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IN FOCUS: ROME

WHY THE ETERNAL CITY COULD BECOME THE NEXT HOTSPOT FOR LUXURY HOTELS

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‘Why should luxury travellers pay less for a hotel in Rome than in London, Paris or New York? We have the same guests here...,’ a General Manager of a luxury hotel in Rome asked me recently during an interview. His remark poses an interesting question: why are luxury hotels in Rome not able to charge similar rates as those in London or Paris, when they supposedly attract a similar clientele?

A comparison with other European gateway cities illustrates that the business mix of the hotels in Rome is actually slightly different to that of London and Paris. Whilst the latter are not only tourism hot spots but also global business hubs, Rome’s client mix is more leisure and government focused. Although Rome is the political centre of Italy and benefits from demand generated from embassy and government-related events, Italy’s business powerhouse remains in the north in the area around Milan. As a must-see destination for every leisure traveller, Rome enjoys high popularity, but the city does not have the same status and perception as a luxury shopping and lifestyle destination such as London, Paris, Milan, Venice or the French Riviera. Additionally, supply related factors, such as underinvestment and a lower number of international luxury hotel brands, have so far prevented the Rome luxury hotel market from reaching comparable room rates with these other destinations.

Nevertheless, and despite several challenges, Rome remains attractive for investors and hotel operators and has the potential to become the next hot spot for luxury hotel development.

Rome – No Introduction Needed!

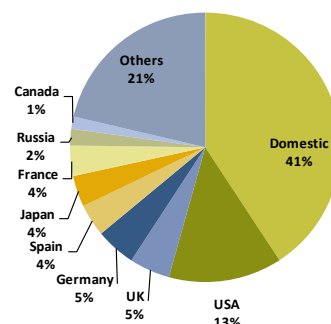
The city’s historical and cultural sites are numerous, well known and draw visitors from all over the world. Rome’s popularity is highlighted by its strong demand growth over the past several years.

FIGURE 1: TOURISM ARRIVALS TO ROME



Source: European Cities Tourism

FIGURE 2: TOURISM ARRIVALS BY SOURCE COUNTRY



The return of US travellers to Europe has been noted in Italy and Rome is expected to benefit as it remains one of the most popular destinations for US travellers. The US dollar materially strengthened against the euro over the past year and is forecast to grow further during 2015, which underlines the strength of the US travel market. Emerging markets such as Asian and Middle Eastern countries (as well as Russia, until recently) have also registered high growth in visitation and are expected to foster further demand for luxury accommodation in the coming years. Visitation from the main European countries Germany, France, the UK and Spain has also demonstrated decent growth. Domestic demand has been resilient and, with the anticipated pick up in the Italian economy, the outlook should remain positive.

FIGURE 3: US\$/€ EXCHANGE RATE SINCE 2006



Source: Oanda

FIGURE 4: ECONOMIC INDICATORS ITALY

	Year	Real GDP growth (%)	Consumer Price Inflation (av %)	Exchange Rate €:US\$
Actual	2009	(5.1)	0.8	1.40
	2010	1.2	1.6	1.30
	2011	0.5	2.9	1.40
	2012	(2.4)	3.3	1.29
	2013	(1.8)	1.3	1.33
Forecast	2014	(0.4)	0.2	1.33
	2015	0.2	0.1	1.22
	2016	0.6	0.6	1.18
	2017	0.9	1.0	1.20
	2018	1.0	1.3	1.21
	2019	0.9	1.4	1.24

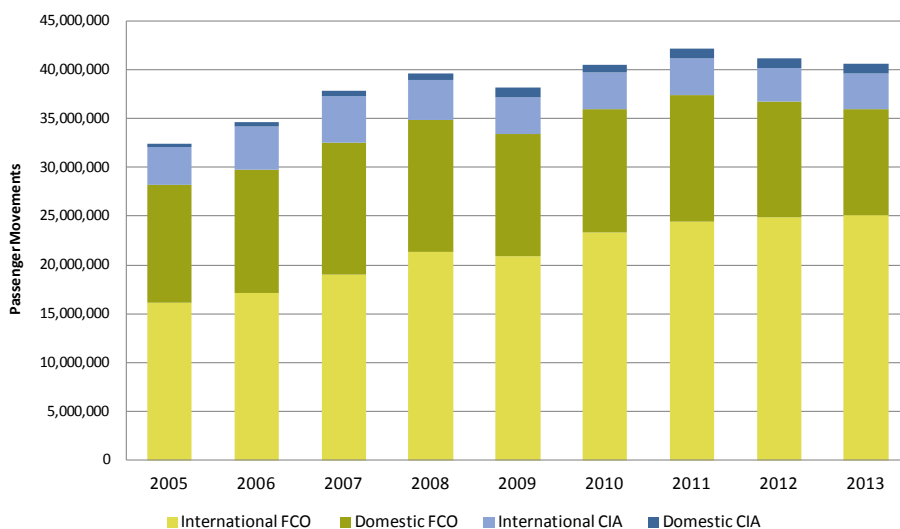
Source: Economist Intelligence Unit, January 2015

Airport Demand

After two years of declines in total passenger movements at Rome’s main airport, Leonardo da Vinci International (FCO), year-to-November 2014 figures show a healthy pick up of 6.2% compared to the previous year, driven by both domestic and international arrivals. Rome’s low-cost hub, Ciampino (CIA), which is some 15 km southeast of

the city, also recorded good growth for year-to-November 2014 with an increase in total passenger numbers of 7.5% on the same period in 2013.

FIGURE 5: PASSENGER MOVEMENTS AT FCO AND CIA AIRPORTS



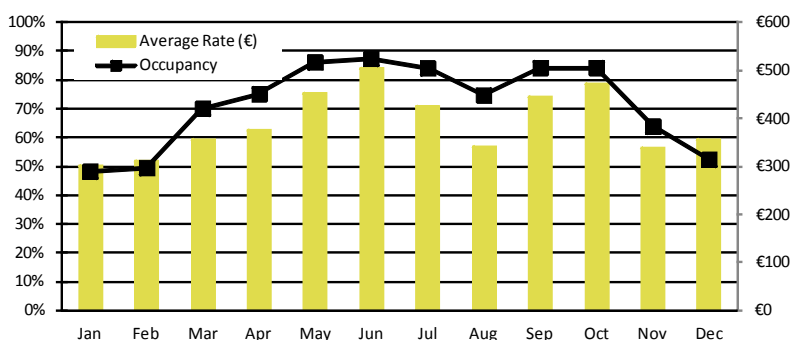
Source: Airports Council International

pronounced, with market occupancies falling below 50% in January only. During the peak months, market occupancies reach 85-90%, which supports Rome’s strength as a premier city within Europe – one that is capable of luring large numbers of visitors.

Seasonality

Rome has a relatively broad seasonality, with the low season running from December to February and, to a lesser extent, in August. Given its extensive leisure attractions and its status as an established weekend-break location and a sound economic hub, Rome’s seasonality is not

FIGURE 6: LUXURY HOTELS – MONTHLY PERFORMANCE 2013 (€)



Source: HVS Research, EBTL, Performance of Luxury Hotels during 2013

The Economy and Luxury Fashion: The Difference between Rome and Milan

Milan’s luxury hotels are achieving higher rates than its counterparts in Rome, partially due to the fact that Milan has a broader range of international luxury hotels than Rome. Furthermore, Milan has always been

seen as the economic centre of Italy. Milan not only hosts the country's stock exchange, it also serves as the centre of the industrial northern part of Italy and is famous worldwide for fashion and luxury goods.

Milan will be getting a lot of attention this year as it hosts the next world fair (Expo Milano 2015) from 1 May to 31 October, and the city aims to attract some 20 million visitors during this time. It is hoped that the Expo will increase awareness of Milan as a leisure destination. Whilst Rome generally has sufficient leisure tourism, Milan's luxury hotels sometimes struggle to attract leisure demand on weekends and during the low season. Milan also has some potential oversupply concerns with several new high-end luxury hotels opening over the next few years. Three hotels alone are scheduled to become operational before the beginning of the Expo: the 104-room Mandarin Oriental, the 240-room Excelsior Hotel Gallia, a Luxury Collection Hotel and the 139-room ME by Meliá. Additionally, a W Hotel has also been announced for a 2016 opening.

Luxury Hotel Performance Benchmark – Why Are Rates in London and Paris Higher?

The following analysis of the top luxury assets in Rome, London and Paris shows that Rome lags significantly behind Paris and London when it comes to average rate.

FIGURE 7: PERFORMANCE COMPARISON – TOP LUXURY HOTELS IN ROME, PARIS AND LONDON (€)

	Rome			Paris			London		
	Occupancy	Average Rate	RevPAR	Occupancy	Average Rate	RevPAR	Occupancy	Average Rate	RevPAR
2014 Jan-Nov	74%	413	304	77%	947	725	77%	727	561
2013	72%	401	287	63%	1,052	667	77%	746	577
2012	71%	380	270	60%	1,071	646	79%	794	629
Rooms Sample:	875			1,477			934		

Source: HVS Research

There are several reasons for this:

- Rome lacks the prestigious 'Palace Hotels' of Paris, which owing to their heritage and status can command average rates of above €1,000. London has more international luxury hotel brands (after the recent addition of Shangri-La and Rosewood only a few are missing to complete the collection);
- Several hotels in Rome suffer from underinvestment because capital expenditure has been deferred for too long. Some hotels are even in need of a complete renovation and therefore do not offer the same overall quality as assets in Paris and London;
- Average room rates are also influenced by suite sales. However, the quality and number of suites in Rome's luxury hotels is generally inferior compared to high-end properties in London and Paris;
- The area of Rome that houses many of the existing luxury hotels is no longer a prime luxury area. The focus of high-end travellers has shifted from the Dolce Vita area in Via Veneto to the high-end shopping and tourism quarter of Piazza di Spagna and Via Condotti.

Lack of Luxury Supply – Why are there no Four Seasons, Mandarin Oriental, Peninsula or Rosewood Hotels in Rome?

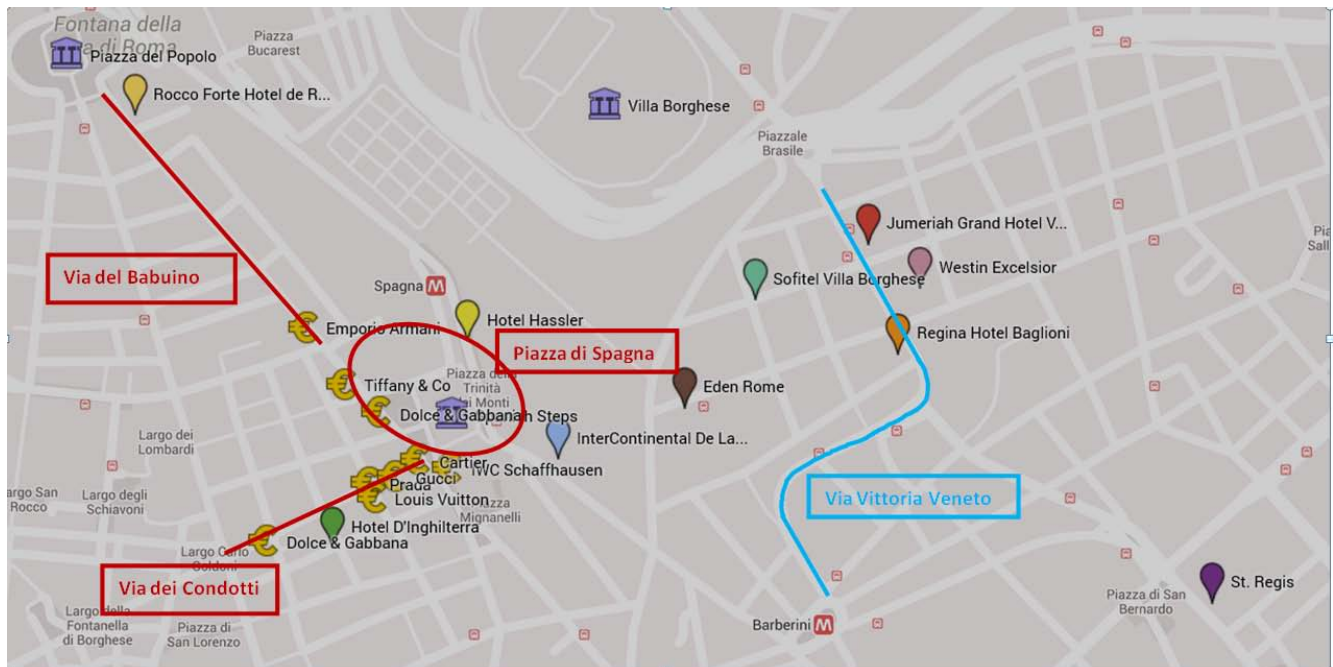
Several international luxury hotel brands have managed to establish a presence in Rome but many others have not (yet) found the right opportunity to enter the Italian capital. Not because of a lack of interest, but more due an absence of the right location, partners and projects. Developing a luxury hotel in Rome appears to be challenging because of a shortage of available sites (many buildings are either protected or owned by the church or families), tough planning legislation and a high development risk. 'It is quite likely that you find some ancient bone when digging two storeys underground, which could stall your development for a significant time', commented one general manager. Nevertheless, opportunities exist with the right partner, location and project as the city is currently lacking high-profile luxury developments in prime locations, and there are currently some noteworthy

developments in the pipeline with the potential to change the luxury hotel landscape and enable the city to push for higher rates.

Location – Luxury Moved from Via Veneto to Via Condotti and Piazza di Spagna

Via Veneto used to be associated with the famous Dolce Vita and the area hosts a number of luxury hotels. However, the luxury retail industry has since moved to the more pedestrian-friendly area around the Piazza di Spagna and Via Condotti, which attracts higher footfall. The map below shows that high-end fashion shops and luxury brands such as Tiffany & Co, Louis Vuitton, Cartier, Prada, and so forth can all be found in this area. Streets with the highest retail rents are Piazza di Spagna, Piazza San Lorenzo and Via Condotti. On the other hand, with the exception of the Hotel D'Inghilterra, there are no luxury hotels in the immediate area. The Rocco Forte de Russie and the Hotel Hassler enjoy the best strategic locations and are also said to be rate leaders in the city. It should be noted, however, that location alone does not guarantee high room rates – both of these hotels have great reputations and the Rocco Forte de Russie also benefits from a stunning courtyard and well-designed facilities and suites.

LOCATION OF LUXURY RETAIL STORES COMPARED TO LUXURY HOTELS



Underinvestment

Another reason why Rome's luxury segment achieves lower average rates than other prime European gateway cities is the underinvestment of certain assets. Several independent and internationally branded 'luxury' or upscale hotels suffer from underinvestment and are in need of capital expenditure in order to properly meet the demands of luxury clientele. Whilst this underinvestment currently limits the city's average rate growth, it also underlines the potential once certain hotels are properly renovated and repositioned.

Opportunities & Pipeline

There are signs that the luxury landscape is about to change:

- The Eden Hotel is expected to undergo an extensive renovation and repositioning following its takeover by the Dorchester Collection during 2013. The hotel has a great history, reputation and good location in proximity to the main luxury shopping area and leisure demand generators such as the Spanish Steps, Villa Borghese and Via Veneto. The hotel has the potential to compete with the Rocco Forte Hotel de Russie for the leadership position in the market;

- Although nothing has been publicly announced at this stage, it is likely that the recently sold St. Regis, InterContinental De La Ville, Boscolo Aleph and Boscolo Palace hotels will undergo significant renovations over the coming years. Middle Eastern owners generally have a long-term investment view and are therefore normally keen to preserve real estate assets at high standards;

IMPRESSION OF THE ROMAN PENTHOUSE AT THE REGINA HOTEL BAGLIONI



Source: Baglioni Hotels (www.romanpenthouse.baglionihotels.com)

- Following its acquisition by Mayola for Investments (a Qatari-owned investment vehicle), the Baglioni Hotel Regina with its 'Roman Penthouse' set a new precedent for luxury suites in Rome. The stunning suite can be separated into various rooms, has its own roof terrace and offers magnificent 360 degree views over Rome;
- Shangri-La is said to be adding another asset to its European portfolio with plans to open a hotel opposite the Westin on Via Veneto. However, there is currently no official information regarding this project;
- A project involving a luxury lifestyle hotel brand is also in the planning stage but is confidential at the moment. The hotel is expected to become operational in the next two to three years;
- The Aldrovani Hotel, albeit behind Villa Borghese in an 'out of the way' location, is an interesting asset with 122 rooms, pleasant courtyard gardens, a two-Michelin star restaurant by Oliver Glowling and branding potential in combination with an overall upgrade of the rooms and facilities. It would not be a surprise if an operator decided to partner with the current owner for this asset in the coming years;
- Four Seasons has been associated with a project at the State Mint and Polygraphic Institute, the stunning building at Piazza Verdi. No official update is available at this stage, but the development is expected to include a 200-room hotel and several luxury apartments, some of which will be branded. The project is not in a prime hotel location, which indicates that the focus might be on the residential component.

Hotel Investment Market

Rome has always been an interesting market in which to invest, with prime real estate always in high demand. Figure 8 shows recent transactions in Rome.

Foreign investment, particularly from the Middle East, has dominated luxury hotel purchases in the recent years. The Hotel Eden, which was acquired by the Brunei Investment Agency (owner of the Dorchester Collection) for reported €105 million is one of the exceptions.

An interesting case is the InterContinental de La Ville, which has transacted several times during the past eight years. The hotel was always sold as part of a portfolio. At the peak of the market, Morgan Stanley originally purchased seven InterContinental hotels (Amsterdam, Madrid, Vienna, Rome, Budapest, Cannes, Frankfurt) from InterContinental Hotels Group in 2006 for a reported €634 million. Toufic Aboukhater, a Lebanese high-net-worth individual, acquired the portfolio in 2011 for €450 million, a significant discount which reflected the hotel transaction market in the aftermath of the financial crisis. Toufic Aboukhater sold the portfolio again in 2012 (after taking out

the Vienna property) for an undisclosed price to GSSG, a Qatari holding company which then resold the portfolio to Katara Hospitality in 2014 for an undisclosed sum.

FIGURE 8: LUXURY HOTEL TRANSACTIONS ROME (€)

Transaction Date	Hotel	Rooms	Transaction Price (£)	Transaction Price per Room (£)	Buyer	Seller
Oct-14	The St. Regis Rome	161	110,000,000	683,000	Qatar Holding	Starwood
Oct-14	Boscolo Palace Roma	87	65,500,000	753,000	Millennium & Copthorne Hotels	Boscolo Hoteles
Aug-14	Hotel Aleph	95	40,000,000	421,000	Al Faisal Holding	JV: Raiffeisen Bank, Banca Agrileasing, Veneto Banca, UniCredit
Jun-14	InterContinental De La Ville Roma ²	192	Undisclosed	Undisclosed	Katara Hospitality	GSSG Holdings
Nov-13	Baglioni Regina		Undisclosed	Undisclosed	Mayola for Investments	Baglioni Hotels
Aug-13	Hotel Eden	121	105,000,000	868,000	Brunei Investment Agency	Starwood
Jul-12	InterContinental De La Ville Roma ²	192	Undisclosed	Undisclosed	GSSG Holdings	Toufic Aboukhater
Jan-12	Hotel delle Nazioni	100	50,000,000	500,000	Sorgente SGR	Fimco Immobiliare Srl
Mar-11	InterContinental De La Ville Roma ²	192	34,100,000	178,000	Toufic Aboukhater	Morgan Stanley (MSREF)
Sep-08	Ambasciatori Palace Hotel	151	100,000,000	662,000	Royal Group Hotel & Resorts	
Jan-08	Hotel Aleph	95	52,250,000	550,000	JV: Raiffeisen Bank, Banca Agrileasing, Veneto Banca, UniCredit	RREEF Fondimmobiliari SGR
Jul-06	InterContinental De La Ville Roma ²	192	48,030,000	250,000	Morgan Stanley (MSREF)	InterContinental Hotels Group

¹ Transaction price not published

² Allocated value as part of a Portfolio

Source: HVS Research

Overall, the potential to drive returns for investors is good, as bottom-line returns are decent with gross operating profit margins for luxury hotels typically ranging from 25-35% (for well managed hotels). Managing staff, unions and costs can be challenging but is essential for driving profitability in rooms and food and beverage departments. Also, taxation can be an issue. Creative concepts are needed for hotel food and beverage outlets as competition from independent restaurants is strong.

Potential to drive rate premiums lies in the high-end suites business and the ability to attract luxury guests. Strong hotel brands may aid the luxury perception and positioning.

Outlook

Rome will always remain an attractive leisure destination. With the Italian economy anticipated to improve and with growing demand from the USA, the Far East and the Middle East, the city is well positioned for further growth. Limited new supply in the luxury segment and renovations of existing hotels are expected to drive rate and demand for luxury accommodation.

Investors from all backgrounds are expected to remain keen on acquiring (hotel) real estate in Rome. Hotel operators will continue to scout opportunities and, owing to the development challenges, may potentially be included to be more flexible with management contract negotiations.



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