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July 27, 2011

INVESTOR EYE CANDY

Hotels are sexy again. Two years ago, a **JW Marriott** in New Orleans sold for $60M. This year, $94M. And less than a year ago, the **Best Western Tuscan Inn** in San Francisco was purchased for $30M, only to be sold again for $53M. What's **luring investors**? Hospitality gurus gave us the lowdown at *Bisnow*'s **New York Hotel Investment Summit** this morning at The Roosevelt.

"Hotels are more than just **bricks and mortar**," LW Hospitality Advisors CEO **Dan Lesser** told the crowd of **325**. Investors love the **minute-to-minute repricing** and yield management, compared to other sectors in which the only fluctuation is the **cost of capital**.

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The primary markets have seen a real turnaround, price appreciation, and **RevPAR growth**, says Starwood Hotels & Resorts Worldwide VP **Mark Purcell**. Thank **cost containment measures** that owners and management have taken during the downturn (now pillows only get *junior* mints). But insurance and energy prices are still a major concern.

REITs will continue to be active, but **private equity**'s making a comeback, says Morgans Hotel Group VP of development **Richard Russo**, who expects more assets to come to market. However, REITs are **flush with cash**—some are able to close all cash in as few as **10 days**. Not a REIT? Come in with plenty of capital or financing in place early. Bottom line: if you're a serious player, you better have **cash available**, the panelists warn. We'll also see opportunities for **lifestyle brands** to consolidate. "It's easy to build one [lifestyle] hotel, but after the **initial buzz wears off**, you need a strong company behind you," he says.

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Major metros aren't getting all the love, according to PMZ Realty Capital managing partner **Michael Sonnabend**—capital's readily available for the big cities to small towns and full-service to limited concepts. The one thing these deals all have in common: **experienced borrowers**. So lifestyle brands, you're not as lucky—financers want a **track record** (raising your own capital may be more successful). The biggest market change: **CMBS** as the largest new source of money. "It's spreading to secondary markets with solid deals and reasonable rates," he says. But Dan warns that some CMBS lenders are concerned with the **government debt situation**, with the Aug. 2 deadline causing a **little fear**.

Greenberg Traurig New York real estate chair **Stephen Rabinowitz**, who moderated, with the panelists. Financing is more difficult on the **development** side, but deals are getting done in major markets—the availability to finance new construction is very limited, Michael says. There's more talk than development, Dan adds—you hear of 50 in New York City, but we're lucky if **10** of those get done. But the country is littered with old hotels **ripe for demolition** (we can suggest a few from our travels), so expect to see some more **wrecking balls**.

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What about 2011's biggest catchphrase: **distress**? Depends on if the distress is in **operations** or the **capital stack** overlaying the asset, Dan says. But one thing's for sure: if lenders own them, they want to get **rid of them**, and *quickly*. "Lenders want to know how fast you get NOI up so they can get out of there versus a three-year time frame," Mark says.

Fundamentals and investors' **hunger for yield** are driving plenty of deals, according to RLJ Lodging Trust VP of acquisitions **Jeffrey Dauray**, who kicked off the dealmaking panel. Fueling pricing: the pressure to get **abundant capital deployed** and **limited opportunities**. He expects more **trophies in gateway cities** to come to market the second half of the year, and we're in the early stages of a **portfolio-acquisition wave**.

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Allied Advisors is one firm benefiting from the frothy market—senior managing director **Richard Rudd** tells us that his firm has done as many transactions by dollar volume year-to-date as it did **all of last year**. "We predict **doubling** for 2011," he says. Buyers are stabilizing properties and exercising more **leverage discipline**, sticking to about **65%**.

If you look at NYC's hotel sales this year, **all but three** involved REITs, points out Denihan EVP of acquisitions & development **Ellen Brown**, whose firm recently sold interest in six Manhattan assets to **Pebblebrook Realty Trust**. Why a JV? "If you can't beat them, **join them** in someway," she urges. As lenders work through portfolios of loans and you know the **day of reckoning** is near, you should be able to find partners.

Question:

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Though it's hard to compete with REITs on hotel deals, HEI Hotels & Resorts found a sweet spot—**assets with turnaround needs**. REITs are **less comfortable** with tackling these types of assets, says SVP of development **Russ Urban**. Distress is motivating sellers today, but more activity in the next 12 to 24 months will be provoked by **capital and funds** versus operational distress.

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Arent Fox partner **Richard Brand**, who moderated, with the panelists. There's not enough inherent need for **new construction**, and a **sheer lack of demand growth** will keep development at bay. "Financing doesn't have the best terms," Russ says. But what's refreshing is the financing available for properties that need turning around, Ellen says—her firm is focusing on **deep renovations** versus new development. But what about New York specifically? Stayed tuned for **part two** tomorrow.

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