

## CHAPTER 3

### THE NET ECONOMIC BENEFIT OF TOURISM TO AUSTRALIA

#### *Introduction*

3.1 Two questions are basic in addressing the issue of the costs and benefits of foreign investment in the Australian Tourist Industry. The first concerns whether tourism provides a net economic benefit to Australia; it is discussed in this chapter. The second, concerning whether foreign ownership in Australian tourism affects that benefit for Australia, is examined in Chapter 9.

#### *Problems in Measuring the Economic Benefit of Tourism*

3.2 The national economic benefit of various industries can be difficult to establish. It is not simply a matter of examining growth across various indicators. With regard to tourism, the Industries Assistance Commission has advised that large levels of expenditure in the tourism industry can be misleading in assessing the impact of tourism. The impact is appropriately measured not in terms of gross spending, but rather in terms of the net benefits that it generates: the costs associated with tourist needs, for example hotels and airline services, must be set against the gross benefits.<sup>1</sup> The IAC concluded that tourism growth entailed a net benefit because of the contribution it made to the increase in GDP. Despite the difficulties involved in formulating a method of establishing net economic benefit, the consensus seems to be that there is such a benefit.

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<sup>1</sup> Industries Assistance Commission, *Travel and Tourism*, 1989, p. 36

## *Methodologies for Assessing Net Benefit*

### Input-Output Analysis

3.3 The economic benefit of the overall tourism industry has been considered by the Industrial Assistance Commission (now known as the Industry Commission) in a discussion paper.<sup>2</sup> The IAC advised that input - output analysis has been employed to trace direct tourist expenditure through linkages between industries to calculate how much additional expenditure is generated. The Bureau of Industry Economics estimated, using this method, that each \$1 million of tourist expenditure was accompanied by an additional \$555 000 of expenditure on goods and services required by the tourist industry.<sup>3</sup>

3.4 The IAC has explained the limitations of the input - output method: it contains no price mechanisms and so is unable to account for a number of important consequences of increased tourism.<sup>4</sup> Similarly, another method known as the ORANI model, has limitations, but it does enable many of the cost pressures to be taken into account.

### The ORANI Model

3.5 The IAC has used the computer-based ORANI model of the Australian economy to predict the benefits of tourism on the economy. ORANI embodies microeconomic detail on the nature of production and demand in the economy and treats the economy as a system of inter-related industry sectors. The IAC's report *A guide to the IAC's use of the Orani Model* explained that this framework is especially suited to the analysis of 'what if ...' questions. The type of answers provided are not forecasts of the actual outcome (since this could be influenced by

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<sup>2</sup> IAC Discussion Paper No. 2 *Some Economic Implications of Tourism Expansion*, March 1989

<sup>3</sup> *Ibid*, p. 25

<sup>4</sup> *Ibid*.

many other factors) but are conditional projections of the influence of one particular policy change alone. This has been seen as an advantage of the ORANI model since it provides a framework for analysing important elements of an issue, rather than producing a definitive answer.<sup>5</sup> The Bureau of Tourism Research has commented on the inadequacies of input-output analyses and the virtues of the ORANI model:

Input-output analysis can give a picture of the importance of tourism to the economy. However, it is inadequate for judging the full economic impact of growth in tourism expenditure. Growth in one sector of the economy has ramifications for all other sectors which must be recognised. For example, as tourism competes for resources with other Australian industries, growth in tourism will increase costs to other industries.<sup>6</sup>

3.6 Nevertheless, reservations have been expressed about the use by the IAC of the ORANI model to identify changes in GDP as a measure of the impact of tourism on economic welfare for the following reasons:

- changes in GDP are not an indication of changes in net benefit for a community's welfare;
- while models such as ORANI are the best ways of determining the inter-industry effects of expanding tourism expenditure, their outputs in terms of changes in GDP cannot be interpreted as 'net benefits', or 'change in welfare' except under stringent assumptions not even approximated in the Australian economy; and
- ORANI is not intended to be a benefit-cost model and it is inappropriate to use its outputs as if they were measures of benefits and costs.<sup>7</sup>

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<sup>5</sup> Industries Assistance Commission, *A guide to the IAC's use of the ORANI Model*, 1987, pp. iii,iv

<sup>6</sup> Bureau of Tourism Research, *Australian Tourism Data Card*

<sup>7</sup> *Tourism in Australia*, p. 15

### *The Net Benefit of Tourism*

3.7            Whatever the difficulties involved, it seems clear that the economic benefit of the tourism industry to Australia can only be determined if the three elements are assessed together: domestic, outbound and inbound tourism.

#### *Domestic Tourism*

3.8            Domestic tourism is leisure-related expenditure by Australians at home. A benefit of such expenditure includes the maintenance of (or increase in) tourism employment. The costs include additional pressure on desirable holiday localities, wear of infrastructure and (where foreign ownership is involved) the repatriation of profits. Overall, however, it is difficult to imagine that domestic tourism could produce a negative net effect unless it generated imports significantly and/or tourist facilities and services were owned by foreign interests to a very significant degree and the profits were repatriated.

#### *Outbound Tourism*

3.9            Outbound tourism, by contrast, must be the least benign for the Australian economy. Outbound tourism is not without some benefits for the national economy; for example the purchase of Qantas air fares retains expenditure in Australia. Nevertheless, the major proportion of outbound tourism represents expenditure abroad.

#### *Inbound Tourism*

3.10           Inbound tourism is a significant foreign exchange earner for Australia bringing in around \$6 billion annually. There may be a benefit from tourism even if the economic value of inbound tourism is balanced against losses through outbound tourism. The Chairman of the Australian Tourism Industry Association (ATIA), Sir Frank Moore, suggested:

If we had not developed any inbound business or any international tourism at all, we would in fact have many more Australians going overseas than are now going. Nobody would suggest that the tourism industry therefore was worth less because we had not pursued our opportunities. The harder we fight and develop inbound tourism, the less need there is for Australians to go overseas to enjoy the same international levels and standards. I cannot for the life of me understand why one group is offset against the other because they are two entirely different areas.<sup>8</sup>

3.11 The development of a substantial inbound tourism industry may have provided significant foreign earning benefit in its own right, but also mitigated the potential costs associated with outbound tourism from Australia. The IAC has pointed to the significance of price competitiveness with regard to inbound tourism. Similar considerations apply to domestic tourism. The recent growth in inbound tourism has been associated with a large reduction in the real cost of tourism in Australia. For inbound tourists the cost has been lowered further because of the depreciation of the Australian dollar against other currencies, especially in 1986.<sup>9</sup>

3.12 While unable to quantify it, economists who presented evidence to the Committee were confident that net economic benefits accrued to Australia from overseas tourism. Professor G. Withers and Dr H.R. Clarke of the Department of Economics at La Trobe University were unequivocal on the issue, advising that the Australian aggregate economy benefits from inbound tourism, and that there is a net average gain, in economic terms to Australians from such tourism.<sup>10</sup> These economists note, however, that this conclusion requires that tourists pay all relevant costs including public sector, environmental, pollution and congestion costs caused by their presence and activities. There must be no external costs imposed upon the

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<sup>8</sup> Evidence, p. 229

<sup>9</sup> *Travel and Tourism*, p. 49

<sup>10</sup> *Submission No. 93*, p. 1, para. 1

Australian community. The economists stated that whether this condition is met is a matter for further investigation.<sup>11</sup>

3.13 Of course, some of the costs associated with providing the transport and accommodation infrastructure used by tourists are incurred overseas. For example, half of Qantas' revenue is spent overseas on such items as aircraft, fuel, promotion, sales offices, interest payments and the like.<sup>12</sup> Further, there are doubts about the ability of increased inbound tourism to make any fundamental difference to the size of the current account deficit. The argument runs along the following lines. In a world which there is a floating exchange rate,

... the foreign exchange rate market will operate to lessen demand for other goods and services, since an increase in tourism expenditure will push up the value of the home currency, and discourage exports and encourage imports. Additional receipts from foreign tourism will only lessen the current account deficit to the extent that aggregate savings increase more than aggregate investment. Since there is no reason to expect that extra tourism expenditures would encourage domestic savers to save more, the effects on the current account will be negligible.<sup>13</sup>

This study goes on to note that there is a need for further investigation of this question. Research appears to be required as the issues raised are fundamental for policy directions.

3.14 As part of the research program associated with its inquiry into travel and tourism, the IAC simulated a 20 per cent increase in inbound tourism using the

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<sup>11</sup> *Submission No.93*, p.3

<sup>12</sup> *Ibid*, p. 37

<sup>13</sup> P. Forsyth and L. Dwyer, *Measuring the Benefits and Costs of Foreign Tourism*, Discussion Paper No. 428, February 1992, Australian National University, Centre for Economic Policy Research. pp. 18-19

ORANI model. This research suggested that there would be substantial economic effects in the short term including:

- an increase in total exports of around 1.3 per cent;
- increased imports both as the expanding tourist industries purchase imports from overseas, and as the import-competing sector becomes less competitive;
- an improvement in Australia's balance of payments equivalent to around \$235 million in 1987-88 dollars, considerably less than the initial increase in tourist exports of \$900 million; and
- increased employment, despite net losses in the traditional export and import-competing industries, of around a quarter of a per cent, or 17,000 jobs.<sup>14</sup>

3.15 In addition to the IAC, the BTR<sup>15</sup> has recently published a study which employed the ORANI model to assess net benefits. The model employed by the BTR is known as ORANI-F, and the report was entitled *The Medium Term Significance of International Tourism for the Australian Economy*.

3.16 The report is useful as a comprehensive attempt to assess the benefit of increased foreign tourism. It provides a detailed discussion of the effects of an increase in inbound tourism over more than one hundred different sectors of the economy.<sup>16</sup> The BTR study contrasts with other net benefit analyses in that it presents its results in macroeconomic terms; other economists have concentrated on the microeconomic effects. The La Trobe University economists who advised the Committee on this matter, for instance, claimed in support of the principle that

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<sup>14</sup> *Some Economic Implications of Tourism Expansion Discussion Paper No. 2*, p. 28

<sup>15</sup> Bureau of Tourism Research, *The Medium Term Significance of International Tourism for the Australian Economy*, June 1991, p. 6

<sup>16</sup> *Ibid*, p. 7

economic net average gain results from inbound tourism (provided that foreign tourists cover associated costs):

More tourists mean (in the absence of external costs) increased business and trading opportunities for existing firms in Australia and hence both increased production and consumption possibilities for Australian residents.<sup>17</sup>

3.17 The conclusions drawn from the BTR study have important policy implications, not so much for tourism policy but for macroeconomic policy in general. In the study it was argued<sup>18</sup> that growth in tourism crowds out growth in other areas of the economy. If spare capacity exists, for example in parts of the labour market for which tourism is an employer, there is scope for a net increase in output as a result of inbound tourism growth. Typically, air transport benefits from tourism growth, as do communications, entertainment, leisure, restaurants and hotels, whereas mining and agriculture generally are adversely affected by the exchange rate effects of tourism growth in the medium term. The study concluded:

Whether or not inbound tourism growth generates balance of payments improvements depends critically on how government manage macroeconomic conditions. Unless conditions are such that increased inbound tourism expenditure is prevented from feeding into net additional demand for imports, increased tourism will not be reflected in an improvement in the balance of payments. If it is desirable that Australian's dependence on overseas savings fall in the medium term, then national savings must increase in order to finance any increase in investment induced by the increasing receipts from tourism exports. ...

An important feature of expansion in inbound tourism is that it changes the composition of Australia's exports. ... it reduces Australia's reliance on the traditional commodity exports in the rural and mining sectors. ...

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<sup>17</sup> *Submission No. 93*, p. 4

<sup>18</sup> *The Medium Term Significant of International Tourism for the Australian Economy*, p. 7



This diversification reduces the volatility of our export prices and receipts<sup>19</sup> ...

3.18 The BTR report on the economic net benefit of inbound tourism is the first in a series. The others will examine the regional effects of inbound tourism growth, and the effects of growth in domestic tourism, both at the national and State level. While these studies will be useful in their own right, the BTR needs to canvass the question of the limitations of the methodologies employed in these studies. It should seek the opinion of the Treasury and the Australian Bureau of Statistics in addition to leading academic economists.

3.19 Further, the BTR needs to produce similar studies on the benefit of domestic tourism and the economic effect of outbound tourism before a comprehensive picture of the economic benefit of tourism can be compiled.

### *Recommendations*

3.20 That the BTR canvass with government authorities, practising economists and academics alternative economic models for net benefit analysis, and that the BTR be provided with additional resources to allow it to carry out additional research functions.

3.21 That the Commonwealth Government request a BTR study into the costs and benefits of domestic tourism and outbound tourism and prepare a more comprehensive net benefit analysis of Australian tourism.

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<sup>19</sup> *Ibid.*

