CBRE HOTELS

CBRE Hotels – HOTEL INVESTMENT

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CBRE Hotels
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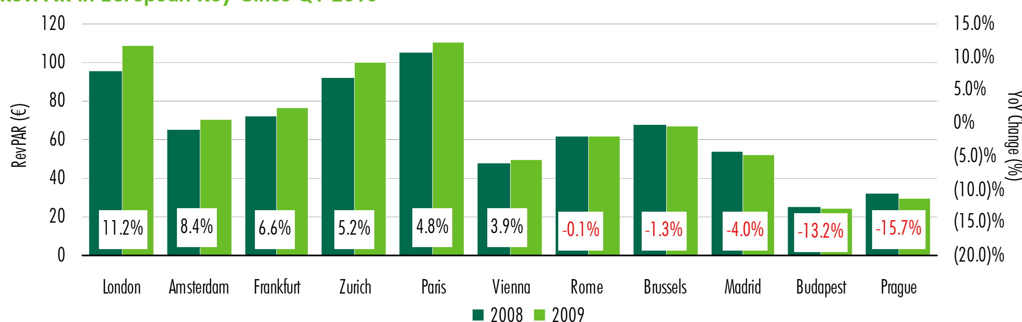
SNAPSHOT ON REVPAR

CBRE Hotels monitors the development of hotel market performance across EMEA. A summary of the RevPAR of major European capitals during the past three month and their performance for Q1 2010 compared to Q1 2009 is shown in the table below.

YEAR	MONTH	Amsterdam	Brussels	Budapest	Frankfurt	London	Madrid	Paris	Prague	Rome	Vienna	Zurich
		REVPAR (€)										
2009	Jan	€ 65.23	€ 58.42	€ 31.34	€ 76.90	€ 102.18	€ 73.79	€ 117.22	€ 26.58	€ 72.47	€ 57.54	€ 85.21
2009	Feb	€ 80.12	€ 74.03	€ 33.41	€ 87.36	€ 116.07	€ 94.39	€ 108.75	€ 31.58	€ 97.40	€ 56.31	€ 83.95
2009	Mar	€ 108.43	€ 94.83	€ 41.47	€ 76.00	€ 123.17	€ 94.02	€ 135.31	€ 36.91	€ 117.69	€ 83.54	€ 111.64
2009	Q1	€ 65.31	€ 67.80	€ 24.98	€ 72.13	€ 95.28	€ 54.04	€ 105.37	€ 32.10	€ 61.91	€ 47.75	€ 91.85
2010	Q1	€ 70.77	€ 66.94	€ 24.49	€ 76.90	€ 108.55	€ 51.86	€ 110.39	€ 29.23	€ 61.86	€ 49.63	€ 99.63
	Change[1]	8.4%	-1.3%	-13.2%	6.6%	11.2%	-4.0%	4.8%	-15.7%	-0.1%	3.9%	5.2%



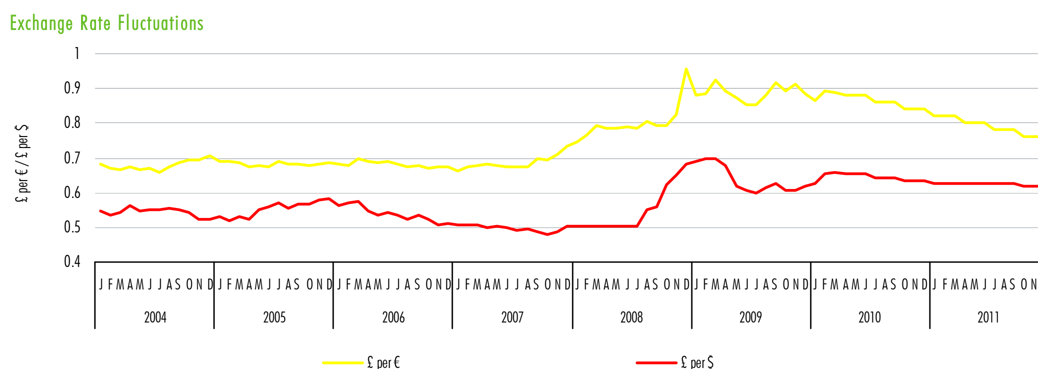
Source: STR Global

[1] Year-on-year change based on local currency to avoid distortions from exchange rate fluctuations.

- Data for London comprises Central London only; Paris refers to Paris Ile de France.
- There is a clear split between north-west and south-east Europe: Stronger markets with typically higher RevPAR (€) exhibited positive year-on-year growth during the first quarter, whereas southern and eastern European cities continued to see year-on-year RevPAR decreases, from already low RevPAR (€) levels.
- Currency fluctuations impacted on Budapest's and Prague's RevPAR, which if expressed in € shows less of a decline on Q1 2009. For London and Zurich, on the other hand, year-on-year RevPAR growth is higher if based on RevPAR (€) than if expressed in local currency.
- Overall, London's RevPAR stands out, as it shows the highest level both nominally (expressed in € for this comparison) and year-on-year growth. Because percentage increase becomes more and more difficult to achieve the higher the nominal figure is, this only shows London's impressive resilience in 2009 and the start of a recovery in 2010 – sending positive signs to Europe that the downturn might be shorter lived than feared.

WHAT ARE THE MOST INTERESTING MARKETS TO INVEST IN AT THE MOMENT?

- **London is hot again!** The London hotel market surprised many market forecasters with the resilience of its trading performance during the recession, across all sectors, and appears to be leading the way towards recovery, as shown in the market snapshot. From an investor point of view, a solid performance is enhanced by the current exchange rates, with a weak pound working to the investors' advantage



Source: CBRE Research (Jan 2004 – Mar 2010), RBS Exchange Rate Forecast (April 2010 – Dec 2011)

- **UK Gateway Cities coming back.** Hotels in destination cities, like Edinburgh, or those in strong airport locations in the UK, also benefit from the lack of supply coming to market in London. The weak Sterling is a window of opportunity for international investors to target the UK, and the lack of available product in the market for London means investors do consider alternative options – if market conditions are considered solid and the product offered is an attractive opportunity.

- **Continental Europe remains cautious.** Most countries in Continental Europe appear to be lagging the trend in the UK by up to a year or even more in terms of Capital Markets activity, as was true at the start of the recession. Investors are particularly cautious when looking at Central and Eastern Europe, for during the economic downturn, the rise in uncertainty in respect of both trading and future yield movements triggered most investors to focus on domestic investment opportunities and markets with proven track record, rather than trying to make a quick buck from opportunities in newer markets.

- **European trophy assets remain strong.** Although investors remain cautious when looking at European hotel investments as a whole, trophy assets will always attract interest. Buyers range from international hotel investors including private equity and sovereign wealth funds, hotel companies, as well as high net worth individual and institutional investors. With very little product in the market at the moment, and many opportunity funds waiting for their break to come, trophy assets will still be able to command sharp yields.

- **Nothing but prime!** For hotels, investor focus has clearly restricted to prime opportunities only, and any secondary investments – be it by location, type of income, asset condition or performance – remains difficult to sell, if at all. Hotel investments typically follow the trend laid out by commercial property investment, however, with a slightly longer lead-in period. The length of this lead will depend on how much supply comes to the market and how yields will develop as a consequence of that.

- **More cash then they can spend.** Overall, there's a large amount of equity, both on-shore and off-shore, seeking a home. However, with many hotel owners waiting for prices to recover, little product is being offered for sale in the market. Additionally, debt availability remains an issue, albeit one showing signs of improvement. With loan-to-value ratios much below those of the previous boom years, Internal Rates of Return (IRR) and in turn hotel values remain under considerable pressure.

ARE LEASE CONTRACTS MORE INTERESTING AT THIS MOMENT THAN MANAGEMENT CONTRACTS?

- In anticipation of more secure and predictable income streams, leases are often favoured over management agreements, certainly by institutional investors but also increasingly by alternative investors that lack the asset management savvy and experience to extract value from management deals.

- Investor appetite for leases shows a similar flight to security and predictability of income; in particular institutional investors seek the reliability of fixed income streams, even if offering less upside in the foreseeable future than their performance-linked counterparts. However, with a wall of institutional capital facing very few deals in the prime market place, many institutional investors are forced (and have started) to also consider more secondary opportunities, both in terms of market and type of income.

- All of this applies to existing leases. However, considering the current vulnerability of the market and its overall weak trading performance, many investors are hesitating to enter into new lease agreements, as they fear they could achieve better lease terms once the market has (at least partly recovered). For the same reasons, those operators confident enough to take a lease could obtain very favourable lease terms in the current market, as they have only limited competition, since most operating companies are not in a position to assume the liability of fixed rental payments.

- Overall, we expect demand and value for leases to increase as covenants start to strengthen again. Key factors are: a stable fixed income with CPI or RPI link (preferably annually); good physical condition of the assets with minimal capex requirements; and a reasonable ratio of rent to EBIDTAR (around 1.5x).

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