AVISON YOUNG

Mid-2022 Recap

Canada Hotel Market

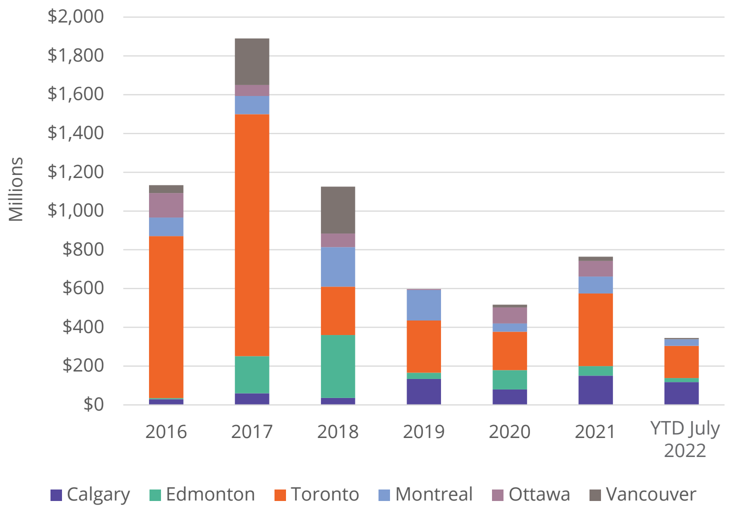
Market overview

Canada's hoteliers can see the light at the end of the tunnel. Market performance in July 2022 was the best since the onset of the pandemic with RevPAR recording its strongest-ever result at $162.10, according to STR. The inflation experienced during the last two quarters has bolstered the rise in ADR; however, occupancy rates have reflected strong consumer appetite to travel. The national occupancy rate of 75.5% in July 2022 was at a level not achieved since August 2019 (78.8%) and surpassed July 2019's result.

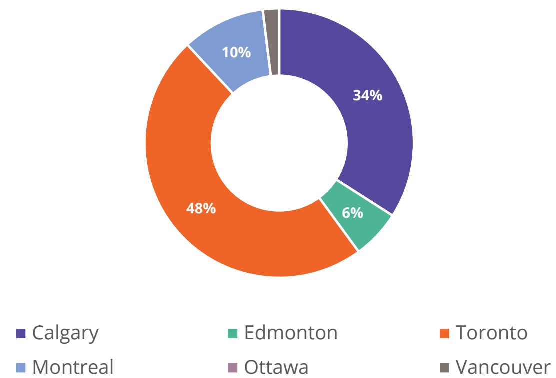
In 2020 and 2021, it was clear that certain industries were affected by the pandemic more than others. Among commercial real estate asset types, hospitality has arguably experienced the strongest head winds. The positive performance metrics reported in July were a welcome change and a well-timed one, as government support programs dried up as of May 2022.

Hotel market performance across the board has improved dramatically in 2022 versus 2021; however, transaction velocity has been down compared with a year ago. From January to July 2021, $386.5 million in transactions were posted in Canada's major markets. During the same period in 2022, transaction activity was down in terms of both capital (down 10% to $346.8 million) and number of trades (down 44% to 32). Transaction volume in the last four years has come down but three of the four years were heavily impacted by COVID-19.

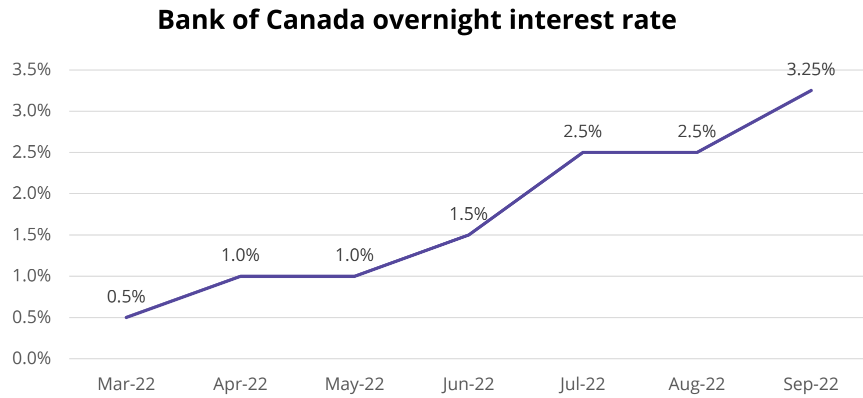
Investment sales volume by market (Annual)



Investment sales volume by market (YTD July 2022)



The first five months of this year accounted for 28 of the 32 transactions year-to-date*, with a material slowdown taking place in June and July. The two main reasons for this slowdown are, firstly, rising interest rates making financing more difficult to secure and, secondly, hoteliers are experiencing positive hotel performance which hasn't been realized, for many, since pre-COVID-19 times.



Among Canada's major markets, Toronto (encompassing the Greater Toronto Area and Greater Golden Horseshoe) posted the highest investment volume through July 2022, with $166.8 million. The largest transactions included The Oakes Hotel, Niagara Falls ($112.5 million) and two Banff Hotels acquired by InnVest Hotels for $70 million.

Jeff Hyslop, Senior Vice President, Asset Management and Investment for InnVest Hotels, comments: "Canadian lenders are still in the 'show me' phase of recovery but strong Q2 and Q3 results should bolster confidence in the hotel space." The positive performance shown in July's STR results is a good indication of what's to come for the recovery of the industry.

Notable Canadian hotel transactions in 2022 (mid-year)

Hotel Name	Region	Transaction Date	Total Price	Price per Room	Purchaser	Vendor
Oakes Hotel	Niagara Falls	4-Jul-22	$112,500,000	$474,684	Hilton Niagara Falls/ Fallsview Hotel & Suites	Kerrio Corporation
Charltons Hotel portfolio	Banff	5-Feb-22	$70,000,000	$427,000	InnVest Hotels	Charlton's Evergreen Court Ltd.
Motel 6 Whitby	Whitby	13-Jul-22	$18,500,000	$150,407	M6 Whitby Hospitality Inc.	G6 Hospitality
Union Bank Inn	Edmonton	10-May-22	$11,118,904	$147,500	2399430 Alberta Inc.	Mike Priestner Automotive Group

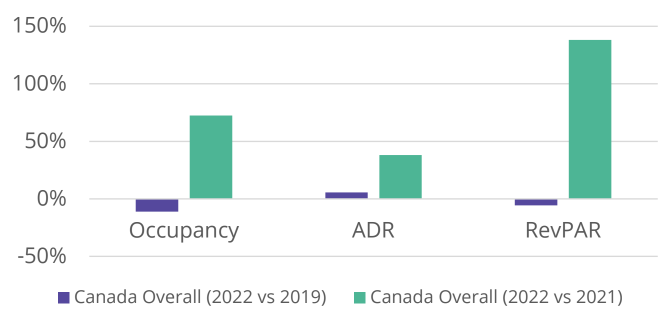
**Hotel transactions from January 1, 2022 - July 31, 2022.*

2022 performance

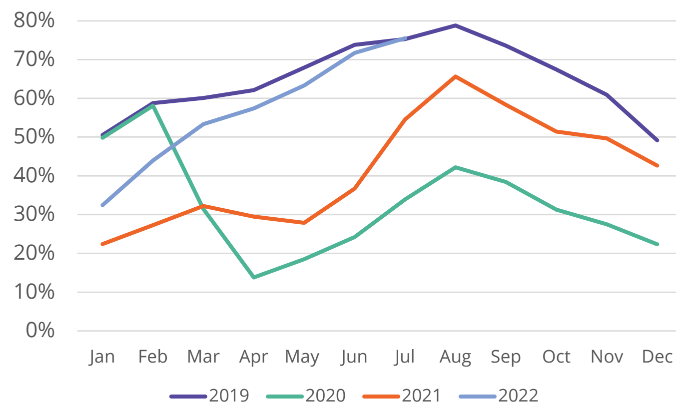
Overall, Canada's hotel market experienced year-over-year increases of 69% in Occupancy, 37% in ADR and 131% in RevPAR as of July 2022 – all great testaments to the health of the sector. Cautious optimism reigns when comparing 2022 with 2019 (pre-COVID-19) figures, as Canada is still below the 2019 benchmark – down 13% in Occupancy and 9% in RevPAR – but up 5% in ADR.

Furthermore, a look at national Occupancy for the last four years (2019 to 2022) reveals that July 2022 surpassed the performance achieved in July 2019 (75.5% vs. 75.3%).

Canada percentage change in Occupancy, ADR, and RevPAR (2022 vs 2019 and 2022 vs 2021)



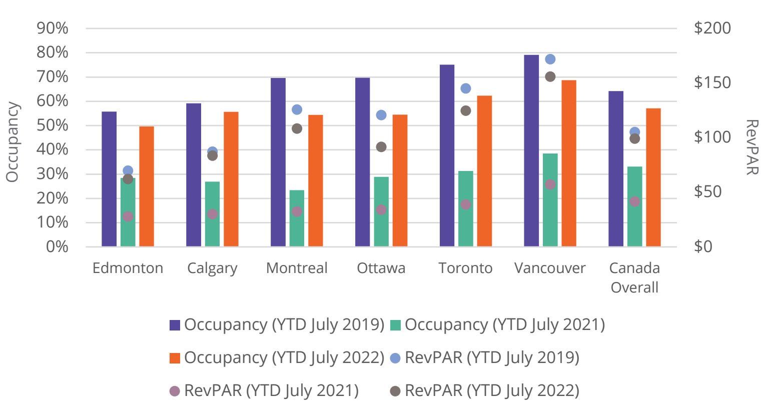
Canada Occupancy Rate (Jan 2019 – July 2022)



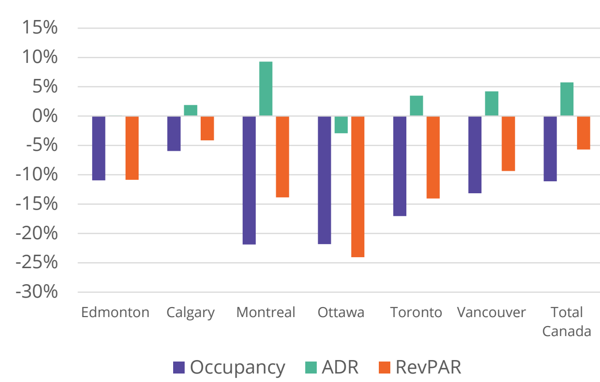
Hotel performance by market

According to STR's performance metrics, Canada's hotel market bounced back during the first seven months of 2022 – nearly returning to 2019 levels. Among the country's six major markets, Vancouver performed the strongest in ADR, Occupancy and RevPAR with $226.84, 68.7% and $155.86, respectively. Edmonton posted the lowest metrics with $125.40 ADR, 49.6% Occupancy and $62.23 RevPAR – however, these represented a significant improvement year-over-year (up 74% in Occupancy, 28% in ADR and 123% in RevPAR). While comparing to YTD July 2022 Vs YTD July 2019 YTD metrics it is clear that Montreal and Ottawa have had the most challenging recovery in occupancy and RevPAR. While Calgary has been the most resilient market with a dip of only 5.9% in occupancy and 4.1% in RevPAR. Montreal has bounced back in 2022 from 2021 however by experiencing the largest percentage change in Occupancy and RevPAR, with 132% and 234%, respectively, while Toronto posted the highest percentage change in ADR with 61% year-over-year.

Occupancy and RevPAR by market (YTD July 2019/2021/2022)



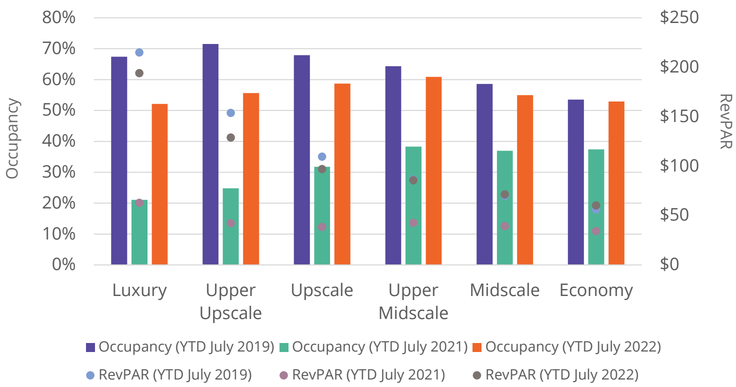
Occupancy, ADR, and RevPAR by market (% change YTD July 2019 vs July 2022)



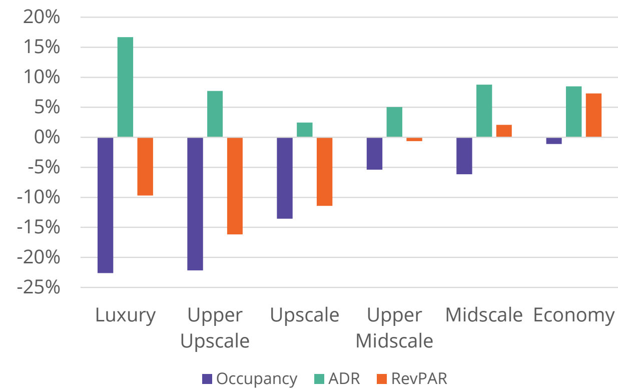
Hotel performance by class

By asset type, Upper Midscale reported the highest Occupancy as of July 2022, with 60.9%, while Luxury was lowest at 52.1%. However, the Luxury class had the strongest ADR and RevPAR ($372.15 and $194.06, respectively) – in contrast with the Economy class, which posted the lowest ADR and RevPAR ($113.84 and $60.25, respectively). Year-over-year, Luxury experienced the largest bounce-back in Occupancy (up 147%) and RevPAR (up 208%), while Upscale had the strongest growth in ADR (36.4%). However, Luxury and Upper Upscale hotels have still struggled to return to occupancy and RevPAR levels experienced in 2019. Luxury has experienced the largest decrease in occupancy of 22.6%, while Upper Upscale has experienced the largest decrease in RevPAR of 16.1%. The steadiest asset class compared with pre-COVID-19 data is Economy, with RevPAR growth of 7.3% from July 2019 to July 2022 – highlighting the resilience of Economy-class branded hotels throughout the pandemic.

Occupancy and RevPAR by class (YTD July 2019/2021/2022)



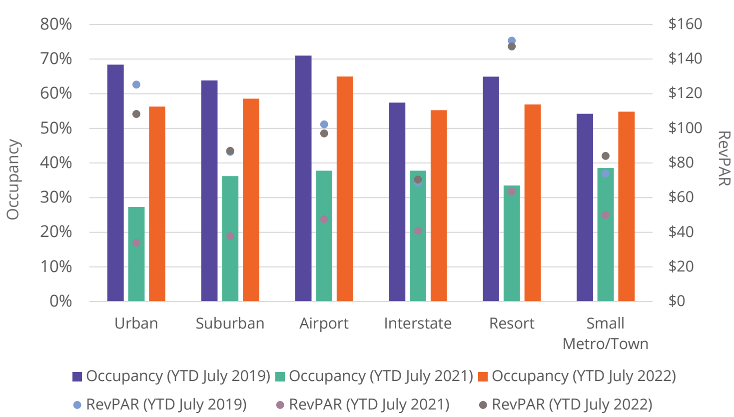
Occupancy, ADR, and RevPAR by class (% change YTD July 2019 vs YTD July 2022)



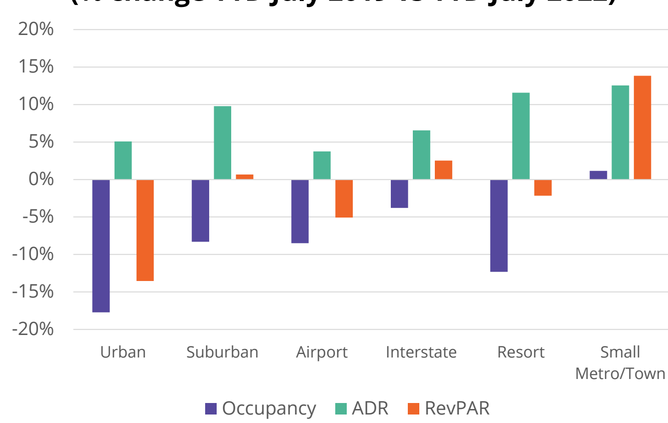
Hotel performance by location

Leisure travel has had the most profound impact on hotel market results. As of YTD July, airport hotels have had the strongest occupancy of 64.9%. Comparing YTD July 2022 to YTD July 2019, Urban located hotels have had the most difficult time returning to the performance metrics experienced in 2019, with a decline of 17.71% in occupancy and 13.53% in RevPAR. This should come as no surprise as many people have been putting off travel plans over the course of COVID-19 and want to make up for lost vacation time. Airports across the globe are having difficulty with staffing levels and, as a result, are struggling to keep up with the boom in travel demand – and Canadian airports are not exempt from this reality. The Government of Canada has reported that in June 2022, air departure traffic was 58 times higher than in spring 2020. The silver lining of airport delays is that they are evidence of demand for travel and hospitality across the globe. The ongoing popularity of domestic travel may be a factor in the performance of the Small Metro/Town hotel location category, which has outstripped its 2019 metrics by 1.2% in Occupancy, 12.6% in ADR and 13.8% in RevPAR.

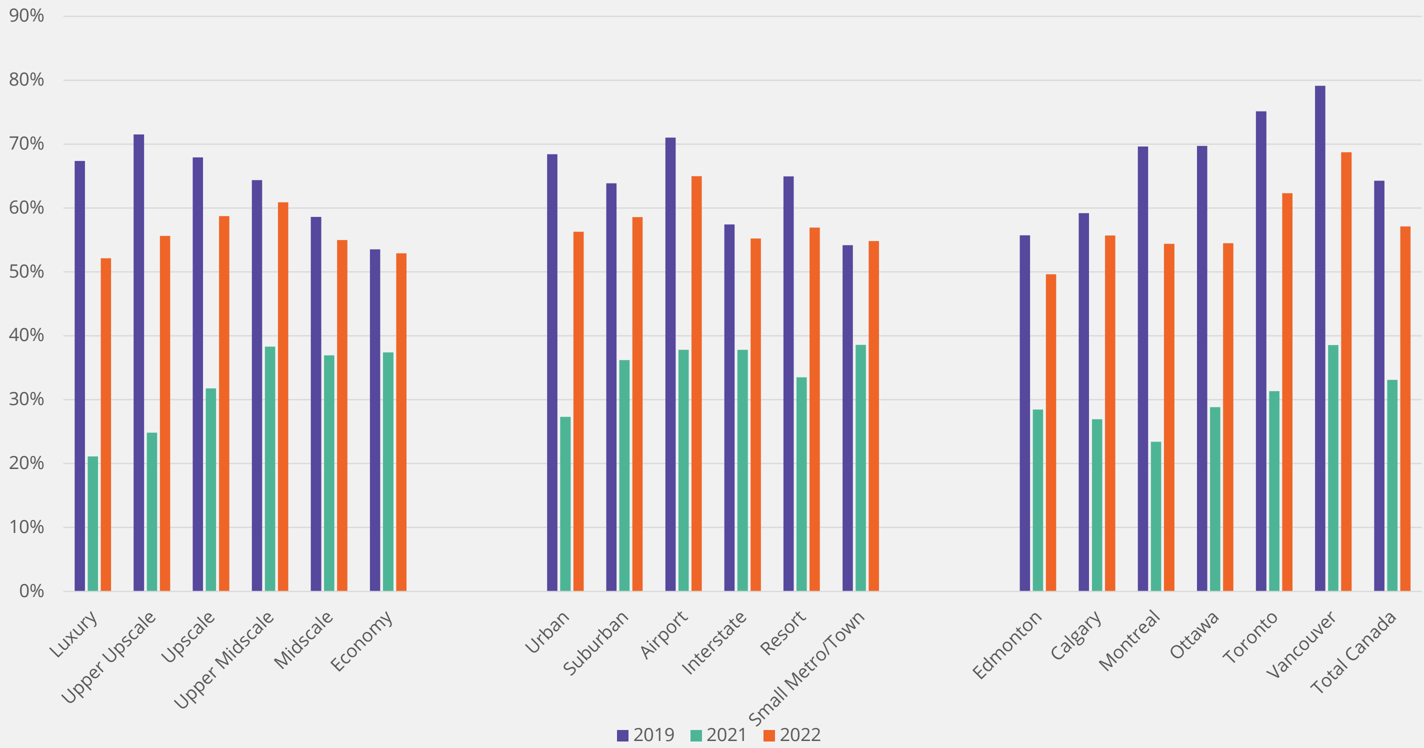
Occupancy and RevPAR by location (YTD July 2019/2021/2022)



Occupancy, ADR, and RevPAR by location (% change YTD July 2019 vs YTD July 2022)

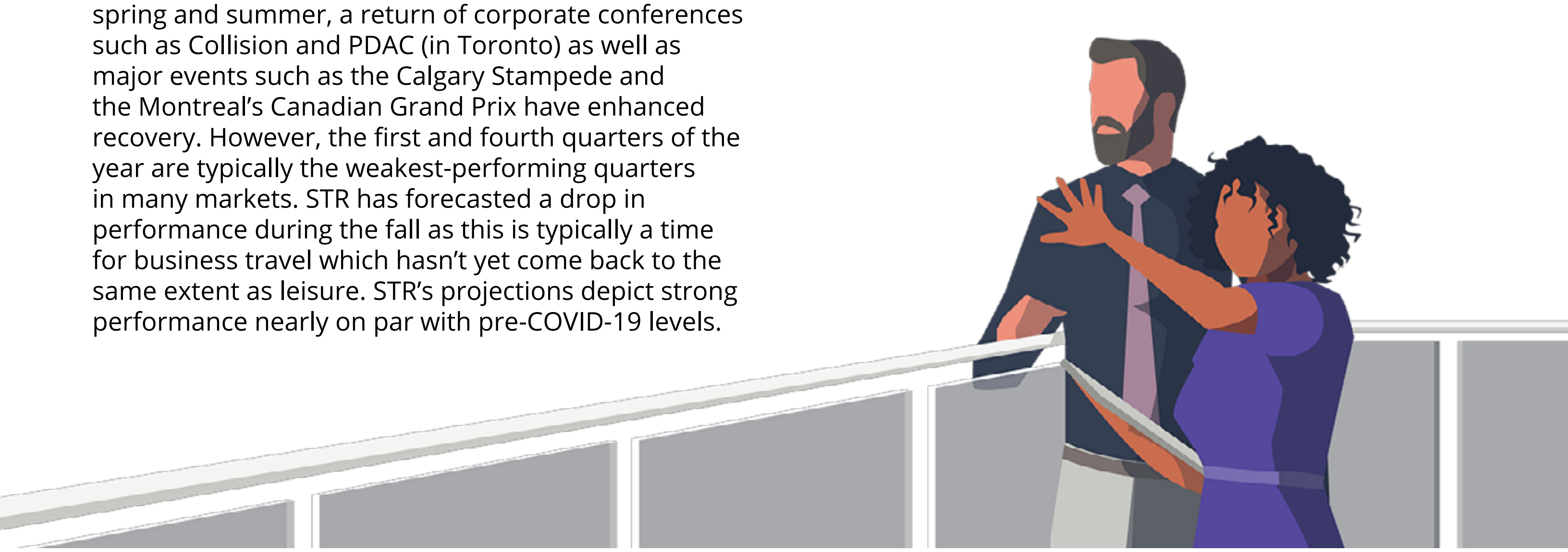


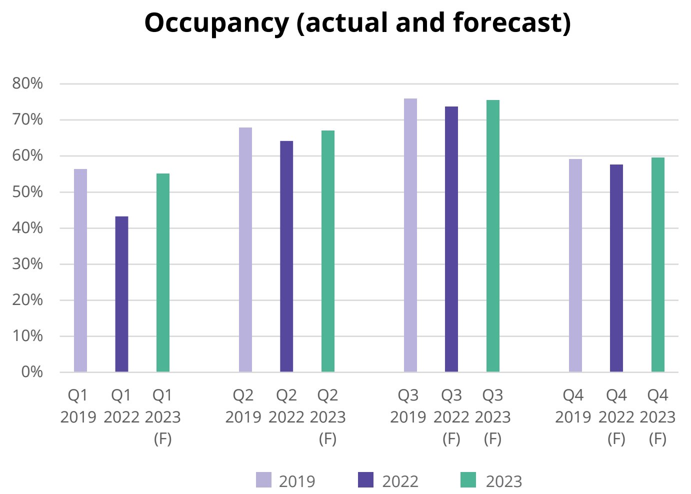
Occupancy comparison summary
(YTD July 2019, 2021, and 2022)

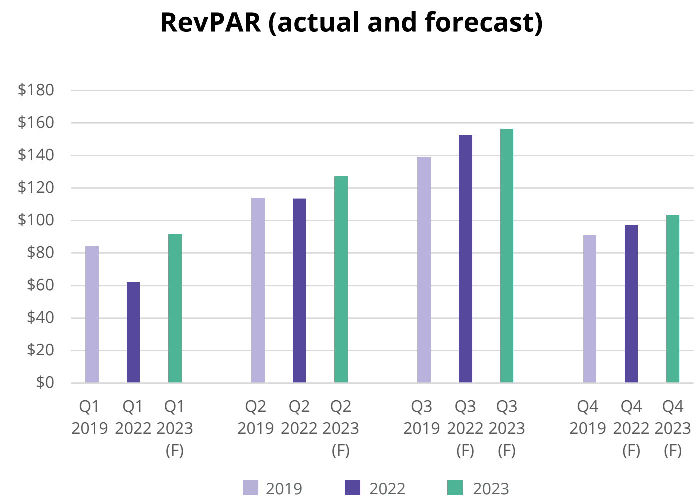


Looking ahead

Following the strong summer performance, hoteliers will need to focus on booking pace for fall and winter months when performance is typically derived from corporate travel and group bookings. Throughout the spring and summer, a return of corporate conferences such as Collision and PDAC (in Toronto) as well as major events such as the Calgary Stampede and the Montreal's Canadian Grand Prix have enhanced recovery. However, the first and fourth quarters of the year are typically the weakest-performing quarters in many markets. STR has forecasted a drop in performance during the fall as this is typically a time for business travel which hasn't yet come back to the same extent as leisure. STR's projections depict strong performance nearly on par with pre-COVID-19 levels.







Laura Baxter, Director of Hospitality Analytics – Canada for STR, comments: “Based on stronger-than-anticipated occupancy and ADR growth and a positive outlook for the rest of the year, the most recent full year forecast for 2022 prepared by STR and Tourism Economics has been revised upwards, with nominal RevPAR expected to reach 2019 levels this year. Both occupancy and ADR have been upgraded with occupancy expected to rise 18 percentage points in 2022 compared with 2021 to 59.9%, while ADR is forecast to grow 28.4% to $179.

“Looking ahead to 2023, we are expecting a period of sustained growth with further year-over-year improvements, albeit at a much slower pace than in 2022. Occupancy is expected to rise by 4.6 percentage points to 64.5% while ADR is forecast to grow 4.3% to $186.

“On a quarterly basis STR has predicted Q4 2023 to surpass Q4 2019 in occupancy with 59.6% compare to 59.2%, while Q2 2023 is predicted to out perform Q2 2019 with $127.10 compare to $113.99.”

In the fall 2022 and winter 2023, the typical seasonal drop-off will ensue, and we are expecting aspects of the business mix to change, with different components of pent-up demand like group and business travel to benefit hotels while other segments such as transient leisure somewhat taper off. Baxter’s remarks indicate some of the reasoning behind STR’s positive sentiment about what lies ahead for the hospitality sector.

Lessons learned

Hotels do not operate in a vacuum. They are an integral part of an overall economic community within the geographic area where they are situated. The health of other commercial real estate assets is impacted by the same factors as hotels in that area. Understandably, there are different risk elements attached to each asset class, resulting in a range of expected returns on both debt and equity investments.

Lessons from the COVID-19 pandemic (2020-2022):

- Hotels were considered too important to fail as government support (to an extent and varying by region), lender patience and brand cooperation (particularly on cap ex) helped prop up the industry.
- Leisure assets (i.e., resorts) proved more resilient than urban assets as people were restricted from cross-border travel, boosting "staycations."
- Remote work options took hold, generating a new customer segment blending leisure and business trips (aptly named the "bleisure" segment).
- Maximizing available outdoor space at hospitality assets became more meaningful.
- An anticipated abundance of deeply distressed hotel sales did not materialize.
- Several hotels were acquired as "change of use" investments.
- Pent-up travel demand appears to be recovering with strength.
- Construction cost increases related to supply chain issues will limit new construction.
- Diversification is important.

Lessons from the Global Financial Crisis recovery (2009-2019):

- Both ADR and Occupancy recovered annually to record levels achieved in 2018 and 2019 in many markets.
- General economic recovery mirrored hotel performance results.
- Daily pricing power of hotels tends to recover beyond CPI during growth periods.
- Branding and loyalty programs became more important to investors and lenders as they offered a "base" of business through global distribution (GDS) and central reservation (CRS) systems and brand proliferation.
- Valuations amongst all real estate asset classes grew through improved returns and cap rate compression.
- Transparent market performance metrics became more accessible (in most markets) through data companies such as STR.
- New market entrants (e.g., Airbnb and Expedia) affected the industry.
- Hotel REITs survived, then flourished.
- An anticipated abundance of deeply distressed hotel asset sales did not materialize.

Overall takeaways from periods of crisis

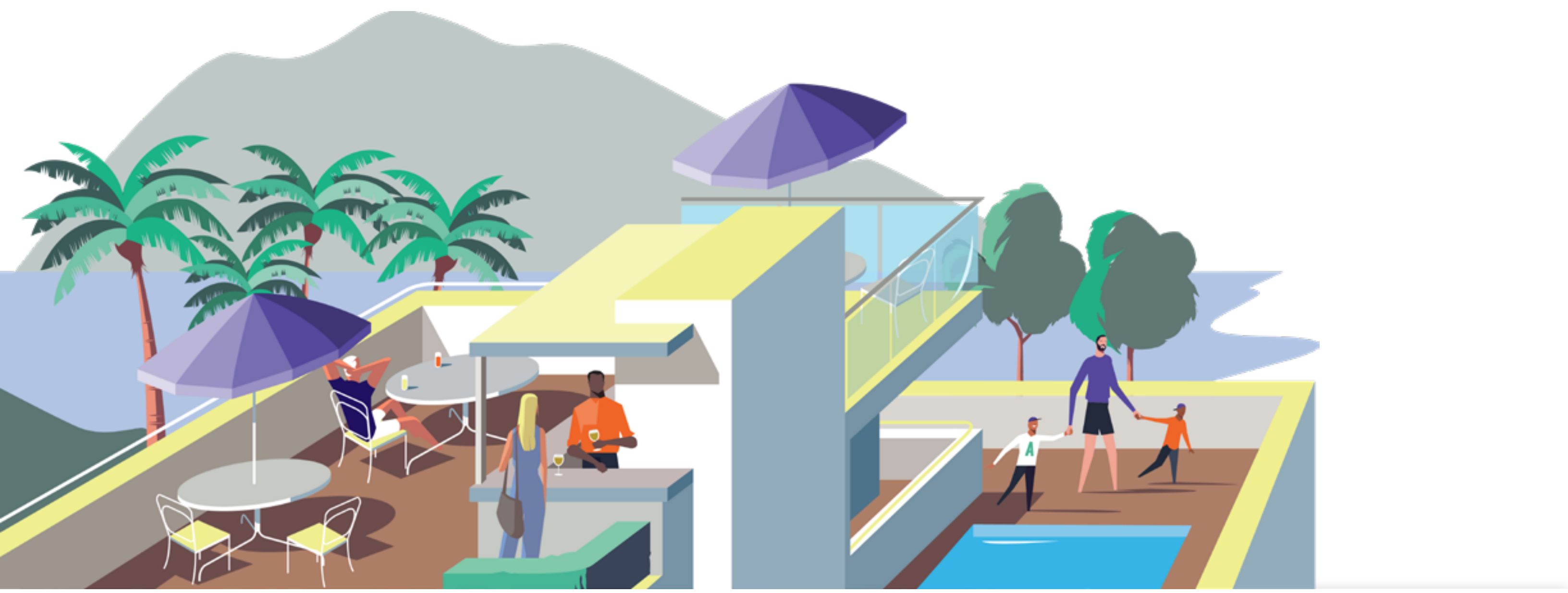
- Don't panic, especially if you don't have to.
- Investment, brand, management and lender partner agreements should have aligned interests.
- Due to the lower market liquidity attributes, a patient long-term commitment to the asset class will yield more beneficial results.
- They are a capital-intensive investment.
- Deferring capital and ROI investment opportunities adversely impacts value. A full understanding of capital expenditure requirements (i.e., brand-driven PIPs) is key.
- Financing attributes differ significantly (i.e., lower leverage and higher spreads) from other CRE assets.

Turning knowledge into strategy

Real estate investment knowledge accumulated through periods of growth, decline, recession and financial and health crises is invaluable. No real estate asset class, including hotels, operates independently of macro- or microeconomic factors impacting any market. Since real estate is cyclical, each class has unique attributes that benefit or hinder potential results depending on the position within the business cycle.

Hotel real estate investments have typically offered a unique hedge against inflation since pricing can be adjusted daily. This has placed hotels among the riskier asset classes, but that translates into greater yield potential. Presently, the global economy is facing an inflationary period and a rising interest rate environment. This could imply significant yield potential for both debt and equity investments within this asset class.

Over that last two decades, hotel market performance has become more transparent in most markets. Hotel financial reporting has adopted a uniform system of accounts, allowing for easier comparison across the industry. STR is the dominant firm tracking occupancy and ADR results across markets and several new firms have started to use data to create useful predictive analytics tools for hotel investors, allowing that collected knowledge to be turned into effective investment strategies.



Get more market information

Contact our hospitality group for investment sale, debt placement, and asset advisory services.

Curtis Gallagher*
Principal, Canadian Hospitality Lead
+1 416.673.4018
curtis.gallagher@avisonyoung.com

Haig Basmadjian
Senior Associate
+1 403.232.4316
haig.basmadjian@avisonyoung.com

Graeme White*
Associate
+1 647.598.2318
graeme.white@avisonyoung.com

Jolene Keats
Director, Eastern Canadian Hospitality
+1 902 579 1245
jolene.keats@avisonyoung.com

Bobby Singh*
Associate
+1 905.283.2326
bobby.singh@avisonyoung.com

AVISON YOUNG

avisonyoung.ca

* Sales Representative