**Point of View** is an occasional *PREA Quarterly* column offering the opinions of leading individuals in real estate. The *PREA Quarterly* welcomes opinions from PREA members on significant issues affecting our industry.

# Why Travel and Leisure? Investing in the Unforgettable

**Steven Siegel**
KSL Capital Partners

## Introduction

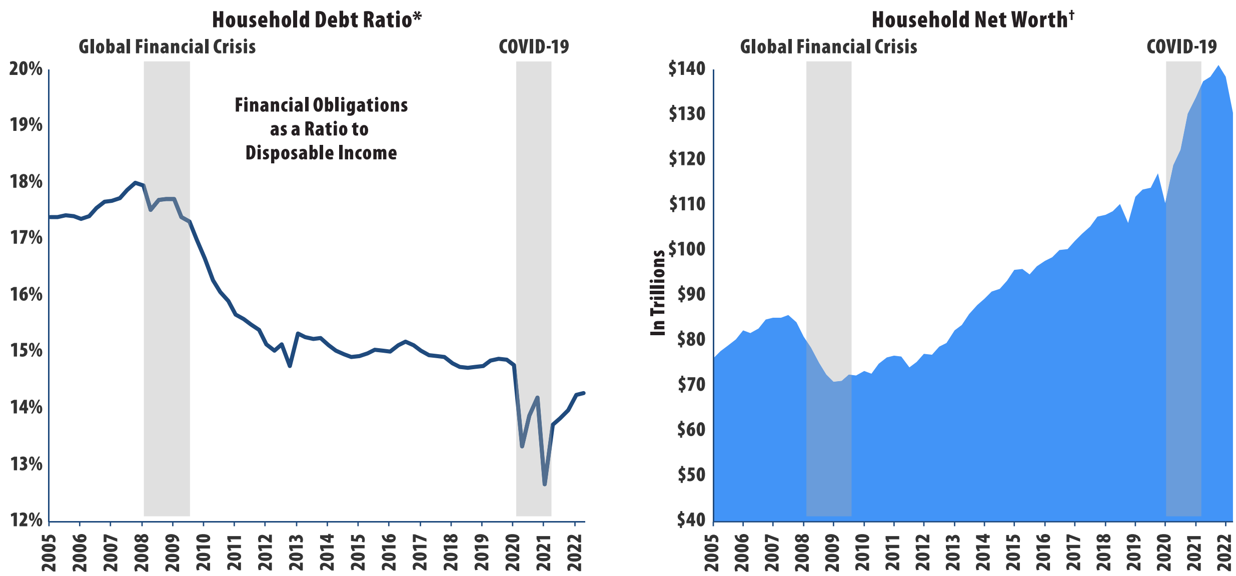
Predominately underpinned by real estate, travel and leisure is a key component of the global economy. Consumers are spending increasing amounts on active, experience-based recreation and vacations. In 2019 (the last full year prior to the pandemic), US travel and tourism spending was $1.2 trillion, according to the US Travel Association, and it accounted for 10.2% of worldwide gross domestic product (GDP). Although travel and leisure spending contracted significantly during the pandemic, the World Travel and Tourism Council (WTTC) forecast it would return to near 2019 levels in 2022.[1] Despite the current macroeconomic uncertainty, consumers today are in a much stronger financial position than in prior recessionary periods, such as the global financial crisis, which is aiding the trend (Exhibits 1 and 2).

The rapid rise of the middle class in emerging economies, a trend toward investing in experiences over material goods, and greater accessibility to booking channels and information via new technologies are expected to continue to drive travel and leisure spending in both the US and worldwide. Indeed, since 2000, US consumers have spent increasing amounts of their wallets on experiences (travel

1. 2022 actual data will not be available until later in 2023.*

**Exhibit 1: Household Balance Sheets Remain Strong**

Household debt has fallen 18% since the start of 2005. Household net worth has grown by 71% over the same time period.

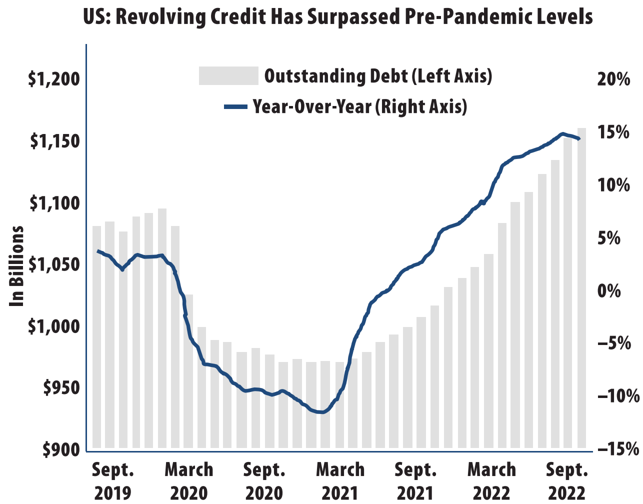


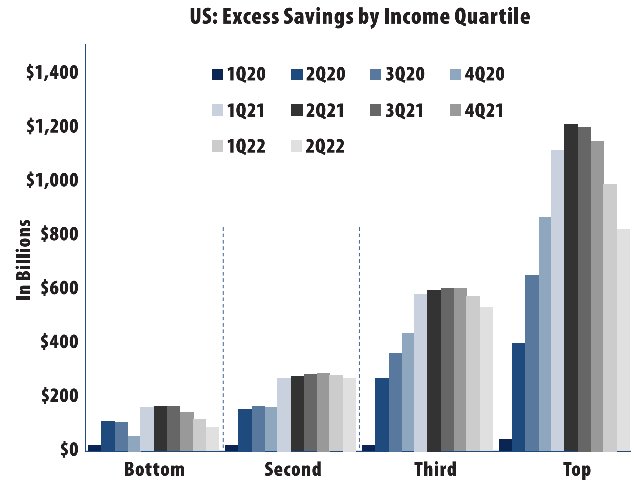

**Sources:** Federal Reserve, NBER

*Quarterly data through 2Q2022. Financial obligations ratio is the ratio of household debt payments and payments such as rent and auto leases to disposable income.

†In 2020 dollars. Quarterly data through 2Q2022. Net worth of households and nonprofit organizations. Measures assets, such as housing and financial assets, minus liabilities.

**Exhibit 2: KSL's Target Consumer Is Maintaining Excess Savings**




**Source:** Oxford Economics/Haver Analytics and Tourism Economics, an Oxford Economics Company

and leisure) versus material goods, with travel and leisure spending increasing approximately 140% compared with only about 70% for material goods.[2]

## The Importance of Travel and Leisure

Based on recent data published by the WTTC, travel and tourism in 2021 accounted for 6.1% of worldwide GDP, or about 60% of its contribution prior to the beginning of the COVID-19 pandemic. In 2021, travel and tourism accounted for approximately 9% of jobs worldwide. In the US alone, travel and tourism accounted for 5.5% of GDP in 2021 and nearly 7% of total jobs despite the impacts of the pandemic, according to the WTTC. Prior to the pandemic, travel and leisure was the fastest-growing segment of the US economy, accounting for 11% of total consumer spending, with its growth outpacing that of health care, financial services, education, and housing (Exhibit 3).

The WTTC forecasts that travel and leisure's contribution to GDP will grow at a 5.8% compound annual growth rate (CAGR) over the coming decade and create 126 million new jobs; global GDP is forecast to grow at a 2.7% CAGR.

## The "Mass Affluent" Consumer

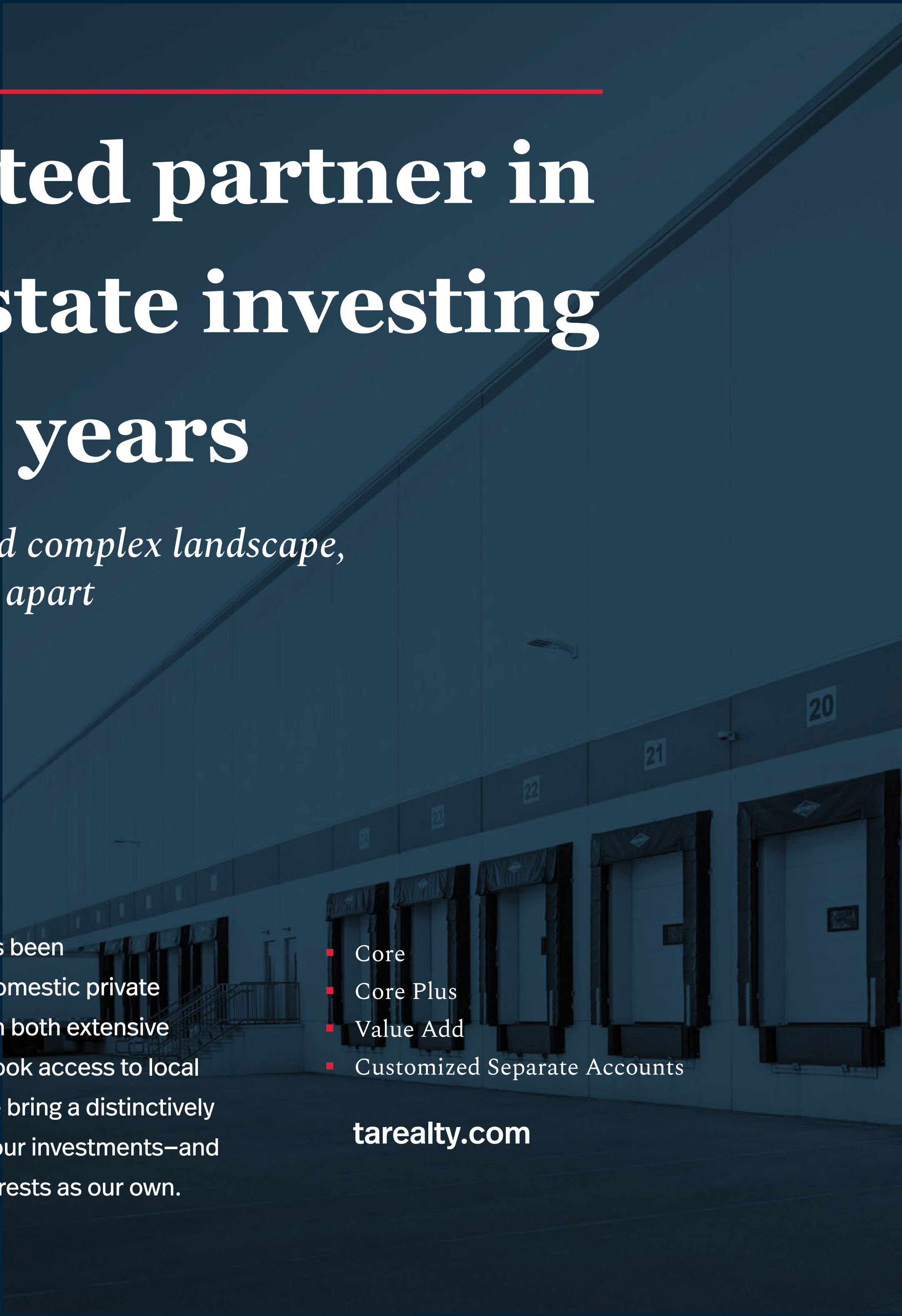
Core to KSL Capital's investment thesis is investing behind the "mass affluent" consumer, defined as having a household income of more than $100,000 per year and typically with a college education, who is generally less sensitive to economic cycles.[3] The desire for recreation, health, wellness, and time with friends and family is integral to the lifestyle of this consumer, and travel and leisure businesses, such as hospitality, clubs, and fitness and recreation businesses, help facilitate this lifestyle.

As the global economy grows, wealth creation will increase the number of mass affluent households. Credit Suisse estimates this cohort will increase globally by about 20% by 2026. Western Europe, the US, and China will likely be the biggest benefactors of the growing global population of mass affluent travelers. In KSL's view, based on demographic trends and a developing middle class in emerging economies, long-term demand for travel and leisure is resilient and expanding.

The desire to travel, recreate, and seek out opportunities for health and wellness generally remains strong regardless of the economic climate.

2. Bureau of Economic Analysis; Personal Consumption Expenditures by Function; material goods defined as personal spend on clothing, footwear, household furnishings, motor vehicles, technology, sports and recreation equipment, personal care and beauty, jewelry, watches, and other personal items.

3. The definition of "mass affluent" varies by income across the globe. To adjust varying costs of living, KSL utilizes $105,000 of household income for comparative purposes to the US definition of mass affluent.



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When disruption does occur, it is generally brief and the recovery is rapid. Although the investment market for travel and leisure is cyclical, recessionary periods historically have been followed by periods of strong growth leading to new peak performance levels. The period following the global financial crisis was one of prolonged growth in most travel and leisure businesses. In the US, for example, revenue per available room (revPAR), a common hospitality performance metric, demonstrated positive growth for 101 consecutive months following the global financial crisis.[4]

## Impact of Inflation

Travel and leisure has historically outpaced the rate of inflation because of its ability to quickly reprice a given offering. For example, the net operating income (NOI) of US resorts has grown at about twice the inflation rate, with this premium maintained during high inflation periods (e.g., 1972–1982). Across the US during this period, resort NOI increased more than eight times, with US resorts' NOI margins increasing by more than 1,000 basis points, according to CBRE (Exhibit 4).

## Market Sectors

### Hospitality

*Includes lodging, restaurants, management companies, resort-based recreation, and meetings.*

**Market Trends:** COVID-19 had a material impact on the hospitality sector. From 2019 to 2020, total US hotel room night demand fell by approximately 36%, according to Smith Travel Research. However, as vaccines became more readily available, demand rebounded quickly and, in many areas, today exceeds pre-pandemic levels. Leisure spending on hotels, for example, has increased by 5.7% over 2019 pre-pandemic levels.[5] Despite the challenging investment climate, KSL believes there is ample opportunity to make successful investments in hospitality.

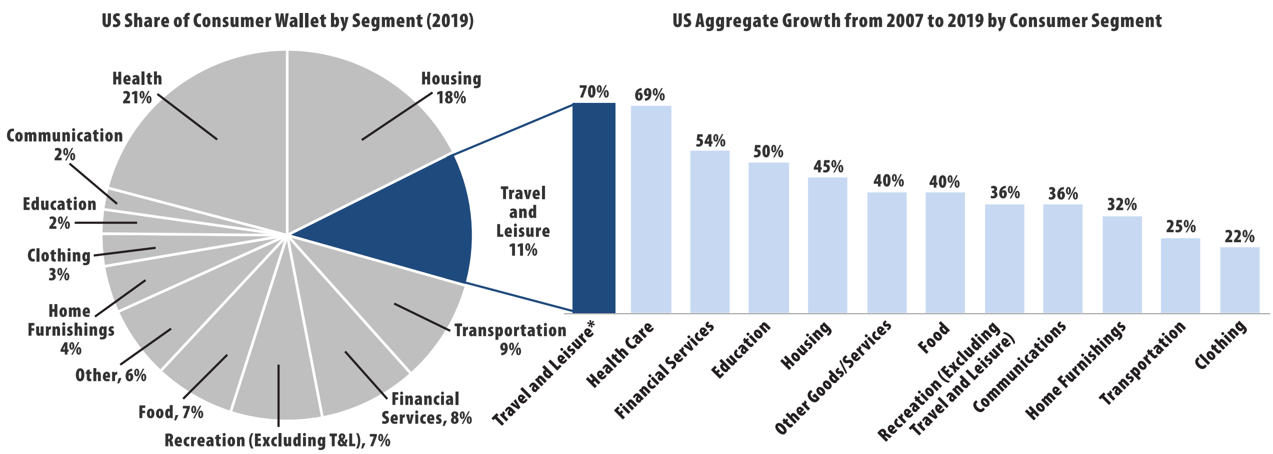
### Recreation

*Includes public golf courses; ski resorts; spas; cruise lines; gaming; leisure retail; marinas; franchised health, beauty, and wellness; and ticketed park attractions (such as water parks and theme parks).*

**Market Trends:** Recreation businesses have demonstrated a long-term stability in levels of participation, reflecting recreation's core place in consumers' lifestyles. In times of weaker economic growth, these businesses tend to be more resilient in the face of economic forces because they are less reliant on corporate demand as a portion of

4. RevPAR represents total guest room revenue divided by the total number of rooms available.
5. Defined as "Personal Consumer Spending on Hotels" per Bureau of Economic Analysis, U.S. Department of Commerce, as of August 2022.

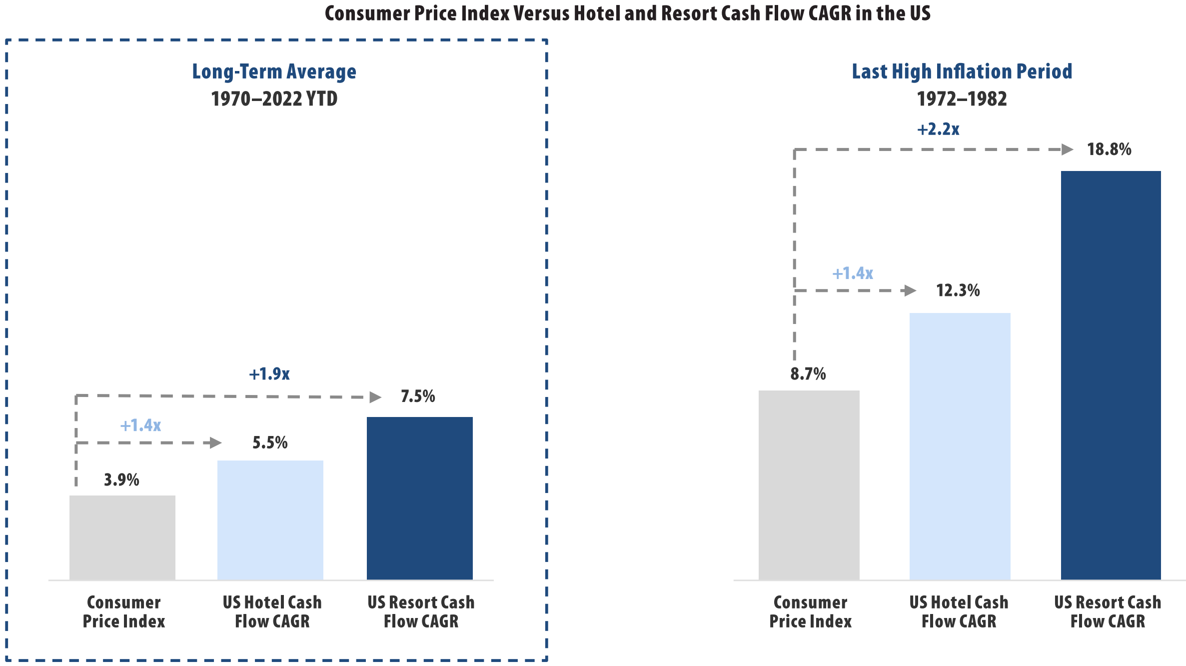
**Exhibit 3: Consumer Spending Across All Sectors**




**Source:** Bureau of Economic Analysis; Personal Consumption Expenditures
*Includes hotel and resort accommodations, packaged tours, membership clubs, experiential activities, food and beverages purchased outside the home, air travel, and foreign travel by US residents.

**Exhibit 4: Outperformance in Inflationary Environments**

Historically, US resort NOIs have grown ~2x the inflation rate, with this premium maintained during high inflation periods (1972–1982).




**Source:** CBRE Trends in the Hotel Industry
**Notes:** Cash flow defined as NOI. YTD 2022 data as of June 30, 2022.

the revenue base and tend to focus more on individual consumers for whom such recreational activities are more central to their lifestyle. In the right markets and targeting the right consumers, these businesses tend to be less cyclical than hospitality businesses.

## Clubs

*Includes health and fitness, private golf and tennis, business, social, lodging and private residence clubs, and other membership programs.*

**Market Trends:** Similar to the recreation segment, clubs are core to consumers' lifestyles and values and have experienced significant long-term growth. They also tend to share the same stability as recreation businesses. For example, from 1993 to 2019, the US health club industry grew at a 7% CAGR to $35 billion in revenues in 2019, according to IHRSA. KSL believes memberships at upscale health, golf, and country clubs have been relatively resilient in recent years, likely buoyed by consumers in upper income brackets and the desire of consumers to remain closer to home and "staycation."

## Development

*Includes residential, condominium, condo-hotel, and fractional development typically associated with leisure amenities.*

**Market Trends:** The pandemic has accelerated the demand for resort real estate as people seek out less-crowded locations and access to outdoor activities made easier by the increasing acceptance of working from home. KSL believes the market for resort real estate in unique and memorable destinations will continue for the foreseeable future. The National Association of Realtors reported that existing second-home sales unit volume grew 16% from 2019 to 2020 and grew 33% in 2021 on a seasonally adjusted annualized basis. KSL believes use-oriented real estate located close to consumers' homes or at well-established resort locations will continue to expand and that demographics support continued long-term growth in second-home ownership.

## A Strategic Approach to Travel and Leisure Investing

The travel and leisure industry is one of the largest contributors to the global economy, and its importance

cannot be overestimated. By identifying these themes and attributes, investors can develop portfolio strategies in anticipation of cyclical shifts. For example, in periods of economic growth, "offensive" subsegments such as hospitality and travel services stand to benefit because they rely on both leisure and corporate demand. The balance of these demand drivers varies by investment, but corporate demand generally is more cyclical, tending to expand more quickly during periods of economic growth and contract more rapidly during periods of economic weakness. As a result, in less-robust times, investors should focus on more "all-weather" leisure investments (e.g., leisure-focused hospitality, recreation, and clubs), which are less reliant on corporate demand and have proved over many years to have relatively stable demand.

Ultimately, each investment is unique and should be reviewed in the context of both subsegment and investment attributes. Depending on the opportunity, investors should not be rigid in their approach to offensive and all-weather investments, depending on the overall economic climate. Periods of distress, for example, often create unique opportunities to acquire offensive investments. Likewise, an offensive asset may be unappealing even in periods of growth if the asset has stabilized and has poor potential for growth. Having the ability to hold, invest in, and reposition properties, in the end, is a question of price and the view of an asset's potential, both in terms of organic growth and attractiveness to the market of future buyers. ■

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*Steven Siegel is a Partner and COO of KSL Capital Partners.*