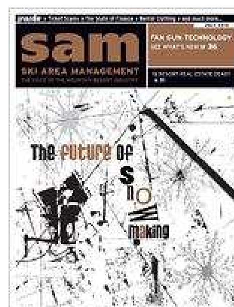

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Real Estate Gets Real
by Ken Castle

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Will resort real estate ever recover from The Great Recession? If it does, who will buy, and what will they be looking for?

Speculators, who helped spur double-digit appreciation at resorts for nearly two decades, are largely gone from the vacation property market. But there is plenty of speculation about what comes next.

For the moment, at least, we've seen the end of the frantic pre-sale events, the fast-track building projects, and the euphoria of using real estate as a cash cow to bankroll chairlifts, terrain expansions and day lodges. The party is over, but the hangover remains. And it's more painful than anything the industry has experienced in decades.

"We've entered a new reality," says James Chung, president of Reach Advisors, a New York-based strategy and research firm. "In 2006, we were being told that ski resort real estate could never drop in price and that demand would always outstrip supply. The common line was, 'They don't make mountains anymore.' But we were in a bubble, and supply wasn't a function of demand as much as capital availability. Everyone said [ski resort] real estate was a brilliant investment, but in fact it never was an investment. It's actually the worst class of real estate, because it doesn't appreciate on an inflation-adjusted basis."

Granted, some people made a quick profit by flipping properties, but Chung believes that had more to do with timing and luck in an overheated market.

He ticks off the current downsides: Real estate prices in many locations have plummeted 40 percent or more. There is a huge inventory of properties that will take years to work through, plus a shadow inventory that is being withheld from the market. In addition, he calculates another 25,000 units planned for the next five years, many of which won't get built.

Timeshares and fractionals—once hailed as the antidote to high prices—are losing steam because "their cost exceeds their value," Chung says. That's due in part to expensive annual maintenance fees and amenities that most people don't need or want. "These were not consumer-driven; they were developer-driven," says Chung. "The economic challenge with this model is that it only works when there is a solid middle class with excess cash, and we don't see that happening in the foreseeable future."

Another big trend, says Chung, is that Baby Boomers, the backbone of the vacation market for nearly two decades, seem to be tapped out. "This generation is now beyond its peak years of real estate purchasing," he says.

Chung believes that whatever model evolves next will be based on actual consumer demand. "Developers got fat and happy from behaviors that don't exist anymore. They're going to have to rethink the future and realize that they're not going to see the profit margins of the past," he says.

NEXT-GENERATION BUYERS

Claire Humber, director of resort planning for the SE Group in Burlington, Vt., says that the shoppers who are left are "more educated, more investigative and more practical. They are doing their homework, and there's no spontaneous buying." Developers, she adds, must bone up on the aspirations of Echo Boomers, Gen-Xers and Millennials. In the latter category, a number of 20-somethings have already purchased primary homes, much earlier in life than their parents did, thanks to the profusion of foreclosures, short sales, steep price declines, and tax credits. Will these multitasking, text-messaging, teamwork-driven young people eventually

hunger for the same experiences in the outdoors as the Boomers did? Or will they want something different?

And what about those Boomers? As they downsize or enter retirement, are they likely to relocate to a mountain resort, where artificial hips and gimpy knees have to cope with freezing temperatures and icy sidewalks? Or will they prefer a warm-weather climate with a golf course around the corner? So far, there are no answers to those questions, although SE Group is completing a survey that may offer some clues.

Developers agree that the buying demographics have shifted from older Boomers to 40-somethings with children. These buyers are well-traveled, fussy about what they want, and intend to be avid lifestyle users rather than investors.

Kevin Barnes, a 48-year-old financial advisor from Belvedere, Calif., who has stayed at the Yellowstone Club and owns property in Solitude, Utah, says that his family chose the 2,000-acre Martis Camp development near Northstar for their main retreat because they could build a custom home. "We looked around at five or 10 existing homes in Tahoe, and there was always something wrong," he says. "We just fell in love with the amenities at Martis Camp." The community offers an 18-hole golf course and private skiing access to the backside of Northstar. The Barnes' 1.8-acre lot is on the 10th fairway and has a view of Northstar's slopes.

What prompted the Barneses to buy during the height of the recession? "If we had purchased in normal times we wouldn't have had the selection and the prices probably would have been 20 percent higher," he says. "But the best thing was being able to shop without competing against other buyers."

COLLATERAL DAMAGE

Despite some new buying activity, the resort real estate recession has continued unabated through the first half of 2010. Other casualties include shops and restaurants at ski area villages that were built in the late 1990s and early 2000s. All too often these projects, tethered to residential property sales, have proven to be money pits for tenants. Consumers' thrifty habits during the winter seasons, combined with lean shoulder periods, have led to numerous business closures and failures. After vacationers left, few locals ever replaced them. Thus, many villages failed to become new centers of their communities and are largely deserted for much of the year. A looming issue for resort planners is how to make these places viable—if it's possible to do so.

For example, in Aspen, property values have plummeted 20 to 40 percent, single-family home sales were down by 8 percent in 2009, and commercial vacancies have approached an unheard-of 8 percent, according to a new report from the Aspen Appraisal Group. Further, the long-awaited Snowmass development at Base Village is in suspended animation after funding for owner and developer Related WestPac vanished in 2008.

East West Resort Development of Avon, Colo., the developer of four-seasons residential projects in Truckee, Calif., and at Northstar-at-Tahoe, put nearly $1 billion of real estate into bankruptcy earlier this year—Northstar Highlands and two golf-oriented communities. On March 31, the new Ritz Carlton Highlands also went into default on $18.7 million in payments on $157 million in loans. The hotel has continued to operate while East West negotiates with the project's lender.

THE GOOD, THE BAD, AND THE UGLY

With the downward trend in resort real estate now in its fourth year, there are nonetheless some bright spots. A handful of new projects have either recently opened or are scheduled to open by the end of the year. Most were planned before the recession and were under construction during the height of the real estate downturn—perhaps a fortuitous bit of timing.

Vail Resorts has two of them. One Ski Hill Place, a ski-in/ski-out luxury condominium lodge at the base of Peak 8 in Breckenridge, opened in June, and has been drawing a steady stream of buyers. It is the first RockResorts property at the ski area, and it benefits from its proximity to the BreckConnect Gondola, which links Peaks 7 and 8 with the historic mining town. The wholly-owned units range from studios to four bedrooms, with a footprint of from 500 to 2,000 square feet.

One Ski Hill Place at Breckenridge opened in June and has attracted buyers, but not at the typical pace. To spur sales, Vail Resorts and others are sweetening the pot with discounts and memberships.

Over at the base of Vail Mountain—the most active resort real estate market in the U.S.—The Ritz-Carlton Residences will open this fall. The Bavarian-style development consists of 71 whole-ownership residences, ranging from two bedrooms to a six-bedroom penthouse, as well as 45 fractionals. More than two-thirds of the whole-ownership units have been sold, helped along by 15 to 20 percent discounts and value-added spiffs such as social membership in The Arrabelle Club, which offers ski valet service, private lockers and other facilities.

Will more Vail Resorts clients begin buying property again? "This last winter we saw consumers returning to their historic staying habits, with increases in ski school, dining and rentals," says Jeff Jones, Vail Resorts' CFO and senior executive vice-president in charge of real estate. "We think real estate is going to lag this consumer spend on the mountain, but not too far behind."

Other projects underway at Vail Mountain include Solaris, scheduled to open this summer, with

78 whole-ownership condominiums, retail shops, restaurants, a movie theater, a bowling alley and an ice skating rink. Not far away, the Four Seasons hotel is also rising, but it has been mired in delays and disputes. Originally planned to open in 2008, it still has no set opening date.

A few dark clouds still linger over Vail Valley. The Eagle County Economic Council reported that the fourth quarter of 2009 saw significant declines in real estate transactions and property values. The council's report said that no new developments are likely to start before 2013, or come to market before 2017.

There aren't many bright spots, either, at other mountain resorts across the country. While master planning continues at a number of ski areas, including Killington, Stowe and Sun Valley, new projects that have opened or are nearing completion are few and far between. Most, like the Vail projects, were in construction during the worst part of the recession.

Among the newcomers is Montage Deer Valley, an opulent lodge in the Empire Canyon area at the mid-mountain point of Deer Valley Resort. Projecting a December opening, this property boasts 174 luxury guest rooms and suites, 81 private residences on the upper floors, a 35,000-square-foot spa, conference facilities, restaurants, shops and multiple forms of indoor and outdoor recreation.

In the East, one new standout project is the Hope Lake Lodge & Indoor Waterpark at Greek Peak Mountain Resort, in central New York, which opened in December to rave reviews. Kevin Morrin, director of ski area sales and marketing, says that quarter-share fractionals for the 106 condominium units were 65 percent sold out by the end of the season. At that time, prices ranged from $57,000 for a four-sleeper to $189,000 for a 10-sleeper. Morrin says the sales pace picked up after the complex opened for the winter. Last season the hotel attracted new business from Canadian skiers, he says, as well as more ancillary spending among the established clientele from Rochester, Scranton, Ithaca, Long Island and Buffalo. "We've seen a huge increase in some of our higher-end products such as ski school," says Morrin. The 41,000-square-foot indoor waterpark—rare among ski areas—has helped drive traffic.

Left: Unfinished projects such as the base area at bankrupt Tamarack ski area are not uncommon. Right: Conversely, the new Hope Lake Lodge at Greek Peak in New York is 65 percent sold out.

A CLOUDY FUTURE

With so much property and master planning still in transition, no one is willing to hazard a guess about what comes next, since even well-branded signature properties are on the ropes. Developers are going back to the drawing board, trying to figure out how to move existing inventory and what, if anything, will inspire future buyers.

"What we do know is that the perpetual growth theory of real estate is impossible," says Brent Harley, president of Brent Harley & Associates in Whistler. "We need to look at balance, figuring out how much capacity your mountain has and what quality of experience is needed to create a sustainable level of visitation. The way to end the disconnect between enthusiasm for development and the realities of the marketplace is to return to the heart of why people go to the mountains in the first place. If we can rekindle that passion and pay attention to providing an authentic experience, then we can really create successful mountain communities."

FOREIGNERS TO THE RESCUE?

Might investors from the BRIC countries—Brazil, Russia, India and China—bring deep pockets to new real estate ventures, just as previous waves of investment from Japan, France and Australia did? No way, says Paul Mathews, president of Ecosign Mountain Resort Planners, a Whistler-based company with major international clients. While Russia and China are rapidly building ski resorts and thinking about hosting future Winter Olympics events, "They don't yet feel comfortable being overseas. I don't see any interest from these countries in coming here," he says.

However, that mood may be changing. China was never seriously impacted by the global recession, and Chinese investors are actively shopping for hotel properties in California. Last year, Hong Kong-based Keck Seng Investments purchased San Francisco's W Hotel for $90 million, and in March the Chinese real estate development company Shenzhen New World Group bought the Los Angeles Marriott Downtown out of foreclosure at a bargain price of $60 million, according to the San Francisco Chronicle. Chinese buyers have the same incentives that fueled the Japanese property investment boom here in the 1990s: high land prices at home and ultra-low interest rates from their banks—far below those of American lenders. Will these well-heeled companies look beyond the cities to resort destinations in the mountains?

—KC

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