

Covid-19 Impact & Pathway to Recovery

Hotel Market Update May 2020
Colliers International

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Introduction

The Covid-19 pandemic is having a profound impact on the global tourism and hotel sector. It will likely reshape the way our industry operates for many years, ultimately redefining the short stay accommodation sector as we know it.

There is no doubt there will be some casualties in our sector as owners and operators establish whether they can efficiently run their businesses in this new post Covid-19 era. However, this will also create opportunities for others who can quickly adapt and adopt new strategies in the marketplace.

New Zealand will remain reliant to some degree on how global markets emerge from this pandemic and so we will need to adopt a 'holding pattern' until clear trends emerge.

However, there are a range of initiatives we can immediately implement that will prepare us for changes in the marketplace that will inevitably happen.

At the date of this report, New Zealand is one of the first countries globally to effectively control the virus. This will allow us to adopt a range of early demand led initiatives including a comprehensive domestic tourism drive led by Tourism NZ, the possibility of a trans-Tasman and/or South Pacific bubble and bi-lateral tourism partnerships with other countries who have the virus at manageable levels.

Other initiatives include the early hosting of global sporting and cultural events such as the America's Cup and APEC that are both still scheduled for 2021.

New Zealand has a unique opportunity to be an ideal testing ground for many tourism-focussed initiatives and become a benchmark and market leader in the 'Road to Recovery' for the global tourism sector.

In this report, we outline some of the key impacts the pandemic has had to date and provide our outlook on what the post Covid-19 recovery process may look like for the New Zealand hotel sector.



Impact on Demand & Performance

Demand

New Zealand took its first steps to prevent the spread of the virus with border restrictions on passengers travelling from mainland China on 3 February, followed by restrictions on travellers from Iran and northern Italy over subsequent weeks.

New Zealand then closed its international borders on 20 March followed by a five-week nationwide lockdown that concluded on 28 April.

Since then we have seen a staged re-opening of our economy in line with rapidly declining virus cases, although our international borders remain closed. The exception being returning New Zealand citizens and residents who face a 14-day mandatory isolation period in designated hotels.

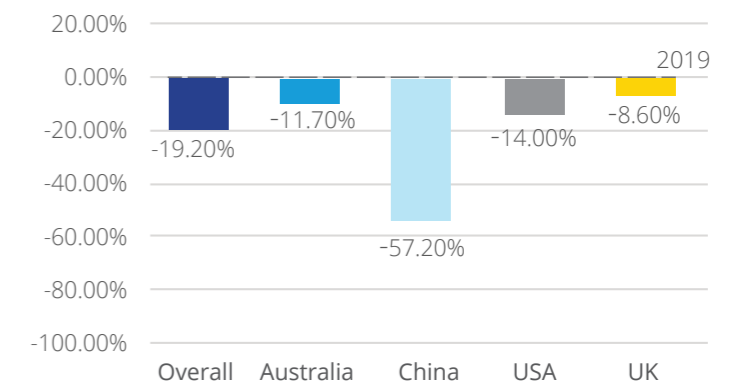
The result of these measures is a significant reduction in inbound demand with airline capacity in late April having shrunk from circa 600 to just 30 flights per week.

We highlight below key international arrivals to New Zealand in the first quarter of 2020.

Based on anecdotal evidence, it is likely the 4 million international visitors forecast by MBIE for 2020, will shrink by a minimum of 50% by the end of the 2020 calendar year.

Domestic demand has also been significantly compromised with full travel restrictions in place until 14 May 2020.

International Visitor Arrivals YTD 29 March 2020



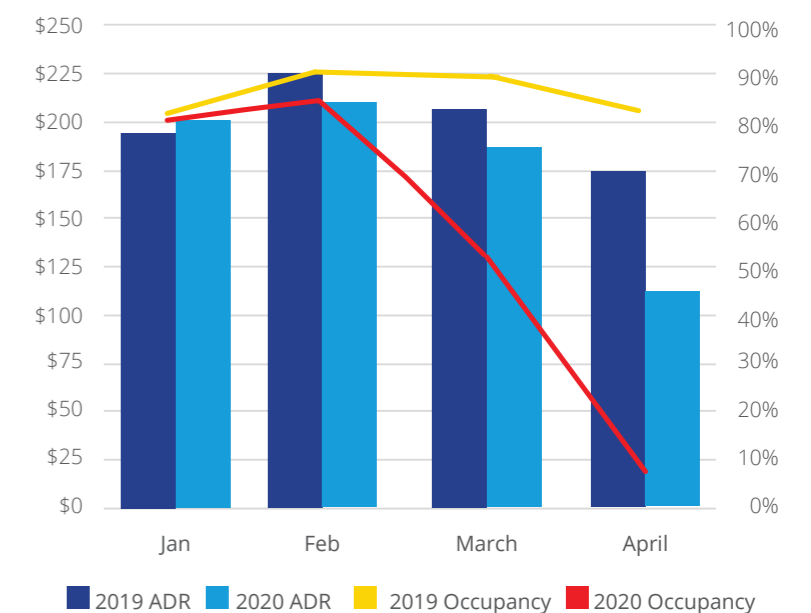
Source: Provisional International Travel Statistics, Stats NZ

Trading Performance

Despite a rapid decline in inbound demand, the impact of Covid-19 was not widely felt in the hotel sector until the later stages of Q1 2020 when border closures and a nationwide lockdown were implemented.

We summarise the monthly performance of the wider NZ Hotel sector for the YTD 30 April 2020 compared to the same period in 2019 in the chart adjacent.

NZ Hotel Performance Jan-April 2019/20



Source: Tourism Industry Aotearoa and Colliers International

Impact on Current & Future Supply

Existing Inventory

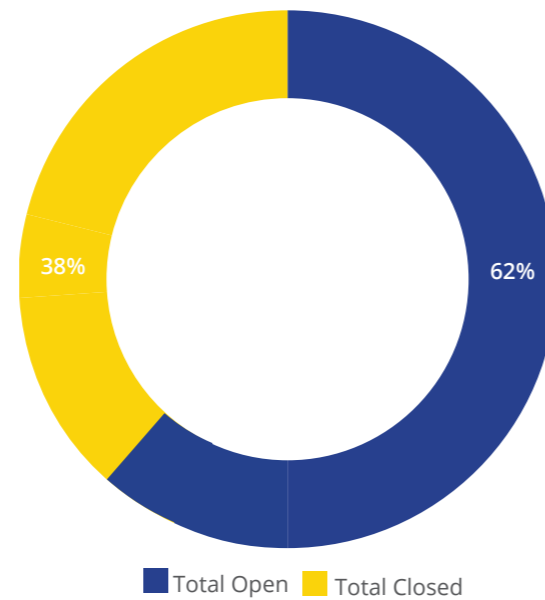
The New Zealand hotel sector as represented by the five main regions (Auckland, Rotorua, Wellington, Christchurch and Queenstown) currently comprises circa 23,000 rooms across 200 hotels and serviced apartments (typically of a three to five-star standard).

A survey undertaken in early April 2020 found that close to 40% of hotel rooms were temporarily closed or placed in 'hibernation' with another 40% open but operating with limited inventory and skeleton staff.

The exception being a number of hotels (under 20) located primarily in Auckland contracted by the Ministry of Health for mandatory self-isolation purposes, essential service workers and international visitors awaiting repatriation flights.

Many closed hotels will look to reopen once domestic travel is permitted on 14 May 2020, noting however some hotels will not open until circa Q3 2020 or longer depending on when sustainable levels of demand return.

NZ Hotel Closures by Room Count



Source: Colliers International

New Development

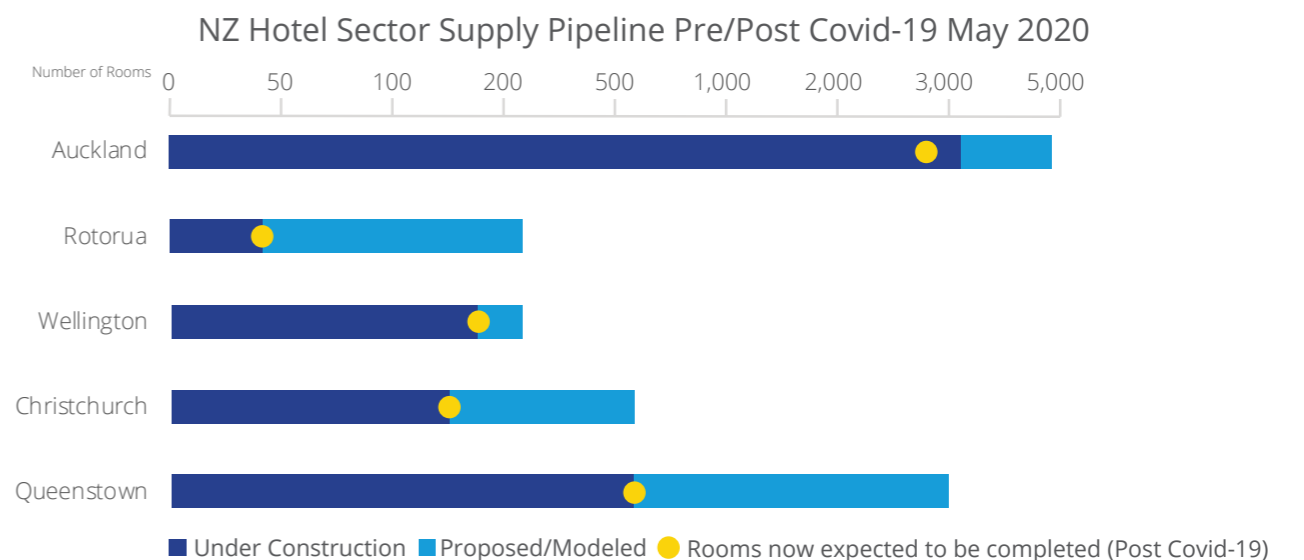
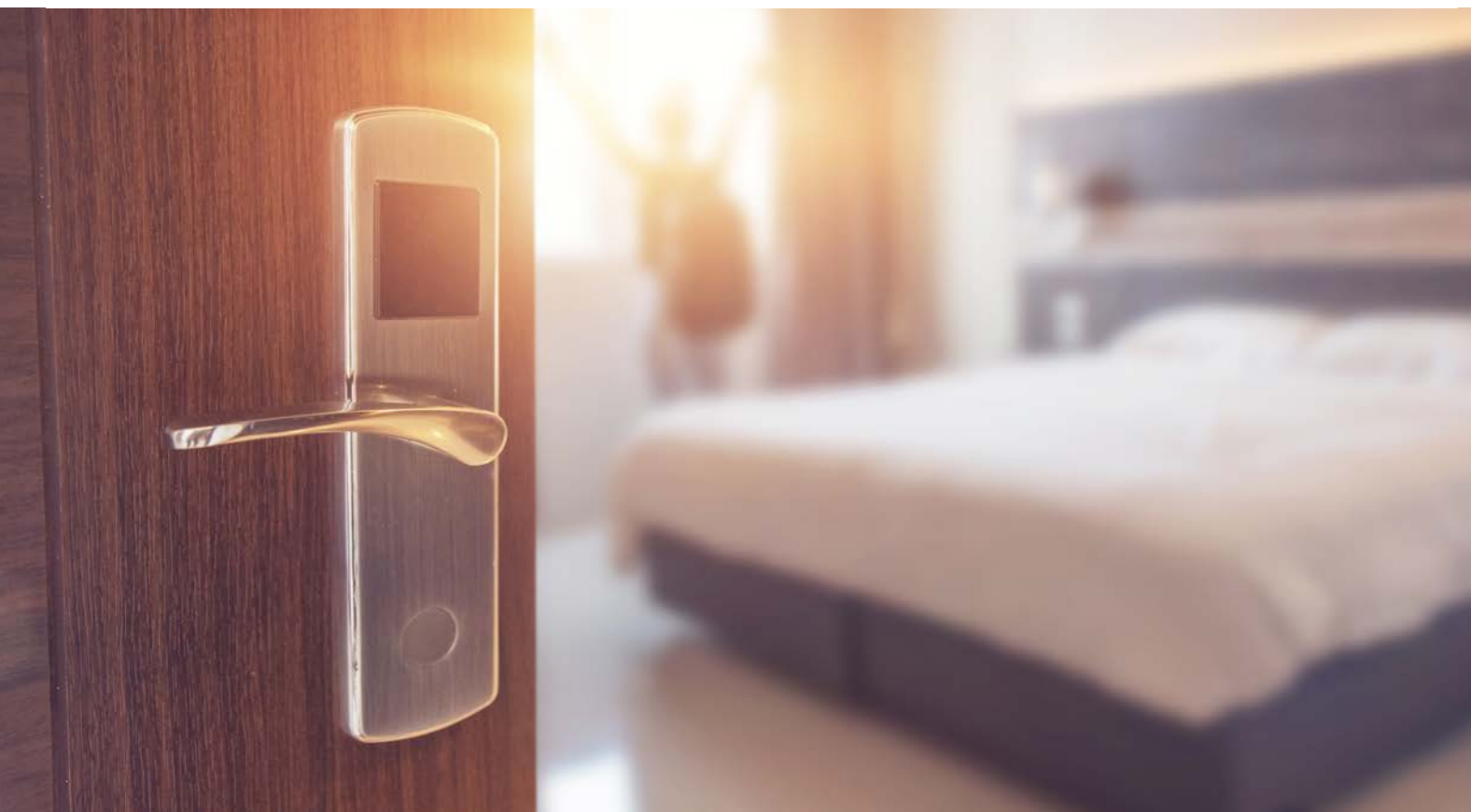
Covid-19 will certainly have an impact on the future supply pipeline throughout the country:

- Currently 27 hotels are under construction (circa 4,200 rooms) with most of these projects located in Auckland and Queenstown.
- The majority of these developments will be completed, although most will face a delay in the order of 3 to 6 months.
- A number of projects will elect to stage their opening as demand recovers with a small number seeking deferment, until they have a better understanding of how we emerge from the pandemic.
- Examples of this include the 244 room InterContinental Hotel at Commercial Bay in Auckland and the 146 room Mercure Hotel at Auckland Airport.
- There remains a large number of mooted developments earmarked across the country anticipated to add a further 3,425 rooms to our total inventory.

Looking forward, we believe very few (if any) proposed developments will now take place in the short-medium term due primarily to a tightening in liquidity and a recalibration of key performance metrics.

There is the strong possibility some of the existing hotel inventory, notably serviced apartments (which make up circa 20% of short stay accommodation), will elect to move into the long-term rental or owner occupier sector as was evident in past economic downturns.

All of the above factors will lead to a notable reduction in total existing and forecast hotel inventory from pre-Covid-19 levels, which will in turn assist the demand/supply pendulum in a post Covid-19 environment.



Source: Colliers International

Pathway to Recovery

Domestic

As New Zealand transitions from a nationwide lockdown, we will see the emergence of a 'domestic led recovery' for the wider hotel sector. This will fuel the start of a recovery process as seen in countries such as China and South Korea, which have recently eased lockdown restrictions.

Prior to Covid-19, domestic guests (business and leisure) accounted for over 50% of hotel room night demand with the exception of Queenstown (34%). We believe this will provide a valuable foundation for recovery throughout the remainder of 2020.

New Zealanders undertook 3.2 million overseas trips in 2019 and with our national borders currently closed we believe many will elect to travel domestically, creating additional demand particularly in key leisure destinations such as Queenstown and Rotorua. Business demand should also return in Wellington, Auckland and Christchurch.

The Government has also tasked Tourism New Zealand to initiate a new domestic marketing campaign to restart domestic tourism and support the post Covid-19 recovery phase for the wider industry.

International

We are anticipating the early stages of an inbound recovery by Q3 or Q4 2020 based on a 'Trans-Tasman Bubble,' provided Covid-19 remains contained in both countries. Australia is our largest visitor source market, with 1.5 million visits in 2019 (40% of all international visitor arrivals) and spending close to \$2.6 billion.

Bi-lateral travel agreements with those countries that have controlled Covid-19 are also possible, with the best prospects at this present point in time being the Southeast Asian seaboard including China, Hong Kong, Taiwan, South Korea, Thailand, Vietnam and Singapore.

However, we believe that any widespread inbound demand will not be back in notable numbers before Q1 2021. This is also reliant on a vaccine being found and airlines and airports creating a safe and sustainable travelling environment.

There also remains the possibility New Zealand can host a range of major sporting events scheduled for 2021 including the 36th Americas Cup, Women's Rugby and Cricket World Cups and Men's Softball World Championship.

Recovery Process 2020 to 2025

The consensus at this point is the recovery will not be immediate (V shaped), but more of a graduated improvement over time, perhaps best described as a 'Hockey Stick Recovery Cycle' with wider demand re-emerging in 2021 and building progressively throughout 2022 and beyond.

Based on modelling completed at this early phase of the cycle, we believe the recovery will also result in a 'recalibration' of key performance metrics, as we emerge to a new paradigm in a post Covid-19 environment.

The impact of our border closures and lockdown will result in a sharp decline in RevPAR of approximately 30-60% across key regions for the 2020 calendar year, based on low occupancies and corresponding pressure on room rates.

As previously mentioned, the recovery process will be predominantly driven by domestic guests, many of which will be price sensitive.

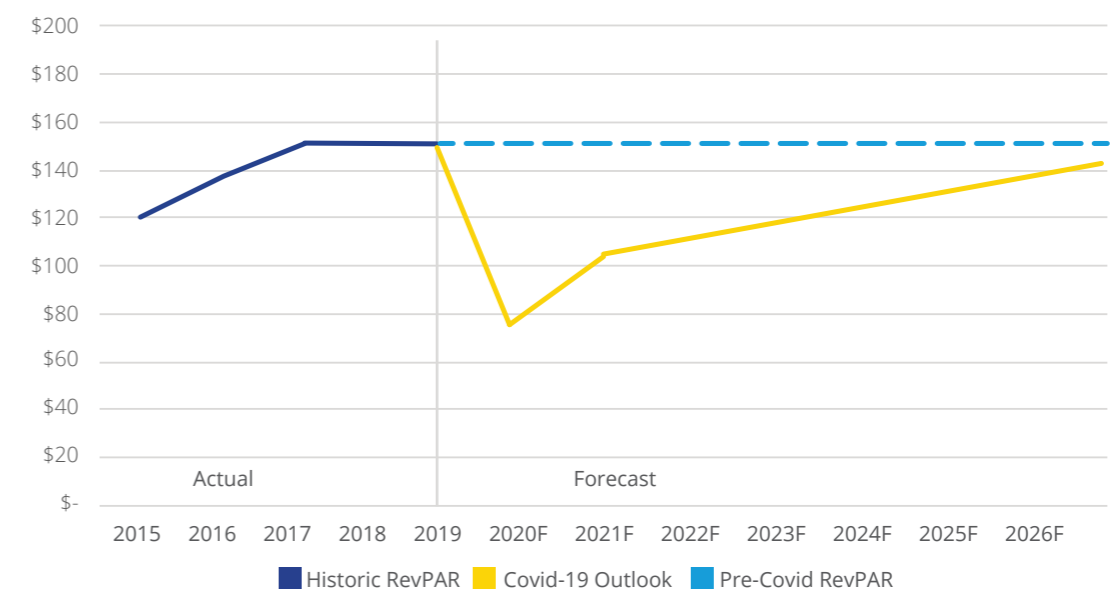
From 2021 we will see a notable improvement in occupancy and room rates as inbound demand returns.

While we remain confident the medium-long term prospects for the New Zealand tourism/hotel sector are positive, the wider impact of the pandemic could see the hotel sector take up to five years to recover to pre-Covid-19 levels.

However, we believe a silver lining exists for the New Zealand tourism sector if we continue to control the virus and implement sustainable and safe travel practices across our industry. This could create new opportunities that could in turn increase demand levels above our current forecasts.

We summarise below a possible 'recovery scenario' for the key regions in the NZ hotel sector:

NZ Hotel RevPAR Outlook



Source: Colliers International

We have undertaken detailed forecasts for each of the key regions and welcome you to contact us should you have any specific requests.



Investment Yields & Values

Prior to Covid-19, investor sentiment and demand remained strong, especially for well located, quality hotel assets. While the short term outlook is uncertain, the medium-long term prospects for tourism/hotel investment remain sound.

Those investors who can weather the next 18 months, will likely emerge in a stronger position having fully re-evaluated their operating model and re-positioned themselves for a robust recovery. Given their long-term ownership objectives, their investment return profile will remain largely unchanged.

Conversely, those owners who are under capitalised or unable to sustain some pressure on their balance sheet may need to evaluate their position and divest or restructure their business and/or assets.

While the impact of Covid-19 on hotel yields and discount rates is yet to be fully tested, any repricing is likely to be largely reflected in the revised cash flow projections being produced.

It is also important to note that based on previous downturns, hotel values have quickly recovered, so short term losses, are often temporary in nature.



Closing Remarks

Although Covid-19 will have a significant impact on the hotel sector in the short-term, we know that the \$9 trillion global tourism industry will bounce back, but, the question remains when and in what form?

We remain confident that the \$40 billion New Zealand tourism industry will again prosper in the knowledge that people of all walks of life love to travel and that New Zealand is a 'bucket list destination' for many millions of people around the world.

We also remain confident that our private and public sectors are committed to ensuring we have a sustainable, vibrant and globally appealing tourism offering into the foreseeable future.

We hope you have found this report insightful. Please feel free to reach out should we be able to assist you in these challenging times.

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