Marriott International, Inc.
Morgan Stanley
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Stephen Grambling, Morgan Stanley: I'm very excited to introduce our next speaker, Leeny Oberg, who is Chief Financial Officer and EVP of Development for Marriott, the world's largest hotel brand. Leeny, thank you for joining us.

Kathleen Oberg, Marriott International: Thank you. It's great to be here.

Stephen Grambling: So over the past year, you've hosted an Analyst Day, launched some new brands with Four Points Express, City Express, StudioRes, and consistently raised guidance, actually. So we'd love to just hear to kick things off and the key messages from your Analyst Day. And then I guess as we think about the longer-term opportunity for Marriott, help frame that out.

Kathleen Oberg: Sure. So thank you. Good morning. Great to be here with you all.

I think you've heard all of us talk about the robust environment for travel, and I think we really see this not as a single year but as a multi-year, decade kind of trend right now where we're very excited about what we see over the next number of years.

We'll obviously always be impacted by macroeconomic environments of the locales where our hotels are situated. But when you really look more broadly about consumers' desire for experiences and a bit of a shift away from goods towards experiences, and the fundamental increase in leisure trips even before COVID, I think we're very excited about the outlook for our industry, frankly, for years to come.

And then I will put on top of that the strength of the brands and Bonvoy, and I think that that is where with the kind of platform that we have that really presents to a consumer a really unique value proposition that helps everything from the planning and the execution of your travel, as well as controlling your experience. But then also more broadly, the actual value of being a member in the program.

And so when we talked last September, we talked really in the classic equation of RevPAR plus rooms growth plus some operating synergies delivering extraordinary EBITDA and solid growth. As you know, rooms growth of 5% to 5.5%, and we continue to feel comfortable with that two-year CAGR that we talked about for 2024 and 2025 and then also adding to it from the RevPAR growth perspective that we gave.

So, as you described, we actually moved our EBITDA target for the year. In May, we moved it up to, in very rough terms, around $5 billion. And I think that really demonstrates the execution of our growth strategy in addition to a really healthy demand environment for travel.

And then last, but not least is the supply environment, which, while of course, I would love to see lots more new construction of hotels, the reality is we really do see that with lower supply, growth particularly in the U.S., that impact and it's been several years, frankly, I think will also provide a good balance for the company's performance as we continue to do more and more conversions, which

[1] Not a verbatim transcript; extraneous material omitted and edited for clarity and misstatements.

doesn't impact the supply picture, but also then evens out when you're looking at demand and supply balance.

Stephen Grambling: So I think it was last year actually. I didn't ask the question directly. So I'm just curious if you can give us an update, when you're saying health environment, that was mainly -- it sounds like a longer-term trend, but what are you seeing currently as you think about different segments, looking at leisure, the business traveler and also group?

Kathleen Oberg: Sure. So we continue to see a robust environment for travel in our business. For the month of April, as an example, we had RevPAR growth globally, systemwide of 6.5%. And actually, in the U.S. & Canada, that was 5.6% in the month of April, impacted, as I'm sure many of you know, by the year-over-year easier comparison of no Easter in the month of April this year as compared to Easter being last year in the month of April. We of course as you know saw the pain of that in the month of March and saw obviously that several hundred-basis-point improvement to the month of April.

And then you saw from an international RevPAR standpoint, you saw 9% for the month of April, which really is an amalgamation of the particularly strong demand, mid-teens, actually RevPAR growth in EMEA and in Asia Pacific outside of Greater China, with CALA being pretty close to double digits, so very strong.

The one weak area was Greater China and that was a mix of several things. You're clearly seeing a slower economy there. But there also were several other kind of impacts that just kind of smacked the month of April, particularly tough weather for several weeks in a big chunk of the country, which wasn't helpful.

And then you've got this continuation of the trend where you aren't still seeing many inbound cross-border guests into China. And you're actually seeing the higher-income Chinese travelers going outbound, which they've really started to do in numbers this year as compared to last. So you put that all together and we actually had negative RevPAR growth in the month of April for Greater China. But you put that all together with the incredible strength of the other markets and you end up with 9% international for a global number of 6.5%, so really continuation of strong demand.

Stephen Grambling: So it sounds like China is the only area where it's a little bit shaky. Are you seeing any forward signs of demand improving in that market? It sounds like air capacity --?

Kathleen Oberg: I do think April was smacked, particularly, by some of the elements that I mentioned. And business travel is clearly impacted by the slower economy. But I do think that you should not expect to see the same level. I don't have a prediction for the rest of the quarter yet. But certainly, I don't think we'll be as bad as it was in April.

The booking trends, as you know, are extremely short for transient. And I will say, in China, since the recovery of COVID, they've been shorter still. I mean, you'll hear a lot of hotels in Greater China talking about their transient booking window being under a week. So it's definitely tough to tell in terms of a view for the rest of the quarter.

But again, better. But I would say continuing to reflect relative to our other international regions a weaker environment.

Stephen Grambling: Fair enough. Let's zoom back out rather than focusing on RevPAR, I guess what are

some of the drivers that are in your control as you think about major initiatives that you and the leadership team are prioritizing?

Kathleen Oberg: So I'm sure you're all familiar with our NUG conversation and that is one that is near and dear to our hearts because at the end of the day, we really want to be able to deliver to all of our Bonvoy members the widest range of travel locations, whether it is a certain price segment, a certain location, a certain tier, or a certain kind of hotel. And with that, we obviously work very hard on the luxury end.

I'm sure you saw our announcement yesterday of three outstanding luxury conversions in North America, Turtle Bay in Hawaii, Pelican Hill out in Newport Beach, and then one right here in midtown Manhattan. So really exciting in-the-year-for-the-year conversions that really demonstrates our emphasis on the luxury brands, as well as really making sure that we've got fabulous opportunities for our customers to earn and redeem points at luxury locations around the world.

But then also, as you know, Stephen, moving down into the midscale tier of lodging, which for us over the past 18 months has been a new market entry point for us. One that really arose as a result of combination of conversations, both with our customers kind of first level Bonvoy members, if you will, traveling salespeople who say, it's great that I can find a Fairfield, but I really would like to be able to find in a tertiary market, something that I still can stay within the Bonvoy system.

And then also in the extended-stay space where you've got folks going and staying somewhere for three or four weeks as they work on a project. So we announced this week at NYU entry into the transient midscale, probably heavily conversion market, in addition to StudioRes, which we announced a year ago and have really terrific, terrific number of projects.

On StudioRes, we've got 140 projects that are already that we've got engaged with owners and then working on another 100 more. So I would say a terrific demand from owners and franchisees to be able to add more hotels that really fit the widest range of stay opportunities for our guests. And that, at the end of the day, that's what we're really trying to do.

And then I'll add to that that, I think, the digital experience and all the tech work that we're doing is a critical part of our strategy right now. That is, I would say, about one-third. We're going to really start rolling it out to the properties next year. So we're very excited with how that's coming and believe it will have both revenue opportunities and productivity enhancement opportunities and provide value for all of our constituents.

Stephen Grambling: One of the areas that you touched on the very beginning, but I'll circle back on is Bonvoy. That's something that I think, you had at the five-year anniversary was in March. Can you walk us through some of the major milestones that have been achieved since that launch and then how you think about the opportunities for it going forward?

Kathleen Oberg: I think we always talk about Bonvoy being the moat around the castle of our portfolio of brands. And I think we only believe that more strongly now than ever. And I can remember for many of you saying the word Bonvoy five years ago and many of you looking at me like what, and then having Rewards and SPG rolling off your tongue.

I was recently teaching at a business school and I was talking to them about the programs and they were all like SPG, what's SPG? So it's amazing how quickly time rolls forward. And now I think Bonvoy

has become a well-known brand name that really provides the halo for all of our brands and has grown both in its penetration at our hotels meaningfully. So we're looking at mid-60%s over all of our hotels and close to 70% in the U.S. So really just tremendous growth in terms of understanding on the part of the customers about the value of being a member of Bonvoy.

But just as important is that we've really been able to expand the experience of Bonvoy, make it much better when you think about the digital experience. You now can search in more ways on Bonvoy than you could before in terms of not just saying you want to go to a certain city but that you're looking for a certain kind of experience. There's more there.

And then obviously, all the non-RevPAR fee-related opportunities that are built into Marriott Bonvoy through the credit cards now in 11 countries, which provides, as you know, a really strong delivery of fees, a residential brand portfolio, travel insurance, HVMB, the Homes & Villas by Marriott Bonvoy. So I think, again, you continue to see the broadening of the experience and value of Bonvoy for our customers, which is all designed to continue to deepen and widen that moat.

Stephen Grambling: The first thing that you highlighted was room growth. I guess, what is the health of the development market as we look across different key geographies? We've heard from some of your peers that perhaps there's been some slowing in construction starts. But be curious to hear if you're seeing that and how you're trying to navigate the environment.

Kathleen Oberg: Sure. So we'll start in the U.S. As I'm sure many of you know, the way new hotel supply works is very much tied to the macroeconomic picture of a certain country. So for example, in the U.S., which is a very well-established economy, you're looking at some of the lowest supply growth that we've seen in a long time, probably about half of what it was pre-COVID. And really, even that is really concentrated on the lower-end tiers.

So certainly on new construction, while this year we've seen an increase relative to a year ago, probably 25% more new construction starts in the U.S. than a year ago. That's still about 50% of what it was in 2019. Now the good news is you've really seen that replaced by conversions and a growing acceptance on the part of owners worldwide of the value of converting into one of our brands, be it a hard brand or a soft brand.

And there, it's been really encouraging to see how internationally those conversions are now just as typical than they were in the U.S. Where in the U.S., since we started Autograph, it's been over a decade ago, it's been quite typical. But I think that has only grown as owners have seen the financing environment be tougher and the value of being associated with a low-affiliation cost and high-revenue-producing brand has grown.

But then outside the U.S., it's really gained a lot more acceptance of converting into one of our brands. And so there we're looking at probably getting close to a third. Around 30% of our room openings, we would expect over the next couple of years to come from conversions. When you do look at other parts of the world, it varies tremendously.

Couple of comments that I'll make that I just think are interesting. Greater China, while the demand environment has clearly been more challenging in the short term, the development pipeline and openings has continued to be very strong. Part of that is our extension into kind of the lower end. So we're seeing great acceptance of our select-service brands in Greater China. And that pipeline has grown as well as the openings.

And then I'll just point out a couple other. India has been absolutely extraordinary. Makes sense, you've got an economy that's been growing quite rapidly and with a growing middle class. And I'd say, Marriott has a really spectacular leadership position in terms of growing our brands in India and the hotels have been performing very well. APEC delivered over delivered about 10% rooms growth net last year in that region of the world. So I say continued very strong growth there.

Stephen Grambling: On the conversion side and maybe there's a broader question about what the pipeline looks like, but I know some conversions aren't in the pipeline. Is there any difference in the structure of those contracts as we think about fees per room and the contribution to the business when we look at a percentage of RevPAR should be a percentage of fees?

Kathleen Oberg: So I would say, structurally, no. I'd say fundamentally not. The only thing I'll point out, which is, I think something that you're all familiar with is that if you're doing a deal at the higher end, the luxury end, as compared to lower end, you are more likely to have key money involved. So if you hear us do a luxury conversion, it's more likely there's key money involved.

While if you do a conversion down in midscale, there's not likely to be key money involved. And that's actually a very kind of consistent trend with the way our development is done overall because we are doing more conversions, particularly at the upper end. I think you are seeing a trend of a bit more key money usage then perhaps when money was close to free.

But from a value perspective of the contract, we're not seeing a diminution of the value of the contracts in a material way. So we're very disciplined about how we look at how much capital we put into deals. So while there may at the very top end be key money usage on a conversion, it's still very much in line with the kind of value that we would expect to create.

On your fees per key question, clearly, as we move into more relatively lower RevPAR markets, and given our fees are overwhelmingly driven as a percentage of RevPAR or room revenues at a hotel, you would naturally expect that maybe those fees per key over time will go down. But the reality is that we've got several offsetting things. One is that we are growing, relatively speaking, more internationally than we are in the U.S. That tends to be more managed more, full-service. You tend to get incentive fees earlier in Asia than you do in the U.S., and so that is helping your fees per key.

You've also got non-RevPAR-related fees like the credit cards. They are generally growing a tad faster than the RevPAR-related fees. So you put that all together and you get actually that you should expect fees per key overtime to continue actually to go up a bit.

Stephen Grambling: Okay. Maybe a follow-up on key money, just to make sure that that's clear. So you're seeing no real change in the competitive environment in terms of deploying key money in your underwriting for where you do and don't?

Kathleen Oberg: I guess here what I would say is that everybody's chasing conversion. There's no doubt. It's highly, highly competitive. I'm sure you're hearing that from all of my competitors. And so by that very nature, there is, of course, going to be a way that you compete over various aspects of the term, aspects of what the hotel is going to need to have invested in it, as well as key money. So it's one tool.

And as I was saying, we aren't doing as many new build luxury hotels as perhaps before. And from that perspective, you would expect to see a bit more key money. But I would say we use key money on

roughly almost a third of our deals. And I'd say average key money might be about $1 million per deal. But again, at the lower end, almost always nothing. And at the higher end, it's going to be more than $1 million.

Stephen Grambling: Yes. Fair enough. One of the other questions we've been asking everybody is just around margins, industry margins. I guess we could be more focused on owner margins. You can talk about your margins. I feel like that's a little bit more straightforward. But if you can touch on maybe both of those, how you think about the puts and takes for this year and maybe looking longer term?

Kathleen Oberg: So I'll do our margins first because that's the easiest. I think you should continue to expect that we will grow our margins. It's pretty straightforward there, as you look at continuing to grow rooms and RevPAR and having some operating leverage. As we move forward, you should expect that they will continue to improve. They're already pretty good.

On the hotel margins, you're right. Depending on where you are, a tough dynamic in terms of continuing rising labor costs and now you are clearly seeing normalizing RevPAR in the U.S. We actually, so far this year, saw our managed margins in the U.S. be roughly flat. Obviously, we're outside the U.S. when you're having RevPAR numbers that are like 10%, 12%, and 14%, your margins are growing and that must the case in those markets.

But in the U.S., it is clearly something that we are incredibly focused on. We are seeing labor wage pressures moderate. They still exist, but they do moderate. And we obviously, as you know, we're still seeing pretty decent ADR growth as well, just obviously moderated quite a bit relative to last year.

I think the way I would describe is something that we've worked on very hard over the last number of years, and that is to really be working on our productivity at the hotels and being very careful on the revenue management side and thinking about the types of guests and the types of the business that they bring in terms of food and beverage and all the other components that they bring to a hotel because at the end of the day, you're really trying to provide the most operating profit per key that you possibly can.

And I think as I said, with our roughly flat margins year to date, we've done a good job. But I think we will need to continue to see that we find productivity savings to manage this normalizing ADR and continued pressure on wage rates.

Stephen Grambling: Great. One of the things that we heard yesterday was our economists talking about their expectations for rate cuts at the end of the year. Remind us of your capital allocation priorities and how you think about managing the balance sheet in that environment where rates are still high, but maybe they're going to come down.

Kathleen Oberg: So I think we've set ourselves up to really manage whatever comes our way. And I'd say first of all, we do use commercial paper, which I do hope over time will benefit from what happens in the interest rate markets. At the moment, it's more expensive than I would like, and we do not have as much of it as we used to carry pre-COVID, and I don't expect that we will.

So broadly speaking, we are at the low end of our targeted leverage ratio range, which is 3 to 3.5 times debt to EBITDAR. We really have been at the low end ever since we came out of COVID, and I would expect we stay there. That gives us tremendous flexibility for whatever changes we see in the economy.

If you go from 3 to 3.4 on our leverage ratio, it's either a massive amount of debt or a massive change in EBITDA. So we feel very comfortable with where we are and do not anticipate currently having a change in our allocation of capital, which first and foremost, goes to growing our business in ways that add shareholder value. And then after that, are returning the capital to shareholders through a modest dividend and share repurchase.

I think you've heard our numbers for this year of $4.2 billion to $4.4 billion, as expected, return of capital to shareholders. And we continue to have very strong cash generation in the business. It's really an extraordinary characteristic of our business model.

Stephen Grambling: I guess, it's an election year right now. How does that usually impact your business? And then, are there any key proposals that you're watching for that could impact financials?

Kathleen Oberg: So it is interesting. This year, I think, it's one of the largest years of national elections worldwide. Somebody gave me a number, there are like 50 national elections worldwide, which I think has everybody watching the economists and any other global news services very carefully. We operate in 141 countries. So we really do pay close attention to what's going on in the environment.

But I would also say it won't surprise you. For our business, what we look to most of all is to have a healthy, thriving economy in whatever countries that we're operating. So always that's what we're hoping for out of an election.

I think in the U.S., we would imagine that if it is that President Biden wins another term, it's likely to be a bit more of the same. I think if it turns out that Trump wins, then you could see a bit more volatility, which we'll all have to take into consideration. But at the same time, I think you have to look at the law making side, too, which is that I think whether who ends up controlling the House or the Senate, you've got the likely situation that it will be very tight, both ways.

And so I think it could mean that we still end up with law making that it is tough for things to get through and to see major changes. So in the business for this year, there might be a few more people who stay home around election week, but it tends not to have a massive impact on the business. And frankly, something that as we went into the year, we took into consideration for the various conventions, et cetera. So it was already embedded in our numbers.

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Stephen Grambling: Makes sense. We have time for one or two from the audience. I have a couple on my end if people are bashful. A brave soul is up. Jamie.

Unidentified Participant 2: Thanks. Just back on the conversions. We've seen quite a few portfolio transactions like own one with MGM and IHG earlier talking about the NOVUM deal in Germany, how competitive that was and everyone was after it. I guess, that probably include you. But the fee –

Kathleen Oberg: As I said, we're all quite competitive.

Unidentified Participant 2: Just the two questions. The fees on some of these look a bit low relative to the rooms, partly key money, partly structure. And secondly, are there a lot more of those in the pipeline? And could we expect sort of 1%, 2% extra NUG growth from these sorts of announcements?

Kathleen Oberg: Well, I hope so. That would be lovely. The numbers of 5% to 5.5% don't assume any large strategic transactions. They do assume our more normal pace. And based on the 547,000 in the

pipeline that we had at the end of Q1, that is the more kind of classic, normal, that may have several smaller multiunit deals in them.

In addition to MGM, we announced one right around the call that was 14 midscale conversions of hotels in Japan for Four Points Express. And I think that's a great example where an owner or franchisee can really see the benefit of doing several hotels in one fell swoop rather than all in just onesies and twosies. So I do think again, along with the comfort of conversions, I would expect to continue to see more of those.

We're very large. So I think, the reality is, as we get over 1.6 million rooms and on towards 1.7 million, you're going to be looking at those multiunit opportunities to grow, as being a normal course of what we're doing.

In terms of the fee components, I think then it does become more transaction-specific. When I think about the conversions that are kind of our normal, run-of-the-mill, if you will, conversions, they really have a much more classic typical fee structure that fits with the brands, involves an amount of capital that is reasonable, clearly still very strong accretion to value to the firm, et cetera.

I think, you know, for MGM, obviously that is a unique transaction. In a way, you've really got hotels sharing two powerful brands. So that's not going to necessarily have the same standard franchise fee arrangement, but it's still going to be a clear reflection of all the revenues that we drive to those hotels. And obviously, the more we drive, the more we get.

And may not look exactly like your typical franchise agreement, but still incredibly, incredibly value-enhancing to the company, overall. But I would say MGM was a pretty unique transaction and not one that comes along every day. So I think generally speaking, the vast majority of our conversions are pretty classic conversions into our normal royalty parameters.

Stephen Grambling: We've gone about a minute over. Please join me in thanking Leeny Oberg from Marriott.

Kathleen Oberg: Thank you.

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