

2016 HOSPITALITY LAW CONFERENCE

FEBRUARY 22-24, 2016



BUY VS. BUILD – MAKING COMPLEX DECISIONS

John Keeling- Valencia Group

Cliff Risman- Gardere

Nate Sahn- CBRE Hotels

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PRESENTERS



Cliff Risman

Partner, Gardere

- ❖ Cliff advises clients in the development, acquisition, financing, and operation of domestic and international hotel, resort, and mixed-use properties and the negotiation of management, franchise, development and design agreements
- ❖ Cliff is a member of the by invitation only International Society of Hospitality Consultants and has been recognized by Chambers and Partners as a leading lawyer nationwide in Leisure & Hospitality.



Allen R. Wolff, Esq.

Executive Vice-President, Valencia Group

- ❖ John Keeling is Executive Vice President of Valencia Group, primarily responsible for sourcing and vetting hotel acquisition and development projects. Valencia specializes in the development and operation of luxury independent hotels. In 2015 each of the four urban Valencia hotels was rated the number one hotel in its respective city by *Condé Nast Traveler* magazine.
- ❖ A recognized authority on hotel matters, Mr. Keeling has been quoted in the Wall Street Journal, New York Times, Newsweek, Business Travel News, Hotel Management, and numerous weekly business journals and daily newspapers



PRESENTERS



Nate Sahn

Senior Vice-President, CBRE Hotels

- ❖ As a member of the Hotel Group, which successfully transacted 250 hotels during 2013/2012 with a total sales consideration of over \$2.0 billion, Mr. Sahn is based in the firm's Chicago office and works on national hotel advisory and disposition projects, specializing in single asset and small portfolio transactions
- ❖ Mr. Sahn utilizes his hotel operational experience, hospitality education and financial analysis expertise to best serve the company and client's expectations. Involved in every aspect of the transaction process including hotel valuation, development of disposition strategy, oversight of the marketing process, solicitation and negotiation of offers and coordination of the due diligence process



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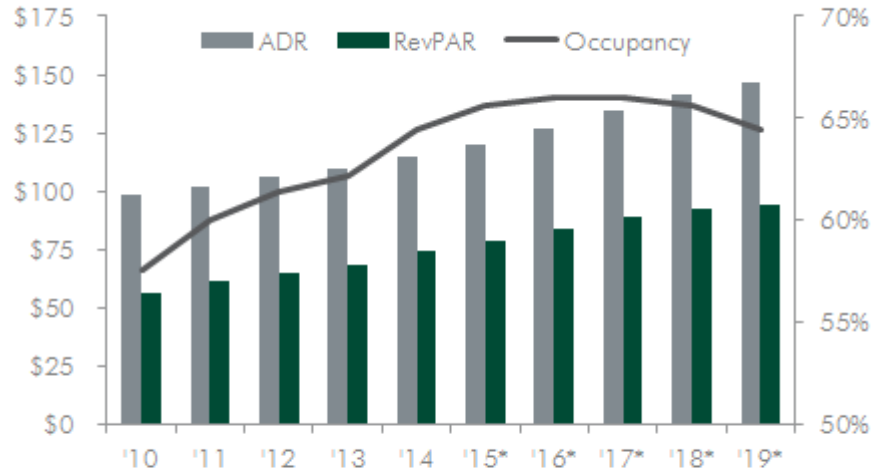
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NATIONAL LODGING MARKET

U.S. HOTEL PERFORMANCE



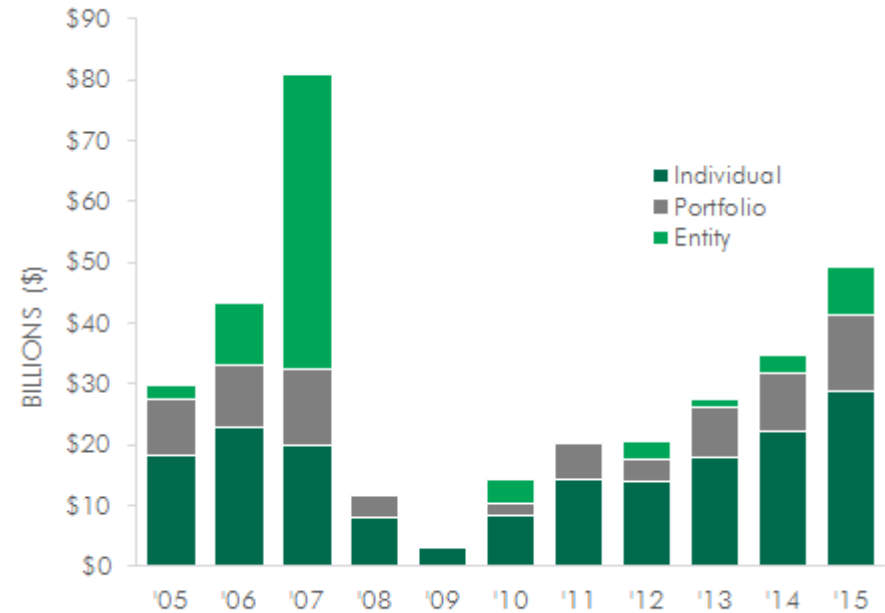
Footnotes:

1 CBRE Hotels' Americas Research Hotel Horizons® December 2015 – February 2016 National Edition.

2 The periods denoted by an asterisk indicate projected performance.

Even though supply growth is expected to pickup in 2016, the lodging industry should continue its record breaking performance for the foreseeable future according to CBRE Hotels' Americas Research. Further uptick in demand will result in the seventh consecutive year of rising occupancy. ADR growth is forecast to increase by an impressive 5.5%, which continues to be the catalyst for the lodging market's exceptional RevPAR achievements. This factor translates into hard earned cash as expense margins are reduced and profitability is maximized. As such, CBRE Hotels' Americas Research is forecasting net operating income increases greater than 10% in 2016.

U.S. HOTEL TRANSACTIONS – VOLUME SUMMARY



Source: Real Capital Analytics, Q4 2015.

According to Real Capital Analytics, the hotel sector posted 42% growth in investment activity for 2015 on sales of \$49 billion. The 2015 story was aided by portfolio and entity level transactions but it was not the only story of growth. The sale of individual assets grew 32% in 2015 with volume of \$29 billion. 2015 marks the highest level ever seen for individual asset sales in the hotel sector.

Volume did grow faster for the mega-deals however, with 59% annual growth for the portfolio and entity level deals. The \$20.5 billion in sales for these mega-deals in '15 was the second highest level for transaction volume of these types behind the 2007 peak.

WHY BUY HOTELS?

- Up until the 3rd quarter of 2015, the transaction market was robust, driven by the attractive debt markets, low cost of capital and rising hotel profits
- REITS and other public buyers were the driving force in the transaction market directly responsible for over 25 percent of the trades
- Continuous strong fundamentals have driven hotel profits to record levels over the last 48 months
 - Between 2011 and 2015 – RevPAR growth was driven in balance between occupancy and ADR growth as shown below
 - On a going forward basis – RevPAR growth will be driven by mostly ADR as occupancy growth slows amidst new supply
- Supply increases while still below the national long run average, isare being felt in some markets more than others. This is shown in the attached slide below that identifies which markets are over supplied and which others represent good building opportunities
- Many analysts have signaled to the market that we are past the peak in the lodging cycle and that the sustained RevPAR growth will not continue for the long term



WHY BUY HOTELS?

- Signaling from market analysts that we are past the peak, coupled with economic problems in Asia, resulted in a culmination of factors that has put downward pressure on REIT stocks resulting in significant declines over the last quarter. Hotel REIT's in general are down between 10-40%, which has effectively put them on the sidelines as buyers. Continued reports about reduction in RevPAR gains coupled with supply increases have led to a mass conservative outlook from lenders in the hotel space. As such, LTV's are declining and rates are increasing. This is leading to cap rate increases despite the fact that hotel profits continue to grow and should do so for the near term
- CMBS lenders who were driving the transaction market coupled with new financial regulations have effectively reduced their penetration in the space, thus making transactions more difficult



WHY BUY HOTELS?

- What deals are attractive to buy?
 - Power branded select service and extended stay deals are still attractive with many suitors – stocks that focus in this space like INN and Apple REIT, are poised to perform well
 - Cap Rates for these assets have increased 25-50 basis points since the 3rd quarter of 2015
 - Value add properties with a “true story” are gaining attention
 - Up branding
 - RevPAR growth story
 - Renovation Story
- Avoid the time lag inherent in development (from planning and permitting through construction)
- Relationship of purchase price to replacement/development cost



WHY BUILD HOTELS?

- Several new brands have entered the hotel space
- The boutique segment is driving the new brand marketplace – experience driven lodging
- New builds can fill a void in a respective market
 - Both independents
 - Power brand boutiques like
 - Autograph
 - Curio
 - Canopy
 - Tribute
 - RL
 - Even
- Mid-scale, extended stay, and limited service new brands are emerging as well
 - Marriott A/C
 - Moxy by Marriott
 - TRU by Hilton
 - Home 2 Suites
 - Cambria Suites



WHY BUILD HOTELS?

- Several niches are trying to be filled
- Where is building most rampant
 - Urban markets
 - Strong suburban
 - Secondary / tertiary
- Up until 2016 Financing for new hotel projects has been ample
 - With lenders taking a more conservative view on the hotel space and agreeing with the implied perception that we are near the end of the cycle how will that impact new projects going forward?
 - Which deals get approved?
 - Which deals get denied?
- Brand/management desire for new product and participation in development via use of their balance sheets

