Executive Summary of Evaluation

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<th>Name of Evaluation</th>
<th>Poverty Literature Review Summary: Tourism and Poverty Reduction¹</th>
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Background

Investments in tourism have the potential to impact poverty both directly and indirectly. The literature review suggests that the direct ways in which tourism impacts the poor is through the significant linkages that the sector has upstream and downstream. These linkages with suppliers of goods and services, such as farmers, tour agents and artisans can have a potential impact in income for micro and small entrepreneurs. Jobs in the tourism sector are also more accessible to the poor as they require relatively fewer skills with employers providing the necessary training. Further, spending in the local economy by tourists can generate induced effects on job and income also.

Objectives

This note summarizes a literature review conducted by IFC on identifying the transmission links of the tourism sector to poverty and economic growth. This exercise was undertaken as part of IFC’s Poverty Action Plan, to better understand how IFC operations in specific sectors across its investment and advisory operations result in eradicating poverty and boosting shared prosperity.

Analysis

Indirect effects of the tourism sector to poverty

Development of the tourism sector has broad impacts on the macro and local economy which through growth will influence poverty. According to the World Travel and Tourism Council, travel and tourism generates about 12 percent of global GDP and contributes to an average of 40 percent of GDP in developing economies. It accounts for 66 percent of service exports in developing countries and is the main source of foreign exchange for 47 of the world’s 50 least developed countries. These statistics provide context to the indirect effects of tourism on an economy’s growth and hence the impact on poverty.

¹ This note has been summarized from the poverty literature review conducted for IFC by Hayat Abdulahi Abdo, Economist, Global Manufacturing, Agribusiness, and Services (CMGSF). The note is available on IFC’s poverty webpage: http://ifcnet.ifc.org/ifcint/deveffectiveness.nsf/Content/home
Beyond the increase in GDP and foreign exchange which can catalyze fiscal changes benefitting the poor, investment in the tourism sector also has trickle down effects through improvements in infrastructure, public and social goods. Change in the production structure in the economy can also be poverty reducing, specifically since tourism provides easy entry for unskilled labor, specifically women, which is discussed in the next section. Further, investment in tourism can indirectly induce investment in infrastructure which can have larger benefits to a wider group of people. Finally, taxes generated in the tourism sector are transferred to the local and national governments for the purpose of expanding public goods.

Direct effects of tourism to poverty through employment and entrepreneurship

Robust empirical evidence suggests that a substantial amount of the financial benefits from tourism flow to poor households (including unskilled and semi-skilled workers, and small enterprise and communities). Various studies have shown that the benefits accruing to the poor from the tourism flows range from 14 to 37 percent. These flows underline different transmission links:

**Direct effects:** Employment and wages for the poor is a critical path out of poverty and flow from tourists through hotel suppliers (restaurants, transport companies, etc.) to the poor. Jobs in the tourism sector are more accessible to the poor as they require relatively fewer skills with employers providing the necessary training. Employment in this sector is thus often regarded as the main contribution to the benefits of tourism to unskilled households. In countries with generous minimum wage legislations, tight labor markets and that require highly skilled staff, wages from formal sector employment can have a significant impact on the poor and can often lift a family out of poverty sustainably.

Besides wages from the formal sector, tourism can also *generate incomes to the informal, micro and small businesses.* For example incomes generated to people such as the tour guides, tourist taxi drivers, craft retailers, fruit and juice sellers, etc. For the poor that live around the tourist destination, studies show that this is the most successful channel of income flow from tourists to the poor.

**Indirect and induced effects:** Further income can be generated for the poor households through *local spending* by employees in the tourism sector. These indirect effects affect three main groups of the poor (a) farmers who sell food to hotels and restaurants. For example, *in Ethiopia, 90 percent of the food eaten by tourists is sourced locally, mostly from rural small-holding farmers and so approximately 44 percent of the total hotel expenditure on food was transmitted back to poor producers.* (b) the diverse range of micro and informal entrepreneurs that provide goods and services to the tourism sector (e.g. laundry, security, construction and consumable goods) and (c) finally the unskilled workers that supply inputs into the tourism sector such as construction, furnishing and light manufacturing.

Studies suggest that indirect effects are about 60-80% in size of the direct effects and the share of the benefits to the poor is much larger in the case of indirect effects than the direct effects. Of course, the size of this multiplier depends on several factors including the destination, local availability and quality of supplies, services and labor.
Conclusions and Recommendations

The literature review and case studies discussed above suggest a strong link between tourism and poverty reduction. The transmission links for the direct effects and indirect effects through linkages to the local SME’s and induced effects are clearer than the broader macro effects. Most of the people that benefit from the tourism sector are unskilled workers, informal and micro-entrepreneurs and small farmers, who service the sector in the supply and distribution chain or through induced effects, and who potentially fall in the base of pyramid. The challenge is to understand how to strengthen these links in order to maximize impact.

Further, while the dynamic effects of tourism on the economy can be significant, more could be done to better understand their link to poverty. The existing literature also doesn’t isolate the various income and employment effects for resort and business hotels and the literature on the absolute poor is also limited. These gaps point to potential areas of analysis for the sector towards better understanding the impact on the poor.

Poverty Impact of two IFC investments*

**Hyatt Regency in Kiev, Ukraine:** The 234-room Hyatt Regency is a centrally located business hotel in Kiev. IFC provided a long term senior loan of US$29.5 million towards total project cost (estimated at US$75 million) and it was IFC’s first investment in the hotel sector in Ukraine and the first branded 5-star hotel in Kiev. The hotel has created 500 direct jobs (62% Women); generates US$10 million annually for the local economy through purchases; pays the government around US$4 million annually in taxes and fees; and creates foreign exchange earnings of between US$25-30 million annually. A survey of hotel customers showed that they spend on average US$337 per day on transport, souvenirs, meals, drinks, communication, and other out-of-pocket expenses. This is estimated to generate an extra US$2.5 million going directly into the local economy. IFC’s value addition to the success of this project is significant. IFC shared its global expertise and knowledge of the sector and provided useful feedback the client both during project implementation and operation; this was particularly important for this client as this was its first venture into hospitality. IFC’s willingness to lend also attracted parallel lenders, enabling to complete the project financial plan. IFC’s environmental and social standards were important in ensuring issues like water quality were tackled effectively at an early stage of the project; these might have been expensive to resolve had they not been flagged early. These had strong demonstration effect by setting standards for subsequent investments in the sector in Kiev.

**Peru Orient Express Hotels (POEH), Peru:** POEH is a 50/50 joint venture between a local sponsor, Peru Hotels S.A., and Orient Express Hotels Ltd (“OEH”), an international operator of boutique hotels as well as luxury trains around the world. IFC provided financing towards the refurbishment of the Monasterio Hotel in Cusco and the Machu Picchu Sanctuary Lodge (MPSL) in Machu Picchu. The 123-room Monasterio Hotel and the 32-room MPSL have created 308 direct jobs, of which 23% are female, and the employees are paid wages 25% above the local market. Additionally, they receive additional remuneration from the 10% service charge levied and regular training. The hotel has contracts with about 50 local suppliers including farmers with the total annual purchase of about US$1.5 million. A survey of hotel guests showed that they spend on average around US$326 per day outside the hotel on souvenirs, transportation, tours, meals, etc., most of which are supplied by local micro and small businesses. OEH has brought higher customer service standards, hotel management and marketing techniques to Peru and thus changed the profile of tourists traveling to Peru by attracting upscale travelers with higher spending patterns and longer stays, which in turn will impact the flows to the local SME suppliers indirectly.

*The detailed case studies are available on the MAS website*