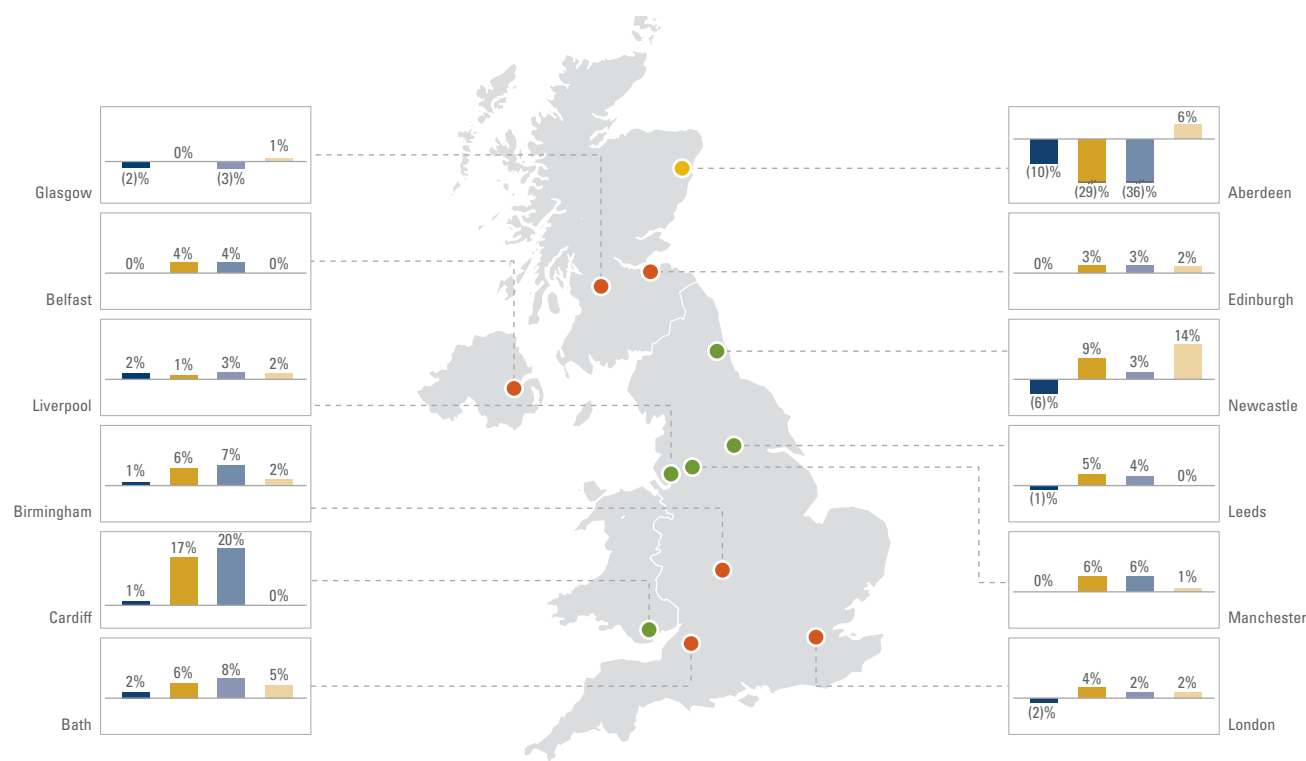


Hotel Bulletin: Q4 2015

The majority of the 12 cities reviewed in the Hotel Bulletin recorded RevPAR growth throughout 2015. The top performer this quarter, Cardiff, was able to capitalise on demand generated by hosting a number of Rugby World Cup matches. Despite hosting the most matches, London’s performance in Q4 2015 was suppressed by dwindling Christmas shopper footfall. Total transaction values in 2015 surpassed pre-downturn levels for the first time, largely due to a strong final quarter. This Hotel Bulletin highlights potential investment opportunities in the UK airport hotel sector and analyses the markets around Gatwick and Heathrow to determine investor opinion on the new runway debate.

FIGURE 1: Selected UK hotel markets – demand and supply



■ Occupancy percentage change⁽¹⁾ (Q4 Y-o-Y) ■ Average room rate percentage change (Q4 Y-o-Y) ●●● Active pipeline >10%, 5% to 10%, <5%
■ RevPAR percentage change (Q4 Y-o-Y) ■ Supply percentage change since 31 December 2014

Notes: Q4 covers the three months to the end of December | Q4 Y-o-Y compares the average of Q4 2015 to the average of Q4 2014 | Supply and pipeline analysis relate to numbers of hotel bedrooms |
(1) Occupancy percentage change represents actual rather than absolute percentage change | Active pipeline refers to hotel bedrooms with a confirmed opening date in the next three years.

Demand

London unable to convert Rugby World Cup demand

In comparison with double digit growth recorded last year, RevPAR growth in 2015 was subdued for the majority of cities reviewed in the Hotel Bulletin. In Q4 2015, occupancy levels fell for eight of 12 cities. In a continuing trend, rate rises mitigated the impact of this, resulting in overall average RevPAR growth of 2% in comparison to Q4 2014. Flat or declining occupancy is historically followed by plateauing rates, indicating that a peak in hotel trading may nearly have been reached.

For the fourth consecutive quarter, London recorded occupancy decline (2%) compared with the previous year despite hosting Rugby World Cup matches in October, including the final. Q4 figures were weakened by poor December performance (9% fall in RevPAR compared with December 2014) as fewer visitors travelled to the city for Christmas shopping. Footfall in London in December was down 5% on 2014 figures¹ as online shopping activity increased² and anxious travellers stayed away following the terrorist attacks in Paris in November.

Cardiff was the top performer for a second consecutive quarter with 20% RevPAR growth. The Welsh capital hosted five Rugby World Cup matches in October which lifted demand metrics, in particular average room rate, for the quarter as a whole.

Aberdeen has been the worst performer of the 12 cities reviewed for every edition of this Bulletin in 2015. Oil and gas companies have made severe cuts to investment and corporate spend in response to oil prices falling by around 75% since June 2014³. Hotels in the city are heavily exposed to corporate trade and, as such, have felt the full effect of this trend. In Q4 2015, RevPAR fell by 36%, the largest quarterly decrease recorded to date. With the World Bank having recently lowered its forecasts for oil prices and active pipeline at 10% of current supply, a significant recovery in performance in Aberdeen is not expected in the short to medium term.

Glasgow’s hoteliers recorded a small decrease in RevPAR (3%). This is in comparison to strong demand growth in Q4 2014 when the city hosted high profile events including the MTV Europe Music Awards and the 2014 Sports Personality of the Year Awards. In comparison to Q4 2013, RevPAR grew significantly (37%) in 2015.

Investment indicators

Although high-level demand and supply metrics alone will never fully inform an investment decision, the chart below is intended to highlight demand and supply data for cities that may attract, or concern, investors.

The interaction of demand growth, historical supply change and active pipeline are considered. Demand growth has been calculated as the average RevPAR growth for the last four quarters to provide an indication of recent demand trends. Historical supply change has been calculated as the increase in rooms in the last two years to allow for an appropriate amount of time to contextualise recent trading performance. Active pipeline has been included in the analysis to provide an insight into each city’s hotel market in the upcoming years. Only hotel bedrooms with confirmed opening dates are included.

Belfast has consistently recorded high demand growth throughout the year (9% average), making it a seemingly attractive prospect for investors. However; this market has been untested by new supply with no new bedrooms opening in 2015 and only 35 new bedrooms in 2014. Including closures, supply in the city has declined by 1% over the past two years. As such, investors may be concerned about performance once the current pipeline (15% of supply) reaches the market.

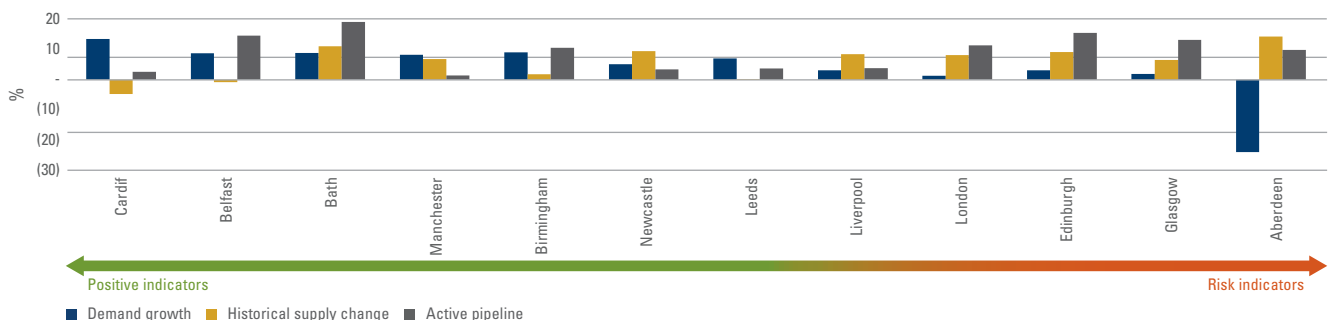
The Hotel Bulletin now provides investment indicators for each of the 12 cities analysed for the previous four quarters (Figure 7 to Figure 18) in order to illustrate the changing profile for each city over the year.

After strong performance in Q1 2015, Glasgow’s demand levels have gradually declined while maintaining a relatively large active pipeline. As such, the city has moved toward the risk end of the spectrum in Figure 2.

The investment indicator graphs show a pattern of decline across the majority of cities. Demand growth figures have fallen over the year for all 12 cities. In absolute terms, average RevPAR year-on-year growth has declined by 10%.

Source: 1. FootFall (UK) Regional Index, 2. The Guardian, 3. Brent Crude Index

FIGURE 2: Investment indicators



Source: AM:PM, HotStats

Notes: Demand growth calculated as the average quarterly RevPAR change for the last four quarters | Historical supply change calculated as the change in hotel bedrooms between December 2013 and 2015 | Active pipeline calculated as the active pipeline as a percentage of current supply | The shading of the arrow reflects positive (green) or risk (red) indicators.

Supply and pipeline

In Figure 3 below, we compare the proportion of current supply (inner circle) and active pipeline (outer circle) in the UK market by sector. In a continuing trend, the budget sector makes up the largest portion of total UK supply and active pipeline. Three star hotels account for only 3% of current active pipeline as the grading continues to be squeezed between limited and full-service hotels.

Over 10,000 bedrooms opened in the UK in 2015 and a further 16,000 are expected to come onto the market in 2016.

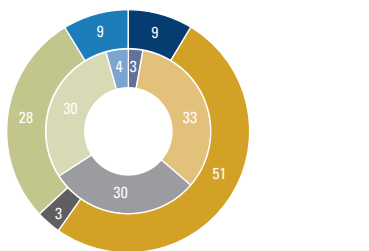
Approximately 7,000 bedrooms of these are due to open in London, more than double the number opened in 2015. Even London hoteliers, used to robust performance in almost any conditions, may be concerned by this large impending increase in supply given recent limited demand growth in the city.

Edinburgh’s hotel market is due to gain 1,140 bedrooms in 2016, over half of which (682 bedrooms) relate to two Premier Inns and three hub by Premier Inns. This will increase Edinburgh’s supply of budget hotel bedrooms by 18% and increase Whitbread’s presence in the city by 69%.

Notable new openings and developments this quarter include:

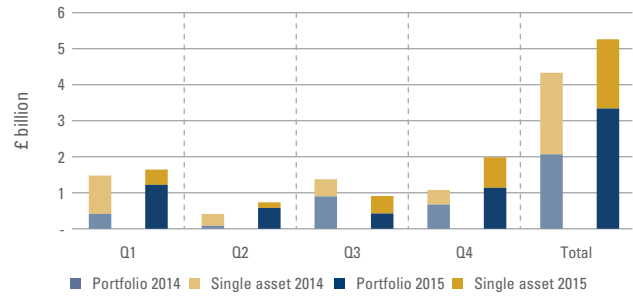
- ▶ Four new hotels (654 bedrooms) have opened under various Hilton brands in Q4 2015. These include the group’s first hotel in Oxford and the five star Hilton London Bankside, the opening of which increases its London hotel portfolio to over 10,000 bedrooms. Hilton Worldwide have also signed a franchise agreement with Urban&Civic for a 357 bedroom Hampton by Hilton (the largest in Europe) at Stansted Airport.
- ▶ Travelodge has expanded its presence in London to over 8,000 bedrooms following the openings of the 80 bedroom Travelodge London Hackney and the 78 bedroom Travelodge London Richmond. A further 391 bedrooms are due to open in London in 2016.
- ▶ IHG has opened the five star 453 bedroom InterContinental London – the O₂, the largest new UK hotel to open in 2015. The hotel is owned by AEG Europe and Queensgate Investments and is managed by Arora Hotels. Third party operators are increasingly being trusted with upscale, and even flagship, assets.

FIGURE 3: UK current bedroom supply and active pipeline 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 4: UK transaction value



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

Transactions

£2.0 billion of transactions completed in Q4 2015, of which £1.2 billion related to portfolio assets. The majority of this (£1.0 billion) was attributable to the sale of the Ribbon Portfolio of 22 IHG branded hotels, the final tranche of the previous LRG portfolio, to Apollo Global Real Estate.

The total value of transactions in 2015 (£5.3 billion) was £1.0 billion greater than the previous year. Total transaction value has now surpassed pre-downturn levels for the first time.

Two significant global corporate acquisitions were announced in the quarter. Marriott International has agreed to buy Starwood Hotels and Resorts for a reported \$12 billion. This transaction is expected to complete in mid-2016 and will create the world’s largest hotel company with 1.1 million bedrooms across 5,570 hotels in over 100 countries.

In addition, AccorHotels has agreed to buy luxury brands Fairmont, Raffles and Swissôtel for approximately €2.6 billion. The group of three brands includes 115 hotels and resorts with 43,000 bedrooms. The majority of the hotels acquired are under management contracts with approximately 30 years term remaining, which will provide long-term earnings visibility without impeding Accor’s asset light strategy.

It is unlikely that either acquisition will have a significant immediate impact on the UK branded hotel market. Starwood Hotels and Resorts only have ten hotels (2,738 bedrooms) in the UK and the group acquired by Accor only manages the Fairmont St. Andrews and The Savoy, London.

Notable transactions completed this quarter include:

- ▶ Following the completion of its purchase of the LRG Ribbon Portfolio, Apollo completed the back-to-back sale of the 906 bedroom Holiday Inn Kensington Forum for a reported £345 million to Queensgate Investments.
- ▶ A joint venture between NH Hotel Group and AXA Investment Managers purchased a development for a reported £89 million in London’s Tech City. The site is due to be developed into the UK’s first how hotel, the lifestyle brand of Spain’s NH Hotels. The 190 bedroom hotel is due for completion in 2019.

Focus on: airport hotels

In this edition of the Hotel Bulletin we have analysed the UK airport hotel sector to highlight potential opportunities for investors in this market. We have also taken a closer look at Heathrow and Gatwick, the two current front runners in the debate for expansion in London/the South East.

Hotel airport market investment indicators

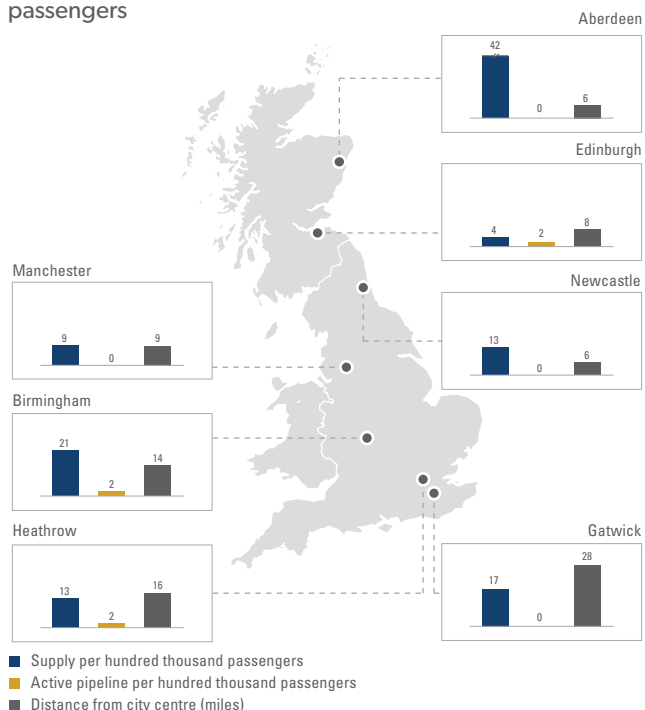
A number of factors underpin demand and investment decisions in the airport hotel sector. These include macro factors, such as GDP growth and disposable income, as well as location specific issues including destinations served, duration of flights and transport links to nearby city centres. Relationships between these factors can be complex. For example, current fuel prices are likely to enable greater spending on flights and hotels; however, political uncertainty may lead to some travellers staying at home.

Figure 5 compares hotel supply and active pipeline per hundred thousand passengers and shows distance to the nearest city for each hotel for seven UK airports to highlight markets that may have capacity for expansion. The average supply and active pipeline per hundred thousand passengers in 2015 were 17 and 1 respectively.

Edinburgh’s supply per hundred thousand passengers (4) is significantly below average and, as such, investors may consider there to be scope for additional capacity. However, the airport is a comparatively short distance from the city centre (8 miles), which has numerous attractions to draw passengers away from airport hotels.

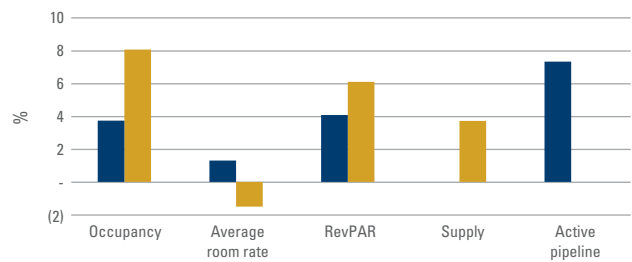
Aberdeen’s bedroom supply per hundred thousand passengers (42) is more than double the average of the seven airports examined despite its short distance to the centre of Aberdeen (6 miles).

FIGURE 5: Supply and active pipeline per hundred thousand passengers



Source: AM:PM, Civil Aviation Authority
 Notes: Supply and pipeline figures reflect number of airport hotel bedrooms per hundred thousand passengers in 2015 | Distance to the airport is measured in miles.

FIGURE 6: Heathrow and Gatwick: annual demand, supply and active pipeline growth



Source: AM:PM, HotStats
 Notes: Occupancy, average room rate and RevPAR refer to average percentage change compared with 2014. Supply refers to percentage change compared with December 2013. Active pipeline is measured as percentage of current supply.

The recent slump in oil prices has contributed to a 5% fall in passenger numbers compared with the previous year. Falling demand metrics and a seemingly oversupplied airport hotel market may concern hoteliers in this area.

Experienced investors are also likely to review developments in local markets closely. Birmingham has recently enhanced direct routes with China following runway expansion. Manchester Airport is planning £1 billion of investment which is forecast to increase annual passenger numbers by over 10 million in the next decade. There may be an opportunity in Manchester, where supply (9) is below average and there are no bedrooms in the active pipeline.

Gatwick or Heathrow for airport expansion?

Gatwick and Heathrow are the two largest airports in the UK in terms of passenger numbers. Heathrow reported over 70 million passengers in 2015 while Gatwick reported over 40 million.

The current debate surrounding London/South East airport expansion is centred on Heathrow and Gatwick. In July 2015, the Airport Commission recommended Heathrow for an additional runway; however, it is likely that the current debate will continue for the foreseeable future and certainly until after the London Mayoral elections in May. In this Focus, we have considered how recent demand and supply metrics and speculation about the location of the new runway impact investor decisions.

In 2015, Heathrow recorded 4% year on year RevPAR growth while Gatwick recorded 6% growth. The greater RevPAR increase in Gatwick is largely due to higher growth in passenger numbers in the same period (8% in Gatwick versus 2% in Heathrow). 443 bedrooms opened in Gatwick in 2014 whereas no bedrooms have been added in Heathrow since 2012. Strong RevPAR growth following a recent increase in supply indicates that the hotel market in Gatwick is robust and therefore seemingly attractive, albeit there were a number of closures in 2013 and 2014 which investors will factor into their assessment.

Heathrow has a much higher pipeline than Gatwick with 742 bedrooms in the active pipeline and 4,211 (49% of current supply) in the wider pipeline. In comparison, Gatwick has no bedrooms in the active pipeline and only 5% of current supply in the total pipeline. This information suggests that investors are confident in Heathrow expansion and are making investment decisions accordingly, despite stronger recent performance in Gatwick.

Source: AM:PM, HotStats

Investment indicators for Q1 2015 to Q4 2015

FIGURE 7: Glasgow

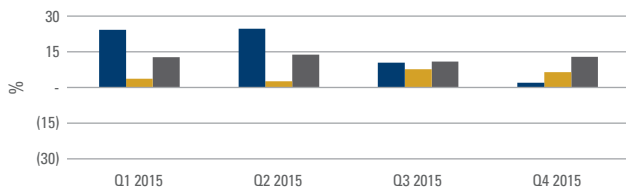


FIGURE 13: Aberdeen

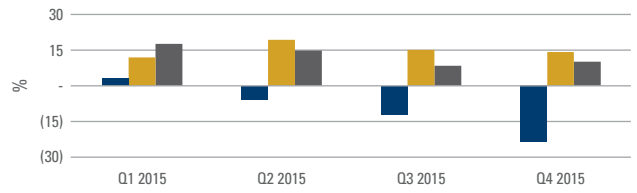


FIGURE 8: Belfast

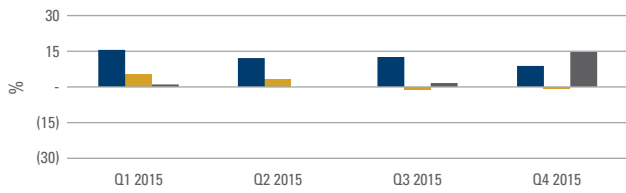


FIGURE 14: Edinburgh

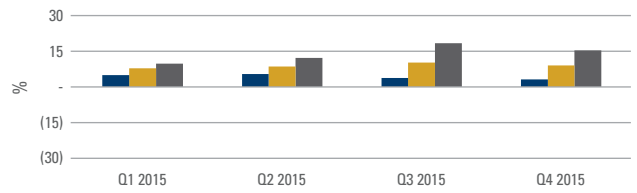


FIGURE 9: Liverpool

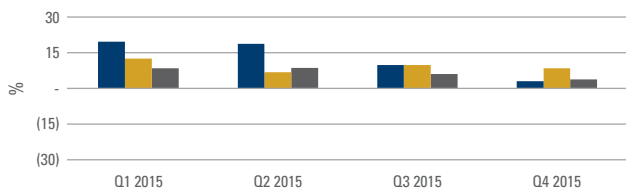


FIGURE 15: Newcastle

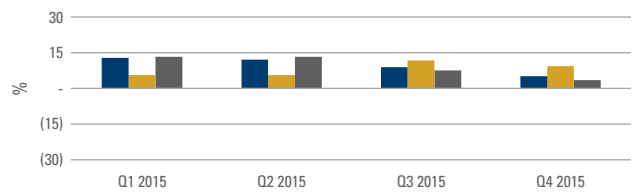


FIGURE 10: Birmingham

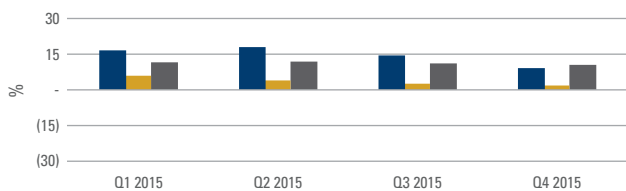


FIGURE 16: Leeds

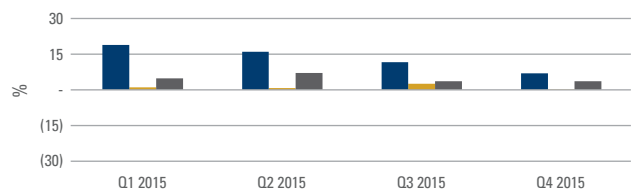


FIGURE 11: Cardiff

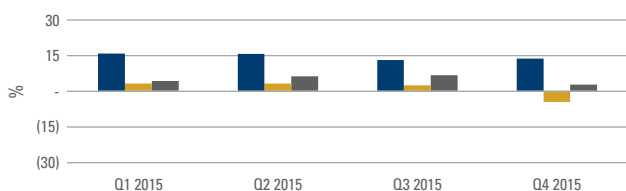


FIGURE 17: Manchester

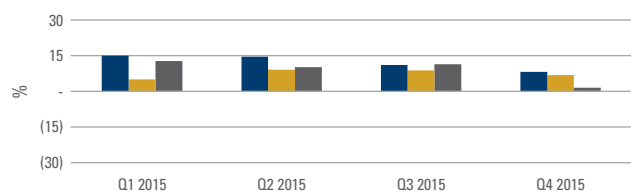


FIGURE 12: Bath

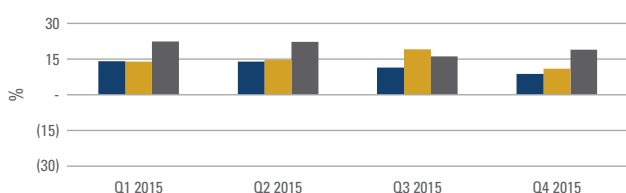
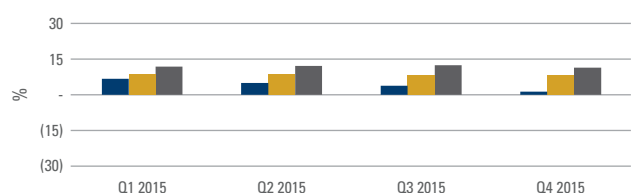


FIGURE 18: London



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 the active pipeline as a percentage of current supply.

FOR MORE INFORMATION, CONTACT:

Graeme Smith

Managing Director, AlixPartners
gsmith@alixpartners.com
+44 (0) 20 7332 5115

Russell Kett

Chairman, HVS
rkett@hvs.com
+44 (0) 20 7878 7701

Alan Gordon

Director, AM:PM
alan.gordon@ampmhotels.com
+44 (0) 188 783 0430

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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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