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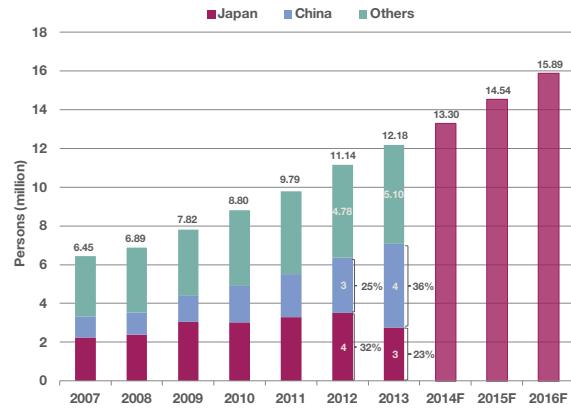
Savills World Research
Korea

Asian Cities Report **Seoul Hospitality**

1H 2014

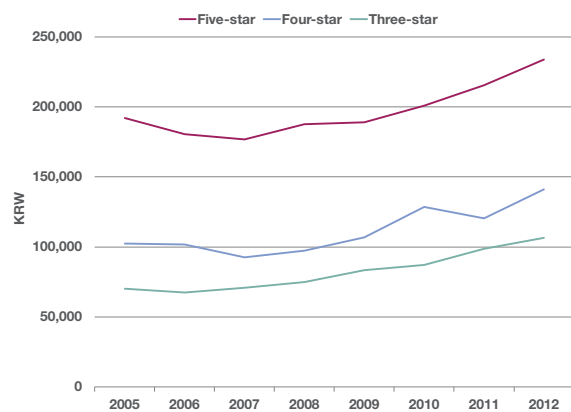


GRAPH 1
Overseas tourists and countries of origin, 2007–2016F



Source: Savills Korea Research & Consultancy

GRAPH 2
Average daily room rates, 2005–2012



Source: Korea Culture and Tourism Institute (KCTI)

GRAPH 3
Occupancy rates, 2007–2012



Source: KCTI

Tourism in Korea

The number of international visitors has increased by an average of 11.2% per annum since 2007, reaching over 10 million for the first time in 2012. This trend has continued and international visitor arrivals recorded an historical high in 2013 at 12.2 million, up 9.3% from the previous year. Compared with 2007, almost double the number of international visitors who arrived in Korea in 2013.

Korea's K-pop culture, Korean Wave, beauty and health services, cuisine, and shopping are the key attractions for international visitors.

The Korean travel industry is highly dependent on Japanese and Chinese tourists, and together they account for about 60% of total international visitors. Before 2013, the number of Japanese visitors grew steadily. However, in 2013, Japanese visitor arrivals declined by 22% due to the weakness of the Japanese yen and political conflict between Korea and Japan.

In the meantime, the number of Chinese visitors rose by 52.5%, exceeding the number of Japanese visitors in 2013. While Japanese visitors prefer free independent travel, Chinese tourists tend to visit Korea with low-priced package tour groups. In 2013, Chinese visitors accounted for 35.5% of total international visitors, followed by Japan (22.6%) and the US (5.9%).

Seoul hotel market overview

As of 2013, statistics showed that there were 177 hotels with 28,468 rooms in Seoul, an increase of 11% compared with 2012. By grade, five-star hotel rooms account for 36%, and four-star hotels for 23% of total hotel stock in Seoul. Therefore, the proportion of existing Seoul hotel room inventory is highly weighted towards upscale hotels.

Seoul hotel performance

According to statistics from the Korea Hotel Association, total revenue of hotels in Seoul was KRW2.13 trillion in 2012, an increase of 11.2% from the previous year.

In 2012, room revenue reached KRW1.08 trillion (51%), while other service revenue stood at KRW1.05 trillion (49%). However, in five-

star hotels, other service revenue exceeded room revenue by 132%.

Average daily room rates (ADR) have increased since 2009, with an average annual growth rate of 7.8%, and a year-on-year growth of 9.7% from 2011 to 2012. The ADRs for five-star, four-star and three-star hotels stood at KRW233,681, KRW140,991 and KRW106,399 respectively in 2012. By hotel grade, four-star hotels had the highest ADR growth rate at 9.7%, while three-star and five-star hotels grew by 8.5% and 7.4% respectively. Despite four-star hotels having the highest growth rate in ADR, there is still a wide gap between five-star and four-star hotel ADRs.

According to a Hotel Tourism Association study released in 2012, more than 90% of visitors stay in three- to five-star hotels. Hotel room sales are therefore highly dependent on overseas visitors, with 80% of hotel room revenue attributed to overseas customers and 20% to domestic customers. On the other hand, 77% of banquet and restaurant services revenue comes from domestic customers and 23% from overseas customers.

Due to the significant growth in overseas tourist arrivals, demand for hotel rooms rapidly increased, with supply outstripping demand. This pushed occupancy rates up to 83.7% for three-star hotels, 82.7% for four-star hotels and 77.7% for five-star hotels in 2012. As three- to four-star hotels offer more reasonable ADRs, these tend to have higher occupancy rates.

Hotel supply

Between 2012 and 2013, 26 hotels representing 2,758 rooms were added to the Seoul hotel market. The luxury and international brand hotels included Conrad Hotel in Yeouido (434 rooms) and JW Marriot in Dongdaemun (170 rooms), while the limited service hotel brands developed by REITs comprising travel agencies and institutional investors included Aventree in Jongro (155 rooms), CeterMark in Insadong (250 rooms) and T Mark in Myeongdong (288 rooms). In addition, Ninetree (144 rooms) in Myeongdong, a limited service hotel brand developed by Parnas hotel (68% of the total share is owned by GS E&C) opened in 2012.

New supply forecast

There has been a significant increase in hotel development due to high demand and limited supply. In order to expand tourism infrastructure, the government has provided incentives for hotel developments in terms of increased floor area ratios and easing development regulations. According to the Seoul Metropolitan Government, as of Q1/2014, about 120 new projects have received approval permits, and over 19,600 hotel rooms are scheduled to be added to the Seoul hotel market by 2017. In 2014, about 8,000 hotel rooms are approved for new development in Seoul. However, only 85% of planned projects are under construction.

If all scheduled development projects are delivered, supply and demand levels will be in balance in 2016. However, if overseas visitor arrivals continue to grow, a shortage of accommodation is expected in 2017. Meanwhile, there are several large mixed-use development projects in the planning stage and these are expected to include hotel components. As these projects obtain approval from the government, hotel supply levels for the near future will increase from current anticipated levels.

Before hotel development surged in Seoul, luxury high-end hotel rooms accounted for almost 40% of total hotel stock, and overseas tourists had little choice but to pay high ADRs.

Recently, limited service hotels which offer reliable services at reasonable room rates have become popular with international tourists. From an investor's perspective, limited service hotels require less initial investment and have lower operating costs compared with full service hotels. Additionally, since it is possible to develop limited service hotels through the conversion of older existing office buildings, especially if the building is located in a central business district with public transportation networks or a shopping hub, there has been a significant increase in this type of supply.

As interest in hotel investment and development has grown, a range of companies have entered the hotel business and created local hotel brands. The main players in the Seoul hotel market are the luxury

full service hotels owned by Korean conglomerates. However, upcoming new supply largely comprises limited service hotels by local Korean brands and international budget hotel brands.

Korean conglomerates, which already have a presence in the hotel market, have launched limited service hotel brands and are aggressively expanding their business lines. These include Shilla Hotel (owned by Samsung) launching Shilla Stay, Lotte Hotel (owned by Lotte) launching Lotte City Hotel and Parnas Hotel (owned by GS) opening NineTree, while both Chosun Hotel (owned by Shinsegae) and Walkerhill Hotel (owned by SK Networks) are preparing to launch their own brands. In order to expand their market share at the initial stage, hotel management and operating companies prefer to master lease instead of owning the hotel property. Up to 2016, about 11 limited service hotels by Korean conglomerates (3,500 rooms) are expected to be completed.

In addition to the conglomerates, Hana Tour and Mode Tour (the two Korean tourism agencies with the highest market share), and Daelim Corporation, KT&G, and KT Estate have recently entered the hotel business. As more diverse players participate in the hotel sector, the completion of new hotel supply will escalate.

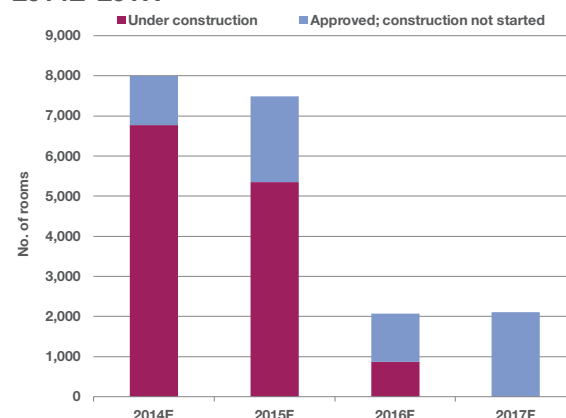
Hotel transactions

Since 2011, the number of REITs investing in hotel property in Korea has grown from zero to six, with a total asset volume of KRW0.9 trillion, accounting for 7.3% of the total REIT volume as of Q4/2013. In 2013, six hotels with 1,888 rooms (306 rooms are under development) were owned by REITs.

Due to the short supply of hotel rooms, operator and investor interest in the hotel sector has grown. Hotel operators with professional know-how and institutional investors with abundant liquidity are forming strategic business partnerships. Investors can expect lower hotel operating risk while hotel operators are able to expand their business portfolios with no initial investment.

The majority of hotel transactions are now completed by REITs and real estate funds. There have also been several transactions occurring before the completion of construction. ■

GRAPH 4
Hotel development construction status, 2014E–2017F



Source: Seoul Metropolitan Government

GRAPH 5
Supply and demand, 2012–2017F



Source: Savills Korea Research & Consultancy, Seoul Metropolitan Government

TABLE 1
Major hotel transactions, 2012–2013

Hotel operator	Year of completion	No. of rooms	Transaction amount (KRW bil)	Amount per room (KRW 100 mil)	Investor
Shilla Stay (Mapo)	2015	387	117	3.0	Hana Asset Management
Sheraton D-Cube (Guro)	2011	269	140	5.2	JR AMC
Lotte City Hotel (Janggyo)	2015	435	140	3.2	KDB AMC
Shilla Stay (Shindaebang)	2015	313	68	2.2	Richmond AMC
Ibis Ambassador (Jongro)	2013	363	75	2.1	Richmond AMC
Shilla Stay (Dongtan)	2013	286	100	3.5	National Pension Service

Source: Savills Korea Research & Consultancy prepared with public information

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