Branded hotels hold the key to the future

Melvin Gold,
independent hotel consultant

The hotel industry will grow but it will look very different in 2031 with more branded hotels, more budget properties and fewer independents, says hotel industry consultant, Melvin Gold.

The 1991 census suggested that there were some 525,589 hotel rooms in the UK. Twenty years later, according to a study that I undertook for Travelodge earlier this year (which is summarised in Table 35) there are now some 728,681 rooms.

For those with really long memories, or good history books, 20 years prior to that, in 1971, the government was actually offering grants of £1,000 per room (£1,250 in London) to hotel developers in order to stimulate hotel construction. This was a significant sum in those days. As a result over 50,000 new rooms appeared.

In his book *Profile of the Hotel and Catering Industry*, Professor Rik Medlik noted that, "….more hotels were built in Britain in a few years than in the whole period 1900-1970. Much obsolete stock was replaced and, in conjunction with the new bedroom capacity and separately, a significant hotel modernisation took place."

Such incentives are a distant dream for investors, developers and hoteliers today. But hotel development continues unabated.

In my report I estimated that from 1974, after the grant scheme ended, until the end of 2010, the UK hotel industry grew at a net compound annual growth rate of just over one per cent. Of course there were periods of economic slump when development slowed, and periods of boom, when supply levels grew far quicker than the long-term trend. Based on the current supply level, around 7,300 rooms per annum would need to open in the UK to maintain this level. As the figures in Table 40 show, this figure has easily been maintained in the last decade. Will they continue into the future?

The story is not quite that simple of course. A glance at the new hotel openings in Table 42 suggests that more openings have occurred in the larger cities than in smaller towns, rural and seaside areas; London has certainly seen 166 new hotels open in the last decade (74 in the budget category) not counting the huge refurbishment programmes undertaken by some of the capital's leading hotels, such as the Savoy and the Four Seasons (Table 41). London's performance remains resiliently high; proof, if it was required, of the economic truism of the inter-relationship between supply and demand. The capital has a global allure in all market segments and this underpins its performance and the inexorable increase in its hotel stock.

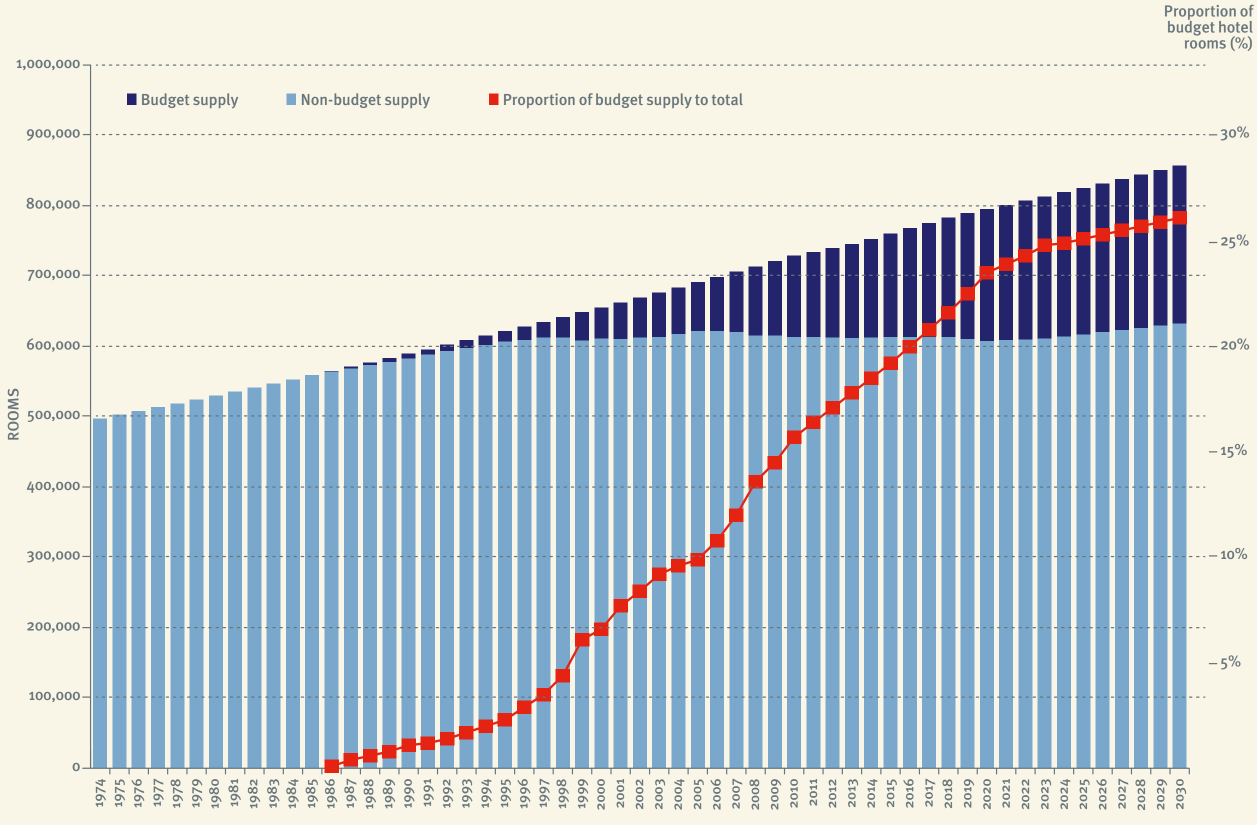
But beyond the importance of location, what lies behind the eye of this storm of construction is the critical importance of the branded budget hotel sector. It holds two keys – branded and budget.

The first branded budget hotel – a Travelodge near Burton-on-Trent – opened in 1985, just 26 years ago. At the end of 2010, the branded budget hotel sector was over 115,000 rooms in 1,440 hotels – a market which has more than doubled in the last decade. This year, the number of budget properties has swollen to 1,502 (120,555 rooms) – see Table 46. There are some differences in portfolios used in my report and in Table 46 but these are minor.

Travelodge's new property at Ramsgate – one more in the company's expansion in the budget sector.

Hotel growth to 2030

Figure 4: How the UK hotel market will grow



Source: Melvin Gold Consulting

Looking ahead, in my report to Travelodge, I used a compound growth rate of 0.75 per cent per annum from 2011 to 2013, then a return towards the one per cent rate for five years from 2014 to 2018 before returning to a rate of some 0.75 per cent on a compound basis from 2019 to 2030. This is well below the long-term trend identified earlier and some may view it as conservative.

However, these assumptions would see the addition of around 128,100 rooms in the 20-year period to 2030 – compared with the 95,000 rooms that have opened between 2002-2010 – which would bring the total quantum of supply to around 856,750 rooms. This implies an average annual net increase of 6,405 in the next two decades. In fact, the number of new rooms will probably be higher than that because some existing supply will leave the market for alternative uses or redevelopment.

Of this number, the branded budget hotel supply will grow to 224,266 rooms in 2030, some 109,070 rooms above today's level of sector supply. This implies that there will be only be a net growth of 19,030 rooms in other segments of the market which is likely as a number of existing hotels will be converted or redeveloped to budget brands.

Under this scenario the proportion of budget supply will grow from 15.8 per cent in 2010 to 26.2 per cent in 2030 – a figure which seems achievable given that budget supply in France is currently around 24 per cent and in the USA it is at 32.8 per cent.

The net result is that it is inevitable that the industry will become far more branded than at present. At the end of 2010 around 39.7 per cent of the total supply was corporate branded and a further 6.6 per cent was branded through consortia membership. This implies that branded supply would be at least 66 per cent (including consortia) by 2030.

In fact, because nearly all new supply will be branded in some way, and because there will be a net loss of rooms in the independent sector, an even higher percentage of the UK's hotels will be branded, which will bring the UK to nearer the current proportion in the USA which is around 68.5 per cent.

This is a significant new market sector that has emerged in the last decade – there were only 50,000 budget hotel rooms in 2001. Some of the early properties were conversions or developments adjacent to pubs and restaurants at the roadside or in motorway service areas, but those most recently opened are newly built and are now generally in the big cities (a more recent trend), smaller towns, seaside resorts and attractive rural areas.

Furthermore (and somewhat unusually) demand, which is not always obvious prior to development, has been proven to be led by supply. Operators claim that many of their clients have rarely or never used UK hotels previously – a relief, perhaps, to the many private sofas, floors and spare rooms that had run at high occupancy around the country. No surprise then that the two largest hotel brands (Premier Inn and Travelodge) in the UK are in this segment, or that there are two others in the top seven UK hotel brands (Holiday Inn Express and ibis).

If these have been the winners then it has to be recognised that there have been losers, too. The industry has seen many hotel closures although not as many as most observers, including myself, would like to see.

The days of the independent hotel or bed and breakfast establishment cannot yet claim to be over but there must be a question mark over the future of the least efficient and the least attractive. Boutique hotels, designer hotels and similar properties (for example, Hotel du Vin, Malmaison and others) have been as much a part of the hotel development trend in recent years as the budget sector. As a result, the entrepreneurial spirit of their pioneers has led the industry in another new direction.

Equally there are many independent hoteliers who have invested in their product and their people to ensure that their customers get value for money and remain loyal. They will survive. Regrettably there are also a significant number of properties that cannot make such a claim. At best they survive through unsuspecting first-time visitors who never return; at worst, they give the industry a bad name.

On-line review sites now provide a platform for these properties to be easily identified prior to a visit, and with plenty of new supply in many locations, hoteliers must remember that it is now all-too-easy for savvy customers to exercise an informed choice. As a result, under-invested independent hotels, and even some under-invested mid-market branded properties, will find tough times ahead unless they can satisfy the requirements of the increasingly well-informed and demanding 21st century hotel guest. Constant refurbishment is essential but, unfortunately, banks and other funding institutions are now reluctant to lend into the sector, and particularly to SMEs, even when there is a good business plan.

Little surprise, therefore, that some hotels are closing their doors for ever. Comparing the 2007 and 2010 databases of Hotel Data Ltd. in order to identify hotel closures in the period, it's clear that there has already been some attrition.

Looking at independent hotels with over 30 rooms, 161 hotels with more than 7,000 rooms in total closed within the period. The numbers were boosted by some branded properties that had closed, although they were surprisingly few (Regent Palace Hotel and the Kensington Palace Hotel in London, are notable examples). An investigation of hotels with over 10 rooms would have revealed a far higher number but it's likely that 10,000 rooms have closed during the 2007 to 2010 period, which suggests that the supply growth and changes in market circumstances are having an impact on independent hotel operations.

This fallout from the independent and mid-market sector can only be expected to continue in the face of the introduction of yet more hotels as well as the trend towards branding, not only in the budget sector. Even before the recent banking and economic crises, the financial sector was showing great reluctance to fund the new development of unbranded properties and currently it is almost impossible to obtain funding for an unbranded hotel development in the UK. This will not change soon.

Ownership structures may vary – there are already examples of wholly owned and operated, fixed leases, variable leases, management agreements and franchises in this sector of the market. The common thread is the support of a brand in the operation and funding of the hotel.

Franchising may well become more common in the future as international companies such as InterContinental Hotels Group, Accor and Hilton favour this method in their current expansion plans. This is especially true at the budget end of the market. Indeed Accor's All-Seasons brand, Hampton by Hilton and easyhotel, among others, look set to be almost exclusively developed through franchise agreements.

The future of the sector will thus be more branded, and certainly more branded budget. Only the best of the independent sector will thrive. But having said that, the UK hotel sector looks set to have a vibrant future. It has survived the present recession with some significant but not extensive casualties. Few hotels have actually closed because of insolvency. New hotels are still being planned (see Tables 43-45).

When consumer confidence picks up and the economic situation eases, travel will pick up, too. It's likely that world travel arrivals will breach the one billion mark (Table 13) within the next few years. Of course there are imponderables but, with all the usual provisos, UK hotel industry growth is achievable and, indeed, likely.

Melvin Gold is an independent hotel consultant and operates Melvin Gold Consulting Ltd (www.melvingoldconsulting.com). The report prepared for Travelodge and entitled "Quantification of serviced accommodation supply in the United Kingdom and consideration of related issues" is available free of charge via the company's website.