The tourism sector has been experiencing strong growth, as evidenced by the excellent performance of hotel units and by the record levels seen year upon year since 2010, in all major tourism indicators. Several factors explain the recent performance of this industry:

• The strategy implemented on the part of national tourism organizations which has shifted to the structuring and marketing of products and tourist destinations adapted to the demands of the market;

• International and national economic growth;

• The increase in flight connections from feeder markets, in addition to the opening of new routes and markets;

• Security fears in the north of Africa, which contributed to channeling the demand to more established destinations.

In this context, the tourism sector has witnessed an exceptional performance, with the last three years recording consecutive double-digit revenue growth. This performance has sparked the interest of international investors in tourism-related real estate, finding in these assets investment options at attractive returns. The cities of Lisbon and Porto, and the region of the Algarve, are today appealing destinations for international capital which recognizes the value upside of these locations.

In response to growing interest from property investors, Cushman & Wakefield has prepared this study on the Portuguese hotel market, which seeks to systemise key information to support the decision-making process. The main objective of this Business Briefing is to combine occupational data on the sector, with information on the operational performance of hotels and the dynamics of investment in hotels as property assets.

Eric van Leuven
Head of Portugal

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1. DEMAND

MACRO INDICATORS

The demand for hotels initiated, in 2010, the upwards trend which has remained until today. Security concerns in the main destinations of the Middle East and the north of Africa were important drivers for growth, which was then consolidated thanks to the higher quality of the supply and also the economic recovery, which has driven domestic demand. The increase in overnight stays from January to September in the country displays growth of 7.3% when compared to 2016, with our estimates pointing to 57.4 million overnight stays by the year-end.

OVERNIGHT STAYS - PORTUGAL

The number of guests has grown sharply throughout the past decade, with an increase of 54% in the last 10 years, compared to 42% recorded in overnight stays. This growth reflects a slight correction in the average stay, which decreased from 3 days to 2.85 between 2006 and 2017 and is explained by a sharper increase in demand for the city break destinations of Lisbon and Porto, as opposed to beach destinations, such as the Algarve and Madeira.

GUESTS EVOLUTION

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Occupancy rates increased in line with other indicators, registering a sharp increase at a national level, rising from 57% in 2006 to the 70% recorded today. The Autonomous Region of Madeira and the Metropolitan Area of Lisbon are the areas which performed best in terms of occupancy, with rates of 81% and 78% respectively.

DEMAND PROFILE

In the past 10 years the tourism sector has undergone several strategic changes which have positioned Portugal as a more diversified destination. Over the past decade, the main drivers of demand for sun, sea and sand destinations have extended to a range of specialised products in several sectors, such as culture, nature, leisure and gastronomy.

The cities of Lisbon and Porto (leisure and culture destinations), as well as the Azores (nature destination), have played a crucial role in this diversification process, and are the regions which recorded the largest growth in demand.

MARKET SHARE EVOLUTION - 2006/2017*

- North region almost duplicated overnights in the last decade
- Decrease in Algarve market share
- Increase in Greater Lisbon and North region market share
- Decrease in the Autonomous Region of Madeira

The change of the tourism profile in Portugal is displayed in the evolution of demand indicators. Although the growth in the tourist market has been felt in the country as a whole, there are significant differences between regions.

The most established destinations, such as the Algarve and Madeira, have lost some market share when compared to the northern region or the Metropolitan Area of Lisbon. The Algarve remains the main national tourist destination, having captured 16.1 million overnight stays between January and September of this year, but the hotels in the Lisbon region received the highest number of tourists, in the order of 4.74 million.

Among the most significant factors in the growth of the market in the past decade are the increase in the proportion of foreign tourists and a greater variety of emission markets. In 2006, the proportion of foreign tourists in Portugal was 53%, increasing to 62% in 2017, an absolute increase of 4.8 million foreign tourists over the past decade, or around 75% increase.

Throughout the last decade, France has recorded the largest absolute growth in the number of tourists, followed by the United Kingdom, Germany and Brazil. The increasing share of guests originating from minority markets, particularly Poland and Switzerland, is also noticeable, and an advantage to the sector in terms of risk diversification.
The growth in tourism demand has had a direct impact on the performance of hotel units, whose main operating indicators have all showed improvements. The occupancy rate increased 6 percentage points in the past decade, settling at 63% in 2016.

**OCCUPANCY RATE PER REGION**

![Bar chart showing occupancy rates per region for 2007 and 2017.]

- **80%** Madeira is the leader in terms of occupancy.
- **76%** Lisbon falls to 2nd place in terms of occupancy.
- **+14%** Azores is the 2nd region with the largest growth in occupancy.

Even so, the growth of the hotel sector in Portugal in the past decade has been extraordinary and reflects the enormous potential of the country as a tourist destination.

Source: INE | * January to September
2. SUPPLY

DISTRIBUTION OF HOTEL SUPPLY - PORTUGAL

The supply is mostly composed of hotel units, which account for 77% of the total accommodation units. Short stay accommodation, not accounted for in these data, has become an important alternative for tourists, essentially competing with hotels and touristic apartments. Resorts remain relatively insignificant on a national level, though their presence in the regions of the Algarve and the centre (west region) is more relevant.

Hotel supply in Portugal, today estimated at 1,500 units, is concentrated mainly in 4-star units, representing 34% of supply, followed by 3-star units which account for 30% of total projects. 5-star hotels still have a relatively modest share, of only 10% and around 150 projects.

With regard to future supply in Portugal, the market trend is for specialisation and qualification, both in terms of the product and service. The category of the projects opened in recent years reflects this trend; of the 170 hotel units opened since 2014, the 4-star category is dominant, corresponding to around 90 openings.

Portugal currently has around 2,200 hotel establishments and similar*, which offer more than 135,000 lodging units**. The majority of the hotel supply in Portugal is concentrated in the regions of the Algarve and Madeira and the urban centres of Lisbon and Porto. More recently, the archipelago of the Azores has begun to position itself as a tourist destination with enormous potential, currently representing a larger proportion of supply than in the past. The region of Douro, in the north of the country, also provides considerable supply and growth potential.

Future supply is estimated at over 120 projects due to open in the next 3 to 5 years. The majority of these are hotel units and situated in the Metropolitan Area of Lisbon (around 50 projects), as well as in the northern region, where over 30 new tourism developments are planned.

* Cushman & Wakefield property database
** Accommodation units: Bedrooms, apartments and houses
The hotel industry is characterised by highly fragmented ownership and a reduced presence of international operators.

The 20 largest operators in the market account for only 15% of hotel units, although the number of rooms is more significant, representing 37% of the total.

With regard to the level of internationalisation of the sector, among the 10 largest operators present in the market, only 4 are international brands.

**MAIN HOTEL OPERATORS IN PORTUGAL**

**Grupo Pestana**

- Dom Pedro Hotels
- Turim Hotéis
- Accor Hotels
- Hoti Hotéis/Meliá Hotels & Resorts
- Discovery Hospitality Real Estate
- Eurostars Hotels
- Marriott & Starwood Hotels
- Tivoli Hotels & Resorts
- Dolce Hotels & Resorts

The Pestana Group is the largest hotel operator in Portugal, with approximately 70 units and more than 5,000 rooms. Accor Hotels is the second most represented operator in the country and the largest international brand, with a network of 32 units and over 3,300 rooms.

The Vila Galé Group follows in terms of size, with 21 hotels and over 3,000 rooms.

Among the international operators present in Portugal, in addition to the aforementioned Accor, Melia hotels (in partnership with the local Hoti Hotels), Marriott & Starwood and the Intercontinental Hotel Group are of particular note.
3. HOTEL OPERATIONS

The hotel industry in Portugal was severely affected by the economic crisis. Overnight stays recorded sharp falls from 2008, only recovering to pre-crisis volumes in 2013. With regard to revenues, the downward trajectory began in 2009 and was only fully recovered in 2014. Several factors contributed to the recovery of the sector, notably international and national economic growth, but the substantial reorganisation of the hotel industry was also key, characterised by mergers and acquisitions, resulting in optimised hotel accounts.

From 2014, hotel income confirmed the reversal of the cycle, with successive annual double-digit growth in total revenues recorded since that year.

The breakdown of revenue in the hotel sector reflects the highly positive effect of the increase in average daily rates.

Throughout the past decade, accommodation revenue has grown from a 66% share of total income, to 72%. Income resulting from F&B and other represented only 28% of the total.

The average daily rate in Portugal has increased 40% in the past decade, with the Algarve region recording the sharpest growth, over 60%.

The Metropolitan Area of Lisbon stands out in terms of average daily rate, when compared to the rest of the country, at €56. The northern region has the second highest average price today, €44, followed by the Algarve, with €42.

4. SHORT STAY ACCOMMODATION

The short stay accommodation market began its early growth in Portugal from 2010 onwards but more significantly from 2013, when supply in the city of Lisbon had reached 2,000 units, and in Porto 500. Currently, Airbnb records active supply in Lisbon of around 14,000 units and 6,000 in Porto.

Short stay accommodation is seen by tourists as alternative to traditional lodging, and as such competing with hotels. However, conventional hotels seek to differentiate themselves through the provision of services, adding value to the experience of tourists, with short stay accommodation therefore being a complementary offer.

This type of accommodation has, over the past 7 years, proved to be attractive, considering the retention rate of property (the share of currently active units when compared to the total units available in the market since the start of the data analysis in 2010), which in Lisbon and Porto is the highest among comparable markets, both in terms of relative size and type of destination.

Although short stay accommodation is traditionally exploited by private individuals, the increasing professionalisation is notable. Currently, short stay accommodation portfolios represent over 70% of the total supply in Lisbon and Porto.

In Europe, and in comparison with similar tourist destinations, the city of Barcelona dominates supply. Lisbon finds itself in 5th place of the 8 cities reviewed, while Porto is the city with the lowest amount of short stay units.

The average prices reflect a reality comparable to that of the hotel market, with Portuguese cities practise the lowest prices within the sample.

Source: INE | *January to September

Source: Airdna | * Airbnb
5. LISBON

The Metropolitan Area of Lisbon is the largest tourist destination in Portugal, in terms of visitors, with over 4.7 million guests between January and September of 2017 - 10% more than in the same period of 2016.

Lisbon International Airport is the main point of arrival for foreign tourists, with 12.1 million passengers in the first half of the year, 22% more than in 2016. Arrivals by cruise liners at the Port of Lisbon still hold a relatively small share of total arrivals of foreign tourists to the capital, but have growth potential. Between January and September of 2017, the city received 225 cruise liners, carrying 365,000 passengers. The recently opened new cruise terminal at Santa Apolónia, uniquely close to the in the centre of the city, will bring increased capacity to Lisbon.

Tourism in the Metropolitan Area of Lisbon is distributed between the cities of Lisbon, Cascais and Sintra, in addition to the beach areas to the north and south of the city. The city of Lisbon is an important and award-winning business and city break destination and also a starting point for tourists who visit other regions of the country.

Greater Lisbon currently has 360 hotel establishments, offering around 31,500 accommodation units*. Future projects due to open in the next 3 to 5 years total around 50 units, the vast majority of which in the city of Lisbon.

The current hotel supply is also concentrated in the city, with 61% of units and 66% of rooms.

Hotels are located mainly in the historic centre, with a significant cluster also in Parque das Nações, and more recently along the river front.

Hotel supply in Lisbon is generally of a higher category than the rest of the country, with 5-star hotels accounting for 15% of all projects and a larger share than the national average of 4-star hotels too.

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There are known intentions for around 40 projects for the city of Lisbon, adding circa 3,500 accommodation units. The majority of the projects are located in the city centre and are in the 4 and 5-star categories.

Although the sustainability of the growth rate in recent years is sometimes questioned, the growth of demand is actually 3 times higher than that of supply: while the forecast for new openings in the city of Lisbon over the next 3 years implies an increase in capacity of the order of 3%, overnight stays in the capital over have grown at an average annual rate of 11% in recent years.

The city of Lisbon has a far higher concentration of operators than the rest of the country. The 10 largest operators in the city account for 26% of hotel unit and 44% of rooms, with Portuguese operators in the majority.

The Sana Group has the largest number of hotels and rooms in operation in Lisbon, followed by the VIP group and, in third place, Accor Hotels.

* Source: Cushman & Wakefield property database
Hotel units in the city of Lisbon captured 84% of all overnight stays in the Metropolitan Area of Lisbon in 2016, and 79% of hotel revenue, confirming the city’s dominant status in the hotel industry in the region. Lisbon also presents highly favourable key performance indicators, far superior to those seen in the rest of the country, with an occupancy rate in the order of 82% in September and an average daily rate of more than €100, almost double the amount in the Metropolitan Area of Lisbon in the same period.

**MAIN HOTEL OPERATORS - LISBON**

- Olissippo Hotels
- Turim Hotéis
- Accor Hotels
- Sana Hotels
- Grupo Alfa Hotels
- Vip Hotels
- Marriott & Starwood Hotels
- Intercontinental Hotels Group - IHG
- Hoti Hotéis/Meliá Hotels & Resorts
- HF Hotéis Fénix

**HOTELS OPERATIONS - LISBON**

- **€692 milhões** Hotel income 2016
- **+16%** Increase in income 2016
- **€11 milhões** Overnight stays 2016
- **+11%** Increase in overnight stays - 2016
- **82%** Occupancy rate 2017*
- **€102** Average daily rate in 2017*

Porto has also recorded substantial growth in tourism in the past years, and is today one of Europe’s favourite city break destinations. Both the historic centre of the city and the nearby Alto Douro Wine Region have been awarded Unesco World Heritage status and this explains in part the success of the city as a tourist destination, but it was the increase in international flight connections to the Francisco Sá Carneiro International Airport which was the main driver for growth.

In the first half of 2017 the airport received over 5 million passengers, representing growth of 18% when compared to 2016.

The cruise liner market is still at an early stage, but the opening of the new, striking terminal in the Port of Leixões in 2015 should trigger growth in this industry, which between January and September welcomed 83,000 passengers and 83 cruise liners.

The Metropolitan Area of Porto today has more than 170 hotel establishments, offering around 12,000 accommodation units*. Future projects due to open in the next 3 years exceed 30 units, the vast majority of which in the city of Porto.

**6. PORTO**

- **5 milhões** Porto Airport Passengers 1st Half 2017
- **18,5%** Increase in 2017 (y.o.y)
- **83.000** Cruise passengers from January to September 2017

* Source: Cushman & Wakefield property database

* January to September
The city of Porto holds a very significant share of the total hotel supply in its metropolitan area, accounting for 52% of units and 56% of rooms. The hotels are largely concentrated in the historic centre, with a significant cluster also located in the Boavista area (essentially focused on business tourism). With regard to the category of hotels, the city shows a larger proportion of units of 3-stars and less, by contrast to the breakdown at national level, where 4 and 5-star categories are more prevalent.

The increasing draw of the city for international tourists is attracting investment in new hotel units, with 18 new projects currently planned for the city, representing over 1,200 rooms. Almost all of the new hotels planned for Porto in the next 3 years are of 4 and 5-star categories.

**HOTEL SUPPLY - PORTO CITY**

![Map of Porto showing hotel supply](Image)

- **+90** Establishments
- **+6,200** Rooms
- **19** 4* Hotels
- **31** 3* Hotels
- **7** 5* Hotels

This growth represents an average annual increase in the order of 3%, a far lower rate than that of demand, where the average annual growth between 2014 and 2016 has been close to 15%.

The city of Porto has a higher concentration of operators than Lisbon, with the 10 largest hotel groups accounting for 31% of all units and 57% of all rooms on offer. In contrast to Lisbon, international chains operate the majority of supply, providing 60% of rooms.

The Fénix Hotels have the largest supply of rooms in the city, followed by the Marriott & Starwood Hotels and, in third place, the Hoti Hotels/Meliá.

**MAIN HOTEL OPERATORS - PORTO**

- **HF Hotéis Fénix**
- **Eurostars Hotels**
- **Hoti Hotéis/Meliá Hotels & Resorts**

**HOTELS OPERATIONS - PORTO**

The city of Porto dominates the tourist market of the wider northern region: in 2016, hotel units in the city captured 49% of overnight stays and 61% of hotel revenues. The city presents very satisfactory key performance indicators and its growth reveals the potential of the sector. In 2016, the increase in overnight stays was in the order of 15%, 4 percentage points higher than Lisbon, while revenues grew more than 25% in just one year, 9 points more than the capital.
7. INVESTMENT

The tourism sector has gained prominence in property investment activity at a global level. International investors have a growing appetite for this type of assets, thanks not only to attractive rates of return, but also to a trend for diversification in terms of portfolio asset allocation as well as country risk.

According to Real Capital Analytics (RCA), investment in the hotel sector in core world markets has increased its share of total transactions from a mere 4% in 2008, to 12% in 2016.

Assets in the United Kingdom, Germany and France have the preferences of investors in the sector, having attracted over €80 billion of investment, more than half the volume invested in the whole of Europe.

RCA calculate investment in hotel assets in Europe over the past decade to be €135 billion, showing a growing trend between 2008 and 2014 and a fall from 2015, albeit still with significantly higher volumes than the average for the decade.
Local investors hold a significant share of total investment, 47%, although foreign investment has maintained a larger share. European investors in Portuguese hotels have been a minority in the past decade, representing only 10% of volume, with Thai capital accounting for a very significant share (total around 380 million), corresponding entirely to the purchase of the Tivoli portfolio by Minor International.

With regard to the profitability of this asset class, the analysis of MSCI in its property market index, IPD, displays higher average annualised returns than other segments of the markets. In 2016, the annualised return of hotels in the pan-European IPD portfolio reached 9.1%, while the core property sectors recorded 5.7% in retail, 7.2% in offices and 9.1% in industrial. Annualised returns over 5 years were 7.5% for hotels, 7% for retail, 7% for offices and 9.6% for industrial.

In Portugal, lack of scale of hotels in the portfolios does not allow for the release of returns on the part of IPD, however, with regard to yields on acquisition, since 2014, these averaged 6.4%, varying between 5% and 7.5%.

In terms of price per room, growth has been witnessed in the past 3 years. Transactions of distressed assets, or assets in the recovery phase, between 2014 and 2016, recorded amounts in the order of €130,000 per room. More recent sale and leaseback transactions of urban hotels, saw a significant price increase, to ca. €165,000 per room. Assets in premium locations would today command a price per room of more than €250,000.

The trend will be for hospitality assets, particularly urban hotels in Lisbon and Porto, to become a more established asset class and to command a greater proportion of investors' allocations. Yields should contract further as more professional operators with the capacity to achieve operational efficiencies enter the market.
8. TRENDS

PRODUCT QUALIFICATION
Future supply will concentrate on units of the upper categories.

OPERATOR CONSOLIDATION
The current multitude of operators in the market will decrease substantially through the growth of dominant brands, by acquisition and organic growth.

CONSOLIDATION OF DOMINANT DESTINATIONS
Algarve, Lisbon, Porto and Madeira

GROWTH OF ALTERNATIVE PRODUCTS
Nature - the Azores and Algarve hinterland
Surf - Coastal areas west of Lisbon, and along the Alentejo towards the Algarve
New sun, sea and sand destinations – Troia, Alentejo coast
New cultural destinations – Évora, Coimbra, Aveiro, Guimarães, Braga

MANAGEMENT PROFESSIONALISATION
Operational hotel management will increasingly be undertaken by specialist companies.

SEPARATION OF PROPERTY AND MANAGEMENT (“BRICKS & BRAINS”)
Institutional property investors will play an ever-increasing role in the ownership of hospitality assets.

PERSONALISED SERVICE
Service will increasingly focus on the individual needs and wishes of customers.