



# 2019 Caribbean Hospitality Financing Survey

Travel, Leisure & Tourism

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May 2019



# Introduction

We are delighted to present KPMG’s 15th Annual Caribbean Hospitality Financing Survey, highlighting financing trends in the region’s hospitality and tourism industry and the outlook for the future of the industry.

We eagerly awaited the results of this year’s survey because our Confidence Barometer, which records the financing community’s confidence levels in our region’s tourism industry, had recorded an amazing sequence of nine consecutive years of increased confidence levels from 2009-2018. We were hopeful that a major milestone of a decade of annual rises in confidence could be accomplished, however, it was not to be. This year has seen a correction in confidence levels of both banks and non-banks, the latter category comprising private equity firms, family offices, developers, etc.

Furthermore, for the first time since we included non-banks in our survey their confidence levels have dropped below those of banks.

A correction was inevitable at some point, but why did it happen? You may recall our delight, yet genuine surprise last year, when confidence levels maintained their upward trajectory despite the devastating impacts of hurricanes Irma and Maria. It may be that as time progressed the full implications of the hurricanes have been recognized with a corresponding decline in confidence. Another factor could be the perception that the economic cycle is moving through its different phases and whilst most respondents still believe the region’s economy is either at its peak or approaching it, some of our non-bank respondents have opined that the economy may be moving towards recession.

Certainly, it seems that those respondents lacking confidence have particularly strong views which have had a somewhat disproportionate impact on confidence levels.

All of these factors tell a cautionary tale that should be acknowledged but must be put in perspective. All financiers are adamant that the hurricanes have not changed their appetite for financing tourism projects in the region and some have an even greater appetite pursuant to the hurricanes.

Lessons have certainly been learnt though; insurance coverage is increasing, insurance policy wording is being paid more attention to by insurer and insured alike and some insurers have exited the market.

The appetite of financiers is primarily directed towards financing existing hotels for expansions, renovation and refinancing.

However, whilst there has been a reduction in appetite for financing acquisitions, there has been a surprising “uptick” in appetite to fund new builds, particularly by banks.

The more bullish nature of the banks versus non-banks was not expected, yet it can be seen throughout the survey results. They are more confident, consider the region’s economy to be at a more positive stage in the economic cycle, they have a greater appetite for financing and they are more optimistic when presented with a lending opportunity in the region.

Seaweed made its first appearance in the survey. The sargassum challenges faced by many countries in the region was proactively raised by respondents as a factor impacting financing activity in the region as were labour issues along with the critical factors of airlift, crime, and ability to recover from hurricanes which tend to feature annually. Governments are cited once again as having a key role in mitigating some of these challenges.

In conclusion, whilst the dip in confidence levels may have served as a timely reminder of the laws of physics and economics in the sense that what goes up cannot continue on an upward trajectory indefinitely, at least not for 10 years it seems. It may also be a reminder that we have a realistic, pragmatic financing community who retain their appetite for financing tourism projects in the region but, not unreasonably, require certain fundamentals to be in place before loosening the purse strings.



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# Industry outlook

## Confidence levels correction

Confidence levels for banks had increased for an astonishing nine years including last year despite the disastrous 2017 hurricane season. However, there had to be a correction at some point and it happened this year. Consequently, a potential historic milestone of a decade of steadily increasing confidence levels was not quite met.

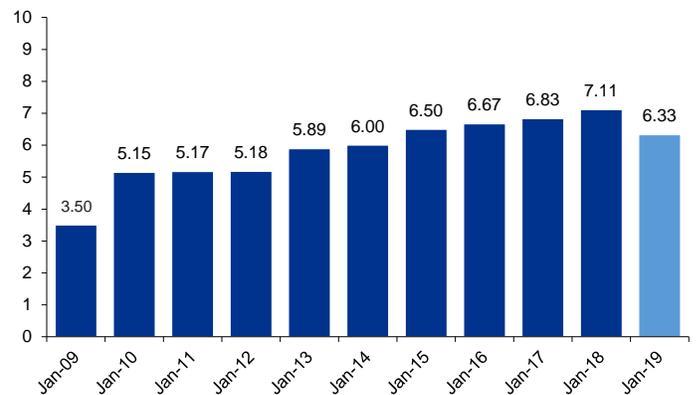
Furthermore, the confidence levels of non-banks were lower than the confidence levels of banks for the first time since we started to include private equity, family offices and developers in this survey.

The reasons for the dip in confidence are not entirely clear although a correction was inevitable at some point. However, we do recall being shocked last year that confidence levels increased after the devastating impact of hurricanes Irma and Maria. It may well be that with the passage of time the full impact of the hurricanes has deflated confidence somewhat although, as we will see elsewhere in this report, financiers do still overwhelmingly state that their appetite for financing tourism projects in the region has not been negatively impacted by the hurricanes.

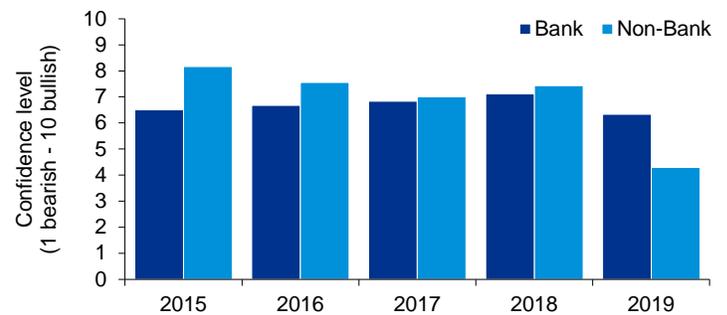
It does appear that those respondents who indicated a decline in confidence tended to have stronger views than those with higher levels of confidence. Some of the non-equity respondents, for example, raised the dreaded prospect of a possible move towards recession.

On balance, however, we feel that whilst the correction in confidence levels should strike a cautionary note and should not be ignored, they should nonetheless still be put in perspective. There are enough positive comments and indications of a stable financing environment to mitigate somewhat the apparent dip in confidence.

## Banks - Caribbean Financier Confidence Barometer



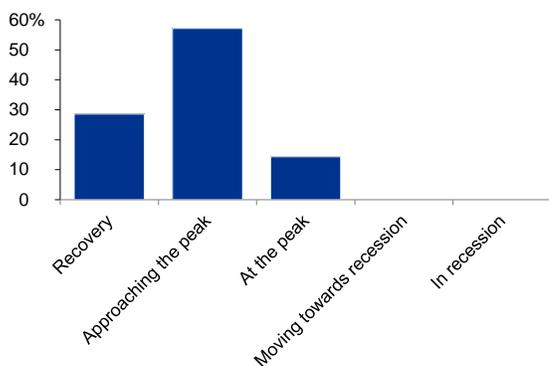
## Banks vs Non-banks - Caribbean Financier Confidence Barometer



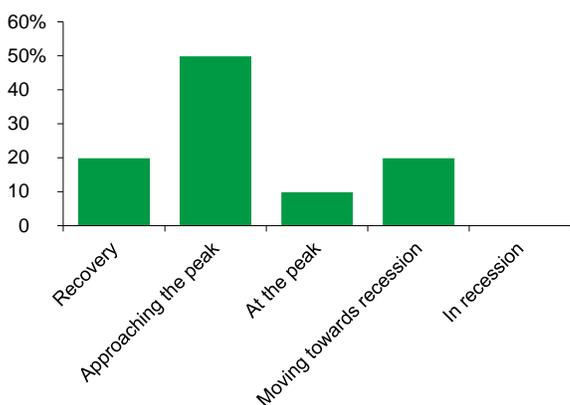
## State of economic cycle

Two years ago the overwhelming majority of banks (66%) and non-banks (86%) believed that the Caribbean was still in the recovery stage of the economic cycle. Last year, half of the banks and 57% of non-banks thought the economy was approaching its peak. This year 57% of banks and 50% of non-banks indicated the economy is approaching the peak with less respondents indicating a recovery phase and as stated previously, we received the first opinions that the economy may be moving towards recession. Although not a dramatic shift there appears to be a distinct movement in the economic cycle, specifically from left to right in the bar charts below.

### Banks' view on economic cycle



### Non-banks' view on economic cycle



## New landscape

In recent years there has been a unanimity of opinion that the financing landscape has changed. In that regard the traditional lenders such as the Canadian banks are not as dominant regionally as they once were, nevertheless, they still remain very much part of the new landscape. The industry's opinion regarding the current position of the Canadian banks is very clear.

83% (2018:77%) of bank respondents consider the best description of the new role of Canadian banks to be that they are "back in the market but more selective than before" with the balance (23%) seeing little activity from the Canadian banks.

The views of non-banks were broadly split equally, between those who saw little activity from the Canadian banks and those who saw them back in the market in a more selective role.

## So who else is financing tourism projects in the region?

We received lots of different responses to this question, many referring to local and regional banks and several other financing sources.

*"Family offices, high net worth investors and strategic corporate players."*

*"Seeing some interest from U.S. hedge funds."*

*"Debt/Real Estate funds."*

### Availability of capital

Respondents were asked whether they agreed that positive data such as the Caribbean Tourism Organisation's forecast of 6-7% growth in 2019 was still not translating into greater availability of capital. They agreed strongly with the statement.

*"There is general institution hesitation to release capital due to the economic uncertainty."*

*"Availability of capital is still targeting expansions and refinancing of existing cash flowing assets: New development outside of the all-inclusive sector remains challenging."*

However respondents seemed to think there is finance available for strong projects with the right metrics and stakeholders.

*"There is capital available for deals in certain locations to strong borrowers with track records."*

*"Capital still available for well structured/managed assets."*

**When asked whether lending positions had changed given the stronger operating key performance indicators and generally favourable outlook, the majority of banks and non-banks stated that their lending position had not changed.**

*"KPI/risk metric remain fundamental lending principles. Position remains highly selective and cautious."*

*"We finance typically on more modest indicators in projections to assess projects."*

*"We have been positive for a while."*

### Minimum Investment

Non-banks were asked whether insufficient scale was an issue when investing in the Caribbean and whether they had a minimum investment amount. Some respondents said they had a minimum, when on the other hand, most quoted a range of US\$10m—US\$100m with the majority, in the US\$10-US\$50m range.

*"Minimum US\$10m. Sweet spot between US\$25—US\$50m."*

*"Minimum would be US\$20m."*

*"US\$15m."*

*"US\$30m."*

*"US\$100m but the condo business model is a bit different."*



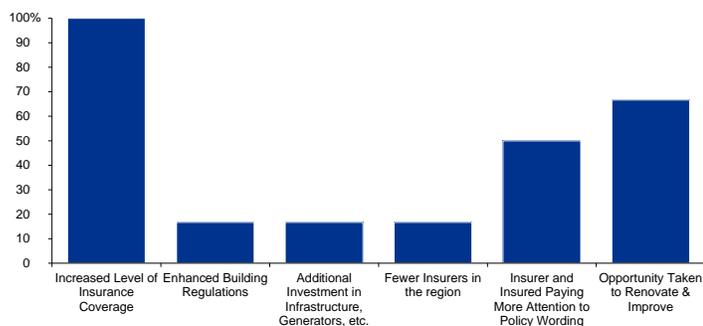
# Hurricanes

The 2017 hurricane season had a devastating impact on the region's tourism industry with several destinations experiencing direct hits from two major hurricanes; Irma and Maria.

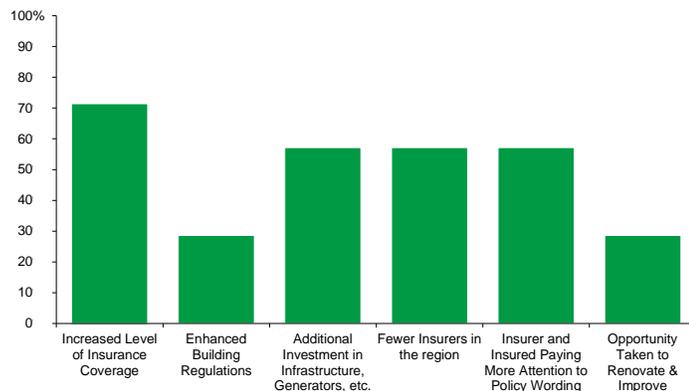
Accordingly, it is reassuring that all banks and non-banks retained their appetite for financing tourism projects in the region with 17% of banks and 14% of non-banks even expressing an increased appetite.

However, clearly some important lessons have been learnt, pursuant to the hurricanes.

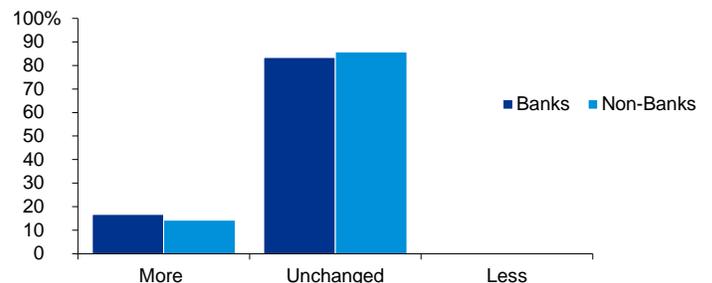
## Bank's opinions - Changes seen in industry as a result of 2017 hurricanes



## Non-bank's opinions - Changes seen in industry as a result of 2017 hurricanes



## Impact hurricanes have had on your financing appetite for tourism projects



## Insurance coverage

All banks and 71% of non-banks are seeing an increased level of insurance coverage following the hurricane.

## Policy wording

The majority of financiers are seeing both the insurer and insured pay more attention to policy wording.

## Renovation

Two thirds of banks are seeing resorts take the opportunity to renovate and improve.

## Exit of insurers

Interestingly, the majority of non-banks are seeing some insurers exit the region.

## New investment

The majority of non-banks are also seeing an increase in investment in infrastructure, generators, etc.

## Enhanced building regulations

Somewhat surprisingly, few financiers are seeing enhanced building regulations.



# Appetite for issuing senior debt

One of the most positive set of results we received was in response to a question as to what appetite financiers had for issuing senior debt to existing hotels.

Nearly all banks (86%) and non-bank respondents (88%) said they had a positive appetite for issuing senior debt to existing hotels for refinancing, expansion and renovation.

Compared to last year, the positive appetite for financing acquisitions declined for both banks, 71% versus 86% in 2018, and non-banks, 43% versus 67% in 2018.

Not surprisingly, new builds were the most difficult category to register a positive attitude, yet an unexpectedly high 57% of banks had a positive appetite for new builds, up from 33% last year. However, the positive attitude of non-banks declined from 43% last year to 29% this year.

These are generally high percentages, particularly for financing existing hotels. The generally more bullish attitude of banks versus non-banks is illustrated by the banks' surprisingly high positive appetite for new builds although both banks and non-banks exhibited a reduced appetite for financing acquisitions.

These results regarding the appetite for issuing senior debt are illustrated by quotes from several of our survey respondents. When asked what types of hospitality projects they have financed over the past year and where their focus will be over the next 12 months, their interest covered the entire spectrum.

*"Resort re-development and Villa re-development."*

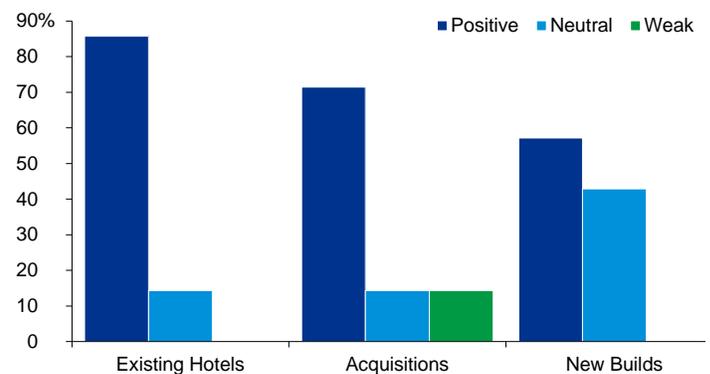
*"Refinancing one major hotel project and one major resort."*

*"Construction loan for a new luxury resort."*

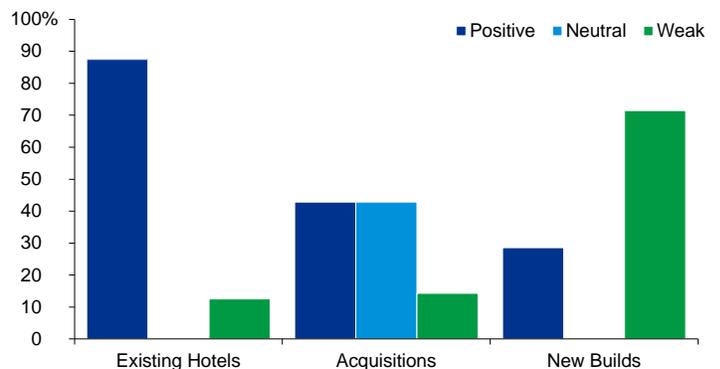
*"New hotel resort build."*

*"Some hotel purchases and a few restaurants."*

## Appetite for Issuing Senior Debt—Banks



## Appetite for Issuing Senior Debt—Non-banks

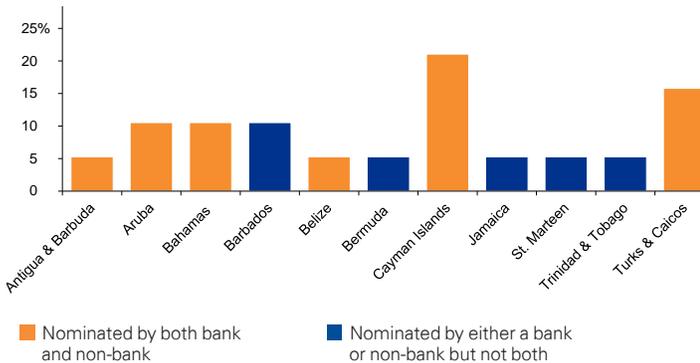




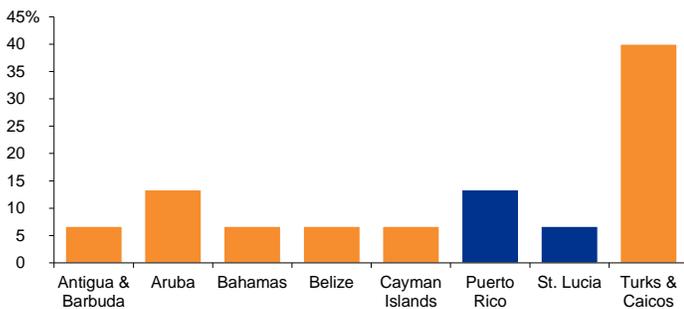
# Financing trends

When we looked at which destination in the Caribbean financiers are most bullish about, there were 13 different destinations put forward of which only six were nominated by both bank and non-banks and which are highlighted in orange. This further corroborates the position seen in recent years that the financing landscape has changed and that the new landscape involves financiers favoring a small number of jurisdictions for whatever reason, rather than financing projects across the entire region.

## Banks' top countries for new financing



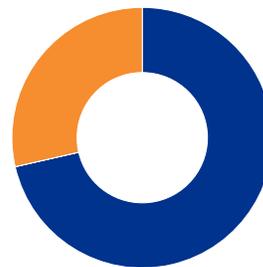
## Non-banks' top countries for new financing



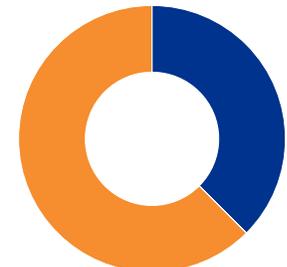
All financiers agree that either financing is more readily available this year or there has been no material difference when compared to last year. Half of non-banks believe it has become more difficult to conduct business in the Caribbean, although only approximately one third of banks share this view.

## Banks' view on financing environment this year compared to last year

■ Financing more readily available    ■ Financing less readily available    ■ No material difference

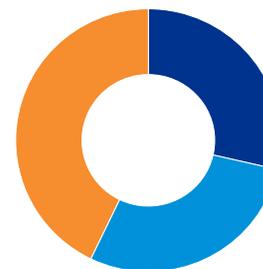


## Non-banks' view on financing environment this year compared to last year



## Banks' view on level of difficulty to conduct business in the Caribbean

■ More    ■ Less    ■ Just the same



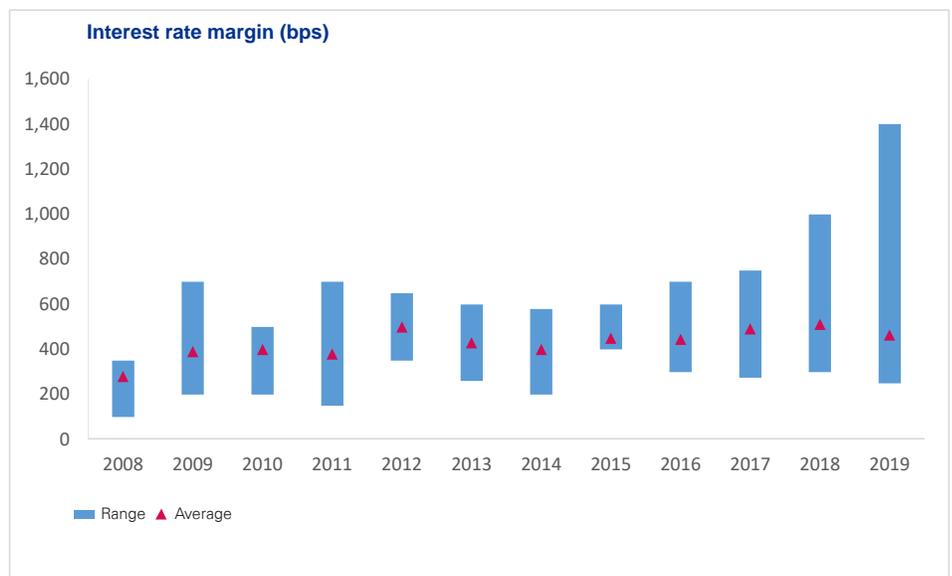
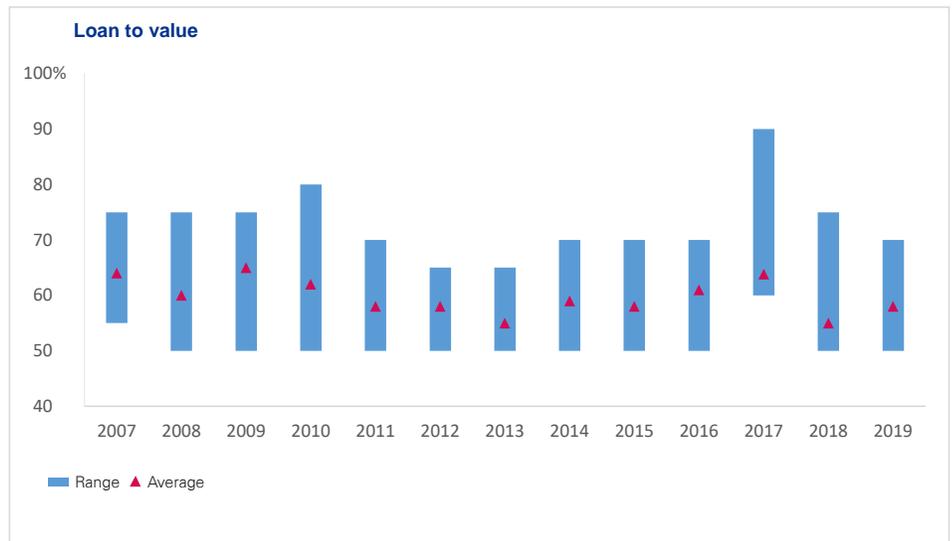
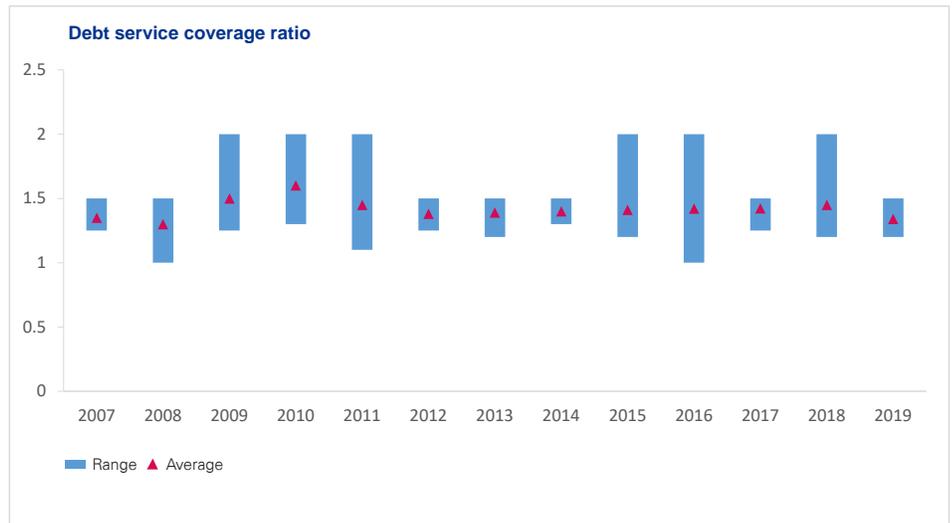
## Non-banks view of level of difficulty to conduct business in the Caribbean



Regarding the terms of financing, there have been no significant changes since last year although any changes have tended to be positive from a borrower's perspective. For example, the average loan to value ratio has risen to 58% and the average interest rate margin has fallen slightly to 464 basis points.

However, once again the big issue is not the terms but whether or not the financing is available.

It is highly unlikely that there is anything in the average loan terms that will prevent an investor moving forward should they be fortunate.



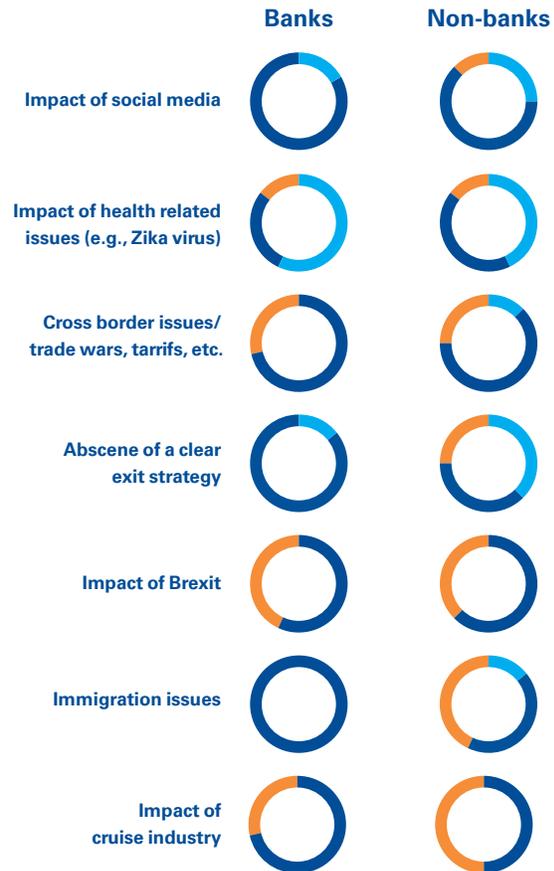
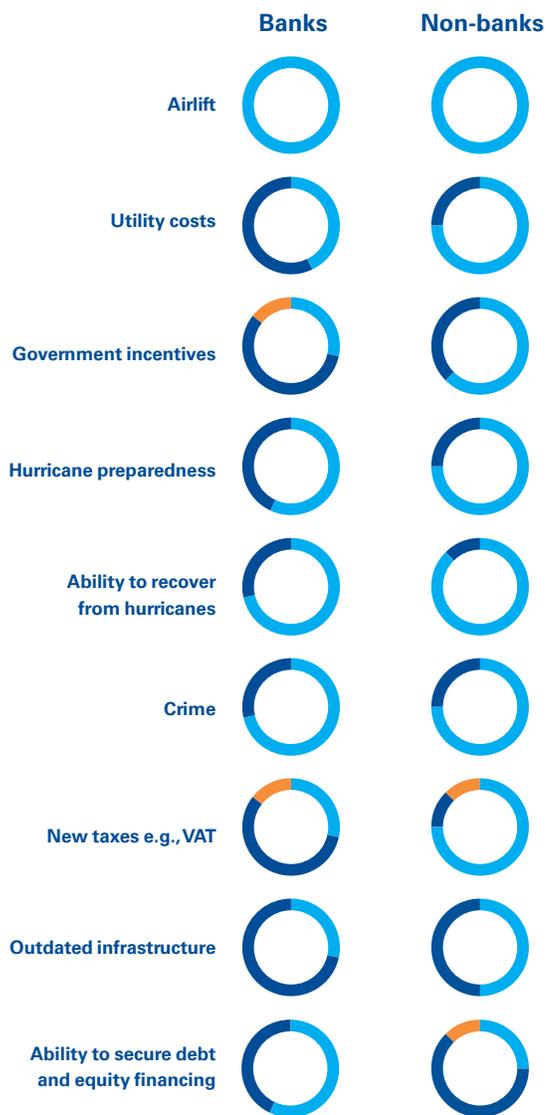
# Other trends

The critical issues impacting financing activity in the region are once again very clear.

Airlift was yet again identified as the most critical issue for both banks (100%) and non-banks (100%).

For banks the second most important issues were the ability to recover from hurricanes (72%) and crime (72%). Non-banks also attributed great importance to the ability to recover from hurricanes (88%). However, other issues volunteered by respondents included labour availability concerns, seaweed (sargassum) and the prospect of a U.S. recession—that word again!

■ Very important
 ■ Moderately important
 ■ Not important



**Respondents had some ideas on how these critical issues could be mitigated, which typically involved a role for governments in the region.**

*“By a comprehensive long-term tourism strategy by each jurisdiction that aligns other policy areas.”*

*“Investment in regional infrastructure and planning.”*

*“More cooperation between governments.”*

*“Local governments need to be educated to understand the impacts of their decision on the most important resource many islands have, tourism.”*

One respondent, who could be called a pessimist or realist depending on your viewpoint, stated:

*“These are a part of the regional landscape and unlikely to change.”*

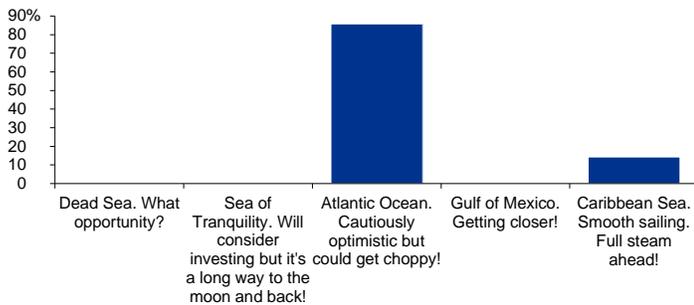


# A sea of opportunities

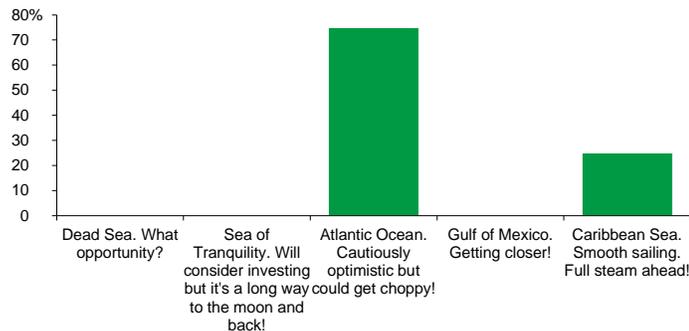
We asked financiers to consider the sea of opportunities for lending in the region.

Both banks (86%) and non-banks (75%) overwhelmingly voted for the "cautiously optimistic" option when asked how they would typically react to a lending opportunity in the Caribbean. Banks again proved more optimistic than non-banks.

## Banks' reaction to "sea of opportunities"



## Non-banks' reaction to "sea of opportunities"



**We asked survey participants what was the most "out of the box" innovative opportunity they could think of for the regional tourism industry in 2019.**

*"Private sector financing for convention centres."*

*"100% environment/sustainable resorts."*

*"Focus on medical tourism campuses attached to high-end product development."*

*"Issuance of work permits applicable with Caribbean for tourism employees."*

*"More cooperation on regional airline connections."*

*"A solution to remove the excess seaweed."*

**When asked, what single new opportunity excites you the most and fills you with optimism about the future of the tourism industry in the Caribbean, we received the following responses amongst others.**

*"Many luxury projects, back on the agenda."*

*"The move to transparency and accountability by governments."*

*"The state of the US economy."*

*"Infrastructure development."*

*"Continued prosperity in the Philadelphia/Boston/NY corridor."*

**When asked what opportunities respondents see for the region's tourism industry in 2019 and beyond.**

*"Airport Financing."*

*"Rebuilding opportunities in countries with hurricane damage."*

*"Many limited service/select service hotels across the region."*

*"Highly selective infill projects."*

*"Increase in employment opportunity."*

*"Many hotels in the luxury segment have benefitted from a complete refurbishment due to the local hurricanes."*

# KPMG's Caribbean Travel, Leisure and Tourism Contacts

Please contact the KPMG member firm represented in your country if you have any questions. KPMG member firms are represented throughout the Caribbean region, and have a specific knowledge and understanding of the business, cultural, economic and political facets of conducting business in each country.

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