Spain’s tourism renaissance will drive economic growth this year

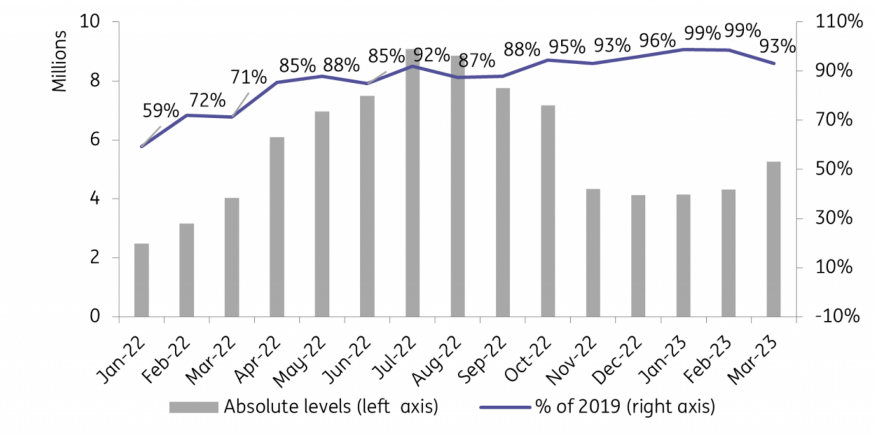
The recovery of the tourism sector in Spain is expected to continue, putting the industry at the centre of economic growth this year. However, due to macroeconomic uncertainty, high price pressure in the sector and lagging long-haul travel, it may take until 2024 for the number of international visitors to return to pre-pandemic levels

Spain's tourism industry will continue to recover this year

Spain's tourism revival expected to continue despite macroeconomic challenges

Despite macroeconomic challenges, Spain's tourism sector rebounded strongly in 2022. The country saw a remarkable increase in the number of international visitors, rising by 130% from 31.2 million in 2021 to 71.6 million in 2022, showing a strong appetite to travel again after two years of strict travel restrictions. Although disposable income was under severe pressure in many European countries last year, consumers refused to cut back on their travel spending. That being said, the number of international tourists entering Spain still remained 14% below pre-pandemic levels, proving that there is still a long way to go to full recovery.

Number of international visitors entering Spain, in absolute values and as % of 2019 levels



Source: INE

Challenges on the horizon: factors hindering the growth of international tourism in Spain

There are several factors that could hamper the growth of international tourism. One is that for Spain's main source countries, the UK and Germany, which accounted for 22% and 13% of international visitors in 2019 respectively, the economic outlook looks bleak. In the UK, the cost-of-living crisis has hit hard and we expect the UK economy to grow by only 0.2% this year. Meanwhile, the German economy has contracted over the past two quarters and is officially in a technical recession. We expect economic growth in Germany to stagnate this year. While the sharp fall in purchasing power is not currently deterring Europeans from travelling, it could cause price-sensitive travellers to swap Spain for cheaper destinations.

Unfavourable exchange rates are also encouraging British travellers to choose Turkey over southern European countries including Spain. A recent report by the European Travel Commission showed that Turkey had 69% more arrivals from the UK in the first quarter of this year than in 2019, while the number of arrivals in Spain was lower than in 2019. This shift in preference can be attributed to the significant price difference. The depreciation of sterling against the euro, combined with the continued devaluation of the Turkish lira against the euro, has made travelling to Turkey much more affordable for British tourists than visiting southern European countries such as Spain.

Another factor hampering recovery is the current travel restrictions on Russian travellers. In 2019, Spain welcomed 1.3 million visitors from Russia, accounting for about 1.6% of total tourist arrivals. This particular group of visitors will be completely absent in 2023. And Spain will not get a boost from Chinese tourism this year either. Although Chinese tourists are eager to travel again, they are favouring domestic trips or visits to neighbouring countries. The number of Chinese tourists visiting Spain was relatively modest even before the pandemic: about one million Chinese tourists travelled to Spain in 2019, which was only 1.3% of the total number of visitors that year.

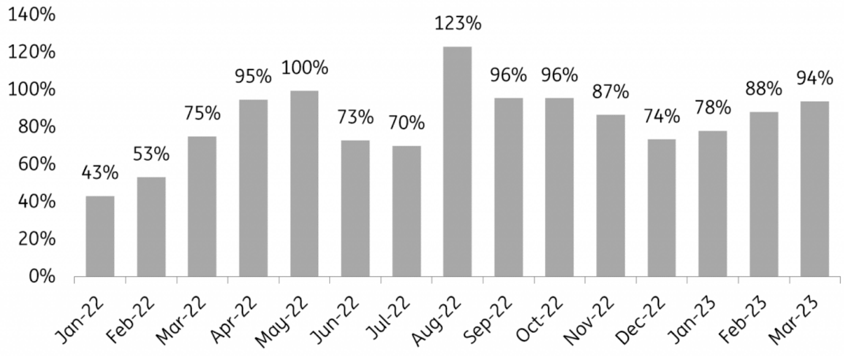
Business travel to Spain bounces back to pre-pandemic levels

Spain is witnessing a remarkable recovery in business travel after the sharp decline during the pandemic. In the first quarter of 2023, the number of international business travellers increased by 48% compared to the same period last year, returning to pre-pandemic levels. Business travellers represent a significant proportion of the total number of visitors. In 2019, 5.4 million foreign visitors visited Spain for professional reasons, or 6.5% of the total number of foreign visitors in 2019. This means that more than one international arrival in 20 comes to Spain for business reasons.

Last year, business travel recovered more slowly than leisure travel. Due to the shift online during the pandemic, many companies became more selective about the necessity and frequency of business travel, opting more for digital meetings or conferences. In addition, economic uncertainty and the energy crisis also caused a pullback in business travel at the turn of the year. While business travel was already at 96% of its pre-crisis level in October 2022, it fell to 74% in December as many companies adopted cost-saving measures and reduced their travel budgets.

Business travel has been steadily catching up since the beginning of this year. The Spanish economy has recovered strongly from the energy crisis, growing by 0.5% in the first quarter, and business confidence has returned. In March, the number of international business travellers was already back to 94% of the 2019 level. We expect that the recovery will persist throughout this year, resulting in half a million additional business travellers visiting Spain compared to 2022. Towards the end of the year, however, we might see a slight decline again if the pace of recovery slows and the US economy falls into recession.

Number of international visitors coming to Spain for professional reasons, in % of their number in 2019



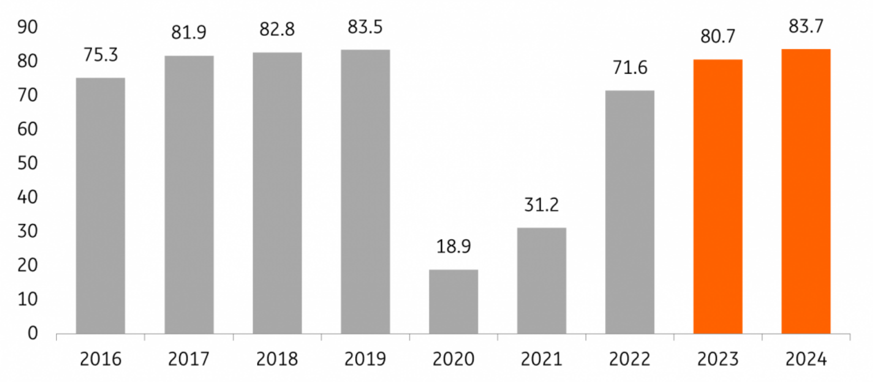
Source: INE

Outlook for international travel in 2023

Despite the headwinds, the first months of 2023 already showed a promising start for international tourism in Spain this year. In the first quarter, the number of foreign visitors reached 97% of pre-pandemic levels. Falling energy prices and stable labour market conditions may have underpinned the tourism sector. If this trend continues into the summer peak, it is likely that tourism figures in the summer months could match or even exceed 2019 levels for the first time.

The recovery in international travel is expected to continue into 2023, albeit at a slower pace than last year. The tourism sector is benefiting from continued strong travel appetite and a slightly improved economic outlook, thanks to a sharp fall in energy prices. However, persistent macroeconomic concerns will slow the pace of recovery, especially in the second half of this year. All in all, we expect a total of 80.7 million tourists to visit Spain in 2023, up by 13% from the previous year but still 3% below the pre-pandemic level. It will probably take until 2024 for the annual number of international tourists to reach 2019 levels again.

Number of international visitors entering Spain each year, including ING forecast (in millions)



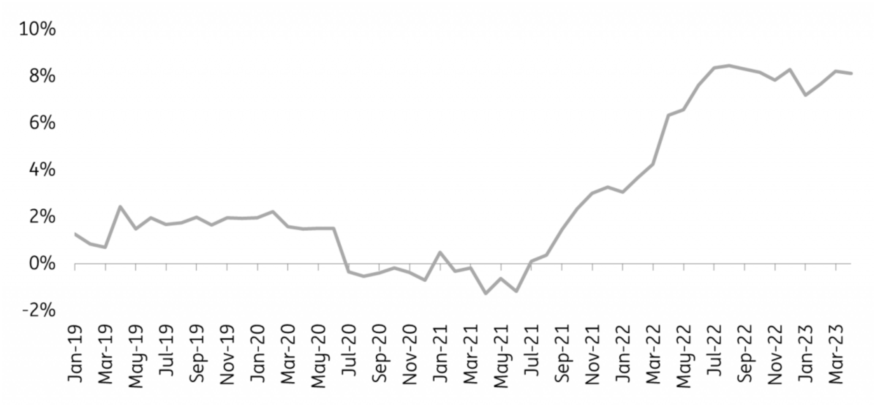
Source: INE, forecasts ING

Inflationary challenges in the tourism sector remain elevated

Inflation in the tourism sector remains stubbornly high, with significant pressure on all tourism activities. The consumer price index (CPI) for tourism and hospitality, a specific category within the broader index measuring price changes for tourism and hospitality-related goods and services, stood at 8.1% in April. This figure is just slightly below the peak level of 8.5% recorded in August 2022. Since the start of the pandemic, prices for tourism products and services have risen by an average of 16%.

Inflationary pressures can be attributed to two main factors. First, there are general inflationary pressures due to the increased cost of labour, raw materials and other inputs, which are passed on to consumers. In addition, sustained high demand and consumers' increased willingness to spend on travel and accommodation have given travel and accommodation providers greater pricing power. This allows them to capitalise on this higher demand by raising prices more easily.

Price pressures in the tourism sector show no signs of cooling yet



Source: INE

Increased price levels also have negative consequences. They may lead to a drop in domestic demand, especially among price-conscious travellers or those with limited disposable income. Moreover, potential international visitors may opt for alternative destinations that offer similar travel experiences at more affordable prices. Those who still visit Spain will adjust their spending patterns to mitigate the impact of high prices.

In March, foreign tourists spent an average of €168 per day, up 7% from March 2022. However, given average inflation of 8.1% in the tourism sector, this equates to a 1% drop in real spending. It seems that, in order to cope with significant price increases, visitors are cutting back on certain expenses, such as choosing cheaper accommodation, budget-friendly restaurants and cost-effective activities. In addition, many travellers shorten their trips as another effective strategy to reduce overall travel costs. While the average duration of a trip was 8.0 days in March last year, it has now dropped to 7.6 days.

Tourism will be the main catalyst for economic growth this year

Tourism is a significant contributor to Spain's GDP. According to data from the World Travel and Tourism Council (WTTC), for the year 2019, tourism represented 12.4% of Spain's GDP. This includes the direct impact of sectors such as accommodation, catering, transport and tourist attractions. Taking into account indirect effects as well, tourism's total contribution to Spanish GDP reached 15.2%.

Further recovery of the tourism sector will play a central role in the country's growth this year. After a significant decline during the pandemic, Spanish tourism could further restore its importance to the Spanish economy. With household consumption declining and expected interest rate hikes dampening investment dynamics, tourism will be a key driver of growth this year. Our forecast is for growth of 1.9% for Spain, surpassing the eurozone's expected growth rate of 0.5%.

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