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ISRAEL HOTEL MARKET OVERVIEW 2020 THE PATH TO RECOVERY?

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Key Takeaways

- **Tourism arrivals to Israel hit another record in 2019**, growing to 4.5 million (see Figure 1) and resulting in improved hotel performance throughout
- **Hotel values across Israel gained a further 5.2% in 2019** on the back of similar average RevPAR growth for all markets
- **We expect a gradual but accelerating recovery following COVID-19** – RevPAR projected to return to 2019 levels by 2024
- **Supply growth slows** – projects will be delayed or abandoned altogether
- **Hotel values to decline in 2020** – to remain depressed until EBITDAs ‘hit the bottom’ and there is evidence of recovery
- **Longer term, values will recover** as cash flows improve and capital markets return to more traditional parameters
- **Opportunity for high returns** – well-capitalised buyers could take the opportunity to buy distressed assets well below replacement cost and recent norms

Foreword

The restrictions imposed due to the COVID-19 pandemic have severely hit every sector across the globe, and the hospitality industry is undeniably among the hardest hit. In Israel, strict lockdown measures were implemented in mid-March, forcing all except non-essential businesses to close, including most of the country’s hotels.

Fortunately, there is light at the end of the tunnel for the lockdown phase and, on 4 May 2020, Prime Minister Netanyahu outlined a gradual easing of lockdown restrictions; the focus of hoteliers has thus shifted from how to manage the closure to developing a sound reopening strategy. While this was a positive sign for hoteliers, it is important to make a distinction between when hotels will be allowed to reopen and when they should reopen. As with the rest of Europe, we expect hotels to reopen gradually in Israel and that they will likely need to continue making use of the government’s unemployment benefits until demand returns in sufficient quantities, especially from international visitors, to justify a more profitable operation than the cost of remaining closed.

No-one knows the timeline as to how long this pandemic will last or the final net impact on the economy. What we do know is that the hospitality industry is extraordinarily resilient. Past ‘shock’ events and downturns have caused business to plummet; however, the industry performance has always recovered and Israeli hotels have become especially adept at managing the impact of such events. Even though the pace and degree of the COVID-19 downturn are unparalleled, we are of the opinion that the hospitality industry in Israel will recover and, as in the past, this downturn will create the opportunity for strong returns through well-timed and well-executed investment strategies.

In this report, we examine a set of recovery scenarios addressing the range of potential impacts on hotel values in Israel. We analyse the past hotel performance to determine the baseline for this and we review the tourism market profile to understand the factors affecting the anticipated short- and mid-term return of travel.

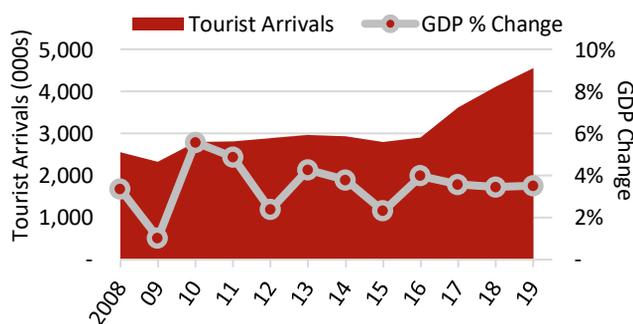
The Context in Recent Years

A Thriving Economy

The Israeli economy has flourished over the last decade and has recorded one of the best performances across all OECD countries. Since 2008, GDP growth has averaged 4.0% a year, which compares to the OECD average of 2.9%. Israel's economy is characterised by its strong service and industrial sectors, which mainly focus on high-tech products, biomedical equipment, chemicals, and military technology. The country is also referred to as the 'Start-up Nation' owing to its incredible number of start-ups, rumoured to be the highest per capita in the world.

Undeniably, the travel and tourism industry has also played an important role, being one of the largest economic sectors in Israel. It contributed US\$22 billion (5.6%) to GDP in 2019 and provided close to 230,000 jobs (5.7% of total employment), according to the WTTC.

FIGURE 1: TOURIST ARRIVALS AND GDP CHANGE
Israel



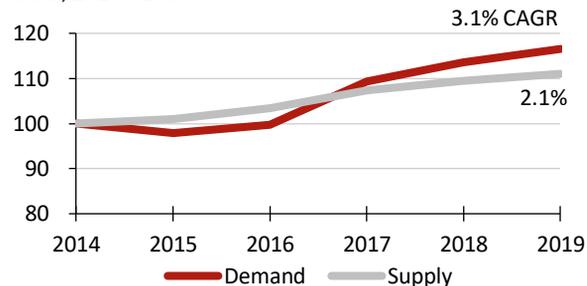
Source: Central Bureau of Statistics

Tourism Acceleration

The political situation in the region has had a crucial impact on inbound and outbound tourism flows. Following years of geopolitical tension in Israel and the neighbouring states, 2017 marked the turning point and was among the best years in the country's history in terms of international visitation. Combined with targeted marketing actions, easing of regulations for visas and an increased number of air routes thanks to the Open Skies agreement

which came into effect in 2013, the Israel tourism industry showed impressive growth from 2.9 million tourist arrivals in 2016 to 4.5 million in 2019 (see Figure 1). Local hoteliers benefitted from this inflow, as reflected in the solid performance of all markets under review (see Figure 3).

FIGURE 2: SUPPLY AND DEMAND GROWTH IN ISRAEL
Index, 2014 = 100



Source: Central Bureau of Statistics

Supply is Lagging Behind

As shown in Figure 2, demand growth has outpaced supply growth over the last three years, highlighting the strong potential of the destination to welcome new hotels, especially at the budget end of the spectrum. To accelerate the construction of new hotels, the Ministry of Tourism launched a number of initiatives in 2016. One of the main pillars was the creation of a governmental grant scheme in order to provide additional support to developers in a country where banks are generally hesitant to lend for hotel purposes. Another important initiative was the implementation of a centralised planning process and other regulatory improvements. Before this was introduced, investors had to deal with a number of different planning committees in order to obtain a permit, thus making the entire process extremely lengthy (sometimes between five and ten years). This process has now been centralised and is handled by the National Infrastructure Committee, thus cutting bureaucracy. These initiatives have been proven to be effective; more than 22,000 rooms are expected to enter the market in the next couple of years, albeit that the realisation of this might be delayed owing to the current pandemic.

Hotel Market Performance

Mirroring the positive trends in demand and limited supply growth, Israel's hotels recorded a RevPAR increase from US\$137 in 2016 to US\$169 in 2019, representing a compound annual growth rate of 7%.

The strongest RevPAR growth was recorded in Jerusalem at a compound annual growth rate of 14% between 2016 and 2019. This was followed by Tel Aviv (8%), Haifa (6%), the Dead Sea (4%) and Eilat (3%).

FIGURE 3: OCCUPANCY AND AVERAGE RATE COMPARISON

	2016			2017			2018			2019			Sample Size Rooms
	Occupancy	Average RevPAR		Occupancy	Average RevPAR		Occupancy	Average RevPAR		Occupancy	Average RevPAR		
		Rate (US\$)	(US\$)										
Tel Aviv	70%	221	155	73%	236	172	75%	245	185	76%	256	194	6,027
Eilat	72%	208	150	76%	203	154	74%	217	160	76%	217	165	4,435
Jerusalem	55%	180	99	66%	174	115	70%	196	138	73%	203	149	3,913
Dead Sea	76%	189	143	79%	202	159	76%	208	158	77%	211	163	1,466
Haifa	64%	158	101	65%	168	109	66%	172	114	68%	175	119	833
Israel (Average)¹	67%	203	137	72%	208	150	74%	220	162	75%	225	169	16,674

¹ The average of the samples of hotels in the five destinations

Source: HVS Research

Like much of the world, Israel's hotel industry took a massive nosedive as travel came to a halt in mid-March 2020. Only a small number of

hotels remained in operation, and the occupancy levels for these opened hotels are generally in single digits.

The Path to Recovery?

Israel began reopening the country to domestic tourism with a phased approach on 4 May 2020. Simultaneously, the Tourism Recovery Task Force has been working alongside Ministry officials to outline a recovery strategy by implementing the appropriate health and safety measures to keep travellers safe, including the 'Purple Standard' protocol, a new Standard Operating Procedure for hotels operating in the country. Our report next year will clearly need to contain a deeper reflection of what actually transpires. As many countries in Europe reopened their borders in June, many of Israel's hoteliers had hoped to see their country taking a similar decision but, as the country is currently experiencing a second wave of the virus, this is likely to be delayed. However, Greece, Cyprus and Israel are considering setting up a 'corona corridor', allowing cross-border travel

between those countries in a common effort to partially revive international tourism; it is planned to take effect on 1 August, although the situation remains unclear.

In terms of fiscal policy, the Israeli government announced a NIS94 billion (US\$27 billion) economic stimulus package to support vulnerable sectors and some NIS300 million (US\$86 million) will be allocated to the tourism sector.

While regulations and stimulus packages will frame and assist recovery, they will represent just a fraction of the rebound equation. The characteristics of the market, from its demand sources to the destination's transport links or its supply dynamics, will play a significant role in the recovery of the hospitality industry once international travel resumes.

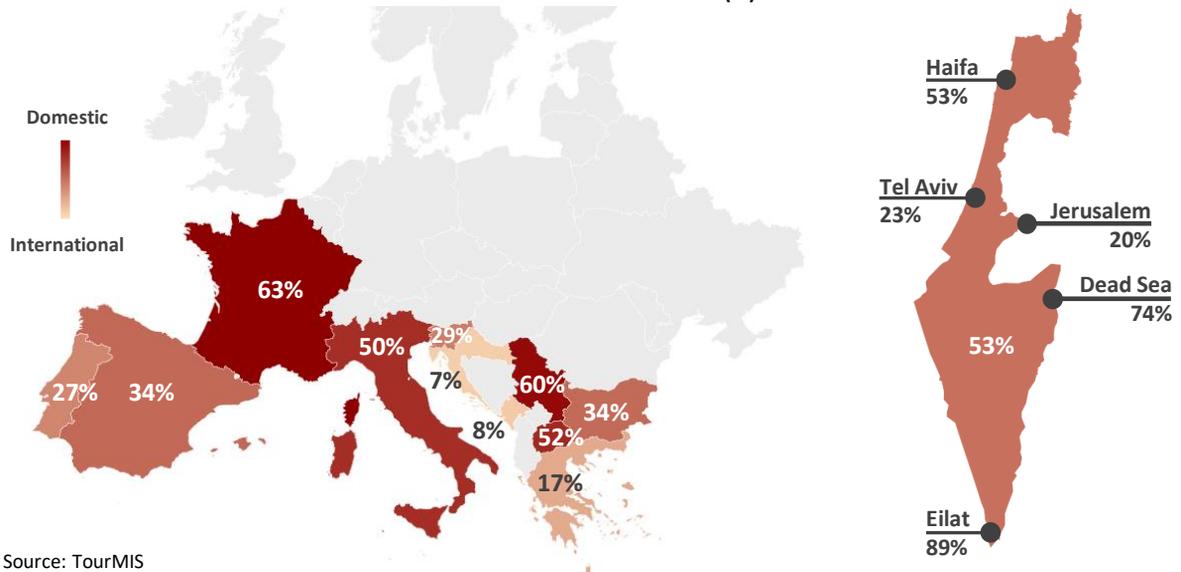
The Tourism Market is Going Local

Countries and markets with less reliance on international demand and air travel are likely to see a faster recovery than others. Figure 4 provides an overview of the proportion of room nights arising from domestic guests. In comparison to many southern Mediterranean countries, Israel should be in a relatively good position with more than 50% of overnight demand derived from domestic tourism. However, in markets such as Tel Aviv and Jerusalem, overseas tourists represent some 80% of total overnights, implying a greater

challenge than those relying primarily on domestic demand such as Eilat and the Dead Sea region.

It is also important to look at this from the other side of the equation and consider what happens when holidaymakers who typically travel overseas for their holiday instead book 'staycations'. In 2019, Israelis took more than 9 million trips abroad, and we are carefully monitoring this space and to what extent these holidaymakers will replace the international demand in the short term.

FIGURE 4: COMPARISON OF DOMESTIC SHARE OF TOURISM OVERNIGHTS (%)

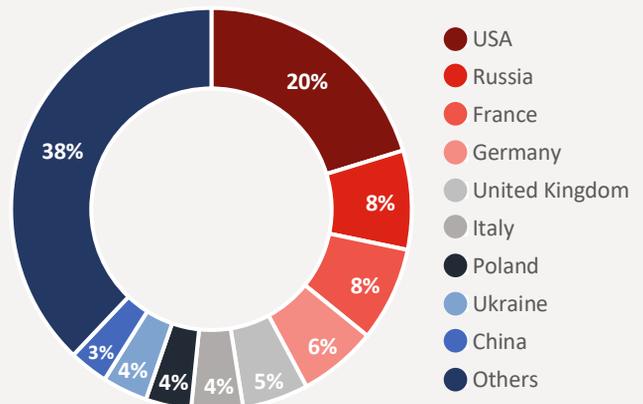


Assessing Israel's Traveller Profile

Hoteliers must drill down into the details of their region's source markets, demographics and segmentation to guide their strategy for recovery. As shown in Figure 5, the top feeder market visiting Israel in 2019 was the USA with more than 1.25 million visitors, followed by Russia, France, Germany and the UK. These five markets together accounted for 47% of total international visitation to the country in 2019 and the economic recovery and containment of the virus in those countries, as well as the rate at which international travel resumes, are crucial for Israel's tourism recovery.

FIGURE 5: KEY INTERNATIONAL SOURCE COUNTRIES

% of International Arrivals, 2019

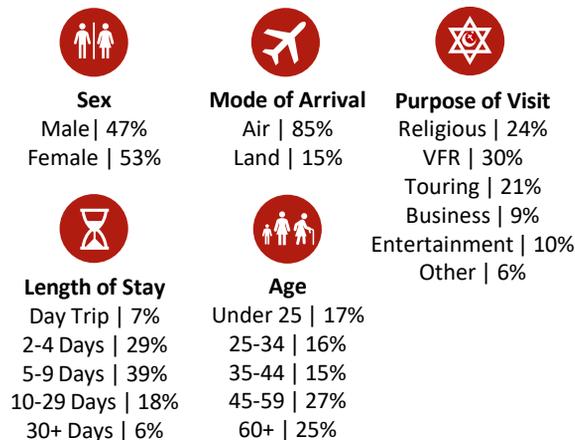


Source: Central Bureau of Statistics

Leisure Tourism to Recover First

As shown in Figure 6, the vast majority of Israel's visitors are leisure-related, and we expect those to return first – particularly those visiting friends and family – whilst long-haul travellers are likely to be slower to return. The country also has a high percentage of returning guests (some 50% of all international tourism to Israel), which we hope hoteliers recognise and take advantage of. People in the age group of 45 and under account for almost half of total visitation. Not surprisingly, recent trends from China show that the young and the non-family segment are resuming travel earlier, and we expect a similar trend in Israel. Business demand is likely to return unevenly and more slowly depending on company travel policies and type of sector. We expect MICE (meetings, incentives, conferences and events) and group business to be the slowest to return.

FIGURE 6: TRAVELLER PROFILE
ISRAEL, 2019



Source: Central Bureau of Statistics

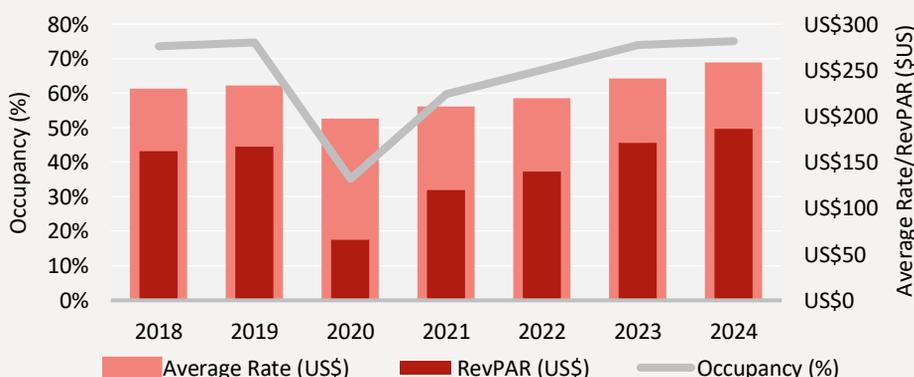
RevPAR Recovery Anticipated by 2024

Taking into consideration the factors mentioned in this report, along with the performance thus far in 2020, the forecast presented in Figure 7 reflects the current expectation for the timing and pattern of recovery.

HVS's RevPAR outlook for Israel envisages a 60% decrease in 2020 followed by a sharp increase, driven primarily by occupancy, in 2021. Occupancy is expected to recover by 2023, roughly 3½ years from now, followed by average rate a year later (in real terms). We note that the situation remains fluid; forecasts may change as time passes and as more light is shed on the rate of recovery.

We expect occupancy in economy and midscale hotels to be less vulnerable, especially those which primarily rely on transient segments. The more vulnerable hotels are likely to be luxury and upper-scale hotels and those most reliant on meetings, incentives, conferences and events (MICE). These general trends are consistent with what we have seen in previous downturns. Following 9/11 and the Global Financial Crisis, hotel RevPARs typically took some six years to be restored to their previous peak levels, and we consider it likely that this will be the case with regard to COVID-19, albeit that the pace of growth will be slower owing to certain markets taking longer to return.

FIGURE 7: PERFORMANCE OUTLOOK FOR ISRAEL'S HOTEL MARKET



Source: HVS Research

Hotel Development

At the start of 2020, the pipeline across the country had never been as strong, with more than 12,000 rooms (22% of existing supply) expected to open in the next few years. However, we expect the current situation to delay the construction and opening of some of the hotels, while some projects in the planning phase may be cancelled. Moreover, there may also be some hotels, currently closed, which might never reopen because of cash or capital

shortages and may need to be repurposed. We are carefully watching this space to determine which projects will be delayed or cancelled.

Figure 8 provides an overview of recently opened properties and new supply in Israel. The opening dates exclude possible delays caused by the current situation, and we expect more certainty around those projects over the next 12 months.

FIGURE 8: RECENTLY OPENED PROPERTIES AND NEW SUPPLY

Proposed Property	Hotel Group/Operator	Location	Number of Rooms	Opening Date ¹
Dave Levinsky	Brown Hotels	Tel Aviv	27	Opened
Theodor	Brown Hotels	Tel Aviv	34	Opened
WOM Allenby	Brown Hotels	Tel Aviv	40	Opened
Hotel Bobo	Brown Hotels	Tel Aviv	200	Opened
Deborah Brown	Brown Hotels	Tel Aviv	90	Q3 2020
Brown JLM	Brown Hotels	Jerusalem	46	Q3 2020
Selina Neve Tzedek	Selina	Tel Aviv	30	Q3 2020
Selina Kinneret	Selina	Migdal	78	Q3 2020
Abraham Hostel Eilat	Abraham Hostels	Eilat	100	Q3 2020
Isrotel Kedma	Isrotel	Sde Boker	162	Q3 2020
Nobu Tel Aviv	Nobu	Tel Aviv	38	Q3 2020
Six Senses Shahrut	Six Senses	Shahrut	59	Q4 2020
Kempinski David Hotel	Kempinski	Tel Aviv	250	Q4 2020
Isrotel North Yarkon	Isrotel	Tel Aviv	154	2021
InterContinental Jerusalem	IHG	Jerusalem	229	2021
NYX Jerusalem	Fattal Hotels	Jerusalem	168	2021
Lilinblum 15 hotel	Fattal Hotels	Tel Aviv	60	2021
The Kabbalah House	Fattal Hotels	Tel Aviv	90	2021
Prima Dizengoff Street	Prima Hotels	Tel Aviv	70	2021
Prima Allenby Street	Prima Hotels	Tel Aviv	106	2021
The Modani Luxury Spa Resort	Dan Hotels	Netanya	134	2022
Isrotel Jerusalem Boulevard	Isrotel	Tel Aviv	130	2022
Pullman Jerusalem	AccorHotels	Jerusalem	270	2022
Ben Sira Hotel	Fattal Hotels	Jerusalem	88	2022
Fattal Beit Alliance	Fattal Hotels	Jerusalem	90	2022
Alberto Hotel	Isrotel	Tel Aviv	93	2022
Isrotel 99 Dizengoff	Isrotel	Tel Aviv	130	2022
Isrotel Ein Bokek	Isrotel	Ein Bokek	47	2022
Astral Lite Hotel	Astral Hotels	Eilat	500	2022
Palatin Hotel (reopening)	Fattal Hotels	Tel Aviv	87	2022
Isrotel Zion Square	Isrotel	Jerusalem	250	2022
easyHotel ²	easyHotel	Tel Aviv	667	2022
Swell Beach Hotel Ashdod, Curio Collection	Hilton	Ashdod	84	2022
Hilton Garden Inn	Hilton	Ashdod	160	2022

¹ Provisional and subject to further announcements

² Three hotels in Tel Aviv

Source: HVS Research

FIGURE 8: NEW SUPPLY (CONTINUED)

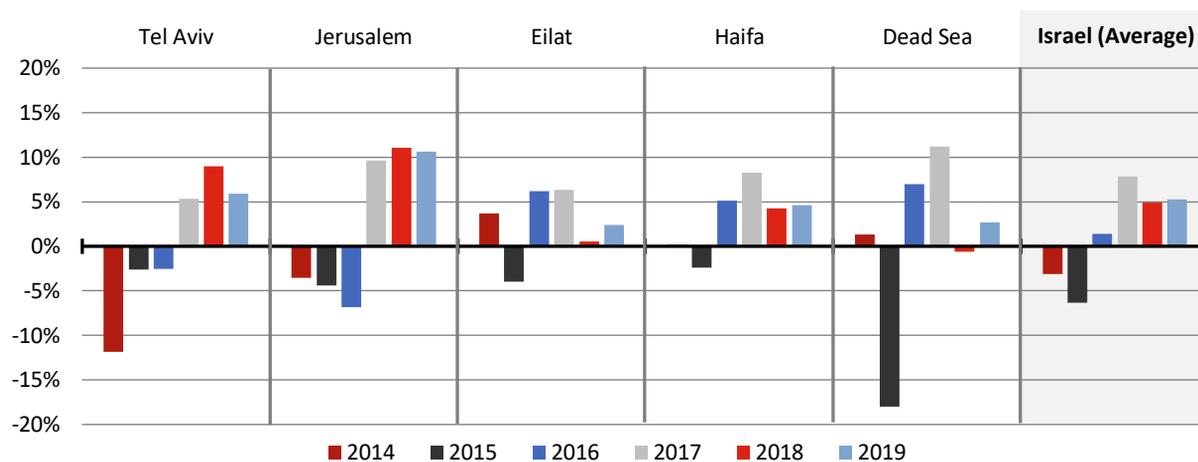
Proposed Property	Hotel Group/Operator	Location	Number of Rooms	Opening Date ¹
Isrotel Leon Towers	Isrotel	Tel Aviv	235	2023
Tzuba Spa Hotel	Fattal Hotels	Tzova	152	2023
Shmuel Hanagid House	Fattal Hotels	Jerusalem	72	2023
Swissôtel Sun Bat Yam	AccorHotels	Bat Yam	276	2023
Alkunin MGallery by Sofitel	AccorHotels	Tel Aviv	44	2023
Isrotel Eilat North Beach	Isrotel	Eilat	180	2023
Mandarin Oriental Tel Aviv	Mandarin Oriental	Tel Aviv	225	2023
Brown Hotel Ben Gurion Airport	Brown Hotels	Airport City	200	2024
Isrotel Basel Complex	Isrotel	Tel Aviv	132	2024
Brown 42° Eilat	Brown Hotels	Eilat	155	2024
MEININGER Tel Aviv	MEININGER	Tel Aviv	210	2024
Proposed Hotel Dead Sea 1	Fattal Hotels	Ein Bokek	198	2024
Proposed Hotel Dead Sea 2	Elad Hotels	Ein Bokek	253	TBC
Proposed Hotel Dead Sea 3	Elad Hotels	Ein Bokek	330	TBC
Proposed Hotel Dead Sea 4	Africa Israel Hotels	Ein Bokek	220	TBC
Proposed Luxury Hotel, Golf & Spa	TBC	Mount Arbel	150	TBC
Proposed Hotel Modi'in	TBC	Modi'in	50	TBC
Proposed Hotel Negev Desert 1	TBC	Yeruham	24	TBC
Proposed Hotel Negev Desert 2	TBC	Yeruham	24	TBC
The Nitzba – former Foreign Ministry	TBC	Jerusalem	360	TBC
Mishkenot HaTeatron	TBC	Jerusalem	76	TBC
The Braun Hotel	TBC	Jerusalem	46	TBC
The Bishop's House	TBC	Jerusalem	50	TBC
Sea Gate Hotel (Nitsba)	TBC	Netanya	70	TBC
The German Colony Hotel	TBC	Haifa	270	TBC
Princess Hotel (Nitsba)	TBC	Eilat	420	TBC
Proposed Upscale Hotel North Beach	Fattal Hotels	Eilat	182	TBC
The Setai Akko	The Setai	Acre	TBC	TBC
The Setai Glilot	The Setai	Tel Aviv	TBC	TBC
The Setai Tel Aviv Promenade	The Setai	Tel Aviv	TBC	TBC
Brown Salame Street	Brown Hotels	Tel Aviv	190	TBC
Sarona Hotel (Nitsba)	TBC	Tel Aviv	880	TBC
Isrotel Mugrabi Square	Isrotel	Tel Aviv	170	TBC
Proposed Luxury Hotel Jaffa Port	Africa Israel Hotels	Tel Aviv	69	TBC
Proposed Luxury Hotel Herbert Samuel Promenade	TBC	Tel Aviv	416	TBC
Proposed Upscale Hotel	TBC	Tel Aviv	250	TBC
Proposed Luxury Hotel Rothschild Boulevard	TBC	Tel Aviv	135	TBC
Proposed Development Kikar Atarim	TBC	Tel Aviv	165, 220	TBC
Proposed Development (Luxury and Upscale)	TBC	Tel Aviv	160, 340	TBC
Dan Accadia Herliya (extension)	Dan Hotels	Herzliya	1,140	TBC

¹ Provisional and subject to further announcements

Source: HVS Research

Hotel Values and Investment

FIGURE 9: PERCENTAGE CHANGE IN HOTEL VALUES
(BASED ON US\$)



Source: HVS Research

Historical Market Value Changes

The indications for changes in hotel values in Israel are based on trading results from 2013 to 2019 and our view of trading prospects and investment appetite as of 31 December 2019.

2019 saw increased momentum with an overall increase in values of 5%, with growth recorded

across all markets (see Figure 9). Jerusalem and Tel Aviv hotels led the growth, which is not surprising given the impressive performance of hotels in both markets.

Scenario Analysis: Estimating Future Values of Israeli Hotels

Looking forward, and to give some perspective in these uncertain times, we have modelled three scenarios addressing the range of potential impact on hotel values in Israel. Our model considers a base line and three alternative scenarios which reflect the range of potential impact on hotel performance. We stress that the impact of current conditions on an individual property will depend on the characteristics of the property, its market, and its location – some hotels might experience a stronger recovery and appreciation, while some may take longer to recover.

Similarly, creativity and flexibility are likely to be the fuel of the recovery. Hotels that will thrive after this crisis are likely to be those that embrace agile

principles and rapidly understand customers’ evolving needs beyond the health and safety measures now being implemented. We consider that Israel’s history of volatility has not only demonstrated the value of being agile, but also how to succeed in such environments. We therefore remain cautiously optimistic when considering the Israel hotel industry’s ability to recover at an accelerated pace compared to other countries in the Mediterranean region.

Figure 10 illustrates our base line and valuation scenarios as described, leading to our conclusions of value in Figure 11. We stress that these are illustrative only and an actual valuation of an individual hotel may not produce the same results.

FIGURE 10: SCENARIO ANALYSIS AND KEY ASSUMPTIONS

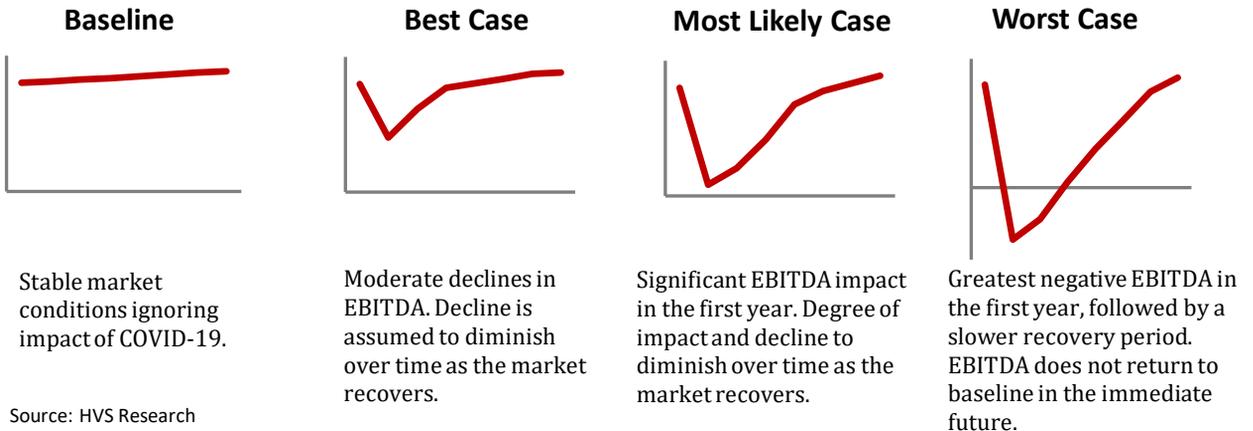
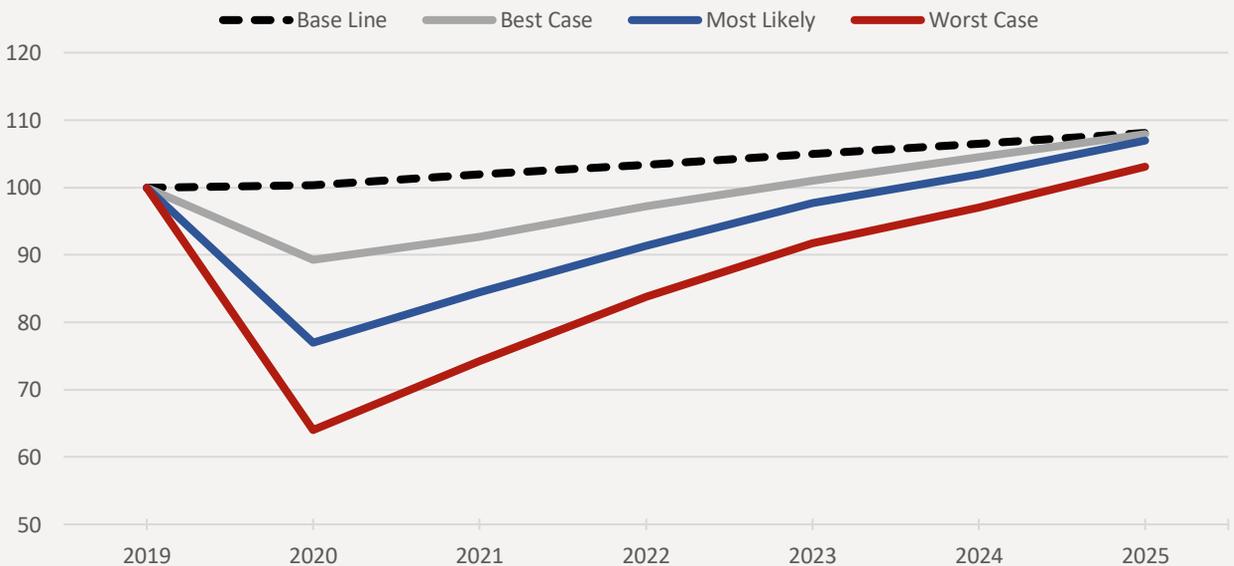


FIGURE 11: HOTEL VALUE EVOLUTION INDEX, 2019 = 100



Best Case

Values fall by 5-10% in 2020 and return to pre-crisis levels in 2023/24.

Most Likely Case

Values fall by 10-25% in 2020 and recover by 2024/25.

Worst Case

Values fall by 25-35% in 2020 and recover by 2025 or later, depending on the recovery pace of international tourism.

For context, the overall European market showed a 23% decline in value in the Global Financial Crisis in 2008-09 (please refer to our 2020 European Hotel Valuation Index report).

Conclusions

No-one knows the timeline as to how long this pandemic will last or the final net impact on the economy. What we do know is that the hospitality industry is extraordinarily resilient. Travel will return in the long run and we are cautiously optimistic when considering the Israel hotel industry's ability to recover at an accelerated pace compared to other countries in the Mediterranean region. Although this crisis is unprecedented and still deeply uncertain, Israel's hoteliers have had exceptional experience on how to thrive in periods of uncertainty.

Hotel values in Israel will remain depressed until EBITDAs 'hit the bottom' and there is evidence of recovery, but we strongly consider they will recover as cash flows improve and capital markets return to more traditional parameters. Last year saw a phenomenal increase in the number of visitors to Israel, and hoteliers will benefit greatly from persuading a proportion of them to return as quickly as circumstances allow to help spearhead the recovery of international demand.

– HVS –



About HVS

HVS, the world's leading consulting and professional services organisation focused on the hotel, mixed-use, shared ownership, gaming and leisure industries. The company celebrates its 40th anniversary in 2020 and performs 4,500+ assignments each year for hotel and real estate owners, investors, banks, operators and developers worldwide. HVS principals are regarded as the leading experts in their respective regions of the globe. Through a network of 60 offices and more than 350 professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. [HVS.com](https://www.hvs.com)

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With offices in London since 1990, **HVS London** serves clients with interests in the UK, Europe, the Middle East and Africa (EMEA). We have appraised some 4,000 hotels or projects in 50 countries in all major markets within the EMEA region for leading hotel companies, hotel owners and developers, investment groups and banks. Known as one of the foremost providers of hotel valuation and feasibility studies, and for our ability, experience and relationships throughout Europe, HVS London is on the valuation panels of numerous top international banks, which finance hotels and portfolios.

In Israel, HVS has worked on hotel valuations and feasibility studies throughout the country, in Jerusalem, Tel Aviv, Herzliya, Netanya, Akko, the Dead Sea, Mitzpe Ramon, the Galilee area and Eilat. Russell Kett has been a regular speaker on the hotel sector at conferences in the country.

We are grateful to the many hoteliers in Israel who provided operating data and other information for this report, as well as the Ministry of Tourism. We would welcome the participation of even more hoteliers to enable greater representation of the country's hotel sector.

About the Authors



Simon Hultén is a senior associate with the HVS London office. Before joining HVS, Simon held various positions in the hospitality industry. His main responsibilities now include hotel feasibility studies, valuations and

market overviews for European hotels. He holds a BA (Hons) in Hospitality Management from Glion Institute of Higher Education with a specialisation in hotel development and real estate.



Russell Kett, FRICS is chairman the London office of HVS. He has 40 years' specialist hotel consultancy, investment and real estate experience, focused on providing valuation, feasibility, shared ownership, property, brokerage, investment, asset

management, strategy and related consultancy services, advising hotel companies, banks, developers and investors on all aspects of their hospitality industry related interests, throughout the EMEA region. Russell is a frequent writer, moderator and speaker on the international hotel industry, especially topics relating to hotel valuation, investment, marketing and finance. He is a frequent visitor to Israel and maintains a home there.

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