



APRIL 2018

SOUTH KOREA OVERVIEW

OPPORTUNITY: HIGH-SPEED RAIL AND WINTER OLYMPICS

Jaehyun Yoo

Manager

Daniel J Voellm

Managing Partner



South Korea Tourism Overview

Korea is a popular tourist destination for both Japanese and Chinese visitors, who, when combined, accounted for nearly 50% of its total international visitors in 2017. The geographic proximity plus its charming tourism offerings are ideal for short getaway visits, particularly to the capital city Seoul.

The Korean tourism industry is driven by the peppy cultural trend called ‘Hallyu’, also known as the Korean wave. Originating from popular media, including K-Pop artists and TV dramas, it gradually spread to industries such as cosmetics, food, electronics, etc. According to the Korea Foundation for International Culture Exchange (KOFICE), the Korean wave effect on production inducement was estimated to be approximately KRW 15.6 trillion (USD 14bn) in 2015.

Among the numerous regional tourism destinations, Korea consistently ranks within the top 5 destinations for Chinese travelers for more than 10 consecutive years.

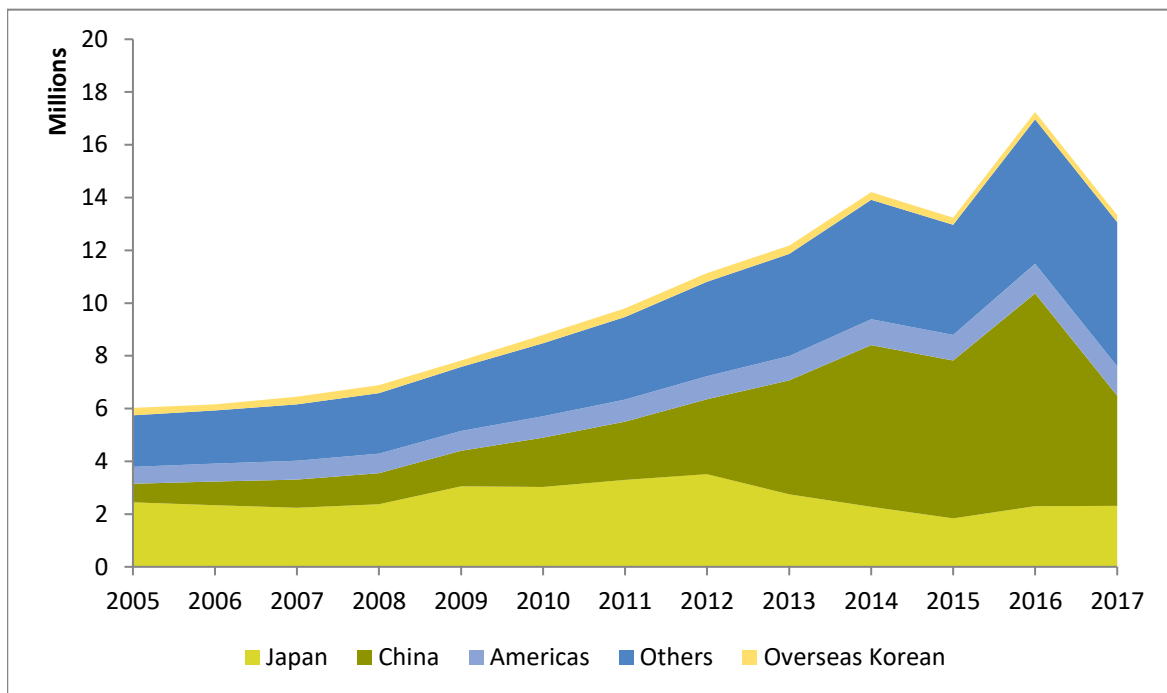
STATUE OF KING SEJONG & KEY DESTINATION IN SOUTH KOREA



The Korean peninsula protrudes into the sea between China and Japan. The west coast of the Korean Peninsula is bounded by the Korea Bay to the north and the Yellow Sea to the south; the east coast is bounded by the East Sea. Two hundred kilometers of open water separate the peninsula from eastern China. The Japanese islands of Honshu and Kyushu are located approximately 200 km to the southeast.

The total area, including the surrounding islands, measures 99,720 km², of which about 99% (96,920 km²) constitute the land area of the Republic of Korea. This includes about 3,000 islands. Jeju Island, which lies off the southwestern corner of the peninsula, is the country's largest island.

FIGURE 1: VISITOR ARRIVALS 2005-2018



Source: Korea Tourism Organization, 2018

Visitor Arrivals

In 2005, South Korea recorded total international visitors of 6.0 million. The majority of international visitors were Japanese, at 2.4 million, which accounted for approximately 40% of the total international visitor arrivals, followed by China and the US at 11.8% and 8.8%, respectively. While total international visitor arrivals increased in subsequent years, Japanese visitation levels decreased at a compound annual growth rate (CAGR) of 19.5% between 2012 and 2015 due to an unfavorable exchange rate between the Korean Won and Japanese Yen. However, following the easing of visa restrictions for mainland Chinese, the Chinese market registered very strong growth, compensating for the decline in Japanese visitors, further boosting the local tourism industry. In 2016, total inbound visitor arrivals to South Korea reached an all-time record high, at over 17 million. However, in 2017, South Korea suffered a significant decrease mainly from the Chinese visitor arrivals which was triggered by a political event between China, North Korea, South Korea, and the United States (US).

Threat: Political dispute

The Korean peninsula is divided into two nations, the Democratic People’s Republic of Korea (North Korea) and the Republic of Korea (South Korea). Sixty-three years after the hostilities of



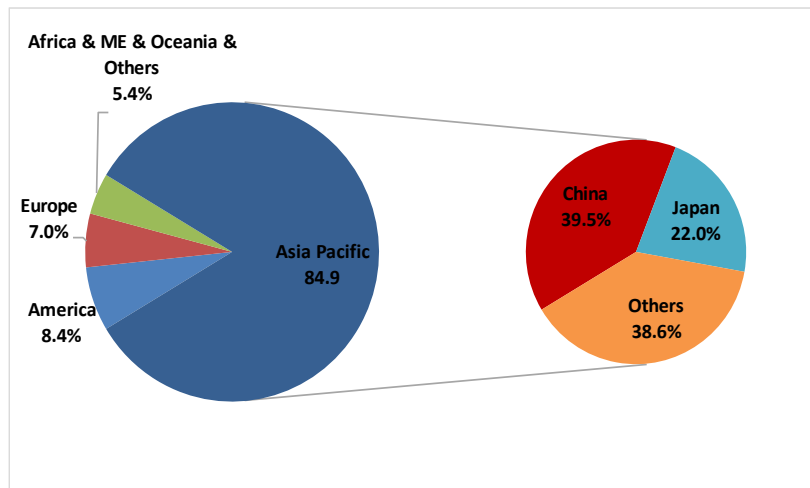
Source: Local Media

the Korean war ended, no peace agreement has been reached and both countries are only in a ceasefire state, leading to military and political risks between the two and neighboring countries. Following a series of nuclear weapons test and missile launches, South Korea together with its US allies agreed to deploy the Terminal High Altitude Area Defense (“THAAD”) Missile system in 2016. The

deployment was strongly objected to by the Chinese government as THAAD’s radar called TPY-2 has a range of 2,000 km, posing a threat to Chinese national security.

Impact on the South Korea tourism industry

FIGURE 2: INTERNATIONAL VISITOR BREAK DOWN BY NATIONALITY 2017

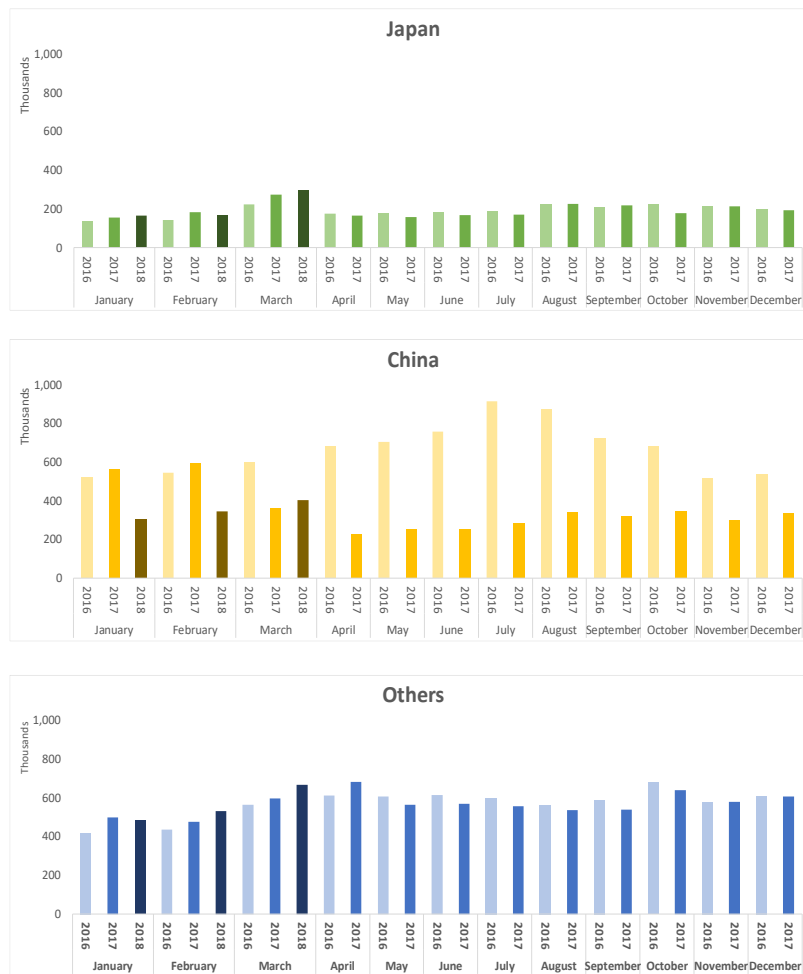


The South Korean tourism industry depends heavily on Chinese tourists. In 2016, over 8 million Chinese visitors visited Korea which accounts for roughly 48% out of total international arrivals and 55% of all Asia Pacific. However, in 2017, subsequent to the THAAD deployment

decision, China implemented regulations on Korean media content and applied stricter regulations towards Korean goods such as cosmetics. The limited exposure to the Chinese market plus the discouragement of tour operators to provide outbound travel packages to South Korea negatively affected Chinese visitor arrivals to South Korea.

As a result, in the period from March 2017 to December 2017, Chinese inbound tourists decreased from 8 million to 4.1 million and continue to limit the performance of the South Korean tourism market.

FIGURE 3: INBOUND 2016 VS 2017, JAPAN, CHINA AND OTHERS



Turn-around Opportunity: Olympics & High-speed rail

The Winter Olympics 2018 was held in Korea exactly 30 years after the initial Summer Olympics in 1988. Through the event, South Korea became the fifth country to host the big 4 international sports competitions events after France, Germany, Italy, and Japan. Namely; the FIFA World Cup, both Summer and Winter Olympics and the IAAF World Championships.

According to the Blue House (Cheongwadae), the PyeongChang Olympic Games impacted the Gross Domestic Product growth by 0.2 percentage for the first quarter of 2018 by increasing consumption expenditure by 1.4 trillion won. In addition, the Bank of Korea has forecasted the economic effect of the total investment (the production inducement amount) to be roughly 16.4 trillion won (USD 15.2 billion).

PYEONGCHANG WINTER OLYMPICS



The Gangwon province is divided horizontally by one of the biggest mountain ranges called “Taebaek”, which also facilitates pleasant weather conditions and harbours the beauties of nature. On the other hand, it also hinders the accessibility, as it horizontally penetrates Gangwon province separating the west and the eastern parts, making the east coast of the Gangwon less accessible to visit due to the long travel time and rugged road condition.

The Winter Olympics in 2018 was held in Gangwon province, Pyeongchang county, which lies approximately 200 km east from central of Seoul (CBD) or 3 hours and 30 minutes by vehicle. In the run-up to the Winter Olympics, the Korean government constructed the high-speed railway (KTX) to Gangneung city which has been operational since December 2017.

Thanks to the Winter Olympics, the **high-speed railway (KTX)** significantly reduced the travel times from Seoul to major districts in Gangwon province such as Hoengseong, Pyeongchang, and Gangneung by cutting the journey time from 3.5 hours to within 2 hours. Apart from the directly induced demand from the Winter Olympics, the high-speed rail opened more opportunities for Gangwon province as a tourist destination.

Focus: Gangneung city

EAST COAST OF GANGNEUNG CITY

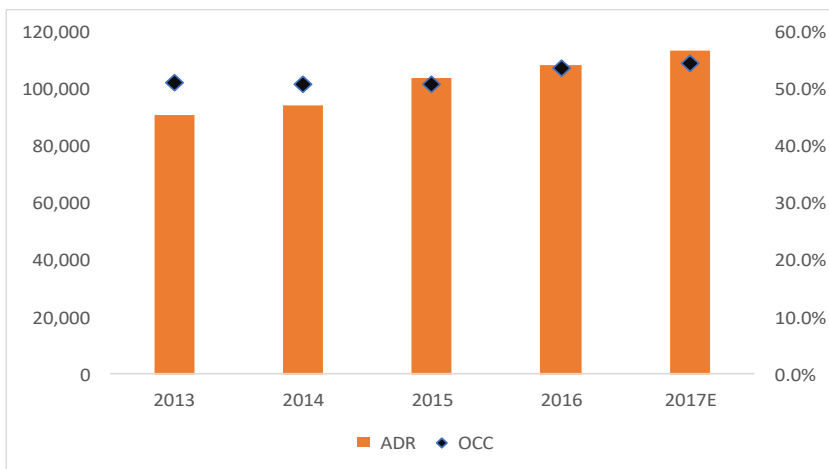


Gangneung City is the largest and the central city of Gangwong province which lies on the east coast of South Korea with 1,040 km² in size and a population of approximately 217,000. Although located at a similar latitude as Seoul, due to the Taebaek mountain range, the cold Northwest wind rises above the Taebaek mountain range causing a Föhn phenomenon, resulting in warmer weather in winter with a maritime climate aspect.

Due to the deep coastal area and the turbulent flow of water, Gangneung is gifted with abundant marine resources and a relatively stable temperature throughout the year. Gangneung is highly favored as a summer vacation spot providing access to famous destinations such as Gyeongpo, Jeongdongjin, and Sokcho. In total, there are over 40 beaches, averaging over 1 million visitors annually.

Hotel Performance in Gangneung City

FIGURE 4: OVERALL GANGNEUNG HOTEL PERFORMANCE 2013-2017E

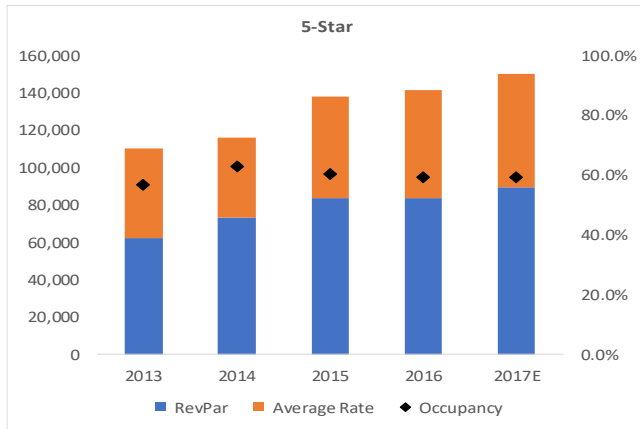


Throughout all the hotel ratings, Gangneung City showed a relatively stable hotel performance in both occupancy and average rates, as the city has earned its name domestically as a famous leisure destination for decades.

Source: KTO, HVS Research

Starting in 2017, due to the preparations for the Winter Olympics held in February 2018, Pyeongchang received Winter Olympics related induced demand. Such induced demand positively impacted the hotel market performance. However, due to the high-speed railway (KTX) access cutting traveling time to within two hours from Seoul, the option to visit Gangneung City as a day trip destination became more viable, which was one of the drawbacks for the lodging industry. This effect mostly impacted the lower categories of, mostly overpriced, hotels and motels, where value-oriented tourists would not stay overnight. On the other hand, the higher hotel categories registered positive momentum, mainly from the higher spending demand profiles.

FIGURE 5: 5 STAR HOTEL PERFORMANCE 2013-2017E



Comparing performances across the ratings, the 5 -Star category continuously increased average rate from KRW 110,000 to KRW 150,000 while increasing the occupancy from 56.8% to 59.5% from 2013 to 2017.

RevPar showed a steady growth from KRW 63,000 in 2013 to KRW 89,000 in 2017. This development was supported by the opening of new, high-end supply.

The 4 -Star category showed a similar pattern but with more stability in occupancy and average rates ranging from KRW 77,000 to KRW 87,000 and occupancy from 47.4%% in 2013 to 50.4% in 2017. RevPar is relatively stable for this segment, performance ranging from KRW 37,000 in 2013 to KRW 44,000 in 2017.

FIGURE 6: 4 STAR HOTEL PERFORMANCE 2013-2017E

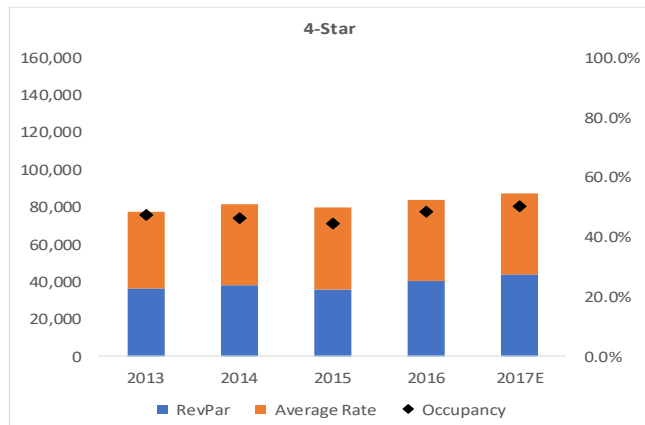
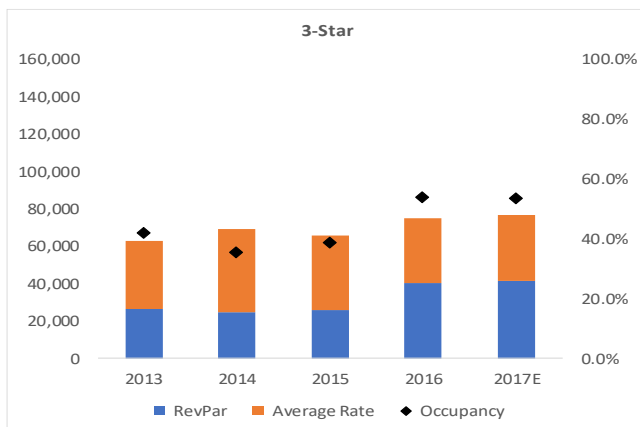


FIGURE 7: 3 STAR HOTEL PERFORMANCE 2013-2017E



The 3 Star hotel average rate ranged from KRW 63,000 in 2013 to KRW 77,000 in 2017 but with a high increase in occupancy from 42.2% to 53.7% respectively.

RevPar for 3 Star category increased slightly from KRW 27,000 in 2013 to KRW 41,000 in 2017.

Conclusion

South Korea remains a popular tourist destination for regional travelers in Asia, and Seoul firmly maintains its position as the pulse of the Korean tourism industry. However, due to the political instability from continuous threats from North Korea and diplomatic issues with China, South Korea is unable to push its tourism performance upwards.

However, by hosting the Winter Olympics in 2018, it gained an ease of political retention in North East Asia and the possibility of a North Korea nuclear freeze. Such events, in the long-run, are expected to influence the tourism industry positively, however, more detailed analysis for each market is required. In general, the diversification away from tour group demand to FIT travelers from other source markets is beneficial to the overall tourism industry in the medium-to-long term.



Gangneung City, which benefitted the most from the Winter Olympics, certainly received a high exposure in both the domestic and foreign tourism markets. Although, the city was already well-known domestically for its attractiveness as summer and winter holiday destinations, the support from the high-speed railway, and the additional exposure from the Winter Olympics further boosted the attractiveness of the city. Additional development here will help to diversify the Seoul experience with convenient beach access by train for those seeking contrasting experiences and feel like venturing out of the capital densely developed urban environment.



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HVS, the world's leading consulting and services organization focused on the hotel, mixed-use, shared ownership, gaming, and leisure industries, celebrates its 38th anniversary this year. Established in 1980, the company performs 4,500+ assignments each year for hotel and real estate owners, operators, and developers worldwide. HVS principals are regarded as the leading experts in their respective regions of the globe. Through a network of more than 35 offices and more than 500 professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. HVS.com

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Everywhere.**

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The Hong Kong team has worked on a broad array of projects that include economic studies, hotel valuations, operator search and management contract negotiation, development strategies for new brands, asset management, research reports and investment advisory for hotels, resorts, serviced residences and branded residential development projects.

About the Authors



A hospitality enthusiast, **Jaehyun, Yoo** is a Manager in HVS Hong Kong joined in 2015. Graduated with a Bachelor of Science degree from University of Nevada Las Vegas School of Hospitality

Administration, Jaehyun has experience over 10 countries in APAC work closely with investors, owners and developers. Strong understanding of the hospitality real estate sector, providing valuable advisory services.



Daniel J Voellm, MRICS, Managing Partner, HVS Asia-Pacific, is based in Hong Kong and has provided advice in all major markets across 20 countries in the region. Daniel works closely with key institutional

and private owners of hotel properties, financiers, developers and investors, and has gained a strong understanding of their investment requirements and approaches to assessing the market value of investment properties. Daniel further advises on property and concept development and strategy and expert testimony.