



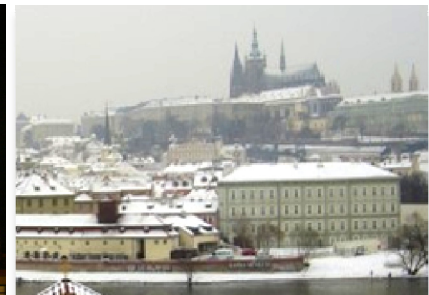
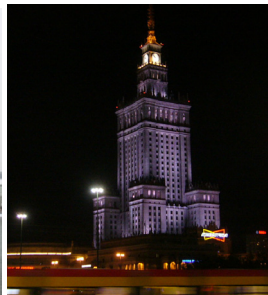
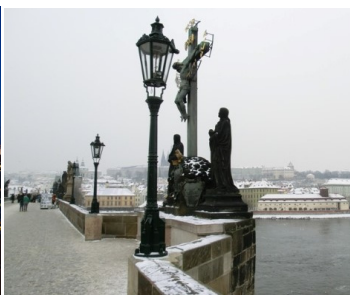
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BARGAIN HUNTING FOR LUXURY HOTELS – WHICH CAPITAL CITY PROVIDES THE BEST VALUE FOR MONEY?

A COMPARISON OF THE LUXURY HOTEL MARKETS IN BERLIN, PRAGUE AND
WARSAW

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Affordable Luxury – a Comparison of Three Hotel Markets

The capitals of three neighbouring countries – Berlin, Prague and Warsaw – have a reputation for being affordable destinations. These cities are also home to a large number of international-standard luxury properties, so guests might wonder, ‘where can I get the best value for money?’ To answer this question, we analysed the characteristics of the luxury hotel markets in these cities. By examining the dynamics between supply and demand, we explore how occupancy and rates vary amongst the three markets, illustrating how luxury hotel rates compare to those of upscale hotels. From a guest’s point of view, a luxury hotel is affordable and provides a good value proposition if the price difference to the upscale category justifies the superior quality and extra services. So getting value for money means happy guests, but what about the hoteliers? From their perspective, it’s all about maximising rooms revenue per room (RevPAR) and bottom-line profits; thus, we provide an illustration of the RevPAR dynamics across the three markets.

Upscale versus Luxury – Rate as a Differentiator

What is the difference between a luxury and an upscale hotel? Borders between the two categories seem to be blurring more and more. Star categories are often established by governments and may not be the best way to differentiate the two segments. Star ratings generally focus more on the facilities, rather than on service.

Nowadays, hotel companies are more focused on brand positioning than star categories. The industry has even seen owners ‘voluntarily’ downgrading their hotels in order to remain competitive whilst still offering the same standards (specifically for the MICE segment). This trend is the result of a decrease in corporate travel budgets, particularly in the financial and pharmaceutical sectors.

In all this confusion, two characteristics can still be used as indicators of whether a property belongs to the upscale or the luxury class: a hotel’s brand and its average rate. These factors tend to capture the service element better than the star categorisation. Hotel companies have invested vast amounts of money and energy into keeping brands and positioning consistent. More importantly, the price a customer is willing to pay for the service, location and facilities the hotel offers is reflected in the prices paid, and average rate is therefore a better differentiator.

SUPPLY AND DEMAND

In order to determine the city that provides the best value for money in the luxury segment, the three markets have to be analysed in regards to their respective size and the underlying hotel market dynamics. A comparison of the

current supply and demand illustrates that the sizes of the three hotel markets vary significantly.

Demand Overview

Berlin is the largest of the three cities in terms of population. The German capital is one of the leading cultural, political and economic cities in Europe. High visitation numbers underline its significance. Berlin’s strong growth rates over the last ten years in visitation, bednights and airport arrivals clearly outperform Prague and Warsaw (see Figure 1).

FIGURE 1 DEMAND STATISTICS

	Berlin	Prague	Warsaw
Population	3,500,000	1,270,000	1,700,000
Annual Visitation 2012	10,849,000	5,398,000	2,495,000
% International	38%	87%	40%
Number of Bednights 2012	24,896,000	13,618,000	4,326,000
Average Length of Stay (Days)	2.3	2.5	1.7
CAGR Visitation 2002-12	9%	8%	5%
CAGR Bednights 2002-12	8%	3%	5%
Airport Arrivals 2012	25,237,000	10,795,000	9,572,000
CAGR Airport Arrivals 2002-12	8%	6%	7%

CAGR: Compound Annual Growth Rate

Sources: Airports Council International; Berlin Tourismus Marketing GmbH;

Statistik Berlin Brandenburg; Czech Statistical Office; Institute of Tourism Poland;

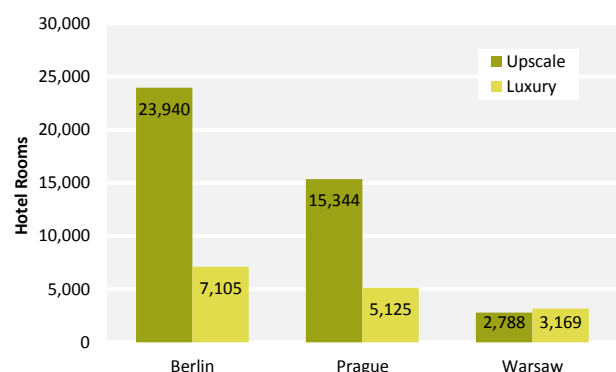
Central Statistics Office Poland

Berlin and Warsaw are both domestically driven markets, whereas in Prague the percentage of international visitors reaches almost 90% of total visitation, highlighting the city’s reliance on foreign demand. Notably, all three markets have achieved strong growth in visitation and bednights over the past ten years.

Supply Comparison

The comparison of existing supply (see Figure 2) shows that Berlin and Prague have a much higher room count than Warsaw.

FIGURE 2: EXISTING SUPPLY COMPARISON (BY NO. OF HOTEL ROOMS)



Source: HVS Research

Berlin, owing to the scale of its hotel visitation, unsurprisingly has the largest number of upscale and luxury hotel rooms out of the three cities.

Interestingly, despite a lower demand base (measured by total visitation and number of bednights), Prague registers a relatively large amount of upscale and luxury supply, as a percentage of total hotel room supply and also in terms of the ratio of available luxury and upscale rooms per inhabitant or visitor (see Figures 3 and 4).

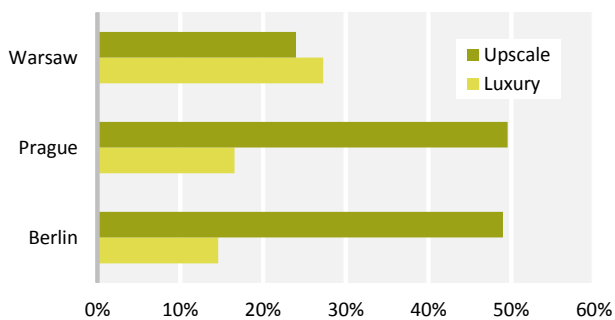
FIGURE 3: AVAILABLE HOTEL ROOMS (LUXURY AND UPSCALE COMBINED) COMPARED TO POPULATION AND VISITATION

	Berlin	Prague	Warsaw
Available Luxury and Upscale Rooms per Year*	11,331,000	7,471,000	2,174,000
Available Hotel Rooms per Inhabitant	3.24	5.88	1.28
Available Hotel Rooms per Visitor	1.04	1.38	0.87

*Available hotel rooms = luxury rooms + upscale rooms x 365 days

Sources: HVS Research; Statistik Berlin Brandenburg; Czech Statistical Office; Central Statistics Office Poland

FIGURE 4: AVAILABLE HOTELS ROOMS AS A PERCENTAGE OF TOTAL ROOM SUPPLY



Source: HVS Research

In Berlin and Prague, upscale hotel rooms make up almost half of each city's total room supply. For Berlin, it should be noted that there is also a large amount of non-classified lodging facilities (such as hostels, extended stay, privately rented apartments and so forth) accommodating travellers (and these have not been accounted for in the total rooms supply).

Prague enjoyed a boom in tourism demand after the Velvet Revolution in 1989, which resulted in a dramatic increase in hotel beds. This growth only slowed after the global financial crisis in 2008 and 2009. Although many international hotel brands are present in the Czech capital, a large majority of properties remain unbranded and managed independently.

Warsaw is the only market that has more luxury supply than upscale hotels. The city's hotel market is dominated by international brands, and it is relatively 'young' as most hotels were built during the post-Soviet era and international

operators managed to secure almost all of the development projects in prime locations.

Pipeline

FIGURE 5: NEW SUPPLY COMPARISON (BY NO. OF NEW HOTEL PROJECTS)

	Berlin	Prague	Warsaw
Upscale	10	1	2
Luxury	3	—	1

*Only confirmed projects

Source: HVS Research

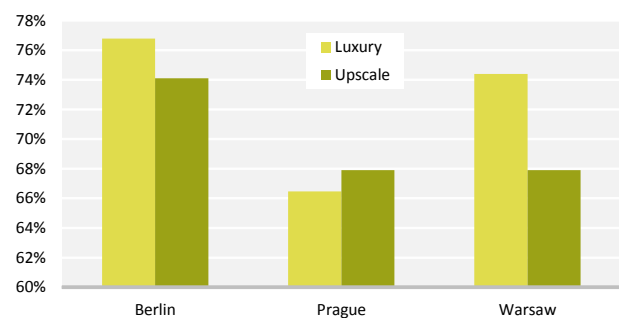
Berlin has the biggest upscale pipeline. The city remains attractive to developers for several reasons: barriers to entry are relatively low since, unlike other European gateway cities, Berlin does not have a development space issue; plus, German cities are still attractive investment-wise as the country has a low-risk profile and a stable economic outlook; furthermore, due to Berlin's status as one of the key gateway cities in Europe, some operators are willing to accept lower profitability in order to be represented in the market.

OCCUPANCY AND RATE DYNAMICS

As a result of the different supply and demand characteristics of each market, occupancy and average rate vary significantly amongst the capitals.

Occupancy Comparison

FIGURE 6: 2012 OCCUPANCY – LUXURY VS UPSCALE



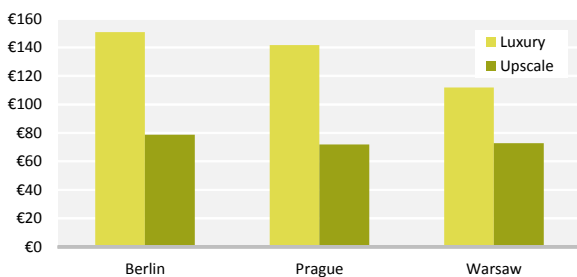
Source: HVS Research

Berlin is the occupancy leader in the upscale segment. On average, upscale hotels in Berlin achieved about 74% occupancy in 2012, which was significantly higher than Prague and Warsaw (both around 68%). Berlin has a good leisure-demand base, due its cultural offering, and manages to capture more demand throughout the whole week. The more corporate-focused Warsaw generally achieves lower occupancy levels during weekends. Although Prague is a very popular tour operator destination, group-leisure demand is generally well absorbed by the large amount of hotel beds in the city.

Achieving an average of 77% occupancy in 2012, Berlin also leads the way in the luxury segment; however, Warsaw follows closely with 74% whilst Prague only achieved 66%. Luxury hotels in Warsaw outperform the upscale segment by offering lower rates in order to attract weekend business. In Prague, luxury hotels achieved a lower average occupancy in 2012 compared to upscale supply, as some of the high-end properties were pursuing a more rate-focused strategy.

Average Rate Comparison (€)

FIGURE 7: 2012 AVERAGE RATE – LUXURY VS UPSCALE



Source: HVS Research

Again, Berlin leads the way, achieving the highest average rates in the luxury and upscale categories. Prague’s luxury hotels recorded high rates, not far behind Berlin. Warsaw’s luxury segment registered comparably low rates, but its upscale hotels are at similar rate levels to Berlin and Prague.

However, a simple comparison of average rates is not sufficient to determine which city provides the best value for money. The room rates of the three capitals have to be put into perspective and analysed further by comparing the differences in upscale and luxury rates.

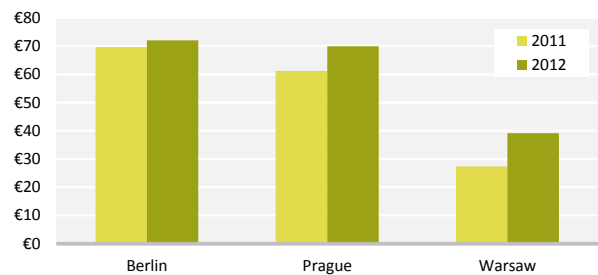
WHICH CITY WINS THE ‘BARGAIN’ CONTEST?

It’s no secret that hotel guests want the highest quality for the lowest price possible. The internet, and particularly online travel agencies, has helped commoditise hotels, adding transparency and comparability.

Rate premiums – what they mean for guests and hoteliers

The analysis of the difference in rates between upscale and luxury hotels (rate premium) demonstrates in which city guests enjoy the best value for money when staying at a luxury hotel. However, the value perception for hoteliers (and investors) appears to be different. Whereas bargain hunters prefer staying in luxury hotels for a lower price, hoteliers naturally focus on optimising RevPAR (the product of occupancy and rate) and profits.

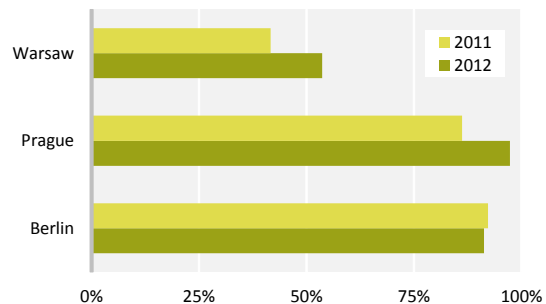
FIGURE 8: AVERAGE ROOM RATE PREMIUM



Source: HVS Research

A comparison of luxury and upscale average rates shows that Prague and Berlin’s luxury hotels had much higher premiums over the upscale category than Warsaw. The average rate of a luxury hotel in Berlin was about 90% higher than at an upscale hotel. Prague showed a similar situation of high premiums. Notably, rate premiums in each city improved between 2011 and 2012 (albeit average rates of luxury hotels are still below pre-crisis peak years).

FIGURE 9: RATE PREMIUM AS A PERCENTAGE



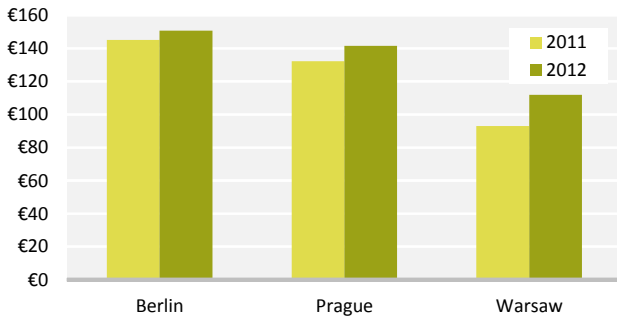
Source: HVS Research

Both Berlin and Prague have seen considerable growth in supply in the upscale segment over the past few years. The growing supply, coupled with the economic uncertainties and difficulties in the Eurozone, put pressure on room rates in the upscale and midscale segments, which led to heavy discounting practised by many hoteliers. Prague’s upscale rates were particularly impacted as the unbranded hotels pursued aggressive pricing strategies.

The relatively high premium demonstrates that guests are still able to find good value for money in the upscale segment in Berlin and Prague. This makes Warsaw the clear winner for bargain hunters as premiums for luxury hotels in the Polish capital are much lower than in Berlin and Prague.

The main reason why Warsaw’s luxury hotels are not reaching a high premium over the upscale category lies in the strong seasonality the market is experiencing (weekend/weekday and annual).

FIGURE 10: COMPARISON OF AVERAGE RATES – LUXURY HOTELS

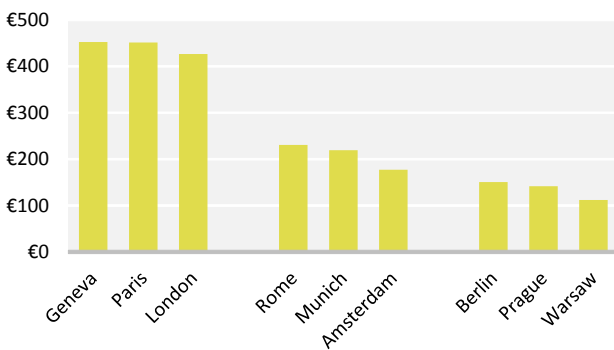


Source: HVS Research

How do Berlin and Prague compare to other cities?

Even though Warsaw has a lower rate premium, luxury hotels in Prague and Berlin still provide an attractive value proposition. When compared to top gateway cities in Europe, hotels in Berlin and Prague remain more affordable (as illustrated in the comparison chart below).

FIGURE 11: COMPARISON OF 2012 AVERAGE RATE – LUXURY HOTELS



Source: HVS Research

WHAT IS THE HOTELIER’S PERSPECTIVE?

Affordable hotel prices might make guests happy, but hoteliers (and investors) try to maximise RevPAR and bottom-line profits and are therefore eager to maintain high room rates whilst maximising yearly growth rates.

All three markets provide good value for money for luxury hotel guests, but unsurprisingly many hoteliers would like to see higher rates. However, market dynamics prevent hotels from reaching performance levels comparable to other gateway cities.

The reasons behind low rates in luxury hotels

In the case of Berlin and Prague, the main reason for these lower rates is the abundance of luxury hotels. Berlin’s governor Klaus Wowereit’s famous quote describing the city as ‘poor but sexy’ also applies to the luxury hotel sector. Although its rates exceed those in Warsaw by far, the sector

(with many excellent luxury hotels) does not achieve the same rate levels as other top gateway cities. Luxury rates in Berlin even lag behind the other large German cities such as Munich, Frankfurt or Hamburg. Although an important city in Europe, the German capital is waiting for a true international airport (the latest announced opening date is April 2014; however, this will need to be seen to be believed). Nevertheless, once the airport is fully operational, the city will have good potential to improve accessibility for international travellers, which could result in a potential increase in high-end visitors.

Prague’s luxury sector has not seen any recent developments, and the top rate tier of the luxury market is very much driven by the high rates of the Four Seasons, a clear leader in the market owing to its unique location and brand power. An interesting case is the Augustine Hotel; the property was formerly operated by Rocco Forte Hotels but is unbranded at the moment (apart from the affiliation with Leading Hotels of the World) and its future is uncertain. Although the hotel is not in a prime location, there are potential opportunities for rate growth with the right operator, brand and strategy, which could have an influence on the overall market. Despite its cultural offering, Prague has not yet managed to attract a sufficient volume of high-paying clientele (in particular from Far- and Middle-Eastern countries). A large part of its leisure demand originates from tour series or weekend ‘city-break’ stays, both generally rather low-priced segments.

THE CHARLES BRIDGE: ONE OF PRAGUE’S TOURIST ATTRACTIONS



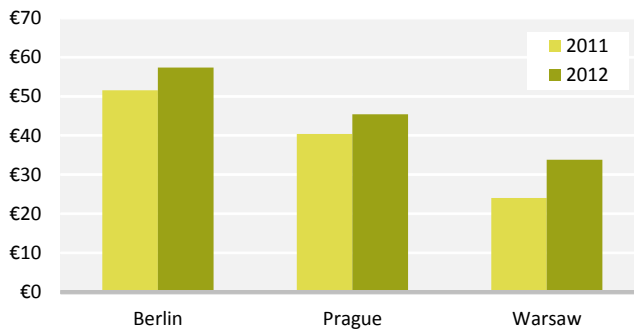
Warsaw is not (yet) positioned as an international leisure destination, and a large part of the business is domestically driven. Average rates are low as luxury hotels are competing with upscale and even midscale hotels for leisure guests during low-demand periods. The absence of high-end trophy assets, apart from the Hotel Bristol, is another reason why average rates in the luxury category are comparably lower than Berlin and Prague. The recent renovation of the Bristol and the transformation of the former Hotel Europejski into a Raffles (at estimated cost of about €65 million, scheduled to be finished in 2016) may provide opportunities for growth in the luxury category.

HOTEL BRISTOL: THE LEADING LUXURY HOTEL IN WARSAW



RevPAR Dynamics

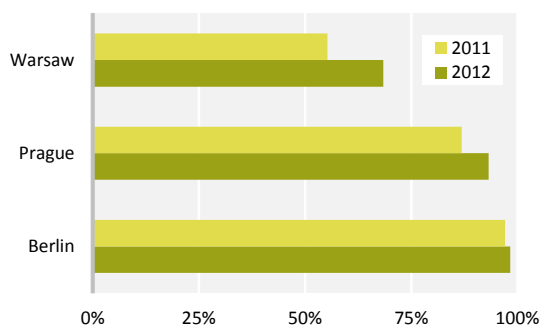
FIGURE 12: REVPAR PREMIUM (€)



Source: HVS Research

Hoteliers in Berlin reported the highest RevPAR premiums amongst the three markets during 2011 and 2012. Prague’s high rate premium was impacted by a low occupancy in the luxury segment; consequently, RevPAR premiums for luxury hotels in Prague were notably lower than Berlin’s. Warsaw’s RevPAR premium increased from 2011 to 2012, but was generally well below Berlin and Prague. As occupancy in Warsaw’s luxury hotels was high compared to its upscale counterparts, the low RevPAR premium was the result of a marginal rate difference between the two categories.

FIGURE 13: REVPAR PREMIUM AS A PERCENTAGE



Source: HVS Research

Luxury hotels in Berlin achieved RevPARs that were almost twice as high as those of its upscale counterparts. Prague showed a similar trend during 2012, with a RevPAR premium of almost 100%. However, RevPAR premiums in Warsaw, albeit showing a strong improvement from 2011 to 2012, lagged behind. Warsaw’s rate and occupancy increases during 2012 in the luxury segment were largely related to business connected with the UEFA European Football Championships.

CONCLUSION

From a guest perspective, Warsaw offers the best value for money when it comes to luxury hotels.

Although the premium for luxury rooms is higher in Berlin and Prague than in Warsaw, luxury hotels in all three destinations are comparatively affordable when compared to other European gateway cities.

Oversupply of hotel rooms, absence of high-spending leisure clientele, low demand on weekends and dependence on the domestic corporate market are factors that explain to a certain extent why luxury hotels rates in the three markets are still lagging behind other important European cities.

On the other hand, hoteliers in all three markets are working on strategies to improve RevPAR. The lower rate for luxury hotels when compared to other gateway cities illustrates that there are opportunities for growth in the longer term; however, the supply and demand dynamics currently limit the scope for rate increases. Still, the small pipeline of new luxury and upscale hotels in Prague and Warsaw and the steady growth projections in tourism arrivals in all three cities are signs that these markets have potential to recover and grow further in the future.

Luxury hotels in the three cities are likely to continue providing a good value proposition for visitors until the underlying supply and demand factors change significantly. But opportunities for this to happen exist in all three markets; it will just be a matter of time...



About HVS

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