Rooms Aplenty, Hotels Make Way for Homes, Offices

Oversupply and high financing costs force developers in many cities to convert projects into residential or commercial properties

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A massive oversupply situation in markets such as Chennai, Hyderabad and Pune is pushing several hotel developers to convert their upcoming projects into residential or commercial properties.

The proposed The Oberoi luxury hotel in Hyderabad, for example, has been put on the backburner and the developer is mulling over alternate use of the project as a commercial centre, an industry expert said. "The market isn't promising the projected average room revenues (ARRs) of ₹16,000 a night, which has led to the developer to rethink the project," said an industry expert, who did not wish to be named. The developer, Maha Hotel Projects, however, denied any such development.

In Chennai, meanwhile, Viceroy Hotels sold its JW Marriott hotel to local developer Ceebros, which is now pulling down the unfinished structure to build apartments.

Industry insiders say the oversupply situation that has impacted hotel occupancies and room rates has forced several developers to re-work their projects and opt for conversion.

According to an India Ratings and Research (Ind-Ra) report on the hotel industry, there is an increasing number of projects being shelved in the hospitality sector as of 2014 and hotel companies are delaying and shelving new projects (40%-50%) due to the prevailing economic downturn and increased stress levels.

"Lower liquidity and rising financing costs, longer stabilisation periods along with a rise in construction and land costs are making hotel projects unviable," the report said.

An Ind-Ra report said delay in obtaining clearances is a major factor in slowing down of hotel projects

Achin Khanna, MD of consulting and valuation practice at hotel consulting firm HVS South Asia, said a lot of developers like DLF, Emaar and Unitech entered the hospitality space in the late 2000s and, in conjunction with hospitality management companies, announced a number of projects which have not been actualised.

Experts said that several developers entered the hospitality sector, lured by the higher floor space index (FSI) that hotel projects were granted when compared to residential or commercial properties.

"However, after the projects were announced, developers started to realise that hotels require a locking in of capital for longer periods (5-7 years) which wouldn't give returns as high as the sale of residential apartments," said Mudassir Zaidi, national director for residential agency at real estate consultancy Knight Frank India.

In addition to this, most developers did not take into account the fact that valuation of hotels is based on business rather than real estate, which is higher. "So there was a difference in valuation when the owners wanted to sell the projects," Zaidi said.

The Shangri-La hotel project in Bangalore, being built by the Adarsh Developers, was supposed to be ready by 2013. But it has not been completed yet. "The developer is waiting for the market conditions to improve," said an hotelier who did not wish to be named. An email query sent to the developer did not elicit any response till Tuesday evening.

The Ind-Ra report said delay in obtaining clearances is a major factor in slowing down of hotel projects. It estimates that 80% of the new projects announced (by value) have been stalled over financial years 2012 and 2014.

Experts said a hotel project costs four times the value of a residential or commercial project. In addition to this, the return on investment is not lucrative.

"The return on investment in a hotel project is around 4%-6%, whereas commercial projects give returns to the tune of 8%-10%," said Priyakant Amin, director at Convention Hotels India. According to Amin, hotels, as a class of asset, have become unsustainable due to the higher rate of interest and short term tenure of loan, which creates pressure on the cash flows.

An upscale hotel project by Emaar MGF in Kochi has not seen any progress since 2010. While the developer was in early talks with Canadian hotel chain Four Seasons, the project has been in a limbo. An email query sent to the developer did not elicit any response till Tuesday evening.

Many developers are resorting to alternate use of half-done hotel projects in cities like Chennai, Bangalore, Hyderabad and Pune, where flexible land-use norms allow project plans to be altered. "Some of the projects have been changed for mixed use in cities like Hyderabad, since they are looking for alternative revenue streams," said Ashish Jakhanwala, MD at SAMHI Hotel Investment.

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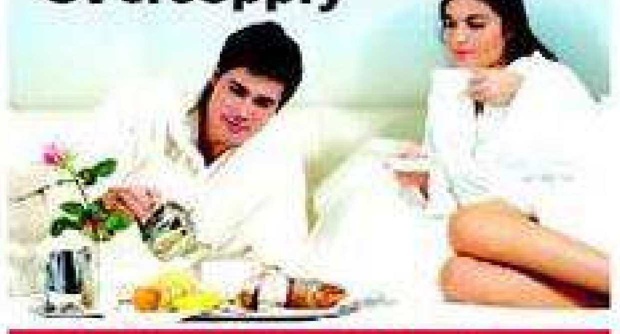
Projects Hit by Oversupply



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Some of the hotels affected by massive oversupply situation:

SOLD: JW Marriott Chennai by Viceroy Hotels

STALLED: Planned upper-upscale hotel by Emaar MGF in Cochin

ON HOLD: Shangri-La hotel project in Bangalore by the Adarsh Developers

STALLED: The Oberoi Hyderabad project by Maha Hotel Projects