South Korea Overview | Focus: Seoul Hotel Market

South Korea Tourism Overview

Korea is a popular tourist destination for Japanese and Chinese visitors, which both combined account for almost 60% of total international visitors in 2015. The geographic proximity and attractive tourism offerings cater to short getaway visits, particularly the capital city Seoul.

The Korean tourism industry is driven by the cultural trend called ‘Hallyu’ or Korean wave. Starting from popular media including performing K-Pop artists and TV dramas gradually spread to industries such as cosmetics, food, electronics, etc. According to the Korea Foundation for International Culture Exchange (KOFICE), the Korean wave effect on production inducement was estimated to be approximately, KRW 15.6 trillion (USD 14bn) in 2015.

Among the numerous regional tourism destinations, Korea consistently ranks within top 5 destinations for Chinese travelers for the last 3 years.

The Korean peninsula protrudes into the sea between China and Japan. The west coast of the Korean Peninsula is bound by the Korea Bay to the north and the Yellow Sea to the south; the east coast is bounded by the East Sea. Two hundred kilometres of open water separate the peninsula from eastern China. The Japanese islands of Honshu and Kyushu are located 206 km to the southeast.

The total area, including the surrounding islands, measures 99,720 km², of which about 99% (96,920 km²) constitute the land area of the Republic of Korea. There are about 3,000 islands belonging to the Republic of Korea. Jeju Island, which lies off the southwestern corner of the peninsula, is the country’s largest island.

The majority of the Korean population of about 50 million does not practice any religion (43.3%), followed by Christian (31.6%) and Buddhist (24.2%).

Visitor Arrivals

Figure 1: Visitor Arrivals 2005-2015
In 2005, South Korea recorded total international visitors of 6.0 million. The majority of international visitors were Japanese at 2.4 million which accounts approximately 40% of the total international visitor arrivals, followed by China and the US at 11% and 9%. While total international visitor arrivals increased in subsequent years, Japanese visitation levels decreased at a compound annual growth rate (CAGR) of 19.5% between 2012 and 2015 due to an unfavourable exchange rate between the Korean Won and Japanese Yen. However, following the easing of visa restrictions for mainland Chinese, the Chinese market registered very strong growth, more than compensating for the decline in Japanese visitors further boosting the local tourism industry.

**Figure 2: Currency and Japanese Visitors to Korea**

Figure 2 illustrates the correlation between Japanese Yen over Korean Won and Japanese visitors to Korea. Since Shinzo Abe was elected as the prime minister of Japan in 2012, the government implemented the policy called “Abenomics” to boost the domestic demand and gross domestic product by monetary easing and structural reform. The policy resulted in an unfavourable exchange rate for Japanese visitor to Korea, limiting the number of tourist arrivals.

**MERS Outbreak in 2015**

In May 2015, Korea experienced the outbreak of Middle East Respiratory Syndrome (MERS) which led to the death of 38 people and negatively impacted the Korean tourism industry. During the MERS outbreak, from June to August, South Korea recorded a significant YoY drop in foreign visitors of 40%, compared to a 12.4% YoY increase for the same period in 2014. July 2015, the worst of the three months, registered a 53.5% YoY drop.

**Recovery from MERS**

Figure 3: Visitor Arrivals 2005-2016 YTD August

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**Recovery from MERS**
Due to the government support and promotion such as President Park visiting China for military parade commemorating the defeat of Japan after World War II and advancing the dates for the Korea Grand Sale, to October 2015, the decline in inbound tourism was reversed, reaching 3.65 Million visitors for the last quarter of 2015. From January to May 2016, Korea recorded a YoY increase of 10.6%, while June to August registered an increase of 100.9% over 2015 and 20.6% over 2014, showing a healthy growth and full recovery.

**Other risks in Korea (Political)**

The Korean peninsula is politically divided into two nations, the Democratic People’s Republic of Korea (North Korea) and the Republic of Korea (South Korea). 63 years after the hostilities of the Korean war ended, no peace agreement has been reached and both countries are only in a ceasefire, leading to military and political risks between the two and neighbouring countries. Following a series of nuclear weapons test and missile launches, South Korea together with its US allies agreed to deploy the Terminal High Altitude Area Defense (‘THAAD’) Missile system in 2016. The deployment was strongly objected to by the Chinese government as THAAD’s radar called TPY-2 has a range of 2,000 km, posing a threat to Chinese national security.

**What does it mean to Tourism Industry?**

The South Korean tourism industry depends heavily on Chinese tourists. In 2015, approximately 6 million Chinese visitors visited Korea which accounts roughly 45% out of all international arrivals. Considering China’s track record for economic retaliation to Korea during the ‘Garlic War’ in 2000, there is a downside risk in the exercise of soft power. At the time the Chinese government banned importing polyethylene and mobile phones from South Korea as and act of economic retaliation when South Korea increased the tariff on imported Garlic.
from China to safeguard the Korean agriculture.

Similar to the Garlic incident, the THAAD crisis is expected to have a negative effect on the Korea tourism industry. Subsequent to the THAAD deployment decision, China started strengthening regulation about Korean media content in China and applied more strict standards toward Korean cosmetics. Decreased access to the Chinese market can negatively impact visitor arrivals. More imminent, according to the local press\(^1\), the China central government unofficially gave instructions to major provinces such as Shanghai, Guangzhou, Tianjin and others for travel agencies to reduce the number of group tourists by 20\% by restricting travel package sales.

**Focus Market: Seoul, Capital of Korea**

Seoul is the capital and largest city of South Korea. At a population of more than 10 million, the city is home to over one-fifth of the South Korean population. Seoul is the heart of the country’s economy, politics and culture with a rich history spanning 600 years.

Due to the convenient air access and competitiveness of Korean air carriers, Seoul has been the main benefactor of the ‘Korean wave’ phenomenon, welcoming the majority of tourists to the country.

The city is served by two main airports, **Incheon International Airport** and **Gimpo Airport**. Incheon International Airport opened in early 2001, replacing the international function of the old Gimpo Airport. The Incheon International Airport serves as the national hub for international arrivals, currently serviced by 69 airlines, offering connectivity to more than 160 destinations worldwide with annual capacity of 44 million passengers. Incheon airport is also directly connected to the domestic High Speed Rail System KTX, providing access to all major cities in the country. **Gimpo Airport** connects the city to mostly domestic destinations and five major cities in East Asia that are located within a range of 2,000 kilometres - Beijing, Shanghai, Taipei, Osaka and Tokyo. The airport is currently served by five domestic airlines and six international airlines, namely All Nippon Airways, Japan Airlines, China Eastern, China Southern Airlines, Shanghai Airlines and Eva Air with an annual capacity of 34.7 million passengers.

**Hotel Performance in Seoul**
Despite increasing visitor arrivals, occupancy and average rates slightly decreased since 2013 due to the decline in the high-spending Japanese source market and increase in supply around Seoul. Although the number of Chinese visitors increased rapidly, the majority are tour groups, opting to stay in more affordable accommodations in the outskirts of Seoul. Thus, both occupancy and average rate were negatively impacted in 2014 and 2015. Moreover, in 2015, the MERS outbreak had a major negative impact on both occupancy and average rate for a three-month period. For 2016, we forecast a recovery in occupancy levels as the market normalizes during the summer months affected by MERS in 2015. However, average rate remains under pressure, as operators applied value-based pricing policies to stimulate demand on the back of MERS and facing new supply entering the market.

Comparing performance across the segments, the Super Deluxe segment continuously decreased average rate from KRW 222,400 to KRW 196,500 while maintaining the occupancy at average of 70.5% from 2013 to 2015, reflective of the decline in the Japanese visitor arrivals. The Deluxe segment showed a similar pattern but with more fluctuation in occupancy, relying more heavily on leisure travellers. Deluxe hotels’ average rates declined from KRW 118,400 to KRW 108,200 and occupancy declined from 80% in 2013 to 70% in 2015. The First Class hotels’ average rate remained relatively stable compared to the other two segments however, the occupancy level showed a different trend with a peak at 70% in 2014 and 2013 and 2015 closer to the 60%-mark. All segments are showing a recovery in occupancy levels in 2016, however rebuilding average rate will take a longer time, challenged by the change in visitor arrival mix.

**Conclusion**

South Korea is one of popular tourist destinations for regional travellers in Asia and Seoul is the pulse of the Korean tourism industry. However, due to the consecutive decrease in high spending Japanese source market since 2012 combined with unfavourable event such as MERS, Seoul was unable to push the overall average room rate upwards.

Despite the historical performance shown in Figure 6, the hotel performance in Seoul is projected to gradually improve as the Japanese Yen slowly strengthens compared to the Korean Won bringing Japanese tourists back to Seoul in the medium-to-long term, which will also be a positive sign for new hotel development opportunities in the Deluxe segments. On the other hand, although the Chinese visitor arrivals show healthy growth, the growth does not directly benefit the Seoul hotel market performance as the Chinese tourists are price oriented and together with the political tension between South Korea and China, a careful observation in the Chinese tourism market is needed.

Ultimately, the locational focus of the tourism traveller and high attraction value of the Myeongdong area
concentrates leisure demand to a relatively small area of Seoul. Opportunities for developments in other parts of the city remain, yet those require tailored positioning strategies and business models to cater to local demand.

Footnote:


About Daniel J Voellm

Daniel J Voellm, Managing Partner HVS Asia-Pacific, is based in Hong Kong and has provided advice in all major markets across 23 countries and territories in the region. Daniel Voellm started his career at HVS in the New York office; as Vice President at the global headquarters, he conducted a wide range of appraisals and market studies as well as underwriting due diligence services in 22 US states and in Canada. Daniel brings a strong understanding of the hospitality industry to HVS. His experience in hotel and food and beverage operations in Germany, Switzerland, England and the USA is complemented by an Honours Bachelor of Science degree from Ecole Hôtelière de Lausanne in Switzerland. Daniel works closely with key institutional and private owners of hotel properties, financiers, developers and investors, and has gained a strong understanding of their investment requirements and approaches to assessing the market value of investment properties. Daniel further advises on property and concept development and strategy. For more information please contact, [email protected]