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CAIRO I SHARM EL SHEIKH

BEFORE AND AFTER

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Introduction

Egypt has endured dramatic political turmoil and instability over the course of the last two years. Beginning in January 2011, the Egyptian Revolution began as a campaign of non-violent civil resistance, which despite its non-violent nature, resulted in 846 dead and 6,000 injured. On the 11th February, 2011, after persistent protest and pressure, history marked the resignation of President Hosni Mubarak and resulted in administrative and legislative control of the country being surrendered to the Supreme Council of the Armed Forces. The volatile months that followed were defined by tens, and sometimes up to hundreds, of thousands of demonstrators protesting for action against former regime figures, public prosecution, and corrupt officials. Demonstrations continued into 2012 with ongoing demonstrations protesting the disqualification of several candidates in the then-upcoming presidential elections. In June 2012, Mubarak was sentenced to life imprisonment and it was announced that Mohammed Morsi had won the presidential election.

As a result of the turbulent episode between 2011 and 2012, the hospitality sector endured the backlash and the repercussions of the infamously entitled *Arab Spring*, with the hotel sector being among the hardest hit both locally and regionally. Throughout this publication, HVS reviews the macroeconomics, the recent performance of the hotel industry in the popular tourist destinations of Cairo and Sharm El Sheikh, and provides an indication of the short-term and the mid-term outlook for the industry.

A Macroeconomic Perspective

Tourism in Egypt typically contributed over 10% to the gross domestic product (GDP) of the Egyptian economy. According to official figures, visitation to Egypt declined by 47% between 2010 and 2011, resulting in a decline of 42% in terms of tourist revenues. Economic growth weakened considerably in 2011 as a result of the domestic situation, with 2012 experiencing a minor ripple effect. Assuming internal stability and a rise in foreign direct investment (FDI), the growth of the economy is expected to return to previous levels by 2014. Egypt has asked the International Monetary Fund (IMF) for a stand-by credit facility of US$4.8 billion, the results of which should be negotiated during the time of writing this publication. The loan should boost confidence among investors and allow the introduction of other external support, thereby pushing investment inflows.

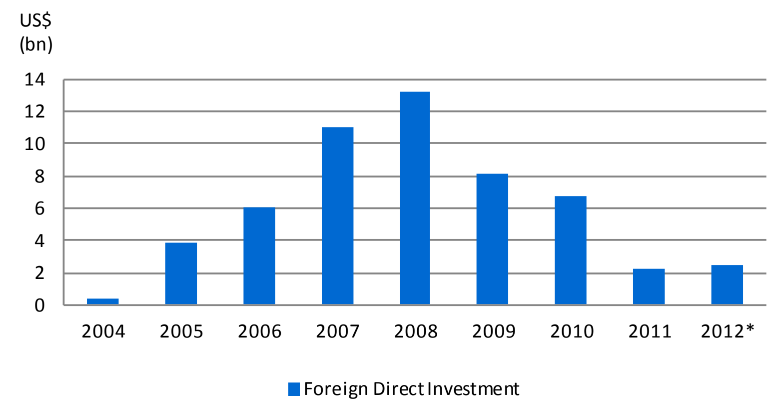
Figure 1: Egypt Economic Indicators

	Actual*		Forecast*					
	2010	2011	2012	2013	2014	2015	2016	2017
Real GDP growth (%)	5.1	1.8	2.2	3.3	6.2	6.7	7.1	6.4
Consumer price inflation (av %)	11.1	10.2	7.6	8.2	7.8	7.5	7.9	8.1
Budget balance (% of GDP)	(8.1)	(10.0)	(11.1)	(10.5)	(9.0)	(7.7)	(7.0)	(6.2)
Current-account balance (% of GDP)	(2.6)	(3.3)	(3.2)	(3.0)	(1.2)	(0.5)	0.1	0.1
Exchange rate EGP:US$	5.63	5.94	6.05	6.82	6.77	6.54	6.12	6.09

Source: Economist Intelligence Unit, October 2012

According to reports, FDI in Egypt has made a partial recovery in the meantime, reaching US$2.5 billion in the first six months of 2012. This compares to US$4.1 billion in the first half of 2010, which remains significantly below previously levels of investment; nonetheless, showing signs of returning confidence when compared to 2011 figures. Compound annual growth between 2004 and 2011 reached approximately 28%, while year on year growth between 2010 and 2011 resulted in a contraction of roughly 67%.

Figure 2: Foreign Direct Investment

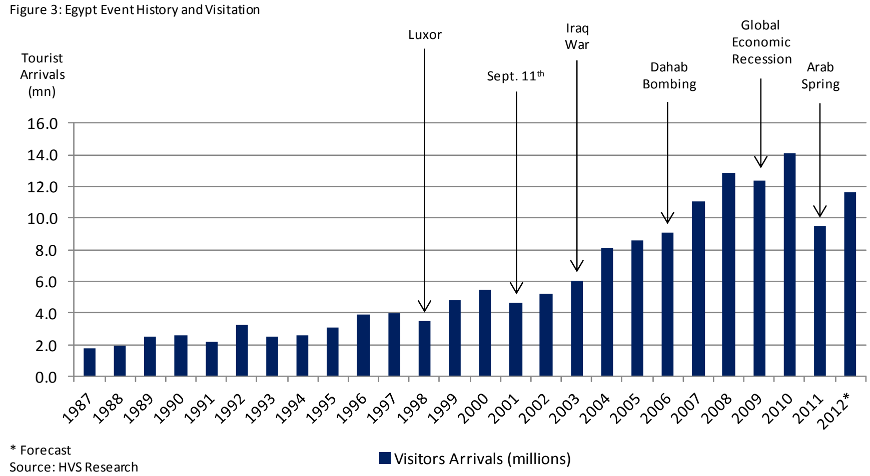


Source: Central Bank of Egypt
* Year to June

The History

Egypt has long been an attractive tourist destination, with lenient regulations and the unrestricted hospitality policies attracting millions of Europeans annually. As one of the most populous countries in Africa and the Middle East, Egypt plays host to ancient monuments such as the Giza pyramid complex and the Great Sphinx, as well as ancient ruins such as those of Memphis, Thebes, Karnak and the Valley of Kings. Moreover, Cairo is Africa's largest city and has been renowned for centuries as a centre of learning, culture and commerce. Historically, Egypt has endured and been subject to numerous periods of instability. Nonetheless, the resilience of the country's tourism sector was tried and tested, and the resulting trends are indicated in Figure 3; following war, terrorism, and economic instability, the country rebounds persistently. With a 32% decline registered in 2011 in terms of visitation, Egypt expects to end the year with 11.6 million visitors, an increase of 22.1%.

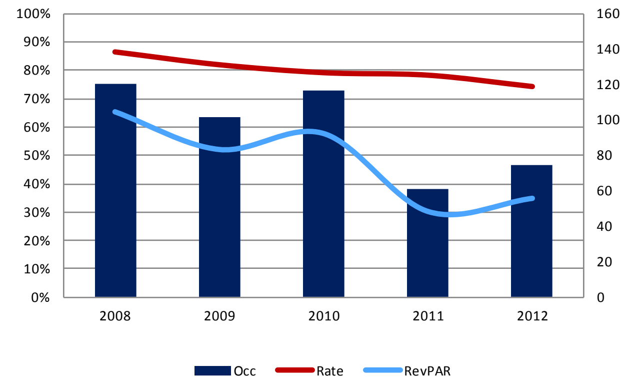
Figure 3: Egypt Event History and Visitation



* Forecast
Source: HVS Research

Cairo, having been at the epicentre of the turmoil, experienced a significant decline in tourism, resulting in occupancy of roughly 38% in 2011, a decline of approximately 50% over 2010 figures. Average rate, on the other hand, remained stable between 2010 and 2011 at US$125.10. As Cairo emerges from the instability and the damaged visitor confidence, average rates have witnessed a year-to-date decline of roughly 5.0%. Notwithstanding, hotel occupancy in the capital has experienced 22.0% growth over 2011 to 46.7%, reflecting the resilience illustrated earlier. As a result of the dynamics of average rate and occupancy, RevPAR has grown by 15.0% between 2011 and 2012, minimizing the losses incurred from the contraction in average rate.

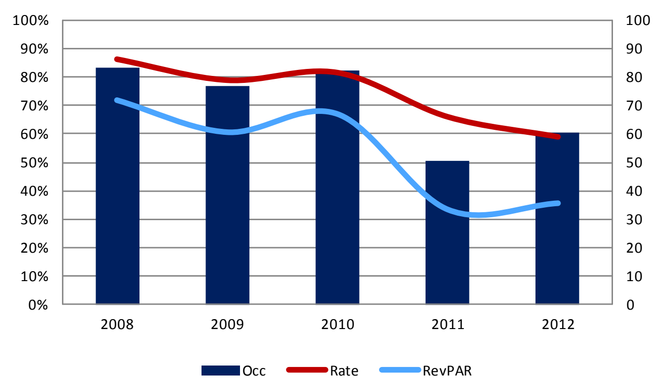
Figure 4: Cairo Key Performance Indicators



Source: HVS Research

Sharm El Sheikh, on the other hand, was formerly a port, however, commercial shipping has been greatly reduced as a result of strict environmental laws introduced in the 90s. The natural resources of Sharm El Sheikh as well as its proximity to European tourism markets stimulated rapid tourism growth between 1982 and 2000. During this time, the number of resorts in the area increased from three to 91. Accommodated room nights recorded similar growth during this period, increasing from 16,000 in 1982 to 5.1 million in 2000. By 2011, hotel supply was estimated at 180 hotels, constituting nearly 30% of the total supply in Egypt and powered by the five-star sector. Sharm El Sheikh is dominated by the leisure segment, which is typically made up of wholesale leisure and FIT leisure. The destination also boasts an international congress centre, thereby generating additional demand with the meeting and group segment.

Figure 5: Sharm El Sheikh Key Performance Indicators



Source: HVS Research

Following the *Arab Spring*, Sharm El Sheikh experienced a dramatic decline in tourism, resulting in occupancy of roughly 51% in 2011, a decline of nearly 40%. Similar contractions were experienced in average rate, which declined by approximately 20% to US$66.08 between 2010 and 2011. Figures in 2012, on the other hand, indicate that occupancy has rebounded to 60.3%, an increase of 20.0%, albeit at the expense of average rate, which exhibits a contraction of approximately 11.0% and mirrors the trend observed in Cairo. As a result of the dynamics of average rate and occupancy, nonetheless, RevPAR exhibited growth of roughly 7.0% over 2011, reinforcing also in Sharm El Sheikh that confidence is gradually being restored.

And The Future

According to a release of recent statistics, growth in the demand for accommodation is in line with the figures presented earlier. According to Egyptian Minister of Tourism, Hisham Zaazou, tourist growth in the first ten months reached almost 19.0% over the same period last year, with 9.6 million tourists visiting the country. Moreover, this number was expected to climb to 11.6 million by December 2012. Nonetheless, the question presents itself as to the avenue that the new regime will pursue under Morsi's stewardship. Whilst the FJP repeatedly denies plans to restrict tourist activities, such promises have failed to reassure sceptics, who express concern that the Brotherhood may not be capable of accepting the predominantly packaged and all-inclusive holidays in Egypt's tourist hotspots, replete with parties and alcoholic beverages. Equally harbouring the potential to incite instability, are relations with neighbouring Israel and the status of the peace treaty signed in 1979. Though the Muslim Brotherhood announced that Egypt would continue to abide by all its international and regional treaties, recent moves by the Egyptian military are counterproductive to the treaty.

In spite of this and based on the assurance currently endowed, the outlook for the two popular destinations in Egypt remains optimistic. Assuming that the worst is behind them, and a return to growth evident among the key performance indicators, Egypt is expected to return to previous levels of hotel and resort visitation within the medium- to long-term. It may be deduced that the hotel sector will follow a similar growth pattern that is forecast for the Egyptian economy, subject to sustained stability. Notwithstanding, a majority of visitation to Egypt originates from Europe. With ongoing economic turmoil in the western world, the resilience of Egyptian tourism is also dependent on factors outside of its own control. One thing does remain certain; Egypt will forever remain host to ancient ruins, culture and six thousand years of recorded history.

About HVS

HVS is the world's leading consulting and services organisation focused on the hotel, restaurant, shared ownership, gaming, and leisure industries. Established in 1980, the company performs more than 2,000 assignments per year for virtually every major industry participant. HVS principals are regarded as the leading professionals in their respective regions of the globe. Through a worldwide network of 30 offices staffed by 400 seasoned industry professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. For further information regarding our expertise and specifics about our services, please visit **www.hvs.com**.

HVS has a team of Middle East experts that conducts its operations in the Middle East and North Africa. The team benefits from international and local cultural backgrounds, diverse academic and hotel-related experience, in-depth expertise in the hotel markets in the Middle East and a broad exposure to international hotel markets. Over the last four years, the team has advised on more than 300 hotels or projects in the region for hotel owners, lenders, investors and operators. HVS has advised on more than US$48 billion worth of hotel real estate in the region.

About the Authors

Rico Picenoni is an Associate, working with the HVS Dubai office, specialising in hotel valuation and consultancy. Rico holds a BSc from l'Ecole Hôteliere de Lausanne, Switzerland. Providing over six years of operational experience in various management positions, Rico has performed consulting and valuation assignments in multiple markets, across various asset classes in the Middle East.

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Hala Matar Choufany, MRICS is the Managing Director of HVS Dubai and is responsible for the firm's valuation and consulting work in the Middle East and North Africa.

Since joining HVS, she has worked on several mid and large scale mixed use developments and conducted numerous valuations, feasibility studies, operator search, strategy advice, return on investment and market studies in Europe, MENA and Asia. Hala has in-depth expertise in regional hotel markets and a broad exposure to international markets and maintains excellent contacts with developers, owners, operators, investment institutions and government entities.

Hala holds an MPhil from Leeds University, U.K., an MBA in Finance and Strategy from IMHI (Essec-Cornell) University, Paris, France and a BA in Hospitality Management from Notre Dame University, Lebanon. Hala is fluent in English, French and Arabic.

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