

Productivity and Tourism

Final Report

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SQW

Contents

Executive Summary	i
1. Introduction	1
2. What is productivity	3
3. Overview of the sector	7
4. Productivity in tourism and hospitality	12
5. Sector views	25
6. Overview of current interventions.....	32
7. Conclusions.....	35

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Contact: Bruce Macdonald Tel: 01312430721 email: bmacdonald@sqw.co.uk

Approved by: Bruce Macdonald Date: 20/11/15
Director

Executive Summary

Productivity

1. Productivity is one of the main measures of economic performance for the UK and Scottish economies generally, as well as for specific sectors. At a national level, policy makers have struggled to understand why productivity has failed to grow over the past few years (the productivity puzzle).
2. Raising output per worker provides the basis for greater profits and higher wages, both of which are also attractive for investment. Productivity growth is therefore a key determinant of economic growth. The incomes and living standards enjoyed by people living in an economy are strongly determined by the volume of goods and services that they produce. In hospitality and tourism businesses, labour productivity is low relative to many other sectors, but broadly comparable with other labour intensive service activities such as cleaning, retail and care.
3. At a UK level, GVA in accommodation and food and drink services has grown but so too has employment. The ONS's productivity data, which uses GVA per hour rather than per employee, indicates that labour productivity in the sector has not improved significantly in real terms over the last 20 years.
4. Labour productivity will always be lower than many other services and manufacturing because it is inherently a "people" business. There are fewer opportunities to mechanise or automate the work, and even then, doing so could have a negative impact on attracting visitors and on the diversity of the hospitality and tourism product that Scotland offers.
5. However, the sheer size of the sector and the number of people employed means that even relatively small improvements in productivity would represent significant gains for the economy. The issue is not so much the level of productivity, but that improvement would help raise profits and wages, making the sector as a whole more attractive to work and invest in. And this is fundamental to a sustainable tourism sector.

Overview

6. In Scotland GVA per worker was £16,832 in 2013 compared with £45,752 in food and drink, £59,596 in Life Sciences and £58,968 in Creative industries in the same year. However GVA per worker in the tourism sector has grown from £13,974 in 2008 (20%). Part of the reason for the lower value is that there are a larger number of part-time workers. Adjusting for this (GVA per *full time worker*) would increase the value by around 20%.
7. Accommodation and food and drink services are by far the largest elements of the hospitality and tourism sector. Productivity in accommodation is higher and has risen faster than in food and drink services, while in some of the visitor attractions, such as museums and gardens, productivity is lower, although the figures are less reliable given the smaller numbers and difficulties of measuring GVA within the non-market sub-sectors.
8. Productivity in the core parts of the tourism and hospitality sector in Scotland is similar to the rest of the UK, outside London. Compared with other EU countries, productivity in the UK is

similar to Germany and the Netherlands but well behind France, Denmark, Norway, Belgium and Austria. It is striking that turnover per employee in these countries is considerably higher than in the UK, as are wage costs. Within Scotland, there are large differences in productivity across local authorities, although care should be taken as sample sizes are likely to be small. Aberdeen City and Shire, Edinburgh, Stirling and Perth have higher levels of GVA per head than Highland, Dumfries and Galloway or Glasgow. It doesn't appear to closely follow the pattern of visitor numbers.

9. We would expect the size of a business to have an effect on productivity. Economies of scale usually mean that larger businesses will have higher levels of productivity. There will be a stronger incentive (and resources) to invest and train. The analysis found no labour productivity improvement between businesses with employment of 5 to 9 and the group with 10 to 19, across all three subsectors, and that size had little effect on productivity within restaurants and food service businesses.
10. Finally, the report emphasises that these indicators reflect the entire output of the accommodation, food and drink and beverage service sub-sectors and that in many cases the majority of this is not related to tourism. Only around 30% of food and beverage sales are made to tourists while 70% is made to local residents. The expenditure of tourists and the influence of tourism is therefore only a part of the picture.

Influences

11. The main influences on productivity are:
 - **volume of sales** - attracting more customers and increasing sales makes better use of the capacity
 - **leadership and management** - good leadership and management will recruit and retain the right staff, introduce new ideas and systems, invest in improving assets and use ICT tools to make the most efficient use of resources.
 - **balance of skills** - tends to be towards customer service with less emphasis on understanding productivity and delivering services more efficiently
 - **increasing and improving the use of technology/innovation** - focus more on reducing costs of suppliers, staff rostering, use of point of sale information, calculating margins etc.
 - **Investment** - it has become more difficult for businesses to access finance and fund investments that could help improve facilities and productivity.
12. There is no doubt that the overall productivity data hides a broad spectrum of performance. The sector lends itself to "lifestyle" businesses, where the owners are perhaps less worried about maximising productivity and profit. Combined with the seasonal challenges of the sector and the fact that it supports jobs in many rural and remote areas, it is perhaps not surprising that there is such a wide range of productivity.
13. The Living Wage will come into force in April 2016 and will have an immediate impact on the wage bills of many businesses in the sector, large and small. Although, in theory, wages are part of the valued added the business generates, and therefore it should be a redistribution of

the surplus, it will also have indirect effects on the incentives for business owners and managers. In some cases it could reduce re-investment and impact on productivity if for example, rooms are not refurbished, marketing curtailed or less investment in ICT. Alternatively, if the costs are passed on through higher prices it may have some impact on demand.

14. Alternatively it was argued that paying higher wages could generate more commitment from staff and help retain them; higher wages would help focus businesses on how they deploy staff, providing a greater incentive to reduce excess capacity where possible. It would be expected that an increase in the cost of labour would encourage investment to save labour. In practice, its impact will vary from business to business, but it certainly raises the importance of improving productivity and a bigger role for the agencies that support the sector.
15. The report also provides specific examples of actions to improve productivity. These include:
 - making more use of the experience of longer term staff
 - using IT to monitor demand and plan rotas more effectively
 - using changes in wages to redesign jobs to minimise downtime
 - identifying times or areas of business that are underutilised
 - using feedback to focus on what customers want
 - identifying opportunities to work as part of the “destination”
 - using benchmarks to better manage margins and analyse performance
 - encouraging staff to look for ways to work more productively.

Conclusions

16. With increasing pressure on wages, productivity is set to become more important to businesses. It is an opportunity to focus more on how it can be improved. The size of the industry, means that even small improvements would generate improvements in profits and wages, making the sector more sustainable.
17. **Overall, the paper concludes that productivity in general should be higher up the agenda of businesses and supporting agencies in the sector. While the focus on the customer journey and service is essential, there should be greater attention paid to operational efficiency.**
18. Of all the areas related to productivity, the main theme was in developing leadership and management skills. This is the basis for influencing many of the other factors that determine productivity.
19. In addition to actions designed to grow markets, activity to support productivity should focus on the following three areas:
 - **leadership and management skills**
 - **better/more use of ICT**

- **better/more use of data and analysis.**
20. The analysis by business size suggests that this should be focussed on smaller businesses, for example with around 10 to 20 employees.
 21. Case study examples that show where these actions have worked, and demonstrate financial benefits for businesses and staff would also help generate interest.

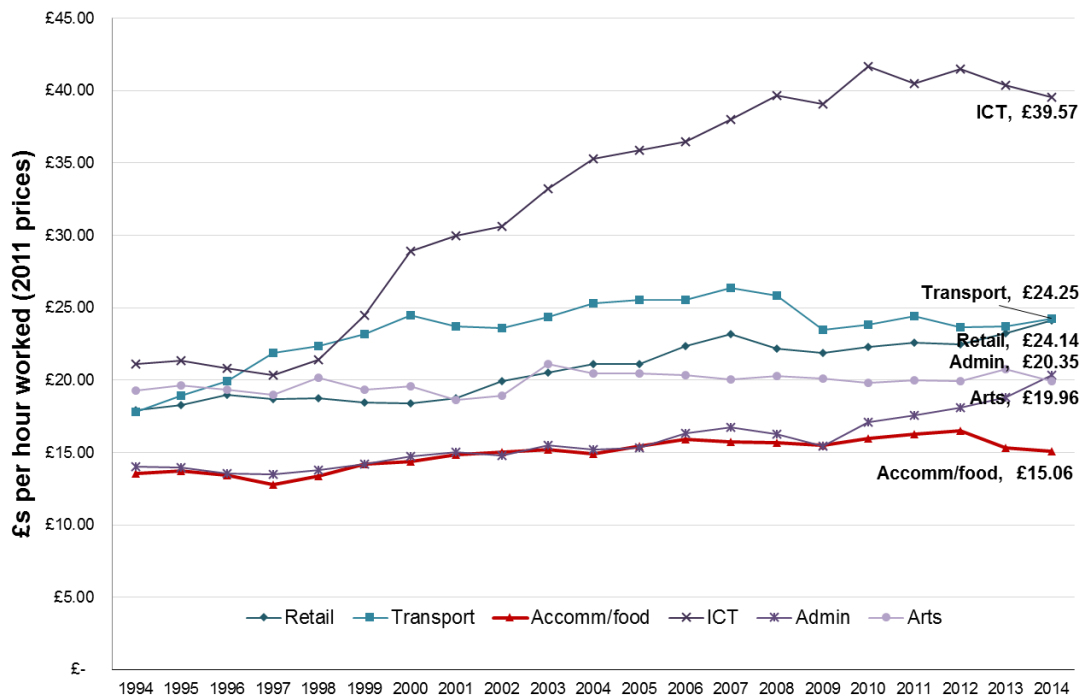
1. Introduction

- 1.1 Productivity has become an increasingly important topic over the last couple of years. In part because of UK data that shows that while economic growth (GDP) has been increasing, the output per worker has not. However, the interest in productivity has also highlighted the significant differences in performance between sectors both relatively and in absolute terms. For many reasons, tourism and hospitality businesses often have relatively low output per worker. The sector's reliance on "people" means that issues around skills and how staff are deployed as well as investment and innovation are often cited as impacting on levels of productivity. This report examines some of these issues and also presents some business views on the current position and areas where improvements can be made.

Context

- 1.1 Productivity is increasingly seen as one of the main measures of economic performance for the UK and Scottish economies generally, as well as for specific sectors. At a national level, policy makers have struggled to understand why productivity has failed to grow over the past few years (the productivity puzzle), and this has led to a greater focus on measures to improve it.
- 1.2 Productivity in all sectors is important for business owners and for workers. Higher output per worker provides the basis for greater profits and higher wages, both of which are also attractive for investment. Productivity growth is therefore a key determinant of economic growth and living standards. The incomes and living standards enjoyed by people living in an economy are strongly determined by the volume of goods and services that they produce. As the Nobel prize-winning economist Paul Krugman has said:
- Productivity isn't everything, but in the long run it is almost everything. A country's ability to improve its standard of living over time depends almost entirely on its ability to raise output per worker.*
- 1.3 Productivity, as measured by output per worker, in the tourism and hospitality sector has historically been much lower than most other sectors. This is because so many of the services that it provides depend on people, with fewer opportunities for mechanisation. The sector also faces in challenges in managing seasonality, high turnover of staff, access to finance, as well as growing or even just maintaining demand. The increases in the minimum/living wage next April have also focused attention on productivity.
- 1.4 It is therefore important to understand what productivity is, how it can be influenced and potentially, what can be done to improve it.
- 1.5 At the core of the issue are two elements. Why is labour productivity low relative to other sectors and, secondly, why has it remained at roughly the same level for the last 20 years. Figure 1-1 shows the pattern of output per hour worked in the UK for a number of sectors. While it is true that none have recovered significantly since the financial crisis that started in 2008, in the last few years, output per hour in accommodation and food has diverged further from retail, administration and arts employment.

Figure 1-1: Output per hour worked (UK £s per hour worked)



Source: ONS Labour productivity data 2014 - <http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcm%3A77-393176>

2. What is productivity

- 2.1 Productivity growth is important because it is a key determinant of economic growth and therefore living standards. Growing productivity means producing, on average, an increasing amount of value per person employed. This increase can represent more profit for businesses, resources for further investment and increases in wages for workers.
- 2.2 Productivity describes the relationship between the inputs to the production process, such as labour, capital and materials, and outputs such as goods and services. It is most simply defined as the ratio between output and input.

$$Productivity = \frac{Output}{Input}$$

- 2.3 In other words, productivity describes the efficiency with which inputs such as labour, capital and materials are used to create the output of goods and services. The most common, and best understood measure of productivity is labour productivity, or the value added per worker, although there are others. Total Factor Productivity, for example is the portion of output not explained by the amount of inputs used in production. Its level is determined by how efficiently and intensively all inputs are utilized in production. However measuring this is more complicated and the results are harder to explain.
- 2.4 Productivity means different things to different people. The public sector, or society generally is interested in the total value that is added by business activity. This includes the share that is retained as profit, as well as the wages and salaries that represent income for employees. This is what is “added” to the economy generally.
- 2.5 For a private business, wages and salaries are considered to be a cost, and the main focus is on the surplus (over and above all costs) that allows profits to be made and re-investment in the business. All things being equal, an increase in wages therefore reduces the resources available for re-investment and profit – although the value added remains the same. Although higher wages do not in themselves impact directly on value added, they could do if they impact on levels of investment, or retain or attract more skilled labour.
- 2.6 Output is usually defined as Gross Value Added (GVA)¹ which is the value of goods sold (or turnover) minus the “intermediate” inputs that have been bought in. For example in food services it is the “added value” that a business creates by assembling or processing the ingredients and selling them to a customer. The business is selling the food for more than the sum of the raw materials. This is the value that it “adds”. Although this is the standard measure of productivity, it is not an indicator that businesses would use.
- 2.7 An alternative would be to measure output as turnover or sales, Sales per worker (or per hour worked) or even sales per £ spent on labour costs. These ratios though are only really useful for comparisons *within* a sector, but not in comparing across sectors, where some businesses have high turnovers (but also high input costs) and low margins. This would skew productivity comparisons. In contrast, GVA reflects what the businesses and workforce are

¹ Gross Value Added (GVA) is a measure of the income generated by businesses within their industries and sectors, less the cost of goods and services used to create the income.

creating or contributing to the national economy and can be compared across all sectors. Using wages as the denominator instead of labour time also causes problems in measuring economic contribution as the ratio would improve where wages are reduced.

- 2.8 GVA statistics are produced for the UK by the Office of National Statistics (ONS) for sectors and regions. In Scotland, the Scottish Government reproduce this data as part of the Scottish Annual Business Survey and this is used to compile the Growth Sector database.
- 2.9 There are several measures of labour input that can be used. The choice often depends on the data that are available. Table 2-1 summarises the strengths and weaknesses of different labour productivity measures.

Table 2-1: Comparison of labour productivity measures

	Strengths	Weaknesses
Output per hour worked	Provides the greatest precision about the amount of labour that has been used.	Per hour worked data can often be of low quality or not available.
Output per worker	The number of workers available is the ultimate constraint on volumes of labour.	Does not account for the difference between full- and part-time labour.
Output per job	Benefits from a greater availability of detailed industry information.	Does not account for the fact that one worker can hold multiple jobs.

Source: ONS Productivity Handbook

Business and public sector perceptions

- 2.10 There is an important distinction to make at the outset between **productivity** and **profitability**. Profitability reflects the ability of a business to generate income relative to all its costs, including labour, whereas productivity describes the volume of output relative to the volume of inputs². For a firm that is seeking to maximise its profits, **productivity may be only one of a whole range of considerations in its decision making process.**
- 2.11 GVA represents the total value added and how this is then distributed between owners, shareholders, employees or reinvested, is then a separate issue. However, all can agree that increasing the value of output per worker is good for everyone (increasing the size of the cake).

What determines productivity?

- 1.6 Research³ shows that many factors influence productivity. The main ones are:
- a. **Investment** - relates to **investment in physical capital** such as equipment and buildings which can be used to improve the production process. Generally speaking, the more capital workers have at their disposal, the easier they will find it to produce more and better quality output. It would include *IT such as booking systems or CRM systems, investment in buildings, improvements, equipment as well as access to finance in order to fund investment. Studies find that this type of investment is improves*

² Australian Government, *Demystifying Productivity*, 2013

³ Syverson, Chad (2011), *What Determines Productivity?*, Journal of Economic Literature, 49:2, 326-365, Office for National Statistics (2007), *Productivity Handbook*, pg. 20

productivity - Syverson⁴ (2011) documents **productivity growth in IT-using industries**.

- b. **Innovation** - is broadly defined as the successful exploitation of new ideas. *Successful exploitation of new ideas can be in the form of new technologies, new products, new structures and processes that can reduce costs, such as ovens, laundry systems, point of sale systems, rostering, equipment etc.*
- c. **Skills** – complement physical capital and help firms take advantage of new technologies and organisational structures. Skills levels describe the **quantity and quality of labour of different types available** in a firm, industry or economy. *The quantity and quality of labour of different types. This covers both the importance of leadership and management skills, as well as basic staff skills. It can include recruitment and retention, training, skills and wages*
- d. **Competition and enterprise** – theoretically, competition *can move market share towards more efficient businesses, shrinking relatively less efficient firms and opening up room for better performing businesses. Heightened competition can induce firms to invest in productivity raising actions that they may otherwise not do. However, it would also appear that competition that drives down income can limit access to the resources needed for investment.* Foster et al⁵ (2006) find that aggregate productivity growth in the U.S. retail sector is almost exclusively through the exit of less efficient single-store firms and by their replacement with more efficient national chain store affiliates.
- e. **Managerial practice** - managers coordinate the application of labour, capital and intermediate inputs, however poor management can lead to disorganised production operations. *Better management will improve organisation of labour and equipment, systems, motivation and retention of staff and marketing.* Bloom and Van Reenen⁶ (2007) show that higher quality management practices are correlated with higher measure of productivity. They show that two factors are important predictors of the quality of management in a firm – more **intense competition in the firm's market is positively correlated with best-practice management**, and **management practice scores are lower when the firm is family-owned**. Bertrand and Schoar⁷ (2003) find that **managers with MBAs have significantly higher return on assets**.
- f. **Regulation** can have *positive and negative impacts on productivity. Environmental regulations, health and safety, quality grading are all examples of standards that hospitality businesses must adhere to. They impose costs, but in some cases can also help increase demands. Hospitality businesses have a responsibility to provide a safe environment for guests and regulations provide customers with confidence. The new living wage will also have an impact, potentially reducing resources for investment, but also encouraging more focus on deploying staff.* In simple economic terms intervention in the market by regulation can inhibit competition and add costs which reduce

⁴ Syverson, Chad, 2011, "What Determines Productivity?" Journal of Economic Literature, 49:2, 326-365.

⁵ Foster, Lucia, John Haltiwanger, and C. J. Krizan. 2006. "Market Selection, Reallocation, and Restructuring in the U.S. Retail Trade Sector in the 1990s." Review of Economics and Statistics, 88(4): 748-58

⁶ Bloom, Nicholas, and John Van Reenen. 2007. "Measuring and Explaining Management Practices across Firms and Countries." Quarterly Journal of Economics, 122(4): 1351-1408.

⁷ Bertrand, Marianne, and Antoinette Schoar. 2003. "Managing with Style: The Effect of Managers on Firm Policies." Quarterly Journal of Economics, 118(4): 1169-1208.

productivity. Greenstone et al⁸ (2011) show how environmental regulations reduce manufacturing firms' productivity levels. However, regulation could also encourage appropriate investment for the longer term (in tourism regulations on food standards or fire safety make a place more attractive to visit).

- g. **Ownership** *Scottish owned versus foreign owned – there is evidence that foreign owned businesses are more productive in many industries. They operate internationally because they have higher productivity models as well as resources for investment, scale benefits and can be the source of new ideas.* Bloom and Van Reenen⁹ (2007) show that ***U.S. based international firms operating in the EU are more productive than their EU counterparts, and this productivity advantage is primarily derived from IT capital.***

⁸ Greenstone, Michael, John A. List, and Chad Syverson. 2011, "The Effects of Environmental Rights on US Manufacturing Productivity". Unpublished.

⁹ Bloom, Nicholas, and John Van Reenen. 2007. "Measuring and Explaining Management Practices across Firms and Countries." *Quarterly Journal of Economics*, 122(4): 1351–1408.

3. Overview of the sector

- 3.1 Businesses that work in tourism and hospitality are typically labour intensive. It is frequently described as a “people” business with less opportunity for investment in mechanisation than, say manufacturing. Often it involves working with perishable products (food) and has to deal with shifts in demand over the year (seasonality) or even through the day. For example mealtimes, or evenings, where it may not be possible to reduce the number of workers for short periods. As a result it is often necessary to have capacity in order to cope with busier times.
- 3.2 Businesses also tend to need a core staff, which is an overhead, regardless of how busy they are, and this means that labour productivity is highly dependent on the level of sales. A pub may have three staff working each evening regardless of whether 10 or 100 customers visit. Their productivity can vary dramatically depending on how busy they are.

What is included in the sector

- 3.3 There are different definitions of the tourism and hospitality sectors can vary. For Scotland we have adopted the sustainable tourism definition used by the Scottish Government in its Growth Sector data. Although it includes a relatively long list of sub-sectors identified using SIC codes (Table 3-1). In fact, 80% of activity is in three categories; restaurants and mobile food service activities, hotels and similar accommodation and pubs and bars. Sustainable tourism under this definition supports 213,000 jobs and generates GVA of £3,240 million.

Table 3-1: Composition of Employment in Sustainable Tourism by subsector in Scotland

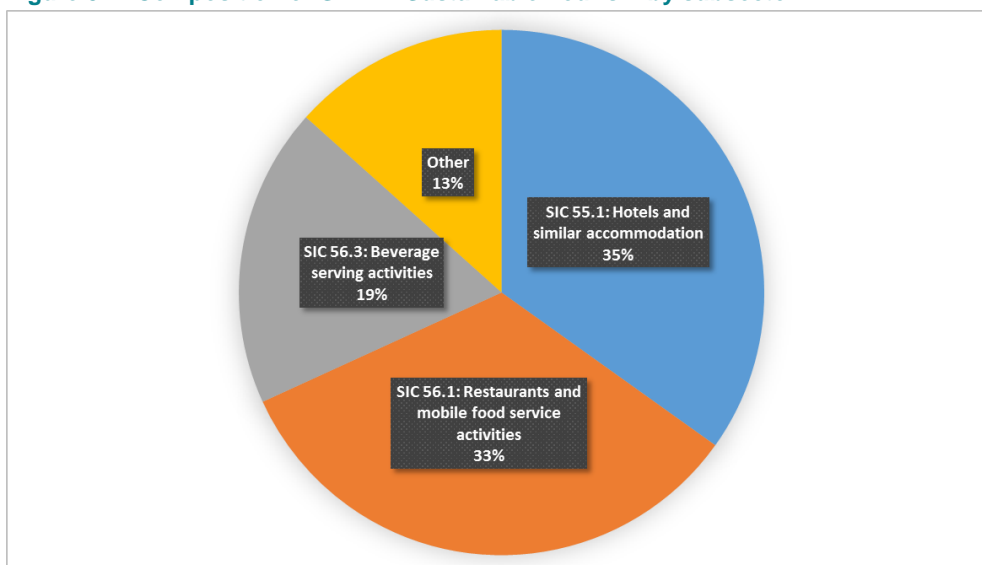
Sustainable Tourism definition by SIC code	Employment	% of total
SIC 56.1: Restaurants and mobile food service activities	84,400	40%
SIC 55.1: Hotels and similar accommodation	53,600	25%
SIC 56.3: Beverage serving activities	32,600	15%
SIC 93.11: Operation of sports facilities	13,600	6%
SIC 91.02: Museum activities	4,400	2%
SIC 93.199: Other sports activities (not activities of racehorse owners)	4,100	2%
SIC 55.2: Holiday and other short-stay accommodation	3,400	2%
SIC 55.3: Camping grounds, recreational vehicle parks and trailer parks	2,500	2%
SIC 91.03: Operation of historical sites/buildings/similar visitor attractions	2,400	1%
SIC 91.04: Botanical and zoological gardens and nature reserve activities	2,000	1%
SIC 79.9: Other reservation service and related activities	1,700	1%
SIC 79.12: Tour operator activities	1,000	1%
SIC 93.21 Activities of amusement parks and theme parks	800	0%

Source: Scottish Government Growth Sector database (accessed August 2015)

- 3.4 The composition of the sector is slightly different when analysed using GVA (Figure 3-1). This shows 35% of GVA generated by hotels and similar accommodation, 33% from restaurants and food service and 19% from pubs and bars.

- 3.5 These three subsectors; accommodation and food and beverage services dominate activity representing over 80% of the sustainable tourism sector and are therefore play a disproportionate role in the productivity estimates for the sector as a whole.

Figure 3-1: Composition of GVA in Sustainable Tourism by subsector



Source: Scottish Government Growth Sector Database 2012 data (accessed August 2015)

- 3.6 It means that 80% of the figures for the “sustainable tourism” sector are made up of the activities of businesses in these three sectors.
- 3.7 A further issue for the “tourism” sector is that the businesses that are categorised within the definition of the tourism sector do not just cater for tourists, but also for local residents. In fact in some places businesses such as bars and restaurants will not cater for tourists at all, although they are included as tourism sector businesses. The productivity figures that are reported are largely for hospitality sectors, rather than related to tourists.

How much of this activity is actually supported by tourists?

- 3.8 The sector analysis refers to *tourism*, but in practice tourism only makes a proportion of the output of these sectors. For example, food and beverage services are used by the entire population not just tourists. ONS has produced a Tourism Satellite Account (TSA) analysis for the UK. The UK-TSA sets out the contribution that tourism makes to the economy of the UK as a whole and to individual “tourism industries” in particular. Such industries invariably serve tourists and non-tourists alike and the UK-TSA includes a series of “Tourism Ratios” which estimate the proportions of products supplied in the UK.
- 3.9 The analysis uses the internationally adopted definition of tourism (used by ONS Tourism Intelligence Unit). The two main areas of interest for the Scottish definition are in accommodation and food and beverage services. Of these, less than 30% of the value of food and beverage services supplied is “tourism” consumption. This includes excursions and day trips. Therefore 70% of the output of this sector is not from tourists, but serving local demand.
- 3.10 Table 3-2 shows the proportion of output from each sub-sector that is generated by tourists. It highlights the problem that while these sub-sectors are included in the definition of the tourism sector, in practice they are only partially dependent on it.

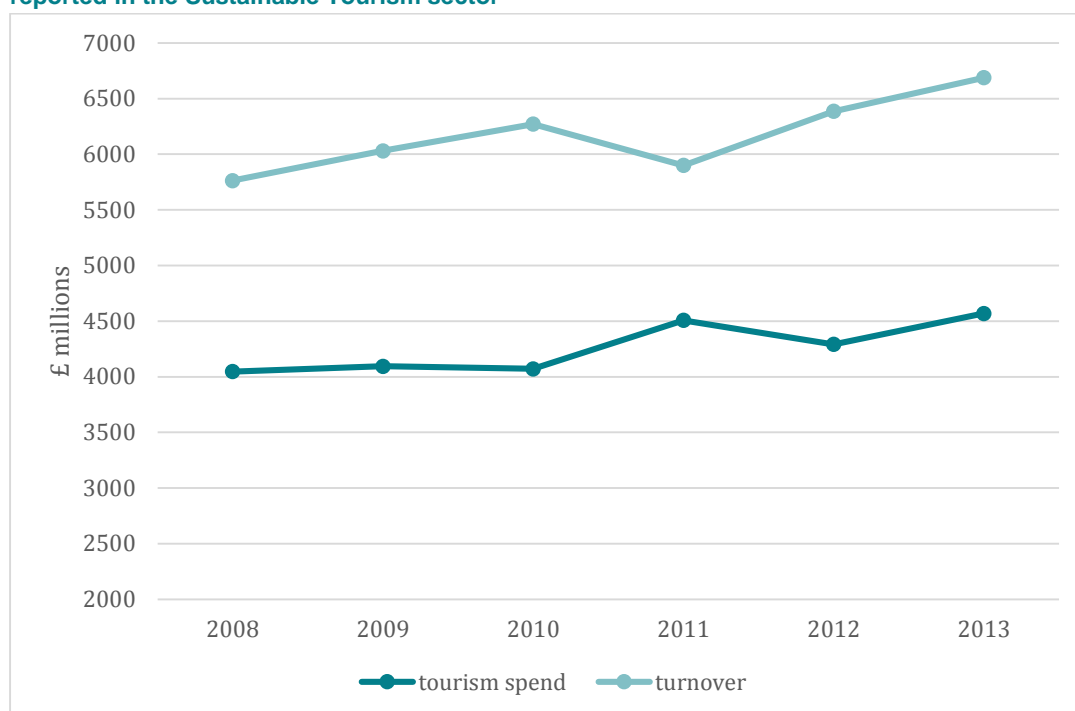
Table 3-2: Total domestic supply and internal tourism consumption (at purchasers' prices) (£m) 2012

Sub-sectors	Tourism ratios
Accommodation services for visitors	66.1%
Food and beverage serving services	27.9%
Railway passenger transport services	50.9%
Road passenger transport services	33.5%
Water passenger transport services	17.9%
Air passenger transport services	70.4%
Transport equipment rental services	4.4%
Cultural activities	26.4%
Sport and recreation activities	22.1%

Source: Office for National Statistics, Tourism Satellite Accounts (June 2015)

- 3.11 Finally, it is also useful to understand the relationship between the reported value of tourist expenditure alongside the estimates of turnover presented for the Sustainable Tourism Growth Sector. As expected Figure 3-2 shows that the turnover of the sector is higher than total tourist expenditure, but there does not appear to be a strong correlation. While turnover rises to 2010, visitor expenditure is flat, but when tourist expenditure rises in 2011, turnover in the sector falls.
- 3.12 It highlights the difference between the performance of Sustainable Tourism sector and the estimates of tourist activity produced by the GBTS and IPS surveys. It is surprising that the growth in tourism expenditure (as in 2011) does not appear to be reflected in higher sales in the Sustainable Tourism sector.
- 3.13 The main point is that the definition used to measure the productivity of the tourism sector includes a lot of activity that is not related to tourism. It also means that improvements to productivity among tourism businesses would only have a small effect on the statistics for the Sustainable Tourism sector.

Figure 3-2: Comparing tourism expenditure in Scotland (GBTS and IPS) with the turnover reported in the Sustainable Tourism sector



Wider effects

- 3.14 The tourism and hospitality sector is also important in how it supports other economic activity. The most obvious example is in the provision of meeting space, accommodation and other facilities for businesses. Large conference centres are critical in supporting sectors such as Offshore Europe in Aberdeen. There are also links with food and drink, and cultural and creative industries. The Edinburgh Festival is clearly an important part of Scotland's Creative industries, but depends on the supply of accommodation and food and drink services.
- 3.15 More generally, having high quality facilities is fundamental to delivering a successful business environment. It is simply expected that there are places to stay, restaurants to eat at and shops to visit. High quality services will reflect better on a destination than poor ones.
- 3.16 Although it is not reflected in traditional economic measures, better performing tourism and hospitality businesses contribute to the quality of lives of residents. Improvements in choice and quality are valuable to all the residents that use them. Improving the range of facilities and services in a locality, theoretically, also contributes to increases in property prices. This would be a tangible benefit for residents.
- 3.17 A similar assumption is behind the possibility that good tourism and hospitality generally make places more attractive to live in. They play a cultural role in places and in their attractiveness.
- 3.18 The sector is also important because of the employment opportunities it provides. Research from the World Travel & Tourism Council (WTTC) and Oxford Economics showed that Travel & Tourism employs a higher proportion of women and young people than is represented in the workforce as a whole. A study by CEBR found that

- travel and tourism provides a disproportionate number of youth employment opportunities with over 1/3 of all workers in the industry aged under 30
- the proportion of self-employed workers in the industry exceeding that of the wider economy;
- the industry offers flexible jobs for students, those in training and young people
- women make up 51% of the industry workforce, far higher than the UK average.

3.19 The productivity data shows tourism and hospitality as a heavily labour intensive service industry. Many of the employment opportunities cannot easily be substituted by technology without undermining the value of the service. And because hospitality and tourism has to be delivered “on-site” (unlike a factory which could be located anywhere) it means that the employment it creates are disproportionately important in rural and remote areas, as well as from an equalities and distributional perspective.

3.20 These arguments all highlight the importance of the sector and that regardless of productivity, its quality has knock on effects throughout the economy. Improving productivity is important to sustain and attract investment, pay better wages and generate profits, but it should also be seen in the context of its wider contribution.

4. Productivity in tourism and hospitality

Overall productivity growth in the UK and Scotland

- 4.1 At a UK level all sector labour productivity in 2014 (as measured by output per hour) remains slightly lower than in 2007, prior to the economic downturn. This absence of productivity growth in the seven years since 2007 is unprecedented in the post-war period. In Scotland, however, output per hour has grown by 4% since 2007, although the rate of growth has also slowed since 2010. The result is that Scottish productivity has caught up significantly with UK levels (Scottish productivity has increased from 92% of the UK average output per hour in 2007 to 98% of the UK average by 2013).
- 4.2 The failure for productivity to revert to the pre-crisis trend has stimulated a great deal of analysis. Of most interest here are investigations of how different sectors have responded. One sectoral analysis of productivity was undertaken by the Bank of England and summarised by the CBI in its paper *The UK's Productivity Puzzle? What Business Really Thinks (2015)*¹⁰. This identifies the four sectors that have exerted the largest impacts on the productivity gap; government services, mining & quarrying, hotels & restaurants and financial services. Together, these make up over a third of workforce jobs in the UK, 30% of GVA, but they more than account for the entire productivity gap (. The paper goes on to set out hypotheses for the declining productivity in three of these sectors, but does not provide any insight into hotels and restaurants.
- 4.3 The analysis does describe changes in the food and drink retail sector where the entry of lower cost "discount" retailers has triggered heavy price competition and impacting on labour productivity. This has led to more resources being deployed toward differentiation and maintaining a competitive edge. In an effort to compete, many retailers have been taking on more people to provide a more personalised customer service. A reversal of previous investments in efficiency (e.g. rolling out automated check-outs), which were viewed less favourably by customers. It is worth considering that the drive to boost customer satisfaction (in response to Tripadvisor) could have similar effects in the hospitality sector and may result in employing more people.

Labour productivity in tourism and hospitality in Scotland

- 4.4 GVA per head from 2008 for sustainable tourism (alongside the other Growth Sectors) is shown in Table 4-1.
- 4.5 The tourism figure of £16,832, in 2013, is considerably lower than other sectors. However it has improved significantly over the past five years. Despite a sharp fall in 2013, productivity per head has grown by 20% over this period. Only the Creative Industries sector has grown more quickly (31%).
- 4.6 Improving productivity requires GVA to grow more quickly than employment. Between 2008 and 2012, GVA rose steadily, while employment in the sector fell slightly, leading to

¹⁰ The UK's Productivity Puzzle? What Business Really Thinks (2015), CBI using ONS data - <http://cbi.binarydev.net/news/cbi-boss-on-uk-economy-rebalancing/the-uk-s-productivity-puzzle/>

improvements in labour productivity. The data for 2013 shows a further increase in GVA, but a larger increase in employment, which has the effect of reducing productivity. **The employment increase is mainly within the Restaurants and mobile food service activities.**

Table 4-1: GVA per head for Scottish Government Growth Sectors (£s per worker)

	2008	2009	2010	2011	2012	2013
Food and Drink	42,067	41,065	40,119	44,174	39,975	45,752
Life Sciences	65,177	50,583	62,826	63,730	73,855	59,596
Energy	491,624	357,856	374,811	401,009	352,335	364,324
Sustainable Tourism	13,974	15,244	16,681	15,944	18,444	16,832
Creative Industries	45,134	40,188	40,959	49,245	50,202	58,968

Source: Scottish Government Growth Sector database (accessed August 2015)

- 4.7 Examining the changes in GVA per employee in the subsectors, provides some evidence of where the changes have taken place. While hotel activities and camping grounds have remained relatively stable, other short stay accommodation has fallen sharply in 2013, However, single year figures are not as robust as using longer term averages.

Table 4-2: GVA per employee for KEY SUB-SECTORS within Sustainable Tourism growth sector (£s)

	2008	2009	2010	2011	2012	2013
Hotels and similar accommodation	18,210	17,962	19,359	17,965	22,775	22,349
Holiday and other short-stay accommodation	17,872	19,835	20,225	16,763	25,439	21,502
Camping grounds, recreational vehicle parks and trailer parks	27,292	25,613	29,134	26,297	26,707	27,177
Restaurants and mobile food service activities	12,521	13,116	14,780	15,457	16,771	13,188
Beverage serving activities	13,820	14,339	17,442	14,789	19,447	17,607

Source: Scottish Government Growth Sector database (published 2015)

- 4.8 An alternative way of looking at productivity was considered in a paper by David Battersby¹¹. This presented sales revenue per £ of labour costs. It showed a wide range of returns with the best businesses generating around five times the lowest. It suggests that these overall statistics hide a very broad spectrum of performance, even within sub-sectors.
- 4.9 We have looked at this ratio of GVA to labour costs for all the Growth Sectors in Table 4-3. In effect this shows the GVA per £1 spent on labour costs. Sectors that invest more heavily in mechanisation understandably generate a greater return per £1 of labour, but the low labour costs mean that the ratio for tourism is slightly above life sciences and not far below creative industries.

¹¹ David Battersby, Boosting Skills can raise Productivity, Hospitality Digest 2014, Institute of Hospitality

Table 4-3: GVA per £ of labour costs

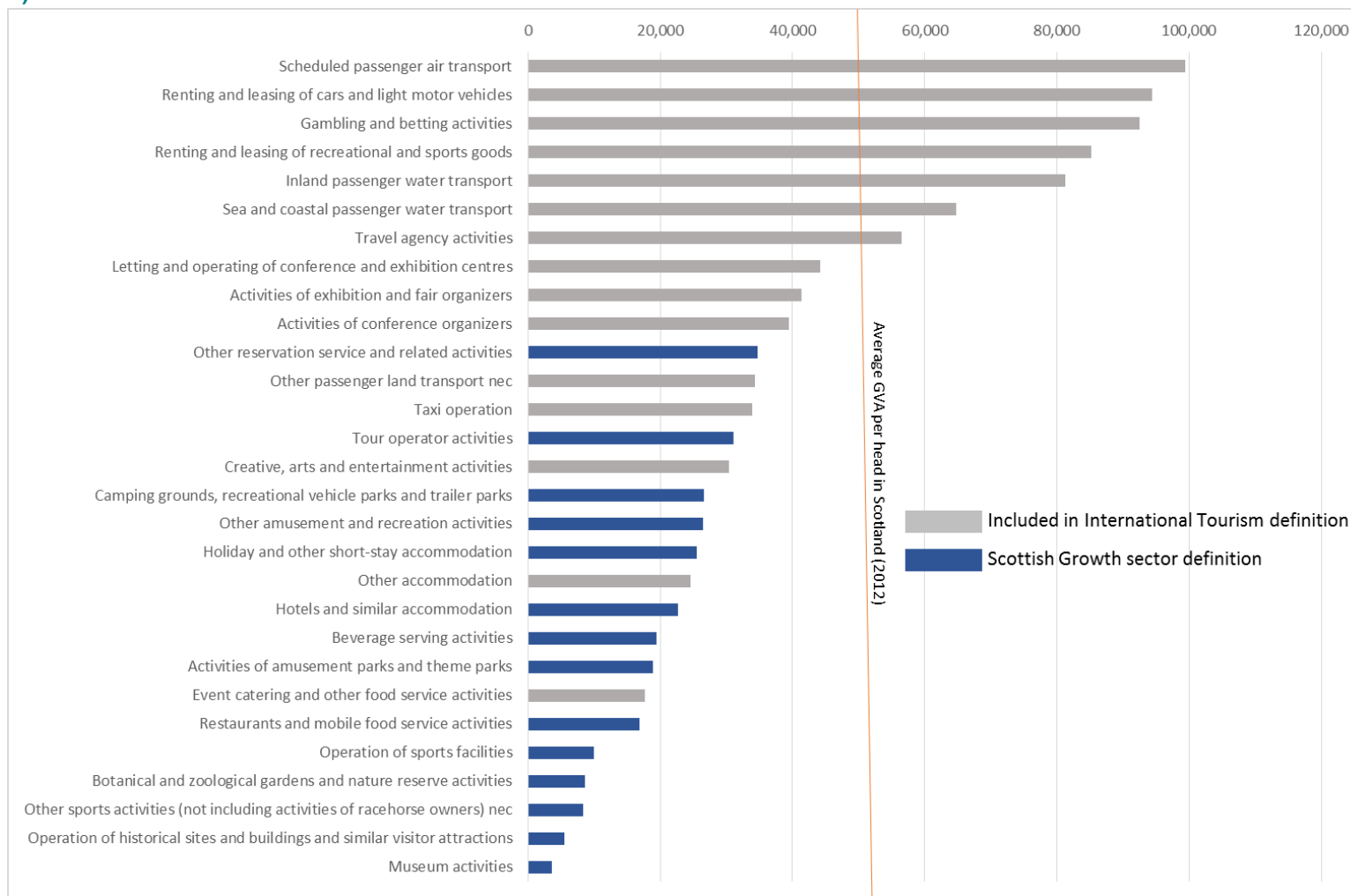
	2008	2009	2010	2011	2012	2013
Food and Drink	£3.12	£2.83	£2.91	£3.09	£2.79	£2.95
Life Sciences	£1.37	£1.15	£1.32	£1.36	£1.71	£1.54
Energy	£8.41	£6.42	£6.24	£6.19	£5.00	£4.89
Sustainable Tourism	£1.51	£1.55	£1.55	£1.52	£1.61	£1.64
Creative Industries	£1.65	£1.65	£1.66	£1.79	£1.77	£2.07

Source: Scottish Government Growth Sector database (accessed August 2015)

Subsectors and types of business

- 4.10 The definition of the tourism and hospitality sectors can have a big impact on productivity figures. Figure 4-1 on the following page, uses two different definitions to show how they compare. The lighter grey bars are the subsectors used in the internationally adopted definition (used by the Office for National Statistics, Tourism Intelligence Unit). The darker bars are categories used in the narrower Scottish definitions.
- 4.11 The chart shows GVA per head in Scotland (2012) for the sub-sectors in these two definitions. It essentially emphasises how the Scottish definition is more focused on the core tourism elements – which also have a much lower GVA per head.

Figure 4-1: GVA per head in Scotland, using the sub-sectors in the International tourism definition adopted by the Tourism Intelligence Unit, Office for National Statistics (2012)



Source: Scottish Government Growth Sector data edited by SQW accessed July 2015

- 4.12 We know that 80% of the activity in the sustainable tourism definition is in accommodation and food and drink services, and therefore it is the rates of productivity in these that will determine overall productivity figures. It is also clear from the sub-sector analysis that these three are among the lower productivity sub-sectors, specifically restaurants and mobile food service activities.
- 4.13 A number of the other “tourism” sectors, such as museums, gardens and sports facilities are operated directly by the public sector or through separate Trusts. This makes it harder to provide estimates of GVA. Because there is no “profit” GVA is assumed to just be the employment costs.
- 4.14 This underestimates the social and economic value of these activities. Maintaining and providing access to heritage buildings, the educational value of museums or the health and community benefits of sports facilities are not captured as “value” by a simple measure of GVA. The previous chapter calculated that these activities represent a small part of the overall tourism sector, less than 10% of employment and less than 5% of turnover and GVA.

Geography

- 4.15 How do the Scottish figures compare with the rest of the UK? Table 4-4 shows that labour productivity tends to be slightly lower in all the subsectors. The main reason for this is because of the much higher levels of productivity in London. The Scottish figures overall are slightly higher than the most of the English regions and Wales (see Figure 4-2).
- 4.16 Growth in productivity has been similar overall, although there are differences within the sub-sectors. The biggest difference is in the restaurant and food service sub-sector, where productivity has grown 5% over 5 years in Scotland compared with 26% in the UK. The closure of pubs has improved productivity within the beverage serving category at a higher rate in the UK than in Scotland. Productivity in hotels in Scotland has grown more rapidly than in the rest of the UK.

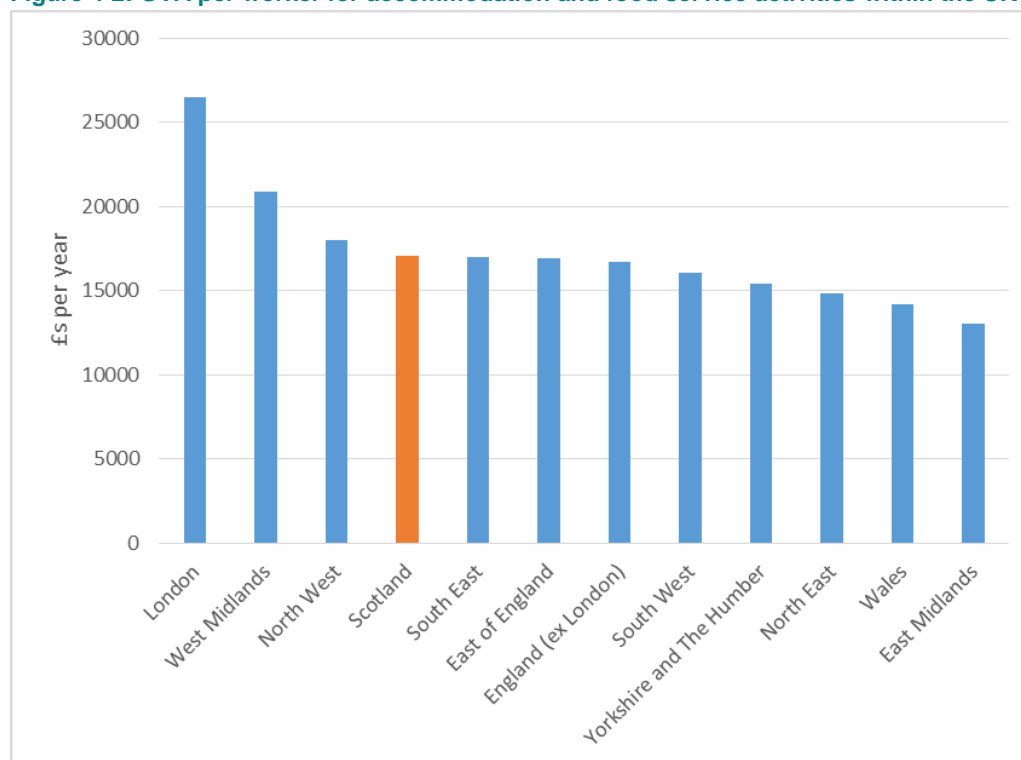
Table 4-4: GVA per worker in Scotland and the UK (2013 data) in £s

SIC categories	Scotland	Scottish growth 2008 - 2013	UK	UK growth 2008 - 2013
All accommodation and food & drink services	17,181	19%	19,473	21%
Hotels and similar accommodation	22,349	23%	25,532	8%
Holiday and other short-stay accommodation	21,502	20%	30,100	24%
Camping grounds, recreational vehicle parks and trailer parks	27,177	0%	34,297	-4%
Restaurants and mobile food service activities	13,188	5%	16,734	26%
Beverage serving activities	17,607	27%	19,000	31%

Source: Scottish Annual Business Survey and Annual Business Survey (2013 data)

- 4.17 The London effect is shown in Figure 4-2 using GVA per employment for Section I, Accommodation and Food Service activities. Excluding London, Scottish productivity is actually slightly higher than the overall English figure excluding London.

Figure 4-2: GVA per worker for accommodation and food service activities within the UK (2013)

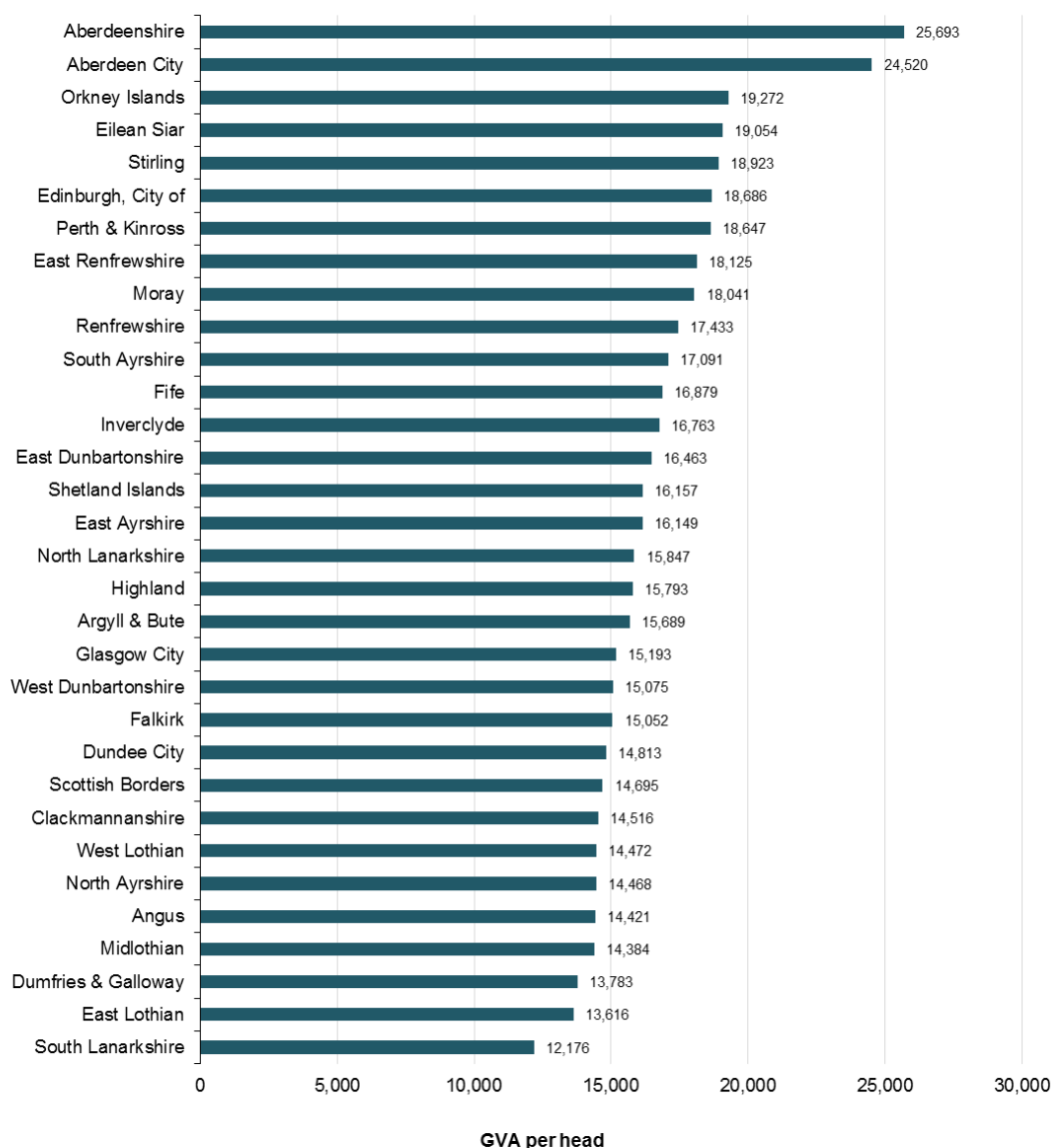


Source: ONS Annual Business Survey (2013) published 2015

Within Scotland

- 4.18 Productivity data for the tourism sector is available at a local authority level up to 2013. Figure 4-3 uses a three year average to avoid some of the inconsistencies in the data. This shows Aberdeen City and Shire, Edinburgh, Stirling and Perth with higher levels of GVA per head than Highland, Dumfries and Galloway or Glasgow. It doesn't appear to closely follow the pattern of visitor numbers. Higher visitor numbers or a high proportion of visitors does not necessarily appear to mean higher productivity. Nor does it indicate that productivity is associated with rural or urban authorities.
- 4.19 There may be a link to disposable income with some of the wealthiest areas associated with higher levels of GVA per worker. These may also be the areas with higher spending tourists, perhaps because prices are set by local demand as much as by visitors.
- 4.20 For example a restaurant that sets prices for a wealthier resident market (e.g. London) would tend to generate higher levels of GVA per worker. It would also increase visitor expenditure. It may have to pay higher wages, but this would be included within the GVA. It is also possible that higher productivity businesses such as larger international operations would locate in wealthier markets, which would allow higher prices to be charged.

Figure 4-3: GVA per head (3 year average 2011-2013) for tourism growth sector



Source: Scottish Government Growth Sector database (accessed 2015)

Size of businesses

- 4.21 It is likely that productivity in smaller businesses in each sub sector have lower productivity than larger ones. If Scotland has a larger number of smaller businesses than other sectors it is likely to lead to lower levels of productivity as there would fewer opportunities to benefit from economies of scale.
- 4.22 Table 4-5 shows the proportion of employment in each business size-band for the Growth Sectors. In tourism, only around 25% of employment is in businesses with less than 10 employees. This is less than the proportion in the creative and food and drink sectors. The main characteristic is the high proportion of businesses in the 10 to 49 size-band (29%) which is almost double the proportion in all the other sectors. There is similar proportion of large

businesses (50 or more employees) in tourism as there are in the creative and food and drink sectors.

- 4.23 While the tourism sector is dominated by smaller businesses this is not unusual in comparison with other parts of the economy. In fact, the prevalence of small diverse businesses could be seen as part of the attraction of Scotland’s tourism offer.

Table 4-5: % of employees working within businesses by size (2014)

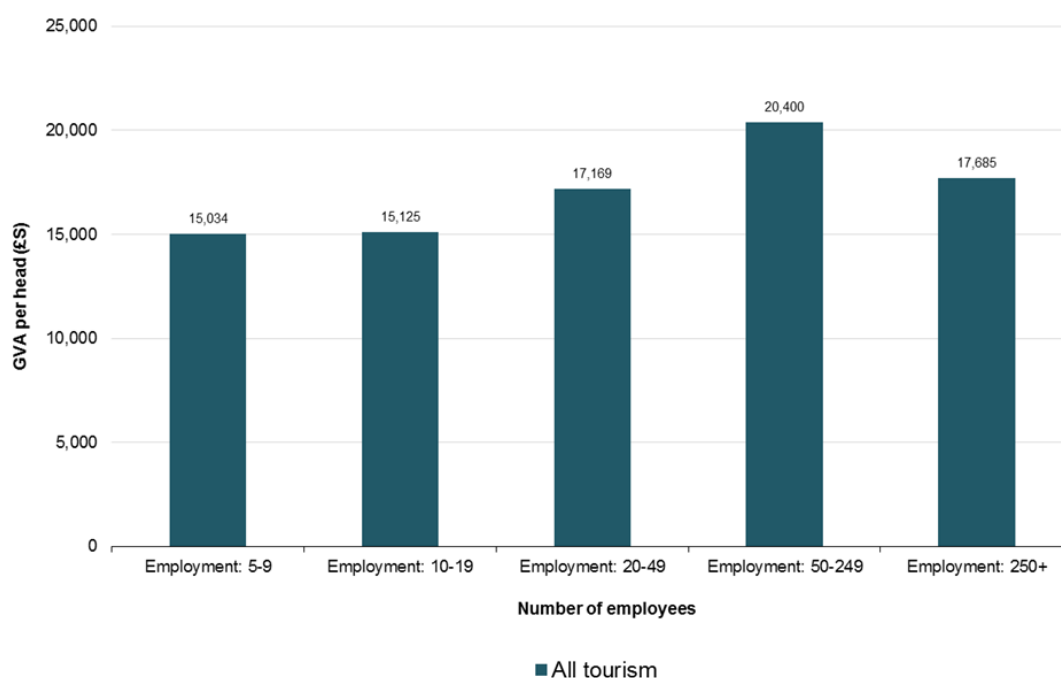
No. employees	Tourism related Industries	Food and Drink	Financial and Business Services	Life Sciences	Energy (including Renewables)	Creative Industries (including Digital)
0 - 9	25%	43%	22%	8%	7%	38%
10 to 49	29%	11%	11%	12%	4%	19%
50+	47%	46%	67%	80%	88%	43%

Source: Scottish Government Growth Sector database (accessed 2015)

Productivity difference by size of business

- 4.24 We would expect the size of a business to have an effect on productivity. Economies of scale usually mean that larger businesses will have higher levels of productivity. There will be a stronger incentive and resources for investment and training. GVA per head figures are shown in Figure 4-4. The chart uses the average GVA per head over the three years 2011-13.
- 4.25 For all tourism there is higher productivity in businesses with 50 – 249 employees but this falls again among the larger ones. There is also little difference between businesses with employment of 5-9 and 10-19.

Figure 4-4: Average GVA per head 2011-2013 by size

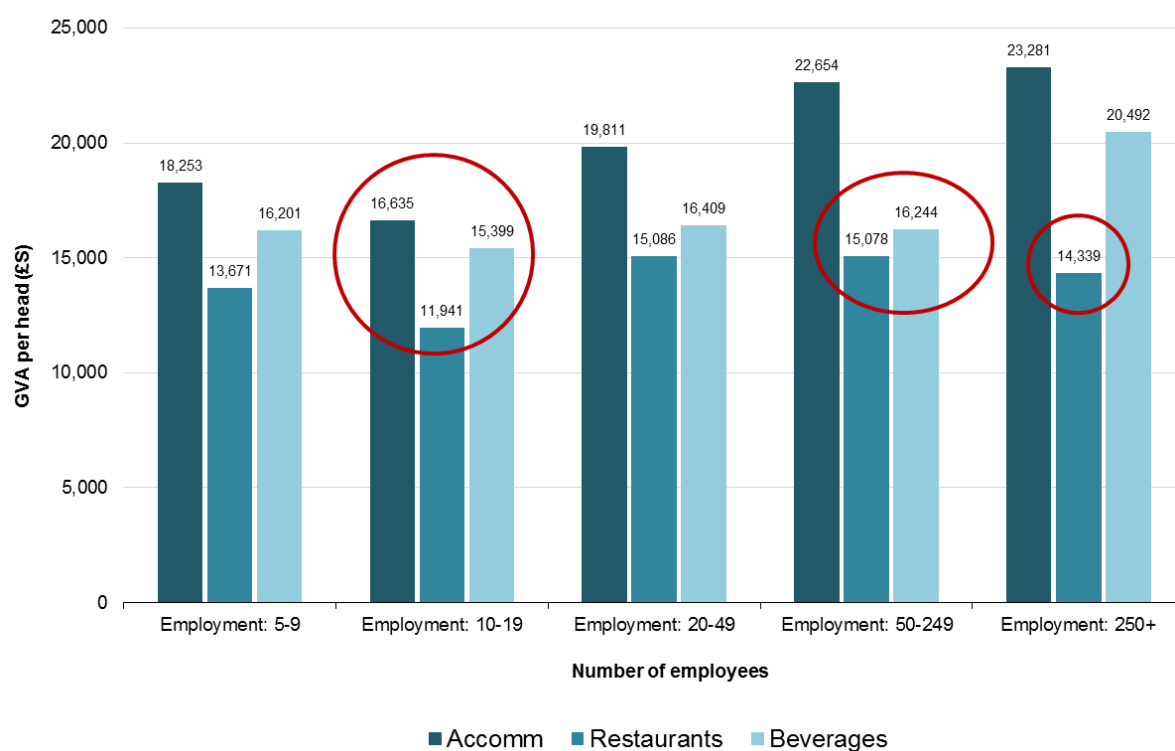


Source: Scottish Annual Business Survey (2013 data)

4.26 The analysis in Figure 4-5 shows the differences for the three main subsector. There are four areas that stand out:

- There is virtually no productivity improvement between businesses with employment of 5 to 9 and the group with 10 to 19, across all three subsectors.
- Productivity among accommodation businesses with 10 - 19 is actually lower than businesses with employment of 5 - 9. There is a significant difference between the smaller and larger businesses, which is not apparent in the other subsectors.
- There is very little difference in productivity in beverage services businesses with employment of less than 250. There seem to be are virtually no economies of scale.
- Productivity in restaurants and food service businesses is slightly higher in businesses with employment of more than 20, but there is little difference between large and very small businesses.

Figure 4-5: Average GVA per head 2011-2013 by subsector and size



Source: Scottish Annual Business Survey (2013 data)

4.27 Our conclusion is that labour productivity is weaker among two groups:

- All businesses between 10 and 19 employees
- Larger (50+) businesses in the food and drink service subsector.

Full and part time employment

- 4.28 Tourism employs a lot of part-time and seasonal workers. Depending on how employment is measured this could contribute to lower productivity figures. Simply dividing output by the number of employees would underestimate productivity per worker.
- 4.29 The Annual Survey of Hours and Earnings (ASHE) provides data on the number of hours worked by sector. In Accommodation and Food services, the sub-sectors that dominate hospitality, the survey estimates that there are a combined 53,000 people working full time in Scotland and 52,000 part-time.
- 4.30 The mean hours worked in the food and drink service sub-sector is well below hours worked in accommodation. For the combined sector, accommodation and food and beverage services, the mean is 28.9 hours a week. This compares with 33.1 hours a week across all Scottish industry and 32.0 in the service sector.

Table 4-6: Full and part time jobs and hours in tourism and hospitality sectors (2014)

	Full time	Part time	Mean hours per week
Accommodation	22,000	11,000	32.5
Food and drink service	31,000	41,000	27.2
Total accommodation and food and drink service	53,000	52,000	28.9
Scotland All Industries and Services	1,557,000	646,000	33.1

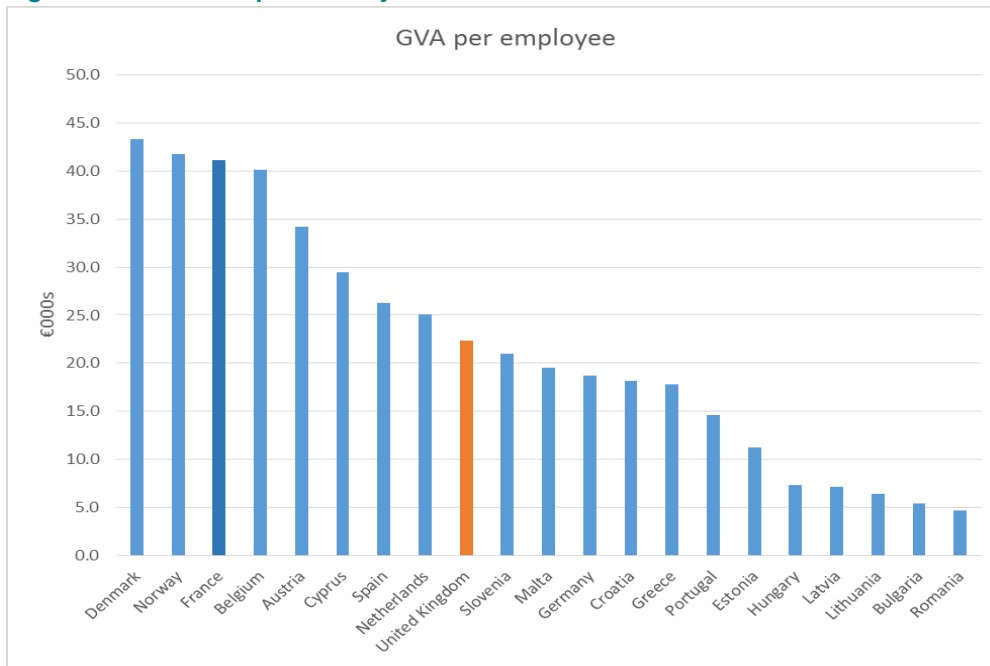
Source:: ASHE data 2015

- 4.31 On this basis, productivity per full time equivalent jobs would be slightly higher in accommodation and food and beverage services. The number of hours worked in these sectors is 87% of the average hours worked per job in the economy. In food and drink services it is 82%. This would mean that the GVA per full time equivalent would rise to £19,277 if the sector worked the same hours as average in Scotland.

Comparison with other countries

- 4.32 Eurostat provides a range of productivity related data for the accommodation and food services sector across the EU. In simple terms, GVA per employee in the UK is broadly similar to Germany and the Netherlands, but significantly different from France, Norway and Denmark (Figure 4-6). In fact GVA per employee in these countries is twice the value for the UK. Reviewing other data also shows that **turnover per employee in France is double the value in the UK.**

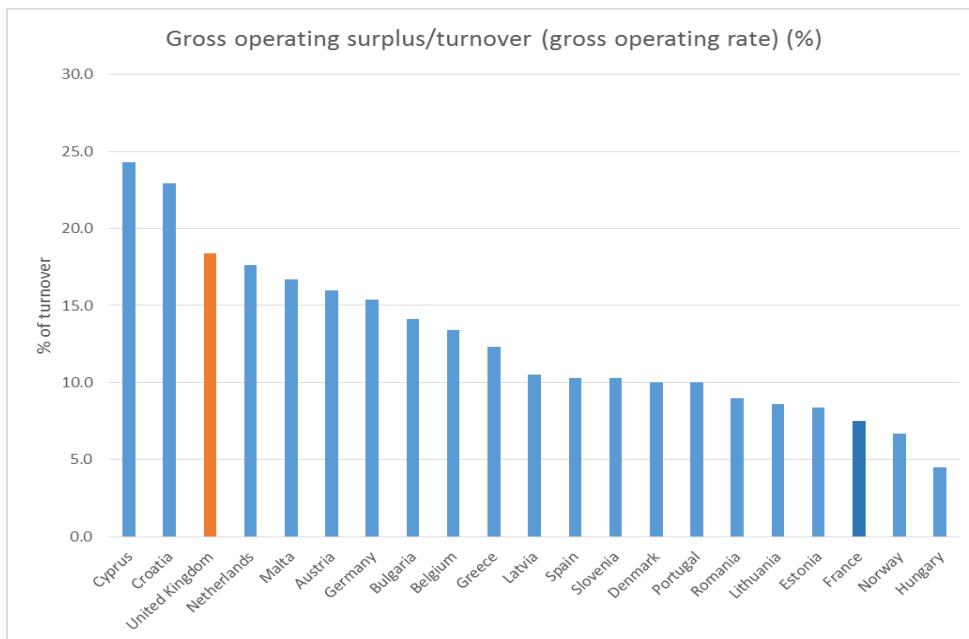
Figure 4-6: EU labour productivity accommodation and food service sectors



Source: Eurostat 2013 data (accessed 9/15)

4.33 By contrast, the Eurostat data shows the gross operating surplus of UK businesses in accommodation and food and Drink services is one of the highest in Europe (Figure 4-7).

Figure 4-7: Gross operating surplus as a % of turnover (2013 data)¹²



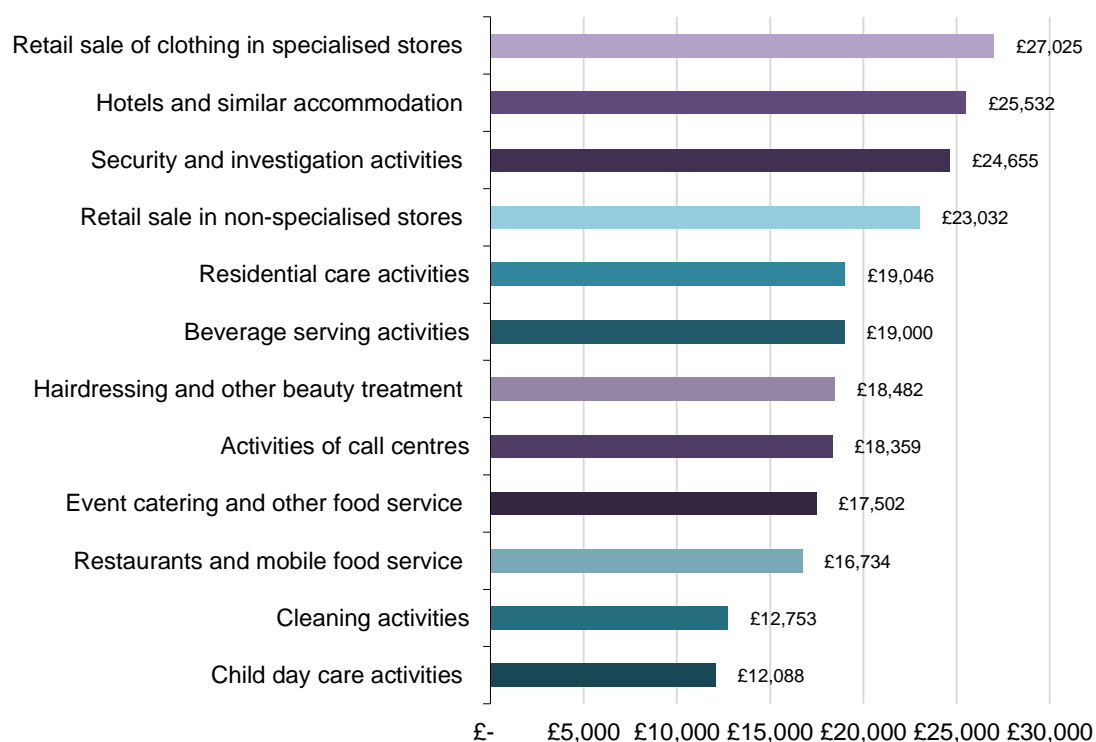
Source: Eurostat 2013 data (accessed 9/2015)

¹² This is an indicator of profitability that corresponds to the share of gross operating surplus in turnover. The gross operating surplus is the surplus generated by operating activities after the labour factor input has been recompensed. It can be calculated from the value-added at factor cost less the personnel costs.

Comparison with other sectors

4.34 Productivity as measured by GVA per worker in the tourism/hospitality sectors are comparable with other labour intensive service activities. Figure 4-8 shows the 2013 data for examples of retail, care, security and cleaning activities alongside some the hospitality sub-sectors. GVA per worker in food service is slightly higher than child care and cleaning, but below most retail activity and hairdressing.

Figure 4-8: GVA per employment (2013) for comparator service activities in the UK



Source: ONS/Annual Business Survey 2013 (accessed 9/2015)

Conclusions on data

- Labour productivity in the tourism and hospitality sector is low compared with most other sectors in the economy, and at a UK level, has not grown in real terms for 20 years.
- In Scotland, using the Sustainable Tourism definition, GVA per worker is £16,831 and this represents an improvement of 20% over the past five years.
- Within the sub-sectors, there is large difference between the productivity of accommodation and food/drink service activities. GVA per worker in the latter is very low at just over £13,000. The figure has fallen recently because of large increase in employment in 2013.

- The figures are broadly similar to regions in England, excluding London. Within Scotland there are also big differences with GVA per worker ranging from £30,000 in the north east to £15,000 in Glasgow (although these are likely to be small samples).
- In sustainable tourism, around 40% of employment is in businesses with less than 20 employees. This is less than the proportion in the creative and food and drink sectors, but a lot more than in energy, life science and finance.
- Productivity is weaker among two groups; all businesses between 10 and 19 employees and the larger (50+) businesses in the food and drink service subsector.
- Part-time/seasonal employment also contributes to low productivity per worker, particularly within food and drink services. Allowing for this would increase the Sustainable tourism GVA to around £19,300.
- While GVA per employee in the UK is broadly similar to Germany and the Netherlands, it is well behind France, Norway and Denmark. In fact GVA per employee in these countries is twice the value for the UK. Reviewing other data also shows that turnover per employee in France is also double the value in the UK. However, the operating surplus in the UK is much higher than all these countries.

5. Sector views

Understanding and measurement of productivity

- 5.1 Productivity measures included a range of indicators based on employment or labour input, such as sales divided by wage costs, sales per employee, or based on the number of available rooms such as RevPAR (revenue per available room) or GOPPAR (Gross operating profit per available room). For other businesses, spend per customer, or meals per employee provide other measures. Different types of business focussed on different KPIs.
- 5.2 For many businesses the number of employees is not really an issue, instead it is how effectively they perform. How much output is produced for the investment in labour, and this supports the view that a ratio of labour costs to sales is a better measure for businesses. Although outside the sector, the value of sales would not be an accurate measure of profit – for example, retail or real estate sales would have high sales per employee but low margins.
- 5.3 The interviews reaffirmed the view that labour productivity will always be lower than in many other sectors in the economy. The main reasons were the focus on service, the problems of managing seasonality, the lower skilled nature of some of the roles, the scale of businesses which makes investment uneconomic, access to finance and the limited opportunities for innovation. The perceptions were that productivity should be improving, although it is also very dependent on levels of demand.
- 5.4 One of the elements that underpins a lot of the discussion is the diversity of businesses within the sector; in what they do, where they are and how big they are. One of the problems of quoting productivity figures is that undoubtedly hide wide variations even within subsectors.
- 5.5 The impression is that while there are a number of highly productive businesses in all subsectors, there is also a long tail of much poorer performers that effectively drag down the sector and sub-sector statistics. Productivity statistics by size of business will help highlight these differences. All of the consultees were part of large businesses and productivity was important to managing them, however they felt that this was not the case in smaller businesses. This was either because small business owners were less interested in productivity, or lacked the experience and analytical capabilities.
- 5.6 The conclusion was that any activities to promote improving productivity should be carefully focused. It is less relevant to those that are already very good and those that are not interested, and should concentrate on the middle group of businesses, with potential and incentive to improve.

Factors which influence productivity levels within the sector

- 5.7 Of the potential influences on productivity, the most important is the **level of demand and sales**. This has a big impact on productivity figures, almost regardless of anything else. It allows businesses to make better use of excess capacity. Simply increasing the number of customers reduces the impact of overheads.

- 5.8 The second priority element is the **quality of leadership and management**. This will drive many of the other influences on productivity. Good leadership and management will ensure that resources (including people) are used efficiently, that there is appropriate investment in new technology, in the building and facilities and in marketing. Good leadership and management will also invest in developing employee skills and motivate staff.
- 5.9 A paper written by David Battersby draws on findings of the Best Practice Forum, This claimed that more than a third (37%) of working time in the hospitality sector is wasted as a result of identifies a number of “doing too much, waiting around, transporting, unnecessary actions and dealing with faults. It claimed that much of this is down to **poor planning, a lack of work organisation and inadequate supervision of staff**”.
- 5.10 For most consultees, it was the quality of this management that can have the biggest effect on all aspects of productivity, both generating sales and in delivering services more efficiently.

Skills

- 5.11 The consultations raised two important issues in discussing productivity. The first is that the **training and staff development is often focussed on customer satisfaction**. Initiatives like World Host or Glasgow Welcomes are about improving service. The Scottish tourism strategy itself encourages businesses to think about the customer journey. *“Its heart is growth via quality, authentic visitor experiences...delivering them to the highest possible standard at each and every point of the customer journey.”* Understandably most of the strategy and the actions are around customer service and generating visitor numbers rather than smarter delivery.
- 5.12 The Skills Development Scotland, Tourism Investment Plan is similar, although it does emphasise leadership and management, much of this is focussed on generating sales and improving customer service skills, rather than improving operational efficiency.
- 5.13 Consultees considered that there was a case for shifting the focus more towards how effectively these tourism services are being delivered. While selling is clearly very important, we also need to think more about how efficiently services are being delivered if we want productivity to improve.
- 5.14 Consultees were also concerned about whether the sector had the leadership and management to address some of the issues that were impacting on productivity. Many of Scotland’s most important hotels and groups are implementing plans to improve productivity. There were views that more could be done to help develop the leadership capabilities within the sector and particularly to promote the benefits of stronger operational analysis.
- 5.15 Central to most of the examples that were provided is the use of IT, for example in helping back office activities, roster planning, data gathering and performance measurement. It was felt that the good businesses were doing this, but it was not as widespread as it could be. The emphasis in ICT has been very much on marketing, web-sites and social media rather than operational tools.
- 5.16 The discussions also considered the balance between the “people” skills that are core to working in the hospitality sector and the analytical skills that are required to measure and drive better performance. They are not mutually exclusive, but there was a broad view that

there can be too little emphasis on the analytical aspects of working in the sector compared with the customer service side.

Box title

People 1st conclusions

A recent People First highlights the issues around skills and productivity in the sector. It specifically highlights issues around staff recruitment and retention. It found that low productivity was **“in large part caused by high levels of labour turnover, which also makes the sector’s current recruitment needs extremely challenging and diverts existing investment in training and development away from addressing skills gaps”**.

It reported that many in the workforce are part time and that this trend has increased by 7% since 2009. This particularly impacts on the hospitality services; pubs, bars and clubs and restaurant industries. The People First report also reported lower wages in the tourism sector. Average pay was reported as £18,127, compared to £27,271 across the economy as a whole.

Finally training was also considered to have a big influence. The report found that tourism sector businesses were slightly less likely to have provided training in the past 12 months, compared to businesses across the economy as a whole (60% vs 66%) and that this has fallen from 82% of sector businesses that provided training in 2009. Separately the UKCES Employer Skills Survey 2013 found that 41% of hospitality and tourism businesses have a training plan and a quarter have a dedicated training budget.

- 5.17 A related issue is whether the industry is recruiting the right people. Is it attracting enough people with the analytical, accountancy and IT skills? This is harder given the competition in the labour market for more numerate skills.
- 5.18 Recruitment is also related to perceptions of the sector, which tend to be that it is often low paid with unsociable hours. Consultees suggested that on the continent the perceptions of the sector were better and the status of those working in higher than in Scotland and the UK. The data from Eurostat suggests that in France in particular turnover per employee, pay and productivity are all higher. Encouraging young people to consider a career in the sector has been a long term objective within the sector, but the People 1st report indicates that there continue to be skills shortages, falling investment in training and low pay.
- 5.19 Consultees felt that there were benefits to working in the sector that were often overlooked, particularly the opportunities for talented people to advance quickly and develop transferable skills, and that there were other benefits such as meals and quality of working environment that are not recognised.

Innovation

- 5.20 The opportunities for innovation in the hospitality sector are not perhaps as dramatic as in others, but can be important in improving productivity. Innovation can be about new structures and systems as well as products. The falling number of “full-service” hotels and the

growth in the provision of simpler, less labour intensive accommodation models, is one example. These models make more use of automatic check-in and check-out, self-service breakfast and offer limited meals. Where there are other facilities nearby, there is no need for the hotel operator to provide them, particularly if they are less profitable. These types of models are innovations within the sector and should result in higher levels of productivity.

5.21 The use of ICT was a key driver of innovation and productivity, although the suggestion from consultees is that the hospitality sector tends to be slow in taking up and implementing new technology. There are several strands to this:

- New ICT tools are important because they allow better management of the business. They can speed up budgeting and accounting, procurement, communications etc., all of which are factors impacting on productivity.
- Secondly, ICT is a core part of measuring performance and this provides the basis for improving productivity. For example, point of sale systems have provided businesses with the tools to analyse performance in sales and manage inventories more effectively, customer counters can monitor visitor numbers. The internet can help “smarter” procurement by allowing price comparison of suppliers and online ordering. However, this also increases the demand for ICT skills, which businesses will not always have.
- Finally, ICT and the internet have revolutionised the marketing and promotion in the sector. On the plus side this has enabled a range of new tools to promote businesses through blogs, Twitter, Facebook, web-sites, on-line booking, targeted promotions etc. But it also makes the market even more competitive on price (which is much more transparent) and on quality, given the importance of feedback sites. This creates opportunities but also puts more pressure on business margins.

Issues around seasonality and variable demand

5.22 Seasonality also has major impact on productivity. Having to service changing demand across the season or even on different days, makes managing capacity more difficult. Although staff numbers can be reduced during quieter times, productivity will still fall significantly below the levels achieved at busier times (because of the overheads such as buildings, heating, rent, holding stock, core staff etc.). It may still be profitable to remain open, but productivity will be lower at quiet times. Using flexible pricing is one way to try and even out demand.

5.23 Seasonality also impacts on the recruitment and investment in staff. Because of the seasonality of demand, businesses constantly face the challenge of recruiting staff for part-time or short time roles. This means a high level of staff turnover, which impacts on levels of training, skills and productivity. This can suit some staff that are looking for temporary work – the sector is vital for student income – but is less attractive to others.

Tripadvisor and customer service

5.24 A further and important change in the hospitality market over the past ten years has been the rise of Tripadvisor and other customer feedback services. On one hand more transparency and greater competition would be expected to improve productivity as it would drive out

poorer performing businesses, but it is also possible that while this has provided big benefits to the customer, it may bid down prices, while also forcing businesses to focus more on quality and customer service, rather than increasing margins.

- 5.25 It is possible that this has played a part in concentrating effort on customer satisfaction and led to more recruitment (as retail businesses have sought to “personalise” services, rather than more focus on improving operational efficiencies.

Investment and access to finance

- 5.26 The main issues raised in relation to investment were both how important it was to the hospitality/tourism sector overall. We would expect to see productivity benefits as new accommodation or restaurant stock is replaced by new more modern facilities. In this context investment in better facilities allows operators to raise prices as well as deliver services more efficiently.
- 5.27 An argument was made that potential investment has been prevented because of difficulties in accessing finance since the financial crisis. Lenders have been less willing to make loans to accommodation businesses in particular in part because of lower asset to loan ratios (lenders will look at the value of building, which has fallen). Since the financial crisis lenders have also been reluctant to invest in property based businesses, given that this was a cause of the problems in 2008. Even for larger hotel groups, securing funding has become harder.
- 5.28 As a result it has become more difficult for businesses to access the investment that could help improve facilities and productivity. While many sectors have faced issues in accessing finance, the hospitality sector was thought to have been disproportionately affected.

Barriers to higher productivity levels

- 5.29 Overall consultees felt that productivity has not been high on the agenda in the sector. In part this has been because of challenges of finding a common definition, but also because of the focus on customer service.
- The need for more leadership and management capability to understand and implement productivity improvements.
 - Limited use of ICT tools for planning analysis and performance measurement
 - Skills shortages (and cost of) attracting the people that can help improve productivity
 - Limited scale and seasonality – makes it harder for small businesses to justify investment
 - Low wages have been a benefit in reducing short term costs and in responding to demand for greater customer service, but can also reduce the incentive to invest in improving productivity
 - Access to finance – over the past five years access to finance for tourism and hospitality businesses has become much tighter and made it harder to fund investments to improve productivity

- 5.30 Perhaps one of the issues over the past five years has been the combination of an increasing focus on customer service and feedback, limited access to finance for investment, and low wages, making it easier to take on more people, rather than improve labour productivity.
- 5.31 There are also different models for improving productivity in different types of business. The larger ones are likely to have higher productivity with more focus on cost management, economies of scale and brands that help maintain demand across seasons. Smaller businesses are likely to face greater challenges and it is probably here that more could be done. The lowest levels of productivity are among food and drink service businesses and there may be more specific support that could be offered here.
- 5.32 Overall, the main message from the consultations was that productivity should be higher up the agenda. There should be more of a balance between the focus on improving customer service and on operating efficiently.

Living wage

- 5.33 The consultations identified a number of arguments about how the increase in the minimum wage would affect businesses and productivity. It will come into force in April 2016 and will have an immediate impact on the wage bills of many businesses in the sector, large and small. The impact will depend on a number of things. In some cases it may reduce re-investment in the business, which could impact on productivity, if for examples, rooms are not refurbished, or marketing curtailed. If the costs are passed on through higher prices it may have some impact on demand.
- 5.34 Alternatively it was also argued that paying a higher wage could create more commitment from staff, and help retain them. It was also argued that higher wages would help focus businesses on how they deploy staff, providing an incentive to reduce excess capacity where possible. It would be expected that an increase in the cost of labour would encourage it to be substituted for capital.

Actions for improving productivity

- 5.35 The consultations also identified a number of more practical ideas of which could help businesses improve productivity.

Actions suggested to raise productivity

- In recruitment and training emphasise the importance of efficiency and operation of the business.
- Use the experience of longer term staff. They will have the best ideas for improving operations and could be incentivised to find ways of making savings.
- Using feedback can help focus on what customers want – helping to invest time and money in the right things – is it necessary to provide some facilities?
- IT can be used to monitor demand and plan rotas more effectively. This only works where staff contracts are sufficiently flexible to respond. Changes in wage levels may provide an opportunity to assess how to deploy staff more effectively
- Equally, increases in wages can provide the basis for redesigning jobs that minimise downtime and encourage greater multi-tasking
- Identify times or areas of business that have excess capacity or are underutilised. Identifying these and limiting or finding other uses for them can generate income or reduce costs.
- Look at opportunities to work as part of the “destination” both in terms of collaborating to increase demand and sales opportunities, but also ways of sharing costs. This could include training, staff, procurement, marketing or selling services to other local businesses
- Tighter management of margins and analysis of performance. Use benchmarks to measure performance and identify the most and least profitable areas of the business.
- Encourage staff to look for ways to work more productively. This could include finding ways to reward them for ideas as well as for better performance.

6. Overview of current interventions

- 6.1 In relation to the delivery of current interventions by SE and partners. Many activities focus on increasing tourism and hospitality markets, and in that sense would be expected to have some positive impact.
- 6.2 However, some interventions focus not only on attracting more visitors and increasing expenditure, but on improving the processes for delivery. For example, innovations that do not attract visitors but reduce costs (easier to clean rooms or beds, new ovens or better IT systems) will improve productivity but would not be considered to be contributing to tourism targets (which tend to be around visitor numbers, expenditure or employment).

Key interventions and impacts on productivity

- 6.3 Table of the main measures and commentary on their contribution to productivity.

Table 6-1:

Intervention	Objectives/description	Productivity
Tourism Innovation	<p>Supporting Sector Team to identify and prioritise strategic/international growth opportunities that can be exploited by investing in innovation</p> <p>Creating opportunities for businesses within and across sectors to collaborate in innovation</p> <p>Initiate Good Practice Pilots.</p> <p>Drive up demand for innovation support in our growth companies using intelligence.</p> <p>Supporting the development of new projects at critical stages of SE or partner approval.</p> <p>Being responsive to sector team demands to use our wider I&E services to drive innovation (OD, ICT, Market Development etc) to support growth.</p>	<p>Innovation support in general tends to focus on the development of new products, packages or marketing. These are measured in terms of increased sales.</p> <p>An alternative would be put more focus on supporting activities that impact on productivity. For example, innovation in processes, reducing costs and enabling staff to increase output.</p> <p>Innovation support and encouraging businesses to be innovative is important for productivity. But this could be made explicit in how it is delivered and crucially in how success is measured</p>
Digital Tourism Scotland	<p>Drive growth, profitability and quality in tourism across Scotland through improving businesses' skills, capabilities and confidence to invest in digital technologies.</p> <p>Inspire and support tourism businesses to lead the way on digital innovation and compete globally with other tourism destinations.</p> <p>Enable tourism businesses to innovate and develop exceptional experiences that will encourage visitors to stay longer and spend more.</p> <p>Enable tourism businesses to exploit and benefit from digital marketing opportunities which will enable them to reach markets globally.</p>	<p>Like innovation much of the focus is on using digital to improve communication with potential customers and improve experiences.</p> <p>The objectives are given as to increase skills in digital and use of digital technology to better meet customer needs and improve marketing. These both focus on increasing sales, rather than using technology for greater efficiency.</p> <p>Within this intervention there is more scope to consider digital technologies to better manage the business.</p> <p>The consultations indicate that using data better and improving analysis would improve productivity. This intervention</p>

Intervention	Objectives/description	Productivity
Destination Development	SE's Destination development approach is about enabling the sector to work together more effectively in specific geographies. The benefits of are better co-ordination, planning, research and leadership.	<p>could support developing capability in order to do this.</p> <p>The destination approach is helping the sector work together through its local tourism groups. These are business led, and while much of the activity is around growing markets there are opportunities to work together to better manage costs and efficiency through sharing resources, strengthening leadership and approaches to management.</p> <p>As with other interventions, the structures exist, and it would be possible to do more to raise the profile of productivity. Perhaps providing more examples of good practice in sharing costs and ideas to improve use of data and analysis. The destinations are already working to strengthen leadership, and from the consultations this clearly an area which can directly impact on productivity.</p>
International sector plan	<p>The International sector plan is divided into attracting inward investment and working with the trade.</p> <p>For example, Inward investment focuses on upper scale/luxury accommodation and resorts to improve the quality of provision in Scotland's seven cities. Major infrastructure opportunities with a tourism component and on Tourism Head office and back office opportunities</p> <p>Trade activities include:</p> <p>Working with groups to encourage and support international sales, identifying companies with the capacity to export and internationalise their products and services, developing market specific projects and training for growth markets and improving the customer experience for international visitors.</p>	<p>Although productivity is not an explicit aim, internationalisation itself tends to improve productivity, both in attracting strong businesses to Scotland and in enabling the best Scottish businesses to sell overseas.</p> <p>Supporting these activities should impact on productivity, although it is not a key part of the rationale for international support.</p> <p>Part of the work to identify opportunities and match this with the capabilities of Scottish businesses should reinforce the importance of profitability.</p> <p>It is likely that the businesses that are engaged with SDI and this support are among the more profitable and productive ones.</p>
Non-tourism specific support	There are a range of other initiatives delivered through various partners that are offered across sectors. For example, through SDI, SDS and local authorities. These include support for internationalisation, skills and innovation	<p>While internationalisation support naturally focuses on developing international markets and increasing sales, skills support is extremely important in developing productivity.</p> <p>In particular SDS are very interesting in how their skills development (and the new Skills Investment Plan for tourism) can contribute to improving productivity. Many of the conclusions in this paper are relevant for this.</p>

Source: SQW

Summary and service gaps

- 6.4 The brief analysis suggests that support for tourism and hospitality businesses tends to focus on two things:
- improving customer experience and satisfaction
 - improving marketing and communication with customers.
- 6.5 This is reinforced by the businesses themselves and these are often the areas that they are more comfortable with. The way that the success of interventions is measured also lends itself to a focus on sales. For example it is based around changes in satisfaction or increases in turnover, while it is harder to measure changes in efficiency.
- 6.6 Our conclusion is that for tourism businesses the structure for interventions to support productivity is there. Specifically, with initiatives around innovation, digital, destination development and skills, through SDS. However, much of the emphasis is on satisfaction and sales. There could be scope to shift the focus within these interventions to help improve profitability and productivity.
- 6.7 There are two useful reports which support this. Work on skills undertaken for SDS develops a business development “ladder” in tourism/hospitality and suggests that as businesses become more sophisticated they move upwards; from initially focusing on customer satisfaction and marketing up to profitability. This is something that our consultations would support. There are also several reports produced for Nesta that support the view that the use of data and analysis, particularly online data, is increasingly important for all businesses¹³ and that “datavore” businesses¹⁴, that analyse and use data more extensively, perform significantly better than those that do not.

¹³ The analytical firm: Estimating the effect of data and online analytics on firm performance (Nesta Working Paper No. 14/05)

¹⁴ The Rise of the Datavores (Nesta 2012)

7. Conclusions

- 7.1 Productivity is important and increasingly seen as such. It is essentially understanding how much value is added relative to the inputs. The most recognisable and accessible measure is labour productivity and this is also the main measure of productivity used by the Scottish and UK governments.
- 7.2 Overall, this paper concludes that productivity should be higher up the agenda of tourism and hospitality businesses and supporting agencies. Much of the focus in the sector has been on increasing sales and customer service, and while these continue to be critical, less attention has been paid to how efficiently these services are delivered. Looking forward, the living wage in particular means that businesses will have to look for ways to improve labour productivity. Achieving this requires a greater emphasis on management, how staff are deployed, how investments are made and how innovation and ICT are used.

Context

- 7.3 In tourism and hospitality, labour productivity is low but comparable with other labour intensive service activities such as cleaning, retail and care. Accommodation and food and drink services are by far the largest elements of the hospitality and tourism sector. Of these, productivity in accommodation is higher than in food and drink services.
- 7.4 At a UK level, GVA in accommodation and food and drink services has grown but so too has employment. The ONS's productivity data, which uses GVA per hour rather than per employee, indicates that labour productivity in the sector has not improved significantly in real terms over the last 20 years.
- 7.5 Productivity in the core parts of the tourism and hospitality sector in Scotland is similar to the rest of the UK outside London. Compared with other EU countries, productivity in the UK is similar to Germany and the Netherlands but well behind France, Denmark, Norway, Belgium and Austria. It is striking that the turnover per employee in these countries is considerably higher, as are wages and salaries. However, Eurostat data indicates that the UK sector generates higher operating surpluses (as a proportion of turnover) than any of these countries.
- 7.6 Within Scotland, there are differences in productivity across local authorities, although care should be taken as sample sizes are likely to be small. However, they show an average GVA per employee ranging from £25,700 in the north east, £20,200 in Edinburgh, £15,200 in Glasgow and £13,800 in Dumfries and Galloway.
- 7.7 Labour productivity is relatively low (compared to many other services and manufacturing) because it is inherently a "people" business. There are fewer opportunities to mechanise or automate the work, and doing so could also have a negative impact on attracting visitors and on the diversity of services that Scotland offers.
- 7.8 It is also possible that the emphasis on visitor satisfaction, as well as the growing importance of customer feedback sites such as Tripadvisor, has led to a much greater focus on customer

service, which typically requires more people (and has coincided with a period of relatively low wages).

Influences

7.9 The main influences on productivity are:

- **volume of sales** - many businesses have core staff numbers and overheads. Attracting more customers and increasing sales makes better use of the capacity. This directly improves productivity. This is why it is surprising that employment has grown almost as quickly as turnover.
- **leadership and management** – good leadership and management will recruit and retain the right staff, introduce new ideas and systems, invest in improving assets and use ICT tools to make the most efficient use of resources.
- **balance of skills** - tends to be towards customer service with less emphasis on understanding productivity and delivering services more efficiently. More could be done to encourage a more analytical assessment of how the business makes money. A recent People 1st report also highlights the impact of high labour turnover on productivity. Low wages, increasing part time jobs and less training were also considered to have an effect.
- **increasing and improving the use of technology/innovation** – this has tended to focus on marketing and social media, and less on using software to reduce the costs of suppliers, plan staff rostering, gather point of sale information, calculate margins etc. Likewise innovation has been about new offers for customers and less about new systems or processes for the business.
- **Investment** - it has become more difficult for businesses to access finance and fund investments that could help improve facilities and productivity.

7.10 There is no doubt that the overall productivity data hides a broad spectrum of performance. The paper by David Battersby found very large differences in the best and worst performers. Tourism and hospitality is slightly unusual in that people often set up businesses with little or no business experience. The sector lends itself to “lifestyle” businesses, where the owners are perhaps less worried about maximising productivity and profit. Combined with the seasonal challenges of the sector and the fact that it supports jobs in many rural and remote areas, it is perhaps not surprising that there is such a wide range of productivity.

7.11 This has implications for both understanding productivity and how to provide appropriate and effective support. For example, the key areas are likely to be smaller and medium-sized businesses where these barriers are more severe, and where support could make the biggest difference.

Living wage

7.12 This will come into force in April 2016 and will have an immediate impact on the wage bills of many businesses in the sector, large and small. Although, in theory, wages are part of the valued added the business generates, and therefore it should be a redistribution of the

surplus, it will also have indirect effects on the incentives for business owners and managers. In some cases it could reduce re-investment and would impact on productivity if for example, rooms are not refurbished, marketing curtailed or less investment in ICT. Alternatively, if the costs are passed on through higher prices it may have some impact on demand.

- 7.13 Alternatively it was also argued that paying higher wages could create more commitment from staff and help retain them. It was also argued that higher wages would help focus businesses on how they deploy staff, providing a greater incentive to reduce excess capacity where possible. It would be expected that an increase in the cost of labour would encourage investment to save labour. Its impact will vary from business to business, but it certainly raises the importance of improving productivity and a bigger role for the agencies that support the sector.

Conclusions

22. With increasing pressure on wages, productivity is set to become more important to businesses. It is an opportunity to focus more on how it can be improved. The size of the industry, means that even small improvements would generate improvements in profits and wages, making the sector more sustainable.
23. **Overall, this paper concludes that productivity in general should be higher up the agenda of businesses and supporting agencies in the sector. While the focus on the customer journey and service is essential, there should be greater attention paid to operational efficiency.**
24. Of all the areas related to productivity, the main theme was in developing leadership and management skills. This is the basis for influencing many of the other factors that determine productivity.
25. In addition to actions designed to grow markets, activity to support productivity should focus on the following three areas:
- **leadership and management skills**
 - **better/more use of ICT**
 - **better/more use of data and analysis.**
26. The analysis by business size suggests that this should be focussed on smaller businesses, for example with around 10 to 20 employees.
27. Case study examples that show where these actions have worked, and demonstrate financial benefits for businesses and staff would also help generate interest.