



## Domestic Market Helps Sustain Tourism Growth

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### Executive Summary

- Boosted by the stellar performance of the domestic travel market, the Canadian tourism industry finished 2006 with another year of positive growth, building on the solid gains achieved in 2005. Canada's international markets fell short of expectations, but strong growth in domestic travel offset these weaknesses.

The strength of the domestic market was especially apparent in the Canadian airline industry, which benefited from the significant expansion of domestic air travel demand. Domestic travellers also helped buoy the accommodations industry in 2006. But the decline in international visits weighed heavily on Canadian hotel room revenues, keeping growth modest.

- Unfortunately, Canada's U.S. travel market continues to decline, stifled by soaring energy costs, the crumbling U.S. housing market and the slowdown in the U.S. economy. Also, high gasoline prices continue to encourage more Americans to fly rather than drive to their holiday destinations, cutting further into Canada's beleaguered rubber tire market. At the same time, the relatively high cost of flying to Canada creates a distinct price disadvantage compared with U.S. domestic destinations, as well as some European ones. Confusion over passport requirements as part of the Western Hemisphere Travel Initiative (WHTI) is only exacerbating these challenges.
- The performance of Canada's traditional overseas tourism markets has also been troubling. The World Cup soccer tournament was partly to blame for poor visitation out of Europe last year, but the lack of a rebound in subsequent months suggests Canada's traditional European markets have largely matured, offering only modest growth potential. One issue is Canada's price disadvantage in a global marketplace that is increasingly competitive. Yet, the expansion of the global tourism market has also contributed to the emergence and growing importance of non-traditional tourism markets, such as China. As Toronto expands its role as a key gateway for Chinese visitors, more central and eastern Canadian destinations are gaining access to this rapidly expanding market.
- Looking ahead, overall growth in the Canadian tourism industry is expected to stay on the decelerating trend that began in the latter part of 2006. The domestic market is expected to lose some steam, in line with the more subdued outlook for the Canadian economy. Prospects for the U.S. travel market are not expected to improve either. The first implementation date for the WHTI is scheduled for January 23, 2007, creating another hurdle for U.S. visits to Canada. Meanwhile, the slowing European economy and the increase in the value added tax in Germany will likely limit growth and deter a strong recovery in overseas visits to Canada this year. However, the recent open-skies agreement between Canada and the U.K., and the Canadian government's plans to liberalize its air service agreements, have helped improve the outlook for Canada's overseas markets over the medium and long term.



## Consumer (Traveller) Overview - Canada and the United States

- **Consumer confidence supports improvement in winter travel intentions:** After exhibiting a "wait and see" attitude earlier in the fall, Canadian travel sentiment appeared to strengthen by October, supported by solid consumer confidence. The October 2006 Travel Intentions Survey by the Canadian Tourism Research Institute indicated that nearly 47 per cent of the Canadians polled intended to take a winter vacation between November 2006 and April 2007, up from 33 per cent a year earlier. Those planning to stay in Canada for their longest trip rose to 20 per cent, up from 12.4 per cent in 2005. Intentions for trips to the United States and other international destinations also rebounded.
- **Canadian business travel growth to level off:** The pace of growth in Canadian business travel is expected to level off slightly this year, according to a recent forecast by the Canadian Alliance of Business Travel. Most of the companies surveyed anticipated their travel expenditures will increase this year, although fewer expected their trip volumes to increase.
- **Vacation intentions of Americans appear stable:** The latest Consumer Confidence Survey report by the U.S. Conference Board, Inc. revealed that U.S. travel intentions remained relatively steady in December. Intentions for domestic trips were on par with the previous survey in October, but intentions for trips outside the U.S. had declined. Although consumer confidence appeared to improve in December, it is expected to remain volatile as household budgets react to low savings rates and high debt loads.

The Travel Industry Association (TIA) recently predicted that the pace of U.S. travel spending would slow over the winter travel season. The TIA estimated that growth in U.S. travel industry revenues reached 7.5 per cent in 2006, year-over-year, but will slow to 5.3 per cent in 2007.

- **U.S. weekend getaway trips on the rise:** The TIA's latest TravelScope revealed that American weekend getaway trips have increased by 10 per cent in the last five years. The shoulder seasons (April/May and September/October) are the prime times for weekend getaways. The report noted that weekend travellers spend more and participate in more activities than the average leisure traveller, fitting in as much as they can into their short trip.

## Travel Supplier Overview - Canada and the United States

- **Air travel demand remains robust:** Solid economic fundamentals and strong income growth in Canada have helped sustain robust levels of domestic air travel demand. Air Canada and WestJet both reported record-high load factors and solid increases in passenger traffic for 2006. The falling price of oil has also benefited the airlines, but neither has indicated plans to reduce fuel surcharges anytime soon. In fact, recent research showed that airfares are rising: in January, Air Canada's fares were up by an average of 4 per cent, year-over-year, while WestJet's airfares jumped 10 per cent.
- **Domestic travel helps offset weak international visits:** Strong domestic travel demand continues to support revenue growth for the Canadian hotel industry, despite the weak level of U.S. visits to Canada. PKF Consulting reported that revenues per available room rose 6.3 per cent between January and October 2006, compared with the same 10 months in 2005. According to HVS International, Canadian hotel demand increased 2.4 per cent during this period.
- **U.S. international air demand continues to grow:** U.S. airlines have also been benefiting from lower jet fuel costs and incremental airfare hikes. By early January, jet fuel prices had fallen to their lowest levels since December 2005. Demand for international air travel continues to drive growth in overall U.S. air travel volumes, while demand on domestic routes has levelled off.

## International Overview - Europe

- **U.K. demand for pre-packaged holidays continues to drop:** All the major U.K. tour operators have reported a drop in bookings for the 2006-2007 winter season, although MyTravel noted that its prices had increased over the previous year. Thomas Cook reported that demand for package holidays in the U.K. fell 8 per cent in 2006, in large part because of growing interest among travellers in building their own packages. Meanwhile, the Association of British Travel Agents (ABTA) expected a record number of outbound trips over the Christmas holiday period, noting that many skiers were expected to take advantage of the heavy snowfalls in parts of Canada and the United States as well as the favourable exchange rates.
- **Air France-KLM forms new venture to serve French leisure market:** Air France-KLM plans to launch a new low-cost carrier in the spring of 2007 to serve point-to-point medium-haul leisure routes under the brand of transavia.com, a partner in the venture. The new airline will focus on meeting the specific needs of French leisure travellers, who were described as preferring medium-haul destinations and being less likely to travel, overall, than other western Europeans. Air France-KLM said that most leisure travel growth in France is being driven by the Internet, where online travel agency bookings are growing much more rapidly than traditional package bookings.
- **German demand for longer holidays expected to soften this winter:** The overall performance of the German outbound travel market last year was disappointing, according to the *World Travel Trends Report 2006-2007* by ITB Berlin and IPK International. The report suggested the World Cup tournament was partly to blame for this trend, although demand picked up significantly in the latter part of the year. The report also noted that German online holiday bookings continue to register strong growth, driven primarily by the expansion of dynamic packaging. Looking ahead to the winter season, the report suggested that short breaks between November 2006 and March 2007 will increase 3 per cent, while longer holidays of five days or more are expected to decline slightly (-1%) from the previous year.

## International Overview - Asia-Pacific

- **Japanese senior and luxury segments offer strong potential:** H.I.S. Co. Ltd., a leading Japanese travel company reported strong growth in all its customer segments in 2006, despite a minimal increase (1%) in overall Japanese outbound travel. Looking ahead, the company plans to expand its Internet sales strategies, partly by launching an online hotel booking system, to cater to the growing Japanese online travel market. It also plans to launch new products aimed at seniors and affluent travellers, two travel segments that are expected to see above-average growth this year. The company expects that in 2007, continued growth in Japanese corporate earnings will help keep overseas travel demand on a "gradual upturn."
- **Korean outbound trips surge over holiday season:** Korean vacation package and air ticket sales for trips abroad during the Christmas holiday season nearly doubled this year over last, according to the *Korea Times*. Korean Air reported that Southeast Asian sun destinations and Japanese ski trips were especially popular. *Korea Times* suggested there was some pent-up travel demand from the summer, when the World Cup tournament kept many Koreans closer to home.
- **Australian outbound travel demand remains solid:** The strong Australian dollar continues to fuel overseas travel, and this trend is expected to continue at the expense of the domestic travel market. Tourism Australia recently forecast that outbound trips will increase at an average annual rate of nearly 4 per cent over the next 10 years, while domestic trips grow only 0.5 per cent annually.

## Tourism Leading Indicator Index - Summary Table

Because of the constantly evolving nature of today's travel environment, it is increasingly important to be able to anticipate fluctuations in travel demand, in order to make better business decisions. The Tourism Leading Indicator Index provides insights into the near-term outlook for the tourism industry, by tracking the progress of the economic and non-economic factors that affect travel demand from Canada's key tourism markets, including the domestic market.

The rating for each component of the index indicates how that component is expected to affect travel from the source market over the near term. Meanwhile, the overall rating indicates the expected performance of the source market in the near term, relative to the same time period in the previous year.

Travel Market	Economic Factors		Non-Economic Factors		Overall Tourism Leading Indicator
	General Economic Trends	Price Competitiveness	Traveller Trends (to/within Canada)	Supplier Trends (to/within Canada)	For travel to/within Canada
Domestic	↑	↔	↑	↔	+
U.S.	↔	↓	↓↓↓	↑	-
U.K.	↑	↓	↓	↑	0
France	↔	↔	↑	↑	+
Germany	↔	↓	↓	↔	-
Mexico	↑	↓	↑↑	↑	+
Japan	↓	↓↓↓	↓	↔	-
Korea	↑	↓	↑	↔	+
China	↑↑↑	↑	↑↑	↑	++
Australia	↑	↓	↔	↓	0

### Ratings Key:

#### Economic Factors and Non-Economic Factors:

Range from ↑↑↑ (significantly adds to demand) to ↓↓↓↓ (significantly impedes demand).

↔ represents neutral effect on demand.

#### Overall Tourism Leading Indicator:

Ranges from +++ (significantly improving) to --- (significantly deteriorating). 0 represents no change.

- **Economic Trends:** A more subdued economic environment persists. Fortunately, consumer spending and consumer confidence in most markets remain upbeat. Although lingering concerns exist about Canada's overall price competitiveness as a tourism destination, for the time being the gap in competitiveness appears to have stabilized and, for some markets, even been reduced.
- **Traveller and Supplier Trends:** Nothing significant has changed since the last index was reported, except that the U.S. travel market faces the additional hurdle of the passport requirement imposed by the implementation of the WHTI for air travellers returning to the U.S.
- **Overall Tourism Trends:** In general, there are few changes since the last index was reported. For the most part, there is small growth potential for most of Canada's key markets except China and the United States. On one hand, the Chinese market is expected to continue to generate solid growth. On the other hand, the U.S. travel market to Canada continues to struggle.

For more details on the travel demand of each market, as well as on the methodology used to produce the index, please refer to the full *Tourism Intelligence Bulletin* report.