

New Zealand Hotel Performance and Profitability

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Horwath HTL Limited

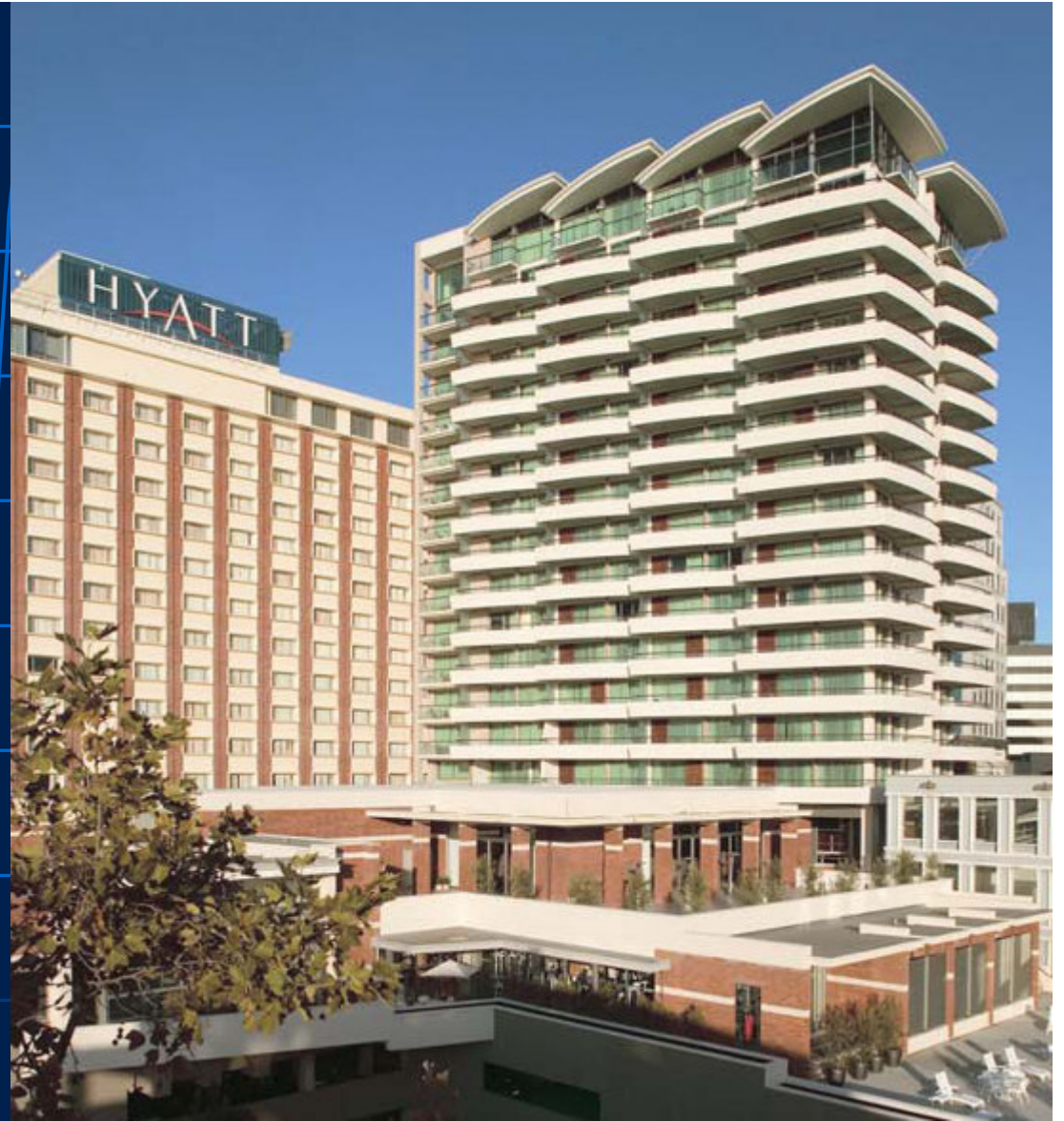
Outline

- Required rate of return
- New hotel development cost
- Hotel investment
- Profitability to generate required rate of return
- Revenue required to generate profit required
- Room rate required to generate revenue required
- Medium term room rate movements and construction cost index
- Visitor outlook
- Rooms required outlook
- Hotel investment required
- Conclusions



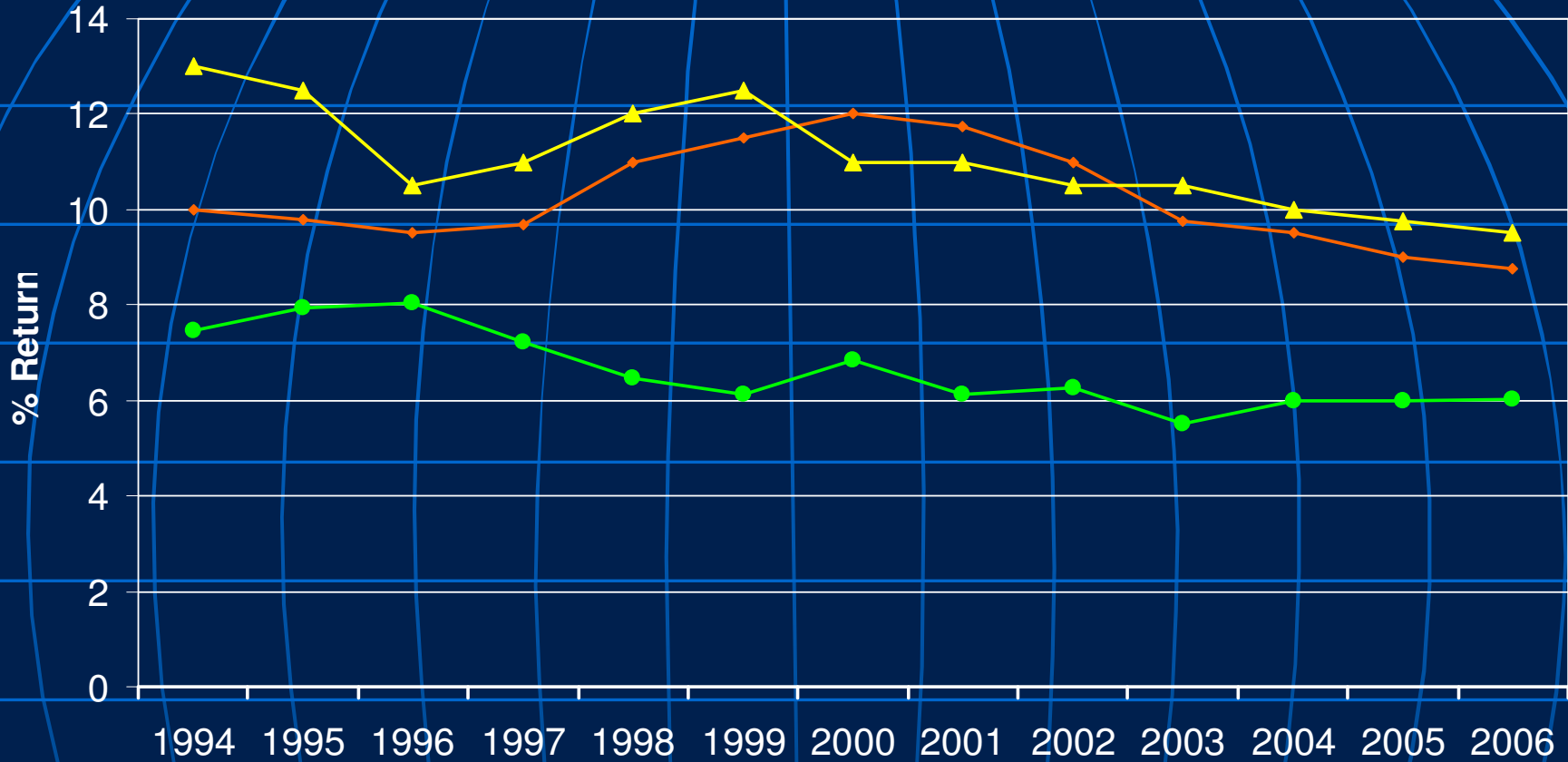
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Required rate of return



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Rate of Return on Investments



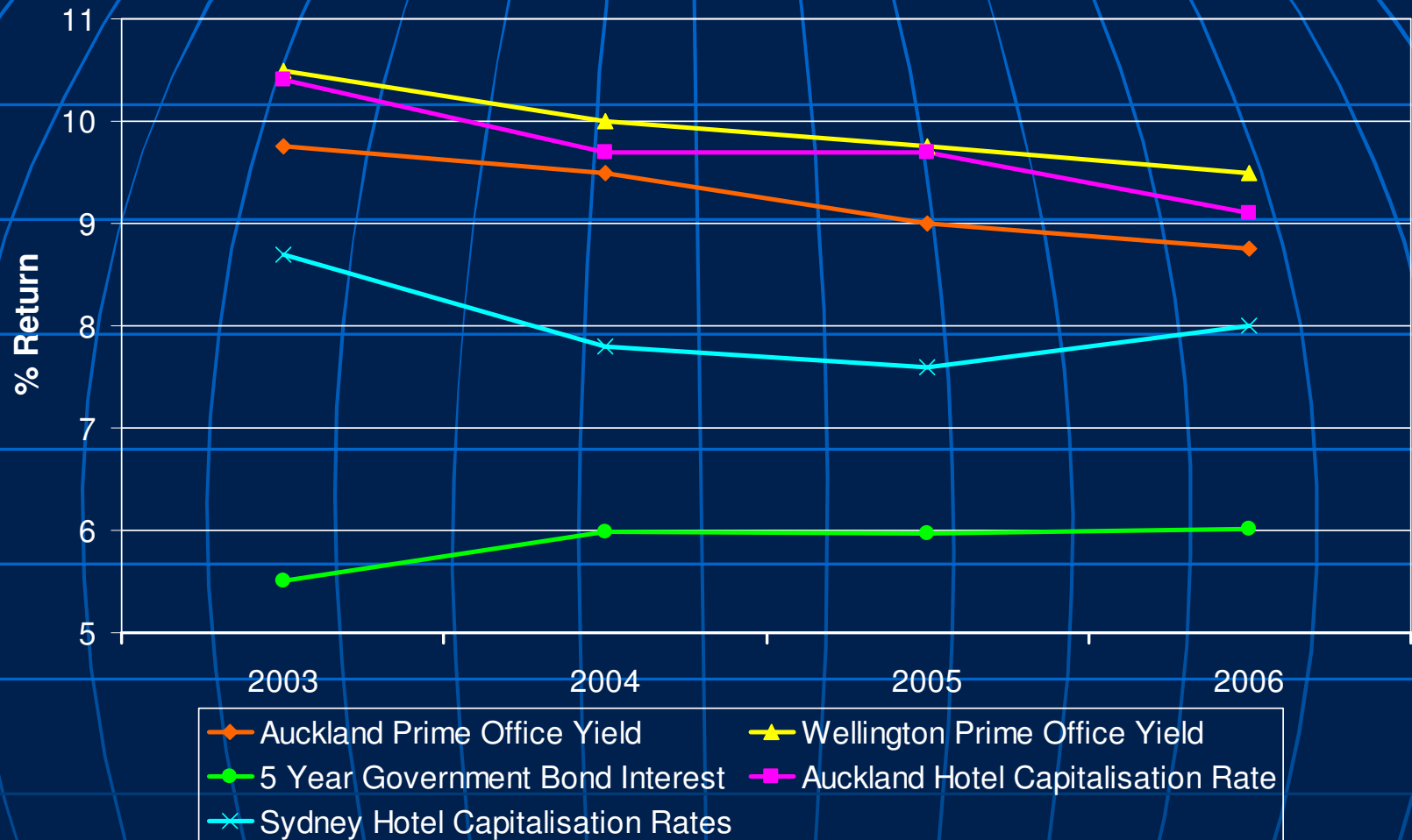
—◆— Auckland Prime Office Yield —▲— Wellington Prime Office Yield —●— 5 Year Government Bond Yield

(Source: CB Richard Ellis, RBNZ)



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Hotel Investor Survey of Capitalisation Rates



(Source: CBRE, RBNZ, Sonnenblick-Goldman Company
2006 Australia, NZ & Pacific Hotel Industry Survey of Investors)



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What is the Required ROI for Hotels?

	Return on Investment %
5 Year Government Bond Yield	6.00
ANZ 5 Year Term Deposit Rate	7.50
Auckland Prime Office Yield	8.75
Bridgecorp 5 Year Deposit Rate	9.25
MFS Pacific 5 Year Deposit Rate	9.25
Wellington Prime Office Yield	9.50
Existing Hotel (IRR)	7.50 – 10.00
New Hotel (Yr 5 stabilised)	10.00 – 13.00

(Source: RBNZ, CBRE, Horwath HTL Market Research, other websites)



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Hotel Construction Costs

- Construction costs for non-residential buildings have been escalating rapidly since 2001, and is forecast to increase on average by 4.4% pa

(Source: NZIER)

- Construction costs have been growing at a faster rate than room rates and hotel profitability

- making new hotel feasibility an increasing challenge

- Australian developers are also experiencing the same problem

(Source: Jones Lang LaSalle Hotels)



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Hotel Investment – New vs Existing

New Hotels

- escalating construction costs
- escalating price of land in key desirable locations
- competition from existing hotels who do not have same pressure to raise ADRs
- few new opportunities to “lead” the market – therefore more likely to be price takers
- best opportunities in boutique hotels in prime locations

Existing Hotels

- better information re existing performance and potential for performance improvement opportunities
- opportunity for capital gain
- potential for vacant possession
- purchase prices are at a discount to replacement cost
- as ADRs rise, purchase prices may rise and yields fall further



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Profitability target required to justify new hotel investment



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Profit target for Required ROI new 3* – 4* hotel

- Required return on investment 13%

Assumptions for a new 3* – 4* hotel in NZ:

- Development cost per room \$222,300
- Average size of hotel 230 rooms
- Development cost \$51 million
- Profitability required \$6.6 million



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Revenue Target to Generate Required Profit new 3* – 4* hotel

- Required profit \$6.6 million
- Assumed Net Operating Profit ratio 30%
(after management fees, FF&E, rates,
insurance and owners costs)
- Revenue required to achieve
\$6.6 million annual profit \$22.2 million



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ADR Target to Generate Required Revenue new 3* – 4* hotel

- Revenue required \$22.2 million

Assumptions for a 3* - 4* hotel in NZ:

- Average Occupancy Rate 75%
- Rooms Revenue is 63% of Total Revenue
- ADR required to achieve
\$22.2 million Total Revenue \$221.69
- NZHC 3* - 4* ADR y/e April 2007 \$118.34
(53% of target ADR)



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Profit Target for Required ROI new 4½* - 5* hotel

- Required return on investment = 13%

Assumptions for a 4½* - 5* hotel in NZ:

- Development cost per room \$363,750
- Average size of hotel 180 rooms
- Development cost \$65 million

Profitability required \$8.5 million



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Revenue Target to Generate Required Profit for a new 4½* – 5* hotel

- Required profit \$8.5 million
- Assumed Net Operating Profit ratio 27%
(after management fees, FF&E, rates,
insurance and owners costs)
- Revenue required per year to achieve
\$8.5 million annual profit \$31.5 million



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ADR target to generate Required Revenue new 4½* – 5* hotel

- Revenue required \$31.5 million

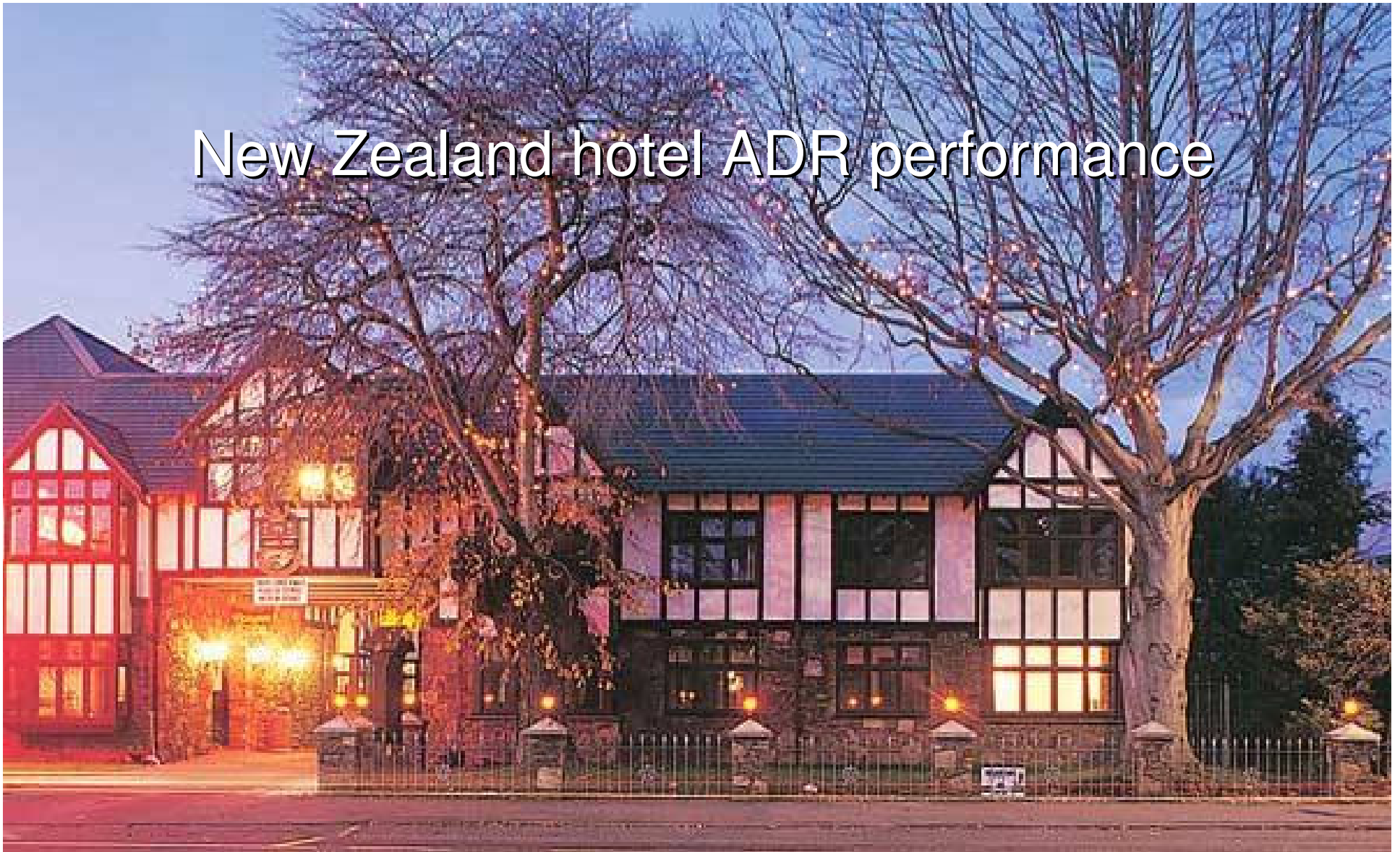
Assumptions for a new 4½* - 5* hotel

- Average Occupancy Rate 70%
- Rooms Revenue is 61% of Total Revenue
- ADR required to achieve
\$31.5 million Total Revenue \$418.14
- NZHC 4½* - 5* ADR in April 2007 \$159.82
(28% of target ADR)



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New Zealand hotel ADR performance



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Average Room Rates in Other Main Cities

Main Centre Markets	Average Daily Room Rate NZD (YE March 2007)
Auckland	150
Sydney	255
Hong Kong	263
Tokyo	268
New York	337
London	342
Paris	349

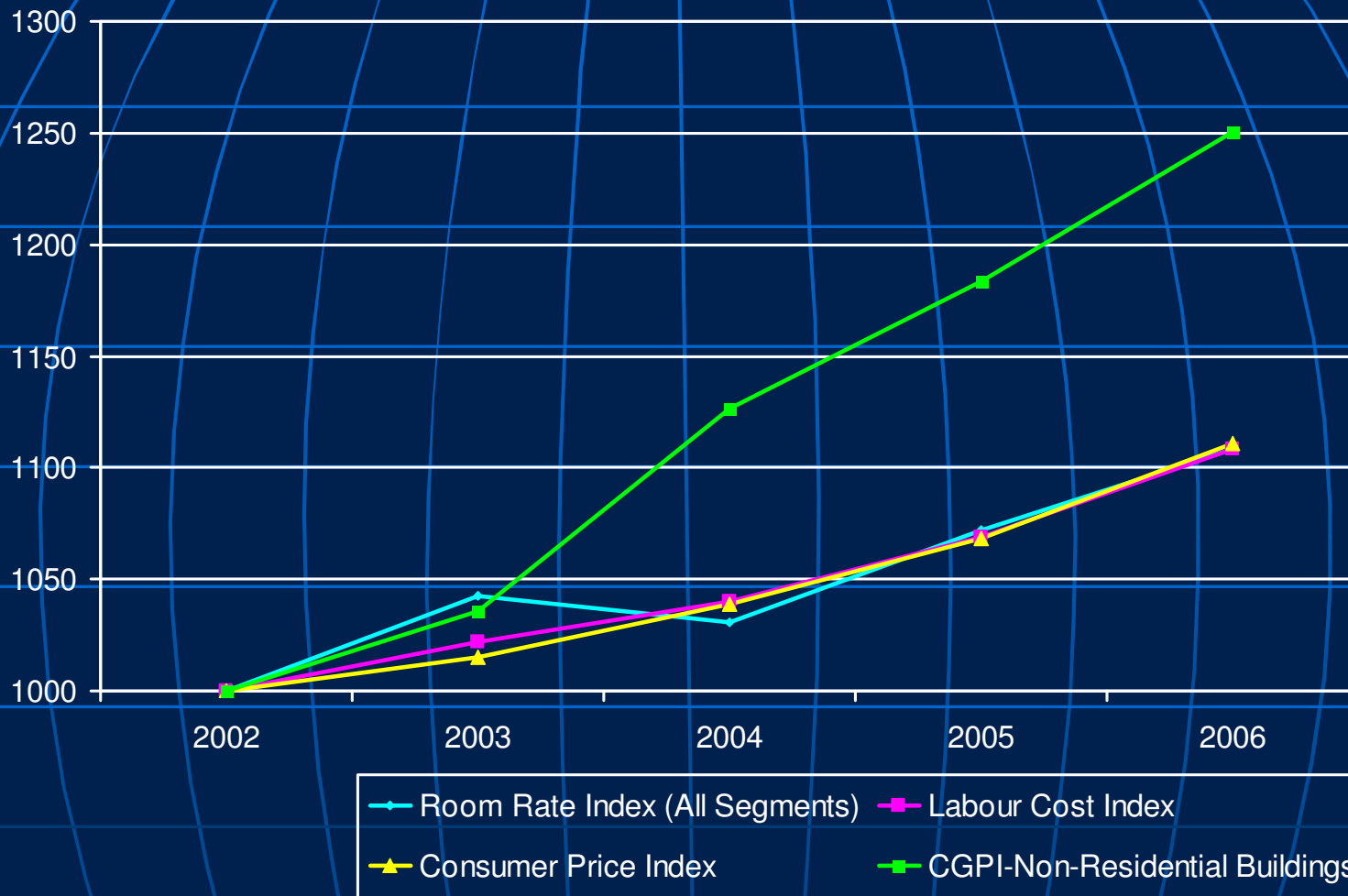
(Source: NZHC, Smith Travel Research, The Bench)

Note: NZ\$1 = US\$0.66, the average exchange rate for 12 months ending March 2007



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Medium Term Cost Index Movements



(Source: Statistics New Zealand, NZHC, Rider Hunt)



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NZ Visitor Forecast to 2015 (Ministry of Tourism)

- International visitor arrivals are projected to increase by 4 - 5% per annum
- Domestic visitor numbers are projected to grow between 0.5% to 2% per annum

	2006 Actual	2015 Forecast
International Visitors	2,421,560	3,529,395 (+46%)
Domestic Visitors	17,368,000	18,818,681 (+8%)



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Visitor Night Forecast

- International visitors stay 19 nights on average
- Domestic visits ALS approximately 3 nights

(000s)	2006 Actual	2015 Forecast
International Nights	46,251	66,353 (+43%)
Domestic Nights	51,583	55,891 (+8%)



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Hotel Guest Night Demand

- 13.5% of international visitor nights and 7.2% of domestic visitor nights were spent in hotels (2006)
- This proportion will grow faster for international visitors than for domestic travelers

	2006 Actual	2015 Forecast
Total Hotel Guest Night Demand	9,958,000	14,680,000 (+47%)



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Hotel Room Night Demand

- Room density:
1.8 international visitors
1.4 domestic visitors

	2006 Actual	2015 Forecast
Total Hotel Room Night Demand	6,180,000	8,944,000 (+45%)



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Required Hotel Room Supply

- New hotel room supply is required in order to meet the projected hotel room night demand
- Compounding annual average growth is 3.7%

	2006 Actual	2015 Forecast
Hotel Room Night Supply	11,227,000	15,517,000 (+38%)
Hotel Room Supply	30,759	42,512 (+38%)



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Required Level of Hotel Investment

- The yearly required level of hotel room supply translated into dollar terms is the yearly required level of new hotel investment
- The current rate of new hotel investment is far from this target

(NZ\$ million)	2007 Forecast	2015 Forecast
Required annual level of new hotel investment	223.2	522.7



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Hotel Occupancy Rate and Seasonality

- In 2006, New Zealand average annual occupancy is 55.0% and is forecast to grow to 57.6% in 2015
- Why can't we simply fill all the existing hotel rooms to meet growth in demand?

Average Occupancy	2006 Actual	2015 Forecast
Summer (Nov – Feb)	61.3%	66.0%
Shoulder (Mar, Apr, Sep, Oct)	56.3%	63.9%
Winter (May – Aug)	47.5%	43.0%



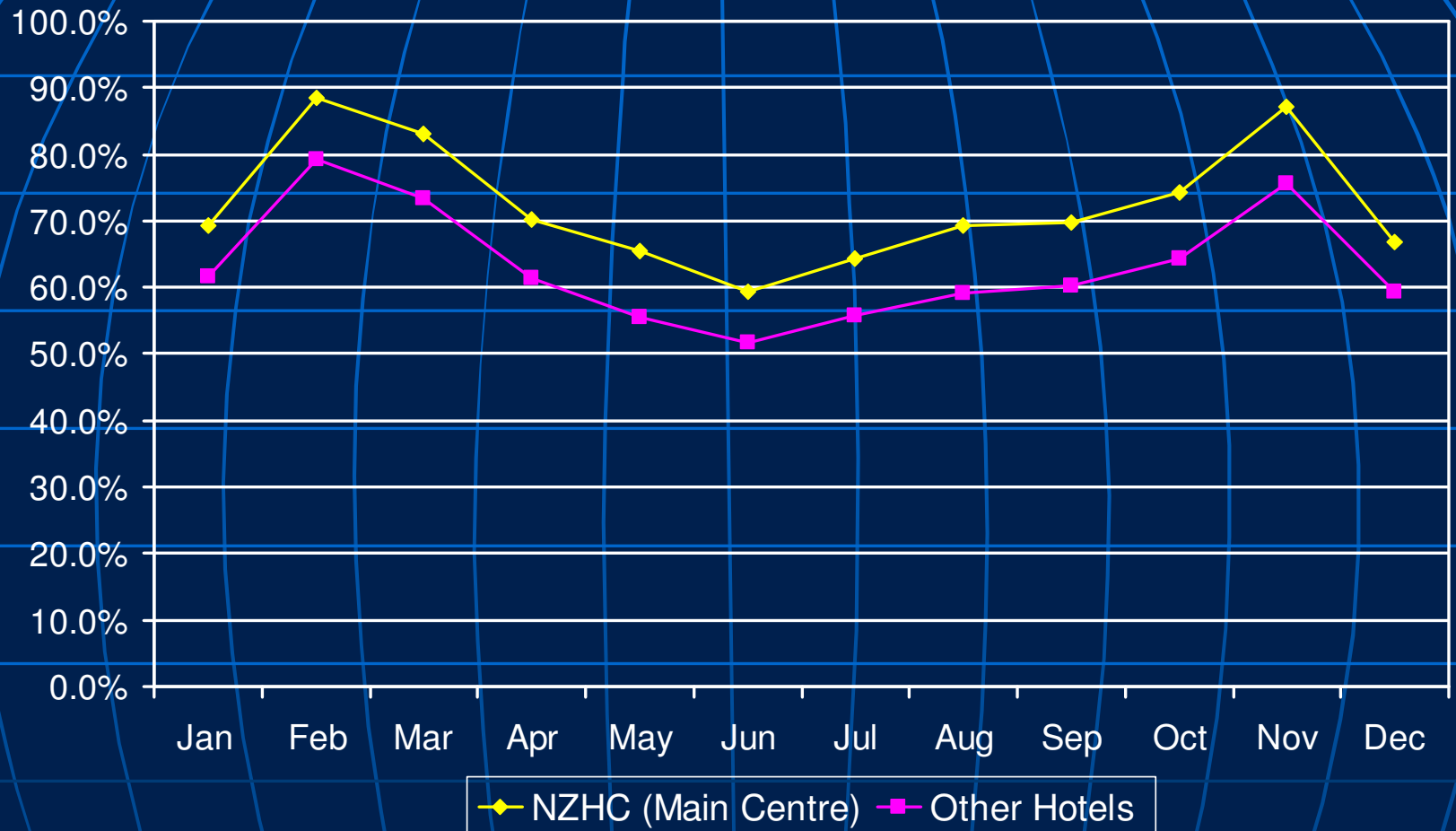
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Seasonality of hotel demand



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Hotel Monthly Occupancy Rates for 2006



(Source: NZHC, Commercial Accommodation Monitor)

Note: NZHC main centres are Auckland, Rotorua, Wellington, Christchurch and Queenstown



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Why is new hotel investment low?

- Low current room rates resulting in low profitability hence low incentive for new investment
- Most owners have acquired existing hotels with discounted passing value and so are making a reasonable return on their investment with the current low room rates
- Existing hotels may believe that raising their room rates could result in losing market share
- However, in order for new investment to be feasible, achievable room rates needs to be much higher



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NZ Hotel Investment – Challenges

- Most new investment is into existing hotels
- Most new developments are currently strata titled
- Profitability generally too low to attract significant new hotel investment – due to low room rates
- Cash yields / ROI need to be higher than lower risk commercial property to attract new investment
- High visitor volumes from lower yielding international visitor markets could deter investors



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Strategies for Growth

- charge significantly higher room rates in summer to compensate for lower occupancy in winter
- focus inbound visitor demand in the shoulder season in particular
- stimulate domestic and international conference demand in the shoulder and winter seasons
- event development
- focus on regional marketing / visitor dispersal during peak and shoulder seasons



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Time's up!



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