March RevPAR Monitor: Business travel continues to decel; Lowering RevPAR ests.

Leisure and Group/Convention demand holding fairly steady

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What's Inside

An in-depth update to our RevPAR outlook

The trend is not your friend right now. Based on forward-looking observations in our RevPAR data analytics lab combined with conversations with private hotel owners over the past eight weeks, we continue to see deceleration in demand for individual business travelers. While the hotel companies are keeping pricing fairly steady, up 2-3% y/y, the number of reservations being made at these prices most notably for individual business travel as seen in weekday OTA data, continues to soften (which translates into occupancy declines) with each subsequent observation and conversation. We note that visibility ("the booking window") on this customer is 45-60 days at most and is reflective of strength or weakness in the economy over the previous 2-3 months. For all hotel REITs (ex-Ryman (RHP, Hold)) and the Hilton, Hyatt, and Marriott C-corps, the corporate individual business traveler is their "bread & butter" customer and comprises 45-55% of their business. While Choice (CHH, Hold) and Wyndham (WH, Buy) also derive approx. 45% of their business from individual business travelers, their business traveler is far more weighted to small businesses than larger corporates and we observe small businesses still holding fairly steady. **Because of the above observations we are again cutting our RevPAR forecasts for US full-service branded hotels.**

The relative good news is that leisure and group/convention trends continue to be mostly "steady-eddie" with RevPAR trends tracking up low-single digits on average for the next several quarters. Additionally group demand accelerates in 2020 from 2019, however most of improvements are lost on a same-store basis due to additional hotel room supply of approx. +3% for top 25 markets. Secondly, San Francisco, to which many hotel REITS have high exposure, is on track to exceed initial 2019 expectations (see Major Markets section for further discussion on San Francisco).

- **However, we begin to see a slow-down in group/convention trends beginning in 4Q2020 and continuing into 2021**. We observe and calculate that 2021 group RevPAR group tracking down low-single digits at this point.

Over the past eight weeks in our data from OTAs we observe US full-service branded hotels pushing pricing closer to +2-3pts y/y for mid-week business (proxy for individual business travel) whereas the number of reservations (same-store) made at those prices are tracking down 2-3pts y/y. By comparison, 2018 US full service ADR grew approx. 2.5pts. whereas occupancy was flat y/y.

- **Net-net, because of this trend and softness in In-The-Quarter-For-The-Quarter (ITQFTQ) corporate demand trends we are lowering our 2019 RevPAR forecast for US full-service hotels (AKA the typical Hilton (HLT, Buy) or Marriott (MAR, Hold) branded hotel) by 50 bps. to +0.0-2.0% from +0.5-2.5% previously and reducing our 1Q19 projection to -0.5 to +1.0% from +0.5-2.5% prior**.
  - By comparison during 4Q18 earnings calls:

- **Hilton**: forecasted 2019 US RevPAR growth consistent with their system-wide guidance range (+1-3%) based on expected steady fundamentals and continued pricing increases. Through the first half of March based on STR results, we calculate their 2019 US RevPAR growth is tracking approx. +0.1% YTD.

- **Hyatt (H, Hold)**: forecasted 1-3% global RevPAR growth (US not broken out). Through the first half of March based on STR results, we calculate their 2019 US RevPAR growth is tracking approx. +0.5% YTD.

- **Marriott**: 2019 North America RevPAR growth expectation remains at +1-3%. Through the first half of March based on STR results, we calculate their US RevPAR growth is tracking approx. +0.2% YTD.

- **We are lowering our 2Q19 forecast to +0-2% from +0.5-2.5%**.

Quarterly Tracking

	1Q19	2Q19	2019E
	Overall	Overall	Overall forecast
Feb-19	-0.5% to +1.0%	+0-2%	+0-2%
Dec-18	+0.5-2.5%	+0.5-2.5%	+0.5-2.5%
Oct-18	+1.5-3.5%		+1-3%
Aug-18			+1-3%
Jul-18			+1-3%

Source: STRH Research

This all begs the question: Do the +1-3% RevPAR forecasts for Hilton, Hyatt, and Marriott need to come down? *Our answer is probably not just yet as the bottom half of the range is still achievable*. That said, we attach a much higher probability that the high-ends will need to come down come July/August earnings as we see a slim-to-none chance at this moment these companies will hit or exceed the high-end of their guided ranges.

What does it all means for the lodging stocks? As we have always said, having to cut headline RevPAR forecasts is never a catalyst for the lodging stocks and unfortunately we continue to believe this to be the case.

- *Frankly we are a bit surprised that lodging stocks have been holding in there as well as they have of late, which we attribute to several factors*: **A) REITS**: Attractive balance sheets for many, fairly well-covered dividends with attractive yields, aggressive and proactive property-level cost cutting measures, and valuations towards the lower-end of historical ranges; **B) C-Corps**: An oversold condition going into 2019; record y/y net unit growth percentages, asset-lite characteristics and net debt/EBITDAs that are within target ranges which subsequently allow for aggressive share repurchases, and valuations that are slightly above the mid-points of historical ranges. Additionally helping both is an economy that does not appear to be falling into recession in the next twelve months.

- **Picking the stocks/sectors: We continue to prefer cruise stocks over most lodging stocks at the moment. Specifically within cruise lines our favorite is Norwegian (NCLH, Buy) followed by Royal Caribbean (RCL, Buy)**. Within hotels we continue to favor C-Corps over hotel REITS (we favored hotel REITS for the first half of last year). In an environment of low RevPAR growth combined with gradually increasing wages/margin pressures, returns for hotel owners is a major headwind to EBITDA growth. Hotel stocks, but especially hotel REIT stocks, typically work best when there is a spark to RevPAR growth and at this moment we are not seeing such sparks like we did at this time one year ago.

- **Please see additional discussion at the end of this report on more specifics for the C-Corp, Hotel REIT, and Vacation Ownership sectors**.

Group/convention trend observations: 2019 is a soft year for nearly every major market except for San Francisco and Las Vegas. The good news is **2020** improves. However **2021** again decelerates and city-wide RevPAR growth will be further diluted by two more years of compounded 3% supply between now and then. **Looking in our crystal ball, signs point to 2021 shaping up to be a year of close to zero RevPAR growth for US full-service hotels (same-store).**

- Interestingly the convention markets in 2019 that are dogs, namely Chicago and DC, turnaround 180 degrees in 2020, whereas San Francisco group/convention is actually tracking at negative y/y growth for 2020 due to the difficult 2019 comp. While San Francisco group/convention faces a very difficult y/y comparison in 2020, because of low new supply and strength in the transient segment the city should still see positive (low-to-mid single digit) RevPAR growth in 2020.
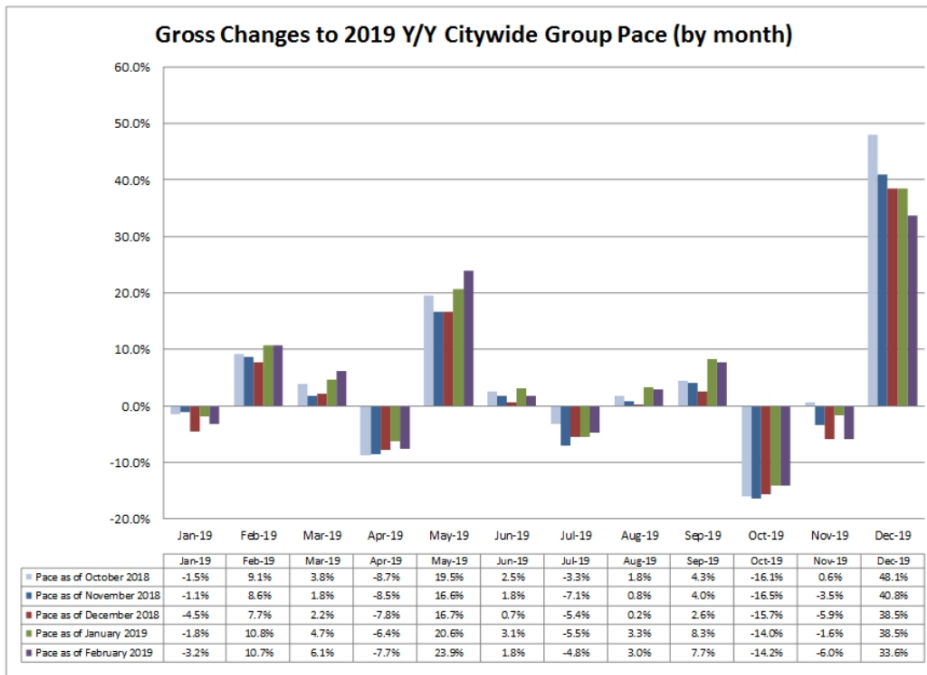
<u>Looking at our most recent forward-looking demand and pricing observations</u>:

1Q19

- **January**: Started off soft due to the shift of New Years one day later in the week this year. The month finished at approx. flat to +0.5% RevPAR growth for full service US branded hotels.
- **February**: As we predicted, February will likely be the strongest month of the quarter as it finished at approx. +2% for full service US branded hotels. We believe the relative strength was due to Valentine's day shifting to a Thursday from a Wednesday last year and from an easy Nor'easter comp the last week of the month.
- **March**: Because of softness in last-minute transient-business demand, expectations have slipped. Two months ago we observed this month tracking towards +0.5-2.5%. However we now see it closer to flat to down 1%. Regarding this year's easter shift, we believe the shift will be somewhat neutral to March and April. Specifically:
    - Week ending 3/23/19: **Difficult** group comp;
    - Week ending 3/30/19: **Easy** group comp;
    - Week ending 4/6/19: **Easy** group comp; and
    - Week ending 4/13/18: **Difficult** group comp.

2Q19

- **April**: In addition to the weak transient-business demand trends, we see Easter as a neutral and the month around flat to down 1%, a cut from our prior outlook of +0.5-2.5%.
- **May**: This expectation is unchanged but our suspicion is this forecast will come down as we get closer to that 30-45 days transient-business booking window. Group business looks exceptionally strong for May.
- **June**: Will be hurt by July 4th moving to a Thursday this year from a Wednesday last year. Recall last year the last week of June benefited from July 4th moving to a Wednesday from a Tuesday whereas the July 4th week in 2018 was hurt by this shift. We see June around flat-ish.

Gross Changes to 2019 Y/Y Citywide Group Pace (by month)

	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19
Pace as of October 2018	-1.5%	9.1%	3.8%	-8.7%	19.5%	2.5%	-3.3%	1.8%	4.3%	-16.1%	0.6%	48.1%
Pace as of November 2018	-1.1%	8.6%	1.8%	-8.5%	16.6%	1.8%	-7.1%	0.8%	4.0%	-16.5%	-3.5%	40.8%
Pace as of December 2018	-4.5%	7.7%	2.2%	-7.8%	16.7%	0.7%	-5.4%	0.2%	2.6%	-15.7%	-5.9%	38.5%
Pace as of January 2019	-1.8%	10.8%	4.7%	-6.4%	20.6%	3.1%	-5.5%	3.3%	8.3%	-14.0%	-1.6%	38.5%
Pace as of February 2019	-3.2%	10.7%	6.1%	-7.7%	23.9%	1.8%	-4.8%	3.0%	7.7%	-14.2%	-6.0%	33.6%

Source: STRH Research, TAP

International results and expectations: 1Q19 International tracking below guidances

According to STR, local currency RevPAR in Europe was +3.3% y/y in February vs. +3.8% in January. Hurt by 875 bps of FX headwinds last month (vs. 979 bps in January), results in Europe in US$ of -5.5% y/y compare to -5.9% in the prior month.
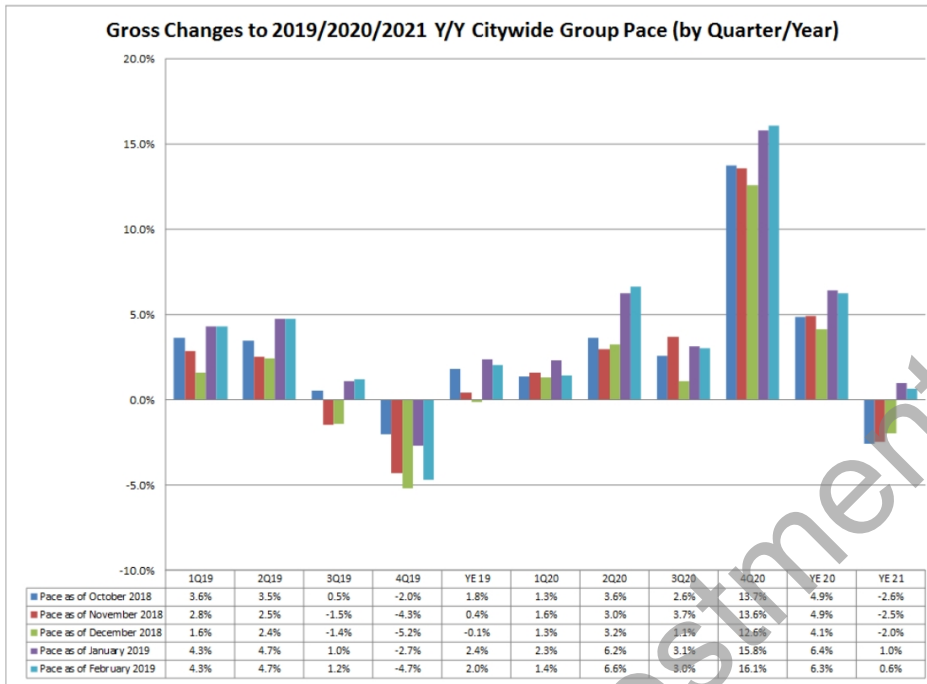
Local currency RevPAR in Asia Pacific was +1.3% y/y in February vs. -0.1% in January. Looking at results from Asia-Pacific converted into U.S. dollars, Asia-Pacific RevPAR was -5.1%. There was a ~633 headwind vs. local currency performance of +1.3%.

1Q19 estimated regional actuals vs. 2019 C-corp expectations:

- **Europe**: HLT guided for European RevPAR growth in 2019 (in constant currency) to be "consistent with the systemwide range" (+1-3%) and MAR projected (in constant currency) mid-single digits growth for both 1Q and 2019. **We note that the Russian World Cup will be a difficult y/y comp for Europe this summer**.
  - Our projection for 1Q European RevPAR growth in local currency is +2-4% (unchanged estimate from last month) (by comparison we estimate 1Q18 was ~ +7%). In US$, our projection for 1Q European RevPAR growth is mid-single digits negative (our prior estimate was low-to-mid single digits negative). We note that MAR and HLT's European exposures are overexposed to select European markets and countries and thus it is likely that MAR and HLT's European performance will naturally differ from our European aggregated results.
- **Asia-Pacific**: HLT is guiding 2019 RevPAR up mid-single digits with China up mid to high single digits and MAR is guiding up mid-single digits for both 1Q and 2019.
  - Our projection for 1Q Asia-Pacific RevPAR growth in local currency is low single digit positive (unchanged from our prior estimate).
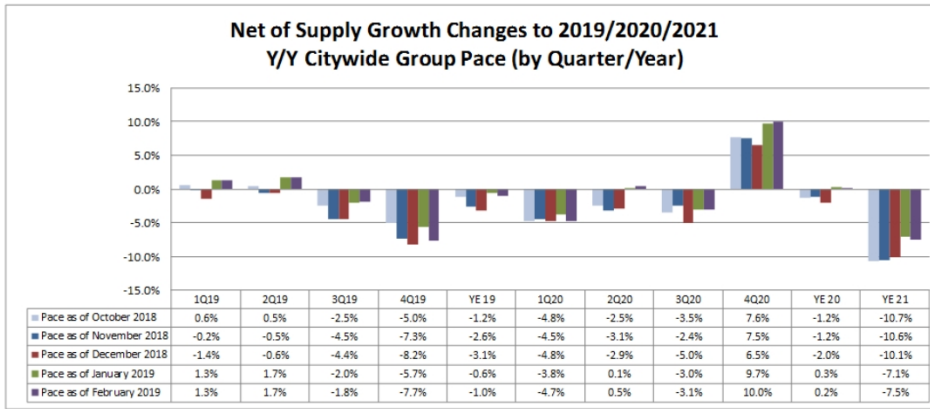
Hyatt, InterContinental, and Marriott have the greatest exposure to Europe and Asia. From Europe, MAR generates approximately 15% of EBITDA, IHG (NR) 15%, WH 15%, and H and HLT 10% each. Of these companies, H and MAR have the greatest exposure to Asia (~10-20% of EBITDA). Each of the other companies generates 5% to 10% of EBITDA from the Asia-Pacific region.

Examining the forward-looking group/convention trends: On the surface, we would describe headline forward looking trends for 2019 and especially for 2020 as "not that bad." However, over the next several years urban hotels will see approx. 3% new supply growth annually and those headline "gross demand" growth rates will be diluted on a "same-store" basis by this new supply. *We surmise that if you're a city convention bureau or hotel brand (C-corp), you're probably happy about the 2020 pace of demand. However if you're a hotel owner in that city you are less enthusiastic because of the new hotels opening up around the block from you that will take some of that demand.*

Gross Changes to 2019/2020/2021 Y/Y Citywide Group Pace (by Quarter/Year)

|	1Q19	2Q19	3Q19	4Q19	YE 19	1Q20	2Q20	3Q20	4Q20	YE 20	YE 21
Pace as of October 2018	3.6%	3.5%	0.5%	-2.0%	1.8%	1.3%	3.6%	2.6%	13.7%	4.9%	-2.6%
Pace as of November 2018	2.8%	2.5%	-1.5%	-4.3%	0.4%	1.6%	3.0%	3.7%	13.6%	4.9%	-2.5%
Pace as of December 2018	1.6%	2.4%	-1.4%	-5.2%	-0.1%	1.3%	3.2%	1.1%	12.6%	4.1%	-2.0%
Pace as of January 2019	4.3%	4.7%	1.0%	-2.7%	2.4%	2.3%	6.2%	3.1%	15.8%	6.4%	1.0%
Pace as of February 2019	4.3%	4.7%	1.2%	-4.7%	2.0%	1.4%	6.6%	3.0%	16.1%	6.3%	0.6%

Source: STRH Research, TAP

However, when we add approx. 3% of annual urban hotel supply over the next several years, the same-store projection looks less encouraging:

Net of Supply Growth Changes to 2019/2020/2021 Y/Y Citywide Group Pace (by Quarter/Year)

|	1Q19	2Q19	3Q19	4Q19	YE 19	1Q20	2Q20	3Q20	4Q20	YE 20	YE 21
Pace as of October 2018	0.6%	0.5%	-2.5%	-5.0%	-1.2%	-4.8%	-2.5%	-3.5%	7.6%	-1.2%	-10.7%
Pace as of November 2018	-0.2%	-0.5%	-4.5%	-7.3%	-2.6%	-4.5%	-3.1%	-2.4%	7.5%	-1.2%	-10.6%
Pace as of December 2018	-1.4%	-0.6%	-4.4%	-8.2%	-3.1%	-4.8%	-2.9%	-5.0%	6.5%	-2.0%	-10.1%
Pace as of January 2019	1.3%	1.7%	-2.0%	-5.7%	-0.6%	-3.8%	0.1%	-3.0%	9.7%	0.3%	-7.1%
Pace as of February 2019	1.3%	1.7%	-1.8%	-7.7%	-1.0%	-4.7%	0.5%	-3.1%	10.0%	0.2%	-7.5%

Source: STRH Research, TAP

- **2019**: Our net-of-supply group pace for 2019 is -1.0% (Approx. 100-150 bps. lower ex-San Francisco). To this we add approx. 3 percentage points of rate growth to come up with a projection that same-store Group RevPAR is tracking at approx. +2% y/y for 2019 at the moment. We note that 2019 will show massive gains in SF due to the completion of the Moscone Center renovations.


2019
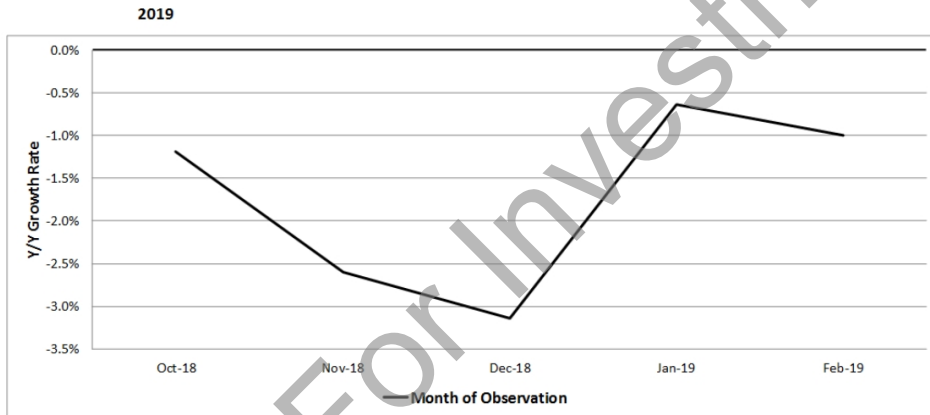
Source: STRH Research, TAP

- **2020**: Our net-of-supply group pace for 2020 is +0.2%. To this we add approx. 2.5 percentage points of rate growth to come up with a projection that same-store Group RevPAR is tracking at approx. +2.5% y/y for 2020 at the moment, with approx. 25% of final group reservations on the books.
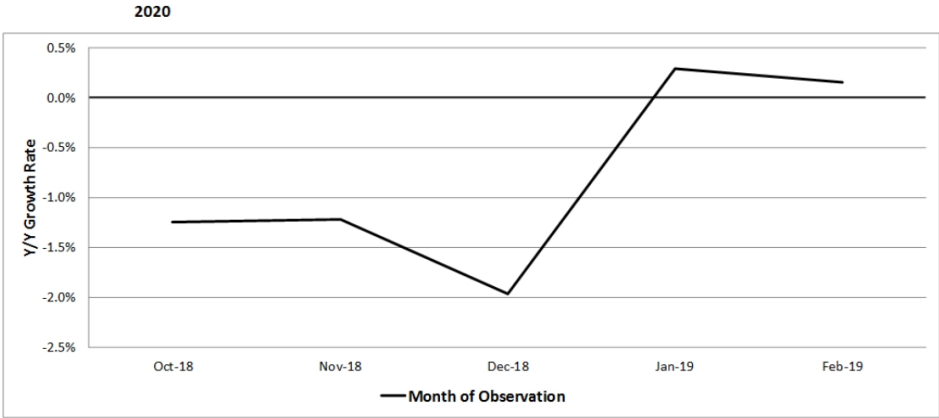
Source: STRH Research, TAP

- **2021**: Our net-of-supply group pace for 2020 is -7.5%. To this we add approx. 2 percentage points of rate growth to come up with a projection that same-store Group RevPAR is tracking at approx. -5% y/y for 2021 at the moment, with approx. 10% of final group reservations on the books.

2021

Source: STRH Research, TAP
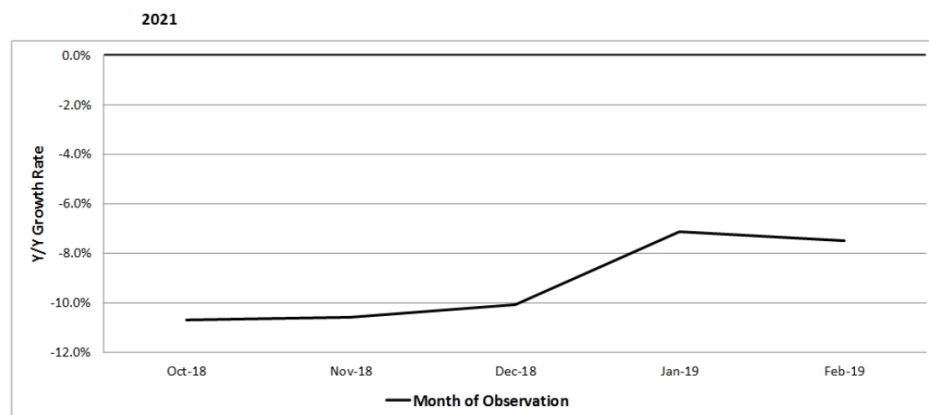
Segmentation By Company			
	Transient Corporate	Transient Leisure	Group
REITS			
CHSP	45%	20%	35%
DRH	45%	20%	35%
HST	45%	15%	40%
PK	45%	20%	35%
RHP	5%	15%	80%
RLJ	55%	25%	20%
SHO	45%	20%	35%
PEB (not covered)	60%	20%	20%
	Transient Corporate	Transient Leisure	Group
C-corps			
CHH	45%	45%	10%
H	40%	20%	40%
HLT	50%	20%	30%
MAR	45%	20%	35%
WH	45%	45%	10%

Source: STRH Research, company filings

Major Markets:

Not surprisingly, due to completed renovation of the convention center, San Francisco will be the outstanding market over the next year although group business for 2020 is showing negative growth mostly due to the very difficult y/y comp as the pent-up 2019 demand moves on to other cities such as Chicago and Washington DC.

- We observe **Houston** getting "less bad" as the year progresses as the difficult y/y comps end in August.

Ranking the big six major US markets for 2019. Group/meeting bookings are the best way to think about market outperformance/ underperformance for time periods more than 90 days out. A healthy (or weak) convention calendar really drives city performance (with the notable exception of NYC as that is mostly a transient market). Based on initial group/ convention bookings, we lump the top six markets into three buckets:

2019:

1. **Well above average**: SF

2. **Average**: Boston, Los Angeles

3. **Below average**: New York City

4. **Well below average**: Chicago, Washington DC

Additional color on the big six:

Boston:

1Q19: Average

2Q19: Above average

2019: Below average

Est exposure to Boston market								
	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
Boston	17%	13%	6%	15%	2%	0%	4%	15%
Rank	1	4	5	2	7	8	6	2
Note: Est. exposures include surrounding areas								
Source: STRH Research, Company data								

Chicago:

1Q19: Well below average

2Q19: Below average

2019: Well below average

Group/convention outlook for Chicago

Pace as of	1Q19E	2Q19E	3Q19E	4Q19E	YE 19	1Q20E	2Q20E	3Q20E	4Q20E	YE 20	YE 21
Feb-19	-23.8%	6.0%	2.1%	-16.4%	-6.6%	33.0%	17.9%	-2.4%	-4.1%	9.7%	9.4%
Jan-19	-25.2%	-2.8%	2.1%	-16.8%	-9.7%	33.4%	19.1%	-3.6%	3.2%	11.7%	8.3%
Dec-18	-30.0%	-10.0%	-5.1%	-18.3%	-14.8%	24.7%	21.8%	-6.9%	-0.1%	9.5%	10.7%
Nov-18	-31.1%	-9.2%	-5.6%	-18.3%	-14.8%	27.7%	20.0%	2.4%	2.8%	12.3%	11.2%
Oct-18	-32.4%	-7.9%	-7.7%	-18.2%	-15.0%	19.3%	27.3%	-1.0%	2.7%	13.1%	6.8%

Source: STRH Research, TAP

Est exposure to Chicago market

	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
Chicago	7%	13%	4%	5%	4%	0%	4%	7%
Rank	2	1	5	4	5	8	5	2

Note: Est. exposures include surrounding areas

Source: STRH Research, Company data

Los Angeles:

1Q19: Below average

2Q19: Average

2019: Average

Group/convention outlook for Los Angeles										
Pace as of	1Q19E	2Q19E	3Q19E	4Q19E	YE 19	1Q20E	2Q20E	3Q20E	4Q20E	YE 20	YE 21
Feb-19	-4.1%	-3.6%	-16.2%	7.7%	-4.7%	-1.2%	22.4%	52.0%	28.5%	23.0%	-21.1%
Jan-19	-4.9%	0.0%	-17.4%	10.4%	-3.7%	-1.9%	23.4%	50.0%	29.5%	23.0%	-20.1%
Dec-18	-12.3%	8.3%	-16.8%	20.4%	-2.3%	-8.6%	19.8%	48.7%	17.9%	17.6%	-23.6%
Nov-18	-15.4%	6.8%	-19.3%	21.0%	-4.2%	-6.8%	10.6%	50.3%	20.0%	16.1%	-26.1%
Oct-18	-27.6%	-1.3%	-31.3%	7.6%	-15.5%	-21.1%	9.6%	48.4%	-0.9%	6.9%	-21.4%

Source: STRH Research, TAP

Est exposure to LA market								
	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
LA	7%	2%	5%	13%	0%	0%	5%	6%
Rank	2	6	4	1	7	7	5	3
Note: Est. exposures include surrounding areas								
Source: STRH Research, Company data								

NYC:

1Q19: Well below average

2Q19: Average

2019: Below average

A major headwind to same store RevPAR growth in NYC remains several years of compounded 4-6% new supply growth. Per Lodging Econometrics, city-wide new room supply grew 5.1% in 2016, 4.9% in 2017, 3.4% in 2018, and is projected to grow 7.9% in 2019 and 4.8% in 2020. Even if some of these expected new hotels never open, it is difficult to envision that NYC will not have continued pressure from above-average supply over the next several years. **We believe RevPAR growth in NYC will be down low-single digits 2019**.

Est exposure to NYC market								
	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
NYC	5%	12%	8%	1%	7%	0%	5%	4%
Rank	4	1	2	7	3	8	4	6
Note: Est. exposures include surrounding areas								
Source: STRH Research, Company data								

San Francisco:

1Q19: Well above average **(likely the best quarter of 2019 for any major city)**

2Q19: Well above average

2019: Well above average

Group/convention outlook for San Francisco											
Pace as of	1Q19E	2Q19E	3Q19E	4Q19E	YE19	1Q20E	2Q20E	3Q20E	4Q20E	YE20	YE21
Feb-19	71.2%	51.4%	8.4%	74.1%	49.6%	-28.9%	7.3%	-12.9%	-8.9%	-12.0%	0.4%
Jan-19	82.0%	53.9%	7.4%	76.3%	52.6%	-28.4%	23.5%	-13.0%	-8.9%	-9.2%	6.9%
Dec-18	85.9%	50.1%	8.4%	75.7%	52.6%	-29.8%	32.0%	-15.4%	-10.1%	-9.0%	-9.5%
Nov-18	86.9%	52.6%	8.2%	75.9%	53.5%	-30.5%	36.5%	-15.1%	-10.2%	-8.4%	-2.7%
Oct-18	90.4%	57.9%	14.7%	76.0%	58.0%	-28.0%	37.9%	-15.1%	-10.1%	-7.2%	-2.5%

Source: STRH Research, TAP

San Francisco all along was expected to be the top growth market in 2019 due to the Moscone reopening, however we believe the city will finish above initial expectations:

First, what were the expectations for the market in 2019?
- Based on data from Tourism Economics (the same company behind STR's RevPAR forecasts), the San Francisco Travel Association/Convention Bureau was forecasting +5.6% RevPAR growth in 2019.
- Secondly, we look at HVS's San Francisco - San Mateo 2019 forecast which is +7.6%
- Combining the two, we estimate the city-wide expectation was approx. +6-7% with the investor "whisper expectation" for the hotel REITS, which have their hotels for the most part near the Moscone Center, closer to double-digit growth.

Next, looking at actual STR results YTD, the San Francisco MSA did:

1. Jan + Feb: +18.9%.

2. First half of March: approx. +25%

From the STR results YTD from above, this implies the rest of the year needs to do approx. +4% to hit +7% for the year. Based on forward looking checks and from conversations with hotel owners, **we believe +4% should be easily achievable as the rest of the year should at a minimum average mid-to-high single digit RevPAR growth with even higher growth for those hotels closer to the Moscone Center.**

Est exposure to SF market								
	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
San Francisco	27%	4%	10%	19%	13%	0%	11%	9%
Rank	1	7	5	2	3	8	4	6
Note: Est. exposures include surrounding areas								
Source: STRH Research, Company data								

Washington DC: Government per diems for 2019 hotel rooms are only up 1% y/y. Obviously the government shutdown did not help tourism and business did not help tourism and business activity. Government business is typically 5-10% of hotel business in the US, but much higher in Washington DC.

1Q19: Below average due to weak transient visitation

2Q19: Below average

2019: Well below average

Group/convention outlook for Washington, D.C.										
Pace as of	1Q19E	2Q19E	3Q19E	4Q19E	YE 19	1Q20E	2Q20E	3Q20E	4Q20E	YE 20	YE 21
Feb-19	16.6%	-25.8%	4.9%	-0.7%	-5.5%	-26.0%	2.9%	43.9%	58.5%	13.1%	-10.5%
Jan-19	18.6%	-25.6%	7.6%	3.5%	-3.8%	-25.6%	1.9%	46.7%	56.1%	13.2%	-11.3%
Dec-18	20.6%	-28.7%	4.5%	3.0%	-5.7%	-25.8%	-0.8%	43.5%	56.4%	12.1%	-11.2%
Nov-18	16.1%	-32.4%	10.7%	1.1%	-7.8%	-23.8%	-0.3%	49.3%	59.2%	14.6%	-6.8%
Oct-18	19.5%	-31.7%	12.6%	2.6%	-6.3%	-22.4%	0.2%	53.1%	59.9%	16.1%	-6.3%

Source: STRH Research, TAP

Est exposure to DC market								
	CHSP	DRH	HST	PEB	PK	RHP	RLJ	SHO
DC	3%	5%	9%	7%	4%	16%	5%	11%
Rank	8	5	3	4	7	1	5	2
Note: Est. exposures include surrounding areas								
Source: STRH Research, Company data								

Current expectations for Top 25 Market new supply:

Supply By Top 25 Markets (Sorted by Pipeline Rooms Growth as % of Census) As of 4Q18						
	Census Rank	YE 2016 Growth Rate	YE 2017 Growth Rate	YE 2018 Growth Rate	2019F Growth Rate	2020F Growth Rate
Nashville	22	3.7%	4.3%	7.2%	6.2%	5.6%
New York City	4	5.1%	4.9%	3.4%	7.9%	4.8%
Miami	14	4.3%	3.4%	2.6%	4.2%	2.4%
Los Angeles	6	1.0%	4.2%	1.7%	2.0%	4.3%
Dallas	8	3.2%	5.8%	3.3%	4.1%	4.0%
Detroit	21	2.4%	3.1%	3.0%	3.0%	4.5%
Seattle	19	2.3%	4.4%	7.3%	3.1%	2.7%
Denver	16	2.6%	5.6%	5.4%	3.2%	3.8%
Boston	12	4.3%	3.1%	3.8%	4.4%	3.1%
Houston	9	6.9%	4.0%	3.0%	4.0%	1.8%
San Diego	11	1.7%	1.3%	2.2%	2.7%	0.3%
Philadelphia	18	1.5%	3.2%	2.2%	1.2%	3.6%
Atlanta	7	1.4%	1.7%	2.7%	2.1%	2.5%
Phoenix	10	1.6%	2.8%	1.5%	1.4%	3.7%
Orlando	2	1.8%	0.8%	1.6%	1.3%	1.9%
Minneapolis	24	6.0%	1.8%	4.3%	2.6%	4.7%
Tampa	17	1.5%	4.0%	2.2%	1.5%	2.8%
San Francisco	15	0.1%	1.8%	1.2%	1.6%	1.5%
Anaheim	13	3.3%	2.0%	1.0%	1.6%	3.4%
Saint Louis	26	1.3%	2.1%	2.0%	2.0%	1.6%
Washington D.C.	5	2.0%	2.0%	1.8%	1.0%	0.9%
San Antonio	20	1.9%	1.4%	2.0%	1.8%	1.9%
Chicago	3	2.5%	2.3%	2.1%	1.0%	1.4%
Norfolk	28	0.0%	1.2%	0.0%	1.5%	0.8%
Oahu Island	36	1.3%	0.6%	0.0%	0.0%	0.6%
Total Top 25 Markets		2.6%	2.9%	2.6%	2.7%	2.7%

Source: Lodging Econometrics, STRH Research

Notes: The largest market in the U.S., Las Vegas, is not included in this chart due to its casino orientation. 2019-2020 are forecasts.

(please see the PDF for a higher quality version of the RevPAR guidances)

RevPAR Guidance (1Q19 and FY 19)			
C-Corps	**1Q19**	**FY 19**	*Notes*
CHH	Unchanged	+0.5-2.0%	*Domestic RevPAR*
H		+1-3%	*Comparable systemwide*
HLT	+1-3%	+1-3%	*Systemwide*
		+1-3%	*US*
		+1-3%	*Americas ex-US*
		+1-5%	*Europe*
		Roughly flat	*Middle East/Africa*
		Mid single digits (+) with China mid-high single digits (+)	*Asia Pacific*
MAR	+1-3%	+1-3%	*Worldwide*
	+1-2%	+1-3%	*North America*
	+2-4%	+2-4%	*Outside North America*
	Mid-single digit (+)	Mid-single digit (+)	*Asia Pacific*
	Low-single digit (+)	Low-single digit (+)	*Caribbean & Latin America*
	Mid-single digit (+) (assuming no disruption from Brexit)	Mid-single digit (+) (assuming no disruption from Brexit)	*Europe*
	Low-single digit (-)	Flattish	*Middle East/Africa*
PLYA		Slightly negative to slightly positive	*Comparable systemwide*
WH		+1-3%	*Includes La Quinta after 1 yr of ownership and excludes Knights Inn from 2018 base*
		+5-7%	*Total portfolio*
REITS			
CHSP	+1-3%	+1.5-3.5%	
DRH		+0.5-2.5%	
HST		+0-2%	
PEB (Not Covered)	+3-5%	+1-3%	*Same-property*
PK		+2-4%	
RHP		+1.5-3.5%	*Same-Store Hospitality RevPAR (ex-Rockies)*
RLJ		+0-2%	
SHO	+2.5-4.5%	+0-3%	

Source: Company reports and conference calls

Additional discussion on C-Corps, hotel REITS, and Vacation Ownership names for 2019:

For the C-Corps domestically, we believe Wyndham hotels will have the relatively strongest RevPAR growth rates due to heavy exposure to the economy segment, where new supply is minimal. On the other hand we see HLT as the relative RevPAR underperformer domestically due to high new supply growth rates in the Upscale and Upper Midscale segments. *Conversely*, for new room growth Wyndham will be the laggard and Hilton and Hyatt will be the outperformers. Net-net profitability-wise for a C-Corp it is better to have an additional point of rooms growth than an additional point of RevPAR growth due to the very high margin nature of adding size to the system.

- **For the hotel REITS in 2019 we expect Chesapeake (CHSP, Hold) and Pebblebrook (PEB, Not Rated), due to San Francisco exposure, to be the RevPAR and margin growth leaders, followed by Ryman (RHP, Hold) given limited new completion in their mega-convention hotel category**. At the other end we believe **RLJ** (RLJ, Hold) will be the RevPAR and margin growth laggard due to new supply/competition in its chain scale segments.
- **As we have been writing about for months, one surprise we are forecasting for 2019 RevPAR growth is an acceleration in ADRs as hotels push pricing**. However, such pushes will result in an equal or slightly greater drop in occupancy.

C-Corps: Even in this low growth RevPAR environment, profits are set to increase and companies have ample cash flow and balance sheet capacity to continue share repurchases. It is for these reasons that we continue to favor the hotel C-Corps over the hotel REITS. Within the C-Corps HLT remains our favorite. The primary driver of earnings for C-Corps will not be RevPAR growth but rather global unit/footprint growth. For Hilton and Marriott we estimate 6.6% and 5.7% net rooms growth in 2019, with the rule of thumb being approx. 1.5x unit growth = EBITDA growth.

- **In 2019 international lodging supply growth will become increasingly important to the C-corps**: Due in part to relatively low domestic RevPAR growth (we see no major positive sparks near-term in US lodging demand), we believe investors in the Lodging C-corps will remain focused on the lodging pipeline as key to 2019 and 2020 earnings growth. For the Lodging C-corps in our coverage (ex-Playa (PLYA, Buy), a Caribbean/Latin American focused portfolio), we still see the US as the primary source of new rooms growth for the foreseeable future (currently we see rooms growth for the C-corps as approximately 50-75% in the US and the remainder international). However, due in large part to the mature US lodging market, we continue to expect pipeline mixes will shift increasingly to international markets, especially into Mainland China.
  - **China is the dominant international market for new-build hotels** for most of the Lodging C-corps – no other country comes close (other key markets for growth today are Germany, SE Asia, the UK, and Japan but China pipeline growth by rooms is at least 6-10x these other markets). While we believe most hotels under construction will continue to open (and this should satisfy unit growth well into 2020) we believe friction resulting from US-China

trade negotiations could weigh on overall/global pipeline growth in the mid-term for hotels not yet under construction or approved for development by the franchisors. Investors should be focused not just on 2019/2020 net unit/rooms growth but also the growth and size of the total development pipelines.

- **For US hotel pipeline development in 2019**, we do not see the C-corps pipeline growth as uniform given company-specific considerations although for all the C-corps we see the greatest new build growth in the select-service chain scales (primarily Upscale to Midscale). Given the RevPAR premium (higher fee generation) in the US market for these brands relative to some international/emerging markets, we still consider US pipeline growth as very important for near-term EBITDA expansion:

  - **CHH** continues to push urban growth for Cambria. We continue to see growth opportunities for CHH in particular with Comfort Inn/Suites following the brand's repositioning as well as with the relatively newly acquired WoodSpring Suites. *Secondly, we see CHH as the one company whose net room growth percentage will actually increase in 2019, due to the Comfort Inn refresh program winding down.*

  - **H**'s opportunities are also driven in part from select-service development given its lower base of existing distribution for Hyatt Place/Hyatt House as well as conversion opportunities from the Two Roads brands (due to the recent acquisition we see this as a 2H19 and later story).

  - **HLT**'s pipeline growth will likely be bolstered in 2019 by the relatively nascent Tru and Home2 Suites brands and likely Motto later in the year. We see Tru as one of the core long-term growth opportunities for HLT in the US given developer interest in new-build midscale hotels under HLT's strong loyalty program (MAR and H have no equivalent products in Midscale and both companies appear to be focused on higher-rated select-service hotel development). HLT's net unit growth (NUG) is relatively straightforward given the current focus on new-build development.

  - **MAR**'s growth will continue to be driven from its select-service legacy Marriott brands such as Courtyard and Residence Inn in addition to the wider green space from Legacy Starwood brands (in particular Aloft, Element, and over time Sheraton). We still consider MAR's decision to "deflag" (remove from the portfolio) off-strategy Starwood hotels as a long-term positive although there may still be some noise in 2019 in near-term net rooms growth from unit deletions (this issue will likely dissipate over the course of the year as many hotels scheduled to depart the MAR system have already left).

  - **WH**'s pipeline development is in part a refinement following the focus on deflagging off-strategy hotels. Within the US, we believe investors will be very focused on growth from the relatively recently acquired La Quinta and AmericInn brands. Both brands were regionally focused and thus there are growth opportunities in new markets within the US.

- Even though we see a gradual slow-down in RevPAR growth, we believe Incentive Management Fees (IMFs) will be less volatile than in previous cycles and will continue to grow at a moderate pace.

  - What is important to consider in today's lodging environment is that the increasing diversification of managed hotels – increasingly international and increasingly in regions where profitability hurdles are not commonplace – reduces the dynamic of IMF volatility. For example, in 2007, roughly two-thirds of MAR's managed hotels had an IMF contribution to MAR earnings; in 2009 only ¼ of hotels contributed IMFs. We would not expect such a significant variance to occur today even in a 2008-like RevPAR environment simply due to the change in geographic exposure. While IMF generation was a big topic for investors in the past – and we believe is still relevant today – we expect a low worldwide RevPAR growth environment with mid-single digit rooms growth to combine for moderate incremental IMF growth in 2019.

For hotel REITS, outside of CHSP and PEB due to their large San Francisco exposures, we do not envision any material organic same-store earnings growth in 2019, and in fact most consensus EBITDA estimates look too high by 1-2%. However, fundamentals support stable dividend payouts for hotel REITS, with many yielding over 5%:

Ticker	Current Yield	2020 Base Case Payout Ratio	2020 Scenario Case Payout Ratio	2020 Est. Net Debt/EBITDA		Current PT	2020 Price Target Based on Scenario Case	Price Target Downside Based on Scenario Case
HST	4.2%	59%	66%	1.2x		$22	$19	14%
DRH	4.5%	63%	73%	4.x		$11	$9	18%
SHO*	4.8%	69%	81%	1.1x		$15	$13	13%
RHP	4.3%	69%	82%	4.6x		$76	$64	16%
PK**	7.4%	72%	83%	3.6x		$34	$29	15%
RLJ	7.4%	77%	90%	3.8x		$20	$16	20%
CHSP	5.6%	81%	93%	3.5x		$26	$22	15%

Source: STRH Research, company filings, FactSet

Note: Our modeling does not assume companies make acquisitions to replace disposed assets

*Assumes same special dividend payment as prior year

**Assumes same special dividend payment as prior year (ex-$0.30 from gains from 2018 hotel sales)

- **The bad news for hotel REITS is rising labor costs which will unfortunately likely result in margins flat at very best to down 75bps y/y**. Through February 2019, our analysis of nearly 1,000 P&L statements of high-rated full-service hotels in the U.S. (Luxury and Upper Upscale hotels, both privately and publicly owned) indicates YTD GOP profitability of +60 bps on Rooms RevPAR of +2.5% (source: HotStats). With expected slower RevPAR growth later in the year and tougher comps, we expect margins will come down. Labor costs remain a headwind to margin growth given that many Lodging REITS currently estimate Rooms RevPAR growth of +2.5-3.5% is needed to maintain flat EBITDA margins. In our conversations with both public and private hotel owners, we currently hear that labor costs are growing between 3-4% for most hotels. With labor costs generally growing faster than revenues (ex-the positive tailwind from a strong expected convention year in San Francisco), we expect margins will be flattish to more likely down up to 75 bps y/y in 2019.

Vacation Ownership: Following 2017 where stock price appreciation was primarily driven by an M&A bubble and 2018 where that bubble pop, the companies have tremendous potential to repurchase shares. All four public timeshare companies have indicated willingness to repurchase shares.

- Under **Hilton Grand Vacations'** (HGV, Buy) new $200M share repurchase program, the company bought back 2.5M shares or about 2.6% of its market cap in December. Assuming the company increases its net debt/adj. EBITDA to the higher end of its target range of 1.5-2.0x net leverage, there is ample buyback potential opportunity. We estimate about $600M could be returned to shareholders in the form of buybacks over the next two years, or approx. 20% of the market cap.

- **Marriott Vacations** (VAC, Buy) repurchased 1.2M shares for $94M in 4Q. Subsequent to the end of the quarter it purchased another $78M of shares. The company outlined 2019 adjusted free cash flow between $400-475M, realistically it should have about $350-450M of additional cash that could potentially be returned to shareholders after accounting for one time charges. We believe it not likely given the size of last year's acquisition that VAC will make any sizable acquisitions this year and hence free cash flow and balance sheet should be used rather for share repurchases and dividends.

- **Wyndham Destinations** (WYND, Buy), in 4Q the company repurchased 2.6M shares for $100M. At December 31st WYND had $816M remaining on its share repurchase authorization. Subsequent to the end of the quarter, the company repurchased another $40M of shares through February 25. Concurrent with earnings the company boosted its quarterly dividend by 10% to $0.45 per share. Assuming the company keeps its net debt/adj. EBITDA at the current rate of 2.8x, within its own target rate of 2.25-3.0x, there is significant buyback potential opportunity. We estimate approximately $600M could be returned to shareholders in the form of buybacks over the next two years, or approx. 15% of the market cap. This is on top of the $1.80 (annualized) dividend, a current yield of approx. 4%.

Companies Mentioned in This Note

Choice Hotels International, Inc. (CHH, $76.62, Hold, C. Patrick Scholes)
Chesapeake Lodging Trust (CHSP, $28.38, Hold, C. Patrick Scholes)
DiamondRock Hospitality Company (DRH, $11.04, Hold, C. Patrick Scholes)
Hyatt Hotels Corporation (H, $71.32, Hold, C. Patrick Scholes)
Hilton Worldwide Holdings Inc. (HLT, $82.45, Buy, C. Patrick Scholes)
Host Hotels & Resorts, Inc. (HST, $19.00, Hold, C. Patrick Scholes)
Marriott International, Inc. (MAR, $122.17, Hold, C. Patrick Scholes)
Park Hotels & Resorts Inc. (PK, $31.28, Buy, C. Patrick Scholes)
Playa Hotels & Resorts N.V. (PLYA, $7.62, Buy, C. Patrick Scholes)
Ryman Hospitality Properties, Inc. (RHP, $83.61, Hold, C. Patrick Scholes)
RLJ Lodging Trust (RLJ, $17.83, Hold, C. Patrick Scholes)
Sunstone Hotel Investors, Inc. (SHO, $14.34, Hold, C. Patrick Scholes)
Marriott Vacations Worldwide Corporation (VAC, $93.36, Buy, C. Patrick Scholes)
Wyndham Hotels & Resorts, Inc. (WH, $49.38, Buy, C. Patrick Scholes)
Airbnb (Private)
InterContinental Hotels Group (IHG, $59.90, NR)
Pebblebrook Hotel Trust (PEB, $30.62, NR)

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