

# Caught in the Crossfire – the Impact of the Recent Uprisings in the Arab World on Regional Hotel Values

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## Recent History

The Arab world has been growing in importance and influence in recent years, which has resulted in increased interest from hotel operators and investors. From an operational perspective, both leisure and commercial trade have grown exponentially throughout the region, although Egypt has long been highly dependent on tourism, which accounts for 11.5% of GDP. Libya, on the other hand, has benefitted from the relatively recent release of sanctions and, until recently, the acceptance of her leaders by the Western world. The number of quality hotels in and around Tripoli was expected to increase at a CAGR (compound annual growth rate) of 17.8% from 2010 to 2014\*. Libya is now the twelfth largest oil exporter in the world and is such an important supplier that the price of Brent Crude oil increased as a result of the country's recent anti-government protests, with talk and rumour of the price reaching US\$200 per barrel. It was below US\$85 in late 2010. This increase in oil prices affects consumer confidence and also the cost of travel, potentially reducing the number of guests at a hotel. It can also increase the cost of supplies to a hotel.

Marrakech has increased in popularity and is now seen as both a short and longer-break destination. In fact, much of this region is now widely accepted as a winter sun destination for the mass markets in northern Europe. On the back of this increased acceptance and interest in Morocco as a holiday destination, many hotels have recently opened or are due to open in the country. Nervousness from travellers may impact the number of tourists to the region as a whole, whether or not that country is suffering from unrest. Morocco and Tunisia are not the only high profile destinations to be affected; Bahrain was becoming increasingly popular and even Yemen had started to enjoy increased tourism. All are already experiencing a significant dip in demand in 2011.

## The Unrest – the Impact on Trading Performance

Whether or not a hotel property has been physically damaged during the protests, the short-term impact on those hotels caught up in the midst of the unrest has generally been dramatic, particularly in Egypt and Libya where both employees and guests have been unwilling to travel (or leave) the hotel. There were reports from the coastal resorts of Tunisia of holidaymakers being trapped inside their accommodation. These situations are short-term and are only relevant during the protests. But, what happens once the protests are over?

## Commercial Trade

Oil companies in Libya are reported to be running at a fraction of capacity, or have shut down altogether. Whilst this is perhaps only a short-term reaction, with all or most of the foreign workers having left the country, there will be a delay before production is running at high levels again. The return of foreign workers will help to the boost hotel occupancy; a potential positive short-term reaction may be foreign workers choosing the security of hotels rather than apartments when they return. Previously many will have had apartments, but they may now not want to commit to a long-term contract and also favour the safety of a hotel. However, workers on long-term assignments may opt to use apartments rather than hotel rooms for additional space and comfort. Visitors to the various industries are likely to take longer to return and it is these workers that many hotels depend on. It is likely that companies will be cautious about flying anything more than the minimum of staff into presently unstable locations once the situation improves. However, there may be opportunities for hotel demand from consultants reviewing the region's business and any damage, which could replace some of the longer-term

## Summary

This article highlights the impact that the pro-democracy uprisings in countries such as Tunisia, Egypt and Libya have had on the region's hotels, including dramatic changes in values.

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losses. Travel insurance may also be a problem, with companies unlikely to issue cover, or at least reasonably priced cover, until governments remove any travel restrictions.

### **Tourism**

The short-term impact of the protests on tourism is clearly dramatic: no holidaymaker is interested in visiting a war zone. However, hopefully the violence is short-term and, once the country is considered to be safer, hotel owners, operators and governments will be keen to welcome back tourists as soon as possible. It is unlikely that travellers will return in the same numbers immediately, however cheap the holiday, so the region should experience a slow return of confidence, which may take years rather than months, depending on the outcome of the troubles. It is encouraging to note that previous major disruptions to travel and tourism in the region have resulted in a relatively quick recovery – people's memories appear to be quite short in this regard.

In the longer-term, however, this could prove to be good news as travel and visa restrictions may be eased; this would make visiting these countries simpler and promote tourism, and in particular short breaks.

### **Damage to Infrastructure**

Once the conflicts are over the speed of the region's recovery will also be determined by the amount of damage inflicted to buildings and the infrastructure. If, for example, airports or roads require repair or rebuilding, access to hotels and resorts will be limited and may deter travellers. Similarly, if hotels require repair to become habitable or have a reduced rooms stock, the available income will be decreased. Hoteliers will also have to check that their suppliers are still able to deliver, and in sufficient quantities, before they re-open their doors for business.

This same argument applies to the labour of a hotel and its suppliers. Many employees may have been injured, or worse, during the violence. Finding a suitable workforce and potentially training new employees may reduce the capacity of hotels further in the short-term.

However, in the longer-term, once these immediate issues are resolved, the market may find itself able to deliver recently refurbished hotels with improved infrastructure to the international market, and thus enjoy a more rapid increase in trade, perhaps to levels not previously enjoyed. Additionally, with a potentially freer movement of the labour force and a growing economy the local employees should become more skilled and experienced. Whilst this may lead to a higher labour cost in the country of operation, it could also reduce the need for foreign workers and thus reduce overall labour costs.

### **New Supply**

Concerns over the oil price coupled with the general unease in the region have slowed the decision-making process for many developers considering whether to invest in the market. Whilst this is frustrating, it may also help the recovery. For example, if hotel market supply remains static or has even reduced as a result of damaged properties there are fewer rooms to be filled. This could lead to a stronger percentage occupancy, which will boost confidence and should therefore speed up the recovery of the market. The delay of some of the many proposed hotels should also aid the recovery and allow the existing hotels to restore demand levels. This will provide a strong base and foundations for the overall development of the region's hotel industry.

### **The Impact of the Recent Worldwide Downturn**

Many of the Arab world's cities and countries have been developing a short-break market, so they suffered when an air of caution over household spending crossed over Europe. However, this came after several years of significant growth and was seen as a blip on an otherwise upward trend. Unfortunately, even those countries that are considered stable will now suffer from the volatile perception of the region and also the impact of increased oil prices, with the cost of travel and supplies both likely to increase, reducing occupancy and profits. The short-break market for the Arab world is likely to be affected for several years. Hotels therefore have to reconsider their target markets and perhaps look closer to home and concentrate on attracting tourism from other parts of the region and especially from within their own country.

In the West, there remains a keenness to travel to and a desire to explore this exciting and historic part of the world, although we suspect it may take a number of years for the region to fully recover. Other markets that visitors have shied away from in recent years, such as Greece and Spain, may now become the main beneficiaries

of any tourism downturn in the Arab world.

## Conclusion

The value of hotels in the short-term has clearly been impacted by the conflicts, but depending upon the final outcome the uprisings may prove to be beneficial and result in record values in the longer-term as the market recovers.

From an investor's perspective, if the changes in the region are permanent and lead to a style of government which is acceptable to the Western world, each country will benefit from almost unlimited assistance to create a stable economy and democracy. This in turn should lead to improved trade and a steady but growing economy, and, given the natural resources in the Arab world, this should then encourage investors to consider the region once again.

Regarding hotel performance, commercial trade is likely to return before tourism. Although companies may be willing to ask employees to explore the 'new world order', families may not be as quick to choose the region as a holiday destination. A boost in hotel trade from the returning commercial segment should lead to an increase in values prior to any improvement in valuation parameters. The parameters will only improve once investor sentiment and appetite for the region returns. And with both an increase in trade and improved sentiment hotel values could eventually reach record highs. Our research suggests that values may have fallen by more than 50% in the short-term but based on the positive assumptions mentioned above could increase by circa 35% above previous levels once a stable environment is established.

On a similar note, if the uprisings are followed by a temporary period of disquiet, once order has been restored and economic and political stability demonstrated, the appetite to visit the region should return. A lingering potential problem could occur if there is no definitive result from the protests, for example if Libya remains divided with an unpopular leader and economic sanctions. If the existing governments remain in power but promise to make changes to their countries, this could have a big impact on hotel values. That level of instability could undermine all of the hard work recently undertaken and neither visitors nor investors will be encouraged by a 'wait and see' result.

The overall impact on the region's trade will not be clear for a number of months or years, but one thing is certain – it will be an interesting ride ahead for hotel operators and owners.

\*CW Hotel Beat May 2010

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