



Disruptive forces

BTG Advisory looks at rising consumer spending, notwithstanding the disruptive forces of political and economic uncertainty, and how technology is helping to meet the challenge of maintaining margins in a rapidly evolving environment.

Innovation is transforming the leisure and hospitality sector. The sharing economy has produced new business models that are enabled by sophisticated technology. These are broadening the marketplace, offering new services as well as new ways to buy and access them. They are also shifting customer expectations and purchasing patterns.

Although travel, hospitality and leisure are generally among the first sectors to be affected by political and economic uncertainty, in recent months the market has seen steady, continuous growth, notwithstanding the implications of Brexit and the election of the Trump administration in the US.

According to the British Hospitality Association (BHA), the UK hospitality industry is the sixth largest contributor to export earnings and fourth largest employer, accounting for 4.49 million people, or 10% of the workforce, and over 180,000 businesses.

ONS figures for the year ending March 2016 indicate that the people of Britain were spending more on restaurants and hotels, with households spending on average more than £45 a week for the first time in five years. This reflects the swing in household spending from goods to services and the cultural shift from products to customer experience.

Furthermore, notwithstanding the general availability of affordable, sophisticated communication technology, companies are spending more than ever before on business travel.

According to the Global Business Travel Association (GBTA), business travel spending topped \$1.2 trillion in 2015, growing 5% over 2014, and was forecast to reach \$1.3 trillion in 2016.

Business travel supports the core elements of the leisure and hospitality industry – transport, hotels, and restaurants – and business travellers seeking streamlined services and a friction-free experience have embraced the sector's digital transformation.

The sharing economy has shifted the focus of travel and hospitality operators from providing services to offering holistic experiences through mobile apps, artificial intelligence (AI) and connected devices – the Internet of Things (IoT) – that provide personalised, on-demand functionality designed to remove pain points and create a tailored experience.

This brings opportunities for the big global operators to leverage innovation by finding new ways to augment and enhance traditional services and create new ones, but it also brings challenges in the form of increasing competition from market entrants offering competitively priced alternative services and more demanding customers with 'always-online' access to a broad choice of offerings and whose preferences and expectations change as the market develops.

Brexit and Market Uncertainty

Economic factors include a slowdown in economic growth, and consumer and corporate uncertainty. In the US, the Trump administration promised a business-friendly agenda, particularly towards the hotel industry, but restrictions on travel and immigration impact both the consumer and the service aspects of the industry, and leisure and hospitality stocks declined following the travel ban announcement.

In the UK, there is concern about the effect of Brexit on the sector. Although the weaker pound could potentially boost inbound leisure travel, fewer European tourists visited London in the three months after the shock Leave win in the Brexit referendum, with visitor numbers falling around 2% from 2.98m to 2.92m between July and September 2016.

On the corporate finance front, while the weak pound makes UK assets more attractive, the UK's uncertain outlook could deter investors and inhibit new deals. This was indicated by the dramatic slowdown in deal levels in the run-up to the Brexit referendum and the fact that some deals that were anticipated to close in 2016 have been deferred.

The impact on employment is a more immediate dilemma. Hotels and restaurants rely on migrant workers, who are prepared to work for minimum wages and a potential shortage of skilled labour from the EU is likely to impact margins. According to the BHA: "Between 2011 and 2015, the number of migrant workers in the hospitality and tourism sector has increased by 22%, with the majority of this increase coming from EU countries."

Consequently, in December 2016, the CEOs of restaurant chains including Leon, Wagamama, Pizza Express, Wahaca, Yo! Sushi and Carluccio's wrote a joint open letter to Prime Minister Theresa May, published in the *Evening Standard*, asking her to give assurances that they will be able to retain foreign EU workers after Brexit and to ease the burdens caused by soaring business rates, taxes and the weak pound.

Deal Activity and Brand Consolidation

Accommodation supply is another consideration. There are 625,000 hotel rooms across the UK and plans to add a further 18,000 in 2017 – 7,000 of them in London. Hoteliers are concerned that this could slow down trading and reduce margins, which will already be damaged by employment issues following Brexit.

RevPAR (revenue per available room) reached a 15-year high for London hotels in 2015, but higher operating expenses diminished profit margins and there was a 0.5% decline in 2016. Although occupancy levels were high by global standards at 80%, this represented a decline of 0.8% on 2015. The UK regions had a better year in 2016, with occupancy levels increasing by 0.5% and RevPAR by 2.3%. (Source: HotStats)

2016 saw continued M&A activity in the hospitality sector. JLL expects global hotel real estate transactions to maintain their 2016 level of \$60bn. This reflects the steady increase in international travel, although some destinations, notably, France, Belgium and Turkey, have been affected by terrorist activity.

While 2016 fell short of the 2015 peak, consolidation among parent companies continued, with major transactions including Marriott International's acquisition of Starwood Hotels & Resorts and HNA Tourism Group's purchase of Carlson Hotels, and announced stake acquisition in Hilton Worldwide.

According to JLL, the rationale for hotel brand consolidation is that equity analysts favour brands with a broad range of offerings in terms of service levels and geography. Full-service brands that changed ownership at parent company level since 2014 represent 30% of all full-service branded rooms globally.

Technology-powered Market Disruptors

The most significant driver of change is technology, which underpins the online market place and the sharing economy.

Online Bookings

Online travel agencies (OTAs) represent a significant market force. Statista predicts that the online travel industry will grow from \$533bn in 2015, to \$762bn by 2019.

Online booking system provider TrekkSoft collated the following statistics:

- "Tour and activity providers tend to get 30–40% more bookings after implementing an online booking system" (TrekkSoft, 2016)
- Millennials "fluent and comfortable with booking plans online, as well as on mobile and tablet devices" (HVS, 2013)

As the online marketplace matures, consumer behaviour in terms of how people find and book travel, hotels and restaurants is shifting. As websites improve and include real-time pricing and efficient payment processing – along with packages and offers – more people are booking directly with airlines and hotels, and comparison sites are having to up their game to retain market share. The main way they do this is by including customer reviews, which have become an important influencer.

Importantly, mobile accounts for a growing percentage of online bookings. According to Google, mobile travel-related searches increased by 25% in 2016 and conversion rates on mobile sites increased by 88%. Furthermore, 65% of travellers make same-day hotel reservations from a smartphone.

Online Travel Booking Statistics

	Data
Number of travel bookings made on the internet each year	148.3 million
Percentage of all travel reservations made on the internet	57 %
Percentage of same-day hotel reservations made from a smartphone	65 %

Internet Source for Hotel Booking

	Share of Bookings
Brand website: Website where distribution is operated and managed by the brand (e.g. www.marriott.com/).	65.4 %
Merchant website: (e.g. Expedia/Hotels.com, Travelocity and Orbitz).	19.5 %
Opaque website: Customers choose a fare or rate without knowing the brand of the supplier until after the item is purchased (e.g. Priceline).	11.3 %
Retail website: Third-party distributor where the hotel lists inventory at the same price that it is sold to the consumer and hotel pays distributor agreed commission (e.g. HRS, Bookings, Venere in Europe).	3.7 %

Source: Statistic Brain

This trend is set to continue, particularly as advances in mobile payment methods are making mobile bookings easier.

The Sharing Economy

The sharing economy is forcing traditional operators to find new ways to differentiate themselves from disruptive market entrants.

Peer-to-peer intermediaries such as Airbnb, Uber and Deliveroo are accelerating the pace of change and altering the value of physical assets.

It took just four years for private rental platform Airbnb to establish a significant market share that futurist Anders Sorman-Nilsson compares with Marriott, adding that 10% of Airbnb bookings are business bookings.

Traditional Hotel Operator Vs. Sharing Community	
Marriott	Airbnb
88 years to build	4 years to amass
697,000 rooms	650,000 rooms
80 countries	192 countries

Source: Anders Sorman-Nilsson's Futurist keynote: Disruption in the Hospitality Industry

According to travel management firm Concur, the value of corporate spending on Airbnb increased by 42% in 2016. Airbnb for Business has announced partnerships with American Express Global Business Travel, BCD Travel, and Carlson Wagonlit Travel which will integrate Airbnb for Business into their platforms and allow employees and travel managers to book accommodation.

However, lack of regulation, including health and safety standards, and the fact that peer-to-peer platforms do not own the assets they trade in – Airbnb owns no properties, Deliveroo has no restaurants, Uber has no cars – means that there are no across-the-board standards for the sharing economy, and this is a potential deterrent for business travellers, who may also require workspace and meeting facilities. But Airbnb is making inroads into the leisure market. According to Morgan Stanley's AlphaWise survey, 12% of leisure and corporate travellers have used Airbnb in the last 12 months and these figures are expected to rise. However, Airbnb's minimum stay requirements are a deterrent to business travellers. Single night stays account for around 25% of hotel bookings.

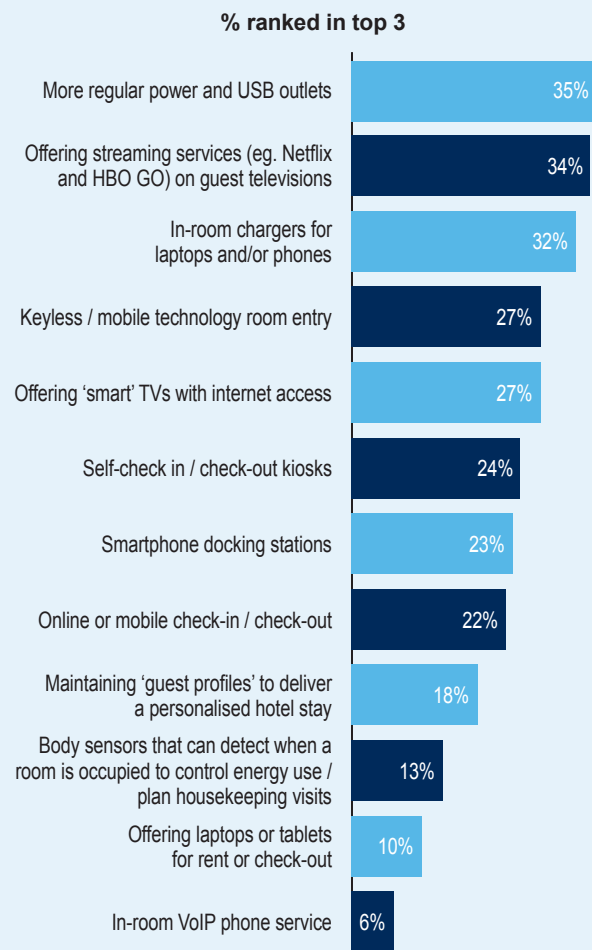
The global and international hotel and leisure brands retain a loyal customer base, particularly among business travellers, because they offer consistent standards of accommodation – and they need to comply with regulatory requirements for health and safety, for example – convenient services like 24-hour check-in, free cancellation and on-site amenities like room service and laundry. They are using technology to build their brands across different platforms and offer additional services and facilities.

Global hotel chains are also competing directly with the disruptors. As the sharing economy matures, hybrid business models are developing, including the branded, hotel-chain-owned Airbnb equivalent. AccorHotels, Europe's largest hotel group (which also owns the Savoy in London and Raffles in Singapore) bought British serviced home rental company onefinestay for €148m. Wyndham Hotels, whose brands include Ramada and Travelodge, has taken a stake in another London-based start-up, LoveHomeSwap, a subscription service that allows homeowners to swap homes. And InterContinental Hotels Group, the world's largest hotels operator by number of rooms, announced a partnership with Norwegian Stay.com

Hotel Tech

Hotels are also raising their technology game. They are learning from the community-based, hyper-local focus of the shared economy and introducing technology-enabled services that resonate with business travellers and millennials – and support their brands. Unsurprisingly, the top priority for business travellers is internet access, and 75% of respondents to a GBTA study were satisfied with in-room internet access. However, they were also interested in using technology that most hotels do not offer.

Which New Hotel Technology Innovations Are Business Travellers Most Interested in? (n=787)



Source: GTBA Foundation

Apps, Chatbots and More

Market entrants, both peer-to-peer such as Airbnb and Uber, and third-party delivery platforms such as Deliveroo and UberEATS, rely on mobile apps to offer a personalised experience. Mainstream hotel chains too are introducing services that cater for guest preferences.

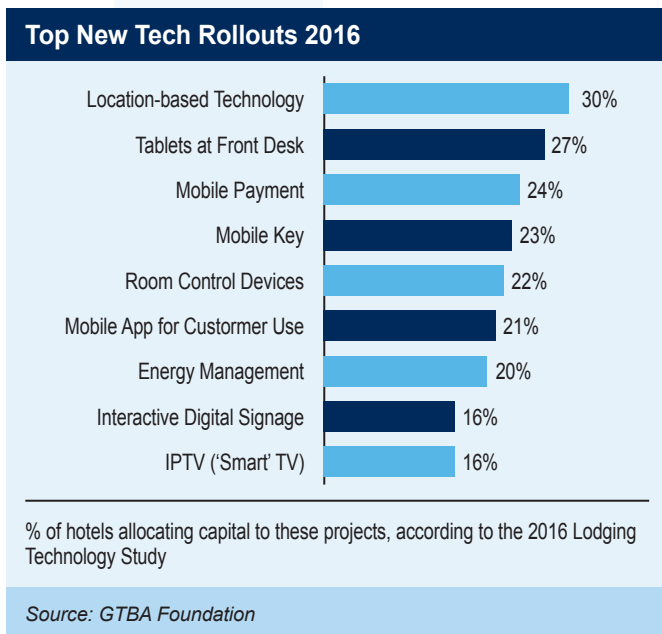
For example, hotel apps enable guests to book and check into hotels – and order room service – as well as providing mobile payments and mobile keys.

According to a GBTA study, in 2016, 61% of business travellers downloaded at least one of the seven major hotel chains' apps on their smartphone. Apps are used most often to check the status of a reservation (43%) and book a hotel stay (39%), and although only 25% of respondents used mobile check-in, they indicated that if keyless entry expands, they would be likely to use mobile check-in more frequently.

Jolyon Bulley, COO InterContinental Hotels Group (IHG) – the Americas, told *Forbes* that he was excited by the potential that digital technology offers the sector, highlighting “the capacity to view social listening as a great insight provider, the strengthening of direct booking channels into our hotels, and using our loyalty program as a channel for us to strengthen our brands and our owners' returns”. IHG are applying advanced analytics to the data generated by the 99 million members of the IHG Rewards Club programme, which offers loyalty incentives including special rates and extra services. Bookings made through the IHG app were up 50% year-on-year, as at February 2017 and more than 1,800 properties allow mobile check-out. Digital revenue for the year totalled \$4.3bn, with mobile digital revenue reaching \$1.6bn and for the first time constituting more than 50% of global digital traffic (60% in China).

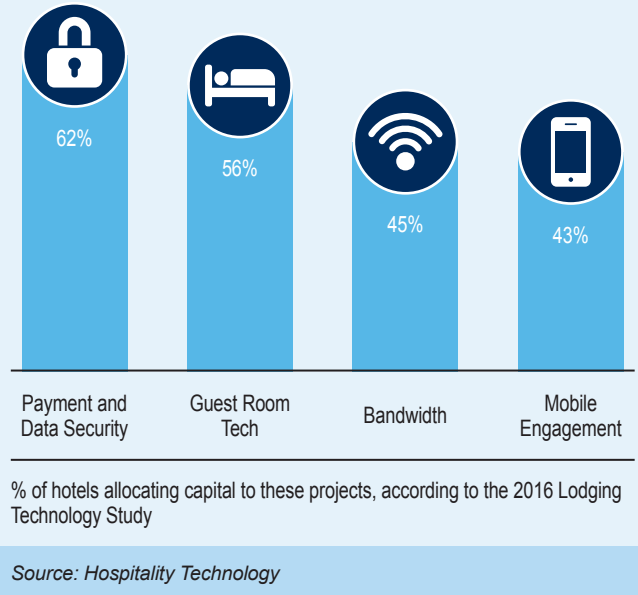
Meanwhile Marriott has been working to personalise its mobile app, which is available in five languages and includes personalised digital features such as custom travel content and mobile key capabilities.

Hotels are investing in the latest technology as this differentiates their properties from the sharing economy. Hospitality Technology highlighted the top tech rollouts for hotels in 2016:



The top priorities were payment and data security, guest room tech, bandwidth and mobile engagement, which would include apps.

Priorities for 2016 Hotel Tech Spending



Robot Restaurants

Technology is a significant factor in trends affecting the restaurant sector. Economic and geopolitical issues exacerbate the effect of multiple labour issues, including pay regulations, notably the national living wage and national minimum wage, and concerns about restrictions on worker mobility because, like hotels, restaurants rely on migrant workers and casual labour.

This has led to the development of smart technologies to streamline and automate processes, with the idea of reducing staffing requirements, and once the initial investment has been offset, maintaining margins. These increasingly include customer facing processes, ranging from booking and ordering apps, accessed via a variety of devices including Apple Watch, to fully automated fast food outlets. Dominos introduced a chatbot for a limited menu; Wingstop's chatbot service covers its entire menu, and includes six interfaces for digital ordering, including via social media and Momentum Machines has developed a burger-making robot for its restaurant in San Francisco.

Gamification touched restaurants during summer 2016, when the viral augmented reality game Pokémon GO led to restaurants creating PokéStops to attract customers. Having seen for themselves the effectiveness of augmented reality, some restaurants have created games for guests to play and others have introduced interactive ordering and services. One example is Inamo in London, which has an interactive menu that projects an image of the food onto your plate as you scroll through the menu and enables you to order food, play games and book a taxi home. Other establishments use VR for training.

The boom in food delivery companies reflects the ubiquitous shift to online shopping, and perhaps that busy professionals and entrepreneurs are less likely to spend time cooking. According to Euromonitor, the European market for takeaway and delivery reached £18.4bn in 2016, while the value of food bought in restaurants fell by 7.6% per cent to £135.3bn. Food delivery companies like Deliveroo and Just Eat have enabled high-end restaurants to add a take-away option, giving customers more choice and extending restaurants' reach. Food delivery companies are attracting significant investors. A *Financial Times* article stated that Deliveroo's latest investment round gave the company a reported value of about \$600m. Just Eat has market capitalisation of close to £3bn. In 2016, digital businesses Amazon and UberEATS entered the food delivery space. Online ordering has also created new business models, such as online-only restaurant EatFirst www.eatfirst.com, which is accessed via its website or app, social dining platforms, and even immersive dining events such as Gingerline www.gingerline.co.uk

The Feedback Loop

The sharing economy, like the online marketplace relies on the feedback loop, and operators recognise the influence of authentic customer reviews, which have become an integral part of the travel planning process. A TrustYou survey found that 95% of respondents read reviews before booking. Leisure travellers read an average of 6–7 reviews before booking (spending an average of 30 minutes, although 10% spend more than an hour); business travellers read an average of five (Tnooz, 2015).

An Uncertain Future

Disruption has created a new normal in travel and hospitality and although there are economic and operational challenges, advances in technology have led to something of a renaissance across many parts of the sector. The sharing economy has revitalised the industry, attracting more business while forcing traditional operators to consider their customers' various requirements. Increased use of technology enables them to enter a dialogue with customers to uncover their preferences which are used to personalise services and design a broader choice of services and brand offerings. And technology brings opportunities as well as challenges. As well as creating a climate of innovation, tech-powered hospitality is creating employment. Although tech can replace some workers, it is also creating new roles, which have become key to competitive advantage. For example, Hilton Hotels & Resorts has added 140 positions in the past two years to manage the company's data centres, websites, mobile apps and IT support. The new hospitality experience, whether via the sharing economy or more conventional hotels and restaurants, is personalised, seamless and friction free – but only if the technology works!

For Further Information

If you would like to discuss any of the issues raised in this update or would like to know further details about the services we provide to the sector, please contact:



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