



ECONOMIC ANALYSIS OF TOURISM CONSUMPTION DYNAMICS: A Time-varying Parameter Demand System Approach

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Abstract: This study considers the dynamics of the consumption behaviour of tourists from an economic perspective. The evolution of various demand elasticities is explored using a time-varying parameter almost ideal demand system model. The top four source markets for tourism in Hong Kong are examined, and three major tourist expenditure categories, including shopping, hotel accommodation and meals outside hotels, are investigated for each market. Elasticity analysis reveals different consumption trends and patterns across the source markets. The findings will serve as a useful reference for Hong Kong tourism-related industries and the government in their efforts to enhance the competitiveness of Hong Kong as an international tourism destination. **Keywords:** tourism consumption, time-varying parameter, almost ideal demand system, demand elasticity, evolution, Hong Kong. © 2011 Elsevier Ltd. All rights reserved.

INTRODUCTION

International tourism plays an increasingly significant role in national and global economies. Tourist expenditure on shopping, hotel accommodation, food services, transport, visitor attractions, entertainment and so forth contributes substantially to developing and developed economies by generating gross domestic product (GDP), creating employment and providing socio-economic development opportunities. In 2008, more than 80 countries earned over US\$1 billion from international tourism, with worldwide receipts reaching \$944

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billion (UNWTO, 2009). Given the importance of tourism consumption to a destination's economy and its direct link to the performance of tourism-related businesses, tourism demand analysis has attracted increased attention from both academics and practitioners. It is of great importance to study the consumption behaviour of tourists from an economic perspective. The economic study of tourism is set within a well-established academic discipline, with a firm theoretical foundation and well-tested methodologies (Stabler, Papatheodorou, & Sinclair, 2010). In this discipline, the modelling of tourism demand "is one of the most developed and rigorous areas of the economic analysis of tourism" (Stabler et al., 2010, p. 425).

In particular, demand elasticity analysis can be used to assess tourists' consumption behaviour scientifically and to generate useful managerial implications for tourism-related industries and tourist destinations. Various demand elasticities, such as income elasticity, own-price elasticity and cross-price elasticity, can be calculated based on an estimated demand model to determine the sensitivity of tourist demand for tourism goods and services to changes in a tourist's disposable income, the price of tourism products and the price of alternative consumption products. Such analyses can help tourism organisations to manage and promote a destination effectively in a competitive environment, and can guide tourism service providers in setting appropriate pricing strategies (Cortés-Jiménez, Durbarry, & Pulina, 2009).

This study aims to provide new insights into the dynamics of Hong Kong inbound tourists' consumption behaviour regarding a group of tourism goods and services and to evaluate the competitiveness of Hong Kong as an international tourist destination. The remainder of the paper is organised as follows. In the next section, a brief review of the relevant literature on tourism consumption is provided, with a particular focus on past empirical studies using the almost ideal demand system (AIDS) model. Section 3 includes the discussion of various versions of the AIDS model, followed by an introduction to the empirical research design and data collection. The results of the empirical study are presented and discussed in detail in Section 4. The concluding remarks and managerial implications of the study's findings are presented in Section 5.

RELEVANT LITERATURE

A variety of modern econometric approaches have been employed to model the relationship between tourism demand and its economic determinants. These include the autoregressive distributed lag model, error-correction model, vector autoregressive model and system-of-equations approach (see Li, Song, & Witt, 2005, and Song & Li, 2008, for comprehensive reviews of the application of these methods in tourism demand analysis). The system-of-equations approach in particular has several advantages over its single-equation counterparts. By including a number of tourism goods and services, such as restaurant dining and hotel accommodation, in the system and estimating them

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