



SPECIAL STUDY

Hoteles Hesperia Enables Rapid Growth with SAP

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IDC OPINION

Hoteles Hesperia is a Barcelona-based hotel chain with 47 three, four, and five-star hotels located throughout Spain, and in the U.K., Belgium, Andorra, and Venezuela. In 2004, it generated revenues of €171 million and remained strongly profitable with earnings before interest, taxes, depreciation, and amortization of €29 million.

The chain had been growing for years, but by 2001 adding new hotels had become increasingly complex and time consuming. The local IT set-up was difficult to maintain and central management had a very limited view of the activities of the individual hotels. In a bold move to streamline and simplify operations, Hesperia embarked on a project to centralize all IT and accounting completely, so that the individual hotels would use centrally hosted applications and shared accounting services. Hesperia selected SAP R/3 (now available in mySAP ERP) combined with Simhotel from CCS as its new application platform and the solution went live in April 2003, since which time several key performance indicators have improved dramatically:

- ☑ *Accelerated integration of new and acquired hotels into the chain.* It takes one week to implement and configure the combined SAP R/3 and Simhotel applications and train staff as opposed to eight weeks before the SAP implementation. Thus, should Hesperia decide to acquire a group of six hotels, these can become fully integrated into Hesperia within less than two months instead of a year.
- ☑ *Reduction in accounting support staff per hotel.* Four new hotels now result in one additional central accounting employee whereas previously they would have resulted in five.
- ☑ *Faster performance of key processes.* For example, the month-end procedure now takes five working days as opposed to ten before SAP, while the annual consolidation of accounts takes four working days compared with twenty before.
- ☑ *Revenue per available room*, which is the most important indicator in the hotel industry, *has improved since implementation*, partly because of SAP, and partly because of both an increase in sales and service staff and hotel refurbishments.

Taken over ten years, the post-tax financial impact of implementing SAP R/3 and Simhotel can be summarized as follows:

- ☑ The return on investment (internal rate of return after taxes) will be 20%
- ☑ The initial investment will pay itself back after a period of 68 months or 5.7 years
- ☑ The main savings result from staff reassignment and cost avoidance from centralizing accounting and IT, improved volume purchase efficiencies, scrapping legacy systems, and faster execution of internal processes

IN THIS STUDY

Introduction

Hoteles Hesperia is a hotel chain with more than 3,000 employees working in 47 three, four and five-star hotels, located throughout Spain and in the U.K., Belgium, Andorra, and Venezuela. The privately owned company has its headquarters in Barcelona, Spain, and had total revenues of €171 million in 2004 with an EBITDA (earnings before interest, taxes, depreciation, and amortization) of €29 million. The chain has been expanding aggressively over the last five years and expects the process to continue in the years to come.

Challenges

By 2001, the increasingly saturated Spanish hotel market required a larger scale if hotels were to maintain profit margins. Hoteles Hesperia's growth path, fueled by the acquisition of struggling hotel chains in Spain, enabled it to increase its volume and reap economies of scale.

However, a number of factors inhibited this expansion strategy:

- ☒ *Slow integration of hotels acquired into the chain.* Hoteles Hesperia had to implement its own business applications in every newly acquired hotel, hire qualified local accounting personnel and train them in the new business applications and accounting procedures. Integrating a new hotel into Hoteles Hesperia was typically a two-month project. These time-consuming integration projects severely limited the chains acquisition opportunities.
- ☒ *Lack of current and consistent information for central management* Individual hotels reported results monthly and the central administration consolidated results on a bi-annual basis. It was difficult for management to monitor and benchmark the operational and financial performance of the individual hotels. Furthermore, answering questions such as "what was the average price per room this month?" or "what are total purchases from supplier X year to date?" was very difficult and time consuming.
- ☒ *Lack of timely and relevant operational data for individual hotel managers.* The legacy applications did not support hotel managers in their day-to-day decision-making or in the planning process. As the manager of the five-star Hesperia Tower, Reinhard Wall, explains: "We based many critical pricing and purchasing decisions on assumptions and gut feeling rather than on concrete facts."
- ☒ *High cost of maintaining existing business applications.* These applications — DATISA for back office, Lanmark for hotel operations, and Squirrel for point of sale — were not integrated and were reaching maximum capacity. When the Lanmark application was taken off the market, support deteriorated. Furthermore, the proprietary code of the applications was difficult or impossible to modify. Moreover, the fact that these applications were implemented and operated locally in each hotel limited overall IT operating efficiencies.

Solution

In the fall of 2001, Hoteles Hesperia and the consulting arm of its certified public accountants, BearingPoint, formalized a project to replace the local legacy systems with a single integrated, centralized solution covering both the back-office functions, such as accounting, procurement and human resources, and the front-office functions related to hotel operations.

At the time, the idea of having no local business applications in the individual hotel was controversial. Critics pointed to the risks of communication failure, which would leave hotels with no application access, and to the difficulty of central administration accommodating local IT needs. However, high-availability broadband connections were becoming available in Spain at reasonable prices. Top management was determined to centralize accounting and IT in order to have a real-time view of hotel operations and be able to integrate new hotels rapidly.

Evaluation Process

For the back-office functions, the project team considered SAP R/3 and Microsoft Business Solutions Navision. SAP R/3 was selected on the basis of a recommendation from BearingPoint due to SAP's strong European presence, broad functional coverage, and the availability of SAP skills at BearingPoint.

The team also evaluated four different front-office solutions: Simhotel from Spain-based CCS, Opera Enterprise Solution and Fidelio Financials from U.S.-based Micros, Ulyses from Spain-based ITS, and Medallion from U.S.-based Softbrands, which is the successor to the previous hotel management solution, Lanmark. A formal evaluation process rated several of the vendors highly in terms of functionality, maturity, and references.

Finally the team selected Simhotel because of its built-in integration with SAP, which was real-time and certified by SAP. Additionally, because Simhotel was built as a SAP module, it provided the best support for the vision of a single, centrally-hosted solution. Moreover, the team selected Simhotel because it was considered simple to customize and adapt due to its use of the SAP language, ABAP/4.

The team selected Simhotel even though the product had been launched relatively recently, did not at that time cover auxiliary areas such as spas and events, and had only been implemented in a chain of five hotels in Valencia. The upside of these issues was that CCS was prepared to allow Hoteles Hesperia a central role in determining the current and future functional coverage of the product. This influence on the overall product direction of Simhotel was another important reason for choosing it.

Implementation Process

In January 2002, implementation kicked off with a 14-person team, equivalent to 8 full-time staff. The team was made up of members of the IT department, finance, purchasing, accounting, and hotel operations. Its members also included consultants from BearingPoint. It was supervised by a steering committee headed by the CEO, Javier Illa.

The entire project was planned to take 13 months. The team spent the first 14 weeks defining the 15 core business processes, 5 of which were considered critical. In April, after the initial process definition phase, two parallel project tracks were initiated. One focused on implementing back-office functionality in SAP R/3, the other on working with CCS to implement all the required enhancements to Simhotel. This process took approximately 7 months.

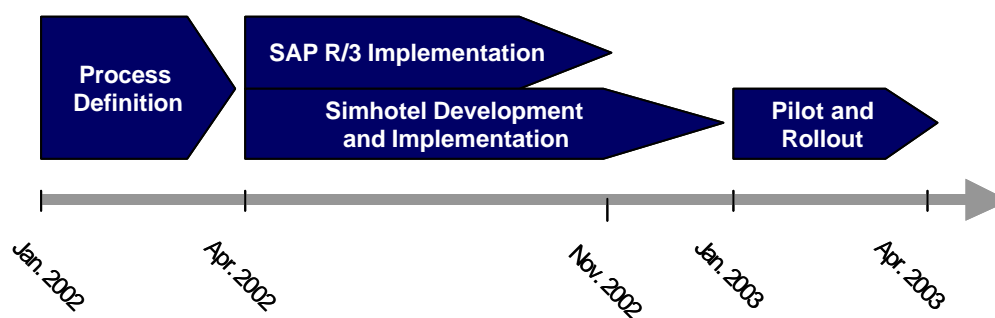
A three-month rollout phase was planned to begin in November 2002 after 7 months of implementation. The back-office SAP R/3 went live in November 2002 as planned. However, the team decided to postpone the Simhotel rollout phase by three months, which began in January 2003 instead of November 2002. The rollout phase ended in April 2003 instead of January 2003.

This three-month delay resulted partly from unexpected factors, such as the large numbers of improvements to Simhotel and complexities in defining processes and data models, and partly from changes in the original scope of the project. For example, the team decided to include more hotels in the initial rollout than planned and to have a higher rate of knowledge transfer from BearingPoint than planned.

The initial implementation budget was exceeded considerably, mostly because the original scope was expanded with new modules such as HR. The CEO of Hoteles Hesperia, Javier Illa, explains: "The budget overrun was approved because we made certain changes to the original plans. We did not want to get caught between two systems, so our top priority was to proceed as fast as possible. There was no turning back."

FIGURE 1

Implementation Timeline



Source: IDC, 2005

At the beginning of the project BearingPoint did not have deep knowledge of core processes in the hospitality industry. However, industry knowledge was not crucial to Hoteles Hesperia. Instead, the chain mainly used BearingPoint for implementation methodology and process skills, structured analysis of business processes, and functional and technical knowledge of SAP.

Currently, all of Hoteles Hesperia's 41 hotels in Spain and Andorra run SAP R/3 and Simhotel. The six international hotels were not included in the original scope of the implementation due to country-related differences in areas such as taxes, accounting, and payroll. Further rollout is planned to three hotels located in Belgium and U.K. for 2006.

Implementation Challenges

The implementation team encountered several challenges during the project:

- ☒ *Unexpected high number of new requirements to the Simhotel solution.* When planning the project, the team expected significant new developments from CCS to accommodate new requirements by Hoteles Hesperia. However, the number and scope of new requirements exceeded initial expectations, which meant that Simhotel development was finalized in October instead of May 2002.
- ☒ *Unplanned difficulties in establishing common process descriptions and data models across the chain.* Many hotels had their own ways of handling processes such as procurement and invoicing. Establishing a common process and data model is a highly complex task that has a significant impact on the daily operations of the individual hotels.

Benefits

The primary objectives of the decision to change business applications and centralize accounting and IT were strategic. Management wanted streamlined, easy-to-implement support operations to back up growth through planned construction and opportunistic acquisitions. Furthermore, they were looking to centralized support operations to leverage economies of scale in the increasingly saturated and competitive Spanish hotel market. Finally, they wanted consolidated, real-time data in order to make fact-based decisions on tactical and strategic issues.

General manager Ramón Aragonés describes the change: "This implementation has really changed the view we have from head office. Before, we had to visit a hotel personally to understand how it was doing; now we have the operational information available, of good quality and in real-time." Controller Max Nesweda summarizes the position as follows: "With SAP R/3 and Simhotel, we became a chain instead of a group of hotels."

Hotel manager Reinhard Wall concludes: "Pricing in the hotel business is extremely complex and dynamic. Our ability to make the right decisions on pricing a certain room category to a particular sales channel, such as a travel agent, a hotel portal, or a certain type of customer, depending on the number of available rooms, season, and other factors is crucial to success. The combined SAP R/3 and Simhotel solution enables us to react faster on real-time information and involve more people in these daily business decisions. Furthermore, solid operational data and the ability to drill down, track KPIs, and create useful reports are critical when making strategy plans for individual hotels."

Key Performance Indicators

Key performance indicators of the strategic objectives have improved since the go-live in April 2003:

- ☒ *Accelerated integration of new or acquired hotels into the chain.* It takes one week to implement and configure the SAP R/3/Simhotel applications and train staff as against eight weeks before the SAP implementation. Thus, should Hesperia decide to acquire a group of six hotels, these can be fully integrated into Hesperia within less than two months instead of a year.
- ☒ *Reduction of accounting support staff per hotel.* Currently four additional hotels result in one additional central accounting employee whereas before they would result in five. In other words, productivity per additional accounting employee has increased five times.
- ☒ *Faster execution of key processes.* For example, the month-end procedure takes five working days as against ten before SAP, and the annual consolidation of accounts now takes four working days compared with twenty before. After implementing SAP R/3, Hoteles Hesperia consolidates accounts monthly instead of annually, which significantly improves the information available to top management.
- ☒ *Revenue per available room*, which is the most important indicator in the hotel industry, *has improved since implementation*, partly because of SAP, and partly because of both an increase in sales and service staff and hotel refurbishments
- ☒ *Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) as a percentage of revenues improved by 2.1 percentage points from 2003 to 2004.* The EBITDA as a percentage of revenues was 16.7% in 2004. This improvement is the result of a number of factors, but it serves to indicate the overall profitability of the chain.

Return on Investment

Hoteles Hesperia's SAP implementation is expected to break even by the end of 2008, 68 months after the initial rollout. Over a period of ten years, the investment will have generated €1,970,000 at net present value after tax. This corresponds to an annual return after tax of 20%.

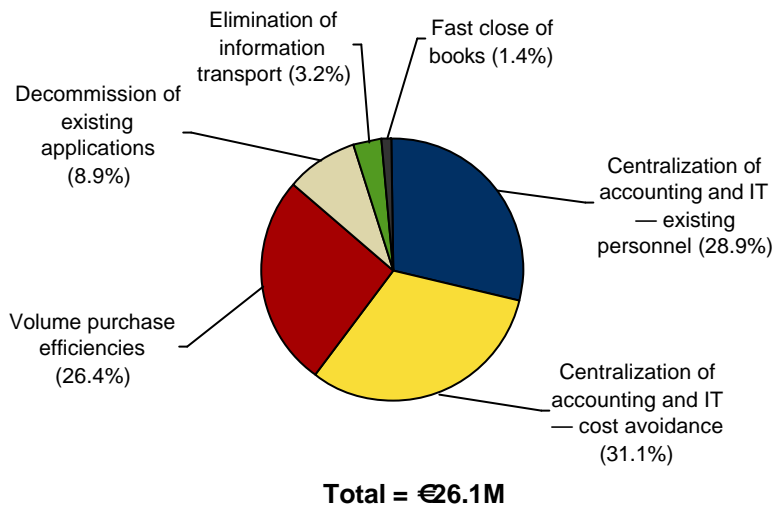
The benefits driving these results arise mainly from savings in accounting and IT staff following centralization of these functions. Each local accounting employee was quite highly qualified and well paid due to the diversity of tasks at each hotel. In the central accounting department more junior, lower-paid staff were hired since each position involved fewer tasks. Furthermore, the number of accountants per hotel was reduced significantly following the centralization, further reducing payroll costs.

Since go-live in April 2003, the chain has acquired 10 new hotels and is soon to launch another 4. These additional hotels have led to only a limited increase in central accounting staff enabling the chain to avoid substantial payroll costs for local accountants.

Additionally, the chain has been able to increase the volume discounts from key suppliers dramatically, because the SAP software allows complete documentation of purchases by supplier. Finally, several other benefits generate savings, as shown in Figure 2.

FIGURE 2

SAP R/3 and Simhotel Benefit Breakdown by Type



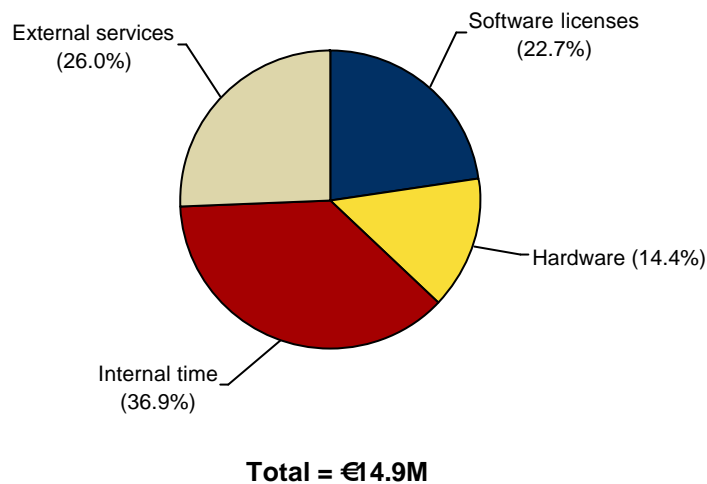
Source: IDC, 2005

On the cost side, external services and software each make up approximately a quarter of the total cost over the 10-year analysis period. More than 60% of the cost of external services relates to BearingPoint's initial implementation support while the remainder is for maintenance services from CCS. About half of the software cost is attributable to Simhotel, 20% to SAP R/3, and 27% to middleware, such as Microsoft SQL server and IBM MQSeries, together with additional niche applications such as MIS InVision business intelligence tool, Ideas yield management application, XRT treasury application, and Maitre POS applications. Hardware is the smallest category, as is normal when implementing this type of complex application. The hardware platform used was IBM xSeries servers with the Microsoft Windows operating system.

The largest cost category is internal time. This results partially from the internally driven process definition portion of the project, but is mainly because the project bears the full burden of the new central application department. The cost breakdown is shown in Figure 3.

FIGURE 3

SAP R/3 and Simhotel Cost Breakdown by Type



Source: IDC, 2005

The ROI analysis for Hoteles Hesperia is relatively conservative, because IDC chose not to factor in future growth, although the chain has grown by at least four hotels annually and expects to continue to do so. The decision to keep the ROI calculation static was made in order to avoid making hypothetical assumptions and to ensure valid and reliable results. Incorporating the chain's forecast annual growth of four hotels would have more than doubled the ten-year post-tax NPV.

Furthermore, a number of benefits could not be quantified as savings due to a lack of data. These unquantified benefits include significant reductions in bad debts, simplification of the inter-company invoicing process, improved cost control due to stronger enforcement of accounting rules for expenses, significant reduction in payroll errors, and lower unit prices in purchasing due to a better bargaining position.

Lessons Learned

Looking back on the SAP implementation, Hoteles Hesperia has learned a number of lessons:

- ☑ Strong operational knowledge within the implementation team proved very valuable. The project manager from Hoteles Hesperia, Rufino Perez, had previously worked on implementing the legacy applications in the new hotels acquired by the chain. His intimate acquaintance with the day-to-day challenges of hotel management lent the implementation team added credibility and valuable knowledge.

- ☒ Resistance to change from local hotel managers was less than originally expected. Handing over the IT and accounting function from local management to a new central department was expected to cause controversy. However, only a few hotels objected to the initial plans. Resistance was partly eliminated by giving hotel managers visibility and influence over the change process. As Javier Illa explains: "With the new application platform, local employees feel that they work for a chain rather than an individual hotel. Most people take pride in that."

Future Plans

Hoteles Hesperia now has accounting, controlling, purchasing, invoicing, inventory, human resources, corrective maintenance, and the core hotel processes in place.

The next steps include:

- ☒ Integration between the combined SAP R/3 and Simhotel solution with a custom-developed CRM application. The CRM application will also be managing customer self-service applications, service quality management, and contract management during 2005.
- ☒ Implementation of recently developed modules in Simhotel covering additional hospitality areas, principally spa facilities, events, and catering during 2005.
- ☒ Implementation of SAP's preventive maintenance module to complement the corrective maintenance functionality already implemented during 2005.
- ☒ Rollout of SAP R/3 and Simhotel in the chain's Belgian and U.K. hotels during 2006.
- ☒ Integration between the combined SAP R/3 and Simhotel solution and outside channel partners, such as global travel distribution systems, Internet travel portals, and major travel agencies during 2006.
- ☒ Improved implementation of the SAP NetWeaver Business Intelligence component in the areas of purchasing and human resources in 2006.

Appendix: ROI Details

The objective of the ROI analysis is to demonstrate and quantify the value of a software solution, based on observed and quantified data.

IDC applies certain assumptions across SAP ROI case studies to ensure comparable results:

- ☒ *An average corporate tax rate of 40%.* Most European countries have corporate tax rates in the range of 30% to 40%. IDC has selected 40% to ensure a conservative, yet comparable post-tax view of the net benefits of a software solution.
- ☒ *A discount rate of 10%.* The 10% rate reflects an average cost of capital of approximately 5% plus an added risk premium of five percentage points. The risk premium reflects the fact that projected cash flows may change due to unforeseen developments and events.

The analysis period of this case study is 10 years, which differs from the normal one of five years. Research shows that investments in ERP applications have useful lives in the five- to ten-year range, depending on the industry, application area, and size of organization. The decision to apply a ten-year analysis period was made on the basis of the all-encompassing and strategic nature of the implementation at Hoteles Hesperia.

After conducting many on-site interviews, IDC applied the incremental, observed, and quantifiable costs and benefits in an ROI calculation. The results are shown in Table 1.

The ROI of 20% was calculated using the internal rate of return method and represents the average annual rate of return after taxes. It is comparable to the annual after-tax yield of investment alternatives, such as stocks and bonds.

The net present value after taxes of €1,970,000 represents the net benefit of the entire project to Hoteles Hesperia in today's money. The project added €1,970,000 to the total market value of Hoteles Hesperia, assuming a transparent equity market.

TABLE 1

ROI Calculation

Common Assumptions											
Average Corporate Tax Rate	40%										
Discount Rate	10%										
Cash Flows (€M)	Initial	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
Net Cash Flow After Taxes	-3.71	0.29	0.88	1.21	1.19	1.00	1.00	1.00	1.00	1.00	1.00
Discounted Net Cash Flow After Taxes	-3.71	0.27	0.73	0.91	0.82	0.62	0.56	0.51	0.47	0.42	0.39
Cumulative Discounted Net Cash Flow After Taxes	-3.71	-3.45	-2.72	-1.81	-1.00	-0.38	0.19	0.70	1.16	1.59	1.97
Annual Rate of Return After Taxes (%)	20%										
Ten-Year Net Present Value After Taxes (€M)	1.97										

Source: IDC, 2005

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