W HOSPITALITY GROUP
Plot 10, Babatunde Crescent
off Oniru Market Road
Lekki Phase 1
Lagos, Nigeria
Tel: +234 803 321 0646
www.w-hospitalitygroup.com

THE HOTEL CYCLE **SEPTEMBER 2016**

My mantra has always been "don't generalise about Africa", a continent of 54 sovereign states, each as different from one another as are the 50 states of the USA, and the c50 countries in Europe (the exact number depends on how you count!). We used previously to group the African countries into three "blocs" – North Africa, South Africa and the bit in the middle, sub-Saharan Africa.

Looking at how the hotel industry in Africa has performed in the last two to three years, the continent is dividing more and more, according to how each nation's economy is performing. Almost without exception, GDP growth is a metric directly affecting hotel occupancies. West Africa which, with a few exceptions such as Senegal and Côte d'Ivoire, has many countries dependent on one or sometimes two extractive industries – Nigeria's oil, Ghana's oil and gold, Sierra Leone's iron ore, and so on. These countries are experiencing far lower GDP growth than in previous years, with lower demand and therefore prices for their exports, and the hotel sector is negatively affected accordingly. Look at Lagos, for example, the largest city in the region, and one of the largest hotel industries in terms of supply in sub-Saharan Africa:

The Lagos Hotel Industry				
	2013	2014	2015	2016 (Jan-Jul)
Hotel Occupancy	61.9	56.0	52.1	44.7
GDP Growth	5.4	6.3	2.7	-1.8 (FY)
Sources: STR Global (hotel occupancies); IMF July 2016 (GDP growth)				

The decrease in 2014 was due to the impact of the Ebola outbreak elsewhere in West Africa, which affected the hotel industry throughout the whole continent, and the onset of the oil price crash in the second half of the year – the figure for the first half of the year was 63%.

In East Africa, however, in cities such as Nairobi, Addis Ababa and Dar es Salaam the hotels are trading in the 60s and 70s, because the impact of commodity price reductions is felt less (and indeed, for importers of energy and raw materials, is a benefit). The economies of these countries are much more diversified, and are benefiting from a recovery in tourism numbers after declines caused primarily by terrorist activity.

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So we can now see a clear difference between (most) countries in West Africa and (most) countries in East Africa, a further divide in this far from homogenous continent, mono-sectoral economies vs diversified economies. Even in the five countries in North Africa, Morocco, whilst affected overall due to its proximity to other countries in the region, saw a slight increase in July 2016 YTD occupancies (to 57.9% compared to 56% in 2015, both figures Casablanca, source STR), compared to the disastrous results in Egypt, Tunisia and Libya, all affected by terrorist activity and subsequent economic malaise.

There seems to be an inevitable cyclicality in the world's economies, and therefore in the fortunes of the hotel industry. Boom and bust, some call it, although the peaks and troughs are less pronounced than during the post-war years of the second half of the 20th Century, as central bankers and politicians get better at handling recessions and recoveries. Because economies have an in-built cyclicality, so too does the hotel industry in major cities, where the hotels are dependent on business travellers and corporate conference activity for their mid-week business, and (mostly) domestic tourism for their weekend room sales.

This cyclicality needs to be reflected in projections made for new hotel projects, on which investment decisions are made, by assuming a downturn in profits every 7 to 10 years (somewhat spurious – why that particular year?), or stabilising the occupancy at a "prudent" level, lower than if continued growth been assumed or, and probably the best way, by stress-testing the stabilised projections with "what-ifs" such as reductions of profit vs serviceability of debt.

What does a hotel owner and general manager do when faced with unforeseen external events that cause the reservation clerk's telephone to fall silent? Well, this may sound like "told you so", but some measures can and should have been designed-in from the get-go.

In many African cities energy costs are high, not just because of running air-conditioning units 24/7, but also due to the need to run on generators for much of the time. Does your hotel have the ability to isolate wings of the building, and/or floors, when there are no guests occupying those rooms? And did you purchase different sizes of generator, so that a smaller unit, cheaper to run, is there when occupancies are low.

The same applies to water – did you think of the need to use less water when choosing your toilet flushes and your taps? Can you recycle grey water to use for the garden?

Hotels have high levels of fixed costs, as even if the property is empty, you still need staff for when guests do arrive, you have to keep the reception area lit and cooled, and there needs to be food and drink available. Over time, however, the majority of fixed costs can be made to be variable, which needs to be thought through not just at the time costs have to be reduced due to lower revenues, but also built into the systems and procedures in place when opening the hotel, to allow flexibility when required.

What sort of contracts were signed with the staff, including the expatriate personnel? Can you reduce their hours? Is any level of service charge guaranteed, or is it entirely flexible according to revenues? Laying off staff is often essential, to protect profits, but should be a last resort – the people make the product, guests often feel loyal to a particular hotel because of a connection to the staff that they encounter each time they visit. Breaking that connection will endanger revenue.

And, of course, protecting revenues is as important as reducing expenditure. In the face of a general downturn in the market, reducing prices is a futile gesture, but often the only tactic that inexperienced managers know of. It will not increase the market, just create a price war where nobody really wins – reducing your revenues means less cash available for maintenance, the property starts to deteriorate, you reduce your rates to compensate, ad infinitum. OK, so cash is king, and some cash is better than no cash at all, but rate integrity is also highly important in the long run.

Better than reducing prices is to add value, perceived or real, such as including breakfast in the room rate, or offering an extra night at half price, or free.

And protecting the revenue from your loyal and remaining customers, ensuring that they remain loyal, not tempted away by bargains elsewhere. Even more so than usual, the customer becomes the centre of everything that is done in the hotel, the centre of attention through his or her stay, from first arrival at the security gate, to leaving through that same gate a day or two later. Did your staff, in the nicest possible way, extract as much cash as possible from that guest? Were the receptionists, the barman and the headwaiter upselling?

Not forgetting that one of the biggest demand on cash is the bank, from whom the money was borrowed to build the hotel. That's why the stress testing of projections is so important – did you assume a constant 80% occupancy when showing you could pay interest and principal on the loan? Was the bank gullible enough to believe you?! Your loan terms need to have the flexibility to restructure when the operating scenario is demonstrably different from that prevailing when drawing down the loan.

It's tough times in Lagos and many other African cities right now. But, as I said, the cycle is inevitable, and the bad times will not last for ever. In many cases, exactly when the upturn will occur is difficult to judge, but it will come, that I am sure of.

Trevor Ward
W Hospitality Group, Lagos
trevor.ward@w-hospitalitygroup.com

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