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Mexico Hotel Market: A Robust Industry Navigates Uncertainty

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Industry Overview

The evolution of Mexico's hotel industry over the past 25 years has accompanied important structural economic and political changes, including greater integration to the global economy and the gradual, if at times inconsistent, construction of democratic institutions. It has similarly accompanied key trends in the global hotel industry, including development of a wide array of lodging products, rapid evolution of distribution systems, and merger and acquisition activity, to name just a few.

For Mexico, as well as other counties in Latin America, it is good to consider contextual elements. According to the World Tourism Organization (WTO), the tourism sector constituted approximately 10.4% of global GDP in 2018, representing about one in ten jobs around the world. This industry grew from an estimated 25 million international visitors in 1950 to over 1.4 billion in 2018. The WTO has forecast continued industry growth to reach 2.1 billion travelers by 2029. Historically, leisure travel has accounted for approximately 78% of total international travel spending, while business travel spending has equated to roughly 22%.

Mexico's has a robust hotel industry that runs across both business and leisure travel. While the official Ministry of Tourism (SECTUR) database places total hotel supply at 22,560 properties and approximately 808,000 rooms, an HVS analysis of more representative branded and non-branded hotels that might be visited by business and leisure travelers places the inventory at approximately 2,860 hotels and 358,200 rooms.

Branding Trends

In the hotel industry, as in others, Mexico has historically been receptive to international brands and has also realized the development of prominent domestic brands. Over the past decade, both Mexican and international brands have significantly expanded their footprints in both the business and leisure travel sectors. In Mexico's three largest urban areas, namely, Mexico City, Guadalajara, and Monterrey, the presence of branded hotels is relatively high, at 66% of the rooms inventory. In a large sample of other urban and industrial centers, the branded rooms inventory is equal to 55% overall, but varies by specific market. Meanwhile, Mexico's extensive inventory of resort properties exhibits a high degree of branding, at 76% of rooms inventory.

Mexico Branding Trends by Market Type

	Total		Percentage of International Brands		Percentage of Regional/National Brands		Percentage of Independent Brands	
City	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms
Mexico, Guadalajara, Monterrey	503	66,761	30 %	40 %	20 %	26 %	50 %	34 %
Other Urban-Industrial Cities	1,620	138,420	19 %	28 %	18 %	25 %	64 %	46 %
Resort Areas	741	153,011	34 %	57 %	14 %	19 %	52 %	24 %
Total	**2,864**	**358,192**	**25 %**	**43 %**	**17 %**	**23 %**	**58 %**	**35 %**

Source: HVS

These data illustrate both an acceptance of and potential for greater penetration by hotel brands in Mexico. In fact, the activity of national and international hotel chains confirms this trend, since many seek to enter their market or expand their presence. Some chains look to grow through one-off deals with local developers that control a site, while others seek to establish master development agreements with developers in pursuit of portfolio investment strategies.

Selected New Brands in Mexican Hotel Market

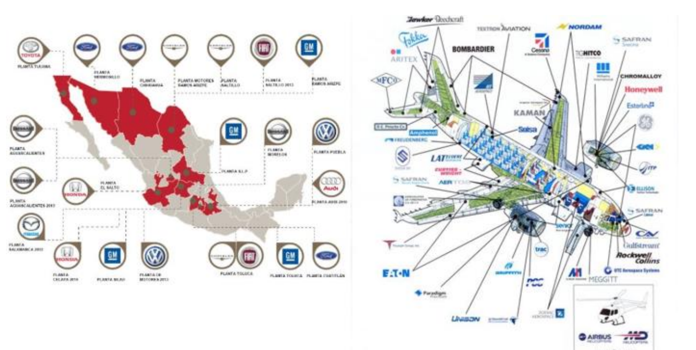
Trends in Business Lodging

Mexico's economy has been and remains on a path of integration with the global economy since 1992, driven in large part by entry into the North American Free Trade Agreement (NAFTA) with the U.S. and Canada, and the resulting shift from a commodity-based economy highly dependent on oil exports to one driven by export manufacturing. Shifts in the economy spurred significant increases in Foreign Direct Investment, giving rise to increased demand for hotels that might service business travel. Following the U.S. presidential election of 2016, trade relations between the U.S. and Mexico came under review, with detailed negotiation of a new version of NAFTA. As of the current date, the U.S., Mexico, and Canada had agreed to terms for a new agreement, referred to as the U.S.-Mexico-Canada Agreement (USMCA), which is to be fully ratified by each county's legislative body in the coming months.

Mexico's economy is currently experiencing considerable uncertainty, following the inauguration of the Andrés Manuel López Obrador administration in December 2018. Initial signals on the direction of the new administration have been mixed. The announced cancelation of a partially completed airport facility in Texcoco (on the outskirts of Mexico City) and the unsettled investment markets may result in the potential for select travel-related growth to go unrealized. It remains to be seen if the Santa Lucia airport facility proposed by the new administration will be completed, and this, in part, makes up for what seems to be a lost opportunity. Separately, it is possible that private airport operators in cities such as Guadalajara, Monterrey, and Cancún will be able to expand their platforms to pick up the slack.

The economy has been flat over the past year and currently hovers near recession. If public and private investment in infrastructure pick up in 2020, and if the USMCA comes to be ratified, it is possible that the current unease will subside in some measure, leading to mild economic growth. Current economic estimates project GDP growth at 1.08% and 1.80% for 2020 and 2021, respectively. The new administration has vowed to reduce corruption and to improve security measures. Any progress regarding these issues would be welcome by all sectors of Mexican society.

Selected Economic Drivers – Auto and Aeronautic Industry Participants



Source: Automotive Meetings and MexicoNow

Recent uncertainty and a strong U.S. dollar had caused a gradual devaluation of the Mexican peso over the past three years, creating short-term inflationary pressure, as well as rising interest rates. As the economy has faltered, interest rates have recently been adjusted downward. While different elements are likely to have some impact on economic conditions in the short term, economic analysts tend to agree that Mexico remains well positioned, with fairly sound fundamentals, and that the mid- to long-term impact of these issues is likely to be moderate.

The faltering economy in 2019 has had a limited effect on business lodging. In most urban markets, occupancies are off, generally by one to three points, while average rates have dropped by 3% to 5%. Uncertainty has curtailed new investment and related business travel, as well as some group business. In some markets, including Mexico City and Monterrey, planned supply additions remain in the pipeline. In smaller markets, recently expanded hotel inventory footprints and limited economic activity have resulted in limited development.

Trends in Leisure Lodging

Mexico enjoys a robust leisure sector, with a history that spans many decades. The initial development of mythical destinations, such as Acapulco and Puerto Vallarta, have received domestic and international visitors since the 1960s. The country increased its visibility notably as an international destination by hosting the Olympic Games in 1968 and the first of two World Cups in 1970. Today, it ranks among the top ten travel destinations in the world, as measured by tourist arrivals.

Key markets in Mexico are found in the Cancún–Riviera Maya Corridor, Los Cabos, and the Puerto Vallarta-Nayarit Corridor. In the coming years, several markets could enter new growth and consolidation phases, provided that infrastructure improvements, proper planning, and the development of a quality hotel inventory are pursued. Such markets include Mazatlán, La Paz, the Costa Alegre Corridor, and the Huatulco-Puerto Escondido Corridor.

Over the past 15 years, the composition of Mexico's hotel offering has changed, as the traditional inventory of European Plan (EP) hotels has been complemented by a significant inventory of properties operated under the All-Inclusive (AI) model. As acceptance of this format has expanded, AI hotel chains have varied their products, achieving segmentation by location, type of experience, product offering, and guest profile. Notwithstanding the growth of the AI concept, EP hotels remain relevant, offering carefully positioned experiences, frequently associated with hotel chains with a vast global reach, extensive loyalty programs, and solid administrative platforms. In fact, across Mexico, EP and AI hotel inventories are viewed as being complementary. Together, they generate lift, promote destinations, provide for an active work force, and bring vendors of goods and services to market.

Supply of Four- and Five- Star Hotels – Selected Leisure Markets

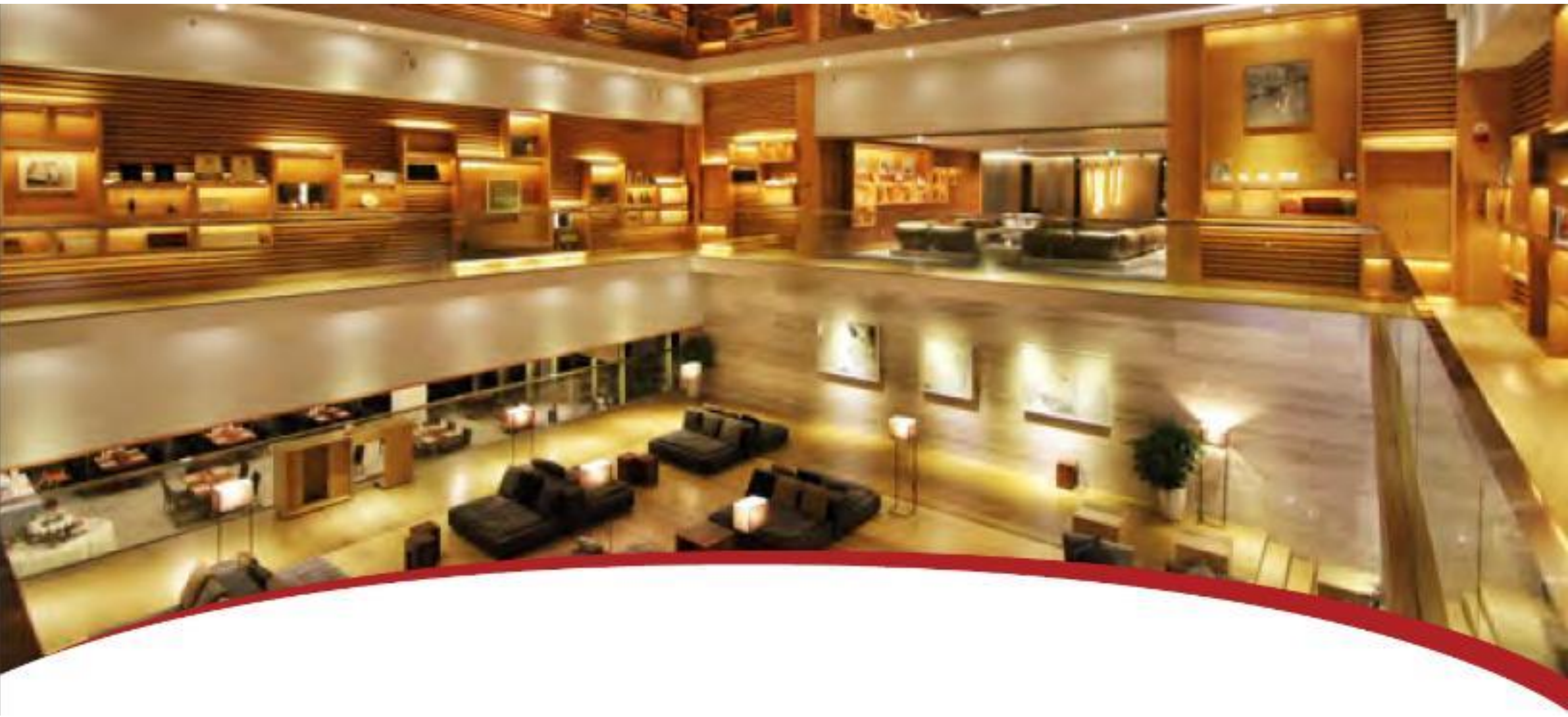
	European Plan			All-Inclusive			
	Number of Hotels	Number of Rooms	%	Number of Hotels	Number of Rooms	%	Total
Cancun	47	9,295	20%	68	37,368	80%	46,663
Riviera Maya	83	5,861	12%	86	44,775	88%	50,636
Puerto Vallarta	83	14,086	52%	19	12,924	48%	27,010
Riviera Nayarit	23	2,269	22%	23	8,203	78%	10,472
Los Cabos	43	5,413	36%	30	9,831	64%	15,244
Acapulco	71	11,429	84%	6	2,107	16%	13,536
Ixtapa-Zihuatanejo	23	1,995	36%	12	3,507	64%	5,502
Huatulco	40	1,822	47%	8	2,039	53%	3,861
	413	**52,170**		**252**	**120,754**		**172,924**

Source: SECTIUR, HVS

The luxury hotel market in Mexico is well established but often receives less attention than larger and more visible segments of the market. Certain luxury hotels in Mexico are recognized in the United States as premium destinations for high-end guests and celebrities. In fact, it is worth noting the wide and diverse range of luxury hotels in Mexico and the potential to grow in this segment, as it constitutes a differentiated leisure segment. Mexico offers some 48 luxury properties accounting for 5,473 rooms. A select number of hotels in Mexico reach average rates in the range of $500 USD to $800 USD, and a handful exceed this range. However, average rates are not considered the only parameter for an asset's designation in a luxury designation. Rather, certain hotels under domestic and international brands are positioned as luxury products, even with somewhat lower average rates, based on the experience that combines a highly differentiated location, product, and level of service.

Mexican leisure destinations have an established track record in planning and executing master-plan projects that combine hotel and residential components. In the 1970s, the Mexican government introduced the National Fund for Tourism Promotion (FONATUR), with the mandate of creating a platform that could facilitate the development of select leisure destinations. Initially in Cancún, and in other destinations later, FONATUR created large-scale, master-plan projects characterized by clear land tenure, relatively good infrastructure, and attractive recreational amenities. Although the results are uneven among destinations created by FONATUR, the fund anchored development initiatives along the Caribbean, Pacific, and Baja California coastlines. Over time, private developers undertook carefully planned and executed projects under similar premises. Mexico is at the forefront of this type of development, with a vast offering that has served as a development platform for domestic and foreign investors.

Over the past year, as business markets have experienced declines resulting from economic and political uncertainly, most leisure markets have similarly felt limited impact. In addition, the current government eliminated Mexico's federal tourism promotion agency, the Consejo Nacional de Promoción Turística, shifting responsibility for such functions on state and municipal governments and private hotel owners. In some market areas, occupancies have been slightly off with more significant declines of 3% to 5% in average rate. Still, investment activity remains buoyant, as hotels in vacation destinations tend to generate U.S. dollars and depend largely on international travel rather than local economic drivers. Along Mexico's Caribbean coast, some impact has been associated with an expanding seaweed patch of Sargassum that stretches across the Atlantic Ocean. Local authorities and property owners have taken steps to mitigate this issue. An additional element of risk is presented by security concerns of varying degrees in different Mexican resort markets. While serious incidents involving tourists are extremely rare, certain regions of Mexico confront problems related to drug trafficking that government authorities seek to curtail. The impact of this phenomenon is compounded by the adverse effect it brings to Mexico's image. Notwithstanding challenges, Mexico's hotel leisure sector is well positioned. Mexico's location bordering the U.S., the quality of visitor experiences, and a growing inventory of hotels offering a high-quality product should combine to allow for increased demand.



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