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Wyndham Hotels & Resorts, Inc. (WH)

Q2 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the Wyndham Hotels & Resorts Second Quarter 2019 Earnings Conference Call. At this time, all participants have been placed on a listen-only mode and the floor will be open for your questions following the presentation. [Operator Instructions]

I would now like to turn the call over to Matt Capuzzi, Vice President of Investor Relations. Please go ahead.

Matt Capuzzi

Vice President-Investor Relations, Wyndham Hotels & Resorts, Inc.

Thanks, Keith. Good morning and thank you for joining us. With me today are Geoff Ballotti, our CEO; and David Wyshner, our CFO.

Before we get started, I want to remind you that our remarks today will contain forward-looking statements. These statements are subject to risk factors that may cause our actual results to differ materially from those expressed or implied. These risk factors are discussed in detail in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission and any subsequent reports filed with the SEC.

We will also be referring to a number of non-GAAP measures. Corresponding GAAP measures and a reconciliation of non-GAAP measures to GAAP metrics are provided in our earnings release, which is available on our Investor Relations website at investor.wyndhamhotels.com. In addition, we will provide supplemental information on our website after the call.

With that, I will turn the call over to Geoff.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

Thanks, Matt. Good morning and thanks, everyone, for joining us today. We're very excited to report our second quarter results with growth across all of our key metrics. We had our fifth consecutive quarter of positive net rooms growth in the United States. We grew our international net rooms by 7%, RevPAR increased both in the U.S. and globally, and our adjusted EBITDA grew 27%.

This morning, David and I would like to highlight key accomplishments in the quarter and provide an update on some of our more important growth opportunities. Starting with our goal to drive quality net rooms growth. We ended the second quarter with 817,000 rooms in our system. This was an increase of 3% since last June, including a 1% year-over-year net room growth in the United States.

Excluding 2018 acquisitions and divestitures, we have gone four for four so far this year by, one, increasing domestic room additions; two, increasing international room additions; three, decreasing domestic room terminations; and four, decreasing international room terminations.

We opened over 7,500 domestic rooms in Q2, an increase of 11% versus last year's second quarter, including over 1,300 La Quinta rooms from 14 La Quinta Del Sol prototypes across nine different states. Our retention rate in the United States has improved to 96% over the past 12 months, as we brought second quarter terminations down by 8% year-over-year. And importantly, we're delivering this rooms growth, while continuing to strengthen the quality of all of our brands with overall guest satisfaction and social media reviews scores up across the entirety of our system.

And according to the most recent J.D. Power Guest Satisfaction Survey released yesterday, our brands continue to top the charts. Microtel by Wyndham finished number one in the economy segment for the 16th time in the past 18 years and Wingate by Wyndham again finished number one in the midscale segment for its fifth consecutive year.

Internationally, we grew our system by over 20,000 rooms, or by 7% year-over-year. Our fastest growing region was again Southeast Asia, which grew by 22%. Latin America grew by 7%. And in China, where we are the largest international hotel franchiser and where we expect to open around 500 hotels over the next three years, we grew our direct franchise system by 10%. Our international retention rate has improved to 95% over the last 12 months.

Our global pipeline increased 10% year-over-year, or 4% sequentially to 188,000 rooms, principally reflecting 7% growth in domestic new construction and 21% growth in international new construction. Our strong second quarter results highlight that Wyndham is very well positioned to serve the needs of the select service hotel developers around the world.

We also achieved some significant milestones this quarter related to the La Quinta integration. We were very pleased to announce in April that we completed the migration of La Quinta, off of its legacy technology and onto Wyndham's distribution platform. The brand is now fully operational on our cloud-based reservation, property management, digital, loyalty, reporting and call center platforms. La Quinta franchisees are now benefiting from a fully integrated credit card interface and increased direct contribution from our award-winning Wyndham Rewards loyalty program.

The systems are working well and we were able to prove the value and the stability of this technology in the very first week after the cutover when a third-party service provider suffered a major outage and we were able to reroute reservation calls that La Quinta and its legacy platform could not have previously handled. We faced a very tough comp at La Quinta this past quarter. Last year, second quarter RevPAR was up 6%. This year we gave that back. La Quinta RevPAR was down 5%. La Quinta's geographic mix, particularly its concentration in hurricane-impacted and energy markets helped us last year, but hurt us this year.

Over the last year, La Quinta's RevPAR growth has been in line with the mid-scale average and the brand continues to deliver a RevPAR index premium of 119% versus the STR midscale segment. In addition, La Quinta's system size increased another 1% sequentially and the brand now stands at over 90,000 rooms.

As David will address in his remarks, the integration is now substantially complete and we expect to be achieving our full run rate synergies in the next few weeks. We used the first half of this year to revisit elements of our business that are not contributing to earnings or to our strategic priorities. And as a result, we expect to exit two legacy hotel management arrangements that have been unprofitable for us, which David will also cover in a moment. While we continue to see hotel management opportunities both domestically and internationally in support of our core hotel franchising business, we're no longer seeking guarantee-type deals like these legacy arrangements we're planning to exit.

This morning, we'd like to discuss the work we're doing around our new construction prototypes and brands along with our strong international growth and expansion. Last quarter, we updated you on the launch of Microtel Moda, a new and innovative prototype for our award-winning Microtel by Wyndham brand that is valued engineered to reduce cost, both to build and operate, while emphasizing modern efficiency to maximize franchisees' return on investment. This new design is helping us to further elevate the economy experience for the everyday traveler and we've seen tremendous excitement and interest from developers with over a dozen new construction Moda prototypes secured in our pipeline since we launched it at the Hunter Hotel Investment Conference a few short months ago.

And more recently, our midscale new construction brand AmericInn by Wyndham received Brand Council approval for another new interior design prototype. As a result, we hired one of the industry's leading design firms to create a new FF&E scheme that complements AmericInn's modern contemporary exterior and helps move the brand forward, while maintaining the identity and the rich heritage of AmericInn. Owners are telling us they like it because it looks great and is more cost efficient to both build and to operate and it's beginning to draw significant interest with several of these new construction prototypes also now in our domestic pipeline.

And finally, La Quinta's dynamic new construction, Del Sol prototype continues to wow developers. We signed seven new construction Del Sols during the second quarter and the 14 new La Quintas that we opened in Q2 were the most openings in any quarter for the brand since 2016.

With these three new construction prototypes, Microtel in the economy segment, AmericInn in the midscale segment, and now La Quinta in the upper midscale segment, Wyndham has a tremendous value proposition to provide to hotel developers in each of our core chain scales.

Our franchise sales teams are ecstatic about these offerings and we're equally thrilled with the progress they have made selling them to developers in such a short amount of time. Moreover, we're also upgrading our new Hawthorn Suites extended-stay prototype, which will round out our new construction design portfolio on both a

standalone and dual-branded basis with three new construction [ph] Hawthorne (00:09:52) La Quinta dual-branded developments executed since we acquired the La Quinta brand.

We continue to see excellent opportunities to grow internationally. We have seen significant interest in La Quinta in both Latin America and in the Caribbean. And we recently signed a deal with a developer in the Caribbean for eight new La Quintas, with four scheduled to open in 2021. In our Europe, Middle East, Eurasia and Africa regions, we opened nearly two-and-a-half times as many rooms this quarter as compared to the same period last year. And we opened 50% more rooms in Latin America and 30% more rooms in China on a direct franchise basis.

The rapidly expanding population of the traveling middle-class in international markets represents a major growth opportunity for Wyndham over the next decade. And we continue to position our select service franchise brands to capitalize on this demand for value-driven quality lodging accommodations.

Onto the marketing front, our multimillion dollar, fully integrated by Wyndham umbrella advertising campaign has driven guests in record numbers to wyndhamhotels.com to learn more about our wide variety of brands and our hotels, along with our award-winning Wyndham Rewards loyalty program. The campaign has helped to deliver a lift in ad awareness, ad recall, search impression and it's built a foundation of positive awareness for all 20 of our brands, which ultimately drives consideration in bookings. In addition, we've launched a multimillion dollar comprehensive La Quinta by Wyndham advertising campaign that includes television, radio and digital ads that we plan to continue to run throughout the rest of 2019.

Wyndham Rewards member occupancy continues to grow and is now running at over 40% for our domestic economy portfolio. Importantly, La Quinta's share of occupancy in its first two full months in the program increased to 180 basis points compared to 2018, a clear indication of the benefit La Quinta properties are seeing from increased member engagement.

Wyndham Rewards has consistently been ranked among the top hotel loyalty programs in the industry and our teams are focused on retaining this best-in-class status for our owners and for our members. Since making the program even more rewarding this year, we've seen a healthy increase in free night redemptions in the 7,500-point category, where almost one-third of our system resides. Our teams are now focused on enhancements to our mobile app that will further enhance and streamline bookings, engage our guests during their stay and provide Wyndham Reward members with a more personalized seamless experience.

We're proud of what the program has achieved so far and we are confident that our enhancements will continue to make it even more rewarding for our franchisees and for our guests. And our Blue Thread marketing relationship with Wyndham Destinations continues to strengthen. Blue Thread sales grew 50% in 2018 and have grown 22% year-to-date through April. We have both benefited from this year's Blue Thread call transfer programs, the increased Wyndham Rewards points purchased for use as a sales incentive and the expansion of in-hotel guests marketing programs.

The incremental tour volume we helped generate is complementary to Wyndham Destinations' existing sales channels and produces 25% higher sales per guest, resulting in additional margin on every Blue Thread sale.

On the partnership front, we're enhancing the value we provide to guests through new relationships with businesses like DoorDash. Since launching, Wyndham Rewards partnership with DoorDash in May, orders have risen steadily and we're seeing significant weekly increases in the number of on-property guests taking advantage

of the zero dollar delivery fee. DoorDash deliveries are a natural tie-in to enhance the guest experience at our economy and midscale hotels, since most of our select service hotels don't have that F&B beyond breakfast.

Before handing the call off to David, it would be remiss not to mention our focus on culture and social responsibility, two elements that remain critical to our long-term success. From an ESG perspective we're developing a new hotel-specific green certification program that will be used to support our efforts to engage franchisees on improving their carbon, energy, and LED lighting usage footprints along with their water conservation and waste diversion efforts. Importantly, we are piloting a Go Green program to our over 77 million Wyndham Rewards members by offering reduced housekeeping and towel and linen service for multi-night stays in exchange for Wyndham Rewards points.

More importantly, our values-driven culture grounded in the strong foundation established by our former parent company Wyndham Worldwide is fueled by our continued focus on attracting, retaining, and engaging the very best and brightest people in our industry. Recently, more than 80% of our 16,000 team members completed the Gallup Employee Engagement survey and Gallup told us that Wyndham Hotels & Resorts surpassed top quartile levels of engagement, representing a strong baseline as a new company for us to grow and highlighting the strength of our team members' commitment to our long-term goals.

And with that, I'll now hand the call over to David, who will walk us through the financial highlights. David?

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

Thanks, Geoff, and good morning, everyone. Today I'll discuss our second quarter results as well as our La Quinta synergies, our balance sheet, capital allocation, and our 2019 outlook. My comments will be primarily focused on our adjusted metrics. You can find our complete results in our earnings release, including reconciliations of adjusted amounts to GAAP numbers.

We believe the adjusted figures we're providing are helpful in understanding how our business performed and how it will look on a go-forward basis. We anniversaried the acquisition of La Quinta and our spin-off in May. So, Q2 is the last quarter where year-over-year comparisons are being skewed by those events.

We grew our top line 23% in the second quarter to \$533 million, including \$98 million of incremental revenues from La Quinta. Adjusted EBITDA increased 27% to \$159 million in the second quarter, including \$30 million of incremental EBITDA from La Quinta without which our adjusted EBITDA growth would have been around 5% in constant currency. As we discussed on our last call, we elected to incur a higher proportion of our marketing spend in the first half of this year to support our new to support our new by Wyndham marketing campaign and our Wyndham Rewards loyalty program. This timing difference suppressed second quarter organic growth by 13 points.

As Geoff mentioned, we expect to exit two unprofitable hotel management arrangements that were initiated in 2012 and 2013. In connection with one arrangement that covers 22 U.S. hotels, our guarantee obligations have been exhausted. So, we expect this agreement to terminate, including our ability to recapture guaranteed payments we previously made. As a result, we recorded a non-cash impairment charge of \$45 million and a \$9 million contract termination charge in the second quarter, primarily related to the anticipated loss of the recapture opportunity.

In order to terminate the other arrangement, which covers eight U.S. hotel properties, we have signed a non-binding letter of intent to exit the arrangement by making payments representing a significant discount to our

remaining potential guarantee exposure, which is approximately \$70 million. As a result, we expect to incur a cash contract termination charge in the third quarter in order to sunset that arrangement.

With the termination of these two deals, our future annual maximum hotel management guarantee obligations will decline from \$26 million to \$5 million and we will no longer have any multi-property guarantee obligations. The planned terminations have no impact on our adjusted EBITDA this year, but we expect them to provide an EBITDA benefit of around \$8 million in 2020. That said, we expect to shrink our managed portfolio later this year as CorePoint executes on its property disposition strategy, as well as next year as a result of these planned terminations.

Turning to our operations, royalty and franchise fee revenues increased \$13 million, or 12% in the second quarter, largely due to having two additional months of La Quinta's results this year. License fees primarily from Wyndham Destinations were \$33 million compared to \$25 million during the second quarter of 2018. Our global RevPAR grew 5% in constant currency in the second quarter and increased a fraction of a point excluding acquisitions and divestitures, despite a headwind of about 80 basis points due to lapping the incremental hurricane-related demand that we had in the second quarter of 2018.

U.S. RevPAR grew 5% in the quarter and was also up a fraction of a point excluding 2018 acquisitions and divestitures, despite a hurricane headwind of about 150 basis points. The 2017 hurricanes will no longer significantly impact our driver comparisons as we move into the third quarter. Excluding acquisitions, divestitures and the hurricane effect, our U.S. RevPAR growth was driven primarily by higher occupancy. We saw the strongest results in our Howard Johnson, Microtel, Hawthorn and Wyndham brand brands and in the Mountain and Mid-Atlantic regions. Generally speaking, U.S. RevPAR growth was modestly softer in the second quarter than in the first, which we believe is consistent with broader macroeconomic and industry trends.

In our Hotel Franchising segment, revenues increased 15% year-over-year in the second quarter, including \$36 million of incremental revenues from La Quinta. Excluding the impact from 2018 acquisitions and divestitures, revenues increased 3% in constant currency. Our Hotel Franchising segment adjusted EBITDA grew 26% to \$162 million, including approximately \$24 million of incremental contribution from La Quinta. Excluding the impact from 2018 acquisitions and divestitures, adjusted EBITDA for that segment grew 9% in constant currency despite an 11-point impact from increased marketing expenses.

In our Hotel Management segment, revenues increased \$55 million compared to the prior year period, reflecting \$62 million of incremental revenues from La Quinta. Excluding the impact from the acquisition, revenues declined primarily due to lower cost reimbursement revenues, which have no impact on earnings. Our Hotel Management segment adjusted EBITDA increased \$8 million year-over-year, reflecting approximately \$6 million of incremental adjusted EBITDA from La Quinta.

With the migration of La Quinta's technology platform and loyalty program now behind us, we're in the final stage of the LQ integration. The principal remaining work being done is decommissioning legacy La Quinta reservation systems, completing some day two items associated with the systems migration and removing the temporary resources we had in place to assist with the transition. During the second quarter, our results included \$14 million of synergies from La Quinta, or a run rate of \$56 million annually, 80-plus percent of our target. As expected, we will reach full run rate La Quinta synergies of \$64 million to \$70 million a year during the third quarter.

On our balance sheet, at June 30, we had \$107 million of cash and our net debt balance – and our debt balance was approximately \$2.1 billion carrying in all-in weighted average interest rate of 4.8%. Our net leverage was 3.3

times the midpoint of our full year 2019 outlook for adjusted EBITDA in the lower half of our 3 to 4 times net leverage target.

Excluding specific cash outflow items, namely \$188 million of tax payments related to the La Quinta current acquisition and \$46 billion of transaction in separation-related expenses and insurance reimbursed capital expenditures, free cash flow in the first half of 2019 was \$72 million compared to \$100 million in 2018. The decline is primarily due to the timing of tax payments and higher interest expense, partially offset by the increase in adjusted EBITDA.

For the full year, we continue to expect our normalized free cash flow to approximate our adjusted net income as our business is inherently a cash business. We should also note that in addition to our free cash flow, we received \$40 million from Wyndham Destinations in Q2, as part of the excess net proceeds from Wyndham's 2018 sale of its European vacation rentals business. We believe these proceeds should largely offset the cash cost of exiting our unprofitable hotel management contracts.

We returned \$78 million to shareholders in this second quarter through \$50 million of share repurchases and \$28 million of common stock dividends. In our first four quarters as an independent company, we repurchased 4% of our outstanding shares in addition to paying a 2% dividend yield. Our capital allocation approach remains intact. We are focused on the organic growth of our business and we will deploy a portion of our free cash flow for development advances and similar opportunities in order to support that growth. We will also maintain a dividend that we intend to grow over time. Beyond that, we will allocate cash flow to execute opportunistic tuck-in acquisitions that are both strategic and accretive and to share repurchases.

Finally, we are reaffirming our 2019 full-year outlook for rooms growth. We have updated our outlook for organic RevPAR growth to approximately 1% to reflect recent trends. We have revised our forecast for revenues almost entirely due to lower cost reimbursement revenues that have no impact on earnings. We updated our outlook for adjusted EBITDA slightly to reflect a significant progress we have made in integrating La Quinta and favorable results at our owned hotel in Puerto Rico, as well as a modestly softer RevPAR environment than we had anticipated and we lowered our effective tax rate by a percentage point.

These changes result in a higher adjusted net income outlook than our previous forecast and we increased the midpoint of our adjusted EPS estimate by \$0.065 to reflect both the projected increase in our adjusted net income and our share repurchase activity in the second quarter. As a reminder, our adjusted EPS guidance excludes the impact of future share repurchases we expect to make this year. From a seasonality perspective, after generating approximately 26% of our expected full year 2019 EBITDA in the second quarter, we continue to expect to generate roughly 30% in the third quarter and the remainder in the fourth.

In conclusion, we continued our earnings and rooms growth momentum from the first quarter and we reached a significant milestone with the La Quinta integration nearing full run rate on cost synergies. We are adhering to a disciplined capital allocation framework to drive shareholder value. And with more than 9,000 hotels primarily in the economy, midscale and upper midscale segments, we have the advantage of being able to serve the majority of the needs of the majority of travelers in markets throughout the world. As a result, we remain confident and passionate about our business, our growth potential, and our ability to deliver on our 2019 forecast.

With that, I would like to turn the call back over to Geoff.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

As David said, we feel great about our momentum and our progress towards our 2019 goals. We're successfully executing on our business plan. We're expanding our strong market position and we're strengthening our industry-leading loyalty program. We continue to work to enhance the value what we're providing to our franchisees in terms of direct business and contributions. And we look forward to hosting them all at the largest gathering of hoteliers in the industry, the Wyndham Hotels & Resorts Global Conference, which is coming up in 61 short days from now in September.

And with that, David and I would be pleased to take your questions. Keith?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Thank you. And we'll take our first question from Joe Greff with JPMorgan. Please go ahead.

Joseph Greff

Analyst, JPMorgan Securities LLC

Q

Good morning, guys. I have two questions. One with the lodging equity valuation higher today than three months ago and six months ago, have you noticed any sellers of brand emerging trying to ascertain how broad or how deep external growth opportunities might be for WH? And then I have a second question.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Joe, we do continue to think there are opportunities out there. I don't know that the move in valuations has really changed things that much other than that if you look back six months ago at the very beginning of the year, coming off the really soft equity market conditions in November and December, that probably would have been a tough time to unlock a transaction. But I think we do see opportunities that are potentially out there, and we will continue to look at them over time. But I don't know that the change in valuations over the last few months has dramatically changed that landscape.

Joseph Greff

Analyst, JPMorgan Securities LLC

Q

Great. And then I think I probably know the answer to this, but obviously with the domestic RevPAR growth sort of in the 1% plus or minus range and decelerating from where it's been the last year or two. Has this or why hasn't this altered the newbuild enthusiasm of the development community? And that's all for me.

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Yeah. I think as we look at the opportunities that are out there to earn significant returns in economy, midscale and in upper midscale lodging really with the select service or limited service format that we provide, there are a lot of markets out there where ongoing development and/or conversion to our brands can make a lot of sense. And I think as Geoff walked through, the strategic decision and execution we made to have an important new prototype in the economy space, a revised room design for AmeriInn in the midscale space and in the really great La Quinta Del Sol prototype, which leads to building in the upper midscale space, we've got a strategic approach and a go-to-market set of prototypes that we're finding very attractive for developers who are being very thoughtful about what markets those make a lot of sense to be building in. So we're excited about the potential

that those prototypes have going forward as well as about the results we've been seeing for them so far this year, including as we roll out the Moda prototype for Microtel.

Joseph Greff

Analyst, JPMorgan Securities LLC

Thank you.

Q

Operator: Thank you. And we can take our next question from David Katz with Jefferies. Please go ahead.

David Katz

Analyst, Jefferies LLC

Hi. Good morning, everyone. I wanted to ask about unit growth and RevPAR related to La Quinta. And I know there was a time where you sort of broke those out specifically. But if there's anything you can – anything qualitative or quantitative you can give us about how those are doing. I know you did make some, David, in your comments, in your remarks, David, but anything else would be helpful?

Q

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

Yeah. We'll start RevPAR, Joe, and – I'm sorry, David. And we did say, as I said in my remarks, that RevPAR for the overall La Quinta brand was down 5% in the quarter versus 6% in the quarter last year, again some really tough comps. When you think about last year's hurricane, all of the workers that were flooding into those La Quinta hotels on the remediation work, last year Q2 was very strong. We've talked before in the past about RevPAR index for the La Quinta brand. It was at 119% for the quarter. And our job is to continue to grow that RevPAR going forward. And it's certainly over the last few weeks it's been trending in the right direction, as we introduce new rate and revenue management tools and revenue management services for the hotels.

A

On the net unit growth, we're thrilled, as we talked about. We're up 200 basis points year-on-year and we are up 80 basis points sequentially in La Quinta net units. Retention remains strong. We ran a 98.5% retention rate last year and we're running a 99% retention rate this year year-to-date. And our new construction sales team and certainly our architectural design and construction team has never been busier.

We opened 23 Del Sols so far since acquisition. We have 41 Del Sols under active construction and we've grown the brand now to over 90,000 rooms and up to 924 units – 924 hotels and just see tremendous growth opportunities, as we talked about, not only domestically, but also now are beginning to see in our Latin America region actual executions and beginning to see great interest in in markets in Europe and also surprisingly, as we've talked, about in Asia.

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

And I would just add to that that, as Geoff mentioned, we faced a really tough comp at La Quinta this past quarter, because RevPAR have been up 6% in the prior year second quarter. The comp, as we move into the back half of the year for La Quinta, is not nearly that difficult kind of ranging the flat to up 3% range for the back half of the year. So it's sort of an anomalous comp that we were facing versus second quarter of 2018.

A

David Katz

Analyst, Jefferies LLC

Q

If I can be just a bit more direct about it and not have it count as my follow-up question. I just want to make sure within that La Quinta, the sort of – the go live or the reservation system, specifically around the CorePoint assets where there's been discussion about RevPAR being a little choppy since that's occurred. I just want to sort of get your perspective on whether some of that choppiness is sort of done and how much of that we're seeing in here?

And then just my last follow-up was really about the return of capital and how we might think about that continuing to accelerate over time, because it does appear that you're returning nearly equivalent amounts to your peers, but I think at the end of the day that's kind of where the rubber meets the road for us? And that's it for me. Thank you.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Thanks, David. I will take the first on the La Quinta technology integration and let David address the second part of that question, and we won't count it as a follow-up.

David Katz

Analyst, Jefferies LLC

Q

Thank you.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

The technology migration we view as a considerable tremendous success. Recall that this was 10 months in the making of just intensive groundwork. We were 10 months ago beginning to take out property management systems and replace legacy PMSs with state-of-the-art property management systems. Our La Quinta franchise service directors, our incredible DFOs, our HTCS teams were out there for 10 months training the GMs, the front office managers and the revenue managers. And on April 3, we achieved what a lot of people thought was had never been achieved before, the largest one day migration of any technology platform in the industry.

And the system has been operating exactly as we expected. It has been more stable, it has been more safe, it has been more secured. There was considerable change – dramatic change for revenue managers with more rates and more distribution channels. And so, to your comment on whether it was choppy, yeah, we do think that those first two weeks were a bit weaker. But the impact on the second quarter, we believe, was limited. And we believe that that second quarter RevPAR was, just as David said, due to a very tough comp of being up 6%, which then flattened by year-end in Q1. And then David, you could take the second part.

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Yes. On the capital allocation and deployment front, absent finding any significant acquisitions, we continue to expect to return a significant amount of capital to shareholders. It's been a big and important part of our history as an organization and we expect to continue that. I think the last 12 months' numbers that I highlighted in my remarks are helpful as we think about it going forward. The fact that we were returning about 2% to shareholders in the form of our dividend yield and about 4% over the course of the year through share repurchases, that's pointed to our ability to be returning essentially close to 6% to shareholders over a 12-month period, even while we're in the process of integrating La Quinta.

David Katz

Analyst, Jefferies LLC

Q

Thank you.

Operator: We'll take our next question from Patrick Scholes with SunTrust. Please go ahead.

Patrick Scholes

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Good morning, Geoff and David. I had several questions here. It looks like on your retention rate, you at 96% certainly hit that target sooner than we were expecting. Is there still opportunity to improve that retention rate from here?

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Yeah, absolutely, Patrick. Good morning. Our retention rate has been going up as our attrition rate has been coming down and there is opportunity. Our ability, as we said to you a few years ago, our desire to move from 93% to 94% last year, we achieved it. We said we wanted to get to 95% this year. And being able to reduce our attrition in Q1 domestically and move it from 95% to 96% was huge for us. And internationally, to move it to 95% was also considerable. Our goal over time, as we've said, is to move it up another point and we'll continue to do that by continuing to focus on the brands that need work. But so many of our brands, so many of our economy brands now are running retention rates well above 95%.

When we're looking at the Days Inn brand running north of 95%, or Super 8 running 97%, we're beginning to feel that the work we've been focused on, that our teams have been focused on is really starting to resonate. We have brands like Microtel that continue to run at 99% and we believe we're running in the economy segments now well ahead of the economy averages domestically and we need to continue to work on that as we continue to bring in great new brands like AmericInn and La Quinta, which are also running 97%, 98%, 99%. So our goal is still over time to move from 95% to 96% and if we could do that, [ph] David (sic) [Patrick] (00:40:16), that means another point or so of growth.

Patrick Scholes

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Okay. Thank you for that color. Then my follow-up question. Yesterday, Hilton had talked about observing weakness in China, specifically in the leisure customer. Is that something you folks are also seeing as well?

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

We have not. We had no indication of any impact or slowdown on either our franchised or managed business in China in Q2, Patrick. In fact, we look at it on a constant currency basis. Our same-store view saw our RevPAR actually improve a little bit by, I think it was 50 basis points of growth in the Q. And again, no slowdown either on demand, as in our comments we talked about, very strong demand and growth for our direct franchise brands as we said, with a 10% net room growth.

Our masters saw good solid room growth at 8% and nearly all of our 20% pipeline growth in China is direct business now, which absolutely thrills us. We can't say enough about the job of the team over there in China. We've grown from a dozen to over 100 franchise sales, marketing, operation professionals and they are just knocking it out of the park with our historical brands. Our Wyndham brands are growing, our Ramada brands are growing, our Ramada Encore brands are growing.

And we have the ability as we've talked about to introduce new brands into that market and the job that that team is doing introducing the Wingate by Wyndham brand into China, the Microtel by Wyndham brand into China and the Garden, all have new executions and new openings and they're some of the best representation of product that we have in those brands globally. And also finally, we've talked a lot about Days Inn. Our team is killing it right now in terms of getting those franchisees to sign direct franchise agreements with Wyndham now that we've taken back control of the Days Inn master.

Patrick Scholes

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Okay. Thank you again for that thorough explanation.

Operator: Thank you. Our next question is from Shaun Kelley with Bank of America. Please go ahead.

Dany Asad

Analyst, Bank of America Merrill Lynch

Q

Hey, good morning, guys. This is actually Dany on for Shaun. Maybe just a follow-up first on the last question. Maybe can you help parse out the change in RevPAR guidance for us? So if we're thinking about it by region, could you give some color on China, maybe what are the biggest moving pieces here that are bringing us the RevPAR from 1% to 3% to that 1% globally?

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Sure. In terms of the change that we're seeing versus the prior guidance, the biggest issue has been in the U.S. That's where we're seeing softness. The international regions have been performing well. So that's, I would say, not a driver of it. And that's true pretty much across the range of international regions. The softness again is driven by the U.S. The other piece that's interesting and worth noting is that we actually expect international RevPAR in constant currency to be up a bit more than 1% and we expect U.S. RevPAR probably to be up a little bit more as we look at our point estimates. And the reason we end up at approximately 1% overall is that the mix shift where we have faster international growth but lower average RevPAR, that faster growth is reducing our global RevPAR growth by about a half a point compared to where the – where it would be if on an equal basis or on a same growth basis.

Dany Asad

Analyst, Bank of America Merrill Lynch

Q

Got it. Okay, and thank you very much. And then the follow-up, I guess, is, so we understand the nature and the rationale behind the management contract terminations and I think it makes a lot of sense. But can you just remind us of the contract structure you have in place with CorePoint and whether that's different from the rest of your management agreement? So if I'm – just to be a little bit more specific, so like under what circumstances would those contracts be impacted by either change of control and then how do we think about them magnitude for your – to your overall management segment?

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Dany, great question. I think the starting point is that the CorePoint management agreements are percentage of revenue based and they don't have a guarantee or incentive components associated with them. So, they are not the sort of guarantee-heavy or guarantee-laden deals that we're looking to exit. They operate more like a

franchise agreement where the management fees that we generate are a percentage of revenues. We like those sorts of structures. I think as we think about the management business going forward, we love percentage of revenue. We will be willing to do some things that have incentives associated with them, but we don't want to get involved with guarantees going forward.

The other issue to think about with respect to the CorePoint relationship is that they're looking to sell some of the properties in the system. If they do so, we fully expect to hold on to the franchise agreements, and we have very strong protections to do that. The new owners may very well look to take on some of the management responsibilities. We get a payment if that happens on the vast majority [ph] of their hotels. That was part of the structure we negotiated upfront, and we're fine with that. We're supporting and helping CorePoint as they work through the process of divesting of some of their assets. And so, we're fine with that. But we do expect that that will shrink our managed portfolio a bit over the next six months or so. But again that was all part of the transaction that was originally negotiated and we do get a termination payment if any of those managed – if most of those – on most of those hotels, if the management agreements go away.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

But having said that, we are working with both owners of these guaranteed deals on retention. And our general managers and our teams are consistently recognized by those ownership groups as among the best performers to the extent that we could retain them on either a franchise basis or post-sale unencumbered basis. If that's possible, that's what we're looking to do, as we have just a demonstrated ability to continue to grow without guarantees going forward.

Dany Asad

Analyst, Bank of America Merrill Lynch

Q

Understood. Okay. Thank you very much. Thanks.

Operator: We'll take our next question from Ian Zaffino with Oppenheimer. Please go ahead.

Mark Zhang

Analyst, Oppenheimer & Co., Inc.

Q

Hey, good morning, guys. This is actually Mark on for Ian. Thanks for taking our questions. So, most of our questions have been answered, but just can you give a quick update on your U.S. rooms deletion initiatives? How much is lost and how much should we expect for the balance of the year? Thanks.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Sure. Yeah. As I said earlier, we're continuing to see improvement. We had a 10%, 90 basis point improvement on our term rate domestically and we're looking to continue to move that as we have from 93% to 94% to 95% and we'd love to see it stabilize at 96%. And as I said, as the work has been essentially completed with so many of those brands that I mentioned, Days, Super, Micro are now all at 96% or above. We're feeling really good about being able to get there over time.

Mark Zhang

Analyst, Oppenheimer & Co., Inc.

Q

Okay, terrific. And then just a quick one on the capital allocation front, specifically on M&A. Is there anything in the pipeline right now that you guys are interested in and then where does your interest lie with the current state of the market? Thanks.

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Sure. I think we will continue to look at opportunities that are out there and as they come along, it's not appropriate for us to comment on at any time on whether there's something in process. But I think the opportunity exist for us to continue to look at transactions both in the U.S. and internationally, most likely primarily focused on the select service space, whether it's economy, midscale or upper midscale. And the reason for that, we talked about a few conference calls ago, is that when you look at AmericInn or La Quinta or other brands that are out there, our ability to generate substantially more earnings from a brand that's currently independently owned or separately owned, then it generates on its own, really makes a further consolidation, a sensible thing for us to pursue.

It's part of our history. We've averaged a brand acquisition about every 18 months or so over the last 20 or 30 years. And it's really the ability to generate significant synergies from a brand acquisition that is a big driver of why over time we look to pursue that. But again, as we mentioned on the last call, if we don't end up doing a transaction this year, that's okay, too.

Mark Zhang

Analyst, Oppenheimer & Co., Inc.

Q

Okay. Terrific. Thanks, guys.

Operator: We'll take our next question from Anthony Powell with Barclays. Please go ahead.

Anthony F. Powell

Analyst, Barclays Capital, Inc.

Q

Hi. Hello. Good morning, everyone. Just a question on the domestic new construction development pipeline, which had some nice growth. We've heard more from some of the larger competitors that they're looking to grow their presence in the midscale and upper midscale chain scales. What advantage do you see Wyndham having relative to some of these larger brands in terms of the ability for franchisees to get financing and just overall value proposition relative to say some of the larger peers?

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Sure. Thanks, Tony. Yeah. As David was just saying, I mean, the advantages are in the design of our new prototypes. So we could not be more thrilled with what's gone on so far in Q1 and Q2. For us, to see a 7% new construction increase in our domestic pipeline is something that hasn't happened in a long, long time as our international new construction pipeline continues to click along. And we really point to, as David just said, that that award winning new construction prototype that our franchise sales teams are out there selling, whether it's the Microtel Moda that we launched at Hunter that has had so many La Quinta owners begin to look at it and think that this is a brand that we want to build, a brand with a proven ability to drive unbelievable RevPAR index. It's really a category killer from a RevPAR index in the economy space that could be built at \$60,000, \$65,000 a key is what we think differentiates us. And as we pick up that, that pipeline continue to grow it and continue to convert more from our pipeline that's new construction where we're seeing great progress and momentum on a forward-looking basis.

Anthony F. Powell

Analyst, Barclays Capital, Inc.

Q

And I should probably know this, but in terms of from signing to delivery, what's the average I guess time for a domestic new construction hotel in your system?

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Sure. It's generally 12 months of permitting, another 12 months of construction and anywhere between 24 to 36 months before it opens. We ask that question of Krishna Paliwal, our Head of Architecture, Design & Construction who joined us from La Quinta the other day and he thinks the average is right around 32 months from signing to opening.

Anthony F. Powell

Analyst, Barclays Capital, Inc.

Q

Got it. And one more...

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

And he would know.

Anthony F. Powell

Analyst, Barclays Capital, Inc.

Q

Got it. And a question on U.S. RevPAR, it seems like you expect a slight acceleration. You're at, I guess, roughly 1% organic year-to-date, you expect slightly over 1%. Is that just due to the easier comps from the hurricanes or is there something else going on, on that you expect a slight recovery on the RevPAR?

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

No. I think David Wyshner's explanation was spot on. I mean, we're still seeing strong consumer confidence out there domestically. We had a solid July 4th industry-wide. We're seeing strong weekend occupancy, especially in the economy segment. And the real bigger issue that David touched on was some slowing in average rate most notably in the midscale brands and most notably midweek.

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

And you're right, the hurricanes impacts impacted the first half in a way they don't in the second. So if you adjust the first half numbers for that, there's more consistency between the first half and the second half.

Anthony F. Powell

Analyst, Barclays Capital, Inc.

Q

Okay. Great. That's it for me. Thank you.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Thanks.

Operator: And we'll take our next question from Dan Wasiolek with Morningstar. Please go ahead.

Dan Wasiolek

Analyst, Morningstar, Inc.

Q

Good morning, guys. Yes. So with your [indiscernible] (00:54:30) development metrics on an improving trend, just wanted to ask about the U.S. royalty rates. It seems in the footnotes that it was noted that those rates have declined versus prior periods when you exclude acquisitions and divestitures. Just wondering if that's mix or timing related or what's behind that?

David B. Wyshner

Chief Financial Officer, Wyndham Hotels & Resorts, Inc.

A

Sure. What we've seen over the last year is a little bit faster growth in Trademark and our soft branding, which reduces our average royalty rate a little bit. I think as we look over time, we generally expect royalty rate to grow in – to remain fairly consistent. But certainly, over the last year or so, the significant growth that we've been able to achieve in The Trademark brand, the rapid ramp-up of that brand to more than 100 hotels has negatively impacted our royalty rate a little bit. But generally, over time our push is going to be to continue to move royalty rates up, particularly in our international region where the growth in indirect franchising will be helpful to our ability to do that.

Dan Wasiolek

Analyst, Morningstar, Inc.

Q

Okay. Great. And then just one final question here, on the loyalty room-night mix, I'm wondering if you – you've mentioned I think that it's over 40%. How did that compare with the prior-year period? And I might have missed this, but what number of loyalty numbers are you guys currently at? Thank you.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

A

Sure. Moving backwards in terms of numbers, we saw an 11% organic growth in our Wyndham Rewards members, roughly 6 million of members to 77 million is our current count. Your question before that, share of occupancy, we are up 300 basis points or are running 300 basis points up year-to-date. And our comment that I think excites the teams that are listening into this more than anything is to see the economy Wyndham Rewards share of occupancy up now over 40% when it was half of that a few years ago.

The thing that brands like Super 8 are running 42% share of occupancy now, when that number was in the teens before this program was re-launched, gives us – just thrills us. To think La Quinta running 48%, 180 basis points ahead of where it was last year, gives us great belief that brands like La Quinta could be performing as brands like Hawthorn Suites and AmericInn now at over 50%. But we're seeing – it's our one of our fastest growing channels. And our job now is to engage more of our elite members, who are growing at three times the rate that the base is growing to drive that share of occupancy even higher.

Dan Wasiolek

Analyst, Morningstar, Inc.

Q

Very good. Thank you.

Operator: Ladies and gentlemen, this will conclude today's Q&A session. I'd like to turn the floor back to Geoff Ballotti for closing remarks.

Geoffrey A. Ballotti

President, Chief Executive Officer & Director, Wyndham Hotels & Resorts, Inc.

Thanks, Keith. And thanks everyone for your time this morning. We appreciate your attention and interest in Wyndham Hotels & Resorts and we look forward to talking to you soon. But before we go, we'd like to remind you all to please remember to tune into the 15th Wyndham Championship from August 1 through August 4, airing on the Golf Channel and CBS. Enjoy the rest of your summer.

Operator: Thank you. This will conclude today's Wyndham Hotels & Resorts second quarter 2019 earnings conference call. Please disconnect at this time and have a wonderful day.

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