

# Brokers brace for rash of hotel sales

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TULSA – Dan Falls has fielded increasing inquiries, while Stephen Karbelk has charted rising sales. Peter Holmes witnessed both.

By most accounts, hotel brokers expect a deluge of default or foreclosed properties. While this promises increased business, it raises fears of plunging hotel values.

“Our hope is that you don’t see the market just flooded with foreclosed hotels, because it will drive down the values and is sort of a self-fulfilling prophesy,” said Holmes, chief operating officer of Oklahoma City-based HotelBrokerOne. “The more hotels you put on the market at bargain-basement sale prices, the more it drives down the value of the other loans. It’s a cascading effect you don’t want to have.”

While Oklahoma’s hospitality sector outperforms national counterparts, it claims home to several brokerages targeting that continental market, from HotelBrokerOne to Tulsa’s established auction house Williams & Williams and the year-old upstart National Commercial Auctioneers.

With many analysts expecting 10 percent of the nation’s 40,000 hotels and motels to either default or be foreclosed over the next 12 to 18 months, this banquet may provide plenty for all – except that commercial mortgage-backed securities (CMBS) prop up a good portion of the underperforming hotels.

Early returns suggest those loan managers want to get out of their problems quick. That may point to the faster auction process over traditional property presentations and sale.

Karbelk, founder of NCA, is working through his seventh hotel auction this year, with more on the horizon.

“Of all the major commercial property types, we think hospitality is going to have the biggest opportunity for sales,” he said. “We think we’ll do anywhere from 15 to 20 hotels this year and we’ll be one of the top five hotel brokers in the country. They’re a complicated auction, because you’re not just selling the hotel, you’re selling the business. It’s a very tight, complex transaction.”

Falls, vice president of commercial real estate with Williams & Williams, expects increased action from the number of inquiries he’s handled.

“Most of those are coming from holders of boutique hotels, not from the large national chains yet,” he said. “I think they have deeper pockets and can ride it out longer.”

That mirrors the advice Holmes relayed to his clients.

“We as a firm have advised a lot of clients that if they can afford to hold and if they can make the capital investment to keep a property viable, or if it’s making losses, if they can afford to sustain the losses, then they should do so,” he said.

That strategy reflects the tremendous plunge hospitality property values endured the last two years.

“Among the top performers, we have not seen quite the dramatic drop-off, but we are definitely seeing values take a hit in the bottom 50 percent of the marketplace,” said Holmes. “Maybe 40 to 50 percent of the value of those properties has evaporated in the last 18 months or so.”

While he considers that something of an overcorrection, Holmes fears it could take 10 years before hotel properties return to their 2006 or 2007 levels.

“I would tend to agree with his comment,” Falls said. “You see an average of seven- to 10-year cycles, especially in hospitality.”

But he questioned whether owners of troubled hotels should wait for a recovery.

“Unless you truly had a crystal ball and knew of the time period, I fear you’ll have to wait out for some time,” Falls said. “This isn’t going to get better anytime soon. And for every day you wait is another dollar you’ve lost. The sooner you dispose of your hurting asset, the better you will be.”

Karbelk said divesting now, when things are worse, could actually speed commercial real estate’s healing process.

“I’m a clear believer in the ‘ripping off the Band-Aid’ approach,” he said. “You’ve just got to clear the bad properties off the market and then values will go back up again.”

But even Karbelk hopes the anticipated sales form a manageable flow and not a tsunami.

“What we have to be careful of is that it’s sort of parceled out methodically and not all at one time,” he said, echoing Holmes. “We don’t want to flood the market with too many deals. You want to make sure what needs to get sold, gets sold. The ones you think you can reposition and add value to, spend some time with those.”

Karbelk based his stand not on the perceived lower returns from auction, but from the lending market’s continued tight credit.

“The biggest challenge is still finding financing,” he said. “That’s putting downward pressure on pricing.”

While that may hold true on the national level, at an upcoming Square Feet Tulsa Roundtable several Tulsa bankers complained about recession-lowered loan demand. BOK Financial also raised that point in Tuesday's annual meeting.

"I can't tell you the last reasonable loan request in the commercial real estate arena that we did not approve," First Bank of Owasso President and Chief Executive Dominic Sokolosky said. "There's just not a lot of activity."

The differing views may reflect lowered market demand for the older properties dominating today's defaults.

"The buyers are gravitating towards the newer properties, as are the consumers, and so the older hotels are just getting tougher to finance and to sell," said Karbelk.

Many potential buyers at National Commercial Auctioneers events found alternatives to traditional loans.

"We're seeing a lot of buyers having investors backing them instead of a bank," Karbelk said. "That just takes a little more work to put together."

Williams & Williams auctions also have attracted a lot of cash buyers, said Falls, either with their own money or grouped pools.

"Very nice triple-net properties can still get funds, just like they could three years ago," he said.

Whatever course it takes, the potential sales activity promises a salve for many broker wounds. Holmes said HotelBrokerOne's year-to-date sales activity parallels 2009 – but that year suffered a 50-percent drop from 2008, which endured a whopping 80-percent plunge from 2007 marks.

"We see the second half of this year to have possibly as much as a 100- to 150-percent increase over last year," he said. "That's obviously what we're hoping for."

"We anticipate a great many properties coming to market," said Holmes. "We anticipate they will come to the market with a mandate to sell, which is great. If the mandate to sell is auction, that will be great for those National guys. We think a lot of those will come with a mandate to be listed and presented. We think we will sell quite a few properties."