

Q3 2016 Hotel Bulletin

Strong performance for key UK tourist cities post Brexit vote

The Q3 2016 Hotel Bulletin analyses the first full quarter of data following the EU referendum in June. Very early trends suggest that a divide could be emerging between leisure and corporate focused markets. Cities with larger tourist industries recorded strong RevPAR growth as international visitors flocked to benefit from a weaker Pound, whereas cities outside this group continued recent trends of plateauing or declining RevPAR. This quarter's Focus examines the independently branded hotel market, where a number of groups have created unique customer propositions and enjoyed significant success.

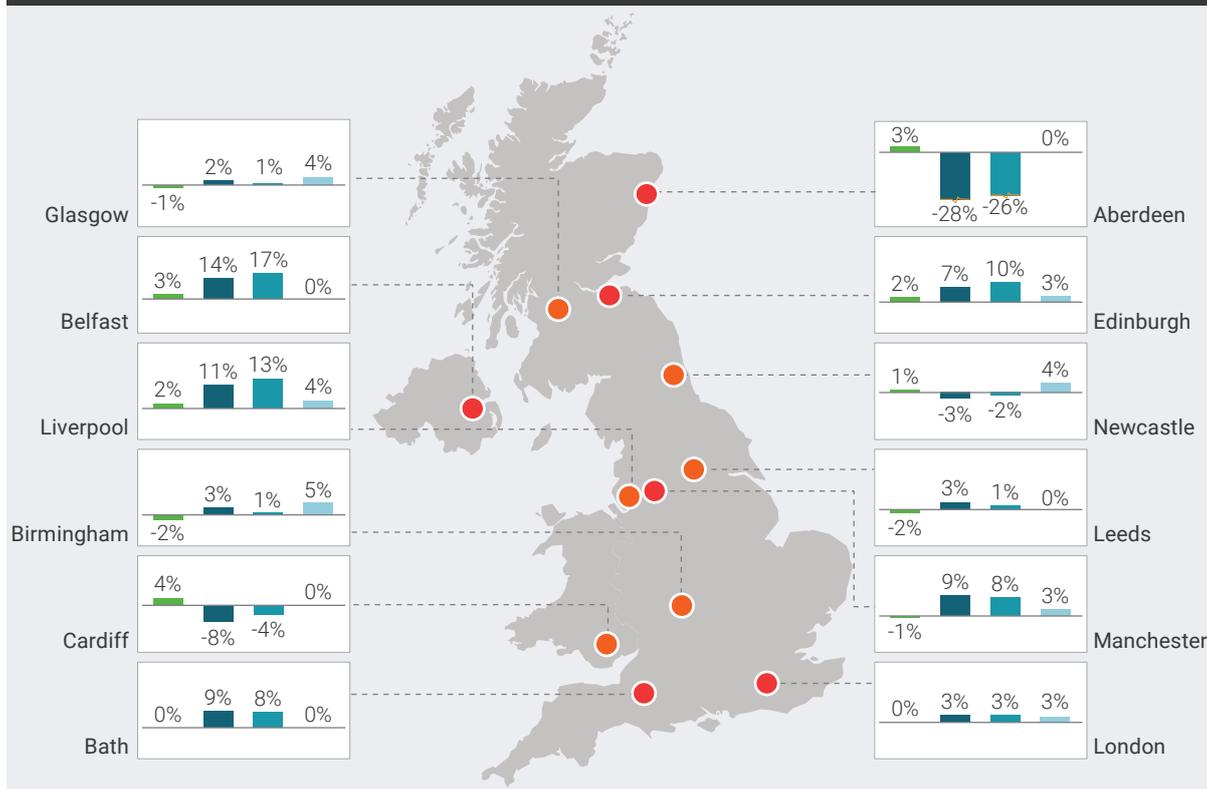
DEMAND

RevPAR performance in Q3 2016 varied widely amongst the 12 cities reviewed in the Hotel Bulletin. Average RevPAR growth of 3% was bolstered by strong performances in cities including Belfast and Liverpool. In contrast, Aberdeen's hotel market's significant RevPAR decline continued. Excluding Aberdeen, the remaining 11 cities recorded average growth of 5%.

Q3 2016 data highlights the immediate impact of Britain's vote to leave the EU in June 2016. It is too early to draw any definite conclusions with only one quarter of data, but the tourism and hospitality industries appear to have received an immediate boost from the depreciated Pound.

Foreign exchange movements have resulted in UK holidays being comparatively cheaper than travelling abroad. Foreign visitors have been quick to take advantage; July saw the highest ever levels of inbound tourism in the UK with 3.8 million visits¹. Staycations also flourished in Q3 2016, with 6% more Brits taking a staycation over the August bank holiday in 2016 than in 2015².

FIGURE 1: Selected UK hotel markets – demand and supply



■ Occupancy percentage change⁽¹⁾ (Q3 YoY) ■ Average room rate percentage change (Q3 YoY)
■ RevPAR percentage change (Q3 YoY) ■ Supply percentage change since 30 September 2014
● ● ● Active pipeline⁽²⁾ >10%, 5 to 10%, <5%

Notes: Q3 covers the three months to the end of September | Q3 YoY compares the average of Q3 2016 to the average of Q3 2015 | Supply and pipeline analysis relate to numbers of hotel bedrooms | 1 Occupancy percentage change represents actual rather than absolute percentage change | 2 Active pipeline refers to hotel bedrooms with an opening date in the next three years

Increased traveller numbers have not led to significant occupancy growth (1% average growth in Q3 2016). However, the impact has been discernible when compared to recent occupancy (1% average decline over the last four quarters).

Hoteliers have been able to charge higher rates, particularly in tourist hotspots. In Bath, average room rates increased by 9% in comparison to Q3 2015. Hoteliers were able to increase prices as higher rates were still affordable for overseas visitors when translated to their home currencies. Many holidaymakers had made their arrangements for summer 2016 in advance of the Brexit vote, meaning that the positive impact for leisure focussed hoteliers may increase in the coming months.

With the exception of Manchester, cities that traditionally attract corporate customers have recorded weaker growth in Q3 2016.

There may be a negative 'lag' on the corporate sector, as corporate trips and conferences that would have been booked before the Brexit vote may be put on hold.

London has recorded a trend of falling occupancy levels over the past six quarters. Flat occupancy in Q3 2016 suggests that this decline may have been stemmed by additional tourists taking advantage of the weakened Sterling. Overall RevPAR increased by 3% as a result of higher rates.

The top performer in Q3 2016 was Belfast (17% RevPAR growth). The city has developed a strong offering for tourists in recent years and its Titanic Experience exhibit was awarded Best European Tourist Attraction at the World Travel Awards in September.

Liverpool, another strong leisure market, recorded strong RevPAR performance in Q3 2016 (13% RevPAR growth). The city hosted over 10,000 attendees³ at the 2016 Labour Party Conference in September resulting in a significant boost in RevPAR during this month.

Aberdeen was the worst performer in Q3 2016 by a significant margin (26% RevPAR decline). The city's hotel market has faced difficulties as a result of its reliance on corporate travellers to oil and gas businesses in the city. Uncertainty regarding oil prices continues with further falls following recent doubts about whether Iraq will agree to OPEC's proposed production cuts⁴.

Sources: 3. www.labour.org.uk, 4. Financial Times

SUPPLY AND PIPELINE

In figure 3, we compare the proportion of current supply (inner circle) and active pipeline (outer circle) in the UK market by sector. In Q3, extensions to existing properties accounted for 24% of new bedrooms opened as hoteliers look to maximise revenue from existing sites.

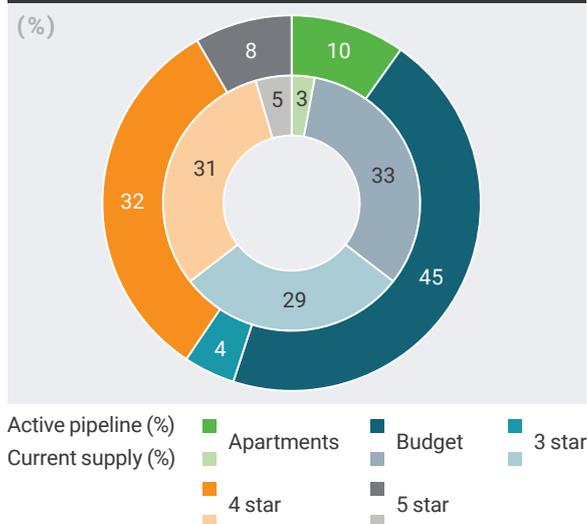
Whitbread opened nine Premier Inns in Q3 2016 (735 bedrooms) as it continues with aggressive expansion plans. The brand now covers over 65,000 bedrooms in the UK and has a further 826 bedrooms due to open by the end of the year, nearly 600 of which are extensions of existing hotels.

Marston's Inns, Travelodge and J D Wetherspoon also opened several new hotels in the budget or value segments in Q3 and all have been actively expanding their portfolios throughout 2016.

Notable new openings and developments this quarter include:

- AccorHotels has opened its first IBIS Hotel in Cambridge. The 231 bedroom hotel is located next to the railway station and above the UK's largest multi-storey cycle park.
- Dutch brand citizenM opened two new hotels in London in Q3 2016, one in Shoreditch and one opposite the Tower of London. The addition of 586 bedrooms from these two properties has more than doubled the brand's total bedrooms in the UK.
- Ireland's Staycity opened its tenth extended stay UK property, a 197 unit aparthotel in York, which is leased from LaSalle Investment Management.

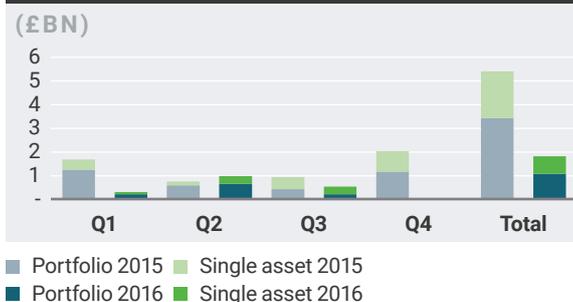
FIGURE 2: UK current bedroom supply (inner circle) and active pipeline (outer circle) by grading



Source: AM:PM

Note: Active pipeline includes developments with a confirmed opening date in the next three years. The budget category includes hostels, budget, and two star hotels

FIGURE 3: UK transaction value



Source: HVS

Note: Only disclosed hotel transactions over £6 million included in this analysis

TRANSACTIONS

Transaction values in Q3 2016 (£522 million) were nearly half of that recorded in Q3 2015. Total transaction values in 2016 to date are significantly lower than the September year-to-date figure in any of the last three years. Following the leave vote in June's EU referendum, there is no strong indication of what form Brexit will take and this uncertainty appears to have contributed to some delays.

The Sterling depreciation recorded since June will have materially impacted overseas investors. Many investors will be seeking opportunities to take advantage of favourable exchange rates, which have made UK assets cheaper in their home currency.

In a continuation of the trend noted in the last few quarters, Asian investors have maintained their interest in the UK hotel market. Hong Kong's YT Realty Group acquired a partial interest in a London Travelodge from Goldman Sachs for £42 million while China's Junson Capital acquired the DoubleTree by Hilton London Docklands Riverside for a reported £80 million.

Other notable transactions completed this quarter include:

- Legal and General completed the sale and leaseback of the hub by Premier Inn development at King's Cross for a reported £85 million, with half payable on exchange. Whitbread will operate a 25 year lease at £3.5 million annual rent representing a net initial yield of just under 4%.
- Marriott International's acquisition of Starwood Hotels & Resorts completed in September creating the world's largest hotel company with over 1.1 million bedrooms worldwide.

FOCUS ON: INDEPENDENTLY BRANDED HOTELS

With loyalty programs continuing to grow in importance to retain customers, the global brands appear to be determined to own a brand portfolio that caters for all its customers' needs from low-cost to luxury. Ownership of the customer is a key battle ground as the global brands compete with online travel agents (OTAs) such as Expedia and booking.com to secure the initial booking transaction.

Meanwhile, independently branded hotels (smaller international brands and national/regional domestic brands) have been developing and diversifying, differentiating themselves from the perceived 'cookie-cutter' nature of some of the global brands. Independently branded hotels have been growing by targeting specific parts of the market and in many cases have been laser focussed on creating their customer proposition for this market to find significant success.

Location, location, location – options for expansion

London

London's behemoth hotel market comprises 21% of all UK hotel bedroom supply¹. As well as being one of the world's top corporate centres, the city benefits from a huge leisure market. Half of the UK's top 50 visitor attractions (including the entire top 10)² are located in London.

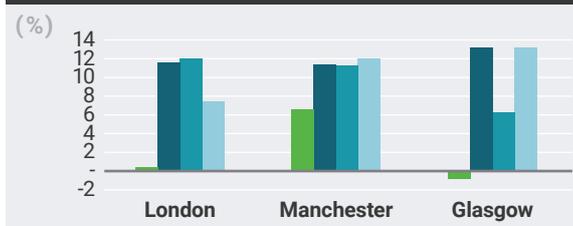
Independently branded groups have already enjoyed success in the city with groups including Z Hotels and Qbic setting up hotels in the capital. The steady stream of incoming tourists and business travellers allow most hotels to maintain a buoyant base level of occupancy and room rate. This consistent and diverse demand means that hotels can source demand without having to rely on a global brand's platform.

Certain key issues to consider before choosing London include stiff competition for sites (and therefore high asset prices) and recently plateauing demand metrics. However, London remains in a different league to other cities in England in terms of absolute RevPAR an, as such, remains an attractive target for expansion.

Manchester

Manchester has transformed in recent years into a seven-night-a-week city with one of the strongest cultural and commercial offerings in the UK. Manchester has benefitted from significant investment from commercial developers and the

FIGURE 4: Key supply and demand metrics for Glasgow, Manchester and London



- RevPAR average percentage change (last four quarters YoY)
- Supply percentage change since 30 September 2013
- Active pipeline as a percentage of current supply
- Independent active pipeline as a percentage of current independent supply

Source: AM:PM, HotStats

leisure sector continues to thrive from hosting two of the world's largest football clubs and venues such as the Lowry Centre and the MEN Arena. Despite significant growth in supply over the last two years (8%), Manchester hotels have recorded robust, unhindered RevPAR growth. Hoteliers should keep in mind that a large portion of visitors to Manchester are business travellers. Brands like Club Quarters, which target business travellers, could be well placed to take advantage of this market building on the success of brands like Malmaison.

Glasgow

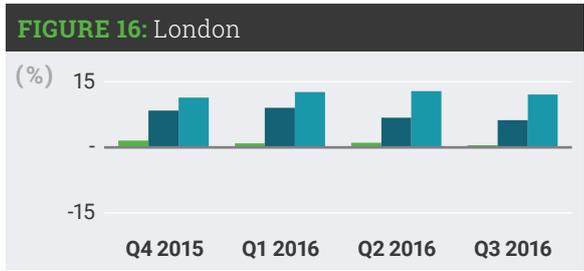
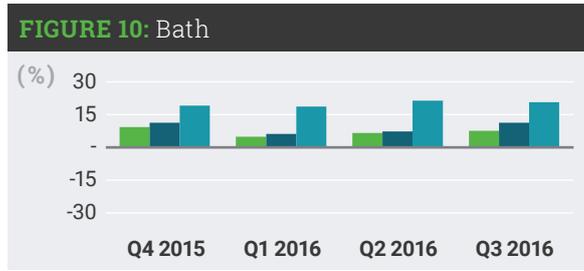
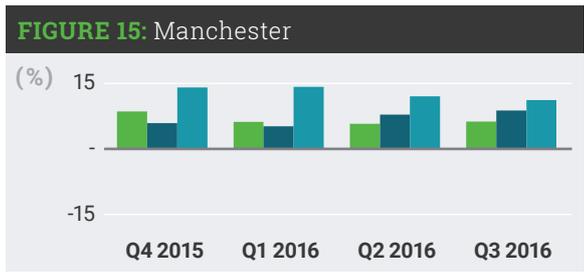
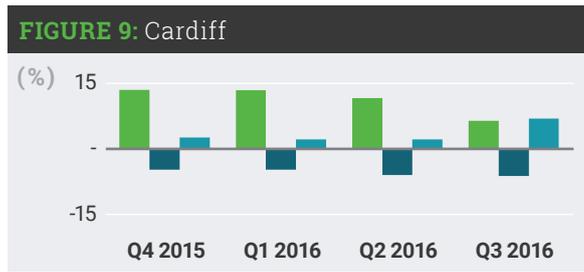
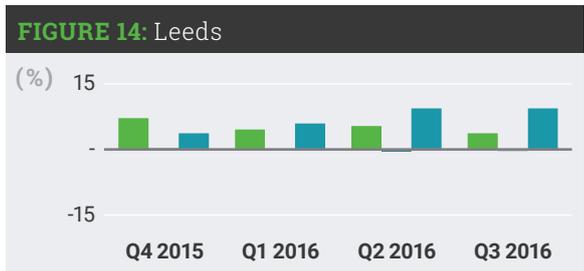
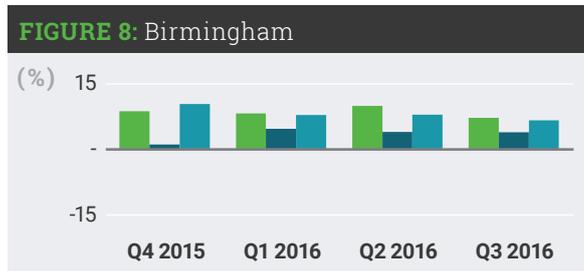
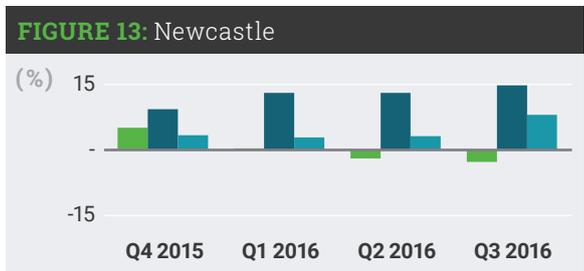
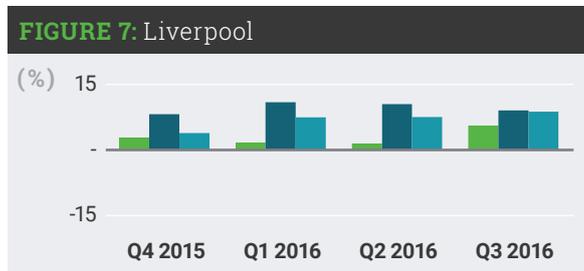
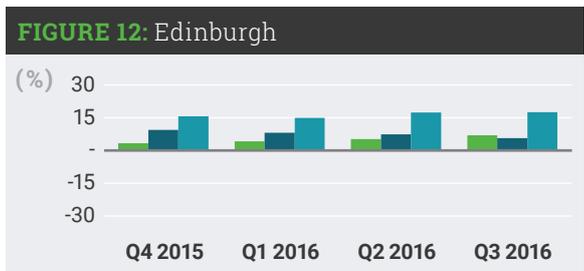
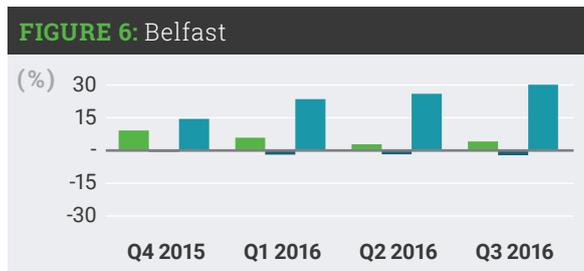
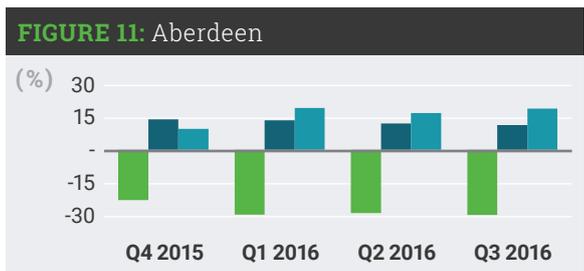
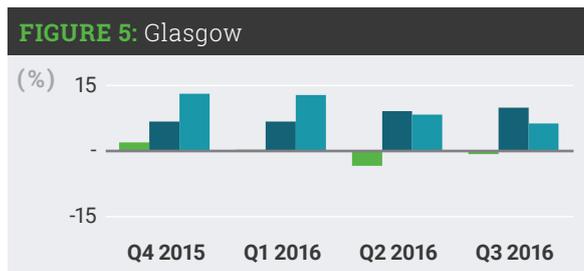
Glasgow has changed dramatically since the 1980s. A number of regeneration projects have transformed it into a vibrant post-industrial city. For leisure customers, Glasgow has three major football stadia, and entertainment venues including the SECC and the SSE Hydro.

Tourists travelling for events at these venues are generally more price sensitive when considering where to stay. To accommodate, 40% of hotel bedrooms are in the budget sector (versus 33% nationally). The city is popular with independently branded hotels in this segment; citizenM and Z Hotels have opened in Glasgow and a Motel One is due to open in 2017.

CONCLUSION

There are undoubtedly a number of challenges facing independent operators competing against larger, branded hotel chains. These include accessing finance (equity investors and lenders have typically perceived a lower level of risk with global brands) and an inbuilt consumer tendency to book a global brand, in part due to the broader reach of larger loyalty programmes. However, if an independently branded hotel is able to outperform competitors (either on price, service, style or location), there is significant scope for success in the UK market. **A**

INVESTMENT INDICATORS FOR Q4 2015 TO Q3 2016



Key for all: Demand growth Historical supply change Active pipeline

Source for all: AM:PM, HotStats

Notes: Demand growth calculated as the average quarterly RevPAR change for the previous four quarters | Historical supply change calculated as the change in hotel bedrooms in the last two years | Active pipeline calculated as confirmed pipeline bedrooms as a percentage of current supply

ABOUT AM:PM

AM:PM are a leading source of market intelligence on the UK & Ireland hotel industry. We maintain extensive data relating to hotel supply to help clients gain a comprehensive and unrivalled understanding of the size and structure of the hotel industry.

We offer a suite of subscription-based online products that allow clients to search, analyse and benchmark the hotel sector. This includes access to a unique hotel database with details of over one million hotel rooms covering the past, present and future hotel supply throughout the UK & Ireland.

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