Australia | November 2022

Hotels & Hospitality

JLL Hotel Operator Sentiment Survey 2022

Australia

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Introduction

As the industry continues its recovery path out the biggest disruptor in history, operators remain at the forefront of a shifting hotel environment. JLL Hotels & Hospitality Group launched the inaugural Australian Operator Sentiment Survey (HOSS) in October 2022, to gain perspective on what hotel operators are currently focussing on and foreseeing in the sector moving forward.

Over 30 key international and domestic hotel operators within Australia were invited to participate in the survey and share their insights on the sentiment and trends shaping the hotel landscape.

The general sentiment in the market is relatively optimistic, however realistic of the challenges and opportunities that lie ahead. In this report we have identified key themes through the lens of the operators that are shaping the market moving into the year ahead.

1 GOP supported by strong rate growth

Across the country, hotel trading conditions are much stronger than most had originally anticipated for this point in time. Despite occupancy levels remaining challenged, trading recovery has largely been driven by the strong average daily rate (ADR) premiums that are being achieved across the country. Rates are currently (YTD October 2022) sitting well above both 2021 and 2019 levels, for the same period.

As a result, YTD RevPAR continues to show strong signs of recovery, led by markets with strong domestic leisure demand profiles. As of YTD October, all key markets with the exception of Melbourne (-15%) and Sydney (-21%%) have seen RevPAR recover to their respective pre-COVID levels (YTD October 2019); Cairns (+21%), Gold Coast (+20%), Brisbane (+15%), Canberra (+7%), Hobart (+6%), Perth (+3%) and Adelaide (+2%).

This aligns closely with operators' current expectations of Gross Operating Profit (GOP) recovery. With most markets having already recovered YTD GOP back to full year 2019 levels. The majority of respondents are of the belief that Sydney, Melbourne and Perth are lagging slightly behind and will likely return to full-year pre-COVID levels of GOP over 2023.

When is your expectation of GOP recovery for your portfolio to 2019 full year levels?

	2022	2023	2024	2025+
Sydney	37%	42%	21%	0%
Melbourne	0%	63%	38%	0%
Brisbane	44%	33%	22%	0%
Gold Coast	47%	33%	20%	0%
Adelaide	69%	13%	19%	0%
Perth	27%	47%	27%	0%
Other Markets	67%	22%	11%	0%

Source: JLL HOSS 2022

As hotels have entered improved **trading conditions** over **2022, businesses are benefiting from refined operating structures and operating procedures that were introduced over the last two years.**

Cost efficiencies coupled with an improvement in RevPAR has led to an improvement in departmental and overall profit margins.

2 Labour shortages remain a critical challenge

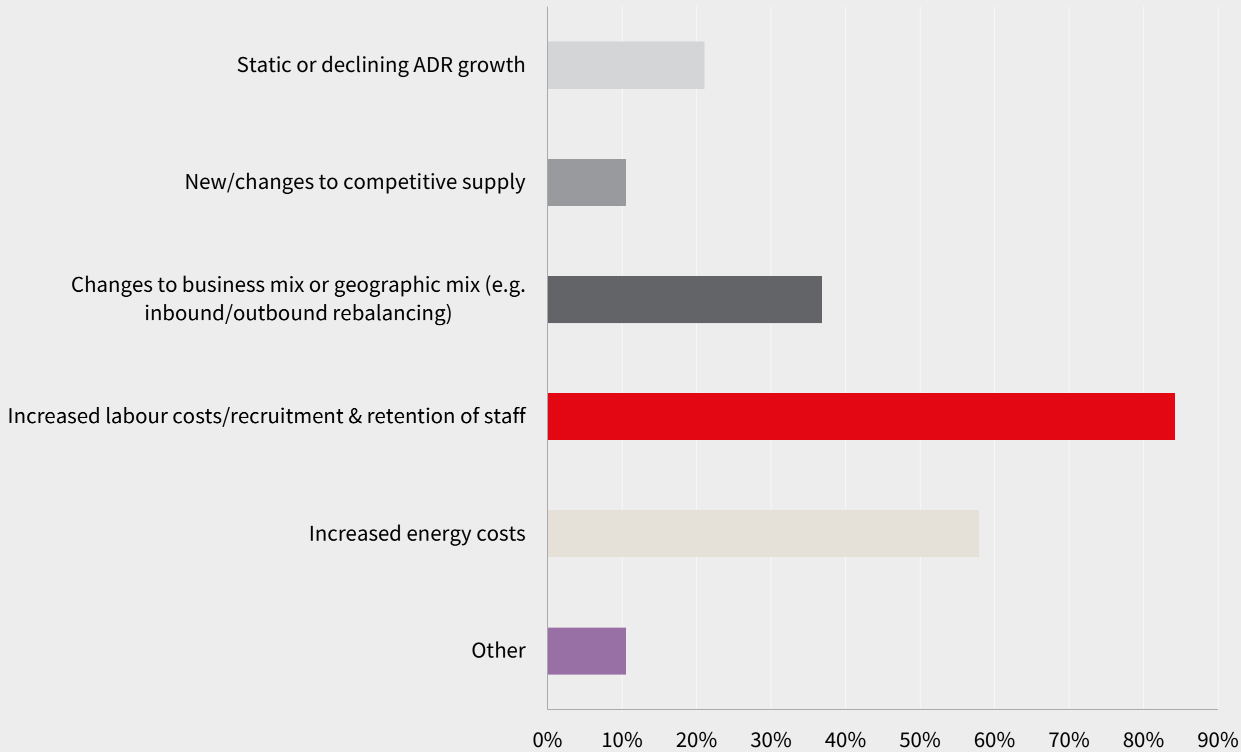
The hospitality industry continues to struggle with significant labour and staffing issues. The increase in labour costs, recruitment & retention of staff is currently the number one challenge facing operators, with over 80% of respondents expecting it to hamper GOP performance heading into 2023. As a result of these challenges, many hotels and F&B venues are still unable to operate at their usual capacity or productivity levels, which is causing serious headaches for both owners and operators.

As per SEEK's Employment Report, job ads in the Hospitality & Tourism industry have fallen 8.1% year-on-year to October 2022, however this still reflects over 30,000 hospitality jobs currently advertised online nationally. The highest job vacancies include F&B staff (kitchen, bar and wait staff), housekeepers and managers.

Many groups are having to deploy new ways of attracting and retaining staff, including using cash and other incentives to attract new workers. However, the steady recovery of overseas students and migrants should see these vacancies begin to be filled over the short term.

In addition to labour shortages, over 50% of operators believe rising energy costs and inflation will hamper GOP performance and over 35% anticipate that shifting demand profiles (e.g. changes to business mix or geographic mix) will also have an impact. Other concerns raised included; static or declining ADR growth, changes to competitive supply, economic headwinds/contraction and struggling occupancy levels.

In your view, which of the following is most likely to hamper GOP performance in 2023?



Source: JLL HOSS 2022

Based on our internal review of 2023 business plans, headwinds over the coming year include labour costs and the recruitment/retention of supervisory and senior management staff. However, the relaxation of Visa restrictions and the return of inbound migration has begun to steadily alleviate the current employment market.

3 Key focuses for 2023 business planning

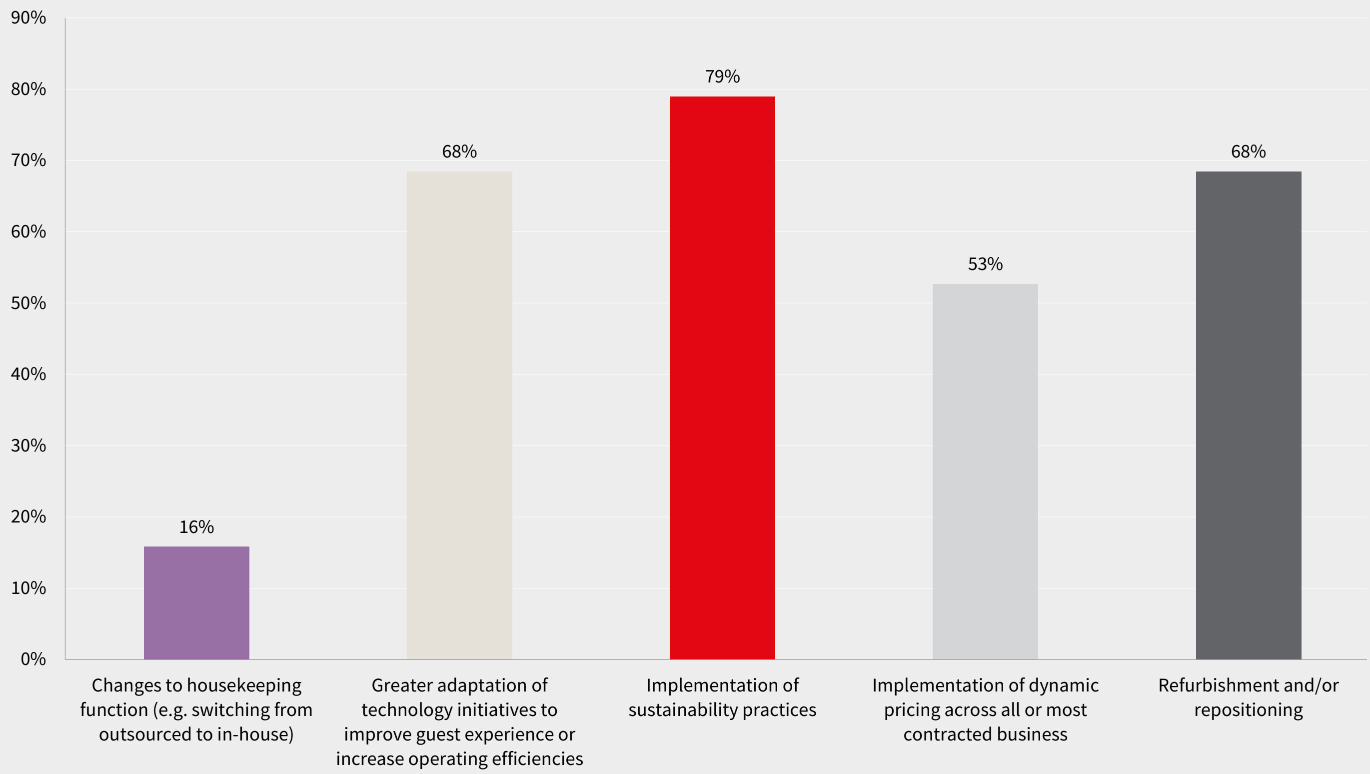
As we review 2023 business plans, it is evident there is an increased focus on sustainability and the improvement of guest experience with the use of technology. The first step with technology in many instances is to move forward with keyless check-ins and streamlining the hotel's building management systems to improve energy efficiencies. This is often followed by the opportunity for more major refurbishment or repositioning plays.

Sustainability

New technology

Refurbishment/repositioning

As part of 2023 business planning, are you contemplating any of the following?



Source: JLL HOSS 2022

4 ESG is now a number one priority

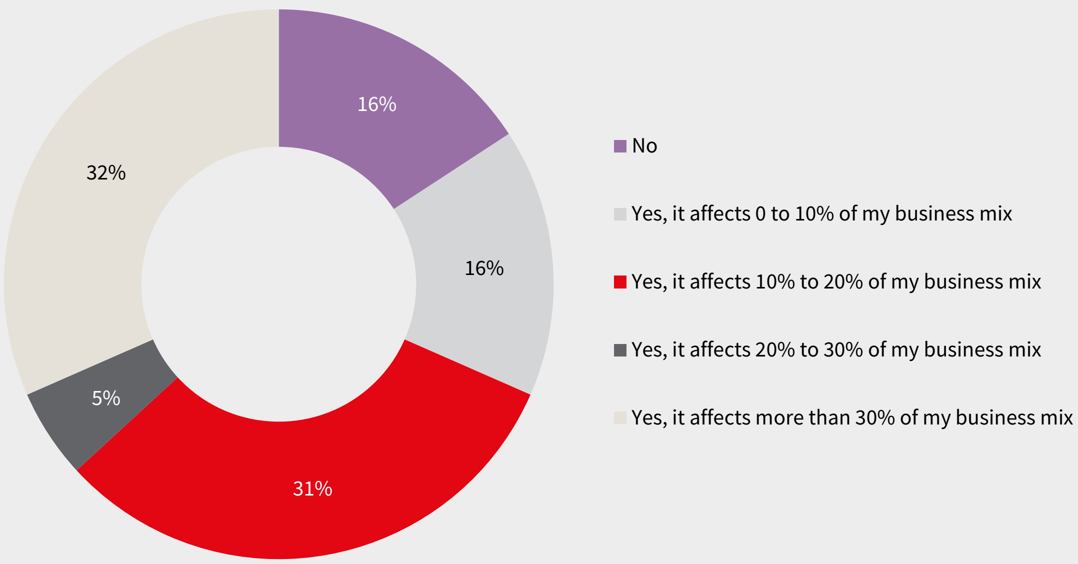
ESG is rising in prominence and now a growing focus area in hotel operations across the country, however mandated initiatives in corporate accounts still have some way to go. Operators tend to be more on the front foot when it comes to ESG and implementing action plans, with only 16% of respondents having not mandated any ESG initiatives. The major focus on ESG upgrades is currently on the operations side of the equation. However in Australia, retrofitting and refurbishing existing assets is also an emerging focus, to upgrade older stock to comply with new sustainability goals.

This ESG journey is already beginning to affect occupancy levels and a hotels bottom line. For example, on a leisure front, a recent Booking.com survey concluded that 78% of travellers intend to stay in more sustainable properties in the coming year. On a corporate front, as more and more companies pledge Net Zero goals, this will directly affect their travel and expenses (T&E) governance. With many groups already electing not to send staff to stay in properties that do not align with their pledges.

The main challenges operators are facing is the lack of data and difficulty in determining KPI's to measure success goals. However, some HMA's now have specific ESG metrics which operators can use to assess performance. Changes to reporting guidelines and the Uniform System of Accounts for the Lodging Industry (USALI) is also spurring positive changes among hotel operators, as well as the introduction of ratings sources outside the traditional hotel environment (e.g. NABERS and Green Star certifications).

Operators must continue to work with owners on this journey – the JLL Sustainability Survey 2022 concluded 43% of respondents agreed that case studies with clear ROI's is the way to convince owner partners on ESG initiatives. We also expect the looming possibility of 'brown discounts' for non-ESG complying hotel assets, will likely result in further awareness and action to help preserve and enhance real estate values. Many hotel owners and operators are already continuing to seek and implement energy and operational savings.

Are your contracted corporate accounts mandating ESG initiatives to be in place?



Source: JLL HOSS 2022

There is no doubt that ESG and Net Zero carbon targets are now a major focus for hotels. In our view, the measurement of key metrics under a new section titled Energy, Water and Waste (EWW) in the 12th revised edition USALI is likely to be introduced in early 2023. This will be a very important unified step the industry takes to provide improved reporting and benchmarking of EWW costs and usage.

5 Hotel technologies accelerate post-COVID

Operators are increasingly focussed on implementing new technologies to improve guest experiences, flexibility and increase operating efficiencies (e.g. keyless check-in, contactless payments, building monitoring systems, etc.). Post-COVID this trend has accelerated, with both operators and owners faced with a new wave of operational challenges.

- The future adoption of sustainability initiatives is strongly tilted towards technology, with most operators now investing in new technologies that will underpin ESG solutions.
- Operators are now having to place a greater focus on improving health and wellbeing, by providing access to amenities including exercise programs and telehealth services (e.g. HotelCare.Health).
- The current labour shortages have also led to increases in developments in automation and artificial intelligence (AI), improving efficiencies through hotel website chatbots and online concierges.

The leading new technology functions set to be introduced by operators in 2023 include;

New initiatives to promote direct bookings through proprietary channels rather than third-party websites

Contactless F&B ordering and payments

Energy management and real time building level energy monitoring

Keyless digital check-in and mobile entry (removal of physical room key)

Following COVID, technology has taken pole position in improving guest experiences and hotel efficiencies. While QR codes evolved prior to COVID, hotel and food & beverage operators are embracing QR codes for in-room dining, restaurant, bars and poolside dining. The advent of QR codes for poolside dining has seen an immediate uplift in food and beverage revenues.

In addition to this, technology initiatives by operators to drive direct bookings will be of great assistance in improving the financial returns for hotel owners, by minimising costs associated with bookings from third party channels.

6 New supply expected to moderate over the near term

Two thirds of operator development teams expect a decline in the number of new development projects across the board, as the current unprecedented supply cycle nears its end. It is anticipated that given current supply chain issues, interest rates and rising construction costs, the focus will shift towards refurbishment and repositioning of existing assets. Whilst some new projects will still commence construction over the coming years, it is likely this increase will be offset by a rise in existing hotel rooms coming out of the market, as is already evident.

These emerging supply trends are currently being mirrored by investors, who are strongly searching for strong upside potential, through potential refurbishment or rebranding opportunities. Capital is also targeting assets with value-add opportunities, in the conversion and redevelopment of older hotel assets into alternative uses (e.g. build to rent, luxury residential, office, etc.).

The significant current supply wave has seen a record number of new rooms enter the market across Australia, with a heavy weighting towards upper-upscale and luxury product, ultimately improving the overall quality of the market. This is placing increased pressure on older assets to upgrade, prior to them running the risk of becoming obsolete.

According to a recent investor survey carried out by JLL, nearly 80% of hotel investors said they are targeting value-add investment opportunities in the sector. Many investors are now preferring to buy existing assets needing refurbishment, repositioning, or rebranding, with the return prospects often much more appealing.

A recent example in the Australian market is the reopening of the Kimpton Margot Sydney by Australian hospitality fund manager Pro-invest. After acquiring the Primus Hotel Sydney in 2021, Pro-invest refurbished and repositioned the Art Deco asset, which now offers new innovative culinary experiences and a new lifestyle offering.

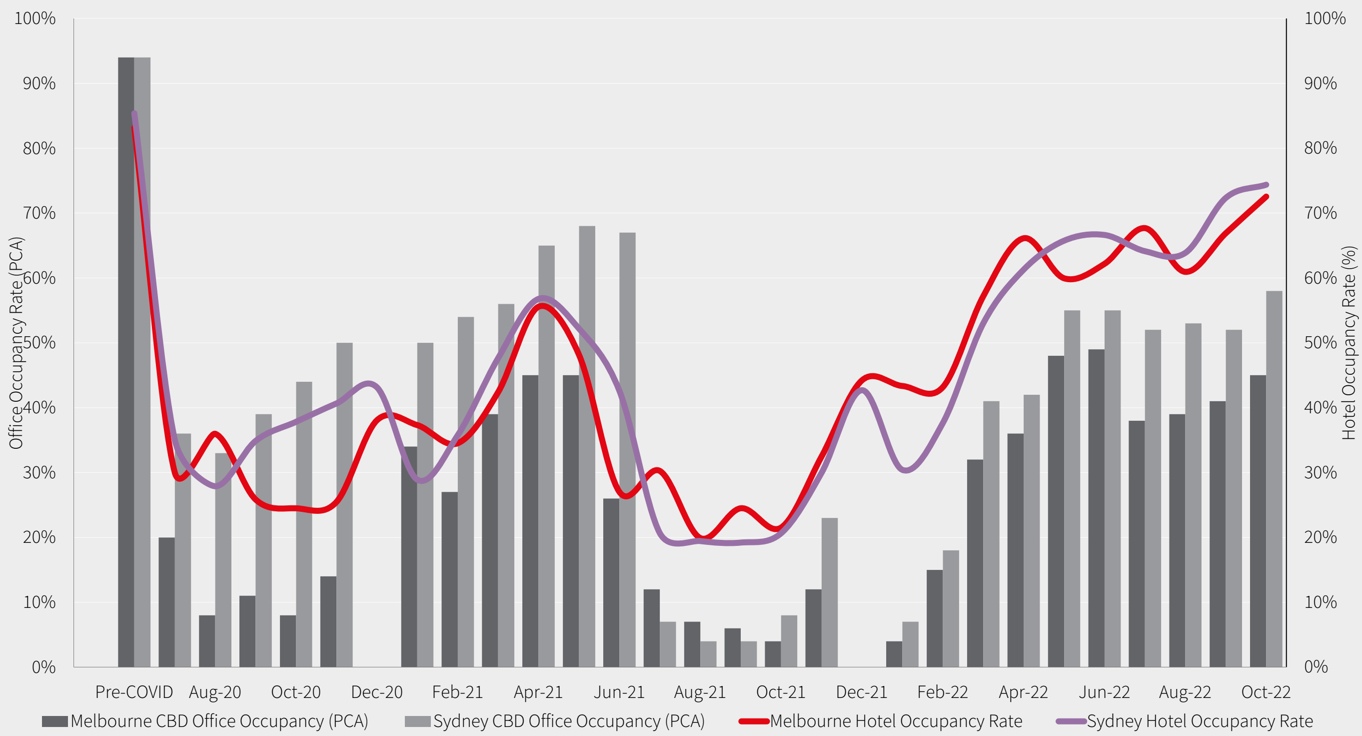
7 Corporate and MICE segments steadily return

Historically, hotel occupancy levels have been largely driven by domestic corporate demand, especially for the key economic hubs of Sydney and Melbourne. Therefore, the return of workers and reactivation of CBD offices remain critical to the steady recovery of the corporate segment of the hotel market and is key to the sustained performance and growth of city hotels moving forward. The Property Council of Australia's (PCA) office occupancy survey commenced at the onset of the pandemic and over the past two years has demonstrated strong correlations to hotel occupancy data (STR).

Circumstances surrounding COVID-19 and the rise in flexible working has resulted in a staggered return to the office. The implications of this for CBD hotels and the hospitality sector more broadly is the large decline in corporate travellers, as it reduces the need for interstate or international travel to attend face-to-face meetings or conferences. Despite this, corporate travel and in-person conferences are showing positive signs of recovery and this momentum is anticipated to continue into 2023.

This sentiment is being mirrored by most operators, with close to 80% of respondents expecting residential conferencing to recover to 2019 levels over the course of 2023. This is a much more optimistic outlook for corporate and MICE segments than previously forecast, given strong levels of conferencing already booked in over the coming year.

CBD office occupancy levels strongly correlate to hotel occupancy



Source: JLL, STR, PCA

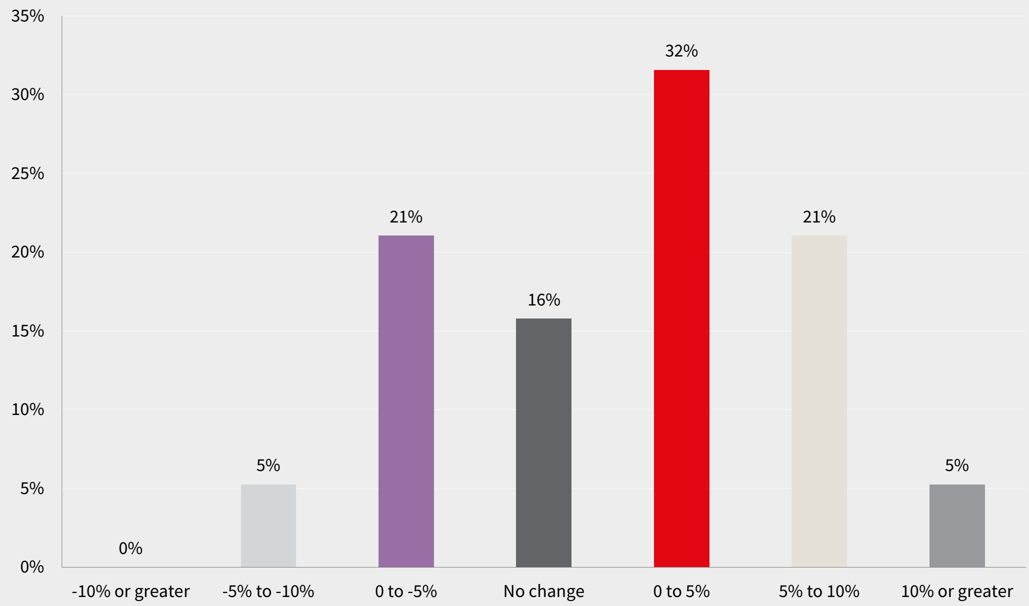
Over the past couple of months there has been a rebound in corporate demand, which is now showing tailwinds in preparation for a return to pre-COVID levels over the course of 2023. Improvement in international airline capacity and the cost of air travel will bolster the volume of conference and event attendees next year.

8 Opportunities still lie within regional markets

Despite increased air travel facilitating the return of overseas holiday making, together with some concerns over consumer confidence levels, operators are of the view that this will not negatively impact regional markets over 2023. 74% of respondents are expecting RevPAR to remain the same or continue to increase in regional markets over the coming year.

This regional optimism is being fuelled by a range of emerging themes including; uncertainty and the rising cost of international travel, newly discovered local leisure destinations, increased convenience of domestic travel and travel stability. This also fuels new opportunities within these markets, through the refurbishment and upgrade of aging assets.

Broadly speaking, what is your expectation for regional market RevPAR performance in 2023, in light of increased international air travel?



Source: JLL HOSS 2022

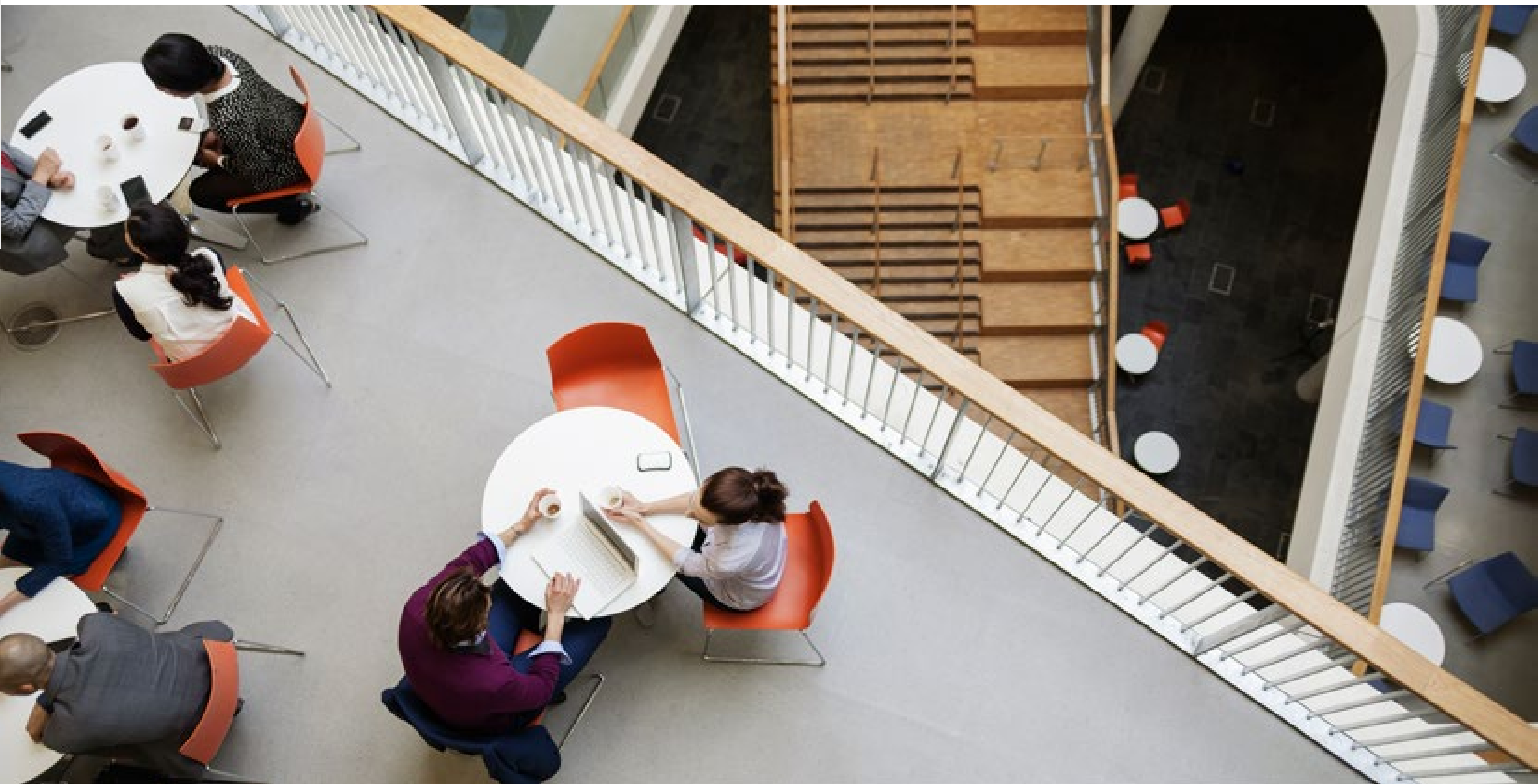
Regional markets have an opportunity to review soft refurbishments in the low and shoulder months of 2023, to remain competitive and provide value for money to guests. As well as this, the travelling market is also faced with the option to consider overseas destinations or to continue rediscovering Australia.

9 Lease structures remain unpopular

As has always been the case in the hotel industry, HMA's and franchise agreements are the dominant operating arrangement over leases, given a favourable balanced structure between an owner and operators responsibilities, risks and returns. Lease structures typically tend to be more focussed towards economy and midscale hotels and serviced apartments, however, continue to remain relatively unpopular amongst key operators in Australia.

- Prior to COVID, only a quarter of operators have or had considered lease operating structures.
- And of those that had, 40% expect they would no longer consider lease structure moving forward.

Leases are being considered on a case-by-case basis primarily by domestic and regional operators. Following COVID market conditions, we are also seeing the covenants around 'Force Majeure' being revamped in new lease agreements.



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