

HVS

HVS | HODGES
WARD
ELLIOTT

2018 EUROPEAN HOTEL LENDING SURVEY

Peter Szabo
Associate

Simon Hultén
Analyst



HVS.com
HVSHWE.com

HVS London and HVS Hodges Ward Elliott
7-10 Chandos Street, London W1G 9DQ

Highlights



The headwinds from geopolitical insecurities have proven surmountable, providing an upswing in confidence among hotel lenders compared to one year ago, suggesting an even more positive momentum in **availability of debt across all hotel projects** and segment types, including new developments.



A continued **'borrower's market'** with **historically low interest rates** and compressed lending margins was seen in 2017.



The end of the prolonged era of cheap money in Europe is becoming apparent, yet **investors and developers will most likely benefit from the current conditions** in the coming 12 months.

Hotel Financing – A Continued Borrower's Market

Through our work with hotel investors and developers, we have seen abundant hotel financing for all project types across European markets in recent years. The combination of continued strong growth momentum in hotel values across Europe as well as historically low interest rates has resulted in an increase in hotel transaction volumes, with many investors seeking the use of all available debt.

This survey, conducted among hotel teams of leading European banks with maximum loan amounts ranging from €20 million to €600 million, consisted of four topics: (1) lending parameters, (2) availability of debt by project and chain-scale segment, (3) loan characteristics, and (4) an outlook on lending criteria. Figure 1 highlights the primary countries covered by the respondents of this survey.

FIGURE 1: OVERVIEW OF PRIMARY MARKETS COVERED BY THE SAMPLE



Results

1. Senior debt is abundant for all project types

Lenders have reported that debt for hotels is widely available across Europe. Our respondent banks are all willing to issue senior debt for existing property acquisitions, refinancing, renovations and expansions. Interestingly, hotel refinancing is most active in Central and Eastern Europe (CEE), with a number of loans only recently refinanced or settled.

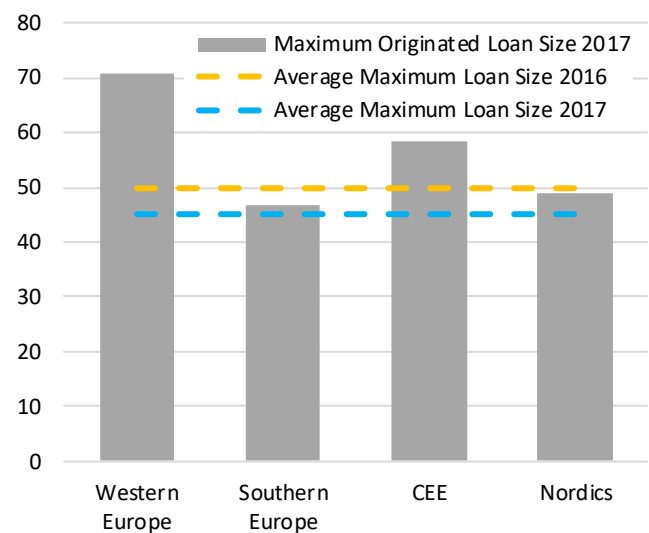
While debt is available for all project types, the market for development financing is smaller than for investment financing, with not much more than 20% of loans being given to such projects. This attitude mirrors banks' perception of the market being at a more mature phase in the cycle, resulting in more cautious lending for new developments and fears of possible oversupply, particularly in Western Europe.

2. Western European banks are decreasing loan sizes

With a view across various hotel lenders, it is still Western European banks that can issue the largest loan quantum. However, as the current investment cycle reaches its ninth year in 2018, the average loan size without syndication has started to decrease slightly in the most mature hotel markets.

Our respondents indicated that smaller regional banks continue to finance projects of similar sizes as before, but major international banks have slightly decreased the loan quantum they offer. While borrowers certainly benefit from a wide variety of options for small- and medium-sized projects, for loans above €250 million only the largest European hotel lenders are able to provide syndicated funding.

FIGURE 2: MAXIMUM ORIGINATED LOAN SIZE (€MILLIONS)

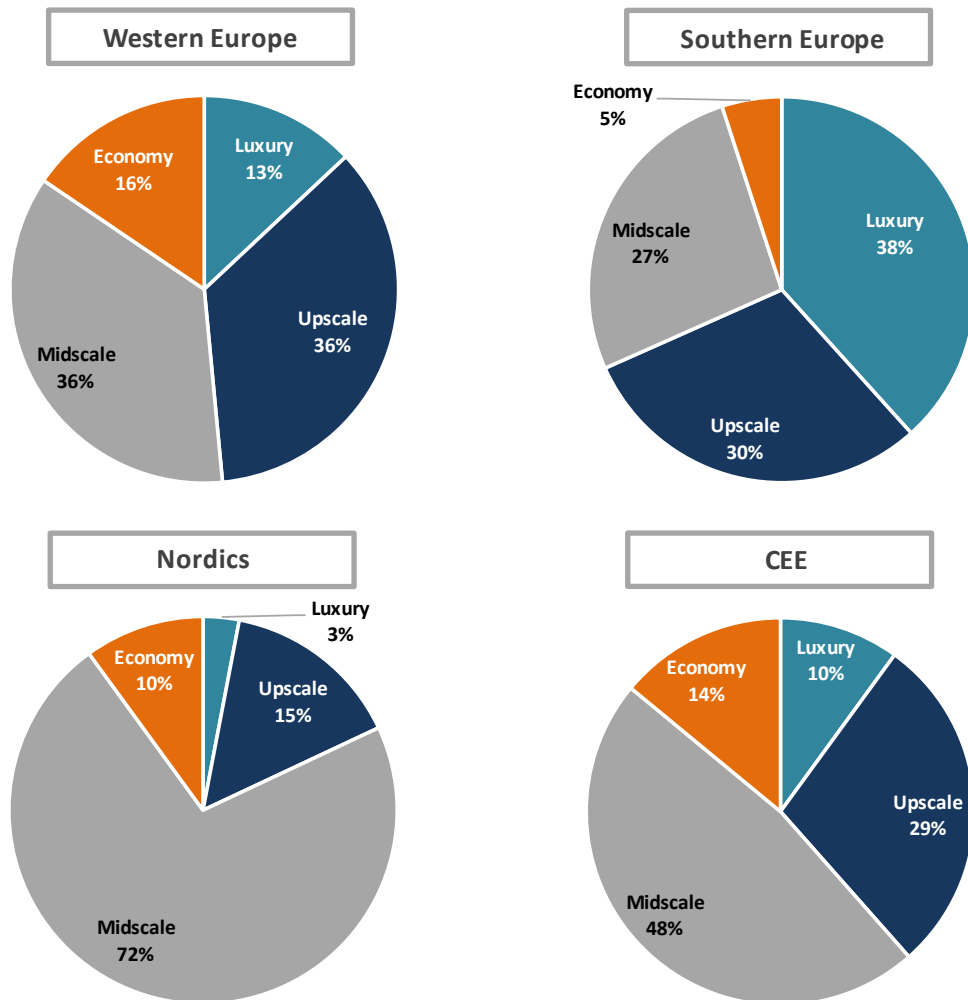


Source: HVS – London Office

3. Lenders continue to prefer full-service properties at the higher end of the chain-scale segment

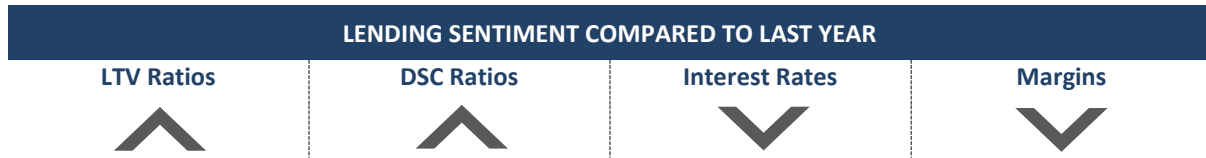
Upscale and midscale hotels continue to be the most favoured type of hotels to receive loans, followed by the luxury segment. Economy properties have received the least amount of financing from our respondents. The exception to this rule is the Nordics, where lenders allocate an average of only 3% of their loans to luxury hotels and have a clear preference for midscale properties.

FIGURE 3: PORTION OF LOANS GIVEN BY CHAIN-SCALE SEGMENT



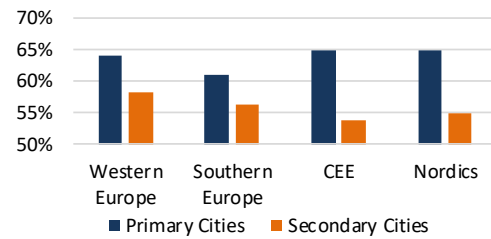
Source: HVS – London Office

4. Borrowers continue to benefit from competitive lending margins



In line with improving hotel performance, all respondents indicated a loan to value (LTV) ratio at or above 50%, with lenders on average increasing their maximum acceptable LTV over the past 12 months by 2.3% to 59.8%. The regional differences shown in Figure 4 also reflect the perception of risk around the maturity of the cycle, as many banks consider Western Europe to be at a more mature phase in the cycle and are thus applying more conservative maximum LTVs.

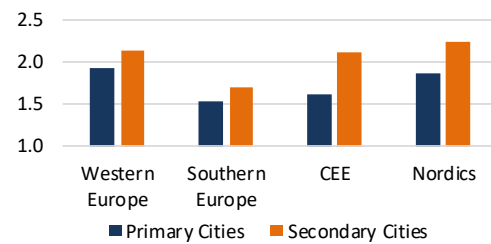
FIGURE 4: LTV RATIOS



Source: HVS – London Office

Debt service coverage (DSC) ratios range from 1.5 to 2.25 across all surveyed markets. While these figures might seem relatively high, it is important to keep in mind that banks are operating in a very low interest rate environment. These low financing costs along with compressed margins and long amortisation periods all act as factors that increase DSC ratios. It is likely that when interest rates increase in the future, DSC ratios will compress.

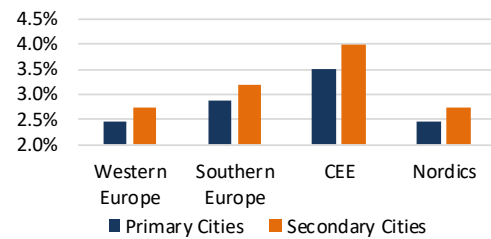
FIGURE 5: DSC RATIOS



Source: HVS – London Office

Fixed interest rates continue to be offered at historical lows, below 4% in all major markets. A slight decrease of 0.28%, likely due to increased competition among lenders, can be observed over the last 12 months for hotels with management agreements in Western Europe. Banks offer less favourable terms for secondary markets.

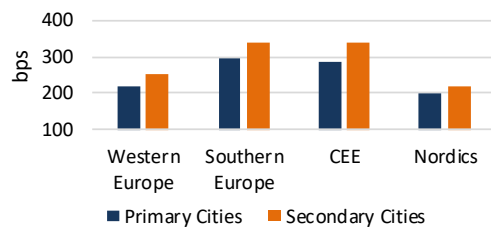
FIGURE 6: FIXED INTEREST RATES



Source: HVS – London Office

Variable floating rates in basis points (bps) follow a more varied trend, with average margins ranging from 200 bps in primary markets in the Nordics to 350 bps in secondary markets of Southern Europe. While regional differences in lending margins do exist, borrowers continue to benefit from highly competitive lending terms across Europe.

FIGURE 7: MARGIN ON FLOATING INTEREST RATES



Source: HVS – London Office

5. Positive sentiment in hotel financing for the future, challenged by alternative lenders

As we look ahead, the collective sentiment among our respondents is positive. Western and Southern European banks expect a continued increase in the size and number of their hotel loans and a higher proportion of hotel loans compared to other real estate loans over the next 24 months. Interestingly, responses from Western European banks show a more optimistic view compared to last year, reflecting a resilient and growing European hotel industry in combination with a robust global economy.

FIGURE 8: OUTLOOK ON LENDING CRITERIA

	Western Europe	Southern Europe	CEE	Nordics
<i>Size of Loans</i>	↗	↗	—	—
<i>Number of Loans</i>	↗	↗	↗	—
<i>LTV Ratio</i>	—	—	—	—
<i>DSC Ratio</i>	—	—	—	—
<i>Proportion of hotel loans compared to other real estate asset loans</i>	↗	↗	—	—
<i>Interest Rates</i>	↗	↗	↘	↗
<i>Lending from Alternative Lenders</i>	↗	↗	↗	↗

Source: HVS – London Office

Western European, Southern European and Nordic banks have indicated that interest rates are likely to be on the rise again, given the current low interest rate environment. Whilst the ECB may begin its first move upwards as late as 2019, the Bank of England already started raising rates for the first time in a decade and it seems likely that other Western European banks might increase their margins in the coming year.

With the UK hotel market thriving in 2017 following the previous year's Brexit vote, lenders are positive about lending in Britain thanks to increased international arrivals and strong market fundamentals. In spite of cost challenges in a post-Brexit economy, banks continue to rank the UK as their most preferred hotel lending market along with Germany and the Netherlands.

Looking forward, new hotel lending for high-street banks is likely to be for either new acquisitions or refinancing, with almost all respondents agreeing that alternative lenders will become more prominent for riskier projects.

Conclusion

Over the past year, cautiousness derived from increased political risks and economic policy challenges has been replaced by a more positive outlook for hotel lending, and our survey of European hotel lenders indicates a continued appetite for hotel investments in Europe. With strong hotel market fundamentals, debt continues to be available for all project types at compressed margins in most regions, leading to the continued broad popularity of hotels as an alternative real estate asset class and increasing investor interest.

Although we cannot expect interest rates to remain at these historically low levels in the long-term, investors will most likely continue to benefit from attractive terms during the next 12 months and be able to secure financing for their hotel investments.

Notes:

About HVS

HVS, the world's leading consulting and services organisation focused on the hotel, mixed-use, shared ownership, gaming, and leisure industries was established in 1980. The company performs 4,500+ assignments each year for hotel and real estate owners, operators, and developers worldwide. HVS principals are regarded as the leading experts in their respective regions of the globe. Through a network of more than 40 offices and more than 350 professionals, HVS provides an unparalleled range of complementary services for the hospitality industry.

HVS.com

**Superior Results through Unrivalled Hospitality Intelligence.
Everywhere.**

With offices in London since 1990, **HVS LONDON** serves clients with interests in the UK, Europe, the Middle East and Africa (EMEA). We have appraised some 4,000 hotels or projects in more than 50 countries in all major markets within the EMEA region for leading hotel companies, hotel owners and developers, investment groups and banks. Known as one of the foremost providers of hotel valuations and feasibility studies, and for our ability, experience and relationships throughout Europe, HVS London is on the valuation panels of numerous top international banks which finance hotels and portfolios.

About HVS Hodges Ward Elliott

HVS Hodges Ward Elliott is the hotel brokerage and investment banking division of HVS. Operating within the European marketplace, HVS Hodges Ward Elliott acts on behalf of its clients in the sale and financing of hotels and in operator or brand searches and selection. Assignments include individual assets and portfolios, with transactions having been successfully concluded in most major European markets.

For further information about the services of the London office, please contact Charles Human on +44 20 7878 7771 or chuman@hvs.com.

The HVS logo consists of the letters 'HVS' in a white, serif font, centered within a red rectangular background. The letters are slightly shadowed, giving them a three-dimensional appearance as if they are floating above the background.

HVS | HODGES
WARD
ELLIOTT

About the Authors



Peter Szabo is an associate at HVS Hodges Ward Elliott, having joined the firm in 2016. His primary responsibilities include financial analysis, development of hotel sale materials and due diligence. Peter is a native Hungarian

speaker and also speaks German. He holds a BSc (Hons) in International Hospitality Management from Ecole hôtelière de Lausanne with a specialization in hotel development.



Simon Hultèn is an Analyst with the HVS London office. Before joining HVS, Simon held various positions in the hospitality industry. His main responsibilities include hotel feasibility studies, valuations

and market overviews for European hotels. He holds a BA (Hons) in Hospitality Management from Glion Institute of Higher Education with a specialisation in hotel development and real estate.