International
Business Outlook '16

The Future of Business Revealed.

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Business Outlook '16

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"In its 80th anniversary year, the team at Christie & Co enjoyed a successful 2015 and continued to share the work, difficulties and triumphs, for, with and on behalf of our clients, adhering to our founders' simple ethos of promoting our clients' interests first and foremost."

David Rugg, Chairman

Many of our predictions from last year's Business Outlook have come to pass. Relatively subdued volumes coming to the market in 2015 created a scarcity of assets that further fuelled price growth, while continued low interest rates and an improved lending environment created an appetite to acquire. This disparity between supply and demand looks set to continue in 2016.

Low volumes

In the business retail market, Christie & Co experienced continued 'business blocking' during 2015. Interest receivable on deposits is at an all-time low and many private business owners are simply staying put. Coupled with the fact that banks have mostly disposed of large portfolios of over-geared loans, the result is that volumes in the market remain stubbornly subdued. In 2016 we may see some spin-off sales from large portfolios that have been bought in recent years as the acquirers sell off the assets that don't fit with their medium-term aspirations.

Funding landscape

As Nick Baker, Managing Director of Christie Finance, explains, the lending market has been diversifying since the recession and there are a range of challenger banks in the market. It's interesting that crowd funding is also becoming a source of asset and debt funding for new and expanding businesses. It appears less appropriate for business-purchase finance, as where any acquisition is uncertain, vendors are understandably reluctant to engage with potential purchasers whose finance is in the public realm.

Value uptick

With the exception of the Care sector, values have largely recovered to pre-recession levels. Encouragingly, merger and acquisition activity has been evenly spread across all our business sectors. This is one key differentiator between 2015 and 2014, when the Hotel market was hectic but other sectors weren't to the same extent. We expect the value of businesses across the medium term to continue to rise and outstrip pre-recession levels, in line with any increase in their profitability.

The changing buy-to-let environment

The Government's decision to reduce future buy-to-let mortgage interest tax relief contrasts with business-purchase mortgages whereby currently all interest is allowable. This decision, coupled with the announcement in November's Spending Review of an increase in stamp duty on buy-to-let properties of 3%, is likely to impact the landlord market in 2016. Stamp Duty on business acquisitions remains unchanged.

Uncertainty remains

Though we expect values to rise in the medium term, there are still areas of uncertainty in several of our sectors caused by factors such as the Living Wage, as our sector heads explain in this Business Outlook. Our consultancy team wrote an incisive report on the implications, following this surprise announcement last April. In June 2015 we published our report 'The UK Nursing Workforce: Crisis or Opportunity', which was debated in the House of Lords, and we will continue to research the area of staffing costs, which is highly relevant to all our business sectors. Our teams across the UK and abroad have the specialist knowledge and research available to gauge the effect of various scenarios on business growth.

The impact of politics

The UK has been through quite a period of political change in 2015 and the continued impact on our markets is varied. The dominance of the SNP in Scotland is dissuading migration from the South which has historically provided lifestyle buyers to Scotland, while in contrast the awaited referendum on the UK's membership of the EU doesn't particularly impact our domestic businesses. Political instability elsewhere in the world only serves to enforce the UK's safe haven status.

Legislative change

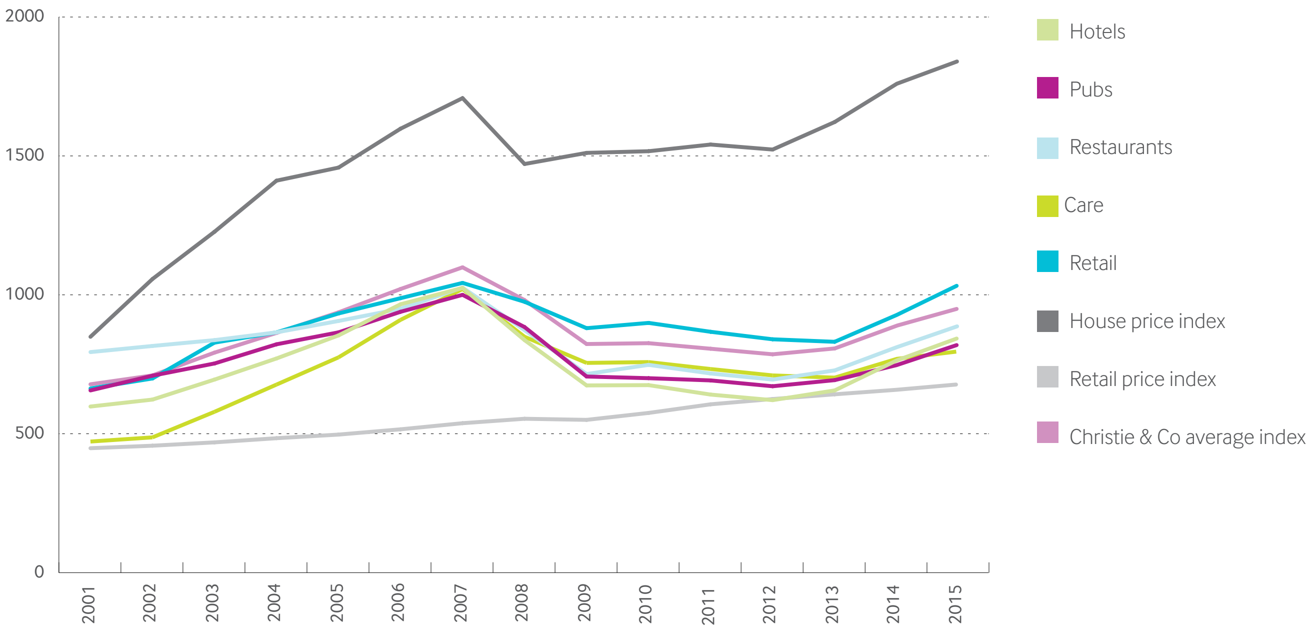
As we start a new year, as an industry, we are faced with a number of legislative processes which will have an impact on all of the sectors that Christie & Co covers. Whilst the implementation of the National Living Wage will undoubtedly create challenges within certain sectors, it would appear that most operators are proactively tackling it and drawing up inventive plans to limit the impact on their businesses. Across all of our sectors, it is likely that corporate operators will undergo strategic reviews of their estates and poorer performing units will come out of the corporate sphere and return to the individual sector. We have already seen that there is a ready market waiting for such investment opportunities. A second, more recent example saw the Department of Health announce in December that funding for community pharmacy in 2016/17 will be cut by £170m – a reduction of more than 6% in cash terms. Rumour has circled the market for some months, but as yet we've seen no reduction in purchaser appetite. The announcement may accelerate some operators' plans to exit the market, however, with over 4,000 registered applicants nationally, others may see any potential increase of pharmacies being put up for sale as a real opportunity to acquire in an easing market.

Overseas interest continues

Overseas investment volumes should continue to rise in 2016. Good businesses enjoying secure tenure of sufficient scale in an open market will always attract overseas investment, but the nationality of those purchasers varies depending on currency and political restrictions. Christie & Co's teams speak 23 languages between them and our network of offices puts us in an unrivalled position to advise clients on cross-border interactions.

Index based on average sale prices

from a base of 100 in 1975



"Throughout 2015, activity continued at a consistent pace, particularly in terms of value, with prices still moving forward albeit not at the same speed as 12 months ago, particularly within the Hotel market. The Care market is exhibiting some caution due to the National Living Wage announcement. However, there is growth to come across all of our sectors and Christie & Co is well positioned to meet it."

Chris Day, Global Managing Director

Caution outweighs enthusiasm

At the moment, the market lies in very similar territory to where we were in 1995, the start of a long, positive but undulating road to the bubble of 2006-2007. Momentum is limited in some markets and those markets that do take off are likely to readjust as buyers exercise caution. This will be fuelled by economic and political uncertainty and very low yields exacerbated by historically low interest rates resulting in very high pricing.

Investors could change direction

In 2016, the landscape of low borrowing and high availability of money could lead to the creation of REITs focused on our operational markets. We've seen a few US REITs enter the Care market, for example, and we could see UK entities emerge. If private equity investors start to consider their exit routes they may also need to look at REITs as an alternative to the IPO market, as in general, investors are more cautious. The UK market could increasingly mirror the market seen in the US for the last three years.

However, REITs aside, we could see some large portfolios in 2016 go for an IPO rather than re-trade to private equity houses. Some portfolios will be worth well in excess of £1bn and there aren't necessarily capital sources of that size to achieve alternative exits.

Overseas interest

The international investment market is varied and in 2016 we expect to see a variety of outcomes. International investors are indicating that they still want to invest in Europe, but they remain cautious of what is happening in their home markets. China is facing economic and political challenges, but on the other hand it's getting easier to move money out of the country and the flow of capital out of China is unlikely to dry up; a more likely effect is that uncertainty will reverberate into countries like Singapore and Indonesia.

Some US funds that are more susceptible to shocks in the market, such as China's troubles, have also taken the foot off the gas for the time being. Once we're through this period, however, they will realise there hasn't been a seismic change and we'll be off again. This is a pause for breath.

Demand for our services will increase

At the moment there are a large number of consolidations occurring between large commercial real estate agencies, resulting in fewer players with knowledge of our specific markets. The opportunity this presents for Christie & Co lies in our specialist knowledge of the sectors that we operate within and our lack of conflicts. Demand for our valuation work is increasing as companies increasingly outsource services.

We are able to provide joined-up advice through our network of European offices and we have a big focus in the coming year on growing our international teams, particularly in France, Germany and Spain. Our increasing strength and depth across all European markets means that globalisation is a challenge we can help our clients to meet.

Movement in average prices year on year in per cent

	2012	2013	2014	2015
Hotels	-3.1%	5.7%	17.2%	9.2%
Restaurants	-1.4%	4.7%	11.1%	9.9%
Pubs	-3.3%	3.3%	8.6%	10.1%
Care	-0.7%	-1.1%	9.8%	4.7%
Retail	-0.9%	-1.0%	11.3%	10.3%
Medical*			13.5%	10.8%

* Data relates to pharmacy only

"The Pan-European context for those involved in the Hotel sector markedly improved in 2015, but risk profiles remain variable as one would expect for a continent with such diverse cultures, business environments, economic climates and legal systems. This variability has presented opportunities for those investors looking for opportunistic returns, while at the same time offering safe haven status in other jurisdictions. Our team, which is present in 32 locations across Europe, has been able to offer industry leading advice and deal opportunities regardless of the type of hotel investment in question."

Andreas Scriven, International Managing Director & Managing Director Consultancy

Europe's risk spectrum

Depending on risk appetite there is a European market to suit a variety of investors. For those who are seeking opportunistic returns in a recovering market, Spain offers significant opportunity. The only exceptions are Barcelona and, to a lesser degree, Madrid where prices have started to match those in other major cities across Europe. It is no surprise that Germany continues to attract investors who will trade lower returns for increased stability, both in trading and yield profile.

Smaller markets such as the Netherlands and Belgium have increasingly become attractive to those seeking a balance between opportunity and stability. France was lagging behind most markets even before recent events in Paris and is expected to continue to struggle with macro-economic, political and other regulatory issues. That being said, opportunity does exist for those who know what they are looking for.

International interest

International investors intensified their activity in Europe in 2015 and we expect this to continue in 2016. US funds are looking for opportunities as their domestic markets offer ever-dwindling return opportunities and Asian capital continues to look for a home, something Christie & Co has been able to assist with across Europe. The drivers for investment originating from Asia are extremely diverse and having a keen understanding as to the variability in decision making processes, source of funding and strategic objectives is vital for sellers to understand.

The (re)emergence of the mega deal

Following a number of years where deal volumes have consistently improved we are now witnessing the (re)emergence of major acquisitions and mergers that are likely to reshape both the European and global hospitality landscape. Marriott's acquisition of Starwood will have implications for owners as the overall footprint and brand offering of the combined company will be reviewed and some rationalisation of assets is to be expected. Accor's acquisition of Fairmont, Raffles and Swissotel will be a real test for the company and how it is able to integrate a portfolio of luxury brands into its already wide offering. It is unlikely that the Marriott and Accor deals will be the last of this kind, with the likes of Hyatt and IHG now looking to make their next move.

Deals of a different nature, but of significant impact include an influx of Chinese capital which led to the acquisition of Club Med, Louvre and Kew Green among others. The rationale for these investments is varied, with some buyers looking to bring back brands, concepts or management platforms to China, whereas others remain focused on building a portfolio of assets across Europe and beyond. We see no reason why this appetite and activity will slow in the near future, unless there is a significant change to the geo-political or macro-economic environment in China.

Local knowledge – global context

It remains critical that investors seeking to enter or expand their European portfolios fully understand the dynamics of the local market they are looking at. Certain markets are already trading well above 2007 peak levels, whereas others are still materially below the previous peak. Supply dynamics are changing rapidly as new hotels are being developed at pace following years of very limited supply additions in most markets. Investor appetite is also shifting from markets that have seen significant investment in recent years, most notably the United Kingdom, to markets that still hold the promise of market recovery.

Christie & Co's Hotels team, the largest in Europe, is able to advise on all these aspects and more, ensuring our clients make well reasoned decisions in a fast changing market.

Market predictions

Continued recovery is expected across all major European Hotel markets.

Overseas capital will play a key role in driving pricing forward.

Further consolidation is likely, in both a European and global context.

Secondary churn from non-performing loan portfolios will reinvigorate the single asset transactional market in regional locations.

20

experienced consultants across Europe

Advised on Pan-European hotel and care transactions worth over

£10bn

"In 2015 valuation activity improved markedly, dominated in the first half by large hotel portfolios. Improving economic conditions, increasing confidence and the continued availability of finance all meant that people were no longer waiting to grow their businesses, and were taking the opportunity to benefit from the low cost of borrowing."

Darren Bond, Managing Director – Valuations

Transactional Activity

It has certainly been a sellers' year, with transaction pricing returning to pre-crisis levels. However, while some banks are still disposing of non-performing loan portfolios that have been held back, the majority of significant transactions have been carried out. Most portfolios have gone to global opportunity funds and in 2016 we expect to see a further wave of secondary transactions as opportunistic investors seek to exit their investments, buoyed by strong growth in trading performance and market sentiment. We've also seen the pricing of transactions increase – a portfolio that changed hands just two years ago could be valued significantly more today, following investment and an improved trading position. It's too early to say the market is getting overheated, but it is riding towards a peak, assisted by a shortage of opportunity.

Opportunity funds

The opportunity funds that entered the market post-recession are very active. The main global players invested heavily in the market and are already looking to dispose of assets, having made very healthy levels of returns. Funds might have planned to have a longer hold, but because of the rapid improvement in the market, secondary churnings have come about faster than anticipated. Some larger portfolios are being exchanged in cash transactions bought to effect deals quickly, with a view to getting the assets revalued 6-12 months later in order to add debt.

The return of capital expenditure

With the return of confidence and finance has come the return of more normalised capital expenditure. The period from 2007-2012 saw assets starved of investment, but now we've come out the other side. Owners are looking to maximise value, so where they can see a return to improving an asset, they will invest. Some global funds have morphed to become asset managers with a team directed to maximise value. There are still unloved assets but we will see investment increase as buyers are looking for opportunities to acquire an asset that needs improvement and an opportunity to create value.

Regions and further afield

During 2016, we expect to see continued confidence in regional markets across most sectors. Outside London many assets still haven't returned to pre-recession values, so investors see an opportunity, though the risk is higher. We will start to see values more comfortably reach beyond the pre-downturn peak. Some investors will look at broader European markets to diversify their portfolio. In the UK lots of money is chasing a few deals, and markets such as Spain have improved in confidence.

Regulation and economic changes

Across all sectors there is uncertainty about the National Living Wage, as in almost all of our markets the biggest overhead is payroll. During 2016 we expect transparency to increase about the impact on transactions and subsequently valuations. There is also uncertainty around interest rate rises, though increases are unlikely to come in until at least late 2016 / early 2017, which will encourage people to continue to redistribute funds.

UK banks are now regulated to undertake three yearly valuations of assets, so we have seen an uptick in activity which will continue throughout 2016. At Christie & Co we use our knowledge of the market to continuously innovate, ensuring our valuation advice meets the constantly changing needs of clients.

Market predictions

During 2016, we expect to see continued confidence in regional markets across most sectors as values return towards pre-downturn peak levels.

We expect transparency to increase about the impact of the National Living Wage in the coming year.

In 2016 we expect to see a further wave of secondary transactions as opportunistic investors seek to exit their investments, buoyed by strong growth in trading performance and market sentiment.

Owners are expected to continue to take advantage of low-cost borrowing, with interest rate rises unlikely in 2016.

45+

RICS Registered Valuers

£10bn

worth of assets valued in 2015

"In 2015 levels of business distress returned to pre-recession levels, the availability of finance was positive and the recovery continued, but with growth slowing in the latter part of the year. While a continued period of ultra-low interest rates played its part, the decision when to raise rates could be crucial to continued stability."

Stephen Jacobs, Director

Distressed asset activity

At Christie & Co we recorded a drop of 28% in distressed asset disposals in 2015, while valuations involving impaired assets were down by 37% on the previous year. The continuing decline was expected, as levels of distress returned to pre-recession levels and insolvency appointments were at the lowest point since 2007.

The banks

According to the British Banking Association, the availability of finance was positive, characterised by an increasing number of loan approvals to SMEs. Participation in the Funding for Lending scheme, which will run until at least January 2018, has facilitated a rise in accessible lending to businesses. These trends were reflected in an increase in the number of valuations we undertook on behalf of banks for secured lending purposes in 2015.

Interest rates

While some see continued low interest rates as essential to a prolonged period of stability others are concerned about the distortion that easy access to cheap credit will have on asset prices and consumer debt. Without gradual rate rises to dampen debt enthusiasm, there is a danger that borrowing will pose a risk to future economic growth.

In October 2015, the Governor of the Bank of England, Mark Carney, insisted rate rises were a "possibility not a certainty" and in November the Bank stated that interest rates could remain at their historic low until 2017.

Certainty and timing are crucial. If rates rise too soon this could be self-defeating, derailing the recovery, slowing the economy and putting pressure on weaker businesses which could fail. Repeatedly delaying action, however, could result in the need for bigger incremental rises than markets expect, equally creating risk for businesses and the recovery.

The latest Business Distress Index from insolvency trade body R3 found that one in five businesses would suffer financial difficulty if interest rates rose by 1% in 18 months with 4% saying they would struggle to pay their debts.

If rates rise at a sustainable level, we predict that levels of distress will either stay constant or decline further in the coming year, while banks' lending will stay positive.

Growth

Late payment and over-trading problems, due to rising demand in goods and services associated with the recovery, were suspected to be behind the rise in 2014 of "Zombie" businesses - those that are only able to pay the interest on their debts. While the continued decline in distress and the number of Zombie businesses is an indicator that many companies have successfully negotiated such trickier parts of economic growth, its slowdown in the latter part of 2015 will have had an influence.

A key concern is the cooling of the global economy and its effect on domestic growth. A continued slowdown in global trade, as some economists predict, will impact on the UK economy and the ongoing recovery of UK businesses in 2016.

Market predictions

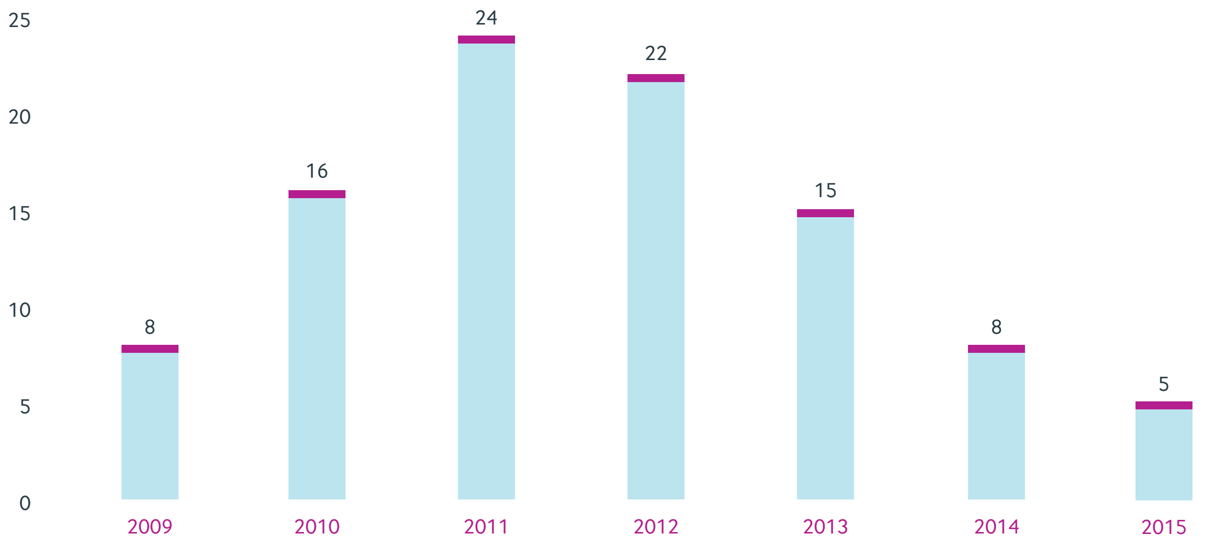
If rates rise at a sustainable level, we predict that levels of distress will either stay constant or decline further in the coming year, while banks' lending will stay positive.

Without gradual rate rises to dampen debt enthusiasm, there is a danger that borrowing will pose a risk to future economic growth.

The ongoing recovery of UK businesses in 2016 will be impacted by any continued slowdown in the global economy.

Business distress - I

Distressed assets as a percentage of all assets instructed for disposal



Business distress - II

Distressed assets instructed for disposal by sector

"With over 80 hotel professionals across the UK and Europe in Brokerage, Valuation and Consultancy services, and a newly formed Asia desk dedicated to the sector, Christie & Co is one of the largest and certainly the best placed hotel adviser in the market."

Barrie Williams, Managing Director – Hotels

UK Hotel transactional market

At c.£10bn of UK transactions, 2015 is set to be a record year from an investment perspective, albeit at the time of writing, some £3.4bn of transactions are slated to complete in Q4 2015. We expect this trend to continue through 2016, as the regional market continues to be attractive to all types of investors, including overseas buyers seeking improved returns, a stable economic environment and acceptable legal jurisdiction.

Some of the important brokerage transactions for Christie & Co in 2015 (for differing reasons) included the Radisson Blu Bristol, the Indigo Liverpool, the Arora International Hotel at Heathrow and the London Road Fire Station, Manchester.

RevPAR growth continues

Operationally, RevPAR has been growing steadily for the last few years across London and the regional markets, though 2015 grew at a slower pace. PWC's September forecast for full year 2015 was RevPAR growth of 2.7% for London, driven predominantly by rate growth of 1.8%, whilst the regional markets are set for 6.3% RevPAR growth, based on 4.6% rate growth. This compares to 3.4% RevPAR growth in London and 10.4% RevPAR growth in the regional market in 2014.

With 2016 RevPAR forecasts of 2.3% for London and 4.2% for the regional markets, there appears to be continued confidence in the economy and in the employment market. With GDP growth assumptions of around 2.5% per annum, UK consumer spending and business investment will be the main growth drivers.

Investors

London remains a strong home for investment, however the significant growth in transaction volume in 2015 has largely been driven by the regional market, which has seen increased investor confidence. While high net worth individuals and institutional investors continue to show interest, private equity firms and overseas buyers have been prevalent, as they realise debt availability has improved and acceptable returns can be made as the economy and hotel operational performance continues to grow.

Interest from Asia

Asian investment is not just about China. We saw significant interest in 2015 from countries such as Hong Kong, Singapore, Taiwan and Malaysia. The number of investors from Asia is only going to increase throughout 2016, as will the number of in-bound Asian tourists looking to stay in hotels that are managed by companies who understand their culture.

Looking ahead

There may be some large scale transactions in 2016 (together with our Irish colleagues, we have the launch of The Gresham hotel sale process, one of Dublin's most famous hotels in January), but our expectations are for regional transactions to dominate the volume. Hotel operational performance will continue to power ahead, overseas investor demand will remain strong and availability of debt funding will aid private equity investment. Christie & Co is best placed to take advantage of the Hotel market in 2016 with its substantial UK and European office base, highly experienced and knowledgeable personnel and unrivalled access to market information.

Hotels

"Over the last two years, we have seen a shift in attitudes within the Asian markets with investors who had previously concentrated solely on residential and office opportunities now considering hotels in Europe."

Joanne Jia, Head of Investment – Asia

Christie & Co now has a dedicated Asia desk covering the region and we spend a significant amount of time travelling to visit investors to make sure we understand their requirements.

Over the last two years, we have seen a shift in attitudes within the Asian markets with investors who had previously concentrated solely on residential and office opportunities now considering hotels in Europe.

London and Paris are consistently the first choices, but investors will now consider other capitals and key cities such as Dublin, Barcelona, Madrid, Frankfurt, Munich and Berlin. However, an increasing number of investors, especially investment funds, are looking at tier one UK regional cities such as Manchester, Liverpool or Birmingham.

As 2016 progresses, we expect investment from Asia to continue to rise, especially capital from China. Following President Xi Jinping's visit in October, more Chinese investors have become interested in the UK. With Christie & Co's dedicated Asia desk, we are well placed to help their search.

Hotels

Movement in average prices year on year in per cent

2012	2013
-3.1%	5.7%
2014	**2015**
17.2%	9.2%

Carine Bonnejean, Head of Consultancy – Hotels

In addition to advising on most major UK hotel transactions, in 2015 we received increasing demand for our services in markets such as Spain, Ireland, France, the Netherlands and Italy as investors look further afield for opportunities. There is also a notable return of hotel development activity across Europe which has led to more feasibility studies, best use advice and planning support, as well as interest in alternative accommodation categories such as hostels and serviced apartments.

We anticipate similar trends to continue this year with increasing pan-European activity. In the UK, industry-wide considerations such as the new National Living Wage, the upcoming business rates revaluation and supply pipeline will be key issues for us to consider during due diligence processes.

Case study - Radisson Blu, Bristol

Christie & Co was instructed on behalf of Evolve Fund Services Limited to market the Radisson Blu, Bristol hotel.

This profitable, 176-bedroom purpose built hotel, operated by Rezidor Hotel Group, opened in 2009, occupies a highly prominent and central location in Bristol City Centre. The sale was concluded with an overseas investor after significant interest from UK and international companies and provides an opportunity for the purchaser to capitalise on the continued strengthening of the local hospitality trading environment and improving economic conditions throughout the UK.

Market predictions

There may be some large scale transactions in 2016 but our expectations are for regional transactions to dominate the volume.

Hotel operational performance will continue to power ahead, overseas investor demand will remain strong and availability of debt funding will aid private equity investment.

The amount of inward investment from Asia will increase in 2016.

80+

hotel professionals across the 16 UK and 16 European offices

500+

hotels currently available for sale with a value of over €2bn

International

"Germany is a sellers' market and there is strong demand from German institutions and pension funds, as well as overseas investors from Asia and the US. While investors used to only be interested in the key cities, lately there has been demand for secondary or even tertiary cities."

Lukas Hochedlinger, Managing Director Germany, Austria & CEE

Germany

At the moment Germany is very strong and cities that have seen a marked increase in RevPAR, such as Frankfurt and Berlin, are also seeing more development. 2015 saw increased investment from German institutions such as Union Investment and investors still seek quality assets that present good value; they're sitting on money so need investment opportunities. There are some opportunistic funds that are UK-backed and Asian investors are getting more active, but their share is still small. The feedback we get is that they would invest if there were more opportunities in the market.

Austria

The Austrian market is much smaller than the German market, but with 130m overnight stays per year, tourism plays an important role. There is strong demand for hotels in Vienna, which is one of the world's top conference destinations, and a robust amount of development as a result. Activity in secondary locations continues to come from mainly regional parties.

Central and Eastern Europe

Fortunes in Central and Eastern Europe have been mixed, with some markets having picked up, while others stagnate. Many investors are interested in Poland, but other areas are also seeing activity such as Prague and the Croatian coast. In Prague, trophy assets are more attractive to overseas investors, whereas in other provincial areas, regional investors prevail. Other CEE markets such as Romania, Bulgaria, Hungary and Slovakia are picking up but from a slow base. Prior to the global credit crisis, the region experienced an influx of new supply, but following the fall in the market, these new developments have tailed off with little new stock in the area.

Hotel types

In general, the Hotel sectors that are growing are the budget and mid-range markets, including brands such as Premier Inn and Moxy. We are also seeing a growth in lifestyle brands in Germany and Austria, such as 25hours and Ruby, which we expect will continue in 2016. There are fewer openings of premium brands in Germany and Austria as development costs are much higher. Demand for resort hotels continues to fall unless a trophy asset comes to market.

Strengthening our position

Germany is one of Christie & Co's most important Hotel markets and in the coming year we will be allocating more resource to make our offering even stronger. With a new management structure now comfortably in place, we will continue to seek opportunities for growth and to increase our presence as demand for advice continues to grow.

Case study - Avalon Hotel

Christie & Co acted as agent in the sale of the 4-star Avalon Hotel Freizeit Auefeld to the German branch of US casino and hotel operator Trans World Hotels (TWH) in June 2015.

TWH purchased the property from a private owner and will operate the hotel themselves. This was the second deal with TWH, following its acquisition of Hotel Columbus near Frankfurt Airport in autumn 2014.

"Performance was fairly stable across the Scandinavian markets during 2015; the markets are absorbing new supply, and occupancy levels are generally recovering. However, rates still lag behind but are expected to catch up somewhat next year."

Kimmo Virtanen, Director Scandinavia, Russia and the Baltic States

From the middle out

Across the region the mid-range Hotel market is quite saturated and as a result, most opportunities lie in expanding either the high-end, full-service market or the budget, limited-service market. In Helsinki and Stockholm, boutique hotels are becoming increasingly more popular and Copenhagen is experiencing the same phenomenon, but it is difficult to find new supply opportunities of any kind and the city already has the most developed limited service sector in the region.

Baltic region

The Baltics are broadly in a similar situation where there are now full or limited-service hotels making an appearance rather than mid-range hotels. International hotel brand penetration is increasing in the market and there are new hotels in the pipeline, but at the moment there are more development opportunities than transactions. Part of the market has been hit by trade sanctions with Russia, so despite moderate GDP growth estimates, we predict only moderate growth for 2016.

Finland

The Finnish market has been stagnating for a couple of years and GDP growth rate for 2016 is at the lower end of the Eurozone. Economic growth is being kept to a modest level further fuelled by the current trade sanctions with Russia. In 2016, Helsinki's market growth will be partially hampered by new supply entering the market as Nordic Choice, Cumulus and Fabian are expected to open new hotels. However, there are opportunities ahead; we are currently advising on several other developments with potential for international operators who are looking to open hotels after 2016.

City growth ahead

In 2016, Stockholm and Copenhagen will both continue to absorb the increasing volume of visitors and rates may rise gradually. Some new supply is anticipated in Stockholm in the next couple of years, predominately from national or regional brands. The long awaited penetration of international brands has been postponed mainly due to the operational structures required by domestic investors historically. However, there are some early signs that there will be a solution for this in the next year or so. Copenhagen has suffered from high barriers of entry for new supply and operators as there are limited vacant properties or sites available. Therefore, there are only two or three potential developments that could conclude after 2016.

Russia

The Russian market keeps growing despite challenges such as a poor exchange rate which will hamper growth in 2016. We have seen new hotel development not just in Moscow and St Petersburg but also in Sochi, for example, due to the 2014 Winter Olympics. There are approximately 6,000 rooms being developed for the Fifa World Cup 2018 across the country although there is a concern whether demand for these rooms can be sustained after the event.

Boosting trade

Apart from limited supply, the lack of trading across all regions could be down to a lack of visibility in the market. Christie & Co is working to make the market more liquid by providing a platform to allow investors to market assets more effectively and understand the dynamics of the markets and regions. To serve these markets better Christie & Co opened its Stockholm office in April 2015 as a response to the Swedish Hotel market being the fifth most active in Europe in 2014. We now offer a wider pan-Nordic platform using our in-depth knowledge of the region.

"The Swedish economy has been growing strongly since 2009 and the outlook for 2016 is positive."

Marcus Josefsson, Consultant Scandinavia, Russia and the Baltic States

Given the link between economic growth and demand for hotel rooms, we anticipate strong future growth in Sweden's Hotel market during 2016.

Though domestic travel has accounted for two thirds of the market in Stockholm historically, international visitor numbers are predicted to rise, particularly as Stockholm remains a popular international conference destination and Arlanda airport is due to expand; as of September 2015 international demand for rooms accounted for 43% in Stockholm.

As a market with relatively few international brands, now is an excellent time for overseas hoteliers to get involved with the strong pipeline of rooms under development.

Case study - Copenhagen Gate

Christie & Co was commissioned by Harbour P/S to prepare a feasibility study and advise on operator search and selection for one of the most significant development projects in the Danish capital - 'Copenhagen Gate, Gate L & Gate M'.

The planned development project is envisaged to consist of two mixed use high-rise towers located at the tip of Langelinie and Marmormolen piers with 24 floors and 27 floors respectively. These are connected by a bridge, giving the project its name. Besides office, bars and restaurants, the towers are planned to accommodate two hotels and potentially serviced apartments.

Following a feasibility study prepared for a proposed international full-service 4-5* hotel (12,000 m^2) and a limited-service 2-3 star hotel (8,000 m^2), the Nordic office of Christie & Co is currently actively involved in negotiations with potential operating companies for both hotels.

The construction start is scheduled for 2016/17 conditional on a satisfactory occupancy level. Harbour P / S and Christie & Co is actively engaged in finding tenants for the two towers, Gate L & Gate M.

"Although the first quarter of 2015 saw a slowdown in the French market, particularly in Paris due to the terrorist attacks at the start of the year, global performance looks stable compared with 2014, but we still need to analyse the potential impact of the November 2015 terrorist attacks in Paris."

Florence Mebrouk, Managing Director France

The draw of France

France remains a very popular destination for tourists from across the globe, with visitor numbers expected to hit 85m in 2015 and the tourism sector representing 2m jobs and 7% of the global GDP of France. The French Government is keen to improve the visitor experience further, so is likely to stimulate investments in order to increase lodging capacity over coming years. Consumer confidence in France lagged behind the rest of Europe, mainly due to the unemployment rate (c. 10%).

Investment

Investment for 2015 is estimated at €1.7bn. The majority of investors are still French institutional investors or US private equity funds. However, we are seeing the entrance of Middle Eastern investors, as well as many from China.

The biggest transaction in 2015 was Jin Jiang's acquisition of Louvre Hotels - from Starwood for €1.3bn, although this is not included in the annual investment total. Maranatha bought a €350m portfolio of six luxury hotels in Paris and Nice totalling c. 500 rooms from the Le Roy family. IHG sold the Intercontinental Paris Le Grand to the Qatari fund Constellation Hotels Ltd for €330m and the new owner is to spend an additional €60m Capex. The hotel comprises 470 rooms including 70 suites, as well as the famous Café de la Paix.

In 2016 we might see AccorHotels decide to have their HotelInvest division quoted as a new REIT (SIIC) as it has been an active buyer in recent years and could be large enough to stand alone.

Competition is high

Many investors seek a trophy asset in Paris, but at the moment there are no premium hotels coming to the market, so subsequently some investors have moved their search and are looking at other cities with a minimum of 250,000-300,000 inhabitants and at assets worth at least €20m. However, in general, investors are not interested in secondary cities although cities such as Lille, Strasbourg and Bordeaux do maintain their performance. Marseilles, Nantes and Toulouse suffer from too many rooms per visitor and returns are affected.

New asset types

In 2016, the rise of one new hotel concept in particular should continue in Paris - lifestyle hotels that target young travellers, such as Meininger, Generator or Christopher's Inn. However, they seek specific spaces with large, sociable bar/lobby areas so there are limited possibilities. Outside Paris there is still scope for the expansion of budget hotel groups such as B&B or Okko Hotels.

The rise of AirBnB

A notable concern among hoteliers is the rise of AirBnB, particularly in Paris which is the company's biggest market in Europe. The Paris administration is trying to control AirBnB use but this is difficult and AirBnB looks set to grow. Hoteliers will need to be more innovative in order to attract customers.

Case study - Coypel Paris

The Parisian Hotel market remains attractive and significant, especially when the asset presents a genuine potential for improvement and growth.

The sale of the Hotel Coypel also demonstrates the importance of alternative financing methods, such as risk-capital initiatives. Consistency between vendor price expectation and value potential was also decisive in this transaction.

"Performance in Ireland's Hotel market steamed ahead in 2015, particularly in Dublin where substantial growth in demand resulted in RevPAR growth above 20%. Strong performance was also witnessed in other parts of the country, with average RevPAR growth of around 10%."

Maureen Bayley, Director Ireland

Economic growth

In 2015, the market was buoyed by a robust economic performance and growth in Ireland surpassed expectations due to higher than expected domestic consumer confidence and spending. There has also been a significant increase in international visitors to Ireland, primarily from the UK and the US aided in part by favourable exchange rates.

Weak development pipeline

Dublin's Hotel sector growth is somewhat hindered due to a lack of pipeline of future bedroom stock. Very few opportunities have come on board over the last few years relative to the level of inward investment growth in the economy and improvement in consumer sentiment. There are a number of hotel development projects mooted for Dublin city however the majority will not come on stream before 2018.

Continuing High Levels of Activity

Across Ireland, while there were marginally fewer asset disposals in 2015 than in 2014, the volume of spend in the sector increased overall through rising values across the country along with increased appetite for lending to the sector from the domestic banks. A large number of hotels that have been in distress situations with their lenders for a number of years have now transacted, or have been refinanced out of these distress situations, while a significant portion of the balance were traded by the banks via portfolio loan sales. The banks are advancing their final phase of deleverage in 2016. While the biggest sales to shape the Irish Hotel market in 2015 was Dalata's acquisition of the Bewleys Moran Portfolio and Loan Star Funds acquisition of Jurys Inns for €455m and €970m respectively, there have been a number of significant single asset disposals over the year, highlighting the healthy interest in the sector from both domestic and international investors.

Investor market

Irish hotel groups and investors have been highly acquisitive since 2013 and are looking at all opportunities that arise, but there is also demand from overseas investors looking for trophy assets. John Malone has emerged as one of the biggest buyers of hotels in Ireland over the last few years having teamed up with local developer/businessman John Lally. Other active domestic investors include Tetrarch Capital, Dalata Hotel Group, McGettigan Hotel Group and Great National Hotels to name a few.

Investment

For the economy and the Hotel market to continue to grow, further investment is needed. Ireland has seen a lot of infrastructure improvements over the last 10 years but more needs to happen for it to remain competitive both as a travel destination and as a country. Works are currently underway on the LUAS interconnector line (LUAS Cross City) in Dublin and other infrastructure improvements are mooted, particularly in relation to public transport.

Predictions

- More supply is needed for Dublin and until this comes, rates will continue to be pushed. There is only one new hotel confirmed to open in the city, which is the Holiday Inn Express on O'Connell Street due to open by mid-2016.
- In terms of transactions, we have yet to see second round sales of hotels bought out of the property downturn, but these will come. As market norms return, we would expect to see some 'natural churn' occur.
- "We will see a number of new international investors entering the market for both prime Dublin and more regional hotel assets over the course of 2016".
  Dave Murray, Director of Brokerage - Ireland

"Poland's Hotel market has been growing for several years and 2015 was no different. Investor interest is at a high, matched by a rising number of rooms coming to the market."

Adam Konieczny, Country Head Poland

Tourists keep coming

Poland's popularity among tourists, both foreign and domestic, has been increasing and this is likely to continue in 2016. Demand and occupancy rates have been on the rise for several years, particularly in Warsaw, Krakow and the Tri-City area around Gdansk, Gdynia and Sopot.

Investors take note

Poland's Hotel investment market may still be in its infancy, but there are many reasons why investors are convinced of the country's potential. Factors include the improvement of hotel indicators, more hotel chains, the enhancement of the country's meetings and conferences industry, improving road and rail infrastructure, and also favourable property prices in comparison to key European markets such as London, Paris or Munich.

In general, investors are mainly looking for branded, well-established business hotels, while chain-affiliated city-centre economy or mid-scale hotels are proving to be successful. There were a number of notable transactions in 2015, such as Union Investment's acquisition of the Radisson Blu in Wroclaw from UBM Development Group AG, and the acquisition of the Sheraton in Warsaw as part of a Pan-European portfolio by Benson Elliot and Walton Street Capital.

Overseas money

There is rising interest in hotel acquisitions from German, French, British and American investors. Paradoxically, the crisis in Ukraine seems to have had a positive effect on the Polish Hotel investment market since those investors who previously planned to put their money in Ukraine and Russia are now withdrawing from those markets and moving West, allocating their capital in countries such as Poland.

The rise of mid-range hotels

While Poland's Hotel market is still dominated by the upscale segment and investors are keen to have trophy assets in their portfolios, we have observed a shift in interest from the high-end towards the midscale market and more sustainable hotels. There is also strong potential for investors in the budget sector, as expansion plans in this segment have so far been rather limited. Until recently, the majority of investors were only interested in lease agreements, but now they are increasingly considering management contracts.

Predictions

- The outlook for Poland's Hotel market continues to be positive with new hotel developments, new chains coming to the market and investors expanding their gaze to include regional cities.
- As we are observing significant rises in the number of visitors, we are predicting ADR increases this year, particularly in Warsaw where new supply was limited.
- Good KPIs will encourage developers to prepare new projects with limited availability of plots in the city centre of Warsaw potentially leading to conversion projects, most notably in office buildings from the 1990s.

Case study - Warsaw

The Warsaw office has been involved in a number of hotel advisory and valuation assignments.

These include due diligence support for a planned mid-tier hotel with 300 bedrooms in the city centre of the Polish capital as well as a RICS compliant valuation of a branded budget hotel with close to 150 bedrooms in Wroclaw for an international operator. Also, with the annual conference Spotlight Hotel Investment Poland – which Christie & Co co-organised for the second time in 2015 and attracted more than 200 attendees – Christie & Co Warsaw successfully established a platform for players in this emerging Hotel market.

"The Spanish Hotel market in 2015 has seen a clear recovery after the worst years of economic downturn. In 2012, investment in Spain's Hotel sector totalled €540m while in 2015 the total surpassed €1.6bn. The market is highly active and we expect there to be a rise in transactions in 2016."

Inmaculada Ranera, Managing Director Spain & Portugal

Tourists continue to arrive

Spain has made a remarkable economic recovery and the tourism market continues to flourish. In 2014, Spain received almost 65m visitors and in the first seven months of 2015, 38m foreign visitors arrived in the country, a 4.7% rise on the same period in 2014. Occupancy and ADR figures have increased year on year. RevPAR has grown on average 4% over the past five years, though there is still room for rate growth compared to the rest of Europe.

Investors' interest increases

Spain has again become an attractive option and both domestic and international investors are highly active. International transactions such as the sale of Barcelona's W Hotel to a Qatari fund and the purchase of Madrid's Hotel Ritz by a joint venture between Mandarin Oriental and the Saudi conglomerate Olayan Group, show the increasing interest from the Middle East and China. We have helped a number of overseas funds to carry out due diligence processes regarding hotel assets in Spain and we expect this appetite to continue in 2016.

Interest expands

Madrid's market is booming and values are now starting to top those in Barcelona. However, although there is still some difficulty in secondary cities where domestic demand has not yet returned, both tourists and investors are starting to look further afield. Seville, Valencia and Malaga are improving and there is already a lack of opportunities in Bilbao and San Sebastian. The interest of international investors continues in consolidated holiday destinations such as the Canary and Balearic Islands. Difficulties faced by other countries with Mediterranean coasts are driving more tourists to these locations, which are seeing their records surpassed every season.

REITs emerge

Spain's first hotel REIT was formed between Hispania and Grupo Barceló in 2015 with an initial investment of €421m in 16 hotels with an aim to add and manage 12,000 rooms across the country. We expect to see growth in this area this year.

New projects emerge

Appetite is strong for new hotel projects, though most focus on building conversions rather than new developments as the market remains cautious. Several landmark and office buildings are being converted in Madrid, Malaga and Barcelona. Across the county, 80% of current projects are related to 4 or 5 star hotels, and 84% of the projects are concentrated in consolidated destinations: Madrid, Barcelona, Malaga or the Balearic Islands. It is expected that these developments will attract more international brands to the country although hotel owners and operators will have to make efforts to differentiate themselves in this increasingly competitive environment.

Case study - Hotel Amaral

After the re-opening of the Madrid office in September, the first deal was brokered in the city in November.

The Hotel Amaral, a 3 star hotel with 126 bedrooms was leased by Playa Senator, a chain that is expanding on its development plans in Spain.

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