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Chicago racked by room glut

Hotel market hit by declining demand, falling rates as new properties open and compete for dwindling tourism dollars

By Mary Ellen Podmolik | Tribune reporter
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The Wit, a boutique hotel that opened in the Loop last week, seeks to impart a playful, chic sense of humor on its guests. For local hoteliers, though, there isn't much to smile about.

Hotel occupancy and average daily room rates have posted double-digit percentage drops over the first four months of this year compared with the same time last year.

The decline is to be expected, given that consumers have pulled back discretionary spending and tourism is down nationally. The catch locally, though, is that the numbers are unlikely to improve as the summer travel season gets under way and consumer confidence improves, because the law of supply and demand is off kilter. Despite demand being down, the city's supply of hotel rooms is on the way up.

The opening of four new hotels, plus extra rooms that will join the inventory at Trump International Hotel & Tower, will add 989 rooms to the downtown Chicago market this year.

Mark Eble, Midwest vice president of hotel consultant PFK Consulting, predicts that in the greater Chicago area the revenue per available room, a critical industry benchmark, will be down 18 percent this year.

"The hole that we're in now is one of the worst that anybody alive has seen, but Chicago is not as bad as many other cities," Eble said. "Cleveland and Detroit would love to have Chicago's worst day."

Existing hotels are offering sizable discounts in a bid to entice visitors to sleep at their properties rather than a competitor's. In April alone, the average room rate in downtown Chicago hotels was about \$162 a night, 23 percent less than the roughly \$210 per night guests paid during April 2008, according to data from Smith Travel Research Inc.

As a result, total revenue for the 35,000-plus rooms in downtown Chicago has plunged 25 percent year to date.

"If you have the confidence to travel, there are bargains to be had all across the board from the top-of-the-line luxury hotels, but saving 30 percent on a \$500 room is different than saving 20 percent on an \$80 room," said Chicago hospitality consultant Ted Mandigo. "It gives people that might have traveled to the three-star [hotel] the opportunity to experience the four- and five-star service."

The newest entrants in the market are feeling the pressure. Marketing budgets have been increased, local residents are being invited to sample restaurant menus, and employee work

schedules have been made more flexible. And while new hotels typically offer special introductory rates to attract business, the newcomers are quoting rates lower than those in the financial projections made to lenders that helped them secure funding two to three years ago when tourism was hot.

"It's a cyclical industry, and we're in a down market," said David Pisor, founder and chief executive of Elysian, which opens July 15 on Walton Street near State Street. "In some ways it's an advantage because you open leaner and more hungry."

At The Wit, ECD Co. President Scott Greenberg concedes his introductory rates are \$30 lower than he originally planned, the menus at the three restaurants have been made more value-oriented, and he has opted not to market the 60 hotel condos in the \$100 million property at State and Lake Streets. Still, he said he plans to "prove a lot of doomsayers wrong that you can't build a new hotel in the Loop."

Part of the reason for Greenberg's optimism is that he has time on his side. Two years ago, when he negotiated the \$82 million construction loan with Capmark Finance Inc., Greenberg was able to get an additional four years to pay it off.

"Sometimes it's better to be lucky than smart, and this is one of those times," Greenberg said. "We pushed for four more years of term, and who knew?"

The two other new names downtown are LaQuinta Inns & Suites, which opened at Madison and Franklin Streets last month, and Hotel Felix, which markets itself as an eco-friendly boutique hotel that opened in March near Huron and Clark Streets.

"We are ahead of budget, in rate and occupancy, which I'm frankly flabbergasted by in this environment," said John Rutledge, president and CEO of Hotel Felix owner Oxford Capital Group LLC. "That doesn't mean there are as many people showing up or spending as much money or staying as long, because that's not the case."

Rutledge partly attributes the early success to the fact that Hotel Felix was a rehab of Hotel Wacker, bought in December 2007 at 40 percent of the replacement cost and financed with "plenty of cushion."

"We wouldn't do this kind of deal now, but we're glad we did this deal," he said.

Meanwhile, Rutledge has pushed off the redevelopment of 13 floors of the [IBM Building](#) on Wabash Avenue into a hotel. Likewise, Greenberg has no immediate plans, or financing, to push forward with Aloft [Millennium Park](#) at Balbo Avenue and Wabash and Aloft [Lincolnshire](#).

Such delays, and there are plenty of them, are actually the silver lining to the predicament the market finds itself in.

Two years ago there was a laundry list of hotel projects planned for Chicago. Those plans have since been scuttled or mothballed until the market improves and financing becomes available.

The most visible sign of the market's seizing is the Shangri-La, whose unfinished concrete shell sits at Wacker Drive and Clark. Had those properties continued, the glut of rooms in the market would have been worse, and any rebound would have taken longer to achieve.

"There's stuff on drawing boards, but the drawing boards have been put in dusty closets," Greenberg said.

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