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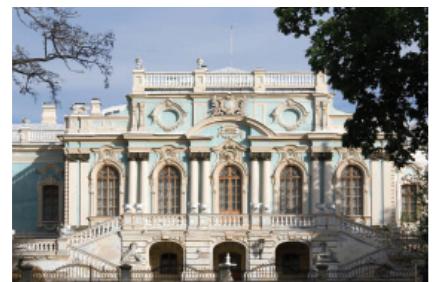
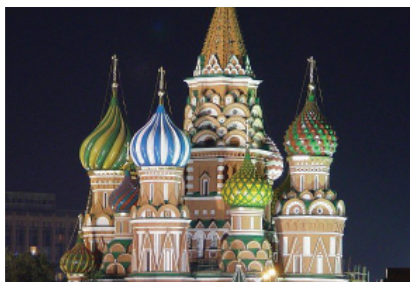
RUSSIA, THE CIS AND GEORGIA TRENDS AND OPPORTUNITIES 2013

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Introduction

Following the success of last year's Trends & Opportunities publication, this year we continue to monitor the main hotel markets in Russia, the CIS and Georgia. This publication analyses the 2012 operational performance of the hotel markets in the region and gives insight into the relationship between the state of local economies and trends in the travel industry. This publication is released to complement our existing Russia, the CIS and Georgia Hotel Valuation Index, which covers hotel value trends in the same markets across the region.

This year, in addition to an overview of operational data, we have included a detailed analysis of payroll trends across the hotel markets, which allows for the comparison of payroll against some of the key operational

figures of hotels. This analysis will allow hospitality professionals to benchmark their payroll data against the industry average and their respective segments (available for Moscow and a countrywide comparison for Russia), as well as assist in following best practices. Additionally, the analysis will compare payroll trends in internationally branded versus local hotels.

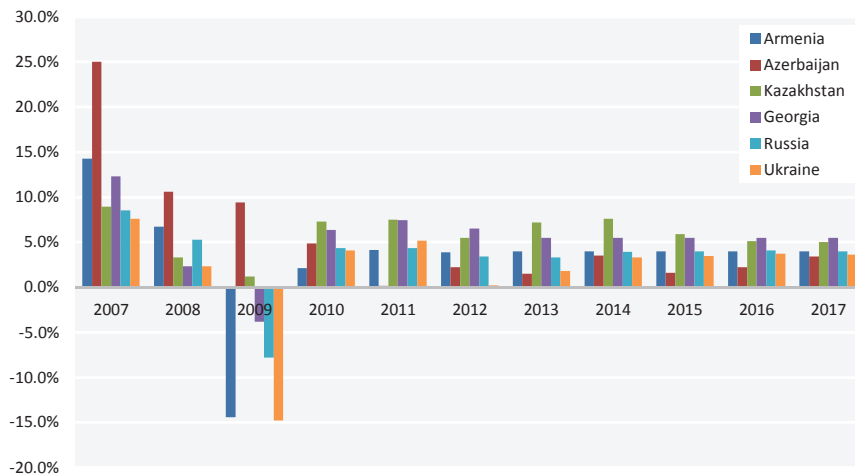
Overview of Local Economies

The general macroeconomic environment and trends have a significant impact on the Travel & Tourism industry. We therefore begin our overview with a few economic indicators across the countries included in this publication.

According to World Bank and Economist Intelligence Unit (EIU) forecasts, the CIS and Georgia are not expected to show any aggressive growth owing to a slight reduction

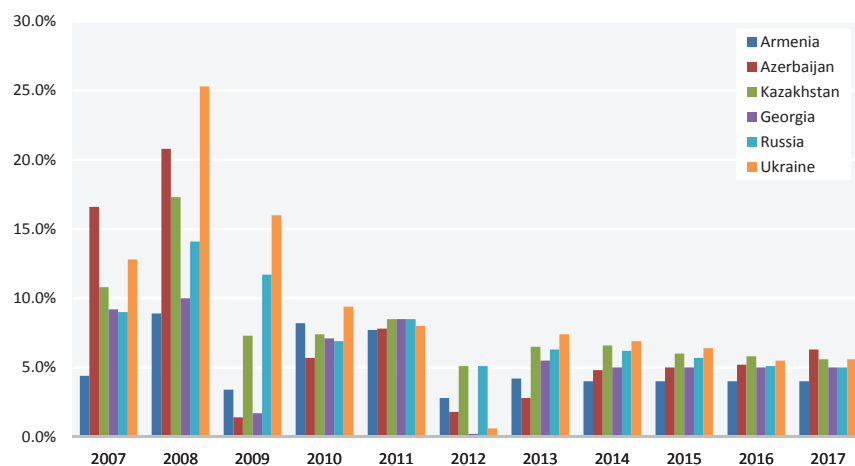
in commodity prices and unstable worldwide economic growth. The average GDP growth in the region from 2011 to 2012 was 3.6%, with Georgia leading the ranks at 6.5% (and Ukraine registering the lowest growth of 0.2%). It should be noted that when comparing the actual GDP figures with the forecast for 2012 at the time of the previous publication, we can see some differences. Four of the six countries achieved a lower GDP growth than was forecast: Armenia and Kazakhstan fell only slightly behind (-0.4 and -0.1 percentage points, respectively), while Azerbaijan registered 1.5 percentage points lower growth in GDP than forecast and Ukraine 2.3 points. Russia and Georgia exceeded the forecast by 0.2 and 1.3 percentage points, respectively. Despite economic growth, these numbers further underline that the local economies are not recovering as fast as originally forecast. Nonetheless, experts from the EIU, the World Bank and Euromonitor maintain a positive outlook for the region, forecasting GDP growth at an average of 4% per annum from 2014 onwards. Owing to

CHART 1: HISTORICAL AND FORECAST GDP GROWTH



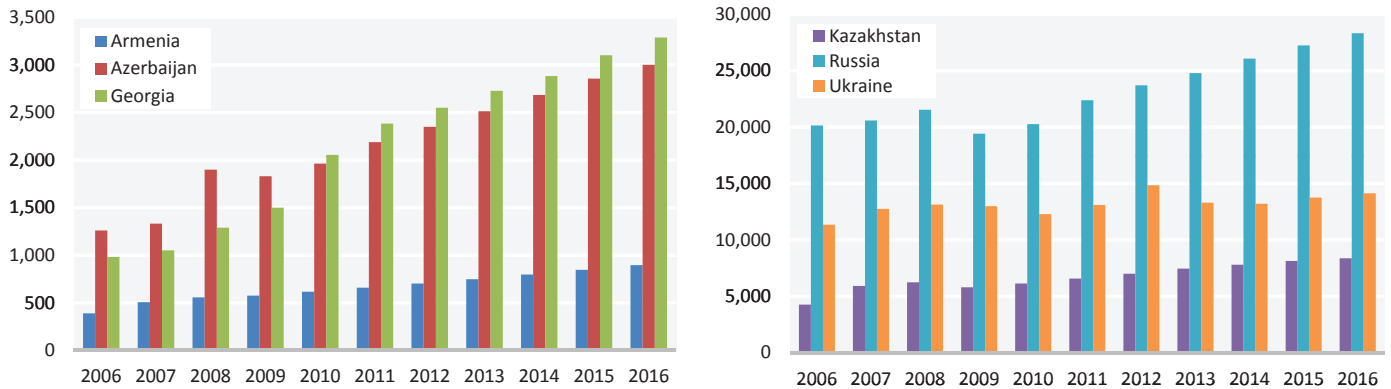
Sources: Economist Intelligence Unit; World Bank 2013

CHART 2: HISTORICAL AND FORECAST INFLATION



Sources: Economist Intelligence Unit; World Bank 2013

CHART 3: HISTORICAL AND FORECAST INTERNATIONAL ARRIVALS (000S)



Source: Euromonitor International

the fact that Russia, the CIS and Georgia are strongly related to the Eurozone, the region remains exposed to the turmoil from the European financial markets.

Chart 2 displays the historical and forecast inflation in the region. It is important to note that inflation in 2012 was the lowest since 2007 (except for Azerbaijan, which exhibited lower inflation in 2009), showing a drastic fall from 2011. In 2011, the average inflation across the region was 8.2%, falling to 2.6% in 2012. This is equivalent to a 68% decrease, with inflation in Georgia and Ukraine falling by 98% and 93%, respectively. All of the countries surveyed registered lower inflation at the end of the year than originally forecast. Nonetheless, the forecast for the region brings inflation back up to an average of 5% a year.

Travel to the Region

Despite expensive air travel and complex visa procedures (in some countries), international arrivals to Russia, the CIS and Georgia grew on average by 10% from 2010 to 2011, and are forecast to grow by 8% in 2012 (Euromonitor releases its Travel & Tourism data at the end of April). The slowdown may partly be a reflection of the extraordinary growth

experienced in 2011 as a result of the recovery in global travel following the dip caused by the worldwide economic crisis.

Since 2006, Georgia has shown the strongest compound annual growth rate for international tourist arrivals (17%); however, we should consider that the base figure in 2006 was relatively low. Russia and Ukraine top the table in absolute numbers (including the forecast increases of 2012) with growth of more than 3.5 million arrivals in six years.

In the medium term, all of the countries are forecast to exhibit growth at a compound annual rate of 5% between 2013 and 2016, with the exception of Ukraine, which is forecast to grow at a compound annual rate of only 2% (partly due to the exceptional increase experienced for the Euro 2012 football championship).

Development of Travel & Tourism

Another indicator of development in the Travel & Tourism sector is the amount of capital invested in the industry as a proportion of overall investment in the country (shown in Chart 4). In percentage terms, the largest investment in the Travel & Tourism industry in

CHART 4: CAPITAL INVESTMENT IN THE TRAVEL & TOURISM INDUSTRY

	By % Contribution to Total Investments 2012	Rank		Growth in 2013	Rank	By % Contribution in 2023	Rank in Terms of Growth over 2013-23
		By % Contribution	By Absolute Contribution				
Armenia	2.7%	154	144	5.9%	57	2.1%	172
Azerbaijan	2.0%	171	108	3.9%	98	2.0%	69
Kazakhstan	5.3%	92	47	9.2%	21	5.4%	25
Russia	2.7%	155	17	0.3%	154	2.5%	51
Ukraine	2.2%	164	73	4.9%	77	1.5%	176
Georgia	3.4%	128	142	7.0%	47	3.3%	88
World average	8.1%			3.9%			

* WTTC ranks out of 184 countries

Source: World Travel & Tourism Council

CHART 5: CONTRIBUTION OF VISITOR EXPORTS TO TOTAL EXPORTS

	Visitor Exports of Total Exports 2012	Rank		Growth in 2013	Rank	By % Contribution in 2023	Rank in Terms of Growth over 2013-23
		By % Contribution	By Absolute Contribution				
Armenia	17.0%	58	123	-1.0%	157	13.2%	183
Azerbaijan	6.6%	101	71	5.7%	48	4.7%	181
Kazakhstan	1.9%	163	78	-6.5%	180	0.8%	182
Russia	3.1%	146	21	7.2%	31	4.9%	64
Ukraine	6.2%	105	50	6.8%	35	5.2%	81
Georgia	19.7%	49	94	5.1%	61	21.0%	63
World average	16.6%			2.8%			

* WTTC ranks out of 184 countries

Source: World Travel & Tourism Council

2012 was made in Kazakhstan, which amounted to 5.3% of the total investment in the country (the world average is 8.1%). The lowest amount in percentage terms of total investment was made in Azerbaijan and totalled 2.0%. Such a low indicator in Azerbaijan can be partly explained by the fact that a lot of the major investments in the Travel & Tourism industry in Azerbaijan were made in the run up to the hosting of the Eurovision Song Contest, which was held in 2012.

It is worth mentioning that Russia is the only BRIC country that is not in the top ten of the capital investment list for Travel & Tourism in absolute terms, and neither is it forecast to be ranked in the top ten in the next ten years. The highest investment witnessed in the Travel & Tourism industry in 2012 is in the USA (in absolute terms) and it is forecast that China will reach the top rank by 2023.

Kazakhstan, which topped our table in 2012, is forecast to continue increasing investment in the Travel & Tourism sector with a growth rate for 2013 of 9.2%, followed by Georgia with 7.0% growth. In the long term, Kazakhstan will keep its leading position in terms of growth of investment, increasing on average by 6.5% a year, followed by Russia with projected growth of 5.7% over the next ten years. The lowest increase is expected in Ukraine (1.4%), which will lead to a reduction of the tourism investment portion of total investment in the country to only 1.5% (the highest drop among the listed countries by 2023). Kazakhstan

is the only country forecast to increase its share of Travel & Tourism in overall investment (an increase of 0.1 percentage points).

From these data and forecasts, we can conclude that investment in the Travel & Tourism industry in the reviewed countries is not expected to surpass the pace of other investments as their proportion of total investment is expected to drop over the next ten years (with Kazakhstan the only exception, as already mentioned).

The World Travel & Tourism Council (WTTC) tracks visitor exports, which is spending within the country by international tourists for both business and leisure trips, including spending on transport. If we look at the visitor exports contribution and its growth as a portion of total exports in the reviewed countries over the forecast period, as shown in Chart 5, it can be noted that in Georgia visitor exports amounted to 19.7% of total exports in 2012, compared to 1.9% in Kazakhstan and 3.1% in Russia. In absolute terms, however, Russia is leading the region and is 21st worldwide. In 2013, the highest growth is expected to be witnessed in Russia and Ukraine, followed by Azerbaijan; however, in the long term, visitor exports are expected to decrease in all countries except for Georgia (up 1.3 points) and Russia (up 0.1 point).

Analysing the statistical data and forecasts discussed above, it can be noted that along with the recovery of the region after the economic

CHART 6: CONTRIBUTION OF TRAVEL AND TOURISM TO EMPLOYMENT

	Employment Direct Contribution	Rank		Growth in 2013	Rank	Growth by 2023	Rank
		By % Contribution	By Absolute Contribution				
Armenia	1.9%	153	142	0.8%	182	-1.7%	182
Azerbaijan	2.0%	148	92	6.9%	166	0.4%	166
Kazakhstan	1.5%	167	73	0.2%	174	-0.2%	174
Russia	1.4%	172	17	4.4%	163	0.6%	163
Ukraine	1.9%	151	35	5.8%	175	-0.5%	175
Georgia	4.0%	77	100	1.5%	160	0.6%	160
World average	5.4%			1.3%		2.0%	

* WTTC ranks out of 184 countries

Source: World Travel & Tourism Council

downturn, the Travel & Tourism industry is showing positive growth. However, the development of the industry is expected to fall behind other industries in the region, as shown by forecast decreases in investment and visitor exports.

According to the International Monetary Fund (IMF), unemployment rates in the reviewed countries for 2012 range from 5% to 7% and have been steadily declining over the past two to three years. The only exception is Georgia, where unemployment rates have been estimated at 15%, which is the highest in the region. Moderate unemployment rates in five of the six observed economies are a good indicator of the economic stability, especially at times of continuing worldwide economic turmoil. However, in the context of payroll trends (reviewed later in this publication), it should be noted that, according to the World Bank, Armenia, Georgia and Ukraine have been ranked in the 'lower middle income' category with a gross national income per capita in the range of US\$1,026 to US\$4,035 a year. Azerbaijan, Kazakhstan and Russia on the other hand are in the 'upper middle income' category with gross national annual income per capita in the range of US\$4,036 to US\$12,475.

According to the WTTC, Travel & Tourism directly supported 1,655,500 jobs in Armenia, Azerbaijan, Georgia, Kazakhstan, Russia and Ukraine combined. Direct contribution of the tourism industry to the total employment of each country in particular ranged from 1.4% in Russia to 4.0% in Georgia (5.4% worldwide). As discussed in our Russia, the CIS and Georgia Hotel Valuation Index 2012, the Georgian government has put considerable efforts into developing tourism in recent years (measures such as the cancellation of visas for EU, US, CIS and Canadian citizens), and as a result the Travel & Tourism industry has contributed more to Georgia's employment than the other countries in the region. The highest forecast increase in employment contribution for 2013 is for Azerbaijan and represents a 6.9% increase on 2012. In the long term, Azerbaijan, Georgia and Russia are forecast to increase their Travel & Tourism contribution to overall employment. Armenia, Kazakhstan and Ukraine are

forecast to decrease their contributions by 1.7%, 0.2% and 0.5%, respectively.

Industry Performance

In 2012, hotel markets in the CIS and Georgia continued to exhibit signs of recovery in levels of demand, with most of the markets registering a positive increase in marketwide occupancies. Yekaterinburg (22%), Tbilisi (12%) and Kazan (10%) observed double-figure increases in occupancies, while the remaining markets with positive growth only registered an average increase of 4.3%. This increase is quite different to what was registered in 2011 (when all markets exhibited increases in occupancy); however, it should be noted that part of the growth in 2011 was attributed to recovery from the global economic crisis. From all the markets which registered an increase in occupancy, only Moscow, St Petersburg, Almaty and Samara had new hotels opening throughout the year. Kiev (-13.3%) and Baku (-12.7%) were the only two markets to show decreases in occupancy levels, which can be partly attributed to the significant number of new hotels entering the market during the year. In 2012, Kiev and Baku showed increases in supply of 24% and 44%, respectively, which led to concurrent decreases in occupancy. Looking back at the past six years, Moscow and Rostov continue to be the least volatile markets in terms of occupancy with compound annual growth rates of 1.3% and 0.6%, respectively. Moscow's stability is expected, as it is the main business and commercial destination of the region, which means the city is less dependent on seasonality and travel continues even in times of economic unrest. Rostov, on the other hand, can be described as a 'wait and see' market. Supply has been stable and so has demand; however, the future pipeline in the city is very aggressive and will almost certainly put considerable strain on operating performances once all of the announced hotels are operational. Kazan and Yerevan continue to be the only two markets (in addition

CHART 7: KEY OPERATING CHARACTERISTICS BY MAJOR CITY – OCCUPANCY

	2007	2008	2009	2010	2011	2012	% Growth 2012	Compound Annual Growth 2007-12
Moscow	65.4%	65.0%	62.6%	67.1%	68.4%	69.7%	1.9%	1.3%
St Petersburg	64.4%	60.2%	44.4%	52.7%	55.8%	58.1%	4.1%	-2.0%
Yekaterinburg	55.4%	55.5%	31.0%	30.0%	38.4%	46.9%	22.1%	-3.3%
Rostov	59.7%	57.8%	53.8%	56.7%	60.3%	61.5%	2.0%	0.6%
Samara	56.8%	52.7%	36.3%	44.5%	49.6%	53.9%	8.7%	-1.0%
Kazan	41.8%	49.3%	49.1%	45.0%	51.0%	56.3%	10.4%	6.1%
Kiev	64.5%	63.6%	46.6%	47.5%	51.7%	44.8%	-13.3%	-7.0%
Baku	64.4%	59.6%	46.6%	43.8%	51.0%	44.5%	-12.7%	-7.1%
Astana	58.0%	49.3%	40.6%	44.1%	47.4%	48.2%	1.7%	-3.6%
Almaty	72.0%	60.0%	50.0%	42.0%	46.4%	49.4%	6.5%	-7.3%
Tbilisi	75.5%	70.5%	46.4%	50.1%	61.6%	68.9%	11.9%	-1.8%
Yerevan	48.3%	45.9%	49.9%	49.4%	51.6%	54.3%	5.2%	2.4%

Source: HVS Research

CHART 8: KEY OPERATING CHARACTERISTICS BY MAJOR CITY – AVERAGE RATE (€)

	2007	2008	2009	2010	2011	2012	% Growth 2012	Compound Annual Growth 2007-12
Moscow	254	266	170	161	171	171	0.2%	-7.6%
St Petersburg	119	136	108	94	102	97	-4.9%	-4.0%
Yekaterinburg	70	75	97	97	105	93	-11.4%	5.8%
Rostov	61	72	55	56	60	61	0.8%	-0.2%
Samara	99	102	80	81	85	78	-8.8%	-4.8%
Kazan	91	88	85	71	73	80	9.8%	-2.5%
Kiev	198	195	157	151	149	151	1.6%	-5.2%
Baku	165	158	171	155	134	135	0.4%	-4.0%
Astana	170	180	197	193	203	200	-1.5%	3.3%
Almaty	270	290	220	218	218	200	-8.3%	-5.8%
Tbilisi	124	127	126	115	100	109	9.0%	-2.5%
Yerevan	105	95	75	78	82	86	4.9%	-3.9%

Source: HVS Research

CHART 9: KEY OPERATING CHARACTERISTICS BY MAJOR CITY – REVPAR (€)

	2007	2008	2009	2010	2011	2012	% Growth 2012	Compound Annual Growth 2007-12
Moscow	166	173	106	108	117	119	2.1%	-6.4%
St Petersburg	77	82	48	50	57	56	-1.0%	-6.0%
Yekaterinburg	39	42	30	29	40	44	8.2%	2.4%
Rostov	36	42	30	32	36	37	2.8%	0.4%
Samara	56	54	29	36	42	42	-0.9%	-5.8%
Kazan	38	43	42	32	37	45	21.3%	3.5%
Kiev	128	124	73	72	77	68	-11.9%	-11.9%
Baku	106	94	80	68	68	60	-12.4%	-10.8%
Astana	99	89	80	85	96	96	0.2%	-0.5%
Almaty	194	174	110	92	101	99	-2.3%	-12.7%
Tbilisi	94	90	58	58	62	75	21.9%	-4.3%
Yerevan	51	44	37	39	42	47	10.4%	-1.6%

Source: HVS Research

to Moscow and Rostov) which register a positive compound annual growth rate over the past six years.

In terms of average rates (in euro), seven of the 12 markets registered a positive increase in 2012. It was expected that in 2012 guests would become more price sensitive, therefore average rates were severely under pressure and any new supply had a visible impact. (It is important to note that in 2012 we have expanded the list of participants in this publication, many of which were in lower price segments, thus artificially decreasing the average rates from 2011.) Despite the range of average rate increases from 0.2% (Moscow) to 9.8% (Kazan), the average increase (among positive growth markets) was only 3.8% versus 5.4% in 2011. The average rate change in euro terms for Moscow was insignificant, therefore in the table we see that the rounded number hasn't changed, despite 0.2% growth from 2011. Yekaterinburg (-11.4%) registered the highest drop in average

rates, but this can be partly explained by the highest occupancy growth in the region (22.1%) – the city's room stock has been completely overdeveloped, and thus price wars come as no surprise as the hotels struggle to survive. Samara (-8.8%) and Almaty (-8.3%) became good examples of cities that lost average rate owing to new hotels opening (especially given the markets' fairly limited existing supply) as well as continuing pressure on rates from price-sensitive clientele. When reviewing the average rates in local currency, we can see that the drop in the euro against the rouble, for example, meant that even a decrease in average rate in local currency (such as -2.2% in Moscow) was still positive growth in euro terms (0.2%). With the weakening of the euro in 2012 (owing to continued European financial turmoil) in relation to all of the local currencies reviewed, half of the markets which registered decreases in local currency reported an increase in euro terms. Over the past six years, however, most of the local currencies weakened against the euro,

CHART 10: KEY OPERATING CHARACTERISTICS BY MAJOR CITY – AVERAGE RATE (LOCAL CURRENCY)

	2007	2008	2009	2010	2011	2012	% Growth 2012	Compound Annual Growth 2007-12
Moscow	8,890	9,709	7,548	6,488	6,977	6,821	-2.2%	-5.2%
St Petersburg	4,165	4,964	4,795	3,788	4,162	3,861	-7.2%	-1.5%
Yekaterinburg	2,450	2,738	4,307	3,909	4,284	3,701	-13.6%	8.6%
Rostov	2,135	2,628	2,442	2,257	2,448	2,408	-1.6%	2.4%
Samara	3,465	3,723	3,552	3,264	3,468	3,085	-11.1%	-2.3%
Kazan	3,185	3,212	3,774	2,861	2,978	3,192	7.2%	0.0%
Kiev	1,426	2,126	1,774	1,590	1,636	1,552	-5.1%	1.7%
Baku	203	177	197	166	150	136	-9.5%	-7.7%
Astana	29,240	30,348	41,370	37,755	40,864	37,760	-7.6%	5.2%
Almaty	46,440	48,894	46,200	42,645	43,883	37,760	-14.0%	-4.1%
Tbilisi	317	295	305	266	235	231	-1.7%	-6.2%
Yerevan	46,284	40,983	40,418	36,878	42,476	44,385	4.5%	-0.8%

Source: HVS Research

CHART 11: KEY OPERATING CHARACTERISTICS BY MAJOR CITY – REVPAR (LOCAL CURRENCY)

	2007	2008	2009	2010	2011	2012	% Growth 2012	Compound Annual Growth 2007-12
Moscow	5,814	6,311	4,725	4,354	4,772	4,754	-0.4%	-3.9%
St Petersburg	2,682	2,988	2,129	1,996	2,322	2,243	-3.4%	-3.5%
Yekaterinburg	1,357	1,519	1,335	1,173	1,645	1,736	5.5%	5.0%
Rostov	1,275	1,519	1,314	1,280	1,476	1,481	0.3%	3.0%
Samara	1,968	1,962	1,289	1,453	1,720	1,663	-3.3%	-3.3%
Kazan	1,331	1,584	1,853	1,288	1,519	1,797	18.3%	6.2%
Kiev	920	1,352	827	755	846	695	-17.8%	-5.4%
Baku	131	105	92	73	77	60	-21.1%	-14.3%
Astana	16,959	14,962	16,796	16,650	19,369	18,200	-6.0%	1.4%
Almaty	33,437	29,336	23,100	17,911	20,362	18,653	-8.4%	-11.0%
Tbilisi	240	208	141	133	145	159	10.0%	-7.9%
Yerevan	22,355	18,811	20,168	18,218	21,918	24,101	10.0%	1.5%

Source: HVS Research

meaning that the average rate decrease since 2006 was observed in more markets when converting to euro than originally reported in local currencies. Baku is the only exception, where a stronger local currency means that a 7.7% compound annual decrease in average rate over the past six years in local currency, turned into a 4% decline in euro terms. Nonetheless, the overall message from 2012 is that rates are under pressure and will decrease at any sign of new competition or declining economic conditions.

RevPAR performance in euro terms was positive for seven markets, with Tbilisi (21.9%) and Kazan (21.3%) topping the table. Yerevan (10.4%) was the only other city to register a double-figure increase in RevPAR. Growth in these markets was backed by both occupancy and average rate increases and partly aided by currency fluctuations. Yekaterinburg, despite a heavy drop in average rate, still registered a positive (8.2%) increase in RevPAR. As expected,

Baku (-12.4%) and Kiev (-11.9%) exhibited the largest decreases in RevPAR in euro terms. It should be noted that Samara and Astana show the same RevPAR values in 2011 and 2012, while exhibiting a small percentage change. This is due to an insignificant change and the rounding of the figures in the table. In local currency, five markets showed positive increases in RevPAR. Kazan (+18.3%) tops the table ahead of Tbilisi (+10.0%) as the Georgian lari strengthened more against the euro than the Russian rouble did. It is important to note that in euro terms the RevPAR performance over the past six years continues to be negative for nine of the 12 markets (this figure was seven in local currency terms). In 2012, RevPAR growth or decline was mostly dictated by fluctuations in average rates, as we have seen occupancy increase in most markets (except Baku and Kiev). Since RevPAR is the most accurate measure of hotel revenues, it is important to understand that increased occupancy does not always guarantee RevPAR growth.

CHART 12: DISTRIBUTION OF EXISTING AND PROPOSED BRANDED HOTEL ROOMS BY MAJOR CITY

	Existing Supply 2011	Existing Supply 2012	Proposed Supply 2013-18	Rank	New Supply as a % of Total for the 13 Markets	Increase over Five Years	Rank
Moscow	13,000	13,484	6,413	1	37%	48%	7
St Petersburg	6,800	6,908	1,259	3	7%	18%	13
Yekaterinburg	800	800	155	13	1%	19%	12
Rostov	100	100	1,179	4	7%	1,179%	1
Samara	670	874	195	12	1%	22%	11
Kazan	780	780	540	8	3%	69%	4
Sochi	800	1,609	3,791	2	22%	236%	2
Kiev	1,800	2,222	803	7	5%	36%	9
Baku	1,350	1,940	912	6	5%	47%	8
Astana	700	700	960	5	6%	137%	3
Almaty	1,400	1,596	363	10	2%	23%	10
Tbilisi	830	830	400	9	2%	48%	5
Yerevan	450	450	216	11	1%	48%	6
Total	29,480	32,293	17,186			53%	

Source: HVS Research

Hotel Supply

Despite economic turmoil in the region and continued crisis in the Eurozone, hotel development continued in 2012.

Hotel supply in the region continued to grow in 2012 and has increased by 10%, with most of the new hotels (65%) opening in Kiev, Baku and Sochi. The number of proposed projects in the 12 surveyed markets (plus Sochi) is forecast to increase supply by approximately 50% in the medium term. This figure is lower than last year (70%) as hotel openings in these markets outpaced newly announced developments. Moscow continues to dominate the future pipeline with almost 40% of future supply. Kiev opened much of its announced room stock in time for the Euro 2012 football championship, and we can see that its share in the proposed pipeline for the region has decreased to 5% (from 11% in 2011). Sochi continues to be ranked second behind Moscow in terms of future hotel openings, owing to the fact that not all the hotels planned for the 2014 Winter Olympics have opened. Rostov has the fourth-largest potential pipeline; however, it is the largest increase in percentage terms as the city has the lowest base of international quality accommodation. Such a large increase in hotel stock in a city is bound to put immense pressure on the operating performance of all hotels in that market. Yekaterinburg and Samara have the lowest proposed pipeline from all the reviewed markets.

Chart 13 summarises the distribution of hotel rooms by brand. It is important to note that while this publication concentrates on 12 key markets in Russia, the CIS and Georgia, Chart 13 addresses the total supply of these brands in the greater

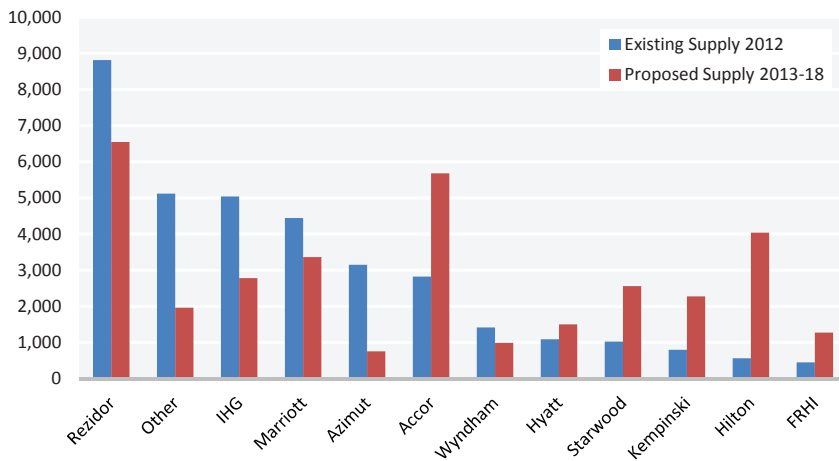
region. In this year's publication, the sample of hotels was expanded to include local brands.

Rezidor continues to dominate the region in terms of existing hotels with 26% of the surveyed room stock. Compared to 2011, Rezidor has increased its presence by almost 20%, whereas Marriott (second place in terms of growth) increased its room stock by 18%, albeit from a smaller base. InterContinental Hotels Group (IHG) remains the second-largest hotel operator in the region with more than 5,000 rooms in operation in 2012. Marriott and Accor are the only other international operators to boast more than 2,000 rooms in the region. Azimut is the only local operator to get in the top five brands by room stock, with more than 3,000 rooms. Wyndham, Hyatt and Starwood have more than 1,000 rooms each in the region as of 2012.

When looking at the proposed pipeline of hotels, Rezidor continues to be at the top with almost 20% of all proposed hotels in the region. Accor, Hilton and Marriott remain in the same places as 2011 and, together with Rezidor, represent almost 60% of all proposed hotels in Russia, the CIS and Georgia. IHG, Starwood and Kempinski follow with proposed hotel stock of more than 2,000 rooms each. The total proposed room stock for the region in the medium term is almost equal to the existing one. This means that if all the projects are realised, the existing hotel market capacity of international quality accommodation for the entire region will almost double in the next few years.

Despite certain setbacks in hotel development, many markets are again becoming attractive to investors. Such interest is mirrored in the increased announced supply in Russia, the CIS and Georgia.

CHART 13: DISTRIBUTION OF EXISTING AND PROPOSED BRANDED HOTEL ROOMS BY HOTEL OPERATOR – RUSSIA, THE CIS AND GEORGIA



Source: HVS Research

Future Trends

Our analysis of hotel markets in Russia, the CIS and Georgia shows that the recovery process from the 2008/09 crisis is not complete. As we have seen in 2012, many hotel markets have become extremely price sensitive and any new developments can easily decrease rates in the market. Taking into account the sizeable proposed pipelines, we estimate that hotel markets will continue to remain price sensitive and operators will have to adapt to increasing competition. Even though we consider that in the long term hotel performance will improve, short- to medium-term pressure on operating performance will exist as a result of increasing hotel stock.

As witnessed in 2012, the value of the euro dropped in relation to all of the local currencies, which meant that operating performance in euro terms increased. As many brands report their operating results in either euro or US dollars, any potential future currency fluctuation can impact the reported figures.

As the Sochi Winter Olympics are just around the corner, hotel development has turned elsewhere. With the announcement that the FIFA World Cup is to be held in Russia in 2018, hoteliers are starting to pay closer attention to the host cities. More than 60% of the total required room supply is supposed to be positioned in the three-star segment, and thus the majority of the construction/renovation projects that are expected to be completed in the coming years in the listed host cities are targeted at boosting midscale room supply. Even though the total number of existing rooms in the host cities corresponds to the

minimum requirements, most the room stock is worn out, outdated products from the Soviet era. An estimated 19,000 rooms are expected to be built or refurbished by 2018 to meet FIFA's minimum requirements.

In the last publication, we talked about the lack of institutional investors in the region. We can't say that anything major has happened in one year; however, another large-scale development deal has been announced: the development of Holiday Inn Express hotels by Regional Hotel Chain. As local hotel markets continue to mature, we should see more of these large-scale deals taking place.

Opportunities

Last year we talked about the opportunity for the development of midmarket and budget hotels and we still consider this to be the key opportunity in hotel development in the region. As hotel markets become more price sensitive, the high-cost operations of luxury hotels will become harder to sustain. That is not to say that in the right location a luxury development will not be successful, but across the whole region, where the average rate potential of many markets is limited (often lower than desired by luxury hotel operators), midmarket and budget hotels will prosper. This is partially backed by the announcement of large-scale deals in recent years, which have all taken place in the midmarket and budget segments.

As mentioned above, the region is characterised by many dated assets, which are currently underperforming owing to their economic obsolescence. An opportunity exists for investors to purchase these assets and renovate them into international quality hotels. This will be faster than developing a new hotel and often cheaper. Hotel brands, on the other hand, should encourage conversion as this will allow them to expand faster in the region.

The past 18 months have witnessed some high-profile hotel transactions, albeit all in the upscale and luxury segments. As hotel markets mature and more hotels become operational, opportunities to purchase operational assets will become more common.

Additional Factors – Payroll Trends

The hotel business is people serving other people. Owners and operators are always keen to employ the best human capital for their assets. In last year’s publication we reviewed compensation trends alone. This year we would like to analyse the relationship between payroll and revenue, because employing expensive and highly qualified personnel is only as good as the revenues they generate.

Russia Comparison

Chart 14 presents an overview of the main trends in Russia. We can see from the chart that Moscow exhibits the lowest percentage of payroll to total revenue at 23.2%. This trend is not surprising, as hotel revenues in Moscow (€71,737) are significantly higher than the country average (€54,327). When compared to the regional cities, Moscow’s revenue per employee is more than double. Rooms payroll as a percentage of rooms revenue in Moscow is more than 3% lower than in the Russian regions, further underlying the effect of high average rates in the city. St Petersburg, on the other hand, is less than one percentage point higher than Moscow at 7.6%. F&B payroll follows a similar pattern for Moscow and St Petersburg; however, when comparing the regional cities to St Petersburg, the latter exhibits a higher percentage of F&B payroll. This may occur for a number of reasons: St Petersburg has a diverse offering of restaurants, which means that employers have to pay higher salaries to keep their staff and might also get lower revenues; on the other hand, the less competitive restaurant industry of the regional cities means that more customers will choose hotel F&B outlets, thus increasing revenues. Conversely, Moscow’s high salaries and the presence of luxury hotels in the sample are once again outweighed by the higher revenues. The number of rooms department employees per room is fairly constant across all markets at close to 0.2.

When compared to the seemingly similar developing market of India, a few interesting trends emerge. As you can see from Chart 15, payroll as a percentage of total revenues is about 25% higher in Russia vs. India. At the same time, in the rooms department the figures are similar, while F&B

CHART 14: RUSSIA COMPARISON

	Moscow	St Petersburg	Russian Regions	All Russia
Payroll as % of Total Revenue	23.2%	26.7%	31.1%	25.1%
Annual Revenue per Employee (€)	71,737	47,469	30,067	54,327
Annual Payroll per Employee (€)	16,660	12,669	9,336	13,635
Annual Payroll per Occupied Room (€)	62	52	44	52
Annual Payroll per Available Room (€)	44	21	22	31
Rooms Payroll as % of Rooms Revenue	6.8%	7.6%	9.8%	7.8%
F&B Payroll as % of F&B Revenue	20.1%	29.3%	23.9%	23.7%
Employees per Room	0.96	0.61	0.86	0.85
Rooms Employees per Room	0.21	0.19	0.22	0.21

Source: HVS Research

CHART 15: RUSSIA VS INDIA

	All Russia	All India
Payroll as % of Total Revenue	25.1%	20.3%
Rooms Payroll as % of Rooms Revenue	7.8%	7.7%
F&B Payroll as % of F&B Revenue	23.7%	16.7%
Employees per Room	0.85	1.96

Source: HVS Research

shows about a 40% difference. And, of course, India’s head count per room is about twice that of Russia’s.

We derive a few facts from this: Indian labour is cheaper, so employers in hospitality can afford the luxury of having twice as many staff as Russia’s hoteliers while maintaining a relatively low payroll cost. Less efficiency is realised in F&B in India as compared to the rooms department, just like everywhere. Although Indian hoteliers could probably save on labour and achieve a higher bottom line, there’s a cultural factor at play here: India is a highly service-oriented culture, and having lots of staff on hand is normal. When dining out, guests in India expect a lot of attention and personalised service, and Indian hoteliers are serious about satisfying all of their customers’ needs.

Segment Comparison

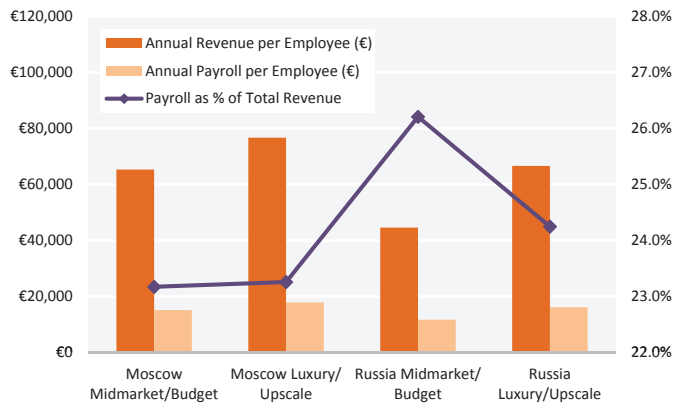
When comparing hotels across segments, we see that the payroll per employee in Moscow’s Luxury/Upscale segment is almost 20% higher than the Midmarket/Budget segment. Across Russia, the difference is almost double at approximately 40%. If we explore the relationship between revenue per employee, we can see a similar difference (almost 20%) in

CHART 16: LUXURY/UPSCALE VS MIDMARKET/BUDGET

	Moscow Midmarket/Budget	Moscow Luxury/ Upscale	Russia Midmarket/Budget	Russia Luxury/ Upscale
Payroll as % of Total Revenue	23.2%	23.3%	26.2%	24.2%
Annual Revenue per Employee (€)	65,353	76,732	44,629	66,636
Annual Payroll per Employee (€)	15,144	17,846	11,697	16,158
Annual Payroll per Occupied Room (€)	46	80	40	73
Annual Payroll per Available Room (€)	33	57	24	45
Rooms Payroll as % of Rooms Revenue	6.2%	7.2%	7.9%	7.9%
F&B Payroll as % of F&B Revenue	22.4%	22.8%	23.1%	24.4%
Employees per Room	0.79	1.16	0.73	1.01
Rooms Employees per Room	0.15	0.29	0.18	0.26

Source: HVS Research

CHART 17: PAYROLL COST VS REVENUE



Source: HVS Research

Moscow. Across Russia, however, the revenue per employee is almost 50% higher in the Luxury/Upscale segment, which means that the payroll as a percentage of total revenue is also the highest in that segment (26.2%).

If we compare rooms payroll as a percentage of rooms revenue, we see that the Midmarket/Budget segment of Moscow records the lowest percentage (6.2%), which further underlines the fact that Moscow commands high average rates. As a result, operational expenses are lower in percentage terms (even if the absolute figure is higher). Luxury/Upscale hotels have on average 40-50% more employees per room, when compared to the Midmarket/Budget segment. If we narrow this down to just rooms department employees per room, we see that Luxury/Upscale hotels can employ almost twice as many employees per room as hotels in the Midmarket/Budget segment. Chart 17 depicts the relationship between the annual payroll and revenue per employee and the resulting percentage of total revenue that payroll represents.

International vs. Local Brands

As local operators increase their presence in the market and become more competitive with their international counterparts, it is important to understand the payroll trends in international vs. local hotels.

CHART 18: INTERNATIONAL VS LOCAL BRANDS

	Russia International Brands	Russia Local Brands
Payroll as % of Total Revenue	23.1%	31.4%
Annual Revenue per Employee (€)	67,304	33,987
Annual Payroll per Employee (€)	15,537	10,675
Annual Payroll per Occupied Room (€)	58	42
Annual Payroll per Available Room (€)	37	23
Rooms Payroll as % of Rooms Revenue	7.5%	9.1%
F&B Payroll as % of F&B Revenue	23.5%	24.8%
Employees per Room	0.87	0.78
Rooms Employees per Room	0.21	0.20

Source: HVS Research

As we see from Chart 18, annual payroll per employee in international hotels is almost 50% higher; however, the significant difference in revenues per employee (almost twice as high in international hotels) means that in percentage terms international operators spend 27% less on payroll from the total revenue. F&B payroll is similar across brands; however, in the rooms department international hotels are more effective, spending 7.5% vs. 9.1% on staff. As shown in Chart 19, international brands employ more employees per room (around 12% more); however, in the rooms division the figures are similar at 0.2 employees per room.

CHART 19: EMPLOYEES PER ROOM



Source: HVS Research

Conclusion

In today's highly competitive market the only diversifier and determining factor for success is the staff you employ. However, it is important to realise that if payroll is high, revenues should match this in order to justify the expensive personnel.

Benchmarking your hotel's operational performance and payroll figures against the market will let hoteliers better understand their returns on human capital.

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About HVS

HVS is the world's leading consulting and services organisation focused on the hotel, restaurant, shared ownership, gaming, and leisure industries. Established in 1980, the company performs more than 2,000 assignments per year and clients include virtually every major industry participant. HVS principals are regarded as the leading professionals in their respective regions of the globe. Through a worldwide network of 31 offices staffed by more than 300 seasoned industry professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. For further information regarding our expertise and specifics about our services, please visit www.hvs.com.

With an office in Moscow since 2007, HVS Moscow serves clients with interests in Russia and the CIS. HVS has appraised almost 4,000 hotels or projects in 50 countries in all major markets within the EMEA region for leading hotel companies, hotel owners and developers, investment groups and banks. Known as one of the foremost providers of hotel valuations and feasibility studies, and for our ability, experience and relationships throughout Russia and the CIS, HVS Moscow is on the valuation panels of numerous top international banks which finance hotels and portfolios.

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