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Implications for keeping hotels competitively positioned as stock of rooms grows older

Keeping hotels competitive will hinge on renovations, repositioning and reprogramming of existing assets rather than on new supply

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Aging room inventory now dominates many of the largest hotel markets, with more than half of all hotel rooms over 20 years old. This aging room stock coincides with a muted development pipeline, leaving little new supply to offset the existing base.

As a result, hotel developers with the balance sheets and conviction to build in the current environment are likely to complete new projects that will face limited new competition and an increasingly older peer set.

For other hotel operators, remaining competitive is likely to hinge on renovations, repositioning and reprogramming of existing assets rather than on new supply. Only a sustained easing in interest rates and construction costs would materially change the risk calculus for developers in these markets with aging hotel stocks.

That appears unlikely, however, as rising prices for fuel and construction materials like aluminum stemming from the war in Iran are pushing up costs months after they showed signs of stabilizing, according to a recent Wall Street Journal article. Until construction costs stabilize and interest rates come down, both consumers and investors will continue to operate within this hotel environment defined by older hotel stock.

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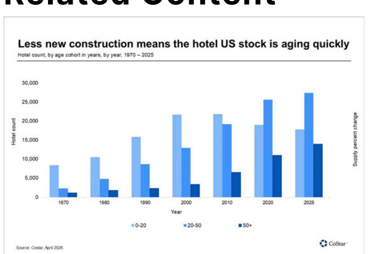

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Some notable exceptions to this trend exist. New York City stands apart as the clearest counterexample. Just 42.3% of its hotel rooms are older than 20 years, giving it the youngest inventory among the Top 25 global hotel markets. In addition, the number of rooms currently under construction is 13.8% of the existing 20-year-old inventory, giving New York the highest ratio among large global markets.

Even with a relatively modest base of aging hotel stock, New York continues to add new hotel rooms at a pace that materially refreshes its room stock. Over multiple cycles, developers have sustained reinvestment regardless of broader macroeconomic conditions, preventing the market from aging in the first place.

However, the earlier-planning pipeline for hotel rooms in development has slowed sharply as recent regulatory changes have rendered many proposed hotel projects in New York City unworkable. These recent changes include ending most as-of-right hotel development and requiring new hotels with 100 or more rooms to obtain special permits, approval from the city council and limited their use of subcontractors for housekeeping.

While projects already underway will keep inventory relatively young in the near term, the medium-term outlook for New York's new room supply is more constrained. Capital is therefore likely to gravitate toward maintaining and upgrading existing assets rather than pursuing new construction.

Several other markets exhibit a similar, though less pronounced, dynamic. Nashville, Tennessee, Miami, Phoenix and Dallas all post shares of 20-year-old hotel room inventory at or below the midpoint of the Top 25, while maintaining construction ratios well above many peers. In these markets, hotel development activity remains sufficient to counterbalance aging pressures.

The remaining hotel markets on the list, such as Seattle, Minneapolis, San Francisco, Orange County, California, and Oahu, Hawaii, have extremely limited hotel construction activity and a majority of rooms older than 20 years. San Francisco illustrates the imbalance most starkly, with more than 83% of its hotel rooms older than 20 years, and in-construction supply accounting for just 0.2% of that aging base.