Hotel transactions environment remains complex

ATLANTA—Everyone involved in the hotel industry knows there have been plenty of issues to work out in the lending environment. Speakers on the "Buying & Selling Hotels Today" panel earlier this month at the Hunter Hotel Investment Conference said the hotel lending complexities that have plagued the industry for the past 30 months aren't going to change any time soon.

"Not everybody's out of the woods," said Teague Hunter, president of Hunter Realty Associates. "There are loan maturity issues … we still have things to work through."

"The next 12 months will continue to bring complexity," said C.K. Patel, president of BVM Holdings in Atlanta, adding that uncertain oil prices bring another layer of potential setbacks to hotel deals.

Jim Gray, VP of CW Capital Asset Management of Bethesda, Maryland, said uncertainty over the commercial mortgage-backed securities market casts a shadow over hotel deals. He said there is US$18.5 billion in CMBS maturities coming due between now and the end of 2012, and that is a daunting number to get refinanced in an already tight lending environment.

Deal landscape improves

Patel said two things must happen for a deal to be considered good for a buyer: maintaining the franchise agreement and incorporating property improvement plan capital into the sale price.

The panelists agreed that in some cases an owner should complete a PIP before bringing an asset to market.

"But it really depends on what buyer wants to do," Kolessar said. "If they're going to change the flag, it does no good for you to do brand standards."

Hunter said it's a moot point in the current environment.

"Most of the time people don't have the money so it's not an option," he said. "If it's simple and obvious, do it. But it's usually complicated."

Gray said CW is spending money on a selective basis on the better brands in the better markets.

Moderator Glenn Haussman said deal-making began making a comeback in 2010 after hitting the bottom in 2009. He outlined the number of deals made during the past four years:

- 2007: 3,547 deals
- 2008: 1144 deals
- 2009: 513 deals
- 2010: 1,298 deals

Hunter said he expects his company's activity to double this year over last year, which was double over 2009.

Jeff Kolessar, senior VP of development for Philadelphia-based GF Management, said the company closed 20 "sales events" last year.

"This year we already have six ranging from (US)$800,000 to (US)$124 million," he said. "It's a wide range of deals, but there are buyers out there."

The REIT stuff

He said one drawback for companies to complete deals is the premium prices that real-estate investment trusts are bringing to the table to acquire hotels. "The premiums most of the REITs are paying are pretty substantial," Kolessar said.

Patel had one piece of advice for potential buyers: "Don't follow the REITs. Their prices are too high."

"If the REITs are buying at 4 and 5 (capitalization rates) in major markets, then that's where you don't want to be," Gray said. "You want to be in tertiary market with higher caps."

Hunter said it comes down to simple arithmetic when comparing REITs with other potential buyers in today's market.

"Your money's more expensive than the REIT's money is," he said. "You have to roll up your sleeves and provide value-adds. Be brighter, smarter, faster, quicker. … The REITs are making a living off (loan) maturity issues."

Patel provided two main reasons owners are selling: they can't get their bank to work with them on restructuring a loan or they are trying to sell to raise capital to acquire a better property.

Properties on the block

Gray said properties his company will be selling include those that are approaching functional obsolescence and those that are capital starved and bleeding operation losses.

"Right now it's a lot of everything out here," Hunter said, adding that there are plenty of distressed hotels on the market. "We've always had a bifurcated market; it's more than ever today."

The panelists identified markets they consider "winning markets:"

Patel: The Northeast and California. "The Northeast has always come back pretty fast. California, it has the land values."
Hunter: "Major metros are where everyone wants to be. You're going to hear that over and over and over again."
Gray: "The larger cities are going to appreciate faster but the better buys are in the tertiary markets."

Kolessar said he is starting to see good assets come to market—product such as Hilton Garden Inn, Holiday Inn Express and Hampton Inn. Most were acquired in 2006 or 2007 and are simply overleveraged.

"The first question I always ask when looking at a property is 'when was the loan originated?'" he said. "You can tell a lot from that."

Most deals today are all-cash transactions, although the panelists said lenders are starting to be more active in the exploratory stages. Patel said regional and local banks are still shy about lending because of prohibitive government regulatory issues.

"The vast majority of our deals are all cash," Hunter said. "Financing contingencies today are not allowed."