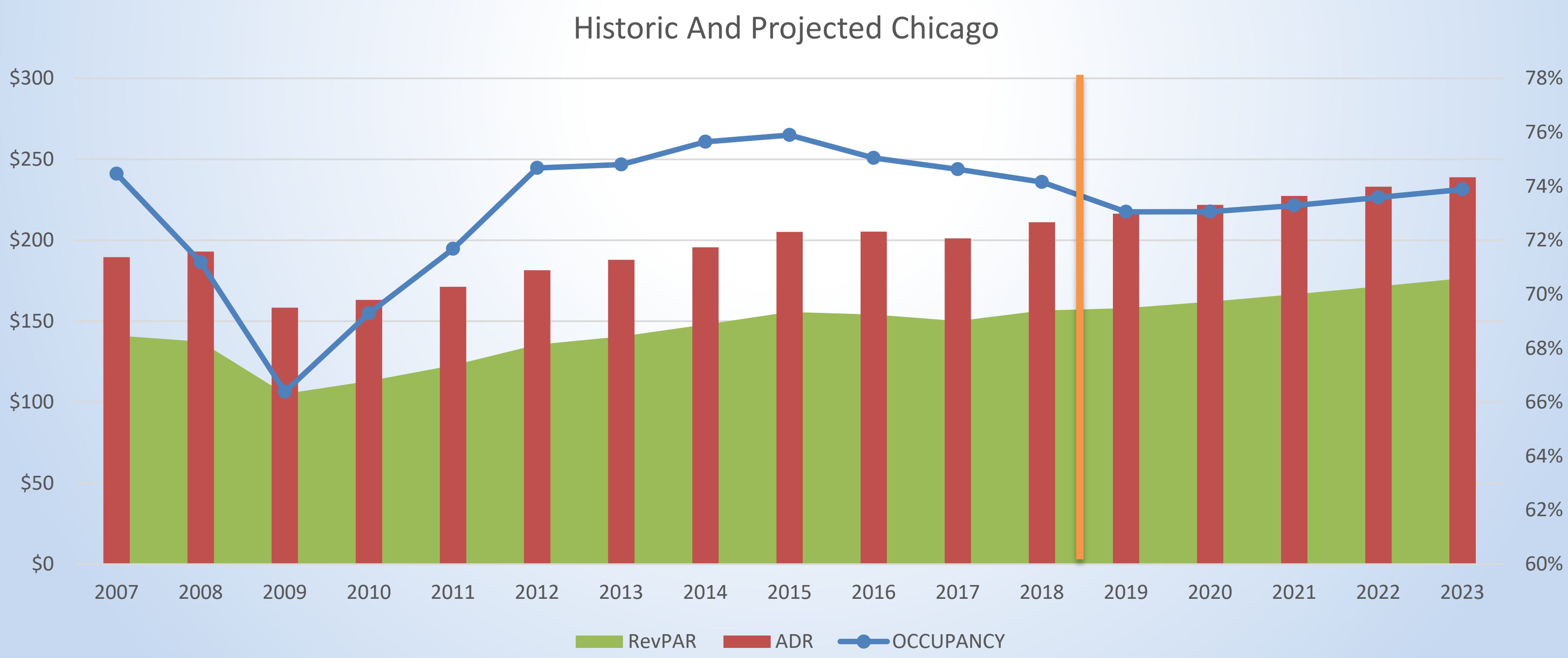
MAI Chicago Hotel Outlook:

March 2019

Chicago's mid 70% occupancy trend continues despite new building.

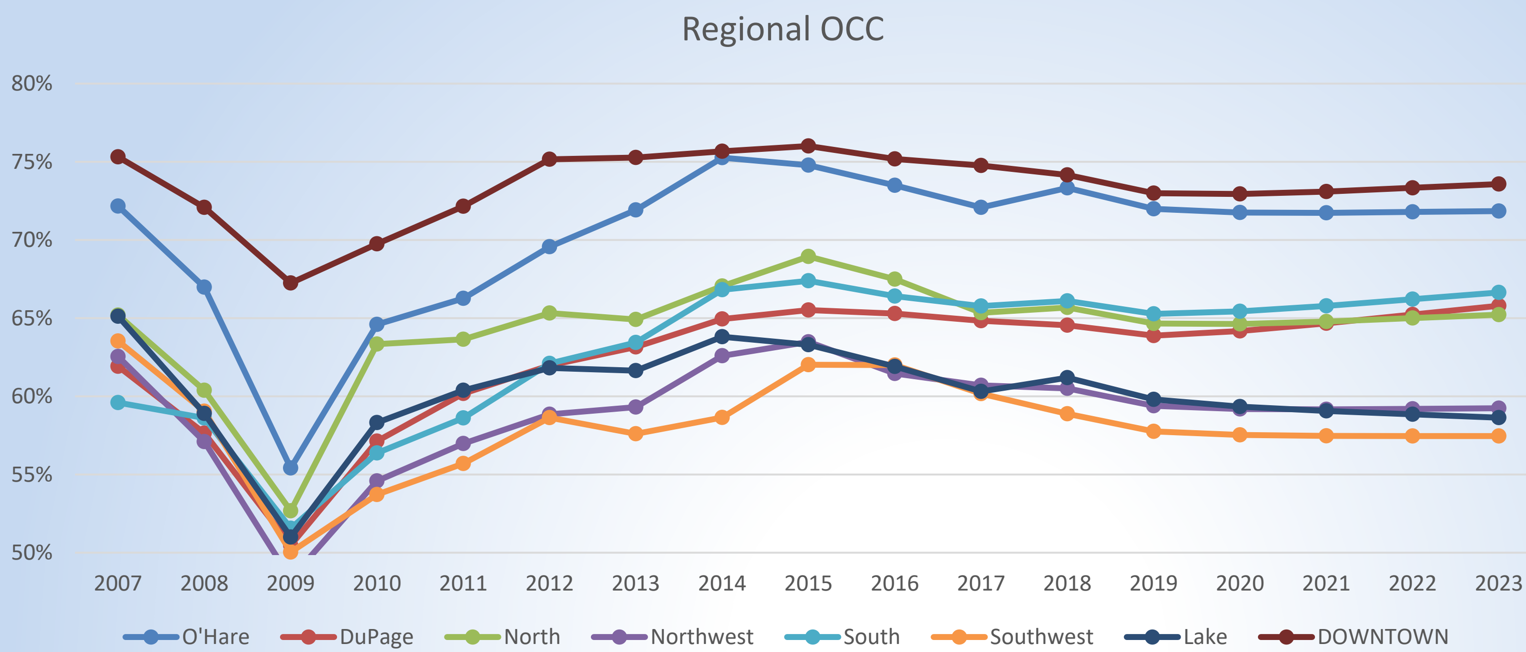
During the recession, it only dropped down to the mid 60's, while everywhere else saw drops to low 50% occupancy.
Chicago Dropped Rate to gain demand (by over $30), during the recession, but also in response to minor drops, such as 2016.
New properties are not pushing rate, creating a luxury price gap.

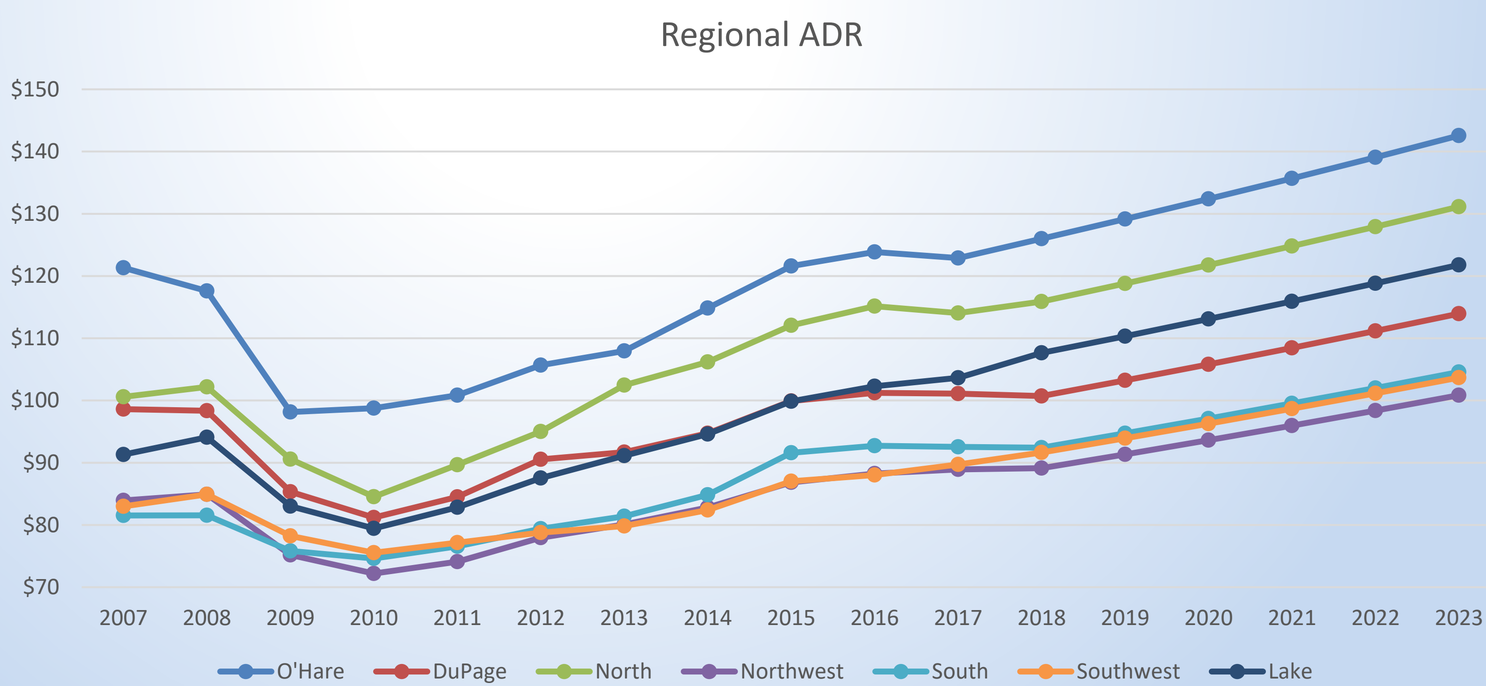


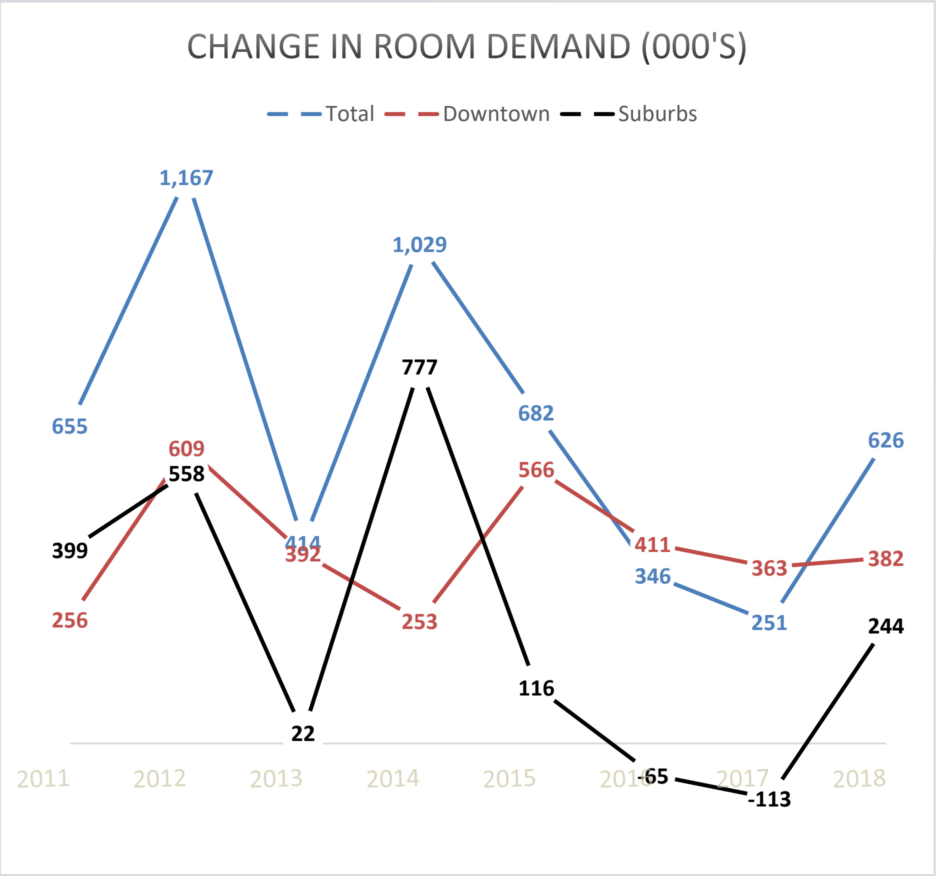
Dynamic Shift in Convention Business

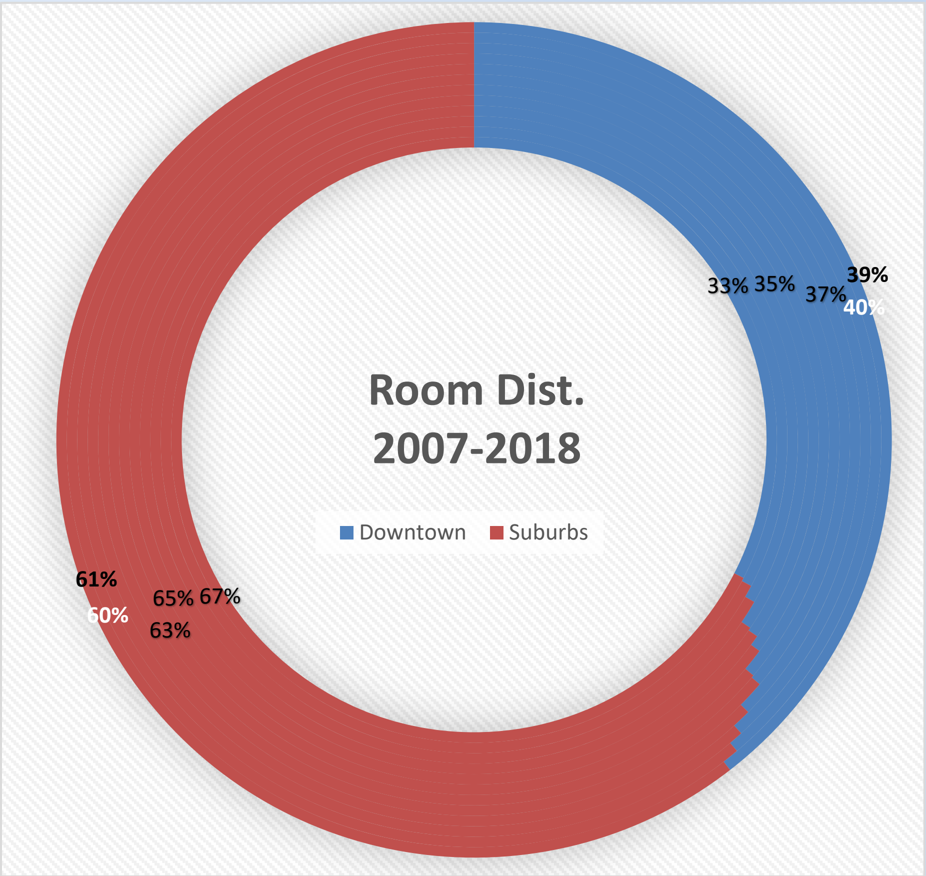
Demand Source	United States	Chicago
Commercial	35%	35%
Group Business	25%	30%
Group Leisure	10%	20%
Leisure	30%	15%

- Impact of Technology
  - Frequency of Meetings/Major Product Releases less important
  - More regional events-to address technology and legislative impact on operations/industries
  - Shorter trade shows
    - Internet research before attending to be more efficient
    - Available data
    - Ability to use technology to reduce space requirement
  - Tracking of leads and impact on attendance
    - Short term focus on costs vs. long term impact on business.
- New Competition
  - Facilities in Major Markets
  - Development of facilities in secondary markets
    - Can now host smaller and regional groups, competing with major cities.
- Increase in SMERF business
  - Changes in family dynamics-more dispersed
  - Large retiring groups with time on their hands
  - Increasing specialty interest and affiliations
  - More group leisure activities
    - Amateur sports
    - Increased activity in traditional leisure categories


Regional OCC
80%
75%
70%
65%
60%
55%
50%
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022
2023
O'Hare
DuPage
North
Northwest
South
Southwest
Lake
DOWNTOWN


Regional ADR
$150
$140
$130
$120
$110
$100
$90
$80
$70
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022
2023
O'Hare
DuPage
North
Northwest
South
Southwest
Lake





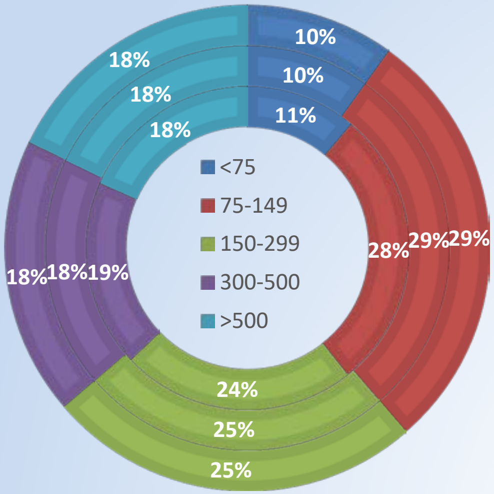
The suburbs decreased from 67% to 60%

Regionally, hotel building booms have preceded most recessions, though they are NOT a leading indicator.

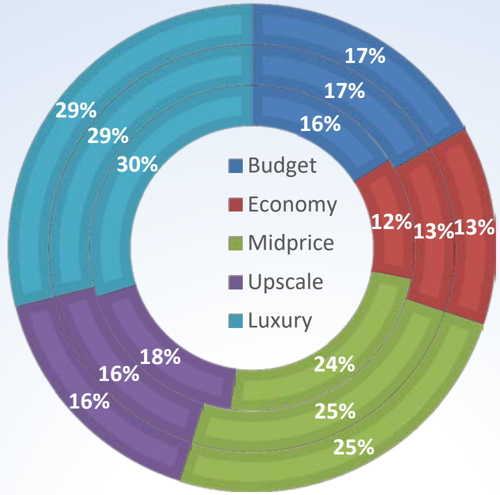
-On their own, overbuilding causes temporary depression of occupancy, while rates typically do not fall much; this time, we have seen more aggressive movement, due to the sheer scale of the new development.

We need to generate about 500,000 room nights annually to keep up with supply growth in the CBD market.

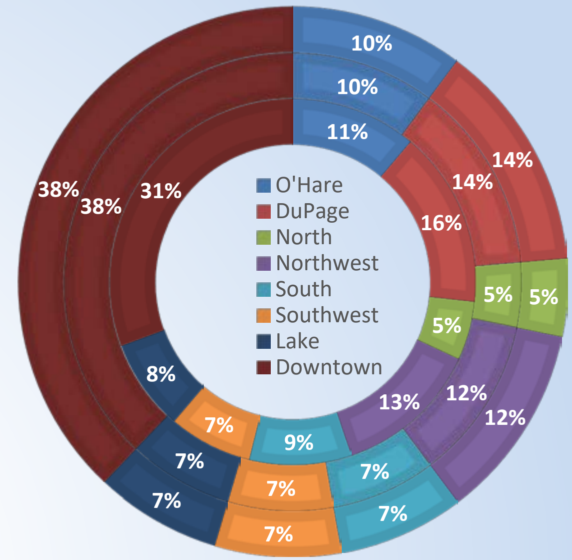
PROP SIZE 2008, 2018, 2023



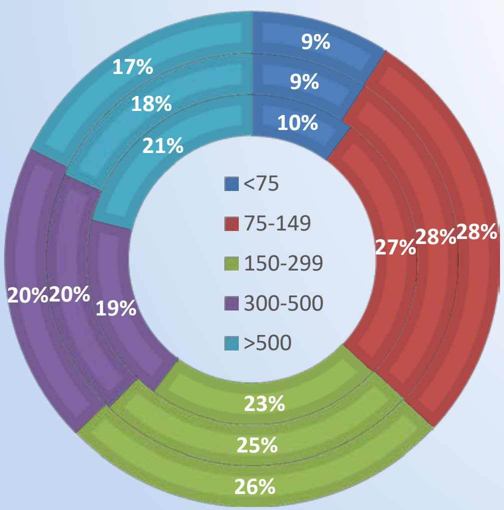
TYPE, 2012, 2018, 2023



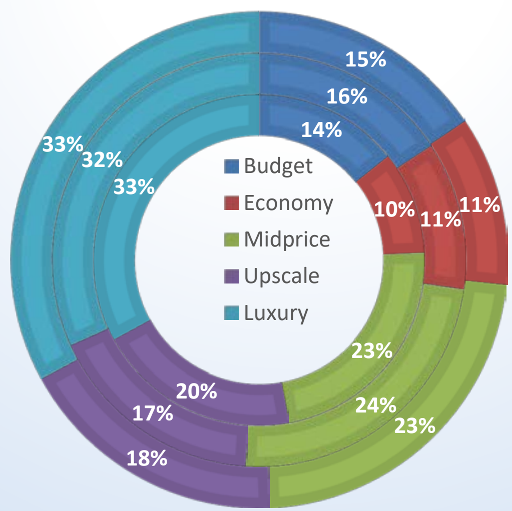
DIST., 2008, 2018, 2023



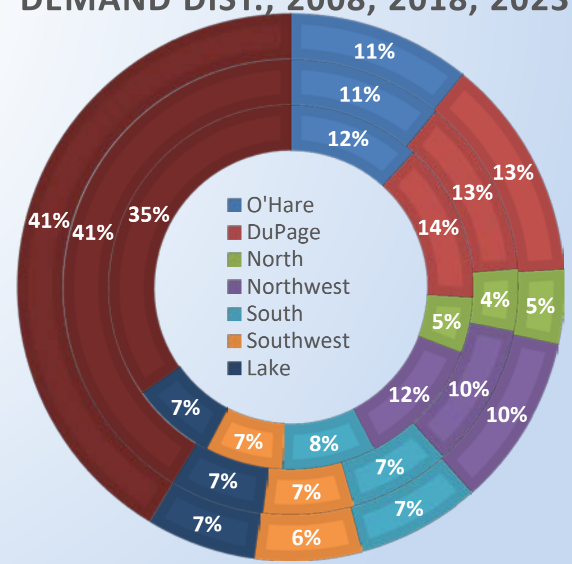
DEMAND 2008, 2018, 2023



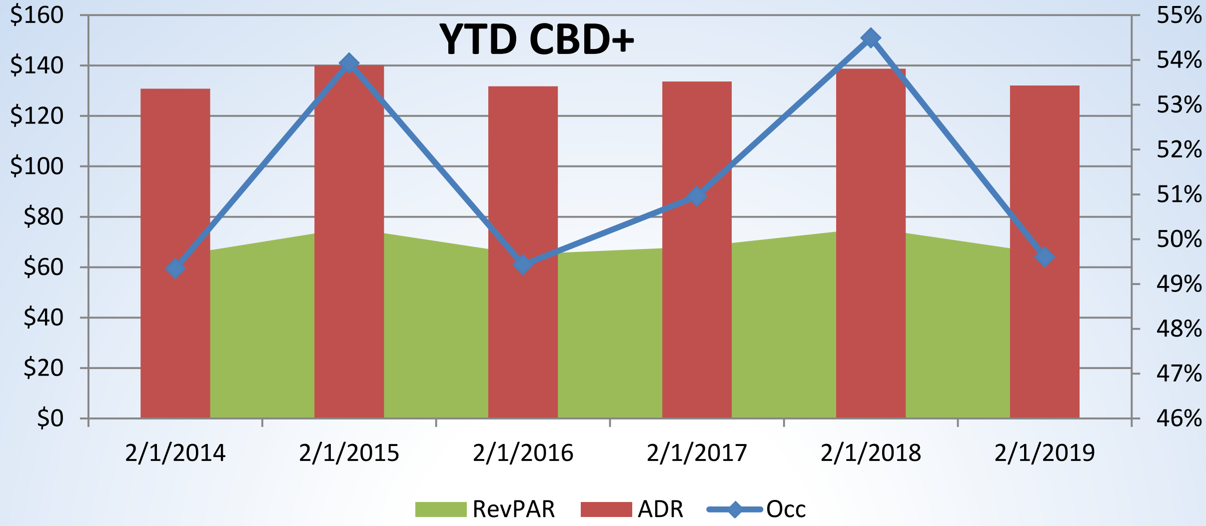
DEMAND, 2012, 2018, 2023

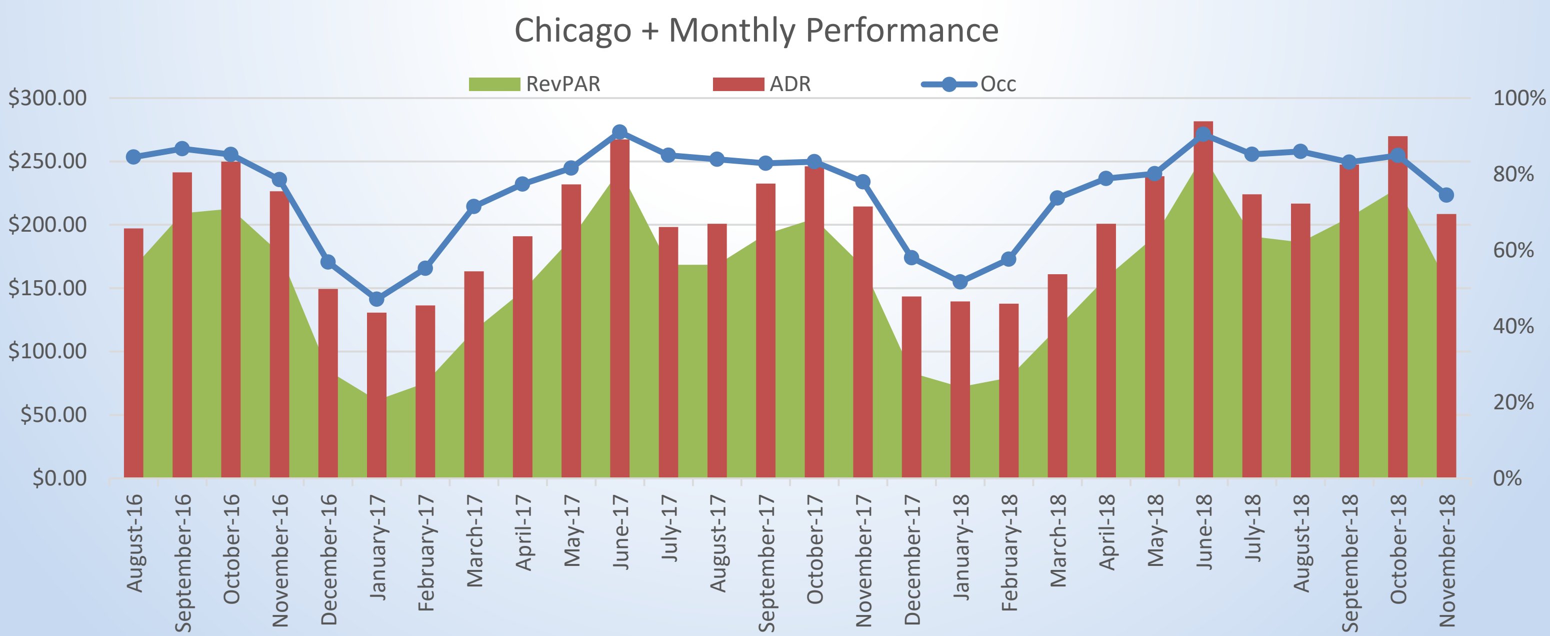


DEMAND DIST., 2008, 2018, 2023



Luxury, between 150-200 rooms, downtown Chicago saw biggest growth: changes slow


YTD CBD+
$160
$140
$120
$100
$80
$60
$40
$20
$0
55%
54%
53%
52%
51%
50%
49%
48%
47%
46%
2/1/2014
2/1/2015
2/1/2016
2/1/2017
2/1/2018
2/1/2019
RevPAR
ADR
Occ


Chicago + Monthly Performance
RevPAR
ADR
Occ
$300.00
$250.00
$200.00
$150.00
$100.00
$50.00
$0.00
100%
80%
60%
40%
20%
0%
August-16
September-16
October-16
November-16
December-16
January-17
February-17
March-17
April-17
May-17
June-17
July-17
August-17
September-17
October-17
November-17
December-17
January-18
February-18
March-18
April-18
May-18
June-18
July-18
August-18
September-18
October-18
November-18

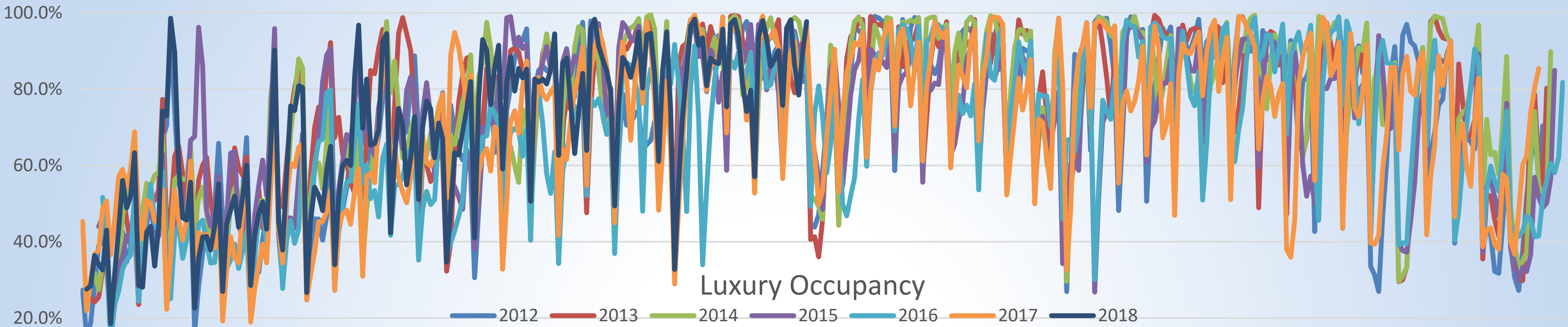
Chicago is eating the suburbs and we can prove it.

- Our attitude is still based on the last recession. We think hotel business can be induced to show up.
- Chicago, really the whole US hotel industry is largely INELASTIC.
  - Rate is a secondary factor compared to convenience, loyalty programs, habit, amenities, service, etc.
  - Conventions and commercial are largely negotiated by someone other than the guest.
- Our estimate is that around 60% of the market is NOT rate sensitive.
  - This means to make a product appeal to 40%, you are giving a discount to 100%, rather than losing some portion of that percentage.

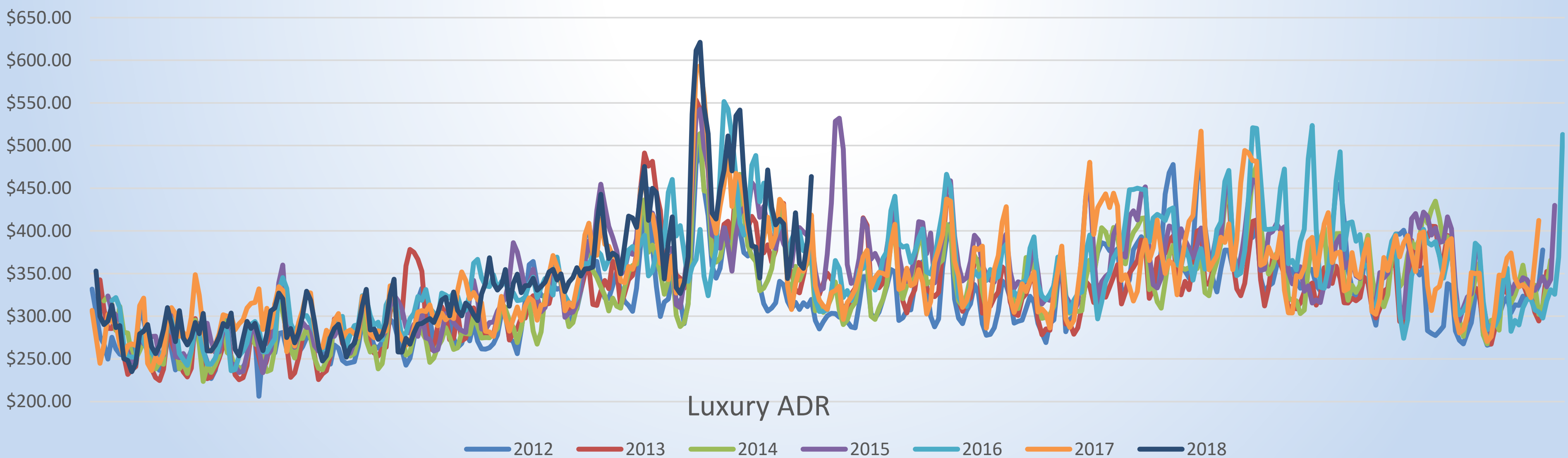
Chicago still needs to push rate

- Or rather, it could, if hotels chose to.
  - We've said before hotels are leaving money on the table. Downtown could improve by $25 a night, tomorrow, if hotels and owners had the stomach for it.
- We learned the wrong lesson from the recession:
  - Hotels are cannibalizing the suburbs by matching them in rate offseason, but this is largely INELASTIC demand.
- Despite new upper upscale supply, rate is anemic.
  - A priority in keeping occupancies higher than they should be has led to significant discounting. It would be healthier all around to focus on RevPAR
- Because Chicago doesn't push rate, the suburbs can't, and it means that ADR growth will continue to be anemic.

Our previous graphs had too much noise to show this well. We've sorted them by week rather than date to prove what we mean.

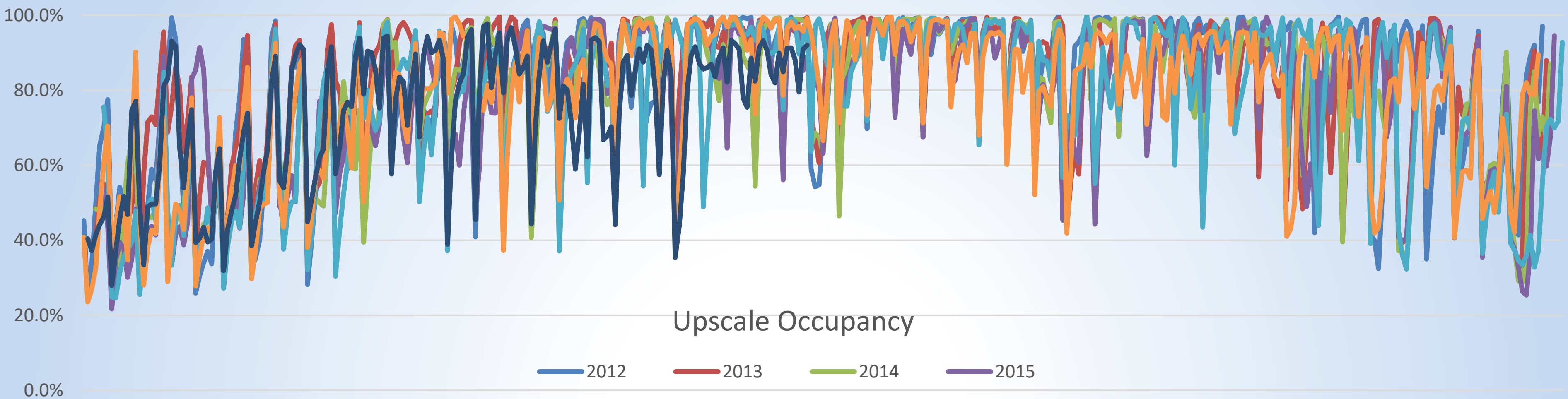


Luxury runs at around $250 in winter, and sees event-based spikes through the summer and fall

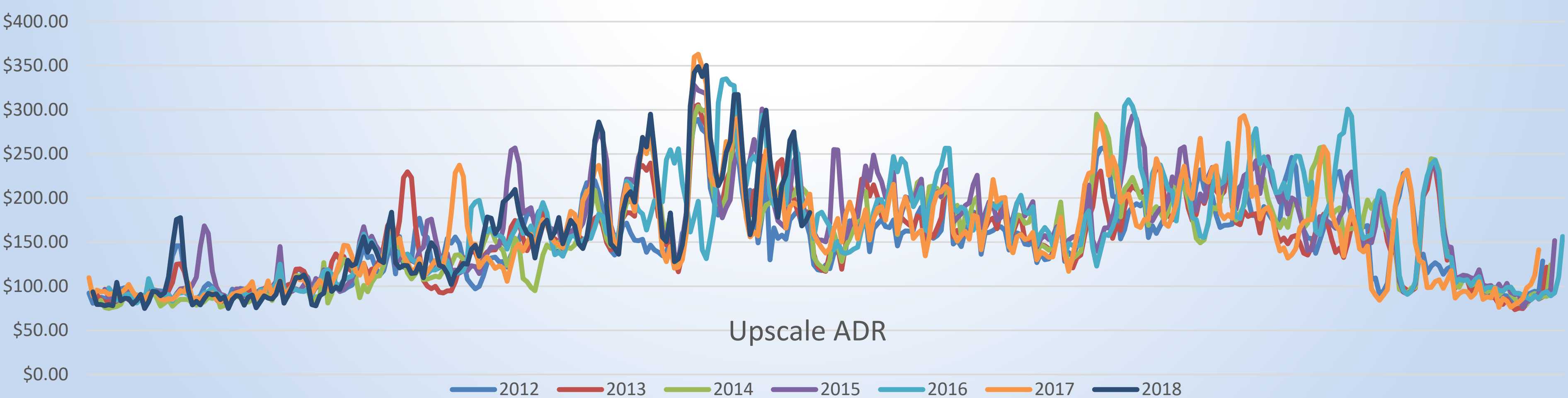


There is not a strong year-over-year increase in rate during the offseason.

Upscale starts and stays higher in occupancy than Luxury, and features more fill days

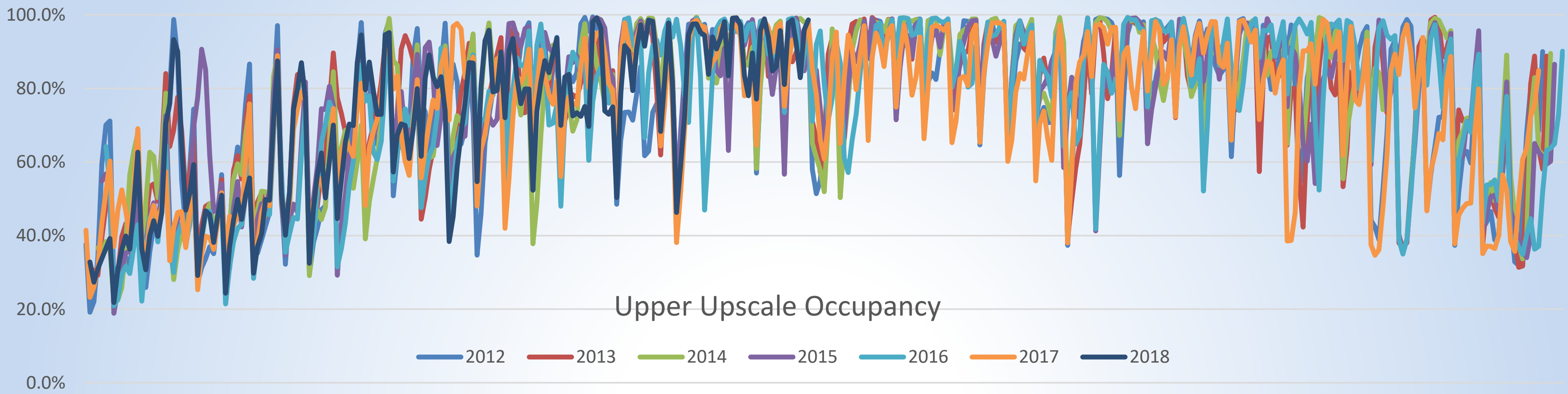


Rates start at under $100 for winter and move up during event and convention periods.

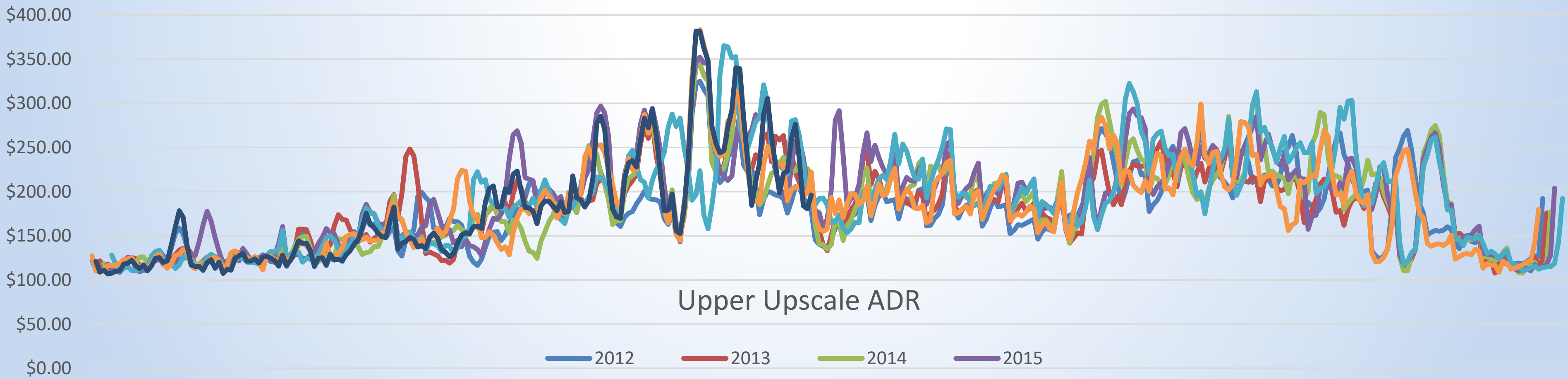


These low rates compete directly with the suburbs for inelastic business. Little RevPAR gained.

Upper Upscale Mirrors Upscale, with more weekday-weekend variation

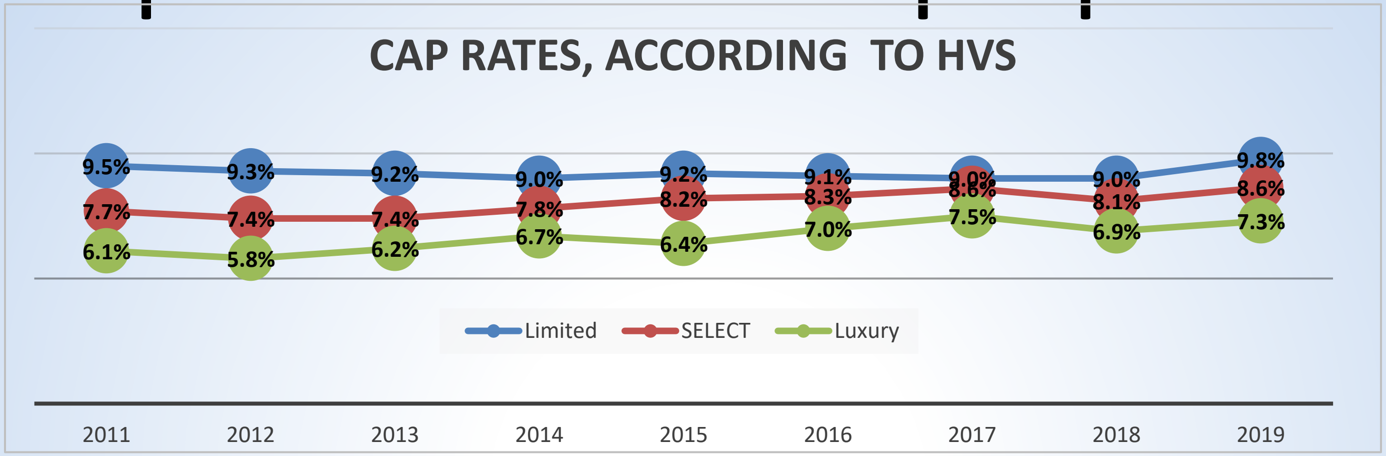


Rates start at around $110 and are almost exactly the same as Upscale during peak.



This means there is a $130 difference between Upper-Upscale and Luxury that no one is taking advantage of. It also means that Upscale has nowhere to go and there is nothing to distinguish the two segments. Upper upscale is the culprit that eats into upscale, which in turn eats into suburban figures. The suburbs can't go lower, so the only place that can move is this segment.

Cap Rates in Hotel properties



Impacted by: Lack of Surprises in Sector (Despite Late Cycle)

Major Purchases in 2018 were Luxury, Single-Asset

-$41 Billion. PPK increased by 21% to $153k

-Plaza, Waldorf, Grand Wailea, London House

Less activity this year and beyond should revert rates, price per key should drop

Forced rebranding by Franchisors

Chicago Average cap <8%, Suburbs 8.49%

Trends in Transactions

- Hotels still retain a premium over other commercial real estate
  - Limited service still highest but flat
  - Select Service and Extended stay have increased
  - Luxury still lowest cap but rose strongly.
- Chicago's cap rates are average for the nation at 7.5%.
  - Comparatively NY is 6.3% and Houston is 8.3%
- Nationally, Down significantly from 2016
  - Volume lower by 18%
  - Fewer portfolio deals overall, REITS out of market
- Lower Foreign investment.
  - 2016 saw several high-value deals across the country and in Chicago
    - Anbang alone makes up the difference
      - (InterContinental and Fairmont, 2016) $952M
      - Also has now had its assets seized by China's Government.
    - Union Investment RE (London House) $315M, Per key $697k
  - Trophy sales such as these are largely done.

Trends in Hotels

- Hotels are more profitable than they have been for years.
  - Some of this is because major renovations have already happened,
  - Also because of continued efficiency and shifts in operations. Grab and go; revised food service.
  - Largest change in costs is in “other”, or more practically, phones, PPV, and ubiquitous OTC costs plus fees (Resort fees; in-room-safe; internet).
  - Channel costs are dropping: Marriott vs. OTCs

Suburban Hotel Future

- A growing issue in the next few years
- Franchises are beginning to remove branding on hotels over 20 years old.
  - Forces new development in existing clusters to maintain a major flag, spurring construction.
  - Forces older hotels to re-brand to lower scale flags, resulting in discounted sale prices.
  - We expect for a cluster of 5 hotels, 1 new construction building.
- The end result will be a wave of downgrading similar to what happened with the roadside motels 20 years ago.

Overall Outlook

- Development in the CBD continues at an unprecedented pace, driven by new development areas and in-fill development.
- Rates continue to be conservative as brands and properties fight for market share rather than rates.
- Channel costs are coming down.
- Hotels are more experiential, less cookie cutter
- Occupancies will continue to dwindle as construction continues.