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The implications of the falling US dollar for global tourism

Although current trends do not seem to support the evidence, our report on Canada outbound travel in this issue of *Travel Markets* shows that Canadian demand for travel to the USA has in the past always closely tracked the C$:US$ exchange rate. Similarly, research by Global Insight suggests that US outbound travel generally has increased and decreased in line with the strength of the US dollar – although there has historically been a longer time-lag than in the case of the Canadians.

Certainly, while other factors such as household income, socio-demographic trends and consumer confidence also have an influence, no other economic indicator has the unilateral ability to affect travel patterns like exchange rates. A shift in the real (inflation-adjusted) exchange rate between an origin and destination country automatically acts as a price lever that can make a destination either prohibitively expensive or invitingly affordable. Looked at differently, origin markets can be suppressed or revived as a result of their currency-determined purchasing power.

The value of the US dollar will continue to decline over the next several years, analysts currently believe, although the rate of decline will slow from that of the past year and a half. Among the major industrialised nations, the dollar's future decline is expected to be greatest against the euro (against which it has already lost close to 30% of its value since late-2001). The drop against the Canadian dollar (at 18% so far) will be limited to only an additional 3-4%. For the UK (-16% to date) and Japan (-18%), the declines are expected to fall between these extremes.

So who benefits and who loses?

Clearly, although there will almost certainly be a time lag for most destinations, those with currencies linked to the dollar will benefit as prices implicitly fall. Conversely, those destinations with rising currencies vis-à-vis their source markets will become more expensive and will suffer. This should facilitate a much needed recovery in US tourism and will benefit much of the Caribbean, where most currencies are fixed to the dollar.

In addition, Asian countries with little recent currency movement on the dollar – eg China, Hong Kong, Malaysia, Singapore and Thailand – should benefit as lower-cost destinations. In Europe, the eurozone could well suffer as the strong euro encourages travel out of the region by its residents and discourages inbound travel.

However, these assumptions are too simplistic in that they fail to take into account various countries' dependencies on specific markets. As an example, Ireland faces a larger hurdle than Spain because of its higher dependence on the US market. Although both have currencies fixed to the US dollar, Hong Kong will benefit more than mainland China.

A more scientific approach to determining relative exchange rates

In order to understand and quantify the true exchange rate impact on travel, USA-based Global Insight has developed a new series called the 'tourism-weighted exchange rate' (TWER). The TWER is calculated as the average exchange rate for a destination, weighted by each of its origin markets' share of total arrivals. This is then is adjusted for relative inflation in the origin and destination to calculate a measure of the average change in prices for tourists to each destination. The concept measures the average price benefit or cost incurred by shifts in exchange rates between a destination and its origin markets.

As a guide – and further information on TWER is available from Global Insight – Canada and Ireland are forecast to be strongly affected as a function of their strengthening currencies and their dependence on the US market. In contrast, Egypt, Argentina and Venezuela should benefit as their respective currencies have depreciated even more than the US dollar and they have become extremely inexpensive destinations.

All the eurozone is at risk, with Ireland and Netherlands heading the list of destinations most likely to be affected. The UK and other non-euro-based countries in Europe should benefit. In the case of the UK, although it will be less attractive to Americans – a very important source market – it will be more attractive to its neighbours, which will more than compensate for this effect. In Central Europe, Hungary, Russia, Slovakia and the Czech Republic will all struggle against relatively stronger currency-induced prices for their attractions.

Asia also has exchange rate winners and losers. Indonesia, Australia, New Zealand, South Korea and Malaysia will, on average, be more expensive to its source markets over the 2000-05 time period. However, Japan, Hong Kong, Singapore, China and Taiwan will benefit from relatively weaker prices vis-à-vis their source markets.

In summary, some countries seem to be entering 2004 with the chips stashed against them. We will return to the subject in the course of the year to judge the accuracy of the predictions. But then who ever takes exchange rate forecasts – or even economic or travel forecasts – seriously?