STIMULATING ACCOMMODATION CAPACITY IN IRISH TOURISM

A REPORT PREPARED FOR THE IRISH TOURISM INDUSTRY CONFEDERATION, AUGUST 2023

Contents

INTRODUCTION

Tourism is a key contributor to economic activity and employment in Ireland. It is an indigenous industry, which has a strong regional economic and employment footprint.

In the context of the challenges facing the Irish economy now, particularly the concentration risk inherent in the very strong Exchequer revenue and employment dependence on a small number of large multi-national corporations, it is imperative that the tourism sector is as robust as possible and that it makes as significant a contribution as possible to Ireland's sustainable economic growth and development over the coming years. The economic contribution from tourism comes through employment and the taxes generated for the Exchequer particularly in the form of export earnings. The importance of the two key indigenous economic sectors – agri-food and tourism – must be recognised and supported.

This short paper looks at one significant challenge facing the tourism sector now, which is the lack of visitor accommodation. This issue is addressed in this paper and is divided into two strands:

1. It was acknowledged prior to Covid-19 that there was a significant shortage of tourism accommodation as per numerous Fáilte Ireland reports. This has now been exacerbated by Government's over-reliance on tourism accommodation to house Ukrainian refugees and asylum seekers.
2. Under the EU Just Transition Fund, €68m is being allocated to Ireland to be administered by Fáilte Ireland to invest in tourism initiatives between 2023-2026 in the region must adversely affected by the closure of peat extraction bogs in the Midlands, an area with an already acute shortage of tourism accommodation. Of the Just Transition Fund €38 million is being allocated for Regenerative Tourism business supports and €30 million for a Tourism Trails Network to be divided across the entire affected region.

There is a significant tourism accommodation supply issue in Ireland, particularly in the regions. The danger with such a high level of Government-contracted hotels for an extended period is that these properties may effectively be repurposed and may never come back into the tourism economy thereby fundamentally impacting the tourism landscape of the country. The high-risk scenario is that when Government contracts end, there will be a further reduction in the stock of accommodation, particularly in the regions.

Current national estimates for growth in overseas tourism to Ireland suggest 13.2 million international visitors by 2032, up from a previous high of 9.7 million in 2019 when there were circa 60,000 tourism bedrooms in the country.

Using 2019 as a baseline and applying a ratio of international visitors to the stock of tourist bedrooms at the time would suggest that 5,500 extra bedrooms will be needed in the next 10 years to maintain the ratio. Historically there has been a natural attrition of 1%-2%[1] of

[1] Many industry analysts suggest that the attrition rate will be higher in the coming years due to the impact of Government contracts

tourism bedroom stock in Ireland each year which would suggest a loss of circa 6,000 bedrooms over the next decade.

Therefore it is reasonable to assume that 11,500 additional tourism bedrooms will be needed in Ireland by 2032.

Currently, aside from some activity in Dublin and Cork, there is little appetite for new hotel construction due to high build costs, expensive sites, high cost of capital, and planning delays. A recent Cushman and Wakefield report on the sector in July 2023 stated that *"construction and financial costs currently represent key constraints on further development in the Irish market."*

Cushman and Wakefield estimate that 3,600 new hotel rooms are forecast to be delivered to the Irish market in the coming years but that *"the vast majority of these new rooms (84%) are destined for the Dublin market."*

It seems very clear that regional Ireland, in particular the 8 county area in the Midlands that will receive the Just Transition Funding of €68 million, has very little in hotel development pipeline.

If Government wants to address this problem, it will have to introduce various measures to encourage new hotel development particularly in targeted areas. Without such interventions, the lack of viability will prevent an increase in tourism accommodation from occurring thereby limiting economic activity, impacting jobs, and foregoing tax revenue to the exchequer. It will greatly undermine the impact of the Just Transition funding for the area.

This short paper argues that policies need to be put in place to increase the supply of tourism accommodation. Suggested proposals include:

- Tax breaks such as Accelerated Capital Allowances or an EIS scheme for regionally targeted areas where Fáilte Ireland analysis shows a deficit in tourism accommodation.
- Changes to planning and regulation to facilitate development in targeted areas.
- Area Specific Incentives such as commercial rates holiday.
- Public-Private Partnerships should be explored with local authorities
- Targeted Fáilte Ireland investment in attractions

CONTRIBUTION OF TOURISM TO IRISH ECONOMY

2019 was the last normal year for Irish tourism as 2020 and 2021 were badly affected by Covid-19 as was Q1 2022. In 2019, Fáilte Ireland data show that 9.67 million tourists visited Ireland from overseas. A further 1.28 million visitors arrived from Northern Ireland, giving total out-of-state visitors of 10.95 million tourists. A further 11.6 million domestic tourists are estimated by Fáilte Ireland.

Table 1: Overseas Tourist Numbers to Ireland (2019)

REGION	NUMBER OF TOURISTS (000s)	MARKET SHARE
Great Britain	3,487	36.0%
Mainland Europe	3,609	37.3%
North America	1,902	19.7%
Rest of world	676	7.0%
Total	9,674	100.0%

Source: Key Tourism Facts 2019, Fáilte Ireland, March 2021

The economic contribution of tourism is incredibly significant at both a regional and national level. Fáilte Ireland estimates that every €1 million of tourist expenditure helps to support twenty-seven tourism jobs; 1,000 additional overseas tourists support twenty jobs in the tourism industry; and for every euro spent on tourism, both domestic and overseas, twenty-three cent is generated in tax revenues for the Exchequer.

The CSO has recently released its first Tourism Satellite Account (TSA) for the sector – an internationally recognised harmonised framework for measuring tourist activity. The output highlights the importance of tourism to the national economy, utilising supply and demand side data, drawing on National Accounts and more refined employment data, including activity in tourism related industries.

Using 2019 data – the last full year of data pre-pandemic – the TSA also allows for the first time comparisons on tourism performance with other EU destinations.

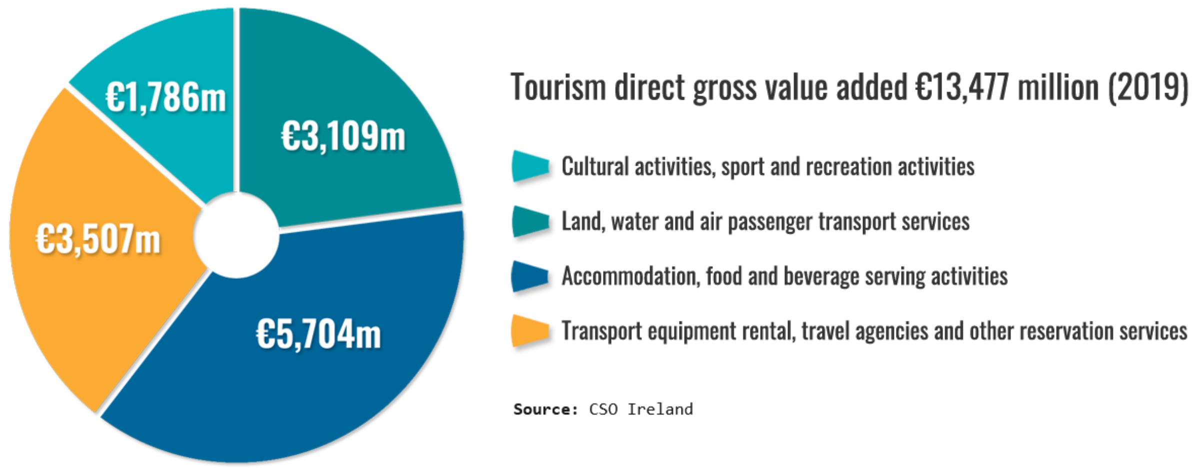
KEY FINDINGS

- Tourism consumption amounted to €10 billion in 2019 – 73% from inbound tourists and 27% from domestic trips.
- Tourism accounted for 4.4% share of Gross Value Added (GVA) in the Irish economy.
- 284,800 directly employed in almost 46,000 tourism-related enterprises, based on full time job equivalents – 13% share of total employment across the economy. Total employment related to tourism is estimated to increase to 352,000, when jobs in non-specific tourism businesses are taken into account.
- Tourism generated approximately €2,000 per head of population.

Using the TSA methodology of both supply side and demand side data allows for a determination of the extent of the economic impact driven directly by tourist expenditure – Tourism Direct Gross Value Added (TDGVA). The CSO's estimate shows that tourism contributed €13.5 billion to the Irish economy in 2019, accounting for 4.4% of total Gross Value Added (GVA) in the economy. Across the EU the average ratio was estimated at 4.5% in the same year.

The main tourism industry contributors to TDGVA in 2019 in Ireland were accommodation and food and beverage services for visitors (€5.704 billion).

The CSO's analysis proves definitively that tourism and hospitality is the largest indigenous industry and biggest regional employer in the country.



THE INADEQUATE SUPPLY OF TOURISM ACCOMMODATION

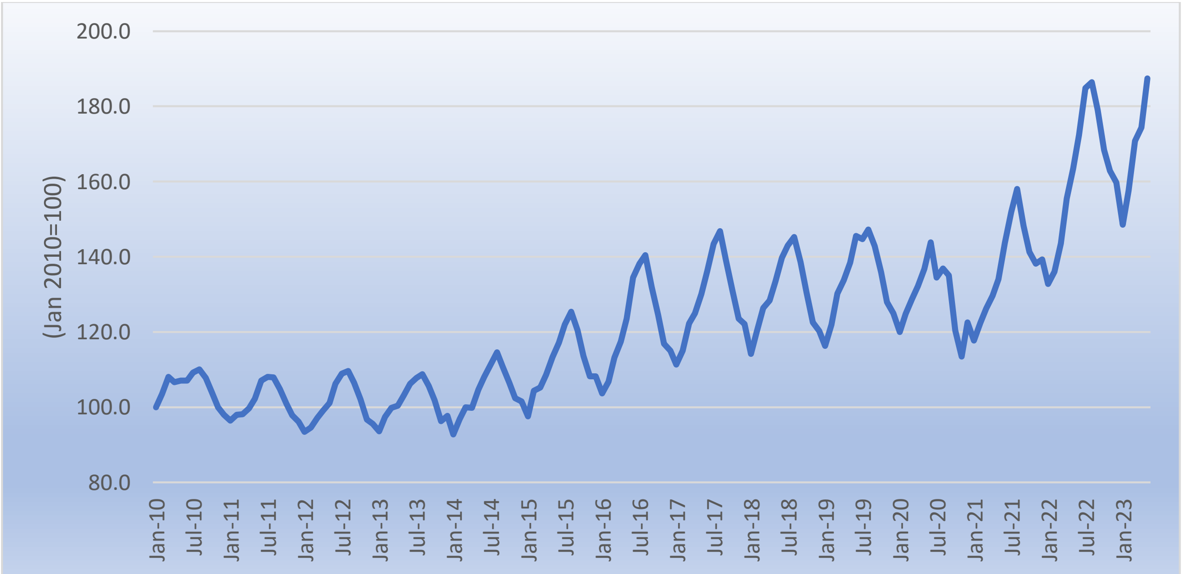
Recent research from Fáilte Ireland[i] presented an upbeat assessment of the Irish tourism performance in 2023 despite significant cost of business challenges and profitability concerns. However, the shortage of hotel accommodation is highlighted as a significant challenge.

The reality is that public contracts to accommodate internationally displaced persons are taking considerable stock out of the accommodation market. This has been estimated by Fáilte Ireland as 1 in 5 tourism bedrooms no longer available to the tourism economy. There is an acceptance of the moral duty to help, but it leaves some areas with little or no accommodation for tourists. This comes on top of some establishments not reopening after Covid.

In the Fáilte Ireland research, inbound tour operators cite lack of accommodation as a key challenge. While demand is buoyant, supply is a problem. In the research 13 out of 24 operators cite 'public contracts for accommodation' and 11 out of 24 cite 'fewer hospitality businesses open post-pandemic' as concerns. There are also concerns about the cost of the accommodation that is available.

The reality is that if beds are scarce, if people have nowhere to stay, visitors will not come. Likewise, if the cost of accommodation continues to increase, the competitiveness of the Irish tourism offering will be seriously damaged, and this will inevitably affect demand.

Figure 1: Cost of Accommodation Services



Source: CSO PxStat

In the year to May 2023, the cost of accommodation services increased by 14.7 per cent. The lack of bedroom supply is a key factor driving the cost up and increased consumer prices risks affecting Ireland's value proposition.

According to ITIC,[ii] the contraction in availability of accommodation for tourists has inevitably led to an increase in the price for the visitor, particularly at times of high demand exceeding available supply. The reduction in available tourist accommodation is most evident in several popular west coast counties, including Mayo and Clare.

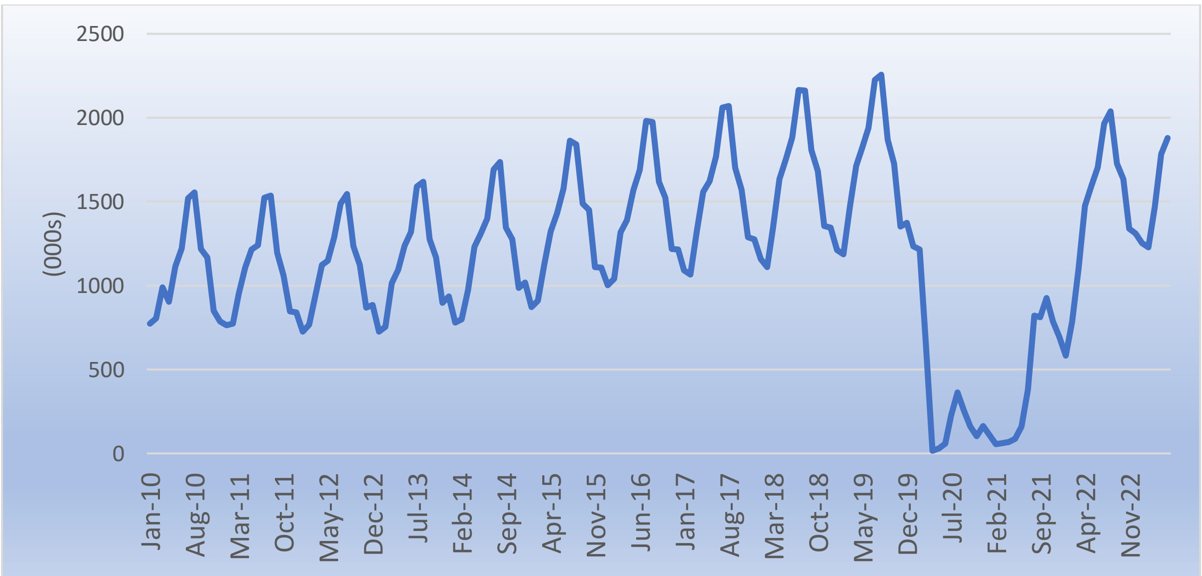
The immediate impact on the tourism economy includes:

- Higher prices for accommodation where demand exceeds supply.
- Reduction in employment in the sector.
- Loss of visitor footfall in traditional tourism areas, less visitor spending in local economies, and a threat to the continues viability of downstream businesses catering to visitors.
- Loss of group and tour traffic due to sharp reduction in the supply of mid-market hotel accommodation.

Regrettably no CSO tourism data has been made available since before the pandemic. Aviation numbers, which include Irish and non-Irish citizens, from the CSO data show that inward arrivals into Ireland are increasing at a significant pace:

- In 2022 there was 17.26 million arrivals by air and sea into Ireland. This is still 14.3 per cent lower than 2019, but the trend is very firmly in an upward direction.
- In the first 5 months of 2023, there was 7.61 million arrivals into Ireland, which is 37.4 per cent ahead of the same period in 2022 and 2.9 per cent higher than the first quarter of 2019.

Figure 2: Inward Travel to Ireland



Source: CSO, Air and Sea Travel Statistics, May 2023.

Fáilte Ireland[iii] has suggested that 2023 is set to be the year for air travel recovery with all world regions now open to international travel. On the week starting June 26th, 2023, global air capacity was 2.5 per cent below where it was in the same week in 2019. Air access to

Republic of Ireland (ROI) was above the European average during the first quarter of 2023, reaching 102 per cent of its 2019 seat capacity level versus 92 per cent for Europe. Planned seat capacity to ROI for Summer 2023 is expected to be at 103 per cent of its 2019 levels, with an average of 500,000 seats per week. It suggests that seat capacity is due to be above its 2019 levels for Rest of World (111 per cent), Mainland Europe (104 per cent) and Great Britain (102 per cent) in summer 2023, while North America is very close to a full recovery (98 per cent).

The latest data from CBRE[iv] highlights the pressures on the supply of accommodation and the consequences for Irish tourism. The trading performance of hotels is strong so far this year.

- In the year to May occupancy levels in Dublin averaged 78 per cent; Cork averaged 74.5 per cent; Limerick averaged 80 per cent; and Galway averaged 75 per cent. These occupancy rates are in line with 2019 levels but are expected to increase further over the coming months.
- The average daily rate (ADR) is also increasing sharply. In the year to May, the ADR across all stock in Dublin reached €170; €144 in Cork; €119 in Limerick; and €133 in Galway. CBRE points out that in Dublin a record-breaking ADR of €209 for the month of May was achieved.
- CBRE points out that while the top-line performance is strong, '*hotel operators are still experiencing increased operational costs due to higher wages, utilities and F&B expenses and this is impacting bottom-line performance*.'

The high occupancy rates and the higher room rates are reflecting stronger demand as well as problems on the supply side. A significant issue is that a large proportion of hotel stock is currently not available in the market due to the shortage of residential stock and the consequent use of hotel rooms for emergency accommodation. These rooms are unlikely to come back into the market anytime soon as the Ukraine war shows no signs of ending for the foreseeable future.

In a Fáilte Ireland briefing to the tourism industry at the end of June 2023, Fáilte Ireland estimated that 13% of registered tourism bed stock as well as 7% of unregistered tourism bed stock is under contract to Government for humanitarian reasons. Thus 1 in 5 visitor bedrooms nationally is unavailable to the tourism economy.

Fáilte Ireland estimate that the use of tourist accommodation for the housing of displaced Ukrainian citizens and international protection applicants could cost non-accommodation tourism providers up to €1 billion in lost revenue this year. Furthermore, that the 'lack of availability of tourist beds means activity providers, visitor attractions and many in impacted areas will have their business survival' put at significant risk.[v]

The Chief Executive of Fáilte Ireland warned that the tourism sector needs as much tourism accommodation stock as possible returned to tourism as quickly as possible. He warned that '*in addition to the short-term business loss and the long-term consequences for the quality of* *some rural tourism destinations, this situation also creates conditions that facilitate pricing practices that put Ireland's long-term reputation at risk*.'

Fáilte Ireland findings outline the absolute numbers of people accommodated in Ireland, with 76,143 beds under contract, and 29,555 in Fáilte Ireland registered properties. The presentation showed that there are now five counties with more than 20 per cent of available registered bed capacity out of use for tourism – Offaly, Mayo, Leitrim, Meath, and Clare. Clare is top of the list at 33 per cent, followed by Meath at 28 per cent.

It is generally accepted that prior to the Ukraine crisis, there was already an issue with supply. CBRE[vi] research suggests the notwithstanding the number of hotel rooms currently out of the market, Dublin remains relatively undersupplied, as is evidenced by the upward pressure on room rates and the occupancy levels. However, it also points out that Dublin has fewer hotel rooms than overseas cities of similar size. It estimates that Dublin has 25,860 hotel bedrooms, compared to 39,180 in Stockholm and 42,000 in Amsterdam.

Overseas Visitors Forecasts

Tourism Economics, part of Oxford economics and a renowned international travel and tourism consultancy firm, estimates that the number of overseas visitors to Ireland is projected to expand from 9.7 million in 2019 to 13.2 million by 2032.

As previously stated, it is estimated that Ireland needs as many as 11,500 additional tourism bedrooms to meet this projected rise in demand.

THE EU JUST TRANSITION FUND & THE IMPLICATIONS FOR TOURISM

The EU Just Transition Fund (EUJTF) is Pillar 1 of the European Union Just Transition Mechanism. The purpose of the EUJTF is to assist the most affected territories in transitioning to a climate neutral economy.

Investments under EUJTF are complemented by a combination of grants & loans to private sector entities under a dedicated window of InvestEU instrument (Pillar 2) and through a specific Public Sector Loan Facility (PSLF) managed by the EIB (Pillar 3). PSLF beneficiaries are public sector entities including private law bodies with a public service mission.

Following approval by the Government on 29th November 2022, the European Commission adopted Ireland's *Territorial Just Transition Plan* and associated Programme, incorporating €84.5 million of funding from the EU Just Transition Fund for 2021 - 2027.

When national co-financing is included, this new Programme will provide for investments of up to €169 million, which will be targeted at the economic transition of the Midlands region for the period to 2027. Bord na Móna's portfolio of c.80,000 hectares include over 130 bogs, which mirror the proposed Territory – largely in Laois, Longford, Offaly, Westmeath, as well as parts of adjoining counties of Roscommon, Galway, Tipperary, and Kildare.

The immediate challenge during the transition out of peat is the impact on jobs and communities in the impacted region as the labour-intensive peat industries are wound down. However, the wider socio-economic impacts and the resulting impacts on rural depopulation are of crucial importance. In the affected areas, there are limited alternative local-employment opportunities for workers with highly specific and hard to transfer skillsets. Development of local social enterprise, retail and tourism are seen as crucial to provide tangible opportunities for economic growth of direct benefit to impacted communities.

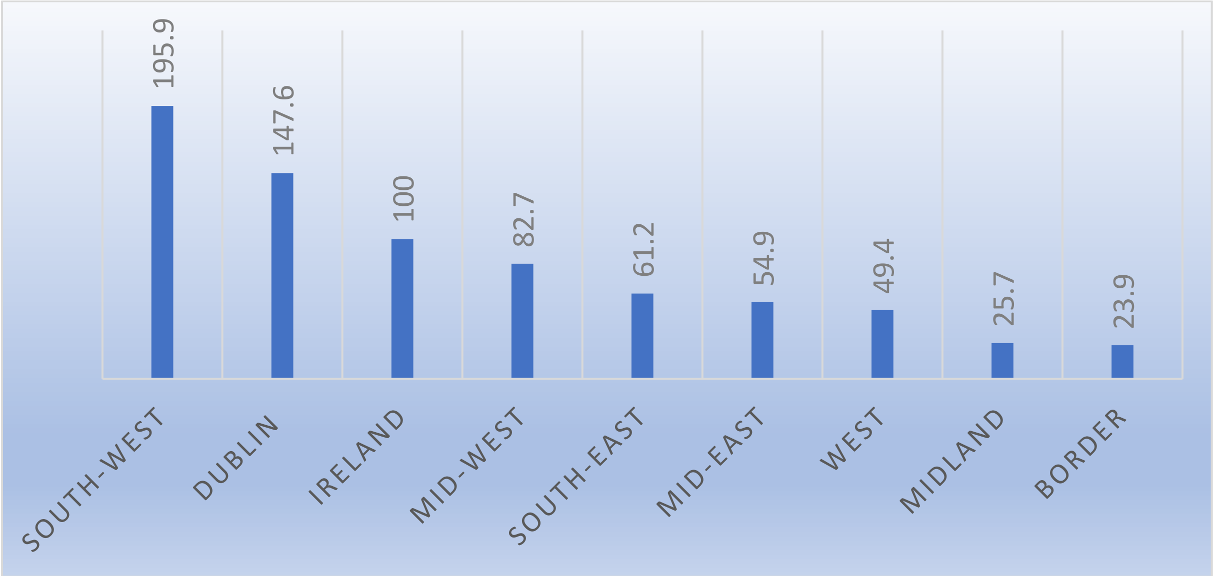
Under the EU *Just Transition Fund* the EU has awarded Fáilte Ireland funding for an investment of €68 million in tourism in the Midlands region. €38 million is being allocated for Regenerative Tourism business supports and €30 million for a Tourism Trails Network to be divided across the entire affected region.

It is intended that the *Regenerative Tourism Scheme* will be a driver of employment for the midlands area, with the funding to be broken down under four strands. These strands will deliver a strategic network of connected walking, cycling and water trails across the Midlands; help support public, private, and community-based tourism enterprises to enhance and sustain local economies; and provide a range of supports for smart transformation and entrepreneurship.

The reality is that the Midland region lacks adequate tourism accommodation stock and the expenditure of €68m in EU Just Transition Funding by Fáilte Ireland on tourism initiatives between 2023-2026 can only work if there is an adequate supply of accommodation. The relevant counties represent less than 5% of both hotels and bedrooms within the country featuring collectively as they do 41 hotels (out of a national figure of 835) and 2,354 bedrooms (out of a national figure of 64,452).

The imperative for promoting tourism and other economic activity in the Midland region is clear. In 2021, CSO data show that Gross Value Added (GVA) per person in the Midland region is 74.3 per cent lower than the national average. The ending of peat extraction in the region will serve to exacerbate this situation.

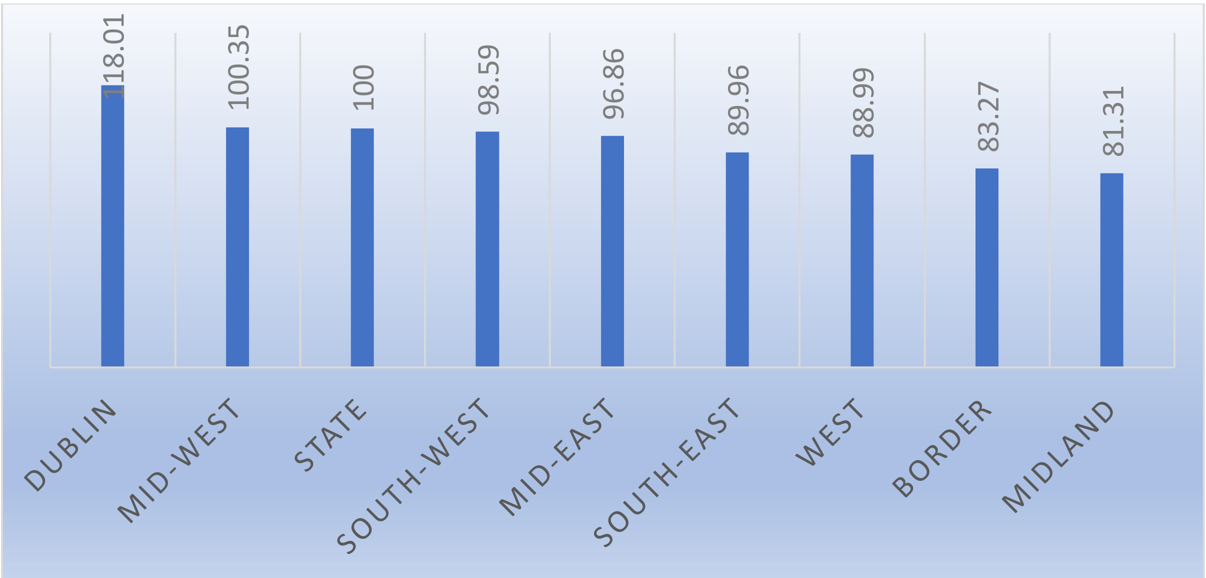
Figure 4: Index of Gross Value Added (GVA) per Person by Region (2021)



Source: CSO

Figure 5 shows the index of disposable income per person on a regional basis. The Midland region has the lowest and is 18.7 per cent lower than the national average.

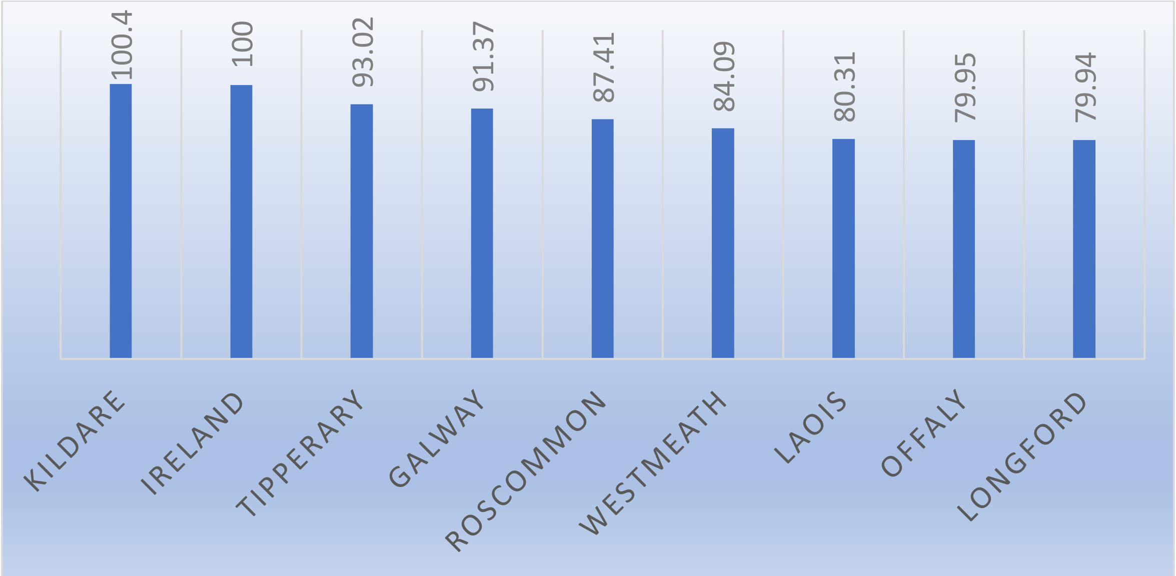
Figure 5: Index of Disposable Income per Person by Region (2020)



Source: CSO PxStat

Figure 6 shows disposable income per person in the counties that are included in the Just Transition Fund. Longford, Offaly, and Laois are all close to 20 per cent below the national average.

Figure 6: Index of Disposable Income per Person by County (2021)



Source: CSO PxStat

The foregoing analysis demonstrates the extent to which those counties most exposed to the closure of peat bogs are economically deprived. The investment of €68 million in tourism attractions in those counties is badly needed. However, the problem is that investment in tourism attractions without having sufficient accommodation to keep visitors in the area for a longer period would prove very difficult. However, only €3 million of the funding that Failte Ireland is allocated can be used for accommodation. Hence, it will be necessary for some type of State intervention to ensure that sufficient accommodation is created.

PROPOSED SOLUTIONS

THE CHALLENGE

In the context of the lack of supply of accommodation due to a combination of the refugee crisis and the already pre-existing shortage of accommodation, measures need to be introduced as a matter of priority to preserve the national and regional economic activity and employment that results from tourism activity. If the lack of bedroom supply is allowed persist, hotel prices will continue to rise, and this will combine with the lack of availability of accommodation to damage inward and domestic tourism.

A further requirement for accommodation will come from the need to ensure that the €68 million Fáilte Ireland investment programme in tourism attractions under the Just Transition Fund in the Midlands region will require a significant increase in the supply of visitor accommodation in that area. If this supply of accommodation is not forthcoming, it is likely that the EU Just Transition funding will not achieve their full potential and that number of visitors to the affected counties will be undermined and/or visitors will be day trippers.

The reality is that there are too few hotel investments under way outside of selected urban centres. If there is limited hotel investment in cities then the chance of any investment in regions like the Midlands is unlikely in the absence of a range of incentives. Currently the Midlands region where the Just Transition funding is earmarked is poorly served by hotels. Data according to Fáilte Ireland shows Laois (10 hotels, 554 bedrooms), Westmeath (15 hotels, 1,103 bedrooms), Offaly (7 hotels, 372 bedrooms), Longford (3 hotels, 92 bedrooms) and Roscommon (6 hotels, 203 bedrooms). Thus these counties represent less than 5% of both hotels and bedrooms within the country featuring collectively as they do 41 hotels (out of a national figure of 835) and 2,354 bedrooms (out of a national figure of 64,452).

The business environment for many hotels is challenging now, despite the high occupancy rates and higher average daily rates in parts of the country. In regions such as the Midlands the challenges for hoteliers are particularly acute. Much of the week tends to be very quiet, and the challenge is to limit losses. The only real revenue is earned at the weekends.

For hoteliers in general, the key challenges are:

- Staff shortages, particularly Chefs.
- Labour costs are rising.
- Energy costs have increased significantly over the past couple of years.
- Interest rates have increased sharply since July 2022, and look set to rise further as the European Central Bank attempts to bring inflation under control.
- The cost of room refurbishment, which is essential to maintain acceptable standards is very high. For some hotels, up to 8 per cent of turnover is allocated to capital expenditure.

In relation to the hotels that are currently being used for refugee purposes, the incentive for hoteliers to go back to being a hotel are not compelling. Hoteliers are guaranteed a certain income and virtually 100 per cent occupancy rates, and staffing requirements are relatively low. The danger is that many of the hotels being used to accommodate refugees may never return to the hotel stock.

PROPOSALS

Accelerate Capital Allowances

Investment in hotel stock is very low due to a combination of high build costs; high operational costs; and the higher cost of capital. It is estimated by the sector and developers that the cost of delivery is at least €200,000 per room, depending on the standard of the hotel. The result is that in the absence of some tax incentives, the viability of new hotel development is not compelling.

Tax incentives are effective in driving development, particularly in an environment where viability of development is very stretched.

Capital allowances are a form of incentive available to business for specific capital expenditure. They provide savings for the developer by reducing the tax otherwise payable by business where they spend money on certain capital assets.

Such capital allowances do not have a strong reputation, due in large part that the last time they were utilised, they were not regulated properly and arguably lasted too long. However, notwithstanding such reservations, tax incentives have been used in the past to address market failure and have resulted in a significant increase in the supply of residential and commercial property. Such accelerated capital allowances must be closely monitored and controlled to ensure they achieve their objectives, which in this case is to increase the supply of hotel accommodation, particularly in the regions.

The reality is that hotel investment is not particularly viable now, and if Government wants to increase the stock of visitor accommodation, tax incentives will be required. Without such incentives, the development will not occur, and tourism growth and the sustainable jobs it creates will suffer.

Incentives should be directly linked to geographic areas where Fáilte Ireland analysis shows that there is a deficit of visitor accommodation.

Area Specific Incentives

Based on the identification of areas where there is a requirement to increase accommodation, specific area-based incentives could be considered. These incentives could take the form of a tourism-based EIS scheme; a 10-year holiday from commercial rates; or some form of specific grant funding. Once again, such incentives should be directly linked to geographic areas where Fáilte Ireland analysis shows that there is a deficit of visitor accommodation.

Legislation Changes and the Regulatory Environment

The cost of new hotel build is very high, but for some operators, there may be potential to add more hotel rooms by allowing development in adjoining properties. The current regulatory environment makes this very difficult. Changes to the regulatory/legislative environment to allow expansion to adjoining premises in streetscapes would be effective in bringing alternative additional accommodation on stream. This would also address the issue of derelict/empty commercial properties.

For hotels with the requisite grounds, the promotion of the development of eco-pods would provide considerable accommodation, particularly during the warmer weather peak tourism season. Hotels with adequate grounds would also benefit from capital allowances for the constriction of much needed staff accommodation.

Public-Private Partnerships

As in other markets including the UK, consideration should be given to public-private partnerships. According to Knight Frank in the UK, local authorities committed £93m of investment, through private-public partnership schemes, where hotels formed the primary focus in a development project and which have either outline or detailed planning permission granted.

Upon completion of the hotel development, local authorities have the choice of either retaining ownership of the hotel and receiving an annual rent into the Local Authority's revenue budget or selling the hotel to a private operator.

This could be a way of stimulating hotel development in areas particularly where there is a significant hotel deficit and evident market failure.

Targeted Fáilte Ireland Investment

When Failte Ireland is giving consideration to the development options for the €68 million Just transition Funding, it could be more appropriate where possible to strategically locate the investment close to existing hotels, who would then be in a position to expand room capacity. Extension of existing room capacity would be considerably cheaper and more viable than a greenfield hotel build.

CONCLUSION

There is a serious tourism accommodation supply issue in Ireland, particularly in the regions, with circa 11,500 additional bedrooms required by 2032 to meet demand and allow the tourism economy to fulfil its potential. The high-risk scenario is that when Government contracts end, there will be a further reduction in the stock of accommodation, particularly in the regions.

If Government wants to address this problem, it will have to introduce various measures to encourage new development in targeted areas. Without such interventions, the lack of viability will prevent an increase in accommodation from occurring. A number of potential Government interventions have been outlined in this short paper. Increased accommodation capacity will engender sustainable tourism growth that can drive socio-economic benefits throughout regional Ireland.

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