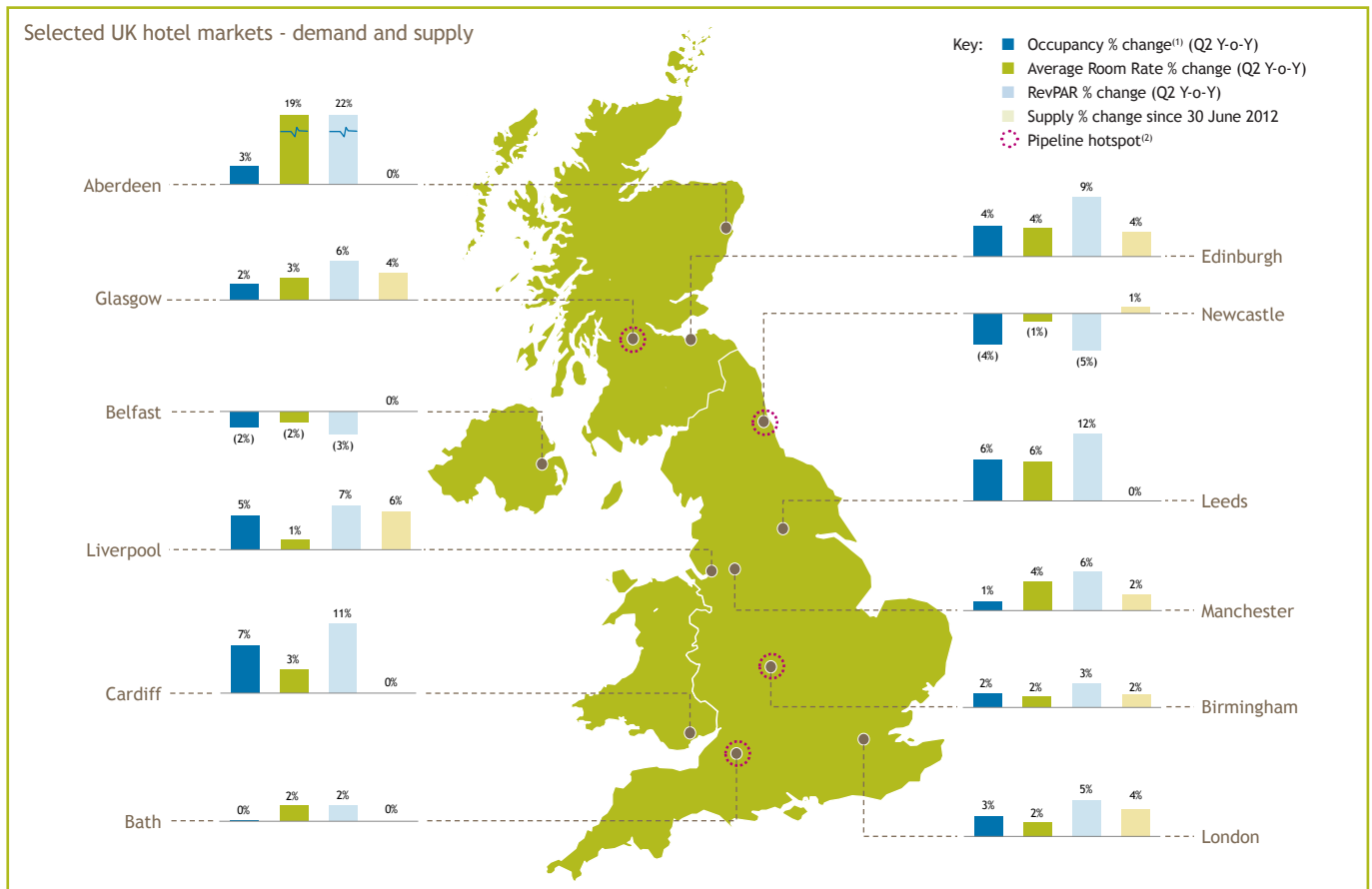


Hotel Bulletin: Q2 2013

Profitability growth returned to the regions in Q2 2013 for the first time on a last twelve months basis since the downturn. London also recorded positive results; however weak comparators, due to the Diamond Jubilee, masked what was otherwise a flat quarter. This issue's city focus is on Liverpool, a hotel market that has doubled in size in the last decade.



Source: AM:PM, HotStats

Note: Q2 covers the three months to the end of June 2013

Q2 Y-o-Y compares the average of Q2 2013 to the average of Q2 2012

(1) Occupancy percentage change represents actual rather than absolute percentage change

(2) Pipeline hotspots are cities with an active pipeline greater than 10%. Active pipeline refers to hotels with an opening date in the next three years

Key highlights of period

Performance continues to improve

Both London and the regions recorded RevPAR increases in Q2 2013, albeit on the back of weak comparators in the previous quarter due to the Diamond Jubilee and Easter falling in Q2 2012. Out of the 12 cities covered in our report, ten recorded RevPAR increases.

Input costs have generally increased, however staff restructuring schemes have begun to result in significant payroll savings. Improved revenue performance and cost control has resulted in the regions returning to profit growth on a LTM basis for the first time since the downturn.

Slow but steady improvements in performance should give hoteliers more confidence to plan and invest for the future.

Supply and transactions subdued, but not for long?

New supply levels in the second quarter remained subdued in comparison to 2012. The low supply levels are not indicative of the longer term trends in market size, with 28,092 bedrooms remaining in the active pipeline.

Following such a strong Q1 2013, Aston Hotels was the only portfolio transaction to complete in the quarter. There were however a number of single asset sales suggesting that the gap in valuation expectation is continuing to narrow.

The debt market for hotels is widening to include alternative providers such as debt funds, credit investors and family offices attracted by the cash generative and asset-backed nature of hotel assets.

Demand commentary

Quarter results

Performance in the quarter has been positive on the whole, with ten of the 12 cities reviewed recording RevPAR increases.

Following a flat first quarter, RevPAR in London increased by 5% in Q2 2013. This increase has been exaggerated by the absence of Diamond Jubilee celebrations, which in June 2012 led to a RevPAR decrease of 7% compared to the previous year. Excluding this effect, performance metrics in London remained flat. This effect was experienced in other areas of the country. For example, RevPAR increases of 3% and 11% in Birmingham and Cardiff respectively were exaggerated by respective June 2012 RevPAR decreases of 8% and 20% compared to the previous year.

The regions returned to profitability growth in the second quarter for the first time since the downturn on a LTM basis. This has been driven by continued increases in RevPAR, payroll efficiencies and a decline in commission paid to travel agents in Q2 2013.

In Q2 2013 Aberdeen recorded a 22% increase in RevPAR compared with Q2 2012. Increases are attributable to oil and gas industries coupled with a low level of new supply coming onto the market. Developers concerns over the susceptibility of the city's hotel market to the price of oil and gas appear to have been overcome due to the longevity of strong performance. Aberdeen now an active pipeline equal to 9% of current supply.

Leeds recorded a 12% increase in RevPAR in the quarter of albeit on the back of 4% decrease in Q2 2012 compared to Q2 2011.

Belfast recorded a RevPAR decrease of 3% in Q2 2013. Events surrounding the centenary year of the sinking of the Titanic led to a RevPAR increase of 26% in Q2 2012. As such, hoteliers may be encouraged by the only modest 3% decline recorded in Q2 2013.

Newcastle recorded a 5% decrease in RevPAR in the month, demonstrating that performance is still being impacted by the 15% increase in the size of the Newcastle hotel market between June 2011 and June 2012. Quarterly RevPAR growth was last experienced in Q4 2011.

Slow and steady improvements in RevPAR and profitability should give hoteliers a foundation to plan and invest for the future rather than continuing to weather the downturn.

Supply commentary

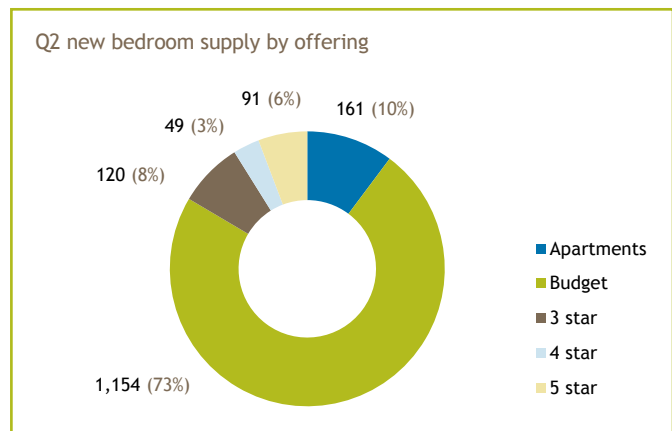
Notable openings

New openings remained at a low level in Q2 2013 in comparison to the high levels of new supply experienced in 2012.

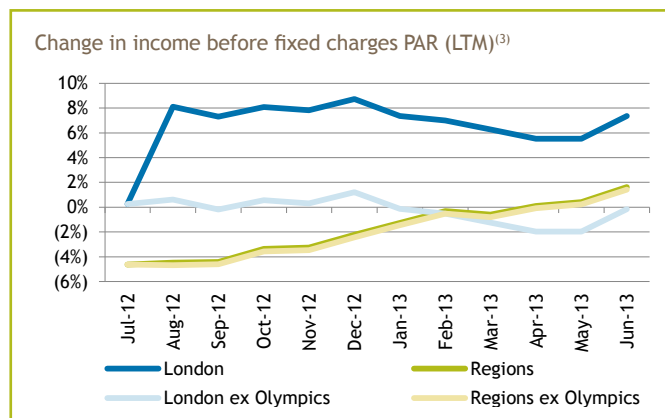
1,575 bedrooms opened in the second quarter. Both Travelodge and Premier Inn continued to expand, opening 253 and 367 bedrooms in the quarter respectively. The two hotel groups now have 88,647 bedrooms in the UK, which equates to 16% of the UK hotel market.

Notable openings in the second quarter included:

- The 224 bedroom Holiday Inn Express Birmingham Snow Hill following the £23 million conversion of Kennedy Tower by Sanguine Hospitality in a Downing Investors funded BPR scheme. The hotel is operated by Interstate Hotels & Resorts. This marks the first new opening since the acquisition of Sanguine by Interstate and demonstrates the develop-to-manage strategy.
- The 91 bedroom Park Inn Glasgow brings the UK Park Inn portfolio to 22 hotels and marks a return to the city for the brand after a two year absence.
- Great Northern Hotel Kings Cross. The Grade II listed building has had £40 million spent on its renovation after being closed for 12 years. The five star hotel is independent of brand and is operated by Robson Asset Management.

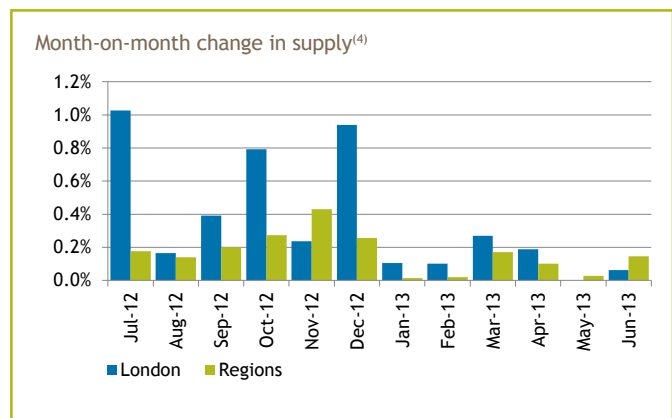


Source: AM:PM



Source: HVS, HotStats

Note: (3) Graph shows rolling 12 month average of monthly year-on-year IBFC PAR (ex Olympics data assumes 0% Y-o-Y growth in August)



Source: AM:PM

Note: (4) Graph shows supply compared with the previous month

In the pipeline

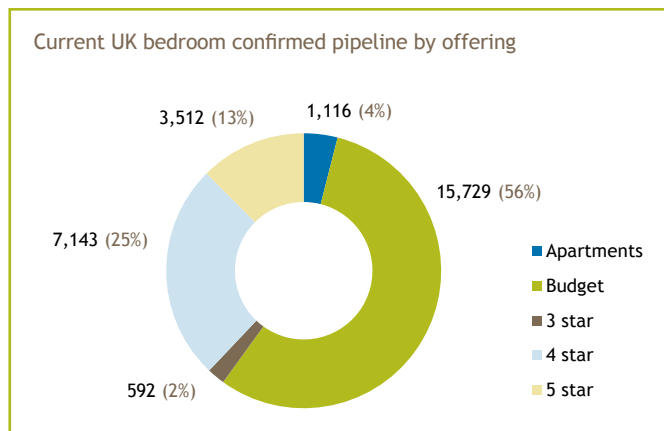
The 2012 trend of increased new supply appears likely to continue with 28,092 bedrooms in the active pipeline. Travelodge and Premier Inn continue to dominate, with 31% of the total active pipeline.

Newcastle (16%), Birmingham (15%), Glasgow (14%) and Bath (13%) have active pipelines over 10%. Newcastle's recent performance suggests that current hoteliers in the city may continue to struggle with further material growth in supply, especially given the 16% supply increase in the last two years.

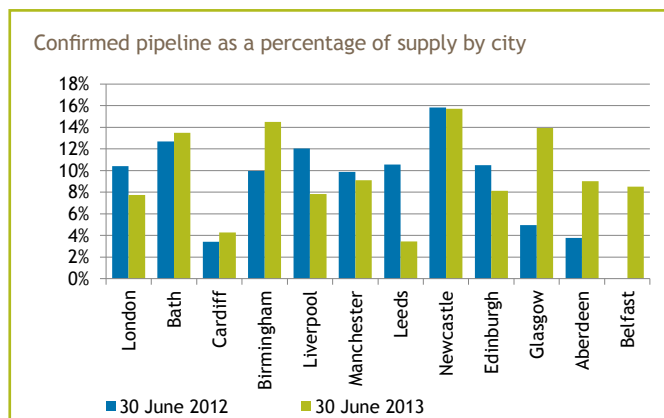
Notable assets in the pipeline include:

- GE Real Estate and Endurance Land have submitted plans to convert offices in London's Midtown at 15 Old Bailey into an 83 bedroom boutique hotel. With the recent addition of significant amounts of high quality office stock in the city such as Heron Tower, developers may look for alternative uses for Grade II listed buildings.
- The 452 bedroom InterContinental London The O₂ is set to open in 2015, representing the third InterContinental hotel in London. It remains to be seen whether there will be sufficient demand for the five star hotel in the area, especially given the 142 bedroom Four Seasons in Canary Wharf and other nearby pipeline projects.

Whitbread unveiled its new concept The Hub by Premier Inn in Q2 2013, offering smaller bedrooms at a lower price point. The Hub is likely to enable Whitbread to add more hotel rooms in high population density locations than with Premier Inn alone.



Source: AM:PM



Source: AM:PM

Note: The pipelines above only include developments with a confirmed opening date

Transactions

Following a Q1 2013 which included the completion of the Principal Hayley, Marriott, Malmaison / Hotel du Vin deals, the portfolio transaction market has paused for breath. The only transaction was Dominvs Investments acquisition of the three asset Aston group for an undisclosed sum.

Single asset transactions however are continuing to complete. Notable transactions include:

- Dhillon Hotels' sale of the 250 bedroom Paragon Hotel in Birmingham for an estimated £5 million.
- Aran Handa's Cairn Hotel Group acquired the former Washington Hotels three star 77 bedroom Queensferry Lodge Hotel in Fife for approximately £4 million. The Group now owns 22 hotels with over 2,000 rooms.
- Oaktree Capital Management acquired Quintain Estates' 50% stake in the four star 361 bedroom Hilton London Wembley for £30 million. Oaktree is also understood to have set aside up to £300 million to invest in serviced apartments in London.
- Three Travelodge transactions completed in the quarter, namely the Travelodge London Farringdon, the Travelodge London Woolwich and the Travelodge Bath Waterside. Yields achieved in the transactions were 5.4%, 6.8% and 9.0% respectively, which highlights the disparity in valuations realised in central London, non-central London and the regions.

BDL Management and Redefine Hotels merged in the month to form Redefine BDL Hotels, a group that now operates over 6,500 bedrooms throughout the UK. The merger follows Interstate Hotels & Resorts' acquisition of Sanguine Hospitality in March. Real estate owners are increasingly trusting the operation of their hotels to specialist management companies.

De Vere Venues is expected to be sold before the end of the year. Private equity are favourite to acquire the group, demonstrating the continued attraction of hotel groups to this type of investor.

Bank funding in the second quarter

The debt market for hotels in the UK is widening far beyond traditional high street banks. Debt funds, credit investors and family offices are gaining an appetite for the cash generative and asset-backed nature of hotel businesses.

With yields on hotel lends often in line with yields being offered on speculative grades of debt, it is unsurprising that new parties are entering the market.

Debt funders continue to have a preference for multisite groups with a good operator and a proven track record.

Notable funding in the quarter include:

- Cairn Hotel Group completed a £31.5 million refinancing with HSBC's Yorkshire and North East Corporate Centre, with £6.5 million set aside to support a refurbishment programme and fund new acquisitions.
- LRG group, the joint venture between Singapore sovereign wealth fund GIC, Silverpeak Real Estate Partners and Realstar completed a refinancing of £585 million of existing debt. LRG group has a stake in over 10,000 bedrooms throughout the UK.

Whilst many of the more institutional funds are targeting prime hotel real estate, others are supporting experienced hotel investors in looking at larger regional opportunities.

Source: AM:PM, Mergermarket, HSBC Newsroom, Freshfields.com

Focus on: Liverpool

The market

Liverpool was one of the most heavily impacted cities during the second world war and through the 1970s and 1980s large parts of the city remained derelict. Since then the city has transformed beyond all recognition. A regeneration funded by European grants was highlighted when Liverpool became the European City of Culture in 2008. Work has not stopped; tourists are now attracted to Liverpool by entertainment venues such as the Echo Arena, shopping centres such as Liverpool One, art galleries including the Tate Liverpool and sports grounds including Anfield and Goodison park.

In the last decade, the size of Liverpool's hotel market has doubled to respond to this change. The city is now the seventh largest hotel market in the UK.

Liverpool's corporate market is not as developed as its leisure offering. There are approximately 33% fewer businesses per 10,000 residents aged 16 or over in comparison to the Great Britain average. This gap is likely to narrow as Liverpool continues to invest, with the £5.5 billion Liverpool Waters development and planned improvements in infrastructure likely to attract national and international businesses.

Performance

The relationship between rates and occupancy is more volatile in Liverpool than corporate centres such as Manchester. Leisure customers are more flexible than corporate clients; a key challenge for hoteliers in the city is maintaining rates without sacrificing occupancy.

Performance in the last 12 months has been mixed. Apart from a RevPAR improvement coinciding with Liverpool's hosting of the Moby awards in November, performance until January 2013 was down on the previous year. In a city reliant on tourist revenue, changes in event success can have a material impact on year-on-year performance.

Since February, RevPAR has improved in every month in comparison to the previous year, which is particularly impressive given the cold weather experienced in the first quarter and the early timing of Easter. As always, the Aintree Grand National represented a strong period for Liverpool with RevPAR in April 24% higher than the average for the year.

In recent years, demand has remained buoyant in Liverpool despite the increase in supply, which is a testament to the dramatic improvement in the leisure market. Developments should attract corporate customers to the area, and in the long-term, Liverpool hoteliers are likely to enjoy more predictable revenue streams and an increase in average rates.

Source: AM:PM, HotStats, Liverpool Economic Briefing 2013

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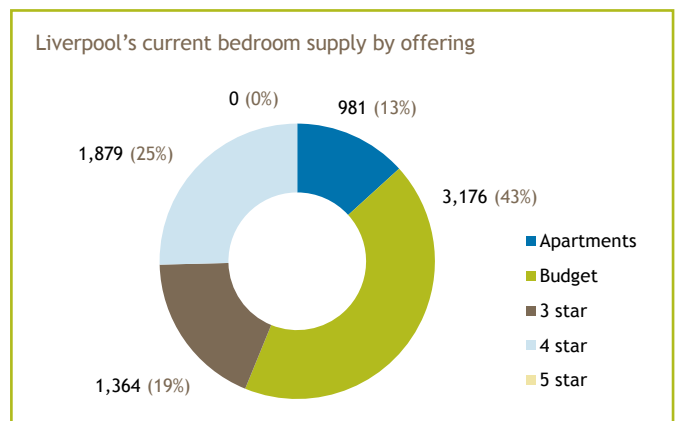
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Supply, pipeline and transactions

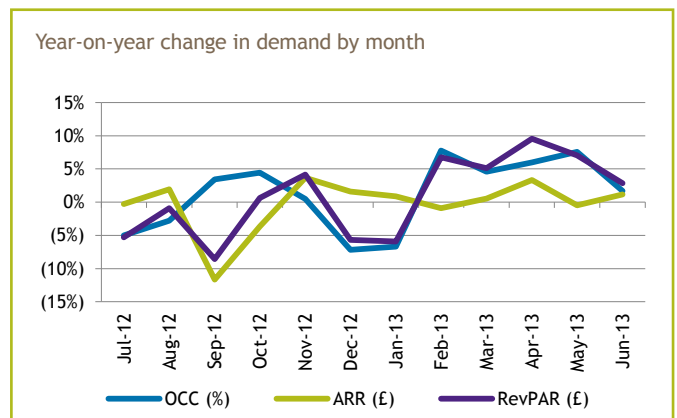
Hotel supply has approximately doubled in the last decade in Liverpool, with 3,902 bedrooms (38 hotels) opening during this period. Budget offerings dominate the market with 43% of bedrooms. 44% of bedrooms are three and four star and the city does not currently have a five star hotel. The substantial improvement in the leisure market in recent years is attracting new concept brands, notably Z Hotels' first opening outside of London and the opening of the 52 bedroom Hoax Hostel.

The Liverpool corporate hotel offering is set to expand with the continued regeneration. Out of the 578 bedrooms in the pipeline 403 are four star, including the 87 bedroom Doubletree by Hilton. A higher proportion of four star bedrooms will likely result in an increase in average room rates.

The Liverpool transaction market has been quiet in the last 12 months with the exception of sales of the Malmaison Liverpool and the Liverpool Marriott Hotel City Centre that were sold as part of portfolio transactions in Q1 2013. The appetite for acquisitions in the city is likely to remain subdued whilst there is site availability and a number of new developments in the pipeline.



Source: AM:PM



Source: AM:PM, HotStats

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