JANUARY 2013

DLA PIPER
2013 HOSPITALITY OUTLOOK SURVEY

DLA PIPER

EXECUTIVE SUMMARY

Despite political gridlock in Washington DC, and some concerns about economic growth, an extraordinary number of US hospitality executives expect their industry to perform well in 2013. Almost 84 percent of respondents polled for the DLA Piper Hospitality Outlook Survey described their outlook as "bullish," the highest recorded since 2011 when 88 percent of respondents described themselves as bullish. This year's survey incorporated the views of 110 hospitality executives in 19 states.

Undergirding this year's optimism: Confidence that the broader US economy will continue its steady, albeit modest, growth. Others cite increased growth in business and convention-related travel, as well as projected strength for hotel transactions. Most of the people surveyed expect hotel real estate values to rise at least somewhat. They have a broad expectation that hotel operators will succeed at boosting room rates. And they believe those market conditions have created especially good opportunities for investors buying hotels now.

A few things are tempering executives' enthusiasm, primarily political gridlock in Washington. When the survey was conducted in December, more than half of respondents believed that the "fiscal cliff," if not averted, would be a significant deterrent to deal making in 2013. Even after a deal was reached, many respondents said the deal had failed to decisively solve the country's fiscal problems.

The bullishness is having some interesting effects on executives' views about which hotel assets will perform the best in the future. For example, 83 percent of executives anticipate that hotel operators will raise nightly room rates this year. The expectation of rising room rates could reduce operators' thirst for group bookings at bulk rates, which were a bulwark for hotel owners during the recession. Now two-thirds of respondents expect flat occupancy for groups. And many apparently believe that hotels with calendars packed with group bookings at bargain rates will be potentially less attractive to hotel investors than hotels with more flexibility to raise room rates as demand rises in the coming year or two.

On the other hand, transient bookings are on the upswing and may be the catalyst for hotel operators to raise these rates. Transient bookings specifically may be rising as China prepares to send over 100 million leisure tourists into the international market in 2013. Respondents had the opportunity to share their view on how the US hospitality industry should prepare for the increase of up to 10 million visitors from the country (See Verbatims on p. 3), and a majority of respondents confirmed that some of the key priorities hotel executives should have top of mind is to hire Chinese speaking executives to communicate with guests effectively, and to raise hotel rates.

HIGHLIGHTS OF DLA PIPER'S 2013 HOSPITALITY OUTLOOK SURVEY INCLUDE:

- The percentage of respondents who believe hotel asset values are headed upwards nearly doubled, to 82. But executives remain cautious: 60 percent predict that values will rise only "slightly."
- In a slight drop, 85 percent of respondents believe market conditions have created good buying opportunities for well-capitalized investors, down from 91 percent last year.
- The upscale market remains the most attractive opportunity, say respondents. The midscale market remains their second-most attractive opportunity.

- While private equity is once again seen by most executives as the most active type of hotel investor in 2013, the portion of respondents who insist foreign investors will lead the way has doubled, to 20 percent.
- Commercial lenders will be the most active type of lender, say 43 percent of respondents, up from 34 percent last year.
- Respondents believe Brazil remains the most attractive opportunity for outbound US investors. The future World Cup host received 35 percent of the votes, with China placing second, at 25 percent.
- Spain has replaced Italy as the European country most likely to experience economic problems—43 percent of respondents cite it, while only 16 percent cite Italy, a near-reversal of last year's numbers.
- Among the 16 percent of respondents who describe themselves as "bearish" about the hospitality industry, just over half cited the struggling US economy as the top concern.
- 71 percent of respondents said that political gridlock in Washington, DC remains a chief hurdle facing the recovering industry.

VERBATIMS

Respondents were asked to share their thoughts on the following in an open forum for comment and feedback. The following represent select verbatims received from survey respondents.

***The US has about 5 million hotel rooms and almost no new supply in the construction pipeline. At the same time, China is ramping up to send about 100 million leisure tourists into the international market this year. If the US gets its anticipated share, that will mean an additional 10 million visitors from China alone. What should the US hotel industry to do prepare for this potential influx*?** *Please explain:*

- Do not build new rooms; fill the rooms that already exist. Rather, hire bi-lingual staff that speaks Chinese. The urban affluent Chinese people speak English but the rural less affluent do not speak English. They need to feel welcomed in their native language by staff and printed materials and signs.
- Raise rates. As an industry we run 62 to 63 percent occupancy across the board. There is capacity with existing supply. The additional tourists will create a rate growth opportunity.
- Hire Mandarin speakers!
- Hire and train Chinese-speaking staff. Very few Chinese speak or understand English. Need bi-lingual signs, menus, etc. Educate all personnel in dealing with the Chinese. Be ready for problems due to their unfamiliarity of Western hotel rooms and culture. Learn their needs and desires - They like twin beds, they don't know to put the shower curtain inside the bathtub. These are very new tourists, first time visitors.
- Continue to keep development in check. Simple math: If the Chinese visitors have an average length of stay of 5 nights, the 10 million visitors will raise US hotel occupancy by only about 2.7 occupancy points.
- Let's not overreact here. Nothing from a supply standpoint. There is ample capacity.
- Prepare to raise rates, control demand flow and recoup some for the money we have given to the Chinese.
- Learn how to be sensitive to the cultural and service needs of that customer segment.
- Wait to see what happens with the fiscal cliff as this may impact all economies.
- Upgrade our airports and transportation infrastructure
- Make visiting easy as far as passport entry and easy visas

VERBATIMS

Now that that the fiscal cliff has been averted, what impact will it have on the hotel industry in 2013?

- Neutral: Had it not been averted, the effects may have been significant. By averting the fiscal cliff, we have avoided a potentially significant negative impact, but it also didn't create a positive impact.
- Now we are facing the next debt-ceiling crisis, which could stall the market like it did in mid-2011.
- It has not been averted, just delayed!
- Economic growth will still be slow. Still have some big cost cutting hurdles to get through.
- We still face a significant deficit problem and potential downgrade of US securities. A downgrade and the potential for increased interest rates will likely have a significant impact on hotel capital markets as with real estate markets in general. We remain in very uncertain times, which mean that investment discipline must be maintained.
- First, the fiscal cliff is a non-event designed to scare people. The problem, however, has not been averted. Only a Band-Aid has been applied to slow the bleeding.

Q1. HOW WOULD YOU DESCRIBE YOUR 12-MONTH OUTLOOK FOR THE US HOSPITALITY INDUSTRY?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Bullish	92	83.6%	
Bearish	18	16.4%	
Total Responses	110		**20% 40% 60% 80% 100%**

- For the fourth consecutive year, a majority of respondents (84 percent) describe their 12-month outlook for the US hospitality industry as "bullish."
- This is up from 80 percent in 2012, but still well off the Survey's record-high of 88 percent set in 2011.
- In 2009, only 5 percent of respondents described their outlook as bullish, following a recession that created a challenging marketplace.

Q2. WHAT IS THE PRIMARY REASON FOR YOUR CONFIDENCE?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Expected growth of US economy	30	32.6%	
Increased business travel and conventions	23	25.0%	
Increased international tourists	8	8.7%	
Foreign investment in the US market	5	5.4%	
Increased lending by banks following the recession	5	5.4%	
Projected strength for hotel transactions in 2013	21	22.8%	
Total Responses	92		**20% 40% 60% 80% 100%**

- On the heels of a rebounding US economy, the majority of bullish respondents (33 percent) attribute their confidence to an expected growth of the US economy in 2013.
- Bullish sentiment was also attributed to increased business travel and conventions anticipated in 2013 (25 percent) and projected strength for hotel transactions in the year ahead (23 percent). In 2012, 31 percent of respondents attributed their bullishness to an uptick in business travel.

Note: This question was only made available to those respondents who described their outlook as "bullish."

Q3. WHAT IS THE PRIMARY REASON FOR YOUR LACK OF CONFIDENCE?							
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**				
Struggling US economy/concerns over a double dip	9	52.9%					
Fear of fiscal cliff repercussions	3	17.6%					
Ongoing European debt crisis	2	11.8%					
Lingering inability to increase rates	1	5.9%					
Volatility in financial markets	2	11.8%					
Total Responses	17		**20%**	**40%**	**60%**	**80%**	**100%**

- For the fifth consecutive year since DLA Piper has launched this Survey, the struggling US economy (53 percent) remained the top concern of "bearish" respondents. In 2012, 74 percent of respondents attributed their bearish sentiment to the struggling US economy.
- Given the uncertainty of the fiscal cliff (during the time when this survey was originally distributed), 18 percent of respondents referenced their lack of confidence in the US hospitality industry due to potential fiscal cliff repercussions.

Note: This question was only made available to those respondents who described their outlook as "bearish."

Q4. THE POLITICAL GRIDLOCK IN WASHINGTON, DC REMAINS A CHIEF HURDLE FACING THE RECOVERING HOSPITALITY INDUSTRY IN 2013. AGREE OR DISAGREE?							
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**				
Agree	37	38.5%					
Somewhat Agree	36	37.5%					
Neutral	8	8.3%					
Somewhat Disagree	7	7.3%					
Disagree	8	8.3%					
Total Responses	96		**20%**	**40%**	**60%**	**80%**	**100%**

- While a majority of respondents are optimistic about the outlook for the 2013 hospitality industry, the tense situation in Washington and its possible effects on the hospitality industry remain concerns.
- Similar to 2012, despite the bullish sentiment reported in Question No. 1, a majority of respondents (76 percent) either agree or somewhat agree that political gridlock in Washington, DC remains a chief threat facing the recovering hospitality industry in the year ahead.

Q5. IF THE FISCAL CLIFF IS NOT AVERTED, THIS WILL BE A SIGNIFICANT DETERRENT ON DEAL ACTIVITY WITHIN THE HOTEL SECTOR OVER THE NEXT 12 MONTHS. AGREE OR DISAGREE?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Agree	26	27.4%	
Somewhat agree	32	33.7%	
Neutral	18	18.9%	
Somewhat disagree	9	9.5%	
Disagree	10	10.5%	
Total Responses	95		20% 40% 60% 80% 100%

- Almost a quarter of respondents, 23 percent, cite projected strength for hotel transactions as the reason for their bullishness. However, when addressing a question about the fiscal cliff, 61 percent of respondents either agreed or somewhat agreed that the fiscal cliff, if reached, would have been a significant deterrent on deal activity within the hotel sector over the next 12 months.
- This feedback is parallel to that given about political gridlock in Washington DC. The majority of respondents (76 percent) report being concerned that the political gridlock facing DC could impact the recovering hospitality industry.

Note: This question was provided before a fiscal cliff deal had been made. A follow up question was provided to respondents after the cliff had been averted.

Q6. WHERE DO YOU THINK HOTEL ASSET VALUES ARE HEADED DURING THE NEXT 12 MONTHS?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Up	21	21.9%	
Up slightly	58	60.4%	
No significant change	17	17.7%	
Down slightly	0	0.0%	
Down	0	0.0%	
Total Responses	96		20% 40% 60% 80% 100%

According to a number of industry reports on the US hospitality industry, pricing of US hotel assets is rising and gaining momentum.

- Respondents have witnessed this trend, as well. 82 percent of respondents expect hotel asset values to trend upward or slightly upward in 2013, compared to 47 percent of respondents in 2012 who noted that they expected hotel assets to rise in the year ahead.
- Only 18 percent of respondents believe there will be no significant change to hotel asset values in the year ahead, which is drastically lower than the 51 percent of respondents from the 2012 Survey who predicted no significant, imminent change in asset values.

Q7. WHICH SECTOR OF THE HOSPITALITY INDUSTRY REPRESENTS THE MOST ATTRACTIVE OPPORTUNITY FOR INVESTORS IN THE NEXT 12 MONTHS?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
Economy/budget	3	3.1%	
Midscale	30	31.3%	
Upscale	45	46.9%	
Luxury	8	8.3%	
Resorts	7	7.3%	
Mixed-use/branded residential	3	3.1%	
Total Responses	96		20% 40% 60% 80% 100%

- For the fourth consecutive year, respondents rank the upscale sector as the most attractive investment opportunity (47 percent).
- Similar to 2012, this is followed by the midscale (31 percent) and luxury (8 percent) sectors.

Q8. FOR WELL-CAPITALIZED INVESTORS, DO YOU THINK CURRENT MARKET CONDITIONS HAVE NOW CREATED GOOD BUYING OPPORTUNITIES?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
Yes	82	85.4%	
No	14	14.6%	
Total Responses	96		20% 40% 60% 80% 100%

- 85 percent of respondents believe that market conditions have created good buying opportunities for well capitalized investors. That is down slightly from 91 percent in 2012.

Q9. ACCORDING TO RECENT DATA, COMMITTED OCCUPANCY FOR THE GROUP SEGMENT, A BLOCK OF HOTEL ROOMS RESERVED FOR EVENTS AND CONVENTIONS, IS FLAT WHILE THE TRANSIENT SEGMENT, INDIVIDUAL BUSINESS AND LEISURE TRAVELERS, IS THE DRIVING FORCE BEHIND THE RISE IN OCCUPANCY AND ADR. IS THIS TREND LIKELY TO HAVE AN IMPACT ON INVESTMENT DECISION MAKING IN 2013?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
Yes	66	68.8%	
No	30	31.3%	
Total Responses	96		20% 40% 60% 80% 100%

- In light of the fact that transient hotel business has been outpacing that of the group segment, a majority of respondents (69 percent) believe that investors will be targeting hotels that are more focused on the transient business.

- This appears likely because hotels that are group oriented may not benefit from any rate increase opportunities over the next few years.

Q10. WITH THE DOMESTIC US HOTEL INDUSTRY ON THE BRINK OF A WIDESPREAD RECOVERY, DO YOU ANTICIPATE HOTEL OPERATORS WILL RAISE THEIR RATES IN 2013?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
Yes	79	82.3%	
No	17	17.7%	
Total Responses	96		**20% 40% 60% 80% 100%**

- Given the predictions that the US economy will improve in the year ahead and that transient business will be on the upswing, a majority of respondents (82 percent) anticipate that hotel operators will raise their rates in 2013.

Q11. WHAT TYPES OF INVESTMENT DO YOU EXPECT TO BE MOST ACTIVE IN THE US HOSPITALITY INDUSTRY IN THE YEAR AHEAD?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
Foreign investors	19	20.2%	
Insurance companies	0	0.0%	
Pension funds	6	6.4%	
Private equity	58	61.7%	
REITs	11	11.7%	
Other (please specify)	1		
Total Responses	94		**20% 40% 60% 80% 100%**

- The majority of respondents (62 percent) expect private equity investors to be the most active in the US hospitality industry in 2013, down from 76 percent in 2012.
- Foreign investors still have faith in the US economy and US real estate market and consider it a safe place for investments. To that end, 20 percent of respondents expect foreign investors to be the most active in the US hospitality industry in 2013. This is up significantly from 2012, when 7 percent of respondents believed foreign investors to be the most active.
- 12 percent of respondents expect REIT investors to be the most active in the year ahead. That's down slightly from 13 percent in 2012, and far less than the 50 percent who expressed this belief in 2011.

Q12. WHAT TYPES OF LENDERS DO YOU EXPECT TO BE THE MOST ACTIVE IN THE US HOSPITALITY INDUSTRY IN THE COMING YEAR?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Commercial banks	39	43.3%	
Hedge funds	10	11.1%	
Investment banks	24	26.7%	
Mutual insurance/assurance companies	10	11.1%	
Pension funds	7	7.8%	
Other (please specify)	5		
Total Responses	90		20% 40% 60% 80% 100%

- For the fourth consecutive year, respondents expect commercial banks (43 percent) and investment banks (27 percent) to be the most active lenders in the US hospitality industry in the coming year.
- Notably, respondents are split about whether mutual insurance/assurance companies (11 percent) or hedge funds (11 percent) will be the most active lenders in 2013.

Q13. WHICH REGION REPRESENTS THE MOST ATTRACTIVE OPPORTUNITY FOR OUTBOUND US INVESTORS IN THE NEXT 12 MONTHS?			
RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Brazil	32	34.8%	
China	23	25.0%	
Eastern Europe	3	3.3%	
India	12	13.0%	
Mexico	4	4.3%	
Middle East	1	1.1%	
Russia	1	1.1%	
Western Europe	16	17.4%	
Total Responses	92		20% 40% 60% 80% 100%

- With the World Cup and Olympics on the horizon, a majority of respondents (35 percent) believe that Brazil represents the most attractive opportunity for outbound US investors in the next 12 months.
- Surprisingly, for the first time in five years, Western Europe pushed out India as the third most attractive opportunity for outbound US investors. Since 2009, Brazil, China and India, respectively, remained the three most attractive markets for US investors, according to respondents.

Q14. IN THE EUROZONE, WHICH OF THE FOLLOWING COUNTRY'S SOLVENCY CONCERNS YOU THE MOST?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
France	11	12.1%	
Germany	7	7.7%	
Greece	19	20.9%	
Ireland	1	1.1%	
Italy	14	15.4%	
Portugal	0	0.0%	
Spain	39	42.9%	
Total Responses	91		**20% 40% 60% 80% 100%**

- Respondents are concerned about the solvency issues of several Eurozone nations, but they are most concerned about Spain (43 percent), which has become the latest epicenter of the Eurozone financial crisis. This follows a report from economists at Societe Generale SA (GLE), which shows that Spain's budget deficit exceeded 9 percent in 2012. It also follows a separate forecast from the International Monetary Fund showing that total debt for Spain will reach 97 percent of gross domestic product this year.

Q15. BETWEEN THE US AND WESTERN EUROPE, WHICH REGION'S HOSPITALITY INDUSTRY WILL BE STRONGER IN 2013?			
RESPONSES	**COUNT**	**%**	**PERCENTAGE OF TOTAL RESPONDENTS**
United States	87	93.5%	
Western Europe	6	6.5%	
Other (please specify)	1		
Total Responses	93		**20% 40% 60% 80% 100%**

- With the Eurozone continuing to face a variety of solvency issues, 94 percent of respondents believe that the hospitality industry will be significantly stronger in the US than in Western Europe in 2012. This is up slightly from 2012, when 91 percent of respondents said they believed the U.S. hospitality industry would be significantly stronger than that of Western Europe.

METHODOLOGY

In December of 2012, DLA Piper distributed a survey via email to top executives within the hospitality industry, including CEOs, COOs, CFOs and other senior executives, which was completed by 110 respondents.

Question No. 2 was only made available to those respondents who described themselves as “bullish” in Question No. 1.

Question No. 3 was only made available to those respondents who described themselves as “bearish” in Question No. 1.

The verbatim question relating to the fiscal cliff was only made available after a fiscal cliff deal had been made.

Due to rounding, all percentages used in all questions may not add up to 100 percent.

CONTACTS

For a copy of the complete results for DLA Piper's 2013 Hospitality Outlook Survey, please visit www.dlapiper.com and search "Hospitality and Leisure" or contact one of the following:

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