# Consulting report of solberri hotel

Business

Solberri Hotel January 20 2012 This report is in response to the request by Solberri hotel group for a review of its facing issues and identification of possible solutions. Consulting report ? STATE OF AFFAIRS Solberri is a group of resort hotels registered as a listed company with 12 resort hotels in Europe. Established in the 1980s, it had run successfully until 2003 and also incurred losses in 2005 and 2006. To improve the situation, Solberri implemented strategy changes to the hotel operatingenvironmentsuch as the pricing changes and a refurbishment program.

With these adjustments, situation gets better with a large forecast cash surplus in this financial year. Currently the chain of hotels is faced with critical issues revolving around its operation including human resources that are better explained with the help of SWOT analysis in Appendix 1. It is important for Solberri to make use of the management tools to understand the current situation and to achieve the revenue target, increased share holder value and better customer satisfaction. ? ISSUES IN HAND Solberri is faced with multiple issues that act as a barrier to meet theirgoalsand target.

From our review and understanding of the environment we put forth the below issues and rank them as priority and other issues. Priority issues: •Poor customer experience that could be a result of ethical issues such as oPoor treatment of General manages and senior employees. oMisdistribution of tips oInvestment in unprofitable environmentally friendly initiatives. •The potential need to borrowmoneyto enhance spas before the 2007/08 Peak season •The need to raise occupancy rates and earnings generated from extra charges to hit the planned revenue for the financial year ending September 2008 •The poor share price and vulnerability of Solberri

Other issues: •Installation of solar panels •Non-participation in the international star ratings system •Potential problems with the quality of outsourced services •Upgrading website to include a virtual tour of facilities . ? ISSUE ANALYSIS In this section, the analysis is done for top priority issues. Customer service and relevant HR issues. The quality of customer service is crucial to companies' survival in service industry. Unfortunately, the service provided by Solberri failed to meet the expected standard of its customers.

The main reason for poor customer service is employees' lack of skills andmotivation. The majority of Solberri employees are temporary, with limited knowledge of the hotel industry and relevant skills. Besides, all short-term employees only receive two days introduction training which is apparently insufficient. The customer service can be improved in two aspects. In the short term, Nick Silva, customer service Director, needs to review staffing level immediately to meet the upcoming demand. Strict selection and a specific regular training program are needed to ensure the quality of its employees.

In the long term, adjusting the ratio of the number of long-term employees to that of short-term ones is necessary. Too many temporary employees lead to poor customer service and low stock of talents, resulting in General managers working long hours and under highstress(more details in ethical issues). Though more long-term employees mean more costs, the benefits from improved customer service will outweigh the costs. Furthermore, because recognition of employees' efforts can stimulate them to offer better service, some motivation measures are recommended.

According to ERG theory, people in different levels have different needs. Most temporary employees are in the existence level, they need money to maintain their existence requirements, and therefore incentives such as bonus will be useful. However, most long-term employees are in relatedness and growth level, so incentives such as vocation award or decision making involvement will be suitable. With the new recruitment, training and incentives, it’s estimated that an additional employee cost of €7. 5 million will be incurred, a 12% increase from last year. Ethical issues

Two ethical issues will be discussed in this report. a. Poor treatment of employees. General Managers and key senior employees are working under high stress over 16 hours every day. Solberri gets into ethical issue of overworking employees and paying no compensation. Due to a shortage of senior employees, their workload is unlikely to be reduced immediately. Therefore, the hotel should compensate for their overwork. To solve this problem fundamentally Soberri should reserve sufficient elites by increasing its long-term employees. b. Misdistribution of tips.

When Solberri collected all the tips and evenly distributed them to employees, an ethical issue arose for the transparency and fairness of such distribution. Such controversial tips distribution should be changed back to the traditional way—employees can keep the tips for themselves. For those non-facing-customer employees who don’t get tips, Solberri is recommended to increase their bonus to make up the difference. Forecast cash surplus investment issue Before analyzing the four proposals, it’s important to know how much cash is available for investment.

Since Solberri is under loan covenants and other financing alternatives such as rights issue can’t raise funds in a short time, the only source of funds is the internal capital. It’s estimated that 59 million cash will be generated from operations in this financial year. After deductingfinancecosts, tax, dividends and additional HR reform costs in the first issue, there’s only €30. 9 million cash available. (Appendix 2. 1) The total amount for the four proposals is €123 million (Appendix 2. 2).

Solberri has to perform a cost benefit analysis to choose the most profitable proposal as it is clear that Solberri doesn’t have enough funds to implement all of them. Proposal A is to extend the number of rooms at the four “ Premier” hotels by adding each another 200 rooms and supporting facilities. It’s estimated to generate €10 million NPV for each hotel over a 5-year period based on an 80% occupancy level. However, this may have some negative effects since the additional rooms and facilities make the hotel more crowded and less comfortable. Therefore, the 80% occupancy level is not guaranteed.

Besides, it’s just the first year that Solberri has had such high occupancy levels. Extending the number of rooms in such a large scale is too risky. Proposal B is to invest in refurbishment and extend spa facilities at the remaining hotels. The forecast cost is €6 million for each hotel. The high level of bookings at the 4 “ Premier” hotels during the 2008 Peak season has demonstrated the success of the refurbishment plan. So this proposal contains relatively little risk. Furthermore, spa facilities have become a key selling point in resort hotels.

This new trend provides great opportunity for Solberri to escape from the Red Ocean, the very competitive market of traditional resort hotels. By differentiating itself by providing exclusive spa facilities, Solberri can successfully grab the Blue-ocean market, namely the profitable and rapidly-developing market of resort hotels with exclusive spa facilities. Finally, refurbishing the hotels can improve Solberri's profit margin. However, refurbishing all the remaining hotels simultaneously is beyond Solberri's financial ability. It's recommended that Solberri refurbish only three hotels—two " Superior" and one " Super Plus".

Refurbishing the " Super Plus" hotels is riskier since there is no previous experience and the refurbishment will need to close permanently 15 rooms in each hotel. But if Solberri only refurbish " Superior" hotels, in a short time, there will be a gap in middle-priced hotels, which is unfavorable to the company's strategic development. Proposal C is to acquire an additional resort hotel costing 24 million. The expected NPV is €39. 2 million (Appendix 2. 3). Besides, the breakeven occupancy level is 60% (Appendix 2. 4), which is quite easy to achieve. So Proposal C seems profitable with reasonable risk.

However, the initiate cost is too large as it's for only one hotel. Compared with Proposal B, it's too risky for Solberri in its first year with such good performance. Proposal D is to invest in environmentally friendly initiatives including the installation of solar panels costing €6 million and other environmental initiatives costing €9 million. Though investing in these initiatives cannot generate profits for the company directly, it can help establish Solberri as a socially responsible company which will be positive to its image. But funds are so limited that investing in all these in unrealistic.

It’s recommended that Solberri invest in the solar panel project first since it can produce cost savings of 0. 6 million per year and defer the others. Loan covenant restriction The €20 million loan negotiated at the end of 2007 has loan covenants restricting the company’s further loan financing within 2 years from December 2007, resulting in a probable capital shortage for its future development. Solberri can try negotiating with the bank for removal of restriction by showing them the latest forecast figures and the high level of bookings. However, the good performance of only one year wouldn’t be convincing enough to the bank.

Solberri can also try refinancing by issuing additional stocks through public offering or private placement. However, due to the relatively high standard and costly registration of public offering, private placement is preferable. With low threshold for issuing, private placement is feasible for Solberri whose business just began to pick up after slow seasons. With the good performance this year, it’s probable that the Solberri will attract strategic investment from institutional investors via private placements to ensure its future development. The poor share price and vulnerability of Solberri

RECOMMENDATION Customer service and related HR issues. It is recommended that Solberri immediately work out a plan for recruitment and training, to ensure job fit and effective training among all employees. Employees who can’t provide the high standard of service will be refused or assigned to non-facing-customer positions. Moreover, Solberri should set up appropriate motivation mechanisms such as bonus and vacation rewards. It is also recommended that Solberri enlarge its long-term employee proportion by training some short-term employees to be skillful long-term ones.

In this way, more employees will cultivate a sense ofresponsibilityand can handle the previous temporary employees' work in non-peak season. Ethical issues It's recommended that Solberri compensate for employees' overwork. In the long run, the company needs to enlarge its senior employee reserve. It's recommended that Solberri abandon its controversial tips distribution and set up a bonus system for non-facing customer employees to make up their income difference. Forecast cash surplus investment issue

It's recommended that Solberri spend its forecast cash surplus on Proposal B to refurbish and extend the spa facilities at two " Superior" hotels and one " Super Plus" hotel, which costs €18 million in total. Since it's just the first year Solberri has performed so well in these years, it's better for it to be conservative towards investment. It's also recommended that Solberri invest in the installation of solar panels at all 12 hotels costing €6 million and postpone other environmentally friendly initiatives due to its limited funds. These two plans will result in €6. 9 million cash retained Appendix 2. 5), which will help improve the liquidity of Solberri. . Loan covenant restriction It is recommended that Solberri try to negotiate with the bank for removal of the restriction. If it's not workable, Solberri could try seasoned equity offering to refinance either by public offering or private placement, while private placement seems to be most feasible for Solberri and thus is highly recommended. If external financing doesn't work, it is highly recommended that Solberri try all means to control its costs. The poor share price and vulnerability of Solberri ? CONCLUSION

Solberri is now at a crucial time since it's the first time it has had such good performance in these years. It is now facing several important issues. The most important ones are how to solve the poor customer service problem and which investment proposal to choose for its future development to increase the occupancy level for all the hotel rooms. It is believed that the analysis and recommendations above can serve as useful references for its decision-making. Solberri has to differentiate itself in the market through a shift by showcasing its spa facilities as its forefront in capturing holiday makers.

With a change in visa regulations in Europe Solberri may opt to pay more attention to its local clients by offering the day use of the hotel's services and facilities during non-peak seasons. To position itself as a " holiday resort hotel", there should be a refurbishment of Solberri's hotels to " Premier" standards ? SWOT ANALYSIS STRENGTHS •Good reputation with a long history; •Proven track record of range of spa facilities •Successful refurbishment program •Many of long-term employees have worked for Solberri for over 10 years with rich experience. •Stable co-operation with several travel agents. Experienced board directors. •High sense of Corporate Social Responsibility( 1 hotel won a bronze award in the Green Tourism business awards, 2007 •High level of bookings for Peak season 2008 with large cash surplus forecast WEAKNESS •Outdated informationtechnologysystems. •Restrictive loan covenant. •Difficulty in enforcing agreed quality service levels. •Declining share price compared to 2002 •Poor customer service with disappointing customer feedback. •Low level of repeat booking. •Lack of motivation of short-term employees. •Poorly structured financial planning. •Resignation of Finance Director. OPPORTUNITIES High level of bookings and a forecast cash surplus of €59 million which can be used for further expansion, refurbishment program, paying dividends, and(or) meeting CSR by investing in environmentally friendly initiatives; • Huge potential market for Spa service •Pricing structure changes to boost occupancy levels •Effective use of variety of media to generate more sales THREATS • External completion from other hotel industries • Understaffing and poor service to meet the high level booking that could impact reputation •Resistance from •Competitors having state of art information technology can be market eaders. • Fall in spa revenues of one " premier" hotel due to a rival business operated by an ex-manager. •Difference of opinion amongst management staff may delay the strategy implementation. WORKINGS 2. 1. 1 Investible surplus €59 million is cash generated from operations before finance costs, tax and dividends, which should be deducted. Besides, the additional operation cost incurred by human resources management should also be deducted in order to get the available cash for investment. 2. 1. 2Cost of finance S. No. AmountRate of InterestDetailsDuration for CYInterest Cost a. 12 m10%Oct- Dec ' 073 months€0. 3 m b. €6 m8%Repayable in Sep 20101 yr€0. 48m c. €15 m11%June 20121 yr€1. 65m d. €20 m10%Jan-2008 to Dec ' 149 mths€1. 5m Total€3. 93 m Notes: a. €12 million loan at 10% repayable in December 2007 -As its repayable date is in December 2007, the interest expense incurred in this accounting period is only for three months (October 2007 to December 2007). €12 million*10%*3/12 = €0. 3 million b. €6 million loan at 8% repayable in September 2010 -€6 million*8% = €0. 48 million c. €15 million loan at 11% repayable in June 2012 -€15 million*11% = €1. 5 million d. €20 million loan at 10% beginning in January 2008 and repayable in December 2014 -As this loan began in January 2008, the interest expense incurred in this accounting period is only for nine months (January 2008 to September 2008). €20 million*10%*9/12 = €1. 5 million 2. 1. 3 Tax expense As stated in the case, the post-tax profit for the year ended September 2008 will be €27 million. Based on the tax rate of 32%, the taxable income = €27 million/(1-32%) = €39. 7 million . Therefore, the tax expense = €39. 7 million*32% = €12. 7 million 2. 1. 4 Dividends

In 2007, Solberri made a profit of €5 million and paid €2 million for dividends, which equals a dividend per share of €0. 083. It's recommended that Solberri double the DPS this year, making the total dividends expenditure as much as €4 million. 2. 1. 5 Additional operation cost As is mentioned before, the high occupancy level this year will incur additional operational cost due to the employee recruitment, training and motivation. It' estimated to be around €7. 5 million based on an estimated 12% increase compared with 2007 when the staff costs were €62 million. Cash Available for Investment( in million)

Investible surplus( before deduction)= €59. 00 Less: Interest cost –€3. 93 Tax expense –€12. 7 Dividend expense –€4. 00 Additional operation cost –€7. 5 Net surplus= €30. 9 2. 2. Total cost for all four investment proposals : ProposalInvestment cost per hotelNumber of hotelsTotal cost A€9 million4€36 million B€6 million8€48 million C****€24 million D€15 million Total cost€123 million **Total cost for Proposal C = acquiring cost + refurbishing cost + marketing cost = €5 million +€16 million+€3 million = €24 million Total cost for Proposal D = €15 million 2. . Expected NPV of Proposal C As is shown in the case, when occupancy level equals 95%, the NPV will be €100. 0 million. When it's 80%, the NPV will be €35 million. When it's 50%, the NPV will be –€25 million. And their probabilities are 25%, 60%

and 15% respectively. Therefore, the weighted average NPV = €100. 0 million*25% + €35. 0 million*60% +(-€25 million)*15% = €42. 2 million However the marketing cost of €3 million is excluded in the above NPV, so the expected NPV of Proposal C = €42. 2 million – €3 million = €39. 2 million 2. 4. Breakeven occupancy level of Proposal C When occupancy level equals 95%, the NPV will be €97 million.

When it's 50%, the NPV will be -€28 million. Thus, when the occupancy level decreases by 1%, the NPV will decrease by €2. 78 million. [€97 million - (-€28 million)] / (95-50) = €2. 78 million In this way, when the occupancy level changes by about 35% (97/2. 78), the NPV will decrease to zero. Therefore, the breakeven occupancy level is around 60%. 2. 5 Estimated cash retained Estimated cash retained = cash available for investment – investment costs = €30. 9 million –€24 million = €6. 9 million Comparison between Solberri and Shangri-la Asia Limited with the DuPont Model 3. 1 DuPont Model of Solberri 2007 Return on Equity (ROE) 0. 568 Return on Assets (ROA) 0. 3086? Equity Multiplier (EM) 1. 8409 Profit Margin 0. 0314? Total Asset Turnover 0. 9815 1 /(1—Debt Ratio 0. 4568) Net Income/Net Sales Net Sales/Average Total Assets Total Liabilities/Total Assets 3. 2 DuPont Model of Shangri-la Asia Limited 2007 Return on Equity (ROE) 0. 1046 Return on Assets (ROA) 0. 1029? Equity Multiplier (EM) 1. 016 Profit Margin 0. 3069? Total Asset Turnover 0. 3354 1 /(1—Debt Ratio 0. 0159) Net Income/Net Sales Net Sales/Average Total Assets Total Liabilities/Total Assets Comparison between Solberri and Shangri-la Asia Limited with the DuPont Model 3. DuPont Model of Solberri 2007 Return on Equity (ROE) 0. 0568 Return on Assets (ROA) 0. 3086? Equity Multiplier (EM) 1. 8409 Profit Margin 0. 0314? Total Asset

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Priority issues: •Poor customer experience that could be a result of ethical issues such as oPoor treatment of General manages and senior employees. oMisdistribution of tips oInvestment in unprofitable environmentally friendly initiatives. •The potential need to borrow money to enhance spas before the 2007/08 Peak season •The need to raise occupancy rates and earnings generated from extra charges to hit the planned revenue for the financial year ending September 2008 •The poor share price and vulnerability of Solberri Other issues: •Installation of solar panels Non-participation in the international star ratings system •Potential problems with the quality of outsourced services •Upgrading website to include a virtual tour of facilities . ? ISSUE ANALYSIS In this section, the analysis is done for top priority issues. Customer service and relevant HR issues. The quality of customer service is crucial to companies' survival in service industry. Unfortunately, the service provided by Solberri failed to meet the expected standard of its customers. The main reason for poor customer service is employees' lack of skills and motivation.

The majority of Solberri employees are temporary, with limited knowledge of the hotel industry and relevant skills. Besides, all short-term employees only receive two days introduction training which is apparently insufficient. The customer service can be improved in two aspects. In the short term, Nick Silva, customer service Director, needs to review staffing level immediately to meet the upcoming demand. Strict selection and a specific regular training program are needed to ensure the quality of its employees.

In the long term, adjusting the ratio of the number of long-term employees to that of short-term ones is necessary. Too many temporary employees lead to poor customer service and low stock of talents, resulting in General managers working long hours and under high stress (more details in ethical issues). Though more long-term employees mean more costs, the benefits from improved customer service will outweigh the costs. Furthermore, because recognition of employees' efforts can stimulate them to offer better service, some motivation measures are recommended.

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Since Solberri is under loan covenants and other financing alternatives such as rights issue can’t raise funds in a short time, the only source of funds is the internal capital. It’s estimated that 59 million cash will be generated from operations in this financial year. After deducting finance costs, tax, dividends and additional HR reform costs in the first issue, there’s only €30. 9 million cash available. (Appendix 2. 1) The total amount for the four proposals is €123 million (Appendix 2. 2). Solberri has to perform a cost benefit analysis to choose the most rofitable proposal as it is clear that Solberri doesn’t have enough funds to implement all of them. Proposal A is to extend the number of rooms at the four “ Premier” hotels by adding each another 200 rooms and supporting facilities. It’s estimated to generate €10 million NPV for each hotel over a 5-year period based on an 80% occupancy level. However, this may have some negative effects since the additional rooms and facilities make the hotel more crowded and less comfortable. Therefore, the 80% occupancy level is not guaranteed.

Besides, it’s just the first year that Solberri has had such high occupancy levels. Extending the number of rooms in such a large scale is too risky. Proposal B is to invest in refurbishment and extend spa facilities at the remaining hotels. The forecast cost is €6 million for each hotel. The high level of bookings at the 4 “ Premier” hotels during the 2008 Peak season has demonstrated the success of the refurbishment plan. So this proposal contains relatively little risk. Furthermore, spa facilities have become a key selling point in resort hotels.

This new trend provides great opportunity for Solberri to escape from the Red Ocean, the very competitive market of traditional resort hotels. By differentiating itself by providing exclusive spa facilities, Solberri can successfully grab the Blue-ocean market, namely the profitable and rapidly-developing market of resort hotels with exclusive spa facilities. Finally, refurbishing the hotels can improve Solberri’s profit margin. However, refurbishing all the remaining hotels simultaneously is beyond Solberri’s financial ability. It’s recommended that Solberri refurbish only three hotels—two “ Superior” and one “ Super Plus”.

Refurbishing the “ Super Plus” hotels is riskier since there is no previous experience and the refurbishment will need to close permanently 15 rooms in each hotel. But if Solberri only refurbish “ Superior” hotels, in a short time, there will be a gap in middle-priced hotels, which is unfavorable to the company’s strategic development. Proposal C is to acquire an additional resort hotel costing 24 million. The expected NPV is €39. 2 million (Appendix 2. 3). Besides, the breakeven occupancy level is 60% (Appendix 2. 4), which is quite easy to achieve. So Proposal C seems profitable with reasonable risk.

However, the initiate cost is too large as it’s for only one hotel. Compared with Proposal B, it’s too risky for Solberri in its first year with such good performance. Proposal D is to invest in environmentally friendly initiatives including the installation of solar panels costing €6 million and other environmental initiatives costing €9 million. Though investing in these initiatives cannot generate profits for the company directly, it can help establish Solberri as a socially responsible company which will be positive to its image. But funds are so limited that investing in all these in unrealistic.

It's recommended that Solberri invest in the solar panel project first since it can produce cost savings of 0. 6 million per year and defer the others. Loan covenant restriction The €20 million loan negotiated at the end of 2007 has loan covenants restricting the company's further loan financing within 2 years from December 2007, resulting in a probable capital shortage for its future development. Solberri can try negotiating with the bank for removal of restriction by showing them the latest forecast figures and the high level of bookings. However, the good performance of only one year wouldn't be convincing enough to the bank.

Solberri can also try refinancing by issuing additional stocks through public offering or private placement. However, due to the relatively high standard and costly registration of public offering, private placement is preferable. With low threshold for issuing, private placement is feasible for Solberri whose business just began to pick up after slow seasons. With the good performance this year, it's probable that the Solberri will attract strategic investment from institutional investors via private placements to ensure its future development. The poor share price and vulnerability of Solberri

RECOMMENDATION Customer service and related HR issues. It is recommended that Solberri immediately work out a plan for recruitment and training, to ensure job fit and effective training among all employees. Employees who can't provide the high standard of service will be refused or assigned to non-facing-customer positions. Moreover, Solberri should set up appropriate motivation mechanisms such as bonus and vacation rewards. It is also recommended that Solberri enlarge its long-term employee proportion by training some short-term employees to be skillful long-term ones.

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It's recommended that Solberri spend its forecast cash surplus on Proposal B to refurbish and extend the spa facilities at two " Superior" hotels and one " Super Plus" hotel, which costs €18 million in total. Since it's just the first year Solberri has performed so well in these years, it's better for it to be conservative towards investment. It's also recommended that Solberri invest in the installation of solar panels at all 12 hotels costing €6 million and postpone other environmentally friendly initiatives due to its limited funds. These two plans will result in €6. 9 million cash retained (Appendix 2. ), which will help improve the liquidity of Solberri. . Loan covenant restriction It is recommended that Solberri try to negotiate with the bank for removal of the restriction. If it's not workable, Solberri could try seasoned equity offering to refinance either by public offering or private placement, while private placement seems to be most feasible for Solberri and thus is highly recommended. If external financing doesn't work, it is highly recommended that Solberri try all means to control its costs. The poor share price and vulnerability of Solberri ? CONCLUSION

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With a change in visa regulations in Europe Solberri may opt to pay more attention to its local clients by offering the day use of the hotel's services and facilities during non-peak seasons. To position itself as a " holiday resort hotel", there should be a refurbishment of Solberri's hotels to " Premier" standards ? SWOT ANALYSIS STRENGTHS •Good reputation with a long history; •Proven track record of range of spa facilities •Successful refurbishment program •Many of long-term employees have worked for Solberri for over 10 years with rich experience. •Stable co-operation with several travel agents. Experienced board directors. •High sense of Corporate Social Responsibility( 1 hotel won a bronze award in the Green Tourism business awards, 2007 •High level of bookings for Peak season 2008 with large cash surplus forecast WEAKNESS •Outdated information technology systems. •Restrictive loan covenant. •Difficulty in enforcing agreed quality service levels. •Declining share price compared to 2002 •Poor customer service with disappointing customer feedback. •Low level of repeat booking. •Lack of motivation of short-term employees. •Poorly structured financial planning. Resignation of Finance Director. OPPORTUNITIES •High level of bookings and a forecast cash surplus of €59 million which can be used for further expansion, refurbishment program, paying dividends, and(or) meeting CSR by investing in environmentally friendly initiatives; • Huge potential market for Spa service •Pricing structure changes to boost occupancy levels •Effective use of variety of media to generate more sales THREATS • External completion from other hotel industries • Understaffing and poor service to meet the high level booking that could impact reputation •Resistance from Competitors having state of art information technology can be market leaders. • Fall in spa revenues of one “ premier” hotel due to a rival business operated by an ex-manager. •Difference of opinion amongst management staff may delay the strategy implementation. WORKINGS 2. 1. 1 Investible surplus €59 million is cash generated from operations before finance costs, tax and dividends, which should be deducted. Besides, the additional operation cost incurred by human resources management should also be deducted in order to get the available cash for investment. 2. 1. 2Cost of finance

S. No. AmountRate of InterestDetailsDuration for CYInterest Cost a. €12 m10%Oct- Dec ‘ 073 months€0. 3 m b. €6 m8%Repayable in Sep 20101 yr€0. 48m c. €15 m11%June 20121 yr€1. 65m d. €20 m10%Jan-2008 to Dec ‘ 149 mths€1. 5m Total€3. 93 m Notes: a. €12 million loan at 10% repayable in December 2007 -As its repayable date is in December 2007, the interest expense incurred in this accounting period is only for three months (October 2007 to December 2007). €12 million*10%*3/12 = €0. 3 million b. €6 million loan at 8% repayable in September 2010 -€6 million*8% = €0. 48 million c. 15 million loan at 11% repayable in June 2012 -€15 million*11% = €1. 65 million d. €20 million loan at 10% beginning in January 2008 and repayable in December 2014 -As this loan began in January 2008, the interest expense incurred in this accounting period is only for nine months (January 2008 to September 2008). €20 million*10%*9/12 = €1. 5 million 2. 1. 3 Tax expense As stated in the case, the post-tax profit for the year ended September 2008 will be €27 million. Based on the tax rate of 32%, the taxable income = €27 million/(1-32%) = €39. 7 million . Therefore, the tax expense = €39. 7 million*32% = €12. 7 million 2. . 4 Dividends In 2007, Solberri made a profit of €5 million and paid €2 million for dividends, which equals a dividend per share of €0. 083. It’s recommended that Solberri double the DPS this year, making the total dividends expenditure as much as €4 million. 2. 1. 5 Additional operation cost As is mentioned before, the high occupancy level this year will incur additional operational cost due to the employee recruitment, training and motivation. It’ estimated to be around €7. 5 million based on an estimated 12% increase compared with 2007 when the staff costs were €62 million. Cash Available for Investment( in million)

Investible surplus( before deduction)= €59. 00 Less: Interest cost –€3. 93 Tax expense –€12. 7 Dividend expense –€4. 00 Additional operation cost –€7. 5 Net surplus= €30. 9 2. 2. Total cost for all four investment proposals : ProposalInvestment cost per hotelNumber of hotelsTotal cost A€9 million4€36 million B€6 million8€48 million C****€24 million D€15 million Total cost€123 million **Total cost for Proposal C = acquiring cost + refurbishing cost + marketing cost = €5 million +€16 million+€3 million = €24 million Total cost for Proposal D = €15 million . 3. Expected NPV of Proposal C As is shown in the case, when occupancy level equals 95%, the NPV will be €100. 0 million. When it's 80%, the NPV will be €35 million. When it's 50%, the NPV will be –€25 million. And their probabilities are 25%, 60% and 15% respectively. Therefore, the weighted average NPV = €100. 0 million*25% + €35. 0 million*60% +(-€25 million)*15% = €42. 2 million However the marketing cost of €3 million is excluded in the above NPV, so the expected NPV of Proposal C = €42. 2 million – €3 million = €39. 2 million 2. 4. Breakeven occupancy level of Proposal C

When occupancy level equals 95%, the NPV will be €97 million. When it's 50%, the NPV will be -€28 million. Thus, when the occupancy level decreases by 1%, the NPV will decrease by €2. 78 million. [€97 million - (-€28 million)] / (95-50) = €2. 78 million In this way, when the occupancy level changes by about 35% (97/2. 78), the NPV will decrease to zero. Therefore, the breakeven occupancy level is around 60%. 2. 5 Estimated cash retained Estimated cash retained = cash available for investment – investment costs = €30. 9 million –€24 million = €6. 9 million Comparison between Solberri and Shangri-la Asia Limited with the DuPont Model 3. DuPont Model of Solberri 2007 Return on Equity (ROE) 0. 0568 Return on Assets (ROA) 0. 3086? Equity Multiplier (EM) 1. 8409 Profit Margin 0. 0314? Total Asset Turnover 0. 9815 1 /(1—Debt Ratio 0. 4568) Net Income/Net Sales Net Sales/Average Total Assets Total Liabilities/Total Assets 3. 2 DuPont Model of

Shangri-la Asia Limited 2007 Return on Equity (ROE) 0. 1046 Return on Assets (ROA) 0. 1029? Equity Multiplier (EM) 1. 016 Profit Margin 0. 3069? Total Asset Turnover 0. 3354 1 /(1—Debt Ratio 0. 0159) Net Income/Net Sales Net Sales/Average Total Assets Total Liabilities/Total Assets

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