

US hotel deal flow shows slowdown

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Story Highlights

Nearly \$6 billion in hotel transactions occurred during the first half of 2012, less than half of what was done during the same period a year ago.

"My view is it's a little challenging if you're trying to be a high leverage borrower," said Watermark Capital's Michael Medzigian.

Only 16% of deals were done by REITs during the first half, compared to 35% a year ago.



The Hilton Garden Inn New Orleans French Quarter/CBD was acquired by a joint venture of Carey Watermark Investors and HRI Lodging for \$22.8 million.

REPORT FROM THE U.S.—When Brian Stage was named president of Wedge Hotels Corporation in January 2010, his mission was clear: Find opportunities to grow Wedge's portfolio.

Two and a half years later, Wedge made its first acquisition under Stage's leadership. The company acquired for an undisclosed sum four Hilton-branded hotels in secondary U.S. markets.

Wedge, now with eight hotels in its portfolio, has been careful to ensure it is chasing the right targets and that the economics on any potential deal work. "It's a long road, and it should be," said Stage, formerly the president of Carlson's Radisson brand. He added that the company sees good value looking in secondary and tertiary markets partly because those locations were not hit as hard during the downturn.

While Stage and other sources interviewed for this report said they're seeing opportunities to acquire hotels, transactions data reveals a less active deals picture. According to numbers released by STR Analytics' Hotel Transaction Almanac Midyear 2012 Update, there was nearly \$6 billion in hotel transactions through June. That's less than half the \$13.1 billion in volume seen during the comparable period in 2011.

Jones Lang LaSalle Hotels, which tracks deals of \$5 million and higher, saw deal volume of approximately \$5.7 billion through the first half of 2012, down 30.5% from \$8.2 billion through the same period a year ago. JLLH does not include recapitalizations, foreclosures or the recently announced [\\$1.9-billion acquisition](#) of the Motel 6 brand by Blackstone Group in its analysis.



Brian Stage
Wedge Hotels Corporation

"Investors are very enthusiastic about hotels as an investment class," said Gilda Perez-Alvarado, senior VP at JLLH.

Financing challenges

An overall lack of transaction financing has been a stumbling block for deals in the past, though the debt market is loosening, sources reported.

"Debt is definitely available; it's more so available than last year," Perez-Alvarado said. She added that qualities lenders are looking for in a deal

include strong in-place cash flow for the asset in question and strong sponsorship.



Michael Medzigian
Watermark Capital
Partners

Since beginning operations as a non-listed real-estate investment trust in March 2011, Carey Watermark Investors closed on six hotel transactions, said Michael Medzigian, chairman and managing partner of Watermark Capital Partners and president and CEO of Carey Watermark Investors. In June, Carey Watermark announced the \$22.8-million joint-ventured acquisition of the 155-room Hilton Garden Inn New Orleans French Quarter/CBD.

The company's investment criteria include urban select-service properties with some degree of barrier to entry and hotels with solid cash flow. "We like the hotel investment environment," he said.

Typically, Carey Watermark looks for debt in the 50% to 55% loan-to-cost range, Medzigian said.

"We're seeing good availability of the kind of debt we're borrowing," he said. "My view is it's a little challenging if you're trying to be a high leverage borrower."

REIT buying stalls

STR Analytics' analysis showed that REITs, at one time aggressive buyers of hotel assets, are continuing to back off. Just 16% of hotel transactions were done by REITs during the first half of 2012. By comparison, 35% of deals during the first half of 2011 were done by REITs.

Pebblebrook Hotel Trust, for one, acquired three hotels through July: the Hotel Milano in San Francisco, the Hotel Vintage Park Seattle and the Hotel Vintage Plaza Portland in Oregon.

During the same period a year ago, [Pebblebrook](#) bought six hotels and also entered into a \$910-million joint venture with Denihan Hospitality Group to [acquire six Manhattan hotels](#).

During the company's second-quarter conference call with analysts, Pebblebrook's Chairman, President and CEO Jon Bortz appeared confident deals were a possibility for the second half of the year. The REIT owns 23 hotels (17 wholly owned) comprising 4,162 rooms.

"I think what we can say is that the activity level in the second half for the industry and hopefully for us will be significantly higher than it was in the first half," Bortz said. "We've seen a very positive momentum in the number and quality of assets in the major gateway markets that we have an interest in, and we believe that (we) will continue to get at least our share in both on-market and off-market transactions."

Plenty of opportunities

While transaction volume isn't as robust overall as it has been in the past, sources said they are still seeing opportunities aplenty.

"I think the second half of the year is looking pretty interesting," Perez-Alvarado said. Private-equity firms will be big players on the U.S. transactions scene and REITs are likely to be busier during the second half of the year, she added.

JLLH expects hotel transaction volume in 2012 will at least match 2011 with an estimated \$15 billion in deals.

Medzigian said Carey Watermark has a strong deal pipeline from which to work. "Things are getting more active now," he said. "I don't think it's a decline, but I don't think you'll see transaction volume double."

Stage shared a similar sentiment: "My perception is it's not necessarily slower," he said. "I actually think things are continuing to bubble along."