Dubai, United Arab Emirates – Market Snapshot

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November 2009

Dubai, United Arab Emirates – Market Snapshot

This market snapshot is the fifth in a series of articles that HVS will be producing every month on a series of key markets. In writing these articles we aim to combine the market expertise of HVS with STR Global data for each key market. Our analysis for this market is based on a sample of more than 25,800 rooms, as provided by STR Global. We consider that in today's challenging environment a regular update is more vital than ever in helping to assess the challenging market conditions and determine the best strategy for each hotel.

Highlights:

- According to the ACI World Traffic Report 2008, Dubai International Airport ranked twentieth worldwide and first in the Middle East in terms of passenger traffic with 37,441,440 passengers. Year-to-September 2009 exceeded the 30 million threshold, with double-digit growth year-on-year (YOY) for May up to and including September. This can be attributable in part to the introduction of flydubai, emirates low cost airline, as well as an increase in the number of routes served by Emirates Airlines.
- As a result of the global economic downturn, year-end occupancy dropped from 82.1% in 2007 to 76.9% in 2008. Nonetheless, Dubai was able to achieve an average rate increase of 8.0% that year. However, dwindling occupancy during 2009 exacerbated great pressure on average rate which, in August, reached almost half what it was at the beginning of 2009;
- The first half of 2008 saw an increase in supply of 4,032 hotel rooms whereas the second half of the year witnessed an increase of only 612 hotel rooms. However, the first half of 2009 witnessed an increase in supply of 17.1% on the first half of 2008.

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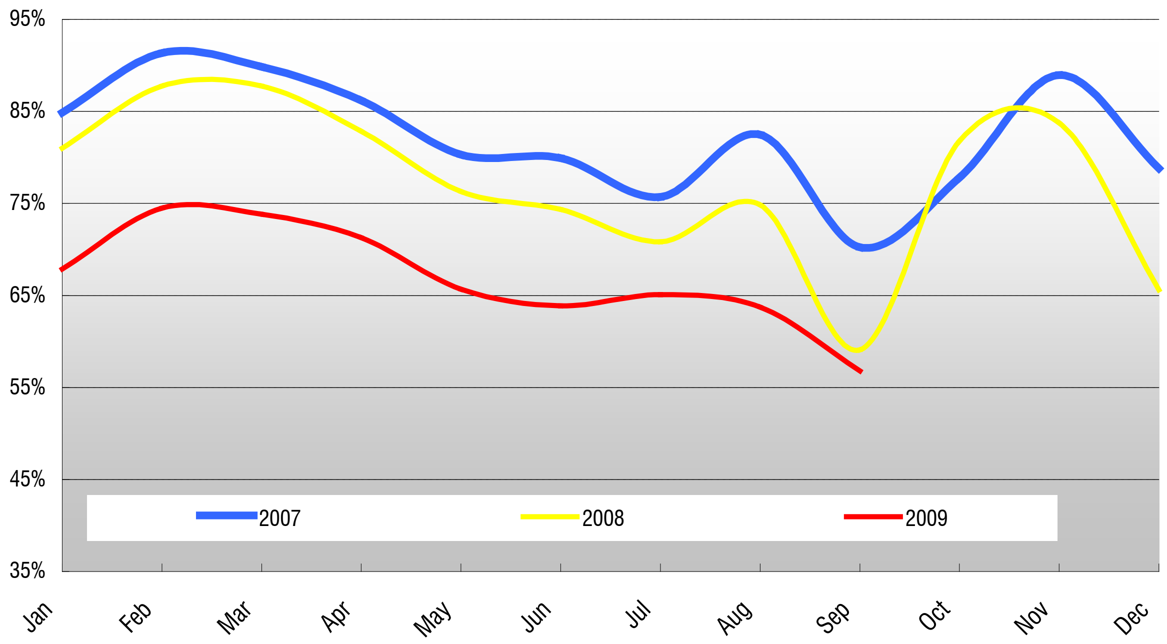
Hotel Demand Patterns

- Passenger arrivals increased at a CAGR of 16.0% over the last decade, and Dubai International Airport is still witnessing aggressive growth a every month through 2009;
- The number of hotel guests has been on the rise, marking an annual increase of 8.3% in 2008. Hotel guests for the first half of 2009 increased by 4.7% YOY, with the number of guests exceeding 3.85 million;
- Europe, and notably the UK, is the largest source market for Dubai. The UK and Ireland markets together generated 854,601 visitors in 2008, an increase of 14.0% compared to the previous year. In the first half of 2009, these visitors amounted to 383,197 while GCC guests in Dubai hotels increased by 35.0% for the first half of 2009. This compensated slightly for the loss from the UK and Ireland markets which seem to have slowed down owing to the economic crisis;
- The Middle East region witnessed the largest increase in passenger movement globally in 2008;
- Dubai Metro, one of the most advanced railway systems in the world, was launched on 9 September 2009, with stations in key business and leisure destinations within the Emirate, connecting it from end to end;
- Serious attention is currently being given to develop sustainable growth in the logistics and transport industry.

Seasonality

Dubai is a balanced destination with clearly segregated submarkets; city centre hotels and beach hotels. Although both submarkets witness low occupancy in the summer, business and leisure demand together render seasonality less pronounced throughout the year. Table 1 shows the seasonality of hotel occupancy in Dubai for 2007, 2008 and Year-to-September 2009 for the overall hotel market.

Table 1 **Seasonality – Monthly Occupancy 2007, 2008 and Year-To-September 2009**



Source: STR Global

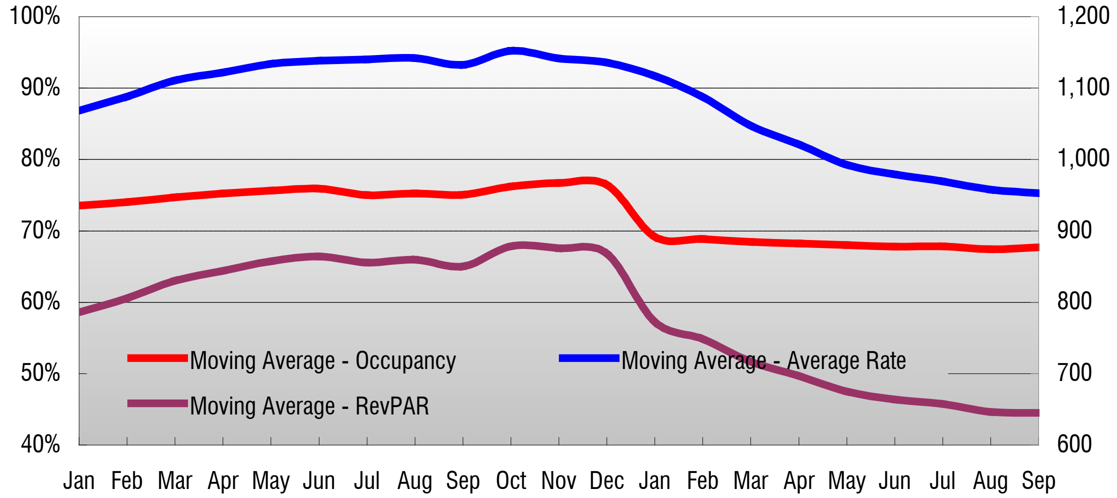
Table 1 indicates that for all three years, the high season for tourism arrivals extends from January to April (peaking in February), while the trough is typically from May to mid-October (bottoming in September) as business and conference visitors take holidays. It is worth noting that from 2007 to 2009, Ramadan overlapped with September.

We also note that during the period in question, both extremes decreased; both the lowest and the highest occupancies for each year went lower and lower. Occupancy in the lowest month, September, plunged from 70.2% in 2007 to 59.1% in 2008 and 56.8% in 2009. Occupancy in the highest month, February, plunged from 91.4% in 2007 to 87.7% and 74.5% in 2008 and 2009, respectively. This can be partly explained by the financial crunch over this period which gradually reduced business tourism demand. Another factor behind such a trend is the increasing yearly supply, notably in the five-star segment, which typically has a lower occupancy than that of the aggregate market represented in our sample.

The fourth quarter of the year typically forms the shoulder demand. With the first three quarters of 2009 consistently following the pattern marked in 2007 and 2008, it would be reasonable to expect an increase in occupancy from October to December, albeit at lower levels than what was commonly witnessed in the past. Year-to-September 2009 occupancy is 13.0% lower than its 2008 counterpart.

Table 2 shows the twelve-month moving average of hotel occupancy, average rate and RevPAR in Dubai from January 2008 to September 2009.

Table 2 **Twelve-Month Moving Averages – Occupancy, Average Rate and RevPAR January 2008-September 2009**



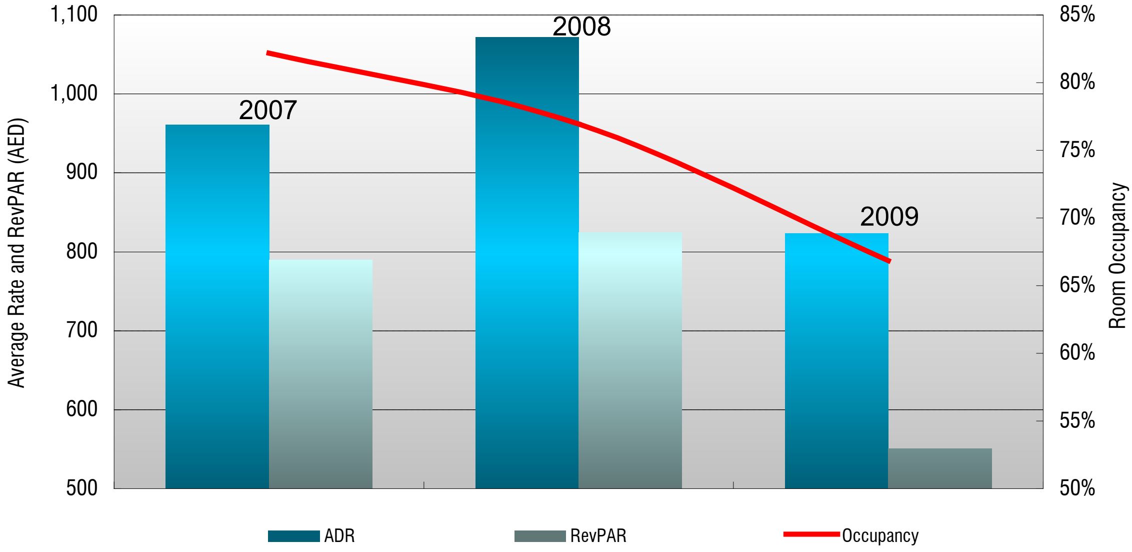
Source: STR Global

Table 2 shows the flat occupancy curve for 2008, dropping significantly in December, then going flat again until September 2009. This shows us that the dire financial times did not affect seasonality but merely scaled down the volume of business year to year.

Hotel Performance

The analysis in this market snapshot is based on a sample of mostly branded hotels within the Dubai hotel market. The sample includes 25,852 rooms spread across 98 properties. Table 3 shows the Year-to-September hotel performance for the hotel market in Dubai from 2007 to 2009 in AED.

Table 3 Year-To-September Hotel Performance in Dubai - 2007-2009 (AED)



Source: STR Global

Year-to-September occupancy dropped from 82.2% in 2007, to 76.9% in 2008 and 66.8% in 2009. The drop in occupancy in 2008 is attributed to the increase in hotel supply that year as well as big employers starting to shrink their allotments with hotels as a result of the financial crunch. This drop continued further between September and end-of-year 2008. Since December 2008, monthly occupancy drops YOY were in double figures, easing off slightly in July and September 2009. This can be explained by Dubai's high dependency on international accommodation demand. In the absence of significant domestic demand, topped by dramatised news about the impact of the crisis on the city, this 'panic', among both operators and guests, further impacted occupancy negatively.

Despite these drops in occupancy, Dubai hotels were able to achieve (on average) an increase in average rate of 12.0% by Year-to-September 2008 (to AED 1,072). This can be explained by two factors. Firstly, operators of the five-star hotels in the market were still at a point where occupancy drops were tolerable and did not necessitate compromising average rate; they were still above the threshold occupancy rate. Secondly, monthly average rates in 2008 were witnessing double-figure rates of growth YOY, up until September when decreases were met in September, November and December. October witnessed a YOY increase of 17.6%. It is worth mentioning that this was the only month that witnessed an increase in occupancy in 2008.

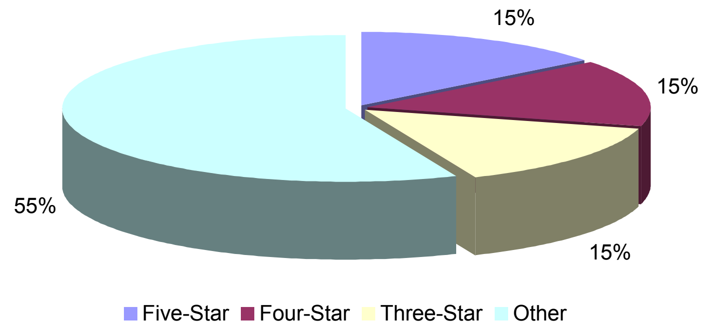
We consider that it was just after October 2008 that average rate was being undercut and all the way through to September 2009. During that period, monthly average rate declines YOY ranged from 5.6% (December) to 31.0% (May). Year-to-September 2009 average rate was 23.0% below that of its

2008 counterpart, at AED 824. The resulting YOY RevPAR drop was of -33%, at AED 551. This stands 30.0% below what it was in 2007.

Supply

By June 2009, the Dubai hotel market comprised 40,943 hotel rooms, up from 37,261 hotel rooms by the end of 2008. Table 4 shows the city's mix of hotel supply as of June 2009.

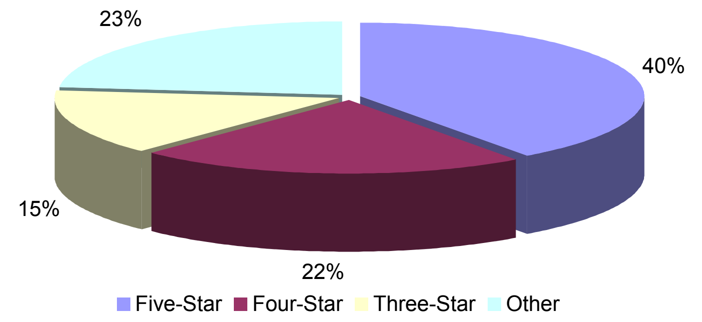
Table 4 Existing Hotel Supply – Dubai (June 2009)



Source: DTCM

As can be seen from the Table 4, there is an equal number of properties for each of the five-star, four-star and three-star standings. This becomes less counter-intuitive when we look at the number of available rooms supplied by each asset class, as shown in Table 5.

Table 5 Existing Room Supply – Dubai (June 2009)



Source: DTCM

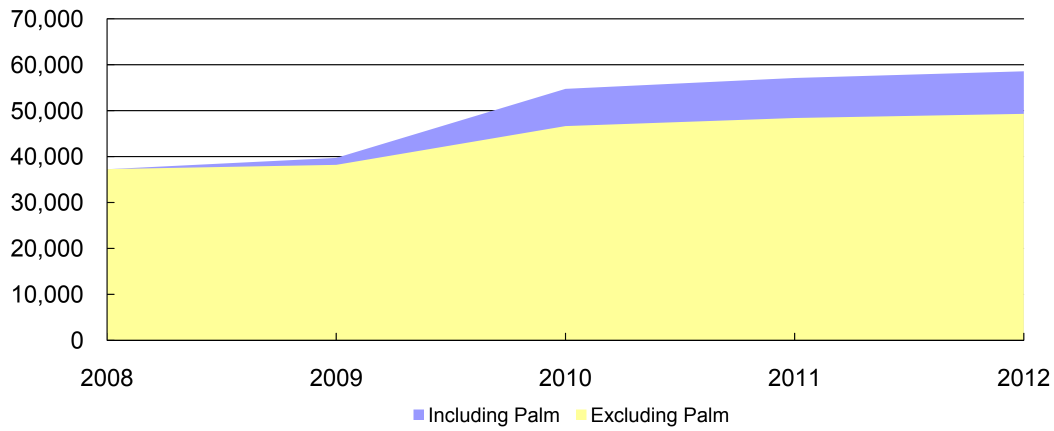
This market room mix reflects the need for further expansion in the three-star market supply, especially in times when guests become more price-sensitive. There are more one-star and two-star hotel rooms than there are of the three-star standing. We can also infer the higher average room count associated with five-star properties when compared to four-star ones. In turn, four-star properties are typically bigger in size than their three-star counterparts. In fact, since 2002, the average hotel size in Dubai was on the rise showing the increased preference for five-star developments in the Emirate.

New Supply

With a lot of the construction that has been going on in Dubai now being put on hold, and with several hotels being planned among major projects, it becomes quite speculative to tell what will happen with regards to announced openings. Business Bay, a massive community development that was being executed up until mid-2008, was planned to offer about 2,000 hotel rooms, all of which were scheduled for completion by 2009. We have excluded these hotel rooms for the purposes of this market snapshot in the absence of accurate information on development stages.

We therefore present in Table 6 the 'most likely' supply of hotel rooms until 2012. Incomplete developments on The Palm Jumeirah are being reviewed, rescheduled or cancelled.

Table 6 Future Supply of Hotel Rooms in Dubai (2009-12)



Source: HVS Market Intelligence

Consistent with the existing hotel offering, five-star hotels dominate the proposed supply of hotels in Dubai. However, we consider it not be unlikely that these properties will be revised in terms of positioning and hence, conforming to the post-crisis market needs. Such needs, although identified, are still untapped. We note the flatter supply curve when compared to supply curves we were accustomed to seeing a year ago. This is a positive outcome of the limited availability of financing means following the global financial meltdown.

Conclusion

As mentioned earlier, it is not unreasonable to expect the market to perform better during the fourth quarter of 2009, as was the case in 2008, 2007 and the past decade for that matter. Except for the variance of the occurrence of Ramadan, seasonality remained the same over the years and up-to-date. However, with the new supply entering the market, in most part over 2010 and 2011, it would be unlikely that performance figures hereon go back to 2007 and early 2008 levels. Moreover, the dominance of the five-star hotel offering in the Dubai market contributed in inflating the aggregate market average rate, rendering it prone to big decreases in times of distress, as is happening now. If the positioning of the properties in the pipeline gets revised, it will be even harder to restore performance levels witnessed before, albeit that growth rates seen in the past can return.

At present, there is still a gap in the three-star and four-star hotel products. Although these asset classes do not provide investor returns of the margin or scale of the five-star product, they can produce a more steady revenue stream, owing to their performance being less volatile in an economic downturn. Although guests of a three-star hotel could be more price sensitive, RevPAR variances across economic cycles are typically lower for this asset class than their five-star counterpart.. We also note that the profitability levels previously witnessed among five-star hotels have decreased. If and when these will be restored is highly dependent on how the market landscape will be in the coming few years.

All in all, in times like these, a strategy that includes all hotel asset classes should be put in place. Dubai's lower rates today could be an advantage when seen in conjunction with the increased intra-regional travel. As a mass-tourism destination, Dubai should now, more than ever, complete its impressive hotel portfolio to reap the benefits of this trend.

Infrastructure developments, the most recent addition to which was the Dubai Metro, have endowed Dubai with a comparative advantage relative to other MENA cities, as a destination of choice for both business and leisure tourism. Efforts to ameliorate the logistics offering in the Emirate are due to enhance Dubai's position further. Having identified the measures that need to be taken, Dubai will succeed in restoring itself on the tourism map once again.

About the Authors

Nehme Ayoub joined the Dubai office's Consulting & Valuation practice in May 2008. Before joining HVS, Nehme led the investment team at Noor International Holding. While in Boston, he honed his skills at Mercer and Bank of America's Investment Services in the areas of finance and portfolio analysis. During his years at college, Nehme worked as an intern with Banque Du Liban, Deloitte and Société Générale pour les Études et l'Entreprise. Nehme holds a masters degree in Economic Policy from Boston University and a bachelor in Economics from the American University of Beirut.

Hala Matar Choufany is the Managing Director of HVS Dubai and is responsible for the firm's valuation and consulting work in the Middle East and North Africa. She initially joined HVS London in 2005 and moved to HVS Shanghai in September 2006 where she helped grow the HVS Shanghai office and its business in the Asia region. She relocated to Dubai in September 2007 and now looks after HVS's interests in the Middle East. Before joining HVS, Hala had four years' operational and managerial hotel industry experience. She lectured at Notre Dame University in Lebanon on International Travel and Tourism. Hala holds an MPhil from Leeds University, UK, an MBA from IMHI (Essec- Cornell) University, Paris, France and a BA in Hospitality Management from Notre Dame University, Lebanon. Hala has worked on several midscale and large-scale mixed-use developments and has conducted numerous valuations, feasibility studies, operator searches, return on investment analyses and market studies in Europe, the Middle East and Asia.

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