TR Mandigo & Company
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338 N. Highland Avenue
Elmhurst, IL 60126
(630) 279 - 8144
TedMandigo@trmandigo.com

Analysis of Market Conditions

Analysis of Market Conditions for The O'Hare Hotel Market
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Prepared by:
TR Mandigo & Company
338 N. Highland Avenue
Elmhurst, Illinois 60125
TEL: (630) 279-8144
FAX: (630) 279-4701

The O'Hare market area is heavily impacted by air passenger traffic, such that the lines between traffic and occupancy are basically parallel.   Unlike many other areas, O'Hare had a relatively quick recovery from the worst of the recession, and managed to move ADR up by 5% in 2011.

O'Hare International Airport statistics hit their peak in 76,581,145 passengers in 2006, then declined with caps imposed by the FAA to minimize passenger delays and reduce ground traffic congestion during peak "pushes".   With the runway expansion and opening of a new runway and taxiway in 2009 these caps were lifted, and despite the current recession, air passenger traffic is rebounding. With the continued construction and release of capacity we expect the statistics to reflect a continuing growth, reaching and exceeding the historic highs. The charts on air passenger traffic are presented later in this report.

Colliers reports on office statistics for the metro area with the O'Hare sub market data indicating the current office supply, vacancy rate, asking lease rates and absorption. The current inventory of office space as of the 1st quarter of 2012 is 14,291,911 square feet with a vacancy rate of 22.6%, down 0.4% from 2011. It remains just above the strong performance of the north suburban and west suburban markets around Deerfield and the Oak Brook/Naperville clusters, though its condition is improving while they are losing tenants. The asking rate of $30.64 per square foot for class A space is the highest of all the suburban markets, and the newly opened 137,000 square foot Wintrust Financial Corporation lease demonstrates the strength of this market. The absorption rate reflects a recent negative trend with a drop of 40,000 square feet of class B space on a year to date basis.

The convention activity at Rosemont is centered on the Donald E. Stephens Convention Center and the Hyatt Regency O'Hare as the major facilities in the suburban market. These two properties compete strongly for mid-sized groups with both the Chicago Central Business District properties and mid-sized metropolitan areas throughout the mid-west. The 840,000 square feet at the Stephens Center historically catered to the commercial segment, but with increased competition and price negotiations from McCormick Place the market has shifted to public shows and local business activity.   We have estimated about 1/3rd of the total market accommodated in the O'Hare area is convention and corporate group based. Airport area hotels also pick up some overflow from the 90 fill days in the Chicago CBD and activity in the local area.

The new Rivers Casino opened strongly and has remained the highest by far than any of the other Illinois operations. Its year end attendance was 1,946 Million with a mid- July opening date, generating $50.5 Million in taxes. Thus far, it has remained quite strong in the first part of 2012, over doubling the attendance and revenue of the other casinos in the state.   It appears to be harming the business of these other facilities somewhat, though attendance is up 23% over last year.   Packaging and interaction with that area amenity will continue to provide only a little additional support for area hotel development, as its business is likely almost entirely day trippers.   If a hotel is built on the casino site, it may capture some of that business, but it is best to think of it as an additional area amenity, rather than a source of demand for hotel nights.

EXISTING SUPPLY

The current market at O'Hare consists of around 53 properties, depending on the definition. The area it covers includes portions of Des Plaines, Chicago as it parallels the Kennedy Expressway (I-90), the entirety of Rosemont, and portions of nearby suburbs including Schiller Park and Norridge.

Despite the large number of hotels, many of these are small or independent hotels, and of the larger properties, a significant number are over 40 years old. These properties generally drive down the overall average daily rate significantly, and also negatively affect the occupancy percentage.

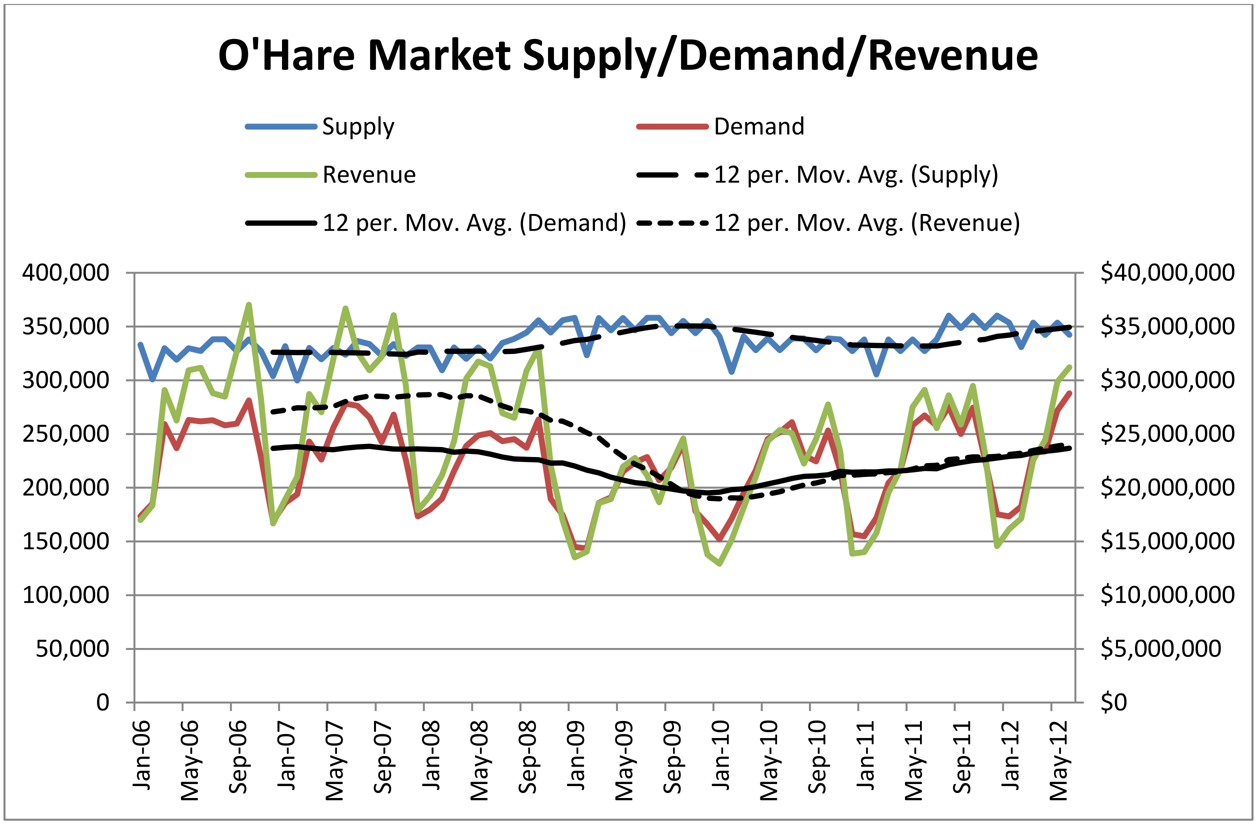
Of the hotels that remain, a number of midrange and upscale properties serve the immediate area. Most of these properties lie along three major thoroughfares: Mannheim Road, Des Plaines River Road, and Higgins Avenue, or a side street of one of the three. These hotels represent the construction boom of around the year 2000, and before that, the mid-to late 1980's. A few properties in the area were built around or before 1970. These midrange hotels tend to be under 250 rooms, generally provide shuttle service to the airport, and include a moderate amount of meeting space. They may target either business travelers or families, or small groups.

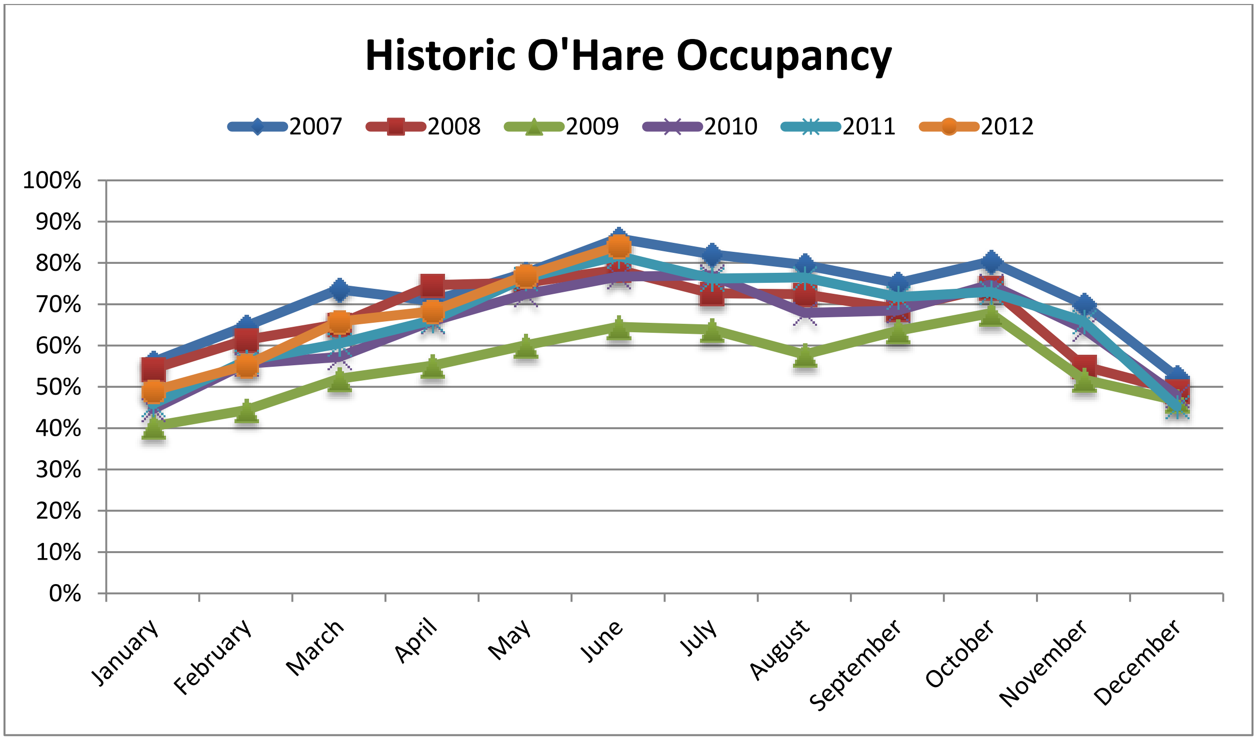
When most people think of Rosemont, they probably think of large hotels, and for good reason. After downtown Chicago, Rosemont has by far the largest number of large hotels in the region. While a few large hotels were built in the region prior to 1970, including the 470 room **Marriott Hotel**,the construction of the 1,096 room **Hyatt Regency** in 1971 cemented River Road in particular as the heart of area hotel development. The 860 room **Hilton O'Hare Airport** followed in 1973, and the 503 room **Crowne Plaza** joined in 1975. During the rapid growth of the mid-1980's, the 525 room **Westin**, 295 room **Four Points**, 294 room **Embassy Suites**, 300 room **Hilton Rosemont**, 256 room **Marriott Chicago Suites**, and 180 room **Courtyard Chicago** were all built on or near Des Plaines River Road, surrounding the Donald E Stephens Convention Center (itself built in 1975).

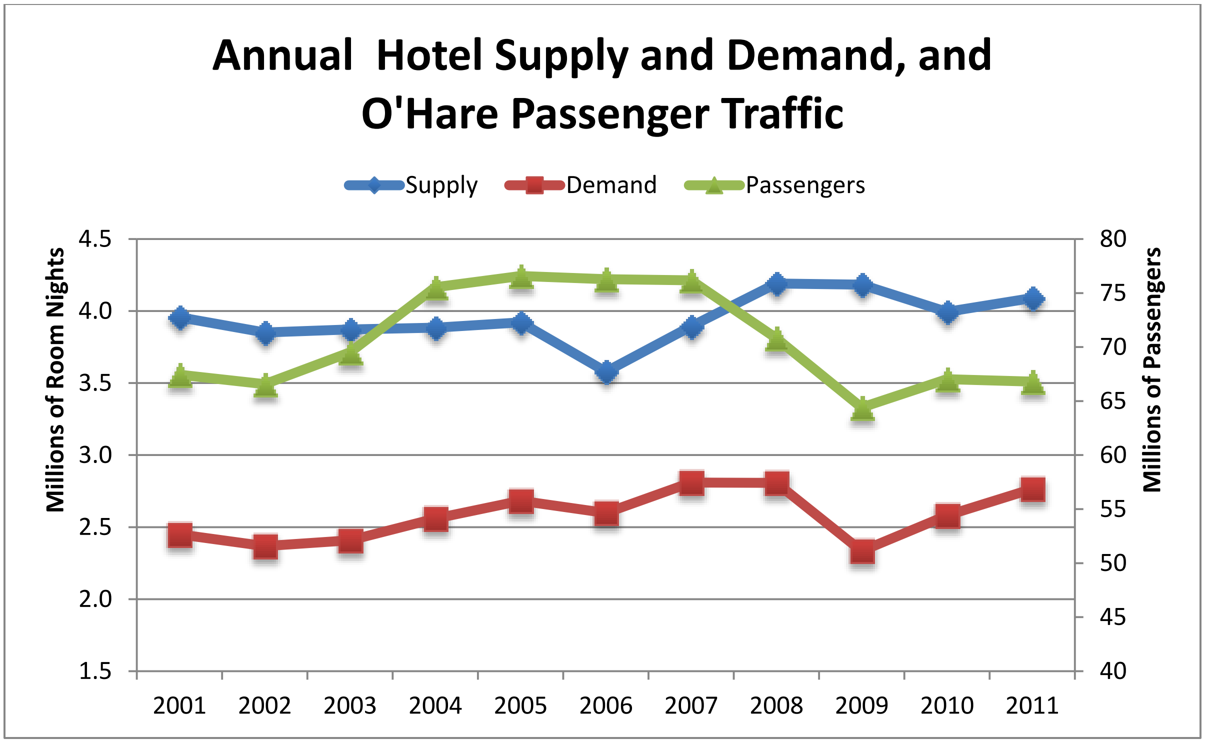
Later additions to the area include the 362 room **Renaissance**, 369 room **DoubleTree**, 251 room **aloft**, and the 556 room **InterContinental**.

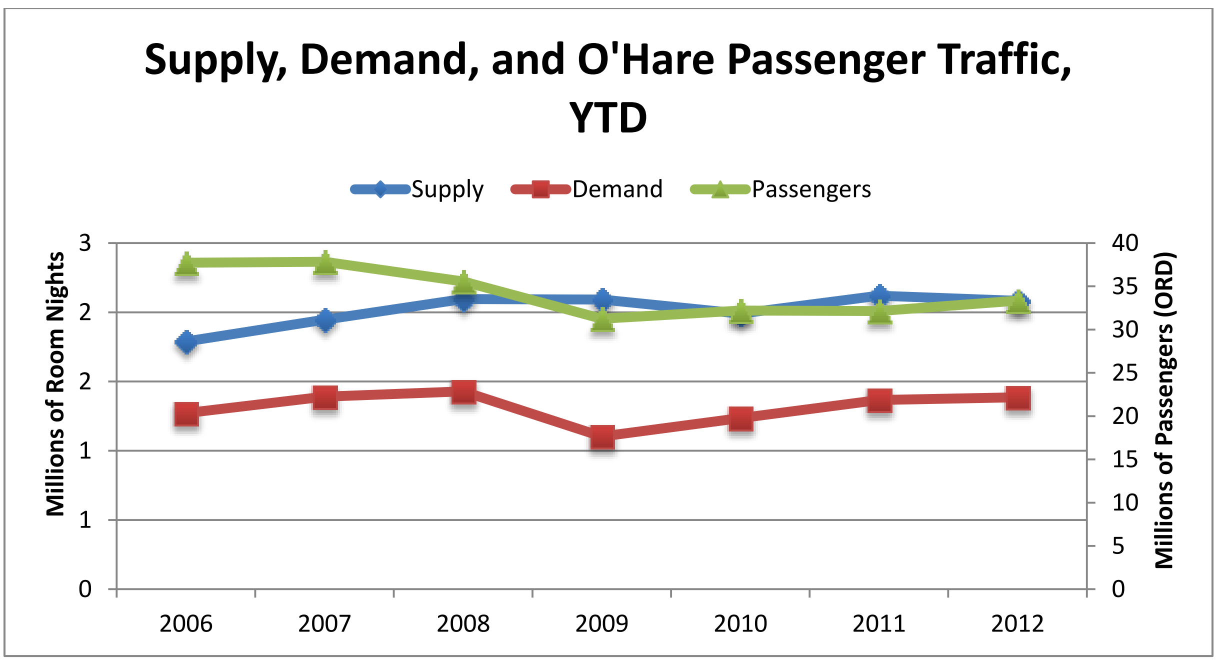
Hotel business at the airport follows a seasonal pattern similar to air travel, with peaks occurring in early summer and early fall. Although the airport and surrounding area includes both business and leisure traffic it's obvious from the statistics as presented that the largest portion of the total demand is derived from the business travelers through O'Hare. The higher rates and convenience of the location to serve the metro area contribute to the higher level of business patronage.

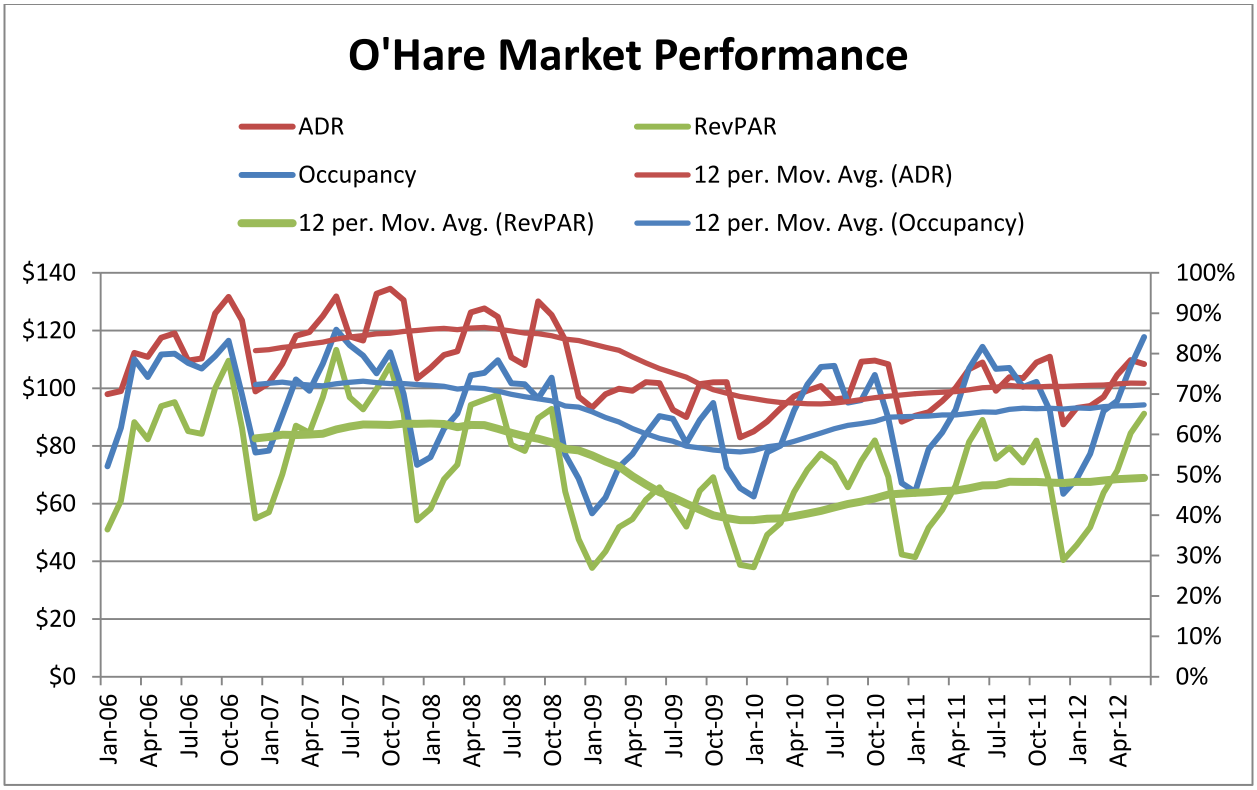
Much of the leisure travel is airport related, enhanced by local promotions by area properties for weekend events and package pricing. This is supplemented by the attendance at public shows at the Donald E. Stephens convention center and larger convention based hotel operations.


O'Hare Market Supply/Demand/Revenue
Supply
Demand
Revenue
12 per. Mov. Avg. (Supply)
12 per. Mov. Avg. (Demand)
12 per. Mov. Avg. (Revenue)
400,000
350,000
300,000
250,000
200,000
150,000
100,000
50,000
0
$40,000,000
$35,000,000
$30,000,000
$25,000,000
$20,000,000
$15,000,000
$10,000,000
$5,000,000
$0
Jan-06
May-06
Sep-06
Jan-07
May-07
Sep-07
Jan-08
May-08
Sep-08
Jan-09
May-09
Sep-09
Jan-10
May-10
Sep-10
Jan-11
May-11
Sep-11
Jan-12
May-12


Historic O'Hare Occupancy
2007
2008
2009
2010
2011
2012
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
January
February
March
April
May
June
July
August
September
October
November
December


Annual Hotel Supply and Demand, and O'Hare Passenger Traffic
Supply
Demand
Passengers
Millions of Room Nights
Millions of Passengers
4.5
4.0
3.5
3.0
2.5
2.0
1.5
80
75
70
65
60
55
50
45
40
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011


Supply, Demand, and O'Hare Passenger Traffic, YTD
Supply
Demand
Passengers
Millions of Room Nights
Millions of Passengers (ORD)
3
2
2
1
1
0
40
35
30
25
20
15
10
5
0
2006
2007
2008
2009
2010
2011
2012


O'Hare Market Performance
ADR
RevPAR
Occupancy
12 per. Mov. Avg. (ADR)
12 per. Mov. Avg. (RevPAR)
12 per. Mov. Avg. (Occupancy)
$140
$120
$100
$80
$60
$40
$20
$0
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Jan-06
Apr-06
Jul-06
Oct-06
Jan-07
Apr-07
Jul-07
Oct-07
Jan-08
Apr-08
Jul-08
Oct-08
Jan-09
Apr-09
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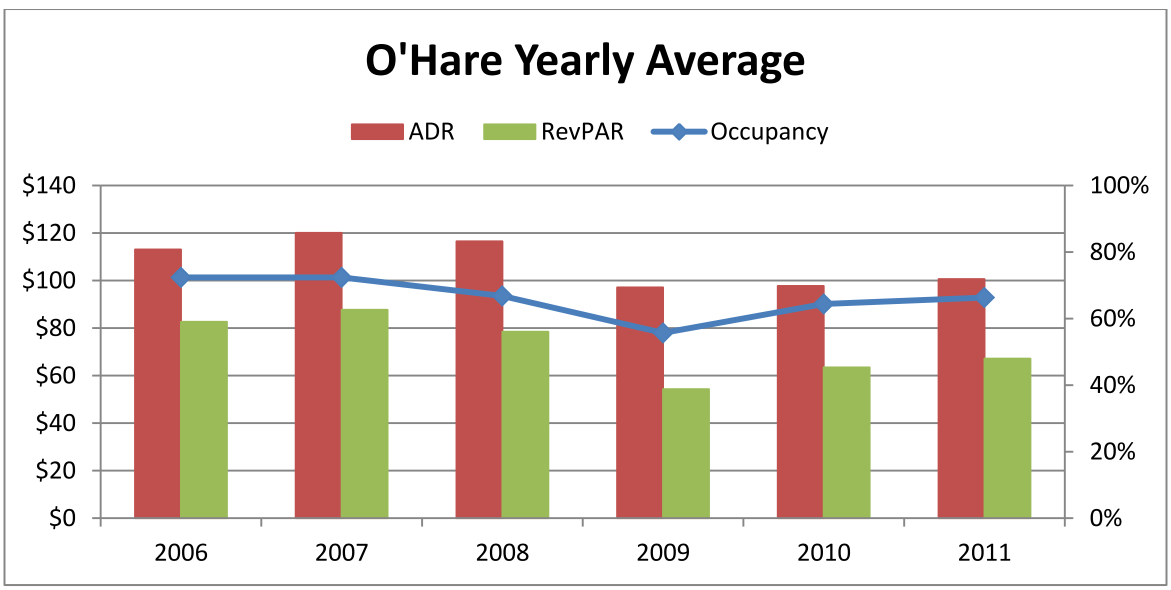
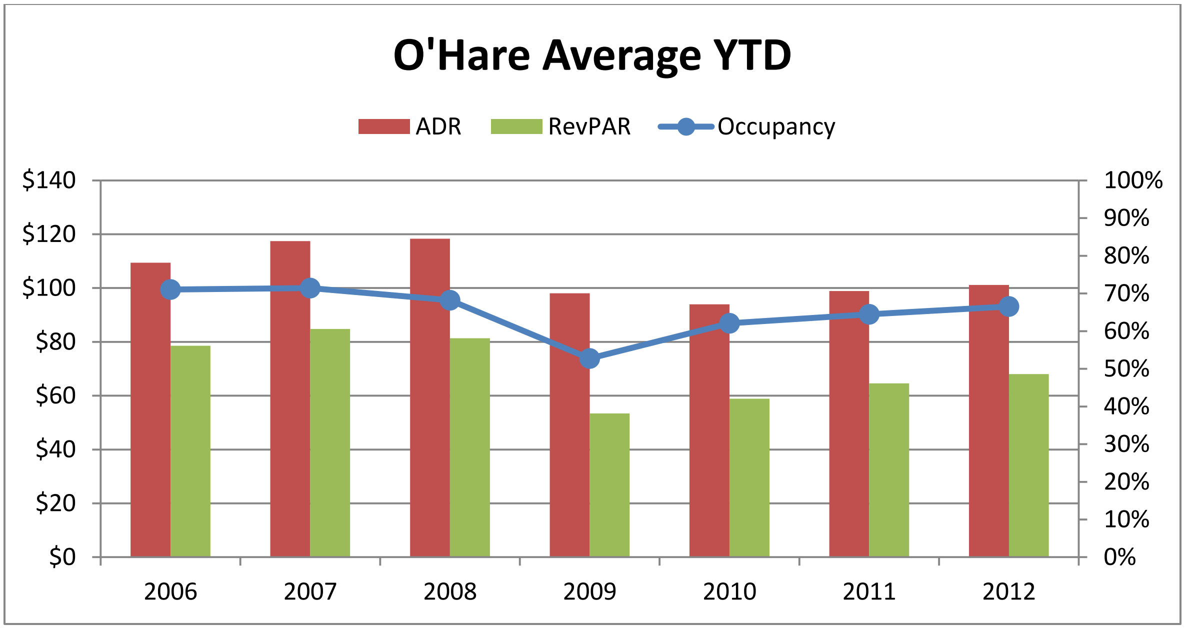
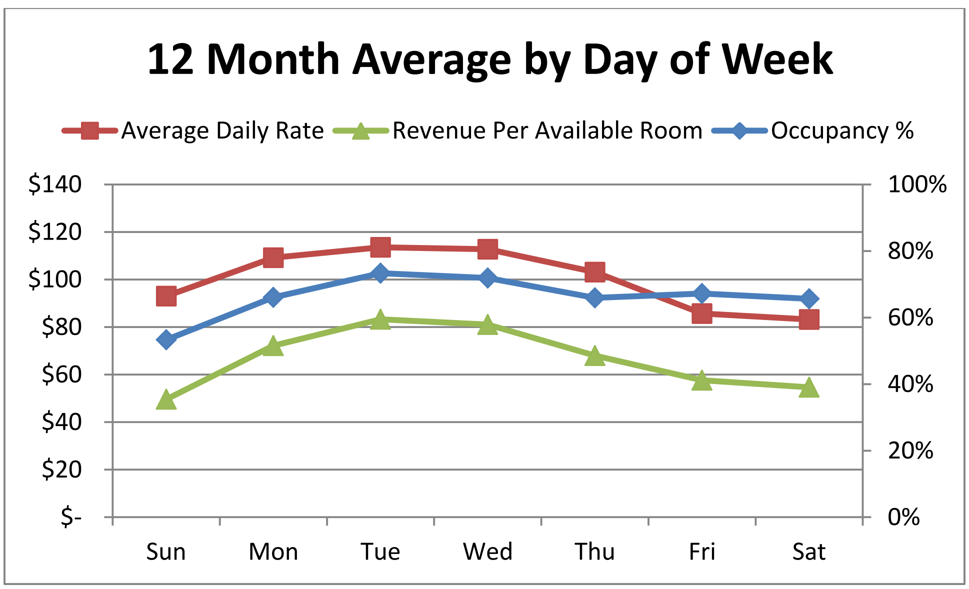
Oct-11
Jan-12
Apr-12


O'Hare Yearly Average
ADR
RevPAR
Occupancy
$140
$120
$100
$80
$60
$40
$20
$0
100%
80%
60%
40%
20%
0%
2006
2007
2008
2009
2010
2011





OVERALL MARKET PERFORMANCE

The O'Hare market, despite being on the outskirts of Chicago and separated from downtown by at least 30 minutes of travel under the best of conditions, behaves more like the downtown market than the surrounding suburbs. This is clearly seen in the way that the market recovers from recessionary periods. For the clearest example, we contrast this performance with the downtown market and nearby DuPage, as numbers in most northwest suburban markets are generally at or below these levels. The relationship between the downtown, suburban and O'Hare markets has historically resulted in a stronger performance for the O'Hare market area.

In broad terms, the O'Hare market is a secondary market, or the first overflow market, from downtown Chicago. This is because, in very generic terms, assuming the Chicago MSA was a wheel; both the commercial and cultural center would be located in the Downtown area. Though there are numerous businesses, and major demand generators located in the immediate area, as a rule of thumb, the average guest would likely prefer to stay downtown, all things being equal. Of course, the pricing, proximity to destination and personal factors all play a very important rule in hotel selection. The reason for making this distinction at all, is that it is important to understand that while O'Hare is a secondary market when compared to downtown, it has a much stronger draw than the surrounding suburbs.

For example, although occupancies and rates dropped precipitously in 2009 across all segments, DuPage remains well below the O'Hare market to this day. A longer historical view confirms that the DuPage Market is not as strong as it was 10 years ago. This results from a loss of the overflow business from the downtown market that provided some overflow to surrounding areas for 60 to 90 fill days annually. With the additional supply in the downtown market and reduced convention attendance, this support level was lost during the 2001 recession and the suburban market never recovered. The O'Hare market, on the other hand, has retained some of the overflow as it is the most convenient and logical referral market for major convention activities. In addition, unlike many other markets, the O'Hare area has sufficient infrastructure to support large groups and business clients compared to all other areas, except downtown. Thus the O'Hare market, while impacted as strongly as the rest of the suburban markets as travel diminished, recovered more quickly and will sustain that improved performance, paralleling the CBD performance as demand stabilizes to pre-2009 levels.

In the past 3 years, strong supply growth occurred in all three markets, although this was offset slightly by numerous closures. At O'Hare, for example, the conversion of the old Sofitel to a Hilton, and the impact of the 556 room Intercontinental Hotel opening was partially offset by the closing of the Wyndham and the closing of rooms at the Hyatt for renovation. The new supply entering the Chicagoland market, broadly speaking is generally fairly upscale, while closures tended to be older properties. These newer properties have faced considerable hurdles in entering the market, and in the case of the Intercontinental, haven't yet achieved their target occupancy or rates.

Numbers show that recovery is already well underway, with occupancies increasing in virtually all markets last year, with some slight gains in average daily rate. These gains are still well below historic highs.

The drop in both occupancy and rate that the suburban markets have seen when compared to the highs achieved in 2007 is going to take longer to come back up, as the many overflow days they traditionally counted on are essentially gone. We anticipate that 2012 will see the O'Hare market increase by 4 percent in ADR within the next year, and around another 2.5% in occupancy, or around $105 and 68%, although this will still put it well below its historic highs.

The suppression of rate increases is exacerbated by the increasingly competitive corporate and leisure meetings market where new products and a more aggressive marketing program by all the area properties has led to rate compression during all but the very peak spring and fall convention seasons. The impact of these rates will gradually offset by more aggressive pricing strategies in the commercial sector and peak meeting periods.

The slower rate recovery is also attributed to the lead time for booking larger groups at the large convention hotels, where group rates were negotiated during the dog days of the recession. It will take another year to burn off the pre-committed lower rate positioning in place during the lowest part of this recessionary cycle.

Other factors influencing rate discounting include the extensive corporate contract discounts employed by either existing agreements with the market's franchises or aggressive pricing from the operators in the market area. Marketing and sales for most hotels in the group of significant hotel operations within the defined market are fairly aggressive due to the abundance of competition in the market.

Incredibly short lead times on bookings are the new reality, and we still don't know how to deal with it. The rates go all over the board because while we all know that we need to be able to manage revenue closely; we can't do it very effectively with these lead times. We see this continuing into the future and as an industry we need to adapt to this new reality.

In addition, continuing pressure from OTC (Online Travel Companies) as a primary referral channel has served to slow down rate growth considerably.

For many of the suburbs, downtown overflow has dried up, so demand has to be generated by localized sources. Fortunately in the case of O'Hare, one of the largest demand generators around lies just off their doorstep. In general, the hotel market lives and dies with airport traffic, which is affected by gas prices and the overall economy. Essentially, this market is hyper-sensitive to these fluctuations, and the strength of the market always closely reflects general economic conditions. As such, it is one of the first places to be hit by any downturn.

However, we feel that O'Hare should bounce back much faster than the suburban market in general, as it always has done, historically. Because it actually has a strong demand generator, when business returns, it is able to ramp up quite quickly. We would estimate a relatively strong increase in ADR in the market in general. We also anticipate somewhat strong occupancy growth in the future, though we have capped the market at around 73% Occupancy based on historic performance. Given current trends and market recovery the airport market should rebound to this level by 2015.

There are several projects in the planning stages, though we anticipate that only a few will open in the near future.

RECENTLY COMPLETED AND PROPOSED PROPERTIES

The site of the O'Hare Garden Inn on Higgins Road, between the Spring Hill Suites and the Marriott is the location of a planned 994 room platinum LEED hotel complex, called the Platinum Chicago Convention Center, including 4 separate brands, a 1,365 foot parking deck to meet zoning requirement and over 190,000sq/ft of common area shared meeting space. This project has been in planning stages since at least 2006, though has yet to get off the ground. The project is dependent on the international financing program currently pursued by the developer.

The Nursery Site, proximate to the Marriott on Higgins Road at Dee Road (NE River Road) has been discussed as a potential hotel site on several occasions. As the market rebounds it's possible the project would be revived. The most recent plans for this site were for a 250 room limited service property. The project is a planned development by the City of Des Plaines, and has been the subject of speculation since at least the year 2000, though plans have been tabled several times in the past during recessions. The other components of this development are of more interest to the developer and he has put out feelers for a company to develop a hotel on the site. It is unlikely to move forward at the present time.

Raymond Management Co. out of Middleton Wisconsin has had a long term plan to construct a 220 room Hampton Inn & Suites at the northwest corner of Higgins and Des Plaines River Road. Like many other projects, plans were put on-hold in 2008, though according to STR it has resumed as of May 2012, and so should open in June of 2014.

The Airport Authority is discussing the development of an additional on-property hotel at the International terminal, similar to the Hilton, but smaller in size. Early estimates place it at 350 rooms, and would link it to the terminal. It would be a full service property with moderate meeting space, and would be subject to a land lease. This is a long term project, possibly getting underway as the airport expansion is completed with an estimated start date of not earlier than 2015.

In addition, the Airport Authority is intent on redeveloping the Cell Phone lot into a rental car hub for the airport, connected by tram to the terminal, and has plans to include a mixed use retail strip in the development. This would likely include service facilities, including restaurants and a gas station. They have discussed a hotel at the site, and the Authority is aggressively seeking an upscale development. However, studies completed to date find support in the area primarily for an extended stay or limited service hotel of a much more modest size. There is no set timeline on the hotel component of this project but it is likely years away.

The retail development where Muvico is located on Bryn Mawr at one point included plans for a hotel component. At the current time, Rosemont plans to create a shopping center in the area. The hotel project has been tabled for several years; however it could quickly be revived when market conditions improve. This project would be a limited service facility of unknown size, taking advantage of the retail infrastructure planned for the overall development. It is unlikely to move forward.

The PUD for Rivers Casino in Des Plaines includes the development of a hotel facility to serve the gaming operation and surrounding business. This is a phase two construction plan, and because of economic conditions at the current time, it is not imminent. The market is currently served by the nearby Courtyard and Hilton Garden Inn. This may happen at some point, but plans are not yet completed.

O'Hare Lakes, to the west of the tri-state from the Rivers Casino, has plans for extensive re-development, including office, retail, and possibly multiple hotels with as many as 700 rooms to serve the airport, casino, and local office markets. Tentative discussions have included a pedestrian ramp across the tri-state for casino patrons. This would be a phased development and is heavily contingent on availability of financing. It is unlikely to move forward as a hotel project at least in the short term.

All of the above projects are in early stages of planning, and depend on a considerable improvement of the lending market and the economy as a whole. None of these projects have any sort of firm timeline at current and would take a considerable time to get going should the market recover.

The rooms inventory at the airport was reduced by the closure and demolition of the low-rise components (240 rooms) of the former Ramada Inn, with the remaining rooms in the "newer" tower re-branded as a Holiday Inn Express property. The Wyndham with 468 rooms was closed by Sage Development and probably will not return to the transient lodging market. This property was developed in the 1960's and suffers from economic obsolescence and has a significant mold and mildew problem.

FULL YEAR	Occupancy	% Change	ADR	% Change	RevPAR	% Change	Properties	Rooms
2006	72.35%		$113.05		$82.63		49	9806
2007	72.34%	-0.013%	$120.04	6%	$87.66	6%	47	10666
2008	66.77%	-7.702%	$116.51	-3%	$78.43	-11%	49	11483
2009	55.67%	-16.625%	$97.10	-17%	$54.26	-31%	49	11462
2010	64.37%	15.639%	$97.67	1%	$63.47	17%	47	10907
2011	66.28%	2.961%	$100.60	3%	$67.16	6%	53	11618
2012	68.00%	2.593%	$104.62	4%	$71.14	6%	53	11410
2013	70.00%	2.941%	$108.28	3%	$75.80	7%	53	11410
2014	71.00%	1.429%	$111.53	3%	$79.19	4%	54	11653
2015	72.00%	1.408%	$114.88	3%	$82.71	4%	54	11653
2016	72.00%	0.000%	$118.33	3%	$85.19	3%	54	11653
2017	72.00%	0.000%	$121.88	3%	$87.75	3%	54	11653