

JULY 2014 PERTH HOTEL

Market Insight

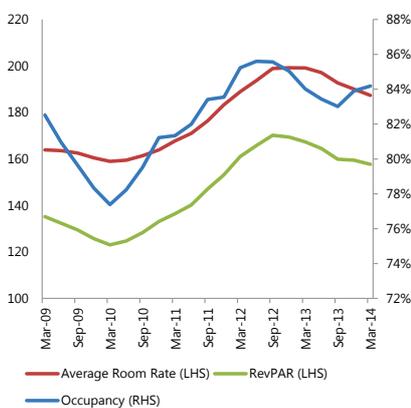
LUXURY GLOBAL HOTEL BRANDS TARGET THE PERTH MARKET

During the year ended March 2010, the adverse economic climate brought on by the Global Financial Crisis, caused a short term reduction in room occupancy and placed pressure on operators to stimulate demand through room rates. A decline in room occupancy of some 5.0% to approximately 77.4% was recorded in March 2010, which combined with a decline (-3%) in average room rate to \$158.99 resulted in a 9% decrease in revenue per available room (RevPAR) to \$123.03.

In the subsequent two and a half years, the Perth Hotel market experienced a significant recovery in the underlying fundamentals. The quarter on quarter increases in both room occupancy and average room rate from June 2010 to June 2012 caused RevPAR to increase by a total of 32.9% over the equivalent period.

Figure 1
Perth City Hotel Market

Average Room Rate, RevPAR & Occupancy



Source: Knight Frank Research/ABS



Artist's impression of the Ritz Carlton hotel to be built at Elizabeth Quay, which will comprise 204 rooms

The virtually static room supply in the Perth City market over the past five years, coupled with a resource driven boom in corporate travel, led to a significant increase in room occupancy that reached a height of 85.6% in the year ended June 2012. Consequently, during the years ending Jun-11 and Jun-12, annual average room rates surged by 7.3% and 13.2% respectively which saw RevPAR increase by 12.5% and 18.2% during the same periods.

Annual room rates peaked at \$199.20 in December 2012, however have since declined following a significant reduction in resource driven corporate demand resulting in falling room yields.

More recently, April 2014 recorded a marginal pickup in RevPAR (0.4%), suggesting that stability was being restored to the market. In addition, room occupancy had experienced positive growth for five of the six months leading into April 2014. However, Perth's RevPAR declined sharply in May 2014 by 7.8%, with operators again reacting to softer conditions by stimulating demand through lower room rates. Room occupancy declined during May 2014 by 2.1% following three successive months of positive growth. A combination of factors is believed to have contributed to the recent fall in hotel market indicators. Weekend

discounting spurred on by softer levels of leisure tourism following the release of the federal and state budgets, as well as an absence of any major events attracting tourists to Perth may have adversely effected the market during May. Furthermore, seasonality may be responsible for softer hotel market conditions leading into the winter months.

A continued re-basing of room rates may occur throughout the remainder of 2014. Thereafter, a period of stabilisation may follow with restricted growth in RevPAR over the short to medium term, while the market adjusts to prevailing demand conditions. However, further down side risk is likely to be a factor in the medium to long term as proposed new room supply enters the market.

Despite a reduction in corporate demand, Perth continues to suffer from a shortage of hotel accommodation with major new supply not expected until 2016. Although WA's resource sector has been a key driver of demand, it has also played a key role in inflating construction costs thus making new hotel development opportunities unviable. As a result, returns on hotel accommodation investment, when compared to other uses of capital, have been inadequate to stimulate hotel development over recent years.

In 2011 the State Government announced an incentives program aimed at stimulating supply in Perth's hotel sector. The specifics of this incentives program included providing state land at reduced rates, flexible floor space bonuses and infrastructure grants.

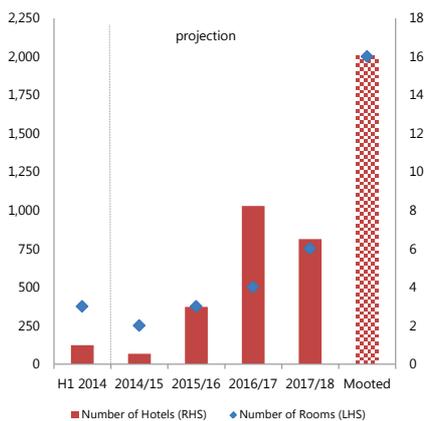
Development Activity

It is estimated that the total supply of hotels, motels and serviced apartments within the broader Perth metropolitan area was 11,174 rooms as at June 2013. The supply located within Perth City amounts to 5,931 rooms across 47 establishments. Of this, seven hotels comprising 1,917 rooms (17% of total metropolitan stock) are considered to be



Artist's impression of the Double Tree Hilton hotel to be built at Elizabeth Quay, comprising 241 rooms

Figure 2
Perth City Hotel Supply Forecast
Number of Rooms & Number of Hotels



Source: Knight Frank Research
NB includes Burswood & Ace Cinema site (Subiaco)

five-star establishments, including Pan Pacific Perth (486 rooms), Crown Metropol (396), Hyatt Regency (367), Duxton (306), Parmelia Hilton (273), the Richardson (74) and the Terrace (15). Over the past five years, hoteliers in Perth have had little need to refurbish or upgrade their properties due to the strength of resource driven corporate demand. As a result, the other 83% of hotel rooms in Perth is dominated by older stock.

With a number of projects recently being announced in Perth, hotel supply is set to increase over the next few years, albeit the impact of any bulk room additions are unlikely to be felt until late 2016 and into 2017. A significant portion of new supply consists of luxury global brands which when completed will increase the proportion of five-star establishments in the Perth market. Not only will these new additions revitalise the city's aging supply, but also push owners

to upgrade or refurbish existing stock.

Knight Frank is currently tracking 5,485 rooms across 43 establishments which are either under construction, approved or seeking approval within the broader Perth metropolitan area. The majority of this potential supply (3,574 rooms across 29 establishments) is located within the Perth City LGA. However, given the current softer demand conditions, it is unlikely that all proposed developments will go ahead.

Key luxury hotels expected to enter the Perth market over coming years include:

- **Crown Towers**, a \$568 million development at the Crown complex in Burswood comprising 500 rooms which is due for completion in 2016.
- BGC's, **Westin Perth** (\$250 million) which will be located on the former FESA site at 480 Hay Street and will

Table 1
Select Major Hotel Supply – Perth Metropolitan

Project Name	Region	Status	Developer	No. of Rooms	Estimated Completion
The Old Treasury Building	Perth CBD	Under Construction	FJM Property	48	2015
Hotel Alex Perth	Northbridge	Under Construction	The Cicero Project Pty Ltd	74	2015
Crown Towers	Burswood	Under Construction	Multiplex Ltd	500	2016
Ibis styles Hotel	East Perth	Under Construction	Rehawk Property Group	228	2016
Aloft	Rivervale	DA Approved	BGC	224	2016
Double Tree (Hilton)	Fremantle	DA Approved	SKS Group	150	2017
Westin Perth	East Perth	DA Pending	BGC	300-350	2017
The Ritz-Carlton	Perth CBD	DA Approved	Far East Consortium	204	2018
Double Tree (Hilton)	Perth CBD	DA Approved	SKS Group	241	TBA
IHG – Holiday Inn Express	East Perth	DA Approved	Sunfire Asset	224	TBA
Amara Business Hotel	East Perth	DA Approved	-	266	TBA
Duxton Hotel (extension)	Perth CBD	DA Approved	-	126	TBA
Kings Hotel (extension)	Perth CBD	DA Approved	-	52	TBA

Source: Knight Frank TBA: To be advised

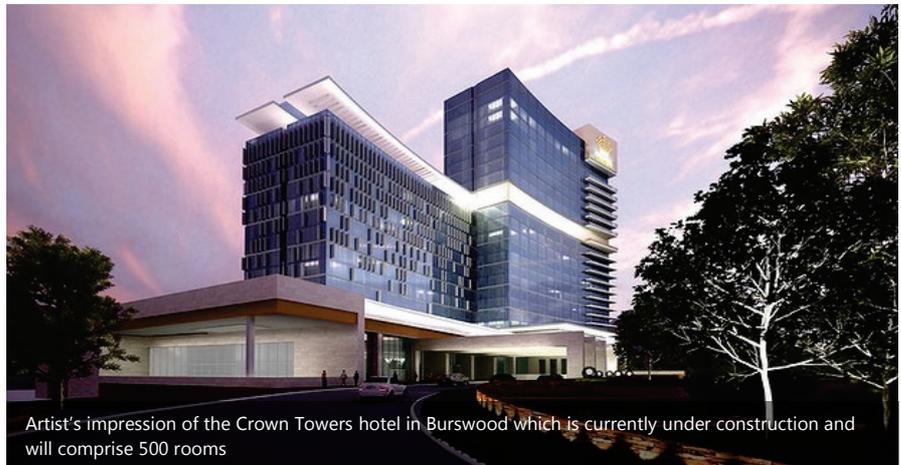
include a minimum of 300 rooms with the potential for 350 rooms.

- A 204 room **Ritz-Carlton** (\$350 million) which will be constructed on the eastern side of Elizabeth Quay (site 9) and is due for completion in 2018.
- In addition, **Hilton Worldwide** plan to build two of its boutique, Double Tree by Hilton properties that will include a 241 room hotel at Barrack Square, Perth (completion date to be advised) and a 150 room hotel in Fremantle (due for completion in 2017).

Investment Activity

Despite the hotel development pipeline picking-up, investment activity within the Perth market has continued to decline from its 2011 peak of \$151 million. Declining sales volume figures can be attributed to a softening in hotel operating metrics, as well as tightly held stock. In the twelve months ending 31 December 2013, sales activity injected \$75.98 million into the Perth hotel market, which is a 19.4% decrease from the \$94.3 million that changed hands in 2012, albeit skewed by the Esplanade Hotel sale (\$88.5 million).

The most recent hotel sale in Perth was the Sebel Residence, at 60 York Street in East Perth, which sold to Sunshine Adventure in September 2013 for \$19.2 million reflecting an initial passing yield of 8.7%. The 4.5, AAA Tourism Star Rated establishment comprises 3,711m² of strata area at a rate of \$5,174/m². The Sebel residence occupies part of two interlinked buildings of a larger mixed-use development, known as South Cove which comprises residential apartments, offices, restaurants and bars. The property opened in October 2003 and is contained on levels



Artist's impression of the Crown Towers hotel in Burswood which is currently under construction and will comprise 500 rooms

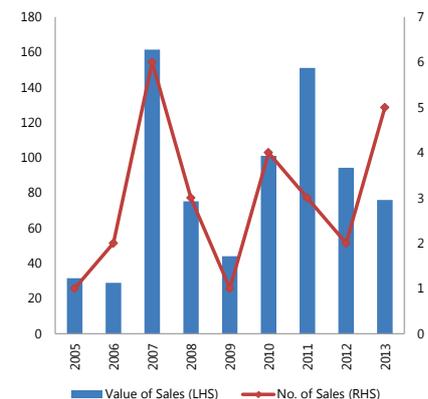
two to five of two interconnected buildings known as Blocks A and B. Room occupancy at the time of sale was 77.0% while the average room rate was \$258.00 per day. The sale reflected a rate per room of \$336,842 and an IRR of 10.75%.

In addition, Esplanade River Suites, at 112 Melville Parade in Como sold in January 2013 to Narada Hotel Group Limited for \$30.93 million reflecting an initial passing yield of 9.4%. The property was originally constructed in 1922 and underwent a major redevelopment before reopening as the Esplanade River Suites in 1998. The 101 room, 4.5 star hotel was sold with 74.0% occupancy, an average room rate of \$213 and a RevPAR of \$158. The sale reflected a rate of \$306,200 / per room and an IRR of 12.4%.

The largest transaction to occur over recent years was the sale of the Esplanade Hotel in Fremantle, which sold in November 2012 to Primewest for \$88.5 million reflecting an initial passing yield of 12.5%. The 4.5 star, 300 room hotel was originally constructed in 1897 and was progressively extended in 1903, 1996 and 2003. As at July 2012, the

hotel was operating at 85.0% occupancy with an average room rate of \$213 and a RevPAR of \$181.05.

Figure 3
Perth Hotel Sales Activity 2005 - 2013
(\$ million) Sales Value



Source: Knight Frank Research

Private investors, syndicators and owner occupiers are the most active purchasers in the market. Private investors and syndicators will typically favour hotels with well-structured lease arrangements in place offering a base rent and turn over rent at

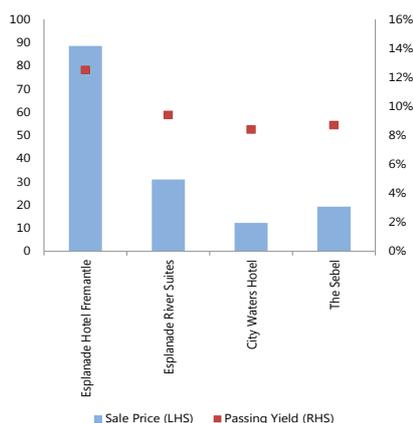
Table 2
Major Hotel Sales Activity – Perth Metropolitan

Name / Suburb	Star Rating	Price (\$ mil)	Initial Yield (%)	No. of Rooms	Average Room Rate (\$)	Room Occupancy (%)	RevPAR (\$)	Sale Date
The Sebel Residence, East Perth	4.5	19.20	8.7	57	258.00	77.0	198.50	Sep-13
City Waters Motel, Perth	3	12.25	8.4	61	113.00	81.0	91.53	Apr-13
Esplanade River Suites, Como	4.5	30.93	9.4	101	213.00	74.0	158.00	Jan-13
Esplanade Hotel, Fremantle	4.5	88.50	12.5	300	213.00	85.0	181.05	Nov-12
Joondalup City Hotel	-	5.80	12.6	35	130.80	82.0	107.26	Aug-12
Citygate, Perth	4.5	61.00	6.5	278	165.00	86.0	142.00	Dec-11

Source: Knight Frank

threshold. Alternatively, these buyer types will seek hotel investments with a management agreement in place. Owner occupiers favor walk-in, walk-out opportunities.

Figure 4
Major 2012/2013 Perth Hotel Sales
(\$ million) Sales Value > \$10 million



Source: Knight Frank Research

WA Tourism

Western Australians continue to travel out of the country at an increasing rate with data showing that outbound passenger movement from WA for leisure grew by 7.8% during the twelve months ending 31 December 2013. The most popular destination was Indonesia which was closely followed by Thailand.

Notwithstanding this outbound travel, Western Australian's are also travelling within their State in increasing numbers, with 3.0% growth in intrastate visitor numbers and 1.2% growth in visitor nights, both exceeding the national average. However, despite this growth, overnight spend decreased by 5.5%. The Holiday/Leisure segment, which is the

largest segment, was the primary driver of growth in intrastate visitation, recording a 10.6% increase during CY 2013. However, intrastate business visitation declined by 10.2% over the equivalent period whilst the national average was stable. The number of nights also declined, down 16%.

Significant increases were recorded in interstate visitation and nights in WA during CY 2013 showing growth of 12.8% and 23.2% respectively, both well ahead of the national average. Interstate spend also grew significantly, up 28% which can be attributed to increases in visitor numbers, visitor nights and the average length of stay. The Business segment which grew by 19.1% and is the largest interstate visitor segment was the primary driver of growth in interstate visitation.

Although international visitation in WA continued to climb with an increase of 2.1% being recorded during CY 2013, it fell below the national average (5.6%). The Holiday/Leisure and Visiting Friends and Relatives segments facilitated most of the growth, which grew by 7.9% and 7.2% respectively. Strong growth in these segments however was offset by declines in visitation by those visiting for all other purposes, particularly those visiting while 'in transit' and those visiting for business purposes. Despite growth in visitation, expenditure declined, down 3.1% which fell below the national average of 4.9%.

Outlook

Looking ahead, the Perth hotel market will likely experience softening compared to recent years as resource driven corporate travel remains subdued. A reduction in corporate travel however will likely prove favorable for the general tourism market as

availability and affordability of hotel rooms moves to more appealing levels.

A 2011 State Government demand forecast suggests that an extra 1,900 hotel rooms are needed by 2020 to cater for Perth's growing tourism industry. Current forthcoming hotel supply is sufficient to achieve this figure. However, the softening in trading conditions being driven by room rate decline, allied to the costs of developing new hotels, is likely to make development a difficult task to achieve. Add to this the announced new developments, as well as potential new rooms supply, and it is likely that as proposed hotel projects reach the construction phase, many other proposed developments are likely to be cancelled.

The arrival of luxury global hotel brands in Perth will likely see existing hoteliers upgrade or refurbish their establishments in order to remain competitive. This is demonstrated by the Duxton hotel's plans to undergo a \$100 million upgrade which has gained approval by the State planning panel. The upgrade includes an extra 126 rooms, a 500-person capacity ballroom, function rooms, day spa and rooftop bar, which is not only indicative of the level of demand for new hotel rooms, but also for conference facilities.

Perth's shortage of hotel rooms over recent years has seen room nights demand pushed out of the City. However, as new supply comes online, much of which is focused within the CBD, demand is likely to be drawn back into the City which is expected to adversely impact hotels in fringe locations. However, with the formalisation of the next major round of construction expected to come online from 2016 onwards, it is expected that any softening in the market will be mitigated in the near term.

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