UK Hotels Forecast 2021 – 2022

An emerging recovery

pwc

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Encouraging signs for hoteliers

After the most volatile trading period since benchmarking began, the PwC Hotels Forecast 2021-2022 reveals the green shoots of recovery as demand returns. Though performance is not expected to return to pre-pandemic levels by Q4 2022, there are finally encouraging signs for hoteliers.

By the end of 2022, the forecast is that revenue per available room (RevPAR) in London will return to between 43% and 86% of pre-pandemic levels. In the regions, this figure is higher with the forecast between 64% and 100% of pre-pandemic levels.

The speed of recovery will be the major issue for the sector in 2022. Driven by factors outside of the sector's control, the pace and size of the return of tourism, international and domestic business and events will determine the speed and extent of the recovery. There are, however, encouraging signs for the return of tourism. When surveyed by PwC Research, 63% of people said they plan to take either more or the same number of holidays in 2022.

This year has seen above average new supply with cities such as Bristol, Manchester, London and Glasgow all seeing significant new openings. This new supply coupled with dampened demand is taken into account in our forecast. With many businesses now operating a hybrid working model for employees, this is likely to subdue demand across both London and regions for domestic business stays.

Common across all areas of our forecast is a difficult Q1 2022. With revenues at a reduced level, the majority of government financial support withdrawn and rent and tax bills due, managing cash flow and operations will be critical to ensure success for hotels across the UK.

In our previous forecast, we predicted a dramatic fall in virtually every part of the sector. Regrettably, the reality was even harder for hotels as new lockdowns caused trading to cease for almost five months at the start of 2021.

This year, to help account for the unpredictable path of the pandemic, we have modelled three scenarios: slow, moderate and strong rebounds. Our assumptions behind each can be found on page 10.

Source: Econometric forecasts: PwC September 2021, Benchmarking data: STR

"I'm pleased to be able to bring a much more positive forecast to the sector this year. That is not to say recovery will be easy or straightforward, but I believe with the right planning and strategy, hotels across the UK can look forward to significantly better trading over the next 12 months.

Sam Ward, UK Hotels Leader

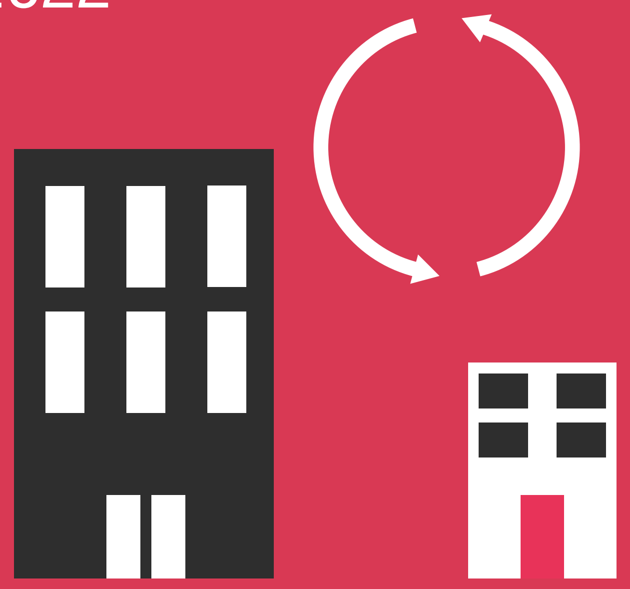
Hotels Forecast in numbers 2022 – Moderate rebound scenario

Occupancy
2022

London
56%
(+63.7% vs 2021)

Regions
63%
(+25.4% vs 2021)

ADR – Average daily rate
2022



London
£112.30
(+32.9% vs 2021)

Regions
£67.00
(+8.9% vs 2021)

RevPAR – Revenue per available room
2022

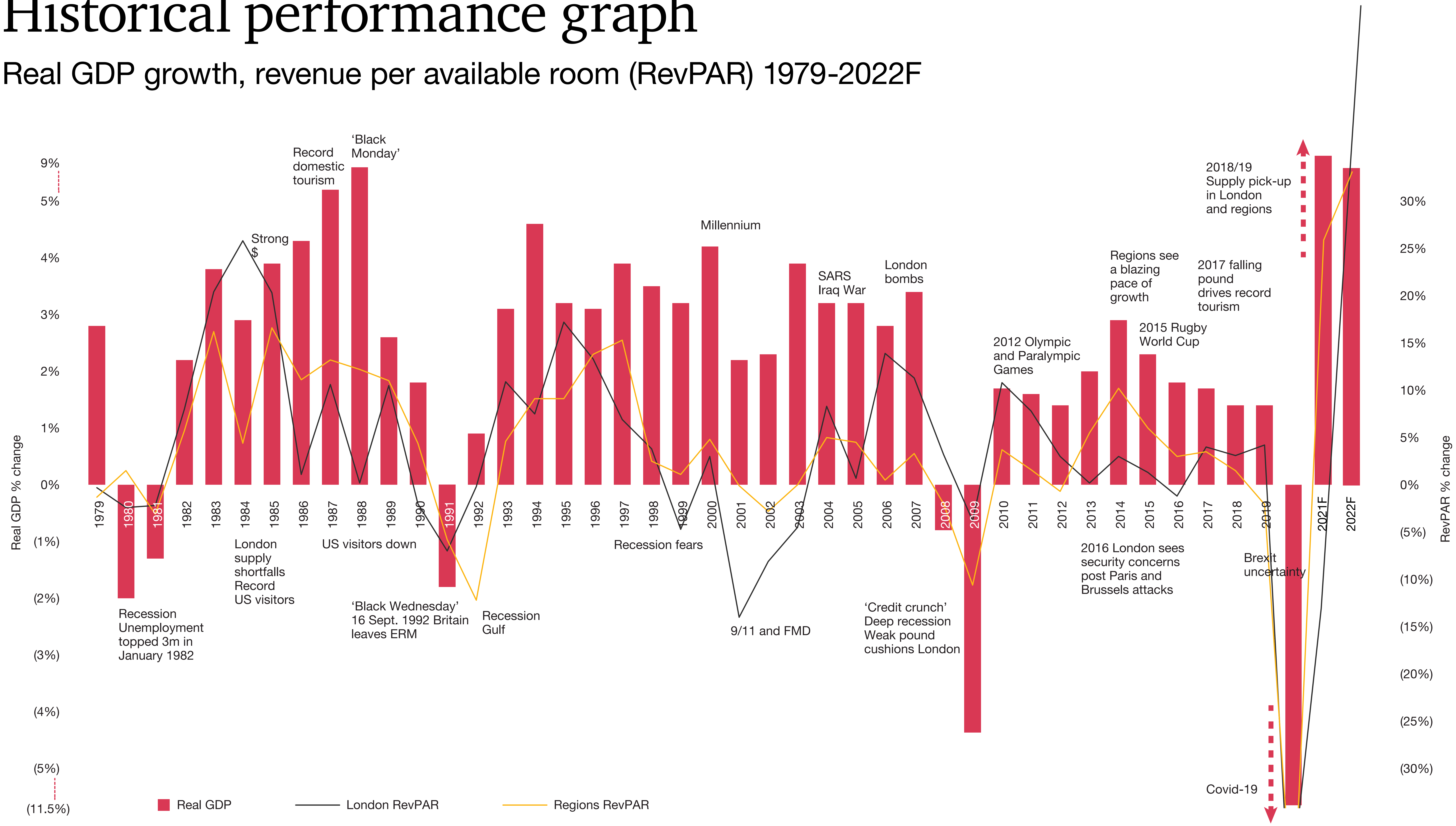
London
£63.70
(+110.5% vs 2021)

Regions
£42.00
(+32.5% vs 2021)

Source: Econometric forecasts: PwC September 2021, Benchmarking data: STR.

Historical performance graph

Real GDP growth, revenue per available room (RevPAR) 1979-2022F



Source: Econometric forecasts: PwC September 2021

NB: Dual axis GDP on left and RevPAR on right

Macroeconomic data: National Statistics

Benchmarking data: STR July 2021

S1: Moderate Rebound
RevPAR % change

2021	
London	-13.3%
Regions	25.6%
2022	
London	110.5%
Regions	32.5%

A two-speed race: London and the Regions

London: In need of a sizeable recovery

The London hotel sector is simultaneously dealing with a lack of both international tourism and domestic business travel. These have combined to make for an exceedingly difficult trading period.

The luxury hotel market in London has seen occupancy as low as 18% which is in part down to the absence of high-spend tourists from the USA and the Middle East. It has been the mid and budget range of hotels that have fared best from domestic tourism demand.

In all three scenarios for London, the forecast is for improvement across average daily rate (ADR), revenue per available room (RevPAR) and occupancy. Indeed, in the most optimistic of our three scenarios, occupancy could reach 86% of 2019 levels in 2022.

Hotels must continue to innovate and adapt to the markets available to them. Many businesses have publicly stated their ambitions to cut business travel even as restrictions are lifted. Hotels that previously focussed on the business market should think about how to capture a stronger domestic tourism market, looking at this as a real opportunity and, as it returns, the international tourism market.

Regions: An uneven recovery

The UK regions have seen mixed fortunes during the pandemic. Staycations have provided a significant boost for coastal and leisure destinations. In fact, occupancy and ADR in August 2021 significantly outperformed August 2019. However, some cities and non-tourist destinations are still experiencing dampened demand.

In regional cities such as Bristol, Birmingham and Edinburgh, a combination of both decreased demand and increased supply have suppressed occupancy. The potential return of large scale events, conferences and meetings will have a direct impact on regional cities and their recovery. With some large events having long planning cycles, the events market may take further time to recover, especially if uncertainty persists around potential restrictions.

For those areas boosted by staycation demand, summer 2022 may again see more subdued trading conditions if international travel is back on the agenda for the domestic market, and pent up demand for guaranteed sun is released. The latest PwC Research shows that 37% of people still plan to holiday within the UK in 2022. On balance, we expect staycation demand to be similar to summer 2021.

"In a complete reversal of fortunes, RevPAR in many regional leisure destinations is double that of London. Despite the lifting of restrictions and the first signs of a recovery in international tourism, there is still a long way to go.

Stephen Broome,
PwC UK Lead Hotel Consultant

“The first quarter of any year is difficult for hoteliers but planning and communication with stakeholders is critical to get through this period. Some businesses may need help in Q1 and it’s important to communicate this upfront.

Mark Addley, PwC UK Real Assets Business Recovery Services Leader

Actions for hoteliers

Plan your finances for Q1 2022

The first quarter of the year has always been difficult for hotels without any major holidays to drive demand and with tax bills due at the end of March. Normally, hotels rely on strong results from December to see them through. However, that trading period is unlikely to recover to pre-pandemic levels for 2021. The sector must plan accordingly, manage cash flow and put in place the right strategies to ride out this tricky quarter.

Plan how to recoup labour and energy cost increases

Labour shortages in hotels in certain key positions are at a critical level.

This has led to an above inflation increase in wage rates as hoteliers struggle to retain and attract staff. In addition, there are reports of hoteliers needing to restrict availability due to an inability to service the volume of business. This rising payroll cost pressure appears likely to continue into 2022 and beyond.

At the same time, other operating costs are also increasing at a rate well above inflation. In particular, energy costs driven by seven-year highs in global oil and gas prices, that will have a knock-on effect on other operating costs such as laundry.

In what could be described as a perfect storm, this raft of cost increases coincides with the phased changes in the rate of VAT, from the reduced rate of 5%, to 12.5% on 1st October 2021 and to the standard rate of 20% from 1st April 2022.

The ability for hoteliers to pass on the full impact of these increases in taxation and operating costs, to preserve profitability, will probably present a challenge in markets where demand is weaker and room availability plentiful.

Invest at the right time in technology

Technology has the power to transform both front and back of house operations. In reference to the pandemic, tactical investment to provide a contactless experience for guests can work for both reassuring guests and also managing staffing levels and costs.

Back of house, with the need to manage demand and operation costs carefully, technology can enable businesses to engage in the longer-term planning needed to see themselves through leaner periods.

Know your traveller profile

Hotels should consider their current traveller profile, ensuring they have CRM technology through multiple channels to capture this and make sure the right facilities are open for that traveller. Similarly, hotels should think about what facilities could be added or changed to suit the needs of the domestic traveller if international business does not resume at the pace expected, so investment in infrastructure should be a key consideration.

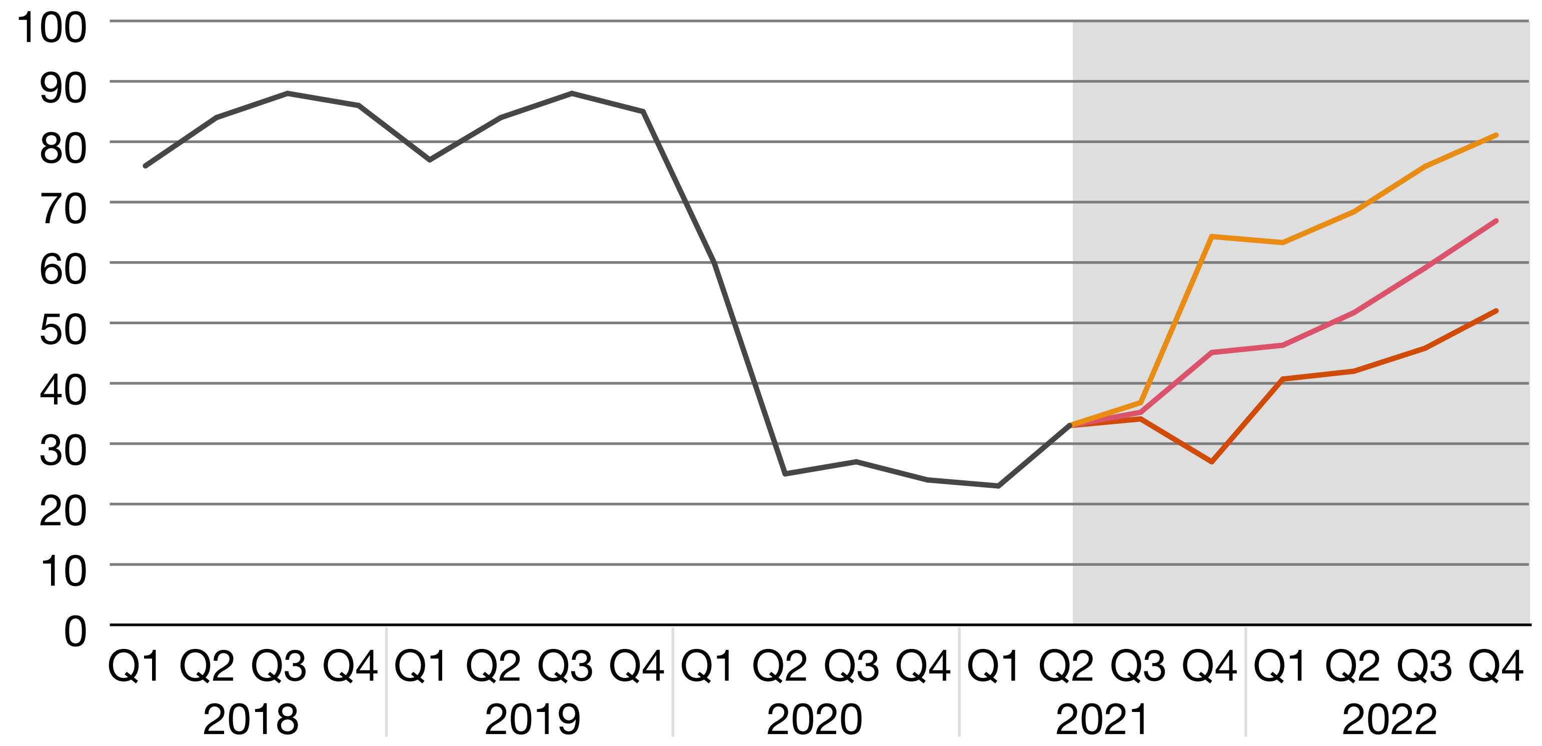
Reduced operating hours and closure of some facilities have become a part of pandemic life, not just in hotels. However, travellers remain discerning and expect to be communicated with clearly about what to expect from their stay with the right to cancel planned trips within a respectable time frame with no financial penalties.

Forecast in figures – London

Slow rebound | Moderate rebound | Strong rebound | Historical

London: Occupancy (%)

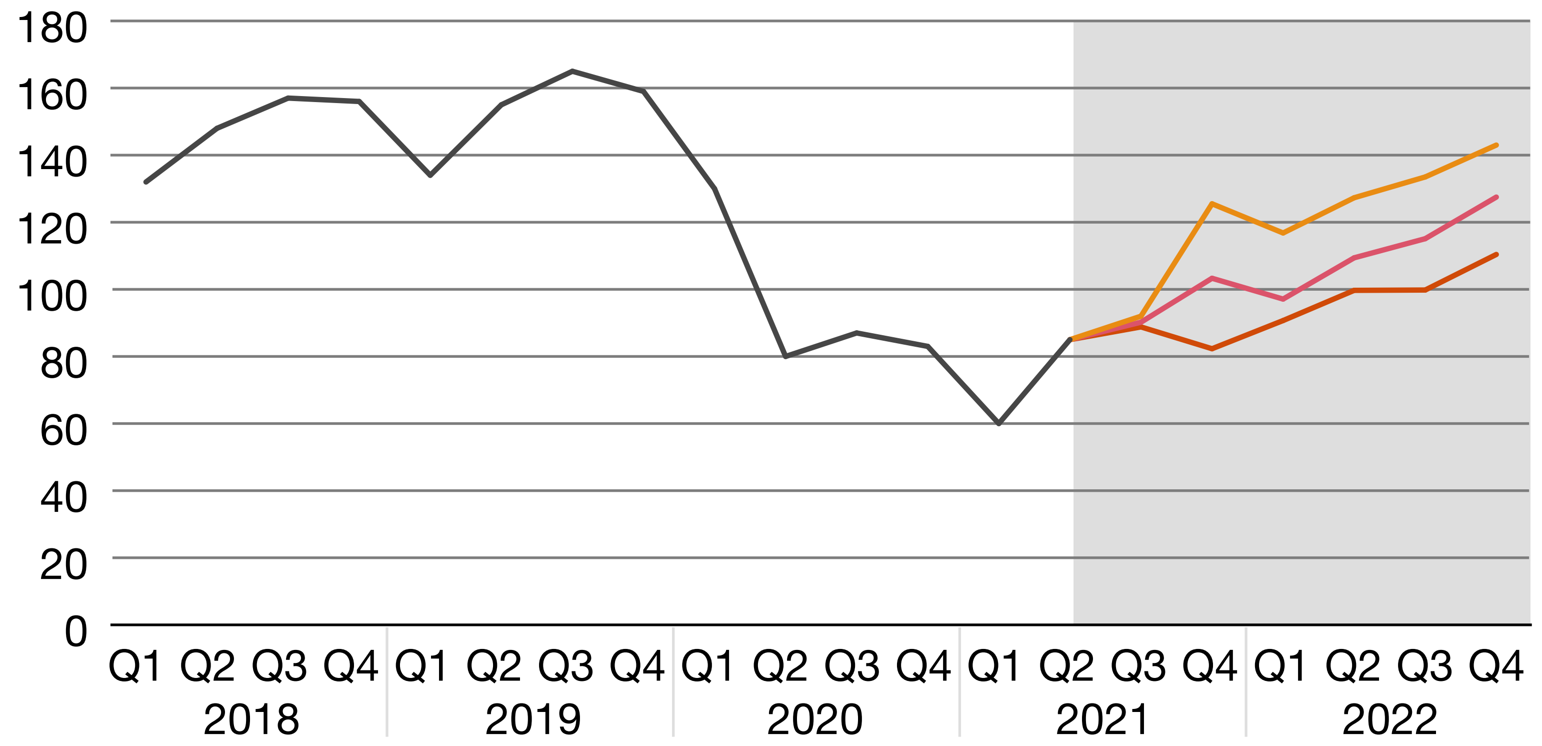
For our occupancy forecast we expect levels to reach between 62% and 96% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	34	35	37
Q4 2021	27	45	64
Q1 2022	40	46	63
Q2 2022	42	52	68
Q3 2022	46	59	76
Q4 2022	52	67	81
2019		83	
2020		37	
2021	29	34	39
2022	45	56	72

London: Average Daily Rate (ADR)(£)

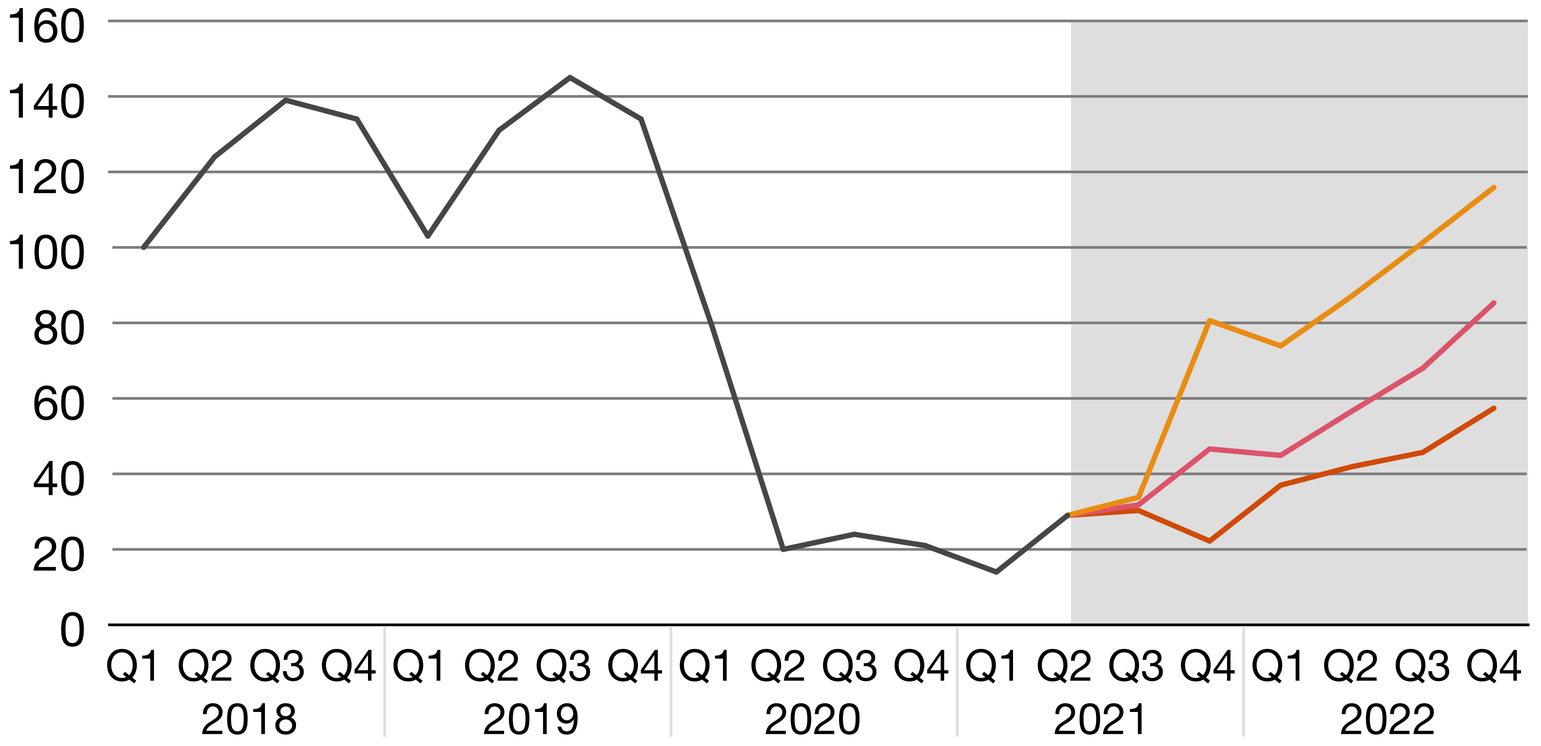
We expect ADR in London Hotels to reach between 70% and 90% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	89	90	92
Q4 2021	82	103	126
Q1 2022	91	97	117
Q2 2022	100	109	127
Q3 2022	100	115	134
Q4 2022	110	128	143
2019		153	
2020		95	
2021	79	85	91
2022	100	112	130

London: Revenue per available room (RevPAR)(£)

Our RevPAR outlook is lower and more uncertain: we expect it to reach between 43% and 86% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	30	32	34
Q4 2021	22	47	81
Q1 2022	37	45	74
Q2 2022	42	57	87
Q3 2022	46	68	101
Q4 2022	57	85	116
2019		128	
2020		35	
2021	24	30	39
2022	46	64	95

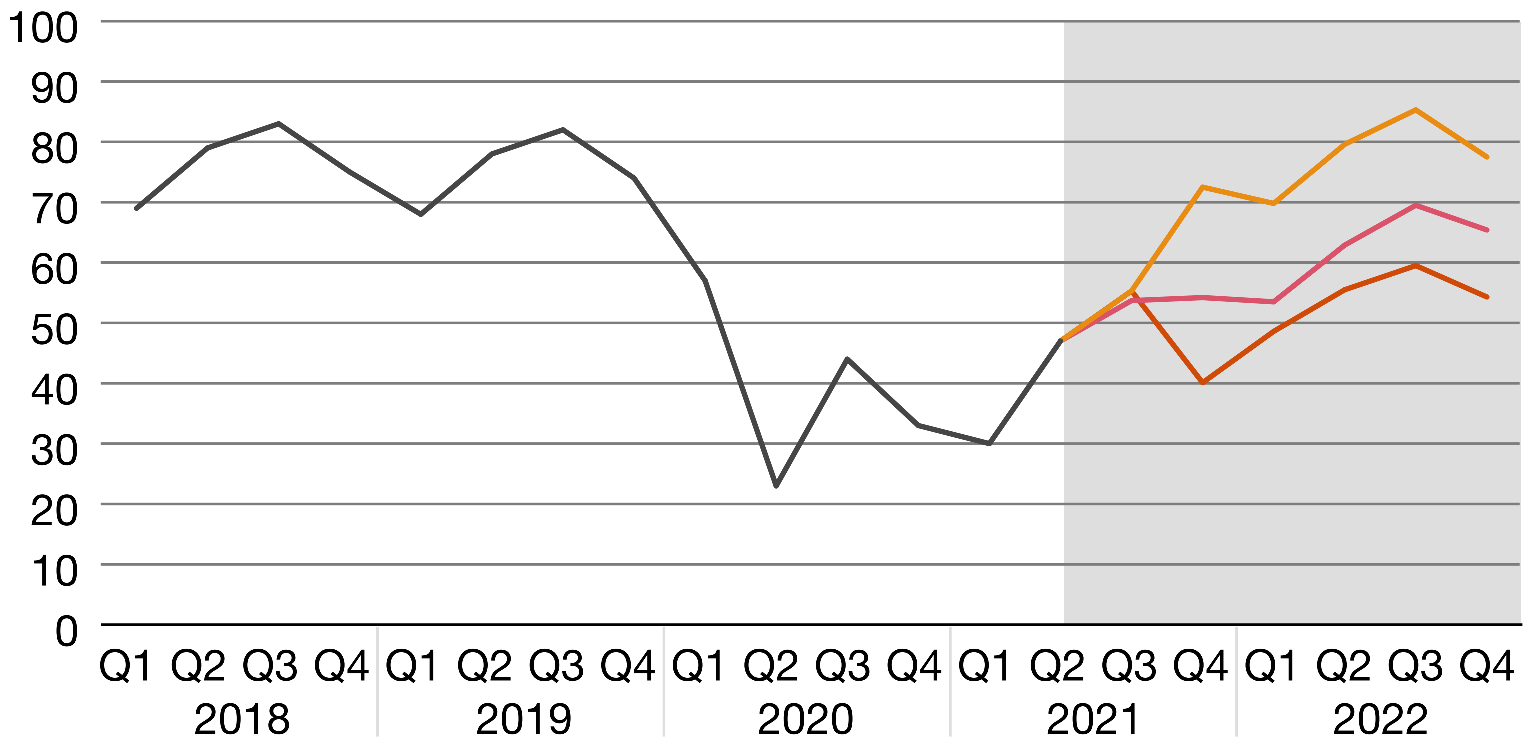
Source: Econometric forecasts: PwC September 2021, Benchmarking data: STR

Forecast in figures – Regions

Slow rebound Moderate rebound Strong rebound Historical

Regions: Occupancy (%)

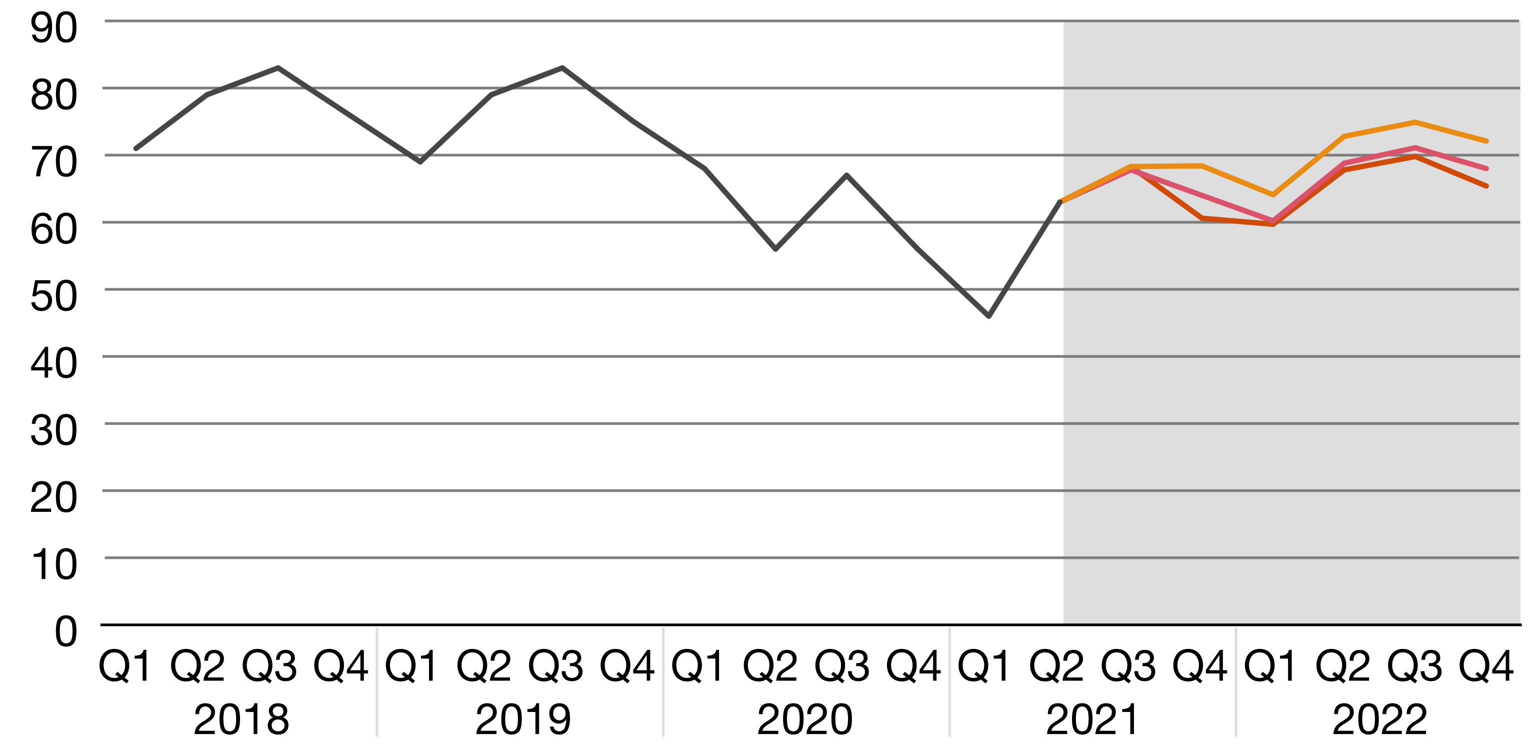
Occupancy in the regions is also heavily reflective of scenario, reaching between 73% and 105% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	55	54	55
Q4 2021	40	54	72
Q1 2022	49	53	70
Q2 2022	55	63	80
Q3 2022	59	70	85
Q4 2022	54	65	78
2019		76	
2020		41	
2021	45	50	59
2022	54	63	78

Regions: Average Daily Rate (ADR)(£)

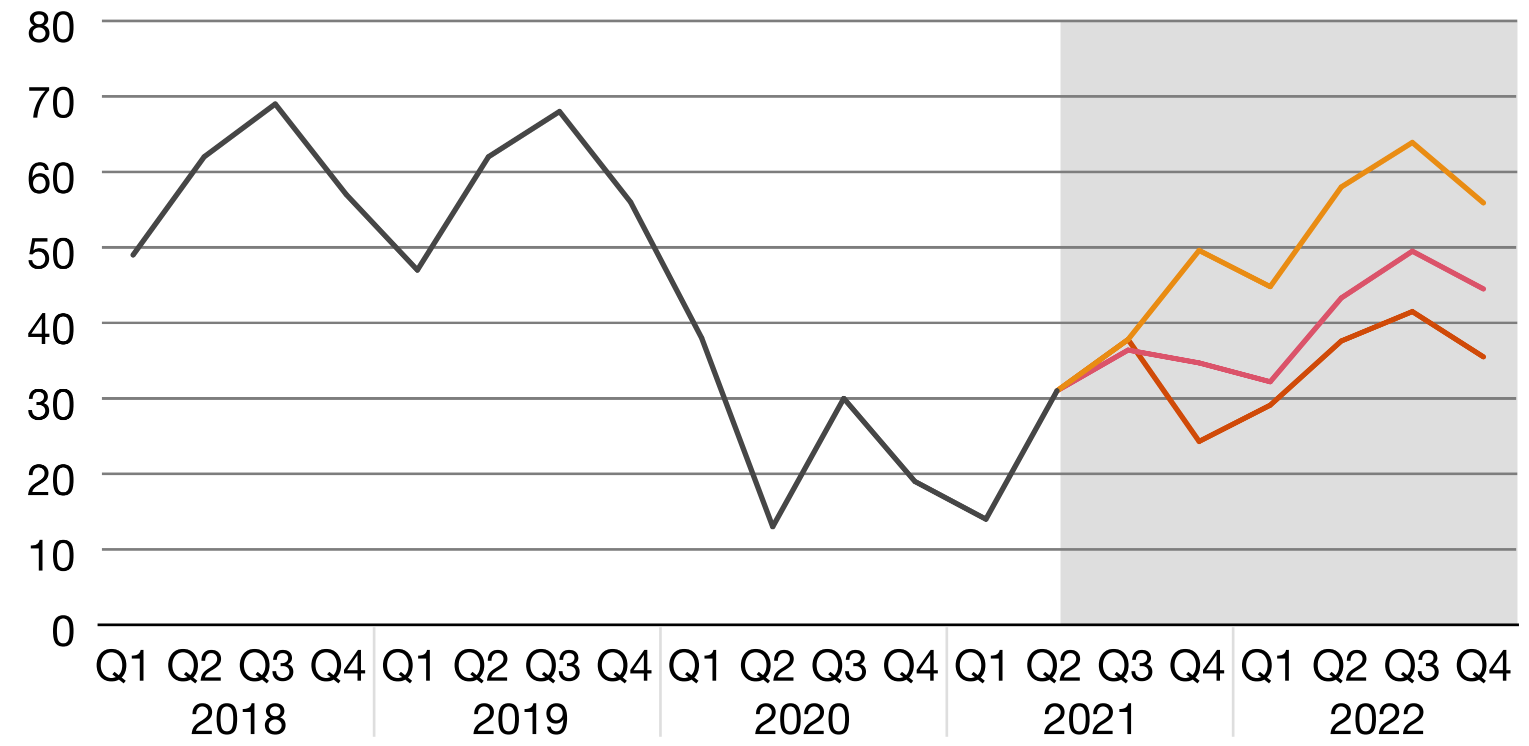
We expect ADR in the regions to reach between 87% and 96% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	68	68	68
Q4 2021	61	64	68
Q1 2022	60	60	64
Q2 2022	68	69	73
Q3 2022	70	71	75
Q4 2022	65	68	72
2019		77	
2020		62	
2021	61	62	64
2022	66	67	71

Regions: Revenue per available room (RevPAR)(£)

Similar to London, the regions RevPAR outlook is lower and more uncertain, reaching between 64% and 100% of pre-pandemic levels by Q4 2022.



	Slow rebound	Moderate rebound	Strong rebound
Q3 2021	38	36	38
Q4 2021	24	35	50
Q1 2022	29	32	45
Q2 2022	38	43	58
Q3 2022	41	49	64
Q4 2022	36	45	56
2019		58	
2020		25	
2021	28	32	40
2022	36	42	56

Source: Econometric forecasts: PwC September 2021, Benchmarking data: STR

Deals and restructuring: A surge is forecast from March 2022

Despite the greatest downturn across the sector since benchmarking began, with government support and greater leniency from lenders, the sector has largely been able to weather the storm.

Some regional areas especially have benefitted from an unusually high staycation demand, with both occupancy and average daily rates actually surpassing their pre-COVID-19 highs.

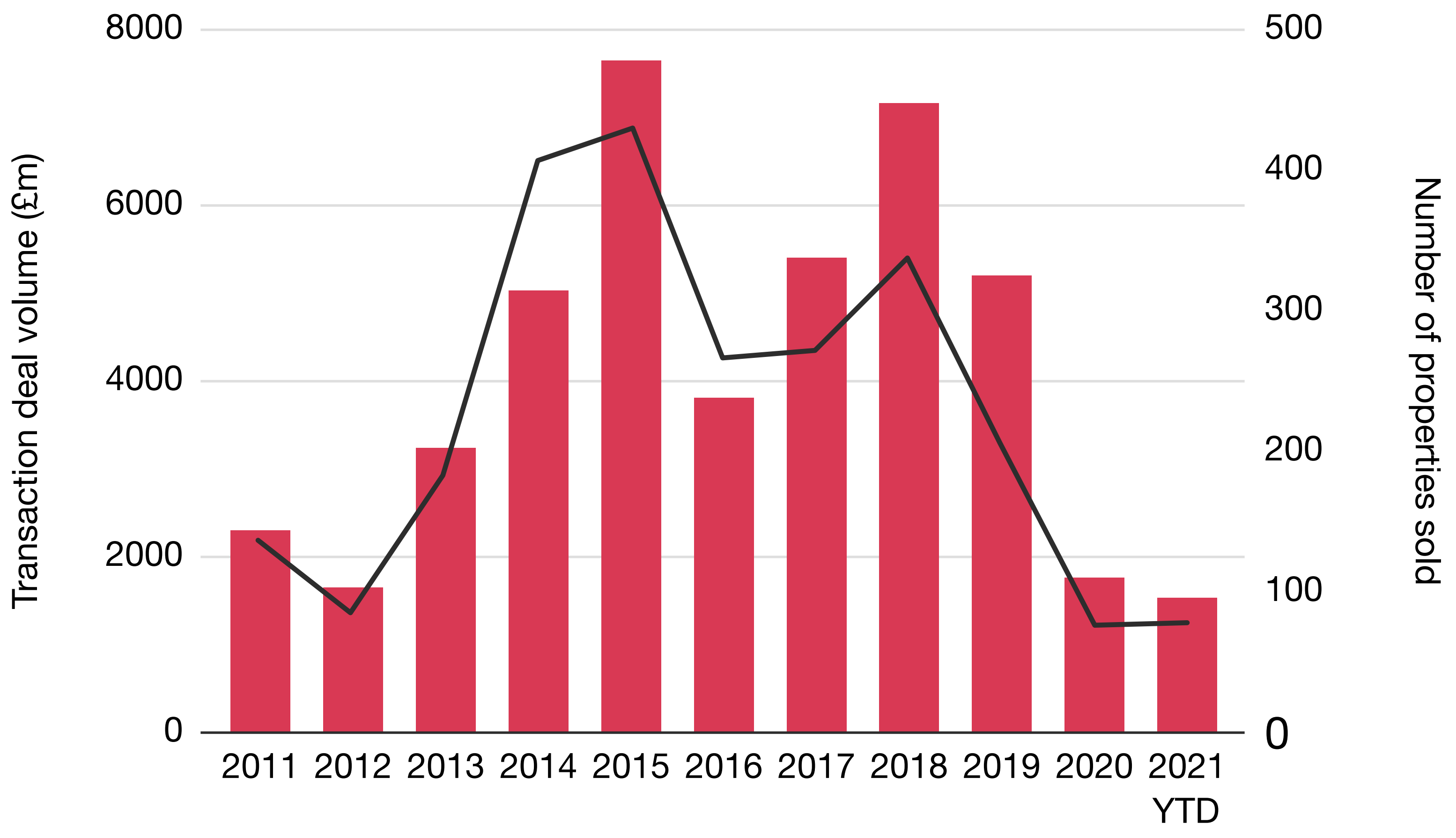
Since the pandemic started, we have seen access across the sector to additional financing through the Coronavirus Business Interruption Loan Scheme (CBILS) as well as supplemental financing from alternative lenders. In some cases, shareholders have also been under pressure to input more equity into their businesses despite the ongoing support from incumbent stakeholders as well as the government.

Although there have only been a small number of insolvencies in the hotel sector since the pandemic began, by March 2022 the picture could be very different, as hoteliers may find themselves battling lower levels of occupancy without the help of the VAT rate cut, furlough schemes and business rates relief. This may be particularly acute in London, where our slow scenario forecasts just 40% occupancy in Q1 2022.

An increase in deals activity

This year we have seen an uptick in transaction volume compared with 2020, such as Warner Leisure Hotels as a part of the Bourne Leisure Group majority sale to Blackstone. We also anticipate some large transactions to conclude in Q4 of 2021. Pricing has remained buoyant during this time due to a large amount of capital looking to invest in the sector but with only limited assets coming to market.

Transaction deal volume (£m) in UK from 2011 – 2021 and number of properties sold



Going into 2022 we expect an increase in transactions but do not see it recovering to the levels of 2019. We anticipate that 2022 will be a period where businesses will look to stablise their income and cash flow levels before they consider selling to ensure they maximise value. Businesses that consider selling during 2022 will likely be as a result of cash flow pressures and operational difficulties.

Source: Real Capital Analytics and PwC analysis

Active restructuring will increase from Q1 2022

Clearing banks have continued to be supportive of their hotel sponsors since the pandemic started, with few enforcements having been reported. However, most new financings into the sector appear to have been provided by alternative debt funds. Recent transactions include the refinancing of the Ability Group by Lone Star and a London Hyatt hotel by KSL.

It is likely that clearing banks will look at some loan sales as an option, as they are now thinking about ways to reduce their exposure to the sector. It is key that any buyer must be a reputable lender with sector experience. Loan sales have been successful in other Real Asset sectors, such as the recent sale of the Mercatus shopping centre loan portfolio by NatWest. This is likely to trigger more banks to do the same in the hospitality space.

What do hoteliers and lenders need to consider?

Going into 2022, if occupancy levels continue to be low, restructuring may be the right option for some businesses.

1. Liquidity pressures remain and there will be a need for more sustainable hybrid lease structures, sharing both risk and reward between tenant and landlord.
2. Catch up CapEx is a key focus, as many hotels have deferred all but necessary expenditure over the last twelve months.
3. We anticipate continued requests of lenders to waive covenants, or provide additional liquidity support. Extension of facilities will also be a core focus over the next twelve months.
4. There is the possibility that even well capitalised hotel owners could struggle with ongoing future cash flow shortfalls, especially where development is required. This will present more opportunities for the alternative lender universe.

Methodology

For both London and the regions, we have created three separate forecasting models taking into account the unpredictable nature of the pandemic and the effect this has on demand. The three scenarios are: slow, moderate and strong rebounds.

The pandemic is expected to create different recovery profiles for both London and the Regions. For example, while the return of international travel will be a key determinant of demand and prices in London, the state of the UK economy – measured by UK GDP – is expected to be a much more significant driver in the Regions. As a result, we have developed two sets of scenarios for both London and the Regions. These are summarised in the table below.

Source: Econometric forecasts: PwC September 2021, Benchmarking data: STR

	S0: Slow Rebound	S1: Moderate Rebound	S2: Strong Rebound
London	In this scenario, we assume that global tourism and **air passenger travel numbers return to 50% of pre-pandemic levels by Q4 2022.** We assume that virus variants and an increase in hospitalisations among unvaccinated people lead to **tightening restrictions after the summer** and through to the winter (Q4 2021).	In this scenario, we assume that global tourism and air travel passenger numbers return to **65% of pre-pandemic levels by Q4 2022**. We assume that the successful vaccine rollout prevents hospitalisations and leads to **a gradual reduction in all restrictions**, without further lockdowns.	In this scenario, we assume that global tourism and air **travel passenger numbers return to 85% of pre-pandemic levels by Q4 2022**. We assume that the successful vaccine rollout prevents hospitalisations and further outbreaks, leading to a **faster reduction in restrictions**, compared to the moderate scenario. We assume all restrictions are removed by Q4 2021 (inc. public awareness campaigns).
Regions	In this scenario, we assume a slow recovery in UK GDP, which reaches pre-pandemic levels **by the end of Q4 2022** (GDP growth of 6.5% this year and 4.1% in 2022). This, combined with the end of the furlough scheme, results in lower consumer confidence and spending. We assume that virus variants and an increase in hospitalisations among unvaccinated people lead to **tightening restrictions after the summer** and through to the winter (Q4 2021). **Staycations continue to support regional demand in summer 2021** – at similar rates to 2020. However, weak GDP growth and **consumer confidence weigh on the sustained recovery of domestic tourism**.	In this scenario, we assume a moderate recovery in UK GDP, which reaches pre-pandemic levels **at the start of Q3 2022** (GDP growth of 6.8% this year and 5.3% in 2022). The end of the furlough scheme does not lead to rising unemployment, as a recovering economy increases the demand for jobs. We assume that the successful vaccine rollout prevents hospitalisations and leads to **a gradual reduction in all restrictions**, without further lockdowns put in place. **Staycations continue to support regional demand in summer 2021** – at similar rates to 2020. However, as the economy recovers and international travel returns, **regional demand beyond 2021 is driven mostly by favourable economic conditions**, rather than staycations.	In this scenario, we assume a strong recovery in UK GDP, which reaches pre-pandemic levels **by the end of Q1 2022** (GDP growth of 7.2% this year and 5.5% in 2022). The end of the furlough scheme does not lead to rising unemployment, as a rapidly growing economy leads to a buoyant labour market. We assume that the successful vaccine rollout prevents hospitalisations and further outbreaks, leading to a **faster reduction in restrictions** compared to the moderate scenario. All restrictions removed by Q4 2021 (inc. no public awareness campaigns) **Staycations continue to support regional demand in summer 2021** – at similar rates to 2020 However, as the steep recovery in the economy and international travel takes place, **regional demand beyond 2021 is driven by favourable economic conditions, rather than staycations**.

Our econometric modelling approach: 2021 and 2022 forecasts

We conducted a literature review of academic research and tested several model specifications as part of an ongoing process to improve model performance. Based on our findings, we used the two-stage least squares (2SLS) instrumental variables approach. The 2SLS approach has several advantages, namely, it does not require any distributional assumptions for explanatory variables, e.g., variables may take a binary or non-normal form. It is also computationally simple and allows the use of diagnostic testing procedures for problems such as heteroscedasticity, unit roots and specification error. In addition, the two-stage approach allows us to estimate demand and price separately rather than projecting occupancy rates directly, recognising that these are driven by different factors. However, the challenge of producing robust estimates using the 2SLS approach is the selection of ‘instruments’ or variables that have an effect on price, but only through their influence on hotel demand.

Our model specifications differ for London and the Regions, particularly in the first stage regression where we estimate demand. We include quarterly dummies and the UK stringency index, which is used to measure lockdown severity. Notably, for London we include the lagged demand, lagged exchange rates, and changes in international passenger numbers, while for the Regions we only include UK GDP.

Results from the Hansen J statistic suggest that the instruments are exogenous, and the model is valid at the 5% level. Equally, the t-tests in the first regression suggest that the variables are significant at the 5% level. This suggests that the instruments are both relevant and independent of the dependent variable.

The econometric model was used to generate forecasts for Q3 2021 up until Q4 2022, and these were generated separately for London and the regions. Forecasts for ADR growth and hotel demand were generated using PwC forecasts of macroeconomic variables, IATA international passenger forecasts, and assumptions on the trajectory of COVID-19 restrictions. We supplemented this with additional forecast data for hotel supply for London and the regions provided by AM:PM to produce forecasts for occupancy rates. Adjustments were made to ensure the comparability of STR and AM:PM data and an attrition factor was applied to simulate periodic drop-offs in rooms supply. RevPAR forecasts were constructed using ADR, demand, and supply forecasts.

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