MARKET REPORT

HVS South America Outlook & Opportunities 2023: Clearing Skies Ahead

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Brazil

After overcoming the impact of the Omicron variant, the Brazil hotel market began a notable recovery. The demand growth allowed average daily rate (ADR) to increase. In 2022, most of the major cities recorded a RevPAR close to the 2019 level, and those with a sound mix of corporate and leisure demand even surpassed 2019 levels. The resort market was a key driver. While former president Jair Bolsonaro's supporters generated political turmoil in October 2022 after his defeat in the presidential election that year, this disruption had little impact on hotel demand.

The first months of 2023 show an upward trend both in occupancy and ADR, which is expected to continue during the remaining months of the year. With a modest new supply pipeline, hotel performance is anticipated to continue improving, indicating opportunities for new developments. In the Brazilian resort markets, there are ample opportunities

for leisure-oriented developments, from standalone European-plan or all-inclusive properties to master-planned developments. Also, international brand penetration in key markets is still low, representing opportunities to increase their footprints. The high interest rates and the lack of available financing remain the primary challenges for investors.

Peru

Peru’s sound economic performance in pre-pandemic years translated to solid hotel results and attracted investments not only to Lima but also to regional business travel cities and leisure destinations. Some markets suffered from sudden increases in supply just before, during, and after the height of the pandemic. The combination of increased supply and reduced demand resulted in lower occupancies and ADR. Many properties faced difficulties meeting their debts, which caused commercial banks to stop financing new projects. The brief term of former president Pedro Castillo from July 2021 to December 2022 added uncertainty to the markets, causing many investments to remain on hold or be canceled.

Violent protests started in Peru when Congress removed the then-president from office and his vice president Dina Boluarte became Peru's head of state. The unrest, which continued from December 2022 to mid-February 2023, affected the hotel industry because many airports were closed for several days. Therefore, many trips were canceled in Q1 2023. Also, reservations for groups and leisure guests during the remainder of 2023 were canceled or postponed. As a result, the outlook for 2023 is modest for several of Peru’s key hotel markets.

However, with the political situation currently under control (though still fragile) and hotels operating normally, demand is expected to return, and new supply is anticipated to be absorbed. The expansion of Jorge Chavez International Airport is anticipated to be a key driver and to set a new pattern for travel. With a rigid lending environment, many projects are on hold or canceled. This trend, together with sound economic prospects, strong lodging demand fundamentals, and reasonable hotel operating costs, could represent an opportunity for investors, especially in select destinations within northern Peru and for leisure-oriented products associated with natural resources and local culture. Some urban destinations also present opportunities on a targeted basis.

Colombia

The pandemic caused a severe economic recession for Colombia in 2020. During that time, social unrest and public demonstrations frequently escalated into violent events with police and military involvement.

Colombia's 2022 presidential elections put some companies' investment decisions on hold, affecting corporate travel in the short term. However, in 2022, hotel demand in Colombia significantly increased in all segments. Some markets, like Cartagena, Santa Marta, and Medellin, observed impressive rises in both occupancy and ADR.

In 2023, the hotel performance is expected to continue a recovery. The country's potential in the leisure sector and meeting and events segment, together with strong domestic demand and reasonable operating costs, indicate considerable opportunities for future development in leisure destinations and targeted opportunities in business markets. The main challenges are increasing development costs and interest rates.

Argentina

Argentina had some of the tightest restrictions and longest quarantines related to the COVID-19 pandemic. In Q1 2022, occupancy for the country was less than 80% of the 2019 level. Beginning in the second quarter, as corporate demand and meetings and events returned and leisure demand continued to grow, occupancy experienced a pronounced increase, reaching the 2019 level in Q4 2022.

The economy is expected to contract in 2023 due to runaway inflation, a falling peso, depleted savings, high interest rates, and uncertainty due to October's presidential elections. However, the outlook for the hotel industry is optimistic for 2023 since the corporate and group demand segments are expected to grow, albeit at a slower pace. Leisure demand is also anticipated to increase; we expect that this segment will be the most affected by the low cost of Argentina as a result of a weak peso. In the context of growing demand and currency devaluation, several markets have experienced improved operating margins, although the market is affected by high inflation, since hotel rates tend to adjust faster and more significantly than operating costs.

Argentina presents select opportunities for hotel brands to increase their footprints, as several of the country's secondary and tertiary cities are underserved by quality hotel supply. Also, brand penetration in Buenos Aires is limited, creating opportunities to develop midscale and upscale products. With regions and attractions like Patagonia, Mendoza, and Iguazu, among others, Argentina is well positioned for investments related to luxury and experiential tourism. Due to the lack of financing and risk perception of the country, most of the hotel developments are anticipated to be undertaken by local investors.

Chile

The hotel industry in Chile was one of the most affected by the pandemic in South America. The change of president in Q1 2022 also influenced hotel demand. The market's demand gradually recovered in 2022, with occupancy surpassing the 2019 level in the fourth quarter.

The hotel outlook for 2023 is moderate since the economy is forecast to slow slightly. China's reopening is anticipated to contribute to the Chilean economy's improvement in the short term, while mining strikes and higher-than-expected inflation and interest rates are downside risks. Despite the challenges, economic fundamentals remain solid, and Chile's hotel outlook is favorable, with a moderate new supply pipeline.

In terms of developments, opportunities remain modest in select business destinations, as well as for boutique hotels in markets associated with natural resources. Chile features large and sophisticated financial markets and a great number of important institutional investors when compared to other countries in South America. However, access to hotel

financing is currently limited, as many hotels faced difficulties meeting their debts during the pandemic and as interest rates increased. As Chilean markets recover and new opportunities arise, financing for hotel projects is anticipated to return.

Conclusion

The hotel industry throughout South America has recently faced challenges. Most of the countries were severely hit by the pandemic, and recent presidential elections generated political and economic unrest or uncertainty, temporarily affecting lodging demand and causing some investors to enter a "wait and see" mode. In some countries, left-wing presidents won, and political turmoil followed. A less supportive external environment also influenced the investment climate through such factors as higher development costs and tighter financing conditions.

Despite these issues, most markets have continued to recover. The pace of recovery has been different in each market, depending on its drivers. In general, the recovery in certain leisure and industrialized areas is going relatively well, while full-service hotels in capital cities and other large urban centers are recovering more slowly.

There is interest in business lodging opportunities on a targeted basis and for urban mixed-use projects, as well as potential for brands to expand their footprints in secondary and tertiary cities and in specific segments of the region’s primary markets. Leisure markets also provide opportunities for the development of luxury products, lifestyle-oriented and all-inclusive standalone hotels, and master-planned and mixed-use projects. Countries like Ecuador, Uruguay, Bolivia, and Paraguay present opportunities on a select basis. Several South American countries are attractive because much remains to be done. In many countries, the potential to attract regional and international demand is considerable, and in many markets, development and operating costs are lower than in more developed economies, potentially allowing for higher returns. The rhythm of new developments will be influenced mainly by inflation expectations, interest rates, and access to reasonable financing.

Please reach out to Fernanda L'Hopital if you would like further insight or require assistance with a development in South America. She would be excited to advise on the projects and investments you are considering in the region.