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Issue 6 – July 2005

Executive Report

The magazine for the Tourism, Hospitality and Leisure industry

Reaching your target

The challenges of building health and fitness club membership

Getting personal

Who are your customers?

Audit.Tax.Consulting.Corporate Finance.

Issue 6

July 2005

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Welcome

Seeing the potential in the travel, hospitality and leisure industry

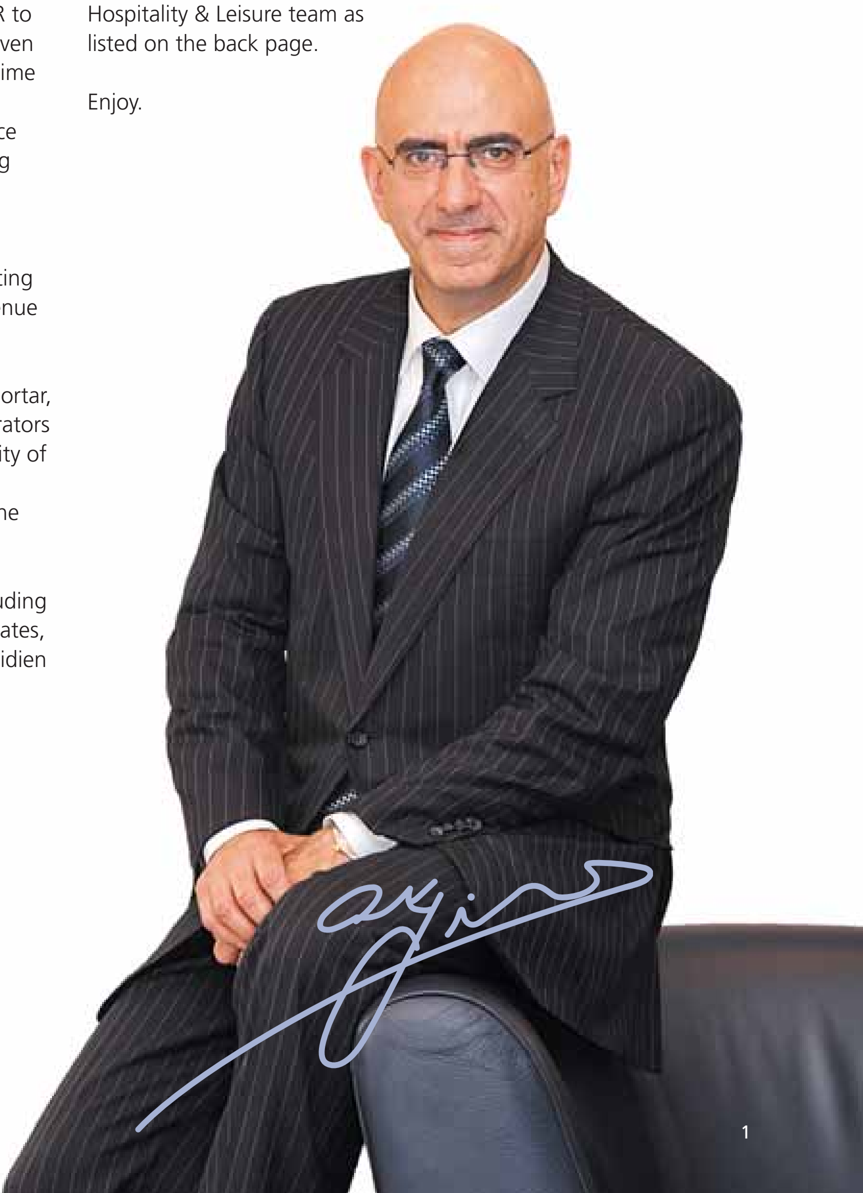
Something very strange has happened since our last edition six months ago - no major catastrophes! I know I am tempting fate to say that we seem to be heading towards a sustained recovery in our industry, but the most recent trends show:

- Airline travel is well up on the first 6 months of this year with a year on year RPK increase expected to be around 9% and the outlook shows continued growth across all markets. However, rising fuel prices are a major concern and many of the US carriers are still grappling with loss making operations
- The hospitality industry has bounced back in terms of RevPAR to almost pre-S11 levels, albeit at a lower level of profitability given increases in the cost base over the past 4 years. For the first time in the industry's history, we have a global operator - Marriott International - providing the market with profitability guidance into 2008, a positive note of confidence for the future. Falling supply of new products in the USA and Europe will further underpin growth in RevPAR into the future
- The cruise line industry is booming with the duopolists reporting record earnings. Supply constraints mean that cruise net revenue yields should continue to rise well into the future
- The global gaming industry is booming, both in bricks and mortar, casinos and on-line, with a number of the major on-line operators contemplating an IPO. While questions remain over the legality of on-line gaming for US nationals, the possible flotation of the major operators will result in multi-billion dollar entrants to the stock markets
- M&A activity is bubbling up with a spate of recent deals including Cendant's acquisition of eBookers and Gullivers Travel Associates, Marriott International's joint venture with Whitbread, Le Meridien and Wyndham, to name a few.

The encouraging trends are providing our industry with a much needed respite from fire fighting and an injection of profitability. However, this is not the time for complacency. Oil prices are on the rise, many of the European economies are still in the doldrums and consumer confidence, even in the most robust economies in Europe, is faltering. This is the time for our industry to catch-up on investment in the brands, customer relationships and people, the key drivers of success in a rapidly changing world.

As always, we welcome your feedback. Please contact me on akyriakidis@deloitte.co.uk or any members of our global Tourism, Hospitality & Leisure team as listed on the back page.

Enjoy.



Country snapshot

Canada – the country's your oyster

Why it's still one of the top ten travel choices

Tourists don't need to make a world trip when they can find everything in one country. The incredible diversity of Canada and its population provide every outdoor adventure and cultural experience imaginable – from skiing to hiking and white water rafting, and from high-fashion shopping to multi-cultural festivals.

Canada is the ultimate variety destination. It's been ranked within the top ten travel destinations consistently since 1990, with 20 million international tourists arriving every year. Importantly, it's considered a safe place to visit and exchange rates make it an affordable choice.

Tourism – one of the largest providers of jobs in Canada – is vital to the country's economy and in this article, we consider why Canada remains such a popular choice for international and domestic travellers.

Multiculture, multichoice

The country is marked out by the world's largest navigable coastline. It's the second largest nation in the world but with one of the lowest density populations – 32 million – making it incredibly appealing to both immigrants and tourists.

The population is so ethnically diverse – supported by an unprecedented code of multiculturalism – that more than 100 languages are spoken in a patchwork of ethnic communities and mini-cities flourishing within cities.

The west coast has three magnificent mountain ranges and more than 650 parks and recreational areas. The east coast boasts more than 90 sandy beaches for swimming and boating and some of the friendliest people on earth. In between, the pristine prairies, the remarkable great white north, and outstanding urban cities offer unrivalled sightseeing, sports events, adventures, and cultural experiences.

Such diversity, in terms of landscape and people, makes Canada a unique travel destination. Domestic tourists enjoy the discovery of different cultures, especially in the major cities, while the millions of international visitors can take their pick of cultural or landscape backdrops. Overall, Canada's reputation as a safe, open-minded and inexpensive place to visit, gives both domestic and international visitors a travel package that's hard to beat.

The great outdoors

While Canada's biggest cities; Toronto, Vancouver and Montreal, are the main tourist destinations, the great outdoors also has millions of fans. More than 50% of Canada's land is blanketed with rich forest ranges, accounting for 10% of the world's remaining forests and 20% of the world's remaining wilderness areas.

Tourists come to enjoy nature and ski, snowshoe, hike and camp in the great Canadian Rocky Mountains, relaxing in the quality amenities provided in the resort towns of Banff, Jasper, Lake Louise and Whistler – considered one of the best ski resorts in the world. In British Columbia, it is possible to ski, golf and enjoy a gourmet meal in a bistro all in one day. And the northern territories, namely Yukon,

Northwest Territories and the polar desert of Nunavut, offer the chance to see wildlife such as muskoxen, caribou and polar bears, and take part in fishing and hunting excursions.

Travellers can bike or drive along outstanding coastlines, including the perimeter of Newfoundland on the east coast where the Vikings first set foot on the shores of the New World, 500 years before Columbus. Here, visitors can see the jagged cliffs overlooking the Atlantic, primeval boreal forests, mammoth icebergs drifting offshore and whales and other marine life.

There are thousands of rivers on which to canoe and whitewater raft, and two million lakes where cottages and boats can be rented. One of the most popular outdoor destinations is Niagara Falls, the largest waterfall in the world by volume, averaging a deluge of 2,538 cubic meters of water per second.

Few other countries offer the choice of beachfront vacations, ice-fishing excursion, ski trips, wine tours – plus the chance to schedule in stopovers in cities that offer diverse, world-class dining and great sightseeing.

Multi-cultural harmony

In the next decade, around a quarter of Canada's population will consist of highly-visible minorities. China and India are the two main sources of immigrants, but others include Korea, the Middle East and Western Asian. The official policy of multi-culturalism enables people to celebrate their heritage while promoting racial and social harmony.

This has created a diversity of cultures, particularly in Vancouver and Toronto. Only 60% of the nation's population has English as its mother tongue; another 22% – mostly those living in the bilingual province of Quebec – speak French at home.

This cultural mix has resulted in some enticing tourist attractions, such as Toronto's Caribana, the largest Caribbean festival in North America. Created in 1967 as a community heritage project, almost one million people converge on Toronto for the parade and festivities each year from Trinidad, Jamaica, Haiti, Puerto Rico, Barbados and many other places.
The annual Toronto International Film Festival is second in importance to Cannes, attracting 250,000 Canadian and international delegates. In 2003, it delivered more than $33 million in tourism.

Montreal, often considered the Paris of North America, is the second largest French-speaking city in the world after Paris.
The city hosts more than 40 festivals and major international events, including the longest St. Patrick's Day parade. The Festival International de Jazz de Montreal, which

celebrates its 25th anniversary this year, has become a world-class event, bringing in almost two million visitors in 2003.

Montreal is also recognized as a major fashion centre and is one of only two North American cities – the other being New York – listed in the prestigious Cities of Fashion guide. Further north, Quebec City hosts the world's biggest annual winter celebration, the 'Carnival de Quebec', which brings people

from all over the world to experience snow baths, night parades, slide runs, ice fishing, concerts, snow sculptures, horse-drawn sleigh rides, husky- powered dogsled rides, and skating.

Out west, Alberta offers the Calgary Stampede, the self-proclaimed greatest outdoor show on earth. The rodeo attracts a global audience, injecting more than $125 million into Calgary's economy every year.

The cultural range of Canada not only creates a massive choice, it enables domestic travellers to experience a whole new world without crossing a border or worrying about currency fluctuations.

Good news ahead

Canada's tourism industry was hit by international events in 2003, such as the Iraq War and the aftermath of 9/11, as well as two domestic incidents – the outbreak of SARS, and an electrical blackout that hit much of the eastern seaboard, including Toronto. About 2.9 million occupied room nights were lost compared to the previous year, with Ontario bearing 62% of the loss.[1]

It took more than five months for recovery to get underway, but by 2004, the tourism industry had rebounded successfully. Domestic tourism revenue, air travel spending and accommodation rates were all up. This welcome growth created 538,000 jobs, breaking the previous annual record of 279,000.[2]

Even better – Canada is still seen as a 'safe' destination. Government funding, particular in Ontario, is helping to lure tourists from countries other than the US, while the weak dollar will encourage more visitors.

The pace will quicken next February, when Toronto will debut the $30-million-dollar British musical theatre production of 'The Lord of the Rings', the most expensive and most ambitious stage musical ever conceived. And in 2010, Vancouver will host the winter Olympics, as well as the Paralympics Winter Games.

Millions will visit these attractions and discover that Canada – rather than the world – is their oyster.

1 Canada Tourism Commission.
2 Canada Tourism Commission.

Ryan Brain
Senior Manager, Toronto
Tel: +1 416 601 6500
Email: rbrain@deloitte.ca

When expansion's on the menu

The five ages of eating out

Eating out covers the whole spectrum of experiences – from the romantic, celebratory, social occasion, to the grab and go of the fast food outlet. Somewhere in between is the ritual of business professionals 'doing lunch' and the eat-while-you-wait fix at airports and railway stations.

Whether it's a haute cuisine extravaganza or a simple pizza at the local trattoria, one thing's for sure – people are doing a lot more of it than ever before.

Gone are the days when a meal out was a rare treat to mark an important occasion. In some of the more affluent countries today, more meals are consumed outside of the home than at the dining room table.

Consumers' eat away from their home base for pleasure, convenience, because of time pressures, or – increasingly – just grazing or snacking, and food service companies are having to adapt to these changing social patterns while meeting the increasing demand for quality.

No time to cook

These trends can be seen clearly in the US and across Europe, especially as dual-income families have more disposable cash and less time to spend on the preparation of food.

However, in the UK and US, although the food service industry remains a major employer and contributor to the economy, the industry is becoming saturated and the domestic markets are beginning to slow. As can be seen in the table below, the eating out market in the US is forecast to be lower, relative to other markets, while the UK – although more buoyant – is suffering from intense competition.

Many operators, keen to exploit the increasing trend for eating out – but recognising the limits within their traditional geographic boundaries – are therefore looking overseas for new growth opportunities. But this appetite for expansion doesn't come without risk. There are critical considerations that have to come into the equation, including:

- Assessing the broad economic factors, the political and social climate and the regulatory and tax regime.
- Identifying markets where it is safe to do business and the eating out industry is in full growth.
- Defining the most appropriate business model. The options for a restaurant company, franchise, joint venture or company-owned model will depend on the economic climate and the capacity for investment within each country.
- Deciding on the level of infrastructure investment, both at a domestic level within head office to manage international operations and locally, to provide support and logistics.
- Checking the suitability and flexibility of the brand when it's extended internationally. Consumer awareness and responsiveness will determine whether the brand will have to be adapted to suit international consumers.

The value of eating out in foodservice channels (profit sector), by country (US$ billions), 2004-2009

	US$ billions		CAGR
	2004	**2009**	**2004-2009**
France	20.1	22.1	1.9%
Germany	17.5	19.3	2.0%
Italy	26.0	30.2	3.1%
Netherlands	3.8	4.2	2.2%
Spain	7.7	9.4	4.2%
Sweden	3.8	4.7	4.7%
UK	31.3	36.4	3.1%
Other Europe	22.0	25.3	2.8%
Europe total	132.1	151.6	2.8%
US	199.5	218.8	1.9%
Overall	**331.6**	**370.5**	**2.2%**

NB: Includes Cafes, Pubs and Bars, Nightclubs, Restaurants, Takeaways (main activity), Hotels & Lodging, Street & Mobile Vendors, Retail, Leisure and On-board (e.g. Air, Rail, Sea) Values are based on retail selling prices.

Source: Datamonitor's Global Foodservice markets Database 2004-2009.

Using proven SWOT or risk analysis methodologies will match market suitability to styles of operation – whether that's the good old gastropub, a chain of bistros or all-you-can-eat specials.

The five ages of eating out

Deloitte's extensive experience in the industry reveals a set of common characteristics that define the five ages of development in a country's eating out market. This knowledge can help identify countries with the most potential; for instance, those that are either experiencing or about to enter rapid growth, but where other operators have yet to establish a presence. Understanding where a country sits within these five ages should be set against a backdrop of the wider issues of stability and security within that domain.

B.C. – Before casual dining

- Economic and political climate is stable.
- Limited eating out opportunities tending to be dominated by local cuisine.
- Eating out occasions are rare.
- Possible presence of fast food multi-nationals.

Medieval – The 'Steak House' era

- Signs of economic growth and general affluence.
- Eating out limited to special 'celebratory' occasions.
- Eating out market dominated by a few large providers.
- Consumer demonstrates conservative tastes – 'stick to what you know' – eg popularity of Beefeater/Berni steak houses in the UK in the 1970s.

Renaissance – A more sophisticated palate

- General economic conditions remain positive.
- Consumers begin to eat out more and demand variety of cuisines.
- Foodservice companies establish restaurant brands to meet this demand.

The five ages of eating out

B.C.
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Medieval
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Revolution
Lets try everything

New Age
Choice for all

Revolution – Let's try everything

- General economic growth increases and consumers are more affluent.
- Eating out occasions increase (particularly as economic growth drives growth in disposable income).
- Eating out market fragments as many new entrepreneurial brands and operations established (from a variety of cuisines).
- Quality and consistency of service and product can suffer during high growth.

New Age – choice for all

- Spend per head goes down as people eat out more, and for more reasons.
- Consumers want to 'customise' their meals and look for wider choices.
- Consumers are reluctant to forego eating out in economic downturn.
- Foodservice companies begin to consolidate brands to enjoy economies of scale as market matures and growth slows.
- International markets may be explored for source of future growth.

Critical crossroads

Food service companies faced with saturated or highly-competitive domestic markets will find overseas expansion enticing, but thorough analysis is critical before making any investment decisions. Deloitte's deep understanding of the issues mentioned in this article can provide some valuable pointers.

Jon Lake
Assistant Director, London
Tel: +44 20 7007 2765
Email: jolake@deloitte.co.uk

Reaching your target

Earlier this year, a survey was conducted through the Deloitte internal website across eight countries, including UK, Germany, Netherlands, Italy, Spain, Australia, China and Hong Kong. Questions were aimed at current gym members, past members and non-members to gain a quantitative understanding of drivers of gym use, gym selection and factors influencing the gym experience.

There were over 3,500 responses to this survey and this article contains a selection of the results, which – combined with Deloitte's deep experience of the health and fitness industry – will assist club operators plan for a healthier future.

Overall, the three key messages for club owners and operators are:

- Ensure price discounting and promotion activity are closely linked with well executed induction/retention programmes.
- Invest in improving the quality of local club management and that of supporting systems and processes to better manage customer relationships.
- Consider the aspects of gym membership that appeal most to customers when looking into consolidation opportunities.

An expensive welcome

As competition to fulfil consumer demand for health and fitness intensifies, promotions and price discounts are commonplace across the industry. However, efforts to gain these incremental members can be much greater than those needed to keep existing members happy. While location and convenience are clearly the dominant driver for gym selection, those who join with price and/or promotion as key criteria, tend to show a higher propensity to churn than 'regular' members (Fig. 1). Members attracted by the headline price are less likely to incorporate a fitness habit into their lifestyle or to make full use of facilities.

Activities such as inductions, 'fitness check-ups' and organised activities/classes can help retention. Offering personal training can also be useful, but will prove a more difficult sell to members focused on cost.

Why won't they join?

It's important to understand why members choose or ignore a particular gym, and the Deloitte survey shows some interesting differences between men and women. For instance, men tend to substitute gym membership with other sports or fitness activities, and therefore see no reason to join, while women are more aware of the impact gym membership will have on their budgets, (Fig. 2), and are more likely to regularly question the value they get from their membership. Women also prefer a gym that's closer to home or work.

These findings suggest that members strongly influenced by discounted prices or promotions are not only harder to retain, but they more likely to be women.

Quality management counts

After the more tangible factors, such as location and facilities, the quality of local club management has a major impact on a club's strength as it will:

- Have insight into demographic profiles and behaviour of the local club members.
- Control the execution of acquisition and retention activities.
- Create an environment that meets local needs.

Local management's role becomes even more important when looking at the factors that influence women's and men's gym experiences.

Women are more likely to make decisions based on discounted prices and promotions and appear to be more influenced by intangible factors – such as the atmosphere in the club and the friendliness of club

Figure 1. Key purchasing criteria

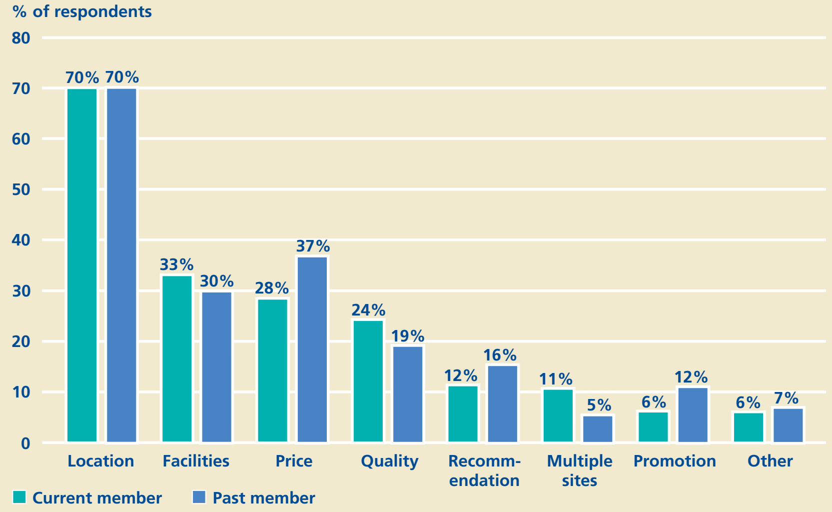
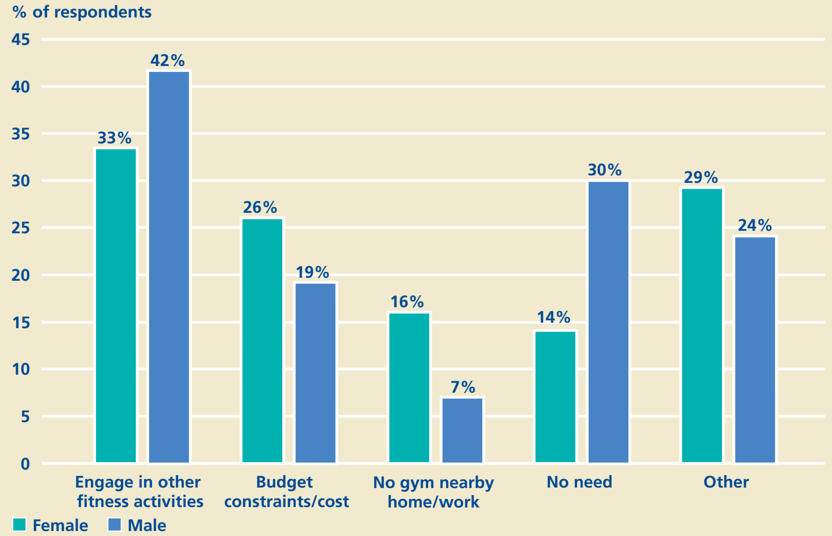


Figure 2. Reasons for not joining



staff (Fig. 3) – whereas men are more concerned with the quality, condition and availability of the gym equipment.

Improving club management should therefore be an essential part of a strategy to reduce attrition.

There still appears to be huge differences in the quality of management, even within a particular chain, as well as an apparent disconnect between head office and club staff. This can be changed through:

- Standardisation of all processes related to a member's lifecycle.
- Introduction of more sophisticated systems to enable more effective interaction with members.

Industry consolidation

In the more penetrated markets, such as the UK, there is much talk about consolidation – particularly given the strong presence of private equity owners in the sector. Most merger analysis focuses on investor's interests, overheads and other cost synergies, which alone are not likely to make a merger look attractive. Overlapping geographies are likely to be seen in a negative light from this view point. However, when viewed from a customer perspective, merger analysis would prize overlapping geographies in urban areas combined with 'higher spec' facilities in suburban areas, to better meet customer needs. Operators who have achieved scale in urban areas have observed positive changes in consumer behaviour when multiple site use is encouraged.

The 'network' effect

A 'network model' exists when an operator has multiple sites – ideally reasonably close to each other so that members can use more than one club, including facilities in both town centres and the suburbs. Most members select a club close to home or work, choosing a work-based club for either convenience or as a status symbol, whereas home-based venues are typically selected because of their facilities, services and social aspects.

A networked model has several advantages for operators through:

- Increased attractiveness to new members.
- Potential to reduce churn due to moving and life-style changes.
- Potential to minimise the need to install costly facilities in all sites, such as pools and crèches.

Figure 3. Factors influencing gym experience

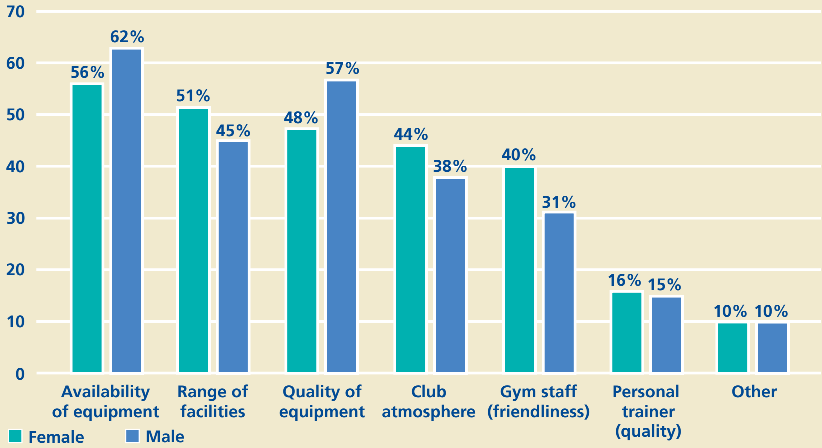
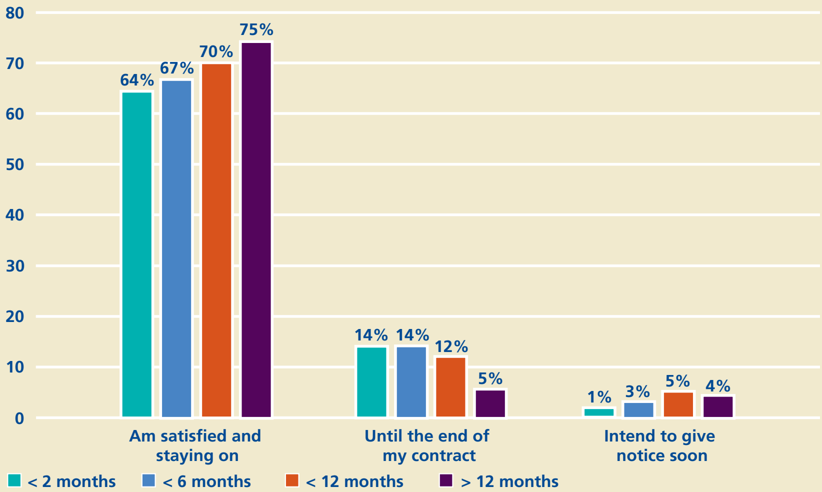


Figure 4. Intention to stay with gym



Members looking for a specific facility will usually travel further – especially if they only use the facility on an irregular basis. Churn rates are also lower when members have access to 'high value' facilities – even though most never will use them.

The logical consequence is that suburban sites should take on a more social feel with a wider range of facilities, while the urban sites could be more utilitarian to minimise costs and enhance convenience, when networked together. An overlapping urban footprint combined with a 'country club' suburban operation makes more sense to members than several locations offering similar facilities. This networked approach may help to unlock the consolidation logjam.

The longer they stay, the longer they stay

Acquisition and retention strategies in health clubs have evolved, moving from mass marketing, followed by little or no direct contact until – maybe – an exit interview. Now, operators are launching more complex induction programmes, which cover the first three months of membership.

Member satisfaction surveys are core to a club's retention activities, with successful clubs listening to concerns and then responding to them quickly. It's important to note, though, that members' satisfaction changes over time.

Our survey implies that the longer a member stays with their gym, the more likely he or she is to be happy and intend to stay on (Fig. 4). This may seem obvious, but the gradient of increasing satisfaction seems generally constant over the first 12 months of membership, and continues at a broadly similar rate past then, suggesting that satisfaction is built up gradually over time, rather than from offers or short term benefits at the start or during the early stages of membership.

Interestingly, the proportion of members planning to leave at the end of their contract period – 14% – stay relatively constant over the first 12 months of membership, implying that a decision is made either at the start or quite early on. Some people will have joined in preparation for a particular event, such as a marathon, but knowing when and why these decisions are made – and responding – could cut attrition rates.

Keep them coming back

More than 40% of members left their gyms within 12 months of joining (Fig. 5), and there are no distinct points during the first year that members decide to quit. While some operators have induction programs lasting up to 3 months, regular retention activities over a longer period are more likely to embed the relationship throughout the first year – and beyond.

Former members welcome

Clubs acquire new members from three main sources:

1) Individuals who have never belonged to a gym.

2) Members of other clubs.

3) Ex-members of same club, or chain.

With many health clubs losing around half of their membership base each year, 'ex-members' maybe worth pursuing, so it's important to know why they left in the first place.

Changing to a network model, for example, could help retain those who are moving house or changing jobs. The survey shows the major reason for leaving as moving house at 26% (Fig 6), while some exit surveys show this to be as high as 40% – probably because it's an easy option to give when leaving. Worryingly, around 20% left because they either never went or because they were dissatisfied with their gym. Here, local club management should be tracking the frequency of visits to identify those who may be close to leaving.

Gaining a deeper understanding of lifestyle changes given by members could help reclaim around 15% of those who left, potentially through different membership options. Interestingly a very low percentage of members left having achieved their objectives (1%).

Moving house can quickly make some ex-members virtually impossible to contact, unless they have supplied personal email and mobile phone details and are happy to be contacted in this way. As this group constitutes only about a quarter of those who leave, accessing the remaining members could benefit growth, but it's important to realise that ex-members' data quickly loses value. Contact details become obsolete, and the initial enthusiasm for joining a gym evaporates.

The survey also shows that an ex-member's intention to rejoin decreases the longer they are away from their gym (Fig. 7).

Digging in the database of ex-members will reveal:

- Those who have moved (and therefore changed addresses).
- The 'de-gymed' population that could be lured back.

Figure 5. Length of time with gym before leaving

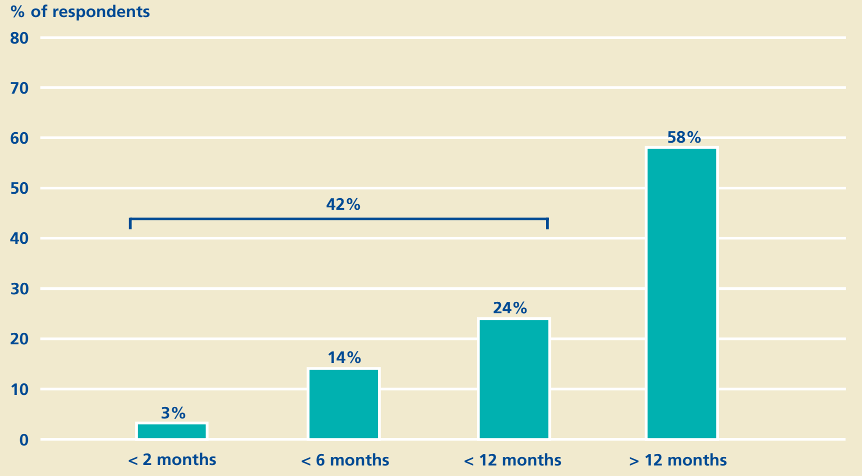


Figure 6. Primary reason for leaving

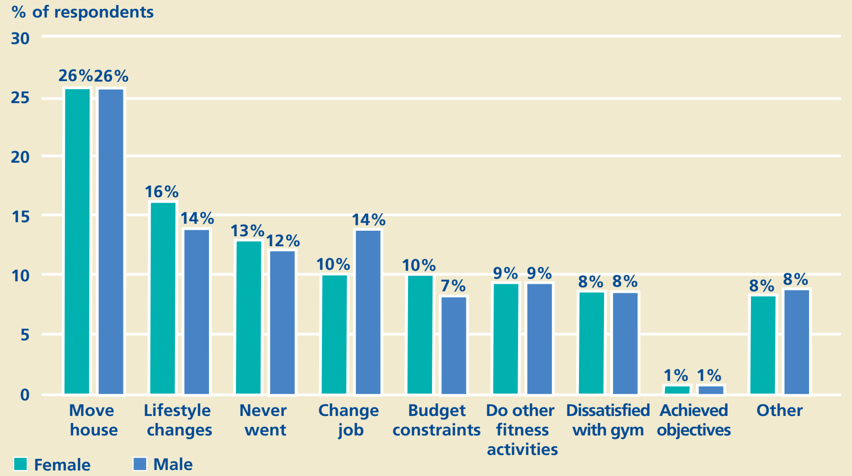
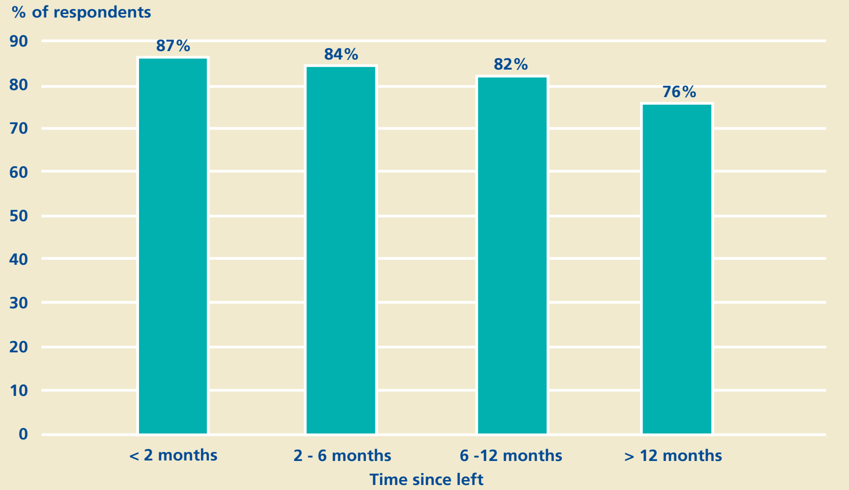


Figure 7. Intention to rejoin



- Those who are now with a competitor or have firmly decided to stop using fitness facilities.

Based on a churn rate of 50%, and converting the 26% movers data to an annual average (which equates to a person moving once every 7.7 years), the portion of the ex-member database that could be contacted and potentially re-signed falls to about 50% within one year (Fig 8.).

On the positive side, 50% of a large database (or even 38% when the analysis is carried out using 40% movers) filled with good prospects should still be immensely valuable. However, operators have to decide how much of their marketing budget should be spent on contacting these potential members. For example, ex-members who have gone to competitors could be lured back at the end of their contract. One thing is for certain – operators can't waste time on this.

Travel choices

It is generally accepted that the closest club will suffice for most people, unless it's viewed as being in some way defective by potential members. Travel time is typically 10 minutes or less, but adding transport type and country to the analysis reveals a few other dynamics (Fig 9.):

- Different transportation patterns and cultural differences.
- Varying degrees of market development.
- Stark differences between members living and/or working in major urban centres and the rest of the sample.

Tolerance of long travel times in major urban areas – such as London and Hong Kong – is higher than in more suburban areas. In 'second-tier' cities – such as Sydney and Amsterdam – the average travel time is noticeably shorter. Not unsurprisingly, bicycles feature strongly in Amsterdam (not shown). Outside major cities, people prefer to drive and ample parking becomes a major differentiator. The high travel times shown in China are probably because of under-provision rather than a generally higher tolerance of travel or a willingness to walk past a suitable club.

Figure 8. A changing ex-membership base

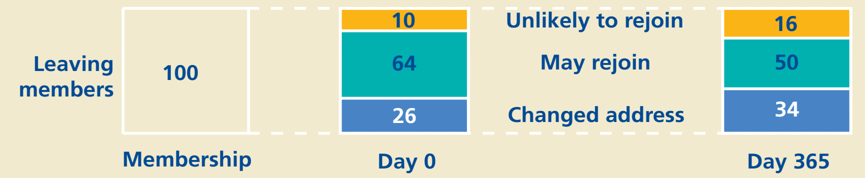
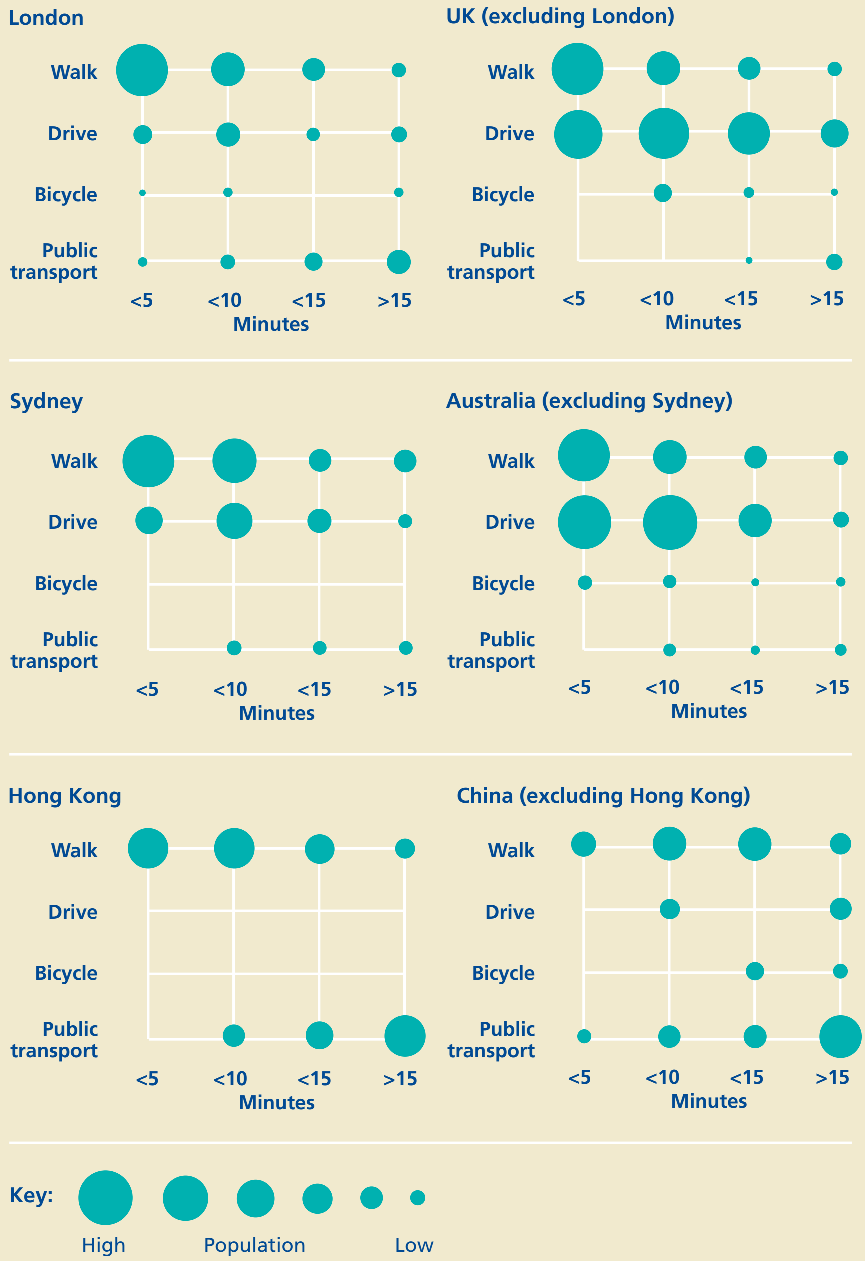


Figure 9. Travel choices – representing how individuals travel to the gym



Adrian Balcombe
Partner, UK
Tel: +44 20 7007 2944
Email: abalcombe@deloitte.co.uk

Alan MacCharles
Assistant Director, UK
Tel: +44 20 7303 0860
Email: amaccharles@deloitte.co.uk

Tony Drabble
Manager, UK
Tel: +44 20 7303 8761
Email: tdrabble@deloitte.co.uk

Getting personal

Who are your customers?

What do they need today? What might they need tomorrow? How will you keep them satisfied? Is satisfaction enough? What can you do to ensure they keep coming back to you time after time?

The ability to answer these questions is more vital than ever in today's competitive landscape. Estimates suggest that it is up to ten times more expensive to acquire a new customer than to retain an existing one. Building customer loyalty is not only the basis for repeat business, but also a means of broadening offerings, and cross-selling services. For a mature business customer retention is the key to increased profits.

Far-sighted tourism & leisure operators go beyond instant gratification to embrace the lifetime value of their customers. Evidence suggests that such companies are better prepared to withstand economic downturn, and the impact of shock events such as 9/11. Saga, the over-50's travel specialist with a famously loyal customer following, managed to buck industry trends by posting a significant profit increase during the turbulent year of the SARS crisis and Iraq war.

In this article we discuss some of the reasons why it is now more crucial than ever, and also more difficult than ever, to identify and build strong relationships with the customer. We also consider some of the means by which companies in our industry might do this.

Tourism and leisure, fuelled by the growth of broadband, is one of the fastest growing e-commerce sectors. Attention has focused on the battle between operators and intermediaries for supremacy in cyberspace. Meanwhile, it is clear that technology is shifting the balance of power in the direction of the customer.

Armed with a wealth of information, travel and leisure shoppers are able to compare offerings and prices as never before, and to make purchases from the comfort of an armchair. New "meta-search" engines like Kayak and Sidestep make this even easier by trawling the Internet in search of the best deals.

Web-savvy customers are also making increasing use of the internet to share feedback on tour operators, hotels and visitor attractions.

"In 2005 there will be 21 million fewer nuclear families (married couples with kids) in western Europe than 1995". (Datamonitor)

"Around 95% of advertising is aimed at under-35s, but the majority of wealth and assets is held by people aged between 50 and 65. The UK's over-50s spend over £240bn a year, which amounts to over 40% of consumer spending".

(Help the Aged)

"There will be over one billion internet users worldwide by the end of 2005".

(eT forecasts)

"For the first time ever more leisure travel dollars in the US will be spent online than offline in 2005. In the US, some $66 billion, or 58%, of leisure travel will be purchased online in 2005".

(PhoCusWright).

Consumer review websites are fast becoming a first port of call for would-be shoppers.

The impact of new technology, by vastly increasing customer knowledge and choice, is likely to make consumers more demanding, more critical, and more fickle than ever before. And therefore harder to retain.

For the tourism and leisure sector, these changes will accelerate many of the long-term trends that are already re-shaping the industry, and subtly altering the identity of its customers.

Decline of the mass market

Individual purchasing decisions form a pattern of buying behaviour over time. These decisions emerge from a complex melting pot of social, cultural and economic influences.

For many years the travel & leisure industry designed products for a relatively stable customer base, in which familiar, identikit offerings could be targeted at broad social categories. This was typified by the standard 7 or 14 day beach package holiday, aimed squarely at the average nuclear family with two parents and two point four kids.

Hotels, resorts, restaurants and pubs had clear-cut demographic profiles. Leisure activities were mapped to static social groups. Football was predominantly male and working class; museums and art galleries middle class, and so on.

Marketing techniques made use of relatively crude profiling, based on broad age bands and social categories such as ABC1s. It was easier to know who your customer was in the old days.

To claim that all of this has now changed would be a gross exaggeration. The "mass market" customer still exists and will continue to be the lifeblood of many companies.

As a leading tour operator recently commented: "If you listened to some reports, you'd think that everyone wants to live in a tent in Outer Mongolia eating dried yak meat for a month…but our customers are looking for something more familiar!"

Nevertheless, figures suggest that the mass market is shrinking year after year, while real growth lies elsewhere.

Many commentators agree that contemporary western society is in a process of fragmentation, in which long-established identities are being broken down and re-fashioned.

Mega Trends

A wave of new "mega-trends" [1] is beginning to converge, creating new kinds of customers. Unfortunately, the identities of these customers are likely to be far more complex and changeable than ever before. Some of the key mega-trends and their implications for operators are as follows:

Age confusion. Children grow up faster, but adults behave younger. Over-50s prefer safaris to sewing. 10 year olds want hotel rooms with Wi-Fi and i-Pods. "Young fogies" go on caravan holidays, visit bingo halls, and play Scrabble in bars. Thirty-something "adultescents" read Harry Potter and seek out the latest white-knuckle rides.

The "grey" market is an untapped goldmine, but fraught with difficulty. Thomson Holidays used the "Young at Heart" brand for 20 years, but abandoned it when feedback showed the age group felt patronised by this description.

Gender confusion. Traditional roles are blurred, as women gain economic power and have fewer children, while men take an active role in parenting and become more fashion-oriented. Bars and sports teams may target women, while spas may target men.

Lifestages. Declining birth rates, increased longevity and change in gender roles mean that conventional lifestages are delayed or skipped altogether. Travel and hospitality operators have to cater for more singles, older people with young children, as well as family structures where divorce, remarriage and step-children may produce complex age combinations.

Luxury and budget. Customers can't always be slotted neatly into spending categories according to income. Evidence shows a growing trend towards economising in some areas, whilst splurging in others. Travellers may fly no-frills, but upgrade to a luxurious hotel.

Comfort and security. Enthusiasm for interior decoration, cookery and garden design, and the popularity of pampering activities, form a trend towards "cocooning". Alongside this goes an increased need for security in the uncertain post 9/11 world. Hotel operators introduce more home comforts and design principles in their rooms, and deploy biometric technology to increase guest security.

Connectivity. The decline of the nuclear family creates a desire for new forms of social belonging, which can take highly diverse forms ranging from the rising popularity of book groups, to the huge success of websites like www.friendsreunited.com. Some resorts are turning to the village concept popular with retail malls and mixed-use developments. The 21-acre The Ritz Carlton, Lake Las Vegas has created an urban-style resort with a retail village, featuring a casino, office space, luxury condominiums, shopping, restaurants, and pedestrian promenades.

Getting Personal

Once people derived their identities from the cohesive groups to which they belonged: ties of family, company, community, class, and gender. Now they are more likely to see themselves as individuals. Shopping and leisure choices reflect this and are creating an ever increasing demand for personalised services. This trend lies behind the emergence of boutique hotels like InterContinental Hotels Group's Indigo and Choice's Cambria.

The challenge for big companies is to provide the level of personalisation customers want on a mass scale. Many customers react against the global uniformity of a McDonalds and seek something more "authentic". Some hotel operators may choose to create an experience of personal choice by offering a variety of brands in the same complex.

Meanwhile, the Internet and individualisation march hand in hand. The rise of Dynamic Packaging in the travel industry shows how technology can transform a mass market product into a customised one that appeals to the independent mind-set of today's shopper.

Work & play

The 1980's slogan "work hard, play hard" has come to fruition. Working hours are longer than ever. Demand for leisure services continues to grow fast as customers seek to balance work pressures with recreation. However traditional boundaries between the spheres of work and leisure are becoming blurred. Technology is eroding the difference between workplace and home space, as mobile phones and BlackBerries enable people to work anywhere, anytime.

Marriott's hotel rooms illustrate how hotel operators are catering for a new generation of travellers whose trips are equal parts work and play, and who yearn for the comforts of home even when they're thousands of miles away. According to a Marriott spokesman, "People sit on their beds, laptop open, with a glass of wine, TV on in the background. If you watch them, it looks like work and relaxation together."[2]

The Experience Economy

Customers crave a new intensity of experience and want to have stories to tell their friends, whether by jetting off on weekend city breaks, visiting exotic destinations or sampling the latest exercise craze for Pilates or pole-dancing. Companies like Lastminute.com are capitalising on this appetite for new horizons and spontaneity.

The creation of memorable experiences may hold the magic key to building relationships with customers. Some analysts have gone as far as to say we are entering a new economic phase: the "experience economy." According to this view, just as developed societies have moved from the manufacturing to the service phase, the next stage will be the transformation of services into high-value experiences.

Economists like Gilmore and Pine in the US argue that stimulus-hungry consumers are growing bored with mass-produced services that have turned into price-driven commodities. They argue that the future economy will be based on providing customers with a unique experience for which providers can charge a higher price.[3]

Companies become "experience stagers." Disney, one of the most successful operators in our industry, has been trailblazing this approach for many years. But not all companies have to open theme parks. The Starbucks phenomenon typifies this process. More than just a cup of coffee, Starbucks' success is based on the successful staging (at premium price) of an experience which combines comfort, a hip ambience, tasteful surroundings and technology.

It is hard to accept that price will no longer be a key factor in selling future services (the airline and fast-food markets suggest otherwise). However the idea of the "experience economy" is one that the industry should be able to successfully leverage in building strong customer ties. Tourism & leisure companies trade in the stuff of dreams, pleasure and entertainment. It ought to be far easier for them to create memorable experiences, than for, say, financial service providers.

Technology & imagination

When it comes to tracking the complex needs of customers, and cementing strong relationships, there is no single approach that is going to meet all requirements. A creative combination of "hard" and "soft" techniques, of technology and imagination, is likely to yield greatest success.

The online travel boom is leading to a huge growth in the amount of customer

"Per capita consumption of alcoholic drinks among UK women increased 27% between 1998 and 2003".

(Datamonitor)

"In 1971, more than half of us (53%) lived in households of four people or more. By 2003, that figure had fallen to just over one third (37%). A quarter of all children now live in one-parent households".

(UK Office for National Statistics)

"60% of young men aged between 20 and 24 are now living with their parents. In 1991, only 50% of men in the same age group were living at home".

(UK Government)

"UK package holidays, as a proportion of total overseas holidays sold, fell from 55% in 2004".

(Mintel)

transaction data available for storage and analysis. Indeed, the battle to control this knowledge is a key part of the power struggle between supplier and intermediary. The anticipated rise in RFID usage will lead to the further rise of this information mountain.

This growth is leading to a renewed interest in Customer Relationship Management (CRM) software. In the wake of the post 9/11 downturn many companies scaled down strategic investment in CRM systems. However CRM sales are now on the rise again, as software begins to move towards the next stage of sophistication, the generation of deep insights into customer behaviour and predictive analysis.

Big ticket operators endeavour to re-create the intimacy of the village pub on a mass scale. CRM offers a way of capturing knowledge of customer needs, and offering large-scale personalised service based on this knowledge. Behaviour patterns can be tracked over time, and used to cross-sell or up-sell as appropriate. CRM also allows companies to identify their most lucrative, "high value" customers, and to prioritise them with loyalty programs and red carpet treatment.

A pioneer approach has been Harrahs' Winners Information Network (WINet). The database provides an integrated, nationwide system that allows real-time communication between all Harrahs' casinos. Sales reps are armed with critical information about every customer's tier (platinum, gold or diamond), as well as their eating and spending preferences. The same customised service can be offered regardless of whether the customer is visiting New Jersey or Las Vegas. CRM has enabled Harrah's to develop segmentation and marketing programmes around the expected lifetime value of each customer. When customers walk in, Harrah's staff greet them by name and reward them for returning. The most profitable visitors are tempted back with lavish promotions.

Emotional connections

Innovative companies incorporate lifestyle preferences in their online customer interactions. US hotel operator Joie de Vivre Hospitality uses its "Hotel Matchmaker™" tool, which guides customers through questions about their personal tastes, interests and personalities before matching them up with an appropriate hotel, suggested itinerary, and local activities. Joie de Vivre aims to make the customer's web experience as uniquely memorable as the actual stay.

Ultimately the most successful companies will build loyalty through the creation of highly differentiated experiences. An attention to detail is important, as in the identification of "high impact moments". Starwood developed its iconic "Heavenly Bed" to satisfy one such moment for weary business travellers — the feeling when they first collapse onto the duvet. Such moments can engender emotional connections which are highly effective in winning repeat business, and word-of-mouth recommendations.

In developing these experiences companies need effective customer feedback loops. But the new buzzword on the block is "co-creation." This goes way beyond traditional feedback to engage customers in new creative ways, from participating in advertising, to having input into the actual design of products and experiences. The interaction between company and customer becomes not just the place where value is extracted, but also where it is created.[4]

Companies and customers may even form web-based virtual communities around a particular destination or activity. For example, tour operators may seek to partner with increasingly popular online travel blogs like MyTripJournal.com.

This may be blue-sky thinking, and more of a future possibility than a present reality. What is beyond doubt is that today's operators need to develop business models that are much more customer-centric than in the past.

This might mean maximising customer lifetime value by developing a suite of niche brands, through which the same guests can progress, as Starwood is doing with its W Hotels for a hip 20-plus age group, Westin for travellers in their 30s and 40s, and St. Regis for affluent older travellers.

It might also mean shifting the focus of strategy from winning market share to increasing share of a customer's wallet, turning low-value into high value customers and rewarding them as operators like Harrah's have done.

It might even mean creating the executive role of Chief Customer Officer as a focus through which compartmentalised business lines can be channelled, as Delta Airlines, and many consumer goods firms have done.

It will certainly mean importing new thinking from senior management in the Fast Moving Consumer Goods (FMCG) sector as InterContinental and Starwood have done, as the focus shifts from managing assets to managing customer-led brands.

The old boundaries between operators, distributors and sellers are dissolving, and it has been said that now "everyone is a retailer."[5] This means that everyone is now customer-facing. Those who use this as an opportunity to build long-term loyalty will enjoy the rewards. Those who don't may find customers voting with their feet. Or more likely with their mouse-clicks.

1 Datamonitor, Global Consumer Trends, July 2004.

2 Michael Jannini, executive vice-president lodging brand management, Marriott (New York Times 11th March).

3 Gilmore and Pine, The Experience Economy, 1999 etc.

4 Prahalad and Ramaswamy, The Future of Competition, 2004.

5 "Everyone is a retailer", Deloitte Research Consumer Brief, May 2004.

John Worthington
Research Analyst
Tel: +44 20 7303 0455
Email: jworthington@deloitte.co.uk

Online gaming – in the spotlight

Gaming – both real and virtual – is moving into the mainstream, evolving from a restricted and questionable activity to a leisure pursuit enjoyed by millions worldwide.

The signs of change are everywhere – Singapore has lifted a 40-year ban on casino gaming, a building bonanza in China could see the lights of Macau outshine those of Las Vegas within five years, and the UK's deregulation is being closely watched by its European neighbours.

In the digital world, broadband penetration is driving the take up of online gaming, with bullish predictions for growth setting the market at $21 billion by the end of the decade, confirming that online gaming – much like online music – is here to stay.

The year ahead will be a critical one for the virtual betting and gaming industry. It will either survive as a standalone industry or be consumed into the product mix of established online content providers or consumer businesses. This article looks at the stakes in play.

Out of the shadows

Global gambling markets are adapting to the new spirit of liberalism which is bringing betting and gaming out of the shadows.

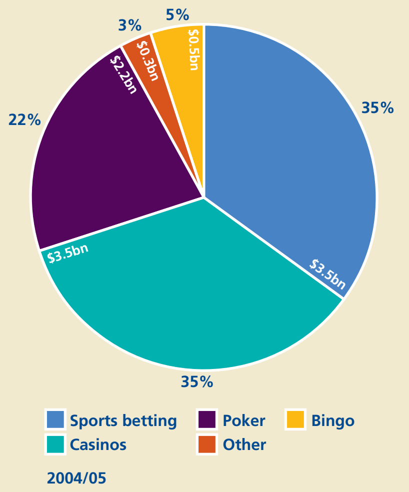
In Macau, new casinos are being constructed at an impressive pace by operators such as Las Vegas Sands, Wynn Resorts and MGM, and is set to rival Las Vegas. Singapore has plans for two super casinos and, in the UK, the recent Gambling Act, although watered-down, is driving new growth, and much of Europe, especially newcomers to the EU, are watching developments closely.

Worldwide, governments are juggling with the same issues. The benefits of opening up their gambling markets, with the added appeal of extra income from tax, may be justified by more liberal attitudes, but this has to be balanced against social responsibility.

While governments consider their options, online operators have been pushing ahead and capturing market share, operating mostly from offshore locations such as Gibraltar, Malta, Antigua and Alderney.

Online gaming, spawned from the dotcom boom, is now a diversified product mix, offering traditional sport books through

Product Revenue Split



to multi-player poker. Clearly, this is an industry gearing itself up for a dramatic step change.

Online gaming will be transformed through two critical, and fundamentally linked, fronts – credibility and consolidation. But before it can move into the mainstream it needs to deal with several pressing issues:

- The general perception of the industry and the risks it takes.
- Its legal standing.
- The potential for growth.
- The consequential social impact.

Perception v's reality

There is a perception that online betting and gaming businesses are themselves taking a gamble. However, while there is a strong element of risk management for any operator, this is largely revenue protective rather than revenue generative. The real gamblers are the players.

Looking at two of the online market's fastest growing areas – betting exchanges and online poker – the 'gambling' risk is removed from the operators hands, insufficient liquidity, comparable to insufficient critical mass or market share in more traditional businesses, is the overriding operational risk.

Today, online betting and gaming businesses need to be just as focused on customer relationship management, marketing and pricing as they are on managing risks.

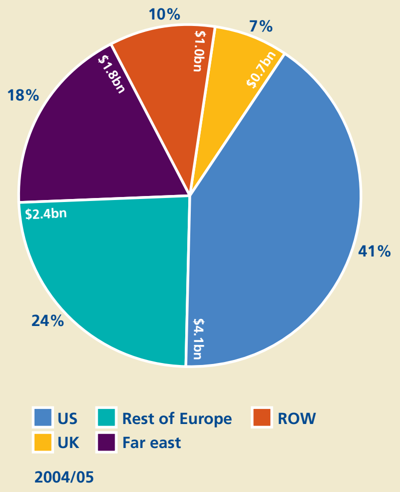
The legal questions

Undoubtedly, one of the biggest risks to the emerging web-based gaming businesses is regulatory and legal uncertainty. This is not something the City, or most investors, are comfortable with, as demonstrated when North Dakota's decision to reject an online poker licensing bill brought down online gaming stock by 5-10%.

There are three core strands to the current legal landscape – important questions over legality in the US; challenges to the provision of online gaming within Europe; and new regulation in the UK. All of these have an impact on the maturity of online gaming, which depends on investors and consumers having faith in the industry's future.

Beyond this lies China, which offers massive potential but has significant political and practical obstacles to overcome.

Geographical Revenue Split



The legal backdrop in the US is formed by the 1961 Federal Interstate Wire Act, which is being used to challenge the legality of US citizens gambling online.

While opinions are divided as to whether a case against an online gaming operator accepting US bets would succeed, the government continues to impose indirect limitations on the industry by restricting advertising and payment mechanisms, including credit cards. Recently, Esquire magazine was served an Informational Subpoena for publishing Online Gaming adverts, and the US senate is set to discuss the possibility of banning banks and credit cards from accepting online gaming transactions.

This action reflects the US government's strong response to the World Trade Organisation's judgement on the case between Antigua and the US, in which Antigua claimed the US was discriminating against foreign providers of gaming.

In a preliminary ruling last year, the WTO backed Antigua. However, when the US appealed, it was agreed that the government does have the right to restrict remote gambling to protect public morals and public order. Such restrictions must, however, be applied consistently to both domestic and foreign operators.
A parallel can be drawn between this and attempts by European states to restrict online gaming, where the European Court of Justice has ruled that restrictions must be applied to protect citizens, but not national operators. Similarly, any restrictions should be consistent.

The picture is quite different in the UK. The Gambling Act, passed in April this year, legalises online casinos and seeks to create a sound regulatory environment for the industry. Whether operators will now choose to re-locate to the UK will probably be limited by the higher tax rates, compared to offshore locations, but the foundation has been laid for a benchmark that will help the industry gain credibility. While links with the UK's regulatory environment inevitably will carry costs, these can be balanced against the benefits of an enhanced reputation.

As the UK market shapes up, other European countries are expected to introduce similar legislation, further strengthening the industry's image across Europe.

So, while the US climate remains uncertain and China still has a big question mark over it, Europe is opening up for business, and online gaming is gathering speed. Acceptance as a legitimate business activity, rather than an outright ban, will enable it to be more effectively controlled, as history shows, prohibition failed before and could do so again.

Potential for growth

Despite the US situation, there is significant potential for global growth through increased broadband penetration, continual liberalisation and wider geographic reach. Forecasts for the industry are bullish, with some analysts expecting the revenues of $3bn in 2000 to have increased to $21bn by 2010 as per the table below.

Projected revenue to 2010

2000 – $3.2bn
2003 – $7.5bn
2006 – $11.9bn
2010 – $20.8bn

The social consequences

The strongest threat to the future of online gambling as a mainstream leisure activity is its impact on society. Managing the issues of problem and under-age gaming will be critical to the industry's success and the credibility of the UK regulatory environment, and these provocative issues are not ones that investors are used to dealing with. The political involvement in the emerging industry increases the need for best practice governance and compliance to build on the credibility established by a solid regulatory framework.

Perceptions are bound to change as the online gaming market becomes more mainstream, and these will be influenced by the major operators' actions to build credibility through compliance and governance, de-risking their business models in the eyes of investors. Operators who can build investor confidence can then leverage this trust, a valuable asset, and move on with consolidation strategies.

Gaining credibility

A robust control and compliance environment is a prerequisite for continued growth, a healthy return on investment, and consolidation.

The UK is set to establish a reputable jurisdiction for online operators to be 'accepted by – but not regulated by'. Although the UK may have an uncompetitive tax rate which will inhibit an inward flow of companies, the allowance of European Economic Area (EEA) registered operators to market, advertise, trade and list within it will secure a central role for the UK.

Meanwhile, small states with the flexibility to provide attractive tax environments, such as Gibraltar, Malta, the Isle of Man and Alderney, will strengthen their position as dominant locations for online operations. Partygamings recent move to Gibraltar, and its proposed UK listing, illustrates this trend.

As the establishment of a regulatory environment in a respected, established gaming jurisdiction is fundamental to widespread acceptance by consumers, offshore operators will be encouraged to adopt the UK regulatory environment as best practice, even if they stay where they are. This will reassure customers and investors, while building credibility for themselves.

For expansion to continue, the veil of secrecy must be removed and replaced with transparent and independently verifiable practices that meet strict standards and are externally monitored on an ongoing basis.

Consolidation will follow

With a redefined image, legal questions settled, growth opportunities secured and social concerns managed, online gaming will be able to take its place as a mainstream industry. When this point has been reached by a few key operators, rapid consolidation will follow.

Organisations that can achieve reputational stability and secure investor confidence will begin to transform the industry from its currently fragmented and embryonic state, capturing the value of economies of scale, increased liquidity and geographical breadth. When this happens, barriers to entry that have been limited so far will rise.

We're not there yet, but we are heading in the right direction. PartyGaming and Cassava Enterprises are just two of a number of businesses at various stages of investigating potential floats on the London Stock Exchange. With estimated valuations of £3bn and £1.6bn respectively; the markets are starting to stir.

The response will provide a taster of things to come, either way it will act as a catalyst for the development of the industry.

The outcomes of the year ahead may well determine online gaming's ability to survive as a standalone industry. The alternative is being consumed by the established online product providers or consumer businesses, who have already secured the credibility and confidence that online gaming so desperately seeks.

Simon Oaten
Manager, Audit
Tel: + 44 20 7007 7647
soaten@deloitte.co.uk

Contacts

For more information about the solutions offered by Deloitte, contact your nearest Tourism, Hospitality and Leisure expert.

United Kingdom

London
Adrian Balcombe
+ 44 20 7007 2944
abalcombe@deloitte.co.uk
Nigel Bland
+ 44 20 7007 2761
nbland@deloitte.co.uk
Gerry Boyle
+ 44 20 7303 6317
gboyle@deloitte.co.uk
Julia Felton
+ 44 20 7007 3438
jfelton@deloitte.co.uk

London
Alex Kyriakidis
+ 44 20 7007 0865
akyriakidis@deloitte.co.uk

Karen Potts
+ 44 20 7007 2980
kpotts@deloitte.co.uk
Marvin Rust
+ 44 20 7007 2125
mrust@deloitte.co.uk
Tim D Steel
+ 44 20 7007 0898
tdsteel@deloitte.co.uk
Nick van Marken
+ 44 20 7007 3354
nvanmarken@deloitte.co.uk
Manchester
Dan Jones
+44 161 455 6872
danjones@deloitte.co.uk
Leeds
Chris Wray
+ 44 161 455 8690
cjwray@deloitte.co.uk
Crawley
Graham Pickett
+ 44 1293 761 232
gcpickett@deloitte.co.uk

Asia/Africa/ Middle East/Pacific

Auckland
Nick Main
nmain@deloitte.co.nz

Beijing
Terry Wang
terwang@deloitte.com.hk

Dubai
Firas Eid
feid@deloitte.com
Hong Kong
Richard Ho
richo@deloitte.com.hk
Martin Hills
marhills@deloitte.com.hk
India
Mani Bharadwaj
mabharadwaj@deloitte.com
South Africa
Rob O'Hanlon
rohanlon@deloitte.co.za
Sydney
Peter Forrester
pforrester@deloitte.com

Canada

Ryan Brain
rbrain@deloitte.ca

Continental Europe

Amsterdam
Joop Kluft
jkluft@deloitte.nl
Onno Oldemn
ooldemn@deloitte.nl
Athens
Michael Hadjipavlou
mhadjipavlou@deloitte.gr
Austria
Michael Koevesi
mkoevesi@deloitte.at
Frankfurt
Reinhard Drewes
redrewes@deloitte.de
Madrid
Javier Jimenez Garcia
jjimenezgarcia@deloitte.es
Malta
Nick Captur
ncaptur@deloitte.com
Milan
Marco Zalamena
mzalamena@dt.deloitte.it
Munich
Michael Mueller
micmueller@deloitte.de
Paris
David Dupont-Noel
ddupontnoel@deloitte.fr
Alain Pons
apons@deloitte.fr
Rome
Nadia Fontana
nfontana@deloitte.it

South America

Brazil
Walter Dalsasso
wdalsasso@deloitte.com.br
John Auton
jauton@deloitte.com.br

United States

Atlanta
Randy Conyers
rconyers@deloitte.com
Mark Diamond
mdiamond@deloitte.com
Dave Herskovits
dherskovits@deloitte.com
Dwight Mathews
dmathews@deloitte.com
Chicago
Richard Carlson
rcarlson@deloitte.com
Howard Engle
hengle@deloitte.com
Tom Linden
tlinden@deloitte.com
Las Vegas
Steve Comer
scomer@deloitte.com
Larry Krause
lakrause@deloitte.com
Los Angeles
Ron McNair
rmcnair@deloitte.com
Neale Redington
nredington@deloitte.com
Steve Steinhauser
ssteinhauser@deloitte.com
McLean
Steven Tapp
stapp@deloitte.com
Miami
John Zamora
johnzamora@deloitte.com
New York
Michael Gamache
mgamache@deloitte.com
Guy Langford
glangford@deloitte.com
Steve Theriot
stheriot@deloitte.com

New York
Adam Weissenberg
aweissenberg@deloitte.com

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Tel: +44 (0) 20 7936 3000. Fax: +44 (0) 20 7583 1198.

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