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## **In This Game, Paper Beats Brick**

By Carl Cronan

During good economic times, hotel investors focused largely on the best deals available for existing properties and potential sites. Now that the current recession is official, they are increasingly looking at the paper supporting the sector.

Hotel specialists are responding to the trend toward debt opportunities tied to distressed properties by expanding their services to handle distressed assets. Besides working with lenders and other financial institutions in evaluating assets, they are working with investors who are interested in acquiring loans on hotels that may be on the brink of foreclosure.

"As the market has shifted over the past 12 months, a lot of the investors we deal with are interested less in hard assets and more in hotel notes and mortgages," Geoff Davis, president of HREC Investment Advisors in New York City, tells GlobeSt.com. Those investors seek stronger yields and safety from the capital stack of performing assets, while also looking at loan-to-own prospects from those properties facing default, he says.

HREC Investment Advisors, part of Denver-based Hospitality Real Estate Counselors, last month hired William Lee as SVP at its New York office to focus on note sales and equity and debt recapitalizations. Lee has more than \$8 billion of commercial real estate transactions to his credit, having previously worked with Anglo Irish Bank, the Carlton Group and HVS.

"We are out there in the marketplace capitalizing on our long-standing relationships with investment banks, regional banks and hedge funds that are looking to get out of their positions," Lee says. He adds that HREC expects its transaction volume of notes and mortgage loans in the hotel sector to increase dramatically in the coming year.

While plenty of other commercial real estate brokerages are starting their own distressed-asset divisions, Davis says they tend to be generalists while HREC deals specifically with buyers and sellers specifically interested in hospitality paper. The firm was founded in 1994 and has eight offices across the country.

"A lot of what we do in that arena is not broad-based marketing, but more targeted," Davis says. For example, HREC would target 10 to 15 prospective buyers for a hotel note brought to it by a lender, he says.

Industry peers that have expanded services in response to the declining market include the Tampa-based Plasencia Group, which has received a rush of requests by clients for guidance in dealing with distressed hospitality assets. The company assists lenders and financial institutions in working through highly complex aspects of hotel operations.

"Hotels need to be treated as operating businesses, rather than pure real estate," says Lou Plasencia, the firm's chairman and CEO. "People tend to forget that hotel rent rolls are typically one night in length."

Plasencia also notes that economic constraints have impaired hotel values by as much as 30% in many cases. "Both borrowers and lenders need to realize that this could mean there is no longer any equity in a particular asset," he says.

Davis says the overheated market for hotels caused the sector's operating performance to decline

at such a traumatic level that has forced many seemingly healthy assets into distress. He points to HREC's experience with debtor-in-possession sales, workouts and value preservation as giving it an advantage over other hotel consultants, adding that its principals have handled 65 REO hotel sales.

"We've seen some mistakes made by people buying notes based solely on yield parameters without really understanding how that particular asset is operated," Davis says. "It all comes down to the underlying fundamentals of what is a unique operating business, as opposed to other forms of commercial real estate."

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