

Supply Impacts Boston Market

Boston and Suburb Forecast for 2008

By Thomas Dolan and Laura Kalcevic

Boston's leadership position in New England's hotel market has historically been driven by several key factors: population density, high per-capita personal income, abundance of tourist attractions, and a strong economy. And room rates at Boston hotels reflect that preeminence; in fact, despite being below their historical highs of 2000, they are among the highest in the nation.

But there is a major issue facing Boston. Substantial new supply entering the market over the next few years will likely hamper occupancy.

Over the last few years, the city realized growth in revenue, demand and occupancy. In 2006, the city's lodging market realized a solid RevPAR gain, resembling the rate of growth of 2004, a year boosted by the Democratic National Convention. While demand moderated in 2005 and 2006, it did continue to grow, pushing occupancy up to its highest level since 2000.

The year-to-date data, through June 2007, indicates that demand continues to grow. But the growth in demand has been outpaced by the new supply (for example, the new Westin and Intercontinental hotels) resulting in lower market-wide occupancy.

Table 1 summarizes the historical trends between 2001 and 2006, as well as the year-to-date trends through June 2007. The data is based on hotels located in the city of Boston, where the inventory totaled 15,858 rooms as of December 2006, and increased to 16,548 rooms as of June 2007.

In real terms, the market appears to be stable and healthy, despite the fact that RevPAR remains below the 2000 peak of \$154.19. The mid-year 2007 data indicates that RevPAR will continue at a pace below those 2000 levels. Most major metropolitan U.S. markets have now exceeded their 2000 RevPAR levels. The fact that Boston remains behind the curve is chiefly a result of a slow-moving commercial segment.

Despite the slower commercial activity, Boston's economic outlook is categorized as positive, according to the Federal Reserve's Beige Book, which tracks business sentiment across many sectors. The software, information technology, and staffing sectors are forecasted at double-digit growth rates. And the city's meeting and group segment reflected this strength, displaying extremely strong volume through 2005 and 2006, which contributed to the strong gains in RevPAR.

Conversely, the outlook for 2007 is substantially weaker than the actual results for 2006. However, it is our understanding that pre-bookings for 2008 suggest a return to 2006 volume levels. The leisure-segment demand—international demand is generally the strongest indicator of this segment's health in Boston—has also rebounded.

Inventory

The market will need to be in fine form in future years in order to absorb new inventory. Two new hotels opened in 2006 and four hotels are currently under construction.

TABLE 1 Historical City of Boston Results

	2001	2002	2003	2004	2005	2006	Year-to-Date Through June		Average Annual Compounded Change 2001-2006
							2006	2007	
Average Daily Room Count	13,888	13,935	14,566	14,999	15,299	15,858	15,447	16,548	
Available Room Nights	5,069,105	5,086,137	5,316,647	5,474,495	5,584,300	5,788,201	2,795,986	2,995,188	
Change	1.3%	0.3%	4.5%	3.0%	2.0%	3.7%	—	7.1%	2.7%
Occupied Room Nights	3,537,815	3,614,010	3,752,925	4,036,455	4,151,318	4,399,715	2,086,768	2,149,114	
Change	(10.3%)	2.2%	3.8%	7.6%	2.8%	6.0%	—	3.0%	4.5%
Occupancy	69.8%	71.1%	70.6%	73.7%	74.3%	76.0%	74.6%	71.8%	
Average Rate	\$177.66	\$163.10	\$151.50	\$165.60	\$173.08	\$191.30	\$184.11	\$193.50	
Change	(9.2%)	(8.2%)	(7.1%)	9.3%	4.5%	10.5%	—	5.1%	1.5%
RevPAR	\$123.99	\$115.89	\$106.94	\$122.10	\$128.67	\$145.41	\$137.41	\$138.84	
Change	(19.6%)	(6.5%)	(7.7%)	14.2%	5.4%	13.0%	—	1.0%	3.2%

Source: Smith Travel Research

TABLE 2 Speculative Projects – City of Boston

Project Name	Opening	District	Quality	# Rooms	Developer
Columbus Center	Jan. 2010	Back Bay	5.0	162	CUIP-Winn LLC
W Hotel	Planning	Midtown	4.0	N/A	Sawyer Enterprises
Five-Star Hotel	Planning	Waterfront/Conv. Ctr	5.0	175-250	New England Development
Core Black	Planning	Waterfront/Conv. Ctr	4.0	300-400	John Drew Co.
Courtyard/Residence Inn	Planning	Waterfront/Conv. Ctr	3.5	+/- 500	Madison Properties
Hilton Garden Inn/Homewood	Planning	Fenway Park	3.5	300	Robert Sage

Total Speculative: 1,225-1,400 rooms

Source: Source: Smith Travel Research

There are six hotels that have entered or are committed to enter the market between 2006 and 2008, adding a total of 2,294 rooms to the existing supply. This new inventory will be a minimum of four-star quality and pricing. The key areas of development are the Waterfront/Convention Center District and the Downtown Waterfront District. In addition, there are three speculative projects that will likely be constructed in the Waterfront/ Convention Center District.

This development is occurring largely on the basis of the Boston Convention & Exhibition Center, which opened in mid-2004, and has thus far operated without a large block of rooms available within walking distance. This segment may face challenges in the next few years. Although group demand can reasonably be expected to grow in tandem with the supply growth, the new hotels will also be competing for the market's existing share of commercial and leisure demand.

Table 3 illustrates the historical trends for the Greater Boston lodging market, including the city of Boston.

The Greater Boston market also experienced healthy RevPAR growth from 2004 through 2006, but it has also moderated into 2007. Table 4 (page 24) provides a better perspective on the suburban markets by excluding the city of Boston's hotels from the Greater Boston statistics.

As exhibited in the table, occupancy levels have remained low in suburban Boston, reaching only 62.8% in 2006; nevertheless, RevPAR experienced strong growth over the past three-and-a-half years. The low occupancy has discouraged developers.

The mid-year 2007 data indicates that market demand is flattening and average rate growth is beginning to slow. Any new supply expected to enter the market will further aggravate an already slowing market.

In our opinion, there are several key variables at play for the city of Boston and the suburban lodging market:

1. How fast will the South Boston/Waterfront District mature? As a complement to the BCEC and the new hotels, the neighborhood requires a retail presence and more office space in

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TABLE 3 Historical Greater Boston Results

	2001	2002	2003	2004	2005	2006	Year-to-Date Through June		Average Annual Compounded Change 2001-2006
							2006	2007	
Avg. Daily Rm Count	43,076	44,485	46,286	46,700	46,760	47,800	47,146	48,330	
Avail. Room Nights	15,722,783	16,237,006	16,894,290	17,045,519	17,067,437	17,446,823	8,533,414	8,747,714	
Change	—	3.3%	4.0%	0.9%	0.1%	2.2%	—	2.5%	2.1%
Occupied Rm Nights	10,182,187	10,277,594	10,213,806	10,945,253	11,145,387	11,717,308	5,526,873	5,602,561	
Change	—	0.9%	(0.6)%	7.2%	1.8%	5.1%	—	1.4%	2.8%
Occupancy	64.8%	63.3%	60.5%	64.2%	65.3%	67.2%	64.8%	64.0%	
Avg. Rate	\$135.39	\$123.59	\$116.95	\$124.10	\$129.95	\$141.40	\$137.16	\$144.32	
Change	—	(8.7)%	(5.4)%	6.1%	4.7%	8.8%	—	5.2%	0.9%
RevPAR	\$87.68	\$78.23	\$70.71	\$79.69	\$84.86	\$94.96	\$88.84	\$92.43	
Change	—	(10.8)%	(9.6)%	12.7%	6.5%	11.9%	—	4.0%	1.6%

Source: Smith Travel Research

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TABLE 4 Historical Greater Boston Results Less City of Boston

	2001	2002	2003	2004	2005	2006	Year-to-Date Through June		Average Annual Compounded Change:
							2006	2007	2001-2006
Avg. Daily Rm Count	29,188	30,550	31,720	31,701	31,461	31,941	31,698	31,782	
Avail. Room Nights	10,653,678	11,150,869	11,577,643	11,571,024	11,483,137	11,658,622	5,737,428	5,752,526	
Change	—	4.7%	3.8%	(.01)%	(0.8)%	1.5%	—	—	1.8%
Occupied Rm Nights	6,644,372	6,663,584	6,460,881	6,908,798	6,994,069	7,317,593	3,440,105	3,453,447	
Change	—	0.3%	(3.0)%	6.9%	1.2%	4.6%	—	0.4%	1.9%
Occupancy	62.4%	59.8%	55.8%	59.7%	60.9%	62.8%	60.0%	60.0%	
Avg. Rate	\$112.89	\$102.16	\$96.89	\$99.85	\$104.34	\$111.39	\$108.69	\$113.72	
Change	—	(9.5)%	(5.2)%	3.1%	4.5%	6.8%	—	4.6%	(0.3)%
RevPAR	\$70.40	\$61.05	\$54.07	\$59.62	\$63.55	\$69.92	\$65.17	\$68.27	
Change	—	(13.3)%	(11.4)%	10.3%	6.6%	10.0%	—	4.8%	(0.1)%

Source: Smith Travel Research

order to sustain a node of hotel development over the long term.

2. When will commercial demand return in earnest? Recovery in this segment has been slow, and it seems that some "next big thing" is necessary to really stimulate the technology sector. Harvard's recently announced plan to construct a 500,000-square-foot stem cell research incubator could be a harbinger.

3. What is the fate of the Hynes Convention Center? Although a recommendation by a state advisory panel on this Back Bay facility was expected by now, it has yet to be released. The smaller convention center continues to operate despite the opening of the BCEC. Given its recent performance, its closure seems unlikely.

4. Finally, it appears that the Boston market's overall growth has begun to slow in terms of occupancy and average rate, which means the party could be over unless one of the three stated variables take hold. ■

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