HVS

MARKET REPORT

Market Intelligence Report 2013 Seattle

JULY 15, 2013

Seattle, WA is known worldwide for its reputation as a coffee & music haven, as well as extraordinary attractions including the Space Needle and Pike Place Market. This article shows trends in hotel supply, demand, & performance within the city.

Known worldwide for its reputation as a coffee and music haven, as well as extraordinary attractions like the Space Needle and Pike Place Market, Seattle also boasts a high quality of life, a highly educated workforce, a variety of outdoor activities, and a strong economic base that includes high-tech, clean-tech, bio-tech, manufacturing, telecommunications, and healthcare companies. These factors have created a favorable climate for hotels in Seattle and surrounding markets that should extend over the near term.

Economy Update

The following table illustrates historical and projected employment, population, and income data for the overall Seattle market.

HISTORICAL & PROJECTED EMPLOYMENT, HOUSEHOLDS, POPULATION, AND HOUSEHOLD INCOME STATISTICS

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Year	Total Employment	% Chg	Office Employment	% Chg	Industrial Employment	% Chg	Households	% Chg	Population	% Chg	Household Avg. Income	% Chg
2000	1,412,730	—	406,553	—	272,897	—	944,020	—	2,362,740	—	$102,041	—
2001	1,359,630	(3.8) %	393,440	(3.2) %	259,829	(4.8) %	953,620	1.0 %	2,385,230	1.0 %	100,726	(1.3) %
2002	1,330,830	(2.1)	392,396	(0.3)	238,253	(8.3)	957,730	0.4	2,393,970	0.4	102,952	2.2
2003	1,323,830	(0.5)	393,591	0.3	226,039	(5.1)	963,400	0.6	2,407,440	0.6	105,635	2.6
2004	1,346,330	1.7	400,382	1.7	228,831	1.2	973,460	1.0	2,433,000	1.1	133,804	26.7
2005	1,390,570	3.3	412,173	2.9	239,830	4.8	988,560	1.6	2,471,540	1.6	118,211	(11.7)
2006	1,429,570	2.8	422,324	2.5	247,862	3.3	1,005,000	1.7	2,513,540	1.7	127,507	7.9
2007	1,474,030	3.1	431,617	2.2	255,724	3.2	1,019,360	1.4	2,549,610	1.4	135,815	6.5
2008	1,458,170	(1.1)	428,853	(0.6)	246,333	(3.7)	1,036,550	1.7	2,594,250	1.8	134,383	(1.1)
2009	1,373,670	(5.8)	403,949	(5.8)	232,123	(5.8)	1,054,680	1.7	2,636,910	1.6	124,699	(7.2)
2010	1,385,200	0.8	407,904	1.0	233,464	0.6	1,067,730	1.2	2,669,470	1.2	128,627	3.1
2011	1,415,700	2.2	412,440	1.1	246,249	5.5	1,080,960	1.2	2,711,570	1.6	136,585	6.2
2012	1,453,760	2.7	420,835	2.0	260,029	5.6	1,094,260	1.2	2,747,100	1.3	140,954	3.2
Forecasts												
2013	*1,481,160*	*1.9 %*	*429,518*	*2.1 %*	*266,354*	*2.4 %*	*1,111,180*	*1.5 %*	*2,780,770*	*1.2 %*	*$146,582*	*4.0 %*
2014	*1,521,610*	*2.7*	*442,297*	*3.0*	*273,174*	*2.6*	*1,130,310*	*1.7*	*2,814,000*	*1.2*	*154,590*	*5.5*
2015	*1,566,920*	*3.0*	*456,426*	*3.2*	*281,304*	*3.0*	*1,150,230*	*1.8*	*2,845,680*	*1.1*	*163,023*	*5.5*
2016	*1,602,960*	*2.3*	*467,684*	*2.5*	*285,806*	*1.6*	*1,169,620*	*1.7*	*2,877,330*	*1.1*	*170,479*	*4.6*
2017	*1,622,390*	*1.2*	*474,433*	*1.4*	*287,052*	*0.4*	*1,188,300*	*1.6*	*2,910,210*	*1.1*	*176,093*	*3.3*
Average Annual Compound Change												
2000 - 2012		0.2 %		0.3 %		(0.4) %		1.2 %		1.3 %		2.7 %
2000 - 2007		0.6		0.9		(0.9)		1.1		1.1		4.2
2007 - 2010		(2.1)		(1.9)		(3.0)		1.6		1.5		(1.8)
2010 - 2012		2.4		1.6		5.5		1.2		1.4		4.7
Forecast 2012 - 2017		*2.2 %*		*2.4 %*		*2.0 %*		*1.7 %*		*1.2 %*		*4.6 %*

Source: REIS Report, 4th Quarter, 2012

With the exceptions of the recent recession and the earlier dot.com bust, the Seattle market has realized gains in total employment annually during the historical period shown. Industrial employment has realized the largest declines and increases over the years, concurrent with the hiring and layoff cycles typical of the manufacturing and distribution industries. Households and the overall population of Seattle noted 1% to 2% growth from 2004 through 2012.

Employment, household size, and population are forecast to grow modestly through 2017. Household average income is forecast to grow at rates that are more significant as higher-paying jobs in the technology industries are expected to grow.

The following table illustrates unemployment statistics for King County, the Seattle MSA, the state of Washington, and the U.S. from 2002 to 2011.

UNEMPLOYMENT STATISTICS

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Year	County	MSA	State	U.S.
2002	6.1 %	6.7 %	7.3 %	5.8 %
2003	6.2	6.8	7.4	6.0
2004	5.2	5.7	6.2	5.5
2005	4.7	5.0	5.5	5.1
2006	4.2	4.5	4.9	4.6
2007	3.6	4.0	4.6	4.6
2008	4.4	4.9	5.4	5.8
2009	8.6	9.1	9.4	9.3
2010	9.1	9.7	9.9	9.6
2011	8.1	8.7	9.2	9.0
Recent Month - Dec				
2011	7.1 %	7.7 %	8.5 %	8.5 %
2012	6.1	6.7	7.7	7.8

* Letters shown next to data points (if any) reflect revised population controls and/or model re-estimation implemented by the BLS.

Source: U.S. Bureau of Labor Statistics

The Seattle market realized strong growth across a variety of industry segments following the end of the recent recession; this was particularly evident in the high-tech industry with the expansions of Amazon.com, Microsoft, Facebook, Google, and Twitter. Amazon.com has become a driving force in the market, with 582,000 square feet of new office space completed in 2011, 325,000 square feet completed in 2012, and a combined total of 3.1 million square feet in the pipeline. In addition, manufacturing has grown, in particular at Boeing, which has received a significant number of post-recession aircraft orders. There is some concern of Boeing's long-term stability in the area given competition from Airbus, the potential for Boeing to expand operations to South Carolina, continued labor union issues, and potential defense spending cuts by the federal government. The grounding of all fifty 787 Dreamliner aircraft in early 2013 because of the risk for potential battery fires has also hurt perception of the company, which is working to address the issues and return the cutting-edge aircraft to operation; on April 19, 2013, the Federal Aviation Administration announced it had approved changes to the design of the Boeing 787's battery system, marking the first step toward returning the grounded aircraft to service.

Office Space Market Update

The following table details Seattle's office space statistics, which are important indicators of the market's propensity to attract commercial hotel demand.

OFFICE SPACE STATISTICS – MARKET OVERVIEW

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	Submarket	Inventory Buildings	Inventory Square Feet	Occupied Office Space	Vacancy Rate	Average Asking Lease
1	Central Seattle	282	38,760,000	33,372,400	13.9 %	$30.96
2	Kirkland/Redmond	129	8,531,000	7,473,200	12.4	25.21
3	Northend/Snohomish	171	7,390,000	6,296,300	14.8	24.38
4	Bellevue/Issaquah	240	20,250,000	17,273,300	14.7	32.81
5	Renton/Kent/Sthend	136	7,343,000	6,035,900	17.8	20.92
	Totals and Averages	**958**	**82,274,000**	**70,451,100**	**14.4 %**	**$29.33**

Source: REIS Report, 4th Quarter, 2012

As mentioned previously, the expansion of Amazon.com is a driving force in the market. In addition, Microsoft's expansion

efforts include a 313,800-square-foot facility currently underway in Redmond and an additional 233,700-square-foot building in the planning phase. With low vacancy rates in the submarkets of Central Seattle, Kirkland/Redmond, and Bellevue/Issaquah, it is expected that speculative development projects will become more prevalent across Seattle.

The following table illustrates a trend of office space statistics for the overall Seattle market.

HISTORICAL AND PROJECTED OFFICE SPACE STATISTICS – GREATER MARKET

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	Seattle Market							
Year	Available Office Space	% Chg	Occupied Office Space	% Chg	Vacancy Rate	Asking Lease Rate	% Chg
2000	66,891,000	—	63,999,000	—	4.3 %	$31.47	—
2001	70,885,000	6.0 %	62,268,000	(2.7) %	12.2	28.84	(8.4) %
2002	71,932,000	1.5	60,817,000	(2.3)	15.5	25.32	(12.2)
2003	72,774,000	1.2	60,727,000	(0.1)	16.6	24.04	(5.1)
2004	73,191,000	0.6	61,965,000	2.0	15.3	23.53	(2.1)
2005	73,410,000	0.3	63,867,000	3.1	13.0	23.87	1.4
2006	73,489,000	0.1	66,636,000	4.3	9.3	25.79	8.0
2007	75,046,000	2.1	68,176,000	2.3	9.2	29.49	14.3
2008	77,146,000	2.8	68,966,000	1.2	10.6	30.86	4.6
2009	80,609,000	4.5	66,657,000	(3.3)	17.3	29.43	(4.6)
2010	81,405,000	1.0	68,363,000	2.6	16.0	28.64	(2.7)
2011	81,785,000	0.5	69,526,000	1.7	15.0	28.83	0.7
2012	82,274,000	0.6	70,460,000	1.3	14.4	29.33	1.7
Forecasts							
2013	*82,344,000*	*0.1 %*	*70,985,000*	*0.7 %*	*13.8 %*	*$30.01*	*2.3 %*
2014	*82,765,000*	*0.5*	*71,948,000*	*1.4*	*13.1*	*30.87*	*2.9*
2015	*83,397,000*	*0.8*	*73,067,000*	*1.6*	*12.4*	*31.92*	*3.4*
2016	*84,354,000*	*1.1*	*74,425,000*	*1.9*	*11.8*	*33.50*	*4.9*
2017	*85,348,000*	*1.2*	*75,724,000*	*1.7*	*11.3*	*35.15*	*4.9*
Average Annual Compound Change							
2000 - 2012		1.7 %		0.8 %			(0.6) %
2000 - 2007		1.7		0.9			(0.9)
2007 - 2010		2.7		0.1			(1.0)
2010 - 2012		0.5		1.5			1.2
Forecast 2012 - 2017		*0.7 %*		*1.5 %*			*3.7 %*

Source: REIS Report, 4th Quarter, 2012

Although the closure of Washington Mutual, layoffs at Microsoft, and other events during the recent recession resulted in a significant increase in vacancy in 2009, other industries were not hit as hard, and overall vacancy never reached the 20% mark that many urban areas realized across the U.S. Healthcare, education, the Port of Seattle, and the Bill & Melinda Gates Foundation remained particularly strong during the downturn. Vacancy is expected to continue the decline that began in 2010, while the average lease rate should increase as the market strengthens.

Hotel Construction Update

Proposed hotels in the pipeline for Seattle include the following:

- Hotel Ballard (29 units)
- Holiday Inn Express Federal Way (81 units)
- Bellevue Park Hotel Bellevue (108 units)
- Artemis Hotel Des Moines (250 units)
- Hampton Inn First Avenue Seattle (174 units)
- Luxury Hotel Fifth Avenue Seattle (184 units)
- Hyatt Fifth Avenue Northern Seattle (126 units)
- Embassy Suites Stadium Place (297 units)

- Hilton Garden Inn Denny Triangle (222 units)

Many new hotel projects have been rumored for the greater Seattle market, including a 1,200-room, full-service hotel; however, given the stringent financial requirements to build a hotel in the present economic climate, the percentage increase to the overall market supply in Seattle should be minimal. New hotel projects in the Downtown market are expected to move forward as the economy gains strength. In addition, smaller limited- and select-service projects in the Puget Sound are anticipated to be built as lodging demand continues to improve and more private financing becomes available.

Outlook on Market Occupancy and Average Rate

Hotel demand is expected to grow as the economy continues to strengthen and area corporations continue to expand. Occupancy growth is anticipated, concurrent with growth in hotel demand; however, occupancy levels may be affected in markets receiving large amounts of new supply. Average rate is expected to realize significant gains as lodging demand continues to strengthen, and new high-quality supply should support further average rate growth, provided area hoteliers do not start to discount rates to retain occupancy—a practice widely adopted during the recent recession but less likely in the more stable economic climate of the present.

Recent Hotel Transactions

The following table summarizes hotel transactions in Washington State over the last two years.

REVIEW OF HOTEL TRANSACTIONS

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Property	Location	Sale Date	Price	Rooms	Price/Rm
King Oscar Motel Pacific	Pacific, Washington	Jan-13	$3,800,000	120	$31,667
Hawthorn Suites Seattle Kent	Kent, Washington	Jan-13	8,675,000	152	57,072
Courtyard by Marriott Seattle North Lynnwood Everett	Lynnwood, Washington	Jan-13	11,638,656	164	70,967
Best Western Plus Heritage Inn	Bellingham, Washington	Dec-12	8,833,000	91	97,066
Days Inn Everett Mall	Everett, Washington	Nov-12	2,624,000	76	34,526
King Oscar Tacoma Inn	Tacoma, Washington	Nov-12	2,500,000	153	16,340
Quality Inn & Suites Federal Way	Federal Way, Washington	Oct-12	2,980,000	65	45,846
Holiday Inn Express & Suites Everett	Everett, Washington	Oct-12	10,300,000	99	104,040
Hilton Seattle	Seattle, Washington	Sep-12	63,000,000	237	265,823
Rodeway Inn & Suites Vancouver	Vancouver, Washington	Aug-12	2,000,000	63	31,746
Klondike Motel	Republic, Washington	Aug-12	600,000	20	30,000
Holiday Inn Sea-Tac	Seattle, Washington	Jul-12	26,600,000	259	102,703
Baymont Inn & Suites Bremerton	Bremerton, Washington	Jul-12	3,300,000	155	21,290
Hotel Vintage Park	Seattle, Washington	Jul-12	32,500,000	124	262,097
Silverdale Beach Hotel	Silverdale, Washington	Jun-12	6,800,000	151	45,033
Days Inn Bellevue	Bellevue, Washington	Jun-12	5,150,000	106	48,585
Quality Inn & Suites Everett	Everett, Washington	Jun-12	4,075,000	82	49,695
Holiday Inn Express Vancouver Mall	Vancouver, Washington	Apr-12	6,700,000	91	73,626
La Quinta Inn & Suites Spokane	Spokane Valley, Washington	Apr-12	4,357,750	65	67,042
Americas Best Value Inn Lakewood	Lakewood, Washington	Apr-12	1,350,000	54	25,000
Holiday Inn Express Bothell Canyon Park	Bothell, Washington	Mar-12	6,025,000	62	97,177
Fairfield Inn by Marriott Kennewick	Kennewick, Washington	Mar-12	4,365,000	62	70,403
Cascade Mountain Lodge	Concrete, Washington	Mar-12	192,000	14	13,714
Blue Spruce Motel	Tacoma, Washington	Feb-12	1,100,000	28	39,286
Forks Motel	Forks, Washington	Dec-11	3,400,000	73	46,575
Sea-Tac Motel	Seattle, Washington	Oct-11	3,700,000	144	25,694
Arlington Motor Inn	Arlington, Washington	Sep-11	885,000	41	21,585
Econo Lodge Fife	Fife, Washington	Aug-11	3,100,000	96	32,292
Red Ranch Inn	Sequim, Washington	Aug-11	675,000	55	12,273
Quality Inn Sea-Tac Airport	Seattle, Washington	Jun-11	4,150,000	104	39,904

The most notable transactions in 2012 were the Hilton Seattle and the Hotel Vintage Park, which sold at a price per key of $265,823 and $262,097, respectively. The remaining sales in the market ranged from $104,040 down to $12,273 per key, with pricing highly dependent on historical performance and on the conditions of sale, including if the property was under financial distress.

Brokers' Outlook

According to HVS interviews with brokers active in the market, limited-service hotel cap rates range between 7% and 10%, depending on a property's performance history, with the rooms revenue multiplier (RRM) ranging from 2.5 to 4.5. Exposure time is anywhere from three to nine months, depending on the seller's motivations. Brokers report that now is a good time to either hold or buy, with typical risks involved. These investment parameters hold for select-service hotels; however, exposure time for these properties is forecast to be shorter, noting only a two- or three-month window. Full-service hotels are noting much lower cap rates, ranging from 3.5% to 9%, depending on the quality and location of the property.

Conclusion

Overall, the Seattle market boasts sound lodging dynamics, and the continuing growth in the area's employment is

expected to spread its positive effects to the local hotel industry. The only major concern at this time is the amount of current and rumored hotel development, which could significantly affect occupancy, average rate, and RevPAR should a high number of rumored hotels come to fruition. Otherwise, the overall outlook for the Seattle market remains optimistic.