

SAS International Hotels

Update of the 1993 company profile

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Key figures SIH (incl. hotels under contract)

	1994	1993	1992	1991	1990
Number of hotels	30	34	32	28	25
Number of rooms	?	8,004	7,100	6,023	5,924
Employees	?	5,192	4,536	3,813	3,877
Gross profit margin %	?	25.6	21.1	22.4	23.1
Operating result (million NOK)	?	48	-19	-32	4
Net result after financial items (million NOK, before taxes)	?	-103	-126	-1047	-465

1. Changes at SAS

SIH's mother company SAS has gone through some very troubled years. The deepest recession in the history of the airline industry, a very severe crisis of the Nordic economies and the failure of SAS 'total travel strategy' and the break down of the Alcazar merger schemes, all added to SAS' problems.

In reaction to this, SAS has embarked on a new 'no frills' strategy, headed by the new president Jan Sternberg, former Executive Vice President of the Swedish Telecom company Ericsson. Mr. Sternberg does not present himself as a visionary strategy like Mr. Jan Carlzon. He prefers 'back to basics' instead of a prestige strategy. SAS must only do those things which can be noted by the traveller, all other things are to be contracted out.

At present the management is giving top priority to improving efficiency and profitability. Long-term strategic work is given less attention. It is still unclear whether SAS will go it alone or look for a partner. Mr. Sternberg has claimed that he never believed in the Alcazar project. He would welcome cooperation, but is opposed to a merger.

The SAS management is now said to be more interested in examining what a stand-alone alternative would mean for the company. A strong intercontinental flight network would in the long term require a larger passenger volume than can be provided by SAS's Scandinavian home market. A merger or close cooperation with one or several major airlines in Europe would therefore be needed.

SAS has stakes in some smaller airlines, including British Midland of the UK and Spanair, which operates both scheduled and charter flights to Spain. SAS also cooperates on a relatively superficial level with Swissair and Austrian Airlines within the EQA.

In September 1994, SAS announced a cooperation with the Latvian government and with Baltic International Airlines to establish a new airline company. This seems to indicate a strategic orientation of SAS to its Northern and North-Eastern European home market. This seems to be confirmed by the announcement of the purchase of a new fleet of short- and mid-range airplanes.

These links hardly form a basis from which SAS can expand into one of the dominant European airlines with a global network. It does, on the other hand, offer SAS the opportunity to build up a stronger flight network within Europe, while possibly retaining some intercontinental routes.

A SAS that was a strong and profitable airline within Europe could be an attractive alternative to a SAS that was only a small part of a large global company. There is of course a danger that it could become marginalised into a small airline with only European routes.

During 1994 the SAS workforce was to be reduced by 40% (9.000 out of 23.000), including 3,000 jobs which will disappear from the airline itself this year. Many of these jobs were to disappear by the sell out of non-core activities. Over 1994 SAS sold:

- * SAS Leisure and Airtours UK, sold with a profit of 374 m. SEK
- * participation in LanChile
- * SAS Service Partner sold for 270 m. SEK
- * SAS Leisure (charter flights, holiday travel etc) was sold for SEK 870m to Airtours of the UK at the end of April with a profit of 374 m. SEK

* Diners Club Nordic, sold for 200 m. SEK

Apart from the sale of the above-mentioned companies, some 25 aircraft will also be disposed of.

Parts of SAS Trading have also been sold. SAS is to retain its airport and in-flight duty-free sales operations but will transfer them to its airline company from SAS Trading, which is to be wound up. SAS Trading will remain in existence until the EU abolishes tax-free sales in five years time. The hotel activities are said to be the only exception of the 'back to basics' philosophy of the airline company.

All this resulted in the SAS mother company becoming profitable again in 1994, both for its operating results and its net results. Compared to the 1st half year 1993; with a loss 609 million SEK before tax and depreciation, the 1st half year 1994 was very good; a profit 617 million SEK excl. sales of Diners Club Nordic and SAS Service Partners to Gate Gourmet.

The very high net debt decreased with 3,94 billion SEK. to 9,95 billion SEK.

2. Consequences for SIH: WIN project and other restructuring

SAS's new line of concentrating on the airline business, left SIH management insecure of the future of their company. SIH's as a loss making company with an ill-devised strategy did not look like a dear possession for SAS. SIH management set itself 2 tasks, which had to be achieved in a 2-5 years period:

- increase the value of SIH
- remain flexible.

Even before SAS had to face a radical change of strategy as a consequence of the faltering of the Alcazar project, SIH had embarked on a radical cost cutting strategy; the WIN project. This aimed at reducing variable costs between 1993 and 1995 by 20% on an annual basis. In the beginning of 1994 this was followed by the 10+ project, aimed at increasing revenues with at least 10%. But 10+ also has resulted in more cost-cutting measures.

The WIN project is organised centrally, leaving local managers with little more than the duty to reach centrally planned targets. For instance Brussels sets standards for the ratio of the number of permanent employees to the number of employees needed when the hotel is fully booked. In a Swedish R/S hotel this has been lowered from 75% to 60%.

In Norway local management threatened local unions to cooperate with the costcutting programs, otherwise SIH headquarters in Brussels would intervene. On the other hand, local circumstances still define the exact ways of implementing WIN, as SIH hotels are not situated in standardized buildings, compete in different local situations and vary greatly in size from the giant Scandinavia Hotels in Oslo (491 rooms) and Copenhagen (542 rooms), the Plaza in Hamburg (560 rooms), to the smaller Berns' hotel (63) and Trondheim (106 rooms).

Employment effects of WIN vary. In the Scandinavia Hotel in Oslo, management wanted to dismiss 120 employees and sub-contract many services. In Denmark already 3 out of every 4 rooms is cleaned by outside personnel. Also dishwashing is subcontracted. In Finland permanent staff levels have decreased from 125 to 85 (in a 260 room hotel). At the Portman hotel in London, WIN was implemented at the same time of the refurbishing, which led to the decrease in the numbers of high skilled maintenance staff personnel.

In Brussels management wanted to dismiss 25 employees, at the end 10 persons had to leave, but the technical department increased with two persons. In Amsterdam manning levels at this department did not change.

At the Park Avenue hotel in Gothenburg, job rotation schemes have resulted in the firing of unskilled workers, where later newly hired temporarily 'day-to-day' workers filled in the gap.

WIN has resulted in increased pressure on flexibilization, for instance housekeeping is now expected to assist banquet during peak hours. Other cost-cutting measures include purchasing cooperation with other hotels chains, like in Norway where 11 out of SIH's 34 hotels were located in 1993 (7 out of 31 in 1994). The Norwegian branch of SIH and Rica Hotels signed an agreement in January 1994 to cooperate on purchasing and services. The goal is to centralize and reduce daily expenses incurred

from food and beverage, laundering, maintenance, and technical services that involve the upkeep and purchasing of refrigeration systems. Together, the two companies spent Dollars 134 million in 1993 in these areas.

Another consequence has been SIH's aim to cut all unnecessary luxury, sometimes even to close the restaurant. SIH stated: 'We have made a complete review of all our activities and focus only on those services that the customer wants and is willing to pay for. We have discarded the old-fashioned belief that a hotel should provide everything'. On the other hand, for some services which are kept inhouse, outside clients will be acquired.

SIH downtraded business travellers by introducing a reduced cost alternative to its Royal Club executive brand. Business Class will replace Royal Club in 16 of the 23 SAS hotels that feature it. Prices are ten to 15 per cent lower. The SAS Portman Hotel in London is among those which will move over to Business Class.

The 'Foodissimo' concept is designed to bring costs down of the restaurant operations. In future in 21 hotels only convenience food will be served. The restaurants should prove their profitability, even when an internal rent is charged. Most food will be ready-made purchased, bakery and butchery departments in the kitchens will close. Personnel requirements will change from specialist to generalist, the chef will become a manager responsible for achieving financial targets. Just like SIH already has international room and conference standards, Foodissimo will provide a food standard for all SIH hotels, except those where the gourmet restaurant can achieve a profit of at least 30%. But even there some Foodissimo concepts will be introduced. After a trial period at the Hamburg Hotel, Foodissimo will be launched in London, Amsterdam and the Scandinavia in Oslo, to be followed by all 5 hotels in Denmark, and the one in Malmö, the 4th phase will include all Stockholm hotels (except Berns'), to be followed by the 5 Norwegian hotels (except Bergen).

*** It will be useful for workers representatives to compare early experiences with Foodissimo, as it will have serious consequences for the number and skill-level of employees in Food&Beverages.**

SIH restructuring programme also resulted in the selling of some hotels that did not fit in with SIH core strategy. Four hotels in Norway, around the North-Cape and were disposed of. The former Inter-Continental Royal SAS hotel in Cologne was sold outright to the German hotel company Dorint (which already was the most important shareholder), The Hamburg hotel is sold but still under SIH management. SIH will take its time to sell all its property, waiting for a good price. SIH also wants to sell the SAS Scandinavia Hotel building in Oslo and then lease it back. The value of the building is estimated at several hundred million kroner. Olav Thon Gruppen is reported to be among the interested buyers, as are insurance companies and finance companies. SAS also wants to sell the Park Royal Hotel building near Fornebu airport, the SAS Royal Amsterdam building and hotel properties in Brussels and Düsseldorf. The sale of these properties would raise much wanted cash for the airline. In 1990, SAS sold three hotels in Copenhagen to three limited partnership companies for DKr 1.3bn.

The hotel operation SIH is at present showing an operating surplus, but is undercapitalised. This can be changed when the company sells its property assets, which according to SAS are worth an estimated SEK 2.5bn. (compare: SAS is aiming to reduce its total debts from SEK 16bn to SEK 6bn, so selling of these hotel properties can pay for 25% of SAS debts).

SIH managing director Bjorn Gullaksen said the company wanted to continue running

hotels but did not want to own real estate. So, new developments are financed by local developers (e.g.: Parkring Vienna by Bank Austria with its daughter company the Z-Treukonsult Beteiligungsgesellschaft, the Hanoi Royal Hotel, which is to open in 1996 by a Singapore investment company and the Hanoi Tourism Service Company, Toserco, which is owned by the city of Hanoi).

Comparing 1992 and 1994 figures on the distribution of SIH's hotel operations gives the following picture:

	1992	1994
Owned	8	5
Leased	13	11
Managed	10	14
Franchised	1	1
Total	32	31

3. Comparison with 1993 conclusions

In the profile of SIH written in 1993, we concluded that the strategy of SIH was marked by reversals of major decisions only taken a few years before, like the 1992 Coronado deal, the Inter-Continental deal, the creation and closing down of the SIH Holding (1990-1991), etc. Has this been changed for the good in 1993-94? The next table provides for an overview:

- | | |
|--|--|
| - 1989-91 catering expansion, turned back 1992 | - 1994: sale of SAS Service Partner |
| - increase in activities SAS Leisure | - 1994: sale of SAS Leisure |
| - increase in ownership over 1992 in spite of strategic intent | - 1994: sale of property, disposal of Cologne hotel to Dorint, announcement of possible franchise strategy |
| - aim: 2 or 3 properties more each year | - 1994: 60 new hotels up to 2000 |
| - 1993 Swissotel alliance | - 1994: Radisson deal, end of Swissotel alliance |
| - net result far worse than operating profit -> bad asset management (1991 large loss as result of Inter-Continental deal and net financial costs) | - 1993: net financial costs and provisions and write-down of fixed assets increased over 1992. |

According to mr. Ritter "SIH has put the Inter-Continental traumas once and for all". But it is still too early to be sure that SIH now is on a stable new course especially as the sector is changing so much (see chapter 5).

4. Radisson

SIH found itself in 1993 in a difficult position: Expansion was needed to make productivity grow, to enlarge market share and to increase profits. But SIH was heavily indebted to SAS and SAS did not want to provide for more capital. Instead SAS insisted on SIH repaying loans. So SIH decided that to enlarge its brand awareness outside Europe and to get access to large global reservation systems by means of a strategic alliance with another international hotel chain. Three possible alliances were considered: a marketing cooperation, like the one with Swissotel started in 1993, a joint-management alliance or a franchise alliance. SIH contacted almost every major hotel chain. Accor was very keen on giving SIH the right to develop the Formul 1 concept in Scandinavia. But the budget Formul 1 hotels would not have fitted within SIH's upmarket hotel operations.

In the end, a deal was struck with the American Radisson chain. Radisson is the brand name of the Carlson Hospitality Group. Radisson Hotels International and Carlson Hospitality Group, Inc. are part of Carlson Companies, Inc. Corporate headquarters are located in Minneapolis. Carlson is one of America's largest privately owned corporations with system-wide revenues of Dollars 10.7 billion in 1993 including 7 milliard on Carlson Travel. Compared to this, SIH is very small. SAS is the fourth largest airline in Europe with 1993 revenues of Dollars 5 billion, SIH only accounts for 2,8 milliard SEK. The next table gives the position of both hotel chains in the world league:

top hotel companies (Based on number of rooms)

Name of company	Number of rooms
1 Hospitality Franchise Systems - Parsippany, NJ	369,485
2 Holiday Inn Worldwide - Atlanta	336,465
3 Best Western International - Phoenix	276,797
4 Choice Hotels International - Silver Spring, Md.	239,696
5 Accor - Paris	238,990
6 Marriott Corp. - Bethesda, Md.	170,211
7 ITT Sheraton Corp. - Boston	129,184
8 Hilton Hotels Corp. - Beverly Hills, Calif.	96,288
9 Forte plc - London	78,833
10 Carlson Hospitality Group - Minneapolis	77,934
11 Promus Cos. - Memphis	77,091
12 Club Mediterranee - Paris	63,525
30 Scandic Hotel AB	14,000
51 SAS International Hotels	7,946

Beside its travel agencies (which have recently merged with Accor's Wagonlit travel agencies), and hotel activities, Carlson is also engaged in restaurants, with chains like

Country Kitchen, and TGI Friday.

Radisson has over 300 hotels, in 33 countries, with over 70.000 rooms. Its 25 properties in Europe include London, Geneva, Lausanne, Berlin and some in Eastern Europe and one in Scandinavia. The addition of the 28 new Radisson SAS hotels brings the total number of hotel locations in the Carlson Hospitality Group to 343 hotels in 39 countries.

While no merger of the companies is involved, the SAS properties will be renamed Radisson-SAS Hotels Worldwide. SIH becomes the head franchisor for Radisson in Europe. Existing Radisson hotels will remain what they were, unless in Europe they want to come under the R/S umbrella. This also depends on existing contracts with the owners. Within the UK, Radisson has given the exclusive rights for developing Radisson hotels to the Edwardian group, which operates 9 Radisson/Edwardian 'country house' hotels in London. This exclusivity only counts for London within the circular-road though. Outside the London circular-road, Radisson hotels might be developed by both Edwardian and SIH.

The agreement between Radisson and SIH, which has been signed for 30 years, gives SIH the exclusive right to develop Radisson hotels in Europe. The stated objective of the agreement is to have 100 hotels before the end of the century 2000, which means an increase of 60 hotels in 6 years!

SIH will manage and run the hotels, which will take on the Radisson/SAS Hotels Worldwide logo, while Radisson will market them globally and connect the hotels to the present reservations system. This 'seamless/no-interface' reservation system of Radisson is said to be one the world's most advanced reservation system, and access to it is one of the main benefits for SIH. Other benefits for SIH include:

- SIH is strong in Europe and Radisson is strong in America. Thus both chains complement each other with little overlap, except in London and Stockholm. Radisson did not have its own European management team.
- Both players concentrate on luxury hotels.
- Both players apply special 'cushioning' packages in connection to overnight staying at the hotels.

But there are also some disadvantages:

- Radisson is a chain based on franchising, whereas SIH is based on management contracts.
- Radisson is based on a very broad concept of hotelling with many choices up to the franchise-takers, whereas SIH has a very clearly defined concept.
- Radisson is not strong in Asia nor in the Middle-East, whereas in Europe it is not very well known.

Another disadvantage was the termination of the recent alliance with Swissotel, which was the result of the Radisson deal. SIH agreed in 1993 upon a long-term joint marketing alliance with another airline-owned hotel chain: Swissotel. As part of the marketing pact, Swissotel and SIH merged their global sales operation. Further collaboration was to be extended via joint promotion and the merger of sales and marketing operations.

After the Radisson deal was struck, the agreement with Swissotel was terminated. Swissotel said it had already decided to link up with Datalead, the reservation system for the Leading Hotels of the World chain, from September 6 1994. Datalead will allow Swissotel to connect with such reservation systems as Galileo, Amadeus or

System One.

The Carlson Hospitality Group, the owner of Radisson, also had a cooperation with Swissotel, and also with Mövenpick. These too were cancelled in favour of SIH.

Mövenpick Hotels International (MHI), hotel arm of the German-Swiss Mövenpick restaurant group, is now looking for a new partner. Radisson Hotels notified MHI that it will not be renewing its collaboration contract with it at the end of 1994. This decision came after Radisson Hotels formed the alliance with SIH. A Mövenpick spokesman said the group had also been informed about Radisson's plans and the deal had been cancelled in mutual understanding. Mövenpick was in talks with other partners and cooperation with a European partner was preferable to a US partner. Mövenpick added the five-year cooperation with Radisson had not led to the expected expansion in its US business and Radisson had also pursued a different strategy than Mövenpick.

New structure?

SIH headquarters in Brussels will oversee the R/S activities in Europe. Reporting lines and ownership structures will remain what they were. Thus SIH employees will remain employees of SIH.

Within R/S management, which in fact is the old SIH headquarters of Brussels, a new layer has been created between the president and the area manager: the area managers are divided into a group of 5 and a group of 4 areas, with both a senior vice-president operations in charge of them.

Thus there are now 2 layers between the president and the general manager (GM) of the individual hotel:

- * CEO/Executive committee
- * Senior VP operations
- * Area manager
- * GM

This looks like a very heavy overhead burden (compare: Scandic aims at 2-3 layers between the president and the reception).

Several other functions are organised on a level higher than the individual hotel, e.g. a new function has been created: director of national accounts, to deal with customers who are important for more than 1 hotel. On a higher level, the director of international accounts deal with customers who are important for more than one country.

SIH is operated in a very centralised way. For instance, autonomy over the investment budget of a GM is very low. For investments above a certain level (\pm 10.000 SEK), the Chief financial officer, the Vice-president technical development and the Area manager have to give permission.

SIH uses a very complex planning system (LOTS), which takes a 5-day course for managers to understand the basics of it. The local GM makes a yearly businessplan, which has to be approved by the area manager, but also other managers of the Brussels' HQ have a say, for instance on the Human resources part, the Human resources (HR) manager is involved. After it has been approved, the local businessplan goes to the board who has to take the final decision.

As to central HR management, the main tool is the corporate HRM plan. This has 2 elements:

- the 2-yearly climate analysis. On the basis of this analysis, corporate HR department sets targets for improvement for individual R/S hotels.

- reports on ratio's like the personnel costs ratio. This is subject of discussion between HR, the Area manager and the GM. Clear set norms are not applied.

SIH's 15 central concepts (like No Excuse, Late Check-out, Room Styles, etc.), its GM guide book, etc. work out in full detail how a SIH hotel should be operated. So, how will present Radisson and new R/S hotels fit into this structure? This question is especially important to establish which hotels will be included as future members of a SIH European works council. Should franchised hotels be viewed as integral parts of SIH? Note for instance that the Luleå hotel (SIH's only franchised hotel) is not on the list to introduce the Foodissimo concept. As Radisson is a franchise chain, and R/S intent to grow very rapidly in Europe, it seems likely that R/S will contain more franchised hotels in future.

All present and new R/S hotels will pay a fee to SIH based on their revenue, since SIH is the head-franchisor. SIH will pay a sum to Radisson 'based on a specific formula'. Prior to settling a franchise deal, hotels will be checked in detail as to whether they fit in with SIH standards. The "Yes I Can" training of R/S is mandatory for all employees. After this, a yearly audit by R/S will decide whether the franchised hotel may still bear the R/S brand name. The franchise-taker pays a fee for R/S central marketing and reservation support.

SIH management tools like LOTS, GM Handbooks, climate analysis and monthly HR reports are not mandatory for franchised hotels, but they can make use of it for a fee. On the basis of this information, one might conclude that franchised R/S hotels can be viewed as independent companies.

SAS and SIH: a new relation?

Although a 100% daughter company of SAS, the autonomy for SIH management has never been clearly defined and remained a question of bargaining between SIH management and its board of SAS supervisors. The Inter-Continental deal for instance had been pushed by SAS president Jan Carlzon.

As a result of the Radisson deal, the future of SIH is no longer solely depending on SAS. One might speculate on the question why SAS did not sell SIH when it was looking for cash to cover its losses. The very complicated balance sheet of SIH makes it hard say much about it. But some experts state that SIH was not sold because it would not have made much money for SAS because of its heavy debts on the one hand, and the low prices paid for real estate on the other hand. (SIH's cash-flow on the other hand was still big enough to repay its debts to SAS.)

Both aspects are changing and so may be the future of SIH within SAS. SAS continues its hotel operating strategy for the time being, contrarily to SAS's strategy to concentrate on its air traffic operations. Also the 'fly&stay SAS' strategy will be continued, e.g. by loyalty programmes. According to Mr. Ritter (Hotline extra, august 1994) SIH growth is no longer limited to destinations served by SAS. (As SAS flies to 102 destinations in 34 countries, this would leave tremendous growth opportunities for SIH all the same).

SIH is to open new hotels in Riga, Latvia, in concordance with SAS' new joint venture with the National Latvian Airliner. It is also planning a new hotel in Paris. In addition, talks are underway with two small Mediterranean hotel chains which would like to join the Radisson SAS cooperation. Besides a resort hotel at the Red Sea is being considered. This goes to show that at present SAS's airline policy still is one of the factors defining SIH's strategy, but it no longer is the only factor.

5. Sector background and perspectives

To understand the Radisson/SIH deal, it might be useful to provide for some more sector background, especially to understand the way American hotel chains are targeting Europe. Choice taking over Primevere in France and striking many franchise deals in Europe, and Sheraton (ITT) taking over the Ciga chain, are but two examples of this trend.

Leading hotel companies have entered a new era in the quest for globalization. They realize that because of emerging markets, rapidly changing governments, new lending sources and stiffer competition, strategies for worldwide expansion must differ in the 1990s. For instance, US hotel experts think strategic alliances with developers outside the United States are essential. Thus Carlson's strategy of teaming up with European partners is only part of a more general trend.

Hotel companies can't expect to achieve success internationally by flying in someone when there is a problem or new deal pending. They have to have experts stationed at strategic points worldwide if they want to grow globally.

They also need to do mergers with foreign companies or build strategic alliances to help gain entrance and acceptance in new foreign markets. There is so much fragmentation in some areas of the world that foreign hotel companies have to work with regional or local companies under one umbrella group or one agreement to accelerate growth. The 'hub-and-spoke' system used by Choice Hotels International might serve as an example Radisson is trying to follow. This allows the company to offer master franchises abroad, resulting in Choice's brands proliferating throughout particular countries and regions.

It is interesting to note that some experts expect to see alliances with non-hotel companies, such as airlines. This would be a reversal of the trend of the early 1990s when airline companies dropped their hotelchains, like for instance Air France did when it sold its 59 Meridien 4-star hotels to Forte.

These recent trends have resulted in luxury hotelchains taking up their favourite game of monopoly once again. Fierce take-over battles have been fought over the past year and will continue. It is not hard to predict that many chains will change ownership.

Another important trend is the increasing separation between ownership and management, as we have seen with SIH also. In the past operational hotels activities were repeatedly obscured by ownership transactions which had much larger financial consequences. Top management often took more interest in the real estate business than in hotel operations. The stricter separation between ownership and management will give an extra incentive to innovations in management, resulting in more efficiency drives, faster introduction of new technologies, etc.

This trend will be combined with a continuing pressure on prices, also for the business traveller segment. (e.g. in the Netherlands Shell, Philips and the government are cooperating in travel purchasing, accounts over several hundred million guilders).

Thus we may conclude that take-overs and cost-cutting will mark the luxury hotel sector for the years to come, resulting in an unstable employment situation.