

Hospitality Vision US Performance Review



The US Lodging Industry Stumbles

The global economy went through some turbulent times during 2008. Across the globe, financial institutions collapsed, were acquired or re-capitalized by governments. Stock markets plummeted and some governments, including the United Kingdom (UK) and United States of America (US) organized rescue packages to save their failing financial systems. There was also a dramatic rise in inflation across the world in early 2008, with the UK, Euro zone and US seeing rates rising to levels last seen in the early 1990's. By year end however, the threat of deflation had become the greater concern, as the sharp slowdown in global economic activity brought numerous commodity prices down from their lofty highs. Financial market de-leveraging helped create a crisis in confidence in the final quarter of the year, with both individuals and corporations sharply cutting back spending on numerous categories, including travel and leisure.

It was not all doom and gloom for the industry in 2008. In March, the Open Skies agreement enabled airlines from the US and EU to fly to and from any point in the US and any point in the EU. Additionally, stronger spending by international visitors throughout the year helped offset the weakness from domestic travelers. And, despite the weakening economy, aggressive cost cutting in the lodging industry throughout 2008 has reportedly helped margins.

In early 2009, industry representatives have been preparing recommendations to present to President Obama, particularly with regard to attracting overseas visitors. In developing these recommendations, the US Travel Association noted that the industry employs one out of every eight US workers, drives more than \$700 billion in spending, and is a major economic force in each of the 50 states.

Economic meltdown knocks tourism

The global tourism industry saw a significant slowdown in most world regions in 2008 – particularly in the final quarter – as the economic meltdown trickled through and impacted the number of tourists and business travelers making trips and staying in hotels. However, unlike previous historic events that hurt the hotel industry – such as September 11, 2001 and SARS – the unprecedented economic climate is expected to last longer than either of those events, which creates the potential for even greater damage.

In the US, tourism continued to soften as 2008 progressed. The US Bureau of Economic Analysis has been reporting slowing gains in travel and tourism spending. In the third quarter, total spending was up a mere 0.4% from the prior three-month period. After adjusting for inflation, spending was down a hefty 8.1%. Sharp increases in third-quarter airline fares were largely the cause of the decline. Most other sectors, including accommodations, also experienced weakness in real terms.

Strong spending by international tourists in the US helped the US tourism industry, although the gains became less robust in the second half of 2008. In September 2008, for example, visitors spent \$12.4 billion, an increase of 16% over September 2007. In contrast, spending in the first four months of 2008 was up 23% from the first four months of 2007. Spending from nonresidents in the US, however, represents only about 12% of total US travel and tourism expenditures, according to the US Bureau of Economic Analysis. The remaining 88% is spent by US residents travelling for leisure or business.



While figures for travel-related spending in the final three months of 2008 were not available at the time this report was written, preliminary data suggest a sharp worsening, particularly in travel from US residents. The deterioration in the financial and employment markets in the fourth quarter left many consumers reeling. As a result, confidence tumbled and consumers cut back sharply on all types of spending.

The Conference Board, a global independent membership organization reported that its Consumer Confidence Index, which declined through most of 2008, fell to an all-time low in December. Nonauto retail sales in December recorded the biggest drop since record-keeping began in 1992, according to the Commerce Department.

Relative to travel, international passenger traffic for North American carriers dropped 4.8% in November. The number of visitors to Las Vegas was down 9.8% in November from a year earlier according to the Las Vegas Convention and Visitors Authority. And occupancy in the US hotel industry in November was down 10.6% from November 2007, according to Smith Travel Research (STR).

Further, year-to-November 2008 revenue per available room (revPAR) in the US reportedly fell 1.3% compared with the first 11 months of 2007. This decline was driven primarily by a 4% drop in occupancy to 61.8%. In contrast, average room rates rose \$3 to \$107, according to recent data from STR. Although most cities in the US reported declines in revPAR, as can be seen in Table 1, each city has a different tale to tell.

Looking ahead, spending among travelers, already lower due to economic factors, may well remain miserly in 2009. In particular, cost will be a significant factor for corporate travelers in 2009, and those once flying in business class will likely downgrade to economy, while the hotel suite guest may settle for something less luxurious.

According to the International Air Transport Association, global passenger traffic is expected to slow further in 2009, down 3%, representing the first annual decline since 2001. It expects industry revenue to decline 6.5% this year.



Most analysts expect that it will take until 2010 before the industry experiences a rebound. Travel-related spending should eventually see a boost from lower oil prices, which will bring transportation costs down. And the current pullback in hotel construction should eventually help align supply with demand.

Table 1 – Hotel performance in key US cities: year-to-November 2008 versus year-to-November 2007

	Occupancy, %			Average Room Rates, \$			RevPAR, \$		
	2008	2007	% change	2008	2007	% change	2008	2007	% change
Total United States*	61.8	64.4	-4.0	107	104	2.8	66	67	-1.3
Anaheim-Santa Ana, CA	69.9	73.1	-4.5	124	122	1.0	86	90	-3.6
Atlanta, GA	60.2	64.4	-6.5	92	90	1.7	55	58	-4.9
Boston, MA	68.3	70.3	-2.7	155	153	1.4	106	108	-1.4
Chicago, IL	65.2	69.2	-5.8	133	131	1.6	87	90	-4.2
Dallas, TX	60.3	61.3	-1.7	94	92	2.5	57	57	0.8
Denver, CO	65.0	67.3	-3.4	107	100	6.7	69	67	3.0
Detroit, MI	56.7	59.6	-4.8	87	85	2.3	50	51	-2.6
Fort Lauderdale, FL	66.1	67.4	-2.0	126	128	-1.3	83	86	-3.3
Houston, TX	68.3	66.9	2.1	101	92	9.6	69	61	11.9
Las Vegas, NV	87.1	91.0	-3.9	121	134	-9.5	NA	NA	NA
Los Angeles-Long Beach, CA	72.7	76.2	-4.7	129	124	4.5	94	94	-0.4
Miami-Hialeah, FL	72.1	72.5	-0.6	159	156	1.6	114	113	1.0
Minneapolis-St Paul, MN-WI	63.6	67.4	-5.7	103	98	4.8	66	66	-1.2
Nashville, TN	62.0	66.9	-7.3	96	91	5.5	59	61	-2.2
New Orleans, LA	64.0	58.3	9.7	119	117	1.6	76	68	11.5
New York, NY	82.4	83.7	-1.5	274	264	3.7	226	221	2.2
Norfolk-Virginia Beach, VA	56.8	62.4	-9.0	90	89	0.8	51	56	-8.2
Oahu Island, HI	75.5	77.1	-2.1	170	167	1.8	128	129	-0.4
Orlando, FL	66.3	68.6	-3.4	107	106	0.7	71	73	-2.7
Philadelphia, PA-NJ	67.0	70.7	-5.3	123	120	3.0	83	85	-2.5
Phoenix, AZ	60.8	68.2	-10.8	126	122	3.8	77	83	-7.4
San Diego, CA	71.6	74.7	-4.1	144	140	2.3	103	105	-1.9
San Francisco/San Mateo, CA	76.2	76.2	-0.1	157	150	5.3	120	114	5.2
Seattle, WA	70.0	73.2	-4.3	128	123	3.8	89	90	-0.7
St Louis, MO-IL	60.2	62.3	-3.3	88	86	2.3	53	53	-1.0
Tampa-St Petersburg, FL	58.0	62.5	-7.2	108	104	3.1	62	65	-4.3
Washington, DC-MD-VA	69.0	70.3	-1.8	154	151	2.4	107	106	0.5

*Excludes Las Vegas

Source: Smith Travel Research & Las Vegas Convention and Visitors Authority

Will Chicago win gold?

In President Obama's hometown of Chicago, year-to-November 2008 saw revPAR fall 4.2% to \$87 – however with Obama's historic win the city hopes to see an influx in tourist arrivals in 2009 which should help boost hotel performance. Year-to-date 2008 occupancy fell to 65.2%, while average room rates rose 1.6% to \$133.

In April 2007, the city was selected as the US Bid City for the 2016 Olympic and Paralympic Games and will compete with other international cities to become the official host city. If Chicago secures its place as host of the 2016 Olympic Games, it will be a great achievement for the city and further its standing in global tourism arena.

Already one of North America's busiest airports – with 59.7 million passenger arrivals year-to-October 2008 – Chicago O'Hare International Airport is undergoing extensive refurbishment which is due to be completed by 2013. The expansion plans include a new terminal, and additional gates and parking facilities which will be a welcome boost should the city secure its bid as Olympic host city in 2016. A number of new hotels, including the InterContinental Chicago, the Mandarin Oriental Chicago and the JW Marriott Chicago Downtown, are due to open over the next two years which will help the city's Olympic bid.

Dallas attracts business travelers

In Dallas, occupancy fell 1.7% year-to-November 2008 to just above 60%. This was offset by a 2.5% rise in average room rates to \$94. As a result, the area experienced a marginal increase in revPAR of 0.8%. With an eye toward attracting more business travelers, Dallas is considering investing in convention center space to host meetings and conferences. The city will also receive a boost as President George W. Bush sets up an office in the area and begins planning for his presidential library at a nearby university.

Fort Lauderdale softens

Fort Lauderdale saw revPAR decline 3.3% year-to-November 2008. As occupancy fell 2.0% to 66.1%, average room rates in the city lost \$2 compared to 2007, to settle at \$126. The decline in revPAR was the seventh-worst of the cities followed by STR. The local economy remains impacted by falling real estate prices and the softening in tourist activity. According to the Office



of Federal Housing Enterprise Oversight (OFHEO), Fort Lauderdale home prices declined a sharp 18% year-over-year in the second quarter of 2008. This represented the fourth consecutive quarterly decline. Employment in Fort Lauderdale continues to weaken; it was down nearly 3% in November 2008 from a year earlier. In 2008, flights into Fort Lauderdale reportedly were pared back by several major airlines as a result of higher jet fuel prices.

Houston reports double-digit revPAR growth

Houston was one of only two US cities to report double-digit revPAR growth year-to-November 2008, gaining 11.9%. Occupancy rose to 68.3% from 66.9%. Average room rates rose 9.6 % to \$101.

Houston is the fourth largest and most populous city in the nation (trailing New York, Los Angeles and Chicago). More than 38 million people each year fly in and out of Houston's two major airports: Bush Intercontinental and William P. Hobby. Houston is also home to the Houston Livestock Show and Rodeo, the largest rodeo in the world, attracting more than 1.8 million visitors per year.

Houston's relatively healthy regional economy is likely helping hotel demand. Employment has continued to grow in 2008 and home foreclosures remain low. STR has reported that 39 hotels opened in Houston in the year-to-November.

Safe bets in Las Vegas?

Las Vegas has seen a dramatic fall in gaming revenue year-to-November 2008. On the Las Vegas strip, gaming revenue was down 9.3%¹ to \$5.6 billion compared with the same period last year according to the Las Vegas Convention and Visitors Authority. It is not surprising therefore that hotel performance has in turn been affected, with occupancy falling to 87.1% year-to-November 2008. Average room rates plummeted 9.5% to \$121 - \$13 less than the similar 2007 figure.



Las Vegas' McCarran International Airport is ranked as the sixth busiest in North America in terms of passenger arrivals. Year-to-November 2008, the airport saw 40.9 million passengers pass through its terminals. By 2017 the airport is expected to reach capacity and as a result, a new \$2.4 billion terminal is under construction and due to open in 2012.

Oversupply could dampen the City of Angels

RevPAR remained relatively stable in Los Angeles year-to-November 2008 as a 4.7% decline in occupancy was counterbalanced by a 4.5% rise in average room rates. The city took fifth position in terms of occupancy, at 72.7%. Average room rates stood at \$129 compared with \$124 in the same period in 2007. Los Angeles' Mediterranean-type

climate continues to make it a popular travel destination. The recent opening of a new crop of luxury hotels suggests the city is resistant to economic challenges. Among the new luxury hotels that opened in 2008 were the 297-room SLS Hotel at Beverly Hills and the 201-room Montage Beverly Hills. Hyatt International opened its luxury Andaz hotel brand that includes art installations throughout the property. Furthermore, several older hotels in Los Angeles received multimillion-dollar upgrades, enabling them to charge higher room rates. These new hotels and upgrades were clearly planned to meet the growing demand for more and better rooms in the city.

These new hotels, planned in a booming era, now stand in contrast to today's global economic challenges. Domestic and international arrivals to LA's major airport hub, Los Angeles International Airport (LAX), suggest tough times ahead. Year-to-September total traffic at LAX was down 2.1%. Additionally, passenger traffic at LA Ontario International (LA/ONT) dropped year over year by 25.9% this past September.

Will the sun shine in Miami?

Hotels in Miami took sixth place in terms of occupancy. The year-to-November 2008 rate was 72.1%, representing a marginal decline from the 2007 figure. With \$3 added to average room rates, revPAR grew 1%. Although the domestic market fell during the summer of 2008, the city, like several other major metropolitan areas, benefited from international travelers – particularly from Europe and South America – as a result of the weak dollar.

While Miami at year-end was affected by the economic downturn, the falloff in occupancy is also partly due to an increase in hotel supply. During the third quarter of 2008, in Miami Beach alone, the Fontainebleau and Eden Roc returned more than 1,000 rooms to the market after extensive renovations, The Epic brought another 400 rooms to downtown Miami during December. Approximately 4,400 rooms were added during 2008 and another 5,000 are expected in 2009 and 2010.

¹ LVCVA.com



Unfortunately the year ahead does not look promising, and recent analysis by PKF found that out of the 50 top US markets, five of the seven markets expected to see the largest declines in revPAR during 2009 are in Florida including Miami, Orlando, West Palm Beach, and Tampa. The other two will be in Oahu, Hawaii and Phoenix, Arizona.

New Orleans continues to recover

New Orleans was one of only two US cities to report double-digit revPAR growth. Year-to-November 2008 revPAR was up 11.5%. Occupancy rose to 64% from 58%. Average room rates rose 1.6 % to \$119.

In October 2008, the city's football team played one of its games in London against the San Diego Chargers as part of a week-long promotion to encourage Britons to visit and invest in New Orleans after Hurricane Katrina devastated the city in 2005. In addition to the football game, the organizers hosted a mini-Mardi Gras for Londoners to sample New Orleans culture.

Strong tourist demand boosts New York City

New York City, is ranked as the top US city to visit by Global Insight, an economic and financial analysis and forecasting company. It is home to many entertainment, financial, fashion and performing art companies. With its mixture of cultures, it appeals to international travelers, offering access to world class museums, entertainment, and fine dining.

Attracting 47 million visitors both international and domestic from a broad demographic - beating the prior year by one million visitors - it is not surprising that the city managed to achieve strong results. Year-to-November 2008, it took the top position in terms of average room rates and revPAR. Even though occupancy declined from the prior year, it still achieved an impressive 82.4% rate, taking second place after Las Vegas, which reached 87.1%. Average room rates in New York rose 3.7% to reach \$274.

In October 2007, a \$30 million global marketing campaign was launched called "This is New York City." The campaign hopes to raise annual visitor numbers from 47 million in 2008 to 50 million by 2015. Further, in November 2008, the US Department of Homeland Security allowed citizens of South Korea and six Eastern European countries (including Czech Republic, Hungary, Estonia, Latvia, Lithuania and Slovakia) to enter the US without a visa. The Visa Waiver Program (VWP) may be a welcome boost to help the city achieve its tourism targets.

As a result of the slowing global economy, New York City Mayor Michael Bloomberg predicted that 2009 would be a tougher year for New York City tourism; hotel occupancy rates had already started to fall at year-end. International tourist arrivals have also started to slow. This is especially troubling because international visitors generally tend to stay longer and spend more. While New York City is not exempt from the current economic slowdown, the city is expected to remain a popular destination in 2009, relative to other major US cities.

Occupancy suffers in Orlando²

In Orlando, Florida year-to-November 2008 saw revPAR in negative territory. Occupancy fell 3.4% to 66.3% compared with the same 11 months of 2007. However average room rates rose 0.7% to \$107, resulting in an overall revPAR decline of 2.7%.

Three out of the four Florida markets followed by STR have reported revPAR declines for the year to date. Only Miami has managed to hold on to positive territory, albeit barely with its 1.0% increase.

² Orlando hotel occupancy, revPAR and ARR numbers do not include Walt Disney World Hotels & Resorts

One of the factors affecting Orlando's decline in occupancy is a reduction in airline capacity. In 2008, many airlines cut flights and increased fares as a result of higher fuel costs and lower airline bookings. This, coupled with an increase in hotel supply, has led to softening hotel performance in Orlando. In November 2008, occupancy fell a shocking 15.2% for the month, one of the sharpest drops across the US.

As with other Florida cities, the local travel industry is being impacted by weakened domestic and international travel demand. Orange County (which includes the city of Orlando) saw its hotel-tax collections drop 13% in November as a result of the sharp pullback in travel. It was the sixth consecutive month that tax collections declined. The city, however, is constructing a new basketball arena and performing-arts center in its downtown, which should eventually help hotel demand.

Favorable exchange rates benefit San Francisco

San Francisco reported the third-highest occupancy in the US year-to-November 2008 at 76.2% after Las Vegas and New York. It also reported the third-highest revPAR at \$120, not including Las Vegas. Average room rate increases drove most of San Francisco's revPAR growth.

San Francisco has benefited from a favorable exchange rate as the weak dollar offered greater value for Asians traveling to the US. Although some industries see the weak dollar as being detrimental to their businesses, hoteliers have been cashing in as eager shoppers flock to the US.

In October 2008, the Mayor of San Francisco announced that a Tourism Improvement District would be a key part of his economic stimulus package. The district could generate \$27 million in the first year and would include a \$9 million upgrade to the Moscone Center, with almost \$18 million being spent promoting and marketing the city and its hotels.

Celebrations in Washington DC

Hotels in Washington DC reported a marginal increase in revPAR year-to-November 2008, rising just 0.5% to \$107 – the fifth highest revPAR across the US. Occupancy fell below 70% while average room rates rose 2.4% to \$154. Several million visitors were expected during the 2009 Presidential inauguration of Barack Obama on January 20th, and many hotels offered special packages during the four-day celebration. The celebrations were a welcome boost to the city's economy, as many hotels held special events which required a significant number of catering. Hotel performance likely benefited from the celebrations.

Tough times ahead

While 2009 is expected to be a tough year for global tourism and business travel, the US lodging sector is likely to return to growth in 2010. According to STR, hotels in the US will see an overall revPAR decline of 2.5% in 2009, and occupancy will dip to 59.1% - the lowest levels since 2003. Average room rates should see marginal improvements to close the year at \$108, according to STR.

Longer term, growth in employment, improvements in corporate profitability, a better supply/demand balance helped by slowing new construction, and gains in consumer net worth will likely add to the demand for lodging. Any drop in airfares, mostly from lower energy prices, should also help the industry.



Hoteliers are likely aware today that slashing rates to bring in additional business is not beneficial in the long term, since it takes average room rates much longer to recover than occupancy levels. Instead, some hotels are offering price incentives such as free meals or spa treatments to attract business. The current tough economic environment, however, is making it difficult for companies to avoid lowering prices.

Despite the current economic challenges, the US lodging industry is likely to continue to benefit longer term from the rising incomes being experienced in much of the developing world. Planning today for the upcoming changes in technology, demographics and societal concerns that may impact the lodging industry may help companies thrive in the years ahead.



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