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Builders Pull out of Hotel Ventures as Profits Dry up

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Leading property developers are pulling out of proposed deals with hospitality majors, including Royal Orchid Hotels and Ramada Worldwide, as cash flows in the real estate sector are slowing. Realtors are reconsidering plans to enter the hospitality sector, according to sources.

Real estate developers with presence in National Capital Region (NCR), Bangalore, Chennai, Pune, among others, are opting out of four and five-star hotel projects. According to sources, a five-star hotel in Pune shelved its plans recently as its developer pulled out of the commitment.

“The return on investment in a hotel will not be as high as it will be in putting the land to commercial use. Committing to the hospitality sector means waiting for five or more years (till the hotel becomes operational) to get returns,” says Shivaram Malakala, executive director of Habitat Ventures, Bangalore.

“Developers are looking at realising their money through any alternative means and are thus in the exit mode,” he says.

However, Wyndham Hotel Group International, which is promoting Royal Orchid Hotels and Ramada Worldwide, has denied any such development.

Says Sunil Mathur, director (international development), Indian Ocean Region, Wyndham Hotel Group, “All our projects are doing fine. They could be delayed by a month or two but none of them have been shelved.”

While Bangalore is said to have around 10 such properties up for sale, NCR has over five properties. Last year, over 20 four-star hotels were slated for construction in Bangalore, of which six properties have begun operations.

According to a Mumbai-based hospitality consultant, the developers are facing cash crunch and have either put the property (unfinished buildings in some cases) on sale or have asked the hotel companies to find them partners who can invest in the venture.

Properties that were worth Rs 30 crore, for instance, are being sold at a discount of over Rs 25-50 lakh. To be sure, players in the field believe that this slowdown could benefit the big players in the market and hoteliers will look to acquire land in areas where it was otherwise difficult for them to make purchases.

“If the real estate market slows down and there is still demand for hotel rooms in that micromarket, a developer might want to mitigate his risk of holding on to unsold inventory by considering lower immediate returns in a hotel project,” says Shreenath Shastry, national director (hospitality and leisure), Knight Frank (India).

In 2007, over a dozen global chains, including the Hilton, Accor, Marriott International, Berggruen Hotels, Cabana Hotels, Premier Travel Inn and InterContinental Hotels group, announced plans to set up over 350 five-star, four-star and budget hotels and 50 villas in India.

Most of these chains joined hands with real estate developers. The plans would roughly translate into 65,000 additional hotel rooms a quantum leap, considering that over the past decade the total number of hotel rooms in all categories only grew by 10 per cent to about

92,000 rooms.

The slowdown in the real state sector can, however, soften the occupancy rate of hotels in the metros and leisure destinations, say analysts.

The occupancy rate in metros at present is between 75 to 80 per cent, which could go down to around 70 per cent in the next few months as the off-season will begin. "If the off season is weaker than usual, there could be a down grading of hospitality stocks," said an analyst.

"Builders could be putting the land to commercial use as the land rates (FSI cost) are too high (more that 50 per cent of the cost of the project for a hotel), and the commercial market is bullish. Also, a particular micro market may see many hotel rooms coming up, as a result of which a non-hotelier developer may develop cold feet.

Feasibility studies to that effect have a tendency to scare a developer as it is easy to predict supply and difficult to predict demand for hotel rooms," adds Shastry.
