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Chinese Investment Trends in U.S. Hotel Real Estate

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The rising trend of Chinese investment in the U.S. real estate market dates back to 2010, just as the nation's economy was pulling out of the recession. The impact of Chinese investment in U.S. residential and commercial properties—including hotels—has become increasingly pronounced every year since.[1]

Summary

Investment out of mainland China in U.S. hotel real estate has been on the rise for years. What's driving the trend, and how has it affected hotel markets in the U.S.?

1 Comments

Hotel and Hotel Portfolio Investment out of China

The following tables show major single-asset transactions made by Chinese investors in the last five years. The two transactions in New York, one of which was recorded at approximately $1.4 million per room and the other at over $2 million per room, especially caught the attention of the industry.

Property	Location	Sale Date	Price	Rooms	Price per Room	Year Opened
Hyatt Regency Orange County	Garden Grove, CA	Oct-15	$ 136,118,667	656	$ 207,498	1986
Waldorf Astoria New York	New York, NY	Feb-15	1,950,000,000	1,425	1,368,421	1931
Baccarat Hotel & Residences New York	New York, NY	Jan-15	230,000,000	114	2,017,544	2015
Marriott Los Angeles Airport	Los Angeles, CA	Dec-14	155,833,333	1,004	155,212	1973
Luxe Los Angeles City Center	Los Angeles, CA	Jul-14	104,150,000	178	585,112	1965
DoubleTree by Hilton Monrovia	Monrovia, CA	Jun-14	43,000,000	171	252,941	1986
Marriott Torrance South Bay	Torrance, CA	Nov-13	76,000,000	487	156,057	1985
Sheraton Gateway Los Angeles	Los Angeles, CA	Nov-13	96,000,000	802	119,701	1981

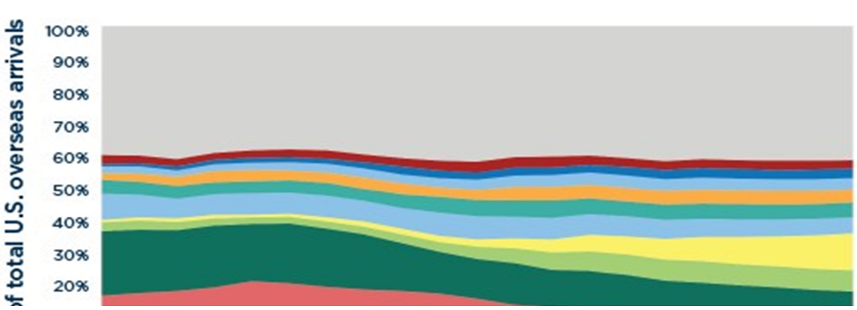
Source: HVS

Chinese investors have recently started to invest in hotel portfolios, as well. In February 2016, Hersha Hospitality Trust sold a 70% majority interest in seven Manhattan hotels to Chinese investment firm Cindat Capital Management for a total purchase price of $571.4 million. In March 2016, The Blackstone Group agreed to sell Strategic Hotels & Resorts, Inc. to China's Anbang Insurance for approximately $6.5 billion. In April 2016, HNA Tourism Group announced its plan to acquire Carlson Rezidor Hotel Group; HNA had already acquired a 15% **stake** in Red Lion Hotels Corp in 2015.

Motivations

The last decade has brought a surge of Chinese visitors to the U.S., an impetus for Chinese investment in hotels in U.S. gateway cities. According to the National Travel and Tourism Office, 2.19 million Chinese visitors traveled to the U.S. in 2014, a 21% increase over the prior year; these visitors contributed over $2.3 billion in travel spending. Moreover, U.S. inbound travel from China is expected to continue to grow, and Chinese investors have been focusing on acquiring mid-scale hotels to capture the demand from the country's middle-class.

China Widens Share Among Top Overseas Travel Markets to U.S.



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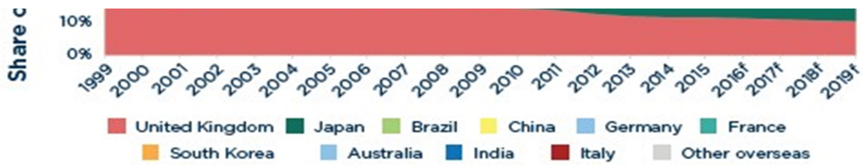

Source: U.S. Department of Commerce

Concerns about the market slowdown in China and the devaluation of the Yuan led Chinese investors to seek a safer investment environment or a better return. According to the Asia Society, "Chinese investors are attracted to U.S. markets given [the higher] return potential, array of investment opportunities, economic and property market stability, strong foundation of property rights, and the sheer size and maturity of the market." According to the Rosen Consulting Group (RCG), Chinese commercial real estate acquisitions in the U.S. totaled $17.1 billion from 2010 to 2015. Hotel investments totaled $3.7 billion, or 21% of the total commercial real estate acquisitions.

A growing number of Chinese individual investors are using EB-5, an immigration program, as a vehicle to invest in U.S. hotel developments. The EB-5 regional center program has become an effective tool for fostering investment and creating jobs within the U.S. In the wake of the economic *downturn*, the EB-5 program has emerged as a viable *alternative* to traditional *financing*. According to the State Department, over 80% of visas issued through the EB-5 program are from China. Investors who use this investment tool are heavily motivated by the opportunity for U.S. residency and its associated benefits of educational opportunities and higher quality of life.

The EB-5 program has continued to be an alternative financing tool for commercial real estate development as construction-loan qualification requirements become more restricting. On December 16, 2015, the EB-5 visa program was officially extended through September 30, 2016, as part of the omnibus spending bill reached by Congress.

Institutional investors are attracted to the potential returns on a hotel project, along with the opportunity to expand their presence in the U.S. These institutional investors include insurance companies, such as Anbang and Sunshine Insurance, as well as some of the largest Chinese real estate developers and operating companies, including Greenland Group, Wanda Group, and Oceanwide.

The following details some recent Chinese investments in U.S. hotels.

- Shanghai Greenland purchased the Metropolis site in Los Angeles, California, in early 2014. The first phase of the mixed-use development will include a 38-story residential tower and the 350-room, 18-story Hotel Indigo. This phase is slated for completion in late 2016.

- Wanda Vista Tower Chicago, approved in November 2015, is expected to offer over 400 residences and a luxury Wanda Vista Hotel; the project is planned to be complete by 2020. Wanda's One Beverly Hills is also a hotel/residential mixed-use development; the project is anticipated to include a 134-room luxury boutique hotel, 193 residences, and new public gardens and open space.

- Oceanwide Plaza in Downtown Los Angeles will include a 49-story building with a mall and a 183-room luxury hotel, as well as two 40-story residential towers. The project is under construction and is expected to be complete in September 2018. Oceanwide Center in San Francisco is another mixed-use development, consisting of two towers. One tower is planned to feature a 169-room hotel and approximately 150 residential units; the taller tower will rise 34 stories and is planned to include 1,010,000 square feet of office space and approximately 110 residential units. The site was acquired in early 2015. If completed as proposed, the 905-foot tower would become San Francisco's second-tallest building after Salesforce Tower, which is under construction and is expected to open in 2018.

  In New York, Oceanwide purchased a site near the South Street Seaport in August 2015; the company also plans to invest in a mixed-use development. Additionally, in West Oahu, Oceanwide purchased a site in late 2015 and has plans to develop a 150-room luxury hotel and 150 condominiums.

Lastly, hotel investment helps diversify Chinese investors' portfolios. Although Chinese investors have invested in all types of commercial real estate, office properties, multi-family properties, and hotel assets register the higher volumes in transactions. The buyers for hotels include private equities, tourism companies, real estate firms, construction companies, and institutional investors.

Trends

Private and institutional Chinese investors have learned to work with local professionals, hire local people for their projects, and become increasingly knowledgeable about the local market and hotel transactions in the U.S.

HVS research has uncovered the following trends, which have become predominant in Chinese investment over the past several years.

1. While gateway cities are attractive to the majority of Chinese investors, major cities such as Dallas, Chicago, and Seattle have drawn recent attention because of their strong performance growth. According to STR, the Dallas market realized 10.0% RevPAR growth in 2015, reaching $69.81; the Chicago market realized 6.9% RevPAR growth in 2015, reaching $99.88; and RevPAR in the Seattle market grew 8.8% in 2015, reaching $113.14. Nevertheless, Chinese investors have less experience or presence in these markets versus the gateway cities; therefore, investments in the non-gateway markets have been cautious, with few hotel transactions and hotel developments yet to emerge.
2. Chinese construction companies, already active in U.S. hotel markets, show potential for increased investment in future years. Shanghai Construction Group America (SCGA) is a wholly owned subsidiary of Shanghai Construction Group (SCG). The group developed the Hyatt Place Flushing in 2014 and purchased the Hyatt Regency in Garden Grove, California, in late 2015. Two Fulton Square/SCG Plaza II in New York, which is under construction, will include two residential towers, an office tower, and a boutique hotel.

   China Communications Construction Group bought a development site in Miami's Brickell neighborhood in late 2014. The development plan has not been finalized; reportedly, the plan could ultimately comprise a mixed-use project with condominium, hotel, and office elements.
3. China has permitted insurance companies to invest in real estate overseas since 2012, although they are only allowed to invest up to 15% of their total assets in international markets. Sunshine Insurance and Anbang both purchased trophy hotels in the U.S. in 2015; furthermore, Anbang announced plans to acquire Strategic Hotels for $6.5 billion in 2016.

   An article published by Cushman & Wakefield indicated that the current investment holding of all Chinese insurers totals $13.4 billion, or 0.8% of total assets. Overseas investments are estimated to be half of this. By this measure, there exists tremendous room for Chinese insurers to ramp up investment overseas, with the U.S. a preferred destination.
4. China has reformed the approvals and registrations process for outward foreign investments in recent years, which has boosted investment activity across the board. In late 2015, China's State Council announced its approval of the Qualified Domestic Individual Investor program (referred to as "QDII2"), which allows individuals from six cities, including Shanghai, to invest directly in overseas assets like stocks, bonds and real estate. Additional structural reforms and loosened restrictions on capital outflow are expected in the near future. This should further boost Chinese investment in U.S real estate, where hospitality assets have come increasingly to the forefront in recent years.
5. In December 2015, President Barack Obama signed a new law that allows foreign pensions to buy as much as 10% of a U.S. publicly traded real estate investment trust (REIT) without triggering Foreign Investment in Real Property Tax Act (FIRPTA) liability; investment limits previously stood at 5%. The new law potentially opens the door even wider for overseas investors.

Conclusion

Will the recent trend of Chinese investment be a repeat of Japanese investment in U.S. real estate in the early 1990s? While there are some similarities between the two cycles of investment, there are also distinctions. For one, individual Chinese investors are more conservative in buying in at reasonable prices and express a cautious interest in learning how to maintain real estate in the U.S. Furthermore, Chinese institutional investors have demonstrated an investment approach that values capital preservation and long-term business goals.

There have also been concerns about whether the investments from China are sustainable given the slowing Chinese economy. But it should be emphasized again that Chinese companies are looking at U.S. real estate as a stable way to diversify outside their own economy. Chinese buyers continue to invest heavily in U.S. real estate, especially in gateway markets in New York and California. Hence, the wave of Chinese investment in U.S. real estate appears anything but negligible or short-lived.

[1] This article focuses on investments in U.S. hotels from investors from mainland China, though Chinese Americans and investors from Hong Kong, Taiwan, Singapore, and Southeast Asia are also active in hotel markets in California, New York, New Jersey, and Texas.

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