

Travel, Logistics & Transport Infrastructure Practice

# Reimagining the \$9 trillion tourism economy—what will it take?

As national borders consider reopening, a partnership between governments and the tourism industry will be essential.

*by Margaux Constantin, Steve Saxon, and Jackey Yu*



**Tourism made up** 10 percent of global GDP in 2019 and was worth almost \$9 trillion,<sup>1</sup> making the sector nearly three times larger than agriculture. However, the tourism value chain of suppliers and intermediaries has always been fragmented, with limited coordination among the small and medium-size enterprises (SMEs) that make up a large portion of the sector. Governments have generally played a limited role in the industry, with partial oversight and light-touch management.

COVID-19 has caused an unprecedented crisis for the tourism industry. International tourist arrivals are projected to plunge by 60 to 80 percent in 2020, and tourism spending is not likely to return to pre-crisis levels until 2024. This puts as many as 120 million jobs at risk.<sup>2</sup>

Reopening tourism-related businesses and managing their recovery in a way that is safe, attractive for tourists, and economically viable will require coordination at a level not seen before. The public sector may be best placed to oversee this process in the context of the fragmented SME ecosystem, large state-owned enterprises controlling entry points, and the increasing impact of health-related agencies. As borders start reopening and interest in leisure rebounds in some regions,<sup>3</sup> governments could take the opportunity to rethink their role within tourism, thereby potentially both assisting in the sector's recovery and strengthening it in the long term.

In this article, we suggest four ways in which governments can reimagine their role in the tourism sector in the context of COVID-19.

## **1. Streamlining public-private interfaces through a tourism nerve center**

Before COVID-19, most tourism ministries and authorities focused on destination marketing,

industry promotions, and research. Many are now dealing with a raft of new regulations, stimulus programs, and protocols. They are also dealing with uncertainty around demand forecasting, and the decisions they make around which assets—such as airports—to reopen will have a major impact on the safety of tourists and sector employees.

Coordination between the public and private sectors in tourism was already complex prior to COVID-19. In the United Kingdom, for example, tourism falls within the remit of two departments—the Department for Business, Energy, and Industrial Strategy (BEIS) and the Department for Digital, Culture, Media & Sport (DCMS)—which interact with other government agencies and the private sector at several points. Complex coordination structures often make clarity and consistency difficult. These issues are exacerbated by the degree of coordination that will be required by the tourism sector in the aftermath of the crisis, both across government agencies (for example, between the ministries responsible for transport, tourism, and health), and between the government and private-sector players (such as for implementing protocols, syncing financial aid, and reopening assets).

Concentrating crucial leadership into a central nerve center is a crisis management response many organizations have deployed in similar situations.<sup>4</sup> Tourism nerve centers, which bring together public, private, and semi-private players into project teams to address five themes, could provide an active collaboration framework that is particularly suited to the diverse stakeholders within the tourism sector (Exhibit 1).

We analyzed stimulus packages across 24 economies,<sup>5</sup> which totaled nearly \$100 billion in funds dedicated directly to the tourism sector, and close to \$300 billion including cross-sector packages with a heavy tourism footprint. This

<sup>1</sup> See "Economic impact reports," World Travel & Tourism Council (WTTC), wttc.org.

<sup>2</sup> "International tourist numbers could fall 60-80% in 2020, UNWTO reports," World Tourism Organization, May 7, 2020, unwto.org.

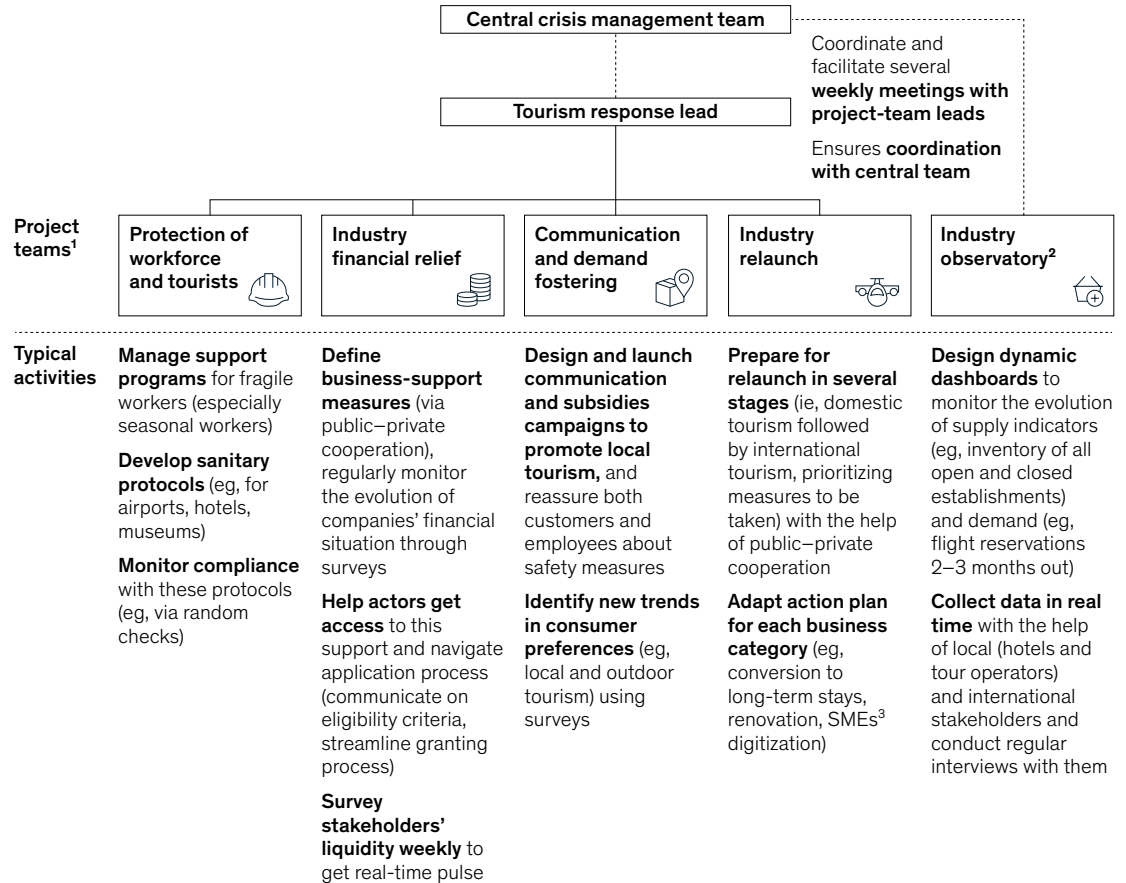
<sup>3</sup> See Riccardo Boin, Alex Cosmas, Alex Dichter, and Nina Wittkamp, "A new approach in tracking travel demand," May 29, 2020, McKinsey.com.

<sup>4</sup> See Mihir Mysore and Ophelia Usher, "Responding to coronavirus: the minimum viable nerve center," March 16, 2020, McKinsey.com.

<sup>5</sup> Australia, Bahrain, Belgium, Canada, Egypt, Finland, France, Germany, Hong Kong, Indonesia, Israel, Italy, Kenya, Malaysia, New Zealand, Peru, Philippines, Singapore, South Africa, South Korea, Spain, Switzerland, Thailand, and the United Kingdom.

## Teams are built to reflect real-world needs rather than existing organizational entities.

### A tourism nerve center as an agile team across public and private sectors



<sup>1</sup>Typical full-time teams include data analysis, legal, communications, finance or budget, supply chain, and procurement.

<sup>2</sup>Can be part of a central crisis management observatory.

<sup>3</sup>Small and medium-size enterprises.

stimulus was generally provided by multiple entities and government departments, and few countries had a single integrated view on beneficiaries and losers. We conducted surveys on how effective the public-sector response has been and found that two-thirds of tourism players were either unaware of the measures taken by government or felt they

did not have sufficient impact. Given uncertainty about the timing and speed of the tourism recovery, obtaining quick feedback and redeploying funds will be critical to ensuring that stimulus packages have maximum impact.

## 2. Experimenting with new financing mechanisms

Most of the \$100 billion stimulus that we analyzed was structured as grants, debt relief, and aid to SMEs and airlines. New Zealand has offered an NZ \$15,000 (US \$10,000) grant per SME to cover wages, for example, while Singapore has instituted an 8 percent cash grant on the gross monthly wages of local employees. Japan has waived the debt of small companies where income dropped more than 20 percent. In Germany, companies can use state-sponsored work-sharing schemes for up to six months, and the government provides an income replacement rate of 60 percent.

Our forecasts indicate that it will take four to seven years for tourism demand to return to 2019 levels, which means that overcapacity will be the new normal in the medium term. This prolonged period of low demand means that the way tourism is financed needs to change. The aforementioned types of policies are expensive and will be difficult for governments to sustain over multiple years. They also might not go far enough. A recent Organisation for Economic Co-operation and Development (OECD) survey of SMEs in the tourism sector suggested more than half would not survive the next few months, and the failure of businesses on anything like this scale would put the recovery far behind even the most conservative forecasts.<sup>6</sup> Governments and the private sector should be investigating new, innovative financing measures.

### Revenue-pooling structures for hotels

One option would be the creation of revenue-pooling structures, which could help asset owners and operators, especially SMEs, to manage variable costs and losses moving forward. Hotels competing for the same segment in the same district, such as a beach strip, could have an incentive to pool revenues and losses while operating at reduced capacity. Instead of having all hotels operating at 20 to 40 percent occupancy, a subset of hotels

could operate at a higher occupancy rate and share the revenue with the remainder. This would allow hotels to optimize variable costs and reduce the need for government stimulus. Non-operating hotels could channel stimulus funds into refurbishments or other investment, which would boost the destination's attractiveness. Governments will need to be the intermediary between businesses through auditing or escrow accounts in this model.

### Joint equity funds for small and medium-size enterprises

Government-backed equity funds could also be used to deploy private capital to help ensure that tourism-related SMEs survive the crisis (Exhibit 2). This principle underpins the European Commission's temporary framework for recapitalization of state-aided enterprises, which provided an estimated €1.9 trillion in aid to the EU economy between March and May 2020.<sup>7</sup> Applying such a mechanism to SMEs would require creating an appropriate equity-holding structure, or securitizing equity stakes in multiple SMEs at once, reducing the overall risk profile for the investor. In addition, developing a standardized valuation methodology would avoid lengthy due diligence processes on each asset. Governments that do not have the resources to co-invest could limit their role to setting up those structures and opening them to potential private investors.

## 3. Ensuring transparent, consistent communication on protocols

The return of tourism demand requires that travelers and tourism-sector employees feel—and are—safe. Although international organizations such as the International Air Transport Association (IATA), and the World Travel & Tourism Council (WTTC) have developed a set of guidelines to serve as a baseline, local regulators are layering additional measures on top. This leads to low levels

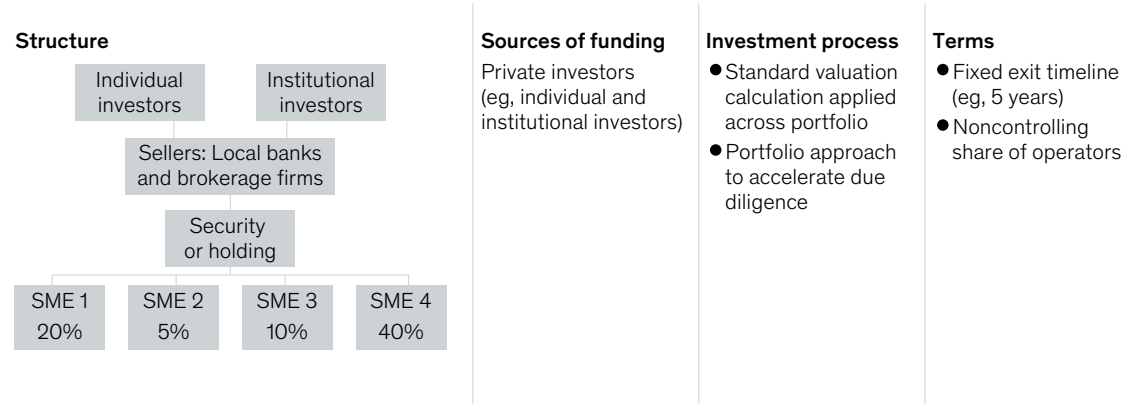
<sup>6</sup>See *Tourism policy responses to the coronavirus (COVID-19)*, OECD, June 2020, [oecd.org](https://www.oecd.org/).

<sup>7</sup>See "State aid: Commission expands temporary framework to recapitalisation and subordinated debt measures to further support the economy in the context of the coronavirus outbreak," European Commission, May 8, 2020, [ec.europa.eu](https://ec.europa.eu/).

Exhibit 2

**Facilitating the investment of private capital in the hospitality sector can ensure continuity of supply in the tourism industry, especially in subsectors and geographies heavily reliant on SMEs.**

Illustrative model



of harmonization regarding regulations imposed by local governments.

Our surveys of traveler confidence in the United States suggests anxiety remains high,<sup>8</sup> and authorities and destination managers must work to ensure travelers know about, and feel reassured by, protocols put in place for their protection. Our latest survey of traveler sentiment in China suggests a significant gap between how confident travelers *would like to feel* and how confident they *actually feel*; actual confidence in safety is much lower than the expected level asked a month before.<sup>9</sup>

One reason for this low level of confidence is confusion over the safety measures that are currently in place. Communication is therefore key to bolstering demand. Experience in Europe indicates that prompt, transparent, consistent communications from public agencies have had a similar impact on traveler demand as CEO

announcements have on stock prices. Clear, credible announcements regarding the removal of travel restrictions have already led to increased air-travel searches and bookings. In the week that governments announced the removal of travel bans to a number of European summer destinations, for example, outbound air travel web search volumes recently exceeded pre-crisis levels by more than 20 percent in some countries.

The case of Greece helps illustrate the importance of clear and consistent communication. Greece was one of the first EU countries to announce the date of, and conditions and protocols for, border reopening. Since that announcement, Greece’s disease incidence has remained steady and there have been no changes to the announced protocols. The result: our joint research with trivago shows that Greece is now among the top five summer destinations for German travelers for the first time. In July and August, Greece will reach inbound

<sup>8</sup>See Vik Krishnan, Ryan Mann, Nathan Seitzman, and Nina Wittkamp, “Hospitality and COVID-19: How long until ‘no vacancy’ for US hotels?,” June 10, 2020, McKinsey.com.

<sup>9</sup>See Kay Chen, Will Enger, Jackey Yu, and Cherie Zhang, “Hitting the road again: How Chinese travelers are thinking about their first trip since COVID-19,” May 14, 2020, McKinsey.com.

airline ticketing levels that are approximately 50 percent of that achieved in the same period last year. This exceeds the rate in most other European summer destinations, including Croatia (35 percent), Portugal (around 30 percent), and Spain (around 40 percent).<sup>10</sup> In contrast, some destinations that have had inconsistent communications around the time frame of reopening have shown net cancellations of flights for June and July. Even for the high seasons toward the end of the year, inbound air travel ticketing barely reaches 30 percent of 2019 volumes.

Digital solutions can be an effective tool to bridge communication and to create consistency on protocols between governments and the private sector. In China, the health QR code system, which reflects past travel history and contact with infected people, is being widely used during the reopening stage. Travelers have to show their green, government-issued QR code before entering airports, hotels, and attractions. The code is also required for preflight check-in and, at certain destination airports, after landing.

#### **4. Enabling a digital and analytics transformation within the tourism sector**

Data sources and forecasts have shifted, and proliferated, in the crisis. Last year's demand prediction models are no longer relevant, leaving many destinations struggling to understand how demand will evolve, and therefore how to manage supply. Uncertainty over the speed and shape of the recovery means that segmentation and marketing budgets, historically reassessed every few years, now need to be updated every few months. The tourism sector needs to undergo an analytics transformation to enable the coordination of marketing budgets, sector promotions, and calendars of events, and to ensure that products

are marketed to the right population segment at the right time.

Governments have an opportunity to reimagine their roles in providing data infrastructure and capabilities to the tourism sector, and to investigate new and innovative operating models. This was already underway in some destinations before COVID-19. Singapore, for example, made heavy investments in its data and analytics stack over the past decade through the Singapore Tourism Analytics Network (STAN), which provided tourism players with visitor arrival statistics, passenger profiling, spending data, revenue data, and extensive customer-experience surveys. During the COVID-19 pandemic, real-time data on leading travel indicators and "nowcasts" (forecasts for the coming weeks and months) could be invaluable to inform the decisions of both public-sector and private-sector entities.

This analytics transformation will also help to address the digital gap that was evident in tourism even before the crisis. Digital services are vital for travelers: in 2019, more than 40 percent of US travelers used mobile devices to book their trips.<sup>11</sup> In Europe and the United States, as many as 60 percent of travel bookings are digital, and online travel agents can have a market share as high as 50 percent, particularly for smaller independent hotels.<sup>12</sup> COVID-19 is likely to accelerate the shift to digital as travelers look for flexibility and booking lead times shorten: more than 90 percent of recent trips in China were booked within seven days of the trip itself.<sup>13</sup> Many tourism businesses have struggled to keep pace with changing consumer preferences around digital. In particular, many tourism SMEs have not been fully able to integrate new digital capabilities in the way that larger businesses have, with barriers including language issues, and low levels of digital fluency. The commission rates on existing

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<sup>10</sup>Based on IATA Air Travel Pulse by McKinsey.

<sup>11</sup>Global Digital Traveler Research 2019, [Travelport, marketing.cloud.travelport.com](https://marketing.cloud.travelport.com); "Mobile travel trends 2019 in the words of industry experts," blog entry by David MacHale, December 11, 2018, [blog.digital.travelport.com](https://blog.digital.travelport.com).

<sup>12</sup>Sean O'Neill, "Coronavirus upheaval prompts independent hotels to look at management company startups," Skift, May 11, 2020, [skift.com](https://skift.com).

<sup>13</sup>See Will Enger, Steve Saxon, Peimin Suo, and Jackey Yu, "China's travel recovery gains steam: How families are planning their summer vacations," June 12, 2020, [McKinsey.com](https://mckinsey.com).

Exhibit 3

## Government-supported platforms or data lakes could allow the rapid creation of packages that include SME product and service offerings.

### Tourism Exchange Australia (TXA)<sup>1</sup>

#### Matchmaker

Promote tourism experience by connecting suppliers with distributors and intermediaries to benefit from the breadth of product offerings:

- Aggregates offerings; offers diverse product categories (eg, accommodation, attractions, events)
- Enhance diversity and packaging of offerings to optimize visitors experience
- Share data and provide analytical insights



<sup>1</sup>TXA is a national booking-exchange platform providing a competitive marketing advantage by making products both visible and bookable on a multitude of distributors, facilitating a cost-effective way to market the industry.

platforms, which range from 10 percent for larger hotel brands to 25 percent for independent hotels, also make it difficult for SMEs to compete in the digital space.

Governments are well-positioned to overcome the digital gap within the sector and to level the playing field for SMEs. The Tourism Exchange Australia (TXA) platform, which was created by the Australian government, is an example of enabling at scale. It acts as a matchmaker, connecting suppliers with distributors and intermediaries to create packages attractive to a specific segment of tourists, then uses tourist engagement to provide

further analytical insights to travel intermediaries (Exhibit 3). This mechanism allows online travel agents to diversify their offerings by providing more experiences away from the beaten track, which both adds to Australia's destination attractiveness, and gives small suppliers better access to customers.

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Governments that seize the opportunity to reimagine tourism operations and oversight will be well positioned to steer their national tourism industries safely into—and set them up to thrive within—the next normal.

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