



HOTEL & LEISURE ADVISORS

Washington, D.C. Lodging Market's Resiliency & Outlook

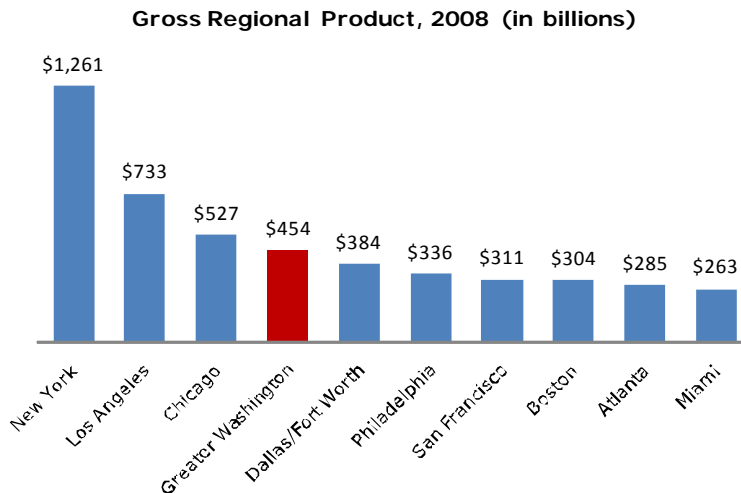
By Thomas E. Lewerenz

Introduction

Hotel markets are largely affected by both macro and micro economic factors. However, the Washington, D.C. hotel market is somewhat unique because it includes the nation's capital, which lends itself to many benefits. Most importantly, this hotel market is more resistant to economic recession than other U.S. metropolitan markets. Its international status contributes significantly to both leisure and group demand. Washington, D.C. is home to the federal government, and the private sector is closely aligned with the business of the federal government, which is an economic anchor to the market. As a result, the lodging market enjoys a consistent base of demand.

Economy

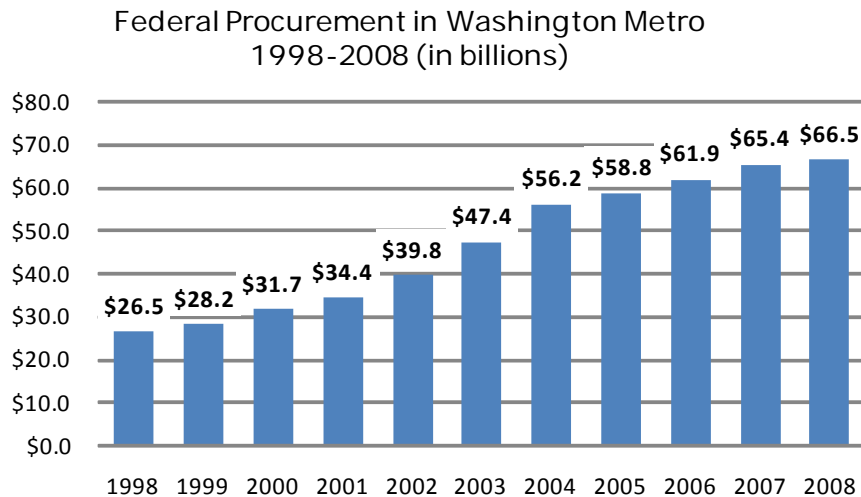
The Washington Metropolitan Area is the fourth largest in the U.S. with a \$454 billion Gross Regional Product (GRP). Additionally, the Washington Metropolitan Area's economy ranked fifth globally for Gross Domestic Product (GDP) per capita in 2008, which led all major U.S. metropolitan markets (World Knowledge Competitive Index).



Source: GMU Center for Regional Analysis

As the nation's capital, domestic and international political activities abound. Many of these activities contribute significantly to the economic fabric of the area, thus creating a diversified base of demand generators for hotels. Business, tourism, and conventions thrive.

The metro area's economy is anchored by the federal government. It influences the area in a myriad of different ways. One of the more direct and quantifiable means is through procurement. The following graph illustrates the billions of dollars injected into the metropolitan economy.



Source: US Census Consolidated Federal Funds Reports, GMU Center for Regional Analysis

Federal procurement to the Washington Metropolitan area leads the nation. According to recent data, this area received approximately \$20 billion more than California (ranked second).

Currently, however, the U.S. and metro area find themselves within a global recession. According to data from the George Mason University (GMU) Center for Regional Analysis, the metro's economy appears resilient. From 1990 to 2008, its GRP compound annual growth rate (CAGR) has been 3.7%, but the area's economy likely saw negative growth in 2009.

In comparison, the region has performed better than the U.S., most notably since 2008. According to the U.S. Bureau of Labor Statistics in its January 2010 preliminary report, 99 of the nation's largest 100 labor markets in the U.S. lost jobs in 2009. The Washington-Arlington-Alexandria market lost 15,700 jobs, which equates to a -0.5% change, resulting in an unemployment rate of 6.2%. Of the five markets that lost more than 100,000 jobs in 2009, the largest drop was Chicago (182,300), followed by Los Angeles, New York City, Detroit, and Atlanta.

The Metropolitan Washington Council of Governments stated in its *Growth Trends to 2030 Newsletter* that "Two-thirds of all new jobs [Washington Metropolitan Area] are anticipated in service industries such as engineering, computer and data processing, business services, and medical research" which will require hotel accommodations. Similarly, IHS Global Insight forecasts positive growth. Its economic experts believe that the Washington Metropolitan Area's GRP will increase by \$558 billion between 2009 and 2014, which equates to 4.1% CAGR.

Hotel Performance

The Washington, D.C. hotel market, as defined by Smith Travel Research, is comprised of 10 tracts totaling 654 hotels and 101,536 total rooms.

Submarket	Upper-Priced Rooms			Lower-Priced Rooms			Total		
	Properties	Rooms	Market	Properties	Rooms	Market	Properties	Rooms	Market
District of Columbia	92	24,930	24.6%	23	2,429	2.4%	115	27,359	26.9%
Bethesda-Silver Spring	22	4,417	4.4%	19	1,595	1.6%	41	6,012	5.9%
Arlington	29	8,850	8.7%	13	1,230	1.2%	42	10,080	9.9%
Alexandria	26	5,051	5.0%	25	2,745	2.7%	51	7,796	7.7%
Fairfax/Tysons Corner	28	6,334	6.2%	19	1,865	1.8%	47	8,199	8.1%
I-95 Fredericksburg	23	2,580	2.5%	55	4,350	4.3%	78	6,930	6.8%
Dulles Airport Area	35	6,907	6.8%	25	2,812	2.8%	60	9,719	9.6%
Frederick/Rockville	25	4,663	4.6%	30	3,005	3.0%	55	7,668	7.6%
Suburban Maryland	27	5,892	5.8%	49	4,074	4.0%	76	9,966	9.8%
Suburban Virginia	25	3,692	3.6%	64	4,115	4.1%	89	7,807	7.7%
Total	332	73,316	72.2%	322	28,220	27.8%	654	101,536	100.0%

Source: PKF Hospitality Research *Hotel Horizons*, Smith Travel Research

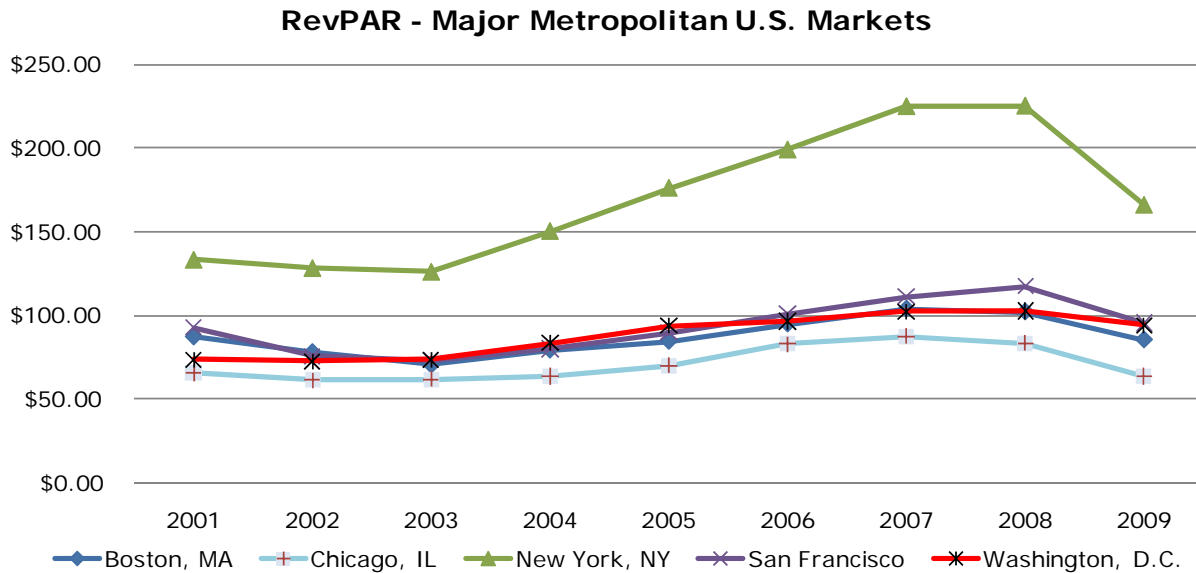
As illustrated in the table above, the greatest concentration of hotel rooms is within the District. Upper-Priced rooms realized an average daily rate (ADR) of \$176.07 while lower-priced rooms achieved an ADR of \$95.67.

The table below compares the Washington, D.C. hotel market to other major metropolitan areas. It illustrates the benefits of the diverse economy in the Washington, D.C. Metropolitan Area, as recorded by Smith Travel Research. Of the major metropolitan areas examined, the Washington, D.C. hotel market achieved the highest compound annual Revenue per Available Room (RevPAR) growth from 2001 to 2009 and was the only lodging market not to record a double-digit RevPAR decline between 2008 and 2009.

Occupancy	2001	2002	2003	2004	2005	2006	2007	2008	2009	CAGR	
										2001-2009	2005-2009
Boston, MA	64.5%	63.3%	60.4%	64.2%	65.3%	67.1%	68.4%	66.5%	62.2%	-0.5%	-1.2%
Chicago, IL	61.1	59.3	60.5	62.1	64.0	67.5	67.5	63.3	56.6	-1.0%	-3.0%
New York, NY	73.2	73.7	75.0	81.0	82.8	82.5	83.4	81.9	77.2	0.7%	-1.7%
San Francisco	65.3	61.3	62.8	68.0	71.6	73.0	75.1	75.3	71.6	1.2%	0.0%
Washington, D.C.	65.6	65.4	66.4	70.6	71.3	68.3	68.3	67.0	64.9	-0.1%	-2.3%
ADR	2001	2002	2003	2004	2005	2006	2007	2008	2009	CAGR	
Boston, MA	\$135.49	\$123.39	\$116.95	\$123.98	\$129.82	\$141.49	\$151.78	\$153.70	\$137.49	0.2%	1.4%
Chicago, IL	107.78	103.63	102.51	102.46	109.54	122.94	129.65	131.88	112.70	0.6%	0.7%
New York, NY	181.95	174.13	168.06	185.75	212.84	241.40	269.74	275.04	215.14	2.1%	0.3%
San Francisco	142.06	123.42	116.68	118.11	125.60	138.56	148.35	156.13	133.60	-0.8%	1.6%
Washington, D.C.	112.29	110.95	110.85	118.51	131.51	141.54	149.93	153.26	144.93	3.2%	2.5%
RevPAR	2001	2002	2003	2004	2005	2006	2007	2008	2009	CAGR	
Boston, MA	\$87.35	\$78.10	\$70.65	\$79.56	\$84.73	\$95.01	\$103.77	\$102.14	\$85.58	-0.3%	0.2%
Chicago, IL	65.83	61.45	61.99	63.58	70.15	82.92	87.54	83.47	63.75	-0.4%	-2.4%
New York, NY	133.27	128.33	126.11	150.46	176.21	199.04	224.93	225.24	166.11	2.8%	-1.5%
San Francisco	92.81	75.69	73.32	80.26	89.91	101.12	111.35	117.54	95.59	0.4%	1.5%
Washington, D.C.	73.72	72.61	73.61	83.68	93.79	96.71	102.44	102.73	94.04	3.1%	0.1%

Source: Smith Travel Research

The following graph demonstrates the underlying strength and consistency of the Washington, D.C. hotel market through its reduced RevPAR volatility.



The positive performance of the Washington Metropolitan Area illustrated in the preceding graphs is primarily related to the following:

- Industrial Sectors:** The top three employment sectors in the District and Metropolitan Area are Professional/Technical/Scientific Services, which includes consulting, accounting, engineering, and legal firms; Public Administration, much of this employment is attributable to various offices and agencies of the federal government; and, Health Care/Social Assistance, which includes major health care employers such as Washington Hospital Center and Children's Hospital NMC. A strong service sector, professional firms with national and international scopes, and government typically contribute to significant hotel demand.
- Office Space:** The metro's office market realized modest positive absorption (630,000 square feet in 2009 as compared to 3.4 million in 2008), as government, health care, and contractors associated with the federal government leased office space. Although the overall vacancy increased 240 basis points in 2009, it remains lower than most large metro areas due to the stabilizing influence of the federal government. In 2009 vacancies rose; consequently, rents declined 6.9%. Construction levels have declined, but they remain elevated at this point in the cycle – particularly in the District. Despite weak conditions, the metro area remains one of the top performing markets in the nation, according to Delta Associates.
- Federal Per Diem Hotel Room Rates:** The U.S. General Services Administration (GSA) sets lodging rates annually for each fiscal year (October 1 – September 30). Its goal is to match the average rates charged by mid-range hotels in each market, based upon the most recent full calendar year's Smith Travel Research data. In seasonal markets, multiple per diem rates are set. FY 2009 seasonal rates for the District and neighboring Maryland counties and Virginia cities and counties, ranged from \$165-\$233, which had been increased from \$154-\$201 in FY 2008. Given the recent hotel

rate discounting that occurred in the hotel industry, FY 2010 hotel per diems have been adjusted down slightly to \$170-\$229.

- Convention Center Demand:* The largest convention facility in the area is the Walter E. Washington Convention Center, located in downtown Washington, D.C. This facility, which first opened in 2004, covers six city blocks and 2.3 million square feet of total space. The Convention Center offers 700,000 square feet of exhibit space. The District hosted 15 citywide conventions in 2009, which attracted approximately 190,000 delegates, and 24 citywide conventions in 2008 with about 274,000 delegates. However, the stalled progress of the 1,167-room Marriott Convention Center Hotel has affected future bookings. The largest eight conventions booked for 2010 range in room nights from 19,700 to 40,800, but the number of citywide conventions is fewer than the previous year according to Destination DC, formerly known as the Washington, D.C. Convention & Tourism Corporation.
- Leisure Demand:* Tourism is a key component of the area's economy and lodging demand. In 2008, the District hosted 16.6 million visitors, a 3% increase from 2007. Domestic travel rose 2% to 15.2 million, while international visitation showed double-digit growth for the second straight year, rising 22% to 1.4 million. The District is the eighth-most visited American destination for international travelers. The Washington Metropolitan Area captured a greater percentage of all overseas visitors to the U.S. as market share increased from 5% to 6%, according to Destination DC.

New Supply & Pipeline

The total number of U.S. rooms in construction in December 2009 decreased by 47.4% from December 2008, to 97,302 rooms, according to STR/TWR/Dodge. The total active U.S. hotel development planned pipeline includes 303,788 rooms, which is a 29.0% decrease from December 2008. (Note: planned pipeline data includes projects in the planning and final planning stages).

Of the top 10 markets by rooms under construction, the Washington, D.C. hotel market ranks fourth.

Top 10 U.S. Markets by Rooms In Construction for 2009			
Region	Existing Supply (rooms)	In Construction (rooms)	In Construction (as % of Existing Supply)
New York, NY	92,327	11,618	12.60%
Houston, TX	69,402	3,854	5.60%
Dallas, TX	76,331	2,591	3.40%
Washington, D.C. - MD-VA	102,363	2,522	2.50%
Atlanta, GA	94,154	2,369	2.50%
LA-Long Beach, CA	96,682	1,877	1.90%
Orlando, FL	117,861	1,662	1.40%
Las Vegas, NV	163,555	1,321	0.80%
Seattle, WA	39,372	1,232	3.10%
Chicago, IL	108,600	1,203	1.10%

Source: STR/TWR/Dodge

Within the Washington, D.C. hotel market, Alexandria has the highest percentage of new rooms under construction relative to the size of its submarket (10%), followed by Arlington and the Dulles Airport (tied at 4.4%). In contrast, the District has the least number of hotel rooms under construction relative to its submarket (1.4%).

Considering the higher barriers to entry, the government sector's net absorption of office space, per diem lodging rates for the District and immediate MD/VA areas, and RevPAR performance, the District and Arlington offer the best opportunities for new hotel development. New hotel supply in Alexandria will likely take some time to absorb this significant increase.

Outlook

Economic cycles are inevitable, but the Washington Metropolitan Area is one of the more resistant markets in the U.S. The region's consistent level of base hotel demand, as demonstrated by the relatively low RevPAR volatility, status as the nation's capital, and the federal government's continued growth and increased presence indicate that this hotel market will be one of the first to demonstrate sustained RevPAR growth as the nation recovers from the current economic recession.

Contact:

David J. Sangree, MAI, CPA, ISHC
President
Hotel & Leisure Advisors, LLC
14805 Detroit Avenue
Suite 420
Cleveland, OH 44107
Phone: 216-228-7000 ext. 20
Fax: 216-228-7320
Email: dsangree@hladvisors.com
Web: www.hladvisors.com