Marcus & Millichap

Hospitality Research REPORT

Spring 2005

Executive Summary

- Completions will decline to 23,000 rooms this year, down from 26,000 in 2004.
- The value of the U.S. dollar relative to foreign currencies has fallen, lifting travel to the U.S. and raising lodging demand. The weakness of the U.S. dollar is expected to persist in 2005.
- Occupancy is forecast to pick up 180 basis points to finish the year at 62.9 percent. In 2004, occupancy increased 200 basis points.
- Hotel operators have been able to get by with small staffs in recent quarters, but a pickup in occupancy means larger payrolls. An increase in labor costs will diminish bottom line results.
- With room demand firming, operators will have greater pricing power in 2005. A 4.3 percent increase in ADR is projected.
- The increase in 2004 RevPAR was driven primarily by improved vacancy. In 2005, an increase in ADR will push up RevPAR 7.3 percent.

Hospitality Industry Firing on All Cylinders

Low long-term rates and favorable supply and demand dynamics will keep lodging investors active in the quarters ahead. The resilient U.S. consumer has supported a steady level of leisure travel demand over the last year, while foreign travel to the United States has also picked up. Business travel returned last year, and pent-up demand should continue to unwind through 2005. On the investment side, several portfolio sales have taken place over the past year and more than $1 billion was raised in the public markets for companies that invest in hospitality assets.

Room Additions Remain in Check

New supply in the nation's 25 largest markets increased in 2004 following five consecutive years of decline. Nearly 26,000 rooms were put into service last year, up from the 19,000 rooms added in 2003, but well off the pace set in 1996 when more than 106,000 were constructed. It should be noted that Las Vegas accounted for approximately 25 percent of the 2004 construction total. The construction pipeline indicates that deliveries will ease this year, with 23,000 rooms expected to come online. Developers remain cautious despite the recovering economy and increased leisure and business travel. Since 2001, new construction has averaged only 1.5 percent of existing stock, while in the five years leading up to 2001, hotel room inventory increased by average of 5 percent annually. Tempered construction over the past several years has helped owners build occupancy and regain profitability more quickly coming out of the most recent downturn.

Opinions Vary on Convention Center Assumptions

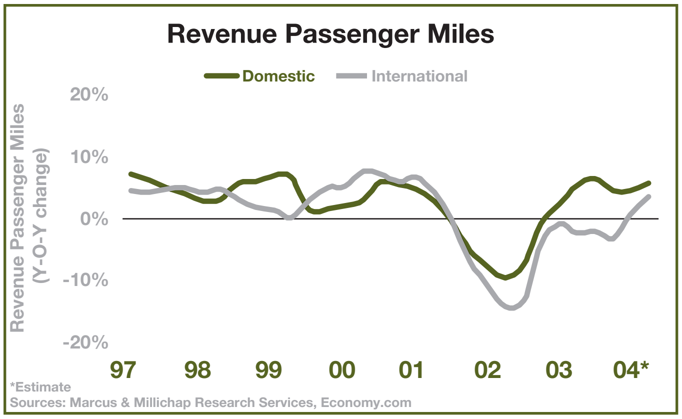
There are varying opinions on the future of the convention business. One suggests that the convention marketplace is declining in a manner that is unlikely to generate increased business for any community, as advances in communications technology are driving a decline in convention attendance. The wisdom of cities that subsidize new or expanded convention facilities and hotels comes into question when looking at the market from this perspective. For the lodging sector, however, it appears that traditional convention markets such as Chicago, New York, Atlanta and New Orleans are benefiting from the business. All of these markets posted improvement in lodging fundamentals last year, results that were supported by the cities' steady flow of convention business.

2005 Hospitality Forecast

- 3.6% increase in travel expenditures
- 23,000 rooms will be completed
- 180 basis point increase in occupancy
- 4.3% increase in room rates
- 8.0% increase in sales prices

Economy

Gross domestic product (GDP), expressed in 2000 dollars, increased 4 percent in 2004, and is forecast to expand 3.0 to 3.5 percent in 2005. Hotel occupancy has typically had a positive correlation with GDP. The various chain-scale segments, however, are affected differently by economic expansion. According to one forecast, the luxury, upper-upscale and upscale segments stand to record the greatest improvement in fundamentals this year. These segments are favored by business travelers and, as the reasoning goes, with business travel accelerating and corporate profitability running strong, expense accounts will not be scrutinized as closely as they were during the downturn. In turn, operators of properties in these segments will be able to pass through significant daily rate hikes. ADRs for the luxury, upper-upscale and upscale segments are forecast to increase 5.8 percent, 5.7 percent and 4.8 percent respectively, compared to 4.3 percent for all chain-scale segments last year.



Cheap Greenback Supports Hospitality Sector

Since peaking in value in 2002, the U.S. dollar has fallen 15 percent against a trade-weighted basket of foreign currencies. The decline has fortified local and regional economies that draw significant numbers of foreign tourists. In 2004, for example, New York and Washington, D.C., each saw international tourism volume augment improvements in inbound domestic travel. As a result, hotel fundamentals improved in those markets.

The U.S. dollar could weaken further in 2005, due primarily to the significant current account deficit that the United States continues to run. While the weakness in the greenback persists, the hospitality sector in gateway cities such as New York and Washington, D.C., will continue to outperform other domestic markets, as foreign travelers continue to take advantage of favorable exchange rates.

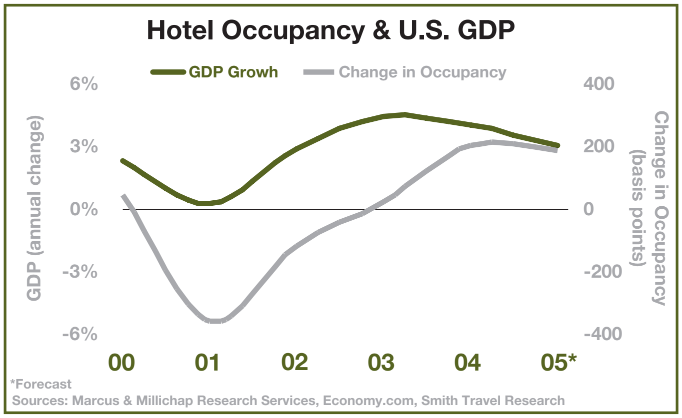
Increased Staffing May Pressure Bottom Line

The current good times for hospitality operators have a potential downside. As occupancy improves, operators will face increasing pressure to expand payrolls. Accommodations employment registered nine month-to-month increases in 2004, the best showing since 1999. For the year, employment in the industry posted a 1.8 percent gain.

Payroll costs typically represent the largest expense line item for hotels. Overall employment in the leisure and hospitality sector is forecast to expand 3.9 percent in 2005. Payrolls at luxury, upper-upscale and upscale properties could record the greatest share of the increase, as these segments implemented the deepest staffing cuts during the recent downturn.

Capital Flows Into Publicly Traded Lodging REITs

More than $1.2 billion was raised in the initial public offerings of hospitality REITs in 2004. As a result, expectations for this year's investment climate are positive, with sales of lodging assets expected to increase in the months ahead as the capital is put to work. In fact, the public market capitalization of publicly traded lodging REITs expanded 51 percent last year, to $14.7 billion, signaling a surge of capital into the hospitality sector. Total market capitalization for publicly traded hospitality REITs increased 18 percent during the year to $817 million.



Travel

Hotel occupancy is expected to rise 180 basis points in 2005, to 62.9 percent. Occupancy rose 200 basis points in 2004 as leisure travel remained steady and corporations sent more workers on the road after cutting travel budgets in previous quarters. Emboldened by rising demand, hotel operators raised ADR 4 percent last year, to $86.41, and a 4.3 percent increase is expected this year. With occupancy increasing and ADR on the upswing, RevPAR is expected to climb 7.3 percent, to $56.62.

International Arrivals Pushed Demand Higher

Foreign travel to the United States made a notable recovery in 2004, reversing a decline that began after 9/11. For the year, foreign visitors constituted 9 percent of U.S. lodging demand, as measured by room-nights. While representing a significant reduction from the 13 percent of total demand registered in 2000, the result is an improvement from 2002 and 2003. To be sure, much of the gain in 2004 came as a result of a weak U.S. dollar. With weakness likely to continue in 2005, and European economies likely to grow stronger in the quarters ahead, the prospects for an increase in the number of foreign arrivals appears promising. Still, some impediments to growth in international tourism remain. Although the United States has not suffered any terrorist strikes since 9/11, legislation such as the Patriot Act and the U.S. Visit program have deterred many prospective travelers.

Surveys Say More Travel in 2005

If recent surveys are a reliable indicator, 2005 looks like a strong year for domestic and international travel. Spending by domestic and international travelers in the U.S. is forecast to increase 5.3 percent in 2005 to $624 billion. In 2004, spending rose 6.9 percent from the previous year. Additionally, forecasts call for a 3.6 percent spike in business travel in 2005, to 149 million trips. The expectation of increased travel is attributed to an improving economy and fewer corporate travel restrictions.

Approximately 60 percent of corporate travel managers expect their firm's travel budgets to increase in 2005, the highest level since 2001. A trend to watch in 2005 is whether lengthy security check-ins negatively affect corporate travel more than safety and terrorism concerns. Finally, a recent index of consumer sentiment found that more vacations are intended within the first six months of 2005. The index receded in early 2005, however, raising the possibility that the previous reading was an aberration.

Chain-Scale Performance

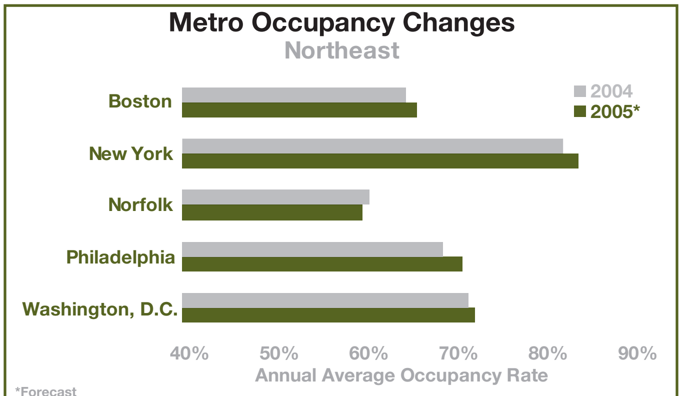
Properties in all chain-scale segments are showing improvement. Occupancy gains have been greatest in the luxury, upper-upscale and upscale segments. The luxury segment's occupancy rate hit 71 percent in early 2005, up 200 basis points when compared to the same period last year. Upper-upscale occupancy rose 70 basis points to 69.8 percent, and upscale properties were 68.4 percent full, up from 67.6 percent one year earlier. Driven by ADRs that were from 6.0 percent to 8.7 percent higher than one year earlier, RevPAR was up 11.7 percent, 7 percent and 8.6 percent for the luxury, upper-upscale and upscale segments, respectively. Results in the lower-grade chain segments were also up in early 2005. In midscale without food and beverage properties, occupancy improved 140 basis points to 61.1 percent, while a 7.4 percent hike in ADR lifted RevPAR 9.9 percent. At the low end, occupancy at independent properties was up 80 basis points to 59.1 percent, year-over-year, in early 2005.

Luxury Players Stir

With luxury travel waking from a four-year slumber, Hilton Hotels has initiated plans to expand one of its lesser known luxury flags. Over the next five years, the firm plans to raise the number of Conrad Hotels from 17 to 50 worldwide. New domestic locations are in the works, as a project is under way in Las Vegas, and a Conrad recently opened in Miami. The Conrad properties are lining up to compete with deluxe flags Ritz-Carlton and Four Seasons. The Mandarin chain is also looking to expand its luxury holdings in the United States; the firm recently opened a location at Columbus Circle in New York. Meanwhile, the staid Ritz-Carlton chain is searching for ways to attract greater numbers of young, affluent travelers. The firm is reportedly considering loosening its dress code to appeal to the casual sensibilities of the younger demographic.

Northeast Overview

Lodging fundamentals in gateway cities such as New York and Washington, D.C., should continue to improve if the U.S. dollar remains weak. Properties in other metros will ride higher on strengthening local economies.



*Forecast
Sources: Marcus & Millichap Research Services, PPR

New York City

Improved performance is expected in 2005 as favorable foreign exchange rates and a sustained level of domestic travel raise occupancy at New York City hotels to 82.7 percent. In 2004, international travel to the city increased 10.3 percent and helped drive annual occupancy to 80.7 percent, up from 75 percent the year before. Greater occupancy yielded a 10.7 percent gain in ADR to $186.09 and a 19.6 percent jump in RevPAR to $150.86. In early 2005, ADR was up 13.9 percent year-over-year.

More than $1 billion in sales were recorded last year and purchases of assets for conversion to multi-family use exceeded $160 million. The latter deals include the 805-room Plaza Hotel, which will be converted to a mixed-use building with 150 hotel rooms. Completions in the market totaled 500 rooms, and approximately 850 rooms are slated for delivery in 2005. These include Holiday Inn Express and Courtyard by Marriott properties.

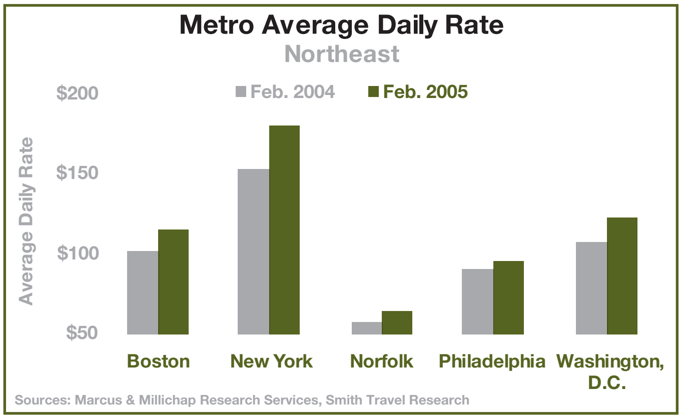
Washington, D.C.

Domestic and international travel, plus the return of business travel, fueled performance gains last year, and should help carry occupancy in area hotels to 71.2 percent in 2005. A 420 basis point rise in hotel occupancy to 70.6 percent plus a 7 percent bump in ADR raised RevPAR at Washington, D.C., properties 13.7 percent in 2004, to $83.73. Local convention business appears to be off to a fast start in 2005, helping to drive 11.2 percent and 10.7 percent year-over-year gains in ADR and RevPAR, respectively.

More than 2,400 rooms were completed in the market last year, including 633 rooms in the District. In 2005, a 385-room Embassy Suites on K Street is slated for an August opening, and is one of 10 properties encompassing 1,704 rooms set for delivery this year. Also, the 1,500-room Gaylord National Hotel and Conference Center in Oxon Hill, Md. is planned, with building to start as early as late spring. On the investment side, institutions accounted for more than 80 percent of dollar volume last year. These buyers will continue to target assets with 200-plus rooms, where the median price rose to $150,000 per room last year.

Boston

Convention bookings for 2005 have already exceeded 2004 levels. Combined with steady international and domestic travel, this should help to lift occupancy to 65.1 percent in 2005. Occupancy was running 200 basis points ahead of the 2004 pace in early 2005. In 2004, occupancy at Boston properties rose 380 basis points to 64.2 percent, driven by the Democratic convention and increased inbound air traffic. Higher occupancy and a 6 percent spike in ADR lifted RevPAR 12.6 percent in 2004 to $79.56. Properties have been trading for a median price of approximately $46,500 per room, with most investment occurring in suburban markets. New supply totaled 900 rooms in 2004, but deliveries will rise to 1,445 rooms in 2005.



Sources: Marcus & Millichap Research Services, Smith Travel Research

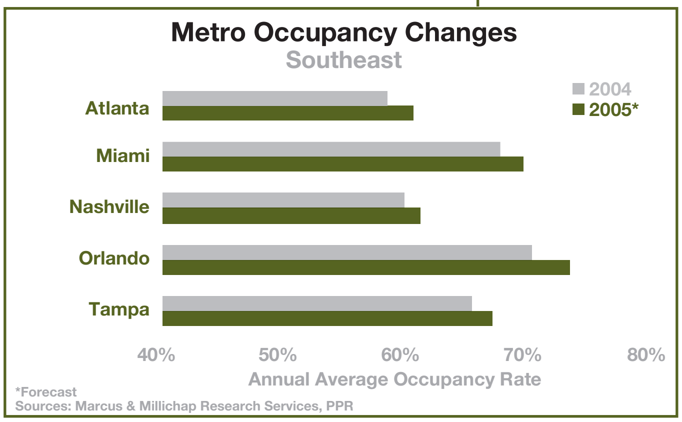
Southeast Overview

Many markets in the region draw both leisure and business travelers. With the former remaining strong and the latter picking up steam, improved hospitality fundamentals should result.

Atlanta

An expanding local economy should help raise occupancy to 60.4 percent in 2005, from 58.7 percent in 2004. ADRs expanded 3.2 percent during 2004, to $76.18, and were up 4.2 percent in early 2005. RevPAR put on 8.1 percent to end last year at $44.69. Only 611 rooms are scheduled to come online in 2005, though more than 2,600 rooms are in the planning phase. These projects include Starwood's 500-room development across from Lennox Square Mall, which could start this year. Approximately 1,100 rooms were added last year, including the 341-room Intercontinental.

On the investment front, sales volume was up more than 50 percent last year. A portfolio buy of the Extended Stay and Hometown Inn chains accounted for a large portion of last year's deals.



Tampa

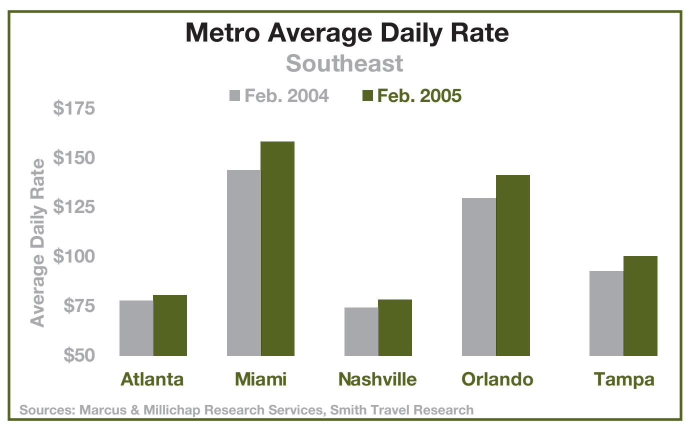
Fundamentals are expected to firm as a recovering national economy supports domestic travel, and the ocean cruise industry continues to emerge as a potent source of demand. Occupancy is forecast to rise 170 basis points to 67.4 percent in 2005 as completions fall by almost 50 percent to 532 rooms. An 8.2 percent year-over-year gain in ADR was posted in early 2005, while occupancy was up 200 basis points.

The median price per room increased 20 percent in 2004, to $72,500. In-state investors have been focusing on small properties on or near Pinellas County beaches. In a large deal, a REIT paid $128,000 per room for the recently refurbished 238-room Hilton Tampa Westshore.

Orlando

With visitor volume projected to crack 50 million for the first time, occupancy in Orlando is forecast to hit 73.8 percent by year-end 2005. Occupancy registered an 800 basis point increase in 2004, to 70.7 percent, helping to fuel a 3.8 percent rise in ADR and a 17 percent jump in RevPAR, to $62.06. ADRs were posting a 7.6 percent year-over-year gain as of early 2005.

Completions are forecast to fall below 1,000 rooms this year, down from more than 1,700 in 2004. The 1,280-room Rosen Shingle Creek Resort Hotel on Universal Boulevard is among the projects under way and is slated to come online in 2006. After a lackluster year in 2003, investors returned last year, raising the median price per room 50 percent to $30,000.



Miami

Occupancy is projected to increase to 70 percent in 2005. Gains are being powered by a weak dollar luring foreign tourists and the area's easy air access from major Northeast population centers.

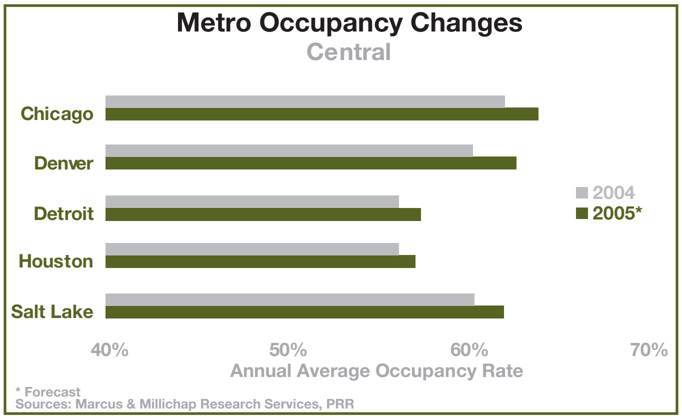
Improved occupancy drove RevPAR growth of 14.1 percent to $77.96, and a 7.8 percent spike in ADR to $114.48. ADR was up 11 percent in early 2005. Approximately 325 new rooms are expected in 2005. Condo conversions are reducing local hotel inventory, and conversions may be a factor in more deals going forward.

Central

Properties in the Central region rely upon business travel as the primary source of demand. If a greater-than-expected gain in this travel sector is registered, the region could outperform our forecasts.

Chicago

Chicago hotel occupancy is forecast to rise 170 basis points this year to 63.7 percent. This follows a 150 basis point increase in 2004, which permitted owners to record a 2.5 percent gain in RevPAR. Current projections could be exceeded with a stronger rebound in the business travel sector, a key demand generator in the local market.



Approximately 925 rooms are forecast to come online this year in the Chicago metro area, up from 733 rooms in 2004. More than $150 million in sales were recorded in 2004, up from $127 million the year before. The largest deal saw Host Marriott pay $81.5 million, or $179,120 per room, for the 455-room Embassy Suites Chicago Lakefront.

Denver

Occupancy in Denver hotel properties is projected to remain at less than its long-term average of 64 percent in 2005. While the year-end 2005 forecast of 62.5 percent is 230 basis points more than year-end 2004, leisure and business travel to the city has been steady but not strong enough to produce greater occupancy gains.

Completions in 2005 will total 1,004 rooms, up from approximately 500 rooms in 2004. Local buyers have been active, purchasing more than $70 million in assets in 2004, slightly more than the year before. Institutional investors, however, are likely to step up their activity in the quarters ahead due to the stability of the local market and the area's mix of leisure and business travelers.

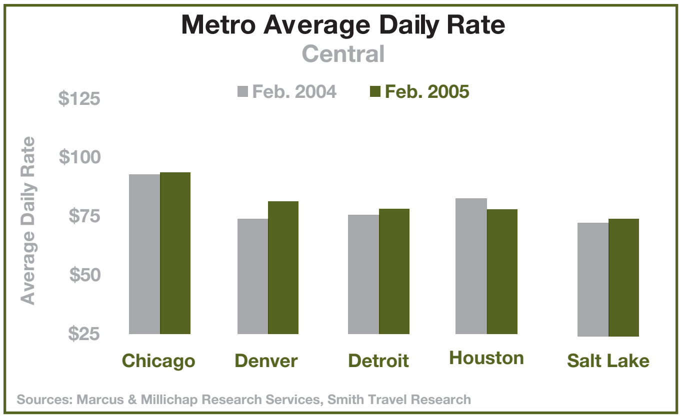
Houston

Houston hotels will record only a modest 80 basis point gain in occupancy in 2005, to 57 percent. Despite a rebounding economy and solid results in the vital energy sector, business travel has not recovered sufficiently to generate better results at local properties. RevPAR in 2004 put on 6 percent to finish the year at $42.76, but the result is attributable to a 5 percent spike in ADR.

Construction may dampen prospects for greater improvement. Completions in 2005 will total 1,171 rooms, representing 2 percent of the market's stock. New supply is spread over several chain segments: approximately 500 rooms in the mid-market without food and beverage, 400 luxury rooms and 200 upscale rooms.

Salt Lake City

Occupancy is forecast to climb to 61.8 percent at year end, up from 60.2 percent in 2004. RevPAR increased 4.5 percent in 2004, carried by a 240 basis point improvement in occupancy and a 0.3 percent gain in ADR. Going forward, local property operators will draw strength from steady job growth of 1.8 percent annually, and room demand from the area's $750 million per year ski industry.



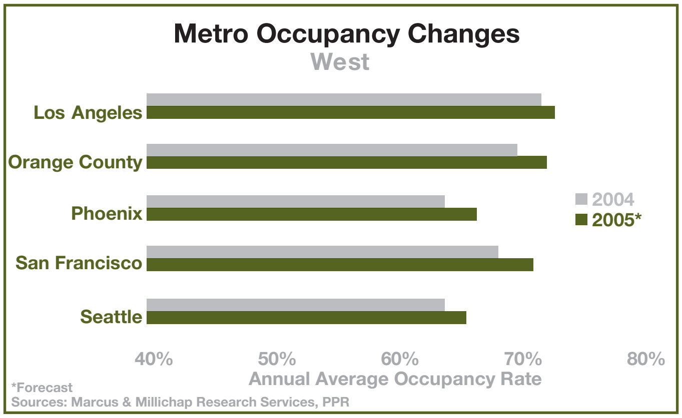
The metro will benefit from a light construction pipeline in the quarters ahead with only 160 rooms scheduled to come online in 2005. As a result, owners should be able to build bottom lines on even modest spikes in room demand.

Western Overview

Hospitality assets in the Western region turned in stronger occupancy last year, and continued improvement is expected in 2005 as local economies find sure footing.

Los Angeles

Sustained strength in tourism and an accelerating recovery in business travel will boost occupancy in Los Angeles hotels to 72.5 percent in 2005, up from 71.6 percent the previous year. A buildup in leisure and business travel generated a 420 basis point occupancy gain last year and a 12.9 percent jump in RevPAR to $68.82.



Approximately 660 rooms are slated for delivery this year. The planning pipeline, however, has more than 2,500 rooms. Sales topped $500 million in 2004 for the second consecutive year, and the median price per room increased 39 percent to $65,000. Private buyers and institutions are focusing on major flags, such as Best Western and Holiday Inn, a trend we expect will continue through 2005.

Orange County

Following a 300 basis point occupancy gain in 2004, Orange County hotel properties are forecast to post a 220 basis point increase in occupancy to 71.7 percent in 2005. Business and leisure travel have registered significant improvement, and visitor volume should rise in the quarters ahead, driven partly by the celebration of Disneyland's 50th anniversary.

Approximately 175 new rooms are expected to come online in 2005, two times the number of completions in 2004. A 300-room Ritz Carlton in Irvine is one of eight planned projects, totaling 1,400 rooms, in the metro. Investors remain highly interested in the market and its long-term prospects. The median price per room was up 13 percent to $67,000 in 2004. Many private buyers and institutions are establishing or growing their portfolios in the market, which will keep prices rising throughout the year.

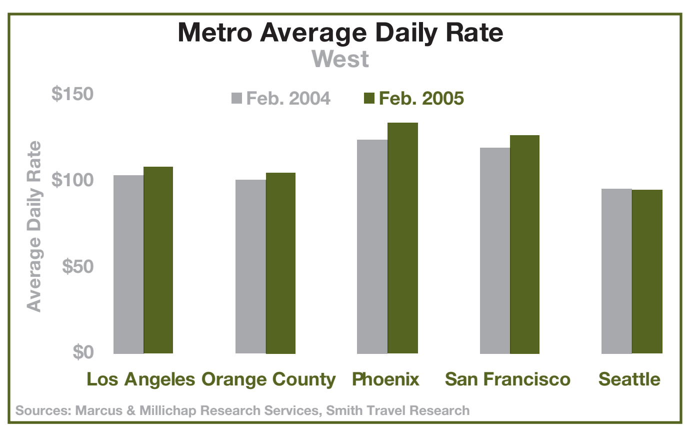
Phoenix

A growing local economy and continued strength in domestic travel will help raise Phoenix hotel occupancy to 66.2 percent in 2005, up from 63.7 percent last year. A 430 basis point jump in occupancy in 2004 triggered a 3.3 percent rise in ADR and a 10.8 percent hike in RevPAR to $62.01.

About 740 rooms are projected to be completed in 2005, up from 600 in 2004. The projects include a 128-room Hilton Garden Inn in Scottsdale and the Radisson Hotel & Conference Center, which will bring 247 rooms to Ft. McDowell. Low barriers to entry, few "must-have" locations and steep seasonal rate discounting have kept large national investors out of the market for the most part. Still, private buyers are active, supporting a 7 percent increase in the median price per room last year to $33,000.

San Francisco

With business travel recovering, domestic leisure travel steady and the U.S. dollar soft relative to Asian currencies, occupancy at San Francisco hotels is expected to climb 290 basis points to 70.8 percent in 2005. In 2004, a 500 basis point increase in occupancy led to a 1.1 percent gain in ADR and 9.3 percent growth in RevPAR to $80.16. Investors pushed the median price per room up 3.4 percent last year to $81,649. We expect prices to rise further through 2005 as tourism posts strong gains and the local economy expands.



Marcus & Millichap
NATIONAL HOSPITALITY GROUP

Robert B. Hicks
National Director
National Hospitality Group
Tel: (916) 677-4100
rhicks@marcusmillichap.com

Capital Markets Outlook

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

With 10-year U.S. Treasury yields hanging in the low- to mid-4 percent range despite an improving economy and tightening monetary policy, even Alan Greenspan conceded the trend is a "conundrum" that defies explanation. Whether 10-year rates begin to climb, and where they settle, or whether they remain stuck around current levels is a topic of interesting discussion these days in the financial markets.

On the one hand, an accelerated pace of job creation in the quarters ahead will spur personal income growth and initiate a buildup of inflation, resulting in rising interest rates. Additionally, countries such as Japan and China have been big buyers of Treasury debt lately. A significant unwinding of foreign positions in U.S. Treasury debt would also lift long-term rates, though the prospect of this scenario evolving appears remote.

Several factors seem to be holding down yields as well. For example, with major equity indexes providing uninspiring returns and considerable uncertainty, a desire for safety and yield among all types of investors has forced many to settle for government debt yielding slightly more than 4 percent. Sustained strong buying of U.S. Treasury debt, such as what has occurred in the past two years, has suppressed long-term rates, and a persistent strong bid into Treasury securities will continue to hold down yields.

For hospitality property borrowers, now is the time to lock in long-term financing. Loan spreads for hospitality assets tightened in 2004 and could compress further in 2005. Lenders are inclined to view the hospitality industry's rebound favorably, and also see limited new supply in many markets as a positive development. Loans on many properties are being written from 115 basis points over the 10-year Treasury to 135 basis points over for the best assets and 140 basis points to 180 basis points over for lower-grade properties. Debt-service coverage begins at 1.3x, and LTVs greater than 70 percent are unusual, except for a flagged property in a good location with a sound operating history.

Market Highlights

Metro Area	Inventory (rooms)	2005 Completions Forecast	2005 Avg. Annual Occupancy Forecast	February 2005 ADR	2004 Preliminary Med. $/Room
Las Vegas	154,925	4,026	88.6%	$89.78	$51,041
Orlando	118,299	997	73.8%	$140.73	$30,000
Los Angeles	106,499	656	72.5%	$104.69	$65,151
Chicago	102,513	925	63.7%	$93.15	$29,070
Dallas	96,823	1,653	58.9%	$82.47	$20,846
Atlanta	94,890	611	60.4%	$80.76	$27,495
Washington	91,325	1,704	71.2%	$129.02	$150,834
New York	81,985	850	82.7%	$180.79	$95,321
Houston	62,153	1,171	57.0%	$77.54	$36,507
Phoenix	55,786	742	66.2%	$130.03	$32,954
Orange County	54,541	175	71.7%	$100.78	$66,666
San Diego	54,527	937	71.1%	$117.18	$59,641
San Francisco	52,704	266	70.8%	$119.25	$81,649
Miami	49,441	324	70.0%	$157.81	$70,263
Boston	48,083	1,445	65.1%	$114.07	$46,528
Seattle	44,393	528	65.4%	$92.22	$37,925
Tampa	42,881	532	67.4%	$99.77	$72,500
Philadelphia	42,117	404	70.2%	$96.10	$52,612
Denver	37,370	1,004	62.5%	$81.16	$31,904
Fort Lauderdale	31,166	815	73.3%	$114.79	$77,777
Overall U.S.			62.9%	$91.23	$48,297

The information contained in this report was obtained from sources deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, express or implied, may be made as to the accuracy or reliability of the information contained herein. Sources: Marcus & Millichap Research Services, Brookings Institution, Carlson Wagonlit Travel, CoStar Group, Inc., economy.com, Greater Ft. Lauderdale Convention & Visitors Bureau, Las Vegas Convention and Visitors Authority, Property & Portfolio Research, Smith Travel Research, The Conference Board, Travel Industry Association of America,

Marcus & Millichap
Real Estate Investment Brokerage Company

Prepared and edited by
Art Gering
Senior Market Analyst
2398 E. Camelback Road
Suite 550
Phoenix, Arizona 85016
Tel: (602) 952-9669
agering@marcusmillichap.com

For information on national hospitality trends, contact:
Erica L. Linn
National Research Manager
Tel: (602) 952-9669
elinn@marcusmillichap.com

Price: $300