Hospitality Research State Report

California

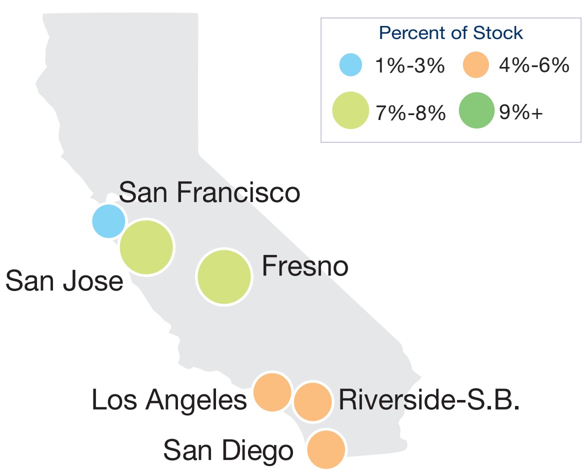
Second Half 2018

Supply Pressures, Wildfires Weigh On Regional Occupancy

Supply pressures drive down occupancy in several markets. Annual occupancy remained flat in California during the year ending in June as supply began to weigh on the rate in many of the state's largest markets. Los Angeles and San Francisco were particularly affected, with occupancy falling more than 100 basis points in each market during that same time. Nearly 3,600 rooms opened in Los Angeles during the past 12 months while more than 1,100 were placed into service in San Francisco. The trend will likely continue as a significant number of rooms are underway and in the planning pipeline in both metros. In San Francisco, the reopening of the convention center will likely minimize a further impact on vacancy as the closure of the space limited the number of events in the city.

Wildfires lure travelers away from parts of California. A number of wildfires throughout California have affected visitation to the state. It is estimated that 11 percent of travelers canceled their trips to California due to the wildfires, resulting in a $20 million loss in the tourism industry during July of this year. To help drive tourism back to the West Coast, officials in California are teaming up with those in nearby states also affected by the fires to reassure travelers. If successful, the campaigns could benefit occupancy improvement.

Under Construction % Of Existing Rooms



Sources: Marcus & Millichap Research Services; STR, Inc.

Hospitality 2018 Outlook

10 basis point increase in occupancy

Occupancy: Occupancy in California will tick up 10 basis points in 2018 to 75.4 percent. Supply pressures are limiting further improvement throughout the state.

3.2% increase in ADR

ADR: The average daily rate climbs 3.3 percent this year to $166.46, following a 2.2 percent increase registered in 2017.

3.4% increase in RevPAR

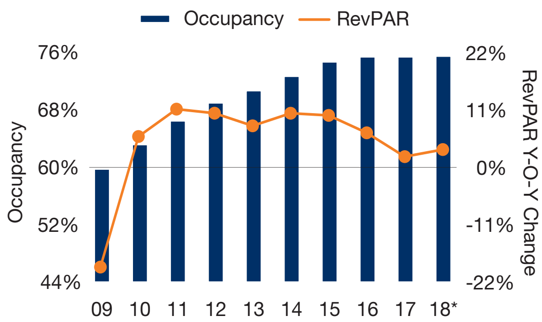
RevPAR: The increase in ADR combined with an uptick in vacancy will lift RevPAR up 3.4 percent to $125.99 by year end. In the prior year, RevPAR rose 2.1 percent.

State Highlights

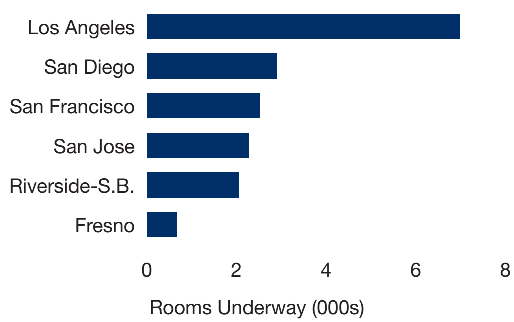
- San Francisco's Moscone Center has been under renovation since 2015 and the closure of both Moscone North and South earlier this year limited the number of larger events in the city. Once it is reopened, the center will have the capacity to host roughly a dozen more conventions, potentially generating more room demand in area hotels.
- Proposed regulations on short-term rentals within Los Angeles could bode well for hotels. The ordinance would limit the number of days an individual could rent their home to 120 days a year and prevents residents from renting out a home or apartment that is not their primary residence. This would prevent individuals with vacation homes from using home-sharing services and reduce the use of apartments as short-term rentals.
- Strong office-using job growth will likely drive room demand from business travelers in San Diego. This sector posted a 3.1 percent increase in staffs during the past 12 months.

Marcus & Millichap

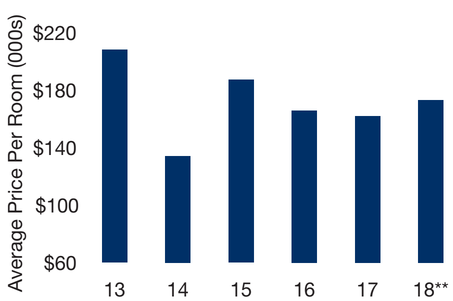
Annual Occupancy & RevPAR



Rooms Underway as of June 2018



Hotel Sales



* Forecast
** Trailing 12 months through 2Q
Sources: Marcus & Millichap Research Services; STR, Inc.

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Occupancy Trends

- Midyear occupancy ticked up 10 basis points in California from the same time period last year. On an annual basis, occupancy stayed flat during the year ending in June at 75.4 percent. In the previous annual period, occupancy rose 40 basis points.
- In San Diego, record tourism continues to sustain room demand in the metro with visitation reaching a record quarterly high in the first three months of 2018. Annual occupancy in San Diego rose 40 basis points during the past four quarters to 78 percent.
- San Francisco maintains the highest annual occupancy rate among the major metros in California at 82.4 percent in June, despite a 110-basis-point decrease year over year. In Los Angeles, occupancy fell 120 basis points amid elevated supply pressures during this time to 79.5 percent. Anaheim also posted an occupancy decline, with the rate falling 60 basis points during the past four quarters to 77.6 percent.

Revenue Trends

- Revenue metrics accelerated at a faster clip during the past 12 months ending in the second quarter than they did the prior year. The annual average daily rate in the region climbed 3.1 percent to $164.11 during this time while RevPAR edged up 3.0 percent to $124.05.
- ADR in Anaheim, Los Angeles and San Francisco rose more than 3 percent during the last four quarters. Anaheim posted the largest growth, with ADR rising 3.4 percent. RevPAR in the metro rose 2.5 percent during this same time. ADR and RevPAR in Los Angeles rose 3.1 percent and 1.5 percent, respectively. The average daily rate in San Francisco rose 3.2 percent while RevPAR climbed 2.0 percent.
- In San Diego, ADR rose 1.8 percent during the year ending in the second quarter. This increase combined with the uptick in occupancy generated a 2.6 percent advance in RevPAR.

Sales Trends

- Transaction velocity has held steady throughout California during the past 12 months. Nearly half of all trades were in Los Angeles, San Francisco and Riverside-San Bernardino. Of these three markets, prices were highest in San Francisco at an average of $279,000 per room. Hotels in the metro changed hands with first-year returns in the mid-7 percent band. Higher cap rates were found in Los Angeles, averaging in the mid-8 percent area.
- The number of independent hotel sales picked up 6 percent during the year ending in June. These properties traded with average first-year returns in the low-8 percent band. Average prices for independent hotels declined roughly 5 percent during this time to $199,000 per key.
- Outside of independent hotels, a significant number of transactions comprised limited-service assets. These properties provided lower entry costs than the regional average, with prices near $90,000 per key.