MONACO'S GREATEST GAMBLE

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Few destinations are more synonymous with risk-taking and excess than Monaco. But the tiny Mediterranean principality's latest development is audacious even by its own standards. Despite the downturn, the state is embarking on its first international expansion. It could be...

IT ONLY TAKES a few moments in Monaco to discover that the state has a space problem. At under two square kilometres, it is small enough to fit into Hyde Park and is crammed with condominiums, casinos and banks. Indeed, lack of space is so acute that in 1999 its railway station was relocated underground to permit the construction of 150,000 square metres of buildings above. It now literally has to think outside the box to grow.

In a bid to draw in more visitors, Monaco's leisure operator, Monte-Carlo SBM has begun to take over and brand hotels outside the confines of the principality. SBM has €800m to draw on after years of sparkling results but, as the downturn deepens, it faces the risk that it could be cashing in its chips too early.

Monaco's new direction is epitomised by the Monte Carlo Bay hotel. The soaring structure opened in 2005 and was the first new hotel SBM had opened in 75 years. It looks like it would be more at home in Las Vegas than on the Riviera. Belle époque balustrades have been replaced by a more minimalist Art Deco style dripping with glitzy touches. It has Europe's first sand-bottomed swimming lagoon and a fountain choreographed to classical music. Crucially, its casino is the only one inside an SBM hotel to have no table games. In a destination made famous by Bond and baccarat, the Bay has made a big splash and helped SBM shake off its greying image.

Founded 146 years ago, SBM has a monopoly concession to run Monaco's casinos until 2027. It owns five of them as well as 32 restaurants, an 18-hole golf course, opera house, tennis club and several of the Riviera's hippest

nightclubs. Its four hotels include the world-renowned Hôtel de Paris and the Hermitage but the Bay is the most innovative. With no construction space left in the state, SBM had to reclaim 10-acres of land to build the 334-room, €200m resort. The strategy was spearheaded by Bernard Lambert, SBM's skilled chief executive.

Classically-trained at Nice's hotel school, Lambert cut his teeth working for the luxury Meurice chain before spending nearly 30 years at Méridien rising to become CEO of the global hotel company. He took over the top job at SBM in 2002 and immediately got to work on the Bay project.

"We created something nobody was expecting – a true international resort, unique in Europe," says the smartly-suited Lambert. Waitresses encircle his table in the Bay's Blue Bay restaurant overlooking the sparkling Mediterranean. There isn't a cornice or chandelier in sight.

"We wanted to bring a new facet to our current range of products," he says adding that this positioning paid off. "The whole complex almost broke even after one year of operations. The hotel does over €30m." He explains that in its first year of operation it even brought €4m of business to SBM's other hotels as more guests were drawn to Monaco but the Bay lacked availability.

With an average rate of just over half the €500 charged by the Hôtel de Paris, the Bay has made Monaco more accessible and Lambert says that it has "a younger and more of a family crowd." However this was only part one of a plan to bring the state into the 21st century.

Destinations don't come much more opulent than Monaco. Shopping centres are adorned with chandeliers, and spotlessly-clean streets are lined with palm trees wrapped in fairy lights. Classical music is even piped to hidden speakers in the streets. But this alone isn't enough to out-do European resorts gifted with gaming de-regulation and others farther afield which have been opened up by low-cost travel. "Dubai is a competitor," says Lambert adding "on the French Riviera, Cannes has the promenade and we don't have that. Also, Barcelona, Prague, Budapest." He is taking the fight right to their doorsteps.

"We want to become a global luxury leisure brand," says Lambert and in December 2008 he announced Monaco's first ever international expansion. In late 2011, the first SBM-managed hotel outside Monaco will open – a 93 suite five star resort and spa in Marrakesh. It will be called 'Jawhar, (the jewel), by Monte-Carlo SBM' but there is much more to it than just branding.

"Marrakesh is close enough to us and is a destination for short breaks from all over Europe so it's a good window for us for promotion," explains Lambert adding that "we have already identified precisely the priority segments and markets." In addition to the

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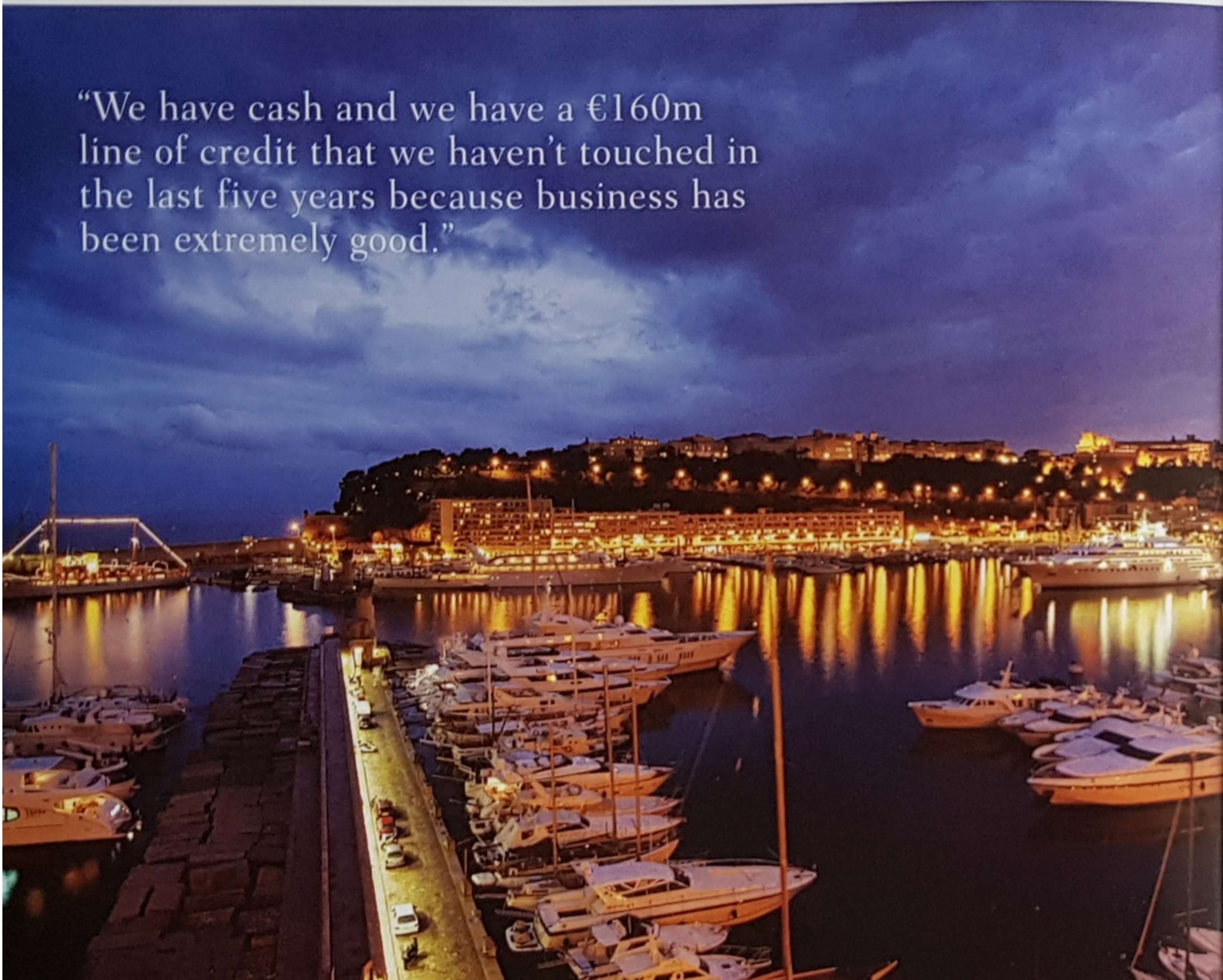

branding in the name and the obligatory in-room SBM directory. There will also be more innovative marketing such as having signature dishes from Monaco on its restaurant menu. He has a long shopping list for further expansion.

"We are looking in Paris, London, Milan, Geneva, Berlin, Budapest, New York and Los Angeles," says Lambert adding that although the majority of the deals he is planning are management contracts, SBM may acquire one hotel outright. "I wouldn't mind owning a hotel in London or in Paris," he says and reveals that his ideal target in the UK capital would have between 120 and 150 rooms and be in Mayfair. And although casino operation in European cities is not on the cards for SBM, due to the difficulty of acquiring licenses, it could be possible in resort destinations. Lambert's plans are far from half-hearted.

He hopes to have a collection of 15 hotels over the next ten years although he won't say when the next deal will be finalised – he simply says that there are, "more to come."

Global expansion for a luxury brand may seem daring at the moment given the weak health of the economy but Lambert is bullish. He is confident that international development and investment is a strategy for coping with the downturn. Lambert believes that SBM's risk is mitigated since it will own very few hotels. "To tell you the truth," he adds, " today the situation with the worldwide economy will offer opportunities we had never thought of ...deals are going to become cheaper than a year ago". And Lambert doesn't have to worry about securing funding.

TOP LEFT: MONACO'S SCENIC HARBOUR, HOME TO SOME OF THE WORLD'S MOST EXQUISITE YACHTS.

TOP: THE FAMOUS CASINO SQUARE IN MONACO.

BOTTOM LEFT: BERNARD LAMBERT, CEO OF MONTE CARLO'S SBM.

He expects to spend up to €800m on the expansion and explains, "we have cash and we have a €160m line of credit that we haven't touched in the last five years because business has been extremely good." The reward could be well worth the risk since the ultimate objective is to drive more guests to Monaco through what Lambert refers to as 'windows' around the world. With the downturn deepening it could be crucial for Monaco to cast a wider net.

Lambert forecasts that, once opened, the expansion will bring SBM an additional 10% of revenue over the following four years. It could come at just the right time.

After three years of record growth, the sparkle came off SBM's results in its annual results to the end of March 2009. The company's revenue fell 12.6% to €400m with its operating profit tumbling. It fell 69% to €19m – a big drop but it still finished the year with a profit which is a feat in itself. Surprisingly the main driving force behind this was not a fall in occupancy at SBM's hotels. Hotel revenue was down 6% to €174.9m but gambling earnings took a bigger hit. Following the introduction of a smoking ban in November last year casino takings crashed 19% to €210.7m and as the downturn has deepened, SBM has struggled further.

Its latest results are for the three months to the end of June 2009 and they show revenue of €104.6m which was down 15.8% on the same period the previous year. This was largely down to a 20.1% fall in hotel turnover as fewer guests stayed in the principality. Lambert says that this has been driven by a "significant drop of US and UK markets," and, "shorter visibility on group business (fewer incentives, travelling shorter distances for a shorter period, with less participants)."

He faces the Catch 22 situation that the glitz and glamour which has made Monaco famous is not something that many companies want to be associated with in a downturn, even if it is priced competitively. "They don't want to be seen as going to a luxury destination like Monaco in view of the financial situation," Lambert says and so SBM is looking beyond the banking and high-tech sectors which it has traditionally relied on. Nevertheless, Lambert adds that the pharmaceutical and automobile sectors are "still active" in Monaco when it comes to product launches.

SBM is also well diversified in terms of guests' geographical origin since, "no nationality accounts for more than 15%, which contributes to mitigate the risks," says Lambert. He adds that the type of guest visit is pretty evenly split with most SBM hotels running a business-leisure split of 40-60.

Despite the downturn, Monaco's status as an offshore finance centre has also helped keep its corporate guest numbers afloat compared to its competitors. Monaco secured fairytale status in 1863 when Europe's first casino opened there and its profits grew so great that Prince Charles III, great-great-great-grandfather of Monaco's ruling monarch Prince Albert, was able to abolish all taxation on Monaco's citizens.

The upshot is that although there are just 6,000 native Monegasque citizens, Monaco has 32,000 residents. They stretch from celebrities such as Sir Roger Moore and Shirley Bassey to business luminaries like Easyjet founder Sir Stelios Haji-Ioannou and Michael Smith, chairman of private equity firm CVC. As a result of the well-heeled corporate travellers visiting the principality, the helicopter service between Nice and Monaco is the most travelled helicopter route in the world with 68 daily turnarounds and 90% of this being business travel. Lambert adds that this year SBM strengthened its cross-promotion relationship with private jet fractional ownership scheme NetJets.

Lambert has also had an

unexpected windfall which should boost SBM's bottom line in the next quarter. We are in the midst of a deep downturn. Disposable income is dropping and business travellers are trading down to economise. So where would you find a resort refurbishing a grand hotel? Only in Monaco of course.

On 15th May 2009, one of Monaco's oldest and most historic properties, the Beach Hotel, re-opened after a multi-million dollar refurbishment. Built in 1928, the Beach Hotel is located on a secluded bay on the outskirts of the principality and is steeped in history.

Eva Peron stayed there in 1947 during her Rainbow Tour of Europe to promote Argentinian interests and the hotel's pastel-coloured lobby looked like it came straight out of an Agatha Christie thriller. This all changed as Paris-based designer India Madhavi brought a contemporary touch to the Beach Hotel making it a worthy neighbour to the Bay. Lambert confirms that sales and the key indicator of revenue per available room have been higher at the hotel this summer than last year. It sets a tough precedent.

"The big challenge is to keep the company afloat, as far as the obvious historic assets are concerned, while getting ready for better times in 2010 and 2011 when we will have new projects and new offerings," says Lambert.

SBM faces a different challenge when it comes to growing gaming revenues given the smoking ban. Lambert's strategy to cope with this includes outdoor gambling and casting out its net to pull in high rollers from all corners of the globe. SBM has sent agents into exclusive country clubs, golf clubs and cigar dens in Shanghai, Hong Kong, Guangzhou and Beijing to, "lure people that travel, that are educated and that want to see Europe". It has an impressive hook to pull in punters; complimentary all-inclusive travel and accommodation packages for gamblers waging over €20,000.

"We are targeting what I call the haute-couture type of clients. They're not in the mass market and groups. So that's haute-couture in terms of gambling," says Lambert. And SBM has not put all its money on one spin of the roulette wheel as agents have also been sent to Delhi, Bombay and Bangalore. To give it further presence, SBM has also opened a regional office in Singapore and is planning another in Beirut. It is also taking its brand beyond physical borders with Monaco's first online gaming site.

Monaco abides by French law to regulate online gaming and since this prohibits many table games, the Monaco site focuses on sports betting. In February 2009, SBM acquired a 50% stake in Mangas Capital which controls the BetClic online business and Lambert's aim for the partnership is simple, "to become one of the main players on a pan-European basis."

Last year SBM also diversified into poker and is throwing its weight behind it by even hiring professional poker player Isabelle Mercier to promote the game.

But for all of Monaco's image of excess and spending its way through the recession, it knows its limits. The principality had planned further land reclamation on a giant scale which would solve its space problem for once and for all. The project was set to add 275,000 square metres of land and was projected to cost around €10bn but the downturn put paid to this.

"In the current climate, it would be irresponsible to launch a project of this scale," said Prince Albert in December 2008, when the plan was shelved. This sounded a note of caution but perhaps the best indication of Monaco's outlook is the demand for SBM's stock.

The Monegasque State holds 69.5% of SBM's share capital with the majority of the remainder traded on Paris' Euronext exchange at a market capitalisation of €585.2m. In July last year, the Qatari Diar real estate investment company, a unit of one of the most aggressive sovereign wealth funds, launched a bid for 30.4% of SBM's stock. The offer represented a 31% premium on the share price before it was announced and valued the business at €1.3bn.

However, SBM took out an ad in the French press to say that the price offered was "insufficient" and didn't reflect, "in any way the company's real value." It added that it would only support Qatari Diar's offer if it was limited to 10% of SBM's capital. Qatari Diar walked from the deal. It evoked a similar battle in the 1960s when Greek shipping magnate Aristotle Onassis secured a majority stake in SBM only to be forced into minority ownership by Monaco's late Prince Rainier who issued 600,000 new shares and passed a law to make them non-transferable. Times change but the allure of Monaco does not.

TOP: THE MONACO SKYLINE; AS SPACE IS GETTING MORE AND MORE SCARCE, THE PRINCIPALITY'S BUILDINGS RISE HIGHER AND HIGHER.