TAX POLICY AND US HOTEL INDUSTRY ECONOMIC IMPACTS

NOVEMBER 2017

EXECUTIVE SUMMARY

To quantify the potential impacts of tax policy changes on the hotel industry and the industry's valuable contributions to the US economy, Oxford Economics conducted a scenario analysis for the American Hotel & Lodging Association (AHLA). The analysis highlights a five-year period beginning in 2018, and focuses on tax policy changes under tax cuts of $1.5 trillion over a ten-year period, which we believe will cause real GDP growth to accelerate to 3.0% in 2018 before gradually slowing.

The results show that tax cuts provide a stimulus to the economy and are expected to generate a boost to hotel industry operations, cause additional guest spending at restaurants and stores in the travel destination, and increase hotel capital investment—all benefitting the broader national economy.

Specifically, the tax cut scenario analyzed in this study would support:

- $57.4 billion of additional hotel guest spending in the US (onsite at hotels and ancillary guest spending, such as at local restaurants and stores);
- $131.7 billion of additional sales at US businesses, including additional purchases by hotels of supplies and services;
- $22.3 billion of additional wages and salaries for US workers, equivalent to the annual compensation of 94,700 employees for five years; and
- $3.9 billion of additional state and local tax revenues.

With lower personal income taxes and broad increases in employment, wages and salaries, US consumers would have more discretionary income for travel. Meanwhile, increased business activity and investment would support stronger business travel. Employee training and meetings with customers would increase as businesses respond to the stronger economy.

Under this tax cut scenario, **direct hotel guest spending would be $57.4 billion higher** over the five-year period, compared to a scenario without tax cuts. More hotel guests means more spending in local communities, including stores, restaurants, and attractions. That would also contribute to higher state and local tax revenues, including occupancy and sales taxes.

This increased demand at hotels would support hiring new employees and additional shifts for existing ones, as well as additional capital investment in hotels. **All told, this investment would result in an estimated $22.3 billion in additional direct wages and salaries for employees at hotels and other business serving hotel guests or involved in hotel construction or renovation.**

Tax Policy Assumptions

This analysis is based on assumed characteristics of legislation that may be passed by Congress. In the scenario with tax policy change it is assumed that: (1) there is a reduction in personal income and corporate taxes that results in net tax cuts over ten years; (2) many, or all, of the tax cuts, sunset after ten years; and (3) the tax cuts disproportionately benefit higher-income households. Other assumptions were also made in performing the analysis.

The impacts of tax policy changes were quantified using Oxford Economics' Global Economic Model. In the framework of this model, tax reductions stimulate economic activity in the short-term, but moderating factors impact the positive effects, including, but not limited to, a reduction in tax revenue, increased government debt, and higher interest rates.

1. OVERVIEW

Tax policy changes have been a central part of the political dialogue over the past year and various proposals have been put forward to simplify the tax code. These proposals have also implied reductions in both corporate and personal tax rates. To quantify the potential impacts of tax policy changes on the hotel industry and the industry's valuable contributions to the US economy, Oxford Economics conducted a scenario analysis for the American Hotel & Lodging Association (AHLA).

As part of this analysis, we prepared two macroeconomic scenarios to analyze how tax policy changes would affect the broader economy:

- **No Tax Cut Scenario:** No tax policy changes.
- **$1.5 Trillion Tax Cut Scenario:** Tax policy changes that result in net tax cuts of $1.5 trillion over a ten-year period

Based on these scenarios and previous research Oxford Economics conducted for AHLA, we analyzed the impacts to the hotel industry and its broader contribution to the US economy over a five-year period beginning in 2018.

The results show that tax policy changes that provide a stimulus to US economic activity are expected to generate a boost to hotel industry operations, as well as cause additional guest ancillary spending (e.g. at restaurants and stores in the destination) and capital investment by hotels. This boost to the hotel industry would further benefit the broader economy.

In the **$1.5 Trillion Tax Cut Scenario**, we estimate real GDP growth would accelerate to 3.0% in 2018, before gradually slowing. Relative to the No Tax Cut Scenario (2.0% GDP growth in 2018), this short-term boost would lift personal income, employment, consumer spending and investment. These effects would result in increased hotel demand, spending by hotel guests, and hotel capital investments; thereby supporting increased earnings by hotel employees, purchases from suppliers, and indirect and induced economic impacts. As shown in Fig. 1, the economic impacts of the hotel industry in the $1.5 Trillion Tax Cut Scenario would support:

- $57.4 billion of additional hotel guest spending in the US (onsite at hotels and ancillary guest spending, such as at local restaurants and retail stores) over a five-year period (all estimates reported in real, 2015 dollars);
- $131.7 billion of additional economic output, representing sales at US businesses;
- $22.3 billion of additional wages, salaries and other labor income for US workers (equivalent to the annual compensation of 94,700 employees for five years), including $11.0 billion of direct labor income earned by employees at hotels, other businesses serving hotel guests or involved in hotel construction or renovation (equivalent to the annual compensation of 55,300 employees for five years); and,

- $3.9 billion of additional state and local tax revenues (e.g. occupancy, sales and property taxes).

Fig. 1 Impact summary: $1.5 Trillion Tax Cut Scenario

Difference relative to No Tax Cut Scenario	**Cumulative impact** (5-years, 2018 to 2022)	
	Direct	**Total**
Direct hotel guest spending (onsite at hotels and ancillary), real	**$57.4**	
Output (business sales), real (billions)	$61.1	**$131.7**
Wages, salaries and other labor income, real (billions)	$11.0	**$22.3**
State and local taxes, real (billions)	$2.5	**$3.9**

Note: Total hotel industry impacts include direct impacts (hotel guest spending onsite at hotels, ancillary guest spending, and capital investment) as well as indirect and induced impacts. Monetary amounts in billions of real 2015 dollars. Wages, salaries and other labor income are also referred to as labor income.
Source: Oxford Economics

2. ECONOMIC ANALYSIS

2.1 TAX POLICY ASSUMPTIONS

Tax policy proposals at this stage are initial blueprints, and are expected to change in the legislative process. These proposals give early, and likely rough indications of the tax legislation that may be ultimately passed by Congress.[1] For this analysis, we have assumed the following:

- In the $1.5 Trillion Tax Cut Scenario, there is a reduction in personal income and corporate taxes that results in net tax cuts over a ten-year period. These tax cut amounts are net of government spending reductions undertaken to help offset tax revenue reductions.
- No additional infrastructure spending is assumed as part of the $1.5 Trillion Tax Cut Scenario relative to the No Tax Cut Scenario.
- Many or all of the tax cuts are assumed to sunset after ten years to comply with the rules of budget reconciliation. Government spending cuts partly offset tax revenue reductions, but such cuts are back-loaded in the decade. Additionally, some offsetting revenue is raised through one-time tax holidays, such as on foreign earnings and/or carried interest income.
- The tax cuts disproportionately benefit higher-income households, which have a lower propensity to spend additional income.
- The legislation passes in 2017, and tax cuts are implemented at the start of 2018.

2.2 ANALYZING THE TAX POLICY SCENARIO

We quantified the impacts of tax policy changes within the framework of Oxford Economics' Global Economic Model. In this framework, tax reductions stimulate economic activity in the short-term because increased disposable (after-tax) income for households would increase private consumption (consumer spending); additionally, business investment and hiring would increase in anticipation of stronger economic activity and consumption growth, and higher after-tax returns on investment. Increased economic activity would support additional wages and salaries, further boosting consumption, and generating demand for additional production by domestic companies.

However, these positive effects would be moderated by several factors. Higher-income households are anticipated to spend only a portion of any direct tax cuts, limiting the short-term impacts on consumer spending. Similarly, only a portion of corporate tax cuts are anticipated to be channelled to domestic investment. Separately, lower tax rates would reduce tax revenues. The net reduction in tax revenue, only partly offset by government spending cuts and stronger economic growth, would increase the Federal deficit. Government borrowing to fund the larger deficit would increase interest rates, partly crowding out private investment.

[1] We conducted our macroeconomic analysis based on assumptions as of October 5, 2017.

Also, in anticipation of the effects of fiscal stimulus, the Federal Reserve would be expected to increase interest rates more quickly to manage inflation risks. Higher interest rates would cause the US dollar to strengthen, slowing exports and increasing imports, dampening domestic production.

2.3 IMPACTS TO US ECONOMY

The impacts to the US economy in the two scenarios are presented in Fig. 2 and summarized as follows.

- **No Tax Cut Scenario:** Assumes no change to existing tax policy. GDP growth moderates to 2.0% in 2018, before gradually slowing to 1.5% by 2022. GDP growth over these five years averages 1.7%, with inflation at 1.6%.
- **$1.5 Trillion Tax Cut Scenario:** Assumes $1.5 trillion of net tax cuts over ten years. GDP growth accelerates to 3.0% in 2018, and then slows. By 2020, GDP *growth* is slower than in the No Tax Cut Scenario; however, the *level* of GDP is higher throughout the period (0.7% higher on average relative to the No Tax Cut Scenario). On average during the five-year period, real personal disposable income in the $1.5 Trillion Tax Cut Scenario is 1.6% higher than in the No Tax Cut Scenario, and real consumer spending is 1.2% higher.

We have focused on the first five years following implementation of tax policy changes as the period during which the effects of such policy changes can be most accurately analyzed.

Fig. 2 Impact to US economy: $1.5 Trillion Tax Cut Scenario

	2018	2019	2020	2021	2022	Average
Growth rates						
GDP, real						
No Tax Cut	2.0%	1.7%	1.7%	1.6%	1.5%	1.7%
$1.5 Trillion Tax Cut	3.0%	2.0%	1.2%	1.3%	1.5%	1.8%
Inflation (price index growth)						
No Tax Cut	1.6%	1.6%	1.6%	1.6%	1.7%	1.6%
$1.5 Trillion Tax Cut	1.6%	1.7%	2.0%	2.2%	2.3%	2.0%
Difference in levels relative to No Tax Cut Scenario						
GDP, real	1.0%	1.2%	0.7%	0.4%	0.4%	0.7%
Personal income, disposable, real	1.5%	1.9%	1.7%	1.5%	1.4%	1.6%
Consumer spending, real	1.1%	1.5%	1.4%	1.1%	0.9%	1.2%
Fixed investment, real	1.8%	1.9%	0.4%	-0.2%	-0.2%	0.7%
Difference in level of interest rates relative to No Tax Cut Scenario (in basis points)						
Interest rate, 10-year gov. bonds	56	106	91	68	65	77
Interest rate, corporate borrowing	59	91	67	46	45	61

Note: Inflation is based on private consumption expenditure deflator.

Source: Oxford Economics

3. IMPACT ON THE LODGING SECTOR

Increased economic activity in the $1.5 Trillion Tax Cut Scenario would benefit hotels and the broader travel sector. Households would have more to spend on travel, not just because of lower personal income taxes, but also because of broader increases in employment, and wages and salaries, stemming from increased economic activity. As consumer spending increases, discretionary categories, such as travel, would benefit disproportionately relative to areas such as housing and utilities. In an environment of stronger economic growth, consumer and business confidence would improve. Meanwhile, increased business activity and investment would support stronger business travel, both in the transient segment and in the group segment. Many categories of business travel represent a form of business investment, such as employee training and meetings with customers, and would be expected to increase initially as businesses respond to the stronger economy.

We have analyzed the potential impacts to the lodging sector in a framework that includes hotel supply, demand (occupied room nights) and price effects linked to economic drivers. To report the results in a summary format, we have focused on demand, average daily rate (ADR), and room revenue in real dollars.

As shown in Fig. 3, we estimate hotel demand growth would accelerate to 3.1% in 2018 in the $1.5 Trillion Tax Cut Scenario, supporting a 3.0% increase in ADR (in nominal dollars), and a 4.5% increase in room revenue (in real dollars). Similar to the broader economy, the impact to the pace of growth would gradually slow, but overall, room revenue in the $1.5 Trillion Tax Cut Scenario would average 2.1% higher than in the No Tax Cut Scenario.

Fig. 3 Impact to US lodging industry: $1.5 Trillion Tax Cut Scenario

	2018	2019	2020	2021	2022	Average
Lodging industry, growth rates						
Demand						
No Tax Cut	1.7%	1.9%	2.1%	1.9%	1.9%	1.9%
$1.5 Trillion Tax Cut	3.1%	2.2%	1.5%	1.5%	1.8%	2.0%
ADR, nominal						
No Tax Cut	2.3%	2.2%	2.2%	2.2%	2.1%	2.2%
$1.5 Trillion Tax Cut	3.0%	3.0%	2.4%	2.5%	2.6%	2.7%
Room revenue, real						
No Tax Cut	2.4%	2.5%	2.7%	2.5%	2.2%	2.5%
$1.5 Trillion Tax Cut	4.5%	3.5%	1.9%	1.7%	2.1%	2.7%
Lodging industry, difference in levels relative to No Tax Cut Scenario						
Demand	1.5%	1.8%	1.2%	0.8%	0.7%	1.2%
ADR, nominal	0.7%	1.4%	1.6%	1.9%	2.5%	1.6%
Room revenue, real	2.1%	3.1%	2.3%	1.6%	1.4%	2.1%

Source: Oxford Economics

Increased demand at hotels would support hiring of new employees, and additional shifts for existing hourly employees. This would expand the wages and salaries paid by hotels. As a result, hotels and hotel employees would tend to pay higher levels of state and local taxes, including income and sales taxes. Also, increased volumes of hotel guests would generate increased spending in local communities, such as at local stores, restaurants, and attractions. Stronger demand would also tend to support moderate ADR increases in the short term, given the lags inherent in constructing new hotels. This would also contribute to higher occupancy tax revenues, as well as other local tax revenue, such as sales tax receipts.

Direct hotel industry impacts in the $1.5 Trillion Tax Cut Scenario are summarized in Fig. 4. We have provided two sections for direct spending.

- **Hotel guest spending:** represents the majority of the direct spending impact, and includes spending onsite at hotels as well as ancillary spending, such as at restaurants, retail stores and transportation providers.
- **Direct spending:** represents direct hotel guest spending plus capital investment in hotels, such as renovations and construction of new hotels.

Overall, in the $1.5 Trillion Tax Cut Scenario, cumulative direct hotel guest spending would be $57.4 billion higher than in the No Tax Cut Scenario over the five-year period. Direct wages, salaries and other labor income at hotels, the businesses benefiting from guest spending, and construction-sector firms, would be $11.0 billion higher than in the No Tax Cut Scenario over the five-year period. The wage, salary and other labor income impact, which would represent additional earnings by existing employees, as well as new hires, would be equivalent to the annual compensation of 55,300 employees for five years. Direct state and local taxes would be $2.5 billion higher than in the No Tax Cut Scenario over the five-year period.

Fig. 4 Direct hotel industry economic impacts: $1.5 Trillion Tax Cut Scenario

Monetary amounts in billions of real 2015 dollars

	2018	2019	2020	2021	2022	Average	Cumulative
Direct impacts, difference relative to No Tax Cut Scenario							
Hotel guest spending (onsite at hotels and ancillary), real	$11.0	$16.7	$12.6	$8.8	$8.3	$11.5	$57.4
Direct spending (hotel guest spending and capital investment in hotels), real	$11.7	$17.8	$13.4	$9.4	$8.8	$12.2	$61.1
Wages, salaries and other labor income, real	$2.1	$3.2	$2.4	$1.7	$1.6	$2.2	$11.0
State and local taxes, real	$0.5	$0.7	$0.6	$0.4	$0.4	$0.5	$2.5

Note: Direct spending is also referred to as direct output (business sales). Direct wages, salaries and other income is also referrred to as direct labor income.

Source: Oxford Economics

Increased hotel guest spending and capital investment in hotels would support broader indirect and induced economic impacts (Fig. 5), such as through spending by hotel employees, and through purchases by hotels of inputs from suppliers. Overall, in the $1.5 Trillion Tax Cut Scenario, the increased total economic impacts of the hotel industry relative to the No Tax Cut Scenario would include $22.3 billion of cumulative labor income over the five-year period (equivalent to the annual compensation of 94,700 employees for five years), and $3.9 billion of additional state and local tax revenues.

Fig. 5 Total hotel industry economic impacts: $1.5 Trillion Tax Cut Scenario

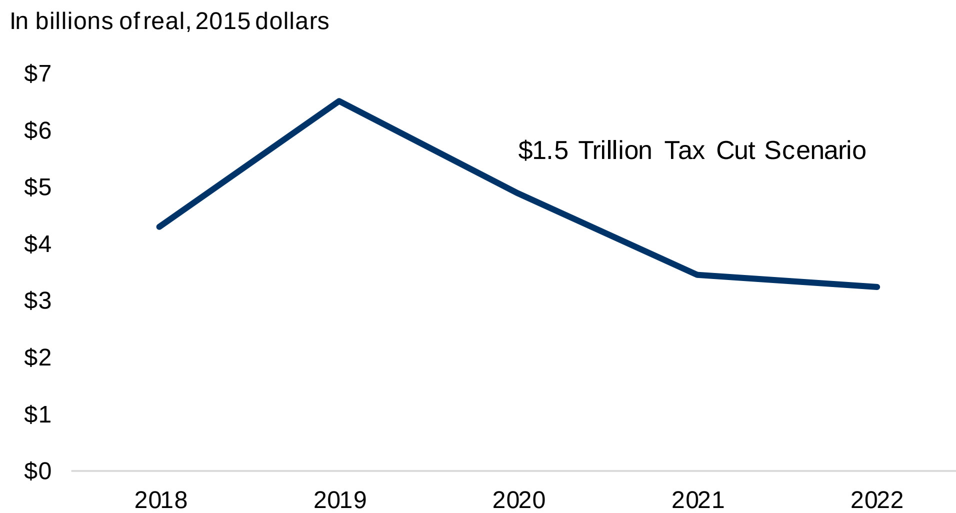
Monetary amounts in billions of real 2015 dollars
Total hotel industry impacts include direct impacts (hotel operations, guest ancillary spending, and capital investment) as well as indirect and induced impacts

	2018	2019	2020	2021	2022	Average	Cumulative
Total industry impacts, difference relative to No Tax Cut Scenario							
Output (business sales), real	$25.2	$38.4	$28.8	$20.2	$19.1	$26.3	$131.7
Wages, salaries and other labor income, real	$4.3	$6.5	$4.9	$3.4	$3.2	$4.5	$22.3
State and local taxes, real	$0.7	$1.1	$0.8	$0.6	$0.6	$0.8	$3.9

Note: Total wages, salaries and other income is also referrred to as total labor income.
Source: Oxford Economics

The total impact to labor income in the $1.5 Trillion Tax Cut Scenario by year is shown graphically in Fig. 6. The peak impact is anticipated in 2019, with $6.5 billion of additional labor income.

Fig. 6 Total hotel industry labor income impact relative to No Tax Cut Scenario



Source: Oxford Economics

November 9, 2017

The modelling and results presented here are based on information provided by third parties, upon which Oxford Economics has relied in producing its report and forecasts in good faith. Any subsequent revision or update of those data will affect the assessments and projections shown.

For further information:

Adam Sacks adam.sacks@oxfordeconomics.com
Aran Ryan aran.ryan@oxfordeconomics.com

Oxford Economics
303 W. Lancaster Ave, Suite 2E, Wayne, PA 19087
Tel: +1 610-995-9600