Most economic forecasters are offering similar lackluster predictions.

A *Wall Street Journal* poll of 56 economists forecast a 3.6% increase in Gross Domestic Product (the measure of all goods and services) this year, a little less than 2004.

The Business Roundtable, CEOs of 160 leading U.S. companies, projected healthy growth for the first half of 2005, down slightly from 2004, and the possibility of slower growth in the second half the year. Spokeswoman Johanna Schneider says the group expects GDP to grow 3.5% this year, slightly below 2004 and slightly above the 30-year average.

The Conference Board, made up of 100 top CEOs, is looking for somewhere between 2.5% and 4.5% growth this year. The key is how successful companies are in boosting prices. If price increases stick, expect higher growth. If consumers reject higher prices, growth will slow. "Even the most pessimistic case isn't all that bad," says Conference Board economist Ken Goldstein. "At the same time, we're not walking toward a pot of gold either."

The Travel Industry Association of America is more optimistic. A forecast released at TIA's 30th annual Marketing Outlook Forum in October 2004 noted that the year past was the year of recovery the industry has been waiting for. Travel expenditures were projected to hit $593 billion by the end of 2004, up 6.9% from 2003. An expected 5.3% increase in 2005 should bring travel spending to $624 billion.

But how forecasters come up with those predictions is a lot more complex than Goldilocks' story. And what the forecasts imply for specific industries such as travel, or individual sectors such as retailers versus hotels vs. airlines vs. tour operators, is more complicated still.

Everybody is affected by the economy, consumers, retailers and suppliers alike. Take oil prices, which boost the cost of fuel for airlines, hotels, tour operators and every other supplier. Higher supplier costs turn into higher prices or lower supplier profits, neither of which is good for travel retailers, who are also paying higher energy prices.

Exchange rates also play into the impact of the economy on travel. A weak

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PREPARATION AND RESPONSE

How should an individual business owner or manager respond to economic changes?

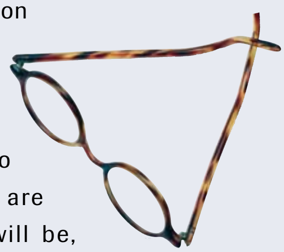
By working backward from visible effect – business is booming, business is flat, business is tanking – to the original causes. The goal is to determine what is likely to happen to the economy, then reposition the business to ride the new economic wave before competitors or clients even see the changes coming.

"One of your responsibilities as a business owner is to look into the future and prepare for it," explains Bruce Tepper, CTC, CITE, vice president of Joselyn, Tepper & Associates. "Listen to what the pundits are predicting, not because they are necessarily right, but because they establish general thinking patterns and mental tone. When it comes to discretionary spending, perception and expectations drive real expenditures. Whether people feel buoyant or not is more important that the actual numbers that get reported."

If the pundits who appear on nightly newscasts predict a bad economy, consumers tend to reign in discretionary spending, including travel – time to pitch tried and trusted products. When the pundits don rose colored glasses to predict boom times, expect discretionary spending to jump – emphasize those once-in-a-lifetime experiences. Whichever way the economy is moving, Tepper notes, emphasizing value over price is the key to maximizing profits.

Agencies with a strong local client base should also track the local business climate. Local industries can have a greater impact on local spending than national trends.

"If I had an agency in central North Carolina, I'd watch the furniture industry closely," Tepper says. "That's your window on future travel spending. An agency in Detroit should care passionately about auto sales. If auto sales are good, travel sales will be, too." - F.G.



The Travel Industry Association of America's most recent forecast for 2005 projects a fairly optimistic 5.3% increase over 2004, bringing travel spending to $624 billion.

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dollar has turned the U.S. into a bargain destination for Europeans. Currency trends are boosting business for U.S. hotels, car rental firms, tour operators, restaurants, and anyone else who sells to the inbound market.

Conversely, that same weak dollar has discouraged Americans from visiting Europe. Lower exchange rates also hurt tour operators and other suppliers with overseas operations by increasing their operating expenses.

Bottom line: If you work in the travel industry you need to pay attention to currencies and overall economic trends.

What To Watch

The problem is figuring out what to pay attention to. No economic indicator is an island. Trends such as rising profits influence other trends such as consumer confidence. Confident consumers tend to spend more, which encourages business investment and hiring, which plays into interest rates, which impacts inflation and productivity, all part of an ever-changing dance of trends and counter trends that makes economic forecasting as much art as science.

Winston Churchill reputedly complained when he asked two economists the same question, he got three different answers. More than a half-century later, government, industry and association economists unloose a growing barrage of economic indicators, statistics, polls, and opinions.

Goldstein, from the Conference Board: "The economic stewpot has three essential ingredients. Number one is material and commodity prices, number two is labor costs, and number three is productivity."

Schneider, from the Business Roundtable: "The basic driver is the uptick in global growth. Other major drivers of the U.S. economy include individual buying power and consumer confidence."

Not so fast, says Daniel Laufenberg, vice president and chief economist for American Express Financial Corp. He told Travel Professional that the major driver of the U.S. economy is the demand for U.S.-produced goods and services. "How successful we are at creating new products will be the primary source of job growth," Laufenberg explains, "while how successful we are at producing more with less (increased productivity) will be the key to keeping inflation low and remaining competitive."

Who is correct? All three. The cost of materials is vital to any business, be it the price of rare earth elements for computer screen makers or the price of computer screens for retail travel agencies. So are labor costs, productivity, consumer buying power, consumer confidence, product demand, new products, and inflation. And there are other factors shaping the economy, including demographics, political events at home and abroad, geography, consumer psychology, and disasters both natural or human-caused.

Practical Impact

Which factors are more important depends on where you stand in the economy. Since travel is largely a retail and service industry, factors that affect consumer spending are the most important. But even within travel, different sectors read the economic tea leaves differently.

Michael Palmer is executive director of the Student-Youth Travel Association. From his perspective, demographics rule. And demographics say today's seniors and baby boomers are on the way out. His market, travelers 26 years of age and younger, will be buying travel for the next 50 years.

"The youth market accounts for 20% of all travel dollars spent in the U.S.," Palmer says, "$110 billion annually. They are already the largest growth segment in the package tour market."

That's fine for 2025 or 2015, says Brent Green, author of *Marketing to Leading-Edge Baby Boomers*. But what about 2005 and 2010? Demographics rule, and demographics say today's baby boomers are the biggest and biggest-spending travel market in history – and they plan to continue traveling.

"The population is getting older every year," Green says. "You are talking about people who have proven that they are willing, even eager, to spend serious money on travel, even if they can't really afford it. Engaging aging markets is the key to success."

The New Decision Makers

The key is looking at both markets together. Boomers, born between 1946 and 1964, make up about 38% of the population, Green says, and control half the nation's disposable income. But their travel decisions are heavily influenced by Generation Y, young people born between 1980 and 1994.

"Mom used to make travel decisions for the family," Palmer says. "Now it's the kids. Their parents, Gen Xers and late Boomers, have the highest earning base in history. Their boomer grandparents have the highest asset base we have ever seen. And they are both spending it on the kids."

TIA statistics confirm that all three generations are buying travel. But not like they did five years ago.

"We have entered a new era of shopping behavior, characterized by a consumer who is much more cautious, who pauses before buying," says Candice Corlett, principal at WSL Strategic Retail in New York City. "There is a

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"We have entered a new era of shopping behavior, characterized by a consumer who is much more cautious, who pauses before buying. The new 'normal' is about making choices, about not having it all."

— Candice Corlett, principal, WSL Strategic Retail

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new normal, defined by frustration and reduced expectations for lives, jobs, savings, security, and shopping. The new normal is about making choices, about not having it all."

Terror, travel hassles, and war don't encourage consumer confidence, she explains, but the real roots of today's buying behavior are economic. WSL's biannual How America Shops survey points the finger at the dotcom meltdown of late 2000.

"People watched their paper wealth vanish," Corlett says. "It shook them to the core. Then you had years of headlines highlighting malfeasance by banks, churches, insurers, telephone companies, energy suppliers. September 11 didn't help, but economics drove the change."

Four years later, consumers are buying, but they are buying cautiously. Nearly 60% of buyers now pause and question need before buying. Two-thirds say it is important to get the lowest price. Over half will drive farther to get a lower price.

One piece of good news is that more people shop specialty stores. Price is important, but value – the relationship between price, product and experience – rules.

Corlett points to retailers such as Gap (clothing), Trader Joe's (groceries), and Circuit City (consumer electronics) who have convinced consumers that experience is more important than price. Travel companies have a strong incentive to use the same strategy.

That's because travel is suffering less than other sectors. Only 16% of consumers report canceling or postponing travel, Corlett noted. That compares with 28% who are driving less because of higher gas prices, 31% who have postponed a major purchase, and 61% who reported changing their buying habits.

Not too hot, not too cold, and Goldilocks may have had it right after all.

7 Seven Measures: **What To Watch**

You work or own a business in the travel industry, and you know you need to keep a watchful eye on the direction of the economy. But what, exactly, should you track among the dizzying array of indicators?

While there are no hard and fast rules – and the economic fortunes of your local area should figure into the mix – Vince Wolfington, chairman of the World Travel & Tourism Council and CEO of Carey International, keeps track of seven measures to forecast the economy and travel sales.

- Low or falling **commodity prices** indicate an upbeat economy. Conversely, high commodity prices are a drag on profits.
- Falling or flat **interest rates** are another positive sign. Rising interest rates, especially sharp increases, slow investment and employment.
- Low or falling **inflation** is good. Rising inflation is tolerable in the short run as long as increases are slow and slow.
- **Stock market trends** telegraph economic expectations. Don't worry about day-to-day changes, Wolfington cautions, but a long-term upward trend suggests a growing economy.
- **Consumer confidence** predicts discretionary spending. The more confident people feel about the economic future, the more they spend.
- Changes in the **GDP growth rate** indicate whether consumers have more or less money to spend now and what they're likely to have in future.
- Wolfington's final predictor is the **political climate**. Consumers spend more freely when the political process moves with a minimum of rancor, infighting, and finger-pointing.

Wrapping it all together, at the end of 2004, he notes, commodity prices, interest rates and inflation were all rising slowly, the stock market was flat to slightly up, consumer confidence was up somewhat, economic growth was up over 2003, and the political climate in Washington was murky.

"Travel and tourism is back," he concludes, "but it is back compared to 2003, when things were terrible. I don't see any indicators that tell me 2005 is going to be anything great, but it's not likely to be terrible, either." - F.G.