



Mixed reviews for county, state hotel market

By THOR KAMBAN BIBERMAN, The Daily Transcript
Tuesday, October 12, 2010

Lodging experts say the hotel market has bottomed out -- but one might not know it looking at the number of foreclosures in San Diego County and across the state.

Both Alan Reay, **Atlas Hospitality Group** president, and hotel consultant and area hotel developer Robert Rauch said that RevPAR (revenue per available room) bottomed out at mid-year and has started to increase.

That may come as cold comfort to those who have their hotels in default or lost them.

Atlas reported that 13 hotels in San Diego County have gone all the way through the foreclosure process -- a figure that was the highest of any California county.

San Diego was followed by Riverside County, with 12, and Los Angeles and San Bernardino counties, with 11 each.

Aliso Viejo-based **Sunstone Hotel Investors** (NYSE: SHO) -- which walked away from the 258-room W Hotel earlier this year -- is walking away from the 220-room Holiday Inn on First Avenue downtown, handing or has handed back another nine hotels, and says it wants to acquire more to feed its investors.

Qualified Sunstone officials could not be reached for comment Tuesday.

When asked about the future of hotel real estate investment trusts, Reay suggested that even ones with a less than stellar history continue to lure investors and therefore will have a better chance than most of purchasing assets for bargain basement prices.

Reay pointed out that just because a REIT purchased a hotel at the bottom of the market, it's no guarantee of success.

"REITs are basing their pricing on pretty optimistic projections," Reay said, suggesting that this could mean trouble later.

Both Reay and Rauch said defaults will continue to be part of the picture next year, regardless of what RevPAR has been doing.

With 52, Los Angeles had the highest number of hotels that were in default, but were yet to be in foreclosure.

Los Angeles was followed by San Diego, with 41 and San Bernardino County with 47.

Atlas reported that 529 California hotels are in default or have been foreclosed upon this year. The largest of these to go through foreclosure was the 512-room Holiday Inn in San Jose.

High profile notes that have gone into default here include the \$186.5 million loan is secured by the 329-room Park Hyatt (formerly the Four Seasons) Aviara Resort in Carlsbad.

Broadreach Capital Partners and **Maritz Wolff & Co.** own a majority stake in the Aviara asset.

The other note in default is a \$73 million construction loan secured by the 184-room Hotel Se in downtown San Diego recently placed in Chapter 11 bankruptcy by **Fifth Avenue Partners**.

Rauch said the Park Hyatt Aviara Resort has a better chance of weathering the storm if for no other reason than it is a "branded" hotel.

"I think they can resurrect themselves if they can restructure the loan," Rauch said. "I think a hotel like this can survive, but it can't survive at its current debt level."

First, a lender must decide whether to place a hotel into default and then whether to take a property through the foreclosure process.

Both can look ugly on a balance sheet. Despite those pitfalls, Reay said lenders are becoming more proactive about these troubled instruments.

"There's a willingness amongst lenders to put loans into default," Reay said. "We had pray and delay, pretend and extend, but now lenders see the reality and pressures are being brought to bear."

Randy Hulce, **Trigild Corp.** managing director of hospitality, agreed.

"While lenders aren't going to flood the market with these hotels, there will be a lot of pressure from regulators telling them to clean up their balance sheets," Hulce said.

That said, Reay and Rauch added there may be room for negotiations with lenders. Reay noted that finding a white knight doesn't hurt, either.

Extended Stay Hotels, which filed a \$7 billion Chapter 11 bankruptcy and was facing the demise of its brand and the loss of its hotels last year, just emerged from bankruptcy after an investment partnership of the **Blackstone Group**, **Paulson & Co.**, and **Centerbridge Partners** paid \$3.9 million to acquire the hotel group. Extended Stay owns 600 hotels including several in San Diego.

Hulce, whose firm acts as a receiver for troubled assets including hotels, said there is still plenty of trouble out there.

"I think we will see an increase in defaults next year. I notice we're seeing a number smaller hotels in trouble that are valued at \$10 million or less," Hulce said. "I think we'll see some occupancy gain next year but it won't be enough for the rates to gain significantly."

Atlas agreed, stating the California market is still sitting on a time bomb.

"We are still seeing a disproportionate number of hotels operating under some form of forbearance agreement, which is creating a huge 'shadow' inventory of distressed deals that are yet to hit the default market," Atlas wrote. "We estimate that this is as high as 1,000 hotels in addition to the 529 in default or foreclosed."

Hulce said while there may be a lot of problems for hotels as a whole in California, he remains very confident in San Diego.

"I'd still rather be in San Diego than Fresno," Hulce said.