Horwath HTL
Hotel, Tourism and Leisure

MARKET REPORT

Poland: *Hotel Market*

APRIL 2019

Economic situation and development

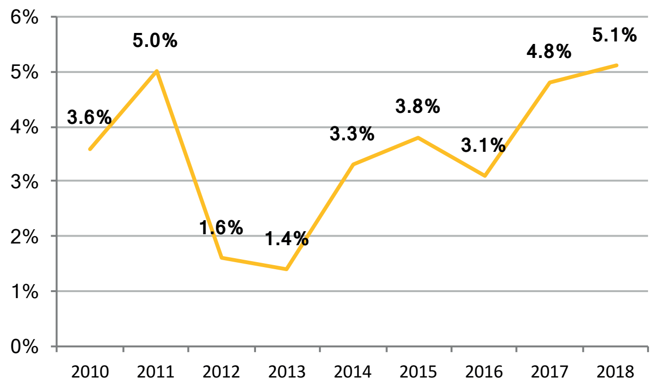
Poland is not only gradually reducing the distance to the richest EU countries but is now in the elite group of the 25 most developed economies in the world.

Poland ranked 36th in the world in the level of globalization, measuring 169 countries using th Global Connectedness Index. Growing ADR and Occupancy levels of hotels in major Polish cities were encouraging investors to open new hotels.

In 2018, Poland was promoted in the FTSE Russell index to the group of developed markets. It was the first promotion over the last ten years. It is also the first country in Central and Eastern Europe to join this elite group of world economies. It is a chance for Poland to increase the flow of foreign capital into the country.

The Polish economy is steady and and experiencing an increasingly stable expansion. Polish GDP is consistently growing. In the region and among the 28 European Union countries Poland still records one of the highest gross-domestic- product (GDP) growth. GDP rose in 2018 by 5.1% year on year, while amongst EU countries GDP growth was 1.9% overall and -1.8% in the Euro zone.

GDP Growth in Poland in 2010 - 2018



Source: Central Statistical Office, 2019

According to Brand Finance, the brand "Poland" holds 23rd place in world ranking with an increase of value of 14%. It means that the value of the national brand is built on information such as the positive political transformation in 1989 and the steady economic situation during the world financial crisis. This rapid development and positive change encourages many foreign investors.

In the 2018 ranking prepared by UNCTAD (United Nations Conference on Trade and Development) assessing internationalization of the economy places Poland in sixth plave worldwide.

Since mid-2018 all of Poland's territory has become a special economic zone. The new regulations allow tax exemptions for investors for 10-15 years. Not only large but also small and medium enterprises are now able to apply for incentives.

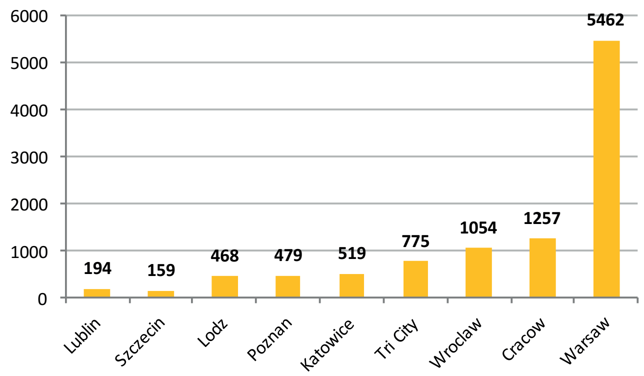
Favorable economic conditions, along with a cheap and well-educated Polish workforce and a huge domestic market, make Poland one of the most attractive locations for foreign direct investment (FDI) in Europe. Since 2004, when along with joining the EU, the Polish market became much more 'reachable' for those other than domestic investors, the inflow of foreign direct investment has significantly increased compared to the beginning of the decade. Poland has become a key destination for many investment portfolios.

As a result, there is an active office supply market, led by Warsaw as well as other major Polish cities such as Cracow, Poznan, Wroclaw, Gdansk and Lodz. According to Cushman & Wakefield the office market in Poland continued to progress in 2018 and is still dominated by Warsaw, which holds a 53% market share of the total modern office stock.

The highest investment activity recorded was in the office market in Warsaw. The investment activity in the office market in regional cities, mainly Cracow, Wroclaw but also Gdansk, Lodz, Katowice and Poznan has been high in recent years too (Wroclaw is the third city in Poland, after Warsaw and Cracow, to exceed 1 million square meters of office space in stock).

In 2018, investment activity in the Warsaw office market reached a record value of EUR 1.7 billion in 28 transactions. In comparison, 12 transactions were carried out in the regional cities with a total volume of EUR 0.9 billion.

The supply of office space in major Polish cities in 2018



Source: Colliers International, March 2019

The above are the cities with a significant boost in the economic market of the country. Warsaw has almost 5.5 million square meters of office space supply, according to

Colliers International. There is 1.8 million square meters of modern office space under construction in Poland. The new supply completed in 2018 accounts for 744,000 square meters.

The fastest developing areas in Warsaw are Sluzewiec and Wola. The stable demand for the office space and commercial real estate is driven by extraordinarily intensive development of the Business Process Outsourcing (BPO) sector developing almost 15 years in Poland. The real boom for these services began in 2010. The extremely dynamic development of this industry in Poland is surprisingly positive. In terms of the level of employment it can be compared to traditional economic sectors such as motorization. The vast majority are entities with foreign capital - they are responsible for 81% of employment in the entire sector.

The Polish economy in recent years has revived large investments in infrastructure: construction of national and local roads; expansion and construction of new airports, including Gdansk, Poznan, Wroclaw, Rzeszow, Katowice, Warsaw- Modlin, Szczecin, Lodz, Olsztyn-Mazuria, Lublin and Radom. The current number of airports in Poland grew to 15 during last few years. The government is currently carrying out the strategic project of a new airport with connection to the railway hub in central Poland.

According to the forecasts of the Civil Aviation Authority in Poland, the number of passengers at Polish airports will be increasing in the next 15 years. In 2035 the total number of passengers serviced on Polish airports will amount to 94 million.

Recently, public funds were also invested in modernising the railway lines and stations. In December 2014, thanks to the launch of Pendolino trains, the travel time between Warsaw - Cracow was shortened to 2.2 hours, and from Warsaw - Gdansk to 2.5 hours.

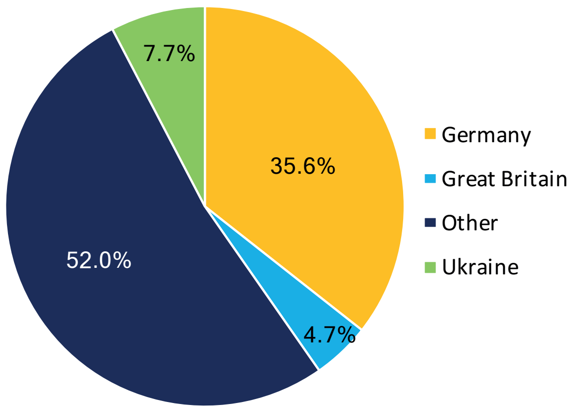
Major investments have been made in road development. In total, this resulted in around 3,500 kilometers of new roads and highways. In the years ahead 1,500 kilometers are under construction, from which almost 500 kilometers are scheduled to be open in 2019.

A boost of for tourism in Poland

Poland is recognized as a country with great development prospects, huge infrastructure investments and a and a tourism destination with many varied attractions. After many events of worldwide recognition Poland became an attractively perceived place on the map of Europe. Hosting events with worldwide recognition has helped to create a positive perception of Poland within Europe. Poland has hosted many important events such as United Nations Climate Change Conference (twice), UEFA European Championship in football, World Cup in volleyball (twice), World Cup in handball, Eurobasket, World Youth Days, NATO summit to name a few.

There has been a sustainable increase in the number of people coming to Poland. The statistics of Ministry of Sport and Tourism in Poland cite around 19 million tourists (each person that stayed overnight in Poland) traveling to Poland in 2018. In 2018, Warsaw Chopin Airport exceeded 17.7 million passengers per annum, which shows an increasing trend comparing to previous years.

Nationality of foreign visitors to Poland (2017)



Source: Central Statistical Office, 2019

In 2017, 83.8 million foreigners came to Poland which was 4.1% more than in the previous year. Among them, 18.3 million were tourists (4.5% more than in 2016) and 65.5 million one-day visitors (4.0% more than in 2016). In the case of foreign tourists, the main purpose of the visit was visiting relatives or friends (almost 38%), followed by recreation, holidays (around 27%) and business matters (almost 25%). One-day visitors came to Poland mainly for shopping (almost 84%), then for recreation, holidays (over 4%) and for business purposes (almost 4%).

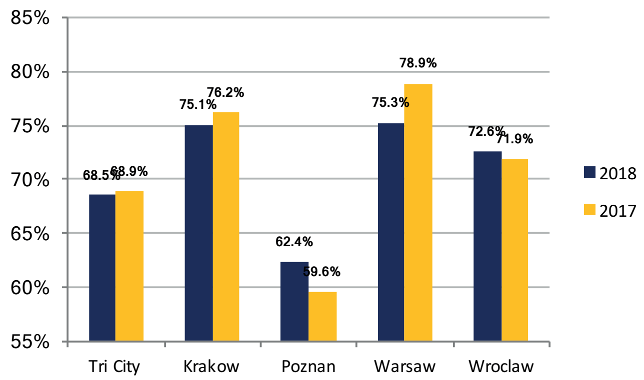
German tourists play a dominant role in the Polish tourism market. They contribute to 35.6% of all tourist arrivals to the country. Another important group for Poland are Ukrainians. They contribute to 7.7% of all tourist arrivals. According to the Polish Tourist Organization, Poland notes also increasing number of tourists from Asian countries such as: India, China, Japan, and an increase is predicted in following years.

Poland also has a strong domestic tourism market because there is a solid leisure base in holiday resorts, as well as the business areas developed in the city. The motivation of the Poles to travel has been recently stimulated by the development of governmental social policies specifically the "500+" program.

According to the World Travel & Tourism Council, the total contribution of Travel & Tourism to Poland's GDP in 2017 was 4.5% and is forecast to rise to 5.5% of GDP in 2028. Leisure travel spending (inbound and domestic) generated 70.6% of direct Travel & Tourism GDP in 2017 compared with 29.4% for business travel spending. Domestic travel spending generated 29.8% of direct Travel & Tourism GDP in 2017 compared with 70.2% for inbound travel spending.

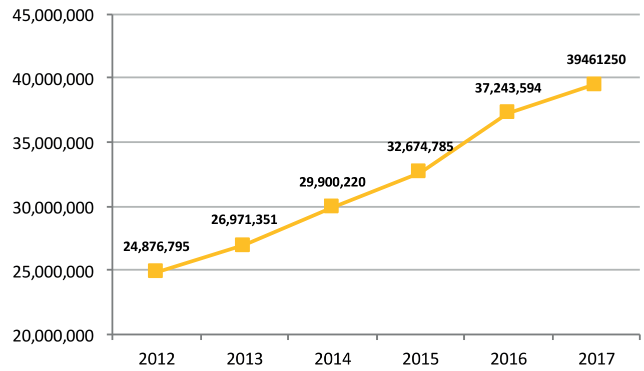
Data gathered by STR Global, shows that Warsaw and Cracow were in the leading position in terms of occupancy rate as of December 2018. However the occupancy rates in main Polish cities are slightly decreasing due to a vast growth of supply of hotel beds.

The occupancy rate in main cities in Poland in 2018 and 2017



Source: STR data , December YTD2018 vs. December YTD2017

Number of overnight stays in hotels in Poland



Source: Central Statistics Office, 2019

Hotel Development

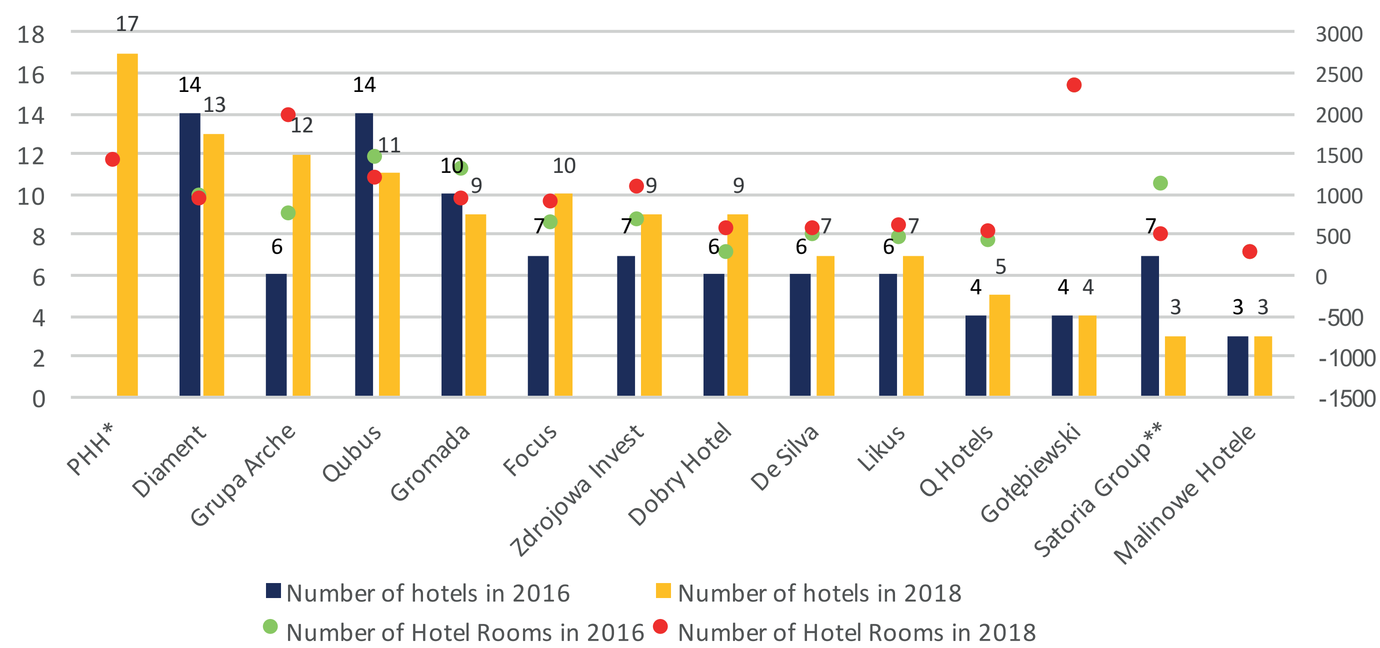
The Polish hotel market has been in the midst of intensive growth for several years. Growing ADR and Occupancy levels of hotels in major Polish cities were encouraging investors to open new hotels. As a result new hotel brands and new hotel chains are entering Polish market with incredible speed.

Both domestic and foreign hotel chains operate across Poland. According to Horwath HTL in 2018 there are 366 categorized chain hotels in Poland, both domestic and international (in 2016 there were 330 chain hotels).

Among Polish hotel chains, the biggest growth in the number of opened hotels was noted by Arche Hotel Group, which doubled the number of hotels since 2016. This hotel chain often builds hotels as condo properties, which makes the financing faster and enables such a rapid growth in the number of hotels. Polish hotel chains like Zdrojowa Invest, Focus Hotels or De Silva also opened new hotels.

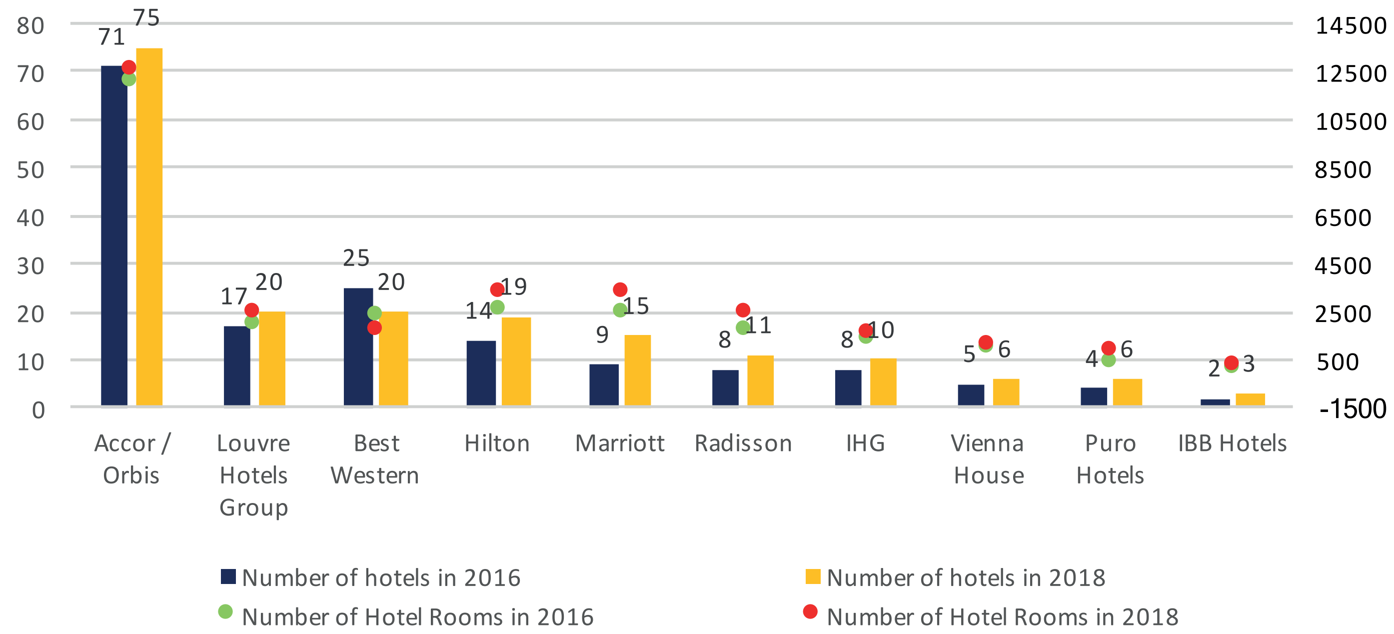
In 2019, Chopin Airport Development, the state owned management company owning 8 hotels under international brands in Poland, was transformed into Polish Hotel Holding, which took over Polish hotel chains AMW, GAT and WPUT. The goal of PHH is to consolidate state owned hotel chains and adjust them to modern standards of hospitality. Horwath HTL had the privilege of advising PPH in this process.

Selected Domestic hotel chains in Poland in 2016 vs 2019



Source: Horwath HTL 2019
**PHH – Polski Holding Hotelowy -Polish Hotel Holding, in addition to 17 listed hotels PHH is also managing 8 hotels under international brands (they are included in the list as chain hotels)*

Selected International hotel chains in Poland in 2016 vs 2019



Source: Horwath HTL 2019
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For the last couple of years international hotel chains have been intensifying the developments of their brands in Poland. Since 2016, the only international chain that noticed a decrease in the number of hotels is Best Western.

Currently, the top three international hotel chains in terms of the number of hotel rooms in Poland are Accor/ Orbis, Hilton Worldwide and Marriott International. All of them noted an intensive growth in the number of hotels and hotel rooms since 2016, the growth primarily achieved through the application of franchise agreements.
What makes it even more interesting is that international hotels chains are launching new hotel brands in the Polish market. Since 2016, we have experienced the introduction of a number of new hotel brands in major Polish cities, for example Indigo Hotel (IHG), Moxy (Marriott International), Renaissance (Marriot International), Metropolo by Golden Tulip (LHG) and first Leonardo hotel.

Moreover, new luxury international brands have entered the Polish market – in 2018 the first Raffles hotel was opened in Warsaw with 106 rooms. In 2019, another luxury hotel entered the Warsaw market but this time belonging to Polish hotel chain – Likus hotel, which is a private own company. In Cracow in 2019 Accor has opened its first MGallery.

One of the signs that the development of the hotel market in Poland has entered a new stage is the interest of international hotel chains in opening hotels in resort destinations. Radisson will open a Radisson Blu in Zakopane (2019, mountain area), Hilton will open a new hotel in Świnoujście (2020, coast) and Accor is building a MGallery in Jurata (coast).

Boom in the Polish hotel market

Within next year we are expecting a rapid growth in the number of new hotel projects – also chain hotels. Accor alone is planning to open 17 new hotels in Poland within next couple of years.

The biggest growth in the number of new hotels coming to the market will be visible in major Polish cities. Based on initial announcements, by 2021 over 21 new hotels will open in Warsaw, creating a new supply of 4,400 hotel rooms (30% of current room supply). It is a similar situation in Tricity (Gdansk, Gdynia and Sopot) where within the next 3 years, nine hotels will open, creating a new supply of over 1,900 hotel rooms which makes up 30% of current supply.

It has already been announced that a number of new hotel brands will appear in Poland for example: Marriott International has already announced new hotels under brands like Residence Inn, Four Points by Sheraton or Autograph Collection, Louvre Hotel Group announce Royal Tulip brand, InterContinental will open Crown Plaza, Leonardo Hotels will open new NYX Hotel and Radisson will open Radisson RED. Moreover new chains like Motel One or Nobu Hotel will enter the Polish market and numerous hotel chains such as Barcelo, Zoku, Selena, Arcotel are working on the announcement of new projects.

Buoyant investment market

With recent yield compression, conservative investors are more inclined to move to alternative asset classes. This sentiment boosted investment within the hotel sector across the CEE with investors piling into some markets.

A gradual increase in ADRs and the top lines resulted in an increased interest in the Polish hotel market by Polish and foreign investors. The Polish Investment market started to be a destination for international instructional investors, although the interest is only for transactions involving large hotels with established brands located in the largest Polish cities.

Hotel properties contributed to a record volume over the last 2 years. The share in the total transaction activity increased rapidly in 2017, amounted to over 1 billion Euros and approximately a quarter of total annual volume. The most significant to be enumerated include: The Westin Hotel, Sheraton Grand, Gromada in Cracow, The Radisson BLU at Grzybowska and Warimpex portfolio acquired by a Thai investment vehicle. The recent prime asset acquisition includes Sheraton in Warsaw, which was sold to a UK-based investment fund.

A characteristic feature of the Polish market is an active role of the State Treasury in the hotel market selling unprofitable assets for redevelopment and preparing a visible market consolidation of public assets.

Throughout 2018, there were approximately 20 hotel transactions concluded in Poland. The overall investment volume halved in comparison to 2017, which was a result of the lack of investment product.

Hotel properties with secured long-term leases are the most sought after investment products. Although, there is materialized interest from opportunistic investment funds for acquiring hotels with management contracts.

Alternative development models

As a consequence of lack of investment products, there is a popular tendency for lease agreements offered by most hotel brands. Another apparent trend is the redevelopment of office and residential properties into hotels. In a buoyant market there is a visible model of building conversions or even changing building function before building completion, as was the case with the Ibis at Grzybowska Str. in Warsaw.

As the typical hotel products are lacking or seem overpriced, investors are looking into alternative acquisition models like buying receivables from the financial institutions with the aim to take-over distressed hotel assets. There are several assets on the market looking to be repositioned.

Yields and market indicators

A visible yield compression on the hotel market is a result of prime asset acquisitions, by worldwide funds, coupled with high demand from investment funds active in the Polish market. Initial yields on hotel transaction vary from just over 6% to 8.5% or even higher for properties in need of renovation and active asset management.

Direct transparent transaction yield data is lacking. There is a visible rising pattern of capital values within the hotel sector in the long-term, as reflected in the statistics. It seems to be confirmed by an overall investors' sentiment observed in the market. At the same time, a significant drop in secondary locations will be seen in the coming quarters.

A stable demand for trophy assets with stable income is observed, which coupled with limited supply has triggered a secondary market for hotel buildings, as displayed by the Sheraton Warsaw transaction.

A visible yield compression on the market is a result of prime assets acquisitions, secured by long-term leases, coupled with high demand from active investment funds.

At the same time, yields for prime properties just outside the western Polish border decreased from 5% to 3%. This fact, coupled with the rising wall of global capital chasing investment product added pressure on Polish cap rates. Branded hotels in Warsaw and Cracow with a volume comprising a minimum 120 keys are the most sought after product for global investors active within the CEE.
It can be concluded, that current capitalisation rates of hotel properties followed the pattern of prime properties representing other real estate asset classes like office and retail.

As some hotel owners seem to be testing the market with price tags based on record-low yields, there seems to be a decreasing interest from seasoned Polish-based investors for these assets. An lengthened exposition period for some properties might be a herald of a down-turning property cycle. Despite the fact that ADRs on some markets showed a downward trajectory, the capital values of hotel assets are considered to perform well within the next 3-years.

Authors

Dariusz Futoma
Managing Partner
Horwath HTL Poland
dfutoma@horwathhtl.com

Agata Przeniosło Drozd
Partner & Senior Consultant
Horwath HTL Poland
aprzenioslo-drozd@horwathhtl.com

Wojciech Doliński MRICS REV
Valuation Partner
Horwath HTL Poland
wdolinski@horwathhtl.com

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Horwath HTL Poland
Celebrating 10 years of business in Poland
Warsaw Wawer Przewodowa 42J
04 -874 Warsaw, Poland
Phone: +48 601 296 989