[Join Our Email List]

RobertDouglas MARKET INTELLIGENCE. CAPITAL SOLUTIONS

ROBERTDOUGLAS MARKET PULSE
APRIL 20, 2020

Those of us in tourism have been the front-line troops in this global battle against the coronavirus. Our industry was the first to feel the full force of the crisis and its accompanying economic shock, but the battle is far broader now and is affecting industries that are larger and more capital-intensive than the hotel investment world. In our third edition of the RobertDouglas MarketPulse we look not only at the hospitality industry but also at data and trends we are seeing in a few key sectors.

Banking

% Loans by Category	Wells Fargo	Bank of America	JPMorgan Chase	Citigroup	U.S. Bancorp	Top 5 Total
Commercial Loans	37%	45%	32%	44%	35%	39%
Residential Mortgages	34%	28%	30%	16%	28%	28%
Credit Card Loans	4%	10%	16%	23%	8%	12%
Commercial Real Estate Loans	16%	6%	12%	8%	15%	11%
Consumer Loans	9%	10%	10%	9%	15%	10%
Total Loans Outstanding	*100%*	*100%*	*100%*	*100%*	*100%*	*100%*

"Why do we always start with banking," you ask? Because, as Willie Sutton was once reported to have said, **"that's where the money is."** JP Morgan, Wells Fargo, Bank of America Merrill Lynch and Citi all announced **Q1 earnings this week that were down 40% or more**, and we expect Q2 to be worse. They also announced billions of dollars in reserves for bad loans. To date, the banking sector has been a strong anchor in rough seas. That anchor's hold is going to be tested in the coming months as more sectors come under pressure.

Airlines: Slashed Schedules and Mothballed Planes

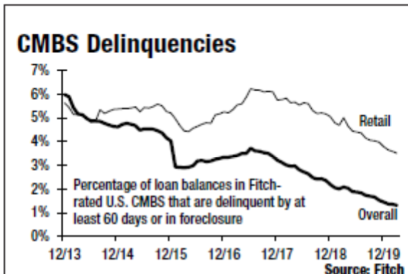
In the past few weeks, roughly **100,000 Americans** boarded a plane each day. In April of 2019 by comparison, daily traffic never dipped below **2,000,000 passengers,** a drop in demand of more than 95%. The Transportation Department has responded to this crisis by allowing airlines to reduce flights by **up to 90%** and still retain control of routes and gates. What does this mean in real terms? United Airlines has cut flights to its giant Newark hub from **400 to 15 flights** and American Airlines has cut flights to NY area airports from **260 to 13 flights,** and those reductions are being mirrored across the nation**.** Unfortunately, those schedules cannot be restored overnight. It may take months for those fleets to fully come back on line given the maintenance and safety requirements that must be met (*for more on that, airplane geeks can google, "where airlines store grounded planes in a pandemic*"). The silver lining is Delta and American are accelerating the **retirement of their oldest planes**.

Retail: There's Supermarkets and Amazon, and There's Everything Else

Thank God for all those amazing grocery, warehouse, distribution and agricultural workers who are keeping our nation fed, but when you get beyond the supermarkets and pharmacies, retail is a mess. The latest sales figure showed retail sales **down a record 8.7% in March,** the largest drop since data started being **collected in 1992**. We know that figure understates the real pain since most stores operated more or less normally through February.

Finally, the decline is really a tale of two cities: grocery stores and everybody else. Grocery sales **were up 26.7%** while sales at clothing and accessory stores **plummeted 51%**, home furnishing sales **dropped 27%**, sporting goods sales **fell 23%** and electronics sales **declined 15%.**

Roughly **one-in-four U.S. jobs** are tied to retail and consumer spending comprises roughly 70% of economic growth in the country. Like the hotel industry, most retail properties across the industry are shuttered other than those with a grocery store or pharmacy. The job loss in retail exceeds that in the hotel industry **and the $30B drop in market cap** of **Simon Property Group** alone exceeds the combined market cap of the hotel REIT industry.

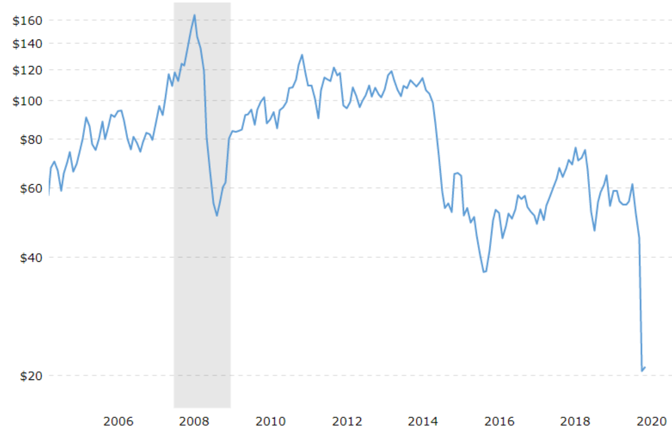


	March (%)	Month Earlier (%)	Year Earlier (%)
Retail	3.51	3.59	5.00
Hotel	1.44	1.51	1.65
Office	1.29	1.33	2.56
Mixed-use	0.86	0.85	1.66
Multi-family	0.41	0.41	0.51
Industrial	0.25	0.32	0.96
Other	0.68	0.66	0.63
OVERALL	**1.31**	**1.35**	**2.08**

CMA

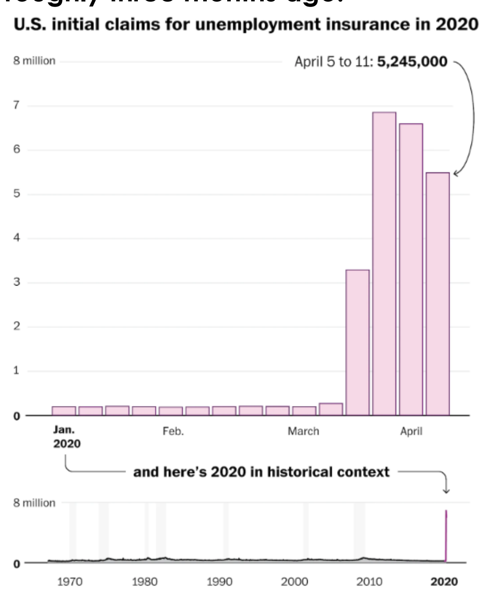
Oil & Gas: Giving New Meaning to the Word "Volatility"

You asked for it - the world delivered. **A barrel of oil is officially the same price as a cocktail in Manhattan.** With demand now at historic lows, oil at **$20 a barrel**, and the 713M barrel Strategic Petroleum Reserve already at 90% of capacity, the upstream pressure on oil and gas fields is enormous. One major oil field service company in **Houston announced 6,000 job cuts** earlier this week and the expectation is that the industry is going to have to continue shrinking. The energy business is both a big employer and a big user of capital. The industry has **more than $200B** of loans outstanding and the pain from defaults will fall disproportionately on the energy-heavy regional banks in Texas, Oklahoma, Kansas and Colorado. Between **2014 and 2015,** oil prices dropped in half to roughly **$50/bbl** and **114 energy companies filed Chapter 11**. The next wave of BK's is just heating up.



Crude Oil Prices since 2005

While we remain cautiously optimistic, the statistics being reported are something we never anticipated when we rang in the New Year roughly three months ago:



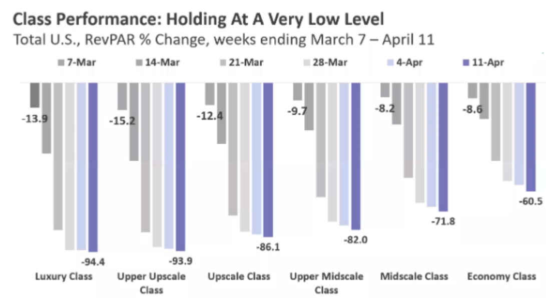
Washington Post

- **Institutional hotel asset managers** have confirmed that they have closed roughly 85% of the hotels in their portfolios and of the 15% still open, 25 and 50 percent are doing purely corona-related business
- **Trepp reports** that 21 of the 24 largest loan portfolios referred to special servicers are hotel portfolios
- **The U.S. Department of Labor** reported that the deluge of jobless claims has continued. 5.5 million new claims were made for the week ending April 11th bringing the four-week total to a stunning 22 million, or 13% of the U.S. workforce
- **US Travel Industry** is projected to lose $400 billion in 2020, approximately seven times the impact of 9/11 and GDP is expected to fall 5.7% in 2020
- **Carnival Cruise Lines ,** the world's largest cruise line, raised $4 Billion of senior secured notes with a coupon of 11.5% and closed its offering of 72 million shares of common stock at $8
- **Walt Disney World** in Florida announced its plans to furlough about 43,000 workers after it closed last month due to the coronavirus
- **Sonder ,** a billion-dollar apartment-rental startup labeled a hospitality industry disruptor, has furloughed one-third of its workforce, or 400 people
- **Danny Meyer's Union Square Hospitality Group** laid off 2,000 employees, nearly 80% of its workforce
- **Baird Hotel Stock Index (HNN):** -42.1% YTD

The State of Play in Hospitality or "Wait, What?!"

STR year-over-year stats for the week ending April 11th, 2020 (data from STR):

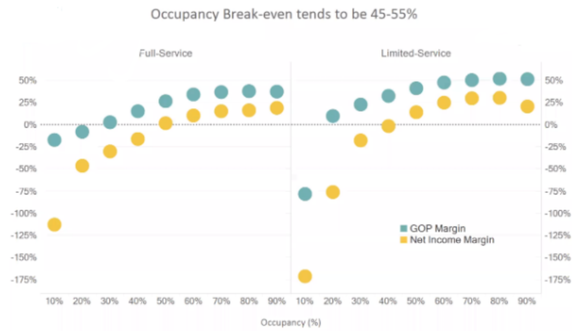
- **US RevPAR fell -83.6%** , the largest drop in STR history - STR expects declines in the 80 - 90% range to become the new norm for the foreseeable future
- **Class Performance:** Luxury and Upper Upscale properties have experienced the steepest RevPAR declines, 94.4% and 93.9%, respectively. **But, we are still selling rooms, less than 1 million per day**



- **For the last 4 weeks, all 645 STR submarkets** experienced RevPAR decline

- **New York City** saw a slight increase in occupancy from 14.2% to 18.3%, largely attributable to first responders including doctors, nurses, etc.. Interestingly, a completely unscientific survey of NY hotels (HotelTonight) suggests that hotels in the Financial District are holding up a bit better than Midtown, with room rates being quoted in the range of $149 - 179 versus Midtown's range of $79 - 109
- **Break-Even Occupancy**, which will strongly impact when hotels decide to re-open, is estimated by HOST to be 40-55% depending upon the nature of the hotel (limited service vs. full service, etc.)

Who Are the Buyers of Hotels Today?

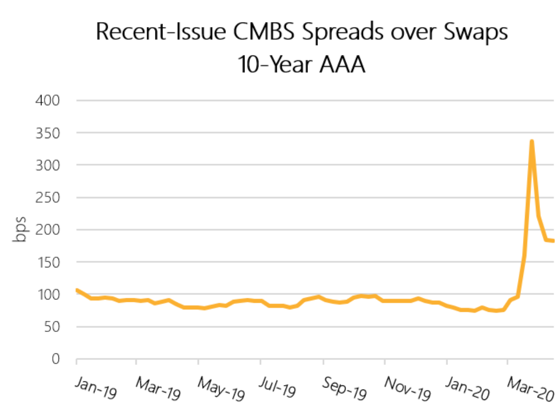


Everyone thinks they know the answer to this question..."private equity funds, of course." It seems like the obvious answer and yet our very recent experience in the market suggests a more nuanced answer.

Private equity funds are definitely prowling the market, an d they will be the dominant buyers of **portfolios that require truckloads of equity**, large teams to evaluate properties and a willingness to deal with complex financial/legal structures. They will also be active in the structured finance markets buying **CMBS securities**, mezzanine and whole loans. However, we are seeing a surprising number of **high net worth family offices** and private strategic investors partnered with new hotel brands wading resolutely into the market. These investors don't see the current environment as **"an opportunity to be vultures."** Rather, they see an opportunity to buy solid properties at prices that are a steep discount to their peak value but higher than the private equity funds can justify. We saw the same phenomenon in the early 90's when private investors like **Prince Alwaleed, Kwek Leng Beng, and Great Eagle** accumulated large urban portfolios in the gateway markets of North America and Europe. The difference today is that the capital is domestic and is willing to buy across the continent, including resorts and independent hotels.

Debt Capital Markets Update

New York Life's motto **"We were built for times like these"** is a testament to that 175 year old company, but it can also be applied to much of the finance industry. In a time of unprecedented challenges, lenders of every kind appear to be working steadily towards solutions.



The undertone in the market is that nobody is looking to punish borrowers for something that was not their fault. Master servicers are stepping up to bridge payments to bondholders, special servicers are building capacity, banks and life co's have been responsive to borrower requests and debt funds are starting to sort through the competing pressures of distressed borrowers and anxious line lenders.

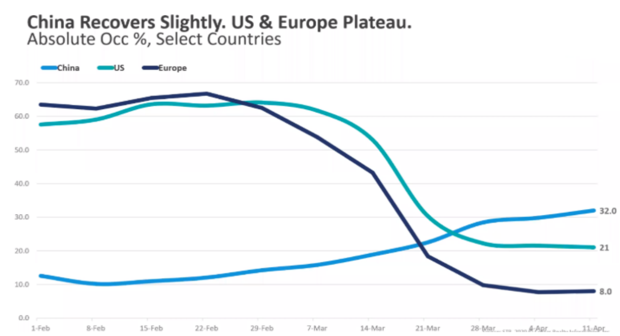
One special servicer alone saw **$3B of forbearance requests** from nearly 500 borrowers last week, overwhelming their 8-person team. Their initial response was to create a **one-forbearance-fits-all response** allowing borrowers to draw down **FF&E and other reserves** to cover losses for a p eriod of three months (and paid back in the next 12 months). That will not be a long-term solution, but it will buy borrowers and themselves time to develop more comprehensive solutions.

Fitch expects US CMBS loan delinquencies to peak around 8.5% with **hotel and retail peaking at 30% and 20% respectively.** As of March 31st, 2020, Retail CMBS loans have occupied **49% of special servicers' time, with Hotel loans at 12%.**

A few lenders, mostly funds, are dipping their toe back into the market. Recent non- recourse quotes we've received reflect leverage of **55-60% LTV** (today's value), spreads of **500-650bp over LIBOR**, a 6-12 month interest reserve and a 24-month lockout. A few bank lenders are also cautiously active, but with stringent underwriting standards and recourse.

Loan Restructuring / Modification Blueprint

We hope that every hotel borrower has already **reached out to their banker,** but we suspect that the conversations held two weeks ago probably bought a few months of respite but will **not carry owners through this downturn**. Now is the time to start planning for the **"U Recovery"** that's likely to occur **rather than the "V Recovery"** we all hoped for. What does that mean? First, don't reinvent the wheel if you don't need to; **consider hiring an advisor**. Many advisors have strong expertise from the last recession and are also seeing how a broad range of lenders are responding. A few early steps:



- **Find and quantify the cash**
    - Identify every source of cash you have in your reserves:
        - Renovation reserves with lender
        - FF&E reserves
        - Debt Service reserves
        - Tax and Insurance Reserves with municipalities, etc
- **Be proactive** . Call all the stakeholders involved and present a thoughtful restructuring/modification analysis - it is much better than your lender calling you
- **Renovate** in this low occupancy period if you have the means to do so
- **Consider bringing in capital** to strengthen your balance sheet
- **Pay debt service** if you have the money - the best debt in the market is what is already in place : while base rates are down, it does not mean that the all-in rate will be lower than prior rates, and leverage will be limited

We will continue to share our insights with you and hope this correspondence finds you safe and healthy.

Sincerely,

RobertDouglas

If you have any questions about the RobertDouglas Market Pulse or would like to be added to our distribution list, please contact Alexander Bauman at abauman@robert-douglas.com.

To discuss your capital market needs please contact:

Robert Stiles
Principal & Managing Director
(415) 578-9247
rstiles@robert-douglas.com

Douglas Hercher
Principal & Managing Director
(212) 993-7424
dhercher@robert-douglas.com

Stephen O'Connor
Principal & Managing Director
(310) 402-2820
soconnor@robert-douglas.com

Evan Hurd
Principal & Managing Director
(212) 993-7425
ehurd@robert-douglas.com

LINKEDIN WEBSITE

RobertDouglas is a real estate investment banking firm with offices in New York, Los Angeles and San Francisco that specializes in the sale, financing and equity capitalization of hotel, resort and gaming properties throughout North America. Founded in January 2013 and currently led by its four partners, Rob Stiles, Doug Hercher, Stephen O'Connor and Evan Hurd, RobertDouglas offers access to exceptional domestic and international institutional investor and lender relationships as it combines the capital markets sophistication of top-tier investment banks with diligent hotel underwriting and proven asset management experience.