CHAPTER 1.5

Hospitality: Emerging from the Crisis

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The year 2011 sees the hospitality sector across the world emerging from a period of significant challenge and considerable change. This has impacted different regions of the world in a variety of ways. Some are already seeing a strong recovery, as demonstrated by Asia, while others continue to lag some way behind, as is the case in Europe.

The year 2007 was a record year for the sector, with world tourist arrivals reaching 900 million and healthy double-digit revenue per available room (revPAR) growth across the globe. The global economic crisis, the absence of credit, and the fragile recovery in Europe now evident has resulted in some markets continuing to struggle while others resurge. In contrast to 2007, in 2010, Asia Pacific leads the pack in revPAR growth at 21.3 percent, exceeding Europe's absolute revPAR for the first time. When we compared 2010 performance to that of 2007, only one region—Central and South America—is ahead of its 2007 peak, by $12. While Asia Pacific is on par with its 2007 performance, Europe is $18 short of its own top performance in 2007.

This chapter takes a look back to hospitality performance across the globe before and during the crisis, and then reviews where the industry is today as it emerges from the crisis (Figure 1).

2007: Tourism before the world economic crisis

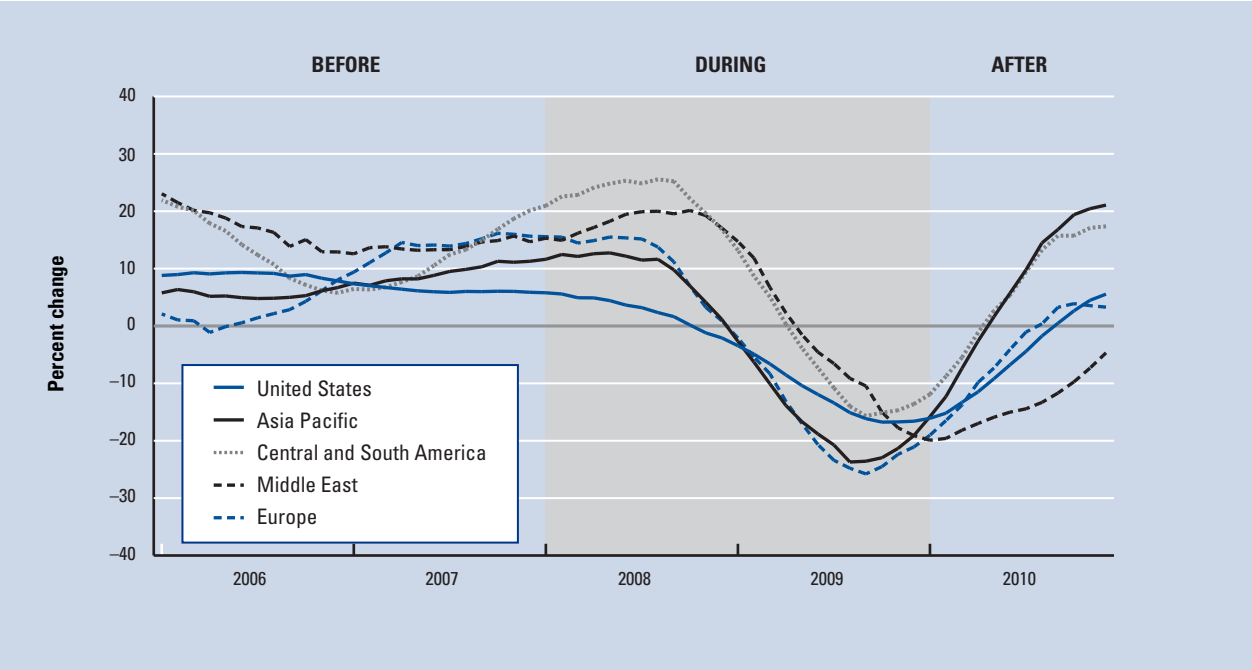
World tourist arrivals passed another milestone in 2007 to reach 900 million, overtaking tourism forecasts for the fourth successive year. This 6 percent year-on-year increase was even more remarkable given that the worldwide figure had hit the 800 million mark just two years previously.

There were around 52 million more international travelers than the previous year, confirming how eager people were to take advantage of cheaper airfares and easier access to emerging markets. Strong economies across most regions, but particularly in China and India, where more people had more disposable income than ever before, were an important factor in this increase.

Aviation was also experiencing a major shake-up. The inaugural flight of the A380 double-decker airbus from Singapore to Sydney in October 2007 was an important milestone, with Airbus predicting massive growth in the number of passengers worldwide. The introduction of this supersize aircraft was expected to generate increased demand at a time when the United States and the European Union (EU) had finally agreed to liberalize the transatlantic air travel market. From March 2008, European and American airlines would be able to fly to any destination in Europe and the United States, ending years of restrictions and leading to more flights and lower fares.

Note: All hotel performance data have been sourced from STR Global Limited and Smith Travel Research, Inc. All tourist arrival statistics have been sourced from the World Tourism Organization (UNWTO).

Figure 1: Global revPAR performance, before, during, and emerging from the crisis



Source: STR Global and Smith Travel Research Inc.

With so many more people traveling, it is no wonder that 2007 was a year of double celebrations for hoteliers and a double first for the hospitality industry (Box 1). Asia Pacific, Central and South America, Europe, and the Middle East not only celebrated double-digit growth in revPAR but also in average room rates.

Best performers were hotels in Central and South America with a revPAR growth of 19.4 percent, followed closely by the Middle East at 16.9 percent. Europe came in third place with 15.8 percent, but was still the revPAR king in terms of absolute revPAR, which stood at $114. At the back of the pack was Asia Pacific, with 12.5 percent.

The impact of the world economic crisis

2008: Entering the crisis

Although an extremely positive year worldwide for travel, 2007 was the last year to see such growth before the global economic crisis reached the industry. Across the globe, 2008 presented a challenge; it was only a matter of time before the tourism industry fell victim to the economic slowdown. The industry did make headlines for many positive reasons during 2008, including the Open Skies agreement in March, the 2008 Beijing Olympic and Paralympic Games, and the long-awaited opening of the $1.5 billion Atlantis Hotel in Dubai. Just beneath the surface, however, hotel performance was starting to struggle. With plunging global economies and unprecedented bailouts by governments around the world, it was only a question of time before tourism experienced the same troubles.

During the first half of 2008, when the full extent of the financial crisis was still some way off, the number of international tourists was still growing, and was up 5 percent above 2007 figures. Most world regions were reporting double-digit growth in hotel performance until mid way through the year. Then the deepening recession took its toll, with many world regions seeing performance take a nose dive in the final quarter of the year.

As business travelers and tourists started to think twice about trips away, there was a significant slowdown in revPAR. North America ended the year with a 1.6 percent decline, while Asia Pacific and Europe saw growth of less than 2 percent. Central and South America and the Middle East, however, went on to turn in double-digit revPAR growth, up 14.5 percent and 18.3 percent, respectively, confirming that, even though the market was difficult, it was not uniformly so around the world.

Adding up the total number of travelers, the UNWTO said that figures started to fall in the second half of the year, with year-on-year performance running at –1 percent, bringing down the net growth for 2008 to 2 percent. This was an obvious slowdown from the 7 percent growth recorded in 2007, but it still meant that an additional 16 million people had traveled around the world, taking the number of tourist arrivals to a record high of 924 million.

If we look at performance country by country, it is easy to see the correlation between sports and politics on hotel performance. The Beijing 2008 Olympic and

Box 1: 2007 regional review

Asia Pacific

More than 185 million international tourists visited the Asia Pacific region in 2007—an increase of 10 percent over the previous year. Several factors were behind this growth, including the phenomenal expansion of low-cost airlines. These companies were transporting a new wave of travelers from China and India and opening up new source markets, such as Russia. Fierce competition among the low-cost carriers was also bringing down the cost of travel, making it an affordable option for many more people and subsequently pushing up the demand for hotel rooms.

The two countries that made the biggest impact on the region's tourism during 2007—and on its economy as a whole—were China and India. While the dragon limbered up for the 2008 Olympics, China was enjoying excellent GDP growth and attracting a massive amount of foreign investment. Its newly rich population was keen to explore life beyond their national borders, and eager to spend their money on vacation. India, too, was booming, and attracting many more tourists—tourist arrivals to India were up 13 percent in 2007—while its emerging middle classes were anxious to spread their wings. By 2007 the impact of these two economic powerhouses was being strongly felt in their own backyards—the greater Asia Pacific region—and worldwide.

Central and South America

Tourist arrivals to Central and South America were up 11.1 percent and 8.1 percent, respectively, during 2007. An important factor was the weak US dollar, which kept US travelers—keen to get good value for money—closer to home.

Another driver was the decision made by 12 countries across South America to allow their citizens to travel among them without a passport. Those signed up to the pact are Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Suriname, Uruguay, and Venezuela; tourism figures suggest this strategy is working.

The region also received a massive global accolade in 2007, when more than 100 million voters worldwide placed three of the region's most famous attractions—Mexico's Chichen Itza pyramid, Brazil's statue of Christ the Redeemer, and Peru's Machu Picchu—on the list of the New Seven Wonders of the World. The others—the Taj Mahal palace in India, the Great Wall of China, Petra in Jordan, and the Coliseum in Rome—are geographically spread, but the concentration of "wonders" in Central and South America will enhance the region as a preferred destination.

Hoteliers in this region had already achieved the world's best growth in revPAR in 2007, which was up 19.4 percent to $74, with average room rates increasing by 17.2 percent.

Europe

In 2007, Europe remained the favorite destination of more than half of the world's travelers. Even though the sports and culture calendar for 2007 was not as busy as it had been the previous year, the region remained on top of the world when it came to revPAR performance—up 15.8 percent to $114. Generally, a strong economy drove both corporate and leisure business, and several key cities, including Paris and London, had high-profile events such as the Tour de France Grand Départ in London, the biennial Paris Air Show, and the Rugby World Cup.

Europe's share of the global tourism market topped 480 million in 2007—up 19 million over the previous year—and seven of the world's top 10 tourism destinations were in Europe. France took pole position, with Spain, Italy, the United Kingdom, Germany, Austria, and Russia completing the list.

One of the main drivers behind increased tourism in Europe was the growth of low-cost air travel. In September 2007, the low-cost players provided almost 22 million seats on 133,000 flights with companies extending their networks rapidly.

The Middle East

The Middle East increased revPAR by 16.9 percent to $108 in 2007, exceeding growth in both Europe and Asia for the fourth consecutive year. That year also marked the fourth of double-digit growth in the region. As in previous years, average room rates were the main driver, up 11.3 percent to $150, while occupancy increased 5 percent to 71.6 percent.

Hotels in the Middle East during 2007 had the kind of business growth rates that hoteliers in other parts of the world could only dream about. While Dubai, the hothouse of the region, took the largest share of the limelight in recent years, its neighbors started getting in on the act.

However, the Middle East remained a politically volatile region, and some countries can only watch this dynamic growth with envy. Iraq and Lebanon, for example, faced uncertain futures. But despite concerns over safety and security, the Middle East attracted 46 million international tourists in 2007—up 5 million over the previous year—with Saudi Arabia and Egypt increasing visitor numbers rapidly.

The United States

The United States saw revPAR rise a modest 6.1 percent in 2007, to $67. Growth was driven primarily by average room rates, which ended the year at $104, while occupancy dipped slightly to 64.2 percent. The weakness of the dollar made the United States an attractive destination for international travelers during the year, and it made staying at home an attractive option for Americans otherwise interested in traveling abroad. Despite an increase in activity from overseas, the US economy started to slow in 2007. Housing prices were down roughly 20 percent compared with their 2006 peak, commodity prices were high, and consumers started to feel the pressure on spending.

Paralympic Games, for instance, allowed the city's hotels to push up room rates by more than 450 percent on the opening night of the Games. Formula 1 racing in Singapore and the European Football Championships in Switzerland and Austria had a similar—though not as spectacular—impact on hotel room prices.

Outbreaks of political unrest in Thailand, the war in Gaza, and the bombings in India all had the expected impact on tourism in the affected countries. And fluctuating oil prices took their toll on some airlines.

When record highs of $147 a barrel hit in July, many airlines went into liquidation—including long-haul low-cost carriers Oasis Hong Kong and Zoom Airlines Inc., as well as European budget carrier XL Leisure Group. Other operators cut schedules and altered their timetables to cope with falling demand. Many of the enablers of the growth seen in 2007 were starting not just to weaken but to be removed.

At the end of 2008, the outlook for 2009 was naturally cautious, with the UNWTO predicting either a stagnation or a slight decline in international tourist arrivals, forecasting a drop of between 1 and 2 percent. Meanwhile, most economists were expecting the recession to hold down employment as well as housing and equity markets for some time to come. Unlike specific, individual events that have knocked the tourism industry, 9/11 and SARS for instance, the economic gloom was considered likely to keep consumer confidence—and therefore spending on travel—down for a much longer time.

2009: Global tourism plummets

Entering 2009, many hoteliers foresaw the time as one that would determine survival of the fittest. Most economists expected the global slowdown to last into 2010, with the inevitable loss of jobs during the year ahead. The strategy for the tourism industry in 2009 was to focus on survival, and for hotels in particular this meant providing value for money. Concentrating on what they do best, what differentiates them from others, and providing the essentials of good hospitality would help them to maintain their brand strengths as hoteliers competed to fill their rooms.

Tempting as it is to slash room rates to bring in business, this is not a long-term solution, as it takes average room rates much longer to recover than it takes occupancy levels. Reductions in airfares because of low oil prices—$35 a barrel in February 2009 compared with $147 in July 2008—helped to keep hotel rooms partially booked.

Hotel performance around the world remained weak at the half-way point in 2009. Europe was the most affected region, as revPAR there fell 31.3 percent, followed by Asia Pacific and the Americas. The Middle East continued to be the least affected region, witnessing a revPAR decline of 17.5 percent.

As the swine flu pandemic escalated and more cases and deaths were reported around the world, the tourism industry looked at ways to stop the spread of the virus. News stories reported that some airlines and cruise companies took extra precautions and refused to carry passengers who were showing symptoms. What the overall impact this pandemic would have on hoteliers at this time was still uncertain, but at a time when consumers and businesses were already cutting back on travel, this was a further contrary factor in the generation of room night demand.

In the second quarter of 2009, however, the first economies started to emerge from the recession and hoteliers hoped for increased consumer and business confidence to drive the recovery. Germany, France, Singapore, and Thailand were among the first to emerge from the recession, although it would still be some time before hoteliers saw a positive impact on performance. In July, the hotel industry suffered from terrorism once more when the JW Marriott and Ritz Carlton hotels in Jakarta were targeted by a suicide bomber. The A (H1N1) influenza also continued to spread around the globe, but it did not seem to cripple tourism demand in the affected areas in the same way SARS had in mid 2003.

Hotels in Central and South America saw revPAR fall 14.0 percent to reach $67 in 2009, the least severe declines of all global regions. North America took second place, behind Central and South America, reporting declines of 17.0 percent to arrive at $54. This decline was a result of occupancy falling 8.7 percent to 52.2 percent and $10 being stripped off average room rates to settle at $98. These results put North America at the bottom of the global league table in all three performance indicators. RevPAR in the Middle East fell 18.3 percent, to land at $124. Despite this, the region continued to post the highest occupancy, average room rates, and revPAR in the world. RevPAR in Asia Pacific fell 19.4 percent to $73 during 2009. Despite the full year double-digit declines in the region, hotel performance picked up during the latter part of 2009, with occupancy increasing 9.8 percent in December alone to attain 62.1 percent. This was good news for the region and confirmed that Asia Pacific was on the road to recovery, supported by improving economic conditions. Europe remained the worst performer in 2009, with revPAR dropping 21.2 percent to $81.

Emerging from the world economic crisis: Asia leads the way

The year 2010 marked more than just a new decade: it marked the beginning of the recovery process in many of the world's economies and an upturn in hotel performance (Box 2). The last two years have proved that not all regions are created equally, and shown a dramatic difference between the top- and bottom-performing regions in terms of hotel performance.

How have the regions fared compared with their performances in 2007? Are any of them close to their 2007 peak? In terms of revPAR growth, Asia Pacific

Box 2: 2010 regional review

Asia Pacific

Asia Pacific was the frontrunner in terms of recovery in 2010, getting off to a strong start in January with revPAR growth in excess of 20 percent. China performed particularly well in 2010, with revPAR up 30.9 percent, and its prospects for the future look good. The World Tourism Organization predicted that China would overtake France to become the world's largest tourist destination by 2015. The World Expo 2010 in Shanghai also helped the recovery process in Asia, boosting performance in the city.

The region's hospitality sector is recovering well from the economic crisis and, as at 2010 year-end, has come out on top. The fundamentals of strong economic growth, an increasing middle class, and increasingly available air travel will continue to support the strong performance of the hospitality industry in Asia.

Central and South America

Central and South America took the second spot in terms of revPAR growth during 2010, rising 17.4 percent to attain $78. Many countries in the region are experiencing strong economic growth, which is boosting the area's domestic travel. However, on the flip side, the region's strong exchange rates are discouraging international inbound travel. Brazil is a prime example of this trend, which has seen revPAR rise 32.8 percent, driven principally by regional travel. The region suffered a number of setbacks in 2010, including the devastating earthquake in Chile in February, the floods in the Cusco region of Peru that trapped tourists at the famous Inca ruin Machu Picchu in April, and landslides in Mexico in September. Past experience has taught us that natural disasters do not generally impact tourism over the long term, however, and the effects of these disasters are not expected to override the recovering growth rate overall.

Europe

The Icelandic volcanic ash cloud caused widespread chaos over much of Europe during April 2010, closing European air space and grounding all flights in and out of the region. A number of European countries, including Greece and Ireland, sought emergency bailout packages during the course of the year, putting extra pressure on the region's economy and consumer confidence. This pressure has been softened in part by the weak euro making Europe more affordable for American tourists.

The year 2010 saw modest revPAR growth of 3.3 percent in Europe. The market is underperforming all of the regions in absolute revPAR terms, aside from Central and South America, which—with revPAR growth of 17.4 percent—is likely to overtake Europe shortly. RevPAR in Europe is currently sitting at levels not seen since 2006 and is $19 off the region's peak in 2008.

Europe's hospitality sector is likely to continue to experience challenging markets in to 2011. With rising travel costs, reductions in low-cost airline supply, and slow underlying economic growth, the region will continue to lose ground to Asia. While difficult to prove, the economic crisis may well have accelerated the shift of hospitality growth from Europe to Asia.

The Middle East

Hotel performance in the Middle East at the end of 2010 was down 4.4 percent to $123, the only region to remain in negative growth. Over the past few years, hotels in the Middle East experienced fast and strong growth due to a supply shortage combined with increased interest in tourism in its burgeoning destinations. Now that supply has filled the gap, it is only natural that hotel performance is experiencing an adjustment. Although the timing of the global economic crises exacerbated

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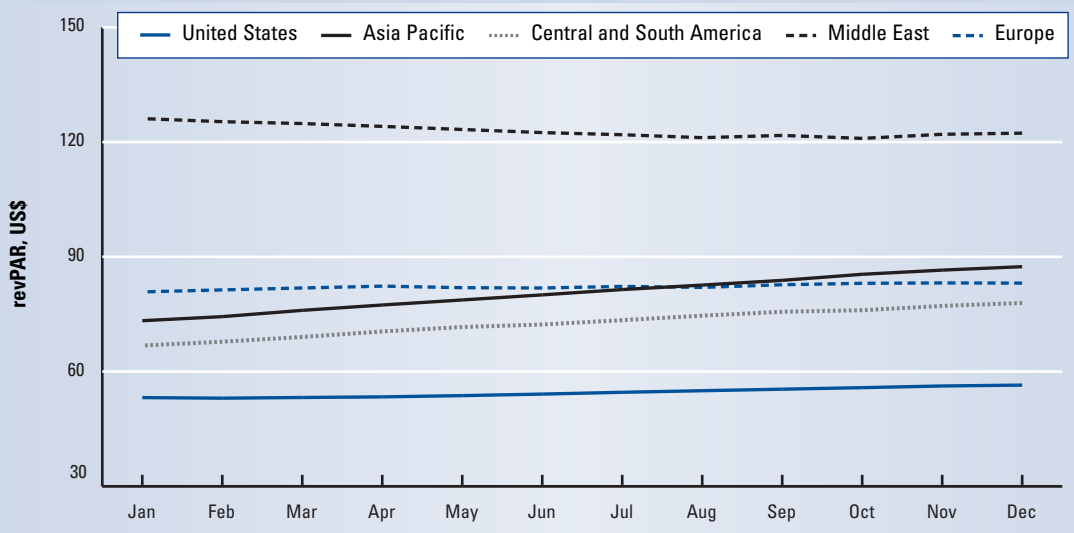
Global absolute revPAR performance, 2010



Source: STR Global and Smith Travel Research Inc.

Box 2: 2010: regional review *(cont'd)*

the decline, hotels across the Middle East still achieve the strongest average room rates ($201) and revPAR globally at $123, as can be seen in the figure. This revPAR is $35 higher than in Asia Pacific, the next best performing region.

The Middle East's geographical position as the crossroads between West and East, coupled with its well-developed infrastructure, particularly for aviation, will see it fare well in the future with continuing visitor growth forecast. According to year-to-November 2010 results from STR Global, the Middle East saw a 9.2 percent increase in hotel supply (higher than any other world region), an increase that will continue to put pressure on hotel performance in the region as the supply pipeline remains substantial.

The United States

The United States reported a modest 5.6 percent growth in revPAR during 2010, to reach $56. March 2010 was the first month of positive revPAR growth in the country, after 19 consecutive months of decline, and has been strengthening each month: November posted the strongest monthly growth in 2010 of 11.8 percent. The US economy made a slow but steady recovery during the year. Unemployment in the United States hit a seven-month high in November 2010 and started to raise concerns about the strength of recovery. In the same month, the Federal Reserve announced that it would be pumping $600 billion into the economy to help stimulate growth—the second major stimulus package the Fed has introduced to try kick-start recovery. However, the high unemployment rates and the weak housing market in particular are hampering growth. The oil spill off the Gulf of Mexico also threatened the tourism industry along the Gulf Coast. When a BP Deepwater Horizon oil rig caught fire and eventually sank, spewing thousands of barrels of oil a day into the Gulf of Mexico, tourism destinations along the coast suffered in its wake. Many coastal resorts and beaches along the Gulf Coast suffered serious losses as a result.

Table 1: Global hotel performance, 2010 vs. 2007

	2007 revPAR	2010 revPAR	Percent change
United States	66	56	–15.2
Asia Pacific	88	88	0.0
Middle East	136	123	–9.6
Central and South America	66	78	18.2
Europe	101	83	–17.8

Source: STR Global and Smith Travel Research Inc.

came out the clear winner, with revPAR up 21.8 percent over 2009, as highlighted in Figure 2. In comparison with its 2007 performance, revPAR in the region is now the same as 2007 at $88, as can be seen in Table 1. The next best performing region in terms of revPAR growth was Central and South America, up 17.7 percent in the year. It can proudly boast that it is the only region that has surpassed its 2007 performance, with revPAR now at $78—some $12 higher (18 percent more) than 2007. All other regions fell into single-digit growth during 2010, apart from the Middle East, which is still experiencing revPAR declines of 5.8 percent for the year.

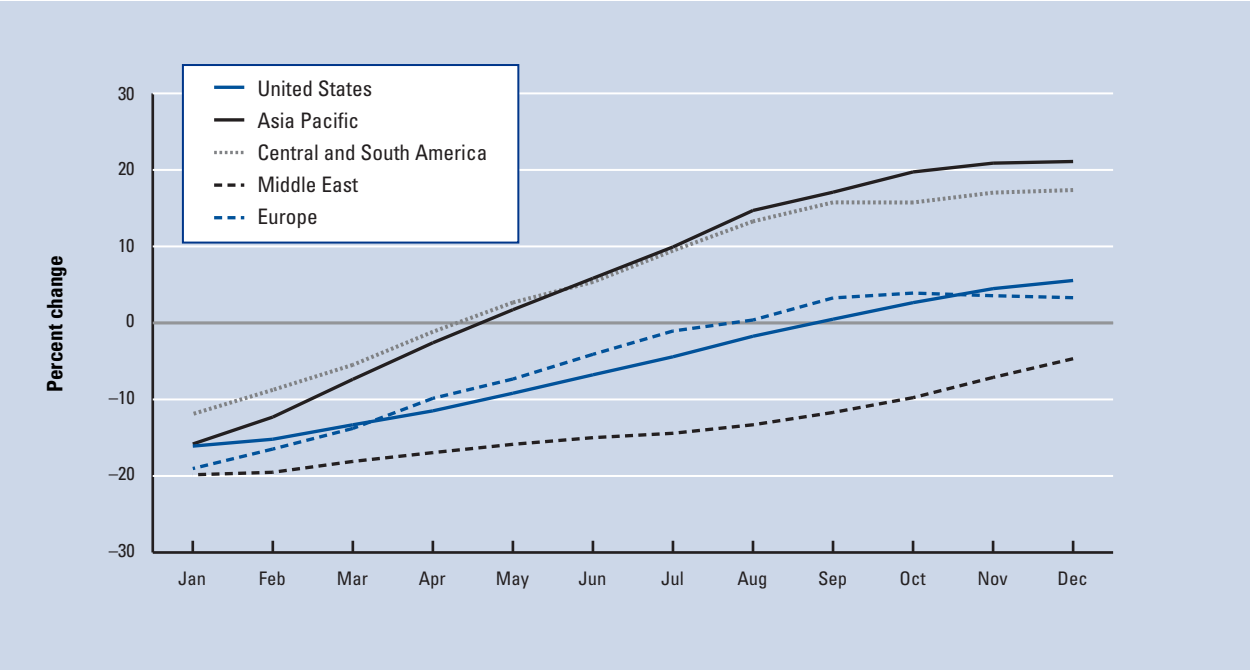
The crisis has been very different for each region. Europe has been hit the hardest and has the most to lose in the structural shift that may have been accelerated with the move to the East. With 51 percent of global travel to Europe in 2007, the stakes were high. With low growth envisaged for some time in Europe and the dramatic decline it experienced in the last three years, it may now be that Asia Pacific is signaling it is time for Europe to move over as it takes the lead—the first signs are there. As shown in Table 2, Asia Pacific has seen the lowest percentage decrease in travel during the period and has surpassed 2007 levels.

A recent Deloitte report, "Hospitality 2015," focused on seven areas, illustrated in Figure 3, that will be critical to the development of the hospitality sector through to 2015. The report highlighted the argument that, as consumer demand recovers, it will be reshaped by two key demographic trends. In established markets such as those of the United Kingdom and the United States, the rise of the affluent, time-rich, and travel-hungry baby boomer generation—aged 45 to 64—will evolve and grow. By 2015 in the United States alone, boomers are expected to control 60 percent of the nation's wealth and account for 40 percent of spending. With more time for leisure as they approach retirement, spending can be expected to be more focused around travel.

In emerging markets such as India and China, however, there will be a significant rise of the middle classes, generating an increase in demand for both business and leisure travel. GDP per capita in China is forecast to more than double between 2010 and 2015, providing the population with greater disposable income to spend on hospitality; India is forecast to have 50 million outbound tourists by the end of the decade. Each is a potentially huge feeder market. While much of the development until recently has focused on the upscale and luxury market, the greatest potential in these markets lies in the growth of branded mid-market and budget product aimed primarily at the domestic traveler.

Indeed, the Indian government has identified a shortage of 150,000 hotel rooms, with most of the undersupply in the budget sector. Understanding the desires and motivations of the Chinese and Indian traveler will be fundamental to success in these markets.

Figure 2: Global revPAR performance, percent change (2010)



Source: STR Global and Smith Travel Research Inc.

Table 2: World tourist arrivals, millions

							PERCENT CHANGE		
	2005	2006	2007	2008	2009	2010	2008–07	2009–08	2010–09
World	802	846	901	919	880	935	2.0	–4.2	6.7
North America	89.9	90.6	95.3	97.7	92.1	99.2	2.6	–5.7	7.8
Asia Pacific	153.6	166.0	182.0	184.0	181.6	203.8	1.1	–1.3	12.6
Middle East	37.8	40.9	46.9	56.0	53.2	60.0	19.3	–4.9	13.9
Europe	441.0	463.9	485.4	487.6	460.0	471.5	0.5	–5.7	3.2

Source: UNWTO.

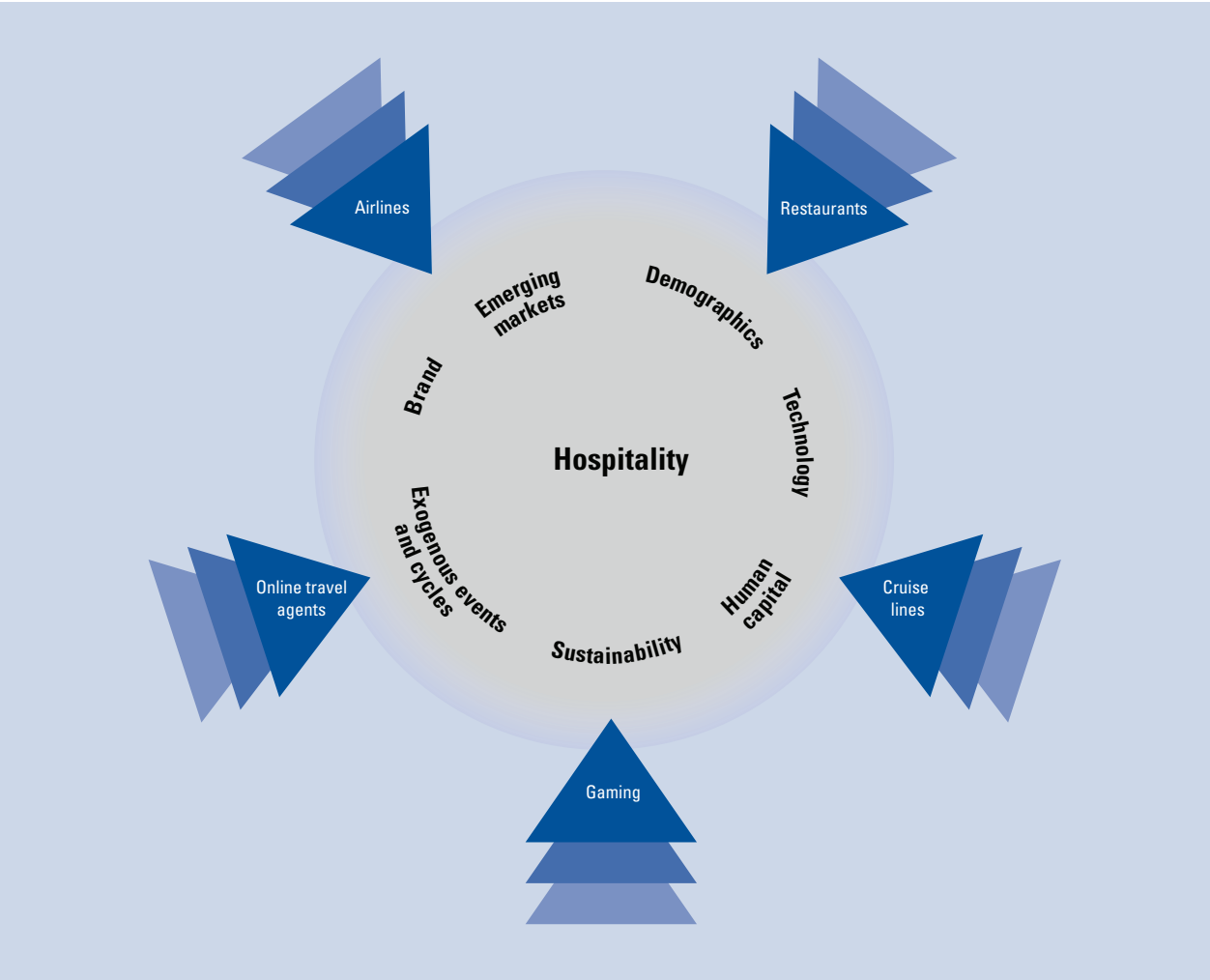
While the growth in these emerging markets is significant, it should not distract from the absolute size of the mature markets. It is forecast that the share of global tourism GDP will shift by less than 5 percent from mature hospitality markets to emerging markets by 2015.

The travel and hospitality industries are expanding rapidly in a number of emerging economies across the globe. Countries with a forecasted average annual industry growth rate from 2009 to 2015 of 5 percent or more include the BRIC nations—Brazil, Russia, India, and China—and certain countries in South East Asia, the Gulf States, North Africa, and the West African coastline.

This growth compares with forecasted growth rates of around 2 to 3 percent in more mature markets (the United States, the United Kingdom, France, and Japan). However, with the key exceptions of China and India, these emerging markets are unlikely to become truly significant on a global scale, despite the fact that their hospitality industries show rapid relative growth. By 2015, China and India will each have absolute year-on-year industry growth comparable to or greater than the United Kingdom, France, and Japan. By 2019, Chinese absolute industry growth is forecast to exceed that of the United States.

Emerging markets present hospitality groups with significant opportunities, but they also offer unique challenges. This is particularly the case in India, where hospitality is lagging behind the Chinese market, which opened up earlier and presents fewer hurdles for new entrants. Despite this, many brands that have already begun their expansion into China are now assessing

Figure 3: Seven key areas needed for development of the hospitality industry to 2015



Source: Deloitte, 2010.

"where next" and are reinforcing their long-term commitment to the Indian market.

The economic crisis has undoubtedly impacted regions in differing ways for the hospitality sector, yet its most significant impact may have been to accelerate the shift East. While the mature markets of Europe and the United States remain large in absolute terms, their continued growth is likely to be significantly outstripped by Asia Pacific, which is already proving its strength in the speed of its recovery in 2010.

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