Hotel News Resource

What If The Naysayers Are Right? U.S. Hotels Could Lose 6.1 Percent In Revenue

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A recently released analysis by PKF Hospitality Research (PKF-HR) found that if an economic recession were to occur in the United States during 2008 - 2009, it would result in a 6.1 percent decline in rooms revenue for the U.S. lodging industry through 2010.

With all the rumblings of a potential decline in the nation's economy, PKF-HR felt it important to conduct a special econometric analysis that measured the impact a hypothetical economic recession would have on U.S. hotels.

'We do not anticipate a near-term economic recession, but some industry participants are beginning to worry since times have been so good for so long,' said Mark Woodworth, president of PKF Hospitality Research. 'Our current forecast without a recession calls for a compound annual growth rate of 5.5 percent in RevPAR for the typical U.S. hotel during the next three years. However, should the unexpected happen and economic indicators such as gross domestic product, employment, and real personal income slow down or decline, then the average U.S. hotel is forecast to achieve annual RevPAR growth of just 2.0 percent through 2010.'

This special recession analysis was made in conjunction with the release of PKF-HR's latest national Hotel Horizon forecast. Each quarter, PKF-HR produces Hotel Horizon reports for six national chain-scale segments and 50 major markets across the country. Each report contains a five-year econometric forecast of supply, demand, occupancy, ADR and RevPAR.

A Hypothetical Recession

'Since we are not forecasting a recession, we analyzed the economic indicators from the last two downturns to simulate a future economic recession,' Woodworth noted. The last two U.S. economic downturns occurred from 1990 to 1991 and 2000 to 2001. During these two periods, annual GDP change averaged 1.4 percent. Concurrently, employment declined 0.2 percent and real personal incomes increased 0.8 percent. For reference purposes, PKF-HR's current outlook for the U.S. lodging industry is based on average annual GDP growth of 2.9 percent, employment gains of 3.0 percent, and real personal income increases of 1.1 percent from 2008 through 2010. PKF-HR uses Moody's economy.com as its source for economic forecast data.

'Our analysis of the historical relationship between hotel performance and the nation's economy found that lodging demand closely follows the downward movement of GDP during economic recessions,' observed Woodworth. Therefore, when we simulate an economic recession that has a trough in 2009, we foresee most of the fall off in lodging industry performance to occur that same year.'

What Will Likely Happen

Using the baseline economic forecast provided by Moody's economy.com, which assumes no economic recession, PKF-HR is forecasting the U.S. lodging industry will achieve average annual RevPAR growth of 5.5 percent from 2007 through 2010. This is substantially greater than the long term annual average of 3.3 percent.

'Given where we are in the lodging industry cycle, it is not surprising that ADR growth will be the main driver of RevPAR growth the next few years,' said Woodworth. We continue to be impressed with the ability of hotel managers to raise the contract rates for their big corporate accounts, as well as take advantage of the negotiating leverage they possess with meeting planners.

'Many people are worrying about the record volume of new hotel projects in the development pipeline. However, given the current costs of construction, lending environment and investor expectations, we believe the growth in demand for hotel accommodations will absorb most of the new supply. Therefore, we are only forecasting slight declines in occupancy in 2007 and 2008.'

What May Happen

In the event of an economic recession that parallels the previous two national downturns, the U.S. lodging industry could lose an estimated 6.1 percent in revenue. This is the result of 2.2 percent fewer occupied rooms and the inability to raise room rates as aggressively because of more competitive market conditions. 'Using our pessimistic economic assumptions, the hypothetical loss in lodging industry revenue would mostly be the result of a drop in occupancy, not a decline in ADR,' explained Woodworth.

'Prior to the industry recessions of the early 1990s and 2000s, we observed a big run up in supply,' noted John (Jack) B. Corgel, Ph.D., the Robert C. Baker Professor of Real Estate at the Cornell University Hotel School and senior advisor to PKF Hospitality Research. 'Given the relatively slow growth in supply seen since 2002, plus the current disciplined financing environment, an economic recession would result in a slowdown of the progression of proposed hotel projects through the development pipeline.' Under PKF-HR's recession scenario, an estimated 66,000 fewer rooms will be built during the next three years.

PKF-HR believes hotel management's recent ability to practice yield management and drive room rates above expectations will bode them well through an upcoming recession. 'During our recession scenario, we believe U.S. hotel room rates will continue to grow,' said Woodworth. 'However, the growth will be less than the pace of inflation and roughly 2.6 percentage points less than our expected pace of ADR growth.'

An economic recession will have varying degrees of impact on the major segments of the lodging industry. Woodworth comments, 'History has proven that the hotels that are most vulnerable to a decline in utilization are those that are already lagging in performance. Given the recent sub-par results of midscale with food and beverage properties, we would be most concerned about this chain-scale segment if a recession were to occur.

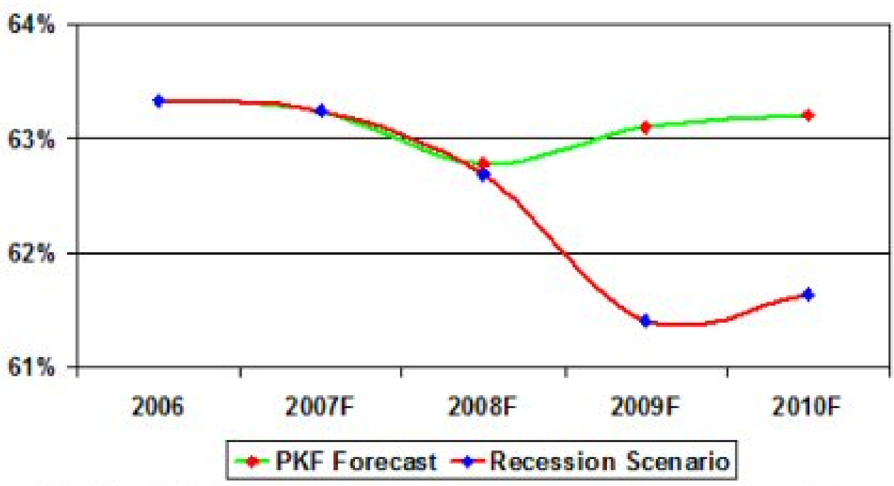
'It needs to be emphasized that PKF-HR is not forecasting an economic recession. However, we are always assisting our clients to prepare for possible future economic conditions.'

U.S. Hotel Industry
The Impact Of A Hypothetical Recession
on the U.S. Lodging Industry

	Occupancy			Average Daily Rate			Revenue per Available Room		
Year	Expected Case	Recession Scenario	Difference in Forecast Performance	Expected Case	Recession Scenario	Difference in Forecast Performance	Expected Case	Recession Scenario	Difference in Forecast Performance
2008	62.8%	62.7%	-0.1%	$ 109.01	$ 108.80	-0.2%	$ 68.44	$ 68.20	-0.3%
2009	63.1%	61.4%	-1.7%	$ 115.01	$ 110.55	-3.9%	$ 72.56	$ 67.88	-6.5%
2010	63.2%	61.6%	-1.6%	$ 121.68	$ 112.83	-7.3%	$ 76.90	$ 69.55	-9.6%

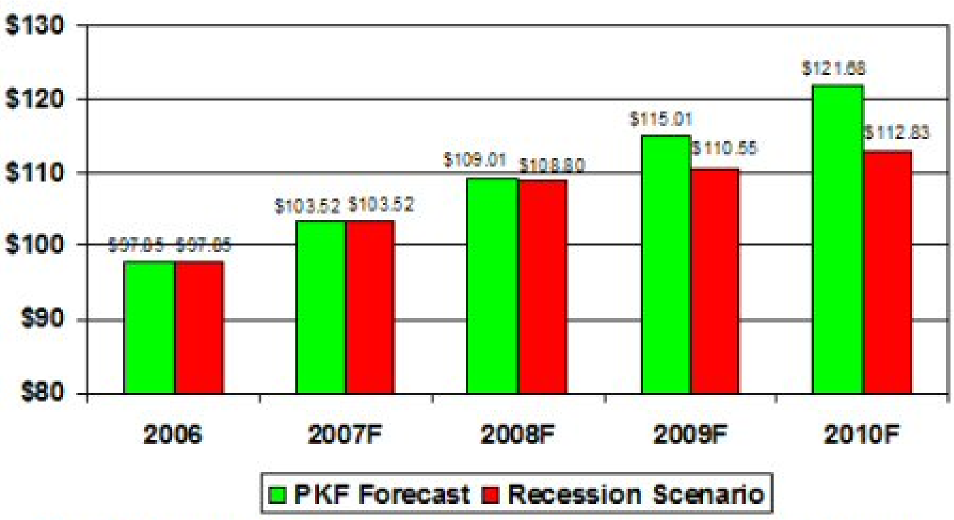
Source: PKF Hospitality Research

U.S. Hotel Industry
Forecast Occupancy Levels - 2006 to 2010
All U.S. Hotels



Note: * Hypothetical scenario - Based on average of two previous U.S. economic recessions
Source: PKF Hospitality Research (STR – Historical)

U.S. Hotel Industry
Forecast ADR - 2006 to 2010
All U.S. Hotels



Note: * Hypothetical scenario - Based on average of two previous U.S. economic recessions
Source: PKF Hospitality Research (STR – Historical)

To purchase a copy of the November 2007 Hotel Horizons report for the United States, please visit the firm's online store at www.pkfc.com/store, or call (866) 842-8754.

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