Impending U.S. hotel debt maturities and implications for transactions

U.S. Hotel Capital Markets Research

JLL SEE A BRIGHTER WAY

Research

United States

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jll.com

Our methodology

JLL's report examines all single-asset, hotel securitized loans nationwide, as well as in the top-25 markets (as defined by STR). The objective is to assess the level of financial stress that is likely to occur as these loans come due at their impending maturity date. To evaluate, JLL recalculated the debt service coverage ratio (DSCR) for loans maturing between 2024 and 2032 with the assumption that they will refinance. The calculations assume refinancing at an interest rate of 7.7% for fixed rate loans and 8.3% for floating rate loans, which reflect the average securitized debt interest rates as of Q1 2024. Using the new DSCR calculations, JLL categorized each maturing loan as either "critical stress" (DSCR less than or equal to 1.0), "moderate stress" (DSCR between 1.0 and 1.25), or "healthy/stable" (DSCR greater than or equal to 1.25). This analysis was also carried out for the top-25 markets as well as for institutional-quality SASB product to determine the extent of financial stress faced by maturing debt in 2024. By using this methodology, JLL aims to reveal the true level of financial stress associated with the upcoming "wall of maturities" in both the broader U.S. and the top-25 markets, as well as for institutional-quality hotels.

Key findings

1 U.S. hotel profitability lags pre-Covid levels, particularly in top gateway markets, posing a challenge for loan maturity extensions and refinancings, thus making transacting a strong exit strategy.

2 Persistently high interest rates are exacerbating financial stress for owners & investors facing impending debt maturities, compelling them to consider transacting.

3 Record-high property insurance costs are lowering hotel cash flows, primarily in top gateway markets, making refinancing a challenge for maturing debt.

4 $4.2 billion in maturing debt volume in 2024 will face critical stress in the current debt cost environment and catalyze transactions through the balance of 2024.

5 Over the next five years, $2.2 billion of institutional quality, hotel SASB loans will face critical stress, and present a short-term opportunity for investors to acquire higher-quality assets in prime locations.

6 21 of the top-25 U.S. markets that refinance at maturity in 2024 will observe moderate to critical stress, totaling $2.1 billion in debt volume. Expect top gateway markets to drive increased hotel transactions.

Executive Summary

$5.8 billion of U.S. hotel single-asset securitized loans, including CMBS and CRE CLOs are coming due for maturity in 2024. Despite the U.S. hotel industry demonstrating strong RevPAR performance, there are multiple headwinds that could impede the refinancing of these securitized loans and compel owners to transact instead. These headwinds include the lagging profitability of U.S. hotels, persistently high interest rates, and historically-high costs of property insurance.

As such, if the looming $5.8 billion "wall of maturities" in 2024 were to be refinanced at today's interest rates, then a significant $4.2 billion of the total volume would be under critical stress, evidenced by a debt service coverage ratio falling at or below 1.0. This represents 71.4% of total maturing debt volume in 2024 that would not generate sufficient net operating income to cover debt service. With the amount of maturing debt in critical stress expected to decline over the next few years, the opportunity to invest in the dislocation is now.

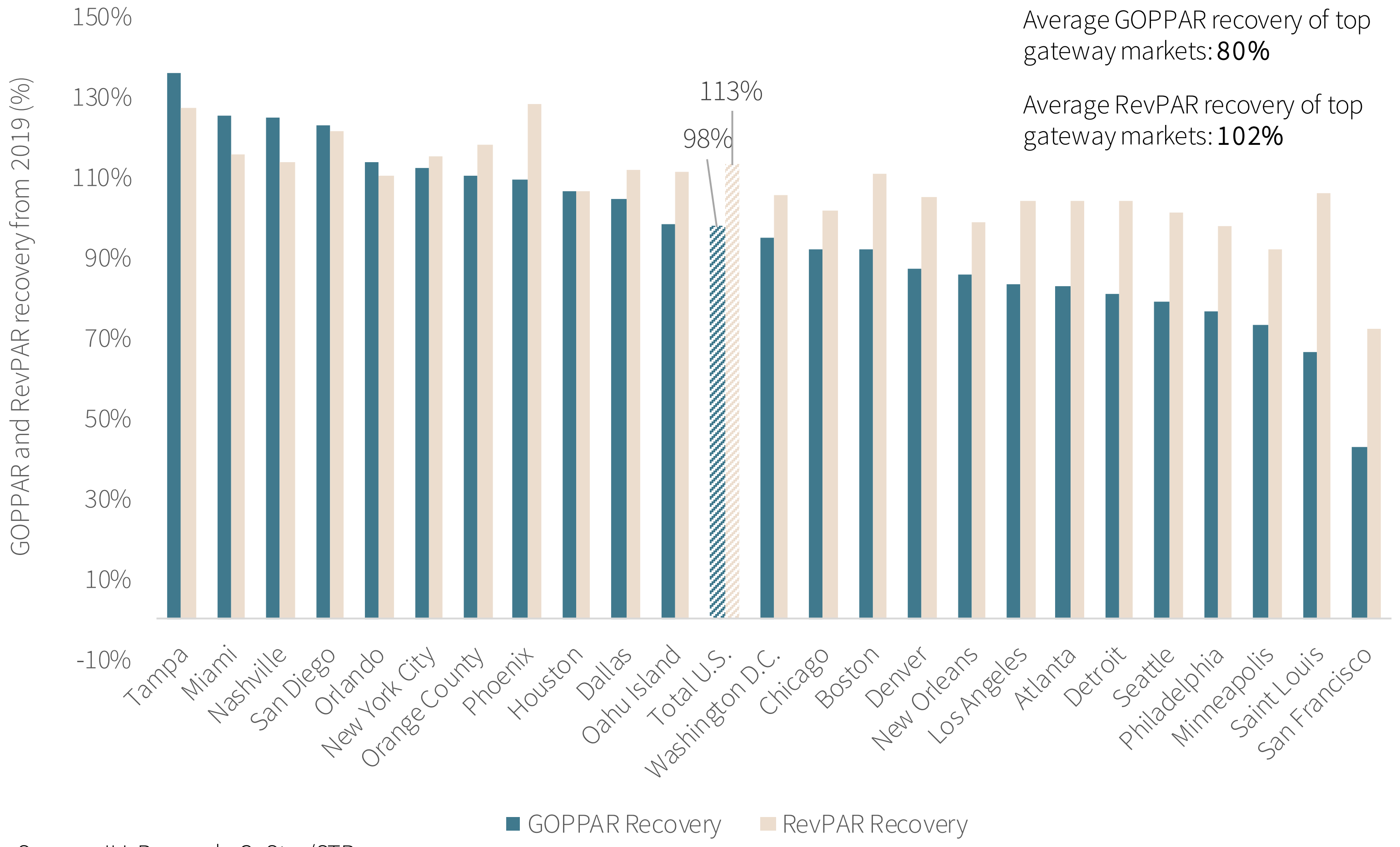
Expect these loan maturities to predominantly catalyze transactions in top gateway markets as they observe the highest concentration of debt in moderate-to-critical stress if refinanced at maturity in 2024.

U.S. hotel profitability lags, particularly for the top gateway markets, posing a challenge for loan maturity extensions and refinancings.

U.S. hotel RevPAR surged in 2023, exceeding 2019 levels by 13.2%. This growth was primarily driven by robust domestic leisure demand, as well as the early returns of some business and group travel. Despite this strong top-line performance, profitability has remained elusive in markets heavily reliant on the recovery of international, business, and group demand. These markets are also grappling with high labor costs, increasing property taxes, and other operational expenses. The impact is particularly evident in the top gateway markets, where GOPPAR is an average of 20% lower than 2019 levels. GOPPAR recovery in the top gateway markets is also behind the overall nation by 12 percentage points.

With the added financial strain of elevated debt costs and renewed PIP requirements, look for markets lagging in profitability to face challenges extending their loan maturities via refinancing and pursue transactions as a strong exit strategy.

2023 U.S. and top-25 market hotel RevPAR & GOPPAR performance indexed to 2019



Source: JLL Research, CoStar/STR

Note(s): Data is as of year-end 2023. GOPPAR = Gross operating profit per available room. Las Vegas has been omitted from the analysis due to its high concentration of casinos and differences in profit reporting. Gateway markets include NYC, DC, Chicago, Boston, LA, SF, and Seattle.

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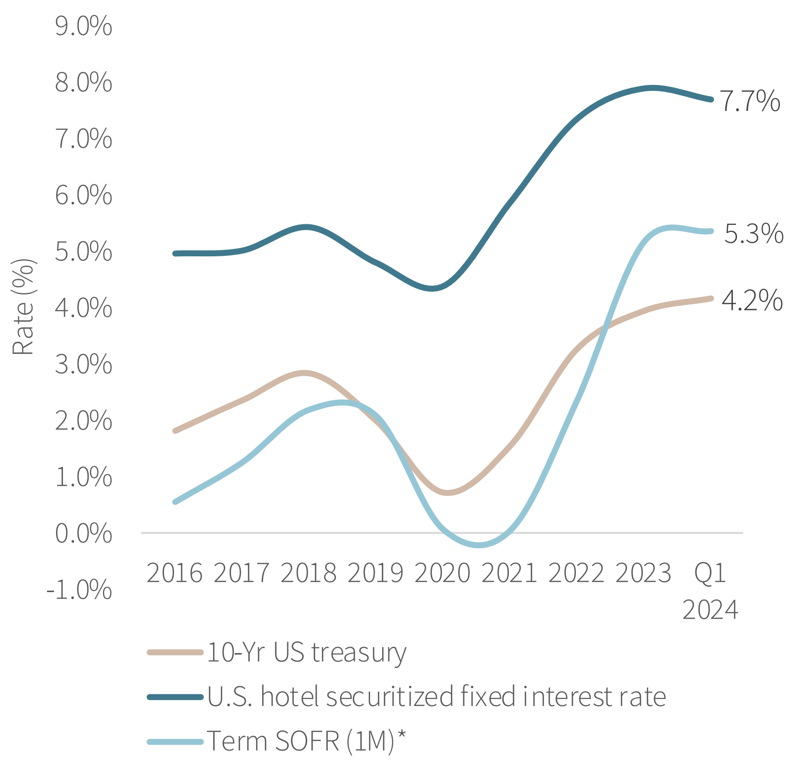
Persistently high interest rates are exacerbating financial stress for owners & investors facing impending debt maturities, compelling them to consider transacting.

With $5.8 billion worth of hotel securitized loans approaching maturity in 2024, borrowers are faced with the decision of either refinancing or selling their assets. However, given today's environment of persistently high interest rates, refinancing is a less attractive option for borrowers. Since 2020, average fixed interest rates for U.S. hotel securitized loans have increased by 332 basis points, reaching 7.7% in Q1 2024. And for floating rate loans, the average is 8.3%. These interest rates are expected to remain at elevated levels, as 10-year U.S. treasury, 1-month SOFR, and hotel securitized interest rates have stabilized at or near all-time highs from 2023 to Q1 2024.

The U.S. Federal Reserve's ongoing policy of maintaining restrictive rates for a longer period is expected to underpin these elevated rates through the year. Consequently, borrowers facing impending loan maturities will find refinancing to be an unfavorable option, compelling them towards considering transaction opportunities instead.

Given this "higher for longer" interest rate backdrop, owners are more likely to explore transactions rather than refinance their existing loans.

Average U.S. hotel securitized debt market interest rate by origination year vs benchmark rates



Source: JLL Research, Trepp, FRED
Note: Data is as of March 2024 and pertains to single-asset U.S. hotel securitized loans (CMBS & CRE CLOs) with fixed and floating interest rates by origination year. Las Vegas has been omitted from the analysis due to its high concentration of casinos and differences in profit reporting. Benchmark rates and securitized debt interest rates have been annualized.

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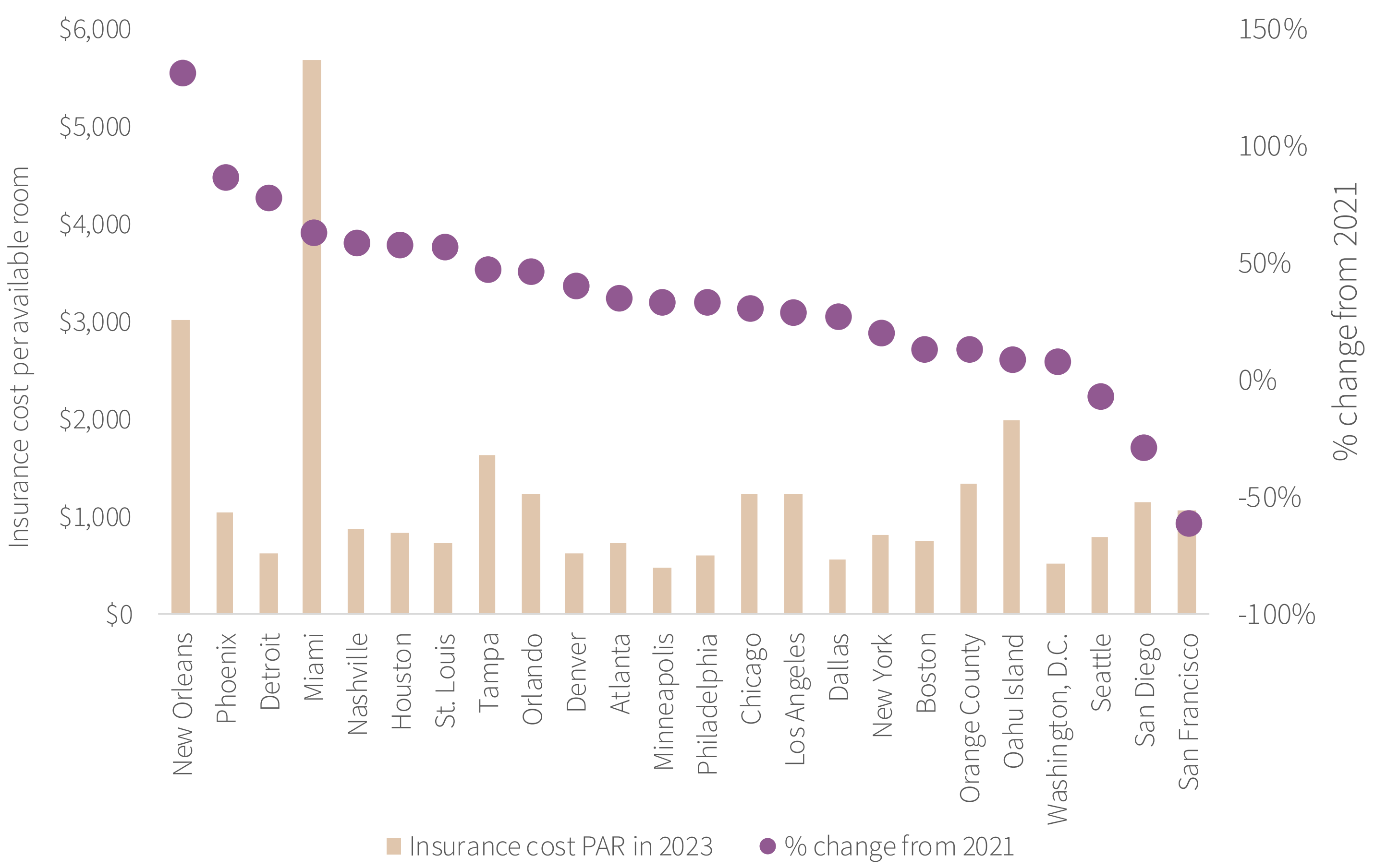
Record-high property insurance costs are lowering hotel cash flows, primarily in top gateway markets, making refinancing a challenge for maturing debt.

The historic growth in property insurance costs poses a significant challenge to hotels, disrupting their cash flows and elevating their credit risk. This is especially pronounced in gateway markets situated along the coast, which are highly exposed to climate-related risks.

Among the top-25 markets, in 2023, New Orleans witnessed the highest surge in property insurance costs compared to 2021 at 131%. Other top gateway markets including Miami, Los Angeles, Chicago, New York, and Boston also experienced double-digit growth in insurance costs. These escalating expenses directly impact hotels' cash flows, making it more challenging for these hotels to meet their debt service obligations.

The financial strain posed by rising insurance costs will encourage owners to consider transactions in the face of impending maturities, particularly in top gateway markets.

U.S. hotel insurance cost per available room (PAR) by top-25 market in 2023



Source: JLL Research, Costar/STR
Note(s): Data as of year-end 2023 and is the most recent data available.

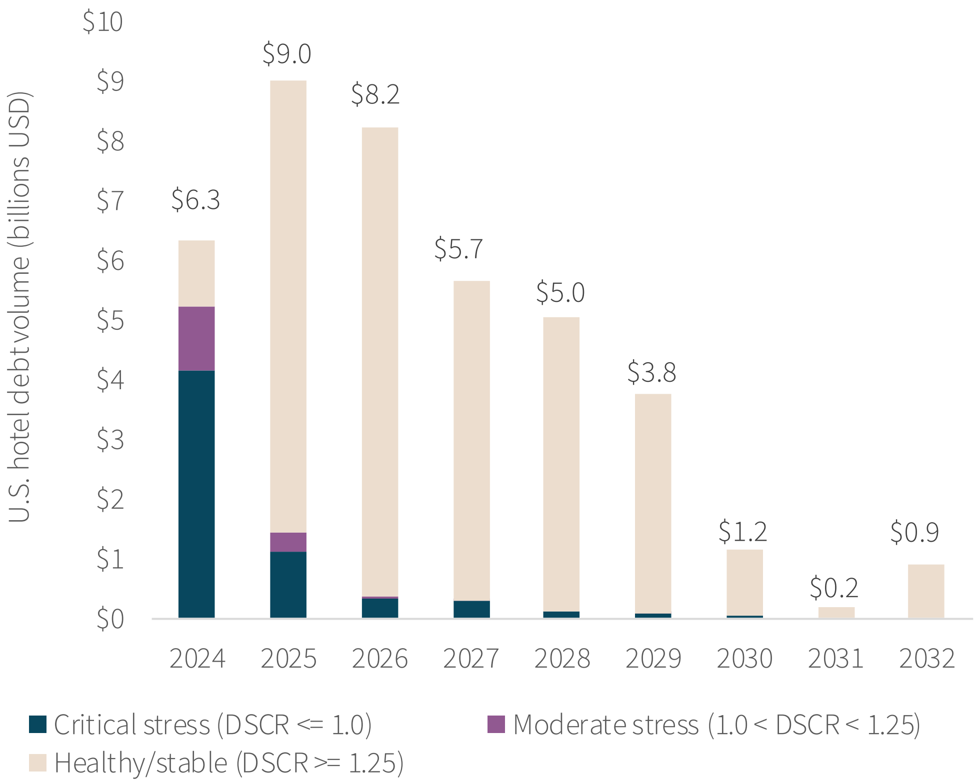
$4.2 billion in maturing debt volume in 2024 will face critical stress in the current debt cost environment and catalyze transactions in the near-term.

By the end of 2024, $5.8 billion worth of U.S. hotel securitized loans will come due for repayment, requiring full payment, refinancing, extension, or sale. However, if these loans were to be refinanced at current interest rates, a large majority of them would struggle to generate enough income to cover their debt costs. In fact, 71.4% of these maturing loans will be in critical stress, where their debt service coverage ratio will fall below 1.0. This indicates that these loans will be unable to generate sufficient net operating income to meet their debt obligations.

The number of maturing loans in critical stress is expected to decline over the next few years, decreasing from 145 loans in 2024 to just 9 by 2028. This presents a short, near-term window of opportunity for investors to take advantage of the market dislocation.

As such, look for these debt maturities in critical stress to drive U.S. hotel transactions through the balance of 2024.

Maturing debt volume by DSCR level, (after refinancing*)



Maturing debt in critical stress

	Total loans	Total volume $B
2024	145	$4.2 B
2025	65	$1.1 B
2026	15	$0.3 B
2027	20	$0.3 B
2028	9	$0.1 B

Source: JLL Research, Trepp; DSCR = Debt service coverage ratio. Note(s): Data is as of March 2024 and pertains to single-asset U.S. hotel securitized (CMBS & CRE CLOs) loans that are maturing over the next five years. Las Vegas has been omitted from the analysis due to its high concentration of casinos and differences in profit reporting. Hotels that have no data reported (or data that is out of date) have been excluded.
*Average DSCR at refinancing has been calculated based on an interest rate of 7.7% for fixed-rate loans and 8.3% for floating–rate loans.

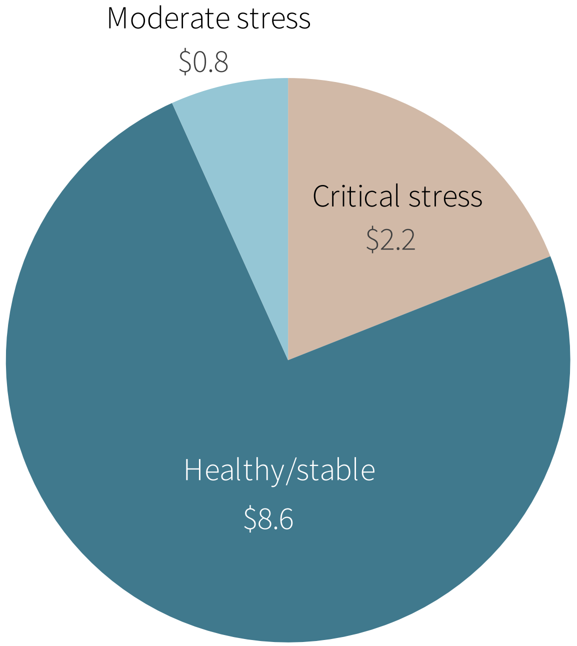
Over the next five years, $2.2 billion of institutional quality, hotel SASB loans will face critical stress and present a short-term opportunity for investors to acquire higher-quality assets in prime locations.

Over the next five years, a significant opportunity is emerging for well-capitalized investors as approximately $2.2 billion worth of institutional quality hotel SASB loans are projected to face critical stress. This presents a near-term opportunity for investors to acquire high-quality hotel assets.

Institutional quality hotels are typically higher-quality, full-service hotels, located in prime locations. Lenders often prefer these types of hotels for single-asset single-borrower (SASB) loans due to their strong demand drivers and solid financial performance. These locations often experience high demand from both business and leisure travelers, resulting in higher occupancy rates and stronger financial performance. By acquiring these assets, investors can position themselves to benefit from the continued growth of these markets.

With the concentration of maturing institutional quality hotel debt expected to encounter critical to moderate stress exclusively in in 2024 and 2025, this represents a short-term investment opportunity for investors to acquire higher-quality assets in prime locations.

Total U.S. hotel SASB debt volume maturing between 2024 and 2028 (in billions USD)



Source: JLL Research, Trepp, FRED
Note(s): Data is as of March 2024 and pertains to U.S. hotel single-asset single-borrower (SASB) loans that are maturing over the next five years. Las Vegas has been omitted from the analysis due to its high concentration of casinos and differences in profit reporting. Hotels that have no data reported (or data that is out of date) have been excluded. *Average DSCR at refinancing has been calculated based on an interest rate of 7.7% for fixed-rate loans and 8.3% for floating–rate loans.

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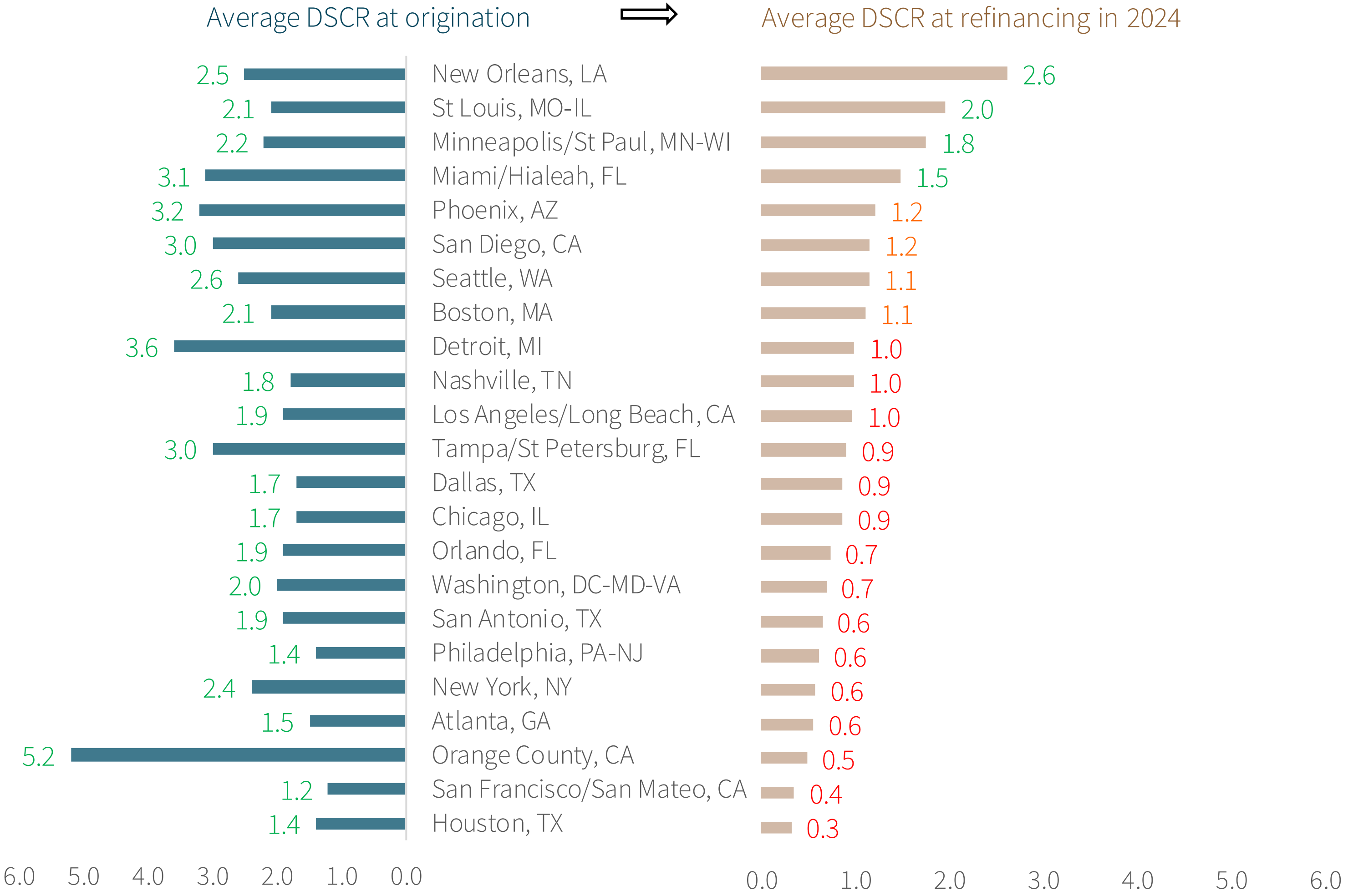
21 of the top-25 U.S. markets that refinance at maturity in 2024 will observe moderate to critical stress, totaling $2.1 billion in debt volume.

Profitability challenges are significantly impacting hotels in top gateway cities, leading to concerns about their financial stability. In 2024, 21 of the top-25 U.S. markets are expected to face moderate to critical stress when refinancing their loans upon maturity, totaling $2.1 billion in debt volume. This suggests that they will not be able to generate sufficient income to cover their debt obligations. Primary markets affected include San Francisco, Los Angeles, New York, Washington D.C., Chicago, Seattle, and Boston. In these gateway markets, the debt service coverage ratios are below 1.25.

In the face of moderate to critical stress upon refinancing at maturity in 2024, these top gateway markets are likely to drive increased transaction activity.

Average DSCR across U.S. top markets, at origination vs. at refinancing in 2024



Source: JLL Research, Trepp; DSCR = Debt service coverage ratio. Note(s): Data is as of March 2024 and pertains to single-asset U.S. hotel securitized loans that are maturing in 2024. Hotels that have no data reported (or data that is out of date) have been excluded. Las Vegas has been omitted from the analysis due to its high concentration of casinos and differences in profit reporting. No loans in Denver, CO are maturing in 2024. Average DSCR at refinancing has been calculated based on an interest rate of 7.7% for fixed-rate loans and 8.3% for floating–rate loans.

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Glossary

Conduit/CMBS

Type of CRE mortgage loan backed by a diverse selection of other mortgage loans that are packaged and sold to investors.

CRE Collateralized Loan Obligation (CLO)

Single security backed by a pool of CRE debt in which the individual borrowers make payments to the company that pooled the loans.

Debt service coverage ratio (DSCR)

A financial metric used to assess the ability of a borrower to cover their debt obligations, specifically the interest and principal payments, using the income generated from the property. This is calculated by dividing the net operating income by total debt service.

In this report there are three categories of DSCR:

Critical Stress	Moderate Stress	Healthy/Stable
DSCR <= 1.0	DSCR is between 1.0 – 1.25	DSCR >= 1.25

Extensions

Loan maturity extensions refer to agreements between lenders and borrowers to extend the maturity date of a loan beyond its original term. This is initiated when the borrower is unable to repay the loan at its original maturity date.

Fixed or Floating Rates

A floating rate, refers to an interest rate that can change over time. Unlike a fixed rate, which remains constant for the duration of a loan and is tied to a benchmark index.

Gross Operating Profit per Available Room (GOPPAR)

A per room measure of a hotel's profitability by dividing the gross operating profit (revenue minus expenses) by the number of available rooms.

Refinancing

The process of replacing an existing loan with a new loan that has different terms to obtain better interest rates, payment terms, etc.

Securitized Debt Maturity Date

The date in which a securitized debt instrument is set to mature or expire, and all principal and interest payments associated with the securities must be repaid to the investors..

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Research at JLL

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