HVS

MARKET REPORT

Monterey Peninsula

AUGUST 19, 2003

In 2001, the Monterey market area felt the effects and aftershocks of many of the same events that caused occupancies to plummet in the greater San Francisco Bay Area.

In 2001, the Monterey market area felt the effects and aftershocks of many of the same events that caused occupancies to plummet in the greater San Francisco Bay Area. The Salinas-Monterey market was one of five California markets, out of 22, to experience occupancy declines in the double digits, and one of only four markets to experience a decline in average room rate. According to Smith Travel Research overall occupancy in the Salinas-Monterey area declined from 71.8% for year-end 2000 to 63.0% for year-end 2001, representing a decline of 12.3%. Average rate moved in tandem with occupancy and dropped 2.2% from $116.49 in 2000 to $113.92 in 2001. The end result was a 13.4% decline in room revenue, the sharpest decline of any of the 22 California lodging markets studied. Year-to-date data, through the first five months of 2002, show modest declines in occupancy (2.6%), average rate (2.6%), and room revenue (4.7%). In terms of occupancy, the outlook is favorable for the year as occupancies will likely finish above last year in the third and fourth quarters of 2002 resulting in a year-end occupancy above that earned in 2001. Average rate growth is less likely however, as average rate through May 2002 was $2.78 below the average at the same time last year. The Monterey Peninsula lodging market includes properties located in Carmel, Marina, Big Sur, Pacific Grove, Salinas, Seaside, and the city of Monterey. The peninsula includes a range of lodging products, from the motels in the inland markets of Seaside, Del Rey Oaks, and Monterey, to the upscale resorts associated with Pebble Beach, Carmel, and Big Sur. As of January 2002 the area supported 151 hotels with 8,618 hotel rooms; of these, 59 hotels with 4,380 hotel rooms are located in Monterey. Due to high barriers to entry into the market, including limited space in areas zoned for lodging development, supply growth has been limited during the past decade. The city of Monterey has a moratorium on development that makes the probability of future development, beyond what is already approved, unlikely. According to officials at the Monterey County Convention and Visitors Bureau, approximately 1,000 new hotel rooms have been approved in five different projects throughout the county over the next few years. Among the projected new supply is a 230-room upscale hotel that is approved for a vacant parcel of land on Cannery Row. This property will be the last new lodging development in the city of Monterey unless the city's charter is amended. The extremely high barriers to entry into the lodging market throughout Monterey County will always keep the number of lodging facilities limited. As a result, the Monterey Peninsula will be able to maintain the small seaside community atmosphere that is so attractive to visitors today. Monterey County is located at the approximate midpoint of California's Pacific coast, placing it within easy driving distance from most of Northern California and the Central Valley. According the officials at the Monterey County Convention & Visitors Bureau, roughly 62% of visitation to the Monterey Peninsula was generated from the San Francisco Bay Area (in 2000). The tourism

industry in Monterey benefited greatly during the latter half of the 1990s from its location proximate to the bastions of high technology. Monterey's market mix was evenly split between the leisure and meeting and group segments. Individuals in the San Francisco Bay area used Monterey as a personal escape while firms located in the area used Monterey for company retreats. Monterey has also long been a favorite with government associations as it has historically been more affordable than larger convention cities such as San Francisco. While the San Francisco Bay Area will continue to be a primary feeder market to the Monterey Peninsula, in times of limited demand, the area is striving to market itself to other demand sources. Due to the large percentage of business from the greater Bay Area, particularly from Silicon Valley and San Jose, Monterey felt the effects of the weakening economy earlier than other parts of the state. By April 2001, the decline in occupancy percentage was in the double digits, compared to the same month in 2000. Percentage occupancy decline, compared to the same month in the prior year, would remain in the double digits through the summer. At summer's end, the events of September 11th and the ensuing proclivity to stay at home further wounded the lodging market. The Monterey Peninsula lodging market was the beneficiary of significant increased demand during the latter half of the 1990s, particularly from the burgeoning technology industry located within a two-hour drive. Hoteliers used this increased demand to foster above-inflationary average rate growth for five consecutive years. The icing on the cake was the hosting of the US Open Golf Championship in 2000, which provided opportunity for a roundly 12% rate increase from the previous year. A challenge now facing hoteliers in the area will be to maintain the high average rates that they have been able to charge in recent years. If the average rate trend from the early 1990s is any indication, rate growth may be extremely tough to come by over the next few years. Despite the current melancholy, overall, the Monterey lodging market is in an enviable position. Though the slump in demand has been felt deeply in the area, the limited supply will allow a faster recovery and lack of new supply will lead to above-inflationary rate growth in the long term.