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Q3 2019 US Lodging Market Update

The near-term lodging outlook appears choppy as prognosticators have downgraded projected 2020 national RevPAR growth.

By **Daniel Lesser** | October 25, 2019



(<https://images.globest.com/contrib/content/uploads/sites/304/2019/10/lesser-resized.png>) **Daniel Lesser**

While the U.S. continues to be in the midst of its longest uninterrupted economic expansion in modern history, slowing growth metrics along with abundant geopolitical uncertainties are heightening perceived risk of impending recession. Concerns include:

- U.S. GDP growth is decelerating and during the near-term increases are anticipated to remain modest;
- The Conference Board's consumer confidence index fell to 125.1 in September, down from a revised August 2019 reading of 134.2;
- Trade with Canada and Mexico falls into the same uncertainty now gripping U.S. relations with China and Europe. A failure of Congress to ratify a new NAFTA deal which will govern trade relations with these two neighboring countries is a warning sign that illustrates how political volatility could drag down the U.S. economy even if its fundamentals remain strong;
- The Federal Reserve Bank of New York's recession probability indicator, which gauges the likelihood of a recession within the coming 12 months, rose steeply from around 10 percent at the beginning of 2019 to 37.9 percent in August;
- An inverted interest rate yield curve has endured for several months, a phenomenon that has signaled each U.S. economic recession since 1950;
- Ultra-low interest rates continue to trend downwards. While this is a positive for borrowers, it is also raising speculation that America is destined for negative yields like where Japan and much of Europe have been stuck for some time;
- Washington DC is currently in an impeachment frenzy;
- Unknown effects of Brexit which depend on whether the UK leaves with a withdrawal agreement, or before an agreement is ratified ("no-deal" Brexit);
- In response to a proposed extradition bill, which included an agreement with mainland China, since June, Hong Kong has been subject to mass demonstrations with continuous violent clashes and rioting;
- The Middle East is currently more combustible than ever. Conflict(s) resulting in global ramifications could break out in various cities/countries for a multitude of reasons;

Despite daily warnings of possible economic fragility, jobs creation statistics remain relatively steady and personal incomes continue to grow, both of which could sustain the financial system during whatever rough patches may be encountered.

Not everyone believes a recession is imminent, and contrarians can point to other metrics that paint a much sunnier picture. Either way, the prevailing view seems to be that when the next recession hits, it will be less severe than the last one.

Through this past August the U.S. hotel industry's expansion cycle reached 114 months, as hotel revenue per available room (RevPAR) declined year over year only two months during this period, namely during August 2018 and in June 2019. Generally, national hotel supply and demand growth are in equilibrium resulting in relatively flat occupancy levels and lackluster RevPAR growth stemming from average daily rate increases barely equal to inflation (and decelerating).

America's hotel sector has been operating at peak levels for the past three years as an expanding economy has readily absorbed accelerated supply growth in most markets. Notwithstanding rising salary and wage rates and slowing revenue growth, operators have controlled costs sufficiently to achieve GOP margins at their highest levels since the 1960s. With everything said, the near-term lodging outlook appears choppy as prognosticators have downgraded projected 2020 national RevPAR growth.

The LW Hospitality Advisors (LWHA) Q3 2019 Major US Hotel Sales Survey includes 41 single asset sale transactions over \$10 million, none of which are part of a portfolio. These transactions totaled \$3.725 billion and included approximately 13,100 hotel rooms with an average sale price per room of \$283,000. By comparison, the LWHA Q3 2018 Major U.S. Hotel Sales Survey identified 57 transactions totaling roughly \$6.4 billion including 15,300 hotel rooms with an average sale price per room of nearly \$419,000. With more than 28 percent fewer trades and a 42 percent decline in total sales dollar volume during Q3 2019, the U.S. hotel transaction market has clearly slowed down when compared to Q3 2018 along with a growing disconnect between seller prices and buyers' bids.

Notable observations from the LWHA Q3 2019 Major U.S. Hotel Sales Survey include:

- Twelve or roughly 30 percent of the total number of Q3 2019 sale transactions occurred in two states. With seven Q3 2019 hotel sales, Florida

continues to be the most active transaction market followed by five trades in California;

- NYC continues to experience a challenging environment for hotel investment as only one sale occurred during Q3 2019 subsequent to zero during Q2 2019;
- Ten of the 42, or almost a quarter of Q3 trades, were for greater than \$100 million each. Six of the Q3 trades were between \$100 and \$200 million and two of the Q3 trades were between \$200 and \$400 million;
- Premier Group WLL based in Bahrain acquired the 215 room Four Seasons Hotel One Dalton Street, Boston for \$268 million, or \$1.250 million per unit from Carpenter & Company, Inc. who recently developed the property with a 61-story mirrored glass tower that separately includes a 160 Four Seasons Private Residences;
- Blackstone purchased the 1,260 room Hyatt Regency Atlanta for \$355 million or \$282,000 per unit from Hyatt Hotels Corporation who will continue to operate the facility. Opened in 1967, the Hyatt Regency Atlanta was designed by internationally acclaimed architect John C. Portman, Jr. and was the first contemporary atrium-style hotel ever constructed;
- Two Q3 trades occurred above \$500 million each. Caesars Entertainment Corporation (Caesars) sold the 2,548-unit Rio All-Suites Hotel & Casino in Las Vegas to Imperial Companies for \$516.3 million, or \$203,000 per unit. Caesars will continue to operate the property pursuant to a lease for a minimum of two years at \$45 million in annual rent. The transaction also provides the buyer an option to pay Caesars an additional \$7 million for the extension of the lease under similar terms for a third year. Caesars reportedly will retain its rewards customers and the hosting rights to the annual the World Series of Poker. Also, a joint venture between Trinity Real Estate Investments LLC and Elliott Management Corporation acquired the 950 room JW Marriott Phoenix Desert Ridge Resort & Spa for \$602 million, or \$634,000 per unit;
- Suffolk University's acquisition of the Ames Boston Hotel highlights several trends: One, universities are challenged to obtain adequate land and student

housing, particularly in urban locations. Two, development sites in urban gateway markets in the U.S. are trading at a premium. Three, Investors and real estate users have become more creative, and are willing to pay up in order to meet their objectives, and four, supply of hotel rooms does not always grow. Fluctuating markets often result in changing highest and best property uses culminating in lodging facilities being converted or demolished to make way for alternative income producing opportunities.

- GIC Private Limited, formerly known as Government of Singapore Investment Corporation entering into a joint venture with Summit Hotel Properties to acquire the 88-guestroom Hampton Inn & Suites in Silverthorne, CO is intriguing. An overseas sovereign wealth fund investing 49 percent of a \$25.5 million capitalization in a Rocky Mountain town is illustrative of global capital chasing yield by seeking opportunities in a relatively small sized deal situated in a rural resort area;
- Sophisticated hotel centric investors continue to execute capital recycling strategies within the lodging sector. Entities that are active purchasers and sellers of hotels include:

1. Ashford Hospitality Trust
2. Blackstone
3. Brookfield Property Partners L.P.
4. Clearview Hotel Capital
5. Columbia Sussex Corporation
6. Elliott Management Corporation
7. GAW Capital Partners
8. Highgate
9. Host Hotels & Resorts Inc.
10. Hyatt Hotels Corporation
11. Noble Investment Group
12. Park Hotels & Resorts
13. Peachtree Hotel Group
14. Pebblebrook Hotel Trust

15. RLH Corporation
16. Starwood Capital Group
17. Summit Hotel Properties
18. Trinity Real Estate Investments
19. Wheelock Street Capital
20. White Lodging

Additional commentary on the U.S. hotel market based upon my observations:

- With enormous amounts of equity from all over the globe chasing yield at this stage in the cycle, the hotel sale transaction market remains relatively robust. Savvy investors continue to see compelling rationales to capitalize on opportunities to obtain irreplaceable locations and buildings, evidenced in part by the reported frenzied bidding amongst more than a dozen investor groups for Anbang Insurance Group's 15 property \$5.8 billion luxury hotel portfolio;
- M&A activity in the sector also remains robust as demonstrated by the recently announced merger of two significant independent hotel operators, namely Aimbridge Hospitality and Interstate Hotels & Resorts, which will result in a combined management portfolio of more than 1,400 hotel properties in 49 states and 20 countries. Another example is Park Hotels & Resorts Inc.'s closing its \$2.5 billion acquisition of Chesapeake Lodging Trust.
- Secondary and/or tertiary cities such as Charlotte, Houston, Salt Lake City, and Tampa continue to evolve into attractive markets for investors challenged to identify quality hospitality investment opportunities in high priced first-tier cities such as Boston, Los Angeles Miami, New York, and San Francisco;
- The sector continues to be flush with CMBS and other debt products which support lower all in borrowing costs and often provide a compelling thesis to refinance owned assets and return equity, versus placing them on the market for sale;

- A continued strong U.S. dollar and political factors are contributing to weakened inbound international travel trends which places negative pressure on hotel performance in several gateway markets including New York, San Francisco and Washington DC;
- Operating expense models have changed across the industry, particularly in union markets. A higher proportion of costs are now fixed rather than variable with occupancy, particularly labor, as government and/or union work rules have created challenges to flexing schedules;
- Several markets have passed legislation imposing stricter restrictions on alternative accommodations such as AirBNB and VRBO which should drive incremental compression hotel room nights;
- The Hotel Advertising Transparency Act of 2019, a bipartisan bill was recently introduced in the U.S. House of Representatives that if ratified would prohibit resort/amenity/facility and other fees from being introduced to travelers late in the booking process. Fees have become increasingly popular at full service and resort properties, and as ADR growth has slowed these high margin revenues enhance net operating income while remaining competitive in terms of the advertised room rate. Added disclosure and full pricing transparency should create a more level playing field, but certain hotels' relative value proposition could be negatively impacted in the eyes of price-sensitive consumers.

Although perceived risks to a positive outlook are evolving, the U.S. economy remains resilient, though risks to a positive outlook are mounting. Economic and geopolitical uncertainty is negatively impacting cross-border transaction volumes and in the near-term broader growth uncertainties will remain a headwind for global investor sentiment. History has proven that a late cycle mind set positions markets to be more intensified towards signs of difficulties, and that such sentiments can “talk the market down” and turn into a self-fulfilling prophecy and induce a recession.

Everything in life is relative. Consider that during the Great Recession of a decade ago, on average the U.S. lodging industry produced profits, albeit lower than prior years. During the economic recession of the early 1990's, coupled with the negative effects of the Persian Gulf War, the U.S. hotel industry was largely unprofitable. Although growth of current record high lodging fundamentals may be slowing, nonetheless future growth is anticipated to endure. Due in part to the lack of long-term credit worthy tenancies and that with continuous resetting of room rates, hotels are fundamentally long-term investments. At any point in a cycle, shrewd lodging investors that pay market prices predicated upon underwriting (not necessarily holding) a minimum ten-year projection period tend to realize healthy returns.

SELECT MAJOR U.S. HOTEL SALES SURVEY - Q3 2019

Q	PROPERTY	LOCATION	NO. OF ROOMS	ESTIMATED SALES PRICE	ESTIMATED PRICE/ROOM	BUYER	SELLER	
Q3	Birmingham Marriott	Birmingham	AL	295	\$39,900,000	\$135,254	Columbia Sussex Corporation	N/A
Q3	JW Marriott Phoenix Desert Ridge Resort & Spa	Phoenix	AZ	950	\$602,000,000	\$633,684	JV Trinity Real Estate Investments LLC & Elliott Management Corporation	Blackstone Group
Q3	Red Lion Hotel Anaheim Resort	Anaheim	CA	308	\$23,000,000	\$74,675	N/A	RLH Corporation
Q3	Irvine Marriott	Irvine	CA	485	\$152,000,000	\$313,402	Plaza Investment & Consultancy LLC	CBRE Global Investors Ltd.
Q3	Newport Beach Marriott Bayview	Newport Beach	CA	254	\$78,000,000	\$307,087	Clearview Hotel Capital LLC	Host Hotels & Resorts Inc.
Q3	Citizen Hotel, Autograph Collection	Sacramento	CA	196	\$53,200,000	\$271,429	Cambridge Landmark	Platinum Equity
Q3	Hyatt Regency La Jolla At Aventine	San Diego	CA	417	\$147,000,000	\$352,518	GAW Capital Partners	JV Walton Street Capital & JMA Ventures
Q3	Homewood Suites by Hilton - Boulder	Boulder	CO	112	\$16,900,000	\$150,893	JV Sage Hospitality & Brue Baukol Capital Partners	N/A
Q3	Grand Hyatt Denver	Denver	CO	516	\$115,180,000	\$223,217	TRTG GHD LLC	UBS Realty Investors LLC
Q3	Hampton Inn & Suites Silverthorne	Silverthorne	CO	88	\$25,500,000	\$289,773	JV Summit Hotel Properties & GIC	N/A
Q3	Hotel Madera	Washington	DC	82	\$23,300,000	\$284,146	Roch Capital	Pebblebrook Hotel Trust
Q3	Hyatt Place Washington DC/Georgetown/West End	Washington	DC	168	\$44,300,000	\$263,690	Artemis Real Estate Partners	Renaissance Centro
Q3	Regency Hotel Miami	Miami	FL	176	\$25,800,000	\$146,591	OPB Capital Group Fund 1 LLC	10 Le Jeune Inc.
Q3	Lord Balfour Hotel	Miami Beach	FL	81	\$34,750,000	\$429,012	Henley Investments	N/A

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Q	PROPERTY	LOCATION	NO. OF ROOMS	ESTIMATED SALES PRICE	ESTIMATED PRICE/ROOM	BUYER	SELLER
Q3	Richmond Hotel ¹	Miami Beach	FL 92	\$87,900,000	\$955,435	JV Deutsche Finance America & Bilgili Holding & SHVO	Patti and Allan Herbert
Q3	Sanctuary Hotel ²	Miami Beach	FL 32	\$14,400,000	\$450,000	Blue Road LLC	JV Sanctuary South Beach Inc. & Sanctuary SB Properties LLC & Sanctuary RonRuss Properties & MJK Group LLC
Q3	South Seas Hotel	Miami Beach	FL 118	\$52,000,000	\$440,678	JV Deutsche Finance America & Bilgili Holding & SHVO	Majestic Hotel Corp.
Q3	Residence Inn by Marriott Fort Lauderdale Pompano Beach/Oceanfront	Pompano Beach	FL 106	\$44,000,000	\$415,094	Impulsive Group	Claremont Cos.
Q3	Westin Tampa Bay	Tampa	FL 244	\$57,600,000	\$236,066	Castlerock Asset Management	Impact Properties
Q3	Hilton Atlanta Airport	Atlanta	GA 507	\$101,000,000	\$199,211	Wheelock Street Capital, LLC	Park Hotels & Resorts
Q3	Hyatt Regency Atlanta	Atlanta	GA 1260	\$355,000,000	\$281,746	Blackstone	Hyatt Hotels Corporation
Q3	Hyatt Place Augusta	Augusta	GA 115	\$16,400,000	\$142,609	Raines Hospitality	M&E Hospitality
Q3	Courtyard by Marriott Savannah Downtown/Historic District	Savannah	GA 156	\$29,750,000	\$190,705	Peachtree Hotel Group	Ashford Hospitality Trust
Q3	Courtyard by Marriott Chicago Downtown/River North	Chicago	IL 337	\$40,900,000	\$121,365	Blackstone Group	Host Hotels & Resorts
Q3	Chicago Marriott Suites O'Hare	Rosemont	IL 256	\$39,000,000	\$152,344	Vinayaka Hospitality	Host Hotels & Resorts, Inc.
Q3	Ames Boston Hotel ³	Boston	MA 114	\$63,500,000	\$557,018	Suffolk University	Invesco Real Estate
Q3	Four Seasons Hotel One Dalton Street, Boston	Boston	MA 215	\$268,000,000	\$1,246,512	Premier Group WLL	Carpenter & Company, Inc.

1) Transaction includes 18-unit apartment complex and parking lot

2) Hotel closed since Hurricane Irma in 2017

3) Buyer will utilize building as a student housing facility

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Q3	Courtyard by Marriott Chapel Hill	Chapel Hill	NC	169	\$31,000,000	\$183,432	Atma Hotel Group	Noble Investment Group
Q3	Hilton Garden Inn Raleigh-Durham/Research Triangle Park	Durham	NC	177	\$15,100,000	\$85,311	N/A	N/A
Q3	Holiday Inn Newark Airport	Newark	NJ	191	\$18,400,000	\$96,335	Regal Hospitality	JV RJB Associates LP & Fundamentals Inc.
Q3	Hooters Casino Hotel	Las Vegas	NV	657	\$135,000,000	\$205,479	JV OYO Hotels and Homes & Highgate	JV Junius Real Estate Partners & Trinity Hotel Investors LLC
Q3	Rio All-Suites Hotel and Casino ⁴	Las Vegas	NV	2548	\$516,300,000	\$202,630	Imperial Companies	Caesars Entertainment Corporation
Q3	Kimpton Ink48 Hotel	New York	NY	222	\$82,700,000	\$372,523	Brookfield Property Partners L.P.	PGIM Real Estate
Q3	Holiday Inn Saratoga Springs	Saratoga Springs	NY	168	\$21,800,000	\$129,762	JLK Global Fund U.S. 3 Inc.	Saratoga Pelican Associates LLC
Q3	Embassy Suites by Hilton Nashville Airport	Nashville	TN	296	\$80,200,000	\$270,946	Square Mile Capital	Starwood Capital Group
Q3	Hampton Inn & Suites Nashville - Downtown	Nashville	TN	207	\$101,500,000	\$490,338	JV Hakash Holdings, Douglas Development, & Triangle Capital Group	LCP Group and SEDCO Capital
Q3	Holiday Inn Nashville-Vanderbilt (Downtown)	Nashville	TN	297	\$75,600,000	\$254,545	Vanderbilt University	Natchez West
Q3	Marriott Plaza San Antonio	San Antonio	TX	251	\$34,000,000	\$135,458	JV White Lodging & REI Real Estate Services	Ashford Hospitality Trust
Q3	Residence Inn by Marriott Arlington Pentagon City	Arlington	VA	299	\$99,100,000	\$331,438	Blackstone	Host Hotels & Resorts, Inc.
Q3	Hotel Sorrento	Seattle	WA	76	\$21,000,000	\$276,316	Magnetic ERV	Sorrento Hotel Investors LLC
Q3	Embassy Suites by Hilton Milwaukee Brookfield	Brookfield	WI	203	\$19,200,000	\$94,581	2019 Brookfield Investment LLC	Brookfield Hotel Limited Partnership

4) Seller will continue to operate property pursuant to a lease for a minimum of two years at \$45 million in annual rent. Buyer also has the option to pay seller an additional \$7 million for the extension of the lease under similar terms for a third year. Seller retains its rewards customers and the hosting rights to the annual the World Series of Poker.

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