

**NEW HOTEL ASSET MANAGEMENT
PRINCIPLES & PRACTICES
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GLOBAL ASSET MANAGEMENT CHAPTER

By

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Mr. Sogno began his career in New York City after graduating with honors at Ecole Hôtelière de Lausanne, Switzerland. Mr. Sogno established a number of business ventures, initially focusing on hospitality and real estate. He joined HVS International New York, and he established a new venture at the Cushman & Wakefield headquarters in Manhattan. During this period, Mr. Sogno supervised major hotel transactions (over 900 hotels), and provided technical support for valuations and financial projections for hospitality facilities throughout the USA, Canada and the Caribbean. In 2005, Mr. Sogno began working for Kingdom Hotel Investments (KHI), founded by HRH Prince Al-Walid bin Talal bin Abdul Aziz Al Saud member of the Saudi Royal family, and was employed to asset manage a large portfolio of luxury full-service hotels in 21 countries in Europe, Middle East, Africa and Asia. As Vice President of Asset Management, Mr. Sogno had diverse responsibilities including: asset management of various hotels including Four Seasons, Fairmont, Raffles, Mövenpick, and Swissotel, valuation of all KHI portfolio, assisting with the Initial Public Offering (IPO) of KHI at the London Stock Exchange and the Dubai International Financial Exchange.

AS WE ENTER THE 21ST CENTURY, a new world order is creating an increasingly interdependent global economic system as a result of declining trade and investment barriers, advances in transportation, telecommunication and a globally dispersed and integrated production and marketing supply chain for goods and services. All of these changes will have a significant impact on the travel, tourism and hospitality industry.

According to the World Travel and Tourism Council (WTTC) 2006 report, the global demand for Travel and Tourism in 2006 was expected to post \$6.5 trillion of economic activity, which is

expected to grow to \$12.1 trillion by 2016. The globalization of major operators and investment funds is the natural step in this evolution and asset managers have to embrace the new challenges. While operational savoir faire, financial expertise and valuation knowledge remain the necessary skills for asset managers, the challenges and opportunities of globalization must be comprehended in order to manage current international real estate portfolios.

Global Investments: Challenges & Opportunities

Global Economic Growth and impact on Travel and Tourism

Since 2004 world economic output has experienced the longest period of sustained growth for more than two decades. Economic and tourism growth has been driven, in large part, by emerging market and developing countries. While the more mature developed countries grew at the still respectable rate of 5.1%, the emerging market and developing countries grew at 7.7%. Access to last-minute inventory through online channels has continued to stimulate latent demand in more mature source markets, but also increasingly in less mature travel regions like Asia and the Pacific, where accessible pricing has opened up travel to an increasing number of people. The strong economic growth of the Asian economies, for example – China, India, Hong Kong (China) and Singapore – has resulted in greater disposable income which, in turn, has resulted in growing demand for foreign travel.

In 2007, international tourist arrivals grew by an estimated 6% to reach a record figure of nearly 900 million – an astonishing achievement given that the 800 million mark was only reached two years earlier. This represents nearly 52 million more arrivals than in 2006, well over the total count for either the Middle East or Africa. A recent survey conducted by UNWTOⁱ

summarizes the importance of global tourism trends and implications for international investments.

All the different regions registered increases; the Middle East leads the regional growth ranking, with an estimated 13% rise to 46 million in international tourist arrivals. The Middle East is emerging as a strong tourism destination with visitor numbers climbing much faster than in the world overall. In second place were Asia and the Pacific up by 10% to 185 million, followed by Africa, with +8% to 44 million. Africa confirmed its momentum sustaining the growth of 2006, and has now averaged 7% growth a year since 2000. The Americas (+5%) did much better than last year, achieving 142 million arrivals, driven by the good results in North America as the USA doubled its growth rate. Europe, the world's largest destination region, with a share of over 50% of all international tourist arrivals, grew by 4% to reach 480 million. Investing in these rapid growth emerging markets is lucrative and provides a higher return on investment than those from mature developed countries; however without local expertise, asset management can be challenging: for example operational impediments, legal issues, market constraints and risks.

Tables 1 and Tables 2 on the opposite page outline the global lodging performance and current and projected pipeline of hotel construction in different regions of the world.

Table 1

Lodging Industry Global Performance Trends

Global Performance (Data in US Dollars)									
Year-End	Occupancy		ADR		RevPAR		Change from 2006 - 2007		
	2006	2007	2006	2007	2006	2007	Occ.	ADR	RevPAR
Asia Pacific	70.6 %	69.6 %	\$ 115.58	\$ 129.33	\$81.55	\$ 89.98	-1.4 %	11.9 %	10.3 %
Central & South Asia	67.8	67.0	150.20	199.91	101.88	133.93	-1.2	33.1	31.5
Northeastern Asia	71.6	68.2	121.27	124.66	86.78	85.03	-4.7	2.8	-2.0
Southeastern Asia	66.9	69.5	87.57	107.75	58.57	74.91	4.0	23.0	27.9
Australia & Oceania	74.3	74.8	124.36	145.41	92.39	108.83	0.7	16.9	17.8
Americas	63.4 %	63.3 %	\$ 99.02	\$ 105.16	\$62.74	\$ 66.57	-0.1 %	62.0 %	6.1 %
North America	63.3	63.3	98.44	104.46	62.35	66.03	-0.1	6.1	6.0
Caribbean	68.2	66.5	195.75	206.44	133.59	137.35	-2.5	5.5	2.8
Central America	68.4	70.7	106.41	119.41	72.82	84.39	3.3	12.2	15.9
South America	61.8	63.8	92.18	109.39	56.96	69.76	3.2	18.7	22.5
Europe	68.9 %	69.1 %	\$ 137.74	\$ 161.25	\$94.90	\$ 111.45	0.3 %	17.1 %	17.4 %
Eastern Europe	66.0	65.6	160.57	185.80	105.99	121.83	-0.7	15.7	14.9
Northern Europe	72.0	71.7	139.52	165.76	100.44	118.93	-0.3	18.8	18.4
Southern Europe	65.2	64.9	137.99	161.23	90.00	104.66	-0.5	16.8	16.3
Western Europe	67.0	68.4	131.79	150.71	88.26	103.15	2.2	14.4	16.9
Middle East/Africa	66.5 %	69.7 %	\$ 144.50	\$ 168.26	\$96.11	\$ 117.28	4.8 %	16.4 %	22.0 %
Middle East	66.6	68.8	178.36	206.31	118.84	142.00	3.3	15.7	19.5
Northern Africa	66.3	72.7	79.66	91.77	52.82	66.75	9.7	15.2	26.4
Southern Africa	66.4	66.7	133.57	161.47	88.75	107.73	0.4	20.9	21.4

Source: The Bench, Global Partners with Smith Travel Research

Table 2

Global Hotel Construction

Global Pipeline & Forecast for New Openings					
	Total Projects	Total Rooms	2008 Forecast	2009 Forecast	2010 and Beyond Forecast
United States	5,807	779,307	133,623	170,417	505,936
Other Amer.	911	154,871	38,557	52,658	67,588
Europe	949	163,919	43,847	54,352	65,720
Middle East	527	155,989	27,558	43,428	88,805
Africa	146	29,727	8,170	9,216	12,341
Asia Pacific	2,218	495,867	144,039	172,340	179,488

The LE Pipeline consists of ground-up new hotel construction, condo hotels and real estate conversion projects that, when opened, will add to the future supply of guestrooms. The pipeline includes only those projects: Announced into the public domain, having dedicated land parcels, being actively pursued by the developer as of the close of the quarter.

Source: US based, Lodging Econometrics

Challenges, Strategies and Opportunities

Considering the growth momentum there are many positive trends emerging globally which international investors should consider and capitalize on. Overseas investments provide many benefits such as stronger growth rates and diversification. In addition, since hotel markets are not synchronized in their variation of value, common sense suggests that when one region is down there are opportunities in another. Many hotel owners are now geographically diversifying their portfolio to avoid excessive concentration in specific markets. Once investors have decided on investment goals and acceptable levels of risk, reviewing international investment opportunities becomes much less intimidating.

Common Challenges

Despite a geographically balanced portfolio the common risks associated with exposure to international investments remains a challenge and should be considered by asset managers.

Country instabilities – The lodging industry is often the first victim of terrorism, political instability and war. International investors will always have to face these issues and they are difficult to anticipate; but hotel owners should define their own acceptable levels of risk, be equipped to deal with crisis and have a diverse portfolio to limit the financial impact. If a hotel investor wants a higher return, they must generally accept more risk. The extra return for a given level of risk is the “risk premium” that is necessary to induce investor to invest internationally where cash flows may be more volatile. . Some recent examples directly affecting the tourism industry includes: the 2006 war in Lebanon (Middle East), Kenyan political instability following the 2007 election (Africa), Thai political unrest with the coup d’état in 2006 to blockage of airports in Phuket, August 2008 (Asia).

Legislative Practices – Governmental policies in emerging countries are often not transparent and legislators tend to implement unanticipated regulations without consulting their economic partners. These changes disturb the local economy and add more uncertainty amongst investors. The most common issues are capital structures and taxes. In some countries, such as Thailand, the tax laws are designed to protect local investors and restrict foreign ownership of real estate properties. As it can be cumbersome and expensive to create a tax efficient investment structure for the ownership of a foreign asset, reputable legal support is necessary. Another frequent example of legislative malpractice is with the state control of airport and regulated airline industry. The state owned airlines are often protected which limits the number of international carriers with airlift to the country. With government intervention and limited or no multi lateral open sky agreements,ⁱⁱ international tourist visitation is impeded. In addition, most emerging country governments control the airports and therefore the tourist flow. This is often used as a political tool as it allows governmental control of the development of certain areas in the country and their economic power. Due to their geographical condition, island markets are the most affected by this problem (e.g. Langkawi, Malaysia, Bali, Indonesia).

Currency Risk – Like other challenges that affect economic risk in a real estate investment, hotel investors must consider the fluctuation of the local currency against their own. In 2008, the strength of certain currencies against the US Dollar, notably the Euro, presented a challenge for the hotel industry, particularly in Europe, which saw a downturn in visitor numbers from the US and UK. The reverse effect was that the US benefited from influx in both European and Asian travelers. The Middle East, where most currencies are pegged to the US Dollar, hotel

performancesⁱⁱⁱ achieved double-digit growth since 2003. In many emerging markets, hotels are now quoting their room rate in Euros rather than the traditional US Dollar. The Asian currency crisis following the 1997 bursting of the real estate bubble in all major Southeast Asian cities, the Indonesian economic meltdown in 1998, and the more recent depreciation of the Thai Baht following political unrest and escalating inflation rates in Thailand has also affected trading performances. Such examples demonstrate currency risk is very real. Investors in foreign market must diversify their locations to alleviate exposure to currency risk.

Prices of commodities – Increase in oil prices, spiraling construction costs, and also higher land prices often result in developers finding it harder to secure financing, and when they do it's almost certainly at a higher cost. The current development hot spots include Eastern Europe, Morocco, United Arab Emirates, Qatar, India, Vietnam, Macau SAR, Hong Kong SAR, Taipei and Singapore. While these developments will stimulate previously untapped demand, some projects may also face further delays due to commodity prices. Projects that offer lower operational risk, such as those in prime locations with an experienced operator, are more likely to proceed.

Operators Challenges – International hotel operators face additional challenges created by the nature of their decision to expand globally:

- Outside US and Europe, other operators are much smaller and often hotels are independent. Lack of scale for small operation limits their distribution system and revenue/yield management. The limited corporate marketing support results in excessive dependence on the tour operators. This is particularly true for resort hotels.

- Most of the operators are currently challenged by the rapid growth of their footprint and often the owners pay the price. Beside the human resources challenges and limited marketing, often operators are also not as accountable for their financial projections in Asia.
- Implementation and monitoring of brand standards results in wide service disparities between the properties managed by the same operator.
- Establishing and using criterion to select the optimal brand affiliation for the owner. These selection factors may include analyzing the business mix, assessing the benefits versus cost, and potential conflicts of interest and impact issues associated with territorial restrictions, such as the proximate market positions of two brands, which are owned by the same operator, such as The Ritz Carlton and Bvlgari brands in Bali.
- Outside the US, the growth of mixed-used developments is challenging hotel operators. Some of the issues confronting them are similar to those faced by U.S. operators involved with mixed use projects. These include the setting-up contracts, revenue allocation, and relationship between owner/operator/HOA. Service apartment, time-share/fractional are also gaining popularity as investment products internationally. Due to the lack of legal frameworks, the industry will face some serious issues in the future.
- The lack of comparable data outside large urban areas is often a challenge for asset managers. Compared to the US, international asset managers are limited to monitoring occupancy and average room rates with the competition, not Profit and Loss statements. The key challenge for asset managers is the establishment of benchmarks to analyze operating ratios. This is primarily because of large variations in labor costs between countries.

Common Investment Strategies

The best global investment strategies optimize returns while protecting owners from downside risk. Some of the more important principles and experience based guidelines and strategies when investing globally are discussed below.

- Owners must define their investment strategy, create a competitive bidding environment with the selection of operators, and assemble a team of qualified, experienced consultants and legal counsel to enhance their leverage going into the negotiation with the operator.
- Investors should concentrate on capital cities and prime resort destinations
- Supplementing “location, location, location”, is “DD, DD, DD”. Due Diligence processes are key steps before making an investment decision. It is important to understand the product, the physical condition of the asset, and numerous other factors based on a comprehensive checklist that includes, Legal due diligence, Technical due diligence, and Financial due diligence.^{iv}
- Investors should purchase insurance to adequately protect their assets based on the risk profile of the location. Insurance coverage can include business interruption, property and terrorism insurance. Furthermore, the coverage should always protect against appropriation of property by the local government, war, rioting and destruction, in countries with high political risk. For instance, the World Bank offers coverage in some emerging countries which allows hotel owners to secure their investment.^v
- Acquire real estate assets or real estate-secured non-performing loans at well below replacement cost in crisis countries (particularly in Asia).
- Seek exposure in markets with high barriers to entry.
- Enhance yield by leveraging in markets where costs of funds is still low.

- Consider multiple exit strategies: negotiate favorable terms to terminate the operator contract and buy out partnership, minimize tax exposure.
- Source qualified employees.
- Use financial expertise to construct an efficient capital structure to optimize cost of capital.

Every market is vulnerable to crisis and every hotel needs to have a plan to protect its profit. During unpredictable periods the revenue usually declines suddenly and the operator needs to react promptly to avoid significant losses. A profit protection plan will provide targeted actions to shield profit and goes far beyond the regular cost saving. Each action should be measurable and it should allow the operator to take prompt action to contain losses generated by the regular hotel operation. A well conceived plan will allow the operator to respond and rebound. Once created, the profit protection plan can be updated every year. In case of actual crisis, the plan will be adapted and modified to fit the situation. As long as there is a plan in place, the management team can focus on generating incremental revenue.

Profit Protection Plan can include the following:

- Produce a budget re-forecast
- Reduce provision as revenue decreases
- Close some floors to save energy
- Close selected F&B outlets and reduce provisions
- Limit outsourcing and maximize use of hotel staff
- Reduction of number of employees
- Encourage multitask employees
- Reduce lower rated travel agents and tour operators

Regional Challenges of Investing Globally

While common challenges, opportunities and strategies exist when investing globally, as previously discussed, the economic, political, cultural, and social environment is different from country to country. Based on projects and assignments in the Middle East, Africa and Asia Pacific the specific challenges and opportunities in these regions are discussed individually.

Middle East

The past few years, the Middle East has experienced an unprecedented level of hotel activity with an abundant creation of very successful hotel owning companies. The rapid proliferation of lodging products provided a final spur to the development of the hotel asset management function. The increased complexity of the lodging industry's structure in different countries, with its gamut of products ranging from budget through mid-scale to boutique and luxury properties, has required a rapid development of asset management^{vi}. Despite political uncertainty in Iraq, Iran and Syria, and continued tension between Israel and its neighbors (Palestine and Lebanon), the Middle East remains the fastest-growing region in terms of tourism arrival, ahead of the Asia Pacific region^{vii}. According to figures from the World Tourism Organization (WTO), the number of tourist arrivals in the Middle East grew by 13.2% between 2006 and 2007, which clearly reflects the tourism industry's potential and its resilience to political shocks in the region. The growth in tourism in the region has been driven mainly by intraregional visitation. Arab visitors account for the majority of tourists in the region, with the exception of Dubai. The increase in disposable income and liquidity generated by high oil prices are primary drivers of visitation. Tourist arrivals from the Americas and Europe are dominated by corporate travelers, who increasingly look at the opportunities arising in the region from the diversification and privatizations programs. Dubai, Oman, Egypt, Syria and Jordan, where

leisure tourism is predominant, are benefiting from improving regional economies and continuing appreciation of the euro.

Middle East hotel operations and investments have different characteristics from those of the Western countries. Overhead expenditure, market vulnerability, investor sentiment and financing structures are the key differences. Many Middle Eastern hotels are government owned and, as privatization programs are increasingly applied in the region, there is an opportunity to create a more liquid and transparent hotel investment market. Public spending continues to drive most of the economic and tourism developments in the countries of the GCC. By contrast, non-GCC countries rely on private spending and investment. However, the increased liquidity of the private equity markets in the region is improving with the private sector's role in the investment and the development of the hotel and tourism industries.

Most currencies in the Middle East region are pegged to the US dollar and, given the recent appreciation of the euro; the region is becoming increasingly attractive, in terms of purchasing power, to the European leisure markets. Although hotel financing in the region has in the past been conservative, recent indications show a trend towards more aggressive hotel debt financing in aspects including mortgage lending ratios, mortgage amortization periods and debt-servicing structure. Taxation laws are less strict than they are in other parts of the world, notably Europe and USA. This provides an additional premium to the net return on equity to potential hotel investors, when compared to the returns of a typical hotel investment in the Western region.

The significant amount of large-scale development under way throughout the region (for example, in Dubai, Abu Dhabi, Qatar, Egypt, Bahrain and Jordan) is further stimulating levels of both visitation and private investment. The latter is further fueled by the gradual relaxation of freehold legislation in several countries.

The Dubai Bubble? – According to Sheik Mohammed’s 2015 Vision, the government plans to increase Dubai's GDP to \$108 billion supporting key sectors: the free zones, airports and ports, tourism and retail, and real estate. In 2007, 29 million passengers used the Dubai International Airport which represents an increase of 19% over 2006. The new development of Jebel Ali Airport (Dubai World central) is expected to increase the number of passengers to 60 million by 2010. This new airport will have the capacity of over 120 million passengers a year. Emirates Airlines has already become the 8th largest airline and its continued growth makes Dubai even more accessible. With approximately 1.5 billion people living within a 2 hour flying distance, Dubai is now a destination in its own right with increasing exposure on the world stage. Hotel Occupancies have been steadily increasing each year in Dubai, where they grew from 82 percent in 2006 to 84.4 percent in 2007.

Other challenges and opportunities to consider:

- construction pipeline vs. cost
- limited number of hotel transaction
- human resources (recruitment outside the region, housing, training)
- new local management companies (e.g. Jumeirah, Rotana Hotels), Sharia-compliant hotels
- creation of new regional and international hubs (Dubai with financial center, theme parks, technology, health, retail; Abu Dhabi with culture and high-end leisure; Qatar with universities, research and sport; Bahrain’s financial center)

Africa

Overall, Africa has sustained its above average tourism growth with international arrivals above 8% in 2007, representing 44 million travelers, according to the latest UNWTO World Tourism Barometer. Africa has always been left out of the tourism boom. While Kenya, Tanzania, Zambia, Mauritius, Morocco, Tunisia and Algeria all enjoyed strong growth, two of Africa's biggest destinations stagnated or suffered—South Africa and Zimbabwe.

From South to North

On the supply side, there is a tremendous need for this market to be developed and investors who understand this market will capitalize on opportunities in this region. . For example, the Gulf nations are disillusioned over the way they are regarded and treated in Europe and the US, and the Arab world is now looking at places closer to home to travel and invest in. Middle Eastern companies understand the mentality in Africa more than Western firms, focusing on the opportunities rather than the risk. Buoyed by high oil prices, dissuaded from investing in the west and encouraged by Africa's proximity, the GCC firms are specifically targeting tourism real estate investments. For instance, South Africa's largest ever property transaction involved the investment arm of Dubai government. Their consortium committed more than US\$2 billion to purchase and development of Cape Town's Victoria and Alfred Waterfront. Four new hotels are now planned for the site, including a 1,000 room Jumeirah Beach hotel. Firms such as IFA Hotels and Resorts are accessing the equity markets in the region by being listed on the Johannesburg Stock Exchange. Developing the hotel sector in Africa nevertheless raises challenges for the Middle Eastern companies just as it does for other international firms. The

most significant problem remains that of human resources, staffing and managing world-class hotels.

Human Resources Challenges – According to Department of Environmental Affairs and Tourism 2010 FIFA World Cup South Africa™ will open up about 80,000 job opportunities in the local tourism and hospitality sector in South Africa. Over the next three years, it is estimated that the industry will require about 24,100 cooks and chefs, 23,500 waiters and waitresses, 15,000 cleaners, 7,800 cashiers and 8,000 managerial staff. The key challenge within the industry at present is that demand for staff far outstrips supply. In general, Africa lacks trained staff to work in upscale hotels. While companies are overcoming this by importing qualified people from beyond the region, it can only be a short-term solution and one that doesn't benefit Africa's workforces as it should. It is another urgent reminder of the need to develop professional hospitality schools in Africa to meet the industry's ever-growing needs in the future.

Perceived Political Instability is a Challenge – In general Africa's history of inter-regional, communal, ethnic and dictator driven instability and the perception of being a safe haven for terrorists have sent cautionary investment signals to investors. A case in point is Kenya, is now re-gaining stability after the unrest posted by the election process at the end of 2007, which strongly affected tourism and investment flows in the region. The country has always been one of the Africa's main destinations for Safaris, with 1.6 million international arrivals in 2006. International tourism has now the opportunity to experience a strong comeback, thanks to the famed wildlife and costal attractions.

Successful story - The North African countries with the fastest growth rate in tourism sent out a clear message that its own private sector will now play a more prominent role in developing its all-important travel industry, indicating that it is ready to use expertise acquired over several decades of steady growth to spearhead new initiatives that would put a large number of unknown sub-Saharan countries on the map. In Morocco the numbers of visitors and the average room rate have increased significantly over the past few years. The tourism push is also seeing secondary cities like Fez and Tangier benefiting from both large corporate investment and fledgling foreign individual interest. The contraction in its neighbor's market contrasts starkly with the building explosion being encouraged by King Mohammed VI, who decided a few years ago that tourism could be a panacea for his kingdom. Aiming to increase visitor numbers to 10 million by 2010^{viii} he has been establishing development incentives along Morocco's impressive Atlantic coastline, as well as inland. This ambition has been boosted by the European open skies policy that has seen low-cost flight operators opening new routes into the country. Currently Marrakech airport is being extended to cope with this new influx. Morocco has already been dubbed the new Dubai and developers from the United Arab Emirates have recently committed to long term, billion-dollar investments that would bring luxurious lifestyle resorts in and around Morocco's most popular destination. Bound by a common faith, many Middle East investors have turned to Morocco as a friendly Islamic nation with huge investment potential, better than both Egypt (whose industry is not as well organized) and Tunisia (a smaller country with less growth potential). Examples of investments from the GCC highlight potential of intra-regional involvement in Morocco's tourist industry:

- Emirati groups such as Emaar and Dubai Holding have yielded contracts worth US\$9 billion extending across projects in Rabat, Marrakech, Casablanca and Tangiers

- UAE-based Reem Investments, a private investment company will invest US\$1bn in the Atlas Garden project outside Marrakech
- Kuwaiti-Moroccan Development Group Walid Al-Fehaid is upgrading its Morocco chain, Farah Hotels
- Bahrain-based Gulf Finance House has started a \$1.4bn development in Tangiers
- Qatari Diar Real Estate Investment Company will invest \$335m in tourism projects building three hotels, adding 3,000 room and a golf course in Tangiers

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| <p>Other challenges and opportunities to consider:</p> <ul style="list-style-type: none">- political instability- strong growth in the Maghreb- A need for urban infrastructure improvement- Potential for ecotourism |
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Asia/Pacific

Asia / Pacific saw growth in tourist arrivals that was driven by big increases in China and its special administrative regions of Hong Kong and Macao. Southeast Asia—especially Thailand, Malaysia, Singapore, Cambodia and Vietnam—is becoming one of the world’s favorite tourism destinations with demand outstripping tourist facilities. Hotel investments continue to be a compelling target for global and local investors in this region. Consequently, hotel trading performance will be strong with many markets trading at record highs. Supply increases, while still relatively modest through 2007, will increase over the next couple of years, peaking in 2009. Escalating financing, land and construction costs may, however, result in some projects being delayed over the medium term.

Travel across Asia soared in 2007, with international arrivals increasing 9.4 percent to almost 275 million^{ix}. Against this travel bonanza, growth is expected to moderate over the next three years while retaining its strength and averaging 8.2 percent per annum. Total arrivals are forecast to surpass the 300 million mark by 2009 and reach almost 350 million by 2010. This represents an increase of 61 percent in cross-border visitors compared to 2004. While China (PRC) dominates, accounting for over half of all international arrivals, countries in Southeast Asia are expected to make strong gains over the next few years. In comparison, international tourism to North Asia and India is expected to remain modest. International arrivals to Japan have increased by an average 10.8 percent a year and the country looks set to meet the government target of 10 million visitors by 2010. India's international arrivals have grown at a slightly higher rate, averaging 13.9% a year, albeit from a lower base.

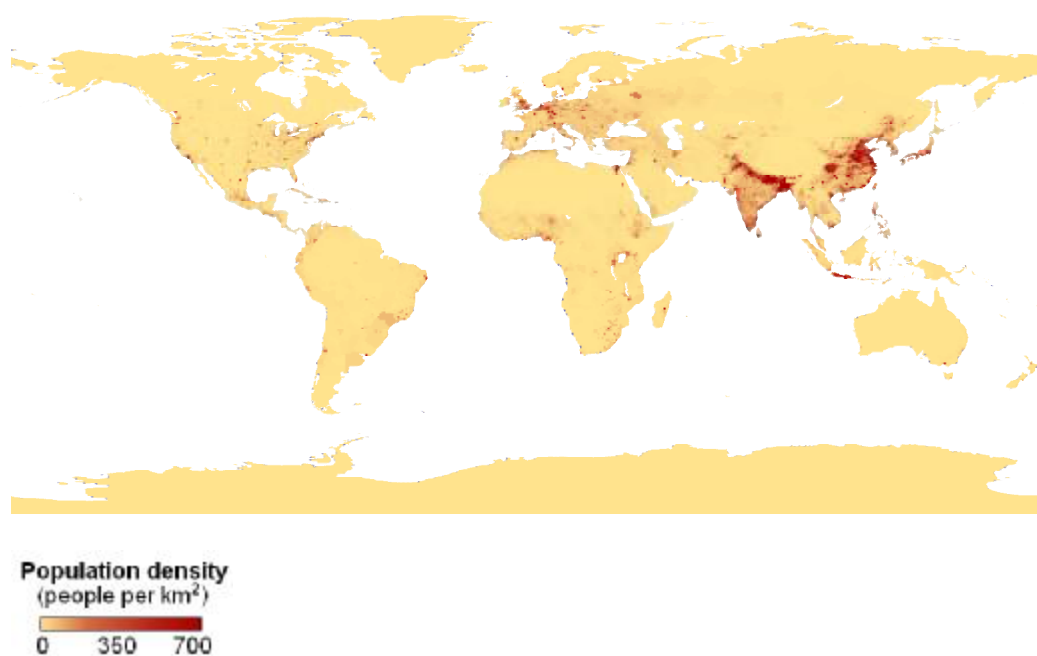
Over the next three years, Asian hotel room stock is forecast to increase by around 25.8 percent (140,000 rooms) or an average of 7.9 percent per annum^x. Development hot spots include India, Vietnam, Macau SAR, Hong Kong SAR, Taipei and Singapore. Higher land prices and spiraling construction costs, has resulted in a softening in investor sentiment as developers are finding it harder to secure finance, almost certainly at a higher cost. Projects that offer lower operational risk, such as those in prime locations with an experienced operator are more likely to proceed.

Counterbalancing the cautionary investor sentiments in these emerging Asian markets is the rapid growth of domestic tourism. With a combined population in excess of three billion, an increasingly affluent middle class with leisure time and the growth of business travel domestic

tourism offers an unparalleled opportunity across Asia. In the region's largest economies – China (PRC), Japan and India – domestic travel dominates, outweighing international tourism by up to 25:1.

Global Demographics and Population Densities A Driver of Market Growth

To understand the market opportunities of hospitality around the world, we need to step back, analyze it on a macro level to start with. Asia accounts for over 60 percent of the world population with almost 3,900 million people (world population 6,450 million). The People's Republic of China and India alone comprise 20 percent and 17 percent respectively. Africa follows with 840 million people, 12 percent of the world population. Europe's 710 million people make up 11% of the world's population. North America is home to 514 million (8%), South America to 371 million (5.3%), and Australia 21 million. The world's population, on its current growth trajectory, is expected to reach nearly 9 billion by the year 2042.^{xi}



Source: United Nations Population Division.

China (20% of the world population) – The lack of understanding about the Chinese market still remains a major obstacle for foreign investors. China will be one of the largest, if not the largest, economy worldwide, and more people from home and abroad will visit and experience China. That is why foreign investors are showing increasing interest in owning hotels in China, employing capital there to enhance future growth. Shanghai is still the preferred investment location, given its position as China's financial centre. Besides the major cities, interest from foreign investors in China's emerging secondary cities including Dalian, Tianjin, Guangzhou, Shenzhen and Sanya is also increasing. However, for foreign investors, China still represents challenges with barriers to entry and developing an understanding of the market is the most important step. While this situation is improving, the opening of the Chinese market remains in its infancy, and procedures surrounding foreign investment mean a transaction can take up to one year to complete, with regulatory approvals potentially taking six months. Over the last decade, Shanghai has developed a reputation as an investor-friendly city with less red tape and procedural delays. Investors are now familiar with the process in Shanghai and are likely to take another 12 to 18 months to understand Beijing's process. It claimed investors still prefer the cities of Shanghai, Beijing and Tianjin. Transparency is also a major issue holding back foreign investors who need credible information to make accurate financial decisions. If the data provided is not available or not reliable, they would hesitate to invest.

Greater China – Positioned as Asia's Las Vegas, Macau saw the opening of the Venetian and the MGM Grand in 2007, making the entry of a new generation of integrated casino-resort to the Special Administrative Region (SAR.) These two developments as well as rival high-end casinos

and a staggering pipeline of new hotels are expected to drive the historical gambling enclave in attracting a higher proportion of visitors from further afield. The recent announcement that the granting of casino licenses will be suspended pending a review of the sector will come as welcome news for these early entrants. Reportedly, Macau SAR already rivals the entire US state of Nevada in gambling revenue, raking in more than US\$10.3bn in 2007. Investment in transport infrastructure and improved links with the rest of the region will also support the continued growth of the tourism industry^{xii}.

Hong Kong SAR is one of Asia's premier financial centers, leisure and MICE destination, with China being its largest feeder market. Record visitor arrival and no new upper-tier openings boosted the performance of the five-star hotel market in 2007. Almost 12,000 new rooms are expected to open in Hong Kong SAR between 2008 and 2010. More than ever Hong Kong now faces stiff competition for tourist dollars from other Asian destinations such as Singapore, Vietnam and Macau.

India (17% of the world population) – While attracting only a small proportion of international visitors relative to its massive population base, India has one of the most diversified tourism profiles and any Asian country. Only 10% of international visitors come from within Asia, with the majority being from Europe, North America and the rest of the world. While distance plays a part, improvements to transport infrastructure, increasing capacity at major airports and enhanced connectivity with Asia, as well as the government's target to double visitor arrivals by 2010, could see this shift over the next few years. The 2006 implementation of the UPA's Open Skies Policy, which allowed domestic carriers to commence international flights, start-up of

various low-fare carriers and fleet expansion by domestic players has pushed India's doors open even wider.

Indian hotel development has recently been very dynamic and must be understood. It is important for investors and developers to solidify their core competencies domestically while outlining and implementing the best policy for entry into this emerging market. At this point it is evident that this developing nation holds great potential for investors. But business styles and norms in foreign countries can be very different and India is by no means an exception. Domestic companies are aggressively adding rooms and setting up Greenfield projects. Foreign hotel companies are making full use of the relaxed norms for foreign direct investment in India. In the next five years, we should expect to see around 40 different hotel brands dotting the Indian landscape. More than 53,000 hotel rooms^{xiii}, all corresponding to hotels with brand affiliation, are in various stages of planning and development in the above ten cities, and expected to enter in a phased manner by 2011. Despite all the interest generated by mid-market and budget hotel development, around 53 percent of the development is still concentrated in the luxury and first class (Five-star Deluxe and Five-star) segment. This segment is also characterized by its higher service orientation, which makes it particularly vulnerable to the manpower crunch. The industry will need to learn to absorb people in huge numbers.

Other challenges and opportunities to consider:

- Massive expansion of the low cost carrier network
- Strong growth of domestic business and leisure travel
- Easier access to commercial and consumer credit
- Strong growth of ecotourism
- The strong performance growth of the hotel property sector against other real estate investment classes in recent years is likely to continue in the future
- Local and communal politics hinder progress
- Socio-Political-Economic-Cultural diversity within country (challenge and opportunity)
- Poorly enforced legal systems
- Poor infrastructure to facilitate tourism
- Poor hygiene and sanitation standards
- Lack of hotel asset managers (operators are often requesting Asset Manager from their owners)
- Standards of service and construction quality much higher in certain places (e.g. Japan)

Conclusion

The chapter has attempted to present evidence that the current and future growth trajectory of the market, travel and tourism, demographics, and investment points towards a strong case for hotel investors and operators to consider international expansion. However, it is also clear that these opportunities are accompanied with challenges which need to be clearly understood before an investment decision is made. While the level of transparency in various emerging regions does not match the developed regions of the world, third party information on performance, investment pipeline, country risk analysis and profile is much better today than it was a few years ago. Asset Managers may rely on these resources along with their knowledge of local and regional markets to advise their ownership on international investments.

References and Endnotes

- ⁱ UNWTO World Tourism Barometer, Volume 6, No. 1, January 2008
- ⁱⁱ Open skies refers to a bilateral (and sometimes multilateral) Air Transport Agreement which liberalizes the rules for international aviation markets and minimizes government intervention — the provisions apply to passenger, all-cargo and combination air transportation and encompass both scheduled and charter services
- ⁱⁱⁱ STR Global HotelBenchmark™ Survey and Smith Travel Research
- ^{iv} Asset Managers must look beyond budget, Global Asset Solution, December 2007
- ^v The Multilateral Investment Guarantee Agency (MIGA), established in 1988 as a member of the World Bank Group is an example of the World Bank's role in providing political risk mitigation services. See chapter on Political Aspects of the International Travel and, Tourism and Lodging Industry in *International Hotels: Development and Management*, written by Chuck Gee and contributing author A.J. Singh. (Lansing, Mich: The Educational Institute of the American Hotel and Lodging Association, 2008)
- ^{vi} Asset Management Vital for the Middle East, Global Asset Solution, October 2007
- ^{vii} Middle East Hotel Survey – Outlook, Market Trend and Opportunities, HVS Dubai 2008
- ^{viii} Thriving African tourism backed by private investments, CNN, 2008
- ^{ix} Jones Lang LaSalle Hotels, Asia Overview Digest 2008. This assessment is based on the following 15 countries: Philippines, Lao PDR, Cambodia, Vietnam, Indonesia, Singapore, Thailand, Malaysia, Macau SAR, Hong Kong SAR, China (PRC), Taiwan, Japan, Korea (ROK) and India
- ^x Jones Lang LaSalle Hotels, Asia Overview Digest 2008
- ^{xi} United Nations Population Division of the Department of Economic and Social Affairs. World map from NASA.
- ^{xii} Jones Lang LaSalle Hotels, Asia Overview Digest 2008
- ^{xiii} HVS International Research