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Supply, acquisitions take spotlight

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While speakers at the Meet the Money Conference said there isn't an immediate concern over growing supply, they are closely monitoring that situation.

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LOS ANGELES—Speakers at last week's Meet the Money Conference for the most part were not concerned about the U.S. hotel industry's supply growth rate—but that doesn't mean they're not keeping an eye on it.

"Supply is going to be a concern, although we're more concerned about (competitive) set as opposed to broader markets," said Gary Swon, managing director of Societe Generale, during the "Playing with a full capital stack" panel. "New supply is certainly not a nonstarter or something that will chase us away from a market."

"Supply is coming back but at a slower pace than most people would have expected," said Colin Carroll, VP of investments for Ashford Hospitality Trust, during the conference's "Acquisition strategies that make and shake the market" panel.

Carroll said higher construction costs, relatively conservative lending standards and other uses for the land are prime contributors to the muted supply growth.

Ronald Kim, senior VP of real estate for Orange, California-based Prospera Hotels, said during the during the "Acquisition strategies" panel that land prices are skyrocketing and rising construction costs are also contributors to the tighter supply-growth numbers.

Prospera launched in 2003 with a deep renovation/conversion of a closed hotel, and the company now has three hotels open, two under construction and more land ready to be developed—all in Anaheim, California.

Mike Depatie, president of KHP Capital Partners, said during the same panel that the rate of supply growth is comforting when compared with historical numbers. Carroll said that going into 2016, 14 of the last 18 years will have been below the long-term supply growth average.

Vail Brown, VP of global business development and marketing for STR, told the lunchtime crowd during the "U.S. lodging industry—what lies ahead?" presentation that the current supply growth rate is 0.9%—well below the 20-year compound average growth rate of 1.7%. STR is the parent company of Hotel News Now.

Kyle Jeffers, a commercial real estate banker at Starwood Property Trust, said during the "Capital stack" panel that there's not a simple answer to the supply question, but the fundamental question revolves around demand generators. He pointed to Austin and downtown Los Angeles as specific markets that will be tested when all the new supply comes online.

"Will enough demand be generated to fill the rooms?" Jeffers said.

Each speaker made it clear that they are diligently watching the supply growth trends at the micro and macro levels.

“There's no black-line markets, but we are very cognizant where the supply is an issue,” Cara Leonard, senior VP for Lowe Enterprises, said during the “Capital stack” panel.

Others said unintended consequences could arise from certain supply growth. Tom Morone, principal with CHMWarnick and moderator of the “Acquisition strategies” panel, said the additional select-service hotels being added to the supply pipeline can wreak havoc on some existing properties and markets.

“A great new Hampton Inn next to an old Hilton is pretty devastating,” he said.

Take on transactions
The lack of supply has led to an abundance of transactions, and speakers said they were happy to see the activity.

One target gaining popularity in buyer circles are value-add projects in secondary markets because there are fewer bids for them than there are for cash-flowing large, urban properties, Carroll said.

Owners who are targeting single markets, such as Prospera, are patiently looking for growth opportunities.

“We're not looking at a national stage on the acquisition side,” Kim said, adding that his company likes the Anaheim market because there are excellent demand generators, including Disneyland and the Orange County Convention Center. However, Prospera is poised to expand into other areas of Southern California as well as the San Francisco Bay area.

Most markets still are in prime position in terms of valuations, speakers said.

“The longer distance on the run on the cycle at least from the acquisition side will be the case,” Bill Blackham, president & CEO of Supertel Hospitality, said during the “Thoughts from the executive suite” panel. “The markets we're looking at have values peaking out past 2017.”

Bill Doak, first VP at The CIM Group, said during the “Acquisition strategies” panel that although the company is in “the business of selling now”—he pointed to the recent sales of the Hollywood Renaissance and the Oakland Marriott as examples—it remains interested in making acquisitions, too.

“We focus on the twisted deal, one that's a little hard to get to,” Doak said. “What we're competing with, some of the (real estate investment trusts) and international funds, it's a bit difficult for us.

“Hotels are the highest return expectation and probably the lowest priority in terms of acquisition right now,” he added. “We have a lot of mixed use on the books right now with hotel pieces.”

KHP, which was formed after InterContinental Hotels Group acquired Kimpton Hotels & Restaurants for $430 million in January, also is on the lookout for acquisitions, according to Depatie.

“There's still great opportunity in the boutique, independent lifestyle side of the business,” he said.

Depatie said KHP likes adaptive reuse projects because his team has specialized knowledge to take an old building and turn it into a boutique, modern hotel.

Many other speakers talked about adaptive reuse and deep renovations. Philip Cyburt, CEO of Laurus Corporation, might have summarized it best: “We're buying a lot of hotels and putting more into the hotel than we're buying them for.”