

Hong Kong Hotel Report

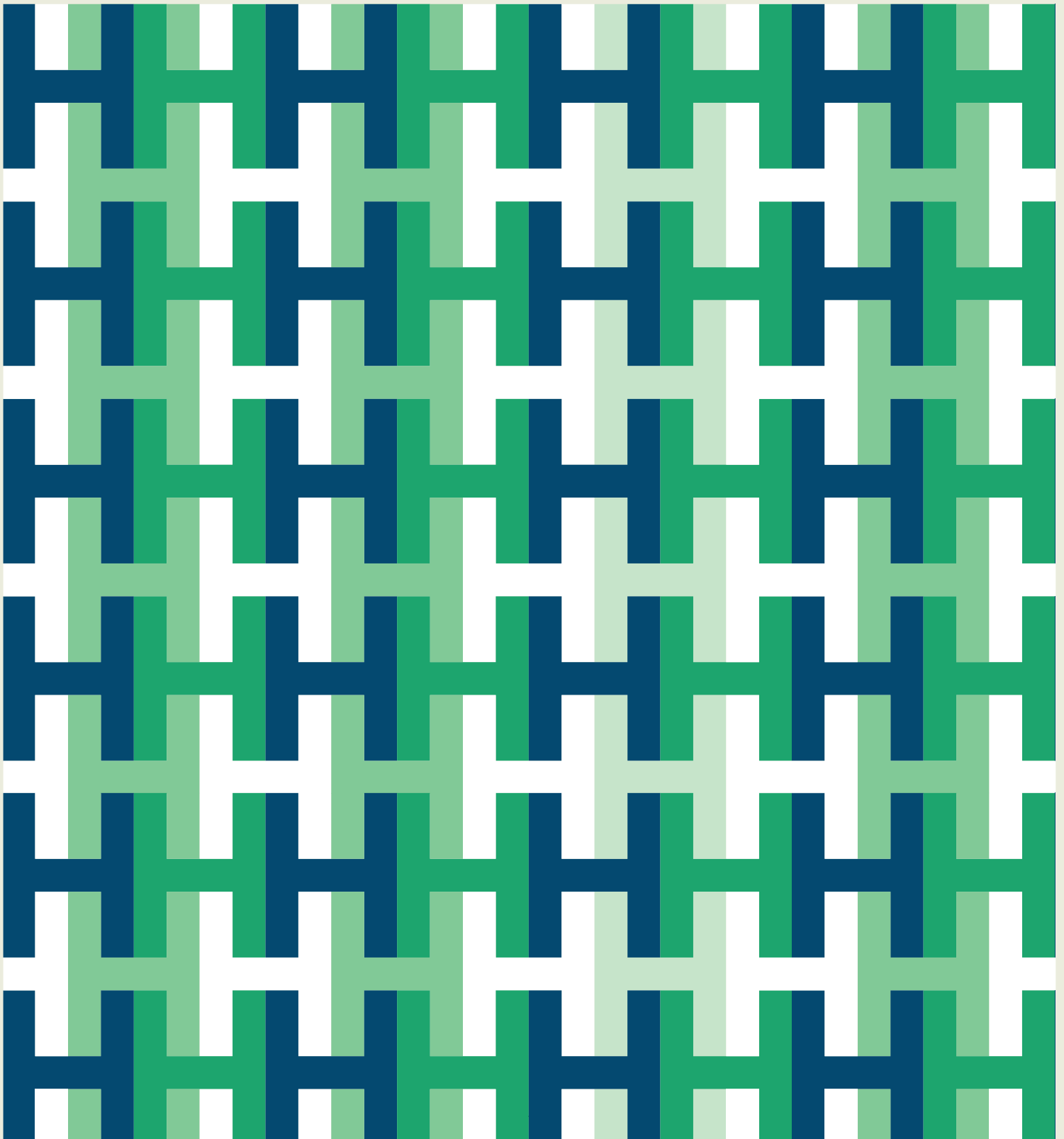


Navigating New Directions

February 2024

This report analyses the performance of Hong Kong's Hotel Market

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Introduction

2023 was a year of recovery, resiliency and growth for the Hong Kong hotel industry. Thanks to the full-border reopening in Hong Kong in early 2023, tourism gradually resumed. The hotel industry staged a visible recovery after the difficult years of the pandemic. In tandem with the influx of visitor arrivals, room and occupancy rates saw significant gains. Nevertheless, even though tourists returned, the recovery in tourist spending and the number of international visitors rebounded slower than expected. The hotel business in general did not fully return to that prior to the Hong Kong protests in 2019 and COVID-19 from 2020 to 2022.

During the pandemic, the hospitality sector corrected appreciably and attracted huge interest from value-added investors in converting these premises into other uses, such as co-living or long-stay accommodation. In 2023, however, investment activity in the local hotel sector became subdued amid the high interest rate environment and prevailing global economic uncertainty.

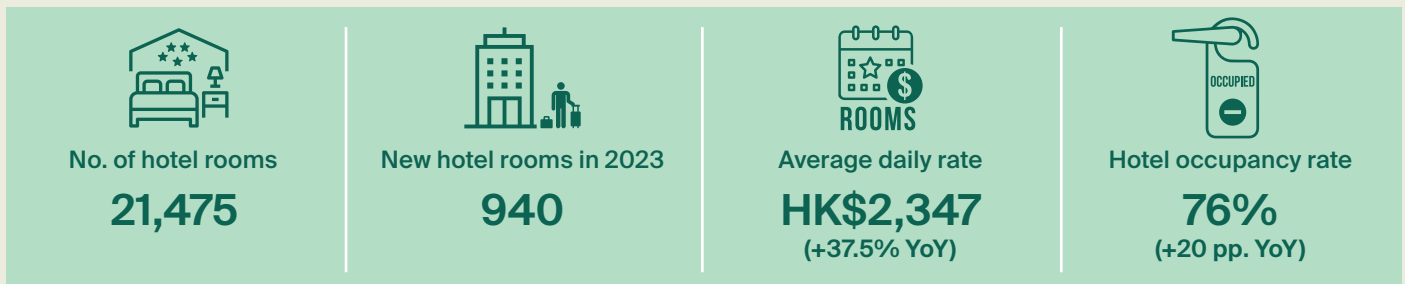
In this report, we look at the performance of hotels in Hong Kong, key trends in the hotel sector, demand and supply, and the industry's outlook and opportunities.

“As the Hong Kong hotel market has been transforming in the past 10 years, hotel operators have readjusted their strategy and always attempt to diversify their revenue sources. On the other hand, investors are acquiring hotels to unleash their asset repurposing potential, primarily converting hotels into student accommodations. This trend is expected to continue in the next 12 months amid high interest rate environment.”



Martin Wong
Director, Head of Research
& Consultancy, Greater China

Five-star hotel key indicators*



*As of December 2023

Key takeaways

1. Hong Kong's hotel sector is on a recovery trajectory, with rising occupancy and average daily rates (ADR) since full border reopening.
2. Inbound tourist numbers and spending are recovering and are generally favourable; hotel business has still not fully recovered; it has improved, but is still well below the pre-pandemic level.
3. Five-star hotels, which are in the High Tariff A hotel segment, outperformed the overall market with higher revenue per available room (RevPAR) and stronger year-on-year (YoY) growth in the performance indicators. This was mainly because of the better marketing promotions of five-star hotels. Additionally, the poorly performed Medium Tariff Hotels create stress and the drop in values make good targets for hotel conversion to occur.
4. Investment sentiment in the hotel sector was dampened in 2023 with plunging transaction volume and limited market activity due primarily to interest rate hikes and the gloomy economic outlook.
5. Despite weakened investment sentiment, the hotel conversion trend continued, as investors seized the opportunity to convert existing Medium Tariff hotels or hotels under stress into youth hostels in response to growing number of Chinese Mainland and overseas students.
6. Looking ahead, we expect the sector to recovery, with more favourable demand-supply dynamics. Market momentum will be driven by improving inbound tourism, including leisure and Meetings, Incentives, Conferencing and Exhibitions (MICE) visitors.
7. On the investment front, we expect hotel transactions for asset repurposing to remain a key investment theme in the near-term. Medium Tariff Hotels transactions to remain active for largely discounted capital value of hotel assets and strong fundamental demand from overseas students and non-local professionals.

Tourism statistics

Hong Kong's tourism sector has shown signs of revival since the border reopened, with more bookings for hotel rooms, and increased footfall in retail shops and attractions. The total number of visitors reached 33,999,660 in 2023, up 5,523.8% YoY. Overnight visitor arrivals in Hong Kong bounced back to 17,159,320 up 2,922.2% YoY. About 72% of the visitors were from the Chinese Mainland, 53.7% of whom were same-day visitors and 46.3% of whom were overnight visitors.

According to the Airport Authority Hong Kong (AAHK), Hong Kong International Airport (HKIA) handled 39.5 million passengers in full year 2023, increasing by 7 times YoY. All passenger segments experienced substantial YoY growth. Traffic to and from Southeast Asia, Chinese Mainland and Japan saw the largest growth.

However, the number of inbound visitors, especially international tourists, was still far below the pre-pandemic level. The strong HKD reduced the desire of foreign travellers to visit Hong Kong. The number of international tourists reached 7,239,207 in 2023, up 3,055.2% YoY. But the number

of arrivals was still far from the pre-pandemic level of 14,109,325. The total number of visitors recovered to about 51% of the pre-pandemic level, and passenger traffic at HKIA recovered to about 53%.



Performance overview

Given the steady return of Chinese Mainland tourists and the modest growth in international arrivals, hotel performance has been recovering and reported a strong YoY increase in occupancy and average room rates. The occupancy rate in 2023 increased by 20 percentage points YoY to 76% for High Tariff A hotels and increased 12 percentage points YoY to 84% for High Tariff B hotels. The occupancy rate for Medium Tariff hotels increased 18 percentage points to 84%.

In terms of average daily rate (ADR), High Tariff A hotels room rates outperformed, with their ADR rising vastly since the border reopening. The ADR of High Tariff A hotels in 2023 was HK\$2,347, soaring 37.5% YoY, and the ADR of High Tariff B and Medium Tariff hotels increased 33.3% and 9.9% YoY, respectively, to HK\$1,098 and HK\$730. The stronger rebound in High Tariff A hotel room rates suggests that international luxury hotel brands were more successful with their attractive online marketing campaigns on social media and in distribution channels.

Revenue per available room (RevPAR) of High Tariff A hotels showed the strongest revival of all segments, reaching \$2,257 in December 2023, for a 103% YoY increase and 126% higher than in December 2019, indicating the performance of the High Tariff hotel segment has rebounded to the pre-pandemic level. In contrast, Medium Tariff hotels underperformed, as demand for quarantine hotels ended in the post-pandemic period.

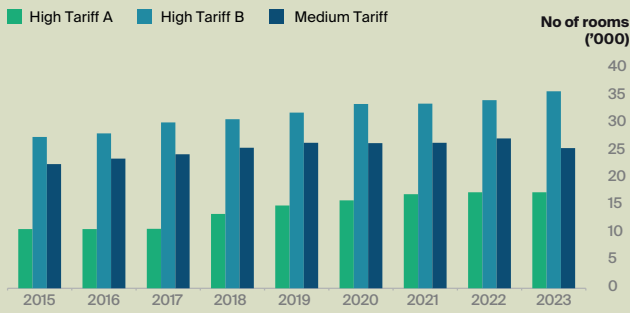
Table 1: Key performance indicators of 5-star hotels in 2019-2023

	New supply of 5-star hotel rooms	Average daily rate of 5-star hotel rooms	Hotel occupancy rate in of 5-star hotel rooms
2023	940	HK\$2,347 (+37.5% YoY)	76% (+20 pp. YoY)
2022	804	HK\$1,707	56%
2019	1,574	HK\$1,982	74%

Source: Hong Kong Tourism Board / Knight Frank Research

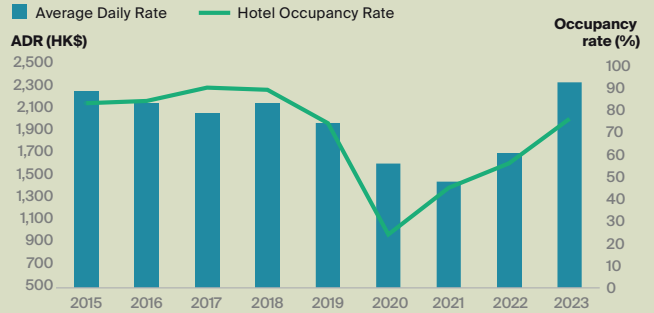


Chart 2 : Hong Kong hotel stock by category



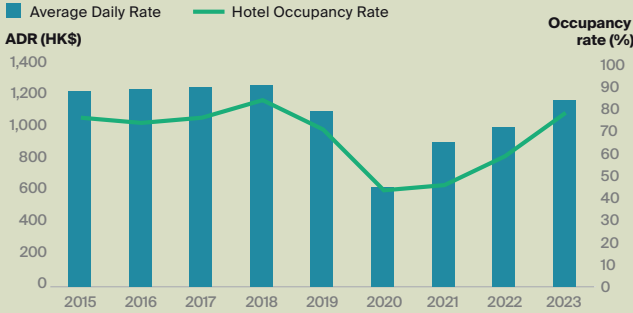
Source: Hong Kong Tourism Board / Knight Frank Research

Chart 3 : Hong Kong's High Tariff A hotel performance



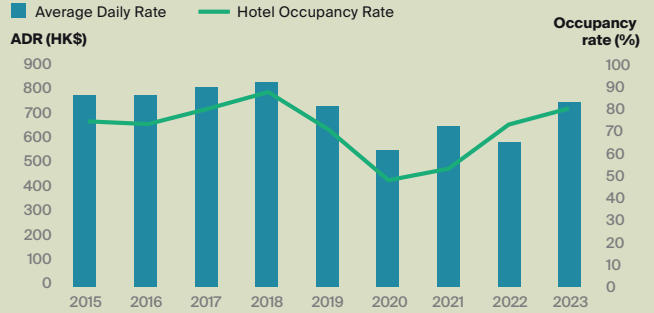
Source: Hong Kong Tourism Board / Knight Frank Research

Chart 4 : Hong Kong's High Tariff B hotel performance



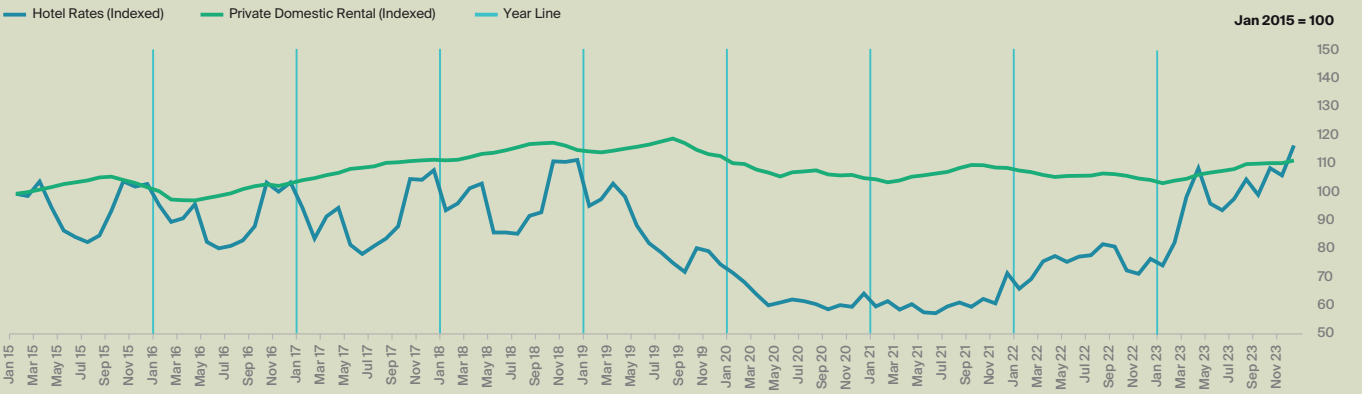
Source: Hong Kong Tourism Board / Knight Frank Research

Chart 5 : Hong Kong's Medium Tariff hotel performance



Source: Hong Kong Tourism Board / Knight Frank Research

Chart 6 : Rental rates of hotels and private domestic housing



Source: RVD / Knight Frank Research

Hotel performance drivers

Two hotels in Hong Kong made it to the top five of the World's 50 Best Hotels Award: Rosewood Hong Kong was ranked second, and The Upper House was ranked fourth. This international recognition is testament to the two hotels' outstanding hospitality service and world-class facilities.

In fact, the increasing spending of locals and tourists on fine dining restaurants and award-winning bars in hotels contributed to the higher non-room revenue in the post-pandemic era. The proportion of non-room revenue for hotels achieved ADR of HKD\$2,351 and above, which accounted for 53% of total revenue in 2019, according to the Hong Kong Hotel Industry Summary review, increased

to 60% in 2022. The spending behaviour of MICE visitors and high spenders shifted after the pandemic, so non-room service items are highly valued by hotel operators.

Food and beverage revenue for hotel operators has become increasingly important since the end of the pandemic. High Tariff A hotels, for example, are keen to collaborate with famous brands across sectors to offer a unique experience for guests. For instance, The Peninsula Hong Kong collaborated with Hong Kong's iconic Star Ferry to offer afternoon tea and sunset cocktail cruises. In other efforts to drive food and beverage revenue, the hotel also partnered with Le French May to host exclusive concerts and dinners.

Hotel supply

The recent hotel supply pipeline has been limited, as operators remained cautious over the past three years amid the economic uncertainty. New supply includes Hotel Ease Access Lai Chi Kok (119 rooms), Le Meridien Hong Kong, at Cyberport (170 rooms), and Regent Hong Kong, in Tsim Sha Tsui (497 rooms). The latter two stopped operations during the pandemic to undertake extensive renovations. In addition, Mondrian Hong Kong (324 rooms), of Accor Group, opened in Tsim Sha Tsui in December 2023. This is a five-star hotel with Victoria Harbour views and a globally acclaimed restaurant and bar on the top floor.

In 2024, four medium-scale hotel projects are scheduled to open: the Metropark Hotel Hong Kong, in Hung Hom, the Dorsett Hotel, in Kai Tak, the Kimpton, in Tsim Sha Tsui, and the Hilton, in Sheung Wan. As Tsim Sha Tsui is a must-visit destination for visitors and a shopping hub with attractive arts and cultural offerings, hotel demand in the area remained high. With the two newly opened five-star hotels and an upcoming luxury boutique hotel, the district is poised to welcome another 1,313 new rooms in 2023-2024.

Dorsett will open its 373-room flagship hotel in Kai Tak in August 2024, adjacent to Kai Tak Sports Park, which is expected to be opened by the end of 2024. The new hotel is expected to cater for longer-staying business travellers, visitors attracted by major sports events and concerts in Hong Kong, and guests arriving from the nearby cruise terminal.

Table 2: List of new hotels* that were opened in 2022-2023

Quarter Opened	Districts	Name of Hotel	No. of Rooms
Q1 2022	Chek Lap Kok	Regala Skycity Hotel	1,208
Q1 2022	Tai Kok Tsui	Starphire Hotel	154
Q1 2022	Sheung Wan	Lander Grand Hotel	51
Q2 2022	Wan Chai	China Rich Hotel	78
Q2 2022	Wan Chai	J Link Hotel	80
Q2 2022	Tung Chung	The Silveri Hong Kong-MGGallery	206
Q3 2022	Wong Chuk Hang	The Fullerton Ocean Park	425
Q3 2022	Wan Chai	Aki Hong Kong-MGGallery	173
Q4 2022	Central & Western	Y Hotel Hong Kong	96
Q4 2022	Wan Chai	Ying'nFlo, Hong Kong, Wan Chai	70
Q4 2022	Cyberport	Le Meridien Hong Kong	170
Q2 2023	Lai Chi Kok	Hotel Ease Access Lai Chi Kok	119
Q3 2023	Admiralty	Ying'nFlo, Wesley Admiralty	251
Q4 2023	Tsim Sha Tsui	Regent Hong Kong	497
Q4 2023	Tsim Sha Tsui	Mondrian Hong Kong, 8A Hart Avenue	324

*Excluded serviced apartment

Sources: Knight Frank Research

Table 3: New confirmed hotel projects in 2024

Planned Date of Completion	Districts	Property	Developer	No. of Rooms
Q3 2024	Kai Tak	Dorsett Kai Tak, Shing Kai Road	Far East Consortium International Limited	373
Q3 2024	Tsim Sha Tsui	Kimpton Hong Kong, 11 Middle Road	Empire Group	492
Q4 2024	Sheung Wan	Motto by Hilton Hong Kong Soho, 83 Jervois Street	Yau Lee Holdings Limited	274
Q4 2024	Hung Hom	Metropark Hotel Hong Kong, 1 Cheong Tung Road	China Travel Service Property Investment HK Limited	536

Source: Knight Frank Research / Market news

Hotel investment landscape

Investment sentiment hammered by high interest rates

Higher interest rates, resulting in the higher cost of funds, became an obstacle for investors in making investment decisions. As the U.S. Federal Reserve continued to raise the interest rate and the HKMA raised the base rate to 5.75% in July 2023, banks in Hong Kong raised the cap for the HIBOR-based rate (prime rate) accordingly to 5.875% to 6.125%. The higher cost of lending dampened investment sentiment, as investors took a wait-and-see approach to avoid taking risks amid the economic uncertainty.

In 2023, there were four en-bloc hotel transactions over HK\$100 million, totally HK\$6.8 billion, up 9.2% YoY. Hotel transactions contributed 17% of total commercial volume, only 1 percentage point to retail volumes. Despite the weak market sentiment, the figures show higher resilience in the hotel investment market compared to other commercial segments, but we believe that high financing costs were the main reason for reduced market movement.

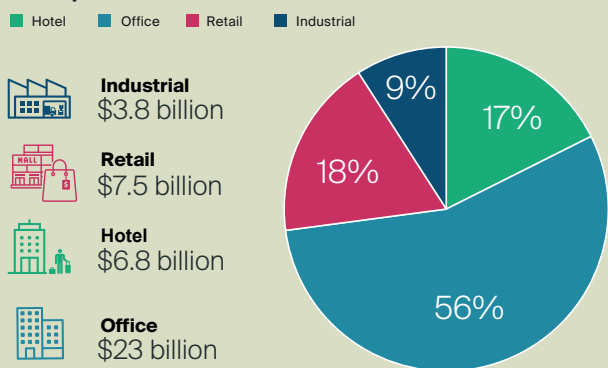
Table 4: En-bloc hotel transactions in 2023 (>HK\$100 million)

Transaction Date	Property Name	District	No. of Rooms	Consideration (HK\$ million)	Price Per Key (HK\$ million)	Seller	Buyer
Oct 23	De Fenwick*	Wan Chai	54	898	16.6	Leung Tat-bor and related party	CTG Hotel
Jun 23	Butterfly on Victoria	Causeway Bay	132	469	3.5	Eric Chu Nap-kee	K. Wah International
Apr 23	Pentahotel Hong Kong Kowloon	San Po Kong	695	2,000	2.9	New World Development	Angelo Gordon & Co., Wang On
Mar 23	The Kimberley Hotel	Tsim Sha Tsui	546	3,400	6.4	China Cinda Asset Management	China Tourism Group

*Serviced apartment

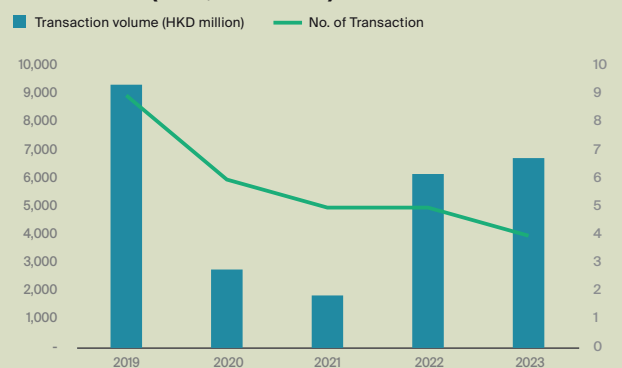
Source: Knight Frank Research

Chart 7: Commercial property transactions in the past 12 months



Source: Knight Frank Research

Chart 8: Hong Kong Hotel Investment Trend 2019 to 2023 (>HK\$100 million)



Source: Knight Frank Research

Hotel conversion to alternative accommodations a spotlight

With the significant growth in the number of non-local students and reliable rental income flow even in the stronger market, student accommodation has numerous enticing prospects. In recent years, we witnessed the prevailing trend of hotel conversions into student residences, as they provide lucrative returns for investors. In 2022-23, 102,542 students enrolled in University Grants Committee (UGC)-funded programmes, 21,709 (21.2%) of whom were non-local students. The percentage of non-local students increased by 4.7 percentage points over the past six years, and this is expected to soon almost double to 40%, as the government announced in the 2023-24 Policy Address. With the rising trend of non-local students enrolling in UGC-funded programmes, there is strong demand for university student accommodation.

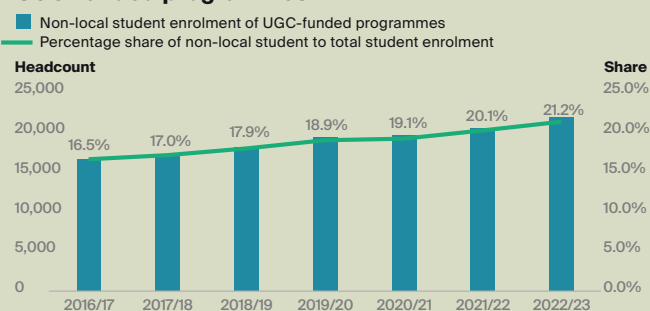
Investors have spotted opportunities in acquiring Medium Tariff hotels or stressed assets with reasonable prices for conversion, as they are often sold at a lower price than en-bloc residential buildings. Some hotels have been converted into student residences or youth hostels, given the inadequate supply of student accommodation offered by universities. Converting hotels into student residences is relatively straightforward and efficient, as the existing layout already has individual rooms and common areas. Hence, investors have been actively eyeing this low CapEx, high-return business opportunity.

One example is Y83, in Hung Hom, operated by Crystal Group. The building was previously Hotel Sav (388 rooms), owned by Chuang's Group. It was sold for HK\$1.65 billion

(HK\$4.26 million per key) to AEW Capital Management in March 2022. With a capacity to house almost 600 students, Y83 provides 20,000 sq ft of communal space, including a cafeteria, common rooms, collab spaces, a gym, an activity studio and pantries, with newly fitted rooms and furniture. Crystal Group also operates student accommodation in Jordan and Western district. Even though the rooms are leased with a rental premium compared to nearby studio units for lease, the property is fully occupied at present.

Another recent example is PentaHotel, in San Po Kong, which was owned by New World Development. It was sold to Wang On Group and Angelo Gordon & Co. for HK\$2 billion (HK\$2.88 million per key) in April 2023. Wang On Group announced in June 2023 that the Group planned to convert the property into a student residence with about 720 rooms.

Chart 9: Non-local student enrolment of UGC-funded programmes



Source: Census and Statistics Department / Knight Frank Research

Outlook

Given the gradual recovery in visitor numbers and limited new supply of five-star hotels in the coming year, we expect the occupancy level and hotel ADR to continue to pick up in the near term. With limited upcoming hotel supply in the pipeline, market demand should be able to absorb the new supply, especially in major tourist districts. High Tariff A hotels are expected to continue to outperform, as operators strive to differentiate themselves through the provision of high-quality services and amenities, along with effective marketing campaigns. Therefore, revenue per available room (RevPAR) should continue on the upswing in 2024, continuing to surpass the 2019 level and potentially rebounding back to the 2018 level.

Inbound tourism looks set to continue to increase in 2024, as planned infrastructure and new tourist attractions, such as Kai Tak Sports Park, The East Kowloon Cultural Centre and SKYCITY, are expected to support the growth of the hotel sector in the future. In addition to an annual mega tourism campaign set to be organised by the Hong Kong Tourism Board, with events such as 'Arts in Hong Kong' and Hong Kong Harbour Fiesta, city happenings, like the Rugby Sevens and the Hong Kong Marathon, will continue to attract overseas leisure visitors. We believe Hong Kong

should focus on spurring the recovery of people who prefer to stay overnight, particularly business travellers, as well as MICE and long-haul travellers, given their stronger spending power. The Hong Kong Tourism Board has attracted over 30 major B2B conventions for the next few years, which are expected to attract over 300,000 participants, including the WOW (World of Web 3) Summit and Fortune Innovation Forum.

In the hotel investment market, High Tariff A and B Hotels continue to outperform the Medium Tariff hotels. Medium Tariff Hotels will be under pressured and they make good targets for student conversions. However, investment sentiment should remain conservative, with subdued transaction volume in H1 2024 amid the high interest rate environment and external economic challenges. Recent statistics show that the U.S. inflation rate slowed down significantly, and the labour market cooled down, so interest rates should be near their peak. The Fed indicated that rates should decline thrice in 2024. Thereby, we expect to see more Medium Tariff Hotels transactions latter in the year and more hotel conversion activities to accommodate the influx of newcomers.

We like questions. If you've got one about our research, or would like some property advice, we'd love to hear from you.

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