FORESIGHT
Issue 75 - January 2010

FORESIGHT is a monthly commentary on significant issues within the inbound tourism sector. 'Market Focus' discusses economic, social and political factors that underlie demand for tourism now and in the future. In addition, a spotlight is focused on a significant tourism issue. This month 'Market Focus' takes a look at what is happening in the so-called 'BRIC' markets in both economic and tourism terms, while 'Issue of the Month' considers the current state of UK and European aviation.

Market Focus – The BRIC markets

Brazil, Russia, India and China between them account for 42% of the world's population, have a combined landmass equivalent to 28% of all dry land and constitute 24% of the global economy. These figures from the US Census Bureau and International Monetary Fund are just a handful of the many statistical nuggets that can be used to make the point that the BRIC countries are simply too important too ignore.

In tourism terms the BRIC nations are not yet in the top flight, with Tourism Economics estimating that in 2010 outbound travel will constitute some 55 million trips. Even if we include trips from China to Hong Kong and Macau (which the 55 million figure does) the BRIC markets are forecast to account for just 6% of all international trips in 2010 (5% if Hong Kong and Macau trips are excluded).

Demographics

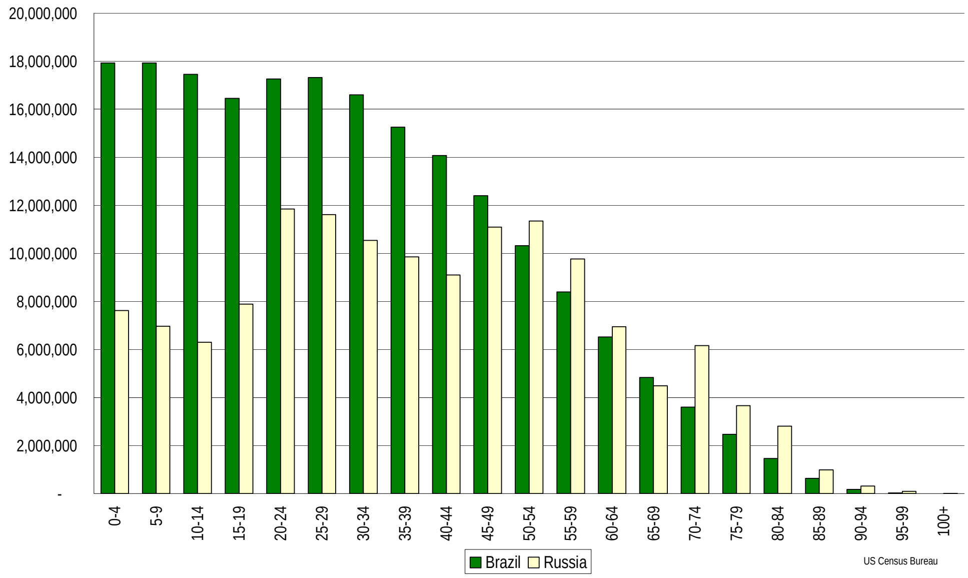
What is the demographic make up of the BRIC markets? Well in terms of population the table (based on forecasts for 2010 made by the US Census Bureau) reveals that while all four markets have a sizeable populous it is truly China and India that account for the largest shares.

	Population in 2010	Median age
China	1,347,563,498	34.4
India	1,173,108,018	25.9
Brazil	201,103,330	28.9
Russia	139,390,205	38.5

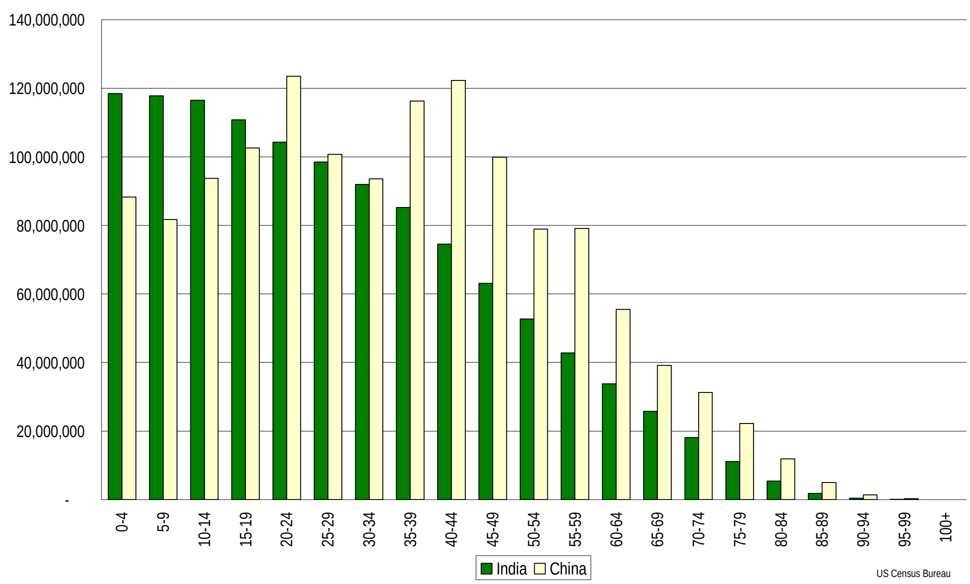
The following series of charts describe the age profile of the four markets in 2010 and we can readily see that India and Brazil have very 'young' populations whereas China and Russia have a flatter age distribution – the 'median age' column in the above table helps drill this point home, with a 13 year gap in the median age in India to that in Russia.

In understanding population dynamics we can start to identify which age groups of potential tourists are forecast to grow in size in the years ahead and which groups are set to diminish. The second series of charts presents US Census Bureau forecasts for population growth by five year age band over the period 2010 to 2020. In 2020 Brazil is forecast to be home to an additional 22 million whereas the resident population of Russia is set to contract by more than seven million. Meanwhile China is predicted to see population numbers increase by 83 million in the next decade while in India numbers will jump by 153 million.

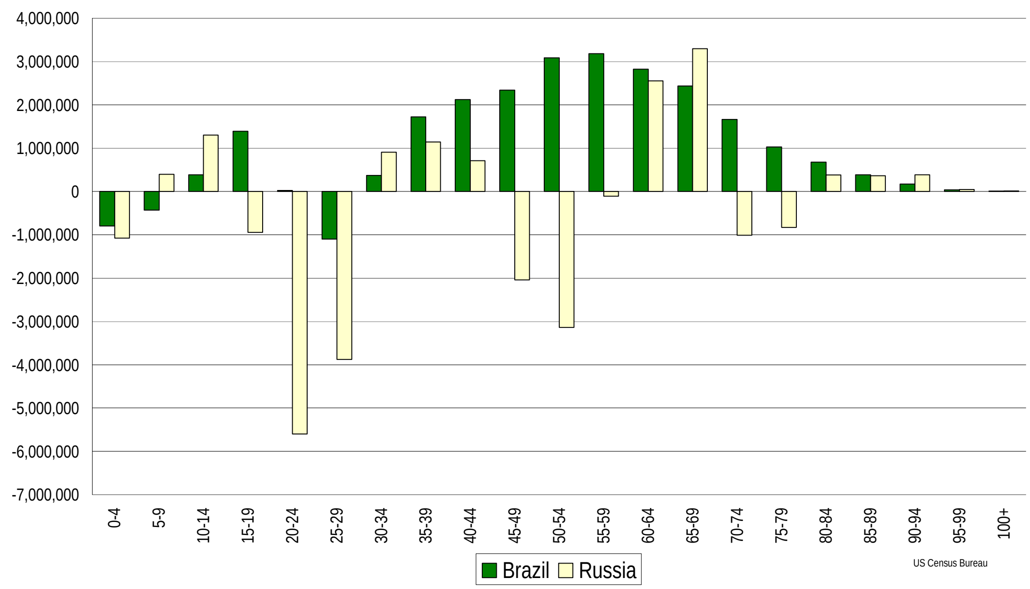
Population of Brazil and Russia in 2010



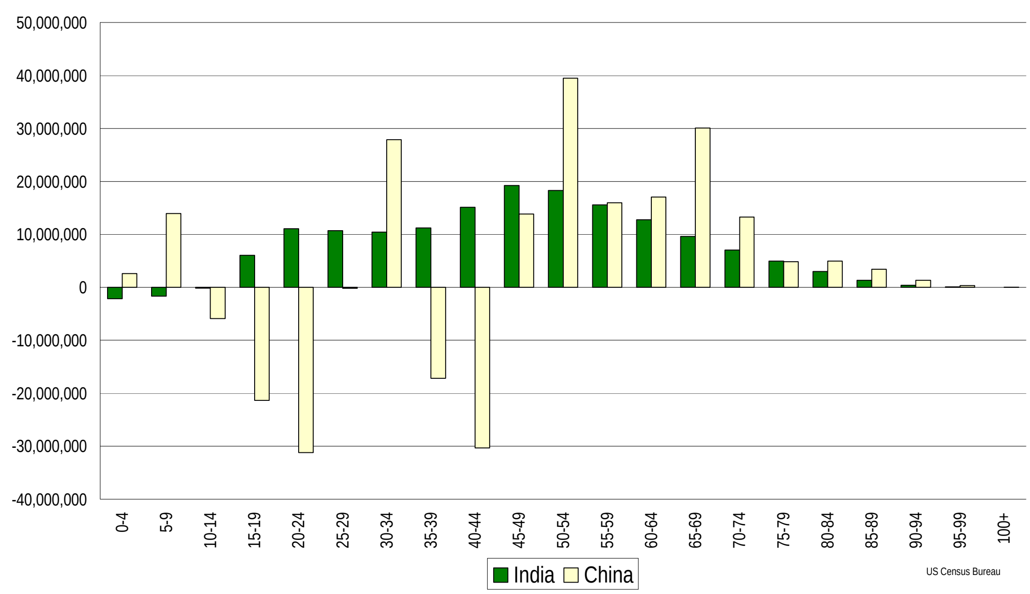
Population of India and China in 2010



Forecast population change 2010 to 2020 for Brazil and Russia



Forecast population change 2010 to 2020 for India and China

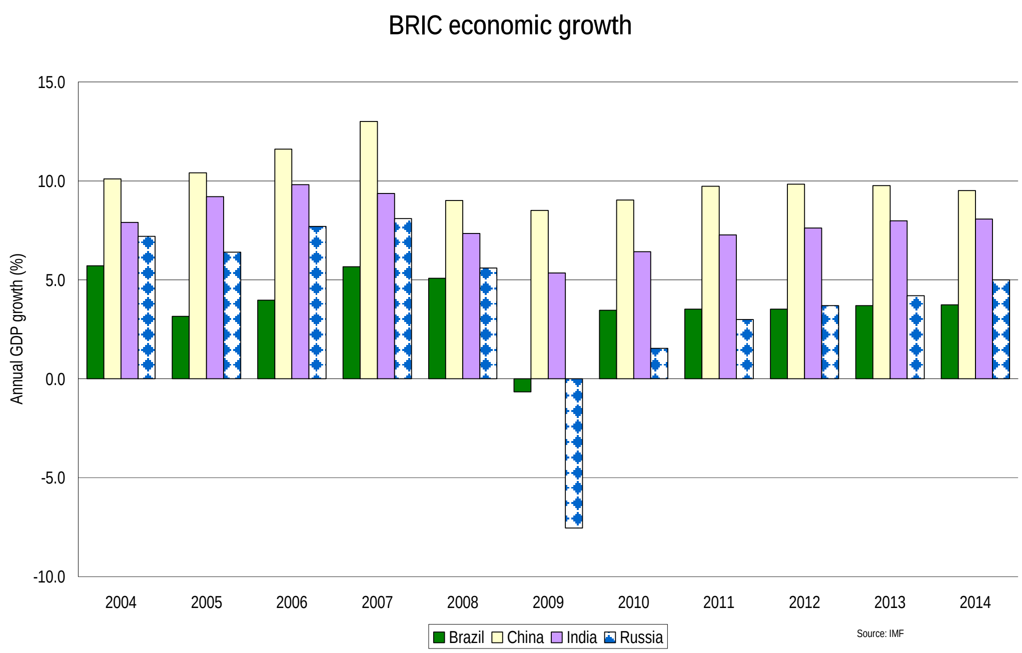


Brazil's population is forecast to increase in the majority of age cohorts, while in Russia the sharpest declines will be among those aged in their twenties and between 45 and 54. The population of India is expected to increase in all bar the very youngest age groups while in China the bulk of population growth will be due to rising numbers of people aged 45+.

Economics

We have already seen that the BRIC economies account for one-quarter of all economic activity on earth (compared with less than one-sixth back in 1992), and the International Monetary Fund forecast that this share will continue to expand in the coming years, reaching 27.4% by 2014. Both Brazil and Russia account for roughly 3% of global activity, India 5% and China very nearly 13%.

The following chart demonstrates why it is that the BRIC markets, and China and India in particular, have grown their share of the world economy. The IMF estimates and forecasts show the annual rate of economic growth, measured in terms of Gross Domestic Product for the period 2004 to 2014. Western economies are fairly cock-a-hoop if they get annual economic growth of 4% per annum, so China's relentless double-digit growth is truly exceptional even for a rapidly developing nation. It is apparent from the chart that only Brazil and Russia are forecast to have seen an economic contraction in 2009, with this being far more severe in Russia than in Brazil.

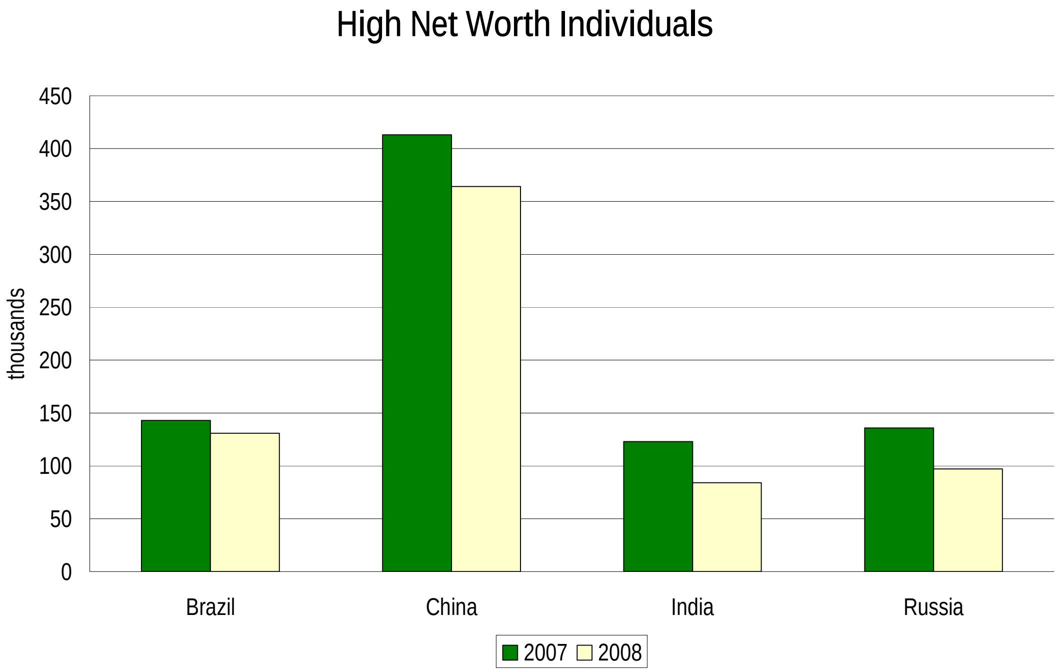


Although it is Russia that has faced the full icy blast of the global economic downturn, we can see from the table that in terms of income per head those living in Russia are by far the wealthiest (on average) of the BRIC nations, with per capita income five times greater than in India and twice that of China. Averages can, however, distort, especially when the denominator, in this case the population, is a large number.

Forecast GDP per capita (based on purchasing power parity) in 2010	
Russia	$15,617
Brazil	$10,882
China	$7,210
India	$3,125

From the following chart based on the Merrill Lynch Wealth Report we can see that there are many so-called 'High Net Worth Individuals' living in each of the BRIC nations. A HNWI is defined as someone with investable assets of US$1 million or more, excluding primary residence, collectibles, consumables and consumer durables. China was home to more than a third of a million High Net Worth Individuals in 2008, with Brazil in second spot at 131,000.

The global economic downturn has resulted in a sharp fall in the number of HNWIs in all four markets.



Perceptions

The following table pulls together a handful of the findings from the 2009 Anholt GfK Nations Brand Index Survey. Respondents are asked to rate many countries across a host of different dimensions. The results for the BRIC markets in relation to perceptions of the UK are shown for the overall Tourism, Culture and People dimensions.

	The UK's rank		
	Tourism	Culture	People
Brazil	13	10	15
China	7	4	7
India	2	4	5
Russia	5	5	9

Ranks are out of 50 so it is encouraging to see that the UK is consistently in the top half, but of note that Brazilians are less favourably disposed to the UK in terms of these dimensions than is the case in China, India or Russia. Respondents in India provide the most upbeat assessment of Britain as a tourism destination, its culture and people.

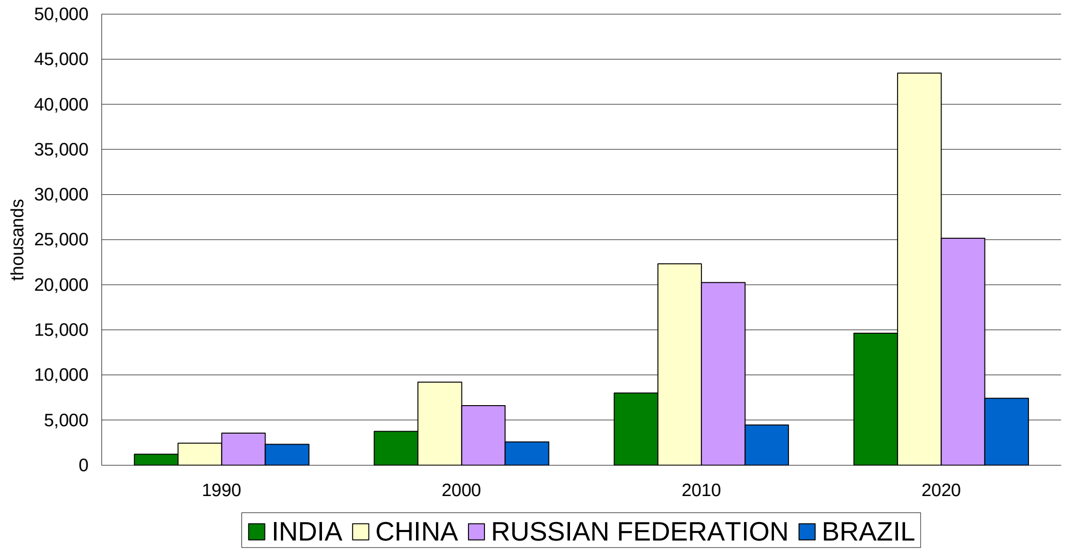
Outbound travel

The following series of charts show outbound visits from the four BRIC markets in 1990 and 2000 alongside forecasts for 2010 and 2020 based on Tourism Economics projections.

The first chart shows outbound travel to all destinations, revealing that during the 1990s China superseded Russia in terms of outbound volumes, a situation that is expected to persist in 2010 by a small margin.

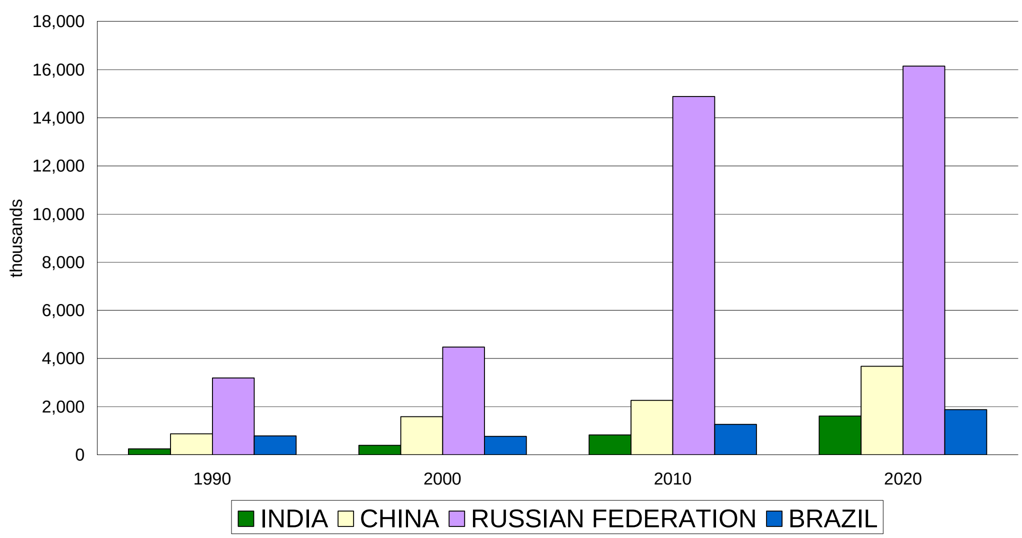
Between 2010 and 2020 the number of outbound visits from China is forecast to double to nearly 45 million while outbound growth from Russia is forecast to be much slower, with an increase from around 20 million to 25 million. Meanwhile during the coming decade outbound travel from India is forecast to grow substantially to 15 million trips per annum, but to put this in context Britons made nearly 70 million such trips in 2008.

Outbound tourism to all destinations - past, present and future

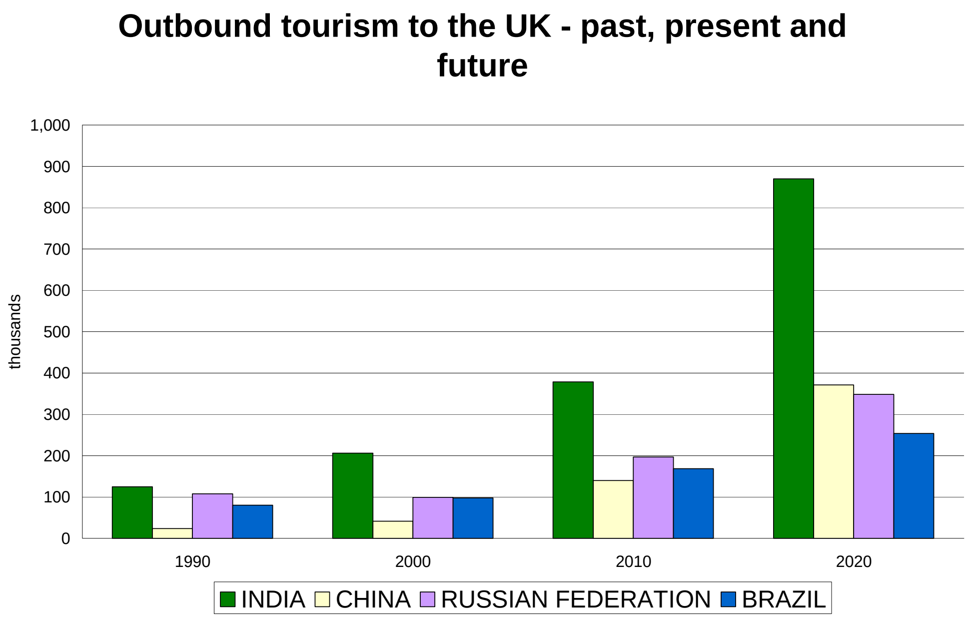


Looking at outbound travel where the destination is Europe it is apparent that Russia dominates, unsurprising given its geographic proximity. However, despite rapid growth in travel to Europe between 2000 and 2010 Tourism Economics expect sluggish growth during the following decade. By 2020 Europe is forecast to be welcoming 4 million visitors from China and 2 million from India (as a comparator back in 2000 the UK alone welcomed 4 million visitors from the USA).

Outbound tourism to European destinations - past, present and future



We find a different story if we focus on outbound visits to the UK. Back in 1990 the number of visits to the UK from India, Brazil and Russia was very similar at around 100,000. By 2000 the number of visits from India had doubled to 200,000 with visits from the other three markets being close to levels seen a decade before. By 2010 India is forecast to have forged further ahead with nearly 400,000 visits, roughly double that from the other three markets. A further doubling to nearly 900,000 visits per annum is forecast by 2020, with China having moved into second spot by that stage with nearly 400,000 visits per annum.



Global players

If current projections prove accurate a few decades from now the BRIC countries will be dominating the global economic stage, and with economic power will come greater influence in the arena of geopolitics. Equally the share of global tourism that is to, from and within the BRIC countries will grow over the years ahead, but just as is the case for today's 'developed' tourism source markets the majority of outbound trips will be intra-regional not inter-regional.

Nevertheless, the long-haul outbound market will grow too, so it is crucial that the UK positions itself ready to capture a growing market share of travel from these countries as millions of people enjoy income levels that permit regular international travel for the first time. This is about building awareness of the diversity that Britain has to offer, addressing perceived and real barriers that may inhibit travel to the UK, and ensuring that Britain is marketed in ways that maximises the undoubted opportunities that lay ahead.

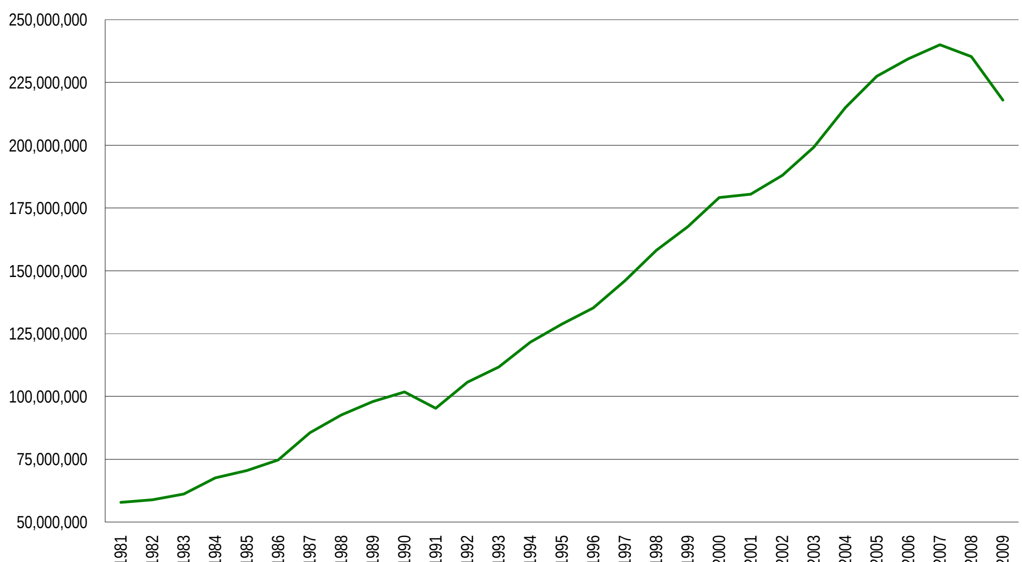
Issue of the Month – UK and European aviation

The Copenhagen Climate Change Summit has come and gone, with a conclusion that was perhaps more chaotic than an airport departure lounge after heavy snowfall, but one certainty is that the debate about how to influence the forecast climate outcomes in the decades to come will continue well into the future. Aviation will never be far from this debate and with three out of every four international visitors to Britain arriving by air, and more importantly these visitors contributing 86% of all inbound visitor spending (equivalent to £14.1bn in 2008), the health of UK aviation is critical to the vitality of Britain's visitor economy.

Long run growth shudders to a halt

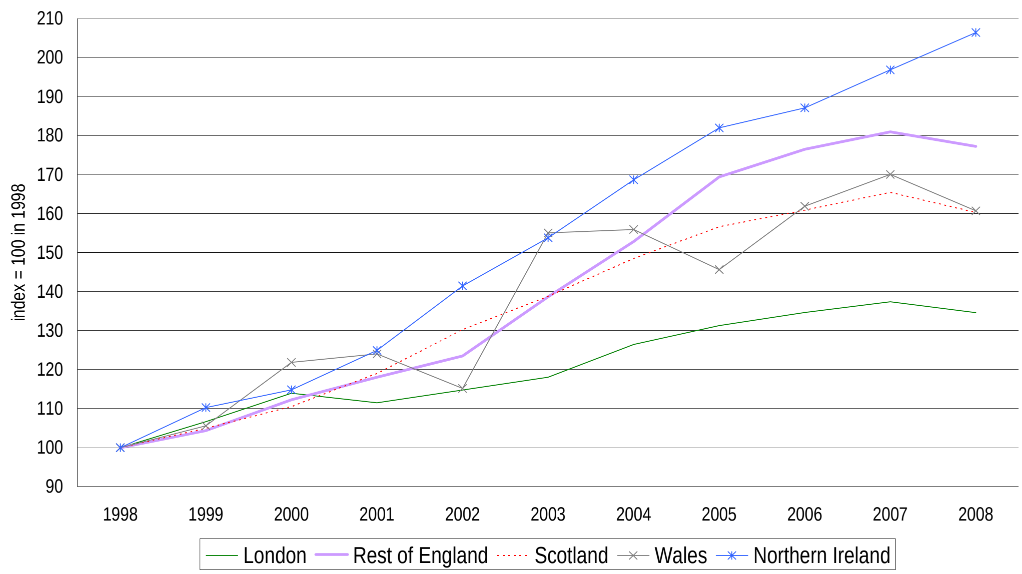
The extraordinary growth experienced in air travel to, from and within the UK over the past three decades is readily apparent from the following chart; when Ronald Reagan became US President UK airports handled 50 million passengers a year and by the time it was the turn of Barack Obama the figure was nearly five times as great. The peak year was 2007 with 240 million terminal passengers since when an unprecedented decline has set in brought on by the global economic downturn. Based on VisitBritain projections using provisional airport data for the first eleven months of 2009 we estimate that UK airports handled 218 million passengers in 2009, a decline of 10% on 2007.

Terminal passengers at UK airports



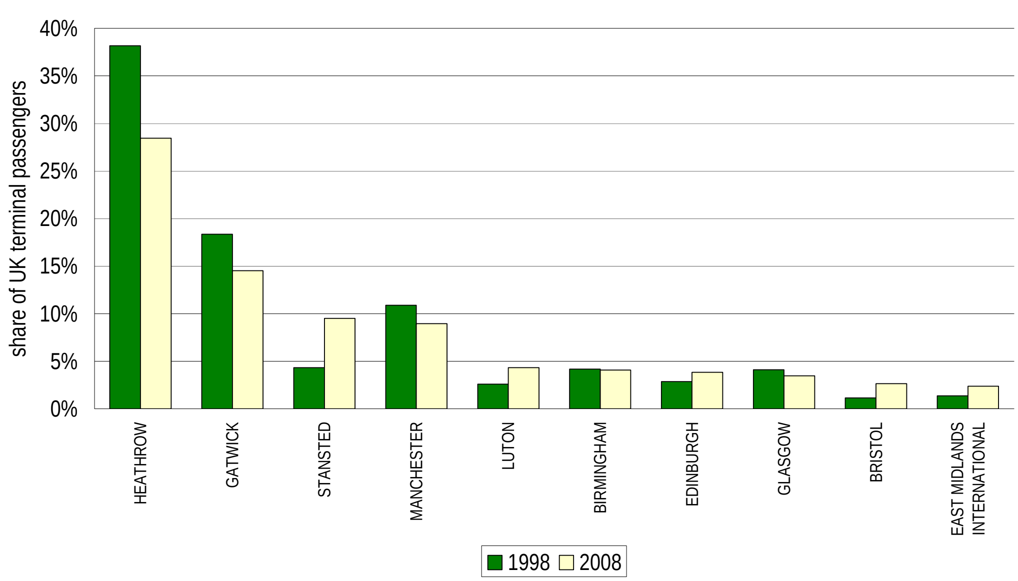
The growth that UK aviation has experienced in recent years has not been uniform across different parts of the country or across airports. The first of the following two charts looks at indexed growth since 1998 for London, remaining parts of England, Scotland, Wales and Northern Ireland, measured in terms of terminal passengers. We can see that passenger numbers at Northern Ireland airports has more than doubled with an increase of nearly 80% at airports in England outside of the London area. London area airports, where capacity constraints are most acute, have witnessed growth of 35% in the decade since 1998.

Airport terminal passengers



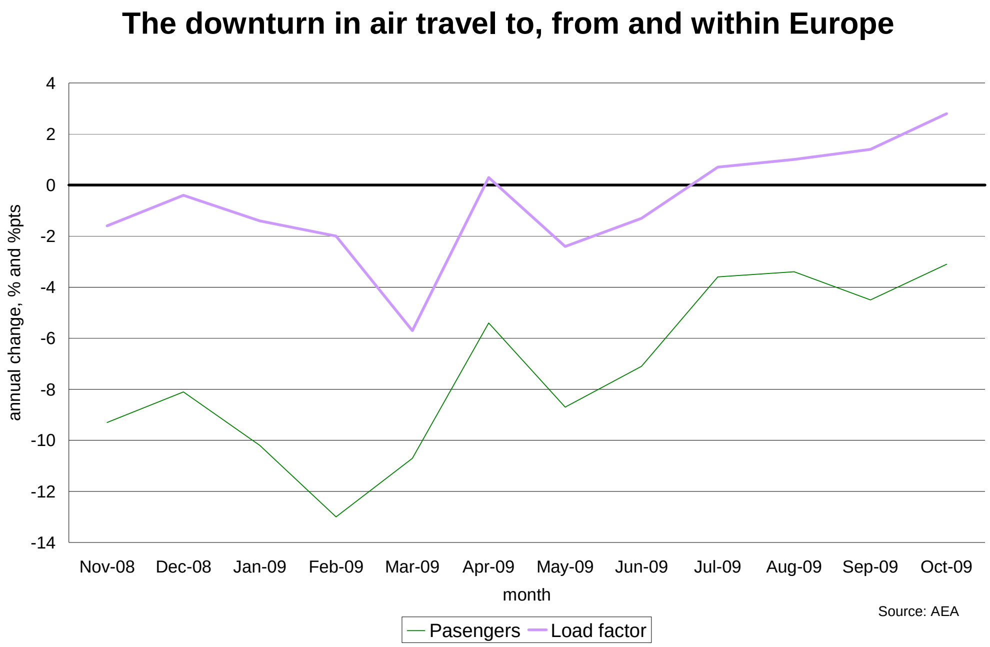
If we examine the share of terminal passengers by airport we can see that a small number of airports dominate the market, but there has been a significant shifts in recent times. Back in 1998 Heathrow accounted for 38% of all passenger traffic, just ten years later this figure is 28%. Gatwick's share has slipped from 18% to 15% whereas the only airport witnessing a significant increase in share is Stansted, moving from 4% of all passenger traffic in 1998 to 9% in 2008. Outside of the London area Manchester Airport has seen a decline from 11% to 9% of all traffic while Edinburgh, Bristol and East Midlands have grown their market share.

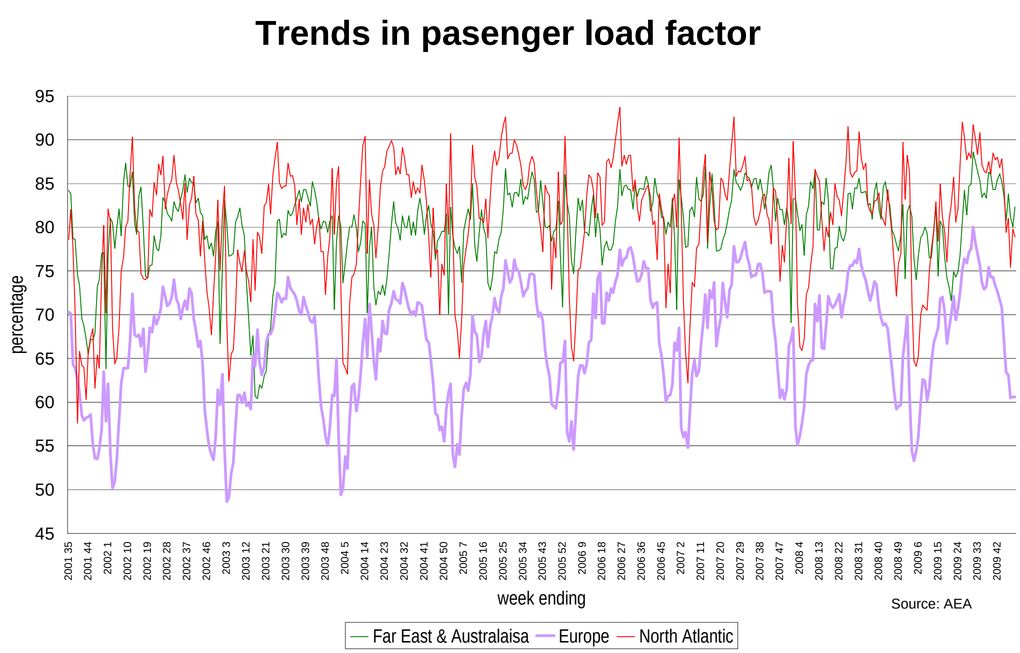
Share of terminal passengers - top airports



The European dimension

The downturn in air travel is by no means restricted to the UK. The following chart presents data published by the Association of European Airlines (representing most full service European carriers) for the period since autumn 2008. We can see that the number of passengers that European airlines carry has been declining substantially throughout the past year or so and that for much of the period load factors (that's the proportion of seats that are filled) has been in negative territory. However, brought on by capacity cuts and the use of smaller aircraft by operators load factors have been improving since late summer on an annual comparison basis.





Looking at average load factor for European airlines by route sector (the second chart on the previous page) over the past seven years reveals that long-haul routes consistently deliver higher load factors than do intra-European routes. We also notice that intra-European traffic is far more seasonal in nature than is long-haul traffic to and from Europe.

Can airlines make a profit?

So far we have looked at passenger volumes and load factors, but of course for airlines it is all to do with how much revenue they make, and the economic downturn has accelerated the trend for business travel to involve sitting at the back rather than the front of the plane or indeed to move from full service to low cost operators.

Airlines have found themselves between the proverbial rock and a hard place, with consumers demanding ever more competitive fares and operating costs having been impacted by rising oil prices (most markedly during the summer of 2008). Increased taxation on air travel in some markets, including the UK where Air Passenger Duty increased in November 2009 and is planned to rise further in November this year, makes for a challenging environment.

According to a recent American Express Global Business Travel Forecast airlines are planning fare hikes in 2010 in the region of 0-5% for economy class short-haul fares and 1-6% for long-haul premium fares. The list of global airlines that have failed in recent months continues to expand, with the likes of Sterling and Flyglobespan among the aircraft liveries no longer seen on UK runways. A number of flag carriers are struggling too, with Japan Airlines having been bailed out by the Japanese government.

The majority of airlines around the world probably had quite a long wish-list for Santa last month, with lower operating costs and customers willing to pay higher fares both being near the top. According to IATA (the International Air Transport Association) the collective losses of global airlines (excluding many low-cost carriers) in 2009 was $11bn, with the forecast for 2010 set at a loss of $5.6bn.

In the UK British Airways has been the focus of much media attention over recent months with the airline expecting to make a sizeable loss in the current financial year on the back of a loss of £401m in 2008/9. While the planned 12 day strike by cabin crew was deemed illegal by the High Court the company and Unite Union are yet to settle their dispute, making for an uncertain start to 2010. One bright note for the airline was its recent announcement that after just three months the double-daily all business class flights between New York and London City are making a profit.

British Airways is by no means alone in facing a challenging environment, recently Lufthansa took down the 'For Sale' sign that it had placed on bmi on the grounds that now was not the best time to sell, but in order to shore up finances bmi has axed a number of routes in recent weeks freeing up lucrative slots at Heathrow.

Economic worth

A recent Oxera report investigated the economic importance of the UK aviation sector. The study found that in 2007 the sector **directly** generated £8.8bn of economic output, equivalent to 0.7% of the total Gross Value Added of the UK economy. If all of the supply chain effects are allowed for then the economic worth of the aviation sector is estimated at £18.4bn, or 1.5%

of the UK economy. Oxera found that the aviation sector directly underpins 141,000 jobs in the UK, rising to 234,000 (0.85% of total UK employment) once supply chain effects are included.

Looking at the amount the aviation sector directly contributes to the Exchequer in terms of tax revenues the report estimated a figure of £4.8bn in 2007/8, equivalent to 0.9% of tax revenues, a figure that increases by £3bn once the supply chain is allowed for. Oxera note that before allowing for Air Passenger Duty aviation contributes 32.5% of the wealth it generates in tax, a very similar proportion to the UK economy overall at 32.1%.

If APD is taken into account the tax contribution of wealth generated by the aviation sector (in GVA terms) increases to 54.5%. The report notes that 'the tax burden faced by the UK aviation sector is currently higher than that faced by other European countries'.

Emissions trading

The European Commission intends to start implementing emissions trading on flights to, from and within the European Union from 2012 onwards, and while costs will be borne by the airlines there seems little doubt that airlines will consider passing these additional costs on to the travelling public. According to Ascend Aviation Insight based on typical load factors the additional cost per passenger for a short-haul flight within Europe would be €3, for a visitor returning from Britain to the Eastern Seaboard of the USA €12 and to return to the Fare East €25.

The EU Emissions Trading Scheme (ETS) will require all airlines regardless of nationality that operate within EU boundaries to submit emissions reports. Any airline that breaches carbon limits set by the EU will be permitted to buy 'carbon emissions' from other airlines that are operating below their quota. If an airline fails to comply with the scheme it will face penalties and ultimately could be banned from flying within the EU.

According to the EU while the EU's total greenhouse gas emissions declined by 3% between 1990 and 2002 emissions from the aviation sector increased by nearly 70% despite improvements in aircraft technologies and operational efficiency. The EU believes that its scheme will serve as a model for emissions trading schemes adopted by other countries or groups of countries meaning that the EU ETS 'can form the basis for wider, global action'.

It is going to be a bumpy road ahead before the EU scheme is fully operational and not just in terms of setting up the technical and administrative aspects. The US Air Transport Association recently announced that it planned to sue the European Union over the planned scheme and launched court action in London citing that the scheme 'violated US-EU bilateral Air Transport Agreement of 2007 and the Kyoto protocol'.

The main complaint by the US airlines is that aviation emissions trading should be tackled on a global sectoral basis rather than through the actions of individual countries or groups of countries. Although not as strident in their opposition, IATA has aired its concerns about the planned EU scheme but has said that airlines should plan to comply 'under protest'.

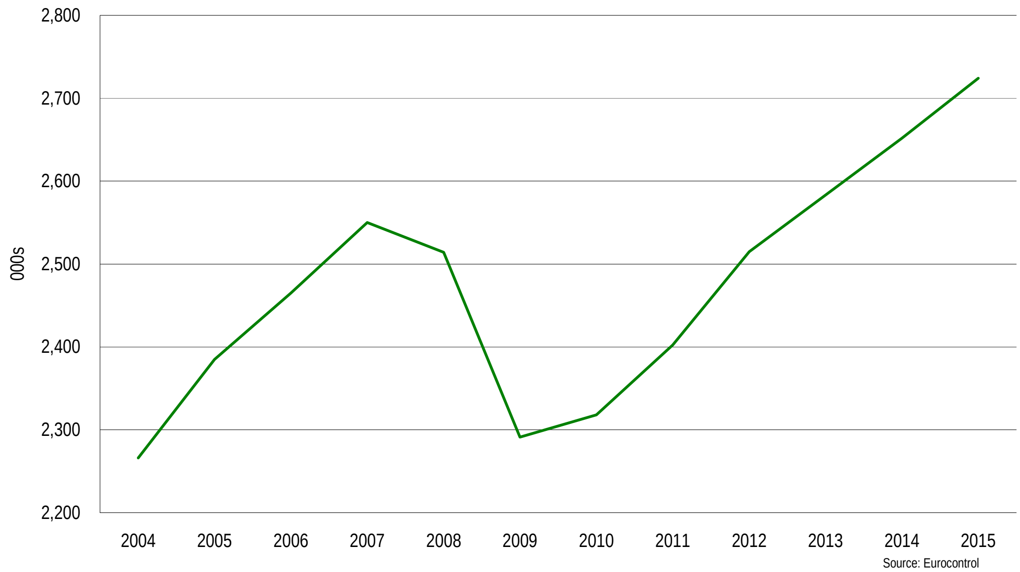
Will growth resume?

According to Eurocontrol (the European Organisation for the Safety of Air Navigation) estimates for the number of flight movements, air traffic to, from and within the UK peaked at

2.55 million movements in 2007. As is evident from the following chart the downturn that set in during 2008 accelerated in 2009, taking the number of movements down to 2004 levels at about 2.3 million. If Eurocontrol forecasts prove to be correct growth in 2010 will be at best mediocre, with 2007 levels not expected to be exceeded until 2013.

Many airlines have responded to the slump in demand for air travel by renegotiating orders for new aircraft or by cancelling orders altogether. Indeed, Ryanair recently announced that its negotiations to purchase a further 200 aircraft from Boeing ended unsuccessfully and that it was to bring forward plans to significantly reduce growth and capital expenditures during the period 2012 to 2015.

Flight movements in the UK, past, present and future



Given the undoubted importance of aviation to the UK economy in general, and inbound tourism in particular, it is very encouraging that there are now signs of a recovery in passenger demand (though the wintry weather hitting both the UK and many parts of Europe and North America could result in a gloomy set of traffic figures for December 2009) and that the global economy is recovering.

Boom times for UK or global airlines are not just around the corner. The sector will face a new raft of challenges over the coming years outwith the normal turbulence caused by fluctuations in demand and supply. Global political leaders will continue to grapple with climate change and how to tackle it over the next few years, and it is vital that aviation is treated firmly but fairly in this regard.

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Index		Market Focus	Issue of the Month
Issue 1	November 2003	USA, Canada and Mexico	Implications of an ageing population in Britain
Issue 2	December 2003	France, Italy, Portugal and Spain	Airport capacity in Britain
Issue 3	January 2004	Poland, Russia, China and South Korea	Visits to Britain by British Nationals living overseas
Issue 4	February 2004	Britain	School holidays and their impact on seasonal spread
Issue 5	March 2004	Australia and New Zealand	West Nile Virus
Issue 6	April 2004	The EU Accession States	
Issue 7	May 2004	South Africa, Nigeria, Kenya and Ghana	The Internet Part 1: Consumers
Issue 8	June 2004	India and Pakistan	The Internet Part 2: Businesses
Issue 9	July 2004	Belgium, Netherlands, Luxembourg and Ireland	Trends in Cross-Channel Travel Behaviour
Issue 10	August 2004	Japan, Hong Kong, Philippines and Taiwan	Cost of visiting Britain compared with other destinations
Issue 11	September 2004	Brazil, Argentina, Chile and Venezuela	What might climate change mean for tourism in Britain
Issue 12	October 2004	Norway, Sweden, Denmark and Finland	London's Olympic Bid – implications for British Tourism
Issue 13	November 2004	Britain	Smoking in public places
Issue 14	December 2004	UAE, Saudi Arabia, Kuwait and Iran	Outlook for inbound tourism to Britain in 2005
Issue 15	January 2005	Germany, Austria and Switzerland	Inbound tourism and the value of Sterling
Issue 16	February 2005	Malaysia, Thailand and Singapore	Britain's ethnic diversity
Issue 17	March 2005	Greece, Romania, Bulgaria and Croatia	Britain's transport infrastructure
Issue 18	April 2005	Israel, Egypt and Turkey	Foreign Direct Investment & inbound business tourism
Issue 19	May 2005	Poland, Czech Republic and Hungary	Inbound study visits
Issue 20	June 2005	USA, Canada and Mexico	Low-cost Airlines
Issue 21	July 2005	France, Italy, Spain and Portugal	Weddings, Stag Weekends and Hen Weekends
Issue 22	August 2005	Latvia, Lithuania, Estonia, Ukraine and Belarus	The Day Visit Market
Issue 23	September 2005	Russia and China	Quality
Issue 24	October 2005	Australia, New Zealand and South Africa	Daylight Saving
Issue 25	November 2005	India, Sri Lanka and Bangladesh	Outlook for Inbound Tourism in 2006
Issue 26	December 2005	Twenty-five years of Inbound Tourism	
Issue 27	January 2006	Benelux and Ireland	Tourism Satellite Accounts
Issue 28	February 2006	Japan, South Korea and Hong Kong	Tourism and the Disability Discrimination Act
Issue 29	March 2006	Brazil, Argentina and the Caribbean	Tourism and the National Lottery
Issue 30	April 2006	Nordic region and Iceland	Next generation aircraft
Issue 31	May 2006	Central Europe	The cruise line boom
Issue 32	June 2006	UAE, Kuwait, Bahrain and Oman	The power of football
Issue 33	July 2006	North Africa, Malta and Cyprus	Wind Farms and the Visitor Economy
Issue 34	August 2006	Inbound tourism - the global context	
Issue 35	September 2006	Singapore, Malaysia and Thailand	International tourism balance of payments deficit
Issue 36	October 2006	Greece, Turkey, Bulgaria and Romania	Inbound visitor decision lead times
Issue 37	November 2006	Inbound visits by the over 55's	Seasonality
Issue 38	December 2006	Outlook for Inbound Tourism in 2007	
Issue 39	January 2007	USA and Canada	Second homes
Issue 40	February 2007	Ferry passenger visitors	Accommodation choices
Issue 41	March 2007	What will shape tourism in the next decade?	
Issue 42	April 2007	The value of tourism in the UK	Holiday activity perceptions (Part 1)
Issue 43	May 2007	India and Japan	Holiday activity perceptions (Part 2)
Issue 44	June 2007	Inbound holiday visitors	The role of nature and wildlife in UK tourism
Issue 45	July 2007	The changing face of overnight domestic tourism	
Issue 46	August 2007	Inbound visitors using the Channel Tunnel	The impact of the Channel Tunnel Rail Link
Issue 47	September 2007	Inbound visitors aged 16-24	Climate change and what it might mean for UK tourism
Issue 48	October 2007	Special edition: Inbound visitors' travel group composition and 'activity mix	
Issue 49	November 2007	Poland, Czech Republic and Hungary	The Credit Crunch
Issue 50	December 2007	Outlook for Inbound Tourism in 2008	
Issue 51	January 2008	Inbound 1-3 night visits	The British Weather
Issue 52	February 2008	Lesser known Asian markets	Heathrow Terminal 5
Issue 53	March 2008	The Middle East	The EU/US Open Skies Agreement
Issue 54	April 2008	Inbound visitors staying 15+ nights	Domestic consumers and the 'credit crunch'
Issue 55	May 2008 (Updated December 2009)	Special edition: Business tourism	
Issue 56	June 2008	The DCMS 'Taking Part' Survey	
Issue 57	July 2008	USA	Inbound visits to friends and relatives
Issue 58	August 2008	Russia and China	The Olympic and Paralympic Games
Issue 59	September 2008	Camping and caravanning	Day visits – motivators and barriers
Issue 60	October 2008	Visits to visitor attractions	Five years on from the Aviation White Paper
Issue 61	November 2008	Turkey	Information sources: usage and reliability
Issue 62	December 2008	Outlook for Inbound Tourism in 2009	
Issue 63	January 2009	Britain as part of a multi-country trip	The Euro
Issue 64	February 2009	Special edition: Forty years since the Development of Tourism Act	
Issue 65	March 2009	Latin America	The value of the visitor economy
Issue 66	April 2009	What do inbound visitors do?	Immigration and emigration
Issue 67	May 2009	Holiday intentions of Europeans	UK and global economic outlook
Issue 68	June 2009	Lesser known African markets	Global action to support tourism during the downturn
Issue 69	July 2009	Gender of inbound visitors	The importance of coach travel for UK tourism
Issue 70	August 2009	Global tourism trends	Destination inspiration sources
Issue 71	September 2009	Special edition: Inbound visitor activities in 2008	
Issue 72	October 2009	'Miscellaneous' inbound visitors	Monarchy and inbound tourism
Issue 73	November 2009	Inbound visitors who travel by car	Knowledge of the exchange rate and impact on travel
Issue 74	December 2009	Outlook for Inbound Tourism in 2010	