HVS International

European Hotel Transactions Article
2002 Country Analysis

The UK

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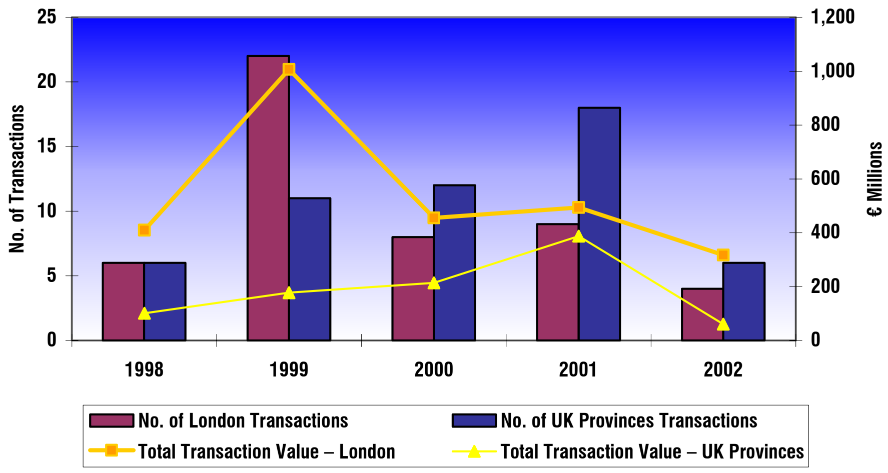
Market Review – The UK

Historically, the UK has dominated the European hotel investment market, and this generally continues to be the case today. In 2001 the UK represented 37% of all single asset transactions recorded by HVS International (based on rooms sold) compared with 46% in 1999. HVS recorded some 30 deals in 2001, of which only seven transactions involved central London hotels. The most significant single asset sale resulted from the disposal of one of Compass's Signature Hotels, the Cumberland. Nomura's Principal Finance Group acquired the hotel for approximately €238 million (€267,000 per room), achieving an initial yield of around 7.3%. The second-largest single asset transaction was the 216-room Berners Hotel for €81 million to JJW Hotels & Resorts (€377,000 per room).

London's single asset sales in 2001 improved marginally on the previous year in terms of sales volume, by 8%, totalling some €494 million (including two hotels at Heathrow). The UK provincial market proved more liquid, with total investment increasing by 84% over the previous year, totalling some €395 million. For the first time investment within the UK provincial market is shown in 2001 to be on a par with the level of investment generated by London.

Figure 1 London and UK Provinces Single Asset Transactions 1998-02



The effect of the softening in the economy, and a considerable weakening in trading, has resulted in a relatively illiquid market in 2002. This is largely as a result of a significant difference between the asking price of the seller and that which the buyer is prepared to pay.

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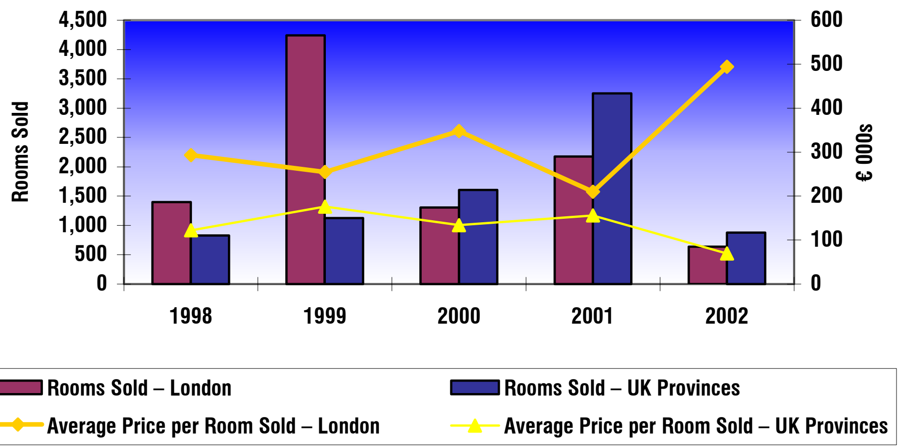
HVS has recorded four notable London sales to date in 2002, with the most significant transaction (on an average price per room basis) being the sale of the exclusive 53-room, 47 Park Street property (previously flagged under Accor's Sofitel Demeure brand) for €43 million in a joint venture agreement between Marriott and Orion European Real Estate Fund. This is now being marketed as Marriott's first Executive Residence in Europe, an up-market, urban fractional ownership product. One further significant transaction involved the sale of a majority stake in the 450-room London Hilton on Park Lane for approximately €248. The sale involves a joint venture agreement between Land Securities, the existing owner, and London & Regional, with the latter taking a controlling interest.

With few other London transactions, the average price per room in 2002 is somewhat distorted, as indicated in Figure 2.

Figure 2 UK Single Asset Hotel Transactions – Average Price per Room Sold 1998-02



Portfolio activity in 2001 was exceptional, totalling approximately €4.5 billion. The tremendous level of activity can be attributed to the decision by Compass plc (formerly Granada Compass plc) to sell off its hotel investment portfolio, which was made up of the old Forte empire. Six Continents acquired the 79-strong Posthouse Hotels portfolio for approximately €1.3 billion (approximately €108,000 per room). All Posthouse Hotels have since been rebranded as Holiday Inn, with the exception of around 15 hotels not deemed as suitable for conversion, many of which have since been sold on. Meanwhile, Macdonald Hotels acquired the 48-strong Heritage Hotels in a joint venture agreement with the Bank of Scotland for approximately €385.4 million (€124,000 per room).

Prior to the sale of Compass's various hotel portfolios, the investment vehicle of the Japanese bank Nomura, Principal Finance Group (PFG), entered the UK hotel investment market with the acquisition of the 17-strong Principal Hotel Group for approximately €418.2 million (€167,000 per room). Nomura, under the company name of Grand Hotels (M) Acquisitions, proceeded to successfully acquire the 128-strong worldwide Le Méridien portfolio for €1.9 billion, of which 17 are operated in the UK.

In addition to the disposal of the Compass hotel inventory, much of the investment activity that arose during 2001 was in the form of sale and leaseback structured deals. Nomura financed its acquisition of the Le Méridien portfolio following the sale and leaseback of 12 UK properties. The deal, which was entered into with the Royal Bank of Scotland (RBS), provided funds worth €1.6 billion. Hilton also undertook its first wave of sale and leaseback activity, with RBS once again the investor. The deal involved some 11 properties, and provided funds of €512 million. A third major sale and leaseback deal that completed in 2001 was between Accor and London & Regional: this deal involved some 13 UK properties and raised €98.5 million of capital.

Despite the difficult trading environment of recent times, the momentum of innovative financing deals has continued into 2002. Thistle entered into a uniquely structured 'sale and managementback' deal with the property company Orb Estates. The deal, which involved 37 properties, some 5,500 rooms, completed for €950.5 million. This deal was followed later in the year by Hilton's entering into its second sale and leaseback, with a further ten hotels, some 2,043 rooms. The deal, in which Hilton itself has taken a 40% equity stake, involved the formation of a limited partnership between Hilton, the property company Rotch, the hotel investment company Farnsworth Group and the Bank of Scotland, and realised a further €488 million of capital after consideration for Hilton's investment. Most recently Jarvis Hotels has secured a sale and leaseback deal with a private equity consortium led by Lioncourt Capital for €237 million in exchange for a 34-year lease. The deal involves nine UK properties, some 1,341 rooms.

Following the wealth of portfolio deals in the past two years we can expect investors to rationalise their portfolios further than that already witnessed. A cautious outlook seems set to remain for the remainder of 2002, although the hotel investment market is likely to pick up somewhat and improve substantially in 2003. Corporate deals are likely to continue, with further sale and leaseback and other innovative financing deals expected, with the anticipated sale of Travelodge, the UK's second-largest budget hotel operator, providing considerable interest. Nomura is also rumoured to be disposing of a number of Principal Hotels that have failed to meet Le Méridien's brand standards. Economic factors such as the continued low interest rates are also likely to boost investment activity.

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