Marriott International, Inc.
J.P. Morgan Gaming, Lodging, Restaurant & Leisure Management Access Forum Transcript[1]
March 12, 2021

Joseph Greff – J.P. Morgan Chase & Co, Research Division: All right. Good morning, everyone. Welcome to day two of J.P. Morgan's Gaming, Lodging, Leisure and Restaurant Management Access Form. That's a mouthful. Up next for this coming fireside chat session, we're happy to have with us Leeny Oberg, Executive Vice President, Chief Financial Officer of Marriott International. Welcome, Leeny. As always, nice to have you here.

I do want to start out and again, express my condolences and wishes to the Marriott and Sorenson family. Arne was a very special person, more than just a very talented executive. We had a keynote session with Jamie Dimon yesterday. And the hour before he was with us, he was at a Business Roundtable event. And he mentioned that the BRT had a nice testimonial for Arne. And Jamie mentioned same thing, a talented executive, but just a real good human being. So, I just want to start off with that. The other thing I'd like to start off...

Leeny Oberg - Marriott International, Inc. - Executive VP & CFO: Well, thank you very much. We really appreciate it.

Question and Answers

Joseph Greff: Of course. Maybe a good point to start off with this conversation is, obviously, we have Tony, who's relatively well-known to investors, given his visibility at past Investor Days, and the same thing with Stephanie. Maybe you can just talk about, obviously, Tony as CEO and succeeding Arne. And then Stephanie, I think you need about two or three pages to detail her role as, ostensibly, the number two person. Can you talk about the structure and maybe who's underneath Stephanie? And to the extent that anything might be different with Tony versus Arne previously?

Leeny Oberg: Sure. So again, thank you. We appreciate your thoughts. It has been, as you might imagine, a time of incredible sadness and reflection here at Marriott. I know you, too, Joe, feel like I do, which is incredible fortune of having worked with Arne for 20 years. And we're moving forward really in the spirit of his legacy, which is with a real sense of purpose and optimism and energy. Because, as you know, that's what Arne was always about, in addition to his incredible generosity with people.

Arne had a really special way of working with his leadership team, which was an incredibly collaborative style. So, it wasn't kind of always a series of Leeny's in her row and Stephanie's in her row. We really work together a lot. And so, everybody was very familiar with the

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

challenges, the priorities and the strategies of everyone else. And it was really important to Arne that we all be moving in the same direction together. And so, I think in that regard, having Tony and Stephanie move to these spots just keeps us along on that same path.

Tony, obviously, as you know, under his leadership over the past, I think, probably 15 years almost as dead of Development, has added thousands and thousands of hotels and has overseen the growth of the company's brands and deals all over the world. And has tremendous relationships with owners and franchisees, amazing knowledge of how deals get constructed, design of brands and operations, et cetera. So, I think a great background for the company, as well as for where we are right now when you think about both the desire to help our owners and franchisees get through this, the best they can and come out healthy on the other side, but also with a sense of growth moving forward.

And then similarly, Stephanie and all of her oversight over consumer operations. One of the most critical parts of our strategy, as you know, Joe, is the growth and overall umbrella brand of Marriott Bonvoy. So, she will continue to oversee that entire area and then add to that the responsibilities for development, and -- the development organization that Tony has now stepped away from.

So then when you think about the remainder of the kind of the direct reports to the CEO, they remain the same. So, for example, I report to the CEO; our General Counsel reports to the CEO; Stephanie reports to the CEO; head of International, Craig Smith; and Liam Brown, head of North America, report to the CEO. So again, we'll take where we were and try to move forward with great determination.

Joseph Greff: Great. Excellent. How do you -- how is Marriott thinking about adapting or anticipating to any changes coming out of the pandemic with respect to leisure or business transient travel or group travel? And then how maybe do you anticipate development changing coming out of the pandemic? And whether there's differences geographically or differences between full-service and limited-service? I know it's kind of an open-ended amorphous question. But I would imagine there has to be changes that you're anticipating to strategically attack.

Leeny Oberg: Yes. Sure. So first, when we think about the business, one of the things I always like to remind people is that our general managers are really operating in an environment that is always seeing constant change. I'm always impressed by their ability to adapt quickly and be nimble to whether it is a natural disaster, whether it's a pandemic or, frankly, whether it's a deep recession. They are in the mode of constantly trying to maximize what they can do in their marketplace with the competition they've got and the economic forces at play. So, one thing I'll say is that they're used to this.

I can't say anybody is used to the pandemic, but they are used to having to constantly morph the kinds of business that they're getting. Certainly, as a company, from the leisure perspective, that's a part of the business. That as we entered the pandemic, it was growing faster than other segments of our business. So we've only accelerated the work that we've done in localization and personalization and making sure that people know drive-to opportunities for them for

leisure that are available and open the Bonvoy Escapes, where you can get a great rate on something nearby.

And then kind of all the opportunities around people needing a place to work during the day if they find that their home environment for remote work doesn't work. They've got a clean, safe place that they could come in a hotel, which we've got programs there.

And then I think more broadly, it is about this sense of a bit of the melding of business and leisure, where in some respects where you used to have Monday through Thursday being classic business nights and Friday through Sunday being classic leisure nights. I think now there's some really exciting opportunities, actually, to think about that stretching out over many more combinations and permutations. So there, again, I think there's as much opportunity as there is the potential for shift in the way the segments behave.

On the development front, it won't surprise you. There are the realities that right now for new build in many markets, the business are -- the banks are sitting by the sidelines and just kind of waiting to see how this rolls out. So certainly, in some of the conversations that we're having, there's interest and good dialogue, but not always signing on the dotted line because there's more need to have comfort around the financing.

At the same time, clearly, on the conversion side, there are meaningfully more conversations and really having our developers paying even closer attention to those possibilities. Where you see a hotel that may be kind of particularly struggling or kind of raising their hand about opportunities to strengthen their P&L, we obviously are paying a lot of attention to.

Joseph Greff: Great. There are a lot of things we can sort of address in that topic. But kind of maybe -- kind of putting to the backseat, the vagaries of near-term RevPAR performance, but also I want to maybe touch on a little bit later some of the green shoots that you and others are seeing in travel.

When you think about development and you said banks are hesitant right now and sort of in a wait-and-see mode, I'm presuming that's more specific to urban larger hotels, less so limited-service or select-service hotels. Does that mean if there is less of an available pool of capital for development? Does that mean you're getting more requests for that? And how do you sort of approach that?

Leeny Oberg: Sure. Well, first of all, I would say, you know this, Joe, the full-service new build urban market in the U.S. has been meaningfully quieter over the last five years than for upscale. And so, the vast part of new build has been, on the supply side, has been in the select-service areas anyway. So yes, there is more financing available on a relative basis. But I would say, overall, there's definitely been a bit of a pause across all segments.

And also, similarly, for the deals that were already financed and under construction, none of that is changing. Those financings are moving along and those deals -- those hotels are getting built, and we expect them to open. We've seen really next to no drop off from our under-construction pipeline of hotels. And then, again, depending on your market and how they are

emerging from COVID is where you can naturally see the trend in new signings, where Mainland China, for example, they're clearly farther along. While Europe, of course, is probably in one of the toughest positions, given all the restrictions and the really particularly low levels of business activity in those markets.

On the capital side, I would say, there's not -- again, it's not like the banks are kind of -- yes, there is lower LTVs when they're thinking about these deals, which would point to your question. But we aren't seeing a dramatic step up in the fundamental request for capital.

Joseph Greff: Yes. Your $575 million to $650 million of investment spend for this year is obviously below historical levels?

Leeny Oberg: Yes. And that's got $220 million of maintenance capcx in it, which includes a bunch of tenant improvements to develop our new headquarters building. So, if you really think about that, it is definitely, relatively speaking, a lower level.

Joseph Greff: Got it. We tend to associate periods of demand declines and periods of owner stress, what I want to call it, generally creating opportunities on the conversion side. Can you talk about what you're seeing on that front, particularly? What tends to be the big conversion brands? And who are you getting those conversions from? What brands are moving over to Marriott brands?

Leeny Oberg: So, it won't surprise you that the biggest area for these are our soft brands. So, Tribute, Autograph, Luxury Collection. The greatest example was the 19-hotel, almost 7,000-room conversion deal that we announced in January for all-inclusive with our partner Sunwing. And that's just a fabulous example where there clearly is, I think, a hope on the part of the owner to get the best of both worlds.

So, where there is already a strong set of hotels, that there is more that can be driven on the P&L from associating with Bonvoy and Marriott International's large global network of experiences and locations. So again, those are just perfect examples, I'd say.

One of the nice things is we see, generally speaking, where Autograph had kind of started at its core in the U.S., what we do see now is much more a sense of global conversions, where Asia Pacific has many more conversions than it had five years ago. So that concept is becoming more familiar with owners and, frankly, it provides us with fantastic opportunities because it is a bit of plug-and-play where you can have a dialogue and then -- and move to converting a hotel onto our system quickly.

And if you think about it, broadly speaking, in our signings, in Q4, 21 percent of our signings in Q4 were conversions. Conversions have typically been kind of mid-teens of room adds over the last several years. And often, as you're coming out of a downturn is when you see that percentage go up.

Joseph Greff: Great. And this year and last year, not surprisingly, slightly higher-than-average room deletions or churn, how do you see that beyond this year? I mean do you think you kind

of took a, I don't want to say a kitchen-sink approach to deletions, but would there be any kind of residual sort of hotels that need to sort of leave the system beyond what you have in 2021? And to put things into perspective, in 2021, you had a couple of chunky things in there that really kind of augmented that percentage churn.

Leeny Oberg: Right. So, I think, first of all, we've talked about our standard of 1 point to 1.5 points of deletions from the system. It is kind of being a fair normal run rate for us. And we had -- frankly, in 2020, we had expected that maybe it might be as high as 2 percent. But we have worked a ton with our partners, both in terms of reducing costs as well as trying to work through their cash flow issues, et cetera. And we ended up at 1.5. So, we were pleased with where that was.

In the numbers that we've given for 2021, we've obviously got the 1 percent related to the SVC Hotels. That was a unique portfolio that you're aware of, that we really don't have that situation in the company. That's a legacy deal from many, many years ago and, frankly, overwhelmingly, much older hotels that we look forward to have an opportunity to put some great new product in those locations.

But so, for the rest, we have talked about guidance of the normal 1 to 1.5, with maybe an extra 50 basis points related to COVID. And we'll see how that, kind of, comes about. I don't think you're looking at a perpetual, higher level of deletions over the intermediate and longer term. I think that, again, we're pleased with what we're seeing in the resilience of demand, and we can talk about that. So...

Joseph Greff: Yes. On that topic, though, would it be possible to see actually not a perpetually higher level in the medium term, but rather a little bit lower than average level in the medium term because you sort of pulled forward some of those deletions?

Leeny Oberg: No. I think 1 to 1.5 percent, remember that you've got tons of churn of agreements expiring. Could it be -- end up at 1 percent, that would be delightful. But I wouldn't -- I still think in that ballpark of 1 to 1.5 percent is the right place to think about. And again, it's going to take us a little while to work through the recovery from COVID. So, I would love to say that we'll end up at 1 percent in the longer term. But I think it's going to take a couple more years to get to that -- to be able to get to that potential forecast.

Joseph Greff: Got it. And we'll be also thinking this is sort of, I guess, this period of time over the last 12 months has been remarkable in what Marriott and other brand companies have done in taking out costs for the third-party hotel owners. Can you remind us what level of those costs might be permanent on behalf - I know from your P&L's perspective, it's a net wash. But for them, it obviously has helped them. Can you talk about what sticks and might what come back? And does that have any kind of longer-term strategic impact, whether it's marketing or branding or anything like that?

Leeny Oberg: Sure. So, every hotel is going to be a little bit different in how this works. And when we think about what we've been able to do on the reimbursed cost side, it has generally

been really impressive to be able to get to these levels of, call it, again, from a rough average perspective of 35 percent reductions as we're looking at 2021 compared to 2019.

And some of these do, obviously, fall into the category of permanent reductions where we have worked really hard to come up with more flexible labor scheduling, better ways of thinking about how we're doing certain parts of productivity in the hotels, different parts of - kind of looking at all kinds of disciplined costs, like IT and HR and back-office finance and all those sorts of things. And yes, so I do think there is a chunk of them that are permanent. However, as the hotels fill back up, Joe, there's obviously a number of these costs that have to go up as occupancy goes up. So, we'll have to see where the balance is.

What I think is great when we look at 2021 and you compare that to an expectation of revenues still being down meaningfully from 2019 for the full year to think we've been able to reduce costs to almost hold margins flat, I think, is really impressive. But to be able to kind of break out how much fixed is permanent, we'll need to get farther into the occupancy pickup to be able to tell you exactly how much stays with...

Joseph Greff: Right. Because I mean the stuff that...

Leeny Oberg: There's some permanent improvement.

Joseph Greff: Right. Because the -- of that sort of pass-through to you guys that maybe we gave short shrift to in the past, I mean that feeds the beast. That's the competitive advantage, right? That's where you see the scale of marketing in 2019 was like $6 billion of third-party marketing and customer loyalty support, which is a huge advantage.

Leeny Oberg: Yes. And what you know is that overwhelmingly 85 percent of what we charge to the hotels is based on revenue. So, it's going to fluctuate with revenue. So, some of that will just naturally move on.

Joseph Greff: And this might be a tough question to answer, but how important is this most recent round of federal stimulus to your owner community?

Leeny Oberg: So really helpful. There's the pointed help, which is on things like expansion and extension of the PPP loans and things like that. I see it as being kind of some identifiable help for them, which will help in the short term. The much more important component is the broader perspective of how this can help the macroeconomic recovery from this event.

And when you think about the fact that the U.S. economy has driven 77 percent -- roughly 70 percent by consumer spending, the reality of this stimulus package has the possibility to float all boats at a higher level, which is extraordinarily helpful for the demand levels at our hotels. For economic activity as businesses get going again and need to go out and people want to buy - they need to make more cars, make more washers and dryers, new programs and IT services for companies. All of that is incredibly helpful for jobs, for business activity, for business travel, for groups and for leisure. So, all of that fundamental macroeconomic activity is the part that I look to the most.

Joseph Greff: All right. Maybe you can switch a little bit to what you're seeing on the demand side looking at leisure, looking at group. And if you have sort of any comments on how the booking window has trended more recently?

Leeny Oberg: So here we are, almost exactly to the day, a year after basically the global pandemic shut down everything, particularly with a slam in the U.S. watched everything go down overnight. And I will say, it's really nice to see some momentum around the world, particularly where vaccines are really starting to roll out.

So, for example, Joe, when you see that January occupancy[2] globally was as we expected, right in line at 31 percent with December. We actually saw that in February, it popped up globally to 37 percent. And in March[3], we're actually seeing that positive trend continue above February's trend. So, from a RevPAR perspective, additionally, RevPAR -- the RevPAR decline was 5 points better in February than it was in January, which again, tended to be more in line with December.

And again, all -- while there may be a little bit easier comps in February to February of 2020, you can still see the same kinds of improvement when you compare it to 2019 levels. And one of the best parts is that in the U.S., it's some of the most dramatic. So again, as you compare RevPAR in February in the U.S. compared to 2019's February with comp sets in both of those, you see a 500 basis point improvement in RevPAR, and that kind of all points to nice, strong resilience of demand as things start to open up.

Around the world. Obviously, it varies. Mainland China, meaningfully ahead of the rest of the world. We saw -- kind of during the Chinese New Year, we saw Hainan pick up as the government opened up - kind of suggested that it was fine for domestic travel. We saw occupancy go from 39 percent to 79 percent in a week in Hainan.

And then kind of everywhere you go. So, in Asia Pacific, outside of China, you're also seeing certain markets like Australia, Korea, Japan, India, see some pockets of really nice improvement. And even in Europe, where we have 35 percent of our hotels still closed, we still, in February, saw 3 percentage points pick-up in occupancy.

So, I think all of this does kind of give you some comfort about the resilience in lodging demand and interest in travel as things recover. The different segments, no surprise. Leisure's first, leisure's strongest with drive-to. I think a little bit about from a macroeconomic sense in the U.S., you definitely saw unemployment rates jump the most for the lower end of the wage scales and unemployment only went up. I think it was like 200 basis points for people with a college degree. So that pent-up demand for leisure spend and travel, I think we really are

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[2] Transcript has been corrected to occupancy rather than RevPAR, as stated.

[3] Transcript has been corrected to March rather than February, as stated.

seeing in the leisure part of our markets, which is great. And again, I can go into the three segments, depending on kind of what you would find most helpful to you.

Joseph Greff: So maybe we can talk about group. I know group is sort of a lagging demand indicator, but it's something to pay attention to, particularly, I guess, maybe from a perspective of sort of attrition and rebooking. But your group revenue pace or position is in pretty good shape for the back of this year and certainly for 2022 on both volumes and price, all things considered.

When we think about a typical year - I don't even know what a typical year is in lodging anymore - but when we think of a typical year, how much of an annual group's business is in the quarter for the quarter or in the year for the year in terms of that might be the highest rated or the highest margin business? And so if that is more difficult to get in 2022 for the reason that nothing really has moved out of 2022 and, therefore, the available space might be limited, then how do you think about those things given the lead time associated with group?

Leeny Oberg: So, let's first go back to the Great Recession. Because I think it's worth mentioning that I do think we've got a bit of a different group behavior pattern than you had then. One of the things that was really happening back in the Great Recession was severe concerns about the health of the economy. And so, group bookings that were kind of being done for the out years suffered. And so, there was more rate pressure when you think about that.

First of all, we typically come into a year with 75 percent of our group already on the books. And as you know, in this pandemic, what you've seen is people canceling it, canceling close-in group, group that maybe in the next six months because they were concerned, their folks couldn’t travel and feel safe traveling. But they weren't canceling in out years. And many of those bookings were done in 2018 and 2019, which, as you remember, was a pretty strong time for the sense of future occupancy. And so, group rates were pretty good.

So, I don't think you're looking at 2022, 2023 and 2024 as seeing that we're kind of already stuck with, if you will, really low-rated business. And we are starting to see -- I noticed the other day, we had one sellout in August of 2021 for a very large one of our group houses by a company who, frankly, is trying to get in there and get something done. And that, obviously, is great to see.

When I think about the rates, I think we've talked about this before that the average daily rate that we've got on the books for 2022 is actually up. It's actually up single digits. While the group that we've got on the books for this year, the ADR is down, but still only down 5 percent -- under 5 percent. So I think that you've got the possibility with hopefully a fairly steep curve in the resilience of demand to really see that continue to help cause a faster recovery in rate overall than you saw back in the Great Recession.

Joseph Greff: Got it. Maybe we can talk about balance sheet, net leverage and capital return. Can you remind us longer term what you're targeting from a balance sheet perspective before you can reinstate a capital allocation program, including a dividend and buyback? And actually,

how does that manifest itself? If you're run rating, if you're in the fourth quarter, you multiply fourth quarter adjusted EBITDAR by 4 and you compare that to your adjusted net leverage -- lease-adjusted net leverage and you're kind of there, does that mean we should be assuming it's right around the corner? But I'll let you address that, holistically.

Leeny Oberg: Yes. So, this gets back to what we were talking about in the last question, and this is all about the pace of the return. As we've talked about, if you say, RevPAR moves one point differently than you expect for a full year, that ends up being roughly $40 million compared to 2019 -- and comparing to 2019. If you compare it to 2020, it's obviously a lot numbers, so it's a lot less. So. it's a solid $40 million in fees and then whatever it is on owned lease, and you're not really looking at a difference from a corporate expense standpoint. So, it's very strong flow-through for EBITDA.

And that is the game for us in leverage right now is that we're doing very well in terms of kind of managing our cash and, hopefully, really seeing continued ability to move to a better, better position on our cash flow. And so really, when you look at a leverage ratio, it's overwhelmingly about getting that EBITDA back. And in that regard, it's going to be all around the pace of that return of demand and RevPAR.

So, when you think about our philosophy, we really do want to be investment grade. That for us is a leverage ratio kind of in the 3 to 3.5x, and we've got a ways to get back there. And it all depends on how you determine your pace of the return of demand to get there. We'll obviously continue to be super disciplined about investment and our use of cash, and we're tracking it as carefully as you might imagine. But it really -- we're really confident we can get there. It's really all about the resilience of demand.

And then when you think about then returning capital, I think, Joe, you should expect a similar sort of pattern as we had before, which is a modest dividend -- modest cash dividend with the flexibility that then share repurchase provides over and above that to either invest in the business or to return it to shareholders.

Joseph Greff: And the thinking today, which I think I kind of maybe know the answer, but the thinking today behind maintaining a minimum level of investment-grade rating, that rationale today versus year's past, can you explain? I mean part of it was giving you access to cheap financing and serving as a backstop to development. But can you sort of explain that today?

Leeny Oberg: Yes. Sure.

Joseph Greff: I'd say the availability of capital and the terms in the cost of that capital, whether you're investment grade or not is, I would imagine, indistinguishable.

Leeny Oberg: So, we really do like the flexibility of the investment-grade debt rating. In terms of, as you know, we're able to raise capital in the bond market, really with next to no covenants, very straightforward, very easy, unsecured general corporate credit. And frankly, we've been able to kind of manage floating rate and fixed rate debt in a way that has kind of

provided a good hedge to upturns and downturns in the economy with the use of things like commercial paper.

Now clearly, the pandemic - I think the reality is the pandemic has demonstrated that the Great Recession's dramatic 25 percent can easily be eclipsed and something can be far worse than that. I do expect we probably will not use as much commercial paper in the future as we did before. But I still think the flexibility and the nimbleness that the investment-grade credit provides us for making moves when we want to, either to invest or on the financing side, that we still think in the long term, in a cyclical business like ours, gives us an advantage in our overall capital structure.

Joseph Greff: I think stronger capital structure, better balance sheet equates to a better equity value valuation multiple. So, I agree on that.

Leeny Oberg: I mean we have long-term contracts, right? So long-term asset business, long-term contracts, fee-based business, and I think the balance of that with our balance sheet is really good.

Joseph Greff: Great. Well, with that, I see we're at our end of a lot of time at 10:50. So thank you so much as always, Leeny. I appreciate the conversation. This was fun.

Leeny Oberg: Yes. Take care. Bye-bye.

Joseph Greff: Bye-bye.

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pandemic, including limiting or banning travel and/or in-person gatherings or imposing occupancy or other restrictions on lodging or other facilities; the impact of the pandemic and actions taken in response to the pandemic on global and regional economies, travel, and economic activity, including the duration and magnitude of its impact on unemployment rates and consumer discretionary spending; the ability of our owners and franchisees to successfully navigate the impacts of COVID-19; the pace of recovery when the pandemic subsides or effective treatments or vaccines become widely available; general economic uncertainty in key global markets and a worsening of global economic conditions or low levels of economic growth; the effects of steps we and our property owners and franchisees have taken and may continue to take to reduce operating costs and/or enhance certain health and cleanliness protocols at our hotels; the impacts of our employee furloughs and reduced work week schedules, our voluntary transition program and our other restructuring activities; competitive conditions in the lodging industry; relationships with customers and property owners; the availability of capital to finance hotel growth and refurbishment; the extent to which we experience adverse effects from data security incidents; and changes in tax laws in countries in which we earn significant income. Any of these factors could cause actual results to differ materially from the expectations we express or imply in this document.