Outlook for Hotels Remains Bifurcated in 2022; Investment Demand Surging Back This Year

Summer vacations jump-started recovery. The U.S. lodging sector entered the autumn season having made up substantial ground during the spring and summer months. Loosened capacity restrictions, vaccine availability and pent-up travel demand led to a marked increase in trips taken and rooms occupied. By the end of July foot traffic through airport checkpoints had recovered to about 80 percent of 2019 volumes, driven largely by leisure travelers, while hotel occupancy had roughly doubled from where it began 2021. Nightly rates improved even more notably, with the average daily rate for July surpassing the same metric from two years prior by 6 percent. Although partially mitigated by inflation, the rapid ADR recovery underscored the strong demand to get away that manifested this year.

Summer-to-autumn transition reveals seasonal walk back in visitation. From the start of August into the first weekend of October occupancy followed its traditional pattern, declining 630 basis points to 61.7 percent. The reduction was largely seasonal, with the start of in-person schooling limiting travel for many families. For the same window in 2019, occupancy fell by a similar 600-basis-point margin. Rising COVID-19 infection rates may have also weighed on travel plans. Of the areas reporting steep climbs in cases, many were also favored vacation spots. Moving into 2022 hotel room demand nationally will likely follow typical seasonal patterns while trailing pre-pandemic levels by a shrinking margin. Property performance will still vary significantly by location and service level, however.

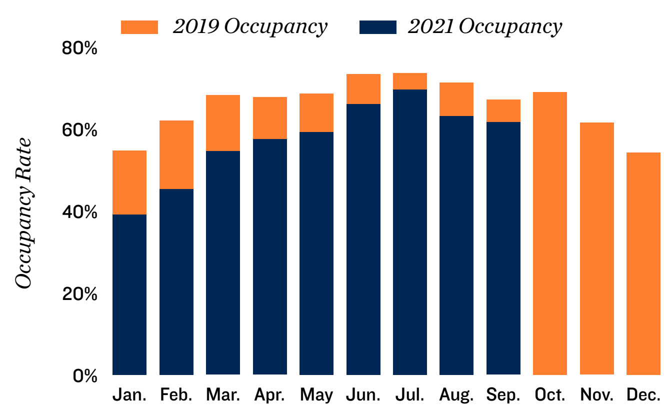
Leisure demand still dominant in 2022. Hotels in popular vacation destinations are projected to perform best next year, including those near beaches and parkland. These types of settings, including the Florida Keys, Colorado Springs and Virginia Beach, captured a large amount of demand during the past spring and summer. Hotels in drive-to locations reliant on regional vacationers will continue to draw travelers; however, they may lose some guests to more well-known areas as comfort with flying improves and barriers to international travel lighten. Therefore, while leisure travel is expected to grow further in 2022, room demand may be more diffused across markets as the overall economy will be more widely open.

More potent need to unwind lifts outlook for resorts next year. Resorts are likely to benefit in the months ahead as vacationers venture farther and seek relaxing settings after a challenging period. As of September 2021, resorts were still about 12 percent less occupied on average than two years prior, although ADR had climbed 22 percent above the same benchmark. Higher nightly rates are offsetting fewer reservations, resulting in an above-pre-pandemic level of revenue per available room. Even if a price ceiling on ADR manifests, resort RevPAR should continue to improve in 2022 due to climbing occupancy levels. Room demand will be aided by more international visitors.

Business travel outlook mixed. Hotels that cater to business travelers will continue to face hurdles next year. Travel for business purposes has so far lagged leisure trips in recovery. While vaccines and tests are widely available, the potential for new coronavirus variants presents ongoing safety concerns that will prompt many employers to minimize staff travel. As such, the number of business trips is likely to trail more traditional levels by a wider margin than the leisure segment. That does not mean business travel will not improve next year in comparison with 2021. Barring a significant reversion in the health crisis, more conventions and trade shows should take place in 2022, with greater emphasis on physical attendance, prompting greater professional travel.

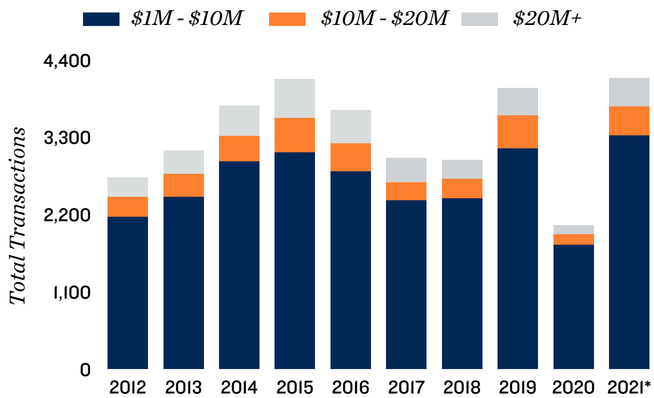
Select number of properties continue to be severely impaired. Hotels in major urban centers and frequent convention markets will see improved operations in 2022 but will remain the most troubled segment. Through September of this year hotels in core areas reported RevPAR values more than 25 percent below levels from two years prior, a steeper margin than for most other hotels. The problem is compounded in the country's largest gateway markets that typically cater to numerous international visitors, including New York and San Francisco. Both metros reported occupancy rates for the month of September that were 20 percentage points or more below the same period in 2019 and had the highest rate of temporary room closures. The return of certain health precautions in these metros may dissuade some visitation to the area until the pandemic notably improves. Overall, a prolonged drought in demand in many densely packed locales extends the road to recovery.

Occupancy Narrows Margin With 2019

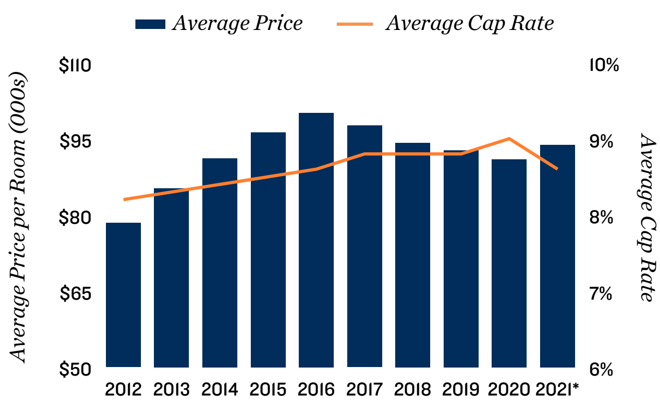


Sources: Marcus & Millichap Research Services; CoStar Group, Inc.

Investors Return in Force This Year



Recovery Drives Cap Rate Compression



** Through 3Q*

Sources: Marcus & Millichap Research Services; CoStar Group, Inc.; Real Capital Analytics

Investors Clear Sidelines as Operations Improve

After period of caution, buyers look to hotels again. Despite the lingering challenges facing the lodging sector, investors are showing no signs of backing off. Hotel transaction activity has surged this year, with more properties changing hands between April and September than in all of 2020. While ample capital was set aside at the onset of the health crisis, anticipating widespread discounting, actual distress has been comparatively limited. Competition for listings has instead lifted sale prices for assets. The average sale price for the 12-month period ended in the third quarter was $94,000 per room, more than 3 percent above the mean measure for 2020. The average cap rate over the past four-quarter span was 8.6 percent, a compression relative to the 9.0 percent yield recorded in 2020. Buyers are gravitating to markets where hotels outperformed this year or are well positioned for next year. This includes assets in California, Florida, Texas and North Carolina. As more hotels report positive operations, investor criteria will widen. Even in more challenged environments such as New York, the transaction pipeline is still greater than in recent pre-health crisis years as investors come off the sidelines. This behavior illustrates that while hotels across the country may follow more than one path forward in the coming months, the long-term outlook for the sector is overwhelmingly positive.

Top 20 Markets by RevPAR Recovery

Metro	Sept. 21 Occupancy	Change From 2019	Sept. 21 RevPAR	Change From 2019
Myrtle Beach, SC	61.2%	630	$91.61	57%
Sarasota, FL	55.5%	730	$74.57	50%
Daytona Beach, FL	50.1%	620	$61.37	50%
Mobile, AL	66.6%	890	$83.30	49%
Florida Keys*	66.4%	-400	$224.10	47%
Jackson, MS	66.3%	1,280	$61.34	42%
Fort Myers, FL	56.4%	720	$71.08	41%
Charleston, SC	65.2%	520	$104.18	29%
Portland, ME	82.3%	180	$167.81	28%
Savannah, GA	63.0%	390	$82.42	24%
Florida Panhandle	62.8%	-50	$93.49	23%
Norfolk-Virginia Beach, VA	63.2%	-30	$77.03	20%
Riverside-San Bern., CA	62.7%	-30	$82.77	20%
California Central Coast	72.2%	-400	$179.60	19%
Milwaukee, WI	61.8%	-670	$94.08	17%
Knoxville, TN	64.6%	440	$64.52	17%
Jacksonville, FL	62.5%	180	$74.54	16%
Fort Lauderdale, FL	56.0%	-460	$72.47	16%
Colorado Springs, CO	74.9%	-200	$124.00	16%
McAllen-Brownsville, TX	63.0%	140	$57.50	15%
United States	**61.6%**	**-550**	**$56.97**	**-7%**

** Due to impact of Hurricane Irma in Sept. 2019, values for Florida Keys are for the month of August*

Sources: Marcus & Millichap Research Services; CoStar Group, Inc.

Hospitality Division

Brian Hosey

First Vice President | National Director, Hospitality

Tel: (202) 536-3700 | brian.hosey@marcusmillichap.com

Prepared and edited by:

Cody Young

Senior Market Analyst, Editor | Research Services

For information on national hospitality trends, contact:

John Chang

Senior Vice President | National Director, Research Services

Tel: (602) 707-9700

john.chang@marcusmillichap.com

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