



**Digitisation of
the travel and
hospitality industry**

**Part 1:
Imperative
For Change**

July 2017

Part 1: The imperative for change

The travel industry is moving towards an increasingly connected future in which platforms, personalisation and integrated technology play a central role. Predictions for the near future are a wake up call for all incumbent businesses.

Travel and tourism continues to be a high-growth industry but the progress of digitisation is increasing the level of competition, putting pressure on revenues and profits. To take advantage of market growth, incumbent businesses need to understand the direction of change and the most promising strategies for success.

This paper forms the first in a three part series examining the direction of change in travel and hospitality with exclusive insights from industry leaders. Contributors include senior executives at IHG, Sabre, Hilton, Carlson Rezidor and the World Travel and Tourism Council, among others.

The three
reports cover

- 1 The current state of the industry and imperative for digital development
- 2 Leading strategies for success for incumbent businesses
- 3 Overcoming barriers to change

Growth and competition

Travel and tourism outperformed the global economy for the sixth year running in 2016, reaching a total of 10.2% of world GDP (\$7.6 trillion).¹

According to the World Tourism Organisation (UNWTO), international tourist arrivals grew for the seventh consecutive year, reaching 1.2 billion in 2016.² Asia and the Pacific regions have shown the strongest growth.³ UNWTO projects that international travel will grow at an average of 4% p.a. to 2030 (Fig 1).

International tourist arrivals forecast to reach 1.8B by 2030

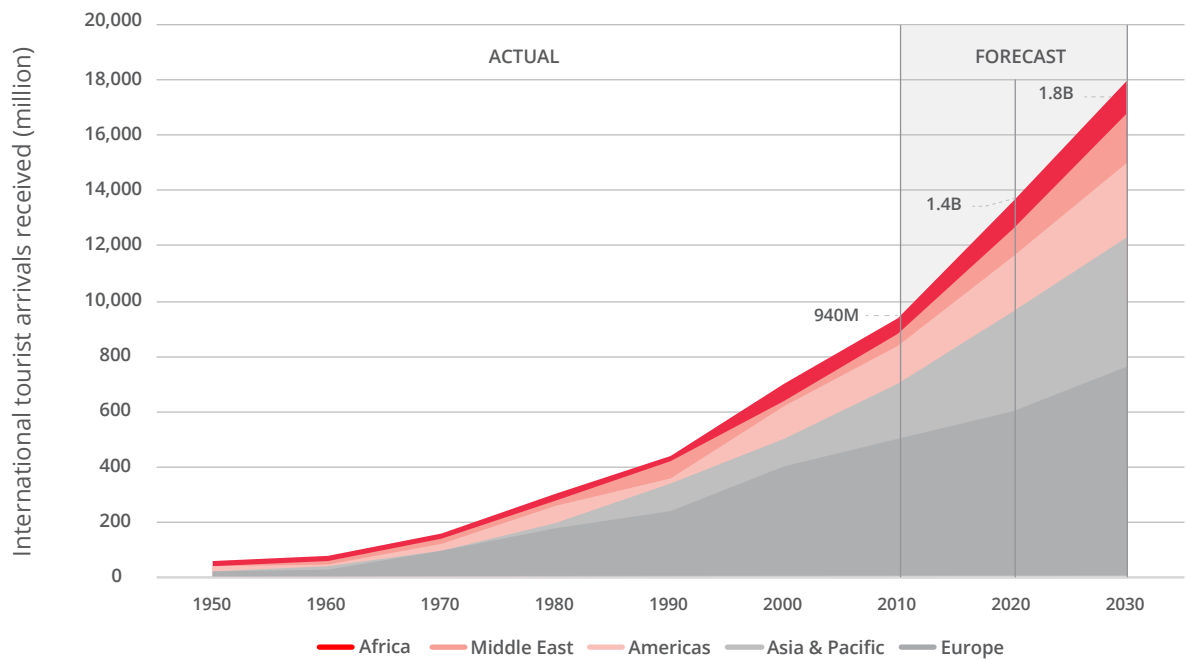


Fig 1. UNWTO tourism towards 2030: Actual trend and forecast 1950 - 2030

SOURCE: UNWTO

What remains to be seen is which businesses will benefit most from this continued growth and which will lose out. It is here that digital readiness will be the greatest differentiator.

Growth in direct contribution to GDP 2016

Travel and tourism growth second only to information and communication

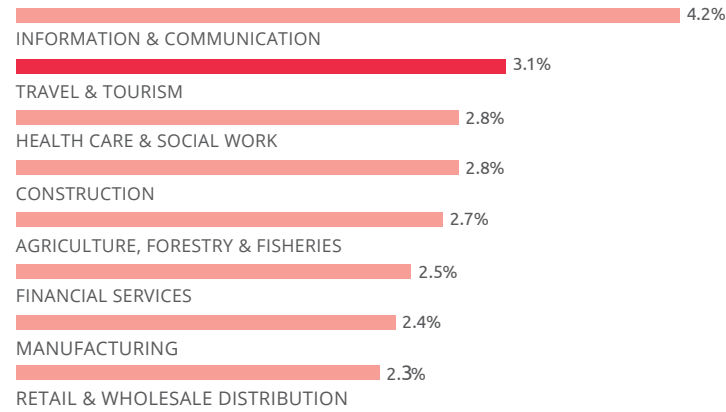


Fig 2. World industry GDP growth: Travel & Tourism second only to Information & Communication
 SOURCE: World Travel & Tourism Council (WTTC) Global Economic Impact & Issues 2017

Digital differentiation

As digital technology reduces transactional friction it increases the level of competition, exerting downward pressures on revenue and profit. Digital penetration currently stands at 44% for the travel industry, behind healthcare, high-tech, retail and media⁴. While it can appear that digitisation is already advanced, in reality we are living through the early stages.

Current levels of digitisation across all industries have already reduced average revenue growth by 6 points and EBIT growth by 4.5 points with increasing pressure forecast as digital penetration continues (Fig 3).

Digitisation puts pressure on revenue and profit growth

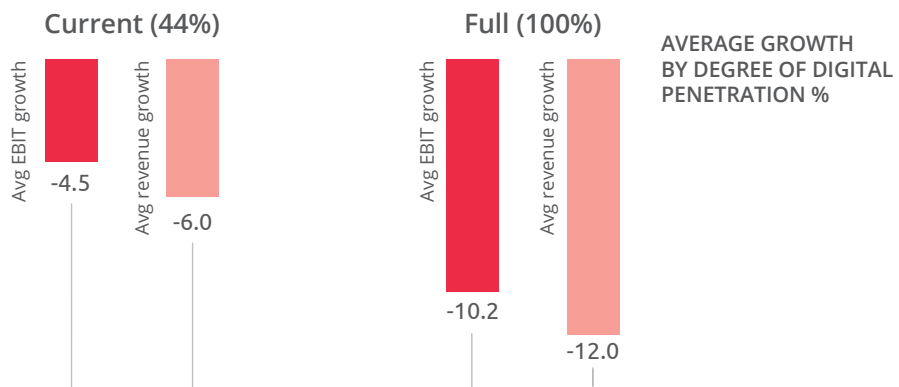


Fig 3. Average revenue and EBIT growth by degree of digital penetration (%)
 SOURCE: The case for digital reinvention, McKinsey 2017



This pressure will not impact all companies evenly. Those who identify opportunities for disruption and make bold and distinctive plays stand to gain disproportionately at the expense of laggards who will struggle to survive. In the middle ground the incumbents who rapidly adapt and execute their transformations well also stand to make gains and take advantage of the upward pressure of industry growth.⁵

“The travel and tourism industry is extraordinarily robust and resilient. If you look back over time at hotels or airline businesses, car rental or cruise businesses... all of these sectors and companies have found ways of either pivoting their business model or reinventing and repositioning themselves as very different entities.”⁶

David Scowsill
President & CEO, World Travel & Tourism Council

Over the coming decade from 2016-2025, the digitisation of aviation, travel and tourism is expected to create up to **\$305 billion in industry value**.⁷ This will come from increased productivity of people and assets, increased demand for personalised products and services and new efficiencies from sharing models.

The World Economic Forum predicts a shift of \$100 billion from traditional players to new competitors as OTAs take an even larger portion of booking revenue and undifferentiated hotels lose market share to short-term rentals.⁸

*The important question is not whether your business will change, **but how.***

The direction of change

Rapid technology adoption and innovation

Digital technology is evolving with consumer adoption at an increasingly rapid pace. To understand where your customers are heading it is wise to pay attention to the early adopters.

Increasing prevalence of mobile technologies

- 1 Smartphones generated one in five online hotel bookings in the second quarter of 2016.⁹
- 2 88% of travellers with smartphones would switch to another site or app if yours doesn't satisfy their needs.¹⁰
- 3 Smartphone ownership is now above 70% in the UK¹¹ and nearly 80% in the US.¹²

Research by Google shows that an increasing amount of time is spent researching trips on mobile phones, with 40% of US travel site visits coming from mobile in 2016. Visit session times are shrinking and yet conversion rates have grown by nearly 10% on mobile travel sites.¹³ Customers are using their phones to search for specific pieces of information and these figures suggest that if they don't find it they will quickly go elsewhere.

Consumer expectations are evolving

- 1 Making a task easier is the top motivating factor for downloading travel apps.¹⁴
- 2 Ease of use and navigation is nearly twice as important as any other travel app feature.¹⁵
- 3 When people have a negative brand experience on mobile, they are 62% less likely to purchase from that brand in the future than if they have a positive experience.¹⁶
- 4 59% of people are likely to recommend a brand if it delivers a frictionless experience across channels.¹⁷
- 5 89% of US marketers reported that personalisation on their websites or apps resulted in an increase in revenue.¹⁸

The progression of digital technology continues to raise consumer expectations. Consumers are becoming increasingly empowered and discerning with the wealth of information available online.

Trust and ease of fulfillment is key to decision-making and personalisation forms an integral part of this process. In a market where there is endless choice, and where customers are wary of being misled, established brands can succeed by easing the path to purchase. User experience (or UX) has become the top priority for both customer retention and advocacy.

A hand holding a smartphone with a network overlay graphic. The background is a blurred green and white pattern with a network of white lines and dots overlaid on it.

Actionable insights from big data

Improved data intelligence is being used to target consumers based on intent. Analysing preferences and buying behaviour enables targeted offers along the customer journey. The challenge lies firstly in capturing the right data and secondly in making it accessible enough to access at speed for decision making.

Alex Alt, President of Sabre Hospitality Solutions, describes the process as **'data intended'**¹⁹: building data-collecting functions into products, along with the ability to use the collected data to provide insights that inform decision-making.

The addition of cloud computing is crucial to the wide accessibility of this data, enabling availability across all brand touch points. At scale, cloud computing can provide services at low unit costs with improved resilience, availability and security.

The new shape of social media

Messaging platforms, including Whatsapp, Facebook Messenger and others, have become an integral to the social media landscape. Whatsapp has replaced some of the functions of Facebook, Twitter, email and text messages for sharing photos, making plans and communicating with friends and colleagues.

Considering all age groups, Facebook continues to be the most popular social media platform with 1.87 billion active users.²⁰ But when you look at growth Whatsapp and Facebook Messenger lead the pack, gaining over 500 million new active users in the past two years (Fig. 4). Companies including the BBC and Just Eat have already started using Whatsapp to engage with customers.²¹

Direct messaging leads social media growth

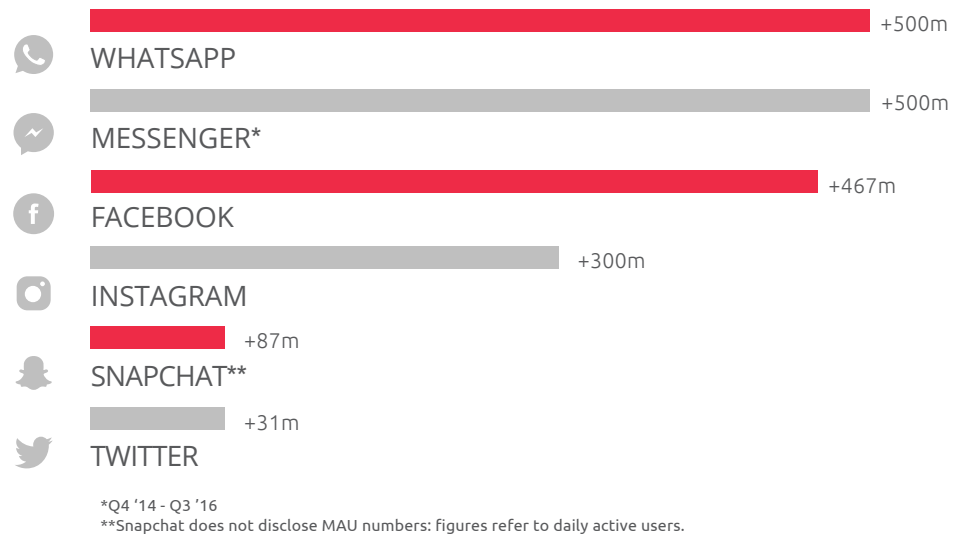


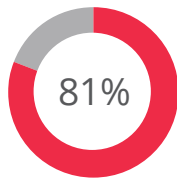
Fig. 4 Absolute increase in monthly active users (MAUs) on social media platforms Q4 '14 - Q4 '16

SOURCE: Company filings and announcements, Statista February 2017

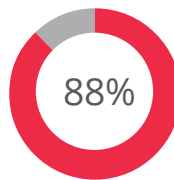
Companies are trying to understand the way young people interact with new technology and a few have recognised the need to bring younger voices into their decision-making. Both Accor and Mövenpick have established Gen-Y or millennial committees comprised of employees and outsiders under 35 years old.

Olivier Chavy, CEO and President of Mövenpick hotels recounts a conversation with his Gen-Y committee: 'I asked them, "What do you want me to do when you arrive in my hotel?" They told me, "When I land, send me a Whatsapp". You know, I'm 53 years old I never thought that sending a Whatsapp was more powerful than an app.'²² At this stage in digital development the wisest leaders will be those who recognise the limits of their digital expertise and seek out informed opinions.

The power of consumer reviews



of people read reviews and check ratings²³



of consumers say they trust online reviews as much as personal recommendations²⁴

“TripAdvisor’s consumer reviews, whether they’re for hotels or restaurants or attractions, have been fundamental to changing and improving the consumer experience... The whole review approach has put the power in the consumer’s hands.”²⁵

David Scowsill
President & CEO, World Travel & Tourism Council

The challenge for travel and hospitality companies is to make the review process advantageous for their business. Success comes in two parts. The first is visibility: 54% of TripAdvisor’s global users will not book a hotel that has no reviews. The second is responsiveness: the majority of TripAdvisor users (65%) are more likely to book a hotel which responds to traveler reviews, versus a comparable hotel which doesn’t provide management responses.²⁶

New interfaces and artificial intelligence

“Artificial intelligence and robotics will allow us to engage with the consumer in a way that we haven’t done before; truly understanding behaviours, needs and desires.”²⁷

Wolfgang Neumann
Chairman, Board Director & CEO
Carlson Rezidor Hotel Group

Artificial intelligence is the next step in responding to consumer input and enabling mass personalisation at scale. It is already enabling businesses to predict customer desires and changes in demand based on past data. AI can help businesses optimise messaging, pricing, distribution and availability to improve revenue and profitability.

Alex Alt of Sabre predicts that the next big development will include the evolution of voice recognition, including chat bots programmed to recognise and respond to natural language.²⁸ Using Apple's Siri, or Amazon's Alexa to book travel from your sofa may very quickly become a reality.

The Internet of Things

“Customers are becoming accustomed to controlling their life from the palm of their hand, from their smartphone. The expectation of being able to do that in other parts of their life should carry through to travel, either on business or for leisure.”²⁹

Chris Silcock
EVP & CCO, Hilton

By 2020 there will be approximately 6.6 connected devices per person.³⁰ With intelligent automation and control, devices can connect themselves seamlessly without human intervention. This already includes smart thermostats in the home, electric cars that can read the next destination from your Google calendar and hotel room choice and setup from your smartphone. The Internet of Things enables users to instantly personalise the world around them. Technology that adapts to location and preferences and anticipates consumer needs is set for enormous growth.



Industry evolution and disruption

Disruption is already evident in the travel and hospitality sector. Competitive forces are shifting significantly, forcing incumbents to reconsider their positioning.

The continued rise of OTAs

The power of online travel agents has grown rapidly. As the sector matures Priceline, Expedia and Ctrip have emerged as the three major players, outstripping the growth of their competitors. Google has entered the market with instant booking for hotels and restaurants, while the boundaries between OTAs and metasearch sites continue to blur.

With hotels comparatively more fragmented than airlines, OTAs look set to continue to eat into hotel revenues. Both metasearch and OTA sites ease the search and selection process for customers and thus continue to fill a valuable niche in the customer journey; 47% of OTA bookers surveyed said 'ease of use' was their reason for doing so.³¹

“ I continue to think that the transient market is going to be OTA-dominated - hotels will have to fight very hard to identify and hang on to customers that are best described as transient simply because it's easier to find an OTA booking tool (rather than a hotel website) if you're a transient customer, or because transient-oriented loyalty schemes that one or two of the OTAs offer will further enhance the value of the OTA offering.”³²

David Roche,
Chairman of Guestline and former President at Expedia

It has become near impossible for major hotel chains to compete with the big OTAs on advertising spend and thus on visibility. Expedia's marketing expenses have increased at a rate that few brands can fathom, with \$4.37 billion spent in 2016 (Fig. 5).

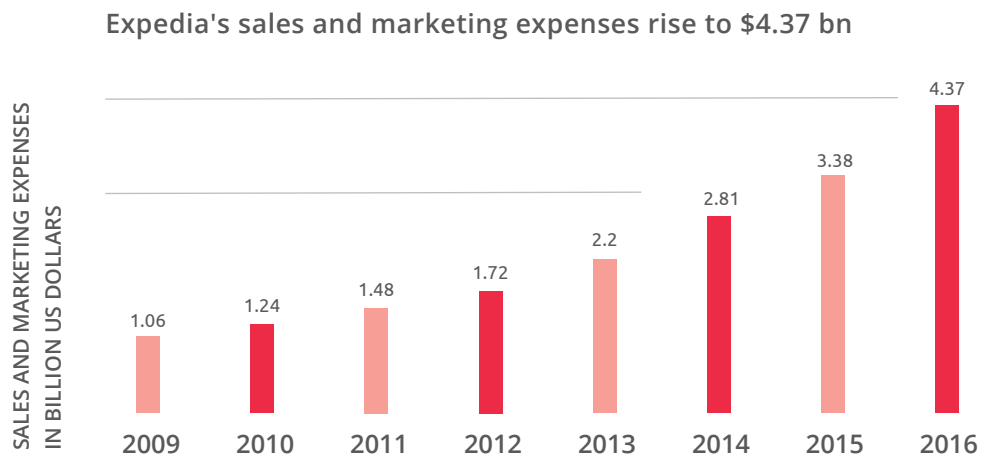


Fig. 5 Sales and marketing expenses of Expedia, Inc. worldwide 2009-2016
 SOURCE: Statista 2017

Priceline spent \$3.5bn on pay per click advertising in 2016. But note that Google was the company's biggest advertising channel.³³ Arguably Google's travel business is bigger than both Expedia and Priceline put together. The industry has yet to see what Google's end goal is here.

Airbnb and the sharing economy

Disputes continue on the extent to which Airbnb bookings encroach on the hotel market. A recent report from Morgan Stanley showed rising Airbnb adoption; of those surveyed, **approximately 49% said they had replaced a traditional hotel stay with an Airbnb stay in 2016 (Fig.6)**³⁴. The rate of growth since its foundation in 2008 has been phenomenal and follows that of similar sharing economy business models, such as Uber.

The sharing economy has extended to reach both high and low ends of the market in travel. Aside from competitive pricing, the merits of immediacy and convenience have played a significant part in this growth. Appealing to customer demands in an ultra-connected world has propelled these asset-light businesses rapidly into the mainstream.

“ Airbnb are technology-enabled, but they’re changing the way that services are provided and the nature of the experience... there are elements of the booking and the stay experience that hotels can learn from and evolve to better meet the needs of the next generation of travellers.”³⁵

Matt Luscombe,
previously CCO Europe, IHG

Airbnb replaces traditional hotel bookings

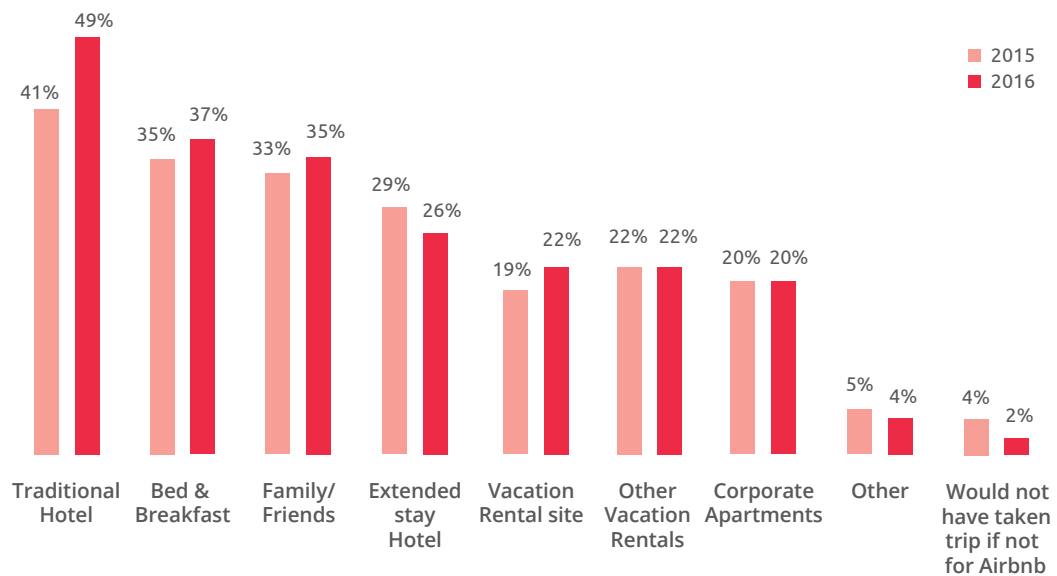


Fig. 6 Accommodation alternatives that Airbnb replaced (among Airbnb users past 12 months 2015 and 2016)

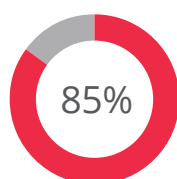
SOURCE: AlphaWise, Morgan Stanley Research

What should alarm incumbent businesses is the level of digital prowess and speed to market of these new enterprises. For traditional businesses to develop a similar level of digital readiness in talent management, hyper-personalisation and data-as-an-asset will take between four and eight years according to World Economic Forum estimates.³⁶ The time to start is now.



Functional fragmentation and consolidation

The growing number of travellers worldwide creates new opportunities for the provision of services. Limited service hotels with lower prices strike a balance in providing the basics with easy access to local amenities, allowing owners to focus on RevPAR. With this comes the potential fragmentation of traditional hotel services, including the provision of food, exercise facilities and entertainment.



85% of leisure travellers decide on activities only after having arrived at their destination ³⁷

According to Google, 85% of leisure travellers decide on activities only after having arrived at their destination leaving opportunities wide open for offers that capture their attention. For full service and destination hotels this poses opportunities to exceed customer expectations by providing activities and recommendations on arrival. It is also fertile ground for disruption, with customers readily turning to recommendations via mobile.

New businesses have capitalised on opportunities to aggregate and curate offerings around exercise (ClassPass), wellness (MindBody), beauty (StyleSeat, Treatwell), food (OpenTable, GrubHub, UberEats), and in-room entertainment (Netflix, Spotify). Airbnb has already expanded into trips and events, extending their offer from accommodation to the full travel experience.

The rise of the east

China's influence on the travel and hospitality industry is substantial and growing. It is projected to become one of the world's biggest overseas investors, tripling its investments to almost \$20 trillion by 2020.³⁸ In 2016 the National Development and Reform Commission (NDRC) and the China National Tourism Administration announced plans to invest 2 trillion yuan (\$290 billion) in tourism by 2020, prioritising key tourism projects and encouraging private investment.³⁹

There has been a rapid consolidation of hotel companies under leading Chinese conglomerates. Of the top ten hotel brands in the world, two are now Chinese owned: Jin Jiang International and Carlson Hotels (recently bought by China's HNA Tourism Group).

China leads best performing outbound travel markets

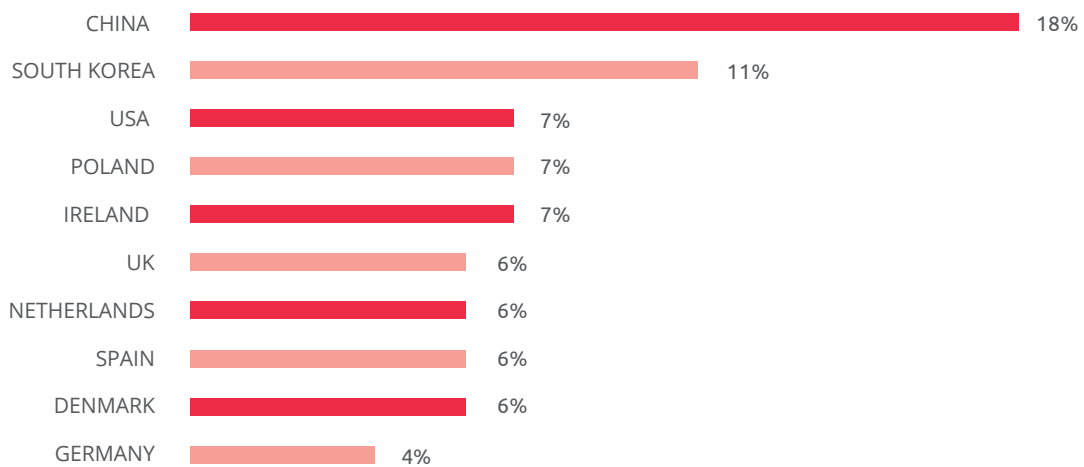


Fig. 7 Best performing outbound markets 1-8, 2016.
Increase in outbound trips (%)

SOURCE: World Travel Monitor 1-8, IPK International 2016

But it is not just China's in-bound markets that are growing. Millions of Chinese tourists are adding demand to markets around the world. According to the World Travel Monitor, China was the best performing outbound travel market in 2016 (Fig. 7), spending a total of \$261 billion on foreign travel, more than any other country's outbound travellers.⁴⁰

McKinsey estimated just 4 percent of urban Chinese households as middle class in 2000, but this grew to 68 percent by 2012.⁴¹ This middle class has grown rapidly in spending power and influence. Although China's population as whole is aging, the middle class is getting younger; of citizens living in China's cities, nearly half are under 35. They are most likely to be university graduates and privileged only children who have grown up online.⁴²

Expectations are shifting, both on the part of Chinese consumers and the tourism industry at large. As the Chinese influence continues to grow, the balance of power with the US may be expected to shift. This carries substantial implications for the future development of travel and tourism.

Conclusion

2017 sees the world travel and hospitality industry in a complex state of change. While growth and investment are strong, competition is high and rising. As digital technologies permeate the industry, the need to stake a distinctive claim whilst adapting to new methodologies becomes central to growth and success. Diagonal lines of competition are now the ones to watch; OTAs are gaining ground and status, while the sharing economy is already shifting the way consumers purchase and engage with travel.

The prospects for rapid growth and financial gain have never been higher. International sources of finance and new consumer markets are open for opportunities. For those that can secure their place in the digital economy there is everything to gain.

Expectations are evolving at a rapid pace as digital technology enables consumers to be more connected, more informed and more immediate in taking action. The rules of engagement have changed and with it the nature of the exchange that customers expect.

The second paper in this series explores the key success factors for incumbent businesses in the current market.

- ¹ World Travel & Tourism Council. Travel & Tourism Global Economic Impact & Issues 2017.
- ² UNTWO 2016 Annual Report.
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- ⁴ The case for digital reinvention. McKinsey. February 2017.
- ⁵ The case for digital reinvention. McKinsey. February 2017.
- ⁶ PACE Dimensions independent research June 2017.
- ⁷ Digital transformation initiative: aviation, travel and tourism industry. WEF, January 2017.
- ⁸ Digital transformation initiative: aviation, travel and tourism industry. WEF, January 2017.
- ⁹ Growth of mobile travel bookings in 6 charts. Skift, October 2016.
- ¹⁰ Travel booking trends revealed in let's-book-it moments. Google, July 2016.
- ¹¹ Ipsos Tech Tracker Q1 2016.
- ¹² 198.5 million people in the U.S. owned smartphones (79.1 percent mobile market penetration) during the three months ending in January. Comscore reports January 2016.
- ¹³ How micro-moments are reshaping the travel customer journey. Google, July 2016.
- ¹⁴ Google/Ipsos, U.S., "How People Use Their Phones for Travel," n=500, smartphone users aged 18-64 who used a smartphone for travel in the past month, Oct. 2016.
- ¹⁵ Google/Ipsos, U.S., "How People Use Their Phones for Travel," n=500, smartphone users aged 18-64 who used a smartphone for travel in the past month, Oct. 2016.
- ¹⁶ Google/Purchased, U.S., "How Brand Experiences Inspire Consumer Action," n=2010 U.S. smartphone owners 18+, brand experiences=17,726, April 2017.
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- ¹⁸ eMarketer/Evergage, "2016 Trends in Personalization," conducted by Researchscape. Data was provided to eMarketer by Evergage; June 14, 2016.
- ¹⁹ PACE Dimensions independent research June 2017.
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- ²⁴ BrightLocal, Local Consumer Review Survey, 2014. Appears in The rise of comparison shopping on mobile. Think with Google. July 2016.
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- ²⁶ TripAdvisor network effect and the benefits of total engagement. January 2017.
- ²⁷ PACE Dimensions independent research June 2017.
- ²⁸ PACE Dimensions independent research June 2017.
- ²⁹ PACE Dimensions independent research June 2017.
- ³⁰ Digital transformation initiative: aviation, travel and tourism industry. WEF, January 2017.
- ³¹ Channel surfing: where customers shop for travel online. Phocuswright 2016.
- ³² PACE Dimensions independent research June 2017.
- ³³ Priceline Group spent \$3.5 billion on PPC in 2016. Trooz.
- ³⁴ Who will Airbnb hurt more – Hotels or OTAs? ...One year later. Morgan Stanley, 2016.
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- ³⁶ Digital transformation of industries: Consumer industries. WEF, January 2016.
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- ³⁸ Preparing for a new era of Chinese capital. Rhodium Group & Metrics (Mercator Institute for China Studies). June 2015
- ³⁹ China targets \$290 billion investment in tourism by 2020. Reuters. Dec 2016.
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- ⁴¹ Mapping China's Middle Class. McKinsey. June 2013.
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