



Ray Algar and Neil Burton look at how the emergence of 'cross shopping' and new super-budget clubs will affect the mid-market health club sector

Price war on the gym floor

So, are you a Waitrose or a Lidl shopper? A few years ago, you would have been one, neither, but certainly not both. How things change. Now, British consumers are running rings round marketers by being a Waitrose shopper on Monday and a Lidl customer on Wednesday. Marketing textbooks tell you this should not be happening. Prosperous consumers used to shop at premium quality outlets, while the financially-challenged ('hard-pressed' and 'of moderate means' to use the geo-demographics parlance) were reluctant guests at their local budget or value store. But not any more. And it is not just groceries where we now display extraordinarily promiscuous buying behaviour. Chief executives now fly easyJet; people mix and match a £500 Hugo Boss suit with a Debenhams shirt, and sales directors drive to a £26 per night Travelodge in their luxurious Mercedes. The figure below illustrates the pervasiveness of this trend (see illustration).

How can this be? What we bought, and from where, used to represent an accurate indicator of who we were, and where we were going, but this is no longer so. Precision-guided purchasing is the new game in town and if the best price for Illy espresso coffee is the local Netto store, then off to Netto we go. If we then pack those Netto items into a recycled Marks & Spencer carrier bag, this sends a message that we are smart and 'savvy' buyers, enjoying the power we now wield, as the internet peels away the layers of the once complex and mysterious world of consumer goods pricing.

So what has changed?

'Cross-shopping' appeals because consumers are fast realising that discount or low-cost operators are not peddling inferior goods. You can sleep well at a £15 Travelodge, easyJet is not selling seats on obsolete aircraft and Aldi's German dark chocolate at 89p is a BBC award-winning bargain. Consumers are increasingly compelled to look at low-cost providers for themselves, often with some dinner-party encouragement from friends, and they start

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thinking: 'why do I need to pay more?'

It is now a badge of honour to pay less; it demonstrates wisdom. Simultaneously, low-cost operators are furiously benchmarking their own products against branded lines to ensure that shoppers do not have to trade-off taste for a lower price. It is also not just groceries where they are infiltrating. Pick up a UBS phone from Lidl and make free internet calls for just £13, or a cordless high-power drill for £10 from Netto.

Consumers are also finding the internet a liberating and far more enjoyable experience to search, check and 'comparison shop' now that the UK is migrating from clunky dial-up to super-fast broadband connections. We are now approaching 12 million UK broadband connections and a quick flick of a mouse takes us to PriceRunner where we can interrogate the 'honesty' of a retailer's offering by effortlessly checking the price from at least 10 retailers along with genuine user reviews. Never has there been so much pricing transparency and consumers are enthusiastically embracing this newfound power.

Broken Promises

There is also a pervading undercurrent of mediocrity in many service offers. Paying a premium price for a cruise, hotel, restaurant meal or health club is no longer a guarantee of a memorable experience. Our service expectations are rising, while actual delivery is often no more than adequate. Be honest; when was the last time you were left surprised and impressed by a leisure experience? Consumers are

responding by demanding that service providers 'unbundle' the proposition into a menu of parts which are then 're-bundled', according to budget and preference. Mobile phone companies have begun this process. Why would you want a phone tariff that includes text messaging when you never text? It is a more compelling consumer proposition if individuals choose the service elements that have specific personal value. It is the antithesis of 'feature-creep', where service providers continually add more and more to their offer, both as a means of justifying a higher price and because they are unclear of what consumers really need. McFit, a German low-cost health club operator charges members 30p for a shower. Some may think that is daft. However, the reality is that many gym members do not like using club changing rooms, especially female users. So 'free showers' provides no added utility to these members. In fact, if we really think about it, all health clubs 'charge' members when they shower after a workout. McFit is just being more transparent in opening their costs to members and then letting them choose. 'There is no such thing as a free carrier bag' is how one low-cost retailer puts it.

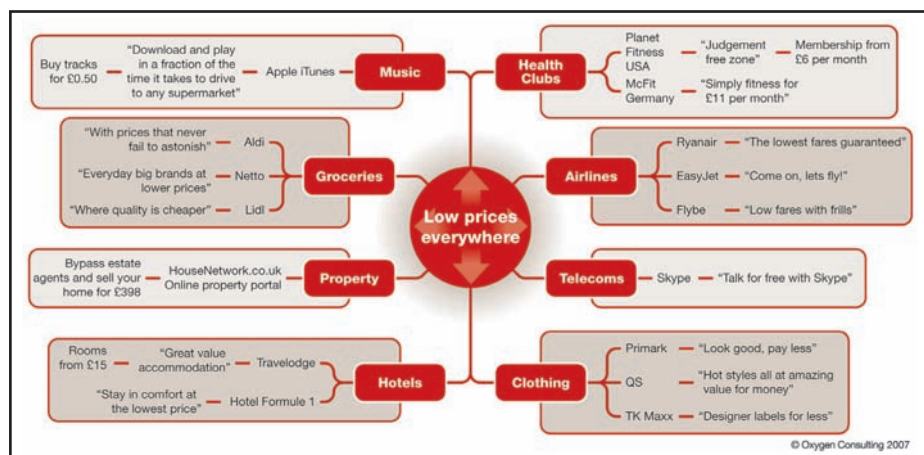
This way for self-service

You wait in a queue 10-people long to book next week's Pilates class. The receptionist dexterously handles telephone calls, while simultaneously logging class requests. After nine minutes, you are at the front of the line and desperately hoping that there is one place left, and no traffic warden waiting to welcome you back to your car. Fast-forward one week. 'Sorry, I have no record of you booking this class' is the response from reception. In the rush, it transpires that the receptionist booked the wrong day.

No wonder self-service is sweeping the country. It is compelling for many reasons; it offers convenience, accuracy, speed, satisfaction and privacy. Give consumers the right tools and they will do it themselves, and enjoy it. It is fun to check-in for a flight online, browse the aisles for a seat, cleverly avoiding seat 62c, which is uncomfortably near to the on-board toilet. Sometimes, staff add little or nothing to the customer experience, so low-cost providers are eliminating them. Consumers are familiar with self-service; UK consumers have been helping themselves to groceries since the 1950s and cash out of walls since 1967.

A low-cost operator is coming your way soon

Low-cost operators are not new. Southwest Airlines, the American pioneer of discount flights is now 36 years old and easyJet is heading for its 13th birthday. 'Making flying as affordable as a pair of jeans' was how it promoted its inaugural Luton to Edinburgh flight. So, are any sectors immune from



these ferociously efficient operators? Health clubs used to be, but not any more.

Welcome to McFit

Rainer Schaller, a charismatic entrepreneur has been quietly building Germany's largest (by membership size) club chain based on a 'low fees' strategy. McFit charge a flat fee of just £11.50 per month, which is 62% lower than the average German club membership rate. With 83 clubs and more than 520,000 members, this privately-owned company is consistently outperforming its rivals, measured by new club openings and membership growth. The product quite simply is a super-sized gym, a 27,000 sq ft (2,500 sq m) box filled to the brim with cardio-vascular and strength machines. Imagine the last time you toured a health club walking through reception, the café bar, past the fitness studio, onto the changing rooms and through to the pool. At McFit, the tour starts and stops with the gym - everything else has been stripped away.

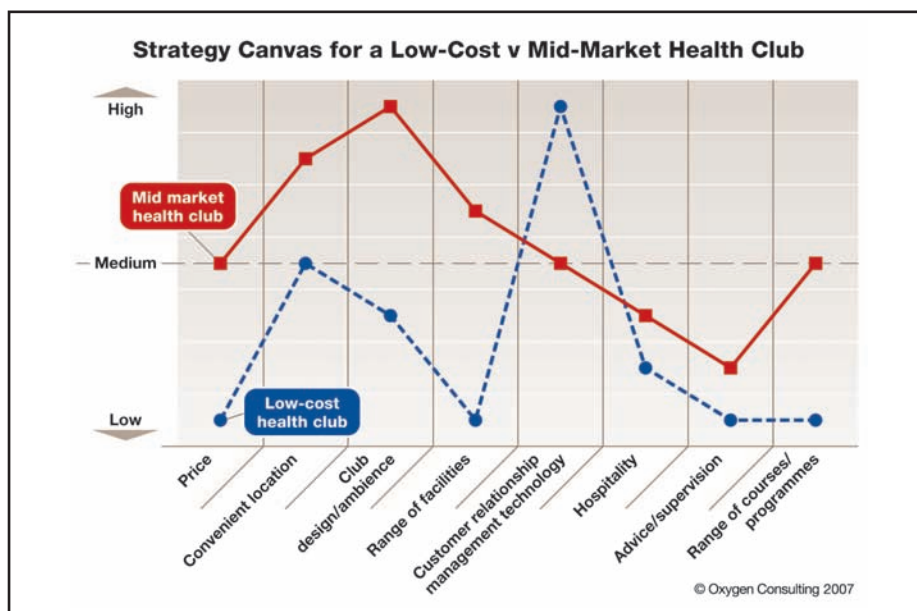
A new consumer proposition

The low-cost club undertakes a quest to eliminate all non-core elements such as swimming pools, crèche, café bar, health/beauty, retail and studios. Aligned to this is a philosophy of reduction, a zealous approach to scaling back to achieve harmony between efficiency and delivering the brand promise. 'Bring your own' should be printed on the reverse of a low-cost membership card to remind members that 'frills' are not part of the deal.

'Less is more' becomes the driving mantra. No need for reception desks here, because reception staff have been eliminated, along with gym instructors, sales staff and layers of management, replaced by a skeleton team of new hybrid staff, ready to turn their hand to an array of operational scenarios. Once stripped back, the emphasis turns to adding new competitive factors that disrupt the industry norm and create a compelling new consumer proposition. Self-service is applied everywhere, from joining/booking online, automatic card dispensers and programming via touch-screen terminals.

The reward is dramatically low membership fees. Fitspace, a UK-based low-cost gym operator, sells annual memberships for £11.60 per month, which is 72% lower than the national average price, and with no contract. You can join a Planet Fitness club in the United States for £5.50 per month. The trade-off, you may be thinking, is that low-cost clubs are situated on contaminated brownfield sites with panoramic views of the gas works, but they are not. Fitspace shares a prominent site in Bournemouth with Asda and Costa, and members benefit from free parking. Similarly, McFit target large towns and select sites on key arterial roads to attract commuters.

'Do less, but do it well' is another low-cost characteristic. Some new members turn up perhaps expecting home-grade exercise equipment thrown into a dirty room. Imagine their delight when they see wall-to-wall quality commercial grade equipment from Precor. Consequently, these clubs are attracting both experienced club users and first-timers. The former group are attracted by the price and the simplicity of the proposition. They say; 'I just want a clean, well-equipped gym'. The first-timers like the low joining barriers (small joining fee, low monthly price and short contract cancellation



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period). The result is that first-time club users represent up to 50% of some low-cost clubs.

Taking on the middle-market

These low-cost chains have the 'mid-market' health clubs in their sights. The competitive play used to be mid-market versus premium, with the former claiming they could offer 'more for less'. 'Affordable fitness' was the Fitness First slogan as they redefined the small club proposition. The problem is these 'affordable' mid-market clubs now look flabby compared to their super-lean low-cost upstarts. The following diagram illustrates how the low-cost operators are competing with their mid-market rivals.

For several years, the mid-market clubs have been living off well-designed clubs that really impress during the sales tour, but soon lose their charm as members settle into an exercise menu that rarely changes. What starts as a waiter-driven service quickly reverts to a help-yourself. As these clubs have quietly moved from 'advice included' to a paid-for personal training model, they have left the door gaping for low-cost operators to move in and take the high ground. 'Why pay for something you never get' is the low-cost operator's war-cry. So they remove the things that were not provided, or used, and offer low, low prices. Notice in the diagram that customer relationship management (CRM) technology is higher for the low-cost operator. This is because the completeness and integrity of customer data is an embedded characteristic of the low-cost business model. You cannot join a low-cost health club without providing accurate personal information, including an e-mail address. Even premium-priced health clubs cannot claim an e-mail address for every member. This means

that low-cost clubs can now deploy e-mail and SMS (text) to stay close to members, which represents a step-change in the typical member experience, all for £14 per month.

So, will low-cost club operators sweep across the UK as they are doing in Europe and the USA? Access to affordable property may hinder their challenge, but it has not hindered Lidl in building more than 400 UK stores, with 40 more planned for 2007. This is even with Competition Commission constraints that prevent store purchases from grocery multiples. Lack of human talent will not hinder growth, as these clubs are virtually unstaffed.

"Perhaps the biggest threat we face is that someone from outside our sector, with a huge war chest of cash and a proven customer-centric business model, will build 1,000 shiny new facilities and offers budget-busting membership deals" is the view of Fred Turok, chairman of LA Fitness.

So, how will the mid-market respond?

"By making sure the market knows what we offer, and what we do better", was how Rasmus Ingerslev, the chief executive of FitnessDK, Denmark's largest club chain, responded when we posed the question to him.

"Focusing on the elements where the budget clubs cannot and do not want to compete", suggests Herman Rutgers, the European director for the International Health, Racquet and Sportsclub Association. Fundamentally, the health club industry is entering a new chapter where the conversation is not about a race to the lowest price, but about clubs thinking long and hard about who they are, what they stand for, what they do really well, and their role in enriching members' lives.

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