Although the federal government remains the dominant influence in Washington, D.C., a diverse array of industries and institutions have contributed to and supported the growth and expansion of the region. The finance, education, healthcare, and scientific-research industries are strongly represented in and around the District, and the region is home to 20 colleges and universities, as well as Adventist HealthCare and multiple major regional hospitals. Some of the most influential financial institutions call D.C. home, including the Federal Reserve, the World Bank, the International Monetary Fund, and the U.S. Export-Import Bank. Greater Washington, D.C. also stands among the nation’s top markets for commercial office space and global real estate investment. A world-class array of museums and cultural attractions support a robust tourist trade, while the convention center hosts multiple regional, national, and international events each year.

The D.C. Lodging Market

The Washington D.C. lodging market has historically been one of the most stable of the major U.S. markets, principally due to the volume of demand related to the federal government. This demand includes government and military employees, as well as private-sector employees traveling on government-related business. Although the levels of demand fluctuated during the recession and subsequent government shutdown and sequestration, the volume of travel related to government activity, complemented by steady tourism demand, sustained occupancy in the mid-60% range even in the slowest years. This stability extends to the average daily rate (ADR), as the government-related demand is tied to the federal per-diem rate, which is set annually. Although the per diem varies by season, this rate is an anchor for the market and serves as a benchmark for corporate and group rates. Thus, while RevPAR for the top 25 U.S. metropolitan markets declined 19% in 2009, the D.C. market experienced only an 8.6% decline. Average rate in D.C. fell by only 5.5% that year, compared to over 22% in New York City and approximately 15% in Chicago and San Francisco.

The controlled downside provided by the government sector comes at a cost. Given the magnitude of demand that is tied to this rate, it is difficult for the market to achieve ADR growth beyond the parameters of the per-diem change. Rate growth has been further constrained by the sequestration, which reduced government travel activity in 2013 and enabled other segments to benefit from discounted rates offered in response to sluggish government demand. Because of these influences, average rate in the market remained essentially flat between 2009 and 2014. RevPAR demonstrated similar stability between 2009 and 2013, but significant occupancy...
growth in 2014 supported a RevPAR increase of over 5.0% that year. This pace of growth was sustained in 2015 and continued into 2016, as government demand stabilized and was supplemented by increased activity in the commercial and convention sectors of the market. In 2015 occupancy surpassed the 70% mark for the first time since 2005, and the impetus of RevPAR growth shifted to average rate, which outpaced inflation in both 2015 and 2016. ADR growth was also supported by the opening of new, higher-rated supply.

**Supply Trends**

More than 800 hotels and approximately 111,500 rooms constitute the lodging landscape of the Greater Washington, D.C. MSA. The District of Columbia itself offers approximately 130 hotels totaling more than 30,200 rooms.

![Pie chart showing the distribution of hotel chains in D.C.](source)

Upper-Up-scale Assets Represent Largest Percentage of Hotels in D.C.

The market’s breakdown by chain scales is in line with national trends for economy, midscale, upper-midscale, and upscale hotels; however, approximately 41.5% of all guestrooms in the District of Columbia are classified as upper-upscale, representing a proportionately greater share of the market when compared with similar markets in the U.S.

The inventory of hotels located in the District of Columbia has increased by 3,680 rooms (12.2%) since 2014; another 2,000 guestrooms are scheduled to open by the end of 2017. In total, over 30 hotels are under construction or proposed for development in the market. These projects are in varying stages of development, and it is unlikely that all will be completed, but supply is expected to increase by at least 15% by 2020. Although this volume of new supply is significant, it is notable that all the hotels that opened within the past decade have been absorbed. Furthermore, as of 2016, both occupancy and average rate had regained their prior peak levels. While the recovery from the recession contributed to this growth, this historical resilience suggests that the new supply will have only a moderate impact on the market’s overall performance. In the near term, the influx of new hotels is anticipated to cause some competitive pressure that will affect both occupancy and average rate. However, the impact is expected to be muted in 2017 due to a strong convention calendar; the market will also benefit from demand related to the inauguration and the Women’s March in January. Moreover, the change in administration, the related changes in various governmental positions and entities, and the public- and private-sector responses to those changes, should generate additional demand through at least the first quarter of the year.

**Convention Activity**

The convention segment has been a key segment supporting the lodging market. The Walter E. Washington Convention Center (WEWCC) opened in 2003, replacing a dated, inadequate facility that had limited the market’s opportunities to participate in the convention segment. With the opening of the Marriott Marquis in 2014, the convention-center-and-headquarters-hotel package was complete, and attendance surpassed the 1.3-million mark for the first time since the new center opened. More significantly, the mix of events has shifted to include a greater number of citywide events (defined by the market as conventions that require more than 2,500 room nights on the peak night). This trend benefits the lodging market by increasing the number of hotel rooms that benefit from convention activity while also limiting the inventory available to other demand segments, creating...
the opportunity to maximize average rates.

**Walter E. Washington Convention Center Trends**

Source: Events DC

Some of the events expected to occur in 2017 include annual meetings of the American College of Cardiology, the Society for Neuroscience, and the U.S. Travel Association’s IPW. The booking-window periods have decreased in recent years, and figures for the 2018 and 2019 events on the books currently show a decline, but the CVB is optimistic about the ultimate outlook for these and subsequent years, including sustaining a greater proportion of citywide events. The market continues to be a popular convention destination for meeting planners and attendees. The government and local institutions are a valuable resource in terms of speakers, and there are numerous venues for special events to supplement the convention center facilities.

**Tourism and Visitation**

Tourism is a mainstay of the Washington, D.C. economy and a significant demand generator for the local lodging market. The city is the eighth most popular destination in the U.S., after New York, Miami, Los Angeles, Orlando, San Francisco, Las Vegas, and Honolulu. In 2015, a total of 21.3 million people visited the city, up from 15.0 million in 2005. Of these visitors, 2.0 million originated from outside the U.S., up from 1.0 million ten years earlier. The most popular destinations are the National Park Service locations on the Mall (33.5 million visitors in 2015) and the Smithsonian locations on the Mall (27.4 million visitors in 2015).

**Total Visitation to Washington, D.C. ($ Millions)**

Source: Destination DC

Total visitor spending in 2015 equaled $7.1 billion; of this amount, $2.4 billion was spent on lodging, and about $2.0 billion was spent on food and beverage. Although comprising only 7% of the total number of visitors, international travelers accounted for 27% of total visitor spending in 2015.
Forecasts prepared and published by Destination DC anticipate that visitation levels will continue to increase over the next four years. Total visitation is expected to reach 24.5 million by 2019.

Airport Activity

The greater Washington, D.C. area benefits from the availability of three major airports: Ronald Reagan Washington National Airport (DCA), Washington Dulles International Airport (IAD), and Baltimore International Thurgood Marshal Airport (BWI). Collectively these three airports provide access to most major domestic and international destinations, either through direct or connecting flights. This ease of access facilitates travel for both tourists and the convention segment. It is also a key attribute that supports local business activity, including the government sector. The passage of the FAA Reauthorization bill in 2012 increased the number of takeoff and landing slots at DCA; the expansion of service at this most-conveniently located airport has resulted in over 4.2 million additional passengers annually. During the same period, BWI recorded 1.4 million additional passengers, and IAD 1.4 million fewer passengers, primarily due to changes in flight service. All three airports are currently undergoing renovation projects, including an expansion at DCA, which should support further increases in passenger activity in future years. Moreover, the extension of the Metrorail service to IAD will significantly improve the accessibility of this airport and is expected to enhance the appeal and utilization of this facility.

Hotel Transactions

Transaction activity in Washington, D.C. since 2014 has comprised 23 sales with a collective value of $1.7 billion. Excluding the St. Regis and Marriott Wardman Park, which were partial-interest transactions, the average sale prices have been strong (at roughly $400,000 per room), demonstrating investor confidence in the market. Transaction activity over the past three years consists of a more diverse array of assets than was the case several years ago, particularly in the District itself; thus, the range of prices per room has widened. Nevertheless, quality assets in reputable neighborhoods continue to command strong prices, as evidenced by the June 2016 sale of the Graham Georgetown at $649,000 per room, the March 2015 sale of the Hilton Garden Inn Washington D.C./Georgetown at $447,000 per room, and the December 2015 sale of the Ritz-Carlton Georgetown at $581,000 per room. Transacting at $1,327,000 per room, the sale of the Rosewood Washington, D.C. in April 2016 commanded one of the highest prices of any major hotel transaction nationwide.

The level of investor interest is reflected in the capitalization rates indicated by the sales. Although capitalization rate data are not available for all transactions, the available data indicate cap rates ranging from 4.2% to 8.3%, with an average of 6.2%. The median cap rate was 7.0%, and the mode was 7.4%; half of the reported cap rates fell between 7.0% and 7.5%.
With limited available land and development constraints, including restrictions that limit building height in the District to 130 feet and high construction costs, Washington, D.C. has significant barriers to entry that are particularly favorable to investors with a long-term investment perspective. These attributes, along with the city’s role as the U.S. capital, have historically been attractive to investors, and particularly international buyers. From a hotel investment perspective, the stabilizing presence of the federal government, strong tourism industry, improving convention segment, and expanding commercial base enhance the market’s appeal, although the pending increase in supply has given some cause for concern. Washington, D.C. has perpetually ranked among the top five U.S. markets on the Association of Foreign Investors in Real Estate’s annual survey. However, D.C. dropped to 6th in the U.S. and 15th globally as of January 2017; this decline in rank is attributed in part to D.C.’s high barriers to entry and the high costs of hotel investment in the market.

The Outlook for the Market

The overall outlook for the Washington D.C. market is favorable. The federal government will continue to be a significant demand generator for the lodging industry and stabilizing presence for the economy overall. Although the opportunity for notable ADR growth is somewhat constrained by the government per-diem rates, increasing levels of demand from the commercial and convention segments of the market should enable hoteliers to optimize average rate during peak demand periods. This in turn will lead to increases in the per-diem rates in subsequent years. Near-term concerns principally comprise the potential new supply. If additions to supply outpace demand growth, the hard-won rate increases of the past three years could be undermined, and the pattern of minimal rate growth that characterized the post-recessionary years could return. In this regard, the positive demand factors anticipated for 2017 should be beneficial. Demand related to the inauguration, Women’s March, and the change in administration will all occur in the first quarter of 2017, which has historically been the market’s slowest period, thus mitigating the impact of the new supply. The strong convention calendar, and particularly the number of citywide conventions on the books, should benefit the market through the balance of the year.
**About Chelsey Leffet**

Chelsey Leffet is a Director and head of the Washington, D.C. HVS Consulting & Valuation office. Chelsey has consulted on hundreds of hotels throughout the Mid-Atlantic, including major Beltway markets. Prior to joining HVS, Chelsey worked in guest services, operations, and restaurant roles at ARAMARK Higher Education; Lighthouse Resort Services in Corolla, North Carolina; the Columbus Inn in Wilmington, Delaware; and the Bellmoor Inn and Spa in Rehoboth Beach, Delaware. Chelsey earned her BS in Hospitality Management and her MBA from East Carolina University. Chelsey resides in Washington, D.C and is a certified general appraiser. Contact Chelsey at (202) 434-8793, or [email protected].

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