MARKET REPORT

HVS Webinar: Higher Interest Rates are Here to Stay but the "Old Normal" will Come Back

JULY 6, 2023

In the latest of HVS's series of webinars, 425 attendees heard a topical discussion from a line-up of expert speakers on the current status of debt finance within the Hotel sector.

We were delighted to welcome 425 delegates to our webinar on **The Status of Hotel Debt Finance** on Wednesday 5 July, hosted by HVS in conjunction with Bird & Bird, AlixPartners and EP Business in Hospitality.

Tim Barbrook of HVS Hodges Ward Elliott and **James Salford** of Bird & Bird led off with a detailed presentation, explaining how we have got to where we are now, focusing on the impact of inflation and its effect on interest rates, and predicting what the future holds. They commented that lenders are now tending to focus their support on budget / limited service and luxury hotels. Interest cover ratios (ICRs) and loan to value ratios (LTVs) are under pressure but alternative lenders have also emerged. Transaction activity has slowed down but hotels are now seen as a mainstream asset class. However, they expect several borrowers to default in the next two years; their loans will at least require refinancing or they will have to raise new finance. So they predicted there will be some distress, but more likely "soft enforcement" by lenders will prevail as opposed to formal insolvency. Interest rates are expected to get worse before they get better and are not forecast to return to their previously low levels. Higher interest rates are here to stay, the "old normal" will come back and hotel values are likely to fall, they concluded.

Graeme Smith of AlixPartners then moderated a lively panel session comprising representatives from three traditional banks and two alternative lenders. We learned that **Bob Silk** of Barclays is "very old" and has "seen all of this before". He nevertheless stressed the importance of cash flow projections as opposed to LTVs. **Theo Hajoglou** of Cheyne Capital stressed the importance of sponsors' reputations, whilst **Dan Williams** of Virgin Money is focused on debt serviceability and interest cover as key metrics. **Paola Orneli** of Aareal Bank confirmed that her bank's underwriting is currently based more on a hotel's performance in the absence of transactional evidence, and commented that Aareal's average LTV was around 56%; and that, in common with most of the panel, ICRs are currently significantly below 2x. **Callum Laithwaite** of Starwood Capital confirmed his company's focus is on luxury hotels and the domestic UK market, with mostly refinancings.

With regard to lending for new hotel development there was general acceptance but on a case-by-case basis. (Call me a cynic but I took this to mean that most decisions are likely to be negative.) Bob Silk however summed up hotel development finance succinctly – "Customers need to have deep pockets and lots of development experience."

Watch the full discussion below:

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