CTC Tourism Intelligence Bulletin – Issue 10: November 2002

The Tourism Intelligence Bulletin continues to monitor the tourism industry around the world. This issue reveals tourism intelligence gathered in September and October 2002.

Tourism Progressing Despite Disparities

Executive Summary

- Canada's tourism industry continues to move toward financial stability. In the third quarter of 2002, Air Canada and Canadian low-cost carriers again posted profits. Not surprisingly, Canadian hotel occupancy rates in September were better than last year. In fact, even August occupancies indicated that the industry had already rebounded to match last year's pre-September 11th performance. While these positive findings suggest Canada's tourism sector continues to progress, industry gaps remain.
- These gaps are not good because they are making the tourism recovery less robust than it could be. Whether it's the gap between the rate of recoveries in the Canadian and U.S. economies, the difference in confidence between business and leisure travellers or the price of refundable and non-refundable tickets, "disparity" seems to be a underlying challenge within the tourism industry.

Emerging Trends and Issues - Consolidation in the Airline Industry

- As the tourism industry continues toward recovery, airlines, particularly U.S.-based airlines, are undergoing dramatic change. In the current operating environment, it appears that the most desirable business model for airlines involves some form of low-cost travel. With size and inflexibility working against them, many major airlines are considering consolidation as an alternative to bankruptcy. While consolidation may result in fewer airlines, many believe it might also produce a more focused industry, one capable of delivering a broader range of alternatives for air travellers, something travellers have been wanting for years.
- At this stage, it appears the advantages of consolidation may outweigh the costs. Proponents believe that consolidation can lead to more alternatives for travellers because its benefits extend to international air transportation as regional carriers hook up with international carriers. By doing so, mid- and small-sized communities would potentially enjoy more links to foreign cities after consolidation and these links would be open to even greater levels of competition.
- As the industry consolidates, who will emerge from the mix? The general consensus suggests low-cost carriers will have a more prominent role, again bringing more choice to travellers. Over the last two years, low-cost carriers have outperformed the major airlines. And they have done well despite challenging economic conditions.

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Consumer (Traveller) Overview

- The gap between refundable and non-refundable fares appears to be one of the main concerns of business travellers today. In fact, in Canada and the U.S., the major air carriers have gone as far as restricting the reuse of non-refundable tickets. According to a survey of business-travel managers by Runzheimer done after the implementation of non-refundable fare restrictions, 36 per cent of respondents indicated they intend to change their travel policies to reflect the use of non-refundable tickets. More dramatically, 23 per cent indicated that they will cut travel in response to the restrictions.
- The Travel Industry Association of America (TIA) reported domestic and international travel spending continues to be soft in the U.S. and isn't expected to recover to year-2000 levels until sometime in 2004. Still, overall leisure travel by Americans was up 2 per cent for the first half of 2002, compared with the same period a year earlier. More impressively, in-region or trips close to home, were up 8 per cent during this same period. However, TIA warns that any recovery could be derailed by a number of new political tensions, including war.

Travel Supplier Overview

- Canada's major airline (Air Canada) and low-cost carriers posted third-quarter profits this year. In the U.S., third-quarter results were once again disappointing for the major airlines. After posting significant losses, many are working with their unions to reduce labour expenses. Some are also cutting back or closing facilities in an effort to further reduce expenses. Other tactics include grounding airplanes, deferring the delivery of new airplanes and opening call centres overseas.
- The Canadian hotel industry appears to be back on solid ground. According to Pannell Kerr Forster Consulting Inc., both national hotel-occupancy levels and revenue per available room (RevPAR) achieved pre-September 11th levels in August of this year for the first time since the terrorist attacks. Meanwhile, in the U.S., national hotel-occupancy levels and RevPAR remain distressed - especially at airport hotels. As hotel negotiations continue with companies for 2003 rates, the picture remains unclear as to when an industry turnaround might occur, giving buyers an edge.
- Fortunately, even U.S. travel agents are cautiously becoming more optimistic - at least according to the most recent Travel Agent Confidence Index conducted by Travel Weekly. When asked to predict the outlook for the travel industry at regular intervals during the next 12 months, U.S. travel agents reported they don't expect much in the short-term, but anticipate a turnaround in six months to a year. The optimism is based on the belief that leisure travel, especially cruises and domestic tour packages, will continue to book well.

Economic Overview

- The economic landscape in both Canada and the U.S. is split. Businesses remain cautious while consumers generally remain confident. For once-exuberant firms, the sliding stock market has taken the wind out of their sails. Business investment has been down, if not flat, over the last 18 months in both Canada and the U.S. and this situation will not be resolved soon. The uncertainty surrounding the impending war in Iraq is also holding up any significant recovery in investment spending. Fortunately, consumers have remained confident. Unemployment rates as well as historically low interest rates are driving record home and light-vehicle sales in North America.
- Widespread weakness in the summer and early fall economic data releases confirmed that the economic recovery in Euroland has stalled. A stronger euro and the deteriorating global outlook have hurt export sales while domestic demand has been undermined by weak consumer spending, the result of declining financial wealth.
- South Korea, China and Taiwan will lead total output growth in Asia. For Japan, there is a glimmer of hope. It appears that the government is going to do something about the decade-long deterioration in the country's financial system starting with the announcement by the Bank of Japan that it will purchase stock holdings directly from the nation's troubled banks.

Opportunities

- According to the Canadian Tourism Research Institute's latest Winter 2002 Travel Intentions Survey, a surprising 74 per cent of potential travellers indicated that they will likely or very likely still take their winter trip if a war breaks out in Iraq. However, the survey indicates 26 per cent are not likely to go. Last year, after September 11th, safety concerns had more of an impact on outbound travel than they did on domestic travel. In fact, many planned outbound trips were replaced by domestic trips because of safety concerns. In the short term, suppliers may find that targeting the domestic market will, once again, represent the safest bet to minimize risk, even with an escalation in political tensions.
- The Japan Association of Travel Agents released a benchmarking study for suppliers interested in doing business with older Japanese citizens in the medium term. The survey, Travel by Next-Generation Senior Citizens, investigated what features are significant to travellers aged 50 to 59. According to the survey, these travellers will take trips more frequently and will become important clients to their travel agents. Overall, they intend to spend a great deal of money on special-interest tours, but will economize on normal travel. As well, most Next Generation Senior Citizens intend to travel with their spouses and are very likely to select Canada or Oceania when they are looking for an ecotourism or green tourism experience.
- Leisure travel is poised to continue to lead the tourism recovery. Research from the Travel Industry Association of America reveals Americans want to make a connection with family, heritage or nature. Americans should have more time to travel because for the first time in the nearly 30 years since Harris Interactive has been asking the question, the number of working hours decreased significantly. In fact, many of those additional leisure hours were spent in Canada. Even with heightened travel fears after September 11th, overnight travel from the U.S. still managed to increase. If political tensions rise further in the future, U.S. arrivals in Canada might, once again, increase because Americans perceive Canada as a safe country.

In Brief

Canada's tourism industry continues to move toward financial stability. In the third quarter of 2002, Air Canada and Canadian low-cost carriers again posted profits. Also posting positive financial results was the Canadian hotel industry. Not surprisingly, Canadian hotel occupancy rates in September were better than last year. While these comparisons are difficult because of the impact of the terrorist attacks last year, August figures indicated that the industry had already rebounded to match last year's pre-September 11th performance.

While the rate of recovery for Canada's tourism industry continues to exceed that in the U.S., the weight of persistent disparities will take a toll. Whether it's the gap between the price of refundable and non-refundable tickets, the difference in confidence between business and leisure travellers or the rate of recovery in the Canadian and U.S. economies, "disparity" seems to be a underlying challenge facing the tourism industry's recovery. These gaps are not good for the industry because they are making the recovery less robust. The latest data from both Statistics Canada and The Conference Board of Canada suggests that both the level of economic growth and consumer confidence in Canada are weakening - mirroring the trend that already existed in the U.S. While the latest Canadian tourism data suggests continuing progress, the persistent gaps within the industry remain troubling.

In fact, recently the big six U.S. airlines implemented further restrictions on non-refundable tickets, making the gap between these and refundable tickets even wider. With the change, airlines hope that business travellers will return to business class to acquire the flexibility of non-restrictive refundable tickets. But, as a survey by Runzheimer reported, many companies are likely to continue to search for alternatives to traditional business-class travel. This means airlines, especially the U.S. majors, will need to consider other options to achieve financial stability.

Forming partnerships and alliances to obtain economies of scale is one option that is being explored. Alliances allow suppliers to expand their networks with less risk. This is preferable because, at the present time, risk is something many tourism suppliers cannot afford.

Emerging Trends and Issues - Consolidation in the Airline Industry

As the tourism industry continues toward recovery, airlines, particularly U.S.-based airlines, are undergoing dramatic change. Since the beginning of the year, the market penetration of low-cost carriers has been striking. In the current operating environment, it appears that the most desirable business model for airlines involves some adaptation of back-to-basics, low-cost travel. Meanwhile, with size and inflexibility working against them, many major airlines are now considering consolidation as an option for survival. While consolidation may result in fewer airlines, some believe it might also produce a more focused industry, one capable of delivering a broader range of alternatives for air travellers, something travellers have been wanting for years.

All things considered, the airline industry in Canada is recovering well, especially compared with its counterparts in the U.S. Positive quarterly operating results for not only Canada's low-cost carriers (WestJet and Jetsgo), but also Air Canada, suggest that Canadian carriers have been actively implementing and experimenting with methods to further improve their financial performance. In fact, it appears that the successful operation of Air Canada's low-cost brand, Tango, played a major role in Air Canada being the only major international North American carrier to post a net profit in the second and third quarters.

The speculation is that some of the major U.S. airlines will consolidate. Consolidation may happen through mergers or by outright failure of one or more of the major airlines. At this stage, it appears the advantages of consolidation outweigh the costs. Over the next three years, it is possible that low-cost carriers will nearly double their respective market shares.

Industry consolidation has both critics and supporters. The critics assume that it will limit competition and the resulting collusion will lower service and result in higher prices. On the other hand, the financial health of the international airline industry is so bad that some insiders believe that consolidation may be the best way to resolve this difficult situation.

In fact, the argument for consolidation may be best summarized by Clyde Prestowitz, President of the Economic Strategy Institute (ESI), who says that "given the unique dynamics of airline networks, that assumption (increased costs) appears to be not only false, but the exact opposite of what is likely to happen." He goes on to say that consolidation can lead to more alternatives for travellers because the benefits of consolidation extend to international air transportation as regional carriers hook up with international carriers. Ultimately, mid- and small-sized communities would enjoy more links to foreign cities after consolidation and these links would be open to even greater levels of competition. In this respect, access to international flights will allow these communities to benefit economically from the globalization of businesses and markets.

As the industry leans toward consolidation, who will emerge from the mix? The general consensus suggests that low-cost carriers will have a more prominent role, again bringing more choice to travellers. Over the last two years, low-cost carriers have outperformed the major airlines and they have done well in spite of challenging economic conditions.

This past October, the Business Travel Coalition (BTC) published its outlook for the U.S. airline industry for 2004. After consulting with industry experts and analyzing relevant data, it came up with three scenarios. The first scenario assumes a rosy economic outlook and government support of the industry. The second assumes a moderate economic recovery and slow change in the industry due to bankruptcy protection. The third scenario - and the one that seems to be the most likely - assumes the failure of one or two major airlines. These failures cause the balance of the remaining network to restructure aggressively. Costs and productivity would be driven to levels currently seen among the low-fare airlines. Smaller, more efficient and more competitive major network airlines would emerge. In the end, low-fare carriers could potentially represent 30 per cent of the market.

The consensus among insiders is that the air-travel industry will eventually recover but not before further realignment and restructuring. The short- to medium-term outlook for air travel continues to suggest that the major airlines will focus internally to achieve stability while, at the same time, lower-cost alternatives gain in popularity. While the prognosis for the Canadian airline industry still includes further realignment by the key players and potential newcomers, it is expected to be less disruptive than what lies ahead for the U.S. airline industry. Although many believe the time for change is near, air access alternatives will once again have to confront the challenges posed by Canada's limited market size and vast geography.

Regardless, the tides of change appear set to shape an industry that delivers a broader range of alternatives for air travellers via consolidation and the further penetration of low-cost carriers. On-going growth in the tourism industry requires that the turbulence caused by these tides of change will eventually subside, leaving in their wake an industry that is more financially sustainable.

Consumer Overview - Canada and the United States

Business Travellers

The gap between refundable and non-refundable fares is the main concern of business travellers today. As Runzheimer reported in its Travel Management Report, business travellers have had to contend with a faltering economy, commission cuts to agencies, September 11th, capacity cuts, airline bankruptcies, zero commissions, cutbacks in travel budgets and the high cost of air travel. With the implementation of restrictions on non-refundable tickets, any sympathy travellers may have had for the major airlines is starting to slip away. Many feel that while the implementation of restrictions adds immediately to the bottom line of the air carriers, ultimately, it doesn't address the main reason why business travellers have not returned to the skies in significant numbers: the large gap between refundable and non-refundable fares.

In Canada and the U.S., the major air carriers have restricted reuse of non-refundable tickets. Travellers may no longer rebook an unused ticket within one year from the date of issue. Instead, they will lose the full value of the fare if they fail to contact the airline prior to the scheduled trip date and pay an associated change fee.

According to a survey of business-travel managers by Runzheimer done after the implementation of non-refundable fare restrictions, 36 per cent of respondents indicated that they intend to change their travel policies in 2002 or 2003 to reflect the use of non-refundable tickets. A total of 23 per cent indicated that they will cut travel in response to the restrictions. An overwhelming percentage (93%) believe the new restrictions are an attempt by the airlines to force business travellers to purchase refundable tickets.

Interestingly, the majority of business-travel managers (55%) believe Web-advertised fares are interfering with their corporate-travel policies. This, according to a survey by Northstar Media Research. More than one-third (37%) of respondents are concerned employees' use of Web-advertised fares will jeopardize their airline deals. Among measures companies are taking to minimize use of Web fares, reminding travellers of proper booking procedures and discouraging outside bookings are the most common (41%).

Business-travel managers are also witnessing shrinking lead times for meetings. According to a Meetings Today survey, 25 per cent of respondents said the average lead time for their companies' small meetings was less than one month. This is a sharp increase in the number of respondents from the 14 per cent who indicated as such in the spring of this year. About 67 per cent of respondents said their average small-meeting lead time was 90 days or less, the traditional definition of a short-term meeting.

The Travel Industry Association of America (TIA) reported that the volume of business trips has declined in recent months. Business travel fell nearly 9 per cent for the first six months of this year compared with the same period a year earlier.

In September, Accenture announced that more than one-third (35%) of respondents to a business-travellers survey indicated they expect to travel more for business between now and the end of the first quarter of 2003 than they had during the past six months. The survey also revealed that 13 per cent have increased their use of low-cost carriers over the past six months and 17 per cent indicated that their use of these carriers will increase in the next six months. Mid-range hotels are expected to be the primary accommodation choice for more than half of respondents (57%); only 16 per cent plan to stay in luxury-chain hotels.

Fortunately, the outlook for international business travel is improving. According to a survey by American Express, 35 per cent of international business travellers expect to increase their number of international trips next year, while the majority (56%) expect to maintain their current level of international travel. Among respondents from 14 countries, Canadians and Americans were found to be the most confident regarding how safe they felt while flying (97 per cent felt safe to some degree). Asians and Australians were the least confident (79%).

Not surprisingly, alternatives to travel remain popular. In September, Wainhouse Research announced the results of a business-travellers survey in which more than 70 per cent of respondents stated they were still interested in alternatives to travel. Compared with the time before September 11th, 62 per cent reported increasing their use of Webconferencing, 25 per cent reported increasing their use of videoconferencing and 12 per cent reported increasing their use of teleconferencing.

Runzheimer released the results of its U.S. Domestic Business Travel Price Index. In the third quarter of 2002, travel prices increased 7.5 per cent compared with the third quarter of 2001. Compared with the second quarter of 2002, the prices of car rentals, meals and lodging all increased significantly while airfare costs dropped. Meanwhile, American Express reported in its Business Travel Monitor that during the second quarter of 2002, the gap between restrictive and non-restrictive fares widened as the lowest-discount fares continued to decrease while business-oriented fares remained stable.

Leisure Travellers

The recovery in leisure travel continues but North Americans are changing their travel patterns. In the past year, travel by auto and recreational vehicle has increased and trips taken tend to be closer to home. Making a connection, whether it's with family, heritage or nature, are prevalent themes among leisure travellers today.

The Travel Industry Association of America (TIA) released its travel forecast in October. After falling nearly 6 per cent last year, domestic and international travel spending continues to be soft and isn't expected to recover to year-2000 levels until sometime in 2004. TIA warns that any recovery could be derailed by a number of new political tensions, including war. For the first half of 2002, leisure travel by Americans was up 2 per cent compared with the same period a year earlier. Meanwhile, in-region trips, or those close to home, were up 8 per cent during this same period.

Other winners in the U.S. leisure-travel market were cruise travel (up nearly 4 per cent during the first half of 2002) and recreation-vehicle (RV) rentals. During the last quarter of 2001, RV rentals skyrocketed by 30 per cent compared with a year earlier and have remained at that level throughout this year.

A study by D.K. Shifflet and Associates reported security checks, random searches, new airline ticket fees and other inconveniences are keeping people off planes, particularly for short trips. The number of people flying commercially between 200 and 400 miles dropped 22 per cent in the year after the September 11th attacks. Meanwhile, the America Automobile Association (AAA) reported the number of TripTiks it prepared increased almost 25 per cent in the first six months of the year compared with the same period a year earlier. TripTiks are primarily used for road travel.

Travel-Supplier Overview - Canada and the United States

Airlines - Canada

Canada's major airline, Air Canada, as well as the Canadian low-cost carriers, all posted third-quarter profits. Air Canada announced a third quarter profit of $125 million, an improvement of $1.03 billion from the same period a year earlier. Yearly comparisons are affected by the adverse effects of September 11th last year. Still, Air Canada attributed its positive performance to disciplined capacity management and cost control in tandem with a market-segmentation strategy. September, in particular, was a good month for Air Canada as it reported a 19 per cent increase in revenue passenger miles and a 10.3 per cent increase in capacity, both compared with a year earlier.

In addition, Air Canada launched Zip, a new discount subsidiary. Zip is starting with six aircraft that will fly between Vancouver, Edmonton, Calgary and Winnipeg. Eventually, the airline will fly across Canada. According to Zip, its purpose is to reduce Air Canada's cost on these routes.

Meanwhile, WestJet posted a $23.1 million profit for the third quarter of 2002, an increase of 77.3 per cent compared with the same period a year earlier. WestJet attributed the impressive results to a tighter focus on longer-haul flights and their launch in the Toronto market. For September, WestJet reported its revenue passenger miles increased 67 per cent compared with one year ago.

Transat A.T. Inc. announced that its net income for the third quarter ending July 31, 2002 was $6.3 million, compared with $5.9 million a year earlier. Transat A.T. stated sales volumes remained lower than expected but noted that the market is improving.

According to the National Post, WestJet is expanding at a 50 per cent annual rate. By 2008, WestJet could have as many as 94 aircraft. Starting in January next year, WestJet intends to increase the number of non-stop flights it operates between a number of city pairs.

Jetsgo made two announcements in October. It plans to double its size to six planes and it will start flying its first transborder routes. It also launched a two-for-one seat sale through the Christmas season - a normally unheard-of event. Jetsgo reported a 62 per cent load factor for September. Comparison with last year is not possible as Jetsgo started flying only recently.

Conquest Vacations announced in October that it will more than double its airline fleet in partnership with Skyservice, the company that owns the planes. Conquest will continue daily service year-round to several major Canadian cities while beefing up its offerings to the U.S. and other foreign sun destinations over the winter.

Airlines - U.S.

Third-quarter results were once again disappointing for the major U.S. airlines. For some, such as Northwest, the results include an after-tax grant from the federal government under the Airline Stabilization Act. Overall, the weak results were attributed to the continued depressed levels of business travel and increased security costs, taxes and insurance costs. America West was the only major airline to record an improvement compared with last year. It did so by lowering and simplifying fares, reducing delays and slashing costs.

Table 1. Airline revenue, net profit or loss

Airline	RevenueQ3, 2002 vs. 2001 (U.S. $)	Net Profit or Loss Q3, 2001 (U.S. $)	Net Profit or Loss Q3, 2002 (U.S. $)
Southwest Airlines	+4.2%	+$151 million	+$75 million
Alaska Airlines	+5.5%	+$25 million	+$11 million
AirTran Airways	+21.6%	-$11 million	+$1 million
Midwest Express Airlines	-4.8%	-$3 million	-$9 million
America West Airlines	+6.0%	-$43 million	-$31 million
Continental Airlines	-3.0%	+$3 million	-$37 million
Northwest Airlines	-1.2%	+$19 million	-$46 million
American Trans Air	-1.3%	+$0.001 million	-$61 million
Delta Air Lines	+0.6%	-$259 million	-$326 million
American Airlines	-7.0%	-$414 million	-$924 million

To cut costs, Northwest announced in October that it would close facilities and transfer jobs while American Airlines will temporarily park 42 aircraft starting early next year. Meanwhile United Airlines said it had reached an agreement with four of its five unions on a framework to reduce labour expenses over five years. It will also lay off 1,250 staff. Delta stated it will lay off 12 per cent of its workforce by April 2003, a reduction of up to 8,000 employees, including 1,500 flight attendants. Delta also announced it expects to save millions each year by becoming the first U.S. airline to open a call centre in India.

United Airlines warned in October that a bankruptcy filing cannot be ruled out. However, its first priority remains carrying out a successful restructuring plan outside of bankruptcy courts by engaging in discussions with lenders, suppliers and others. Meanwhile, US Airways, currently under bankruptcy protection, announced in October that it will lay off additional staff in November as it works to reduce its flight schedule by 13 per cent.

The Air Transport Association (ATA) reported that overall airline traffic increased in September, at least compared with September 2001, as revenue passenger miles (RPMs) increased 26.7 per cent. However, compared with September 2000 - perhaps a more appropriate comparison due to the systemwide shutdown in 2001 - RPMs declined 12.8 per cent. Air service still has not returned to pre-September 2001 levels.

According to the ATA, average domestic airfares increased 0.5 per cent in September compared with the same month a year earlier, but were still down 17.8 per cent from September 2000. Meanwhile, average international airfares were up 4.2 per cent compared with September 2001.

To control costs, the major airlines are tweaking their policies regarding restrictive ticket rules. In October, US Airways stated customers purchasing non-refundable tickets will be able to take alternate flights using new standby coupons. The new coupons will cost US$ 100 (CDN$ 157) and are valid for one-way travel on the originally scheduled travel date. This marked the third change in the US Airways standby policy in less than six weeks. Most other major U.S. carriers will continue to allow free same-day standby on non-refundable fares until January 1, 2003, at which time they, too, will start charging US$ 100 (CDN$ 157).

Increased partnerships and alliances between the major airlines may help further reduce costs. In October, United Airlines and US Airways announced that they will begin electronic ticket interlining, allowing passengers to use a single e-ticket for an itinerary involving both carriers. United has already established e-ticket interlining with Air Canada, American, Continental, Delta and Northwest Airlines. Meanwhile, Delta, Continental and Northwest released a planned alliance that, while short of a merger, will allow them to sell seats on each others' flights and earn frequent-flier miles. This is an effort to broaden their route offerings with little additional investment.

The Business Travel Coalition released scenarios regarding how the U.S. airlines industry will look in December 2004. The most likely scenario sees one or two major airlines going under, a moderate recovery for both the economy and business travel demand, and structural changes in airline costs and productivity.

Hotels - Canada

The Canadian hotel industry is holding up well. In August, Atlantic Canada posted the largest growth in terms of revenue per available room (RevPAR) compared with other regions in Canada. Luxury properties are starting to see a more robust recovery after lagging behind other service-level segments. National hotel-occupancy levels achieved a rate of 70.6 per cent in September, up 6.1 per cent from a year earlier.

According to Pannell Kerr Forster Consulting Inc. (PKF), the average daily room rate for Canadian hotels in September increased by 3.9 per cent compared with last year to $121.92. Meanwhile, RevPAR climbed 10.2 per cent to $78.26. Regionally, Whistler resorts and Prince Edward Island experienced the strongest RevPAR gains in September.

To date, three major Canadian hotel properties have reported third-quarter results. One, Fairmont Hotels and Resorts, noted that the third quarter is traditionally its strongest one. RevPAR during this time increased by 2.9 per cent compared with a year earlier. Legacy Hotels Real Estate Investment Trust attributed its results to improvement throughout its portfolio combined with the acquisition of Sheraton Suites Calgary Eau Claire. Four Seasons Hotels Inc. stated its disappointing results were the result of an asset-impairment charge.

Table 2. Earnings

Company	2001 (Q3)	2002 (Q3)
Fairmont Hotels and Resorts	US$ 54.4 million	US$ 74.2 million
Legacy Hotels REIT	CDN$ 31.0 million	CDN$ 37.5 million
Four Season Hotels Inc.	CDN$ -12.3 million	CDN$ +32 million

Hotels - U.S.

Unfortunately, the plight of the U.S. hotel industry continues. Revenue per available room (RevPAR) remains distressed, especially at airport hotels that are struggling with airlines' decreased capacity. As hotel negotiations continue with companies for 2003 rates, the picture is unclear as to when an industry turnaround might occur, giving buyers an edge. For their part, hotels are continuing to look to groups and expand an unusual trend whereby guest-room rates for corporate group blocks are sometimes among the highest charged by a property. In contrast, leisure or transient travellers are often being offered price discounts before they even ask.

Business Travel News reported corporate buyers of hotel rooms are increasing their requests for value-added amenities significantly this fall compared with other years. Underlying the shift in priorities is the fact that negotiated 2003 rates are expected to be flat compared with 2002. Amenities being sought include extra services such as complimentary shuttle service, free local calls and continental breakfast.

Revenue per available room continued to slide during the third quarter of 2002 compared with the previous year. Overall, hotels attributed the results to weaker lodging demand, especially in business travel. For many chains, however, net incomes were positive, primarily because of cost cutting.

Table 3. Hotel revenue per available room (RevPAR) and net income

Hotel	RevPAR Q3, 2002 vs. Q3 2001 (U.S. $)	Net Income Q3 2001 (U.S. $)	Net Income Q3 2002 (U.S. $)
Marriott International, Inc.	-6.8%	$101 million	$103 million
Starwood Hotels and Resorts	-2.7% (North America)-2.4% (Worldwide)	$30 million	$52 million
Hilton Hotels Corporation	+1.2%	$21 million	$48 million
Prime Hospitality	-7.1%	$5 million	$2.2 million
Host Marriott Corporation (REIT)	-9%	-$7 million	-$38 million

Marketing efforts by hotel chains were studied by the Center for Hospitality Research at Cornell University to determine the effects of decreasing or increasing marketing budgets during critical times. According to the survey, 70 per cent of all hotel managers surveyed had redirected their sales and marketing efforts to some degree in response to the events of September 11th. On average, sales and marketing budgets were reduced 8.6 per cent in 2001 compared with 2000. Concurrently, the total profits for these properties dropped 19.7 per cent. Of those that increased their budgets (by an average of 4.3%), profits fell 11.9 per cent.

Travel Agents

U.S. travel agents are cautiously becoming more optimistic — at least according to Travel Weekly's Travel Agent Confidence Index. When asked to predict the outlook for the travel industry, agents reported that they don't expect much in the short term but anticipate a turnaround in six months to a year. The optimism is based on the belief that leisure travel, especially cruises and domestic tour packages, are booking well.

Additionally, agents believe hotel bookings should experience a boost in the next three to six months but business travel will not begin to approach pre-September 11th levels for at least another 12 months or longer (79%). One-third of respondents don't believe airline bookings will ever reach pre-September 11th levels.

IATA's Bank Settlement Plan (BSP), the system of tracking airline tickets sold through Canadian travel agencies, reported that compared with last year, average domestic and international airfares for Canadians again increased in September. During that month, the average domestic airfare paid by leisure travellers was up 13 per cent while domestic business-travel airfares was up 11 per cent, both compared with the same time period a year earlier. Airfares to the U.S. were up a more modest 4 per cent while overseas airfares declined 2 per cent.

In the U.S., the Airlines Reporting Corporation (ARC) reported that average weekly sales-per-travel-agency for the month of September posted a 50 per cent improvement to US$ 39,567 (CDN$ 62,038) compared with the same month last year. However, it should be noted that due to the impact of September 11th, yearly comparisons are difficult. In fact, the total receipts for international and domestic air travel collected by ARC in September increased 46 per cent and 16 per cent, respectively, compared with September 2001.

Travel Weekly's 2002 U.S. Travel Industry Survey reported that travel agents book 90 per cent of all cruise travel and 87 per cent of vacations packages, making them an indispensable, influential link between travellers and travel suppliers.

International Overview — Overseas

United Kingdom and Ireland

In September, low-cost carriers outperformed British Airways easily in terms of passenger-load increases.

Table 4. Number of passengers (% change)

Carrier	Sept 2002 vs. Sept 2001
easyJet	+134% (includes acquisition of GO)
Ryanair	+33%
bmi	+18%
British Airways	+2.2%

British Airways' passenger numbers on U.S. routes continued to decline but premium traffic did well in September, increasing 18.1 per cent compared with 2001. However, compared with September 2000, this is 21 per cent lower. Bmi attributed its strong September growth to a switch from a conventional fare structure to one that more closely mirrors its low-cost competitors.

Aer Lingus is also changing to mimic low-cost carriers. It announced cuts to its business-class fares by up to 50 per cent. It also introduced less expensive economy airfares, with price cuts of up to 60 per cent, and abolished ticket restrictions.

British airport operator, BAA, reported air traffic at U.K.'s airports has returned to 2000 levels. In September, BAA handled 8.1 per cent more passengers compared with September 2001 and was on par with September 2000 levels. BAA attributed the increase to fierce competition between no-frills and traditional scheduled carriers, which pushed fares down and prompted more air travel. Stansted Airport saw the greatest increase in traffic of all U.K. airports.

Other good news for the airline industry came from Travelmole which reported airlines have made few cuts to their transatlantic schedules for this winter, signaling an improvement in the industry. The U.K.'s regional airports will bear the brunt of the few cuts.

According to the Travel Industry Association of America (TIA) and British tour operators, adventure holidays are a big hit with U.K. citizens and, as a result, the adventure-holiday market has grown at an annual rate of 10 to 15 per cent over the past five years. Conversely, traditional sun, sea and sand holidays have grown only 4 to 5 per cent over the same period.

According to TIA, the average number of nights for an outbound trip by U.K. travellers is eight. As well, prepaid packages are considered to be good value and 33 per cent of travellers use them. Meanwhile, a 2002 holiday survey by MORI for the Association of British Travel Agents found that 6 per cent of U.K. consumers who booked a package holiday in the past 12 months actually made the transaction online, an increase from just 1 per cent two years ago. The main reason quoted for those not booking online (19%) was that better deals were available elsewhere.

The tourism industry in England is focusing on the implications for the family holiday sector if proposed changes to the timing of the English school year go ahead. The government is presently proposing a six-term year, with two-week breaks in both October and April, and a shorter summer holiday. First Choice, a major tour operator, believes that shifts in timing, destination and type of family holidays booked would result.

A study by American Express revealed that while only 9 per cent of international business travellers expect to travel less in 2003, respondents from the U.K. were slightly less confident as 15 per cent expect to take fewer business trips in 2003 compared with 2002. BTA announced that the U.K. is the leading country in Europe for international-association meetings, overtaking France but still lagging behind the U.S.

France

After announcing the privatization of Air France, the French government stated in October that it will now delay the sale for up to a year. Finance Minister Francis Mer attributed the delay to weak stock markets, something he said would result in a sale price that does not reflect the carrier's true value.

Air France estimated that a pilots' four-day strike in September resulted in a EUR80 million (CDN$ 123 million) revenue loss. Still, Air France increased revenue per passenger kilometre (RPKs) in September by 4.8 per cent compared with September 2001 and increased its traffic by 4.1 per cent. Without the strike, Air France estimates its traffic would have grown by 13.3 per cent.

For the winter of 2002/03, Air France announced plans to boost available capacity by 7.5 per cent, restoring seating capacity to the level originally scheduled for last winter. Capacity to Canada and the U.S. is expected to benefit from the increases.

Air France stated it is following the lead of other major carriers and will no longer pay base commissions for tickets issued in Canada. It also introduced off-peak business-class travel fares. A reduction of 15 per cent will be offered to business travellers flying between 9:00 a.m. and 4:00 p.m. on the domestic network.

Germany

Lufthansa reported nine-month net earnings for 2002 of EUR344 million (CDN$ 545 million), up from EUR65 million (CDN$ 103 million) for the same period a year earlier. The positive results were attributed to strict cost discipline.

In September, passenger traffic on Lufthansa flights increased 7.5 per cent compared with September 2001. Frankfurt Airport operator Fraport AG announced passenger numbers had returned to September 2000 levels.

Lufthansa also announced it expects to expand its winter schedule by 13 per cent, restoring most of the capacity cuts it made last winter. This number will be just under the number of flights it operated in 2000. It also expects to add more than 3,000 jobs next year.

Competition for passengers heated up as Air Berlin announced the launch of a city-shuttle service in September. With the launch of this new service, the number of airlines competing for business in the German low-cost airline sector is now seven. And the country's leading rail operator also announced price cuts in an effort to woo airline passengers back onto the rails.

Eurowings, Lufthansa's low-cost airline, reported it sold 50,000 tickets in its first two weeks of operation. Executives at Eurowings expect the airline to break even in late 2003 or early 2004.

According to the German travel and tourism magazine, FVW, package bookings for the upcoming winter season are strong. Eastern European ski regions are said to be bestsellers as they are relatively inexpensive compared with other favourites such as Austria. Tour operators report growth for ski packages that include diverse events such as evening parties, mountaineering and hiking.

Italy

Alitalia announced a net loss of EUR49 million (CDN$ 75 million) for the first six months of 2002, compared with a loss of EUR260 million (CDN$ 398 million) for the same period a year earlier. Alitalia said the overall improvement was due to the effectiveness of its 2002/03 "Two-Year Plan" launched after the events of September 11th last year. Alitalia cut its prices on its domestic routes by an average of 30 per cent-but only from September 15 to December 15 of this year.

Air One reported that for the first nine months of 2002, it increased its traffic numbers by 80.4 per cent compared with the same period a year earlier. Air One expects to surpass its target of 3.5 million passengers for the entire year.

The Netherlands

KLM posted a net profit of EUR87 million (CDN$ 133 million) for the quarter ending September 30th. This represents a 70 per cent increase compared with a year earlier. The positive result was attributed to cost cutting and capacity trimming. For September, KLM reported overall passenger traffic increased 7 per cent compared with a year earlier. The weakest routes were through the mid- and south Atlantic.

KLM is on track to combine its U.K. and Dutch regional carriers, resulting in a feeder operator for its Amsterdam parent. This move should save the company about 20 per cent in overhead.

Buzz, KLM's low-cost carrier, launched a promotional campaign that will run until November. It involves giving away parking spots that are closer to Stansted airport and offer access to the airport's Fast Track system. It is the first time BAA, the major U.K. airport operator, has cooperated with a low-cost carrier. KLM also announced that on November 1, buzz became an independent company within the KLM Group.

Japan

Consolidation in the airline industry has reached Japan. Japan Airlines System Corp., the new group comprising Japan Airlines and Japan Air System, was listed formally on the Tokyo Stock Exchange and the integration of its operations has started. By integrating operations, the new company hopes to increase profits and compete with All Nippon Airways (ANA) in the domestic market, which is also consolidating. ANA announced it signed an alliance agreement with Japan's low-fare airline Air Do.

The Travel Industry Association of America (TIA) reported major Japanese wholesalers experienced rising demand for bookings in September and October. The upswing in bookings was partially attributed to postponement of travel due to the World Cup finals.

TIA also reported long-haul markets from Japan suffered more than short-haul markets in 2001 compared with the previous year. During that period, the number of Japanese arrivals to the U.S. declined by 19 per cent while Canada saw a 3 per cent decline. For overseas leisure trips, TIA reported that visiting natural and scenic attractions was the top activity preferred by Japanese, followed closely by shopping.

According to a survey by the Japan Travel Bureau (JTB), elderly tourists are keen to learn about foreign history, nature and culture. In fact, to accommodate this growing market (Japan has a record number of people who are 100 years old or more), JTB Corp. announced it will open up a retail outlet catering exclusively to middle-aged and senior travellers.

Korea

Korean Airlines (KAL) reported traffic levels rebounded strongly in August from the post-World Cup slowdown in June and, in fact, increased 0.5 per cent compared with the same month a year earlier. Traffic growth was expected to be maintained into September. For the month of August, KAL recorded a net profit of KRW 48.6 billion (CDN$ 62 million), up from KRW 2.6 billion (CDN$ 3.3 million) a year earlier. Given its strong monthly and year-to-date performances, KAL expects to achieve its full-year operating profit target of KRW 310 billion (CDN$ 395 million).

However, growth will not occur on domestic air routes as they are being scaled back by both Korean Airlines and its main competitor, Asiana Airlines, due to mounting losses from low fares and rising competition from new highways. South Korea has opened new highways in a bid to ease heavy traffic congestion, especially in coastal areas. However, approximately 70 per cent of both carriers' annual revenues come from international operations.

According to the Travel Industry Association of America (TIA), Asian travellers, including South Koreans, still value package tours. TIA further stated credit cards are not as prevalent among Asian travellers as they are among North Americans. Challenges for Canada and the U.S. include security concerns, sluggish economies and a maturing market (which means a desire for more destination variety).

Hong Kong

Cathay Pacific released passenger traffic figures for the month of August showing a 10.9 per cent increase compared with August 2001. Passenger-load factors remained strong, as well. Cathay Pacific attributed the results to strong leisure-travel demand.

Dragonair recorded a 19 per cent increase in the number of passengers it carried in August compared with a year earlier. Increased capacity and the first full month of its Taipei route helped contribute to the growth.

The Australian Tourism Commission (ATC) released a Hong Kong Market Profile in which it was noted that Hong Kong is an extremely competitive market for travel agents. As well, the airlines have a huge influence on both travel agencies' pricing strategies and on their itinerary planning. The ATC also expects short-haul, single-destination travel to increase in the future at the expense of outbound travel to long-haul destinations. Destination competition focuses mainly on price, with only minor product or package variation.

Taiwan

In October, China Airlines raised its 2002 pre-tax profit target by 56 per cent to TWD$ 2.2 billion (CDN$ 99 million). The change was made because the cargo business turned out to be stronger than expected. EVA Airways, meanwhile, raised its pre-tax profit forecast for 2002 by 37 per cent to TWD$ 1.41 million (CDN$ 63.6 million), citing strong cargo traffic and lower fixed costs.

For August, China Airlines reported a decrease of 1.5 per cent in operating revenue. Meanwhile, EVA Airways announced its revenue rose 30 per cent compared with August 2001 because of improving passenger and cargo traffic on the Taipei-Hong Kong route.

China Airlines announced it won government approval to buy a 25 per cent stake in Shanghai-based China Cargo. This marks the first time Taiwanese authorities have allowed one of their airlines to invest in the Chinese Republic's aviation industry. China Airlines also announced in October that it had been readmitted to the International Air Transport Association (IATA) after a 28-year absence. China Airlines believes membership in IATA will ease the clearance of accounts and allocation of slots between China Airlines and other member air carriers. China Airlines is now the only Taiwanese member of IATA.

Airwise News reported that Air Canada suspended service on its Taipei-Vancouver route as of October 27. Air Canada stated the suspension will end in March but further reductions could happen at a later date.

The Australian Tourism Commission (ATC) released a Hong Kong Market Profile stating short-haul, intra-Asian travel is expected to increase in popularity as long as the economic and political situation in Taiwan remains difficult. Further, ATC found that competition between long-haul destinations is fierce, with price-led promotions dominating the marketplace.

Australia

In October, Qantas announced it expects to remain on course for another year of profitability, with buoyant yields and load factors. CEO Geoff Dixon said international, domestic and regional operations all performed well in the quarter ending September 30th. Qantas will also continue to develop its low-cost carrier, Australian Airlines, that was launched in October.

The Australian Tourism Commission (ATC) announced a new initiative, Vision One Million, which aims to build inbound tourism from Japan. The initiative involves a long-term partnership between leaders of the top travel companies in Japan and the Australian tourism industry. According to the ATC, this is the first time key Japanese travel companies have made a long-term commitment to promote a single destination.

New Zealand

Air New Zealand (ANZ) announced its most recent financial year (which ended June 30th) was better than anticipated. Total revenue for fiscal 2001/2002 declined by 9.5 per cent compared with the year before, largely due to decreased off-shore travel demand. ANZ's net loss after unusual items and tax was NZD$ 319 million (CDN$ 244 million). For the current fiscal year, ANZ expects to realize pre-tax earnings of NZD$ 200 million (CDN$ 152 million).

ANZ will launch its no-frills domestic carrier, Air New Zealand Express, in November of this year. ANZ estimates using Air New Zealand Express will save its corporate customers an average of 18 per cent on domestic travel yearly.

Economic Overview

North America

The economic landscape in both Canada and the U.S. is split. Businesses remain cautious while consumers generally remain confident. For once-exuberant firms, the sliding stock market has taken the wind out of their sails. Business investment has been down, if not flat, over the last 18 months in both Canada and the U.S. and this situation will not be resolved soon. The uncertainty surrounding the impending war in Iraq is also holding up any significant recovery in investment spending.

Consumers remain confident, however. Historically low interest rates, as well as unemployment rates, are driving record home and light-vehicle sales in North America. Employment growth in Canada is the strongest it has been in nine years. The Canadian economy should lead North American growth in 2002 growing 3.6 per cent versus 2.5 per cent and 1.6 per cent in the U.S. and Mexico, respectively. In 2003, Mexico will lead its NAFTA partners rising by 4.2 per cent compared to healthy 3.7 and 3.9 per cent gains in the U.S. and Canada, respectively.

Europe

Widespread weakness in the summer and early fall economic data releases confirmed that the economic recovery in Euroland has stalled. Business confidence is dropping in most European countries and OECD leading indicators in the euro area are all on the decline. A stronger euro and the deteriorating global outlook have hurt export sales while domestic demand has been undermined by weak consumer spending, which has been affected by declining financial wealth.

Meanwhile, the U.K. economy is healthy thanks to solid gains in real wages. In 2003, real GDP growth will pick up in line with a rebound in growth in the United States, the U.K.'s largest trading partner. Monetary policy in the United Kingdom will remain accommodate and this should support consumer spending in 2003.

This year, the French economy has been plagued by the same factors that have affected almost every country in Europe, namely weak consumer and business confidence as well as declining investment spending. Recent declines both in the euro and in business confidence suggest that businesses are unlikely to accelerate their spending or hiring in the near future.

The German economy has been hit by declining confidence among businesses, poor labour market conditions and a weak global recovery. The floods in August did not help, either. This year, the economy will be lucky to record real GDP growth of 0.5 per cent.

Asia-Pacific

South Korea, China and Taiwan will lead total output growth in Asia. After a lull in 2001, the Hong Kong economy is coming back to life and is expected to recover in 2003. Political uncertainty will weigh in on the already anemic Philippine and Indonesian economies.

There is also a glimmer of hope in Japan. It appears that the government is going to do something about the decade-long deterioration in the country's financial system. The Bank of Japan recently announced that it will purchase stock holdings directly from the nation's troubled banks. In the absence of a strong rebound in global economic activity, Japan's weak economy and strong yen point to building deflationary pressures for both the remainder of this year and 2003.

Opportunities

According to the Canadian Tourism Research Institute's latest Winter 2002 Travel Intentions Survey, a surprising 74 per cent of potential travellers indicated they will likely or very likely still take their winter trip if a war breaks out in Iraq. On the flip side, the survey indicated 26 per cent are not likely to go. Last year, after September 11th, safety concerns had more of an impact on outbound travel than they did on domestic travel. In fact, many planned outbound trips were replaced by domestic trips because of safety concerns. In the short-term, suppliers may find that targeting the domestic market will, once again, represent the safest bet to minimize risk, even with an escalation in political tensions.

The Japan Association of Travel Agents released a benchmarking study for suppliers interested in doing business with older Japanese citizens in the medium term. The survey, Travel by Next-Generation Senior Citizens, investigated what features are significant to travellers aged 50 to 59. According to the survey, these travellers will take trips more frequently and will become important clients to their travel agents. Overall, they intend to spend a great deal of money on special-interest tours but will economize on normal travel. As well, most Next Generation Senior Citizens intend to travel with their spouses and are very likely to select Canada or Oceania when they are looking for an ecotourism or green tourism experience.

Research from the Travel Industry Association of America (TIA) suggests Japanese have a preference for packaged travel, with older and female travellers most likely to choose a packaged tour. Among all travellers, the top motivating factors in selecting a destination are: best value for money; outstanding scenery; having fun and being entertained; shopping; going places not visited before; and having an opportunity to increase knowledge. Packaging tours and focusing marketing efforts on these factors will ensure a suppliers' product is competitive.

Leisure travel is poised to continue to lead the tourism recovery in the U.S. TIA research reveals Americans want to make a connection with family, their heritage or nature. Americans should have more time to travel because, for the first time in the nearly 30 years since the Harris Poll has been asking the question, the number of working hours decreased significantly. From 1973 to 1980, the number of hours spent working rose from 41 to 47. In 1994, the number of hours worked went up to 51, then dropped back to 50 in 1998. It had remained unchanged until this year when it fell back to 47.

Summary

As the tourism industry continues toward recovery, airlines, particularly U.S.-based airlines, are undergoing dramatic change. In the current operating environment, it appears that the most desirable business model for airlines involves some form of low-cost travel. With size and inflexibility working against them, many major airlines are now considering consolidation. For many, it appears the advantages of consolidation outweigh the costs. As the industry leans toward consolidation, the general consensus suggests low-cost carriers will have a more prominent role.

While the pace of recovery for Canada's tourism industry still exceeds that in the U.S., persistant gaps within the industry remain troubling. These gaps are not good for the industry because they are making the recovery less robust. Political uncertainty isn't helping either. According to the Canadian Tourism Research Institute's latest Winter 2002 Travel Intentions Survey, 26 per cent of potential travellers indicated they will not likely take a winter vacation if a war breaks out in Iraq.

Last year, after September 11th, safety concerns had more of an impact on international travel than they did on domestic travel. Even with an escalation in the current political situation, suppliers may find that targeting the domestic market will, once again, represent the safest bet to minimize risk. In addition, U.S. travel to Canada should also hold up well because Americans perceive Canada as a safe country.

For additional research information, please see
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