

## Market Close-up: NYC Hotel

**Overview and Economy.** The New York MSA is the largest in the U.S., with a population of over 20 million. It is the third largest U.S. hotel market, with nearly 124,000 rooms in 653 hotels, according to Lodging Econometrics. At the end of the second quarter of 2020, the region had 18,354 hotel rooms in 106 properties under construction. Real (2019 dollars) running 12-month revenue per available room (RevPAR) fell a stunning 33.4% to \$148.44 in August 2020, compared to \$223.64 the prior year. The real average daily rate (ADR) also decreased 12.5% from \$258.20 to \$225.90 per key over the same period. The near-term outlook for the MSA hotel market will be muted for as long as virus fears persist.

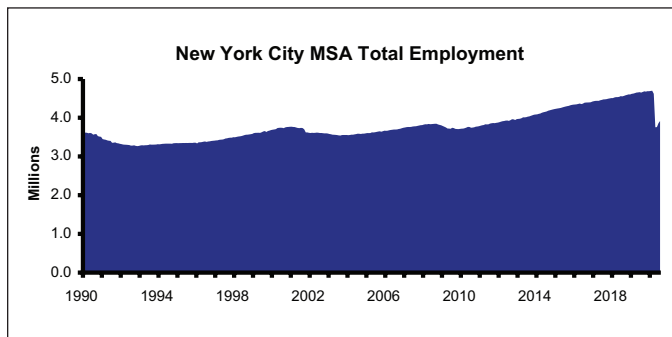


figure 1

Between February and April 2020, Payroll employment in NYC declined by 944,000 (20.1%), recovering 161,000 jobs (4.3%), to a total of 3.9 million jobs through July 2020. The top Fortune 500 companies in the MSA include JPMorgan Chase, Verizon Communications, Citigroup, MetLife, and Goldman Sachs Group.

Prior to COVID-19, all sectors in the were growing, but none saw year-over-year growth through July 2020. Leisure and hospitality (-58.3%) was hit the hardest, followed by mining, logging and construction (-23.6%) and manufacturing (-21.6%). The industries with the highest employment in MSA are education and health services (966,000); professional and business services (687,500); and government (569,600).

In previous issues, we have discussed a covariance analysis that was first published in the *Wharton Real Estate Review* (Spring 2007) and is regularly updated in this publication. The analysis examines how various economic indicators behave in individual metropolitan areas based on national economic changes. Specifically,

for each MSA, we estimated an equation, which summarizes how a 100-basis point (bp) change in national employment affects the local indicator. The equation consists of a constant (“alpha”) for each market and a “beta,” which is a multiplier applied to the national percent change in employment. The alpha indicates MSA growth that is independent of national growth, so if there is no national job growth, alpha is the expected annual percentage change in MSA employment. The beta for the U.S. as a whole is, by definition, equal to one. An MSA with a beta of one registers (on average) an increase of 100 bps in employment growth plus alpha when national employment rises by 100 bps. A beta that is less than one indicates that the MSA does not boom (or bust) to as great an extent (around its trend) as the national economy, while a beta of greater than one indicates that such an MSA experiences swings of greater magnitude than the percentage changes at the national level.

With an employment beta of 0.9, employment in the NY/NJ MSA responds with 10% lower magnitude than national employment changes. The MSA has an alpha of -0.31, indicating that local employment falls by 0.31% when U.S. job growth is zero. NYC has a break-even point of 0.35, indicating that the MSA will see positive expected annual employment growth as long as U.S. employment 0.35% or greater. The model’s R-squared statistic of 0.66 indicates that the forecasting model for the NY/NJ metro employment growth explains future job growth with 66% “fit.”

Our model projects that the NYC would lose 6.3% of jobs given that national employment declined by 6.3% during the Financial Crisis. In fact, during the Financial Crisis, the NYC lost 3.6% of jobs. During the recovery, while U.S. employment grew 17.6% from the bottom through February 2020, metro employment increased 26.8% over the same period, far above our predicted 12.1% growth from the bottom. Between February and April 2020, the U.S. lost 14.5% of jobs, while the MSA lost 20.1% through the same period, well above the predicted 11.6% loss. This reflects its prolonged regulatory shutdown. As the economy began to reopen, U.S employment increased by 7.1% through July 2020, implying corresponding growth of 6.4% in the MSA, versus actual growth of 4.3%. The extended shutdown has muted the jobs rebound.

The MSA unemployment rate reached 9.3% in November 2009 and steadily declined during the

recovery, reaching 3.5% in February 2020. In comparison, the national unemployment rate peaked at 10% in October 2009, and declined by 640 bps, to 3.5% through February 2020. In the wake of the shutdown, the official NYC and U.S. unemployment rates spiked to 19.8% and 14.7% in July and April, respectively. The official U.S. rate subsequently dropped to 10.2% in July and 8.4% in August. While directionally correct, the unemployment rates are under-reported by the BLS by at least 300 bps due to survey errors.

standing 24.1% below the 2010 recessionary low and 46.2% below the long-term high. Real ADR in the MSA was \$225.90 in August 2020, a decrease of \$32.32 per key (-12.5%) over the prior year. By comparison, real U.S. RevPAR and ADR were \$58.49 and \$115, respectively in August 2020.

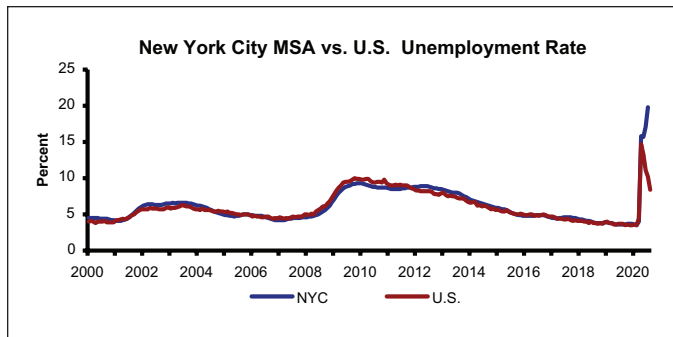


figure 2

**Hotel Market Statistics.** The MSA’s rolling 12-month occupancy rate stood at 86.3% in February 2020 but rapidly dropped to 65.7% through August, even as the economy began reopening. This is in comparison to NYC’s long-term average (since 2008) occupancy of 83.3%, the 2009 low of 76.3%, and the all-time high of 87.4% seen in May 2018. NYC’s hotel occupancy rate ranked first among STR’s Top 25 U.S. markets in August 2020. By comparison, the U.S. average occupancy rate was 50.9% in the same period.

Real RevPAR in the MSA stood at \$148.44 in August 2020, a decline of \$74.47 per key (-33.4%) compared to a year earlier. The latest RevPAR is a new all-time low,

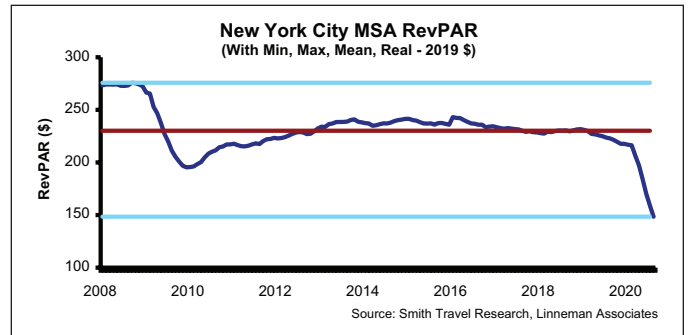


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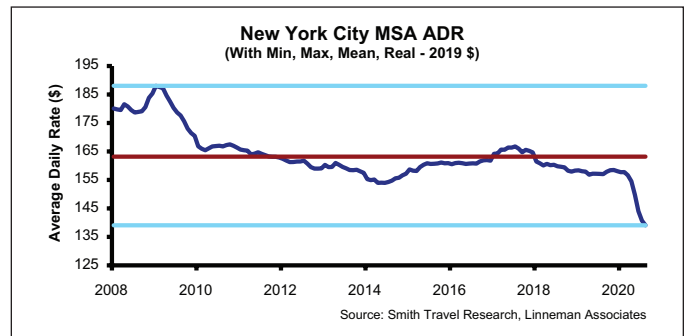


figure 5

**Visitor Trends.** New York City the largest city in the nation and received tens of millions of tourists every year prior to 2020. Notable architectural and tourist sites include the Empire State Building, Central Park, the Statue of Liberty, Freedom Tower, and the headquarters of the United Nations. Unfortunately, tourism ground to a halt as the city became the epicenter of the COVID pandemic and travel (especially international) largely ceased.

According to the Port Authority of New York and New Jersey, New York City achieved its ninth consecutive annual record of 65.2 million tourists in 2018, 13.6 million of whom were international, with top countries for visitors being from the UK, China, and Canada (each one million visitors), Brazil (718,000), France (662,000), and Germany (587,000). Day trips to the city are common from surrounding areas like Philadelphia, upstate

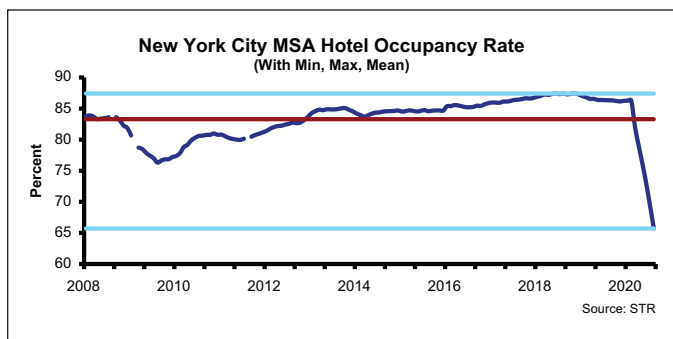


figure 3

New York, Connecticut, and New Jersey, while overnight trips draw tourists from across the nation.

**Investment and Sales.** Real 12-month rolling hotel sales volume in the MSA stood at nearly \$1.8 billion through August 2020, more than \$4.2 billion (70.4%) lower than the June 2019 level. The latest sales volume is 47.5% below the long-term average of \$3.4 billion but still well above the 2010 low of \$401 million. However, it is 79.2% below the 10-year historical high of \$8.6 billion.

In the second quarter of 2020, the real four-quarter moving average real price (2019 dollars) per hotel room in the MSA stood at approximately \$299,000, 10.3% below its long-term average (since 2005) of \$334,000 per room. By comparison, the current real U.S. pricing is about \$94,000 per room, which is 34.3% below the national long-term average. Local hotel sales pricing decreased by 12.9% over the last year, while U.S. pricing dropped by 31.1%. Given the lack of transactions, there is currently no meaningful price of a hotel room as of the end of May.

We examined private transaction cap rate series from RCA. Given that such data is notoriously difficult to track, it is not surprising that there are breaks in the data

series. RCA reported that the second-quarter 2020 cap rate was 7.5%, on par with long-term average. But with the absence of new transactions it is difficult to guess how high cap rates have risen. We suspect they would need to be 10% on trailing-12 month NOI to generate any interest among buyers.

Major buyers of NYC hotel properties over the last two years include: UBS (\$719 million, one property acquisition); SoftBank Group Corp (\$719 million, one property); Mubadala Investment (\$654 million, one property); GFI Capital Resources (\$530 million, two properties); and Magna Hospitality Group (\$456 million, four properties).

Major sellers of NYC hotel properties over the past two years include: L&L Holding (\$719 million in one property disposition); Maefield Development (\$719 million, one property); Fortress (\$719 million, one property); Jynwel Capital (\$654 million, one property); and LaSalle Hotel Properties (\$565 million, four properties).

**Construction Pipeline.** According to Lodging Econometrics, 34 new hotels (6,091 rooms) were completed in the MSA in 2019, resulting in a 5.2% growth rate in the existing inventory. In the first half of 2020, six hotels (778 rooms) were completed, with 31 more properties (3,431 rooms) scheduled for delivery in the second half of 2020. If all 378 projects (4,209 rooms) are completed in 2020, NYC would see 3.4% growth in hotel inventory. At the end of the second quarter of 2020, there were 106 hotels (18,354 rooms) under construction, 18 hotels (3,898 rooms) scheduled to break ground in the next 12 months, and 27 hotels (4,050 rooms) in the early planning stages in the MSA. In aggregate, the construction pipeline consists of 151 hotels (26,302 rooms), about 21.1% of existing inventory. Many of these projects will be mothballed or cancelled.

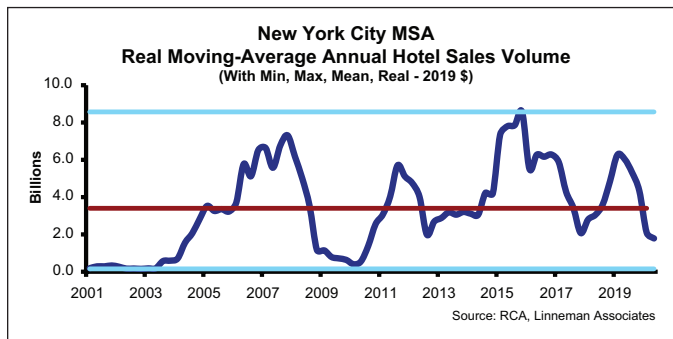


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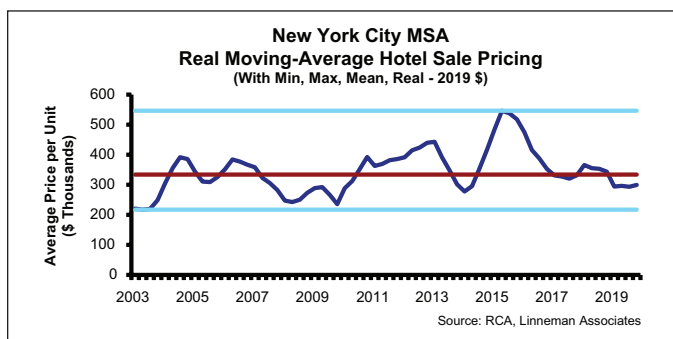


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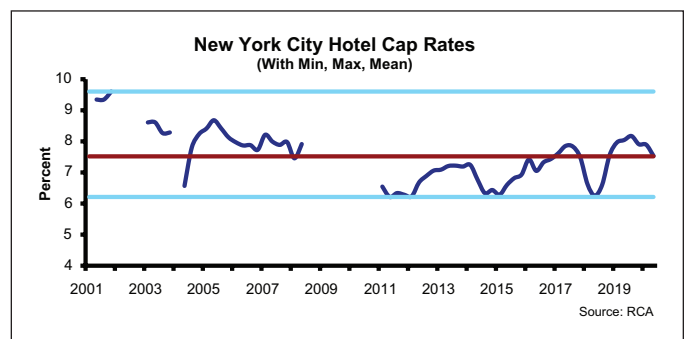


figure 8

**Opportunities and Challenges.** New York City is among the oldest cities in the U.S. and is the most densely populated in the country. Its status as a financial, cultural, transportation, and economic hub normally mean tens of millions of visitors each year. World renowned tourist destinations include the Empire State Building, the Statue of Liberty, Central Park, Freedom Tower, and the Broadway Theater area. A plethora of companies headquartered in NYC also attract millions of business visitors every year, and the United Nations headquarters brings diplomatic envoys and tourists alike. All of these factors contributed to a booming hotel industry prior to COVID.

The pandemic and the government shutdown that followed brought the hotel industry to a grinding halt. NYC in particular was hit worse than most of the nation, as it became the epicenter of U.S. COVID cases and related media coverage. As a result, hotel occupancy plummeted. Perhaps the most high profile victim of the ruined hotel industry is Hilton's 478 room hotel in Times Square. On October 1 the popular 44-story hotel will be permanently closed, resulting in the loss of 200 jobs.

At the height of the pandemic, the NYC government closed all "non-essential" businesses, including homeless shelters. Additionally, non-violent prisoners were released from jails. As a result, thousands of homeless people now had nowhere to go but the street. To alleviate this problem, the Department of Homeless Services relocated 10,000 homeless people into 60 empty hotels. In late September, the process of transferring the homeless people back to homeless shelters began.

New York City was also an epicenter of the widespread civil unrest that swept the country in May and June. Following the highly publicized deaths of George Floyd and Breonna Taylor, every major city in the U.S. saw protests against police brutality. After extreme measures taken by police, many of these protests turned into riots, with many individuals largely unrelated to the social justice movement capitalizing on the chaos to loot high-end NYC businesses. This unrest made tourists even less likely to visit the city than they would have been with only the virus to fear. Since the initial days of chaos, clashes between the police and protesters have remained common in New York City.

The city government is finally allowing businesses to reopen to the public and is encouraging visitors from

surrounding areas like New Jersey and Connecticut to visit. Starting September 30, restaurants will be allowed to have customers dine in once again, albeit at a limited capacity. Open air attractions like the botanical gardens and zoos have reopened, and museums reopened in late August. Finally, popular tourist attractions like the Empire State Building are also reopening to visitors. As consumer confidence slowly returns, people will feel more comfortable travelling, and the hotel industry will be slowly revitalized.

**Outlook.** The truth is that nobody knows what near-term job growth will be, but we use our best estimates of job recovery nationally and within each MSA. Our statistical employment forecasts are net of construction jobs due to the volatility and short-term nature of that sector. We forecast that the New York City MSA will add about 166,000 non-construction jobs (41,000 per year) in 2021-2024. We expect that the second-quarter occupancy rate of 72.9% will decrease to 64% by year-end 2020 and will then slowly strengthen as jobs are regained.

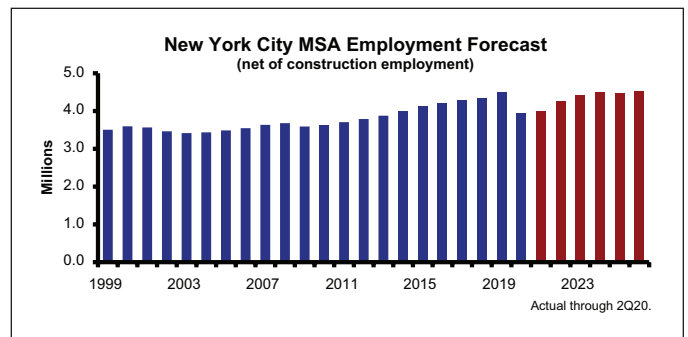


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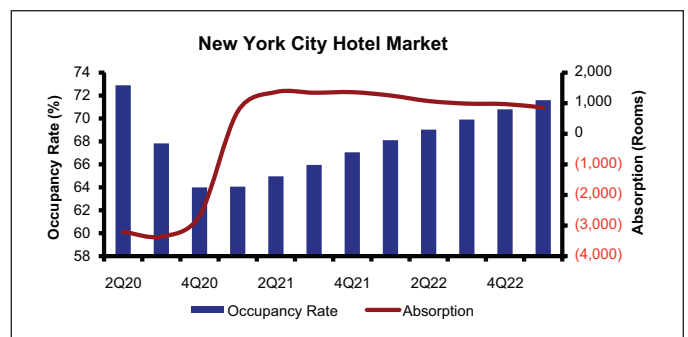


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