Date: 7th April 2014

Graham Wason
Chairman
The Campaign for Reduced Tourism VAT
C/O British Hospitality Association
Queens House
55/56 Lincoln's Inn Fields
London, WC1A 3BH

Dear Graham

THE CAMPAIGN FOR REDUCED TOURISM VAT

Purpose of this note

Five Lines Consulting have been commissioned by The Campaign for Reduced Tourism VAT to answer the following question:

> *"The fact that many UK hotels are full and profitable suggests demand does not need a fiscal stimulus, particularly in places like London".*

Response

Average percentage bedroom occupancy levels in the English regions (the regions outside of London), Scotland and Wales over a 10-year period from 2003 through to 2012, according to annual surveys by two consultancy firms, were as follows:

	STR Global	TRI
English regions	69.6%	68.6%
Scotland	71.7%	72.8%
Wales	69.3%	71.5%

Source: British Hospitality – Trends and Developments 2012 / HotStats 2013

Hotels are rarely simply 'full'. The average bedroom occupancy statistics suggest that typically between a third and a quarter of all hotel rooms in the country are empty.

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These consultancy firm surveys are heavily biased towards three, four and five-star 'full-service' hotels – many of which are part of a recognised hotel brand – that typically enjoy significantly higher average room occupancy levels than lower quality hotels, rural hotels, seaside hotels and other forms of visitor accommodation.

Hotels in London tend to operate at higher average room occupancy levels than non-London hotels. Average percentage hotel room occupancy in London hotels according to the same two annual surveys over the 10-year period to 2012 were as follows:

	STR Global	TRI
Highest annual	82.3%	79.6%
Lowest annual	73.7%	74.3%
10-year average	79.3%	82.5%

Source: British Hospitality – Trends and Developments 2012 / HotStats 2013

Even in London, average occupancy levels have not risen above 83% in any year, so - typically - around a fifth of hotel rooms are empty / unsold. This pattern of bedroom occupancy is set to continue. For example, latest data for London's occupancy levels - from PwC - for 2013[1], and forecasts for 2014 and 2015[2] are 81%, 82.7% and 82.9% respectively.

The nine-year average Gross Operating Profits between 2003 and 2011 is shown in the table below[3]. This illustrates the variance in profitability across the UK, particularly outside of London. Once fixed and other business costs are incurred (e.g., rents, rates, debt repayment and tax), this can significantly reduce profitability. In many cases – as discussed later in this note – this has resulted in hotels becoming insolvent.

[1] *Source: PwC – The Right Kind of Growth, UK Hotels Forecast 2014.*

[2] *Source: PwC – UK Hotels Forecast Update for 2014 and 2015.*

[3] Gross Operating Profit is the hotel profit before fixed costs such as insurance, rents, and rates, as well as interest charges, and taxation.

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	STR Global	TRI
London	46.5%	46.0%
English regions	35.5%	32.9%
Scotland	32.9%	32.5%
Wales	31.6%	32.2%

Source: British Hospitality – Trends and Developments 2012

Although London may be seen to outperform other parts of the UK in terms of hotel trading, it is important to remember London is in a fragile position competitively. Not only is the success of the Capital's tourism sector influenced by many 'external' economic and other factors – which has stemmed the flow of international tourists at certain times over the past ten years[4] – but London also competes on the global stage with other major cities such as Paris, Madrid, Rome, etc. It is also important to reflect on the fact that c. 53% of all international tourist expenditure is in London (i.e., £9.4 billion)[5], so if London struggles to attract overseas visitors, this has a negative knock-on effect for the rest of the UK (in terms of tourist volumes and expenditure).

Over recent years, the hotel industry has been badly affected by the economic recession. This is shown in the table below. Between 2008 and 2013, there was an average of 255 hotel industry insolvencies each year.

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[4] Research undertaken by PwC has shown the various factors which have influenced tourism demand to London and the UK generally over the past 35 years. The factors that influence tourism demand include the Gross Domestic Product of the UK and key source markets (e.g., USA, Canada, Japan, etc.), international crises (e.g., the 1991 Gulf War, '9/11', SARS, the Iraq War, the 2005 London Bombings, etc.). *Source: PwC – UK Hotels Forecast Update for 2014 and 2015.*

[5] *Source: British Hospitality – Trends and Developments 2012.*

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Type of insolvency	2008	2009	2010	2011	2012	2013
Compulsory Liquidations	44	36	32	41	41	22
Creditor Voluntary Liquidations	46	66	60	81	94	74
Bankruptcies	49	55	82	72	82	73
Receiverships	5	18	21	8	7	35
Administrations	26	68	51	80	51	59
Company Voluntary Arrangements	5	12	13	6	12	2
Total	**175**	**255**	**259**	**288**	**287**	**265**

Source: The Insolvency Service (BIS), 2014

According to KPMG, although *"the overall number of businesses entering insolvency has dropped, the [Insolvency Service] figures reveal that certain sectors are still struggling and remain under unrelenting pressure. The hotel and restaurant sector is being hit particularly hard"* (source: Jane Moriarty, Restructuring Partner, KPMG Press Release, 2013).

Concluding remarks

Thank you again for commissioning Five Lines Consulting for this piece of analysis. Please let me know if you have any questions.

Yours sincerely

Rob Bailey

Director
Five Lines Consulting Ltd

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