IRISH HOTELS FEDERATION

SUBMISSION

to the

MINISTER FOR FINANCE

BUDGET 2012

HOTELS AND GUESTHOUSES SUPPORTING ECONOMIC RECOVERY

September 2011

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ONE PAGE SUMMARY

The number of overseas visitors increased by 12.7% in the first half of 2011. This is the first welcome sign of a return to tourism growth following the declines of recent years and illustrates the strong potential role that tourism can play in economic recovery if a supportive policy environment is implemented. The IHF strongly welcomes the tourism related policy measures in the May Jobs Initiative. The IHF also welcomes the recognition by Government of the potential of tourism for generating economic recovery. Despite these positive developments, the hotel and guesthouse sector still suffers from the substantial problems which previous submissions have identified. These must be dealt with if the potential of the sector is to be realised. There is large over capacity of hotels. The market remains well below the pre economic crisis level despite the 2011 growth. The increased numbers in 2011 compared to 2010 are mainly due to the negative effects of the disruption caused by the volcanic ash in spring 2010. Revenue per room in 2010 has continued the decline of recent years. The availability of credit to the sector is very constrained. Many hotels are not commercially viable because of the costs and revenue situation and the overhang of debt. The commercial sustainability of the sector continues to be threatened by unfair competition from non viable bank controlled hotels offering uneconomic prices. Many hotels have gone into receivership or come under bank/NAMA control and many more will follow in the absence of appropriate policies. NAMA continues to cast a layer of uncertainty over the sector. In addition, recent renewed international macroeconomic uncertainty will negatively affect inward tourism.

The Government should play its part in the task of maximising the contribution of the hotel and guesthouse sector to economic recovery in Budget 2012 by:

1. *Increasing the real level of funding for Fáilte Ireland and Tourism Ireland's marketing budget.*
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 2010 level.*
3. *Reducing energy costs and reducing local authority rates by 30%. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.*
4. *Ensuring the availability of appropriately priced credit, the introduction of limited incentives to encourage debt restructuring schemes in existing hotels and the establishment of a bank for reconstruction and development.*
5. *Facilitating the orderly reduction of excess 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.*
6. *Allowing the JLC system to disappear without introducing a replacement system.*

EXECUTIVE SUMMARY

The 2011 tourism performance will be a substantial improvement on 2010. Despite this the hotel and guesthouse sector continues to experience many of the same serious economic problems which have been referred to in previous submissions including large debt burdens, unfair competition from bank-controlled and insolvent non-viable hotels, severe lack of credit, surplus capacity, low profitability, uneconomic prices and high costs by international standards. As stated in previous budget submissions the sector is in a crisis situation. The Irish economy which determines the domestic tourism segment continued to perform weakly in 2010 and 2011 and only very modest growth in consumer expenditure is expected in 2012. The international economy will grow in 2011 and 2012 with a Euro area growth of about 2% in each year. Of great concern to the IHF is the expectation that even with Irish economic growth resuming in 2011, the 2007 volume of Irish consumer expenditure and economic activity will only be regained by about 2014 or 2015 according to Government projections.

IHF is appreciative of Government efforts and initiatives such as the tourism VAT reduction, the support for marketing and the reduction of the air tax but much more needs to be done.

The difficulty of 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. The hotel and guesthouse sector is currently facing low levels of demand (despite the visitor increase in 2011), 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. Many leading hotels have gone into receivership or come under bank/NAMA control and the sector faces unfair competition from bank controlled hotels operating on a cash flow basis with commercially unsustainable prices.

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. Two thirds of hotel bednights in 2010 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 the ambitious medium term economic growth strategy which is clearly needed in the Irish economy.

The current tourism and hotel positions are weak:

- International visitors increased by 12.7% in the first six months of 2011. The increased numbers in 2011 compared to 2010 are mainly due to the negative effects of the disruption caused by the volcanic ash in spring 2010. The number of international visitors in the first six months of 2011 was 10.4% less than 2009.
- Domestic holiday nights increased between 2010 and 2011.
- The average room rate declined by 5.5% in 2010 following declines of 11.8% in 2009 and 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 was 22% lower in 2010 than in 2008.
- Profits per room declined in 2010 which was only 60% of the 2008 level.
- 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 or are under the control of banks or NAMA and more will follow.
- Hotel occupancy rates increased in 2010 and 2011 but remain at low levels. These lower occupancy rates are being achieved only with lower prices.
- The Failte Ireland Tourism Barometer for the first half of 2011 reported that 43% of hotels and 30% of guesthouses had experienced an increase in the number of bednights compared with 2010. This is a substantial improvement on the previous year.
- In the first six months of 2011 the hotel room occupancy rate increased from 49% to 51% but it is still low by previous standards.
- While lower prices are desirable to promote tourism the current room rates are not commercially sustainable alongside the Irish cost base.

While some of the negative factors affecting the hotels sector are beyond the control of the government such as the international economic situation, Budget 2012 is capable of substantially improving the tourism and hotel/guesthouse situation. It can sustain and consolidate the tourism resource and enhance competitiveness.

The strategic policy and sectoral objectives for tourism must be to grow rapidly to contribute to economic recovery by increasing its market shares of both domestic and international tourism.

Budget 2012 can begin this process and should address the following areas by:

1. Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland's marketing budget 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 the national conference centre. Attention should also be given to developing integrated regional tourism products in conjunction with the industry to address regional imbalance. Marketing activity is a main determinant of market share. 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, introducing a four year freeze on all public sector charges at the 2010 level.
3. Reducing energy costs and reducing local authority rates by 30% for 2011. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.
4. Ensuring the availability of appropriately priced credit to the hotel/guesthouse sector, the introduction of limited incentives to encourage debt restructuring schemes in existing hotels and the establishment of an SME bank for reconstruction and development.
5. 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.
6. Allowing the JLC system of establishing wage rates to disappear without the introduction of any replacement system.The IHF maintains that 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 and the vast amount of other employment legislation.

1. IHF Welcomes Recent Tourism Initiatives

IHF welcomes the priority being given to tourism by the Government. In particular we welcome the recent tourism initiatives including the VAT reduction, the air tax reduction, the support for tourism marketing and the visa reform. In addition the recent visits by the British monarch and the US president have raised the profile of Ireland. We believe the hotel and guesthouse sector has great potential to support economic recovery but that potential will be achieved only if appropriate policy measures are taken, beginning with Budget 2012, which will support the measures already introduced.

2. Hotels and Guesthouses and Economic Recovery

The Irish tourism and hotel/guesthouse sector is in a crisis situation despite the recent positive policy measures and the resumption of growth in 2011. 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. It is essential for national economic recovery that Ireland's tourism sector is well positioned to take advantage of the continuation of growth in the international economy and the modest resumption of Irish growth in 2012.

The medium and long term potential of the Irish tourism sector is strong if we get through the present difficulties with most enterprises intact and if Government introduces the appropriate supportive policies. The achievement of substantial tourism growth requires that the "Ireland" marketing presence in international markets must be enhanced, 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 that the economy adjusts 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. In the past, 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 2010 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 were 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 ten years since the 2001 Act came into force and only three of the 88 rating areas in the country have had the 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.

The 2012 budget 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. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.

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 a specific marketing drives to attract corporate conference business in order to maximise the benefits from the National Conference Centre and develop integrated regional tourism products in conjunction with the industry to address regional imbalance. 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.

Cost competitiveness is a key issue and the national 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, productivity, management, cost and 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 potential of the hotel/guesthouse sector in its Budget 2012 strategy by:

1. Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland international marketing budget and initiating specific additional marketing activity to attract new business/conference visitors to derive maximum benefit from the availability of the national conference centre. Attention should also be given to developing integrated regional tourism products in conjunction with the industry to address regional imbalance.

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 2010 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. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.

4. Ensuring the availability of appropriately priced credit, the introduction of limited incentives to encourage debt restructuring schemes in existing hotels/guesthouses and the establishment of a bank for reconstruction and development.

5. Facilitating the orderly reduction of excess capacity through adjustment of the tax regulations concerning tax allowances for hotel development including the facilitating of change of use and ensuring that planning issues do not inhibit this capacity reduction.

6. Allowing the JLC system of establishing wage rates to disappear without introducing any replacement structures or system, to encourage competitiveness and support commercial viability.

IHF recognises that the Government's finances are in a very difficult position in 2012 and future 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. IHF is confident that the tourism related Exchequer payback provides better value for money than 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 require 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.

3. Continuing Weak Economic Environment in 2011 and 2012

3.1 Economic Growth in 2011 and 2012

There was a modest international economic recovery in 2010, with a Euro area growth of 1.7% following the decline of 2009. This recovery is expected to continue in 2011 and 2012. However, in recent months there has been an increase in uncertainty due to the international sovereign debt and banking problems. The OECD May 2011 projections shown below are likely to be revised downwards when the next set are published in November. Despite the uncertainties, 2012 should still generate moderate economic growth.

In those economies of particular relevance to Irish tourism there will be 2012 growth of between 2% and 3%. As shown below, the May 2011 OECD projection is for 2.0% growth in the Euro area in 2012. UK growth will be 1.8% and USA growth will be just over 3%. The principal mainland EU markets for Incoming tourists will grow by between 1.6% and 2.5%. The performances of Germany and the Netherlands will be lower in 2012 than in 2011. As noted above recent uncertainties will lower these performances. The extent of the downward revisions will depend on forthcoming measures to reassure financial markets on sovereign debt. Consumption volume growth will perform worse than GDP internationally. The expected 2012 consumption volume growths are Germany 1.4%, France 1.9%, Italy 1.2%, Netherlands 1.3% and UK, 1.1%.

Table 1 International Economic Growth 2009, 2010, 2011 and 2012

GDP GROWTH %	2009	2010	2011	2012
USA	-2.6	2.9	2.6	3.1
UK	-4.9	1.3	1.4	1.8
FRA	-2.7	1.4	2.2	2.1
GER	-4.7	3.5	3.4	2.5
ITA	-5.2	1.2	1.1	1.6
NETH	-3.9	1.8	2.3	1.9
EURO	-4.1	1.7	2.0	2.0

Source OECD May 2011

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. As shown below total domestic demand will perform poorly in 2012.

Table 2 Irish growth projections 2011 and 2012 % Volume

	GDP 2011	GDP 2012	CONSUMER EXPEND 2011	CONSUMER EXPEND 2012
GOVERNMENT(April)	0.8	2.5	-1.8	0
OECD(may)	0	2.3	-2.1	0.3
CENTRAL BANK(July)	0.8	2.1	-2.4	-0.6

Source: Various organisations.

The GDP growth forecast for 2012 ranges between 2.1% and 2.5% although these will probably be revised downwards as 2011 progresses. Unfortunately the consumption performance will be much weaker than the GDP growth. The central bank expects consumption volume to continue to decline in 2012 while the OECD expects a very small increase. The Government projections are for no change in consumption volume. This suggests a very weak environment for domestic tourism in 2012 following on the previous years of consumption volume decline.

3.2 Economic Prospects in the Medium Term

Even with a resumption of GDP growth in 2011 there will be no quick return to the economic activity levels of 2007. The level of Irish economic activity will be lower in 2014 than it was before the economic collapse in 2007. Based on Government medium term assessments it will be about 2015 before the GDP 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.

One of the sectors with strong potential for achieving higher growth is international tourism. Budget 2012 must strengthen the foundations to achieve this growth through building on the stimulation measures recently introduced. While continuing the necessary task of correcting the public financial imbalances, Budget 2012 should support a clear strategy of achieving higher tourism 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 2011 is an increase of 2.5% in the CPI compared with declines in 2009 and 2010. 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 increase by only 1.5% in 2011 and will increase by 1% in 2012. Wage growth is expected to be 0.75% in both 2011 and 2012 following small declines in 2009 and 2010. These changes will not be sufficient to regain lost cost competitiveness. Government must not depend on market forces and the recession to improve cost competitiveness. Budget 2012 must directly focus on improving cost competitiveness.

Government can begin this process by freezing all its own charges and by reducing the intended energy price increases. The priority must be the immediate economic crisis rather than medium or longer term issues such as green energy. Substantial cost reduction must be implemented in energy companies and banks as well as the non-commercial public sector.

Commercial rates continue to be an excessive burden on the sector. In 2010 and 2011 councils began to appreciate to a greater extent, the burden which rates impose but the response was inadequate. On average there was a very small decrease. This contrasts with the substantial decline in hotel revenues, costs and prices. A much more radical response to public sector costs and charges 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. 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.

As an immediate step the Government should introduce a country wide 30% reduction in Local Authority rates applicable to hotels and guesthouses. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.

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.

The minimum wage issue has been worsened by the operation of the Joint Labour Committees (JLC) system for part of the industry. The JLCs imposed statutory wage levels which were effectively minimum wages which were higher than the official minimum wage and also imposed other legally binding conditions of employment to which other economic sectors were 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 IHF welcomes the recent court decision which ruled against the JLC structure. Instead of attempting to establish a new JLC type structure which would be compatible with the legal ruling, the Government should take this opportunity to operate labour markets without a JLC type structure and, instead, rely on the general labour legislation.

The Hotel Industry Survey illustrates the growing share of labour costs relative to turnover and the very large increase in 2009 and 2010 compared to previous years. The 2011 Survey for Ireland and Northern Ireland lists the 2010 share at 41.8% which is up from 32.2% in 1999 and 35.4% in 2004. The 2010 share is slightly below the 2009 level of 42.3%. When the 2010 Northern Ireland figure (35.7%) is removed the figure for the Republic is over 42%.

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

1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
32.2	33.3	32.4	34.2	35.6	35.4	37.6	37.6	38.8	40.0	42.3	41.8

Source: Ireland and Northern Ireland Hotel Industry Survey

This payroll cost percentage is very high despite efforts the hotel sector has made to control its labour cost base in recent years. Any effort to cope with the new market and economic realities and grow employment should not be hindered by internationally high statutory minimum wages and other labour costs.

3.5 Public Finances Crisis

IHF is acutely conscious that its Budget 2012 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 according to the published timescale. We recognise that proposals such as an 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 initiative 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. IHF argues that there are more savings possible from Local Government than recommended in the report. IHF urges the Government to act along the recommendations of these reports and on the findings of its forthcoming expenditure review and to reduce expenditure to the levels supportable by a competitive, economic growth friendly tax system and revenue.

3.6 Financing and Banking Crisis

It is clear from the evidence from IHF research, banks, NAMA and receiverships that the hotel sector is in a very difficult and deep financing crisis. This problem will not simply work itself out satisfactorily. Revenues have been squeezed by the combination of lower prices, excess capacity and low capacity utilisation rates. Many Irish economy derived 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. IHF welcomes the view of the Minister for Finance that otherwise commercially viable enterprises which provide employment but which are threatened by the direct and indirect effects of the property price collapse should be supported.

The financing crisis for hotels requires a fivefold response from policymakers as argued in previous submissions.

- 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 claw-back 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. At least 50% of the savings achieved

through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their 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 to be directed at the SME sector. Limited tax incentives should be introduced to support equity for debt restructuring schemes in existing hotels to reduce borrowing to a sustainable level.
- 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.

4. The Economic Role of Tourism

Tourism and the hotel and guesthouse sector are substantial national economic resources. The hotel and guesthouse sector has 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 included:

- €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.
- 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 2012.

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.

5. Performance of the Hotel and Guesthouse Sector

The commercial basis of hotels has greatly deteriorated over recent years. The average profit rate declined from 17.8% in 2005 to 10.2% in 2010. The profit rate declined each year between 2005 and 2010. Profit does not include depreciation, bank loan interest or rent where relevant. The survey figures refer to averages of hotels and many hotels operate at lower profit margins.

Between 2008 and 2010, the before tax profit per room dropped from €7,056 to €4,239.

Table 4: Hotel Sector Profit Performance 2005-2010

	2005	2006	2007	2008	2009	2010
Profit Before Tax per Room*	€10,238	€9,786	€9,308	€7,056	€4,650	€4,239
Profit Before Tax per Room (%)	17.8%	16.6%	15.5%	12.8%	10.4%	10.2%
Room Occupancy Average	68.9%	69.8%	69.7%	63.5%	59.4%	59.7%
Total Revenue per Room	€57,640	€59,107	€59,968	€55,116	€44,798	€41,705

*Profit before Tax, depreciation, loan interest or rent.

Source Ireland and Northern Ireland Hotel Industry Survey2011

The combination of increased capacity and the post 2007 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 €59,968 in 2007 to €41,705 in 2010, a decline of 30.5%. The room occupancy rate dropped from 70% in 2007, to 64% in 2008, to 59% in 2009 and to 60% in 2010. Between 2007 and 2010 the revenue per room declined by from €55,516 to €44,798.

These survey statistics are based on a sample 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 56% in 2009 and 56% in 2010 which are the lowest room occupancy rates 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 €37,463 in 2010, a decrease of 22%. IHF recognises 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 and other public sector determined costs.

Price reductions have become a dominant strategy within the sector. In 2010 the average room rate was €73.51. In 2009 the average room rate was €77.81 compared with €88.25 in 2008. The 2007 rate was €97.69. Between 2007 and 2010 the average room rate declined by 24.8%.

In the first five months of 2011 the hotel room occupancy rate increased from 49% in 2010 to 51% in 2011. 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. The guesthouse occupancy rate increased from 37% to 40% over the same period.

Table 5: Hotel Room Occupancy Rates % Jan - May 2010 and 2011

	Jan - May 2010	Jan - May 2011
Hotels	49	51
Guesthouses	37	40

Source Failte Ireland

As shown in Table 6 there has been a large increase in the number of overseas visitors in the first six months of 2011 following the earlier substantial decreases in 2010.

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

	Jan/June 08	Jan-June 09	Jan-June 10	Jan-June 11	% change 10/11
Total Overseas Visitors	3702	3304	2626	2959	12.7
Visitors from Great Britain	1873	1581	1228	1325	7.9
Visitors from North America		447	401	462	15.2

Source: CSO

- In the first six months of 2011 compared with 2010 total overseas visitors increased by 12.7%. This is a very welcome reversal of the declines of previous years since the economic crisis began. The increased numbers in 2011 compared to 2010 are mainly due to the negative effects of the disruption caused by the volcanic ash in spring 2010. The number of international visitors in the first six months of 2011 was 10.4% less than 2009.

However, the 2011 level of almost three million visitors is well below the 2008 level of 3.7 million. Visitors from Britain increased by 7.9% in the first six months of 2011 which also was welcome relative the declines of previous years. However, the current level is well below peak levels of British visitors. North American visitors increased by 15.2%.

Table 7 shows the domestic market performance in 2008, 2009 and 2010 for the first quarter which is the latest CSO domestic trips data. Domestic nights increased in 2010 by 5.4% and holiday nights increased by 1.9%. Both are below the 2008 levels of activity.

Table 7 Domestic Market Jan-Mar 2008, 2009 and 2010 (k) *(Source CSO)*

	2008	2009	2010
Domestic Trips	1851	1760	1785
Holiday Trips	890	739	726
Domestic Nights	4626	4221	4443
Holiday Nights	2336	1706	1738

More up to date data are available from Failte Ireland sources. The 2011 Tourism Barometer (Wave 2 May) notes that 43% of hotel and 30% of guesthouse proprietors reported an increase in business volume in for the first half of 2011 compared with 2010. 28% of hotels and 43% of guesthouses reported a decrease in business volume. 38% of hotels reported an increase in overseas business and 46% reported an increase in domestic business. These figures are a substantial improvement on the 2010 Barometer results.

Table 8 Performance in first half of year compared to last year 2010 and 2011 in brackets

% of Respondents	Up	Same	Down
Hotels	30(43)	21(29)	47(28)
Guesthouses	11(30)	14(27)	74(43)
Hotels Overseas Market	23(38)	20(27)	57(35)
Hotels Domestic Market	38(46)	28(27)	33(27)
Hotels Northern Ireland Market	9(17)	39(45)	49(38)

Source: Fáilte Ireland Tourism Barometer 2011,May.

6 Budget Policy to Support Hotels and Guesthouses

6.1 Context

The IHF Budget proposals are designed to support the contribution of the hotel/guesthouse sector to economic recovery.

The proposals take into account:

- The likely weak (but better than 2009 to 2011) 2012 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/guesthouse 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 its vulnerability to the current lower number of tourists.
- 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 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.

6.2 The Budget Proposal

It is important for the future strength of the hotel/guesthouse sector that Budget 2012 reduces the burden imposed by penal public sector charges and local taxes, that cost competitiveness is promoted vigorously and the hotel excess 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 national economic recovery. 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 2012 can begin this process by:

- Increasing the current real level of activity funded by the Fáilte Ireland and Tourism Ireland international marketing budget and initiating specific additional marketing activity such as to attract new business/conference visitors to derive maximum benefit from the availability of the National Convention Centre. Attention should also be given to developing integrated regional tourism products in conjunction with the industry to address regional imbalance. Marketing activity is a main determinant of market share. Irish tourism can not depend on growth in international markets. We must aim to increase our market share of the now smaller international tourism market.

- 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 2010 level.

- Reducing local authority rates by 30% for 2012. At least 50% of the savings achieved through the implementation of the recommendations in the various Local Government efficiency reports should be passed back to the business sector through a reduction in their rates.

- The intended increases in energy charges should be cancelled and priority should be given to the immediate economic crisis and the need to enhance competitiveness and reduce costs.

- Ensuring the availability of appropriately priced credit, the introduction of limited incentives to encourage debt restructuring schemes in existing hotels/guesthouses and the establishment of 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.

- Allowing the JLC system of establishing wage rates to disappear without introducing any replacement structures or system, to encourage competitiveness and support commercial viability.