

Research Articles

## THE LATIN AMERICAN HOTEL SECTOR

### A DORMANT GIANT

Latin America's tourism and hospitality sector is receiving a lot of attention these days, both from visitors and investors. Over the last few years, the region has made impressive strides and is now better positioned than ever to take advantage of investors' rising interest. The challenge now is to make the most of the current situation and follow in the dramatic footsteps of similar markets such as Asia or the Middle East.

Fundamentals for the industry are strong. Tourism in Latin America is expected to grow above the global average through 2020. The region's RevPAR increased north of 20% in 2007, making it one of the fastest-growing hotel markets world-wide.

The challenges facing Latin America, such as financing difficulties, a fairly illiquid and hardly transparent market, repatriation of funds, lack of infrastructure or economic and political unrest do not seem enough to deter global investors and operators from focusing on a market which they consider has great potential. The international hotel community believes that thriving economies, increased monetary and political stability, growing tourism volumes and an undersupplied branded quality hospitality market will make of Latin America the next big frontier. The sector, traditionally dominated by domestic independent owners, is opening its doors to overseas institutional investors, while international hotel players strive to position themselves in such a promising market.

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## Executive summary

We have concentrated our efforts on South America

Latin America comprises a wide variety of regions and countries and the market dynamics are not necessarily homogeneous in each sub-region. We decided to narrow the scope of this article to South America mostly, leaving only partly aside Central America and the Caribbean.

In this article we touch on various aspects of the Latin American hotel sector

In this article we provide a brief macroeconomic overview of some of the regions' main markets, only to later plunge into the hotel sector's key dynamics: Latin America's inbound tourism industry and feeder markets, hotel market size, main players and new market entrants, hotel operating statistics, investment climate, transaction activity and financing issues, amongst other subjects.

The market is positive about the region's prospects

Throughout our research we have had the chance to speak with various global hotel operators, consultants and bankers about their views on the Latin American hotel sector. Although details of our findings are later outlined in this report, we can conclude that the market remains optimistic and even enthusiastic about the region's potential. That said, they all point out that risks are not to be underestimated.

Increasing macro stability

At a macroeconomic level, Latin America has made a step forward. Despite a difficult past, the region is now increasingly stable, both from a political and economic standpoint.

Sound fundamentals

The World Tourism Organisation (UNWTO) forecasts that international tourist arrivals in Latin America will continue to grow above the global average growth rate of 4.1% through 2020, which provides a basis for optimism in the longer term. Tourism from the US and Europe continues to grow (although intra-regional travel still dominates), whilst the region continues to be short of internationally branded hotel properties.

Many big global hotel companies have recently shown an interest in entering or further expanding in Latin America

Over the last decade, most of the world's main hotel operators have gradually increased their presence in the region, encouraged by a less volatile political and economic environment. Understandably, in an attempt to reduce country risk, international hotel operators primarily focused on the higher end of the market and, in South America specifically, mostly in capital cities and large metropolitan areas. Today, many international groups are eager to enter or expand on the region, as they believe it offers high potential and sound fundamentals. Operators and other market players seem to be trying to place themselves comfortably in a promising market before it gets too competitive.

A rising number

Traditionally, Latin America's hotel market (especially in South

of institutional investors

America) relied heavily on independent owners and private investors. It was not unusual to see domestic individuals acquiring hotel assets in an attempt to raise their social profile rather than pursuing financial returns. Although that is still sometimes the case, the situation is rapidly changing. In recent years, Latin America has increasingly come up on real estate investors' radar screens. As competition is less intense than in other more mature markets, investing in the region can still be done at reasonable yields. While the volume of foreign investment rises, institutional and more established investors look to enter the sector. This, in turn, should help increase the currently low liquidity levels as well as provide market transparency.

RevPAR in South America growing much faster than in other areas

In terms of hotel operating statistics, Latin America continues to lag behind other areas, which is precisely where part of the region's potential is. There is plenty of room for further improvement. RevPAR in South America is still relatively low in absolute terms. From a growth perspective, the story is quite different. In 2007, RevPAR in South America grew by more than 22% in US\$ terms and by 12% in Euro terms, making it the fastest growing region globally.

Third-party financing can present a challenge in certain countries

Financing remains a challenge that investors face in the region. In South America, there are some markets, like Chile, where debt financing is relatively easy to obtain, with high loan-to-values and at reasonable interest rates. Other markets (like Brazil or Argentina) present higher difficulties, which have limited investment activity in the past. That, according to various market participants, should also change for the better as the market matures.

## **Macroeconomic overview**

### **Introduction**

An increasingly stable market...

Latin America's past political and economic instability has for long deterred investors and has partly given the region a negative reputation which is now hard to break. However, the last few years show a changing picture. Latin America is progressively perceived as a safer investment area, undoubtedly helped by the region's increasing stability at all levels. GDP in real terms is expected to grow by 4.3% in the 2007-2011 period.

### **Key economic indicators**

... as improving economic indicators show

In the table below we show key economic trends and forecasts for some of South America's main markets. Although inherent country risk is still there, these markets have made a step forward and are today better placed than they were at the beginning of the decade. This would be especially the case for Brazil, Mexico and Chile.

The most notable of Latin America's countries, Argentina, Brazil, Chile, Colombia and Mexico have stabilised over the years and are becoming

more attractive to overseas investors. Most currencies in the region have considerably appreciated. JP Morgan's Emerging Markets Equity Research team expects 2008 to be a year of growth and relatively low inflation in Latin America.

**Table 1: Key economics indicators**

	2003	2004	2005	2006	2007E	2008E	2009E	2010E	2011E	2012E
<b>ARGENTINA</b>										
Population (m)					39.4					
GDP (US\$bn)					244.2					
Real GDP growth (%)	8.8	9.0	9.2	8.5	8.4	6.2	4.7	4.4	4.6	4.4
CPI (av, %)	13.4	4.4	9.6	10.9	8.8	11.4	10.5	8.2	6.9	5.9
Exchange rate Ps:US\$ (avg)	2.9	2.9	2.9	3.1	3.1	3.2	3.3	3.3	3.3	3.3
(Appreciation)/Depreciation (%)		0.8	(0.7)	5.2	1.5	3.2	3.1	0.0	0.0	0.0
Lending rate (av, %)					10.6	13.3	12.5	10.3	9.0	8.5
<b>BRAZIL</b>										
Population (m)					189.3					
GDP (US\$bn)					1261.5					
Real GDP growth (%)	1.2	5.7	2.9	3.7	5.1	4.5	4.1	4.0	3.9	3.9
CPI (av, %)	14.7	6.6	6.9	4.2	3.6	4.5	4.1	3.8	3.7	3.7
Exchange rate R:US\$ (avg)	3.1	2.9	2.4	2.2	2.0	1.9	2.04	2.12	2.17	2.22
(Appreciation)/Depreciation (%)		(4.9)	(16.7)	(10.7)	(10.6)	(2.6)	7.4	3.9	2.4	2.3
SELIC overnight rate (av, %)					12.0	11.3	10.7	9.5	9.3	9.3
<b>CHILE</b>										
Population (m)					16.6					
GDP (US\$bn)					163.2					
Real GDP growth (%)	4.0	6.0	5.7	4.0	5.3	4.5	5.0	5.4	5.4	5.4
CPI (av, %)	2.8	1.1	3.1	3.4	4.3	5.4	3.4	3.0	3.0	3.0
Exchange rate Ps:US\$ (avg)	691.4	609.4	560.1	530.3	523.1	512.1	524.5	537.3	550.3	563.7
(Appreciation)/Depreciation (%)		(11.9)	(8.1)	(5.3)	(1.4)	(2.1)	2.4	2.4	2.4	2.4
Short term lending rate (av, %)					8.1	8.2	8.0	8.1	8.1	8.1
<b>COLOMBIA</b>										
Population (m)					47.0					
GDP (US\$bn)					171.6					
Real GDP growth (%)	3.9	4.9	4.7	6.8	6.7	5.5	4.5	3.9	3.8	3.8
CPI (av, %)	7.1	5.9	5.0	4.3	5.5	5.0	4.0	4.0	4.2	4.1
Exchange rate Ps:US\$ (avg)	2877.5	2628.4	2321.1	2358.6	2078.0	2134.0	2321.0	2424.0	2497.0	2541.0
(Appreciation)/Depreciation (%)		(8.7)	(11.7)	1.6	(11.9)	2.7	8.8	4.4	3.0	1.8
90-day deposit rate (av, %)					8.1	8.0	8.0	7.5	7.5	7.5
<b>MEXICO</b>										
Population (m)					108.7					
GDP (US\$bn)					872.6					
Real GDP growth (%)	1.4	4.2	2.8	4.8	3.1	2.7	3.4	3.4	3.5	3.6
CPI (av, %)	4.5	4.7	4.0	3.6	4.0	4.1	3.6	3.4	3.4	3.3
Exchange rate Ps:US\$ (avg)	10.8	11.3	10.9	10.9	10.9	11.2	11.5	11.8	12.0	12.2
(Appreciation)/Depreciation (%)		4.6	(3.5)	0.0	0.0	2.8	2.7	2.6	1.7	1.7
Money market rate (av, %)					7.3	7.3	6.9	6.8	7.0	7.0

Source: Economist Intelligence Unit.

## **Brief country overviews**

Sharp recovery from the late 90's/early 00's

### **Argentina**

The country's economy recovered sharply from the recession of the late 90's/early 00's, stimulated by expansionary policies and high commodity prices. In an attempt to further promote growth, lending rates came down in the fourth quarter of 2007. However, Economist Intelligence Unit expects GDP growth to slow from 2008. Inflows of foreign direct investment will average around 2% of GDP, although uncertainty over government policy will persist.

Brazil, a very attractive market

### **Brazil**

Brazil has been perhaps the most attractive market in recent years, showing strong investor interest. Brazil has realised significant macroeconomic improvements. GDP is forecast to grow by 4.5% in 2008 after growing by more than 5% in 2007. Market conditions are favourable, with the Brazilian Real having appreciated substantially in 2007 and remaining strong into 2008. Brazil has also benefited from a rapidly decreasing interest rate environment. This decline is expected to continue even further over the next few years, although at a slower rate. Mari Canton, Principal at Corporate & Realty Advisors, LLC, told us that Brazil, in her view, should be placed at the top of investors' list. She believes that interest rates will stay at current levels (or even increase slightly) before beginning their inevitable descent – and this is where she sees an opportunity. In her view, as interest rates decline, financing capabilities should open and cap rates could descend by around 200-300bp going forward. Brazil's equity capital markets are also the most liquid in Latin America, with the highest levels of turnover and volume.

In 2007, Brazil absorbed US\$35 billion of net direct foreign investments. It is the second most transparent real estate market in the region after Mexico. According to Wenceslao Bunge, Managing Director, Real Estate Group at Credit Suisse Investment Banking Division, going forward Brazil should be better protected against political instabilities. Much foreign institutional capital has entered the market over the last few years, raising corporates' weight on the country's policy making process.

Chile is perhaps the region's most sophisticated market

### **Chile**

Chile could be considered one of Latin America's most attractive environments. It is a sophisticated market but, because of its small size, it tends to present larger opportunities to domestic rather than international investors. However, these are beginning to gradually enter the market. The number of institutional investors in Chile (namely pension funds) is also higher than in other Latin American countries, more reliant on private investment. In terms of the macroeconomic outlook, Chile's forecasts are very promising. That

said, and ahead of a global economic slowdown, it is important to follow the development of commodity prices, given the country's heavy reliance on this type of goods.

Colombia is generating increasing interest

### **Colombia**

Nicolaas Millward, from UBS' Latin American Equity Capital Markets Group, told us that despite political concerns, international investors have felt increasingly attracted to Colombia as a result of strong growth and a stabilising economic environment. Interest rates levels are lower than in some of the other Latin American markets and the economy continues to grow at healthy rates.

Mexico is Latin America's most transparent real estate market

### **Mexico**

Mexico has also seen a mild drop in interest rates over the last three years, declining around 100bp (from 8% in 2005 to 7% in 2007). Money market rates are forecast to remain stable at around 7%. Its tight link to the US economy may be seen as a double-edged sword. Although this underpins the nation's attractiveness to foreign investment, the country is less isolated than other markets from the deep slowdown in the US. On the other hand, thanks to Mexico having a low-leverage culture, the credit crisis has had less of an impact than in the US (lending penetration is much lower than in other countries). Mexico's equity market is not as large and liquid as Brazil's, but it is still considered a very attractive destination by many international investors. Mexico is the most transparent real estate market in Latin America.

Below we provide summary observations from PricewaterhouseCoopers on various Latin American countries.

**Table 2: PWC's view on Latin America's investment climate**

	<b>Risk level</b>	<b>Risk factors</b>	<b>Return expectations (1)</b>	<b>Debt financing</b>
<b>Argentina</b>	Moderate-high	Economic and political volatility	18-20% unlevered	Not available locally. Sourced internationally at premium rates
<b>Brazil</b>	Moderate	Regulatory complexity; safety and security	18-20% unlevered	Limited financing available locally. Mostly sourced internationally at premium rates
<b>Chile</b>	Low	Limited versatility of economy	At par with US	Sourced both locally and internationally at competitive rates
<b>Mexico</b>	Low-moderate	Safety and security	200bp over US levered	Sourced both locally and internationally at competitive rates
<b>Uruguay</b>	Moderate-high	Dependence on Argentina	n/a	Not available locally. Sourced internationally at premium rates
<b>Costa Rica</b>	Low-moderate	Lack of transparency and regulatory inconsistencies	Starting at 22% levered	Sourced both locally and internationally at competitive rates
<b>Panama</b>	Low	Highly speculative real estate market	n/a	Sourced both locally and internationally at competitive rates

Source: PricewaterhouseCoopers.

(1) By institutional investors, based on interviews with industry stakeholders including developers, institutional investors, hotel operators and local market investors.

### Risk premiums

Argentina/Chile: highest/lowest risk premiums respectively

The table below shows the latest bond ratings and appropriate default spreads for Argentina, Brazil, Chile, Colombia and Mexico according to a study undertaken by Professor Aswath Damodaran of New York University's Stern College. According to this study, Chile carries the lowest risk while Argentina continues to be perceived as a higher risk market.

**Table 3: Country default spreads and risk premiums (January 2008)**

	<b>Argentina</b>	<b>Brazil</b>	<b>Chile</b>	<b>Colombia</b>	<b>Mexico</b>
Long-term rating	B3	Ba1	A1	Baa3	Baa1
Adj. default spread (bp)	450	200	70	135	100
Country risk premium	6.75%	3.00%	1.05%	2.03%	1.50%
<b>Total risk premium</b>	<b>11.54%</b>	<b>7.79%</b>	<b>5.84%</b>	<b>6.82%</b>	<b>6.29%</b>

Source: New York University's Stern College and Moody's.

Notes: the long term risk premiums have been calculated as follows:

- **Adjusted default spreads:** Moody's country rating is taken. The default spread for that rating (based upon traded country bonds) over a default free government bond rate is then estimated. This becomes a measure of the added country risk premium for that country.
- **Country risk premium:** the default spread is adjusted by multiplying it by the relative equity market volatility for that market (standard deviation in country

equity market/standard deviation in country bond). An emerging market average of 1.5 (equity markets are about 1.5 times more volatile than bond markets) has been taken to estimate country risk premium.

- **Total risk premium:** the country risk premium is added to the historical premium for the US of about 4.79% (estimated from US historical data) to get the total risk premium.

[Total risk premium] = [historical premium for US] + [country risk premium] being

[Country risk premium] = [relative equity market volatility] x [adjusted default spread]

Taking Argentina as an example: [11.54%] = [4.79%] + [6.75%] being

[6.75%] = [1.5] x [4.5%]

## Tourism market

### Inbound tourism

Tourism in Latin America is expected to grow above the world average

In terms of international tourist arrivals, the Latin American region is growing fast. Although the Americas recorded growth of 4.7% in 2007, Central and South America grew at 11.1% and 8.1% respectively. Forecasts by the UNWTO indicate that international arrivals to Latin America will continue to grow above the long-term average growth rate of 4.1% through 2020. The individual inbound country forecasts show that, although markets like the US or Mexico will remain the leading destinations, the fastest growth rates will be recorded in Cuba (+9.2% in the period 1995-2020), Argentina (+5.1%), Brazil and the Dominican Republic (+5.0%) and Chile (+4.7%).

An increasing number of tourist organisations and hospitality companies in Latin America are realising the sector's potential in the region. According to an article by Travel Daily News, "there is more professional approach from the tourism bodies to cooperate with local communities in order to proceed into a common sustainable tourism policy that will benefit their counties in the long term".

The Latin America Travel Association remains very positive about the region's outlook

According to the Latin America Travel Association's Chairman, the future looks very positive for the region. He argues that above average tourism growth rates are based on a combination of factors, such as (i) growth starting from a low point, (ii) Latin America being the last continent to discover for many seasoned travellers who have now visited Africa, the Far East or other regions, (iii) global factors which have made Latin America seem more attractive (e.g. SARS, 9/11, generally good political stability), (iv) the weakening dollar and (v) the increase in interest in all things Latin.

### Feeder markets

Latin America received 52.5 million tourists in 2006

In terms of international tourist arrivals, Latin America registered 52.5 million tourists in 2006 (a share of 6.2% in global tourism). Of these, 18.4 million (a share of 2.1%) arrived in South America, with the largest inbound markets being Brazil (5.0 million), Argentina (4.2 million) and Chile (2.3 million). Other markets with more than 1

million tourists included Uruguay (1.7 million), Peru (1.6 million) and Colombia (1 million). Central America and the Caribbean still receive a much larger number of tourists, with Mexico being the leading market by far (more than 21 million tourist arrivals in 2006).

Tourism dominated by intraregional travel

In Latin America, intraregional travel dominates. In the case of the so called ABC countries (Argentina, Brazil and Chile), tourists came mainly from other Latin American countries (58% on average, although less in the case of Brazil), Europe (25% although, again, this would be almost 40% in the case of Brazil), the US (only 12%) and other areas (5%).

South America is still heavily dependant on domestic tourism

The figures above show the importance of domestic tourism for these countries. The number of room nights by domestic travellers can be several times larger than those of international travellers, which highlights the potential for midscale hotel development. These figures stress the difference between this region and other areas like Mexico or the Caribbean, much more heavily reliant on US tourism. That said, and whilst intra-regional travel continued to perform strongly, Central and South America saw the number of European tourists increase, as well as higher expenditure from US travellers.

### **Hotel market size**

Around 2 million rooms in Latin America, of which 1.2 million are in South America

According to the figures published by the World Tourism Organisation and the Secretaría General Iberoamericana in a 2007 report called "Turismo en Iberoamérica", Latin America has an estimated 2 million hospitality rooms (including hotels as well as other types of accommodation). To put this in context, this would represent around 10% of the world's total number of rooms (currently at around 20 million units). South America in particular has around 1.2 million rooms, representing a share of around 6.0% of the global room inventory.

However, a very low percentage of internationally branded hotel rooms

Although official figures may show 1.2 million rooms for South America, it seems clear to us that the amount of internationally branded hotel rooms is way below that number, given that (i) most of the 1.2 million rooms are non-hotel types of accommodation and (ii) of all hotels, the rate of penetration of globally recognised operators is very low. PWC confirmed to us that much of the inventory is made up of small, unbranded properties, with the overall consensus being that the region's hotel sector is still underdeveloped. They also believe that it is dangerous to look at this issue from a macro level, given that each market (e.g. Guanacaste, Buenos Aires or Cancun) has very specific supply and demand characteristics. In addition to this, Ernst & Young points to the fact that room inventory in South America is highly atomised and a large percentage of it corresponds to highly seasonal accommodation, which mostly explains the low occupancy rates

achieved in many areas.

### Main international players

The main brands are already operating in the region

Although there are various international hotel groups with presence in Latin America, we have taken a look at the regional portfolio of the so-called "big 5" hotel companies (namely Accor, Hilton, InterContinental Hotels Group (IHG), Marriott and Starwood). Here are our findings by company:

Accor is highly exposed to the Brazilian market

- **Accor:** a total of 179 hotels in Latin America, which represent slightly less than 5% of the group's total portfolio. Of these, 140 (78%) are located in Brazil. Accor and IHG are the two groups with the largest number of hotels in the region. It should be noted, however, that Accor and IHG are, generally speaking, more focused towards the mid to low end of the market.

Hilton has fewer hotels in the region

- **Hilton:** with 47 properties, Hilton is the group with the smallest presence in the region by number of hotels. For Hilton, Mexico is the country with the highest number of hotels within Latin America (18 properties).

IHG's Latin American portfolio is highly geared towards Mexico

- **IHG:** their figures are very similar to Accor's. A total of 172 hotels in Latin America, which represent 4.5% of the group's total portfolio. The difference with Accor is that IHG's presence is mostly geared towards the Mexican market as opposed to Brazil (104 hotels or 60% of its Latin American portfolio).

Marriott has 62 hotels in the region

- **Marriott:** a total of 62 hotels in Latin America, which represent 1.6% of the group's total world-wide portfolio. Marriott relies heavily on its Caribbean portfolio (42% of their rooms in Latin America).

In relative terms, Starwood is the more highly exposed to Latin America

- **Starwood:** the number of properties in the region (60) is very similar to Marriott's. However, these account for almost 7% of the group's global portfolio, making Starwood the operator with the highest exposure to the region in relative terms (by number of hotels). Again, Mexico would be the most important market for the group within the region, with a total of 20 hotels.

**Table 4: Number of hotels in Latin America by country for the main international hotel operators (2007)**

	<b>Accor</b>	<b>Hilton</b>	<b>IHG</b>	<b>Marriott</b>	<b>Starwood</b>
<b>Central America:</b>	<b>9</b>	<b>22</b>	<b>120</b>	<b>24</b>	<b>24</b>
Costa Rica		1	2	3	
El Salvador		1	2	1	1
Guatemala	1		3	1	1
Honduras		1	3	1	
Mexico	8	18	104	16	20
Nicaragua		1	3		
Panama			3	2	2
<b>Caribbean:</b>	<b>15</b>	<b>13</b>	<b>11</b>	<b>26</b>	<b>7</b>
Aruba			1	4	1
Bahamas	1	1		1	3
Barbados		1			
Cayman				3	1
Cuba	3				
Curacao		1		2	
Dominican Republic	4	2	1	3	
Guadeloupe	1				
Jamaica		1	1	1	
Martinique	3				
Puerto Rico		5	5	6	
St. Kitts & Nevis				2	
St. Martin	2				1
Trinidad & Tobago		2	2	1	
Turks & Caicos	1				
USVI			1	3	1
<b>South America:</b>	<b>155</b>	<b>12</b>	<b>41</b>	<b>12</b>	<b>29</b>
Argentina	4	1	6	1	9
Brazil	140	2	15	6	5
Chile	1		9	2	4
Colombia	4	2	4		3
Ecuador	1	3		1	2
French Guiana	2				
Guyana					1
Paraguay			1		1
Peru	2	1	1	1	1
Uruguay	1	1	1		3
Venezuela		2	4	1	
<b>Total LatAm</b>	<b>179</b>	<b>47</b>	<b>172</b>	<b>62</b>	<b>60</b>
<b>Group total</b>	<b>3,800</b>	<b>2,896</b>	<b>3,863</b>	<b>3,803</b>	<b>896</b>
<b>% in LatAm</b>	<b>4.7%</b>	<b>1.6%</b>	<b>4.5%</b>	<b>1.6%</b>	<b>6.7%</b>

Source: Meridia Capital and Accor, Hilton, IHG, Marriott and Starwood.

Note: the figures above exclude hotels not yet open.

Meridia Capital has talked to some of these groups about their views and their expansion plans for the area. They all coincide in saying that they see Latin America as a place with high potential for hotel development. We summarise below each company's main views.

### **Accor: Roland de Bonadona (Director for Latin America)**

#### **Their plans**

Accor has been developing and operating hotels in the region for around 30 years. The group has committed direct investments to launch its brands, set up a central support platform for the region in

Accor's plans include growing through

economy brands and in urban locations mainly Sao Paulo and build partnerships with local investors. Accor told us that, with 52 hotels in operation, Ibis and Formule 1 are advanced leaders in the economy hotel market in Brazil; Mercure is the largest network in South America, whilst Novotel is confirming its positioning as the upper midscale reference in the region. With improving economic scenarios in key countries within the region, Accor believes it is well prepared to strengthen and consolidate its position.

Although the group remains very positive about Brazil, the idea is re-balancing to an extent the weight of other Latin American countries vs. Brazil. Likewise, the idea is to address their focus towards the urban segment rather than resort type of properties. The group believes that the resort market, especially in the North East of Brazil, will suffer from oversupply in the not so distant future. For this reason, Accor prefers to grow mostly through its economy (Formule 1 and Ibis) and midscale (Novotel and Mercure) brands in urban locations.

Accor has 54 hotels (8,000 rooms) already under development. According to the group, more are under negotiation to complete the Accor brand network - mainly in Brazil, Argentina, Chile, Peru, Colombia and Mexico.

By brand:

- Sofitel: one property is under construction in Buenos Aires, with negotiations underway in Sao Paulo, Brasilia, Santiago and Mexico City; the brand is also planning to go to Lima, Panama City, South Argentina and Costa Rica for resort developments
- Pullman: a newly created upscale brand which the group plans to develop in main regional destinations
- Novotel: Accor recently completed the refurbishment of Novotel Sao Paulo Morumbi; 4 properties are under construction in key destinations: Rio de Janeiro, Cuiaba, Buenos Aires and Lima; negotiations are also underway for new hotels in Bogota, Panama City and Sao Jose
- Mercure: 6 units are under construction, with future conversions in Brazil and Argentina
- Ibis: new developments under construction in Brazil (25 units) Mexico (4 units), Lima, Caracas, Bogota, Asuncion, Buenos Aires (2 units) and Chile (3 units)
- Formule 1: 5 properties under construction in Brazil

#### **Ownership structure**

Co-investment with further sale Although Accor owns some of the hotels that they operate within the region (mostly in partnership with independent owners), many

and leaseback / manageback properties are operated under lease or management contracts. Their strategy is to carry out direct investments whenever they need to cover strategic positions, later selling their stake but retaining the hotels' operations (sale and leaseback or sale and manageback).

#### **On competition**

Accor's view is that, until now, most international groups have grown their regional portfolios through upscale and luxury hotels and mainly through franchise agreements rather than through direct investments. Although competition is increasing, Accor believes that they have established a strong leadership in the midscale and economy segments in Brazil (the region's largest economy). As its current portfolio shows, the group has expanded heavily, based on the premise that in these market segments economies of scale are particularly important.

#### **On the Latin American market**

Investors should learn from previous mistakes Accor believes that Latin America presents many opportunities. Yet in many cases, market potential is smaller than in other large developing regions (South America has a limited GDP of around US\$2,000bn). Examples of oversupply in some markets - like in large Brazilian cities at the beginning of the 00's - prove these limits, which should prompt investors to be more careful in the future. Project financing also remains a problem (and even more so after the subprime crisis), especially in countries with higher interest rates.

#### **Hilton: Simón B. Suárez (Chief Development Representative for Latin America)**

##### **Their plans**

Hilton has ten projects in the pipeline in Latin America and the Caribbean:

- Conrad Bimini Resort (Bahamas)
- Hilton Papagayo Resort<sup>1</sup> (Costa Rica)
- Hilton Ushuaia and Hilton Iguazú Resort (Argentina)
- Hilton Bogota (Colombia)
- Hilton Bonaire (Netherlands Antilles)
- Doubletree by Hilton Resort Puntarenas<sup>1</sup> (Costa Rica)
- Doubletree Cariari by Hilton<sup>1</sup> (Costa Rica)
- Doubletree by Hilton San Juan (Puerto Rico)
- Hilton Garden Inn Liberia Airport (Costa Rica)

<sup>1</sup> Started operating in January 2008

Hilton would like Hilton's objective in Latin America in 2008 is to actively pursue the

to expand its family of brands across the region

expansion of their brands, as the market becomes familiar with the development possibilities that Hampton Inn by Hilton, Homewood Suites by Hilton, Embassy Suites by Hilton, Hilton Garden Inn, Doubletree by Hilton, Conrad and Waldorf=Astoria Collection provide in their respective market orientations. The group believes that the Hilton family of brands is underrepresented in the region and is actively looking for ways to fill that gap.

They consider that for their business hotels all capital cities are important, particularly Santiago, Lima, Buenos Aires and Bogota. In addition to this, Hilton is also identifying secondary markets in the larger economies (like in Brazil and Argentina), where their focused service brands (Hilton Garden Inn and Hampton Inn) would find multiple opportunities. The group is also ready to serve markets that are showing extraordinary development, such as the greater Panama metropolitan area and San Jose.

In terms of their resort portfolio, the group is also keen on expanding it, particularly in the Caribbean, Central America and resort destinations in Argentina, Brazil and Chile. For resort projects, emphasis is being placed on the luxury brands (Conrad and Waldorf=Astoria), as well as on the upscale ones (Hilton and Doubletree by Hilton flags).

No countries to avoid for Hilton

Hilton believes that as international commercial best practices become universal and Latin American and Caribbean economies show increasing stability and growth, there are no countries to avoid. Their view is that by considering opportunities where they present themselves they accomplish their commitment to be a true global family of brands.

A franchise and management group

#### **Ownership structure**

Hilton is fundamentally a hotel franchise and management organisation and that guides the composition of their portfolio in Latin America and the Caribbean. More than 60% of their properties are either franchised or managed. In the future, the group expects this proportion to increase significantly.

Intensifying competition

#### **On competition**

According to the group, competition is increasing as high profile companies turn to Latin America in search of opportunities. Asian luxury chains are also beginning to enter the market.

Hilton's view is that most markets are undersupplied and some that had seen the effects of oversupply some years ago seem to have absorbed the additional inventory. This is the case of Sao Paulo, that has seen a recent improvement in occupancy rates and ADRs. Some

although external elements will probably amplify those markets in the medium term. Costa Rica has not experienced yet the positive effect that can be expected from the Dominican Republic/Central American Free Trade Agreement with the US, while Panama can expect additional growth stimulus from the Panama Canal expansion project.

A region increasingly attractive for institutional investors

#### **On the Latin American market**

Hilton believes that global institutional investors are finding the region attractive as the classical “negatives” of the region diminish. Macroeconomic and political risk is decreasing in most destinations. As commercial activity with major international economies (namely the EU, China, India and the US) increases, investors will find stability and predictability in addition to returns that generally exceed those found in the traditional economies. The trade agreements with the US and the EU should accelerate this process.

#### **IHG: Álvaro Diago (Area President for Latin America)**

##### **Their plans**

IHG will consider opportunities in almost every country that presents a recent good record of economic and political stability, optimistic outlook and good infrastructure.

The group has signed several projects, which are currently under development:

- InterContinental Maracaibo (Venezuela)
- Holiday Inn Manaus (Brazil)
- Holiday Inn Campo Grande (Brazil)
- Holiday Inn Panama Canal (Panama)
- Holiday Inn Express Quito (Ecuador)
- Holiday Inn Express Santo Domingo (Dominican Republic)
- Holiday Inn Express San Jose Forum (Costa Rica)
- Holiday Inn Express San Jose Airport (Costa Rica)
- Holiday Inn Express Hotel & Suites Cartagena (Colombia)
- Holiday Inn Express San Pedro Sula (Honduras)

Besides that, the group just converted on February 1st the Corobici Hotel in San Jose to the Crowne Plaza Corobici San Jose (Costa Rica).

Several projects in the pipeline

In addition to this, various other projects are in advanced stages of negotiation and should be signed within the first half of 2008.

When asked about their priorities for the region, IHG told us the

following:

By brand:

- The penetration of the InterContinental Hotels & Resorts brand in capital cities (such as Lima and Bogota) as well as resort destinations (especially in the Northeast coast of Brazil)
- The penetration of the Crowne Plaza brand in primary and secondary cities
- The introduction of the Hotel Indigo brand in cosmopolitan cities in Latin America
- The expansion of the Holiday Inn and Holiday Inn Express brand in Central America, the Caribbean and South America

By country:

- Mexico, due to its proximity to the US and their participation in the North American Free Trade Agreement (NAFTA)
- Brazil, due to its pungent economy, vast territory and exposure to the international market
- Argentina, which has been experiencing economic stability and growth in the past years with positive prospects for the next years
- Colombia, which is recovering its economic position and image in Latin America and the world
- Central America in general, which is also growing and getting more stable, both economically and politically; specifically, the group is actively looking for resorts in Costa Rica

#### **Ownership structure**

Mostly a franchise operator

A large percentage of IHG's hotels in Latin America are operated under franchise agreements. Around 74% of their hotels are franchised, 16% are managed, 8% are leased and only 2% are owned (note: these percentages have been calculated excluding portfolio in Mexico).

#### **On competition**

IHG believes that, for many hotel companies, Latin American is becoming increasingly attractive as an area for future expansion. Some chains that have been in the region for many years are still struggling to expand and others are trying to break through these markets. According to the group, Latin America is very traditional and thanks to their legacy in the region they have been able to gradually but steadily increase their presence there.

International

In the past, growing supply had a negative effect in certain markets

chains should be well positioned ahead of increasing competition

and this may continue to be so in the future. This negative effect ends up affecting all hotels in those specific markets. However, IHG has noticed that thanks to the globalisation phenomenon and guests' increasing loyalty, international chains are the ones who tend to recover the fastest, mostly thanks to the strong structure behind them - especially in Sales, Marketing and Technology.

#### **On the Latin American market**

IHG believes that, despite the negatives, Latin America offers high potential and that institutional investors will find the region's real estate and hotel sectors increasingly appealing. Their view is that, overall, the region has been experiencing sound economic and political stability compared to previous decades and that, although this is a slow process and it may take some time, the sector is moving on the right direction.

#### **Marriott: Rodolfo Guilloli (Vice President Development for Caribbean and Latin America)**

##### **Their plans**

Marriott's most relevant projects in the pipeline include the following:

- 250 room Marriott in Puerto Peñasco (Mexico)
- 170 room Ritz-Carlton in Mexico city, with 170 branded residences
- 290 room Marriott in Merida (Mexico)
- 300 room Renaissance in Panama City (Panama)
- 160 room Marriott in Cuzco (Peru)
- 220 room Ritz-Carlton in Cap Cana (Dominican Republic), with around 200 branded residences
- 120 room Ritz-Carlton in Guanacaste (Costa Rica), with 60 branded residences
- Around 10 Courtyard by Marriott hotels in Mexico, Central America and the Caribbean

Brazil is a priority for Marriott

Mexico continues to be the most successful country for the group in Latin America. However, the main challenge and a big focus of their effort this year will be in Brazil, given its size.

In terms of brands, Marriott has several priorities:

- Take advantages of synergies to continue expanding the Ritz-Carlton brand (both hotel and residences)
- Expanding the Courtyard by Marriott brand in South America and Mexico

- Expanding new brands (such as Edition, the new Marriott-Schrager brand)

Around 70% of Marriott's properties are managed

#### **Ownership structure**

Approximately 70% of Marriott's properties are managed and more than 25% are franchised. Although it owns one or two hotels in the region, the group is looking forward to changing such position. No hotels within the region are leased.

#### **On competition**

Marriott believes that Latin America is generating increasing interest and that peer hotel groups are moving aggressively into the region.

In terms of new development, 2006 and 2007 were two record years for the group

According to Marriott, certain markets are likely to suffer the impact of oversupply if hotel development continues to grow at current trends (such as Panama City). Other markets have not recovered yet from this effect (like Sao Paulo). However, the region as a whole still has significant growth potential. Subscribing this, Marriott reminded us that they just had two consecutive record years in terms of new development in the region.

#### **On the Latin American market**

Marriott is convinced that Latin America will progressively become more attractive for global investors. They have recently seen several major institutional investors come into the market, attracted by the region's potential (such as Goldman Sachs or Lehman brothers, as well as sophisticated mid-sized players such as hospitality funds). This is beneficial for the area, particularly with the existing uncertain environment in the US market.

Outside the "Big 5", we also contacted Four Seasons Hotels & Resorts. Their comments illustrate that it is not only the world's largest hotel groups that are attracted by Latin America's developing hotel market. Other equally international and renowned players also have aggressive plans to grow in the region. Out of a total of 75 operating hotels, Four Seasons currently manages 7 hotels in Latin America (2 in Mexico, 1 in Costa Rica, 1 in Bahamas, 1 in Nevis, 1 in Uruguay and 1 in Argentina).

#### **Four Seasons: Erika Hansen (Development Manager)**

##### **Their plans**

Four Seasons' pipeline in Latin America is as follows:

- In the Caribbean: the group currently has 2 projects announced: Barbados and a resort within the master planned development of Casa de Campo in the Dominican Republic.

- In Central America, they have signed a Letter of Intent for a project on a private island in Belize and are actively investigating both urban and resort projects in Panama.
- In South America, they are pursuing opportunities in Brazil regarding projects in Sao Paulo, Rio and beach destinations. The group is also evaluating projects in Colombia, Chile and Peru.

Four Seasons considers these markets strategic because they are either (i) large business centres (many of which also have a significant tourist draw) or (ii) they are established luxury resort destinations (or on the verge of reaching that "tipping point", as Costa Rica was when they entered the country).

#### **Ownership structure**

A management group with minority investments

Four Seasons is a management services company, which operates under long-term management contracts of typically 80 years. The group neither owns the hotels that it operates nor participates in leases or franchises. However, they are minority investors in several of the hotels that they manage.

#### **On supply**

Four Seasons believes that the luxury segment is undersupplied

Four Seasons told us that they have definitely seen a growing interest in Latin America from their guests and developers. They believe that the large majority of the markets on their priority list are under-supplied in the luxury segment and that it will be quite some time until over-supply is an issue for them or any of their direct competitors.

#### **On the Latin American market**

Increasing investor and guest interest in the region makes Latin America the natural next step for Four Seasons

For them, Latin America is an untapped frontier. As established and reputable international hotel brands begin to show more interest in the region, investors willing to accept the ingrained risk will follow those brands to the market. Four Seasons' view is that currency valuations in particular will be a catalyst for investment in the region (e.g., strength of Euro stimulating Spanish capital to consider South America as an investment alternative). Like Asia and the Middle East, greater transparency will stimulate additional investment, although Latin America will always have its own unique characteristics.

#### **New hotel supply**

Many new hotels are bound to open in the Caribbean and Central America over

Favoured amongst other things because of good weather all year round and their proximity to the US, the Caribbean and Central America have gathered a great deal of new hotel projects that should come into the market over the next two to three years. Numerous hotel brands will either establish their presence in the region or further expand their existing operations. To name an example, The Ritz-

the next two to three years

Carlton Company (owned by Marriott International and with a portfolio of 66 hotels world-wide) plans to open 4 hotels in the Caribbean area between now and 2010 (Turks & Caicos in 2008 and St. Lucia, Bahamas and the Dominican Republic in 2010 – the latter also mentioned above).

In South America, the rate of expansion is significant. Below we provide a few recent examples for some of the region's main markets:

Puerto Madero in Buenos Aires should see the opening of several hotels in the near future

- **Argentina:** according to HVS International, there are several potential projects in the pipeline or already under development in Buenos Aires and outside the capital city. In particular, it is worth mentioning the new 160 room St. Regis hotel in Puerto Madero (due to open in May 2010), the 5411 project also in Puerto Madero (2010), Hotel Faena – a project by Sir Norman Foster - in Puerto Madero (2010), the Park Hyatt, a new luxury hotel from Jumeirah and the Novotel and Ibis hotels for 2008 that Accor mentioned to us. Outside Buenos Aires, Starwood has plans to open two hotels in 2008 (including a Four Points property). There is also the Sheraton Mendoza (opening April 2008), and the Hilton and Park Hyatt resorts in Iguazú, just to mention a few.

HVS's view is that Argentina is leading the business in Latin America. Buenos Aires is the best example, with no other city in the region registering such high levels of occupancy (close to 80%) and ADR (US\$300-350 for luxury hotels).

Sao Paulo severely affected by oversupply issues

- **Brazil:** new hotel supply is limited in Rio de Janeiro and especially in Sao Paulo. Over the last few years, Sao Paulo has suffered an oversupply problem that the city is still digesting. During the late 90's, a large number of condo-hotel projects were brought into the market. These were not easily absorbed by demand at the time. The increase in supply in the mid-scale segment inevitably captured part of the five-star demand. In addition to this, between 2002 and 2003 three boutique hotels opened (Emiliano, Unique and Fasano), as well as the Grand Hyatt and the Hilton. Consequently, occupancy rates fell severely. Sao Paulo is still recovering from the situation, with supply growth in the city being virtually non-existent.

However, hotel supply in the North East of Brazil is rapidly growing

The North East of Brazil, however, is a different story. As stated above, the area is witnessing numerous resort development projects. In fact, it is the only place in the country where it is reasonably easy to obtain financing for new hotel construction. The government sponsors Banco del Nordeste with the aim of encouraging tourism in the region. An expanding international

and domestic flight network should also benefit the area.

Over the long run, Brazil's hosting of the 2014 Soccer World Cup should prove highly beneficial and should strengthen the country's hotel market.

The number of rooms in Santiago is growing at an average rate above 6%

- **Chile:** over the next three years, Santiago expects to see an additional 600-700 rooms come into the luxury/upscale segment. There are currently two important projects under construction: (i) a W hotel expected to open by mid 2009 and (ii) a Hilton hotel. Based on an estimated 10,000 rooms in Santiago (around one-third of Chile's), the number of new rooms represents growth of around 6.5%. This is very much in line with the growth seen over the past 15 years, when the number of rooms grew at a CAGR of 6.1%. For a market characterised by low levels of ADR, new supply could potentially have an effect.

In Chile there are also new hotel projects outside the capital city

Hotel capacity is also growing outside the capital city. According to Hosteltur, Accor is planning to open 10 new hotels in the country over the next four years (mainly under the Sofitel, Mercure and Ibis brands). Other new projects under way include the new 138 room Park Hyatt Patagonia, expected to open in 2009.

Various operators have announced new projects in Colombia

- **Colombia:** Bogota and Cartagena are said to be two very active markets. Both cities are undersupplied and in need of new hotel rooms. Hosteltur stated in a recent article that the government planned to increase Colombia's room inventory by an additional 10,000 rooms by 2010 (current number of rooms in the country is close to 60,000). The "big 5" hotel groups and others such as Hyatt or Sonesta International have already announced their entry into the country or the expansion of existing operations.

It is worth highlighting that out of the "big 5" hotel operators, four already have a presence in Colombia. Only Marriott is missing, although it will soon be able to put its flag on the country. The group has two hotels in Bogota under development (a Marriott and a JW Marriott). In addition to this, the company has signed an agreement with Grupo Poma to develop 5 Courtyard by Marriott hotels in key Colombian cities (the first of which will be in Cali). Hilton, on the other hand, is expanding its operations in the country (the group currently runs a hotel in Cartagena). A new 245-room Hilton hotel is under construction in Bogota. In Cartagena, a W hotel is in the pipeline, while Sonesta expects to open a new mixed-use hotel

project by mid-2009.

Several new hotel projects also in Peru

- **Peru:** according to HVS International, the luxury segment in Peru is undergoing constant growth. The tourism market and the region in general “are experiencing a boom, which accounts for the arrival of new players ready to make the most of the situation”. Last November, a franchise agreement between Starwood and Hoteles Libertador (a domestic chain) involved remodelling the Cuzco hotel and building two new hotels in Lima and Urubamba. The Libertador Cuzco Luxury Collection will re-open in 2009, whilst the new Libertador Urubamba Luxury Collection will open in early 2010. The Westin Libertador Lima (the first Westin in South America) will feature 311 rooms and will also open in early 2010.
- In **Central America**, Costa Rica comes up as the place to be. RevPAR there has doubled over the last 5 years. According to Jones Lang LaSalle Hotels, hotel foreign direct investment is projected to rise by 300% in 2010, sourced primarily by US and Costa Rican partnerships. In addition to this, and according to Hotels Magazine, if Costa Rica is a “must have”, Panama is one that “would be good to have”.

## Operating statistics

### Occupancy rates

Occupancy rates in South America are still quite low

Despite healthy growth rates so far this year, hotel occupancy rates in South America are still low compared to the rest of the world. Taking Smith Travel Research and The Bench figures to December 2007, South America showed an occupancy rate of 63.8%, below that of Asia Pacific, Europe or the Middle East although marginally above that of North America.

**Table 5: Hotel occupancy rates**

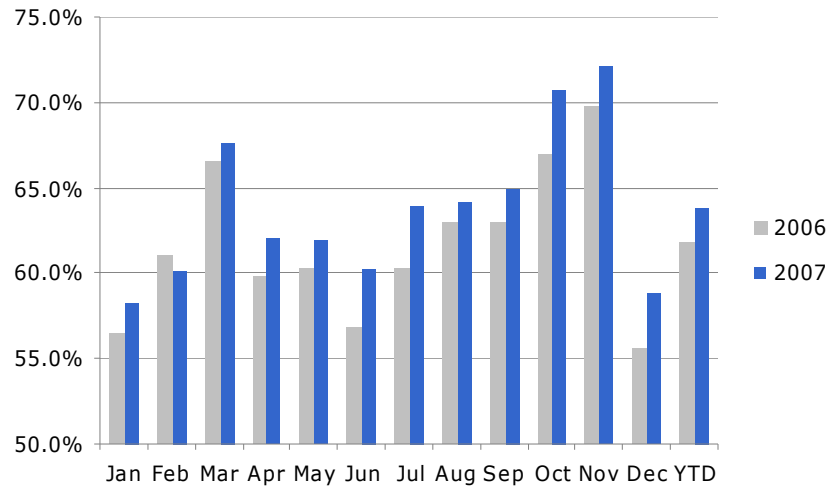
	<b>2007</b>	<b>2006</b>	<b>Growth</b>
Asia Pacific	69.6%	70.6%	-1.4%
Americas	63.3%	63.4%	-0.2%
North America	63.3%	63.3%	0.0%
Caribbean	66.5%	68.2%	-2.5%
Central America	70.7%	68.4%	3.4%
<b>South America</b>	<b>63.8%</b>	<b>61.8%</b>	<b>3.2%</b>
Europe	69.1%	68.9%	0.3%
Middle East/Africa	69.7%	66.5%	4.8%

Source: Smith Travel Research and The Bench.

In terms of seasonality, monthly data for 2006 and 2007 showed that occupancy rates tend to peak in March during the first half of the year (March being a very strong month in the Southern hemisphere). This is

followed by a weaker April to June period, only to progressively recover from July to November.

**Chart 1: South America - monthly occupancy rates**



Source: Smith Travel Research and The Bench.

**Average daily rates**

Average daily rates are also low when compared to other areas

As it is the case with occupancy rates, room rates in South America are considerably below those in other areas. In 2007, the region recorded an average ADR of around US\$109. This is slightly above the data shown for the Americas as a whole. However, room rates are still low compared to Europe or the Middle East and, especially, the Caribbean. In our view, the fact that the Americas shows the lowest rates would be explained by the weight that North America has within the whole region and the larger sample of hotels (including the lower segment) that North America would encompass.

Growth rates in € terms affected by weakness of US\$

In the table below we show ADRs in 2006 and 2007 both in US\$ and in Euros. Due to the significant weakness of the US currency, growth rates based in Euro terms are considerably below those based in US\$ terms. In any case, it is worth highlighting South America's high room rate growth, close to 19%.

**Table 6: Hotel average daily rates**

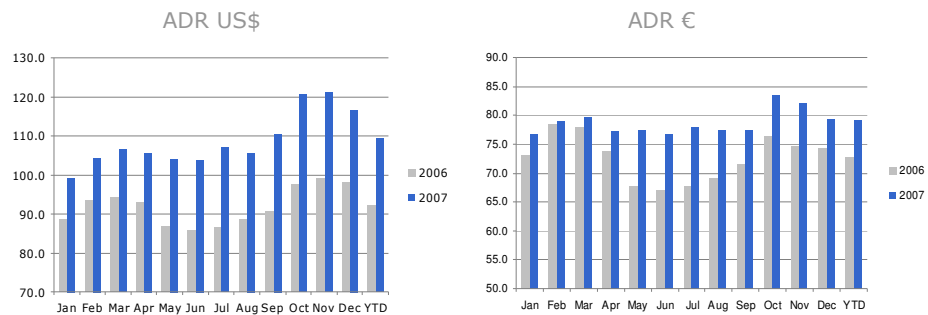
	2007 (\$)	2006 (\$)	Growth	2007 (€)	2006 (€)	Growth
Asia Pacific	129.3	115.6	11.9%	93.6	91.3	2.5%
Americas	105.2	99.0	6.2%	76.3	78.3	-2.5%
North America	104.5	98.4	6.1%	75.8	77.8	-2.6%
Caribbean	206.4	195.8	5.5%	150.5	155.7	-3.3%
Central America	119.4	106.4	12.2%	86.8	84.3	3.0%
<b>South America</b>	<b>109.4</b>	<b>92.2</b>	<b>18.7%</b>	<b>79.1</b>	<b>72.9</b>	<b>8.5%</b>
Europe	161.3	137.7	17.1%	116.6	108.6	7.3%
Middle East/Africa	168.3	144.5	16.4%	121.8	114.2	6.6%

Source: Smith Travel Research and The Bench.

Note: According to the methodology used by Smith Travel Research and The Bench, any aggregated number (which would apply in the case above) uses the exchange rate of each relative month. The implied average exchange rate used for the period as a whole was 1.38US\$/€ in 2007 and 1.26US\$/€ in 2006.

Looking at seasonality trends, the pattern followed by ADRs is very similar to that of occupancy rates.

**Chart 2: South America - monthly ADRs (in US\$ and €)**



Source: Smith Travel Research and The Bench.

### RevPAR

Although with low RevPAR figures in absolute terms, South America was the fastest-growing region in 2007

As a result of the above, RevPAR in South America was not as high as in other areas. In terms of growth, however, the story is quite different. South America has been registering aggressive RevPAR growth, driven mostly by an increase in ADRs (as shown above). In US\$ terms, RevPAR in the region during 2007 grew by more than 22% compared to the previous year. In Euro terms, this translates into a growth rate of 12%, making South America the fastest growing region world-wide.

**Table 7: Hotel RevPAR**

	2007 (\$)	2006 (\$)	Growth	2007 (€)	2006 (€)	Growth
Asia Pacific	90.0	81.6	10.3%	65.1	64.5	1.0%
Americas	66.6	62.8	6.0%	48.3	49.6	-2.7%
North America	66.1	62.3	6.1%	48.0	49.3	-2.6%
Caribbean	137.3	133.5	2.8%	100.1	106.2	-5.8%
Central America	84.4	72.8	16.0%	61.4	57.7	6.5%
<b>South America</b>	<b>69.8</b>	<b>57.0</b>	<b>22.5%</b>	<b>50.5</b>	<b>45.0</b>	<b>12.0%</b>
Europe	111.4	94.9	17.4%	80.6	74.9	7.6%
Middle East/Africa	117.3	96.1	22.0%	84.9	75.9	11.8%

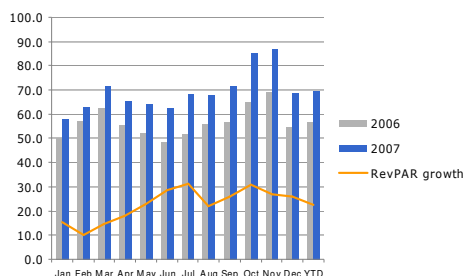
Source: Smith Travel Research and The Bench.

Note: According to the methodology used by Smith Travel Research and The Bench, any aggregated number (which would apply in the case above) uses the exchange rate of each relative month. The implied average exchange rate used for the period as a whole was 1.38US\$/€ in 2007 and 1.26US\$/€ in 2006.

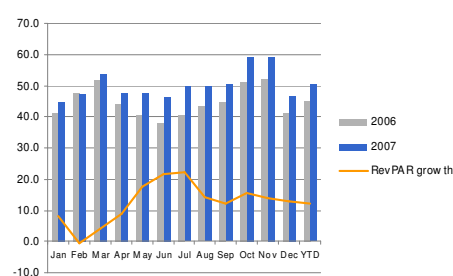
Monthly performance in 2007 shows that RevPAR growth accelerated since the beginning of the year, creating an upward trend. Since May, RevPAR grew north of 10% in both US\$ and in € terms.

**Chart 3: South America – monthly RevPAR (in US\$ and €) and % growth**

RevPAR (US\$) and % growth



RevPAR (€) and % growth



Source: Smith Travel Research and The Bench.

Albeit lower profits, operating margins in Latin America are similar to those in other areas

Although occupancy rates and ADRs in Latin America may be lower than in other parts of the world, margins are not far from those seen in other regions. The cost base in Latin America is below US or European standards. PKF Hospitality Research stated in a recently released report that certain cost categories (such as labour costs and property taxes) are proportionately lower in the Caribbean compared to the US. Despite the fact that this is offset by higher utility and insurance costs, in absolute terms total costs would still be below the levels seen in the Western world. The overall effect is, therefore, similar net operating income margins.

**Performance in key cities**

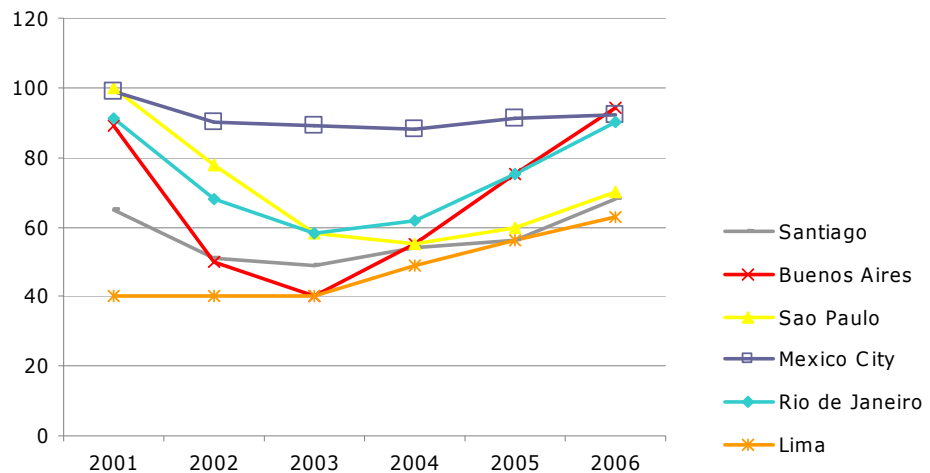
Buenos Aires,

The chart below shows RevPAR figures in US\$ during the 2001-2006

Mexico City and Rio de Janeiro have higher RevPAR figures than Sao Paulo, Santiago and Lima

period for six key cities in Latin America: Santiago, Buenos Aires, Sao Paulo, Mexico City, Rio de Janeiro and Lima. The underlying data shows higher RevPAR figures than those mentioned above. We understand that this is due to the above referring to the region as a whole rather than just large metropolitan areas. In 2006, RevPAR for this group of cities was somewhere in the US\$65-95 range. That said, Buenos Aires, Mexico City and Rio de Janeiro registered higher figures than Sao Paulo, Santiago and Lima.

**Chart 4: Latin America cities RevPAR (2001-2006) (in US\$)**



Source: HotelBenchmark™ Survey (Deloitte) and Meridia Capital estimates.

RevPAR in all six cities recovered sharply from 2003

It is important to highlight the major recovery seen in all six cities from 2003-2004. While performance in Mexico City has been relatively stable, RevPAR in cities like Buenos Aires or Rio de Janeiro has been much more volatile. These cities saw RevPAR decline severely in 2002-2003 but showed a very strong recovery from 2004 onwards. Sao Paulo also suffered a similar downturn, although the recovery was not as sharp. RevPAR in Santiago improved progressively and rose aggressively in 2006. Lima also showed a considerable improvement in RevPAR in the 2004-2006 period, although coming from a lower base.

The first of the two tables below shows Deloitte’s HotelBenchmark™ Survey monthly operating statistics for Buenos Aires, Sao Paulo, Santiago and Mexico City in 2007. According to these figures, Buenos Aires is the market with the highest RevPAR, followed by Mexico City and Santiago and then Sao Paulo. However, despite showing lower RevPAR levels, Sao Paulo has seen the highest growth rates this year, which shows that recovery is on the way. In addition to this, we also include Deloitte’s HotelBenchmark™ Survey’s comments on these countries’ hotel sector.

**Table 8: Monthly hotel performance data (2007)**

	2006	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
<b>Buenos Aires</b>													
Occupancy (%)	73.0	67.6	77.6	81.6	74.2	66.0	64.2	61.2	64.8	72.6	82.3	89.2	79.3
ARR (US\$)	124.0	135.0	138.0	145.0	138.0	135.0	126.0	128.0	132.0	143.0	162.0	167.0	163.0
RevPAR (US\$)	90.5	91.3	107.1	118.3	102.4	89.1	80.9	78.3	85.5	103.8	133.3	149.0	129.3
<b>Sao Paulo</b>													
Occupancy (%)	56.9	51.2	51.7	68.9	62.5	65.1	62.8	62.8	65.9	61.9	69.7	62.4	53.1
ARR (US\$)	88.0	87.0	95.0	107.0	100.0	110.0	101.0	99.0	104.0	112.0	145.0	122.0	90.0
RevPAR (US\$)	50.1	44.5	49.1	73.7	62.5	71.6	63.4	62.2	68.5	69.3	101.1	76.1	47.8
<b>Santiago</b>													
Occupancy (%)	70.6	73.3	68.5	81.6	75.5	62.1	65.6	77.9	72.8	67.6	78.1	86.3	73.1
ARR (US\$)	103.0	121.0	111.0	126.0	127.0	115.0	112.0	104.0	112.0	112.0	129.0	146.0	125.0
RevPAR (US\$)	72.7	88.7	76.0	102.8	95.9	71.4	73.5	81.0	81.5	75.7	100.7	126.0	91.4
<b>Mexico City</b>													
Occupancy (%)	63.1	54.1	65.4	70.8	54.7	63.3	65.2	61.0	62.1	63.1	74.1	73.1	50.5
ARR (US\$)	140.0	149.0	159.0	161.0	155.0	156.0	157.0	146.0	147.0	158.0	148.0	158.0	135.0
RevPAR (US\$)	88.3	80.6	104.0	114.0	84.8	98.7	102.4	89.1	91.3	99.7	109.7	115.5	68.2

**Notes:**  
Data in this table may differ from the data shown in the graph above due to different sample sizes. The chart above is based on a sample that only includes hotels that were already open in 2001 through to 2006. The data shown in this table is based on a HotelBenchmark sample representing approximately 120 hotels across the region. Data for 2006 is 12-month running average.

Source: HotelBenchmark™ Survey (Deloitte) and Hotels Magazine.

**Table 9: Growth rates (in %) for monthly hotel performance data (2007)**

	2006	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
<b>Buenos Aires</b>													
Occupancy	-0.6	-3.2	1.8	-5.2	-6.2	-7.9	4.3	3.8	1.7	2.2	4.2	0.4	16.9
ARR	19.9	24.3	23.0	16.5	11.4	14.7	17.0	11.9	17.8	16.5	20.0	13.8	14.2
RevPAR	19.1	20.4	25.2	10.5	4.5	5.7	22.1	16.1	19.9	19.1	25.1	14.2	33.5
<b>Sao Paulo</b>													
Occupancy	10.1	13.1	-8.2	13.7	14.2	14.6	15.8	11.0	-0.9	-0.1	8.9	3.3	1.4
ARR	12.3	8.5	3.2	16.8	13.0	33.9	27.3	29.0	21.5	35.7	36.4	32.7	29.6
RevPAR	23.6	22.8	-5.3	32.8	29.1	53.4	47.4	43.2	20.4	35.5	48.5	37.1	31.4
<b>Santiago</b>													
Occupancy	10.5	-2.0	-2.6	-4.8	2.9	-10.9	15.4	21.1	13.5	5.1	4.0	3.9	7.3
ARR	10.1	18.2	14.1	4.4	12.9	7.2	13.9	6.6	12.6	13.4	16.7	24.2	16.4
RevPAR	21.6	15.8	11.1	-0.6	16.2	-4.5	31.4	32.3	27.9	19.2	21.3	29.0	24.9
<b>Mexico City</b>													
Occupancy	-0.7	-4.0	-7.3	-9.9	-0.3	-5.0	0.1	4.4	6.1	1.1	1.8	6.8	4.6
ARR	4.3	3.2	3.0	6.0	8.2	10.2	12.9	6.5	5.9	14.4	5.2	6.5	10.0
RevPAR	3.6	-0.9	-4.6	-4.5	7.8	4.7	12.9	11.2	12.4	15.6	7.1	13.8	15.1

**Notes:**  
Data in this table may differ from the data shown in the graph above due to different sample sizes. The chart above is based on a sample that only includes hotels that were already open in 2001 through to 2006. The data shown in this table is based on a HotelBenchmark sample representing approximately 120 hotels across the region. Data for 2006 is 12-month running average.

Source: HotelBenchmark™ Survey (Deloitte) and Hotels Magazine.

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**Table 10: Extract on South America from the Hotel Benchmark™ Global Performance Review (2007)**

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**Argentina**

Good exchange rates and a growth in tourists balanced out Argentina's relatively minor social problems. Latest results from the World Tourism Organisation (UNWTO) confirm that international tourist arrivals are growing, continuing the upward trend since the political instability of 2002 and devaluation of the Peso. Most visitors come from the USA, Brazil or Chile, although more people are coming from the rest of Latin America. Marketing aimed at China is widening Argentina's appeal. With romantic images of Spanish colonial architecture, café culture, and street tango, the vibrant city of Buenos Aires is again capturing the imagination of tourists. In a response to increased demand, the hotel industry is dancing to the same tune. New developments in the four and five-star sector are boosting the city's supply. MICE tourism is seeing strong growth as the government actively promotes this sector.

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**Brazil**

With so much promise, but so many problems, Brazil has yet to fulfil its massive potential as a holiday destination. Stimulated by state investment in infrastructure and incentives targeted at developers, the government tourism body, Embratur, is encouraging hotel investment along Brazil's north-eastern beach resorts. Embratur has also opened dedicated tourism offices in the US and major European cities in an attempt to drive up international arrivals to Brazil, which has traditionally relied on domestic tourism. While around 65m Brazilians holidayed at home in 2006, just 6m international visitors joined them. The importance of more tourists from overseas is clear – while domestic tourists embrace the low-cost culture initiated by GOL Airlines and Accor's Formula 1 brand, international visitors are prepared to spend much more. The 6m international tourists spent around US\$5 billion in Brazil – the same amount as the 65m domestic tourists.

One long-term problem for Brazil has been its lack of air links with Europe. However, new direct flights to Sao Paulo are having an impact. About Rio - with the Ipanema and Copacabana districts already over-developed, there is little land left for construction. Sao Paulo is performing well. Sao Paulo, as the main financial centre of Brazil and with excellent conference and exhibition facilities, is a magnet for MICE tourism.

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**Chile**

Since the devaluation of the Argentinean Peso in 2002 – which severely dented Chile's arrival figures – the government, along with the Corporacion Promocion Turistica (CPT) has been improving facilities to attract high-spending visitors. Aided by Chile's national carrier LAN, long haul arrivals from Europe, North America and, more recently, China rocketed to over 2.2m in 2006, according to the UNWTO.

Economic stability, security and a modern tourism infrastructure have all helped, as have Chile's wide range of products - from ecotourism resorts in Patagonia, to skiing in new luxury centres close to Santiago. As the daily spend of long-haul visitor is nearly three times higher than short-haul, it is understandable that the CPT intend to expand this end of the market. As the central gateway city, Santiago is the hub of all Chilean tourism, and an increasingly important business centre. The boom of hotel construction in 2004 and 2005 - when five international brands were opened - created something of a price war. This calmed down in 2006.

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**Mexico**

Hurricane Wilma wiped out the Gulf coast - the area that brings in 65% of the country's revenue - and so the impact was harsh. 2006 was a year of restructuring, and visitor numbers fell by 2.8%. Economist Intelligence Unit (EIU) estimates that some US\$2.7billion has been pledged towards repairing the damage. The bulk of this money came from private investors. The political climate is stable, as presidential elections have come and gone without the economic shocks that have greeted previous voting. Stable relationships with its US neighbour are also valued, as around 85% of visitors to Mexico cross the border from the US. New air routes between the two countries are encouraging more people to pay a visit. The high-altitude capital of Mexico City enjoyed steady growth throughout 2006.

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Source: HotelBenchmark™ Survey (Deloitte).

## **Hotel investment climate**

Argentina, Brazil and Mexico are said to be some of the strongest markets in Latin America. Foreign investments in Mexico grew considerably after the country achieved investment grade status. Brazil is expected to follow in the future, with investors gradually allocating more funds to the country's real estate market. The region, traditionally dominated by local groups, is quickly opening up to the international investment community.

Meridia Capital has talked to several consulting firms about their views on the Latin American hotel market. Our findings are detailed below.

## **HVS: Arturo García Rosa (Senior Partner and founder of HVS Buenos Aires office)**

### **Strategic areas**

HVS is very optimistic about South America and Buenos Aires specifically

HVS considers that Buenos Aires, Lima and Bogota present interesting opportunities for upscale and luxury mixed-use hotel and residential projects. Meanwhile, North East of Brazil, Cartagena, Costa Rica and Patagonia (both in Argentina and Chile) are considered attractive markets for resort development.

According to HVS, investors are most highly interested in Buenos Aires and the North East of Brazil:

- Buenos Aires is considered a great city, where the level of hotel performance has improved considerably, growing steadily over the last 4-5 years. In 2007, the luxury segment achieved occupancy rates of 70% with ADRs of US\$350. The last quarter of the year was excellent and 2008 is expected be another great year, improving on 2007 performance.
- The North East of Brazil is generating high interest, although this comes mainly from Spanish and Portuguese investors. The area is well known for its natural beauty and its good weather all year round. The fact that it now has direct flights from Europe is a plus.

HVS confirmed that "hotel operators are definitively interested in the South American region". The market as a whole is growing and it is expected to continue growing over the next 4-6 years. This even applies to Sao Paulo which, after suffering from oversupply for years, is now beginning to recover. On Argentina, HVS' view is that investments will, with no doubt, multiply throughout the country as long as problems such as air transport are solved. In the upscale markets of Lima and Santiago, hoteliers have managed to break the US\$200 ADR barrier coupled with sustainable occupancy rates. In addition to this, HVS believes that there is a tremendous opportunity to develop mid market branded properties throughout the region (with

the exception of Sao Paulo), given the huge gap in this market segment.

**On investors**

Global institutional investors are beginning to study the region and to understand its market dynamics. Many will be attracted by the area's high potential. HVS says that they expect to see further movements in this regard during 2008 and no later than 2009.

**On risks**

Most governments are promoting private investment

For years, unstable political regimes have been Latin America's biggest problem. However, as time goes by, governments are beginning to fully understand the rules of democracy and its implications for the macroeconomic environment. Most are promoting private investment, knowing that they will not be able to solve the underdevelopment/poverty problem without a strong and competitive open market.

**Ernst & Young: Luciana Tarnoski (Argentina - Real Estate Group)**

**Strategic areas**

Proximity to the US is important according to E&Y

The markets that are generating the most interest from hotel investors/operators are those located less than four hours away from any Southern airport in the United States. They are considered strategic not only for their climate, geography and culture, but also for their capacity to attract simultaneously both the high end and mass market segments.

While nowadays the most outstanding countries are Mexico, Costa Rica, the Dominican Republic and Panama, others that are strenuously growing are El Salvador, Guatemala and Northern Brazil.

**On investors**

Investor's perception of Latin America is changing

Local investment groups and private investors still dominate the Latin American market. The region has lower tourism volumes than Asia or the Middle East, whilst its financial markets are not as developed. Although this has deterred investors in the past, Latin America is increasingly seen as an interesting area for investment.

**On risks**

Mexican economy's dependence to the US has put additional pressure on the country after the subprime markets debacle. The rest of countries in Latin America are less dependent, although it remains to be seen how isolated from the problem they can be.

Political stability

On the basis that political instability is perhaps one of Latin America's

is key for foreign investment

biggest risks, it is important to evaluate how the lack of consistency within different presidential periods affects the countries' development. The same applies to foreign investment conditions. Countries like Colombia are currently supporting foreign initiatives, while places like Venezuela or Argentina are seen as less inviting.

### **PricewaterhouseCoopers: Isabelle Claver (Director, Hospitality and Leisure)**

#### **Strategic areas**

Mexico, Brazil, Costa Rica, Panama and Colombia, key strategic areas according to PWC

- Mexico: it has the most favourable investment environment and, despite certain risk factors (dependence on US economy, tight environmental restrictions, escalating land prices), it is perceived as an attractive country for foreign investment.
- Brazil: lots of rooms for development, particularly at the midscale level. Natal is a growing market though partly constrained by lack of direct commercial airlift.
- Costa Rica: the darling of Central America. Many investors/brands are waiting to see which of the planned projects come to fruition and whether the demand can match the increase in supply.
- Panama: Panama is being touted as the new Costa Rica. PWC's view is that it still has a long way to go (particularly in the resort markets). However, their phone is ringing more often about Panama.
- Colombia: gaining more interest. That said, political issues may have an impact on the ability to truly develop its tourism infrastructure and attractiveness to visitors from outside the country and region.

There are considerable opportunities in the midscale segment

PWC's thoughts are that, while most of the internationally funded or branded development has been in the upper upscale and luxury segments or in mature resort markets, there is significant opportunity for both development and acquisitions in the midscale sector in secondary and tertiary urban markets and in select major urban markets. This is supported, amongst other things, by a growing middle class and an increasing number of small businesses, which are generating inter-country and inter-territory travel.

#### **On investors**

Latin America's hotel sector has been traditionally dominated by local private investors. Groups like Poma in El Salvador, Irsa in Argentina and Genesis or Ecodesarrollos Papagayo in Costa Rica are well-known names in the area.

Latin America is seen as the next step by many investors and brands

Most international investors and brands are currently focused on the Middle East (Dubai) and Asia (China and India). However, they see Latin America as the next step. Some of them have been very active in the past couple of years in the region. The perception, though, is that there is a limited number of markets within most of the countries, with the exception of Mexico, Brazil and Costa Rica (as a distant third). Therefore, the development strategy tends to be regionally focused rather than country-focused.

#### **On risks**

PWC highlights the region's various risks

There are some country-specific risks that temper interest, such as repatriation of funds, lack of infrastructure, economic/political instability and regulatory complexity/inconsistencies.

About liquidity, many foreign investors are limiting their investment to flagship properties in established destinations because the expectation is that there will be a resale market for those assets within a reasonable holding period.

Other risks to consider are transparency, access to financing, government cooperation/oversight across the region (no one answer for all destinations), political/economic instability and, in select markets (particularly at the high-end segment), potential overbuilding.

### **Transaction activity**

Liquidity problems should improve as the region attracts more interest

#### **Liquidity and transparency issues**

An issue that has characterised the Latin American hotel market is the low level of transactions. Over the last few years, the increase in foreign investment has helped alleviate such liquidity issues, although the situation still persists. The future, however, looks brighter. Hotel operators, investors, consultants and bankers share the view that the market will progressively gain liquidity as the region becomes a focal point of interest.

Such low level of hotel transactions partly explains the lack of data available in the market. The information is not always disclosed, as transactions are often closed by private investors. This, however, should also improve as the number of institutional investors entering the region grows. Jones Lang LaSalle Hotels stated in its "Hotel Investment Outlook 2008" report that "As real estate transparency increases in Latin America, investors become more comfortable with the documentation associated with transfer of title".

HVS believes the hotel market in the region is still

HVS believes that the market is still immature. The hotel business is relatively new in South America and not many deals are closed. That said, it is interesting to see that in the last couple of years several investors have tried to enter the market but have failed due to the

immature

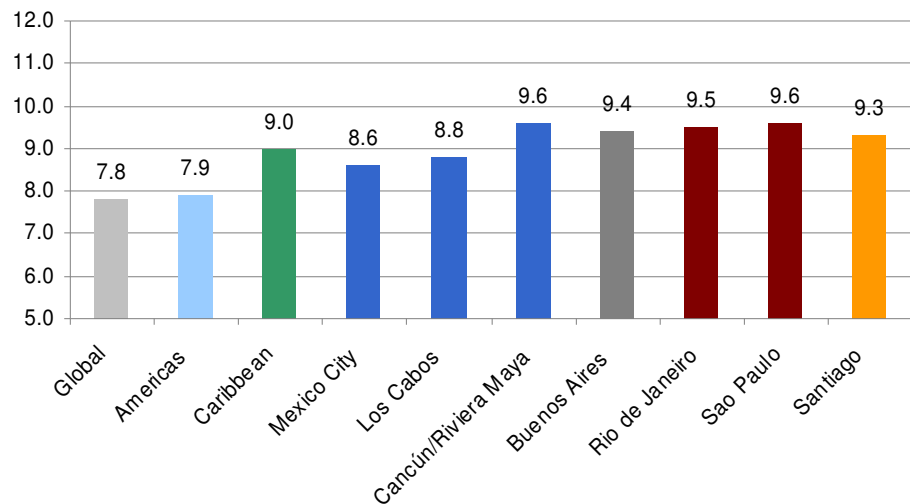
scarcity of product (with a few exceptions). Hotels are a new real estate market for the region and, more and more, developers, banks and investors are beginning to understand its growing importance.

### Cap rates

According to Jones Lang LaSalle Hotels, Latin America had an average initial yield of 9.2% vs. 7.8% globally

In December 2007, the non-weighted average initial yield for the Latin American markets covered by Jones Lang LaSalle's Hotel Investor Sentiment Survey was 9.2%. This compared with an average yield of 7.8% globally and 7.9% for the Americas. Cancun/Riviera Maya recorded the highest cap rate (at 9.6%), whilst Mexico City recorded the lowest at 8.6%. Amongst the four key cities in the Southern cone (Buenos Aires, Rio de Janeiro, Sao Paulo and Santiago), the Chilean capital showed the lowest figure with a 9.3% cap rate.

**Chart 5: Investment yield requirements - initial yield for new acquisition (in %) (December 2007)**



Source: Jones Lang LaSalle Hotels' HISS.

To this respect, JLLH said "Investors' target yields for markets in Latin America remain notably higher, to account for the additional tier of risk associated with investing in these markets. In Mexico/Caribbean and Latin American markets, yields and IRRs increased for the most part since the last survey (July 2007), except in Mexico city, where yields decreased by 120 basis points. In the long term, we expect to see these yields decrease in countries such as Brazil and Chile, with increased economic stability, increased transparency and more stable interest rates. In the Caribbean, target IRRs rose by 90 basis points since the last survey, and cap rates increased by 100 basis points to 9.0%. A number of Caribbean markets will witness increased investment in the long term. Investors reported increased target yields for Rio de Janeiro and Santiago, to 9.5% and 9.3%, respectively".

Below we summarise our findings on cap rates from our conversations with various industry sources.

**Table 11: Estimated hotel cap rates**

<b>Argentina:</b>	
Buenos Aires	9.0% - 11.5%
<b>Brazil:</b>	
Rio de Janeiro	8.5% - 10.5%
Sao Paulo	9.0% - 12.0%
<b>Chile:</b>	
Santiago	8.0% - 10.0%

Source: Meridia Capital estimates.

Cap rates in Buenos Aires are higher

### Argentina

We estimate that cap rates for hotel assets in Buenos Aires are in the 9.0 to 11.5% range, standing at a premium to those in other cities (like Santiago, for instance).

Cap rates in Rio de Janeiro are slightly lower than in Sao Paulo

### Brazil

Cap rates for resort hotels in Rio de Janeiro stand in the 8.5% to 10.5% range. The low end of the range would apply to some of the best neighbourhoods in the city. A deal is even said to have closed at a rate as low as 6%, although that would specifically apply to one of the city's trophy assets. Such low cap rates could be explained by existing high barriers to entry.

In Sao Paulo, yields would increase to the 9.0% to 11.5% or even 12.0% range. The average would be closer to the higher end of the range, mostly due to massive oversupply problems. In turn, such oversupply issues can explain why cap rates sometimes stand close to 9.0% and even 8.0%. The excess room inventory eventually depressed profits, which consequently lowered cap rates – yields ultimately relying on future cash flow upside.

The average in Chile would be close to 9%

### Chile

For Santiago we have narrowed our range to 8.0% to 10.0%, with an average of 9.0% sounding reasonable. The lower end of the range would only apply to the city's landmark properties.

### Prices per room

Despite the lack of transparency, we believe it is important to provide a broad indication of values per room. In Latin America, prices on a per room basis are below the levels seen in the US and especially in Europe – something that would be only partly explained by the lower profit levels that these same assets can generate.

To our knowledge, some of the most important recent hotel transactions that have taken place in South America are:

- In 2004, the 310 room Grand Hyatt in Santiago was sold as part of a portfolio transaction that also included the Four Seasons hotels in Argentina and Uruguay. The Grand Hyatt was said to have been sold for around US\$60 million (US\$194,000/room).
- The Four Seasons Hotel in Buenos Aires was sold for around US\$40 million (US\$242,000/room).
- Four Seasons Carmelo (Uruguay) was sold for around US\$20 million (US\$454,000/room).
- The San Cristobal Sheraton in Santiago was sold at the beginning of 2006 for an estimated value of US\$54 million (US\$104,000 per room).
- The Ritz-Carlton and Crowne Plaza hotels in Santiago were sold in August 2007 for a combined price of €63 million (€126,500/room).

### Financing

International financial institutions are increasingly interested in certain Latin American markets

According to Barbara Pereira, Managing Director for EMEA Debt & Equity Finance at CB Richard Ellis, Latin American real estate finance has ebbed and flowed primarily in parallel with the changing political risk environments of the individual countries within the region throughout the past 20 years. During 2007, international financial institutions began once again targeting specific countries as solid credit risk opportunities. They are dedicating balance sheet allocations for commercial mortgage finance. Certainly, the credit risk for Latin America depends much on the local government leadership and local currency inflation rates in relation to the US\$. In this regard, Mexico, Chile, Argentina and now Brazil, Costa Rica and Panama have attracted interest from lenders outside of the region.

Several factors determine hotel financing

Hotel financing from an international financial institution for Latin American properties depends greatly on several factors in addition to the general political risk of each country and municipality, namely:

- Quality of the borrower's (sponsor) experience, knowledge and relationship to the local market
- Internationally recognised flag or operator
- Solid economics and well proven demand generators for the existing and proposed supply
- Depth of the borrower's financial capabilities to withstand

political change impact on market economics

From a financing point of view, Brazil is currently a more difficult market than Chile or Mexico

Debt financing for hotel projects is easier to obtain in some countries than other. Renewed financial institution interest in hotels is occurring in Brazil, Chile and Mexico. Brazil presents higher difficulties. That said, the country is beginning to attract attention from European countries and Spain in particular, where a number of investors are involved in real estate and hotel investments. As a consequence, Spanish financial institutions are beginning to follow their client base to not only Chile and Mexico, but also to Brazil, the lower Caribbean islands, Costa Rica and Panama.

While Mexico has attracted US and Canadian banks as well as insurance companies at different times throughout the past 20 years, it is also currently experiencing a consistent interest from Spanish lenders. Generally speaking, Chile and Mexico are having a better go of it lately. This is true because of (i) lenders view the political risk of these countries to be less intrusive and (ii) Chile and Mexico, because of this, have been attracting more international financial institutions for a longer time (institutions are comfortable with the real estate markets as well as with the political climates).

The variation between markets really depends upon local factors and, more specifically, on the borrower, the political climate at local levels and tourism-driven property market economics.

HVS gave us an indication of what, generally speaking, investors can expect in terms of hotel financing conditions in three different South American markets:

- Argentina: maximum LTVs of 40-50%; maturity 7-10 years; financing costs at 10-14%, although likely to come down
- Chile: maximum LTVs of around 70%; maturity 20 years; financing costs at 6-7%
- Peru: maximum LTVs of 50-60%; maturity 15 years; financing costs at 7-9%

Chile, Peru and Colombia would be at the top of HVS' list, whilst Brazil would be at the bottom

In terms of accessibility to external financing for hotel projects, HVS believes that Chile would be at the top of the list, followed by Peru and then Colombia. Brazil would stand at the bottom of such list although, as it is the case with Argentina, the market is expected to open gradually. Spanish banks are said to be trying to provide incentives to important clients to stimulate business in the region.

Ernst & Young believes that it is uncommon to find easy financing for hotel projects in Latin America. They argue that this is mostly because of shortage of demand rather than a poor offer. Hotel investments in

the region have been traditionally financed by a pool of private investors rather than with external resources. The region never had a developed financial system adapted to this type of investments. Although there are isolated cases like Colombia, where the market is now evolving towards financing hotel project via bond issues in the capital markets, investors are still rather used to carrying out projects with their own equity.

E&Y argues that LTVs offered by banks in the region do not generally exceed 60% on average. That said, they claim to have participated in deals where LTVs were as high as 80% (with a repayment period of 10 years and with a 12% rate in local currency).

E&Y views, once again, Chile and Mexico as the most developed markets for financing, with Brazil at the other end

It is difficult to generalise and talk about financing conditions for the region as a whole, as the different countries have different dynamics. In Chile, for instance, things are easier in this regard thanks to the country's more developed and sophisticated capital markets. Mexico would be a similar case, favoured by the existing link between its economy and that of the US. On the other end there is Brazil, a market with numerous opportunities but where, according to E&Y, foreign investors will find bigger hurdles to financing than locals.

Ernst & Young's view is that, even though Latin America's capital markets are still underdeveloped compared with other more sophisticated markets, Mexico, Brazil and Chile are showing significant progress.

PWC also provided us with their view on financing conditions in the region:

- Mexico: LTVs of 50% to 75%; 7 to 10-year terms; 150 to 250bp over US rate, although the gap is shrinking (particularly for trophy assets)
- Brazil: maximum LTVs of around 50%; 12% to 15% variable rate
- Chile - maximum LTV of 80%; debt can be sourced locally at competitive rates, similar to US; Chile holds up to its reputation as a solid hotel market with locally available financing
- Costa Rica: LTVs of 50% to 70%; 7.5% to 9% rates

According to PWC, foreign financing entities will typically stick to

We asked PWC about the main issues to consider when trying to finance hotel projects in Latin America. They believe that what borrowers need first is a reliable local partner with equity, political connections and a solid reputation in the market. Availability of funds can be an issue in most countries, with Mexico and Chile being the only notable exceptions. Also, if financing is locally available, it tends

properties affiliated with major hotel companies in established destinations

to be more expensive and limited to smaller projects (US\$20-30 million). Foreign debt is available for projects in certain countries, particularly Mexico, Dominican Republic, Costa Rica and Panama. However, foreign entities there typically stick to flagship properties affiliated with major hotel companies in established destinations. The advent of mixed-use resort development with a focus on resort-residential has eased some of the financing requirements of hotel projects – although these also tend to be flagship developments.

### Final thoughts

Latin America is seen as a region offering great potential

Although Latin America does not come risk-free, it offers great potential for hotel investment. The region lies behind other areas in terms of hotel operating performance, with much room to grow. Expansion should be fuelled by an increasing number of international tourist arrivals, coupled with rising interest from the international investment community.

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