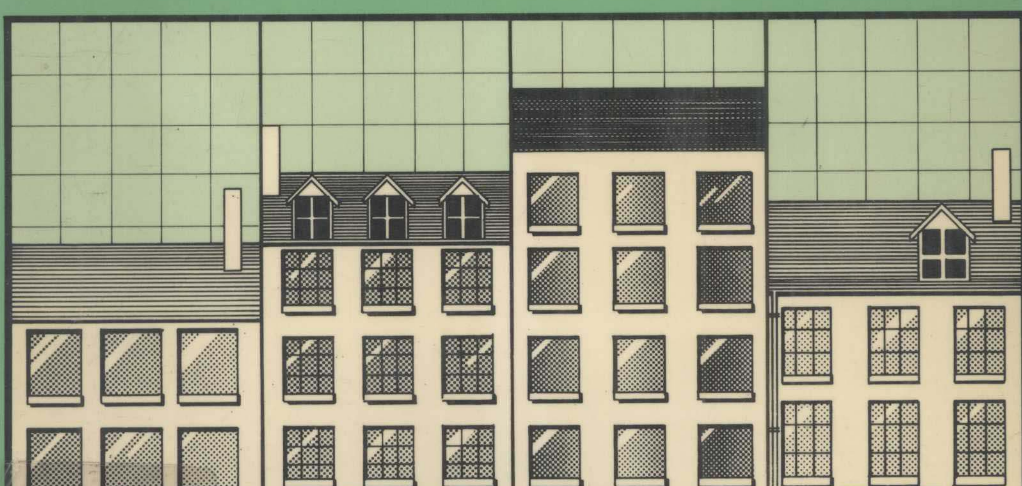
ECONOMICS FOR HOTEL AND CATERING STUDENTS

HOWARD L. HUGHES



Economics for Hotel and Catering Students

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Preface

Many economics textbooks start with a reference to the inadequacy of existing textbooks for the author's purposes. I make no apology for offering exactly the same reason for writing this one. Over several years of lecturing to students on hotel and catering management courses, I have felt that current books are not appropriate. What is the starting-point for this belief?

Students on hotel and catering management courses are usually highly motivated towards a career in that industry; they often see their courses as vocational and not always as educational experiences. They have not come on such a course with the primary intention of studying economics and may regard it as a 'necessary burden'. They may not always see it as being as relevant to their future careers as, say, law or accountancy. In the process of attempting to demonstrate relevance and stimulate interest, a lecturer may find that the economics input becomes 'watered down'.

It is not an easy task to develop an economics input which combines the essential strengths of economics and the unity of the subject with meeting the demands of students. At the heart of the problem is the need to provide a meaningful and significant economics input on a highly vocational course.

I am certain that economics should be an input to such courses since it can:

- Create an awareness and understanding of the economic environment within which all organizations operate.
- Create an awareness and understanding of the interactions between that environment and the organization.
- Introduce the methodology and those concepts of economics that may be pertinent for problem-solving and decision-making in organizations.

The traditional economics course is not particularly appropriate, however, for the education of future managers (regardless of the perceptions of the students themselves). Much of a conventional economics course is fascinating and intellectually stimulating in its own right and is valuable in developing certain 'higher-order' abilities. It may, though, be too abstract, theoretical or remote to be of much direct managerial use.

Industrial economics has some attractions in that it discards much traditional model-building, and emphasizes observation of reality. It is more likely to deal with 'what is' rather than 'what ought to be' and therefore might be appropriate for such vocational courses. But a 'pure' industrial economics course is not necessarily any more appropriate than is a 'pure' conventional course because much of the empirical work undertaken may not be of direct relevance to potential management either.

Another possibility is to move towards an economic study of the hotel and catering industry. A major difficulty is that the industry has not been subject to economic analysis of a nature or on a scale sufficient to write about 'the economics of the hotel and catering industry'. Such an input could therefore become descriptive and a catalogue of technical factors to the exclusion of economics.

If it were possible to present an input of 'the economics of the hotel and catering industry', it is arguable whether even that could provide an adequate economics education. It could, in isolation, present a distorted view; it would be easy to lose sight of the 'whole' economic picture and to fail to view the industry in context.

The industry should, however, form some part of the economics input. A study of the industry should generate interest in the student and demonstrate relevance.

It would seem that the best way forward, at present, is to adopt an amalgam of conventional micro-economics, industrial economics and the hotel and catering industry. The hotel and catering industry will not be the main focus of study but should be introduced as and when appropriate. This is the basis of this book.

There has been here at the polytechnic, and at other centres of hotel and catering studies, a continuous examination of economics, and of its structure, content and approach. It would be a foolish person who could claim that this process could now cease; this book represents only the latest stage of my thinking and I have no doubt that within a year or two I would have written something different.

I have, in this book, been selective in what I have included. Generally I have used the 'need to know' criterion in deciding what to include; I have interpreted that 'need to know' in a sense that goes beyond the immediate 'demands' of hotel and catering students to those wider issues which might be desirable in the *education* of future policy-makers. The selectivity may give rise to some lack of cohesiveness but I hope the benefits will outweigh any problems.

There are omissions compared with a conventional economics textbook (e.g. indifference curves, isoquants, etc.) and there are some concepts and theories which are only lightly touched on. Conversely, there are certain parts of this book which may not be touched on in conventional books (e.g. development of tertiary sectors) and parts which expand on what might be found in conventional books.

I have tried to avoid theories for their own sake, unnecessary jargon and complex model-building. I believe economists have often succeeded in surrounding the subject with a mystique that needs to be stripped away. There is always a temptation to avoid economic theory completely but it is important that students appreciate the theoretical underpinnings of 'the real world'. It is impossible to fully comprehend the complexities of reality without recourse to a theoretical framework.

I have also kept away from descriptive detail in the belief that principles and theories can be enduring whereas description is not. This book is certainly not a description of the hotel and catering industry. The book may appear to some to be too theoretical but students should find it less abstract than many conventional economics textbooks and at the same time more applicable to their industry.

Where the hotel and catering industry has been introduced in the text, I have usually confined my consideration to the 'commercial' sector and within that to accommodation and catering. Welfare and industrial catering and pubs and clubs are covered only briefly in this book.

The economics framework adopted is one that can be applied to other industries and this should facilitate interindustry comparison and set the industry in context. As noted earlier, there is a dearth of economic studies of the industry and the book is, in this sense, clearly not complete. Many of the relationships and activities identified here could form the basis for future empirical work within the industry. At this stage, however, in several parts of this book, it cannot be claimed that there is more than a juxtaposition of theory and conjecture about what happens in the hotel and catering industry. Much more needs to be done if the industry is to be analysed from an economic perspective.

The book, then, is not a book about the hotel and catering industry or its economic aspects, nor is it a conventional economics textbook. It is an economics book for students on hotel and catering management courses.

In particular, it should meet the needs of students on BTEC higher national diploma courses (Structure and Resources units), those studying for 'the Industry' paper of the HCIMA, students on hotel and catering degree courses and those on post-graduate hotel and catering courses. The input of economics is relatively minor on such courses and it is envisaged that the book would be the basis of a 60–90 hour module. With some judicious selection, the book could also be useful to students on diploma courses.

No prior economic knowledge is assumed, though a lecturer is entitled to expect that such students will have some degree of familiarity with current economic events. I have deliberately avoided recourse to mathematical representations of economic relationships as I have never been convinced that it assists the average student to understand economics.

This book has tried to steer clear of those aspects of hotel and catering which are rightly the concern of others – such as marketing, operational research or accountancy. I have tried to concentrate only on the contribution that economics can make. If students succeed in recognizing that other subjects they study have equal or more important contributions to make to particular topics, so much the better.

I have not, either, considered macro-economics at any length. This is not because I believe that it is of little significance but because I believe there is 'no need to know' the fine detail. A detailed study of macro-economics, even at the level encountered in most basic economics textbooks, may be more than is necessary. If lecturers feel otherwise, there are many fine textbooks that can serve.

H. L. Hughes

Acknowledgements

The book is an eclectic one and I must acknowledge my debt to many authors. The sources cited in footnotes and elsewhere will indicate the extent of this debt.

In particular, I must acknowledge that *Profile of the Hotel and Catering Industry* by S. Medlik (with D. W. Airey) has been a starting-point for much of what I have written. On the economics side, my greatest debt is to R. G. Lipsey's *An Introduction to Positive Economics* and to A. R. Prest and D. J. Coppock's *The UK Economy: A Manual of Applied Economics*; both were in their first edition when I was an undergraduate and I am very much their product. The contribution of *An Introduction to Industrial Economics* by P. J. Devine *et al.* has been significant more recently.

On a more personal level I gladly recognize the contribution made to this work by my colleagues – Gary Akehurst, Stuart Horsburgh, Anne Minter, Graham Stone and the late Jack Clare. They have all helped me in many ways, especially by discussing the different approaches to hotel and catering economics.

Students who have endured my experimentation in approach and content over the years deserve a special commendation. They have patiently tolerated and humoured me and even, on occasion, allowed me to believe I was making a valuable contribution to their education.

The library staff at the Hollings site of the polytechnic have been invaluable. Led by Lynn Elliott, they have always been courteous and co-operative; without their willing and cheerful assistance the work would have taken a great deal longer to complete.

My special thanks to Madeleine Barry for turning the most appalling scrawl into her usual impeccable typescript.

Finally, in the true tradition of authors, I reserve most thanks for my wife, Marion, and children, Andrew and Claire, each of whom would like to become more regular customers of the hotel and catering industry. They have inspired and encouraged throughout, as well as served to remind me that there is more to life than economics.

All errors, omissions and misjudgements in the book are, of course, my responsibility entirely. I hope that students and lecturers will not hesitate to bring them to my notice at the earliest opportunity.

CHAPTER 1

Industry

Services

Economics is often considered to be concerned with a study of the way in which individuals, organizations and countries seek to overcome the problem of 'scarcity'.[1]* There are not enough resources available to satisfy the wants of everyone, whether that availability is judged at the level of the individual or of the world as a whole. Those resources which are available to be used in satisfying wants are generally classified as:

1 *Land:* all of the natural resources such as coal, iron ore, fish, water, as well as the land itself and all that grows on it.

2 *Labour:* all human resources, whether skilled or unskilled.

3 *Capital:* all man-made resources in the form of physical assets such as factories, shops, hotels, restaurants, machines, tools, etc.

In addition, a fourth category is sometimes identified, namely 'enterprise'; this is the resource that is considered to take the initiative in bringing together the other resources. It may usefully be included under 'labour'.

However classified, such resources are required in varying forms and proportions if wants are to be satisfied; collectively they are known as 'factors of production'. There is at any one time a fixed quantity of these factors which can be used to satisfy wants, but there are an apparently unlimited number of demands upon these factors. Somehow these unlimited wants and the limited factors have to be reconciled. The economic problem is thus basically one of allocating the scarce resources between competing demands. All wants cannot be satisfied at the same time and choice is necessary:

1 Which goods and services are to be produced and thus which wants satisfied?
2 How are these goods and services to be produced, out of the wide range of technically possible means of production?
3 Who is to receive the goods and services once they are produced?

* References and notes are collected in a section beginning on page 222.

Since resources are so scarce, it is essential that the best possible use is made of them so that maximum satisfaction is obtained; i.e. the allocation of resources needs to be 'optimal'.[2] (See also Chapter 2.)

Basically there are two ways in which an economy might seek to attain this 'optimal resource allocation'. It may operate as a 'market' or 'free enterprise' economy where the unrestricted operation of the price mechanism allocates resources, or it may be characterized by rather more intervention and operate as a 'command' or 'planned' economy, such that some central body allocates the resources. Neither alternative exists in an extreme form in any economy and each economy is a mixture of both systems. Which one is better in terms of achieving an optimal allocation is largely a matter of personal judgement.

All economies, however, are characterized by an output of goods and services to meet wants. Ultimately production, i.e. the transformation of factors into an output, takes place to provide for the wants of the population. These wants may be satisfied by an output of goods or by an output of services. The basic difference between the two is that goods have a physical dimension and are tangible, whereas services do not have such characteristics and are 'invisible'.[3] (In practice, the distinction is not so clear-cut.)

Both goods and services can satisfy wants and they are both capable of being bought and sold. Both thus contribute to the generation of employment and of income in an economy. The fact that services are not reflected in some physical object does not detract from their 'economic worth' in any economy. There is sometimes a tendency to dismiss service producers as being 'unproductive' with the 'real' wealth being generated by the producers of goods. In economic terms, as has been seen, this is not so. Economic activity occurs through the production of goods and/or services. Wants can be met by goods and/or services and it is the fulfilment of such wants that is the objective of economic mechanisms.

Such a view does not imply any judgement about whether services are 'desirable' or 'useful' since these are matters for the individual's value judgements. For instance, the provision of luxury hotels in tourist resorts in some of the poorer countries of the world may be considered undesirable by some, though it remains an economic activity. It may be that some services are considered by some to be more 'useful' than others. Banking and insurance, transport and communications may be vital if manufacturing is to function effectively, whereas other services such as restaurants or entertainment may be less vital and rather more 'frivolous' activities. This will be returned to later when some evaluation of the 'usefulness' of hotel and catering activities in particular will be made. (See Chapter 9.)

The service economy

If any economy is examined it is apparent that its output is a mixture of both goods and services. Table 1 refers to gross domestic product (GDP) which, put simply, is a measure of the economy's output in a year. (See Chapter 8 for further discussion of this.)

Table 1 *Gross domestic product (GDP) by industry – UK 1982.*

		% of GDP at factor cost	
(a)	Agriculture, forestry and fishing	2.4	
(b)	Extraction of mineral oil and natural gas	6.0	
(c)	All other energy and water	5.2	
(d)	Manufacturing	24.3	
(e)	Construction	5.8	
(f)	Distribution, hotels and catering; repairs	12.9	
(g)	Transport	4.4	
(h)	Communications	2.9	
(i)	Banking, finance, insurance, business services and leasing	12.5	
(j)	Ownership of dwellings	6.3	55.1%
(k)	Public administration, national defence and compulsory social security	7.2	
(l)	Education and health services	9.0	
(m)	Other services	6.2	

Source: Central Statistical Office, *Annual Abstract of Statistics – 1984 Edition* (HMSO 1984).

The forms of economic activity that are found in an economy can be grouped into three categories:[4]

1 Primary sector, i.e. mostly made up of agriculture, forestry, fishing.
2 Secondary sector, mostly made up of manufacturing.
3 Tertiary sector, i.e. services (categories (f)–(m) in Table 1).

The tertiary sector includes among others, transport and communications; banking and insurance; education and health; retailing and wholesaling; public administration and defence; as well as the various elements of hotels and catering.

Different studies of economies have included different activities in each of the sectors: construction is sometimes included, for instance, and transport and communication sometimes excluded.[5] Some of the services have been separated out into 'quaternary' and 'quinary' sectors but these terms are not widely used and all services will here be designated tertiary activities.[6]

Economies in the 'developed' world have passed through stages when different forms of economic activity have been dominant. For instance, the UK was a 'primary' economy before the Industrial Revolution of the late eighteenth and early nineteenth centuries and was dependent upon the

Table 2 *UK employees in employment by sectors*

	1961	*1981*
	(% of all employees)	
Agriculture, forestry and fishing	3.2	1.7
Manufacturing	38.4	27.2
Services	46.6	62.9

Source: Central Statistical Office, *Social Trends*, No. 14, 1984 Edition (HMSO 1983).

Table 3 *Relative importance of services and manufacturing in total output*

	1960	*1982*
	(% of economy total)	
Manufacturing	37	24
Services	45	55

Source: *Economic Progress Report*, No. 165 (HM Treasury February 1984).

'secondary' sector after the Industrial Revolution until it may now be considered a 'service' or tertiary economy. (The phrase 'post-industrial' society[7] is slightly misleading in the economic context, but refers to a similar emergence and dominance of services.) Currently, most developed economies are characterized by a very large proportion (if not the majority) of the labour force being employed in the tertiary sector. Well over half of the UK working population is currently employed within this sector (see Table 2). It also accounts for a very large and growing proportion of the output (GDP) of the country: 55 per cent of GDP in 1982 (see Tables 1 and 3).

What has caused this emergence of the tertiary or service economy?

Influences on the service economy

At any one time the proportions of employment and output accounted for by the tertiary (or any other) sector in different countries will differ according to the individual characteristics of each country, but there seem to be a number of common influences that have served to bring about the service economy.

1 There is a tendency for consumer expenditure to alter in structure as changes occur in consumer incomes (in particular, real disposable income of consumers, i.e. income after deduction of income tax and national insurance and after allowance for inflation).

Table 4 shows how the relative importance of various forms of expenditure

Table 4 *Pattern of household expenditure 1960–82*

	1960	*1970*	*1980*	*1982*
	(each category as % of total expenditure)			
Housing	9.3	12.6	15.0	16.6
Fuel, light and power	5.9	6.3	5.6	6.2
Food	30.5	25.7	22.7	21.1
Alcoholic drink	3.2	4.5	4.8	4.6
Tobacco	5.9	4.8	3.0	2.9
Clothing and footwear	10.3	9.2	8.1	7.2
Durable household goods	6.3	6.5	7.0	7.2
Other goods	7.1	7.4	7.9	7.5
Transport and vehicles	12.2	13.7	14.6	14.8
Services	8.9	9.0	10.8	11.5
Miscellaneous	0.4	0.3	0.5	0.4
	100.0	100.0	100.0	100.0

Source: Department of Employment, *Family Expenditure Survey, 1982* (HMSO 1983).

has changed over a twenty-two-year period. Housing, durable household goods (TVs, cameras, washing machines, etc.), transport and vehicles, and services, in particular, have risen in importance, whereas food, tobacco and clothing and footwear have shown a particular fall in importance. This does not mean that consumers have spent less on these categories but rather that the rate of growth of expenditure on them has not kept up with the growth of expenditure on other items – and therefore their relative importance falls.

As consumers become better off and able to purchase more goods and services, the pattern of consumer expenditure usually alters. The proportion of expenditure or income spent on food, for instance, usually diminishes (from 30.5 per cent in 1960 to 21.1 per cent in 1982, see Table 4) and gradually services begin to emerge as significant items of expenditure. New, higher-level wants, perhaps non-essential, can be satisfied. The consumer is no longer preoccupied with basic nourishment and shelter and new demands emerge. (Whether these new demands arise 'naturally' within the individual or are originated by the producers themselves is arguable.)

It is noticeable though, in most studies of the industrial structure of economies,[8] measured in terms of contribution to output, that there is a common tendency towards a reduction in the importance of the primary sector, a rise in the relative size of secondary activities and an initial but *not continuing,* rise in the importance of the tertiary sector. There seems eventually to be a flattening-out of the share of tertiary activities in total output.

Consumer expenditure, after a certain point, shows a continuing and similar rate of increase in the demand for *both* goods and services, without the demand for the former falling relative to the demand for services. In developed