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What Credit Crunch? More Luxury for New Money

European Rising Stars & Established Markets

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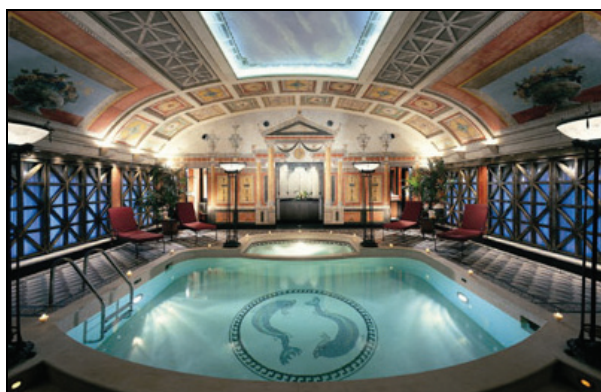
The Dorchester, London



Hotel Arts, Barcelona



Mandarin Oriental, Munich



Principe Di Savoia, Milan



George V, Paris

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This article investigates how luxury is currently perceived, the main drivers of demand for luxury accommodation, the current and future supply of luxury hotels, and the leading luxury brands in Europe. We conclude by analysing performance levels and future supply of luxury hotels in five key cities – London, Paris, Munich, Milan and Barcelona – and offering a view on the impact the global economy may have on the sector.

Luxury goods and services have experienced an unprecedented rise in demand over the past few years. As disposable incomes grew across America and Europe, it is no surprise that the luxury sector has been one of the fastest-growing segments in recent years. High net worth individuals from emerging countries such as Brazil, Russia, India, China and the wealthy Middle East have also become more important for the luxury sector, thus allowing the demand for luxury to remain robust and continue to grow. This in turn had a positive impact on the luxury travel market with more people opting to stay in high-end accommodation. The luxury hotel sector has thus proven to be a dynamic industry that is interesting to many parties, including consumers, investors, developers and owners. On the other hand, after the 'credit crunch' began at the end of 2007, the hotel sector as a whole has started to see a slowdown in investment, development, and (somewhat) demand. This then leads us to ask: as global economies face challenging times ahead, will the luxury hotel sector be able to sustain the downturn?

What is Luxury?

Luxury can be defined in many ways and perceived differently depending on location, culture and even on one's background. One traditional way of defining luxury is as 'a way of life that satisfies all material desires regardless of expense; something agreeable but not necessary or self indulgence in material pleasure' (Penguin Books limited, Harmondsworth, Middlesex, revised edition

1969, G.N. Garmonsway). According to Collins English dictionary, luxury can be defined as being 'indulgence and enjoyment of rich, comfortable, and sumptuous living; something that is considered an indulgence and not a necessity.' All in all, whichever way you may want to define the term, there is a general consensus that luxury is not a necessity but rather a 'treat', which has become increasingly more complex to define, especially when looking at the hotel sector.

Luxury Hotels in the 21st Century

In the 21st century, definitions about luxury hotels are blurring. The blurring of the definition has been exacerbated by the fact that staying at a luxury hotel or resort, and even travelling by private jet, has become more and more affordable – accessible to a wider segment of the population (notably increasingly aspirational and indulgent consumers who would not normally be characterised as luxury or high-end travellers). Once a sign of prestige and a differentiation in social class, luxury has developed into an ever-changing concept that is 'no longer defined through material components, but increasingly through ideal values and experiences'. (Munich University of Applied Sciences/Zarges von Freyberg Consulting). Luxury is now less solid and exclusively reserved, but more modern and flexible. In other words, hotels today want to provide their customers the luxury experience by making it somewhat more intangible with personalised services, such as

private shopping or cooking classes with celebrity chefs, in order to create a memorable stay. Hence, luxury is no longer defined by the number of stars a hotel has, but by its tailor-made services to the individual needs of the guest.

The Luxury Hotel Product

Luxury hotels are usually associated with landmark buildings in well established destinations such as Paris, London or Milan; they provide wealthy visitors with services that are personalised to their needs and demands. Luxury hotels are often associated with tradition and history with design being influenced by a certain time period which in turn maintains the luxurious feel of each hotel in the segment. However, recently, the luxury hotel customer profile has changed. We have recently seen a number of payers in the luxury hotel market invest in their properties not only to make them more attractive to the ever-demanding guest, but also to make them more appealing to the younger and trendier luxury consumer. Consequently, luxury hotel brands and operators have found ways to differentiate their product within the segment.

The demand for luxury is clearly influenced by the type of property and the physical nature of the asset. In fact, the motivation for booking into a luxury hotel is highly influenced by the location of the property, its exterior and interior design as well as the facilities included such as the room types, sizes and amenities, restaurants and spas. However, apart from the physical product, a luxury hotel distinguishes itself primarily by the excellent services it offers.

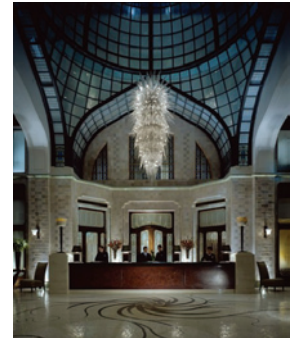
So, what is it that distinguishes the 'luxury hotel product'?

Exterior and Interior (Building)

As mentioned before, luxury is not only perceived by the facilities and services of the hotel but also the visual aspects such as the interior and exterior design. In order to visually differentiate from the competition and reflect uniqueness and exclusivity, luxury

brands are converting historic buildings into hotels and therefore add an aura of charm to their properties. The list of examples throughout Europe is long and includes hotels such as the Four Seasons Gresham Palace in Budapest, a historic Art Nouveau building, exquisitely transformed with ultra-modern comforts. TheStreet.com, a financial company and website stated in March 2008:

'It is difficult to remember what a stay in Budapest was like before Four Seasons Gresham Palace opened. And what a palace it is, one of the finest examples of Art Nouveau architecture in Central Europe, breathtakingly restored with sweeping staircases, stained glass, mosaics and ornate ironwork.' (TheStreet.com, March 2008)



Another example out of the Four Seasons portfolio has just opened its doors in Florence. The conversion of an old palace and convent belonging to the Medici family in the sixteenth century has involved the restoration of some of Florence's most beautiful historic structures and artefacts, some of which are under protection orders, including many sixteenth-century frescoes, hand-painted floors and ancient Chinese wallpaper.

'The Best Name-Drop: You are nobody unless you have booked into the Four Seasons Florence... It's an oasis in the city centre: eight-acre park, pool (unusual), spa (unheard of), two palazzos, one of which is dedicated to quiet with a soft-footed personal concierge.' (Vanity Fair, 2008)



The third example is Kempinski's Çırağan Palace, an Ottoman palace on the banks of the Bosphorus.

When the conversion of a historic building is not possible another opportunity for a luxury hotel is to appoint a renowned architect to design the external features of the building and thus create a landmark property

recognisable by any potential customer the world over. A good example for this is the Burj Al Arab in Dubai, and there are many examples in Europe, such as the Hotel Marqués de Riscal, in the Rioja wine region. The outstanding architecture of the Hotel Marqués de Riscal, a member of the Luxury Collection, was designed by renowned architect Frank O. Gehry and is his second masterpiece in Spain, after Bilbao's Guggenheim Museum.



The W Hotel Barcelona, also known as Hotel Vela, is another example of an avant-garde icon; it will tower over a stunning waterfront, designed by the famous Spanish architect Ricardo Bofill Levi. The new city landmark is expected to enhance W's profile worldwide by setting a new benchmark for hotel design in Europe.



Location

Apart from recognition as a landmark building, location is a very important demand driver for luxury hotels and contributes significantly to the uniqueness and exclusivity of the guest's experience. Many of the luxury hotels are in prime city centre locations. Examples of this include the Ritz in Madrid, George V in Paris and the Dorchester in London.

The main factors in terms of location for luxury resort properties differ somewhat from their counterparts in gateway cities. Luxury resort hotels are characterised by discretion and privacy, creating the perfect hideaway that is secluded and yet easily accessible.

Rooms and Amenities

The guest rooms are a significant element of the guest's experience. In luxury hotel properties, the rooms tend to be larger when

compared to hotels in other segments, offering spacious rooms in order to provide comfort and enhance the lavish feel of the guest's stay. Additionally, such properties usually focus on suites and therefore offer a higher suite ratio, on average accounting for roughly 30% of the total room count.

The sizes of rooms within a luxury hotel vary greatly due to the range of room types on offer. Standard room sizes start from 30-40 m² and can go up to 60 m². Suites tend to start at a larger size, with royal suites averaging at 150-175 m². The size of the guest rooms also depends on location and cannot be generalised for every luxury property.

Independent of the room size, however, luxury hotels started to offer more in-room amenities and services for their guests in order to provide the full luxury experience. General in-room amenities include a private minibar with a selection of drinks and snacks, hairdryers, bath robes and slippers, bath products provided by a famous brand, Internet access, DVD and CD players, iPod docking stations, radio alarm clocks and others. Services may include 24-hour room service, twice daily housekeeping services and complimentary newspapers.

Food and Beverage

Apart from being a revenue generator for luxury hotels, the food and beverage facilities are an important part of the overall hotel experience and a number of hotels have invested significant amounts in refurbishing their food and beverage outlets, in addition to adding renowned chefs to their signature restaurants. During the summer of 2006, Thierry Despont, known for designing the interior of Gordon Ramsay's restaurant at Claridge's, oversaw the makeover of the bar at London's historic The Dorchester. Over the past two years, London alone has seen over five new bars open in its luxury hotels with the intention of attracting a new client base and outdoing one another.

Additionally, restaurants in such hotels tend to be high-quality, fine dining, which may become established dining 'destinations' by being award-winning restaurants. Examples include the Rasoi by Vineet in the Mandarin Oriental Geneva (one Michelin star) serving Indian cuisine; Alain Ducasse at The Dorchester (opened in November 2007); and the three-star Michelin Restaurant Le Meurice headed by Chef Yannick Alléno.



Restaurant Le Meurice, Paris

In some cases the fine-dining restaurant is even more famous than the luxury hotel it belongs to (the Hotel Costes in Paris, for example) and thrives on business from non-resident guests rather than hotel guests.

Spa and Health Clubs

As self-indulgence is becoming a very important demand driver within the luxury hotel market, the spa has become an essential facility in every luxury hotel and is nowadays regarded by consumers as one of the key luxury experiences.

Whereas luxury city centre hotels offer urban spa experiences, resort locations mostly comprise fully fledged extensive spas including the following amenities.

- Indoor and outdoor pools;
- Treatment rooms with heated beds; candlelit and soothingly scented;
- Separate ladies' and gentlemen's luxurious relaxation rooms with fully adjustable electronic loungers and personal music systems;
- Jacuzzis, saunas, steam rooms and experience showers (light, sounds and aromas);
- Mineral water and fresh fruit juices within relaxation areas;
- High-end quality spa products and treatments.

Trends in the luxury spa business range from using natural ingredients (such as flowers, fruits, herbs, spices or plants) to fusions of Eastern and Western treatment techniques. Apart from the classic massage and manicure/pedicure treatments, spas combine classic treatments with holistic and mind-body wellbeing therapies, trigger point therapy, Reiki, meditation, energy healing and activities such as yoga and Pilates. Luxury hotels specialising in wellbeing may also help the luxury traveller to detox, lose weight or relieve stress by offering extensive fitness areas and relaxation zones. Sustainability and eco-friendly spas are also becoming more important.

Professional spa operators such as Six Senses, Angsana and ESPA have prioritised substantial training for all staff to ensure the highest quality of their services.

The in-room spa programme has become an alternative for luxury city centre hotels that lack the space for a stand-alone spa facility. These in-room spas may include a luxurious yet portable spa bed and a spa basket filled with sensory items to be enjoyed before, during and after the treatment.

Whether it is an urban spa, an extensive resort spa or an in-room spa, the successful spa has a relaxing atmosphere and friendly, highly trained professional services.

It is interesting to note that the luxury spa experience need not start in the hotel. The new Airbus A380-800 operated by Emirates between Dubai and New York includes a separate spa area that will offer a number of treatment rooms, waterfall features and birdsong sounds.

Services

Luxury hotels are meant to create a unique experience and exquisite feel for the luxury traveller. Even more important than the physical product is the service a luxury hotel offers its guests. Only with excellent service and innovative ideas to enhance the hotel stay can luxury hotels create this most sought after experience that differentiates them from the competition. Therefore, luxury hotels are becoming more and more innovative when it comes to creating personalised services that

suit each individual's requirements. Amongst these services are valet parking, 24-hour concierge service, pillow menus, complimentary limousine service, laundry and dry-cleaning, and shoe-shining services.

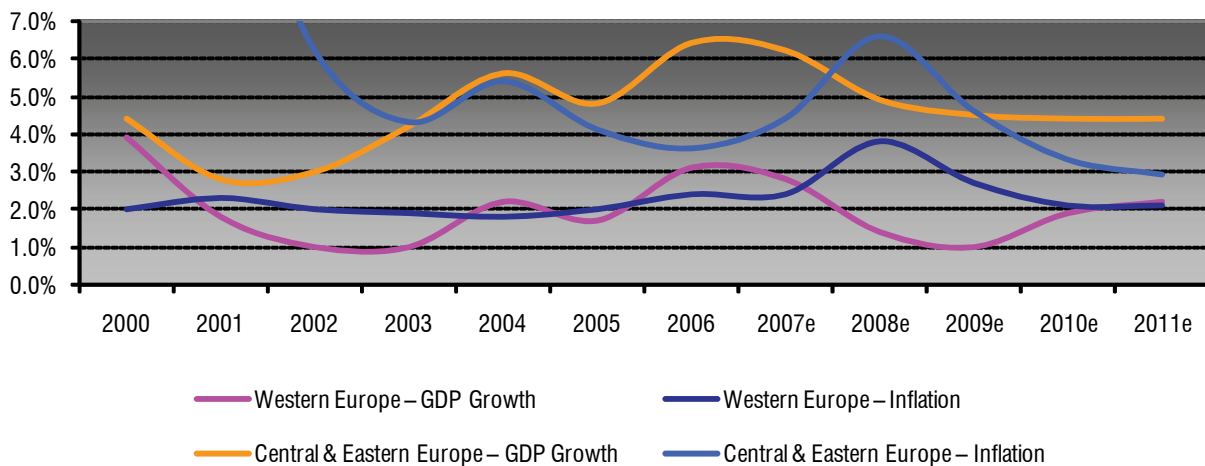
A number of luxury hotels have identified families as a growing segment and offer dedicated services such as babysitting. At the Plaza Athénée in Paris, for example, children are given VIP treatment; the concierge is available to organise family dinners and outings, as well as satisfy any requests for a babysitter. At the Mandarin Oriental hotels, every child receives a welcome gift upon arrival, while children's beds and babysitting services are also available. Pets have become another important 'item' on the guest services list of most luxury hotels as arrangements can be made for dog walking, as well as pet menus to cater for their dietary needs. For business travellers, brands like Four Seasons offer a range of services, including translation and interpreting services, airline reservation, digital cameras, laptops and many others.

Economic Overview

The main economic indicators that have an impact on travel and hotel accommodation are GDP growth and inflation. Table 1 illustrates their development over a period of 12 years broken down into the areas of Western & Southern Europe and Central & Eastern Europe. In 2007 Western & Southern Europe is estimated to have achieved gross domestic product (GDP) growth of 2.8%. The emerging markets of Central & Eastern European countries (such as Poland, the Czech Republic and Hungary) have also performed well, sharing a healthy average GDP growth of 6.2% in 2007. However, the Economist Intelligence Unit (EIU) forecasts that growth in Europe will slow over the next few years.

Consumer price inflation in Central & Eastern Europe has fallen sharply from almost 15.0% in 2000 to a moderate 4.4% in 2007; this is compared to 2007 inflation of 2.4% in Western & Southern Europe. Owing to current economic situations, consumer price inflation in Western and Southern Europe is expected to rise to nearly 4.0% in 2008, before starting to ease in 2009 and then stabilising at around 2.0% from 2010 onwards.

Table 1 Economic Indicators – Europe 2000-11



Note:

Western and Southern Europe includes Austria, Belgium, Cyprus, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom

Central and Eastern Europe includes Bulgaria, Croatia, The Czech Republic, Estonia, Hungary, Lithuania, Latvia, Macedonia, Poland, Romania, Slovakia and Slovenia

Source: Economist Intelligence Unit, September 2008

The European Union's (EU) travel and tourism industry is expected to contribute 3.6% to the EU's GDP in 2008 (US\$659 billion), rising in nominal terms to US\$901 billion (2.5% of total) by 2018. The contribution made by the travel and tourism industry to the worldwide economy (as a percentage of the total) should rise from 10.2% (US\$1,877 billion) to 10.7% (US\$2,642 billion) over the same period.

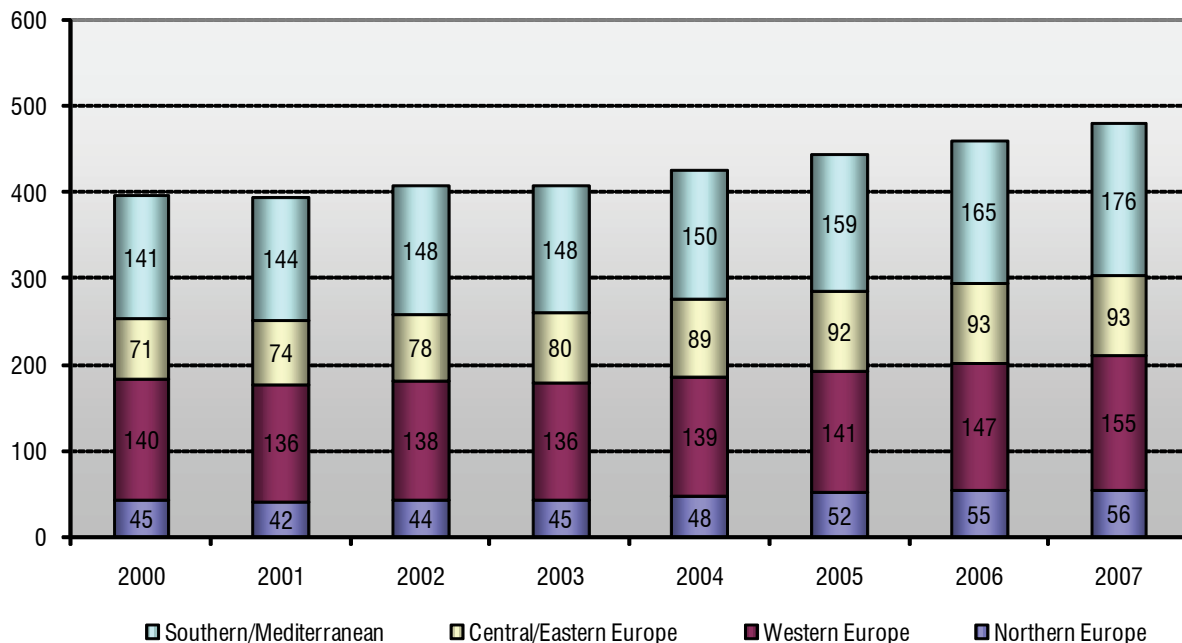
The increasing GDP and wealth throughout Europe over the last few years has made accommodation in upscale or luxury hotels affordable to a larger percentage of the population. However, with the current 'credit crunch' and economic downturn the question remains whether demand for luxury hotels

will decrease. Historic recession, however, shows that the luxury segment proved to be more resilient to economic slowdowns than, for example, midscale hotels.

Travel and Tourism Demand - Europe

The number of international arrivals in Europe grew at a compound annual rate of 2% between 2000 and 2007, from 396 million in 2000 to 480 million in 2007; a good indication that Europe is the most stable tourism region in the world. The strongest annual growth was recorded in the emerging countries of Central and Eastern Europe, as shown in Table 2.

Table 2 International Arrivals in Europe 2000-07 (millions)



Source: World Tourism Organisation

European tourism had a very good year in 2007. The overall growth in the number of international arrivals was an estimated 6% on the previous year. Central/Eastern Europe remained stable with arrivals at the same level, whereas Western and Southern Europe recorded growth in the number of arrivals of 4%. Sporting events such as the Rugby World Cup in France, the America's Cup in Spain and, to a certain extent, the Tour de France, which started in the UK, as well as cultural events have contributed significantly to good

tourism performance in Europe. Furthermore, Europe's tradition and history will always create an appeal for the region as a tourism destination as whole. The continuous expansion of low-cost airlines, now targeting Southern, Central and Eastern Europe in addition to the established Western European city break routes, accelerated the growth in international arrivals in Europe. Specific data for the luxury segment are not available but we assume that it follows the same trend.

Luxury Hotels - Main Demand Drivers

According to a study presented at ILTM (International Luxury Travel Market) in 2007, luxury travel generates approximately 25 million trips a year, with a contribution that accounts for nearly 25% of total spending. On average, luxury travellers are estimated to spend between €7,000 and €14,000 on a luxury trip. Preferred European destinations include locations around the Mediterranean, with Italy being the main hot spot.

The global hotel market has shown great results in terms of performance, which has been largely driven by the growing demand from leisure and business travellers across the board.

As demand for highly authentic and diversified products increases, operators in the segment will need to reinvent their respective products in order to meet existing clients' needs and to differentiate from the competition.

Additionally, demand for luxury products has not only been developing within its established target market, but it has also seen rapid growth in a new, trendy, younger and wealthy clientele, who perceives luxury to be more attainable, accessible and affordable.

The luxury hotel segment in Europe has also seen an increase in the supply of branded assets from operators such as Four Seasons, Mandarin Oriental and Kempinski. Not only have these operators increased their presence over recent years, but the major luxury brands also have a number of projects currently under development (with even more yet-to-be-confirmed developments in the pipeline).

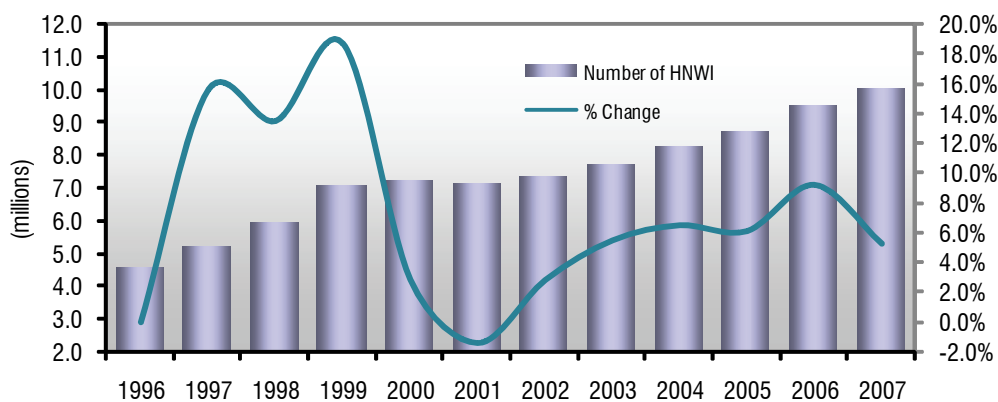
High Net Worth Individuals - An Emergent and Active Consumer

A recent trend that has become more evident within the travel and tourism industry is the rise of younger high net worth individuals; a clientele seeking indulgence and high-luxury products. In terms of wealth, this particular segment prides itself on having an average annual income that ranges from US\$1 million to US\$10 million.

Table 3 illustrates the evolution of high net worth individuals from 1996 to 2007. The number of individuals has increased by approximately 8% with future growth expected.

Table 4 illustrates the wealth growth of high net worth individuals from 2005 to 2007.

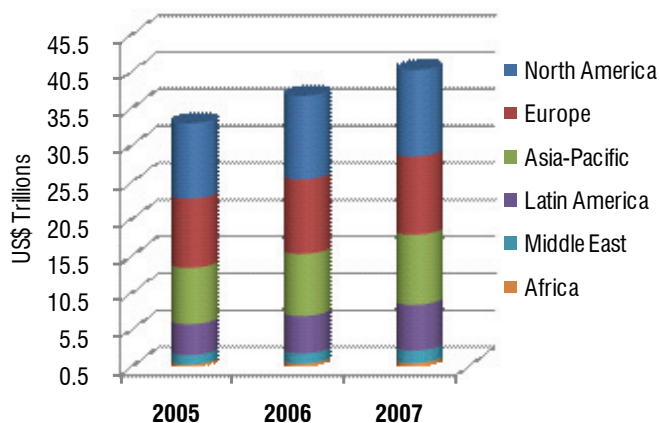
Table 3 Global Growth of High Net Worth Individuals 1996-07



Source: CapGemini, Merrill Lynch World Wealth Report 2008

Table 4 Wealth Growth of High Net Worth Individuals 2005-07

	US\$ Trillions			CAGR 2005-07	% Change 2006-07
	2005	2006	2007		
North America	10.2	11.3	11.7	7%	4%
Europe	9.4	10.1	10.6	6%	5%
Asia-Pacific	7.6	8.4	9.5	12%	13%
Latin America	4.2	5.1	6.2	21%	22%
Middle East	1.3	1.4	1.7	14%	21%
Africa	0.8	0.9	1.0	12%	11%
Total	33.5	37.2	40.7	10%	9.4%



Source: CapGemini, Merrill Lynch World Wealth Report 2008

In 2007, global wealth continued to rise as the report by Merrill Lynch/Capgemini reveals. Total High Net Worth Individual wealth grew by 9.4% in 2007 to reach a total amount of US\$40.7 trillion. Over the past three years, global wealth has shown compound annual growth of 10%. Latin America has seen the greatest growth in wealth in just three years, with an astonishing compound annual growth rate of 21%. Latin America's impressive growth can be explained by its thriving export sector and heightened domestic demand. In 2006 Latin America experienced real GDP growth of 4.8% and attracted substantial foreign investment. Driven by strong corporate profits, IPO activities and ongoing investment in Latin America, the growth in the wealth of High Net Worth Individuals outperformed the growth in all other regions from 2005-07, according to the Merryl Lynch World Wealth Report. Such an increase indicates that there is an opportunity for the luxury sector to cast a wider net in search of its target markets.

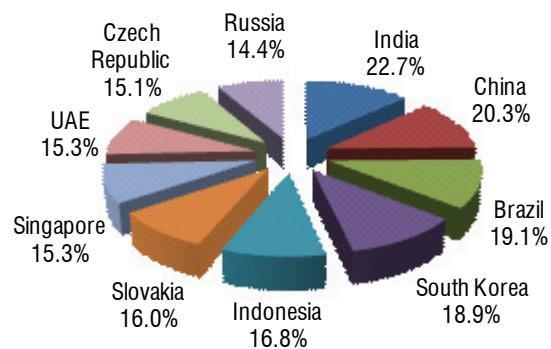
However, as shown in Table 5, the countries with the biggest growth in the number of High Net Worth Individuals include Brazil, Russia, India and China. Therefore, we will further investigate how the BRIC (Brazil, Russia, India, and China) countries impact the demand for the luxury travel and hotel sectors.

BRIC Countries

In 2007, the BRIC countries continued to establish their roles as important economies. While more mature economies showed a slight slowdown, these emerging economies

continued to perform well. While traditionally they have been considered developing countries, the BRIC countries currently present the highest growth in the number of High Net Worth Individuals. The only factor that may impede these economies from higher growth is the rising level of inflation rates which seem to be more pronounced in such nations.

Table 5 illustrates the growth in the number of High Net Worth Individuals by market in 2007.

Table 5 High Net Worth Individual Population Growth by Market 2006-07

Source: CapGemini, Merrill Lynch World Wealth Report 2008

India, China, and Brazil led the High Net Worth Individual population at 22.7%, 20.3%, and 19.1%, respectively. Russia was also in the top ranks of the High Net Worth Individual population table with a 14.4% growth in 2007.

The growth in sales of luxury branded goods, notably in emerging markets, highlights the opportunities for travel and tourism. China is reportedly now the world's third largest

consumer of luxury goods, after Japan and the USA, accounting for 12% of global sales, according to Goldman Sachs, and could overtake both the USA and Japan by 2015. Furthermore, analysts at Bain & Company predict that the luxury market in India could grow by 25% a year over the next three years.

Meanwhile, spending on luxury goods by the fast-growing numbers of high-end Russian consumers – including the teenage children of the ultra-rich – is growing in double figures, and the trend seems set to continue. Russia is also one of the fastest and largest growing markets amongst the new travelling nations.

The BRIC nationals are tending to travel more frequently at a global level with a strong appetite for the high-end luxury products flooding into the European market.

Other Asian countries, such as Singapore, Indonesia and South Korea, are also among the leading growth markets, highlighting the rising share of wealthy individuals in non-traditional source countries for tourism.

Luxury Hotel Supply

As demand for luxury hotels and goods grows, increased competition amongst hotel operators for the sector becomes fiercer as they battle for the same client base. As a result, hotel chains have increased investment in their luxury assets and brands in a way that has resulted in the development of a number of new projects involving luxury products. Table 6 highlights the brands we consider to be the main luxury brands currently operating in Europe and which have proposed assets in Europe. We are aware that all of the following operators are actively looking at expanding their presence.

Table 6 Luxury Branded Supply in Europe

Brand	Operator	Number of Properties	Proposed Developments
Conrad	Hilton	4	1
The Dorchester Collection	The Dorchester Collection	4	0
Fairmont	Fairmont Raffles Hotels & Resorts	4	1
Four Seasons	Four Seasons Hotels & Resorts	14	3
Kempinski	Kempinski Hotels & Resorts	31	12
The Luxury Collection	Arabella Sheraton MA, Starwood	33	1
Mandarin Oriental	Mandarin Oriental	4	5
Maybourne Hotel Group	Maybourne Hotel Group	3	0
Park Hyatt	Hyatt International	7	3
Orient-Express	Orient-Express Hotels, Trains & Cruises	10	0
Raffles	Raffles International Hotels & Resorts	0	2
Ritz-Carlton	Marriott International Inc.	10	0
Rocco Forte Collection	Rocco Forte Collection	11	2
Shangri-La	Shangri-La Hotels & Resorts	0	3
St. Regis	Starwood Hotels & Resorts	3	1
W Hotels	Starwood Hotels & Resorts	1	6
Stein Hotels and Resorts	Stein Hotels	13	3
JW Marriott	Marriott International Inc.	3	0
Grand Hyatt	Hyatt International Hotels & Resorts	1	0
Jumeirah	Jumeirah Hotels & Resorts	2	2

This list is not exhaustive.
Source: HVS Research

Of these brands, Kempinski and The Luxury Collection dominate the region with 31 and 33 hotels, respectively, in approximately 15 different markets. However, it must be noted that some of the hotels in the Kempinski portfolio do not fall into the luxury category. On the other hand, Shangri-La has no

properties in the region at the moment, and the St. Regis brand has only three.

We consider these brands to be the main players in the European luxury sector and further highlight the following.

Conrad has been conservative in its expansion plans, demonstrating a careful evolution in the number of properties in the region. Its first



property opened in 1989, and the most recent opened in 2002, in Ireland. Conrad currently has a total of just over 1,100 rooms, with one further hotel in the pipeline that will add 158 rooms to the portfolio (the Conrad Algarve Palacio Da Quinta due to open in 2010). The hotel group is keen to develop the brand in the region further and we expect target locations for Conrad to be destinations around the Mediterranean.

The Dorchester Collection

was rebranded in 2006 to develop an impeccable portfolio of traditional and contemporary properties in Europe and the USA. The



current portfolio of owned and managed properties includes The Dorchester in the heart of Mayfair in London, a 250-room hotel long favored by the cream of society; The Beverly Hills Hotel, a glamorous and celebrity-friendly 204-room property on Sunset Boulevard in Los Angeles; the elegant Le Meurice, a centuries-old, 160-room property between Place de la Concorde and the Louvre, on rue de Rivoli in Paris; Hôtel Plaza Athénée, a 146-room embodiment of Parisian luxury that stands between the Champs Elysées and the Eiffel Tower; and Hotel Principe di Savoia, a cosmopolitan, 401-room property on Piazza della Repubblica in Milan.

Fairmont Hotels is considered to be a reasonably new brand in the European market. What is striking is that the hotel group appears to follow a



trend of launching its hotels in the region every two years. The first hotel to be established in Europe was the Fairmont St Andrews Resort in Scotland, in 2001. Since

then, Fairmont has added another three properties. At the end of 2007, Fairmont acquired the London landmark hotel The Savoy, which is currently undergoing renovation and rebranding; the work is due to be finished in 2009.

Four Seasons has followed a course of constant expansion in Europe, opening two hotels in 2008: the Four Seasons Hotel Firenze and the Four Seasons



Hotel Istanbul at the Bosphorus. We are aware that the group is looking for some resort properties in high-end destinations in the Mediterranean. For example, we are aware of Four Seasons' wish to operate a hotel with a number of residential units in Montenegro.

Kempinski currently has a portfolio of 31 properties and a development pipeline with another 12 hotels



that are all to be completed by 2011. The brand has grown aggressively and has managed to establish itself in more than 15 countries over the past 20 years. Since 1992 the company has been investing in its portfolio by opening at least two properties every two to three years. Since 2002, however, the brand has been expanding even more rapidly: approximately two to three new hotels have opened each year. By 2011, we expect to see another 2,144 rooms added to the Kempinski portfolio.

The Luxury Collection

brand is well established in Europe and has significant market representation: 33 hotels currently. The brand has evolved



steadily since the opening of its first hotel, in London, in 1973. In the early 1990s, the brand followed a trend of opening at least two assets every two to three years. Since 1997, the brand's expansion strategy has been more dynamic: at least two properties a year have been opened or affiliated. In terms of its future

development strategy in the region, however, the brand seems to be taking a more conservative approach with only one new hotel in the pipeline, which is due to open in 2009.

Mandarin Oriental

first entered the European market in 2000 with the Mandarin Oriental Hotel du Rhône, in Geneva, and the Mandarin Oriental Hyde Park, in London. The company aims to develop in prime locations in order to create luxury properties that may be considered to be trophy assets. Not surprisingly, therefore, future destinations in Europe for Mandarin Oriental include cities such as Milan, Paris, Barcelona and Moscow.



Maybourne Hotel Group,

whose headquarters are in Mayfair, London, owns and manages Claridge's, The Connaught and The Berkeley: three of London's most renowned hotels. Maybourne was known as The Savoy Group until January 2005, when it was acquired by Irish property investment group Quinlan Private. Recently, after completing a £70 million refurbishment of The Connaught, Maybourne Hotel Group revealed that it is poised to announce its first overseas venture. This move will kick-start a phased roll-out of individually branded hotels in international gateway cities. The hotel group is considering locations such as Milan and Moscow within its European target locations.



The **Park Hyatt** brand debuted in Europe in 1990 with the acquisition of the Hotel Villa Magna in Madrid, which is currently undergoing renovation work. The hotel is due to reopen



later in 2008. The brand did not venture into other locations in Europe for another nine years until the opening of a hotel in Hamburg. In 2003, its expansion strategy shifted towards the development of properties in prime European cities, thus resulting in the opening of hotels in gateway cities such as Milan, Paris, Moscow and Zürich within a short space of time. Development plans for the brand are dynamic and strategic, though not aggressive. Future openings are planned in Turkey and Spain.



The majority of **Orient-Express's** European portfolio is in Italy, but the company also operates hotels in rural areas in France, the UK, Spain, Portugal and Russia. In many instances, Orient-Express hotels command one of the highest rates in the market and they are known for their excellent food and beverage facilities; many of the properties have a small (fewer than 100) number of keys and operate seasonally.



The **Ritz-Carlton** concept is a luxury hotel brand offered by Marriott. Ritz-Carlton has grown its portfolio very carefully in Europe both with resorts and with city centre hotels. The company's most prominent urban properties are the Hotel Arts in Barcelona, the Ritz-Carlton Berlin and, most recently, the Ritz-Carlton Moscow. Ritz-Carlton has added an affiliated hotel in Europe each year since 2000.



The **Rocco Forte Collection**

is a group of 11 highly individual hotels; five new hotels are due to open within three years (including an expansion into the Middle East and North Africa: in Marrakech, Jeddah and Abu Dhabi).

Shangri-La Hotels & Resorts

a leading luxury hotel group based in Hong Kong; is made up of 52 hotels in Asia and the Middle East. As of late 2007, 30 new properties were under development, including resorts in Europe and North America. Shangri-La does not yet have a presence in Europe; however, the company has secured sites in two of Europe's key gateway cities: London and Paris, both of which are subject to high barriers to entry. Shangri-La's third development in Europe will be in Vienna.

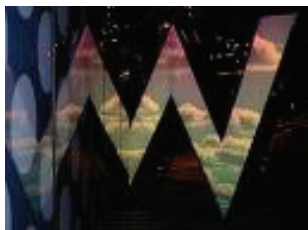


Owned by Starwood Hotels & Resorts, the **St. Regis Hotels & Resorts** brand traces its name and heritage to the internationally acclaimed St. Regis New York, the



original Beaux Arts classic landmark built by Colonel John Jacob Astor IV in 1904. There are 13 St. Regis hotels and resorts throughout the USA, the Caribbean, Europe and Asia, with each property designed to capture the personality of the destination. The Lanesborough in London is understood to be the city's highest performing luxury hotel in terms of average rate and revenue per available room (RevPAR).

Also owned by Starwood Hotels and Resorts, **W Hotels** is a global luxury lifestyle brand with 24 properties in several destinations



around the world. Inspiring, iconic, innovative and influential, W Hotels provides the ultimate in insider access. Each hotel offers a unique mix of sophisticated design, chic comfort, and cultural influences. W Hotels are unique and individual expressions of modern travel and stylish living, featuring international cuisine, destination bars and signature spas. The W Hotels brand is new to Europe having opened its first property in Istanbul in May 2008. The brand, however, has more aggressive plans in terms of development in the region with future

openings in luxury destinations including St Petersburg, Barcelona, Milan and London.

Stein Hotels and Resorts

specialises in the management of small luxury lifestyle hotels across Europe and North America offering a full portfolio of management services. The brand's philosophy is to combine the unique elements of Mediterranean lifestyle with the conveniences of today's modern world to create an atmosphere of relaxed sophistication within a discrete environment. The hotels are characterised by having 25- to 125-rooms with charming architecture and design, in idyllic locations, and in many cases emblematic and historic buildings regarded as local landmarks. With a portfolio of 14 properties in the region, the brand is well established in the luxury market in Europe, especially in London and Spain where nearly half of its assets are located. The Elizabeth will be opening soon in London, as well as another property in Mallorca, the Sa Vinya de Son Net which is expected to have 12 rooms.



JW Marriott Hotels and Resorts

is Marriott's most luxurious brand offering high levels of comfort to leisure and business travellers. The brand currently has a portfolio of 54 properties worldwide, three of which are located in Europe. Currently the brand is still in its early stages as few properties have been developed within the region. The Grosvenor House in London has recently opened after a renovation and rebrand scheme which revealed the property as the brand's newest addition.



Grand Hyatt

hotels serve large business destinations that attract leisure and corporate travellers, as well as large-scale meetings and conventions. The business hotels include state-of-the-art technology,



sophisticated business and leisure facilities, banquet and conference facilities, and specialised programmes that cater to business travel and leisure guests. The Grand Hyatt brand currently has only one property in Europe with the Grand Hyatt Berlin. Since the opening of this asset, the company has not been developing the brand in the region, and has been more active with its Park Hyatt brand. It is important to note that Hyatt has recently announced that it will be playing a more dynamic role in the development of its brands across all regions worldwide.

Jumeirah, formerly known as Jumeirah International, is developing a global super-brand under a single, distinctive and memorable name. All of its hotel



names will feature the Jumeirah identity, yet each will retain their individual style and uniqueness. Jumeirah, which is more commonly known around the Middle East where it originated, has been growing in the European markets. With two European properties in its portfolio, both of which are located in London, the hotel group has plans to establish itself as a luxury brand in the region. Jumeirah has signed an agreement with Beetham Organisation to create the Jumeirah Hotel at Beetham Tower in London; the new £600 million slender curved glass landmark for London is to be built on London's South Riverbank, which is subject to planning permission and expected to open just in time for the London Olympics in 2012.

In addition to the brands highlighted above, we note that brand development continues to grow as hotel operators face stronger competition in the sector. Companies such as Accor, Starwood, Hyatt and Hilton have further enhanced their brand awareness and offering by adding new luxury brands under their flags. Amongst these are Waldorf=Astoria (Hilton), Baccarat (Starwood

Capital), Crillon (Starwood Capital), 1 Hotels and Residences (Starwood Capital), Andaz (Hyatt), and the recently launched MGallery (Accor).

Luxury Hotel Performance in Selected Markets

The European hotel market has proven to be a strong market over the past few years.

Traditionally, it has been an extremely resilient market, despite terrorist attacks, avian influenza and extreme weather, which underlines the sector's ability to rebound from external shocks, such as the terrorist attacks in London and the luxury hotel sector's fast recovery (after just three months).

Between 2003 and 2007 RevPAR in Europe grew by 6% annually. The good years for tourism in Europe in 2006 and 2007 translated into an excellent hotel performance across the continent, with occupancy close to 70% and average rate above €110 overall. Owing to economic conditions, we expect 2008 to experience a slight decrease in occupancy, with average rates remaining in line with the previous year.

European cities are privileged in the number of luxury properties that are available, and many of them have established luxury flagship assets. Table 7 gives an overview of the luxury market performance for both established and emerging gateway cities in Europe. London, Paris and Milan are considered established destinations in the luxury segment and feature stable luxury hotel performance figures as indicated below. Munich and Barcelona are two of the emerging destinations within the luxury segment as they have a significant amount of luxury room stock at present and further luxury developments in the pipeline.

Table 7 Luxury Hotel Performance in Selected Cities 2005-07

	2005			2006			2007		
	Occupancy	Average Rate (€)	RevPAR	Occupancy	Average Rate (€)	RevPAR	Occupancy	Average Rate (€)	RevPAR
London ¹	76 %	477	363	83 %	540	448	84 %	600	504
Paris ²	68	555	376	72	617	446	76	688	525
Munich ³	77	286	220	78	317	246	74	284	210
Milan ⁴	56	430	239	64	464	299	65	482	312
Barcelona ⁵	69	288	197	72	309	224	73	346	253

¹ Sample includes The Dorchester, The Lanesborough, Claridge's, Four Seasons Park Lane, The Berkeley, Mandarin Oriental Hyde Park

² Sample includes Le Meurice, Four Seasons George V, Plaza Athénée, Hotel Le Bristol, Hotel de Crillon, and Hotel Ritz

³ Sample includes Mandarin Oriental Munich (under refurbishment in 2007), Kempinski Vier Jahreszeiten, Hotel Bayerischer Hof and The Charles Hotel (opened in October 2007)

⁴ Sample includes Four Seasons Milan, Bulgari Hotel, Principe di Savoia, Grand Hotel et de Milan, Park Hyatt Milan, and Carlton Baglioni

⁵ Sample includes Hotel Arts, The Palace, Majestic, Omm, Gran Hotel Florida, Claris, Casa Fluster, and Rey Juan Carlos I

Source: HVS Estimates

London has long been an established luxury hotel market, linked closely to the business and leisure demands in the city. The luxury segment has seen some supply growth over the last few years with the opening of properties such as the Mandarin Oriental, as well as a number of renovations and rebranding schemes, such as the acquisition of the Maybourne Hotel Group by Quinlan Private (which resulted in a £70 million refurbishment of The Connaught), and the renovation of the Savoy and the Four Seasons Park Lane. London's luxury segment has enjoyed increasing occupancy rates leading to a rise in average rates, and consequently a growth in RevPAR levels in the past three years.

We expect the market to become slightly more competitive with the addition of luxury properties such as the reopening of The Savoy and the opening of the 195-room Shangri-La Tower Bridge in 2012, as well as the Jumeirah Beetham Tower, the new £600 million slender curved glass landmark for London that is to be built on London's South Riverbank, just before the Olympic Games. In addition, the former Playboy Club and Casino will become the latest addition to Dorchester Collection portfolio as an extension of the existing Dorchester hotel on 45 Park Lane, which has already achieved planning permission. We are also aware of several unconfirmed projects.

Paris is yet another established luxury hotel market, linked closely to commercial demand as well as the fashion industry. The luxury

segment has seen virtually no supply growth over the last few years. However, we note that the following new supply will be entering the city in the near future.

- A 150-room Mandarin Oriental will be located within the redevelopment of a 1930s Art Deco building at 247-251 rue Saint Honoré, in the historic and fashionable centre of the city. The estimated opening date for this hotel is mid 2010;
- The 118-room Shangri-La hotel will be on 10 avenue d'Iena, in Paris's 16th arrondissement. Located near the Eiffel Tower and the Trocadero, the hotel, converted from the Palais Bonaparte, will offer some of the city's finest views of the River Seine. The estimated opening date for this hotel is the beginning of 2009;
- The 213-room Royal Monceau, near the Salle Pleyel and the western end of Faubourg St Honoré, closed in June 2008 for a complete overhaul by designer Philippe Starck. The hotel is due to reopen in 2009. After the renovation, each floor will feature a small lobby overlooking the interior gardens.

Munich has an established luxury segment and is considered to be Germany's main luxury destination. Currently, Munich has a healthy pipeline for future developments in the city, a number of them being within the luxury segment. The opening of new luxury supply will have a positive effect on the

market by enhancing Munich's image as a luxury destination. In 2006, the city achieved record occupancy levels, over 78%, which highlights the city's appeal as a destination.

In October 2007, Rocco Forte opened its landmark property, The Charles Hotel, adding another luxury asset to the city's supply. The hotel added 132 rooms to the local five-star segment and is Rocco Forte's second opening in Germany after the Villa Kennedy in Frankfurt, which opened in 2006.

Milan, similar to Paris, is an established luxury hotel market, whose close links to commercial demand as well as the fashion industry make it an attractive destination for investment in the sector. The luxury segment had seen little supply growth over the last few years until the opening of the Bvlgari Hotel and the Park Hyatt Milan.

Consequently, hotel occupancy suffered in 2005 with the opening of two new hotels, but 2006 and 2007 have proven that this new supply has been successfully absorbed. We expect to see the following developments in the city in the near future.

- A W hotel is expected to open in 2010 in the heart of the Brera district. This hotel will feature 76 rooms and will be the third property managed by Starwood Hotels & Resorts in Milan;
- Casa Armani, the famous Italian fashion house, will open a hotel on the upper floors of its Armani shop, located at the junction of Via Manzoni and Via Montenapoleone. The hotel will have approximately 80 rooms and is estimated to open in 2010;
- A Mandarin Oriental hotel is currently under development on Via Monte Di Pieta. This property is being developed by Statuto Group. The proposed hotel will feature between 97 and 104 rooms and is expected to open in March 2010.

Barcelona is a very well-established, mature market with historical occupancies of around 70%. 2006 and 2007 proved to be very good years for the Barcelona hotel market with occupancies of 70% and 73%, respectively. Barcelona was able to record a strong increase (roughly 14%) in average rate between 2006

and 2007, on account of the limited supply growth in the luxury segment and strong demand from the Free Independent Traveller (FIT) and Meeting, Incentive, Conference and Exhibition (MICE) segments.

Barcelona will further enhance its image as a top-class destination with the following developments.

- The second W Hotel in Europe: a luxury landmark designed by the architect Ricardo Bofill. The W Barcelona will appear as a modern icon above the Catalan capital, along the waterfront. The 473-room hotel is scheduled to open in September 2009 and the total investment is said to amount to €180 million. The hotel will have dining, entertaining and nightlife facilities, a spa, a rooftop bar, a retail outlet, indoor and outdoor pools, and extensive meeting facilities. The W Hotel is being developed by four of Spain's leading real estate consortia – FCC Construction SA, COMSA, OHL SA, and Sacresa – under a long-term concession agreement from the Port Authority of Barcelona.
- The 98-room Mandarin Oriental hotel will be positioned at the very centre of Barcelona, in Paseo de Gracia, a location that will provide easy access to the city's most exclusive shopping area, and its dining and cultural venues. Furthermore, the property will have various dining facilities, bars and a spa including private treatment rooms with water and heat therapies.

The Impact of the 'Credit Crunch'

At the beginning of the second half of 2007, the world began to experience an economic crisis which came to be known as the 'credit crunch'. As the real estate markets started to decline, lending and financing from banks and financial institutions decreased, which led to a slower investment arena in the hotel sector.

Recent credit restrictions have had a reasonable impact on some projects already under construction, which had to be halted or delayed due to lack of financing. New hotel developments have decreased in terms of

project numbers as developers who still need to obtain financing are facing more difficulties when being granted a loan. However, it must be noted that interest in the luxury segment is still very much alive and that financing for trophy assets in prime locations may have an advantage.

In terms of performance, luxury hotels are likely to see occupancy levels drop, which will in turn have an impact on RevPAR levels, as average rates are expected to remain at similar levels as 2007, with growth remaining at inflation levels, if not stabilising. In order to attract demand, it is likely that we will see the market discounting rates in the short term.

The luxury hotel sector has shown to be more resilient to the economic downturn up until now. However, in the face of increased competition amongst operators and the variety in brands in the segment, hotel chains will have to differentiate their services and products in order to stand out in the market and attract their client base. Guest satisfaction in the luxury segment is extremely important and, at times when operating costs are rising, such properties still need to offer their guests an experience that is remarkable and outstanding.

Future Outlook

Prospects for 2008/09 are uncertain as we go into a global economic slowdown which has had an impact across all industries, including the hotel industry. Also, it should be noted that major events (those drawing a large number of spectators) have been few and far between in 2008, compared to 2007 and in particular to 2006. Certain factors, such as climate change, which may possibly result in higher taxes for businesses and individual travellers, and the appreciation of the euro against the US dollar also deserve attention. Conversely, the affluence of and the increase in travel demand from the 'BRIC' countries (Brazil, Russia, India and China) are expected to contribute positively to European tourism and to the luxury hotel segment. Luxury hotels across Europe are expected to record lower

occupancy levels in 2008, with an estimated recovery beginning, at the earliest, in 2010 according to industry professionals. Average rates will remain competitive across the sector as the main players aim to retain their customers and attract new wealthy individuals to the higher end of the accommodation sector.

Brand awareness and differentiation will be significant factors amongst luxury brands as competition increases and the luxury concept widens.

Despite this year's tougher market conditions, hotels continue to attract developers' and investors' interest. Although it is undeniable that as a result of the subprime crisis there is less debt available for investors, it should be noted that opportunities in the market remain, and demand for luxury is still high – especially in gateway cities and for internationally branded luxury hotels. The luxury segment is expected to feel less of an impact from the current situation, as cash-rich high net worth individuals, with increasingly liquid prosperity, continue to give preference to trophy assets and are ready to spend their money on such products and investments. These may well be from the new-found billionaires in the emerging BRIC countries who are keen on European travel and investment opportunities. We expect to see further opportunities in Central and Eastern European markets as these countries still show considerable potential. The credit crunch will also reveal the market presence of brands not only in the luxury sector but across the entire hotel industry, which as a result will clearly indicate where each brand stands and the opportunities available for success.

The luxury hotel market along with the travel industry will continue to grow and draw interest from different parties that regard it as a sound investment opportunity as well as an attractive consumer product. To guarantee sustainability in the future it is necessary that the luxury hotel sector adapts to global changes concerning environmental issues as well as trends in consumer demand.

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