Hotels Are On The Upswing – But For How Long?

lending CRE

Summary: Hotels have seen their ups and downs in the past couple of years. Now, as consumers are flush with savings and ready to venture out again, hotels are seeing a welcomed burst of activity. This is good news for bankers supporting these businesses. Trepp's CMBS delinquency rate for hotels sank to 6.87% in March, a decrease of 95 basis points MoM. But the real question is — will this high level of activity continue?

In 1875, 27Y old Matthew Webb, a merchant navy captain, became the first person to swim the English Channel. While only 21 miles, the channel actually delivered 39 miles of swimming with all the currents. It took Captain Webb 21 hours and 45 minutes. His colleagues in the Navy noted that he was not the fastest swimmer, but he had endurance. That definitely paid off for him!

It seems we have all honed a sense of endurance during the pandemic. But now, many are ready to live it up. Armed with more savings and two years of vacations to make up, many people are booking trips, increasing leisure travel demand. Hotels still hurting from the lack of business travel and corporate events are more than happy to oblige these travelers. With this surge in the hotel industry, we explore what this means for banking and whether it will continue to flourish.

Loan delinquencies dip

Bankers will happy to hear that with the boost in leisure travel, hotels' loan delinquency rates are going down, as these loans convert from delinquent to current status at an outstanding pace. Trepp's CMBS (commercial mortgage-backed securities) delinquency rate for hotels sank to 6.87% in March, a decrease of 95 basis points MoM. To bring some context, when the pandemic hit, hotel delinquency reached close to 25%. While the pandemic isn't eradicated from our lives yet, life appears to be getting back to a regular rhythm.

Profitability rises

More good news. STR, a lodging analytics company, revealed that hotels' profitability has rebounded after a drop due to Omicron. Geographic hot spots like Miami and Phoenix topped pre-pandemic levels of gross operating profit per available room (GOPPAR) in February. GOPPAR rose to almost $59 from close to $20 in January.

"*Following trends in top-line performance, US profitability levels are recovering more quickly from Omicron than with previous variants,*" said Raquel Ortiz, STR's director of financial performance. "*February GOPPAR was roughly 77% of the 2019 comparable, but independents (108%), luxury (94%), and midscale (88%) chains were far above the national average.*"

Many hotels are flourishing

Right now, many hoteliers are able to charge more for rooms and still optimize vacancy rates. According to STR, hotel occupancy reached 66.9% for the week ending March 19th. The occupancy rate has not been that high since August 2021. High prices do not seem to deter travelers, as hotel room rates have risen too. The last week of March 2022 saw average daily hotel rates increase to $149.38. People are feeling more comfortable about traveling and are splurging to enjoy themselves. Some rooms have been reported to cost almost $4,000/night for high-profile events, like Formula 1 racing.

Host Hotels & Resorts Inc. anticipates that this level of leisure travel will continue through the year. CBRE agrees, as it recently adjusted its forecasted date to reach 2019's nominal level revenue per available room (RevPAR) by Q3 2022 instead of Q3 2023 – a full year earlier. Yet there are factors that could affect this upward trend.

Labor

Labor costs are still an issue. They increased over 20% in March, with $19.68 in hourly wages vs. $16.31 before COVID, according to the Bureau of Labor Statistics. The cost of labor is driven by an overall lack of labor, which has stymied many hotels from reaching full occupancy levels.

Geopolitical issues

The war in Ukraine may prevent some international travelers from traveling to the US, which could affect the vacancy and profitability of several high-end and destination hotels.

Inflation

While most people seem to accept paying more for hotel rooms right now, as hotels continue passing on their increasing costs, that acceptance may not last. Budget hotels will be the first ones to feel the effect of this, as their customers are more cost-conscious.

Overall, most analysts believe the travel surge will continue through 2022, as people are looking forward to personal travel. Yet, this leisure spending could dry up and the labor issue could worsen. Be sure to talk to your hotel owners early and often to ensure they are mitigating risks and planning for potential contingencies, so your institution will be ready for anything.

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ECONOMY & RATES

Rates As Of: 05/03/2022 01:12PM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	0.91	0.06	0.85
6M	1.45	0.04	1.26
1Y	2.14	0.04	1.75
2Y	2.77	0.05	2.04
5Y	3.01	0.05	1.75
10Y	2.97	0.04	1.46
30Y	3.02	0.02	1.11

FF Market	FF Disc	IORB
0.33	0.50	0.40
SOFR	**Prime**	**OBFR**
0.30	3.50	0.32