Horwath HTL

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LONDON'S SUBMARKETS

London's hotel market has evolved considerably over recent years with the sector expanding into new areas such as the City/Shoreditch, the Docklands, Greenwich, South Bank and other areas of south London which were previously not on the radar screen of many developers/hoteliers/hotel investors.

Is London therefore challenging Conrad Hilton's famous quote: "You need three things for a successful business - location, location, location"?

This article seeks to examine the major new hotel areas in London relative to the traditional prime areas, what makes the market-leading segments outperform others and whether the new areas really are defying this well-known adage.

When London's hotels were first conceived they were originally integrated within or located close to major railway stations, the principal form of transport at the time, in grand and spacious buildings. Central London (West End and Knightsbridge/Victoria), the location of many of the capital's Royal Parks and attractions, was where many of the capital's hotels, including iconic ones such as The Dorchester, The Ritz, The Savoy, Claridges and The Connaught, established themselves. The major tourist attractions, West End retail and Theatreland which are synonymous with this area continue to draw many tourists and as result has been the prime location for hotel development and ownership in the capital.

London's hotel market has now grown outside the established core zone and into virgin areas. This expansion has been influenced by a number of factors, namely:

- The city's evolution itself, which has developed considerably over the last 20 years and in so doing created new demand markets. The most striking example of this is Canary Wharf which replaced the obsolete docks in the early 1990's with a vast swathe of office space and necessitated the subsequent development of hotels to meet the needs of business travellers to this area;

- The scarcity of available sites in the premium West End and city centre has forced developers to look at less obvious locations, pushing the boundaries for London hotel development;

- The facilitation of global travel has had a major impact with passenger movements at Heathrow growing from 39.6m in 1989 to a peak of 69.4m in 2010 so supply has expanded to meet the demand growth;

- The arrival of budget airlines has influenced demand with an influx of many more cost-conscious tourists to the city, altering the underlying demand pattern;

- New segments entering the market such as budget and boutique: The requirement for economy accommodation was answered by the expansion of branded budget hotels such as Travelodge, Premier Inn, Ibis and Etap which were prepared to take on conversions and crucially often fixed-income leases. This was very attractive to the investment market and has enabled them to compete with other traditional real estate classes and outbid other competitors for sites. The arrival of the boutique hotel product in the 1980's, typified by its independence and creativity in design, also had an impact as atypical, smaller or complex floorplates which would not have conformed to the brand standards imposed by the major operators could be converted to hotel use; and

- The advancement of construction practices and availability of buildings for conversion:
  The conversion of existing buildings to hotels is now much more common with certain buildings no longer deemed fit for their current use and becoming obsolete due to modern requirements which has allowed the London hotel market to expand into new areas. Technological advances has meant that it can now be done cost-effectively.

SUBMARKET	REVPAR 12 MONTHS TO MAY 2012 (£)	REVPAR 12 MONTHS TO MAY 2011 (£)	CHANGE
Knightsbridge/Pimlico/Victoria	167.11	161.53	3.45%
West End	162.86	152.25	6.97%
London South	106.17	98.31	7.99%
Paddington/Bayswater	104.34	98.81	5.60%
Earls Court/Kensington/Chelsea	101.32	94.28	7.46%
London North/Camden	97.17	91.67	6.00%
The City/Shoreditch	91.15	88.60	2.88%
Docklands/Greenwich	81.93	79.16	3.50%
Greater London	111.32	105.81	5.20%
Outer London	52.37	49.90	4.96%

Source: STR Global

The table above illustrates the RevPAR performance achieved by a selection of London submarkets in the 12-months to May 2011 and May 2012.

Knightsbridge/Pimlico/Victoria and the West End lead the sample by some distance, achieving RevPAR of £167.11 and £162.86 respectively (150% and 146% of the overall Greater London RevPAR respectively) according to STR Global (the source for all the performance data here). It should be noted that Knightsbridge is the main rate driver in its subset as Pimlico and Victoria remain more volume driven but at a discount to the Knightsbridge market. The vast majority (86%) of the hotels in the two submarkets are from the upscale to luxury end of the market and while achieving occupancy rates in the low 80's, the RevPAR is largely driven by the strong rates that hotels in these subsets achieve. These submarkets crucially contain the Park Lane set which achieves some of the highest ARR's in London and appeals to the ultra-wealthy, including the Arab and Russian markets, many of whom pay close to rack rate during their stays. Furthermore, these sets capture the hotels with the highest suite ratio in the capital which further pushes the rates achieved.

Hotels in Knightsbridge/Pimlico/Victoria and the West End are not only centrally located but where the vast majority of London's leading leisure attractions and high-end retail are situated and as a result have significant appeal to tourists. In fact, for some travellers these areas represent the only places to stay in London.

South London is one of the principal areas which has experienced a wholesale transformation over the last 20 years, kick-started to some extent by the instatement of Waterloo International station, until recently the London terminus of the Eurostar international rail service (now relocated to St Pancras International). The South Bank has undergone substantial expansion and improvement of its image with new attractions popping up all along it - the London Dungeon is now joined by The London Eye, The Tate Modern, Sea Life London Aquarium, The OXO Tower, White Cube Bermondsey and Vinopolis to name a few - and the development of quality office space.

This area of London is now home to a growing number of corporate tenants including accountancy practices, banks, media and advertising agencies who are choosing to be located here.

Development has spread both east and west (from Wandsworth to Tower Bridge) with high-profile new developments such as London Bridge Quarter and The Shard, Europe's tallest building, Embassy Quarter and New Covent Garden Market continuing to improve the area's image. We have also witnessed an improvement in the services which these areas provide with restaurants, bars and retail servicing the growing number of corporate tenants.

As a consequence of the increase in demand generators, we have seen a surge in new branded hotel supply in south London with a mixture of budget, midscale and upscale hoteliers expanding their brands, including Travelodge, Premier Inn, CitizenM, Park Plaza and Hilton. Future entrants to the market include Shangri-La and Mondrian, illustrating its appeal to the upper-end of the market.

The London South area achieved a RevPAR of £106.17 in the 12 months to May 2012 (95% of the overall Greater London RevPAR) and recorded strong RevPAR growth of close to 8% that period. It is interesting to note that this subset enjoys the highest occupancy rates in set in the high 80's, illustrating its strong appeal to both corporate and leisure guests. These high occupancies could also indicate that the demand generators in these areas are growing faster than hotel supply and therefore there is an opportunity for hoteliers to develop here. The mix of midscale and upscale hotels in this subset will have also had a positive impact on the rates achieved.

The City/Shoreditch and Docklands/Greenwich have also seen considerable new branded hotel development in recent years with expansion across all segments of the market. Since the opening of the Four Seasons Canary Wharf, the first true luxury hotel in this area in 1999, upscale and luxury boutique hotel development has become increasingly prevalent.

Prominent hotels which helped to kick-start the regeneration of the area include Threadneedles Hotel, a luxury offering; Malmaison Charterhouse Square; and the Hoxton Hotel which brought chic industrial style at competitive prices to the up-and-coming trendy Hoxton-Shoreditch area. New upscale entrants include the DoubleTree by Hilton Hotel London – Tower of London, Grange Hotel Tower Bridge, The Boundary, Shoreditch House and Apex Temple Court Hotel while future developments Four Seasons Heron Plaza and 10 Trinity Square are set to considerably improve the luxury hotel offering in the area. Likewise, the budget end of the market has experienced significant expansion with Travelodge and Premier Inn being the main promoters/protagonists.

The City/Shoreditch and Docklands/Greenwich achieved RevPAR of £91.15 and £81.93 respectively in the 12 months to May 2012, the lowest of the subsets (achieving 82% and 74% of the overall Greater London RevPAR respectively). Trading levels tend to be strong from Monday to Friday where these areas typically drive good corporate business although weekends are much more challenging due to the more limited leisure activities in the area, the distance from London's main tourist attractions and as some areas of the City become quieter with numerous shops, pubs and cafés shut (although the leisure-driven areas such as St. Pauls, Smithfield and Spitalfields tend to stay open).

Since this area of the city is highly dependent upon corporate demand, Average Rates can vary considerably between weekdays and the weekend, with rate reductions being offered to leisure guests during weekends and holiday times. As result, year-round occupancy is also more challenged. It should also be noted that half of the subset contains hotels from budget to midscale segments which are likely to have had a downward impact on rates achieved.

So why are these areas of the capital becoming increasingly appealing to hoteliers?

Over recent years, the City and East London have expanded into popular locations for international organisations as the capital has grown and West End office space has been sold at a premium, forcing corporates to consider new areas in their search for cheaper business premises.

Canary Wharf kick-started this regeneration and has now become one of Europe's largest clusters of skyscrapers while Excel London, a major exhibitions and conference centre and an increase in the number of large-scale new office developments in the City such as Heron Tower, 30 St. Mary Axe and Broadgate Tower have further attracted major corporations and thus driven demand for hotels. We are also witnessing new corporate locations in East London emerging such as Tech City (dubbed 'Silicon Roundabout') which is becoming a major new hub for media agencies and technology firms with a digital slant, in an area incorporating Shoreditch, Hoxton and Old Street.

At the same time we have seen improved transport connections in the east with the growth of Stansted and City Airports in particular, facilitating access to the area. Crucially, along with the increase in corporate demand generators, the city has become more diverse with a notable increase in services available in the City/Shoreditch: the retail offer has improved significantly and new restaurants, bars, nightclubs and cinemas have sprung up extending the city workers' time spent in the vicinity from traditional 9am to 5pm to 11pm and beyond.

Moreover, this wholesale rejuvenation includes new residential developments which have taken shape around the City over the last 10 to 15 years and as a result these areas have now become acceptable and potentially even aspirational places in which to live, work and play. This regeneration of the east of London has also been accelerated in the build-up to the London 2012 Olympics.

Attractions north of the river such as St Paul's Cathedral, the Tower of London and Tower Bridge continue to appeal to a significant number of leisure tourists while areas on the City fringe such as Smithfield and Spitalfields markets have become popular weekend tourist destinations.

Further south in Greenwich, the O2 Arena, the world's busiest music arena has further enhanced the area's appeal. However, attractions such as the O2 Arena, National Maritime Museum, Royal Observatory and Old Royal Naval College, are more likely to appeal to tourists for a day trip and those that do stay in the local area are likely to expect a rate discount. It is not envisaged that this trend will change in the short-term.

In addition, we anticipate that the rate differential between weekdays and weekends will remain significant in these two subsets and much more than with the other London submarkets due to the nature of demand. Nonetheless, the City/Shoreditch and Docklands/Greenwich are still emerging and therefore occupancy is likely to grow rate further.

It is evident that Knightsbridge and the West End are likely to continue to be the Capital's hotel market-leaders for some time to come and it will consequently be difficult for new areas to attract clientele away from these hotels.

"Location, location, location" is still paramount for hotels but as new areas have evolved within London, these districts have gained prominence changing the perception of prime locations in London.
The dynamics of the city itself will continue to influence hotel guests since London is one of the world's largest cities and takes a long time to cross, resulting in a preference by guests to be located within close proximity of the main areas where they will be spending the bulk of their time. The growing number of major connecting points (City Airport, St. Pancras International, London Paddington and London Victoria) has facilitated this and it is now possible for tourists to be accommodated in the areas where they embark and where the core of their activities in London are taking place.

It will therefore be interesting to see which districts will grow in popularity in the coming years with future potential contenders such as north London and Midtown high on the list.

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