

## Rising Inflation and Threats of a Recession: Should U.S. Hoteliers Be Worried?

2008-01-31

---

Declining U.S. hotel occupancy levels should be more than offset by rising room rates in 2008 according to PKF Hospitality Research (PKF-HR). Given the recent dour economic news and talk of a potential recession, PKF-HR analyzed the historical relationships between key economic indicators and the performance of the U.S. lodging industry during times of economic stress. While a slowdown in Gross Domestic Product (GDP) growth may lead to moderation of increased demand for hotel rooms, a surge in inflation should allow hotel managers to boost their room rates.

"When economic activity slows down and corporate profits begin to waver, one of the first expense items to get scrutinized is the company's travel budget," said Mark Woodworth, president of PKF Hospitality Research. "Historically, we have observed a softening of corporate and group travel as the most immediate reaction to the threat of a recession. We believe this trend will repeat itself in the first half of 2008.

"Leisure travel, on the other hand, tends to remain fairly constant. People may alter their personal travel plans in search of more modest accommodations, but they still want to take their vacations," Woodworth noted. "Despite the resilience of leisure travel, overall, we expect that 50 percent of the 50 major cities we track will experience an occupancy decline in 2008 and 2009."

According to Moody's Economy.com's January 10, 2008 forecast, the pace of GDP growth is expected to slow down to a 2.2 percent annual rate in 2008, but the Consumer Price Index (CPI) forecast has been adjusted upward to a 2.6 percent annual rate. A rise in inflation has both a positive and negative affect on lodging performance.

"Unlike other forms of real estate, hotel price movements are not restricted by long-term lease agreements. Hotel managers have the ability to adjust their room rates much more quickly in response to an increase in inflation, and they have done so in the past," Woodworth observed. For 2008, PKF-HR is forecasting room rates to rise 5.6 percent, a full three points above the expected pace of inflation.

"On the flip side, a rise in inflation leads to an increase in operating costs," Woodworth said. Due to heavy labor requirements and relatively low levels of automation, hotels have not enjoyed the productivity enhancements experienced by other industries. Hotel operating costs typically outpace the rate of inflation. "We reiterate our guidance about closely monitoring operating expenses in order to retain profitability in 2008."

PKF-HR's projections for the hotel industry are based on its proprietary econometric forecasting model. The model utilizes historical lodging data from Smith Travel Research and economic forecasts from Moody's Economy.com. As of January 10, 2008 Moody's Economy.com was projecting a slowdown in U.S. economic activity, but the probability of a recession was only 14 percent.

"What will keep the economy buoyant, as well as the lodging industry, is the continued growth in employment. Historically, we have seen a strong correlation between changes in employment and lodging demand," Woodworth observed.

"If the nation's economy does fall into a recession, then history says that we could experience an actual decline in lodging demand. If this occurs, then the resulting competitive market conditions could force hoteliers to discount, or even cut, their room rates. Our current 4.6 percent forecast of RevPAR growth for 2008 would most likely be reduced," Woodworth said.

Reductions in demand and ADR are rare. Since 1988, the national ADR has declined from the prior year just twice. Same for total U.S. lodging demand. The only time demand and ADR both declined in the same year was 2001.

"Given the depressing economic news, I understand why hotel owners, operators, investors, and lenders are all very concerned. Fortunately, the financial foundation for most U.S. lodging industry assets is much stronger today than it has been when entering historical recessionary periods. Therefore, we believe the industry is in a much better position to endure the expected economic slowdown," Woodworth concluded.

This article comes from Hotel News Resource

<http://www.hotelnewsresource.com>

The URL for this story is:

<http://www.hotelnewsresource.com/article31003.html>

© 1998 - 2008 Nevistas and the author.

Brought to you by Hotel News Resource

*Distribute your news on our Network*

See what all the buzz is about at:

[http://www.hotelnewsresource.com/Info-news\\_account\\_info.html](http://www.hotelnewsresource.com/Info-news_account_info.html)