IRISH HOTELS FEDERATION

SUBMISSION

to the

MINISTER FOR FINANCE

BUDGET 2011

SUPPORTING
HOTELS AND GUESTHOUSES
TO
SURVIVE THE ECONOMIC CRISIS AND
CONTRIBUTE TO ECONOMIC RECOVERY

September 2010

TABLE OF CONTENTS

ONE PAGE SUMMARY

Despite the relative improvement in the economic environment in 2010, the hotel and guesthouse sector remains in a crisis situation. There is a large over supply of hotel accommodation. The market is much below the pre crisis level. Revenue per room has continued to decline. The credit situation remains bleak. Many hotels are not commercially viable. The future of the sector is threatened by unfair competition from non viable bank-owned hotels offering uneconomic prices. Many leading hotels have gone into receivership or examinership and NAMA casts a layer of uncertainty over the sector.

In the first six months of 2010 overseas visitors declined by 20.5% while British visitors declined by 22.2%. The average room rate has decreased by 11.8% in 2009. The room rate is now at 1999 levels. Room occupancy rates had fallen in 2009 but have increased slightly in the first half of 2010, but at uneconomic room rates.

The Government should play its part in the immediate task of ensuring the survival of the hotel and guesthouse sector and preparing it to contribute to economic recovery in a medium term growth strategy in Budget 2011 by:

1. Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland marketing budgets.
2. Avoiding any tax increases in tourism related products and services at national and local levels and introducing a four year freeze on all public sector charges at the 2009 level.
3. Reducing energy costs and reducing local authority rates by 30%.
4. Immediately removing the Air Travel Tax.
5. Renewing the Employment Subsidy Scheme.
6. Ensuring the availability of appropriately priced credit and the establishment of a bank for reconstruction and development.
7. Facilitating the orderly reduction of excess capacity through adjustment of the tax regulations concerning tax allowances for new hotels and ensuring the planning process and regulations are not a barrier to capacity reduction.
8. Abolishing the JLC system of establishing wage rates to encourage competitiveness and support commercial viability.
9. Removing unnecessary barriers to travellers and introducing a common visa area for Ireland and Britain.
10. Restoring detailed tourism figures from the Central Statistics Office which are vital to efficient marketing and planning.
11. Maintaining the over 66 free rail travel scheme for tourists on Iarnrod Eireann and removing the unnecessary requirement for a limited period trekker ticket.

EXECUTIVE SUMMARY

2010 has been another very poor year for the hotel and guesthouse sector following the disastrous performance in 2009. As stated in last year's budget submission, the sector is in a crisis situation. The Irish economy which determines the domestic tourism segment continued to perform weakly in 2010 and only modest growth in consumer expenditure is expected in 2011 by most forecasters. The international economy will also improve in 2011 with a Euro area growth of about 1.8%. The weak economic situation has been directly and quickly reflected in very substantial declines in tourism volumes and in levels of hotel activity. This 2010 situation follows a disastrous 2009 performance. Of great concern to the IHF is the expectation that even with Irish economic growth resuming in 2011, and possibly in 2010, the 2007 volume of Irish consumer expenditure and economic activity will only be reached in 2015 or 2016 according to IMF projections or slightly earlier according to Government projections.

The IHF is appreciative of Government efforts and initiatives such as the employment subsidy scheme, the credit review process, alcohol excise reduction, support for marketing and the opening of Convention Centre Dublin but much more needs to be done.

The weak demand situation has been intensified by the credit crisis which is making it very difficult for hotels and guesthouses to obtain adequate levels of credit despite the various efforts and initiatives of Government. As in 2008 and 2009 the hotel and guesthouse sector is currently facing low levels of demand, declining prices, excess capacity, low levels of room occupancy, limited availability of credit and a high cost operating environment in Ireland. All the evidence shows that the hotel and guesthouse sector is in a very difficult situation and the emphasis of most operators is on surviving the recession, and hopefully, thereafter placing their enterprises in a position to benefit from the eventual economic upturn. Many leading hotels have gone into receivership or examinership and the sector faces unfair competition from bank owned hotels operating on a cash flow basis with commercially unsustainable prices. In addition the sector faces the uncertainty that many hotels will be under the control of NAMA.

The hotel sector has invested substantially in capacity, facilities and refurbishment in the years before the economic collapse. For the next few years the likely levels of domestic and international tourism will be insufficient to support this increased capacity. It would be ideal if sufficient levels of demand could be generated to utilise the available capacity at sustainable prices. However, that is not likely. 65% of hotel bednights in 2009 were from the domestic market. The domestic market will be weak for several years and fully replacing the demand lost from a weak domestic market with international tourists will take several years. In the meantime the concern is that the over capacity will destroy the short term viability of the overall hotel sector.

In the absence of supportive policy measures, the sector faces a medium term situation of over capacity with damaging consequences for the commercial viability and sustainability of the entire hotel sector. In the absence of appropriate policy initiatives, the hotel and guesthouse sector will not be in a position to actively participate in an ambitious medium term economic growth strategy which is clearly needed.

The current tourism and hotel positions are weak:

- International visitors have declined by 20.5% in the first six months of 2010, British visitors declined by 22.2% following earlier substantial declines in 2009.
- Domestic holiday tourism trips declined by 8.2% between 2008 and 2009.
- The average room rate declined by 11.8% in 2009 following a decline of 9.7% in 2008.
- The 2009 room rate is now at 1999 levels.
- Hotels have introduced substantial cost cutting measures while being constrained by costs such as labour rates and public sector determined costs. The operating cost per room declined by 16.5% in 2009.
- Profits per room declined by 34.1% in 2009.
- The worsened business environment has made it difficult for hotels and guesthouses to obtain required levels of bank credit to cope with the recession despite the various initiatives introduced by Government.
- Many hotels have gone into receivership and examinership.
- In the five years 2003 to 2008 hotel room capacity grew by 41% or almost 18K rooms. The combination of increased capacity and greatly decreased market has substantially reduced hotel occupancy rates. These lower occupancy rates are being achieved only with lower prices.
- The Failte Ireland Tourism Barometer for the first half of 2010 reported that 47% of hotels and 74% of guesthouses had experienced a decline in the number of bednights compared with 2009.
- The room occupancy rate dropped from 70% in 2007 to 64% in 2008 and 59% in 2009. In the first six months of 2010 the hotel room occupancy rate increased from 51% to 54%.
- While lower prices are desirable to promote tourism the current room rates are not commercially sustainable with the Irish cost base.

While many of the negative factors affecting the hotels sector are beyond the control of the Government such as the international economic situation, Budget 2011 is capable of substantially improving the tourism and hotel situation. It can sustain and consolidate the tourism resource and enhance competitiveness.

The strategic policy and sectoral objectives for tourism must be to survive the recession and thereafter begin to increase its market shares of both domestic and international tourism. The proposals are consistent with the “survival action” recommendations of the Report of the Tourism Renewal Group which covered investment in marketing, reduction in access costs, prioritising of public spending on tourism and the support of sustainable enterprises.

Budget 2011 can begin this process and should address the following areas:

1. Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland marketing budgets and maintaining ongoing specific additional marketing activity. The major priority over the next few years must be to regain lost ground in the British market in addition to attracting new business/conference visitors to derive maximum benefit from the availability of Convention Centre Dublin. Marketing activity is a main determinant of market share. Irish tourism cannot solely depend on growth in international markets. We must aim to increase our market share of the now smaller international market. In particular, the short to medium term marketing effort and focus must continue to have the British market as a priority to win back the recent large decline in the number of British visitors.
2. Avoiding any tax increases in tourism related products and services at national and local levels and introducing a four year freeze on all public sector charges at the 2009 level.
3. Reducing energy costs and reducing local authority rates by 30% for 2011.
4. The Government should immediately remove the air travel tax. As an island destination the range, cost and quality of access to Ireland is absolutely critical to overseas tourism and its export earning potential. With the current pressure on airline margins (driven by fuel price volatility airport charges as well as declining demand), Ireland cannot afford to incur competitive disadvantage that makes routes to and from Ireland less attractive for airlines seeking to maximise their return. The risk of competitive disadvantage has been heightened by the recent trend of other Governments removing travel taxes and other access-related levies and charges, in response to their negative economic impact in the current downturn. The air travel tax, and concerns about its future evolution are also having a significant negative impact on confidence in the Irish tourism industry, which is already under severe pressure.

5. Renewing the employment subsidy scheme available to the hotel/guesthouse sector when it expires in November of this year.

6. Ensuring the availability of appropriately priced credit to the hotel/guesthouse sector including the establishment of a bank for reconstruction and development geared towards SMEs.

7. Facilitating the orderly reduction of excess hotel capacity through adjustment of the claw-back regulations attached to capital allowances for hotel development, including the facilitating of change of use, and ensuring that the planning process and regulations are not a barrier to capacity reduction.

8. Abolishing the JLC system of establishing wage rates to encourage competitiveness and support commercial viability. The IHF maintains that radical changes to Ireland's economic and regulatory environment over the past century have made the JLC system obsolete, particularly in light of the National Minimum Wage Act 2000 which has provided Ireland with the second highest gross minimum wage in Europe. Employment law should be created by legislation introduced by the Oireachtas and should apply to all employments and not be created by organisations such as the Joint Labour Committees or the Labour Court.

9. Removing unnecessary barriers to travellers and introduce a common visa area for Ireland and Britain.

10. Restoring detailed tourism data collection which is vital for planning.

11. Maintaining the over 66 free rail travel scheme for tourists on Iarnrod Eireann and remove the unnecessary requirement for a limited period trekker ticket.

1. Supporting Hotels and Guesthouses to Survive the Recession

The Irish tourism and hotel/guesthouse sectors are in a crisis situation. This has been caused by a combination of collapse in the domestic and international tourism markets, the failure of the banking system to provide adequate credit, the very high cost of doing business in Ireland and excess growth in hotel capacity in recent years. Ultimately economic growth will resume and it is essential to national economic recovery that Ireland's tourism sector is well positioned to take advantage of the ending of the international recession in 2010 and the anticipated resumption of Irish growth in 2011.

While it may seem optimistic to be talking of tourism growth in the context of the truly appalling position of 2009 and 2010, we must recognise that the medium and long term potential of the Irish tourism sector is strong if we are to get through the present difficulties and if Government introduces the appropriate supportive policies. While the current emphasis is on survival, the medium and long term emphasis will be on employment growth and activity growth. This will require that the "Ireland" marketing presence in international markets must be maintained, that solid tourism enterprises and entrepreneurs must not be lost to the economy through short-term financial difficulties and that the budget must improve competitiveness particularly through reductions in local authority commercial rates and energy costs and assist the adjustment to sustainable levels of hotel capacity.

The IHF submissions on recent budgets emphasised the competitiveness pressures facing the sector with high domestic labour and input costs, high minimum and regulated wages and the high cost of energy and public services such as local authority rates, water and sewage. In addition, the sector has had to operate with a very strong exchange rate in its two main markets. The sector managed to cope with these difficulties through cost management, reduced profits and good market conditions. The collapse in the tourism market has removed the main bulwark against the high cost of doing business in Ireland. We must as a matter of urgency improve our cost competitiveness. Enhanced competitiveness must be an element of Budget 2011 and public sector prices and charges should be frozen at 2009 levels.

Unfortunately, Government determined costs and prices have not followed the general private sector and hotel sector trends. Many public sector charges continue to increase (in some cases new charges are being introduced e.g. the PSO levy on electricity supplies) and there has not been a programme of reductions in these charges and prices. Hotels and guesthouses have had to reduce costs and many have achieved substantial savings through higher efficiencies and productivity coupled with better procurement procedures. We call on Government to follow the examples of the private sector in reducing its prices and charges. The biggest single cost over which hoteliers and guesthouse owners have no control is local authority rates. Prior to the enactment of The Valuation Act 2001 businesses could seek a revision of their rateable valuations on a number of grounds, including a deterioration in the profitability of the business. The 2001 Act removed this method of seeking relief on the basis that the legislation envisaged that every rateable property in the country would have its valuation revised every five to ten years.

It is now nine years since the 2001 Act came into force and only three of the 88 rating areas in the country have had revisions carried out by the office of the Commissioner of Valuation. At this rate it will take over twenty years to complete the process in all rateable areas, notwithstanding the intention in the legislation that the revised valuations would be further revised every five to ten years.

The revisions which have been completed have resulted in the local authority rates liability of hotels being reduced by on average, more than 30%. Based on this experience it is reasonable to suggest that if the revisions were completed in the remainder of the country similar results would be achieved. In the meantime hoteliers are being forced to pay excessive rates particularly at a time of very difficult trading circumstances.

We believe that Budget 2011 should include an instruction to all local authorities in which a revision of rateable valuations has not been completed to introduce a scheme to waive 30% of rates on hotels and guesthouses

There should be no increases in tourism related taxes and charges.

The Government contribution to marketing should ensure that the level of marketing activity is increased in real terms. In addition there should be support for specific marketing drives to reverse the collapse in the arrival numbers from Britain and to attract corporate conference business in order to maximise the benefits from the opening of Convention Centre Dublin.

Cost competitiveness is a key issue and the policy framework has been too slow in recognising this. Tourism is an international industry competing in the global market for both domestic and overseas tourists. The international economic slowdown has intensified competition. Competitiveness is determined by a wide range of factors including taxation, costs, prices and marketing. Marketing and costs are the two aspects which can quickly respond to policy measures.

The Government should play its part in the immediate task of ensuring the survival of the hotel/guesthouse sector in its Budget 2011 strategy by:

1. Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland international marketing budgets and initiating specific additional marketing activity to attract new business/conference visitors to derive maximum benefit from the availability of Convention Centre Dublin. Marketing activity is a main determinant of market share. Irish tourism cannot depend on growth in international markets. We must aim to increase our market share of the smaller international market.

2. Avoiding any tax increases in tourism related products and services at national and local levels, introducing a four year freeze on all public sector charges at the 2009 level.
3. The Government should instruct all local authorities in which a revision of rateable valuations has not been completed, to introduce a scheme to waive 30% of rates on hotels and guesthouses.
4. The Government should immediately remove the air travel tax. As an island destination, the range, cost and quality of access to Ireland is absolutely critical to overseas tourism and its export earning potential.
5. Renewing the employment subsidy available to the hotel/guesthouse sector when it expires in November of this year
6. Ensuring the availability of appropriately priced credit to the hotel/guesthouse sector and establishing a bank for reconstruction and development.
7. Facilitating the orderly reduction of excess capacity through adjustment of the tax regulations concerning tax allowances for hotel development, including the facilitation of change of use and ensuring that planning issues do not inhibit this capacity reduction.
8. Abolishing the JLC system of establishing wage rates to encourage competitiveness and support commercial viability.
9. Removing unnecessary barriers to travellers and introduce a common visa area for Ireland and Britain.
10. Restoring detailed tourism figures from the Central Statistics Office which are vital to efficient marketing and planning.
11. Maintaining the over 66 free rail travel scheme for tourists on Iarnrod Eireann and removing the unnecessary requirement for a limited period trekker ticket.

The IHF recognises that the Government's finances are in a very difficult position in 2011 and later years and supports strong efforts to correct the imbalances. Adjustments in the public finances are needed to reduce borrowing and to generate the resources which will provide stimulation to the economy including tourism. Consideration of the Exchequer costs of tourism development should also take into account the resulting economic and social benefits and the flows of taxation revenue which accrue to the Exchequer from tourism. Tourism is a good investment for the Exchequer and generates taxation revenue flows which are very substantially in excess of the Exchequer costs. The IHF is confident that the tourism related Exchequer payback provides better value for money that many other economic development/industrial development and other related expenditures.

Without sustainable economic activity there will be no lasting economic recovery. Economic activity and economic growth which will generate employment requires a strong enterprise sector of which tourism is a very essential part. A failure to support tourism with well justified evidence based expenditure and other polices will reduce the possibility of economic recovery. Consequently the IHF calls for support measures within the overall context of recognising the need to reduce public expenditure and borrowing.

2. The Economic Role of Tourism

Tourism and the hotel and guesthouse sector are substantial national economic resources and have invested in skills, marketing, technology, products and services and physical facilities. Despite the substantial recent decline in tourism it continues to contribute greatly to Irish economic activity. The main economic contributions of the tourism industry in 2009 include

- €3.9B in foreign exchange earnings.
- 6.6m overseas visitors.
- Domestic tourism expenditure of €1.4B.
- The Exchequer received €1.3B in taxation from tourism or 3.7% of total taxation revenue.
- Tourism accounted for 3.8% of GNP and 2.5% of Gross Value Added.
- According to Fáilte Ireland data the hospitality industry accounts for 190k full-time, part-time and seasonal jobs.
- Provides regional economic activity to a greater extent than most other industries.
- Generates 2.6% of total exports.
- Provides a substantial entrepreneurial resource as the vast majority of tourism enterprises are small and medium enterprises.

Despite the recent severe difficulties tourism remains a large, strategically important industry and employment generator which is deeply embedded in the Irish economy and should be supported in Budget 2011 to stem the continuing trend of increasing unemployment and the resultant burden on the exchequer.

Of particular significance is the potential future role of international tourism in economic recovery. Future economic growth will be more focused on export activity including the attraction of foreign tourists rather than domestic demand as has been the case in recent years. Despite its present difficulties tourism is very well placed to support export led growth. With a cost competitive economy and good international promotion, the tourism industry is capable of substantial and rapid growth relative to other export sectors.

3. Very Weak Economic Environment in 2010 and 2011

3.1 Economic Growth in 2010 and 2011

There will be a small international recovery in 2010 following the decline of 2009 and this recovery is expected to continue in 2011. However, there continues to be great uncertainty and there remains a strong possibility of a weaker economic performance in 2011. This particularly applies to the two main markets of the USA and the UK. Unfortunately, consumption growth, which is a determinant of tourism activity, is expected to be less than GDP growth in most economies. Despite the uncertainties, 2011 should be a better international environment for Irish tourism than the previous three years. The proposed Budget 2011 measures will help position Irish tourism to take advantage of the improved demand conditions.

In those economies of particular relevance to Irish tourism there will be growth of between 2% and 3%. As shown below, the May 2010 OECD projection is for 1.8% growth in the Euro area in 2011. UK growth will be 2.5% and USA growth will be over 3%.

Table 1 International Economic Growth 2009, 2010 and 2011

GDP GROWTH %	2009	2010	2011
USA	-2.4	3.2	3.2
UK	-4.9	1.3	2.5
FRA	-2.5	1.7	2.1
GER	-4.9	1.9	2.1
ITA	-5.1	1.1	1.5
NETH	-4.0	1.2	2.0
EURO	-4.1	1.2	1.8

Source OECD May 2010

In the buoyant Irish economy prior to 2008 the hotel sector had become increasingly reliant on the domestic market. Two thirds of hotel bednights and a higher proportion of other hotel activities are accounted for by the domestic market. Economic growth and consumer demand growth prospects for Ireland for 2010 and 2011, despite an improvement on performance in 2008 to 2009, are relatively weak. The range of different forecasts is shown below. While 2010 will be an improvement on 2009 the current views range between very small increases or very small declines in economic activity.

The most optimistic forecast expects a growth of 1% in both GDP and consumer expenditure in 2010.

Table 2 Irish growth projections 2010 and 2011 % Volume

	GDP 2010	GDP 2011	CONSUMER EXPEND 2010	CONSUMER EXPEND 2011
ESRI	0.25	2.75	0.25	1.5
IMF	-0.6	2.3	-1.4	0.9
OECD	-0.7	3.0	-2.7	0.6
CENTRAL BANK	0.8	2.8	-1.2	0.9
DAVY STOCKBROKERS	1.0	4.2	1.0	4.0

Source: Various organisations.

The 2011 performance is expected to be much better. The most optimistic forecasts expect a 4.2% growth in GDP and a 4% growth in consumer expenditure. This would be a very welcome change from the 2008 to 2010 period. However, most forecasts for 2011 are less optimistic. The IMF, OECD and Central Bank all expect Irish 2011 consumer expenditure growth to be less than 1%.

3.2 Economic Prospects in the Medium Term

Even with a resumption of growth in 2011 the level of Irish economic activity will be lower in 2014 than it was before the economic collapse in 2007. Based on IMF assessments it will be about 2016 before the GNP levels of 2007 are reached again. Consumer expenditure (in volume terms) which is a major determinant of domestic demand for hotel services and other businesses) will be lower in 2014 than in 2007. The Government's own medium term projections while higher than the IMF also broadly indicate that it will be several years before the 2007 levels of employment, GNP and consumer expenditure will be realised.

The Government must aim for a higher medium term growth than is currently expected to deal with unemployment, emigration, public finances and living standards issues. This will be very difficult and will require improved competitiveness and an enterprise friendly environment.

One of the most likely sectors for achieving higher growth will be international tourism. Budget 2011 must provide the foundations to achieve this growth. While continuing to deal with the public financial imbalances, Budget 2011 should begin a clear strategy of achieving higher growth over the next several years.

3.3 Cost Environment

A range of national and international organisations has identified the high cost of operating a business in Ireland including Forfas, IMF and the ESRI. The current recession will restore some competitiveness through price and cost declines but this is unlikely to go far enough. Current estimates and forecasts are for very modest declines in 2009 and 2010. The current ESRI forecast for 2010 is a decline of 0.5% in the CPI compared with 2009 with an increase in 2011 of 1.75%. The CPI includes the effect of mortgage rates. The EU HICP measure is a better measure of the cost of goods and services. Overall, this is expected to decline by only 1.5% in 2010 and will increase by 0.25% in 2011. Wage growth is expected to be -2.0% in 2009, -3.0% in 2010 and -1.0% in 2011. These changes will not be sufficient to regain lost cost competitiveness. The required adjustment is in the range of 20%. Government must not depend on market forces and the recession to improve cost competitiveness. Budget 2011 must directly focus on improving cost competitiveness.

Government can begin this process by freezing all its own charges and by reversing the announced 5% increase in electricity charges. The priority must be the immediate economic crisis rather than medium or longer term issues.

Commercial rates continue to be an excessive burden on the sector. In 2010 councils began to appreciate to a greater extent, the burden which rates impose but the response was inadequate. In the county councils and city councils the average multiplier decrease was 0.62% with just over half of councils introducing a no change multiplier and just less than half introducing small decreases. This contrasts with the substantial decline in hotel revenues and prices. A much more radical response is needed.

The entire commercial rates system is inappropriate and penalises business. There is no effective method of revising rateable valuations to take into account major worsening of economic circumstances, returns on property or the ability to pay of enterprises which are at the mercy of the monopoly power of local authorities. As an immediate step the Government should introduce a country wide 30% reduction in Local Authority rates applicable to hotels and guesthouses.

Based on the pace of completing the revisions of the rateable valuations since the coming into effect of the Valuation Act 2001 in April 2002 it will take over twenty years to complete the revision process country-wide and this is without making any provision for the review of the revised valuations which the act requires to be carried out every five to ten years.

3.4 Labour Costs

As shown by the National Competitiveness Council and other organisations Ireland is a high cost economy in terms of business costs. Labour costs levels are also high.

The hotel industry is particularly vulnerable to labour cost increases. The industry is very labour intensive and as a services industry there is less scope for productivity improvements than in manufacturing. In addition it is an exposed sector competing in competitive international markets. Its domestic and international customers have a wide variety of alternative holiday destinations and experiences, often in low cost locations.

The hotel industry includes a substantial proportion of low wage occupations. This is a feature of the production processes in the industry and is an international phenomenon. The industry is particularly vulnerable to changes in wage rates at the lower level. Ireland has the second highest minimum wage in the EU and is substantially higher than several countries. This issue is worsened by the operation of the Joint Labour Committees (JLC) system to which part of the industry is subject. The JLC imposes statutory wage levels which are effectively minimum wages higher than the official minimum wage and also imposes other legally binding conditions of employment to which other economic sectors are not subject. Apart from adjustments to premium payments, the current regulated and statutory wage rates do not reflect the dramatic worsening of the business performance and operating environment of the hotel sector since 2008.

The Hotel Industry Survey illustrates the growing share of labour costs relative to turnover and the very large increase in 2009. The 2010 Survey for Ireland and Northern Ireland lists the 2009 share at 42.3% which is up from 32.2% in 1999 and 35.4% in 2004. When the Northern Ireland figure (33.1%) is removed the figure for the Republic is over 43%.

Table 3: Payroll Cost Relative to Turnover (Hotels) (%)

1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
32.2	33.3	32.4	34.2	35.6	35.4	37.6	37.6	38.8	40.0	42.3

Source: Ireland and Northern Ireland Hotel Industry Survey

The hotel sector has made a major effort to reduce its labour cost base. This is necessary to cope with the new market and economic realities. However, its efforts are severely curtailed by the operation of the statutory Joint Labour Committee system of wage determination and by the level of the minimum wage. The IHF calls on the Government to abolish the JLC system of age determination as an important element of a tourism recovery plan.

3.5 Public Finances Crisis

The IHF is acutely conscious that its Budget 2011 proposals impose a burden on the exchequer at a time when the public finances are in dire straits. We agree with the Government that the borrowing level must be reduced. We also accept that proposals such as increased marketing allocation and reduction in commercial rates add to the Exchequer burden. We recommend that the primary approach to correcting the public finances should be the reduction of current expenditure. Additional taxes will be necessary but these should be designed so as not to reduce incentive and to avoid any negative impact on tourism and general competitiveness. The reductions in expenditure should be sufficiently large to support the borrowing reduction and also to make available finance for economic stimulation measures. The McCarthy and Local Government Review reports provide much scope to reduce expenditure. The IHF argues that there are more savings possible from Local Government than recommended in the report.

3.6 Financing and Banking Crisis

The hotel sector is in a very difficult financing crisis. Revenues have been squeezed by the combination of lower prices, excess capacity and low capacity utilisation rates. Costs have not significantly reduced. Consequently, margins are under severe pressure. The unexpected and large decline in financial viability has generated a need for increased bank finance to survive the hopefully short term recession. This need for increased finance has coincided with the very severe banking and credit crisis. Consequently hotels and guesthouses are finding it difficult to obtain adequate levels of bank finance.

The financing crisis for hotels requires a fivefold response from policymakers.

- An orderly reduction of capacity should be facilitated through adjustment of the claw-back regulations attached to capital allowances for hotel development. Currently the tax allowance clawback provision is a barrier to the reduction in capacity. Planning regulations should not be allowed to be a barrier to this capacity reduction.

- The public sector determined cost environment for hotels must be improved, including an immediate reduction of 30% in commercial rates.

- Adequate levels of credit should be made available on a risk sharing basis with banks and/or direct lending by Government using the banking system as an agent. A credit guarantee scheme or equivalent should be introduced. In addition, as part of the medium term higher growth strategy a new bank for reconstruction and development should be established which would be directed at the SME sector. The UK Enterprise Finance

Guarantee Scheme is a useful model for initiating a loan guarantee scheme in this country. Details of this scheme are shown in Appendix 1.

- Tax incentives should be introduced to support new equity investment in existing hotels to reduce the level of borrowing.
- The operations of NAMA should be designed to ensure that unfair market distorting competition should not arise from hotel assets under NAMA control.

Because of the increased risk environment for hotels it is hardly surprising that the credit situation for hotels is weak. However, it is not economically efficient to allow short term financial difficulties to destroy part of the tourism infrastructure. The loan guarantee scheme operated by the UK Government offers the basis for such a scheme in Ireland.

4 Performance of the Hotel and Guesthouse Sector

The commercial basis of hotels has deteriorated over recent years. The average profit rate declined from 17.8% in 2005 to 10.4% in 2009. Profit does not include depreciation, bank loan interest or rent where relevant. The figures refer to averages of hotels and many hotels operate at lower profit margins. Between 2008 and 2009 the before tax profit per room dropped from €7,056 to €4,650.

Table 4: Hotel Sector Profit Performance 2005-2009

	2005	2006	2007	2008	2009
Profit Before Tax per Room	€10,238	€9,786	€9,308	€7,056	€4,650
Profit Before Tax per Room (%)	17.8%	16.6%	15.5%	12.8%	10.4%
Room Occupancy Average	68.9%	69.8%	69.7%	63.5%	59.4%
Total Revenue per Room	€57,640	€59,107	€59,968	€55,116	€44,798

Source Ireland and Northern Ireland Hotel Industry Survey and IHF

The combination of increased capacity and the recent decline in the market has substantially reduced hotel occupancy rates. These lower occupancy rates are being achieved only with lower prices. As seen above, the revenue per room declined from €55,116 to €44,798, a decline of 18.7%. The room occupancy rate dropped from 70% in 2007 to 64% in 2008 and to 59% in 2009. Between 2008 and 2009 the revenue per room declined from €55,516 to €44,798. It should also be noted that these statistics are based on a survey with greater participation by larger better performing hotels. When account is taken of the results of the broader survey carried out by Failte Ireland, which shows that room occupancy fell from a high of 64% in 2007 to 58% in 2008 and 55% in 2009, the lowest room occupancy rate since the early 1980s, the financial performance of the overall industry is even worse.

The hotel sector has made great efforts to reduce costs. In 2008 the operating cost per room was €48,060 and this declined to €40,148 in 2009, a decrease of 16.5%. We recognise the need to achieve additional permanent cost reductions to achieve the competitiveness necessary for a sustained tourism recovery but this effort is constrained by the existence of statutory wage rates set by the JLC system. This system is not appropriate for the new economic and market conditions. It is hindering the enhancement of competitiveness and should be abolished.

Price reductions have become a dominant strategy within the sector. In 2010 the average room rate was €77.81 compared with €88.25 in 2008, a decline of 11.8%. The 2007 rate was €97.69.

In the first six months of 2010 the hotel room occupancy rate increased from 51% in 2009 to 54% in 2010. The occupancy rate is still well below the pre 2008 level. This has been caused by a slight decrease in capacity and a demand increase generated by price discounting.

Table 5: Hotel Room Occupancy Rates % Jan - June 2009 and 2010

	Jan - June 2009	Jan - June 2010
Hotels	51	54
Guesthouses	40	40

Source Failte Ireland

As shown in Table 6 there has been a large decrease in the number of overseas visitors in the first six months of 2010 following the earlier substantial decreases in 2009.

Table 6: Overseas Tourism Performance (Visitors k), Jan-June 08 to 10

	Jan/June 08	Jan-June 09	Jan-June 10	% change 09/10
Total Overseas Visitors	3702	3304	2626	-20.5
Visitors from Great Britain	1873	1580	1229	-22.2

Source: CSO

In the first six months of 2010 compared with 2009 total overseas visitors decreased by 20.5%. The decline in visitors from Great Britain was 22.2% over this period. This is particularly worrying as the British market continues to be the largest national market for Irish tourism.

Table 7 shows the domestic market performance in 2008 and 2009. The total number of trips was constant but holiday trips and holiday nights declined greatly. While the number of trips to hotels did not decline, the number of bednights associated with the trips declined by 2.3%.

Table 7 Domestic Market Jan-Mar 2008and 2009 (k)

	2008	2009
Domestic Trips	8,339	8,340
Holiday Trips	4,398	4,037
Domestic Nights	26,195	26,027
Holiday Nights	15,654	14,320
Hotel/Conf. Centre		
Trips	3,430	3,443
Nights	7,616	7,438

Source: CSO

The 2010 Tourism Barometer (Wave 2 June) notes that 47% of hotel and 74% of guesthouse proprietors reported a decrease in business volume for the first half of 2010 compared with 2009. 30% of hotels reported an increase in business volume. The situation for guesthouses was worse with only 11% of guesthouses reporting an increase. 57% of hotels reported a decline in overseas business compared to 33% reporting a decline in domestic business. 23% of hotels reported an increase in overseas business. It should be noted that the 2009 volume of business was very low due to the severe national and international economic declines.

Table 8 Performance Jan-June 2010 Relative to 2009

% of Respondents	Up	Same	Down
Hotels	30	21	47
Guesthouses	11	14	74
Hotels Overseas Market	23	20	57
Hotels Domestic Market	38	28	33
Hotels Northern Ireland Market	9	39	49

Source: Fáilte Ireland Tourism Barometer 2009, Wave 1

In comparing 2010 average room yield with 2009 for hotels, Barometer Respondents reported a decline in 83% of cases with only 7% having an increase.

5 Budget Policy to Support Hotels and Guesthouses

5.1 Context

The IHF Budget proposals are designed to support the survival of the hotel/guesthouse sector in a period of enormous economic crisis and to prepare it to contribute to a medium and long term strategy of higher economic growth than is currently envisaged. As noted in last year's IHF budget submission the proposals are consistent with the "survival action" recommendations of the Report of the Tourism Renewal Group which covered investment in marketing, reduction in access costs, prioritising of public spending on tourism and the support of sustainable enterprises. The proposals take into account:

- The likely weak (but better than 2009) 2010 and 2011 domestic and international economic situations.
- The weak cost competitiveness of the economy which is in part generated by public sector charges and prices.
- The substantial burden of commercial rates on hotels and guesthouses.
- The large economic contribution of tourism.
- The role that tourism and the hotel sector can play in economic recovery after the recession when growth will have to be higher than is currently envisaged.
- The value for money return on investment in tourism.
- The substantial and rapid negative changes in the financial/business model of hotels and guesthouses since 2008.
- The large increases in hotel capacity and the sector's vulnerability to the recent significant decline in tourist numbers.
- The current crisis situation in the sector.

The hotel sector had geared itself to cope with the volume of demand generated by the buoyant domestic economic activity and good international performance despite its ongoing cost and competitiveness concerns. Consequently, many hotels and also guesthouses are highly leveraged. The business outlook for hotels and guesthouses has quickly and dramatically worsened since 2008. The business and finance model which operated before 2008 is now not relevant or appropriate. Capacity utilisation rates have declined, business volume has collapsed and accommodation prices have fallen greatly. Costs continue to increase despite the best efforts of the hotel sector to reduce those costs which are within its control.

The individual well managed hotel or guesthouse is currently facing and will continue to face decreased revenues and the expected high costs on many inputs. This threatens the viability of the business and generates a need for additional short term financial facilities while adjustments are made to take into account the new commercial realities. Unfortunately, the banks are generally unwilling to facilitate this.

5.2 The Budget Proposals

It is essential for the future strength of the hotel/guesthouse sector that Budget 2011 reduces the burden imposed by penal public sector charges and local taxes, that cost competitiveness is promoted vigorously and the capacity and credit problems of the sector are addressed. While not specifically a budgetary matter the IHF continues to urge that NAMA should be operated in a way which does not distort the operation of the hotel market either through below cost prices of NAMA operated hotels should this arise or inappropriate disposal of assets.

The IHF proposes the following measures to support the survival of the sector and to ensure that the industry will be ready to avail of the international and national economic recovery in 2011. These measures complement the efforts being undertaken by the tourism and hotel sectors. The strategic policy and sectoral objectives for tourism must be to survive the recession and thereafter begin to increase its market shares of both domestic and international tourism. Budget 2011 can begin this process by:

- Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland international marketing budgets and initiating specific additional marketing activity such as to attract new business/conference visitors to derive maximum benefit from the availability of Convention Centre Dublin and to regain lost ground in the British market. Marketing activity is a main determinant of market share. Irish tourism cannot depend on growth in international markets. We must aim to increase our market share of the now smaller international tourism market. The British market should be prioritised for the immediate future to reflect its importance to Irish tourism and the current substantial decline in the number of British visitors in 2009 and 2010.
- Avoiding any tax increases in tourism related products and services at national and local levels, introducing a four year freeze on all public sector charges at the 2009 level and reducing local authority rates by 30% for 2010. The recently announced increase in electricity charges should be cancelled and priority should be given to the immediate economic crisis and the need to enhance competitiveness and reduce costs.

- Immediately removing the air travel tax. As an island destination, the range, cost and quality of access to Ireland is absolutely critical to overseas tourism and its export earning potential.
- Renewing the Employment Subsidy Scheme available to the hotel/guesthouse sector which is due to finish in November.
- Ensuring the urgent availability of appropriately priced credit to the hotel/guesthouse sector and establishing a bank for reconstruction and development.
- Facilitating the orderly reduction of excess hotel capacity through adjustment of the tax regulations concerning tax allowances for new hotel and ensuring the planning process and regulations are not a barrier to capacity reduction.
- Abolishing the JLC system of establishing wage rates to encourage competitiveness and support commercial viability. The IHF maintains that radical changes to Ireland's economic and regulatory environment over the past century have made the JLC system obsolete, particularly in light of the National Minimum Wage Act 2000 which has provided Ireland with the second highest gross minimum wage in Europe. Employment law should be created by legislation introduced by the Oireachtas and should apply to all employments and not be created by organisations such as the Joint Labour Committees or the Labour Court.
- Removing unnecessary barriers to travellers and introducing a common visa area for Ireland and Britain.
- Restoring detailed tourism figures from the Central Statistics Office which are vital to efficient marketing and planning.
- Maintaining the over 66 free rail travel scheme for tourists on Iarnrod Eireann and removing the unnecessary requirement for a limited period trekker ticket.

Appendix 1: Details of UK Enterprise Finance Guarantee Scheme

UK DEPARTMENT OF BUSINESS, INNOVATION AND SKILLS

TITLE	**'ENTERPRISE FINANCE GUARANTEE'**
Main Criteria	Viable business proposals that have tried and failed to obtain a conventional loan because of lack of security.
Sectors	Most sectors qualify with some specific exclusions including coal, real estate, agriculture and insurance.
Funding of	Investment funding, working capital & bolstering security value for a broad list of eligible purposes
Borrowers	Start up or established Turnover limit of £25m max.
Term	3 months up to 10 years
% Guarantee	75% of loan amount is guaranteed by U.K. Government as part of Solutions for Business Portfolio
Guarantee Limit	Maximum of £1m loan exposure
Guarantee Fee	2% premium payable by borrower on the outstanding balance of the loan
Service Fee	Not applicable. Lenders may charge an arrangement fee
Loan Rates	Lenders charge normal margins for SME lending.
Appraisal	Approved lenders apply normal commercial criteria
Refinancing	Refinancing is allowed where security value has diminished or serviceability is in doubt.
Security	Lender is expected to take its normal security including Personal Guarantees
Realisation	Claims under the guarantee can only be made after all security has been realised.
Size of Fund	£1bn Fund designed to support up to £1.33bn of new lending by banks
Other Comments	Bank switching is not precluded but is subject to strict rules. EFG is not an equity substitute and promoters must contribute equity and processing target of 20 days.