Horwath HTL

Hotel, Tourism and Leisure

MARKET REPORT

United States:
Hotel Market Trends & Analysis

JUNE 2021

Introduction

Midway through Q2 21, the on-again, off-again nature of the economic recovery has been rocky. Short periods of unexpectedly robust growth in GDP, jobs, personal income, consumer spending and unmet consumer demand have been followed by what is hoped will prove to be only intermittent periods of backsliding in such critical areas as jobs, personal income, production and inflation.

For example, as the relatively weak production side of the economy struggles to overcome supply-chain damage to meet consumer demand, stimulus-induced personal income grew at a record rate in March before nosediving in April, a somewhat expected but nonetheless troubling development exacerbated by the steepest year-over-year rise in the Consumer Price Index since September 2008.

In the wake of massive government spending, near-record household savings, relaxed restrictions on social distancing, a large-scale vaccine rollout and a loose monetary policy, consumer spending, which accounts for 70 percent of U.S. GDP, has been the engine driving the economic recovery. To be sure, the U.S. economy is recovering rapidly from its near-disastrous March-April 2020 Covid contractions.
But is it sustainable?

- Over the 14-month period since pre-Covid February 2020, U.S. money supply (M2) increased by an astounding 30%, from $15.47 trillion to $20.11 trillion.
- April retail sales were 17.9% higher than pre-Covid February 2020, the fastest gain for any 14-month period since 1978-79, a period of double-digit inflation versus the 3.1% increase in consumer prices since February 2020.
- With consumers awash in cash, demand for cars and trucks rarely has been higher—retail spending on motor vehicles was up 33.1% in April versus pre-Covid February 2020.
- On the other hand, motor vehicle production in April was down 18.1% versus pre-Covid February 2020 and prices for new and used vehicles have skyrocketed. New cars are largely unavailable due to the microchip shortage and year-over-year used car prices jumped by an average of 16.8%, or $3,296, as even rental car companies are in the market for pre-owned vehicles.
- Though retail sales overall have soared, the production side of the economy has not. Manufacturing production in April was 2.7% less than in February 2020, principally due to damaged supply chains and a slow-to-return labor force.

Conclusion

Were it not for the production side of the economy remaining mired in difficulty—in April versus pre-Covid February 2020, motor vehicle production was down 18.1% and overall manufacturing production was down 2.7% - the surge in retail sales likely would have been far greater. As it stands now, it seems that it is inflation that is unstoppable.

Gross Domestic Product (GDP)

Following the shortest and deepest recession on record, the U.S. economy, as measured by quarter-over-quarter annualized GDP growth, trended upward for the three quarters ended Q1 21, though Q3 20's record-setting pace was succeeded by a respectable but comparatively lackluster Q4 20 performance. Looking more closely at Q4 20, month-over-month GDP growth rates slowed to +0.6% in October, declined -0.8% in November, and remained flat in December amidst fears of a Covid resurgence and the re-imposition of restrictions following a Thanksgiving holiday of ill-advised pre-vaccine travel and non-immediate-family indoor gatherings.

Q/Q Annualized GDP Growth Rates: 2020 and Q1 2021 (Target Range: 2 to 3 percent)

Q1 20	-5.0%
Q2 20	-31.4%
Q3 20	+33.4%
Q4 20	+4.3%
Q1 21	+6.4%

Source: U.S. Bureau of Economic Analysis (BEA)

After a strong 6.4% Q1 21 annualized growth rate, economic activity is returning to pre-pandemic levels and Fed forecasts are for continued y/y GDP growth but at decelerating rates.

Y/Y GDP Growth Rate Forecasts: 2021 and Beyond

2021	+6.5%
2022	+3.3%
2023	+2.2%
2024+	+1.8%

Source: Federal Reserve Board's Open Market Committee (FOMC)

Following the near-disastrous March-April 2020 Covid contraction, swiftly approved government spending went a long way toward keeping the economy intact while multiple vaccines were being developed. GDP growth in Q1 21, particularly March, can be attributed to these actions and to significant numbers of households getting vaccinated and re-engaging in more economic activity as restrictions eased, businesses re-opened and domestic travel—business and leisure—ticked up.

Pent-up demand, ready access to billions of dollars of pandemic-induced savings, and huge direct deposits into personal bank accounts led to a surge in consumer spending. The recovery, however, promises to be a bumpy one.

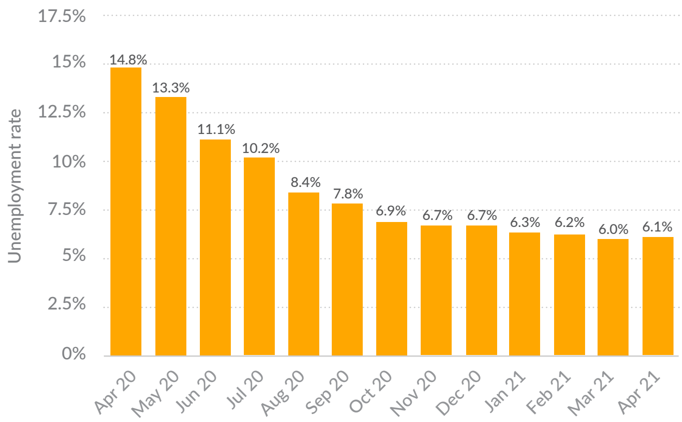
- On the one hand, personal income in March rose by an impressive 21.1%—the largest monthly increase since records have been kept (1959).
- On the other hand, personal income in April declined 13.1%, or $3.2 trillion, as the effects of March's stimulus checks waned.
- Also in April, disposable personal income, after tax and other withholdings, declined 14.6% and personal savings dropped by nearly half, from 28% to 14.9%, but remained sufficiently high to keep month-over-month consumer spending in positive territory—up by a modest 0.5%.

Jobs

By the end of Q1 21, the U.S. had added back 14 million nonfarm payroll jobs, or 62% of the 22.4 million lost in the pandemic. The monthly unemployment rate has declined steadily from its April 2020 apex of 14.8% to its Covid-era nadir of 6.0% in March 2021. However, the pace of new hires is slowing as the Covid-impacted economy continues to find new, less labor-intensive ways to do business.

The 6.1% unemployment rate for April, up 0.1 percentage points over March, reflects the first uptick in a year of near-steady declines. While this directional turn may yet prove to be an aberration, the number of long-term unemployed (looking for 27+ weeks) and newly laid off unemployed (in the past 5 weeks) remains high at 4.2 and 2.4 million respectively.

U.S. Monthly Unemployment – April 2020 to April 2021



Source: U.S. Bureau of Labor Statistics and Statista 2021

Based on the pace of hiring from January to March, forecasters anticipated one million new jobs would be created in April. Instead, seasonally adjusted nonfarm payrolls rose by only 266,000, one of the biggest monthly forecasting misses on record, and the unemployment rate increased, albeit modestly, for the first time in 12 months. At 6.1 percent, or 9.8 million persons, April unemployment remained virtually unchanged from 6.0 percent in March but was higher than the projected 5.8 percent.

On the other hand, unadjusted nonfarm payrolls increased by ±1 million each month of Q1 21, a milestone only ever reached during this recovery. And while the seasonally adjusted April jobs report was disappointing, non-seasonally adjusted job gains continued the Q1 trend and increased by ±1 million as well, led by leisure and hospitality (331,000), restaurants and bars (187,000), arts, entertainment and recreation (90,000), and hotels (54,000).

Assuming the vaccine rollout continues apace as the $1.9 trillion American Rescue Plan is fully deployed during the remainder of 2021, there will be plenty of positions to fill. Somewhat disconcerting, however, is that many businesses, particularly though not exclusively in the services sector, already are reporting difficulty finding workers. In April there were 1.1 unemployed workers available for every job opening, suggesting that, unlike previous recessions, a shortage in labor supply is as problematic as a shortage in labor demand—jobs are available, but people either don't want to work or are unable to work.

So long as supplemental unemployment checks continue to be paid while companies, particularly those in leisure and hospitality, strive to reopen during the peak-demand summer months, and so long as half of the four million workers who left the labor force during the pandemic do not return to the workforce, as is expected, the labor supply problem will worsen. In March, the manufacturing sector alone—which already has been hampered by supply-chain problems, had its recovery further impeded by labor shortages as it sought to fill more new positions than the already robust 53,000 it settled for. That said, unemployment projections are for continued improvement.

Unemployment Rate Projections: 2021 and Beyond

2021	+4.5%
2022	+3.9%
2023	+3.5%
2024+	+4.0%

Source: Federal Reserve Board's Open Market Committee (FOMC)

Inflation

Consumer spending is the biggest factor behind economic growth in the U.S. In March as in 2020, federal stimulus and supplemental unemployment checks helped fuel an economic revival by boosting month-over-month personal income by a record 21.1%—the largest monthly increase on record.

Inflation is running hot and seems unstoppable. In April versus a year ago, producer prices were up 6.2%, the Consumer Price Index (CPI) was up 4.2%, the Bureau of Economic Analysis (BEA) price index rose 3.6%, the biggest increase since 2008, and the core BEA price index, which excludes volatile food and energy prices, gained 3.1%, the biggest monthly gain since 1992. Also in April, core PCE (personal consumption expenditures, excluding volatile food and energy prices) rose 3.1%, among the highest monthly gains in 29 years. Core PCE is the Fed's most relied upon inflation index, so these near-record price increases must be taken seriously, especially as American incomes nosedived in April. Extreme price increases—e.g., automobiles, homes, household durables and lumber—already are threatening consumer spending, as seen in the declining consumer sentiment index for May. Investors worry that if this continues the Fed will be forced to curb its easy money policies.

What is behind these steep price increases across such a broad spectrum of indexes? Some point to the massive, 18% year-over-year increase in M2 money supply to an all-time high in April, subscribing to the theoretical and seemingly logical belief that "inflation is too much money chasing too few goods." Empirically, however, over the past decade central banks have increased money supply numerous times—mostly via quantitative easing (purchasing bonds and other assets on the open market to stimulate lending and investment) without seeing a rise in inflation. The Fed chair even went so far recently as to say that we must "unlearn" the idea that money growth causes inflation.

Accordingly, the Fed maintains these near-record price increases are (a) transitory, insofar as they are a function of overstated year-over-year comparisons with April 2020, a period when prices were falling during the onset of the Covid-19 crisis, and (b) temporary, to the extent they are a function of Covid-related supply chain problems currently being remedied. Once supply again meets demand, prices are expected to normalize, especially as the heady effects of the most recent round of stimulus checks wear off.

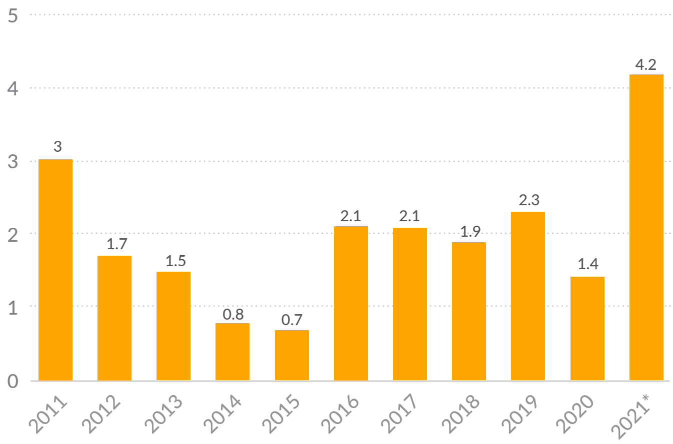
Inflation concerns aside, the March and April reports on business from the Institute for Supply Management (ISM®) are encouraging. They suggest optimism and confidence among purchasing managers that economic activity will continue to increase through the remainder of 2021.

In the 11th straight month of growth, the Services Purchasing Managers' Index (PMI®) for March set an all-time record of 63.7%, dipping only slightly in April to 62.7%. As services were particularly hard hit by the pandemic, these are promising results for a full recovery for a major segment of the economy.

While purchasing activity is strong, price increases are of concern. In April, the ISM® Services Prices Paid Index surged 39.4% year-over-year and 3.8% month-over-month to 76.80 from 55.10 and 74.00, respectively. Damaged supply chains and depleted inventories resulting from Covid lockdowns and stay-at-home orders have created supply shortages which place upward pressure on prices, especially during periods of robust demand.

Money supply growth and base-year comparison arguments notwithstanding, price spikes of this magnitude clearly suggest inflationary pressure is mounting and overshadowing the recovery.

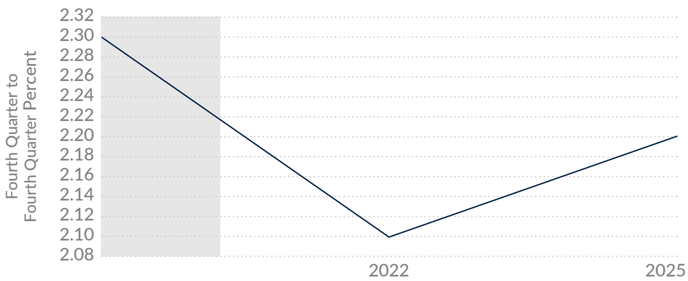
United States Annual Inflation Rates (2011 to 2021)



Source: CoinNews Media Group, LLC

Looking ahead, the FOMC's summary of economic projections for personal consumption expenditures (PCE) are for core PCE to rise 2.3% this year, 2.1% in 2022, and 2.2% in 2023—all manageable but still above the Fed's core inflation target of 2%. (See graph below.)

FOMC Projections for Core Personal Consumption Expenditures



Note: Core PCE excludes volatile food and energy inflation rates.
Source: FRED, Federal Reserve Economic Data, Federal Reserve Bank of St. Louis

Historical Lodging Industry Trends and Future Outlook

The history of the lodging industry is characterized by periods of rapid expansion and development, followed by periods of adjustment and recovery. The paragraphs which follow discuss historical and current industry supply and demand, occupancy rates, average daily rates (ADRs), and revenues per available room (RevPARs). The principal resources used for the following discussion on national lodging industry trends include: AHLA, Business Traveler USA, CBRE Econometric Advisors, Cleveland Research Company, Cornell Center for Hospitality Research (CHR), CoStar, Deloitte LLP, Horwath HTL, The Highland Group, Hotel Business, Hospitality Insights, Hospitality Net, Hotel News Now (HNN), Hotels Magazine, Hotel Online, Kalibri Labs, Linchpin SEO, Lodging, Reuters, STR, Today's Hotelier (by AAHOA), Tourism Economics, Tripadvisor, Yahoo Finance.

The post-Great Recession period of 2010 through 2019 saw the U.S. hotel industry experience 10 consecutive years of RevPAR growth. However, pre-pandemic 2019 was showing signs of an industry-wide slowdown: year-over-year occupancy rates remained flat at 66.1% and ADR increased by only 1.0%, well below the then 2.3% inflation rate, and the resultant 0.9 percent RevPAR growth rate—well below the 3.2 percent average—was the lowest since the recovery began in 2010. These 2019 harbingers of what a non-pandemic 2020 might have looked like are tempered by viewing the data from a different perspective. Rates of growth notwithstanding, 2019 posted the highest numbers ever benchmarked by STR: $131.21 ADR, $86.76 RevPAR, 1.9 billion rooms supply, and 1.3 billion rooms sold.

For the nine-year period of 2010-2018, inclusive, rooms supply growth lagged demand growth. During this state of "positive disequilibrium," year-over-year ADR increases were the norm. Then, for the first time in a decade, the industry entered a state of "negative disequilibrium." In 2019, supply grew 2.0%, narrowly exceeding the 1.9% growth in demand. Typically, whenever supply growth equals or exceeds demand growth, ADR becomes the sole determinant of RevPAR gains, and for the six pre-Covid quarters ended December 2019, this single RevPAR driver's growth rate was sluggish. In fact, year-over-year 2019's ADR growth rate lagged the rate of inflation by 56%, meaning hotel revenue growth did not keep pace with rising wages and other operating costs.

As seen below, demand growth exceeded room supply growth from 2011 through 2018. While 2018's +2.0 percent supply growth rate remained constant in 2019, for the first time since the Great Recession of 2007-2009 it outpaced waning demand growth. Pre-pandemic 2019's 1.9 percent growth in demand represents a year-over-year negative change of minus 24% from the 2.5 percent growth rate of 2018. In other words, demand was beginning to trend down prior to Covid-19.

The year-over-year rate of change in room supply grew steadily from 0.5 percent in 2011-2012 to 2.0 percent in 2018 and 2019. While relatively strong, U.S. supply growth remained manageable through mid to late 2019, when an uneven amount of new inventory was coming online and troubling signs of crowding out were beginning to emerge, especially in the limited-service sector generally and in upper-upscale asset classes in urban markets.

During Covid-recession-riddled 2020, growth rates for room supply and demand declined precipitously, causing a rapid deceleration in pricing power (see below). While alarming, little could be done beyond scaling back and cutting costs, as the root cause, Covid-19, was random rather than systemic.

The aforementioned pre-pandemic 2019 negative disequilibrium became a full-blown crisis in 2020, as seen below in the key performance indicators (KPIs):

- Room supply growth declined from a positive 2.0% in 2019 to a minus 3.6% in 2020.*
- Demand growth decelerated from an already waning +1.9% in 2019 to a blisteringly negative -35.7% in 2020.*
- Occupancy rates fell -33.3% in 2020 from a 23-year record high of 66.2% in 2018 and still-strong 66.0% in 2019.*
- ADR (aka pricing power) decreased -21.3% from a 24-year record high of $131.13 in 2019 to an eight-year low of $103.25 in 2020.*
- RevPAR, which arguably is the most important performance metric, plunged -47.5% from a 24-year record high of $86.64 in 2019 to $45.48 in 2020.*

** Source: CoStar, STR and Tourism Economics.*

Room Supply and Demand

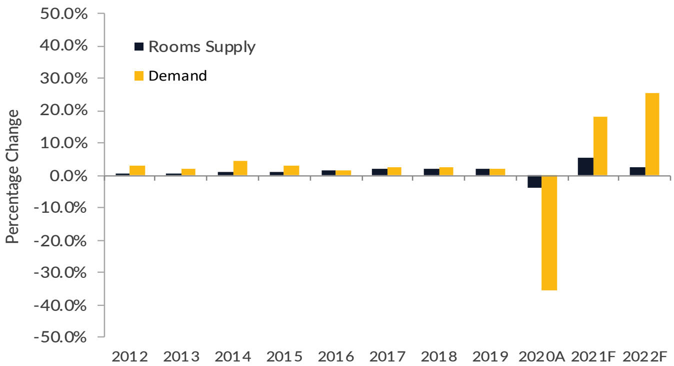
As illustrated in the graph below, demand growth outpaced supply growth from the back end of the financial crisis in 2011 through 2018.

In 2019, 2.0% supply growth exceeded 1.9% demand growth, the first state of negative disequilibrium since the Great Recession. This situation was greatly exacerbated by the Covid pandemic: rooms supply decreased -3.6% but demand decreased -35.7%.

Looking ahead, the outlook is positive:

- **2021 Forecast** – 5.4% supply growth, 18.0% demand growth
- **2022 Forecast** – 2.4% supply growth, 25.2% demand growth

Lodging Industry Supply and Demand Growth



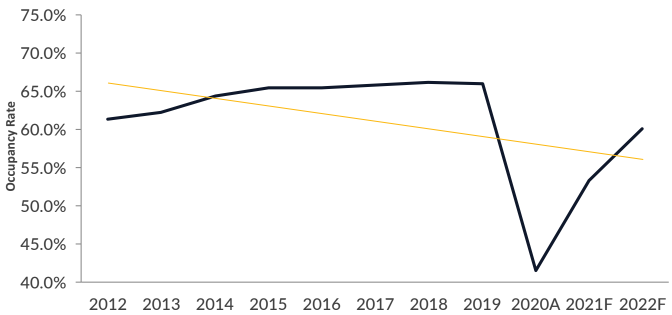
Source: CoStar, STR & Tourism Economics

Occupancy

As illustrated above, year-over-year room night demand growth surpassed room night supply growth for the seven years ended 2018, when occupancy rates peaked at a best-ever 66.2% before declining moderately to 66.0% in 2019.

Then, during the Covid pandemic year of 2020, occupancy rates plunged to 41.6%, an alarming -37% year-over-year decline.

National Occupancy Rates



Source: CoStar, STR & Tourism Economics

As with supply and demand growth depicted in the preceding section, the outlook going forward is for strengthening occupancy growth:

- **2021 Forecast** – 53.3% occupancy, a 28.1% y/y positive change
- **2022 Forecast** – 60.1% occupancy, a 12.8% y/y positive change

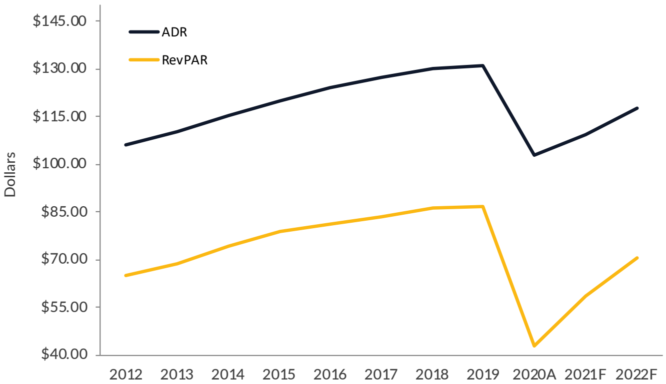
ADR and RevPAR

Two important hotel performance indicators are average daily rate (ADR) and revenue per available room (RevPAR). As seen below, for the eight years ended in 2019, ADRs increased at a compound annual growth rate of 3.1 percent, from $106.21 in 2012 to $131.21 in 2019.

During this same period, RevPAR increased at a compound annual growth rate of 4.2 percent, from $65.10 in 2012 to $86.64 in 2019. From 2012 through 2015, RevPAR growth was simultaneously occupancy- and ADR-driven. From 2016 through 2019, RevPAR growth was overwhelmingly ADR-driven.

RevPAR increased annually from 2012 through pre-pandemic 2019, when it grew at a rapidly weakening year-over-year rate only 0.8%, the lowest growth rate since the Great Recession. Then in Covid-year 2020, RevPAR growth plummeted -50.5%, from $86.64 to $42.88.

National ADR and RevPAR



Source: CoStar, STR & Tourism Economics

Consistent with supply, demand and occupancy growth rates as depicted above, the outlook for ADR and RevPAR growth is strong:

- **2021 ADR Forecast** – $109.47, a 6.3% increase over $103.00 for 2020 actual
- **2021 RevPAR Forecast** – $58.39, a 36.2% increase over $42.88 for 2020 actual
- **2022 ADR Forecast** – $117.34, a 7.2% increase over the $109.47 forecast for 2021
- **2022 RevPAR Forecast** – $70.57, a 20.9% increase over the $58.39 forecast for 2021

Resources

The resources consulted by the authors during the preparation of this report include:
The Associated Press (AP News), Bank of America, Bloomberg, Bureau of Economic Analysis (BEA), Bureau of Labor Statistics (BLS), Center on Budget and Policy Priorities (CBPP), Cision PR Newswire, CNBC, CNN, Conference Board, Congressional Budget Office (CBO), CoStar Economy, Federal Open Market Committee (FOMC), Federal Reserve Bank of St. Louis, First Trust Advisors, Forbes, Fortune, Fox News, Goldman Sachs, Harvard Business Review, Hospitality Insights, Impact Data Source, Institute for Supply Management (ISM), International Monetary Fund (IMF), JPMorgan, Kiplinger, Marcus Millichap, Money Talks News (MTN), Morgan Stanley, Nashville Business Journal, National Association for Business Economics (NABE), National Bureau of Economic Research (NBER), Navy Federal Credit Union, Oxford Economics, Pew Research, PNC Financial Services Group, Rand Corporation, Sky News, Slate, Statista, The Atlantic, The Balance, The Hill, Trading Economics, US News, Wall Street Journal, Washington Post, and World Economic Forum.

Authors

Mike Cummings MAI ISHC
Managing Director
Horwath HTL Norfolk
mcummings@horwathhtl.com

Michael Cummings, MAI ISHC, is a Managing Director in the USA with offices in Norfolk, New York, Orlando, Miami, Denver and Mexico. He brings over 20 years of professional consulting experience to Horwath HTL.

He holds a Bachelor of Science in Business Administration, with concentrations in Finance and Real Estate from Old Dominion University, is a Designated Member of the Appraisal Institute (MAI), a member of the International Society of Hospitality Consultants (ISHC), and actively holds appraisal licenses in over twenty states.

Richard Keegan
Senior Associate
Horwath HTL Orlando
jrkeegan@horwathhtl.com

Richard Keegan is a Certified General Appraiser and Senior Associate in the USA, based in Orlando. He brings over 35 years of hotel management, development, consulting and appraisal experience to Horwath HTL. Richard holds a Bachelor of Arts Degree and Master of Business Administration (MBA) Degree from the University of Wisconsin. He is a Practicing Affiliate of the Appraisal Institute.

Horwath HTL

At Horwath HTL, our focus is one hundred percent on hotel, tourism and leisure consulting. Our services cover every aspect of hotel real estate, tourism and leisure development.

Our clients choose us because we have earned a reputation for impartial advice that will often mean the difference between failure and success. Each project we help is different, so we need all of the experience we have gained over our 100-year history.

We are a global Brand with 45 offices, who have successfully carried out over 20,000 assignments for private and public clients. We are part of Crowe Global, a top 10 accounting and financial services network. We are the number one choice for companies and financial institutions looking to invest and develop in the industry.

We are Horwath HTL, the global leader in hotel, tourism and leisure consulting

Our Expertise:

- Hotel Planning & Development
- Hotel Asset Management
- Hotel Valuation
- Health & Wellness
- Transactional Advisory
- Expert Witness & Litigation
- Tourism & Leisure
- Hospitality Crisis Management

Horwath HTL

Hotel, Tourism and Leisure

AFRICA
Rwanda
South Africa

ASIA PACIFIC
Australia
China
Hong Kong
India
Indonesia
Japan
Malaysia
New Zealand
Singapore
Thailand

EUROPE
Andorra
Austria
Croatia
Cyprus
Germany
Hungary
Ireland
Italy
Netherlands
Poland
Portugal
Russia
Serbia
Spain
Switzerland
Turkey
United Kingdom

LATIN AMERICA
Argentina
Brazil
Chile
Dominican Republic
Mexico

MIDDLE EAST
UAE & Oman

NORTH AMERICA
Atlanta
Denver
Los Angeles
Miami
Montreal
New York
Norfolk
Orlando
Toronto

www.horwathhtl.com