Colliers Hotel Insight

A quarterly digest of key trends in the hospitality sector

Inside this issue

HOTELS – Outlook 2018
OPINION – Key Trends for 2018
HOTEL INVESTMENT – Short-term cap rate expectations 2018

Accelerating success.
“Global economic activity continues to firm up. Global output is estimated to have grown by 3.7 percent in 2017... The pickup in growth has been broad based, with notable upside surprises in Europe and Asia. Global growth forecasts for 2018 and 2019 have been revised upward by 0.2 percentage point to 3.9 percent. The revision reflects increased global growth momentum and the expected impact of the recently approved U.S. tax policy changes. Risks to the global growth forecast appear broadly balanced in the near term, but remain skewed to the downside over the medium term.”

- IMF WEO Jan 2018

Foreword

It’s been a year since we launched our first Hotels Insight and what a busy one it has been! Colliers Hotels is quickly becoming well recognized for its value added, specialist advice that caters to clients’ bespoke needs whether advisory, valuation or brokerage. We look forward to building stronger and even more relationships in 2018.

On that note, welcome to the H2 2017 edition of Colliers Hotels Insight, our quarterly magazine specifically for hotel and other accommodation stakeholders across Asia. This edition features key trends in various destinations across Asia, a highlight of key industry disruptors, and a technical section. We also provide insights and opinions on topical issues within the gaming and leisure sectors.

2017 was certainly the year that political risk once again took centre stage, and firmly set to remain so into 2018 across Asia, Revenue Per Available Room (RevPAR) performance for 2017 (YTD Nov) has been relatively stable, registering a growth of 2.9% on the previous year’s performance. While Central and South Asia properties had the best performance with strong 5.0% growth YOY, North Eastern Asia properties posted 1.5% growth, representing the slowest growth rate, mainly perpetuated by political events.

Overall supply growth paired with a general slowdown in domestic and international consumption has weighed on performance, as disposable income remained tight across the region and globally.

We expect geo-political risk, especially in Northeast Asia, to remain a key factor during the year. Investment is likely to remain largely domestically driven, as initial yields in gateway cities are continuing to remain at relatively low levels. Emerging markets are offering higher returns to compensate for risk bearing and attention remains on the gaming, theme park and wider experiences sectors. The increased Anti-Money Laundering (AML) requirements on casinos and banks, in addition to the full/partial smoking bans in some destinations are likely to weigh on the performance of the gaming sector.

In brief, the outlook for hotels across Asia will remain cautiously optimistic, with asset management, consolidation and effective marketing likely to be the key themes emerging.
Colliers Hotels

Colliers International launched its specialised hotels division in 1985. Today we provide expertise in capital valuations, management agreements, rental advisory feasibility studies, asset management and transaction advisory services, as well as brokerage across Asia Pacific. Our dedicated hotel specialists are based in Australia, Hong Kong / China, India, Singapore and Thailand.

We regularly act on behalf of major institutional property owners / funds for their valuation needs, from single strata units to composite developments and golf courses, for all purposes, including IPOs, listings, acquisitions, disposals and mergers.

In Asia, our team of professionals provides hospitality services across Greater China, including the Mainland, Hong Kong, Macau and Taiwan, as well as Bangladesh, Cambodia, Guam, India, Indonesia, Japan, Korea, Laos, Malaysia, Maldives, Myanmar, Pakistan, Philippines, Singapore, Sri Lanka, Thailand, and Vietnam. Our sizeable hotels, hospitality and leisure team includes senior specialists with extensive experience in the sector, giving us a unique advantage and insight.

Our multi-lingual and multi-cultural team comprised of highly qualified professionals will help clients achieve their real estate goals. Colliers’ professionals have extensive operating and consulting experience in the hospitality industry across the major asset classes, which provides clients with extraordinary value and a single point of contact, through timely, relevant and forward-looking advice. This global division has exceptional relationships with investors worldwide, required for the timely and effective sale of assets. In addition, they have worked with a wide range of clients including corporate hotel clients, private equity, sovereign wealth funds, independent owners, REITS, governments, and banks.

Our Services

Whether you are a startup or well-established owner, developer or investor, we will help you go through the business life cycle by providing specialised, value-added advices that are tailor-made to your specific needs:

- Market Demand and Feasibility Studies
- Valuations – Property and Business
- Plant and Machinery Valuation
- Impairment Testing
- Capital Markets
- Due Diligence
- Internal Business Reviews
- Operator Search and Select
- Benchmarking and Forecasting
- Growing the business: extensions, refurbishments, brand roll out and expansion
- Asset Management
- Business Restructuring – opco / propco
- Needs Analysis / Economic Impact Studies
- Highest and Best Use / Concept Designs
- Transaction Advisory, IPO and REITS listing
- Management Agreements and Lease Reviews
- Litigation Support and Dispute Resolution Project Management and Leasing
- Tourism Strategy and Master Planning
Our Hospitality Sectors

Our track record includes all main asset types from hotels to resorts, heritage properties, serviced apartments, vacation homes, casinos, theme parks, spas, and golf, all being completed projects or new developments. Our specialised sector expertise includes:

> Hotels and Resorts
> Golf
> Casinos and Racecourses
> Health and Fitness
> Spas and Wellness Facilities
> Meetings and Events
> Mixed-use Developments
> Travel Trade
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Tourism arrivals to the Asia Pacific region are expected to have grown by 4.5% in 2017 when compared to 2016, continuing a steady period of growth witnessed since 2010, following the global financial crisis. This rate of growth is expected to continue into 2018, with tourism arrivals in the region reaching record levels. Growth continues to be mainly driven by China and India with the latter in particular set to expand as its GDP per capita improves along with its robust economic growth.

Continued improvements in low cost air transport and accessibility, together with the improving quality of room stock, especially in emerging destinations should continue to provide a platform for those destinations to attract much needed visitation. This will be supported by improved infrastructure as evidenced by the recent opening of Changi Terminal 4 and completion of Phase I of Jakarta’s Soekarno-Hatta Airport. Beijing’s new airport is slated to open in 2019, just in time for Universal Studios and the Winter Olympics. Rail links and public transport improvements are also set to enhance the visitor experience in some destinations such as Manila, where the opening of the Skyway express road, has drastically reduced transfer times to the Makati CBD area from the airport, and the newly opened rail link between Soekarno-Hatta Airport and downtown Jakarta.

Overall, we expect tourism arrivals in 2018 to mirror that in 2017, with another 4.5% growth expected for the region. Geo-political risks, foreign currency movements, absorption of new hotel stock and a slowdown in investment in the sector are likely to be the key themes. Having said that, we do expect some bounce back in performances in destinations such as Seoul and Taipei, both of which experienced a challenging 2017.

RevPAR growth in the region is closely correlated to that of economic performance in Emerging and Developing Asia. This highlights the importance of intra-regional and domestic tourism to destinations, the latter of which is sometimes overlooked. According to STR, RevPAR (in US$ terms) across Asia Pacific improved by a modest 0.7% year to date November 2017, with Australia, French Polynesia and New Zealand being the main drivers. Seoul and Taipei were the worst performing markets.

On average, in 2018, we expect RevPAR growth to continue to be impacted by foreign currency movements, the further evolution of low cost carriers (LCC) and the destinations they serve, together with economic performance and consumer confidence in key source markets. As such, our forecast for RevPAR growth in 2018 is circa 3.0% year on year.

We end with a note which, according to a survey by Carlson Wagonlit, a travel company, we can expect the sharing economy to compete for business travellers on a limited basis, and corporate budgets to remain tight and generally continuing to shy away from luxury.
Destinations to watch in 2018

Our top picks for destinations likely to witness the most growth in 2018. This is based on recent and expected growth trends in international overnight visitation, economic outlook, and the proposed further easing of policy including visa restrictions.

- Xi’an
- Chengdu
- Tokyo
- Colombo
- Xiamen
- Jakarta

In our view, across Asia, Bangkok, Singapore, Hong Kong, Tokyo, Kuala Lumpur and Taipei are expected to firmly remain the leading Asian destinations of choice in 2018.
Key trends for 2018

The tourism sector in Asia has more room for growth in 2018, after posting a strong performance in 2017. An improving regional economic outlook and an upturn in global business and consumer confidence were among the key growth drivers that spurred regional tourism during the last year.

Asia-Pacific is a powerhouse for tourism growth, with the region poised to attract some 321 million foreign arrivals in 2017, an increase of 5.6% on the previous year. This is according to the World Travel and Tourism Council (WTCC) which projected an annual growth of 4.4% in foreign arrivals to the region over the next 10 years.

The growth will mostly be underpinned by South Asia, and in particular India, which at 6.7% per annum, is expected to be one of the fastest growing regions for tourism over the next decade. Accounting for around 10% of gross domestic product (GDP) and one in 10 jobs, it is the only sector that has shown consistent growth over the last six years despite the pandemics and natural disasters. This is clearly a sector that is not only sustainable but forms a vital part of many country’s economy within the region.

Key tourism themes in 2018

1) Rising confidence and optimism

Across Asia, in 2018, we expect visitation - or visitor arrivals - to be underpinned by increasing business and consumer confidence. This in turn will drive many tourism segments including meetings, incentives, conference and events (MICE) as well as business travel combined with leisure.

Visitation to well-established destinations such as Bangkok, Singapore, Hong Kong, Tokyo and Kuala Lumpur will continue to be healthy. Meanwhile, emerging destinations such as Bagan, Osaka, Chengdu, and Colombo are expected to continue to witness double-digit increases in visitation.

2) Upturn in cruise industry

The anticipated upturn in the cruise market will contribute to regional tourism growth in 2018. The cruise business is becoming increasingly desirable, especially those with home ports in Singapore, Hong Kong, Japan, China and Thailand.

According to the Asia Cruise Trends 2017 Report, cruising in Asia is set to reach 3.7 million passengers by the end of 2017, a startling compound annual growth rate of almost 40% since 2012. This increase was primarily driven by a growing Chinese and Indian market. Most Asians prefer to cruise within the region, and the sector is set to continue to expand with double-digit growth in the coming years with several large operators such as Genting (with its new Genting Dream), Royal Caribbean, Carnival and Cunard all expanding capacity.

3) Strong demand for health and wellness

With an ageing and increasingly wealthy population, the market for health and wellness in the region is seeing significant growth. Already we are witnessing trends in higher demand for vegetarian and organic food, with yoga and health and fitness becoming more established in day-to-day routines.

Corporate wellness, already well established in Japan, is quickly catching on in China, and is expected to witness the highest level of growth in the region. Within Asia, Japan, South Korea, Thailand and Indonesia remain the top wellness destinations, with China, India, Japan, South Korea, Vietnam, Indonesia, Thailand and Malaysia the largest domestic and international source markets.

According to the Global Wellness Institute, the wellness tourism in Asia-Pacific is worth around US$111.2 billion as at 2015, dominated by beauty and anti-ageing, nutrition, fitness and personalised medicine. Wellness tourism is projected to grow by 7.5% per annum over the next five years.

China and Japan dominate in 2017, but India is catching up

China and Japan dominated both international and domestic travel in 2017, although India with its sizeable population and increasing wealth is snapping at their heels.

We expect this trend to continue in the short to medium term, with Chinese travellers becoming more sophisticated in their choice of experience, and more Indians travelling abroad. Increase in cross-border investments, further proliferation of low cost carriers, improved accessibility and further easing of visa restrictions will underpin future growth both internationally and domestically.

On the downside, the introduction of tourist taxes, increased visa fees and geo-political concerns, not to mention currency movements will be key influencers going forward with some countries emerging as winners and others, losers.
Key sector trends for 2018

Foreign currency movements - US interest rate policy will continue to influence currency movements across the Region, with weaker currency destinations likely to continue to benefit from inbound travel. Destinations with appreciating currencies are likely to witness some contraction in ADR growth. US interest rates seem to be on an upward path. President Trump has inherited a strong economy poised for continued moderate growth. The planned stimulus package of tax cuts and infrastructure spending should boost growth, but at the cost of higher inflation and interest rates.

LCC - the impact of low cost carriers has been dramatic on tourism arrivals in recent years (take a look at Singapore when it expanded its LCC offering in 2000, and Japan in 2012). This segment is likely to continue to grow, and as existing and new destinations open up, we would expect visitation to follow suit.

Consumer confidence - Asian economies are mostly healthy. Consumer confidence is likely to strengthen gradually across the region. This is likely to influence consumer confidence thereby boosting business and leisure travel. However, lack of hotel supply in some destinations (Tokyo), and too much in others (Singapore, Bali and Shanghai) is likely to temper growth.

Operator consolidation - we are in the cycle where, after a period of divestment, we are once again witnessing consolidation across the hotel industry. We have long held that once markets have matured and the pipeline of additional hotel stock slows, the main way for hotel companies to realise value is through consolidation. In 2018, expect more vertical consolidation as hotels try to reduce the impact of Online Travel Agents (OTAs).

Emerging markets - this represents the best opportunities for further brand penetration across the region and indeed for investors chasing yield. Political risk is being reduced in ASEAN countries, and with visa restrictions being eased, destinations in these areas are expected to continue to attract strong growth (Vietnam and China Tier 2 cities are examples).

Mid-market and lower segments - in mature destinations, we consider these segments represent good value for money investment opportunities. In China, Taiwan, Hong Kong, Singapore and Japan, these represent growth segments given the low penetration of good quality internationally branded stock in these segments.

Technology - more and more technology is being seen as an alternative to lower costs and improve guest experience. Expect more of this in 2018 as smart technology continues to evolve. Existing platforms, especially marketing and booking engines are also likely to continue to improve particularly for mobile devices. Hoteliers will need to ensure they are not left behind and the forefront of search engines especially as they gear up to drive the volume of direct bookings.

The return of value for loyalty - after a period where the value of being loyal was being eroded, expect programs to be revamped to foster instant recognition for loyalty members. This will include free Wi-Fi, discounted room upgrades, F&B discounts, and access to price match or lower rates than those being offered by OTAs.

Smaller rooms and co-living – whilst not a new concept, expect capsule hotels with habitable spaces to grow in demand as the new wave of socially adept travellers take flight. These concepts will also offer good investment alternatives, with strong return on investment and easy conversion and build costs.

Cruising – the cruise market in Asia has witnessed an exponential growth in demand with passengers increasing from 0.8m in 2012 to 4.2m in 2017e, a healthy 430% in just six years. China accounts for over 65% of passengers, although demand is rapidly growing from India. Expect destinations that offer home ports and fly and cruise to do well.
Hotel Investment and Valuation

Capital markets insights

China remains one of the main sources for hotel investment across Asia. The country's position to restrict offshore capital flows last year clearly has had a direct impact, with outbound investment decreasing and deals closer to home in favour. Nevertheless, real estate remains a core investment for most Chinese investors.

Year on year, hotel transaction volume has increased by more than 10%, mainly underpinned by Dalian Wanda’s transfer of its China assets to a related party. The global hotel sector was not immune to a drop in transaction activity, however, the core “safe haven” markets show no signs of slowing down in the region. Singapore, Tokyo and Hong Kong assets continue to trade at compressed cap rates and record pricing despite a softening in demand and additional supply.

Geo-political tensions have led Asian real estate investors to refocus on regional investments, while global interest in trophy and opportunistic acquisitions continues.

Despite capital controls, preliminary data from RCA suggest that total Chinese investment in foreign property assets increased slightly in 2017 from 2016, both including and excluding land development sites. Real estate remains the preferred vehicle for mainland buyers, and hotel investment, though slower, remains the preferred alternative asset class. Overall, despite strong demand driven by both family offices and private equity with Asian real estate mandates, quality inventory remains scarce. Investors with disposition scenarios in the next 18 months, should consider expediting their processes in order to take advantage of favourable market conditions and rich valuations, especially as the outlook for increases in interest rates remain high and as inflation gathers pace.

Of note, as asset prices remain high, investors are now considering taking more development risk, however, this risk must be shared with the developer who not only is required to contribute “real” equity into the project, but also to provide put options guaranteeing a mandated exit to shareholders. These terms are not new to hotel developments but becoming more common to developers looking to raise funds for emerging market projects.

Recent notable transactions

Continuous investment into asset class by institutional investors and the dearth of assets being sold show that yields have been low and are expected to remain at these levels, at least until interest rates increase significantly.

In 2017, most of the transactions across Asia came from gateway cities, where investors remain very active.

<table>
<thead>
<tr>
<th>Hotel</th>
<th>Location</th>
<th>Value per room (USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dalian Wanda China 74 Hotels Portfolio 2017</td>
<td>Various</td>
<td>118,943</td>
</tr>
<tr>
<td>Hotel Jen Upper East Beijing</td>
<td>Beijing</td>
<td>668,793</td>
</tr>
<tr>
<td>Hotel Sunroute Plaza Tokyo</td>
<td>Tokyo</td>
<td>386,538</td>
</tr>
<tr>
<td>Holiday Inn Central Plaza Beijing</td>
<td>Beijing</td>
<td>659,711</td>
</tr>
<tr>
<td>Ascott Residence Trust China Hotel Portfolio 2017</td>
<td>Various</td>
<td>335,419</td>
</tr>
<tr>
<td>Swissotel Nai Lert Park</td>
<td>Bangkok</td>
<td>394,483</td>
</tr>
<tr>
<td>Somerset Youyi Tianjin</td>
<td>Tianjin</td>
<td>407,893</td>
</tr>
<tr>
<td>Sofitel Bali Nusa Dua Beach Resort</td>
<td>Bali</td>
<td>298,800</td>
</tr>
<tr>
<td>Songjiang New Century Grand Hotel</td>
<td>Shanghai</td>
<td>264,602</td>
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<tr>
<td>Belgravia Place</td>
<td>Shanghai</td>
<td>1,132,105</td>
</tr>
<tr>
<td>Banyan Tree China Portfolio</td>
<td>Various</td>
<td>676,302</td>
</tr>
<tr>
<td>Four Seasons Resort Langkawi</td>
<td>Langkawi</td>
<td>1,055,964</td>
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<tr>
<td>Pullman Jakarta Central Park</td>
<td>Jakarta</td>
<td>306,270</td>
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<tr>
<td>Qingdao Copthome Hotel</td>
<td>Qingdao Shi</td>
<td>172,982</td>
</tr>
</tbody>
</table>

Source: Colliers Research.
Note: USD conversions are at time of transaction and represent approximate values.
Cap Rate Outlook 2018

Cap rates across markets, like hotel performance with its dynamic cash flows, will and can vary dramatically. The outlook for cap rates across the region in the short-term is widening, and much will depend on US Federal policy on interest rates, and the impact that will have on currencies, and capital flows. In addition, the economic outlook for key source markets could have an impact on profitability, which may lead to a widening of yields.

Cap rate outlook 2018

<table>
<thead>
<tr>
<th>City</th>
<th>Limited service</th>
<th>Full Service</th>
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<tbody>
<tr>
<td>Tokyo</td>
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<td>Taipei</td>
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<td>Singapore</td>
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<td>Shanghai</td>
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<td>Seoul</td>
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<td>Phuket</td>
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<td>Mumbai</td>
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<td>Kuala Lumpur</td>
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<td>Jakarta</td>
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<td>Hong Kong</td>
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<td>French Polynesia</td>
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<td>Guam</td>
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<tr>
<td>Bali</td>
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<tr>
<td>Bangkok</td>
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</table>

Source: Colliers International
Colliers Hotels Valuations Service

Colliers has a rich valuation experience on multi-market portfolios across Asia Pacific. We undertake more than 250 hospitality valuations each year, including single assets and portfolios for reporting, financing and transaction advisory purposes. Our experience ranges from budget properties to ‘trophy’ assets, many of which also include mixed-use components.

We are currently engaged by a number clients to undertake the annual valuations for their properties for reporting purposes, on a rolling basis for several years. Our close relationship with clients paired with in-depth knowledge of the local markets allow us to perform valuations accurately and effectively.

The valuation team is supported by our Research and Advisory team within the local markets. The Research and Advisory team works closely with our business service professionals, capitalising on our market expertise to provide our clients the necessary market intelligence across all markets – ranging from data collection to comprehensive market analysis, interpretation and recommendations – required to support sound and practical business decisions.

Our market insight and knowledge are our clients’ property, pivotal in accelerating their success. The overall hospitality team is part of one of the largest in Asia Pacific that performs more than 250 valuations per year in the sector, and includes professionals dedicated solely to hotels, leisure and hospitality valuation work, as well as a number of published authors in the field.

Next quarter:

Opinion - High-end restaurants and hotels. Do they fit?
Hotels - Destination of the quarter – Xi’an
Gaming – Update on the Asian Gaming market

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396 offices in
68 countries on
6 continents

United States: 153
Canada: 29
Latin America: 24
Asia Pacific: 79
EMEA: 111

$2.6 billion in
annual revenue

2 billion square feet
under management

15,000 professionals
and staff

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Colliers International Group Inc. (NASDAQ and TSX: CIGI) is an industry-leading global real estate services company with 15,000 skilled professionals operating in 68 countries. With an enterprising culture and significant employee ownership, Colliers professionals provide a full range of services to real estate occupiers, owners and investors worldwide. Services include strategic advice and execution for property sales, leasing and finance; global corporate solutions; property, facility and project management; workplace solutions; appraisal, valuation and tax consulting; customised research; and thought leadership consulting.

Colliers professionals think differently, share great ideas and offer thoughtful and innovative advice that help clients accelerate their success. Colliers has been ranked among the top 100 global outsourcing firms by the International Association of Outsourcing Professionals for 12 consecutive years, more than any other real estate services firm.

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