July Hotel P&L Analyzer: GOP margins -20 bps on Total RevPAR of +3.8%

FY19 RevPAR guide cuts at 2Q earnings add even more pressure to EBITDA margins

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What's Inside

An analysis of recent hotel labor cost trends, one of the critical components impacting hotel EBITDA margins

What's Incremental To Our View

Based on "big data" observations from ~1,000 higher-rated U.S. hotels (data source: HotStats) in our hotel data analytics lab: July: 20 bps of GOP margin loss on approximately +3.8% Total RevPAR (Total RevPAR includes Rooms RevPAR plus outside-of-the-room spend). July RevPAR results came in very slightly better than expected with modest Rooms RevPAR of +1.6% and relatively better Total RevPAR. Margins were slightly down y/y, reflecting the continuing impact of labor cost growth as a material headwind for hotel owners today. Margins would likely be far softer if not for relatively stronger revenue growth in out-of-room spend (food and beverage, ancillary revenue, etc.) and cost containment measures.

During 2Q earnings, many REITS lowered their FY19 RevPAR guidance assumptions; we believe the increased challenges to maintain RevPAR growth (especially room rates) add slightly more pressure for owners to hold EBITDA margins flat in 2019.

The impact of RevPAR changes to EBITDA margins is generally quite different between occupancy and ADR. Over the last few months, occupancy has been pressured (slight percentage change declines); for the most part ADR growth has remained flat to slightly up. However, ADR growth is increasingly shifting to be flattish to slightly down in some weeks (especially Transient ADR) -- we view the ADR trend as relatively more impactful to EBITDA margins than the slight declines in occupancy.

- **Incremental ADR growth tends to flow generously to profits (sometimes 80%-90% to the bottom line). The reverse can also be said when ADR declines.** Given some of the REITS' 2Q earnings commentaries on recent weakness in transient demand trends, we view the potential for room rate cuts to be a potentially rising headwind to 2H19 (and 2020) EBITDA margins. Additionally, the continued pressure of new supply growth to the REITS does not help hotel margins. We anticipate some new hotels may open with even more conservative room rates than budgeted to draw guests if demand is increasingly pressured. **That being said, with full-service ADRs largely hovering in the -1% to +2% territory, we do not see EBITDA margins under significant pressure -- for now.** However, we are attentive to the relatively recent slippage of ADRs in clean comp weeks over the last two months. We will be increasingly focused on ADR changes to business travel in clean comp weeks starting in September, post the August summer travel period. (Please review our weekly STR notes for further insights.)

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<u>July results color:</u> July RevPAR growth came in very slightly better than expected with margins unsurprisingly impacted by continued labor cost growth (labor costs growing moderately with no near-term abatement). Rooms RevPAR of +1.6% and Total RevPAR of +3.8% compare with GOP margins of -20 bps y/y. There was a 400 bps. differential between Total RevPAR growth and GOP margin growth. As anticipated, June's anomalistic GOP margin growth of +30 bps on Total RevPAR growth of +0.5% did not continue in July.

<u>Our 3Q19 and 2019 margin forecasts:</u>

Our 3Q19 margin forecast is -75 bps to +25 bps. Our spread is unusually large for 3Q given the larger influence of leisure during the summer months and our greater caution on weakening transient demand trends during clean comp weeks. Transient demand books closer to the date of arrival than Group. For that reason we have less confidence at this time on where margins will land for 3Q. As we discuss below, portfolios with greater San Francisco exposure (especially for REITS) may have a relatively more challenged 3Q and a relatively stronger 4Q given the trend of citywide group pace and the impact from the 4Q18 labor disruptions (strikes).

- Our disclaimer on the above: please note that there are anomalies for specific REITS due to portfolio changes and property renovations, weather impact, etc., thus we focus on the aggregate numbers. **Hotels owned by the REITS orient more heavily to Upper Upscale versus Luxury, thus our expectations for margin growth for REITS reflects that differential. We expect REITS with a greater proportion of Luxury hotels (ex-idiosyncratic factors as aforementioned) to have a greater opportunity for slight margin expansion (or lower margin declines) in 3Q19 given the shift of July 4th to a Thursday this year from a Wednesday in 2018.**

Our 2019 margin forecast continues to hold at flat to -50 bps. While we believe owners are still able to squeeze profitability through asset management improvements (and/or the disposition of underperforming hotels), slightly worsening RevPAR trends are likely to net out some of the EBITDA margin improvement plans. Per the HotStats data, YTD GOP margin growth continues to be flattish and we do not anticipate the back half of the year to be an easier comp for most higher-rated hotels *and we still do not see a second half acceleration in our RevPAR data analytics lab*. The one major exception here are hotels that were materially negatively impacted by labor strikes in 2H18.

- **We view Ryman Hospitality (RHP, Hold) as a unique outsider in the Lodging REIT space in part as a late-cycle beneficiary** from groups booked in years past, the impressive ramp up of Gaylord Rockies this year, and the expansion in the Entertainment segment. However, **we view RHP as a cyclical stock in a cyclical industry (the good news will not last forever).**

At a high level, we assume somewhat stronger y/y citywide pace in September vs. October being driven by the Jewish High Holidays calendar shift (even though the holidays are shifting to late September/October this year from mid-September last year, we forecast September 2019 RevPAR growth to be low-single digits at best). Similarly, we assume that New Year's Day shifting to a Wednesday in 2020 from a Tuesday in 2019 will lead to stronger y/y group demand in December 2019.

- **Given that many REITS concentrate in specific markets, we view San Francisco to contribute to outsized 3Q19 EBITDA margin headwinds for owners that concentrate in that market.** These headwinds should flip to tailwinds in 4Q19 given much stronger citywide pace and the lapping of the 4Q19 strikes.
- For leisure-oriented hotels, we assume leisure strength in January 2020 given the aforementioned New Year's calendar shift (+ to luxury and resort hotels). The shift of Christmas in 2019 to a Wednesday from a Tuesday in 2018 should lead to stronger y/y leisure demand for the end of December as well.

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Monthly Profitability Metrics

July profitability: Slight RevPAR growth with margins slightly negative.

Industry Metric	July 2019 y/y	YTD		July 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	20	-60	bps	80.6%	78.6%	77.7%	30 bps	77.4%
ADR	1.4%	1.6%	%	$216	$232	$225	2.5%	$220
RevPAR	1.6%	0.8%	%	$174	$182	$175	2.8%	$170
Total Revenue PAR	3.8%	2.4%	%	$272	$305	$289	3.3%	$280
Total Dept. Profit % Total Rev.	0	20	bps	58.5%	60.7%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	50	20	bps	37.9%	35.2%	35.5%	20 bps	35.3%
Total GOP PAR	3.3%	2.3%	%	$92	$117	$108	4.1%	$104
Total GOP % of Total Rev.	-20	0	bps	33.7%	38.5%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

All dollar figures are in USD. 2017 figures have been revised as of December 2018 to account for the updated sample set.

June profitability: Flattish RevPAR growth yet margins were slightly positive.

- **2Q:** Operating Department margins were ~ -20 bps and GOP margins were ~ -40 bps.

Industry Metric	June 2019 y/y	YTD		June 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	-140	-90	bps	81.9%	78.1%	77.7%	30 bps	77.4%
ADR	1.3%	1.7%	%	$229	$234	$225	2.5%	$220
RevPAR	-0.4%	0.6%	%	$188	$183	$175	2.8%	$170
Total Revenue PAR	0.5%	2.1%	%	$307	$310	$289	3.3%	$280
Total Dept. Profit % Total Rev.	30	10	bps	62.0%	61.0%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	40	20	bps	34.0%	34.8%	35.5%	20 bps	35.3%
Total GOP PAR	1.2%	2.1%	%	$123	$121	$108	4.1%	$104
Total GOP % of Total Rev.	30	0	bps	40.2%	39.2%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

All dollar figures are in USD. 2017 figures have been revised as of December 2018 to account for the updated sample set.

May profitability: Moderate RevPAR growth but modestly negative margins.

Industry Metric	May 2019 y/y	YTD		May 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	30	-70	bps	79.9%	77.4%	77.7%	30 bps	77.4%
ADR	2.0%	1.8%	%	$232	$236	$225	2.5%	$220
RevPAR	2.3%	0.8%	%	$186	$182	$175	2.8%	$170
Total Revenue PAR	3.8%	2.4%	%	$316	$310	$289	3.3%	$280
Total Dept. Profit % Total Rev.	-40	10	bps	60.9%	60.8%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total R	20	20	bps	34.9%	35.0%	35.5%	20 bps	35.3%
Total GOP PAR	2.7%	2.3%	%	$125	$121	$108	4.1%	$104
Total GOP % of Total Rev.	-40	0	bps	39.5%	39.0%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

All dollar figures are in USD. 2017 figures have been revised as of December 2018 to account for the updated sample set.

April profitability: Flattish RevPAR and moderately negative margins.

Industry Metric	Apr 2019 y/y	YTD		Apr 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	-70	-100	bps	81.6%	76.7%	77.7%	30 bps	77.4%
ADR	-0.8%	1.7%	%	$238	$236	$225	2.5%	$220
RevPAR	-1.7%	0.4%	%	$194	$181	$175	2.8%	$170
Total Revenue PAR	-0.4%	2.0%	%	$324	$309	$289	3.3%	$280
Total Dept. Profit % Total Rev.	-40	20	bps	62.3%	60.8%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	100	20	bps	33.2%	35.0%	35.5%	20 bps	35.3%
Total GOP PAR	-3.0%	2.2%	%	$132	$120	$108	4.1%	$104
Total GOP % of Total Rev.	-110	0	bps	40.9%	38.8%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

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March profitability: Slightly negative RevPAR growth although y/y margins were modestly positive.

- **1Q:** Operating Department margins were ~ + 40 bps and GOP margins were ~ +50 bps.

Industry Metric	Mar 2019 y/y	YTD		Mar 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	-160	-110	bps	81.1%	75.1%	77.7%	30 bps	77.4%
ADR	1.3%	2.7%	%	$245	$236	$225	2.5%	$220
RevPAR	-0.8%	1.2%	%	$198	$177	$175	2.8%	$170
Total Revenue PAR	2.3%	2.9%	%	$333	$304	$289	3.3%	$280
Total Dept. Profit % Total Rev.	20	40	bps	63.0%	60.2%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	-30	-20	bps	32.5%	35.6%	35.5%	20 bps	35.3%
Total GOP PAR	3.2%	4.3%	%	$142	$116	$108	4.1%	$104
Total GOP % of Total Rev.	40	50	bps	42.7%	38.1%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

All dollar figures are in USD. 2017 figures have been revised as of December 2018 to account for the updated sample set.

February profitability: Decent RevPAR growth resulted in modest y/y margins.

Industry Metric	Feb 2019 y/y	YTD		Feb 2019	YTD	FY2018	2018 y/y	FY2017
Occupancy	-40	-70	bps	76.0%	72.0%	77.7%	30 bps	77.4%
ADR	4.4%	3.6%	%	$235	$231	$225	2.5%	$220
RevPAR	3.9%	2.5%	%	$179	$166	$175	2.8%	$170
Total Revenue PAR	3.6%	3.2%	%	$308	$288	$289	3.3%	$280
Total Dept. Profit % Total Rev.	100	60	bps	60.6%	58.5%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	-40	-10	bps	35.3%	37.5%	35.5%	20 bps	35.3%
Total GOP PAR	7.1%	5.0%	%	$118	$102	$108	4.1%	$104
Total GOP % of Total Rev.	120	60	bps	38.4%	35.2%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

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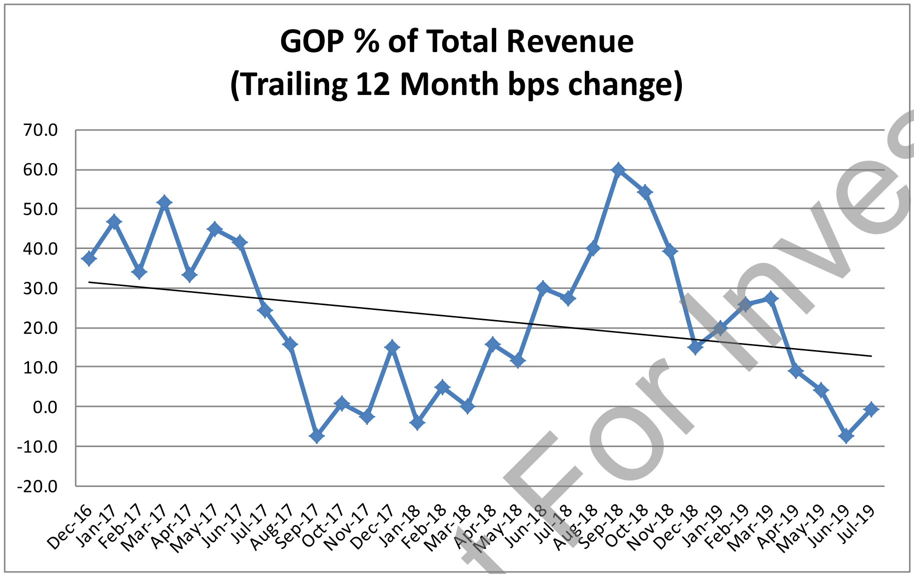
January profitability: Limited RevPAR growth resulted in flat y/y margins.

Industry Metric	Jan 2019 y/y		Jan 2019	FY2018	2018 y/y	FY2017
Occupancy	-110	bps	68.3%	77.7%	30 bps	77.4%
ADR	2.6%	%	$226	$225	2.5%	$220
RevPAR	1.0%	%	$154	$175	2.8%	$170
Total Revenue PAR	2.8%	%	$271	$289	3.3%	$280
Total Dept. Profit % Total Rev.	20	bps	56.4%	60.0%	10 bps	59.9%
Total Hotel Labor Costs % Total Rev.	20	bps	39.7%	35.5%	20 bps	35.3%
Total GOP PAR	2.7%	%	$87	$108	4.1%	$104
Total GOP % of Total Rev.	0	bps	32.0%	37.4%	20 bps	37.2%

Source: STRH Research, HotStats

All dollar figures are in USD. 2017 figures have been revised as of December 2018 to account for the updated sample set.



Source: STRH Research, HotStats

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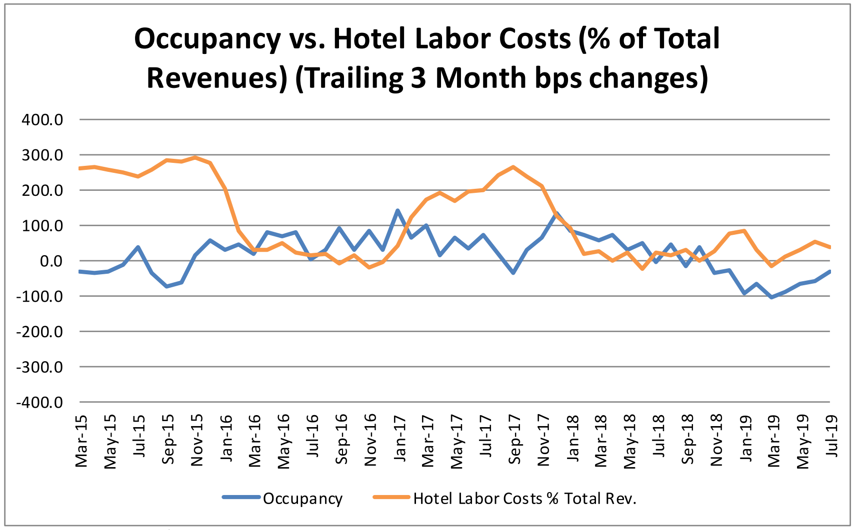
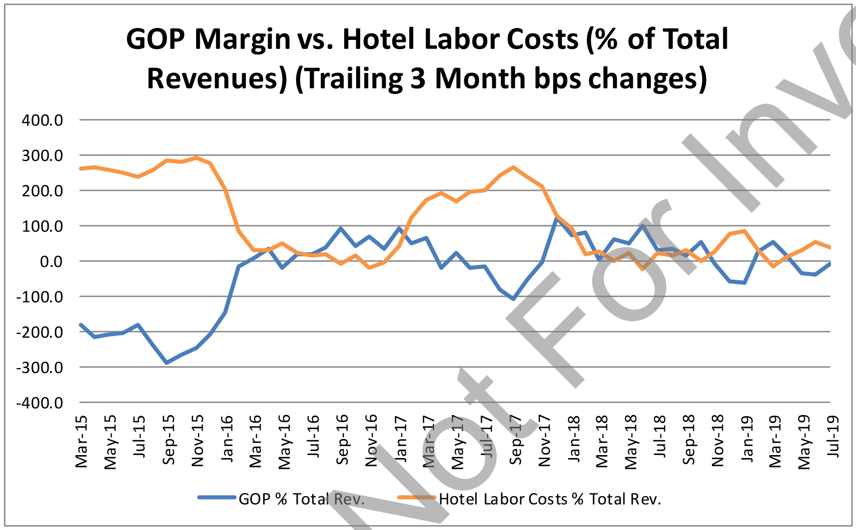
- The following charts highlight trends in labor costs vs. occupancy and GOP margins.



Source: STRH Research, HotStats



Source: STRH Research, HotStats

REIT Margin Guidances*

		3Q Guide	2019 Guide	Margin Guidance Provided
Chesapeake	CHSP	guidance no longer updated due to proposed PK merger		
DiamondRock	DRH	none	none	
Host	HST	none	-25 to +25 bps	Comp Hotel EBITDA margins
Pebblebrook	PEB	-250 to -225 bps	-50 to -40 bps	Same Property EBITDA margins
Park	PK	none	+0-50 bps	Comp Hotel Adjusted EBITDA Margins
Ryman	RHP	none	none	
RLJ	RLJ	none	-70 bps to -10 bps	Pro Forma Hotel EBITDA Margins (Implied guide from 32.3% YE 2018)
Sunstone	SHO	none	-25 to -75 bps	21 Hotel Comp Portfolio Adjusted EBITDAre Margin

*Note: We do not consider EBITDA margin guidances to be comparable across the Lodging REIT space as indicative of the type of margin guidance provided.

Source: Company filings, STRH Research

Companies Mentioned in This Note

Chesapeake Lodging Trust (CHSP, $25.64, Hold, C. Patrick Scholes)
DiamondRock Hospitality Company (DRH, $9.27, Hold, C. Patrick Scholes)
Host Hotels & Resorts, Inc. (HST, $15.69, Hold, C. Patrick Scholes)
Pebblebrook Hotel Trust (PEB, $26.01, Hold, Gregory Miller)
Park Hotels & Resorts Inc. (PK, $23.41, Buy, C. Patrick Scholes)
Ryman Hospitality Properties, Inc. (RHP, $79.13, Hold, C. Patrick Scholes)
RLJ Lodging Trust (RLJ, $16.02, Sell, Gregory Miller)
Sunstone Hotel Investors, Inc. (SHO, $12.87, Hold, C. Patrick Scholes)

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