



By Rick Swig

## Operators Will Face Many Challenges As Economy Continues on Downswing

**CLEARLY THERE IS A DISTINCT SHIFT OCCURRING** in the US economy. For the hotel industry, several issues, real and psychological, have emerged that could impact operations and real estate. The combination of failing housing values, weaker consumer finances and the \$4-a-gallon gas prices will certainly have a real impact on travel. Additionally, there may be a knee-jerk reaction of corporate restrictions on travel and meetings, even though there may be no definitive business trend to justify those limits.

In the first quarter, revenue performance was not significantly impressive one way or another. New supply did outweigh added demand, but the ratios nearly offset each other, while room rate growth was generally in a favorable range of 4% to 5%. This is clearly not the end of the boom

be yielding more than last year, yet the asset's market value is significantly less. Owners will either become longer-term holders or take deep discounts on their property sales.

As the economy stagnates, hotel operators must avoid reactive panic tactics, such as exaggerated room rate discounting. This will only further undermine the valuation and cash flow integrity of their properties. The combination of inexperienced revenue managers, automated revenue-management tools and the pressure to meet RevPAR budgets could lead operators to reduce room rates, a phenomenon that was prevalent in the early part of this decade. While some will point to their "success" of gaining market share through room rate incentives, no one can argue the fact that those tactics gutted the overall revenue potential of most hotel markets, particularly during the period of stabilization that occurred after the downturn in 2001.

If revenue declines do occur, owners will find themselves at odds with brands in respect to service and product standards. The brands were banking on continued growth in the hotel segment to improve general product standards and competitive positioning. The requirement for significant physical product and labor-intensive service enhancements now will be fought by owners with reduced financial means to accomplish those initiatives. It is important to remember that the ample financing that drove significant transaction activity during the past five years also underwrote a substantial portion of physical improvements that were well outside of traditional replacement reserve guidelines of 3% to 5% of annual gross revenues.

Certainly, these issues only scratch the surface. Other considerations include an industry alliance to address federal government barriers for incoming international travelers, the availability of qualified human resources for hotel industry workforces and operational expense trends out of alignment with revenue growth. In time, each of these will have to be addressed to enable successful hotel operations and investment stabilization. ♦

*The views expressed in this article are those of the author and not Real Estate Media or its publications.*

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cycle, but the lodging sector is not immune.

Possible job cuts, plant closures and other traditional recessionary corporate tactics certainly present a challenge for travelers who now are re-evaluating their plans for get-away weekends or summer vacations. The traveling public, as they have in previous economic downturns, will become more conservative in their discretionary travel spending.

Yet broad-brush commentary may be misleading without a segregated review of all segments. Evaluations must be based on comparisons between various industries and tourism segments, such as domestic and international, as well as geographic territories, either regional or defined by urban and suburban. Not all hotel locations are influenced equally.

The most dynamic impact has been felt in hotel sales, although there have been few significant transactions since August 2007. The combination of revised loan pricing, restrictive lending rules and a general lack of credit has brought the market to a screeching halt. While hotel performance has not waned significantly, pricing or valuations of assets have slipped dramatically. This has left owners more confused than ever about how their operations can