

News



Bidding wars could help the slow climb in hotel valuations

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REPORT FROM THE U.S.—The ever-growing line-up of hotel real-estate investment trusts has given some industry experts hope that hotel values might within the year begin a long, slow climb back.

REITs have been busy building up their war chests during the past several months in hopes of picking up distressed hotels at bargain basement prices. This could have the effect of rebuilding hotel prices, which have fallen as much as 50 percent to 70 percent during the past two years, said Daniel H. Lesser, senior managing director-industry leader at CB Richard Ellis in New York.

Indeed, per-room value has fallen by 32.1 percent to US\$55,132 in 2009 from US\$81,196 a year ago, according to the 2009 Hotel Valuation Index by consulting firm HVS.

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"In the back half of next year, there could be a rebound in value as bidding goes on," Lesser said.

Mike Cahill, president and founder of HREC Investment Advisors in Denver, Colorado, shared similar thoughts, though he said he sees pricing stabilization in 2010 before possibly picking up in 2011.

"The more people you have bidding for assets, the better prices they trade for," he said. "That will help, over time, to raise prices."

While a possible pricing rebound is looming, it hasn't come quickly enough for some properties.

More pain to come?

The owners of the 238-room Wyndham Orange County in Costa Mesa, California, could certainly have used an intense bidding war.

Previously owned by Makar Baynorth Costa Mesa, an affiliate of Makar Properties, the property sold at a foreclosure auction on 24 November to international real-estate company Rosanna, for US\$21 million, half of what it was valued at three years earlier. After purchasing the hotel for US\$42 million in 2006, Makar had secured it with a commercial mortgage-backed security loan of US\$31 million.

Struggles with undervalued properties have also popped up recently in company earnings reports. At least three hotel companies have indicated they are planning to give back properties to their lenders.

In a 5 November filing with the Securities and Exchange Commission, Lodgian said it expects to give back six hotels on which it can no longer meet the debt payments.

"The company believes that the anticipated cash flow from the hotels ... will not be sufficient to meet the related debt service obligations in the near-term," according to the report.

In addition, Lodgian revealed it had returned a Holiday Inn located in Phoenix, Arizona, to its lender because the company believed the hotel's value was "substantially" less than its mortgage of US\$9.4 million. "The company believed that it was unlikely that the value of the hotel would increase in the near or intermediate term and the hotel's operating performance would continue to decline," Lodgian said in explaining the reason for the give back.

Morgans Hotel Group Company, meanwhile, also said in a 6 November filing that it does not expect to "commit significant monies" toward the repayment of the debt surrounding its Mondrian Scottsdale. The Mondrian was subject to US\$40 million of non-recourse mortgage and mezzanine financing.

Finally, Sunstone Hotel Investors, Incorporated said in a 4 November filing that it has stopped paying on the Marriott Ontario Airport. The company said its lender declined to work out a loan modification on the property.

Representatives of the companies did not return calls for comment.

The people doing the appraisals for some of the hotel sector's now-distressed properties "had rose-colored glasses on," said Steve Hennis, managing director of hospitality and research firm Hospitium in Arvada, Colorado.

"At some point, this is going to come back to hurt the banks," Hennis said, adding he sees a slow return in valuation lasting from 2010 to 2014.

Mark Woodworth, president of PKF Hospitality Research, said with the mounting problems many hoteliers are facing today, there isn't necessarily a stigma attached to walking away from a debt. "The market is so upside-down it's not held against them," he said.

Back to market

As hotel operators send back the keys to the various properties, lenders will be eager to pass those keys on to someone else, CB Richard Ellis' Lesser said. After all, he said, the banks were never interested in managing the property in the first place.

Hennis said there will likely be an increased level of bidding activity beginning in the first quarter of 2010.

"One way or the other, there will be a push to get assets out to market," he said.