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THE PARISIAN HOTEL MARKET

ILLUMINATIONS FROM THE CITY OF LIGHT

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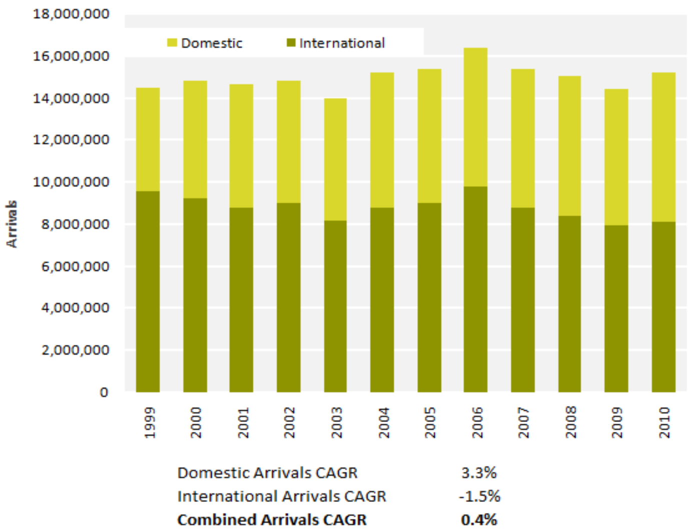
Summary

This article presents an overview of hotel performance for the Paris market from 2007, through the depths of the economic crisis, and into the beginning of the recovery in late 2010; we also provide our views on expected performance for the next three years. Finally, we briefly discuss the transactions market, values per room and new investors over the last year. From these various angles, the resilience of the Parisian market and its bright prospects become evident.

Demand

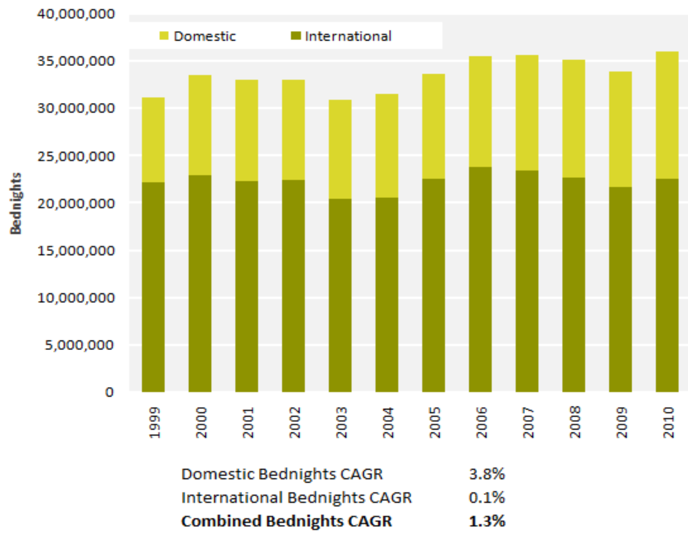
While the number of total **arrivals** has remained practically unchanged since 1999 with a compound annual growth rate (CAGR) of 0.4% – to 15.2 million in 2010 – the proportion of international arrivals has shifted from 66% of the total in 1999 to 55% in 2010, reflecting the strengthening of demand from the domestic market; international demand decreased slightly at a compound rate of 1.5% over this period, while domestic demand increased at a CAGR of 3.3%.

FIGURE 1: ARRIVALS



Source: Paris Tourism Office

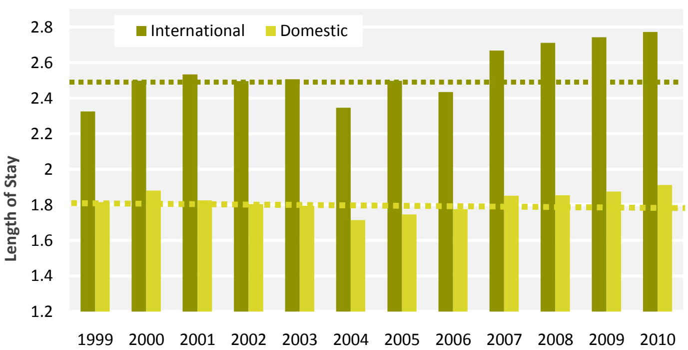
FIGURE 2: BEDNIGHTS



Source: Paris Tourism Office

The number of bednights, however, did see growth; 1.3% to the end of 2010. The same shift towards a greater proportion of domestic demand was seen with domestic demand seeing a CAGR of 3.8% compared to 0.1% for international demand. Total overnight stays in Paris in 2010 were just over 36 million.

FIGURE 3: LENGTH OF STAY (NIGHTS)



Source: Paris Tourism Office

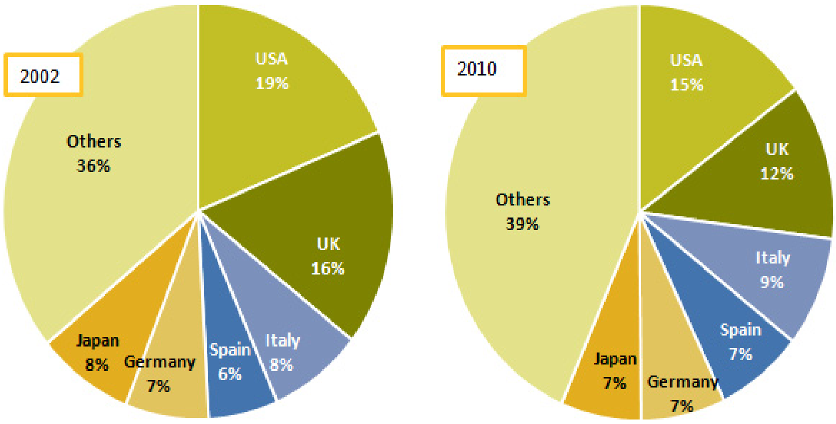
The difference in the rate of change between arrivals and bednights is a result of variations in **length of stay.** While the length of stay for domestic demand has remained practically unchanged since 1999, growing from 1.8 to 1.9 nights, international visitors have tended to stay longer, up from 2.15 nights in 1999 to just under 2.8 in 2010.

In 2010, combined visitation from the two main source countries, the USA and the UK, still represented about a quarter of total international visitation. This is, however, a decrease on the combined 36% the two countries represented in 2002. Foreign visitation to Paris has further diversified since 2002, as demand from various other regions – notably South America, Asia and the Middle- and Far-East – picked up, albeit from a low base. The following graphs show the key changes from 2002 to 2010.

FIGURE 4: MAIN SOURCE COUNTRIES 2002 AND 2010 (MILLIONS)

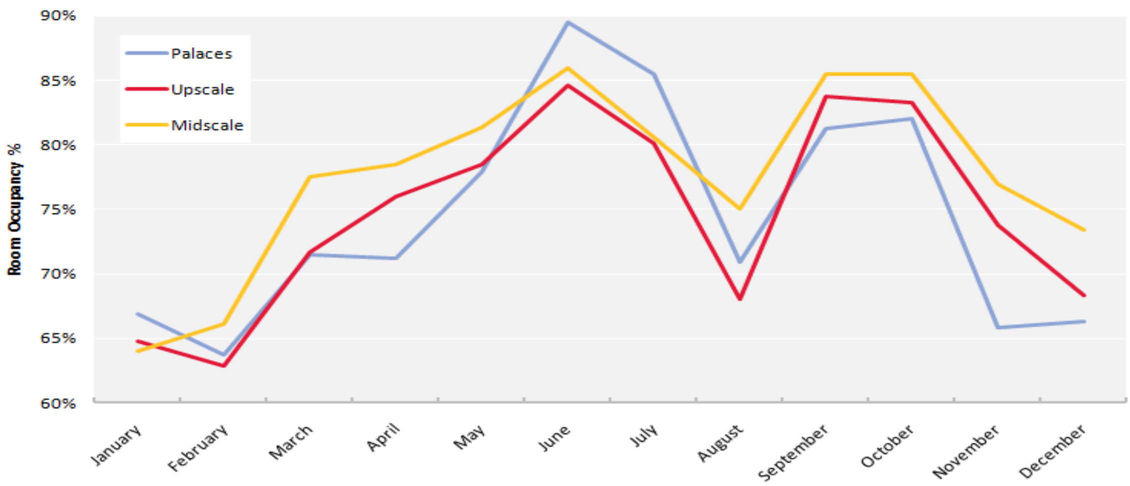
Source Countries	2002	2010
USA	1,692	1,208
UK	1,508	987
Italy	701	695
Spain	520	589
Germany	622	569
Japan	721	544
Others	3,229	3,527
TOTAL	**8,993**	**8,119**

Source: TourMIS



The **seasonality** of demand, depicted in the following graph, shows that midscale, upscale and palace hotels all followed a very similar pattern in 2010.

FIGURE 5: SEASONALITY – 2010



Source: STR Market Reports

As reflected in the graph, Paris experiences the expected seasonality trend for a city, with peaks in demand from May to June and September to October. Although demand during the summer season decreases owing to the slowdown in business activity, leisure demand ensures that it still remains at reasonable levels of around 65-75% throughout July and August. This broad seasonality indicates a healthy balance between business and leisure demand.

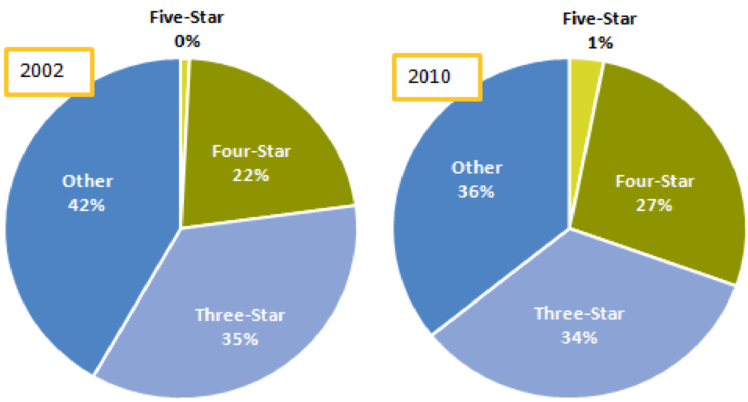
Supply

The total number of hotel rooms in Paris has remained virtually unchanged since 2002, at just about 76,600 in 2010. However, the share of four-star and five-star rooms over this period has increased from less than 23% to over 30%, as the number of hotels in these categories combined increased from 143 to 210. The CAGR for four- and five-star hotel rooms was 18.5% and 2.7%, respectively, over these nine years. This also partly reflect the impact of the change in denomination for hotels which started in 2009. During this period, on the other hand, the number of three-star hotel rooms and other categories slightly decreased, at a CAGR of -0.6% and -1.9% respectively.

FIGURE 6: HOTEL SUPPLY PER CATEGORY 2002 AND 2010

	2002	2010	CAG
Five-Star	616	2,395	18.5%
Four-Star	16,892	20,966	2.7%
Three-Star	27,178	25,851	-0.6%
Other	32,034	27,410	-1.9%
Total	76,720	76,622	-0.02%

Source: Paris Tourism Office



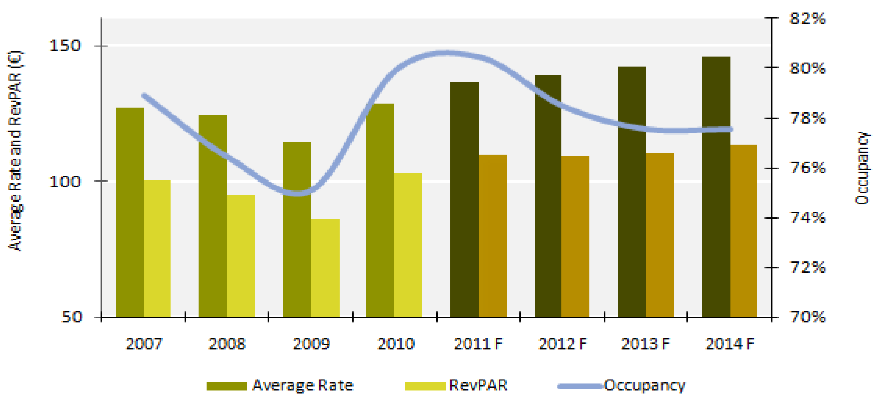
Five-star hotel rooms increased from about 616 in 2002 to 2,395 in 2010 (also partly due to the change in category denomination in 2009). In line with this, the new supply coming into the market is primarily upmarket: two palaces have opened in the last few months, the 149-room Royal Monceau (October 2010) and the 81-room Shangri-La (December 2010). Another two hotels in this category will be opening in the next couple of years: the 138-room Mandarin Oriental in mid-2011 and the Peninsula Hotel in early 2013, with a further 200 rooms. An 80-room hotel under the Cheval Blanc brand is to be developed by LVMH in the former La Samaritaine department store and is expected to open in 2014. In the upscale category, the only confirmed project we are aware of is the 90-room W Hotel Opera (mid-2011). On themidscale category, the only immediate opening we are aware of is the 117-room Courtyard by Marriott in Boulogne (September 2011). High barriers of entry render the development of budget or even midscale hotels within central Paris ('intramuros') somewhat less attractive.

We consider that the strong predominance of Asian brands within the upper end of the new supply should be beneficial in capturing growing Asian demand within the palace hotel category.

Hotel Performance

In correlation with decreases in demand for most European markets in 2008, **midscale hotels** in Paris experienced a slowdown in occupancy compared to the previous year, and subsequent downward pressure on rates in the second half of 2008. A 5% decrease in RevPAR for the whole of 2008 was followed by a steeper 10% decline in 2009 at the height of the recession. The latter months of 2010, however, pointed towards significant improvements in performance, resulting in a rather remarkable recovery of a 20% increase in RevPAR. Both average rate

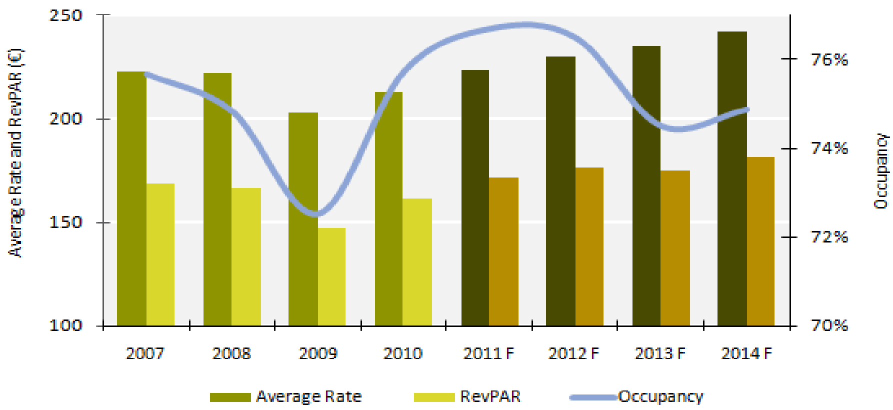
FIGURE 7: MIDSCALE HOTELS PERFORMANCE



Source: STR Global and HVS

and occupancy for midscale hotels were slightly above 2007 figures by the end of 2010, resulting in a net overall gain in RevPAR of 3% over this period. Following the strong recovery in 2010, we forecast occupancy to peak in 2011 before a slow decrease due to the arrival of new supply, and we forecast average rate to grow by 5% in 2011 and between 2-2.5% thereafter.

FIGURE 8: UPSCALE HOTELS PERFORMANCE

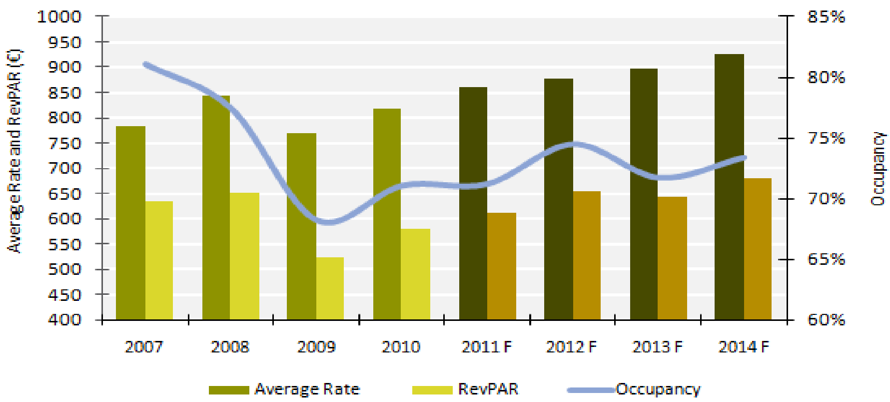


Source: STR Global and HVS

On the contrary, RevPAR performance for **upscale hotels** was slightly less pronounced. A minimal drop in RevPAR in 2008 was followed by a decline of 10% in 2009. Subsequently, a still healthy but milder RevPAR recovery of approximately 10% by the end of 2010 positioned this category of hotels at 4% below their 2007 RevPAR performance. We expect occupancy at upscale hotels in Paris to remain fairly constant at about 75%, despite the new hotels expected to enter the market. Average rate is forecast to increase by 5% in 2011, in line with the increase in 2010, and at between 2-3% thereafter.

Owing to a remarkably strong performance during the first part of 2008, **palace hotels** still posted a 3% increase in RevPAR in 2008 compared to 2007, despite the slowdown in occupancy in the second half of the year. However, the crisis did catch up with the most luxurious hotels in the market in 2009. As a result of both occupancy and average rate decreases for palace hotels, there was a 20% decline in RevPAR on the previous year. Improvements in performance in the fourth quarter of 2010 were reflected in an overall annual increase in RevPAR of 11%, which still left this hotel category trading at an 8% discount on RevPAR compared to 2007. The recovery in occupancy for the palace hotels is likely to be bumpier, as the market absorbs the new supply mentioned earlier. In terms of average rate, we have forecast an increase of 5% in 2011 (slightly below the increase in 2010) as the new supply gains market share, and at around 2-3% thereafter.

FIGURE 9: PALACE HOTELS PERFORMANCE

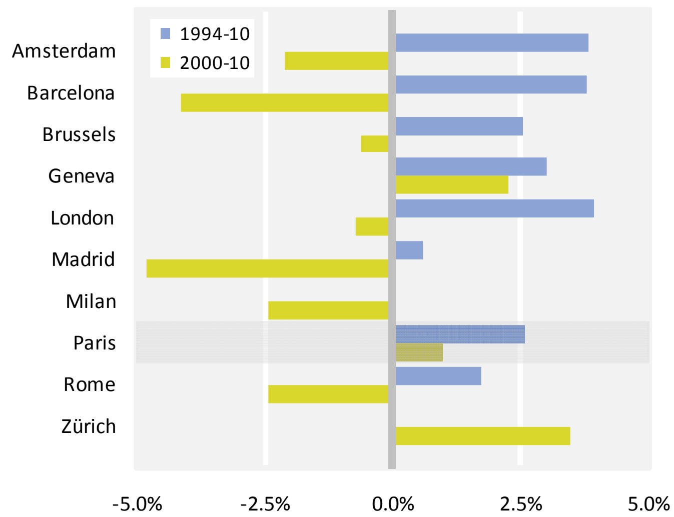


Source: STR Global and HVS

Investment Environment

In our latest European Hotel Valuation Index report, Paris was again ranked first, a position it has held since 2008. **Values per room** stood at €568,800, a 4.0% increase on last year (see Figure 10). Hotels in the French capital experienced a decrease in value of 3.6% in 2009, far smaller than the European average of 13.4%. The 2010 increase of 4.0% is also higher than the European average increase of 1.5%, hence further distancing Paris on the index from other markets in Europe. Given its strong fundamentals and recent hotel performance, we expect a continued recovery in values per room in Paris hotels over the next five years, to approximately €650,000 a room by 2015. High barriers to entry, broad seasonality and a strategic location, amongst other advantages, will continue to benefit the hotel market in Paris.

FIGURE 10: VALUE CHANGES IN THE MAIN EUROPEAN MARKETS



Source: HVS European Hotel Valuation Index 2011

Hotel ownership has become an international investment opportunity. This is clearly demonstrated by the purchase of trophy assets across Paris and London by private individuals and funds. The most noteworthy **single asset transactions** in 2010 were the sale by Starwood Capital of two Parisian landmarks: the 147-room Hotel de Crillon (€250 million) and 230-room Hotel Lutetia (€145 million). The Hotel de Crillon was bought by Saudi investors and is to be reflagged as a Kempinski. It is currently undergoing renovation. The Hotel Lutetia was acquired by Alrov Group, which will retain Concorde Hotels as the operator. Alrov owns several luxury hotels including The David Citadel Hotel and The Mamilla Hotel in Jerusalem, and is developing the Conservatorium Hotel in Amsterdam and the Café Royal in London as luxury hotels. Other transactions were the acquisition of the 118-room Renaissance Arc de Triomphe by Deka Immobilien for €114 million, and the purchase by Algonquin of the 150-room Courtyard by Marriott Paris Saint-Denis, for which the price was not disclosed. The most note-worthy sale in 2011 has so far been the sale of the 192-room Marriott Champs Elysees by Union Investment Real Estate to an undisclosed buyer for €215 million.

The volume of **portfolio sales**, rather than single asset deals, in 2010 was around €3.2 billion, almost triple the level of 2009. The most significant transaction in France was Carlyle Group's acquisition of the B&B hotel group – 223 hotels with more than 16,000 rooms – for €480 million. These hotels are located in France, Germany and Italy. Accor was active in the sale-and-leaseback market, selling five hotels to Invesco Real Estate for €154 million and a portfolio of 48 hotels across Europe to a joint venture between Foncière des Murs and Predica. The value of the transaction was €367 million, and 32 of these hotels are located in France.

France remained one of the most active hotel investment markets in 2010, with a total volume of around €772 million, behind the UK (€1.9 billion) and Scandinavia (€1.2 billion) but ahead of Spain (€680 million) and Germany (almost €200 million).

Conclusions

As highlighted by this brief overview, the fundamentals in the Paris hotel market remain exceptionally healthy, with moderate but sustained demand growth, broad seasonality and overall limited supply increases (except within the palace hotels in the short term). Its strategic geographical location and the wealth of tourist attractions and corporate headquarters in the city make it attractive to both business and leisure travellers, and its resilient performance throughout the depth of the economic recession ensures that the interest from the investment community for assets in Paris is likely to remain robust for many years to come.

About HVS

HVS is the world's leading consulting and services organisation focused on the hotel, restaurant, shared ownership, gaming, and leisure industries. Established in 1980, the company performs more than 2,000 assignments per year and clients include virtually every major industry participant. HVS principals are regarded as the leading professionals in their respective regions of the globe. Through a worldwide network of 30 offices staffed by more than 300 seasoned industry professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. For further information regarding our expertise and specifics about our services, please visit www.hvs.com.

With offices in London since 1990, **HVS London** serves clients with interests in the UK, Europe, the Middle East and Africa (EMEA). We have appraised almost 4,000 hotels or projects in 50 countries in all major markets within the EMEA region for leading hotel companies, hotel owners and developers, investment groups and banks. Known as one of the foremost providers of hotel valuations and feasibility studies, and for our ability, experience and relationships throughout Europe, HVS London is on the valuation panels of numerous top international banks which finance hotels and portfolios. We have appraised more than 50 hotels in Paris and others in Cannes, Lille, Lyon, Marseille, Montpellier, Nice, Toulouse, Strasbourg and other main French cities.

About the Author

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