



## COMPANY UPDATE / ESTIMATE CHANGES / PRICE TARGET CHANGE

### Key Metrics

SOHO - NASDAQ (as of 2/17/2017)	\$7.44
Price Target	\$8.50
52-Week Range	\$4.65 - \$7.35
Shares & Units Outstanding (mm)	16.7
Market Cap. (\$mm)	\$124
3-Mo. Average Daily Volume (000)	66.4
Institutional Ownership	31%
Debt/Total Market Capital (12/16)	67%
Dividend	\$0.40
Dividend Yield	5.4%

### Adjusted FFO Per Share & Unit FY 12/31

	2015	2016	Prior 2017E	Curr. 2017E
1Q	\$0.25	\$0.23	\$0.23	\$0.20
2Q	\$0.52	\$0.39	\$0.47	\$0.43
3Q	\$0.11	\$0.16	\$0.27	\$0.24
4Q	\$0.20	\$0.12	\$0.28	\$0.22
Year	\$1.00	\$0.90	\$1.25	\$1.08
P/FFO	7.4x	8.3x		6.9x

Adjusted FFO excludes the impact of hedging, unrealized gains/losses on warrant derivatives, any increase/decrease in deferred income taxes, losses or gains on the early extinguishment of debt.

Quarterly FFO per share amounts may not add up to annual amounts due to rounding.

Previous numbers have not been restated.

### Revenue (\$mm)

	2015	2016	Prior 2017E	Curr. 2017E
1Q	\$31	\$38	\$38	\$39
2Q	\$37	\$42	\$42	\$42
3Q	\$34	\$37	\$37	\$38
4Q	\$37	\$36	\$40	\$39
Year	\$139	\$153	\$158	\$157

Quarterly revenue amounts may not add up to annual amounts due to rounding.

**Company Description:** SoTHERLY Hotels Inc., Headquartered in Williamsburg, Virginia, is a real estate investment trust (REIT) that owns eleven hotel properties and an interest in a luxury-condo hotel in the mid-Atlantic and Southeastern United States.

## REITs

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## SoTHERLY Hotels Inc.

SOHO - NASDAQ - Long-term Buy - 4

### Fourth Quarter Results

- **Fourth quarter FFO were \$0.17 versus \$0.21 per share last year.** Adjusted FFO per share were \$0.12 compared to \$0.20 last year. Adjusted FFO excludes unrealized gains/losses on warrants and hedging activities, loss on early extinguishment of debt, impairment of notes receivable, franchise termination fees, aborted offering costs, acquisition costs, increases/decreases in deferred income taxes, and several other one time items. Adjusted FFO per share was below ours and the consensus estimate. 4Q16 results were negatively impacted by Hurricane Matthew, a bleak Houston travel market and cancellations, and lower travel business in Florida due to the Zika virus.
- **Consolidated occupancy declined 4.1% for the fourth quarter of 2016 and ADR (average daily rate) increased 1.2%, resulting in a decline in RevPAR (revenue per available room) of 2.9%.**
- **Dividend Increase.** On January 31, SOHO announced a 5.3% increase in its quarterly dividend to \$0.10 per common share.
- **Management initiated 2017 adjusted FFO per share guidance of \$1.02 to \$1.10.** We are lowering our 2017 adjusted FFO per share estimate by seventeen cents to \$1.08 due mostly to guidance assumptions.
- **We rate SOHO Long-term Buy with a two-year target price of \$8.50.** This is a \$0.50 increase from our previous target price. We are now basing our target price on our 2019 adjusted FFO per share estimate. Our previous price target was based on our 2018 adjusted FFO per share estimate.

**Note Important Disclosures on Pages 7 and 8.  
Note Analyst Certification on Page 7.**

**Additional Discussion**

Total hotel revenue was \$35.9 million in the quarter, down 2.2% from the year ago period. Room revenue made up 67.6% of total revenue, compared to 68.1% last year. Room revenue was down 2.9%. Food and beverage sales declined 2.6% in the quarter.

**Table 1 Consolidated Occupancy**

	Quarter ended 12/31/2016	Quarter ended 12/31/2015	Year-over-Year % change
Occupancy	63.2%	65.9%	-4.1%
ADR	\$138.81	\$137.21	1.2%
RevPAR	\$87.73	\$90.37	-2.9%

Source: Company reports & Hilliard Lyons' calculations

**Table 2 Consolidated Occupancy**

	Fiscal 2016	Fiscal 2015	Year-over-Year % change
Occupancy	69.8%	69.9%	-0.1%
ADR	\$140.63	\$134.21	4.8%
RevPAR	\$98.18	\$93.80	4.7%

Source: Company reports & Hilliard Lyons' calculations

Funds from operations (FFO) were \$2.9 million versus \$3.5 million in last year's fourth quarter. FFO per share and unit were \$0.17 versus \$0.21. Adjusted funds from operations (FFO) were \$2.0 million versus \$3.3 million in last year's fourth quarter. Adjusted FFO per share and unit were \$0.12 compared to \$0.20 in the year ago period.

**Outlook**

**Current Environment** - Fourth quarter results were negatively impacted by Hurricane Matthew (which impacted bookings at half of the company's portfolio) and a decline in bookings in Florida due to the Zika virus worries. New supply in the Louisville, Kentucky market, as well as the temporary closing of the convention center there, is negatively impacting SOHO's hotel in that market. SOHO is seeing continued weakness in Houston, Texas.

**Acquisitions & Dispositions** - Subsequent to the end of the quarter, SOHO purchased the hotel commercial unit of the Hyde Resort & Residences in Hollywood, Florida. The purchase price was \$4.25 million. The hotel commercial unit includes the lobby and front desk areas, offices and other spaces. SOHO also entered into a lease agreement for the meeting rooms of the hotel and 400 space parking garage, as well as an agreement to operate and manage the condo association. This property is close to SOHO's Crowne Plaza Hollywood Beach Resort (IHG - \$48.20). Management does not expect to see much impact on revenue from this property until the 4Q17.

In February, SOHO completed the sale of the Crowne Plaza Hampton Marina for \$5.65 million. Proceeds from the sale were used to repay the mortgage debt on the hotel, with the remaining intended to be used for general corporate purposes. Management is looking at one property that it would like to buy and has a couple of properties it would like to sell as 1031 exchanges if an acquisition is made. We believe management will remain disciplined regarding pricing and will not over pay for an acquisition or complete an acquisition just for the sake of growth.

**Financing** - The company refinanced three properties in the 4Q16 at what we view as favorable rates.

**Share Buyback** - In December, SOHO announced a stock repurchase program for up to \$10 million of its outstanding common shares. During 4Q16, the company repurchased 481,100 shares of common stock for \$3.2 million. The company expects to complete the program before the end of 2017, unless extended by the board.

**Estimate** - Management initiated 2017 adjusted FFO per share guidance of \$1.02 - \$1.10. We are lowering our 2017 adjusted FFO per share estimate by seventeen cents to \$1.08.

**Quarterly Income Statement**

	4Q16	4Q15	% Change
Rooms Department	\$24,302,318	\$25,017,420	-2.9%
Food and Beverage Department	9,143,598	9,384,508	-2.6%
Other Operating Departments	2,489,423	2,348,935	6.0%
Total Hotel Revenue	35,935,339	36,750,863	-2.2%
Rooms Department	6,978,596	6,784,028	2.9%
Food and Beverage Department	6,106,707	6,337,605	-3.6%
Other Operating Departments	558,242	593,279	-5.9%
Indirect	13,900,259	14,264,017	-2.6%
Total Hotel Operating Expenses	27,543,804	27,978,929	-1.6%
Real Estate NOI	8,391,535	8,771,934	-4.3%
Depreciation and Amortization	3,758,083	4,007,989	-6.2%
Impairment of Investment in Hotel Properties, net		500,000	
Loss on Disposal of Assets	35,859	(248,673)	
Corporate General and Administrative	1,689,169	1,889,228	-10.6%
Other Operating Expenses	5,483,111	6,148,544	-10.8%
Operating Income (Loss)	2,908,424	2,623,390	10.9%
Interest Expense	(3,862,974)	(4,655,178)	
Interest Income	52,262	9,573	
Equity in Earnings of Joint Venture		(31,377)	
Unrealized Loss on Hedging Activities	29,182	(2,011)	
Impairment of Note Receivable			
Gain on Early Debt Extinguishment	(260,217)		
Gain on Change in Control		42,191	
Gain on Involuntary Conversion of Asset		(37,835)	
Gain (Loss) on Disposal of Assets			
Net Income Before Taxes	(1,133,323)	(2,051,247)	
Income Tax Benefit (Provision)	1,059,236	1,339,288	
Net Income	(74,087)	(711,959)	
Net Loss (Income) Attributable to the Noncontrolling Interest	132,944	189,785	
Net Income Attributable to the Company	58,857	(522,174)	
Distributions to Preferred Shareholders	(805,000)		
Net Income Attributable to Common Shareholders	<b>(\$746,143)</b>	<b>(\$522,174)</b>	
Net Income Per Share (diluted)	<b>(\$0.05)</b>	<b>(\$0.04)</b>	
Weighted Average Shares Outstanding (diluted)	14,895,203	14,490,714	2.8%
<b>Funds From Operations</b>	4Q16	4Q15	% Change
Net Income (Loss)	(\$746,143)	(\$522,174)	
Depreciation and Amortization	3,758,083	4,007,989	-6.2%
Other Adjustments	(97,085)	57,186	
<b>Funds From Operations (FFO)</b>	<b>\$2,914,855</b>	<b>\$3,543,001</b>	-17.7%
Unrealized (Gain)/Loss on Hedging Activities	(29,182)	2,011	
Unrealized Loss on Warrant Derivative			
Decrease in Deferred Income Taxes	(1,102,777)	(1,364,402)	-19.2%
Impairment of Note Receivable			
Acquisition Costs		11,402	
Loss on Starwood Settlement		324,271	
Over-assessed real estate taxes under appeal		497,733	
Loan modification fee	33,980	243,229	
Franchise Termination Fee			
Aborted Offering Costs			
Loss on Early Extinguishment of Debt	260,217		
<b>Adjusted FFO</b>	<b>\$2,077,093</b>	<b>\$3,257,245</b>	-36.2%
<b>FFO Per Share and Unit</b>	<b>\$0.17</b>	<b>\$0.21</b>	-19.0%
<b>Adjusted FFO Per Share and Unit</b>	<b>\$0.12</b>	<b>\$0.20</b>	-40.0%

Previous results have been restated.

Source: Company report

**Condensed Balance Sheet**

	12/31/2014	12/31/2015	12/31/2016
<b>Assets</b>			
Investment in Hotel Properties (net)	\$263,282,720	\$354,963,242	\$348,593,912
Property Under Development			
Investment in Joint Venture	1,987,542		
Assets Held for Sale			5,333,000
Cash and Cash Equivalents	16,634,499	11,493,914	31,766,775
Restricted Cash	6,621,864	5,793,840	4,596,145
Accounts Receivable	1,909,896	4,256,247	4,127,748
Accounts Receivable - Affiliate	197,674	226,552	4,175
Loan Proceeds Receivable		2,600,711	
Prepaid Expenses, Inventory, and Other Assets	3,518,073	4,247,359	4,648,469
Notes Receivable			
Shell Island Lease Purchase (net)			
Deferred Income Taxes	3,408,746	5,390,374	6,949,340
Deferred Financing Costs (net)	5,405,288	4,086,114	
<b>Total Assets</b>	<b>\$302,966,302</b>	<b>\$393,058,353</b>	<b>\$406,019,564</b>
<b>Liabilities</b>			
Line of Credit			
Mortgage Loans	205,291,657	271,977,944	282,708,289
Bridge Loan			
Loans Payable			
Unsecured notes	52,900,000	52,900,000	24,308,713
Series A Cumulative Redeemable Preferred Stock			
Accounts Payable and Accrued Expenses	11,409,759	12,334,878	12,970,960
Accounts Payable - Affiliates			
Dividends and Distribution Payable	852,914	1,651,840	2,315,787
Advance Deposits	1,220,729	1,335,323	2,376,527
Warrant Derivative Liability			
<b>Total Liabilities</b>	<b>\$271,675,059</b>	<b>\$340,199,985</b>	<b>\$324,680,276</b>
Equity			
Preferred Stock			16,100
Common Stock	105,709	144,907	144,685
Additional Paid in Capital	58,659,799	82,771,911	118,395,082
Accumulated Deficit	(32,405,404)	(33,890,834)	(39,545,754)
<b>Total SOHO Stockholders' Equity</b>	<b>\$26,360,104</b>	<b>\$49,025,984</b>	<b>\$79,010,113</b>
<b>Noncontrolling Interest</b>	<b>4,931,139</b>	<b>3,832,384</b>	<b>2,329,175</b>
<b>Total Equity</b>	<b>\$31,291,243</b>	<b>\$52,858,368</b>	<b>\$81,339,288</b>
<b>Total Liabilities and Equity</b>	<b>\$302,966,302</b>	<b>\$393,058,353</b>	<b>\$406,019,564</b>

Balance Sheet Ratio Analysis	12/31/2014	12/31/2015	12/31/2016
Total R/E Investments / Total Debt	102.7%	109.3%	115.3%
Debt to Total Equity	825.1%	614.6%	377.5%
Debt as % of Total Assets	85.2%	82.7%	75.6%
Total Liabilities as % of Total Assets	89.7%	86.6%	80.0%
Shareholders' Equity as % of Total Assets	8.7%	12.5%	19.5%

Previous numbers have not been restated.

Source: Company reports

## Valuation

At 6.9x our 2017 adjusted FFO forecast, SOHO's stock is trading significantly below its peer group. We believe the company deserves to trade at a multiple of 6.5x, which is slightly above the company's median 5 year historic forward multiple of 6.3x (to reflect the company's improving balance sheet), but is still a discount to the peer group. By using a multiple of 6.5x our 2019 adjusted FFO per share estimate of \$1.32, we derive our two year target price of \$8.50. (We note our previous price target was based on our 2018 adjusted FFO per share estimate.)

Lodging/Resorts REITs	Symbol	Closing Price	Current	Yield	Payout Ratio	FFO Per Share			2-Year Exp.	17/16E	Price/FFO	
		2/17/2017	Dividend			2015	2016E/A	2017E	Avg. Growth	Growth Rate	2016E/A	2017E
Host Hotels & Resorts	HST	\$18.39	\$0.80	4.4%	48.5%	\$1.54	\$1.65	\$1.66	3.9%	0.6%	11.1x	11.1x
Hospitality Properties Trust	HPT	\$31.78	\$2.04	6.4%	56.8%	\$3.34	\$3.59	\$3.80	6.9%	5.8%	8.9x	8.4x
LaSalle Hotel Properties	LHO	\$29.79	\$1.80	6.0%	62.1%	\$2.84	\$2.90	\$2.77	-1.2%	-4.5%	10.3x	10.8x
Hersha Hospitality Trust	HT	\$20.84	\$1.12	5.4%	46.3%	\$1.94	\$2.42	\$2.40	11.9%	-0.8%	8.6x	8.7x
Ashford Hospitality	AHT	\$7.65	\$0.48	6.3%	30.4%	\$1.40	\$1.58	\$1.52	4.3%	-3.8%	4.8x	5.0x
Peer Average		\$21.69	\$1.25	5.7%	48.8%	\$2.21	\$2.43	\$2.43	5.1%	-0.5%	8.7x	8.8x
<b>S&amp;P 500</b>	<b>SPX</b>	<b>2,351.16</b>	-	-	-	<b>\$118.23</b>	<b>\$116.83</b>	<b>\$129.74</b>	<b>4.9%</b>	<b>11.1%</b>	<b>20.1x</b>	<b>18.1x</b>
<b>SoTHERLY Hotels Inc.</b>	<b>SOHO</b>	<b>\$7.44</b>	<b>\$0.40</b>	<b>5.4%</b>	<b>44.4%</b>	<b>\$1.00</b>	<b>\$0.90</b>	<b>\$1.08</b>	<b>4.0%</b>	<b>20.0%</b>	<b>8.3x</b>	<b>6.9x</b>

FFO for SOHO is adjusted FFO.  
SPX figures are EPS, not FFO per share.

Source: NAREIT, Baseline, and Hilliard Lyons' estimates

## Dividend

On January 31, SOHO announced a 5.3% dividend increase. The quarterly dividend was raised from \$0.095 per share to \$0.10 per share.

## Suitability

We assign shares of SoTHERLY Hotels a suitability rating of 4 on our scale of 1 - 4 (1=most conservative, 4=most aggressive). Our rating is based on the company's small market cap, low relative trading volume and day to day leasing. We believe these shares are only suited for risk tolerant investors seeking long-term capital appreciation and an attractive dividend yield.

## Risks and Considerations

SoTHERLY Hotels Inc. may not achieve our target price or within the time frame specified due to external factors beyond the company's control or due to internal factors. These risk factors include:

**Economic Risk** - In tough economic environments consumers may spend less on travel. A decline in hotel visits and spending could negatively impact SOHO's results.

**Interest Rate/Leverage Risk** - Like all REITs, SOHO is interest rate sensitive. We are somewhat concerned about SOHO's ability to weather an increase in interest expense in a rising rate environment.

**Asset Size Risk** - SOHO has only \$353.9 million in wholly-owned real estate assets (net of depreciation) and \$406.0 million in total assets. The company is one of the smallest of the publicly traded Lodging/Resorts REITs tracked by NAREIT. Thus, one small acquisition or even the timing of one property purchase can have a material impact on the company's financial statements.

**Stock Liquidity Risk** - With 14.9 million common shares outstanding (16.7 million including operating units), SOHO is very thinly traded on a daily basis. Thus its "micro-cap" size makes it too small for some

institutional investors. Even retail investors with relatively small positions could experience limited liquidity if forced to sell.

**Ownership Concentration Risk** - Management and insiders own a significant amount of common shares and operating units. We view this as a positive in that insiders' interests are in line with shareholders' interests.

**Hotel Management Risk** - REITs are not allowed to manage hotels. MHI Hotel Services manages the hotels for SOHO. Officers and directors of SOHO also own an interest in and are on the board of directors of MHI Hotel Services. We believe SOHO's outside directors, which make up the majority of the board, will make sure no conflict or even the appearance of a conflict exists.

*Additional information is available upon request.*

### **Analyst Certification**

I, Carol L. Kemple, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

### **Important Disclosures**

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

Hilliard Lyons acted as a manager or co-manager of an offering of securities of Sotherly Hotels in the past 12 months.

Hilliard Lyons expects has received investment banking compensation from Sotherly Hotels within the past 12 months.

### **Investment Ratings**

**Buy** - We believe the stock has significant total return potential in the coming 12 months.

**Long-term Buy** - We believe the stock is an above average holding in its sector, and expect solid total returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

**Neutral** - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

**Underperform** - We believe the stock is vulnerable to a price set back in the next 12 months.

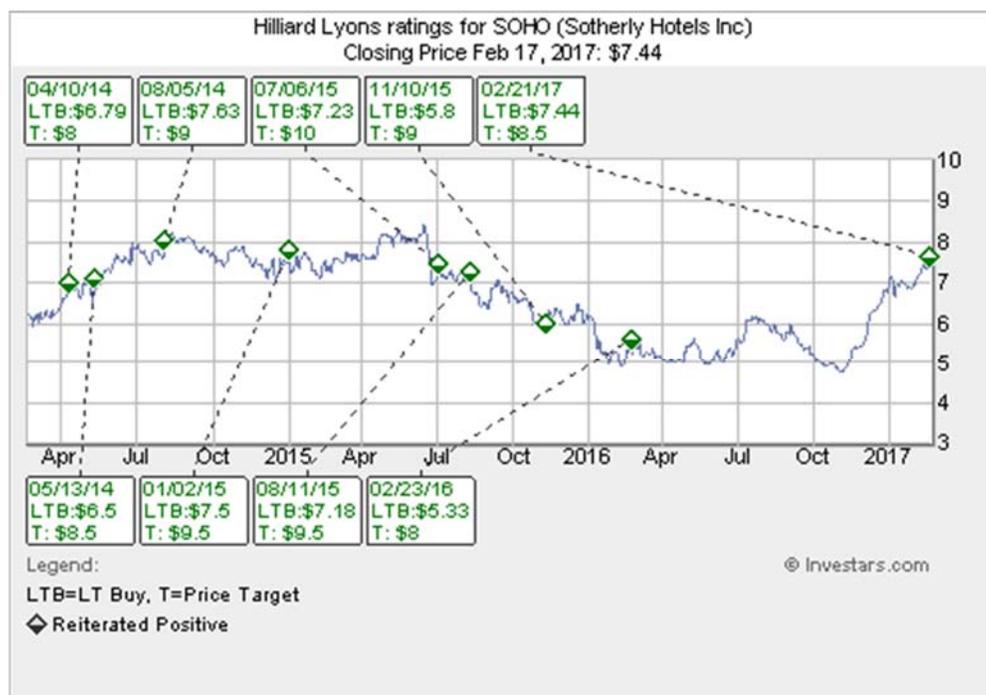
### **Suitability Ratings**

**1** - A large cap, core holding with a solid history

**2** - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks

**3** - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage

**4** - Speculative, due to small size, inconsistent profitability, erratic revenue, volatility, low trading volume or a narrow customer or product base



Our price target reflects a two year time frame.

Rating	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	36	30%	17%	83%
Hold/Neutral	76	62%	7%	93%
Sell	10	8%	0%	100%

As of 6 February 2017

### Other Disclosures

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