Sunstone Hotel Investors, Inc.
Form 424B5
October 31, 2013
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Filed pursuant to Rule 424(b)(5)
Reg. Statement No. 333-171712

CALCULATION OF REGISTRATION FEE

Title of each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee(1)
Sunstone Hotel Investors, Inc. Common Stock, par value $0.01 per share	$311,880,000	$40,170.15

(1) The registration fee is calculated in accordance with Rule 457(o) under the Securities Act of 1933, as amended, or the Securities Act, based on the proposed maximum aggregate offering price, and Rule 457(r) under the Securities Act. In accordance with Rules 456(b) and 457(r) under the Securities Act, the registrant initially deferred payment of all of the registration fee for Registration Statement No. 333-171712.

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PROSPECTUS SUPPLEMENT

(To prospectus dated January 14, 2011)

20,000,000 Shares

Sunstone Hotel Investors, Inc.

Common Stock

We are offering 20,000,000 shares of our common stock.

Our common stock currently trades on the New York Stock Exchange, or the NYSE, under the symbol SHO. On October 28, 2013, the last reported sale price of our common stock on the NYSE was $13.97 per share. Shares of our common stock are subject to ownership and transfer limitations that must be applied to maintain our status as a real estate investment trust, or REIT.

See Risk Factors on page S-13 of this prospectus supplement to obtain information about where to read certain factors you should consider before buying shares of our common stock.

The underwriter has agreed to purchase shares of common stock from us at a price of $13.56 per share which will result in $271.2 million of proceeds to us, before expenses. The underwriter may offer shares of common stock in transactions on the NYSE, in the over-the-counter market or through negotiated transactions at market prices or at negotiated prices. See Underwriting.

Neither the Securities and Exchange Commission, or the SEC, nor any other state or federal regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus supplement or the accompanying prospectus. Any representation to the contrary is a criminal offense.

We have granted the underwriter a 30-day option to purchase up to 3,000,000 shares of common stock at a price of $13.56.

The underwriter expects to deliver the shares in New York, New York on or about November 1, 2013.

Sole Book-Running Manager

BofA Merrill Lynch

The date of this Prospectus Supplement is October 29, 2013.

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Prospectus Supplement

Prospectus

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ABOUT THIS PROSPECTUS SUPPLEMENT

You should read this prospectus supplement along with the accompanying prospectus, as well as the information incorporated by reference herein and therein, carefully before you invest in our common stock. These documents contain important information that you should consider before making your investment decision. This prospectus supplement and the accompanying prospectus contain the terms of this offering of common stock. The accompanying prospectus contains information about our securities generally, some of which does not apply to the common stock covered by this prospectus supplement. This prospectus supplement may add, update or change information contained in or incorporated by reference in the accompanying prospectus. If the information in this prospectus supplement is inconsistent with any information contained in or incorporated by reference in the accompanying prospectus, the information in this prospectus supplement will apply and will supersede the inconsistent information contained in or incorporated by reference in the accompanying prospectus.

It is important for you to read and consider all of the information contained in this prospectus supplement and the accompanying prospectus before making your investment decision. You should also read and consider the additional information incorporated by reference in this prospectus supplement and the accompanying prospectus before making your investment decision. See Incorporation of Certain Information by Reference in this prospectus supplement.

You should rely only on the information contained in or incorporated by reference in this prospectus supplement, the accompanying prospectus and any related free writing prospectus required to be filed with the Securities and Exchange Commission, or the SEC. Neither we nor the underwriter has authorized any other person to provide you with additional or different information. If anyone provides you with additional or different information, you should not rely on it. Neither we nor the underwriter is making an offer to sell the common stock in any jurisdiction where the offer or sale is not permitted.

You should assume that the information appearing in this prospectus supplement, the accompanying prospectus, any such free writing prospectus and the documents incorporated by reference herein and therein is accurate only as of their respective dates. Our business, financial condition, results of operations and prospects may have changed since those dates.

Unless this prospectus supplement otherwise indicates or the context otherwise requires, the terms our, us, we and the Company as used in this prospectus supplement refer to Sunstone Hotel Investors, Inc. and its consolidated subsidiaries. We also use the term Operating Partnership to specifically refer to Sunstone Hotel Partnership, LLC and its consolidated subsidiaries in cases where it is important to distinguish between us and the Operating Partnership. Unless otherwise expressly stated or the context otherwise requires, all information in this prospectus supplement assumes that the option granted to the underwriter is not exercised in whole or in part.

This prospectus supplement and the accompanying prospectus contain registered trademarks that are the exclusive property of their respective owners, which are companies other than us. None of the owners of these trademarks, their affiliates or any of their respective officers, directors, agents or employees, has or will have any responsibility or liability for any information contained in this prospectus or the accompanying prospectus supplement.

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USE OF NON-GAAP FINANCIAL MEASURES

This prospectus supplement contains non-GAAP financial measures as defined by the rules and regulations of the SEC. A non-GAAP financial measure is a numerical measure of a company s historical or future financial performance, financial position or cash flows that excludes amounts, or is subject to adjustments that have the effect of excluding amounts, that are included in the most directly comparable measure calculated and presented in accordance with GAAP in the statements of operations, balance sheets, or statements of cash flows of Sunstone Hotel Investors, Inc.; or includes amounts, or is subject to adjustments that have the effect of including amounts, that are excluded from the most directly comparable measure so calculated and presented. Reconciliations of these non-GAAP financial measures to their comparable GAAP financial measures are incorporated by reference in this prospectus supplement.

We present the following non-GAAP financial measures that we believe are useful to investors as key measures of our operating performance: Earnings Before Interest Expense, Taxes, Depreciation and Amortization, or EBITDA; Adjusted EBITDA (as defined below); Funds From Operations, or FFO; Adjusted FFO (as defined below); and Adjusted Comparable Hotel RevPAR. These measures should not be considered in isolation or as a substitute for measures of performance in accordance with GAAP. EBITDA, Adjusted EBITDA, FFO, Adjusted FFO and Adjusted Comparable Hotel RevPAR as calculated by us, may not be comparable to other companies that do not define such terms exactly as the Company. These non-GAAP measures are used in addition to and in conjunction with results presented in accordance with GAAP. They should not be considered as alternatives to operating profit, cash flow from operations, or any other operating performance measure prescribed by GAAP. These non-GAAP financial measures reflect additional ways of viewing our operations that we believe, when viewed with our GAAP results and the reconciliations to the corresponding GAAP financial measures, provide a more complete understanding of factors and trends affecting our business than could be obtained absent this disclosure. We strongly encourage investors to review our financial information in its entirety and not to rely on a single financial measure.

EBITDA is a commonly used measure of performance in many industries. We believe EBITDA is useful to investors in evaluating our operating performance because this measure helps investors evaluate and compare the results of our operations from period to period by removing the impact of our capital structure (primarily interest expense) and our asset base (primarily depreciation and amortization) from our operating results. We also believe the use of EBITDA facilitates comparisons between us and other lodging REITs, hotel owners who are not REITs and other capital-intensive companies. In addition, certain covenants included in our indebtedness use EBITDA as a measure of financial compliance. We also use EBITDA as a measure in determining the value of hotel acquisitions and dispositions.

Historically, we have adjusted EBITDA when evaluating our performance because we believe that the exclusion of certain additional items described below provides useful information to investors regarding our operating performance and that the presentation of Adjusted EBITDA, when combined with the primary GAAP presentation of net income, is beneficial to an investor s complete understanding of our operating performance.

We believe that the presentation of FFO provides useful information to investors regarding our operating performance because it is a measure of our operations without regard to specified non-cash items such as real estate depreciation and amortization, amortization of lease intangibles, any real estate impairment loss and any gain or loss on sale of real estate assets, all of which are based on historical cost accounting and may be of lesser significance in evaluating our current performance. We believe the use of FFO facilitates comparisons between us and other lodging REITs.

We also present Adjusted FFO when evaluating our operating performance because we believe that the exclusion of certain additional items described below provides useful supplemental information to investors regarding our ongoing operating performance, and may facilitate comparisons of operating performance between periods and our peer companies.

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We adjust EBITDA and FFO for the following items, which may occur in any period, and refer to these measures as either Adjusted EBITDA or Adjusted FFO:

Amortization of favorable and unfavorable contracts: we exclude the non-cash amortization of the favorable management contract asset and the unfavorable tenant lease liability recorded in conjunction with our acquisition of the Hilton Garden Inn Chicago Downtown/Magnificent Mile, along with the favorable tenant lease asset recorded in conjunction with our acquisition of the Hilton New Orleans St. Charles, and the unfavorable tenant lease liabilities recorded in conjunction with our acquisition of the Boston Park Plaza. The amortization of favorable and unfavorable contracts does not reflect the underlying performance of our hotels.

Ground rent adjustments: we exclude the non-cash expense incurred from straightlining our ground lease obligations as this expense does not reflect the underlying performance of our hotels.

Gains or losses from debt transactions: we exclude the effect of finance charges and premiums associated with the extinguishment of debt, including the acceleration of deferred financing costs from the original issuance of the debt being redeemed or retired because, like interest expense, their removal helps investors evaluate and compare the results of our operations from period to period by removing the impact of our capital structure.

Acquisition costs: under GAAP, costs associated with completed acquisitions are expensed in the year incurred. We exclude the effect of these costs because we believe they are not reflective of the ongoing performance of the Company.

Consolidated partnership adjustments: we deduct the non-controlling partner s pro rata share of any EBITDA or FFO adjustments related to our consolidated Hilton San Diego Bayfront partnership.

Cumulative effect of a change in accounting principle: infrequently, the FASB promulgates new accounting standards that require the consolidated statement of operations to reflect the cumulative effect of a change in accounting principle. We exclude these one-time adjustments because they do not reflect our actual performance for that period.

Impairment losses: we exclude the effect of impairment losses because we believe that including them in Adjusted EBITDA and Adjusted FFO is not consistent with reflecting the ongoing performance of our remaining assets.

Other adjustments: we exclude other adjustments such as lawsuit settlement costs (or the reversal of these costs), prior year property tax assessments and/or credits, management company transition costs, and departmental closing costs, including severance, because we do not believe these costs reflect our actual performance and/or the ongoing operations of our hotels.

In addition, to derive Adjusted EBITDA we exclude the non-cash expense incurred with the amortization of deferred stock compensation as this expense does not reflect the underlying performance of our hotels. We also include an adjustment for the cash ground lease expense recorded on the Hyatt Chicago Magnificent Mile s building lease. Upon acquisition of this hotel, we determined that the building lease was a capital lease, and, therefore, we include a portion of the capital lease payment each month in interest expense. We include an adjustment for ground lease expense on capital leases in order to more accurately reflect the operating performance of the Hyatt Chicago Magnificent Mile. We also exclude the effect of gains and losses on the disposition of depreciable assets because we believe that including them in Adjusted EBITDA is not consistent with reflecting the ongoing performance of our assets. In addition, material gains or losses from the depreciated value of the disposed assets could be less important to investors given that the depreciated asset value often does not reflect its market value.

To derive Adjusted FFO, we also exclude the non-cash gains or losses on our derivatives, as well as the original issuance costs associated with the redemption of preferred stock and any federal and state taxes associated with the application of net operating loss carryforwards. We believe that these items are not reflective of our ongoing finance costs.

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Adjusted Comparable Hotel RevPAR is defined as revenue per available room for our 27 comparable hotels adjusted to include the effects of converting the operating statistics for our ten Marriott-managed hotels from a 13-period basis as reported in 2012 to a standard 12-month calendar basis. We believe the calculation of Adjusted Comparable Hotel RevPAR results in a more accurate presentation of hotel RevPAR of the Company s 27 comparable hotels, and that these non-GAAP financial measures are useful to investors in evaluating our property-level operating performance. Our 27 comparable hotels include all hotels held for investment as of September 30, 2013, except the Boston Park Plaza, and also include prior ownership results as applicable in 2012 and 2013 for the Hilton New Orleans St. Charles acquired in May 2013, along with prior ownership results as applicable in 2012 for the Hyatt Chicago Magnificent Mile acquired in June 2012 and the Hilton Garden Inn Chicago Downtown/Magnificent Mile acquired in July 2012.

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INCORPORATION OF CERTAIN INFORMATION BY REFERENCE

The SEC s rules allow us to incorporate by reference information into this prospectus supplement and the accompanying prospectus. This means that we can disclose important information to you by referring you to another document. Any information referred to in this way is considered part of this prospectus supplement and the attached prospectus from the date we file that document. Any reports filed by us with the SEC after the date of this prospectus supplement and before the date that the offering of the securities by means of this prospectus supplement is terminated will automatically update and, where applicable, supersede any information contained, or incorporated by reference, in this prospectus supplement or in the accompanying prospectus.

We incorporate by reference into this prospectus supplement and the accompanying prospectus:

- our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the SEC on February 25, 2013 (including information specifically incorporated by reference therein from our Proxy Statement for our 2013 Annual Meeting filed with the SEC on March 25, 2013);

- our Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2013 and June 30, 2013, filed with the SEC on May 8, 2013 and August 7, 2013, respectively;

- our Current Reports on Form 8-K filed with the SEC on January 25, 2013 (but only with respect to Item 2.01), February 1, 2013, February 19, 2013 (but only with respect to Item 5.02), April 29, 2013, May 6, 2013 (but only with respect to Items 2.01, 5.02, 5.07 and 9.01) and July 2, 2013, and our Current Reports on Form 8-K/A filed with the SEC on July 15, 2013 and July 17, 2013;

- the description of the common stock included in our registration statement on Form 8-A, filed with the SEC on October 7, 2004, together with any amendment or report filed with the SEC for the purpose of updating such description; and

- all documents we file with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, on or after the date of this prospectus supplement and before the termination of this offering.

We are not, however, incorporating by reference any documents or portions thereof, whether specifically listed above or filed in the future, that are not deemed filed with the SEC. The documents incorporated by reference in this prospectus supplement and the accompanying prospectus and, in particular, our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the SEC on February 25, 2013, contain important information about us.

You should read Incorporation of Certain Information by Reference in the accompanying prospectus for information about how to obtain the documents incorporated by reference.

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SUMMARY

The information below is a summary of the more detailed information included elsewhere in, or incorporated by reference in, this prospectus supplement. You should read carefully the following summary in conjunction with the more detailed information contained in this prospectus supplement, the accompanying prospectus and the information incorporated by reference herein and therein. This summary is not complete and does not contain all of the information you should consider before purchasing shares of our common stock. You should carefully read the Risk Factors section on page S-13 of this prospectus supplement to determine whether an investment in our common stock is appropriate for you.

Sunstone Hotel Investors, Inc.

Our Company

We were incorporated in Maryland on June 28, 2004. We are a real estate investment trust, or REIT, under the Internal Revenue Code of 1986, as amended, or the Code. As of September 30, 2013, we had interests in 28 hotels held for investment, or the 28 hotels. The 28 hotels are comprised of 12,942 rooms, located in 12 states and in Washington, D.C.

Our primary business is to acquire, own, asset manage and renovate full-service hotel properties in the United States. As part of our ongoing portfolio management strategy, we may also sell certain hotel properties from time to time. Our hotels are operated under nationally recognized brands, such as Marriott, Hilton, Hyatt, Fairmont and Sheraton. Our portfolio primarily consists of upper upscale hotels in the United States. As of September 30, 2013, our 28 hotels included two luxury hotels, and 26 upscale or upper upscale hotels. The classifications luxury, upper upscale and upscale are defined by Smith Travel Research, an independent provider of lodging industry statistical data. Smith Travel Research classifies hotel chains into the following segments: luxury; upper upscale; upscale; upper midscale; midscale; economy; and independent.

Our hotels are operated by third-party managers pursuant to long-term management agreements with our subsidiary, Sunstone Hotel TRS Lessee, Inc., or its subsidiaries. As of September 30, 2013, our third-party managers included: subsidiaries of Marriott International, Inc. or Marriott Hotel Services, Inc., managers of 10 of the Company s 28 hotels; Interstate Hotels & Resorts, Inc., manager of six of the Company s 28 hotels; Highgate Hotels L.P. and an affiliate, manager of four of the Company s 28 hotels; Davidson Hotels & Resorts and Hilton Worldwide, each a manager of two of the Company s 28 hotels; and Crestline Hotels & Resorts, Dimension Development Company, Fairmont Hotels & Resorts (U.S.) and Hyatt Corporation, each a manager of one of the Company s 28 hotels. In addition, we own BuyEfficient, LLC, an electronic purchasing platform that allows members to procure food, operating supplies, furniture, fixtures and equipment.

Competitive Strengths

We believe the following competitive strengths distinguish us from other hotel investors:

Strong Access to Capital. As a publicly traded REIT, over the long-term, we may benefit from greater access to a variety of forms of capital as compared to non-public investment vehicles.

Low Cost of Capital. As a publicly traded REIT, over the long-term, we may benefit from a lower cost of capital as compared to non-public investment vehicles as a result of our liquidity, professional management and portfolio diversification.

Significant Cash Position. As of September 30, 2013, we had $100.2 million in unrestricted cash and cash equivalents. We intend to deploy a material portion of our excess cash balance towards the repayment of maturing debt, selective acquisitions and capital investments in our portfolio. We have no debt maturities through the period ending December 31, 2014.

Flexible Capital Structure. We believe our capital structure provides us with appropriate financial flexibility to execute our strategy. As of September 30, 2013, the weighted average term to maturity of our debt is approximately four years, and 70.8% of our debt is fixed rate with a weighted average interest rate of 5.4% per annum. The weighted average interest rate on all of our debt, which includes the effect of our interest rate derivative agreements based on variable rates at September 30, 2013 is 4.9% per annum. All of our debt is in the form of single asset non-recourse loans rather than cross-collateralized multi-property pools. We believe this structure is appropriate for the operating characteristics of our business as it isolates risk and provides flexibility for various portfolio management initiatives, including the sale of individual hotels subject to the existing debt.

High Quality Portfolio.

Presence in Key Markets. We believe that our 28 hotels are located in desirable markets with major demand generators and significant barriers to entry for new supply. During the nine months ended September 30, 2013, approximately 91% of the revenues generated by the 28 hotels, including revenue generated prior to our ownership, were earned by hotels located in key gateway markets such as Boston, New York, Washington, D.C./Baltimore, Chicago, Orlando, New Orleans, Los Angeles, Orange County and San Diego. Over time, we expect the revenues of hotels located in key gateway markets to grow more quickly than the average for U.S. hotels as a result of stronger economic drivers as well as higher levels of international travel.

Upper Upscale and Upscale Concentration. The upper upscale and upscale segments, which represented approximately 93% of the hotel revenue generated by the 28 hotels during the nine months ended September 30, 2013, including revenue generated prior to our ownership, tend to outperform the lodging industry, particularly in the recovery phase of the lodging cycle. As of September 30, 2013, the hotels comprising our 28 hotel portfolio averaged 462 rooms in size, and total RevPAR was $144.18 for the nine months ended September 30, 2013.

Nationally Recognized Brands. Most of our hotels are operated under nationally recognized brands, including Marriott, Hilton, Hyatt, Fairmont and Sheraton. We believe that affiliations with strong brands improve the appeal of our hotels to a broad set of travelers and help to drive business to our hotels.

Recently Renovated Hotels. From January 1, 2009 through September 30, 2013, we invested $337.2 million in capital renovations throughout the 28 hotels. We believe that these capital renovations have improved the competitiveness of our hotels and have helped to position our portfolio for future growth.

Seasoned Management Team. Each of our core disciplines, asset management, acquisitions and finance, are overseen by industry leaders with demonstrated track records.

Asset Management. Our asset management team is responsible for maximizing the long-term value of our real estate investments by achieving above average revenue and profit performance through proactive oversight of hotel operations. Our asset management team leads property-level innovation, benchmarks best practices and aggressively oversees hotel management teams and property plans. We work with our operators to develop hotel-level master plans, which include positioning and capital renovation plans. We believe that a proactive asset management program can help to grow the revenues of our hotel portfolio and maximize operational efficiency by leveraging best practices and innovations across our various hotels, and by initiating well-timed focused capital improvements aimed at improving the appeal of our hotels.

Acquisitions. Our acquisitions team is responsible for enhancing our portfolio quality and scale by executing well-timed acquisitions and dispositions that maximize our risk-adjusted return on invested capital. We believe that our significant acquisition and disposition experience will allow us to continue to execute our cycle-appropriate strategy to redeploy capital from slower growth to higher growth hotels. From the date of our initial public offering through September 30, 2013, we acquired interests in 24 hotel properties and sold 42 hotel properties. Pursuant to our cycle-appropriate strategy, our focus shifted from acquisitions to dispositions in 2007, 2008 and for the majority of 2009 as the lodging cycle peaked and experienced a down cycle. Towards the later part of 2009 and into 2010, our focus shifted to the selective acquisition of upper upscale hotels as we entered a recovery phase in the lodging cycle. In light of increasing demand for lodging and generally limited supply of new hotel development, we believe we are currently in the middle phase of a cyclical lodging recovery. Hotels acquired during the early stages of past cyclical recoveries have benefited from multi-year increases in profitability, which in many cases created long-term value in excess of investment hurdles. Accordingly, during the past three years, we selectively acquired interests in seven hotels: the Doubletree Guest Suites Times Square in January 2011; the JW Marriott New Orleans in February 2011; the Hilton San Diego Bayfront in April 2011; the Hyatt Chicago Magnificent Mile in June 2012; the Hilton Garden Inn Chicago Downtown/Magnificent Mile in July 2012; the Hilton New Orleans St. Charles in May 2013; and the Boston Park Plaza in July 2013.

Finance. We have a highly experienced finance team focused on minimizing our cost of capital and maximizing our financial flexibility by proactively managing our capital structure and opportunistically sourcing appropriate capital for growth, while maintaining a best in class disclosure and investor relations program. We remain committed to thoughtfully and methodically reducing leverage while maintaining a focus on creating and protecting stockholder value. During 2012 and the nine months ended September 30, 2013, we reduced our total debt by $180.9 million and $99.5 million, respectively, through amortization, debt repayments and the disposition of hotels with high debt balances. In addition, in March 2013 we redeemed all 7,050,000 shares of our 8.0% Series A Cumulative Redeemable Preferred Stock for an aggregate redemption price of $178.6 million and in May 2013 we redeemed all 4,102,564 shares of our Series C Cumulative Convertible Redeemable Preferred Stock for an aggregate redemption price of $101.1 million.

Business Strategy

Our mission is to create meaningful value for our stockholders by becoming the premier hotel owner. Our values include transparency, trust, ethical conduct, communication and discipline. Our goal during what we believe is the middle phase of the cyclical lodging cycle is to improve the quality and scale of our portfolio while gradually deleveraging our balance sheet. As demand for lodging generally fluctuates with the overall economy (we refer to these changes in demand as the lodging cycle), we seek to employ a balanced, cycle-appropriate corporate strategy that encompasses proactive portfolio management, intensive asset management, disciplined external growth and measured balance sheet improvement as detailed below:

Proactive Portfolio Management. The leaders of each of our core disciplines function as a portfolio management team. The portfolio management team s purpose is to strategically maximize the long-term value of our assets by enhancing our portfolio quality and scale, optimizing our exposure to key markets, and improving the effectiveness and efficiency of our decision making. Accordingly, the team is responsible for developing a portfolio-wide strategy related to brand and operator relationships, asset quality and scale, target markets, capital investments, and portfolio capitalizations. Our portfolio strategy may also include the disposition of certain hotels.

Intensive Asset Management. Through all phases of the lodging cycle, our strategy emphasizes internal growth and value enhancements through proactive asset management, which entails working closely with our third-party hotel operators to develop and implement long-term strategic plans for each hotel designed to enhance revenues, minimize operational expenses and asset risk, maximize the appeal of our hotels to travelers and maximize our return on invested capital. We also focus on improving the appeal and growth potential of our existing hotels through internally-managed hotel renovations.

Disciplined External Growth. By gradually increasing the scale and quality of our portfolio, we may provide our stockholders with greater exposure to key growth markets, improved liquidity and broader access to value-adding transactions. Accordingly, our strategy emphasizes disciplined external growth during the recovery phase of the lodging cycle. Our external growth plan is oriented around investing in institutional-quality hotels that generate returns in excess of our cost of capital, that are additive to the quality of our portfolio, that have attractive growth potential and that may benefit from our asset management competencies. We endeavor to structure our acquisitions in ways that will not only increase the value of our shares of common stock, but will also advance our other corporate objectives, such as improving our financial flexibility and reducing our leverage. During periods of cyclical decline, our strategy may emphasize opportunistically investing in distressed assets and the repurchase of our equity or debt securities. In addition to hotel acquisitions, we may seek to grow our portfolio by making investments in defaulted and/or distressed debt positions in loan-to-own hotel transactions, utilizing our REIT structure to effect strategic combinations with select property owners, effecting portfolio purchases from institutional and other owners seeking portfolio liquidity, and by providing capital solutions to illiquid owners facing debt maturities or capital requirements.

Measured Balance Sheet Improvement. We believe that a low overall cost of capital and significant financial flexibility are very important to the successful execution of our strategy. Our balance sheet strategy is oriented toward maximizing financial flexibility especially during cyclical declines. Accordingly, our financial objectives include the measured improvement of our credit ratios, maintenance of appropriate levels of liquidity, and a gradual reduction in our financial leverage throughout the cyclical recovery phase. Our financial objectives are integral to our overall corporate strategy and, accordingly, we have developed our financial objectives in conjunction with our portfolio management and growth objectives. The lodging industry is economically sensitive. Therefore, our financial objectives are aimed at reducing the potentially negative impact of combining high operating leverage with high financial leverage, while preserving access to multiple capital sources and minimizing our weighted-average cost of capital. We seek to capitalize our acquisitions in a way that will advance our financial objectives. For example, as the measured reduction of our financial leverage is currently a key objective, we expect to fund our acquisitions with a greater proportion of equity capital than debt capital. During the mature phase of the lodging cycle, our financial objectives may include increasing our liquidity position as a means to enhance financial flexibility in the event of a subsequent period of cyclical decline. Our liquidity improvement objective may be accomplished through selective hotel dispositions, capital raises or by retaining excess cash generated by our operations.

Through our industry relationships, our knowledge and experience in both real estate and REIT issues, our extensive experience in acquiring and upgrading hotel properties, as well as our financial structuring capabilities, flexible capital structure, strong liquidity position and REIT structure, we believe we are well positioned to create meaningful value to our stockholders.

Our headquarters are located at 120 Vantis, Suite 350, Aliso Viejo, California 92656, and our telephone number is (949) 330-4000.

Recent Developments

Potential Acquisition

We are currently a party to a purchase agreement to acquire an 802-room hotel, or the Hotel, located in a gateway west coast market, in which we do not presently own any hotels. The purchase price for the Hotel is approximately $262.5 million, or approximately $327,000 per key. We will not incur or assume any debt in

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connection with the acquisition of the Hotel. For the nine month period ended September 30, 2013, the Hotel had an occupancy rate of 87.0%, an average room rate of $243.30 and RevPAR of $211.56. For the twelve months ended December 31, 2012, the Hotel had an occupancy rate of 82.5%, average room rate of $226.07 and RevPAR of $186.59. The Hotel is managed by a globally-recognized hotel brand that currently manages and franchises other hotels for the Company.

The acquisition of the Hotel is subject to satisfaction of customary conditions precedent. Accordingly there can be no assurance that the acquisition of the Hotel will close. If we consummate this acquisition, we expect to use a portion of the net proceeds from this offering to pay the purchase price. If the acquisition proceeds as planned, we currently anticipate closing in December 2013 and we expect to file the historical and pro forma financial statements for the Hotel as required by Regulation S-X Rule 3-05 within 75 days of the consummation of this acquisition.

Preliminary Third Quarter Earnings Results

The following preliminary earnings results for the quarter ended September 30, 2013 reflect preliminary results from our unaudited financial statements, and are subject to customary adjustments that may arise during the completion of the financial statement closing process. Our preliminary results include our ownership period for all 2013 acquisitions and dispositions.

For the third quarter of 2013, we expect:

Metric (unaudited)	**Preliminary Third Quarter 2013 Results (1)**
Adjusted Comparable Hotel RevPAR Growth(2)	7.6%
Net Income ($ millions)	$15 - $16
Adjusted EBITDA ($ millions)	$69 - $70
Adjusted FFO ($ millions)	$47 - $48
Adjusted FFO per diluted share	$0.29 - $0.30

(1) See Risk Factors After we complete the quarterly review process and the preparation of our financial statements for the quarter ended September 30, 2013, we may determine that our preliminary third quarter earnings results are different than the preliminary results set forth in this prospectus supplement.

(2) Reflects the expected percentage increase for the three-month period ended September 30, 2013 as compared to the three-month period ended September 30, 2012.

Set forth below is a reconciliation of the Company s third quarter 2013 preliminary Net Income to preliminary Adjusted EBITDA. The amounts below are unaudited and are in thousands.

	Quarter Ended September 30, 2013	
	Low	**High**
Net income	$ 15,200	$ 16,200
Depreciation and amortization	35,100	35,100
Amortization of lease intangibles	1,000	1,000
Interest expense	18,900	18,900
Income tax provision	400	400
Non-controlling interests	(3,300)	(3,300)
Amortization of deferred stock compensation	1,300	1,300
Capital lease obligation interest cash ground rent	(400)	(400)
Non-cash straightline lease expense	600	600
Adjusted EBITDA	$ 68,800	$ 69,800

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Set forth below is a reconciliation of the Company s third quarter 2013 preliminary Net Income to preliminary Adjusted FFO. The amounts below are unaudited and are in thousands, except per share amounts.

	Quarter Ended September 30, 2013	
	Low	High
Net income	$ 15,200	$ 16,200
Preferred stock dividends	(2,300)	(2,300)
Real estate depreciation and amortization	34,700	34,700
Non-controlling interests	(2,700)	(2,700)
Amortization of lease intangibles	1,000	1,000
Non-cash straightline lease expense	600	600
Income tax provision	400	400
Adjusted FFO	$ 46,900	$ 47,900
Adjusted FFO per diluted share	$ 0.29	$ 0.30
Diluted weighted average shares outstanding	161,400	161,400

The Offering

Common stock offered by us	20,000,000 shares
Total shares of common stock outstanding immediately after this offering (1)	182,870,062 shares
Use of Proceeds	The estimated net proceeds of approximately $271.0 million from this offering (or approximately $311.6 million if the underwriter s option is exercised in full), after deducting underwriting discounts and commissions and estimated offering expenses, will be used (i) to finance the potential acquisition of the Hotel described under the caption Recent Developments Potential Acquisition, (ii) for other potential future acquisitions and (iii) for general corporate purposes, including working capital and capital investment in our portfolio. See Use of Proceeds.
Distribution Policy	To maintain our qualification as a REIT, we intend to make distributions to our stockholders of at least 90% of our REIT taxable income (which excludes net capital gains and does not necessarily equal net income as calculated in accordance with generally accepted accounting principles). Our distributions may be comprised of cash, or a combination of cash and stock as permitted by the Code.
New York Stock Exchange symbol	SHO

(1) This number is based on 162,870,062 shares of our common stock outstanding at October 25, 2013, and does not include:

- 1,210,844 additional shares of our common stock available for future issuance under our 2004 long-term incentive plan, and 200,000 shares issuable in respect of stock options outstanding as of such date; or

- any exercise of the underwriter s option.

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RISK FACTORS

See the information under the heading Risk Factors beginning on page 9 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the SEC on February 25, 2013, which information is incorporated by reference into this prospectus supplement, and other information included in this prospectus supplement, the accompanying prospectus and reports we file from time to time with the SEC that we incorporate by reference herein for a discussion of factors you should carefully consider before deciding to invest in shares of our common stock.

There can be no assurance that the acquisition of the Hotel that we expect to finance using the net proceeds from this offering will close and, if the acquisition does not close, you will be unable to evaluate the economic merits of any other investments that we may make using the net proceeds from this offering.

We have entered into a definitive agreement to purchase the Hotel that we expect to finance using the net proceeds from this offering. Such agreement is subject to customary closing requirements and conditions and there can be no assurance that such acquisition will close. If the acquisition is not consummated, we will have broad discretion with respect to the net proceeds of this offering and cannot assure you that they will be used in a manner that is accretive to stockholders or the timing thereof.

A significant portion of our hotels are geographically concentrated in California, New York, Illinois, Massachusetts and the greater Washington D.C. area and, accordingly, we could be disproportionately harmed by economic downturns or natural disasters in these areas of the country. Should we be successful in purchasing the property that we expect to finance using the net proceeds from this offering, our hotel concentration in California would increase.

As of September 30, 2013, eight of the 28 hotels are located in California, which is the largest concentration of our hotels in any state, representing approximately 28% of our rooms and approximately 29% of the revenue generated by the 28 hotels during the nine months ended September 30, 2013. Our hotel concentration in California will increase if we purchase the property that we expect to finance using the net proceeds from this offering. In addition, as of September 30, 2013, three of the 28 hotels are located in each of the States of New York, Illinois and Massachusetts, as well as in the greater Washington D.C. area. The three hotels located in New York represented approximately 10% of our rooms and approximately 14% of the revenue generated by the 28 hotels during the nine months ended September 30, 2013. The three hotels located in Illinois represented 9% of our rooms and approximately 8% of the revenue generated by the 28 hotels during the nine months ended September 30, 2013. The three hotels located in Massachusetts represented 15% of our rooms and approximately 16% of the revenue generated by the 28 hotels during the nine months ended September 30, 2013. The three hotels located in the greater Washington D.C. area represented approximately 14% of our rooms and approximately 15% of the revenue generated by the 28 hotels during the nine months ended September 30, 2013. The concentration of our hotels in California, New York, Illinois, Massachusetts and the greater Washington D.C. area exposes our business to economic conditions, competition and real and personal property tax rates unique to these locales. In addition, natural disasters in California, New York, Illinois, Massachusetts or the greater Washington D.C. area would disproportionately affect our hotel portfolio. The California, New York, Illinois, Massachusetts and greater Washington D.C. area economies and tourism industries, in comparison to other parts of the country, are negatively affected to a greater extent by changes and downturns in certain industries, including the entertainment, high technology, financial and government industries. It is also possible that because of our California, New York, Illinois, Massachusetts and greater Washington D.C. area concentrations, a change in laws applicable to such hotels and the lodging industry may have a greater impact on us than a change in comparable laws in another geographical area in which we have hotels. Adverse developments in California, New York, Illinois, Massachusetts or the greater Washington D.C. area could harm our revenue or increase our operating expenses.

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After we complete the quarterly review process and the preparation of our financial statements for the quarter ended September 30, 2013, we may determine that our preliminary third quarter earnings results are different than the preliminary results set forth in this prospectus supplement.

The preliminary earnings results for the third quarter included in this prospectus supplement are subject to adjustments that may result from the completion of our quarterly review process and the preparation of our unaudited financial statements for the quarter ended September 30, 2013. Any such adjustments could result in changes in our prelimin