Equity Research Report

September 6, 2023

CONSUMER: Lodging

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Reasons for this report

✓ Latest observations on forward-looking booking and pricing trends for US hotels and anecdotal learnings from industry contacts, including detail on the three main customer segments:
- Individual Business
- Group/convention
- Leisure
- First look into 2024

Sept RevPAR Monitor: Forward trends very encouraging, driven primarily by strength in group segment.

In this report we discuss:

- **Latest observations on forward-looking booking and pricing trends for U.S. hotels and anecdotal learnings from industry contacts, including detail on the three main customer segments:**
  - **Group/convention**
  - **Individual Business**
  - **Leisure (U.S. & Europe)**
  - **2024 first look**
- **Stocks/picks**
  - **Possible that MAR (Hold) at investor day this month notes 3Q North America RevPAR may come in near the high-end if not slightly above their guide**
  - **For C-corps: Hyatt (H, Buy)** remains our favorite name given strength in group and international leisure
  - **For REITS: Ryman (RHP, Buy)** remains our favorite name given group strength and self-help factors

Based upon our analysis of millions of future reservations for mid and higher-end U.S. hotels from multiple "big data" sources and from conversations with hotel owner/manager contacts and executives at very large travel agencies, we see no signs of any demand slowdown and in fact see 4Q23 U.S. RevPAR growth stronger than that of 3Q23. Driving this strength is **1)** a very strong pace of group business, **2)** a lower seasonal mix of (relatively underperforming) leisure business, **3)** a moderate acceleration of business travel growth especially for small and midsized business following 2Q23's relatively difficult y/y comp (following the Omicron-impacted 1Q22, some business and group travel was pushed into 2Q22, making for a difficult y/y comp in 2Q23), and **4)** international visitors returning to the U.S. (floridapolitics.com). **Additionally, based primarily on group bookings, 2024 looks very encouraging and we do not see anything material in the hotel booking data at this moment that indicates the sell-side "bear case" of negative y/y RevPAR growth in 2024 will come to fruition (nor will fundamentals slow in later 2023 as predicted by one vocal industry research & consulting firm, rather we see the opposite).**

It would not completely surprise us if MAR announced at their investor day at the end of this month that their 3Q23 U.S. + Canada RevPAR growth will likely come in towards the higher-end if not very slightly above their +2-4% guide and/or if they very modestly raise their RevPAR guide. *Unless the pace of bookings (intricacies of discussed below) falls off a cliff, we see U.S. RevPAR growth at least at the high-end if not slightly above MAR's 3Q23 U.S. + Canada guide of +2-4%.* While forward-looking U.S. RevPAR trends, ex-San Francisco, look encouraging, we remain more favorable on C-corps than hotel REITS as operating margin pressures for hotel owners and outsized exposure to the San Francisco market, a market whose pace of group bookings continues to look soft for 2024 and 2025, remain concerns for us with the hotel REITS.

The lodging stocks: While there were puts and takes in our latest data checks and industry conversations, overall we continue to summarize our view on the lodging sector at the moment as one of "relative optimism," *though more so for the global C-Corps and less so for the hotel REITS.*

- **Of the lodging stocks our favorite name continues to be Hyatt, which we see having several idiosyncratic catalysts.** Hyatt is a beneficiary of group strength primarily through its legacy portfolio but also to an extent the acquired Apple Leisure Group, the recovery of international higher-rated travel, strength in global leisure demand, a continued push to asset-light, a leading global rooms pipeline, and best of sector balance sheet.

- **For the hotel REITS, our favorite name is RHP.** At 75% of its business coming from groups/conventions, RHP has the greatest exposure to this customer segment and has no hotels located in the especially tech-heavy San Francisco area. We add that RHP's hotels are likely benefitting from several "self-help" factors including having properties in better condition than some other big box comparables and convention centers as well as what has proven to be a smart strategy of maintaining their property-level salesforce during the heart of the pandemic.
  - **As we detailed on Tuesday following our attendance at a local tourism conference, we continue to be cautious on San Francisco in the near-to-mid-term.** With the exception of RHP, most Lodging REITS have mid-single-digit to double-digit EBITDA exposure to the Bay Area including resorts outside the City of San Francisco that are impacted by the Bay Area economy (e.g. Napa, Sonoma, Big Sur, and Sausalito). Although we view the recovery of leisure demand is encouraging and leading corporate and group travel, weakness in convention demand and the tech industry will challenge the opportunity for hoteliers to push room rates. We also view weakness in convention center forecasts as a bad sign for City of San Francisco hotels and the overflow markets to the south and north (Airport area and Marin County, respectively).
  - *For further discussion on hotel operations, departmental margins and profits both in the U.S. and globally, please join us for a webinar with HotStats on Wednesday, October 4th.*

<u>**Our forward-looking observations by customer segment:**</u>

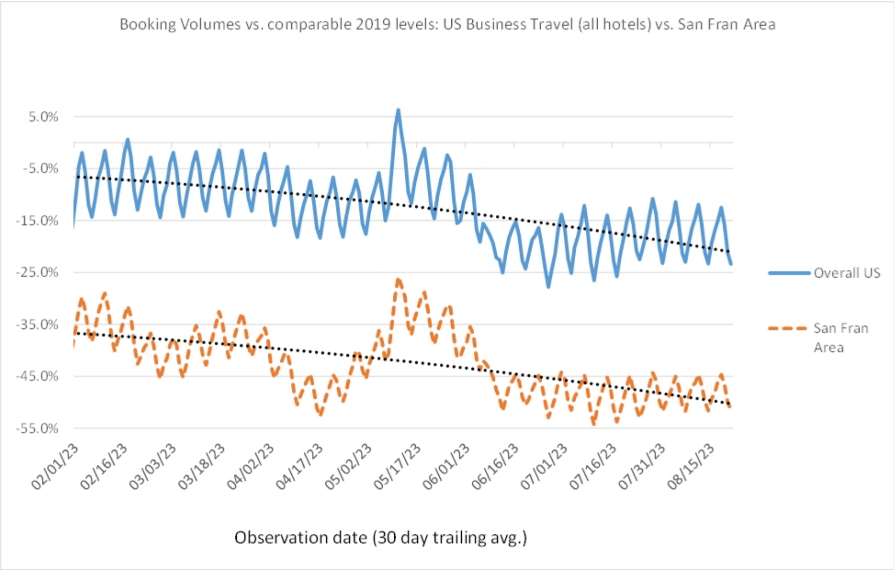
First, we need to highlight the biggest challenge at the moment with forecasting RevPAR growth (and we're sure hotel executive teams can identify with this). Depending on the customer segment, the pace of growth either accelerates or decelerates as arrival dates get closer with the leisure segment accelerating off of a very weak initial pace and the group and business travel segments decelerating off a very strong initial base of business. *While this acceleration/deceleration, as discussed below, is a major wildcard as to exactly where RevPAR growth will finish, our opinion is that the degree of deceleration, unless it substantially picks-up, will not be enough for the companies to at least not hit the high-end of their RevPAR guidances.*

- **Why has there been an <u>accelerating</u> pace of bookings for domestic leisure travel as arrival dates get closer?** We believe it due to resort hotels initially pricing too high and thinking occupancy/demand will not be affected by these higher prices. What these hotels are seeing is that customers are balking at higher prices, especially since they have far more travel options today than 12-18 months ago such as international locations and cruises, and **once such hotels have started to drop rates and/or increase promotions** one-two months out from arrival dates, occupancy has started to fill-in (costar.com).
- **Why has there been a <u>decelerating</u> pace of bookings for individual business and group customers as arrival dates get closer?** We believe it due to individual business and group customers having booked further out than at the same time last year and subsequently these customer segments have less travel needed to book as arrival dates get closer.

Specifically what we observe for 4Q23:
As a reminder, group demand traditionally becomes a larger part of overall U.S. occupancy and hotel revenues after Labor Day and the return to school. Specifically, group demand also shifts from a more social/leisure orientation in the summer to a heavier corporate/ convention mix in the fall.

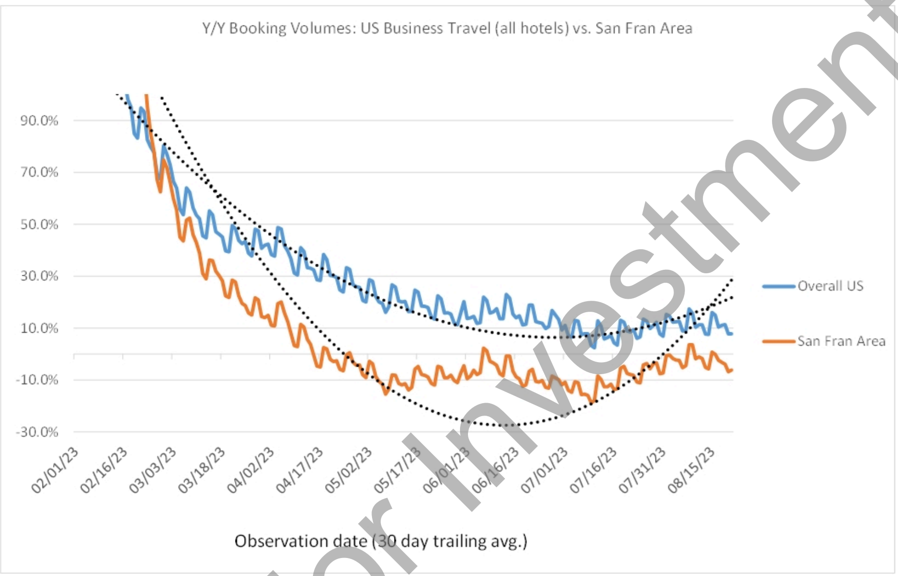
- **Group revenue pace for 4Q23 is currently tracking approx. +13-15% y/y (approx. half from occupancy, half from ADR).** However as noted previously, as arrival dates get closer the pace of revenue growth slows, most notably for expected occupancy growth. For example, August lost approx. 6 points of revenue growth in the 60 days prior due to a weak last minute pace of bookings but still finished approx. +5% y/y as that pace was tracking at a strong up low-double digits y/y back in June.
  - The above positive initial pace of Group blocks may have been best described by PEB's CEO Jon Bortz on the 2Q earnings call: *"It's critical to remember, however, that these positive pace figures are indicators. They're not guarantees of realized business. Of course, it's better when they're up, and up by a lot is better than up by a little."*
- **(Individual) transient business revenue pace at the moment for 4Q23 is tracking approx. +10-12% y/y (approx. two-thirds from occupancy, one-third from ADR).** However, as arrival dates get closer the pace of revenue growth slows, most notably for expected occupancy growth. For example, August lost approx. 4 points of revenue growth in the 60 days prior due to a weak last minute pace of bookings but still finished approx. +3% y/y as that pace was tracking up a strong mid-to-high digits y/y back in June.
  - **We observe that growth is primarily driven by mid and smaller-sized businesses as higher-end corporate business, as seen in "big data" from TRIPBAM, while positive y/y, is less robust.** *Please join us for a webinar with TRIPBAM on Thursday, September 21.* Specifically:
    - Corporate booking volumes remain down around 20% vs. comparable 2019 levels though they are up mid-high single digits y/y. See Exhibits 1 and 2.
    - Pricing on corporate bookings has been holding steady at approx. +5% vs. comparable 2019 levels and up low-single digits vs y/y. See Exhibits 3 and 4.
  - **In greater San Francisco where many full-service REITS have material exposure, excluding RHP, the demand trend lines are similar to the national level, but tracking at lower starting levels.** San Francisco area booking volumes are now about 50% below comparable 2019 levels though we have seen y/y pricing improve over the past 90 days.

Exhibit 1:



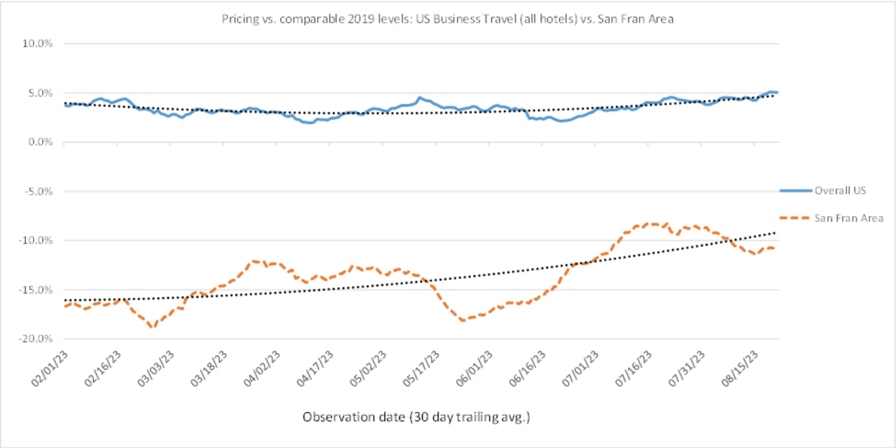
Source: TRIPBAM, Truist Securities Research

Exhibit 2:



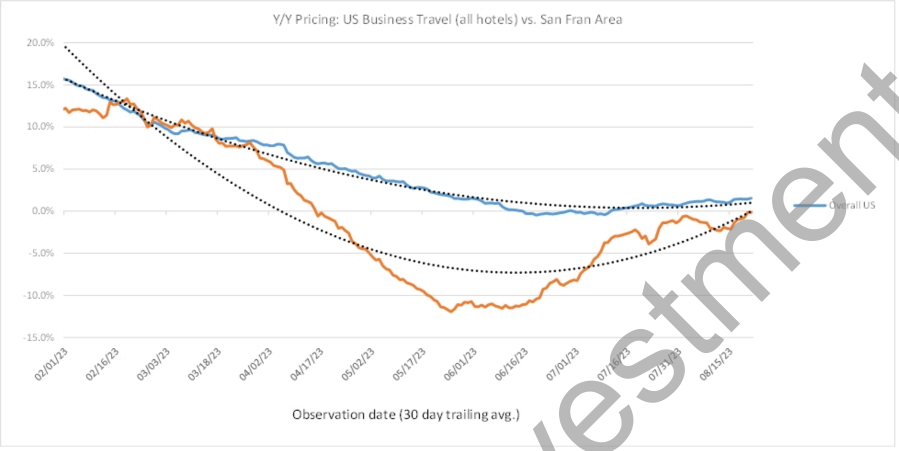
Source: TRIPBAM, Truist Securities Research

Exhibit 3:



Source: TRIPBAM, Truist Securities Research

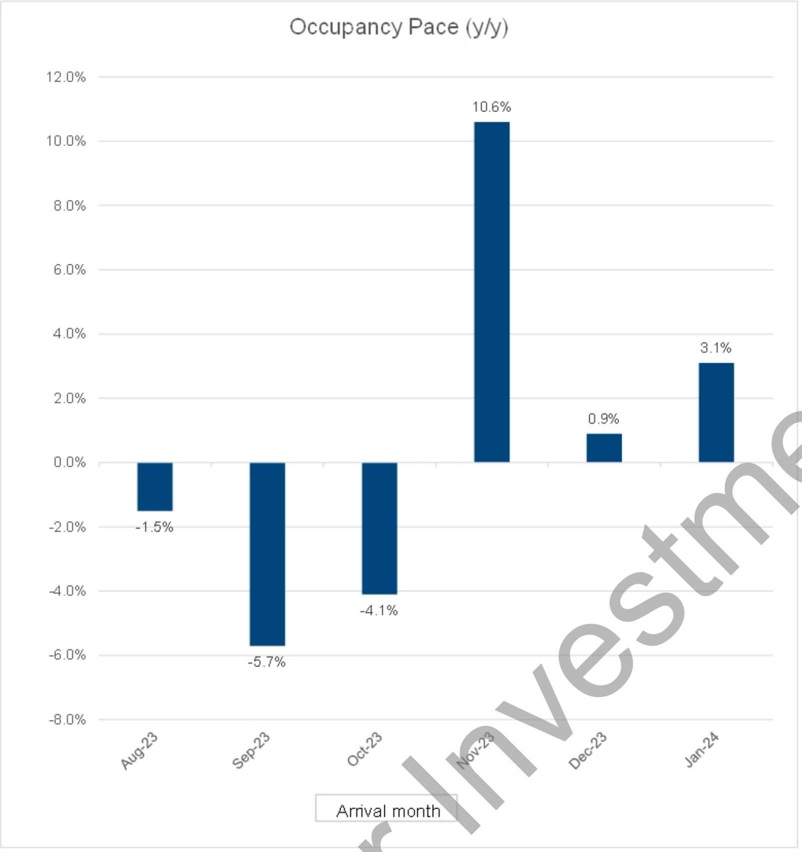
Exhibit 4:



Source: TRIPBAM, Truist Securities Research

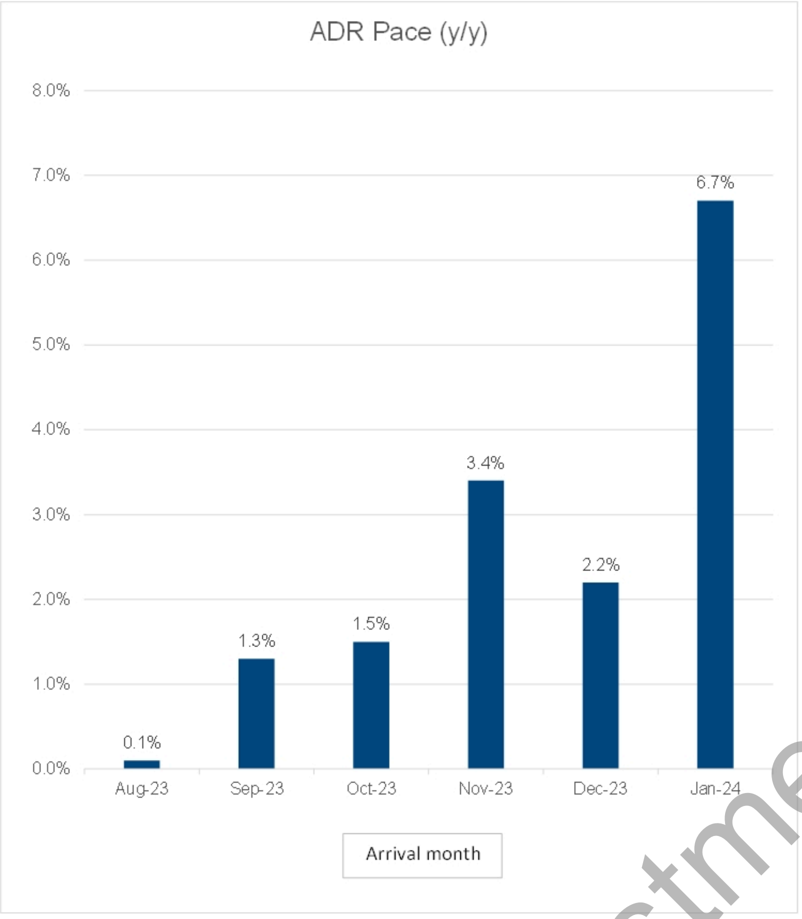
- **Leisure (full-service resort hotels) revenue pace at the moment for 4Q23 is tracking approx. +3-5% y/y (approx. one-third from occupancy, two-third from ADR).** However, as observed for this past summer, as arrival dates get closer the pace of revenue growth **improves**, most notably for expected occupancy growth. For example, August gained approx. 5 points of revenue growth in the 60 days prior due to a strong last minute pace of bookings and likely finished flattish y/y for revenue growth vs. what was looking like a very weak month just 60 days prior.
  - To further help gauge the strength/weakness of higher-end U.S. leisure travel we look at future occupancy, rate, and RevPAR pace for hotels at western U.S. ski resorts, popular destinations for both summer and winter vacations (source DestiMetrics). Our observations on forward occupancy for hotels at U.S. ski resorts:
    - **Y/y occupancy growth was tracking deeply negative for the summer months though last-minute demand pickups combined with reduced pricing (or not pushing room rates as hard) helped shore-up weakness in occupancy.**

Exhibit 5:



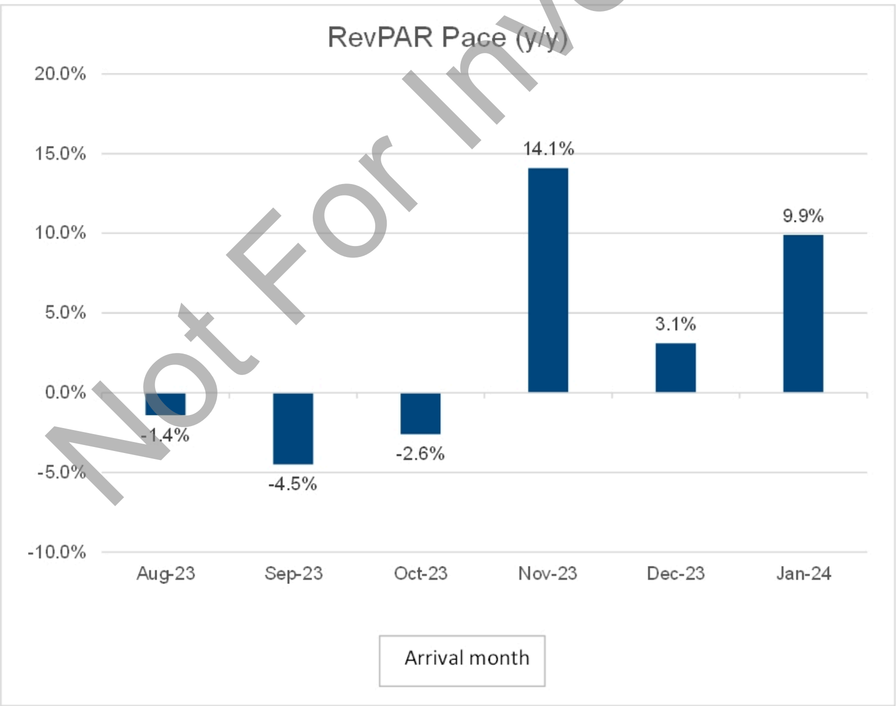
Source: DestiMetrics, Truist Securities Research

Exhibit 6:



Source: DestiMetrics, Truist Securities Research

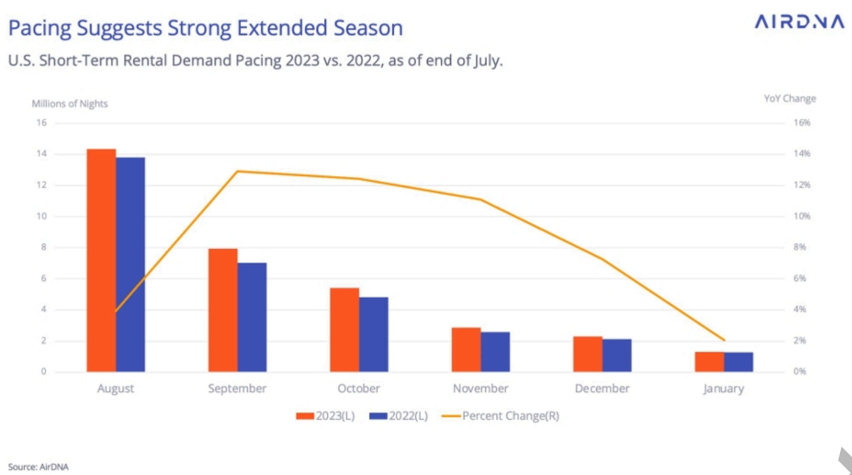
Exhibit 7:



Source: DestiMetrics, Truist Securities Research

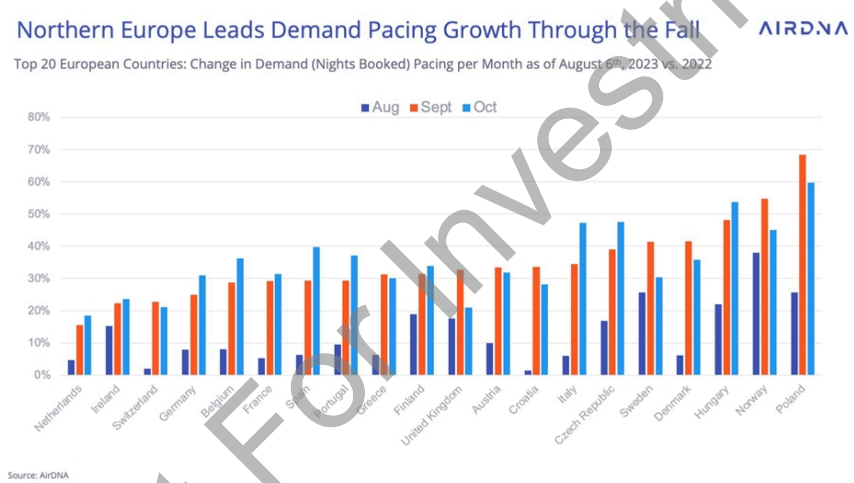
Additionally to gauge strength/weakness in leisure travel we look at data from Airdna. Forward-looking data on short term rentals from Airdna suggests continued strength in demand (bookings) through the fall and early winter. Bookings already made for the months of September through November are more than 10% ahead of where they were at the same point in 2022. However, given the tremendous amount of new short term rental supply coming on, that demand is being diluted amongst more properties. That said, the pace of new short term rental supply additions is decelerating. Short term rental supply was up 12.1% y/y in July, a deceleration from +13.7% y/y in June and +24.4% y/y the same time a year ago.

Exhibit 8:



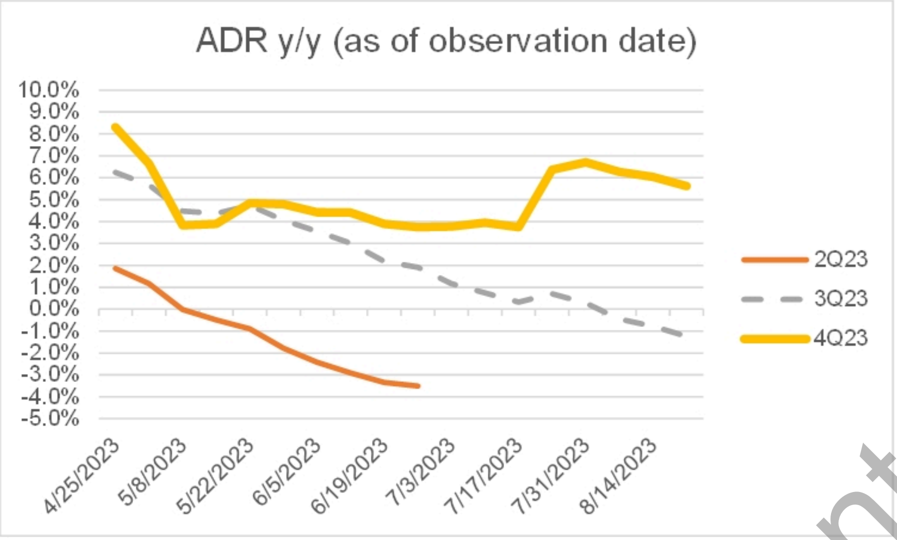
Europe: Per Airdna, as of last month, short term rental demand for the rest of 2023 is pacing 17% ahead of the same time last year. Specifically, September and October demand are pacing 31% and 33% above last year and November and December demand are pacing 20% above last year.

Exhibit 9:



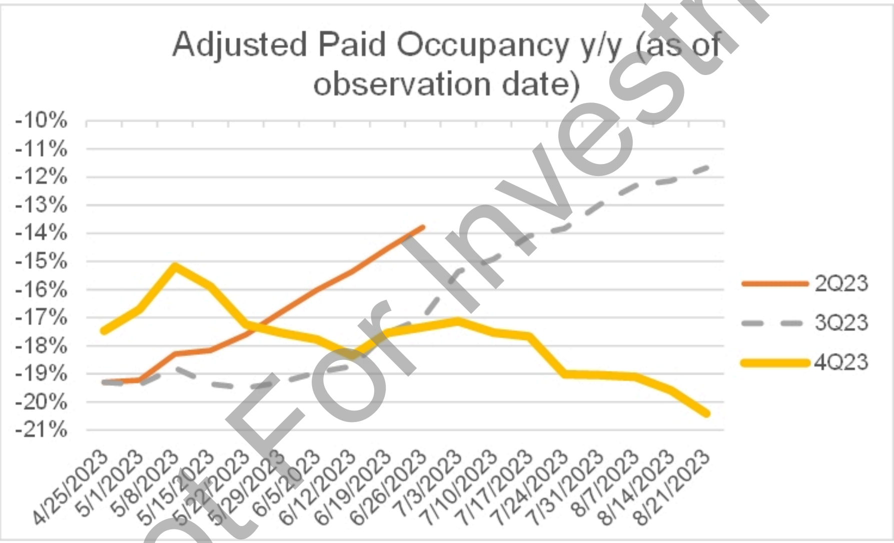
Finally, we wrap our leisure discussion with analysis from Key Data. Our data set tracks bookings and pricing on thousands of U.S. condos and resorts, and we view Key Data as having about six months of forward visibility. In our review of Key Data, we see ADR down low-single digits for 2Q23-3Q23 but same-store occupancy on the books extremely soft, the later which we mainly attribute to the tremendous amount of new short term rental supply growth over the past several years. For 4Q23, ADR is currently tracking up mid-single digits with same-store occupancy down over 20% y/y. Similar to what we observed for 2Q23-3Q23, we believe owners will begin to pull back on ADR growth in order to improve occupancy as arrival dates get closer.

Exhibit 10:



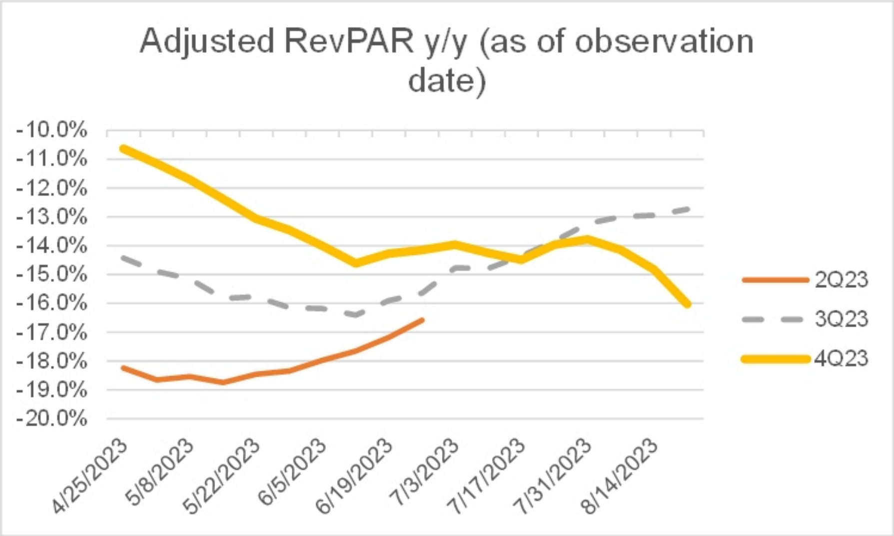
Source: Key Data, Truist Securities Research

Exhibit 11:



Source: Key Data, Truist Securities Research

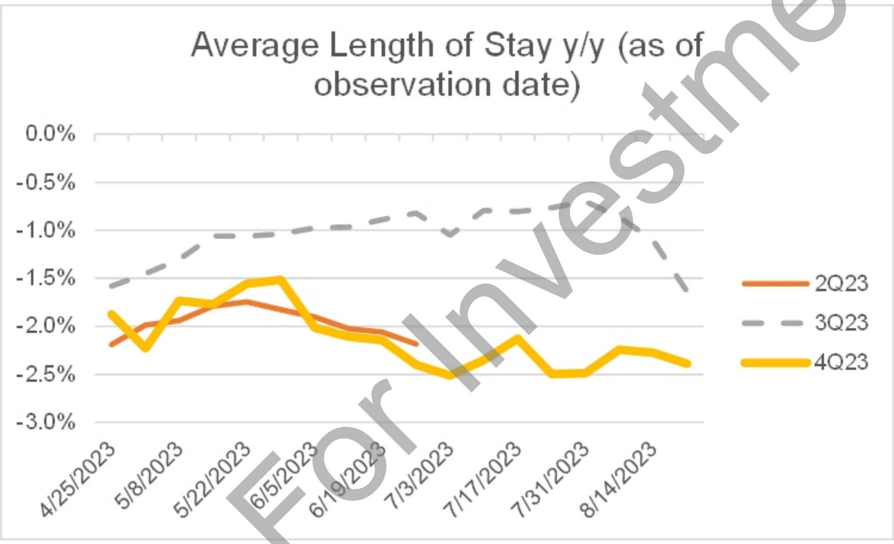
Exhibit 12:



Source: Key Data, Truist Securities Research

- **We also analyze length of stay from Key Data.** We are not terribly surprised to see length of stay compress in 2023 versus 2022 with less remote work combined with the higher cost of travel. That said, the average length of stay is modestly down y/y suggesting still a healthy degree of work/leisure flexibility for longer vacations.

Exhibit 13:



Source: Key Data, Truist Securities Research

First look into 2024, and it looks encouraging (so far…):

- **Groups:** At this moment, what is on the books for U.S. hotels for 2024 is approx. 95% from group "blocks" and we see the pace of the group blocks and pricing on them as the best "indicators" of how that segment of the business is shaping up. Additionally, a strong pace of group bookings typically helps hotels yield manage the remaining unallocated occupancy for optimal RevPAR performance. **Specifically, we observe that current revenue pace from these group blocks is up approx. 8-10% y/y for 1Q24 and up 25-30% for 2Q24 y/y with March being negatively impacted by the timing of the Easter shift whereas April looks exceptionally strong due to this shift (Easter moves to March from April last year).** By comparison, on its 2Q23 earnings call, MAR noted that its group business is pacing up 14% y/y for 2024 and HLT noted its group position pacing up 13% y/y for 2024 (we believe these figures are highly U.S.-centric and due to the booking curve are heavily weighted to 1Q24). *Of course, we do not think that group results will finish at these lofty growth rates, and our best estimate (art/experience + science) is that actual group growth results will be cut by at least half from the above due to the aforementioned decelerations as arrival dates get closer.*
- **Leisure:** Will 2024 be a year of "normalization" for U.S. leisure/resort hotels following 2023 where many Americans headed to Europe for vacations; or in other words will these Americans who finally got to visit Europe after not doing so since 2019 take their vacations in the U.S. after "checking the box" for international travel in 2023? While there is no hard reservation data at this point to quantify such speculation nor will there be until around March of 2024, our intuition will be that some Americans who elected to travel internationally this year will decide to take their vacations domestically next year.
  - **What we do know is that 2024 leisure travel looks to start with a bang due to New Years Day shifting to a Monday from a Sunday.** This subsequently makes it more likely that that entire first week of January will be a school holiday for many districts. Already we see outsized RevPAR strength for January in booking data for hotels at U.S. ski resorts. That said, for U.S. resorts, at this moment they are on average only approx. 30% booked for Christmas/New Years weeks, so still lots of occupancy to fill-in. As noted previously, we observe this January strength in the ADR and occupancy paces for Western U.S. ski resorts.
- **Government customer:** Government business represents approx. 5-10% of business for U.S. hotels (at the lower-end for full-service hotels, at the higher-end for limited service). While it is difficult to predict/forecast what demand from this customer may be for 2024, a positive indicator for hotels is 2024 government per-diems up 7% y/y (to $107 from $98), following 2023 where they only increased 2% y/y (to $98 from $96).

Exhibit 14:

Segmentation By Company

Lodging REITS	Transient Corporate*	Transient Leisure	Group
DRH	35%	35%	30%
HST	40%	25%	35%
PEB	35%	40%	25%
PK	35%	35%	30%
RHP	5%	25%	70%
RLJ	55%	25%	20%
SHO	35%	30%	35%
C-corps	**Transient Corporate***	**Transient Leisure**	**Group**
CHH	45%	45%	10%
H	20%	50%	30%
HLT	50%	20%	30%
MAR	50%	30%	20%
WH	30%	70%	less than 1%
Experiential Leisure	**Transient Corporate**	**Transient Leisure**	**Group**
MTN	0%	95%	5%
PLYA**	0%	90%	10%
Cruise Lines	**Transient Corporate**	**Transient Leisure**	**Group**
CCL	0%	100%	0%
NCLH	0%	100%	0%
RCL	0%	100%	0%
Vacation Ownership	**Transient Corporate**	**Transient Leisure**	**Group**
BVH	0%	100%	0%
HGV	0%	100%	0%
TNL	0%	100%	0%
VAC	0%	100%	0%

Source: Company reports, Truist Securities Research

Companies Mentioned in This Note

Airbnb, Inc. (ABNB, $142.29, Hold, C. Patrick Scholes)
Hyatt Hotels Corporation (H, $111.46, Buy, C. Patrick Scholes)
Host Hotels & Resorts, Inc. (HST, $15.90, Hold, C. Patrick Scholes)
Pebblebrook Hotel Trust (PEB, $14.61, Hold, Gregory Miller)
Playa Hotels & Resorts N.V. (PLYA, $7.37, Buy, C. Patrick Scholes)
Ryman Hospitality Properties, Inc. (RHP, $87.20, Buy, C. Patrick Scholes)
Sunstone Hotel Investors, Inc. (SHO, $8.98, Hold, C. Patrick Scholes)

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