Hotel Market Analysis
Anchorage, Alaska
March 2008

Prepared for

AIDEA

Alaska Industrial Development and Export Authority

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INTRODUCTION

The following report is an update of earlier studies prepared for AIDEA in June 2004 and October 2005 for the purpose of understanding the relative strength or weakness of the local lodging market in Anchorage. The current document has been revised and updated to reflect current economic conditions and performance data for the Anchorage lodging market through year-end 2007, culminating in our projections of future lodging market conditions. The data and opinions set forth in this report are based on interviews with state and local officials, hotel owners, managers, and developers, and a variety of other direct and indirect participants in the Alaska's tourism industry. The data and opinions set forth in this report are based on our fieldwork and follow-up research conducted through March 2008.

ECONOMIC OVERVIEW

Local Market Overview

Anchorage is located on a broad plain at the head of Cook Inlet in the south-central region of the state, occupying an area of 1,955 square miles. Anchorage is Alaska's largest metropolitan area, with an estimated 2007 population of roundly 284,000 persons, constituting roundly 42 percent of the state's total population of approximately 677,000. Population growth in the Borough of Anchorage has averaged 1.0 percent annually between 2003 and 2007, only slightly below the 1.1 percent population growth rate achieved by the state as a whole. As the largest city in the state of Alaska, Anchorage plays a dominant role in the state's economy, especially within the areas of transportation, retail sales, oil and gas, medical services, and financial services. With its well established air, rail, and shipping infrastructure, Anchorage serves as the transportation hub for the entire state of Alaska. Anchorage International Airport is by far the largest single source of visitor arrivals to the state. Anchorage International Airport (ANC) served over 5.1 million passengers in FY-2007, up from 4.8 million in 2003. Passenger volumes at ANC have grown at 1.8 percent annually during the 2003 to 2007 period. Due to Anchorage's strategic location, air cargo is also big business locally; with cargo volumes growing at 5.0 percent annually during recent years.

Economic Indicators

Anchorage posted its 19th consecutive year of employment growth in 2007, adding nearly 1,000 new jobs from 2006 levels and 7,600 new jobs since 2003. As shown in Table 1 on the following page, job growth in the Anchorage Borough averaged 1.3 percent annually during the 2003 to 2007 period, albeit with a gradually declining pattern of annual growth trends. The state employment forecast for 2008 anticipates another year of modest growth in employment in the Anchorage area. Unemployment rates in the market have been trending down in recent years, falling from 6.2 percent in 2003 to 5.0 percent in 2007.

Employment growth in recent years has been strongest within the Education & Health sector, with annual growth of 3.4 percent, representing over 2,400 new jobs, and also in the Financial Activities sector with annual growth of 3.6 percent, representing over 1,200 new jobs. Growth in

Table 1
Anchorage Borough Economic Indicator Summary

Employment:	**2003**	**2004**	**2005**	**2006**	**2007***	**CAAGR**
Total Industries	140,395	141,614	144,382	147,055	148,034	1.3%
% chg.		0.9%	2.0%	1.9%	0.7%	
Goods Producing						
Natl. Resource & Mining	2,153	2,169	2,147	2,330	2,633	5.2%
Construction	8,560	9,146	9,600	9,669	9,244	1.9%
Manufacturing	1,781	1,754	1,848	1,907	1,917	1.9%
Service Providing						
Trade, Trans. & Utilities	32,812	32,839	32,838	33,336	33,427	0.5%
Information	4,477	4,388	4,386	4,390	4,312	-0.9%
Financial	7,986	8,199	8,409	9,222	9,204	3.6%
Prof. & Business	15,890	15,860	16,172	16,500	16,916	1.6%
Education & Health	17,064	18,294	19,050	19,451	19,507	3.4%
Leisure & Hospitality	14,605	14,637	15,184	15,318	15,658	1.8%
Government	29,370	28,947	29,248	29,231	29,319	0.0%
Unemployment Rate:	6.2%	5.9%	5.5%	5.2%	5.0%	
Population:						
State of Alaska	647,773	647,314	664,060	670,958	676,987	1.1%
Anchorage	273,024	277,810	278,294	283,244	283,823	1.0%
Fairbanks	28,924	30,101	31,104	30,179	31,627	2.3%
Fairbanks North Star Borough	82,160	85,453	87,704	87,766	90,963	2.6%
Juneau City & Borough	31,294	31,122	31,225	30,811	30,305	-0.8%
Denali Borough	1,916	1,850	1,823	1,796	1,731	-2.5%
Anchorage International Airport						
Total Air Passengers	4,791,387	4,876,170	5,123,701	5,043,047	5,139,159	1.8%
Cargo Take-off Weights	23,972,815	24,459,763	26,732,329	27,967,542	29,130,772	5.0%
Lodging Tax Reciepts						
Anchorage Borough	$10,216,624	$11,601,141	$11,805,843	$19,196,639	$20,424,208	18.9%
% chg.		13.6%	1.8%	62.6%	6.4%	
Cruise Passenger Trends						
Total Cruise Passengers	777,000	884,400	953,400	958,900	1,029,800	7.3%
% chg.	5.0%	13.8%	7.8%	0.6%	7.4%	
Denali National Park						
Total Visitors	359,838	404,234	403,520	415,935	458,307	6.2%
% chg.	1.8%	12.3%	-0.2%	3.1%	10.2%	
Inflation Trends - CPI-U						
Anchorage	2.7%	2.6%	3.1%	3.2%	2.2%	
United States	1.6%	2.3%	2.7%	3.2%	2.8%	

* *ALMIS Feb-07 Benchmark Data*

Sources:
Alaska Dept. of Labor; US Census, AIA, ACVB, NPS, Anchorage Borough

both sectors has slowed in recent years. The Professional and Business Services sector posted growth of 1.6 percent annually over the period, adding over 1,000 new jobs in the market, with the bulk of this growth in the last several years. In this sector, growth in the oil and mining industries is expected to be offset by declines in the construction related architectural and engineering services. The Construction sector grew at 1.9 percent annually between 2003 and 2007, adding nearly 700 new jobs, but 2007 showed the first recent decline in employment in this sector. While residential construction has largely stalled following a national trend, commercial construction levels remain high and major projects are expected to sustain employment levels in this sector at, or near, current volumes in 2008. The Leisure and

Hospitality sector grew at 1.8 percent annually over the period, adding over 1,000 new jobs. Continued growth in this sector will be supported by a steady stream of new hotel construction projects proposed in the market in coming years.

Oil production related employment is a major driver of the state's resource-based economy, if not a dominant employer. With current record high oil prices approaching $115 per barrel, the State of Alaska was rewarded with massive royalties that filled state coffers in 2007, resulting in extensive state spending in the recently passed $11B operating budget, $2.9B capital budget, and $5B deposited to state savings accounts. The stratospheric rise in oil prices have resulted in a dramatically renewed interest in exploration and development activities in the oil and gas sectors, as evidenced by Shell Oil Company’s continuing efforts to gain approval for exploration of coastal waters in the Beaufort Sea, just offshore from ANWR and its recent involvement in securing $2.1 billion in oil and gas leases in the Chukchi Sea off of Alaska’s northwest coast in February 2008.

The biggest item on the horizon in the oil and gas industry in Alaska hinges on current legislative efforts to secure proposed construction of a proposed $30B natural gas pipeline. Trans-Canada provided the only AGIA (Alaska Gasline Inducement Act)compliant proposal for development of the pipeline, which is currently under reviewed by the Governor’s office and is expected to be presented to the state legislature in the upcoming special session in mid-2008. Meanwhile, Conoco-Phillips announced that it would pursue its own version of the gas pipeline without the $500M in state subsidies offered under AGIA. In early April, BP announced it would join forces with Conoco to pursue development of the gas line, with this new venture expected to spend $600M over the next three years on engineering and fieldwork related to the project. While the outcome is still far from certain, it appears that Alaska may soon be capitalizing on a project that it has pursued for over 30 years. Given the massive cost and scale of this $30 billion project, its economic impact within the state would be substantial, although it is likely to be distributed over a protracted period of time. If this project moves forward, Anchorage would likely play a key role in the development and planning phases, whereas Fairbanks would likely benefit more heavily during the construction phase.

The current level of interest and the amount of capital that is being committed to this project are favorable indicators that provide direct benefit to the Anchorage economy while fueling speculation and anticipatory spending. However, while this project now appears closer to fruition that at any time in its 30-year history, there is still no certainty that it will move forward. While our projections are not predicated on the gas line moving forward, the successful launch of this project would clearly signal the beginning of another major boom period for the economy of the state as a whole.

The tourism sector has a dramatic influence on the economy of Anchorage and that of the state as a whole, with the primary drivers being the cruise industry and the lodging industry. Anchorage is the economic center of the tourism industry in the state, due to its role as the regional hub of transportation throughout the state. Tourism continues to bring more visitors and more money to Anchorage than to any other Alaskan location. Summer visitor studies completed in recent years indicated summer visitors to the state have increased by over 6.9

percent annually between 2003 and 2007, with approximately 38 percent arriving by cruise ship and 52 percent by air. Cruise passenger volumes grew by 7.3 percent annually between 2003-2007 with the Alaska cruise industry reporting roundly 1,030,000 cruise passengers in 2007. Thus far, the 2006 passage of the head-tax on cruise passengers appears to have had no material impact on cruise demand patterns in the state. While Anchorage receives considerable direct benefit from the cruise industry, its role has shifted somewhat in recent years as the cruise lines more efficiently transfer passengers between ship, rail, and plane, moving passengers more quickly through Anchorage and on to their wilderness destinations. While Anchorage is not a key destination for cruise/tour demand, its air, rail, and highway infrastructure ensures that it will continue to play a key role in the logistics of moving visitors throughout the state. Lodging tax receipts in the Anchorage market have posted a tax-adjusted 7.4 percent average annual increase between 2003 and 2007, which is indicative of solid and sustained growth in all segments of demand in the local market during this period.

Denali National Park remains the emotional heart of Alaska's tourism industry and is a dominant component of most land tour packages. Denali National Park visitor volumes were up over 10 percent in 2007 compared to 2006 and averaged 6.2 percent annually over the 2003 to 2007 period. Each of these visitors passes through Anchorage at least once on their migration to the 'great one'. While there have been substantial increases to the hotel inventory in Denali in recent years, much of the increased inventory has been used to accommodate longer stays at Denali, and the bottleneck remains the federal cap on park visitation. Access restrictions within the park will continue to limit the quantity and quality of the Denali experience for many visitors to the state. After numerous rounds of planning since the 1960's, it appears that consensus has finally been reached regarding additional access and development near the southern portions of Denali National Park. Current plans call for development of the new south Denali access road at milepost 134 of the Parks Highway. The new road will extend 3.5 miles to Curry Ridge, where a 16,000 square foot, $26M visitor center and 13-miles of hiking trails are planned for development. While the south access project will benefit all visitors to Denali National Park, the communities and businesses south of the park are expected to see significant benefit.

A variety of macroeconomic factors are influencing demand patterns in the current environment and are expected to continue to do so over the near term. The softening, or near recessionary conditions in the larger U.S. economy, skyrocketing costs of fuel and groceries, tightening lending markets, and the recent collapse of the sub-prime mortgage markets, all translate to lower levels of discretionary income. These factors are expected to exert downward pressure on leisure travel patterns over the near to mid-term. Conversely, the low value of the dollar on the world currency markets tends to enhance domestic travel patterns while allowing the U.S. to capture a larger share of the foreign travel markets. Alaska is expected to remain a highly desirable travel destination for domestic and foreign visitors alike. Also on the positive side, unlike the rest of the nation, Alaska markets may see continued benefit from high oil, gas, and minerals pricing which enhances exploration and development activity in the state's resource-based economy, thereby resulting in upward pressure on commercial demand patterns. While the macroeconomic signals are somewhat negative, we are reasonably confident that Alaska will avoid a major downturn in its economy and that softening or declines in one sector may be offset by growth in other sectors.

LODGING MARKET ANALYSIS

Anchorage Lodging Market Overview

The Anchorage hotel market is largely concentrated in three geographic areas within the city: the downtown core, the airport area, and the midtown area (south of downtown and northeast of the airport). Of these three areas, the larger, first-class hotels (with the exception of the Millennium Alaskan Hotel) are located in the downtown area, while mid-market hotels are more widely dispersed among all three geographic submarkets. Because the distance between these areas is relatively short (approximately a 10-minute drive), most travelers seeking accommodations in Anchorage typically base their decision on factors other than just geographic location within the city.

For the purpose of our analysis, we defined the Anchorage lodging market into two primary tiers of quality, categorized as upscale and mid-scale. Properties have been classified based on physical attributes, service quality, room pricing, and performance. The table on the following page identifies those properties in each of the two primary tiers, including key physical attributes and current seasonal pricing of guestrooms. Our analysis does not include many of the smaller, older, or independent hotels in the market, nor those in several of the outlying areas.

There have been no changes to the upscale lodging market since our prior study. The upscale lodging market currently consists of five hotels: the Hilton, Sheraton, Captain Cook, and Marriott, each located in the downtown core, and the Millennium Alaskan Hotel, located near the airport. These hotels range in size from 248 to 606 rooms; collectively, they represent an inventory of 2,168 available guestrooms. The upscale hotels include full-service facilities offering one or more restaurants and lounge areas and meeting and banquet space ranging from 5,500 square feet to nearly 22,000 square feet. The upscale lodging market experienced no change is the available room supply during the 2003 to 2007 period. The most recent supply change in this submarket occurred with the April 2000 opening of the 392-room Marriott.

The mid-scale market currently consists of 23 hotels, including two with regional brands, 20 with national brands or franchises, and one that is operated independent of a chain affiliation. These hotels range in size from 79 rooms to 246 rooms and represent a current inventory of 2,917 available rooms. Between 2003 to 2007, the daily available room supply in this sub-market increased by a net amount of 495 guestrooms, representing growth in supply of 4.7 percent compounded annually over the period. This supply growth primarily reflects the opening of the Aspen Suites, Fairfield Inn & Suites, Homewood Suites, and the Motel 6, all of which opened in 2004, together with partial year impact from the 2003 openings of the Aspen Downtown, the Ramada Inn Downtown, and minor fluctuations in room counts at the Howard Johnson and the Holiday Inn Express. During this period the two Aspen hotels were sold and converted to the Extended Stay Deluxe brand and the Best Western Barratt Inn lost its affiliation with Best Western and is slated to be re-branded as two different brands, a Quality Inn and Econolodge. The size, type, and quality of facilities offered in the mid-scale market are considerably more diverse than in the upscale market. Most hotels in the mid-scale market are limited-service facilities, although more than 40 percent full-service or focused-service hotels are also included. Most of the mid-scale hotels have relatively limited meeting and conference facilities and, as such, are unable to compete aggressively for group related demand, the bulk of which is captured by the larger hotels downtown. While most of the hotels in our market have three-diamond, AAA ratings, six of the hotels have a two-diamond AAA rating and one has a one-diamond, AAA rating. There has been an increasing trend toward lower participation in the AAA guide in recent years for many of the better quality properties in the market as indicated by the N/R (not rated) designation. We interpret this not as an indication of declining asset quality, but more likely a shift in marketing emphasis on the part of local operators.

Table 2
Profile of the Competitive Hotel Properties
Anchorage, Alaska

						Meeting Space (SF)		2008 Room Rates AAA/Corp Sgl/Dbl		
Mid-Scale Submarket	Location	AAA Rating	Open Date	Rooms	F&B	Total Area	Largest Room	Summer	Winter	Amenities
Extended Stay Deluxe	Downtown	N/R	2003	89	0/0	1,100	1,100	$180-$210	$85-$115	ABCDE
Extended Stay Deluxe	Midtown	N/R	2004	138	0/0	0	0	$185-$220	$95-$115	CDE
Barratt Inn	Airport	◆◆	1963-86	217	1/1	2,400	1,400	$125-$229	$79-$95	CDE
BW Golden Lion	Midtown	◆◆	1977	83	1/1	1,800	952	$173-$183	$89-$99	CE
Clarion Suites	Downtown	◆◆◆	1998	111	1/0	900	900	$140-$233	$140-$233	ABCDE
Comfort Inn	Downtown	◆◆◆	1992	100	0/0	600	600	$190-$240	$100-$140	ABCDE
Courtyard by Marriott	Airport	N/R	1997	154	1/1	1,500	1,000	$239-$299	$139-$179	ABCDE
Days Inn	Downtown	◆◆	1979-94	130	1/0	575	575	$179-$189	$67-$82	DE
Dimond Center Hotel	South Anch.	◆◆◆	2002	109	0/0	1,920	1,280	$124-$269	$124-$269	CDE
Fairfield Inn & Suites	Midtown	◆◆◆	2004	106	0/0	0	0	$98-$197	$98-$197	ABCDE
Hampton Inn	Midtown	◆◆◆	1997	101	0/0	300	300	$269-$319	$179-$209	ABCDEF
Hawthorn Suites, Ltd.	Downtown	◆◆◆	1999	111	0/0	3,000	3,000	$149-$240	$149-$240	ABCDE
Hilton Garden Inn	Midtown	◆◆◆	2002	125	1/1	2,100	2,100	$299-$309	$199-$209	ABCDEF
Howard Johnson Plaza	Downtown	◆◆	1971	246	1/1	7,000	2,500	$85-$149	$85-$149	ACE
Holiday Inn Express	Airport	◆◆◆	1999	129	0/0	576	576	$242-$269	$109-$129	ABDE
Homewood Suites	Midtown	◆◆◆	2004	122	0/0	1,728	960	$309-$489	$229-$359	ABCDEF
Microtel Inn & Suites	Airport	◆◆	1997	79	0/0	400	400	$160-$170	$75-$85	BE
Motel 6	Midtown	◆	2004	85	0/0	0	0	$139	$64-$75	E
Ramada Inn	Downtown	◆◆	1960-03	90	1/1	800	800	$79-$249	$79-$249	CE
Residence Inn	Midtown	N/R	1999	148	0/0	700	700	$285-$395	$169-$205	ABCDE
SpringHill Suites	Midtown	N/R	1998	102	0/0	200	200	$269	$92-$159	ABCDE
Westmark Hotel	Downtown	◆◆◆	1970	200	1/1	5,750	3,700	$139-$239	$139-$239	CF
Coast International Inn	Airport	◆◆◆	1973	142	1/1	5,700	3,700	$84-$169	$84-$169	CE
Subtotal				2,917		39,049				
Upscale Submarket										
Anchorage Hilton	Downtown	◆◆◆	1958-84	606	3/2	21,813	7,680	$290	$180	ABCDEF
Hotel Captain Cook	Downtown	N/R	1965	547	4/4	18,507	9,000	$250-$290	$150 - $190	ABCDEF
Marriott Hotel	Downtown	◆◆◆	2000	392	1/1	10,415	8,122	$187-$308	$187-$308	ABCDEF
Millenium Hotel	Airport	◆◆◆	1986	248	1/1	5,500	2,685	$290-$310	$170-$190	BCDEF
Sheraton Hotel	Downtown	◆◆◆	1979	375	2/2	15,047	9,375	$349	$209	BCDEF
Subtotal				2,168		71,282				
TOTAL				**5,085**		**110,331**				

Amenities: A Pool; B Spa; C Exercise; D Bus. Ctr.; E Gst Ldry.; F Retail

Source: K&M interviews, phone survey, AAA-2008, individual websites

Historical Supply and Demand

Table 3, presented on the following page, summarizes information regarding the historical operating performance of the competitive hotels in Anchorage's mid-scale and upscale markets for the period 2003 through 2007. Key indications from this summary are as follows:

- During 2003, two new hotels were added to the market, followed by four new hotels in 2004. Collectively these six hotels added 630 new guestrooms to the market, all of which occurred in the mid-scale submarket.

- While numerous new hotel projects have been proposed in Anchorage in recent years, repeated delays resulted in no new hotel openings in the market between 2005 and 2007. The next new hotel is expected to open in May 2008, followed by another in spring 2009. This reprieve from new hotel openings has provided the market with an extended retrenchment period and while occupancies have remained relatively flat, average room rates have increased considerably in the last two years.

- Between 2003 to 2007, demand growth in the overall market out-paced supply in three of the five years. In aggregate during this period growth in demand averaged 4.4 percent annually compared to growth in supply of 2.6 percent annually. Demand growth continues to be influenced by strong summer tourist seasons, solid convention and group demand, especially in 2006, and the general economic growth occurring within the state.

    - Occupancies in the upscale submarket have improved steadily in recent years, rebounding from their low in 2003 of 62 percent to roundly 70 percent in 2006 and 2007. Occupancies in this segment of the market are reflective of the large average size of these hotels and their greater reliance on group related demand. The considerable improvement in the upscale submarket over the period reflects growth across all demand segments and strong group and convention related activities throughout the year, including the return of AFN in 2006. According to the ACVB, group bookings for 2008 are slightly lower than 2006, while 2009 and 2010 show moderate improvement. Early sales of the new convention center are expected to ramp-up quickly once the center opens in fall-2008.

    - Within the mid-scale submarket, occupancies increased from a low of 71 percent in 2003 to a high of 75 percent in 2005 and 2006, before declining slightly to the mid 73 percent range in 2007. We attribute the modest decline in occupancy to several factors including diminishing quality in the lower end properties in this sector, which has reduced occupancy, and to the aggressive rate increases implemented by many of the better quality assets in this submarket, which may be driving demand to the upscale submarket during off-peak periods. Nonetheless, considering the large increase in the base of available rooms in this submarket during the period, its ability to maintain such strong occupancies is still remarkable.

- The local market continues to benefit from strong performance across all demand segments. Growth in corporate and government demand is derived from continued economic expansion and diversification in the local economy, high levels of new construction in both the public and private sectors, and anticipatory spending related to high oil and gas prices. Group demand patterns continue to be strong, with ACVB delivering solid convention volumes in 2004, 2005, and 2006, and modest softening in

2007. We expect significant growth beginning in 2009 and beyond as new groups begin to fill the Dena'ina Civic & Convention Center. The leisure travel segment has been remarkably stable in recent years. The contract demand segment continues to grow, albeit slowly, largely fueled by the cargo carriers. While this demand continues to shift between various hotels in search of the optimal combination of price and facilities, it is considered a stabilizing force in the market.

- During the period of supply expansion, 2003 to 2005, average room rates in the overall market were fairly static, in the range of $107 to $108. However, subsequent years showed considerable growth, increasing from roundly $107 in 2005 to $121 in 2007. Recent growth has been influenced by numerous factors including: more aggressive rate increases during periods of no supply change; stabilizing of the newer hotels; renovation of several of the older properties; and lower levels of discounting in the market which often accompanies the opening of new properties. While the long-term growth in average room rate remains at, or near, inflationary levels, the market has benefited from substantial real growth in recent years.

    - Average room rates within the upscale submarket grew significantly in both 2006 and 2007 following several years of dormancy. This rate growth is attributable to strengthening occupancies, lack of growth in rooms supply, and continued rate pressure by the better quality hotels in the mid-scale submarket.

    - Average room rates in the mid-scale submarket also have grown significantly in 2006 and 2007, following the plateau in rates as the market absorbed the sizeable volume of new guestrooms in prior years. Many of the newer, better quality assets in this submarket have aggressively pushed room rates in recent years, with some achieving double-digit growth with rates that have at times exceeded those of the larger, full-service hotels downtown.

- The overall market achieved growth in revenue per available room (RevPAR) during the 2003 to 2007 period of 4.5 percent annually, increasing from roundly $73 to $87. During this same time period, rate growth in the upscale submarket increased at 5.3 percent annually compared to growth in the mid-scale submarket of 4.1 percent annually.

- As in prior studies of the market, lodging performance levels in Anchorage compare very favorably to national averages. In 2007, the Anchorage lodging market posted a 72 percent occupancy rate and a $121 average rate, compared to U.S. averages in 2007 of 63 percent occupancy and a $98 average room rate, as indicated by Smith Travel Research.

Table 3											
Competitive Lodging Market Overview - 2003 through 2007											
Anchorage, Alaska											
	Available Rooms		**Fair**	**Occ.**	**Occupied**	**Market**	**Penetr'n**	**Average**	**Room Revenue**		**REVPAR**
	Daily	Annually	**Share**	**Rate**	**Rm. Nights**	**Share**	**Rate**	**Rm. Rate**	Total	Per Rm.	**Index**
2007											
Mid-Scale Submarket	2,917	1,064,549	57.4%	73%	781,814	58.6%	102.2%	$109.00	$85,027,561	$80.00	92.0%
Upscale Submarket	2,168	791,320	42.6%	70%	551,435	41.4%	97.0%	$138.00	$75,978,165	$96.00	110.3%
Total Market	5,085	1,855,869	100.0%	**72%**	1,333,249	100.0%	100.0%	$121.00	$161,005,726	$87.00	100.0%
% chg.		-0.1%			-1.4%				5.2%	6.1%	
2006											
Mid-Scale Submarket	2,921	1,066,165	57.4%	75%	795,363	58.8%	102.5%	$100.00	$79,496,414	$75.00	91.5%
Upscale Submarket	2,168	791,320	42.6%	70%	556,222	41.2%	96.6%	$132.00	$73,583,304	$93.00	113.4%
Total Market	5,089	1,857,485	100.0%	**73%**	1,351,585	100.0%	100.0%	$113.00	$153,079,718	$82.00	100.0%
% chg.		0.0%			1.7%				7.6%	6.5%	
2005											
Mid-Scale Submarket	2,921	1,066,165	57.4%	75%	795,913	59.9%	104.3%	$94.00	$75,092,647	$70.00	90.9%
Upscale Submarket	2,168	791,320	42.6%	67%	533,058	40.1%	94.2%	$126.00	$67,130,318	$85.00	110.4%
Total Market	5,089	1,857,485	100.0%	**72%**	1,328,971	100.0%	100.0%	$107.00	$142,222,965	$77.00	100.0%
% chg.		5.6%			7.2%				6.3%	1.3%	
2004											
Mid-Scale Submarket	2,649	966,899	55.0%	74%	714,896	57.7%	104.9%	$95.00	$67,998,722	$70.00	92.1%
Upscale Submarket	2,168	791,320	45.0%	66%	524,764	42.3%	94.1%	$125.00	$65,796,057	$83.00	109.2%
Total Market	4,817	1,758,219	100.0%	**71%**	1,239,660	100.0%	100.0%	$108.00	$133,794,779	$76.00	100.0%
% chg.		4.9%			10.3%				9.9%	4.1%	
2003											
Mid-Scale Submarket	2,422	884,203	52.8%	71%	631,500	56.2%	106.5%	$96.00	$60,380,000	$68.00	93.2%
Upscale Submarket	2,168	791,320	47.2%	62%	492,459	43.8%	92.8%	$125.00	$61,384,545	$78.00	106.8%
Total Market	4,590	1,675,523	100.0%	**67%**	1,123,959	100.0%	100.0%	$108.00	$121,764,544	$73.00	100.0%
% chg.		6.1%			-1.0%				-5.1%	-9.9%	
Compound Average Annual Growth Rate 2003 - 2007											
Mid-Scale Submarket	4.7%	4.7%			5.5%			3.2%	8.9%	4.1%	
Upscale Submarket	0.0%	0.0%			2.9%			2.5%	5.5%	5.3%	
Total Market	2.6%	2.6%			4.4%			2.9%	7.2%	4.5%	
Source: Kennedy & Mohn, P.S.											

Cruise/Tour Market Factors

The Anchorage market derives a significant volume of leisure demand from cruise/tour activities within the state. While the bulk of this is generated by the big-three (Princess, Holland America, and Royal Celebrity), secondary tour and motor coach operators are also quite active in the market. As the primary point of arrival or departure in the state, Anchorage also captures pre or post-cruise demand even from visitors on a cruise-only itinerary. Denali National Park is a dominant component of most land tour packages, regardless of the provider. Changes to tour packages and ship disembarkation points in recent years has improved efficiencies for the larger tour operators, thereby enabling them to more expeditiously move passengers from ships directly to their wilderness lodges. While this has exerted downward pressure on hotel demand in Anchorage, the effect of these changes appears to be fully recognized in current demand patterns within the Anchorage market. The volume of cruise/tour demand in the Anchorage market appears to be fairly stable at current levels and we do not expect any further erosion of this demand in the near term.

The dominant players in the state's cruise/tour market are Princess, Holland America, and Royal Celebrity. Neither Princess nor Royal Celebrity has hotel assets in the Anchorage market and as a result, they place their cruise/tour demand in the larger, first-class hotel downtown. While Holland America owns Westmark Hotels, which does have a presence in the Anchorage market, the bulk of their cruise/tour demand is also placed in the larger, first-class hotels downtown.

Princess has repeatedly expanded their two wilderness lodges in Denali in recent years, from a combined rooms inventory in 2004 of 774 rooms to 1,116 rooms in 2008, an increase of 44 percent. Similarly, Holland America completed the 135-room first phase of a potentially 540-room lodge in Denali in 2006. While there are presently no active plans for the second phase expansion of this project, this could change at any time. Several years ago CIRI announced their intention to build approximately 200 new rooms in Denali and while this project has not moved forward yet, it also remains active. CIRI is also planning a 50-room expansion (scaled down from 100 rooms previously) to their Talkeetna Lodge property.

Our recent interviews have produced mixed reviews from tour operators, with several indicating a moderate slowing of demand patterns for 2008, while others indicate that 2008 will be flat to slightly up from 2007 numbers. Macro economic factors including the softening economy in the lower-48, lower levels of disposable income, and perpetually increasing fuel costs could potentially exert downward pressure on demand in this sector of the market.

Seasonal Factors

The Anchorage lodging market is highly seasonal, with market-wide occupancy levels historically averaging greater than 85 percent from June through early September. During much of this period, the better-quality properties in the market typically run at, or near, practical capacity levels. Conversely, occupancy levels during off-peak periods typically fall to the mid-40 percent range, gradually improving during shoulder months. Seasonal demand patterns in Anchorage have moderated somewhat in recent years, as a result of the increase in the available room supply, making more rooms available to meet peak season demands, and also heightening competition for the limited base of demand during off-peak periods. In the mid to late 1990’s, peak season typically ran from May 15th to September 15th, whereas recent interviews suggest this peak now begins in early June and lasts until the beginning of September. Given the significant seasonal swings in demand, hotels in the market have historically used a two-tiered seasonal rate structure, with off-peak advertised room rates typically half the peak season rates. The combined effect of seasonal changes in room rates and demand patterns are visible in the historical trends in hotel room tax receipts reported by the Municipality of Anchorage, as shown in the following table. In 2005, Anchorage residents approved an increase in the lodging tax from 8.0 percent to 12.0 percent to fund construction of the new convention center. Comparisons with prior years should recognize that this tax became effective in January 2006.

Table 4						
Anchorage Hotel Motel Tax Receipts - 2003 - 2007						
	1st Qtr.	**2nd Qtr.**	**3rd Qtr.**	**4th Qtr.**	**Total**	**% Chg.**
2003	1,381,000	2,924,934	4,339,020	1,571,670	10,216,624	
2004	1,501,222	3,340,719	5,044,822	1,714,378	11,601,141	13.6%
2005	1,498,116	3,324,896	5,241,343	1,741,488	11,805,843	1.8%
2006	2,502,674	5,486,493	8,326,573	2,880,899	19,196,639	62.6%
2007	2,755,015	6,056,421	8,755,500	2,857,272	20,424,208	6.4%
% of 2007 Annual	13%	30%	43%	14%	100%	
CAAGR 2003-2007 (1)	7.4%	8.4%	7.7%	4.9%	7.4%	

Note 1: CAAGR reflects tax adjusted basis

Note 2: Lodging tax rate increased from 8.0% to 12.0% in Jaunaury 2006 to fund new convention center

Source: MOA Finance Department - Hotel Bed Tax Receipts

Segmentation

We classified market demand into four general categories: commercial, leisure, group, and contracts. Segmentation data is routinely tracked by hotel operators, although the level of detail and accuracy of the data varies widely between properties. In recent years it has become more and more difficult for hotel operators to maintain accurate segmentation data due to the increased use of Internet booking engines and promotions. While these choices can be attractive to the guest, they hinder the hotel’s ability to accurately track guest segmentation patterns.

Commercial demand is composed of independent business travelers and state and federal government workers. Based on our recent interviews, we estimate this demand represents approximately 42 percent of total demand in the overall market. This demand is reasonably stable throughout the year, with modest declines during summer and holiday periods.

Leisure demand represents approximately 31 percent of total demand in the market for 2007. Demand in this segment consists of independent and packaged leisure travelers, who often come through Anchorage en-route to other areas of the state. The packaged leisure or tour and travel component of this demand, which is heavily cruise oriented, is concentrated almost exclusively within the peak summer season. Due to ocean conditions in the Gulf of Alaska in the spring and fall, further expansion of the peak season window is not expected. However, growth in cruise related demand in recent years has resulted from the addition of newer and larger ships to the Alaska market. According to CLIA, (Cruise Lines International Association), cruise capacity in Alaska has increased on average 6.5 percent annually between 2003 and 2006.

Group demand consists of conventions and meeting related travel to Anchorage, and demand generated by sports teams and school events. Currently, group demand represents approximately 14 percent of total demand in the market. Demand in this segment is typically concentrated during shoulder periods in the spring and fall, although in recent years we have seen increased summer season activity by mid-sized groups.

Contract demand is provided primarily by passenger and cargo airlines serving Anchorage. In 2007, contract demand made up the remaining 13 percent of total demand in the market. Contract demand in Anchorage has historically paid premium rates, due in part to the seasonal timing of demand coinciding with seasonal capacities in the market. However, as the available rooms supply increased and better quality mid-market alternatives became available, rates in this segment have begun to soften. Much of the growth in demand in this segment in recent years has come from the contract airlines and TSA staff, although this component is declining.

Anchorage Convention Center

Since 1997, Anchorage has been pursuing development of a new or expanded convention center to better enable the city to: attract larger groups, accommodate existing groups that have out-grown Egan Center, and allow hosting of multiple events simultaneously. On April 5, 2005 Anchorage voters approved a four-percent increase in the hotel room tax to fund development of a new $103 million, 210,000 square foot convention center. According to Anchorage Convention and Visitors Bureau (ACVB), the Dena'ina Civic & Convention Center broke ground in April 2006 and construction on the project is currently on schedule and on budget, with opening targeted for September 2008. The Dena'ina Center will feature three floors of group-oriented space including a 50,000 square foot exhibit hall, a 25,000 square foot ballroom, a variety of smaller meeting rooms and break-out space, and administration and operation areas. The new facility will increase convention capacity in the city by 300 percent from current levels and will enable the city to host substantially larger groups of up to 5,000 persons, compared to 2,540 person capacity in the existing facility at Egan Center. Dena'ina Center will serve as the cornerstone of Anchorage's new Civic and Convention District, which also includes the existing Egan Center and the Alaska Center for the Performing Arts, all of which will be connected by covered and heated sidewalks in a pedestrian friendly downtown setting. The combined operation of these three facilities will enable Anchorage to accommodate much larger events and multiple events on any given day and should greatly expand the city's ability to attract group and convention related demand. In 1998, Deloitte and Touche completed a study of the proposed convention center which projected that through incremental increases in group sales the new center would enable the city to capture approximately 40,000 new delegates annually at stabilization, representing approximately 90,000 additional room nights of hotel demand. These projections were confirmed in a January 2005 study of the proposed new center completed by Northern Economics Inc. Clearly, the new convention center will be a great asset to the city and, while it is likely to attract new hotel development, it is expected to significantly enhance performance of the existing local lodging market.

SUPPLY AND DEMAND PROJECTIONS

In evaluating the performance potential of the Anchorage lodging market, it is necessary to understand historical and projected changes in the competitive rooms supply and anticipated changes in market demand volumes and patterns over the near to mid-term. Our analysis incorporates new hotels expected to open in the next several years. Projections of growth in future demand reflect contributions from three fundamental sources: unsatisfied demand, induced demand, and underlying growth in demand. A detailed discussion of our analysis is presented in the following paragraphs.

Supply Changes

As shown in the table below, there are eight hotel projects currently proposed for development in Anchorage that we anticipate will impact the performance of the lodging market in future years. While several of these projects are still in the preliminary planning stages, we consider there to be a reasonably high probability that these projects will enter the market in the near to mid-term. Collectively, these projects represent a total of approximately 1,012 potential new rooms.

Proposed Room Supply Changes - Anchorage

Property	Quality	Type	Location	# Rooms	Opening
Upscale market					
Embassy Suites	Upscale	Transient	Mid-town	169	May-08
Crowne Plaza Hotel	Upscale	Transient	Mid-town	166	Mar-09
Mid-scale market					
SpringHill Suites - ANMC	Mid-scale	Transient	Mid-town	164	Mar-09
Comfort Suites	Mid-scale	Transient	Airport	78	Mar-09
Dimond Center Hotel (expansion)	Mid-scale	Transient	So. Anchorage	38	May-10
Tikhatnu Commons (CIRI)	Mid-scale	Transient	East Anchorage	120	May-10
Hyatt Place	Mid-scale	Transient	Mid-town	127	Jun-10
Holiday Inn Express	Mid-scale	Transient	Mid-town	150	Jun-11

Source: K&M - March 2008

As in both of the latest waves of new hotel development in Anchorage, the bulk of preceding projects are being developed by parties that know the Anchorage market intimately, have multiple other hotels operating in the market, and are fully aware of the volume of other new projects in the pipeline. This trend underscores the high degree of confidence many of the current operators place in the stability and resiliency of the Anchorage lodging market.

In addition to the projects detailed above we also identified several other proposed hotel projects that we consider to be somewhat more speculative at the present time.

- a potential hotel of undetermined size at the Anchorage International Airport terminal
- a potential luxury hotel as part of a mixed-use project near the Fifth Avenue Mall in downtown Anchorage
- a potential 350-450 room convention hotel in downtown
- a potential TownePlace Suites hotel in the Mid-town area

- a potential hotel adjacent to the H20-Oasis indoor waterpark in south Anchorage
- a potential reconfiguration of an existing upscale hotel that could result in an approximately 100-room decrease in size

While these projects lack the certainty of the primary projects shown in the preceding table, given their locations or the strength of the developers behind them, we consider it likely that several of these projects may also move forward in the future. Collectively, these projects could represent a net increase of roundly 1,000 additional guestrooms, if all were to go forward, which is highly unlikely. Due to the length of the projection period used in this analysis, we have elected to include several of these projects within our projections of future market conditions. While national indicators suggest that there has been very little fall-out in proposed hotel construction as a result of the current turmoil in the debt markets, this could change as we move through this cycle. In the event that one or more of the projects identified here were not to move forward, this would tend to exert upward pressure on occupancy rates in the market.

Based on our projections of future levels of demand growth and the resulting occupancies in the market, it is reasonable to assume that several of the hotels mentioned above, or other as yet unnamed hotels, will also be built during our projection period. In addition to the eight primary projects, our projections also assume that an additional 180 yet unidentified rooms would enter the mid-market supply between 2011 and 2012. We also include an approximately 450-room upscale convention hotel downtown in mid-2011 and the 100-room reduction in size of one of the existing upscale hotels in 2010.

Demand Changes

Within our analysis, projections of growth in demand reflect the combination of three individual components including unsatisfied demand, underlying growth, and induced demand.

- Unsatisfied demand is that component of new demand that can be accommodated in the market as new hotel rooms open, thereby providing additional capacity during peak periods.

- Underlying growth is projected based on the strength of local and regional economic indicators such as growth in population, employment, growth in room tax collections, and growth in air travel.

- Induced demand reflects changes in the market that result from forces external to the market. Induced demand can be either positive or negative. The opening of a new demand generator within the market might provide a positive inducement of demand, while the opening of competing hotels outside the competitive market, which draws off demand, would result in negative induced demand.

In arriving at our estimates of future demand growth, consideration was given to the mix of demand by segment, seasonal patterns of demand, and the seasonal capacity within the expanding market. Additionally, because of disproportionate growth in the mid-scale market and the resulting transfer of demand between the upscale and mid-scale submarkets, we projected future growth for both submarkets and the overall market. Key factors in our analysis are summarized in the following paragraphs.

- ♦ We estimate underlying growth in demand based on historical changes in key economic indicators, as presented previously in Table 1, tempered with anticipated changes over the near term. The economic data provides support for growth rates generally in the range of one to two percent annually, based on growth in employment, population, and air passenger volumes, with slightly higher growth indicated by room taxes, cruise passengers, and other factors. Our estimates of appropriate growth rates within each demand segment are applied uniformly to both the mid-scale and upscale submarkets.

    - Our projections of underlying growth in demand include growth in the commercial segment of 3.0 percent annually, declining to 2.0 percent at the end of the projection period. Growth in the commercial segment is based on employment growth, anticipated declines in construction activity in the mid-term, and a continued modest contribution from anticipation and optimism surrounding a possible gas pipeline in future years.

    - Within the group demand segment, growth is projected at 2.0 percent annually throughout the projection period, which acknowledges the large volume of induced demand projected to enter the market during the projection period.

    - Leisure demand is projected to grow at 2.0 percent annually during the early years of the projection period, gradually increasing to 3.0 percent annually by the end of our projection period. This estimate reflects anticipated flattening of demand patterns in this segment during the early years of the projection period as indicated by tour operators.

    - Within the contract demand segment growth is projected at 0.0 percent annually during the early years of the projection period, as a result of UPS's recent decision to domicile pilots in Anchorage. Contract demand is projected to grow at 1.0 annually thereafter through the balance of our projection period.

- ♦ Unsatisfied demand is projected based on estimates from managers in the market, which suggest that historically there were between 90 and 120 nights annually when the market filled to capacity and demand was turned away or otherwise unaccommodated. Our interviews suggest that the number of fill nights in the market has been declining in recent years as a result of growth in the available rooms supply. While the market has rebounded somewhat from the low of roundly 60 fill nights indicated in 2003, current interviews suggest that the market experienced on average, approximately 90 fill nights annually in 2007. The experience of individual hotels may vary widely, depending on size, quality, location, and other factors. Our projections include approximately 90 nights of new demand added to the market for each new room opened in 2008 through 2010, declining gradually to 60 nights in subsequent years. Given the somewhat softer performance and larger size of properties in the upscale submarket, 50 fill nights are applied to the proposed convention center hotel project in 2011 and 2012.

- Our projections include the infusion of roundly 70,000 room nights of induced demand captured by the market as a result of the September 2008 opening of the Dena'ina Civic and Convention Center. The bulk of this new demand is induced in 2011 and 2012, it is allocated solely to the group segment, and it is presumed to be primarily captured by the larger group hotels in the upscale submarket. Within our projections we have only induced approximately 75 percent of the total 90,000 room nights of demand originally estimated to be generated by this project.

Table 5, presented on the following page, sets forth our projections of growth in demand throughout the forecast period.

Table 5

Projected Demand Growth by Segment

Mid-Scale Market	**2008**	**2009**	**2010**	**2011**	**2012**	**Mix**
Commercial Demand	355,000	373,900	401,200	423,000	433,800	45%
Underlying Growth	3.0%	3.0%	3.0%	3.0%	2.0%	
Unsatisfied Demand	0	8,200	15,300	9,800	2,300	
Induced Demand	0	0	833	0	0	
Group Demand	78,700	82,800	87,000	93,700	95,600	10%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	2,500	2,500	5,000	0	
Leisure Demand	304,500	318,800	344,500	364,600	377,800	39%
Underlying Growth	2.0%	2.0%	3.0%	3.0%	3.0%	
Unsatisfied Demand	0	8,200	15,300	9,800	2,300	
Induced Demand	0	0	833	0	0	
Contract Demand	61,500	61,500	62,100	62,700	63,300	7%
Underlying Growth	0.0%	0.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	800,000	837,000	895,000	944,000	971,000	100%
Upscale Market						**Mix**
Commercial Demand	223,200	235,500	240,800	253,200	261,400	36%
Underlying Growth	3.0%	3.0%	3.0%	3.0%	2.0%	
Unsatisfied Demand	3,200	5,600	(1,800)	5,200	3,100	
Induced Demand	0	0	0	0	0	
Group Demand	117,100	135,000	145,900	169,000	200,500	28%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	3,200	5,600	(1,800)	5,200	3,100	
Induced Demand	0	10,000	10,000	15,000	25,000	
Leisure Demand	120,000	128,000	130,000	139,100	146,400	20%
Underlying Growth	2.0%	2.0%	3.0%	3.0%	3.0%	
Unsatisfied Demand	3,200	5,600	(1,800)	5,200	3,100	
Induced Demand	0	0	0	0	0	
Contract Demand	111,600	111,600	112,700	113,800	114,900	16%
Underlying Growth	0.0%	0.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	572,000	610,000	629,000	675,000	723,000	100%
Overall Market						
Total Demand	1,372,000	1,447,000	1,524,000	1,619,000	1,694,000	
Commercial Demand	42%	42%	42%	42%	41%	
Group Demand	14%	15%	15%	16%	17%	
Leisure Demand	31%	31%	31%	31%	31%	
Contract Demand	13%	12%	11%	11%	11%	
Total Demand	100%	100%	100%	100%	100%	

Table 6, presented on the following page incorporates our individual projections of growth in supply and demand by submarket into a single presentation of historical and projected changes in the Anchorage lodging market. Based on historical results in the market, we estimate that overall demand growth in the market during the 2003 through 2007 period averaged roundly 4.4 percent annually, outpacing the moderate rate of supply growth during this period of 2.6 percent annually. Our projections reflect supply growth of 6.3 percent annually and growth in demand of approximately 5.4 percent annually. Our projected rate of demand growth is greater than the historical rate of demand growth achieved in the 2003 to 2007 period due to the higher level of rooms growth which will be available to accommodate new demand during peak season periods, and to the benefits expected to be derived from the opening of the new convention center. Overall, we consider this projection to provide a reasonable estimate of future market conditions over the near to mid term.

Based on this analysis, our projections of future market conditions in the mid-scale submarket indicate that occupancy rates will remain relatively stable with occupancies generally in the low to mid-70 percent range throughout the bulk of the projection period, despite continued expansion in the available room supply. Occupancies are projected to fall from recent year levels of 75 percent to roundly 70 percent following the next wave of development. While an occupancy rate of 70 percent is still remarkably strong, occupancies in Anchorage's mid-scale submarket have not dipped to this level since the early 1990's.

Similarly, within the upscale submarket, occupancy rates are projected to fall to the upper 60-percent range following the opening of several new hotels and the early years of operation of the new convention center. Occupancies in this submarket are projected to increase in 2010 as more new demand is attracted to the market by the convention center, before declining again following the assumed opening of a large new convention hotel. We project occupancy levels in the upscale submarket to gradually rebuild in later years, hovering at roundly 69 percent by the end of the projection period.

The blending of these two submarkets indicates overall market occupancies generally in the low to mid-70 percent range throughout the projection period. While the mid-scale submarket is projected to continue the trend of outperforming the larger, upscale properties, the relative gap in performance between these submarkets is expected to diminish considerably from prior years. Much of this rebalancing in the market is attributed to the opening of the new convention center and to a lesser extent, to the expected above-market performance of two new, smaller-sized hotels entering the upscale submarket.

Table 6

Historical and Projected Market Conditions

Historical						Projected				
2003	**2004**	**2005**	**2006**	**2007**		**2008**	**2009**	**2010**	**2011**	**2012**
					Mid-Scale Market					
2,422	2,649	2,921	2,921	2,917	Existing Product	2,917	2,917	2,917	2,917	2,917
					Springhill Suites	0	124	164	164	164
					Comfort Suites	0	59	78	78	78
					Dimond Center (exp.)	0	0	26	38	38
					Hyatt Place	0	0	96	127	127
					Holiday Inn Express	0	0	88	150	150
					CIRI Hotel	0	0	70	120	120
					Unnamed Hotel(s)	0	0	0	106	180
2,422	2,649	2,921	2,921	2,917	Average Daily Rooms	2,917	3,100	3,438	3,699	3,774
884,203	966,899	1,066,165	1,066,165	1,064,549	Annual Room Nights	1,064,549	1,131,341	1,255,021	1,350,174	1,377,354
12.2%	9.4%	10.3%	0.0%	-0.2%	Percentage Change	0.0%	6.3%	10.9%	7.6%	2.0%
631,500	714,896	795,913	795,363	781,814	Market Demand	800,000	837,000	895,000	944,000	971,000
CAAGR		Supply chg.	4.7%			**CAAGR**		Supply chg.		6.7%
CAAGR		Demand chg.	5.5%			**CAAGR**		Demand chg.		5.0%
19,865	83,397	81,017	(550)	(13,549)	Change from prior year	18,186	37,000	58,000	49,000	27,000
3.2%	13.2%	11.3%	-0.1%	-1.7%	Percentage Change					
(15,824)	(16,992)	(20,397)	0	0	Unsatisfied Demand	0	16,469	30,500	19,600	4,500
0	0	0	0	0	Induced Demand	0	2,500	2,500	5,000	
4,041	66,404	60,620	(550)	(13,549)	Underlying Growth	18,186	18,031	25,000	24,400	22,500
1%	11%	8%	0%	-2%	Underlying Growth Rate	2.3%	2.3%	3.0%	2.7%	2.4%
71%	74%	75%	75%	73%	Occupancy	75%	74%	71%	70%	70%
					Upscale Market					
2,168	2,168	2,168	2,168	2,168	Existing Product	2,168	2,168	2,068	2,068	2,068
					Embassy Suites	107	169	169	169	169
					Crowne Plaza	0	126	166	166	166
					Conv. Ctr. Hotel	0	0	0	264	450
2,168	2,168	2,168	2,168	2,168	Average Daily Rooms	2,275	2,463	2,403	2,667	2,853
791,320	791,320	791,320	791,320	791,320	Annual Room Nights	830,359	898,821	877,095	973,395	1,041,345
0.0%	0.0%	0.0%	0.0%	0.0%	Percentage Change	4.9%	8.2%	-2.4%	11.0%	7.0%
492,459	524,764	533,058	556,222	551,435	Market Demand	572,000	610,000	629,000	675,000	723,000
CAAGR		Supply chg.	0.0%			**CAAGR**		Supply chg.		5.8%
CAAGR		Demand chg.	2.9%			**CAAGR**		Demand chg.		6.0%
(30,909)	32,305	8,294	23,165	(4,787)	Change from prior year	20,565	38,000	19,000	46,000	48,000
-5.9%	6.6%	1.6%	4.3%	-0.9%	Percentage Change					
0	0	0	0	0	Unsatisfied Demand	9,626	16,881	(5,357)	15,830	9,308
0	0	0	0	0	Induced Demand	0	10,000	10,000	15,000	25,000
(30,909)	32,305	8,294	23,165	(4,787)	Underlying Growth	10,939	11,119	14,357	15,170	13,692
-6%	7%	2%	4%	-1%	Underlying Growth Rate	2.0%	1.9%	2.4%	2.4%	2.0%
62%	66%	67%	70%	70%	Occupancy	69%	68%	72%	69%	69%
					Overall Market					
4,590	4,817	5,089	5,089	5,085	Average Daily Rooms	5,192	5,562	5,841	6,366	6,627
1,675,523	1,758,219	1,857,485	1,857,485	1,855,869	Overall Market Supply	1,894,908	2,030,162	2,132,116	2,323,569	2,418,699
6%	5%	6%	0%	0%	Supply Growth	2%	7%	5%	9%	4%
1,123,959	1,239,660	1,328,971	1,351,585	1,333,249	Overall Market Demand	1,372,000	1,447,000	1,524,000	1,619,000	1,694,000
-1%	10%	7%	2%	-1%	Demand Growth	3%	5%	5%	6%	5%
CAAGR		Supply chg.	2.6%			**CAAGR**		Supply chg.		6.3%
CAAGR		Demand chg.	4.4%			**CAAGR**		Demand chg.		5.4%
67%	71%	72%	73%	72%	Occupancy	72%	71%	71%	70%	70%

Source: Kennedy & Mohn, P.S.

Average Room Rates

The only thing certain about average room rates is that they are constantly in a state of flux. The direction of change and the relative significance of the change depend on a myriad of forces operating within the market and the response to these forces by the individual operators. Looking strictly at the data, we see that during the period 2003 through 2007, average room rates in the Anchorage market increased at an average of 2.9 percent annually, which represents a marked improvement over the declining rates indicated in our prior study. During this period, many of the hotels in the competitive market achieved growth in average room rates substantially above inflation, as they regained lost ground from prior years. Looking forward, we anticipate that the sizeable volume of new rooms projected to enter the market will significantly curtail growth in average room rates within the overall market in future years. Partially offsetting this downward pressure will be the fact that most of the new rooms entering the market will be competing at the upper end of the rate spectrum within the market, unlike the previous cycle which included the opening of several more moderate rate or economy level properties.

To derive a five-year projection of average room rates, we considered the dual impacts of inflation and anticipated market conditions. We have incorporated an underlying inflation rate of 2.5 percent annually throughout the projection period. Market condition adjustments are based on our estimates of how the market will respond to a variety of factors including, the addition of new rooms in future years, the type and quality of new rooms entering the market, and increased levels of potentially lower-rated group demand following the opening of the proposed convention center.

Our projections of growth in average room rates within the Anchorage market reflect average growth for the overall market at roundly 1.9 percent annually over the 2008 to 2012 period. We project that the market will capture real growth in 2008, prior to the opening of the next wave of new supply. We project rate growth will gradually decline to 1.0 percent in 2010 and 1.5 percent in 2011 as the bulk of the new supply increases competition throughout the market, with nominal rate growth projected for 2012 as the new supply is gradually absorbed within the market. While this projection is considerably more conservative than the 2.9 percent growth achieved by the market in the 2003 to 2007 period, it represents a significant premium over the long term growth in average room rates of roundly 1.0 percent captured by the market over the last decade. Given the size and quality of new hotels expected to enter the market in the near term, we consider this projection to be reasonable. Our projections of growth in average room rate for each submarket are shown in the table on the following page. The resulting average room rate for the overall market is the weighted average reflecting demand patterns and rates within the two submarkets.

Table 7 Projected Average Room Rate And Revenue Per Available Room						
Year/Market	Inflation	Market Response	Total Change	Projected ARR	Projected Occup. %	Projected REVPAR
2007						
Midscale Submarket				$109.00	73%	$80.05
Upscale Submarket				$138.00	70%	$96.17
Overall Market				$121.00	72%	$86.93
2008						
Midscale Submarket	2.50%	1.00%	3.50%	$113.00	75%	$84.92
Upscale Submarket	2.50%	1.00%	3.50%	$143.00	69%	$98.51
Overall Market				$126.00	72%	$91.23
2009						
Midscale Submarket	2.50%	-1.00%	1.50%	$115.00	74%	$85.08
Upscale Submarket	2.50%	-1.00%	1.50%	$145.00	68%	$98.41
Overall Market				$128.00	71%	$91.23
2010						
Midscale Submarket	2.50%	-1.50%	1.00%	$116.00	71%	$82.72
Upscale Submarket	2.50%	-1.50%	1.00%	$146.00	72%	$104.70
Overall Market				$128.00	71%	$91.49
2011						
Midscale Submarket	2.50%	-1.00%	1.50%	$118.00	70%	$82.50
Upscale Submarket	2.50%	-1.00%	1.50%	$148.00	69%	$102.63
Overall Market				$131.00	70%	$91.28
2012						
Midscale Submarket	2.50%	-0.50%	2.00%	$120.00	70%	$84.60
Upscale Submarket	2.50%	-0.50%	2.00%	$151.00	69%	$104.84
Overall Market				$133.00	70%	$93.15
Source: Kennedy & Mohn, P.S.						

CONCLUSION

Based on our current analysis, the Anchorage lodging has performed remarkably well in recent years, slightly outperforming projections in our previous review of the market, with the mid-scale submarket performing largely as expected and the upscale sub-market capturing solid gains. The biggest surprise has been the substantial rate growth achieved in the market in recent years, which has been considerably stronger than our prior projections. While the lodging industry as a whole has achieved significant rate growth during the expansionary economy of recent years, we attribute the growth in Anchorage to repeated delays in the opening of several new hotel projects in the local market and unusually aggressive implementation of rate increases during this slack-tide period in the market. Overall, the outlook for the Anchorage lodging market remains fairly optimistic over the near term and while it is expected to see significant increases in supply, we believe the demand fundamentals are in place to allow the market to absorb the proposed supply changes without major impact. Granted, occupancies will decline somewhat and rate growth will flatten, but barring any major downturn in the economy, the local lodging market is expected to remain comparatively strong. Key factors that are expected to influence the market in the coming years include the drawing power of the new convention center, the potential positive (and negative) impacts of +$100 per barrel oil, and the progress towards securing a natural gas pipeline within the state.

We trust that AIDEA will find the updated analysis and commentary presented in this report to be beneficial for developing an improved level of understanding regarding the current factors influencing the lodging market in Anchorage. Should you have any questions or require clarification on any of the issues discussed in this report, please do not hesitate to contact us.

Sincerely,

Kennedy & Mohn P.S.

Kennedy & Mohn, P.S.

By: Michael J Mohn, MAI
Certified General Real Estate Appraiser
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MJM:tpk

GENERAL ASSUMPTIONS

This market overview study has been prepared under the following general assumptions:

- No responsibility is assumed for matters of a legal nature.
- Responsible ownership and competent property management are assumed.
- The information provided by others is believed to be reliable. However, no warranty is given for its accuracy.
- All engineering is assumed to be correct. The plot plans and illustrative material in this report are included only to assist the reader in visualizing the property.
- It is assumed that there are no hidden or unapparent conditions of the property, subsoil, or structures that render it more or less useful. No responsibility is assumed for such conditions or for arranging for engineering studies that may be required to discover them.
- Full compliance with all applicable federal, state, and local environmental regulations and laws is assumed.
- Full compliance with all applicable zoning and use regulations and restrictions is assumed.
- It is assumed that all required licenses, certificates of occupancy, consents, or other legislative or administrative authority from any local, state, or national government or private entity or organization have been or can be obtained.
- It is assumed that the utilization of the land and improvements is within the boundaries or property lines of the property described and that there is no encroachment or trespass.

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- Projections of future revenue, expenses, net operating income, mortgage debt service, capital outlays, cash flow, or inflation represent our judgment of the assumptions likely to be used by informed persons in the marketplace. These estimates are intended solely for analytical purposes and are not intended to accurately predict future results or events. Actual performance will differ from these projections, and these differences may be significant.

- In accordance with our contract with the client, the accompanying analysis is not intended to be a complete market analysis or appraisal. The purpose of this market overview study is for AIDEA's internal use in evaluating future hotel financing requests within the state.

- Unless otherwise stated in this report, the existence of hazardous substances, including without limitation asbestos, polychlorinated biphenyls, petroleum leakage, or agricultural chemicals, which may or may not be present on the property, or other environmental conditions, were not called to the attention of nor did the consultant become aware of such during the consultant's inspection. The consultant has no knowledge of the existence of such materials on or in the property unless otherwise stated. The consultant, however, is not qualified to test such substances or conditions. The presence of such substances, such as asbestos, urea formaldehyde foam insulation, or other hazardous substances or environmental conditions, may affect the feasibility of the project. Our analysis is predicated on the assumption that there is no such condition on or in the property or in such proximity thereto. No responsibility is assumed for any such conditions, nor for any expertise or engineering knowledge required to discover them.

CERTIFICATION

I certify that, to the best of my knowledge and belief:

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, impartial, and unbiased professional analyses, opinions, conclusions, and recommendations.
- I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest with respect to the parties involved.
- I have no bias with respect to any property that is the subject of this report or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation for completing this assignment is not contingent upon the development or reporting of a pre-determined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this report.
- The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics & Standards of Professional Appraisal Practice of the Appraisal Institute, which include the *Uniform Standards of Professional Appraisal Practice*.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- I have made a personal inspection of the property that is the subject of this report.
- No one provided significant real property appraisal or appraisal consulting assistance to the persons signing this certification.
- As of the date of this report, Michael J. Mohn, MAI has completed the continuing education program of the Appraisal Institute.

Michael J Mohn DSO

Michael J. Mohn, MAI

CCERT Ver.5/2005

Hotel Market Analysis
Fairbanks, Alaska
March 2008

Prepared for

AIDEA
Alaska Industrial Development and Export Authority

Kennedy & Mohn, P.S.
Seattle, Washington

INTRODUCTION

This following report is an update of earlier studies prepared for AIDEA in June 2004 and October 2005 for the purpose of understanding the relative strength or weakness of the local lodging market in Fairbanks. The current document has been revised and updated to reflect current economic conditions and performance data for the Fairbanks lodging market through year-end 2007, culminating in our projections of future lodging market conditions. The data and opinions set forth in this report are based on interviews with state and local officials, hotel owner's, manager's, and developers, and a variety of other direct and indirect participants in the tourism industry in the state and local markets. The data and opinions set forth in this report are based on our fieldwork and follow-up research conducted through March 2008.

ECONOMIC OVERVIEW

Local Market Overview

Fairbanks is located in the Tanana Valley, deep in Alaska's interior region, 358 miles northeast of Anchorage, 125 miles south of the Arctic Circle, and 498 miles south of Prudhoe Bay. The Fairbanks North Star Borough is Alaska's second largest metropolitan area, with a 2007 population of approximately 91,000 persons, constituting roundly 13 percent of the state's total population of approximately 677,000. Fairbanks is the hub of much of the economic activity occurring in Alaska's vast interior region due to its connection to each of the five major highway systems serving the region. Given the remoteness of much of Alaska, the extensive highway system surrounding Fairbanks is a significant asset to independent tourists and commercial travelers alike, with comparatively easy connections north to Prudhoe Bay; southwest to Denali, Anchorage, and the Kenai Peninsula; and southeast to Beaver Creek, Whitehorse, and Skagway.

This geographic location contributes heavily to the allure and the complexities of life and business in Fairbanks. Weather conditions vary dramatically throughout the year in Fairbanks. Winter temperatures average 13 degrees below zero, but can fall to as much as 40 and 50 degrees below zero. In contrast, summer temperatures average 70 degrees and can reach into the 90's during July and early August. During the depths of winter, there may be as few as four hours of daylight each day whereas during summer periods daylight extends to 18 to 20 hours each day.

While temperatures this severe have a natural tendency to limit all but the most essential travel, they also coincide with optimal viewing times for the Northern Lights, which is clearly one of Fairbanks' greatest winter tourism assets. The area's intense winter cold also fuels the economy by providing a perfect environment for advanced cold-weather testing activities that occur in the surrounding area. Despite the often-intense cold, Fairbanks holds a number of winter festivals for residents and guests and during October 2005 and October 2007, was the host city for the Alaska Federation of Natives convention (AFN), the state's largest conference.

Fairbanks is also served by the Alaska Railroad, which opened a new $22.5 million passenger terminal in 2005, located approximately one-mile west of downtown. Air service to Fairbanks is accommodated at the Fairbanks International Airport (FIA), five miles west of downtown. FIA is completing construction of a major new passenger terminal that will be substantially complete later this year, with renovation of existing terminal space to be completed by Summer 2009. These projects will greatly enhance the guest experience at the airport and will improve international arrivals and customs processing. Alaska Airlines provides year round service to Fairbanks, while several other airlines provide peak season connections to the lower-48 and to Europe. Fairbanks infamous “Northern Lights” continues to attract winter tourism from Japan, with 18 private charter flights in 2007, up from 3 flights in 2004. These guests typically stay in the area for four days, alternating between Fairbanks and Chena Hot Springs.

Economic Indicators

As shown in Table 1 on the following page, job growth in the Fairbanks Northstar Borough averaged 1.9 percent annually during the 2003 to 2007 period, representing only a small part of 19 consecutive years of employment growth in the market. Unemployment rates in the market have been trending down in recent years, falling from 6.9 percent in 2003 to 5.2 percent in 2007. State economists forecast continued employment growth in 2008. Employment growth rates in recent years have tapered off to slightly less than one percent growth annually, with the strongest rates indicated within the Manufacturing sector (7.9%), followed by Financial Services sector (5.7%), and the Professional and Business sector (3.6%).

The construction sector in Fairbanks has been a very dynamic sector of the economy in recent years, posting growth of 3.1 percent over the period. Military sponsored projects at Fort Wainwright and Eielson AFB will continue into 2008, as will large State funded projects at the University and at the airport. Private sector construction includes the expansion of Wal-Mart, the remodel of Sam’s Club, a new Safeway, and completion of the Morris Thompson Cultural and Visitors Center downtown. Fairbanks will see three new hotels built in three years, starting with the Alpine lodge in mid-2007, Holiday Inn Express in mid-2008, and Hampton Inn in mid-2009.

Fairbanks is also home to extensive mining activities which, while economically significant, do not contribute substantially to the overall employment base. In 1995, the Pogo gold deposit was discovered about 90 miles southeast of Fairbanks, with subsequent studies indicating that it contains over 5 million ounces of identified gold reserves. After nearly ten years of permitting and construction and $300M in investment, the Pogo Mine officially opened in June 2006. The mine is expected to produce 375,000 to 500,000 ounces of gold annually over a 10-year life and employ 250 to 300 persons. By comparison, the Fort Knox Gold Mine opened in 1997, reportedly with over 4 million ounces of identified gold reserves is producing 330,000 ounces of gold annually with employment of 400 to 425. Recent permits were issued for a heap leach facility at Fort Knox that will increase employment and extend the life of mining activity at this location. High mineral prices in recent years bode well for continued mining activities in the area.

Table 1
Fairbanks Northstar Borough Economic Indicator Summary

Employment:	**2003**	**2004**	**2005**	**2006**	**2007***	**CAAGR**
Total Industries	35,614	36,920	37,898	38,128	38,400	1.9%
% chg.		3.7%	2.6%	0.6%	0.7%	
Goods Producing						
Natl. Resource & Mining	953	981	1,211	1,346	900	-1.4%
Construction	2,482	2,776	2,911	2,764	2,800	3.1%
Manufacturing	517	565	622	632	700	7.9%
Service Providing						
Trade, Trans. & Utilities	7,234	7,477	7,805	7,744	7,800	1.9%
Information	604	576	575	593	600	-0.2%
Financial	1,282	1,312	1,402	1,575	1,600	5.7%
Prof. & Business	1,998	2,102	2,117	2,098	2,300	3.6%
Education & Health	3,901	1,089	4,194	4,277	4,200	1.9%
Leisure & Hospitality	4,000	4,225	4,137	4,109	4,300	1.8%
Government	11,267	11,484	11,552	11,621	11,900	1.4%
Unemployment Rate:	6.9%	6.4%	5.8%	5.6%	5.2%	
Population:						
State of Alaska	647,773	647,314	664,060	670,958	676,987	1.1%
Anchorage	273,024	277,810	278,294	283,244	283,823	1.0%
Fairbanks	28,924	30,101	31,104	30,179	31,627	2.3%
Fairbanks North Star Borough	82,160	85,453	87,704	87,766	90,963	2.6%
Juneau City & Borough	31,294	31,122	31,225	30,811	30,305	-0.8%
Denali Borough	1,916	1,850	1,823	1,796	1,731	-2.5%
Fairbanks International Airport						
Total Air Passengers	830,415	881,118	924,364	918,012	966,898	3.9%
Incoming	419,199	445,750	464,464	462,703	494,879	4.2%
Outgoing	411,216	435,368	459,900	455,309	472,019	3.5%
Cargo (non-transit) 000#	68,485	70,498	78,952	62,676	52,389	-6.5%
Lodging Tax Reciepts						
Fairbanks Northstar Borough	$1,413,877	$1,553,132	$1,520,969	$1,584,040	$1,803,680	6.3%
City of Fairbanks	$1,805,682	$2,142,759	$2,376,095	$2,606,629	$2,685,417	10.4%
Total	$3,219,559	$3,695,891	$3,897,064	$4,190,669	$4,489,097	8.7%
% chg.	3.5%	14.8%	5.4%	7.5%	7.1%	
Cruise Passenger Trends						
Total Cruise Passengers	777,000	884,400	953,400	958,900	1,029,800	7.3%
% chg.	5.0%	13.8%	7.8%	0.6%	7.4%	
Denali National Park						
Total Visitors	359,838	404,234	403,520	415,935	458,307	6.2%
% chg.	1.8%	12.3%	-0.2%	3.1%	10.2%	
Inflation Trends - CPI-U						
Anchorage	2.7%	2.6%	3.1%	3.2%	2.2%	
United States	1.6%	2.3%	2.7%	3.2%	2.8%	

** ALMIS Feb-07 Benchmark Data*

Sources:
Alaska Dept. of Labor; US Census, Fairbanks Borough, FCVB, FIA, NPS

Oil production related employment is a major driver of the state's resource-based economy, if not a dominant employer. With current record high oil prices approaching $115 per barrel, the State of Alaska was rewarded with massive royalties that filled state coffers in 2007, resulting in extensive state spending in the recently passed $11B operating budget, $2.9B capital budget, and $5B deposited to state savings accounts. The stratospheric rise in oil prices have resulted in a dramatically renewed interest in exploration and development activities in the oil and gas sectors, as evidenced by Shell Oil Company's continuing efforts to gain approval for exploration of coastal waters in the Beaufort Sea, just offshore from ANWR and its recent involvement in securing $2.1 billion in oil and gas leases in the Chukchi Sea off of Alaska's northwest coast in February 2008.

The biggest item on the horizon in the oil and gas industry in Alaska hinges on current legislative efforts to secure proposed construction of a proposed $30B natural gas pipeline. Trans-Canada provided the only AGIA compliant proposal for development of the pipeline, which is currently under reviewed by the Governor's office and is expected to be presented to the state legislature in the upcoming special session in mid-2008. Meanwhile, Conoco-Phillips announced that it would pursue its own version of the gas pipeline without the $500M in state subsidies offered under AGIA. In early April, BP announced it would join forces with Conoco to pursue development of the gas line, with this new venture expected to spend $600M over the next three years on engineering and fieldwork related to the project. While the outcome is still far from certain, it appears that Alaska may soon be capitalizing on a project that it has pursued for over 30 years. Given the massive cost and scale of this $30 billion project, its economic impact within the state would be substantial, although it is likely to be distributed over a protracted period of time. If this project moves forward, Anchorage would likely play a key role in the development and planning phases, whereas Fairbanks would likely benefit more heavily during the construction phase.

The current level of interest and the amount of capital that is being committed to this project are favorable indicators that provide direct benefit to the local economy while fueling speculation and anticipatory spending. However, while this project now appears closer to fruition that at any time in its 30-year history, there is still no certainty that it will move forward. While our projections are not predicated on the gas line moving forward, the successful launch of this project would clearly signal the beginning of another major boom period for the economy of the state as a whole.

Between 2003 and 2007, the population in the Fairbanks North Star Borough increased by approximately 8,800 persons, yielding a robust growth rate of 2.6 percent annually. The local military installations, Fort Wainwright Army Base and Eielson Air Force Base accounted for approximately 21 percent of the population in the Borough, or roundly 19,400 persons in 2007. During the 2003 to 2007 period, the military population in Fairbanks grew at 3.4 percent annually, which contributed significantly to the overall growth in population in the area. This growth was attributed primarily to Fort Wainwright, as a result of the transformation of the 172nd Brigade from a light-infantry brigade to a Stryker brigade. Population growth within the City of Fairbanks posted a 2.3 percent average annual growth between 2003 and 2007, reversing a declining trend in population since the late 1990's.

The U.S. military continues to exert significant influence on the economy of the Fairbanks area, with two nearby military bases including Fort Wainwright Army Base and Eielson Air Force Base. Collectively, these two bases reported over 7,700 active military personnel in Q4-2007 (19,378 including family members and dependents). With growth in the military population of 3.4 percent annually in recent years and continued growth expected through 2013. The combined effects of increasing military population and deployment cycles created a substantial need for off-base lodging in the Fairbanks market in late 2006 and early 2007 when the military contracted approximately 400 units in area hotels and apartments, representing nearly 40,000 room nights of demand. While only a portion of this demand was accommodated within the mid-market and upscale hotels in Fairbanks, the resulting compression in the market influenced the performance of all properties. Military sources indicated that this event was likely an isolated occurrence and military demand for off-base lodging in future years is expected to return to more traditional levels of 4,000 to 6,000 rooms annually.

The tourism sector has a dramatic influence on the economy of Fairbanks and that of the state as a whole, with the primary drivers being the cruise industry and the lodging industry. Summer visitor studies completed in recent years indicated summer visitors to the state have increased by over 6.9 percent annually between 2003 and 2007, with approximately 38 percent arriving by cruise ship and 52 percent by air. Cruise passenger volumes grew by 7.3 percent annually between 2003-2007 with the Alaska cruise industry reporting roundly 1,030,000 cruise passengers in 2007. Thus far, the 2006 passage of the head-tax on cruise passengers appears to have had no material impact on cruise demand patterns in the state. Fairbanks continues to benefit from its location as a turn-point for most land-tour alternatives in the state. Air passenger data recorded at Fairbanks International Airport for 2007 indicates nearly 967,000 total passengers for the year, an increase of more than 136,000 passengers since 2003. Average annual passenger growth during this period averaged 3.9 percent. Lodging tax receipts in the Fairbanks market have posted an 8.7 percent average annual increase between 2003 and 2007, reflective of growth in tourist volumes in recent years and increases in the quality and quantity of the available rooms inventory in the market during this period.

In 2007, Fairbanks began a planning process entitled *'Vision Fairbanks'* aimed at identifying opportunities to enhance and revitalize the downtown area. The results of this planning exercise were published in February 2008. One of numerous opportunities identified in the study was potential for development of a civic-anchor for the downtown core. As envisioned by the planners, this component would potentially include a community center, performing arts center, convention center, and potentially a convention hotel. The location recommended for these facilities is near the intersection of Airport Way and Cushman Avenue, at the southern fringe of the downtown core. While this study was only recently completed and implementation is likely years away at best, we understand that the Fairbanks Convention & Visitors Bureau is expected to engage a consultant in 2008 to conduct a feasibility study that will explore the viability of developing a convention center in Fairbanks. The outcome of this feasibility study and the gradual implementation of the recommendations set forth in the Vision Fairbanks study will be important to monitor in future years.

Denali National Park remains the emotional heart of Alaska's tourism industry and is a dominant component of most land tour packages. Denali National Park visitor volumes were up over 10 percent in 2007 and averaged 6.2 percent annually over the 2003 to 2007 period. Fairbanks is a direct recipient of strong demand patterns in Denali, despite the substantial increases to the hotel inventory in Denali in recent years. While much of the increased inventory has been used to accommodate longer stays at Denali, the bottleneck remains the federal cap on park visitation. Access restrictions within the park will continue to limit the quantity and quality of the Denali experience for many visitors to the state. After numerous rounds of planning since the 1960's, it appears that consensus has finally been reached regarding additional access and development near the southern portions of Denali National Park. Current plans call for development of the new south Denali access road at milepost 134 of the Parks Highway. The new road will extend 3.5 miles to Curry Ridge, where a 16,000 square foot, $26M visitor center and 13-miles of hiking trails are planned for development. While the south access project will benefit all visitors to Denali National Park, the communities and businesses south of the park are expected to see significant benefit.

A variety of macroeconomic factors are influencing demand patterns in the current environment and are expected to continue to do so over the near term. The softening or near recessionary conditions in the larger U.S. economy, skyrocketing costs of fuel and groceries, tightening lending markets, and the recent collapse of the sub-prime mortgage markets, all translate to lower levels of discretionary income. These factors are expected to exert downward pressure on leisure travel patterns over the near to mid-term. Conversely, the low value of the dollar on the world currency markets tends to enhance domestic travel patterns while allowing the U.S. to capture a larger share of the foreign travel markets. Alaska is expected to remain a highly desirable travel destination for domestic and foreign visitors alike. Also on the positive side, unlike the rest of the nation, Alaska markets may see continued benefit from high oil, gas, and minerals pricing which enhances exploration and development activity in the state's resource-based economy, thereby resulting in upward pressure on commercial demand patterns. While the macroeconomic signals are somewhat negative, we are reasonably confident that Alaska will avoid a major downturn in its economy and that softening or declines in one sector may be offset by growth in other sectors.

LODGING MARKET ANALYSIS

Fairbanks Lodging Market Overview

The Fairbanks hotel market is unique in several ways; firstly, there is no distinct core or central concentration of hotel properties. Instead, the lodging product is more widely diffused throughout the market. Locationally, several properties are found in, or near, the downtown core, several more are located along the Chena River, near the airport, and the remainder are distributed between these two areas. The latest round of new hotel properties to enter the market will be located in a rapidly developing retail area in the northeast part of the city, near the intersection of the Steese and Johansen Expressways, adding further to the diffuse nature of the local lodging market. However, because the distance between these areas is relatively short, most travelers seeking accommodations in Fairbanks typically base their decision on factors other than geographic location within the city. The lodging market in Fairbanks also has no distinct quality center. In many markets, the larger first-class facilities tend to be concentrated together, often in a downtown core. In Fairbanks, the upscale properties are equally represented in both the downtown and airport areas.

Lodging demand patterns in the Fairbanks market are influenced very heavily by cruise patterns, and independent leisure and packaged tour products that have Denali National Park at their core. This demand is remains heavily concentrated during peak summer season from mid-May through mid-September. During this period, a substantially larger inventory of guestrooms can be sustained in Fairbanks than at most other times during the year. As a result, there are a comparatively large number of guestrooms in the market that are operated seasonally, or change from extended-stay or apartment-type use during the shoulder and off-peak periods, to more traditional transient use during peak season periods. Some properties, such as Wedgewood Resort, Bridgewater Hotel, and Bear Lodge, routinely maintain pure hotel operations on a peak season basis, while others vary the available inventory of guestrooms by season.

The inventory of seasonally operated hotels has changed during each of our prior reviews of the Fairbanks lodging markets and this year is no exception. The Captain Bartlett Inn is currently operating only 30 of its 197 total guestrooms during off-peak periods, down from 60 off-peak rooms in prior years. The former Best Western Fairbanks Inn closed for renovations and re-branding at the end of 2007 and is slated to begin operating its 102 available rooms during peak season only starting in 2008. Conversely, during its first year of operations, the new Alpine Lodge, near the airport, had planned to keep its top floor of guestrooms on hold-warm status during the off-peak season, but pleasantly found adequate demand in the market to keep these rooms open year-round. Changes in the seasonal availability of guestroom inventory in the market in any given year may be prompted by such factors as changing economic conditions, changes in ownership, or a property’s changing competitive position in the market. The ebb and flow patterns of guestroom inventory continue to be beneficial to the market in that they serve as a pressure-relief valve for volatile swings in demand; but they also make market performance comparisons between years more difficult and inherently imprecise.

Similar to our prior analysis of the market, we categorize the competitive lodging market in Fairbanks into two primary tiers of quality, upscale and mid-scale. Properties have been classified based on physical attributes, service quality, room pricing, and performance. However, there has been a shift in the properties included in our analysis this year and going forward during our projection period as a result of changes from year-round to seasonal operations for several of the hotels. Specifically, we have removed the Captain Bartlett Inn and the River's Edge Resort from the historical data trends due to their predominantly seasonal operations, at present. We include the formerly Best Western Fairbanks Inn within the historical data trends, although it is removed from our projections beginning in 2008 due to the planned seasonal operations of this facility. Our analysis also excludes many of the smaller, older, or independent hotels in the market.

The upscale lodging market in Fairbanks consists of four hotels at the present time, including the Westmark and the Springhill Suites downtown, and the Princess Riverside Lodge and Pike's Waterfront Lodge, both located along the Chena River, near the airport. These hotels range in size from 140 to 400 rooms; and collectively, they represent a peak season inventory of 1,073 available guestrooms. The upscale hotels are each full-service facilities, offering at least one restaurant and lounge, and meeting and banquet space ranging from less than 900 square feet to nearly 17,000 square feet. The available room supply in the upscale lodging market has been static at its current level since 2005, following the May 2004 opening of Westmark's new tower, which brought their total inventory up to 400 available rooms. Pike's Waterfront Lodge also opened 28 cabins in June 2004, clustered along a section of riverfront adjacent to the existing hotel.

The mid-scale lodging market in Fairbanks currently consists of six hotels, including three independents and three with national franchises. These hotels range in size from 74 rooms to 148 rooms representing a 2007 peak season inventory of 664 available rooms. The size, type, and quality of facilities offered in the mid-scale market are considerably more diverse than in the upscale market. The three oldest properties in this submarket are full-service properties, offering food and beverage facilities and 1,900 to 2,400 square feet of meeting and conference space. The Comfort Inn and Extended Stay Deluxe, were opened in 1996 and 2001, respectively. These properties are limited-service hotels without food and beverage or significant meeting space. The Extended Stay Deluxe is the former Aspen Hotel which was sold to Blackstone in 2006. Following the acquisition, the buyer renovated the property and added kitchens to the guestrooms, converting it to the Extended Stay Deluxe brand. The newest hotel in this submarket is the Alpine Lodge, which opened in April 2007 with 115 guestrooms. The Alpine Lodge is currently under construction on a 7,000 square foot lodge building that will house a new restaurant and 2,800 square feet of meeting space, which is scheduled to open in May 2008. Reportedly, the Alpine Lodge also has additional land that could accommodate a future guestroom expansion when the market warrants.

The following table identifies those properties in each of the two primary tiers, including key physical attributes and the current seasonal published pricing of guestrooms.

Table 2 Profile of the Competitive Hotel Properties Fairbanks, Alaska										
					Meeting Space		2008		
		Date			Total	Largest	Rack Single/Double		
Mid-Scale Submarket	**Submarket**	**Opened**	**Rooms**	**F&B**	**Area (SF)**	**Room (SF)**	**Summer**	**Winter**	**Amenities**
Alpine Lodge	Airport	2007	115	0/0	4,305	3,000*	$189-$219	$79-$109	BCDEF
Extended Stay Deluxe	Airport	2001	97	0/0	1,200	1,200	$170-$189	$80	ABCE
Best Western Fairbanks Inn	Downtown	1970	102	1/1	2,400	1,400	$134-$179	n/a	CE
Comfort Inn	Downtown	1996	74	0/0	500	500	$162 - $189	$72-$80	ABCE
Regency Fairbanks	Downtown	1985	128	1/1	2,200	1,175	$195-$246	$75-$102	CDE
Sophie's Station	Airport	1986	148	1/1	1,925	1,225	$185-$245	$89-$99	CE
Subtotal			664		12,530				
Upscale Submarket									
Westmark Fairbanks Hotel	Downtown	1984-2004	400	2/1	16,700	5,400	$185 - $234	$89 - $109	CDEF
Princess Riverside Lodge	Airport	1993-2001	325	2/1	9,450	4,800	$199-$219	$89 - $139	BCDEF
Pike's Waterfront Lodge	Airport	2000-2004	208	1/1	6,330	2,800	$234-$250	$89-$159	BCDEF
Springhill Suites	Downtown	2001	140	1/1	860	500	$229	$89 - $104	ABCDEF
Subtotal			1,073		33,340				
TOTAL COMPETITIVE MARKET			**1,737**		**45,870**				

Amenities			
A	Pool	D	Bus. Ctr.
B	Spa/Steam	E	Gst Ldry.
C	Exercise	F	Retail

** Meeting space to open 2008*

Source: K&M interviews, AAA-2008, individual websites

Historical Supply and Demand

Table 3, presented on the page 10, summarizes information regarding the historical operating performance of the competitive hotels in the mid-scale and upscale markets in Fairbanks for the period 2003 through 2007. Key indications from this summary are as follows:

- The growth in the available room supply in the overall market shows a net gain of 451 available rooms on an annualized basis over the 2003 to 2007 period, indicating a compound average annual growth of 8.1 percent. The upscale submarket accounted for 271 new rooms, reflecting the addition of the Westmark tower in May 2004 and the 28 new cabins at Pikes Lodge one month later. The mid-scale submarket accounted for 180 new rooms (annualized) during the period, including 102 rooms at the Best Western Fairbanks Inn which re-opened for year-round operations in May 2004 and the opening of the 115-room Alpine Lodge in late April 2007.

- Based on historical data and our recent interviews in the market, we estimate that rooms demand in the overall market grew at 12.3 percent annually over the 2003 through 2007 period. Within the mid-scale submarket demand growth was approximately 13.6 percent annually, compared to 11.5 percent annually in the upscale submarket. Given the highly seasonal nature of demand patterns in the Fairbanks market, demand growth rates in both submarkets are heavily influenced by increases in the available rooms supply during peak summer periods when the better quality hotels in the market typically operate at or near capacity. Growth in recent years was also enhanced by the fact that supply changes in the upscale submarket were readily absorbed by the major tour operators in the market, which is considerably less likely to occur at the newer limited-service properties in the mid-scale submarket.

- The resulting occupancy rates in the overall market showed significant increases in recent years, climbing from 56 percent in 2003 to 59 percent in 2004 as a result of opportune timing of new supply additions. Occupancies fell in 2005 to 56 percent as absorption of the new rooms continued. Generally speaking, during the 2003 through 2005 period fluctuations in occupancy rates were influenced by the timing of new supply and rotational shifts in off-peak convention activity, namely AFN. Market occupancies were pushed upward in 2006 and again in 2007 due to an unforeseen influx of a large component of military demand which caused the market occupancy rate to swell to 60 percent in 2006 and 65 percent in 2007.

- Based on our interviews with officials at Fort Wainwright, we estimate that roundly 51,000 room nights of military demand was contracted in the Fairbanks market during the 2006/2007 period. We estimate that approximately 29,000 room nights of this demand were accommodated within the hotels in the competitive market, with the balance occurring at properties outside of the competitive market as defined. Approximately 70 percent of the demand within the competitive market was captured by hotels in the mid-scale submarket with the remaining 30 percent captured by the upscale market hotels. The resulting compression in the market benefited all hotels during this period, regardless of whether they were the direct recipients of military demand.

- The large infusion of military demand was an anomaly resulting from atypical troop rotation patterns and is not expected to recur in future years. As a result, this demand will be extracted from the market within our projections of future year performance. If we exclude the influence of military demand from 2006 and 2007, occupancies for the overall market would have been approximately 59 percent in 2006 and 62 percent in 2007, thereby yielding a somewhat lower average growth rate for the overall market during the period of roundly 10.2 percent annually.

- The ‘flight to quality’ mentioned in our prior studies of the Fairbanks market, has continued in recent years, with the newer properties and the nationally branded hotels generally out-performing the older independent properties. The larger tour-operated hotels, Westmark and Princess continue to do extremely well during summer period as they control a large share of the demand flowing to the market, but they continue to battle amongst each other for meetings and group events to fill their large inventory of guestrooms during off-peak periods.

Table 3
Competitive Lodging Market Overview - 2003 through 2007
Fairbanks, Alaska

	Available Rooms Daily	Annually	**Fair Share**	**Occ. Rate**	**Occupied Rm. Nights**	**Market Share**	**Penetr'n Rate**	**Average Rm. Rate**	**Room Revenue** Total	Per Rm.	**REVPAR Index**
2007											
Mid-Scale Submarket	627	228,905	37.3%	66%	152,200	38.0%	101.6%	$102.00	$15,573,942	$68.00	91.9%
Upscale Submarket	1,052	384,001	62.7%	65%	248,800	62.0%	99.0%	$121.00	$30,019,160	$78.00	105.4%
Total Market	1,679	612,906	100.0%	**65%**	401,000	100.0%	100.0%	$114.00	$45,593,102	$74.00	100.0%
% chg.		4.9%			14.3%				16.5%	10.4%	
2006											
Mid-Scale Submarket	549	200,385	34.3%	63%	126,800	36.1%	105.4%	$95.00	$12,005,116	$60.00	89.6%
Upscale Submarket	1,052	384,001	65.7%	58%	224,100	63.9%	97.2%	$121.00	$27,135,531	$71.00	106.0%
Total Market	1,601	584,386	100.0%	**60%**	350,900	100.0%	100.0%	$112.00	$39,140,647	$67.00	100.0%
% chg.		0.0%			6.4%				9.0%	9.8%	
2005											
Mid-Scale Submarket	549	200,385	34.3%	61%	121,900	37.0%	107.8%	$88.00	$10,712,099	$53.00	86.9%
Upscale Submarket	1,052	384,001	65.7%	54%	207,900	63.0%	95.9%	$121.00	$25,186,409	$66.00	108.2%
Total Market	1,601	584,386	100.0%	**56%**	329,800	100.0%	100.0%	$109.00	$35,898,507	$61.00	100.0%
% chg.		10.3%			6.2%				7.2%	-3.2%	
2004											
Mid-Scale Submarket	515	188,145	35.5%	58%	110,000	35.4%	99.8%	$83.00	$9,183,080	$49.00	77.8%
Upscale Submarket	937	341,897	64.5%	59%	200,500	64.6%	100.1%	$121.00	$24,307,817	$71.00	112.7%
Total Market	1,452	530,042	100.0%	**59%**	310,500	100.0%	100.0%	$108.00	$33,490,897	$63.00	100.0%
% chg.		18.3%			23.0%				29.2%	8.6%	
2003											
Mid-Scale Submarket	447	163,155	36.4%	56%	91,300	36.2%	99.4%	$86.00	$7,873,354	$48.00	82.8%
Upscale Submarket	781	285,065	63.6%	57%	161,100	63.8%	100.4%	$112.00	$18,045,845	$63.00	108.6%
Total Market	1,228	448,220	100.0%	**56%**	252,400	100.0%	100.0%	$103.00	$25,919,199	$58.00	100.0%
% chg.											
Compound Average Annual Growth Rate 2003 - 2007											
Mid-Scale Submarket		8.8%			13.6%			4.4%		9.1%	
Upscale Submarket		7.7%			11.5%			2.0%		5.5%	
Total Market		8.1%			12.3%			2.6%		6.3%	

Source: Kennedy & Mohn, P.S.

- Average room rates within the overall market increased from roundly $103 to $114 during the 2003 to 2007 period, posting a 2.6 percent average annual growth rate, comparable to the underlying rate of inflation. The mid-scale submarket achieved stronger growth in average room rate during the period, 4.4 percent compared to 2.0 percent in the upscale submarket. We attribute the disparity in growth to a variety of factors including the disproportionate capture of military demand between submarkets, the mid-year opening of the Alpine Lodge in 2007, and the re-branding and repositioning of the former Aspen Hotel during 2006 and 2007. We expect some softening in the growth in average room rates within the overall market in 2008 and beyond, with potentially greater impact on the existing properties in the mid-scale submarket as the newer nationally branded hotels enter the market in 2009 and 2010.

- The overall market achieved growth in revenue per available room (RevPAR) during the 2003 to 2007 of 6.3 percent annually, increasing from roundly $58 to $74. Stronger growth was posted by the mid-scale submarket at 9.1 percent annually compared to the upscale submarket at 5.5 percent annually. The disparity in growth rates between submarkets is attributed to those factors noted previously in our discussion of occupancy and average room rates.

Cruise/Tour Market Factors

The Fairbanks market remains heavily reliant on cruise/tour demand generated by the large cruise lines and traditional motor-coach operators. Denali National Park remains the emotional heart of Alaska's tourism industry and is a dominant component of most land tour packages, regardless of the provider. Because most Denali packages include a start, stop, or turn in Fairbanks, the Fairbanks market is inextricably linked to Denali.

The dominant players in the state's cruise/tour market are Princess, Holland America, and Royal Celebrity. Both Princess and Holland America have a significant presence in the Fairbanks and Denali hotel markets, whereas Royal Celebrity typical contracts for rooms at CIRI properties or through other providers. Princess has repeatedly expanded their two wilderness lodges in Denali in recent years, from a combined rooms inventory in 2004 of 774 rooms to 1,116 rooms in 2008, an increase of 44 percent. Similarly, Holland America completed the 135-room first phase of a potentially 540-room lodge in Denali in 2006. While there are presently no active plans for the second phase expansion of this project, this could change at any time. Several years ago CIRI announced their intention to build approximately 200 new rooms in Denali and while this project has not moved forward yet, it also remains active. CIRI is also planning a 50-room expansion (scaled down from 100 rooms previously) to their Talkeetna Lodge property.

Unlike Anchorage, cruise/tour demand in Fairbanks continues to remain stable and has not been adversely impacted by the significant supply changes occurring in Denali. Fairbanks' geographic proximity to Denali and its position as a turn-around point in most itineraries continues to provide a modicum of stability within a potentially transient base of demand. Our recent interviews have produced mixed reviews from tour operators, with several indicating a moderate slowing of demand patterns for 2008, while others indicate that 2008 will be flat to slightly up from 2007 numbers. Macro economic factors including the softening economy in the lower-48 and perpetually increasing fuel costs could exert downward pressure on demand in this sector of the market.

Seasonal Factors

With the exception of aberrant factors in the market in 2006 and 2007, lodging demand patterns in Fairbanks are highly seasonal, with peak season occurring from mid-May through mid-September, when cruise/tour related demand is at its peak. Peak season demand is predominantly leisure related and is heavily influenced by the major cruise lines and smaller tour operators, with much of their demand concentrated in the larger, upscale hotels in the market, and to a lesser extent, the seasonally operated properties. Many of the properties in the mid-scale submarket cater more heavily to the smaller tour operators and independent leisure travelers, and they receive little direct contribution from the major cruise/tour companies. Off-season periods occur during the balance of the year, when leisure travel is minimal and the market relies more heavily on demand from the commercial and group segments. An increasingly significant amount of off-peak leisure demand is also attracted to Fairbanks during the height of the winter when the Northern Lights are readily visible in the surrounding area. Much of this demand is drawn from international markets in Asia and reportedly this component of demand has expanded rapidly in recent years, from three chartered 747 flights in 2004 to 18 chartered flights in 2007. Similar to the cruise/tour demand segment, this demand tends to be concentrated within the larger, full-service properties in the market.

Given the significant seasonal swings in demand, hotels in the market have historically used a two-tiered seasonal rate structure, with off-peak advertised rates 50 percent or more below the peak season rates. The combined effect of seasonal changes in room rates and demand patterns in recent years are visible in the historical trends in hotel room tax receipts reported by the City of Fairbanks and the Fairbanks North Star Borough, as shown in Table 4.

Table 4
Fairbanks Hotel Motel Tax Receipts - 2003 - 2007

		1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Total	% Chg.
2003	City	203,470	468,777	937,433	196,002	1,805,682	-1.7%
	Borough	135,649	482,181	502,425	293,620	1,413,875	11.0%
	Total	339,119	950,958	1,439,858	489,622	3,219,557	3.5%
2004	City	202,259	658,129	1,046,797	235,573	2,142,759	18.7%
	Borough	138,415	558,093	596,293	260,600	1,553,401	9.9%
	Total	340,674	1,216,222	1,643,090	496,173	3,696,160	14.8%
2005	City	216,742	695,601	1,214,552	249,200	2,376,095	10.9%
	Borough	128,040	541,317	591,122	260,489	1,520,968	-2.1%
	Total	344,782	1,236,918	1,805,674	509,689	3,897,063	5.4%
2006	City	221,137	833,824	1,283,391	268,277	2,606,629	9.7%
	Borough	128,203	573,083	623,908	258,846	1,584,040	4.1%
	Total	349,340	1,406,907	1,907,299	527,123	4,190,669	7.5%
2007	City	258,787	857,719	1,305,931	262,981	2,685,417	3.0%
	Borough	158,703	315,042	1,021,234	308,701	1,803,680	13.9%
	Total	417,490	1,172,761	2,327,165	571,682	4,489,097	7.1%
Total Market							
% of Annual (2007)		9%	26%	52%	13%	100.0%	
CAAGR 2005-2007		10.0%	-2.6%	13.5%	5.9%	7.3%	
CAAGR 2003-2007		5.3%	5.4%	12.8%	3.9%	8.7%	

Source: Fairbanks Convention & Visitors Bureau - Hotel Bed Tax Receipts

Segmentation

We classified market demand into four general categories: commercial, leisure, group, and contracts. Segmentation data is routinely tracked by hotel operators, although the level of detail and accuracy of the data varies widely between properties. In recent years it has become more and more difficult for hotel operators to maintain accurate segmentation data due to the increased use of Internet booking engines and promotions. While these choices can be attractive to the guest, they hinder the hotel's ability to accurately track guest segmentation patterns. The following segmentation data reflects operator perceptions for 2007, excluding the influence of atypical military impacts in recent years.

- ♦ Commercial demand is composed of independent business travelers and state and federal government workers. Demand in the commercial segment is reasonably stable throughout the year, with modest declines during summer and holiday periods. Based on our recent interviews, we estimate this demand represents approximately 27 percent of total annual demand in the overall market in 2007.

- ♦ Leisure demand consists of independent and packaged leisure travelers, many of which come to Fairbanks while en-route to Denali. The packaged leisure component of this demand segment is heavily cruise-oriented and is concentrated almost exclusively within the peak summer season. We estimate the leisure demand segment to represent approximately 51 percent of total annual demand in the market.

- ♦ Group demand consists of conventions and meeting related travel to Fairbanks, and demand generated by sports teams and school events. Demand in this segment is typically concentrated during shoulder periods in the spring and fall. Current interviews suggest that group demand represents approximately 16 percent of total demand in the market.

- ♦ Contract demand is provided primarily by airlines and railroads serving Fairbanks. This demand makes up approximately six percent of total demand in the market and remains fairly heavily concentrated in the upscale submarket.

SUPPLY AND DEMAND PROJECTIONS

In evaluating the performance potential of the Fairbanks lodging market in future years we have considered historical and projected changes in the competitive rooms supply and anticipated changes in market demand volumes and patterns over the near to mid term. Our analysis incorporates the addition of new hotels that are expected to open in the market over the next several years. Projections of future demand growth reflect contributions from three fundamental sources: unsatisfied demand, induced demand, and underlying growth in demand. A detailed discussion of our analysis is presented in the following paragraphs.

Supply Changes

The table below identifies recent and proposed changes to the inventory of available guestrooms within the competitive market. Based on our research and interviews in the local market, we are aware of two new hotels and one recently opened hotel, all of which have been classified within the mid-scale submarket. Two of these new hotels will open in the rapidly developing retail area in northeast Fairbanks, near the intersection of the Steese and Johansen Expressways. At present, there are no hotels located in this area of Fairbanks. While somewhat pioneering in terms of location, both of these hotels will benefit from their affiliation with primary national brands with strong reservation systems and guest loyalty programs; each of these attributes is generally lacking in the Fairbanks market. While these hotels are not expected to benefit directly from the primary sources of cruise/tour demand in the market, they are expected to be extremely formidable competitors for motor-coach and independent leisure travelers, corporate/government travelers, and sports teams. Furthermore, the proximity of these hotels to the primary retail outlets in Fairbanks is also expected to enhance their performance as Fairbanks is increasingly able to satisfy bush-provisioning needs for much of Alaska's interior, a function that had previously been served by Anchorage.

Recent and Pending Room Supply Changes - Fairbanks

Property	Quality	Type	Location	# Rooms	Opening
Recent Changes					
Alpine Inn	Mid-scale	Transient	Airport	115	Apr-07
Pending Room Changes					
Holiday Inn Express	Mid-scale	Transient	Northeast	115	Jun-08
Hampton Inn	Mid-scale	Transient	Northeast	101	Jun-09

Source K&M - March 2008

Demand Changes

Within our analysis, projections of growth in demand reflect the combination of three individual components including unsatisfied demand, underlying growth, and induced demand.

- Unsatisfied demand is that component of new demand that can be accommodated in the market as new hotel rooms open, thereby providing additional capacity during peak periods.

- ♦ Underlying growth is projected based on the strength of local and regional economic indicators such as growth in population, employment, growth in room tax collections, and growth in air travel.

- ♦ Induced demand reflects changes in the market that are induced by forces external to the market. Induced demand can be either positive or negative, with the opening of a new demand generator providing a positive inducement of demand, while the opening of competing hotels outside the competitive market, which draw off demand, would result in negative induced demand.

In arriving at our estimates of future demand growth, consideration was given to mix of demand by segment, seasonal patterns of demand, and the seasonal capacity constraints within the market. Key factors in our analysis are summarized in the following paragraphs.

- ♦ We estimate underlying growth in demand based on historical changes in key economic indicators, as presented previously in Table 1, tempered with anticipated changes over the near term. The economic data provides support for growth rates generally in the range of two to four percent annually, based growth in employment, population, air passenger volumes, and room taxes. These growth rates are applied uniformly to both the mid-scale and upscale submarkets.

    - ▪ Our projections of underlying growth in demand include growth in the commercial segment of 2.0 percent annually throughout the projection period. Growth in the commercial segment is based on employment growth, declining construction activity over the mid-term, and modest contribution from anticipation and optimism surrounding a possible gas pipeline in future years.

    - ▪ Within the group demand segment, growth is projected at 1.0 percent annually throughout the projection period. This level of growth is exclusive of continuation of AFN rotations that are presumed to occur in future years.

    - ▪ Leisure demand is projected to grow at 0.0 percent annually during the early years of the projection period, gradually increasing to 2.0 percent annually by the end of our projection period. This estimate reflects anticipated flattening of demand patterns in this segment during the early years of the projection period as indicated by tour operators.

    - ▪ Within the contract demand segment growth is projected at 0.0 percent annually throughout the projection period, reflecting no significant changes in the key support industries within this segment.

- Unsatisfied demand is projected based on 75 fill nights annually at a 75 percent occupancy rate for the two new nationally-branded hotels projected to enter the market. This demand is allocated equally to the commercial and leisure demand segments.

- Our estimates of induced demand reflect a negative inducement of roundly 23,000 room nights of military demand from the commercial/government demand segment in 2008. AFN demand is reflected based on an assumed six fill nights during each alternating future year. A corresponding level of demand is extracted during even numbered years when AFN is presumed to be held in Anchorage. This adjustment is applied uniformly to the mid-scale and upscale submarkets. Total AFN influence is estimated at roundly 10,000 occupied room nights in 2007. Our projections also include approximately 5,000 room nights of negative induced demand, allocated equally between 2009 and 2010 that is expected to be drawn away from the Fairbanks market by the projected opening of the new convention center in Anchorage. Lastly, our estimates include roundly 5,500 room nights annually in 2009 and 2010 that are expected to shift from the upscale segment to the mid-scale segment as a result of the new nationally branded hotels opening in the mid-scale segment during future years.

Table 5, presented on the following page, sets forth our projections of growth in demand throughout the forecast period.

Table 5
Projected Demand Growth by Segment

	2008	2009	2010	2011	2012	
Mid-Scale Market						**Mix**
Commercial Demand	42,200	49,100	54,000	55,100	56,200	34%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	1,700	3,300	1,200	0	0	
Induced Demand	(16,000)	2,750	2,750	0	0	
Group Demand	15,400	20,000	15,800	20,700	16,200	10%
Underlying Growth	1.0%	1.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	(3,750)	4,400	(4,400)	4,700	(4,700)	
Leisure Demand	71,700	77,800	82,500	83,700	85,400	51%
Underlying Growth	0.0%	0.0%	1.0%	1.5%	2.0%	
Unsatisfied Demand	1,700	3,300	1,200	0	0	
Induced Demand	0	2,750	2,750	0	0	
Contract Demand	7,800	7,800	7,800	7,800	7,800	5%
Underlying Growth	0.0%	0.0%	0.0%	0.0%	0.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	137,000	155,000	160,000	167,000	166,000	100%
Upscale Market						**Mix**
Commercial Demand	46,800	45,000	43,200	44,100	45,000	19%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	(6,800)	(2,750)	(2,750)	0	0	
Group Demand	39,200	43,400	35,000	41,700	35,800	15%
Underlying Growth	1.0%	1.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	(6,300)	3,800	(8,800)	6,300	(6,300)	
Leisure Demand	135,000	132,300	130,900	132,900	135,600	58%
Underlying Growth	0.0%	0.0%	1.0%	1.5%	2.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	(2,750)	(2,750)	0	0	
Contract Demand	16,200	16,200	16,200	16,200	16,200	7%
Underlying Growth	0.0%	0.0%	0.0%	0.0%	0.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	237,000	237,000	225,000	235,000	233,000	100%
Overall Market						
Commercial Demand	24%	24%	25%	25%	25%	
Group Demand	15%	16%	13%	16%	13%	
Leisure Demand	55%	54%	55%	54%	56%	
Contract Demand	6%	6%	6%	6%	6%	
Total Demand	100%	100%	100%	100%	100%	

Table 6, presented on the following page, incorporates our individual projections of demand growth by segment and submarket into a single presentation of historical and projected changes in supply and demand within the Fairbanks market. Collectively, our estimates of unsatisfied, induced, and underlying demand growth indicate a 1.6 percent average annual increase in demand for the overall market from 2008 through 2012. This rate of demand growth is substantially below the historical rates of demand growth achieved by the market in recent years, although this was a period marked by considerable changes in supply and other anomalies in demand that are not expected to be repeated in future years. Overall, we consider our projection to be reasonable given the highly unique dynamics of the Fairbanks market.

Based on this analysis, our projections of future market conditions in the mid-scale submarket indicate that occupancy rates will decline substantially in 2008 to 60 percent as a result of the lack of military demand, the continued stabilization of the Alpine Lodge, and the opening of the Holiday Inn Express. Further declines are projected in 2009 and 2010, with occupancies falling to a low of 56 percent in 2010 as the mid-scale sub-market grapples with the third new hotel opening in as many years. Occupancies are projected to gradually rebuild in later years as the new assets begin to stabilize, reaching 58 percent in 2012, a presumed non-AFN year. Similarly, our projection of future market conditions in the upscale submarket indicate occupancy rates are expected to decline roundly three percentage points in 2008 to 62 percent. Continued slippage in occupancies is projected in subsequent years, falling to a low of 59 percent in 2010 as the newer mid-market hotels gradually siphon off demand from the upscale submarket. Gradual rebuilding is projected in later years with the upscale submarket reaching 61 percent occupancy by the end of our projection period.

Table 6
Historical and Projected Market Conditions

Historical Market Conditions						Projected Market Conditions				
2003	**2004**	**2005**	**2006**	**2007**		**2008**	**2009**	**2010**	**2011**	**2012**
					Mid-Scale Market					
447	515	549	549	627	Existing Product	562	562	562	562	562
					Holiday Inn Express	60	115	115	115	115
					Hampton Inn	0	59	101	101	101
447	515	549	549	627	Average Daily Rooms	622	736	778	778	778
163,155	188,145	200,385	200,385	228,905	Annual Room Nights	226,865	268,719	284,049	284,049	284,049
	15.3%	6.5%	0.0%	14.2%	Percentage Change	-0.9%	18.4%	5.7%	0.0%	0.0%
91,300	110,000	121,900	126,800	152,200	Market Demand	137,000	155,000	160,000	167,000	166,000
	CAAGR	Supply		8.8%		**CAAGR**		Supply chg.	5.8%	
	CAAGR	Demand		13.6%		**CAAGR**		Demand chg.	4.9%	
3,141	18,700	11,900	4,900	25,400	Change from prior year	(15,200)	18,000	5,000	7,000	(1,000)
	20.5%	10.8%	4.0%	20.0%	Percentage Change					
0	3,900	1,900	0	4,400	Unsatisfied Demand	3,400	6,500	2,400	0	0
0	0	0	4,600	16,000	Induced Demand	(19,750)	9,900	1,100	4,700	(4,700)
3,141	14,800	10,000	300	5,000	Underlying Growth	1,150	1,600	1,500	2,300	3,700
	16%	9%	0%	4%	Underlying Growth Rate	0.8%	1.2%	1.0%	1.4%	2.2%
56%	58%	61%	63%	66%	Occupancy	60%	58%	56%	59%	58%
					Upscale Market					
781	937	1,052	1,052	1,052	Existing Product	1,052	1,052	1,052	1,052	1,052
					Proposed hotels	0	0	0	0	0
781	937	1,052	1,052	1,052	Average Daily Rooms	1,052	1,052	1,052	1,052	1,052
285,065	341,897	384,001	384,001	384,001	Annual Room Nights	384,001	384,001	384,001	384,001	384,001
	19.9%	12.3%	0.0%	0.0%	Percentage Change	0.0%	0.0%	0.0%	0.0%	0.0%
161,100	200,500	207,900	224,100	248,800	Market Demand	237,000	237,000	225,000	235,000	233,000
	CAAGR	Supply chg.		7.7%		**CAAGR**		Supply chg.	0.0%	
	CAAGR	Demand chg.		11.5%		**CAAGR**		Demand chg.	-0.4%	
(4,452)	39,400	7,400	16,200	24,700	Change from prior year	(11,800)	0	(12,000)	10,000	(2,000)
	24.5%	3.7%	7.8%	11.0%	Percentage Change					
0	14,800	6,500	0	0	Unsatisfied demand	0	0	0	0	0
0	0	0	2,000	6,800	Induced Demand	(13,100)	(1,700)	(14,300)	6,300	(6,300)
(4,452)	24,600	900	14,200	17,900	Underlying Growth	1,300	1,700	2,300	3,700	4,300
	15%	0%	7%	8%	Underlying Growth Rate	0.5%	0.7%	1.0%	1.6%	1.8%
57%	59%	54%	58%	65%	Occupancy	62%	62%	59%	61%	61%
					Overall Market					
1,228	1,452	1,601	1,601	1,679	Average Daily Rooms	1,674	1,788	1,830	1,830	1,830
448,220	530,042	584,386	584,386	612,906	Overall Market Supply	610,866	652,720	668,050	668,050	668,050
	18%	10%	0%	5%	Supply Growth	0%	7%	2%	0%	0%
252,400	310,500	329,800	350,900	401,000	Overall Market Demand	374,000	392,000	385,000	402,000	399,000
	23%	6%	6%	14%	Demand Growth	-7%	5%	-2%	4%	-1%
	CAAGR	Supply chg.		8.1%		**CAAGR**		Supply chg.	2.3%	
	CAAGR	Demand chg.		12.3%		**CAAGR**		Demand chg.	1.6%	
56%	59%	56%	60%	65%	Occupancy	61%	60%	58%	60%	60%

Average Room Rates

In analyzing the Fairbanks lodging market, we acknowledge the qualitative and competitive differences between properties in the upscale and mid-scale markets. However, we also acknowledge that seasonal variations in demand patterns create major changes in rooms pricing within the market, which tends to blur the traditional lines of competition among properties during off-season periods. As a result, while the upscale properties command a moderate premium in room rates during the peak season, there is little difference in room rates between the upscale and mid-scale properties during shoulder or off-peak periods. Furthermore, because the larger, tour-oriented properties in the market focus almost exclusively on packaged leisure demand during peak season, they can often alienate demand in other segments. During shoulder and off-peak periods, the larger hotels position themselves to recapture this demand by offering more aggressive pricing discounts. Given the generally superior quality of their facilities, this tactic results in an un-level competitive playing field where the lesser quality properties are at a distinct disadvantage. As long as the better quality hotels in the market continue to aggressively discount during off-peak periods, rate growth in the market will remain stifled and the more modest quality properties will be largely ineffective competitors during these periods. While we anticipate that the newer hotels with their stronger brand recognition and loyalty programs will be impacted somewhat less by this practice, the rate-ceiling in the market is likely to continue to be established by the Westmark and Princess hotels.

The only thing certain about average room rates is that they are constantly in a state of flux. The direction of change and the relative significance of that change depend on a myriad of forces operating within the market and the response to these forces by the individual operators. During the 2003 to 2007 period, average room rates essentially grew at inflationary levels in the Fairbanks market. The mid-scale submarket posted stronger growth during this period than did the upscale market, although this growth was clouded by the opening a new hotel and the renovation and repositioning of another. In contrast, rate growth in the upscale submarket was less influenced by material changes to product quality or timing of new inventory. Overall, we anticipate a continuation of this trend in future years, with the mid-scale submarket achieving stronger growth than the upscale submarket due to the opening of two new, nationally branded, hotels.

To derive a five-year projection of growth in average room rate, we considered the dual impacts of inflation and anticipated market conditions. We have incorporated an underlying inflation rate of 2.5 percent annually throughout the projection period. Market condition adjustments are based on our estimates of how the market will respond to a variety of factors including, the softening economy, flattening of growth in the cruise and tour industries, and the new rooms entering the Fairbanks market in future years. We project growth in average room rates within the overall market at roundly 2.3 percent annually over the projection period, reflecting a modest slowing of growth from recent years. We project the mid-scale submarket will achieve rate growth averaging 3.1 percent annually during the projection period, compared to 2.2 percent annually in the upscale submarket. Our projections of growth in average room rate for each submarket are shown in the following table. The resulting average room rate for the overall market is the weighted average reflecting demand patterns and rates within the two submarkets.

Table 7 Projected Average Room Rate And Revenue Per Available Room						
Year/Market	Inflation	Market Response	Total Change	Projected ARR	Projected Occup. %	Projected REVPAR
2007						
Midscale Submarket				$102.00	66%	$67.82
Upscale Submarket				$121.00	65%	$78.40
Overall Market				$114.00	65%	$74.59
2008						
Midscale Submarket	2.50%	1.00%	3.50%	$106.00	60%	$64.01
Upscale Submarket	2.50%	-0.50%	2.00%	$123.00	62%	$75.91
Overall Market				$117.00	61%	$71.63
2009						
Midscale Submarket	2.50%	1.00%	3.50%	$110.00	58%	$63.45
Upscale Submarket	2.50%	-0.50%	2.00%	$125.00	62%	$77.15
Overall Market				$119.00	60%	$71.47
2010						
Midscale Submarket	2.50%	1.00%	3.50%	$114.00	56%	$64.21
Upscale Submarket	2.50%	-0.50%	2.00%	$128.00	59%	$75.00
Overall Market				$122.00	58%	$70.31
2011						
Midscale Submarket	2.50%	0.50%	3.00%	$117.00	59%	$68.79
Upscale Submarket	2.50%	0.00%	2.50%	$131.00	61%	$80.17
Overall Market				$125.00	60%	$75.22
2012						
Midscale Submarket	2.50%	0.00%	2.50%	$120.00	58%	$70.13
Upscale Submarket	2.50%	0.00%	2.50%	$134.00	61%	$81.31
Overall Market				$128.00	60%	$76.45

Source: Kennedy & Mohn, P.S.

CONCLUSION

Based on our current analysis, the Fairbanks lodging market has performed remarkably well in recent years due to several factors including; the improving quality of the guestroom base in the market, several strong years of growth in cruise/tour demand, the recurrence of AFN, and a significant one-time influx of military demand. However, when projecting performance of the market in future years, several of these factors are expected to absent, thereby causing a moderate softening in projected performance levels in future years. While we do not anticipate any further shifts in the guestroom inventory from year-round to seasonal operations, the continually improving quality of the year-round guestroom base in Fairbanks will likely make it impossible for any of the existing seasonal hotels to shift back to year-round operations. Barring a major announcement regarding a definite gas-pipeline project, we expect the next several years to be a period of retrenchment in the local market. The existing hotels in the market will be forced to compete with several newer assets from two of the strongest national hotel brands on the market. Ultimately, this heightened level of competition will be beneficial for the market as a whole, although it may be increasingly painful for those properties with more dated facilities or modest quality.

We trust that AIDEA will find the updated analysis and commentary presented in this report to be beneficial for developing an improved level of understanding regarding the current factors influencing the lodging market in Fairbanks. Should you have any questions or require clarification on any of the issues discussed in this report, please do not hesitate to contact us.

Sincerely,

Kennedy & Mohn P.S.

Kennedy & Mohn, P.S.

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This market overview study has been prepared under the following general assumptions:

- No responsibility is assumed for matters of a legal nature.
- Responsible ownership and competent property management are assumed.
- The information provided by others is believed to be reliable. However, no warranty is given for its accuracy.
- All engineering is assumed to be correct. The plot plans and illustrative material in this report are included only to assist the reader in visualizing the property.
- It is assumed that there are no hidden or unapparent conditions of the property, subsoil, or structures that render it more or less useful. No responsibility is assumed for such conditions or for arranging for engineering studies that may be required to discover them.
- Full compliance with all applicable federal, state, and local environmental regulations and laws is assumed.
- Full compliance with all applicable zoning and use regulations and restrictions is assumed.
- It is assumed that all required licenses, certificates of occupancy, consents, or other legislative or administrative authority from any local, state, or national government or private entity or organization have been or can be obtained.
- It is assumed that the utilization of the land and improvements is within the boundaries or property lines of the property described and that there is no encroachment or trespass.

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- Projections of future revenue, expenses, net operating income, mortgage debt service, capital outlays, cash flow, or inflation represent our judgment of the assumptions likely to be used by informed persons in the marketplace. These estimates are intended solely for analytical purposes and are not intended to accurately predict future results or events. Actual performance will differ from these projections, and these differences may be significant.

- In accordance with our contract with the client, the accompanying analysis is not intended to be a complete market analysis or appraisal. The purpose of this market overview study is for AIDEA's internal use in evaluating future hotel financing requests within the state.

- Unless otherwise stated in this report, the existence of hazardous substances, including without limitation asbestos, polychlorinated biphenyls, petroleum leakage, or agricultural chemicals, which may or may not be present on the property, or other environmental conditions, were not called to the attention of nor did the consultant become aware of such during the consultant's inspection. The consultant has no knowledge of the existence of such materials on or in the property unless otherwise stated. The consultant, however, is not qualified to test such substances or conditions. The presence of such substances, such as asbestos, urea formaldehyde foam insulation, or other hazardous substances or environmental conditions, may affect the feasibility of the project. Our analysis is predicated on the assumption that there is no such condition on or in the property or in such proximity thereto. No responsibility is assumed for any such conditions, nor for any expertise or engineering knowledge required to discover them.

CERTIFICATION

I certify that, to the best of my knowledge and belief:

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, impartial, and unbiased professional analyses, opinions, conclusions, and recommendations.
- I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest with respect to the parties involved.
- I have no bias with respect to any property that is the subject of this report or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation for completing this assignment is not contingent upon the development or reporting of a pre-determined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this report.
- The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics & Standards of Professional Appraisal Practice of the Appraisal Institute, which include the *Uniform Standards of Professional Appraisal Practice*.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- I have made a personal inspection of the property that is the subject of this report.
- No one provided significant real property appraisal or appraisal consulting assistance to the persons signing this certification.
- As of the date of this report, Michael J. Mohn, MAI has completed the continuing education program of the Appraisal Institute.

Michael J Mohn DSO

Michael J. Mohn, MAI

CCERT Ver.5/2005

Hotel Market Analysis
Juneau, Alaska
May 2008

Prepared for

AIDEA
Alaska Industrial Development and Export Authority

Kennedy & Mohn, P.S.
Seattle, Washington

INTRODUCTION

This following report represents our initial baseline study of lodging market conditions in Juneau, Alaska. This study provides an overview of key economic factors and estimated lodging market performance data through year-end 2007 and culminating in our projections of future lodging market conditions. The purpose of this study is to provide AIDEA and local market participants with an independent, third-party perspective regarding the relative strength or weakness of the Juneau lodging market and those factors that would reasonably be expected to impact the market over the near term. The data and opinions set forth in this report are based on interviews with state and local officials, hotel owners, managers, and developers, and a variety of other direct and indirect participants in the tourism industry in the state and local markets. The data and opinions set forth in this report are based on our fieldwork and follow-up research conducted through May 2008.

ECONOMIC OVERVIEW

Local Market Overview

Juneau, Alaska's capitol city, is located in the rugged mountainous region of the state's southeastern panhandle. Juneau lies approximately 900 miles northwest of Seattle and 600 miles southeast of Anchorage. Juneau is the third largest city in Alaska with a 2007 population of roundly 30,300. The terrain of the area is predominantly mountainous, with Mount Roberts and Mount Juneau bordering the city to the northeast, and Gastineau Channel bordering the city to the southwest. This topography creates a naturally imposed shortage of developable land in Juneau that provides significant barriers to entry and impacts the pace of economic growth and the price of land. Another key feature is that Juneau is accessible only by air and water, and is home to a limited road system extending from a point approximately six miles southeast of downtown and terminating approximately 40 miles to the northwest at Echo Cove. Unlike other markets in the state, Juneau's more limited accessibility impacts all sectors of the economy, some favorably and others not. This limited accessibility is also at the heart of long-standing debates regarding 'the road' and 'the capital', both of which have significant economic ramifications to the market, now and potentially in the future.

Given the unique transportation constraints of the Juneau market, key transportation-related indicators provide an initial pulse on the local economy. These indicators show comparatively healthy growth in travel patterns in Juneau in recent years. Air access to Juneau is provided by Juneau International Airport (JNU), which hosted over 594,000 passengers in 2007, demonstrating average growth in passenger volumes of 2.8 percent annually in recent years. Terminal facilities at the airport were constructed in three phases between 1948 and 1980 and while air travel volumes to Juneau have more than doubled since 1984, there have been no corresponding expansions to the airport's terminal facilities. In recent years the airport has obtained funding from federal, state, and local sources to finance a planned $20.7 million multi-phase renovation and expansion of airport passenger terminal facilities. Construction on this project is expected to start in spring 2009. The Alaska State Marine Highway System (ferry) provides year-round service to Juneau from a variety of maritime cities in Alaska and the

Northwest. Juneau is the highest volume destination within the ferry system, bringing nearly 73,000 passengers in 2007. Ferry passenger volumes have grown at an average of 2.5 percent annually in recent years. One of the strongest economic forces in Juneau is the cruise ships, which frequent this port from mid-May through early September each year. Cruise ships brought approximately 957,000 passengers to Juneau in 2007, an increase of 4.0 percent over 2006, and an average growth rate of 5.5 percent compounded annually since 2003.

Economic Indicators

As shown in Table 1 on the following page, job growth in the Juneau Borough averaged a scant 0.7 percent annually during the 2003 to 2007 period, with several years of nominal growth bracketed by modest declines at the beginning and end of the period. Unemployment rates in the market have been gradually trending down in recent years, falling from a high of 5.8 percent in 2004 to a low of 4.4 percent in 2007. State economists forecast modest employment growth in Juneau for 2008.

The single largest employment sector in Juneau is clearly the Government sector, which accounts for 40 percent of all employment in the market in 2007, representing over 7,300 jobs. Federal government jobs represent 12 percent of the total Government sector, with 58 percent provided by state government, and the remainder by local government. However, the role of government in the Juneau market extends well beyond the direct creation of jobs in the market. Government employment in Juneau has shown modest declines in recent years, averaging -1.2% annually, shedding 370 jobs over the 2003 to 2007 period.

In contrast to declines in Juneau's largest employment sector, Juneau's smallest employment sector, Mining, has shown the strongest employment growth rate in the market (10.0%), albeit representing only 154 new jobs over the period. Growth in mining employment is largely attributed to pre-startup at the Kensington Mine, a $238 million project, located north of Juneau. This project incurred a setback two years ago involving a dispute over how mine tailings were to be handled. Final resolution of the tailings dispute is nearing completion, with official opening of the mine projected for early 2009. Employment in this sector is expected to increase further upon opening of Kensington, with employment for the mine estimated at 200 initially and increasing to a peak of approximately 400. Additional stability in this sector has been provided by high minerals prices in recent years which have fueled increased exploration activity, resulting in the extended life of several mines in the state including the Greens Creek Mine near Juneau.

Respectable average annual employment growth rates were also achieved between 2003 and 2007 within the Financial Services sector (4.6%) and in the Trade, Transportation, & Utilities sector (4.1%). Employment growth was also achieved within the Manufacturing, Education & Health, and Leisure and Hospitality sectors, ranging from 1.7 percent to 2.7 percent annually. Collectively, these five employment sectors added over 850 new jobs to the market during the period.

Table 1
Juneau Borough Economic Indicator Summary

Employment:	**2003**	**2004**	**2005**	**2006**	**2007***	**CAAGR**
Total Industries	17,464	17,255	17,644	18,028	17,983	0.7%
% chg.		-1.2%	2.3%	2.2%	-0.2%	
Goods Producing						
Natl. Resource & Mining	332	332	348	457	486	10.0%
Construction	1,024	755	858	900	878	-3.8%
Manufacturing	255	263	276	292	284	2.7%
Service Providing						
Trade, Trans. & Utilities	2,871	3,027	3,153	3,266	3,370	4.1%
Information	307	286	302	301	285	-1.8%
Financial	537	553	577	627	643	4.6%
Prof. & Business	832	864	923	900	856	0.7%
Education & Health	1,531	1,629	1,653	1,727	1,641	1.7%
Leisure & Hospitality	1,523	1,493	1,545	1,504	1,638	1.8%
Government	7,692	7,492	7,408	7,470	7,322	-1.2%
Unemployment Rate:	5.7%	5.8%	5.3%	4.8%	4.4%	
Population:						
State of Alaska	647,773	647,314	664,060	670,958	676,987	1.1%
Anchorage	273,024	277,810	278,294	283,244	283,823	1.0%
Fairbanks	28,924	30,101	31,104	30,179	31,627	2.3%
Fairbanks North Star Borough	82,160	85,453	87,704	87,766	90,963	2.6%
Juneau City & Borough	31,294	31,122	31,225	30,811	30,305	-0.8%
Denali Borough	1,916	1,850	1,823	1,796	1,731	-2.5%
Juneau International Airport						
Total Air Passengers	532,616	548,551	564,549	575,637	594,101	2.8%
Incoming	266,044	274,306	282,679	286,955	297,267	2.8%
Outgoing	266,572	274,245	281,870	288,682	296,834	2.7%
Cargo (non-transit) 000#	11,627	12,495	18,023	20,181	16,604	9.3%
Lodging Tax Reciepts						
Juneau City & Borough	$897,011	$906,280	$886,240	$1,061,798	$1,184,151	7.2%
% chg.		1.0%	-2.2%	19.8%	11.5%	
Alaska State Ferry System						
Embarking Passenger Traffic	66,123	67,095	65,581	65,269	72,876	2.5%
% chg.		1.5%	-2.3%	-0.5%	11.7%	
Cruise Passenger Trends						
Alaska	777,000	884,400	953,400	958,900	1,029,800	7.3%
% chg.		13.8%	7.8%	0.6%	7.4%	
Juneau	771,857	850,703	915,000	919,893	957,000	5.5%
# Ship Calls	581	580	586	613	646	2.7%
Inflation Trends - CPI-U						
Anchorage	2.7%	2.6%	3.1%	3.2%	2.2%	
United States	1.6%	2.3%	2.7%	3.2%	2.8%	

** ALMIS Feb-07 Benchmark Data*

Sources:

Alaska Dept. of Labor; US Census, JIA, JCVB, NPS, Juneau Borough

Oil production related employment is a major driver of the state's resource-based economy, if not a dominant employer. Similarly, outside of its governmental oversight role, Juneau's role in the oil and gas industries in the state is quite limited. Nonetheless, the current record high oil prices have provided the state with massive royalties that filled state coffers in 2007, resulting in extensive state spending in the recently passed $11B operating budget, $2.9B capital budget, and $5B deposited to state savings accounts. The stratospheric rise in oil prices have resulted in a dramatically renewed interest in exploration and development activities in the oil and gas sectors, as evidenced by Shell Oil Company's continuing efforts to gain approval for exploration of coastal waters in the Beaufort Sea, just offshore from ANWR and its recent involvement in securing $2.1 billion in oil and gas leases in the Chukchi Sea off of Alaska's northwest coast in February 2008.

The biggest item on the horizon in the oil and gas industry in Alaska hinges on current legislative efforts to secure proposed construction of a proposed $30B natural gas pipeline. Trans-Canada provided the only AGIA compliant proposal for development of the pipeline, which is currently under reviewed by the Governor's office and is expected to be presented to the state legislature in the upcoming special session in mid-2008. Meanwhile, Conoco-Phillips announced that it would pursue its own version of the gas pipeline without the $500M in state subsidies offered under AGIA. In early April, BP announced it would join forces with Conoco to pursue development of the gas line, with this new venture expected to spend $600M over the next three years on engineering and fieldwork related to the project. While the outcome is still far from certain, it appears that Alaska may soon be capitalizing on a project that it has pursued for over 30 years. Given the massive cost and scale of this $30 billion project, its economic impact within the state would be substantial, although it is likely to be distributed over a protracted period of time. If this project moves forward, Anchorage would likely play a key role in the development and planning phases, whereas Fairbanks would likely benefit more heavily during the construction phase. Juneau will likely benefit only indirectly as home of many of the state's key agencies that will be involved in the planning, permitting, and monitoring of this massive project, and in determining where state proceeds will be spent. While this project now appears closer to fruition that at any time in its 30-year history, there is still no certainty that it will move forward. While our projections are not predicated on the gas line moving forward, the successful launch of this project would clearly signal the beginning of another major boom period for the economy of the state as a whole.

Between 2003 and 2007, the population in the Juneau Borough showed a -0.8 percent average annual decline, with nearly 1,000 fewer residents in 2007 than in 2003. Unlike the state as a whole and the other primary metropolitan markets in the state, Juneau has experienced a net out-migration in recent years, with more persons leaving the city than arriving. The Juneau Economic Development Corporation attributes this decline to a variety of factors including, capitol creep and concerns over potential relocation of the legislature, downward pressures on federal government jobs, and delays surrounding the Kensington Mine.

Other travel-related growth indicators in the Juneau area during the 2003 to 2007 period include growth in air passenger volumes (2.8%), growth in ferry passenger volumes (2.5%), and growth in lodging tax receipts (7.2%).

The tourism sector in the Juneau economy is predominantly linked to the cruise industry, which while it brought nearly one million visitors to Juneau in 2007, it creates only limited demand for overnight lodging. Like many other coastal towns and cities in Southeast Alaska, the cruise lines use Juneau as stopover point, offering passengers half-day to full-day shore excursions where they can stroll the downtown area and waterfront or choose from a variety of packaged day-tour alternatives before returning to the ship to disembark for the next stop. While downtown retailers and local tour operators benefit significantly from this demand, hotels in market generally see little benefit. The limited amount of overnight demand generated by the cruise lines is typically captured by the hotels in the downtown area and it results from the turning of ships by several of the smaller cruise operators and occasional crew changes by the larger operators. Juneau has embraced the cruise ship market and has seen visitor volumes grow rapidly to the point where future growth is limited by the existing capacity constraints within the market. According to the Juneau Convention and Visitors Bureau, existing cruise ship infrastructure is now operating at capacity with a maximum of five cruise ship dockings per day. While cruise passenger volumes in the market have grown at 5.5 percent annually over the 2003 to 2007 period, a more constrained level of growth is anticipated in the future.

A variety of macroeconomic factors are influencing lodging demand patterns in the current environment and are expected to continue to do so over the near term. The softening or near recessionary conditions in the larger U.S. economy, skyrocketing costs of fuel and groceries, tightening lending markets, and the recent collapse of the sub-prime mortgage markets, all translate to lower levels of discretionary income. These factors are expected to exert downward pressure on leisure travel patterns over the near to mid-term. Conversely, the low value of the dollar on the world currency markets tends to enhance domestic travel patterns while allowing the U.S. to capture a larger share of the foreign travel markets. Alaska is expected to remain a highly desirable travel destination for domestic and foreign visitors alike. Also on the positive side, unlike the rest of the nation, Alaska markets may see continued benefit from high oil, gas, and minerals pricing which enhances exploration and development activity in the state's resource-based economy, thereby resulting in upward pressure on commercial demand patterns. While the macroeconomic signals are somewhat negative, we are reasonably confident that Alaska will avoid a major downturn in its economy and that softening or declines in one sector may be offset by growth in other sectors.

Within the Juneau market, there are several large-scale issues that continue to exert pressure on the local economy and therefore warrant further discussion.

- ♦ First and foremost, Juneau has endured numerous attempts to relocate the state capitol, dating back as far as statehood, in 1959. Supporters of the capitol move say that it is important for the seat of government to be closer to the major population centers, with easier access between constituents and the legislators (read as road access), whereas opponents argue that Juneau's location is economically vital to Southeast Alaska and that access to decision-makers is improving all the time. Voters have both rejected and approved various ballot measures to move the capitol and/or the legislature, but thus far they have been largely unwilling to incur the mammoth costs for such a project. While

Juneau has managed to survive these earlier attempts, the issue clearly remains unresolved, as evidenced by the introduction of two similar bills during the 2008 legislative session.

- On a similar but related front, since 1992 Juneau has sought to mitigate its isolation and access issues and potentially improve its bid to retain the capitol by connecting its limited road system to the balance of the state. The Juneau Road Project is a $374 million proposal to construct approximately 50 miles of new highway from Juneau extending north along Lynn Canal, culminating in a high-speed ferry that would connect the last 18 miles to Skagway. While this project had the support of the Murkowski administration and partial funding, since taking office in 2006, the current governor has cancelled $31M in early spending for the project, characterizing it as premature.

While we cannot predict if, when, or how these key issues will be resolved, the magnitude of uncertainty that they bring is stifling to the local economy.

LODGING MARKET ANALYSIS

Juneau Lodging Market Overview

The Juneau lodging market includes a wide variety of accommodations including full-service hotels, mid-market to economy hotels, and Bed & Breakfast inns. The focus of our analysis is on the full-service and mid-market, limited-service hotels. Most hotels in Juneau are located either in the downtown area or in the Mendenhall Valley, near the airport, approximately eight miles north of downtown. While the larger, full-service hotels are located in the downtown area, due to their age and condition, these properties are not materially different than many of the mid-market, hotels located in the valley. Due to the location of the state capitol and the cruise ship docks in the downtown area, the downtown hotels retain a competitive advantage in attracting demand from these sources. Conversely, the properties in the Valley are better positioned to attract the more traditional commercial demand, non-legislative government demand, and independent leisure demand arriving by air or via the Alaska State ferry system. In the current environment, the downtown properties tend to compete most directly with the other downtown hotels and the valley properties typically compete most directly with their counterparts in the valley. Accordingly, given the nominal differences in quality and rate structure, we find that the most meaningful discussion of lodging market performance trends in Juneau should be defined along competitive lines (Downtown vs. Valley) rather than along qualitative lines (Upscale vs. Mid-scale). Additionally, the Juneau lodging market has a rather large concentration of hotels with an extended-stay orientation, which we attribute to the large influence of government demand in the market. While many of the hotels in the market offer some component of over-sized rooms, each of the last three hotels built in Juneau are of this product type, typically featuring over-sized guestrooms, kitchens, and even laundry facilities. Given the comparatively small size of the Juneau market, our analysis includes the more traditional transient oriented hotels and the extended-stay oriented hotels.

The Downtown submarket in Juneau consists of five hotels at the present time, including the Westmark Baranof Hotel, Goldbelt Hotel, Prospector Hotel, Driftwood Lodge, and the Juneau Hotel. With the exception of the regionally-branded Westmark, the remaining hotels are all independent. These hotels range in size from 62 to 195 rooms; and collectively represent a peak season inventory of 496 available guestrooms. Three of the hotels in the Downtown submarket are full-service facilities, offering a restaurant and lounge, and meeting and banquet space ranging from roundly 1,700 square feet to 5,100 square feet. The weighted average age of guestrooms in the Downtown submarket is 43 years. Many of the hotels in this submarket are negatively affected by their age and the modest levels of capital reinvestment in recent years. Due to the fully-developed nature of Juneau’s downtown core and the resulting lack of available land, the available room supply in the Downtown submarket was essentially static for almost 30 years prior to the opening of the Juneau Hotel which was constructed in several phases between 2003 and 2008. The Juneau Hotel is located at the edge of the downtown core, adjacent to the Douglas Bridge. This hotel operates with a total of 72 rooms with approximately one-half being extended-stay oriented, apartment-style units and the balance being more traditional transient hotel rooms.

The Valley submarket consists of four hotels, including the Extended Stay Deluxe (formerly the Aspen Hotel), the Travelodge, Best Western, and Frontier Suites. Three of the competitive hotels in this submarket benefit from nationally recognized franchises or affiliations, and one operates as an independent hotel. These hotels range in size from 55 to 104 guestrooms representing a 2007 peak season inventory of 340 available rooms. Two of the hotels in this submarket are full-service properties with a restaurant, lounge, and limited meeting facilities. The Valley submarket includes the bulk of the newer lodging facilities in Juneau and the only hotels in the market that offer indoor pools. Hotels in the Valley submarket have a weighted average age of 15 years compared to the Downtown submarket with a weighted average age of 43 years.

The following table identifies those properties in each of the two primary submarkets, including key physical attributes and the current seasonal published pricing of guestrooms.

Table 2
Profile of the Competitive Hotel Properties
Juneau, Alaska

						Meeting Space		2008 Rack Single/Double		
Downtown Submarket	**Class**	**Date Opened**	**Rooms**	**AAA Rating**	**F&B**	**Total Area (SF)**	**Largest Room (SF)**	**Summer**	**Winter**	**Amenities**
Westmark Baranof Hotel	Upscale	1939/1960's	195	◆◆	2/1	5,100	2,068	$149-$279	$149-$279	CF
Goldbelt Hotel	Upscale	1972	105	◆◆	1/1	2,129	780	$179-$189	$130-$139	N/A
Prospector Hotel	Mid-scale	1972	62	N/R	1/1	1,745	1,173	$169-$189	$129-$149	D
Driftwood Lodge	Mid-scale	1977	62	N/R	0/0	0	0	$94-$125	$68-$98	N/A
Juneau Hotel	Mid-scale	2004/2008	72	N/R	0/0	900	900	$169	$109-$129	E
Subtotal			496			9,874				
Valley Submarket										
Extended Stay Deluxe	Mid-scale	2000	95	◆◆	0/0	1,100	1,100	$169 - $189	$109 - $119	ABCE
Travelodge	Mid-scale	1985	86	N/R	1/1	2,372	1,400	$169-$189	$99 - $119	ABC
Best Western Country Lane	Mid-scale	1982	55	◆◆	0/0	0	0	$169-$179	$129-$139	DE
Frontier Suites	Mid-scale	1998/00	104	N/R	1/1	860	500	$129-$199	$109 - $159	CE
Subtotal			340			4,332				
TOTAL COMPETITIVE MARKET			**836**			**14,206**				

N/R - not rated

Amenities			
A	Pool	D	Bus. Ctr.
B	Spa/Steam	E	Gst Ldry.
C	Exercise	F	Retail

Source: K&M interviews, AAA-2008, individual websites, JCVB

Historical Supply and Demand

Table 3, presented on the page 10, summarizes information regarding the historical operating performance of the competitive hotels in the Downtown and Valley submarkets in Juneau for the period 2005 through 2007. Key indications from this summary are as follows:

- ♦ The growth in the available room supply in the overall market shows a nominal net gain of 27 available rooms on an annualized basis over the 2005 to 2007 period, indicating a compound average annual growth in supply of 1.7 percent. The only property to enter the market during this period was the 72-room Juneau Hotel, which was developed in multiple phases, thereby diffusing its impact on the market. On an annualized basis, this property had 20 of its available rooms open in 2005, increasing to 47 available rooms in

2007. The remaining 25 rooms will effectively enter the market in 2008 (18 rooms) and 2009 (7 rooms).

- ♦ During the 2005 to 2007 period all of the new rooms supply growth was concentrated in the Downtown submarket, yielding average growth of 3.0 percent annually. This contrasts with prior development cycles in Juneau when the Valley submarket received all of the new supply growth, following the opening of the Aspen Hotel in 2000 and the Frontier Suites, between 1998 and 2000.

- ♦ Based on historical data and our recent interviews in the market, we estimate that growth in rooms demand in the overall market grew at 3.6 percent annually over the 2005 through 2007 period, outpacing the annual growth in supply of 1.7 percent. Within the Downtown submarket growth in demand averaged 5.5 percent annually during the period, compared to rooms supply growth of 3.0 percent annually. In the Valley submarket, demand increased at 1.6 percent annually with zero growth in rooms supply. Each of these indicators suggests a moderate strengthening of demand for lodging within the submarkets in recent years.

- ♦ The resulting occupancy rates in the overall market showed modest increases in recent years, increasing from 64 percent in 2005 to 67 percent in 2007. Occupancy rates in the Downtown submarket increased from 58 percent to 61 percent during the period compared to Valley submarket where occupancies increased from 73 percent to 75 percent.

- ♦ In terms of occupancy, the Valley submarket typically outperforms the Downtown submarket by a fairly wide margin. We attribute this to several factors including less seasonal volatility in demand in the valley combined with the generally newer facilities and smaller size of the properties in this submarket.

- ♦ Average room rates within the overall market increased from roundly $96 to $105 during the 2005 to 2007 period, posting a 4.6 percent average annual growth rate. Rate growth was fairly evenly distributed between the two submarkets, although not so between the various individual hotels within each submarket. The Downtown submarket saw average room rates increase from $97 to $106 over the period, indicating a 4.5 percent annualized growth. The Valley submarket saw average room rates grow from $94 in 2005 to $104 in 2007, a 5.2 percent annualized growth. While increases of this magnitude are a positive indicator, they were not evenly distributed throughout the market, with some properties achieving double-digit growth while others captured little more than inflationary growth.

- ♦ Significant growth in average room rates has been a fairly common theme in the hotel industry as a whole in recent years. With an expanding economy and strong travel patterns, hoteliers sought to recapture rate increases that had been foregone in earlier years. While this underlying trend also appears to be present in Juneau, we attribute some portion of the strong rate growth in recent years to renovation and aggressive rate repositioning efforts by individual properties in the market.

- The overall market achieved growth in revenue per available room (RevPAR) during the 2005 to 2007 period of 6.3 percent annually, increasing from roundly $62 to $70. Stronger growth was posted by the Downtown submarket at 7.7 percent annually, with RevPAR increasing from $56 to $65, whereas the Valley submarket achieved RevPAR growth averaging 6.3 percent annually, increasing from $69 to $78. While a stronger RevPAR growth rate was achieved in the Downtown submarket, it still remains markedly below the RevPAR achieved by the Valley submarket, primarily due to the large differential in occupancies combined with little difference in average room rates between the submarkets.

Table 3
Competitive Lodging Market Overview - 2005 through 2007
Juneau, Alaska

	Available Rooms		Fair	Occ.	Occupied	Market	Penetr'n	Average	Room Revenue		REVPAR
	Daily	Annually	Share	Rate	Rm. Nights	Share	Rate	Rm. Rate	Total	Per Rm.	Index
2007											
Downtown Submarket	471	172,065	58.1%	61%	104,700	53.0%	91.2%	$106.00	$11,135,161	$65.00	92.9%
Valley Submarket	340	124,100	41.9%	75%	93,000	47.0%	112.3%	$104.00	$9,687,967	$78.00	111.4%
Total Market	811	296,165	100.0%	**67%**	197,700	100.0%	100.0%	$105.00	$20,823,128	$70.00	100.0%
% chg.		1.9%			3.7%				9.3%	6.1%	
2006											
Downtown Submarket	456	166,460	57.3%	60%	99,100	52.0%	90.8%	$100.00	$9,869,553	$59.00	89.4%
Valley Submarket	340	124,100	42.7%	74%	91,500	48.0%	112.4%	$100.00	$9,188,138	$74.00	112.1%
Total Market	796	290,560	100.0%	**66%**	190,600	100.0%	100.0%	$100.00	$19,057,691	$66.00	100.0%
% chg.		1.5%			3.3%				7.8%	6.5%	
2005											
Downtown Submarket	444	162,080	56.6%	58%	94,100	51.0%	90.1%	$97.00	$9,129,540	$56.00	90.3%
Valley Submarket	340	124,100	43.4%	73%	90,400	49.0%	113.0%	$94.00	$8,542,510	$69.00	111.3%
Total Market	784	286,180	100.0%	**64%**	184,500	100.0%	100.0%	$96.00	$17,672,050	$62.00	100.0%
Compound Average Annual Growth Rate 2005 - 2007											
Downtown Submarket		3.0%			5.5%			4.5%		7.7%	
Valley Submarket		0.0%			1.4%			5.2%		6.3%	
Total Market		1.7%			3.5%			4.6%		6.3%	

Source: Kennedy & Mohn, P.S.

Cruise/Tour Market Factors

As noted previously, the Juneau market is well entrenched with the cruise lines, but its location off of the primary road system in the state greatly limits its ability to participate significantly in the tour side of the cruise/tour market. Excepting several of the smaller cruise operators that turn their ships in Juneau, the bulk of the Juneau market is comprised of cruise-only activity. Typical cruise packages in the market are 7 to 10-day excursions, one-way itineraries (cruise one-way, fly home) originating in Seattle, Vancouver, or San Francisco and terminating in Seward or Whittier and then reversing the cycle southbound. Similar itineraries are available for passengers wishing to cruise both ways. For most guests that select a land-tour component to add to their cruise, this begins in Whittier or Seward, working its way north through Anchorage, Denali, and then Fairbanks.

The dominant players in the state's cruise/tour market in Alaska are Princess, Holland America, and Royal Celebrity. Only Holland America has a presence in the Juneau lodging market through its ownership of the Westmark Baranof Hotel in downtown Juneau. For reasons noted previously, this hotel benefits only indirectly from its relationship to Holland America, and potentially to its detriment, capturing a limited amount incidental demand, likely at discounted rates.

As shown in Table 1, cruise ship passenger volumes in Alaska have been growing steadily in recent years, primarily through the addition of more and larger ships to Alaskan waters, rather than through expansion of the typical cruise season which runs from mid-May though mid-September. Juneau is a primary stopover point for nearly all cruise itineraries, consistently capturing over 90 percent of the total cruise passenger volumes coming to Alaska each year. According to the Juneau Convention & Visitors Bureau, growth trends in this sector are expected to flatten as the infrastructure that supports the cruise ships in Juneau is currently operating at capacity. These capacity constraints may have augmented the recent development of cruise ship oriented tourism facilities at Icy Strait Point in Hoonah, Alaska, adding yet another alternative to the varied offerings of the major cruise lines in southeast Alaska.

Our recent interviews with cruise/tour operators in the state have produced mixed reviews, with several indicating a moderate slowing of demand patterns for 2008, while others indicate that 2008 will be flat to slightly up from 2007 numbers. Macro economic factors including the softening economy in the lower-48 and perpetually increasing fuel costs could potentially begin to exert downward pressure on demand within the cruise/tour sector of the market. However, given that the typical 7-day cruise of southeast Alaska is one of the least costly of the Alaska cruise/tour alternatives, Juneau's position in this market likely has limited downside risks in the near term.

Seasonal Factors

With the exception of legislative influences, lodging demand patterns in Juneau follow the typical seasonal patterns of most other markets in the state. Peak season is often identified by changes in rate structure at area hotels, which typically occurs during mid-May through mid-September, and coincides with the beginning and end of the cruise season in Alaska. With limited demand provided by cruise activity in the market, most peak season demand consists of independent leisure travelers and smaller packaged tours. Legislative activity in Juneau provides a much needed off-season boost to hotel demand patterns in the market during the spring of each year, typically January through April. Off-season periods occur during the balance of the year, when leisure travel is minimal and the market relies more heavily on demand from commercial, group, and non-legislative government activities.

Government related travel in Juneau is generated from two primary sectors: legislative activities and other government agencies including forest service, NOAA, Coast Guard, State DOT/PF, and a host of others. Demand generated by legislative activities is provided by state legislators, lobbyists, and anyone with a pet cause to support or defend. The bulk of this demand is typically captured in the downtown submarket and typically occurs during the January to April period each year. Conversely, most of the demand generated by government agency activities tends to be captured by hotels in the valley submarket and tends to occur fairly consistently throughout the year.

The legislative session begins each January and these sessions historically ran for 120-days. However, in 2006 voters passed an initiative that reduced the statutory length of legislative sessions from 120 days to 90 days, beginning in 2008. The trial-run for the 90-day session occurred earlier this spring and, while the session adjourned on time, some legislators felt it was rushed and that public involvement was limited. Similar commentary was received from hoteliers, who indicated that with fewer opportunities to meet with legislators, demand generated from lobbying activities was reduced significantly. A special 30-day session is scheduled to occur June 2008 to consider the natural gas pipeline project and potentially a second special session later in the year to address state energy issues. The timing of the special sessions is of particular concern to local hoteliers who fear that the market may be ill-equipped to accommodate the simultaneous needs of legislative and leisure travelers and that this could potentially be used against Juneau in the continuing efforts to gain support for a capitol move.

The combined effect of seasonal changes in room rates and demand patterns in recent years are visible in the historical trends in hotel room tax receipts reported by the City and Borough of Juneau as shown in Table 4.

Table 4
Juneau Hotel Motel Tax Receipts - 2003 - 2007

		1st Qtr. *(2)*	2nd Qtr.	3rd Qtr.	4th Qtr.	Total *(1)*	% Chg.
2003	Total	137,813	158,019	326,366	315,297	897,011	
2004	Total	96,765	155,143	286,399	306,359	906,280	1.0%
2005	Total	122,633	159,000	313,974	319,744	886,240	-2.2%
2006	Total	125,943	183,668	340,508	343,142	1,061,798	19.8%
2007	Total	153,281	220,862	376,942	393,646	1,184,151	11.5%
Total Market							
% of Annual (2007)		13%	19%	32%	33%	100.0%	
CAAGR 2003-2007						7.2%	

Note 1: Annual total shown after year-end adjustments for accual/reversal
Note 2: Quarterly tax collections lag demand by one quarter, with Jan-Mar taxes due in April

Source: Juneau Convention & Visitors Bureau - Hotel Bed Tax Receipts

Segmentation

We classified market demand into four general categories: commercial, leisure, group, and contract. Segmentation data is routinely tracked by hotel operators, although the level of detail and accuracy of the data varies widely between properties. In recent years it has become more and more difficult for hotel operators to maintain accurate segmentation data due to the increased use of Internet booking engines and promotions. While these choices can be attractive to the guest, they hinder the hotel's ability to accurately track guest segmentation patterns.

- Commercial demand is composed of independent business travelers and state and federal government workers. Demand in the commercial segment is reasonably stable throughout the year, with modest declines during summer and holiday periods. The government component of this segment increases substantially each spring and during special session periods. Based on our recent interviews, we estimate this demand represents approximately 54 percent of total annual demand in the overall market in 2007.

- Leisure demand consists of independent and packaged leisure travelers and is concentrated primarily during the peak summer season, with more modest levels during the balance of the year. We estimate the leisure demand segment to represent approximately 36 percent of total annual demand in the market.

- Group demand consists of conventions and meeting related travel to Juneau, and demand generated by sports teams and school events. Demand in this segment is typically concentrated during shoulder periods in the spring and fall. Current interviews suggest that group demand represents approximately 7 percent of total demand in the market.

- Contract demand in Juneau is provided primarily by airline crews. This demand makes up approximately three percent of total demand in the market and is concentrated in the Downtown submarket.

SUPPLY AND DEMAND PROJECTIONS

In evaluating the performance potential of the Juneau lodging market in future years we have considered historical and projected changes in the competitive rooms supply and anticipated changes in market demand volumes and patterns over the near to mid-term. Our analysis incorporates the addition of new hotels that are expected to open in the market over the next several years. Projections of future demand growth reflect contributions from three fundamental sources: unsatisfied demand, induced demand, and underlying growth in demand. A detailed discussion of our analysis is presented in the following paragraphs.

Supply Changes

Based on our research and interviews in the local market, we are aware of no other new hotels planned for development in Juneau at the present time. Several definite, but only minimally significant, changes to the guestroom inventory are expected to occur in the market in the near term. The Juneau Hotel will continue to gradually open its remaining inventory, with the last phase of construction scheduled to open in June 2008. This addition equates to an annualized allocation of 18-rooms entering the market in 2008 and 7-rooms in 2009. According to management at the Westmark Baranof Hotel, planned renovations will reduce the available room count at this hotel from 195 to 192 beginning in 2009.

To our knowledge, several hotel developers active in the state have expressed an interest in developing new hotels in Juneau, recognizing the dated quality of much of the inventory. However, thus far, these developers have not been successful in acquiring suitable sites for development. Based on recent and projected performance levels in the Juneau market, we have assumed that an additional hotel will be built in the Valley submarket during the later part of our projection period. Our projections reflect development of an approximately 75-room property opening in mid-2010.

Demand Changes

Within our analysis, projections of growth in demand reflect the combination of three individual components including unsatisfied demand, underlying growth, and induced demand.

- Unsatisfied demand is that component of new demand that can be accommodated in the market as new hotel rooms open, thereby providing additional capacity during peak periods.

- Underlying growth is projected based on the strength of local and regional economic indicators such as growth in population, employment, growth in room tax collections, and growth in air travel.

- Induced demand reflects changes in the market that are induced by forces external to the market. Induced demand can be either positive or negative, with the opening of a new demand generator providing a positive inducement of demand, while the opening of competing hotels outside the competitive market, which draw off demand, would result in negative induced demand.

In arriving at our estimates of future demand growth, consideration was given to mix of demand by segment, seasonal patterns of demand, and the seasonal capacity constraints within the market. Key factors in our analysis are summarized in the following paragraphs.

- We estimate underlying growth in demand based on historical changes in key economic indicators, as presented previously in Table 1, tempered with anticipated changes over the near term. The economic data provides support for underlying growth rates generally in the range of one to three percent annually, based on growth in employment, population, air passenger volumes, and room taxes, while historical growth in rooms demand has averaged 3.5 percent annually in recent years. The following growth rates are applied uniformly to both the Downtown and Valley submarkets, yielding average underlying growth of 2.2 annually during our projection period.

- Our projections of underlying growth in demand include growth in the commercial/government segment of 2.0 percent annually throughout the projection period. Growth in this segment reflects modest underlying growth in employment, declining local construction activity, with the expectation that increased state spending will gradually bolster many of the state agencies based in Juneau.

- Within the group demand segment, growth is projected at 1.0 percent annually throughout the projection period, recognizing the nominal contribution of demand derived from this segment.

- Leisure demand is projected to grow at 1.0 percent annually during the early years of the projection period, increasing to 2.0 percent annually by the middle of our projection period. This estimate reflects anticipated flattening of demand patterns due to external economic forces that are expected to have somewhat greater impact on independent travel patterns.

- Within the contract demand segment growth is projected at 0.0 percent annually throughout the projection period, reflecting no significant changes in the key support industries within this segment.

♦ Unsatisfied demand in the Downtown submarket is projected based on 50 fill nights annually at a 75 percent occupancy rate for the new guestrooms projected to enter the market during the projection period. No deduct is taken for the reconfigured inventory at the Baranof. This demand is allocated equally to the commercial and leisure demand segments. Given the stronger occupancies achieved in the Valley submarket, unsatisfied demand is projected based on an estimated 65 fill nights annually.

♦ Our estimates of induced demand reflect a negative inducement of roundly 8,000 room nights of demand from the commercial/government segment in 2008, reflecting the shift from a 120-day to a 90-day legislative session. Our interviews in the market consistently indicated that this change had a material impact on demand patterns during the 2008 legislative session. We have allocated approximately 85 percent of this impact to the Downtown submarket, with the remainder allocated to Valley submarket.

Table 5, presented on the following page, sets forth our projections of growth in demand throughout the forecast period.

Table 5
Projected Demand Growth by Segment

	2008	2009	2010	2011	2012	
Downtown Submarket						**Mix**
Commercial Demand	47,800	49,000	50,000	51,000	52,000	48%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	400	200	0	0	0	
Induced Demand	(6,800)	0	0	0	0	
Group Demand	11,100	11,200	11,300	11,400	11,500	11%
Underlying Growth	1.0%	1.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Leisure Demand	36,100	36,700	37,400	38,100	38,900	36%
Underlying Growth	1.0%	1.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	400	200	0	0	0	
Induced Demand	0	0	0	0	0	
Contract Demand	5,300	5,300	5,300	5,300	5,300	5%
Underlying Growth	0.0%	0.0%	0.0%	0.0%	0.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	100,000	102,000	104,000	106,000	108,000	100%
Valley Submarket						**Mix**
Commercial Demand	53,300	54,400	56,800	58,800	60,000	58%
Underlying Growth	2.0%	2.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	0	0	1,300	900	0	
Induced Demand	(1,200)	0	0	0	0	
Group Demand	2,400	2,400	2,400	2,400	2,400	2%
Underlying Growth	1.0%	1.0%	1.0%	1.0%	1.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Leisure Demand	37,500	37,900	39,600	41,000	41,800	40%
Underlying Growth	1.0%	1.0%	2.0%	2.0%	2.0%	
Unsatisfied Demand	0	0	900	600	0	
Induced Demand	0	0	0	0	0	
Contract Demand	0	0	0	0	0	0%
Underlying Growth	0.0%	0.0%	0.0%	0.0%	0.0%	
Unsatisfied Demand	0	0	0	0	0	
Induced Demand	0	0	0	0	0	
Total Demand	93,000	95,000	99,000	102,000	104,000	100%
Overall Market						
Commercial Demand	52%	52%	53%	53%	53%	
Group Demand	7%	7%	7%	7%	7%	
Leisure Demand	38%	38%	38%	38%	38%	
Contract Demand	3%	3%	3%	3%	3%	
Total Demand	100%	100%	100%	100%	100%	

Table 6, presented on the following page, incorporates our individual projections of demand growth by segment and submarket into a single presentation of historical and projected changes in supply and demand within the Juneau market. Collectively, our estimates of unsatisfied, induced, and underlying demand growth indicate a 2.4 percent average annual increase in demand for the overall market from 2008 through 2012. This rate of demand growth is less than the historical rate of demand growth achieved by the market in recent years due predominantly to legislative changes and softening economic factors. Our projections indicate occupancy rates for the overall market are expected to decline approximately three percentage points in 2008 to roundly 64 percent. Further decline would result following the potential opening of a new hotel in the Valley submarket although its impact would also be concentrated in this submarket.

Within the Downtown submarket our projections indicate that occupancy rates will decline in 2008 to approximately 56 percent as a result of the shorter legislative session and reduced lobbying activity, in conjunction with modest increases in supply. With no further supply changes expected later in the projection period, we forecast a slow but gradual rebuilding of occupancies in later years, reaching approximately 60 percent by the end of our projection period. Occupancies could grow slightly faster in future years, depending on the frequency and timing of special sessions, which are not factored into our analysis.

In contrast, the Valley submarket has historically enjoyed a notable premium in occupancy when compared to the Downtown submarket. This premium is expected to be sustained in future years, despite the decline forecast in the Downtown submarket. Changes to legislative sessions are expected to have negligible impact on demand in the Valley submarket and while similarly moderate growth is projected, this submarket appears to have little downside risk in the near to mid term, other than potential supply change. We project occupancies in the Valley submarket will remain in the mid to upper-70 percent range during the early years of our projection period but sustained performance at this level is expected to attract new development in subsequent years, causing occupancies in this submarket to decline. Given the relatively small size of the Valley submarket, the extent of this decline will depend heavily on the number of new rooms that are built. Our projections assume a 75-room hotel will be developed in approximately mid-2010 and that as a result, occupancies in this submarket will decline to a low of 67 percent in 2011, rebuilding slowly thereafter. In the event that a new hotel does not enter this submarket, occupancies would be expected to improve slightly and the Downtown submarket would likely benefit from increasing levels of compression in the Valley submarket.

Table 6
Historical and Projected Market Conditions

2005	2006	2007		2008	2009	2010	2011	2012
				Projected Market Conditions				
			Downtown Submarket					
444	456	471	Existing Product	471	468	468	468	468
			Juneau Hotel (exp)	18	25	25	25	25
444	456	471	Average Daily Rooms	489	493	493	493	493
162,080	166,460	172,065	Annual Room Nights	178,635	180,095	180,095	180,095	180,095
	2.7%	3.4%	Percentage Change	3.8%	0.8%	0.0%	0.0%	0.0%
94,100	99,051	104,747	Market Demand	100,000	102,000	104,000	106,000	108,000
CAAGR Supply chg.		3.0%		**CAAGR**		Supply chg.	0.2%	
CAAGR Demand chg.		5.5%		**CAAGR**		Demand chg.	1.9%	
	4,951	5,697	Change from prior year	(4,747)	2,000	2,000	2,000	2,000
	5.3%	5.8%	Percentage Change					
	500	700	Unsatisfied Demand	700	300	0	0	0
	0	0	Induced Demand	(6,800)	0	0	0	0
	4,451	4,997	Underlying Growth	1,353	1,700	2,000	2,000	2,000
	4.7%	5.0%	Underlying Growth Rate	1.3%	1.7%	2.0%	1.9%	1.9%
58%	60%	61%	Occupancy	56%	57%	58%	59%	60%
			Valley Submarket					
340	340	340	Existing Product	340	340	340	340	340
			Proposed hotels	0	0	44	75	75
340	340	340	Average Daily Rooms	340	340	384	415	415
124,100	124,100	124,100	Annual Room Nights	124,100	124,100	140,160	151,475	151,475
	0.0%	0.0%	Percentage Change	0.0%	0.0%	12.9%	8.1%	0.0%
90,400	91,462	93,018	Market Demand	93,000	95,000	99,000	102,000	104,000
CAAGR Supply chg.		0.0%		**CAAGR**		Supply chg.	5.1%	
CAAGR Demand chg.		1.4%		**CAAGR**		Demand chg.	2.8%	
	1,062	1,556	Change from prior year	(18)	2,000	4,000	3,000	2,000
	1.2%	1.7%	Percentage Change					
	0	0	Unsatisfied demand	0	0	2,145	1,511	0
	0	0	Induced Demand	(1,200)	0	0	0	0
	1,062	1,556	Underlying Growth	1,182	2,000	1,855	1,489	2,000
	1%	2%	Underlying Growth Rate	1.3%	2.2%	2.0%	1.5%	2.0%
73%	74%	75%	Occupancy	75%	77%	71%	67%	69%
			Overall Market					
784	796	811	Average Daily Rooms	829	833	877	908	908
286,180	290,560	296,165	Overall Market Supply	302,735	304,195	320,255	331,570	331,570
	2%	2%	Supply Growth	2%	0%	5%	4%	0%
184,500	190,513	197,765	Overall Market Demand	193,000	197,000	203,000	208,000	212,000
	3%	4%	Demand Growth	-2%	2%	3%	2%	2%
CAAGR Supply chg.		1.7%		**CAAGR**		Supply chg.	2.3%	
CAAGR Demand chg.		3.5%		**CAAGR**		Demand chg.	2.4%	
64%	66%	67%	Occupancy	64%	65%	63%	63%	64%

Average Room Rates

In analyzing the Juneau lodging market, we find comparatively little differential in rate structure between the Downtown and Valley submarkets, despite the larger variance in occupancies. While seasonal variations in rate structure within the market are driven by changing demand patterns, the seasonal rate changes in Juneau are generally less than those found in other major markets in the state. The lower spread in seasonal rates is likely attributable to Juneau's relative lack of cruise/tour demand which impacts both the cost and availability of guestrooms. Similarly, the Juneau market presents a relatively level playing field, without the presence of hotels with significantly higher quality and larger size that enables them to manipulate demand by offering lower priced rooms. With somewhat more homogeneous rooms quality in the market, unfair competition is reduced, which creates an environment that is conducive to gradual rate growth.

Average room rates in Juneau are influenced by the comparatively large component of demand derived from the government sector with per diem rates of $79 off-peak and $129 during peak season. A potential, but unanticipated result of changes in legislative demand volumes may exert modest upward pressure on average room rates in the market as less discounted demand is captured during off-peak periods. However, if operators respond to declining demand by cutting room rates, the opposite could also be true. We assume that operators recognize that cutting rates does not increase demand patterns, but only serves to redistribute the available base of demand.

The only thing certain about average room rates is that they are constantly in a state of flux. The direction of change and the relative significance of that change depends on a myriad of forces operating within the market and the response to these forces by the individual operators. During the 2005 to 2007 period, average room rates in Juneau increased at nearly twice the underlying rate of inflation. Historical rate growth was fairly consistent between the two submarkets, which generally supports our earlier contention regarding comparable quality and a competitively neutral environment.

To derive a five-year projection of growth in average room rate, we considered the dual impacts of inflation and anticipated market conditions. We have incorporated an underlying inflation rate of 2.5 percent annually throughout the projection period. Market condition adjustments are based on our estimates of how the market will respond to a variety of factors including, the softening economy, flattening of growth in the cruise and tour industries, and new rooms that may enter the market in future years. We project growth in average room rates within the overall market at roundly 2.9 percent annually over the projection period, reflecting a modest slowing of growth from recent years. We project the Downtown submarket will achieve rate growth averaging 2.6 percent annually during the projection period, compared to 3.1 percent annually in the Valley submarket. Our projections of growth in average room rate for each submarket are shown in the following table. The resulting average room rate for the overall market is the weighted average reflecting demand patterns and rates within the two submarkets.

Table 7
Projected Average Room Rate And Revenue Per Available Room

Year/Market	Inflation	Market Response	Total Change	Projected ARR	Projected Occup. %	Projected REVPAR
2007						
Downtown Submarket				$106.00	61%	$64.53
Valley Submarket				$104.00	75%	$77.95
Overall Market				$105.00	67%	$70.11
2008						
Downtown Submarket	2.50%	1.00%	3.50%	$110.00	56%	$61.58
Valley Submarket	2.50%	1.00%	3.50%	$108.00	75%	$80.93
Overall Market				$109.00	64%	$69.49
2009						
Downtown Submarket	2.50%	0.00%	2.50%	$113.00	57%	$64.00
Valley Submarket	2.50%	1.00%	3.50%	$112.00	77%	$85.74
Overall Market				$113.00	65%	$73.18
2010						
Downtown Submarket	2.50%	0.00%	2.50%	$116.00	58%	$66.99
Valley Submarket	2.50%	1.00%	3.50%	$116.00	71%	$81.93
Overall Market				$116.00	63%	$73.53
2011						
Downtown Submarket	2.50%	0.00%	2.50%	$119.00	59%	$70.04
Valley Submarket	2.50%	0.00%	2.50%	$119.00	67%	$80.13
Overall Market				$119.00	63%	$74.65
2012						
Downtown Submarket	2.50%	0.00%	2.50%	$122.00	60%	$73.16
Valley Submarket	2.50%	0.00%	2.50%	$122.00	69%	$83.76
Overall Market				$122.00	64%	$78.00

Source: Kennedy & Mohn, P.S.

CONCLUSION

Based on our current analysis, the Juneau lodging market has performed reasonably well in recent years, achieving notable growth in occupancies and average room rates within an environment of comparatively little supply growth. Future years will be negatively impacted by the voter-mandated 90-day legislative sessions, although this could be mitigated somewhat by a greater need for special sessions, provided these continue to occur in Juneau, and preferably during off-peaks periods. Given the relative lack of developable land in Juneau, we do not anticipate this market will experience the significant supply changes that have occurred in other primary markets within the state, but some level of supply growth should be reasonably anticipated in future years. The likelihood of new hotel development in Juneau is enhanced by the relative lack of nationally-branded hotels, of which there are presently few; and none of these are considered primary brands. The overall outlook for the Juneau lodging market is generally considered favorable, despite the moderate declines projected in future years due to demand changes and potential new development. The greatest risks to the Juneau market relate to the uncertainty of its position as the Capitol-city, which stifles economic development on many levels. In our opinion, if the capitol or the legislature were to move from Juneau, other state facilities would likely follow and the impact on lodging in the market would be significant.

We trust that AIDEA will find the updated analysis and commentary presented in this report to be beneficial for developing an improved level of understanding regarding the current factors influencing the lodging market in Juneau. Should you have any questions or require clarification on any of the issues discussed in this report, please do not hesitate to contact us.

Sincerely,

Kennedy & Mohn P.S. 030

Kennedy & Mohn, P.S.

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This market overview study has been prepared under the following general assumptions:

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CERTIFICATION

I certify that, to the best of my knowledge and belief:

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, impartial, and unbiased professional analyses, opinions, conclusions, and recommendations.
- I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest with respect to the parties involved.
- I have no bias with respect to any property that is the subject of this report or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation for completing this assignment is not contingent upon the development or reporting of a pre-determined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this report.
- The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics & Standards of Professional Appraisal Practice of the Appraisal Institute, which include the *Uniform Standards of Professional Appraisal Practice*.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- I have made a personal inspection of the property that is the subject of this report.
- No one provided significant real property appraisal or appraisal consulting assistance to the persons signing this certification.
- As of the date of this report, Michael J. Mohn, MAI has completed the continuing education program of the Appraisal Institute.

Michael J. Mohn, MAI

CCERT Ver.5/2005