Asia-Pac hotel profits -45% to -216% y/y in Feb.: bad for C-corps; leading indicator for U.S. REITS

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What's Inside

Analysis of HotStats data on January/February 2020 revenue and profit results; impact to Lodging C-corps and REITS

What's Incremental To Our View

Our analysis of Asia-Pacific lodging data from HotStats indicates enormous declines in hotel revenues and profits. **The virus demand shock impact is widespread in major China markets: YTD Total RevPAR down ~ 40-60% y/y; hotel profits down triple digits y/y.** Other Asia-Pacific countries' Feb. profits -45% to -122% y/y ex-India (flattish).

Impact:
Hotel C-corps: Far lower Asia-Pac base and incentive fees for 1Q20 and likely the rest of 2020 as occupancies slowly rebound.

Lodging REITS: HotStats data an indicator for an ugly March and April in the U.S.; profits could be down at least 40-60% y/y.

HotStats released February YTD revenue and profit results for Asia-Pacific hotel markets (links here and here). We remind investors that HotStats is our primary provider of data for our US Hotel P&L Analyzer note (our most recent note is linked here); we find HotStats a highly reliable source of in-depth hotel property-level P&L data. This data has great relevance to both Lodging C-corps (e.g.: base and incentive fees, profits for owned hotels) and REITS (e.g.: revenue trends, labor costs, and profitability).

Note: the Asia-Pacific HotStats data discussed below is primarily full-service and select-service hotels (likely an excellent representation of Lodging C-corp exposure in the region, although more relevant for H/HLT/MAR than CHH and WH). **Importantly, some Asian markets took forceful and fast action in "social distancing" vs. what we have seen in other world regions. We assume that such actions could lead to a bigger near-term revenue/profit hit in Asia (see February results below) but also potentially a faster recovery vs. the varied virus containment approaches in other regions of the world.**

- For example, some U.S. Spring Break destinations remained busy into mid-March (Washington Post). European action has been far from uniform by country.

Asia Pacific YTD February y/y results per HotStats indicate double-digit Total RevPAR declines in most major Asia-Pacific markets and more significant profit declines due to hotel operating leverage.

- **January profits were generally flat-to-up for most major Asia-Pacific markets ex-China. The declines became pronounced in February:**
  - **China:** January -45.1%; February: -216.4%.
  - **South Korea:** January: +28.2%; February: -122.4%
  - **Japan:** January: +2.9%; February: -58.5%
  - **India: the sole major outlier in the HotStats dataset.** January: +1.8%; February -3.6%
- **China:** Total RevPAR (room and other revenues) -51.0% YTD February y/y; Gross Operating Profit per available room (GOPPAR) -108.3% YTD y/y.
  - Results were down materially in all provinces listed by HotStats including markets far from Wuhan. **Assuming continued containment in major Asian countries, results in March and April could be somewhat of an indicator for the North American and European recovery (hopefully) later this year, although we note that domestic Chinese travel will likely rebound faster than international inbounds (and Asian inbounds likely faster than Europe and North America given flight restrictions).**
  - **Total RevPAR YTD among major markets well represented by the Lodging C-corps down ~50%:** these markets include Beijing, Guangdong Province (Guangzhou/Shenzen), Hainan (Sanya), and Shanghai/regional provinces (Jiangsu, Zhejiang)
    - Hubei Province (Wuhan): -37.8% (we note that some hotels were likely closed through February)
    - Hong Kong: -60.7%
  - **GOPPAR y/y declines were materially negative in every province but more varied by market**, reflective in our view of the differing labor costs across the country.
    - **Beijing/Guangdong/Hainan/Shanghai area: down ~80% to more than 120%.**
    - Material underperformers include areas far from Wuhan: Liaoning Province -271.8%; Tianjin -302.2%.
    - Hubei: -78.2% (again, we assume some hotels were likely closed)
    - Hong Kong: -103.8%
- **Other Asia-Pacific markets**:
  - **Relative outperformers although still negative include Australia and India** (major market YTD Total RevPAR down single digits, GOPPAR flattish to -14%).
  - **Most other Asia-Pacific YTD Total RevPARs were down low double-digits with GOPPAR down 20-35%.** Markets represented include: Japan, Malaysia, Singapore, South Korea, Thailand, and Vietnam.

Lodging C-corp 1Q fee generation from Asia Pacific cut materially:

- We state the obvious that base and incentive fees will be down materially in 1Q. March may start to provide a relief as China new virus incidents have declined considerably (BBC). However, we would assume the occupancy recovery may be more notable in April assuming a greater "all-clear" is evident.
- Importantly, there are few incentive management fee (IMF) hurdles in Asia-Pacific. For markets where there is profitability, the C-corps will likely receive some proceeds. However, given the overweight to China (assume roughly half of fees from Asia-Pacific are from China), **both base and IMF fee contribution from Asia-Pacific may be down 50% or more in 1Q**.

How the Asia-Pacific results provide some indicators for North America and European markets in March and beyond:

- We start by noting February Rooms RevPAR was -49% in Asia-Pacific (China -82%), per STR. We do not consider -50% RevPAR to be an unrealistic expectation for March in some major U.S. markets especially given reported sub-20% occupancy and hotel closures becoming more pronounced starting in mid-late March. One of the first large public owners to have made hotel closure announcements in the U.S. was Pebblebrook (PEB, Miller, Hold). As we expected many public and private owners are following suit with hotel closures and furloughs/layoffs (WSJ).
- However, we do not consider the GOPPAR declines in parts of Asia-Pacific to be as relevant to much of Europe and North America as the property-level labor force is less expensive in many Asian markets (although with heavier staffing). Additionally, many of these markets have heavier food and beverage operations than what one tends to find in Europe and North America. **Of the major Asia-Pacific markets that have similar operating models to the U.S., we look at Australia and Japan as the best equivalents:**
    - Japan YTD Total RevPAR of appx. -11% vs. GOPPAR of -29%
    - Sydney: Total RevPAR -8.1%; GOPPAR: -13.5%
    - Melbourne: Total RevPAR -6.9%; GOPPAR: -10.9%
- **From the above, we note that GOP margins fell approximately 150-300% that of Total RevPAR, reflecting the profit hit from operating leverage. We find this range a good starting place for evaluating the potential profit loss for Upper Upscale and Luxury hotels in the U.S. given the unprecedented situation of hotels running very low occupancy.** We advise clients that the material EBITDA margin reductions after 9/11 and the Global Financial Crisis provide modest precedence as U.S. Room RevPARs fell at peak 30-35% in the worst month and by and large most hotels stayed open. Having hotels close down en masse has not occurred since the Great Depression, where hoteliers sometimes kept room lights on simply to give the impression that hotels were busy (such marketing efforts would not work today).
- **For hotels that temporarily close, we assume hotels can cut 70-90+% of expenses (70% for big labor-intensive hotels and super-luxury hotels; 90+% for lower-labor intensive hotels and at lower price points).**

Hyatt, InterContinental, and Marriott have the greatest exposure to Europe and Asia. From Europe, MAR generates approximately 15% of EBITDA, IHG (NR) 15%, WH (Buy) less than 5%, and H (Hold) and HLT 10% each. Of these companies, H and MAR have the greatest exposure to Asia (~10-20% of EBITDA). Each of the other companies generates 5% to 10% of EBITDA from the Asia-Pacific region.

Companies Mentioned in This Note

Choice Hotels International, Inc. (CHH, $58.21, Hold, C. Patrick Scholes)
Hyatt Hotels Corporation (H, $48.66, Hold, C. Patrick Scholes)
Hilton Worldwide Holdings Inc. (HLT, $69.39, Hold, C. Patrick Scholes)
Marriott International, Inc. (MAR, $79.14, Hold, C. Patrick Scholes)
Pebblebrook Hotel Trust (PEB, $9.94, Hold, Gregory Miller)
Ryman Hospitality Properties, Inc. (RHP, $32.70, Hold, C. Patrick Scholes)
Wyndham Hotels & Resorts, Inc. (WH, $28.83, Buy, C. Patrick Scholes)
InterContinental Hotels Group (IHG, $35.85, NR)

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