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Small Texas bank doubles down on hotel lending

By John Reosti | September 10, 2020

A Dallas community bank sees opportunity in the hospitality industry.

While many other banks are trying to keep borrowers solvent, the $915 million-asset State Bank of Texas is hiring in hopes to gaining more clients. Its management is relying heavily on experience — hotel lending is the bank's biggest segment — and a view that the business will recover and thrive over the long run.

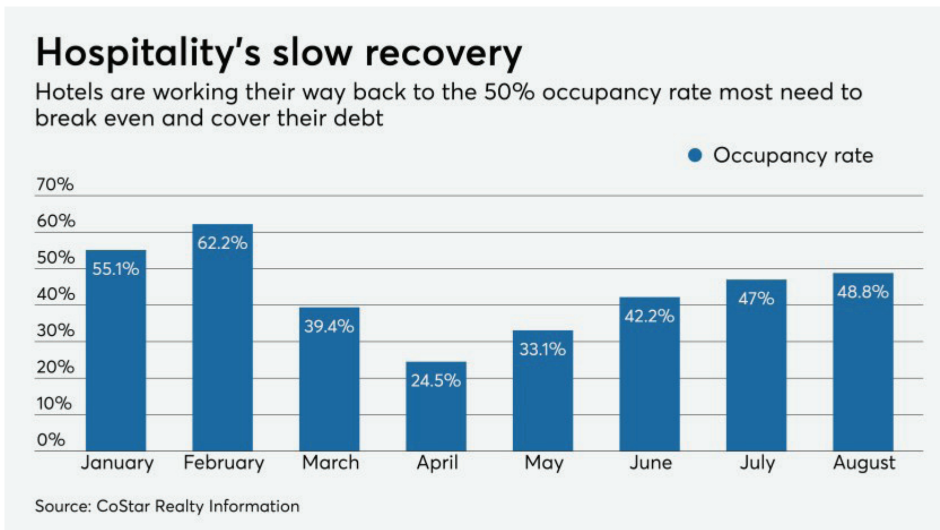
"We're seeing things stabilize, for the most part," Sushil Patel, State Bank's president, said in a recent interview. "At the end of June our deferrals had come down from their April peak by close to 50% and we think that by the end of the third quarter they'll reduce by another 50%."

State Bank is preparing for the hospitality industry's comeback, hiring Melissa Butler, a hospitality lender with 20 years of experience and a background in Small Business Administration lending. The plan is for Butler, who spent 13 years as a lender at PMC Commercial Trust, to lead an expanded SBA operation.

Butler's "focus on hotel lending to the individual owner-operator is right up our alley," Patel said. "It's an opportunistic hire for us. We have not done a lot of SBA lending traditionally."

State Bank is confident it can step into deals when other lenders pull back.

"There are still great hotel loans to be made to great borrowers," Patel said. "We want to be there."



Patel and his family — his father Chan is State Bank's chairman and CEO and the two brothers, Sushil and Rajan, hold key positions — own hotels in Dallas and New York. The elder Patel bought his first hotel in 1976, more than a decade before he helped found State Bank.

The hospitality industry is slowly recovering from the earliest days of the pandemic, when occupancy rates plummeted to an historic low of 24.5% in April, according to data from CoStar Realty Information.

"March and April was a free-for-all," Patel said. "Nobody knew how far we were going to fall. It was quite scary. Nobody had ever experienced this before."

Nationally, occupancy improved to 48.8% in August as many hoteliers neared the levels they need to break even, according to CoStar.

Most hotels need 55% occupancy to cover credit costs, said Brian Martin, an analyst at Janney Montgomery Scott. "Cash flow … is somewhat better than investors understand and appreciate, in our opinion," Martin wrote in a Sept. 4 client note.

At the same time, many banks have reported a decline in loan deferrals for hotel borrowers, though the rate of decline has lagged other sectors such as retail commercial real estate and commercial loans. As a result, hotel-related credits make up a large percentage of banks' deferrals.

Hanmi Financial in Los Angeles, for instance, recently reported that hotel-related deferrals fell by 26% between June 30 and Aug. 31. Because loans in other categories rebounded more rapidly, hotel credits make up two-thirds of the $6.2 billion-asset company's deferrals, up from 47% at the end of June.

Large number of hotels continue to struggle to generate enough revenue to pay expenses, said Chip Rogers, president and CEO of the American Hotel & Lodging Association. The trade group has warned of an historic wave of foreclosures, noting that nearly $21 billion in commercial mortgage-backed securities tied to hotel loans were delinquent by 30 days or more.

"Thousands of hotels are in jeopardy of closing forever, and that will have a ripple effect throughout our communities for years to come," Rogers said in a press release.

Patel acknowledged some of his borrowers are facing challenges.

"People are dipping into savings and other resources to stay current or to somehow service debt obligations and regular fixed expenses," he said.

Yet no two hotels are alike, and some types of locations are doing better than others. According to a report released last week by the AHLA, occupancy at limited-service suburban and interstate properties has surpassed 50%, while rates at full-service downtown hotels that cater to business travelers remain below 40%.

State Bank has historically emphasized loans to multi-unit owner-operators with 10 or fewer properties who take a hands-on approach to managing their hotels, Patel said. The bank has negligible exposure to the luxury sector, which has been one of the hardest-hit segments.

"Our focus in lending is upper midscale and below," Patel said. "Because of that focus, we're going to fare well."

The hotel business was a steady source of revenue for State Bank before the pandemic.

State Bank earned $192 million between 2016 and 2019, and its annual return on assets never fell below 4.5%. The bank remained profitable in the first half of 2020, earning $13.7 million, though net income fell 41% from a year earlier.

Still, the Patels are determined to stick to their knitting rather than chase after business lines where they lack expertise. In January, they hired another veteran hotel lender, Sandesh Patel (no relation) to serve as senior vice president of lending. Sandesh Patel also has experience as a hotel owner-operator.

"Our philosophy has always been, `stay in your lane, stick to what you know," Patel said. "Why would you want to lend to someone you don't know?"