ATTACHMENT IV

As Many As 8,000 American Hotels Might Be Gone By October

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Hard times for the hotel industry mean lost revenue, lost jobs and thousands of rooms in properties nationwide that might close permanently. So what to do with the millions of square feet that will free up?

Some closed hotel rooms could economically be converted into multifamily housing, according to an Altus Group note, specifically discussing the Canadian hotel market, which has experienced its own extreme stress recently.

"While the hospitality sector struggles, demand for multi-family housing — including affordable, market rental, seniors and student housing — remains relatively robust," the note said. "Converting hotels into multi-family housing can help to meet this demand by enabling owners and investors to quickly move supply into the market."

Entrepreneurs have been converting hotels into apartments and other uses for years, but the coronavirus pandemic could create added impetus for the trend.

Los Angeles-based Repvblik has several such projects in the works in the Midwest, Building Design & Construction reports. One of its projects is the conversion of a Days Inn in Branson, Missouri, into 341 units of affordable housing, at $15K to $20K per unit to do the work.

"City councils look positively on these types of developments because they help to ease the housing and economic needs of residents," the Altus Group note says. "There is also a growing track record of conversions that demonstrate how to successfully deliver these projects."

The pandemic has hit the U.S. hotel industry hard, though there was a slight bounce in early summer. Occupancy, average daily rates and revenue per available room, or RevPAR, were all up in June compared with May, hotel industry data specialist STR reports, but all are still at their lowest levels on record for June.

Hotel profitability picked up slightly in June compared with May and April, STR also said, but the metric is still down massively (by 105.4%) compared to June 2019. Some full-service properties are breaking even at 50% occupancy, while some limited-service properties can do so at 45% occupancy.

Even so, as many as 8,000 hotels might close by the end of September, American Hotel and Lodging Association President and CEO Chip Rogers told Northstar Meetings Group. "Right now, many hotels are struggling to service their debt and keep their lights on," Rogers said.

In New York, for example, as many as 25,000 hotels might permanently close because of the pandemic, The Wall Street Journal reports, though without an estimate of the number of properties that might close. Still, that many rooms would be about 20% of the entire NYC area hotel market.

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See Also: Losses Mount For Hotel Owners Burning Through Cash As Recovery Slows

Related Topics: hotel conversion, Altus Group, American hotel and lodging association, STR research

U.S. Hotel Market Now At A Standstill

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U.S. hotel sales have dropped to historic lows, with fewer than 10 properties trading hands nationwide in April, Real Capital Analytics reports.

"We have never seen this level of illiquidity in the hotel market," RCA Senior Vice President Jim Costello wrote. "It is effectively a frozen marketplace."

The coronavirus pandemic wasn't the only factor driving the market down, he said. Sales were already dropping because of excess product in some markets and competition from companies like Airbnb.

The last time the hotel market was even close to being this slow was in 2009, when 21 properties traded, according to RCA data.

A separate survey by the Lodging Industry Investment Council, completed in late April, pointed to a wait-and-see attitude among many would-be hotel investors.

Namely, 64% of investors surveyed said they are still "cautiously underwriting" new lodging investments. But 74% are taking a wait-and-see approach at the same time.

In a March LIIC survey, only 9% of respondents said they believed the total dollar volume of U.S. hotel transactions in 2020 would drop more than half compared to 2019. In the organization's April survey, 32% said that.

Another reason for the slowdown in investment sales seems to be a disconnect between buyer and seller expectations.

"I'd say that the COVID-19 discount gap is too wide right now," Park Hotels & Resorts Chairman and CEO Thomas Baltimore said last week during the company's latest earnings call.

"Sellers would probably like to sell with a 10%, perhaps even 15% discount, depending on their individual needs," Baltimore said. "But I think buyers are looking for somewhere north of 30%, even 40%.

"So I think there's plenty of liquidity trying to get in this sector, recognizing that now is a good window to begin to build up a portfolio, but I think the gap is too wide to really expedite any sort of transaction," Baltimore said. "You should see the number of deals that have blown up here in the last few weeks."

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Related Topics: Real Capital Analystics, Park Hotels & Resorts, Lodging Industry Investment Council

Hotel News Now

Development

Pressures of pandemic slow California hotel pipeline

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Projects continue to enter and remain in California's hotel construction pipeline, but the reality of the coronavirus pandemic is that many projects will never be completed.

By Bryan Wroten
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REPORT FROM THE U.S.—California hotel development slowed over the first six months of 2020, but the full impact of the coronavirus pandemic on new hotel projects likely won't be realized for years.

The latest mid-year hotel development survey from Atlas Hospitality Group found a significant decrease in construction and openings during the first half of 2020 compared to the record-setting pace of the first part of 2019. The number of hotels under construction fell from 234 in the first half of 2019 to 194 this year, a 17.1% decrease. While the number of hotels opening so far was down by just one (35 compared to 36), the number of rooms opening was down by 22.5% (from 4,515 to 3,500).

Conversely, new projects in planning grew by 9% compared to the first half of 2019, with new rooms in planning growing by 5.7%. However, those growth figures don't tell a complete story.

California still has a healthy pipeline of hotels opening in the second half of the year, Atlas Hospitality Group President Alan Reay said. The pace may slow further this year and into 2021. Several hotel projects were completed during the first half of the year, but openings were delayed. In addition to what Atlas Hospitality normally tracks, it is now watching projects being deferred or abandoned.

Hyatt Hotels Corporation's partly built Andaz Palm Springs is now in bankruptcy, Reay said. The incomplete Hotel Indigo Coachella has been shut down. Work on the Tova Hotel in Palm Springs has also stopped. Many of these projects were in trouble or faced delays before the pandemic began, he said.

"If you're struggling to make it work in some of the best of times in the hotel business, 2018 and 2019, when you look at it today, post-coronavirus, it's just going to be impossible," he said. "We put pressure on revenue, pressure on net operating incomes and, really, your construction costs are still the same. In some instances, these projects are going to cost more to finish then what they got appraised for."

The downturn has hurt lenders as well, not just for hotels, but in retail and other product types, Reay said. If lenders start to go under, construction money will run out, leaving many projects only partially built and unlikely to get finished. Some developers now are even looking at changing the use of a property partway through construction. Depending on the build, many are looking at residential use, further reducing future supply.

Reay also noted a lack of new projects starting up. One of the main reasons is that lenders aren't even looking at financing existing hotels today, let alone new projects, he said.

"From a time standpoint, if you're not already under construction, with a construction loan in place, I really don't see people proposing new projects for the next 24 or 36 months," he said.

Developers likely won't even buy land to hold onto until conditions improve for building because holding costs become very expensive, he said. Unless the property is owned free and clear, the project likely is carrying some sort of debt.

When new projects do start up again, extended-stay hotels will likely be popular given the demand during the pandemic, Reay said. While hotels in the economy segment have also performed well, that's not something he expects to see more of in the pipeline given the cost of construction.

In the last major downturn, developers and owners still interested in hotels bought existing properties and renovated, which was well below replacement cost, he said.

"Anyone that's looking to build a convention center hotel or a resort property is going to have a really, really hard time moving forward," he said.

Developers' experiences

R.D. Olson Development has three hotel projects in the works in California, said President and CEO Bob Olson. The firm is moving ahead with deals that have long lead times and in markets that are a good long-term investment, but has dropped out of a few deals made before the pandemic started.

Financing, if available, is incredibly difficult, he said. Lenders have turned off the spigot for 99% of deals until they can figure out what's happening in their markets. The pandemic is playing out longer than anyone anticipated, but it will eventually turn around and the ramp-up should look like a typical recession recovery, Olson said.

For developers who are in early planning or about to start construction and have access to financing, this is likely the best time to develop as prices are coming down, Olson said. Timing-wise, the project would deliver in a rising market.

The combination of years of dramatic construction price increases and the staggering negative effect on revenue per available room from COVID-19 has created an extremely challenging underwriting process for new hotel construction, said OTO Development VP of Real Estate Todd Turner via email. Most hotel projects in planning across the state will be impacted, with many shifting to some other type of use.

California has a large percentage of big tech companies that currently operate in a work-from-home scenario, OTO Development CEO Corry Oakes said via email. Long term, the company believes tech employees will miss the collaboration and culture-building that comes from being together. For the short term, however, the work-from-home approach translates to reduced hotel demand, making underwriting decisions more difficult and pushing out the start of new construction projects.

"Hotel profitability has disappeared, and the resulting financial stress will wipe out a significant portion of hotel equity, forcing a change of financial ownership of many assets," Oakes said. "We believe these issues will need to work through the system before development picks up any meaningful momentum."