

PKF Study Finds US Hotels Extremely Vulnerable to Sharp Declines in Airline Capacity

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According to the latest analytical data from PKF Hospitality Research (PKF-HR), U.S. hotels could face a decline in lodging demand greater than that experienced during the turmoil following the terrorist attacks on September 11, 2001.

Under a worst-case scenario, a 1 percent decline in the number of seats flown within the U.S. will result in a 0.39 percent decline in the demand at the nation's hotels. These findings come from an in-depth econometric analysis performed by lodging experts PKF Hospitality Research.

'Many industry participants have been speculating about the spillover effect a deteriorating airline industry will have on hotels,' said Mark Woodworth, president of PKF Hospitality Research. 'Our research measured the historical relationship between these two components of the travel industry. This allowed us to project just how much business hotels stand to lose given the cutbacks in capacity announced by the major airlines.'

Using historical data from Smith Travel Research, Moody's Economy.com, and the Department of Transportation, and controlling for the effects of changes in income and employment, PKF-HR found what many intuitively believe: a highly significant relationship exists between available seats and hotel room night demand.

'Based on our findings that a 1 percent decline in available airline seats results in a 0.39 percent decrease in hotel demand, if airline capacity is reduced by 10 percent as some have suggested, then lodging demand would fall off 3.9 percent. To put this in perspective, the decline in lodging demand experienced in 2001 was just 3.3 percent,' Woodworth noted.

Given PKF-HR's second quarter Hotel HorizonsSM forecast for 2008, a 3.9 percent reduction in lodging demand for the year would translate into approximately 40 million fewer room nights occupied, or \$4.3 billion in revenue, on an annual basis. 'With losses like this, hotel operators would be forced to make drastic cutbacks in staffing and other operating costs,' Woodworth concluded.

Several factors, however, suggest that the decline might not be quite so bad. 'As one would expect, the airlines are eliminating those flights that are in least demand and lowest in fuel efficiency. Some portion of the demand that would have booked a flight that is no longer available will simply adjust the timing of their travel plans. Trips will still be made,' Woodworth noted.

Location and Rate Matter

'Just as we have observed during the ebbs and flows of the normal lodging cycle, the reaction of U.S. hotels to a major economic shift will differ based on a variety of factors,' he added.

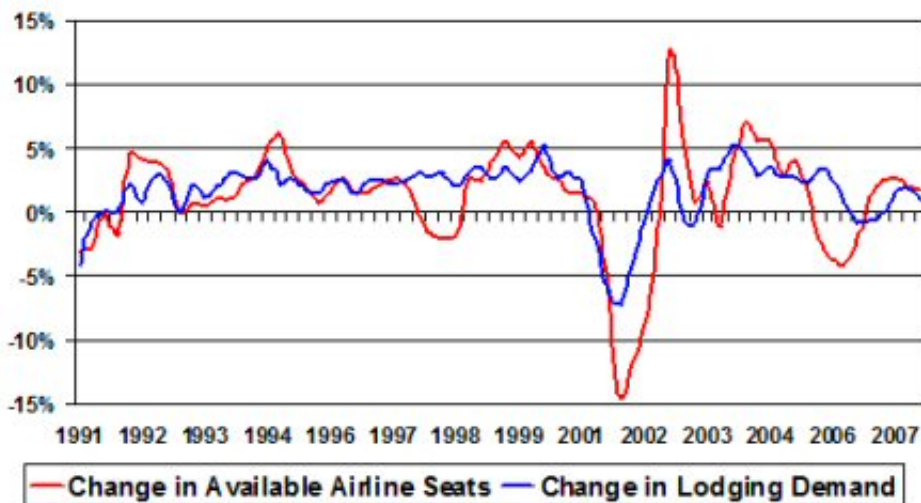
Statistically speaking, the PKF-HR regression analysis found that Miami, Orlando, Phoenix, and Denver have historically shown the most significant relationships between airline seats and lodging demand. This indicates that these cities are the most sensitive to changes in airline service. 'What these markets have in common is that they are either major leisure destinations, or geographically situated in an isolated location away from other major metropolitan areas,' said John B. (Jack) Corgel Ph. D., the Robert C. Baker professor of real estate at the Cornell University School of Hotel Administration and senior advisor to PKF-HR. 'Conversely, cities that are very economically diverse, or those that are easily accessible from other metro areas via automobile or train, are best positioned to withstand cutbacks in airline capacity. Most of the major cities along the two coasts fall into these categories.'

Pricing levels also dictate the vulnerability of hotels to changes in the airline industry. In general, properties in the highest and lowest rated chain-scales are least susceptible to movements in airline capacity, while those in the middle stand to lose the most. 'Historically, the performance of luxury hotels and budget-oriented motels is largely insensitive to changes in airline capacity. Conversely, lodging establishments in the upscale and midscale without food and beverage categories have exhibited the greatest historical vulnerability to changes in the airline industry. These two lodging segments are popular with mid-level business and leisure consumers that don't have quite the economic insulation of executive luxury travelers, or the bare-bones budget of construction crews and thrifty trekkers,' Corgel said.

Conclusion

'Given what is happening in today's economy, there are many moving parts influencing the performance of hotels. What we at PKF-HR have accomplished is isolating the direct impact of the airline industry on lodging, as opposed to the downward pressures on hotel demand caused by the credit crisis, rising gas prices for automobiles, and declining consumer confidence,' Woodworth stated. 'If significant reductions to airline capacity do occur, the potential exists for an extremely negative impact on U.S. hotels. The impact will vary by geographic location and property orientation, but will be hard to completely avoid no matter where, or who, you are.'

Available Airline Seats vs. Lodging Demand Quarterly Change from Prior Year



Sources: Department of Transportation, Smith Travel Research, PKF Hospitality Research

To purchase a second quarter 2008 Hotel HorizonsSM forecast report for the United States, or one of 50 individual markets, please visit the firm's online store at www.pkfc.com/hotelhorizons, or call (866) 842-8754.

PKF Hospitality Research (PKF-HR), headquartered in Atlanta, is the research affiliate of PKF Consulting, a consulting and real estate firm specializing in the hospitality industry. PKF Consulting has offices in Boston, New York, Philadelphia, Washington DC, Atlanta, Indianapolis, Houston, Dallas, Bozeman, Sacramento, Seattle, Los Angeles, and San Francisco.

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