

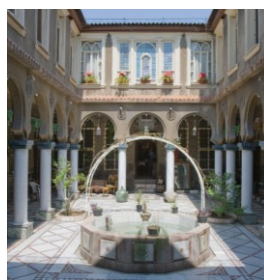


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THE HOTEL INVESTMENT CLIMATE IN SYRIA **SILK ROUTE READY FOR REMIX**

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The Hotel Investment Climate in Syria

In this article we take a brief look at the investment potential of the Syrian tourism market with special emphasis on Damascus as hoteliers and investors gear up to enter Damascus and other Syrian cities in search of new opportunities.

For decades, 'Promise' and 'Potential' have been bywords for the tourism investment market in Syria; however, the political circumstances and strong government regulations kept investors at bay. Finally, a strong urge from the government to diversify the economy (moving away from its reliance on the depleting oil reserves), provide employment to the growing population, and build public infrastructure resulted in reforms in the key economic sectors. Tourism is recognised as a significant contributor to the Syrian economy and continues to perform strongly. According to the Ministry of Tourism in Syria, the total number of visitors reached 6.6 million in the first nine months of 2010, already surpassing the full-year 2009 figures and achieving growth of more than 100% in the last decade. The existing hotels in Damascus and other cities, such as Aleppo and Latakia, reaped the rewards of increased tourism demand and performed strongly. Increased business activity coupled with traditional tourism demand, low current hotel supply and a moderate future pipeline mean that there continue to be lucrative investment opportunities across all hotel categories in Syria, and Damascus in particular.

Syria's emergence as one of the most promising investment options for hotel developers, lenders, operators and investors in the region is mainly attributed to the facilitation of lending by the banks and the Investment Market Forum organised by the Supreme Council of Tourism. Since its introduction in 2005, the forum has succeeded in attracting investment across various asset classes through brisk reforms and special concessions for the sector. At the sixth Investment Market Forum in April 2010, the total number of tourist projects on offer had increased to 92 (from 33 in 2005), including small and medium-sized three-star hotels, open beaches and residences.

Visitor numbers reached 6.6 million in the first three quarters of 2010 and have increased by more than 100% in the last decade.

What Makes Syria a Frontrunner?

Syria is a distinctive tourist destination with rich cultural heritage and vivid elements – beaches, mountains, green forests, lakes and Badia deserts. Arguably the world's oldest continuously inhabited region, Syria was home to its first human settlements 12,000 years ago and bore witness to the growth of civilisation through the first ever writing, the first alphabet and the first recorded music score. The country's vast land of untapped tourism-related potential spans the cities of Damascus, Aleppo, Latakia, Palmyra and others, with a total population of 21.8 million. Damascus is an important stop on the ancient Silk Route for all tourist and commercial traffic and boasts of being one of the most authentic cities in the Middle East. The two largest religions of the world, Christianity and Islam, flourished here.

Syria has traditionally attracted cultural, religious, health and leisure tourism segments, mainly from the Arab countries. With the improvement in the relations with the West and elimination of visa requirement for Iranian and Turkish nationals, the number of visitors coming to Syria has increased hugely. With reforms in the key economic sectors – banking, insurance, construction and real estate – the corporate and MICE (meeting, incentive, conference and exhibition) segments have produced strong demand for quality hotel rooms.

According to the World Travel & Tourism Council (WTCC), the contribution of the travel and tourism industry to employment in absolute terms is expected to rise from 792,000 jobs in 2010 to 1.1 million jobs by 2020. Investment in travel and tourism is estimated at US\$608.3 million, or 6.1% of total investment in 2010; by 2020, this number is expected to reach US\$922.5 million, or 6.4% of total

investment. Real GDP growth for the travel and tourism industry was 4.1% in 2010 and is expected to average 3.3% per annum over the next ten years.

Hotel average rates and occupancy levels in Damascus bounced back in the first nine months of 2010 after a comparatively weaker year in 2009. We expect strong RevPAR levels for the full year 2010. As we enter 2011, the investment climate in the tourism and hotel sector is supported by strong economic indicators and reforms, and the outlook is upbeat.

FIGURE 1: FORECAST OF MAJOR TOURISM INDICATORS 2010-20

Syria	2010			2020		
	US\$ (bn)	% of Total	Growth (%)	US\$ (bn)	% of Total	Growth (%)
Personal Travel & Tourism	17.4	5.0	2.3	34.9	5.5	4.6
Business Travel	3.4	0.6	1.7	5.8	0.6	3.0
Government Expenditure	2.4	3.1	4.2	4.5	3.3	3.9
Capital Investment	7.6	6.1	-5.1	14.1	6.4	3.9
Visitor Exports	42.0	18.5	4.5	71.8	15.9	2.9
Other Exports	10.3	4.5	14.2	21.5	4.8	5.0
T&T Demand	83.1	10.6	4.0	152.7	10.6	3.7
Direct Industry GDP	29.3	5.2	3.9	49.9	4.9	2.9
T&T Economy GDP	68.2	12.1	4.1	121.1	11.9	3.3
Direct Industry Employment	78.0	5.8	2.0	103.4	5.2	2.9
T&T Economy Employment	169.5	12.5	2.6	234.2	11.9	3.3

Source: WTCC Country Forecast – Syria, 2010

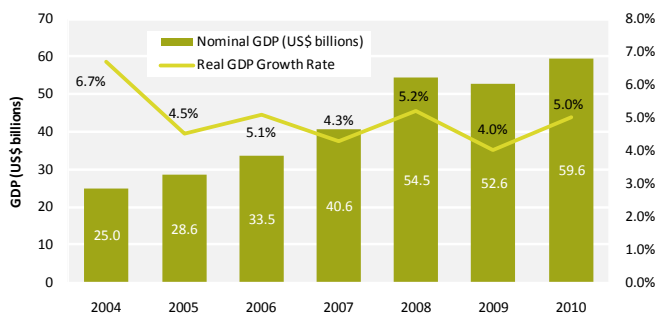
How Favourable are the Syrian Economic Indicators and the Political Developments in the Region?

The gradual liberalisation of Syria’s centrally planned economy is expected to continue; however, the economic debate on reforms remains highly charged. An improvement in international relations and the strategic developments in the region have prompted Syria to play a key role in the Middle East peace process. Syria’s economic performance in 2010 highlights the improvement in its economic climate and supports the future indicator forecasts. Some of the initiatives intended to increase domestic and foreign investment include offering infrastructure investment opportunities to private investors, expanding the Damascus Securities Exchange, relaxing foreign-currency restrictions and boosting bank lending. We summarise the economic indicators as follows.

- The Economist Intelligence Unit (EIU) Syria Country Forecast (November 2010) projected national GDP growth for Syria at 4.2% for 2010 and 4.6% for 2011;
- The EIU has revised the forecast consumer price inflation for Syria in 2010 to 2.9% and 4.4% for 2011, up from 2.6% in 2009. The hotel and restaurant sector ranked second, after education, in posting a year-on-year increase of 14% to the Consumer Price Index (CPI);
- The Central Bank of Syria is expected to continue to implement monetary reforms and reduce restrictions on foreign-currency transactions in order to facilitate foreign investment;
- These measures are expected to help in developing and modernising the banking sector, in which privatised banks can now be 60% foreign owned. In October 2010, the government passed a law allowing the establishment of investment banks, albeit with a high minimum capital requirement. EFG-Hermes, an Egyptian investment bank has already begun operations.

The real estate sector registered a strong performance in 2010 with bright future prospects. While the hospitality sector consolidated on its performance from 2009, retail and office markets witnessed corrections owing to increased supply and remained relatively stable for most of the year. In a recent survey by Cushman & Wakefield, Damascus was ranked as the fourth most expensive retail location among the top ten regional countries surveyed with annual rents of approximately US\$5,000 per square metre. Damascus was also ranked fifth most expensive city for office space among regional cities with an annual rental cost in the capital's Central Business District standing at US\$1,875 per square metre. The pipeline of various projects amounts to approximately US\$2 billion for the coming years. We summarise the key initiatives that have prompted investment in the real estate sector, with emphasis on the hospitality sector.

FIGURE 2: SYRIA'S GROSS DOMESTIC PRODUCT



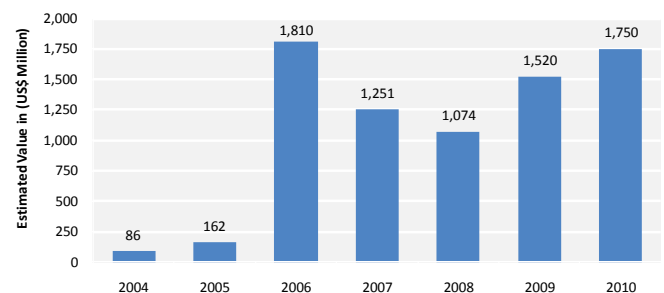
Sources: IMF; HVS Research

- The government's initiatives aimed at attracting tourism investment were extended to include exemptions such as waiving customs and income taxes for hotels' imports for seven years, increasing the exemption period to ten years in the eastern region, and decreasing income taxes by 20% in tourist development areas;
- A comprehensive reform process addressing the economic, financial, legislative and banking sectors gathered

momentum in 2010. The sixth Investment Forum proposed an integrated package of administrative procedures and financial investments in order to develop the business environment and attract investment in tourism projects;

- Lending facilities for home ownership have been relaxed, thus facilitating access to finance. Also, in addition to simplifying the tax structure and reducing the tax rate, the government has launched GCREDI (the General Commission for Real Estate Development and Investment) to oversee related developments in the country. This is expected to stimulate investment in this sector even further;
- Low interest rates, limited alternative investment opportunities in the market and high demand driven by Iraqi immigrants made real estate the preferred choice for investors. The real estate sector has also attracted large investments from local investors and Syrian expatriates;
- While the new laws have already resulted in a number of major new project announcements, it is noteworthy that the majority of these have yet to start construction. The implementation of the proposed reforms will decide the pace of future developments;
- The general real estate market in Syria has been on the rise since 2006 and is now thought to employ around 15% of the active population. The US\$1 billion project by the Majid Al Futtaim group to develop a tourist city outside Damascus; the development of a new holiday resort on the

FIGURE 3: INVESTMENT VALUE OF PROJECTS UNDER CONSTRUCTION



Source: Ministry of Tourism, Syria

Mediterranean coast by real estate company Qatari Diar at a cost of US\$350 million; the US\$8 billion Snobar project near Latakia; and the Antardus project in Tartous at a cost of nearly US\$200 million, which will be managed by the Wahoud group, are the most significant developments in the pipeline. In addition, restorations are taking place in Aleppo, a historic city in Syria where a number of archaeological sites and dwellings (the 'Dead Cities') have been discovered on the banks of the Euphrates River;

- Overall tourist investment in recent years amounted to US\$4.4 billion, with the value of investments currently under construction amounting to US\$6.3 billion. This figure reflects the success of the government's initiatives in attracting investment for real estate and tourism projects.

How is the Investment Climate?

As per the Ministry of Tourism, 94% of tourism investment is made in Damascus, Aleppo and the Syrian Coast. The Ministry of Tourism is seeking to promote and encourage investors to build new projects beyond the six governates. BOT (Build-Operate-Transfer) has been a successful model to attract tourism investors to Syria. It allows the investor to establish a Syrian company with the aim of financing, equipping, completing and operating the project. Damascus has limited availability of commercial plots for future developments. With most of the prime land in state hands, the government is using it as collateral to attract investment while maintaining ownership. The Ministry of Tourism has also invited developers who wish to purchase more than 250,000 m² of land to pitch their visions and master plans for large-scale developments. This flexibility has encouraged developers to propose various mixed-use projects with innovative concepts.

The reduced controls on banking and investment are expected to support the hospitality sector with direct investment from regional and international investors.

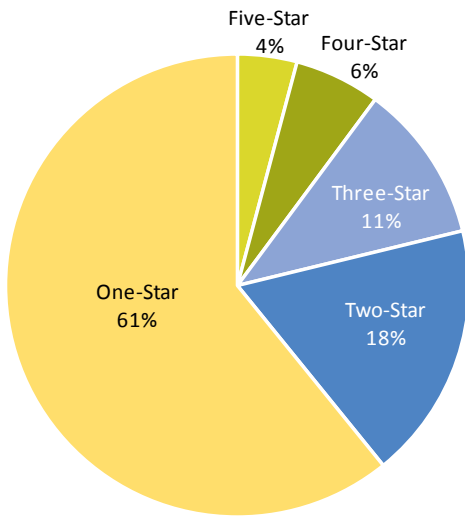
The Syrian government has focused its efforts on improving the investment climate in the country. Tourism development in particular has been targeted with initiatives from the Ministry of Tourism designed to ease bureaucracy and provide financial incentives to promote private investors. Banks are only allowed to lend up to 25% of their paid up capital to one entity. While new legislation has increased the minimum capital requirement for a new bank from US\$97.1 million to US\$194.2 million, it will still remain challenging for the developers of big master plans to secure financing from a single bank. According to the Bank Audi report in December 2010, in an effort to increase lending further, Syrian authorities have reduced the compulsory reserve requirements for commercial banks on the basis of lending volumes provided to small and medium-sized enterprises (SMEs), industrial and tourism projects and micro-finance institutions.

The reduced controls on banking and investment are expected to support the hospitality sector with direct investment from regional and international investors. The hospitality sector is expected to witness an increased inflow on the back of modest global and regional economic recovery.

What is the Composition of the Damascus Hotel Market and what are the High Points of Hotel Performance?

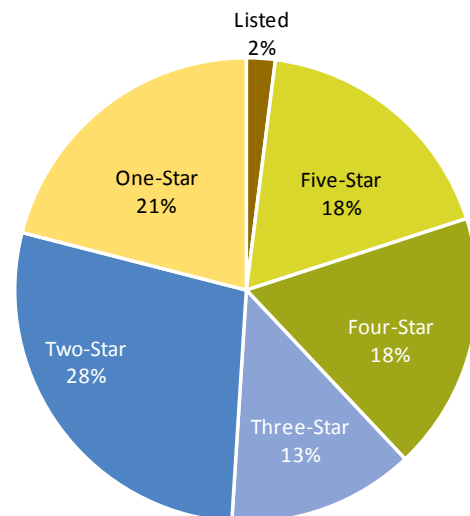
At present, hotel supply in Damascus is in excess of 225 properties across all categories. The market is undersupplied in the branded hotel category with just three international brands (Four Seasons, Sheraton and Dedeman) and one local brand (Cham Palaces & Hotels). In addition, there are many old houses in the Old City of Damascus which have been restored and converted into hotels. These hotels generally have a relatively smaller room inventory and are popular amongst European tourists for the distinctive experience of holidaying in the corridors of history. In the absence of any heritage hotel classification, these hotels follow the regular rating system.

FIGURE 4: HOTEL SUPPLY IN DAMASCUS BY CATEGORY



Sources: Ministry of Tourism; HVS Research

FIGURE 5: GUESTS BY PERCENTAGES IN ALL CATEGORIES OF HOTELS



Sources: Ministry of Tourism; HVS Research

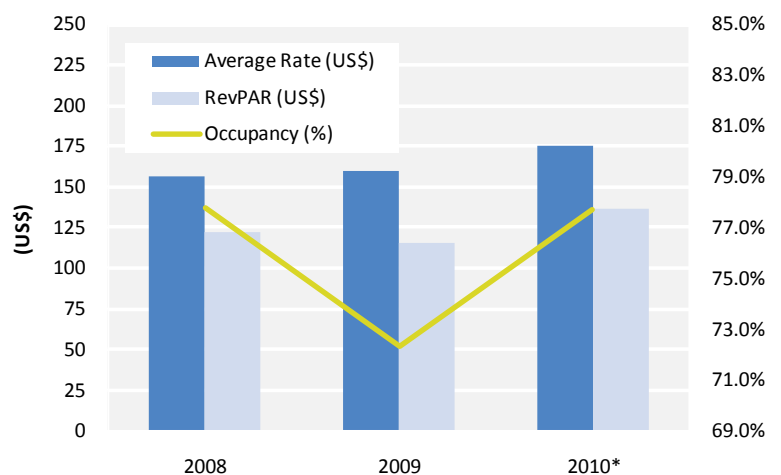
Of all the guests staying in the hotels in Damascus, 36% are captured by the four- and five-star categories. In the high season (April-May and July-September), the city experiences a constant shortage of rooms and almost all the hotels in these segments have to turn away custom. The period of October-December attracts high levels of corporate and MICE demand. With a limited supply of hotels in these categories, the Damascus hotel market offers great potential for investment in the upscale segment.

The listed, two-star and three-star categories of hotels in Damascus leave a lot to be desired when compared to the equivalent international standards of facilities and upkeep. Some of the hotels do not have a website and sell the facility through tour operators or rely on repeat clientele. As this segment of hotels captures the majority of demand in the city, there are remarkable opportunities to invest in the development of budget hotels which meet the expectations of the discerning traveller at a reasonable cost.

The availability and standard of trained manpower is another major challenge faced by hoteliers in Syria. In the World Economic Forum’s Travel and Tourism Competitiveness Report 2009, Syria ranked 93rd of the 133 countries for its human resources and 112th with regards to the extent of training.

2008 was a remarkable year for the hotel industry in Syria and Damascus in particular. Hotels posted impressive year-end results with growth in occupancy and average rates. The events in Gaza and the global economic slowdown had put the downward pressure on occupancy levels in the first quarter of 2009. However, high average rates and a pick-up in demand in the next three quarters of the year produced reasonable year-end results. The spiral effect of the economic slowdown delayed several announced hotel projects, as the petro-dollars of the investors witnessed a sudden squeeze.

FIGURE 6: HOTEL PERFORMANCE OF INTERNATIONALLY BRANDED HOTELS: OCCUPANCY, AVERAGE RATE AND REVPAR – DAMASCUS



Source: HVS Research; *estimated

In our estimation, 2010 witnessed a gradual increase in average rate and occupancy levels, and thus posted higher RevPAR figures across all categories. The overall performance of the market is robust; although our analysis depicts the performance of the internationally branded category, independent and local hotels, like Omayad Hotel, Semiramis, Yafour Hotel and Resort and so forth, also matched occupancy levels and registered growth in average rates over the year. With increased demand, low supply and scheduled refurbishment plans of prominent hotels, we expect 2011 to perform better in all areas.

What is the Current and Future International Branded Hotel Supply in Damascus?

Damascus enjoys a central location with an overall population of 2.4 million, of which 1.7 million live in the city and approximately 690,000 in the surrounding areas. As the tables depict, with a large population base and as the hub of all the commercial, administrative and leisure activities in the country, Damascus is undersupplied with only 933 existing and 1,613 upcoming rooms in the internationally branded category. The largest fraction of this room supply will materialise in 2013. The above list does not include the projects that are either at the planning stage or have not yet broken ground.

FIGURE 7: EXISTING SUPPLY OF INTERNATIONALLY BRANDED HOTELS – DAMASCUS

Property	Category	No. of Rooms	Opening Year
Four Seasons Hotel	Five-Star	297	2006
Sheraton Hotel	Five-Star	283	1978
Dedeman Damascus	Five-Star	243	1976
Queen Center Arjaan	Four-Star	110	2005
Total		933	

Source: HVS Research

The city has a limited number of commercial plots available for future development and as a result the boundaries of the city are extending out. A number of new projects have been announced, some of which are already under construction, in the surrounding areas such as Sabboura and Yafour. These developments will shift the centre of the city from the densely populated Old Town towards the Lebanese border.

As economic activity gathers momentum, the high end of future demand will be captured by the branded luxury hotels, leaving the budget category of hotels capturing the remaining demand. Our analysis clearly outlines a market that is undersupplied and offers opportunities to build hotels across all categories in Damascus.

FIGURE 8: BRANDED HOTELS PIPELINE, CONFIRMED SUPPLY – DAMASCUS

Property	Status	Category	No. of Rooms	Opening Year
InterContinental Damascus	Under Construction	Five-Star	370	2012
Mövenpick Hotel	Development on Hold	Five-Star	268	Unknown
Kempinski Hotel Sulaiman Bacha Khan	Development on Hold	Five-Star	30	Unknown
Kempinski Hotel Damascus	Development on Hold	Five-Star	214	Unknown
Holiday Inn Damascus	Under Construction	Four-Star	300	2012
Yasmeen Rotana	Under Construction	Five-Star	341	2013
Kempinski Hayat	Under Rehabilitation	Four-Star	90	2013
Total			1,613	

Source: HVS Research

What are the Other Significant Hotel Developments in Syria?

While Damascus and Aleppo still attract the majority of investments, the Syrian government is focusing on harnessing the distinctive historic and cultural heritage of the whole country and is encouraging investors to look at other potential destinations as well. Palmyra and coastal areas have witnessed growing interest from investors in recent years and we expect future developments in Syria will be more diverse geographically. We summarise the key developments in Syria below.

- Jumeirah Group, the Dubai-based luxury hotel group, has signed a letter of understanding with Souria Holding to manage Jumeirah Abraj Souria, a five-star hotel in the Baramkeh area of Central Damascus. The mixed-use development, covering 300,000 m², will comprise commercial and retail components, including a shopping mall and an office tower. The project is expected to be completed in 2015;
- Phase II of Emaar's Eighth Gate project is expected to include two hotels;
- Majid Al Futtaim Properties is expected to develop two hotels in the Yafour area;
- Rotana Hotels operates the Afamia Rotana Resort in Latakia and has signed a management agreement for the Gardenia Rotana in Homs. The hotel will have 280 rooms and suites, and is expected to open in 2012;
- Accor Group has signed a management agreement with Syria's Bena Properties to manage two properties at the Taj Halabin Aleppo mixed-use development. With 129 and 150 keys, respectively, the four-star Novotel and three-star ibis hotel are Accor's first projects in Syria;
- Safir Hotels and Resorts has signed a deal with the Syrian Al-Chami Company to manage a Safir Hotel in Aleppo. The hotel is expected to be ready in 2012 and will have 158 rooms;
- Qatari Diar Syria is developing Ibn Hani Bay Resort project in Latakia which will have two hotels and a number of serviced apartments;
- The Porto Tartous project is being developed by Wahoud Group and Amer Group, Syria. It will have a five-star hotel as part of a mixed-use development. Concord Tartous, a 250-room hotel, is also being developed by Wahoud Group and is expected to be completed in 2011.

What are the Potential Red Flags?

- Our primary research reveals that some of the approved hotel projects are on hold, either after breaking the ground or in the construction stage. Damascus is an ancient city and finding archaeological ruins while excavating is not uncommon; however, seeking the necessary permissions to continue construction has delayed proceedings in many cases;
- Many international hotel operators are keen on entering Damascus and Syria. However, limited brand presence and approvals for future expansion remain questionable;
- There are two international airports in Syria – Damascus and Aleppo. Despite the recent renovation, the overall facilities and feel of the airports is not comparable with the international standards that modern travellers expect and requires further expansion to support increasing visitor numbers;
- In the World Bank's latest 'Doing Business Report', Syria ranked 132nd out of 181 countries in dealing with construction permits. The pace of business reforms will determine the future of investment in Syria.

Conclusion

Syria's emergence as a competitive tourism destination has attracted a significant number of investors. The macroeconomic indicators, increasing visitor numbers and strong performance of its hotels have contributed significantly to sustaining growth levels. According to the Syrian Ministry of Tourism, travel and tourism investments in Syria between 2007 and 2009 stood at US\$4 million; whilst the value of travel and tourism investments already in operation is US\$4.1 billion, those investments under construction are worth US\$6.3 billion. These levels of investment have revived the travel and tourism industry and made it a key element in Syria's economic revenue. While the sluggish pace of developments is mainly attributed to the aftermath of the global economic slowdown, Syria will have to ensure that the banking and real estate reforms continue at a brisk pace. In order to attract investors, a professional decision-making and execution mechanism along with an improved regulatory framework is necessary. The Syrian Ministry of Tourism has taken an active interest in facilitating investment in the sector; however, the overall improvement of airports, road and rail transportation and the development of a skilled workforce will decide the future of Syrian hospitality industry.

The hotel market in Damascus and Syria is undersupplied, both in terms of number of rooms and the presence of international management companies. Strong demand, low supply, proposed renovations and an uncertain future supply timeline will continue to strengthen the Damascus hotel market's performance. The Damascus hotel market is poised for strong occupancy and average rate performance in the short to medium term and has the potential for the development of new hotel properties, across all categories.



About HVS

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HVS has a team of Middle East experts that conducts its operations in the Middle East and North Africa. The team benefits from international and local cultural backgrounds, diverse academic and hotel-related experience, in-depth expertise in the hotel markets in the Middle East and a broad exposure to international hotel markets. Over the last four years, the team has advised on more than 100 hotels or projects in the region for hotel owners, lenders, investors and operators. HVS has advised on more than US\$10 billion worth of hotel real estate in the region.

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