

## U.S. Hotel Industry 1H 2023 Summary & Outlook for 2H 2023

by  
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### INTRODUCTION

In late July, the United States Federal Reserve announced a 0.25% increase in the discount rate, being the 11th increase since March 2022, and bringing the discount rate range to 5.25% - 5.5%; in making the announcement, the Federal Reserve chair, Jerome Powell, said “The worst outcome for everyone, of course, would be not to deal with inflation now [and] not get it done.” With this increase in mind and US hotel operating results for 1H2023 released in the latter half of July, it is a good time to look back at 2023 operations and capital markets as of June 30 and to look ahead to the remainder of the year.

### OPERATING PERFORMANCE

According to June 30 data on the U.S. Hotel Markets compiled (and released) by STR, while month over month performance improved, year-over-year results were mixed, though “the Top 25 Markets showed higher occupancy and ADR than all other markets,”<sup>1</sup> growing 0.6% in June and 0.7% for the quarter ending June 30.<sup>2</sup> June’s results for the entire U.S. hotel industry were 69.7% occupancy (a decrease of 0.4% from June 2022), ADR of US\$158.40 and RevPAR of US\$110.33 (increases of 2.3% and 1.9%, respectively). It should be noted that June 2022 was a rather robust month across the U.S. and North America.<sup>3</sup> LODGING (a publication of the American Hotel & Lodging Association) recently stated,

A bright spot for the economy and the hotel industry in Q2 2023 was the increased consumer confidence and sentiment, which, among other things, led to strong demand for guestrooms. This strong demand is expected to continue through the rest of the summer and into the fall with heavy tourist demand through August and the kick-off of the fall conference season after Labor Day [September 4].<sup>4</sup>

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<sup>1</sup> HNR Hotel News, “STR Reports U.S. Hotel Performance for June 2023” ([STR Reports U.S. Hotel Performance for June 2023 \(hotelnewsresource.com\)](https://hotelnewsresource.com)), July 19, 2023.

<sup>2</sup> STR Data Insights Blog (<https://str.com/data-insights-blog/us-hotel-commentary-june-2023>), July 25, 2023.

<sup>3</sup> STR Data Insights Blog (<https://str.com/data-insights-blog/us-hotel-performance-cooled-bit-leadup-summer>), June 26, 2023.

<sup>4</sup> LODGING, “Lodging Econometrics: U.S. Construction Pipeline Up 7 Percent Year Over Year,” (<https://lodgingmagazine.com/lodging-econometrics-u-s-construction-pipeline-up-7-percent-year-over-year/>), July 28, 2023.

## CAPITAL MARKETS

### *Sales*

LWHA's recently published Q2 2023 Major U.S. Hotel Sales Survey<sup>5</sup> is reflective of the mixed market results and, likely, reflective of the rise in interest rates, challenges with new lending, inflationary times and upcoming hotel loan maturities. The Survey shows the results in *Table 1*.

*Table 1*

Period → Category ↓	Q2 2023 Survey	Q1 2023 Survey	Q2 2022 Survey	H1 2023 v. H1 2022 (by %)
# of >\$10 million transactions	84	83	133	-36%
Total transaction (\$\$)	≈ \$3.1 billion	< \$3.5 billion	≈ \$5.3 billion	-50%
Total Hotel Rooms	≈ 12,100 rooms	≈ 12,500 rooms	≈ 21,200 rooms	
Price Per Room	\$257,000	\$279,000	\$248,000	-4%

Besides providing raw data, Dan Lesser (Co-Founder, President & CEO of LWHA) also notes that,

Although U.S. hotel sale transactions continue to be consummated, activity is tepid due to the current disconnect between operating fundamentals and capital markets. . . . Generally, pricing of U.S. hotels remains steady and continues to offer favorable discounts to replacement costs which during the recent past have dramatically risen.<sup>6</sup>

Lesser remains optimistic, citing increasing transient demand, low increases in new supply, “bleisure” travel and a yet-to-occur increase in inbound foreign visitation (while other commentators point especially to Chinese outbound tourism as a major factor in such visitation). He believes that the intermediate term (three to four years) will show a recovery in hotel asset values such that, by 2026 – 2027, “[p]roperty values . . . will no doubt exceed the peak of 2021-2022 as recoveries always exceed previous all-time highs.”

### *Loan Maturities*

COVID's aftermath, if, indeed, the pandemic is over, is reflected dramatically in maturing hotel industry loans for the near future. CoStar has estimated that hotel CMBS loans that had original maturity dates in 2023, 2024 and 2025 amounted to some \$15 billion, \$14 billion and \$6 - \$7 billion, respectively; forbearances and deferrals of COVID-period maturities increased those totals by about

<sup>5</sup> “Inside the Decline of Hotel Transactions in Q2” (<https://www.globest.com/2023/07/18/inside-the-decline-of-hotel-transactions-in-q2/>) by Daniel H. Lesser, July 18, 2023.

<sup>6</sup> *Ibid*, p. 4.

\$12.5 billion in 2023 and \$3.5 billion in 2024 (flat in 2025).<sup>7</sup> It is not entirely clear how the current interest rate environment has affected the repayments (or further deferrals) of those maturing loans, however, data for June 2023 indicates that some 5.4% of hotel CMBS loans had been transferred to “special servicing” at that time, suggesting that there had been defaults on loan covenants (*e.g.*, net worth tests, debt service coverage requirements, *etc.*), current payments (failure to make debt service payments) or maturity without payments.<sup>8</sup> As rates have risen during 2023, the delinquencies or defaults are likely to increase as well.

## 2H 2023 OUTLOOK

Broadly speaking, the outlook for the second half of 2023 is favorable, but achieving favorable results is not without headwinds. “While top-line performance advances, growing operating expenses are projected to limit profit growth over the remainder of the year.”<sup>9</sup> In fact, although it is widely anticipated that 2023 full-year revenue achievement will virtually match 2019’s across the U.S. hotel industry, profit margins are lower due to a combination of inflation and increased personnel and other costs.

New supply is not expected to be a challenge to operating performance for the remainder of 2023. Commentators range from saying “Like other real estate sectors, there is no new [lodging] construction taking place”<sup>10</sup> to a more tempered perspective explaining the dearth of new supply.

Construction costs remain sky high (not to mention the exorbitant cost of financing, if any can be secured for proposed projects), which will delay many new hotel projects, and this new-build low will ultimately contribute to continued strong hotel performance. Supply chain challenges and tighter building regulations are also contributing to the development challenges.<sup>11</sup>

The U.S. Hotel industry is likely to focus on the expense side of its income statements for the foreseeable future, as revenues return to and exceed 2019 levels. There will be much talk and many

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<sup>7</sup> CoStar, “Amount of Maturing Hotel CMBS Loans Balloons This Year After Getting Extensions” (<https://www.costar.com/article/272132985/amount-of-maturing-hotel-cmbs-loans-balloons-this-year-after-getting-extensions>), February 27, 2023

<sup>8</sup> Wolf Street Report, “Third Wave of Hotel CRE Defaults Has Started, Triggered by CMBS Maturities and Variable-Rate Mortgages” (<https://wolfstreet.com/2023/07/11/third-wave-of-hotel-cre-defaults-has-started-triggered-by-cmbs-maturities-and-variable-rate-mortgages/>), July 11, 2023

<sup>9</sup> CoStar, “STR, TE Lift Forecast for US Hotel Average Daily Rate, Revenue Per Available Room,” (<https://www.costar.com/article/83602973/str-te-lift-forecast-for-us-hotel-average-daily-rate-revenue-per-available-room>), June 6, 2023.

<sup>10</sup> Ferguson Partners, “Global Hospitality and Leisure Advisory Prospective Summer 2023” (newsletter), July 2023.

<sup>11</sup> HVS International, “HVS Takeaways from the NYU Hospitality Conference” (<https://www.hvs.com/article/9666-hvs-takeaways-from-the-nyu-hospitality-conference>), June 8, 2023.

articles about using A.I. and technology to accomplish this; some will be successful in harnessing both A.I. and technology; many will trumpet their success, even if it is ephemeral. Room revenue performance, according to Tourism Economics and STR, for 2023 year-end and 2024 is shown in *Table 2*.<sup>12</sup>

*Table 2*

Metric	2022 Actual	2023 Forecast	2024 Forecast
Occupancy	62.6%	63.5%	64.4%
ADR	\$149.06	\$154.28	\$159.03
RevPAR	\$93.29	\$97.95	\$102.49
2019 RevPAR Index	(7.3%)	(2.7%)	1.8%

## CONCLUSION

We believe that the ride will continue to be bumpy, particularly due to as-yet controlled inflation and interest rates that are causing headaches for new construction, acquisition financing and refinancings; it is thought there is much “dry powder” capital sitting on the sidelines, but those will be expensive and insufficiently fast funds to benefit some current owners of hotels with 2023 maturities. How the lenders handle the defaulted hotel loans will speak volumes about the ongoing recovery in the hotel space; they performed well during COVID, and how they perform in the next 18 months will tell a story.

<sup>12</sup> CoStar, “Forecast Projects US Hotel Revenue Growth but Lower Profit Margins” (<https://www.costar.com/article/499374617/forecast-projects-us-hotel-revenue-growth-but-lower-profit-margins>), June 8, 2023.