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Tourism Finance: Investing and Financing in Sustainable Tourism

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Abstract—This study addresses the big problem that tourism projects and initiatives are encountering. Lack of financing is a common challenge hindering the development of tourism, resulting to a number of popular destinations that are slowly dying (e.g. the Great Wall of China, and the Angkor Wat). The purpose of Tourism Finance is to set criteria on which value-adding tourism projects should receive investment funding; and to evaluate a tourism organization's financial needs to better decide on what capital structure (i.e., debt and/or equity) to appropriately raise to minimize the weighted average cost of capital. The method of this research is using qualitative research method with techniques of data collection by literature study and that were conducted by discussing seven potential sources of travel and tourism financing. Output, the result of this research is recommendations for leader in travel and tourism in improving the performance of tourism finance, investments to maintain the financial sustainability of organizations (i.e., business, non-profit and government) involved in the travel and tourism sectors.

Keywords: Financing; Investments; Sustainable Tourism; Tourism Finance

INTRODUCTION

The tourism sector is ahead of the financial sector in recognizing the need to embrace environmental and socio-economic issues. Protection of the environment, cultural heritage sites, and local economies is so fundamental to tourism that the sector is more proactive when it comes to sustainable operations. However, like most other sectors, industries and companies, the lack of financing where tourism projects or initiatives lack adequate access to capital (at reasonable rates) in order to either finance activities, maintain the site, expand operations or discover potential tourist destinations.

Tourism finance is an area of finance dealing with managing the sources of finance and investments to maintain the financial sustainability of organizations involved in the Travel and Tourism Sector. The primary goal of tourism finance is to set criteria in which value-adding tourism projects should receive investment funding. Secondly, it evaluates a tourism organization's financial needs and raise the appropriate type of capital (i.e., debt and/or equity) that best fits those needs, rather than corporations alone, this relatively new field of study may also be also applicable to non-profit organizations and government that encounter financial problems related to the Travel and Tourism Sector.

According to Tugcu (2014), Balli & Curry (2015), tourism sector ranked fourth in world's largest export industry, after fuels, chemicals and food. While, the report of World Travel & Tourism Council (WTTC) reveals that Travel and Tourism totally contribute USD8.27 trillion, which is equivalent to 10.4% of GDP in 2017. WTTC also forecasts that its contribution will rise by 3.8% per year, and can reach to USD 12.45 trillion (11.7% of GDP) in 2028. Also, tourism also directly and indirectly creates around 323 million jobs, which is was 9.9% of total global employment; and this is expected to increase to 413 million jobs in 2028. According to WTTC, invesments pouring into travel and tourism has generated around 11% of economic output and supported 1 in 10 jobs in the global economy. Based on these great contributions of the travel and tourism sector, it will have a great impact on the development of a national economies given its strong growth in recent years.

This situation was described in the studies both in travel as well as the market developments. For example, Balaguer and Cantavella-Jorda (2002) earlier revealed that tourism and travel activities boosts Spain's national economic growth. Ohlan (2016) also showed evidence on the strong impact of tourism to the financial development and economic growth of India both in long-run and short-run. In a related study, Shahbaz et al. (2016) showed evidence that tourism as the key to enhace the overall income level. Lastly, Kumar (2014), stutdied Vietnam economic growth, and found that financial development positively affects both tourism and economic growth.

This study contributes to the literature by examining the decisions managers make in order to carry our sustainable tourism finance operations; and identifying possible sources of financing for tourism projects and initiatives

Tourism finance decisions are the processes involved in the responsible choices that relates to looking for potential investment alternatives that tourism organizations think; identifying financing options through borrowing (i.e., debt) and inviting investors (i.e., equity); and in minimizing the cost of financing, that is, looking for lower interest rates, and reducing the amount of cash dividends given, and instead going for stock dividends for high growth tourism projects.

Investment decisions in tourism initiatives are related to the control and distribution of assets in a tourism-related company, the structure of assets, and the risk of firm invesment percived by tourism investors. This is one of the most important financial decision in order to create and maintain the wealth maximization in tourism projects. A Tourism Financial Manager's investment decision is essential not only for the building of new infrastructures or setting-up of new projects, but also for the expansion of current assets, and replacement of permanent assets. Investments are also needed to comply to enviroment regulations, and adjust to related stakeholder interests.

Invesment decisions of Tourism Financial Managers can be classified into two major groups of choices:

Long-term investment decisions refer to capital budgeting related to travel and tourism fixed assets expenditure, wherein the financial manager must identify and recognize the expected benefit of different tourism projects received over a long period of time, or any tourism projects exceeding one fiscal year.

Short-term investment decisions relate to working capital management or the financing of current assets. Financial managers need to allocate cash and equivalents, and manage receivables and inventories on a daily basis. Tourism firms, especially related to services has fast turnover with high liquidity asset.

Investments in tourism-related businesses vary on the size of investments, and the level of decision-making; they can be clasified into:

Low-level or store level investments - This level of investment decisions are mostly handled by store managers. These includes the creation of new suitable units for inventories like shelves or tables for inventories; purchasing of equipment like t-shirt printing; buying new vehicle for company tours; and deciding the product/service range that should be offered in the store.

High level (Supervior level) - This level of investment decisions are mostly related to expanding the business by opening new stores in new market, new area; closing or continuing investing for expansion of current stores; purchasing, merging or acquiring other related business to support the firms development; and spending in the research and development for new products and services.

Once the tourism-related investment has been decided, the next step is how to identify the ways to finance the project. Financing decision relates to the selection of the way/s (i.e., debt and/or equity) to finance planned investments. Tourism firms have to be concerned about mixing sources of funds through borrowing or inviting investors to create the optimum capital structure. Capital raising can be through the issuance of shares of stocks (i.e., equity) and debentures or notes (i.e., debt). Funds can be accesed from long-term loans or short-term financing through invesments and banks. However, the debt-equity ratio should be concerned and maintained in suitable way to maximize the profitability. Debts are sometimes preferred by firms to increase their ROE (Return on Equity). However, it may increase the risk from the higher payment of interest and principal, and dependence on the conditions of lenders. Earlier, Tsai et al. (2011) reveals the disadvantage of high financial leverage from high borrowing cost which may bring default risk.

Other firms prefer raising funds through equity. Permanent earnings belong to shareholders (as opposed to lenders), however sometimes the rate of returns may not satisfy all investors. Thus, in order to protect and maximize the wealth of shareholders, it is important for a tourism financial manager to keep the balance between different capital sources, and to keep the risk under control. Serrasqueiro and Nuñes (2014), Pacheco and Tavares (2017) both studied the Portuguese small and medium hotels, and found that hospitality firms adjust the level of actual debt to the optimal debt ratio.

Cost of capital decisions relate to minimizing the cost of finance a capital budgeting project, such as building a new hotel or buying a fleet of tourist buses. The cost of capital from debt is the interest rate, while for equity, it's the dividend. The cost of capital metric is used by companies internally to judge whether a capital project is worth the expenditure of resources, and by investors who use it to determine whether an investment is worth the risk compared to the return.

Interest payments from borrowed funds are initially stipulated on the debt contract, and little adjustments can be made by the borrower to minimize the cost of debt. However, more flexibility is done through the distribution of dividends to investors. Since the tourism sector is one of the fastest growing sectors around the world, investors may expect for high and stable distribution. This decision has to be taken when the firms must decide to fund distributions and/or retained earnings.

According to signal theory, the higher rate of dividend can enhance the higher stock price, thus minimize the wealth of shareholders (Borde et al. 1999). However, according to Kim & Gu (2008), tourism is a business with high invesment opportunities, thus tourism companies may keep profits as retained earnings for new investments, which can lead to lesser dividend payouts, this idea is espcially true in case of small hospitality firms which likely in early growth stage. This is consistent with Canina et al. (2001), which showed that the average dividend payout of lodging firms often less than market's payout. The study also found that lodging industry often require high investments, making them to depend on debt with high interest payments. In a related study, Kim and Jang (2009) showed that dividend payments are affected by a firm's financial characteristic and previous dividend amount. Many companies use a combination of debt and equity to finance their businesses and, for such companies, minimizing interest payments and postponing cash dividends are the key drivers of growth.

METHOD

The method of this research is using qualitative research method with techniques of data collection by literature study and that were conducted by discussing seven potential sources of travel and tourism financing.

Those data were analyzed by giving descriptions for each items and expected through those items, leader of tourism, in this case government can be maximally utilized them as references to develop tourism sectors. Thus, tourism finance would be highly increased.

RESULTS AND DISCUSSION

Sources of Tourism Financing

The Travel and Tourism Sector business is in potential period for expansion. However, to expand, the sector needs to understand and solve the question of where to find the budget, and how to collect the funds needed for the invesment. This study enumerates seven possible sources of financing for Travel and Tourism initiatives.

Government Budget

Government's proposed budget has allocation for tourism in a financial year, which also estimates the anticipated government revenues and expenditures. According to the World Bank Tourism Report of 2018, the United States is still the biggest spender for Tourism, followed by China, Japan, France and Indonesia. See Figure 1 for the details. As an example, in 2015, the Indonesian government allocated around USD57.6 million budget to improve roads around Lake Toba, which is the largest lake in Indonesia, and also the largest volcanic lake in the world. The government is constructing a railway line connecting Medan and Lake Toba to improve the accessibility of the lake to

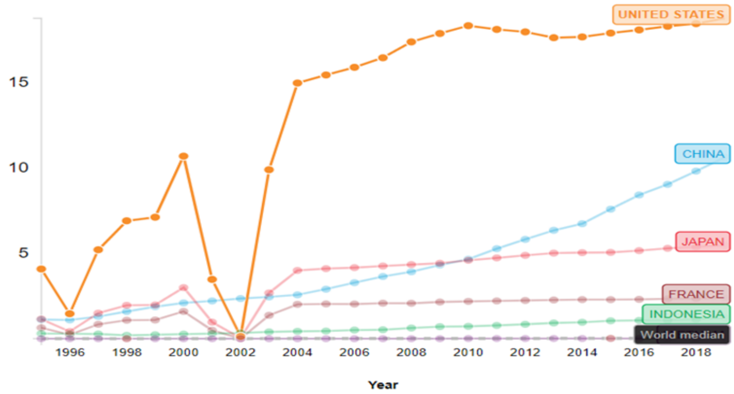

Figure 1

Government Spending On Travel And Tourism Service, USD (Billions)

Source: World Bank (2018)

tourists.

International Grant

International grants are non-repayable funds (or even products) given or disbursed by grant makers, which are often an intergovernmental organization (e.g., UNESCO), partner governments, corporation and foundation aimed at advancing tourism initiatives. For example, between 1975 and 1982, Borobudur's big restoration project received grants from Australia, Belgium, Cyprus, France and Germany. The grant shouldered the restoration cost totaling USD6.9 million (or USD18.1 million in 2018), which involved around 600 people. Borobudur is the world's largest Buddhist temple, and one of the greatest archeological sites in the world.

Development Bank Loans

Another source of tourism financing are loans provided by development banks (e.g., Asian Development Bank, and African Development Bank). These loans help developing economies, and normally are at very low interest rates (i.e., 1% to 2% per year on concessional loans), especially those aimed at developing tourism-related infrastructures and initiatives. In 2014, the Asian Development Bank and the Vietnamese government signed a USD50 million loan agreement to upgrade the country's tourism infrastructure, and create more tourism-related jobs.

State-owned Enterprises Funds

Grants or loans provided by state-owned enterprises (SOEs), aimed at financing the development of tourism-related projects and initiatives. One of the objectives of SOEs is to expand capital, and support government's plans for tourism, especially those in the emerging markets where tourism contribute to a significant part to the national income. SOEs not only work for their own profit, but also benefits the national or social development. For example. Pertamina's hotel operator, Patra Jasa, cooperated with the Indonesia Tourism Development Corporation to develop and maintain the tourism government website "exploreIndonesia.com" portal, which help to improve Indonesian tourism by showing information about major tourist spots, airlines and hotels. Another example is the Tourism Finance Corporation (TFC), a Kenyan state-owned corporation established in 1965, which facilitates and provides affordable development funding and advisory services for long-term investment in Kenya's tourism industry.

Private Domestic Investors

Investments from local private individual or companies are another option. These entities allocate capital for tourism-related projects with the expectation of a future financial return in terms of dividends and capital appreciation. For example, ANGIN (Angel Investment Network Indonesia) acts as a bridge to connect and facilitate investors and entrepreneurs; and provides investment-related services to both investors and entrepreneurs. In Indonesia, Blibli.com is an online shopping site owned by PT Global Digital Niaga, which benefited from Angel investments when it was still starting.

Private Overseas Investors

If investments can't be sourced locally, foreign private individual or companies that provide capital for tourism-related projects are another option. As capitalist, they also expect future financial return in terms of dividends and capital appreciation. For example, Travel Venture Capitalist, based in California, specializes in funding projects related to travel and leisure. One travel and tourism company called Flapper, a Brazilian company for on-demand flying services, including flights to locations inaccessible to commercial aviation; passengers can book affordable jet and helicopter flights to remote islands.

Commercial Bank Loans

If one can't still find financing from the above sources, commercial loans from banks offer services to small-, medium-, and large-sized businesses aimed at financing the development of tourism-related projects and initiatives. Indonesian Commercial banks are seeing challenges in the hotel industry. For example, they are considering the risk of lower occupancy rates during normal days, and not a 100% occupancy during holidays; and the threat of mushrooming cheaper options like guest houses, and transient hotels.

CONCLUSIONS

Educating leaders in the travel and tourism sector is becoming a much-needed skill in a world of constantly increasing competition in attracting tourists. Tourism Finance can become a possible new academic discipline dealing with managing the sources of financing and investments to maintain the financial sustainability of organizations (i.e., business, non-profit and government) involved in the travel and tourism sector. This field can also be involved in financing initiatives to discover new tourist destinations.

To sum, the seven potential sources of travel and tourism financing discussed in the study are the following:

a government's proposed budget allocation for tourism;

non-repayable funds (or even products) gifted or disbursed by grant makers, which are often an intergovernmental organization (e.g., UNESCO), partner government, corporation and foundation;

loans provided by development banks (e.g., Asian Development Banks) at very low interest rates;

grants or loans provided by state-owned enterprises;

capital from local private individual or company investors;

investments from international venture capitalists; and

loans provided by both local and international commercial banks.

Knowing these financing and investment alternatives would ensure that adequate access to capital is available to help keep sustainable tourism initiatives.

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