HOTELS

The UK hotel market continues to show encouraging signs of growth, in terms of RevPAR performance, supply growth and investor appetite.

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Portfolio sales were a prominent aspect of the market in 2018, with the likes of Starwood's Principal Hotels (c.£860m), Apollo's portfolio (c.£750m), Lonestar's remaining Amaris portfolio of Mercure and Hiltons (c.£600m), and Oaktree's Saco Apartments (c.£430m). The market also remained buoyant for regional, single asset transactions, a trend which is likely to continue into 2019.

UK GROWTH

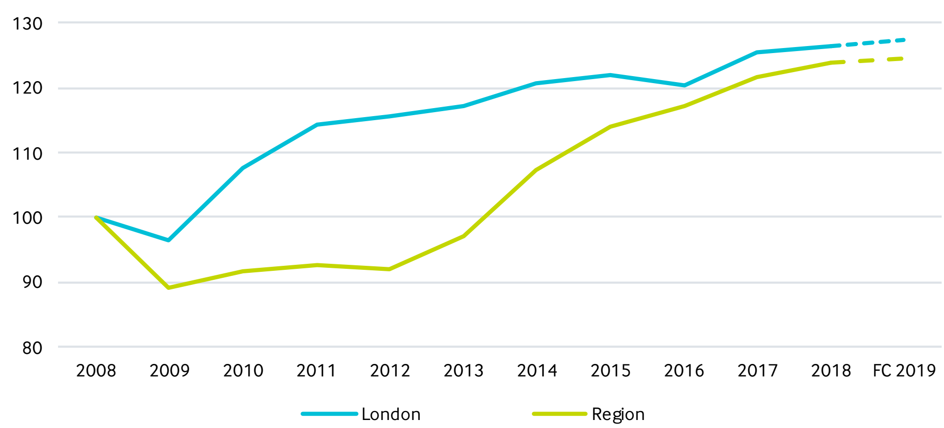
The hotel sector as a whole displays continual evidence of innovation and evolution, through the creation of new and exciting brands and dynamic new hospitality concepts, in keeping with ever-shifting consumer expectations in the sector.

Hotel performance in 2017, although particularly strong, represented somewhat of a market irregularity as the impact of a devalued Sterling generated substantially higher levels of inbound tourism than experienced in previous years. Stabilisation of the Sterling in 2018 has consequently restrained such exaggerated levels of tourism and 2018 has inevitably proven a more challenging year for hoteliers off the back of 2017's strong performance.

Despite subdued year on year consumer behaviour, 2018 displayed positive performance metrics and occupancy and ADR both remain extremely strong in London and the regions. Encouragingly, RevPAR strong growth is also forecast for both London and the regions, with increases of 1.8% and 3.0% respectively from 2017-2019. This will predominantly be driven by rate increases but 2019 performance may be influenced by Brexit developments to some degree too.

In terms of new supply additions to the market (from July 2018 through 2019), there is likely to be over 10,500 new rooms in London across 85 hotels and as many as 25,500 new rooms in the regions across 295 hotels. Specifically, in the regions, the vast majority of this pipeline development is located within key gateway cities including Manchester, Belfast, Edinburgh and Liverpool. Despite the growth of alternative accommodation providers like AirBnB, hostels, and aparthotels, it doesn't appear that this will dramatically impact consumer demand the hotel market.

CHRISTIE & CO 2019 REVPAR FORECASTS (REBASED 2008 = 100)



2018-19 RevPAR Growth Forecast

London:

+0.6%

Regional:

+0.7%

Source: STR, Christie & Co Analytics

MARKET PREDICTIONS

Significant developments in technology are growing and may assist in customer experiences, cost savings and even increased productivity.

CASE STUDY
Hilton Coylumbridge

Christie & Co sold Hilton Coylumbridge, situated on a substantial estate in the Scottish Highlands, on behalf of an affiliate of Starwood Capital to Britannia Hotels.

More choice means that the sector as a whole is able to cater for different types of traveller demographic and different needs, albeit it may create some added competitiveness in price.

Going into 2019, it is likely that both London and the regions will continue to perform well, albeit at a more subdued rate of growth. These positive performances would be supported further if exchange rates remain low, making the UK more attractive to international tourists and a more cost-effective option for UK residents than travelling abroad, hence the continued benefits to the industry from 'staycations'.

FACING HEADWINDS

Whilst we foresee top line revenue remaining relatively stable, with marginal growth potential possible, it will certainly be the underlying profit margins where owners and operators will encounter challenges in 2019. Due to hotel values being inherently linked to profitability, this will ultimately have a wider influence on investors' and lenders' attitudes within hospitality.

The costs and usage of online travel agents has been well documented and is now an important part of the consumer booking system. Another substantial challenge facing operators is the impact of the National Living Wage (set to increase 4.8% to £8.21 an hour in April 2019). Not only will this increased operational cost put a strain on profitability, it will also make the process of sourcing and securing quality staff within hotels more challenging. Compounding the numbers of hotel staff departing the UK many are also pursuing alternative career opportunities outside the hospitality sector. In addition, exchange rate movements have impacted the cost of goods imported, utility costs have increased, as have business rates. When considered together, these headwinds are considerable.

CASE STUDY
Eynsham Hall

Christie & Co sold Eynsham Hall, one of Oxfordshire's leading country house hotels, on behalf of Cathedral Hotels to Ennismore. Eynsham Hall was sold off an asking price of £8,250,000.

Portfolio sales were a prominent aspect of the market in 2018, with regional, single asset transactions keeping the market buoyant

Whilst operational performance will come under pressure in 2019, macro-economic factors such as inflationary pressures and potential interest rate movements may lead to an increase in distressed positions, likely to occur in H2 2019.

CASE STUDY
Five Marriott hotels

Christie & Co acted in the sale of five Marriott hotels, spread across the north east and south of England, to Britannia Hotels for materially more than the combined asking price.

INVESTOR APPETITE

The UK hotel market remains an attractive investment proposition and appeals to a wide range of buyers. International interest has continued with capital from across the globe, particularly from European investors, making up more than 50% of UK investment in 2018.

This was largely influenced by France, but with notable investment from Sweden, plus investors from the Middle East, North America, high net worth individuals, family funds and institutional investors.

Ultimately, the UK market continues to provide a favourable landscape for investors, with appeal continuing to come from the specific asset and its location, price, performance drivers and exit value.

BREXIT

The UK hospitality sector employs 2.9 million people, representing 10% of UK employment and within this number, over 400,000 are EU migrant workers. Under EU treaty provisions, workers are free to enter the UK without any form of work permit or visa, and employers have to undertake a "Legal Right to Work" (LRTW) check before they can begin working. This flexible labour market has proven to be hugely beneficial to employers in the hospitality arena, however over the past two years there has been a shortage of workers due it no longer being the attractive destination for foreign job seekers that it has traditionally been. The main ways of addressing these concerns and retaining staff have been through improved remuneration, a review of staffing rotas, better training and career progression.

The impact on exchange rates has already been seen over the last couple of years. Currency values have positively impacted tourism visitor numbers, with the Sterling's weakness against the Euro and Dollar encouraging international visitors. Where the exchange rate will trade during 2019 is up for debate and likely to depend on a number of economic factors including Brexit, inflation and interest rates. The weak currency is also a significant benefit for overseas investors, making the UK more attractive for international capital.

Whilst risks can be analysed and measured and therefore decisions can be made, uncertainty is much more difficult to quantify and normally hinders investment decisions being implemented. The current uncertainty in relation to the Brexit details, whether we will have a no Brexit deal, the potential impact on the Government and a potential future general election, may impact investors' confidence.

With lower RevPAR growth and significant increases in bedroom supply and overall operational costs, we anticipate that hotel operators are likely to experience either flat or negative movement in 2019's profit margins.