Key themes from STR Asia-Pacific hotel trends call: Still a long road to full recovery in China...

...trends portend an even longer recovery in the US (at least it's a recovery)

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What's Inside

Our takeaways following our investor call with the head of hotel data provider STR's Asia-Pacific region

What's Incremental To Our View

Yesterday we hosted an investor call with the Area Director of STR for Asia-Pacific. We view lodging trends in Asia-Pac as leading indicators for other regions.

China: STR's trends are in-line with our expectations, slow growth led by low-rated leisure. Most hotels have reopened. Urban business and luxury travel are lagging (limited international travel).

Other countries: Disparate results in some respects reflective of government lockdown policies: strict enforcement = faster recovery.

STR forecasts an elongated recovery in Asia-Pac, not V shaped. We/STRH call it a checkmark shape for the US.

Our call with Jesper Palmqvist from STR's Singapore office provided numerous insights to the first region severely impacted by COVID-19 and the first region to start showing the beginning of a lodging demand recovery. We continue to assert that the recovery trends and consumer behavior from these markets has great relevancy as forward indicators for other lodging regions, including the U.S. That being said, we have stated that China and some other markets enacted stricter lockdown policies (and for some countries superior testing) than many other parts of the world and we view said lockdown/testing impact has resulted in a faster recovery than what we may see in some major European and North American markets.

Key themes from STR are as follows:

Recovering first: domestic, local/accessible, leisure, weekend, lower-rated demand. In China: Midscale and Economy hotels have regained half their occupancy from last year (50% today vs. 75% in 2019 and 25% around 45 days ago). As we discussed in our earnings preview, we/STRH assume similar patterns may emerge in the U.S. where domestic low-rated leisure emerges faster than corporate and group demand. **The hotel companies in our coverage universe with the greatest exposure to mid-scale and economy segments are WH and CHH whereas the hotel REITS have the least exposure.**

- Recovering slower in China per STR: corporate, group, and international. Luxury occupancy in China is currently in the 25% range vs. 5% around 45 days ago and 65% in 2019. **We assume a similarly slower recovery for U.S. luxury, fly-to city-center urban markets, group-oriented hotels and resorts, and cities with a larger mix of Asian and European international demand (especially West Coast, Hawaii, NYC, and Florida). Given the above, we assume a slower REIT recovery for RHP, followed by HST and PK, with mixed trends for DRH, PEB, RLJ, and SHO.**
  - Major Tier 1 Chinese markets note similarly weaker trends with Hangzhou's leisure areas (we assume West Lake) supporting the market's near 50% occupancy vs. nearby Shanghai softer. Beijing as a more corporate/government market is the softest of the three cities discussed by STR in depth.
- Positively, while more than half of Chinese hotels were closed in February, over 90% are open today in all chain scales.

What will the demand recovery curve look like? STR assumes a V-shape is unlikely. We noted similarly in mid-March for U.S. Lodging REITS. Partially possible per STR: a U shape. However, STR points to a W-like recovery curve as another possibility until the virus is cured or controlled. **We/STRH call the U.S. recovery an elongated check-mark shape.**

A high level theme: there are encouraging trends for countries with strict shutdown policies and public cooperation. China has already seen leisure rebounds during April holidays. Further, a positive development for Beijing -- announced just hours before our call -- were the meetings dates set for the annual parliament meeting. As this event was delayed by two months, we view the decision by the government to set the meeting in late May as a sign of confidence that the virus issues are largely a non-factor in the important capital city and business-focused market (CNN).

- **Sentiment for domestic Chinese business travel was more encouraging with STR surveyed participants generally expecting normal travel in 2H20 (vs. 25% in 2021+). STR also noted that some group travel was occurring - mostly smaller meetings of under 100 participants. <u>We are nowhere at that stage in the U.S. with absolute group occupancy less than 3% in recent weeks.</u>**
- STR pointed to more varied virus control policies in the Philippines (perhaps somewhat similar to the U.S.) as resulting in generally higher overall occupancy patterns within the region -- but with big swings in demand.
- South Korea presents some encouraging signs but there were far more strict shutdowns, testing, and public cooperation vs. the U.S. so not apples-apples.
- **STR also spoke to another important factor in distinguishing recovery patterns: the strength of the domestic travel market.** For Thailand, much of the resort and luxury demand is driven by international travel. In Australia, strong domestic leisure weekend demand can provide an opportunity for a rebound even if international inbound travel is limited. **We view some comparability in the U.S.; some low incident leisure markets where social distancing is easier may see a faster recovery.**

Other major regional C-corp markets ex-Mainland China have varied results.

- **Japan:** results are "diving" in April given a state of emergency and closures.
- **India:** there has been an extension of the government lockdown with over 50% of STR's sampled hotels closed.
- **Australia and Fiji:** should be on the path to recovery, but again far more strict lockdowns and public cooperation than the US, so not apples-apples.
- **Hong Kong:** occupancy levels continue to remain in the 20s (we note that this market historically was a major inbound business and leisure market from Mainland China and worldwide).

STR ended the prepared remarks by noting "everything will be OK in the end...it's not yet OK...so it's not the end". We/STRH assume similarly. We still feel very confident about the long-term consumer desirability to travel whether for work or leisure. There are plenty of cases suggesting consumers ***eventually*** resume travel beyond previous peak levels post-natural disasters, terrorism, and due to medical incidents (Zika, SARS, MERS, etc.) **However, we do not think that the occupancy recovery will be clearly apparent until there is a vaccine and/or significant testing. And even with an occupancy recovery, an outstanding question of the virus economic impact (and potential loss to rate integrity) remains outstanding for RevPAR to recover to pre-virus levels (we contend**

this recovery will likely take years). STR suggested no significant loss to rate integrity in Asia-Pacific; we view the loss of rate integrity following a U.S. recession to be a more likely scenario in upcoming months as U.S. hotels reopen and fight for demand.

Companies Mentioned in This Note

Choice Hotels International, Inc. (CHH, $78.15, Hold, C. Patrick Scholes)
DiamondRock Hospitality Company (DRH, $6.27, Hold, C. Patrick Scholes)
Host Hotels & Resorts, Inc. (HST, $12.57, Hold, C. Patrick Scholes)
Pebblebrook Hotel Trust (PEB, $12.00, Hold, Gregory Miller)
Park Hotels & Resorts Inc. (PK, $9.69, Buy, C. Patrick Scholes)
Ryman Hospitality Properties, Inc. (RHP, $37.78, Hold, C. Patrick Scholes)
RLJ Lodging Trust (RLJ, $9.91, Sell, Gregory Miller)
Sunstone Hotel Investors, Inc. (SHO, $9.60, Hold, C. Patrick Scholes)
Wyndham Hotels & Resorts, Inc. (WH, $40.47, Buy, C. Patrick Scholes)

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