in the preceding years.

Demand and supply both exhibit a long-term growth trend in this market. Demand has increased in 16 of the last 22 years in Chicago, while supply has increased in 15 of these years. The following chart shows year-over-year changes in supply and demand between 1988 and 2008.

Year-Over-Year Changes in Supply and Demand

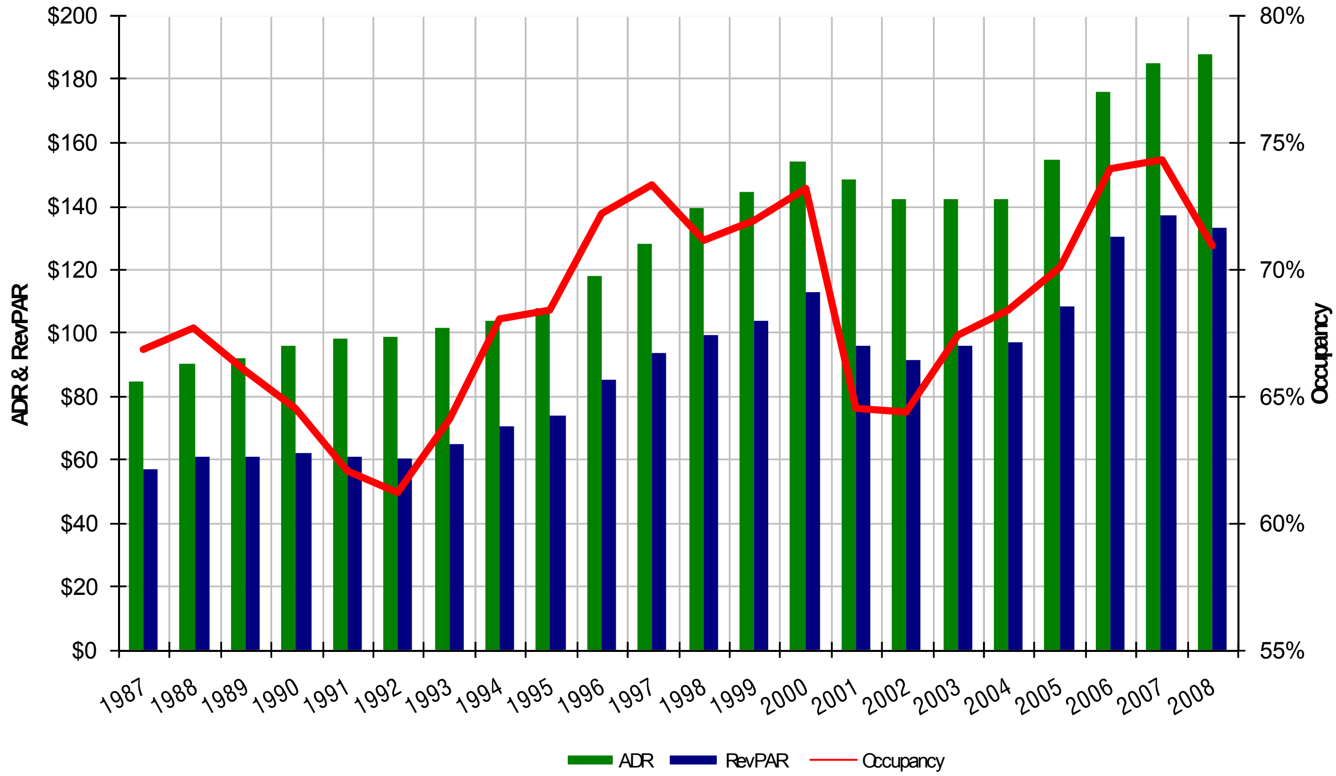


Source: STR

The largest year-over-year declines in demand, in descending order, occurred in 1991, 2001, and 2008 corresponding with the three most recent national economic recessions. In 2001 demand declined by 10.8 percent, reflecting a national downturn in travel due to economic conditions, geopolitical concerns, and the terrorist attacks that took place in September of 2001. Demand increased each year since then. After relatively little supply growth in Chicago between 2003 and 2007, supply increased by 5.2 percent in 2008, thereby exacerbating the negative effects of the economic recession. Corresponding with the national economic recession, demand contracted by 1.1 percent in 2008.

The historical occupancy and average daily rate (ADR) levels in Chicago reflect the relationships between supply and demand. Revenue per available room (RevPAR) is a performance indicator that reflects trends in both occupancy and ADR. The following chart shows annual changes in occupancy, ADR, and RevPAR between 1987 and 2008.

Historical Trends – Performance Measures

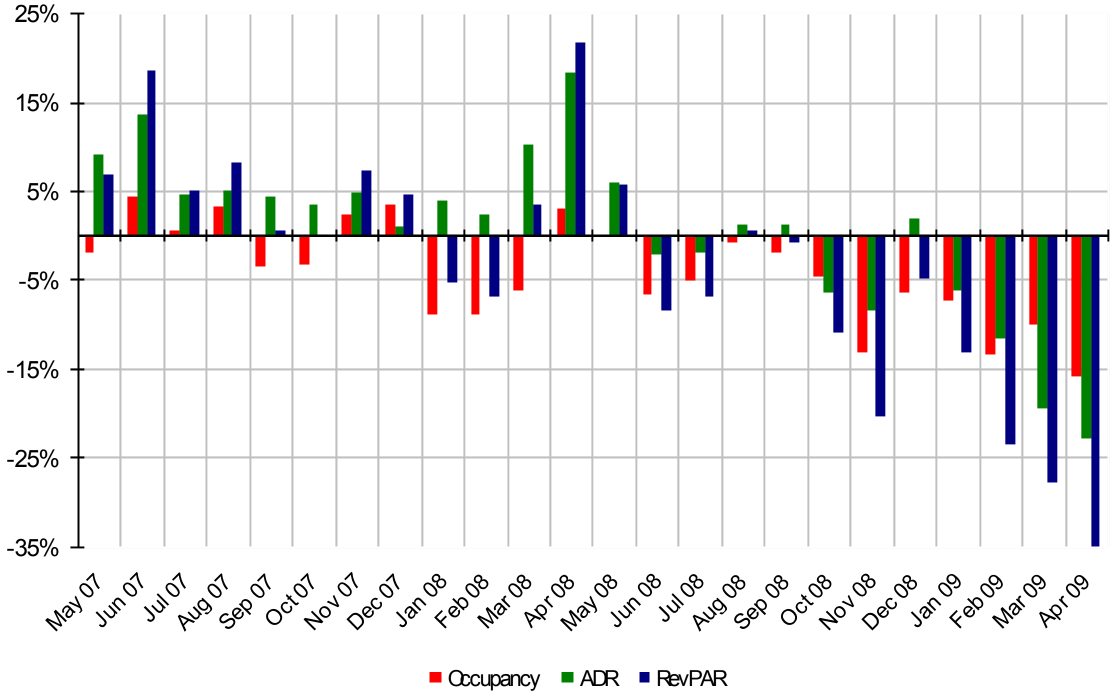


Source: STR

The Chicago hotel market has experienced discernable business cycles since the late 1980s. In 2007 the hotel industry peaked, setting records for the highest occupancy, ADR, and RevPAR levels achieved since 1987, the earliest year for which citywide data records are available. The effects of the national recession negatively affected hotel performance in 2008, when occupancy fell from 74 percent to 71 percent. In 2008, ADR surpassed that of 2007, with an average ADR of $187.6. Nonetheless, increases in ADR were not able to counteract the effect of lower occupancies, resulting in a 2008 RevPAR of $133.0, approximately $4.2 below the RevPAR of 2007.

The past 24 months illustrate the severe negative effects of the recession on the Chicago hotel industry. Hotel performance indicators, with some variation, grew from May of 2007 through May of 2008. From the fourth quarter of 2008 through the first four months of 2009, all three performance indicators have experienced steep declines. The following chart shows year-over-year growth, as a percentage of the monthly figure in the prior year, measured by changes in occupancy, ADR, and RevPAR.

Year-Over-Year Percent Changes by Month – May 2007 through April 2009



Source: STR

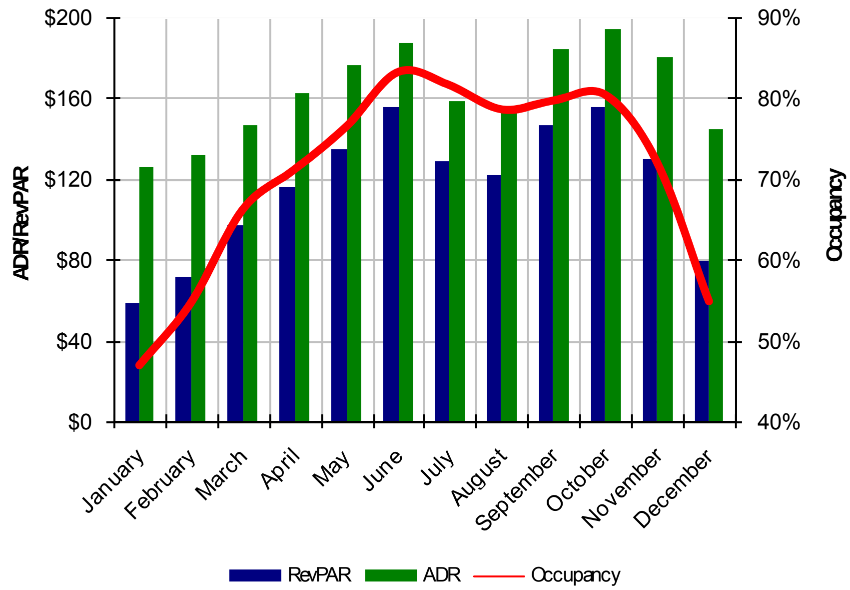
ADR experienced growth in every month between May of 2007 and May of 2008. Occupancy varied during the same time period, consistently falling below the 5.0 decline mark from January through March of 2008. RevPAR generally grew in this same period, experiencing declines in October of 2007, and January and February of 2008. Since May of 2008, occupancies, ADR, and RevPAR have declined rapidly.

The second half of 2008 saw decreases in occupancy and ADR, particularly in the late fall months of October and November. Although December of 2008 saw a RevPAR decline of only five percent, since then, occupancy, ADR, and RevPAR have continued to fall month over month, through April of 2009. However, in April of 2009, for the first time in 2009, the total monthly decline in RevPAR as compared to the same month of 2007 actually shrank, after factoring in the substantial increase from April of 2008. This suggests that June, July and August are likely to experience a deceleration in RevPAR declines as they are compared to drops in RevPAR for these months in 2008.

Seasonal Patterns

As in many markets, the Chicago hotel industry experiences significant seasonality. Market demand fluctuates somewhat predictably in monthly and weekly patterns throughout each year. The following chart shows how occupancy levels, ADR, and RevPAR levels have fluctuated from month to month, based on historical monthly average figures since 2003.

Seasonality Patterns by Month

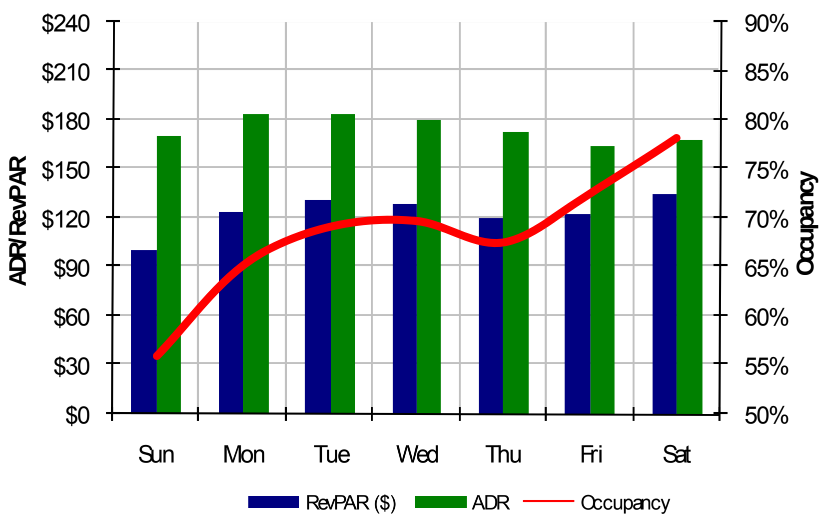


Source: STR

As the preceding chart shows, the late spring months of May and June and early fall months of September and October represent the high seasons for the Chicago hotel industry. During those times of the year, meeting and group demand often peaks, and both commercial and leisure demand levels are also strong. While high occupancies are also attained in July and August, ADR levels during that two-month period are well below those attained in the peak months. The market's low season includes the winter months of December, January and February, when travel activity throughout all demand segments decreases.

The following chart indicates how occupancy levels, ADR, and RevPAR levels fluctuate from day to day throughout a typical week in the Chicago market. These figures are based on average performance data from the period between May 2008 and April 2009.

Day of Week Patterns



Source: STR

Chicago hotels attained the highest RevPAR levels on Saturday, reflecting the importance of the leisure segment during the past 12 months. Historically, RevPAR in the mid-week period, spanning Tuesday and Wednesday, has been relatively high when both commercial and group demand is strong. Chicago hotels typically exhibit their lowest occupancies on Sunday nights, when demand throughout all segments is weak.

Trends in Supply

After several years of slow or negative supply changes in Chicago, there has been a significant introduction of new supply in 2008 and 2009, mainly in the upscale segments. Eight new hotels opened in Chicago during 2008. Through the first half of 2009, four hotels have opened with a total of 880 additional rooms.

During the past six years, a total of 17 new hotels have opened or reopened in Chicago, representing 3,968 hotel rooms. During the same period, eight hotels have closed, representing 521 hotel rooms. Therefore, the net increase in supply was 3,447 rooms between 2003 and 2009. The following table lists the openings and closings identified in recent years.

Recent Changes in Chicago's Hotel Room Supply – Past Six Years

Name of Hotel	Location	Type	No. of Rooms	Opening Date	Closing Date
Courtyard Chicago Downtown	165 E Ontario	Upscale	306	Nov-03	--
Preferred Hard Rock Hotel	230 N Michigan	Luxury	381	Jan-04	--
Hotel Indigo	1244 N Dearborn	Upscale	165	May-05	--
Four Points Mag Mile	630 N Rush	Upscale	226	Jun-05	--
Hampton Inn Theatre District	22 W Monroe	Midscale	135	Apr-07	--
Trump Tower Chicago Hotel	401 N. Wabash Ave	Luxury	339	Jan-08	
SpringHill Suites	410 N. Dearborn	Upscale	253	Mar-08	--
Residence Inn	410 N. Dearborn	Upscale	270	Mar-08	--
Renaissance The Blackstone	636 S. Michigan Ave	Upper Upscale	330	Mar-08	--
Chicago South Loop Hotel	2600 S. State St.	Independent	232	Mar-08	--
Hotel Dana	660 N. State St.	Luxury	216	May-08	--
Club Quarters	111 W. Adams	Independent	89	Jun-08	--
Holday Inn Chicago Midway	6064 S Cicero	Midscale w/o F&B	146	Oct-08	--
Hotel Felix	111 W. Huron St.	Luxury	230	Mar-09	
La Quinta Chicago Downtown	1 S. Franklin	Midscale w/o F&B	233	Apr-09	--
Comfort Suites Chicago	320 N. Michigan Ave	Midscale w/o F&B	119	Apr-09	--
DoubleTree Chicago The Wit	201 N. State St.	Upper Upscale	298	May-09	--
Turf Motel	3126 S Cicero	Independent	(43)	--	Dec-03
Marshall Hotel	4114 W Washington	Independent	(45)	--	Jan-04
Julian Hotel	924 W Belmont	Independent	(58)	--	Aug-04
Jonquil Hotel	1600 W Jonquil	Independent	(70)	--	Jun-05
Mystic Hotel	5522 S Indiana	Independent	(51)	--	Jul-05
Stars Motel	6100 N Lincoln	Independent	(54)	--	Mar-06
South Parkway Inn	2600 S State	Independent	(100)	--	Jul-06
Cedar Hotel	1118 N State	Independent	(100)	--	Sep-07
Net Change in Room Supply (past 5 years)			3,447		

Sources: CCTB, HVS, STR

The development of new hotels does not always lead to a corresponding increase in overall room supply. As newer, better hotels enter a market, lower-rated or inferior hotels and motels may experience significant downward pressure on room rates. This can lead to the decision to close such properties, thereby reducing room supply in the market area. Alternatively, changes in the highest and best use of land can lead to conversions of hotels into other uses. Recent supply changes reveal a continuing move away from independent brands toward nationally branded hotel products. All of the hotels that closed during the past five years in Chicago were independently branded. Twelve of the 17 new hotels that have opened have national brands. Recently, four independent hotels have opened in the luxury and upscale boutique segments.

New Construction & Expansions Planned

Four hotels with a combined total of 880 hotel rooms opened in the first two quarters of 2009. The 188-room Elysian Hotel is currently under construction, with a projected opening in July of 2009. The overall hotel supply in Chicago is expected to increase by 1,068 rooms by year-end 2009.

Additionally, a total of four new hotel properties are expected to open between year-end 2009 and year-end 2011. The anticipated new supply represents a mix of luxury boutique and nationally branded hotels as well as an upscale extended-stay brand. Significant barriers to entry, including increasing energy costs, a lack of available sites, and tightened credit markets continue to be key factors when considering construction of new hotels in Chicago. The following table sets forth the number of new rooms that are anticipated to become available through year-end 2011. No additional hotels are expected to open in 2012.

Recent and Planned Room Supply Changes (2008 through 2011)

Property	Location	Opening Date	Type	Number of Rooms	Development Phase
Trump Tower Chicago Hotel	401 N. Wabash Ave	Jan-08	Independent	339	Open
SpringHill Suites	410 N. Dearborn	Mar-08	Upscale	253	Open
Residence Inn	410 N. Dearborn	Mar-08	Upscale	270	Open
Renaissance The Blackstone	636 S. Michigan Ave	Mar-08	Upper Upscale	330	Open
Chicago South Loop Hotel	2600 S. State St.	Mar-08	Independent	232	Open
Hotel Dana	660 N. State St.	May-08	Independent	216	Open
Club Quarters-Central Loop Hotel	111 W. Adams	Jun-08	Independent	89	Open
Holiday Inn Chicago Midway	6064 S Cicero	Oct-08	Midscale w/o F&B	146	Open
Hotel Felix	111 W. Huron St.	Mar-09	Independent	230	Open
La Quinta Chicago Downtown	1 S. Franklin	Apr-09	Midscale w/o F&B	233	Open
Comfort Suites Chicago	320 N. Michigan Ave	Apr-09	Midscale w/o F&B	119	Open
DoubleTree Chicago The Wit	201 N. State St.	May-09	Upper Upscale	298	Open
Elysian Chicago	11 E. Walton	Aug-09	Independent	188	Under Construction
Hotel Palomar	505 N. State St.	Feb-10	Independent	261	Under Construction
JW Marriott	208 S. LaSalle St.	Jun-10	Upper Upscale	610	Under Construction
Modern Hotel**	330 N. Wabash	2011	Independent	335	Under Construction
Staybridge Suites	127 W. Huron	Jan-11	Upscale	206	Under Construction

**as of May 2009*

***Oxford CG Hospitality Chicago, LLC, an Oxford Capital Group, LLC-led entity, through a Joint Venture with LaSalle Hotel Properties purchased the lower 13 floors of this Mies van der Rohe-designed office building in an all-equity transaction. Pre-construction activities have commenced, while formal construction is expected to commence in 2010/2011 with expected hotel opening in 2012/2013.*

Source: CCTB, Crain's Chicago Business, Respective Properties, Chicago Tribune, Capital Source

Additional properties are in the late planning stages, although we do not expect them to open before 2012. For example, financing and other delays have stalled the following projects:

- Aloft Chicago Millennium Park/City Center (165 rooms)
- Grand Imperial Hotel (170 rooms)
- Hyatt Place (216 rooms)

Numerous additional hotel projects are in early planning phases or have not yet obtained financing. However, it is unlikely that such projects will be realized before the end of 2012. Rather, these projects will most likely appear in subsequent forecasts of supply changes that extend into future years beyond 2012. HVS has identified an additional six additional hotels in the early planning process, some of which have not yet made final branding determinations. These six hotels would represent a total of 1,620 additional hotel rooms.

HVS projects a compounded annual growth rate in supply of between 0.0 percent and 4.3 percent during the four-year period between year-end 2009 and year-end 2012. Based on an evaluation of which projects are under construction or being planned, HVS provides the following forecast of supply changes in Chicago.

Supply Changes – Opened, Under Construction, or Planned

Year	Status	Total Rooms Available	New Projects Open/Under Construction	New Projects in Planning Phase	Room Supply Change	Percent Change
2004	Actual	36,209	—	—	—	—
2005	Actual	36,573	—	—	364	1.0%
2006	Actual	36,385	—	—	(188)	-0.5%
2007	Actual	36,381	—	—	(4)	0.0%
2008	Actual	38,256	—	—	1,875	5.2%
2009	Forecast	39,893	5	—	1,068	4.3%
2010	Forecast	41,528	2	—	871	4.1%
2011	Forecast	42,343	2	—	200	2.0%
2012	Forecast	42,343	—	—	—	0.0%
Total Change (2004 - 2008)					2,047	
Total Change (2009 - 2012)					2,451	
Average Annual Compound Change (2004 - 2012)						2.0%

Sources: Smith Travel Research, CTTB, HVS

Nine new or renovated hotels have opened or are under construction and scheduled to open between 2009 and 2012. However, there a number of projects that had once planned to open in 2011 and 2012 that have recently been stalled. Should any of these projects resume in the end of 2009 or beginning of 2010, there may be additional supply growth in 2011 and 2012. Taking a longer view, the average change in supply from year-end 2004 through year-end 2012 is forecast to be approximately 2.0 percent annually, which matches the longer-term historical average of 2.0 percent.

Near-Term Demand Factors

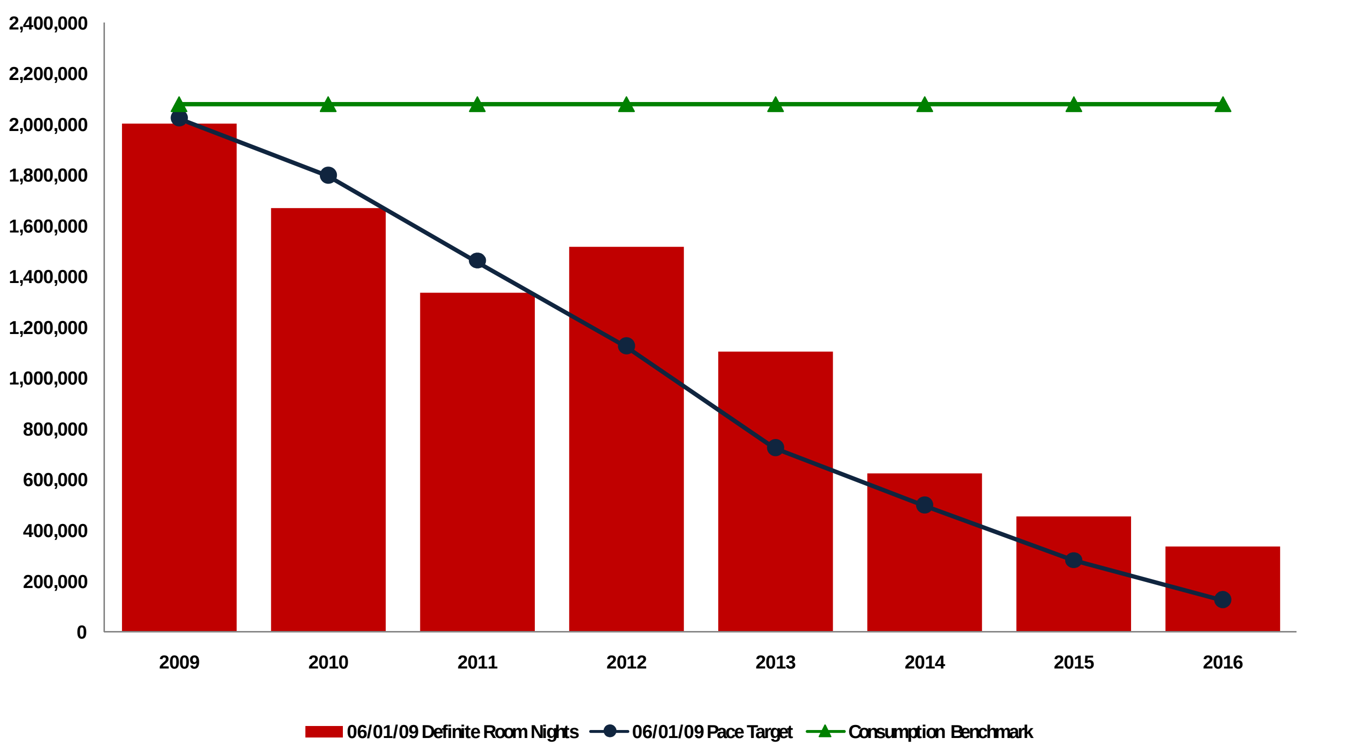
Several near-term demand factors will significantly affect the outlook for Chicago hotels during the next four years. Recently, HVS surveyed the general managers of all Chicago hotels to determine which near-term demand factors they consider to be most important for the industry. The following factors were prominent in these discussions; however, this list is not intended to be comprehensive.

Chicago Convention and Tourism Bureau

The primary marketing organization for the Chicago hotel industry is the Chicago Convention and Tourism Bureau (CCTB). One of the organization's primary goals is to attract large out-of-town groups, requiring large blocks of hotel rooms, to Chicago. The Chicago hotel industry depends significantly on these "citywide" events and other group-oriented room nights sold by the CCTB. Even hotels that primarily target transient corporate or leisure travelers benefit from large volumes of demand in the group segment because fewer rooms are available to serve transient guests when certain hotels commit their rooms to large groups.

The CCTB tracks the advance room nights booked by the CCTB for 2009 through 2016, and compares these actual bookings to a "pace target" in each year. If actual bookings (red bars) equal the pace target (blue line), this would be an indication that the eventual bookings in a given year would equal the consumption benchmark (green line). The following table shows the definite room nights booked by the CCTB through June 1st of 2009 and how it compares to the pace target to meet the consumption benchmark of almost 2.1 million room nights annually.

Room Nights Booked by Chicago Convention and Tourism Bureau



The definite room nights for 2009 are on target so far, indicating that the CCTB will likely match the consumption benchmark in 2009. However, if attrition—event cancellations or reductions in room block sizes—accelerates further, the benchmark may not be achieved. Due to the effects of the national recession, 2010 and 2011 bookings currently suggest that the benchmark will not be achieved in these years. However, if short-term group bookings accelerate in these years, the benchmark could be met or exceeded.

To mitigate the negative effect of the economic recession, the CCTB has undertaken a new marketing campaign aimed at local Fortune 500 companies, in an effort to maximize the number of events held in Chicago by local companies. The CCTB is also trying to capitalize on the public criticism of meetings and events held at resort and luxury destinations, promoting Chicago as “the common-sense choice in uncommon times”.

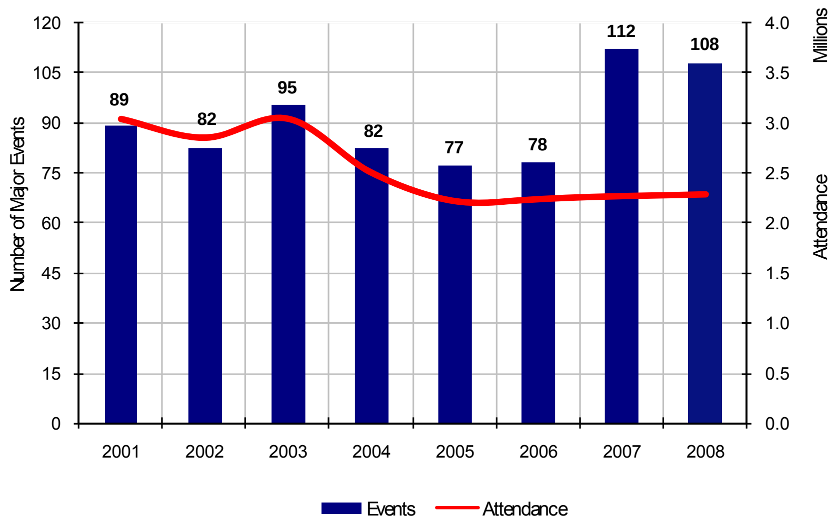
Nonetheless, group demand has softened this year in the Chicago market. As group demand remains weak, many meeting planners have gained negotiating leverage. Some meeting planners are seeking discounted pricing for future years as part of their contracts to book events in 2009 and 2010. This strategy has fueled room night bookings significantly above the pace target for 2012 and 2013, as meeting planners attempt to lock in today’s discounted rates. The data suggests a significant recovery in group businesses will occur in 2012 and 2013.

McCormick Place

McCormick Place is the largest convention center in the United States, offering 2.7 million square feet of exhibition space. The convention center consists of four major buildings: the North and South Buildings, the Lakeside Center, and the newly opened McCormick West Building. Originally built in 1960, McCormick Place has been an important factor in making Chicago one of the world’s premier destinations for major conventions and tradeshows.

The West Building opened in July, 2007. This most recent expansion of the convention center offers an additional 460,000 square feet of exhibition space, a 100,000-square-foot ballroom, and 250,000 square feet of additional meeting space in 61 rooms. The new facility targets mid-sized conventions and tradeshows, which allows Chicago to host multiple conventions simultaneously during periods of peak demand. The following chart shows recent trends in demand, measured by the number of major events and attendance, at McCormick Place, as reported by the CCTB.

McCormick Place – Events and Attendance



Source: CCTB

Since the expansion of McCormick Place in 2007, the number of events hosted at the convention center increased significantly. The new West Building allows McCormick Place to host smaller conventions and meetings that historically have not been booked in Chicago, as well as simultaneous conventions and tradeshows. In 2008, McCormick Place hosted 108 events, drawing slightly greater total attendance than in 2007. The number of events hosted each year at McCormick Place is expected to fluctuate in the near-term, but remain above historical levels, as it reaches a stabilized level of demand.

McCormick Place continued to experience strong demand levels through 2008, despite the economic downturn, due to the fact that most major conventions and tradeshows were booked years in advance. With the national convention center industry experiencing downward pressure in demand at least through 2009, it is likely that McCormick Place, as well, may see a dip in demand levels in the near-term. Additionally, attrition may place downward pressure on attendance as fewer delegates and exhibitors decide to attend conventions and shows that are already booked in future years. However, given an economic recovery within a few years, McCormick Place will continue to represent one of the biggest single demand generators for hotels in the city.

O'Hare and the O'Hare Modernization Program

Chicago benefits from one of the world's busiest airports; O'Hare International Airport served approximately 70.8 million passengers in 2008. Midway International Airport, on Chicago's southwest side, served an additional 17.3 million passengers in 2008. The following table shows the total number of passengers served by O'Hare and Midway from 2004 through April of 2009.

Chicago Airport Passenger Traffic Statistics

	2004	%	2005	%	2006	%	2007	%	2008	%	YTD - April 08	YTD - April 09	%
OHare	75,534	-	76,581	1%	76,282	0%	76,182	0%	70,819	-7%	22,244	19,745	-11%
Midway	19,718	-	17,863	-9%	18,868	6%	19,379	3%	17,346	-10%	-	4,928	-13%

**Year-to-date through April of 2008 not available for Midway (though YTD April 2009 at Midway recorded a reported 12.88 percent decline* in total passengers from YTD April 2008 at Midway)

Source: The Chicago Airport System

O’Hare and Midway, from 2008 through April of 2009, continue to experience declines in passenger traffic. Year-to-date figures through April of 2009 show substantial decreases to year-to-date figures from 2008, with an 11 percent decrease in O’Hare traffic, and a 13 percent decrease in Midway traffic.

The O’Hare Modernization Program (“OMP”) will spend $6.6 billion to reconfigure O’Hare’s runways to significantly increase capacity and reduce delays in all weather conditions at O’Hare International Airport. Federal approvals and funding are already in place for the program. Construction began in 2007 and three phases of development are planned through 2011. As of December 2008, the OMP had awarded nearly $784 million in construction contracts. The first phase of the OMP, the runway redesignation process, is complete. The second phase will include extending existing runways and constructing new runways. The OMP has submitted an application to the Federal Aviation Administration to use approximately $180 million in Passenger Facility Charges to fund design work, which could begin in late 2009.

Health of the Airlines

While O’Hare undergoes these improvements, a number of major airlines continue to struggle, resulting in decreased capacity, and, in some instances, bankruptcy. Most recently, Aloha Airlines, ATA, Frontier Airlines and Skybus have all filed for bankruptcy, with only Frontier Airlines remaining operational.

The Official Airline Guide annually receives airlines’ June flight capacities. As of data received by April 13th of 2009, airports in the state of Illinois are projected to lose a total of 6.9 percent in capacity in June of 2009, as compared to June of 2008. The decrease in Illinois airport capacity is not related to the airports, but rather reflects airlines in those airports cutting flights. The decrease in capacity is driven by a 9.1 percent decrease in airline capacity at O’Hare and a 0.3 percent reduction in capacity at Midway. For comparison purposes, the capacity reduction in Illinois represents a slightly lower figure than the 7.2 percent national average decline in capacity. Additionally, a number of major airports throughout the country are reporting capacity decreases of between 15 and 25 percent, due to airline service cuts and bankruptcies.

The O'Hare Modernization Program should allow significant future growth in passenger volume during the next decade. Although several airlines have announced service reductions during the past year, the long-term outlook for air service in Chicago is positive.

Olympic Games

Chicago's bid for the 2016 Summer Olympics has significantly increased Chicago's presence in numerous media. Local, national, and international print, radio, and television media have covered the selection process. On April 14th, 2007, the United States Olympic Committee (USOC) selected Chicago as the U.S. applicant city. In 2008, Chicago submitted its completed official bid files. The International Olympic Committee (IOC) Evaluation Commission visited the candidate cities, including Chicago, in April of 2009. The final host city selection will be made by the IOC on October 2, 2009, in Copenhagen, Denmark.

Although we have not estimated the direct impacts of this media attention on the hotel industry in Chicago, local area hoteliers believe it has been a significant positive factor affecting overall hotel demand in the city during the past two years. The Chicago bid indicates that Chicago has secured 55,000 hotel rooms in the Chicago metro area, with no minimum stay requirements, and price-controlled room rates. The Hyatt Regency Chicago is the proposed Olympic Family hotel, according to the Chicago 2016 Bid Book. If Chicago is selected as the host city, this would lead to further positive impacts for the local hotel industry as planners, consultants, and media increase travel to, and awareness of Chicago.

Millennium Park

Millennium Park continues to be one of the most popular tourist attractions in Chicago. The 24.5-acre park opened in July 2004; the park's famous Cloud Gate sculpture was completed in April 2006. This year, several new attractions are planned in the Millennium Park area. To commemorate the Burnham plan of 1909, the city is planning on a new outdoor temporary pavilion, available for viewing between June 19th and October 31st of 2009. An additional sculpture exhibit is on view in the Boeing Galleries, which are two adjacent open spaces map of Millennium Park.

Map of Millennium Park

Source: Millennium Park

The recently opened Nichols Bridgeway connects the Art Institute of Chicago's Modern Wing with Millennium Park. The 620-foot bridge offers views of Lake Michigan, Millennium Park, and buildings in the loop. This new connection will enhance the attractiveness of both Millennium Park and the Chicago Art Institute, while providing an even better tourism package for visitors. These new attractions are expected to boost visitation by keeping Millennium Park new and changing.

Industry survey data from priceline.com supports the importance of Millennium Park as a destination. Every year before the Memorial Day holiday, priceline.com releases the results of a survey of customers booking hotel rooms through its website. The survey indicates which neighborhoods are the top destinations for travelers using priceline.com to search for hotel rooms across the country. The following table shows the top five destinations in the U.S. during the past five years.

Top Five Memorial Day Destinations on priceline.com

Rank	2005	2006	2007	2008	2009
1	Las Vegas Strip	Millennium Park	Millennium Park	NYC Times Square	Las Vegas Strip South
2	NYC Upper Midtown	Las Vegas Strip	Las Vegas Strip	Las Vegas Strip South	NYC Chelsea Area
3	Chicago Michigan Ave.	Chicago Michigan Ave.	NYC Upper Midtown	Millennium Park	NYC Times Square
4	NYC Midtown West	NYC Upper Midtown	Chicago Michigan Ave.	Las Vegas Strip North	Boston Copley Square
5	NYC Upper West Side	NYC Midtown West	NYC Downtown/Soho	Chicago Michigan Ave.	Millennium Park/Grant Park

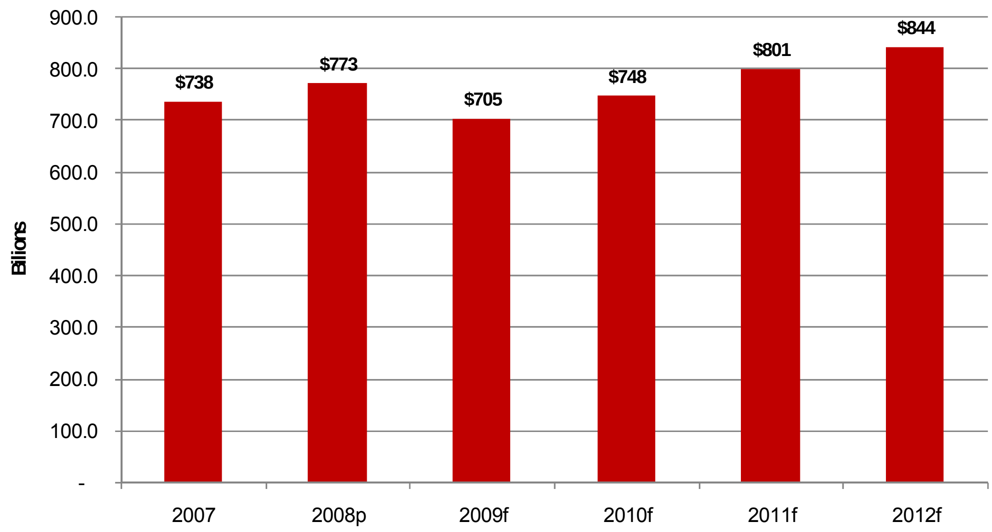
Source: Annual survey by priceline.com

In 2006 and 2007, Millennium Park became the top neighborhood destination in the country for the Memorial Day holiday weekend, based on priceline.com survey data. In 2008, Millennium Park dropped to third place in the rankings. From 2006 through 2008, Millennium Park and Michigan Avenue have both ranked in the top five Memorial Day destinations identified by priceline.com, reflecting Chicago's overall destination appeal. In 2009, Michigan Avenue fell off the list and Millennium Park/Grant Park fell to number five. NYC's Chelsea neighborhood and Boston's Copley Square made the top five in 2009 for the first time.

National Travel Industry Trends

As with prior recessions, during the early 1980's, 1990's, and 2000's, the performance of the travel industry correlates with overall economic conditions. Travel demand and hotel demand are closely related. Therefore, future travel demand forecasts may serve as one indicator for future hotel demand. While travel industry trends differ from region to region, overall national statistics provide an indication of growth or decline. The United States Travel Association tracks passenger traffic and travel expenditures for the country. The following table shows historical, projected, and forecasted travel price indexes, as well as total travel expenditures in the United States.

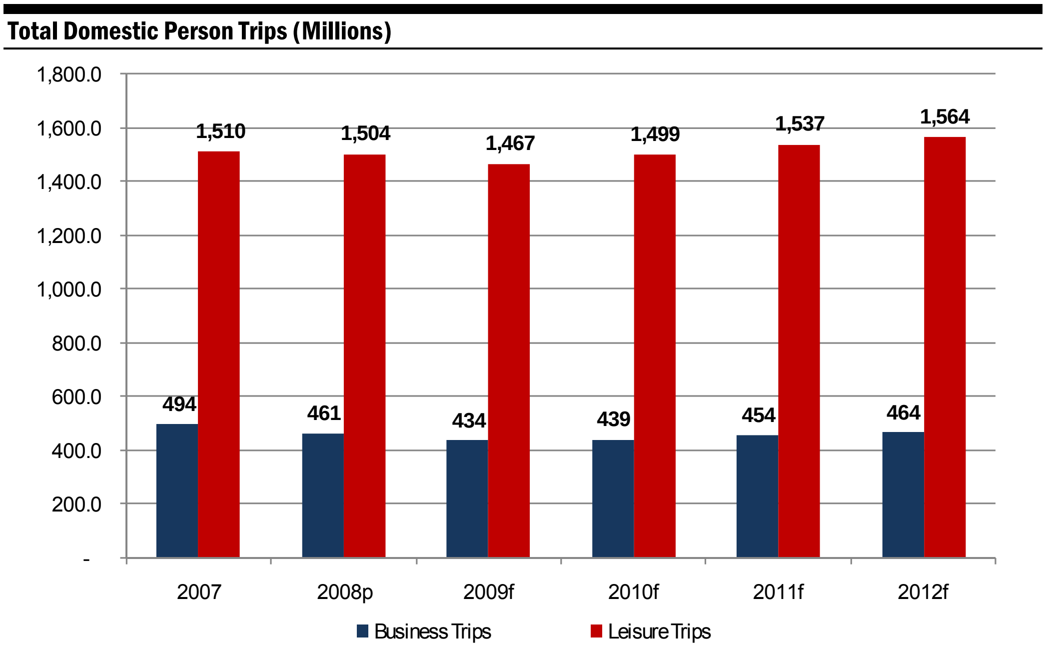
Total Travel Expenditure (2007 through 2012)



Source: U.S. Travel Association ("Annual Travel Forecast")

Data from 2008 shows total travel expenditures of almost $773 billion. The forecast for 2009 shows travel expenditures declining to $705 billion, representing an annual decline of 8 percent. Near-term forecasts indicate resumed growth in travel expenditures in 2010 and beyond. Total travel expenditures are forecasted to recover to above 2008 levels by 2011.

In addition to expenditures, another measure of travel demand is the number of trips people take each year. The U.S. Travel Association tracks two basic categories of trips for leisure and business travel in the country. The following figure shows the number of person trips taken in each of these two categories during the past two years as well as forecasts for 2009 through 2012.



Source: U.S. Travel Association ("Annual Travel Forecast")

Leisure and business travel are both expected to resume modest growth in 2010, with leisure travel rebounding more quickly. Leisure travel is expected to exceed its previous 2007 peak level in 2011. However, business travel is not expected to rebound to its 2007 peak within the projection period shown.

Fortune Ranked Companies

Meeting and convention demand, as well as business travel demand relies heavily on the region's corporate presence. Fortune Magazine tracks the largest companies in each state and city. In 2007 and 2008, 20 companies located in the City of Chicago finished within the Fortune 1000, an increase from the 19 Fortune 1000 in 2006. Harley Davidson and Willis Insurance recently moved their headquarters to Chicago, and Miller Brewing Company, in 2008, moved its headquarters to Chicago.

However, 2009 saw only 17 City of Chicago-based companies land within the Fortune 1000. This was due to the purchase of Wrigley by Marks, and sharp drops in revenue at Tribune and Metal Management that prevented them from placing within the top Fortune 1000 companies.

The following table shows the Fortune 1000 companies located in the Chicago metro area, including suburbs, in 2009.

Fortune 1000 Companies in Chicago Metro Area - 2009

Company	Fortune 1000 Rank	Revenues ($millions)	City
Boeing	34	60,909	Chicago
Walgreen	36	59,034	Deerfield
Sears Holdings	49	46,770	Hoffman Estates
Kraft Foods	53	42,867	Northfield
Motorola	78	30,146	Schaumburg
Abbott Laboratories	80	29,528	Abbott Park
Allstate	81	29,394	Northbrook
McDonald's	107	23,522	Oak Brook
UAL	123	20,194	Chicago
Exelon	134	18,859	Chicago
Illinois Tool Works	148	17,218	Glenview
Navistar International	175	14,724	Warrenville
Integrys Energy Group	185	14,048	Chicago
Sara Lee	199	13,450	Downers Grove
Baxter International	219	12,348	Deerfield
R.R. Donnelley & Sons	233	11,582	Chicago
Aon	307	8,406	Chicago
OfficeMax	313	8,267	Naperville
Fortune Brands	351	7,105	Deerfield
Discover Financial Services	352	7,088	Riverwoods
Smurfit-Stone Container	356	7,042	Chicago
W.W. Grainger	366	6,850	Lake Forest
Anixter International	404	6,137	Glenview
Tenneco	416	5,916	Lake Forest
Northern Trust Corp.	430	5,678	Chicago
Telephone & Data Systems	465	5,092	Chicago
United Stationers	475	4,987	Deerfield
Brunswick	491	4,709	Lake Forest
USG	501	4,608	Chicago
Nalco Holding	536	4,212	Naperville
CF Industries Holdings	563	3,921	Deerfield
Nicor	577	3,777	Naperville
Hospira	597	3,630	Lake Forest
Pactiv	604	3,567	Lake Forest
General Growth Properties	636	3,362	Chicago
Molex	642	3,328	Lisle
Old Republic International	651	3,238	Chicago
Hewitt Associates	653	3,228	Lincolnshire
Unitrin	715	2,820	Chicago
Jones Lang LaSalle	735	2,698	Chicago
CME Group	761	2,561	Chicago
Packaging Corp. of America	812	2,361	Lake Forest
Equity Residential	865	2,149	Chicago
Sauer-Danfoss	879	2,091	Lincolnshire
LKQ	914	1,937	Chicago
Hub Group	944	1,861	Downers Grove
Solo Cup	949	1,847	Highland Park
Tellabs	996	1,729	Naperville
Career Education	1000	1,721	Hoffman Estates

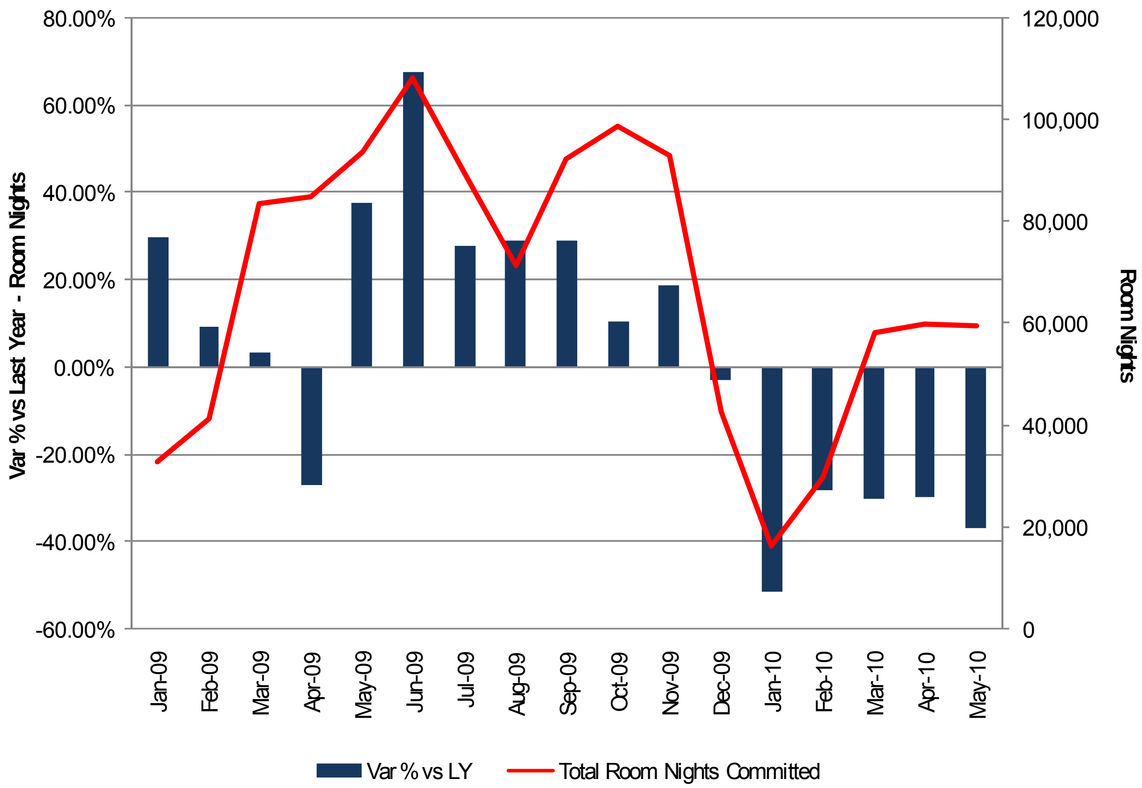
Source: Fortune Magazine

In 2009, there were 49 Fortune 1000 companies in the Chicago metro area, compared to 54 in 2008, 52 in 2007, and 54 in 2009. The drop in 2009 occurred as a number of companies experienced sharp declines in revenues. Nonetheless, the large number of Fortune 1000 companies in the Chicago metro area continues to act as a positive demand factor for Chicago hotels.

Future Booking Demand Data

To better analyze the near-term outlook for the Chicago hotel industry, it is important to look at trends and patterns in the pace of advance room night bookings, and changes from 2008 to 2009 in segmentation, as well as booking channels. One of the most reliable and comprehensive sources of future booking data is Rubicon. Combined with HVS survey data from individual hoteliers, the Rubicon future booking data provides a key insight into the near-term prospects for transient and group room night demand. One indication of how much group room night demand will look in 2010 is the number of group room nights committed in 2009 for events taking place in 2010. The following graph shows the percent change in room nights committed one year in advance, over the same month in the previous year through May 2010.

Pace of Demand: Committed Group Bookings



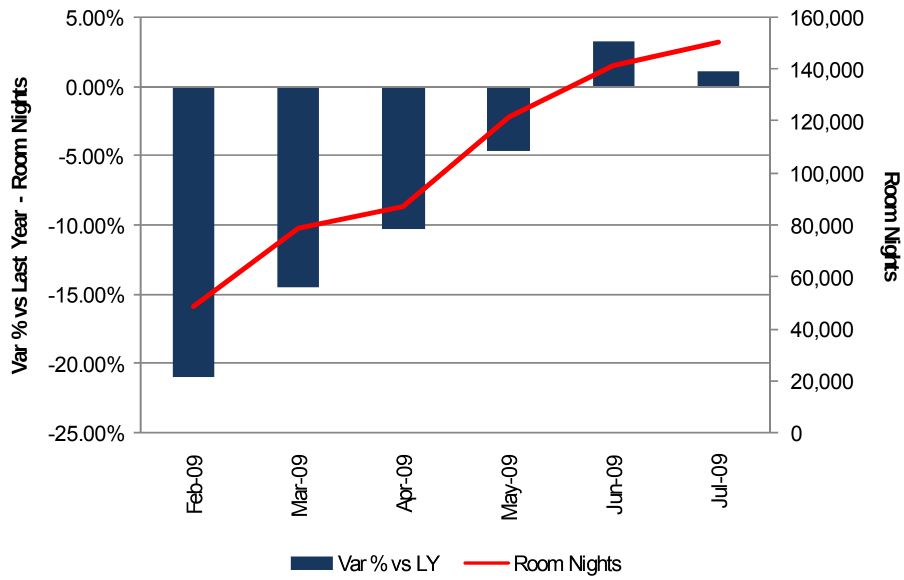
Source: Rubicon©

Unlike, perhaps, other major hotel markets across the United States, the full effects of the recession had not yet been realized in the Chicago market until late 2008, resulting in strong year-in-advance bookings in the group segment through most of 2008 for group events taking place in 2009. Despite the strong commitments for groups made in 2008 for events occurring in 2009, attrition has significantly reduced actual group demand during this period.

Bookings for December of 2009 through May of 2010 show significant declines in committed room nights compared to the previous year. This suggests that meeting planners are not willing to commit to as many rooms in 2010 as they committed to for 2009. This trend is a possible indication that group demand will decline further in 2010. However, this may also reflect meeting planners' desire to operate within shorter booking windows, thus limiting their commitment for next year to protect themselves against attrition penalties.

The following chart illustrates the pace of demand in transient bookings, using room nights booked by the first day of the month prior, instead of the year-in-advance period shown for group bookings. This advance booking period is a more appropriate indicator for transient demand since most individual travelers do not book their travel more than one month in advance. The chart shows the percentage change in transient room nights booked by January 1st of 2009 for the month of February of 2009 compared to transient room nights booked by January 1st for the month February of 2008, and so forth through July of 2009.

Pace of Demand: Transient Bookings

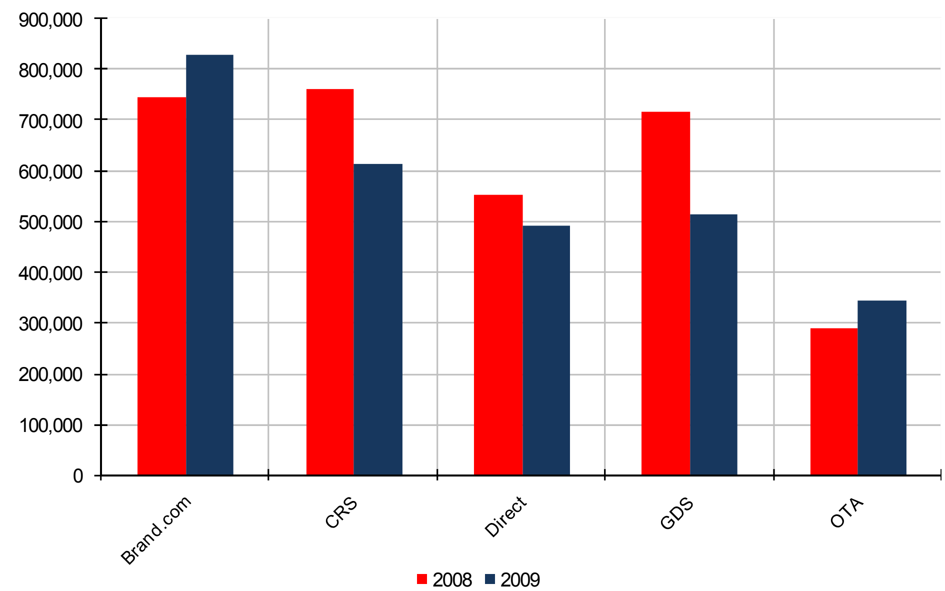


Source: Rubicon©

The preceding chart suggests that transient demand in the Chicago market may resume growth in June of 2009. Although advanced transient bookings declined in each of the months from February through May, compared to the previous year, the declines decelerated each month and finally turned positive for June and July of 2009. This data trend is one positive indicator for demand in the near-term that may partially offset the negative indications pertaining to group booking trends.

The following chart shows the total room nights booked through June of 2010 as of June 1st 2009 compared to booking through June 2009 as of June in 2008, segmented into five major booking channels: CRS (booked through the central reservations office of the hotel company), Brand.com (booked directly on the hotel company's web site), Direct (booked directly with the property), GDS (booked through a global distribution travel agent systems), and OTA (booked through a third party Online Travel Agency).

Booking Channels: 2008 vs. 2009

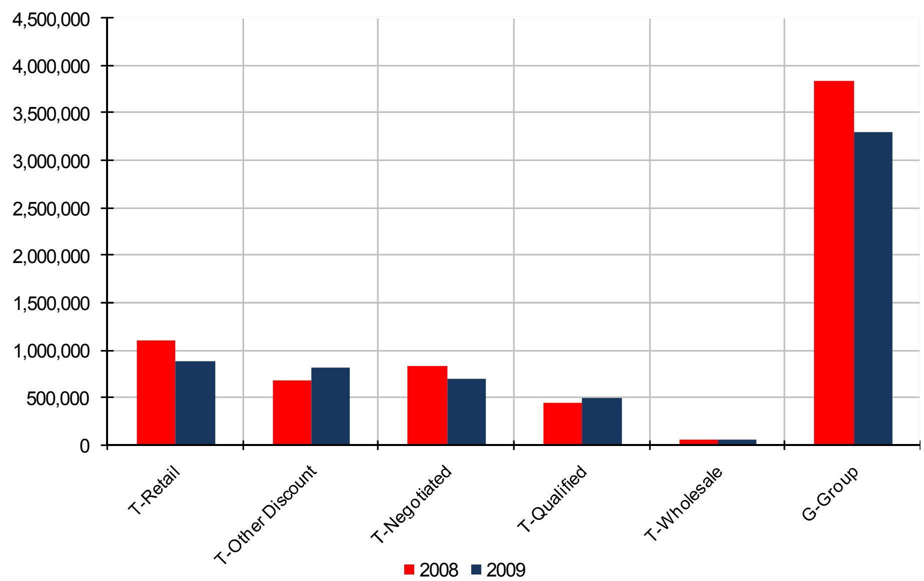


Source: Rubicon©

In 2008, the central reservations office of hotel companies ("CRS") followed by booking directly on the hotel company websites ("Brand.com") were the most widely-used booking channels. These two leading booking channels have been reversed in 2009, with brand websites becoming the most popular channel currently. There have been fewer bookings in 2009 in all other booking channels, as a result of decreased hotel demand in 2009, with the exception of online travel agencies ("OTA"), and brand websites (Brand.com). As happened during the last recession in 2001, travelers became more price-sensitive and increasingly look to book online. Additionally, travelers have become more comfortable and find it easier and more convenient to book online, resulting in increased room nights in the Brand.com segment. The continued strength of bookings in the Brand.com segment indicate that the Chicago hotel industry may have the ability to keep average rate at a higher rate than it did in past recessions, as consumers continue to book through company websites.

The following chart shows the segmentation of total room nights booked through June of 2010 as of June 1st 2009 compared to booking through June 2009 as of June 1st 2008, grouped into six market segments. Transient demand is divided into five segments: retail/rack rate, negotiated (under corporate contracted rates), qualified (affiliation discounts), wholesale, and other discounts (packages, promotions).

Segmentation: 2008 vs. 2009



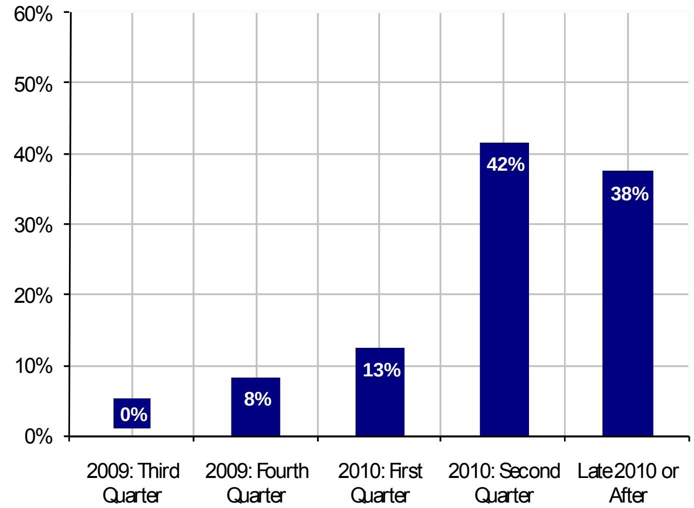
Source: Rubicon©

The group segment represents the largest segment with more than 3.8 million group room nights in 2008 and almost 3.3 million room nights in 2009 according to Chicago hotels that participate with Rubicon. Only two segments experienced increased demand in 2009 over 2008—other discount and qualified. Total committed group bookings have declined 16 percent from 2008 to 2009, while all transient segments totaled declined only five percent from 2008 to 2009, demonstrating that those hotels most reliant on group business may experience lower demand levels than those properties focused primarily on transient business.

Industry Outlook

In May and June of 2009, HVS surveyed hotel managers in Chicago to obtain insights about when they believe the local economy will resume growth. The following figure illustrates when local hotel managers believe economic growth will resume.

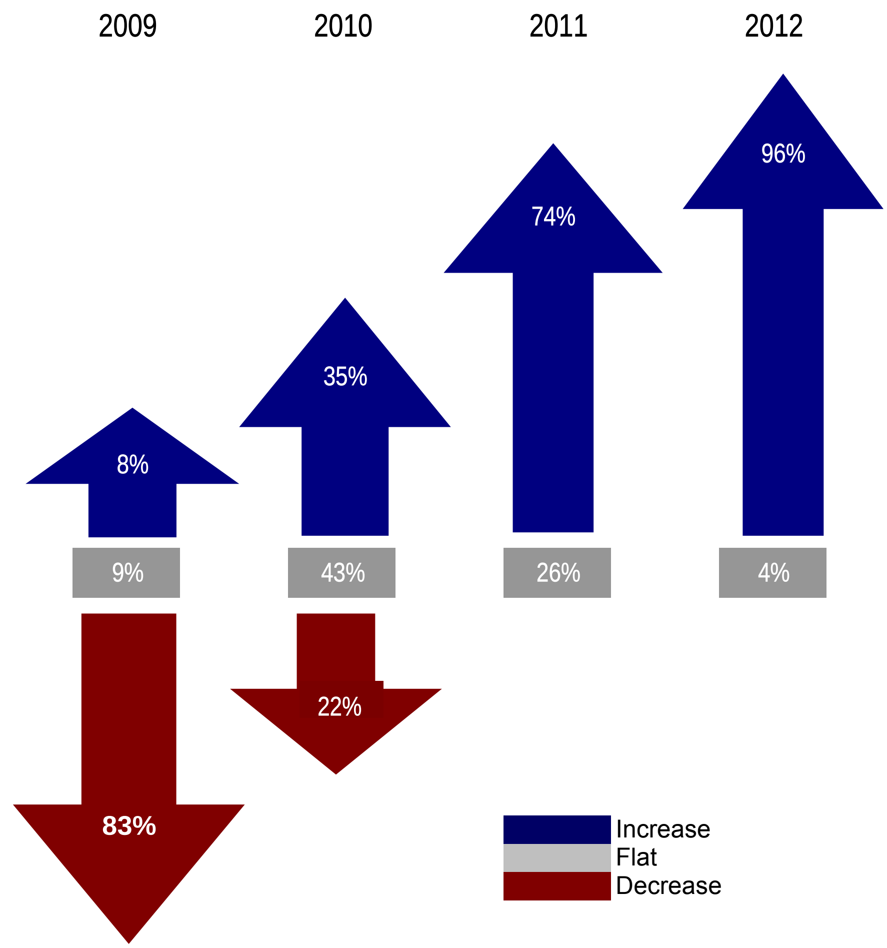
Timing of Local Economic Recovery



Approximately one-fifth of hotel managers believe economic growth will resume in the fourth quarter of 2009 or the first quarter of 2010. The majority of local hoteliers believe economic growth in the Chicago area will not begin until the second quarter of 2010 or later.

The following figure illustrates what percentage of hotel managers believe occupancies will increase, decrease, or stay the same during each of the next four years.

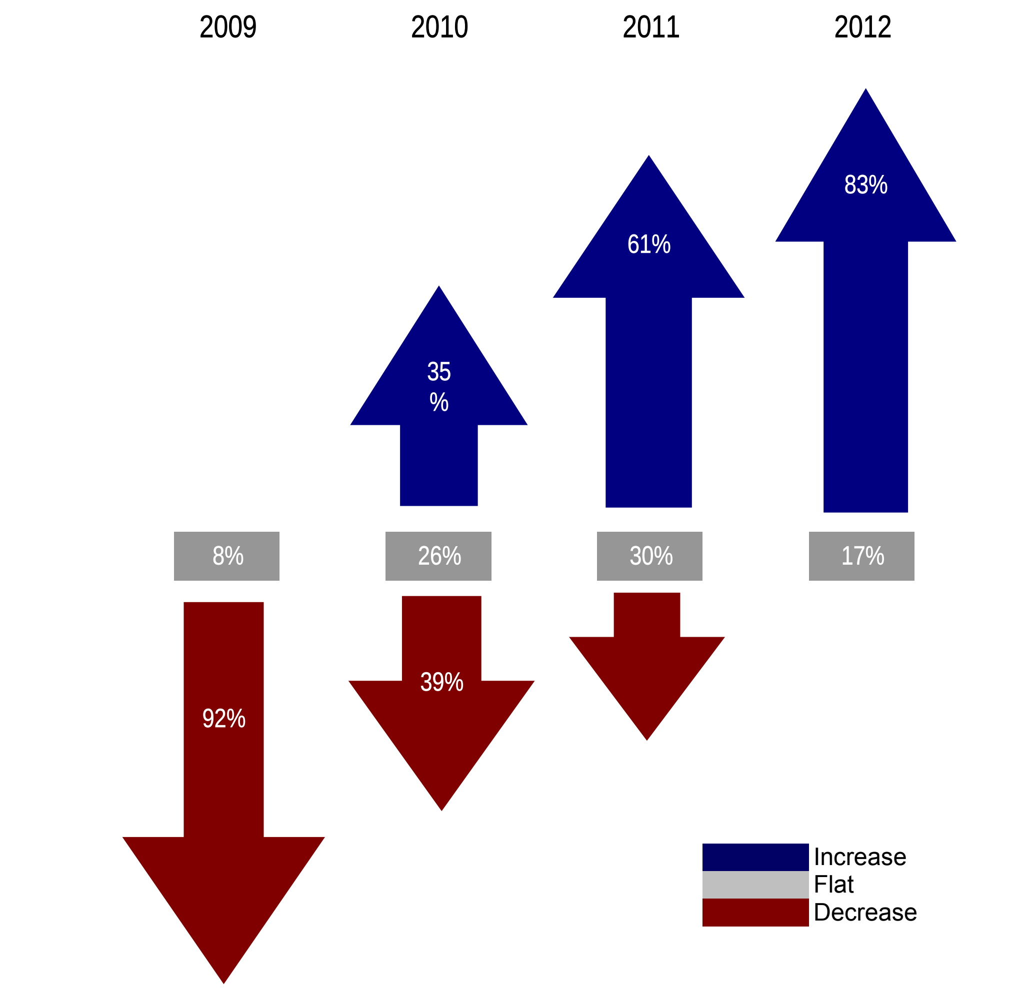
Occupancy Outlook



Consensus from hotel managers indicates expected declines in occupancies for 2009, with only nine percent of managers projecting an increase in 2009 occupancy over 2008. For 2010, managers are more optimistic, although 22 percent still expect decreases in occupancy. A large majority of hotel managers expect occupancies to increase in 2011 and 2012.

The following figure illustrates what percentage of hotel managers believe average daily rates will increase, decrease, or stay the same during each of the next four years.

ADR Outlook

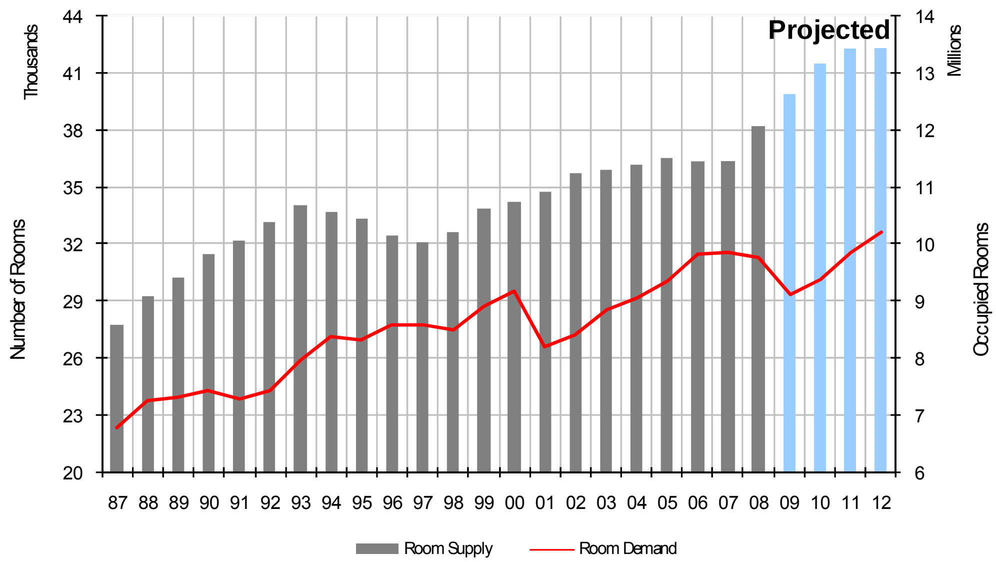


In 2009, approximately 92 percent of hotel managers believe average daily rates will decrease, with no hotel manager expecting an increase in ADR this year. Similar to occupancy, hotel managers are more optimistic about 2010, although 39 percent still expect a year-over-year decrease in average daily rates. In 2011, a majority of hotel managers believe rates will increase, with nearly all hotel managers expecting average daily rate growth in 2012.

Based on the survey findings and additional market research, demand trends are expected to increase after flattening in 2009 and 2010. Supply will continue to increase as several projects currently planned or under construction reach completion by the end of 2011. During the period between year-end 2009 and year-end 2012, HVS projections show annual supply growth rates that range between 0.0 percent and 4.3 percent. In 2010, demand is expected to grow at a slightly slower pace than supply, while in 2011, demand is projected to outpace growth in supply. Therefore, occupancies are likely to drop further in 2010, but increase in 2011 and 2012. This is consistent with survey data that suggests occupancies may not begin increasing again until late 2010 or 2011.

The following chart presents historical trends and our near-term forecast of room supply and demand for the Chicago hotel market through 2012.

Supply and Demand Outlook

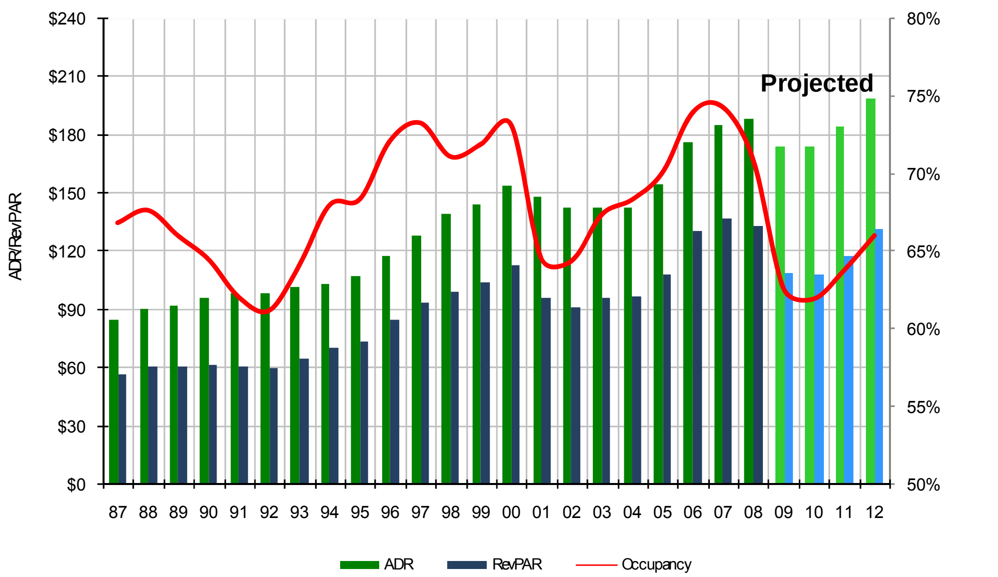


An evaluation of near-term projects indicates that hotel room supply in the city will increase from 38,256 rooms at the end of 2008 to approximately 42,343 by the end of 2012. During the same period, we project demand will increase from about 9.1 million room nights in 2009 to approximately 10.2 million room nights in 2012.

The economic recession will continue to take a toll on the Chicago hotel industry through most of 2009 and planned supply growth in 2010 will keep occupancies relatively low. Some near-term demand indicators and the continued popularity of Chicago's McCormick Place and major league sports teams provide reasons for a moderately positive outlook for the Chicago hotel industry post-economic recovery.

The following chart presents historical trends and our near-term forecast of occupancy, ADR, and RevPAR for the Chicago hotel industry through 2012.

Performance Measures Outlook



After a peak in occupancy in 2007, continued supply growth and significant drops in demand in 2008 and 2009 are projected to lead to lower occupancies through 2010. In 2011 growth in demand is projected to outpace growth in supply. In 2012, ADR is projected to surpass the ADR peak of 2007. Occupancy of 66 percent in 2012, however, is projected to finish below 2007's occupancy of 74 percent. Therefore, RevPAR is expected to top $131 in 2012, slightly below its previous peak of $137 set in 2007.

RevPAR is expected to decrease more than 18 percent in 2009, as occupancies and rates both decline. In 2010, RevPAR is projected to experience a slight decline of one percent, as rates flatten, and occupancy falls one percent, due to an influx of supply. Substantial RevPAR increases are projected in 2011 and 2012 as average daily rates increase and occupancies rebound.

There is considerable uncertainty about the timing of a national economic recovery, and subsequent economic growth. Demand, supply, and performance projections may not be met if any significant shocks to the economy occur or if the anticipated economic recovery does not occur. Therefore, projections are subject to change.

About the Authors

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