

Allianz Research

Back to the beach: Tourism rebound in Southern Europe?

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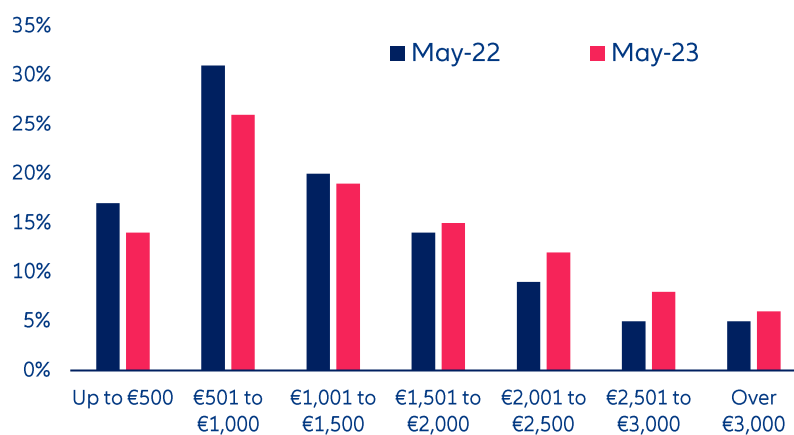
EXECUTIVE SUMMARY

- **Will surging travel prices wash out Southern Europe's all-important summer season?** Beach holidays are the top choice for leisure trips (30.3%) but 41% of European travelers expect to spend more than EUR1,500 on their holidays this summer, up from 33% last year. Nevertheless, we find that an average one-week beach holiday in Southern Europe is still far cheaper than the Caribbean, Australia and the US, and on par with many premium destinations in Latin America, Africa and South-East Asia. And higher prices do not seem to be deterring holiday plans: Revenue per passenger kilometer (RPK) for trips within Europe already reached 92% of the 2019 level during the first quarter of 2023, while air-ticket sales volumes for the May-to-September have also reached 91% of the 2019 summer level.
- **Yet, Southern Europe is caught between the devil and the deep blue sea.** Tourism accounts for the largest share in total gross value added in Croatia (11.3%), closely followed by Portugal (8.1%), Greece (7.7%), Spain (6.9%) and Italy (6.2%). This results in a bad equilibrium of strong structural dependence on foreign tourists and an increasing vulnerability to exogenous shocks (such as the pandemic). It also risks perpetuating the region's inherent structural problems of low-skilled jobs and low productivity.
- **Southern Europe needs to invest in sustainable tourism practices to ensure the preservation of natural environments and cultural heritage for future generations.** Enhancing infrastructure, including transportation networks and accommodation, can also improve accessibility and cater to diverse traveler preferences. And promoting off-season tourism and diversifying offerings beyond traditional beach holidays can also help attract visitors throughout the year.

A day in the sun?

Will surging travel prices wash out Southern Europe's all-important travel season? As of May 2023, 70% of Europeans intended to travel this summer, and beach holidays are the top choice (30%), followed by culture and heritage getaways (16%). However, 41% of travelers also expect to spend more than EUR1,500 on their summer vacations this year (up from 33% last year). Besides food, lodging in particular has become more expensive amid skyrocketing demand and hotels raising rates to cope with higher energy bills and labor costs. The daily rate for a hotel room (global median) has jumped to USD212 as of Q1 2023, up from USD156 in 2022 and USD129 in 2021. But that has not deterred travelers: The median occupancy rate for hotels also continues to increase (from 48% in 2021 to 62% today, the pre-pandemic 'normal' was 71%). As a result, the global RevPAR¹ has increased from USD62 in 2021 to USD84 today.

Figure 1: Planned budget* of European travellers for the summer period (May 2022 vs May 2023 survey)

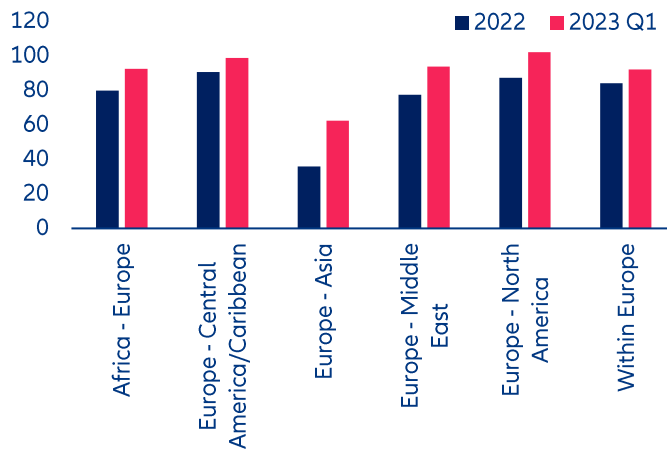


Sources: European Travel Commission, Allianz Research. Note: */ per person & per trip, including accommodation, transportation and travel activities.

In fact, intra-Europe travel is forecasted to grow by +20% y/y this year, accounting for about 515mn arrivals (or 89% of the total number in 2019), and by +14% y/y in 2024. Revenue per passenger kilometer (RPK) for trips within Europe already reached 92% of the 2019 level during the first quarter of 2023 (Figure 2). In volume terms, air-ticket sales in Europe for the May-to-September travel period have also reached 91% of the 2019 summer level.

¹ RevPAR: Revenue per available room. It measures the average revenue earned per available room over a specific period of time. RevPAR is calculated by dividing a hotel's total room revenue by the total number of available rooms.

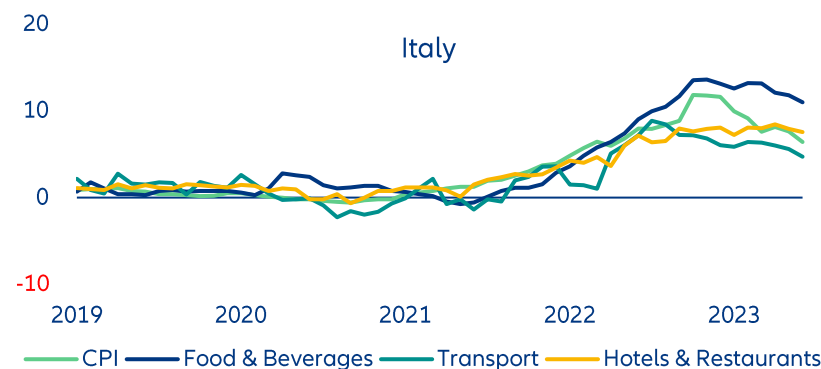
Figure 2: International RPKs by route area (% relative to 2019 level)

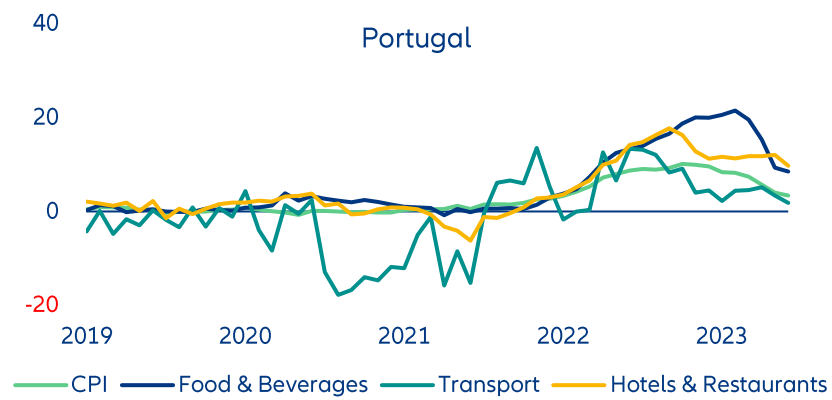
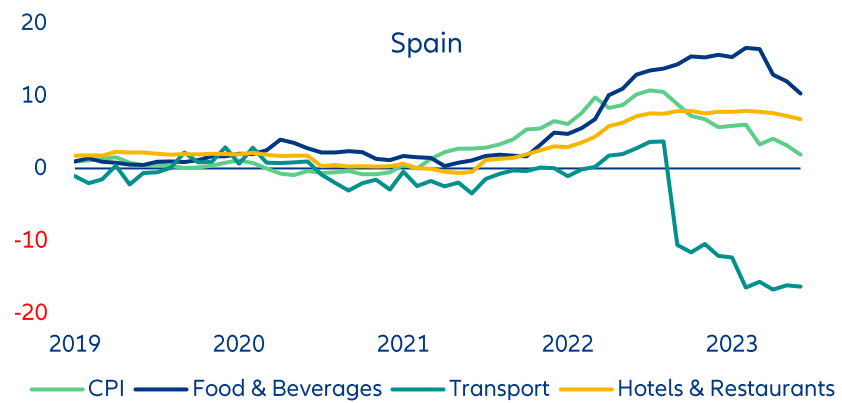
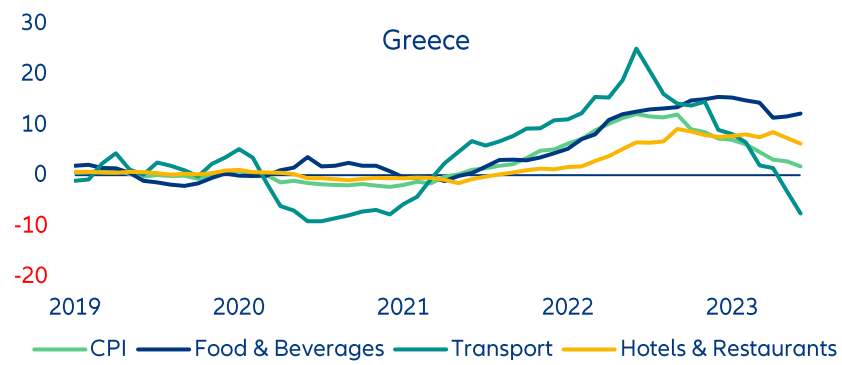


Sources: IATA, Allianz Research

Overall, we find that European beach holidays remain more affordable and bet compared to the and on par with most premium travel destinations Caribbean in Latin America, Africa and South-East Asia. We compile an index of the nominal cost of a one-week beach holiday in 49 jurisdictions, based on the price of a basket of typical expenditures during a beach holiday (three-star hotel accommodation, taxi fares, beverages and meals), excluding air travel costs. In keeping with the concept that similar goods and services should cost about the same in any country (“law of one price”), after adjusting for differences in quality and without tariff and trade frictions, a price comparison across countries offers a proxy for relative purchasing power to illustrate the relative price competitiveness of different beach holiday destinations. While this measure has some empirical shortcomings due to data coverage and timeliness, Figure 4 demonstrates that an average one-week beach holiday in Southern Europe (comprising Greece, Italy, Portugal and Spain) is still far cheaper than in the Caribbean (by about one-third on average) and comparable to advanced economies (Australia and the US). Despite the recent surge in travel-related inflation (Figure 3), Southern Europe is also very price competitive with premium destinations in emerging markets, such as Belize, Maldives, Mauritius, Seychelles and Sri Lanka. Bermuda remains the most expensive beach holiday destination globally, nearly three times as costly as Southern Europe.

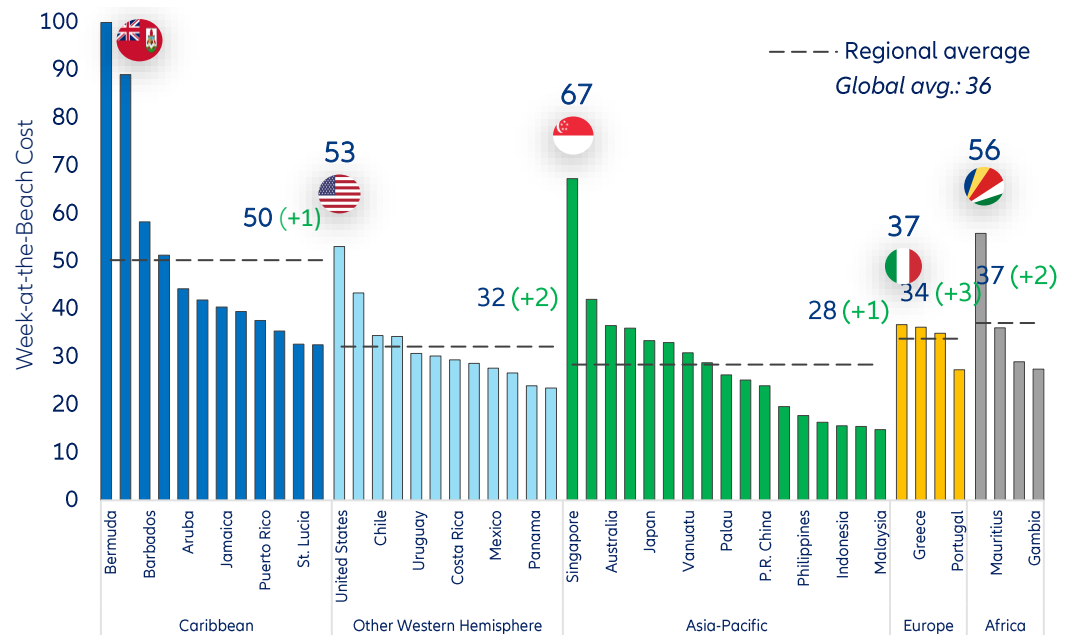
Figure 3: Travel-related inflation developments in Southern Europe’s largest beach holiday countries (y/y %)





Sources: Refinitiv Datastream, Allianz Research

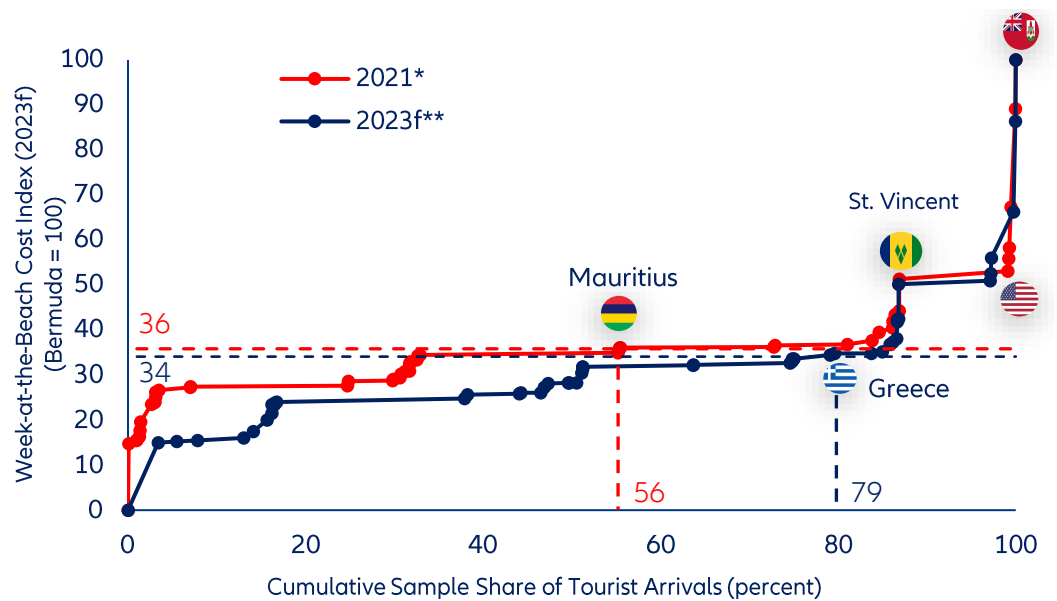
Figure 4: Nominal cost of a one-week beach holiday (indexed, Bermuda = 100)



Sources: Tripadvisor, WorldCabFares, Numbeo, IMF, Allianz Research. Note: The index is based on hotel price data from Tripadvisor and crowdsourced data on meal and deal prices to compute a representative cost of a seven-day vacation; inflation date based on expected average for 2023. The numbers in parenthesis indicate the change of the regional average relative to last year.

Europe can also benefit from the pick-up of beach holiday travel to less expensive destinations since the end of the Covid-19 pandemic. During the pandemic, travel restrictions and hygiene measures did not only entail logistical challenges; international beach holidays also become more expensive: The high cost of the few hotels and restaurants that were still open pushed up the average cost as travel volumes diminished and shifted towards more expensive beach holiday destinations. In contrast, Figure 5 shows that more than three-quarters of total tourist arrivals this year are expected in countries where beach holidays are cheaper than the global average (with Greece as the “cut-off” country).

Figure 5: Lorenz curve of tourism arrivals vs. nominal cost of a one-week beach holiday (indexed, Bermuda = 100)

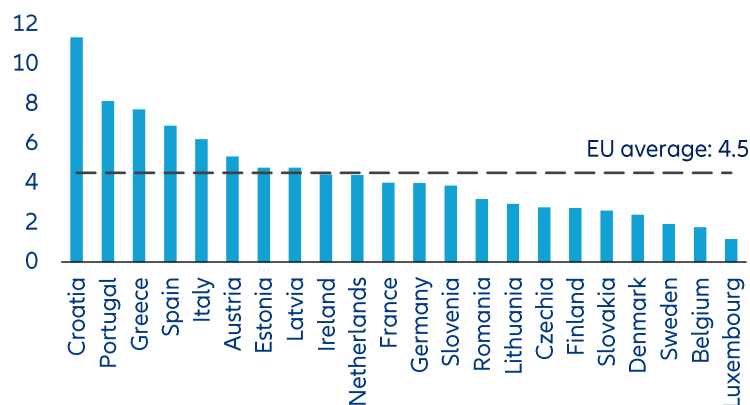


Sources: Tripadvisor, WorldCabFares, Numbeo, UNWTO and Allianz Research. Note: */ price developments based on end-2021 values, tourist arrivals until end-2019; **/ price developments based on forecasted 2023 values, tourist arrivals until end-2021.

Europe is caught between the devil and the deep blue sea

It is hard to overstate the economic importance of tourism in Southern Europe, especially when the summer season creates a wide range of employment opportunities and drives growth in ancillary sectors such as hospitality, transportation, and retail. In 2019, the last year before the Covid-19 pandemic hit the tourism sector, the direct gross value added generated by tourism in the EU amounted to about EUR572bn (or 5% of GDP). Tourism accounts for the largest share in total gross value added in Croatia (11.3%), closely followed by Portugal (8.1%), Greece (7.7%), Spain (6.9%) and Italy (6.2%) (Figure 6).

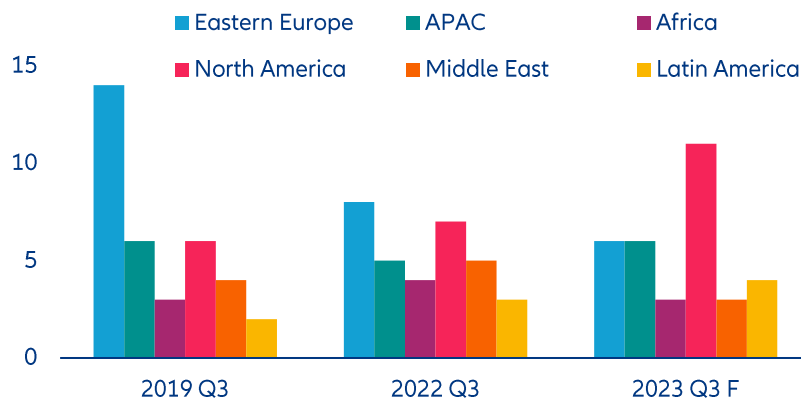
Figure 6: Europe – share of tourism direct gross value added in 2022 (% of total gross value added)



Sources: Eurostat, Allianz Research. Note: based on the ad hoc voluntary data collection on Tourism Satellite Account (2022); no data available for tourism direct gross value added for Bulgaria, Cyprus, Hungary, Malta and Poland.

Europe has progressively gained market share as sanitary restrictions in Asia (especially China) and the appreciation of the USD have redirected global tourism flows. During the pandemic, total direct gross value added from tourism dropped by more than two-thirds to only about EUR184bn in 2020, which decreased the average share of the tourism sector to European economies by 1pp. The number of tourist arrivals plummeted from 238mn in 2019 to about 69mn in 2020 (followed by 92mn in 2021). About three-quarters of the tourism-related sectors experienced a decline of more than 25% of total gross value added, of which travel services (-67% compared with 2019), air transport (-66%) and hospitality (-41%) were hit the hardest. This season, however, the number of visitors to Europe is returning to pre-pandemic levels and is expected to reach 587mn by 2024. Europe now accounts for 62% of global tourist arrivals (up from 51% in 2019), helped in part by the appreciating USD, which has boosted the share of US visitors (Figure 7) even as premium and non-premium airfares for a US-Europe round-trip have increased by +14% and +32% year to date, respectively. However, around 70% of tourism activity in Europe is intra-regional, with France, Spain and Italy the main destinations, hording 36% of total visitors.

Figure 7: European inbound regional tourist arrivals (% of total flights, excluding Western Europe)



Sources: OAG, European Travel Commission, Allianz Research

Southern Europe needs to make strategic efforts in several key areas to enhance its standing as a premier beach holiday destination in light of strong competition from other regions. Less expensive beach holiday destinations in many developing economies are easily reachable. Some of these countries have comparable natural and cultural riches but at lower prices (albeit due to lower labor standards), which could eat into the attractiveness of Southern Europe's tourism industry. Investing in sustainable tourism practices can ensure the preservation of natural environments and cultural heritage for future generations. Furthermore, enhancing infrastructure, including transportation networks and accommodations, can improve accessibility and cater to diverse traveler preferences. Promoting off-season tourism and diversifying offerings beyond traditional beach holidays can also help attract visitors throughout the year.

However, heavy reliance on tourism traps Southern Europe in a bad equilibrium of a strong structural dependency on foreign tourists and an increasing vulnerability to exogenous

shocks (such as the pandemic). It also risks perpetuating the inherent structural problems the region faces in today's globalized knowledge economy², such as a prevalence of low-skilled jobs and low productivity. With other parts of Europe increasingly shifting towards high-skilled, high-value-added manufacturing and high-end services, this could create a growing divergence across Europe.

² *The reorientation towards tourism in Southern Europe is also instructive for Croatia as the most recent Eurozone member country, which has the highest contribution of tourism to total gross value added in Europe. Since the late 2000s, Southern Europe has witnessed strong tourism-led growth thanks to the gradually institutionalized free movement of people within the Union. A greater focus on tourism was the result of reorienting the countries' traditional production strategies underpinned by domestic demand management through deficit spending and industrial policy geared towards price competitiveness, backed by competitive currency devaluations—something the European framework of State Aid regulations, fiscal coordination and currency union rendered no longer possible.*

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