Equity Research

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CONSUMER: Lodging

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Reasons for this report

✓ Analysis of forward-looking booking and pricing trends and for US hotels.

May/June RevPAR Monitor: Not seeing signs of any pullback in forward-looking "big data". U/G PK

In this report we discuss:

- **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**
- **Stocks/picks**

Based upon our analysis of millions of future reservations for US hotels from multiple "big data" sources and from conversations with hotel owner/manager contacts and executives at very large travel agencies, the improving forward trends for business and group travel have stayed on an unabated trajectory of recovery since Jan/Feb's omicron pullback. While the most recent booking volumes for corporate transient customers are still down approx. 20% from comparable May 2019 levels, this is a massive improvement from January were they were down approx. 65% from January 2019 levels. Pricing on corporate transient bookings is now tracking up low-single digits from May 2019 levels (but still down 10%+ when accounting for inflation), also an improvement from the down 5-10% in January vs. January 2019 levels. RevPAR for summer leisure travel continues to be up significantly vs. 2019 with the greatest strength in the higher-end segments. That said, as the summer of 2021 was a big recovery year for leisure travel, we continue to see leisure RevPAR "only" up 5-10 percentage points vs. last summer with all the growth coming from ADR, as there is some modest pressure on occupancy due to the difficult y/y comp, additional home rental supply, and the re-opening of Europe as a tourist destination.

To be clear, we are not oblivious to drumbeats in some economic forecasts and in the media surrounding a possible recession in 2023, rather at this time we do not observe US hotel bookings and pricing showing any pullback (yet), or as the head of travel for one of the world's largest corporate travel agencies noted to us when we asked "the pullback question", "We are not seeing any slowdown, quite the opposite" (conversely, please see our research on cruise lines where we have observed negative pricing trends).

- **Concurrent with this report, we are upgrading PK, the second largest hotel REIT, to Buy from Hold and raising our price target to $22 from $19.** While the hotel REIT subsector continues to be plagued by the structural issues that have made it a long-term underperformer, we find PK's valuation combined the aforementioned demand and pricing trends too compelling to ignore.

Implications for earnings estimates/stocks: *Assuming the above noted trajectory of improvement continues through the rest of 2Q and through 3Q, we believe 2Q/2022 company guidances and consensus earnings estimates should be achievable, if not beatable.* **As far as specific stocks/sub-sectors, we continue to be most favorable on the leisure-centric companies, namely WH (Buy) and the Vacation Ownership companies, HGV (Buy), VAC (Buy), BVH (Buy), and TNL (Buy).** Common characteristics besides high leisure exposure include attractive valuations, recovered balance sheets, and return of capital to shareholders via repurchases and/or dividends. To the list of favorites, we include Hyatt (Buy) given its increasing exposure to leisure via its acquisition of Apple Leisure Group and its progress on selling owned assets and shifting to a more asset-lite company. We also continue to favor RLJ (Buy, Miller) driven partly by our continued view of its relative valuation discount and operational enhancements/hotel repositionings supporting incremental EBITDA growth.

SEE PAGE 9 FOR REQUIRED DISCLOSURE INFORMATION

Lastly, we are encouraged by the progress we are seeing in higher-end corporate and group travel and as noted previously are upgrading PK (Buy) to Buy from Hold.

Before discussing observations on the three main customer segments we have some food for thought, because clearly the market says 2023 will see a slowdown:

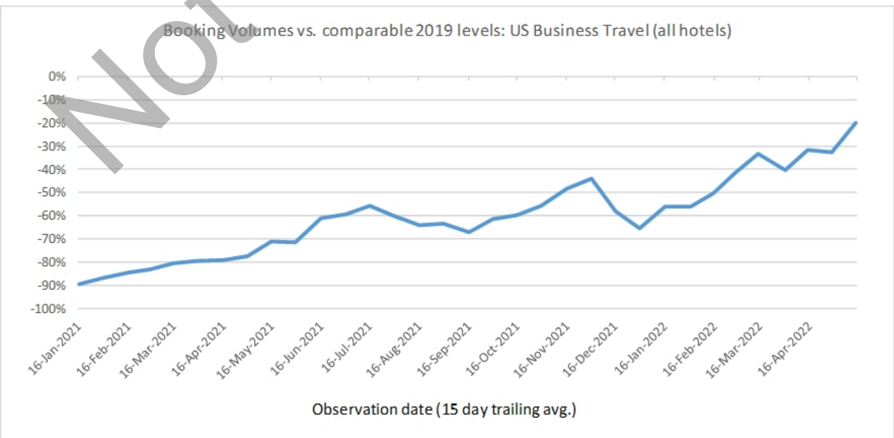
- While our latest observations on forward-looking US hotel bookings and pricing are very positive, the nature of hotel bookings is that there is limited visibility on individual business and leisure travel beyond three months (this summer). *A big unknown is how much of the strength in the pace of business travel bookings is just a "catch-up" from two years of lost business. Then after it has "caught-up", how much gas will be left in the tank and will demand ever get back to 2019 levels (we think probably not?).* In the section we discuss some initial observations on 2023.
- **Room rates, especially for the luxury and resort segments, are hot, and we are experienced and cynical enough to know that when something gets too hot it eventually does not end well for this industry.** Already we are starting to see significant Airbnb (ABNB, Buy, Khan) supply (aka shadow supply) coming back into many warm weather markets and subsequently we expect some of the demand strength will be diluted by this new supply. Please join us on Wednesday, June 15th when we host a webinar with Airdna (private) to discuss the most recent supply, demand, and pricing trends in Airbnb (ABNB, Khan, Hold) and short term rentals.
- For this summer's leisure business, the pace of bookings will likely slow as arrival dates get closer as compared to last year's pace which only got stronger closer to arrival dates. While this makes for a negative headline, we see the slowing pace driven by more limited room availability this summer as more bookings were made earlier in the year whereas last summer many travelers waited until the last minute to book their summer vacations.
- International in-bound demand remains down nearly 50% from pre-Covid levels. As this demand segment continues to gain steam, and assuming Europe and other international markets do not see a recession, this could help offset some (all?) of any recession-driven travel slowdown in 2023, should a recession occur.
- **The one area where we have seen a tangible negative impact to earnings is with higher interest rates, though this should not be a surprise to anyone at this point.** The impact seen so far has been:
  - **Tightening net interest income from securitizations for the vacation ownership companies.** For example, VAC's weighted average coupon on their securitization last month was 4.59%, whereas in November it was 1.64%. Assuming VAC does around $1B of securitizations a year, this increase amounts to approx. $30M annually of lost EBITDA. However, some of this will be recouped by higher interest rates on the initial loans and as companies have often noted, higher VPGs (partially driven by inflation), a measure of sales and selling efficiency, are more than offsetting lost interest income.
- **Share repurchases, which are often paid for by taking on additional debt, become less accretive as debt becomes more expensive.**
- **Interest rates on floating and new debt are higher.**

What does our data and industry contacts say about 2023 at this point? 1) While individual business and leisure bookings for 2023 are de minimis at this point, we have somewhat better visibility with group bookings. For corporate group bookings for 2023 (approx. 20% of bookings committed so far), while still pacing approx. 20% off of comparable 2019 levels, the month-to-month trajectory of improvement is encouraging (see Group discussion later in this report). **2)** Perhaps most importantly, initial indications from our industry contacts are that corporate negotiated rates for 2023 could be up double-digits vs. 2019 levels. Noted was that hotels cannot afford to extend 2019 rates for another year giving rising labor costs and leisure travelers have been more likely to visit midweek while paying a full rate; *ergo hotels will take a stronger stand when it comes to rate negotiations. That said, pricing is one thing and demand/rooms sold is another and this latter point is a major unknown at this time.* Corporate rate negotiations typically begin in June/July and finish in December.

<u>Individual business travel: Examining the most recent forward-looking bookings and pricing:</u>

The improving forward trends for business travel have stayed on a strong trajectory of recovery since Jan/Feb's omicron pullback (Data source: TripBAM).

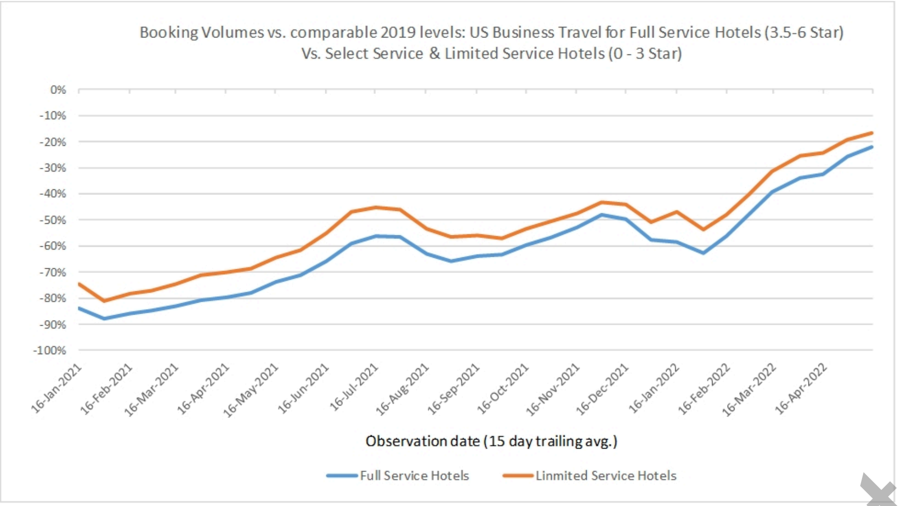
Exhibit 1:



Source: TripBAM, Truist Securities Research

While booking volumes today from larger corporate customers, historically the most important customer segment but surpassed by the leisure traveler over the past 18 months, are still approx. 20% off of comparable 2019 levels, the trend line is encouraging. Reflecting a faster pace of business travel recovery for select and limited service hotels, a category that tends to receive more demand from mid and smaller sized business as opposed to large corporate customers that tend to stay at full-service hotels, recent booking volumes by business travelers for select and limited service hotels are now down approx. 15% from comparable 2019 levels:

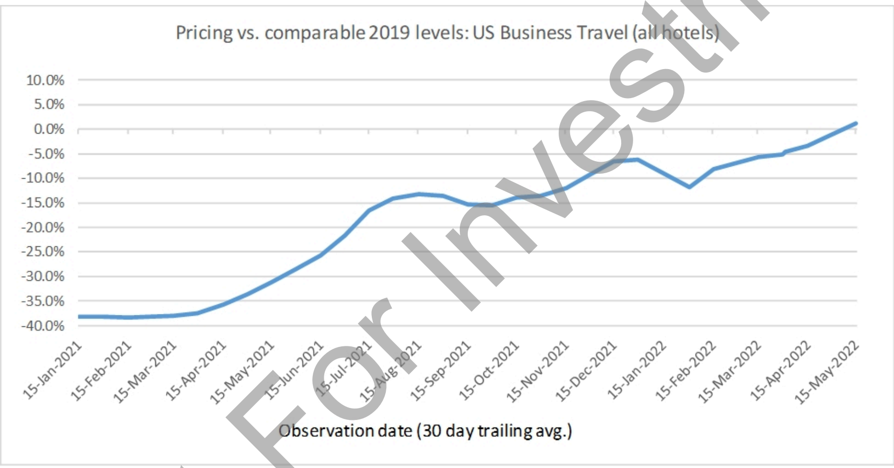
Exhibit 2:



Source: TripBAM, Truist Securities Research

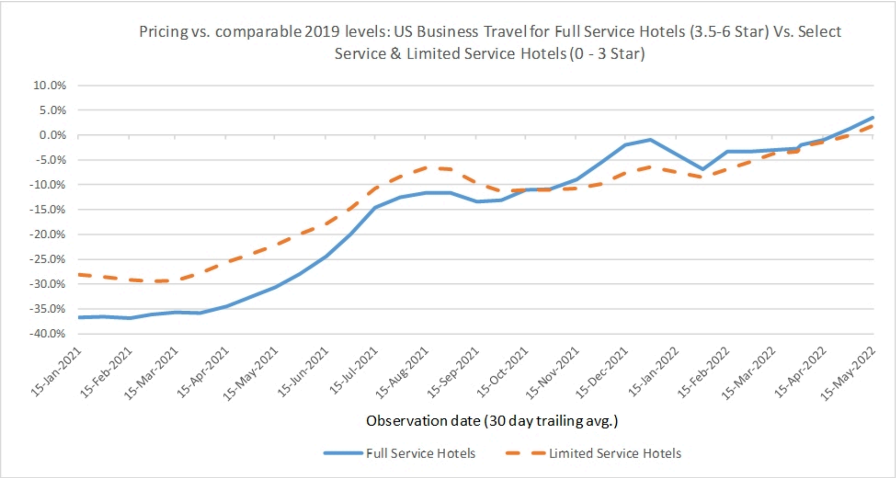
Regarding pricing on new reservations for individual business travel, it is now up low-single digits from comparable 2019 levels for both higher-end properties and less expensive ones, also an encouraging trend line. That said, due to 11% inflation since 2019, "real" ADR for business travel is still down approx. 10% since 2019.

Exhibit 3:



Source: TripBAM, Truist Securities Research

Exhibit 4:

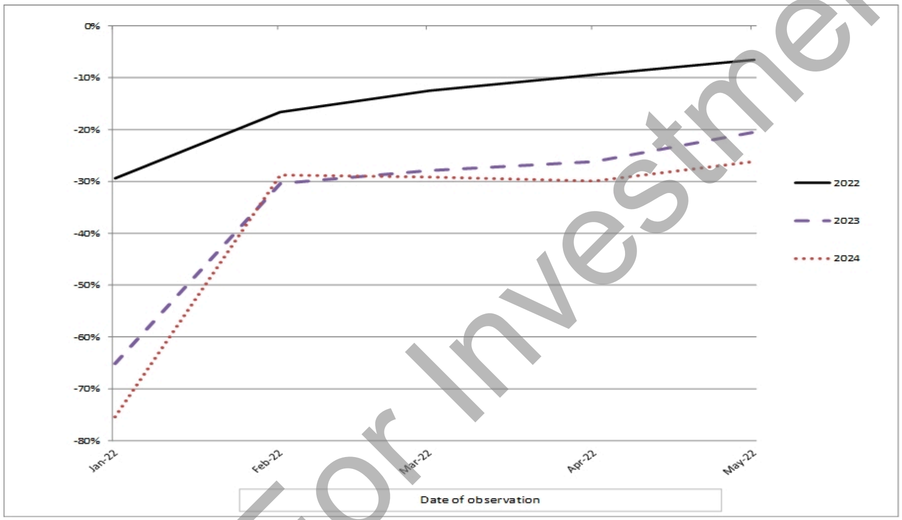


Source: TripBAM, Truist Securities Research

Group observations:

In our analysis of corporate group/meeting trends we look at data from Cvent (Cvent sources approx. 30% of the corporate meetings in the US), amongst other sources. Similar to individual business travel bookings, we observe an encouraging pace of recovery for Groups. As observed in the following chart, we see a stronger pace of recovery for closer-in arrival dates due to the short-term nature of bookings at the moment. Assuming this trend continues, we would expect continued improvement for 2023 and 2024 as arrival dates get closer.

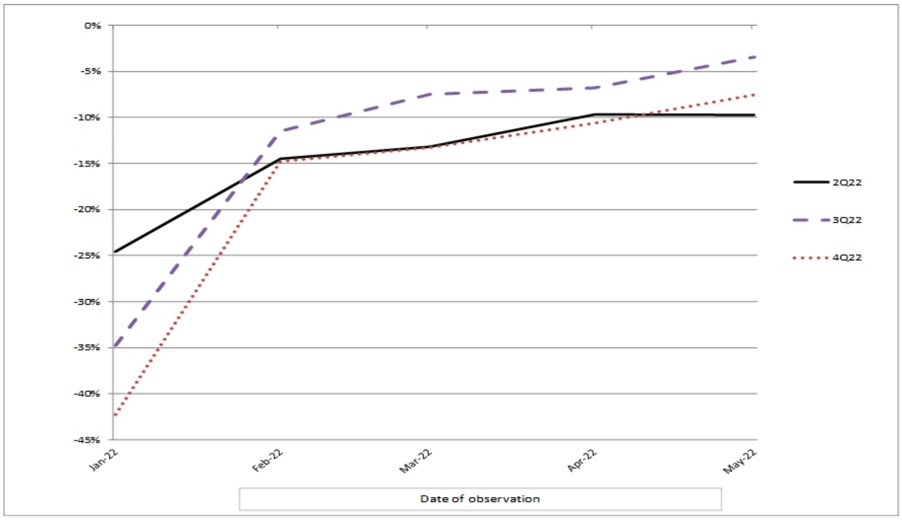
Exhibit 5: Cumulative booking pace vs. comparable 2019



Source: Cvent, Truist Securities

Looking specifically at the booking pace by quarter for 2022:

Exhibit 6: Cumulative booking pace vs. comparable 2019 by quarter

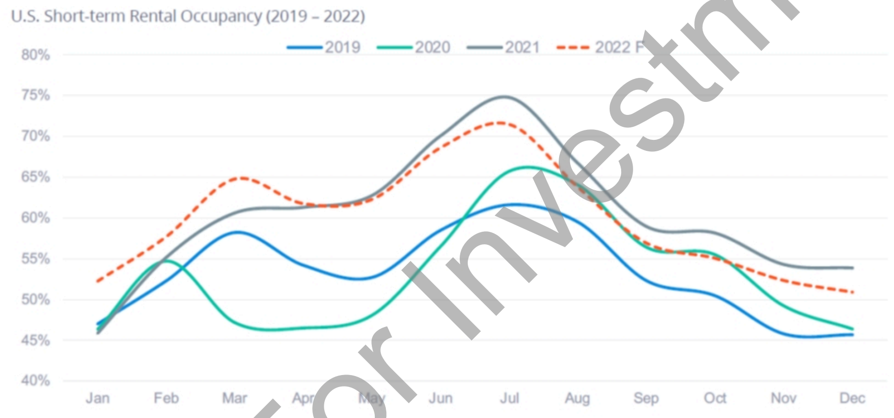


Source: Cvent, Truist Securities

Leisure travel observations:

Leisure booking volumes briefly pulled back in early January but have been on a steady trajectory of improvement since then. From observing forward Airbnb bookings (source: Airdna), due to harder comparisons against last spring and summer's leisure surge, leisure RevPAR for 2022 will likely be below 2021's levels but still well above 2019's levels.

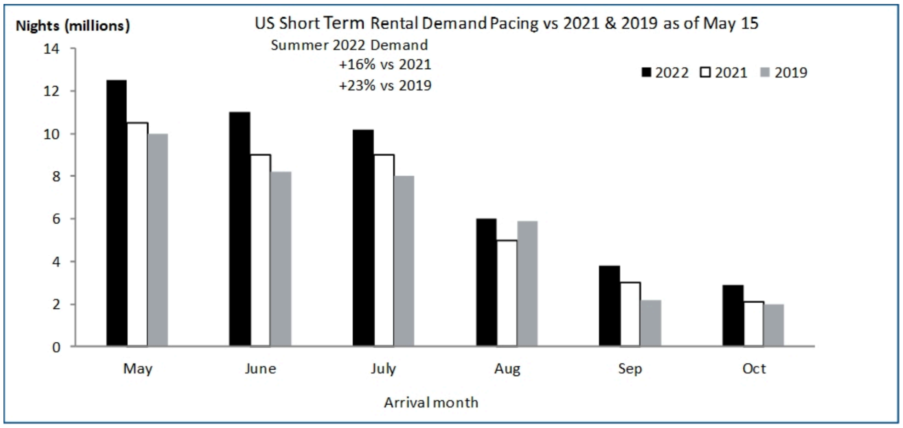
Exhibit 7: Airbnb occupancy forward pacing and forecast. Note that this forecast is a "hybrid forecast" where the forecast for 1H22 is mostly based on actual bookings whereas 2H22 is more based on an economic forecast.



Source: Airdna, Truist Securities

Specifically looking at this summer, we observe that booking pace is well ahead of comparable 2021 and 2019 levels. However, we are the view that as the arrival dates get closer this booking pace will decelerate due to limited last-minute available inventory:

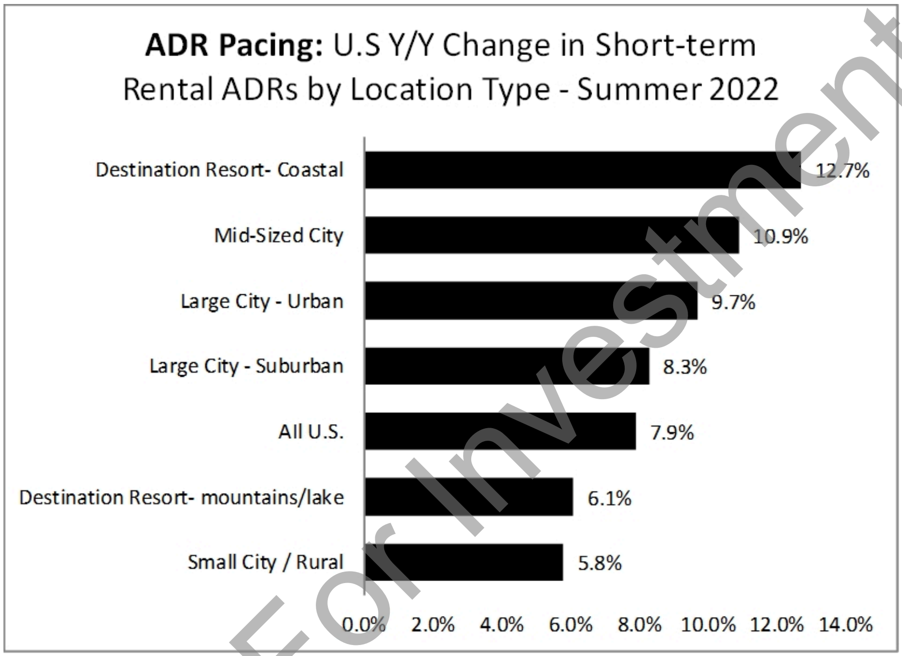
Exhibit 8:



Source: Airdna, Truist Securities

Looking at y/y ADR growth, we observe the summer tracking up 6-13% depending on location:

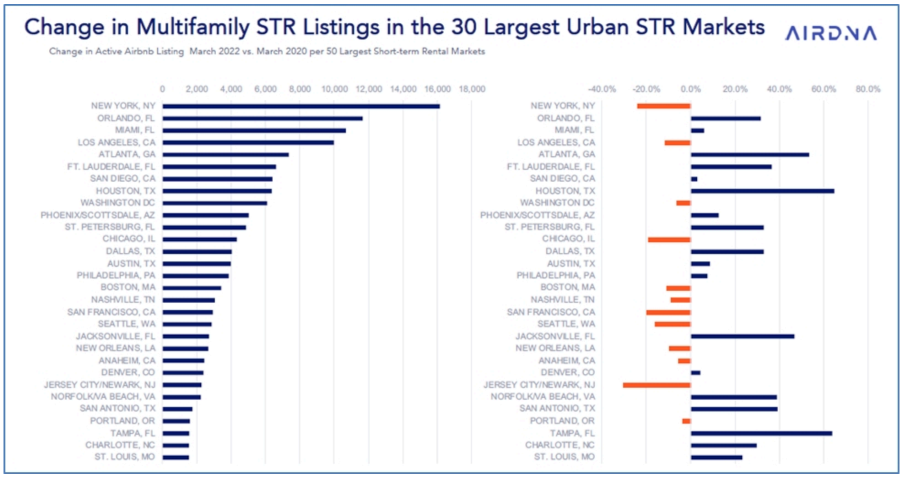
Exhibit 9:



Source: Airdna, Truist Securities

As noted previously, given the strength in warm weather markets, we are starting to see significant home rental supply (aka shadow supply) coming back into many warm weather markets, such as Florida and others, and subsequently, we expect some of the demand strength will be diluted by this new supply:

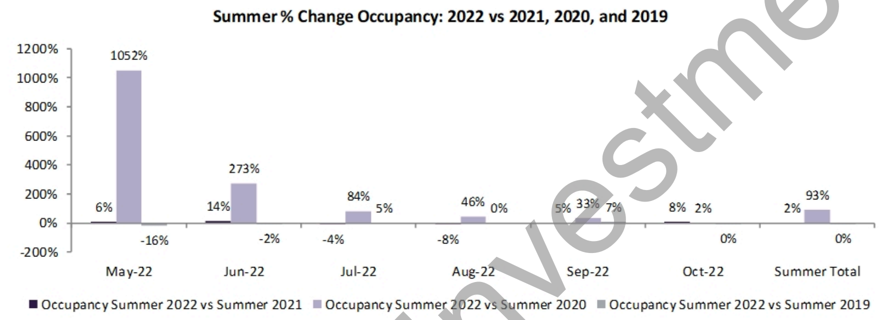
Exhibit 10:



Source: Airdna, Truist Securities

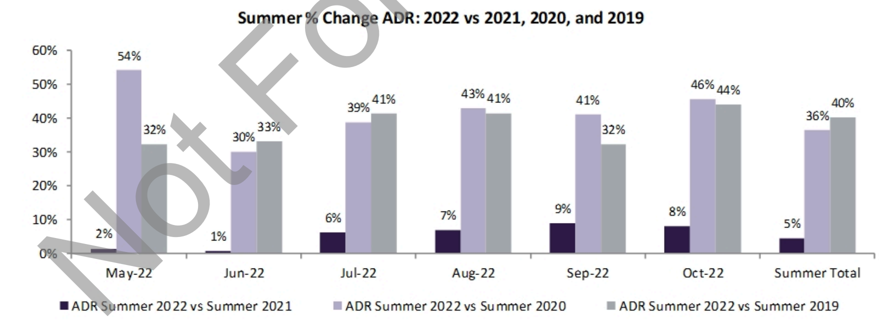
Lastly, to further gauge the strength/weakness of higher-end US leisure travel we also look at future occupancy, rate, and RevPAR pace for hotels at US ski resorts (source DestiMetrics). From this data, we see that, while occupancy vs. summer 2019 is flat, room rates are up significantly. Versus summer 2021, occupancy is also flat and room rates are up mid-to-high single digits:

Exhibit 11: US ski resorts



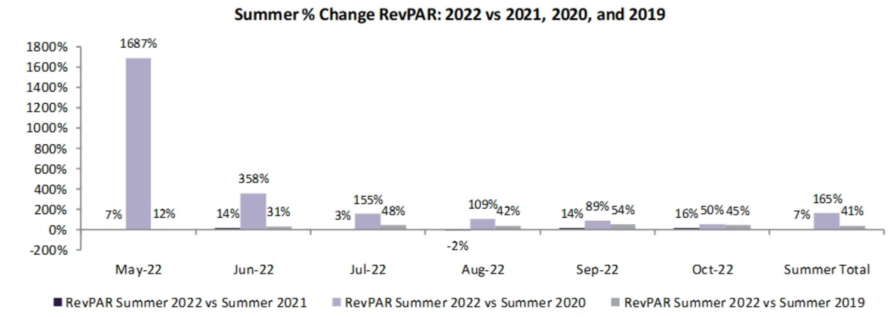
Source: DestiMetrics, Truist Securities

Exhibit 12: US ski resorts



Source: DestiMetrics, Truist Securities

Exhibit 13: US Ski resorts



Source: DestiMetrics, Truist Securities

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

Companies Mentioned in This Note

Airbnb, Inc. (ABNB, $120.87, Hold, Naved Khan)
Bluegreen Vacations Holding Corporation (BVH, $27.86, Buy, C. Patrick Scholes)
Hyatt Hotels Corporation (H, $88.39, Buy, C. Patrick Scholes)
Hilton Grand Vacations Inc. (HGV, $45.75, Buy, C. Patrick Scholes)
Hilton Worldwide Holdings Inc. (HLT, $140.86, Hold, C. Patrick Scholes)
Marriott International, Inc. (MAR, $171.58, Hold, C. Patrick Scholes)
Park Hotels & Resorts Inc. (PK, $18.36, Buy, C. Patrick Scholes)
RLJ Lodging Trust (RLJ, $13.43, Buy, Gregory Miller)
Travel + Leisure Co. (TNL, $51.11, Buy, C. Patrick Scholes)
Marriott Vacations Worldwide Corporation (VAC, $147.72, Buy, C. Patrick Scholes)
Wyndham Hotels & Resorts, Inc. (WH, $80.13, Buy, C. Patrick Scholes)

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