THE INTERNATIONAL SOCIETY OF HOSPITALITY CONSULTANTS (ISHC)[1] ANNOUNCES THE TOP TEN GLOBAL ISSUES & CHALLENGES IN THE HOSPITALITY INDUSTRY FOR 2006

At the recent ISHC Annual Conference held in San Diego, California, ISHC Members participated in a series of roundtable discussions to identify the ISHC Top Ten Global Issues and Challenges in the Hospitality Industry for 2006.

While there were many issues discussed, in the final voting the membership identified the following top ten issues as the ones that can be expected to potentially have the greatest impact on the industry in 2006.

ISHC Top Ten Global Issues & Challenges for 2006

1. Changing Labor Conditions
2. Escalating Operating Costs
3. Impact of Rising Energy Costs on Consumer Travel & Hotel Demand
4. Escalating Renovation and Construction Costs
5. Havoc from Recent Natural Disasters
6. Growing Global Uncertainly About Safety and Security
7. Evolving Customer Expectations
8. Condo-hotels Growing Rapidly
9. Accelerating Change and Merging of Technologies
10. Increasing Consolidation of Hotel Brands/Companies

1. Changing Labor Conditions

The hospitality industry faces labor and human resource challenges including the compression or shrinking of the labor force, union issues and escalating health care and benefit costs among others.

Compression of Labor force - the traditional labor force is shrinking as a result of changing demographics. Slowing population growth rates, an aging population, and fewer persons in the working-age group, have all contributed to the shrinking labor supply.

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Unionization issues: The growth in both unions and interest among employees in unions has increasingly posed challenges to hospitality related operations. Furthermore, union contracts will be expiring in New York, Chicago, Boston and many major cities in 2006, and as a result may potentially disrupt hospitality operations.

Increasing health care costs and other benefits: Significant increases in benefit costs are making it more expensive for employers to hire and retain employees, thus hospitality companies are forced to be more selective in their hiring process.

Immigration issues and temporary work visas: Since the events of September 11th, the United States has become more stringent on immigration and the issuing of work visas, thus decreasing the overall foreign workforce. As many hospitality organizations in the United States rely heavily on foreign employees to fill entry-level positions, hospitality organizations must rely more on alternate sources of employment.

2. Escalating Operating Costs

There is concern that operating expenses will escalate at a greater rate than income, potentially eroding the bottom line. Operators need to monitor the following:

Energy Costs: Global increases in demand and the natural disasters in the Gulf States have stretched energy supplies. Prices increased in 2005 and the forecast is for higher prices in 2006. Energy management/conservation programs and employee awareness are essential to mitigate exposure to dramatically escalating energy costs.

Higher insurance costs: The costs of claims in the Gulf States will translate into higher insurance premiums as well as possible changes in deductibles and/or coverage limits for users. For some, the ability to participate in larger pools, such as chain operations, may soften the blow.

Labor costs and labor shortages: There are national movements to enact living wage ordinances and some major unions are determined to tie together the labor contracts of the top U.S. convention cities in an attempt to strengthen their position at the negotiating table. These potential cost increases come at a time when the industry at large is having difficulty attracting employees. The silver lining is that probable higher wages will result in a larger and more competitive labor pool.

Brand standards: Many brands are changing brand standards, and "raising the bar" via increased services and/or amenities in an attempt to gain a competitive edge in the marketplace which has resulted in increases in operating costs for many hotels.

3. Impact of Rising Energy Costs on Consumer Travel & Hotel Demand

A decline in all types of consumer travel may be possible as higher energy costs take a bigger bite out of personal and corporate budgets, with travel expenditures typically one of the first discretionary items to be reduced or eliminated.

On a positive note, energy's continuing threat to the industry will undoubtedly force industry execs to be more creative, or at least more conservative, in its use and consumption. Participants at all industry levels will need to be more efficient with limited/dwindling supplies, and/or find alternative ways of delivering similar service to their guests without impacting their quality of stay. "Greening" of hotel operations may actually become the norm as opposed to a discretionary program as both consumers and hotels of necessity become more focused on energy conservation.

4. Escalating Renovation and Construction Costs

Increases in renovation and construction costs are resulting in escalating capital reinvestment exposure for many existing hotels and increased capital requirements for new construction.

Existing Hotels: Many branded companies are increasingly demanding improvements and upgrades in the physical condition of hotels and more stringent adherence to brand standards to remain competitive, resulting in escalating capital reinvestment exposure for their hotels.

New Construction: With improved market conditions, developers continue to look for additional opportunities to build hotels. Yet higher costs for construction will be one mitigating factor to new development. There are several factors that will impact the financial feasibility of new construction including: 1) rapid escalation in the price of building materials; 2) higher energy costs and 3) rising interest costs. Most major hotel brands are taking a hard line on improving brand standards and are requiring more costly hotel furnishings and materials. As a result, the cost to build hotels is expected to increase at a pace that is greater then anticipated revenue increases.

The good news is that as higher costs hamper new development, the existing inventory of hotels can benefit by limiting new supply.

5. Havoc from Recent Natural Disasters

Whether a long-term trend from global warming or part of a long-term cycle, natural disasters appear to have become more frequent in recent years. The implications are profound, especially since many affected areas are heavily reliant on tourism for economic vitality. The potential threat of avian flu could have much broader impact than SARS had. New virus strains and other diseases resistant to antibiotics may be on the horizon. Travelers are increasingly choosing destinations in part on the perceived level of risk. Some locations will be winners, while others may need to diversify their economies to supplement tourism.

A secondary effect is the post-event consequences of natural disasters. Some destinations will not be able to accommodate travelers for years to come. Resources that go into rebuilding local infrastructure drain funds that might otherwise go toward economic growth. Even non-impacted locations may not be able to expand as construction resources are focused on those areas in need. It is clear that economic challenges of the future may be structurally different from those of the past.

6. Growing Global Uncertainly About Safety and Security

There is broad concern among travelers about protecting their own safety. These concerns range from the healthfulness of airplane ventilation to vulnerability to terrorism. Governments are increasingly trying to manage risks, sometimes impacting a country's tourism infrastructure, such as when restrictive visitation policies are enacted. The ongoing turmoil in the Middle East, the coordinated bus bombings in London, and various other events around the world has caused travelers to rethink traditional assumptions regarding leisure travel. Some remote and non-traditional destinations may find tourism increasing as a result of those places having the right mix of attributes currently in demand by tourists.

7. Evolving Customer Expectations

The ability to satisfy and anticipate evolving customer needs continues to be a significant priority. Specifically, customers are increasingly sophisticated in their use of technology
to research, select and purchase lodging. Furthermore, customers are resisting a "chain mentality" and there is true opportunity in creating unique and customized experiences, while minding the "bottom line". As a result, marketing approaches will need to be adapted and updated to effectively reach the customer. In addition, true differentiation is increasingly difficult to achieve in the luxury market as it has become "mainstream".

8. Condo-hotels Growing Rapidly

The recent surge in condo-hotels and alternative ownership has brought on a whole new set of risks and challenges for developers, lenders, unit owners and management.

Alternative ownership has presented opportunities for developers, in particular by substantially reducing their financial exposure in developing projects. There are, however, looming issues--from developer representations in connection with the sale of units to product/unit warranties and/or latent defects--- that represent potential liability and exposure for developers down the road. From the customer perspective it remains to be seen whether individual unit owner expectations will be met over time.

The management of condominium hotels has traditionally been extremely challenging. Managing volatile inventory, maintaining and renovating individual condo units, compliance with "owner use" policies and procedures among other issues will present challenges going forward.

9. Accelerating Change and Merging of Technologies

Hospitality systems and their interfaces are rapidly moving to Internet-based technology, which allows dramatically easier and more flexible integration and hence more complete guest/operational data. Many hotel operators are moving to take full advantage of this opportunity to streamline their operations, but adoption is frequently hampered by older systems and outdated infrastructure. The investment required to upgrade is significant, but the full benefits of this change cannot be realized without it.

This highlights the industry's continuing need for education, both of management companies in how to recognize and quantify the business benefits of properly integrated technology, and of the end users in using their systems most efficiently. Most current systems are under-utilized, a situation not helped by the industry's reluctance to invest in regular refresher training for the users. Full optimization of the operation requires effective systems integration and adoption of the new technology.

10. Increasing Consolidation of Hotel Brands / Companies

As brands consolidate and proliferate in their market reach owners are finding it more difficult to select a brand that is not already represented in their marketplace or one that is not influenced by territorial encroachment issues. As this trend evolves owners and management companies are finding a shift in the negotiation power toward the brands that may impact deal structures. Major brand companies continue to isolate consumer segments and strengthen and/or create specific brand niches to address micro-markets while at the same time making it more difficult for the consumer to truly understand the 'inter' and 'intra' brand difference. What makes sense to the hotel developer or the brand becomes confusing to the customer thus impacting both consumer pricing and commoditizing hotel products. Public hotel companies in search of shareholder value are poised to create conditions for additional consolidation, not unlike the online world where 90% of online hotel inventory is managed by only a handful of companies.