Personality Hires

Team 1

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Section 12

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Royal Caribbean Strategic Proposal

Executive Summary

Royal Caribbean is well positioned as the leader of the cruising industry. A position where they can drive industry-level changes. The company has strengths in operational efficiency and unique offerings. There's an opportunity to capture greater market share as the industry expands its consumer base. We recommend Royal Caribbean offer its customers the opportunity to purchase an annual pass for the price of $1,735 which will then give them 15 days out of one year to go on any Royal Caribbean cruise of their choosing on any dates offered, on top of a 10% discount on all onboard purchases.

This strategy will not only further solidify Royal Caribbean's brand of being the innovator, but also increase revenue – especially in slow periods. This project yields an NPV of $29,602,394 and an IRR of 12.88%. **(Model 1-1)** The initial outlay is $695,732,250 in marketing and technology expenses. The project will see positive cumulative cash flows in Year 5. **(Chart 2-2)** We believe this change in model will empower Royal Caribbean to bring new guests into their cruising ecosystem, in addition to automatically placing the consumer mindset into repeat customership. Consumers are familiar with this model in other industries as we have started to see the subscription concept being brought over into non-land-based leisure industries like air travel**.**

There are potential downsides in over-reliance on travel agents to push the new pass since the model does not currently account for referral commissions. This is a migitable factor that can be addressed early on to boost annual pass sales if we are not tracking towards making our intended count.

Client's Vision, Mission & Strategy

Royal Caribbean's mission statement shows how committed they are to ensuring that their customers' experience is memorable and enjoyable. Their purpose is to deliver exceptional service, guaranteeing customer satisfaction by consistently surpassing expectations **(Royal Caribbean Cruises, 2022).** The people-centric approach the company takes to its operation also extends to its employees. This seems almost out of necessity based on one of the weaknesses we will discuss later in this proposal analysis. Keeping employees engaged and motivated is important to Royal Caribbean because it will help enhance their reputation, customer interaction, and overall culture.

Royal Caribbean is consistently aligning its actions with both its mission and vision. They sell their guests on providing a high-quality experience through innovative ship design, unique additions to the base itinerary, and exceptional customer service. They offer the world's tallest slide at sea, onboard skydiving, escape rooms, and the world's first robotic bartenders gives them greater brand recognition with both avid cruisers and potential new cruisers **(Royal Caribbean Cruises, 2022)**.

Royal Caribbean operates through a broad differentiation-level strategy. They do not target their marketing to specific market segments like focused differentiation, and they do not sell fares at the lowest possible price to attract the maximum number of customers like cost-leadership. Royal Caribbean has specifically focused on their offerings as their marketing tactics to appeal to the masses while justifying their not-luxury-but-not-cheap pricing. That is *literally* textbook broad differentiation. This strategy strongly correlates with their mission and vision – always wanting to provide the experience of a lifetime for their customers.

Royal Caribbean's mission and vision are similar to their competitors. Most of the cruise lines within the industry strive to provide excellent customer service and cruising experiences. At this point, it's important to note that Royal Caribbean's most relevant competitors are Carnival and Norwegian. Other cruise lines exist – Virgin, Disney, MSC – but they do not operate at the same level of market share and capacity as the big three. Despite the similarity in missions, neither Carnival nor Norwegian utilize the broad differentiation. Carnival utilizes a cost-leadership strategy, while Norwegian operates with the intent of focused differentiation. This empowers Royal Caribbean to continue to stand out within the market.

As one of the largest cruise lines in the industry, Royal Caribbean is able to constantly set the expectation for new and innovative cruising experiences for consumers all around the world. Offering a fleet of 64 ships that are able to travel to over 1,000 different destinations across the world, it is safe to say that Royal Caribbean is constantly raising the bar for a unique and memorable cruise experience **(Royal Caribbean Cruises, 2022)**. Since the company's founding, they've developed a solid stream of income that allows them to continually grow and advance forward within the industry. Revenue is coming in for Royal Caribbean from primarily the Pacific/ Asia region at 37.9% followed by North America at 22.8% **(Reiff, 2023)**.

Royal Caribbean has done a phenomenal job of rebounding their operations since the COVID-19 pandemic struck and greatly improved their net loss. In 2020, Royal Caribbean saw a massive net loss of $5.77 billion and was able to slightly reduce that loss to $5.25 billion in 2021. However, in the most recent fiscal year of 2022, we saw Royal Caribbean cut their net loss in half bringing it down to $2.16 billion which is an extremely impressive improvement **(Royal Caribbean Cruises, 2022)**. When we look at EBITDA for operation-centric financial performance, Royal Caribbean turned its first profit with an earning of $583,185,000 **(Royal Caribbean Cruises, 2022)**.

The company has been able to make this incredible turnaround using a few tactics. The most obvious reason is being able to raise their Occupancy Rate as the pandemic subsided. Occupancy Rate is defined as a ratio of passenger cruise days to available capacity days. Accordingly, they have been able to sell more in fare and onboard purchases which has helped combat operating at a loss.

Royal Caribbean has not only needed to focus on a financial turnaround. TIME magazine says, “The Cruise Industry Is On a Course For Climate Disaster.” **(De La Garza, 2023)**. Royal Caribbean needs to take the necessary steps to be an environmentally conscientious company, and they are. For example, their new class of ships will turn on-ship waste into usable energy **(Royal Caribbean Cruises, 2023)**. These measures not only support the environment but give cause for current and potential customers, investors, and activists across the globe to support Royal Caribbean.

SWOT Analysis

Starting with an internal analysis of Royal Caribbean, we noted the two biggest strengths of the company. The first strength that Royal Caribbean possesses is operational efficiency. Operational efficiency can be defined as an organization's ability to best utilize their resources and capabilities in order to maximize their desired outcome, minimizing any contributing costs and potential waste, while also still being conscientious of producing a high-quality product for their consumers. Royal Caribbean is able to maintain an Occupancy Rate across its portfolio of 85.1%, which is over 10% higher than their closest competitors **(Royal Caribbean Group, 2023)**. Royal Caribbean is strategic with how they manage their fleet, resulting in optimum ship deployments. We see this intentionality when CEO Jason Liberty is quoted stating the use of Utopia in short-duration Caribbean sailings to "compet[e] with land-based vacation alternatives and driv[e] new-to-cruise customers into our vacation ecosystem," **(Cruise Industry News, 2023)**.

They make data-driven decisions and base their itineraries on customer demand, seasonal trends, and economic conditions. This is easily understandable when reviewing their 2024-2025 Deployment Summary **(Royal Caribbean Cruises, 2023)**. Of course, unforeseen events are always a possibility, which is why Royal Caribbean has plans in place in case something unexpected occurs. Whether it be sudden inclement weather conditions or a global health crisis like we saw in 2020, Royal Caribbean is always one step ahead and works diligently to make sure nothing hinders their smooth operations

Another one of Royal Caribbean's strengths is their unique offerings. Royal Caribbean differentiates themselves from the competition by constantly pushing out new and innovative ship designs that cater to the needs of their customers. We can see an example of this in Royal Caribbean's latest ship, the Icon of the Seas. This new ship is set to become the "world's biggest cruise ship" with amenities including six water slides, seven pools, and nine whirlpools **(O'Hare, 2023)**. Royal Caribbean offers a variety of rare products and services that no other cruise line does such as the world's tallest slide on sea, the only cruise line to offer robotic bartenders on board, the highest viewing deck on a cruise ship, and the first cruise line to introduce bumper cars, indoor skydiving, and surf simulators on board. Due to Royal Caribbean's expansive size, they are able to provide an extensive range of destinations, offer numerous dining and entertainment choices onboard, and leverage its fleet of 26 ships to capture a significant market share **(Royal Caribbean Cruises, 2023).** Their cruise ships offer experiences catered to all consumer segments; no matter who you are or what you are looking for, chances are Royal Caribbean has a package that is tailored to meet your desires.

With strengths, there are also weaknesses, and the two biggest weaknesses that Royal Caribbean possesses are finding and retaining quality talent, and the substantial amount of debt on their books. In order for them to maintain that operational efficiency which is one of their strengths, they heavily rely on their ability to recruit, properly train, and retain their employees. When there is a disruption in this process, their operational efficiency is hindered. Royal Caribbean is aware of this and makes note of it in the risk factors listed in their 10-K, as "critical to [their] success" **(Royal Caribbean Cruises, 2023 pg. 6).** The second weakness is related to the amount of debt that Royal Caribbean has amassed. As of December 31, 2022, Royal Caribbean reports an astonishing $23.4 billion of debt in their financial statements **(Royal Caribbean Cruises, 2023).** This is not unique to Royal Caribbean, in fact, most large cruise companies have a substantial amount of debt on their books **(Juliano, 2023)**. We saw an increase in the number of cruise lines taking on more debt due to the unforeseen circumstances and uncertainty of the pandemic. Because of this, many cruise lines are currently dealing with "a huge debt burden" **(Blenkey, 2022).** Being highly leveraged brings on other consequences, such as a lower credit rating. In cruising, this can be especially costly. To continue to innovate and expand their fleet, Royal Caribbean and all other cruise lines take on debt to do so. A low credit rating makes that debt more costly in the form of interest which will direct cash flows away from operation-centric expenses. Royal Caribbean and its competitors all hold this industry-wide weakness which could restrict them from the business expansion needed to continue to capture share within the growing consumer market.

In the external analysis, we note that both Power of Buyers and Competitive Rivalry is low **(Porter, 1988)**. Taking these considerations into account, we realize that Royal Caribbean's efforts would be best used in pursuing the opportunity of targeting new customers entering the cruise industry for the first time. Specifically, targeting the younger generations as they are the future of cruises. When pulling data from the CLIA 2023 Outlook, we found that 88% of millennials and 86% of Gen-X travelers who have been on a cruise plan to cruise again. Additionally, 77% and 73% of Millenials and Gen-X travelers who haven't been on a cruise say they plan to in the future **(CLIA, 2023)**. Clearly, focusing on younger generations now and fostering a loyal consumer base in this segment will lead to benefits that will last well into the future. By continuing to develop unique offerings and maintaining operational efficiency, Royal Caribbean will keep them coming. In other words, if Royal Caribbean focuses on taking their "cruise virginity", they will be setting themselves up for future success.

Evaluating potential threats to the industry involved taking a look at PESTEL and the factors that most influenced the cruise industry. We found that the factors most relevant to the cruise industry are economic, sociocultural, and technological. The economic and sociocultural factors were closely related as we noted that the ability of consumers being able to allocate money to travel and leisure heavily relies on the state of the economy, lifestyle choices, and consumer preferences and trends. The technological factor comes into play when thinking about issues such as streamlining their technology offerings and expanding on their digital presence.

The biggest threats to the industry we found were the dependence on favorable economic conditions and the possibility of being bypassed by competitors due to not keeping up with technological trends. The economic conditions and general societal trends heavily weigh upon a consumer's mind when making decisions on how they spend their leisure hours. In a stable or growing economy, consumers would be more inclined to spend the extra money on a fun-filled cruise package and enjoy their vacation dining and shopping in all the restaurants and stores the cruise has to offer. On the other hand, when times are tough, consumers will cut back on discretionary spending, and vacations would likely be the first thing consumers cut off. Royal Caribbean notes that economic downturn or changes in consumer habits “may result in cruise booking slowdowns, decreased cruise prices and lower onboard revenues” **(Royal Caribbean Cruises, 2022)**. The technological threat that Royal Caribbean must take preventative action against is keeping up with technological trends in order to not become washed out by other competitors. There is a certain expectation amongst consumers that must be kept up with such as easy online bookings or being able to contact customer service in order to update necessary information for their trip. Consumers want this process to be as smooth as possible, and having an increased digital presence allows for the most efficient and easy process. Anything that caters to the consumer’s needs and facilitates their experience with Royal Caribbean will have them stand out in their customer’s eyes and give Royal Caribbean a competitive advantage.

Companies in the Strongest/Weakest Positions

While the intent and scope of this proposal is specific to Royal Caribbean, we have to understand industry and its players to determine the best business level strategy for sustaining our competitive advantage. In this portion of the proposal, we’d like to define success within the industry using the following cruise lines: Norwegian, Disney, and Linblad **(Linblad Expeditions, 2022)**.

Many would argue that we should define success using Market Share, but that is simply not a good metric for the cruising industry. The Powers of Suppliers **(Porter, 1988)** for capacity are high, so operationally and financially strong cruise lines could have a relatively low Market

Share because they've been capped in capacity by the inability to take on a significant amount of debt. Both EBITDA and Occupancy Rate are calculated to be independent of industry forces as to best represent company performance in financial and operational effectiveness, respectively.. Admittedly, we should not ignore Market Share. We should use it to provide color and context to our analysis.

Accordingly, we've developed **Chart 1-3.** EBITDA and Occupancy Rate serve on our 'X' and 'Y' axis while Market Share is out Z-variable. At first glance, we seem to get a pretty standard story. As a company's Market Share increases, the company loses more money because it has a larger scale operation to maintain. When we turn EBITDA into Net Loss, the story changes. Things are more dire for Norwegian, specifically.

Despite what many would argue as Norwegian being an industry leader via Market Share, they have a disproportionately higher annualized interest and amortization obligation. Therefore, we would characterize them as struggling. Norwegian attempts at a focused differentiation strategy that primarily targets older, wealthier passengers with a premium experience. This is a tough market position to be in because their offering of luxury and exclusivity is almost negated by the fact that their sheer Capacity and Market Share dictate a necessity for cookie-cutting wherein their customers will eventually graduate to smaller cruise lines that innately feel more exclusive.

We should turn our attention to Disney who is serving a mildly successful competitor within this review. Disney capitalizes on its ranking as the 5th most admired company in the world **(The Walt Disney Company, 2022)** to empower a very unique offering not based on the novelty of ship amenities or innovations but in magical moments for guests. Despite having an EBITDA and Net Loss proportional to their Market Share, Disney has indicated a lower relative

Occupancy Rate than its competitors. This speaks to two main factors: (1) higher fare cost with less discretionary funds means less guests and (2) the brand being over leveraged across several travel and tourism locations and sub-industries cannibalized cruise occupancy.

With Lindblad Expeditions, we believe they are thriving in the industry for a few reasons. They have the highest Occupancy Rate with plenty of room to grow considering their average is much higher **(Linblad Expeditions, 2022)**. They are operating in a niche portion of the market where they dominate because they have partnered with the strong National Geographic brand **(Linblad Expeditions, 2023)**. They are well positioned to take advantage of a very eco-friendly image to further drive occupancy and, thus, earnings.

Every cruise line faced the industry-level weaknesses that the pandemic exposed. It should be noted that the remaining companies in 2023 have survived the worst of it and should have a positive outlook on the years ahead. The companies who could not survive… did not, and thus are not reflected in this analysis. Royal Caribbean is in a strong place to capitalize on a profitable EBITDA ($583,185,000), high Occupancy Rate (85.1%), and high Market Share (23.6%) **(Royal Caribbean, 2022)**. It serves as a strong industry leader with the right market positioning to be successful into the future.

Strategic Recommendation

Royal Caribbean is well positioned as the industry leader in innovation and operational efficiency to make waves. Our external and internal analysis have illuminated support for the strategic recommendation that we have developed for the company. We recommend Royal Caribbean offer its customers the opportunity to purchase an annual pass for the price of $1,735 which will then give them 15 days out of one year to go on any Royal Caribbean cruise of their choosing on any dates offered, in addition to a 10% discount on all onboard purchases.

Initially, Royal Caribbean should develop or purchase an extension to their website where you purchase the tickets. This process will involve proper planning, purchasing software, and testing this new extension.

Subsequently, Royal Caribbean should formulate and implement a marketing and advertising tactic aimed at effectively reaching the market. Maximizing customer outreach is crucial for this to be a success, which is why we believe establishing a sales and marketing team would be very beneficial to the positive outcome of this project. This team will be designed to engage and reach both loyal customers and new customers. Creating a new sales and marketing team means Royal Caribbean should open a new department dedicated to the launch and upkeep of this opportunity. One that will work to promote and advertise the annual pass, its benefits, and why it fits the consumer's needs. In developing their website to add an extension dedicated to this recommendation and building a new department, they will be set to be open for consumers to purchase.

Conducting a thorough analysis has allowed us to come up with our strategic recommendation of providing customers with the opportunity to purchase an annual pass with Royal Caribbean. This recommendation heavily aligns with our SWOT analysis, specifically Royal Caribbean's opportunities and weaknesses. Based on our SWOT we discovered that within the cruise industry, it is difficult to get customers on cruises year-round and not just primarily during the summer season. This recommendation allows Royal Caribbean to gain even more customers and revenue through onboard purchases and ticket sales by customers that may not have normally spent during slower seasons of the year. During our analysis, we also discovered the opportunity of capitalizing on the market and consumer demands. "Royal Caribbean says that as many as 50% of the people on a cruise are repeat passengers." **(CIO, 2015)**.

Many of these repeat customers have stated how much they love the onboard experience that cruises offer. Our recommendation will allow cruisers the chance to make a one-time purchase as an investment to be able to go on a cruise or multiple cruises that match their interests. This will in turn generate more revenue for Royal Caribbean as they will be able to reach a larger market of cruise lovers.

We have conducted an additional analysis to gain further insight into how Royal Caribbean operates within the industry. Our strategic group map **(Chart 1-X)** contains three distinctive variables where 'X' and 'Y' represent Net Promoter Score and Average Passenger Days and our Z-variable represents Market Share. This map shows that in fewer Passenger Days Royal Caribbean is making an impact on passengers having a good experience and not needing long itineraries. Royal Caribbean has achieved high customer satisfaction and loyalty in fewer days and, because of that, holds a high Market Share. Our recommendation of the annual pass will give customers the capability to get a couple of days in throughout the year. Royal Caribbean obtained an average passenger day of 6.3, with an annual pass instead of the 6 cruise days happening in a certain time frame it opens the time frame for the whole year. Longating relevance that the Royal Caribbean brand has and stretching out customer satisfaction throughout the whole year, in turn, will increase its Net Promoter Score. Annual passes will help Royal Caribbean maximize what they already do well and create a better overall experience for their customers.

As discussed previously, Royal Caribbean uses a broad differentiation business-level strategy. This strategy directly aligns with our recommended action of utilizing a subscription-based model. A broad differentiation strategy is known for charging higher prices in return for a luxury or desirable product or service. With our recommendation, Royal Caribbean is able to capitalize on the fact that they already offer a desirable service. Offering a subscription model will allow customers more of an opportunity to use and purchase these unique onboard services. Royal Caribbean will be able to reach more customers who are interested in a company that uses a broad differentiation strategy and offers memorable experiences. Our recommendation allows Royal Caribbean to maximize its broad differentiation strategy by reaching more cruisers who will utilize the unique services Royal Caribbean offers.

Recommending that Royal Caribbean develop a subscription-based model of offering annual passes means formulating a new department dedicated to this idea, which means new employees, this impacts Royal Caribbean's talent acquisition and human resources. Although Royal Caribbean may promote or hire from within there are still many positions that can be filled which relies on talent acquisition. A new department increases the demand for specialized talent and skills which talent acquisition will have to identify and attract. There will need to be partnerships with currently used staffing agencies to develop the job description and recruitment strategy to achieve the goal of filling this new department. Furthermore, once this talent is recruited human resources will then have to conduct an onboarding process and properly train the recruits. Human resources will also be impacted by this through workforce planning. Ensuring that once these new employees are hired, things are running efficiently, and the department is appropriately staffed. The implementation of a new department relies on careful planning and coordination which impacts Royal Caribbean’s talent and human resources.

If Royal Caribbean decided to undertake our proposed strategy of implementing a subscription model option to their ticket sales, they would easily be able to leverage their sustained competitive advantage of operational efficiency. We can see that their desired outcome is raising profitability, and the high-quality product they are looking to produce is a variety of unique cruising experiences to as many cruisers as possible across the globe. The strategy we have presented would help improve and sustain this already existing competitive advantage by helping boost their Occupancy Rate through coupling their unique ships and cruising experiences with this bargained annual pass.

Occupancy Rate is defined as a ratio of passenger cruise days to available capacity days. Essentially, this is able to give a comparative measure on how efficient a cruise line is with their available inventory in driving revenue from passenger trips. Royal Caribbean's Occupancy Rate across its portfolio is 85.1%. Meanwhile, Carnival sits at 75% and Norwegian at 72.8%, according to the respective companies 10-Ks. Royal Caribbean has a clear core competency in occupancy by achieving a 10% advantage compared to the other biggest holders of market share and closest competitors in the industry. Royal Caribbean's operating model and offering mix are in a sweet spot to not overload the company with overhead expenditure by operating too many while still holding a low enough price to entice consumers.

Utilizing the subscription model we have presented, Royal Caribbean would be able to further strengthen their operational efficiency by providing a creative way to not only save their consumers some money but also incentivize them to spend more time on a Royal Caribbean ship in a given year, whether they were already planning to or not. There are three main consumer groups that this methodology would target to increase our overall number of customers: those who have never cruised before, our current customers, and consumers who may be more loyal or drawn to other cruise lines already. The first group of those who have never cruised before could be targeted with this method mainly by the bargain they could get. The main attraction of this strategy implementation is that it is something that has never been done before by a cruise line, making it by nature creative and incomparable. For all of these consumer groups, this could be perceived as the perfect opportunity to gain more days on a cruise at a discount. Through our analysis of Royal Caribbean's 10k, we found that the average price for 15 days on board would normally cost $2,477.99. Our annual pass would instead offer these 15 days of onboard cruising for a discount of 30% bringing the total price to $1,734.59 **(Model 1-2)**. This unique offering that is not yet offered by any other cruise line would be incredibly attractive to consumers.

Another reason why this offering is attractive to consumers is because of the sheer flexibility of how the deal operates. Offering a package of 15 days total to consumers at one locked-in price, it gives cruisers the ability to plan their vacations and cruising plans around their schedule throughout the year. Cruisers will also have the choice to choose between a variety of cruise lengths and be able to try different ones out to see what they prefer more or less. Especially when speaking in terms of newer cruisers, they may not normally have the ability to experiment with different length cruises to figure out what suits their needs best, and this package provides the perfect opportunity to do so! Also, on the other hand, for more seasoned and experienced cruisers who may already have an idea of the length of the cruise they prefer, this package will allow them to incorporate their preferences into the way in which they choose to best utilize the annual pass. Overall, this subscription-based model allows us to give our consumers more flexibility and freedom when booking with Royal Caribbean which will in turn help strengthen customer loyalty, brand image, and boost our operational efficiency by exceeding the expectations set by our customers thus aligning perfectly with our client's mission statement.

Though there would technically be an incremental loss seen in ticket sales from cruisers that were already planning on cruising with Royal Caribbean for 15+ days in a given year, the incremental gains from new cruisers who would not have cruised as long or at all coupled with the main point of revenue we would gain from the additional onboard purchases exceeds those losses enough to lead us to having a positive internal rate of return of 12.88% and net present value of $29,602,394 for this project. Increasing onboard purchases would be inevitable given that we would be aiming to have more people on the ships for longer periods of time than they would have been if they did not purchase this annual pass in the first place. Upon doing research we found that the average number of days Royal Caribbean customers are on board one of their cruises is approximately 6.33 days in a year. Having a package offering 15 days of cruising in one year at one lump sum price will incentivize our cruisers to cruise longer periods of time than they historically would have without this discounted option. Another area where we would be able to see additional revenue rolling in would be from the demographic of people who purchase this package and do not utilize it to its full extent of 15 days of cruising. This would then be money in Royal Caribbean's pocket that they did not even have to provide service for.

Looking at the future development potential of this annual pass program for Royal Caribbean, there are a variety of ways in which they could embrace their innovative capabilities to continue to grow this program in years to come. This initial launch includes one main annual pass option that would give cruisers the option to have 15 days of cruising in a given year for a price of $1,734.59. However, after the initial launch of this package, there could very well be the creation of different tiers of this package to give cruisers even more options in terms of what type of annual pass they would like to purchase depending on if they would like to obtain more or less days of cruising annually. This being said, the strategy that we have proposed offers a solid foundational starting point for Royal Caribbean to differentiate themselves from every other cruise line in the industry by offering an annual pass not offered anywhere else yet. An annual pass that utilizes their core competency in operational efficiency to further drive revenue without sacrificing their designation as a broad-differentiation company.

Financial Justification of Strategy

When deliberating the financial justification of our strategy we considered various scenarios and assumptions to be made. Through the utilization of cash flow models analyzing the impact of implementing this program over 7 years, we recommend they pursue this project because it is both feasible and profitable. Our model relied on data pulled from the industry, Royal Caribbean's operations, and various assumptions **(Model 1-2)**. It is important to note that all assumptions were projected on the more conservative side of the spectrum to provide more reliability on results. In addition, sensitivity analysis was conducted in order to determine the possibility of risk inherent in the model given current assumptions (**Model 1-4).**. Given the base scenario, the project yields an NPV of $29,602,394 and an IRR of 12.88% **(Model 1-1)** which is higher than the hurdle rate established for this project. The hurdle rate was calculated by conducting an analysis of Royal Caribbean's current weighted average cost of capital, which we have included in the appendix.

According to **Chart 2-1**, the program generates positive cash flows for all future years. For our project an initial outlay of $695,732,250 is required, which is the marketing and software implementation costs associated with pursuing this subscription model. All future years project a cash flow of over $100 million (**Chart 2-1**). This results in a payback period of approximately 5 years (**Chart 2-2**) One aspect of the project that we deliberated on was what the incremental revenue effect would be on onboard purchases and ticket sales. We settled on only calculating the increase we would expect from the subscription sales on our financial statement while subtracting the pre-existing sales that we would have expected given normal conditions. This is demonstrated on **Chart 2-10** and **Chart 2-11.** Our charts are based on the assumption that a portion of current purchasers would have already purchased tickets and received onboard sales regardless of whether they are part of the subscription program. Other considerations were also taken into account that affected total cash flows, such as increased wages, which we calculated to be a minor percentage of current wages, and which resulted in an increase of $5,920,415.

There are several impacts on our financial statements due to the implementation of this program. Through this subscription model, we are selling tickets at a 30% discount compared to current market price **(Chart 2-9)**. However, our assumptions take into account the ability to capture additional revenue in the form of more passenger cruise days. The more time spent on board allows for more onboard purchases to be made by passengers. We estimated that only 80% of the subscription purchase days would be utilized, which is a reasonable estimate when compared to other subscription models **(Royal Caribbean Cruises, 2022)**. The projected subscription purchases translate to increased passenger cruise days. Our team projects passenger cruise days to increase by approximately 1,000,000 in future years **(Chart 2-4)** resulting in Royal Caribbean's occupancy rate increasing 3% over the span of 7 years **(Chart 2-5).**

To conclude, although our model is built on certain assumptions, we have opted for a conservative approach to ensure the reliability of our proposal. We provided a sensitivity analysis in our model that assisted us in determining which metrics were most important (**Model 1-4).** From those metrics, Royal Caribbean should be able to measure the success of the implementation of our project and decide if it is beneficial to the company. The most important metric to note is the number of subscription purchases. Based on our research, we decided on utilizing a very conservative amount of 2% in our model, although the industry shows a more optimistic projection of 15% **(Royal Caribbean Cruises, 2022)**. For a comprehensive list of all assumptions, see **Model 1-2** which takes into account all the inputs for the model. Ultimately, given that the implementation of our project yields a positive NPV and an IRR of 12.88%, which is greater than our established hurdle rate calculated by Royal Caribbean's weighted average cost of capital **(Model 1-3)**, we arrived at the conclusion that they should pursue this project.

Fall-out and Summary

Implementing a subscription-model into an industry which primarily relied on travel agents is going to be tricky. We not only have to consider what Royal Caribbea's competitors will do but how these midpoint buyers will react.

In our model, we did not account for paying commissions on referrals to the annual pass from travel agents. We opted for a seemingly cheaper option of utilizing a new internal department to manage subscriptions. This could go wrong in two ways: (1) the new department is inefficient and becomes costly to maintain or (2) we rely on travel agents to push the pass and they don't since they won't see commission. We'd recommend responding to situation one by either increasing training for the department or cutting it. For situation two, we'd recommend laying out a referral structure where agents earn a percentage of fares for annual pass referrals. This could be offset by a slight increase in the pricing over time.

As for competitors, we believe they will try to emulate the model as they see it working over time. We would not suggest stressing over this because they're not adequately competent at handling too much greater of an increase in capacity. In fact, we believe their adoption of the model will drive greater Market Share for us in the long run. An interesting response from Norwegian may be to not offer annual passes so as to seem more distinct and distinguished which may help their positioning in the market. We think this is a relatively natural and trivial adjustment in brand perception. There are additional costs not captured which may be incurred such as a greater cost of accounting and finance departments working on these new procedures.

Appendix

Chart 1-1: Strategic Group Map (Occupancy Rate)

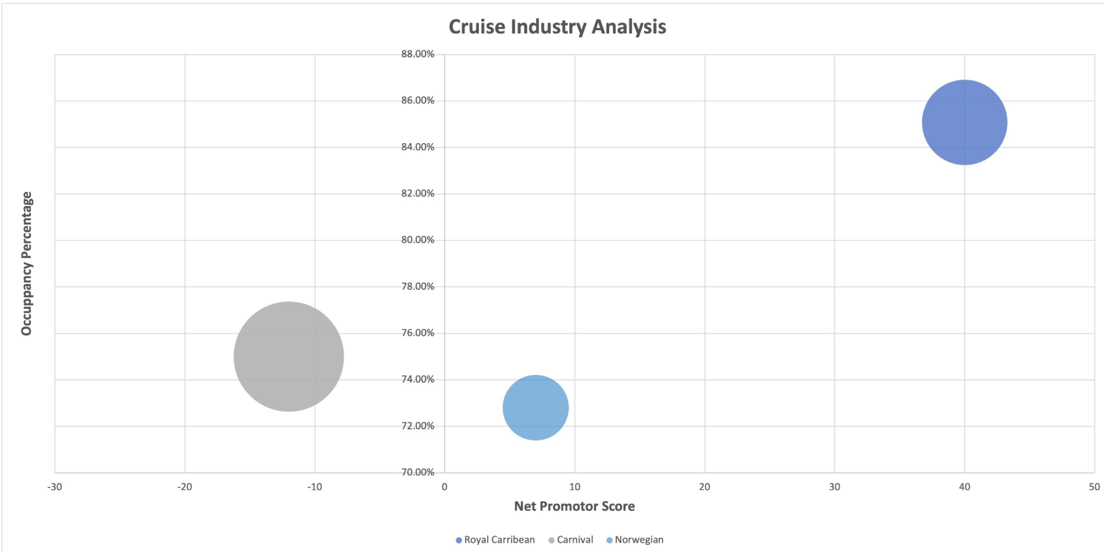


Chart 1-2: Strategic Group Map (Average Passenger Days)

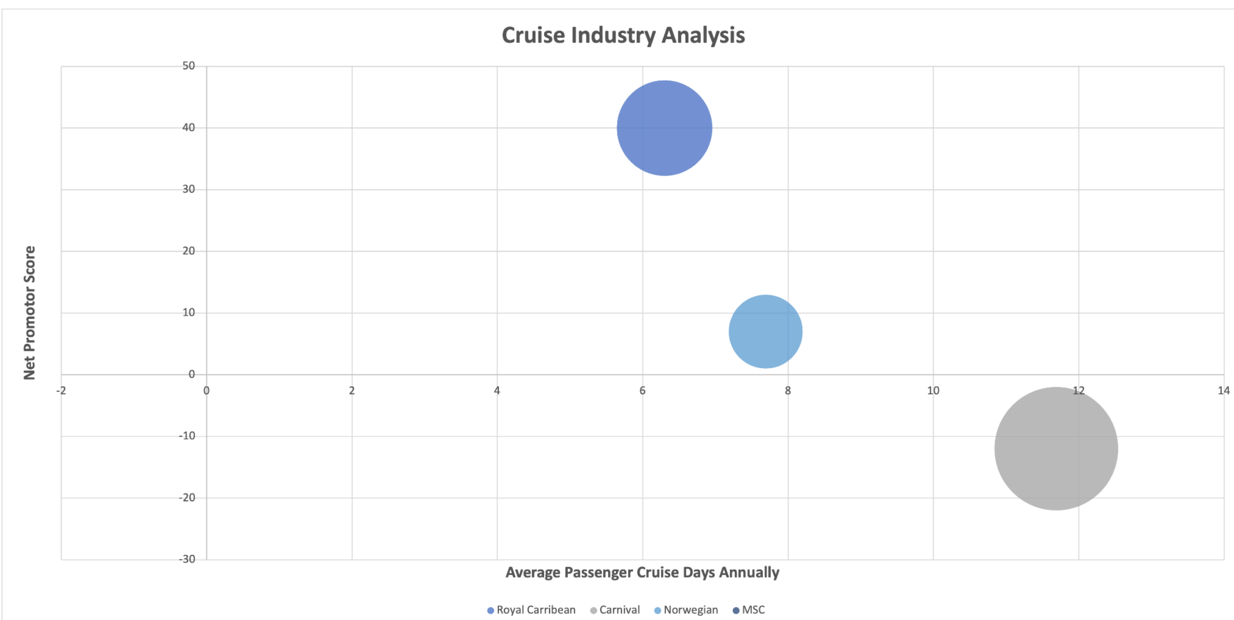


Chart 1-3: Strategic Map for Industry Positioning

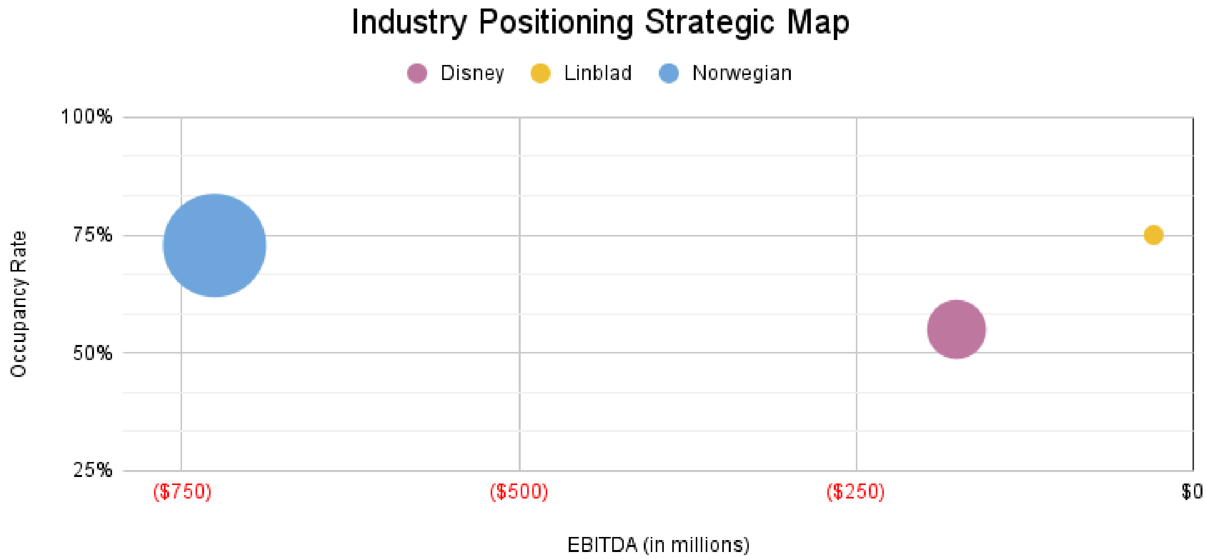


Chart 2-1: Yearly Cash Flows (in dollars)

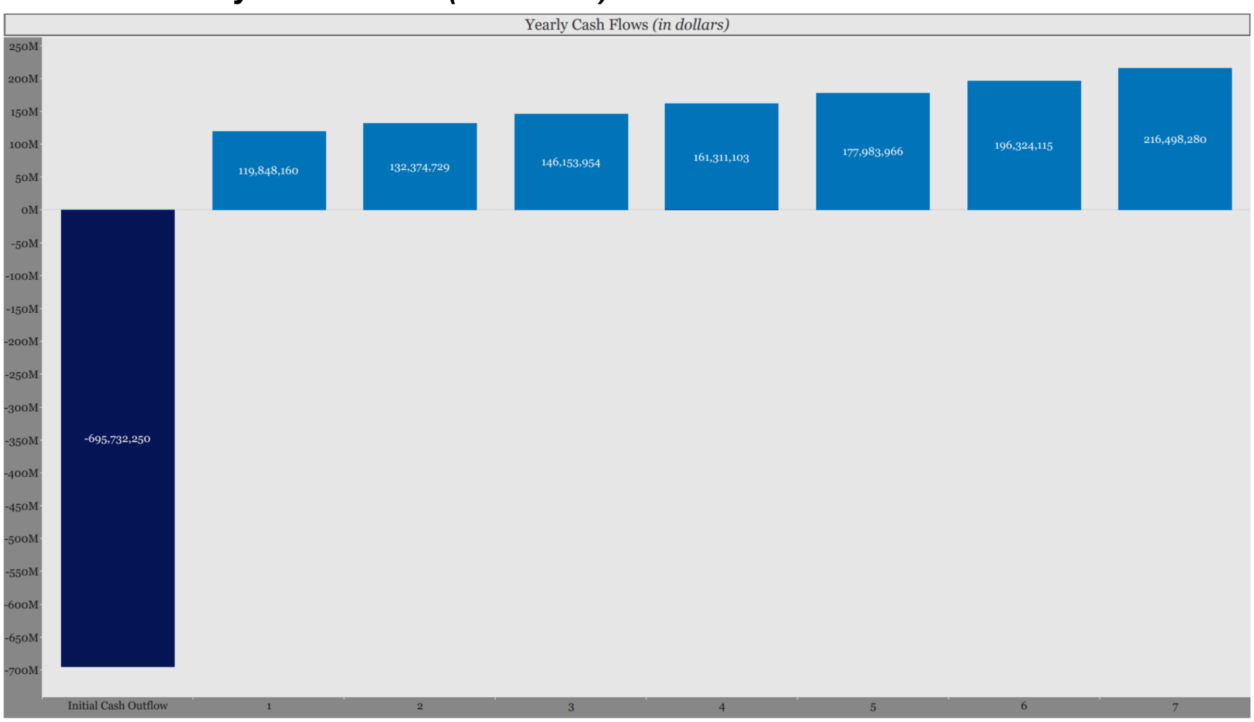


Chart 2-2: Cumulative Cash Flows (in dollars)

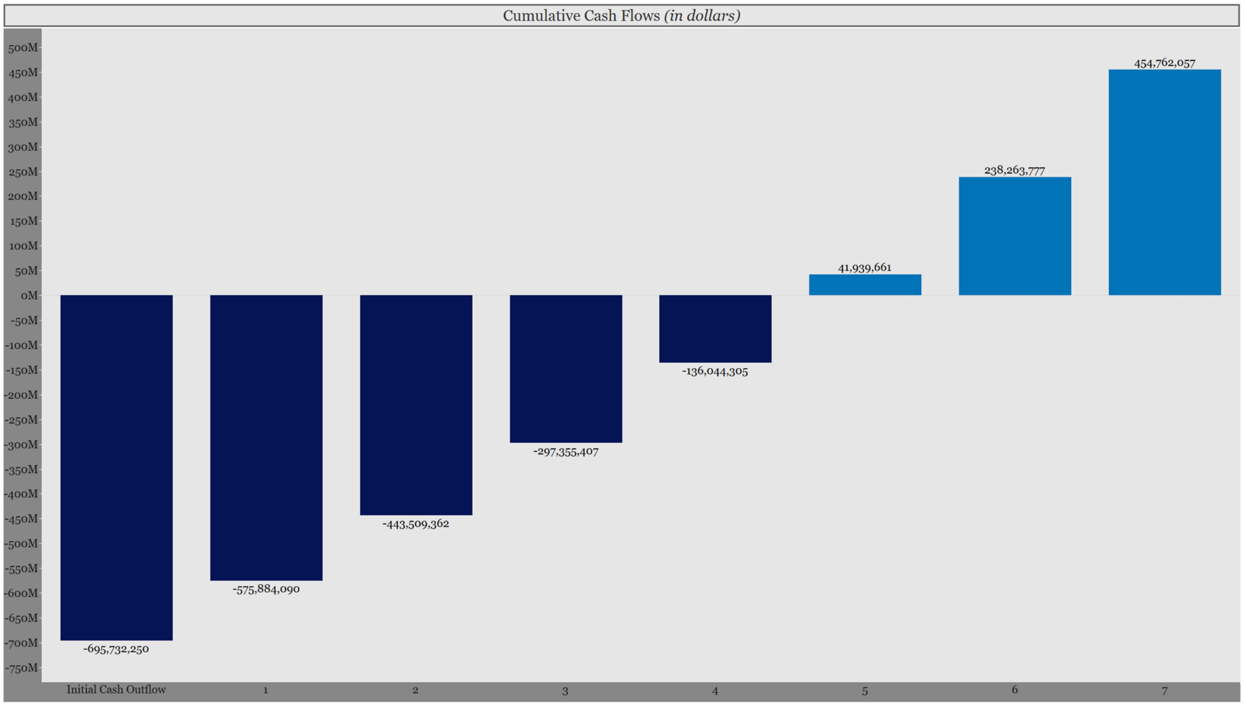


Chart 2-3: Projected Subscription Purchases

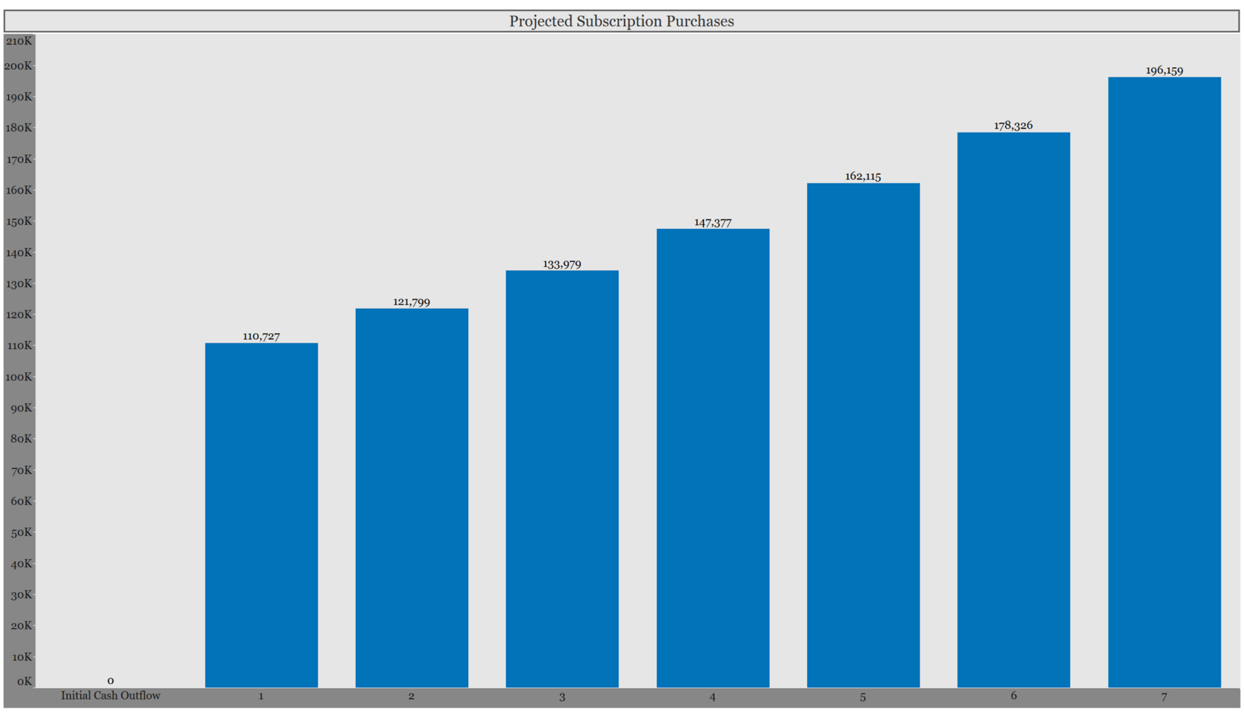


Chart 2-4: Projected Passenger Cruise Day Increase

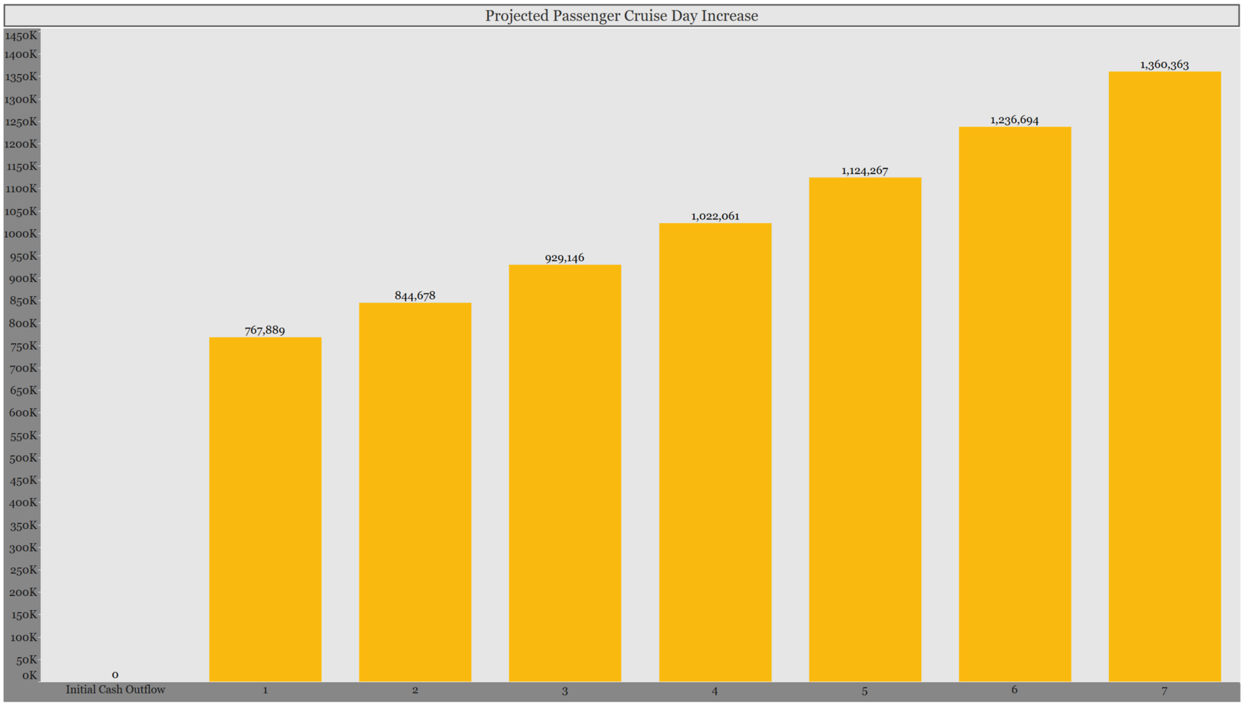


Chart 2-5: Projected Occupancy Rate

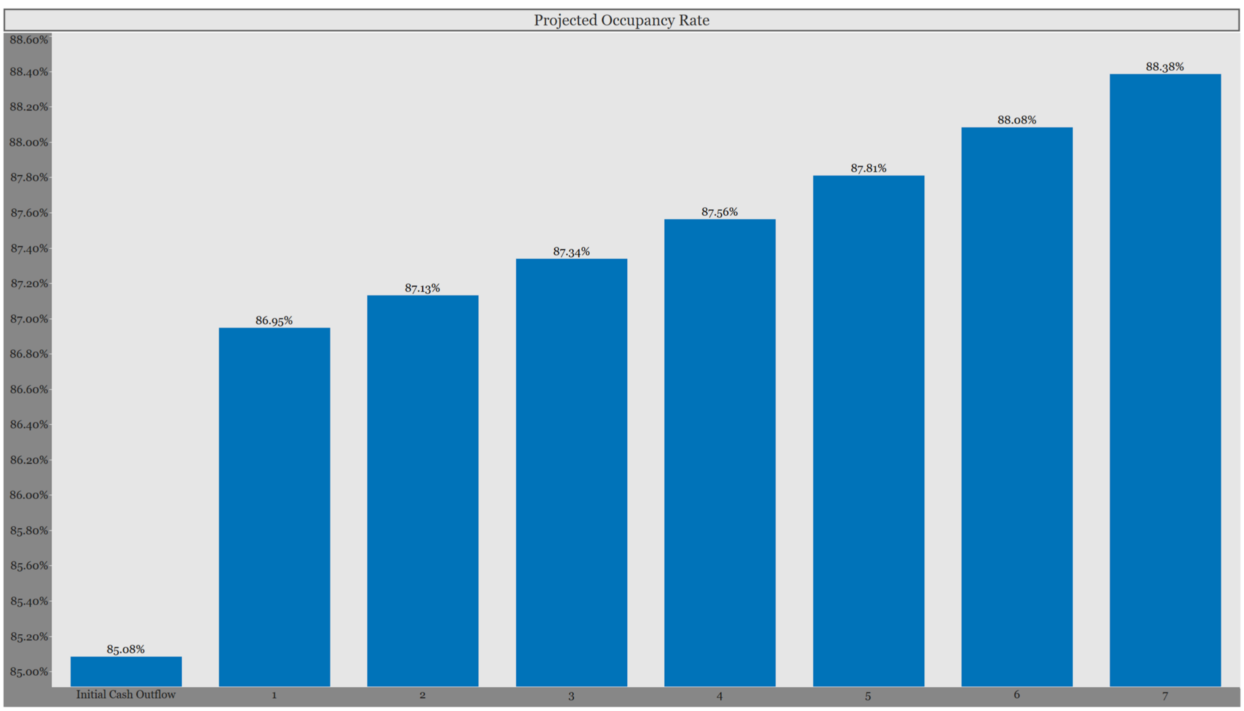


Chart 2-6: Royal Caribbean Revenue Distribution Percentage

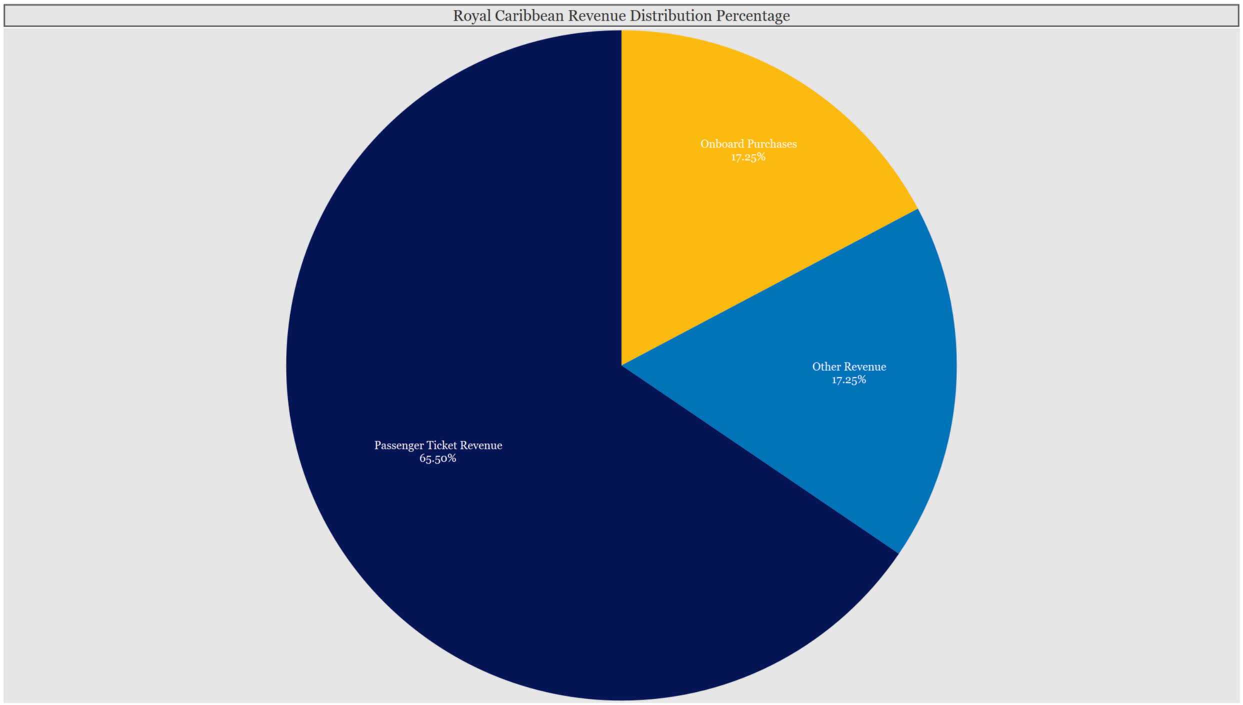


Chart 2-7: Total Revenue Breakout Per Passenger (in dollars)

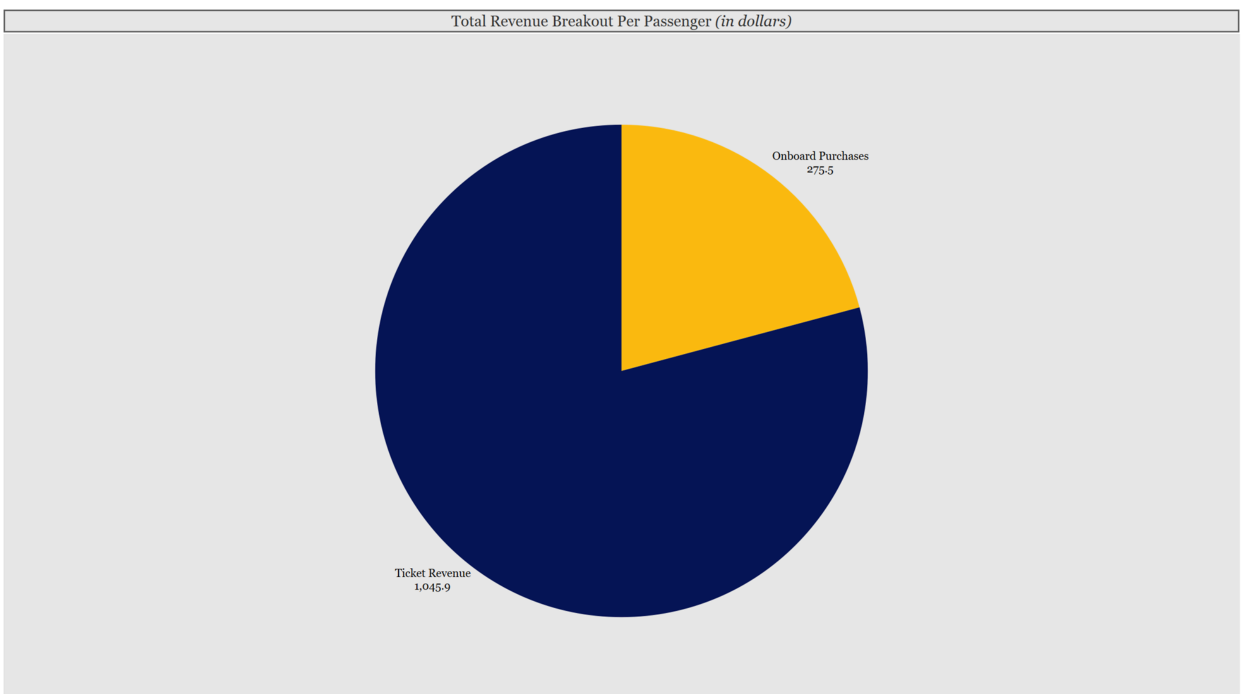


Chart 2-8: Total Revenue Breakout Per Passenger Per Day (in dollars)

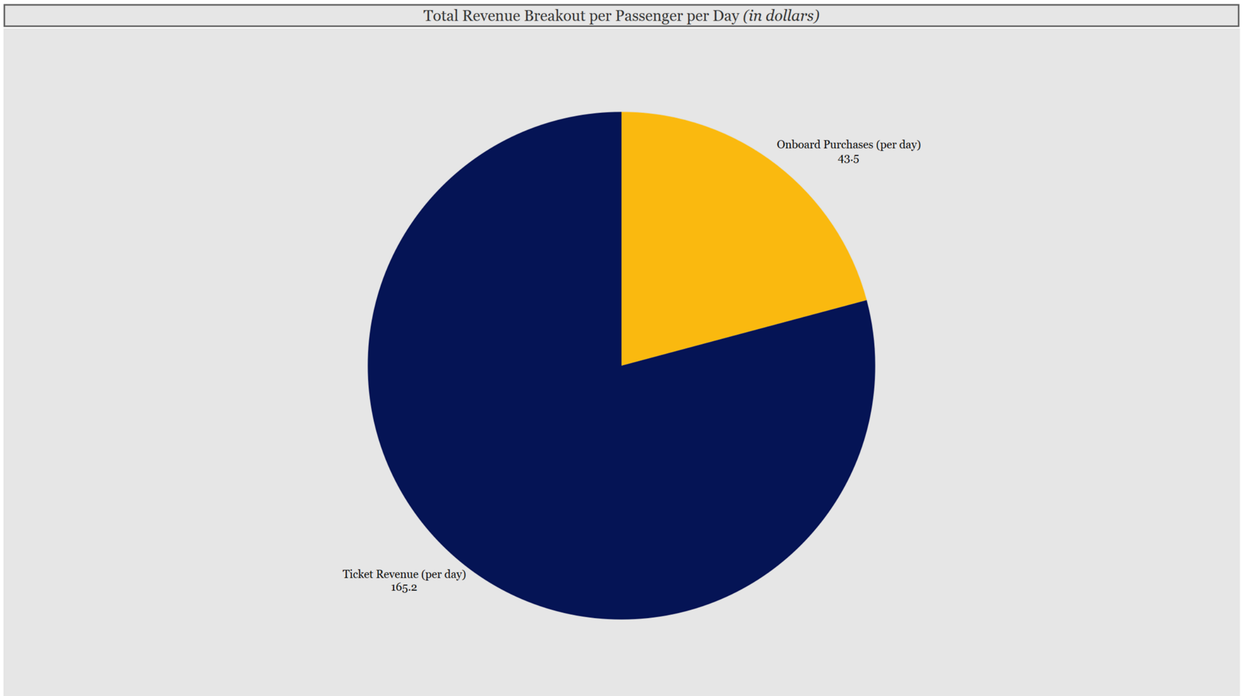


Chart 2-9: Subscription Price vs Market Price (in dollars)

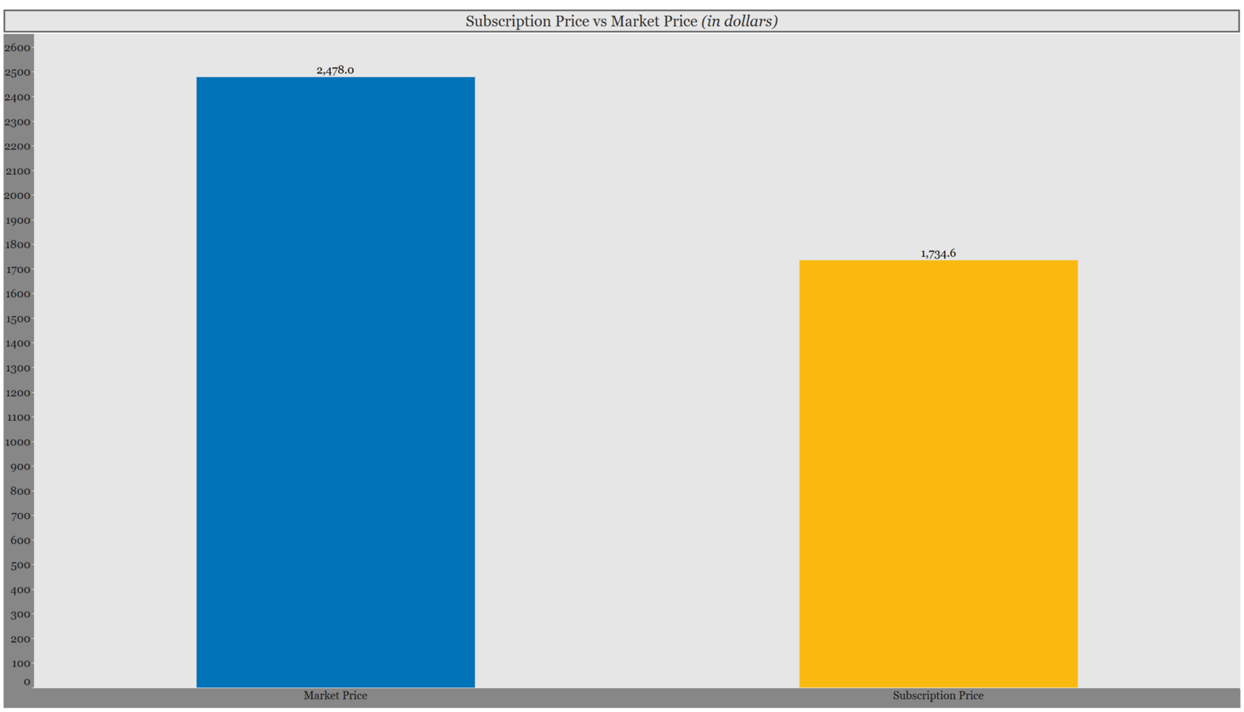


Chart 2-10: Incremental Ticket Sales Revenue (in dollars)

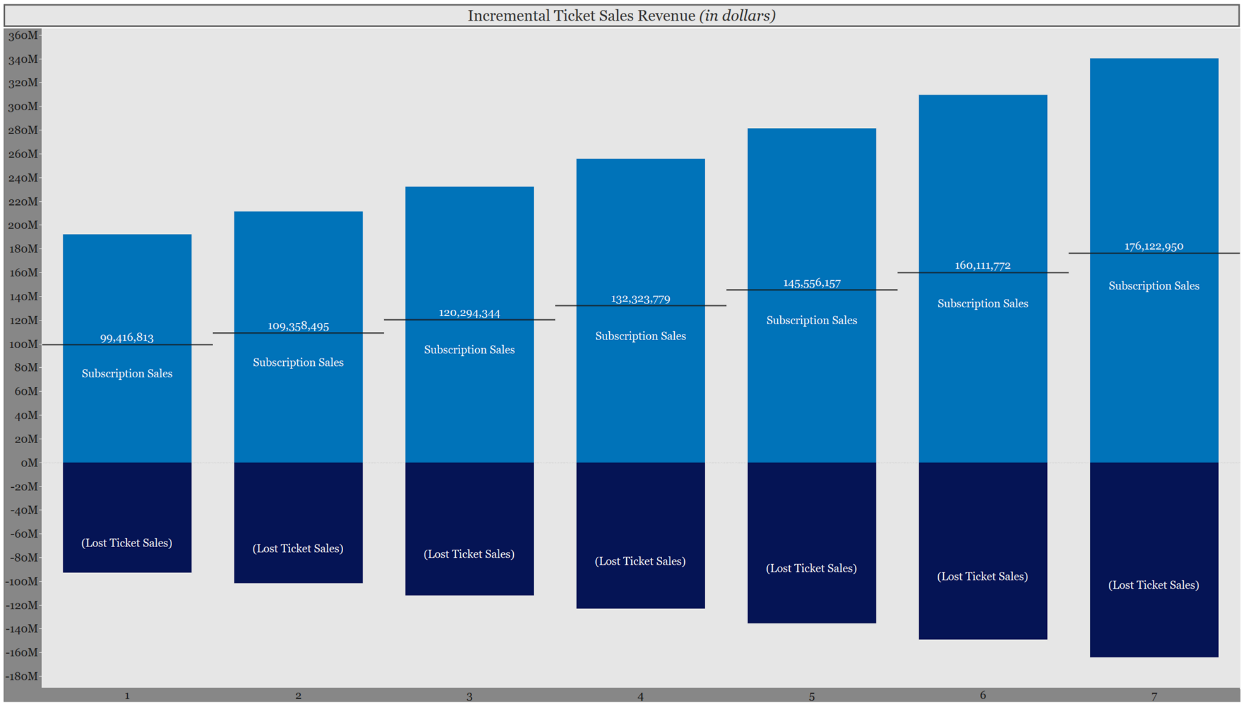
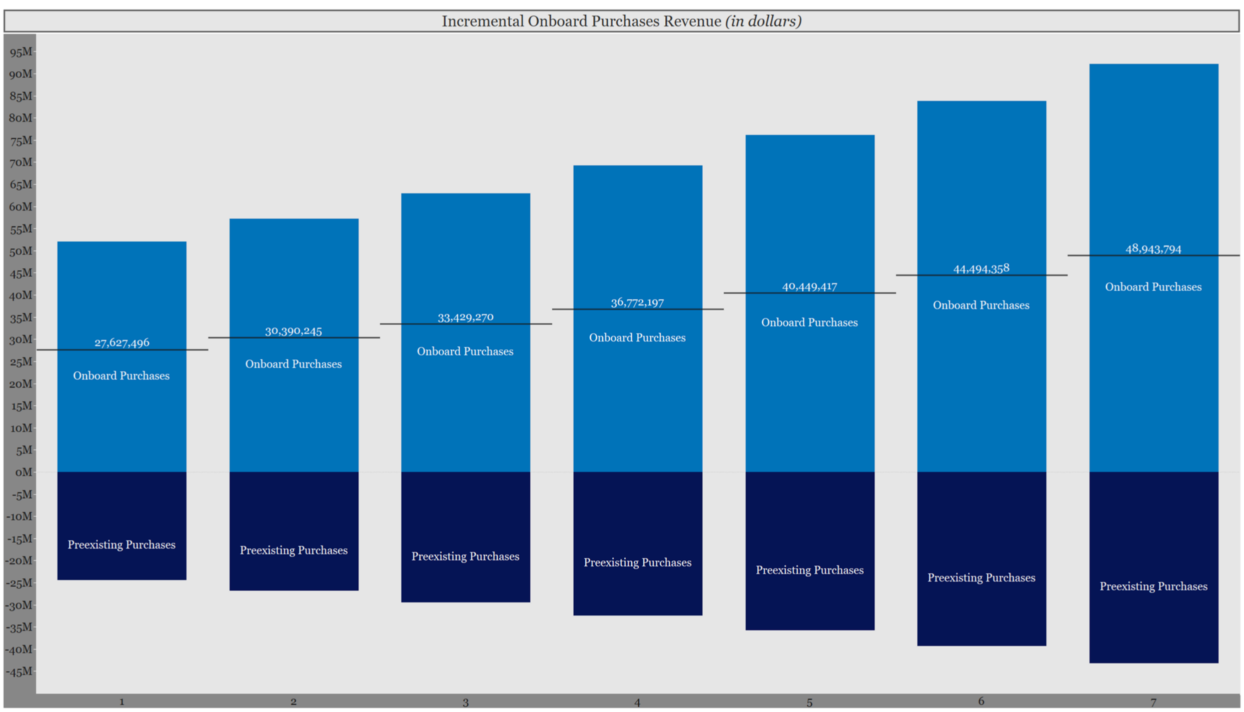


Chart 2-11: Incremental Onboard Purchases Revenue (in dollars)



Model 1-1: Financial Model

	Initial Cash Outflow	*Year 1*	*Year 2*	*Year 3*	*Year 4*	*Year 5*	*Year 6*	*Year 7*
Marketing / Advertising Spend	$ (395,732,250)	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Software Implementation	(300,000,000)	-	-	-	-	-	-	-
Subtotal Initial Costs	*(695,732,250)*	-	-	-	-	-	-	-
Subscription Sales	-	192,065,673	211,272,240	232,399,464	255,639,410	281,203,351	309,323,687	340,256,055
Onboard Purchases	-	52,027,386	57,230,125	62,953,137	69,248,451	76,173,296	83,790,626	92,169,688
(Lost Ticket Sales)	-	(92,648,859)	(101,913,745)	(112,105,120)	(123,315,632)	(135,647,195)	(149,211,914)	(164,133,106)
(Preexisting Onboard Purchases)	-	(24,399,890)	(26,839,879)	(29,523,867)	(32,476,254)	(35,723,880)	(39,296,267)	(43,225,894)
(Increased Wages)	-	(5,920,415)	(5,920,415)	(5,920,415)	(5,920,415)	(5,920,415)	(5,920,415)	(5,920,415)
(Amortization on Software)	-	(30,000,000)	(30,000,000)	(30,000,000)	(30,000,000)	(30,000,000)	(30,000,000)	(30,000,000)
Earnings before Tax	-	*91,123,894*	*103,828,325*	*117,803,199*	*133,175,561*	*150,085,158*	*168,685,715*	*189,146,329*
Taxes	-	1,275,735	1,453,597	1,649,245	1,864,458	2,101,192	2,361,600	2,648,049
Net Income	-	*89,848,160*	*102,374,729*	*116,153,954*	*131,311,103*	*147,983,966*	*166,324,115*	*186,498,280*
Add back Amortization	-	30,000,000	30,000,000	30,000,000	30,000,000	30,000,000	30,000,000	30,000,000
Subtotal Cash Income	-	*119,848,160*	*132,374,729*	*146,153,954*	*161,311,103*	*177,983,966*	*196,324,115*	*216,498,280*
Total Cash Flows	$ (695,732,250)	$ 119,848,160	$ 132,374,729	$ 146,153,954	$ 161,311,103	$ 177,983,966	$ 196,324,115	$ 216,498,280
Cumulative CashFlows	$ (695,732,250)	(575,884,090)	(443,509,362)	(297,355,407)	(136,044,305)	41,939,661	238,263,777	454,762,057
Subscription Purchases	-	110,727	121,799	133,979	147,377	162,115	178,326	196,159
Passenger Cruise Days Increase	-	767,889	844,678	929,146	1,022,061	1,124,267	1,236,694	1,360,363
Projected Occupancy Rate	85.08%	86.95%	87.13%	87.34%	87.56%	87.81%	88.08%	88.38%

NPV	$ 29,602,394
IRR	12.88%
Payback Period (rounded to the year)	5

Model 1-2: Assumptions & Important Inputs

Royal Caribbean Cruise Financial Information		
Passengers Carried	5,536,335	RC 10k
Passenger Cruise Days	35,051,935	RC 10k
Available Passenger Cruise Days	41,197,650	RC 10k
Occupancy Rate	85.08%	
Average Cruise Time per Passenger	6.33 Days	
Total Revenue	$ 8,840,540,000	RC 10k
Total Revenue per Customer	$ 1,596.82	
Total Ticket Revenue per Customer	$ 1,045.92	
Total Onboard Purchases Revenue per Customer	$ 275.45	
Per Day Ticket Revenue per Customer	$ 165.20	
Per Day Onboard Purchases Revenue per Customer	$ 43.51	
Passenger Ticket Revenue %	65.50%	RC 10k
Onboard and Other Revenues %	34.50%	RC 10k
% of Onboard Purchases in Other Revenue	50.00%	
Onboard Purchases % Estimate	17.25%	
Other Revenue (Excluding Onboard Purchases) %	17.25%	
Passenger Ticket Revenue Amount	$ 5,790,553,700	
Onboard and Other Revenue Amount	$ 3,049,986,300	
Onboard Purchases Amount	$ 1,524,993,150	
Other Revenue Amount (Excluding Onboard Purchases)	$ 1,524,993,150	

Marketing / Advertising Spend		
Current Marketing Budget per RC 10k	1,582,929,000	RC 10k
% of Current Budget for Proposal	25%	
$ Amount for Proposal	395,732,250	

Software Implementation	
Software Implementation Total Cost	300,000,000
Useful Life	10 Years
Yearly amortization under straight-line method	30,000,000

Subscription Price + Package	
Days Offered	15 Days
Market Price	$ 2,477.99
Subscr. Discount	30%
Subsc. Price	$ 1,734.59
Onboard Discount	10%

Subscription Purchases + Usage	
% of Pass. Carried	2.00%
Initial Subscr. Purch.	110,727
Growth % of Purch.	10%
Ave Subscr. Use	80%
% Old Customers	80%
% New Customers	20%

Increased Wages Calculation		
Current Wages Exp.	1,184,083,000	RC 10k
% Increase	0.50%	
Wages Increase $	5,920,415	

Tax Rate and WACC		
Tax Rate	1.40%	https://cruiseradio.net/fact-check-do-cruise-lines-pay-us-taxes/
WACC	11.69%	

Model 1-3: WACC

WACC Calculation				
Nominal Risk-free Rate	5.00%			
Expected Risk Premium for the Market	4.75%			
Long-term Debt				
S&P Credit Rating	BB-	https://bondblox.com/news/royal-caribbean-upgraded-to-bb-by-sp		
Credit Spread	2.35%	Credit Table		
Required Rate of Return	7.35%			
Tax Rate	20.00%			
Tax-adjusted Required Rate of Return	5.88%			
Common Equity				
Market Beta	2.46	https://finance.yahoo.com/quote/RCL/		
Required Rate of Return	16.69%			
Source of Funds	*Value*	*Weight*	*RRR*	
Long-term Liabilities	22,334,085,000	46.22%	5.88%	RC 10k
Common Equity	25,988,454,450	53.78%	16.69%	RC 10k
Total Capital	48,322,539,450	100.00%		
WACC			11.69%	
Share price	*101.73*	https://finance.yahoo.com/quote/RCL/		
Shares outstanding (millions)	255,465,000	https://finance.yahoo.com/quote/RCL/		

Model 1-4: Sensitivity Analysis

Sensitivity Analysis

Scenarios	*Base*	*+/-*	*Low IRR*	*High IRR*
Base Case	12.88%			
% of Passenger's Carried	2%	0.5%	4.86%	19.95%
Growth % of Subscription Purchases	10%	5%	8.92%	16.79%
Marketing / Advertising Spend %	25%	5%	9.85%	16.48%
Onboard Discount	10%	5%	12.20%	13.56%
Subscription Discount	30%	10%	6.03%	12.88%
Tax Rate	1.4%	5%	11.68%	N/A

Model 1-5: Credit Spread

Reuters Corporate Spreads for Industrials*

Rating	1 yr	2 yr	3 yr	5 yr	7 yr	10 yr	30 yr
Aaa/AAA	5	10	15	20	25	33	60
Aa1/AA+	10	15	20	30	35	42	66
Aa2/AA	15	25	30	35	44	52	71
Aa3/AA-	20	30	35	45	52	59	78
A1/A+	25	35	40	50	55	65	85
A2/A	35	44	55	60	65	73	90
A3/A-	45	59	68	75	80	89	110
Baa1/BBB+	55	65	80	90	94	104	123
Baa2/BBB	60	75	100	105	112	122	143
Baa3/BBB-	75	90	110	115	124	140	173
Ba1/BB+	115	125	140	170	180	210	235
Ba2/BB	140	180	210	205	210	250	300
Ba3/BB-	165	200	230	235	235	270	320
B1/B+	190	215	250	250	275	335	360
B2/B	215	220	260	300	315	350	450
B3/B-	265	310	350	400	435	480	525
Caa/CCC	1125	1225	1250	1200	1200	1275	1400

*100 basis points equal 1 percentage point.

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