Know Your Stuff

Secure optimal hotel loans by being well-informed and well-prepared

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Lenders want to offer their best terms to projects they think will be successful. If a project's success looks uncertain, it is a lender's nature — if not its duty — to withhold favorable conditions. To get A-plus terms from a lender, borrowers must illustrate the venture's value, primarily regarding the security of the investment.

The process of securing optimal terms can be especially problematic for those in the hotel business. Hotel deals often face a greater perceptual bias from lenders than do other asset classes. There are two major steps involved in trying to secure competitive financing for hotels — making your case and knowing the deal.

Make your case

The hotel-financing business is risky, and you must anticipate a lender's preconceptions of the hotel industry. Help your borrowers prepare cogent responses to lenders' subjective notions and judgments. When writing a proposal, focus on two things: First, what differentiates this project from typical projects the lender sees? Namely, why is this hotel going to be different? Second, are any of the perceived weaknesses actually positive attributes? In other words, how can you portray a decent deal as a great deal worthy of A-plus financing?

Highlight market variables that increase the project's value. Take, for example, an investment banker in northern Minnesota who successfully overcame a location-based bias. Seeking to finance an upscale resort, the banker cited recreational traffic from nearby Minneapolis and St. Paul as a positive characteristic. This traffic, he claimed, presented a four-season demand for lodging in the area. Further, the market research the banker conducted showed an undersupply of upscale resort properties in the region. Lenders saw the project's location as an advantage, rather than as cause for concern.

Critical information about risk must be presented to lenders as positive opportunities. This can include borrower experience. Lenders look for relevant experience — not just in development. In this case, it is evidence of success in a previous, similar project. For prospective borrowers who are new to the industry, one option is to start small, perhaps in a less competitive marketplace and with a smaller project.

Another solution is to show lenders that your borrowers have found potential collaborators who can bring the necessary experience to the team. This approach can create opportunities not only to complete the project but also to develop profitable, ongoing business relationships.

Know how, know who

The second way to ensure competitive financing may be summarized in four words: Know how, know who.

The "how" begins by clarifying your clients' exact financing needs. Suggest that they work with a financial adviser. This can yield powerful restructuring ideas and result in improved terms. In a recent transaction, for example, a banker helped a client restructure financing by securing additional equity investors. The deal, which had exceeded high-cost/high-leverage financing options, was properly capitalized and positioned for low-cost conventional financing. In another case, a banker saved an all-but-dead deal by raising additional short-term equity, thus lowering the loan to value enough for the lender to close the deal. Within 60 days, the project was refinanced conventionally.

It is important to be a creative partner who can optimize all the elements of the capital stack. The goal is to see several steps ahead — from lenders' and borrowers' perspectives — to position the deal for maximum value.

Knowing how means nothing if you don't know who. Lenders' appetites for

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various asset classes change weekly, depending on their own portfolio-management needs. For example, a current high demand for full-service hotels might be perceived as a popular endeavor that will last. But in reality, market research suggests the lending trend is transient. Borrowers must be aware of what is hot, what is selling and what the lending market desires. Essentially, borrowers need to keep a finger on what lenders want.

A borrowers' chance of getting optimal returns — or even getting funded at all — often depends upon the banker finding unpublicized, under-the-radar information. For example, one lender recently trounced the competition with a powerful term sheet because the loan fit into a securitization pool the firm had just begun to develop for sale in the coming months. A well-connected investment banker can often have enough industry knowledge to see this kind of advantage and leverage it into superior terms for borrowers.

Experience matters when choosing a lender. Because of the hotel business's complexity, the easiest way to secure competitive terms is to go to a firm experienced in the nuances of hotel lending. The added value of market knowledge can be especially worthwhile to borrowers on hotel projects, because they already have to take extra measures to overcome lender preconceptions of risk. Investment bankers can also help borrowers improve financing options by connecting them with third-party-management companies or related services.

The ultimate goal is to organize a methodical sales process that achieves maximum demand for the project's financing, which brings the best terms for borrowers.

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