



# Tourism in Iceland: Modest angle of attack

Arion Research  
13 September 2019



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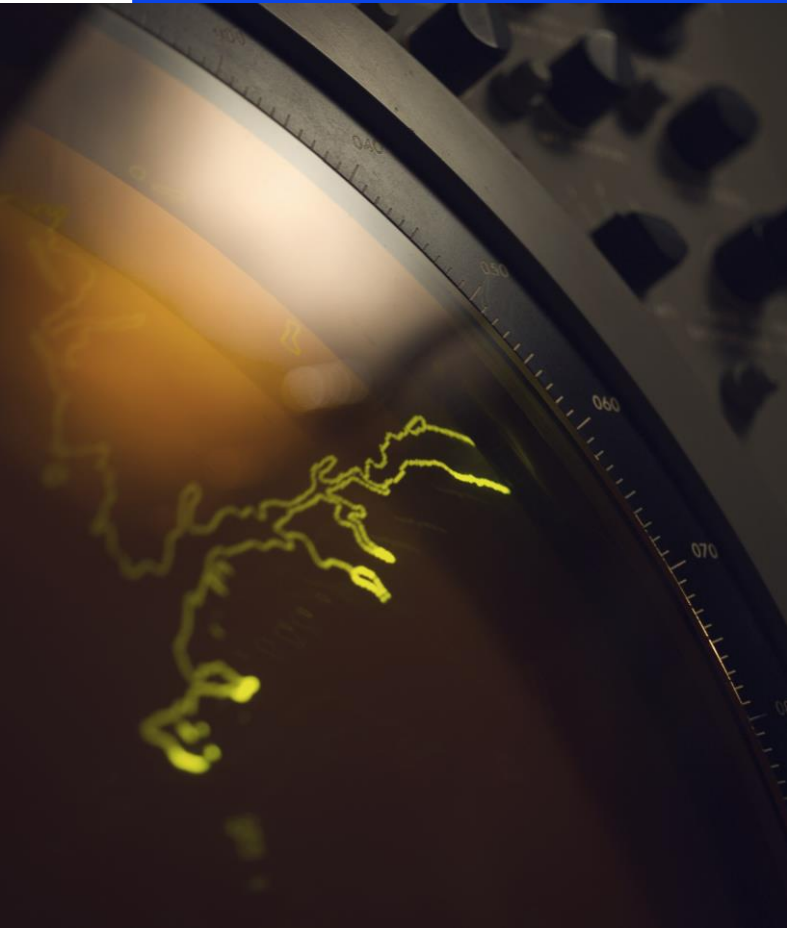
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# Main Findings

- The number of tourists to Iceland has declined by roughly 13% YoY in 2019. A **change in Icelandair's passenger mix** has mitigated the effect of WOW air bankruptcy on the number of tourists. **YTD number of passengers travelling with Icelandair to Iceland rose by 30% YoY** while total number of passengers only rose by 11%.
- Based on Isavia's winter schedule, **we expect 20% YoY decline in the number of available seats, flying to and from Iceland, this coming winter.**
- We expect tourism in Iceland to recover gradually following WOW air's bankruptcy. **Our base case assumes 2% growth in number of tourists in 2020. Grounding of Boeing MAX 8 aircrafts hinders Icelandair's growth ambitions in 2018 and 2019.** Stronger growth in number of tourists mostly rests on whether a new airline or airlines begin operations.
- **On average each tourist visiting Iceland in 2019 has stayed greater number of nights and spent more money**, whether in ISK or in their own currency. Therefore, **contraction in the tourist sector is likely to be less severe** than we were concerned with at the beginning of the year. We highlight three contributing factors; progress has been made in attracting **more affluent tourists**, changes in **Icelandair's passenger mix** and more **reliable data** on number of actual overnight visitors.
- Increased **number of overnight stays** per visitor and growing demand for hotels has **cushioned the effect of fewer tourists on the accommodation market.** However overnight stays in Airbnb have declined significantly as well as overnight stays in vehicles. Surveys show that visitors travelling with WOW air spent on average a shorter period of time in Iceland and were more likely to stay in hostels and apartments than other visitors.
- **The average price of an overnight stay in a hotel room in Reykjavík this summer declined YoY**, and the occupancy ratio has come down, causing revenue per room to contract considerably.
- Depreciation of the ISK has alleviated the effect of fewer tourists **as Iceland no longer holds the top spot on the list of the most expensive countries to visit.**
- The demise of WOW air and subsequent contraction in number of tourists has caused number of tourist related jobs to contract. Despite that **net migration to Iceland could exceed 4,000 people in 2019.** Fewer jobs coupled with a growing work force **increases competition in the labor market** and contributes to a growth in unemployment.
- There is a strong seasonality in the Icelandic labor market, especially in number of tourism related jobs. **We expect that at the end of 2019 tourism related jobs will be around 2,000 fewer than at the end of 2018** and that unemployment rate will climb to around 4% by the end of the year.





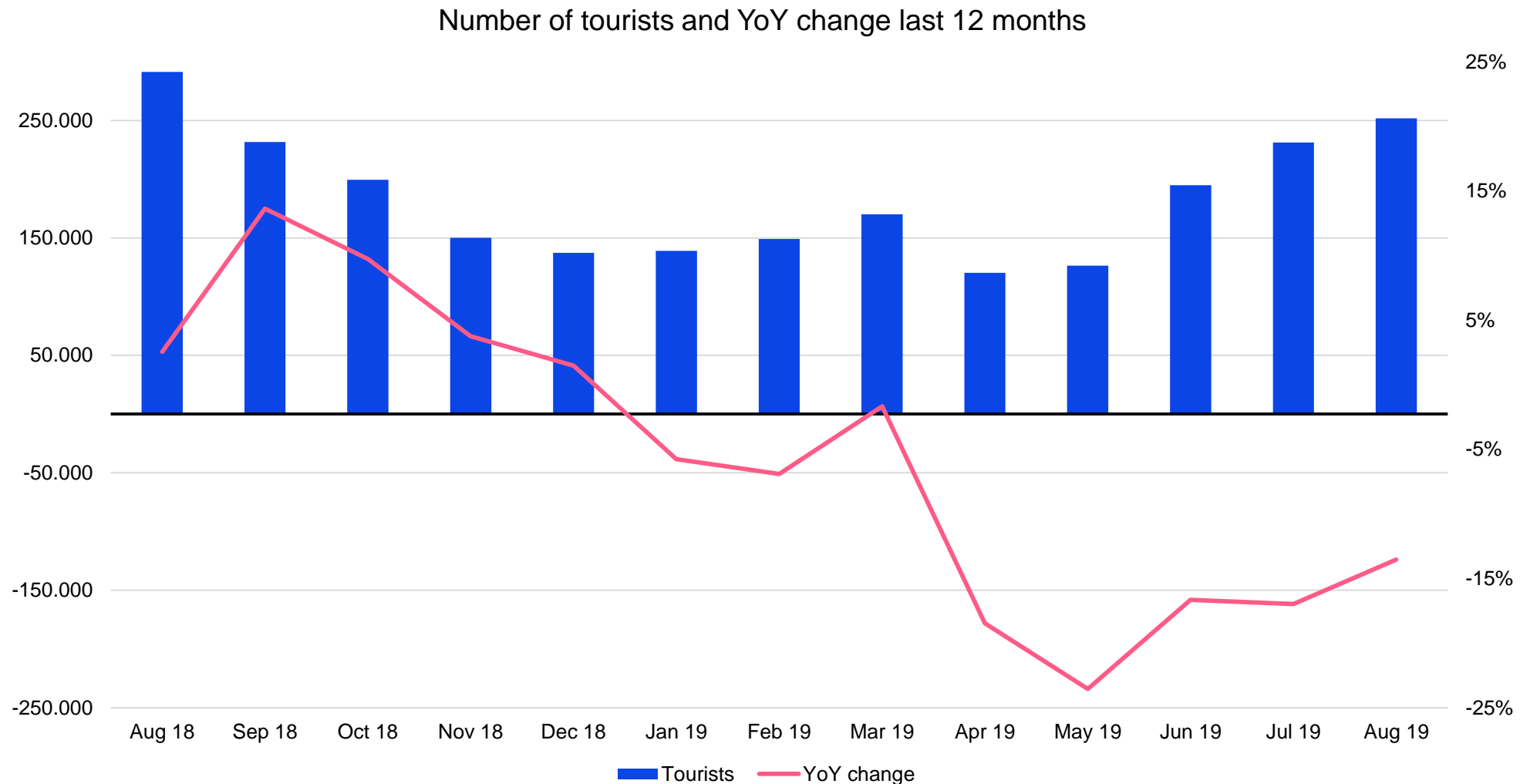
# Foggy skies

Development after WOW air's collapse and tourist arrival scenarios



# 17% decrease in tourism since WOW air's collapse

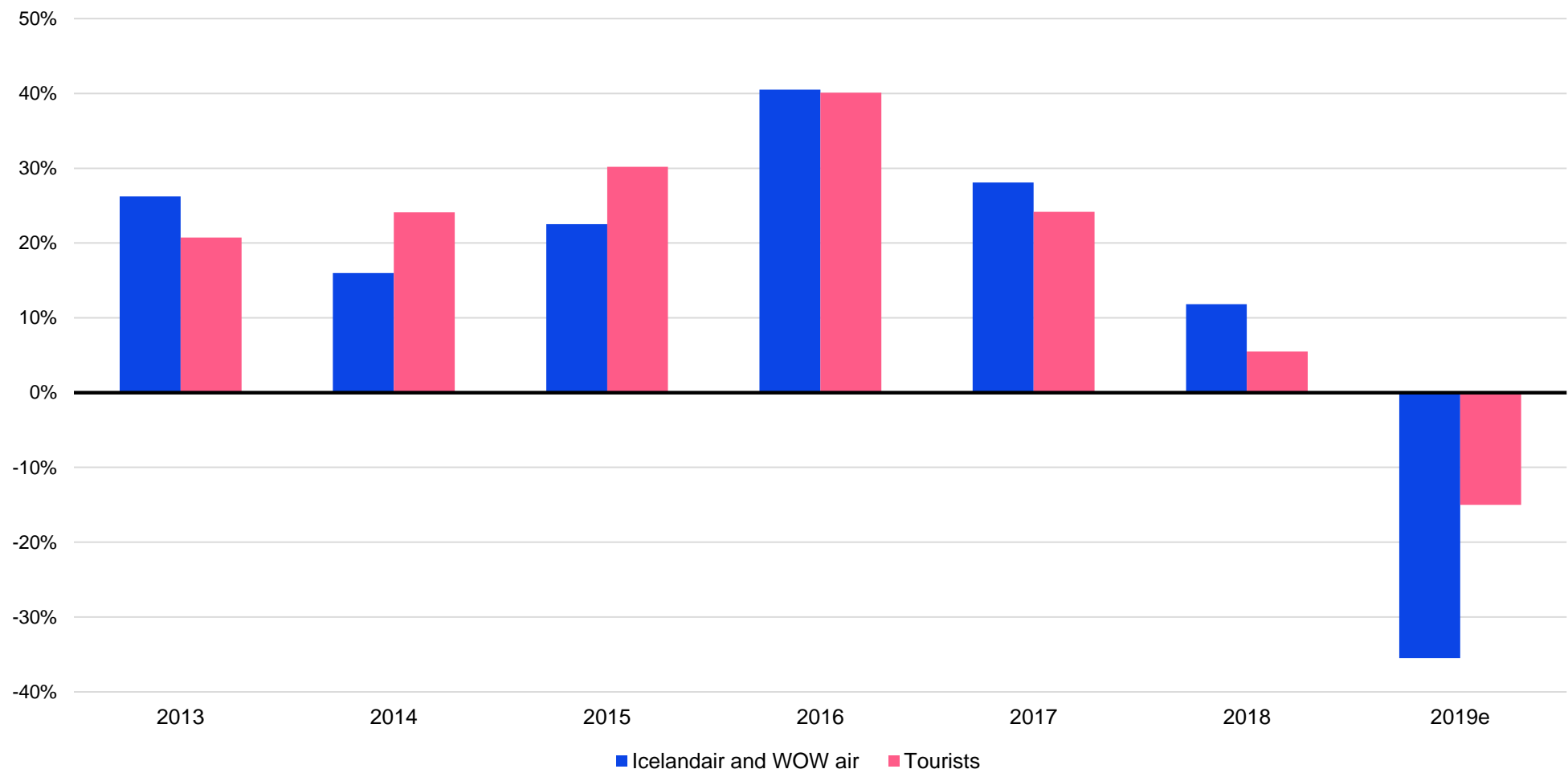
Number of tourists began to decline in the beginning of the year, as WOW air had already reduced its fleet by roughly half before its operations stopped in late March



## In recent years tourism has moved in tandem with changes in the Icelandic airlines capacity

However, the relationship does not appear to be as strong this year as it has been. Following WOW air's collapse, the outlook is for a 35% YoY decrease in total number of passengers flying with Icelandic carriers while we are only estimating a 15% decline in tourist arrivals this year.

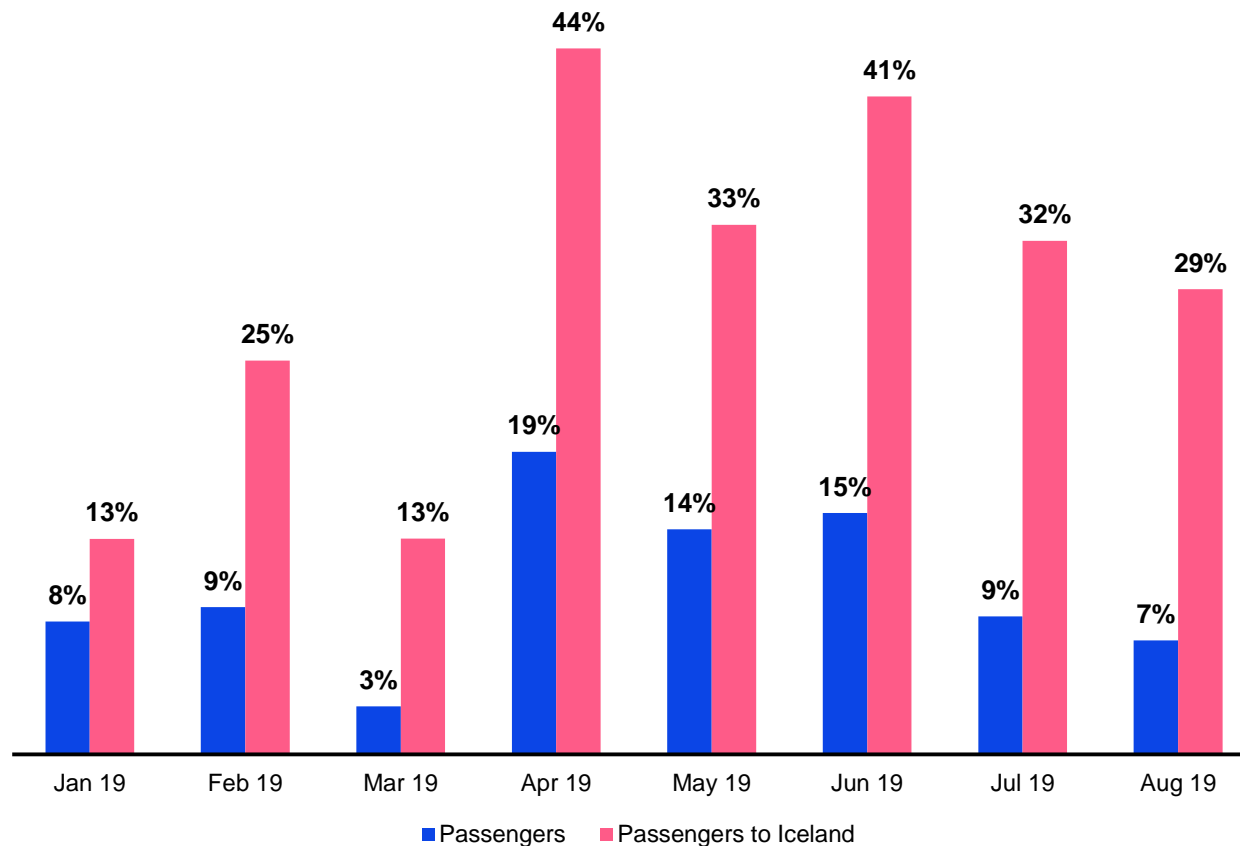
Icelandair and WOW air capacity growth and tourist arrivals via KEF airport



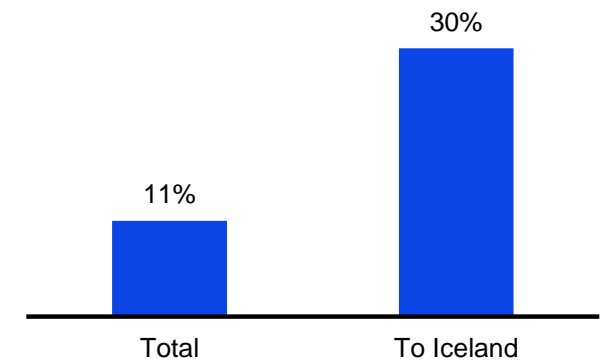
# Why have we not seen greater decline in tourist arrivals?

Mainly because Icelandair's passenger mix has changed significantly from last year. Passengers travelling **to Iceland** with Icelandair have increased by 30% YoY, while **total passengers** in Icelandair's route network has increased by 11%

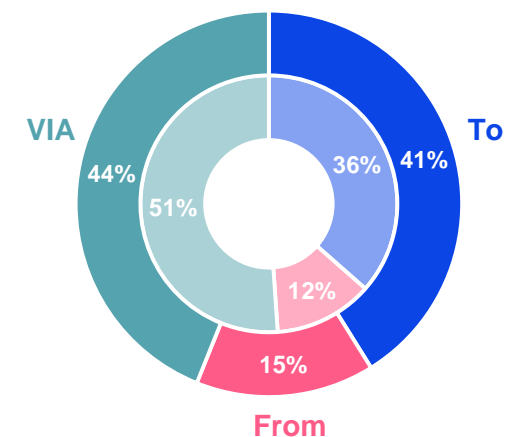
YoY growth in Icelandair's route network  
- YTD



YoY growth  
- YTD

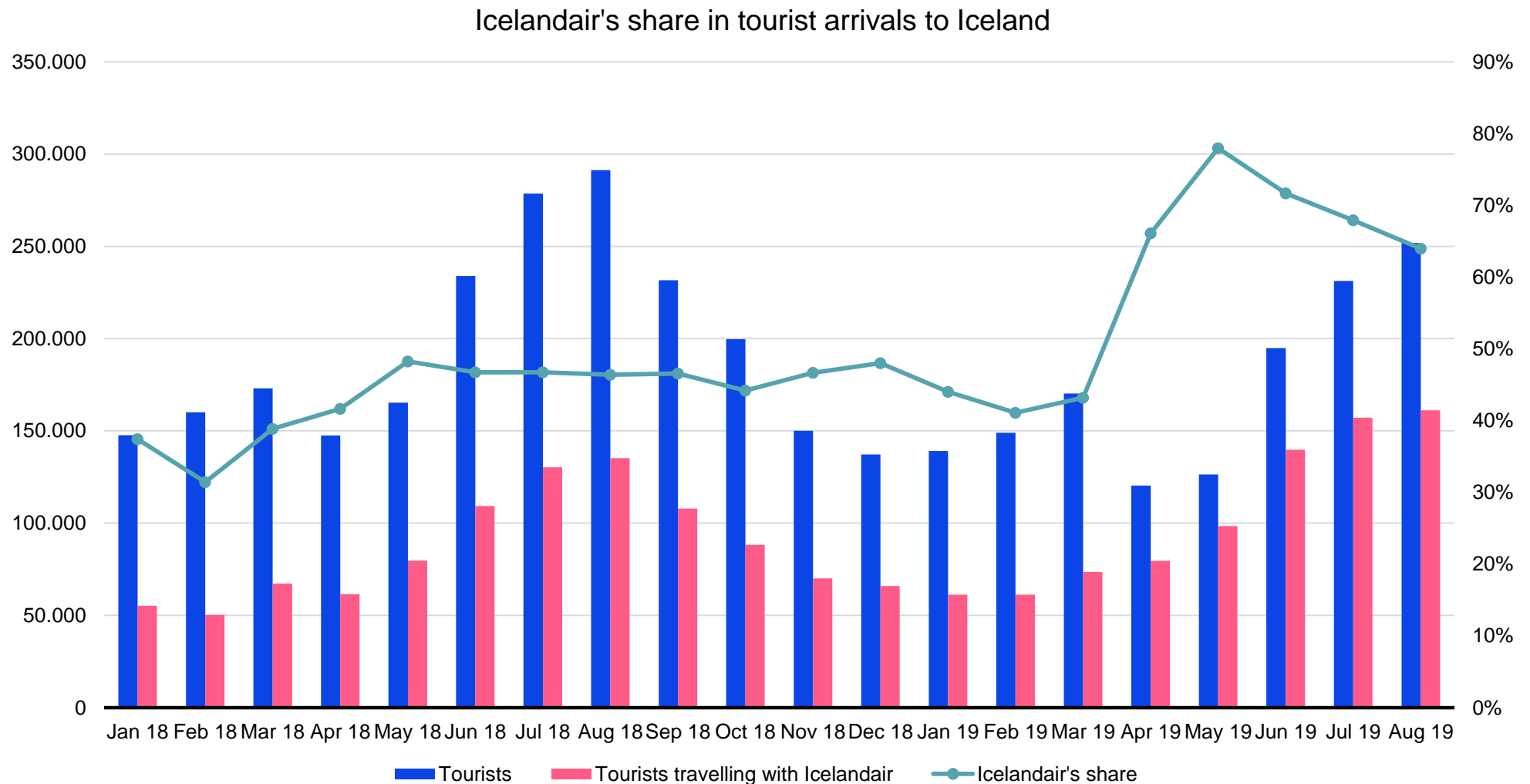


Icelandair's passenger mix  
- inner circle 2018, outer 2019



# Since WOW air's collapse, two out of three tourists have travelled with Icelandair

Icelandair's share in tourist arrivals was 40-50% when WOW air's fleet was at its peak



Sources: Icelandair, Icelandic Tourist Board, Arion Research.

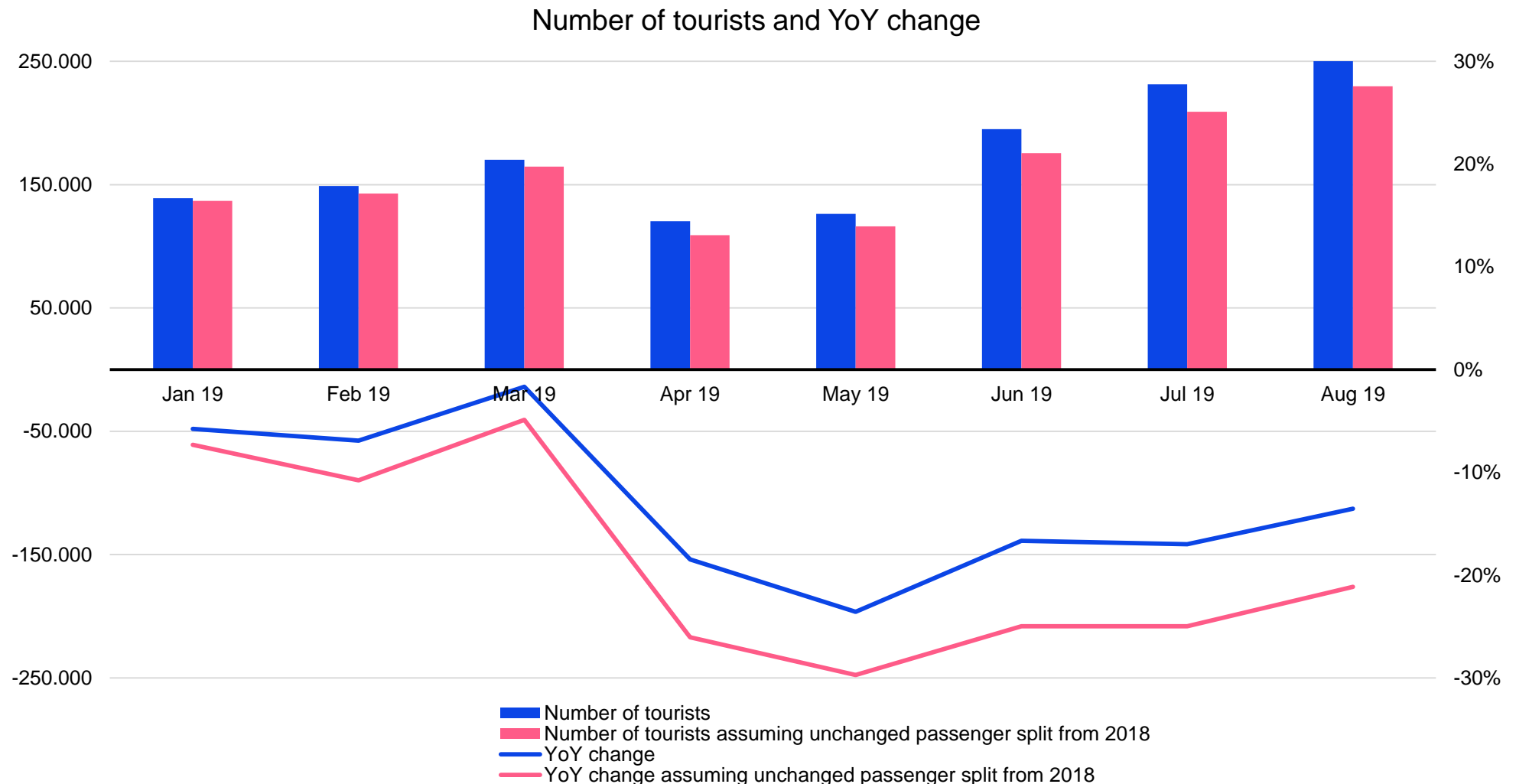
\*Assuming that every passenger travelling to Iceland with Icelandair is a tourist as well as 25% of VIA passengers, which historically have used the company's „Stopover“ concept





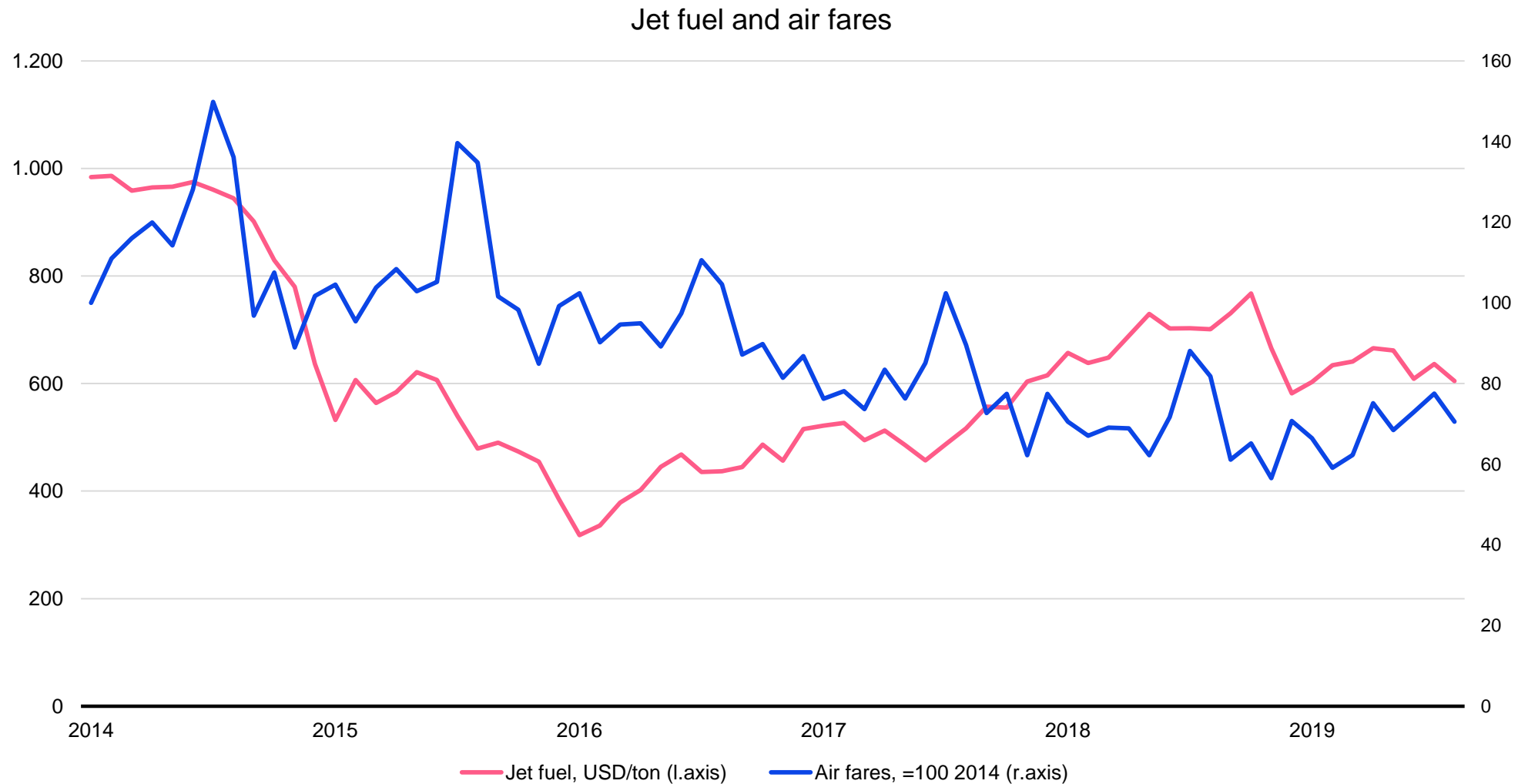
# What if Icelandair's passenger mix had remained unchanged?

If it hadn't been for the shift in Icelandair's passenger mix, we assume that tourists YTD would have been around 100 thousand fewer than what we have seen so far. The YTD decline would thus have been around 20% instead of 13%.



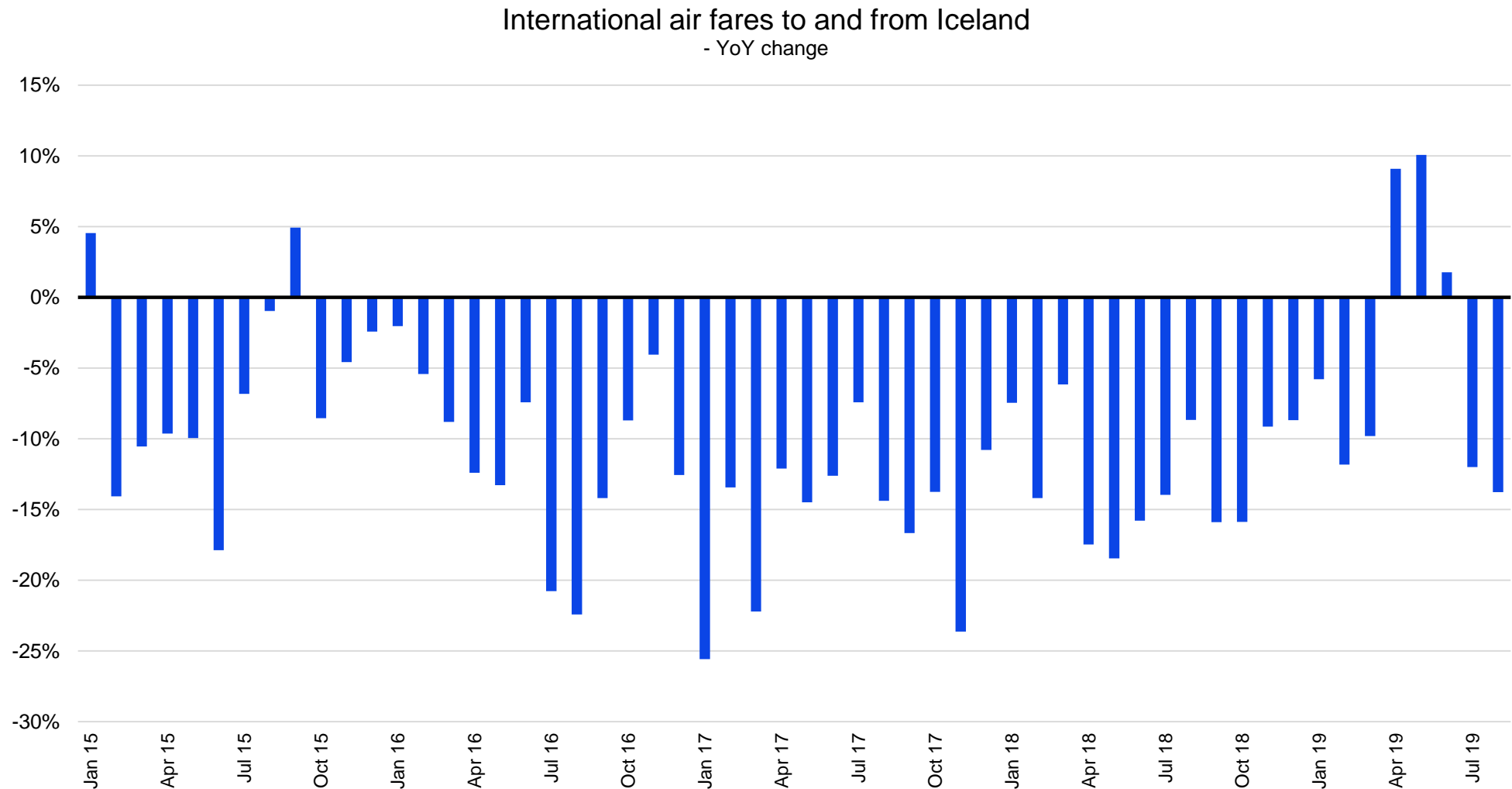
# Airlines external environment has been relatively stable this year. Key question is whether air fares continue their downward long-term trajectory?

Statistics Iceland's latest measurements suggest that seasonal fluctuation in air fares is diminishing



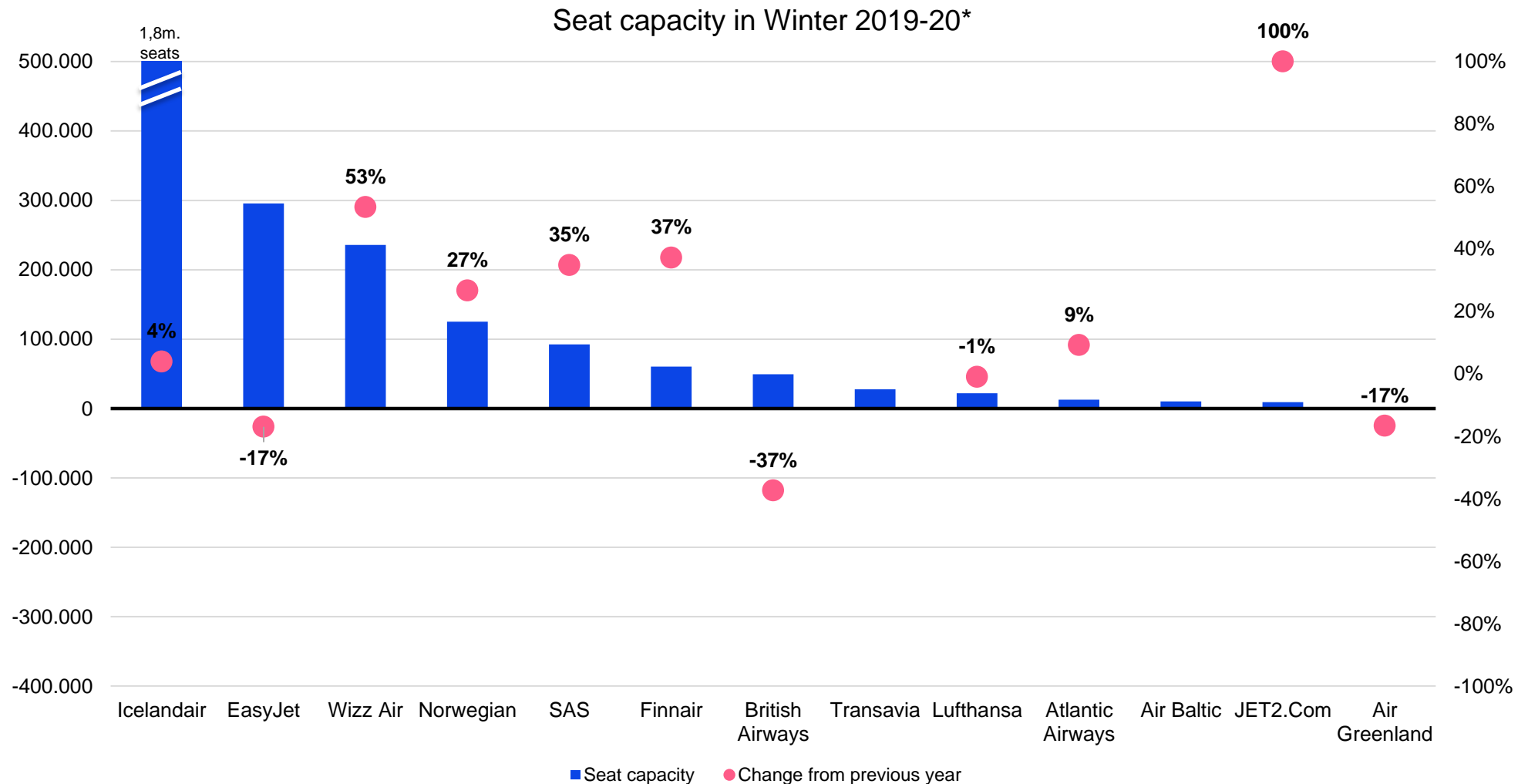
# Air fares: 42 months down, 3 months up...then down again

In the first three months after WOW air's collapse, air fares increased YoY. However, in July they returned to the same old declining trend according to Statistics Iceland



# 7% increase in seat capacity from non-domestic carriers

Fourteen airlines have announced that they will offer scheduled flights to Iceland in the Winter 2019-20

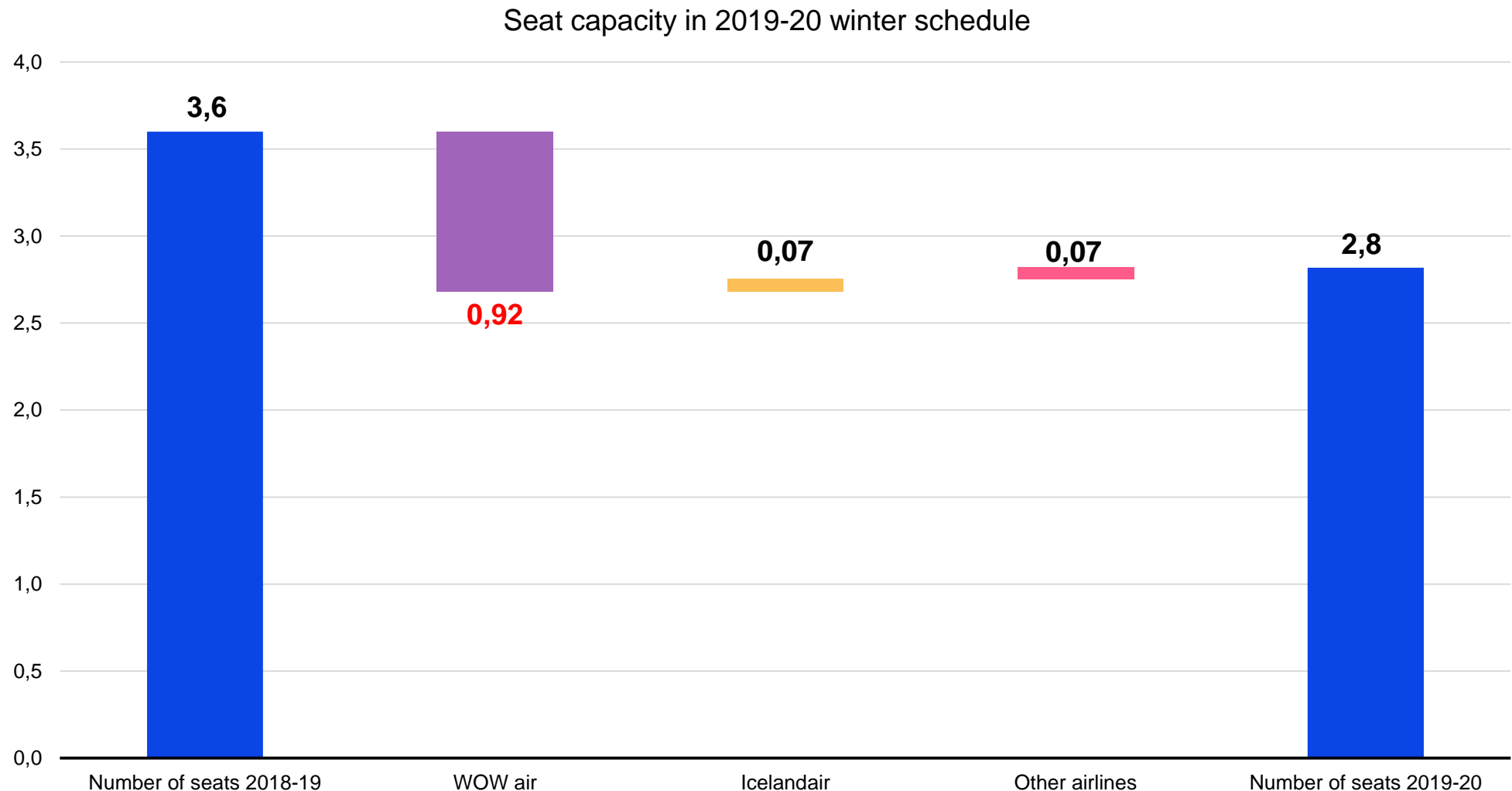


Sources: Isavia, Arion Research. \*Winter schedule is period from 1.11-31.3. Czech Airlines is missing in the chart above. The carrier announced daily flights from Keflavik airport to Prague with layover in Copenhagen. Possible seat capacity from new WOW air also missing



## Around 20% fewer seats available this winter

According to Isavia's Winter schedule. Space left behind by WOW air will only be met to a small extent.



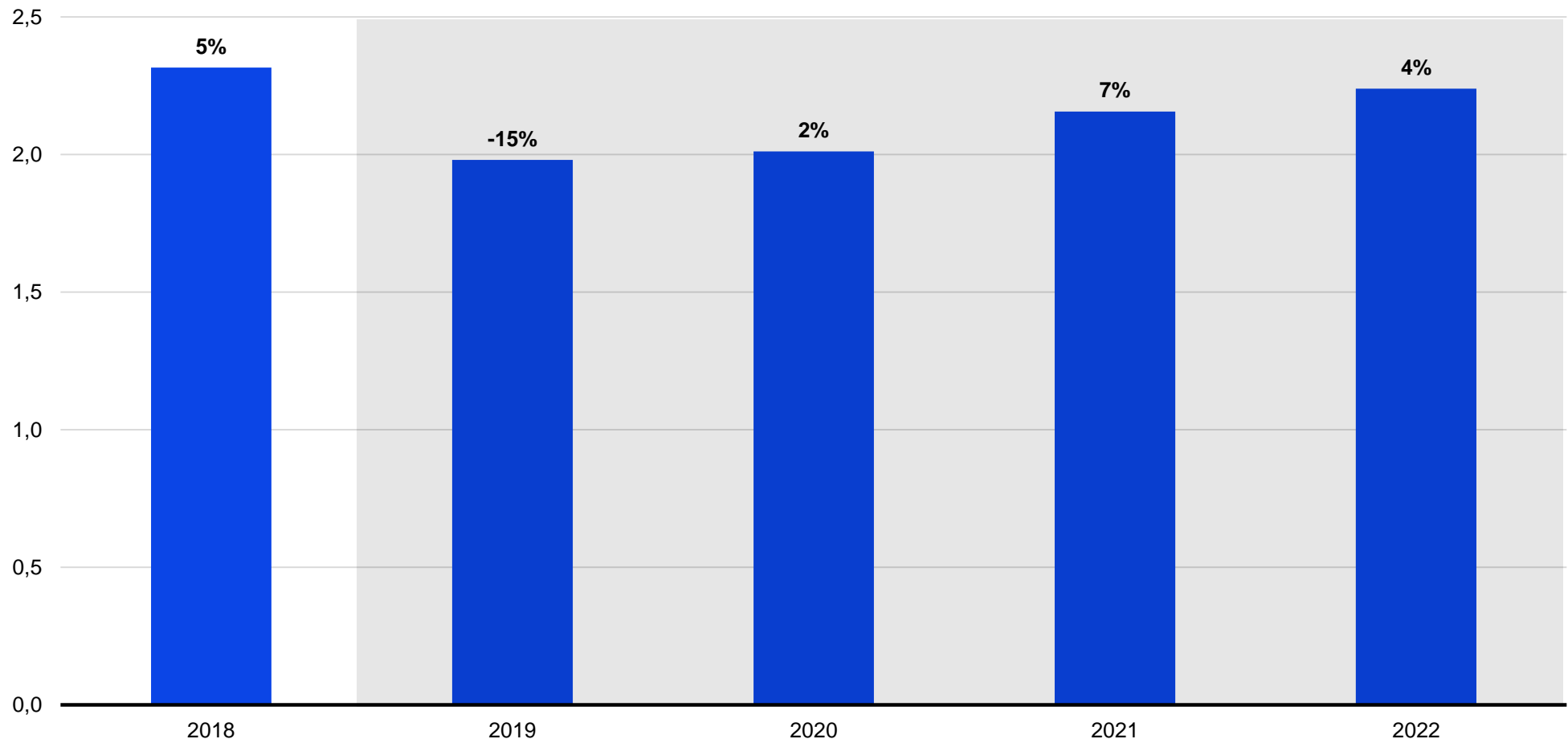
Sources: Isavia, Arion Research. \*Czech airlines seat capacity not included as mentioned on previous slide as well as possible seat capacity from new WOW air



## Our base case assumes slow start after the belly flop in March

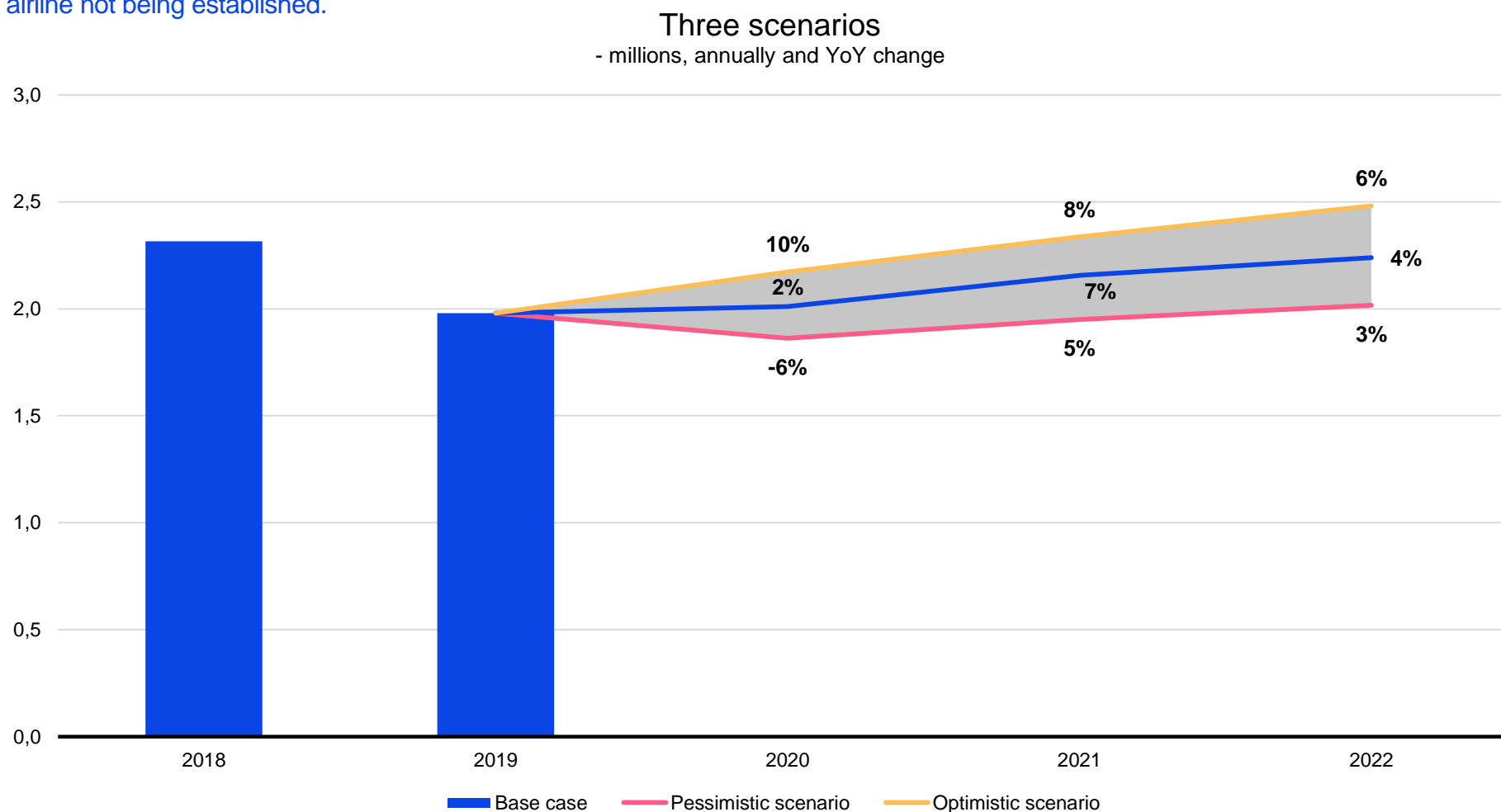
Based on airlines already operating. Even if the grounding of the B737 MAX aircrafts would be lifted soon, we expect delays in deliveries of new aircrafts to Icelandair. Thus, we assume a roughly unchanged capacity for Icelandair between 2019 and 2020.

Tourist arrivals via KEF airport  
- millions annually, % increase



# This time, there's more upside potential in our scenarios

Development in number of tourists this year has been in line with a pessimistic scenario provided in our 2018 report following the demise of WOW air. This time we feel that there is more upside potential than downside risk in our base case forecast. In our optimistic scenario, we are assuming that Icelandair will operate according to its original fleet plan in 2020 as well as WOW air will return to the air. However, in our pessimistic scenario, we assume that grounding of the B737 MAX aircrafts will last in to 2020 with Icelandair reducing capacity YoY as well as a new airline not being established.





## More affluent Tourists

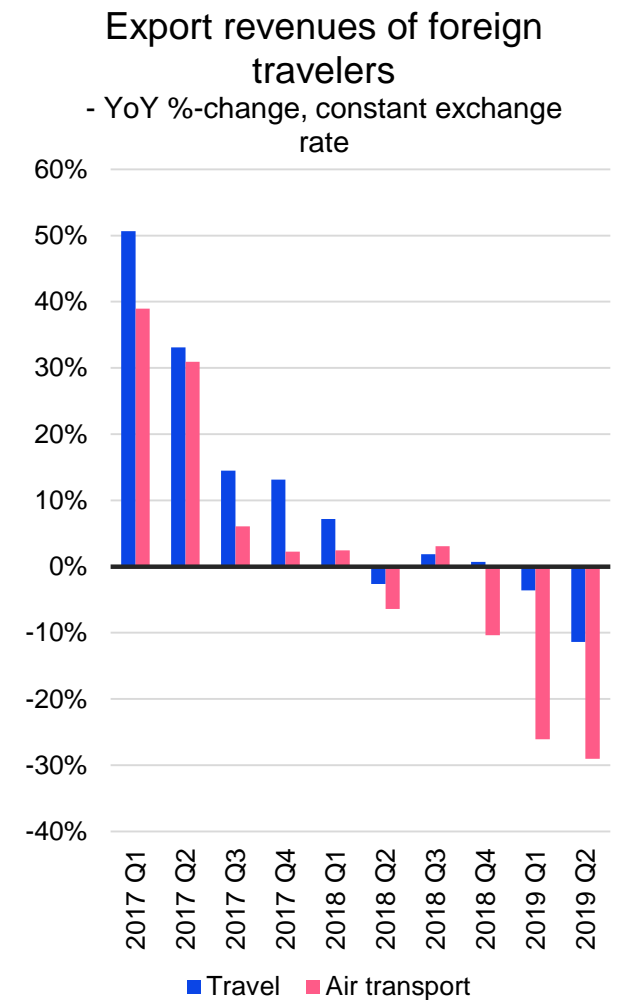
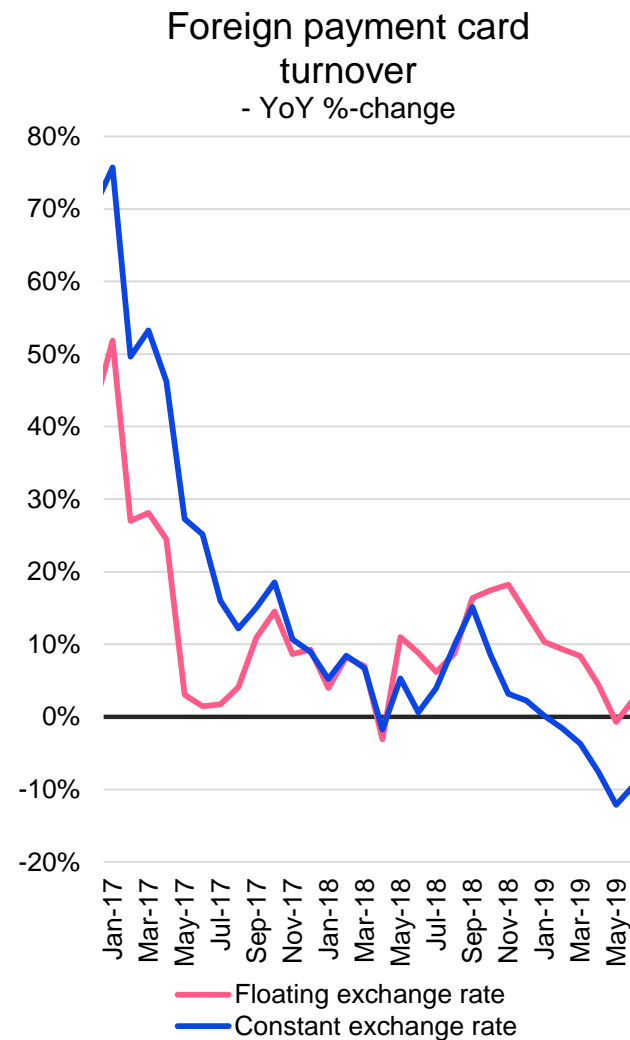
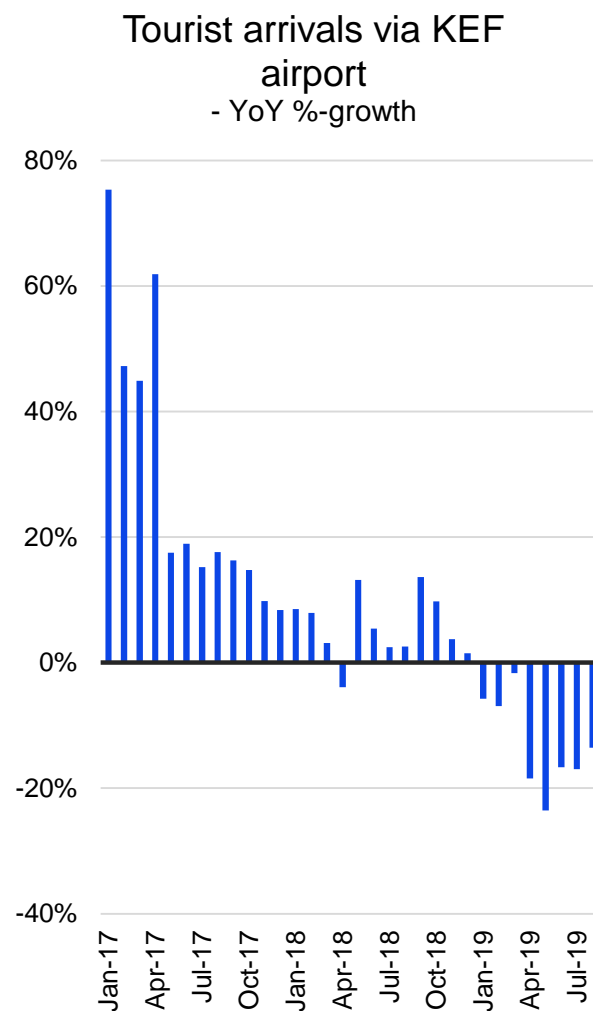
The mix of tourists seems to have changed recently, raising consumption per tourist considerably





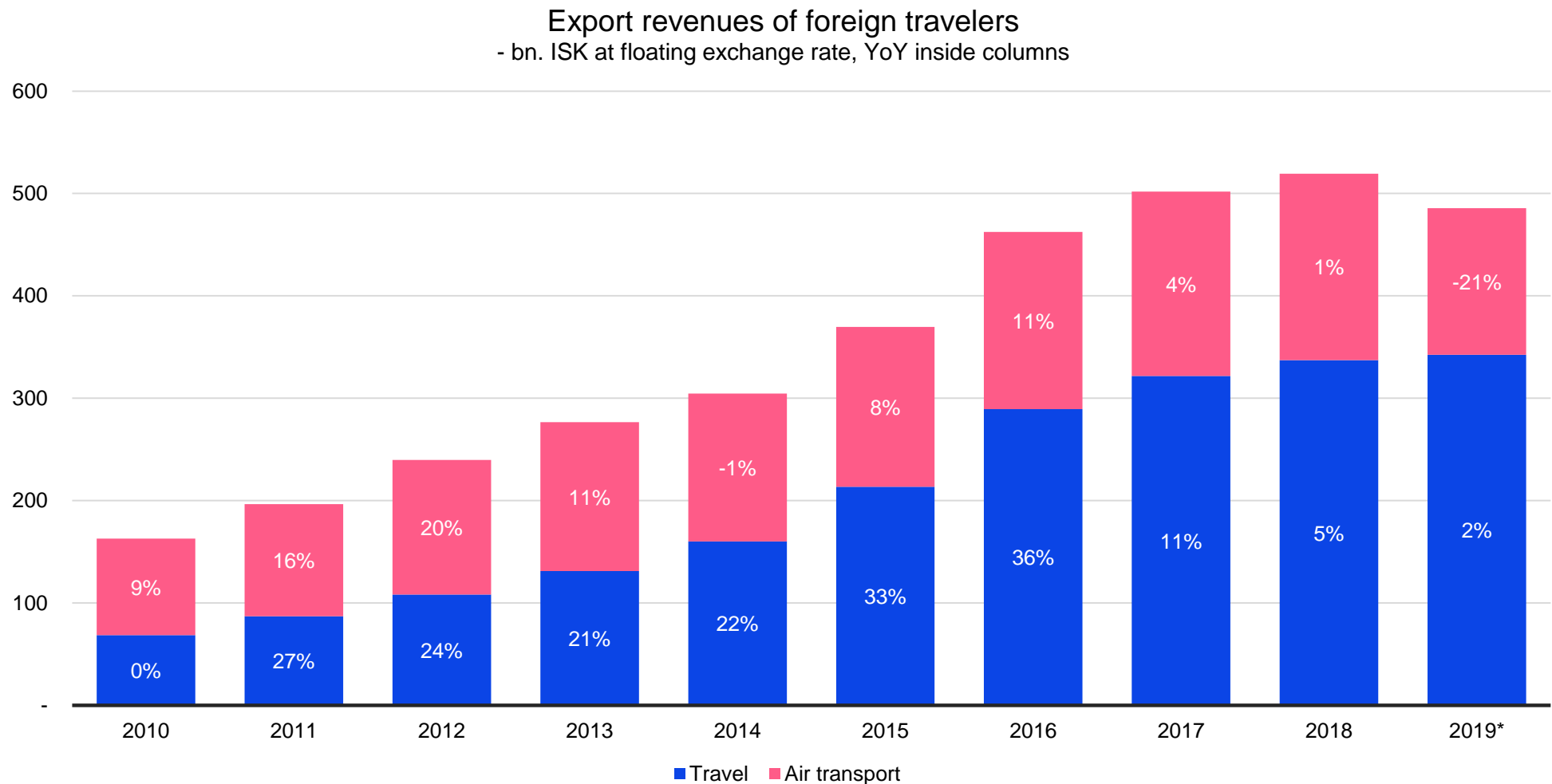
# Fewer tourists means less revenue

The number of tourists decreased by 13,4% YoY in the first eight months of the year. Export revenue from tourists in the service trade balance has decreased by 15% at a constant exchange rate mainly due to less revenue from air transport.

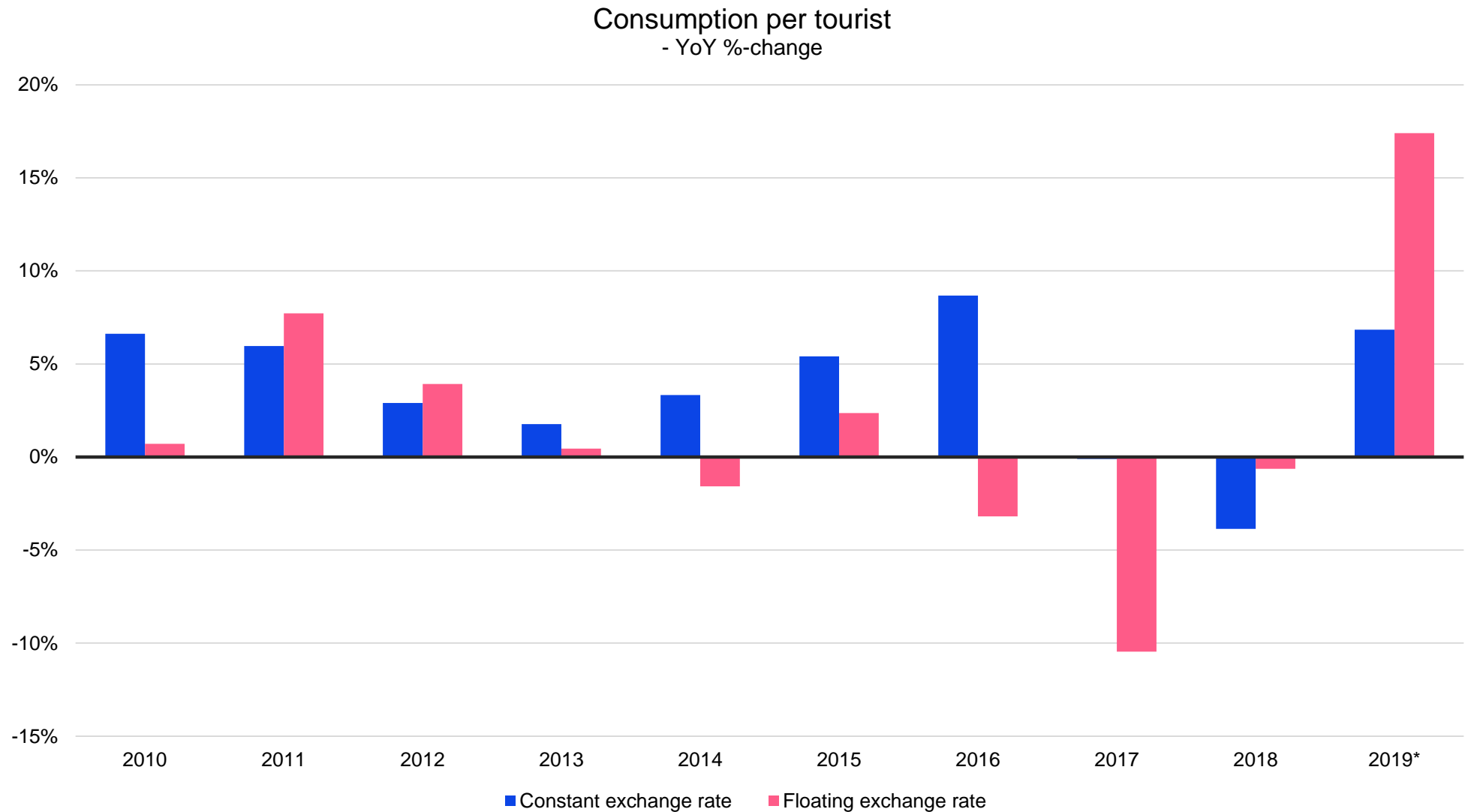


# Total consumption of tourists has increased in ISK

Total export revenues from foreign travelers has not decreased much in ISK. Putting air transport aside consumption of tourists has increased in ISK despite 13,4% fewer tourists!



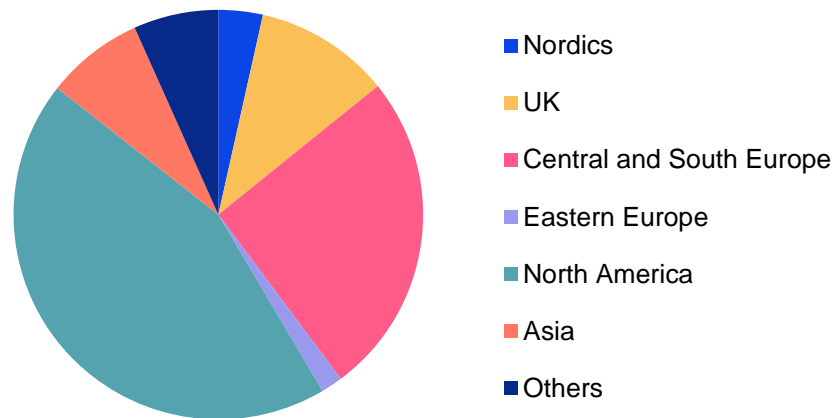
# Consumption per tourist has increased considerably



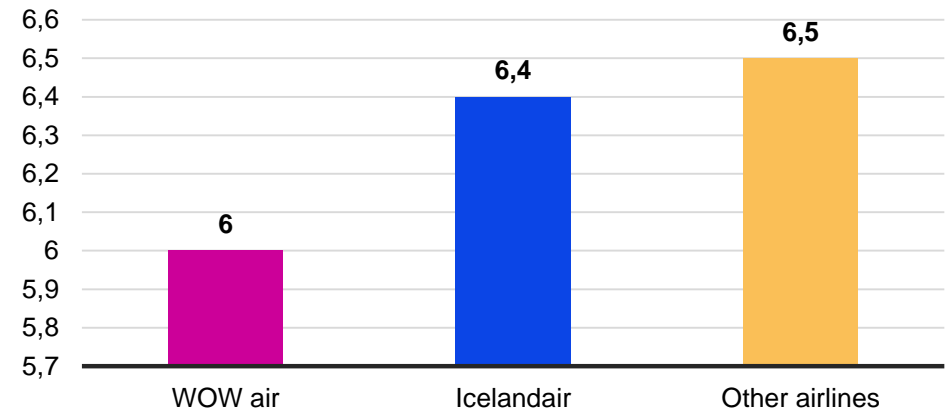
# What differentiated tourists flying with WOW air

A big part of them were from North America, they stayed slightly shorter than others, stayed more in hostels and Airbnb and spent less overall than tourists flying with other airlines.

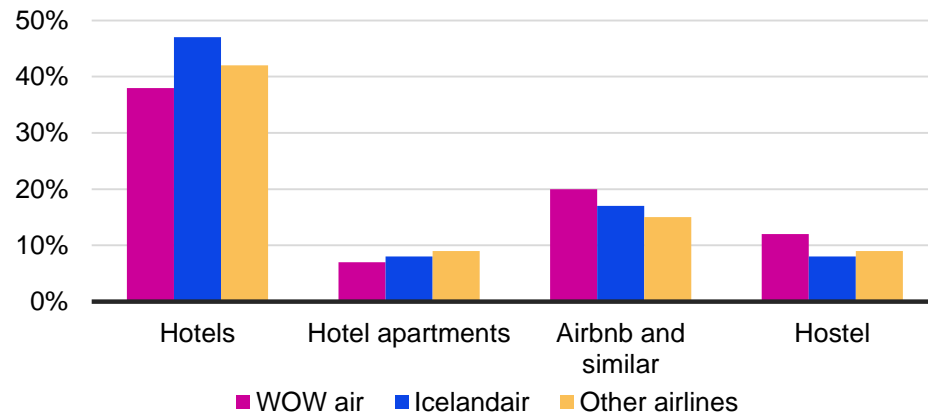
Nationality of tourists traveling with WOW air



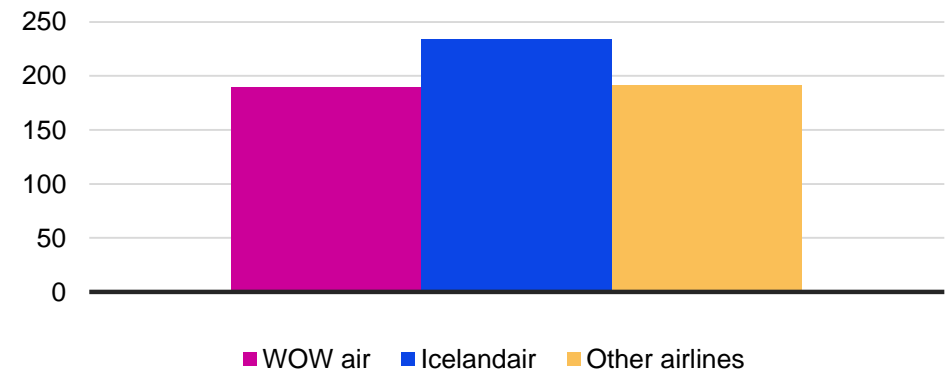
Average number of overnight stays



Type of accommodation by tourists



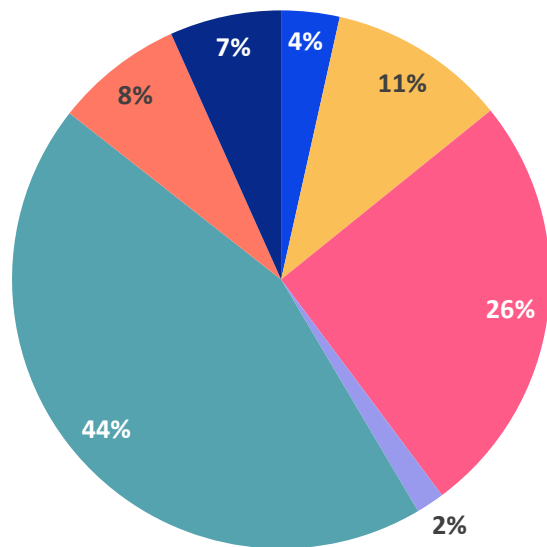
Average spending per tourist  
- thous. ISK



# More reduction in the number of tourists from North America

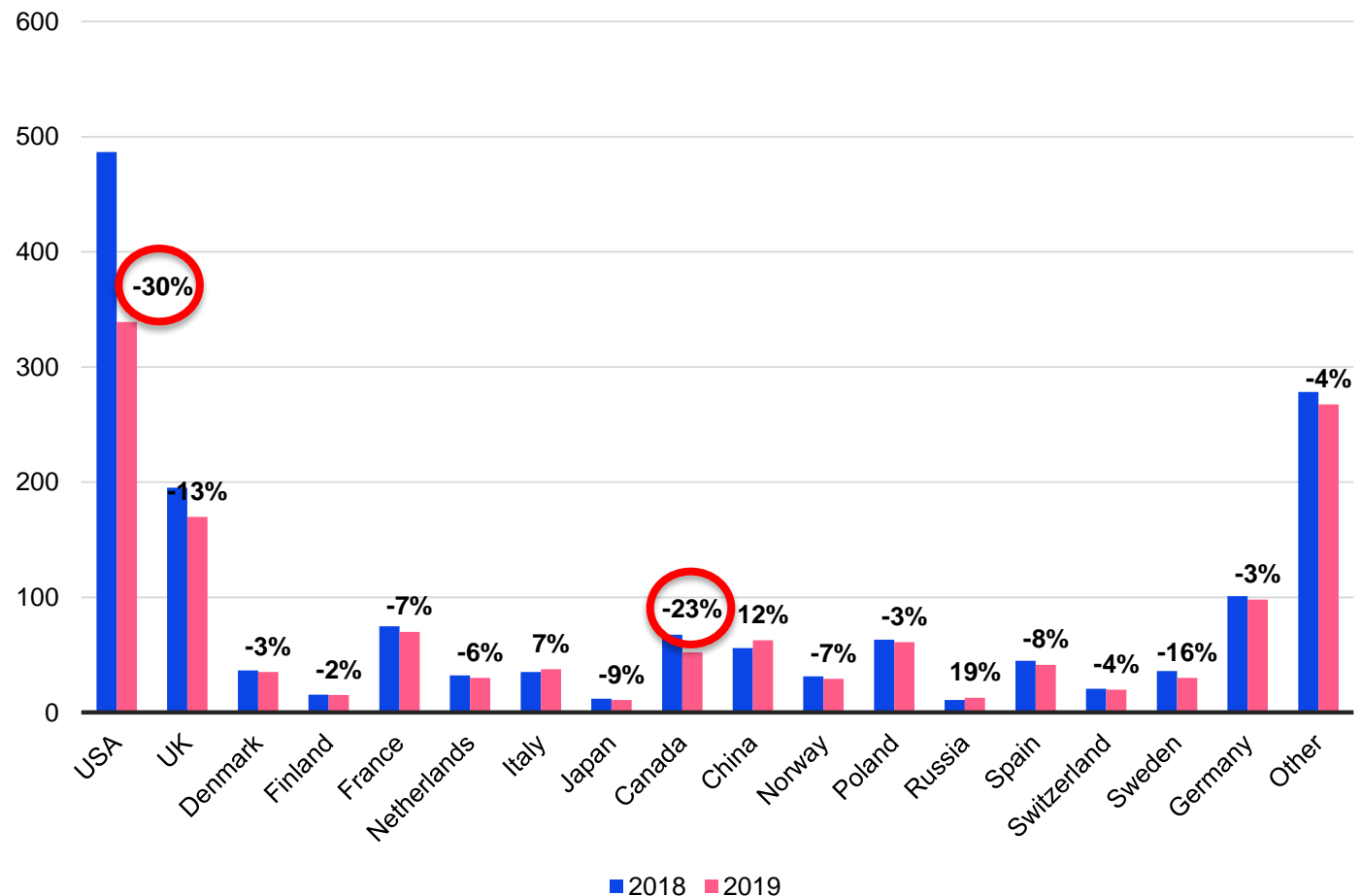
Roughly estimated WOW transported around 40% of tourists from North America last year, it is therefore not surprising that a larger drop in the number of tourists visiting from USA and Canada than most other countries.

Nationality of tourists traveling with WOW air



- Nordics
- UK
- Central and South Europe
- Eastern Europe
- North America
- Asia
- Others

Total number of tourist arrivals via KEF airport  
- thousands and YoY %-change



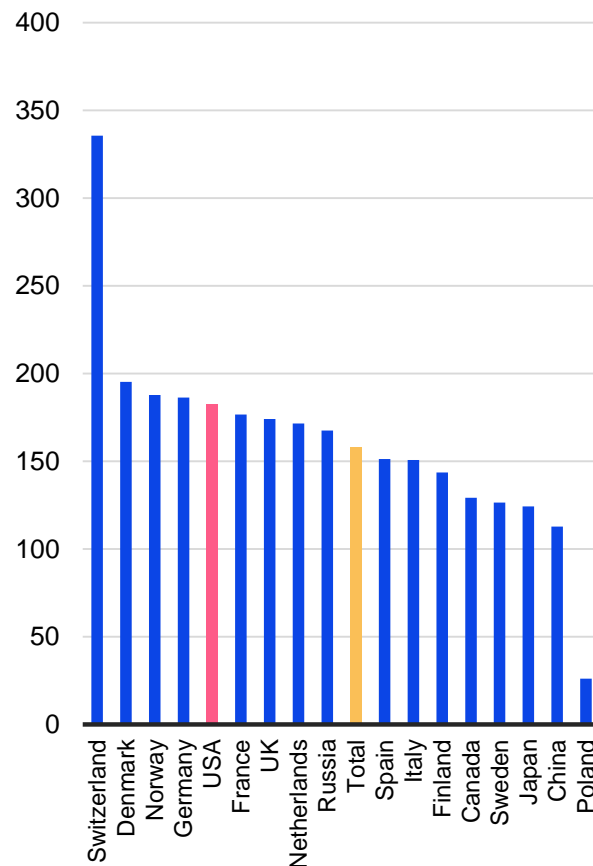
■ 2018 ■ 2019



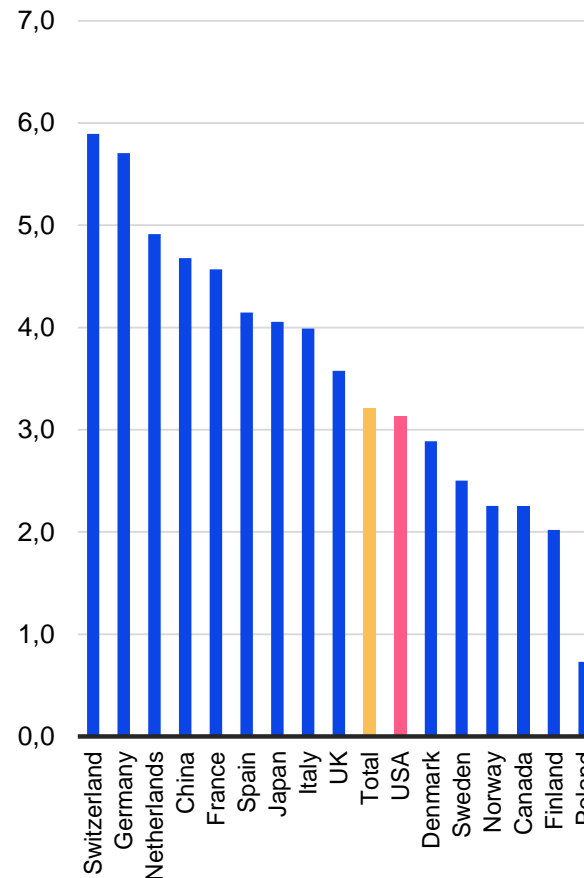
# Americans are valuable tourists

They spend more than the average tourist while they tend to stay shorter than the average tourist

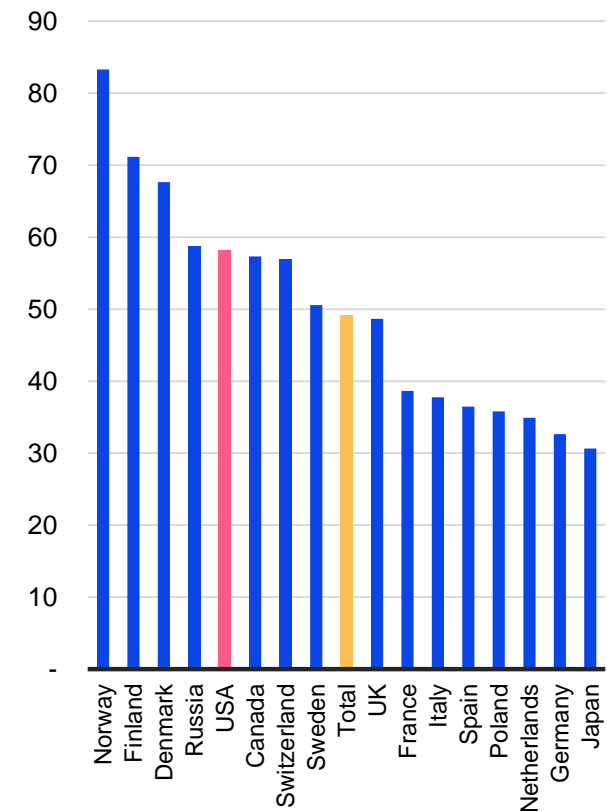
**Consumption** per tourist by nationality in 2018  
- thous. ISK at constant exchange rate



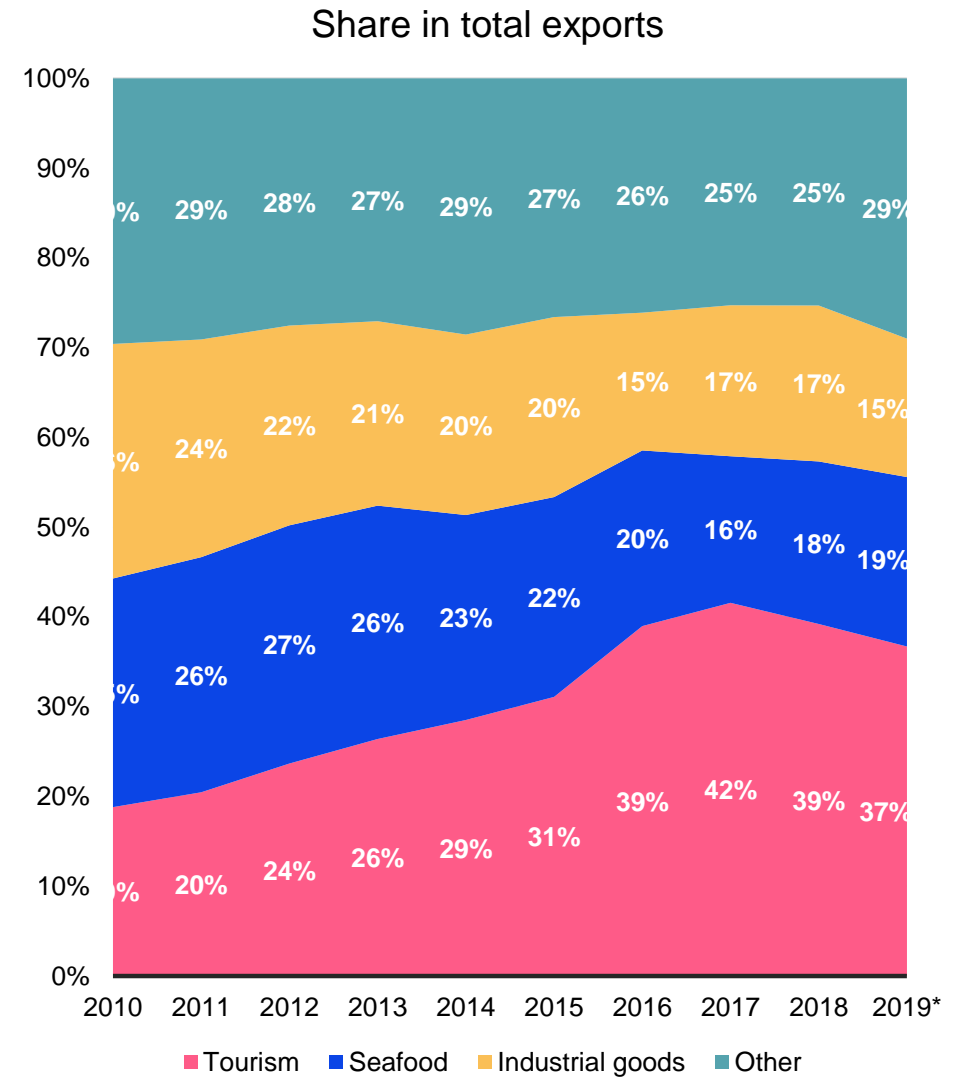
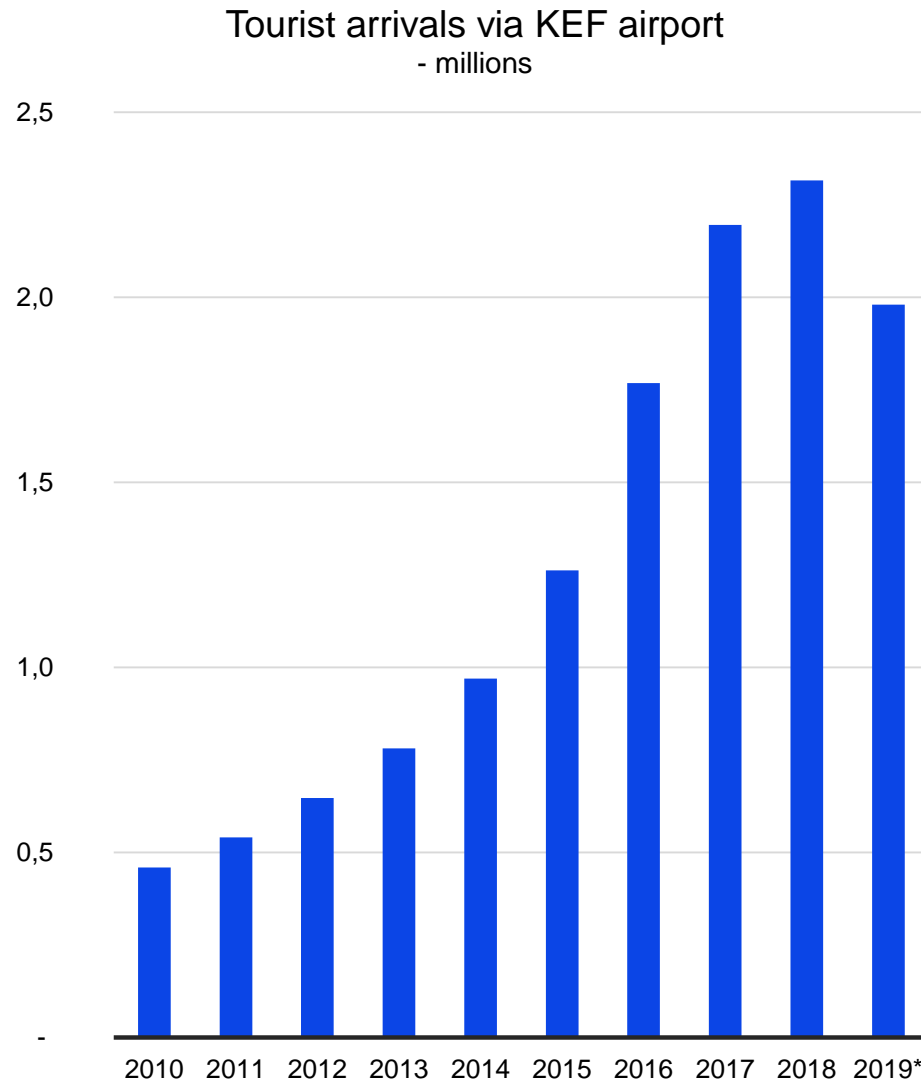
**Registered overnight stays** per tourist by nationality in 2018



**Consumption per overnight stay** by nationality in 2018  
- thous. ISK at constant exchange rate



# Tourism remains the biggest export industry

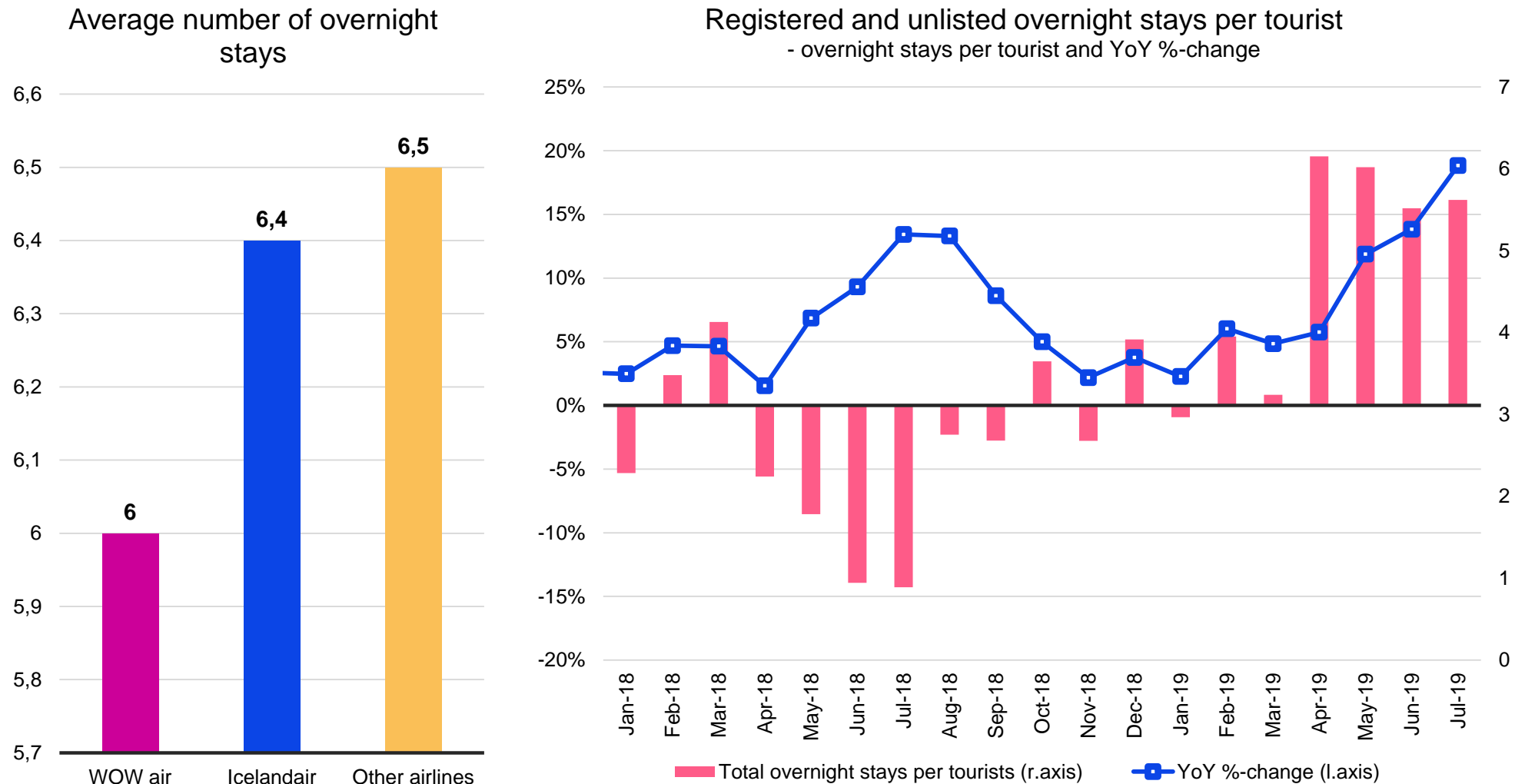


Sources: Iceland Statistics, Iceland Tourist Board, Arion Research \* Arion Research's forecast



# The average tourist stays around 24 hours longer than last year

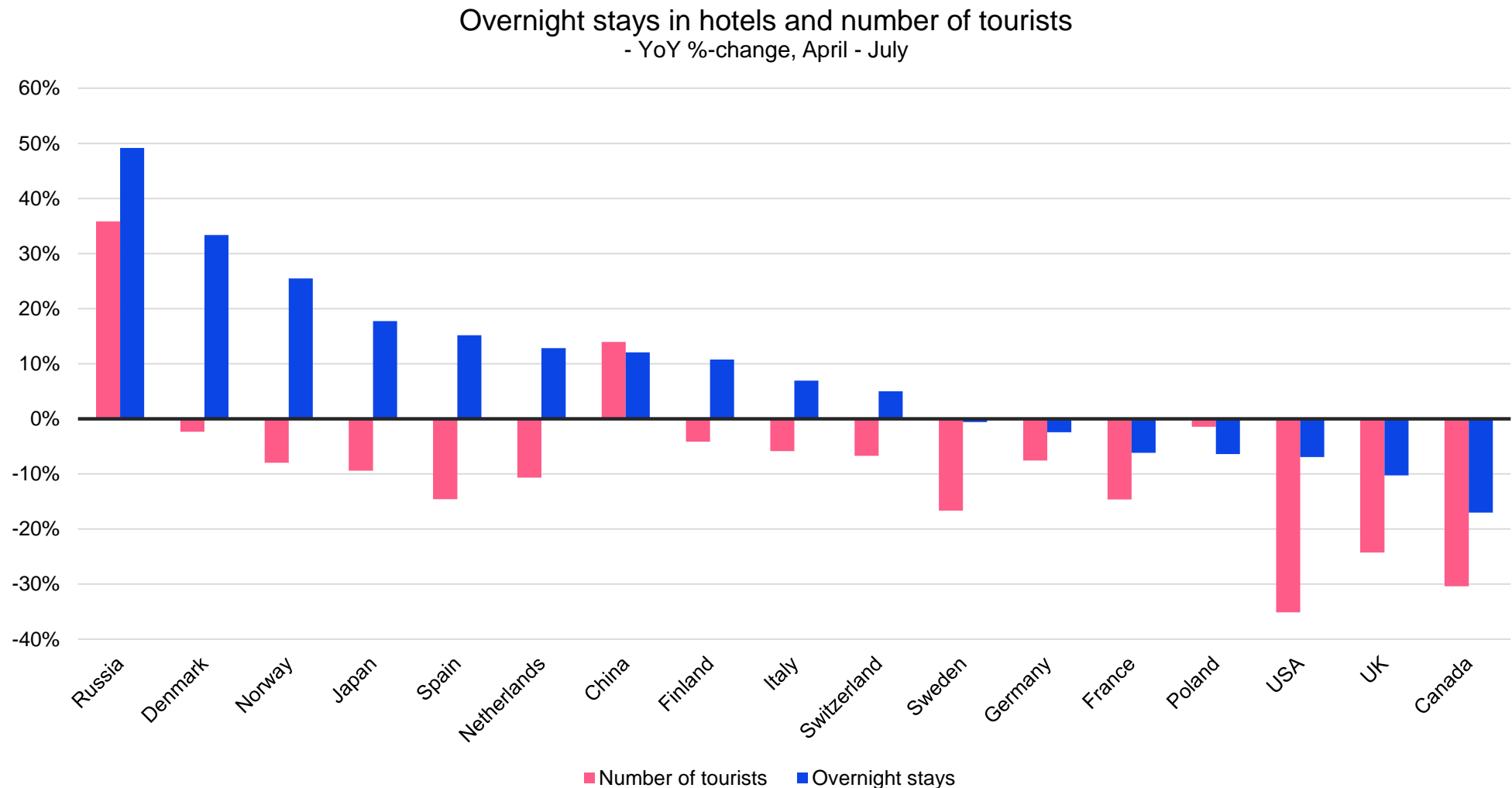
Since WOW air's bankruptcy overnight stays per tourist has increased by 17% on average. Iceland Tourist Board survey shows that tourists travelling with WOW air tended to spend fewer nights in Iceland than tourist travelling with other airlines.





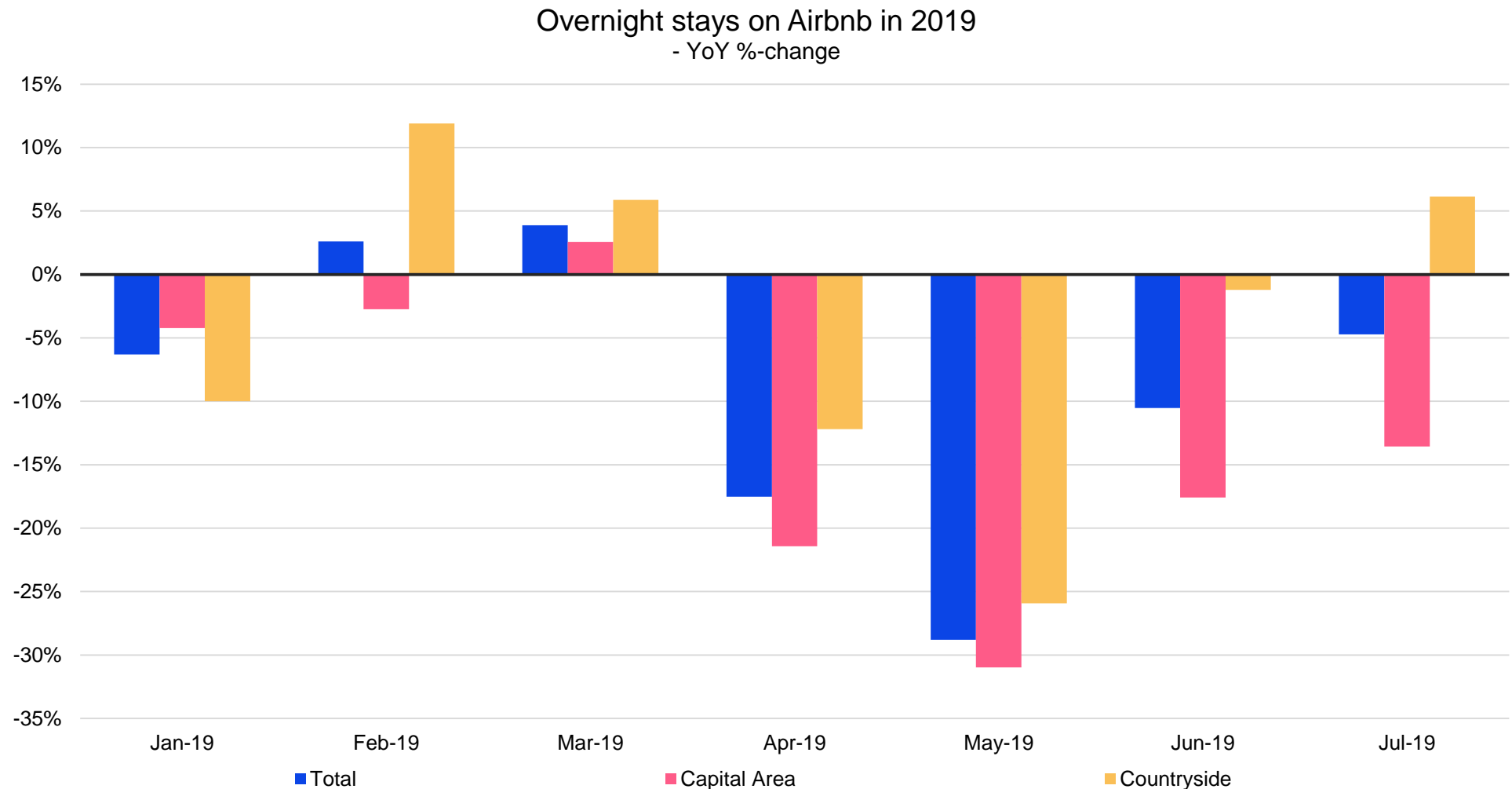
# Fewer tourists but the same number of overnight stays!

Overnight stays in hotels have only decreased by 0,1% since WOW air went bankrupt at the end of March, despite 17% fewer tourist arrivals



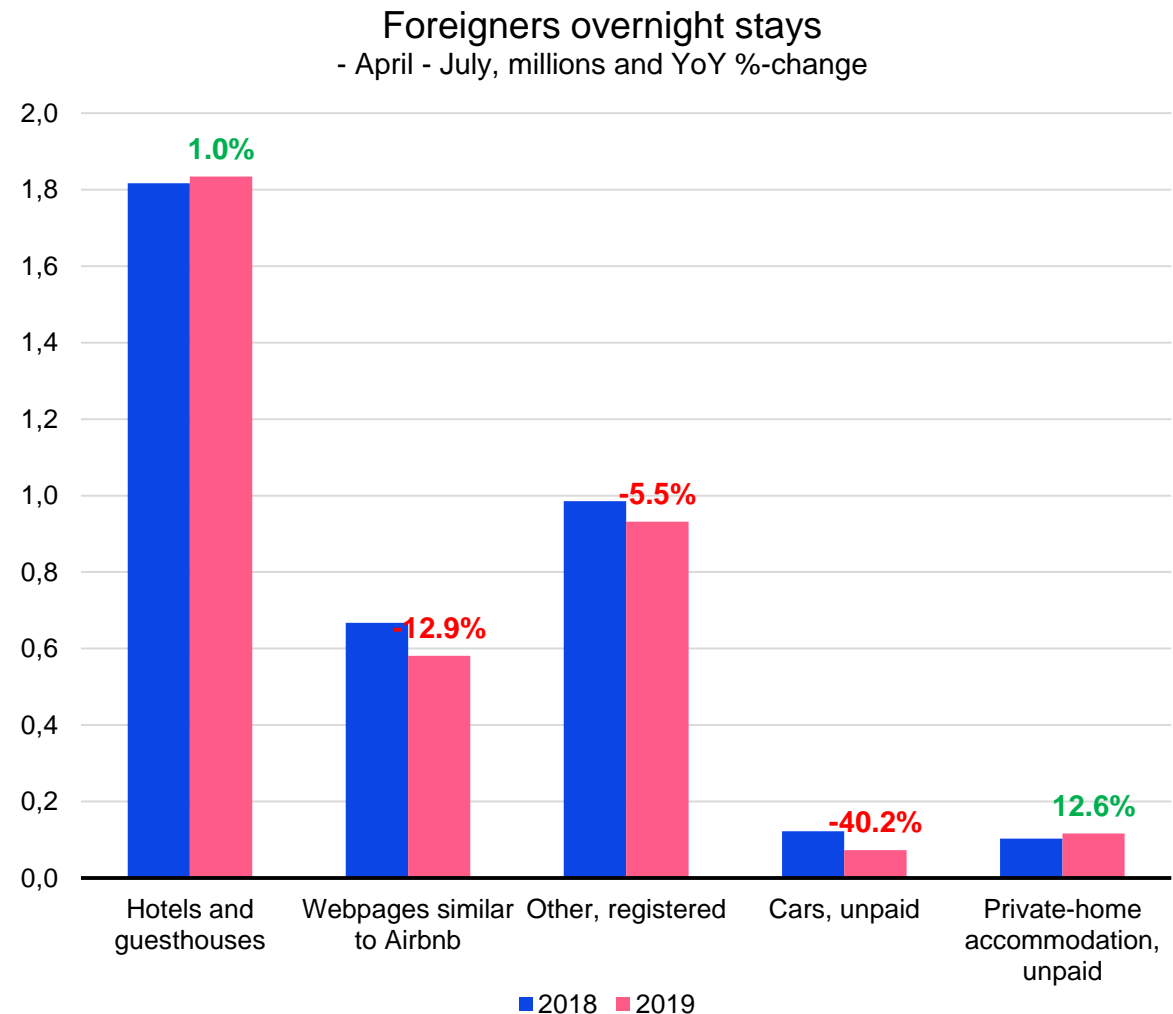
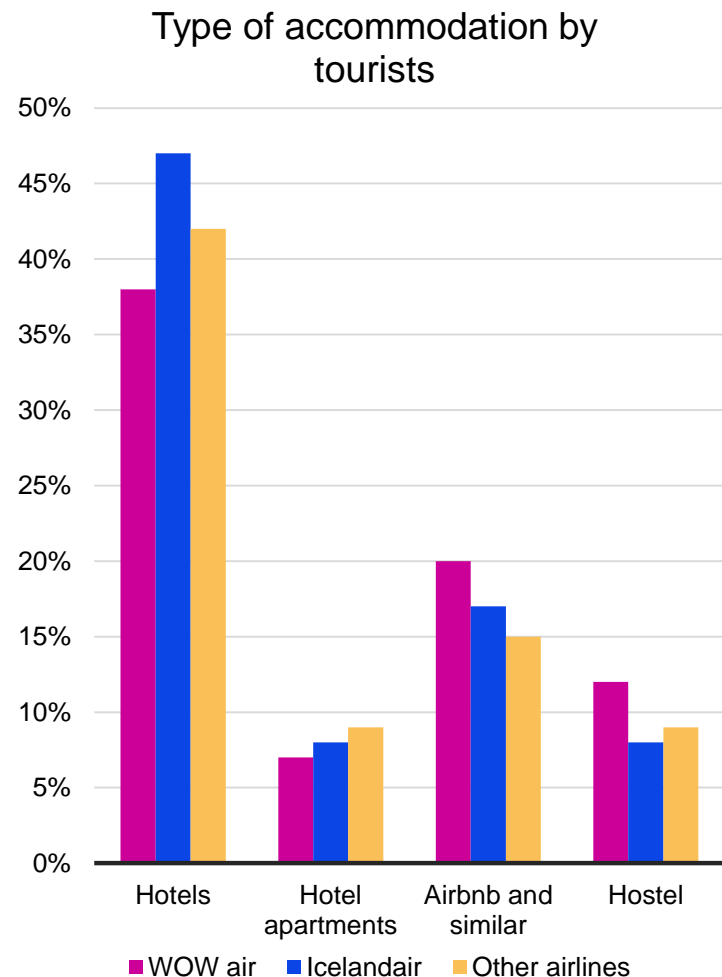
# Airbnb has taken a hit

Since WOW air went bankrupt overnight stays in Airbnb have decreased by 13%, mostly due to a fewer nights being spent in Airbnb in the Capital area.



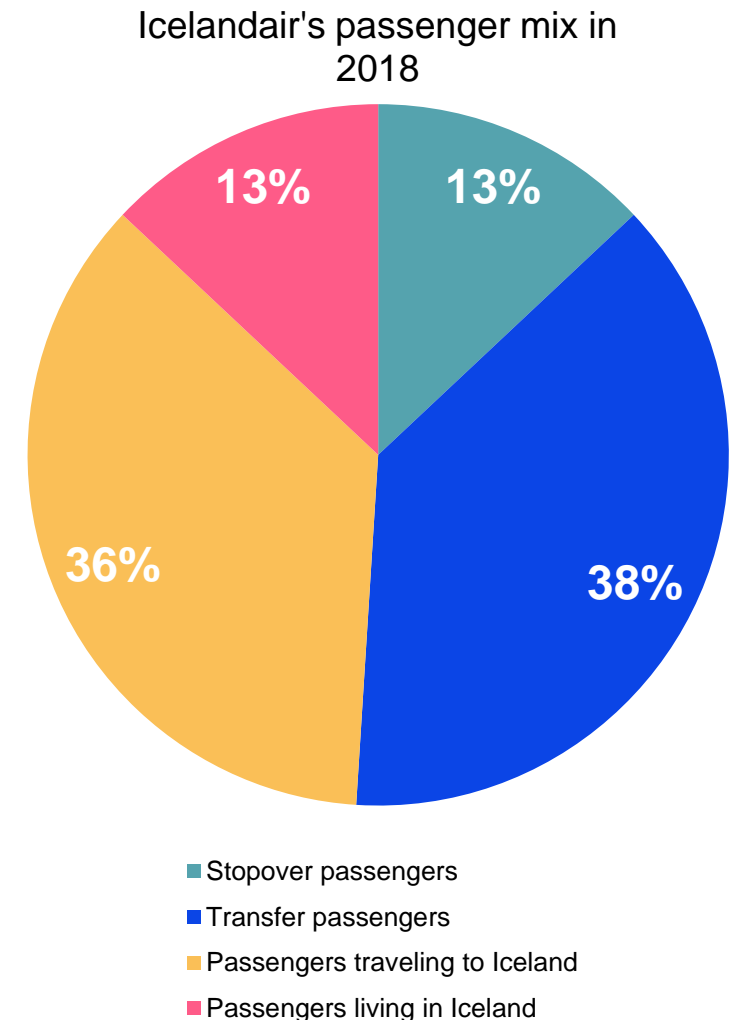
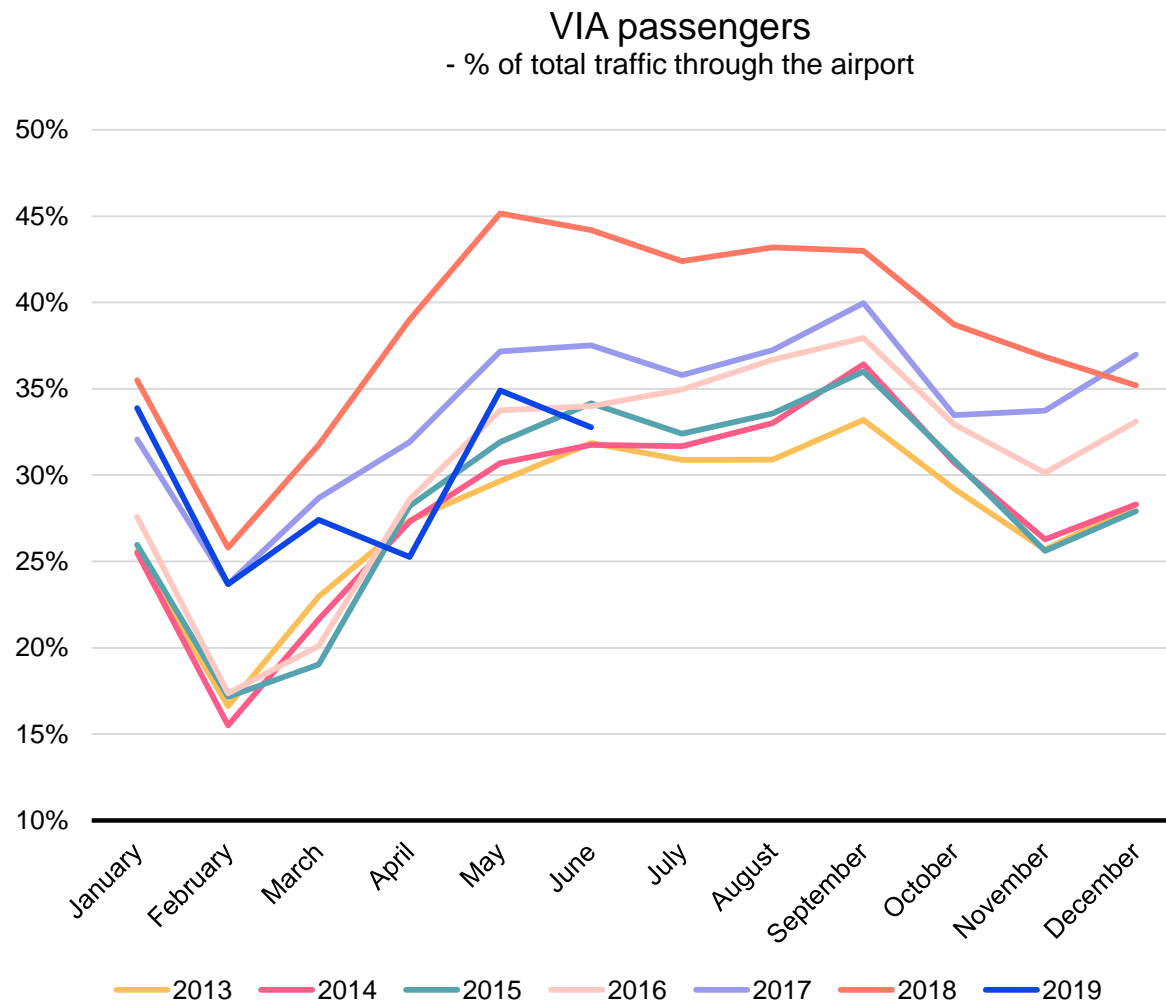
# Tourists are spending more nights at hotels and fewer in other type of accommodation

The passengers of WOW air tended to stay less at hotels than passengers of Icelandair last year.



# Icelandair's different passenger mix has had an effect

About 25% of via passengers are stopover passengers who typically stay shorter. Less emphasis being put on via passengers should lead to fewer stopover passengers leading to longer average stay of tourists and more consumption per tourist.



# The number of tourists has been overestimated

Self connecting passengers are sometimes counted as tourists. Wow air's demise is likely to have reduced the number of self connecting passengers leading to a better estimate of the actual number of tourists. This could partly explain more overnight stays per tourists being counted and a considerable growth in consumption per tourist.





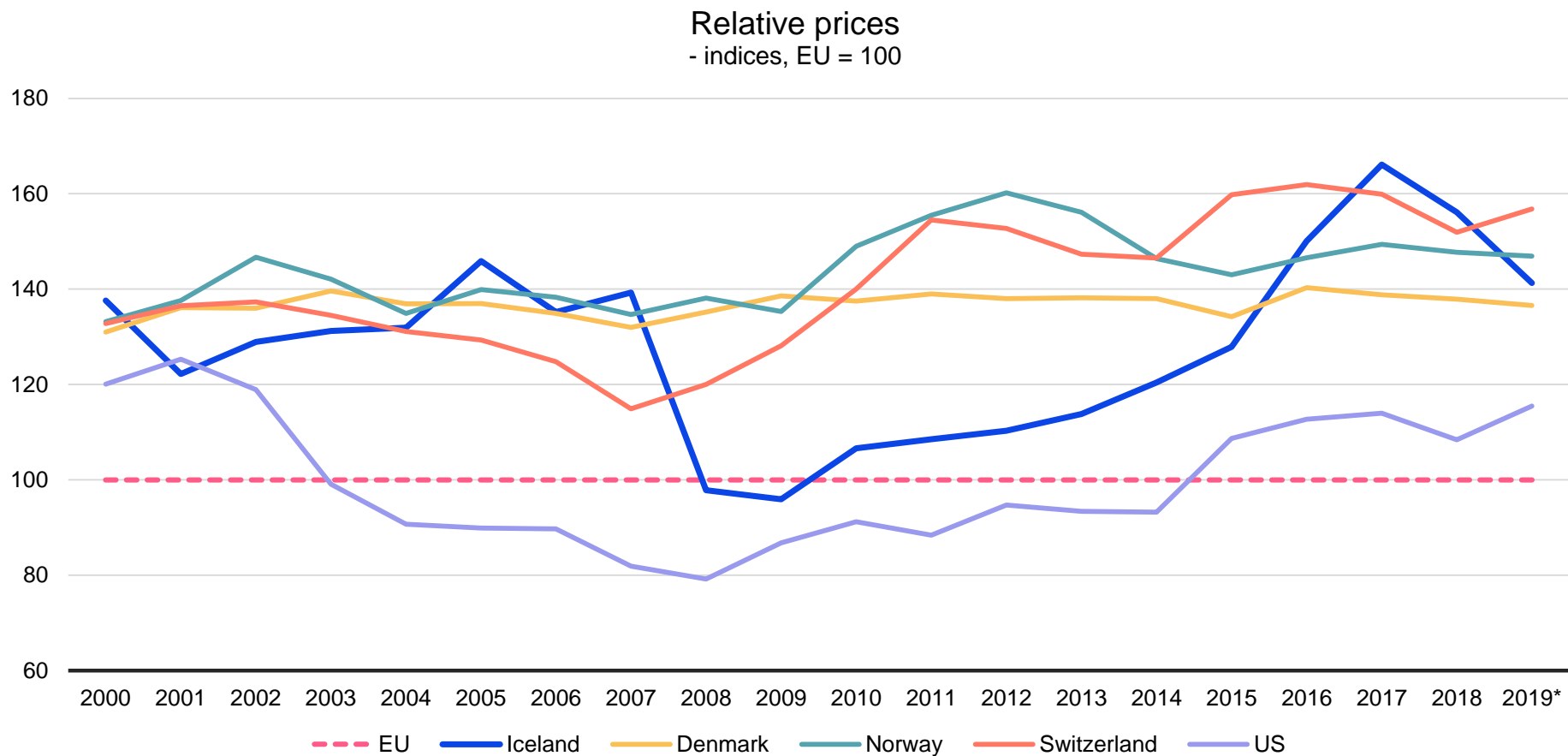
## Iceland has become less expensive

A weaker ISK supports tourism and prices of hotel rooms have slid both in ISK and EUR. Occupancy ratio has come and we expect it to settle around 73%



# Not the most expensive country anymore!

Sure, Iceland is expensive, and in 2018 it was probably the most expensive country in Europe to spend time with prices being on average 56% higher than in the EU and 44% higher than in the US. That is not the case anymore after a depreciation of the króna, coupled with modest inflation, it has again gotten cheaper to visit Iceland. It can now be assumed that Iceland is around 40% more expensive to spend time in than the average EU country and 24% more expensive than spending time in the US.

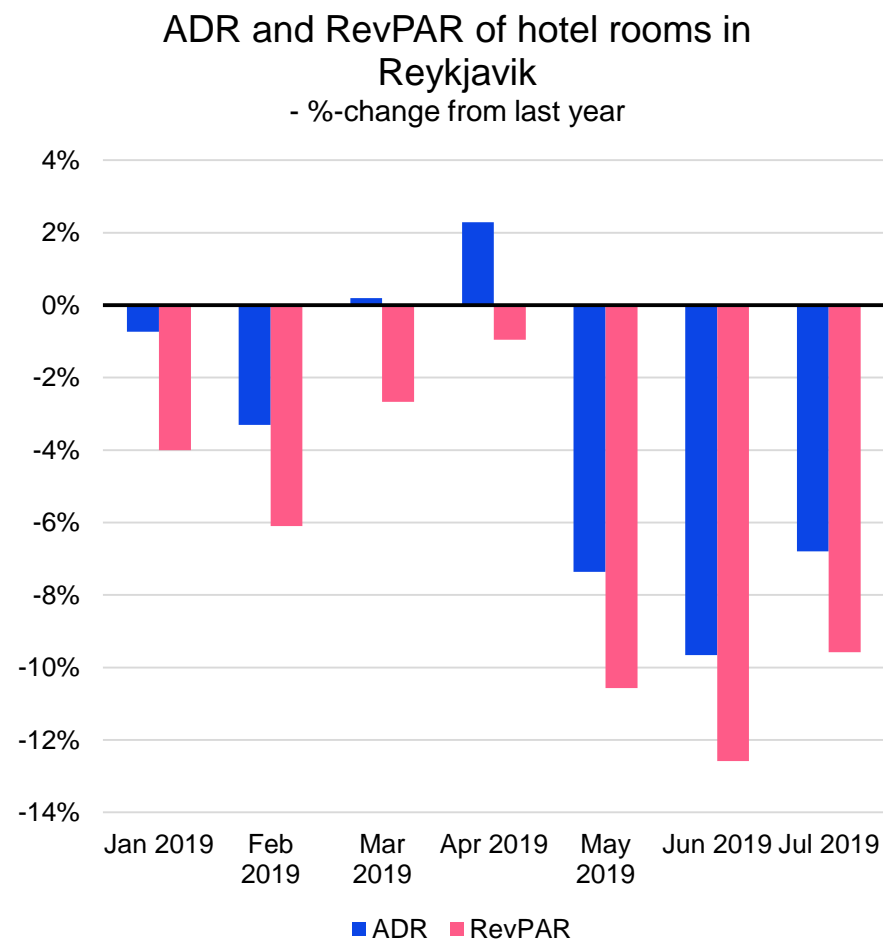
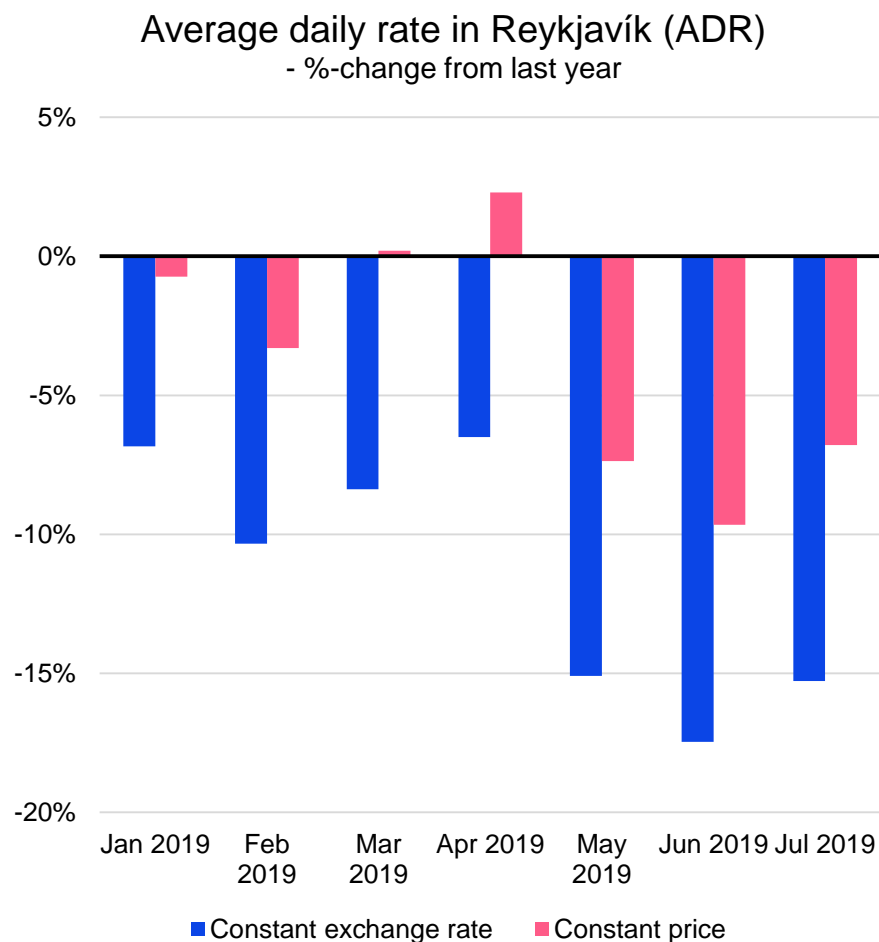


Sources: Eurostat, Arion Research. \* First seven months of 2019.



# Hotel rates have declined, both in ISK and EUR

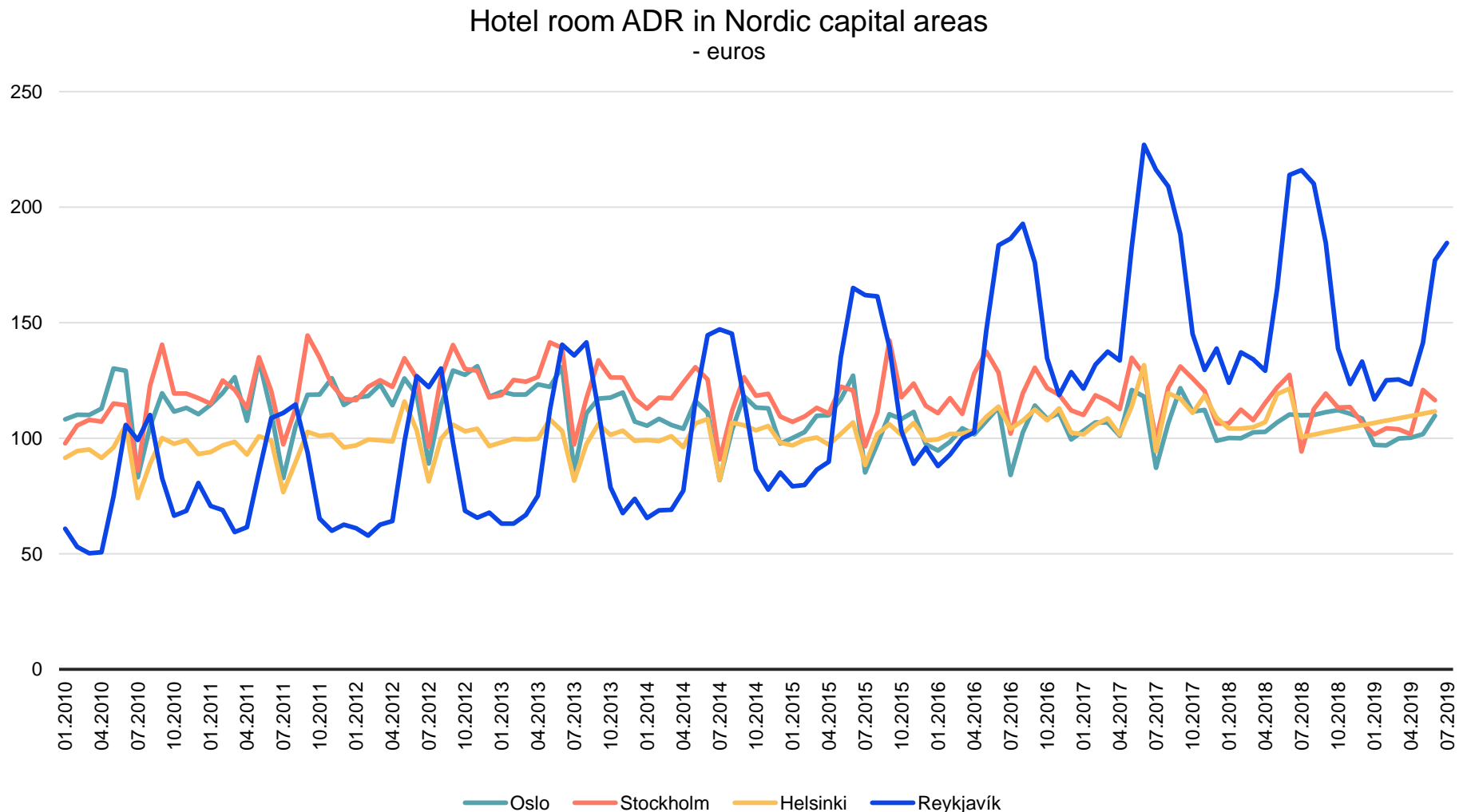
Lower price has probably supported occupancy rates, as they have declined less than number of tourists. Reduction in occupancy rates, coupled with lower price has led to considerable contraction in Revenue per Available Room.





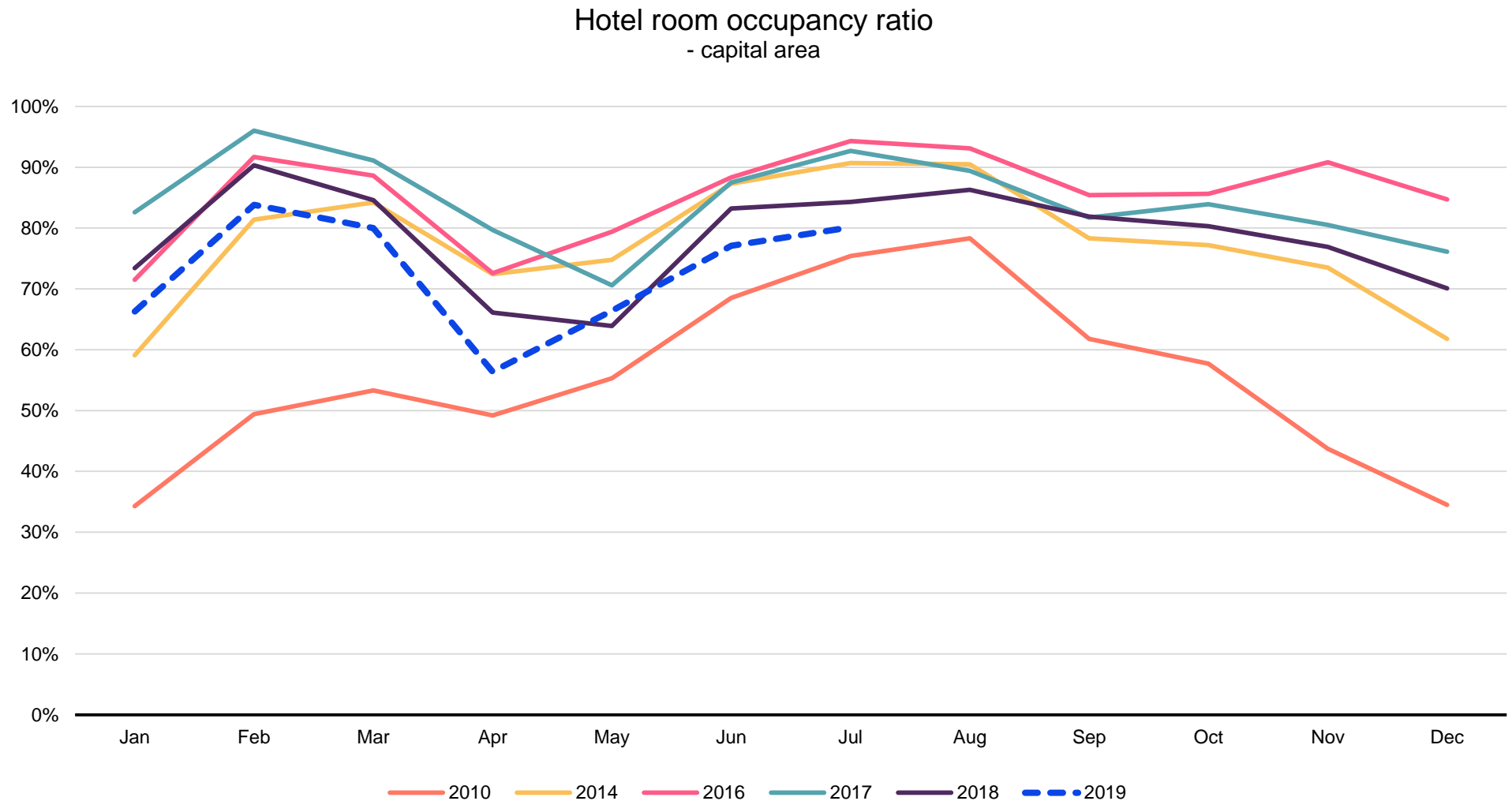
## Prices of hotel rooms in the capital area are still high compared to other Nordic countries

There seems to be more seasonality in prices of hotel rooms in Reykjavík compared to other Nordics capitals. Survey shows that average price for hotel room in Reykjavik in July decreased by around 12% YoY in EUR.



# Occupancy rates have gone down

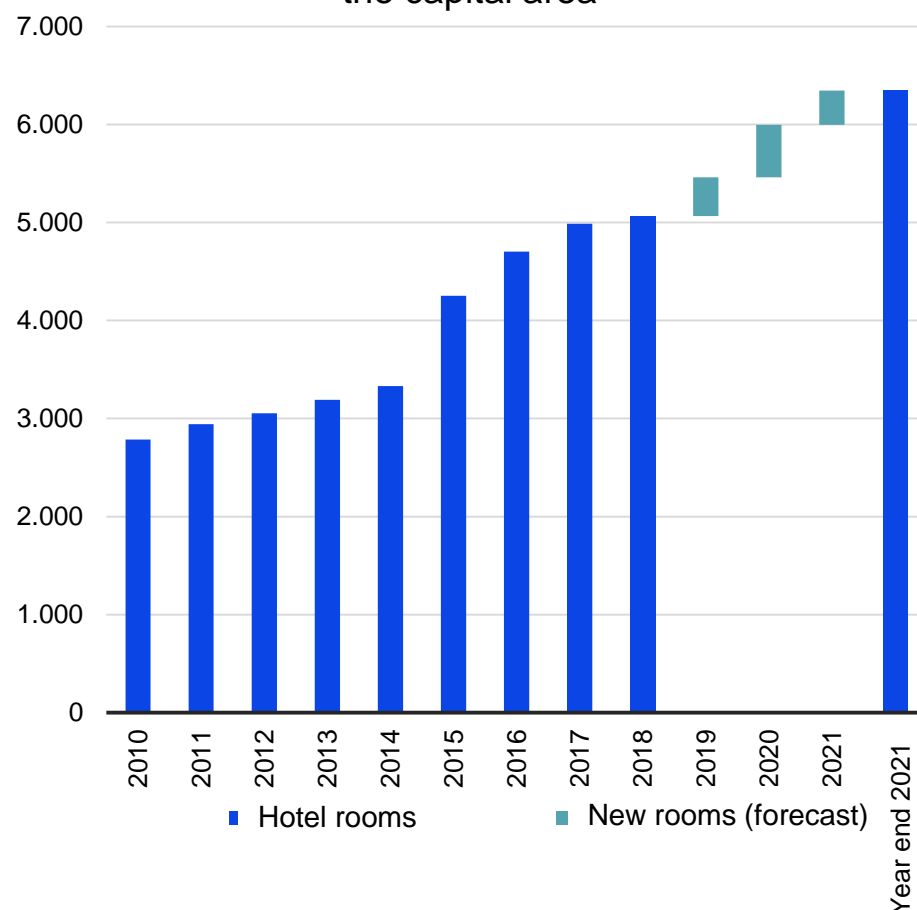
The average occupancy rate of hotels in the Capital area has gone down due to a growing supply of rooms alongside with fewer tourists. However the occupancy rate is still high in comparison to other Nordic cities.



# New rooms starting to welcome its guests

So far this year 270 new rooms have opened and 120 more are expected to be opened before the end of the year. In addition to this, around 900 rooms are under construction, and around 1,150 rooms are in development. In our opinion, it is unlikely that all development projects will realize. Neither do we expect that all development projects to be ready before 2023.

Arion Research's hotel room forecast in the capital area



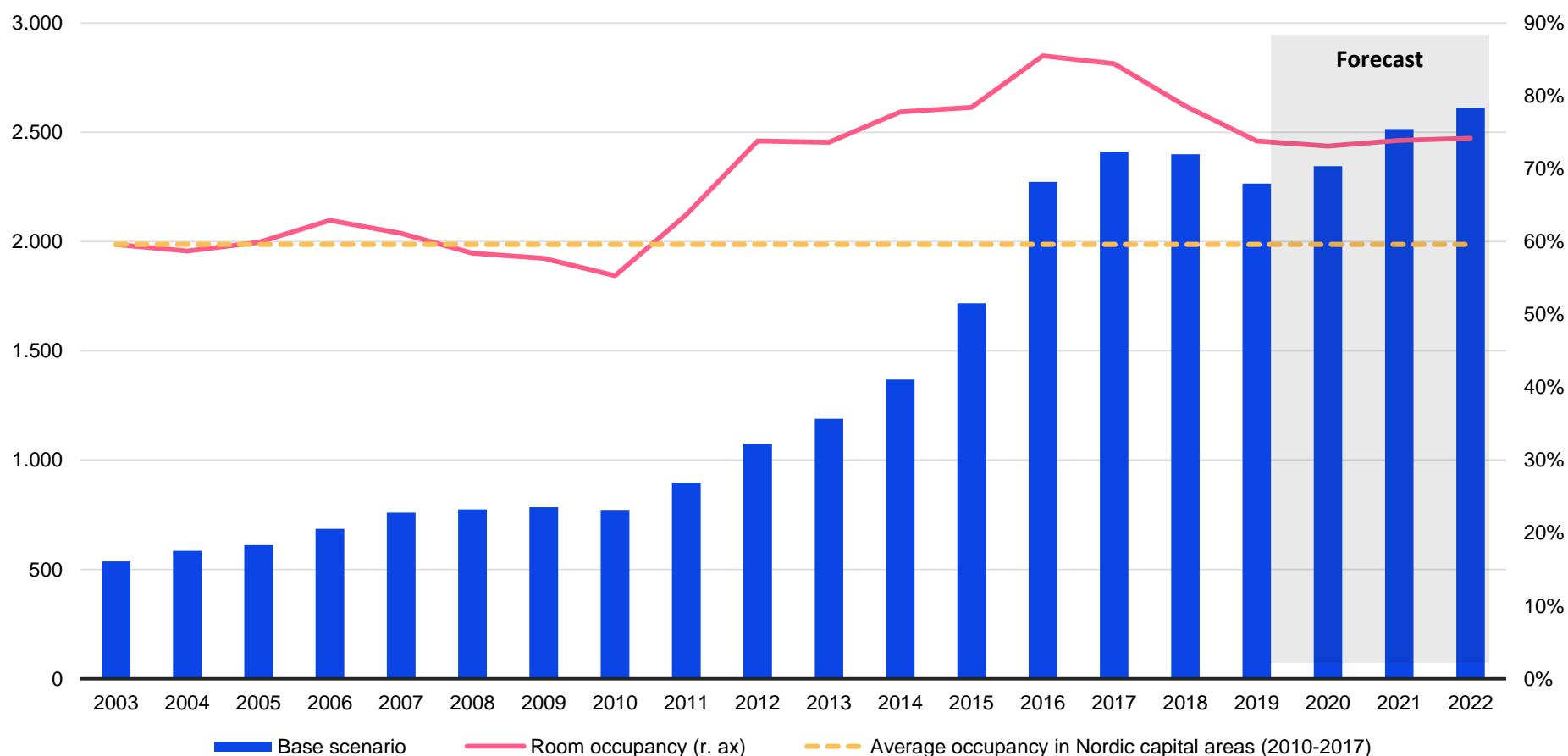
	Rooms	Year	Status
Room with a view - Vegamótastígur 7-9	40	2019	Finished
Oddsson - Grensásvegur 16a	77	2019	Finished
Centerhotels - Plaza (expansion)	54	2019	Finished
Centerhotels - Laugavegur 95-99	101	2019	Finished
City Park - Ármúli 5 (expansion)	27	2019	In construction
Von Guldsmiden - Laugavegur 55	52	2019	In construction
Skipholt 29a	44	2019	In construction
Marriott Edition Reykjavik	250	2020	In construction
Parliament Curio - Landsímareit	160	2020	In construction
Íslandshótel - Lækjargata	128	2020	In construction
Radisson Red - Barónsreitur	195	2021	In construction
Centerhotels - Héðinsreitur	153	2021	In construction
Keahótel - Hallarmúli 2	162	2022	In development
Íslandshótel - Grand hótel (expansion)	100	2022	In development
Íslandshótel - Hótel Barón (expansion)	100	2022	In development
Skipholt 1	84	2022	In development
Guldsmiden - Grandagarður 2	95	2022	In development
Laugavegur 176	120	2022	In development
Hlíðarendi	360	2022	In development
Strandgata HFJ	126	2022	In development
<b>Total:</b>	<b>2.428</b>		
Construction started/finished	1.281		
In development	1.147		



# We predict 73% occupancy ratio in the coming years

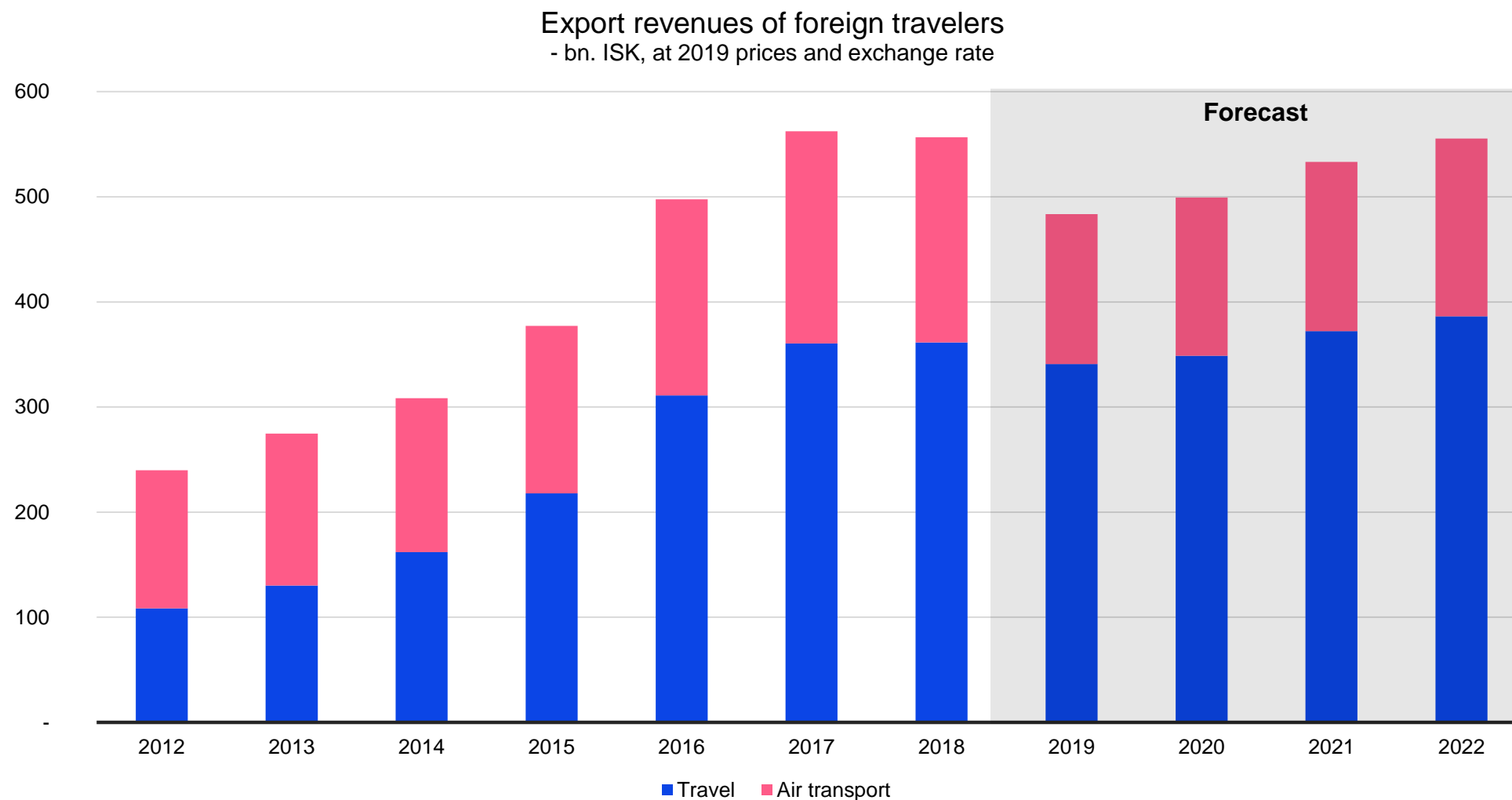
Increased capacity will put pressure on occupancy ratio in the coming years. However, increase in tourist arrivals later on in the forecast period coupled with longer stays offsets this. If the forecast realizes, we expect average occupancy rate to be similar as it was in 2012-2013

Arion Research's forecast for overnight stays and occupancy in the capital area  
- thousands



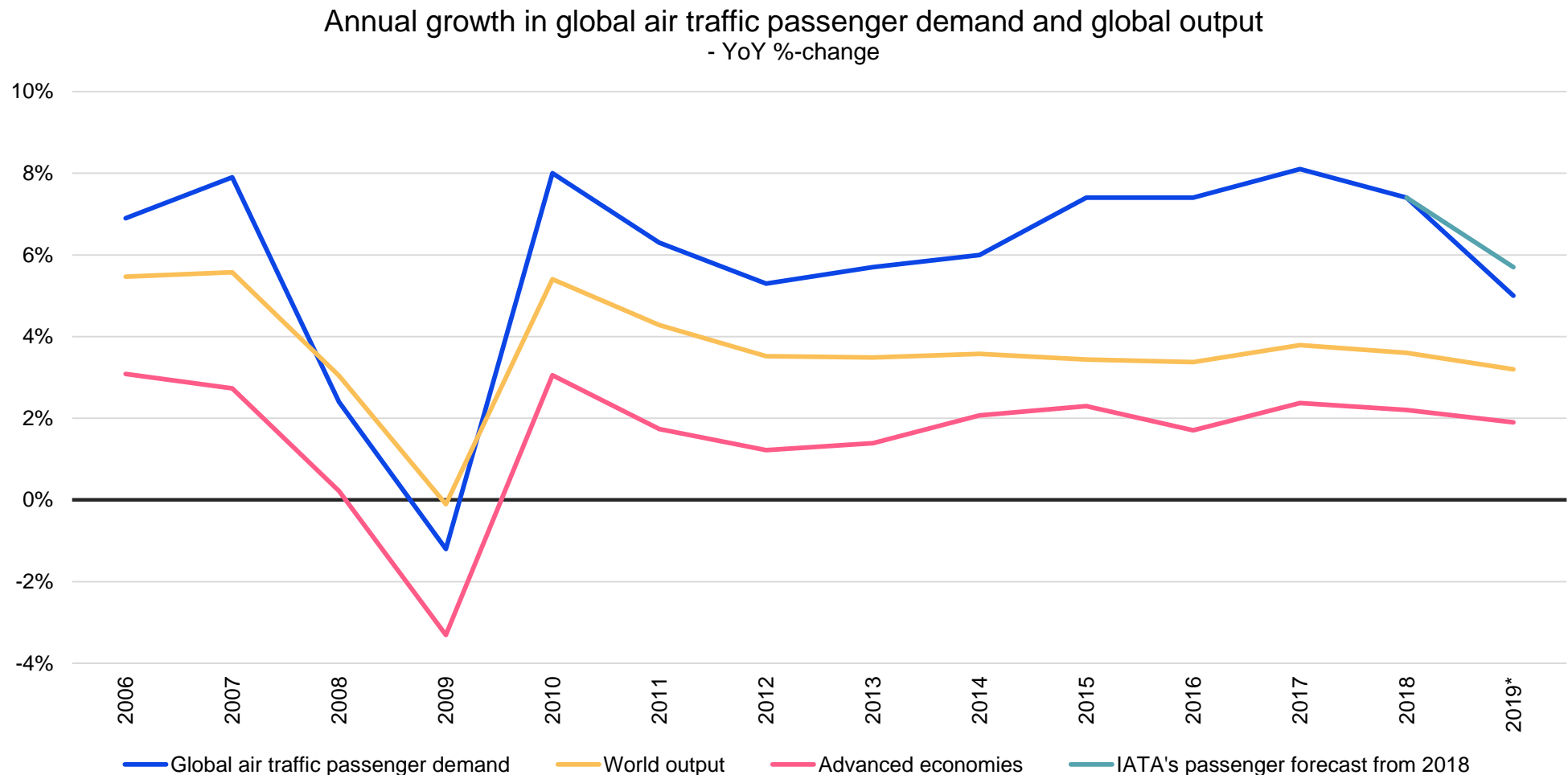
## We expect similar export revenues from foreign travelers in 2022 as in 2018

Based on our base case on number of tourists and given assumptions about tourist's consumption.



# A slowing world economy decreases demand for travel

How much effect might further slow down of the world economy have on Icelandic tourism? That depends on income elasticity. IATA's passenger forecast has been lowered with worsening global economic outlook suggesting the demand for travel to be sensitive to income.





# Tourism is Labour intensive

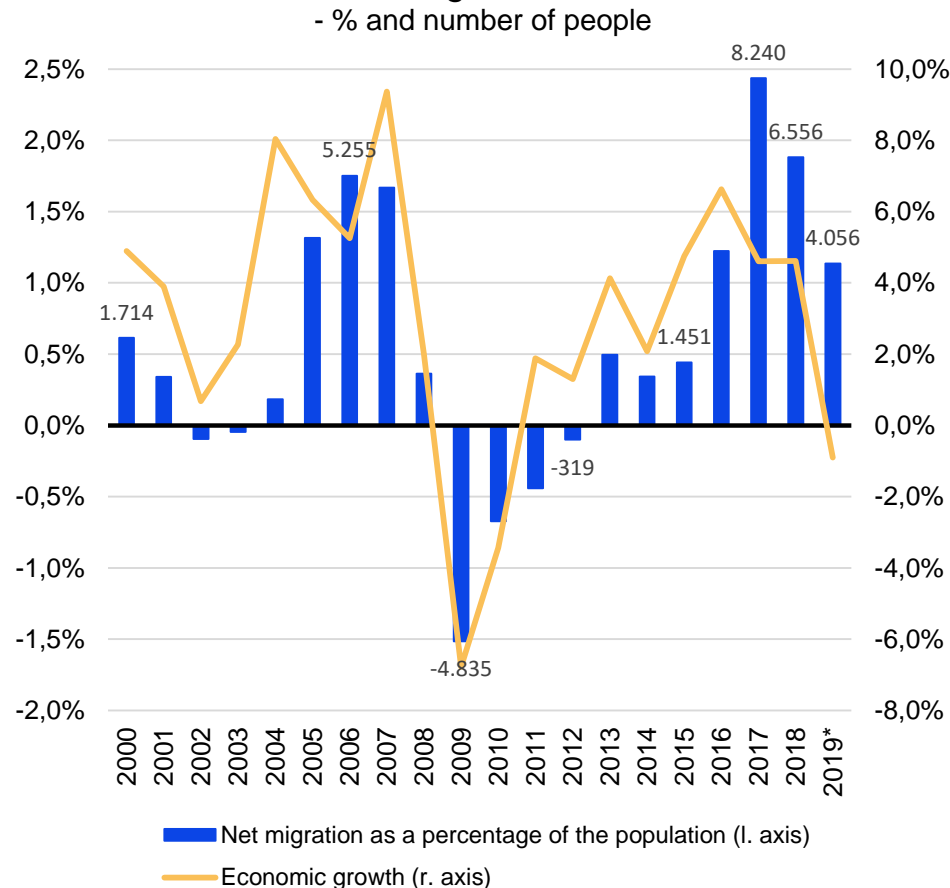
The labour force has had to grow considerably to make the growth of tourism possible, now however unemployment is set to grow.



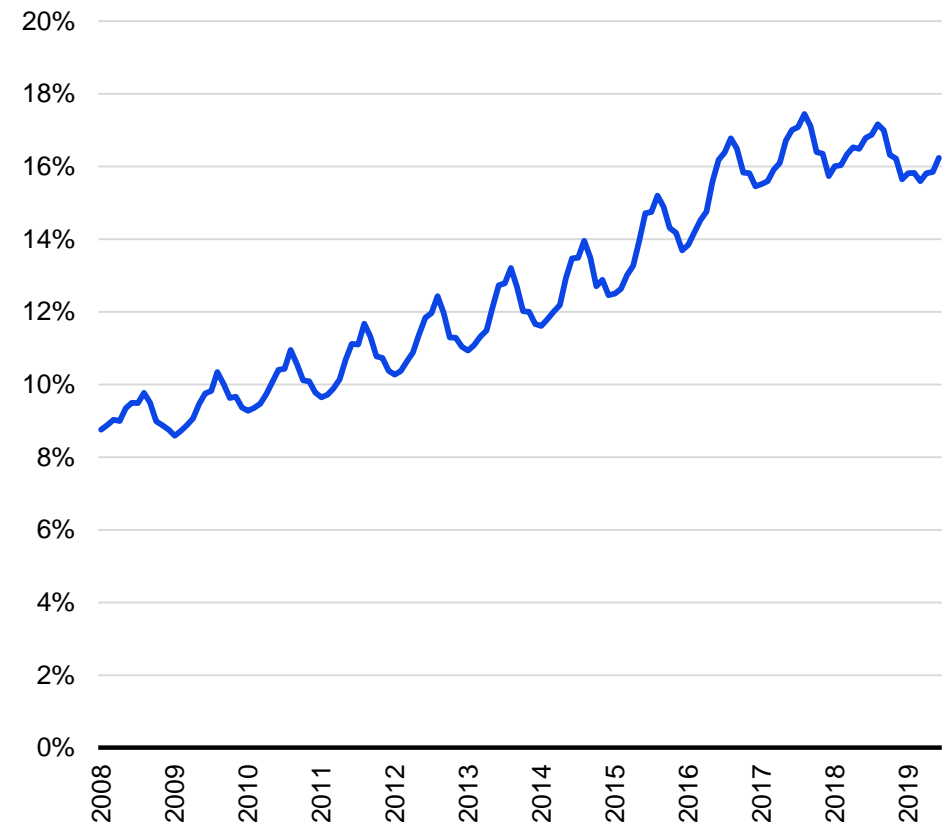
# The growth of tourism has called for a bigger labour force

Historically there has been a good correlation between economic growth and net migration to Iceland. Recently however the correlation has been broken, mainly because of how labour intensive tourism is. Since 2010 17,000 jobs have been created in tourism in Iceland which is 40% of all new jobs in the country this decade.

Correlation of economic growth and net migration  
- % and number of people



The number of employees in tourism as a percentage of the total number of employees in Iceland

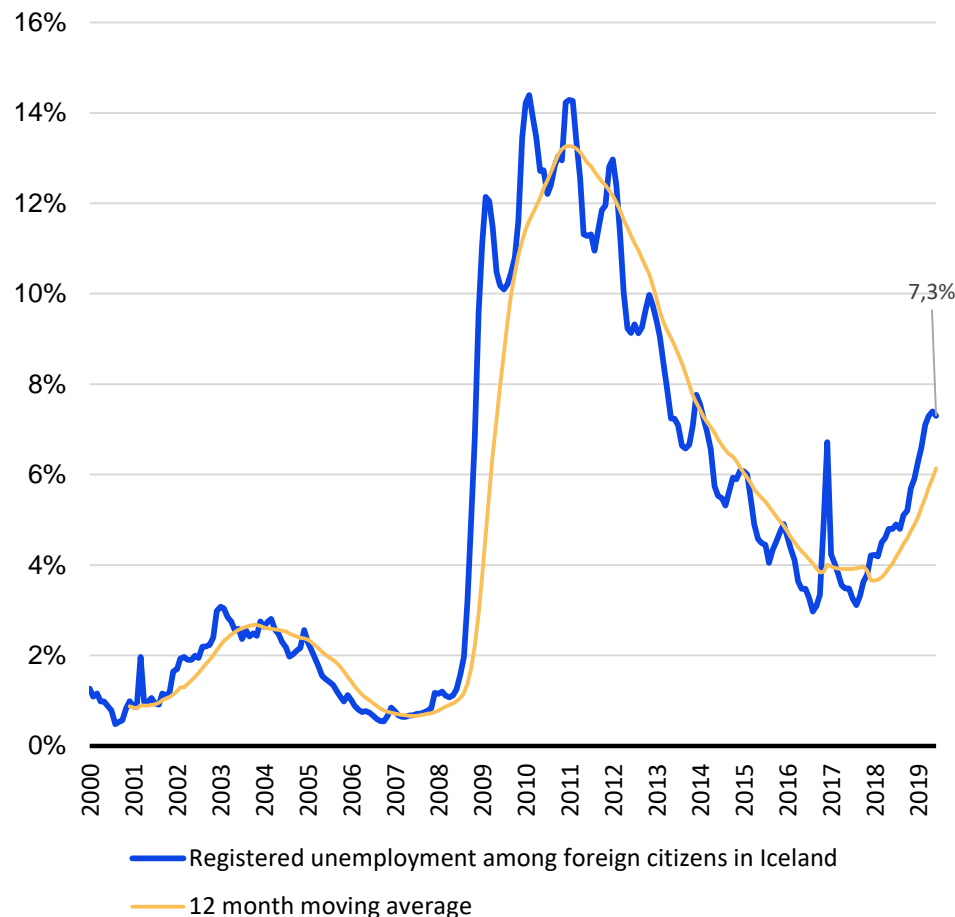




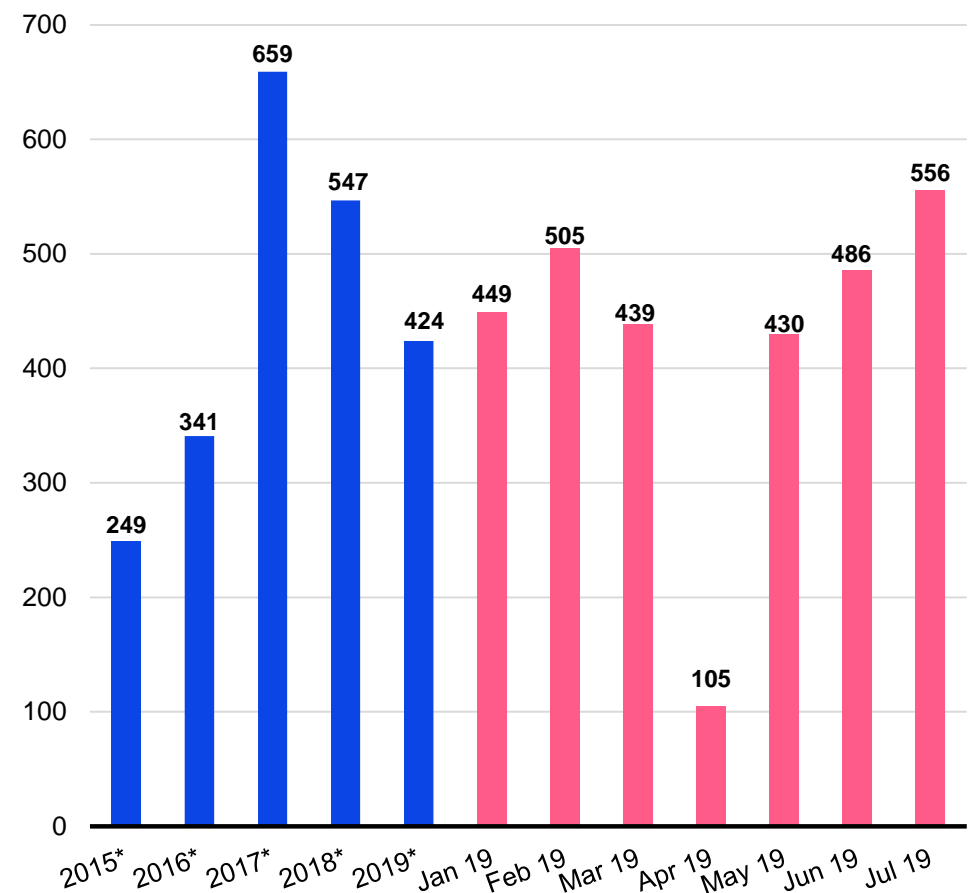
# Net migration still considerable despite rising unemployment

Unemployment among foreign citizens in Iceland has more than doubled in the last two years and has gone from 3.8% up to 7.3%. Despite that net-migration has remained considerable and we expect more than 4,000 foreign citizens will migrate to Iceland this year.

Registered unemployment among foreign citizens in Iceland



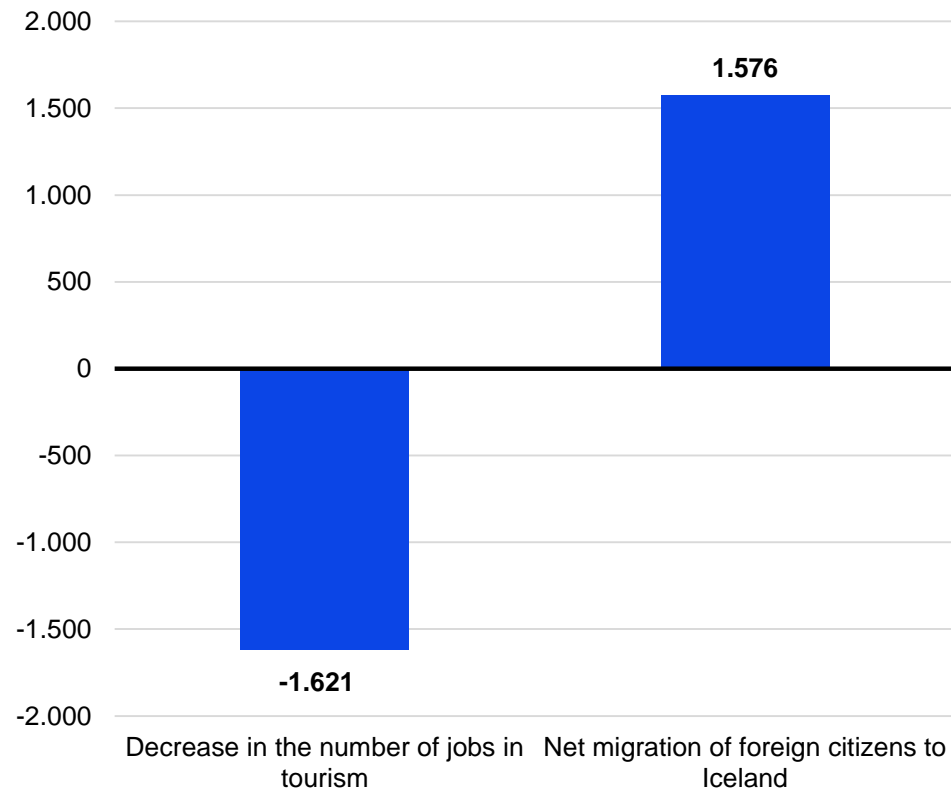
Net migration of foreign citizens  
- monthly basis, (\*) monthly average



# Competition increases in the labour market

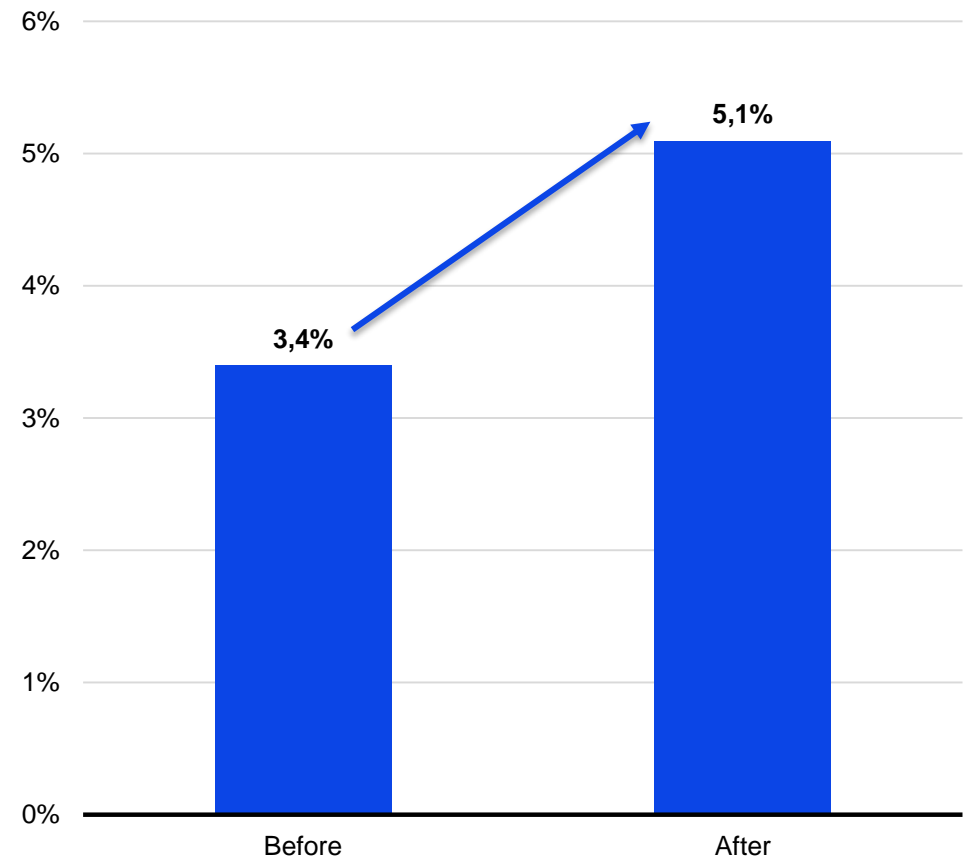
If migration stays the same as it has been in the first months after WOW air went bankrupt and the number of jobs stays roughly the same unemployment will rise and could go above 5% looking twelve months ahead given these assumptions.

Change since the bankruptcy of WOW air



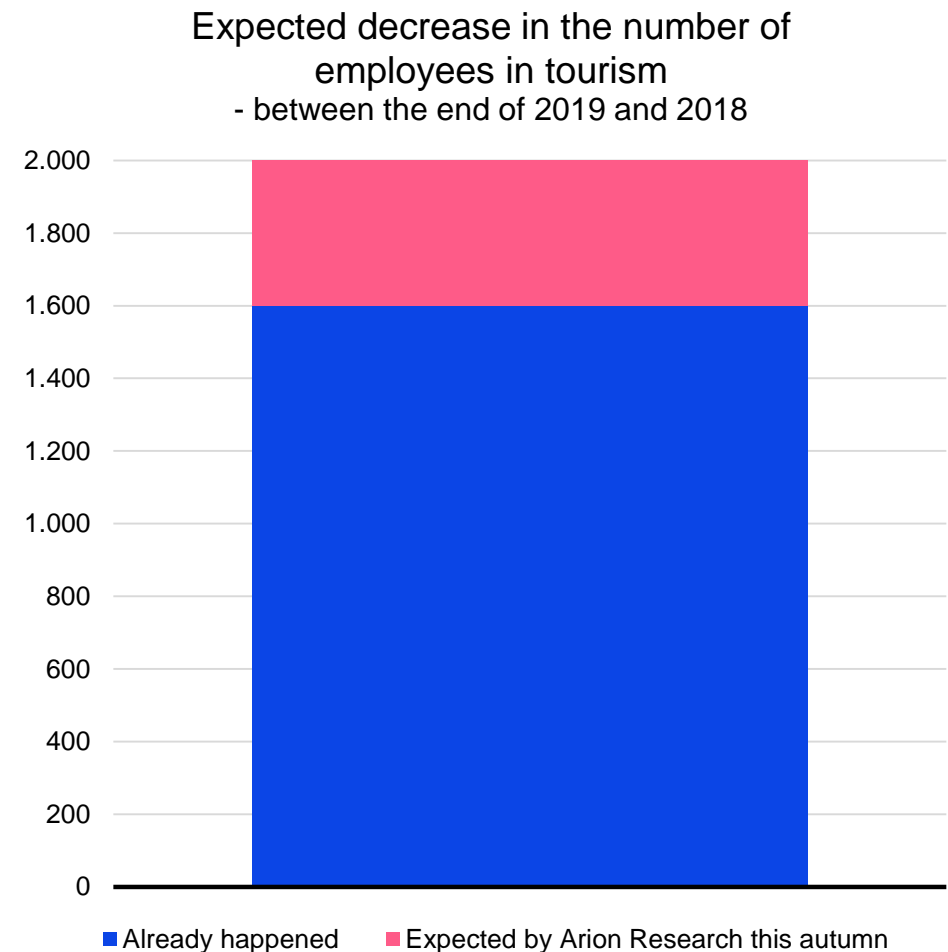
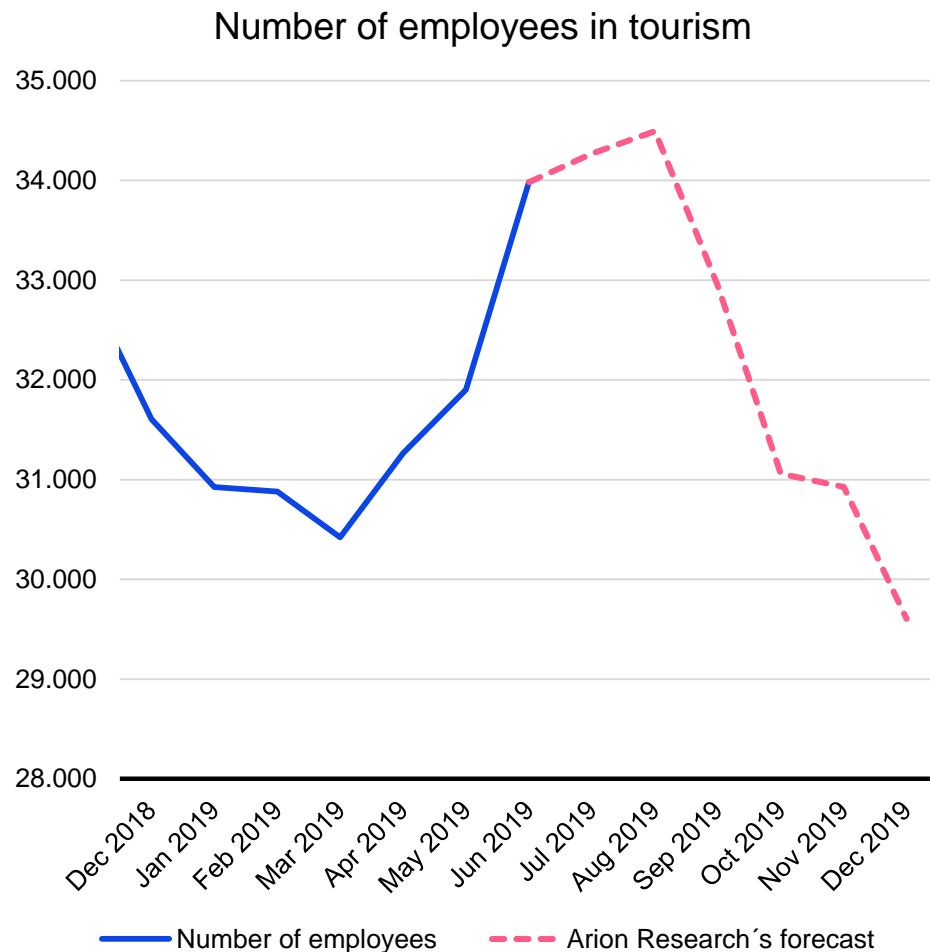
Unemployment

- if migration stays similar to what it has been after WOW air went under and the number of jobs stays similar for a year



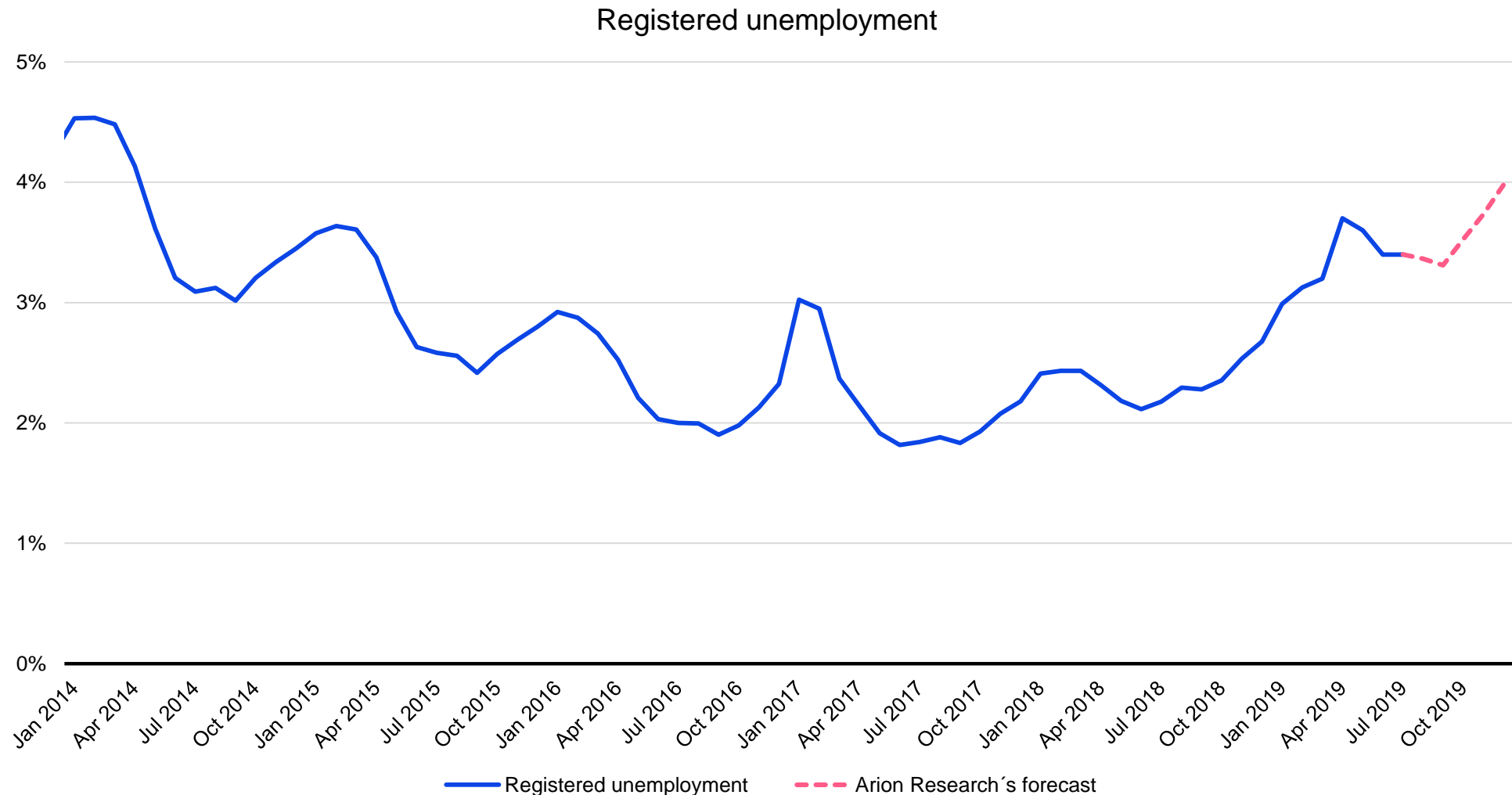
# Decreasing number of employees in tourism

We expect the number of employees in tourism to be two thousand fewer by the end of the year than at the same time last year. The number of employees in tourism is well correlated with the seasonality in number of tourist arrivals. Even so, we expect number of tourist related jobs to decrease more this autumn than mere seasonality suggests.



# We expect unemployment to rise

Due to seasonality, fewer tourist arrivals, slower economic activity and pressure on costs we expect unemployment to rise and to be a close to 4% by the end of the year.



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