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Holland America Line and the Global Economy in 2009[1]

In recent months the global economy has suffered a major downturn. Few countries and few industries have escaped the effects. The uncertainty created by the financial crisis has led to a steep drop in consumption.

A Seattle-based cruise line, Holland America Line (HAL), is a wholly owned subsidiary of Carnival Corporation & PLC, a dual listed company on the New York and London Stock exchanges. HAL seeks your input in analyzing their current position and in developing strategies that can be implemented during and after the current global recession.

Cruises in general are viewed as luxury goods, and this category of consumption is experiencing negative impacts from falling stock and housing prices. Rick Meadows, Executive Vice President for Sales & Guest Programs, and his marketing team at HAL are an upbeat group. Operating out of utilitarian offices on Seattle's waterfront, they are focused on bringing the cruising experience to an ever-expanding market. However, the global economy is creating challenges in the short and medium run.

Holland America Line and the cruise industry

Cruising is a unique combination of vacation and entertainment which includes travel, food and accommodation in the basic price; it accounts for approximately 5% of the world vacation market.[2] Cruise brands are generally classified into three broad categories: contemporary, premium and luxury. Contemporary cruises are usually on larger ships for shorter periods of time (typically up to seven days), and they are the most casual. Premium cruises are usually on intermediate-sized ships for longer periods, and they tend to appeal to more experienced cruise passengers who are more affluent and older. This category offers more comfort and style and is more destination-focused; it also costs more than the contemporary category. A luxury cruise is usually on a small vessel, with high standards of accommodation and service, exotic itineraries, and the highest price tag.[3]

HAL is in the premium category, but some of the company's products are close to the luxury category (for example, a four-month world cruise, or some of the top level accommodations on standard cruises). When asked to name comparable premium brands in other industries, the HAL marketing team cites BMW and Mercedes.

Carnival Corporation has about half of the world market for cruises. RCI (Royal Caribbean) has 30%, and Norwegian Cruise Lines accounts for 10%. As of 2009, Carnival operates 88 cruise ships in North America, Europe, Australia, and New Zealand. The company was founded in 1974 and is headquartered in Miami, Florida. The Carnival brands include Carnival Cruise Lines, Princess, Cunard, Costa, Seaborne, and Holland America. Carnival acquired Holland America in 1989.

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[1] This case was written for the 2009 Global Business Case Competition by Helen Adams, Lecturer, and Debra Glassman, Senior Lecturer, both from the Michael G. Foster School of Business at the University of Washington. It is intended to serve as a basis for student analysis rather than to illustrate either effective or ineffective handling of an administrative situation. Copyright © Adams & Glassman, 2009. All rights reserved.
[2] "Cruise Inc. – State of the Industry," CNBC, www.cnbc.com, March 16, 2009.
[3] Associated Press, "Earnings Preview: Carnival Corp." March 20, 2009, http://news.moneycentral.msn.com.

The largest sources of revenue for a cruise line are passenger ticket revenue and on-board spending. The major sources of on-board spending on a cruise include bars and casinos, spa treatments, and shore excursions. Norwegian Cruise Lines estimates that one quarter of its revenue comes from on-board spending.[4] This spending is projected quite precisely. For example, Norwegian calculated that a cruise on the Norwegian Pearl needed to sell $7.25 of drinks per guest per day in order to break even in that category of on-board spending.[5]

The main costs of running a cruise line are largely fixed – the ship and its operations (including fuel, crew, and port calls). Rick Meadows observes that, "As a fixed cost business, we have to fill every bed. We are like an airline in that respect and unlike hotels."[6]

Capacity in the industry is defined as two berths per cabin. HAL has 794 to 2,124 berths per ship. Since some cabins have 3 or 4 berths, it is possible to be over 100% capacity, and this is a frequent situation.

The variable costs for a cruise line include food and hotel supplies, and there are large economies of scale in these areas.

> Food is a major marketing tool [for cruise lines]...Food budgets...are staggering. Royal Caribbean's The Voyager of the Seas can carry as many as 3,800 passengers and among its provisions for a week-long cruise are 15,000 apples, 1,270 kilos of bacon, 725 kilos of breakfast sausages, 120,000 eggs, 4,500 bottles of champagne and wine, 860 kilos of ham, 5,300 litres of ice cream and sherbet and 10,000 steaks. The weekly food bill can run to $350,000.
>
> And yet, costs of wining and dining passengers seem remarkably low; bulk buying obviously helps. The ultra-luxury Radisson Diamond averaged $23 per passenger per day for food and $6 for beverages on its transatlantic cruise last year.[7]

Travel agents are the primary distribution system for cruise lines. For instance, over 85% of HAL cruises are booked through travel agencies. Rick Meadows says, "It's not unlike the auto industry – you go through a dealer. Airlines and hotels are much more direct to consumer." HAL has long-standing relationships with travel agents. As Meadows describes,

> [I]t's a delicate balance to make sure we keep the primary distribution system healthy. We try to be as easy to work with as possible and let the consumer choose whether to work through a traditional travel agent or work directly with us. We have to be concerned with the health and happiness of travel agents.
>
> We have a formidable sales organization working with travel agents - over 45 sales people in the field and over 100 in the Seattle office.

For Carnival Corporation, the major source of world cruise passengers is North America, which accounts for 66%. Cruises are less popular in Europe, and even less so in Asia, the south Pacific and South America.[8]

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[4] "Cruise Inc.," CNBC, www.cnbc.com, March 24, 2009.
[5] Ibid.
[6] Unless otherwise indicated, all quotes from HAL personnel are from an interview on March 4, 2009.
[7] Michael Hanlon, "Death by Chocolate and other things cruise lines won't tell you," Toronto Star, September 15, 2001.
[8] Carnival Corporation & PLC, 2008 10-K, p.5.

In the industry, cruise passengers average 46 years of age, with above-average annual household income ($93,000).[9] Due to the aging baby-boom generation and improved healthcare, in the ten years from 2005 to 2015, the primary cruise passenger age group (45 years and older) is expected to grow 20% in the US and Canada, and 15% in major western European countries. This provides a growth opportunity for the cruise industry.[10]

Dean Knutson, Market Research Manager, describes the breakdown of new and repeat passengers for HAL:

> It is quite consistent. In the aggregate, about 25% of cruisers are first-timers; 40-45% repeat (at rate of about once every 2 years); and the rest are "alumni" of other cruise lines.

Rick Meadows adds, "Our number of repeaters is unusually high for the industry. The repeaters are fiercely loyal."

However, counterbalancing the anticipated growth in the passenger population are inherent risks in economic and business conditions. Fuel price increases are a major cost; down-turns in financial markets may impact potential passengers' willingness to spend on cruises; other factors may also reduce demand.

Rick Meadows notes that the cruise industry is more flexible in responding to external conditions than other parts of the travel industry. In general, cruises are designed years ahead (as of March 2009, HAL had finished its 2010 planning and was working on 2011). However,

> The beauty of our industry is that ships move. When we look a year out, we still can move [ships] around. It's a very fluid thing. We can redeploy ships to take advantage of what's happening in the market. For example, if international travel falls, we can deploy more ships out of North America. If international travel picks up, we can reverse this. That's a big edge for us.

Beth Humenik, Director of Europe & Voyage Product Marketing, adds, "A good example of redeployment is after 9/11. We moved ships closer in. Passengers did not have to fly to take a cruise leaving from a nearby US port."

A global recession

In the first half of 2007, the US economic expansion, which had begun in 2001, was running out of steam. This was not unexpected six years into a business cycle, and leading indicators suggested a recession was possible. The Federal Reserve was keeping short-term interest rates high, while home-building and house prices were both falling.

If the US had fallen into a "normal" recession, the economic downturn might have been contained. Indeed, many believed that the US economy would have a "soft landing," and that the rest of the world's economies would be "decoupled" from the US downturn. In the summer of 2007, the subprime mortgage crisis made it clear that the US downturn would be worsened by the financial

[9] Cruise Lines International Association, "Profile of the U.S. Cruise Industry," www.cruising.org/Press/sourcebook2009/.
[10] Carnival Corporation & PLC, 2008 10-K.

sector difficulties. What started as a moderate decline accelerated dramatically and spread internationally with the credit crunch in the fall of 2008. Housing bubble burst, stock markets plunged, and countries fell into recession one after another like dominoes. [11] Using its own definition of a recession, the National Bureau of Economic Research subsequently declared that the US business cycle peak was reached in December 2007.

There are strong indications that the recession will be long and deep. In the 4th quarter of 2008, US real GDP fell at a 6.2% annual rate.[12] By March 2009, the US unemployment rate had risen to 8.5%. The combination of economic decline and the threat of deflation had observers making comparisons to Japan's "Lost Decade" and the Great Depression. Exhibit 1 compares the current recession to previous ones. Harvard Professor Robert J. Barro comments,

> The most serious concern is that the downturn will become something worse than the largest recession of the post-World War II period -- 1982, when real per capita GDP fell by 3% and the unemployment rate peaked at nearly 11%. Could we even experience a depression (defined as a decline in per-person GDP or consumption by 10% or more)? [13]

The decreases in macroeconomic indicators in the fourth quarter of 2008 were so severe that many observers used the same metaphor: falling off a cliff. Exhibit 2, which presents industrial production in key regions, clearly shows this pattern. Exhibits 3 and 4 show similarly severe declines for US auto sales and retail sales.

Economists at Morgan Stanley in London further point to

> ... the transmission of shocks around the world from a vertiginous drop in global trade, which according to the available data for January and partial data for February has continued in the first quarter. Our proxy of global exports was down by almost 25% from a year ago in January... It therefore comes as no surprise that export champions such as Japan and Germany are hit especially hard and will likely see the biggest GDP contractions among the major economies this year.[14]

Observers also note country-to-country variations:

> Part of the uniqueness of the current economic turmoil around the world is that many countries are experiencing the same deep recession, but the cause of it varies dramatically from one country to another.[15]

Aggregate consumption is negatively affected by a fall in income, and unemployment adds further negative effects, due to expectations of lower future incomes (see Exhibit 5). The collapse of house

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[11] For example, Ireland was the first euro-zone country to enter recession, in September 2008. The euro-zone as a whole was pronounced to be in recession after the 3rd quarter of 2008. The UK officially entered recession in the 4th quarter of 2008. These determinations were based on the popular definition of a recession being at least two consecutive quarters of negative real GDP growth.
[12] US Bureau of Economic Analysis, www.bea.gov.
[13] Wall Street Journal, March 4, 2009. He references a study co-authored with Jose Ursua for the NBER, "Stock-Market Crashes and Depressions."
[14] Joachim Fels, "Still Sinking and Synching," March 20, 2009.
[15] "Multitude of reasons for recession," Sunday Business Post, April 12, 2009.

prices (Exhibit 6) and the sharp fall in stock prices (Exhibit 7) creates a negative "wealth effect" that further reduces consumption.[16] US households lost 9% of their wealth (a total of $5.1 trillion) in the last quarter of 2008. The value of US residential real estate fell 4% in the same period. Consumption is also negatively affected by uncertainty. The US Consumer Confidence Index fell from 76.4 in February 2008 to 25.0 in February 2009, the latter number being an all-time low.[17]

Markets for luxury goods and travel

In economics, the term "luxury good" means something that a consumer buys proportionately more of as his/her income rises; i.e., the income elasticity of demand is positive and greater than one. Vacation travel is an example of a luxury good.

The effects on consumption by high income households are particularly pronounced in this recession, as job losses are hitting "white collar" jobs in industries such as financial services, along with the sharp decline in portfolio wealth.

> The loss of wealth is concentrated among the most affluent Americans, in large part because they own more stocks and bonds than the rest of the country...As a result of their greater wealth and higher incomes, the affluent tend to spend a lot more than their share of the population would imply. The top 20 percent of income earners spend more than the bottom 60 percent of income earners...[18]

Like other sectors, luxury goods sales tend to fall during recessions, as incomes fall. The very high-end goods are often thought to be more recession-proof, because very rich people are more likely to depend on wealth-generated income rather than on earned income. However, the very rich are particularly sensitive to a sharp fall in the stock market, which has also occurred.

In the US,

> Faced with the sharpest decline in net worth in nearly 50 years, wealthy Americans are re-evaluating their priorities and slashing their spending at a rate unseen in decades - a move that could have dire consequences for the economy, luxury stores and high-end brands...
>
> Luxury sales overall dropped 34.5 percent in the first week of December from the same period a year ago, according to SpendingPulse, a data service provided by MasterCard Advisors, and were down 23 percent in the five weeks ending Dec. 6...
>
> "This is no longer a state of mind, or what feels right," said luxury consultant Robert Burke. "This is a reality of where people's bank accounts and investment portfolios are."
>
> Offering deep discounts can cost high-end retailers beyond falling profits, risking the cachet of their brands. Retailers may also confront problems trying to raise

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[16] "According to Federal Reserve estimates, every $1 increase in housing wealth stimulates 15 cents in consumer spending, but a $1 gain in investor wealth produces only 3 to 5 cents." Lauren Coleman-Lochner, "Caution Rules Consumers' Thinking as Dow Plummets," Knight Ridder Tribune Business News, August 12, 2002.
[17] "The Conference Board Consumer Confidence Index™ Plummets Further in February" *February 24, 2009*
[18] Vikas Bajaj, "Household Wealth Falls by Trillions," New York Times, March 13, 2009.

> prices once the economy improves as consumers accustomed to deep discounts balk at buying items at regular prices.[19]

Accordingly, some retailers of luxury goods are choosing alternatives to price discounts, such as loyalty reward programs or special events for good customers.[20]

Globally, as of October, 2008:

> [T]he worldwide luxury goods market, once thought immune to the ebbs and flows of economic fluctuations, has begun to feel the effects of the worldwide economic slowdown and will likely enter a recession in 2009, this according to the results released today of the 7th edition of Bain & Company's Luxury Goods Worldwide Market Study. ...Turning to 2009, luxury faces its first recession in six years, as exchange rate fluctuations and economic turbulence eat into the confidence of many luxury consumers in mature markets. The study predicts as much as a -7% decline in global luxury sales for 2009 using constant exchange rates...[21]

The uncertainty in the present economic climate is such that even consumers who can afford to spend are cutting back. A deeper psychological response may also be at work – a backlash against "conspicuous consumption." A writer in the Washington Post observes, "frugal living is the new glamorous."[22] In Florida, where tourism is a major industry, the following was recently reported:

> Luxury resorts are accustomed to unusual requests. But Amelia Island Plantation was surprised to get this one from a corporate event planner worried about a function appearing too extravagant: could the resort drop the word "island" from its address?[23]

Some observers point to the post-Great-Depression generation as a possible parallel. This generation was notably frugal – the experience of the Depression led them to save a lot and avoid debt. Perhaps this will have long lasting effects on consumer behavior.

> We've all known people who, having survived the 1930s, never lost their Depression habits of frugality. And so it will be again. ... but even after the economy recovers, deciding to forego that third car or fifth TV or imperial master bathroom or marginally cooler laptop will come more naturally.[24]

An article in the Financial Times adds:

> A recent survey of 500 people in the US, the UK and France pointed to a shift to "value" combined with a desire for "voluntary simplicity". And consumer anthropologists suggest Americans will seek to "un-stuff" their lives, and focus more on the community.[25]

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[19] D'Innocenzio, Anne, "Rich are tightening their Gucci belts this year," St. Louis Post - Dispatch, Dec 26, 2008.

[20] See, for example, Ashley M. Heher, "The Must-Haves Come at a Price," The Star-Ledger, January 27, 2009.

[21] Business Wire 2008, October 29, 2008.

[22] Kelly Marages, "I'm Not Buying Recession Chic," The Washington Post, March 15, 2009

[23] Alex Roth, "Austerity Tide Hits Florida Beaches", Wall Street Journal, March 17, 2009.

[24] Kurt Anderson, "Don't pretend we didn't see this coming for a long, long time," Time Magazine, April 6, 2009.

[25] Jonathan Birchall, "'New' US shopper to emerge from crisis," FT.com, April 8, 2009.

Mary Beth Wressell, Senior Manager for Advertising & Promotion at HAL comments that the post-Depression generation had a sense of vulnerability that may not be present today. She suggests that today the philosophy may be: "life's short, so eat dessert first," quite different than the reaction to the Depression.[26]

Recently, designer goods have suffered profit declines and there has been deep discounting to move high levels of inventory and to generate cash flows. Smaller designer retailers have filed for bankruptcy. Many firms in the US and worldwide have declined to provide the usual sales forecasts due to the economic uncertainty.[27]

LVMH Moet Hennessy Louis Vuitton SA is often considered a bellwether for the luxury-goods industry. For 2008, sales increased 4% for the Paris-based group, the world's biggest luxury retailer, and full-year profit was flat.[28] These results are strong relative to other firms in this global luxury goods industry. Cartier recorded a 7% decrease in sales in the fourth quarter of 2008 and Italian jeweler Bulgari SpA said sales fell 10% in the same period.[29]

Sales for all luxury auto brands were down across the board for 2008. In 2009 the luxury segment of the auto industry is expected to fall below 1 million units sold for the first time since 1996, according to a forecast by Global Insight.[30]

Daimler-Benz CEO Dieter Zetsche says the collapse of luxury auto sales in the fourth quarter surprised him. "Usually, luxury car sales drop a few months after a financial event like we had, but this time it was immediate." Further, he says,

> People don't trade out of brands like Mercedes-Benz easily....We have the highest loyalty rate in the industry. About 40% of Mercedes buyers in the U.S. are over 50 years old, which is the demographic most likely to be rethinking big-ticket purchases as they get nearer to retirement with depleted savings.[31]

One typical response during a recession is for companies to give consumers a reason to spend by emphasizing value. This is the strategy currently being pursued by Starbucks, for example.[32]

> "Value" advertising has typically flourished in downturns, says David Court, leader of the global marketing and sales practice at McKinsey & Co., but it can be a tricky sell. "Advertising works best when the message is incredibly simple," Mr. Court says. "The concept of value is a more difficult thing for the consumer to understand than 'Get a brand I know on sale.'"[33]

As a result of the recession, consumers are cutting back on discretionary spending and "trading down" to less expensive choices. This is true in the travel industry, as well. But Rick Meadows thinks that consumers are combining "trading down" with "trading up", too:

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[26] For a discussion of a variety of consumer responses to recession, see John A. Quelch and Katherine E. Jocz, "Keeping a keen eye on consumer behaviour," Financial Times, February 5, 2009.
[27] Miguel Bustillo, "Retailers Stop Making Sales Forecasts", Wall Street Journal, Feb 6, 2009.
[28] Max Colchester, "LVMH's Diverse Portfolio Buoyed '08 Sales, Profit," Wall Street Journal, Feb 6, 2009.
[29] Ibid.
[30] Sales tracking firm Autodata said sales last year were 1.19 million units, down 21% from 2007 when sales were 1.41 million. Luxury sales have been as high as over 1.5 million in recent years. (David Kiley, "Luxury Car Sales Keep Skidding", BusinessWeek.com, January 13, 2009.)
[31] Ibid.
[32] Janet Adamy, "Starbucks counters pricey image," Wall Street Journal Europe, February 10, 2009.
[33] Juliet Chung, "Coffee gets stepped in value marketing," Wall Street Journal Europe, January 20, 2009.

> There's a new notion of "trading up" and "trading down." Trading down is when some guests may go in a veranda instead of a suite, or they choose an inside instead of an outside cabin. But they've traded up to take the cruise itself.

There is a sentiment in the industry that vacations, once considered a "privilege," are now more of a "right." People who feel they work hard, believe that they have earned the vacation.

While some travel industry organizations and most of the cruise lines remain optimistic about their prospects in the current economic downturn, there is disagreement on this from various sources.

One observer recently commented,

> Both Royal Caribbean and Carnival Cruise ... the two dominant cruise providers, have suffered a downturn in their businesses, which were growing over the years by offering vacationers a luxurious vacation at affordable prices. Unfortunately, bookings had been sinking before the "wave season," the popular January through March months, where people head out of bleak winter habitats to head for warmer locales. The hopeful - or at least less gloomy - prospect for the industry is that the falloff in bookings may have leveled off, even though 2009 should remain difficult overall. Indeed, Carnival Cruise is making much of offering "early booking" discounts.[34]

Another analysis noted,

> As demonstrated by first-quarter results from Carnival on Tuesday, cruising is as susceptible to recession as any other consumer-orientated industry...The problem is that cruising competes against all other holiday destinations available, and retirees living on interest income will feel the impact of the credit crunch. Cruising does not suffer the absence of corporate bookings affecting the hotel sector, but the downward pressure on prices drives down profits for the entire travel industry.[35]

Carnival Corporation - Analysts' forecasts

Carnival Corporation's income statement and balance sheet are presented in Exhibits 8 and 9.

Given the current economic uncertainty, it is not surprising that analysts have widely differing opinions about the cruise industry. Carnival had predicted its first-quarter earnings for 2009 would amount to 20 to 22 cents per share, while analysts polled by Thomson Reuters forecasted earnings of 19 cents per share on revenue of $2.87 billion.[36] Yet Barclays Capital analyst Felicia Hendrix predicted Carnival's first-quarter earnings at 5 cents per share — far short of consensus and the company's forecast — to reflect the much lower revenue produced by last-minute

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[34] Greg Sushinsky, "Cruise Lines Battered But Not Sunk (RCL, CCL)," February 23, 2009, http://community.investopedia.com/news.
[35] "Carnival," Financial Times, March 25, 2009. See also Exhibit 10.
[36] Ibid.

bookings.[37] This large range of analysts' forecasts is consistent with the current mood of uncertainty in which many firms are reluctant to forecast their own earnings.[38]

Carnival's actual earnings for the first quarter of 2009 were 33 cents per share, up from 30 cents per share a year earlier. But revenue was down. Fuel prices, a major cost component, had come down but "failed to offset a drawback in consumer demand."[39] The company reduced its forecast earnings for the whole year 2009.[40]

> Since the start of the year, booking volumes for the remaining three quarters are 10 percent ahead of the prior year, but at "significantly lower prices," the company said. Cumulative advance bookings for the remainder of the year are still behind last year's levels.
>
> The company said it now forecasts full-year 2009 earnings per share to be in the range of $2.10 to $2.30, down from its previous forecast of $2.25 to $2.75. .... In an effort to preserve cash, both Carnival and Royal Caribbean stopped paying dividends last November.[41]

Additionally, both Moody's and Standard & Poor's have downgraded the credit ratings for cruise lines. Carnival's rating has fallen to BBB+, and Royal Caribbean's rating is now BB-. The ratings outlook for both companies is negative, which will increase future borrowing costs. Reuters further commented about Moody's downgrade saying, "Moody's cited falling travel demand as a reason for the downgrade, saying it would lead to lower net revenue and deteriorating debt protection measures."[42]

Holland America in 2009

Contrary to cruising's former image as a predictable experience for retirees, HAL managers see a market with broad demographics and up-to-date features. Meadows says, "We're always thinking about how to re-cast and re-design the product. Our product today is different than even five years ago."

Managing costs and revenues are also important. Yield management is an art, according to Larry Calkins, Senior Vice President Finance and IT at HAL. "We're trying to get better at it. We have made some major strides in the last five years, but we're going to get better," says Calkins.[43]

The company is particularly enthusiastic about their new initiative to implement a CRM (Customer Relationship Management) system. Calkins says, "At the end of the day, we will know everything about customers; we will capture on-board spending, previous trips, etc. We already fill the ships. So it's about filling them at higher yields."

The company also focuses on passenger demographics. Rick Meadows notes that,

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[37] Ibid.
[38] Miguel Bustillo, "Retailers Stop Making Sales Forecasts," Wall Street Journal, February 6, 2009.
[39] Deepa Seetharaman, "Carnival beats profit estimates", Reuters.com, March 24, 2009.
[40] Felicia Hendrix, "Carnival books higher 1Q profit but cuts outlook," http://pulse.alacra.com/analyst-comments, March 25, 2009.
[41] Deepa Seetharaman, loc cit.
[42] Deepa Seetharaman, "Carnival cuts Q2, 2009 earnings outlook," Reuters.com, April 3, 2009.
[43] Interview with Larry Calkins, October 6, 2008.

> Over the last six years, the average age of HAL's passengers has been holding at about 57. That's very exciting – it means we are successful in attracting younger guests. We already have the baby-boomers. If the pattern continues for another five years, we will be getting even more boomers and their kids.

Due to the extreme loyalty of their customers, Meadows feels that, "Once we get the boomers, we'll have them for years to come. We have a very deliberate strategy to attract younger guests, even generations X and Y."

In 2008, 90% of HAL's passengers were from North America. The company wanted to increase the sourcing of passengers from outside this region. Their competition was starting to source heavily in the UK and Europe, and non-North American markets were not saturated. In fact, some of these markets were just discovering cruising. HAL chose to focus on Europe. Calkins thought that HAL cruises would appeal to Europeans: "Our product works well in Europe. Our ships have a very European feel."

International passengers present a trade-off, however. They offer the potential for increasing yields, but they cost more, both in sourcing and in service. The sourcing cost lies in developing the market and the investment spending required for marketing and sales. The service costs come from adjusting things like decor, menus and service levels to different passenger preferences. HAL does not have the distribution channels in Europe that other lines have. It is important to develop relationships with travel agents in the countries where you want to source passenger. Calkins notes that, "Princess, Royal Caribbean International, and Costa Cruises all do a better job in Europe because they have the distribution channels."

However, the recession interrupted the passenger sourcing effort toward Europe, as the company's emphasis shifted to maintaining the current business.

As a result of the recession, the cruise industry in general has experienced shorter booking windows, lower on-board spending, and a need to entice customers with price cuts. Like other cruise lines, HAL has been aggressively discounting its cruises recently. Rick Meadows comments that "we're a fixed cost business...Over the last year, we have had to fill [our ships] using pricing."

> Cruise prices are down 50 percent for South America, down 18 percent to Europe and down 10 to 15 percent for the Caribbean, according to Mike Driscoll, editor of the industry journal Cruise Week...Some prices that are offered now extend to next year...even luxury lines are discounting...In addition to cutting ticket prices, the lines are offering shipboard credits, to be spent on spa treatments, specialty restaurants, drinks and sometimes in the casino...The credits are an alternative to cutting prices further.[44]

The aggressive price discounting has had positive effects for Carnival Corporation. According to a company press release from March 3, 2009,

> For the one-week period ended March 1, 2009, Carnival recorded the highest number of net weekly bookings in its history. Additionally, on a cumulative basis since mid-January, net bookings are up 10 percent compared to the same period in 2008, although pricing is at lower levels. Wave season typically runs from

[44] Robert N. Jenkins, "Setting Sale; The cruise lines are doing what they can to get passengers up the gangplank and into those empty cabins," St. Petersburg Times, March 15, 2009.

about mid-January through early spring and is traditionally the busiest, most important booking period in the cruise industry.

While many repeat customers book fares a long time in advance, many discount offers target potential 'last minute' bookers. A recent advertisement by Hotline proclaimed, "Save 50% on Holland America Alaska Cruises - Book Now."

On the other hand, HAL executives and managers firmly believe that their industry and their products make cruising a good vacation choice during a recession due to the good value. John Delaney, VP for Revenue Marketing at HAL, notes that, "Cruising can be a very good vacation value. Once you go on board, there are no more travel expenses. Food and accommodation are included, as are many travel activities."

Getting out the message of good value for a cruise, is a major focus for HAL and the industry as a whole. William Gibbons, director of the Passenger Shipping Association (the trade group for the UK cruise industry) said recently,

> The world of today is a very different one from that of 12 months ago. Although the cruise industry is not recession-proof it is better placed than many other travel sectors to weather the economic storm...Our research shows people are still looking to go on holiday, and the inclusive nature of a cruise means its future continues to look assured."[45]

Case Questions

Rick Meadows is optimistic about both the short and long term: "HAL is pretty good in a recession. And we are great in a recovery." However, he recognizes that the present environment presents challenges that require active responses. He has hired your consulting firm to develop near-term and longer-term strategies for dealing with the global recession and its aftermath. He has outlined the following brief for you:

1. Develop a set of macroeconomic assumptions and help us answer the following:
    a. When will the recession end?
    b. What will the recovery look like and how long will it last?
    c. Will there be a permanent change in consumer behavior as a result of the recession?

2. Given your assumptions in part 1, recommend a strategy for HAL to weather the recession and its immediate aftermath.
   As part of this strategy:
    a. Address the question of how to best articulate and communicate "value" while maintaining a premium brand image.
    b. Include a strategy for raising prices back to pre-recession levels.
    c. Suggest how to use social networking and other new media.

3. Develop a long-term strategy to increase the percentage of non-North American passengers.
    a. Do you think that Europe is still the best market to target?
    b. Identify the optimal timing for a push into markets outside North America.
    c. Recommend a marketing plan for the new target market(s).

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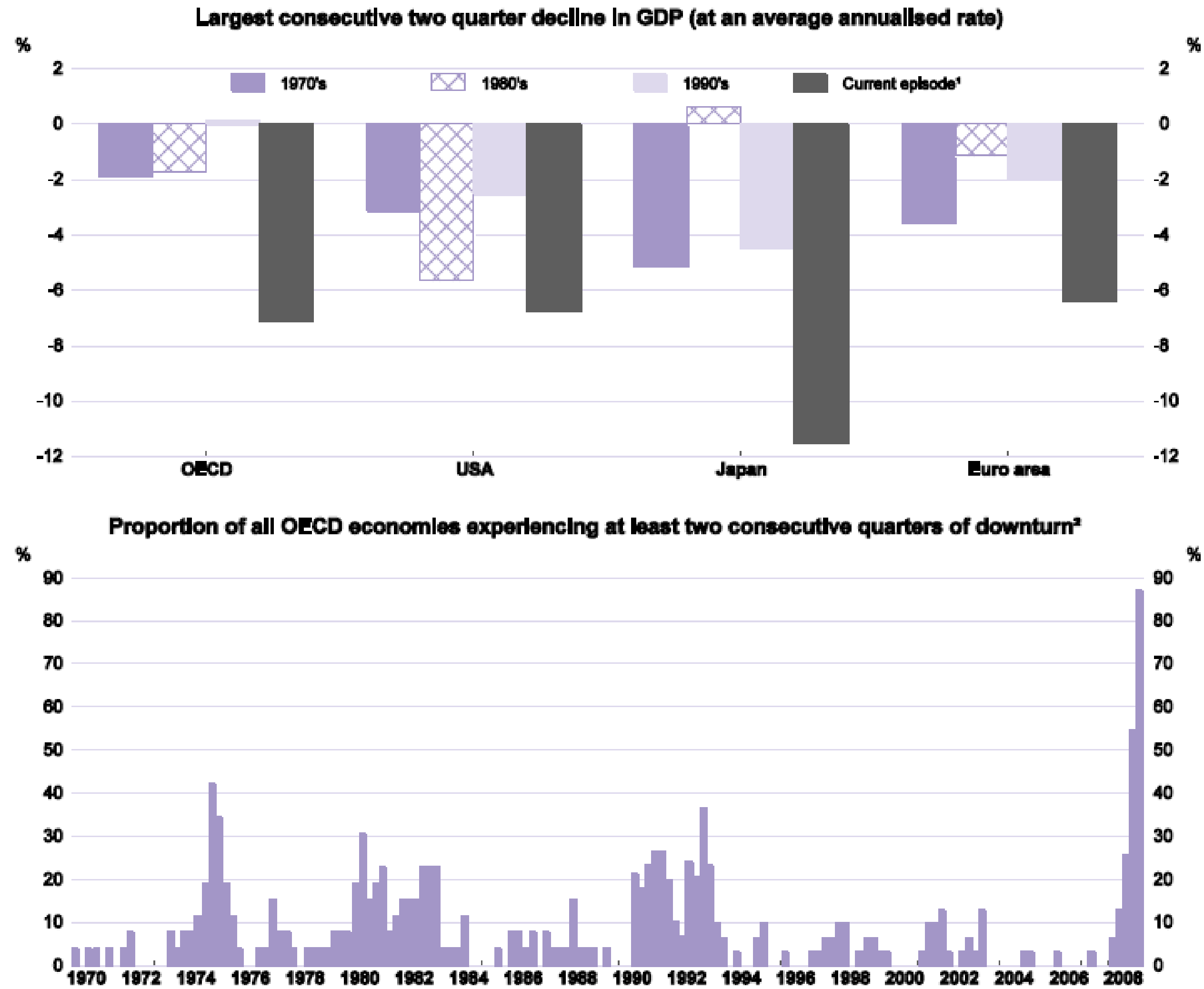
[45] Keith Hamilton, "Recession fails to halt cruise industry growth," Daily Echo, March 17, 2009.

Exhibit 1: GDP declines in OECD countries



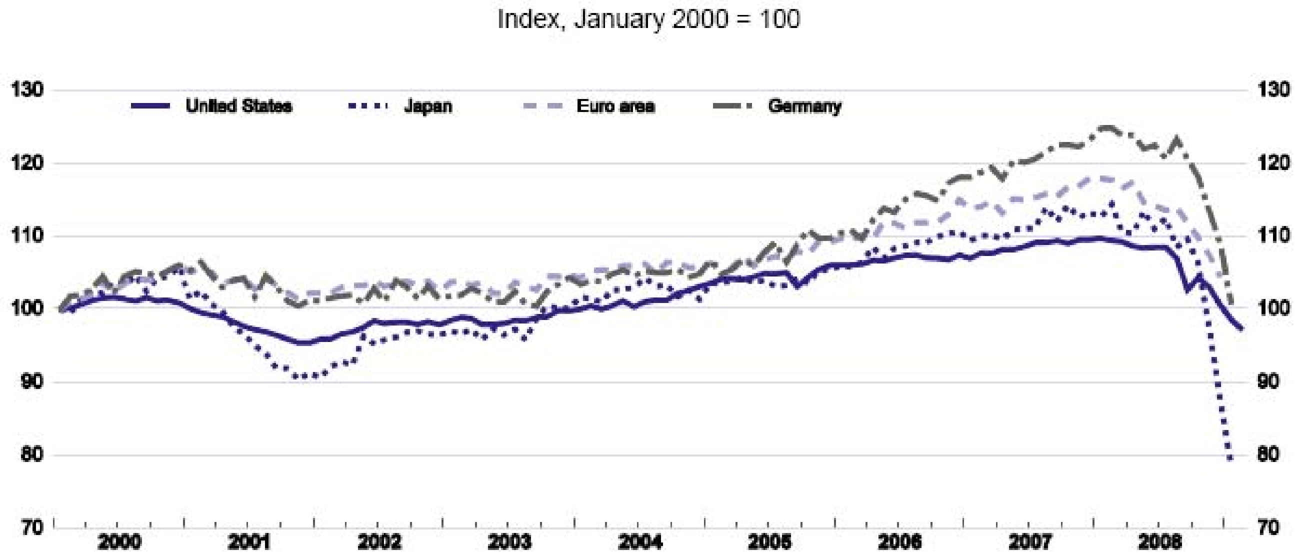
1. 2008q4-2009q1.

2. The last observation is for 2009q1 and relies on estimates of GDP growth.

Source: OECD.

Source: Figure 1.6 "The downturn is the most severe and synchronized in post-war history," OECD Economic Outlook Interim Report, March 30, 2009

Exhibit 2: Industrial production



Source: Figure 1.8 "Industrial production has plunged," OECD Economic Outlook Interim Report, March 30, 2009

Exhibit 3: Auto sales in US

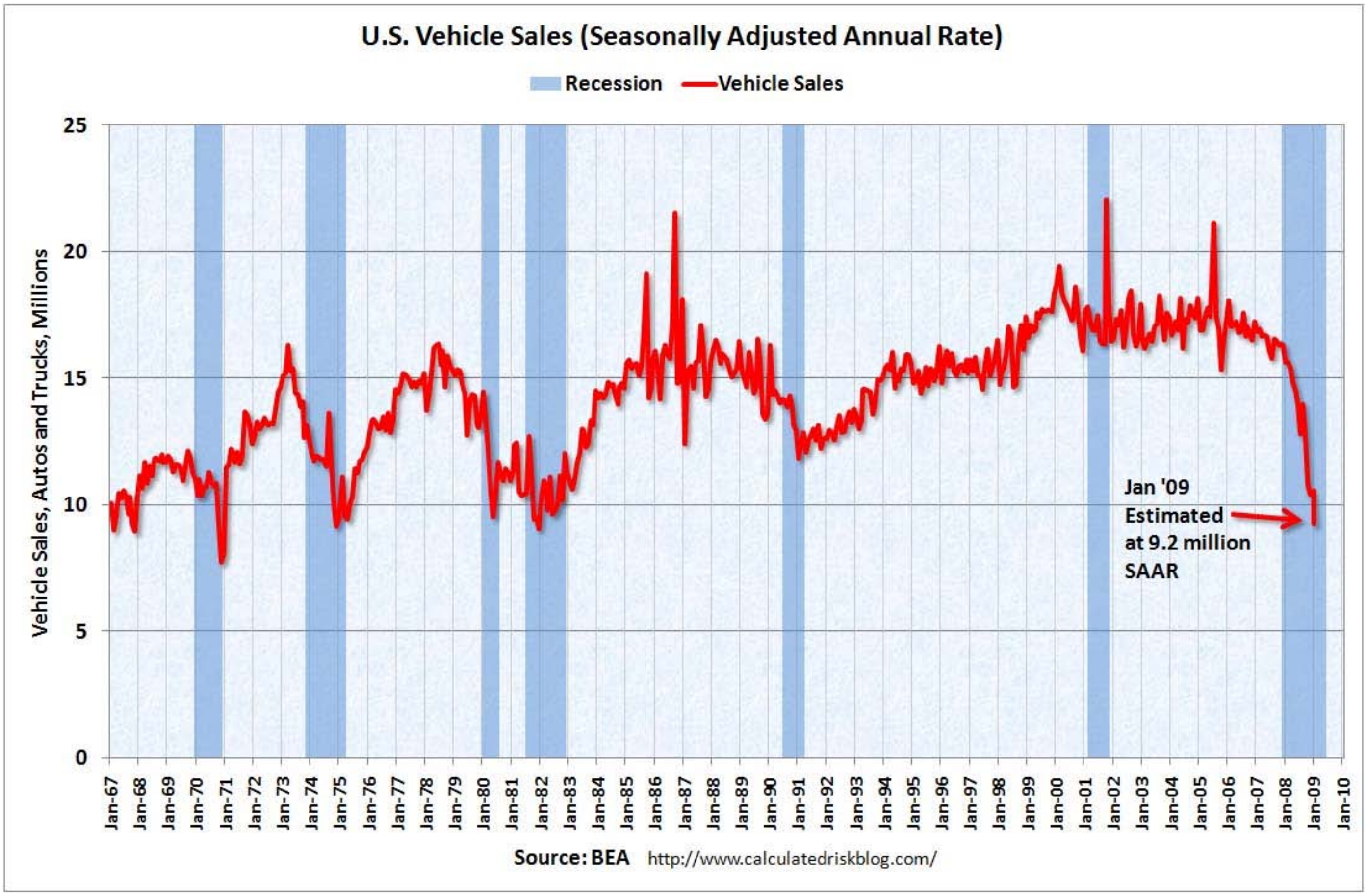


Exhibit 4: Retail sales in US

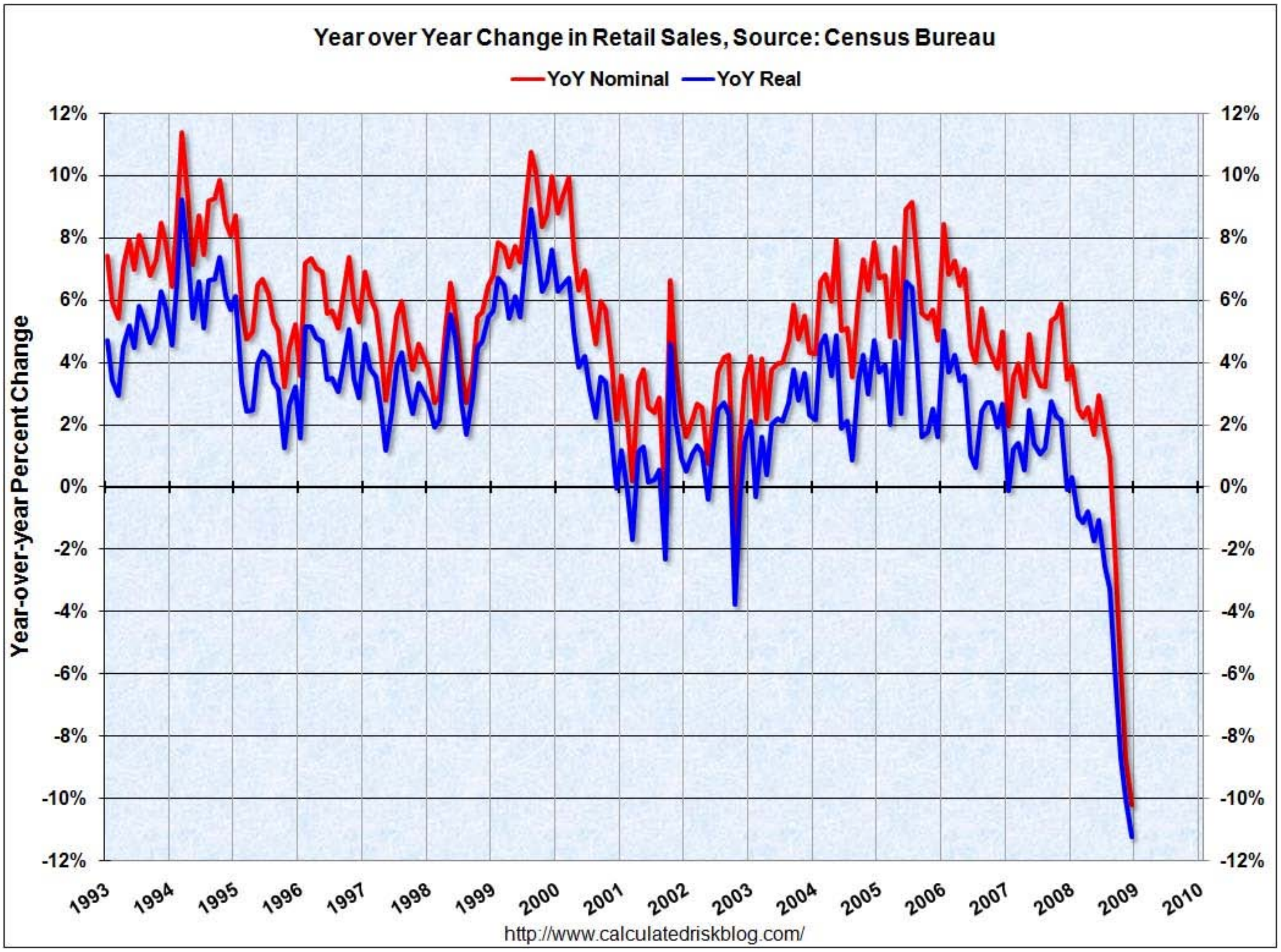


Exhibit 5: Unemployment rates in selected countries

Country	2007	2008	2009
US	4.4	5.1	8.5
Canada	6.1	5.9	7.7
UK	5.5	5.1	6.5 (est)
France	8.8	7.6	8.3
Germany	8.9	7.7	7.3
Switzerland	3.3	2.8	3.3
Japan	4	3.9	4.4

Notes: Data are from the month of January for France, Germany, Switzerland, and UK; from February for Canada and Japan; and from March for the United States
Sources: EIU Country Reports, OECD Main Economic Indicators

Exhibit 6: Changes in the real price of housing

	Per cent annual rate of change				*Level relative to long-term average* [1]		
	2000-2006	2007	2008 [2]	Latest quarter [3]	Price-to-rent ratio	Price-to-income ratio	Lastest available quarter
United States	5.4	-0.4	-6.2	-5.9	117	100	Q4 2008
Japan	-4.3	-1.1	-2.4	-3.8	68	66	Q3 2008
Germany	-2.9	-1.2	-2.7	-1.8	71	64	Q4 2008
France	9.5	4.9	-1.1	-2.7	156	136	Q3 2008
Italy	6.1	3.1	-1.1	-2.9	123	109	Q3 2008
United Kingdom	8.8	8.4	-4.3	-12.1	139	132	Q4 2008
Canada	6.7	8.5	-3.4	-11.5	165	117	Q4 2008
Australia	7.1	8.8	0.4	-6.7	160	128	Q4 2008
Denmark	7.9	2.9	-6.0	-9.1	154	143	Q3 2008
Finland	4.7	5.6	-2.4	-7.1	140	99	Q4 2008
Ireland	8.3	-1.8	-9.6	-13.3	155	128	Q3 2008
Netherlands	2.9	2.6	0.7	-0.3	154	154	Q4 2008
Norway	5.5	11.4	-5.2	-10.7	149	112	Q4 2008
New Zealand	9.2	8.3	-6.6	-11.2	146	143	Q3 2008
Spain	11.2	2.6	-3.7	-6.2	180	144	Q4 2008
Sweden	6.7	8.6	0.0	-4.4	154	119	Q4 2008
Switzerland	1.7	1.3	0.2	2.1	85	76	Q4 2008
Euro area [4,5]	4.5	2.0	-2.0	-3.0	124	109	
Total of above countries [5]	4.1	1.5	-4.0	-5.4	117	102	

Note: House prices deflated by the Consumer Price Index.
1. Long-term average = 100, latest quarter available.
2. Average of available quarters where full year is not yet complete.
3. Increase over a year earlier to the latest available quarter.
4. Germany, France, Italy, Spain. Finland, Ireland and the Netherlands.
5. Using 2000 GDP weights.

Source: Girouard *et al.* (2006), OECD.

Source: Table 1.2 "Real house prices are falling in virtually all countries," OECD Economic Outlook Interim Report, March 30, 2009

Exhibit 7: Stock returns in selected countries

Country	Index	Return Mar 07 – Mar 08	Return Mar 08 – Mar 09
US	S&P 500	-7.2%	-50.5%
Canada	TSX 300	1.4%	-42.6%
UK	FTSE	-11.5%	-38.9%
France	CAC 40	-18.0%	-54.8%
Germany	DAX	-8.3%	-50.6%
Switzerland	Dow Jones Switzerland	-21.2%	-38.9%
Japan	Nikkei 225	-32.2%	-43.5%

Notes: All returns are in local currency, calculated from end of month closing values.
Source: Global Financial Data

Exhibit 8: Income statement for Carnival Corporation & PLC

CARNIVAL CORPORATION & PLC
CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share data)

	Years Ended November 30,		
	2008	2007	2006
Revenues			
Cruise			
Passenger tickets	$ 11,210	$ 9,792	$ 8,903
Onboard and other	3,044	2,846	2,514
Other	392	395	422
	14,646	13,033	11,839
Costs and Expenses			
Operating			
Cruise			
Commissions, transportation and other	2,232	1,941	1,749
Onboard and other	501	495	453
Fuel	1,774	1,096	935
Payroll and related	1,470	1,336	1,158
Food	856	747	644
Other ship operating	1,913	1,717	1,538
Other	293	296	314
Total	9,039	7,628	6,791
Selling and administrative	1,629	1,579	1,447
Depreciation and amortization	1,249	1,101	988
	11,917	10,308	9,226
Operating Income	2,729	2,725	2,613
Nonoperating (Expense) Income			
Interest income	35	67	25
Interest expense, net of capitalized interest	(414)	(367)	(312)
Other income (expense), net	27	(1)	(8)
	(352)	(301)	(295)
Income Before Income Taxes	2,377	2,424	2,318
Income Tax Expense, Net	(47)	(16)	(39)
Net Income	$ 2,330	$ 2,408	$ 2,279
Earnings Per Share			
Basic	$ 2.96	$ 3.04	$ 2.85
Diluted	$ 2.90	$ 2.95	$ 2.77
Dividends Per Share	$ 1.60	$ 1.375	$ 1.025

The accompanying notes are an integral part of these consolidated financial statements.

Exhibit 9: Balance sheet for Carnival Corporation & PLC

CARNIVAL CORPORATION & PLC
CONSOLIDATED BALANCE SHEETS
(in millions, except par values)

	November 30, 2008	November 30, 2007
ASSETS		
Current Assets		
Cash and cash equivalents	$ 650	$ 943
Trade and other receivables, net	418	436
Inventories	315	331
Prepaid expenses and other	267	266
Total current assets	1,650	1,976
Property and Equipment, Net	26,457	26,639
Goodwill	3,266	3,610
Trademarks	1,294	1,393
Other Assets	733	563
	$ 33,400	$ 34,181
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Short-term borrowings	$ 256	$ 115
Current portion of long-term debt	1,081	1,028
Convertible debt subject to current put options	271	1,396
Accounts payable	512	561
Accrued liabilities and other	1,142	1,353
Customer deposits	2,519	2,807
Total current liabilities	5,781	7,260
Long-Term Debt	7,735	6,313
Other Long-Term Liabilities and Deferred Income	786	645
Commitments and Contingencies (Notes 6 and 7)		
Shareholders' Equity		
Common stock of Carnival Corporation; $.01 par value; 1,960 shares authorized: 643 shares at 2008 and 2007 issued	6	6
Ordinary shares of Carnival plc; $1.66 par value; 226 shares authorized; 213 shares at 2008 and 2007 issued	354	354
Additional paid-in capital	7,677	7,599
Retained earnings	13,980	12,921
Accumulated other comprehensive (loss) income	(623)	1,296
Treasury stock; 19 shares at 2008 and 2007 of Carnival Corporation and 52 shares at 2008 and 50 shares at 2007 of Carnival plc, at cost	(2,296)	(2,213)
Total shareholders' equity	19,098	19,963
	$ 33,400	$ 34,181

The accompanying notes are an integral part of these consolidated financial statements.

Exhibit 10: Travel Statistics from the Travel Industry Association

Measurement	Month	Value	% Change Previous Month	% Change Previous Year	% Change YTD
Air Traffic					
Domestic Air RPM (Millions)	Dec 2008	35700.0	8.4	-6.8	-5.1
International Air RPM (Millions)	Dec 2008	17624.7	9.8	-3.5	3.5
Passenger Enplanements (Domestic) (Thousands)	Dec 2008	35479.0	6.2	-6.6	-5.7
Load Factor (Domestic) (Percent)	Dec 2008	79.8	4.6	4.2	-0.4
Employment (Thousands)	Dec 2008	477.8	-0.9	-4.6	0.5
Rail Passenger Traffic					
Amtrak Ridership (Thousands)	Dec 2008	2284.6	-1.8	-1.2	8.1
Auto Travel					
Demand For Motor Gas (Thousand Barrels Per Day)	Dec 2008	9033.0	1.0	-2.4	-3.3
Gasoline Stations' Receipts (Millions $)	Dec 2008	26243.0	-15.9	-35.5	9.1
Hotel/Motel					
Room Demand (Millions)	Dec 2008	65.0	-9.7	-3.6	-1.6
Occupancy Rate (Percent)	Dec 2008	45.3	-12.7	-6.6	-4.2
Room Revenue (Millions $)	Dec 2008	6466.7	-11.8	-6.6	0.7
Employment (Thousands)	Dec 2008	1707.1	0.0	-5.3	-1.6
Restaurants					
Food Services & Drinking Places' Receipts (Millions $)	Dec 2008	37845.0	-2.2	-0.5	3.5
Employment (Thousands)	Dec 2008	9617.1	-0.6	-0.8	1.5
National Parks					
Overnight Stays (Thousands)	Dec 2008	304.6	-31.3	-0.3	-1.8
Recreation Visits (Thousands)	Dec 2008	12434.3	-24.7	-0.2	-0.2

Sources & Notes:
Air Traffic: Air Transport Association, Bureau of Labor Statistics, RPM= Revenue Passenger Miles, Employment excludes scenic and sightseeing air transportation and air courier services
Rail Passenger Traffic: Amtrak
Auto Travel: U.S. Bureau of Census, Department of Energy, Federal Highway Administration, Demand for Motor Gasoline is thousands of barrels per day
Hotel/Motel: Smith Travel Research, Bureau of Labor Statistics, Room Demand is unadjusted room nights sold
Restaurants: U.S. Bureau of Census, Bureau of Labor Statistics
National Parks: National Park Service

Source: Travel Industry Association (www.tia.com) Industry Performance Indicators, accessed 3/31/09