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# The Asian Hotel Valuation Index 1999: Values back on the rise?

As illustrated in this article, 1999 saw the major markets in Asia showing signs of improvement in line with the recovery of many Asian economies. This has resulted in an increase in hotel values by approximately 3% over the last year. In many instances, the recovery of occupancy and average room rate levels, coupled with an improved market outlook, has boosted hotel values for the first time since the start of the economic recession in mid 1997, suggesting that hotel values may be on their way back to pre-crisis levels.

Every year HVS International Singapore estimates hotel values of four and five-star hotels located in twelve capital cities throughout Asia using its sophisticated benchmark study, the Hotel Valuation Index (HVI). In addition to monitoring annual percentage changes in value, the HVI ranks each city relative to an average for the thirteen markets. Operating data for each hotel within a representative sample of hotels selected for each market is aggregated to produce an average performance for the city as a whole. This is used to derive a representative forecast of income and expense for each market, reflecting demand and supply conditions prevailing over the year. A unique discounted cashflow valuation technique developed by HVS International is then applied using the prevailing market rates of return for each city. In order to be able to make a direct comparison from year to year, the sample for each city has remained the same.

**Table 1 - Hotel Values by Market in Asia, 1999**

| | VALUE PER ROOM / US$ | | | | | | |
|---|---|---|---|---|---|---|---|
| | 1996 | 1997 | % Change | 1998 | % Change | 1999 | % Change |
| Seoul | 361,000 | 313,000 | -13% | 259,000 | -17% | 310,000 | 20% |
| Singapore | 376,000 | 322,000 | -14% | 294,000 | -9% | 344,000 | 17% |
| Tokyo | 777,000 | 794,000 | 2% | 633,000 | 20% | 683,000 | 8% |
| Bali | 153,000 | 162,000 | 6% | 101,000 | -38% | 105,000 | 4% |
| Hong Kong | 678,000 | 626,000 | -8% | 357,000 | -43% | 369,000 | 3% |
| Bangkok | 229,000 | 165,000 | -28% | 150,000 | -9% | 75,000 | 3% |
| Kuala Lumpur | 214,000 | 131,000 | -39% | 74,000 | -44% | 75,000 | 1% |
| Jakarta | 221,000 | 199,000 | -10% | 70,000 | -65% | 70,000 | 0% |
| Manila | 216,000 | 201,000 | -7% | 139,000 | -31% | 130,000 | -6% |
| Shanghai | 252,00 | 249,000 | 1% | 202,000 | -19% | 177,000 | -12% |
| Beijing | 254,000 | 215,000 | -15% | 166,000 | -23% | 140,000 | -16% |
| Mumbai | 309,000 | 290,000 | -6% | 250,000 | -14% | 209,000 | -16% |
| Average | 336,667 | 305,583 | -9% | 224,583 | -27% | 230,500 | 3% |

## 1999 PERFORMANCE

The 1999 HVI shows that hotel values across Asia on average, rose by approximately 3% compared to a decrease of 27% in 1998 and 9% in 1997. This confirms

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that Asian hotels are well on the road to recovery from the regional crisis. Of the thirteen markets that have been monitored and analysed, nine showed increases in value, with the remaining four cities experiencing a decline. However, as seen from Table 1, only two markets, showed double-digit percentage increases, namely Seoul and Singapore.

**Table 2 - Asian Hotel Valuation Index**

| City | 1996 | 1997 | 1998 | 1999 |
|---|---|---|---|---|
| Singapore | 0.656 | 0.591 | 0.153 | 0.213 |
| Tokyo | 0.636 | 0.389 | 0.162 | 0.229 |
| Seoul | 0.454 | 0.481 | 0.220 | 0.320 |
| Manila | 0.642 | 0.597 | 0.303 | 0.396 |
| Kuala Lumpur | 0.754 | 0.639 | 0.362 | 0.427 |
| Mumbai | 0.680 | 0.490 | 0.327 | 0.469 |
| Bali | 0.749 | 0.740 | 0.441 | 0.540 |
| Jakarta | 0.918 | 0.861 | 0.546 | 0.637 |
| **Average** | **1.000** | **0.908** | **0.667** | **0.685** |
| Bangkok | 1.072 | 0.908 | 0.565 | 0.945 |
| Shanghai | 1.117 | 0.956 | 0.642 | 1.049 |
| Hong Kong | 2.014 | 1.859 | 0.779 | 1.125 |
| Beijing | 2.308 | 2.358 | 1.382 | 2.082 |

Despite these increases, hotel values in many instances, remain far below their replacement and initial costs hence many hotel owners and banks are still facing difficulties in concluding hotel transactions in the region. Furthermore, with hotel values slowly increasing again, many hotel owners who are not facing any pressure to sell, are riding the storm, holding on to their assets until the market is back up and values are approaching or in excess of pre-crisis levels. As a result, there was little activity for the prominent opportunistic hotel funds seeking to benefit from the marginal upswing.

For many markets, whilst values are likely to increase within the next few years, funding new hotel developments remains difficult as hotel values are still below replacement costs. In response to this, more and more mixed-use projects are being initiated in an attempt to off-set the disappointing low hotel real estate yields with other higher yielding property uses, such as residential and office use. Examples of such developments include the new JW Marriott in Seoul, the Grand Hyatt in Tokyo, and the proposed Conrad Hilton in Bangkok.

## ON THE RISE ....

### Seoul, South Korea

With Korea being one of the first countries to recover from the economic crisis, the hotel market in Seoul is continuing to show strong levels of performance. Not only has the Korean won strengthened against the US dollar, but for the first time in years the Korean won denominated ADR and the US dollar denominated ADR have both increased. Despite the opening of the new COEX Hotel Inter-Continental, it remains difficult to get a hotel room in Seoul, hence the outlook for the city remains positive. Furthermore, with super deluxe hotels now permitted to host wedding ceremonies and the return of Koreans patronising hotel restaurants and F&B outlets, hotel revenues have generally improved hence there has been a greater impact on values which is not only attributable to strong hotel room demand.

Despite the recent sale of the Seoul Hilton in late 1999, troubled hotel owners are unlikely to sell their assets at bargain prices as current market values are sill well below replacement cost values and initial development costs, a large proportion of which are attributable to high land costs.

### Singapore, Republic of Singapore

For the first time in three years, visitor arrivals to Singapore have increased. Despite this, hotels have not

| Table 3 - Ranking of City by % Change in Hotel Value | | |
|---|---|---|
| | 1996 | % Change |
| Seoul | 310,000 | 20% |
| Singapore | 344,000 | 17% |
| Tokyo | 683,000 | 8% |
| Bali | 105,000 | 4% |
| Hong Kong | 369,000 | 3% |
| Bangkok | 154,000 | 3% |
| **Average** | **230,000** | **3%** |
| Kuala Lumour | 75,000 | 1% |
| Jakarta | 70,000 | 0% |
| Manila | 130,000 | -6% |
| Shanghai | 177,000 | -12% |
| Beijing | 140,000 | -16% |
| Mumbai | 209,000 | -16% |

been able to increase their ADR for the third consecutive year. Nevertheless, hotel values in Singapore have increased by approximately 17% over the last year, making it the second strongest performer in Asia. As Singapore continues to position itself as the financial and IT centre for the region, hotel demand is likely to rise further, enabling hotels to increase their ADR and profit margins for the first time in several years. With the improvement in the performance of hotels, values are likely to increase over the next few years, particularly as there is limited new supply entering the market.

Regardless of the improvement in hotel values, transactions, other than for redevelopment purposes, remain few and far between, as owners continue to wait for a full recovery before liquidating their hotel assets. However, investor confidence in hotel real estate is beginning to return. With low hotel investment yields, mixed-used development projects, including a hotel component, are likely to be the best alternative for investors seeking ownership of hotel real estate in Singapore.

## Tokyo, Japan

A slight improvement in economic outlook coupled with a marginal increase in occupancy and average room rate, has resulted in hotel values in Tokyo increasing by approximately 8%, making it the third strongest performer in the region. Despite an improvement in occupancy and ADR, many hotels in the city continue to suffer as food & beverage and banqueting revenues lag behind previous years. The regional crisis has led to many local companies reducing the number of organised events and functions, furthermore, more people are choosing alternative locations for their wedding ceremonies, historically, these have been a lucrative source of revenue for hotels. However, as the entry barrier for new hotels is high with new supply being limited, and as important trade partners of Japan recover from the crisis, the outlook for this hotel market remains positive.

Generally hotel real estate transactions in Japan are limited in number and this is likely to remain the case for some time. However, there are a number of hotel portfolios, owned by distressed sellers, rumoured to be on the market. There is much interest being shown by overseas investors in these deals which are being actively pursued, perhaps things are about to change.

## Hong Kong, China SAR

After two years of declining numbers in tourist arrivals, people are returning to Hong Kong; this is reflected in the higher occupancy levels achieved by hotels. Despite this initial sign of recovery, hotels are continuing to struggle to increase average room rates. The overall result shows some improvement in hotel values. Furthermore, after many years of strong performance and excessive average rates, Hong Kong hotels are now in the process of rationalising their operations in order to adapt to much lower revenues. With little new supply entering the market and a reasonable forecast of economic growth, the outlook for Hong Kong is positive once again.

With hotel values back on the rise, interest for Hong Kong hotels is likely to increase. However as values remain far below replacement costs, hotel sales other than for redevelopment purposes, are likely to be limited.

### Bangkok, Thailand

Over the past twelve months Bangkok has often been considered as the hotel market in Asia with the greatest potential. However, with significant oversupply, both occupancy and average room rates have remained under pressure making it difficult for many owners to service their debt. Whilst many proposed hotel projects have been suspended indefinitely, new developments continue to be a serious threat that cannot be ignored. However, with tourist demand continuing to remain strong and the return of investor confidence, demand for hotel accommodation in Bangkok is likely to increase. Despite this, hotel values in Bangkok remain far below their replacement cost value as growing demand is currently absorbing excess supply.

With income approach based values remaining far below replacement cost values, owners are likely to keep their assets until such time as the gap between the two values narrows. Furthermore, despite the new and improved bankruptcy and foreign investment laws and the overwhelming interest to acquire under performing hotel assets, banks are in no rush to off-load their non-performing loans.

### Kuala Lumpur, Malaysia

Notwithstanding the overwhelming oversupply in the Malaysian capital, for the first time in three years hotel values in Kuala Lumpur have seen a marginal increase of approximately 1%. As hotels stabilise their occupancy and average room rates, the improved market outlook for Kuala Lumpur has resulted in hotel values increasing, albeit marginally. The improvement in the hotel market may be attributed to the return of foreign investors, increase in number of visitor arrivals, and a strong forecast in economic recovery. An impending wave of new supply however, remains a concern as projects which were suspended as a result of the crisis, are resumed, despite hotel values remaining far below replacement costs.

With no pressure to sell and troubled hotel owners being able to restructure their debt, hotel transactions in Kuala Lumpur remain scarce. Furthermore, as many hotels are relatively new, owners have had little time to reduce the debt on their assets through operating the hotel, with values in some cases remaining below the outstanding debt balance, making owners unwilling to part with their assets just yet. Kuala Lumpur continues to be a difficult market with greater long term rather than short term potential.

### Jakarta and Bali, Indonesia

As other countries in the region are recovering from the economic crisis, Indonesia continues to struggle. In Jakarta, hotels continue to operate at low occupancy levels and average room rates. However, Bali has seen some improvement, as demand from key feeder-markets returns. With domestic political difficulties, investor confidence remains low and tourists continue to avoid Indonesia making it difficult for hotel values to improve and recover to pre-crisis levels within the foreseeable future.

Numerous investors looking for opportunities eagerly await the sale of assets, held by the Indonesian Banking Restructuring Authority (IBRA) which will initiate the re-capitalisation of troubled banks. It is likely that IBRA will sell at some point in time and therefore opportunities are likely arise for those who continue to patiently look for deals in Indonesia.

## THE TRAILERS ....

### Manila, The Philippines

Although some consider The Philippines to be the country least affected in the region by the economic crisis, the hotel

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market in Manila continues to be weak despite no new supply entering the market over the last few years. Whilst occupancy levels are beginning to improve, average room rate remains under pressure and will continue to suffer as new hotels enter the market. Furthermore, the hotel market in the city also competes with other types of accommodation such as first class serviced apartments, hence the market outlook remains weak. There is unlikely to be many transactions in this climate.

**Beijing and Shanghai, PR China**

Both cities continue to suffer from an oversupply of hotels in each market. Despite an increase in occupancy, the average rate of hotels in Beijing showed little improvement. Whereas both occupancy and average rate in Shanghai fell further from 1998 levels. Regardless of the current moratorium on new hotel development, more new supply is about to enter both markets hence the short-term outlook for both cities remains weak. However, with the possibility of China entering the WTO coupled with the economic recovery of important trade partners, demand is likely to increase, particularly for hotels located in Shanghai's new development area, Pudong.

With the current constraints on foreign ownership and lack of transparent investment policies, hotel ownership for non-Chinese remains a challenge.

**Mumbai, India**

Political instability and the recent border war with Pakistan have caused hotel demand in Mumbai to drop substantially during 1999. As a result, average room rate has also declined. With the new government in place, political unrest is likely to remain at bay and demand is likely to pick up again. However, with new supply outpacing new demand, a recovery of occupancy and average rate within the next twelve months is likely to be difficult.

## THE OUTLOOK FOR 2000

In general the performance of hotels in key markets across Asia during 1999 has been encouraging, with an overall positive rise in hotel values for the region. The process of economic recovery is more marked in some countries than others and this is reflected in the improved performance of hotels in those markets. Whilst 2000 is likely to see the key performance indicators of occupancy and average rate improve in most markets, there is still the threat of new supply entering the market and delaying an improvement in the overall performance of hotels within that city. Furthermore, whilst the year ahead may see hotel values increase, owners still take account of the replacement cost value of their asset. As long as the gap remains wide and with little external pressure to sell, hotel sales are likely to remain few and far between in the year ahead.

# HVS International

HVS International is a global hotel real estate consultancy operating from eleven offices worldwide, providing consulting services specifically related to the hotel and hospitality industry. HVS International has worked on over 10,000 hotels in more than 60 countries around the world. Our consulting services encompass valuations, feasibility analyses, due diligence, market studies, highest and best use studies, site selections, financial projections, development advice, impact quantification, litigation support and investment analysis.