Ownership

IREFAC members hopeful industry will bounce back faster

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While many members of the Industry Real Estate Financing Advisory Council agreed a return to the performance levels seen in 2019 could take until 2023 or 2024, there are some signs that a rebound could come faster.

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REPORT FROM THE U.S.—Get the COVID-19 virus under control and travel demand will return. That might seem like a simple thesis, but Hilton CFO Kevin Jacobs said there is "plenty of evidence" that simple theory can hold true across the globe.

Speaking during the "Financially speaking: IREFAC insiders" session of the 42nd Annual NYU International Hospitality Industry Investment Conference webinar series, Jacobs said there is optimism looking at countries like China.

"I think you can take your cues from some of the places in the world, particularly China, where the virus has been controlled," he said. "I think we've seen plenty of evidence that there is and will be demand for travel."

He said the U.S. will eventually see a return to normal, but that's reliant on having "people be confident they can travel again."

Michael Medzigian, chairman and managing partner for Watermark Capital Partners, said he expects his company's portfolio of urban and resort properties will return to 2019 revenue-per-available-room levels in 2023.

"The bottom-line (net operating income) (probably won't return) until 2024, in nominal dollars," he said. "I think it will be three or four years, and I think that got de-risked a little bit when they announced the vaccine."

Gilda Perez-Alvarado, CEO of the Americas for JLL Hotels & Hospitality, said most are now underwriting a return in that timeframe. But in the interim, bargain hunters in the market for hotels are likely disappointed with what's actually been available on the market.

"We are not seeing the deep discounts that we all anticipated at the beginning of the crisis," she said.

Perez-Alvarado said investor sentiment has seen a marked improvement since the news broke that Pfizer's trials of a COVID-19 vaccine yielded 90% efficacy.

Hodges Ward Elliott President Mark Elliott said his company is currently underwriting deals with a 2023 return to 2019 performance.

2022 poised for a group comeback

While much of the early prognostications points to either 2023 or 2024 being the point where the hotel industry could see a full recovery with large groups the last to come back, Elliott said there are signs that 2022 could be stronger than expected.

He said he's seeing signs that big groups could returning that year, specifically.

"As I start to talk to owners of 1,000-room hotels, their '22 bookings are accelerating fairly quickly," he said. "I talked to one owner yesterday where they need 180,000 rooms at their 1,000-room hotel for group, and in 2022, they already have 140,000 on the books. In 2023, they already have 145,000 booked."

Co-moderator Jon Bortz, president, CEO and chairman of Pebblebrook Hotel Trust, asked whether that outlook assumes there is no long-term "structural damage" to group and business transient demand, and Elliott said so far he's seen more resilience in the broader economy than he expected.

"I'm stunned at the performance of the S&P 500 in the last couple of quarters, which is a positive sign," he said.

Christopher Jordan, EVP for Wells Fargo Bank, agreed there is hope for a quicker-than-expected comeback.

"I think 2022 could be a very good year, actually," he said.

A big hurdle remaining for the hotel industry, from his perspective, will be the need to get office occupancies back up to "sustain corporate transient demand."

"Until major companies, like mine quite frankly, feel comfortable moving out of this remote work configuration, whether it's a rotation or everyone comes back, you'd say that has to happen before corporate transient comes back," he said.

Asked whether his company is looking to scale back the amount of capital it sinks into the hotel industry, Jordan said they haven't even had the chance to consider such changes yet.

"We really haven't had the mental moment to think that through and crystalize our thoughts around lending to this industry," he said. "We've been so consumed with the day-to-day challenges and just working with clients and stabilizing loans. That hasn't allowed for a lot of quiet time to think about the future."

But he said there will "clearly" be an aftermath associated to a greater perceived risk for hotels from bankers "for some time."

Medzigian said it might be too early to answer what the long-term changes for large groups and business demand will be.

"I think we don't understand yet what the structural issues are," he said. "We tried to buy a great portfolio, so I feel confident it comes back, but how many people are going to stay remote? And is it really a bad thing for us if you're working remote? … Will 10% of the population going to remote work necessarily hurt us? And how many hotels are going to come out of the supply?"

Bortz asked if a "more distributed workforce" could actually bolster demand for group and small meetings.

Hilton's Jacobs said he that might be the case, and he added Hilton officials have learned some functions of jobs even within their corporate structure can be done remotely. But that's not necessarily a bad thing for hotels.

"What that means probably in the long run is low-value travel and less productive interactions get replaced with more productive interactions," he said. "Meetings might be hybrid forever, but that just makes the meeting bigger. I think most people who run these events are thinking about hybrid as an opportunity to sell more badges."

Clawing back from the depths

The ongoing crisis has taught some in the industry that the best-positioned businesses and hotel portfolios still face a greater degree of risk than any had considered before. Medzigian compared the business effects of the pandemic to "a train that came at us so fast."

"There was nothing we could do to stop it. We effectively saw something like 90% to 100% of our revenue gone overnight," he said.

That's something any business quite simply isn't built to survive, Jacobs noted.

"Our revenues went down 90% virtually overnight as well, and we couldn't take our expenses down 90%," he said.

He noted that many owners don't understand that brands are feeling that same pain even as they're asset-light.

"Our system is a giant co-op that's funded based on contributions from owners that are paid as a percentage of revenue," he said. "So overnight, we were burning just as much cash as everybody else was. I think it's important to remember for the people on the other end of the line that a lot of our businesses are similar in that regard, and no business can be or should be expected to operate at 10% of their pro forma revenue."