



Hospitality Directions Europe Edition*

Issue 15 March 2007

With the best of times set to continue, how close behind are the worst of times?

- Despite concerns of weakening industry fundamentals (especially in the US), conditions are still looking good
- Strong economic growth - the UK is expected to have the best performing economy in the G7 this year – will continue to drive business and leisure travel demand and underpin buoyant trading conditions in 2007 and 2008
- PricewaterhouseCoopers' latest UK hotel sector forecast expects RevPAR growth to continue, but at a slower pace than last year
- Growth will be driven primarily by aggressive room rate strategies and records could be broken again this year, as rates surpass 2006 levels
- UK occupancy levels are now in the mid-70s and London is virtually full up at close to 83 per cent occupancy
- For the UK we forecast RevPAR growth of 5.5 and 5.6 per cent in 2007 and 2008, taking expected RevPAR to £64.16 in 2007 and £67.77 in 2008
- For London, RevPAR growth of 5.4 per cent and 5.8 per cent will take RevPAR to £100.45 this year, and £106.27 next year
- In the Provinces, results continue to be more mixed, depending on location. Growth is expected in Manchester, Edinburgh and Birmingham. In Edinburgh, the city's booming hotel sector will see occupancies heading towards 80 per cent this year
- Currently the good times are rolling but the risks of unforeseen events remain and we are only ever a scare away from the declines that regularly impact the sector - see Graph 1 on page 3. Embracing and managing risk is likely to be a key differentiator in the future.

Forecast highlights 2007-2008 (growth %)

	2007			2008		
	UK	London	Provinces	UK	London	Provinces
Occupancy	1.0%	0.4%	1.4%	1.0%	0.7%	1.1%
ARR	4.5%	5.0%	4.2%	4.6%	5.0%	4.4%
RevPAR	5.5%	5.4%	5.6%	5.6%	5.8%	5.5%

London...

- record trading in 2006 as conditions remained buoyant
- future growth but at a slower pace – forecast RevPAR growth of 5.4% and 5.8% in 2007 and 2008
- some aggressive rate strategies drive average ADR to £122 in 2007
- luxury ADR reaches £350+
- strong supply pipeline
- new openings in 2007 include Firmdale's Haymarket hotel set to open this month

Postscript: So far the year has got off to a flying start and, as we go to print, preliminary results for the first two months of 2007 suggest that London still looks hot, with double digit RevPAR growth. We would expect this to moderate in the second half of the year.

Outside London...

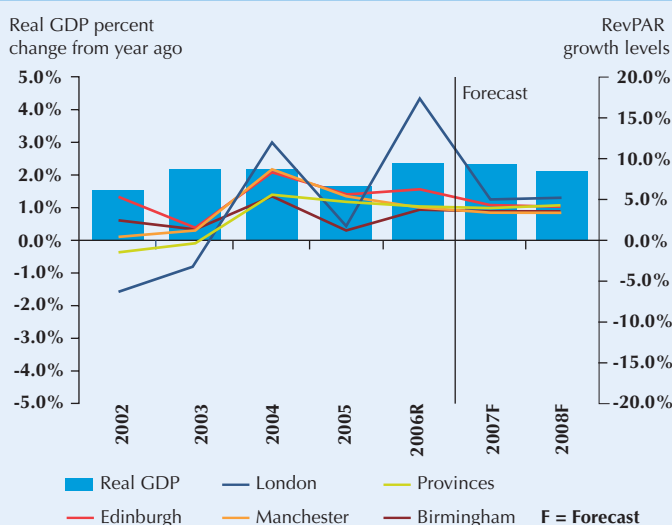
- performance records broken in 2006 but growth not spread evenly
- move to build not buy
- new brand entrants will include Bannatyne, Hilton Garden Inn
- all segments see more activity
- Edinburgh helps Scotland celebrate mini tourism boom as RevPAR growth heads higher
- Manchester appears to have overcome its supply issues – in 2006 at least
- Birmingham sees growth as city's renaissance continues

Risks remain: uncertain and challenging market, cost of borrowing, hard economic landing, terrorism spectre, bird flu, discretionary spending squeeze, taxes APD + proposed bed tax supply issues

Luxury helps lift London results

Conditions still looking good for UK hotels

Forecast for UK and key cities over next three years



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007, **Macroeconomics Data:** Oxford Economics February 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte February 2007

It will not all be easy going, and in the global marketplace, growth does not necessarily mean business as usual. Changes in the global economic environment will facilitate new growth opportunities for some but expansion into new markets and new products will also mean new risks and new costs

Revenues and property prices can't continue rising for ever. Some of the prices paid will put pressure on operators to perform, especially in a downturn, and as interest rates rise, the leveraged positions of some private equity players are likely to become more difficult



Latest UK hotel sector forecast

UK

How long can the good times last?

In a highly competitive real estate market, hotels have become attractive real estate assets and as hotel real estate values continue to increase, a diverse range of private investors are seeking property investments with predictable income streams. Private equity firms secured ownership of approximately 38.4 per cent of the hotel transactions completed globally in 2005, and no doubt this will be higher in 2006. Thanks to the continued separation of hotel ownership from hotel management (the 'opco propco' shake-up) this trend is likely to continue in 2007. While InterContinental has been leading the charge out of hotel asset ownership, others have followed fast. In January Macdonald Hotels & Resorts completed the sale of 24 of its hotels to Moorfield Real Estate Fund for more than £400million. Recently Accor sold its 30 Novotels in the UK to Land Securities in a deal worth £439 million. And there are many more.

The sector's strong performance has generated new investment which in turn means opportunities for expansion, investment in new products, refurbishment, and better management. But the hotel sector is cyclical. There is a direct correlation to economic performance and the sector is vulnerable to a number of risks. Graph 1

shows the events which precipitated some of the good and not-so-good times since 1978.

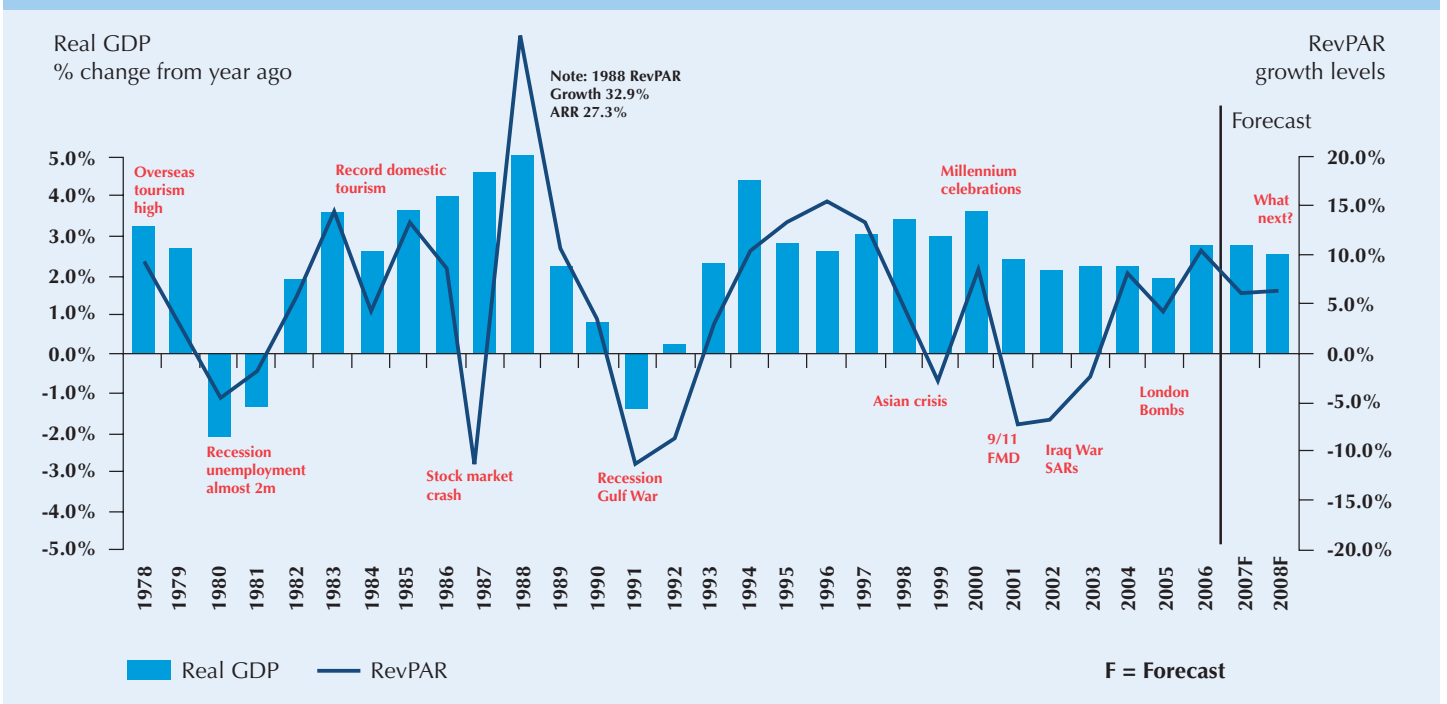
- **Corporate buyers resist rising room rates**

Many investors and owners are becoming more demanding in terms of a return on their investment. In addition some of the pricing structures paid in recent deals put a lot of pressure on operators to perform. The pressure to continually raise room rates, in order to deliver higher revenues, without a commensurate increase in product or service quality, is likely to push corporates towards reviewing their travel policies and managing their spend more effectively. This may include a move towards alternative concepts, particularly extended stay products such as Club Quarters and Bridgestreet which are becoming more popular with corporate buyers.

Nurturing relationships and providing value is important. Today's consumers and corporate buyers have far more brands and types of property to choose from, with new brand introductions and extensions likely to continue. For example Hilton has already announced it is bringing new products to the UK this year. Other new brands not seen in the UK yet include Starwood Capital's luxury Le Crillon brand and Starwood Hotels Aloft brand, both of which are set to travel.

Graph 1: Good times and not-so-good times

Real GDP growth and revenue per available room (RevPAR) 1978-2008



Source: **Econometric Forecasts:** PricewaterhouseCoopers 2007, **Macroeconomics Data:** Oxford Economics 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte, 2007.

Latest UK hotel sector forecast

“The strong market has been hard for corporates as they find relationships being stretched. Hotels are removing last room availability (LRA), room allocations, withdrawing rates and imposing early check out fees which has traditionally been an American tactic that is not enforced in the UK. Aggressively raising rates regardless of relationship is a very dangerous tactic if the market changes”

Samantha van Leeuwen,
Head of UK Hotels Procurement and Venues,
PricewaterhouseCoopers

• Busy supply pipeline

The dearth of reliable statistics on hotel supply make it difficult to draw reliable conclusions, however more companies have stated they intend to build new hotels and many international companies have busy development pipelines. As a result, in the next few years oversupply issues could exacerbate a trading slowdown, because although increases in demand for hotels stimulate the development of new hotels, the adjustment of supply to demand is not necessarily instantaneous or smooth. In the past we have seen periods when demand runs ahead of supply, creating shortages, high occupancy rates and high prices. We have also seen the reverse occur and there have been suggestions that excessive supply in some cities may slow down future RevPAR growth.

• Mind the widening gap

Scale and size matter a lot and there is a widening gap between large and small. Recent research from Plimsoll Publishing shows that of 1,500 hotel operators surveyed 98 per cent of last year's sales growth went to just 128 companies. As consumers expect higher standards and quality, so costs to keep products 'fresh' will continue to rise. A heavier burden of legislation may also fall on businesses in areas such as employment and sustainability. It is likely to be larger companies that have easier access to capital to invest in properties and the ability to pass these costs on more easily.

What else is new in UK?

The UK mid-market is set to see more attention for customers valuing stylish but affordable products. Marriott International intends to open another 50 Courtyard-branded hotels in Europe, including the UK. Soon travellers will be able to stay in a Hilton Garden Inn or budget brand Hampton by Hilton. BDL management has announced it will launch a new hotel group that will roll out some 40 properties over the next seven years. The Ramcore Hotels Group has signed an exclusive agreement with Wyndham Worldwide to develop mid market Ramada Encore hotels – mainly new build properties in key cities with 80 to 150 rooms.

“There are still plenty of sites out there in secondary places”¹

Ewan Campbell, Managing Director, Ramcore Hotels Group

Entrepreneur Duncan Bannatyne has announced a new Hotel Bannatyne in Durham, intended to be the first of five new openings as part of a £15million investment programme. The hotels will adopt a new concept in pricing and marketing, using an online model based on the travel market, where early bookers are rewarded. Normally discounts in the hotel sector are available to guests who book late but this pricing model, aimed at short-stay business clientele and tourists, enables guests who book in advance to have accommodation at a low rate, starting at £20 per night.

“Affordability is the key nowadays and there are not many hotels that offer guests modern and comfortable accommodation at such a low price,”

Duncan Bannatyne

At Chessington World of Adventures theme park in Surrey owners the Tussauds Group has agreed a franchise deal with InterContinental Hotels Group for a 150-room, Holiday Inn London – Chessington. BDL Hotels will manage the property. At the budget end, the Hotel St Lawrence, three miles from Luton airport, is to be converted into the 58-room easyHotel Luton, due to open towards the end of 2007. Eclipse Hotels will operate the property under franchise.

¹ Caterer & Hotelkeeper 23 November 2006

Latest UK hotel sector forecast

UK performance records were broken in 2006 and could be broken again this year

RevPAR grew by 10.1 per cent in 2006 and room rates grew by 6.4 per cent to reach a record £82.11. In terms of our forecast for the UK, room rates will continue to rise and growth of 4.5 per cent and 4.6 per cent over the next two years should drive RevPAR gains of 5.5 per cent and 5.6 per cent in 2007 and 2008. RevPAR could reach £64.14 this year, another record. In 2006 UK occupancy topped the previous 2000 peak and in 2007 and 2008 it should continue to climb a little further reaching the mid-70s.

See Table 1 and Graph 2. For more detailed hotel statistics from 2002-2008 see Appendix 2.

How did we do last time?

We knew 2006 would be an impressive year and forecast strong RevPAR gains accordingly, especially in London. However, we weren't bullish enough and it was only in London's luxury segment and across all Edinburgh key performance indicators (KPIs) where we were virtually spot-on. Much depends on comparison benchmark samples and although our estimates for occupancy growth for most regions were about right, we were too cautious on room rates. Compared to our estimate of 12.9 per cent RevPAR growth for London, hotel benchmarking studies put the growth between 13.1 per cent and 17.8 per cent for the year!

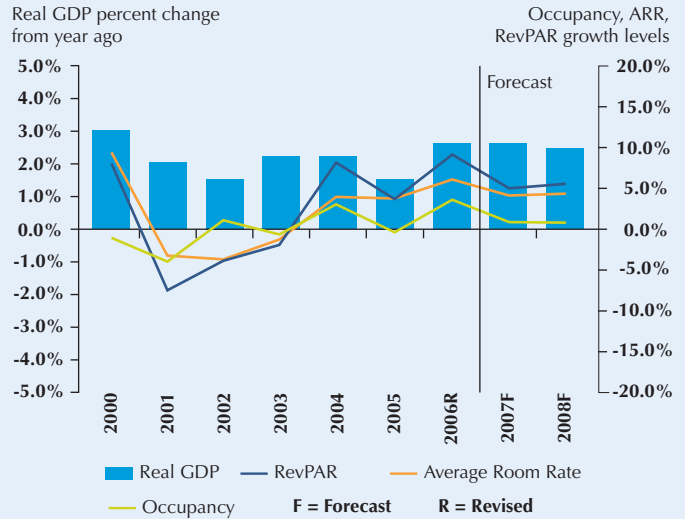
Table 1: PricewaterhouseCoopers Latest Forecast for UK February 2007

	2006R	2007F	2008F
Average Room Rate (£)	82.11	85.78	89.72
% Change	6.4%	4.5%	4.6%
Occupancy (%)	74.05	74.49	75.53
% Change	3.5%	1.0%	1.0%
RevPar (£)	60.80	64.16	67.77
% Change	10.1%	5.5%	5.6%

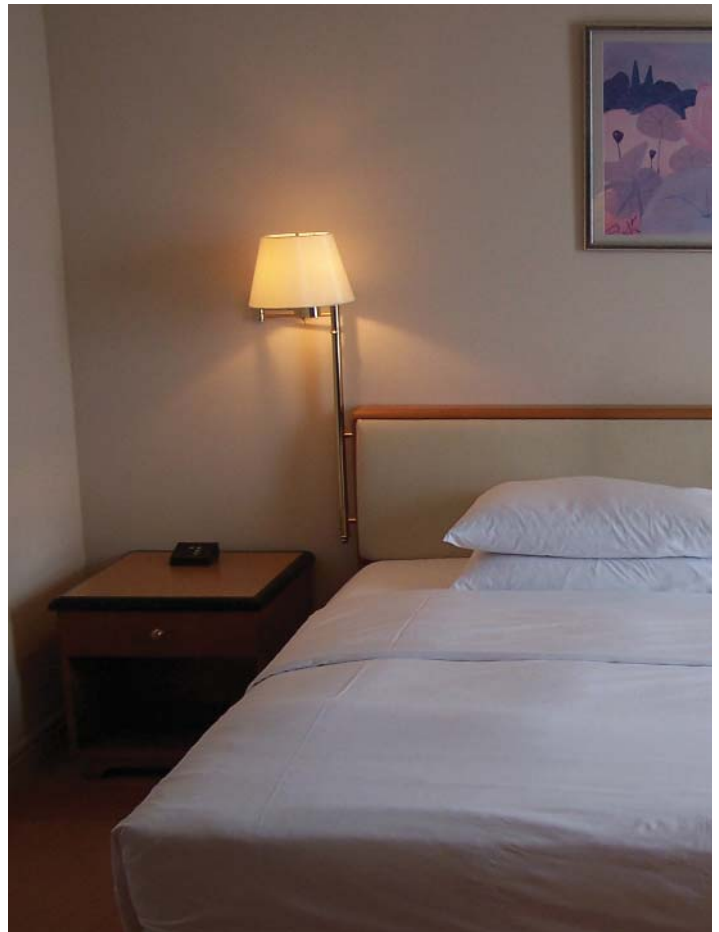
Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast.

Graph 2: UK hotel performance 2000 to 2008

Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007, **Macroeconomics Data:** Oxford Economics February 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte February 2007



Latest London hotel sector forecast

London

Record trading at London hotels where luxury segment is the star performer

Tourism is one of the key drivers of the capital's economy, accounting for around 10 per cent of GDP and providing 10 per cent of employment. However, London competes in a global tourism market and it has been a hard battle to attract tourists. London received over 25 million visits in 2006 – a year on year increase of 2.3 per cent. Foreign visits to London are expected to have grown by over seven per cent in 2006 and accounted for 14.8 million of the total. In contrast, domestic visits declined by 3.7 per cent to around 10.3 million. Looking ahead, VisitLondon expects foreign visitor volumes to grow by almost three per cent this year, but domestic visits are expected to decline by a further three per cent. The US remains the capital's largest single visitor market with 2.3 million visits in 2005. However, according to VisitLondon "the weakness of the dollar and the US market is a growing concern."²

Data for 2006 show that London hotels had a record year, albeit against some poor comparables in 2005. Nevertheless, ARR and RevPAR levels exceeded prior records in 2000. RevPAR growth was the highest annual increase since 1984 and 1985. Occupancy levels averaged reached 82 per cent, an 8.4 per cent gain over 2005, following a 1.7 per cent decline in 2005. Although still not at record 1997 levels when occupancies soared to 84 per cent, they are getting closer and as we explained

Table 2: PricewaterhouseCoopers Latest Forecast for London February 2007

	2006R	2007F	2008F
Average Room Rate (£)	116.06	121.88	127.97
% Change	8.7%	5.0%	5.0%
Occupancy (%)	82.13	82.42	83.04
% Change	8.4%	0.4%	0.7%
RevPar (£)	95.32	100.45	106.27
% Change	17.8%	5.4%	5.8%

Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast.

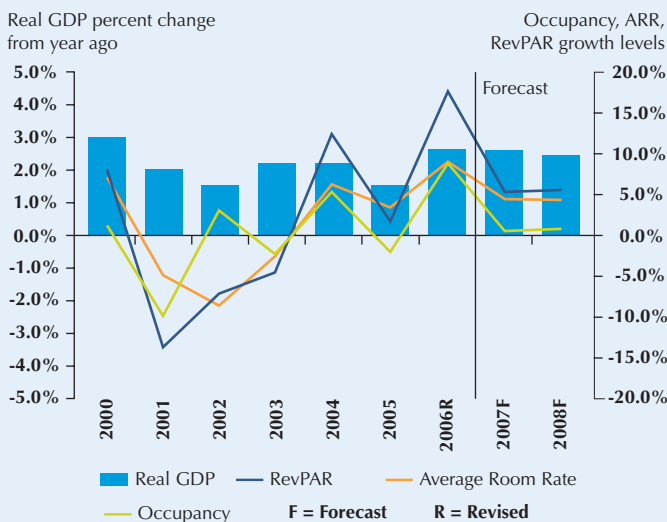
in our last forecast, once occupancy rates approach 83 per cent as they did last year and as we expect in 2007 and 2008, London is essentially full to capacity. For 2007 and 2008 we continue to forecast occupancy growth of just 0.4 per cent and 0.7 per cent respectively.

Let the good times roll

Since 2004 luxury hotels have seen strong room rate growth which has driven high RevPAR growth. At the time of our last forecast we expected 18 per cent luxury RevPAR growth in 2006. In the end, growth reached an exceptionally strong 29.5 per cent, compared to 17.8 per cent for London hotels as a whole, just under 20 per cent for mid market hotels and 16.6 per cent for London's upscale hotels. Luxury ARR reached £297.47 in 2006 with occupancies at almost 79 per cent. We expect a more sedate but strong 10.6 per cent RevPAR growth this year driven by a further 10.3 per cent ARR gain but

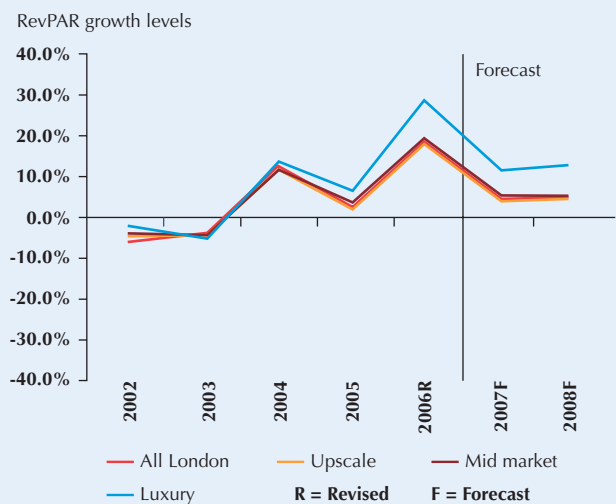
Graph 3a: London hotel performance 2000 to 2008

Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007,
Macroeconomics Data: Oxford Economics February 2007,
Benchmarking Data: Hotel Benchmark TM Survey by Deloitte February 2007

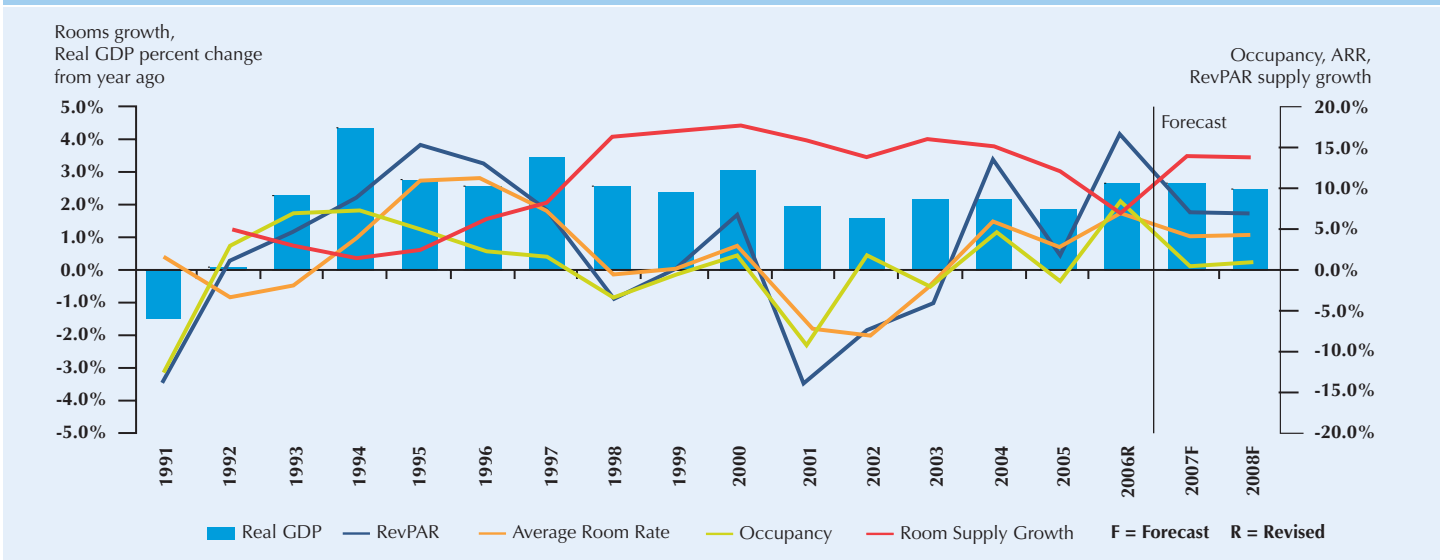
Graph 3b: London's luxury hotels performing strongest



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007,
Benchmarking Data: Hotel Benchmark TM Survey by Deloitte February 2007

Latest London hotel sector forecast

Graph 4: London room supply growth and performance 1991 to 2008



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007, **Macroeconomics Data:** Oxford Economics February 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte February 2007, **Rooms Supply:** Visit London, Census, LDMS

marginal 0.3 per cent occupancy growth. In 2008 we expect further 11.1 per cent RevPAR growth taking room rates over £362 and RevPAR to £288.75. No wonder luxury hoteliers want a presence in London. See Graph 3b.

For London as a whole, 2006 was the third year of ARR growth and with a further five per cent growth expected in 2007 this will take ARR to £121.88. Further growth of five per cent in 2008 will take room rates to £127.97 in 2008, another record year. If we look at real prices and strip out inflation there is still some way to catch up on previous years' pricing power - this year's anticipated ARR rate would equate to a real ADR rate of £59.21³. Looking forward, London's hoteliers should see a more sedate growth pace, with 5.4 per cent growth this year, taking RevPAR levels to just over £100. Similar growth in 2008 will take RevPAR to £106.27. See Table 2 and Graphs 3a and 3b.

How hard will it be to fill all London's new hotels?

Higher occupancy and room rates make existing hotels increasingly profitable (with a high conversion of revenue to profit) and supply shortages in part contribute to London's high profitability and occupancies. According to supply data from Visit London's Hotel Development Monitor, London is set for a period of sustained new hotel development. We have plotted some past and forecast room growth against past and forecast hotel performance, see Graph 4. A period of excess demand



³ 1987=100

Latest London hotel sector forecast

and shortage of bed spaces is normally followed by a period of excess supply, in which hotels have lower occupancy and room rates. For example, the graph shows increased supply following high occupancies and room rates in the years 1995-1997. Figures from Visit London suggest this could happen again between now and 2010, when an additional 11,000+ rooms are expected to be completed. How hard will it be to fill all these new rooms? Well, it depends if and when they come on line, but London is generally considered under-hotelled. A report prepared by PwC for the Mayor's Office in 2002 suggested a shortfall of 36,000 rooms⁴. Since then, a new report prepared for the Mayor's Office estimates the capital needs an additional 2,500 hotel rooms to open each year between 2007 and 2026⁵.

What's new in London?

The re-opening of several hotels following refurbishment is likely to impact trading at the luxury end. The InterContinental Park Lane has now reopened towards the end of its £60m refurbishment and March 2007 will see 60 suites open. Some interesting new plans include Surrey Cricket Club's recent announcement that they are planning to redevelop the Brit Oval. Plans will include a hotel and the scheme will be ready for final Test of the

2009 Ashes. Further west at Twickenham, the end of next summer will see a 156-room Marriott Hotel and a Virgin Active health and leisure club with a swimming pool open. Alongside new offices for the RFU there will be banqueting and conference facilities, plus a 400-seat theatre available for community use on 30 days a year.

"Twickenham will become a destination in its own right with something going on all year round. We are not short of car parking, we are only six miles from Heathrow and fairly close to the centre of London. There will be a surge of economic activity for the local area."

Paul Vaughan, RFU business Operations Director

A 600 room City Inn is to be built in the City with completion due by 2008. Buy-to-let operator Guestinvest has announced plans to develop the old Whitbread Brewery site in Chiswell Street. Travelodge is planning four new London openings in 2007. At the pub level Malmaison recently purchased the Fox & Anchor public house close to its Charterhouse Square hotel in London, where it will add six bedrooms.



Soon more London sports venues will have their own hotels

⁴ Demand and Capacity for Hotels and Conference Centres in London, Report to the Greater London Authority, PricewaterhouseCoopers August 2002

⁵ Hotel Demand Study, Report to the Greater London Authority, Grant Thornton and the Leisure and Tourism Organisation, June 2006

Latest hotel sector forecast for Provinces and other key cities

Provinces

Unsurprisingly given their diversity, the Provinces have seen more mixed results and more modest growth than London. Nevertheless, economic growth and robust domestic and international visitor volumes continue to drive development of the hotel sector in many cities throughout the UK. Some are doing better than others: Belfast, Edinburgh and Aberdeen are reported to be doing well but others like York, Leeds, Sheffield and Nottingham are not. Our own research shows Edinburgh as having the highest average achieved room rates outside London, at almost £80 last year and set to rise to over £85 by 2008. Liverpool celebrates its 800th anniversary this summer and, only a year away from celebrating being European Capital of Culture, has seen some high occupancies, although large increases in room supply this year may slow future performance.

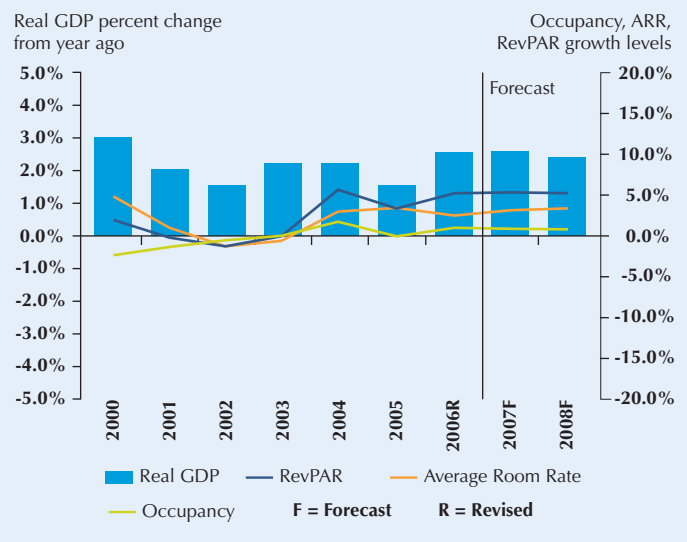
Gerard Basset co-founder of Hotel du Vin has bought a new hotel, the Busketts Lawn Hotel in Hampshire to be opened, after refurbishment, as the 13 bedroom Hotel Terra Vina in August this year and will feature a 60 seat bistro. Paramount Hotels, whose properties include the Lygon Arms in Broadway, is investing in a major refurbishment of its 20 strong, 4 star hotel portfolio. All 2,700 rooms are due for an update.

Overall room rate growth reached 3.7 per cent in 2006 and with occupancy gains of 1.6 per cent, gave an overall RevPAR gain of 5.3 per cent. Our revised forecast expects further RevPAR growth of 5.6 per cent this year and 5.5 per cent in 2008 taking RevPAR levels to £50.59 and £53.39 in these years. This growth is largely driven by room rate gains of 4.2 per cent and 4.4 per cent. Occupancies are likely to remain in the low 70s with only 1.4 per cent growth in 2007 and 1.1 per cent in 2008, nudging occupancy to 72.86 per cent by 2008. See Table 3 and Graph 5.



Graph 5: Provinces hotel performance 2000 to 2008

Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007, **Macroeconomics Data:** Oxford Economics February 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte February 2007

Table 3: PricewaterhouseCoopers Latest Forecast for Provinces February 2007

	2006R	2007F	2008F
Average Room Rate (£)	67.40	70.21	73.28
% Change	3.7%	4.2%	4.4%
Occupancy (%)	71.09	72.06	72.86
% Change	1.6%	1.4%	1.1%
RevPar (£)	47.91	50.59	53.39
% Change	5.3%	5.6%	5.5%

Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
 Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast

Latest hotel sector forecast for Provinces and other key cities

Edinburgh

Edinburgh helps Scotland celebrate a mini tourism boom

The first nine months of 2006 saw overseas visitors to Scotland increase by 14 per cent – almost double the rate for the UK as a whole. Visitor numbers from Europe were up 13 per cent, with North American visitors up 16 per cent. Reasons for this boom include new direct European and long haul services and a targeted marketing campaign⁶. Scotland's airports also enjoyed a surge in international traffic last year. The number of passengers on international flights to and from Scotland grew to nearly eight million, according to new figures from airport operator BAA Scotland. In 2006, Edinburgh airport handled 8.6 million passengers, a rise of 1.9 per cent on 2005. In December it was Scotland's busiest airport, handling 600,514 passengers, a rise of 0.3 per cent on the previous year. This growth helps explain the strongly performing hotel sector where the Scottish capital's vibrant tourism industry combines with strong corporate demand to support high room rates – the average achieved room rate was just over £79 for 2006 and topped £104 in July. Occupancy rates approached or exceeded 90 per cent in five months of last year.

Table 4: PricewaterhouseCoopers Latest Forecast for Edinburgh February 2007

	2006R	2007F	2008F
Average Room Rate (£)	79.41	82.74	86.43
% Change	4.4%	4.2%	4.5%
Occupancy (%)	79.13	79.63	80.06
% Change	2.6%	0.6%	1.0%
RevPar (£)	62.83	65.89	69.20
% Change	7.0%	4.9%	5.0%

Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
 Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast.

The quality of hotels may also help explain their success. According to TripAdvisor's Travellers Choice Awards, four out of ten of Europe's best B&Bs are in Scotland, while the luxury Howard Hotel is in the top 25 world city hotels.⁷ In another award, seven of Edinburgh's boutique hotels, including the Malmaison, Le Monde, the Prestonfield, the Borough and the Glasshouse, have been short listed for 'sexiest hotel' in Scotland.

Our forecast expects average room rates to grow by 4.2 per cent this year, rising to 4.5 per cent in 2008 and taking rates to £82.74 and £86.43 respectively. Occupancies are expected to grow by only 0.6 per cent this year, taking

occupancy levels to almost 80 per cent and with hotels almost at capacity with a little more movement is anticipated in 2008. These growth levels are expected to lift RevPAR by 4.9 per cent and 5.0 per cent in 2007 and 2008 respectively. See Table 4 and Graph 6.

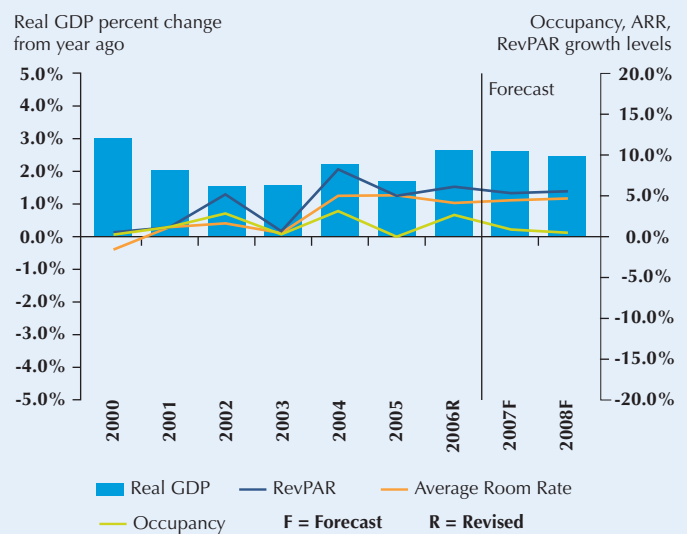
Could a tourism tax put the brakes on?

Plans that could see local councils being given the power to impose a tourism levy independent of central administration have been criticised by the Scottish Tourism Forum (STF). The criticism comes against the background of the independent Scottish Local Government Finance Review Committee backing Edinburgh City Council's recommendation that the Scottish Executive should give local authorities power to apply a discretionary tourism tax. Considerable controversy already surrounds bed tax proposals in the UK and writing recently about this John Whiting, tax partner at PricewaterhouseCoopers has commented:

"There has been speculation that the industry might see an introduction of a 'bed tax' within the UK. That would seem to be a unfortunate move if it did occur as...the hotel industry already pays a substantial amount of tax."

John Whiting, tax partner, PricewaterhouseCoopers 2007

Graph 6: Edinburgh hotel performance 2000 to 2008
 Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007,
Macroeconomics Data: Oxford Economics February 2007,
Benchmarking Data: Hotel Benchmark TM Survey by Deloitte February 2007

⁶ Leisure Opportunities 26 January- 5 February 2007
⁷ The Scotsman 18 January 2007

No more oversupply problems for Manchester ?

The city has a strong events industry which will be further strengthened by the Labour Party's announcement of its intention to hold its annual conferences in Manchester in both 2008 and 2010. Their conference in the city last year is reported to have attracted 17,000 delegates and an estimated £15m in economic benefits. Their decision mirrors the Tory Party's recent announcement that they will hold two future conferences in Birmingham in the same years.

On a longer time horizon, the unexpected decision of the Casino Advisory Panel that Manchester should be the location for the UK's first regional or 'super' casino, is likely to further drive hotel demand in Manchester and help absorb both recent and future increases in supply. However, with a challenge to this decision expected from supporters of other potential locations and a lengthy tendering process likely if Manchester is successful, this boost to the sector is some years away.

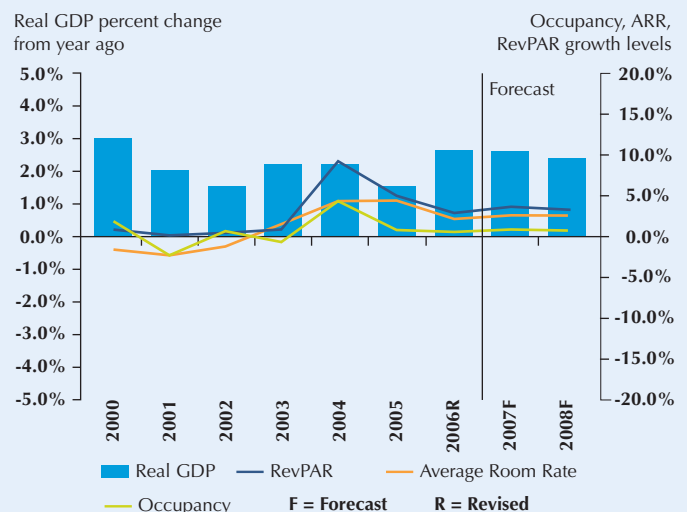
Despite room rates falling in several months of 2006, the city saw a strong rally towards the end of the year. In September room rates reached over £75 and occupancies just over 82 per cent. Overall, Manchester saw RevPAR gains of 3.8 per cent in 2006. Whether this means the City's oversupply worries are a thing of the past remains to be seen. According to research by Jones Lang LaSalle Hotels, the number of hotel beds in the city is now close to 8,000, with supply growing by six per cent and plans for a further 1,291 new rooms over the next few years. New openings include a 215 room Macdonald Hotel near Piccadilly Station due to open at the end of this year and a 228 room Crowne Plaza hotel in the mixed-use scheme at Smithfield, due to open in July 2008. A new 75-bed Sleeperz hotel is to be built on land owned by Network Rail opposite Piccadilly station.

We expect RevPAR gains of 4.1 per cent this year and a further 3.4 per cent in 2008, taking RevPAR to £55.15, driven primarily by room rate growth of three per cent and 2.7 per cent in 2007 and 2008 respectively. See Table 5 and Graph 7.



Graph 7: Manchester hotel performance 2000 to 2008

Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007, **Macroeconomics Data:** Oxford Economics February 2007, **Benchmarking Data:** Hotel Benchmark TM Survey by Deloitte February 2007

Table: 5 PricewaterhouseCoopers Latest Forecast for Manchester February 2007

	2006R	2007F	2008F
Average Room Rate (£)	68.96	71.03	72.98
% Change	2.8%	3.0%	2.7%
Occupancy (%)	74.27	75.10	75.57
% Change	1.0%	1.1%	0.6%
RevPar (£)	51.22	53.34	55.15
% Change	3.8%	4.1%	3.4%

Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
 Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast.

Birmingham

Birmingham's renaissance continues

A new survey shows that expenditure by visitors to events and conferences in Birmingham generates around £1bn on accommodation, £424 million on food and drink, £307 million on shopping, £266 million on travel, £240 million on entertainment and £211 million other expenditure. Reinforcing this position, the City's visitor economy saw a good start to the year, with the Tory Party agreeing to hold two future annual conferences there, in 2008 and 2010. There has been speculation that the events could be worth £40 million to the city. In addition, Birmingham City Council agreed in October 2006 to increase Marketing Birmingham's funding by £2 million per annum from 2008/09 to allow it to create a new subvention fund for conferences and events.

The rejuvenation of Birmingham will help to attract more visitors. The Grade 1 listed Town Hall will reopen after a £35 million refurbishment, providing a new city centre venue for music, political debate and corporate events later this year. In 2009 the Cube opens. This development has residential apartments, state of the art offices, exclusive shops, waterside café bars, a boutique hotel and a panoramic rooftop restaurant. In addition, a new large casino has now been confirmed at the NEC and Fort Dunlop, the old tyre factory reopened its doors as a retail centre towards the end of 2006. In 2007 Birmingham hosts one of Europe's leading sporting events, the European Athletics Indoor Championships at the National Indoor Arena.

On the hotel scene, the city has attracted some stylish new hotels in recent years including the Radisson SAS in the Beetham Tower. The Regency Hyatt recently added the new £1 million Amala Spa and Club. At the budget end the first of Accor's Etap chain opened in Birmingham last year and Travelodge is investing £11 million in Birmingham, including opening two new hotels in Birmingham earlier last year at Fort Dunlop and Walsall and a £200,000 refurbishment of their first city centre hotel located on Broad Street.

Last year hotels in Birmingham generated RevPAR of £46.39, a 4.4 per cent gain on the previous year, driven by occupancy growth of 1.6 per cent and 2.8 per cent room rate gains. Birmingham's room rates reached almost £79 in April but for the year averaged around £67. This was lower than we anticipated in our previous forecast reflecting lower than anticipated occupancy growth.

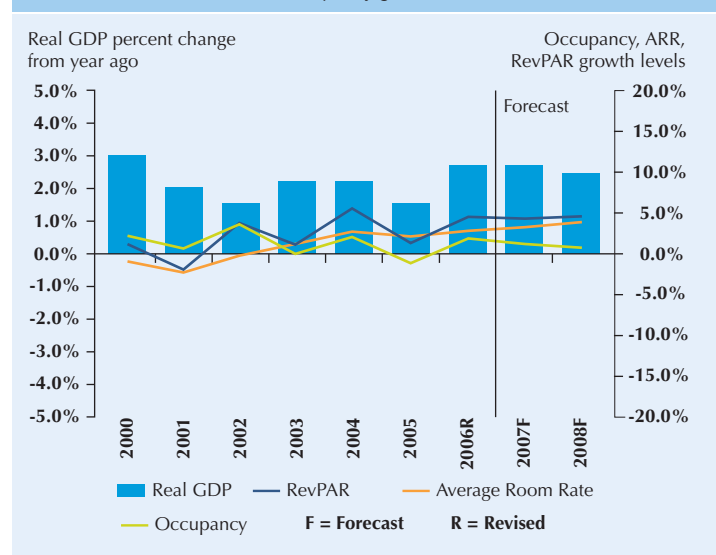
Our latest forecast is for continued growth, with 3.9 per cent RevPAR growth this year, driven by occupancy and room rate gains of 1.0 per cent and 2.8 per cent respectively. RevPAR growth is expected to rise slightly further to 4.2 per cent in 2008, as occupancy growth slows but room rates improve marginally. PricewaterhouseCoopers research shows that even years are traditionally stronger than odd years in terms of exhibitions and major conference events and this may help hotels closer to the NEC. See Table 6 and Graph 8.

Table 6: PricewaterhouseCoopers Latest Forecast for Birmingham February 2007

	2006	2007F	2008F
Average Room Rate (£)	67.32	69.23	71.47
% Change	2.8%	2.8%	3.2%
Occupancy (%)	68.92	69.63	70.28
% Change	1.6%	1.0%	0.9%
RevPar (£)	46.39	48.20	50.22
% Change	4.4%	3.9%	4.2%

Source: **Econometric Forecasts:** PricewaterhouseCoopers Forecasting Model, February 2007
Note: Historic data are from Hotel Benchmark TM Survey by Deloitte. R=Revised. F=Forecast.

Graph 8: Birmingham hotel performance 2000 to 2008
 Real GDP, revenue per available room, average room rate and occupancy growth rates



Source: **Econometric Forecasts:** PricewaterhouseCoopers February 2007,
Macroeconomics Data: Oxford Economics February 2007,
Benchmarking Data: Hotel Benchmark TM Survey by Deloitte February 2007

Appendix 1

The key forecast drivers include strong economic growth and continued travel growth

Macroeconomic outlook: Another year of robust growth in 2007, although consumers are expected to go in for some 'belt tightening'

The UK is expected to be the best performing economy in the G7 this year, with GDP growing by 2.7 per cent, the same rate as in 2006. This rate will exceed growth in the US (2.6 per cent), Eurozone (2.3 per cent) and Japan (2.0 per cent), according to Oxford Economics.⁸ Expansion in the service sector continues at pace and is expected to underpin another year of robust growth in 2007. Beyond this year, GDP growth is expected to dip slightly in 2008, to 2.5 per cent before accelerating to three per cent by 2009.

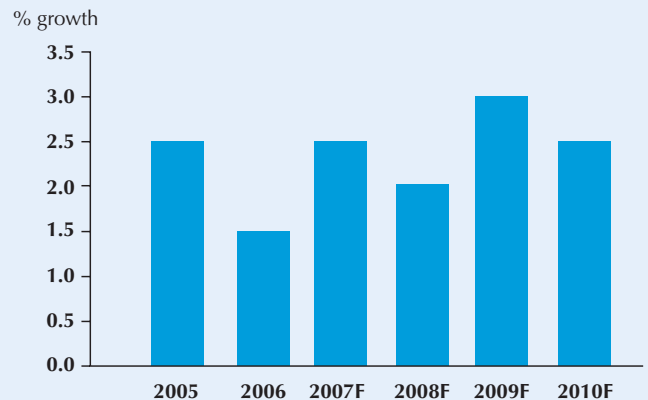
Macroeconomic Data for the UK					
	2005R	2006R	2007F	2008F	2009F
Real GDP per cent change from prior year	1.9	2.7	2.7	2.5	3.0
Consumer prices per cent change from prior year (CPI)	2.0	2.3	2.4	2.0	2.0

Source: Oxford Economic Forecasting February 2007. R=Revised. F=Forecast.

The UK is benefiting from a buoyant global financial services market and high corporate cash flows are supporting a strong recovery in business investment – boosting the London economy in particular. Despite higher interest rates, business surveys suggest that prospects for investment remain positive this year and support economic growth.

For consumer facing businesses there have been mixed messages. Consumer spending is expected to remain cautious in 2007. Reports of buoyant retail Christmas trading suggest that consumer spending rebounded in Q4. This impetus could be short lived though, because rising debt service costs and higher utility bills could force households to reassess their spending plans and adopt more cautious spending patterns, in the light of growing

Changes in real UK households' disposable income*



* Oxford Economics 2007. Years beginning Q1

Source: OEF 2007

constraints on disposable incomes. Marks & Spencer Chief Executive, Stuart Rose, recently warned that he expects consumers to be more stretched financially in 2007 and for the sector to see probable belt-tightening by consumers.⁹ UK household debt is another area for concern and is reported to be rising from around 100 per cent of disposable income in 1997 to around 160 per cent in 2006. Interest rates have been raised three times in six months and as the Economist commented "At some point the consumer is bound to stumble."¹⁰ However, although growth in consumer spending is forecast to remain subdued by past standards, at 2.2 per cent in 2007 this is still higher than 1.9 per cent growth in 2006. Moreover, in the recent past, holidays have proved resilient to household budget cuts.

The appreciation of sterling, particularly against the dollar where it recently hit a 14-year high, and is now considered set to breach the \$2.00 level, is reported to be causing problems for many UK manufacturing firms and for tourism businesses where high prices undermine the competitiveness of the UK against other, often cheaper competitor destinations. On a positive note as the Euro continues to strengthen against the Pound the UK should maintain high growth in visitor numbers from Europe.¹¹

8 Oxford Economics, UK Outlook, January 18 2006

9 Financial Times 10 January 2007

10 A special report on Britain, Economist, 3 February 2007

11 Sterling Strength No Immediate Threat To UK Economy, DOW JONES NEWSWIRES 23 January 2007

Appendix 1

(continued)

Travel drivers robust

Solid global travel growth

Latest figures from the UN World Tourism Organization show there were a record 842m international tourist arrivals worldwide last year, 4.5 per cent more than in 2005.

2006 was another year of good growth above the long-term forecast rate of 4.1 per cent, backed up by one of the longest periods of sustained economic expansion according to the UNWTO. This was despite downside risks facing global tourism 12 months ago – in particular terrorism, health scares due to avian flu and rising oil prices.

Looking ahead to 2007, UNWTO projects the year-on-year rise in international tourist arrivals to be about four per cent, in line with its long-term annual growth forecast of 4.2 per cent over the next 10 years.

Business travel is also on the increase

According to the 11th annual Business Travel Survey of 4,000 travelling UK executives by Barclaycard, 44 per cent of those surveyed travelled more on business last year than in 2005, with a further 34 per cent travelling the same amount. Of the 44 per cent who had travelled more, 47 per cent cited business expansion either in the UK or abroad as the reason for doing so. Of those surveyed 73 per cent travelled to the UK and Ireland most often last year, although this was down from 75 per cent in 2005. The research also found that people still believe that travel is an essential part of their business, with 79 per cent believing their business had benefited from business travel.¹²

...with more than 32m international visits to UK in 2006, an increase of seven per cent

Visits by overseas residents to the UK rose by seven per cent in 2006, from 30 million to 32 million. Visits by residents of Western Europe rose seven per cent to 20.6 million, while visits from North America were up six per cent to 4.5 million. Other parts of the world saw an increase of nine per cent to 7.1 million, according to National Statistics.¹³

However, Tom Wright, VisitBritain chief executive, said that the level of visitors from North America has yet to fully recover to its all-time high of 2000.

'This year we plan to launch a long-term campaign to present Britain in a dynamic light'

Tom Wright, Chief Executive, VisitBritain

Will the domestic market benefit from calls to holiday at home?

Domestic short breaks are robust, according to VisitBritain, and in 2005 Britons took 59.3 million holidays of one or more nights in England. Early figures from domestic tour operators say sales through agents are continuing to grow after the hot summer in 2006.¹⁴ There are hopes that domestic tourism may benefit from environmental calls to holiday in Britain and not fly abroad. VisitBritain CEO Tom Wright has even asked ABTA to consider holding its Convention in the UK this year.

...but issues such as APD may hurt some markets

It remains to be seen whether the controversial 'green' increase in Air Passenger Duty (APD) which came into force on 1 February this year, will depress domestic and international air travel. APD has been increased from £5 to £10 for economy seat passengers on domestic and European short-haul flights, and from £20 to £40 for economy seat travellers on long-haul flights. Many believe there could be a significant effect upon inbound travellers.

'The increase in APD is yet another factor that weakens our international competitiveness and deters visitors from travelling to this country'

Stephen Dowd, Chief Executive, UKinbound

And now a select committee will look at the impact of taxes on UK tourism

The impact of the 'bed tax' (a number of options under consideration by a review of local finances being led by Sir Michael Lyons) and higher flight taxes on the British tourist industry are to be investigated by MPs. An inquiry by the culture, media and sport select committee will also look at how cheap flights abroad are hitting traditional resorts in the UK.

¹² Travel Mole 6 February 2007

¹³ National Statistics News Release 7 February 2007

¹⁴ Travel Weekly 19 January 2007 'Hopes are high for repeat home performance in 2007'

Appendix 2

PricewaterhouseCoopers February 2007 Forecast Hotel Statistics for UK, London, Provinces, Edinburgh, Manchester and Birmingham 2002-2008

Hotel Statistics for the UK	2002	2003	2004	2005	2006R	2007F	2008F
Average Room Rate (£)	71.36	70.35	73.97	77.20	82.11	85.78	89.72
% Change	-3.4%	-1.4%	5.2%	4.4%	6.4%	4.5%	4.6%
Occupancy (%)	70.08	69.65	71.76	71.56	74.05	74.49	75.53
% Change	0.2%	-0.6%	3.0%	-0.3%	3.5%	1.0%	1.0%
RevPAR (£)	50.01	49.00	53.08	55.24	60.80	64.16	67.77
% Change	-3.2%	-2.0%	8.3%	4.1%	10.1%	5.5%	5.6%
Hotel Statistics for London	2002	2003	2004	2005	2006	2007F	2008F
Average Room Rate (£)	98.58	96.41	102.64	106.79	116.06	121.88	127.97
% Change	-8.6%	-2.2%	6.5%	4.0%	8.7%	5.0%	5.0%
Occupancy (%)	74.77	73.09	77.06	75.74	82.13	82.42	83.04
% Change	2.0%	-2.2%	5.4%	-1.7%	8.4%	0.4%	0.7%
RevPAR (£)	73.71	70.46	79.09	80.88	95.32	100.45	106.27
% Change	-6.8%	-4.4%	12.3%	2.3%	17.8%	5.4%	5.8%
Hotel Statistics for the Provinces	2002	2003	2004	2005	2006	2007F	2008F
Average Room Rate (£)	60.10	59.40	62.28	65.00	67.40	70.21	73.28
% Change	-0.6%	-0.3%	3.9%	4.4%	3.7%	4.2%	4.4%
Occupancy (%)	68.38	68.40	69.81	69.98	71.09	72.06	72.86
% Change	-0.5%	0.0%	2.1%	0.3%	1.6%	1.4%	1.1%
RevPAR (£)	41.10	41.00	43.47	45.49	47.91	50.59	53.39
% Change	-1.1%	-0.2%	6.0%	4.6%	5.3%	5.6%	5.5%
Hotel Statistics for Edinburgh	2002	2003	2004	2005	2006	2007F	2008F
Average Room Rate (£)	67.91	68.41	71.98	76.08	79.41	82.74	86.40
% Change	1.6%	0.7%	5.2%	5.7%	4.4%	4.2%	4.5%
Occupancy (%)	74.14	74.84	77.23	77.16	79.13	79.63	80.06
% Change	3.2%	0.9%	3.2%	-0.1%	2.6%	0.6%	0.5%
RevPAR (£)	50.35	51.19	55.58	58.70	62.83	65.89	69.20
% Change	4.9%	1.7%	8.6%	5.6%	7.0%	4.9%	5.0%
Hotel Statistics for Birmingham	2002	2003	2004	2005	2006	2007F	2008F
Average Room Rate (£)	60.83	61.67	63.80	65.48	67.32	69.23	71.47
% Change	-0.8%	1.4%	3.5%	2.6%	2.8%	2.8%	3.2%
Occupancy (%)	67.19	66.97	68.69	67.84	68.92	69.63	70.28
% Change	3.6%	-0.3%	2.6%	-1.2%	1.6%	1.0%	0.9%
RevPAR (£)	40.88	41.30	43.82	44.42	46.39	48.20	50.22
% Change	2.8%	1.0%	6.1%	1.4%	4.4%	3.9%	4.2%
Hotel Statistics for Manchester	2002	2003	2004	2005R	2006	2007F	2008F
Average Room Rate (£)	60.29	61.42	64.05	67.09	68.98	71.03	72.98
% Change	0.0%	1.9%	4.3%	4.7%	2.8%	3.0%	2.7%
Occupancy (%)	70.11	69.60	72.86	73.55	74.27	75.10	75.57
% Change	0.5%	-0.7%	4.7%	1.0%	1.0%	1.1%	0.6%
RevPAR (£)	42.27	42.75	46.66	49.34	51.22	53.34	55.15
Change	0.4%	1.1%	9.1%	5.8%	3.8%	4.1%	3.4%

Source of Forecast: PricewaterhouseCoopers Forecasting Model, February 2007 Note: Historic data are from HotelBenchmark™ Survey by Deloitte.



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