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The intelligence source for the hotel investment community

The UK-REIT arrives

The new tax exempt structure will drive change

The UK Budget delivered a friendly-than-expected approach to Real Estate Investment Trusts.

The much-feared conversion charge was set at a reasonable 2% of gross assets and can be spread over four years. And the great bulk of the rest of the detail is friendly towards the property industry and, more narrowly, the hospitality sector.

Another fear prior to the Budget, for example, concerned distribution requirements. Rather than being set at 95%, as was previously suggested, these are now at 90% after capital allowances.

Mark Nichols, tax partner at law firm CMS Cameron McKenna, said that it appears that there will now be a significant take-up of REIT status by existing quoted property companies once the new regime comes into effect in 2007.

Less clear, however, is whether private property groups, almost all entirely held offshore, will decide to adopt the new status. Nichols pointed out that as such entities are already effectively tax free, there is little advantage in paying the 2% conversion charge.

Tax advisers Chiltern, parent of Chiltern Mondiale, the group that bought the 11 Courtyard by Marriotts in November 2004 from Whitbread, said that it was encouraging that the Government had been prepared to listen to industry representation.

Among the examples it cited was the fact that the interest cover requirement has been reduced from 2.5 to 1.25 times, allowing the possibility of gearing around the 60% level.

But it considered the conversion charge as being set at a high level. It also criticised the restriction regarding the ownership of interests in UK REIT. This restricts investors to holding no more than 10% without incurring some tax (although the REIT status will not be completely lost as was at first feared).

For hotel owners, there is the added complexity concerning management contracts. For budget players, such as Travelodge or Accor's Ibis and Etap brands, leases are acceptable.

For midmarket and upscale hotels, however, leases are generally not acceptable, at least for Anglo-Saxon companies.

In such cases, another entity will have to be created to own the lease. The hotel operating company will then have a management contract with this tax paying entity.

Although more complex, it does not rule out REITs as a possible vehicle for upmarket hotel properties.

The big win for hospitality was in persuading the Government that leisure trading companies should be acceptable property types for REITs. In the first draft of legislation published in March 2004, leisure trading companies were specifically excluded.

Hotel Analyst, together with CMS Cameron McKenna and Jones Lang LaSalle Hotels, formed an industry lobby effort to change the Government's mind. Later joined by the British Hospitality Association, the push succeeded.

HA Perspective: REITs matter to the hotel sector for two reasons: firstly, they are an important potential source of fresh capital and, secondly, a hotel REIT will put hotel property firmly on the map as an asset class in its own right alongside offices and retail.

Although the first reason can be overblown – they are never likely to become the primary source of capital – hotel REITs will have an important impact.

In particular, REITs offer an exit route for much of the private equity that has gone into UK hotels in the last couple of years. And for owner-operators of hotels, it is another route through which property can be split from brand and operations.

The second reason is just as important. Despite attempts by Investment Property Databank to establish an index like its existing products in office, retail and industrial property, it has to date failed to find sufficient information to create a reliable monitor.

Without such an index, institutional investors will remain wary of hotels and treat them as an exotic play that is expected to make higher returns due to its perceived higher risk.

But a viable hotel REIT structure should help calm such fears and provide a source of low cost capital to the industry.

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Editor **Andrew Sangster**
t +44 (0)20 8870 6388
e andrew@hotelanalyst.co.uk

Marketing **Sarah Sangster**
t +44 (0)20 8870 6388
e sarah@hotelanalyst.co.uk

Design **Lynda Sangster**
t +44 (0)20 7378 1457
e l.sangster@langsford.co.uk

Hotel Analyst is published by
ZeroTwoZero Communications Ltd
Studio 23 Royal Victoria Patriotic Building
Fitzhugh Grove London SW18 3SX
t 020 8870 6388 **f** 020 8870 6398
e info@zerotwozero.co.uk
w www.zerotwozero.co.uk

Whitbread at the centre of the storm

Comment by Andrew Sangster

The whispering about corporate activity at Whitbread is again picking-up with the leisure conglomerate now being tipped to launch a bid for budget hotel chain Travelodge.

Such a move seems the only way that the company will end the persistent break-up rumours surrounding it.

Early last summer, Whitbread hit the headlines with reports that private equity firms were lining it up for a break-up. As a former national newspaper financial hack, your correspondent understood the scenario well: the VCs fancied a go at Whitbread, didn't want to go hostile and so thought a few well-placed leaks might pile on the pressure. It has.

Whitbread is now the only large cap travel and leisure stock on the London exchange that can be easily labelled a conglomerate. Barely 10 years ago, investors would have struggled to find anything but leisure conglomerates.

Ladbrokes (now Hilton) was gaming and hotels, Bass (now Mitchells & Butlers and InterContinental) was pubs, bingo, brewing and hotels, Scottish & Newcastle was pubs and brewing, Allied Domecq was pubs, brewing and spirits and Rank Group – erm, where do you start / stop?

All of these companies have since been transformed into focused businesses or been bought (Allied Domecq) or dropped out of the FTSE100 (Rank).

Whitbread has done much to address its conglomerate status, notably quitting its centuries of tradition as a brewer and exiting upscale hotels, but investors are baying for more.

There is a constant stream of City analyst notes that highlight the break-up value of the group. Whitbread's current share price most likely contains a substantial premium due to such expectation.

Only two bits of Whitbread are worth more than £1bn – pub restaurants and budget hotels, with the latter by far the chunkiest part of the company with a valuation somewhere north of £1.7bn.

Sitting in CEO Alan Parker's chair, the rational, strategic option to pursue shareholder growth is to focus on Premier Travel Inn. Bolting on Travelodge for about £1bn would be a neat deal if it could be accompanied with the £1bn sale of the pub restaurant business.

The latter disposal is certainly possible. Quoted pub group Mitchells & Butlers is hotly tipped as a buyer and has the finances in place to do the deal. At its trading update last week M&B said it could raise up to £1bn.

But is Travelodge the right buy for Whitbread? The price of £1bn at first sight seems only slightly above the £712m Compass received from Permira in February 2003.

Since then, Travelodge has sold all of its freeholds, netting Permira £400m in a deal clinched late in 2004. Nonetheless, in the current heady climate, £1bn is probably the baseline for bids.

Post a back-to-back deal, Whitbread is left with a business that spans leisure clubs, coffee shops, high street restaurants and a rump of upscale hotels, as well as being the dominant branded budget player in the UK.

The upscale hotels are already earmarked to go and should bring in £300m plus. The remaining parts are worth a little shy of £1bn with David Lloyd Leisure likely to fetch about £600m and the high street restaurants (Pizza Hut, TGI Friday's and Costa Coffee) just under £300m.

If Whitbread does not want to stagnate, it has to go overseas with its budget hotels operation. Previous attempts at overseas expansion have stalled but this time the need is particularly pressing.

There is enough financial muscle here to buy a significant presence in continental Europe for budget hotels. Perhaps B&B, owned by Eurazeo, or one of Louvre's chains, now in Starwood Capital's hands, might be a target.

In the nearer term, however, is the fascinating issue of how Parker might play the management issue at Travelodge. Would current head of Premier Travel Inn Patrick Dempsey make way for Grant Hearn, a former managing director of Travel Inn and current Travelodge CEO?

Hearn has been particularly impressive at Travelodge, growing the business faster than its rivals despite no funds to buy property outright. Instead, the group has pioneered forward funding for its developments and taken full advantage of the growing acceptance of hotels as leases.

Such an approach at Premier Travel Inn could transform that business and free up cash to fund any overseas forays.

All this assumes, of course, that the private equity funds do not turn hostile and mount a bid for Whitbread themselves. Given the huge amount of money most have tied up in their funds, the barbarians could well return.

Accor suffers as investors demand divestment

Results presentation fails to deliver strategically

Accor suffered the biggest fall in its share price for three years in March after investors were less than impressed with the full-year results presentation. While the profit increase fell short of most expectations the underlying reason for the gloom is the lack of news of divestment plans.

Despite promises to sell €1.5bn of hotel property, Accor failed to assuage the craving from investors for more divestment. And by unveiling plans to invest €2.7bn back into the hotels business, almost twice the amount being raised, Accor further antagonised its shareholders.

Just as with InterContinental, investors have the scent of money in their nostrils and it is hard to see the French giant making peace with the bulk of its backers unless it begins to shed assets.

Shareholders understand the need to grow but are demanding that it is achieved without delving into the cash that can come their way following sell-offs. Accor is taking two big risks: that it can continue with its conglomerate structure (principally its hotels and services divisions) and that it can use its own capital to expand.

At its results, which showed a 17.6% rise in profits before tax and non-recurring items, Accor unveiled plans to add more than 200,000 new rooms by 2010, half in economy and budget properties.

Two-thirds of the growth will be in emerging markets with the rest in mature countries. The bulk, 70%, is intended to be management or franchise and just 30% owned or leased. The targeted return on the €2.7bn of investment is 15%. The expansion plans make sense and offer a sensible way forward but they do not go far enough in terms of divestment.

CEO Gilles Pelisson admitted that the company was considering selling its stake in Carlson Wagonlit but he refused to commit to a timetable. And when challenged on hotel asset disposals, finance director Jacques Stern said that the intention was to reduce capital intensity in mature markets but to continue expansion in emerging markets via hotel ownership as property yields in such countries were high.

What has been announced on the disposal front is the sale of Accor's 1.42% stake in contract caterer Compass Group for €96m; the sale of six Sofitels in the US for $370m; and the sale of 76 hotels to Foncier des Murs for €583m.

The Sofitel divestment was to a joint venture comprising GEM Realty Capital, Whitehall Street and Accor, which is retaining a 25% stake.

The hotels, totalling 1,931 rooms, are located in major metropolitan markets across the US. They are to be managed under 25-year contracts. Accor now plans to form further partnerships with real estate investors to grow its upscale management contract business.

The Fonciere des Murs transaction concerned 59 French hotels, five Thalassotherapy institutes and 12 Belgium hotels. The total room count is 8,300 across Ibis, Mercure and Novotel brands.

This second transaction with FdM, a SIIC (French Real Estate Investment Trust), is notable for including Belgium properties that do not benefit from the same tax advantages as the French ones, and for the lower rents.

The previous transaction, which closed in June last year, saw turnover leases set at an average of 15%. This time it is 14%. As last time, the leases are on12-year terms renewable four times, effectively creating 60-year holds on the property for Accor.

The hunt is now on for a partner to strike a sale and variable leaseback deal with for 130 hotels in Western and Central Europe. These 21,000 rooms have a market value of €1.3bn. It is expected to complete a deal by 2008. Another 150 hotels in the region are to be sold outright or sold with a franchise-back.

Accor said it wants to increase ROCE by 0.6 percentage points by 2008 through disposals expected to have a cash impact of €1.5bn. It will leave the company with just 11% of its upscale hotels as owned or on fixed leases, compared to the 51:49 split as at 2004.

Midscale is expected to see 73% of the hotels on management contracts, franchises or variable rents, compared to 45% in 2004.

During the presentation, no word was said about Accor's stake in Club Med but during the Q&A afterwards, Pelisson said that the lack of a mention did not indicate that this holding was for sale.

The company is committed, however, to retaining and growing its services business. It intends to plough €500m into it and expects to see a return on invested capital of 20%.

Shearings strikes sale and leaseback

WA Shearings, the coach holiday firm, has sold 39 of its UK hotels in a sale and leaseback deal valued at £110m.

The buyer is the Moorfield Real Estate Fund The Moorfield Group is one of the backers of operator Kew Green Hotels.

The yield on the portfolio of hotels is just over 6%. They are held on 25-year leases with annual, CPI-linked reviews.

Shearings will control a planned £25m capital investment programme for the properties scheduled to be spent over the next five years.

The deal comes a year after Shearings merged with the Coach Holiday Group, the owner of the Wallace Arnold brand. This saw Coach Holiday's backer, private equity firm 3i, take-out Shearings' venture capital investor Bridgepoint.

Host unveils European joint venture

Host Marriott and Starwood Hotels have unveiled details of their European joint venture that is part of the $3.8bn sale of Starwood assets.

A Dutch pension fund and GIC Real Estate are linking up with Host to own six European hotels worth $621m.

Stichting Pensioenfonds ABP is to hold 19.9% and Jasmine Hotels, a subsidiary of GIC, the Singapore Government's real estate investment company, is to hold 48%. The remaining 32.1% is to be held by Host. The asset management function will be carried out by Host.

Three hotels in Canada that were part of the wider deal have been taken out due to tax reasons. This has trimmed $276m off the purchase price.

Park Plaza Europe properties refinanced

The owners of three of Park Plaza Hotels Europe's London properties have been refinanced to the tune of £195m.

The move follows stalled talks for a sale-and-leaseback covering the bulk of the group's assets.

Goldman Sachs International Bank has taken on the loans previously held by Bank Hapoalim on behalf of joint owners Bea Hotels and the Red Sea Hotels Group.

The properties are the Riverbank Park Plaza, the Victoria Park Plaza and the Sherlock Holmes hotel.

Hilton Hotels Corp makes quick divestment move

Hilton Hotels Corporation has moved quickly to start its divestment process. Just a week after completing its purchase of the hotel assets of Hilton International, it put two of the largest conference hotels in the chain on the market.

The move is part of HHC's push to return to investment grade status by reducing its exposure to property.

The two hotels up for sale are the London and Birmingham Metropoles, with 1,054 and 794 rooms respectively. The London hotel is the largest conference hotel in the UK and the second largest in Europe.

The properties, which are being marketed by Christie & Co, could fetch as much as £400m. HHC is seeking to retain them on a long-term management contract.

At its full-year results conference call, held at the end of January before the Hilton International deal had completed, HHC's CEO Steve Bollenbach stressed that the sales were not just driven by the need to pay down debt. He pointed out that the company's strong cash flows would enable it to do that anyway, even if it took a year or two longer to obtain investment grade rating.

He said that HHC's strategy is to become less reliant on real estate and obtain more profits from the fee business.

Analysts at Citigroup looked at impact of selling $2.5bn of assets. If this was achieved along with the expected earnings recovery, then investment grade status would be obtained again by the end of 2007 so that debt was below 3.5 times EBITDA.

The analysts commented that factoring in $2.5bn of sales might be conservative given the strength of demand for hotel assets. They listed four drivers: robust industry fundamentals; low interest rates; large increases in construction and replacement cost; and strong residential trends which allow owners to monetize excess real estate.

More recently, HHC has also appointed advisers to sell its LivingWell health and fitness chain in a move that could raise more than £100m.

Following the completion of the £3.3bn sale of Hilton Group's hotels to HHC on February 23, Hilton Group's shareholders have received a bumper payout of £4.2bn equivalent to 62% of the company's market value.

Profit at the company, now renamed as Ladbrokes to reflect the betting business that is left, was up 10%. Like-for-like profit at the hotels division was up 17.3%.

Morgans Hotel Group lists on NASDAQ

Former Schrager berth raises cash

Morgans Hotel Group began trading on the NASDAQ stock market on February 14 when its $20 a share price slipped 2%.

The company is raising $360m, but the net proceeds will be $275m which will be used to pay down debt. The big winner looks to be Ian Schrager, the company's founder who left as CEO in the summer.

RSA Associates, an entity controlled by Schrager, is selling 450,000 shares in the IPO for about $9m. It will retain 2.3 million shares, 6.4% of the company, worth about $46m.

Another big payday for Schrager comes with his contract. He is to receive just over $1m for last year, $750,000 for this year and $500,000 for next year. In addition, he is to receive bonuses of about the same amount each year.

Since exiting as CEO, chairman and president, Schrager has been retained as a consultant. He will continue in this role but he has no exclusion clause and may compete head-on with the company.

His contract sees him retain the services of a driver and secretary and he will have nearly all his other expenses met.

The largest private seller in the IPO is NorthStar Capital, the investment firm co-headed by Ed Scheetz who is also CEO of Morgans. NorthStar is netting $40m but will retain a stake worth 28%.

Morgans has been struggling to make money due to its indebtedness. In the first nine months of 2005, while revenue was up 12% to $190m, it made a net loss of $29m. Interest charges have wiped out profits every year since 2000 and the flotation prospectus warned that substantial net losses are expected for the foreseeable future.

The proceeds from the IPO retained by the company will be used to pay down debt which stood at $660m at the end of September last year. It will see net book value per share turn positive to $1.47 from minus $11.51.

Some of the cash raised will also be used to finance the purchase of the James Hotel Scottsdale, near Phoenix, Arizona, which was bought for $47.5m in January. Morgans also has projects underway in Las Vegas.

The two London properties, owned in a joint venture with Burford Holdings, were refinanced at the end of last year. The properties had been put up for sale but a £107.5m credit facility was arranged instead.

Since leaving Morgans in a full-time role, Schrager has focused on residential projects in New York and a budget hotel in Miami, the Riande Intercontinental. He claims the latter is a real estate investment rather than something he intends to run.

London & Regional sells six in Finland

London & Regional Properties has unloaded six spa hotels from Holiday Club Finland it bought only last June.

The move cuts the €100m turnover of the business bought by L&R in the €120m deal in half, leaving it with nine holiday resorts and a significant timeshare business that is one of the biggest in Europe.

The new owner, Finnish retail co-operative SOK's subsidiary Sokotel Oy, is to pay an undisclosed sum for the business. The combined turnover of the hotels is €50m.

Currently, SOK has 49 properties within its Sokos Hotels and Radisson SAS chains, plus 550 restaurants across Finland. The total room count, excluding the latest deal, is 8,000.

For L&R the move is unusual in that it is typically a long-term holder. But Sokos is an existing partner of L&R, operating a couple of the 31 hotels in L&R-owned company Dividum.

L&R is to continue with both the timeshare business and the development of spa hotels outside of Finland. Last week it signed a deal to buy a 280-room property being built in St Petersburg due to complete in 2007 at a cost of €50m.

A spa hotel is due to open in 2008 in Tallin and the first international Holiday Club Finland spa opened in Sweden in 2004.

Sol Melia and NH emphasise the importance of ownership

Hotel operations only viable with asset ownership

The two Spanish hotel giants, Sol Melia and NH Hoteles, used their full-year results presentations to sell their vision of combining asset ownership with hotel operations.

For Sol Melia, the issue was to focus on asset rotation and for NH, it the focus was on future growth via variable leases or management contracts.

Sol Melia made much of a revaluation by CBRE that showed it currently trades at a 30% discount to the net asset value of its €4bn of owned hotels.

Its solution is to come via its asset management division which is to focus on "the crystallisation of hidden value of company assets while taking advantage of the opportunities of acquisitions".

It has committed itself to realising €100m a year through asset sales while making a similar amount of acquisitions. It will only sell on EBITDA multiples of 12 times or more and only buy on 10 times or less.

A key part of the new approach is to exploit opportunities both in condo hotels and timeshares.

The Americas dominates on both fronts. With timeshare, sales were €27m in the Americas against just €205,000 in the fledgling European operation.

Similarly, the condo development at Paradisus Puerto Rico is already selling some of its 144 units at between $320,000 and $350,000 each and is expected to complete within two years.

At Melia Zaragoza in Northern Spain, which in the third quarter saw a 50% stake bought by building company Grupo Horcona for a 26 times EBITDA multiple, the 60 residential units have yet to start construction.

In total, Sol sold €124m of assets and bought €125m during 2005. The company said the sales were struck at an EBITDA multiple that averaged 24.6 times and the purchases were made at a 7.3 times multiple.

The overall year saw net profit double to €92m thanks both to the asset rotation policy and an improvement in its core hotel business. The company said the oversupply issue in Spanish cities appeared to be over and this helped the European city division push revpar up 4.8%.

There was also confidence expressed in the European resort division. During the past year it improved revpar by 2.9%. Sol's room stock splits 40:60 city:resort.

In contrast, NH Hoteles is far more focused on the city segment, claiming to be the third biggest business hotel operator in Europe. It does, however, have ambitions to grow its resorts operations, particularly golf complexes in the Caribbean.

Expansion in the city hotel segment is to be made in countries where NH already has a strong presence – Spain, Germany and Benelux – or in Italy, the UK and Eastern Europe.

In Spain it opened 12 hotels in 2005 with 1,191 rooms. In Italy, with the opening of NH Santo Stefano in Turin and the signing of NH Orio al Serio in Bergamo it has 1,092 rooms opened or confirmed. In the UK it has opened the NH Harrington Hall in London.

Owned hotels are to be retained to "maintain a strong balance" but new developments are to be undertaken via variable leases, management contracts or minority stakes in ownership.

The current structure of NH has 28% of its hotels owned, 12% managed and 60% leased, including 13 hotels that have call options.

NH is launching a €100m rights issue to buy-out real estate subsidiary Sotogrande and the minorities in its subsidiary in Latin America. The Sotogrande brand is to launched outside of Spain with the first projects in Mexico and the Dominican Republic.

The refinancing of lease contracts in Germany and Austria during the year cost it €54.4m but the German hotels appear to be turning a corner with a EBITA loss of €0.58m against last year's loss of €7.93m.

Net profit at NH was up 13% in the year to €62.2m on hotel sales up 4.9% to €897.5m. Overall revpar was up 4.3%.

MWB takes f&b route to profit

Malmaison and Hotel du Vin, part of property group Marlebone Warwick Balfour, had strong second half of 2005, increasing operating profit 37%.

And the rapid growth of the group – it is targeting 25 properties in the medium term – is being built on a solid foundation through the creation of a robust human resource function that supplies its future employees.

During the six months to December 31, the currently 16-strong group increased revenues by 15% to £36.0m. EBITDA was £11.1m, a 37% increase on last year's £8.1m.

Average rate was £105 against a figure last year that was under £100 and occupancy was static at 81%.

The company said that it had achieved synergies by combining Hotel du Vin and Malmaison, although these were not specified.

But trimming overhead will not make the expensive acquisition of Hotel du Vin pay-off. More likely to succeed is the group's HR development strategy.

Small, idiosyncratic chains usually struggle once hotel numbers begin reaching double figures as the creative and operating team at the top find it increasingly hard to maintain control.

At Malmaison, however, chief executive Robert Cook is determined to avoid this fate by growing his teams from within. Rather than simply imposing a creative vision from the top, he is hoping to instil a culture organically as the group steadily expands.

It is a tough, challenging course he has chosen but so far, so good. Food and beverage, one of the first things to slip if things are not right, grew sales by 16% in the period.

By the end of 2007, it is expected that the chain will total at least 20 properties. New sites for Hotel du Vin have been acquired in Cambridge and York, both at 42 rooms.

A new-build Malmaison is due for completion in Liverpool's Princes Dock by the end of this year, providing 130 rooms, and the Great Western station hotel in Reading is being converted to a 70-room Malmaison due to open in the first half of 2007.

InterContinental returns more but challenges lie ahead

InterContinental is to hand back another £500m to shareholders, taking the total it will return to £2.75bn, more than its market capitalisation on its formation through the demerger from the pubs business.

But while investors have been rewarded for staying with the existing management team, the job ahead looks even tougher.

The scale of the task was made apparent in the figures given out during the company's full-year results presentation.

The key challenge in the new asset-light future is adding new management contracts and franchises. The new additions during 2005, however, were 34,880 rooms, barely more than the 27,476 added five years earlier in 2001.

When the 31,549 room exits from the IHG system are taken into account, the net increase was just 3,331 rooms. This represents a rise in overall system size of well under 1%.

IHG countered this gloom by pointing out that it has 108,500 rooms in its pipeline, the largest amount in the hotel industry. Around 80% of this pipeline is expected to open by 2008 and 38% are under construction.

Certainly, the rate of signings is increasing. Two years ago, in 2003, 71,000 rooms were signed-up to the system. But in 2005, the figure was 108,000.

The rapid pace of the transformation of the business was also made clear. Thanks to the disposals and taking account of the hotels earmarked for sale (mostly a £600m portfolio in continental Europe), 88% of earnings now come from fee income with just 12% from the owned and leased estate.

Franchising and management is now a serious business. Total gross revenues among the franchises were £4.4bn with IHG netting £251m in fees. With a margin of 85%, IHG converted £214m to profit.

The managed hotels generated sales of £2.4bn. IHG took £104m in fees and £62m in profit, thanks to a margin of 58%.

The profit delivered from the owned and leased estate is now the least important of the three types of operation at just £54m. The margin here is 17%. No wonder that IHG describes its newer income stream as higher quality, pointing to the need for less capital and more predictable returns.

A key point raised during the presentation was the need to establish scale. IHG said that the top four hotel companies in the world account for just 11% of global room supply. IHG is the biggest of these with a market share of 3%.

Scale delivers buying power, marketing spend and brand premium. In the UK, where IHG has scale, its system delivers 64% of reservations. But in Spain, where its presence is weaker, system delivery is just 30%.

IHG made much of its organisational changes during 2005 that are expected to deliver higher rates of franchise and management contract wins.

The franchise push is headed by Stevan Porter in addition to his role of running the Americas. Finance director Richard Solomons has been given the task of developing relationships with major investors operating in multiple countries.

- InterContinental has sold 24 European hotels, representing 4,903 rooms, to Westbridge Hospitality Fund, a subsidiary of Westmont.

The €352m deal was struck ahead of schedule, with the assets only being placed on the market earlier this year with an expected disposal timetable of up to nine months.

The hotels have been sold with 15-year franchise contracts. The fees are expected to be about €4m.

EBITDA was €28m in 2005 and this translates to an EV/EBITDA multiple of 12.3 times after transaction costs.

Still on the market are seven InterContinentals in Europe, likely to go for £350m. The frontrunner for this portfolio is Igal Ahouvi, the Israeli businessman that bought 16 Hiltons for nearly £400m and is tipped to buy the 46 UK Marriotts currently up for sale.

InterContinental, meanwhile, is pushing forward with its management and franchise business. Last week it signed a deal to take that will mark the debut of its Crowne Plaza brand in Russia.

The 572-room Crowne Plaza Moscow – World Trade Centre, originally built in 1980, is to undergo extensive renovation.

And the company is also reportedly looking at operating a $800m resort in Orlando, Florida, under its flagship InterContinental brand. The Wall Street Journal said that the development will be called Palazzo del Lago and will include 1,260 rooms, almost half of which will be available to buy by investors on a buy-to-let basis.

There will also be 994 conventional condo apartments on opening, which is scheduled for 2009. The owner and developer of the resort is Hospitality Development Corp. The property will be the third InterContinental managed project featuring a residential component. The other two are in Boston, opening later this year, and one in Sacramento due to open in 2008.

Whitbread commits to conversion to grow budget hotels

Whitbread's purchase of seven former Holiday Inn hotels marks a step-change in its determination to grow its Premier Travel Inn brand.

Opportunities such as this £34.5m deal to buy 1,021 rooms were described by chief executive Alan Parker as "a rich seam to exploit for future growth".

The Premier Travel Inn estate will now number more than 31,000 rooms, putting it comfortably ahead of the 17,000-strong Travelodge, its nearest rival.

But Travelodge had been growing faster over the last few years. Earlier this month it said it expected to reach 30,000 rooms in the next three years, almost doubling from its current size of 17,000 rooms. It also promised to pitch its prices below those of PTI.

Whitbread has reacted by promising to reach 45,000 rooms in the UK by 2010 and pointing to its higher occupancy rates.

The need to enter city centres, given that most of the viable roadside opportunities outside of towns have been exhausted, has driven the switch by PTI into conversions.

Travelodge has been able to make headway with site acquisition thanks to its preparedness to sign-up for fixed leases, making it popular with institutional landlords. Whitbread, in contrast, has grown almost entirely by taking direct ownership.

The latest acquisition was from LRG (Lehman Brothers, Realstar and GIC) who almost a year ago paid £1bn to buy 73 hotels from InterContinental. LRG said it expects to sell the remaining four hotels on the market through agent Christie & Co individually 'in the near future'.

These sales will bring to an end the major ownership reshuffling of InterContinental's UK brands. The Whitbread deal is expected to complete within two months.

US giants set for acquisition spree in Europe and Asia

The big three US brand owners and hotel managers – Marriott, Hilton and Starwood – have reported bumper full-year profits.

The strong results and even stronger forecasts make further trans-Atlantic consolidation – Hilton having already declared its hand – a very real possibility.

Marriott International had the most robust set of numbers, reporting record full-year earnings per share for 2005 of $2.89, up 17% on 2004. Just as impressive were the increased forecasts for 2006, with eps targeted to be in the range $3.08 to $3.18, or a rise of up to 10%.

A key number for Marriott was that management and franchise fee revenue exceeded $1bn, a rise of 18% that takes it beyond the previous peak achieved in 2000. About half of Marriott's managed properties generated incentive fees compared to less than a third in 2004.

Marriott failed to hit its target for new room additions, coming in at 22,000 rather than the 25,000 it had earmarked. For this year, the company is forecasting 25,000 openings, chopping off the top end of its previous forecast of 25,000 to 30,000.

The room openings included 9,000 at full service properties. Some 27% of the 22,000 were conversions from rival brands.

The difficulty in making the number of openings suggests that supply is not increasing that rapidly and this means revpar is likely to prove robust. Revpar worldwide was up 10% in 2005 and the company estimates first quarter revpar growth this year in North American owned properties of 8% to 10%.

The openings problem also means that Marriott has added motivation to make acquisitions. Chief financial officer Arne Sorenson said in a conference call to analysts that "we look at everything". He added: "If we can take part in M&A in a transaction that creates value for shareholders, we'd love to play".

Cash from operations was just shy of $1bn in 2005 at $923m. While this is expected to drop slightly in 2006 to $680m, largely due to timeshare expenses, the company is expecting to be throwing off in excess of $1bn a year by 2009.

Emphasising the increasing profitability was the increase in house profit margin which went up 180 basis points to 35.5%. In China, thanks to the lower labour costs, house margins are nearer 50% although Sorenson said that management contracts in that country were worth roughly the same to Marriott as those in the US due to the difference in structure.

During the year, 50% of managed hotels earned incentive fees compared to 32% in 2004, an increase of a third.

In addition, some $1bn of asset sales is expected this year, including up to $350m relating to its acquisition of CTF.

Sorenson said that he expects to sell around $300m of the CTF properties plus $170m relating to the Whitbread portfolio and another $200m to $300m worth of European assets Marriott has acquired on the open market.

This all adds up to some hefty firepower, even if Marriott took only restrained leverage (and few buyers are).

Meanwhile, Starwood Hotels & Resorts reported final quarter profits up 59%. This was on the back of a 12.2% increase in North American owned hotel revpar and a 9.4% increase worldwide.

The company is forecasting that worldwide like-for-like owned hotel EBITDA will rise by 15% to 17% during 2006. Management and franchise fees will grow by 18% to 20%.

The current year is set to see a total of $5.5bn raised through asset sales, including the completion of the $4.1bn via the Host Marriott deal. About $2.8bn of this is to be returned to shareholders in the form of Host stock.

As with Marriott, cash flow is forecast to be strong, with cash from operations of £1.35bn in 2005 and set to remain close to or above $1bn for at least the next five years.

CEO Steve Heyer told analysts during a conference call that: "We remain significantly under penetrated around the world, which gives us significant opportunity to extend our reach."

China, and indeed the rest of Asia, is clearly one home for this cash. But there are few major deals to be had in this region and progress in this region is most likely to be made via steady, organic development.

Instead it is Europe that looks particularly attractive from a North American perspective. The obvious targets are the listed pan-European or even global operators, with InterContinental on the top of everyone's list.

But smaller, national chains are also likely to come into the frame. The brand owners would prefer to simply sell the Europeans a badge but given the snail like progress to date, an outright acquisition followed by the disposal of the property seems the only real alternative to ensure adequate growth.

Cendant takes management route

Cendant's hotel division is set to buy another management company in the segment above its existing Ramada brand, said Reas Kondraschow, svp and managing director at the US group's international operations.

Kondraschow, speaking at last week's International Hotel Investment Forum in Berlin, said such acquisitions were necessary for Cendant to have 'skin in the game'.

Until the acquisition of the Wyndam International brand and management company late last year, Cendant had stuck to its model of being a pure franchise company.

But this is now viewed as having held back its growth outside of the US. Its strength in its home US territory is such that it is already the world's biggest franchiser of hotels with 6,500 flags and 540,000 rooms. Despite this scale presence, it has struggled to make headway overseas.

Kondraschow told Hotel Analyst that two management company acquisitions were impending: one in China, and one in Europe.

Cendant is due to separate into four separate companies this June or July, comprising: real estate services; travel network (internet); hospitality (the hotels and timeshare business that together account for around 15% of 2005's EBITDA); and vehicle rental services.

Peninsula shrugs off avian threat

Fears about avian flu have failed to dent business at Hongkong and Shanghai Hotels, the owner of the Peninsula brand. The company said that forward bookings and revpar so far this year compares well with 2005.

But it also warned that "the hospitality industry remains susceptible to unforeseen events which could have a major impact on global travel". It added that avian flu was the latest threat.

Profit before non-operating items across its businesses, which include seven Peninsula hotels, was up 39% to HK$688m. Net profit dropped slightly by 4.4%.

The revpar increases at its three North American hotels were all double digit, as was the revpar increase at the group's flagship in Hong Kong at 11%. The biggest revpar hike was in Bejing, at 40%, but this hotel's revpar remains at less than half that achieved in Hong Kong or North America despite its renovation.

Islamic capital makes further move into hotels

Islamic capital is increasingly a force to be reckoned within the international hotel industry. And now a $2.3bn Sharia-compliant hotel fund has been launched.

KM Properties, part of the UAE-base Al Rostamani Enterprise, announced the launch in early April and plans to open its first hotel in Dubai in 2008.

The first phase of the fund is already closed but it is planned to attract international investors in future stages. International presence is expected both in the fund management and company management.

Alongside the fund, KM has created a Sharia-compliant hospitality operating company. This is being staffed by existing industry professionals.

As well as the Dubai property, a 700-room hotel that is being backed by KM to the tune of $290m, three other management agreements have been signed and a further seven are in advanced stages of negotiation.

A new brand will be launched under which the hotels will trade. Future target markets include Saudi Arabia, Morocco, Turkey, Malaysia and India. KM said it is also seeking to manage hotels under established brand names.

Sharia law requires that investors share profits in trading and business activities rather than receive interest payments which are forbidden. The recent UK Budget saw extensions to Stamp Duty Land Tax relief previously available only to individuals widened to companies, thus making the UK a possible market for Sharia-compliant funds.

And in May, the European Islamic Investment Bank is planning to list on London's Alternative Investment Market, hoping to raise £200m. It expects to have regulatory capital in excess of £300m following the IPO.

Meanwhile two Middle East businesses have made further declarations of intent into the hotel industry, totalling $1.1bn.

The two announcements concern Saudi-based business, the Siraj Hospitality Investment Company, with a $500m outlay, and Nakheel, the Dubai-based property company, which has launched a hotel division with $600m of investment.

SHIC is backed by Siraj Capital and the Saudi Arabian General Investment Authority with advice from DTZ. Emaar Properties, which describes itself as the world's largest real estate company, is putting $75m into the fund.

The money is to be invested in hotels and other hospitality facilities in the King Abdullah Economic City in Saudi Arabia.

KHI lists in Dubai

Kingdom Hotel Investments, the owner of a portfolio of mostly Middle Eastern hotels, has announced it has listed on the Dubai International Financial Exchange.

The cash raised from the $1.5bn IPO will be used to expand its portfolio and represents a further push by Middle East money into the international hotel industry.

KHI is headed by Zarmad Zok and has Prince Alwaleed as its majority (55%) shareholder through his Kingdom Holding Company.

The IPO, which took place at the start of March, raised $397m. The company was the first to list on the DIFX. As well as the Dubai listing, which is targeting Middle Eastern investors, KHI is to offer Global Depository Shares on the London Stock Exchange which are expected to attract European institutional investors.

Tim Hansing, senior vp of acquisitions and development, said that the focus of growth would be in emerging markets. Target territories include Asia-Pacific, South Asia, Africa, CIS states and Russia. The company has offices in Singapore and South Africa with one planned for India.

CEO Sarmad Zok said the focus on hospitality and real estate in emerging markets gave KHI a unique competitive advantage.

The current portfolio encompasses 26 hotels in 13 countries, of which 15 are operating with a total of 3,262 rooms. KHI has 25% stake in the George V in Paris.

During the nine months to September 30, revenues were up by 45% to $43.7m and net income was up 47% to $8.2m.

The portfolio is split 57% city hotels and 43% resort. There are three brands: Four Seasons, representing 54% of invested capital; Fairmont 8%; and Movenpick 38%.

Deutsche Bank initiated coverage of the company with a "buy" rating, stating that there is substantial ability to create value "given the potential growth of the group's focus markets".

KHI is separate to Kingdom Hotels International which is the company buying Fairmont, although Prince Alwaleed has majority interests in both.

Macdonald manage back needs work

The news that Macdonald Hotels has appointed advisers to sell around £200m worth of property looks like the trend to sell-off hotel property has penetrated the UK's unlisted groups.

But the lack of detail coming out to the market suggests that the largest privately owned hotel group in the UK still has some thinking to do about how such a transaction is to be structured.

The privatisation of Macdonald back in September 2003 saw it take on significant leverage and the stretch of meeting these interest payments took its toll in its last set of financial results.

The £50m of interest wiped out operating profits of £31m leaving the group £19m in the red for the 18 months to September 2004. The losses means the company is finding it a struggle to find the cash to upgrade its properties.

EBITDA is healthy at almost £46m but the heavy borrowing is putting an unreasonable strain on the long-term prospects for the business.

An obvious route out for the 65-strong chain is to join in the sale and manage back trend sweeping the listed operators, with players like InterContinental, Hilton and De Vere all taking advantage of unprecedented investor appetite for hotel property.

A well structured deal could see Macdonald pay down debt and leave it focused on running the hotels.

A report in the Times newspaper suggests that 20 hotels might be sold for up to £200m. And chief executive Donald Macdonald, never known for resisting a good deal, might be tempted to sell-off 35 hotels if the price was right.

But the current approach being taken by the company appears to be one of using the sale and manage back technique as a refinancing exercise rather than finding a long-term property partner.

Institutional investors might be falling over themselves to proffer cash at hotel property owners but agreements have to factor in ongoing capex requirements unless there is to be disappointment on both sides.

The Macdonald estate is somewhat under invested and, although well managed, it is badged with a distinctly second-tier brand. Investing in such a portfolio demands a sympathetic and experienced partner rather than simply the one prepared to pay the highest price.

Airport hotel fund finds more ambitious backer

The Airport Hotels Unit Trust, the fund that owns the long leases on nine airport hotels, has been bought for over £300m by Arora Family Trust.

The move is expected to put renewed vigour into the UK's pioneering dedicated hotel fund.

The AHUT is a Jersey Property Unit Trust that owns 999-year leases on the nine hotels at Heathrow, Gatwick and Stansted.

The Royal Bank of Scotland has put in place £380m of funding and BAA Lynton Management will continue to oversee the portfolio on behalf of Arora on 10-year contracts.

Jeremey Boyes, asset management director at BAA Lynton, said that following the deal with Arora he expects the fund will now "have more ambition".

Future deals, although still likely to involve airport related hotels, will not necessarily be on BAA sites.

The main beneficiary of the Arora Family Trust is Surinder Arora, a former British Airways employee whose first foray into hotels started in 1999 when he opened a property at Heathrow to provide crew accommodation. He now heads up a business that owns and manages 5,500 rooms.

In October last year, Arora agreed to buy the ground lease of the Terminal 5 hotel at Heathrow for £65m. This 600-room property is to be a Sofitel opening in 2008.

Outside of airports, Arora is part owner of Wentworth, the Surrey golf course that is set to have luxury hotel.

Arora initially bought out 20% of the AHUT that was held by a Middle East based investor. The current deal has seen the acquisition of the remaining 80% held by Scottish Widows, the Shell and Coal Board pension funds and 10% held by the Airport Property Partnership, a JV between Morley Fund Management and airports operator BAA.

The Airport Hotels Partnership, the forerunner of AHUT, was formed in March 2000 with the sale of eight hotels valued at £200m. The four investors put in a total of £85m and BAA retained a 10% stake. RBS provided a £98.3m loan, representing 50% gearing. In early 2005, the fund bought the Express at Stansted for £24m leaving it with gross assets of £255m as at March 31 last year. RBS was advised in the AHUT deal by CMS Cameron McKenna. Macfarlanes and Lovells acted for BAA.

Rezidor Hospitality quiet on IPO prospects

Rezidor Hospitality, one of the fastest growing hotel operators in Europe, has reported that operating profits were almost 2.5 times bigger in 2005 than in 2004.

But the company was tight-lipped on whether it is still on track to seek a public listing during 2006 or 2007, as was planned two years ago.

The EBITDA increase to €45.2m from €18.8m was accompanied by a 20% increase in sales to €587m.

Rezidor was a wholly owned subsidiary of airline group SAS until last summer when Carlson Hotels acquired 25% of the group in return for a renegotiated master franchise agreement.

This deal provided a cost reduction worth €6m for the second half of 2005. The full-year effect is estimated at €11m but this is expected to rise in line with revenue.

Since the deal with Carlson, an IPO remains the most likely exit for the majority owners. Back in 2004, chief executive Kurt Ritter said that the then loss-making unit would take at least three years to grow big enough to seek a listing.

During 2005, Rezidor added 29 new hotel contracts totalling almost 5,000 rooms. This 16% growth in rooms left it with 263 hotels (including 46 under construction) with around 50,000 rooms.

The company has signed a worldwide license agreement with the Italian fashion house Missoni to develop up to 30 hotels in 10 years.

A previous deal with Cerruti appears to have fallen by the wayside. The first property to be opened under this new brand was to be in Dubai Media City. However, the 121-room hotel, which is due to have a second 125-room tower open this year, began trading last month under the Radisson SAS brand.

M&C sets faces against selling

Millennium & Copthorne Hotels is trying to burnish its image as a brand manager as it continues to resist asset disposals.

The argument put forward by chairman Kwek Leng Beng during the full-year results announcement in March was that M&C's size – its market cap is just over £1.2bn – means that shorn of property it would not be a sustainable proposition.

Instead, M&C is trying to make a virtue out of its need to own, operate and brand the bulk of its portfolio.

During its presentation it highlighted the signing of 10 management and franchise agreements which cover properties with a total of 1,839 rooms.

Some City analysts argued that the 10 management and franchise contract wins show that M&C is changing its focus. Of the 91 hotels in its portfolio, just12, including the 10 signings last year, are not owned.

And it is difficult to whip up much enthusiasm for the three "brands" expected to lead the charge into a new asset light future – Millennium, Copthorne and Kingsgate.

M&C has much going for it as a property play. Its assets are generally good quality, being mostly city centre and upscale, and provide a firm underpinning of its share price.

Its current results are also helping to boost sentiment. During the year to December 31, group revpar was up 7.4% and pre-tax profits rose to £95.8m from £91.0m. Operating profit was up 17% to £99.6m. Group revpar in the current year to February 14 was up 9.4%.

Tony Potter, group chief executive, pursued the positive advantages of being a real estate owner during his comments at the results presentation.

"The group is in the unique position of being able to decide whether or not an asset can create greater value through redevelopment for alternative use. This is due to our real estate expertise in parallel to our in-depth knowledge of operating hotel properties," he said.

As examples, he cited the leasing out of the convention centre in Seoul for conversion into a casino at the beginning of the year and the redevelopment of the Orchid Inn and Sunnyvale Hotel into condominiums in the third quarter.

Like most listed property companies, M&C trades at a slight discount to net asset value. UBS estimate that a full hotels disposal could be made at 551p, about 100p more than the current share price.

Quinlan Private sells out at world-record

Quinlan Private, the syndicate of investors that has bought into a swathe of upscale hotel property across Europe, has agreed to sell its Four Seasons in Milan for what it claims is a world record value per room.

The 118-room property is being sold for in excess of €200m to Italy's Statuto Group in a deal that demonstrates Quinlan's impeccable timing of the cycle.

When Quinlan swooped on the Milan property back in late 2002, the then mooted price of €1.5m per room looked heady. But the exit after less than three years has delivered an impressive return to the investors.

The buyer is the Italian real estate group that bought the Danieli in Venice for €177m in May last year. Giuseppe Statuto, owner of the Statuto Group, said that the latest deal completes Statuto's strategy in luxury hotel development.

Quinlan still owns Four Seasons in Dublin, Prague and Budapest plus the three remaining properties in what was the Savoy Group, now known as Maybourne following the disposal of the eponymous property to Kingdom Hotels International and HBoS.

The Savoy sale, for £200m, also netted investors a significant return. According to documents filed in Dublin, the vehicle used to buy the Savoy Group, Coroin, made a profit of €58m from flipping the Savoy just eight months after buying the whole Savoy group from Blackstone for £750m.

The success is only increasing ambition. Irish investors spent €3bn buying property abroad in 2005, figures from the Irish Government's statistics office reveal. Two-thirds of this investment was in commercial property and much of it in the UK.

A study by CB Richard Ellis puts the amount spent by the Irish at €5bn in the UK and a further €2bn in other countries, making the Irish the most active overseas buyers. The CBRE study predicted that €9bn will be spent overseas this year, dubbing the Irish acquirers the "buyaspora".

The challenge for this flood of cash coming to the market will be finding deals that offer comparable returns to those done a couple of years ago. It will take more than the luck of the Irish.

Dawnay Shore delivers on valuation uplift

Dawnay Shore Hotels, the owner-operator set-up to give stock market investors the opportunity to access private equity type return via the listed vehicle the Hotel Corporation, has pushed like-for-like operating profits up 2.9% during 2005.

During the year the company bought seven hotels, increasing its room count from 1,800 to 2,700 across 20 properties.

Looking at the 16 longest held hotels (excludes the three Furlong properties and Walton Hall), revpar was modestly up at £101.36 compared to the previous year's £100.08, a rise of 1.3%.

Hotel operating profit, which is EBITDA excluding head office costs, was up £1m or 2.9% to £33.1m.

The AIM-listed Hotel Corporation owns 49.9% of DSH. This holding represents its principal asset. It reported a profit of £11.5m, including a revaluation gain. During the year it has paid, or is about to pay, a total of 5.8p in dividends.

The structure of the group, with debt accounting for four times the amount of equity, means that shareholders in the Hotel Corporation have a highly leveraged play. During the past year, this has worked to the benefit of shareholders and while hotel property prices remain robust, a strong return can be expected. At the interims, DSH reported a revaluation by Colliers Robert Barry that put a figure of £314m on the chain. This translates to a 24.5% uplift in net assets per share at year end, if the four most recently acquired assets are booked in at cost.

As well as passively benefiting from an increase in value, DSH is seeking to drive further increases through development activity. It cites the example of the Paramount Redworth Hall where a forthcoming 39-room extension is set to yield a net £4m after accounting for construction and financing costs.

DSH said that rising energy prices were such that turnover needs to climb by between 2% and 3% to offset increased costs.

Folio grows on investor appetite

Folio Hotels, the chain ran by former Regal Hotels directors Nicholas Crawley and Charles Holmes, has added 19 properties to bring its portfolio to 27.

The growth has been made possible by the appetite for hotel property among private investors prepared to offer even start-up hotel operators leases on yields of less than 7%.

Washington Hotels, a vehicle created by father and son Alan and Gary Landesberg, brothers David and Elliot Rosenberg, and Galliard Homes, has bought the latest batch for £116m.

The hotels have been let to Folio on 35-year leases and, although other terms have not been disclosed, previous deals done by these same buyers have been let to Folio at sub-7%.

Folio was formed in late 2004 when five hotels were bought from Corus by Leverguide, a vehicle created by the same parties as those involved in Washington. Among the properties in the £50m deal were the Richmond Hill and Richmond Gate hotels in West London.

The biggest was the Richmond Hill property which was bought for £30m on a 6.35% yield. The 138-room hotel is generating a rent of £2.01m, with rent reviews every five years.

A smaller hotel in the package, the 53-room Buckerell Lodge in Exeter, was sold for £4.1m on an initial yield of just below 7%.

The same investor group teamed up through a vehicle called Jefferson Hotels to buy nine hotels from Queens Moat Houses in October last year for around £100m. In this case, Rezidor leased eight hotels and turned them into Park Inns (one is held on a management contract).

The vendor in the current £116m deal is Malaysian conglomerate MUI which is booking a £300,000 gain on the disposal. MUI owns 99% of Corus Hotels, the group formerly known as Regal.

MUI, which also owns a UK retailer Laura Ashley, has been steady trimming its portfolio to pay down debt.

The last full year accounts for Corus, for the year 2004, show a £6.7m loss of which £4.3m were exceptional items. The five hotels bought by Leverguide generated pre-tax profits of £458,000 off sales of £7.07m.

During the year to December 31, 2005, MUI posted a net loss RM396m (US$108m), slightly less than the RM405m loss made the year before. Sales were down 16%.

It said it would continue to dispose of non-core and low-income generating assets.

Bumper deal year in 2005 and more to come

The European hotel investment market recorded a thumping €16.2bn of transactions during 2005, according to the latest Jones Lang LaSalle Hotels research.

This is almost double the level set in 2004 of €9.4bn and a full 42% ahead of what was achieved in 2001, the previous peak, and a year when the Meridien portfolio was in effect sold twice.

The record breaking figures have been achieved thanks to an abundance of stock for sale, said JLL. This was driven particularly by the desire of international hotel chains to sell hotel real estate.

A combination of private equity groups, high net worth individuals and institutions have snapped up what JLL describe as "highly desirable and rarely traded property".

Investor circumstance has been as much a motivator as the buying opportunity, conceded JLL. Opportunistic investors have been "actively seeking to place their funds before markets reach a plateau or interest rates threaten to rise".

In addition, the ever decreasing yields and shortage of supply of more established commercial property segments has driven traditional investors into the arms of hotel property vendors. On top of all this was cheap debt at high leverage.

Thanks to major disposals by InterContinental, Whitbread, Accor and Societe du Louvre portfolio deals in Europe topped €11.1bn. The focus was on the UK and France, accounting for 49% and 30% of deal volume by value respectively.

Single assets (those over €10m in value) have also seen a big surge in activity. The volume reached €5.0bn in 2005, 51% higher than the previous peak for single asset deals reached in 2004.

The single biggest source of investment funds has been private equity, accounting for 40% of the deals. The next biggest source was high net worth individuals, representing 16% of total deal volume. And publicly quoted hotel companies were the third biggest buyers at 10%.

Much of the cash being pumped into hotel investment is from private equity and much of the private equity investment is from US sources. Domestic players remain the biggest source of funds but US-based investors are the biggest non-domestic source.

CHE Group shows faith in mid-market

The much maligned mid-market full-service segment has refused to die despite dire predictions to the contrary for more than a decade.

And now CHE Group, the former Choice Hotels Europe, is once again talking a growth story for such properties.

CHE successfully raised £18.6m in January this year which it is currently ploughing into upgrading its existing hotels and rolling out the limited service Sleep Inn brand.

In the company's own words it is now seeking to transform itself from a "defensive survivor to being a more aggressive force" within its chosen areas of focus.

These areas are the previously mentioned premium limited service and "a focused offering within the mid-market full-service sector".

The easiest bit to sell was the £8.6m which is being ploughed into Sleep Inns. A director of development has been hired to take CHE's Sleep Inn portfolio to 60 properties within five years.

Much tougher to convince investors about, however, is the determination to grow in the mid-market segment. CHE says the segment is currently reinventing itself "as a consequence of the impact on buying methods brought about by low cost air carriers and the internet".

Further rationalisation of CHE's mid-market portfolio is promised as it seeks to "refine its offering in this area". Already re-shaped is the group's sales structure to recognise the role of the online intermediaries.

During 2005, CHE saw sales slump slightly by £0.4m to £79.2m. The pre-tax loss doubled to £0.4m although operating profit held firm at £4.6m.

Rising energy costs was the principal reason gross operating profit margin dropped 0.5 percentage points to 34.8%.

A similar looking set of numbers was also put out last week by Peel Hotels, the nine-strong chain also in the mid-market full-service segment. Operating profit was up slightly by 1.9% and pre-tax profits were static at £1.18m.

What was missing from the Peel results presentation, however, was the vision shown by CHE. Whereas the changed market conditions, and in particular the online threat, was flagged-up by CHE, it seems to be business as usual at Peel.

Shangri-La takes makes long march in China

Shangri-La Asia, the Hong Kong-based owner and operator of deluxe hotels, is continuing its focus on mainland China despite apparently slow profit growth from its investments in the country.

The company grew profits by less than 2% during 2005 in mainland China but still has 10 of its 12 equity development projects there.

Revpar at Shangri-la's existing mainland Chinese hotels was US$78 during 2005, markedly less than the US$188 achieved in Hong Kong. The previous year revpars were $72 and $157 respectively.

But the push into China by Shangri-La, controlled by Malaysian tycoon Robert Kuok, is a long-term affair.

Globally, the group is expanding via management contracts. But in China, Asia's largest deluxe hotelier, is prepared to commit its own capital.

The favoured path appears to be mixed-use developments usually undertaken with development partners such as the connected Kerry Properties Ltd or Allgreen, which is also a related company.

All told, the current scheduled development spending by Shangri-La amounts to $756m, to be funded by existing cash flow and bank debt.

Since being hit by the Asian financial crisis and then SARS, trade for Asian-based hoteliers has been picking-up, particularly in the last 18 months. This helped Shangri-La to report a 33% rise in net profits for 2005 to $151m. Revpar across the 36 owned hotels increased 16%.

Mainland China accounted for $278.6m of the $842m total revenues in the group, the largest contribution from a single country. The group has equity interests in 18 hotels and manages two hotels in mainland China, totalling 9,816 rooms.

In addition to managing all but one of the 36 owned hotels, the company has management contracts at 11 other hotels and 15 hotel development projects ranging from North America to the Middle East and from China to Australia. The management business grew revenues by 33%.

The London Bridge Tower hotel, held on an operating lease and expected to open in 2010, is set to cost $40m in fit-out and pre-opening expenses. Although this project was signed in January 2005, the European debut for the Shangri-La brand will be the Prince Roland Bonaparte in Paris which was bought for €92m in January this year and is set to open its 140 rooms in late 2008.

Timeshare comes in from the cold

Timeshare is attracting the attention of stockmarket investors, heard attendees at the 7th Annual Timeshare and Resort Investment Conference

Timeshare is now a $9bn worldwide industry, according to Rip Gellein, chief executive officer officer of Starwood Vacation Ownership and chairman of the American Resort Development Association.

He told delegates at the 7th Annual Timeshare and Resort Investment Conference that between 1990 and 2004, the compound annual growth rate for the industry had been 9%.

"The future demographic trends are very positive and Wall Street is beginning to pay attention," he said.

There were strengths compared to the hotel business including that it was not cyclical and that occupancies were typically higher, often as much as 20 percentage points compared to hotel industry averages.

Interval International's David Gilbert listed a number of trends that were influencing growth. For consumers these include product credibility, constructive legislation, costs to acquire second homes were increasingly prohibitive, timeshares offer the ability to stabilise the cost of holidays, there was a growing interest in condo accommodation for families rather than hotel rooms and there was product flexibility via the exchange companies (of which Interval is one).

Alongside the benefits to consumers, there were also factors aiding developer interest. These included the ability to accelerate cash flow and to shift debt and equity requirements onto the consumer; the significant synergies in mixed use that see higher occupancy and enhanced use of the resort if timeshare is built alongside; product resilience thanks to holidays remaining essential even during downturns; the single digit penetration of income eligible households; and the cross selling opportunities.

For Scott Berman, a partner of PricewaterhouseCoopers global hospitality and leisure division, the timeshare industry has been legitimised.

"The timeshare industry can be divided into two generations: before 1990 and after," he said. While the snake-oil salespeople of 20 to 30 years ago have gone, it remains important to have a well designed sales programme, he added.

Condo hotels where rooms are sold to individual owners and then put back into a rental pool have been around for a long time, said John Melicharek, partner at law firm Baker & Hostetler, but are hot right now due to a "perfect storm" of low interest rates, lots of baby boomers, dollar depreciation and so on.

He warned, however, that in the US context condo hotels risk violating securities laws as they can be seen as an investment contract. If the rental programme is not carefully constructed then the developer will face the expense and difficulty of complying with securities legislation.

PWC's Berman added that some large brands were retreating from condo hotels. "The jury is still out on the operating company although the real estate has been a success," he said.

Matt Hagler, senior vice president at the Ginn Development Company, said that successful condo hotels were about selling a club not real estate.

> "An industry based on the bonds of family has a strong future. It's a case of good value meeting good values," Bill Marriott

Peter Yesawich, CEO of Yesawich, Pepperdine, Brown & Russell, explained the non-cyclical nature of timeshare by pointing out that between 2002 and 2004 the incidence of travel declined mainly due to falling amounts of business travel. But during this period the incidence of taking a vacation actually increased.

He added that changing social values that were placing more emphasis on getting families together offered an increased opportunity for timeshare.

And timeshare was increasingly acceptable: just over half of the American population now feel either positive or neutral about the term.

A key challenge was overcoming the fact that timeshare costs more to sell than to make. For independents, sales people receive commissions of up to 15% while the sales managers receive another 3%. The most efficient programmes were those that persuaded people to trial and the internet has a key role in attracting people researching opportunities.

The key factor was that timeshare " is not selling bricks but selling a dream", he concluded.

The industry had been hurt in the short term by restrictions on its selling techniques, such as "do not call" lists, but in the longer term it has benefited, said Billy Curran, CEO of InnSeason Resorts. "I was tired of chasing people that did not want to speak to me," he said.

A key change was the arrival of the brands in the 1990s. Deborah Linden, CEO of Island One Resorts, said that the involvement of brands led to more relationship marketing. "Efficiencies can be better by having relationships. Referrals are much more effective," she said.

The net result has been a more educated consumer base and a faster growing industry, said Matthew Avril, managing director of operations at Starwood Vacation Ownership.

It took 20 years, from 1980 to 2000 for the timeshare industry to reach $4bn worth of annual sales. But it took just four years, from 2000 to 2004, to double this to $8bn.

"The large branded companies have been an accelerator of timeshare growth. They have a much larger platform from which to sell," said Avril.

Bill Marriott, chairman and CEO of Marriott International, was a keynote speaker at the conference. He said Marriott's involvement in the timeshare industry dates back to 1984 when it bought American Resorts.

The volume of sales at this entry point was just $5m but Marriott has rapidly expanded its business. "When customers wanted an extra pillow, we sold them a vacation," said Marriott.

Vacation ownership has now grown to be a major and permanent extension of the hospitality industry. "When people buy our stock today, they are thinking as much about the double digit growth in our timeshare business as they are about traditional lodging," said Marriott.

Half of Marriott Vacation Club International's sales come from owner referrals. "This is the ultimate stamp of approval," said Marriott.

The strength of timeshare was that it enhances family values. "An industry based on the bonds of family has a strong future. It's a case of good value meeting good values," said Marriott.

• The 7th Annual Timeshare & Resort Investment Conference took place on October 17th to 19th 2005 at the Peabody Orlando in Florida.

Fears over deals at Berlin

Speakers at the International Hotel Investment Forum debated whether the current flood of deals were being struck at sustainable price levels

Anders Nissen, CEO at Pandox, told delegates at the International Hotel Investment Forum that although it was easy enough to find the money it was harder to find good deals. And he was concerned about the nature of current deals.

"The private equity guys are living in a relative world and compare sectors. But they are comparing fixed contracts to management contracts."

"Maybe we will have to take care of the problem these guys have in a couple of years due to their very aggressive yields," he said.

Lack of knowledge was driving short-term thinking, he argued. "Sometimes I think we are back in the late 1980s. There is too much focus on financial issues."

He predicted that New York would peak out by the end of the year, with London following and then the rest of Europe. He asked: "What will happen when the hotel business cycle begins to decrease?"

But there are plenty more deals to be done, according to Rob Seabrook, evp at Jones Lang LaSalle Hotels. He said that he was anticipating Eu19bn of transactions this year, compared to the Eu16.5bn struck in 2005.

The banking environment was good, investors were more sophisticated and willing to take on risk and operators were willing to divest, he added.

Seabrook was concerned, however, about whether some of the current crop of syndicate transactions left enough room in them to fund capex programmes.

New vehicles were also being created. Jean Luchet, senior vp in the assets financing division of Accor, said that his company's deal with French REIT vehicle Fonciere des Murs was a real partnership that defined a new balance with investor and operator.

The key was obtaining variable leases with no guarantees. The success of the first deal struck in June last year was repeated this year with the exception that yield was down 50 basis points.

Fonciere des Murs now has the biggest portfolio of assets run by Accor, including 12 international sites that came with the latest transaction.

This shows it can do deals outside of France that are still profitable despite no tax advantages, said Luchet.

"What we had in mind was to restructure with a strong commitment from the investors to stay with us. We wanted firstly to sell the assets on the low point of the yield curve and secondly to ensure that we had no difficulty paying the rent," said Luchet.

It was important to have a long term relationship with the investor. The owner needs the capacity to do work on the hotel as needed by the operator. This was hard to do if there is one investor after another, said Luchet.

Ted Darnall, president of Starwood Hotels real estate group, said that the US REIT market had matured nicely since the introduction of the REIT Modernisation Act of 1999 allowing REITs to enter into management contracts.

"It is a quality of portfolio issue now, and those REITs with the best receive the best rating," he said. This has resulted in REITs acquiring international assets, he added.

Starwood wanted to evolve into a branded hospitality management company and wanted to do so with strategic partners, said Darnall.

The company had early conversations with Host who wanted to diversify and wanted overseas assets.

For financial buyers, leverage was allowing them to get higher velocity on their return on equity. "It is more about velocity than appreciation," said Darnall.

The expectations of shareholders post the Host deal is that Starwood will be a growth company. "If we can convince them then we will get a multiple that will keep us independent. The risk for companies transitioning is that they can't meet growth expectations," he said.

InterContinental cannot pay down any more debt otherwise it will be in the business of lending money, said Richard Hartman, managing director for InterContinental EMEA.

"We have already given back £2.7bn. What we do now depends on the opportunities. We may spend," he said.

The company intends to keep about £1bn of real estate – "the InterContinentals that define the brand" – but Hartman said that some of this will be churned.

The past few years had seen a "deliberate cleansing" of InterContinental's system with eight hotels exiting for every 10 brought in. This did not mean that hotels had to be identical products like Coke or Cadbury.

"We will have variation but we have to create variation that is predictable and understandable," he said. The key was getting inside the customer's brain. "Just doing things by the numbers or on the back of great general managers is not enough," he said.

An example of predictable variation would be bringing the Indigo brand to EMEA. Hartman said it would not work in its current format and will need to be redesigned to enable city centre conversions.

Roeland Vos, president for EMEA at Starwood Hotels, said his company was working hard to bring its residential property expertise to Europe from the US. "[Branded property] is becoming more important as part of people's lifestyle. They buy into on a long-term basis which can range from timeshare to straight resi," he said.

Brands are key to penetrating new markets. Vos said that China is developing a need for hotel brands and those brands that develop a relationship with Chinese consumers best will need to be present in the home market.

The arrival of private equity owners en masse was beneficial in that they understand branding, said Vos.

Wolfgang Neumann, area president for Europe and Africa at Hilton, said the private equity gorillas have done a lot for the industry. "They are detached from the business emotionally and look only at returns. They are demanding and challenging," he said.

Sir Rocco Forte was less charitable, however. He said that Blackstone had destroyed the Savoy Group. "They came in and said they were going to flip it in five years. They completely undermined the business," he said.

• The 9th International Hotel Investment Forum was held on March 6th to 8th at the Berlin InterContinental. Hotel Analyst was a media sponsor of the event.

Deal of the year

Best new development:
Four Seasons Hampshire
Single asset deal:
Kingdom Hotels International for purchase of Savoy
Portfolio deal:
Starwood Capital Europe for Societe du Louvre

Private equity continues its march into hospitality

The seemingly unstoppable march of US private equity into the hospitality business took another stride forward with Blackstone's swoop on Hospitality Europe.

The challenge for Blackstone in its latest dabbling, however, is spotting the turn with the eight hotels in the portfolio it has bought for a reported €650m.

The sale of the 3,227 rooms in the HEBV portfolio has been an on-again off-again affair for several years. Last October it again made a formal announcement that it was seeking an exit, either through a sale or an IPO.

The problem for the company is that, in comparison to many hotel assets that have been brought to market, it has been too well managed.

Its hotels, located mainly at airports in Amsterdam, Brussels, Frankfurt, Paris, Prague and Stockholm, are well run (the operators are Starwood, Marriott or Hyatt) and have been actively asset managed. It is hard to see where a repositioning is easily possible.

Despite this, the portfolio appears to have attracted significant interest from other bidders including Whitehall Street and Citigroup. With an initial yield of 6%, Blackstone needs to have more up its sleeve than simply increasing leverage.

Meanwhile, Blackstone has also paid £205.4m for Center Parcs business. The past year has seen Blackstone spend more than $12bn on hotel assets, mostly in North America. Both Europe and Asia Pacific are expected to be key target areas going forward as US opportunities dry-up.

The offer for Center Parcs is pitched at 80p, about 16% higher than the AIM-listed company's previous close but 20p down on the price at flotation two years ago. Poor short-to-medium-term prospects make rival bids unlikely. Pierre & Vacances, which owns the continental European Center Parcs business, had previously shown an interest.

Blackstone already owns the Legoland leisure park and Merlin Entertainments, owner of the London Dungeon visitor attraction, but it is not thought likely to bring the disparate assets together.

Instead, Blackstone is thought to be eyeing the purchase of the property interests that comprise the four villages in the UK business of Center Parcs, currently owned by the Royal Bank of Scotland and Sun Capital.

In the US, Blackstone paid $3.4bn to buy La Quinta Inns and $3.2bn to buy Wyndham International in 2005. This year it bought the REIT MeriStar Hospitality for $4.2bn.

Colonising the hotel industry

Private equity firms have been leading the charge into hotel property investments

The eight to 10 year cycle for private equity funds neatly matches the hotel operating cycle, said Sebastian Bazin, managing director Europe for US private equity firm Colony Capital, speaking as part of the conference programme at MIPIM.

During his keynote presentation 'Investment trusts in the hotel industry', he noted that another attraction for private equity regarding hotels was the less crowded market (although this was rapidly changing). This was partly because investing in hotel property requires industry-specific expertise rather like logistics property investments.

The adaptive nature of private equity means it can exploit inefficiencies in markets to stay ahead of the investment curve, argued Bazin. In addition, as it was discretionary capital within the funds there was no need to go through the same portfolio balancing process as pension funds.

The flexibility and reactive nature of private equity, combined with fewer restraints on management and access to a larger spectrum of investment products, all meant that internal rates of return (IRR) could be achieved that were in excess of 20%.

Bazin rejected the characterisation of private equity returns being built on striking over-leveraged deals. At Colony, the average debt and equity ratio was 50:50, he said.

The average IRR for Colony's investments in Asia was 28%, just above the 27% achieved in Europe. In North America, which was a more mature market said Bazin, IRR averaged 20%.

Where private equity is uncompetitive, however, is with mature assets where there was little chance of repositioning to add value.

The creation of French Sociétés d'Investissements Immobiliers Cotées (SIIC) structure, along the lines of real estate investment trusts in the US, had created more competition.

Bazin said that in the auction for 128 hotels sold by Accor last year, the pricing advantage was 20% to 25% in favour of the SIIC Fonciere des Murs compared to Colony Capital.

In particular, where as Colony had to pay capital gains tax of 35%, Fonciere des Murs had only to pay 16.5% on the latent gain due to its special tax status.

Almost a third of Colony's activity has had to be rethought as a result of the creation of SIICs, concluded Bazin.

Colony was one of the leading hospitality investors, said Bazin, pointing to the 27 transactions it has struck. Its most recent major deal involved the purchase of Raffles Holdings in Singapore and then the merger with Fairmont of Canada.

Globally, 29% of investments are made in hotels and 19% in gaming, meaning almost half of the funds investments are hospitality related.

• **MIPIM was held in Cannes on March 14-17.**

Financial institutions show ambition in hotels

Although it might appear that financial institutions have only recently began investing in the hotel sector, the interest has been there for a number of years, said Anne Lemonnier, a London-based executive director of US investment bank Lehman Brothers.

Speaking during a conference session at MIPIM she said: "Maybe it is that we are more visible right now." Lehman Brothers was part of the consortium that last year paid £1bn to buy a portfolio of 73 InterContinental hotels in the UK.

"We see the hotel industry as one of key asset classes alongside offices and retail," said Lemmonier.

Concerning the balance between generating returns from operations and making a return on the exit of the investment, she said that the exit was crucial to reaching the 20% to 25% returns that her company has historically achieved.

Lloyd Lee, managing director Europe for Starwood Capital, said that he expected to see continued consolidation within the European hotel industry due to the large amount of capital around.

Starwood Capital, a private equity firm, had distinguished itself by operating as well as owning hotel property. With its latest acquisition, Societe du Louvre of France, it had just begun the process of building brands, he said.

The diversification into hotels started at private investment company London & Regional about six or seven years ago, said Daniel Poser, managing director of the hotels wing.

As a private company funded using internal capital, London & Regional could make longer-term investments than could many rival financial investors, he said.

Room rate is not everything

Hotels in Rome had the highest room rate at €185.71 during the first two months of this year among the 10 cities selected for TRI Hospitality Consulting's Europe HotStats sample.

But the Italian capital was only third placed when it came to revenue per available room, coming in at €112.99, below Paris at €114.27 and top placed London with €123.83.

The problem for Rome is that its occupancy rate places it down at seventh on the list with 60.8%. London, on the other hand, has the busiest hotels in the sample with an occupancy rate of 74.2%.

"It is superficially attractive to push room rates as high as possible but unless you also fill your hotels, the net result is not as beneficial as when a more balanced approach is taken," said Jonathan Langston, managing director of TRI.

At the other extreme in the sample of 10 is Hamburg which has the fifth best occupancy at 62.4% but manages to be second from bottom with both rate and revpar. And worst of all is Budapest, which is bottom in all three categories.

The saving grace for Hamburg is that it enjoyed the best increase in revpar in the sample for the first two months of this year. The next best increases came at Paris, Brussels and Rome, respectively, showing that the continental European pick-up in trading is gathering pace. Only Munich recorded a decrease in revpar for the first two months.

"Momentum is usually what investors look for when deciding where to put their money. On this basis, continental Europe appears increasingly attractive," said Langston.

While Budapest is clearly the weakest in terms of absolute performance, it has done better when rate of change is considered, particularly regarding achieved room tariffs. The Hungarian capital had the biggest increase in room rate during the first two months, at 9.1%.

Less impressive in Budapest was the occupancy performance, where a 0.4 percentage point drop put it in ninth place in the sample. This meant that revpar change was mediocre with an 8.2% rise putting it into sixth place.

"Eastern Europe has been the focus for much investor attention of late and there is clearly opportunity. But our figures show that there is still plenty of trading uplift coming in the more established markets in Western Europe," said Langston.

European chain hotels – performance report

The 2 months to February 2006

	Occ %	ARR	RevPAR	Payroll %	IBFC PAR
Amsterdam	65.8	129.69	85.39	42.4	29.08
Berlin	57.8	120.48	69.59	40.4	20.69
Brussels	62.8	110.13	69.19	49.2	18.15
Budapest	51.5	91.06	46.85	37.2	17.09
Hamburg	62.4	93.81	58.53	35.8	24.79
London	74.2	166.82	123.83	29.5	71.88
Munich	60.5	97.64	59.11	34.9	24.26
Paris	68.8	166.19	114.27	45.9	41.52
Rome	60.8	185.71	112.99	46.3	29.68
Vienna	55.7	126.3	70.33	54.1	13.88

The 2 months to February 2005

	Occ%	ARR	RevPAR	Payroll %	IBFC PAR
Amsterdam	66.3	124.56	82.63	42.4	30.39
Berlin	51.7	124.95	64.58	41.6	17.84
Brussels	56.2	112.92	63.47	50.2	15.15
Budapest	51.9	83.5	43.31	37.9	14.51
Hamburg	57.7	89.33	51.54	40	17.52
London	72.7	157	114.09	30.7	65.99
Munich	60.9	100.5	61.2	35.2	28.02
Paris	63.1	163.75	103.33	50.4	31.76
Rome	55.1	188.68	103.94	45.5	38.07
Vienna	55.3	125.12	69.14	53.5	15.94

Movement for the 2 months to February

	Occ Change	ARR Change	RevPAR Change	Payroll Change	IBFC PAR Change
Amsterdam	-0.5	4.10%	3.30%	0.00%	-4.30%
Berlin	6.1	-3.60%	7.80%	-3.00%	16.00%
Brussels	6.6	-2.50%	9.00%	-1.90%	19.80%
Budapest	-0.4	9.10%	8.20%	-1.70%	17.80%
Hamburg	4.7	5.00%	13.60%	-10.30%	41.50%
London	1.6	6.30%	8.50%	-3.90%	8.90%
Munich	-0.3	-2.80%	-3.40%	-0.90%	-13.40%
Paris	5.7	1.50%	10.60%	-8.80%	30.70%
Rome	5.8	-1.60%	8.70%	1.90%	-22.00%
Vienna	0.4	0.90%	1.70%	1.10%	-12.90%

Source: TRI Hospitality Consulting

UK revpar growth remains

Room revenue per available room was up 3.3% during February 2006 compared to the same month a year ago, according to the latest figures from TRI Hospitality Consulting's HotStats survey.

London hotels were strongest with a rise of 4.7%. Both occupancy and room rate increased, up 1.1 percentage points and 3.2% respectively.

Hotels in the provinces had a stronger increase in rate, at 3.8%, but a 0.8 percentage point fall in occupancy meant that room revpar was up less than in the capital at 2.5%.

Overall revpar, taking into account non-room items such as food and beverage, showed a 2.2% increase at all UK hotels in the HotStats sample.

"February has been a steady month for UK hoteliers, with sales revenues keeping just ahead of inflation," said Jonathan Langston, TRI's managing director.

Taking the first two months of this year and comparing them to 2005, shows that room revpar is 3.7% higher and overall revpar 3.0% higher.

London is again ahead of the provinces with a 5.5% rise in room revpar thanks to a 3.7% increase in rate to £94.37 and a 1.3 percentage point hike in occupancy to 74.8%.

UK provincial hotels lag only slightly, however, with a 2.8% rise in revpar. Occupancy virtually stood still, with a small drop of 0.3 percentage points, and rate was up 3.3% to reach £67.70.

"With more subdued topline growth than

The month of February 2006

			Rooms Department Headlines			Business Mix – Rooms				
	Month	Region	Occupancy	Average room rate	Room revpar	Commercial	Conference	Tours/groups	Leisure	Other
Current year	February 2006	London	78.20%	£95.57	£74.72	44.50%	5.90%	16.30%	18.80%	14.50%
	February 2006	Provincial	67.80%	£68.47	£46.40	46.60%	13.50%	6.00%	27.50%	6.40%
	February 2006	All	71.00%	£77.68	£55.14	45.90%	10.90%	9.50%	24.50%	9.20%
	Month	Region	Points	%	%	Points	Points	Points	Points	Points
Year on year change	February 2006	London	1.1	3.20%	4.70%	3.3	-0.3	1.1	-1.3	-2.8
	February 2006	Provincial	-0.8	3.80%	2.50%	2.8	1.5	-0.8	1.9	-5.4
	February 2006	All	-0.3	3.70%	3.30%	2.9	0.7	0.1	0.6	-4.3
	Month	Region	Occupancy	Average room rate	Room revpar	Commercial	Conference	Tours/groups	Leisure	Other
Last year	February 2005	London	77.10%	£92.57	£71.38	41.20%	6.20%	15.20%	20.10%	17.30%
	February 2005	Provincial	68.60%	£65.99	£45.27	43.70%	12.00%	6.80%	25.60%	11.80%
	February 2005	All	71.30%	£74.92	£53.38	43.00%	10.20%	9.40%	23.90%	13.50%

The 2 months to February 2006

			Rooms Department Headlines			Business Mix – Rooms				
	Month	Region	Occupancy	Average room rate	Room revpar	Commercial	Conference	Tours/groups	Leisure	Other
Current year	YTD	London	74.80%	£94.37	£70.60	44.00%	6.90%	16.20%	17.30%	15.50%
	YTD	Provincial	62.70%	£67.70	£42.43	49.70%	13.40%	5.90%	24.30%	6.70%
	YTD	All	66.40%	£77.00	£51.15	47.70%	11.10%	9.50%	21.90%	9.80%
	Month	Region	Points	%	%	Points	Points	Points	Points	Points
Year on year change	YTD	London	1.3	3.70%	5.50%	4.1	-0.3	-1.2	-2.2	-0.3
	YTD	Provincial	-0.3	3.30%	2.80%	5.6	0.6	-1.3	0.4	-5.2
	YTD	All	0.2	3.50%	3.70%	4.9	0.1	-0.9	-0.7	-3.4
	Month	Region	Occupancy	Average room rate	Room revpar	Commercial	Conference	Tours/groups	Leisure	Other
Last year	YTD	London	73.50%	£91.04	£66.93	39.90%	7.20%	17.50%	19.50%	15.90%
	YTD	Provincial	63.00%	£65.55	£41.29	44.10%	12.80%	7.20%	24.00%	12.00%
	YTD	All	66.30%	£74.39	£49.30	42.80%	11.00%	10.50%	22.50%	13.20%

steady

we have seen than in the past couple of years, hoteliers are under even more pressure to contain costs to ensure profits continue to rise," said Langston.

UKinbound, the official trade body representing the inbound tourism industry in the UK, said that figures collected in its monthly survey for January 2006 show that visitor arrivals were up 4.9% for its members.

This was a cause for some optimism, said the organisation, and added that consumers are becoming increasingly inured to the hazards of international travel if the product is good and the price is right.

UKinbound was, however, less impressed with the increasing cost of taxation and regulatory compliance. It said that this has grown faster in the UK over the last 10 years than for any of the country's main competitors. It fears this may undermine the industry's good work and cause it to fail to capitalise fully on the Olympics in 2012.

At BAA, the operator of seven UK airports including Heathrow and Gatwick, passenger traffic was up 2.5% during February compared to the same month a year earlier.

The biggest growth was in long haul flights, excluding North Atlantic, which were up 8.4%. The North Atlantic routes continue to decline, dropping 1.5%.

"We are seeing an encouraging picture for the hospitality industry overall but there are notable areas of concern, particularly with rising costs," said TRI's Langston.

Business Mix – Rate £					Departmental revenues				Departmental revenues mix %				IBFC	
Commercial	Conference	Tours/groups	Leisure	Other	Rooms	Catering	Other	Total revpar	Rooms	Catering	Other	Total revpar	IBFC %	IBFCpar
£122.90	£105.19	£55.79	£63.14	£63.00	£2,097	£906	£154	£3,157	66.40%	28.70%	4.90%	100.00%	40.30%	£1,271
£75.26	£67.55	£47.03	£44.15	£46.47	£1,335	£1,009	£258	£2,602	51.30%	38.80%	9.90%	100.00%	28.90%	£751
£90.99	£74.51	£52.14	£49.11	£55.34	£1,574	£977	£225	£2,776	56.70%	35.20%	8.10%	100.00%	32.90%	£915
%	%	%	%	%	%	%	%	%	Points	Points	Points	Points	Points	%
5.80%	-2.70%	-3.90%	-28.30%	52.60%	4.70%	-0.50%	5.10%	3.20%	1	-1.1	0.1	–	-2.5	-2.80%
6.20%	-12.70%	43.30%	-1.10%	226.80%	3.40%	-1.10%	4.50%	1.70%	0.8	-1.1	0.3	–	-3.4	-9.00%
8.20%	-10.20%	15.20%	-11.90%	123.40%	4.00%	-0.90%	4.60%	2.20%	0.9	-1.1	0.2	–	-3	-6.40%
Commercial	Conference	Tours/groups	Leisure	Other	Rooms	Catering	Other	Total revpar	Rooms	Catering	Other	Total revpar	IBFC %	IBFCpar
£116.18	£108.07	£58.04	£88.08	£41.27	£2,002	£911	£146	£3,060	65.40%	29.80%	4.80%	100.00%	42.70%	£1,308
£70.89	£77.36	£32.81	£44.64	£14.22	£1,290	£1,021	£247	£2,558	50.40%	39.90%	9.70%	100.00%	32.30%	£825
£84.10	£83.01	£45.25	£55.75	£24.78	£1,514	£986	£215	£2,716	55.80%	36.30%	7.90%	100.00%	36.00%	£977

Source: TRI Hospitality Consulting

Business Mix – Rate £					Departmental revenues				Departmental revenues mix %				IBFC	
Commercial	Conference	Tours/groups	Leisure	Other	Rooms	Catering	Other	Total revpar	Rooms	Catering	Other	Total revpar	IBFC %	IBFCpar
£120.07	£107.27	£56.42	£70.59	£62.30	£4,042	£1,783	£298	£6,123	66.00%	29.10%	4.90%	100.00%	39.50%	£2,418
£73.64	£72.62	£46.19	£49.64	£45.97	£2,479	£1,910	£496	£4,885	50.80%	39.10%	10.10%	100.00%	25.80%	£1,261
£88.74	£80.25	£52.34	£55.48	£55.05	£2,970	£1,870	£434	£5,274	56.30%	35.50%	8.20%	100.00%	30.80%	£1,624
%	%	%	%	%	%	%	%	%	Points	Points	Points	Points	Points	%
4.50%	-0.90%	12.10%	-19.00%	12.30%	5.20%	2.20%	4.60%	4.30%	0.6	-0.6	0	–	-1.5	0.40%
4.30%	-5.20%	50.20%	7.10%	179.10%	3.90%	0.10%	3.70%	2.40%	0.7	-0.9	0.1	–	-3.6	-10.10%
6.00%	-3.50%	27.20%	-3.60%	75.70%	4.40%	0.70%	3.90%	3.00%	0.7	-0.8	0.1	–	-2.8	-5.50%
Commercial	Conference	Tours/groups	Leisure	Other	Rooms	Catering	Other	Total revpar	Rooms	Catering	Other	Total revpar	IBFC %	IBFCpar
£114.85	£108.30	£50.33	£87.20	£55.47	£3,843	£1,744	£285	£5,873	65.40%	29.70%	4.90%	100.00%	41.00%	£2,407
£70.61	£76.62	£30.75	£46.36	£16.47	£2,387	£1,908	£478	£4,773	50.00%	40.00%	10.00%	100.00%	29.40%	£1,403
£83.71	£83.19	£41.13	£57.56	£31.34	£2,844	£1,857	£417	£5,118	55.60%	36.30%	8.20%	100.00%	33.60%	£1,719

Source: TRI Hospitality Consulting

Hotel Chains and The Common

Introduction

The Common Standards for Hotels unifies the hotel classification schemes of the UK Tourist Boards and the UK motoring organisations into a singular structure. It is the latest version of the star grading of hotels that was introduced by the Automobile Association almost a century ago in 1912. It is also the most pervasive version that has the goal of imposing its explicit criteria on all hotels in the UK and it has serious implications for hotel chains.

Hotel Classification Schemes

In the Common Standards for Hotels the minimum requirements for one star hotels relates to the facilities, services and products that differentiate hotels from other lesser serviced accommodation such as budget accommodation and guest houses. The requirements for two, three, four and five star hotels are progressive enhancements of these criteria, even in terms of cleanliness, maintenance and hospitality and the differences between star levels are often differentiated by subjective terms such as "acceptable", "good" and "excellent".

The UK now has one of the most comprehensive hotel classification schemes and there are broadly similar approaches in the USA where the American Automobile Association grades hotels with up to five diamonds rather than stars and some continental European countries where grades are inflated so that a four star hotel corresponds broadly to a three star hotel in the UK. Typical examples of other schemes that focus only on selected hotels are The Good Hotel Guide and The Michelin Guide.

In addition, there are many more international approaches that are less systematic and less objective. Tour operators such as First Choice, My Travel and Tui and many online travel agencies such as Expedia and Travelocity typically classify hotels less systematically, while some online agencies such as Trip Advisor and Active Hotels provide subjective customer responses to hotels as the basis of rating. Still other small online agencies such as hotels.nl and even some of the providers of RevPAR data such as The Bench allow hotels to classify themselves. The inevitable outcome of the diversity of approach is that the same hotel is often rated differently.

In spite of the operational diversity, all of the approaches seek to reduce the entire range of facilities, services and products in a hotel to a single, shorthand rating for customers to understand hotel provision and the experience they are likely to encounter in a hotel. They also provide the fundamental basis on which the hotel industry has differentiated hotel supply over the past century. As a result, the impact of the classification schemes should not be underestimated. Hotels are the only hospitality or travel business to have such a comprehensive categorisation and it is remarkable that it has lasted for a century. The question is how effective is it for both hotels and customers in the 21st century.

Over the past century hotel demand and the hotel industry have changed in fundamental ways. The growth of business demand into hotels, the use of hotels as destinations for conferences and leisure activities and the development of hotel chains are among the most important. In contrast, the approach to hotel classification has changed little, apart from incorporating the modernisation of hotel facilities such as the introduction of en suite bathrooms.

In the USA and UK new hotels are almost exclusively affiliated to hotel chains because the hotel capital markets have become more rational and in other countries this development is accelerating. As hotel chains grow and dominate the market, unaffiliated hotel stock declines in volume, quality, market relevance and performance. By the end of 2004, 157 hotel brands accounted for the majority of hotel rooms in the UK. In the current AA scheme the chains have no one star hotels and in London alone they account for 80% of the five star hotel rooms. If there is to be a singular structure for hotel classification then it must square with the reality of the hotel business, which entails that it must accommodate the facts of life of the chains. In terms of the concept of the hotel on which the Common Standards are based and in their assumptions about customer selection of hotels they do not square with the facts of life of hotel chains and they underestimate the ability of customers to make complex choices.

The concept of the hotel

The concept of the hotel used in the Common Standards is a critical issue, particularly when they assert that, "any establishment operating with the word *hotel* as part of their business name will be assessed using the hotel requirements we list". They have produced a set of defining characteristics of hotels and they have the goal, backed by the UK Government, of grading all hotels. As a result they have embarked on a course that will establish them as the regulator of the UK hotel industry. This is a radical development about which we have many concerns.

The first problem about their concept of the hotel is that they require hotels to have a restaurant and bar as well as bedrooms, but it is unclear where the Common Standards for Hotels stand on private hotels, residential conference centres, holiday centres and other hotel equivalents. Their definition of hotel excludes the economy and budget brands from classification as hotels because most of them have limited restaurant and bar provision and not because their bedrooms, lobby, corridors and staircases are inferior to one star hotels. At the very least this is contorted logic to which we will return later.

Standards for Hotels

The second problem compounds the first. Not only must a hotel have a restaurant and bar, but also the constituent parts of the hotel must be consistent in terms of quality. A three star hotel is required to have three star facilities, products and services throughout the hotel – rooms, restaurants, bars and other public areas such as lobbies, sitting areas, corridors and staircases. This conception of the hotel does not account for the economic realities faced by many hotel brands, it constrains innovation by hotel chains in adapting to market demand and it is a threat to the achievement of effective returns on hotel investment.

The alternative and more relevant approach for hotel chains is to start from the notion of the hotel without the requirement to integrate the mandatory range of non-room facilities and services congruent with the quality of the bedrooms. This involves the use of independent supply variables such as hotel configuration and market level.

Hotel configuration

It is a challenge for hotels to achieve double-digit EBITDA margins for non-rooms facilities, while the rooms business can typically achieve EBITDA margins of over 50%. Thus, it is imperative for the chains and their investors to be convinced of the specific demand for non-rooms facilities before they invest and it is contrary to business logic for them to provide uneconomic facilities merely because hotel classifiers, with no interest in performance, impose a requirement.

Hotel configuration systematically ranks the non-room facilities in hotels as follows:

Non-Room Facilities	Hotel Resort	Full Feature Hotel	Basic Feature Hotel	Limited Feature Hotel	Rooms-Only Hotel
Restaurants (minimum number)	1	1	1	1	0
Bars (minimum number)	1	1	1	optional	0
Conference Rooms (minimum number)	1	1	optional	optional	0
Indoor Health and Fitness (minimum number)	1	1	optional	0	0
Outdoor Health and Fitness (minimum number)	1	optional	optional	0	0
Retail Outlets (minimum number)	optional	optional	0	0	0
Casino (minimum number)	optional	optional	0	0	0
Minimum Non-Rooms Facilities	**5**	**4**	**2**	**1**	**0**

Source: Otus & Co

The structure of hotel configuration is also seen in the proportion of hotel turnover derived from bedrooms, 100% in rooms-only hotels declining to around 40% in hotel resorts. The pattern of hotel configuration for affiliated hotels in the UK at the end of 2004 was as follows:

Hotel Configuration	Hotels	Rooms	% Hotels	% Rooms
Hotel Resort	44	5,870	2%	2%
Full Feature Hotel	649	105,420	25%	44%
Basic Feature Hotel	974	64,350	37%	27%
Limited Feature Hotel	479	40,835	18%	17%
Rooms-Only Hotel	481	24,220	18%	10%
Total	**2,627**	**240,695**	**100%**	**100%**

Source: Otus & Co

The brands excluded from the Common Standards for Hotels are predominantly limited feature or rooms-only brands and account for 27% of affiliated room stock. The differences in the five levels of hotel configuration are differences in degree and not differences in kind as the Common Standards have assumed. Thus, the exclusion of the limited feature and rooms-only brands from hotel classification is based on spurious logic.

In addition to the allocation of a star classification the Common Standards for Hotels will position each hotel in a "descriptive sub category" – hotel, country house hotel, small hotel, town house hotel and metro hotel. Each "descriptive sub category" is a confusion of random hotel and location supply variables that are defined so loosely that each sub category is not independent and the same hotel can fit different sub categories. Applying the "descriptive sub category" definitions to the affiliated hotels in the UK there are no metro hotels, 0.5% of the rooms can be designated as country house hotels, 0.8% of the rooms are in small hotels with less than 20 rooms and less than 0.2% can be designated as town house hotels. The remaining 98.5% of the rooms are in hotels. The "descriptive sub categories" are confused nonsense and irrelevant to the chains.

Hotel Chains and The Common Standards for Hotels continued

Market level

Market level is most effectively defined by and is restricted to the level of investment in bedrooms, lobbies, corridors and stairs. It is manifest in the size of bedroom and the extent and quality of their furniture, fixtures and fittings. In this approach market level is not a function of all facilities in a hotel as is the case with the Common Standards. Benchmark brands for each market level include the following and correspond broadly with the bedroom furniture, fixtures and equipment used in the Common Standards for each star level.

Deluxe	Up Market	Mid-Market	Economy	Budget
Conrad	Clarion	Country Inn by Carlson	Bastion	Etap
Four Seasons	Crowne Plaza	Courtyard by Marriott	Campanille	Formula 1
Manderin Oriental	De Vere	Four Points	Comfort	Premiere Class
Maybourne Hotels Group	Grand Hyatt	Holiday Inn	Days Inn	
Orient Express Hotels	Hilton	Holiday Inn Garden Court	Express by Holiday Inn	
Park Hyatt	Hyatt Regency	Howard Johnson	Ibis	
Raffles	Intercontinental	Jolly Classic	Innkeepers Lodge	
Ritz-Carlton	Jolly Master	Novotel	Kyriad	
Rocco Forte Hotels	Le Meridien	Park Inn	Premier Travel Inn	
St Regis	Maritim	Quality Hotels	Sleep Inn	
	Marriott	Ramada	Travelodge	
	Melia	Scandic Hotels	Wetherlodge	
	Millennium	Sol Hotels		
	Radisson	Suite Hotels		
	Renaissance			
	Sheraton			
	Sofitel			
	Swissotel			
	Westin			

Source: Otus & Co

The differences between the market levels are reflected in the different investment at each market level. With other things such as land cost and specific location remaining equal the typical investment per room at each market level is as follows:

Market Level	Investment/Bedroom €
Deluxe	750,000
Up Market	280,000
Mid-Market	175,000
Economy	70,000
Budget	30,000

Source: Otus & Co

Combining hotel configuration and market level provides a more comprehensive view of the pattern of hotel chain provision as follows:

UK Rooms End 2004	Hotel Resort	Full Feature	Basic Feature	Limited Feature	Rooms-Only	Total
Deluxe	55	3,190	260	–	–	3,505
Up Market	5,315	61,910	13,700	75	–	81,000
Mid-Market	500	38,690	34,910	4,890	25	79,015
Economy	–	1,630	15,180	35,720	23,220	75,750
Budget	–	–	300	220	905	1,425
Total	**5,870**	**105,420**	**64,350**	**40,905**	**24,150**	**240,695**

Source: Otus & Co

Over the past 20 years hotel chain room stock in the UK has doubled. In parallel, unaffiliated room stock has declined. We expect this process of consolidation to continue as the chains innovate to meet market demand and capital availability for unaffiliated hoteliers is further constrained. The major trend in portfolio growth during the past 20 years has been in economy and budget, limited feature and rooms-only hotels, which account for 25% of affiliated room stock and which are excluded from the definition of hotel used by the Common Standards. The evolving patterns of demand for hotels and the innovation by the chains to meet that demand is introducing additional combinations of market level and hotel configuration such as mid-market limited feature hotels, which has already begun to emerge and deluxe and up market limited feature hotels, which are planned. If the Common Standards maintain their concept of the hotel the new chain innovations will also be excluded.

The Common Standards focus on hotels and not on brands. They disregard the investment by hotel chains in devising and monitoring their brand specifications and in developing and managing their brand infrastructure to generate target demand. The Common Standards establish each star category as a brand in its own right and they seek to impose these specifications on the chains. Hitherto, the chains have been able to ignore the various classification schemes, but the Common Standards and their background sanctions are designed to insure compliance. As far as hotel chains and their investors are concerned the unsatisfactory concept of the hotel on which The Common Standards is based presents an impediment to adapting to market demand and achieving effective returns.

Customer selection of hotels

The logic of The Common Standards is that a hotel provides a configuration of rooms, restaurant and bar facilities, services and products, which are awarded a star rating. Over the past century the star ratings have been designed to allow potential customers to make assumptions about the hospitality likely to be experienced in any given hotel. The schemes around the world have been the major influence on the perception of hotel supply and the belief that the inherent features of a hotel and thus its classification, is the determinant of customer enjoyment. The higher the rating the greater the prospect of customer enjoyment since the hotel is organised to provide more extensive facilities, services and products. The notion that customers are capable of only one-dimensional choices is clearly not one that applies to the buying of other brands. When buying cars, electrical goods, supermarket own-brand foods, malt whiskies and a host of other brands we daily make far more complex buying decisions based on the perception of brand image, brand values and brand personality. Yet the authors of the Common Standards think that customers can handle only one variable, the star rating, when it comes to hotels. They see customer satisfaction as a function of what the hotel provides to customers. Thus, the hotel classification schemes provide a horoscope for customer enjoyment. The satisfaction that customers can experience is written in the stars!

However, this is not the whole story when it comes to explaining the process by which customers select hotels. There is a choice/sent continuum. At one end is the assumption that customers choose based on the quality of the inherent features of the hotels, represented by their star classification. Hotel classification is solidly fixed at the choice end of the continuum. At the other end customers are sent to hotels. They are the customers who do not have and do not make explicit choices. They include: most conference and meetings customers who stay at the hotel where the event is being held; packaged short and long holiday takers and a proportion of attendees at social functions such as weddings held in hotels. In the UK, these markets account for much of hotel demand in mid-market and up-market hotels and the bulk of the demand of full feature hotels and hotel resorts. They are wholesale markets and are dominated by the chains. The problem with the Common Standards is that they mention conference and meetings facilities, health clubs and retail facilities on only one line in a 49-page document. Almost half of the affiliated room stock in the UK is in hotels with non-room facilities that are ignored by the Common Standards. The implication is that the provision and quality of conference facilities, leisure facilities, retail facilities and casinos do not figure in customer choice of hotel and this is wrong. When it comes to explaining the process by which customers select hotels we have a case of the Common Standards ignoring those features that are important to demand in most hotel brands.

These are not the only areas ignored by the Common Standards. Price does not figure in their evaluation of hotel quality or in their assumptions about the selection of hotels by customers. There are daily examples of four star hotels that achieve higher prices than five star hotels, three star hotels that achieve higher prices than four star hotels and so on due to factors such as location and more effective brand marketing. If the classifiers are right that hotel selection is based on star rating then customers would experience the same enjoyment at similarly rated hotels irrespective of price and this is unrealistic.

As far as hotel chains and their customers are concerned hotel classifiers are the astrologers of the hotel world and their horoscopes are as close to reality as their counterparts in the tabloids.

Paul Slattery, Otus & Co paulslattery@otusco.com
Ian Gamse, Otus & Co iangamse@otusco.com

Irrational exuberance: the trend continues

Simon Allison returns to his theme from the last issue of *Hotel Analyst* about irrational deals

And the trend goes on. A recent report by Jones Lang LaSalle Hotels shows that a record volume of €16.2 billion of single asset and portfolio transactions took place in Europe in 2005 and this year seems set to continue the same broad trend.

On the back of major deals like the Starwood acquisition of the Taittinger portfolio and their joint purchase with Lehman of Meridien's real estate, and of the InterContinental and Whitbread portfolio sales, comes the announcement recently that hotel real estate specialist Hospitality Europe is being bought by Blackstone on a yield rumoured to be around 6%. A further portfolio of InterContinentals in Continental Europe is also stimulating considerable interest.

Apart from the big portfolio sales, trophy deals have been the order of the day in a way not seen for many years – not even in the great boom of 1999-2000. Jones Lang reports six deals in 2005 at more than €600,000 per room – the Savoy, the Intercontinental Paris, the Belfry, the Danieli, the Shelbourne and the Berkeley Court.

The recent sale of the Four Seasons Milan at a price reported to be close to €200 million, or €1.7 million per room, set a new record. With the opportunity funds which acquired the Meridien and Concorde portfolios also likely to sell off some trophies, more eye-popping deals are probably just around the corner.

> Trophy deals have been the order of the day in a way not seen for many years – not even in the great boom of 1999-2000

Looking at these trends, two apparently contradictory patterns appear. On the one hand, the nature of the buyers suggests the prices are actually on the low side; on the other, underlying geo-political and economic trends suggest they are dangerously high.

A close look at the buyers for the portfolios shows an influx of capital from US opportunity funds. The single asset deals are going to local buyers and major institutions like GIC and Bank of Scotland.

This marks a massive change from previous buying sprees. For most of the last 40 years, top prices were paid by whichever group of investors had recently come into money and were spending it like crazy – Middle Eastern buyers on the back of oil money in the 70s, the Japanese in the 80s, newly-formed US private equity funds in the 90s.

Today, the private equity funds are old hands, not starry-eyed trophy-hunters. And, most significantly, all the oil wealth being generated in Russia and the Middle East is simply not arriving in any (visible) quantities in the European hotel market.

> With the exception of the recently-endowed Irish, there is a distinct absence of "typical" trophy buyers

Nor is any of the massive wealth being created in the Chinese industrial boom. With the exception of the recently-endowed Irish, there is a distinct absence of "typical" trophy buyers.

Why is this? The main reason appears to be that both Russian and Arab buyers see better prospects closer to home. The massive growth of the hotel market in Dubai, for example, is now being copied – on a smaller scale – in Qatar, Bahrain and Abu Dhabi.

Post-9/11, many Middle Eastern investors prefer to keep their funds in areas perceived to be friendly, while some also have bitter memories of investments gone wrong in Europe in the past.

If, however, these investment patterns were to change, then a new wall of money could in theory arrive in Europe in the next five to ten years, pushing prices well above today's levels. If, and it's a big if.

The emerging economies have a long way to go and will suck in vast quantities of funds before they're exhausted. And, as I noted in the last edition of Hotel Analyst, not all the European markets look that sexy right now.

It's hard to see much upside in the UK for some time, with taxes and the minimum wage set to go on rising and events of the last few weeks have to throw a question over the European recovery. The French government has capitulated to the "street" without even putting up a significant fight, keeping restrictive French labour laws in place; Italy has produced a tied election which promises yet more stagnation in Europe's most backward economy; business confidence in Germany has fallen back. While the general cyclical recovery will probably continue to produce rising results for hotels in these economies, investors looking for a rebound like that of the 1995-2000 period may be disappointed. Dollar weakness, the probable decline in both domestic and international demand from the UK, Irish, US and Australian economies as their overheated residential property markets cool and the ever-riding trend of commodity prices will all conspire to make an ever-increasing uptick look like a risky bet.

And then there's Iran. Reading the global press, it appears that the world keeps assuming that the problem will simply go away. Well, it could, I suppose. Perhaps the Iranians will eventually agree to fully-fledged UN inspections, they will find no wrongdoing and the crisis will blow over. But I'm not so sure. Let's face it, there's no way that the West is going to allow the Iranian Theocracy to develop a nuclear weapons capability and at some point the proverbial may hit the fan. This will be Not Good for hotels and hotel shares.

> It's hard to see much upside in the UK for some time

Until then, however, we can all keep smiling. The big investment banks and opportunity funds don't often get it all that wrong, and if they're buying top-end properties, there must be some logic to it. And there is. From my vantage point atop one of the world's leading luxury resort companies, I can see a trend that will benefit not only upscale beach hideaways in Asia but also historic trophy hotels across Europe. The Russians and Middle Eastern millionaires may not be buying the hotels to put in their investment portfolios, but they're sure as hell buying them by the night. As a result, the top end of the hotel market is enjoying a gusher, even if everyone else's well is starting to look as if it's drying up.

• Simon Allison is managing director of finance at Six Senses Resorts & Spas and director of HOFTEL, the Hotel Owners Franchisees and Transatlantic League

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The Insider

Immigrants keep UK hotel labour costs in check

Labour costs in the hotel and restaurant sector in the UK dropped by 2.4% during 2005, according to the Bank of England.

The freer labour markets in Britain – one of the few EU countries to allow open access to workers from the 10, mostly East European, accession countries – have helped mitigate the generally rising tide of costs facing hotel operators.

The BoE quotes, in its February 2006 Inflation Report, Government data that shows median pay for the 1.8 million people employed in the hotel and restaurant industry in the UK fell by 2.4%. Overtime pay fell by nearly 20%.

The main factor cited by the Bank for the drop is migrant labour flows, mostly from Eastern Europe, putting downward pressure on pay.

For investors in hotel property, the news is doubly beneficial in that not only does it boost operating profits at the hotel but it also has a macroeconomic impact in keeping wage inflation in check and thus encourages lower interest rates.

Meanwhile other costs have been surging, notably energy. UK gas wholesale prices quadrupled during November, well above the price increases experienced in Continental Europe. And of course the oil price remains high.

One comfort is that hotel and restaurant prices went up 3.4% in the past year compared to a 1.9% rise in general consumer prices.

Hotel IPO pandemic spreads across globe

IPO fever appears to have taken hold of the worldwide hotel industry at present. So far this year, hotel companies have announced float plans in the US, India and Dubai.

And companies in other territories, ranging from the UK to Russia, are thought likely to follow suit.

The latest rumours concern the possibility of Loews Hotels, the hotel operator that is a tiny part of its parent conglomerate.

Loews Corporation played down any prospect of holding an IPO or selling its hotel division. In any case, Loews Hotels is a comparatively small concern, generating $350m of sales and net income of $31.2m last year. The hotel operation represents just 2% of its parent group's total turnover.

The start of such rumours is not surprising in the present atmosphere which is reminiscent of 1996. In that year, six companies listed on the London Stock Exchange alone.

But the current trend is far more geographically spread than a decade ago. Hotel Analyst has reported on the plans by both Kingdom Hotel Investments and IFA Hotels & Resorts in Dubai and by Morgans Hotel Group in the US.

Also flagged have been the ongoing rumours relating to Travelodge, Hyatt and Rezidor.

Other notable IPOs are Royal Orchid Hotels in Mumbai, a chain that operates in Bangalore and Mysore. The company wants to open 15 more properties to take its total to 22.

In South Africa, IFA Hotels & Resorts has completed a reverse takeover of Moribo Leisure listed on the Johannesburg exchange. Moribo currently comprises the Zimbali Lodge operated by Sun International.

And in Russia, upscale property investment group Talion is seeking a Moscow listing which will fund a luxury hotel complex in St Petersburg.

Separately in Russia, the former state run tourist agency Intertourist is planning to build-up a chain of up to 10 hotels over the next three to five years. It will then seek a listing. The company, majority owned by Sistema, took its first step last month by agreeing with Moscow's city council to takeover the Pekin Hotel in a $60m deal.

What this all adds up to is convincing evidence of a remarkable boom in the hospitality industry in most parts of the globe. And it reverses the trend for much of the 10 years since 1996 that has seen a succession of privatisations and delistings.

The tastiest morsels are still to come – across the Atlantic Hyatt is keenly awaited and in Europe both Travelodge and Rezidor will attract considerable attention. It remains to be seen if 2006 can match the excitement of a decade ago.

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