Horwath HTL

Hotel, Tourism and Leisure

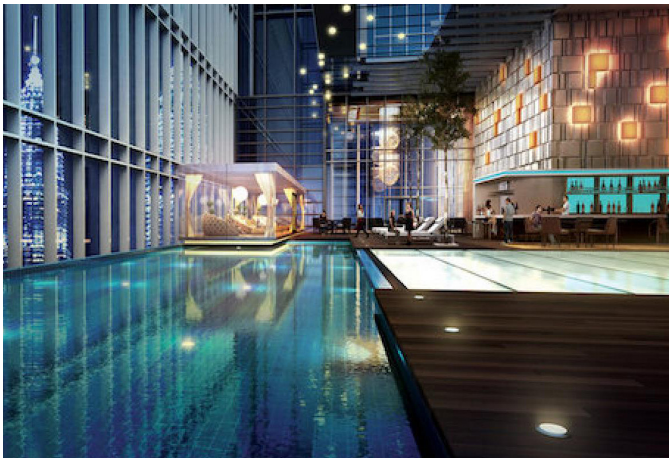
MARKET REPORT

Kuala Lumpur

Top Tier Hotel Market

SEPTEMBER 2021

Source: EQ Kuala Lumpur



Source: Four Seasons Kuala Lumpur

Kuala Lumpur, known as an international commercial and financial centre, is home to the largest number of upper-upscale and luxury hotels in Malaysia. Like other major markets, Kuala Lumpur's hotels faced a devastating and challenging year in 2020 and well-into 2021.

Kuala Lumpur (KL) is the main economic and business centre of Malaysia. It is the centre for finance, insurance, real estate, media and arts of the country. Despite the relocation of the federal government administration to Putrajaya, significant government institutions such as the Central Bank of Malaysia, Companies Commission of Malaysia, Securities Commission, as well as foreign embassies and diplomatic missions remain in KL. The city is equipped with the most advanced infrastructure development in the country, including the presence of KLIA and klia2 airports at Sepang, the Multimedia Super Corridor and the country's main seaport, Port Klang.

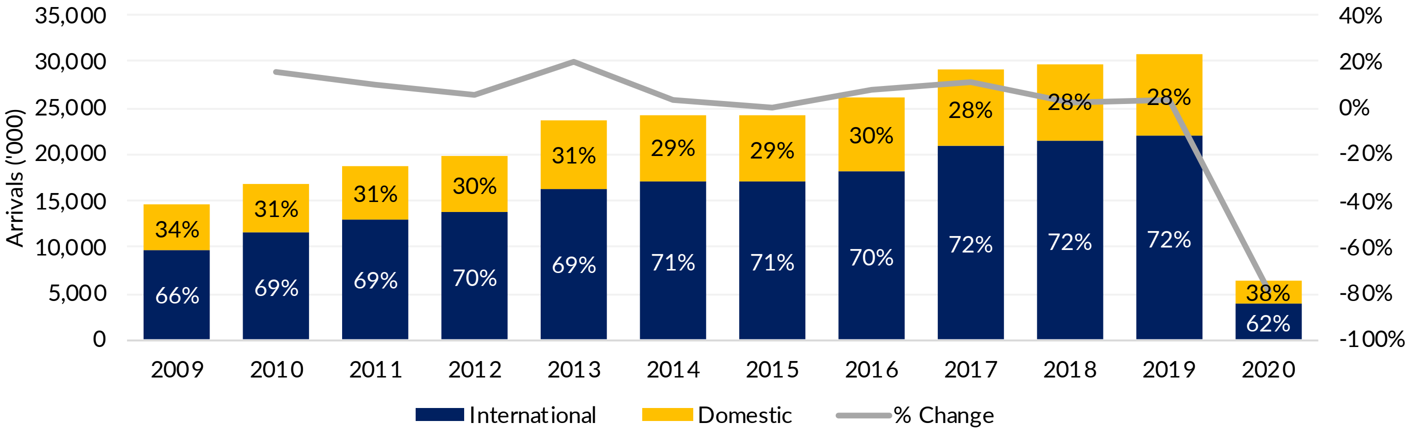
Over the years, KL (with a core population of over 1.8 million) has developed and expanded into the Greater KL (GKL) region, an urban agglomeration around 8 million people contributing 40% towards Malaysia's gross national income (GNI). The government recognises KL and its greater metropolitan area have a critical role in shaping and driving the country's economy and has included GKL as one of the 12 National Key Economic Areas under the Economic Transformation Programme. KL and its surrounding urban areas form the most industrialized and fastest-growing economic region in Malaysia.

As early as the mid-1980s, KL was dominated mainly by domestically managed hotels. During the next two decades, the market witnessed the entry of high-profiled international top-tier brands such as Mandarin Oriental, Ritz- Carlton, JW Marriott, Westin, Le Meridien, and Sheraton, that transformed KL from a once mostly unbranded hotel scene. The pace of new top tier supply slowed after the Grand Hyatt opened in 2012, and the next addition to supply would not be until the opening of the St. Regis in 2016. The top tier hotel inventory observed another influx in 2018 and 2019 with the opening of the Four Seasons, Banyan Tree, Pavilion Hotel (managed by Banyan Tree), Alila, W, and The RuMa hotels. In addition, the EQ Hotel (the former Equatorial) and the Sheraton Imperial went through major revamps and reopened in 2019.

With prolonged closure of borders and an ongoing pandemic, some top-tier hotels in KL decided to temporarily cease operations to mitigate the impact. The resurgence of infections caused by the Delta variant and the ongoing Covid-19 related restrictive movement measures will continue to have a disruptive impact on the operating performances in 2021.

This report analyses the historical performance of the top 24 hotels by class **(12 luxury hotels (premium 5-star) and 12 upper-upscale hotels (standard 5-star)** as categorized by STR Global) in KL and provides a projected trajectory of recovery for the top tier hotel market, with the consideration of comparable future supply entering the city.

Historical Arrivals to KLIA/klia2 (2009 - 2020)



Source: Malaysia Airport Holdings Berhad

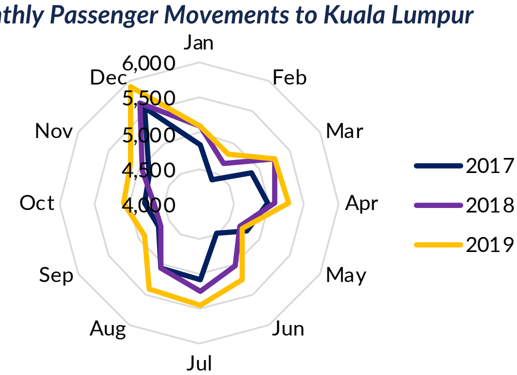
Visitor Arrivals

- The Kuala Lumpur International Airport (KLIA) began its operations in 1998 with a handling capacity of 25 million passengers per annum (mppa) and it has since been optimised to handle up to 30 mppa. The construction of the klia2, a dedicated low-cost carrier terminal, was completed in 2014, making it the world's largest purpose-built terminal, with a capacity of 45 mppa. Currently, the two airports have a combined capacity of 75 mppa.
- Between 2009 and 2019, the year-on-year (y-o-y) growth of the combined number of total passenger arrivals at the two airports was 8%, with a higher growth rate in international arrivals (9%) over domestic arrivals (6%). International passenger arrivals accounted for a larger proportion of total arrivals, at 72% in 2019.
- The number of passenger arrivals only declined in 2015, largely due to the aftermath of the double Malaysia Airline incidences in 2014, severe currency fluctuations during 2015, and route and capacity modifications by Malaysia Airlines.
- While lower growth rates were observed in 2018 and 2019, the number of airport arrivals slumped by nearly 80% in 2020 because of the strict travel restrictions following the COVID-19 pandemic. In addition, domestic arrivals took account for 38% of total arrivals, a notable proportion increase from prior years.
- KLIA / klia2 have set a target of 100 mppa to be achieved by 2030. Malaysia Airports Holdings plans to increase KLIA's capacity further, such as expanding the Main Terminal and introducing KLIA3.

Seasonality

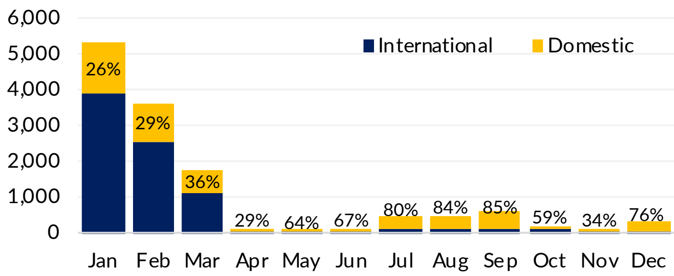
Seasonality trends were fairly consistent prior to 2020. A wide capture of different nationalities ensured that passenger arrivals were relatively stable throughout the year. However, there are still certain peak periods - March, July and December - which are months where major school and public holidays tend to fall into. The months of May/ June are typically low-yielding months due to Ramadan. In 2020, seasonality was severely impacted by the Covid-19 pandemic, as illustrated by the chart below.

Monthly Passenger Movements to Kuala Lumpur



Source: Malaysia Airport Holdings Berhad Note: Values are in thousands.

Passenger Movements at KL International Airport, 2020



Source: Malaysia Airport Holdings Berhad Note: Values are in thousands

Source: Westin Kuala Lumpur

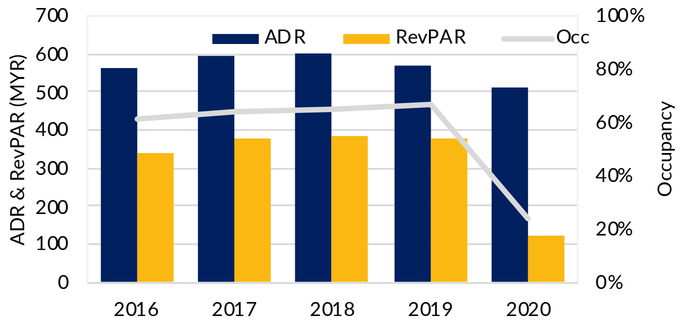
Top-Tier Hotels Occupancy and ADR

Overall, occupancy for KL's top tier hotels was consistently above 64% from 2016 to 2019, indicating relatively healthy demand and supply dynamics of KL's high-end hotel market. The market occupancy slightly slipped in 2018 due to the influx of new supply such as the Four Seasons, W, Banyan Tree, Alila and the Pavilion Hotel, and extensive renovations at the Sheraton Imperial. Occupancy quickly rebounded to 67% in 2019, which demonstrated the KL top tier hotel market's resilience in absorbing new hotel supply.

The average daily room rates (ADR) managed to maintain a growth rate in 2018 instead, as most of the hotels opened in 2018 were luxury hotels with a relatively small room count. However, the lagged pressure of new supply still impacted the top tier hotel market, which led to a 3% slide in ADR in 2019. 2020 was a devastating year for hospitality industry, and this is particularly true for the top tier hotels that targeted the more lucrative international demand. The national borders were shut off to international arrivals on March 18 2020 and has remained closed ever since. Although some upper-upscale hotels were able to capture some quarantine or Covid-related room nights, the occupancy and ADR for the top tier hotels declined by 58% and 17%, respectively.

Luxury Hotels

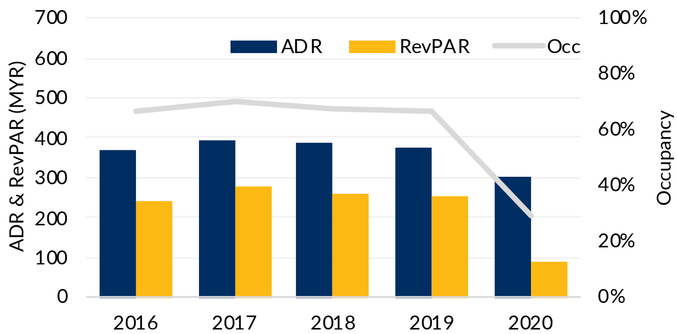
Despite the influx of new luxury hotels in 2018 and 2019, the luxury hotel market witnessed steady growth in occupancy from 2016, registering room-nights demand (RND) growth rates of 13% and 16%, respectively. This demonstrates the resilience of the luxury hotel market to pull in new demand. However, a slip in ADR was observed in 2019 mainly attributed to the pressure from increased inventory as well as shift in strategy by certain properties in maintaining higher occupancy levels at the expense of ADRs. In 2020, RND tumbled 64% from 2019 to an occupancy level of 24%, while the ADR showed a milder decline of 10% to MYR 514 from MYR570. Between 2016 and 2019 (pre-pandemic), the y-o-y growth in ADR was only 0.6% on the back of RND growth of 12% and RevPAR of 3.3%.



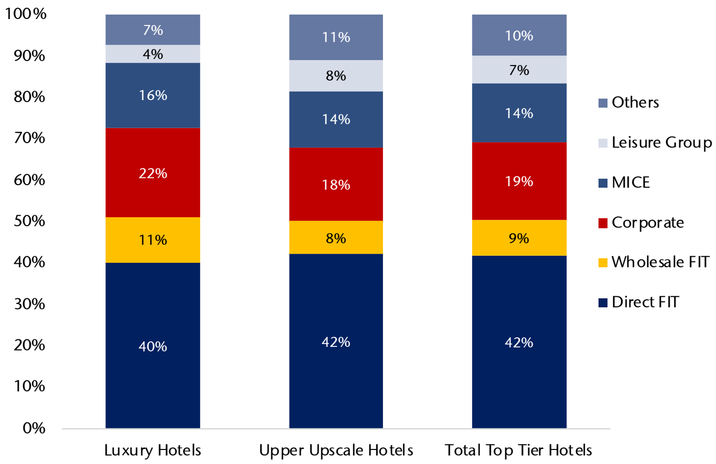
Upper-Upscale Hotels

Historically, the upper-upscale hotels achieved higher occupancy levels than the luxury counterpart, including in 2020. However, the ADRs have been declining since 2017 due to new supply and existing hotels adopting volume strategy.

In 2020, the hotels in this category suffered less decline in RND than the luxury hotels (53%) but higher decline in ADR (20% compared to 10% for luxury hotels), as a consequence of taking quarantine or Covid-related room-nights at a significant rate discount. Between 2016 and 2019, the y-o-y growth in ADR was 0.9% on the back of RND growth of 3.3% and RevPAR of 0.9%. .



Market Mix, 2019



Source: Horwath HTL

The **Direct FIT** segment dominated the top-tier market and accounted for 40% - 42% of total RND captured. The primary demand sources that contributed to this segment in 2019 include the following:

- Majority of the main attractions in KL are situated within the KLCC/Bukit Bintang areas. These areas tend to be popular among leisure guests due to its proximity to dining, entertainment and shopping options and major tourist attractions.
- Foreign leisure FIT travellers typically spent between two and three nights, using the city as a transit hub before heading to other destinations in Malaysia. Domestic tourists, mostly from Penang, Sarawak and Sabah, see KL as a favourable shopping destination or a weekend or school holiday getaway.
- During public and school holiday periods, Direct FIT and OTA demand tends to increase. This demand segment, however, is more susceptible to seasonality patterns compared to corporate demand.
- Direct FIT demand is usually a top rate contributor and is widely sought after by international branded hotels, given their powerful loyalty programs and centralised distribution channels.

As KL is a leading economic and business centre, **Corporate** demand had been a significant demand source. This demand segment has consistently been the second largest demand source. The following are major demand characteristics for the corporate demand segment:

- Location is a major contributing factor when corporate guests choose their accommodation. Corporate guests tend to stay in hotels close to their workplaces. Some corporate guests, due to loyalty programs or corporate rates, would stay at hotels further away from their work places. Furthermore, given traffic conditions in KL, especially during peak hours, corporate guests tend to value proximity. Naturally, hotels with offices attached have notable advantages. Internationally branded luxury hotels tend to have both significant corporate resources and terrific location when competing in this segment.
- Oil and gas companies, financial institutions, retailers, MNCs and state-owned enterprises are major sources of demand. Petronas and its associated companies as well as other oil companies are important room-night contributors.
- Room rates for this segment are one of the highest. Furthermore, demand is relatively stable throughout the year. Hence, corporate demand is very much sought after.
- Corporate demand is highest from Monday to Thursday nights. Weekends and public holidays are the weakest.

The **MICE** demand segment represented 14- 16% of room-nights. MICE demand was mostly in-house and corporate-driven, typically generated by companies with local presence. Leisure-related demand usually comprises weddings and social gatherings. Weddings were well received in KL due to the presence of a variety of high-profile hotels with prestige and desirability.

The **Wholesale FIT** and **Leisure Group** were the two minor demand contributors to the top-tier hotel market. Typically, these are volume-contracted rates, which are heavily discounted but crucial to a hotel's occupancy as it forms a base of demand, particularly during low seasons and weekends. Leisure group guests tend to be even more rate sensitive, which explains why the upper-upscale market captured more in this segment than the luxury market. Moreover, hotels with larger room inventories normally target this demand segment.

Others demand segment comprised government (without the use of meeting facilities), aircrew, long-stay, credit card promotions, associated and related companies, loyalty program redemption and walk-ins. In 2019, the Others demand segment accounted for 7% and 11% of total RND captured for luxury and upper-upscale hotel market, respectively. This demand segment has no real trend associated with the different capture levels of competitive properties.

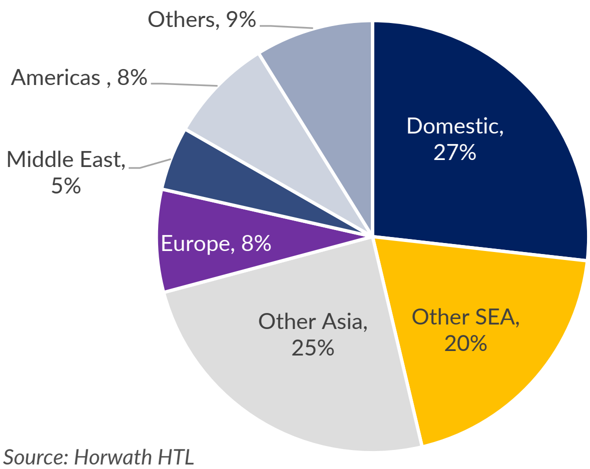
Nationality Mix, 2019

The **Domestic** market was the single most significant contributing by country to the KL top tier hotels' RND in 2019, accounting for 27%. The domestic market contributed demand across all the market segments. However, foreign demand still dominates at 73% of total RND.

In 2019, guests from **Other Asia** formed the second largest segment, with the Japanese and Chinese contributing the most. Demand from Japanese guests is typically corporate-oriented, whereas demand from Chinese guests is mostly leisure-based.

The proportion of **Middle Eastern** guests declined prior to the pandemic, probably due to increasing competitiveness among regional destinations in Southeast Asia as well as Europe.

Other major feeder markets included **Southeast Asia**, mostly from Singapore and Indonesia, as well as Europe, North America and Australia. Increased medical tourism, especially from Indonesia and South Asia was also observed.



Source: Horwath HTL

New Hotel Supply

KL is projected to witness several new hotels over the next 6 years. Most of these projects were planned prior to Covid19 but constructions were delayed to various degrees due to the pandemic. Although none of the new supply is opening in 2021 or 2022, there are over 3,600 rooms (13 projects) slated for completion over the next 6 years. Moreover, the 13 upcoming projects are all international chain-affiliated brands, implying that global hotel brands are endorsing the potentials of KL. The new supply listed below exclude the projects currently put on indefinite hold; also, it is likely that some of listed projects could be postponed or even cancelled in future.

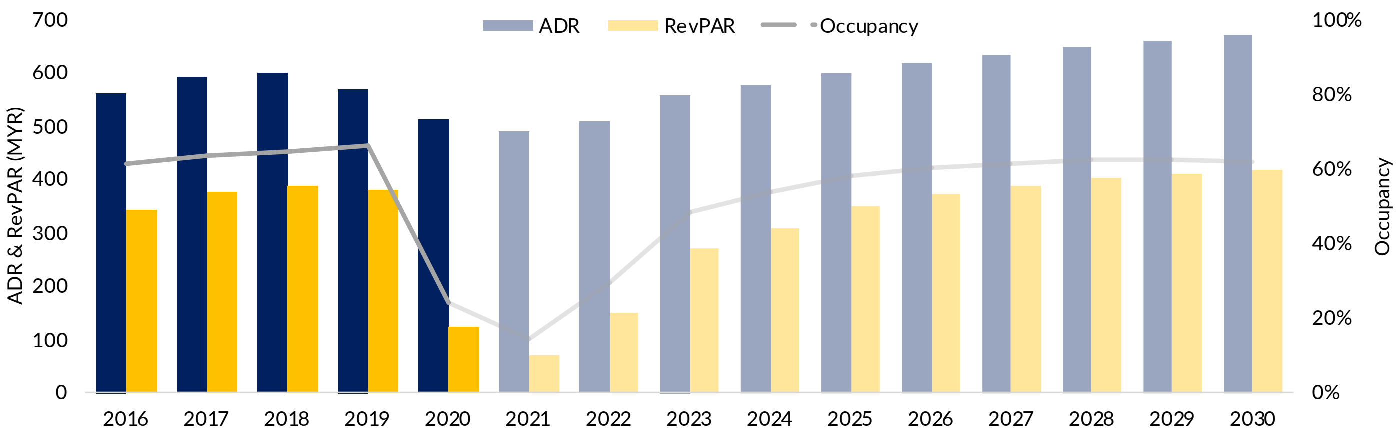
New supply

Luxury Class	Room Count	Expected Open Year
Conrad	504	2023
JW Marriott (extn)	160	2023
Kempinski Hotel & Residences	260	2024
Park Hyatt	232	2024
Jumeirah	190	2024
SO/ Sofitel	207	2024
Regent	250	2025
Edition	350	2026
JW Marriott (Sentral)	451	2027
Total	**2,604**	

Upper Upscale Class		
Hyatt Centric	430	2023
Hotel Indigo	180	2023
Kimpton	471	2024
Hyatt Regency	450	2026
Total	**1,531**	

Source: Horwath HTL

Luxury Market Occupancy & ADR Forecast



Source: Horwath HTL

Recovery: Not just a pandemic, but a changing competitive environment.

KL's top tier hotels are expected to register worsening performance in 2021 as Malaysia has imposed nationwide total or partial lockdown from February 2021 onwards. International borders remained closed and inter-state travel has been banned throughout most of 2021 so far.

Domestic tourism virtually dried up and staycations have not been significant enough. The Malaysian government has rolled out its vaccination program successfully and targets herd immunity for the country by the end of October 2021. In addition, the high infection rates in Selangor and KL in July/August will probably not see domestic tourism returning to KL until the last quarter of 2021. We estimate the 2021 year's performance of the top-tier hotels to decline further compared to 2020.

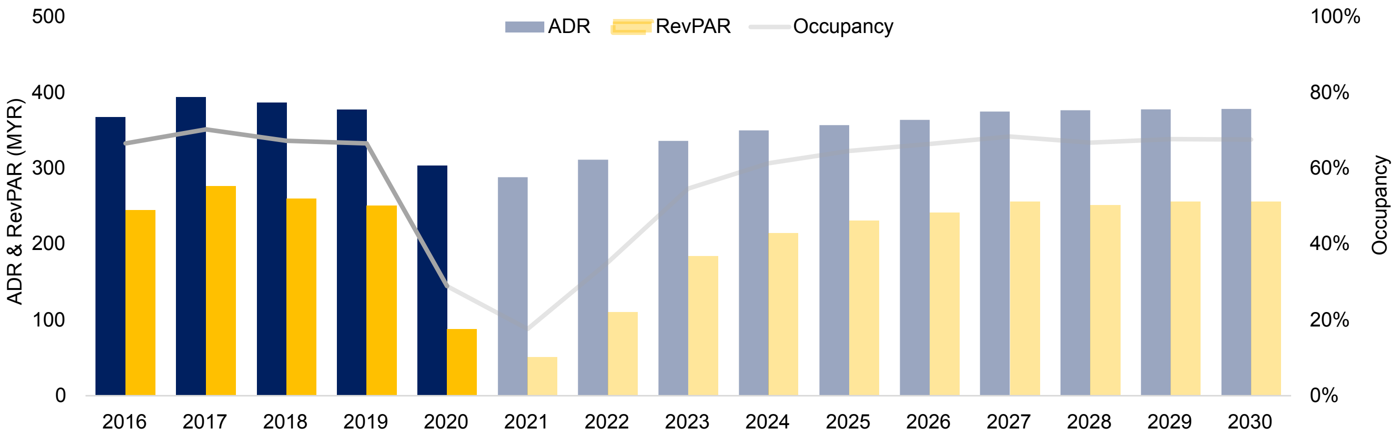
Malaysia commenced its vaccination program in Feb 2021 with a target of having 75% of its population vaccinated by the 4th quarter of the year. As of July 15, 2021, the Federal Territory Minister stated that more than 80% of the population of KL has been fully vaccinated. For the country as at August 31, 2021, close to 45% of its population has been fully inoculated while close to 60% has received the first jab. At the current daily average, Malaysia is targeted to achieve 75% herd immunity by mid-October.

It is reasonable to assume domestic demand will return in the 4th quarter 2021, especially in main tourist destinations such as Langkawi, Penang and Desaru. However, domestic travels could remain subdued on the back of nervousness and caution among Malaysians driven mainly by the more virulent Delta variant. National borders are expected to remain close until the end of the year.
Even if borders are open, most international travellers will stay away as they adopt a wait-and-see attitude. On the back of the foregoing, we project the occupancy and ADR of the top-tier hotels in KL to worsen in 2021 compared to 2020.

2022 is expected to see the national borders opening following the expected achievement of herd immunity by the last quarter of 2021. Demand for hotel rooms would still be dominated by domestic guests at least until the second half of 2022 when international arrivals begin to pick up pace.

The main country generators such as China, Singapore, Middle East (Saudi and UAE) and Japan are expected to immunize more than 75% of their population by the end of 2021, while Indonesia, India, South Korea, Thailand, Australia and Taiwan are expected to achieve herd immunity by mid- to 3rd quarter 2022. The following year, 2023, is not expected to see KL top-tier hotel demand return to pre-pandemic levels as some level of caution would still be carried over to 2023, especially in the first half of the year.

Upper-Upscale Market Occupancy & ADR Forecast



Source: Horwath HTL

Barring any unexpected events, 2024 is the year that the KL top-tier hotel demand levels (RND) return to pre-Covid days (i.e., 2019 levels). In the luxury segment, the significant entry of more than 1,550 guestrooms (2023 - 2024) is projected to induce some level of demand and contributes towards improving occupancy level. The pent-up demand following the pandemic is also expected to contribute higher occupancy levels.

In the upper-upscale segment, the new supply in 2023 and 2024 is not expected to impact the market occupancy levels, where the pace of demand growth will exceed supply growth (contributed mainly by pent-up demand). Over the longer term, we do not project the luxury hotel segment to achieve mid-60 percent occupancy (pre-pandemic levels) but rather in the low 60% range. The upper upscale hotel segment, on the other hand, will be driven mainly by high volume strategy that will see the segment occupancy level registering 2019 level from 2026 onwards.

Both the ADR y-o-y growth rates (2016 - 2019) of the luxury and upper upscale hotel markets have been below inflation rates.

For the luxury segment, the entry of high-profile brands such as St. Regis Four Seasons, W and Banyan Tree have failed to uplift the ADR considerably. In 2020, the growth rate fell 10% and it is projected to decline by another 5% in 2021.

The upper upscale hotels' ADR fell by a significant 20% in 2020 and we expect a further decline of 8% in 2021. The ADR growth rates beyond 2021 for both the luxury and upper upscale hotel segments would depend on the following factors:

- How soon will the ADR register 2019 levels?
- New supply entering the hotel markets.
- Yield strategy versus volume.
- The ADR differential between the two hotel markets.

With the country borders expected to open and international demand returning in 2022 and 2023, respectively, the luxury hotels are anticipated to uplift their room rates to clawback declines in 2020 and 2021. We project the 2019 ADR level to be achieved in 2024. The new luxury hotels supply entering the market by 2024 is expected to help elevate the average room rates ADR, due in part to their brand awareness and expected product quality.

With an enhanced critical mass of luxury hotels in the market by 2024, the luxury hotel market would be in a better position able to dictate its room rates, adopting a yield management strategy and lessen competition from the upper upscale hotels. We project the y-o-y growth of the ADR between 2020 - 2030 at 2.7%. (As comparison, between 2010 and 2019, the y-o-y growth of the ADR of the luxury hotel market was 2.3%).

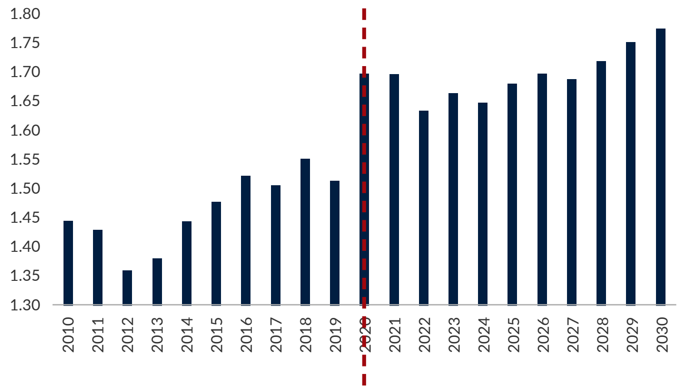
The upper upscale hotel segment is projected to continue its volume strategy at the expense of ADR growth. This will delay the hotel market to register it 2019 ADR, and we project the pre-pandemic ADR level to be achieve by 2028.

Only four new upper upscale hotels are projected to enter the market by 2026. The new entrants are not expected to uplift the market ADR significantly as there are considerable existing hotels in the upper upscale market that will continue with their volume strategy.

The y-o-y growth of the ADR between 2020 and 2030 is projected at 2.2%. As comparison, between 2010 and 2019, the y-o-y growth of the ADR of the upper upscale hotel market was 1.7%. The higher y-o-y growth rate 2020 - 2030 is contributed by the entry of brands that are high profiled that are expected to adopt yield strategy.

The ADR premium of the luxury hotel market over the upper upscale has grown significantly from 1.44 in 2010 to 1.51 by 2019. In 2020, it widened to 1.69 following the significant reduction in room rates amongst the upper upscale hotels. The rate premium is projected to hover in the range of 1.65 - 1.77 between 2024 and 2030 as the entry of more luxury brands is expected to widen the ADR differential.

Rate Premium 2010 - 2030



Source: Horwath HTL

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