Marriott International, Inc.
Bank of America Securities
Gaming and Lodging Conference Transcript[1]
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Shaun Kelley - BofA Securities: Good morning, everyone, and welcome to our next session. I'm Shaun Kelley, the U.S. Gaming and Lodging research analyst at Bank of America. Our next conversation is with Marriott International.

So, let's get that off the ground. It's my pleasure to welcome Marriott's Chief Executive Officer, Tony Capuano. Tony, this is your first time doing this event with us. And hopefully, the last time we do it virtually. So, we'll hopefully be in person next time. But you're joining us from beautiful Rome.

Anthony Capuano - Marriott International, Inc.: I am.

Shaun Kelley: And so, this is the benefit of virtuality is there's no way we could have you if we didn't do it this way. So glad to have you and thanks for joining us.

Anthony Capuano: Well, thanks for the invitation. Great to see you at least on video, Shaun. And as much as I'd like to be in person, it's great to be back in Europe and talking to you from here where business continues to improve.

Shaun Kelley: Fantastic. So, let's just hit it off right there. Obviously, we've -- the big question marks out there relate a lot about the current trajectory of everything going on with the travel recovery. Maybe we can just start with the kind of the big question, I think, in everyone's mind, which is going to be the pattern of sequential RevPAR improvement and possibly the impact of the Delta variant from what we've seen out there. Obviously, it's a little delicate, but we do all have access to kind of the reported RevPAR numbers through the end of the balance of August. So, what can you help us kind of understand about travel behavior as we sit here today versus maybe where we were sitting 6 to 8 weeks ago before Delta was as pronounced of a concern out there as it is today?

Anthony Capuano: Let me frame my response maybe with some broad global statistics, and then I'll try to get a little more granular. As you pointed out, you've seen the numbers. Our global RevPAR in July was down about 23 percent when we compare to 2019, which was a marked improvement over what we saw in June where we were down roughly 38 percent.

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

Now as the August numbers come in, we've seen a slight retrenchment. We think the August numbers will land at about 27 percent down versus 2019, probably a little bit of Delta impact there, but we are seeing some stabilization in the early days of September.

And if I start to move around the world, without question, China saw the biggest impact in August. We had an incredibly strong second quarter in China as Leeny and I shared on the earnings call, but we saw a spike in COVID infections in August. You saw a pretty stringent lockdown put in place really in over 150 markets across China, and that obviously impeded the pace of recovery. We saw a RevPAR decline of about 50 percent in Mainland China in August when you compare it to August of 2019. And remember, that was in comparison to being up about 9 percent in July versus 2019.

Now the good news is, and you've heard me talk about this before, Shaun, one of the great benefits of our business is we can look at these trends in real time. And so now that most of the restrictions have been lifted, we expect to see demand continue to rebound quite quickly across those 150 markets.

In the U.S. and Canada, August RevPAR was down about 21 percent versus 2019, which is a little worse than what we saw in July where we saw about a 17 percent gap. But again, the trend seem to be stabilizing as we get into the early days of September.

If you move around the rest of the world, you almost have to go market by market. I'm at the end of a two-week trip through Europe. I was in Germany last week, in Italy this week. And it's interesting, I was with our Italy team earlier this week. You look at July and August here in Italy, we were running between 40 percent and 50 percent across our Italian portfolio, which is a strong improvement over what we saw just a few months ago. And rate was actually above where we were in 2019 for July and August. So that's quite encouraging.

And even in markets like India, which, obviously, had been heavily impacted by the pandemic, as those numbers start to plateau, we're seeing some steady improvement in that market as well.

Shaun Kelley: So, Tony, let's go a little higher level then. I think what we're really trying to get to is the broader shape of how this recovery plays out. We kind of sit here at a crossroads, we've got Delta, but we would also have the roll off of leisure and sort of the return-to-office trend. We were hoping it would probably be a little bit more pronounced than it is in September.

So just help us think about -- sort of level set expectations for us into kind of the back half of the year here. Coming off of these levels, what makes sense for people to expect as we look out for the balance of the year? What can you see in your booking curves? And just what's a reasonable expectation for maybe the exit rate? And is it any worse than probably what you were thinking 6 to 8 weeks ago? Or is it roughly similar?

Anthony Capuano: Well, Sean, I might frustrate you a little bit because we continue -- as we look into that crystal ball, it's probably a little more opaque than any of us might like. I would say, broadly, we're pleased with the momentum we're seeing in the recovery, and our confidence continues to grow about strong long-term return of travel across all segments. But again, as I mentioned earlier, the pace and the shape of that recovery curve vary sometimes significantly from market to market.

And so, we continue internally to talk about when, not if, and we ask that question by market. I think we're encouraged by what we saw in China. I think during one of the earnings calls, we shared with you some statistics from April where we saw in China, not only a return to pre-pandemic levels of demand, but a return to pre-pandemic levels of demand across each of the segments. And I think at the time, what I said on the earnings call was, that gave us perhaps a road map about how we might see demand recover in other markets around the world.

Certainly, when you look at the potential impact of the Delta variant, the impact that's had on the timing of a return to the office, it is possible that we may not see business transient demand return as quickly as we might have hoped post-Labor Day. But again, it's early to tell. The booking window for business transient is so short right now that it's really tough to know how much of a bump in the road, a delay of a return to the office might really represent.

On the flip side, the federal government's decision to give full approval to the Pfizer vaccine, we think, is great news for us. More and more school districts across the country returning to in-person schooling, we think, is great news for us. And so, we continue to be optimistic, if not a bit frustrated, about having -- not having better visibility into the precise timing of the return.

I can tell you, I've been on the road a ton over the last month, 45 days. As I'm talking to our customers, they are increasingly anxious to get back on the road, I think, particularly in categories that are client service focused. So, whether that's law firms, accounting firms, consulting firms. As I talk with their partners, they are anxious to get back out in front of their clients.

Shaun Kelley: So probably the best place to maybe end the kind of current trajectory piece to ask a little bit about that last comment, we continue to see the sort of ping pong ball move between the idea of structural impairment to corporate behavior and going back to normal just as it would have been. And I think some of that optimism that we were seeing maybe early in the summer did meet with a little bit more concerns around these delays on the return-to-office pattern that we've seen, some major corporations pushing back to the end of the year.

And so, I guess, as you look at it, is there anything in those conversations that you think is changing that maybe the double dip has further embedded them as it relates to technology or behavior? Do you really think that at least in the major pieces of the business transient landscape, this will come back with the cycle, with the corporate profit activity as the Delta variant sort of fades into the next wave?

Anthony Capuano: The one comment I might make in response to that, and as we -- as I mentioned to you before, we went live here, in some ways, I'm the perfect illustration of this. While I am very optimistic about the return of business travel, I do think it may look a little different. And there are two trends that we've started to see emerge that I actually think will endure well beyond the end of the pandemic, both of which, I think, are good news for our business. And so, use my trip to these last two weeks as an example.

Number one, I've probably been attending the IHIF Investment Conference in Berlin for the last 15 or 20 years. And my guess is, if I look back over my calendars, I would fly in overnight from D.C. I'd spend two days in Berlin and I'd fly right back. This time, I thought, if I'm making the trip across, if I'm getting my vaccine status notification in place, I'm going to extend that trip. So, I'm actually here in Europe for two weeks.

The other trend you've heard me talk about in the past is this notion of blending of trip purpose. And again, I did the same thing. I spent a week in Germany. My wife came over. I spent a couple of days of leisure in Italy. She flew home and then I came on to Venice and Rome to pick that business trip back up. And so, I continue to believe business travel will come back. It just might be a little more difficult for you and I to sit in the lobby of one of our hotels and know with absolute certainty every guest that walks by: Are they a business traveler? Are they a leisure traveler? Or are they a group meeting attendee? Or more likely some blend of some or all of those trip purposes.

Shaun Kelley: So, I'm going to bounce around a little bit on our topics, but I think this is an important one, right? Obviously, near and dear to your heart is development and development ties well into brands and kind of how you really grow the size and the flywheel of what Marriott is today. So how do you lean into this blending of trip concept, right? So, I think one area where you've been really ahead of the curve and dynamic is with what you're doing in Homes & Villas. But what are you doing being on the brand front or on the -- working with owners? What are you starting to flex a little bit to try and, I guess, make the hotel product of yesterday meet the sort of new travel needs of tomorrow? Because I agree with you, I think my own needs, my own desires, they've tweaked a little bit and the pressure to maybe rush back is different. You're still going to be present, but you're also going to be trying to balance that out differently than maybe we did previously.

Anthony Capuano: It's a great point. And the good news from Marriott's perspective, because these are big physical assets, it's -- you can't, with a snap of your fingers, transform the physical asset necessarily. But what that means is we rely on the resourcefulness and the adaptability of our associates around the world, and that's a bet I'm really comfortable making. As I travel around the world, I see the creativity and the -- again, the adaptability that you're seeing from our team. So, whether that is better arming our concierge desks to make sure they understand they may have more leisure guests in a hotel that has historically been heavily weighted towards business travelers, and making sure they're armed to provide the sorts of information that, that leisure traveler demands. Maybe being a bit more creative on the offerings that we have in our food and beverage outlets, in our room service menus, again, to try and tailor a little more.

I was at one of our hotels that had gone out and acquired a bunch of bicycles to make available to leisure travelers that wanted to explore that city. And so, I think it will be more on the need anticipation and the service delivery side, which is a place where I'm very comfortable in the ability of our associates around the world to not only meet, but really exceed the expectations of that evolving traveler.

Shaun Kelley: Great. Well, let's stick with the sort of growth and development side a little bit, but get into more traditional metrics that you and I both know. Let's talk about signings and development activity a little bit. What are your latest conversations right now with developers looking like? And how -- and also maybe just your thoughts on the conversion activity out there. Obviously, this time of the cycle tends to lend itself to that activity as there's a lot of volatility. So just maybe start with both of those areas.

Anthony Capuano: Of course. And maybe if it's okay, I'll go in reverse order. I think on the deal signings and the conversion impact side, as you heard in the second quarter earnings call, we had really strong openings through the first half of the year, and about 1/3 of those openings were conversions, which is a very high percentage for us relative to historical averages. Maybe not a huge surprise, but a really encouraging set of data. We are armed with the best set of conversion brands across multiple price tiers that maybe we've ever had in our history, and those seem to really be resonating with our development partners.

On to your first question, as I said, I was at IHIF, which is the biggest development conference in Europe. I can tell you that in a really positive way, my dance card was full. I had 23 owner meetings during the two days that I was in Berlin, owners who are increasingly confident that they have weathered the storm, feeling better about the manner in which they've stabilized their balance sheets, feeling good about the discussions they're having with their lenders, feeling like as demand recovers their liquidity is improving. And they are much more active than even a quarter or two ago in terms of the volume of deals that they're talking to us about, both on the new build side and the conversion side.

Now admittedly, as you point out, given some of the continued constriction we see in the debt markets for new construction, maybe the conversations are a little more heavily weighted on the conversion side, but very active discussions. We had about 1,300 attendees at IHIF. And in a very good way, it felt a little more normal, the same sort of pace of discussions that we've enjoyed over the last couple of years.

Now it's obviously incumbent on our teams to take those really encouraging discussions and ensure that they translate into signings and, ultimately, openings. But the tenor of the conversation was quite encouraging to me.

Shaun Kelley: So, if the lead pattern is certainly there and obviously you've got the brand portfolio necessary for conversion, let's translate that a little bit into the kind of the ultimate number, which is either gross unit growth or NUG a little bit for those who are into the industry parlance. Just help us think about 2022 versus 2020 -- versus 2021 in terms of how all this crystallizes for Marriott. Obviously, there's a little noise with the SVC portfolio and some of those exits or that transition. But sort of on an apples-to-apples basis, help us understand because you do specialize in some of these larger full-service, we know, high dollar and high fee type hotels. Does that lag in construction activity weigh on net unit growth into 2022? Is there any way you can repeat what you've done in 2021? Does that lag last into 2022? How long does that tail before we start to see the next cycle and some of that optimism play through the actual numbers that you're posting?

Anthony Capuano: Yes. And I'm going to give you a little bit different version of my earlier answer. It's -- while we're seeing lots of encouraging signs, the murkiness as we get much beyond the end of the year, makes it a little challenging for us to give you a lot of detailed forecast data into 2022. What I can tell you is we are increasingly confident in the -- both gross and net unit growth percentages guidance that we've given you through the end of 2021. As you point out, we've got that roughly 100 basis points headwind from the SVC portfolio, which we think is a onetime event. If you exclude that from the calculation, we would have guided to about 4.5 percent net unit growth here in 2021.

And again, what gives us lots of optimism as we peer into 2022, I think it's two things. Number one, we continue to have a pipeline of nearly 500,000 rooms with well north of 200,000 rooms under construction, which I think is a really terrific and encouraging leading indicator. And I also think that statistic I shared with you earlier about the front half of 2021 and the volume of conversion activity we saw. Even if the debt markets continue to open a little more slowly than we might like for new builds, that pace of conversion volume should give us lots of optimism as we look beyond the end of 2021.

Shaun Kelley: Great. Let's kind of move on to another tangential to this, which is Marriott, historically, had been actually pretty active on the M&A front, sort of combining new brands -- acquiring new brands that way and obviously rolling them out through your own distribution network. So, we started to see, at this point in the cycle, a little bit of activity. We saw a major deal in the all-inclusive and resort space, in particular, which is an area that you also, I believe, had an announcement in relatively recently. So, can we talk about that type of activity out there? Are you seeing opportunities present themselves? And is this still an area where Marriott would look to grow the portfolio? Or do you want to really focus on the brand family that you have and drive growth through existing brands?

Anthony Capuano: Well, most certainly, right now, we remain pretty focused on deleveraging. As we've said on the earnings call, our priority is really to maintain our investment-grade rating. And as the recovery continues to unfold, we are increasingly confident in our ability to achieve that goal.

But make no mistake, if the right opportunity presents itself, we will certainly evaluate that deal based on its merits. I don't think you should expect us to look at those sorts of deals just to get growth for growth's sake. But if you look -- while the Starwood transaction rightly often consumes this conversation -- if you look at the 3 or 4 years before the Starwood transaction, we had a fairly steady cadence of smaller M&A deals, and they all tended to share similar attributes.

In some cases, they filled a strategic gap in our geographic distribution. So, I think about deals like AC Hotels in Spain, Protea Hotels in Africa. Often, these transactions also gave us a growth platform that we thought had either regional or, in some cases, global growth opportunities. And maybe AC is the best illustration of that when you look at the momentum we have now growing AC on a global basis. So, we'll look at those opportunities. We will balance our desire to maintain our investment-grade rating. And we'll use the same rigor and financial discipline that we've used for as long as we've been looking at M&A deals to evaluate those through the lens of geographic imperative and creation of new growth platforms.

But I do think embedded in your question was a comment about the current brand portfolio. And I would tell you, we are thrilled with the breadth of choice that, that portfolio offers. And we're really thrilled with that breadth of choice for two equally important constituents. Clearly, breadth of choice helps us drive loyalty with our guests, but it also helps us drive loyalty with our owners and franchisees who really need not look beyond the breadth of our portfolio to continue to expand their development pipeline.

Shaun Kelley: One other area I want to take this into is your thoughts on something, maybe perhaps a little bit more transformative. We're now 4 or 5 years removed from Starwood. And obviously, it was a major lift. We all know about the integrations necessary to combine two large and such well-known brands. But Marriott's not been afraid to take risk over the sort of two decades that at least I'm familiar with analyzing the company. I know you've been around for many more decades than that. And it's one thing that fascinates me as a business that has that type of history is one that you'll actually take those types of risks.

So maybe a big picture question, but as sort of the new leader and the new CEO of the business, one area that we view Marriott is heading into and sort of controlling right now is obviously distribution for its partners. Is there the option or have you thought about the idea of doing something more transformative on the distribution landscape? And just help us think big picture about the opportunities that could be out there. Should we be thinking more broadly? And I'm not saying now or a year from now, but maybe the next decade, thinking a little differently then, oh, we're just going to do a brand that has these four-wall boxes because it does feel like people in the travel landscape, particularly some big -- some very, very large companies, some very large market cap are thinking differently about the traditional definition of a stay.

Anthony Capuano: Maybe the way I'll answer that is to use a phrase that I think I've been using with increasing frequency, and that's this notion of business adjacencies. Certainly, our core lodging business drives the vast, vast majority of the company's EBITDA is the foundation of everything we do, and we'll continue to do everything in our power to enhance its performance and grow its footprint. With that said, I think about the last 16 to 18 months, and thank goodness we've continued to explore and advance some of these business adjacencies.

So, I'll give you a few examples. I'm not sure anyone would have faulted us for hitting the pause button over the last 1.5 years and saying, just stay laser-focused on demand recovery. And while that's been at the top of our priority list, during that period, we launched new branded credit card programs in markets like Mexico and South Korea. Here in the U.S., we launched a new partnership with Bonvoy and Uber. We launched just recently a new travel insurance product that's available to purchase through our websites with our partner.

Interestingly, last year, while enormously challenging for our core lodging business, was one of the most successful years we've ever had with our branded residential business. And so, I look at all these adjacencies, and I think it behooves us to continue to evaluate other opportunities to identify adjacencies that we think dovetail well with our core lodging business and that, over time, can evolve into revenue streams for the company. How expansive the mouth of that funnel might be in terms of what we evaluate is certainly to be determined, but I think you should reasonably expect us to continue to explore adjacencies.

Shaun Kelley: Great. Well, let's hit on a couple more things about the core business. I want to switch to operations for a moment, right? A huge topic and one that, as a manager of hotels, is certainly front and center for Marriott is staffing and inflation. So would love to get your thoughts on sort of the current environment for some of the staffing issues that we're hearing out there because, obviously, it's been challenging. I mean, first, operators dealt with the demand headwind, and now they go to reopen, and you can't find the housekeepers you need to drive the occupancy you want, or you can't find the experienced staff to really run the hotel to the service standards that you're used to. So obviously, service is kind of quintessential to the Marriott model. How are you helping owners deal with these headwinds? And what are you actually seeing kind of on the front line right now as it relates to these concerns?

Anthony Capuano: Particularly in those markets where we've seen the strongest demand recovery, that's perhaps where the staffing challenge is most acute. But we have to address it and we have to solve it because those are the markets where we have the best pricing power. But obviously, we can only satisfy our guests as we execute it with that pricing power if we're delivering the service that they've grown to expect in our brands. We are doing all sorts of things. We're obviously running job fairs. In some markets, we are offering onetime incentives to try and fill key staffing gaps.

The other thing, though, that I think we're doing -- and Shaun, I talked a little bit about this in my remarks in Berlin. This is a Marriott issue. I think it's an industry-wide issue. From Marriott's perspective, depending on which consultant you believe, you've seen a significant portion of the workforce in travel and tourism leave that industry segment, perhaps permanently. And so, we need to do, as an industry, a better job of spreading the narrative about what a compelling set of industries this is to build careers.

And certainly, at Marriott, that's a story that I'm enthusiastic and proud to tell. We've got a wonderful story to tell about the number of general managers we have across the system who started in hourly positions. And I think you'll see us ramp up our global communications efforts, our employer branding efforts, if you will, our presence on social media channels to make sure we're telling that story and make sure prospective associates understand the really remarkable opportunities they have at Marriott.

Shaun Kelley: So, I don't typically think of hotels as being sort of that bottom rung of employment, that first job, if you will. I've always thought of this being a more value-added place, a little bit higher up. But obviously, it's a big brush when you paint the kind of overall service and hospitality industry. And when we see the industry statistics out there on inflation or on open positions, the statistics are pretty daunting. So, what level of concern are you hearing from owners back in? Is this like a deafening roar from your owners right now? Or is it a major concern and something that people are worried about, but a manageable risk in the grand scheme of everything everyone in this industry has been through over the last 18 months?

Anthony Capuano: Yes. We're engaged -- one of the -- maybe one of the few positive byproducts of the challenges of the last 18 months, I would submit to you that we are more deeply engaged with our owners and franchisees on a regular basis. We've always been deeply engaged, but maybe the cadence of that has accelerated. And that is certainly to our great benefit, I hope, to the great benefit of our partners. They look at the phenomenon you described as two sides of the same coin. They are most certainly and appropriately concerned about wage inflation, particularly in those markets where the staffing challenges are most significant. At the same time, they look at the impact of inflation and they see it in the pricing power that we're seeing again in those markets where demand is recovering most quickly.

And I think really, the challenge they give us is you have, Marriott, through the last 18 months, identified a long list of really compelling operating efficiencies. Help us understand how you can preserve as many of those efficiencies as possible going forward. And that's the dialogue we continue to have. I'll fly home from Europe this weekend and spend two full days in Washington with a broad cross-section of our U.S. owners and franchisees. And I think that will be a topic near the top of the agenda.

Shaun Kelley: So, a perfect segue and maybe the last two areas I'd like to touch on, which is could we elaborate a little bit on some of those brand standard changes and what's really on the table for owners here? One thing we hear about a lot is opt-in housekeeping at certain levels of brands, and it's not universal across the industry. It's probably not universal across any portfolio of brands. But is that something that is on the table for Marriott? And what other things might you be able to flex with or on that maybe previously hadn't been as front of mind in a more, let's call it, revenue-oriented environment?

Anthony Capuano: All the topics you described, we are in active discussions. We're talking about housekeeping protocols as you might expect. Our point of view is evolving. It is heavily informed by what we hear from both our owner community and our guests, and it varies by market and by quality tier.

Food and beverage, I think, falls into the same category. Are there efficiencies that we have identified? Are there modifications to our operating protocols that are resonating with our consumers that we think have legs even beyond the end of the pandemic? And again, these are the sorts of topics that will go deep with our owner community next week in Washington.

Shaun Kelley: So, it sounds like that one is kind of real time. With the remaining couple of minutes, I'd love to just hit on sort of the last piece of the algorithm. We've talked about top line. We've talked about either the net unit growth and the development side. But sort of the last leg of the stool for Marriott's business model and earnings we always think about is capital return. So obviously, the business in its heyday is highly cash generative by its nature. But help us think about, as we start to return to normal, and I think you've already alluded to the fact that deleveraging is the top priority, but help us think about where do you need to be to get to perhaps back to the kind of classic IG range you'd want to be, whether it's a specific leverage area. Or what do you need to be to actually start to pull again on a capital return lever? And have any of those priorities changed kind of post-pandemic relative to sort of the algorithm we used to see?

Anthony Capuano: So, there's a lot in that question. I'll try and maybe parse my responses.

Shaun Kelley: Sorry.

Anthony Capuano: No, no. It's the right question to ask. I think, again, you've got a little bit of this murkiness. I will tell you that we continue to see strong progress in getting back to that kind of historical 3x to 3.5x leverage ratio. I think if we continue to see the sort of progress we've seen to date, I don't think it's unreasonable that we could be back to talking about return of capital sometime later in 2022.

But our philosophy remains the same, Shaun, and I don't think that will surprise you. We'll first invest in the business where we think the returns are going to exceed our cost of capital, and then we'll look to return excess cash to our shareholders. Whether that's through buybacks or dividends, we'll determine at that point in time. But I think the latter half of 2022, if the recovery continues the way we've seen it recently, I don't think that's an unreasonable expectation.

Shaun Kelley: We have a really broad swath of people on the line here. So just maybe the last kind of component, if I could sneak one in, would be dividends versus buybacks. Is it important to get back to a material dividend, let's call it, a yield above a certain threshold? Yes, I think usually, it's been maybe around 1 percent or a little bit above that. Is that an important priority for you as an executive or do you think for the right shareholder base going forward? And would the rest or excess possibly being targeted more towards buybacks? Or does that ratio change at all?

Anthony Capuano: I don't think it will change materially. But again, until I've got my arms maybe a little more firmly around the pace at which we're going to get back to that leverage ratio, it's a bit hard to say.

Shaun Kelley: Yes. I know it's early. So well, it may be early, and it's early here, but it's getting towards the afternoon there, and I believe you have some priorities for this afternoon. So, I don't want to keep you from that any longer. Thank you for joining us, especially internationally. Glad the connection worked out. And again, your backdrop definitely trumps mind. So, look forward to doing this again state side, hopefully, in person next year, Tony. Appreciate your time.

Anthony Capuano: I can't wait. And thanks again for the invitation. Great to see you, Shaun.

Shaun Kelley: Thanks, everyone. Please stay tuned for our next panel.

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