

PERCEPTION VS. REALITY



One of the pervading problems in hotel industry analysis is how attached people get to certain perceptions. And the problem with perceptions is they are not necessarily rooted in fact, they're usually gleaned

from some erroneous information that flies around from person to person, from cocktail to cocktail party. Before you know it, Bam! That factoid is taken for reality.

So let's pull back the shiny small talk veneer and take a look at some real facts based on a discussion I had with Bruce Ford, SVP of Business Development at Lodging Econometrics recently in front of the crowd at the sold-out BITAC Purchasing and Design West.

Erroneous Perception #1: Operating Performance Softening/Slowing

Truth: Industry will be helped by less new hotels, but also more rooms are offline for renovations.

While a couple of big cities are seeing a slowing down, markets such as Washington D.C. and New York continue to be strong demand generators. Sure, demand is slowing but it's still robust as unsustainable increases ebb. The industry was coming off the bottom so those numbers look exaggerated.

"There is still demand continuing to buy hotel rooms and when they are sold rooms come offline for renovations. We're going to see demand increase again, not as much in 2010 and 2011,

but there will be fewer rooms available," said Ford. That should help keep occupancy rates higher and prompt owners to increase rates. Bottom line is 6 percent demand increases are not sustainable and they'll return to a more normalized yet healthy two to three percent.

Erroneous Perception #2: New Construction is Dead

Truth: The new construction pipeline is returning. We all know people that have seen projects cancelled, mostly because of financing issues. These days people are "getting ready to get ready" to build, said Ford, who added that early planning has stabilized and is increasing at a clip of more than 20,000 rooms per quarter.

"We're in the fourth year of a 10-year cycle, like 1993 and 1994. Focusing on the right things is foreign, because we've been in a project market for many years. Now it's more about relationships. You have to get successful interchanges with people who make multiple decisions on properties," said Ford.

Erroneous Perception #3: There will be a Double-Dip Recession

Truth: The general economy does not totally apply to hotel industry.

"There is a [separate] hotel economy," said Ford. "We may go down first, but what has happened is that people go a certain amount of time without traveling, and then they have to make those trips to see family, they have to travel for work."

Believe it or not, the hotel industry has been trending positive for more than 18 months now and lodging demand looks good.

Additionally, real estate values are recovering, though banking is still a problem. It's why construction is returning to early stages and not yet translating to projects in the ground. Very modest increases in new supply are outweighed by more robust demand increases, which create positive growth for hotel rates and occupancy.

Erroneous Perception #4: Renovations are Underfunded

Truth: You have to renovate to take advantage of the increased demand and many renovations are getting funded as hotels trade owners.

Guest interaction is key. You may not overhaul, but you have "guy across the street" conversations. You have to compete there, and that's spurring renovations.

"New funding resources will be needed to accelerate non-ROI renovation programs, but money is there for areas with a definitive ROI," said Ford. "Additionally, furniture equipment leasing coming back, mezzanine debt coming back to spur these renovations, and the brands will turn the screws more and more to make sure hotels are up to snuff."

The State of the Industry

All of the above news adds up to something not too many are talking about: The business of serving hotels is on the mend. Finally.

And while the healing has begun it's taking time for industry buyers and suppliers to adjust to yet another new dynamic. Fortunately this time the shift is more about opportunity than sheltering a company from risk.

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But even with opportunity abounding there are challenges ahead. Seems odd too much work can be a problem, yet here we are. After three years of trimming the fat, slashing expenses and eliminating business redundancies, companies are lean but now may be understaffed and under stocked on products.

So hotel executives looking to renovate their properties better get started planning now or risk being at the end of long line of projects. In fact the rush of new projects on the drawing boards is making it increasingly difficult to get projects executed in a timely manner. Though hoteliers want their hotels renovated immediately, timelines are lengthening.

You have now officially heard the warning: Renovate now or forever hold your peace.

"Everything is taking longer," said Guy Lindsey, Senior VP-Design & Construction with Sunstone Hotel Investors. "We have had a comedy of errors on a project because products you used to get quickly are harder now. Upholsteries, fabrics, specifically are long now, where they weren't in the past. Because many companies are understaffed they can't process the orders fast enough. The competition is high and it's hurting there."

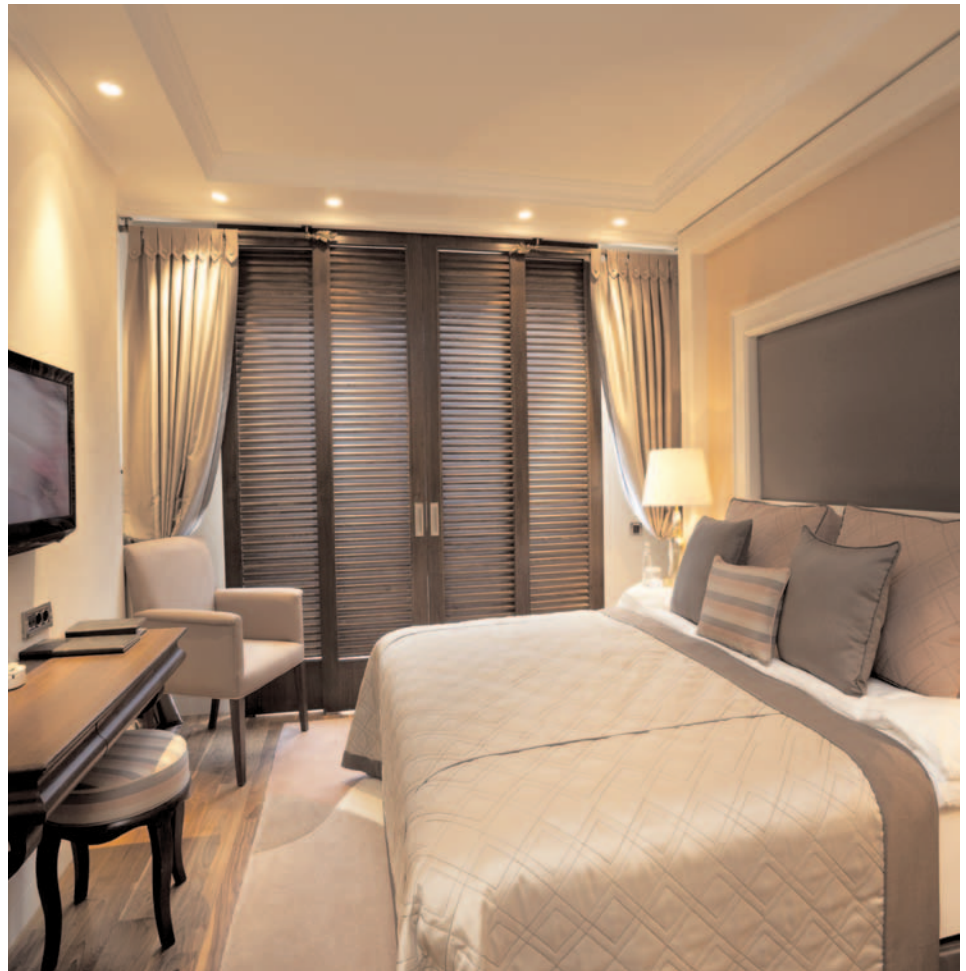
Rick Tomljenovic, Principal, Tristar Hotel Management agrees. "People will not hold a lot of inventory, and we are struggling with that. Occupancy isn't down, rate is down, so closing that wing to do renovations is hard, and scheduling is important," he said.

In fact BITAC attendees are seeing the same issue. In a real time poll taken of attendees, 60 percent said they are experiencing longer lead times for renovation projects, while 40 percent see shorter.

"We are seeing much longer waiting times for products coming from overseas," said Justin Smith, President/COO, Prestige Hospitality Group

Angela King of Restoration Hardware said she is actually losing jobs if she can't fulfill orders quick enough.

"It seems like developers of hotels are in a hurry, and as suppliers we have a hard time because no one is stocking inventory. I've lost jobs because I can't supply quick enough," said King.



Claudia Baker, President of Baker Design Associates says she is seeing longer lead times with everything. "Fabric manufacturers are not stocking, that has almost doubled which creates a barrel effect. When you get fabrication going, it's late. As a designer, getting our projects designed has been cut by a fourth in some cases. Then the manufacturers we love to use are getting swamped," she said.

Lindsey said he is working to accepting this new reality and is adapting accordingly. "We've tried to focus on renovations, and we have gotten through 2012 budget and looking toward 2013. We appreciate what the vendors and manufacturers are going through, we need to prepare for the longer lead times, but sometimes we don't have the window. So we zone in on products we need to fill that space in, and that could mean changing product if we need to," he said.

Supplier competition seems to be rising too according to BITAC attendees. When asked if they see more competition entering the market in your specific segment 39 percent said some and 24 percent

said a lot while just 19 percent said there is less competition as companies have closed in recent times.

"There is tremendous amount of solicitation for new products, and we get to develop relationships with them. I see new faces come in constantly," said Prestige's Smith.

Lastly, Rosewoods' Kluck espoused his philosophy on working together, even if there are long lead times. "We need to work with our suppliers so we're not in the same place we were in the past three to four years. We need to methodically move forward with this. If you can't get it to us for 20 weeks, we need to know. Just be honest and move together as an industry to sustain a longer period of time," said Kluck.

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