

## HISTORY

# A Travel Transformation in Emerging Markets

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I recently penned a blog on opportunities within [leisure and entertainment](#) in emerging markets, including the travel industry. With improved infrastructure and more access to reasonably priced flights, more travelers have been able to explore exotic locations they had previously only read about or seen on television. And, it is not just those in developed markets that are seeing the sights—many people living in emerging markets have more discretionary income available to enjoy leisure travel, too.

Traveling to and within emerging markets is now far easier and faster today than ever—in some places, gleaming airports and train stations even rival or surpass those of developed markets. When I first started doing research more than 40 years ago, air travel simply didn't exist in many developing countries. There were few airports and far fewer airlines. Airplanes were also less efficient and could not travel the distances they achieve now.

Infrastructure on the ground was similarly lacking, with poor roads and limited or no trains. One research trip I took to Indonesia back then offers an example of how difficult it was to get from place to place. My aim was to study soap manufacturing there, which required me to cover the entire country from the north of Sumatra down to the southern tip of Bali. There were few direct flights and travel involved small planes, buses, taxis, water ferries, motorcycles and even bicycles! My journey was often very exhausting before I even started my work.

I started in Medan and traveled to Palembang and other parts of Indonesia to visit the soap factories, often on bumpy dirt roads. There were not many hotels in the modern sense, so I stayed at traditional Indonesian inns (called losmen) which were small facilities, often an extension of someone's home.

Upon arriving in Bali, I discovered my passport was still at the losmen in Surabaya. In those days, it was customary for the losmen or hotel staff to take a guest's passport and keep it until departure. In this case, they had forgotten to give it back to me. In my rush to get to my next destination, I forgot to ask them for it when I checked out.

Losing my passport could have been a major disaster, but fortunately, the great kindness and hospitality of the Indonesians ensured its safe and swift return to me. The police in Bali were nice enough to help me call the losmen in Surabaya, and they sent my passport to Bali on the next bus. I had to delay my travels one day to wait for it to arrive, but I was so thankful to have it back, as I would not have been able to proceed without it.

Today, growing numbers of visitors from around the world are able to enjoy Indonesia's many attractions and travel more easily around the country than I did back in the day. The government has prioritized tourism, and it seems to be paying off—Indonesia jumped to 50<sup>th</sup> in 2015 from 70<sup>th</sup> in 2013 in the World Economic Forum's Travel & Tourism Competitiveness Report.<sup>1</sup> While more investment in infrastructure is needed in Indonesia, air travel has widely expanded. I can now visit several Indonesian companies in one day and use my own mobile phone to call for assistance or make arrangements in most parts of the country.

Tourism is important for Indonesia as well as many other countries in the Association of Southeast Asian Nations (ASEAN).<sup>2</sup> For example, travel and tourism directly or indirectly accounted for nearly 30% of Cambodia's gross domestic product (GDP) and more than 20% of Thailand's GDP, as of 2015.<sup>3</sup>

It's important to note that economists have found tourism has a great impact on a wide swath of the population through what they call the "multiplier effect." That is, tourist dollars reach directly into the retail and hospitality parts of the economy where many people in the middle- and lower-income groups are working.

Chinese tourists are venturing outside their borders in greater numbers and are a key part of tourism growth in Asia and other parts of the world. In 2000, nearly 10 million Chinese tourists visited ASEAN countries, but by 2015, the number had grown to 78 million.<sup>4</sup> The combined ASEAN destinations accounted for 21% of Chinese outbound visitors in 2015.<sup>5</sup> That being the case, it's worth looking at some travel and leisure trends and developments in China.

### **Travel In and Out of China**

The expansion of the travel industry in China is quite remarkable. During the National Day holiday in October 2016 (also referred to as "Golden Week") more than 590 million domestic trips were made nationwide in China, which was up nearly 13% from the same time in 2015.<sup>6</sup> Total tourism spending reached RMB 421 billion, up 14% from the previous year, and the Chinese spent a record amount of money on shopping and food during the holiday week, too. The Chinese aren't only traveling domestically during their holidays, either. Morocco was cited as a hot destination for Chinese tourists during Golden Week last year, and this year's Lunar New Year saw Chinese travelers flock to other countries in Asia as well as to Europe and North America.

Since 2004, China has seen double-digit growth in expenditure every year, leading the world in outbound travel.<sup>7</sup>



High-speed train, Guiyang, China station

Decades ago, leisure travel was unheard of for most Chinese citizens. Today, many Chinese consumers have more disposable income for travel and leisure. In 2001, just 3% of China's population was considered middle income, but by 2011, that figure rose to 18% of the population.<sup>8</sup> In absolute terms, that means more than 200 million people crossed the middle-income threshold.<sup>9</sup> While China boasts the world's largest middle-class population in absolute numbers, it is still below the global average in terms of percentages.

Nevertheless, per-capita disposable income has been on the rise in urban households, up some 165% from 2006 to 2015, reaching 31,195 yuan (US\$4,551).<sup>10</sup>

According to an *Economist Intelligence Unit* report, by 2030, 35% of China's population (representing around 480 million consumers) is expected to meet its definitions of upper middle-income and high-income, with upper middle-income consumers having a disposable income of RMB 67,000–200,000 (US\$10,800–32,100) and high-income consumers having a disposable income above RMB 200,000 (US\$32,100).<sup>11</sup>

### **Leisure Activities in China**

The development of leisure activities in China is ongoing, so I would expect more development in this area. China's government has mandated an increase in service industries as a percentage of GDP as part of an effort to transform its economy toward a domestic-growth orientation versus an export-oriented manufacturing one.

In southern China, Macau has developed a huge service industry based on gaming and is known as the “Las Vegas of China,” but it is morphing into a general entertainment center, which continues to grow. Macau (also spelled Macao) is a semi-autonomous region on the south coast of China that was a Portuguese territory until 1999. Today, it is formally known as the Macao Special Administrative Region of the People’s Republic of China.

On a recent visit to Macau, my colleagues and I visited a hot-springs resort that we had seen in the past. When it first opened about 10 years ago, the facilities were quite impressive, but maintenance had deteriorated since then and the once-crowded attraction had only a few visitors on this subsequent visit. It just goes to show that if you build it people may come—but you need to maintain it! As an investor, it also demonstrates the importance of seeing and assessing a situation first-hand. Even when something looks promising, conditions can quickly change. It’s important to uncover why.

Our travels to Hengqin Island in Zhuhai illustrated the improvements in infrastructure we have seen in the past few decades in the region. Zhuhai became a Special Economic Zone (SEZ) in the late 1970s with the government’s policy that opened a “window” to Macau and the outside world. The SEZs offered foreign investors special incentives, including more favorable tax rates and less red tape. Zhuhai’s SEZ status meant it would receive a boost in infrastructure spending, and we saw plenty of evidence of that.

Today, there are a variety of projects at various stages of development to advance key areas within the zone and aiding development of China’s coastal areas in particular. A Hong Kong-Zhuhai-Macau bridge and tunnel project is still under construction but nearly complete, and will link the regions more closely and likely invite even more visitors.

During my travels in and around China over the years, I’ve seen many new developments including new things to do and see—too many to count!

Those with antiquated notions of China will be greeted with fast, reliable bullet trains, gleaming shopping malls and impressive theaters, sports arenas and other attractions for tourists. There is still plenty of need for more infrastructure development in China. And if its consumer population continues to expand in numbers and purchasing power, no doubt, there will be many more changes and investment opportunities to come!



Riding the rails in China

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## **Important Legal Information**

All investments involve risks, including the possible loss of principal. Investments in foreign securities involve special risks including currency fluctuations, economic instability and political developments. Investments in emerging markets, of which frontier markets are a subset, involve heightened risks related to the same factors, in addition to those associated with these markets' smaller size, lesser liquidity and lack of established legal, political, business and social frameworks to support securities markets. Because these frameworks are typically even less developed in frontier markets, as well as various factors including the increased potential for extreme price volatility, illiquidity, trade barriers and exchange controls, the risks associated with emerging markets are magnified in frontier markets. Stock prices fluctuate, sometimes rapidly and dramatically, due to factors affecting individual companies, particular industries or sectors, or general market conditions.

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1. Source: World Economic Forum, "The Travel & Tourism Competitiveness Report 2015."
2. Countries in the Association of Southeast Asian Nations: Brunei Darussalam, Cambodia, Laos, Indonesia, Myanmar, Singapore, Thailand and Vietnam.
3. Source: World Travel & Tourism Council, "Travel & Tourism Investment in ASEAN," October 2016.
4. Ibid.
5. Ibid.
6. Source: China National Tourism Administration, October 2016.
7. Source: World Tourism Organization, data through 2015.
8. Source: Pew Research Center, "A Global Middle Class Is More Promise Than Reality," July 8, 2015. As defined in this study, people who are middle income live on \$10 to \$20 a day, which translates to an annual income of \$14,600 to \$29,200 for a family of four.
9. Ibid.
10. Source: China's National Bureau of Statistics.
11. Source: *Economist Intelligence Unit*, "The Chinese Consumer in 2030." There is no assurance any estimate, forecast or projection will be realized.