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Phocuswright Special Series

COVID-19 HOTEL FORECAST: CHICAGO

June 2020

In cooperation with

LODGIQ

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Introduction

The global hospitality industry has been ravaged by COVID-19, a classic example of a black swan event. While many are looking backwards to compare the current market environment with the post-9/11 or 2008 Great Recession periods, Phocuswright prefers to look forward – trying to address the tough questions weighing on our collective minds.

Over the coming months, by teaming up with the data science team at LodgIQ, Phocuswright will evaluate a broad swath of hotel-related and other data across a variety of key metropolitan areas. Our key objectives are to model the:

- Level of disruption
- Duration of disruption
- Shape of the recovery curve

The goal is to understand the similarities and differences in hotel market dynamics between destinations. This is especially relevant, as some markets may have yet to peak in terms of the level of infections, while others are seeing active coronavirus case counts decline.

"My interest is in the future because I am going to spend the rest of my life there."

C.F. Kettering

Travel's multimodal nature and interdependency of origin and destination markets within different sectors adds necessary, but not always welcome complexity to the model. Therefore, this forecast is probabilistic, with a high degree of uncertainty. The spread of the virus is path-dependent, non-linear and impacted by measures such as local social distancing and broader geographic quarantines.

The forecasting model will be continually evaluated and refined as more data is collected, stronger signals identified, and new outcomes revealed. Understanding the impact of the virus and the path to recovery across major global markets will help the industry regain solid footing through more informed decision making. The simplest way to understand the impact of the virus is to observe the change to the forecast as the spread progresses.

Chicago

"Hog Butcher for the World, Tool Maker, Stacker of Wheat, Player with Railroads and the Nation's Freight Handler; Stormy, husky, brawling, City of the Big Shoulders," wrote poet Carl Sandburg in 1914. If he had lived in 2020, he might have added "home of the largest convention center in the country."

With its 2.6 million square feet of empty meeting and exhibit space, Chicago's McCormick Place is currently far from experiencing the activity levels described by Sandburg.

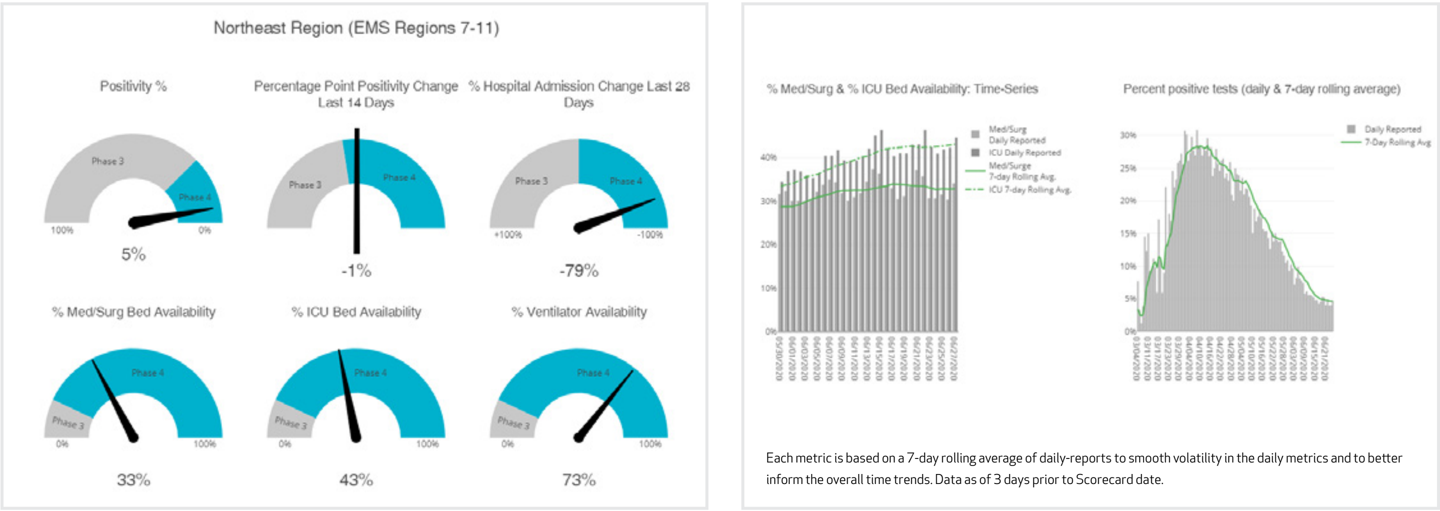
As the third largest city in the country, Chicago experienced its first coronavirus case in late January and locked down with a shelter-in-place order during the third week of March, when Illinois was approaching a cumulative total of 600 total cases and five deaths. 90 days later, Illinois is now recording 600 new cases and 43 deaths per day, based on the latest 7-day moving average.

In a vivid illustration of how community and political perspectives on the virus have changed, Illinois Governor J.B. Pritzker (a last name not unfamiliar to the hotel industry, due to his family's founding of the Hyatt hotel chain) has now moved the state into the Phase 4 "revitalization" segment of its reopening plan. Phase 4 allows group gatherings of up to 50 people, restaurants to seat parties of up to 10 with a minimum of six feet between tables, and standing areas (such as bars) filling to a maximum of 25% of capacity.

A tangible example of Chicago's success in flattening the curve of the virus is the June 24 announcement by the University of Chicago Medical Center that it is no longer dedicating units or floors to care solely for COVID-19 patients. In mid-April, there were 140 COVID-19 patients occupying the hospital's 146 ICU beds. Today, the number of COVID-19 ICU patients has fallen to 18.

The state should be commended for creating a plan, clearly defining the metrics required to be met in order to advance to the next phase, and continually communicating progress by publishing a robust dashboard.

Figure 1:
Illinois Department of Public Health – Regional Hospital Resources Metrics & Benchmarks



As encouraging as those actions and outcomes may be, they somewhat belie the severity of the pandemic's impact. While Chicago and Cook County survived the first wave of the pandemic, there was a significant human cost, with over 1,700 cases and 86 deaths per 100,000 in population. Those figures still reflect a much better outcome than New York City's first wave, which produced 2,600 cases and 262 deaths per 100,000.

It cannot be stressed enough that the impact of this global pandemic is highly localized in nature. The same day as the University of Chicago Medical Center announcement, the Texas Medical Center in Houston (the fourth largest U.S. city) stated that its 1,330 ICU beds were at 97% capacity, with 27% of those beds occupied with COVID-19 patients.

While it is admirable that entire state of Illinois has flattened its 7-day moving average for new cases to approximately 600 per day, Houston provides a cautionary tale. Houston's home of Harris County alone is now approaching 1,000 cases per day. Reopening too early or lacking compliance in wearing masks, social distancing, testing and/or contact tracing processes, can quickly reverse progress in areas where the vast majority have yet to be exposed to an unrelenting virus.

Optimism for a Chicago recovery is well founded, with Illinois currently trending far better than most other states. However, to maintain this trajectory, testing and contact tracing will be essential to control inevitable isolated outbreaks as the local economy reopens.

2020

January

S	M	T	W	T	F	S
			1	2	3	4
5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30	31	

March

S	M	T	W	T	F	S
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

May

S	M	T	W	T	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

June

S	M	T	W	T	F	S
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30				

Chicago Timeline

Following are the major milestones in the fight against coronavirus by Chicago, Cook County and the state of Illinois:

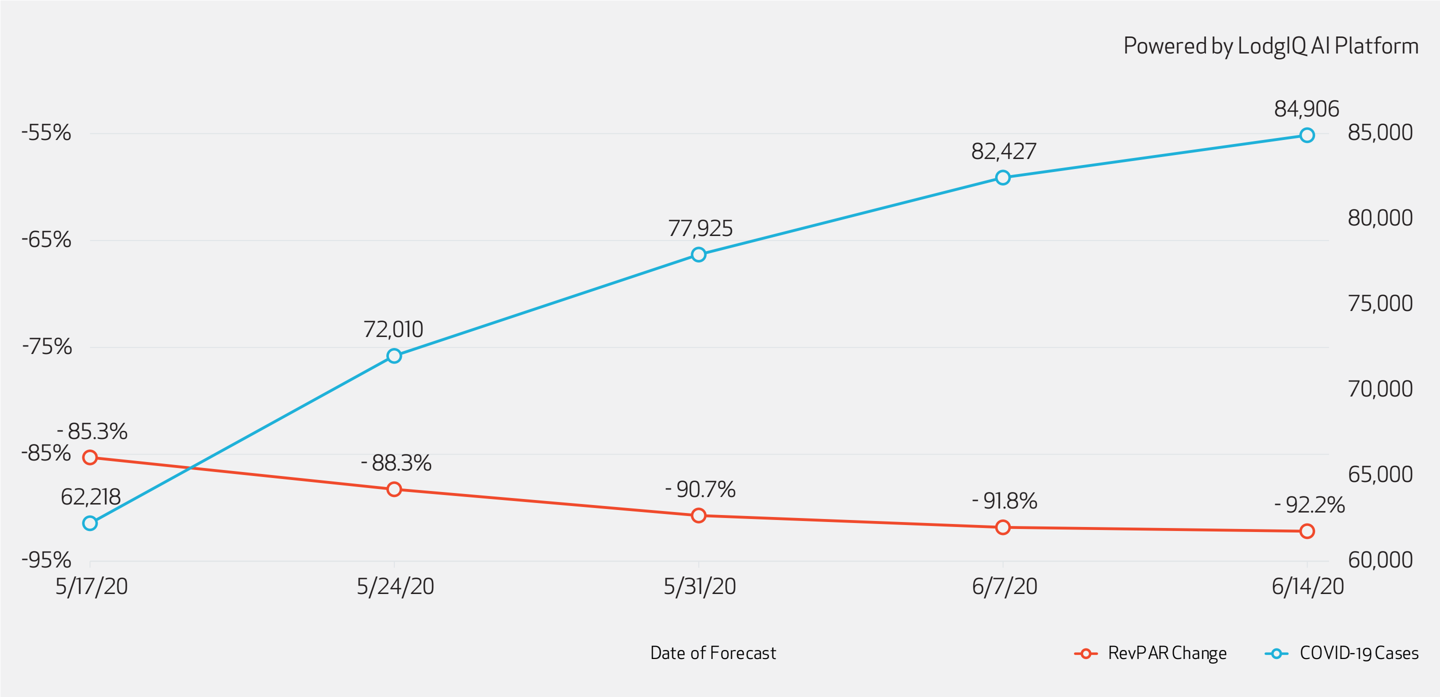
- **January 24** – A Chicago woman in her 60s, returning from Wuhan, China is the second confirmed U.S. case of coronavirus.
- **January 30** – First person-to-person transmission reported in Chicago and the U.S.
- **March 4** – The first large group events planned for McCormick Place in March are canceled.
- **March 9** – Illinois Governor J.B. Pritzker issues Disaster Proclamation as total cases grow to 11.
- **March 12** – Governor Pritzker orders the shutdown of public events with more than 1,000 people. The following day, all public and private schools are ordered closed by March 17.
- **March 16** – Bars and restaurants statewide are closed for on-site consumption. A retired nurse becomes the first Illinois resident to die from the disease.
- **March 21** – Strict statewide stay-at-home order issued, excepting workplaces deemed essential and forbidding gatherings of more than 10 people. (Phase 1 – Rapid Spread)
- **May 1** – Non-essential retail stores open for curbside pickup and delivery. Outdoor activities permitted with social distancing. (Phase 2 – Flattening)
- **May 5** – Governor Pritzker formally presents a five-phase regional "Restore Illinois" plan, categorizing the state into five geographic regions and outlining metric-based criteria for reopening.
- **May 7** – Mayor Lori Lightfoot announces "five-star" plan for Chicago, with stricter restrictions and higher benchmarks than the state plan for easing stay-at-home rules.
- **June 3** – Chicago moves to Phase 3 (Recovery) of Restore Illinois plan. The stay-at-home order is lifted, but gatherings are still limited to no more than 10 people.
- **June 24** – All regions of Illinois move to Phase 4 (Revitalization) of Restore Illinois plan.

Like other cities that introduced strict lockdowns, the negative impact on revenue per available room (RevPAR) has been severe, especially for city center properties. Also, due to Chicago's density and significant reliance on mass transit for access to the downtown core, risks are perceived as greater for employees, urban residents and hotel guests alike.

The top 25 markets in the U.S. continue to lag the national average when it comes to occupancy, putting downward pressure on RevPAR. The headwinds were even stronger in Chicago, as it also lagged the average for the top 25 U.S. markets. The downtown hotel core fared even more poorly, despite a number of properties remaining closed.

As with virtually all cities we have evaluated to date, the forecast model continued to decrease its June forecast as the month progressed, although the decline flattened considerably as Chicago's fundamentals improved – proven by the decision to move to the next phase of reopening as the month closes out.

Figure 2:
Forecast YoY RevPAR Decline – June 2020



Many iconic Chicago hotels, especially on the upscale-to-luxury end of the spectrum, remain temporarily closed for bookings. These include The Four Seasons, The Peninsula, The Waldorf-Astoria, The Ritz-Carlton, The Park Hyatt, The Langham, The Marriott Marquis, The Hilton Palmer House, The Omni, Virgin Chicago… We'll stop there – this is getting too painful.

In the absence of luxury hotel inventory that would normally drive up the average daily rate (ADR), the ADR forecast for the city is structurally lowered due to a shift in chain scale occupancy distribution. One other key consideration is that, as these hotels reopen, the city ADR would be expected to rise. However, the additional inventory will likely depress the growth rates for occupancy and RevPAR, as the denominator for those calculations – the number of available rooms – increases.

June 2020 - Declines

~ 87%	41%	~92%
June YoY Occupancy loss	June YoY ADR decline	June YoY RevPAR loss

Chicago's June occupancy is projected by the model to come in at only 10.4% for the month – off 87% compared to June 2019. The corresponding year-over-year (YoY) RevPAR decline is projected at 92.2%.

Progressively, the RevPAR disruption model runs since May have continued to erode. One may note that the latest model run on June 14 showed a greater degradation for July than for June (-18 points, versus -7 points from the May 17 forecast), with some improvement in August to -10 points. This was due to the estimated timing of the move to Phase 4. With the most recent announcement this week, one could assume July occupancy might be somewhat improved compared to the forecast due to this new information.

Phase 4 will also allow for the opening of Chicago's major tourist demand generators: its zoo, museums, etc. in the downtown core. However, these facilities will be limiting access, so that may temper some pent-up demand for those who are comfortable to begin venturing out – especially with family members.

Figure 3:
Change in Forecast YoY RevPAR Comparing May 17, 2020 to June 14, 2020 Forecast

RevPAR	Date of Forecast	
YoY Change	May 17	June 14
June 2020	-85.3%	-92.2%
July 2020	-66.7%	-84.7%
August 2020	-58.0%	-67.6%

Chicago's 90-day YoY RevPAR disruption forecast shows significant improvement from -92.2% in June to -67.6% in August. This reflects solid progress, especially considering an inventory basis that is expected to grow over the same timeframe.

The city had made notable preparations to support its healthcare system beginning in March – for example, converting McCormick Place into a 3,000-bed overflow hospital, if necessary. Fortunately, the local healthcare system was not overrun, so the space was never needed. As a result of this success, there was less need to house essential workers or medical staff during the peak of the outbreak or for an extended period following it. The only downside was that hoteliers were not able to source contract room business from this segment, like properties in some other cities.

Figure 4:
Forecast YoY RevPAR Decline – July 2020

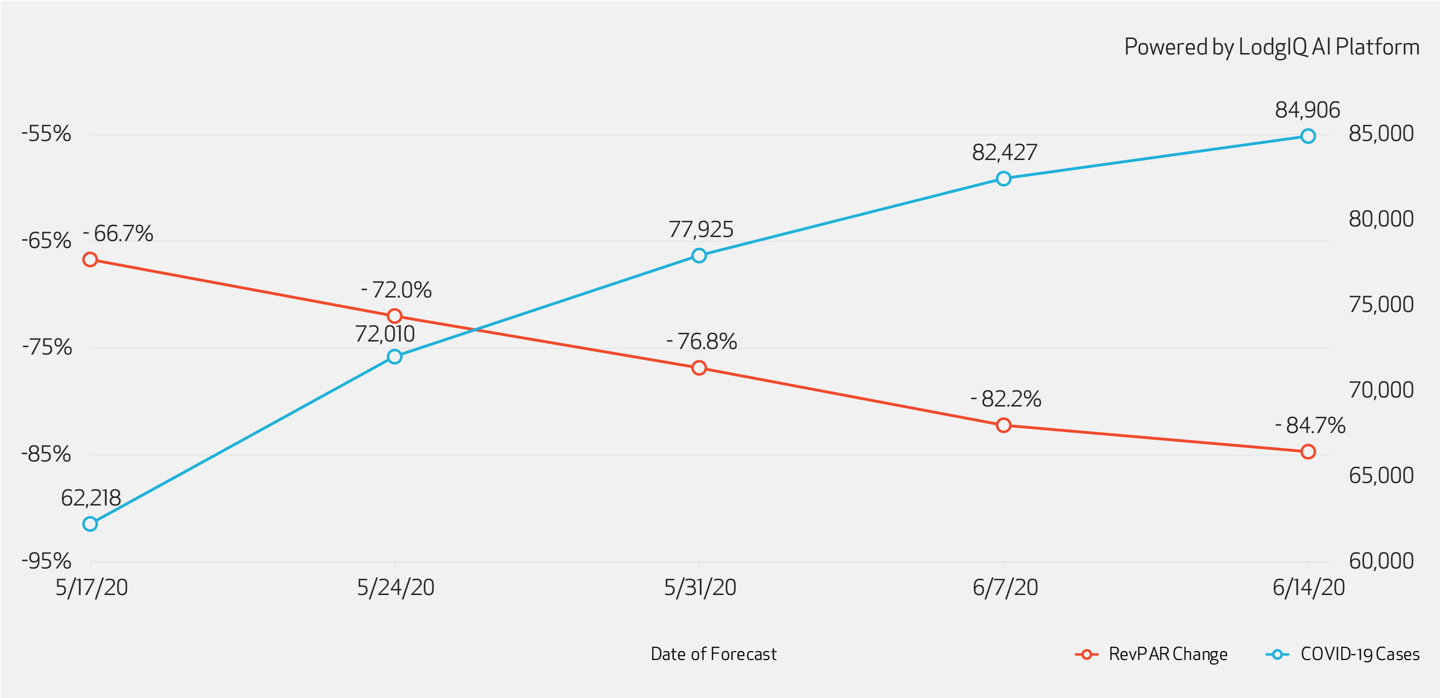
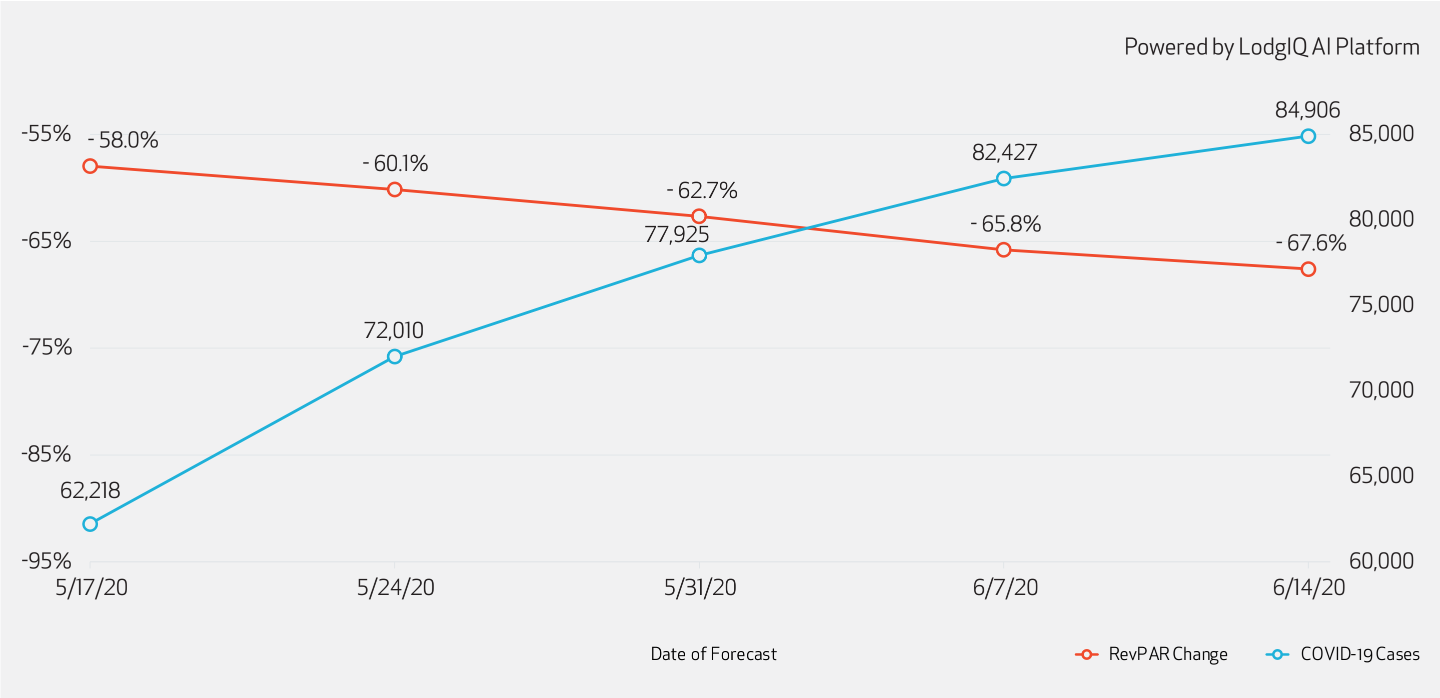


Figure 5:
Forecast YoY RevPAR Decline – August 2020



The model projects June hotel occupancy for the Chicago market to be 10.4%, increasing by 6.7 points (64% growth) to 17.1% in July and adding an additional 13.7 points (80% growth) to 30.8% for August.

Again, a growing occupancy rate as temporary closings expire and return rooms to inventory is a very good sign. One can also observe the improvement in the model's interpretation of market fundamentals by seeing the differences between the May 17 and June 14 forecasts drop 13.5-points for the July forecast, but less than half that much in August. With the earlier than expected move to Phase 4, there is some hope that demand will be even higher for August. The big unknown is how that demand will be impacted by the supply increase for the luxury chain scales.

As luxury hotels have lagged the recovery of lower-tier properties, it will be interesting to see if any of the temporary closings are extended. The same will apply to the large convention-oriented properties, many of which are operating with a significant number of rooms shut down – lowering their inventory basis as well.

Figure 6:
Change in Forecast Occupancy Comparing May 17, 2020 to June 14, 2020 Forecast

Occupancy	Date of Forecast	
	May 17	June 14
June	16.5%	10.4%
July	30.6%	17.1%
August	36.8%	30.8%

In the latest STR statistics available from April, Chicago's group occupancy percentage was 4%. For those startled by that figure, only two of the nation's top 25 markets (New Orleans and New York) had higher group occupancy. It may be some solace for Chicago to learn that the Las Vegas Convention and Visitors Authority reported group convention attendance of ZERO in April 2020.

Downtown hotels traditionally rely on group business for 50% of their occupancy, so hoteliers should not expect a quick return of large citywide conventions filling McCormick Place (the largest convention center in the U.S. with 2.6 million square feet of meeting and exhibition space).

Phase 4's limitations on indoor gatherings of no more than 50 people and 50% of capacity, with outdoor gatherings limited to 100 or 20% of capacity, are not conducive to quickly filling empty hotel rooms with groups.

The Illinois government has clearly expressed that "the only way Phase 5 will begin is with a vaccine, or a widely available and highly effective treatment, or with the elimination of any new cases over a sustained period." The group market in Chicago, therefore, may take a while to recover.

This raises the additional issue of how hotel owners will deal with the revenue shortfall.

Reducing staff to match lower occupancies is one method, but the looming challenge is how to handle debt payments. Trepp reported that the delinquency rate on loans packaged into commercial mortgage-backed securities (CMBS) for local Chicago hotels jumped to 33.5% in May – up from only 2.5% in April. Preliminary June figures indicate that the figure will only grow in June.

For some context, the battering of the retail industry by COVID-19 has been widely publicized. When it comes to local Chicago area retail CMBS loans, their delinquency rate only rose to 13.4% in May, an increase from 7.8% in April. Hotel delinquencies spiking from 1/3 to 2.5x the retail delinquency level is concerning, to put it mildly.

Lenders are currently allowing borrowers to draw from reserve accounts to cover mortgage payments. But the longer demand remains suppressed by the pandemic, the higher the increase in potential for foreclosures.

The good news is that in a low interest rate environment, there may be an opportunity for some deals to be renegotiated. The bad news is that some owners, pressed to generate cash to satisfy lenders, may desperately drop rates to incent a short-term share shift from competitors. Such a practice has historically caused hotel market valleys to deepen and recoveries to extend.

At the present time, Chicago should be commended for limiting the impact of the virus from a public health perspective. Now the challenge will be to walk the fine line where beneficial public health outcomes are maintained, while economic activity recovers.

Hopefully, the metrics-based approach and open communication policy for public health can be extended and aligned with the business community to help the "City of the Big Shoulders" referenced by Sandburg's poem carry the burden of the coronavirus crisis.

Figure 7:
Forecast Occupancy – June 2020

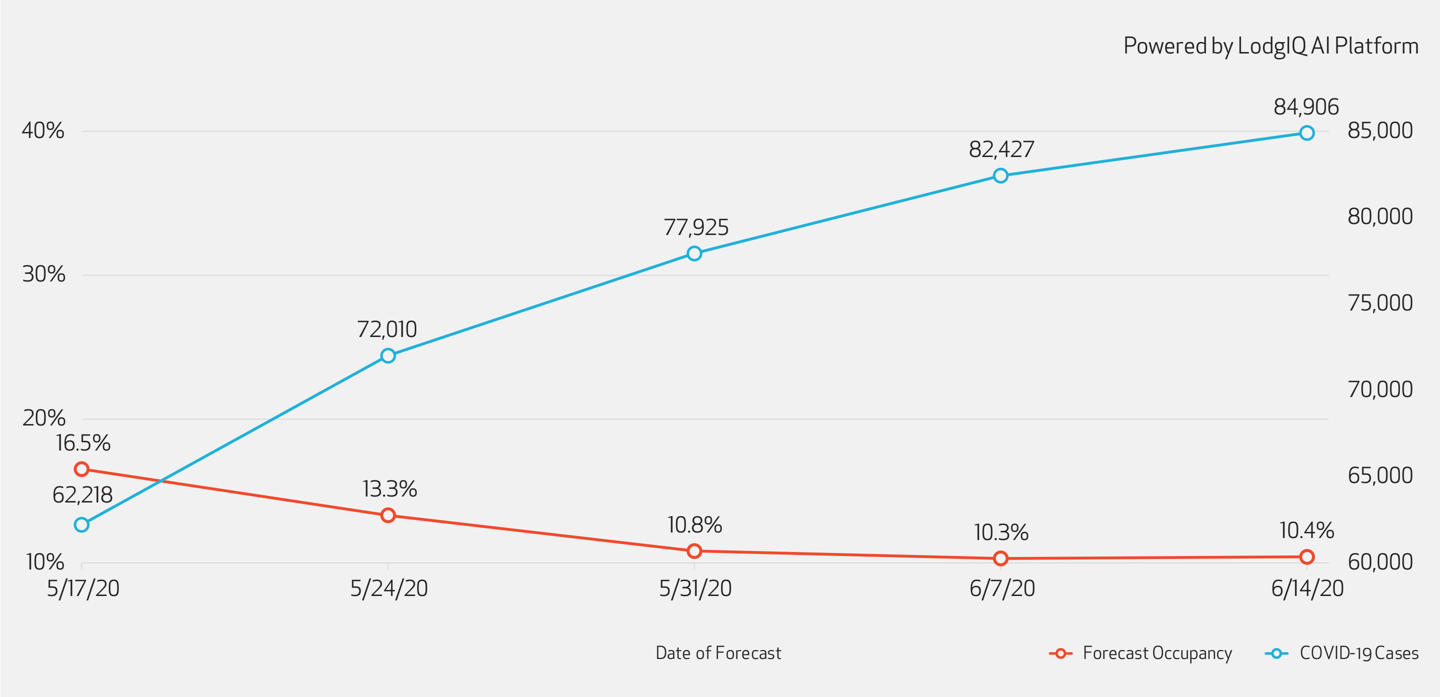


Figure 8:
Forecast Occupancy – July 2020

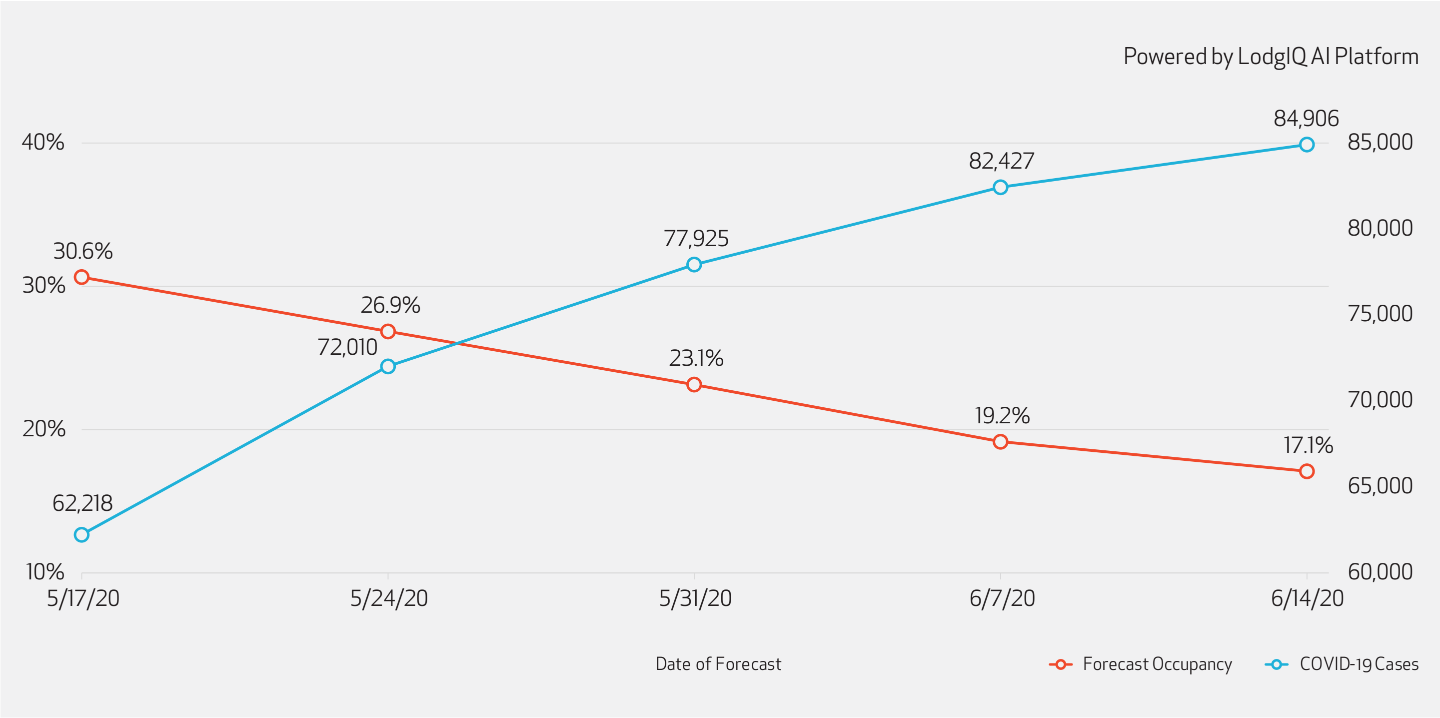
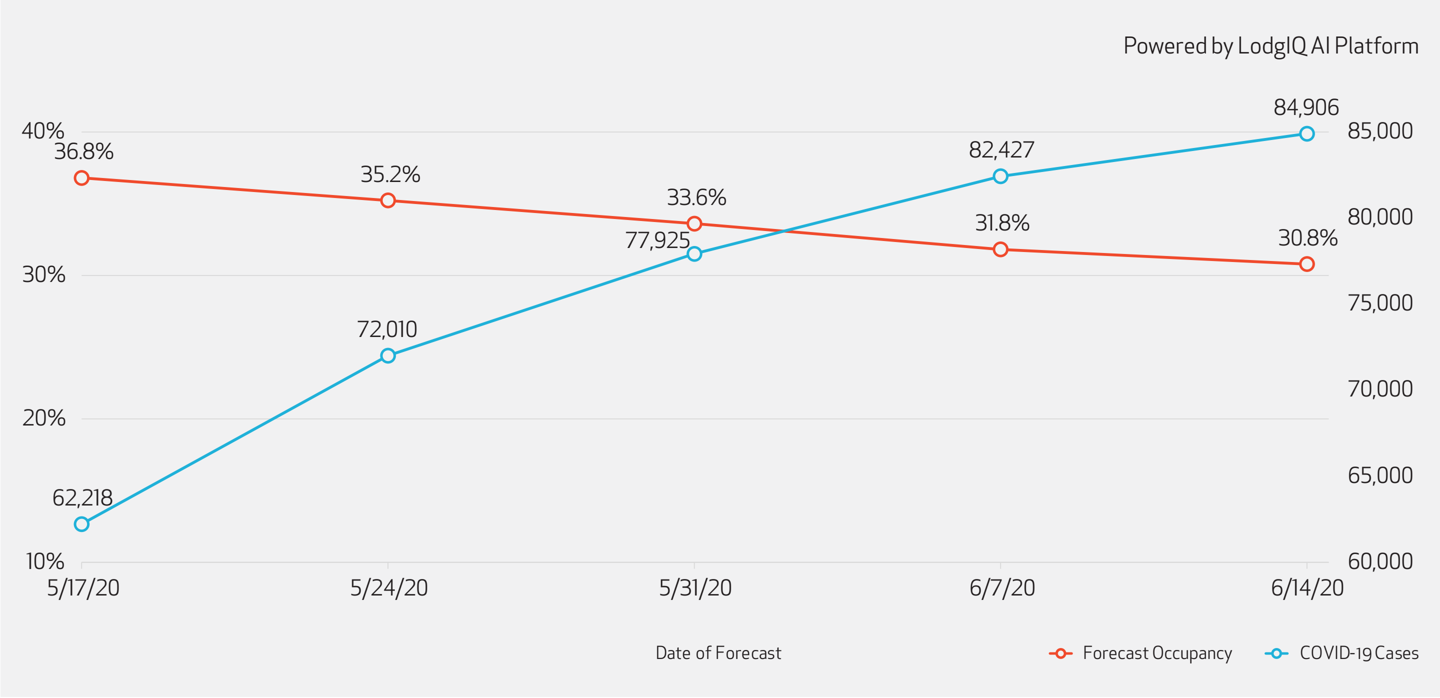


Figure 9:
Forecast Occupancy – August 2020



About the Hotel Forecast Model

We continue to identify leading indicators that signal likely pricing strategies as markets decline and recover. ADRs can be misleading in a market experiencing severe supply contraction, as the mix of available rooms may shift to offer higher ratios of economy or luxury properties. Logically, during significant periods of disruption, travelers may become more price-sensitive, but anxious hoteliers engaging in rate wars may suppress pricing not only for their competitive set, but for the destination overall.

It is also important to remember that as the time horizon expands, greater variation may be expected. As more global markets recover from peak virus caseloads, their outcomes will be captured, with the model continually refined to enhance its precision.

This crisis will pass, but until then, the most urgent questions focus on the depth of the decline, the length of its duration and how the recovery will manifest itself. As the analysis continues, the following factors will be closely monitored to identify early signs of recovery:

- Active cases and mortality rates
- Test counts per million
- Government travel policies
- Stock market and volatility indexes
- Unemployment rates

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Phocuswright is the travel industry research authority on how travelers, suppliers and intermediaries connect. Independent, rigorous and unbiased, Phocuswright fosters smart strategic planning, tactical decision-making and organizational effectiveness.

To complement its primary research in North and Latin America, Europe and Asia, Phocuswright produces several high-profile conferences in the United States, Europe and Asia Pacific. Industry leaders and company analysts bring this intelligence to life by debating issues, sharing ideas and defining the ever-evolving reality of travel commerce.

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The company is headquartered in the United States with Europe and Asia Pacific operations and local analysts on five continents.

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About LodgIQ

LodgIQ uses state of the art BigData Analytics and AI / Machine Learning algorithms to forecast demand and price hotel rooms. LodgIQ is led by a team of experienced hospitality technologists, data scientists and engineers. Seed funded by Highgate Ventures, LodgIQ is re-imagining revenue management with predictive and prescriptive analytics methods. Our flagship product – LodgIQ RM is used by hotels across the globe, day-in and day-out to understand demand and optimize revenue.

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