Hotel defaults, foreclosures rise in California

In the state, defaults and foreclosures are up fivefold since Jan. 1.

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More California hotels are being pushed into foreclosure as tourists and businesses alike scale back their travel plans and owners are unable to pay their mortgages.

Statewide, more than 300 hotels were in foreclosure or default on their loans as of Sept. 30 -- a nearly fivefold increase since the start of the year, according to an industry report released Tuesday.

The list of troubled properties includes the St. Regis Monarch Beach in Dana Point, the downtown Los Angeles Marriott, the Sheraton Universal and the W hotel in San Diego.

Most struggling hotels remain open, but industry experts believe many properties are likely to be closed down in the months ahead, even if they are not in foreclosure, because they are losing so much money. The owners of the renowned Quail Lodge Resort and Golf Club in Carmel, for example, plan to close the hotel Nov. 16.

"I have never seen so many lenders contemplating mothballing properties," said Jim Butler, a hotel lawyer and chairman of the global hospitality group for Jeffer, Mangels, Butler & Marmaro. "It can and it will get worse for the hotel industry."

The problem is not unique to California, but the effect is being felt especially hard here because of tourism's importance to the state.

In Southern California alone, there were at least 140 hotels in default or foreclosure in September, including 55 hotels in the Inland Empire, 33 in Los Angeles County and 30 in San Diego County, according to the report by Atlas Hospitality Group. Statewide, 260 hotels were in default on their loans and 47 had been taken over by their lenders in foreclosure, the Atlas report said.

The industry's woes are compounded by the sour commercial real estate market, which has left many resort operators owing more than their properties are worth. Even as they struggle to make payroll, scores of resorts and inns have given up on paying their mortgages, fueling the skyrocketing level of defaults.

"It's a prolonged downturn, and it will be a long time before we get out of it," said hotel broker Alan X. Reay of Atlas Hospitality, who tracks foreclosures and defaults in the state.

Part of the problem is that unlike home loans, mortgages on larger hotels typically are supposed to be repaid in full after five to 10 years. Many of them are coming due now. But like their residential counterparts, many hotel owners refinanced their places at the top of the real estate market, often taking equity out of their properties. So the loans are ballooning at just the time when there are few guests at the hotels, and the properties are worth little.

"We expect this number to rise dramatically by the end of the year and into 2010, because we're seeing so many hotels operating under forbearance," Reay said.

Industry leaders blame the slump on several factors, including loose lending and irrational exuberance during the boom, an increase in new hotel openings because of the easy money, and a dramatic drop in business travel.

Joseph McInerney, chief executive of the American Hotel and Lodging Assn., tried to put a positive spin on the news, saying, "I think we've bottomed out."

But a leading hotel consulting firm, Smith Travel Research, recently issued a report that predicted no significant improvement for the hotel industry until 2011 at the earliest.

"It's going to be a lot worse than it is now," said Bobby Bowers, senior vice president of Smith Travel Research.

Cities such as Las Vegas, San Francisco, New York and Los Angeles may have a harder time recovering, Bowers said, because businesses remain reluctant to budget for travel and entertainment in cities with reputations for lavish spending.

Bowers partly blamed this on the continuing backlash to news last year that giant insurer American International Group Inc., teetering near collapse, had spent about $400,000 on a retreat at the St. Regis Monarch Beach after taking an $85-billion federal bailout.

Reay said there were comments about this "AIG effect" at a conference he attended last week.

"People were saying that if you've got 'resort' in your name -- you're a golf resort, a spa, whatever -- you have to take it off," he said. "Because the business traveler isn't going to get reimbursed unless it's just the plain Hilton hotel."

At local hotels, managers and owners say they have had to rely on deep discounts and promotional packages just to keep the doors open and staff employed.

"Sometimes you have to do what you have to do," said Marc Loge, a spokesman for the Wilshire Grand hotel in L.A.

David Horowitz, general manager of the Hyatt Regency Century Plaza, said rate cuts and promotions had become almost standard. "We do have to make deals," he said. "We have to keep things going."

But an increasing number of hotels have so little revenue that they can't even afford to pay their operating bills and payroll, not to mention servicing debt.

Owners of such hotels are increasingly handing the keys back to the lenders, and the problem is likely to get worse: As many as 1 in 5 U.S. hotel loans may default through 2010, UC Berkeley economist Kenneth Rosen said.

In some cases the lenders are simply locking up the properties, figuring they'll spend less money on watering the lawns and paying a few guards than they would on keeping the doors open.

A real estate investment trust that owns 40 upscale hotels in the U.S. recently announced plans to forfeit a 293-room Marriott hotel at the airport in Ontario to the servicer overseeing the hotel's $26.6-million mortgage. The investment trust, Sunstone Hotel Investors Inc., based in San Clemente, had announced plans in June to forfeit the 258-room W San Diego hotel because it would not support its $65-million mortgage.

The hotel industry continues to buzz about how that happened this year in the Bahamas, when a lender closed the Four Seasons Resort Great Exuma, a $350-million property built in 2003.

Small resorts also have closed in Big Bear and South Lake Tahoe, the latter involving an owner who allegedly tried to hold down costs by not paying the local room tax imposed by the city and was arrested.