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# Subprime contagion spreads to hospitality transactions

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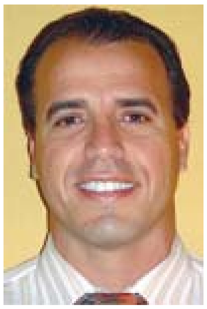
Just last year, we were so upbeat about the future of the hospitality industry in Florida. Things are different now. With obstacles such as an economic slowdown, high energy costs and a decline in travel for both business and consumers, the hotel industry is starting to lose that resiliency it had shown for the last four years.



**Julian Mazili**

Occupancy is down 4% in Florida compared to 2.5% nationally in 2008, while the ADR stayed at more or less the same level as in the previous year. This shows that hotel operators are not panicking by substantially lowering the rate like they did in 2001 and 2002.

The economy segment has been the hardest hit. The reason: Florida has a large number of mid-scale to economy hotels available in the market competing for the same leisure and small business travelers. The summer business will be more sluggish than in previous years, but we predict a quick rebound in early 2009 as demand continues to outpace supply.

As a result of the downturn in the economy and its effect on the hotel industry, hotel transactions are becoming increasingly difficult to accomplish because of the decline in revenue and the tight supply of money in lenders' portfolios. When the times were good, hotel buyers were able to obtain 80% to 85% loan-to-value on hotel transactions.

A year later, all that has changed as lenders have become more conservative. What was once 85% LTV is now 65% LTV. Lenders are tightening their lending guidelines, requiring additional working capital and escrowing funds for property improvements. The hotel industry seemed immune from the subprime mortgage mess, and we did not believe it would have a great affect on hotel transactions. But as the crisis deepens, obtaining financing is becoming more and more difficult, and the pace of the transactions has slowed down tremendously.

In order to find a suitable buyer in this market, sellers need to realize that the cap rates have to go up. When cap rates go up, room values will adjust down and room multiples will decrease.

At this time, hotel investors are staying put, watching the market and waiting for good bargains. 10-31 exchange transactions have also decreased due to the lack of good investment opportunities. Now, investors prefer to pay capital gain taxes rather than jumping into an investment and watching it diminish in value. While taxes are at their lowest in years (15%), and with the elections around the corner, investors prefer to take advantage and cash in on their long-term gains before the expiration of the tax laws in 2010.

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