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CRUNCH TIME!

More than ever hospitality managers across the industry are keeping a concerned eye on the economic downturn and for indicators that show the impact the credit crunch is having on their businesses.

Governments across the world have been taking emergency action to try to stave off recession and in the UK the Chancellor of the Exchequer's Pre-Budget Report was eagerly anticipated.

A key element of the statement was an immediate 2.5% reduction in VAT but some observers felt that this would not achieve the desired results.

The 2.5% cut in VAT from 17.5% to 15% by the Chancellor in his Pre-Budget Report, was not the best way to combat the looming recession, said VAT Director Debbie Jennings of PKF Accountants & business advisers. While it is clear that cuts in interest rates and income tax will give consumers more money to spend, a reduction in VAT will not necessarily encourage people to spend, nor benefit those most in need.

Debbie explained, "Experts agree that a cut in the rate of Sales Tax in Canada did not lead to increased consumer spending. Plus, there is no guarantee that all retailers will cut the price of their products.

"For example, this will make pricing difficult for retailers which normally offer goods at round sum prices and, in any case, many retailers are already offering much larger discounts in the run-up to Christmas. So any benefit for the rate cut is likely to be intangible and has to be seen more in the context of creating consumer confidence."

Debbie continued, "The other point to make is that consumers will only see a direct benefit from the cut in the rate of VAT if they physically spend their money on VAT-bearing goods and services. If all you require is a home, food, water and heat, then the VAT you pay out will be a relatively small amount because homes, food and water do not carry VAT and heating only a 5% rate of VAT which remains unchanged. Therefore it is the wealthiest consumers that will get the most benefit from a VAT cut, although increases in fuel duties, tobacco and alcohol will negate any benefit of the VAT rate cut on those items.

"On the business front, those that are unable to reclaim their VAT, such as banks and insurers, will benefit directly from the cut as their operating expenses will be reduced. Most other types of business will be unaffected financially, as it is a tax borne by the consumer, although they will incur the administrative costs of changing their systems and invoices to incorporate the new rate."

Debbie concluded, "Whether this works or not remains to be seen, but it will add to the country's quickly increasing levels of debt. However, we would expect in future for the rate to be increased, probably to 20%, as the Government seeks to balance its books."

Slow October for UK Hoteliers

So, what has business performance actually been showing? The latest statistics available are for October and they demonstrate that UK hotels experienced a slow October in terms of both occupancy and rooms yield, according to preliminary monthly figures released by PKF Hotel Consultancy Services. Room rate increased in some cities and both Liverpool and Leeds bucked the downward trend.

In London, room rate rose 0.1% on 2007 to £147.45, but the slowdown in business travel meant occupancy saw a 3.2% decline from 86.5% to 83.8%. Overall, this meant room yield was down 3.1% from £127.58 last year to £123.61 this year.

In the regions, occupancy was down 5.8% on 2007 from 77.2% to 72.7%. Room rate also fell 1.5% to £76.19 which meant rooms yield was therefore down 7.6% on 2007, from £59.70 to £55.42.

On a positive note, Liverpool still managed to make impressive gains due to its status for the year as European Capital of Culture. Room rate was up 1.2% from £81.98 to £82.93 while occupancy managed a 3.9% increase to 83.9% for the city. Overall, rooms yield jumped 5.1% from £66.26 last year to £69.61 this year.

Leeds was another northern city to experience some growth as rooms yield was up 0.6% on last year from £59.00 to £59.36.

On the flip side, Cardiff experienced more falls with a 9.4% drop in occupancy and a 16.8% decrease in room rate. As in September, the falls can be explained in part due by the Rugby World Cup matches which Cardiff played host to in 2007, boosting the city's hotels significantly.

Robert Barnard, partner for Hotel Consultancy Services at PKF, commented, "The continued global economic woes mean that the lack of growth experienced by many hoteliers in October, were to be expected.

"It is important to note that the falls overall were fairly moderate and the industry, while feeling the effects, is still holding its own. Occupancy in the capital is still at 83.8%, while in the UK as a whole, the hotels in our survey are at 72.7% of their capacity."

Downturn clearly felt

Meanwhile, the UK chain hotel market reported a 9 per cent fall in profit in October, according to the latest HotStats survey from TRI Hospitality Consulting. The amount of profit generated per available room – expressed as income before fixed charges (IBFC) – fell to a daily figure of £49.76 compared to £54.70 the same month a year earlier.

The lower profit was primarily attributed to higher costs and a shrinking pool of demand. The sample of 509 UK branded hotels reported a 3.2 percentage point drop in average occupancy to 77.4 per cent.

"For most UK hoteliers the effects of the economic downturn were clearly felt in October. With fewer guests and higher operational costs, pressure on profitability was inevitable," said Jonathan Langston, managing director, TRI Hospitality Consulting.

In the Provinces, average profit as a percentage of total revenue in October fell year-on-year from 37.6 to 35.1 per cent. An increase in the national minimum wage which came into force on 1 October may have contributed to the rise in costs. Provincial achieved average room rate dropped by 1.9 per cent to £73.72 which, combined with lower volume, led to an 11.2 per cent fall in daily IBFC to £36.88 per available room.

Profit grows in Liverpool and Newcastle

Some city markets bucked the trend, however, increasing both average room rate and profit thanks to local events. Liverpool's European Capital of Culture status made it a popular leisure destination during the half-term break, and a series of major football fixtures kept demand high. Average occupancy rose by 1.9 percentage points to 81 per cent. In Newcastle, the Great North Run helped daily IBFC increase by 6 per cent to £44.32 per available room.

"Even in a recession there will be demand peaks, and hoteliers will be able adjust their rates accordingly to gain the maximum benefit," said Langston.

Looking at the year so far, the first 10 months of 2008 show London still achieving positive albeit below-inflation revenue and profit growth. Total revenue per available room increased by 3.4 per cent to a daily figure of £137.28 and daily IBFC was up by 2.8 per cent to £63.90.

The Provincial data for the year so far shows a 1.4 per cent decline in total revenue to £100.04 per day per available room and daily IBFC PAR down by 5.3 per cent to £32.81.

Overseas spend down by 2 per cent

In the three months to September 2008, total overseas visitors to the UK decreased by 3 per cent to 9.3 million, according to the latest Government statistics. The amount they spent while in the UK dropped by 2 per cent to £5.14 billion.

Visitors from Europe were up by 2 per cent to 6.6 million, while those from North America dropped by 21 per cent to 1.2 million. Visitors from the rest of the world were down by 7 per cent to 1.5 million, compared to the same three-month period a year earlier.

In more recent data, BAA, the operator of seven UK airports including Heathrow and Gatwick, reported handling 12.4 million passengers during October, a year-on-year drop of 6 per cent. Year to date, BAA´s UK airport traffic shows a decline of 1.9% for the ten months to October at a total of 125.8 million.

Links:

PKF: www.pkf.com
TRI: http://www.trihc.com