

MALAYSIA
HOSPITALITY
INVESTMENT
INTENTIONS
SURVEY
2020

Introduction

No one could have predicted the sheer pace and speed with which COVID-19 gripped the world and the impact that this has subsequently had on the hotel sector in 2020.

Knight **Frank's** Malaysian Hospitality Investment Intentions Survey analysed the investment perspectives of hotel owners, operators and owner operators and the study provides an insight of how they have been impacted by COVID-19 in Malaysia, what is the level of investment demand, investor preferences and what measures could help to provide some relief during this very challenging time.

The research was conducted in November 2020 to try to capture the full scale and impact of the COVID-19 crisis.

“

Billions of dollars have been spent by governments, multilateral agencies and private businesses around the world which has resulted in more than half a dozen effective vaccines being developed and approved for use. In addition there are another 150 potential vaccines in preclinical development and we are now seeing the most massive global vaccination effort in a century. There is hope that international travel can resume soon, but exactly when is the million dollar question. For shrewd hotel investors with strong balance sheets, we believe there is an excellent window of opportunity over the next 12 – 24 months to acquire prime hotel assets in Malaysia.

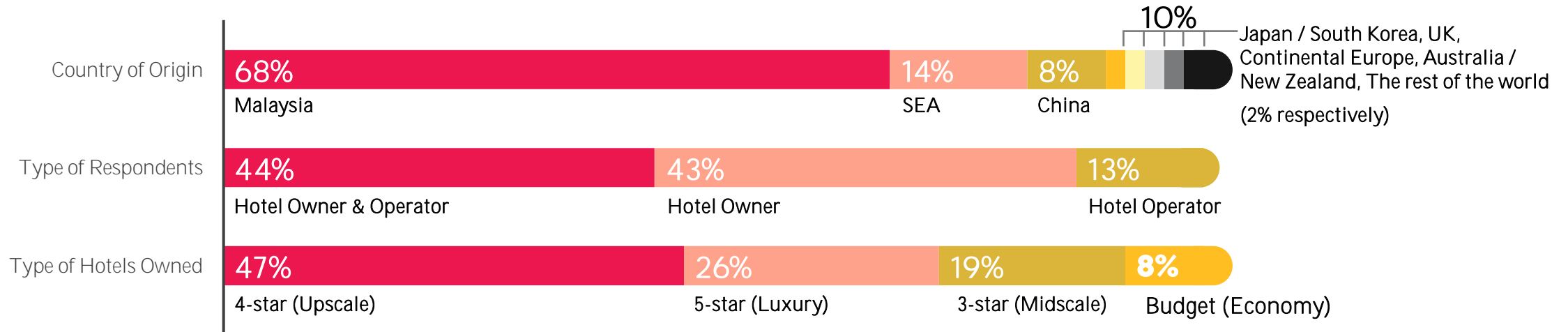
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*James Buckley,
Capital Markets, Executive Director,
Knight Frank Malaysia*



Who Responded to the Survey?

Respondents' profile



The majority of the respondents were from Malaysia. 14% were from other Southeast Asian countries and the remainder were from the rest of world.

Approximately 44% were owner operators, 43% hotel owners and 13% operators. Over 72% of the respondents had already invested in the hotel sector in Malaysia.

Majority of the respondents own / manage upscale and luxury hotels. Overall, close to half of them (approx. 47%) own or manage 4-star hotels in Malaysia whereas, the remaining half primarily consists of 5-star (approx. 26%) and 3-star hotels (approx. 19%), with just a few who run budget hotels.



The Current Hotel Investment Sentiment

Will you or your company be making a purchase / investment into a hotel?

Yes, within the next 6 months to 1 year

16%

Yes, within the next 1 year to 2 years

14%

Maybe, still contemplating

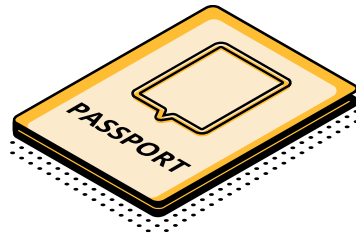
20%

No, looking to dispose

7%

No, not at the moment

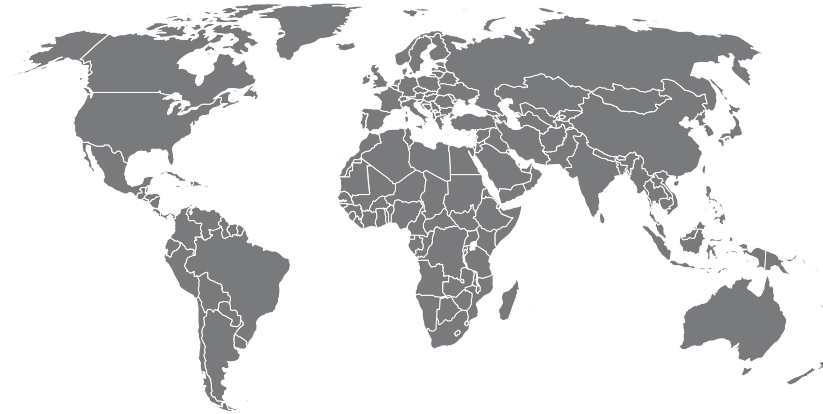
43%



Although the pandemic is causing a global recession and hitting the travel and hospitality sector particularly hard, 14% of the respondents are anticipated to buy hotel assets within the next two years, with 16% looking to make an acquisition even sooner within the next 6 months. We expect these respondents to seek opportunities created by the market volatility and are bullish in looking for undervalued hotels.

In contrast, approximately 43% of the respondents decided not to venture into hotel purchase / investment currently.

Ranking of countries / regions by preference for setting up a hotel operation or investing into a hotel



- | | | | |
|-----|---------------------|-----|-------------------------|
| 1st | Southeast Asia | 5th | Australia / New Zealand |
| 2nd | Japan / South Korea | 6th | Continental Europe |
| 3rd | UK | 7th | Middle East |
| 4th | China | 8th | The Rest of the World |

Investor preference of hotel operation / investment in Southeast Asia is significant with approximately 83% of the respondents ranking the region as the most preferred compared to others. Meanwhile, there is also notable interest in Japan / South Korea with the region ranked 2nd with 69% of the responses, followed closely by the UK at 3rd position with 68% of the responses.

The Attractiveness & Criteria

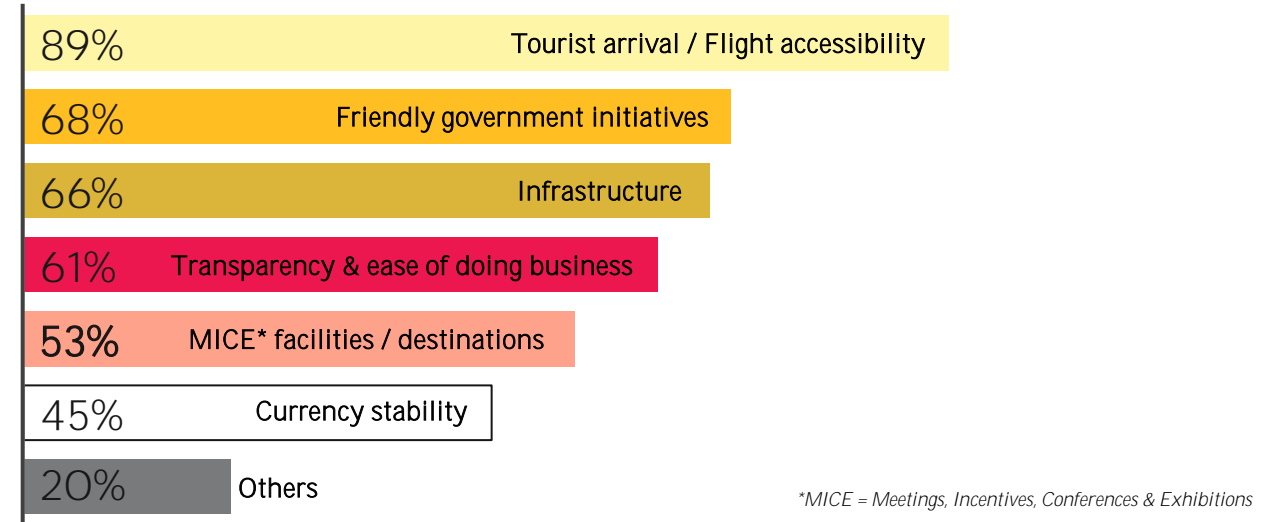
Ranking of Southeast Asian countries by its attractiveness for hotel investment



Zooming closer into the most preferred Southeast Asian region, Malaysia is ranked within the top 3 most attractive countries for hotel investment. Known for its diverse tourist destinations and affordable food & lodging, Thailand has ranked no. 1 in terms of tourist arrival numbers among the ASEAN countries since 2016 as reported by Tourism Malaysia in 2020.

A thriving global financial hub, Singapore is ranked second. The bustling economy of the Asian Tiger makes it attractive for hotel investments.

Ranking of decision making criteria in setting up a hotel operation or invest into the region / country



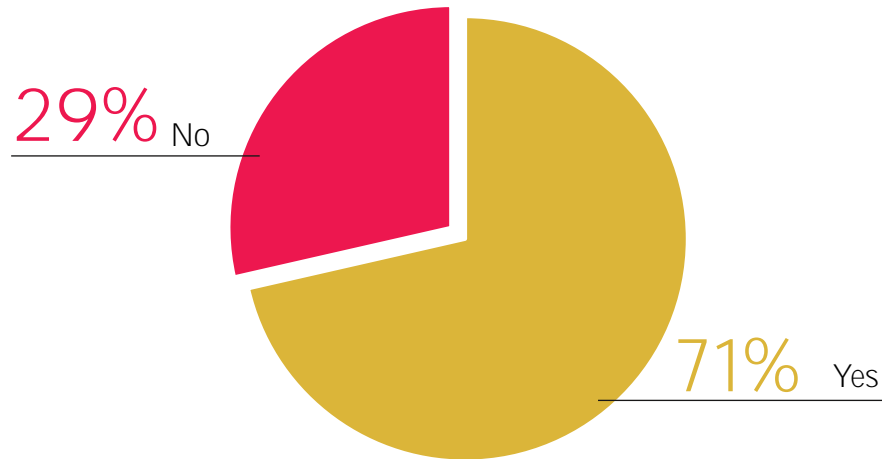
Hotel operation / investment decisions into a specific region or country are largely driven by several key criteria.

The survey results indicated that Tourist Arrival / Flight Accessibility is the most important consideration with 89% of respondents selecting this criteria as the most crucial in their investment decision making process.

Ranked second, Friendly Government Initiatives is also significant in motivating hotel operation / investment as it provides cushion and incentives to hotel businesses in mitigating the impact of the current market sentiment. Almost as important as government initiatives is infrastructure readiness which plays a pivotal role in attracting tourists.

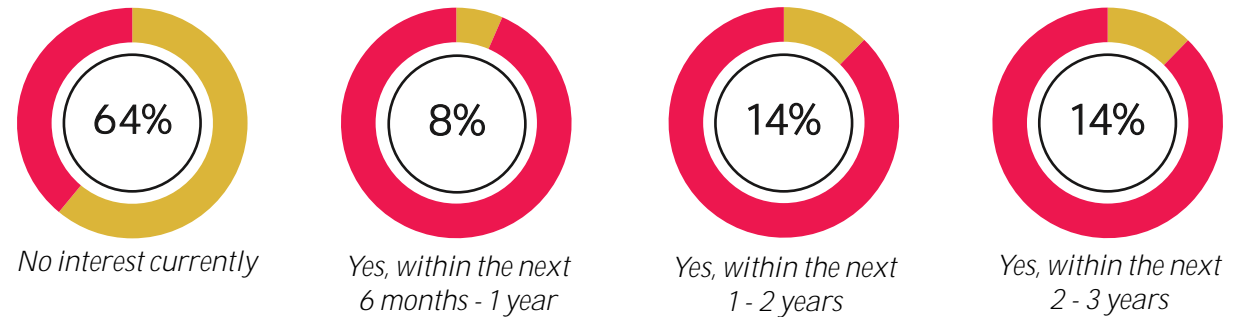
Hotel Investment Strategy in Malaysia

Proportion of investors considering to invest or have already invested into the Malaysian hospitality sector



Overall, more than 2/3 of the respondents indicated that they have already invested or are considering to invest into the Malaysian Hospitality sector. Out of the respondents that answered “Yes”, 70% had expressed interest to acquire hotels in Malaysia in the next 6 months to 2 years. It is clear that there is still significant interest in hospitality investments in Malaysia.

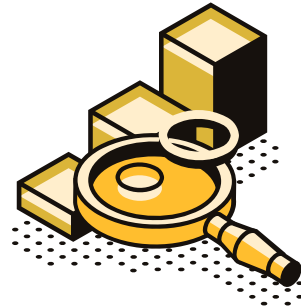
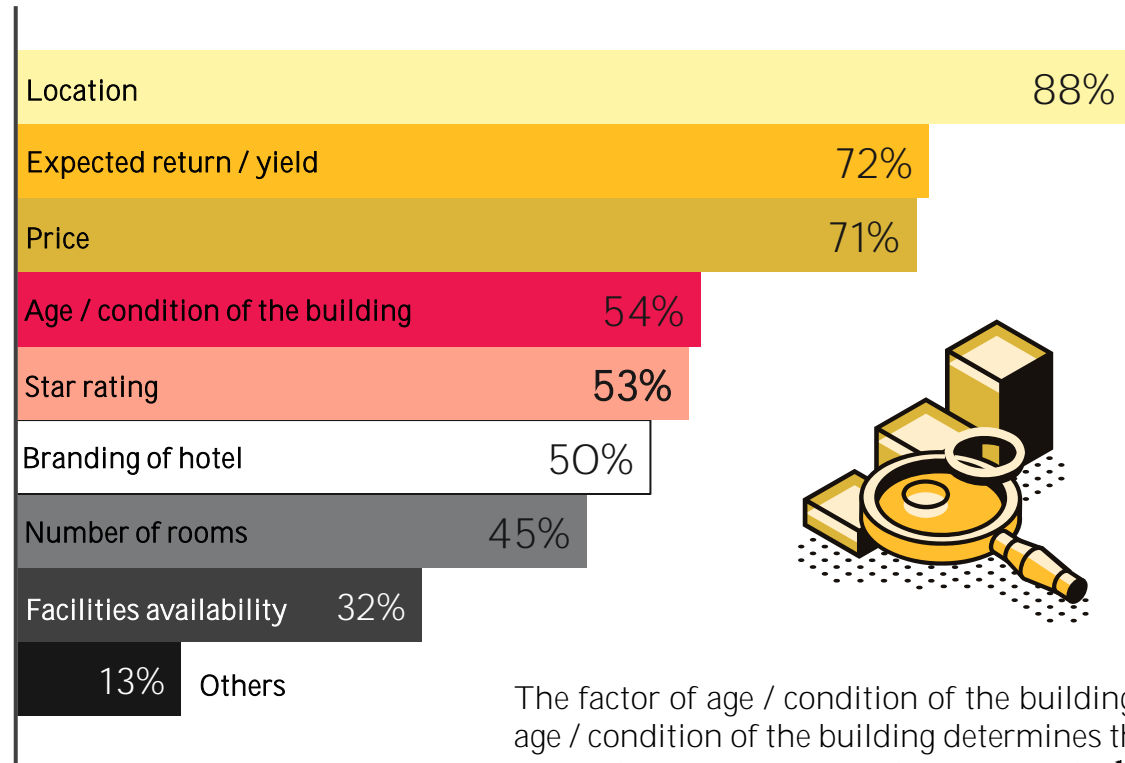
Would you consider increasing your exposure to the Malaysian hotel sector?



Every investor reacts differently to market conditions. Some are very shrewd and are confident in their ability to price hotels correctly. Others may have very little tolerance for risk and are not so comfortable with investing and tend to wait until market activity picks up. Our respondents to this question indicate that about 64% do not have appetite to increase their exposure to hotels whereas 21% are looking to acquire in the next two years (8% in the next 6 months).

Key Factors – Investment in Malaysian Hotels

Ranking of factors in hotel investment decision



Location

The location of the hotel was considered to be the most important factor by investors when buying a hotel. They understand that the hotel performance is driven by guests selecting to stay at a hotel which best caters for their needs and some value location above everything else and are willing to pay that little bit extra.



Return & Price

Investors also consider the expected net return / yield to also be very important and some vendors often price their hotels based off a price per key when in fact, the price of the hotel is driven by its underlying performance.

The factor of age / condition of the building, star rating, and hotel branding were considered equally important to investors. The age / condition of the building determines the amount of CAPEX needed to be invested whilst the hotel branding and star rating is one of the major factors in determining the **hotel's** potential revenue.

Other factors that were mentioned by respondents were the type and number of competitors within a 3km radius, the current operator and the remaining term of the hotel operating agreement. The availability of local skilled and non-skilled manpower was also noted as an important consideration.

Hotel Investment Preferences in Malaysia



Preferred type of hotels

- 57% Business & Conference Hotels / City Hotels
- 23% Resorts (Beach / Highland)
- 14% Boutique Hotels
- 4% Budget Hotels
- 2% Spa & Wellness

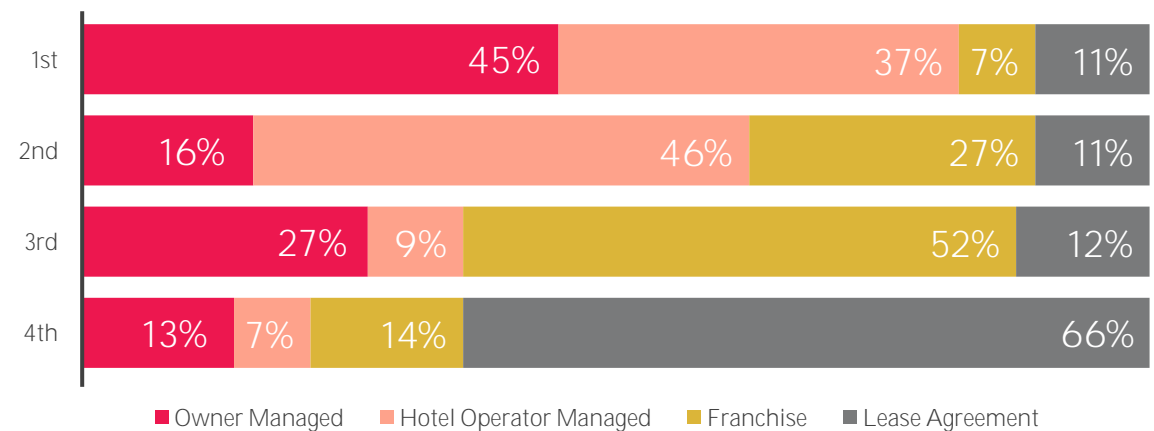
According to the survey results, the graph on the right shows that the most preferred hotel operation of choice is Owner Managed which is recognized by approximately 45% of the respondents. This might be driven by the freedom to make all decisions, taking full control over the hotel operational structure, growth and costs.

The 2nd most preferred choice is Hotel Operator Managed which was chosen by approximately 46% of respondents. The benefits of working with an international hotel operator are the access to the global marketing network and brand loyalty programme. Franchise and Lease Agreement is considered for 3rd and 4th choice respectively.

Business & Conference Hotels / City Hotels remained the most popular hotel type investment. It is the first choice of 57% of respondents as it is known to be highly profitable where the main client segment is business travellers. As most business travellers tend to stay during the week, it helps a hotel to reach higher occupancy on weekdays when the leisure segment is absent and is less reliant on holiday seasons. Kuala Lumpur is a popular destination for international tourists who stop over in the city before continuing their journey to other parts of the country or other Asian destinations.

As Malaysia is well known for its beautiful beaches and lush highlands, 23% prefers Resorts over the rest of the hotel types. Approximately 14% of respondents expressed preference for Boutique Hotels, followed by 4% for Budget Hotels. Spa & Wellness was the least preferred with only 2%.

What is the preferred choice of hotel operation?



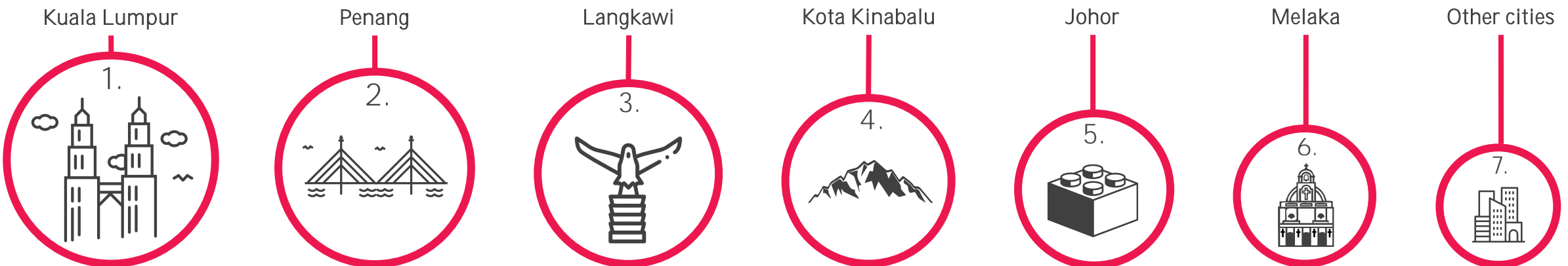
Preferred Location

Which cities in Malaysia are most attractive for hotel investment?

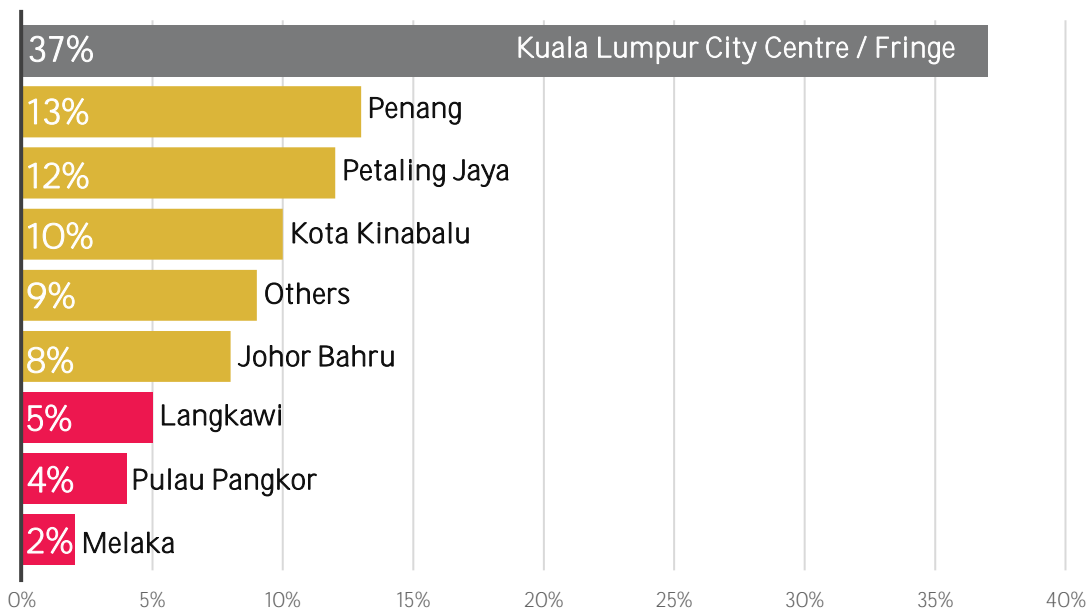
With the best international flight connectivity and being the capital city of Malaysia, 71% of respondents chose Kuala Lumpur as their no. 1 choice for hotel investment. Passenger traffic to Kuala Lumpur International Airport far exceeds any other airport in Malaysia and the ability to attract more business travellers as well as tourists makes Kuala Lumpur the most attractive city for the majority of the respondents.

Penang was the second most popular choice for hotel investment with 63%, with places like Batu Ferringhi and George Town being popular destinations for both international and domestic holiday makers.

Langkawi, an island with outstanding natural beauty placed third, surprisingly ahead of Kota Kinabalu which has the second highest passenger arrival numbers in Malaysia and is also a popular eco-tourism spot.



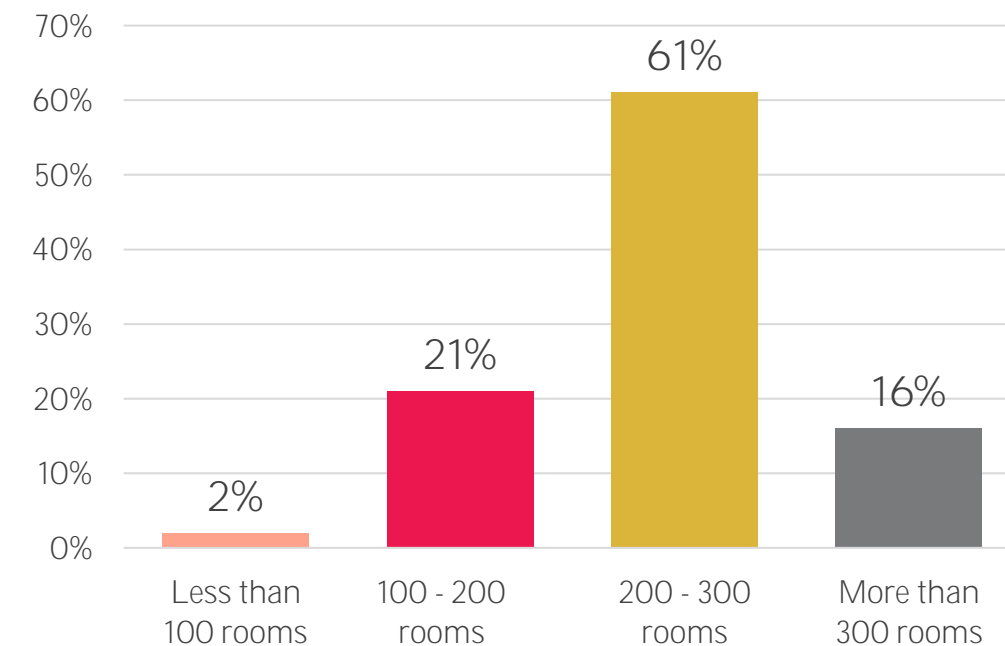
Existing / Preferred location for future hotels



The graph above shows the preferred locations of the **respondents'** existing or future hotel investments in Malaysia. Majority of them prefer to own or acquire hotels located in KL City Centre / KL Fringe as compared to the other states in Malaysia. The split between hotels located in Petaling Jaya, Penang, Kota Kinabalu and Others (Perak, Kuantan & Genting Highlands) are relatively even, whereas the least preferred locations are Johor Bahru, Langkawi, Pulau Pangkor and Melaka.

The control of cost and economies of scale is very important in the hospitality sector. The majority (approximately 61%) of the respondents expressed that the ideal size of a 4 to 5 star hotel / resort should be 200 - 300 rooms in total.

Ideal size (room numbers) of a 4 or 5-star hotel / resort

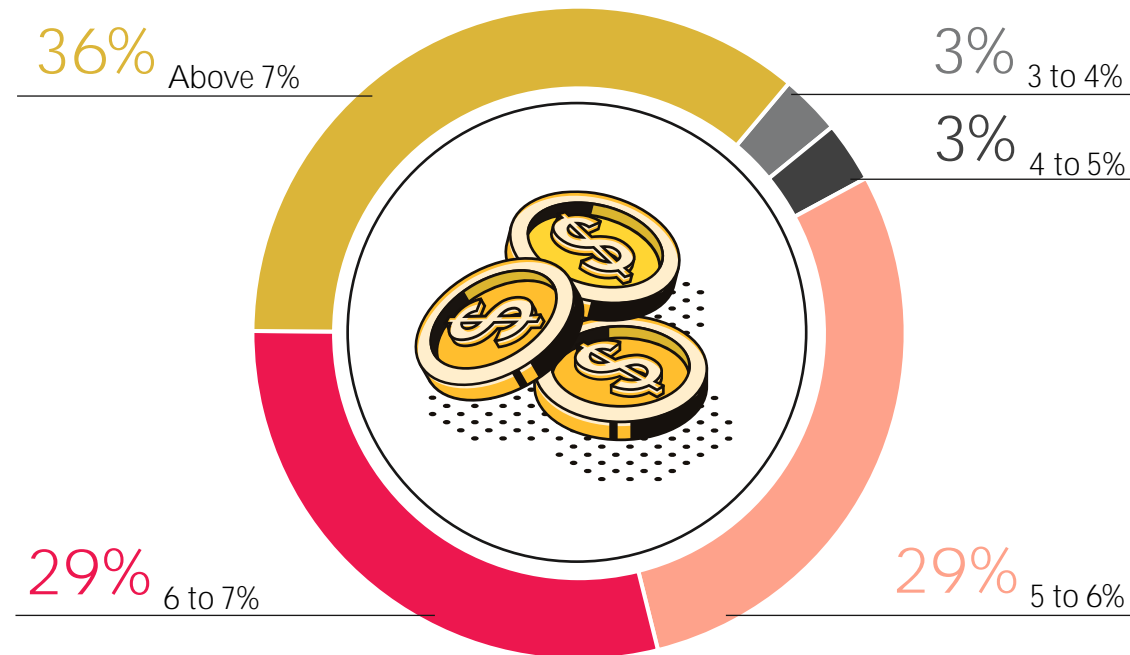


Investment Expectations

Average overall net return / net yield expected for a 4 to 5-star hotel in Malaysia

Hotel sales volumes are principally influenced by availability of capital and the overall performance of the hotel sector. As the pandemic has impacted hotel performance dramatically, well capitalised owners have not wanted to dispose of their hotel until market sentiment improves.

In addition, availability of bank financing for hotel acquisitions is either unavailable or at significantly lower loan-to-value ratios. As a consequence, the number of hotel transactions in 2020 across Malaysia dropped to a total of RM589 million, 30% year-on-year (Source: Real Capital Analytics).



Investors now are seeking higher returns to offset the risk of investing in the sector during the pandemic. 36% of respondents are targeting a net yield of above 7% when acquiring a 4 - 5 star hotel in Malaysia indicating that the bid-ask spread has widened unless vendors adjust their price expectations downwards. 29% of respondents are targeting net yield of between 6 – 7%, and a further 29% target 5 – 6%. Only 6% are targeting net yields of less than 5%.

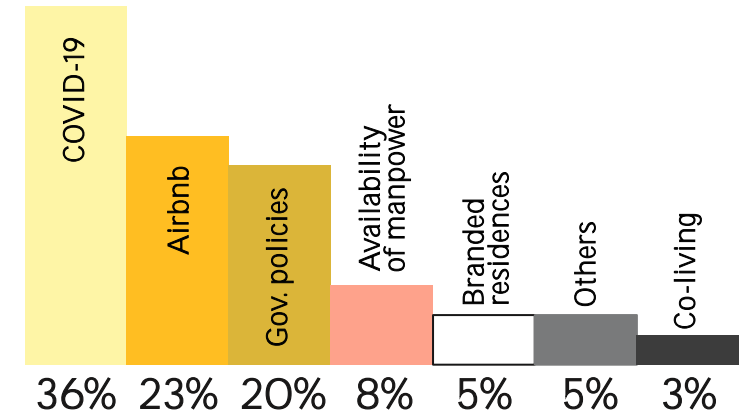
Malaysia is a developing/emerging market and foreign investors expect higher returns to offset country risk (eg political and currency), lower liquidity and transparency.

Major Threats to the Hospitality Business



36% of the responses has named COVID-19 as the major threat to their hospitality business followed by Airbnb at 23% and government policies at 20%. Availability of manpower and competition of branded residences and co-living are also deemed to be threats to the hospitality business.

Major threats to hospitality business

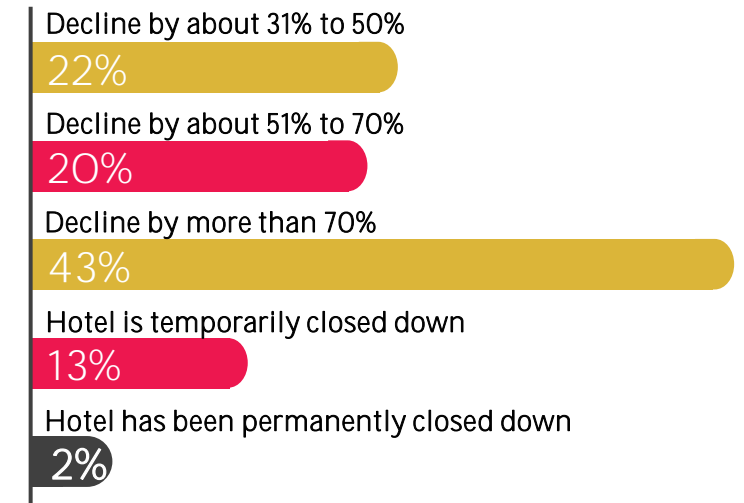


Impact of COVID-19 Outbreak

The hotel industry has been significantly impacted by COVID-19 in 2020 with guests cancelling stays due to interstate travel restrictions and the **country's** borders closed to international tourists. At the worst end of the spectrum, 13% of respondents closed their hotels, whilst 43% have seen a 70% decline in occupancy.

Resort hotels have performed better than city hotels. They have been able to capture the domestic holiday demand and are not as dependent on the weaker corporate segment. Hotel owners are having to carefully plan their resources and focus on creative marketing activities. They are pivoting towards their local community and are offering creative promotions to try to make the most of new trends in consumer behaviour. A good example is the integration of co-working spaces into city hotels to generate extra revenue whilst some hotels are offering long stay options.

How the COVID-19 outbreak impacted the hotel occupancy in 2020



Impact on Average Room Rates

How the COVID-19 outbreak impacted the hotel Average Room Rates in 2020

Decline by about 10% to 20%

10%

Decline by about 21% to 30%

15%

Decline by about 31% to 40%

28%

Decline by about 41% to 50%

22%

Decline by more than 50%

25%

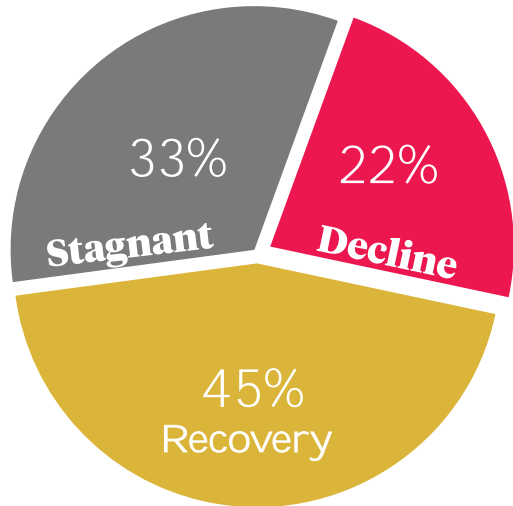


In addition to a steep drop in occupancy, 25% of respondents saw a decline of more than 50% in their average room rate (ARR) in 2020 with a further 22% seeing a decline of between 41 - 50%. With such a sharp drop in revenue, hotel owners and operators have had a hard look at their expenses to see where costs can be reduced.

Examples include reducing overheads in housekeeping, the number of staff at the front desk, restaurant staff and cutting down on food purchasing according to the predicted number of covers or bookings.



The Malaysian Hospitality Sector Outlook in the next 12 months



Majority of the respondents remain positive of the hospitality sector outlook in the next 12 months with 45% of them opining that the sector is on its way to recovery whilst 33% are of the opinion that the sector will remain stagnant and the remainder, on a downward trend.

The general view is that the hospitality sector is currently at its lowest level and that it can only improve after the vaccine is officially rolled out to the market and travel bans are

lifted. The graph on the right shows the vaccination around the world is making good progress and will only speed up as the distribution improves.

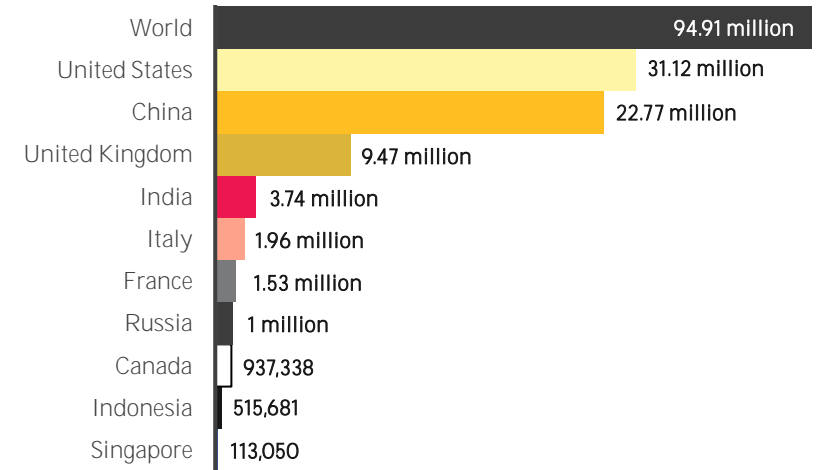
There are also concerns that the lack of government control over Airbnb and issuance of hotel licenses as well as political instability resulting in unclear policies could contribute to a lacklustre outlook of the hospitality sector in the next 12 months.

In order to minimise losses, many of the hotels were willing to be gazetted as quarantine centres over the MCO period. Others have taken this as an opportunity to maintain, renovate or refurbish their hotels and some were creative in renting out their rooms and/or dining area as workspaces.

As soon as the government lifted MCO, the hospitality industry, especially resorts immediately showed signs of recovery with a surge in occupancy rates contributed by domestic travels though the city / business hotels are still struggling to stay afloat where many of them have remained shut.

During the pandemic, some hotel owners have decided to postpone the opening of their new hotels

COVID-19 vaccination doses administered (January 31, 2021)



Source: Our World in Data

until the hospitality market improves. In Kuala Lumpur, the market will see a number of luxury new hotels coming onto the market: Conrad, SO Sofitel, Park Hyatt, Jumeirah, Kempinski and the Regent.

Nevertheless, Malaysia has always been and will continue to remain an attractive tourist and business travel destination. The hospitality sector will bounce back, slowly but surely with the evident pent-up demand as **Malaysia's** hotel rates are still relatively competitive within the region coupled with the gradual rollout of the COVID-19 vaccination globally.

Relief Measures in Improving the Hospitality Sector during the Outbreak

Tourism is an important sector of the Malaysian economy, being the third largest contributor to GDP and employing over 3.6 million people. In 2019, it contributed a total of RM86.14 billion in tourist receipts from the expenditure of over 26 million international tourists. As a key sector, it is important during these very challenging times that adequate relief measures are introduced by the government so that the sector can bounce back quickly as the global vaccination programme gets underway and international borders are opened up.

In the hotel sector, the Malaysian government has provided a wage subsidy from RM600 – RM1,200 per employee and this is limited to Malaysians earning RM4,000 and less each month, depending on the size of the company. We feel this is not very adequate as it only represents 15 – 30% of the RM4,000 monthly salary limit. In contrast Singapore has adopted a similar model being used in the UK, Canada, Hong Kong and Australia. The government pay 75% on the first S\$4,600 of the monthly salary to support those working in the aviation & tourism sectors. In Hong Kong, the government pay 50% of the monthly salary for every local employee with a salary of up to HKD 9,000.

Other ideas that have been put forward by the industry include:

- The temporary reclassification of electricity tariffs for hotels to cheaper industrial tariffs in addition to extending and increasing current utilities discounts for tourism premises.
- A temporary moratorium on quit rent and assessment, extendable dependent on the extent of virus spread.
- Tax cuts on hospitality and tourism to incentivise bookings, so that trade can resume as quickly as possible when the virus threat subsides.



Conclusion

Throughout 2020, the global hospitality industry was hit by successive COVID-19 spikes and the necessary lockdowns to flatten the curve. This inability to control the growth of the virus and the more recent transmissible variant in the UK and South Africa has led to many countries closing their borders to international travellers. With borders closed, hotel owners have put a focus on domestic travelers and this has helped to provide some stability to the sector in Malaysia.

Hopes of a recovery are dependent on the rapid and widespread distribution of the vaccines and it is really encouraging to watch this global story develop. We think 2021 will present an excellent opportunity for investors to acquire prime hotel assets that rarely change hands at reasonable prices. As more people receive the vaccine, international borders will open up, airlines will re-establish their flight networks and international traveller confidence will return.



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