The Japanese Tourism Market: Prospects

The following is an extract from our book J-Wellness 2020: The economics, career options, and investment opportunities, chapter six. ***Conceptasia*** *provides a diversity of consulting services that involve Japan's inbound tourism developments.*

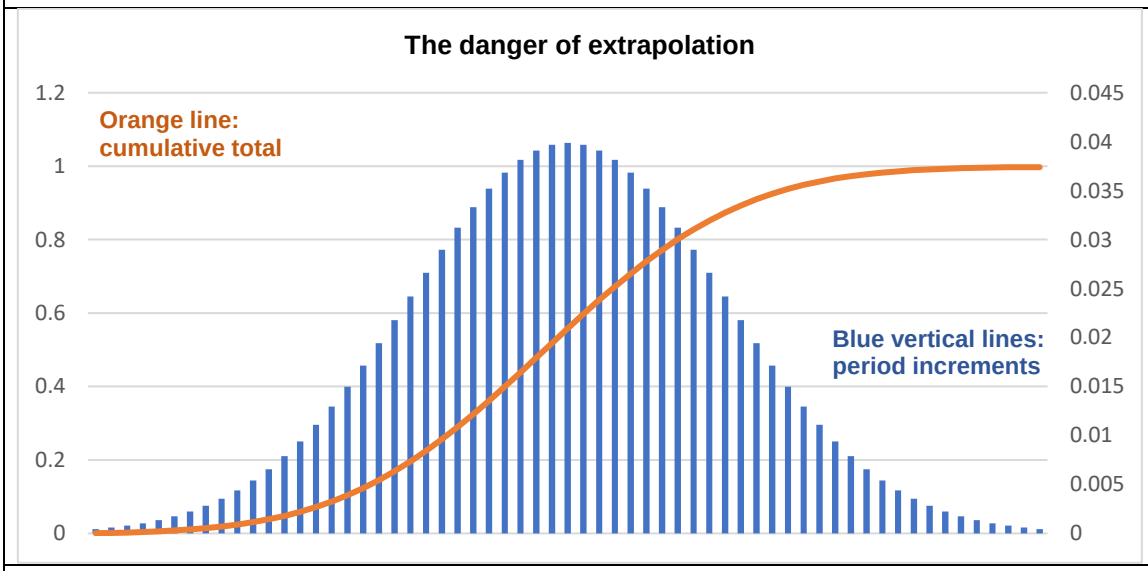
Forecasting is essential in investment, as an asset's value is linked to future cash flows.

We believe that forecasting requires structure, with the use of a simple model capturing the key variables. This also enables an awareness of the risks in the forecast. In contrast, complexity often obscures the core issues.

1) Extrapolation

One approach, and one of the easiest to use, is to extrapolate the experience of recent years to the coming few years. Practitioners are likely to be reasonably correct for a period, and then dramatically wrong. The orange line in Fig.1 is the familiar S-curve that is used to represent the lifecycle of industries. It is also often used to capture the market penetration of new products – from early adopters through to market saturation.

Fig.1 The S-Curve and the Bell curve behind it



Source: Conceptasia, April 2021

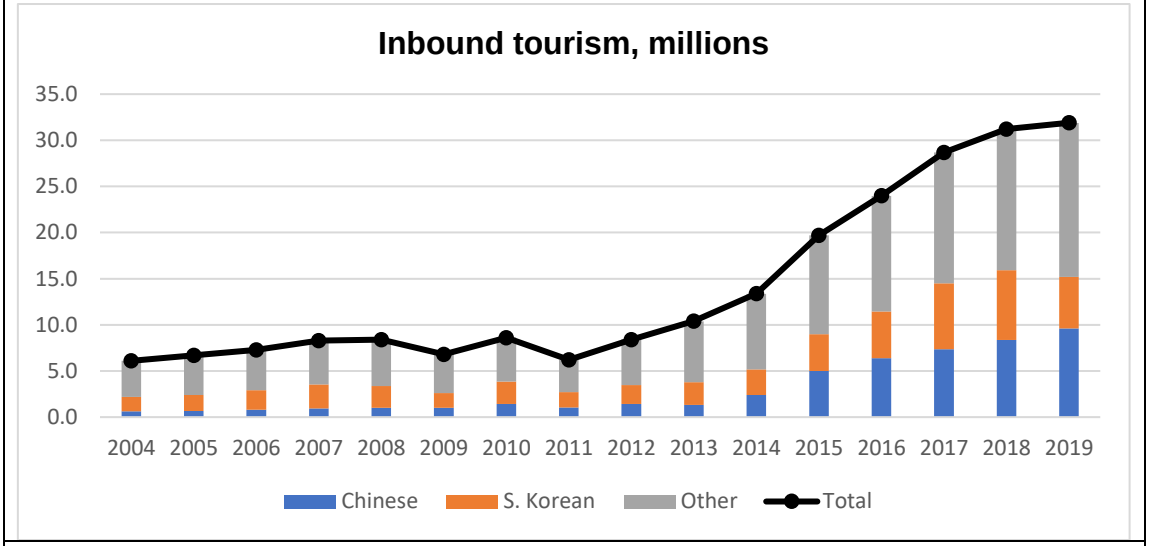
It is easy half-way up the curve, after a series of years of strong growth, to assume growth will continue indefinitely. Instead as the blue vertical lines attest, these are the increments from one period to the next, deceleration is inevitable and irreversible. It is easiest to think of a revolutionary new product like the smart phone. Yes, some people will be persuaded to own more than one, yes, the software and functionality will encourage a replacement cycle, but essentially once everyone has one the market is saturated, ex-growth. As Fig.1 shows, the best of the growth phase was over when market penetration reached around 50%.

There are elements of the above in the tourism industry. The Diffusion Model of Tourism forecasts tourism growth/contraction based on information flows, e.g., social network influencers, blog sites and so on. *Tourism Information Diffusion through SNSs: A theoretical investigation* by Ting Liu, Jianhong Xia and Lesley Crowe-Delaney [(1)] provides a good overview of the approach.

The discovery of an attractive "new" travel destination then spreads through SNS-type networks building momentum until saturation is reached, and/or the next attractive "new" destination is identified.

Common-sense is required with the extrapolation approach.

Fig.2 Inbound tourism, visitors to Japan



Source: Japan National Tourism Organization, Conceptasia, April 2021

How many years does it plausibly take before a new travel destination has been broadly discovered?

A beach destination will appeal to a smaller audience than a country with deep rich traditions, an abundance of natural scenery, and a commitment to hospitality. Nonetheless, premium growth rates relative to the growth of the global tourism market overall should not be expected to persist indefinitely.

2) Benchmarking

Seeking an anchor to expectations, this involves identifying a country with similar tourism attributes, but is already at an advanced stage of developing its tourism market. The difficulty is finding an appropriate peer, taking historical, cultural, and geographical factors into account.

It is best to identify the peer benchmark before looking at the tourism data, since aspirations can influence the decision. For example, from a richness of history perspective Japan could be compared to Italy. However, the tourism attractions of the Mediterranean climate and geography are more likely to be found in Asia somewhere in the ASEAN region, such as in Thailand or Malaysia.

Academic studies find that tourism is highly price sensitive.

This means that neighbouring countries with land borders and minimal border controls, i.e. visiting/transportation costs are low, experience high numbers of tourists. Examples would be France-Germany, the USA-Canada. Japan's geography is different, being an island archipelago.

A possible tourism benchmark for Japan is the United Kingdom (the U.K.). Similarities include:

- Both are advanced economies, G7 nations
- Both are islands situated off continental land masses with largely temperate climates
- Both have long histories and traditions, as well as contemporary arts, culture with international appeal

There are, of course, differences too, with the most important perhaps being the many centuries of overseas migration in the case of the U.K, versus the relative insularity of Japan over this period. With dispersed families, this leads to many visits to the U.K. being to visit relatives.

Fig.3 Japan and the United Kingdom: Key tourism data compared

	Japan	**United Kingdom**
Inbound visits	31.9 million (1)	37.9 million (2)
Inbound visits excluding to meet family/friends	NA	26.1 million (2)
A) Domestic trips (overnight, i.e. excluding daytrips)	323.7 million (3)	118.6 million (2)
B) Population	126.5 million	66.7 million
A/B expressed as average domestic trips per person per year	2.6	1.8
C) Outbound trips	20.1 million (1)	71.7 million (2)
D) Outbound trips excluding to meet family/friends	NA	55.0 million (2)
C/B for Japan; C/B & D/B for the UK: average outbound trips per person per year	0.2	1.1/0.8
E) Direct tourism employment (4)	6.48 million	1.56 million
F) Labour force (5)	68.86 million	33.96 million
E/F expressed in percentage terms	9.4%	4.6%
Tourism GVA (direct) as a % of total GVA (4)	NA	3.2%
Tourism GDP (direct) as a % of total GDP (4)	2.0%	NA
Notes: (1) 2019 Japan data, (2) 2018 UK data, (3) 2017 data, (4) OECD definitions and data, 2017, (5) OECD definitions and data, latest		
Source: National data, OECD, Conceptasia, April 2021		

Three observations

Observation one: As shown above, Japan's inbound tourists are now above those for the U.K. when the latter excludes visits to meet family and friends.

As noted above, Japan and the U.K. have hugely different histories of emigration, and this is probably the explanation for why the U.K. collects these numbers. (2) We believe the number of such visits into Japan is extremely low.

The inbound visits data Japan versus the U.K. suggests a need for caution; the strong growth, catch-up phase of inbound tourism into Japan might be behind us.

The UN World Tourism Organization (UNWTO) provides data on the number of inbound visitors arriving by air or sea (excluding those arriving by land) for some countries, e.g. for France and Italy, but not for Germany. Both France and Italy are exposed to the tourism attractions of the Mediterranean climate and geography. With that caveat on comparability, the 2017 numbers are France: 33.3 million, Italy 35.8 million. Japan's 31.9 million inbound visitors in 2019 is in the same ballpark.

Observation two: The average number of domestic trips excluding day trips is noticeably higher in Japan than the U.K. This appears to reflect the differing behaviour to outbound trips.

The average number of outbound trips per person per year is very different: 0.2 trips in the case of Japan (equivalent to one in five people going overseas each year), and 0.8 trips in the case of the U.K (excluding trips to meet family/friends). If we include trips to meet family/friends, the number in the U.K. becomes over one (1.1) implying that on average everyone leaves the U.K. once a year.

Please note that a simple aggregate of the average number of domestic and outbound trips for the two countries is approximately the same: Japan 2.8 (2.6 plus 0.2), the U.K. 2.9/2.6 (1.8 plus 1.1/0.8). The implication of this data is that the two countries travelling activity is similar, though there is a market opportunity to stimulate outbound trips by Japanese. To the extent that the relatively low outbound trip activity by Japanese people reflects relative price/cost differences e.g. the yen is a relatively weak currency (making overseas travel expensive), then it is another warning signal that inbound tourism might also be at extended levels since the same weak yen makes visiting Japan more attractive.

Observation three: Differences in definitions between countries can make cross-border comparisons difficult. Whilst the data discussed so far is likely to be highly comparable, there could be issues with the data on direct employment in tourism and the tourism industry as a proportion of the economy. In Fig.3, these numbers are all sourced from the OECD, an organization with a good reputation for ensuring compatibility of statistics across countries. The data indicates that Japan is employing considerably more people in the tourism industry than the U.K. and that the tourism industry in Japan is contributing materially less value added to overall GDP. This implies exceptionally low productivity. Given the dominance of traditional family management in the onsen industry, low productivity is not surprising, but the degree implied in the data is dramatic.

Structural issues

The selection of an appropriate benchmark should minimize current structural differences between the two countries being compared. That is now. However, to understand the historic growth rates it is important to be aware of structural changes that have occurred in the recent past. [(3)] Inbound tourism into Japan was exceptionally strong over 2013-17, Fig.2 and Fig.4-6.

Fig.4 Inbound tourism, actual by year, in millions, year on year growth

	2012	2013	2014	2015	2016	2017	2018	2019
Actual, millions	8.36	10.36	13.41	19.74	24.04	28.69	31.19	31.88
Year on Year (%)		24.0	29.4	47.1	21.8	19.3	8.7	2.2

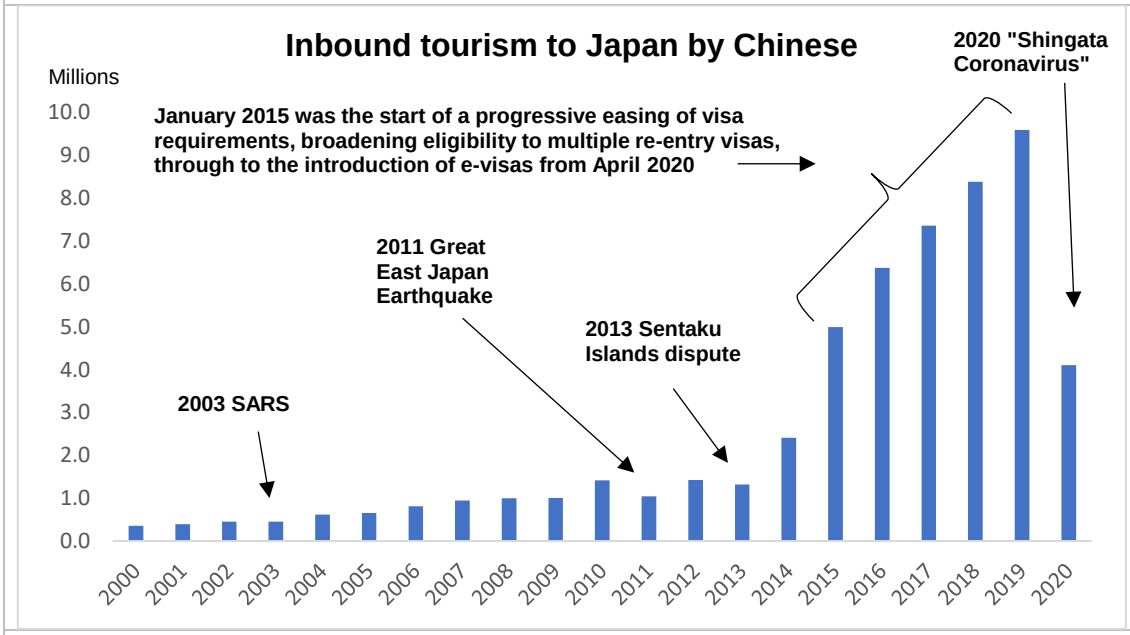
Source: JNTO, Conceptasia, April 2021

This was the period when:

- Since 2013 visa requirements for tourists from Malaysia, Thailand and China have been relaxed. From 2014 visitors from Malaysia and Thailand no longer needed visas. From 2015, Chinese with an annual income more than ¥1.9 million became eligible for 5-year multiple re-entry visas.
- Bank of Japan radical policies were reflected in the Japanese Yen depreciating substantially, from around ¥80/US$ in 2012 to ¥110/US$ or so in 2015
- An expansion of the consumption tax exemption system started from October 2014
- Large increases in ports for cruise ships, and landing spots for Low Cost Carriers (LCCs). Arrival and departure flights from Haneda and Narita (serving Tokyo) increased from 0.5 million to 0.7 million from 2010 to 2013 as Japan implemented an “open sky” policy. (4)

As Fig.5 suggests, we believe that structural impediments, such as visa rules, are much more important than natural disasters or even geo-political friction. The latter appear to have a one-year, temporary impact, the former a multi-year permanent effect. For reference, both Japan and the U.K. now have on-line application processes for Chinese tourist vias.

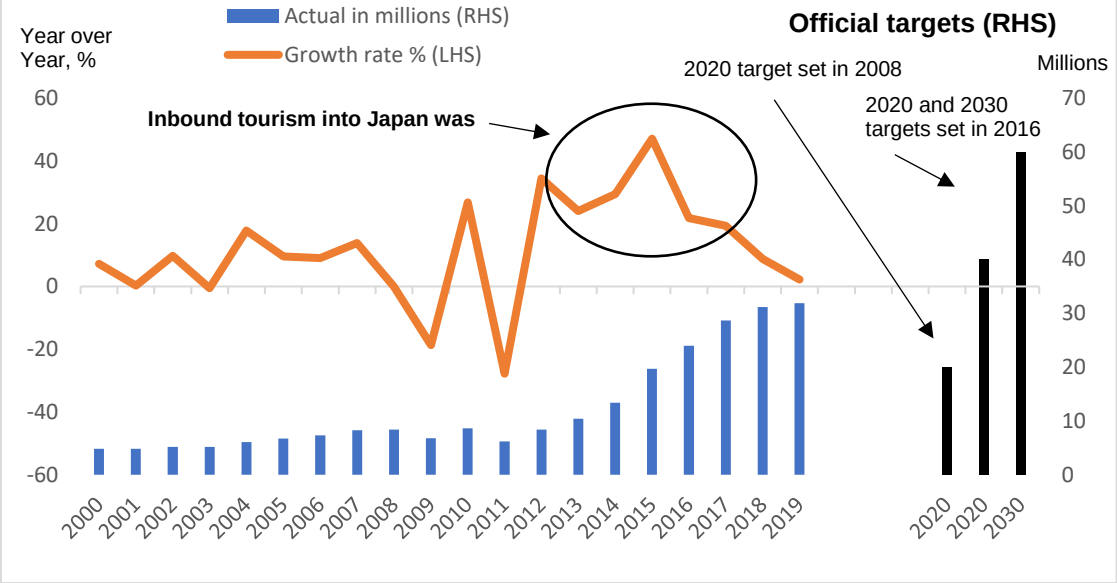
Fig.5 The impact of natural disasters, geo-political friction, and structural impediments



Note: 2020 data is January-March annualised. 2020 actual was 1.1 million.
Source: JNTO, Conceptasia, April 2021

Tourism has become a government priority sector. In 2008, the Japan Tourism Agency was established by the Japanese government and given the goal to increase foreign visitors to 20 million in 2020. In 2016, with inbound visitors set to exceed the 20 million target, Fig.4, the government increased the 2020 target to 40 million, and set a 60 million target for 2030 (as shown in Fig.6).

Fig.6 Inbound tourism, actual by year, in millions, year on year growth; Official targets



Note: 2020 inbound tourism was 4.12 million, -87.1% from the 2019 inbound total of 31.88 million

Source: JNTO, Prime Minister's Office, Conceptasia, April 2021

3) A simple model of the Japanese tourism market

Our model has two elements:

A) Domestic trips, excluding daytrips
B) Inbound tourists

Rather than adding the number of trips together, it is better to use "Guest nights" as the two components have different behaviours, e.g., staying at hotels for different lengths of time. In 2017, 323.7 million domestic trips become 429.9 million guest nights (a multiple of 1.32). In 2017, 28.7 inbound tourists become 79.7 million guest nights (a multiple of 2.78). Using guest nights also links tourism to the hospitality industry more directly.

Fig.7 Japan's Guest Nights data: Japanese, International visitors, Total

	2012	2013	2014	2015	2016	2017	2018	2019
Guest nights: Japanese (m)	413.2	432.4	428.7	438.5	423.1	429.9	420.4	NA
Year on Year (%)		+4.6	-0.9	+2.2	-3.5	+1.6	-2.2	
Guest nights: Int. visitors (m)	26.3	33.5	44.8	65.6	69.4	79.7	88.6	NA
Year on Year (%)		+27.4	+33.7	+46.4	+5.8	+14.8	+11.2	
Total guest nights (mi)	439.5	465.9	473.5	504.1	492.5	509.6	509.0	
Year on Year (%)		+6.0	+1.6	+6.5	-2.3	+3.5	-0.1	
Guest nights: % of total by Int. visitors	6.0	7.2	9.5	13.0	14.1	15.6	17.4	

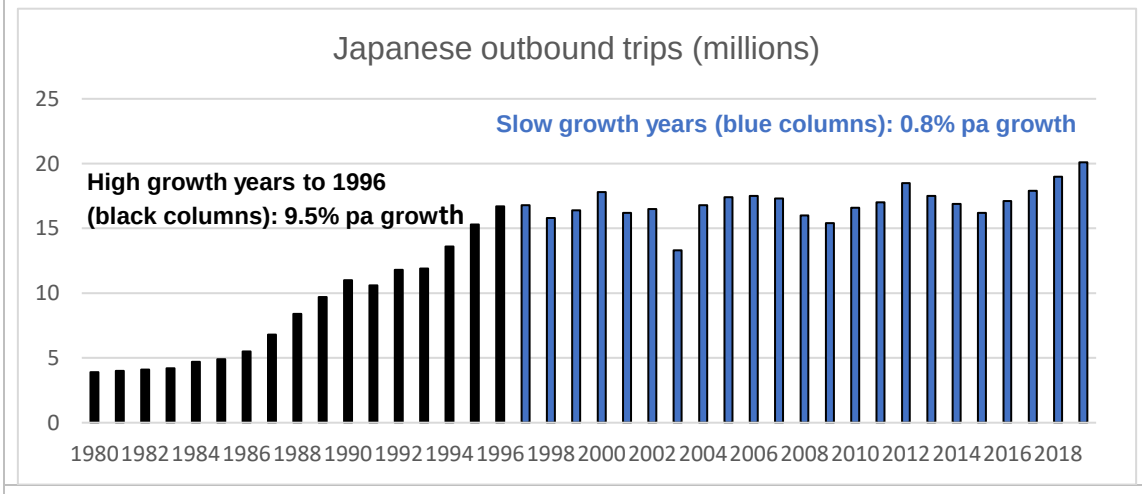
Source: JTA (Overnight Travel Statistics Survey), Conceptasia, April 2021

A) Japanese guest nights

In coming years, the total of Japanese guest nights is likely to be principally driven by demographics, i.e., the shrinking Japanese population. We assume the latter shrinks at 0.5% per year. This implies that the 420.4 million Japanese guest nights of 2018 decline to 405.9 million in 2025 and 395.9 million in 2030. All our forecasts are in Fig.9.

Models and the assumptions therein are best discussed, rather than just being accepted. For example, we should explain why we have chosen population shrinkage as the determinant rather than household income growth proxied by real GDP growth. The latter on a trend basis is probably around +0.5% per year (1% trend labour productivity growth minus the shrinkage in the work force). We believe that household income developments, trend growth and fluctuations therein with natural disasters and the business cycle, are more likely to show up in Japanese outbound trips, Fig.8.

Fig.8 Japanese Outbound Trips, 1980 to 2019, millions



Source: JNTO, Conceptasia, April 2021

Please recall from the benchmarking section discussing Japan and the U.K., that both countries had around 2.8 trips per person per year, but the U.K. had many more overseas trips within that number. A casual look at the last two decades in Fig.8 suggests both a “cyclicality” in the data, and a mild upward trend.

Japan’s outbound tourism high growth years also had assistance from the government. In 1987 the “Ten Million Program” aimed to double the number of Japanese overseas travel from the 1986 level of 5.5 million to 10 million by the end of 1991. In addition, the Plaza Accord of 22 September 1985 resulted in the Japanese yen surging higher: the ¥/US$ exchange rate was 242 at the time of the accord, 153 in 1986 and 120 by 1988. Overseas travel became dramatically cheaper in Yen terms.

B) International visitors' guest nights

In coming years, the total of International visitors' guest nights is likely to be principally driven by the rate of growth of the global tourism market, i.e., the years of premium growth have completed. The global tourism market has grown at 4.2% per year for the last 20 years, [(5)] but with the step-down in global growth, we expect annual growth to trend at 3% per year, from 2018-2030. The UNWTO (United Nations World Tourism Organization) is forecasting 3-4% annual growth. Our 3% annual forecast implies that in terms of inbound tourists, we are forecasting 38.4 million in 2025 and 44.5 million in 2030. Assuming an unchanged 2.78 multiple into guest nights, our forecasts are 106.8 million international visitor guest nights in 2025, and 123.7 million in 2030.

Fig.9 Japanese tourism market: Prospects – our forecasts

	2018	2025	2030
Guest nights: Japanese (millions)	420.4	405.9	395.9
Guest nights: International visitors (millions)	88.6	106.8	123.7
Total guest nights (millions)	509.0	512.7	519.6
Annual growth: 2025 versus 2018, 2030 versus 2025		+0.1%	+0.3%
Guest nights: % of total by International visitors	17.4	20.8	23.8
Inbound tourists	31.2	38.4	44.5
Government target			60.0

Source: JNTO, PM Office, Conceptasia, April 2021

On our forecasts, the Government's new 2020 inbound tourist target of 40 million is not reached until 2027. As shown in Fig.9, the government's 2030 target of 60 million is expected to be missed.

To the extent that the government targets are expected to be met by the industry and/or the media, our forecasts might be regarded as controversial.

However, rather than forecasts, we regard the government's targets as aspirational with the aim of motivating the respective ministries. For a discussion of the government's other inbound tourism targets, e.g., to triple the number of visitor nights in non-metropolitan areas, please see chapter nine: "Where to site a Wellness Boutique Hotel in Japan".

Some risks to our forecasts

1) We are assuming that the impact of the "Shingata coronavirus" has dissipated by 2025
2) The *2020 Tokyo Summer Olympics and Paralympic Games* to be held in 2021 assists in the recovery from the "Shingata" coronavirus shock through the "diffusion model of tourism" social media buzz, but again its effect has dissipated by 2025
3) We have assumed that there is no material backlash against the global tourism industry resulting from its carbon emissions [(6)]

References

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