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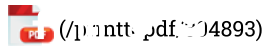
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Harsh reality faces hotel companies in Q3

20 OCTOBER 2020 7:43 AM

With the late-summer leisure bubble bursting and no rebound in group or business transient travel, publicly listed hotel companies will be challenged to paint a happy picture for the third quarter, analysts said.



By Sean McCracken (/Author/733/Sean-McCracken) and Bryan Wroten (/Author/734/Bryan-Wroten)

REPORT FROM THE U.S.—Publicly traded hotel companies will be challenged to come up with any kind of optimistic outlook during third-quarter earnings calls, as analysts say any hopes of a quick recovery have been dispelled.

Michael Bellisario, senior hotel research analyst and director at Baird, said many analysts are now issuing grim analyses of the hotel industry and revising earnings estimates further downward.

"Things are tough, I agree," he said. "I think the biggest thing is that urban, big-box business travel and group business are coming back more slowly than people hoped 90 days ago or even 180 days ago."

Rich Hightower, managing director and lodging research analyst at Evercore ISI, similarly said it's going to be a challenging environment for the hotel industry for the foreseeable future. He believes many people are now coming to the realization that they might have underestimated a demand bubble around the late summer season that seemed to have ended around Labor Day.

"It's pretty clear with the second or third wave we have going on now, and increased (COVID-19) case counts, that the data seems to be rolling over, and it doesn't seem like there will be much of a (demand) push through year's end," he said.

The industry's fortunes will likely remain in flux until a vaccine and therapeutics are widely available to the traveling public, Hightower said.

The New York state government met recently to discuss its strategy for when a vaccine is available, said C. Patrick Scholes, managing director of lodging and experiential leisure, equity research at Truist Securities. In that five-point priority list, those who are healthy people younger than 65 working non-essential jobs are last. Scholes said that matches his description, just as it does many other business travelers, and his company won't let him travel until everyone is vaccinated.

"I'm not alone," he said. "Multiply my scenario by hundreds of thousands of people, millions."

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At this point, Hightower said he's assuming a five-year recovery period from this crisis with a "slow build" in 2021.

Scholes said it's likely 2022 at the earliest that the hotel industry will start seeing performance that's close to what the industry saw before the pandemic. Leisure travel is on a trajectory to recover by the back half of next year, but that also depends on hotel types and whether the markets are drive-to markets. Fly-to business, international travel and urban markets like New York City are going to take a while.

In recent quarters, analysts have focused a lot on how much capital companies have available and their cash burn rate, but Hightower said that cash burn has seemed to have slowed for many companies. But that doesn't fully address the potential crisis.

"Most hotel (companies) are still burning cash every month," he said. "Some can withstand it better than others, and others are closer to the edge. I'm convinced there will be an equity infusion across the space, potentially of several billion dollars."

Bellisario said it will be six months to a year before hotels businesses can get back to operating in a more standard mode of operating as opposed to just burning cash.

"The hotel (real estate investment trusts) I track continue to trade sideways, and the estimates will continue to have to come down for the next several quarters," he said. "It will be hard for them to break out of that trading range, other than Apple (Hospitality REIT) and Summit (Hotel Properties) because of their better fundamentals."

What's the Q3 focus?

Given the bad performance metrics, many hotel brands will be primarily focused on their pipeline and touting how net unit growth remains relatively strong, Bellisario said.

"Net unit growth is still healthy despite the pandemic and the stalling of hotel development," he said. "A lot of the pipeline is in (the Asia/Pacific region) or already under construction."

But he noted analysts and investors might have a hard time cutting through the noise in that regard, noting that "nobody batted an eyelash" over Service Properties Trust's decision to convert their Marriott International portfolio (<https://hotelnewsnow.com/Articles/304735/Service-Properties-Trust-ends-agreements-with-Marriott>) to their sister company Sonesta's brands.

"When we get to February and have Q4 conference calls, people will have forgotten there was a 100-basis-point impact from those terminations," he said. "And the deletions at Wyndham are a real thing."

It's a tale of two hotel industries, Scholes said. Hotels in the economy segment are seeing a U-shaped recovery while those at the upper end, especially in urban locations, continue to severely struggle.

"Unfortunately, that's going to be a big theme for the (Q3) earnings, (Q4) and even into (Q1) next year," he said. "There are early indications of (Q2) next year not looking so hot either for business travel hotels."

Wyndham Hotels & Resorts and Choice Hotels International will beat on those earnings because economy RevPAR was better than modeled a couple months ago, Scholes said. The hotel REITs, particularly the full-service hotel REITs, are likely to miss on RevPAR while Marriott International and Hilton will fit in the middle.

Hightower noted the C-corps remain in relatively better positioning than the REITs due to both their international exposure and asset-light models, although many international markets, particularly in regions like Europe, are not much better off than those in the U.S.

Among the more challenged REITs are Park Hotels & Resorts, which Hightower said is in a bad spot because of relatively high leverage and a portfolio of big-box hotels reliant on group business that's unlikely to return for a long time, and Ashford Hospitality Trust, which Bellisario said is facing major cash issues that threaten its immediate future.

Ashford stockholders recently approved a plan to convert preferred stock to common stock, along with a cash payout, but Bellisario said the company doesn't have the \$30 million on hand to fund the cash component of that plan by the 30 October deadline, even after having delayed it once.

"If we fast forward two weeks, they might have to extend it again," he said. "When we think about how they raise capital, their options are going to be limited, and capital providers know that. ... It's going to be expensive capital and will probably be shockingly high. But they'll figure it out and survive."

Hightower also noted that some issues that would normally be major discussion points, like the possibility of rolling back corporate tax cuts following the U.S. presidential election, are not rising to the top of the agenda simply due to the overwhelming impact of the pandemic.

"Maybe (tax policy is) not all that impactful, right now, but it's something we'd normally care about," he said.

Over the last several quarters, the publicly traded hotel companies have not provided any earnings guidance into future quarters, a practice that will continue this time round as well, Scholes said. Much of that has to do with having a limited booking window.



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"Right now, the booking window is 10 days or less versus 30 to 45 days on average historically," he said. "There's means the company's like, 'We have no visibility. There is no visibility.' It's tough to make a forecast, the put-your-flag-in-the-ground type of forecasts."

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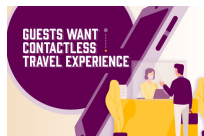
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