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Travel Industry
Q1 2020 Earnings
Notables

Extended stay hotels, Occupancy, RevPAR, RevPAR Index, Rate:

- Every Extended Stay America (**ESA**) hotel has remained open through the pandemic, with healthy occupancy levels and no widespread staff reductions or furloughs. Lean property staffing levels, coupled with demand drivers that are steadier in times of distress and that also grow during periods of expansion, are unique in the industry. There's no one else in the industry that's solely focused on extended stay. There's nobody else in the business that has a distribution engine that is solely focused on delivering extended stay customers. There have only been a couple of weeks when ESA brand-wide occupancy dipped below 60%. Some hotels in good extended stay markets are operating at nearly 100% occupancy. Quite a number of ESA properties are in the 80% and 90% occupancy range, with more hotels with greater than 80% occupancy than hotels with occupancy below 50%, and more hotels with occupancy above 90% than below 40%. Even soft ESA hotels are not as soft as others. The Midwest has been better than the Southeast, New York or California. [Bruce Haase]
- **Choice Hotels** also outperformed their competition in the first quarter on several fronts, with system-wide occupancy rates that were higher than the overall industry, especially for Choice's extended stay brands [Patrick Pacious, CEO]. Choice's 410 extended stay hotels maintained an April occupancy level of 60%, 64% for its WoodSpring brand and above 30% across the Choice portfolio. 60% of the Choice portfolio is performing above 25% occupancy.
- **Park Hotels** has 22 of 60 properties open, operating at significantly reduced capacity with consolidated towers and closed floors, and about 15% of 33,000 total rooms available to guests. The majority of Park's hotels that remained open are either airport or suburban properties that are housing airline crews or special circumstance groups and a small number of urban hotels operating with extremely limited capacity to house medical related demand.
- **Hilton**: "We currently have suspended operations at approximately 950 or 16% of our hotels globally, including approximately 10% of our hotels in the Americas, 60% of our hotels in Europe, the Middle East in Africa, and 15% of our hotels in Asia Pacific. Our sales teams are engaged with customers on business for the back half of the year and into 2021 and beyond. In the last week alone, we booked tens of billions of dollars in Group business in the Americas. In addition, we are starting to see double-digit increases in digital traffic and booking activity across all segments. Global occupancy levels have gone from a low point of 13% to 23% currently." [Chris Nassetta]

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- About 25% of **Marriott** hotels worldwide are temporarily closed, with 16% of North American properties closed. Europe is mostly shut down, with just over three-quarters of Marriott hotels in Europe closed.
- 90% of **IHG's** hotels in the United States are open. In China, 180 hotels were closed, but only 10 are still closed now.
- **ESA** brand-wide RevPAR only declined 35% in March and April, compared to industry-wide declines of approximately 80%, mid-scale declines of 65%, and economy declines of 45%.
- **Choice Hotels'** system-wide RevPAR declined 60% year-over-year but has had consistent daily occupancy improvements in the last two weeks and the growth rate outperformed the overall industry by 430 basis points. Choice's upscale brands experienced RevPAR growth rates 270 basis points better than their competitive set in the first quarter of 2020.
- **ESA's** RevPAR Index in March increased 32% to 122, in April (preliminary) to 155, and in the Quarter overall by 12% to 107.
- **Choice Hotels'** brands have consistently achieved RevPAR share gains versus the competition.
- The biggest declines in **ESA** revenue in the first quarter came from a drop in OTA guests, who were 40-45% of business, but which evaporated quickly and fell 16%, nearly all of this in March. ESA also saw declines in revenue from property direct and from the global distribution system. Partially offsetting those declines were increased revenue from ESA's website and call center. Revenue from guests staying a week or longer increased approximately 3%.
- **Choice Hotels'** franchisees have not tried to chase demand that wasn't out there by lowering rate. [Patrick Pacious]
- **Marriott**: "We want to make sure that we're not dropping rate to chase demand, which is not there and that obviously does nothing for us. At the same time, we compete in an industry which is highly distributed in terms of its pricing. And this is one of the challenges that we bear perpetually. People view us as, okay, you're the largest hotel company in the world, doesn't that give you pricing power. Well, the fact of the matter is, even as the largest hotel company in the world, we've only got [7% percent globally. 16% North America] of all rooms in the world and many of those rooms are priced by our franchisees, not priced by Marriott. And so we're not going to push rates down by any means. We're going to do everything we can to make sure we're maintaining pricing power, but there will be price competition in our industry too as we try and get demand energized and coming back into the system. And we'll do the best we can, making the kinds of judgments that need to be made." [Arne Sorenson and Kathleen Oberg]
- **Hilton**: Honors occupancy at modest business levels has skyrocketed. "When everything is bad, people peel off and go different directions and you have a real opportunity to differentiate yourself." [Chris Nassetta]

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- **Park Hotels** referenced the growth and stickiness of loyalty programs and "when you think about the strength of the brands, and the access that they add to those customers to induce demand, to have direct conversation and to be able to stimulate, you hope that and their desire same as our desire to make sure that we are getting the appropriate and the highest possible rate that we can…. I think given the devastation and given the fact that people are working together and understand the revenue is so critical here, that hopefully we'll have more rate integrity." [Tom Baltimore]
- **ESA** has two long-term rates. One is a retail 30-night rate. ESA has seen strong growth in that rate plan over the last few months compared to last year. ESA has a discounted prepaid rate, for stays of 60 nights, but pay upfront for 30, and has seen exponential growth in that rate plan.
- **Choice Hotels'** brands are at the right price point and location for the type of traveler who has been on the road these past 8 weeks and who Choice expects will lead the return to travel: the resourceful American, Choice's core customer. Choice expects these guests will replace lavish trips with lower cost getaways, presenting an opportunity for Choice's portfolio when folks get back on the road. Choice expects Americans will choose to drive when their ability and appetite for travel return. Choice believes that heightened concern about the safety of air travel, low gas prices and Choice's strong presence in drive-to locations will, taken together, allow Choice to capture an outsized share of pent-up travel demand as stay-at-home orders are lifted [Patrick Pacious].
- Due to the recently passed CARES Act, which creates significantly more depreciation deductions, **ESA's** total taxes for the full year could range from a large refund potentially as high as tens of millions of dollars to a very modest amount of taxes owed.
- Nearly 70% of **Choice's** hotels have applied for or secured SBA loans through the Paycheck Protection Program and Economic Injury Disaster Loans.
- **Hilton**: "Reality is, for our industry, [PPP] hasn't been as -- just because of the complexity of ownership structures and alike, it has not been that helpful. The second wave hopefully is more helpful. But the fed getting ready to launch a Main Street Lending Program, which we're working very hard on to make sure that there is more access. And so, a bunch of our owners by the way, lots and lots, dozens and dozens have had access to PPP. We're hoping that a much larger set of them get access to Main Street Lending Program." [Chris Nassetta]
- **ESA**: Success in the extended stay business is often a very local effort, and ESA has put boots on the ground again. ESA's product and core customer base is also well suited to the current environment. ESA's hotels are generally located in suburban and highway locations, which are convenient for customers that drive rather than fly. ESA has virtually no exposure to traditional group business segment that is essentially evaporated and may take a very long time to recover.
- **Choice Hotels'** business model can play in both the uprising demand cycle and the lowering demand cycle, because of Choice's construction portfolio and conversion

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portfolio. “I would think of it as about two lungs, one on the left, one on the right, and they both keep the entire entity moving during different periods.” [Patrick Pacious]

- **Park Hotels** mentioned that in some markets like New York “It would not surprise us at Park if you had many hotels that never reopen…. there are probably many owner operators who have levered up at 65%, 70% or more who probably don't reopen.” [Tom Baltimore]
- Every **ESA** suite has a full kitchen, which is, of course, essential in an environment where you can't dine out [Bruce Haase]. And ESA has increased free Wi-Fi speeds to allow guests to more effectively work remotely or complete school projects from the comfort of their room.
- **ESA’s** customer mix has shifted in favor of long-term guests with less housekeeping requirements. Nearly 80% of ESA’s recent revenue is now coming from various extended stay customer segments compared to approximately 63% pre COVID-19. Increased extended stay segments include construction, warehousing, distribution, hospital, and medical.
- **Choice Hotels**’ guests are one-third business travelers, passenger airline crews, cargo airline crews, truckers, railroad business, logistics people, trainers, IT support professionals, traveling nurses, and education services, which have had fewer job losses than other sectors. “Our core customers on the business travel side are the people that keep the country moving.” [Patrick Pacious]
- **ESA** has temporarily removed grab-and-go breakfast and implemented every-other-week housekeeping rather than a weekly service for our long-term guests. These brand-wide actions both reduce costs and provide for a safer environment on property for staff and guests.
- **Choice Hotels’** franchisees, who are typically owner / operators with 2 hotels financed with low overall debt levels, are less labor intensive and, in general, operate at higher margins as compared to full-service hotels, allowing owners to flex payroll costs, reduce operating expenses and postpone capital expenditures.
- **ESA** is seeing unexpected wage pressure from unemployment compensation subsidization.

Breakeven Occupancy:

- For **Choice Hotels** on a systemwide basis, breakeven is probably around 30% occupancy, inclusive of debt service.
- For **IHG**: “Hotels break even at around 30 percent occupancy, and we’re running around the mid-20s right now. With government support, and the cost reductions we’re putting through, their health is good. Under pressure, but in a reasonably good place.” [Keith Barr]

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- For **Marriott**: "The breakeven occupancy question is an interesting one. In a way, you could look at our portfolio in the United States and say why are only 16% of the hotels closed, because at those sorts of numbers, there are many more hotels that are losing dollars than that are closed. And that's true. But the question is not so much do they make money by staying open, but the question at the moment is do they lose less by staying open. And our general calculation is that by the time you get to 10% occupancy or so, you're probably better off from a purely financial perspective to stay open, that the losses will be lower than the losses associated with being closed. And remember, when you're closed, you've still got labor costs for some labor that is required. You've still got heating and cooling. You've got security. You've got other costs that cannot be avoided. And so there's not a closing scenario that gets you instantly to a breakeven level. You're still losing money on that. But broadly, you're going to probably break even at 30% or so occupancy in the select brands and maybe 40% occupancy in the full service brands." [Arne Sorenson]
- For **Hyatt**: "I'll give you some color on how we think about breakeven. And I would start by saying, it depends a lot on the location and type of hotel that you're talking about. If you think about a full service hotel in the U.S., occupancy levels at breakeven are about 40% to 45%, and a select-service hotel would be about 10 points lower than that, 30% to 35%. And then, you can think about hotels with lower labor costs, maybe some hotels in some international markets being in that 30% to 35% range as well, and then hotels in higher labor markets would be above that 40% to 45%, potentially." [Joan Bottarini]
- **Hyatt**: "I think, the occupancies that Joan just referenced are at the operating income line. If you looked at gross operating profit, GOP level, if you're familiar with the hotel P&Ls, it would probably be about 10 points lower than each of those numbers that Joan just cited. So, she was talking about breaking even at the operating income line as opposed to the GOP line. In terms of the question you asked about what level of occupancy we might be looking to as we think about targeting reopening our hotels, we think that something like 15% occupancies are about a crossover point between how much you lose by staying closed versus how much you might lose by reopening." [Mark Hoplamazian]

Owners, Brands and Managers:

- For **Park Hotels**: "I have long been a vocal proponent of the need for a rebalancing between brands and owners. If there is a silver lining in this current crisis, I would speculate, this will be one of them. The brands have not been immune to the value destruction of this pandemic. I think it's not going to surprise you that the business has been out of balance. Their business models don't work, but they don't have a healthy owner community and I also think that they also got a bit of a wake-up call when your

business model doesn't work, when your owners have no revenue, therefore, no fees." [Tom Baltimore]
- **Hilton**: "[T]here have been owners that have asked for fee relief. But not -- hand over fist and the reality is, I think there's a real simple reason, our fee structure as you know which is different for different players in the industry, all of our fee structures, whether it's the franchise fee or management fee or the system charges, they're all based on a percentage of revenue. So, we have given the ultimate fee relief, meaning when you're 90% off, there really aren't many fees because there's not much revenue. And so I think most of the owners -- everybody would like every bit of help that they can get. I think most of the owners that I have talked to sort of understand that the fees have been right sized with the demand in the business that they're not at the moment sadly for us and sadly for them, they're not paying us a lot of fees in any event, so that we will continue to look at all options with our community." [Chris Nassetta]
- **Park Hotels**: "On the operator side, we now have 8 operators. Getting that best intel, those best practices, seeing the things that are happening not only across the brand operators, but those independent third-party operators, is always something that, that I believed in and the team here at Park is believed in, that competition is a good thing." [Tom Baltimore]

Conversions:

- **ESA** has had a number of conversion opportunities from competitor brands. Liquidated damages based upon trailing royalty fees are going down, which could make conversion more enticing for owners.
- **Choice** awarded nearly 60 new agreements in the first quarter, nearly 3/4 of which were for conversion hotels. Further, approximately half of the contracts in the first quarter were awarded in the last 2 weeks of March. Choice expects conversions will probably be a much larger contributor to Choice's unit growth over the next couple of years.
- **Marriott**: "Obviously, conversion activity is up right now…. it's fair to say that while conversions step up in a weaker environment, new builds step down and they probably step down at least as much as the conversions step up." [Arne Sorenson]
- **Marriott**: "[O]ne of the differences between now and the Great Recession is our strong portfolio of soft brands, and frankly, the interest that we're seeing in those brands around the world. So the conversion vehicles that we have now as compared to 12 years ago, I do think are meaningfully stronger, which I think is helpful….[N]ormally maybe 15% to 20% of your room openings are conversion and let's say that number goes up to a third…[overwhelmingly in North America from the soft brands]" [Kathleen Oberg]

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M&A and Property Sales:

- For **Choice Hotels**, "There's white space in our portfolio for an upscale extended stay brand. So there may be an opportunity to do something in that space. If something were available, we would look at it." [Patrick Pacious]
- For **Park Hotels**, "I would say that to be brutally honest, I'd say that the COVID-19 discount gap is too wide right now. I think you see sellers would probably like to sell with a 10%, perhaps even 15% discount depending on their individual needs. But I think buyers are looking for somewhere north of 30%, even 40%. So I think there's plenty of liquidity trying to get in the sector, recognizing that now is a good window to begin to build up a portfolio. But I think the gap is too wide to really expedite any sort of transaction, as you've seen the number of deals that have blown up here in the last few weeks."
- For **Park Hotels**, in regard to opportunity for consolidation among REITs: "I've certainly been among the most vocal advocates for that for north of a decade… I -- it would not surprise me, but you will not see Park in that dialogue right here in the near term." [Tom Baltimore]
- **Hyatt**: "We just have to maintain some, I think balance, as we think about deployment of capital at this point and making sure there will be a better visibility to the future before we start making commitments that would consume a lot of capital in one way or another." [Mark Hoplamazian]

Foreclosures / Financing:

- The foreclosure risk in the **Choice Hotels** portfolio is very low. That is an immaterial risk to the Choice portfolio. [Patrick Pacious]
- **Hilton**: "[T]he lion's share of the hotels that get built in our system are not actually financed all that aggressively. You're talking about like 50% loan to cost. You have to remember the amount of liquidity that is in the system. Pre-COVID you're talking about like tripling plus of the money supply from quantitative easing and then even more capital being injected into systems globally. There's going to be plenty of capital looking for productive yields. And I would say, for some period of time it will be a distressed environment" [Kevin Jacobs]

The Economy:

- **Park Hotels**: "I think Hawaii is a great example of what's happening in our great country right now. You've had about 630 cases approximately of COVID-19 across the islands. You've only had 17 deaths. Any loss of life is horrible and very sad. But in the context, 17 is a very small number based on what we're seeing in other jurisdictions. You've got unemployment that's rising at 40% to 50%. And you have a state deficit that's at $1.5

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billion and rising. And so at some point, we need to find a better balance." [Tom Baltimore]

- **Marriott**: "I think what we're seeing across the United States is folks are tiptoeing out of their homes a bit more the last few weeks." [Arne Sorenson]
- **Hilton**: "Everybody knows I'm a born optimist, and that will never change. So, I feel spectacularly good about the long-term for the industry. I feel spectacularly good about our model and the long-term opportunities for Hilton. I think as we get through this and we realize that COVID-19 and these types of viruses are a part of our future, they have been, we have dealt with the seasonal flu. There was a time where dealing with the seasonal flu felt like this. That we will figure out as a global community how to deal with this. I think as people then start to feel like this is a safe environment, they are going to go back largely to their old behaviors, I would bet a lot of money on it. And that's what history would tell you." [Chris Nassetta] "In general, we think the crisis will probably create more opportunities than it hurts." [Kevin Jacobs]
- **Hilton**: "[T]he data is pretty clear that while this is a terrible virus and it's affecting people's lives and it's killing people, which is horrific and every life is important, when you get down to it, it has infected a lot more people that we know and the mortality rate is much, much lower than people have thought and the real data suggests there's a very small part of the population that is really at risk. I think the more of the testing data that comes out even without a vaccine or a therapeutic, the more people are going -- particularly those that are not at risk, the more comfort that they are going to have. [I]n my opinion, this summer, you will see a heck of a lot more people getting on planes and in airports than you see right now." [Chris Nassetta]

China:

- **Marriott**, "The resiliency of demand is evident in the improving trends in Greater China. New bookings continue to pick up with demand driven primarily by domestic travelers. We've talked about China a little bit, and China does appear to be recovering and holding. I know there's lots of debate about whether or not there is a resurgence of the virus in China. We've got tens of thousands of associates working in our hotels and basically have a way of tapping into that community and listening to both their sentiment and to some extent the data. And by and large what we hear there is reassuring that in fact demand is coming back and the virus spread does not appear to be profound. That doesn't tell us for certain where it's going in the next few months, but there is something that's encouraging there. Advantages of China and the United States are they're both domestic markets. In Greater China, our joint venture with Alibaba has been very helpful in rebuilding demand. A recent spring sale run by Alibaba's **Fliggy** travel site was very successful and generated terrific near-term bookings. Bookings from **Ctrip** have also

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grown significantly over the past few weeks and are up over 15% for the first week of May versus the same time last year." [Arne Sorenson]

- **Hyatt**: "The thing that was striking to us is that in China, while occupancy has been building over the course of the month, the last week was quite significantly positive. We even had a few hotels that sold out over the last weekend, due to a holiday weekend. But the very fact that you could even have a hotel that could sell out is kind of a notable thing at this point, to begin with. Yes, the hotels that were in the highest demand are hotels that have a very significant drive to marketplace. And we did see some enhanced demand into Sanya, which is on Hainan Island, which is a fly-to market. But, I would say that really the concentrations of activity have been amongst leisure travelers, and this was a holiday weekend of course. And again, the highest concentration was in some of the drive-to markets. So, that validates what we expect to see elsewhere, which is leisure will lead, drive-to markets will lead." [Mark Hoplamazian]
- **IHG**: "[T]he key thing to remember is the Chinese government's ability to stimulate economic growth and activity is unlike any other country… the ability for the Chinese government to stimulate demand in the second half could cause a significant uptick in performance in the second half of the year." [Keith Barr]
- **Hilton**: "We are starting to see glimmers of travel resuming and economies reopening. In China, nearly all 150 hotels that have been closed due to the pandemic have since reopened with occupancies reaching more than 50% during the May Day holiday this past weekend, up significantly from 9% in early February. Additionally, the majority of our previously halted construction projects in China have restarted." [Chris Nassetta]

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