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Technology, Media & Telecommunications

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# TMT Trends: Predictions, 2005

A focus on the media sector

The background of the entire page is a photograph of three black microphones on silver stands, arranged in a row from left to right. The microphones are angled upwards and to the right. The background is a gradient of blue, darker at the top and lighter at the bottom.

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## Foreword

Welcome to the 2005 edition of Deloitte Touche Tohmatsu's Technology, Media and Telecommunications (TMT) predictions for the global media and entertainment sector.

2005 will see the media find new stability in the digital age. The music industry will be the first to emerge as a master of the internet. Legal downloading will flourish, and a concerted, coordinated and global effort to crackdown on pirates will see illegal activity take a significant blow. Convergence will also generate both headlines and profits for the first time in 2005. Most notable will be the convergence of digital games and movies. Epic games will be developed in parallel with the production of blockbuster movies, with incredible effect. At the same time, consumers' appetite for content in all of its forms will give rise to new platforms for advertisers. But 2005 will serve to demonstrate all too well that it is quality – not quantity – that makes money.

These predictions are the result of comprehensive research throughout 2004, the principal elements of which include:

- input from Deloitte Touche Tohmatsu's member firms' 5,000 Technology, Media and Telecommunications partners, directors and senior managers around the world;
- conversations with Deloitte Touche Tohmatsu's member firms' clients;
- dialogue with leading industry and financial analysts.

Accompanying each of these ten predictions is Deloitte's bottom line: the suggestions to the sector for exploiting each key development that the coming year holds. We trust that this guidance makes this report a valuable reference for your company.

On behalf of Deloitte Touche Tohmatsu and the TMT practices of its member firms, may I take this opportunity to wish you all the best for 2005.

*Igal Brightman*

**Igal Brightman**

Global Managing Partner  
Technology, Media and Telecommunications



## Summary

The long-standing business model for broadcast television – the network model – will, in developed countries, steadily be replaced by a complex and diverse media market with even greater opportunities. Rapid proliferation of channels and media formats has made it increasingly difficult to reach “the masses” through a single broadcast, undermining the power of traditional networks and reducing their value to advertisers. Yet the underlying driver of this **disaggregation** is the public’s insatiable appetite for content and choice, meaning media companies will have more opportunities in the future – not less. New devices and media will flourish, along with new forms of advertising, including embedded advertisements in video games, software, web browsers and even mobile phones.

Convergence will remain a hot topic in 2005, but will provide strong returns for only a handful of media companies. Those that succeed will base their offerings on market needs, picking and choosing their opportunities carefully. Collaboration between game developers and movie studios will be one of the most compelling convergence stories of the year – creating value and extending the life-cycle for both products. Music downloading will gain respectability, with rapid growth in legal downloads and online music sites. At the same time, media and entertainment companies will join forces, working with police in a sustained and successful effort to crack down on piracy.

Companies will spend heavily trying to convince consumers to watch television on mobile phones and other mobile devices. But what consumers really want is simple content such as ringtones, screensavers, and wallpaper that allows them to personalize their phones – a market that is already worth billions of dollars.

Newspaper publishers will see modest growth from their on-line operations, while magazine publishers will enjoy greater success. Niche journals, in particular, will increasingly be offered in electronic form – providing instantaneous global distribution at massively reduced cost. Traditional media outlets will lose their monopoly on content, as more and more people express their opinions on the internet through **blogs** (web logs) and **wikis** (editable web pages). While these sources will not directly threaten traditional media revenue, they will compete for eyeballs and influence, which are the media industry’s underlying currency.

2005 will be a pivotal year for digital terrestrial television (DTTV). The disruptive force of DTTV will be felt on two levels: first, as customers increasingly choose terrestrial broadcasts – rather than cable – for digital TV; and second, as wireless operators experiment with DTTV networks as a way to expand their revenue base.



# Music downloading gets respectable

2005 will see rapid growth in legal music downloads over the internet. Illegal downloading will most likely still dominate, but legal sites will significantly increase their share. Overall, the music industry will finally start to embrace, rather than reject, this new distribution channel.

Growth of legal downloads will be fueled most heavily by the growing quality of online music stores, some of which will outperform top retail stores with respect to choice, price, ease-of-use and speed of purchase. Other factors will include a sharp increase in the installed base of digital music players, the inclusion of CD burners as a standard feature in laptop and desktop computers, and the exceptional quality of legal downloads.

By year-end, the growth of illegal downloading will start to slow, with occasional but high-profile litigation scaring off many casual pirates. Nonetheless, illegal downloads will continue to cost the music industry billions of dollars in lost revenue.

**“Growth of legal downloads will be fueled most heavily by the growing quality of online music stores...”**

## Deloitte Bottom Line

**Embracing the enemy.** The music industry will be healthier but still fragile in 2005. Recovery will be driven at least in part by a shift in attitude, with the industry finally embracing the internet – rather than fighting it.

The internet is more than just an alternative distribution channel for traditional products such as singles and albums. It also provides virtually limitless potential for additional revenue from new forms of content – from ring tones and remixes to live recordings, concert videos and merchandising.

Free or subsidized downloads could even be used as digital flyers to promote high-margin products such as concert tickets. It may seem paradoxical that customers will go out of their way to download songs for free, while willingly paying \$100 for a concert ticket and souvenir T-shirt. But it's a paradox worth exploiting, if that is where the perceived value lies. To maximize these cross-selling opportunities, tour promoters and band managers should actively cooperate with music labels, which have traditionally not been involved in live music.



## The mass audience becomes a mass of audiences

In 2005, the long-standing business model for broadcast television – the network model – is likely to be increasingly replaced by a more segmented, customer-centric approach. The traditional network model is based on the idea of one-to-many broadcasting, with revenue primarily derived from advertising. At its heart is the notion of mass-market reach – the ability to deliver programming and advertising messages to a substantial portion of the population (nationally, or even internationally) through a single broadcast.

In recent years, the number of media formats and channels has exploded, changing the way people consume content, and slowly but steadily dividing the mass market into many pieces.

While audiences are getting smaller, their fervor and dedication are rising. Many viewers are willing to consume content – and pay for it – multiple times, in a variety of formats. Thus a television program is no longer a one-time event, funded by one-time advertising revenue, but the beginning of an extended revenue stream that includes subscriptions, DVDs, toys, apparel, video games, product placement and more.

### Deloitte Bottom Line

**Feeding the content hungry.** The traditional network model has been under threat for some time, and ironically, one of the main reasons for this is the public's insatiable demand for content. People want more programs and more choices – supplied in a variety of formats (both digital and physical) so they can consume it whenever and wherever they want. That appetite for content has fueled the success of DVDs and portable music players, and is driving demand for emerging products such as personal video recorders, portable video players, and video-on-demand. The market may be changing and diversifying, but it's also growing.

**Finding a new approach.** Television companies must develop new strategies that extend their reach into new media channels and products, from screen savers for mobile phones to electronic games and theme parks. They should build portfolios of services around their content to stimulate new forms of consumption. And they must assimilate new skills – particularly product development and service management – that will help them define and capitalize on changing consumption patterns.

# Advertising gets embedded

Audience disaggregation will force advertisers to find new platforms for their campaigns. In the opinion of the Deloitte TMT member firm network, one of the principal emerging platforms for 2005 will be embedded advertising.

The digital equivalent of product placement, embedded advertising will initially take the form of hypertext links in web-based content. As the user's mouse pointer passes over relevant keywords or objects, small pop-ups will appear with a web link to the advertised product. During the course of the year, more advanced forms of embedded advertisement will appear in video games, software (particularly freeware), web browsers and even active desktops on mobile phones. Embedded ads will increasingly be integrated with the primary content – in software, for example, they will appear as toolbar buttons; in games, they will be part of the gameplay itself.

Embedded advertisement promises to be more subtle and sophisticated than banner advertisements and pop-ups. Indeed, they will need to be for consumers to accept them.

Embedded ads will be driven by keywords and content, and will be very precisely targeted as advertisers learn more about each group of consumers. The ads will also be dynamic, updated via an internet connection based on time of day and user activity. Although embedded advertising will still be in its infancy during 2005, its long term impact is likely to be substantial – potentially proving much more effective and measurable than mass campaigns.

**Getting closer to customers.** Embedded advertising is an exciting new concept, both for agencies and their clients. It has the potential to stimulate the advertising business, offering new opportunities for advertisers to communicate directly with the target audience, in a manner that is less intrusive and annoying than many current techniques. Yet success will require a new and relatively complex skill set. Knowing where to reach an audience will not be enough. Agencies must also know when the audience is available, what its members are likely to be doing, and most important, how to capture their interest within that context. Advertisers will also need to stay abreast of technological progress, understanding how it constrains their current advertising approach, and how it might enable new ones.

## Convergence pays off – but only for a few

Convergence will certainly remain a hotly debated topic; however, it is only likely to deliver strong returns for a handful of media companies. Many attempts at convergence will fail, appealing more to engineers and technology enthusiasts than to mainstream consumers.

Businesses that focus on customer needs, and take a highly selective approach to convergence, are most likely to succeed. Convergence of entertainment services on the internet will continue to grow, with initial successes in music downloads being followed by similar efforts for music videos and where bandwidth permits, television programmes and movies. Carefully targeted video-on-demand services over DSL will also begin to stimulate more customer interest, as operators focus on leveraging the value of the **back-catalog**, delivering set-top boxes that allow customers to view programs on their televisions, not just their PCs.

### Deloitte Bottom Line

**Converging on customers.** Successful convergence has everything to do with understanding customer needs. Convergence holds substantial potential, but only when it is relevant to the end users. Customers never demand convergence for its own sake, so in 2005 media companies must try harder to understand what customers want – and are willing to pay for – applying convergence **only** when it satisfies customer needs.

**Converging on media companies.** To date, the biggest push for convergence has come from telecom operators, internet service providers and others, with media companies following their tradition of staying at arms length from the customer. But if they want to win in the convergence game, media companies will need to take the lead – defining and understanding customer needs, shaping the value chain, and staking out the high ground for themselves.

## Games and movies: a blockbuster combination

Growing convergence between game developers and movie studios look set to provide one of the most exciting and compelling story lines in 2005. Blockbuster movies will increasingly be developed in tandem with best-selling games, using the same characters, the same narrative threads, the same look and feel, and in some cases, even the same voice talent (game narration is quickly becoming a standard part of movie star contracts).

The symbiotic relationship between games and movies – and the growing capabilities of videogame consoles and PCs, most of which can now play DVDs – is likely to generate a significant convergence premium, in a form of higher: box office receipts, sales of electronic games, and on-line games activity.

### Deloitte Bottom Line

**Growing legs.** 2005 is likely to see a surge of cooperation between movie studios and electronic game developers. Movie studios should use tied-in electronic games to extend the lifecycle of movie content beyond the box office run, beyond the DVD release, right through to the launch of the sequel. Electronic games developers should factor in a continuous stream of upgrades – including new chapters and new characters – to maximise the life time of the movie. Conversely, electronic games developers should use movies to generate massive publicity for their associated games, across a range of platforms, hence lowering the risk.

## Mixed returns from internet publishing

Many newspaper publishers will probably generate only modestly rising returns from their on-line activities. Newspaper web sites often lack a clear business strategy, and their purpose and value is not always readily apparent to publishers, or even customers. On the other hand, counter to earlier fears the web has not significantly undercut physical circulation, and the public's overall appetite for news continues to show impressive growth.

Periodical publishers are already enjoying significant success on-line – particularly niche journals. In 2005, niche journals are likely to expand their offer of subscription-based electronic versions of their print publications, providing instantaneous global readership and massively reduced distribution costs. In many cases, complete PDF downloads will be available, enabling customers to print and store each issue. Publishers will also include archive and search capabilities, maximizing the value of their existing content.



### Deloitte Bottom Line

As with the music industry, the internet holds strong appeal for publishers to reduce distribution costs and broaden their reach. In 2005, more and more publishers will learn to better harness that power.

**Getting ahead of the competition.** Publishers must move aggressively to leverage the internet before someone else beats them to it, as happened in the music industry. The good news is consumers don't seem inclined to abandon physical media in favor of electronic alternatives – at least not to the extent they did with digital music – and generally seem willing to pay for high-quality, exclusive content. Increased broadband penetration and bandwidth will make the online product even more appealing – enabling new levels of creativity, multimedia, and interaction.

Publishers' online strategies should focus on expanding the breadth and depth of services offered, using the immediacy and reach of the internet to enhance the value of their content, and using its capacity for personalization to deliver custom products and services. Newspaper publishers should also consider how to re-format their electronic content in other ways – for instance, as DVD-based encyclopaedias.

**Using brand to attract a global audience.** The global appetite for news is growing strongly, creating a real opportunity for newspapers to make sustainable and profitable use of the internet. Customers generally buy news based on brand, and there is already evidence that strong brands can attract global online audiences and revenue – selling digital editions, PDF downloads and highly focused advertising space. The extent to which newspaper publishers can carefully flex their existing brand muscle may ultimately determine who wins and who loses in the online world.

**In 2005, niche journals will increasingly offer subscription-based electronic versions of their print publications, providing instantaneous global readership and massively reduced distribution costs.**

## Content for the masses, by the masses

Movie studios, publishers, radio stations, and television networks are no longer the only sources of content. Thanks to the internet, individuals now have the power to publish their own content to the world – and are doing so in record numbers through the use of **blogs** (web logs) and **wikis** (editable web pages).

**Blogs** are personal web journals typically comprised of user-authored postings, photos and links. Most blogs serve as a means for individuals to express their personal views, and in many cases, for readers to post remarks and comments. **Wikis** are editable web pages that encourage all users to add or edit entries, providing an open forum for discussion, information sharing and self-expression.

Both mechanisms have been gaining popularity, with blogs in particular becoming extremely popular and respected. In 2004, political bloggers in the United States were allowed into the Democratic and Republican conventions, providing a personal perspective on the presidential race. The wireless industry also got into the game last year, launching software that allows users to upload text and photos from a mobile phone to a personal web page.

### Deloitte Bottom Line

**Small talk. Big money.** A key question for 2005 will be how to make money from the public's growing desire for self-expression and web writing. Some bloggers, for example, already make a profit selling advertising space on their sites. Although such activities are unlikely to cause a noticeable drop in revenue for traditional media companies, they will increasingly compete for the public's time and attention – creating a potential threat, as well as a possible market opportunity.

User-generated content is a cultural phenomenon and its importance should not be underestimated. Media companies must seek to understand what keeps millions of internet users glued to their computer screens, applying those insights to their own objectives.



## Digital terrestrial TV takes off

Digital terrestrial television (DTTV) is currently being launched in a number of countries, and 2005 will see a substantial increase in the number and size of deployments. Several factors are driving the expansion:

- Governments increasingly view DTTV as a powerful, low-cost broadcast technology that can quickly free up existing TV frequencies for resale to telecom operators and other potential users.
- Terrestrial broadcasters are seriously considering DTTV as a way to fend off competition from digital satellite and cable services, as well as from other digital video technologies such as personal video recorders (PVRs) and video-on-demand (VoD).
- Hardware manufacturers are eager to use DTTV as another opportunity to sell set-top boxes and high definition television sets.

Consumers are also excited about DTTV, seeing it as an inexpensive way to get more channels. Digital terrestrial broadcasting – known as DVB (digital video broadcasting) in Europe and ATSC (Advanced Television Systems Committee) in the Americas and elsewhere – is becoming extremely competitive. Decoders are now available for less than \$100, and in many cases broadcasters subsidize the cost to zero.

### Deloitte Bottom Line

DTTV has the potential to be a highly disruptive technology – giving terrestrial broadcasters a digital, interactive medium that allows them to compete effectively with cable and satellite. Cable operators are particularly vulnerable, due to the high cost of laying cable. They must carefully assess the threat posed by DTTV, and act quickly to protect themselves from the high probability of a competitive onslaught.

DTTV's greatest disruptive impact could come from outside the media world. Several fixed and mobile telecom operators are testing DTTV technology as a way to get more bandwidth, as well as the capacity to deliver entertainment services along with their standard telecom offerings. Although they are unlikely to succeed in the long-term, their efforts may still disrupt the market – confusing consumers, artificially increasing competition, and eroding potential revenue. All broadcasters – even those not planning to deploy DTTV – must carefully consider the impact of telecom players in their market. They have deep pockets and long-standing customer relationships, making for a tough battle ahead.

# Knock-offs get knocked out



In 2005, the media industry will launch its most sustained and successful attack so far on piracy and copyright theft. Media and entertainment companies will coordinate their efforts, working closely with police to quickly and systematically crack down on violators around the world.

The industry already loses billions of dollars each year to piracy and copyright theft – including illegal copies and downloads of DVDs, CDs, and games – and with DVD burners and ripping software becoming increasingly common, the threat is quickly spreading beyond the world of organized crime and into the home.

Media and entertainment companies will focus their efforts on a handful of large pirate businesses that are flooding the market with counterfeit goods. There are likely to be a number of high-profile lawsuits, along with some long jail terms.

## Deloitte Bottom Line

**Discouraging piracy.** Copyright theft has been a part of the media and entertainment business since recording and reproduction technology were first introduced – and will probably never go away. Yet its impact can be significantly reduced. The media industry must start to educate its customers, not just frighten them with litigation. Too many people – particularly teenagers – see copyright theft as a victimless crime. They need to understand that in addition to being illegal, piracy also undermines the industry’s health and well-being – reducing its ability to provide appealing content in the future, and lining the pockets of organized criminals.

More important, media and entertainment companies must learn from the painful lessons of the music industry, where online music consumers resorted to theft because no legal downloading alternatives were available. Movie studios face that same problem today, and must find reasonable and controlled ways to satisfy the public’s insatiable appetite for content. One option is to offer a variety of quality tiers, including a lower-resolution product for those customers that are unwilling or unable to pay for a full-price DVD, and a high-definition, premium-priced product for the most discriminating and affluent consumers. Breaking away from the one-size-fits-all approach could significantly reduce the temptation of piracy.

## Simple phone content sells best

By the end of 2005, there will likely be two billion mobile subscriptions. That represents a huge opportunity for content producers – particularly as improvements in network speed, processing power and screen quality combine to make the consumption of content more appealing.

Despite the vast potential, many experiments with mobile phone content are fated to fail. Many companies will ignore the way people actually use mobile phones – including the social context – and will aggressively push services that exceed the device's practical limitations. For example, a number of companies have grand schemes to offer television programming on mobile phones – yet consumers have expressed little or no interest in watching overpriced television programs on a tiny screen.

By contrast, ring tones, screensavers, wallpaper and other disposable content already represent a multi-billion dollar growth industry. Growing numbers of consumers – particularly young consumers – will pay for content that personalizes their mobile devices. Although it may seem counter-intuitive, consumers often place more value on a song-based ring tone than on the song itself.

### Deloitte Bottom Line

**Keep it simple.** The mobile phone is, **de facto** the most widely adopted networked device in the world, and it's only a matter of time before consumers start to download content on a truly massive scale. Yet experience to date suggests simplicity is what sells best – small, relevant packages of content that can be used to customize the device. Media and entertainment companies, as well as mobile network operators, should focus on this market, instead of trying to force-fit more complex content into the phone. Mobile phones are immensely powerful, but they are not a panacea. Recognizing the device's limitations, and the context in which it is used, will likely help all concerned make the most of its incredible potential.

**Improvements in network speed, processing power and screen quality will combine to make the consumption of content more appealing.**



## About TMT

The Deloitte Touche Tohmatsu Global Technology, Media & Telecommunications (TMT) Industry Group consists of the TMT practices organized in the various member firms of Deloitte Touche Tohmatsu and includes more than 5,000 partners, directors and senior managers supported by thousands of other professionals dedicated to helping clients evaluate complex issues, develop fresh approaches to problems and implement practical solutions. There are dedicated TMT member firm practices in 45 countries and centers of excellence in the Americas, EMEA and Asia Pacific. Deloitte Touche Tohmatsu's member firms serve nearly 80 percent of the TMT companies in the Fortune 1,000. Clients of Deloitte's member firms' global TMT practices include some of the world's top software companies, computer manufacturers, wireless operators, satellite broadcasters, advertising agencies and semiconductor foundries – as well as leaders in publishing, telecommunications and peripheral equipment manufacturing.

Deloitte's member firms work across all service lines: assurance and audit; risk consulting; tax advisory; business and technology consulting; financial advisory and corporate finance; mergers and acquisitions and Sarbanes Oxley compliance. Deloitte's member firm practitioners invest vigorously in understanding and promoting the TMT sector, generating world class insight via Deloitte Research; identifying upcoming industry leaders through the Technology Fast 500 programs and polling leadership opinions via the Deloitte Touche Tohmatsu Global CEO survey.

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This report has been compiled by Paul Lee, Director, Technology, Media and Telecommunications at Deloitte Research.

## Recent TMT thought leadership

"Getting off the Ground: why the move to VoIP is a decision for all CXOs"

"Changing China: Will China's technology standards reshape your industry?"

"Moore's Law and electronic games: How technology advances will take electronic games everywhere"

"2004 TMT Trends Annual Report: Igniting Innovation"

"Cautious optimism: a global survey of CEOs in the Deloitte Technology Fast 500"

"Convergence is dead: long live convergence"

"Making the off-shore call: The road map for communications operators"

"Wire-line predictions 2004"

"Mobile and Wireless predictions, 2004"

# Contacts at Deloitte Touche Tohmatsu and its member firms

**Igal Brightman**  
Israel  
Global Managing Partner,  
Technology, Media & Telecommunications  
+972 3 608 55 00  
ibrighman@deloitte.co.il

## Americas

**Alberto Lopez Carnabucci**  
Argentina  
+54 11 4320 2700  
alopezcarnabucci@deloitte.com

**Marco Antonio Brandao Simurro**  
Brazil  
+55 11 5185 2232  
mbrandao@deloitte.com.br

**Garry Foster**  
Canada  
+1 416 601 6173  
gafoster@deloitte.ca

**Arturo Platt**  
Chile  
+56 2 2703 361  
aplatt@deloitte.com

**Manuel Lópezlage**  
Colombia  
+ 57 2 8837027 x3003  
mlopezlage@deloitte.com

**Francisco Silva**  
Mexico  
+ 52 55 5080 6310  
fsilva@dtm.com

**Manuel Cámbara Moreno**  
Peru  
+51 1 211 8533  
mcambaramoreno@deloitte.com

**Phillip Asmundson**  
USA  
+1 203 708 4860  
pasmundson@deloitte.com

## Europe/Middle East/Africa

**Andre Claes**  
Belgium  
+32 2 6 00 6670  
aclaes@deloitte.com

**Jiri Polak**  
Central Europe  
+420 22 489 58 46  
jpolak@deloitteCE.com

**Gennady Kamyshnikov**  
CIS & Russia  
+7 095 787 0600  
gkamyshnikov@deloitte.ru

**Kim Gerner**  
Denmark  
+45 33 76 33 33  
kgerner@deloitte.dk

**Jari Matula**  
Finland  
+358 40 740 3530  
jmatula@deloitte.com

**Eric Morgain**  
France  
+33 1 55612798  
emorgain@deloitte.fr

**Andreas Gentner**  
Germany  
+49 711 16554 7302  
agentner@deloitte.de

**Dieter Schlereth**  
Germany  
+49 211 8772 2638  
dschlereth@deloitte.de

**Moe Cohen**  
Gibraltar  
+350 48281  
moecohen@deloitte.gi

**Tom Cassin**  
Ireland  
+353 1 417 2210  
tcassin@deloitte.ie

**Ilan Birnfeld**  
Israel  
+972 3 608 5514  
ibirnfeld@deloitte.co.il

**Alberto Donato**  
Italy  
+39 064 780 5595  
adonato@deloitte.it

**Dan Arendt**  
Luxembourg  
+352 451 452621  
darendt@deloitte.lu

**Steve Cachia**  
Malta  
+356 2134 5000  
scachia@deloitte.com.mt

**Omar Fahoum**  
Middle East  
Tel +97317214490  
ofahoum@deloitte.com

**Jan Bune**  
Netherlands  
+31 20 582 4188  
jbune@deloitte.nl

**Jorn Borchgrevink**  
Norway  
+47 2327 9210  
jborchgrevink@deloitte.no

**Carlos Freire**  
Portugal  
+351 21 381 6029  
cfreire@deloitte.pt

**Danie Crowther**  
South Africa  
+27 12 482 0141  
daniecrowther@deloitte.co.za

**Eduardo Sanz**  
Spain  
+34 91 514 5060  
edsanz@deloitte.es

**Luis Jimenez Guerrero**  
Spain  
+34 91 514 5067  
luisjimenez@deloitte.es

**Tommy Maartensson**  
Sweden  
+46 8 506 711 30  
tommy.maartensson@deloitte.se

**Jolyon Barker**  
United Kingdom  
+44 20 7007 1818  
jrbarker@deloitte.co.uk

## Asia Pacific

**Dean Kingsley**  
Australia  
+61 2 9322 7415  
dkingsley@deloitte.com.au

**Parag Saigaonkar**  
China  
+86 10 8518 7800  
psaigaonkar@deloitte.com

**N. Venkatram**  
India  
+91 22 56679125  
nvenkatram@deloitte.com

**Yoshitaka Asaeda**  
Japan  
+81 3 6213 3488  
yoshitaka.asaeda@tohmatsu.co.jp

**Alan Dent**  
New Zealand  
+64 4 495 3913  
adent@deloitte.co.nz

**Shariq Barmaky**  
Singapore  
+65 6530 5508  
shbarmaky@deloitte.com

**Hyun Chul Jun**  
South Korea  
+82 2 6676 1307  
hjunc@deloitte.com

**Clark C. Chen**  
Taiwan  
+886 2 25459988 x3065  
clarkcchen@deloitte.com.tw

### For more information, please contact

Noel J. Spiegel

United States

Partner in Charge of Global Marketing

+1 212 492 4135

nspiegel@deloitte.com

Helen den Held

The Netherlands

Director of EMEA Marketing

+31 10 272 1030

hdenheld@deloitte.nl

Amanda Goldstein

United States

Director of Global Marketing

+1 212 436 5203

agoldstein@deloitte.com

Steven Dow

Hong Kong

Director of Asia Pacific Marketing

+852 2852 5638

sdow@deloitte.com.hk

Hiro Notaney

United States

Director of North America Marketing

+1 408 704 2464

hnotaney@deloitte.com

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