Middle East

2020 Industry Forecast

from BCD Travel Research & Innovation

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Industry Forecast

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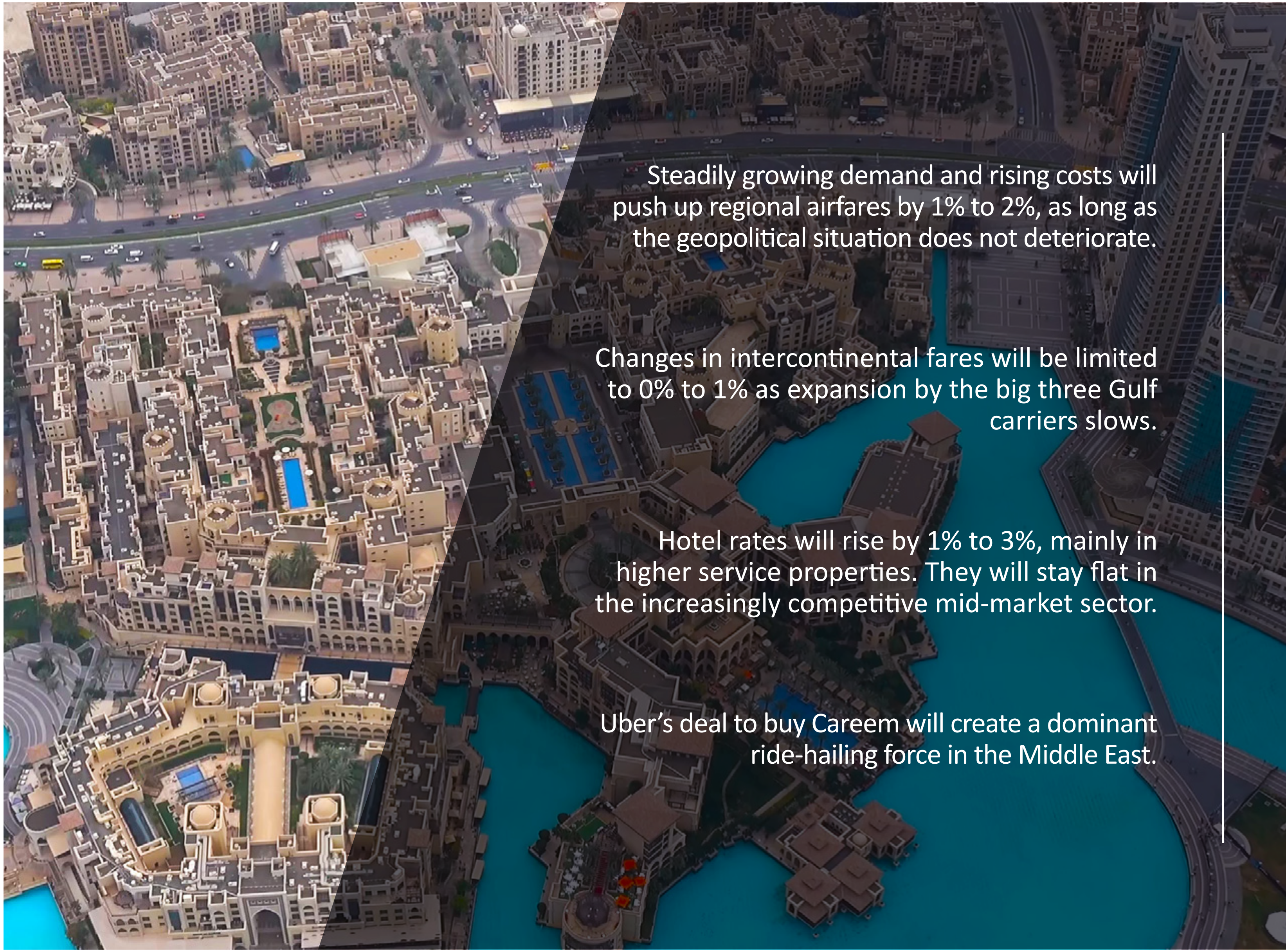

Steadily growing demand and rising costs will push up regional airfares by 1% to 2%, as long as the geopolitical situation does not deteriorate.

Changes in intercontinental fares will be limited to 0% to 1% as expansion by the big three Gulf carriers slows.

Hotel rates will rise by 1% to 3%, mainly in higher service properties. They will stay flat in the increasingly competitive mid-market sector.

Uber’s deal to buy Careem will create a dominant ride-hailing force in the Middle East.

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Air

Current situation

The days of relentless expansion by the Middle East's three mega carriers—Emirates, Etihad Airways and Qatar Airways—appear to be over. Capacity was flat among the region's airlines during the first five months of 2019. And in May, the Middle East was the only region where capacity declined, as average seat kilometers (ASKs) fell 5.9% year over year.

The reductions are partly a natural correction following years of unrestrained expansion. They are also the result of airline restructuring and financial damage caused by a series of ill-fated investments in carriers outside the region, including Air Berlin, Alitalia and Jet Airways. Rising geopolitical tensions are also playing a role: Qatar's dispute with its Gulf neighbors is unresolved; the killing of journalist Jamal Ahmad Khashoggi has damaged relations between Saudi Arabia and Turkey; and Iran is becoming more assertive.

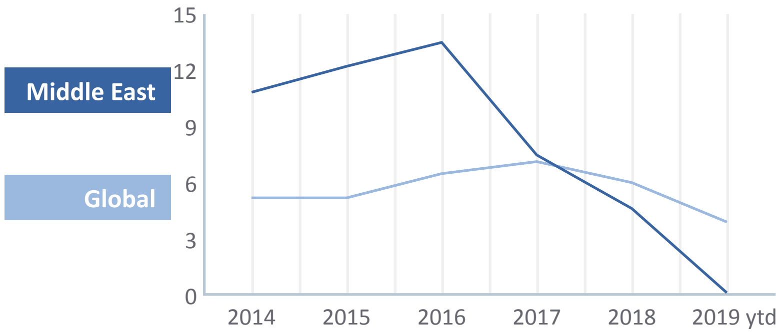
The Middle East is rarely free of political tensions, and its airlines have developed a resilience to the problems around them. For example, Qatar Airways is operating almost as usual, despite Qatar's regional isolation, which has led to the suspension of the busy Doha-Dubai route and the rerouting of many of the airline's flights. It continues to expand, with Isfahan, Iran, and Rabat, Morocco, among the recent additions to its network.

Similarly, although the Khashoggi affair has caused a sharp fall in air travel between Turkey and Saudi Arabia, overall demand in the Saudi market is down only slightly.

Across the Middle East, air travel demand was weak; expanding by just 1.2% in the first half of 2019. Dubai International Airport—the world's third-busiest—recorded a 2.2% drop in passengers during the first quarter, although the grounding of the Boeing 737 Max 8 and the later timing of Easter may have affected demand.[1]

One likely explanation for the stagnation of demand is the growth of direct services between Europe and Asia. More fuel-efficient aircraft, such as the Boeing 787 and Airbus A350, are making "thinner" routes to smaller markets viable. Travelers are switching from slower, indirect journeys through airports in the Middle East to these direct routes.

Global and Middle East airline capacity growth



Source: IATA

The rise of Flydubai

Sister carrier to Emirates, Flydubai is becoming an increasingly important option for business travelers. Launched in 2009 as a low-cost carrier, it increased its appeal to the corporate market in 2013 by including a business-class cabin. Its flights are also bookable through global distribution systems, the reservations channel of choice for the corporate travel industry.

Flydubai offers frequent service to 27 points within the Middle East. It is also developing connections to mid-haul niche destinations. These include Asmara, Eritrea; Juba, South Sudan; Djibouti; and Hargeisa, as well as seven destinations in Central Asia and cities in Eastern Europe. It serves 83 destinations in total.

Flydubai's future growth could be impeded by the grounding of the Boeing 737 Max 8. It has 14 of the aircraft in its fleet, with orders for a further 237 for future development.

1 Gulf Business, May 5, 2019

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India is a major exception to this trend. Demand is growing fast, and airlines are quickly filling the gap in supply left by the collapse of Jet Airways. Emirates has agreed a new alliance with Indian low-cost carrier SpiceJet to maintain its presence in the Indian market. However, the loss of Jet Airways has still reduced competition, leading to a rise in fares on these routes.

The intra-Gulf market (other than Doha-Dubai) has also stayed healthy. Such is the strength of demand that Emirates has replaced smaller aircraft with Airbus A380s on flights from Dubai to Muscat, Oman, and Riyadh, Saudi Arabia.

Apart from India, fares are generally flat, as carriers have so far been successful in adjusting capacity to slower demand. The big three Gulf carriers are keen to secure more business from corporate clients and are offering improved discounts to customers they believe will deliver significant market share. They are, however, increasingly negotiating with clients route by route, rather than offering blanket network discounts.

Outlook for 2020

Much depends on the development of the Iranian situation. If the crisis deepens, air traffic to the Middle East could be affected severely, although that would be only one of many challenges for aviation. Potential disruption to oil supply would drive higher fuel prices, increasing airline costs and, ultimately, airfares.

Even if the Iran situation does not deteriorate, air capacity is likely to remain flat into 2020. Demand will increase slightly. With airline costs likely to rise, fares will rise marginally—on average by 1% for business class travel and by 2% in economy on better-performing routes within the region.

Emirates plans to launch a premium economy service in 2020. Unlike many of its rivals, the Emirates' product is likely to be situated in a fully segregated cabin, separate from regular economy.[2] The service could tempt some corporate customers to increase their spend by upgrading from economy; but others

2 Condé Nast Traveler, July 19, 2019

Israel—market deregulation leads to lower fares

A booming economy has supported a 4% to 5% rise in demand for corporate travel in Israel. Growth in demand for leisure travel is into double digits. However, supply has grown even faster as Israel has pursued an open-skies policy of market deregulation. Carriers from around the world—both traditional and low-cost—have launched flights to Tel Aviv for the first time, fostering competition. For example, over the last two years flag carrier El Al has lost a virtual monopoly to Asia, as Air India, Cathay Pacific, Hainan Airlines, Sichuan Airlines and Korean Air started Israeli services. Singapore Airlines and two more Chinese carriers are considering launching flights, too.

A switch by some airlines to smaller aircraft has barely affected the overall increase in seat numbers. As a result, fares have fallen, especially to Europe, with major low-fare carriers easyJet, Wizz Air and Ryanair all launching Israeli routes.

The competition has made El Al more willing to negotiate corporate deals. But few Israeli companies offer enough volume to justify a negotiation process; most rely on prices negotiated by their travel management companies.

Expect the fare drops to continue in 2020 and for another two to three years as demand catches up with supply.

Our recommendations:

- Encourage travelers to consider using low-cost carriers. But remember most flights to and from Israel take well over two hours.
- Make sure your TMC and booking tool are set up to offer all flight options—not only traditional and low-cost carriers but charter airlines, too, as they are an important source of supply in the Israeli market.

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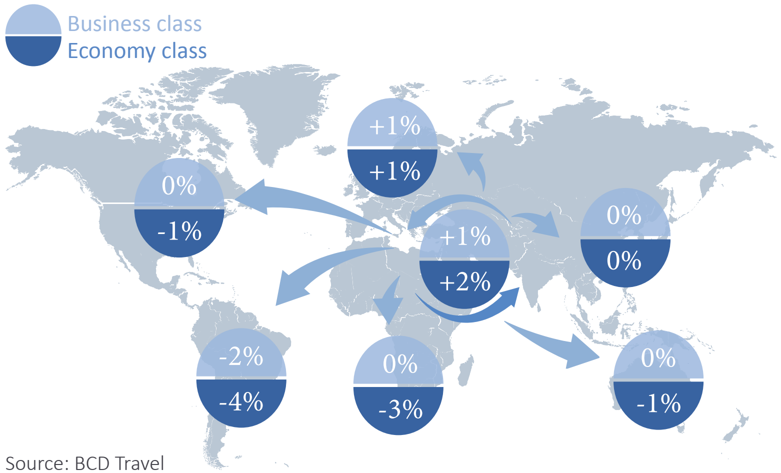
Airfare forecasts

Average ticket prices
% change YoY

	Intercontinental		Regional	
	Business	Economy	Business	Economy
Middle East	1%	0%	1%	2%



Source: BCD Travel

might lower spend by downgrading from business class. Emirates is already targeting this latter group with new basic business fares.

The United Arab Emirates and India are expected to begin discussions later this year to liberalize their bilateral air agreement.[3] A new agreement could increase services and reduce fares in this busy market.

Our air recommendations

- Take advantage of promotional discounts offered by the three Gulf carriers trying to fill their aircraft.
- Gain administrative efficiencies and improve data by shifting payments from invoicing (still the norm in this region) to card.

Emirates offers basic business fares

Emirates has started selling no-frills business class fares offered on an ad hoc basis, depending on route performance. That makes it difficult to assess their suitability for inclusion within corporate programs. The potential savings is as high as 30% on these basic business fares, but they come with a number of restrictions, compared to standard business class service:

- No limousine/transfer
- No lounge access for passengers without elite loyalty program status
- No advance seat reservation
- Nonrefundable or higher change/cancellation fees
- Reduced frequent flyer mileage accrual

These fares are also not subject to corporate discounts.

Look out for Dubai Expo 2020

Dubai's airfares and hotel rates could rise when the emirate hosts Expo 2020 for six months, starting Oct. 20, 2020. If flights to Dubai are full or very expensive, Abu Dhabi may be a good alternative; it's roughly 90 minutes away by road.

3 Gulf News, June 15, 2019

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Hotel

Current situation

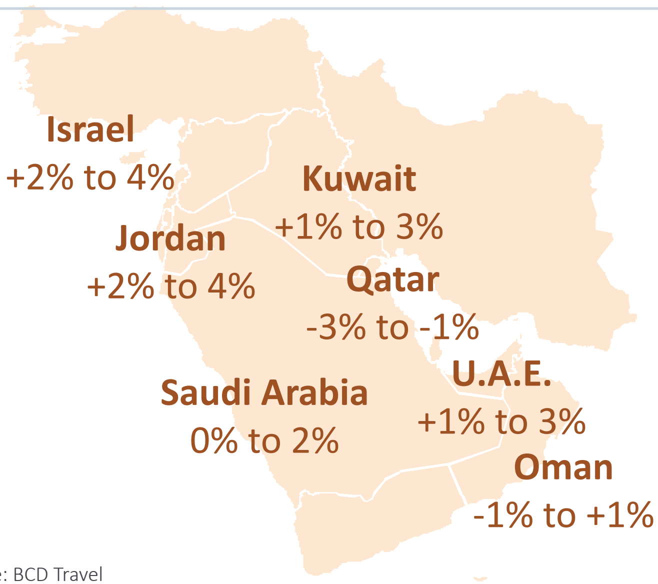
Hotels continue to open across the region, especially in Dubai, where a new wave of construction is bringing properties online to meet the anticipated surge in demand from Expo 2020. The rise in occupancy has brought rates down marginally, especially because the new hotels are generally in lower price brackets. Prices are also dropping in Qatar, where political isolation has depressed demand and lowered rates 10%.

But rates are on the rise in Bahrain and Abu Dhabi. And in Israel, demand outpaces supply, even though Israeli business travelers prefer day trips and rarely use hotels, and technology has made it easier for travelers to search and book independent hotels. However, a shortage of accommodation, especially in Tel Aviv, has pushed rates very high, and they continue to climb.

Hotel forecasts

Average daily rates % change YoY

Middle East	1% – 3%



Source: BCD Travel

Outlook for 2020

Supply will grow substantially. Demand will grow modestly, as long as the Iran crisis does not escalate. Hotel rates will climb by 1% to 3% on average, although they will decrease by this range in Qatar if political differences with its neighbors continue.

Rates in upscale hotels are more likely to rise but will be unchanged for the midscale tier, where competition is increasing.

New hotels are under construction in Tel Aviv. The added supply will not match growth in demand, especially as the Israeli government vigorously promotes inbound tourism. The city will once again see some of the region's strongest rate rises, up 2% to 4%.

Our hotel recommendations

- Investigate the new lower-tier options in a region known mainly for its luxury hotels.
- In major cities, consider hotels in the suburbs as an alternative to central locations. Rates can be significantly lower, and journey times to downtown may only take 30-40 minutes.

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Ground transportation

Ride-hailing

Uber has agreed to acquire local provider Careem.[4] The Careem brand and app will be retained, at least initially. The deal, which should be completed in the first quarter of 2020, could lead to ride-hailing becoming more popular in the Gulf, but will also significantly reduce competition. The acquisition must be approved by regulators in the countries where Careem operates.

In Israel, ride-hailing is often preferred to taxis because pricing is more transparent. Uber and GetTaxi are the two most popular apps in this market.

High-speed rail

The Middle East's first high-speed line, running 453 kilometers across Saudi Arabia from Medina to Mecca, opened in September 2018.[5] It is hoped the new service will stimulate the growth of King Abdullah Economic City. The line will eventually link to a new terminal at the airport in Jeddah. Further expansion could include an east-west service between Riyadh and Jeddah.

4 Reuters, March 26, 2019
5 The Guardian, Sept. 25, 2018

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Methodology

Assumptions

We have assumed, as working hypotheses, that:

- The price of oil (Brent crude) per barrel will average US$67 in 2020.
- World economic growth will be 2.7% in 2019, holding steady at 2.8% in 2020.

Approach to analysis

Our ongoing research and in-depth interviews with experts in corporate travel and meetings management form the basis for our discussion of broader industry developments and trends.

We base our category-specific predictions on our analysis of aggregated transaction data for BCD Travel's corporate clients worldwide.

We analyze and forecast on dynamic baskets using actual air segments, room nights and car rental bookings to reflect potential shifts in travel patterns and booking behavior. The level of aggregation for each measure is determined by the validity of the relevant pool of data.

We weight monthly averages by category transactions for each unit. Regional averages for hotels are calculated using total room nights to weight the forecasts for all countries in that region. Quarterly averages are weighted averages of the months in that quarter. Unless stated differently, we base price developments on local currencies; these developments are therefore subject to foreign exchange fluctuations. We normalize local currency transaction data into leading world currencies, using the daily average conversion rate on the date of travel.

Hotel market tier assignments follow our proprietary classification scheme. We designate luxury and upper upscale hotels as upper tier and all other hotels as lower tier. Air cabin classes are based on our master table of airline booking classes.

When applying economic growth in our regional forecasts, we use figures aggregated at market exchange rates rather than at purchasing power parity (PPP). The PPP approach risks overstating the contribution of emerging markets.

Sources

In addition to aggregated BCD Travel client data, we use the following sources:

- International Air Transport Association (IATA) for airline capacity and traffic
- Oxford Economics for historic and forecast macroeconomic data
- Tourism Economics for room nights by region
- International Monetary Fund (IMF) for macroeconomic projections
- Economist Intelligence Unit (EIU) for macroeconomic projections and oil prices
- Oanda Currency Converter for foreign currency exchange rates
- Official Airline Guide (OAG) for airline capacity
- U.S. Energy Information Administration (EIA) for historic and forecasted oil prices
- Flightglobal.com for airline industry news and analysis

The estimates and projections are based on data available through March and April 2019, respectively, for air and hotel transactions, and through July 2019 for macroeconomic and industry indicators.

Meet the team behind the Industry Forecast

Mike Eggleton
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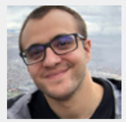

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