Luxury Hotels Risk Default as $850 Rooms Remain Empty

Sept. 24 (Bloomberg) -- Luxury hotel owners risk defaulting on their debt as the recession cuts occupancies and the credit crunch constrains refinancing.

Loans secured by more than 1,500 hotels with a total outstanding balance of $24.5 billion may be in danger of default, according to Realpoint LLC, a credit rating company that tracks commercial mortgage-backed securities. Some of the biggest loans, put on the company's watch list because of late payments, decreasing occupancies or cash flow, were made to luxury properties where rooms can cost more than $850 a night.

"All segments are showing signs of distress but the luxury segment carries much higher loan balances and is more clearly affected," Frank Innaurato, managing director of CMBS analytical services at Horsham, Pennsylvania-based Realpoint, said in a telephone interview.

Lodging owners are struggling after adding rooms and properties at the peak of the CMBS market from 2004 to 2007, when $83.4 billion in hotel-backed securities was issued. Occupancy among chains with the costliest rooms fell to 60 percent in the first half from 70 percent a year earlier, according to Smith Travel Research. The decline was the industry's largest for that period.

"Luxury hotels have been aggressively financed during the peak CMBS issuance years," David Loeb, an analyst at Robert W. Baird & Co., said in a phone interview. "That's why luxury hotel loans crowd these watch lists."

Four Seasons

A $90 million loan secured by the Four Seasons San Francisco, a 277-room, five-star property, is 90 days delinquent and foreclosure proceedings have begun, according to Realpoint. A notice of default has been filed, according to Bloomberg data.

The borrower was Millennium Partners LLC, a real estate firm founded in 1990 by Christopher Jeffries. The company controls 1,860 residential units, more than 2,000 hotel rooms and 1 million square feet (93,000 square meters) of office space, Realpoint said.

Nicola Blazier, a spokeswoman for Four Seasons San Francisco, didn't respond to e-mails and phone calls for comment. Millennium principal Jeffries didn't return a call.

The Dream Hotel, a 220-room hotel on West 55th Street in New York City that features 300-thread count Egyptian bed linens and iPods, is collateral for a $100 million loan taken by Surrey Hotel Associates LLC that's at risk of default, Realpoint said.

The borrower is trying to restructure the debt and defer payments, said Riyaz Akhtar, vice president at Surrey.

More Defaults?

"What's happening to us right now is happening, and will continue to happen, to many hotel properties given the current market," Akhtar said in a telephone interview.

The U.S. hotel loan-delinquency rate may climb to 8.2 percent by year-end, Morgan Stanley analysts led by Andy Day said in a June 23 report. That would match the peak from the last recession in 2001.

Upscale hotels are suffering from "a heightened focus on prudent corporate travel expenditures," as well as the pullback in vacation travel, Day said.

Microsoft Corp., coping with its first annual sales decline, said in July it would slash $3 billion in operating expenses, including travel spending.

The number of luxury-brand rooms in the U.S. as of the end of July rose 9.1 percent from a year earlier to 100,000, Loeb said.

Occupancy Decline

A $190 million loan secured by the 640-room Arizona Grand Resort is 90 days delinquent, according to Realpoint. If the loan is liquidated it may lead to a $111.9 million loss, the credit rating company said.

The property's occupancy rate fell to 64 percent as of December 2008 from 70 percent a year earlier, Realpoint said. The borrower was

Pointe South Mountain Resort LLC, a Grossman Company Properties affiliate. Pamela Kerner, a spokeswoman for Phoenix-based Grossman, declined to comment.

Realpoint also is monitoring a $1 billion loan taken by CNL Hotels and Resorts, a company acquired by aMorgan Stanley real estate fund. The loan is secured by five properties with 14 golf courses, including the Arizona Biltmore in Phoenix and the Grand Wailea Resort Hotel & Spa in Maui, Hawaii.

Falling cash flow and weakening economic conditions put those properties on the watch list, Realpoint said. Revenue is sufficient to meet interest payments, and the assessed collateral value of $1.4 billion lowered the loan's risk, Realpoint said. Alyson Barnes, a Morgan Stanley spokeswoman, declined to comment on the analysis.

Westin Aruba

The Westin Aruba Resort & Spa, managed by Starwood Hotels & Resorts Worldwide Inc., was foreclosed on in May, according to Realpoint. The property is controlled by Wachovia Corp., the ratings company said.

The property's occupancy rate dropped to 41 percent in May from an average of 63 percent in 2008, the report said. Servicers are used when a loan is in or near default and needs to be reviewed or modified, according to Innaurato.

The Westin Aruba has been hurt by competition from a 450- room luxury resort built next door, Realpoint said.

Another property on Realpoint's watch list is the Four Seasons New York, where a standard room with a king-sized bed starts at $855 a night. The hotel is among four used as collateral for a $344.6 million loan, Realpoint said.

The properties' occupancy rate fell to 57 percent in the 12 months through June. At the end of 2007 and 2008 it was 73 percent and 69 percent, respectively, Realpoint said.

'Moderate' Risk

Four Seasons New York's net cash flow "is well below historical trends," the credit rating company said, without being more specific. While the property's revenue per available room and net cash flow have jumped since bottoming in 2003, the hotel "is more recently showing signs of New York's weakening economy," Realpoint said.

The property is owned by Ty Warner Hotels & Resorts.

"We consider this loan a moderate default risk based on declining performance along with the lower expectations on the lodging-resort industry given the current economic conditions," Realpoint said in its report. "Our analysis of the collateral suggests that the combined value of the assets are below the current loan amount."

Donna Snopek, chief financial officer of Ty Warner Hotels, said in an e-mail that the loan "is performing well."

'No Impact'

"Moreover, the properties in the pool are all performing at the top of their respective markets," Snopek said. "We are fully committed to our loan and can assure you that there is no impact to the current high standard of services at this property."

Lowe Enterprises Inc. of Los Angeles, the operator and developer of a 582-room resort on the Pacific Coast, said in August it's trying to restructure a mezzanine loan after defaulting two months after the hotel opened.

The Terranea Resort in Rancho Palos Verdes, California, a $480 million property, opened June 12 with a golf course, three pools and eight restaurants. Lowe is among a group of investors in the property and is in negotiations about restructuring the loan, spokeswoman Jann Diehl said.

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