The Carbon Tax and Australia's Accommodation Industry

Tourism Accommodation Australia

Tourism Accommodation Australia (TAA) represents the needs and interests of the substantial operators of Australia's accommodation industry, providing leadership for its members through advocacy, industrial relations and legal support, intelligence, research, education and networking.

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A division of the AHA

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TAA's concerns continue to grow regarding Australia's recent introduction of a carbon tax. Carbon pricing is impacting heavily on accommodation businesses, with profit reductions of up to 12% attributable to increased costs related to the tax. It is estimated that across the Australian accommodation industry the carbon tax cost will be up to $114.9 million in its first year.[1]

Australia's tourism sector is seen as a leading growth and export-earning industry for Australia, yet government continues to load the sector with unnecessary costs and regulations that stifle its international competitiveness. Along with education, tourism is Australia's major services export. The accommodation industry is key to Australia's $35 billion tourism industry and tourism accommodation contributed $6.2 billion in gross product in 2010-11 (or 1.3% of Gross Domestic Product).

The Australian carbon tax is currently applied to the carbon emissions of about 300 of Australia's largest emitters. It is not directly applied to accommodation, however has caused significant price rises for major cost items to the industry such as electricity, laundry and repairs. Although the Australian accommodation industry is partially trade exposed, it receives no carbon related support or compensation.

Nowhere else in the world is paying as high a price for carbon with the benchmark European Union carbon price about one quarter of Australia's. Most countries have no carbon tax at all. General business costs for accommodation providers in Australia are already among the highest in the world. Cost rises in combination with current flat demand are squeezing margins and creating an environment for a carbon tax led investment drought in accommodation in many parts of the country. The costs of the tax are not only substantial in operational terms; the carbon tax reduces profits and therefore valuations, adds uncertainty and impedes investment.

TAA's position is that this inefficient tax needs to be repealed to put Australia's accommodation back on a more level playing field. The Australian Government must recognise and reverse the impact that the carbon tax is having on the Australian accommodation industry.

Fast Facts

- Carbon pricing is impacting heavily on accommodation businesses, with profit reductions of up to 12% attributable to the tax.
- Across the Australian industry AEC*group* estimates that the carbon tax cost will be up to $114.9 million in its first year.
- The value of a benchmark 200 room average Australian establishment will fall by up to 16.5%.
- The world's next most expensive established carbon price, the benchmark European Union price (which at the time of writing was trading as low as 3.71 euros per tonne CO_2-e), sits at about one quarter Australia's current rate.
- By 2049-50, inflation is forecast to increase the costs of operating a room by 249% whilst the carbon tax per room would increase between 932% and 1,220%.
- It is very difficult for businesses to estimate the future impact of the tax on their costs, feeding uncertainty in the sector as to future profits and unwillingness to invest.
- Australia is at risk of an accommodation investment drought, worsened by the carbon tax.
- The Australian Government must recognise and reverse the impact that the carbon tax is having on the Australian accommodation industry.

[1] Carbon Tax Impacts on the Australian Accommodation Industry, AEC*group* 2013

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How the Carbon Tax Impacts Australian Accommodation

TAA engaged leading national economic consultants AEC*group* to undertake a study of the impact of the carbon tax on Australia's accommodation industry. Whilst the tax is not directly levied on the industry, it indirectly impacts the cost base of accommodation providers. To estimate the impact of the carbon tax on the Australian accommodation industry in dollar terms, current proportional impacts on individual cost items were estimated from the literature and applied to TAA (2012) industry survey benchmark annual expenditure and ABS (2008) benchmark expenditure proportions on a per room basis. The report finds that the tax has already caused a number of cost items for the industry such as electricity, laundry and repairs to rise significantly. Subsequent profit reductions have the potential to adversely impact investment in the sector.

Attracting and justifying funding for new projects and expansions will be much more difficult with reduced margins and a more uncertain outlook. The cost of construction of new rooms is also set to rise significantly under the carbon tax burden. Industry will accumulate less funds to reinvest in new capacity, better quality fit-out and innovative new services.

Accommodation businesses have limited options to mitigate carbon tax impacts. The tax will increasingly impact the accommodation sector as carbon prices rise and the tax extends to additional industries in the future.

Driving Up Costs

AEC*group* estimates that in 2012-13 the carbon tax has already increased costs for accommodation businesses by up to 0.9%. This is a significant impact of 12% of profit on what is already a low margin industry with an average annual profit margin of only 7.2% (as estimated for 2012-13 without the carbon tax). Across the Australian industry AEC*group* estimates that the carbon tax cost will be up to $114.9 million in its first year.

Australian accommodation operators are enduring a range of cost rises with energy costs having seen the greatest immediate impact. As the price of carbon increases and extends to additional sectors such as transport, other major costs such as food and beverages will rise further.

Carbon tax costs are even being nominated as a basis for wage claims in upcoming enterprise bargaining processes. The industry has already shed jobs and consolidated significantly since 2008 due to rising costs. The carbon tax will contribute to this worrying trend across much of Australia.

Stifling Investment

A major concern for Australia is the impact on future investment due to the price increases driven by the carbon tax. In the current environment the tax is stifling investment in accommodation in Australia:

- Increased costs are squeezing margins and reducing profits. AEC*group* estimates the carbon tax will significantly impact average operator profitability by up to 12%;
- The uncertainty of the continued flow-through and pricing of carbon is undermining the credibility of future profit forecasts and increasing investment risk, placing pressure on capitalisation rates to increase (the relationship between current operating profits and asset value);
- The carbon tax is adding directly to the current historically high cost of construction. This is set to further increase as builders continue to pass on the full impact of the tax.

Based on AEC*group's* estimates of a reduction in annual average profit margins and an increase in capitalisation rates due to a less positive outlook, the value of a benchmark 200 room average Australian establishment will fall by up to 16.5%. As a result, finance is more constrained to build an equivalent new hotel at the same time that construction costs are rising.

Financing a new hotel development has already been difficult prior to the carbon tax with some cities (e.g. Perth) introducing government incentives to stimulate desperately needed supply. The carbon tax has significantly increased the gap between the cost and value of a new accommodation development.

By reducing profits, increasing construction costs and increasing business risk the carbon tax will act as a brake on the recovery of the nation's tourism sector in the foreseeable future.

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Tax Burden is the World's Highest

No other country is paying as high a price for carbon. Europe has the next most expensive established carbon price in the world, trading as low as Au$4.67 per tonne CO_2-e (at the time of writing) versus Australia's $23 per tonne CO_2-e

New Zealand, which is a significant competitor to Australia for international tourists, has a carbon price currently about 6% of that in Australia.

Most countries have no carbon tax at all.

Although the Australian accommodation industry is partially trade exposed, it is not compensated as a trade-exposed sector in the design of the carbon tax.

Costs set to Grow

The study by AEC*group* found that the carbon tax is already adding between $284 and $506 per room per year to the cost of providing accommodation, based on the current carbon price of $23 per tonne CO_2-e and the current exclusions and subsidies.

The Commonwealth Treasury forecasts the price of carbon to increase to $352 per tonne CO_2-e by 2049-50. On this basis, costs to industry will increase to $3,465 to $4,714 per room per year.

Over this period, inflation is forecast to increase the cost of operating a room by 249% whilst the carbon tax per room would increase between 932% and 1,220%.

Australian accommodation is already expensive by international standards and operators have reached the limit of being able to pass on costs. The carbon tax adds significantly to the burden of costs which businesses in the current market are forced absorb.

Complex and Uncertain

The Australian carbon tax is complex and uncertain. It applies differently each year – in terms of the actual price, in terms of the exact businesses liable, in terms of the level of compensation available and in terms of the extent to which other sectors pass on the cost.

The carbon tax is actually being implemented through a package of legislation. For example the charging of carbon on refrigerants is legislated through the Ozone Protection and Synthetic Greenhouse Gas (Import Levy) Amendment Regulation 2012 (No. 1), which introduces the carbon tax equivalent as an effective import charge.

Suppliers are unwilling to discuss the potential impact of the carbon price for fear of ACCC litigation if they misestimate. Increases are simply added to contracts when renewed.

It is very difficult for businesses to estimate the future impact of the tax. This feeds uncertainty in the sector and unwillingness to invest for the future.

Recommendations

TAA considers that the Australian Government must recognise and reverse the impact that the carbon tax is having on the Australian accommodation industry.

While average cost increases of up to 0.9% may not appear significant, in an existing high cost, flat demand environment, this is cutting directly into the viability of the industry.

Australia is at risk of a carbon tax led investment drought in accommodation. As the mining boom subsides, this will not assist the economy to restructure to industries such as construction and tourism. Business cannot effectively invest in reducing carbon footprints when their margins are shrinking.

The carbon tax impact on Australian accommodation operators must be removed or mitigated to avoid further painful consolidation in the sector.

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