

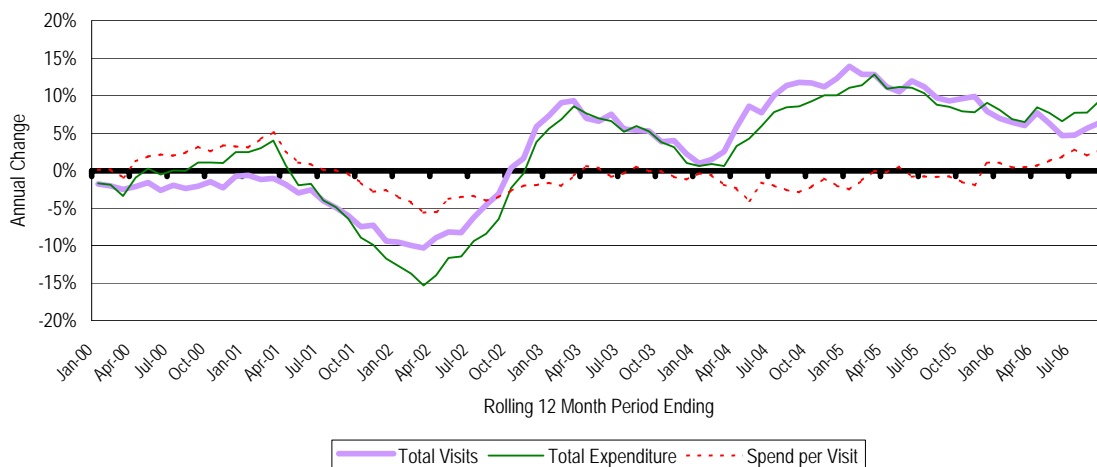


FORESIGHT is a monthly commentary on significant issues within the tourism sector. This month we take a look at the performance of inbound tourism during the first nine months of the year and look ahead to prospects for 2007. Both 'upside' and 'downside' risks to our forecast of the volume and value of inbound tourism are discussed, including changes to transport infrastructure, global economic trends and even new passport rules for US citizens.

January to September... the story so far

Figures from the International Passenger Survey<sup>1</sup> show that during the first nine months of 2006 the number of inbound visitors to the United Kingdom stood at 24.5 million, 7% up on the equivalent period of 2005, with spending 8% up on last year. The following chart highlights the fact that over much of 2006 spend has, for the first time in quite some while, been growing slightly ahead of visits.

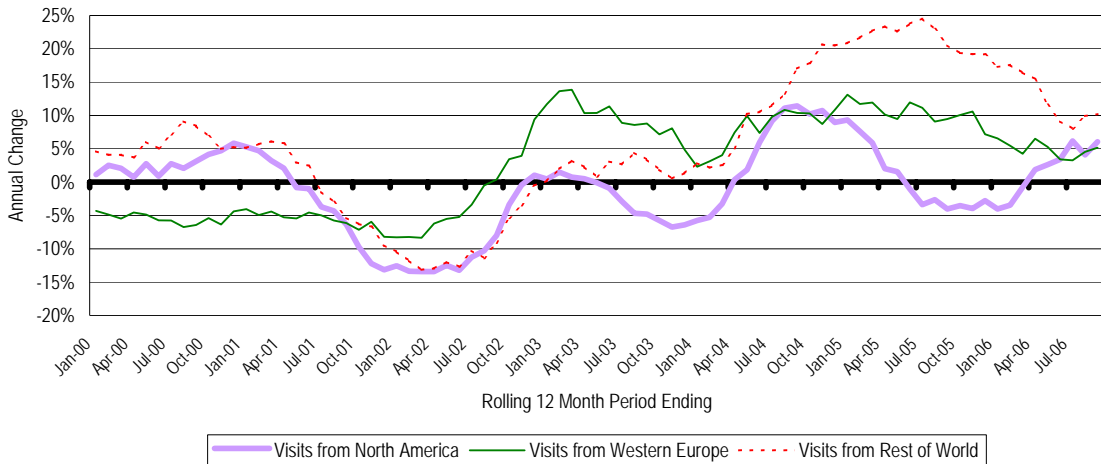
Trends in Inbound Tourism



What might be driving the improvement in spend per visit? One likely cause emerges from the next chart showing the growth in visits to the UK by region of the world. It is clear that visits from North America have been putting in a far stronger performance during 2006 than in recent years. Typically a visit from the US or Canada to Britain generates around twice as much as a visit from France or Germany.

Looking just at the first nine months of the year visits from North America and Western Europe are up 7% compared with the same period of 2005, with visits from all remaining regions of the world combined up 8%.

## Trends in Inbound Tourism by Origin Region

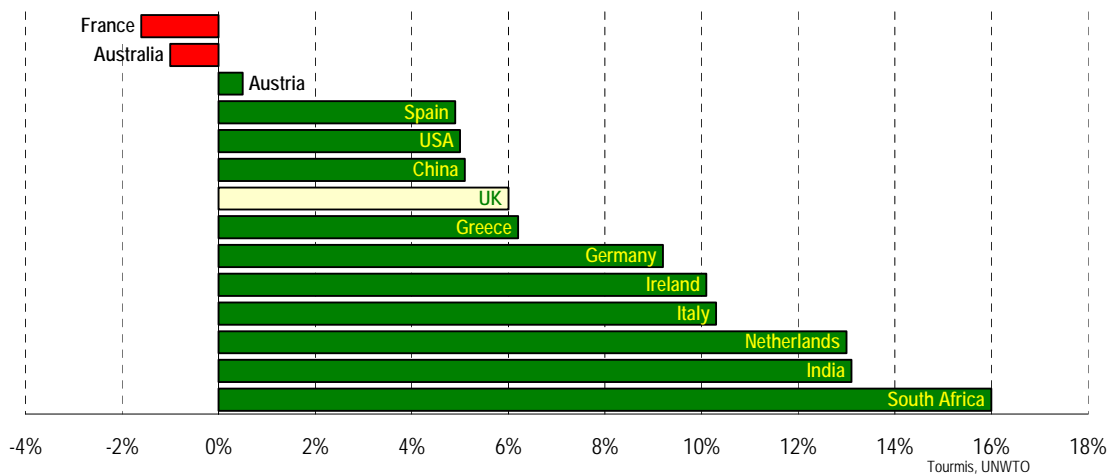


A drop in visits from North America was recorded in August, but this seems to have been a short-lived blip at odds with the trend for much of 2006, it remains unclear whether the poor August was linked to the disruption to air traffic caused by tighter security measures put in place following an alleged terror plot. The good news is that some of our most important 'emerging markets' for the coming years are putting in a very strong performance in 2006, with visits from Russia, China and India all up by double-digit percentages compared with 2005. The picture is not uniformly rosy, however, with visits from Japan and some parts of South East Asia down compared with 2005.

### How is the competition doing so far this year?

Most, but by no means all, major destinations routinely report monthly figures for the number of international visitors that they are attracting. The following chart summarises the 'year-to-date' situation for a selection of markets. Note that the period of 2006 covered varies by market, as do methodologies underpinning data collection, but we still get a flavour for the 'relative' performance of each destination.

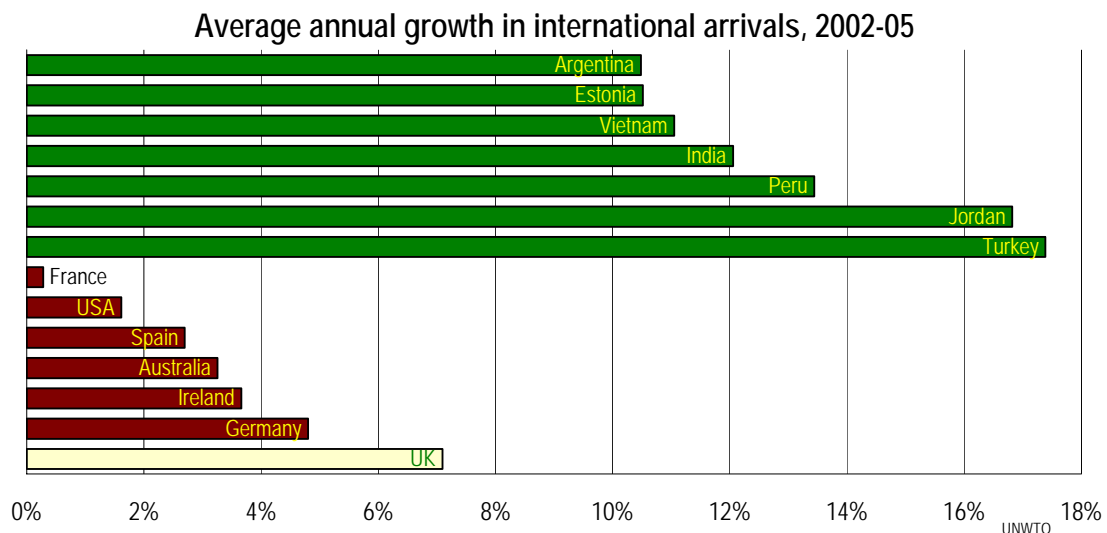
### Year-to-date growth



It is evident that Britain is performing strongly in comparison with many other destinations, but a mix of mature destinations such as Ireland and Italy, and emerging destinations such as India and South Africa are enjoying an even more successful 2006 than are we. Of particular note is the strong performance of Germany, with official figures showing exceptionally strong growth in international tourist arrivals during the period of the FIFA World Cup. Overall the United Nations World Tourism Organisation recently forecast that global international tourist arrivals would be 4.6% up in 2006.

### ...and over a longer time span?

The story emerging for 2006 is in line with that seen over the recent past, with Britain doing rather better than many of what we could term our 'traditional' competitors, but with a battalion of emerging destinations for international tourism outstripping our performance by a considerable margin. This is neatly illustrated in the following chart, highlighting that France, the most visited destination by international tourists, has stood still for the past four years, whereas the UK has seen average annual growth close to 7%, but destinations such as India and Turkey are growing at double-digit rates.



### Inbound volume and value forecasts for 2007

VisitBritain's 'central' forecast is that both the volume and value of inbound tourism will increase by 3.7% compared with 2006. If achieved this would mean that a record 32.5 million overseas residents will visit Britain next year, spending around £15.8bn. This compares closely to the UNWTO forecast for global international tourist arrival numbers to increase by 4% in 2007.

In nominal terms this forecast represents record spending, but we get a stark reminder that declining average spend per visit, driven by declining length of stay, has led to a 'real terms' fall in inbound visitor spending despite record numbers of visitor arrivals. Once we take inflation into account we discover that the central forecast of £15.8bn in 2007 is £650m lower than was achieved in the record year of 1996 – that's a loss equivalent to total spending by visitors from Australia (our sixth most valuable market).

	2007 Volume		2007 Value	
	Total (m)	Yr-on-Yr (%)	Total (£bn)	Yr-on-Yr (%)
Pessimistic	30.9	2.2	15.0	2.2
Central	32.5	3.7	15.8	3.7
Optimistic	34.3	5.2	16.5	5.2

This forecast is, of course, only indicative, being dependent on normal circumstances prevailing and does not factor in unexpected shocks caused by terrorism, health scares and other crises. There are numerous events that may lead to a better or worse year than the central forecast would indicate, hence the 'pessimist' and 'optimistic' scenarios shown in the table. An assessment of some of the 'upside' and 'downside' risks is discussed in the following sections.

### Global economic outlook

Looking at the latest set of economic forecasts released by the International Monetary Fund we find that in 2007 the major economies expected to enjoy the strongest growth rates include China, India and Russia (10%, 7% and 6.5% annual growth respectively), with the best performing 'developed' economies forecast to be South Korea, Australia and Canada (4.3% 3.5% and 3% respectively).

On the European front economic prospects have certainly started to look a touch brighter during 2006, with the European Commission recently indicating that it expected Eurozone growth to reach 2.6% this year, the best performance so far this century. However, the IMF is still cautious about the future expecting France to enjoy growth of 2.3% next year with German expansion limited to 1.3%.

A planned increase in VAT in Germany from January 2007 is thought to have fed through to a jump in consumer spending during the second half of 2006 as consumption of 'big ticket' items is brought forward to avoid the higher tax rates. It remains to be seen whether there will be a decline in consumer spending and consumer confidence during 2007 once the new tax rate is imposed.

The US has unemployment at 4.4% and job creation running at an annual 1.9%, but nonetheless widespread concerns about future prospects remain. Concerns centre on the recent slowdown in US productivity and the burgeoning US trade deficit, especially with China. There remains a possibility that we will witness further weakening in the value of the US Dollar in the coming year if a genuine slowdown in activity takes hold. Clearly Sterling becoming more expensive to visitors from the US due to exchange rate fluctuations would hinder Britain's attempts to recapture the record level of visitor spending by US visitors enjoyed back in 2000.

### Upside risks

The second phase of the Channel Tunnel High Speed Rail Link will open on 14 November 2007, at which point Eurostar services will migrate from Waterloo International to St Pancras. At the same time Ebbsfleet International will open, close to the M25 Dartford River Crossing, and the number of services that call at Ashford International will be curtailed.

There are a number of positive implications associated with the opening of the new rail link, including much improved service reliability and journey times being cut by around twenty minutes – trains from Paris will reach London in 2 hours and 15 minutes with those from Brussels taking just 1 hour 51 minutes.

In addition the move to St Pancras will open up new and improved journey connections, enabling inbound visitors arriving onboard Eurostar to transfer onto high-speed services operating out of St Pancras, Kings Cross and Euston to the Midlands, North of England and Scotland.

EU expansion will be in the headlines right at the start of next year as both Romania and Bulgaria gain full membership status. It is likely that this will result in a number of new air routes opening up as both legacy and low-cost carriers try to take advantage of the new opportunities on offer. Restrictions placed on the number of residents of the new member states taking up employment in the UK could mean that the increase in visitors is not as dramatic as that which we have seen from other Eastern European countries over the past two years.

Growing accessibility from both India and China (including low-cost flights from Hong Kong operated by Oasis), along with new bmi service from Moscow and increased capacity from the UAE should all help to allow further expansion in the number of visitors travelling to Britain from these important markets during 2007.

'Open skies' negotiations between the European Union and USA have spent much of the year bogged down, but slow progress continues. If an agreement can be struck in the months ahead we could see Trans-Atlantic air routes opened up to increased competition, almost certain to lead to new route developments and greater price competitiveness among carriers on high-volume corridors. All this sounds very positive, but it should be remembered that this will be an agreement between the US and EU, we could see the UK's congested hub airports losing out to mainland European airports with spare capacity in the race to attract new routes.

The importance of film and literary connections to the tourism industry was highlighted during 2006 by the unprecedented media attention associated with the Da Vinci Code. Britain, and in particular the Lake District, looks set to be in the spotlight again in the coming months with the release of the 'Miss Potter' film early in 2007.

According to Transport for London the UK will get a £115m tourism boost in 2007 courtesy of the Tour de France, with the Grand Depart being held in London for the first time, along with a second stage between London and Canterbury. As well as huge numbers of tourists lining the route, the race will showcase London and Kent to millions of television spectators around the world.

US citizens face a change in passport requirements from early next year meaning that if they are travelling to or from the US by air to Canada, Mexico or the Caribbean a full passport will be required. Over the coming years this new stipulation is likely to result in an increased proportion of US citizens owning a passport (thought to be little more than one-in-five at present). Clearly such a development would increase the size of the US population able to respond to messages encouraging travel to Britain without the added 'barrier' of needing to acquire a passport for such a trip.

## Downside risks

A year ago it was widely expected that by now some visitors from Singapore would be arriving at Heathrow on the world's largest airliner, the Airbus A380. However wiring difficulties have resulted in significant delays in the delivery schedule and it now looks unlikely that the first passenger carrying plane will touch down in Britain before next October.

A discussion on the price of oil could appear in either this section or that covering 'upside' risks, as in the past few months we have witnessed a long awaited decline in the price of oil, with some airlines reducing, but not eliminating, fuel surcharges. However, during 2007 geopolitical tensions in places as far apart as North Korea, Iraq, Nigeria and Venezuela could lead to the price heading upwards once more.

In only three out of the last twelve months has the amount of rainfall in England and Wales been above average, and although in the short term this is of course good news in driving home the message to potential inbound visitors that Britain is by no means always wet and foggy the longer term threat of drought remains. For many inbound holiday visitors our gardens and parks are an important attraction, were a significant water shortage to develop in 2007 the imposition of Drought Orders by water companies could have a serious impact.

Avian flu has been out of the headlines for a number of months following the discovery of a swan that had died from the disease on the Fife Coast earlier this year, but the virus has not gone away, and latest figures from the World Health Organisation reveal that in the first ten months of this year 109 humans have contracted the H5N1 virus, with 74 of these cases resulting in death.

The threat of terrorism returned in August this year with the foiling of an alleged plot to target Trans-Atlantic airliners. Heightened security measures resulted in the cancellation of over 2,000 flights in the immediate aftermath, but an EU-wide policy has finally been introduced governing what can and cannot be taken through security check-points. It is not expected that the events of August will have any significant longer-term impact on inbound tourism prospects.

The government recently launched a consultation on the fees it sets for issuing visas and administering immigration services. With a planned full rollout of biometric visas by spring of 2008 there is a risk that visa fees may be increased during 2007. Only a minority of visitors to Britain are required to obtain a visa, but countries covered by the requirement include some of our most important emerging markets such as China, India, Russia and Thailand. Not only would any increase in visa fees be a further blow following the significant rise imposed in July 2005, but the move to biometric visas will also place additional requirements on potential visitors.

To obtain a biometric visa each member of the travelling group will be required to have a ten-digit finger scan and have a digital photograph taken of them as part of the application process. This may result in some potential visitors having to make long journeys with their family in order to apply for a visa. Although both the US and Schengen countries are heading down the same road as the UK it looks likely that we will be one of the first major destinations to have implemented a comprehensive biometric visa application process.

Following on from publication of the Stern Review in late October the possibility of 'green taxes' being implemented has been in much discussion. The Swedish government announced plans

to introduce an aviation tax earlier this year, resulting in Ryanair announcing the withdrawal of a number of its flights to the country. However, the ruling party lost the general election and the new government has now dropped the proposal. This change has resulted in Ryanair deciding to reinstate its flights, hence an example of how any unilateral imposition of 'green taxes' could result in a loss of tourism revenue in one country with no overall change in the volume of aircraft movements, simply a redistribution of traffic away from one destination to another.

### **Beyond 2007**

Global Insight forecast average annual growth of 3% for inbound visits to Britain during the period 2007-2010, a figure in-line with UNWTO projections that indicate international tourist arrivals to Europe will grow at an average annual rate of 3% through to 2020. The common consensus appears to be that global tourism has now completed its 'bounce back' from the crises of 2001-2003 and is set to enter a period of more modest growth.

A trio of events on the horizon in 2008 are worthy of a mention. Firstly Heathrow Terminal 5 is due to open in March of that year, offering the opportunity for a step change in the quality of the arrival/departure experience for many of our inbound visitors, and likely to reduce flight delays caused by the unavailability of aircraft stands etc.

Secondly, Liverpool will be European Capital of Culture in 2008, consisting of at least 70 highlights - many of them free - the initial programme features concerts, commissions, exhibitions, festivals and premieres across all cultural genres, from public art, architecture, dance, fashion and film to literature, music, science, theatre and visual art. These events look set to attract both domestic and international visitors to the city.

Finally the Beijing Olympics will take place in the summer of 2008 and the closing ceremony marks the point at which London becomes 'the next Olympic host city' and can start to take advantage of the huge marketing opportunities that this provides.

Undoubtedly other events will unfold over the coming years that are not yet on the radar, but at this stage we can look forward to another solid year of growth for inbound tourism to Britain during 2007.

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