Case #15

Company: A.T. Kearney (Round 1)

Topic: Market Entry, Competitive Analysis

Industry: Hospitality

About the Case

This case has a center piece that is quantitative in nature; the rest of the case may explore various aspects of the market entry decision-making process and does not follow a specific sequence. The case focuses on two key focus areas - the attractiveness of the market [Market sizing and five forces] and long term profits [Sustainability, barriers to entry, core competencies and signaling].

This case allows you to handle various issues at different points, so ask the candidate to choose a starting point, but challenge the candidate probe to give strong reasons to validate his/her choice. An example would be: "I'd like to start by reviewing the company's core competencies because I want to see if this fits into their development model…"

Defining the Problem

Your client is a real estate developer and is currently assessing a new project idea.

Costa Rica has a beautiful coastline which has historically been difficult to access. The nearest airport was over six hours away. As of last year, a new airport was constructed only a half hour away. There has been an investment boom in the region due to the increasing number of tourists (popular with Americans and Asians). The Mandarin Oriental and The Four Seasons, two prominent luxury hotel chains, were the first to enter this market with a 250-room hotel each.

Should your client invest in the tourism opportunity created by the new airport? Would you recommend that s/he enter the market?

Information Gathering
Read this information well before you administer the case. Provide the following information on request.

Prompt 1: Core Competencies

The client has focused on hi-rise apartments (50%) and luxury condominiums (50%) in the past but wants to enter the hotel arena.

Author's Commentary/Notes: *The key insight here is that the client has past experience in constructions of a similar type, but has no direct experience in the hotel industry or service operations.*

They have focused on world-class beaches, such as Playa del Carmen, Marbella, Coral Beach, Tahiti, Fiji, Maldives, Mikonos, etc.

Author's Commentary/Notes: *The insight here is that this client probably has good judgment in spotting travel locations and has a successful track record with the construction of prime properties.*

Prompt 2: Market Attractiveness

- Market size - 875,000 tourists per year (assume 350 days in a calendar year)
  Average duration of stay per tourist - 4 nights
- Average hotel check - $2,000.
- Others - In terms of tourists, you depend on government spend on advertising, on travel agents, and on the network effect of the existing hotels in the area.

Answer:

3.5 million tourist nights / 350 days = 10,000 tourists / night

$2,000 average check/ 4 days average stay = $500/night

Prompt 3: Five Forces Analysis – *This part of the case is exploratory; interviewer should prompt the candidate to list several factors*

- Competitiveness - Other hotels chains that are thinking of entering the market are Starwood, Peninsula, and Imperial Hotels.
- Supplier Power - The local labor market offers a huge supplier of workers (very positive)
- Substitutes - You are fighting with every other “paradise-type” destination, from Disneyland to Vegas to Bermuda. Interest in this area, however, is sky high.
- Barriers to Entry - Government regulations, high capital requirements, unavailable beachfront property.
- Buyer Power – The recent consolidation among travel agencies and proliferation of e-vendors put buyers in a powerful position.

Author’s Commentary/Notes: *The key takeaway here is that despite the competitive nature of the market it is large enough to be profitable, and client has desired capabilities to successfully compete. The level of resources required would be a barrier to entry and maybe there are others that need to be investigated--such as government permits, access to sewage, water, etc.*

Prompt 4: ROI analysis – *Inform the candidate that client has already short listed three available lots. Ask him/her to recommend one of the three such that Return on Investment is maximized? (Show **Exhibit 1**)*

Author’s Commentary/Notes: Note: ROI = Profit/Investment. *Give the candidate several minutes to generate these numbers. A solid candidate will be vocal during the calculations, and may even introduce a written version of the match. That means that instead of just writing numbers, the candidate will write out formulas, such as…*

Revenue = Revs per night * number of nights * number of rooms * nights per year * occupancy rate

By doing this, the candidate demonstrates knowledge of the situation. If a math error comes about, it is much easier to correct and the interviewer recognizes that the candidate has already shown a strong grasp of the problem.

Answer:

Option 1: Lover’s Lair

- Operating Profits: (((($450 revenue – 250 operating costs) * 500 rooms)* 350 nights/year) * 50% occupancy rate) = $17.5 million operating profits/year (a)

- Initial Investment: 30,000 cost/room * 500 rooms + $2,000,000 land = $17 million (b)

- Net Profit: (a)-(b) = $500,000 (c)

- ROI: (c) / (b) = $500,000/17 million = 2.9%

Option 2: Paradise Lost

- Operating Profits: (((($400-200) * 1000) * 350) * 50%) = $35 million
- Initial Investment: 28,000 cost/room * 1000 rooms + $4 million land = $32 million
- ROI: $3,000,000 / $32 million = 9.4%

Option 3: Fookwah Heights

- Operating Profits: (((($350-150) * 1500) * 350) * 50%) = $52.5 million
- Initial Investment: $25,000 * 1,500 rooms + $6 million land = 43.5 million
- ROI: 9 million / 43.5 million = 20.7%

Prompt 7: Factors determining project feasibility – *Ask the candidate to list factors to be considered in determining the feasibility of the project*

Answer:
Good Concerns:

- Competition (what are they focusing on? will it flood the market?)
- Strategy (Where will you compete--low cost, high service, best in class, packages?)
- How should the developer finance the building? Since the hotel will bring jobs maybe the government can help with some tax deductions, free services, etc…

Great Concerns:

- How can they leverage their experience, what values from their other business can they leverage? Would they manage the hotel or build it and then find an operating partner like Starwood or Hilton?
- What are the existing barriers to entry, how would you change them to insure a greater degree of success?

After the candidate offers his/her insights, tell him/her to focus on ROI, first with the room prices specified in ***Exhibit 1*** *and then with the market room price ($500).*

Conclusion: *Ask the candidate to conclude the case with a "go/no go" decision, supporting it with the insights drawn through out the case. Probe into additional concerns the client needs to address.*

Exhibit 1

	Land Cost	Cost/room	Operating Cost	Room Capacity	Price/night
Lover's Lair	$ 2,000,000	$ 30,000	$ 250	500	$ 450
Paradise Lost	$ 4,000,000	$ 28,000	$ 200	1000	$ 400
Fookwah Heights	$ 6,000,000	$ 25,000	$ 150	1500	$ 350

NOTE:

- Average occupancy 50%
- No. of operating days in a year: 350
- Operating expenses are 100% variable
- At ROI 10%, company target is to recover investments within one year