

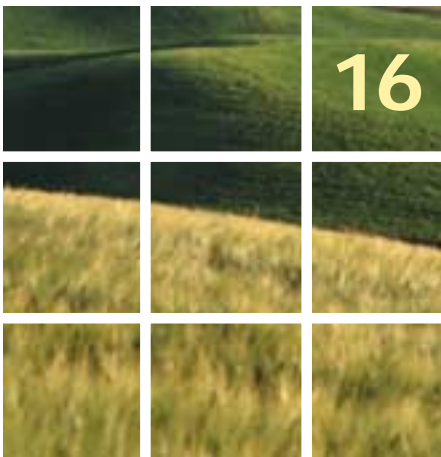


As hospitality industry executives continue to struggle with their traditional growth and development strategies in today's unforgiving capital markets, it is worth considering the value of strategic alliance partnering as a model that can add significantly to shareholder value. Over the years, we have witnessed the ups and downs of the hospitality business cycle and the alternating currents of investor sentiment as it relates to the

represented only five percent of total market value. In the 20 years to 1998, however, they had skyrocketed to 72 percent! And while there has certainly be plenty of downward adjustment to market caps for many "New Economy" companies over the last year or two, one reality remains—that the value of intangible assets, most particularly relationships, distinguishes the winning companies from the losers. Our research further

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Strategic Alliance Partnering in Hospitality



industry. And in the past, some industry executives have tried to time their real estate asset plays to coincide with these cycles, although they invariably get the timing wrong. In fact, for those who have tried and so frequently paid for the consequences, they hardly need to be reminded of that axiom of the modern era—that "timing is everything."

In the meantime, for those dedicated to long term investing, these notions of the cyclical buying and selling of physical assets are generally disclaimed. They are focused on the values that contribute to the business—their employee and customer relationships, their brands, the knowledge they are accumulating and the technologies they use. Most of these values, however, never show up on the balance sheet. But we do not have look far for proof of the reality. The public markets provide us with the data. According to an Andersen survey of over 10,000 publicly quoted companies, there has in fact been a steady decline in the ratio of book to market value. In the late 1970s's, non-book values (the intangibles that do not appear on the balance sheet)

proved that asset-intensive companies happen to produce the lowest returns over the long term—one fifth the return of the least asset intensive group.

What might all of this mean for our industry's hospitality businesses? It suggests that a new business model is required, particularly for those still playing the game using the old rules of engagement. As in all businesses, there appear to be five key strategies that tend to contribute to value creation:

1. expansion into new product or services;
2. leveraging one's own resources or those of others;
3. moving from physical products to intellectual ones;
4. adding new technologies and processes to connect and scale assets; and
5. expanding access to assets through partners and additional channels.

Much has been written about the first four of these, but it is to the fifth—that of allying with others to broaden and expand access—that I turn to here. To



strategic alliances and what they mean for the hospitality industry. The premise—that it is only through such alliances that this tradition-bound sector can truly capitalize on all of its assets—its geography, its vast customer and employee connections, its brand loyalties and its knowledge capital.

For an industry that grew up in the real estate context, constructing buildings and accommodating guests, the value of “hospitality” has traditionally been driven by the cash flows generated by hotel property. We had a geo-centric focus, a “zip code mentality” if you like. Building a hotel chain was all about putting dots on maps and if you could build a brand while doing it, so much the better providing you had the critical mass to support it. But for many organizations today, and not just those in the hospitality industry, building critical mass is not that easy. Especially if at the end of the day, it is all about the customer. Why so? Because customers are not easy targets. They are hard to define, tough to track, difficult to understand and frequently nearly impossible to access, at least on a comprehensive and consistent basis. And they are this way because in a networked world, the array of different relationships grows more complicated every day. The traditional barriers to market: time, distance and the physical are all disappearing. And as they do, new organizations are emerging that are disintermediating all of the traditional relationships.

Realizing that a business organization cannot be all things to all people, smart CEOs these days are focused on how they can leverage their organization’s core competencies. And in the process, they are outsourcing the functions best performed by others. They are also growing their businesses through strategic alliances that allow them to either reach more customers with their existing products and services or deliver new products and services to both their existing customers and the new ones

brought by their strategic alliance partners. This is the world of the networked business—the future world of hospitality.

What makes a good alliance?

There are a number of factors to consider in forging an alliance with another organization, the most obvious of which relate to revenue enhancement and costs savings. Alliances should at least be doing one or the other. On the revenue



enhancement side, an alliance needs to bring new customers to your existing products and services or the reverse—providing your customers with access to additional products and services, thereby enhancing their experience with your organization. There needs to be a compatibility of positioning—is the positioning of the alliance partner in sync with yours? Is the demographic and positioning of its customer base also aligned with yours? Are your products and services relevant to your partner’s customers or its to yours? How will the alliance enhance your customer relationships? How will it add to your value proposition? How will it add value to your brand, if you have one? And on the cost

side, are the potential savings worth the effort? Have you made the business case? Have you tested the premise? Outsourcing non-core functions, focusing on core competencies, staying on strategy and sticking to one’s knitting have become the mantras of many in business. How does the alliance contribute when measured against these goals?

Alliances in hospitality

From “preferred vendor” programs to marketing alliances with travel companies and upscale retailers, from sponsorships with sports organizations to alliances with technology and capital providers, hospitality companies are trying them all. But are such alliances delivering as promised?—undoubtedly to varying degrees. Some have been clear success stories, others either hardly worth the effort or worse, failures that sidetrack management and actually cost hard earned money. On balance, however, strategic alliances are helping to expand the scope and reach of many companies in the industry and are here to stay.

For some alliances, it is not only the more immediate benefits of access to customers, products and services but also to the partner’s other alliance partnerships. A partner’s partner can be just as important as the partner itself. In this view, it is the synergy of the network that also contributes to value. And in the web-enabled networked world that we live in today, this is as we would expect it to be.

Alliances are also about leverage. Many hospitality companies confronting the need for market presence, for marketing infrastructure and for IT have had to deal with the reality that they cannot possibly get there alone, wherever “there” is. They thus must turn to others that can help. To alliance partners in a variety of fields whether they provide access to new markets or provide the infrastructure to run the business.



Aligning your CRM

In an increasingly networked world, the cost of interaction between people and organizations is declining rapidly. Because of this, some analysts believe that the most successful companies of the future will be those that specialize in one but not more than one of three critical business functions: product innovation, customer relationship management (“CRM”) and infrastructure. If this is the case, then we can expect our most successful hospitality businesses to increasingly turn to others in the future to provide them with what they need to succeed. CRM should clearly prevail as the element of choice for those in the business of identifying, serving and retaining customers, while their alliance partnerships will provide the rest.

A significant portion of the “rest” will probably revolve around technology as hospitality companies increasingly rely on third parties to deliver the IT platforms they need to deliver against their customers’ expectations. As always, they will need to ensure they have thought through the strategy and have organized accordingly. But as the industry’s most recent foray into high-speed internet access suggests, there will be some false steps along the way. With a presumption of customer need and the customer’s own willingness to pay for it, many hospitality companies forging various types of alliances, have invested in high speed in-room internet access to find a business model that has failed to deliver. But such outcomes should not inhibit alliance initiatives in the future, especially those that have been well-planned and fill a real need.

Such a need might for example be fulfilled in addressing a particular customer segment or demographic group or in providing an easier method for customers to customize and package their travel. In pulling together a strategic alliance in any of these contexts, however, it is critical to clearly define what

each “partner” expects to get out of the relationship, to communicate clearly and frequently and to try to look at the relationship as one of partnership. In this manner, the respective organizations will take the relationship more seriously and invest in it accordingly.

Capital partners

For many hospitality companies, strategic alliances have involved an alignment of marketing interests. There are, however, a

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number of others that involve capital providers. In these cases, the hospitality organization has typically needed an established and reliable source of capital to grow and on the other side, an entity keen to invest in the sector but concerned about the business risk associated with management and marketing. There are numerous examples of such strategic alliances, some of which have been largely successful and produced growth opportunity and excellent returns, while for others the objectives have not been met, at least not in the way originally intended.

Alliances in procurement and distribution

In the e-Commerce world, we have also recently seen the concept of togetherness taken one step further—bringing major competitors together to co-invest in e-Procurement platforms and efforts (somewhat stalled at present) in attempting to pull together consortia for the distribution of inventory through jointly owned and managed travel portals. In both these worlds (e-Procurement and e-Distribution) there is clearly a great opportunity for hospitality companies to

expand their network of relationships and broaden their sphere of influence. How far this is taken and what it will produce in terms of cost and benefit remain to be seen, but for many it may eventually well be worth the effort.

Alliances—a useful step to partnership

For some businesses, a strategic alliance is the first step in a potentially more involved relationship such as a joint

venture. Here the risks and rewards are more significant and the steps towards such relationships thus taken more cautiously. A strategic alliance as a precursor to a more involved relationship is often a great way for two organizations to get to know each other. And when one considers the barriers to successful merger and integration, not the least of which are conflicting cultures and resistance to change, an alliance can be an excellent way of mitigating these risks before a more formal knot is tied.

For multi-branded hospitality companies, there is always the issue of how to leverage the underlying opportunities across brands and their associated customer groupings. An alliance with a third party can often facilitate this where internally, there may otherwise be tough barriers to overcome. Finding that common ground, where a broader set of customer needs across several brands can be satisfied, should produce significant incremental benefits. And for franchisors looking for a preference with vendors, the need is to identify those relationships that provide lower cost access for vendors, enhanced revenues or reduced operating expenses for



franchisees and profits for the franchisor—a triangulated strategy that requires careful planning and execution.

In the end, perhaps the most important factor contributing to successful strategic alliance partnering is the alignment of each party’s objectives. Without such alignment, an alliance that looks good on paper might survive the early honeymoon period when the enthusiasm is high on both sides but may not stand the test of

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time when the results on the ground must be delivered on a consistent basis.

Choosing the right relationship

Beyond the compatibility of interests and the alignment of objectives, another factor that can become quite significant particularly in the technology arena is the staying power of the partner. If your company is growing rapidly and needs a partner to be there through that period of growth, you cannot afford to have an alliance with an organization that is unable to scale its solutions to your changing size. And associated with scalability, reliability—a partner that is there when needed, can respond rapidly to changes in the market and can support you in that “hour of need”. Backing a startup that does not have a proven track record may appear like a sound strategy in the heat of the technology “flash-point”, but looks less sensible when the dust has settled, the competitive landscape is clearer and your solutions are neither robust nor ready. And if the off-loading of risk, whether it be technological or financial, to a relatively weak partner may again have appeal initially, it will hardly be a solution for the long term.

Compatibility of interests between partners also extends to the need for products and services that are within the realm of the company’s marketing core and its related competencies. They must not be so far removed that too much effort has to be expended matching the new products and services with the real marketing opportunities. This can easily happen when marketing executives get carried away with the concept of owning

the customer relationship. Such ownership of course, has to be earned—it is not a customer given right. Unfortunately, fickleness and disloyalty come quite naturally to many customers and they thus require very careful nurturing if they are to find resonance and value with the new product and service offerings proffered by their favorite hospitality company.

And while most hospitality companies of size have relationships with travel organizations such as the airlines, American Express and the like, there is still competitive advantage to be gained in alliances with others—particularly those that can bring something unique that establishes a point of differentiation. For hospitality companies that have invested fortunes in loyalty programs, there is also value in tying up with other branded companies in related fields where a program of points can for example, be cross-promoted in the context of the partner’s marketing programs. And in a consolidating industry where there is also convergence with other sectors, one to keep an eye on is entertainment. Here there may be some very interesting opportunities for hospitality companies to expand their sphere of

influence if they approach it strategically and organize accordingly.

Alliances across borders

Most foreign hospitality companies that have in the past attempted to expand into the US market have found great difficulty in establishing an identity here without buying into an established brand. The profusion of brands in the US, the huge size of the market and the high costs to establish critical mass are some of the obstacles they have faced. And when US companies take their expansion plans overseas, they too have had great difficulty in establishing mass especially in Europe and Asia/Pac where there are so many different markets and cultures to cover. Franchising for US companies has hardly been a success overseas and management contract strategies of limited potential in environments where owners expect their hotel “partners” to either invest or lease with corporate guarantees. For hospitality companies facing this challenge of cross-border expansion, strategic alliance partnering may also well be the answer.



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