Why has the French hotel

Introduction

France is the third largest economy in Europe and a member of the G7. It has one of the largest and most concentrated hotel businesses in Europe and attracts one of the largest volumes of foreign visitors per year of any country in the world, yet over the past five years its hotel business has under-performed in terms of both demand growth and supply growth.

In this note we identify what happened to French hotel supply and demand over the past five years and explain, more specifically, why it happened.

Developments in hotel supply

The main hotel supply story in Europe over the past five years has been the rich growth in hotel chain supply and the decline in unaffiliated hotel supply as the following table illustrates.

Room stock	2000	2005	Changes	CAGR %
Affiliated	973,580	1,466,850	493,270	8.5%
Unaffiliated	3,926,420	3,540,150	-386,270	-2.0%
Total	**4,900,000**	**5,007,000**	**107,000**	**0.4%**

Source: Otus & Co

Within the affiliated segment the pattern of supply growth was not uniform across the market segments:

Market level	Affiliated rooms Europe 2000	Rooms share % 2000	Affiliated rooms Europe 2005	Rooms share % 2005	Room additions	CAGR %
Deluxe	13,830	1.4%	30,495	2.1%	16,665	17.1%
Up-Market	300,785	30.9%	398,270	27.2%	97,485	5.8%
Mid-Market	449,090	46.1%	661,490	45.1%	212,400	8.1%
Economy	147,450	15.1%	293,660	20.0%	146,210	14.8%
Budget	62,425	6.4%	82,960	5.7%	20,535	5.9%
Total	**973,580**	**100.0%**	**1,466,875**	**100.0%**	**493,295**	**8.5%**

Source: Otus & Co

Growth in branded deluxe and economy room stock outperformed the market. The mid-market, the largest segment performed in line while up-market and budget under-performed.

The supply developments in France illustrate a different growth pattern:

Market level	Affiliated rooms France 2000	Rooms share % 2000	Affiliated rooms France 2005	Rooms share % 2005	Room additions	CAGR %
Deluxe	1,385	0.7%	2,140	0.9%	755	9.1%
Up-Market	27,200	12.9%	28,060	11.2%	860	0.6%
Mid-Market	55,095	26.1%	63,040	25.3%	7,945	2.7%
Economy	74,590	35.3%	89,130	35.7%	14,540	3.6%
Budget	53,000	25.1%	67,090	26.9%	14,090	4.8%
Total	**211,270**	**100.0%**	**249,460**	**100.0%**	**38,190**	**3.4%**

Source: Otus & Co

France is one of the most developed hotel markets in Europe with 48% of hotel room stock affiliated to chains. However, the rate of growth in affiliated hotels over the past five years has been slow. Whereas in 2005, France accounted for 17% of the affiliated hotel rooms in Europe, it accounted for only 7.7% of total chain supply growth since 2000 and its CAGR % has been less than half that of Europe. The sluggishness is not because chain supply has reached its limit in France. The UK has a higher level of hotel room concentration at 53% and over the past five years the chains have added more than double the room stock in the UK than they have in France.

business slowed?

The market level profile in France is very different from every other country and from Europe as a whole. In France, hotel chains are under-represented in deluxe hotels, the smallest segment, and that segment's rate of growth is around half of that in Europe. Up-market rooms account for 27% of the hotel chain room stock in Europe, but only a measly 11% in France where they have grown by less than 1% CAGR since 2000 against almost 6% for Europe. Hotel chains have 5,000 more up-market hotel rooms in London than they have in the whole of France and London has 20,000 more branded up-market rooms than Paris. The picture at the mid-market is little different, 45% of rooms in Europe, but only 25% in France and 2.7% CAGR since 2000 in France against 8.1% in Europe.

When we get below mid-market the share of chain rooms in France is materially greater than Europe as a whole. Economy rooms, such as those in Campanile, Ibis, and Kyriad account for 36% of chain room stock in France against only 20% for Europe as a whole. Budget rooms in France, such as those in Etap, Formula 1 and Premiere Classe, account for a whopping 27% in France against only 5.7% in Europe as a whole. But even these dominant segments in France have under-performed in terms of supply growth. The stellar growth segment for hotel chains in Europe since 2000 has been economy with a CAGR of almost 15% and a third of the new rooms added in the UK. France managed a growth of only 3.6%. The budget segment is dominated by France, which accounts for over 80% of all branded budget rooms in Europe, yet even here the growth in room stock has been sluggish at only 4.8% CAGR.

Of even more note, the annual rate of supply growth in France has declined throughout the period.

Developments in hotel demand

An important feature of hotel demand in France is derived from the number of foreign visitors. The past five years has seen the number of foreign visitors staying overnight in France bounce annually between 77 million in 2000 to 75 million in 2004. A significant proportion of these visitors stay in gites, campsites and holiday centres rather than hotels. Otus estimates that foreign visitors account for around 40 million nights in hotels in France and this translates into around 23 million room nights sold to foreign visitors, most of which are to leisure travellers.

Domestic demand accounts for twice as many room nights sold as foreign demand. Of these, about one third are sold to business travellers.

Deloitte reports that in Paris between 2000 and 2005 RevPAR at mid-market hotels declined by a CAGR of 2.4% to €95.12, that at up-market hotels the decline was 2.6% to €129.58, but that at deluxe hotels there was growth of 1.6% to €425.36.

At the economy and budget levels the two dominant chains Accor and Louvre showed sluggish RevPAR growth. Between 2000 and 2005, Accor struggled to CAGR of only 0.4% to €31.61 as it added more Etap budget hotels than the higher priced Ibis economy hotels. Louvre, which has a room stock split of two thirds/one third between economy and budget brands grew RevPAR by CAGR of 1.6% to a skimpy €30.05.

Even although the demand data is partial in comparison to the supply data it paints a picture of sluggish growth at best over the period and we now turn to the French economy to seek clues to the depressed hotel business.

The French economy

France is the third largest economy in Europe with a 2004 GDP of $2,047 billion, up from $1,921 billion in 2000, a CAGR of only 1.6%. French GDP/citizen ranks only 12th in Europe and is on a declining trend as the population rises and unemployment stays stubbornly above 10% where it has been for most of the past 10 years. In any analysis these are not the general economic conditions to generate much demand or supply in the French hotel business, but to understand the dynamics of hotel demand and supply over the past five years we need to dig below the general numbers and look at the segmentation of GDP into agriculture, manufacturing and services. We start with the smallest segment, agriculture.

Agriculture accounted for 2.8% of GDP in 2000 and despite the highest subsidies from the EU it declined to 2.5% in 2004. Agriculture accounts for around 4% of the French work force and is still very inefficient. Agricultural GDP declined at a CAGR of 1.7% between 2000 and 2004 and agricultural GDP/citizen declined by 2.3% to $844. Agriculture provides very little business demand for hotel rooms or for conferences and agricultural employees are an immaterial source of leisure demand into hotels. The decline in French agriculture over the period, although not positive for the French hotel industry, is unlikely to have accounted for any measurable pressure on hotel demand or supply.

Why has the French hotel business slowed? continued

Manufacturing accounted for 22.9% of GDP in 2000 and declined to 21.8% in 2004. Manufacturing GDP grew between 2000 and 2004 at a CAGR of only 0.3% and manufacturing GDP/citizen fell by 0.3%. The contribution of manufacturing to the French economy is low relative to the other four large EU economies and like Germany, Italy and UK it is struggling with slow domestic demand growth and international cost pressures.

Manufacturing has nearly 10 times the economic significance of agriculture to the French economy, and manufacturers provide business demand for both hotel rooms and for conferences, yet it is still a minority source of domestic business demand. Leisure demand from manufacturing employees comes mostly from executives, there is very little blue-collar demand into hotels and that is mainly unpackaged demand for economy and budget hotels. The very slow growth in manufacturing has had little volume impact on the French hotel business, but increasing cost pressures are driving business demand from manufacturers down the hotel market and limiting the growth in conference demand. Leisure demand from manufacturing employees has reflected this trend.

By far the largest segment of the French economy is citizen services - health, education, welfare and other public services. Citizen services accounted for 41% of the French GDP in 2000 rising to 42% in 2004, a CAGR of 2.2% over the period and well ahead of the growth in the economy as a whole. The growth was the result of the Government soaking up the rising unemployment with more state jobs. The French citizen services segment is large relative to the other four large economies in the EU and the demand it delivers for the hotel business is significant, but tends to be concentrated on rooms at the mid-market level and below and also involves a disproportionately low level of demand for conferences in hotels. Over the past five years room rates available from the citizen service segment have been under downward pressure and this has limited further the growth in hotel demand and supply that this segment has been able to generate.

Market services – retailing, financial services, communications and professional services – accounted for 19.3% of GDP in 2000, rising to 19.5% in 2004, a CAGR of 1.9% and ahead of the 1.6% for the economy as a whole. This is a critical segment for the hotel industry not only because it provides a majority of domestic business demand and most of the domestic demand for conferences and meetings but also because demand from this segment is accelerating. Market service employees are also the largest source of leisure demand into hotels and it has driven much of the growth in the French hotel business over the past five years.

Experience services – hotels, restaurants, bars, gaming, attractions, travel, transport, cinemas, theatres, nightclubs, private health, private education and sports – accounted for 14% of GDP in 2000 rising to 14.3% in 2004, a CAGR of 2.1%, well ahead of the 1.6% for the country as a whole. This segment not only delivers business demand into hotels, but as consumer spending in an economy shifts from consumer goods to out of home leisure activities it also captures the growing domestic demand for hotel based short and long holidays and also accounts for the overseas visitors. Like market services, the growth in experience services is accelerating and is critical for the growth and development of the hotel industry.

Conclusion

For too long we have had to be satisfied with superficial analyses that sought to link hotel growth with the growth of an economy as a whole and this has been peddled as the universal spanner to understand historic and projected hotel demand and supply. Such analyses fail to account for the more specific structures and dynamics of hotel supply and demand. They do not pay attention to the different dynamics of growth in the segments of an economy or to the contributions that the different segments make to hotel demand and supply. In this note we have sought to introduce more useful insights that come even from scratching the surface of an economy just a little. There is much more available and only by diligent and deep analysis can we hope to understand the momentum in the different segments of an economy that provide clearer indicators of the future development of hotel demand and the supply growth that will follow. Contact Otus for more explanations.

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