BELLAVISTA HOTEL RESTAURANT

- SOLUTIONS -

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"*At the beginning of 1990 Mr. Orlandi started some investigation on the management of the last three years.*

He reclassified financial statements of the period 1987-89, but it emerged no clear indications on the malaise perceived by Mr. Orlandi".

Analyze the economic and financial situation of the company, using the balance sheet data and by calculating the indicators that you feel are most appropriate: Is Mr Orlandi's perception correct? What problems emerge from the analysis?

NEEDS:
- Overnight stay
- Holidays

CUSTOMERS:
- Business travelers
- Tourists (German families)

BUSINESS: HOTEL

COMPETITORS:
- Other Hotels on Lake Garda
- Residences on Lake Garda

SUCCESS DRIVERS:
- Location
- Functionality of structures
- Pricing

NEEDS:
- Gourmet cuisine
- Social and work meetings

CUSTOMERS:
- Regular customers
- Local residents
- People aged between thirty and fifty years

BUSINESS: RESTAURANT

CONCORRENTI:
- Others restaurants on Lake Garda

SUCCESS DRIVERS:
- Quality
- High level service
- Pricing

NEEDS:
- Fitness
- Fun

CUSTOMERS:
- Local residents
- Hotel guests
- Customers from other hotels

BUSINESS: SPORT FACILITIES

COMPETITORS:
- Local gyms
- Dance Clubs
- Cinemas and theaters

SUCCESS DRIVERS:
- Functionality
- Pricing

RECLASSIFIED INCOME STATEMENT (€/000)

	1989		1988		1987	
REVENUES	**6.010**	**100,00%**	**5.460**	**100,00%**	**4.580**	**100,00%**
CONSUMABLES	-1.157	-19,25%	-1.005	-18,41%	-857	-18,71%
RENTALS	-264	-4,39%	-246	-4,51%	-191	-4,17%
SERVICES	-70	-1,16%	-66	-1,21%	-147	-3,21%
MAINTENANCE	-227	-3,78%	-228	-4,18%	-151	-3,30%
COMMERCIAL COSTS	-67	-1,11%	-66	-1,21%	-55	-1,20%
ADMINISTRATIVE COSTS	-75	-1,25%	-79	-1,45%	-73	-1,59%
OVERHEAD COSTS	-104	-1,73%	-107	-1,96%	-78	-1,70%
VALUE ADDED	**4.046**	**67,32%**	**3.663**	**67,09%**	**3.028**	**66,11%**
PERSONNEL COSTS	-3.462	-57,60%	-3.019	-55,29%	-2.363	-51,59%
EBITDA	**584**	**9,72%**	**644**	**11,79%**	**665**	**14,52%**
DEPRECIATIONS	-525	-8,74%	-505	-9,25%	-455	-9,93%
EBIT	**59**	**0,98%**	**139**	**2,55%**	**210**	**4,59%**
FINANCIAL CHARGES	-13	-0,22%	-15	-0,27%	-12	-0,26%
NON RECURRENT ITEMS	-3	-0,05%	14	0,26%	-2	-0,04%
INCOME BEFORE TAXES	**43**	**0,72%**	**138**	**2,53%**	**196**	**4,28%**
TAXES	-17	-0,28%	-49	-0,90%	-86	-1,88%
NET INCOME	**26**	**0,43%**	**89**	**1,63%**	**110**	**2,40%**

RECLASSIFIED ASSETS STATEMENT - (€/000)

	1989		1988		1987	
CASH	15	0,82%	18	1,03%	12	0,72%
BANKS	170	9,34%	45	2,58%	65	3,89%
ACCOUNTS RECEIVABLE	45	2,47%	24	1,38%	25	1,50%
ACCRUALS	23	1,26%	20	1,15%	12	0,72%
INVENTORY	32	1,76%	18	1,03%	23	1,38%
CURRENT ASSETS	**285**	**15,66%**	**125**	**7,16%**	**137**	**8,21%**
REAL ESTATE	2.100	115,38%	2.100	120,34%	1.950	116,84%
PLANT	450	24,73%	420	24,07%	390	23,37%
FURNITURE	400	21,98%	350	20,06%	305	18,27%
VEHICLES	35	1,92%	25	1,43%	21	1,26%
(DEPRECIATION FUNDS)	-1.450	-79,67%	-1.275	-73,07%	-1.134	-67,94%
FIXED ASSETS	**1.535**	**84,34%**	**1.620**	**92,84%**	**1.532**	**91,79%**
TOTAL ASSETS	**1.820**	**100,00%**	**1.745**	**100,00%**	**1.669**	**100,00%**

RECLASSIFIED LIABILITIES STATEMENT - (€/000)

	1989		1988		1987	
ACCOUNTS PAYABLE	382	20,99%	228	13,07%	197	11,80%
OTHER PAYABLES	128	7,03%	86	4,93%	28	1,68%
TAX FUND	23	1,26%	50	2,87%	48	2,88%
CURRENT LIABILITIES	**533**	**29,29%**	**364**	**20,86%**	**273**	**16,36%**
MORTGAGES	180	9,89%	240	13,75%	300	17,97%
EMPLOYEE BENEFITS FUND	452	24,84%	412	23,61%	328	19,65%
FIXED LIABILITIES	**632**	**34,73%**	**652**	**37,36%**	**628**	**37,63%**
SHAREHOLDERS EQUITY	500	27,47%	500	28,65%	250	14,98%
RESERVES	100	5,49%	100	5,73%	350	20,97%
RETAINED EARNINGS	29	1,59%	40	2,29%	58	3,48%
NET INCOME	26	1,43%	89	5,10%	110	6,59%
TOTAL SHAREHOLDERS EQUITY	**655**	**35,99%**	**729**	**41,78%**	**768**	**46,02%**
TOTAL LIABILITIES	**1.820**	**100,00%**	**1.745**	**100,00%**	**1.669**	**100,00%**

CASH FLOW STATEMENT- (€/000)

	1987-88	*1988-89*
EBIT	**139**	**59**
Depreciations	505	525
Provisions	84	40
Net Working Capital Flow from Operations	**728**	**624**
Change in Receivables	1	-21
Change in Payables	31	154
Change in Inventories	5	-14
Change in Accrued Income	-8	-3
Change in Debts	58	42
Cash Flow from Operations	**815**	**782**
Taxes	-47	-44
Financial charges	-15	-13
Cash Flow from Current Management	**753**	**725**
Change in Immobilizations	-579	-443
Change in Mortgages	-60	-60
Change in Equity	-128	-100
Net Cash Flow	**-14**	**122**

PERFORMANCE INDICATORS

	1989	1988	1987
ROE = Return On Equity = Net Income/Total Equity = SHAREHOLDERS PROFITABILITY	**3,97%**	**12,21%**	**14,32%**
ROI = Return On Investments = EBIT/Assets = OPERATING PROFITABILITY	**3,24%**	**7,97%**	**12,58%**
Average Cost of Debts = Financial Charges/Total Debts	1,12%	1,48%	1,33%
Debt Rate = Total Debts/Total Shareholders Equity	1,78	1,39	1,17
Net Financial Position (€/.000) = Financial Debts - Cash	-5,00	177,00	223,00
ROS = Return On Sales = EBIT/Revenues = OPERATING MARGIN	**0,98%**	**2,55%**	**4,59%**
Net Assets Turnover = Revenues/Total Assets	3,30	3,13	2,74
EBITDA (€/.000)	**584,00**	**644,00**	**665,00**
EBITDA/Revenues = EBITDA MARGIN = MARGIN PRODUCED BY CORE ACTIVITIES	**9,72%**	**11,79%**	**14,52%**
NFP/EBITDA	-0,01	0,27	0,34
Net Working Capital (€/.000)	-248	-239	-136

The main issue is the reduction of operating profitability !!!

PERFORMANCE ANALYSIS

The analysis of the main profitability indicators over the three-year period of measurement is sufficient to show that **the company as a whole has experienced a significant decline in operating profitability, despite the reasonable increase in revenues.**

Consider that the **ROI (operating profitability of assets)** shows a decrease **from 13% in 1987 to 3% in 1989** and that the **ROS (operating profitability of revenues)** reports a considerable **loss of profit margins, going from 5% in 1987 at 1% in 1989.**

On the other hand, the analysis of the income statement items reinforces this assessment and makes it possible to identify **the main cause in a considerable growth of two cost items:**

- **personnel costs** (which account for 58% of revenues and which increased by 50 % in three years)
- **consumption costs** (which account for 19% of revenues and increased by 30% in three years).

The feeling, therefore, is that **there are major problems in the operational management of the businesses that make up the facility's offer system: accommodation (hotel services), the restaurant (restaurant services), sports facilities.**

The financial situation seems less critical. The Net Financial Position benefits from the company's ability to cash out and debt is mainly aimed at increasing supply debts and debts to the tax authorities, social security and welfare agencies (different debts). **The cost of debt, in effect, is slightly down, given that, moreover, the company does not use short-term bank debt.**

We can conclude that the company has not yet entered into a financial and liquidity crisis, as the good trend of cash flows also demonstrates. However, this risk could occur if the operating profitability continues to decline or becomes negative.

"*He had the impression that some of the many activities that now ran through the hotel facilities weren't productive enough*"

Prepare an income statement that highlights the specific marginality of the each single business unit (hotel, restaurant, sports).

Which of the business units has the best results? Why? Do any of the business units have a negative marginality? Why?

REVENUES AND COST STRUCTURE: VARIABLE VS. FIXED

	HOTEL	RESTAURANT	SPORTS	FIRM
Revenues	**Variables**	**Variables**	**Variables**	**Variables**
Consumptions costs (raw materials)	Variables	Variables	Variables	Variables
Rentals	Variables	Variables	Variables	Variables
Employees (annual)	Fixed	Fixed	Fixed	Fixed
Employees (seasonal)	Fixed	Fixed	Fixed	Fixed
External Services	Fixed	Fixed	Fixed	Fixed
Maintenance	Fixed	Fixed	Fixed	Fixed
Depreciations	Fixed	Fixed	Fixed	Fixed
Employees (annual)	Fixed		Fixed	Fixed
All others firm costs	Fixed			

REVENUES AND COST STRUCTURE: TREACEBLE VS. NOT TRACEABLE

	HOTEL	RESTAURANT	SPORTS	FIRM
Revenues	**Traceable**	**Traceable**	**Traceable**	**Traceable**
Consumptions costs (raw materials)	Traceable	Traceable	Traceable	Traceable
Rentals	Traceable	Traceable	Traceable	Traceable
Employees (annual)	Traceable	Traceable	Traceable	Traceable
Employees (seasonal)	Traceable	Traceable	Traceable	Traceable
External Services	Traceable	Traceable	Traceable	Traceable
Maintenance	Traceable	Traceable	Traceable	Traceable
Depreciations	Traceable	Traceable	Traceable	Traceable
Employees (annual)	Not Traceable			Traceable
All others firm costs	Not Traceable			Traceable

INCOME STATEMENT PER BUSINESS - (€/000)

	HOTEL		RESTAURANT		SPORTS		TOTAL	
Revenues	**€ 3.822.000,00**	**100,00%**	**€ 1.794.000,00**	**100,00%**	**€ 394.000,00**	**100,00%**	**€ 6.010.000,00**	**100,00%**
Consumptions	€ 146.000,00	3,82%	€ 975.000,00	54,35%	€ 36.000,00	9,14%	€ 1.157.000,00	19,25%
Rentals	€ 182.000,00	4,76%	€ 76.000,00	4,24%	€ 6.000,00	1,52%	€ 264.000,00	4,39%
First Contribution Margin	**€ 3.494.000,00**	**91,42%**	**€ 743.000,00**	**41,42%**	**€ 352.000,00**	**89,34%**	**€ 4.589.000,00**	**76,36%**
Employees (annual)	€ 1.710.000,00	44,74%	€ 640.000,00	35,67%	€ 80.000,00	20,30%	€ 2.430.000,00	40,43%
Employees (seasonal)	€ 720.000,00	18,84%	€ -	0,00%	€ 72.000,00	18,27%	€ 792.000,00	13,18%
External Services	€ 24.000,00	0,63%	€ 42.000,00	2,34%	€ 4.000,00	1,02%	€ 70.000,00	1,16%
Maintenance	€ 165.000,00	4,32%	€ 24.000,00	1,34%	€ 38.000,00	9,64%	€ 227.000,00	3,78%
Depreciations	€ 155.000,00	4,06%	€ 64.000,00	3,57%	€ 88.000,00	22,34%	€ 307.000,00	5,11%
Second Contribution Margin	***€ 720.000,00***	**18,84%**	***-€ 27.000,00***	**-1,51%**	***€ 70.000,00***	**17,77%**	***€ 763.000,00***	**12,70%**
Employees (annual)	€ 240.000,00			4,27%	€ -	0,00%	€ 240.000,00	3,99%
Third Contribution Margin	***€ 453.000,00***			**8,07%**	***€ 70.000,00***	**0,00%**	***€ 523.000,00***	**1,09%**

BUSINESS UNITS PROFITABILITY ANALYSIS

The Management Accounting Income Statement per Business allows, in a context of multibusiness company, to calculate with a good objectivity the margins produced by each of the individual businesses, namely **the ability of individual businesses to adequately repay their VARIABLE COSTS and their SPECIFIC (TRACEABLES) FIXED COSTS .**

A first analysis at the level of the **second contribution margin** shows, in effect, how **the restaurant, in 1989, produced a second negative contribution margin, significantly impacting on the decline in the company's overall profitability.**

From a more in-depth analysis it is also possible to appreciate the fact that **the restaurant's first problem is the management of consumption costs which represent its main cost item.**

BUSINESS: RESTAURANT

The analysis of the restaurant's economic situation clearly shows that **the main problem** of this business **is represented by the level of consumptions and the ability of revenues to cover these costs.** Indeed, **the restaurant shows a cost structure in which raw materials account for 54% of revenues.**

Such a high consumption cost is linked, in part, to a structural and functional situation related to the type of activity carried out. Remember, in fact, that Mr. Omero Orlandi presents itself as a **high quality restaurant** that offers good food and is frequented by lovers of good food.

This is a type of service that puts the customer and the service provided at the center of management and which must guarantee high punctuality and reliability of the service. A typology of catering characterized **by an important role of human resources and of the activities that the latter carry out. A service whose performance depends on the ability to segment customers, customize the services offered and select and adequately train human resources.**

BUSINESS: RESTAURANT

However, **such a high level of raw material costs is also the signal of some management problems** such as:

- **inefficient use, by the chef and kitchen staff, of a particularly expensive raw material,**
- **inadequate management of purchase prices and negotiations with suppliers,**
- **selling price too low compared to the quality of the food and the level of service offered to the customer.**

This last consideration is confirmed by the analysis of **the evolution of price over time and the relative trend of demand**. Indeed, there is an elasticity of demand at the positive price (**The price increases but the demand also continues to increase**):

- 1987 - average price € 36.00 - meals /day 95
- 1988 - average price € 42.00 - meals /day 102
- 1989 - average price € 46.00 - meals /day 130

In fact, in the last three years, as the selling price increased (+ 28% approximately), demand has steadily increased (+ 37% approximately).

BUSINESS: RESTAURANT

The first problem of the restaurant, therefore, is that it currently sells its service at a price that is too low compared to the level of quality assured to the customer.

In reality, **a slight increase in the average price of the cover would be easily achievable and the demand, given the level of price elasticity, would remain at least constant, allowing the positive contribution of the second contribution margin.** All this also in light of the degree of operating leverage shown by the restaurant.

From a small simulation it emerges that, for the same fixed specific costs and variable costs and for the same number of covers served (assuming, therefore, a constant demand), the price per covered that would bring the restaurant's second contribution margin to balance is amounting to € 46.69. This would mean only a + 1.5% increase compared to the current price.

At a later time, **after redefining the price policies and the level of efficiency in the use of the raw material, it would be advisable to assess whether it is possible to reduce the specific fixed costs of the restaurant while maintaining adequate the level of service provided to the customer.**

BUSINESS: HOTEL

The hotel management features differ from those of the restaurant.

The weight of variable costs is very small (8% of revenues), while the level of specific fixed costs (especially personnel and depreciation) is particularly high.

The hotel, therefore, shows a first margin of positive and particularly high contribution (91% of revenues) and a second margin (19% of revenues) which contributes positively to company profitability, helping to cover the losses generated by the restaurant. **This could suggest that the hotel is optimally managed. In reality it is necessary to carefully evaluate the type of economic and management structure that characterizes this service.**

It is, in effect, a typical business **"at saturation of production capacity".** A type of service, characterized by **the considerable weight of the fixed structures, which places the individual service units at the center of management and for which it is necessary to seek high levels of volume and efficiency of the structures.** A service based on standard, clear and transparent customer access and access procedures.

BUSINESS: HOTEL

There is, in particular, a parameter, very significant for evaluating the performance of a similar overnight stay service, which shows that there is also ample room for maneuver for the hotel to improve economic results. This is **the average occupancy rate of available rooms.** This parameter has been configured, in the last three years, as follows:

- 1987 - 68%
- 1988 - 70%
- 1989 - 65%.

The hotel, as you can see, has never reached saturation levels of production capacity close to 100%, indeed. In 1989 its available room saturation rate dropped to 65%. **For a structure that has the need to cover particularly high specific fixed costs, this means under-utilizing its production capacity and not maximizing second-level margins.**

A particular analysis deserves the fixed cost structure of the hotel. It would be useful to understand, in fact, **why such seasonal personnel are used so highly and whether such a heavy structure is not oversized compared to the level of service offered to customers.**

Possible Improvements

It is possible to affirm that the most important intervention undoubtedly concerns **the restaurant, which must recover the lost profitability.** Therefore, for this business it is necessary to work in the direction of:

- **increase the average price per covered consistently with the customer's perception of service quality,**
- **optimize the purchasing and use policies of raw materials for food preparation,**
- **reorganize the personnel structure aligning it to the level of service you want to offer to the customer.**

As for **the hotel**, the intervention of Mr. Orlandi should address **the achievement of higher margins**, working as follows:

- **increase the room occupancy rate through appropriate promotional policies,**
- **activate promotional initiatives that make it possible to de-seasonalizing the activity,**
- **realign the personnel structure to the level of service and the occupancy rate of the rooms to be achieved.**

As regards **sports facilities**, finally, while noting **their fair profitability**, there is the possibility of further improving the results:

- **increasing the occupancy rate of facilities through appropriate promotional policies,**
- **ensuring adequate and efficient maintenance of facilities,**
- **improving the level of integration with the overnight stay service to exploit useful commercial synergies.**