Hospitality and Leisure

Hospitality Directions Europe

Market sector briefing

The promise of emerging market urbanites

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PRICEWATERHOUSECOOPERS

Much of the focus of attention of the corporate world over the past five years has been on China and in particular Shanghai. However, hospitality and leisure companies should not lose sight of a trend that is present in other emerging markets as well: the rise of the middle class consumer. Disposable incomes are increasing, aspirations are westernising and shiny new credit cards are buying a plethora of products and services. To enhance our understanding of the future consumption hot spots PricewaterhouseCoopers has developed a city wealth quantitive model. This article analyses what the new economic dynamism means for leisure and hotel markets and products.

The promise of emerging market urbanites

Despite the recent downgrades in economic growth of forecasts around the world, the promise of emerging market consumers remains, as illustrated by this paper.

Introduction

Many businesses have considered what the boom in emerging markets means for their strategy, and there have been frequent reports on the topic by commentators and advisers. However, most analysis has looked at national economies, with the implicit assumption being that it is unnecessary to disaggregate further.

Data at the national level, however, hides the large disparities between the urban and rural populations often prevalent in emerging countries, with urban household wealth and consumption patterns often differing considerably from national averages. In order to be able to assist companies in the hospitality and leisure (H&L) sector in understanding the true economic consumption potential of the residents of large emerging markets cities, we have applied PricewaterhouseCoopers' urban household income model to these markets. This model enables us to quantify the size of consumer markets around the world, including:

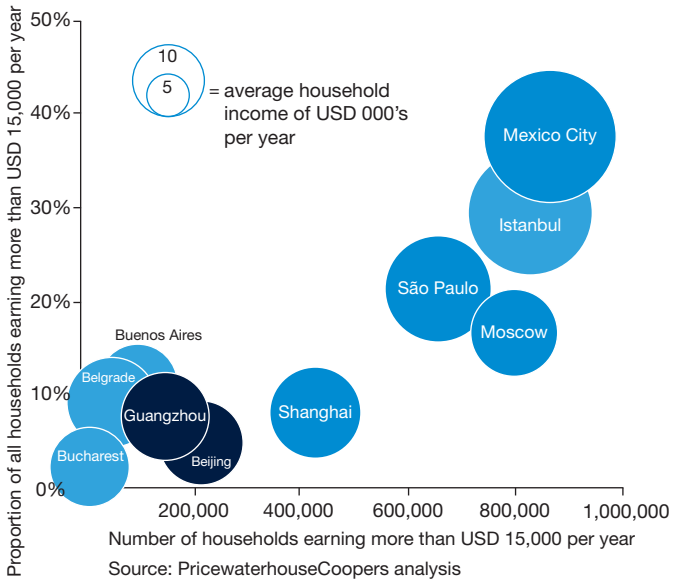
- the number of households in certain income brackets;
- the number of people in those brackets;
- the total income of households in each bracket; and
- the average income of households in each bracket.

Consumer markets beyond Shanghai

Our Consumer Markets Beyond Shanghai report showcases the modelling results for a selection of ten cities. The estimations of the relative sizes of the combined middle-class and upper-class markets in the ten cities are shown in Chart 1 opposite.

Taking Istanbul as an example, we estimate that there are more than 800,000 households that can be classified as being either middle-class or upper-class.[1] While this is a large consumer market even by the standards of developed country cities, it represents less than a third of Istanbul's total number of households. The message is clear: this city is already potentially lucrative and there is a long way to go before its growth potential is exhausted.

Chart 1: Consumption capacities of selected cities



Source: PricewaterhouseCoopers analysis

1 The households referred to in this report as being middle class are those whose annual income is between US$ 15,000 and US$ 45,000.

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The opportunities

The H&L industry is largely focussed on relatively mature markets with high levels of disposable incomes. The number of middle- and upper-class households in leading emerging market cities is approaching critical mass, thus resulting in attractive economic micro-climates for H&L companies. Three sub-sectors in particular stand out as being the most ripe for expansion into emerging markets:

- leisure and business travel accommodation;
- outdoor entertainment parks; and
- branded fast food and drinks chains.

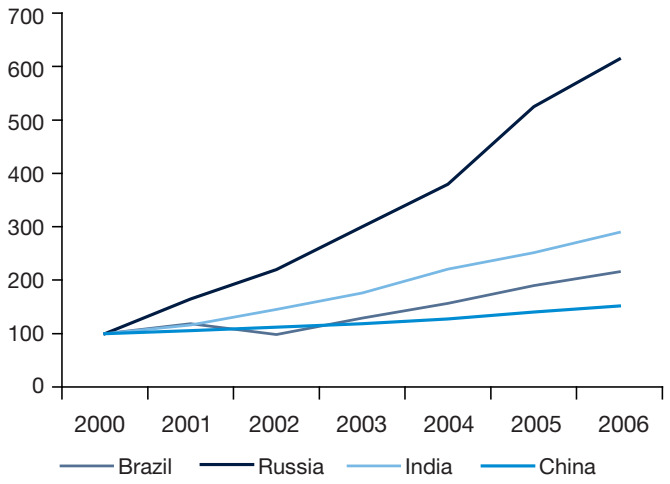
Providing accommodation in growing business and leisure travel markets

Given the general economic attractiveness of emerging markets, one of the main drivers of demand for accommodation in key cities is business travel which is related to negotiation and implementation of deals on foreign direct investment (FDI) and international trade deals. As shown in Chart 2 opposite, the stock of FDI in the BRIC[2] countries has risen considerably in recent years, especially in Russia and India. H&L companies need to continue to support with suitable accommodation products the businesses that are turning to emerging markets.

In addition to meeting the accommodation needs of foreign business travellers, H&L companies should not lose sight of the leisure travel market in countries like Russia. Although some members of the rising Moscow middle and upper classes may spend their disposable roubles on a shopping trip in London's Knightsbridge, others may decide on a ski trip in the Caucasus or a city break in St Petersburg. Rising demand for travel within Russia for both business and leisure purposes is illustrated in Chart 3 opposite. The question for H&L companies is: where will these travellers stay once they have arrived at their destination?

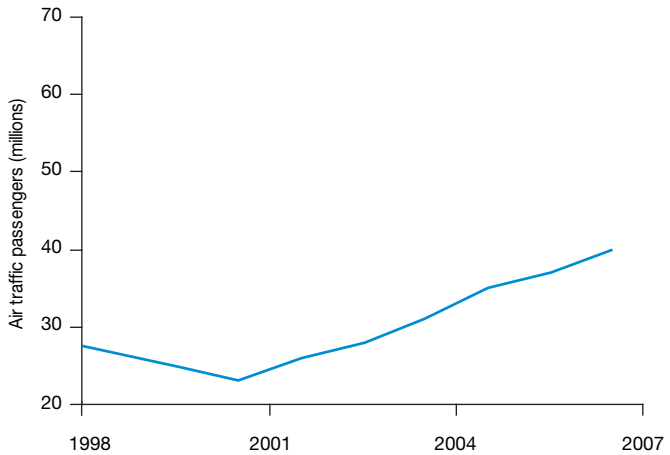
Finally, international tourism receipts across emerging markets are rising. According to the UN World Tourism Organisation, China's revenue from foreign leisure travellers reached US$ 41.9 billion in 2007, rising from US$ 16.2 billion in 2000. The number of international visitors to China increased by 75 per cent over the same period. Similarly, Russia's revenues increased from US$ 3.4 billion to US$ 9.6 billion between 2000 and 2007. These trends offer H&L companies attractive revenue opportunities, but expanding their presence in emerging markets could also be seen as part of maintaining brand contact with mature market customers.

Chart 2: Index of FDI stock in BRIC (2000 = 100)



Source: UNCTAD

Chart 3: Russian domestic air traffic passenger numbers



Source: Russian Federal State Statistics Service

2 Brazil, Russia, India and China

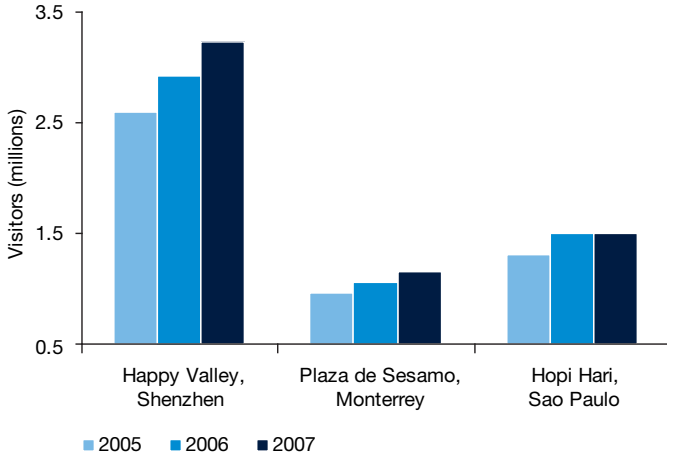
Attracting emerging market middle class families to outdoor entertainment parks

Some of the domestic leisure travel discussed above will be to purpose-built tourism sites within emerging markets. An attractive option for many families could be a regional outdoor entertainment park.

China is already the second-largest amusement park market in Asia Pacific, after Japan. It is also, along with India, a key growth market. Attendance growth is particularly strong in second-tier cities like Shenzhen, as shown in Chart 4 opposite, where incomes are rising quickly but entertainment options are fewer than in Beijing and Shanghai.

Latin America, on the other hand, is a more mature market for outdoor entertainment parks and attendance growth is less dynamic than in the booming Asian markets. However, both regions have a trend in common: the diffusion of income growth to the provinces, which is opening up opportunities for small amusement parks away from the major commercial centres that benefited from the first waves of economic development. An interesting example of this is the forecast growth in the number of middle and upper class households in Guangzhou vis-à-vis Beijing and Shanghai, as shown in Chart 5 opposite.

Chart 4: Amusement park attendance



Source: TEA, Amusement Business, Economics Research Associates

Replenishing the emerging markets shopper

One of the main visible signs of growing consumption capacity in emerging markets is the boom in retailing there. A natural complement to new malls is H&L content, ranging from fast food outlets and cafes to cinemas and bowling alleys.

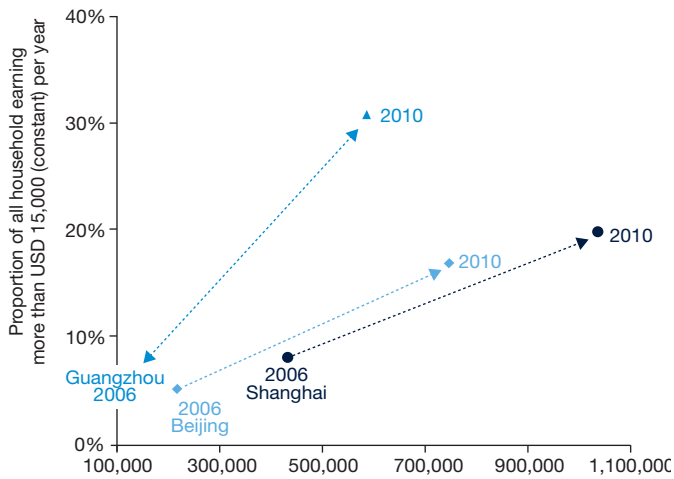
Branded fast food and drinks companies are leading the way, aggressively establishing their presence in even those less prominent emerging markets beyond the BRIC countries. Examples of H&L companies that are already winning market share in some of those markets are shown in Table 1 below.

Table 1: Presence in selected countries

	Costa Coffee	McDonald's	Pizza Hut	Starbucks
Argentina		●		●
Romania	●	●	●	●
Serbia	●	●	●	
Turkey		●	●	●

Source: Official websites of Costa Coffee, McDonald's, Pizza Hut and Starbucks as of 22 September 2008

Chart 5: Consumption capacity trends in China



Source: PricewaterhouseCoopers analysis

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The good news is that the retailing revolution in emerging markets is not expected to slow down over the medium term. This optimistic outlook is illustrated by Chart 6, which shows the forecast growth of retail space in Romania over the next few years.

Often the new malls are built to accommodate new customers in second and third-tier cities in countries well below the radar of those companies focussing only on the BRIC and comparably-sized markets. The middle class consumers in such locations should be seen as extremely attractive to branded fast food and drinks companies for two main reasons:

- they are financially capable and keen to be seen to be customers of branded fast food and drinks chains; and
- they are a largely captive market for the time being, as other entertainment options are relatively narrow.

Checking in

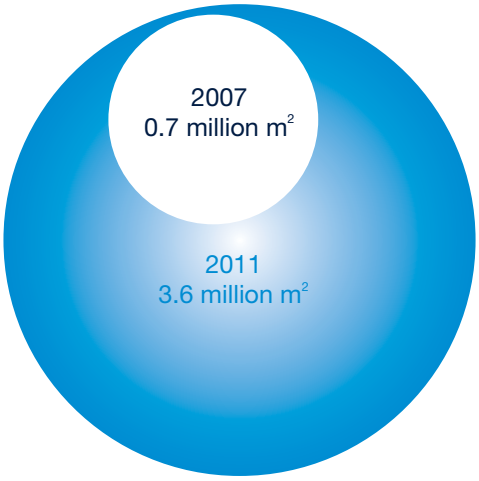
Consider the following facts about some of your current and potential markets:

- although it is not in a BRIC country, Istanbul has more middle class families than Shanghai;
- there are more than 100,000 Muscovite households with annual incomes over US$ 35,000; and
- between 2006 and 2010, the number of middle class households in Belgrade and Buenos Aires will have increased by 100 per cent and 50 per cent, respectively.

And now some questions related to those facts:

- Would you target the residents of Istanbul with the same enthusiasm as when marketing to the Shanghainese?
- How many more upper middle class Muscovites will be starting their day with a branded latte compared to today?
- Are you prepared for a flood of newly affluent entertainment-hungry middle class families in second-tier emerging market cities in the medium term?

Chart 6: Romanian total shopping mall retail space



Source: Research and Markets via newswire

The next steps

One way to apply our urban household income model methodology is to:

1. Identify priority markets

Are you focussing on Brazilian cities with populations over 250,000 residents or Chinese provincial capitals or second-tier cities in central Europe?

2. Determine relevant income brackets

Are you targeting households with incomes over US$ 2,000? or over US$ 20,000?

3. Quantify market segments

Our urban household income model could determine the size of your target market in your target cities.

4. Benchmark across markets

By modelling the market size of comparator cities, including those in which you already operate, the model could provide you with a set of benchmarks for the attractiveness of your target markets.

5. Forecast market dynamics

But what about the future? By utilising our extensive macroeconomic and H&L sectoral forecasting capabilities, we would also be able to estimate the size of your target market in the coming years.

Contacts

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For further hospitality & leisure research and news visit:
www.pwc.co.uk/hospitalitydirections

PricewaterhouseCoopers have produced the following report on emerging markets, please visit pwc.co.uk and search 'Consumer markets beyond Shanghai' to find out more.

www.pwc.co.uk/handl

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