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Market Close-up: Orlando Hotel

Overview and Economy. The Orlando MSA is the 23rd largest in the U.S., with a population of nearly 2.5 million, an 18% increase from 2010-2017. It has 133,982 hotel rooms in 515 hotels, according to Lodging Econometrics. In 2018, 11 new hotels (2,051 rooms) were completed, a disciplined 1.6% increase. A further 9 new hotels (1,768 rooms) are scheduled for delivery in 2019. Real (2018 dollars) running 12-month revenue per available room (RevPAR) fell modestly, to $97.24 in January 2019, compared to $98.18 the prior year, while the real average daily rate (ADR) increased from $123.50 to $126.10 per key over the same period. Rising operating costs are squeezing NOI.

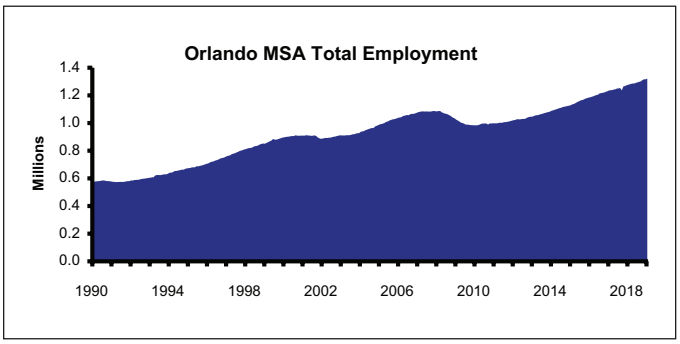
With balmy weather year-round, the MSA is an attractive destination for both business and leisure travelers. Conventions, theme parks, and other attractions draw millions of visitors to the region, generating significant business and tourism revenues. Other MSA entertainment attractions include the National Basketball Association's Orlando Magic, National Women's Soccer League's Orlando Pride and Major League Soccer's Orlando City Soccer, along with professional hockey and football teams. Walt Disney World (four theme parks: Magic Kingdom, Animal Kingdom, Epcot, Hollywood Studios), Universal (two theme parks: Universal Studios, Islands of Adventure), SeaWorld, LEGOLand, Kennedy Space Center, Madame Tussaud's Orlando, and numerous luxury golf courses also draw a significant presence.

The largest industries in the MSA are leisure and hospitality, trade, transportation, and utilities, professional and business services, government, and education and health services. The largest industry in the area, leisure and hospitality comprises 21% of the MSA's total non-farm employment. Corporate headquarters located in the MSA include Hard Rock Café, Longhorn Steakhouse, Olive Garden, Darden Restaurants, Tupperware, and Yard House. The largest employers include Walt Disney World Resort (74,000), Universal Orlando Resort (20,000), AdventHealth (19,300), Orlando Health (15,100), University of Central Florida (9,476), Lockheed Martin (7,000), Westgate Resorts (6,500), SeaWorld (6,000), Darden Restaurants (5,200), and Siemens (4,400).

In previous issues, we have discussed a covariance analysis that was first published in the Spring 2007 *Wharton Real Estate Review* and regularly updated. The analysis examines how various economic indicators behave in individual metropolitan areas based on national economic changes. For each MSA, we estimated an equation, which summarizes how a 100-basis point (bp) change in the national variable affects the local indicator. The equation consists of a constant ("alpha") for each market and a "beta," which is a multiplier applied to the national percent change in employment. The alpha indicates MSA growth that is independent of national growth. If there is no national job growth, alpha is the expected annual percentage change in MSA employment. The beta for the U.S. as a whole is, by definition, equal to one. An MSA with a beta of one registers (on average) an increase of 100 bps in employment growth plus alpha when national employment rises by 100 bps. A beta that is less than one indicates that the MSA does not boom (or bust) to as great an extent (around its trend) as the national economy, while a beta of greater than one indicates that such an MSA experiences swings of greater magnitude than the percentage changes at the national level.

With a very high employment beta of 1.73, the MSA responds 73% more than national employment changes. The MSA also has a high alpha of 1.04, indicating positive employment growth of 1.04% even when U.S. job growth is zero. Orlando has a break-even point of -0.60%, indicating that annual U.S. employment growth can be as low as -0.60%, and the Orlando metro will still have positive employment growth. Its R-squared statistic of 0.85 indicates that the forecasting model for Orlando employment growth explains future job growth with 85% "fit." This relatively high fit reflects the importance of the tourism sector for the MSA.

Our model projects that the Orlando MSA would lose 8.7% of jobs given that the nation lost 6.3% of its jobs during the recession. In fact, during the Financial Crisis, the Orlando metropolitan area lost 104,000 jobs (9.5%). During the recovery, while U.S. employment has grown 16.1% from the bottom through January 2019, metro employment has increased 25.5% through January 2019, significantly less than our predicted 40.6% growth from the bottom. Through January 2019, the MSA had regained 338,000 (325%) of the jobs lost during the recession versus 240% recovered by the nation through the same period. MSA employment has been on the rise since bottoming in December 2009, reaching an all-time high of just over 1.3 million jobs in January 2019.



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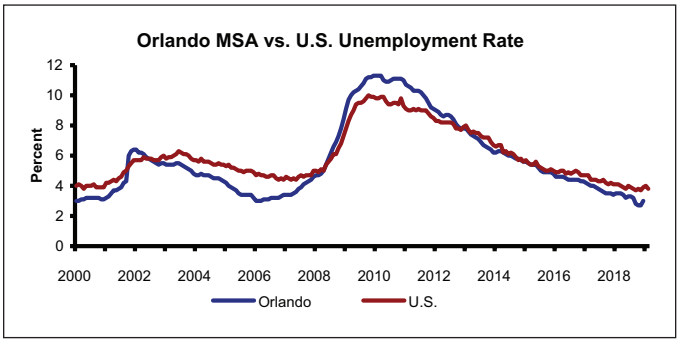

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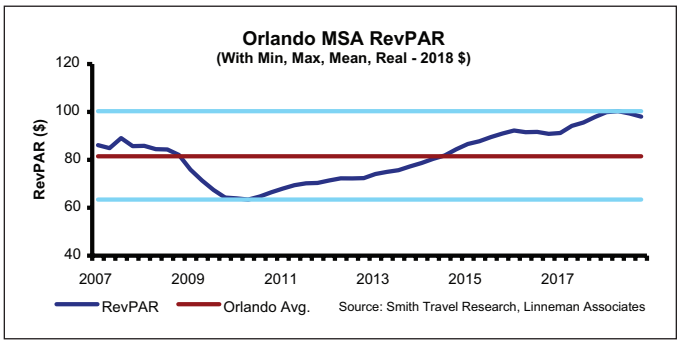

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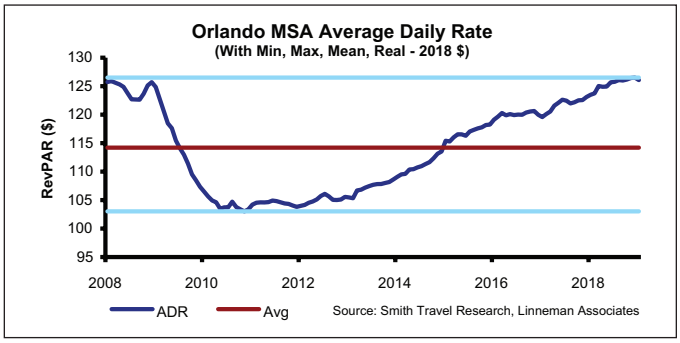

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The MSA unemployment rate reached a cyclical low of 2.7% in October 2018 and ballooned to 11.3% in December 2009. It has since declined steadily during the recovery, standing at 3.0% in December 2018. The national unemployment rate peaked at 10% in October 2009 and has since declined by 600 basis points to 4.0% through December 2018.

Hotel Market Statistics. The MSA's rolling 12-month occupancy rate was 77.1% in January 2019. This is in comparison to the long-term average (since 2008) of 69.2%, the December 2009 low of 60.7%, and the all-time high of 79.8% in June 2018. In January 2019, the MSA's occupancy rates were the 12th-highest of Smith Travel's Top 25 U.S. markets, while the U.S. average occupancy rate was 66.2%.

Real RevPAR in the MSA stood at $97.24 in January 2019, a decrease of $0.94 per key (96 bps) compared to the same period a year earlier. Current RevPAR is 55.3% and 20% above the recessionary low of $62.61 and the long-term average of $80.89, respectively. Real ADR in the MSA was $126.10 in January 2019, an increase of $2.60 per key (206 bps) over the prior year. By comparison, real U.S. RevPAR and ADR were $85.48 and $129.10, respectively in January 2019.

Visitor Trends. In 2017, a record-breaking 72 million people (65.9 million domestic and 6.5 million international) visited Orlando, up 5% from the previous record set in 2016. And while not yet available, 2018 numbers should surpass 2017. This is also noteworthy for giving Orlando the distinction of being the first U.S. city to surpass the 70 million-visitor threshold, according to Visit Orlando. Orlando's record-setting visitation affirms the city as a leader in the U.S. travel industry," said Roger Dow, president and CEO of the U.S. Travel Association. Tourism is a $60 billion industry in the MSA.

The Orlando International Airport (MCO) is the busiest airport in the state of Florida, conveniently located 20 and 13 miles from Disney and downtown Orlando, respectively. MCO handled a total of 44.6 million passengers with 38.6 million domestic and 5.9 million in international passengers in 2017, making it the eleventh-busiest airport in the U.S. and thirty-ninth worldwide. MCO services 80 domestic and 47 international non-stop flights.

MCO's international service includes 14 destinations in Europe, 31 in Latin America/Caribbean, 15 in Canada, and one in the Middle East. Orlando is also

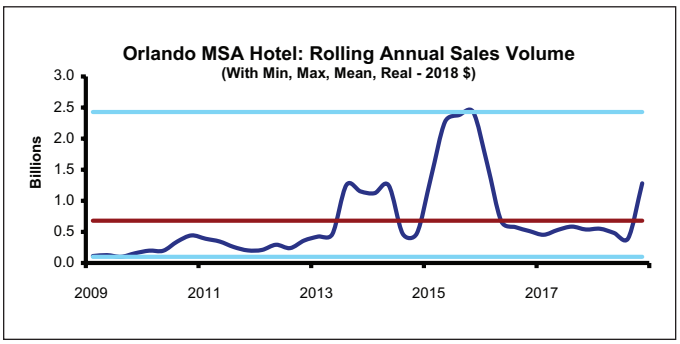
home to the Orlando Sanford International Airport (SFB), which is located 25 and 42 miles from Disney and Downtown Orlando, respectively. SFB handled a total of 2.6 million domestic and 296,000 thousand international passengers in 2017 offering more than 175 non-stop destinations worldwide.

The seven million-square foot Orange County Convention Center hosted about 230 events and welcomed over 1.5 million attendees in 2017. For the third year in a row, Orlando will host Ignite 2019, one of the largest tech conferences sponsored by tech giants Adobe, SAP and Microsoft. Ignite 2019 will be held at the Orange County Convention Center and Hyatt Regency Orlando and will draw a crowd of almost 30,000 attendees. In addition, Orlando has the largest cluster of hotels (150) offering more than five million square feet or more of flexible meeting space.

Investment and Sales. Real 12-month rolling sales volume in the MSA stood at $1.2 billion through December 2018, about 234% higher than September 2018 and 143% a year earlier. The latest real 12-month rolling sales volume is 47% below the 10-year historical high of $2.4 billion but 1,195% and 88% above the recessionary low of $98.8 million in 2009 and the long-term average of $680 million, respectively.

The real (2018 dollars) long-term average price per hotel room in the MSA from 2005 to the fourth quarter of 2018 was $74,304, which compares to $142,300 for the U.S. In the fourth quarter of 2018, the real price per hotel room in the MSA stood at approximately $90,100, 21% above its long-term average since 2005. By comparison, the current real U.S. pricing is about $149,600 per room, which is 5.1% above the national long-term average.

Major buyers of hotel properties over the last two years include: Elliott management ($869.9 million in acquisitions, two properties); Trinity Investments ($869.9 million, two properties); Xenia ($205.5 million, one property); Tishman ($96.5 million, three properties); AD1 GLOBAL ($68.2 million, four properties); Cambridge Landmark ($66.2 million, two properties); and BREIT ($48.4 million, two properties).



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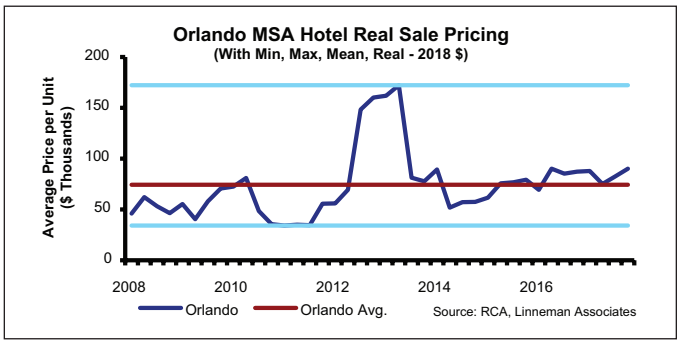

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Major sellers of hotel properties over the past two years include: Blackstone ($903.6 million in dispositions, four properties); Hyatt Hotels ($205.5 million, one property); Dinesh Kalidas ($96.5 million, one property); Interstate Hotels ($66.2 million, two properties); Varde Partners ($66.2 million, two properties); Waramaug Hospitality ($66.2 million, two properties); and New California Hotels ($52.9 million, four properties).

Construction Pipeline. According to Lodging Econometrics, 11 new hotels (2,051 rooms) were completed in the MSA in 2018, a healthy 1.6% growth in existing inventory. Orlando has 18 projects (5,962 rooms) scheduled for delivery in 2019 At the end of the fourth quarter of 2018, there were 31 hotels (4,576 rooms) in the early planning stages, 41 hotels (7,949 rooms) scheduled to break ground in the next 12 months, and 18 hotels (5,962 rooms) under construction. Seven hotels (1,415 rooms) were completed in the first three quarters of 2018, and four more (484 rooms) were completed in the fourth quarter. In aggregate, the construction pipeline consists of 90 hotels (18,487 rooms), accounting for 13.7% of existing inventory and ranking second after Las Vegas out of the top 25 markets.

Opportunities and Challenges. The region is undergoing multiple infrastructure and transportation projects that will positively impact the long-term demand for Orlando hotels. As an example, SunRail, Orlando's commuter rail transit system is pursuing Phase 3 of its planned $77 million-Northern expansion, including 12

additional miles of rail and a new station. However, SunRail is currently weighing options to cover a 50% funding gap for construction.

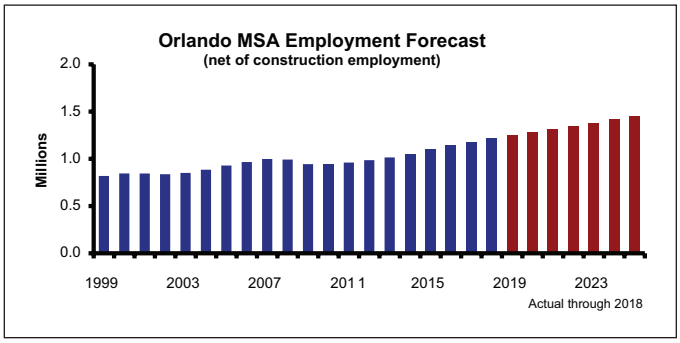
In a separate rail project, the $2.2 billion-Brightline train, which will use the existing Florida East Coast Railway corridor and new track to connect Orlando and Miami, is underway. The Orlando station is near completion, but Phase II of laying more than 170 miles of new track is expected to take three years. Brightline's parent company Virgin Trains USA, a private for-profit rail service, previously received $1.75 billion in bonds through the Florida Development Finance Corp and has requested another $950 million in tax-exempt bonds.

The Florida Department of Transportation's "I-4 Ultimate" project is reconstructing large portions of the region's main thoroughfare. Interstate 4 is getting a 21-mile makeover, from north of State Road 434 in Seminole, through Orlando and to west of Florida's Turnpike in Orange County. The $2.3 billion investment will connect the Gulf of Mexico to the Atlantic Ocean. I-4 Ultimate is a "public-private partnership," expected to generate revenue through tolls. The project began in 2015 and has a planned completion of 2021. The Florida Department of Transportation is also proposing the "I-4 Beyond" project, which will extend the I-4 Ultimate project 20 miles to the north and 20 miles to the south.

Port Canaveral is 50 miles east of Orlando and has been designated as Foreign Trade Zone No. 136. It is the world's only quadramodal foreign trade zone and is also ranked as the second-busiest cruise port in the world. In 2018, the Canaveral Port Authority (CPA) and Carnival Cruise Line inked a 25-year primary term lease with four additional five-year renewal options. They will jointly invest $150 million to develop a 1,800-space parking structure, a two-story 185,000-square feet terminal, wharf updates to accommodate Carnival's new 180-ton, 6,500-passenger ship, and various access improvements, all to be completed by June 2020.

The Orlando International Airport (MCO) is undergoing a $4.2 billion Capital Improvement Program to accommodate increasing passenger and airline demand. MCO's expansion of the south terminal is now under construction and planned for completion in 2021. The new south terminal expansion will connect to the existing terminal facility, which will be a station for the future Brightline train connecting Orlando to South Florida. This will allow up to 10 million more passengers to travel through MCO. A new state permit indicates plans to expand the South Terminal by building a $2.15 billion Terminal C on 282 acres south of the existing terminal. The project is known as the South Terminal C - Phase 1X.

Outlook. Our proprietary employment forecasts are net of construction jobs, due to the volatility and short-term nature of that sector. We forecast that the Orlando metropolitan area will add roughly 27,000 non-construction jobs per year in 2019-2023. The 12-month rolling average hotel occupancy rate stood at 77.5% in December 2018. We project that the Orlando hotel occupancy rate will be 77.9%, 79.2%, 80.9%, and 82.7% by year-end 2019-2022 respectively, with demand growth surpassing significant new supply.



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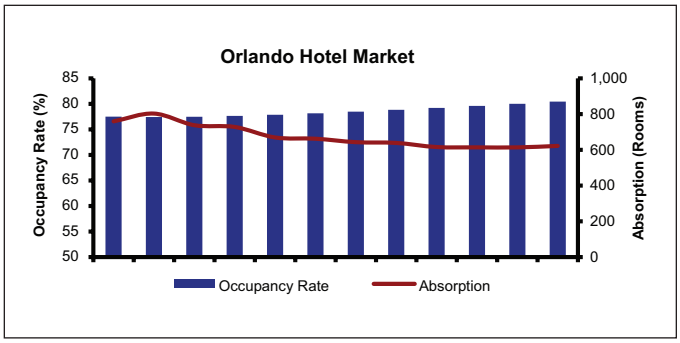

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