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Serviced apartment sector emerges as dominant force

Sydney, NSW (9 September 2010)

The often maligned serviced apartment sector is tipped to become a much more dominant force in the Australian accommodation market according to a new report from CBRE Hotels.

The report highlights that 75% of new traveller accommodation projects either planned or under construction will involve serviced apartments, given the current financing constraints on new hotels and the comparative cost benefits of serviced apartment projects.

Serviced apartment product was first rolled out in Australia in the 1970s in response to growing consumer demand for apartment-style traveller accommodation suitable for extended stays.

CBRE Hotels Regional Director Ken Smith said the industry had matured considerably in the past 25 years, with a proliferation of purpose run, professionally managed serviced apartment operators including Mantra Group, Quest Serviced Apartments, Oaks Hotels & Resorts, Accor Hotels, Toga Hospitality, Mirvac Hotels & Resorts, Meriton Serviced Apartments, Q Resorts and StayWell Hospitality Group.

The CBRE Hotels report highlights a range of opportunities and challenges for the often misunderstood serviced apartment sector – a hybrid commercial/residential asset class which now accounts for a quarter of all casual accommodation in Australia, representing some 957 establishments and 53,118 rooms.

Currently, domestic customers make up 82% of serviced apartment business. "While domestic customers are comfortable with the self sufficiency and independence afforded by serviced apartments, international travellers are less so and lack knowledge of the opportunity," Mr Smith said.

"Without international brand recognition and with limited marketing, many international markets are unaware of the serviced apartment product and Australian serviced apartment operators."

Serviced apartments are ostensibly a residential apartment with varying degrees of service provided by a professional operator. To fit the definition, it must be at least a studio apartment with sleeping and living areas, food preparation areas, catering facilities and a bathroom which can be offered to the public for periods ranging from one night to a maximum of one year.

The report highlights that there are two distinct market segments in this sector, the leisure and the corporate traveller. Demand from the leisure traveller has fostered considerable serviced apartment development in tourist markets, particularly in Queensland which has the largest representation of this product type. Demand from the corporate market has fostered more recent development in urban areas.

ABS data highlights extraordinary growth in the sector's market share over the past decade, with serviced apartments now accounting for 25% of all room nights sold throughout Australia on an annual basis.

CBRE Hotels Queensland Associate Director Paul Nyholt said the growing popularity of the sector had attracted considerable interest from developers – particularly given the current funding constraints in regard to traditional hotel product.

The CBRE Hotels Traveller Accommodation Development Database shows that serviced apartments have represented, on average, just under 70% of all new traveller accommodation to enter the market over the past decade. Market growth is set to continue with serviced apartments representing 75% of new projects currently planned or under construction.

"At a time when it is difficult, if not impossible, to economically support the construction of a new build hotel in one line, serviced apartments are bridging the feasibility divide," Mr Nyholt said.

By strata titling serviced apartment projects, developers were able to tap into the private investor market for financing, a source not available to other forms of casual accommodation. However, Mr Smith warned; "Investors need to understand that they are purchasing an investment that relies on the dynamics of the traveller accommodation market and the ability of that market, the operator and the structure of the offering to support the purchase decision. To counter the poor investment performance of many past projects and to support the sustainability of the sector, future developments will need to be economically supportable not just successfully marketed."

The CBRE Hotels report also highlights a considerable divide between the cost of developing a brand standard hotel and a serviced apartment complex.

An analysis of the cost to build two very similar sized buildings of 10,000 square metres each, undertaken with the assistance of Rawlinsons quantity surveyors, puts the cost of building the hotel at \$4,621 a square metre, versus \$2,738 per square metre for the serviced apartment complex.

This takes into account the fact that hotels generally required low revenue generating guest services and public spaces, such as grand lobby areas, as well as more food and beverage outlets. In addition, serviced apartment product was less reliant on a prime location so could be built on cheaper land that was generally much more readily available.

The CBRE Hotels report also shows that serviced apartments typically produce a stronger operating performance.

“Serviced apartments have outperformed in regard to occupancy and room rates to show a revenue premium of 10% over the wider market in rent years,” Mr Smith said.

However, the sector is still facing its fair share of challenges – including a lack of consistency and clarity in the rating of serviced apartments, a lack of understanding by the wider investment community and a lack of market representation commensurate with its size.

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