

**A New Business Model
for
Timeshare Exchange**

A NEW BUSINESS MODEL FOR TIMESHARE EXCHANGE

WHITE PAPER

Executive Summary

The timeshare exchange business model is ready for a change.

The current model centralises the servicing of the exchange needs of timeshare owners within a duopoly that for the timeshare owner is in fact a monopoly.

Recently, many small, copycat exchange operations have sprung up offering cut-price exchanges with nothing really new in the mix.

New technologies and methods of communication now make it possible to give exchange an extreme make over by changing the business model and distribution channel and by decentralising the service.

This will **allow developers, resorts and management companies to service their clients and to fulfil their owners' exchange needs themselves.**

This is done by giving them access to a single integrated database and software application that runs over the Internet and is shared by all participants without them giving up control of their owners to a third party.

The benefits of this new business model are:

- Reduced costs for timeshare owners.

 - No more membership fees.

 - Exchange fees are "pay to use" and radically less than current fee levels.

- Increased income for Developers, Resorts and Management Companies.

 - This is achieved by sharing with them the income generated from exchange fee revenue in return for them providing the service to their timeshare owners.

- No loss of control or of independence by Developers, Resorts and Management Companies.

Background

The Timeshare segment of the Leisure Industry comprises of various players:

- Developers who build resort properties and create products to sell to the public.

- Marketers who market and sell these products for Developers, if the Developers do not sell for themselves.

Management Companies who manage the resort properties and who perform the “back office” functions of the resort and collect maintenance fees from timeshare owners in order to cover the costs of operating the resort.

Exchange Companies who provide flexibility to timeshare owners.

Trust Companies who secure the holiday property rights of timeshare owners.

Holiday Makers, whether owners of timeshare or renters of holiday properties or prospective owners or renters.

Software providers who provide the software for Developers, Marketers and Management Companies to run their businesses.

Clearly there are permutations of the above where the same entity may perform more than one of the business functions. In fact the trend is for companies to become more “vertically integrated” where they perform more and more of these functions themselves from start to finish.

This and other factors have resulted in the Exchange Companies becoming squeezed and they in turn are moving more vertically and intruding on the traditional business of the Developers. In particular they are buying up Development and Management Companies in order to gain control of the resorts as well and of the timeshare owners. A good strategy for them and perhaps the only one available.

By far the most dominant players are the Big Brand Developers and the Exchange Companies. The future looks to be one where a number of large, branded, vertically integrated companies, will dominate the industry, from development to product creation through marketing and sales to management. Each major player will own its own technology platform and software, creating barriers between themselves and the efficient use of the accommodation. Their size and branding will also create barriers to entry for new participants.

Finally the Consumers will be squeezed for more and more of their “Leisure Dollar” and prices will rise.

And the single site or smaller Developers will be put out of business.

Recent Developments

The traditional form of timeshare entails someone owning the right to occupy a specific week of time in a specific resort in a specific condominium unit.

This means holidaying at the same resort in the same unit at the same time of year, year after year.

The Exchange Companies provide flexibility to this inflexible product by offering to exchange or swap timeshare owners from one condominium into another of a similar size and quality and in the same season. A kind of barter system that operates on a “like for like” basis.

In more recent times Points Systems have changed the barter system of flexibility to a currency system where each week of timeshare accommodation is valued in points based on the size, season, quality, demand and various other factors. Points are then given in exchange for timeshare weeks being deposited with a Points System and the points are used as a form of holiday “currency” to “pay” for the accommodation taken in turn out of the Points System pool of accommodation.

Industry Cost Structure

The ownership of timeshare entails two costs, the cost of acquisition and the ongoing cost of ownership.

The cost of acquisition is a once off, upfront charge that can be financed, allowing for affordable monthly payments over a number of years. Much like the way automobiles are purchased.

The ongoing cost of ownership is the equivalent of the running and maintenance costs of an automobile.

These costs can be broken down into two components:

The annual maintenance fee paid to the Management Company that is required to service and maintain the resort property.

The annual membership and exchange fees paid to the Exchange Companies in order to provide flexibility to the conventional timeshare product.

The annual maintenance fees cover all the operating costs of running the resort including the cost of providing reception, housekeeping and laundry services as well as all maintenance and refurbishment costs.

The annual membership fees and exchange fees paid to the Exchange Companies are for the provision of flexibility through exchange.

In comparative terms, of every £100 spent on the ongoing cost of ownership perhaps £70 is spent on maintenance fees and £30 is spent on providing flexibility.

While there is little “fat” in the first cost, there is room to massively decrease this second cost.

Consider this:

Management Companies earn a percentage of the annual maintenance fees to cover the cost of running their businesses. This fee is normally between 10% and 20%. Thus the Management Companies must provide their services on an income of just £25 to £50 per owner while the Exchange Companies do a lot less and earn a lot more, in fact some £150 per owner compared to the maximum of £50 per owner earned by the Management Company.

So, while the Exchange Companies earn some £30 of every £100 spent on the ongoing cost of ownership simply for providing flexibility, Management Companies earn just £7 to £14 of every £100!

It is this exchange fee income that is open to attack, offering savings in the ongoing cost of ownership to Consumers as well a new business opportunity for Developers, Resorts and Management Companies.

The Size of the Market

There are perhaps some 4 mil timeshare owners worldwide, the majority in the USA.

In Europe there are in excess of 1.2 mil timeshare owners. The growth in Europe is unfortunately not as dynamic as elsewhere.

The majority of these timeshare owners were affiliated to one of two major Exchange Companies when they purchased their timeshare. A large percentage have allowed their membership of their Exchange Company to lapse.

The average length of membership of a timeshare owner with an Exchange Company is perhaps 3½ years. The major reason for the drop off is the high cost of obtaining flexibility.

The Exchange Companies operate a duopoly, but for the Consumer it is a monopoly, as they have no choice. They have to use the one their resort is affiliated to for no other reason than that the Exchange Companies do not compete with each other in the same resort for the timeshare owners. They compete for Developers and then the owners become captive of the Exchange Company based on the Developer or Resort's affiliation.

The Exchange Companies earn in real terms in the region of £150 a year from each member out of membership and exchange fees.

The Opportunity

The disproportionately high percentage of the ongoing cost of ownership that is spent by owners on obtaining flexibility makes this an obvious area to investigate for possible cost savings by using alternative business solutions and a new business model.

There is a massive opportunity to cut the ongoing cost of ownership for timeshare owners AND to offer a new business opportunity to Developer's, Resorts and Management Companies by allowing them to provide the exchange service to their owners, themselves.

Specifically:

Owners. Giving them Value for Money PLUS service.

It is possible to offer savings of some 67% on the current cost of obtaining flexibility. In addition there is a chance to remove the

need to pay annual membership fees. Owners will only have to pay a transaction fee if and when they transact successfully.

The cost of flexibility can be cut from approximately £150 (for membership and exchange) to £50 for a transaction fee payable ONLY if there is a successful exchange transaction. Timeshare exchange would finally become a "Pay to Stay" system.

Developers, Resorts and Management Companies. Giving them back their businesses.

It will be possible to offer these entities the chance and ability to provide the exchange service to their timeshare owners themselves and to earn a share of the money that is currently going to the Exchange Companies. In real terms, Management Companies currently earn £10 to £20 of every £100 spent on maintenance fees. It will be possible to give these companies an additional £24 for each deposit/exchange that they facilitate.

They will earn this share for simply providing their owners with a reservation and exchange service. Their marginal cost increase to do this will be nominal, thus most of this additional income will go straight to their bottom line.

In addition timeshare owners can be offered travel arrangements and the attendant travel commissions will be earned by the Developers, Resorts and Management Companies.

How Can This Be Done?

There is a lack of sophisticated software in the timeshare industry. Specifically there is no software that is web enabled and capable of linking disparate Developers, Resorts and Management Companies together allowing for the pooling of accommodation and thus enabling exchanges to take place by the Developers, Resorts and Management Companies servicing their timeshare owners themselves.

Also the current software is in many cases deficient in logic and capability.

The Merlin suite of timeshare software has been deployed over the Internet for Developers, Resorts and Management Companies to access by using their own computers connected to the Internet. No sophisticated client side software, LANs and Servers are necessary.

Developers, Resorts and Management Companies are able to run their entire Front and Back Office operations on this software. Developers/Marketers are also able to use the software to run their Marketing and Sales operations and to integrate with the Back Office functions without the need to recapture data or to be in the same physical location as their Resort or Management Company or even on the same LAN.

Finally, by pooling information and making this available to other participants over the Internet, independent Developers, Resorts and Management Companies can view the availability of deposited weeks in all participating

Resorts and effect exchanges on behalf of their timeshare owners, themselves. In addition, a generic B2C web site will enable their timeshare owners to make deposits and effect exchanges themselves.

All data is stored on web- and database servers in a secure data centre.

The exchange service that is offered is Points based.

The Financial Model

Developers, Resorts and Management Companies will receive $\frac{1}{4}$ of the service fee for each in bound exchange that they accept on behalf of other participating Resorts and $\frac{1}{4}$ of the service fee for each outbound exchange that they make on behalf of their timeshare owners.

Are There Precedents?

There are similar business models in other industries. Healtheon/WebMD and salesforce.com are two examples. Both are extremely successful. The providing of software services over the Internet with centralised data storage and decentralised service centres is fast becoming an established business model. This business model is termed "Application Service Provider" and in the words of salesforce.com it means "the end of software, as we know it". In the leisure industry it has the added benefit of "giving back their businesses" to Developers, Resorts and Management Companies. For consumers it means cost savings, more choice and improved service and efficiency.

What About The Brands?

It is feasible that in time, some of the Brands will want to use the software simply to avoid having to develop the technology for themselves. Certainly those that have cross utilisation agreement with other Resorts and Brands will be able to use the software to manage these agreements and the movement of stock between them.

What About The Exchange Companies?

The Exchange Companies are the ones that will probably be most affected by this change in the distribution channel as it affects their business model directly. They could develop just such a technology platform but it is doubtful if they can offer the massive savings to the owners and also pass the business opportunity on to the Developers, Resorts and Management Companies without destroying their business model and thus their businesses in the process.