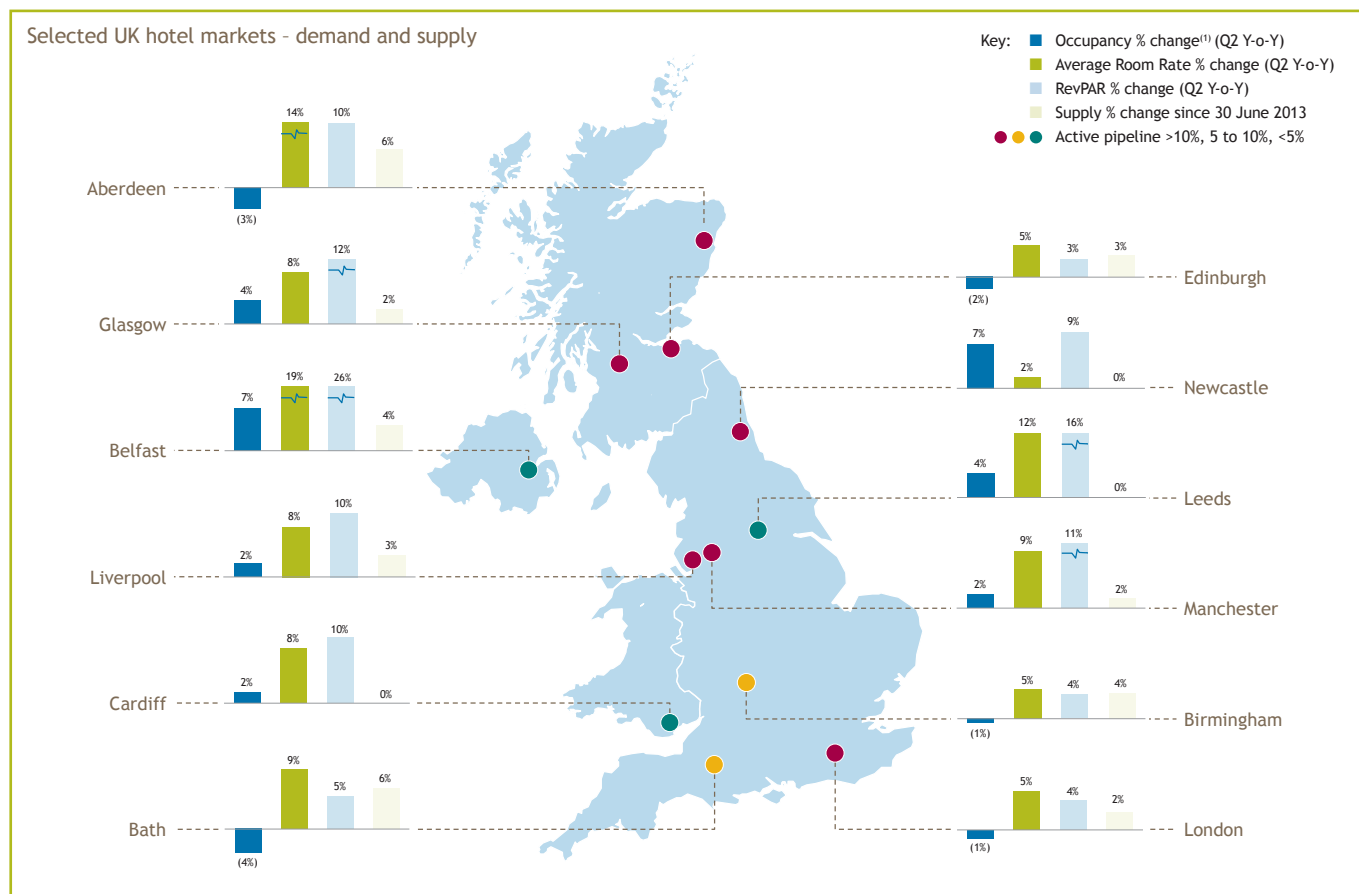


Hotel Bulletin: Q2 2014

Analysis completed in this edition reveals that the majority of cities reviewed are now generating RevPAR beyond pre-downturn levels. The UK transaction market has been dominated by single asset sales this quarter although this is set to change as a number of portfolios progress towards completion. This edition focuses on Edinburgh and considers how the historically robust hotel market may be impacted by a 'yes' vote in September.



Source: AM:PM, HotStats

Notes: Q2 covers the three months to the end of June

Q2 Y-o-Y compares the average of Q2 2014 to the average of Q2 2013

Supply and pipeline analysis relates to number of hotel bedrooms

(1) Occupancy percentage change represents actual rather than absolute percentage change

Active pipeline refers to hotel bedrooms with an opening date in the next three years

Key highlights of the quarter

RevPAR exceeds pre-downturn levels

Eight of the 12 cities reviewed recorded average H1 2014 RevPAR beyond pre-downturn levels, with the remaining four rapidly approaching this level. Reaching this benchmark is a cause for optimism and will give certain hoteliers the confidence to invest time and money in expansion.

Hotel performance in London and the regions has continued to improve in Q2 2014. For the third quarter in a row, all of the cities reviewed recorded RevPAR growth. Rate driven growth is likely to result in profitability improvement.

Single assets dominate transaction market; however, portfolio transactions to come

Over £411 million of transactions completed in Q2 2014, significantly more than the £154 million that completed in Q2 2013. In H1, over £1.9 billion of hotel transactions completed.

In Q2 2014, the majority of transactions were for single assets. This trend is likely to change in the remainder of the year. Already in Q3 2014, Hallmark Hotels, 144 Travelodge hotels, 11 QMH hotels and 19 LRG hotels have transacted and, in addition, a number of other portfolios are progressing towards completion.

Demand

Continued wide-spread growth in Q2 2014

In Q2 2014, and for a third consecutive quarter, all of the 12 cities reviewed recorded RevPAR growth compared to Q2 2013. On average, RevPAR increased by 10%. Consistent and strong growth is encouraging and is likely to leave investors in a confident mood.

RevPAR in London increased by 4% in comparison to Q2 2013 as a 5% increase in ARR more than compensated for a slight drop in occupancy. London's RevPAR has now increased in ten out of the last 12 quarters.

Outside London, RevPAR grew by an average of 11%. Growth was predominantly rate driven in all cities except Newcastle, where RevPAR improvement was underpinned by a 7% increase in occupancy. Hoteliers who continue to improve rates will see the benefit in the bottom line.

For the second consecutive quarter, Belfast recorded the highest RevPAR growth (26%) of the cities reviewed. A significant amount of investment has been made in the city in recent years and in this quarter, performance was buoyed by the Giro D'Italia's Big Start in May. Other top performers included Leeds (16% RevPAR growth) and Glasgow (12% RevPAR growth).

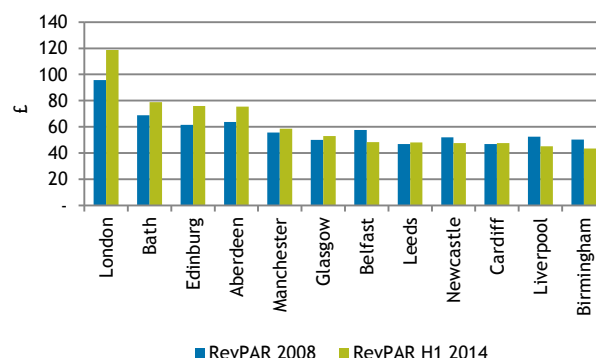
RevPAR returning to pre-downturn levels

The graph opposite compares average RevPAR for the 12 months ended 30 June 2014 and 31 December 2008. Eight of the 12 cities reviewed have now returned to pre-downturn RevPAR levels. Aberdeen, Bath, Edinburgh and London are generating RevPAR which is far in excess of 2008 levels, demonstrating the strength of these markets.

Belfast, Birmingham, Liverpool and Newcastle are the only cities yet to fully recover from the downturn. However, given recent RevPAR improvement and continuing investment in these cities, it is unlikely to take long to surpass pre-downturn RevPAR levels.

After years of flat/declining performance in the UK, returning to 2008 levels is likely to provide confidence to UK hoteliers.

RevPAR 12 months ended H1 2014 versus CY 2008⁽²⁾



Source: AM:PM, HotStats

Notes: (2) Analysis does not consider any inflationary adjustment

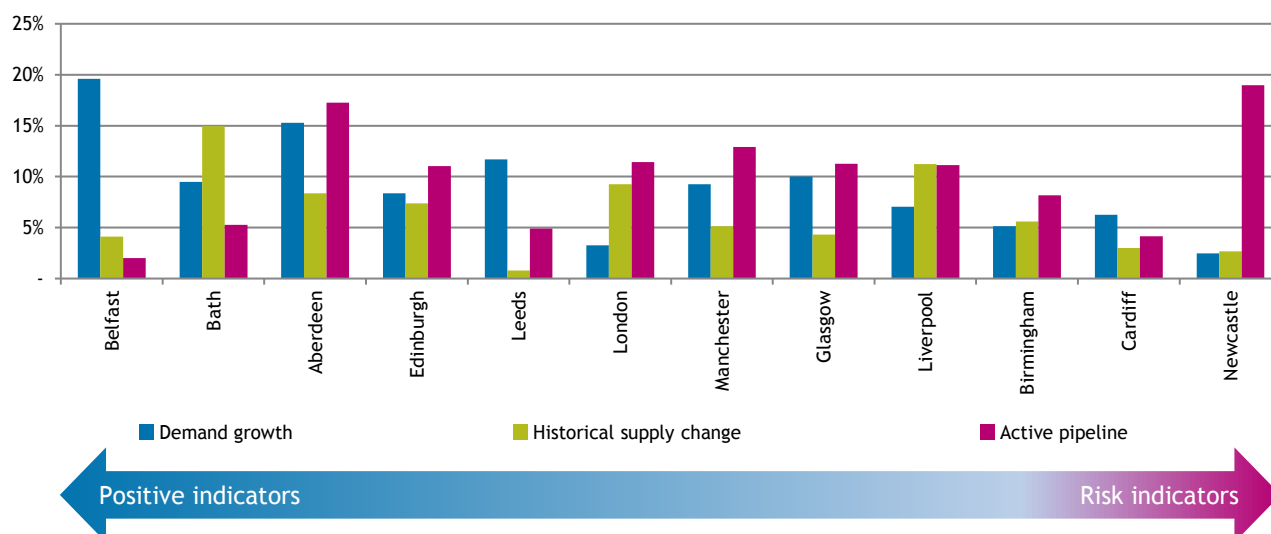
Investment indicators

Although high-level demand and supply metrics alone will never fully inform an investment decision, the graph below is intended to highlight demand and supply data for cities that may attract, or concern, investors.

The interaction of demand growth, historical supply and active pipeline are considered. Demand growth has been calculated as the average RevPAR growth for the last four quarters to provide an indication of recent demand trends. Historical supply has been calculated as the increase in rooms in the last two years in order to allow for an appropriate amount of time to contextualise recent trading performance. Active pipeline has been included in the analysis to provide an insight of each city's hotel market in the upcoming years. Only bedrooms with confirmed opening dates are included.

The UK hotel market is displaying characteristics of a cyclical upturn, with demand consistently growing strongly in spite of additional supply. The forward looking concern is active pipeline growth which is beginning to respond to performance improvement. This is particularly evident in Aberdeen, where active pipeline as a percentage of current supply has increased from 9% to 17% in the past year.

Investment indicators



Source: AM:PM, HotStats

Notes: Demand growth calculated as the average quarterly RevPAR change for the last four quarters

Historical supply change calculated as the change in hotel bedrooms between June 2012 and 2014

Active pipeline calculated as the active pipeline as a percentage of current supply

The majority of the 12 cities reviewed appear to be displaying positive indicators - the arrow has been shaded to reflect this

Supply and pipeline

Budget hotel domination set to continue

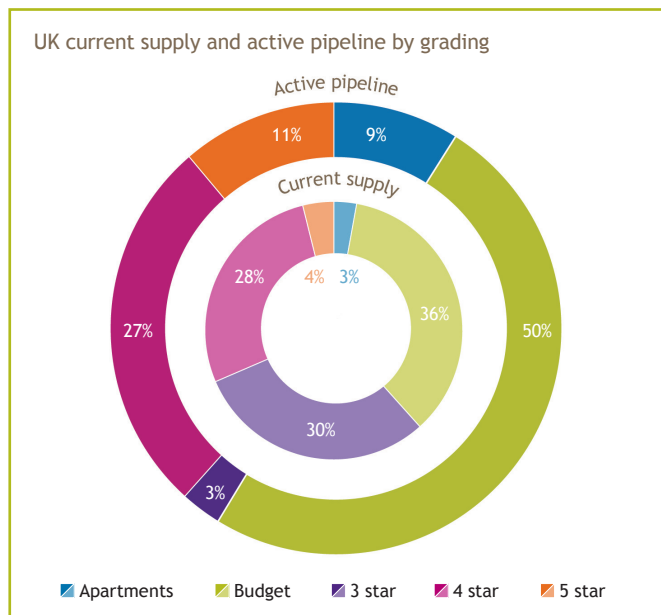
In the graph below (left), we compare the proportion of current supply (inner circle) and active pipeline (outer circle) in the UK market by sector.

The budget market⁽³⁾ remains the largest in the UK and this is set to increase with 50% of active pipeline bedrooms in this category. It is a market that continues to be dominated by brands, with 66% of current supply and 98% of active pipeline being branded. Independent hoteliers in this sector may rightly be concerned about being squeezed out of the market.

Budget hotels on city fringes are likely to benefit from increasing numbers of Chinese tourists visiting the UK, which has increased by 19% each year since 2011. The majority of Chinese tourists travel in tour groups, which favour these types of hotels due to cost considerations. Given the recent easing of visa requirements for Chinese visitors the number of tourists is expected to rise significantly.

Notable new openings and developments in the quarter include:

- Accor Group opened two of their mid-market brand Novotel in London (437 bedrooms) in the quarter. Accor is also developing its aparthotel offering, with four Adagios (608 bedrooms) set to open in Aldgate East, Stratford (both London), Birmingham and Edinburgh.
- The 202 bedroom Shangri-La opened in the quarter in London. The five star hotel, located on floors 34 to 52 of the Shard, cost the Hong Kong based group over £90 million in lease and fit-out costs (approximately £450,000 per room).
- Five Premier Inns (572 bedrooms) opened in London, Glasgow and Wigan in the quarter. A number of less established budget brands continued to expand. Z Hotels opened the 112 bedroom Z Piccadilly, its third hotel in London and fourth hotel in the UK. CitizenM is set to open three hotels (827 bedrooms) in 2015, including the CitizenM Tower Hill which sits opposite The Tower of London and within The Tower conservation area.



Source: AM:PM, Financial Times

Notes: Active pipeline includes developments with a confirmed opening date in the next three years

(3) The budget category includes hostels, budget and two star hotels

Transactions

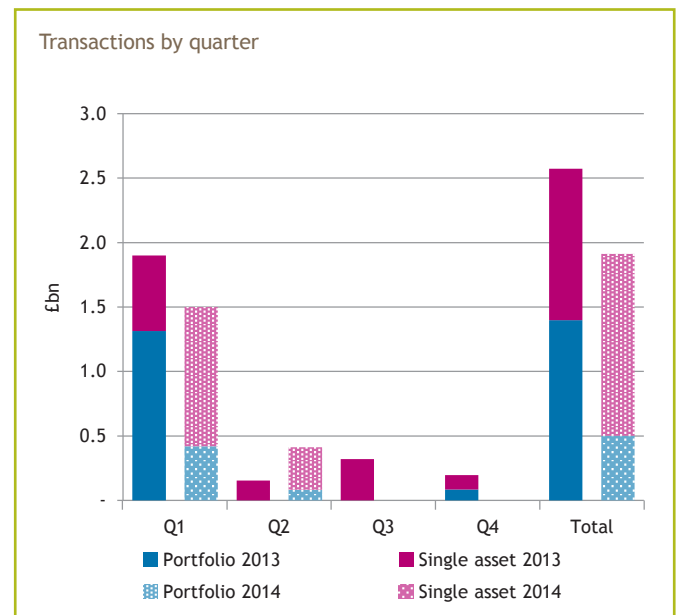
2014 transactions progress toward £2 billion mark

In H1 2014, approximately £1.9 billion of transactions have completed. Over £411 million of these were in Q2 2014, which was over £250 million more than Q2 2013.

The majority of transactions in the second quarter were for single assets. We expect this trend to change in the remainder of the year. To date in Q3 2014, Goldman Sachs, GoldenTree AM and Avenue Capital have acquired 144 Travelodge hotels, Topland Group has acquired Hallmark Hotels, Marathon AM has acquired 11 QMH UK hotels and Kew Green has acquired 19 LRG Hotels. In addition, a number of other portfolios are moving towards completion, including two De Vere portfolios.

Notable transactions include:

- The sale of The Park Inn Hotel & Conference Centre, London Heathrow to AXA REIM for approximately £72 million (over £80,000 per room). The 895 bedroom, four star hotel is the closest hotel to terminals 1, 2 and 3 at London Heathrow. Zolfo Cooper acted as joint administrators of the seller.
- A joint venture between Lone Star and Somerston Capital has acquired the morethanhotels portfolio of 12 Holiday Inn Express hotels with a total of 1,399 bedrooms from a bank consortium.
- Two Holiday Inn Express hotels in Edinburgh and Dunfermline have been acquired by Chardon Trading. Debt funding for the acquisitions was provided by RBS. The hotels are managed by Interstate Hotels & Resorts.
- Kew Green Hotels followed the acquisition of four Holiday Inn hotels in January 2014 with the acquisition of the 110 bedroom Holiday Inn in Bromsgrove.
- Starwood Hotels & Resorts sold its leasehold interest in the 303 bedroom Park Lane Hotel, London back to Sir Richard Sutton's Settled Estates. The hotel will continue to operate as a Sheraton under a new management contract and will undergo a major refurbishment.



Source: HVS

Note: Only disclosed hotel transactions over £6 million included in analysis

Focus on: Edinburgh

The market

Edinburgh's hotel market benefits from strong leisure and corporate demand. It is the UK's most popular conference destination outside London and has recorded average occupancy levels of 78% in the last four years (the highest outside the capital).

The city hosts 12 annual festivals, including the popular Edinburgh Festival and Fringe events. These festivals together attract audiences of over four million each year. Edinburgh's new tram system, opened in May 2014, and current plans for the £850 million redevelopment of the St James Quarter are set to increase the city's popularity further with tourists.

Last twelve month performance

Edinburgh's RevPAR has grown each month compared with the previous year. The period began with significant RevPAR and GOPPAR growth of 30% and 50% respectively in July 2013 as Muirfield hosted the Open Championship, with 142,000 spectators attending over four days.

Strong top line performance continued for the remaining months of the year with the city recording average year-on-year RevPAR growth on a monthly basis of 12%.

From March to June 2014, Edinburgh's hoteliers were unable to grow ancillary revenue streams at the rate of room revenue, which resulted in flat or declining GOPPAR performance. Q3 2014 is likely to be a successful quarter for Edinburgh as the city hosted diving events in the Glasgow Commonwealth Games and the Edinburgh Festival, however, improving profitability performance in the long-term will be crucial for the city's hotel market.

Supply and pipeline

Current supply in Edinburgh is similar to the rest of the UK with the exception of having a lower proportion of three star hotels and a higher proportion of four and five star hotels. Edinburgh's visitors are prepared to pay a premium for this higher-end concentration of hotels as highlighted by Edinburgh's average ARR in the last two years being over 20% higher than the average for the UK (excluding London).

Aparthotels account for 25% of Edinburgh's active pipeline, which is significantly higher than the UK average of 9%. This demonstrates the strength of the city's corporate offering.

Source: conventionedinburgh.com, scotland.gov.uk, telegraph.co.uk

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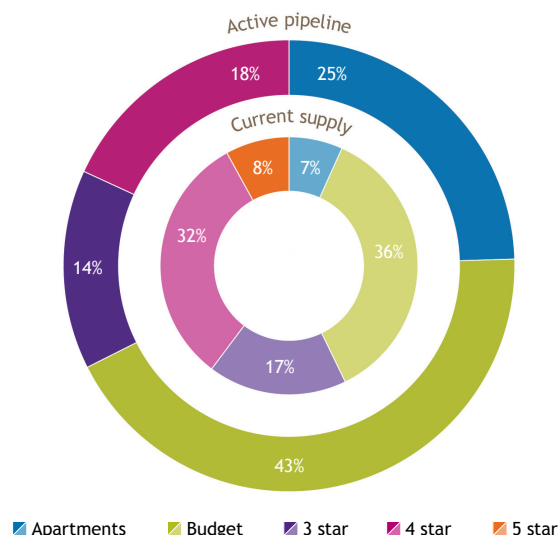
The vote

Independence has been met with scepticism by parts of the Scottish hospitality industry. They consider that investors may be put off by uncertainty surrounding the economy and creation of independent Scottish bodies. That being said, there has been no noticeable sign of investment in Edinburgh hotels slowing down following the announcement of the vote.

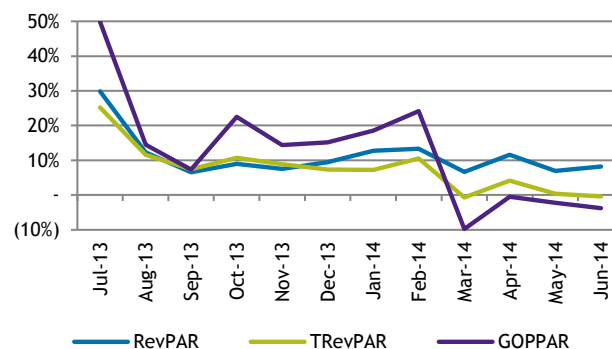
Some argue that Scottish tourism can be marketed more effectively if Scotland becomes an independent nation. The city would also benefit from the influx of professionals advising on structural change which would increase demand for hotel accommodation in the short-to-medium term.

Regardless of the outcome, Edinburgh is likely to remain an attractive city for global investors due to its established corporate and leisure offering. It remains to be seen how other parts of Scotland would be impacted by a 'yes' vote.

Edinburgh's current bedroom supply by offering



Edinburgh's year-on-year change in demand by month



Source: AM:PM, HotStats

Note: The budget category includes hostels, budget and two star hotels

HOTSTATS

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