



The Real Demand for Rooms

By ECS, March 2008

Good Times for Hospitality Industry

The Indian hospitality industry is currently witnessing unprecedented growth, thanks to booming economy and travel by foreign tourists. Despite market debacle and bird flue around, occupancies in Indian business hotels range around 80 per cent and the leisure markets of Goa, Rajasthan and Kerala have poured with foreign tourists like never before. The mismatch between demand and supply for accommodation however, leads to higher occupancies and surge in room rates as compared to past years. This exceptionally going good scenario in Indian hospitality industry is mainly driven by following factors.

Booming tourism Industry

In the third quarter of FY 2008, the hotels and tourism industry has recorded the revenue of \$14 billion, making a whopping 30% rise over the same period of last year. A huge surge in both business and leisure travel by domestic and foreign tourists has fuelled this growth. With India's emergence as a global economy and outsourcing hub, the number of dollar-paying business travelers is on rise.¹

Medical Tourism

According to Confederation of Indian Industry (CII), India is likely to become a major hub for medical tourism, with revenues from the industry estimated to grow from US\$333m in 2007 to US\$2.2 billion by 2012.² India's emergence as low cost and high quality healthcare service provider is expected to boost medical tourism in India, which alternately calls for need of more rooms in future.

Increasing Household Income

The growth in domestic tourism is also supported by rising disposable incomes and cheaper airfares offered by low-cost airlines. An increasing number of

“The industry needs to be recognized and be given the status of an infrastructure industry.”

— Ajoy Misra
Senior VP
(Sales & Marketing)
The Indian Hotels
Company Limited

people are opting for holiday packages, which are now facilitating easier and convenient travel. This has consequently benefited the hospitality industry.

Challenges

The clear picture of room shortage clearly indicates the deficiency of hotel sector to keep the pace with rising demand. The major challenges that hinder the process of growth in number of rooms are mentioned below:

Bureaucratic Constraints

Despite being an important element of economy and employment generator, the hospitality industry isn't treated on par when it comes to concessions. Taxation is complex and heterogeneous throughout the country. The recent tax holiday incentive is granted only to hotels coming up in the NCR region. Hospitality industry is currently witnessing bottlenecks like limitations on hotel bed and FAR (Floor to Area Ratio). Also, the budgetary allocation for tourism, of which the hospitality industry is a major segment, was only Rs 900 crore for 2007-08.³

Moreover, the government has stepped out to offer helping hands with the divestment of many properties under the India Tourism Development Corporation. For the budget segment, it introduced the 'Incredible India Bed & Breakfast Scheme' across the country with the dual objective of providing budget home-stay facilities to tourists and augmenting incomes of urban middle class having surplus accommodation.

Sky Rocketing Real Estate Rates

According to Praveen Chugh, Chairman, Travel Agents Federation of India (TAFI), rigid land use laws, skyrocketing real estate prices and lots of formalities have kept the industry from building more hotels required to accommodate the swell in tourist arrivals.⁴ In the same tone, lands, which are sold through auctions and tenders, have mind-boggling rates that would justify only 'seven-star' properties. The auctioning created an artificial demand, to increase the plot price that never existed.⁵

Poor Infrastructure

According to estimates of the World Travel and Trade Council, India will become the third most rapidly growing tourist market after Montenegro and China in 2013.⁶ To achieve this sustainable growth, industry experts cite that Indian hospitality industry needs to tackle several issues relating to poorly facilitated airports, inadequate hotel rooms, and poor road and transport infrastructure.

"Difficulties of obtaining suitable land, bureaucracy associated with real estate and constraints of infrastructure mean India is an expensive opportunity,"

— Jonathan Worsley,
Co-organizer
Arabian Hotel Investment
Conference (AHIC)

Forthcoming Sport Events

The current situation of room crunch is expected to worsen at around key events, such as Commonwealth Games in 2010 and Cricket World Cup in 2011. India's travel and tourism industry has estimated around 150,000 additional visitors to Delhi for the Commonwealth Games. This calls for a need of about 30,000 rooms and an investment of about Rs 15,000 crore (US\$3.81 billion).⁷

Competition from Foreign Players

Recognizing the huge potential, many global hospitality giants are foraying into India. Given the demand-supply imbalance across cities, several domestic and global players are rushing to claim a pie of this market. Ritz-Carlton and Four Seasons, world's biggest hotel brands are establishing hotels in Bangalore and Mumbai. Brands such as Hilton and Marriott are building 1,600 and 1,800 rooms, respectively, in 2008. New York-based Hampshire Hotels & Resorts (HHR), is also investing Rs 4,500 crore in India. Various other hotel chains are building about 100 new hotels in the country.⁸ The move of foreign players is set to increase the competition for local players.

New Standards of Luxury for Indian hotels

Until recent few years, luxury for Indian hotels was limited to the interiors. But the slew of foreign players in India will soon expect to call for new standards of luxury. Aware of the challenge, Indian hoteliers too are refining their services, but their ability to compete in the luxury segment is still suspect. To address the need of new age luxury standards, Indian hotels need to innovate the culture that genuinely cares for the guest.

Is the demand "Real"?

According to the year-end review of the performance of Ministry of Tourism & Culture, India needs total of 240,000 hotel rooms. However the current availability is just 90,000 rooms, leaving a requirement of additional 150,000 rooms.⁹ The wide gap between demand and supply in India has soared hotel room rates by 48 percent in 2007, while the commercial capital Mumbai recorded a whopping 69 percent rise. Driven by an average room rate that now stands at US\$270, Mumbai recorded a staggering 46.2 per cent revPAR growth. This high potent market has invited several foreign players in India, and current players are planning for big expansion across the country. However it is surprising to know that, despite the tremendous boom in travelers, hotels across India have mere 70 to 80 per cent of occupancies. This actuates the question, where the remaining tourists sought accommodation? It's the growing segment of unconventional accommodation, which lies underneath the tide of hotels. These are the places where unoccupied capacity of luxury accommodation is moving.

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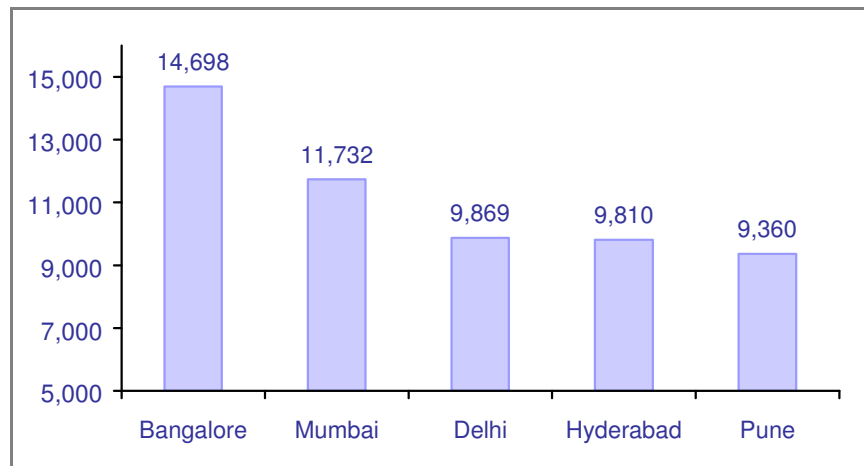
— Jonathan Worsley,
Co-organizer
Arabian Hotel Investment
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driving the need for
different class of hotels"

— Homi Aibara
Aibara Consultants

Alternate Accommodation to Satisfy Real Demand for Rooms

The recent industry estimates suggest that, as Indian economy gets richer, there is a sustained demand for short-duration travel at major destinations and these markets will grow exponentially in the next three-five years.¹⁰

The Near Future Room Supply in Major Cities



Source: The Economic Times, February 06, 2008

The chain with the highest rooms in India is not a hotel. It is Infosys, the IT giant.

Statistics suggests that, expansion of current capacity will set to induce ample availability of rooms in near future. Since travelers are turning way from luxury hotels to unconventional accommodation, these efforts to bridge the demand-supply gap may create oversupply of rooms after 2010. This is something that hoteliers need to keep in mind before setting up the huge investment. Moreover, the question of unfilled rooms in these luxury accommodations is still unanswered. Not only foreign players, but alternate options with cheap rates and homely atmosphere will set to compete with India luxury hotels in near future. This will certainly call for a critical choice to Indian hoteliers, either to shape up themselves as per 'real' demand or slip down the ranks. Some alternatives that are embraced by today's customer segments are mentioned below.

Corporate World Finds its Own Way

Indian organizations are trying to find out new ways to beat the pocket pinching hotel room rates. While Microsoft is using its own videoconferencing technology to carry out live meetings, Infosys has built a 500-room hotel next to it's headquarter in Bangalore. Infosys currently own 15,000 rooms across India, an eighth of all rooms in India. Costly rooms in Tier-I cities are forcing salespeople and other professionals to commute from far away places. It is inevitable for Indian enterprises to adopt such cost cutting models for business visits. This is signaling the turn away of business travelers from hotels and will certainly impact the hospitality business in near future.¹¹

Government to Offer Cheaper options

In an attempt to expand the room supply, Indian government has launched 'Incredible India Bed & Breakfast Scheme' across the country. Government is advertising through newspapers that urge families to convert their homes into bed-and-breakfast operations, which can charge about \$35 a night. The government's goal is to approve enough homes turned hostels to offer another 10,000 rooms in time for the Commonwealth Games in 2010. Looking forward, this cheaper option is likely to become popular for leisure travelers, as it gives a change to experience the flavor of local culture from close.

Unconventional Accommodation

The tremendous boom in inbound travel for the coming years has impelled hospitality industry to expand in order to anticipate the rising need for rooms. This isn't limited to hotels but even unconventional alternative accommodations - home-stays, timeshare resorts, condominiums, etc - that are evolving as a lucrative segment. Another rarely discussed form of budget accommodation which turns the travelers away from hoteliers are religious centers and ashrams. Since they lack in luxury, it's not utilized by business travelers yet. However, given the cleanliness and hygiene of these accommodations, this segment offers huge potential for inbound and foreign tourists. The Krishnamurti Foundation India at Raj Ghat in Varanasi near the Ganges offers such guesthouse accommodation. Other prominent ashrams that are providing reasonable stays throughout India are Bharat Sevashram Sangha, Ramakrishna Mission, ISKCON and Aurobindo Ashram.

At present moment the number of such centers is negligible, vis-à-vis economy hotels, however, it is still a viable option for budget tourists. Travelers are now enthusiastic to travel differently to experience the stay at natural best. Since this alternate accommodation options has unearthed the hidden potential of the Indian market, it reflects the maturity of hotel industry.¹²

Conclusion

Indian hospitality industry today is an ideal example to brush up the economic 'theory of demand-supply'. Expensive room rates, sky-high real estate prices and foreign players move in India is inevitable in such scenario. Booming economy, influx of foreign tourists would certainly boost hospitality industry in future. But contrary picture of 20-30 per cent unoccupied rooms reveal the fact of availability of alternate options that tourists prefer today. These alternatives call for hoteliers to reconsider the ongoing expansion of hotels across the India, eyeing at the huge inbound travel. The popularity of these accommodations will likely to leave high capacity hotels with low occupancy. Hoteliers need to estimate "the real demand for rooms" before they invest huge capital in expansion, otherwise it leads to oversupply of rooms in future and hoteliers would leave with unoccupied rooms.

"The growth of alternate accommodation is a signal of a maturing Indian hospitality market."

—Y Siddharth Reddy,
CEO
Country Club India



Sources

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