Hospitality Investor

Hospitality Investor Sentiment Index

Results for Q2 2023

According to our proprietary Hospitality Investor Sentiment Index, in Q2 2023, the sentiment of our equity investors has moved to **INCREASED OPTIMISM** about the hospitality sector.

Many of the trends in the survey for Q2 2023 would suggest that we are on a positive trajectory towards a higher level of hotel operational profitability and (perhaps) liquidity. There has been a significant upturn in the sentiment regarding consumer demand, regarding both the corporate and leisure segments, and the confidence in profit growth has shown some signs of recovery, albeit from a low base. Perhaps unsurprisingly, this is resulting in greater investor interest in full-service hotel stock.

As in previous quarters, the limited availability of stock and pricing remain an issue for some buyers and with above-average inflation underpinning high interest rates in the short term, the challenges around debt are going to leave some investors struggling to make acquisitions stack up. Nonetheless, the Q2 survey results suggest an increase in competition to acquire stock, and with formal valuations showing some softening more generally, perhaps we are edging closer to an alignment of buyer and seller expectations which will, in turn, result in greater deal flow.

Whilst only recording a marginal increase of 3.7 pts from last quarter, at 51.9, the overall index score has now tipped into positive territory, with a score of +50 signaling an increase in confidence.

The table presents the key indicators from Q2 2023. An index score above 50 indicates an increase and below 50 indicates a decrease.

Positive Key Indicators	Index Score Q2 2023 v Q1 2023		Negative Key Indicators	Index Score Q2 2023 v Q1 2023	
Your confidence in leisure accommodation demand growth (next 12 months)	58.6	+12.0pts	Your unallocated capital to invest in hospitality (dry powder)	62.9	-3.1pts
Your confidence in total profit growth (next 12-months)	41.4	+17.6pts	The price of hospitality investment opportunities	44.3	+6.8pts
The price of debt	84.3	-8.9pts	The competition to acquire hospitality investment opportunities	61.4	+14.8pts
Your use of leverage	30.0	-12.0pts	The time to close a deal	77.1	+12.4pts

Methodology

The Hospitality Investor Sentiment Index gauges the sentiment of equity investors active in the hospitality sector, by polling their opinions on a quarterly basis across consumer demand and operational performance, the demand for, and availability of stock, appetite for risk and the pricing of investment opportunities.

The key elements to the methodology are:

1. A questionnaire answered by senior decision makers, that are members of Questex's Investor Council, representing the leading investment firms.
2. Responses are based on whether confidence levels are 'higher', 'the same' or 'lower' than the previous quarter based on a particular outcome.
3. A diffusion index method is used to arrive at the index score. The resulting index values are bound between 0 (all investors respond lower) and 100 (all investors respond higher), with a theoretical no-change mark at 50 (all investors respond 'the same' or equal proportions respond 'higher' as do for 'lower'). Values above 50.0 indicate an increase and below 50.0 indicate a decrease. The distance from the 50 no-change mark signals the implied rate of change in the variable, the further from 50.0 the greater the rate of change.

Example: Take a movement from 60.0 in Q1 to 55.0 in Q2. Although the level of the index has fallen, it has nonetheless posted above 50.0 in both quarters. The correct interpretation is that the sentiment increased in both Q1 and Q2, but that the rate of increase was slower in Q2 compared to Q1.

4. The overall Questex Hospitality Investor Sentiment Score is based on a weighted average of the quarterly results.

Panel Composition: Investor Council

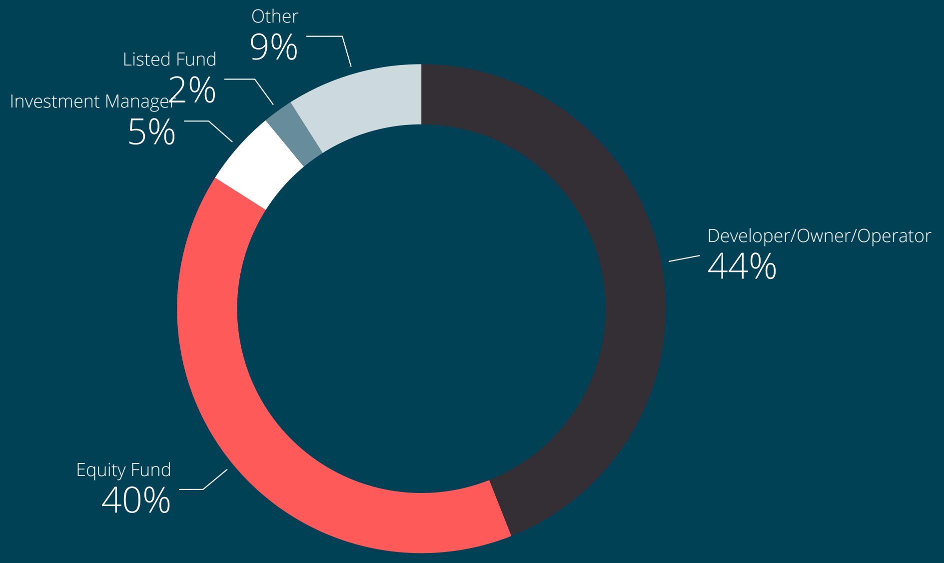
Our respondents are senior decision makers representing the leading investment firms across the world. The diverse representation from an investment and geographical perspective is reflective of the ownership/investment structure of the market and supports the validity of the results.

For this survey, we have seen engagement from large institutional investors and diversified real estate players, as the professionalisation of the sector continues, and does not appear to have been derailed by the current headwinds.

We have seen an extraordinary level of engagement from our global audience for this second survey of 2023, with an ongoing robust response rate as investors seek information and direction. For the first time since 2019, there are signs that the market could be readying itself for a surge of activity.

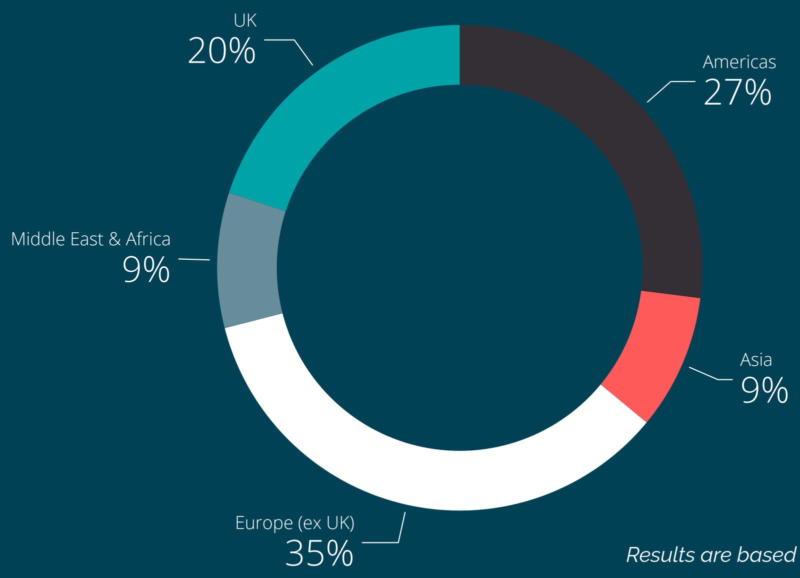
This quarter, the survey saw a high level of engagement from investors in the Americas (20%), as well as Europe (ex UK) (57%), demonstrating the international, cross-border nature of hospitality investment. Notably, the 9% of the sample representing Asian capital is perhaps indicative of increasingly inquisitive Asian outbound capital following a slow return post-pandemic.

What best descibes your organisation?



Results are based on Q1 from the survey

From where does your capital predominantly originate?



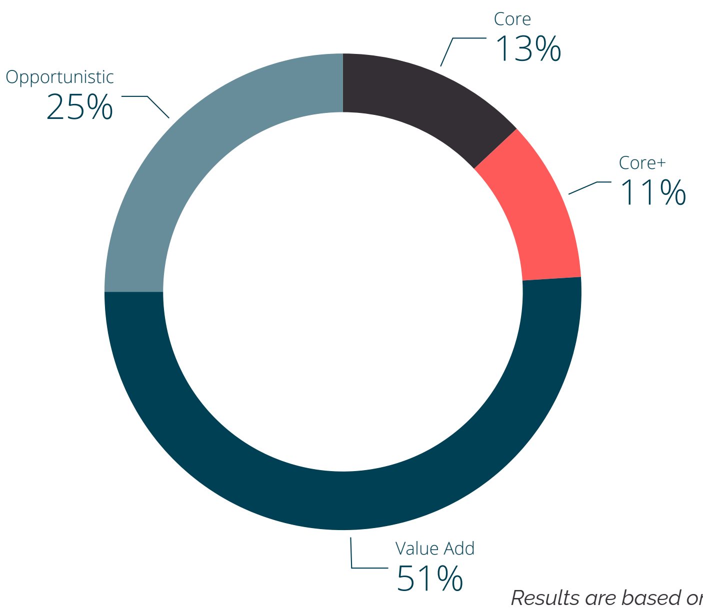
Results are based on Q2 from the survey

Historically, the hospitality industry was a sector which only appealed to owner-operators, hotel specific investors and opportunistic funds. Core participants, which in Q2 2023 comprised 15% of our panel, are becoming more prevalent as it continues to become more transparent, liquid and therefore appealing relative to other more traditional property types. For many, hospitality remains an important value-add component of a diversified real estate portfolio.

Additionally, it's seen as a sector with asset management potential, where investors can be rewarded and add value with almost immediate results – a benefit of nightly rent reviews. The range of different operating structures and markets also means that it appeals to a wide range of investors with different strategies and return requirements.

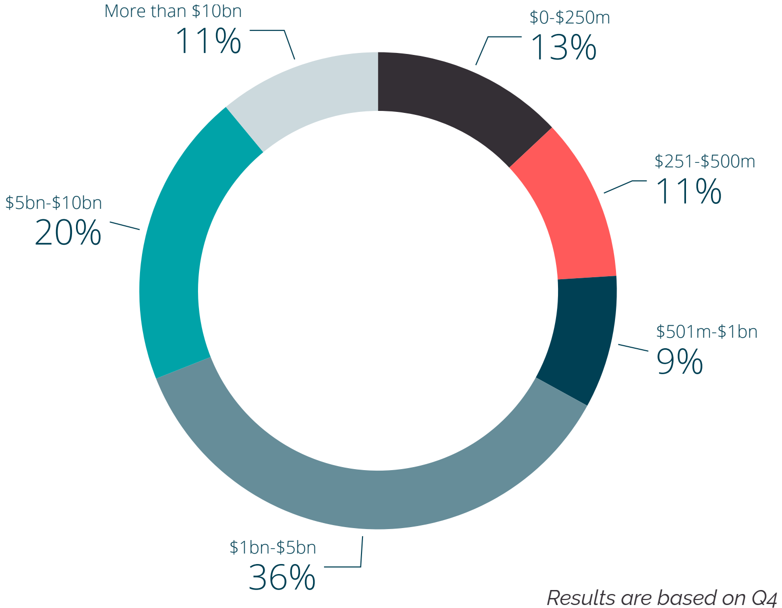
There is a broad representation of investor size on our panel, with 49% of investors having allocated over $1bn in Real Estate and 23% more than $10bn. The total amount of capital under management by our respondents is in excess of €402.9bn (MSCI).

What best descibes your investment strategy?



Results are based on Q3 from the survey

What is the approximate value of your total Real Estate assets under management in USD$?



Results are based on Q4 from the survey

Consumer Demand

Further to four consecutive periods of uncertainty, the view of our Investor Council for Q2 2023 is that consumer demand, in general, is on the way up. With growth anticipated by the majority of respondents for both the corporate and leisure segments in the next 12 months.

The position of our investor audience on corporate demand continues to improve, increasing from an index low of 40.5 in Q4 2022 to hit 61.4 in Q2 2023. And this is supported by the views of some operators who are seeing greater contracted corporate demand, in addition to meetings and events. However, the recovery in demand is unlikely to impact all hospitality businesses equally, with many business travellers travelling less frequently but staying at their destination for a longer duration – extended stay properties, for example, appear well-positioned to capitalise on this trend.

"While the overall quantity of business trips has dropped off significantly since Covid, today's business travel is about fewer, but longer and more purposeful, trips,"

Saskia Gentil, Accor's SVP Sales for Europe & North Africa.

But it is in leisure demand where there has been the most significant shift in opinion, with the index score increasing by 12.0pts to 58.6 in Q2 2023 as operators regain confidence in the market, potentially led by initial visibility on summer bookings and an expectation that we are perhaps through the worst in terms of the impact of inflation on consumer spending.

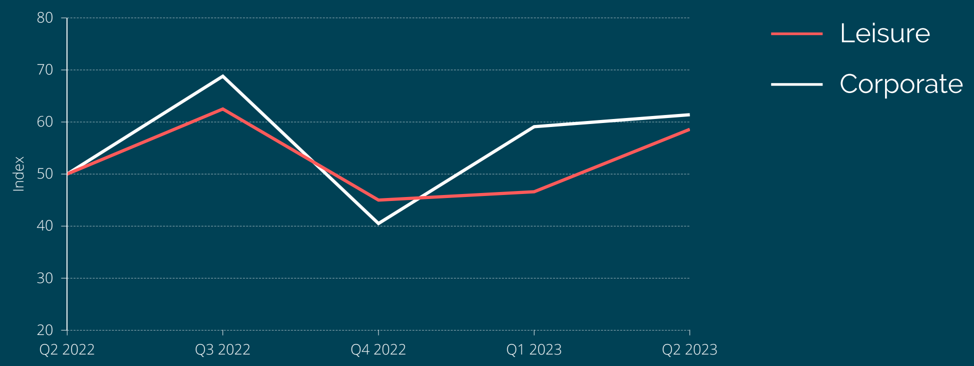
The index score this quarter is only marginally behind the score in Q3 2022 (62.5) when the market was at it's most buoyant on the back of a strong post-pandemic rally.

"Booking momentum remains encouraging, and the travel trends and strong demand for the Easter holidays are a healthy signal. We continue to anticipate capacity to be close to pre-pandemic levels and expect a good summer this year,"

Sebastian Ebel, CEO, TUI Group.

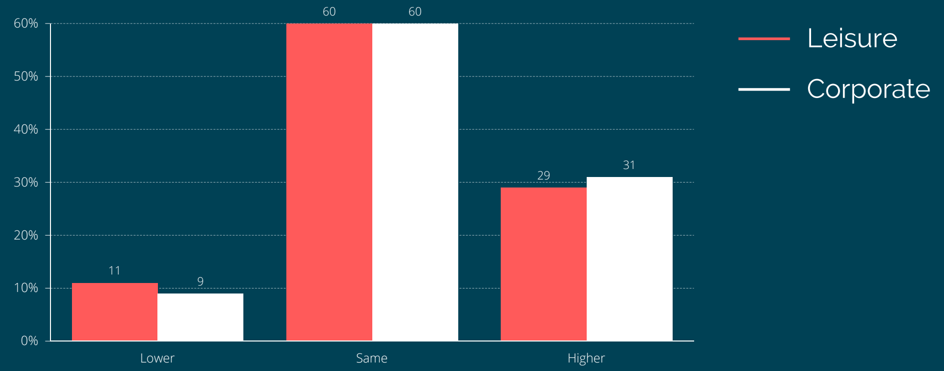
Despite the IMF stating that the medium to long-term growth outlook for the global economy is the weakest in 30 years, our Investor audience remains resolute that hotel demand will broadly buck the trend, with 100% of respondents expecting long-term accommodation demand growth to either remain the same or increase, with an index score of 71.4.

Your confidence in demand growth (next 12-months)



Results are based on Q5 & 6 from the survey

Q2 2023: Your confidence in demand growth (next 12-months) - Q-o-Q



Results are based on Q5 & 6 from the survey

The positive outlook on consumer demand in Q2 2023 is undoubtedly contributing to our investor audience projecting a continued recovery in revenue growth over the next 12 months, with robust demand leading to an increase in overall in-house spend.

In addition, due to the envisaged recovery in both corporate and leisure demand, hotels should start to see a boost across all revenue centres (Food & Beverage, Meetings & Events, Leisure), not just bedrooms.

The investors with capital originating in Asia and Europe (excl. UK) are the most positive about the prospects for revenue growth with 100% of respondents anticipating growth to remain the same or increase. In contrast, 25% of respondents from the UK anticipate growth to be lower, perhaps influenced by the UK's relatively weak economic outlook.

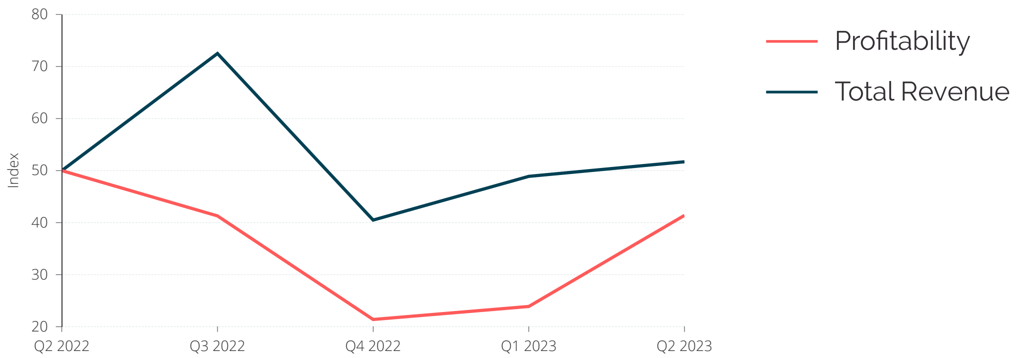
The anticipated increase in revenue has also helped to drive a 17.6pts increase quarter on quarter in the index score for profit growth over the next 12 months, which grew to 41.1. Whilst this is a marked improvement, at below 50, this index score still implies continued pressure on profitability, albeit to a lesser extent than previously expected.

The more positive outlook on hotel profitability is potentially due to cost levels stabilising, which is in part due to a drop in energy costs, which for many means a direct reduction in utilities, but also a subsequent fall in costs throughout the broader supply chain.

Furthermore, the outlook on profitability looks more positive as hotels have discovered (or accepted) that their operation can survive with a leaner staffing structure.

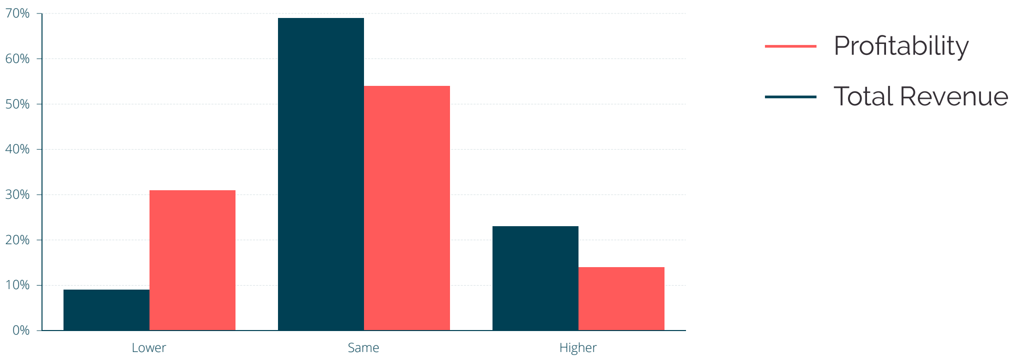
When splitting the audience, there is a stark contrast in opinions: Core and Core+ investors remain muted on hotel profits, with 100% of respondents suggesting that growth will either remain the same or be lower in the next 12 months. This is compared to 60% of Opportunistic investors, who are forecasting profit levels to continue to grow at the same level or stronger.

Your confidence in performance growth (next 12 months)



Results are based on Q9 & 10 from the survey

Q2 2023: Your confidence in performance growth (next 12 months) - Q-o-Q



Results are based on Q9 & 10 from the survey

Investment Focus

For our investor audience, the strongest investment focus remains on Urban markets, with the index score in this category at a robust 61.4 in Q2 2023.

Although there has been a slight increase in the index score for Resort markets, at 48.6, it suggests that the focus on this segment continues to wane following a high score of 59.5 in Q4 2022. This is likely due to the Leisure Resort market coming from a strong post-pandemic base, whereas the urban and corporate market arguably has headroom for growth following a more protracted post-pandemic recovery.

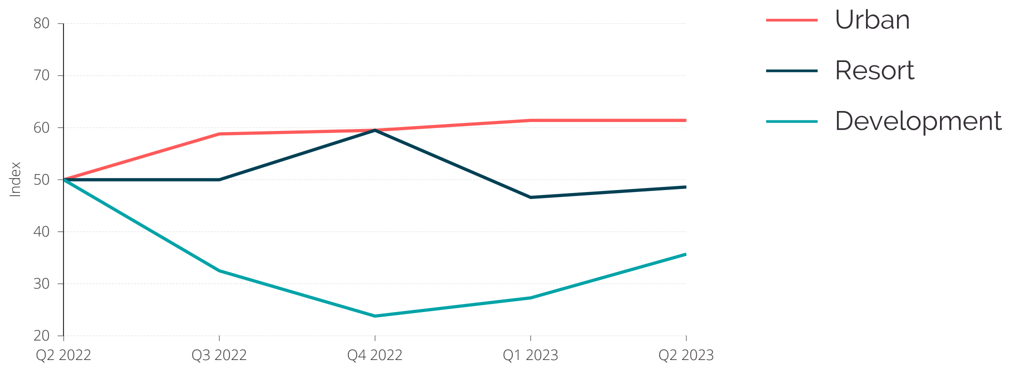
Amidst lingering macro volatility, acquisitions in urban locations in Europe remain particularly sought after, as an asset in downtown Paris or Amsterdam will also retain its prime real estate profile and hence their appeal to long-term, generational investors, according to Patrick Saade, senior managing director of JLL's EMEA hotels and hospitality division.

Development has made a significant recovery from its low of 23.8 in Q4 2022; albeit an index score of 35.7 in Q2 2023 suggests that development is still lower on the priority list for our Investor Council than acquisitions.

And whilst construction costs appear to be stabilising and the gap for new hotel stock in many markets is increasingly apparent, the challenges regarding development viability and securing development finance remain significant.

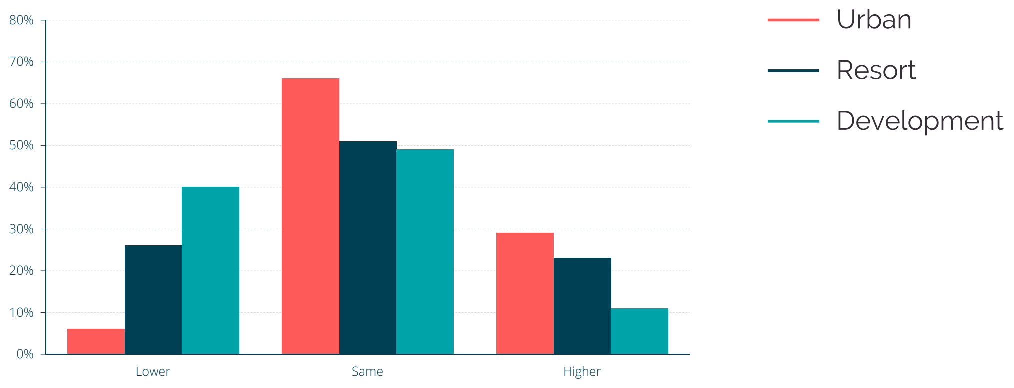
That said, there are examples of hospitality development projects moving forward, under public and private sector partnerships, or featuring within mixed-use schemes, where further value can be attributed in terms of broader economic impact, regenerative benefits or increased amenity provision, for example.

Your investment focus (next 12 months)



Results are based on Q11, 12 & 13 from the survey

Q2 2023: Your investment focus (next 12 months) - Q-o-Q



Results are based on Q11, 12 & 13 from the survey

Investment Demand and Supply

As consumer markets continue to recover and the prospects on revenue growth remain positive, there has been a shift back towards a focus on investment in full-service hotels.

For our Investor Council, the focus of investment in full-service hotels hit a high in Q2 2023, at an index score of 57.1, further to a 12.8pts increase on Q1 2023.

For full-service hotels, multiple revenue centres present a range of opportunities to capture customer spend and generate ancillary revenues. This is compared to a limited-service operation, which can be up to 95% rooms driven.

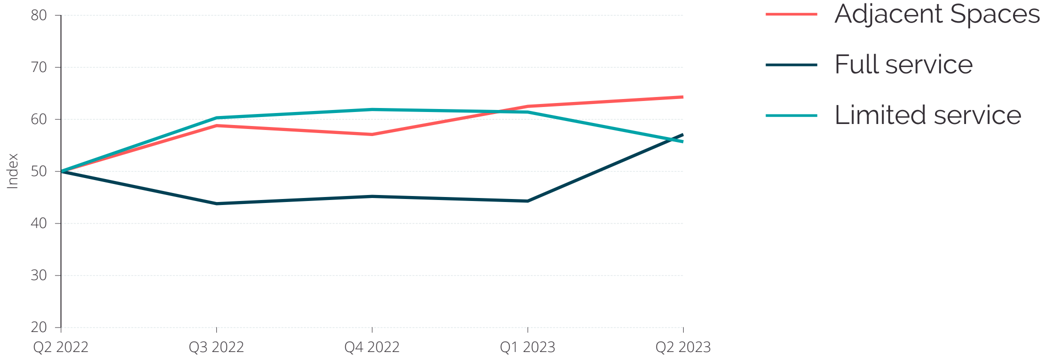
This has been echoed in the index score for the focus of our Investor Council on limited-service hotels, which fell by 5.6pts to 55.7. This is potentially due to post-pandemic hotel rates continuing to hold strong and the anticipated flight to value not playing out entirely as envisaged.

100% of Core and Core+ investors are anticipating an increase in their focus on full-service hotels in the next 12 months, having historically favoured leaner operating models, compared to 92% Opportunistic and 88% Value Add.

The interest of our investor audience in alternative accommodation types remains resolute at an index score of 64.3 in Q2 2023. Which is unsurprising as serviced apartment and hotel concepts continue to perform well, but may also be symptomatic of a shortage of current opportunities to invest in traditional hotel stock.

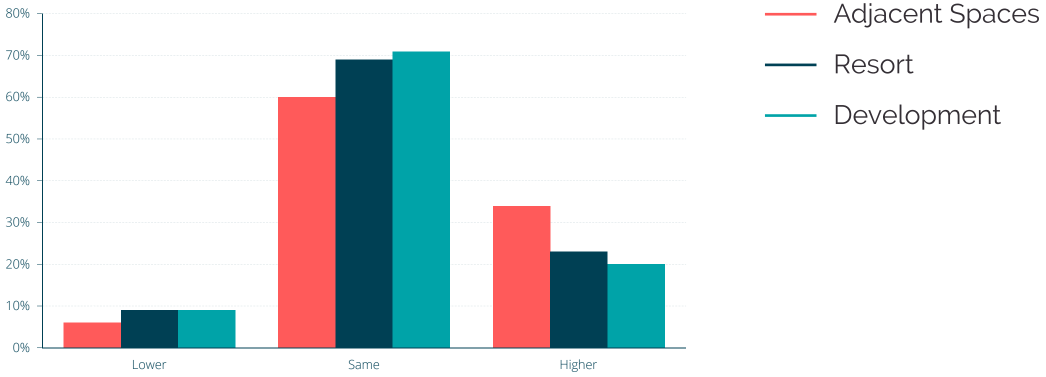
The adjacent spaces segment will have its own dedicated event at IHIF 2023, exploring the evolution of alternative hospitality real estate assets including hostels, co-living, co-working, student accommodation, serviced apartments and more.

Your investment focus (next 12 months)



Results are based on Q14, 15 & 16 from the survey

Q2 2023: Your investment focus (next 12 months) - Q-o-Q



Results are based on Q14, 15 & 16 from the survey

The Q2 2023 survey also saw a further increase in the expected hospitality returns of our Investor Council. This has been one measure which has consistently grown since the survey relaunched, increasing from 56.3 in Q3 2022 to 64.3 this period.

The increasingly positive outlook on hospitality returns may be related to a more positive outlook on revenue generation and profitability, but may also be due to expectations of greater liquidity in the market, a growing pool of active buyers and the potential for bidding up on pricing.

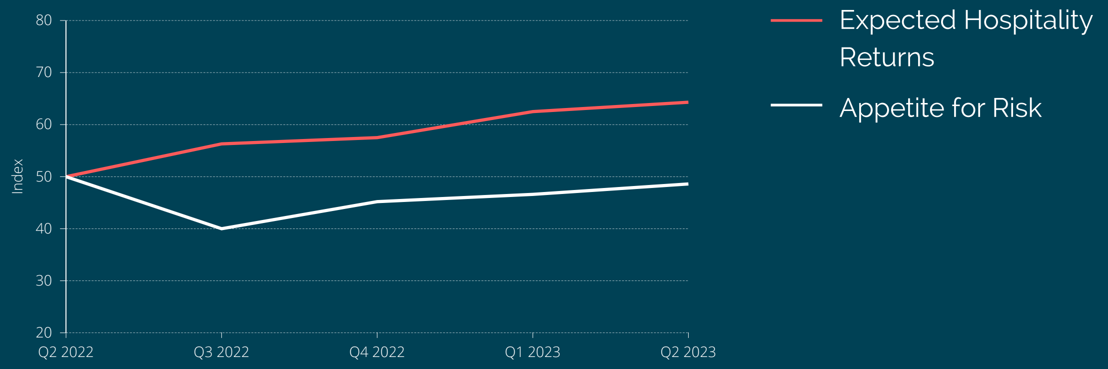
Our investor audience also expressed a greater willingness to take on further risk, with this measure also increasing by 2.0pts to an index score of 48.6. Albeit this is potentially more 'measured' risk as we move towards a period of greater economic and political stability.

The use of leverage has been one measure which has declined significantly this quarter, dropping by 12.0pts to just 30.0.

The move away from a reliance on lending does not come as a shock as the Bayes European Commercial Real Estate Lending Report revealed that borrowers in Europe, on commercial real estate more generally, are now paying up to 6% all-in interest for loans on prime European properties, compared to just 2-3% a year ago. Opportunistic or repositioning assets are priced 60-100 bpd wider.

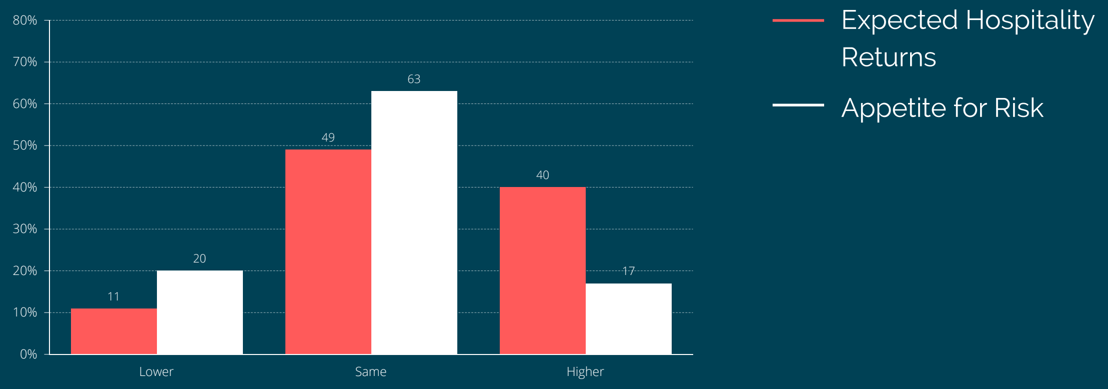
For Neil Kirk, COO at L+R Hotels, all equity transactions are the way to go, *"I know a lot of people will say they can buy all equity, but because of the nature of their IRR [initial rate of return] targets, they will always look for financing in one form or another before acquiring. We don't need to do that and it's made pricing more sensible."*

Acquisition and Asset Management Strategy (next 12 months)



Results are based on Q17 & 18 from the survey

Q2 2023: Acquisition and Asset Management Strategy (next 12 months) - Q-o-Q



Results are based on Q17 & 18 from the survey

Acquisition and Asset Management Strategy

Whilst there has been a slight decline in the availability of unallocated capital to invest in the hospitality sector, down by 3.1pts to 62.9, the sentiment is still positive and investor demand remains significant.

This appetite for investment has been echoed in Hospitality Investor's coverage of late, with Goldman Sachs reportedly investing between €150 million to €200 million in three coastal resorts in Greece, and Blackstone gearing up with the announcement of the final close of its Blackstone Real Estate Partners X fund with $30.4 billion of total capital commitments, which is the largest real estate or private equity drawdown fund ever raised.

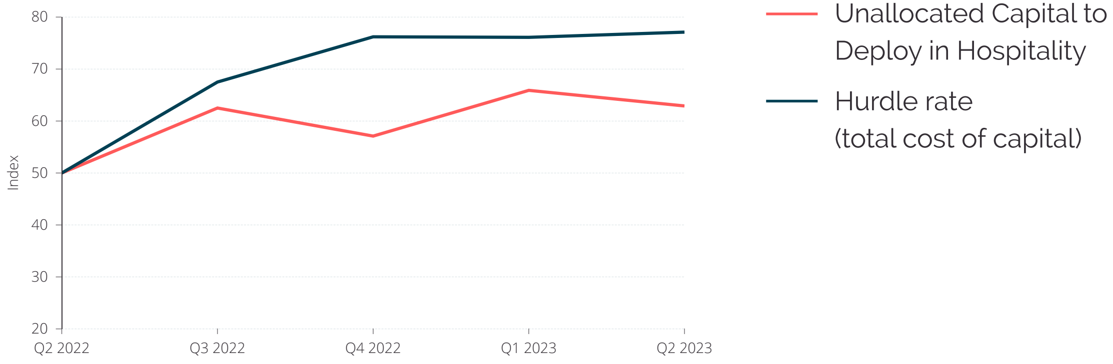
This is a very positive sign for the hospitality industry as where Blackstone leads others follow and having highlighted a potential under exposure to the hospitality space at the Hunter Hotel Investment Conference, Tyler Henritze, senior managing director at Blackstone, stated that they wished their hotel portfolio to be bigger than the pre-Covid level of 12%.

For our Investor Council, the anticipated hold period has further increased, to an index score of 55.7, suggesting that investment strategies and asset management plans are perhaps going to take longer to execute and to yield the required returns.

For Brien Giuntini, partner at Cushman & Wakefield EMEA, the principal of starting to look at a longer term strategy is applicable across all aspects of the operation, including refinancing, as he suggests, "it may be worth reimagining what your portfolio looks like in five years. There are going to be assets that are worse performers, better performers and those that are mission critical assets for the portfolio. The type of lending required today to support each asset within your portfolio will dictate which will be saved and which won't."

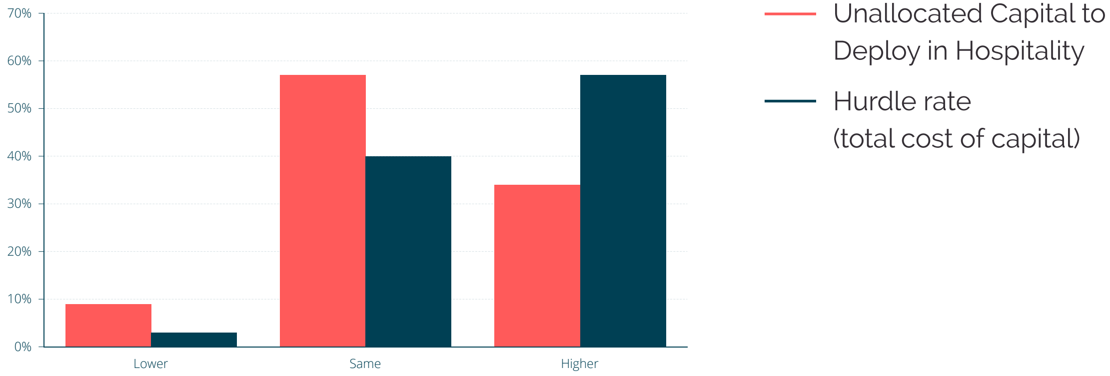
As interest rates continue to creep, the hurdle rate index score for our investor audience has continued to increase to 77.1 in Q2 2023, which is 9.6pts above the response in Q3 2022.

Acquisition Strategy (next 12 months)



Results are based on Q20 & 27 from the survey

Q2 2023: Acquisition Strategy (next 12 months) - Q-o-Q



Results are based on Q20 & 27 from the survey

Acquisition and Asset Management Strategy

According to our investor audience, the appetite to commence a material asset management strategy remained strong at an index score of 65.7 in Q2 2023.

For hotel investors looking to increase the value of their hotel for a potential exit or even priming their asset for a return to a competitive position, the most effective way to achieve this remains commencing an asset management strategy.

In addition, for those hotels which were cash starved throughout the pandemic, now could be the right time to consider investment to, again, elevate the competitive profile of an asset and capitalise on the next phase of economic and overnight demand growth.

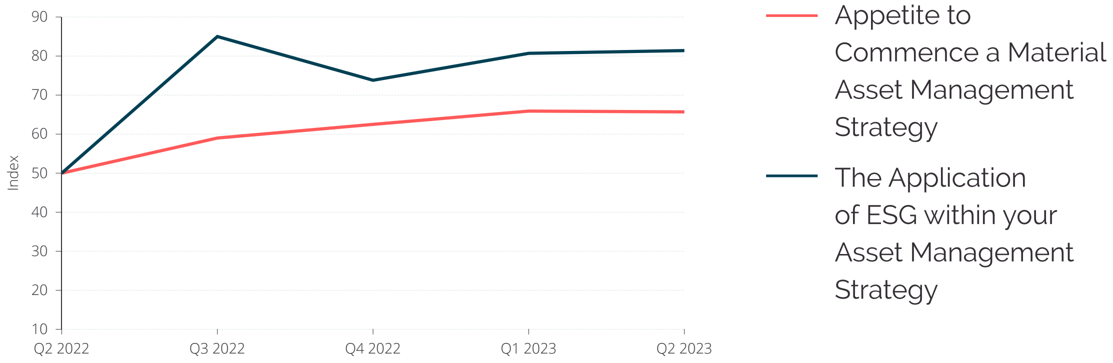
However, owners and operators face a difficult decision of whether to invest to cover a basic reconditioning of product quality or whether now is the time to make the transition to a property which is closer to achieving NZC50 (Net Zero Carbon Emission by 2050) status.

With pressure now coming from regulators as well as consumers, it is no surprise that the application of ESG within an asset management strategy is a hot topic for our Investor Council, with an index score of 81.4 in Q2 2023.

A recent survey, conducted by JLL and the Energy and Environment Alliance (EAA), revealed that the topic of ESG by hotel investors has stepped up and is no longer an after-thought. Yet, according to the survey, only 36% of owners have set aside a sustainability reserve (or transition capex).

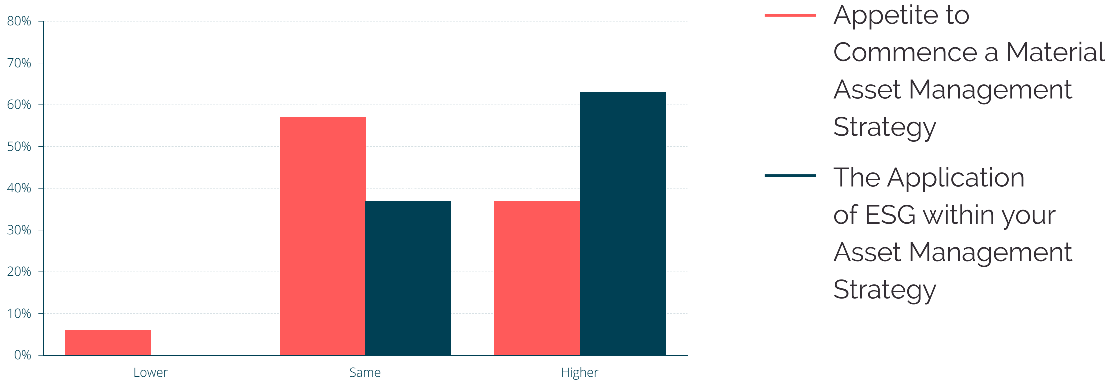
ESG is now a consideration across the entire operation and one key element which should not be overlooked is finance, with citizenM recently securing a dual currency €243.3 million and £201.7 million sustainability linked loan facilitated by HSBC UK and HSBC Continental Europe, ABN AMRO Bank and Aareal Bank.

Asset Management Strategy (next 12 months)



Results are based on Q24 & 25 from the survey

Q2 2023: Asset Management Strategy (next 12 months) - Q-o-Q



Results are based on Q24 & 25 from the survey

Pricing

The results of the Q2 2023 survey saw the availability of investable hospitality stock once again push back up to an index score of 54.3, from 50.0 in Q1 2023. Suggesting greater optimism that an increase in deal flow is not far away.

It is possible that the tap is about to turn on any time now, as a result of hotel owners being faced with potentially unpalatable refinance deals, properties which were pulled from sale pre-pandemic now making their way back to market and a raft of supply waiting behind closed doors for the right time to go to market.

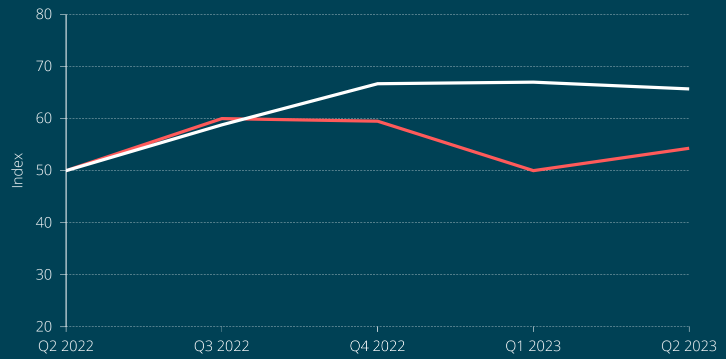
As **Joe Pettigrew, CCO Hotel Asset Management at Starwood Capital** put it, *"When you try to take the yield of your investment, versus the cost of debt, and then also the cost of construction, and the refurbishment and PIP, and all that stuff, a lot of these numbers are not really translating at least for somebody like us to have been making big deals yet".* Speaking with those on the dealmaking front, he said that "everybody's watching this space very carefully" and that the "tap is about to turn on" and when that happens there's going to be a lot more activity in the market.

The focus on hospitality investments (relative to other asset classes/property sectors) has waned slightly in Q2 2023, falling by 1.3pts to 65.7, potentially due to the strong performance of property types, such as build-to-rent and student accommodation. Albeit the sentiment remains positive and well ahead of the index score of 58.8 in Q3 2022.

Interestingly, the Core and Core+ investors remain resolute on the hospitality industry, with 100% of respondents in this category stating that their focus is set to remain the same or increase. Having been slower to engage with hospitality as an asset class, they seemingly now believe in the ability of hospitality to deliver returns.

A proportion of Value Add investors (15%) however, are starting to think about other investment classes, stating that their focus on hospitality may be lower going forward, perhaps becoming impatient by a lack of potentially high-yielding opportunities.

Investment Supply and Demand (next 12 months)

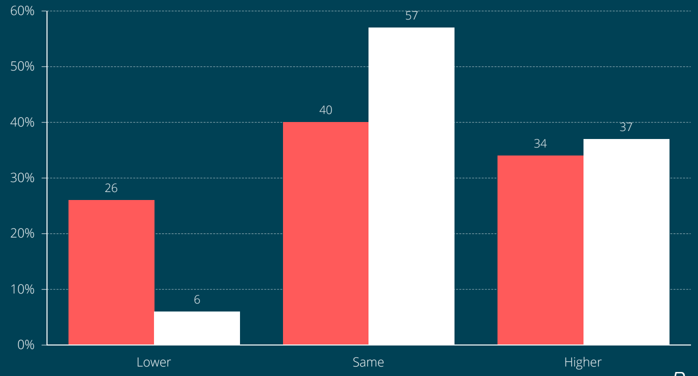


Availability of Investable Hospitality Stock

Focus on Hospitality Investment (relative to other asset classes/ property sectors)

Results are based on Q19 & 21 from the survey

Q2 2023: Investment Supply and Demand (next 12 months) - Q-o-Q



Availability of Investable Hospitality Stock

Focus on Hospitality Investment (relative to other asset classes/ property sectors)

Results are based on Q19 & 21 from the survey

Pricing

According to our survey, the competition to acquire hospitality investment opportunities has increased by a significant 14.8pts this quarter, to an index score of 61.4. Many investors, previously on the sidelines amidst macro-economic volatility, have become active once again.

Unsurprisingly, with the increased cost of capital, the index score relating to the price of hospitality opportunities remains sub 50.0. However, it has been edging up over the past two quarters, driven partly by the increased demand to acquire, and indicating a possible narrowing of the bid-ask spread.

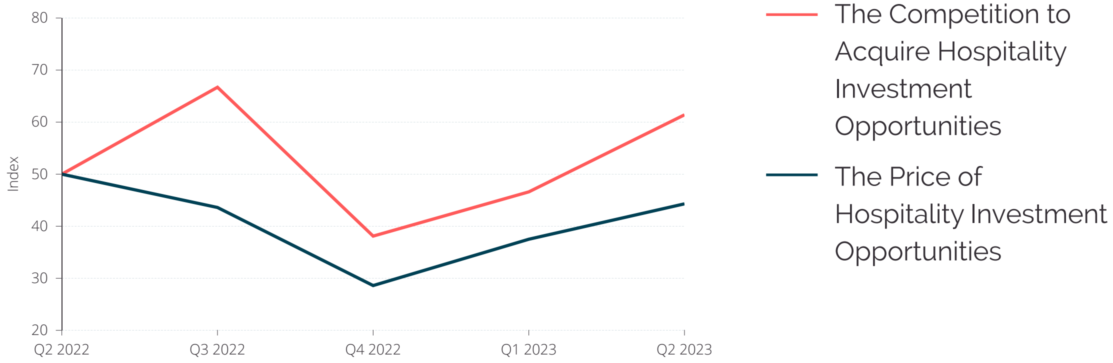
If the price of hospitality opportunities is expected to increase, then one would expect the bid-ask spread to narrow and an increase in deal flow to follow.

The trends continue to point towards increased transaction activity and a more positive macroeconomic environment, however, in the next quarter with further potential rate rises in the balance, the investors likely to be best positioned to compete are those who are eyeing all equity deals.

For those investors who will rely on debt, in the short term at least, it is going to be challenging for them to realistically compete for acquisitions, due to above-average inflation driving high interest rates. Although products such as mezzanine finance may be a lifeline, it comes at a higher cost and understanding those implications is crucial, particularly the difficulty of eventually refinancing or removing it from the capital structure.

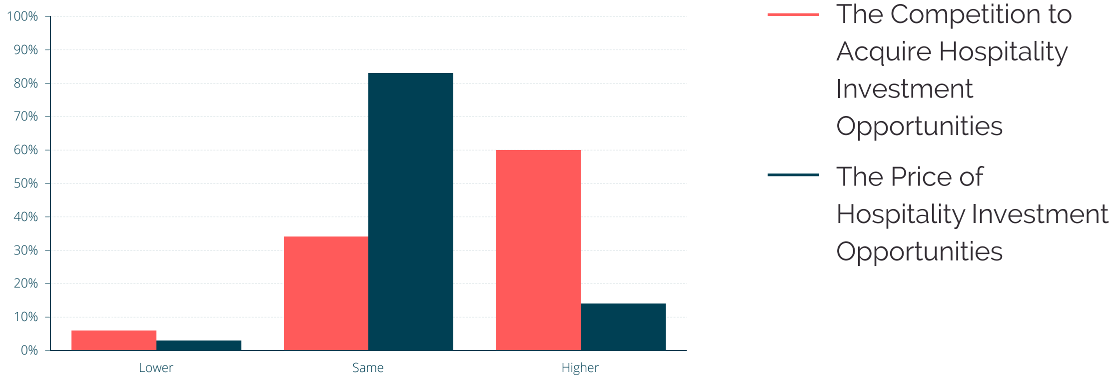
That said, at an overall score of 51.9, the index has moved into positive territory for the first time since the survey relaunched and we will be excited to see the responses to the Q3 2023 survey and the potential increase in activity in the transaction market.

Investment Pricing (next 12 months)



Results are based on Q22 & 30 from the survey

Q2 2023: Investment Pricing (next 12 months) - Q-o-Q



Results are based on Q22 & 30 from the survey

Appendix: Table of Results

The following table presents the full index results for all survey questions.

Index Score	Q4 2022	Q1 2023	Q2 2023
Your confidence in leisure accommodation demand growth (next 12-months)	45.0	46.6	58.6
Your confidence in corporate accommodation demand growth (next 12-months)	40.5	59.1	61.4
Your confidence in long-term total accommodation demand growth (through the cycle)	64.3	67.0	71.4
Your confidence in total revenue growth (next 12-months)	40.5	48.9	57.1
Your confidence in profitability growth (next 12-months)	21.4	23.9	41.4
Your investment focus on urban markets	59.5	61.4	61.4
Your investment focus on resort markets	59.5	46.6	48.6
Your investment focus on development	23.8	27.3	35.7
Your investment focus on alternative accommodation types (extended-stay, hostels, co-living, etc.)	57.1	62.5	64.3
Your investment focus on full-service hotels	45.2	44.3	57.1
Your investment focus on limited-service hotels	61.9	61.4	55.7
Your expected hospitality investment returns	57.5	62.5	64.3
Your appetite for risk	45.2	46.6	48.6
Your focus on hospitality investment (relative to other asset classes/property sectors)	66.7	67.0	65.7
Your unallocated capital to invest in hospitality (dry powder)	57.1	65.9	62.9
The availability of investable hospitality stock	59.5	50.0	54.3

Index Score	Q4 2022	Q1 2023	Q2 2023
The competition to acquire hospitality investment opportunities	38.1	46.6	61.4
The time to close a deal	73.8	64.8	77.1
Your appetite to commence a material asset management strategy	62.5	65.9	65.7
The application of ESG within your asset management strategy	73.8	80.7	81.4
Your anticipated hold period	54.8	53.4	55.7
Your hurdle rate (total costs of capital)	76.2	76.1	77.1
Your use of leverage	33.3	42.0	30.0
The price of debt (margin)	92.9	93.2	84.3
The price of hospitality investment opportunities	28.6	37.5	44.3
Your requirement for brokerage services	50.0	42.0	48.6
Your requirement for valuation/advisory services	47.6	55.7	50.0
Your requirement for legal services	50.0	53.4	52.9
Your requirement for a new brand/operating partner	61.9	53.4	55.7
Your requirement for architecture/design services	45.0	45.5	54.3
Your requirement for new technology	73.8	70.5	64.3
Questex Investor Intention Index Overall Score (weighted)	**44.3**	**48.2**	**51.9**

Contacts

Alexi Khajavi

President, Hospitality & Travel
Questex

akhajavi@questex.com

Joe Stather

Market Leader
Questex Operational Real Estate

jstather@questex.com

Patrick Whyte

Editor in Chief
Hospitality Investor

pwhyte@questex.com

Julie Rey-Gore

Content Director
Questex Operational Real Estate

jreygore@questex.com

Leah Braithwaite

Marketing Director
Questex Operational Real Estate

lbraithwaite@questex.com