Smaller Hotel Investors Cannot Wait Any Longer

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The April HBI Marketplace theme is “2012: The Year of Opportunity”. Interestingly Steve Rushmore wrote two years ago: “2010 is the year to buy”. Who listened to Rushmore then? …the big boys, REITs and equity funds, who had cash. They did the bulk of the buying the last two years. The REITs have been out of the buying scene since 3Q 2011, for the most part because they used all their cash. With the stock market rallying in 2012, they will be back in 3Q and 4Q 2012.

They knew in 2010 that the hospitality industry had seen the bottom. By the end of 2011 we all knew we were past the bottom. RevPAR increased 5.5% in 2010. According to STR Global 90.2% of the 212 hotel markets in the Americas increased RevPAR in 2011. For those large organizations that are in the business of owning hotels, they know buying anytime in the down cycle is good. They know: (1) the cycle will improve; (2) interest rates are at lifetime lows (the cost of money will never be cheaper, inflation is around the corner); and (3) capital costs per room after renovations are still at 30% to 50% discounts to replacement costs. One can withstand slower cash flow initially with those numbers.

Since 15-18 months after the initial fall in 2008, many individual investors said it was too soon to buy. But has anyone heard of hotels bought in 2010 and 2011 being bad investments? NO! They all are or will be home runs. So why would 2012 not be a good year to buy? It may be the last best year to buy!

If one has cash, one has options. One can pay cash or put 50% down for a conventional loan at great rates. This scenario could go like this: 50% from a lender at 6.0%; 25% partners’ loan to the LLC at 6.0% (better than the <1.0% cash one gets at a bank) and then the last 25% is the normal equity. Consider the middle 25% (loan to LLC) is like being one’s own banker and receiving returns on that portion at market lending rates. Another option: SBA loans are plentiful again with 25% and 20% down payments. Even conventional loans have been done with as little as 22% down.

Many smaller investors like the Vantage Hospitality franchisees have also been sitting on the sidelines with cash. Take a zero off amounts REITs look at for revenues, price per room and values and it is all the same for the small investor at $3,000,000 as is $30,000,000 for the big guys. Now is the time to buy. According to Steve Hennis at STR Analytics, “After hotel values dropped a minus 32.7% in 2009, 2010 and 2011 saw dramatic increases of 28.1% and 74.0%, respectively.” That means hotel prices are 50% higher than in 2008 before the bottom dropped out.

How much longer can one afford to wait? By Steve Rushmore’s assessment, most are two years late already.

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