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Introduction

HVS has been in the forefront of providing strategic advisory for virtually every major industry participant for the past 11 years. Having reviewed the market performance for over a decade, it has been particularly interesting to observe and draw statistical co-relation on benchmark performances, market segments and demographic customer profiles for the industry over the long-term horizon. This eleventh edition of HVS's *Hotels in India - Trends and Opportunities* publication provides us with a unique opportunity to understand industry dynamics through twelve years of performance trends representing periods of peaks and troughs.

The article also assesses current trends and presents our views on

future opportunities for the hotel industry across key markets in India. As always, apart from conducting specific research for this publication, we have included macro data provided by the Department of Tourism. The publication briefly discusses the tourism industry in India in the context of the present economic scenario and presents the results of our survey on the performance of mostly branded hotels, analysed by each segment of the hotel market, as well as by major cities.

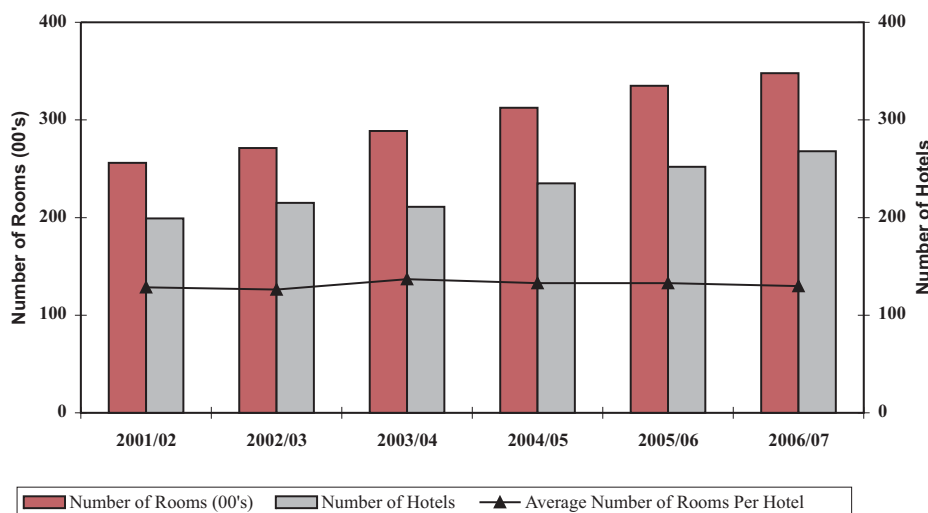
The hospitality boom in India is led not only by the buoyancy in the Indian economy, but also by the supply-demand imbalance that currently exists in most cities. Therefore, in the 2007 edition we have focused extensively on the quantum and classification of new hotels being

developed in major cities over the next five years. For each city we have presented the number of new hotels under various stages of development, their market orientation and suggested the active development ratio. As in previous editions of this report, we have, once again, presented our assessment of industry trends and development opportunities; this is included as part of the 'Future Trends' section. Detailed analysis of new hotel supply has allowed us to predict the kind of man-power requirements the country needs to just match up to the expected growth.

In addition to this document, we publish *The Indian Hotel Industry Survey* on an annual basis, in association with the Federation of Hotel & Restaurant Associations of India (FHRAI). This publication, the only one of its kind in India, provides detailed financial and operating information on the hotel industry, analysed by star category, across all major cities in the country. The next edition (2006/07) will be available by the end of the year.

This year, a record 268 hotels with a total of 34,784 rooms, participated in our survey. Table 1 illustrates survey participation for the years 2001/02 to 2006/07.

Table 1: Number of Respondents



The Indian Economy - An Overview

Rapid growth and strong macro-economic fundamentals have characterised developments in the Indian economy in the past financial year. GDP is estimated to have grown at a robust 9.4% during 2006/07 as against 9.0% in 2005/06. The only time the economy has grown faster was in 1988/89. This acceleration in growth rates was led by Industrial and Services sector activities, which exhibited double-digit growth. Increase in tourist arrivals and visits, augmentation of telecommunication services, escalated development in Information Technology (IT) & IT enabled Services (ITeS) and improvement in the financial services sector has kept the Services sector buoyant in recent years. Maintaining the trend highlighted last year, this sector continues to be a major demand generator for room nights in most of the primary cities and increasingly in the secondary cities of India. The impact on travel expenditure budgets by the IT sector due to recent pressures on margins owing to rupee appreciation is also likely to influence demand in the short to medium term.

Growth in Agriculture and Allied activities decelerated from 6.0% in 2005/06 to 2.7% in 2006/07 resulting in its declining share in the overall GDP of the country. This was attributed to uneven rainfall, low investment, imbalance in fertilizer use, distorted incentive system and low post-harvest value addition. As this sector still employs a substantial section of the

population and plays an important role in the Indian economy, volatility in agricultural production has serious implications for the country's overall growth as witnessed with regards to inflation in the last financial year.

The industrial sector, improving consistently over the last five years, grew at 11.1% in 2006/07 propelled by the robust growth of the Manufacturing sub-sector (12.3% in 2006/07). According to the *Economic Survey 2006/07*, Industry had never consistently grown at over 7.0% per year for more than three years in a row before 2004/05. This sustained growth has led to increased investments and efficiency in utilization of capital. It is believed that the Industrial sector would have performed better had the Mining and Quarrying sub-sector achieved higher growth. Electricity, Gas and Water supply grew by 7.2% in 2006/07 as against 5.3% in 2005/06. The Construction sector, though a major propeller of GDP, showed a decline as compared to last year because of rising interest rates.

The Services sector showed a healthy growth of 11.2% in 2006/07 as compared to 9.8% in 2005/06 benefiting from the availability of skilled labour. Trade, Hotels, Transport and Communication continued to develop at an accelerated pace recording a growth of 13.0% during 2006/07 as against 10.4% in 2005/06. Community, Social and Personal Services continued to expand at 7.8% in 2006/07 showing marginal increase over the previous financial year. Financial, Insurance, Real Estate and

Business Services witnessed a slowdown, growing by 10.6% in 2006/07 as compared to 10.9% recorded in 2005/06, as per independent sources.

The inflation rate at the beginning of 2006/07 stood at 3.9% with an upward trend through the year ending at 6.9% in March 2007. Inflationary pressures may be attributed to both demand and supply trends. According to the Reserve Bank of India (RBI), demand pressures stemmed from elevated asset prices and high investment and consumption demand, while supply side pressures emanated from low domestic production of major food grains amidst rising global prices. Using the various instruments at its disposal, the RBI has tried to contain the inflation in this financial year effectively and aims at containing it at below 5.0%.

Furthermore, 2006/07 saw the Indian rupee gaining strongly against the US dollar. The Indian rupee stood at 44.9 to the US dollar in April 2006, after which it gained strength and touched 43.1 by March 2007 averaging to 43.6 for the previous financial year. We expect the currency to remain strong in the short term as it is being driven by capital flows and strong demand for exports. To substantiate the above, the Indian rupee has remained on an upward trajectory ranging between 39.0 and 41.0 against the US dollar in 2007/08.

Going forward, this financial year has witnessed the adoption of a single currency system by hoteliers across the country due

to the weakening of the dollar against the rupee. It is believed that there is more value for money earned in rupees resulting in a decision to price hotel services in rupees. Foreign customers however, are given the option to settle their bills in an international currency.

A well-performing global economy has provided an environment within the country, which is conducive to development. Purely for monetary policy purposes, the RBI - in its Annual Statement in April 2007 - has positioned the real GDP growth for the current financial year at around 8.5% exclusive of any significant internal or external developments.

The Congress-led United Progressive Alliance (UPA) has completed three years in office as of May 2007. The coalition introduced the Common Minimum Programme that focused on the economic growth and development of the masses and provision of basic necessities to all. However, differences in perspective during the tenure of the government, with regard to economic, social, and foreign policy issues among the parties of the alliance have been hindrances. Frequent disrupting of functioning of parliament has also been a problem. Nevertheless, India has seen a continuity of reforms over a decade and irrespective of varied ideological dispositions, this trend is expected to continue unimpeded.

According to a report by the *Confederation of Indian Industries (CII) 2006/07*, though India has

been lagging behind the world in promoting exports through Special Economic Zones (SEZs), it is slowly catching up owing to the considerable change in the government's outlook and policies towards SEZs. The SEZ Act 2005 along with the two amendments (August 2006 and March 2007) has led to certain regulations being done away with and the process of starting a business has been simplified by bringing in the single window clearance policy. The policy allows 100% FDI in most manufacturing activities and the government is also looking at removing sectoral FDI caps in all sectors for units located in SEZs. Most of the SEZs in the country are presently located in the south followed by west, north, east and central India.

Airport Infrastructure Overview

The total air passenger traffic in India has shown an increase of 31.4% in 2006/07 as compared to that handled in 2005/06. The main reason for higher growth in traffic is due to the contribution of low-cost airlines. With more players entering this segment and the ongoing consolidation, the outlook for the Aviation sector is positive. Jet Airways, after acquiring Air Sahara in April 2007, has repositioned the latter as a niche player between low-cost and full-service airlines, under the new brand name JetLite. Furthermore, Kingfisher Airlines has taken up a stake in Air Deccan and the alliance intends to create an independent company where charter operations - a fast-emerging segment with high potential - of both the companies will be

merged. Kingfisher Airlines also aims at using this ally to fly abroad in case the government does not relax the five-year domestic operation norm for Indian carriers.

Low fare airlines, namely, Air Deccan, SpiceJet and GoAir and other existing airlines have increased their frequency of operations in the existing domestic sectors and started flights to new sectors also. New low fare airlines namely IndiGo and Indus Air have also started operations in 2006/07. Cumulatively, all the players in this sector have contributed significantly towards domestic air passenger traffic showing an increase by 38.5% in 2006/07 as compared to 2005/06. International passenger traffic registered an increase of 15.1% in the same period. Private airlines accounted for 80.7% of the total domestic traffic with low fare airlines accounting for 29.7%.

To substantiate the emphasis on the development of airports in secondary cities and expansion of existing airports across the country, an estimated investment of Rs47,000 crore for modernisation is expected over the next five years. The increase in the levels of passenger and cargo traffic has placed a heavy strain on the airports especially in New Delhi, Mumbai, Kolkata, Chennai and Bangalore. It has highlighted the need for substantial investment to develop and expand the existing facilities. In order to meet the increased demand, the current government has brought in private sector assistance to invest in, and develop airports. The GVK led

Table 2: Key Tourism Statistics

	2001	2002	2003	2004	2005	2006	2007*
Number of Arrivals	2,537,000	2,360,000	2,726,000	3,406,623	3,918,610	4,429,915	4,917,206
Foreign Exchange Earnings (US\$ billion)	\$3.04	\$2.96	\$3.60	\$4.81	\$5.73	\$6.60	\$7.70
Foreign Exchange Earnings Per Visitor	\$1,198	\$1,254	\$1,321	\$1,412	\$1,462	\$1,490	\$1,566
Total Arrivals to New Delhi	33.7%	28.6%	30.8%	32.2%	31.9%	31.0%	30.1%
Total Arrivals to Mumbai	26.7%	25.4%	24.1%	25.1%	24.4%	23.5%	22.9%
Total Arrivals to Chennai	12.0%	11.5%	10.5%	10.3%	9.9%	9.3%	8.9%
Total Arrivals to Kolkata	4.3%	3.8%	3.7%	3.3%	3.0%	2.8%	2.7%
Total Arrivals to Bangalore				4.1%	4.2%	4.2%	3.9%
Total Arrivals to Goa				4.1%	4.3%	4.4%	4.3%
Total Arrivals to Hyderabad				-	1.3%	1.4%	1.4%
Exchange Rate US\$1.00:Rs	47.20	48.20	46.00	44.90	44.50	43.60	40.50

* Note: All figures for 2007 and all exchange rates (weighted for the year) are HVS Estimates

Source: Ministry of Tourism and HVS Estimates

consortium for Mumbai airport plans to include a second runway, a new cargo facility and a new terminal for both international and domestic flights by 2010. The New Delhi airport is expected to have an interim terminal that will be ready by 2008 to ease out traffic until the third terminal comes up by 2010.

Greenfield airports are being constructed in Devanahalli near Bangalore and Shamshabad near Hyderabad, which are expected to be operational by April 2008 and March 2008 respectively. The modernisation process at Kolkata is already in progress while the Chennai airport has recently been sanctioned, along with plans for the announcement of a Greenfield airport.

Table 2 reflects key statistics for the Indian tourism industry.

Trends & Developments in Tourism

The tourism industry in India, despite being an important component of the economy, contributed only 5.9% of the GDP in 2006/07. According to estimates of the World Travel & Trade Council (WTTC), Indian tourism demand will grow at

8.8% from 2004-13, which would place India as the third-most rapidly growing tourism market in the world after Montenegro and China. It would further result in a growth of 7.1% in total travel and tourism GDP. A longer term, sustained growth of the industry depends on how successfully several issues are addressed – relating to old and poorly facilitated airports, inadequate hotels, poor road and transport infrastructure, high levels of taxation and a bureaucratic visa processing system. The budget has proposed an outlay of approximately Rs570 crore for development of tourism infrastructure in 2007/08, up from Rs423 crore proposed in the corresponding period of 2006/07.

Foreign Tourist arrivals in India have been showing an increasing trend, estimated at 4.43 million in 2006, up 13.0% from 2005 (3.94 million). The current government, it appears, is taking active interest in developing tourism in India. The continued 'Incredible India' campaign has had a strongly positive impact on tourist arrivals. Definite efforts are being made to communicate the 'Brand India' message by penetrating the global market and reaching the ultimate

consumer through electronic, print and internet media.

Highlighting the progress in this regard, India has been ranked number one in top travel destinations of the world according to this year's Readers Travel Awards announced by *Condé Nast Traveler*, UK. Moreover, the Incredible India campaign has been ranked as the 'Highest Recall Advertisement' worldwide by *Travel and Leisure*.

While a lot of attention is given to international tourist trends, the true potential of tourism within India can be leveraged by tapping the domestic leisure segment, which is currently estimated at 250 million travelers. According to our estimates, as India gets younger and richer, there will be sustained demand for short duration travel at major gateway destinations and these markets will grow exponentially in the next three to five years. With sustained economic performance, India's Per Capita Income will also continue to witness growth. Moreover, higher disposable income rather than lower savings has influenced the present-day consumption boom in India. This is good news, as income induced spending is

likely to sustain itself for a longer period and higher disposable incomes are also expected to enhance the concept of traveling for leisure thus providing the necessary impetus to destination travel within integrated travel circuits.

In most markets, insufficient room availability and high rates create conditions that are not conducive for large incentive based group travel. Logistical bottlenecks and lack of appropriate infrastructure in these markets also pose a problem. Various state governments in India have expressed keen interest in tourism infrastructure developments.

The economy's buoyancy, initiatives to improve infrastructure, the boom in aviation and real estate, easing of restrictions on foreign investment and, perhaps, most importantly, efforts to communicate the Brand India message – will continue to fuel demand for hotels across star categories in the majority of leisure markets. India's hotel industry is increasingly being viewed as investment-worthy, both within the country and outside. Niche markets such as medical tourism, culture tourism, the Great Indian Temple circuit, ayurveda and yoga, and adventure tourism, will grow rapidly.

Tourism has rapidly emerged as a significant segment of the Indian economy. With active government participation, higher disposable incomes of the population, better positioning of India as an international tourist destination and synergized efforts of all industries towards it, the outlook for tourism in India continues to remain buoyant in the long term.

Survey Results

The HVS survey has been computed by dividing the respondent hotels into their respective classifications according to star category. As before, we have examined the performance of ten major cities across India, wherever a reasonable sample allowed. While most of the data provided to us is in Indian rupees, we have presented survey results in US dollars as well.

Ten years ago, the four metro cities of Mumbai, Delhi, Chennai and Kolkata were the top four market performers, respectively, in terms of Revenue Per Available Room (RevPAR). In 2007, Mumbai has fallen to 3rd spot, Delhi retains its 2nd spot, while Chennai and Kolkata are 6th and 7th respectively.

Recent developments within the industry, backed with a positive outlook for the economy, have resulted in accelerated growth in demand for hotel accommodation over the last two years. The continued demand-supply imbalance has led to exponential rate increases resulting in inflated room rates across key markets in the country, some of which currently rank among the most expensive hotel markets in the world. Over the long term, inflated room rates are expected to have a severe negative effect on the potential demand, especially for Leisure destinations. Our research indicates that the effects of spiraling rates have already been noticed in most markets. For the first time in four years markets have started showing a decline in occupancy. Average rates, on the other hand, showed even a higher

growth than in previous years across these very cities.

This trend resembles the period starting 1996-97 where occupancies had started to decline but average rates continued to rise for a few years thereafter. However, much has changed during the past decade. Today India is in the 'must have' list of the international investment community and there appears to be genuine interest in the country from foreign investors. Mainly Indian companies and businessmen lead the demand boom. The economy is witnessing exciting growth across most sectors and there is a huge demand-supply gap that has formed.

The demand supply gap has clearly benefited the existing hoteliers who have hiked their rates across market segments. However, we now notice that it's beginning to take its toll on the potential demand growth in some of the cities. The high rates have also resulted in the emergence of an unregulated and unorganised hotel / guesthouse sector that is witnessing a boom in cities like Bangalore, Delhi and Pune. The rapid development of standalone hotels is resulting in a parallel supply of rooms in each of these markets, resulting in softening of occupancy performance. For the 2007/08 period, key markets such as Bangalore, Chennai, Delhi and Hyderabad have all seen a decline in absolute occupancy despite year-on-year growth in annual Rooms Per Day (RPDs). For Bangalore, in fact, it's a second consecutive year of decline in occupancy and increase in average rates. Despite the drop

witnessed in the four major markets, overall occupancies across various star categories rose across India indicating a very healthy hotel market and a confirmation to all of us that the secondary and tertiary markets are indeed doing rather well.

Overall, the industry saw a 12-month growth of 30.0% in average rate (in 2006/07), as opposed to a growth of 23.7% the previous year. Occupancy growth, which had been 2.6% the previous

year, showed a marginal growth of 0.7% (in 2006/07). Table 3 reflects room occupancy by hotel classification for the period 1997/98 to 2006/07. Table 4 presents average rate performance in Indian rupees for the same period while Table 5 reflects average rate results in US dollars.

Average rates in 2006/07 witnessed another increase across all market segments. This is partially attributable to the strong demand: All-India occupancy

touched a record 72.0% mark for the first time. While the year-on-year demand growth from certain segments continued, the overall supply addition has been marginal. Due to the widening gap, hotels over the last 3-4 years have re-aligned their yield management and pricing to increase penetration from high paying customers. Our research indicates that when year round occupancies start touching the 70-75% mark, there is substantial unaccommodated demand in the

Table 3: Key Operating Characteristics by Hotel Classification – Occupancy

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month Growth*	Compounded Growth
Overall Average	57.1%	55.4%	53.9%	57.2%	51.6%	57.2%	64.8%	69.0%	71.5%	72.0%	0.7%	2.6%
Five-star Deluxe	62.0%	60.2%	58.3%	60.9%	52.2%	59.3%	65.0%	71.4%	73.8%	74.0%	0.3%	2.0%
Five-star	58.5%	56.4%	55.7%	56.1%	51.4%	57.0%	66.8%	71.1%	70.4%	71.0%	0.9%	2.2%
Four-star	58.2%	55.9%	53.2%	58.7%	52.7%	56.4%	68.7%	71.8%	72.7%	72.9%	0.3%	2.5%
Three-star	47.0%	48.2%	47.7%	48.8%	49.7%	53.6%	59.6%	56.7%	65.9%	68.1%	3.3%	4.2%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 4: Key Operating Characteristics by Hotel Classification – Average Rate (Indian Rupees)

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month Growth*	Compounded Growth
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.		
Overall Average	3,986	3,903	3,505	3,731	3,467	3,269	3,569	4,299	5,444	7,075	30.0%	6.6%
Five-star Deluxe	5,613	5,572	4,910	5,102	4,668	4,335	4,686	5,606	7,168	9,735	35.8%	6.3%
Five-star	3,315	3,516	3,368	3,447	3,277	3,114	3,372	3,897	4,985	6,536	31.1%	7.8%
Four-star	2,538	2,296	2,168	2,392	2,368	2,246	2,580	3,088	3,847	4,995	29.8%	7.8%
Three-star	1,543	1,457	1,505	1,673	1,696	1,669	1,670	1,830	2,212	2,786	25.9%	6.8%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 5: Key Operating Characteristics by Hotel Classification – Average Rate (US Dollars)

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month Growth*	Compounded Growth
	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$		
Overall Average	109.80	90.24	80.58	83.10	73.45	67.83	77.59	95.73	122.34	162.27	32.6%	4.4%
Five-star Deluxe	154.62	128.14	112.88	113.64	98.90	89.94	101.87	124.86	161.08	223.28	38.6%	4.2%
Five-star	91.31	78.57	77.42	76.77	69.43	65.23	73.31	86.79	112.03	149.91	33.8%	5.7%
Four-star	69.92	61.19	49.97	53.27	50.17	46.59	56.09	68.78	86.45	112.84	30.5%	5.5%
Three-star	42.51	37.03	34.59	37.27	35.93	34.63	36.31	40.71	49.71	63.89	28.5%	4.6%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 6: Key Operating Characteristics by Hotel Classification – RevPAR (Indian Rupees)

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month	Compounded
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Growth*	Growth
Overall Average	2,276	2,162	1,889	2,134	1,789	1,870	2,313	2,966	3,892	5,094	30.9%	9.4%
Five-star Deluxe	3,480	3,354	2,863	3,107	2,437	2,571	3,046	4,003	5,290	7,204	36.2%	8.4%
Five-star	1,939	1,983	1,876	1,934	1,684	1,775	2,252	2,771	3,509	4,641	32.2%	10.2%
Four-star	1,477	1,283	1,153	1,404	1,248	1,267	1,772	2,217	2,797	3,641	30.2%	10.5%
Three-star	725	702	718	816	843	895	995	1,038	1,458	1,897	30.2%	11.3%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 7: Key Operating Characteristics by Hotel Classification – RevPAR (US Dollars)

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month	Compounded
	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	Growth*	Growth
Overall Average	62.70	49.99	43.43	47.53	37.90	38.80	50.28	66.05	87.47	116.83	33.6%	7.2%
Five-star Deluxe	95.86	77.14	65.81	69.21	51.63	53.33	66.22	89.15	118.88	165.23	39.0%	6.2%
Five-star	53.42	44.31	43.12	43.07	35.69	37.18	48.97	61.71	78.87	106.44	35.0%	8.0%
Four-star	40.69	34.21	26.58	31.27	26.44	26.28	38.53	49.38	62.85	82.26	30.9%	8.1%
Three-star	19.98	17.85	16.50	18.19	17.86	18.56	21.64	23.08	32.76	43.51	32.8%	9.0%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

market. Unaccommodated demand is often a form of excess demand resulting from the cyclical nature of the hotel business due to presence of weekday and monthly seasonality.

During this high demand period, many cities were completely sold out on a number of nights, resulting in hotels selling a significant proportion of its inventory on rack rates. For 2006/07, the largest increase in average rates was seen in the Luxury segment followed by the Mid-market and Budget segments.

The highest annual growth, in rupee terms, was witnessed in the five-star deluxe (35.8%) and five-star (31.1%) categories, followed by the four-star category (29.8%). The average rate for three-star properties also showed a healthy increase (25.9%). These growths

were much higher than those witnessed 12 months earlier. It may also be noted that over a ten-year period, the compounded average rate growth in rupee terms has been the strongest in the four-star and five-star category followed by three-star and then five-star deluxe hotels. With the appreciation of the Indian rupee against the US dollar, we see that the growth in dollar terms is even stronger.

As highlighted earlier, despite a drop in occupancy for the four major cities in India, it is indeed remarkable to see an across the board growth in terms of occupancy for the various market segments. This was previously only achieved in 2002/03, post the impact of September 11, 2001. However that was within expectations as the base for all occupancies had been relatively lower. Therefore, last year's

continued marginal growth over a relatively strong base in previous two years is quite an achievement and reflects the strong demand indicators emerging from Tier II markets. The three-star (budget) segment witnessed the highest growth in occupancy at 3.3%. This was followed by the five-star category at 0.9% and the five star-deluxe and four-star at 0.3% each. Table 6 presents RevPAR performance in rupees for the period 1997/98 to 2006/07 and Table 7 presents the same in US dollars.

The emergence of relatively new feeder markets like the growing airline industry and consistent demand from niche segments such as Extended Stay, have resulted in a higher level of base demand that ensures a minimum level of occupancy. This demand has been extremely advantageous

for the hotels as it enabled them to indulge in proactive revenue management, rate contracting and micro-segment planning. However, HVS also believes that the demand from Extended Stay segment is assisting in the mushrooming of the unorganised and guesthouse segments. Today, Bangalore has a base of approximately 2,000 rooms in the unbranded segment, which is higher than branded or quality hotel supply. Each of these establishments are able to charge Rs3,000 to Rs7,000.

In terms of RevPAR, all star categories experienced healthy growth in 2006/07. For the second consecutive year the five-star deluxe hotels experienced the maximum growth in rupee terms (36.2%) followed by five-star hotels (32.2%). The four-star and three-star hotels each saw an increase as well at 30.2%. In US dollar terms the five-star deluxe segment showed the highest increase (39.0%), followed by the five-star (35.0%) and three-star (32.9%) segments.

Table 8 illustrates hotel occupancy for ten key cities in India, between 1997/98 and 2006/07. Tables 9 and 10 show average rates for each of these hotel markets, expressed in Indian rupees and US dollars, respectively. Tables 11 and 12 present the corresponding RevPAR data for each city. In 2006/07, the two Leisure markets of Goa and Agra saw the highest occupancy growth at 8.4% and 4.5% respectively, followed by marginal increases in Mumbai (3.3%), Jaipur and Kolkata (0.9%) and Ahmedabad (0.7%). As stated

earlier, all major cities like Delhi, Bangalore, Hyderabad and Chennai saw declines in occupancy. However, in the previous year (2005/06), Hyderabad and Delhi year logged 80% plus occupancies. Hyderabad saw two new hotels commence operations during this period; Delhi, in fact, saw supply being sucked out of the market due to renovations.

HVS believes that the acute shortage of rooms is increasingly being filled by standalone hotels and a fast growing unorganised serviced apartments segment in not only Delhi and Hyderabad but also in Bangalore, Pune and Chennai. We also believe that the aforementioned cities have limited scope for further growth in occupancy in the immediate future, because of weekend seasonality, which remains relatively weak. The high average rates have started to play a serious deterrent to travelers and the rates often do not match up to service quality levels. The desire to increase bottom lines has also resulted in hotels withdrawing many of the freebies that were being offered until recently.

In terms of average rate (rupee terms), the four major metros - Mumbai, Delhi, Kolkata and Chennai - all overtook the previous years' two growth leaders, Bangalore and Hyderabad. Mumbai topped the charts with a staggering growth rate of 42.6%. This was followed by the cities of Kolkata (38.0%) and Delhi (37.2%). Chennai came

in fourth at 28.8%. The IT cities of Hyderabad and Bangalore witnessed a slower growth at 25.1% and 20.3% respectively. Ahmedabad, Agra, Goa and Jaipur also saw robust growth rates that ranged from 15.4% for Ahmedabad to 21.7% for Goa and Jaipur.

In our 2005 edition of this report, HVS had predicted that average rates would go up by 20-25% for the next three years. In 2005/06, the increase was 23.7% while in 2006/07 it was 30.0%. Though this may have brought short-term gains for the existing players we believe that in the medium to long term this would remain detrimental to the overall growth of tourism and business in India. Also these huge increases in average rates mean that the correction, whenever it happens, will be sharper. While we expect the demand-supply gap to continue for many more years, we still run the risk of chasing business away to the guesthouses and the unorganised sector. We expect certain markets to start seeing earlier than expected corrections on the rate front. These include Bangalore and potentially Pune and Hyderabad in the short term. However most other cities will continue to enjoy another 3-4 years of rate improvement.

Hyderabad, Bangalore and now Goa too, are the three cities that have witnessed the highest growths over a 10-year period (compounded growth) at 15.6%, 13.2% and 10.9%, respectively. In fact a market that has grown remarkably slowly during this

Table 8: Key Operating Characteristics by Major City – Occupancy

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	12-Month Growth*	Compounded Growth
Agra	46.1%	46.4%	40.1%	42.5%	33.7%	30.7%	50.0%	57.1%	56.0%	58.5%	4.5%	2.7%
Ahmedabad	71.8%	58.0%	50.8%	55.8%	53.2%	53.8%	63.2%	68.3%	69.1%	69.6%	0.7%	-0.3%
Bangalore	61.2%	59.0%	64.4%	69.8%	64.3%	72.0%	78.5%	81.4%	76.7%	75.5%	-1.6%	2.4%
Chennai	68.4%	64.7%	65.3%	64.6%	56.5%	58.3%	66.6%	72.9%	78.2%	74.7%	-4.5%	1.0%
Delhi	60.2%	54.1%	52.9%	58.9%	53.3%	60.4%	73.1%	79.1%	80.8%	78.1%	-3.3%	2.9%
Goa	59.2%	58.6%	53.3%	60.6%	53.6%	60.5%	59.3%	62.5%	67.8%	73.5%	8.4%	2.4%
Hyderabad	53.4%	66.0%	61.3%	69.1%	68.0%	68.9%	75.9%	78.7%	82.0%	73.3%	-10.6%	3.6%
Jaipur	51.7%	45.6%	47.0%	55.0%	48.3%	44.9%	58.8%	67.2%	65.7%	66.3%	0.9%	2.8%
Kolkata	61.8%	57.8%	54.8%	62.9%	66.4%	65.4%	62.8%	69.0%	76.4%	77.1%	0.9%	2.5%
Mumbai	65.3%	67.6%	64.5%	64.6%	52.0%	63.4%	69.7%	72.0%	76.2%	78.7%	3.3%	2.1%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 9: Key Operating Characteristics by Major City – Average Rate (Indian Rupees)

	1997/98 Rs.	1998/99 Rs.	1999/00 Rs.	2000/01 Rs.	2001/02 Rs.	2002/03 Rs.	2003/04 Rs.	2004/05 Rs.	2005/06 Rs.	2006/07 Rs.	12-Month Growth*	Compounded Growth
Agra	2,027	1,906	1,638	1,586	1,840	1,954	2,431	3,012	3,622	4,310	19.0%	8.7%
Ahmedabad	1,833	2,220	2,705	2,736	2,354	2,164	2,410	2,787	3,111	3,589	15.4%	7.8%
Bangalore	3,451	3,254	3,025	3,602	3,735	3,752	4,832	7,470	8,762	10,545	20.3%	13.2%
Chennai	3,977	3,600	3,424	3,796	3,535	3,224	3,323	3,714	4,357	5,610	28.8%	3.9%
Delhi	4,913	4,626	4,115	4,526	4,338	4,089	4,269	5,103	6,909	9,482	37.2%	7.6%
Goa	2,303	2,863	2,727	2,914	2,676	2,754	3,086	3,985	4,804	5,846	21.7%	10.9%
Hyderabad	1,646	1,579	1,867	2,316	2,414	2,541	2,774	3,772	4,870	6,091	25.1%	15.6%
Jaipur	2,473	2,533	2,514	2,902	2,949	2,728	2,980	3,461	4,407	5,364	21.7%	9.0%
Kolkata	3,951	3,888	3,557	3,698	3,409	2,917	3,021	3,240	3,887	5,366	38.0%	3.5%
Mumbai	6,169	6,297	5,661	5,555	4,932	4,184	4,356	4,822	6,041	8,614	42.6%	3.8%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 10: Key Operating Characteristics by Major City – Average Rate (US Dollars)

	1997/98 US\$	1998/99 US\$	1999/00 US\$	2000/01 US\$	2001/02 US\$	2002/03 US\$	2003/04 US\$	2004/05 US\$	2005/06 US\$	2006/07 US\$	12-Month Growth*	Compounded Growth
Agra	56	50	38	35	39	41	53	67	81	99	22.2%	6.5%
Ahmedabad	50	53	62	61	50	45	52	62	70	82	17.1%	5.7%
Bangalore	95	81	70	80	79	78	105	166	197	242	22.8%	10.9%
Chennai	110	89	79	85	75	67	72	83	98	129	31.6%	1.8%
Delhi	135	111	95	101	92	85	93	114	155	216	39.4%	5.4%
Goa	63	73	63	65	57	57	67	89	108	134	24.1%	8.7%
Hyderabad	45	39	43	52	51	53	60	84	109	140	28.4%	13.4%
Jaipur	68	62	45	65	62	57	65	77	99	123	24.2%	6.8%
Kolkata	109	88	82	82	72	61	66	72	87	123	41.4%	1.4%
Mumbai	170	138	130	124	104	87	95	107	136	198	45.6%	1.7%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 11: Key Operating Characteristics by Major City – RevPAR (Indian Rupees)

	1997/98 Rs.	1998/99 Rs.	1999/00 Rs.	2000/01 Rs.	2001/02 Rs.	2002/03 Rs.	2003/04 Rs.	2004/05 Rs.	2005/06 Rs.	2006/07 Rs.	12-Month Growth*	Compounded Growth
Agra	934	884	657	674	620	600	1,216	1,720	2,028	2,521	24.3%	11.7%
Ahmedabad	1,316	1,288	1,374	1,527	1,252	1,164	1,523	1,904	2,150	2,498	16.2%	7.4%
Bangalore	2,112	1,920	1,948	2,514	2,402	2,701	3,793	6,081	6,720	7,961	18.5%	15.9%
Chennai	2,720	2,329	2,236	2,452	1,997	1,880	2,213	2,708	3,407	4,191	23.0%	4.9%
Delhi	2,958	2,503	2,177	2,666	2,312	2,470	3,121	4,036	5,582	7,405	32.7%	10.7%
Goa	1,363	1,678	1,453	1,766	1,434	1,666	1,830	2,491	3,257	4,297	31.9%	13.6%
Hyderabad	879	1,042	1,144	1,600	1,642	1,751	2,105	2,969	3,993	4,465	11.8%	19.8%
Jaipur	1,279	1,155	1,182	1,596	1,424	1,225	1,752	2,326	2,895	3,556	22.8%	12.0%
Kolkata	2,442	2,247	1,949	2,326	2,264	1,908	1,897	2,236	2,970	4,137	39.3%	6.0%
Mumbai	4,028	4,257	3,651	3,589	2,565	2,653	3,036	3,472	4,603	6,779	47.3%	6.0%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

Table 12: Key Operating Characteristics by Major City – RevPAR (US Dollars)

	1997/98 US\$	1998/99 US\$	1999/00 US\$	2000/01 US\$	2001/02 US\$	2002/03 US\$	2004/04 US\$	2004/05 US\$	2005/06 US\$	2006/07 US\$	12-Month Growth*	Compounded Growth
Agra	26	23	15	15	13	13	27	38	45	58	27.7%	9.4%
Ahmedabad	36	31	31	34	27	24	33	42	48	57	18.0%	5.3%
Bangalore	58	48	45	56	51	56	82	135	151	183	20.9%	13.6%
Chennai	75	58	52	55	42	39	48	61	77	96	25.7%	2.8%
Delhi	81	60	50	59	49	51	68	90	125	169	34.7%	8.5%
Goa	37	43	34	39	31	34	40	56	73	98	34.5%	11.4%
Hyderabad	24	26	26	36	35	37	46	66	89	103	14.8%	17.5%
Jaipur	35	28	21	36	30	26	38	52	65	82	25.4%	9.8%
Kolkata	67	51	45	52	48	40	41	50	66	95	42.7%	3.9%
Mumbai	111	93	84	80	54	55	66	77	104	156	50.4%	3.8%

* Growth in 2006/07 (in absolute terms) expressed as percentage of the figure for 2005/06

period is Mumbai (3.8%). However, with the impending shortage of rooms in Mumbai over the next few years we can expect this to correct itself and HVS strongly believes that Mumbai will remain the most attractive hotel investment market over the next four to five years or even longer.

In terms of RevPAR the trends have been interesting. Two years ago Bangalore led the growth story by registering the

highest increase. Last year Hyderabad became the RevPAR growth leader and achieved a growth of 44.3%. This year it was relegated to last place in terms of RevPAR growth, an indication of what happens when hotel rates reach abnormally high levels. Mumbai (47.3%), followed by Kolkata (39.3%) and Delhi (32.7%) were the RevPAR leaders in 2006-07. Kolkata actually has done remarkably well over the past 2-3 years and should continue to

show improvements until new supply hits this market. Another market that continues to do well is Goa with a RevPAR growth of 31.9%. Future RevPAR performance in secondary destinations, both Commercial and Leisure, will depend upon demand growth from key markets and occupancy improvement is likely to be the most important driver. Secondary markets, typically, have substantially higher rate sensitivity, resulting in longer rate maturity periods.

Hotel Supply

Over the past two years, we at HVS have been tracking the development of new supply very closely. In 2005, the proposed new supply of branded and quality hotels for the ten markets covered by us was 22,400. This rose to 48,500 in 2006 and today has further grown to 77,500. In fact if we were to take all new supply there would be a total of 1,02,000 rooms entering the Indian hotel industry within the next five years. This year's report also shows the new expected supply for Pune and Chandigarh, in addition to the other markets.

We would like to categorically state that this does not include all hotels announced in the media from various sources. HVS has been tracking new supply very closely each year, and we have come to the conclusion that there is a good deal of misinformation and speculation, where new supply is concerned. Today it is

fashionable to make announcements particularly by real estate developers to the media that they are developing 20 or more hotels. With the exception of a few large real estate developers, no one wants to state that they are doing one or two or even three hotels as they might be seen as being small. If they intend an IPO, then there is concern that such a perception could affect their listing. Therefore, we at HVS have put together a list of developments under construction or those announced in each market that have a confirmed tie-up with an operator and have given an unbiased third party probability factor of their prospects within the next five years.

In Table 13, we present the existing and proposed supply entering each of the ten markets covered in this report. The table reflects the proposed supply's anticipated growth over the next five years (2007-2012) and also

shares a probability factor (active supply) to reflect those hotels, which are either under construction or hotels that HVS is confident will open before December 2010. Moreover, we have provided in this table the potential positioning for this new supply and allocated it among Luxury, First class, Mid-market and Budget hotels. Following this table we have presented our views on the supply outlook of all the cities.

Last year, when we undertook the exercise of determining new hotel supply, clearly Hyderabad and Bangalore were expected to see the maximum development at 513.7% and 408.9% respectively. These two IT cities are still very much near the top with expected increases in room supply of 568% for Hyderabad and 534% for Bangalore. They have, however, been overtaken by Pune, which has 1,039% increase anticipated in its potential supply. While the above

Table 13: Distribution of Existing and Proposed Branded Hotels by Major City

	Existing Supply	Proposed Supply	Increase over Five Years	Active Development of Supply	Luxury	First Class	Mid-market	Budget
Agra	1,336	764	57%	32%	-	10.5%	73.8%	15.7%
Ahmedabad	519	2,230	430%	60%	-	30.3%	40.9%	28.9%
Bangalore	2,414	12,882	534%	61%	22.8%	35.7%	34.7%	6.8%
Chandigarh	340	1,567	461%	45%	9.6%	22.3%	45.3%	22.8%
Chennai	2,442	6,213	254%	68%	23.8%	20.5%	40.9%	14.7%
Delhi (NCR)	7,990	19,423	243%	56%	23.3%	25.9%	32.5%	18.3%
Goa	2,450	3,058	125%	58%	37.5%	22.4%	28.1%	12.0%
Hyderabad	1,868	10,619	568%	47%	18.3%	34.1%	34.2%	13.5%
Jaipur	1,388	4,012	289%	56%	12.2%	36.5%	35.3%	16.0%
Kolkata	1,354	3,644	269%	67%	16.9%	30.6%	47.7%	4.8%
Mumbai	7,402	11,578	156%	49%	31.8%	31.8%	24.8%	11.6%
Pune	777	8,072	1039%	77%	14.1%	24.4%	51.8%	9.6%
Other Cities	9,005	17,909	199%	58%	4.2%	23.6%	21.5%	50.7%
Total	39,285	101,971	260%	58%				

table needs to be read carefully and may even come as a shock to many potential investors, we should give careful consideration, if not more weight, to the actual active development of the proposed supply in column four. So while Pune may reflect that 8,072 rooms are under development, we at HVS believe that 77% of this proposed supply will actually get developed by 2010.

There has also always been considerable debate about the number of rooms India actually has. Our estimate is that there are possibly 1,10,000 rooms currently operating in India. This number is based on the number of rooms which are officially approved by the Government of India as well as the number of FHRAI members. We also estimate that there would probably be another 25,000 to 30,000 guesthouses or corporate guesthouses taking the total supply of transient guest rooms to approximately 2,00,000 units/rooms. What however is shocking and a number that we are absolutely confident about is the low number of branded or quality room supply in the country; it stands at below 40,000. This overall number for India is actually lower than that for many international cities around the globe. Therefore when we look at the approximate 1,02,000 rooms being developed or say we use a probability factor of 58% across the country, the numbers of rooms being developed in India still remain extremely low and offer huge potential to investors and operators across all segments.

In most cities this high growth can easily be attributed to the existing low base of quality hotel supply. As previously suggested

the **Pune** market tops our list with close to 8,000 rooms planned. Unlike other cities, considerable construction activity is taking place here in the hotel space and we anticipate that within the next 18 months alone 2,000 rooms will be added to the city supply. This is expected to not only bring down occupancy levels but we anticipate that there will be a short-term oversupply in certain areas within Pune resulting in sharp rate correction in the market. While most of the planned supply in the market is concreted around existing demand areas, the potential for further demand in these areas has saturated, resulting in supply bubbles. We are of the opinion that development of hotels with boutique orientation, positioned between mid-market and first-class, within integrated mixed-use developments, will continue to do well in the medium to long term.

When HVS started the survey 11 years ago, the **Hyderabad** market was ranked 10th and last in terms of RevPAR. Today it has risen to 4th place and enjoys the highest compounded growth rate at 17.5% in terms of RevPAR growth. More Meeting, Incentive, Convention, Exhibition (MICE) business is likely to be induced in Hyderabad with the development of a new airport and the Hyderabad International Convention Centre. Thus, we expect the Hyderabad market to be on an upward trajectory. There is a strong positive correlation between absorption trends of commercial space and demand growth in room nights. Over the long term, the Hyderabad market is expected to add substantial commercial

space, providing necessary impetus for growth and expansion of demand base. Despite the potential 568% growth in new supply, we believe that only 47% of this will actually convert itself into new rooms. There appears to be a lot of hesitation and delays for the various projects. Also it would be recommended that the focus move towards budget hotels as they are expected to outperform the market and give better returns on investment to developers. Hyderabad too runs the risk of going the way that Bangalore and a few other cities did, with corporates beginning to shy away from hotels as they have completely outpriced themselves in the market. Instead corporates set up guesthouses or accommodation rooms for employees are now more the norm.

Bangalore has been on the radar of quite a few developers mainly due to the spectacular performance of the city over the past four years. While new supply has been relatively slow in coming, a fair bit of development is taking place. The city has also witnessed a mushrooming of guesthouses that have eaten into the hotel market, which is resulting in the weakening of occupancy. Once supply-demand equilibrium is reached (around 2009/10), HVS predicts that there will be a sharp rate correction in the Bangalore market. This will actually help bring back some of the unaccommodated demand being utilized by the unorganised sector. We maintain that there remain pockets in Bangalore that are still viable for the development of hotels provided the positioning

is correct. Clearly there is a good opportunity for development of multiple hotels catering to specific demand areas in the budget and mid-market space.

Chandigarh (including Mohali) has only one recognized brand and therefore has an extremely low base of room supply. The city offers excellent opportunities for Food & Beverage, Banquets and so forth. Therefore we believe that First class, Mid-market and Budget hotels will particularly do well. As most real estate companies have land banked in this city there has been no shortage of announcements. We however estimate at this stage less than half (45%) of these projects will actually get developed in the next three years and many of them on futuristic locations. Further, for these new hotels to perform well there will have to be significant development on the IT/ITeS front as well.

Gujurat, as a state, is typically considered a good investment destination; and **Ahmedabad**, as its capital, is certainly gaining from all the interest around hotel development. While there is active development taking place for many projects we believe it is well balanced between good locations and a good mix of products. We do not anticipate development of a luxury hotel of international standards anytime soon. At present 430% increase in supply is expected, however only 60% of this can be confirmed.

HVS believes that **Jaipur** continues to have the potential of converting itself into a more all-round destination, owing to its proximity to the Delhi National Capital Region (NCR), its

positioning in the Golden Triangle (Delhi-Jaipur-Agra) and also because the city is the entry point to many other places of interest in Rajasthan. Jaipur has recently started seeing IT/ITeS coming in and this is giving the Commercial segment additional room nights. With an extremely proactive government in the tourism space, the state and city have clearly benefited. The city has a good mix of branded and unbranded supply, owing to its popularity as a tourism destination. We believe that new supply will get successfully absorbed provided the projects are built to quality, to match the segments they want to compete for, and have their own USP. At present 289% of new supply is expected, however only 56% of this can be confirmed.

Kolkata has done relatively well in the past three to four years. However, with 269% potential supply and 67% probability of this supply entering the market in the next three years, we are slightly worried, as we do not believe that commercial development will be able to take place at the same pace. However what worries us further is that a large part of this development is happening at the upper end of the market. International brands of repute are signing up in locations not conducive to them and are more than likely not to achieve the average rates they typically associate with elsewhere.

We remain extremely bullish on **Chennai**, which historically has performed very steadily. Chennai can expect a 254% increase in its room supply with a high 68% of availability by 2010. Chennai, unlike many other cities, enjoys

the advantage of strong growth in the IT/ITeS sector coupled with good demand from banking and automobile, which has a strong manufacturing base in the city. Unlike other locations the city's hoteliers have not pushed up rates unreasonably and therefore we believe in the long run this will actually help the city to grow more uniformly.

The **Delhi National Capital Region** (NCR) has the largest existing base of supply. While the number of branded / quality hotels is just short of 8,000 rooms, we believe if one were to add the unbranded segment and the unorganised guesthouses, the NCR will have at least four to five times this number of rooms. Last year we suggested that 47 new hotels with approximately 10,800 rooms are coming up. This year this number has increased to 80 new hotels with 19,400 rooms. While this may be music to the Delhi government's ears, they should seriously be worried. Last year we had indicated that 74% of these projects would be developed in time for the Commonwealth Games. This year our research indicates at best only 56% of these projects will be ready. The above takes into account the delay or complete withdrawal of plots in the NOIDA corridor that would have allowed for 3,500-4,000 additional rooms supply to enter the market. The government would be well advised to perhaps put less emphasis in auctioning sites and generating revenue for their respective departments; and more emphasis on granting licenses and other permissions to fast track the developments planned. If spaces are being auctioned off as hotel sites, why

do we still need to seek clearances and licences from 40 plus agencies to build and open these hotels? Another option that could certainly alleviate the problem of room shortage in the NCR is the relaxation of FSI restriction for hotels. The FSI is abysmally low (average 2.0) as compared to other international destinations or even other cities in India.

Mumbai has traditionally been a very good market for hotels and we expect this to remain a star performer in the next five to six years. There is a huge supply-demand gap, which is currently not being met and is not likely to correct itself over the next five years. The city has a new supply pipeline of 156%, however less than half (49%) of this is expected to be realised. We believe the new international convention centre at Bandra Kurla complex and the re-development of the airport will also certainly induce additional demand for the city hotels. For all the new supply entering this market, we believe it still enjoys a good mix of different hotel segments.

Our favorite Leisure destination remains **Goa**. While we have been talking about Goa positively for the past few years, we find that development activity in this small state is quite a challenge and hotels take unusually long to get developed here. The state is likely to see a 125% increase in supply with a probability of 58% completion in the next three years. The addition of a convention centre is also likely to help in the MICE segment, which offers huge potential.

Agra remains a seasonal market, but due to its importance (to

complete the Golden Triangle) is likely to see some additional developments taking place. We believe the market will perhaps grow by 57% and approximately 32% of this might actually get developed.

Going forward, the biggest challenge, given the present supply scenario, will be the availability of quality sites for hotel projects. Site location, accessibility, visibility and proximity to key demand areas are critical factors for long term feasibility of hotels and lack of good sites would have a negative impact on the supply front. The real estate market too, has seen its best times in the last three years, and existing land prices across most cities are somewhat prohibitive, especially for standalone property developers. In the past two to three months there appears to be a slight slowdown on the land valuation front. Prices have stagnated if not slightly corrected themselves. This itself offers a great opportunity to investors who are likely to start looking for bargains.

Future Trends

Clearly operators have focused intensely on increasing rates, even if it has been at the cost of lower occupancies. While this has been a good strategy in the short term, in the near future the operators need to find the right balance between trying to push rates vis-à-vis losing room nights. Rates last year went up by 30% across segments, mainly pushed by very strong performances in Mumbai, Delhi, Kolkata and Delhi (NCR). We expect that rates in these cities will further go up in the short to medium term. However, rates in Bangalore and Hyderabad are

already showing signs of weakening.

Typically, the average rate movement follows the occupancy movement. This has been the case historically, and is a global trend as well. So if occupancy goes up the rates follow. Conversely, if occupancies decline the operators will be hard pressed to reduce tariffs. We believe that in addition Bangalore, Pune and Hyderabad also run the risk of lower occupancies in the near future. Therefore a prudent investor would base his investments on realistic pricing and not on today's inflated rates. This is particularly true for the operators who want to function in the budget and mid-market space.

HVS believes that due to the hardening of debt financing and a credit crunch across the globe – various projects may run into cost overruns and delays in the sub-continent. A lot of the hotel projects currently coming up are being developed without any due diligence to the process in terms of appropriate positioning, creating a unique USP, finding the right operator, etc. We have noticed hotels being constructed without proper plans for interior design, fit outs etc. This leads to unnecessary delays, inferior product development and consequently to poor performance in terms of operations.

F&B space and meeting space is expected to become even more important as we move ahead, particularly for full service hotels. New restaurant concepts are being created and getting a specialist restaurant designer to do one or two restaurants is no

longer considered outlandish. Traditionally the pre-function spaces were very small and were made available as an add-on. Today, modern hotels have been able to convert these areas into revenue generating areas. Most conferences need these areas to host sponsor booths and/or serve food.

Technology is also going to become an important player in streamlining operations and reducing the dependence on man-power. Globally, in-room technology is becoming more sophisticated with interactive computers, TV and music stations. This is to the customer's benefit as many of these services are being provided free to retain the guest.

The problem of inadequate trained man-power persists

already in India and internationally. We foresee some of this shortage being met by the process of hiring more expatriates in India. Also with rising local payroll costs we can hopefully also witness a reversal of man-power movement from the Middle East back to India. HVS firmly considers the issue of man-power shortage within the hospitality sector to be the most serious threat facing the Indian hotel industry. In Table 14, we have extrapolated the potential requirement for man-power across the various cities for the next five years.

Using a base of assumptions we believe that the country today has approximately 69,000 people working for hotels in the branded segment. Going forward we need to see this grow by over 213% to nearly 147,000 employees. This,

of course, also unrealistically assumes that there will be no attrition of employees to other growing sectors such as airlines, retail and BPOs which traditionally also eye this pool of talent for their growing needs. The biggest challenges in the near future are also to be faced in Pune, Hyderabad and Bangalore where unfortunately the talent hunt for rivaling sectors also remains high.

Finally, in order to determine the immediate short-term trends of the hotel industry, we have reviewed key operating statistics for five-star deluxe and five-star hotels in key cities, for the period April to September 2007. Comparisons with the corresponding period last year have also been presented, to illustrate the extent of change.

Table 14: Man-Power Requirements: By 2012-13

Key Cities	Current Man-power ¹ 2006/07	Proposed Additional Requirement				Total 2012/13	Percent Increase
		Luxury ²	First class ³	Mid-Market ⁴	Budget ⁵		
Agra	2,338	-	100	700	100	900	38%
Ahmedabad	908	-	1,200	1,100	500	2,800	308%
Bangalore	4,225	5,900	8,300	5,400	700	20,300	481%
Chandigarh	595	300	600	900	300	2,100	353%
Chennai	4,274	3,000	2,300	3,100	700	9,100	213%
Delhi (NCR)	13,983	9,100	9,100	7,600	2,800	28,600	205%
Goa	4,288	2,300	1,200	1,000	300	4,800	112%
Hyderabad	3,269	3,900	6,500	4,400	1,100	15,900	486%
Jaipur	2,429	1,000	2,600	1,700	500	5,800	239%
Kolkata	2,370	1,200	2,000	2,100	100	5,400	228%
Mumbai	12,954	7,400	6,600	3,400	1,100	18,500	143%
Pune	1,360	2,300	3,600	5,000	600	11,500	846%
Other Cities	15,759	1,500	7,600	4,600	7,300	21,000	133%
Total	68,749	37,900	51,700	41,000	16,100	146,700	213%

¹Assuming Employee to Room Ratio of an average 1.75

²Assuming Employee to Room Ratio of 2.0

³Assuming Employee to Room Ratio of 1.8

⁴Assuming Employee to Room Ratio of 1.2

⁵Assuming Employee to Room Ratio of 0.8

Table 15: Supply and Demand Analysis: April-August 2007 vs. April-August 2006

	Room supply per day			Rooms occupied per day			Occ%			Average Daily Rate (ADR)			RevPAR		
	Apr-Sept 2006	Apr-Sept 2007	Var	Apr-Sept 2006	Apr-Sept 2007	Var	Apr-Sept 2006	Apr-Sept 2007	Var	Apr-Sept 2006	Apr-Sept 2007	Var	Apr-Sept 2006	Apr-Sept 2007	Var
Bangalore	1,961	2,170	10.7%	1,424	1,398	-1.8%	73%	64%	-11.3%	11,555	11,429	-1.1%	8,391	7,363	-12.2%
Chennai	1,729	1,836	6.2%	1236	1270	2.8%	71%	69%	-3.2%	5,085	6,374	25.3%	3,635	4,409	21.3%
Goa	1,720	1,720	0.0%	1090	1120	2.8%	63%	65%	2.8%	3,585	4,378	22.1%	2,272	2,851	25.5%
Hyderabad	1,034	1,448	40.0%	780	922	18.2%	75%	64%	-15.6%	7,079	6,609	-6.6%	5,340	4,208	-21.2%
Kolkata	1,150	1,150	0.0%	802	847	5.6%	70%	74%	5.6%	4,373	5,869	34.2%	3,050	4,323	41.7%
Mumbai	5,626	5,607	-0.3%	3,800	3,922	3.2%	68%	70%	3.6%	7,955	10,265	29.0%	5,373	7,180	33.6%
New Delhi	5,422	5,368	-1.0%	3,583	3,660	2.1%	66%	68%	3.2%	8,450	10,402	23.1%	5,584	7,092	27.0%

Source: HVS Research

Table 15 presents our findings for the same.

Overall performance trends for the first six months of fiscal year 2007 remains encouraging. With the exception of Bangalore, which witnessed a slight decline in rooms occupied per day (RPD) all other markets have seen a growth with Hyderabad showing a very respectable 18.2% growth in terms of RPDs. Notwithstanding these figures, due to the increase in room supply in Bangalore, Hyderabad and Chennai, they all have seen a decline in overall occupancy. Kolkata has shown the most improvement in the market with year-to-date occupancies going up to 74%. Two years ago at this time the city was running at 66% reflecting an improving trend in the market. Mumbai, Delhi (NCR) and Goa are all reflecting positive trends.

Average rate performances remain strong for most markets for the third consecutive year with the exception of Bangalore and Hyderabad. Kolkata, with an increase of 34.2%, once again appears to be the rate leader with Mumbai following at 29.0%. While there has been some supply increase in Bangalore and Hyderabad we do not believe

these are the reasons behind the sudden drop in performance for these two IT cities. We believe the unorganised sector is becoming exceptionally strong in these markets and potential customers are not finding value for money propositions for the existing hotels. It's cheaper to stay in the guesthouses or avoid staying in these cities all together with improved air connectivity. Hotel owners and operators will be well advised to put some better yield management activities in place and ensure that this declining trend is reversed. Perhaps it may be better to hold on to market share rather than focus on annual rate increases.

In terms of RevPAR the market, in the first six months of 2007, has grown by 41.7% for Kolkata and 33.6% for Mumbai. Growth rates in terms of RevPAR have either slowed considerably for most cities or even declined in some cases. This is also due to the fact that over the last 2-3 years the base rates have grown and therefore it remains difficult to continue to grow at the same fast pace. HVS predicts that over the next few years it will become increasingly difficult to push rates further. There may be a few exceptions to this and cities like

Mumbai, Kolkata, Goa and even Delhi are likely to continue to see good growth as there is little immediate supply coming into these markets.

The Indian economy continues to perform strongly, with robust corporate results and a booming stock market the domestic leisure demand continues to be good for markets like Goa, Jaipur and even Kerala. Foreign tourist arrivals have grown by approximately 13.0% in first eight months of 2007. With the peak travel months of October to February coming up we expect the current year to continue to improve. Secondary markets in India will also continue to see improvements in performance as more branded budget and mid-market hotels open in these cities.

Opportunities

For investment purposes Mumbai clearly remains our favorite destination, as the city continues to have a limited supply entering the market compared to our estimates on the demand side. The city is the commercial capital of India and we expect demand to remain exceptionally strong across all segments in this market. While good locations could afford

a luxury or a first class hotel we also see an opportunity to do large format mid-market or budget hotels in this city.

The NCR, while expecting a lot of new supply due to the Commonwealth games in 2010, remains a good choice in many locations provided you enter the correct niche segment. Developers, however, need to be careful not to be swayed by the Games alone but to see the long-term viability of hotel projects. The potential F-1 Race being talked about for 2010 will also add to a long list of reasons for investors to consider this city. The new airport, two potential world-class convention centers are certainly other sources of induced demand in this markets. We also continue to consider that the mid-market and budget hotels have good potential across most parts of the country.

Another opportunity is in the Leisure space. India is certainly ready for family destination resorts built to international standards. These could be done both near eastern and western coastlines or within short distances to major cities. It is important that these destinations be built to international standards and offer value for money to the families they target. These resorts coupled with good MICE business have the potential to create their own niche. A good example of potential development could also be to look at the hills for summer travel and also adventure sports (including winter sports). The advent of Condo hotels into India is also a good possibility with several hotel

operators now willing to lend their name towards the same. In fact HVS believes that destination resorts and Condo hotels can be complementary to one another and therefore may also be developed side by side.

The creation of special economic zones across the country is expected to provide an impetus to exports from the domestic market, especially from the IT and ITeS sectors. While there has been a fair amount of political controversy surrounding these SEZs, we believe each of them has immense potential for the development of hotel projects. HVS believes there would be good opportunity to invest in hotel projects within SEZs. This is particularly true for developers who are developing SEZs but do not necessarily want to invest in hotel assets within them. We at HVS are conducting our first project at a SEZ and believe there is immense potential for mid-market, first class and extended stay products in these locations depending upon the SEZs' internal product mix. Some hotel operators' initial reactions have been that apart from budget hotels, other more upscale hotels may not work in these locations and therefore are hesitant to lend their better brands. However, we at HVS believe that these hotels will do quite well and present a wonderful opportunity for investors as well.

Mixed use developments continue to be a good opportunity for investments as well. However, we understand that if these are to be included with retail format then they are best suited for

mid-market or budget segments. Obviously there may be some variations to the above. We foresee many more similar developments taking place due to the high cost of real estate.

The outlook for the hospitality market in India is optimistic and will continue to remain so, in our opinion. The economy's buoyancy, initiatives to improve infrastructure, growth in the aviation and real estate sectors, and easing of restrictions on foreign investment, will fuel demand for hotels across star categories in the majority of markets. However, investment risks will remain. Therefore, a wise strategy would be to carefully observe the progress of projects under development in various cities, see how infrastructure is changing and the likely local impact on a project. Equally important would be the segment an investor chooses to enter. Just because a site is available for a first class hotel does not mean that it would be the best investment decision for that particular site. A first class hotel on top of a shopping mall with a crowded car parking below may not be a best option for a typical first class guest traveler as s/he could decide to drive a slight distance and stay further away. Alternatively a budget hotel may be a better option as it may be more acceptable, save the additional FSI for perhaps increased retail / commercial space. We anticipate that over the next five to six years India will remain as one of the world's fastest growing tourism markets and the economy will also be hard to ignore.

Acknowledgements

The *Hotels in India - Trends & Opportunities* - 2007 edition report has been developed for the benefit of employees, developers, investors and operators with an interest in the tourism industry in India. The study has been made possible only with the contribution and support of all the domestic and international hotel chains, to whom HVS would like to express its gratitude and appreciation.

If you or any of your colleagues would like to receive complimentary copies of this publication, or HVS Executive Search information, kindly send your e-mail address along with full contact details to Swarn Jaitly at sjaitly@hvs.com. Alternatively, please visit our website www.hvs.com and register yourself.

About HVS

HVS Hospitality Services is the world's leading full-service consulting and appraisal firm devoted exclusively to the hospitality industry. Founded in 1980 in the United States, the company has 24 offices across the globe. Since 1980, HVS has consulted with over 17,000 hotels in more than 70 different countries worldwide. The South Asia office is based out of New Delhi, India and has just completed 10 years of its existence.

The New Delhi team has worked on projects ranging from feasibility and marketing studies; valuation of hotels; residual land value assessments; and operator search & management contract

negotiations; in addition to development strategies for new brands and investment services. Our clients in India include Indian Hotels, EIH Ltd, ITC Hotels, Hotel Leela Venture Ltd, Intercontinental Hotels & Resorts, Mandarin Oriental, Carlson Hospitality, Global Hyatt, Hilton International, Merrill Lynch, Lehman Bros., Credit Suisse, GIC, AIG, IFC, ICICI Bank, Sun Group, Emaar (Dubai) and Kingdom Hotel Investments, among others.

In May 2001, we launched HVS Executive Search, to cater to the staffing needs of the hospitality and related services sectors like real estate, media, finance and aviation. Apart from being the first retained search firm for the hospitality industry in India, HVS Executive Search also provides services in areas of HR Consulting and Compensation Survey & Design. In addition to its New Delhi office, HVS Executive Search has international offices in New York, London, Moscow and Hong Kong. In India HVS Executive Search have offices in Mumbai and Hyderabad.

Earlier this year we added two additional services - these include Marketing and Communication Services and Technology Web Strategies.

HVS Marketing and Communication Services specializes in conceptualizing and implementing marketing strategies that position a brand, focus on consistency of experience and touch points rather than products and services and maximize Web 2.0 through cost efficient Search Engine Optimization and Consumer

Generated Media with an aim to create stronger and more strategic marketing initiatives that address the changing market through innovations in product and segmentation, supplier/ partner affiliations, CRM and e-CRM activities, loyalty programs, advertising and consistent communication.

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This publication has been authored by **Manav Thadani**, Managing Director and Partner with HVS in the New Delhi office. Manav has spent over 12 years with HVS and has worked in the New York, London and Delhi offices of the company. As Managing Director and Partner of the New Delhi office he is responsible for all HVS activities in the region including the *Consulting & Valuation, Executive Search, Marketing & Communication Services and Technology Web Strategies*.

Manav holds a Masters degree in Food Service Management from New York University (NYU), prior to which he completed his undergraduate education in hotel management at NYU. He is also a regular speaker at various hospitality / real estate industry conference and plays host to the annual Hotel Investment Conference - South Asia (HICSA).

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