

US Equity Research

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Ryan Meliker | Analyst | Canaccord Genuity Inc. (US) | rmeliker@canaccordgenuity.com | 212.389.8094

Michael Kodesch | Associate | Canaccord Genuity Inc. (US) | mkodesch@canaccordgenuity.com | 212.389.8095

| Company                | Rating | Price     | Target    |
|------------------------|--------|-----------|-----------|
| <b>REITs - Lodging</b> |        |           |           |
| AHP-NYSE               | Hold   | US\$12.35 | US\$14.00 |
| AHT-NYSE               | Hold   | US\$6.67  | US\$6.00  |
| APLE-NYSE              | Buy    | US\$18.26 | US\$20.00 |
| DRH-NYSE               | Buy    | US\$10.25 | US\$12.00 |
| HPT-NYSE               | Hold   | US\$28.92 | US\$30.00 |
| HST-NYSE               | Hold   | US\$16.97 | US\$17.00 |
| HT-NYSE                | Hold   | US\$19.82 | US\$20.00 |
| INN-NYSE               | Buy    | US\$14.16 | US\$15.00 |
| LHO-NYSE               | Hold   | US\$26.92 | US\$25.00 |
| MAR-NASDAQ             | Buy    | US\$78.07 | US\$81.00 |
| RLJ-NYSE               | Hold   | US\$22.26 | US\$21.00 |
| SHO-NYSE               | Buy    | US\$14.29 | US\$14.00 |

Share price as of November 28 2016

Industry Overview

Takeaways from KOL lunch with LW Hospitality Advisors

Yesterday, we hosted a lunch with Evan Weiss, Principal of LW Hospitality Advisors (LWHA), to discuss the current state of the lodging industry and their outlook going forward. Overall, Evan described his firm's tone as one of cautious optimism, as RevPAR is expected to continue to grow in 2017 and 2018, albeit modestly. LWHA also believes that, generally speaking, asset values are flat to peak levels in certain markets, while they could be down 20% in others. They are most positive on Austin, Nashville and Denver and more cautious on NYC asset values, while suburban asset values have only declined modestly from peak (cap rates up 100-150 bps, offset considerably by stronger cash flows).

Below are details associated with our takeaways from the lunch:

**The bottom line.** Following our lunch with LWHA, we remain cautious regarding REIT NAV growth over the next year. Additionally, we are increasingly cautious surrounding outsized exposure to New York and San Francisco and increasingly favor exposure to secondary markets heading into 2017. That makes us more positive on MAR, INN, APLE and AHT and more cautious on HT, LHO and HST.

**Lending is tighter.** LWHA indicated that lending parameters are tighter and more expensive than a year ago and require stronger sponsorship. Instead of using 2015 cash flows to underwrite debt, lenders have moved to 2013-2014 cash flows as an expectation for mid-cycle potential. The good news is that risk retention rules have not had the impact feared on debt pricing. While smaller issuers have ceased origination, the larger CMBS issuers have only increased interest rates by less than 25 bps to account for risk retention regulation, which goes into effect at the end of December.

**Supply growth may peak in 2017.** LWHA expects supply growth to be 2% in 2017 and 1.5-2.0% in 2018, before moderating in 2019. However, supply is expected to remain a challenge in Manhattan, where LWHA expects 8,000 new rooms opening in 2017 and another 4,000-6,000 in 2018. That is on top of Manhattan's recent supply growth and another 3,000-4,000 rooms in development in Brooklyn and Queens.

**Asset values mixed.** Generally speaking, LWHA believes asset values have declined from peak by as much as 20% in certain markets. However, Denver, Austin and Nashville have been resilient and suburban markets have seen cap rates rise, but stronger cash flow growth has helped offset that. In core urban markets like New York, trophy asset values remain at peak levels as buyers tend to be long term holders and less concerned with short term cash flows. But non-trophy assets are well below peak valuations and values could move lower with challenging fundamentals and rising costs, before they begin to recover again in 2019. Foreign capital has also pushed into secondary and tertiary markets, chasing yield. LWHA notes this is not the same foreign capital that is buying trophy assets, but it is helping support valuations in secondary markets.

LWHA further noted that the lodging sector is a neighborhood business and some asset value have actually increased and several markets have witnessed record setting per room pricing including: Boston, Chicago, Seattle, and Washington DC.

**Technological headwinds could abate.** LWHA believes that technological innovation creates pricing transparency across the lodging industry which limits pricing power. However, Airbnb regulation should have an impact on pricing in major urban markets and the movement toward cancellation rate implementation could help as well. As Lodging follows the airline industry's lead regarding ancillary income, there is cash flow upside across the industry as these efforts gain traction.

**Investment thesis:** Barring an economic recession or renewed economic growth, which we don't forecast in the near term, we believe RevPAR growth is stabilizing around the 2-3% level. In that environment, we believe the group offers modest upside, but prefer stocks that we believe have outsized embedded growth (MAR, INN, APLE and SHO).

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Date and time of first dissemination: November 29, 2016, 04:45 ET

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|-----------------|-------------------|--------|------------|
|                 | #                 | %      | %          |
| Buy             | 567               | 59.62% | 36.16%     |
| Hold            | 290               | 30.49% | 17.59%     |
| Sell            | 30                | 3.15%  | 20.00%     |
| Speculative Buy | 64                | 6.73%  | 68.75%     |
|                 | 951*              | 100.0% |            |

\*Total includes stocks that are Under Review

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