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Hilton Worldwide Holdings, Inc. (HLT)

Q4 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the Hilton Fourth Quarter 2021 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] Please note, this event is being recorded.

I would now like to turn the conference over to Jill Slattery, Senior Vice President, Investor Relations and Corporate Development. You may begin.

Jill Slattery

Senior Vice President-Investor Relations and Corporate Development, Hilton Worldwide Holdings, Inc.

Thank you, Chad. Welcome to Hilton's fourth quarter and full year 2021 earnings call. Before we begin, we would like to remind you that our discussions this morning will include forward-looking statements. Actual results could differ materially from those indicated in forward-looking statements, and forward-looking statements made today speak only to expectations as of today. We undertake no obligation to update or revise these statements.

For a discussion of some of the factors that could cause actual results to differ, please see the Risk Factors section of our most recently filed Form 10-K. In addition, we will refer to certain non-GAAP financial measures on this call. You can find reconciliations of non-GAAP to GAAP financial measures discussed in today's call in our earnings press release and on our website at ir.hilton.com.

This morning, Chris Nassetta, our President and Chief Executive Officer, will provide an overview of the current operating environment. Kevin Jacobs, our Chief Financial Officer and President, Global Development, will then review our fourth quarter and full year results. Following their remarks, we will be happy to take your questions.

With that, I'm pleased to turn the call over to Chris.

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Thank you, Jill. Good morning, everyone, and thanks for joining us today. As our results show, we made significant progress in our recovery throughout 2021. We saw a meaningful increase in demand for travel and tourism, and our team members around the world were there to welcome guests with our signature hospitality as they look to reconnect and create new memories.

We continued to demonstrate our resiliency by remaining laser-focused on providing reliable and friendly service to our guest and by launching several new industry-leading offerings to provide them even more choice and control.

We also continued to expand our global footprint adding even more exciting destinations to our portfolio and achieving a record year of room openings. All of this, together with our resilient business model, translated into solid results.

For the full year, we grew RevPAR 60% and adjusted EBITDA 93%. Both RevPAR and adjusted EBITDA were approximately 30% below 2019 peak levels. More importantly, our margins were 500 basis points above 2019 peak levels, reaching roughly 66% for the full year.

While some costs will come back in as we continue to recover, we remain extremely focused on cost discipline. Given our asset-light business model and the actions we took during the pandemic to further streamline our operations, we expect permanent margin improvement versus prior peak levels in the range of 400 basis points to 600 basis points over the next few years.

Turning to results for the quarter. RevPAR increased 104% year-over-year and adjusted EBITDA was up 151%. RevPAR was roughly 87% of 2019 levels with ADR nearly back to prior peaks. Compared to 2019, occupancy improved versus the third quarter with higher demand across all segments.

Strong leisure over the holiday season drove US RevPAR to more than 98% of 2019 levels for December. Business travel also improved sequentially versus the third quarter, with solid demand in October and November before the Omicron variant weighed on recovery in December.

For the quarter, business transient room nights were approximately 80% of 2019 levels. Group RevPAR improved 11 percentage points over the third quarter to roughly 70% of 2019 levels. Performance was largely driven by strong social business, while recovery in company meetings and larger groups continued to lag.

As we kicked off the New Year, seasonally softer leisure demand, coupled with incremental COVID impacts due to the Omicron variant, tempered the positive momentum we saw through much of the fourth quarter. For January, system-wide RevPAR was approximately 75% of 2019 levels.

Despite some near-term choppiness, we remain optimistic about accelerated recovery across all segments throughout 2022. We anticipate strong leisure trends to continue again this year, driven by pent-up demand and nearly \$2.5 trillion of excess consumer savings. Our revenue position for President's weekend is 7 percentage points ahead of 2019 levels. And our position for weekends generally is up significantly for the year, both indicating continued strength in leisure travel.

Similarly, we expect growth in GDP and nonresidential fixed investment, coupled with more flexible travel policies across large corporate customers to fuel increasing business transient trends. As a positive indication of business transient recovery, at the beginning of January, midweek US transient bookings for all future periods were down 13% from 2019 levels and improved to just down 4% by the end of the month. Additionally, STR projects US business transient demand will return to 92% of pre-pandemic levels in 2022.

On the group side, our position for the year is to remain steady as Omicron-related disruption was largely contained to the first quarter of 2022 with most events rescheduled for later in the year. We continue to expect meaningful acceleration in group business in the back half of the year as underlying group demand remains strong. Compared to 2019, our tentative booking revenue was up more than 25%. Additionally, meeting planners are increasingly more optimistic with forward bookings trending up week over week since early January.

Overall, we remain very confident in the broader recovery and our ability to keep driving value on top of that. This should allow us to generate strong free cash flow growth and our expectation is to reinstate our quarterly dividend and begin buying back stock in the second quarter.

Turning to development. We opened more than a hotel a day in 2021, totaling 414 properties and a record 67,000 rooms. Conversions represented roughly 20% of openings. We achieved net unit growth of 5.6% for the year, above the high end of our guidance, and added approximately 55,000 net rooms globally, exceeding all major branded competitors. Our outperformance reflects the power of our commercial engines, the strength of our brands and our disciplined and diversified growth strategy.

Fourth quarter openings totaled more than 16,000 rooms, driven largely by the Americas and Asia Pacific regions. In the quarter, we celebrated the opening of our 400th hotel in China and our first Home2 Suites in the country. This positive momentum continued into the new year with the highly anticipated opening of the Conrad Shanghai just last month, marking the brand's debut in one of the world's busiest and most exciting markets.

During the quarter, we also continued the expansion of our luxury and resort portfolios with the opening of the Conrad Tulum and the new all-inclusive Hilton Cancun. With more than 400 luxury and resort hotels around the world and hundreds more in the pipeline, we remain focused on growing in these very important categories.

We were also thrilled to welcome guests to the Motto New York City Chelsea, a major milestone for this quickly growing brand and a perfect addition to Hilton's expanding lifestyle category. This hotel exemplifies what it means to be a lifestyle property. It incorporates unique and modern design elements and provides guests with authentic and locally-minded experiences.

We also celebrated the first lifestyle property in Chicago with the opening of the Canopy Chicago Central Loop and debuted the brand in the UK with the opening of the Canopy London City. These spectacular properties joined recently opened Canopy hotels in Paris, Madrid and São Paulo.

In 2021, we grew our Canopy portfolio by more than a third year-over-year, opening hotels across all major regions. We ended the year with 408,000 rooms in our development pipeline, up 3% year-over-year, even after a record year of openings. Our pipeline represents an industry-leading 38% of our existing supply, giving us confidence in our ability to deliver mid single-digit net unit growth for the next couple of years and eventually return to our prior 6% to 7% growth range. For this year, we expect net unit growth to be approximately 5%.

As our guests' travel needs continue to evolve, we again introduced innovative ways to enhance the guest experience. In the quarter, we announced the launch of Digital Key Share, which allows more than one guest to have access to their room's digital key via the Hilton Honors app.

To further reward our most loyal Hilton Honors members, we introduced automated complementary room upgrades, notifying eligible members of upgrades 72 hours prior to arrival. With our guests at the heart of everything we do, we've been thrilled to hear that the early feedback for both industry-leading features has been overwhelmingly positive.

In the quarter, Hilton Honors membership grew 13% year-over-year to more than 128 million members. Honors members accounted for 61% of occupancy in the quarter, just a few points below 2019 levels, and engagement continued to increase across members of all tiers.

We work hard to ensure that our hospitality continues to have a positive impact on the communities we serve. For that reason, we're incredibly proud to be recognized for our global leadership in sustainability. For the fifth consecutive year, we were included on both the World and North America Dow Jones Sustainability Indices, the most prestigious ranking for corporate sustainability performance.

Overall, I'm extremely pleased with the progress we've made over the last year, and I'm very confident that Hilton is better positioned than ever to lead the industry as we enter a new era of travel.

With that, I'll turn the call over to Kevin to give you more details on the quarter.

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

Thanks, Chris, and good morning, everyone. During the quarter, system-wide RevPAR grew 104.2% versus the prior year on a comparable and currency-neutral basis. System-wide RevPAR was down 13.5% compared to 2019 as the recovery continued to accelerate across all segments and regions, driven by border re-openings and strong holiday travel demand. Performance was driven by both occupancy and rate growth.

Adjusted EBITDA was \$512 million for the fourth quarter, up 151% year-over-year. Results reflect the continued recovery in travel demand. Management and franchise fees grew 91%, driven by strong RevPAR improvement and license fees. Additionally, results were helped by continued cost control at both the corporate and property levels.

Our ownership portfolio posted a loss for the quarter due to the challenging operating environment and fixed rent payments at some of our leased properties. Continued cost discipline mitigated segment losses. For the quarter, diluted earnings per share, adjusted for special items, was \$0.72.

Turning to our regional performance. Fourth quarter comparable US RevPAR grew 110% year-over-year and was down 11% versus 2019. The US benefited from strong leisure demand over the holidays, with transient RevPAR 1% above 2019 levels and transient rate nearly 5% higher than 2019 for the quarter.

Group business also continued to strengthen throughout the quarter, with December room nights just 12% off of 2019 levels. In the Americas outside of the US, fourth quarter RevPAR increased 150% year-over-year and was down 17% versus 2019.

Continued easing restrictions and holiday leisure demand drove improving trends throughout the quarter. Canada continued to see steady improvement as borders remained open to vaccinated international travelers.

In Europe, RevPAR grew 306% year-over-year and was down 25% versus 2019. Travel demand recovered steadily through November but stalled in December as a rise in COVID cases led to reimposed restrictions across the region.

In the Middle East and Africa region, RevPAR increased 124% year-over-year and was up 7% versus 2019. Performance benefited from strong domestic leisure demand and the continued recovery of international inbound travel as restrictions eased.

In the Asia Pacific region, fourth quarter RevPAR fell 1% year-over-year and was down 34% versus 2019. RevPAR in China was down 24% as compared to 2019 as travel restrictions and lockdowns remained in place. However, occupancy in the country held steady versus the third quarter as summer leisure travel was replaced with local corporate and meetings business. The rest of the Asia Pacific region benefited from relaxed COVID restrictions and the introduction of vaccinated travel lanes in several key markets.

Turning to development. As Chris mentioned, for the full year, we grew net units 5.6%. Our pipeline grew sequentially and year-over-year, totaling 408,000 rooms at the end of the quarter, with 61% of pipeline rooms located outside the US and roughly half under construction. Demand for Hilton-branded properties remains robust and, along with our high-quality pipeline, we are positioned to emerge from the pandemic stronger than ever.

Turning to the balance sheet. We ended the year with \$8.9 billion of long-term debt and \$1.5 billion in total cash and cash equivalents. We're proud of the financial flexibility we demonstrated through the pandemic and remain

confident in our ability to continue to be an engine of opportunity and growth as we look to reinstate our capital return program. Further details on our fourth quarter and full year results can be found in the earnings release we issued this morning.

This completes our prepared remarks. We would now like to open the line for any questions you may have. We would like to speak with all of you this morning, so we ask that you limit yourself to one question. Chad, can we have our first question, please?

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question will be from Shaun Kelley with Bank of America. Please go ahead.

Shaun C. Kelley

Analyst, BofA Securities, Inc.

Hi, good morning, everyone.

Q

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Hi Shaun.

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Shaun C. Kelley

Analyst, BofA Securities, Inc.

Good morning, Chris. I wanted to dig in a little bit. I thought the margin commentary you gave was interesting, Chris. I mean, in general, we don't think of – I think, we think of hotels being more about recovery beneficiaries than we do it thinking through the pandemic and some of the opportunities that may have presented on the cost side. So, could you just give us a little bit more color on what some of the key buckets are that have changed in your overall operating model that are driving that improvement? And then secondarily, just help us think through, how that might trend over the next couple of years as you kind of ramp up towards that 500 basis point margin target that you mentioned?

Q

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Yeah, I'm happy to do it. And we've put it in the comments because the truth is it's, I would argue, very important. I don't think it's had a lot of focus and it has an intense amount of focus inside this company amongst the management team and, for that matter, with our Board of Directors because the idea was, as you would want to do in any crisis, is take advantage of opportunity.

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And as we went into the crisis, we saw things that we thought we not only needed to do to address the crisis, but we could do to make the business stronger. And so, we didn't obviously have a lot to worry about liquidity. We had a lot to worry about, but our balance sheet was great. We didn't have a lot of liquidity issues. So, we very quickly, not to pat us on the back, but it's true.

Like in March, April of 2020, we were focused on recovery, how do we get to the other side, what are the things that we can do to make this business faster growing, better, stronger and higher margin. And we've been at it ever since and we'll never stop because we think there are opportunities.

I think, if you did the math, it sort of comes in three categories that gets you there. Number one, we're bigger. So, units that have been added at 5-plus percent a year through COVID that haven't been during COVID that productive that are over the next few years going to become productive contributors to earnings. We've had great success in our sort of license arrangements and sort of our non-RevPAR-related fee segment of the business. So, think our HGV business, think our AmEx, but co-brand business generally where we – it's a very, very high-margin business and it has performed very well. If you look at the numbers carefully, 2021, we were already over peak levels for those fees – peak 2019 levels, and we think there's still meaningful growth to come from that.

And then last, but not least and importantly, cost structure. We, like everybody, every business that was dramatically impacted by COVID, had to think about cutting costs in hotels and in corporate and we did that. But again, not patting us on the back, but reality, we said like, we don't want to just take cost out. We want to sort of reengineer the way we run the business to be able to – where we think there might be longer-term efficiencies, realize those and during COVID sort of get – build it into the DNA of the company. And so, we were able to take out a bunch of costs that helped during COVID, but that we think we will be able to keep out. When you put all that together, as we said, we think it's 400 basis points to 600 basis points of sort of real run rate margin improvement. We delivered pretty well against, I thought, last year when we had RevPAR and EBITDA that was 30% off of peak levels and delivering 500 basis point margin levels was pretty compelling as a down payment on what we're saying.

Now it won't be a perfectly straight road, meaning there are – last year, we probably underspent in some areas because it's been hard to hire and all that, corporately. This year, we'll catch up a little bit with that. So, it won't be a completely straight line. But as you look out to like 2023 and 2024, I think, we're in those target ranges, hopefully at the midpoint or beyond those, at least as we model it. And as I said, it's not by happenstance, it's not by luck. It's been a huge focus and I think shareholders should feel comfortable that it will remain an intense focus of the enterprise because we know we can.

And if we can, we should because ultimately, and I won't finish this because I'm sure others have questions that we want to have answer. Ultimately, obviously, we're a free – when we – in a normal time, we're a free cash flow machine. The higher the margins, the higher the free cash flow and having 500 basis point higher margins allows us to drive a lot more free cash flow that allows us to return a lot more capital over time. And as I said in my prepared comments, we intend to start returning capital in the second quarter. That is the second quarter of this year, that is six weeks from now.

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Shaun C. Kelley

Analyst, BofA Securities, Inc.

Thank you very much.

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Operator: Thank you. And the next question will come from Joe Greff with JPMorgan. Please go ahead.

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Joseph Greff

Analyst, JPMorgan Securities LLC

Good morning, everybody.

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

Good morning, Joe.

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Joseph Greff*Analyst, JPMorgan Securities LLC*

I have a two-part question on development. One, it's hard not to notice that the managed footprint has caught up at least relative to the growth rate into 2019. How do you see the footprint growth between managed and franchise growing in 2022? I know you talked about 5% this year, longer term 6% to 7%. And then can you also just talk about what's going on development-wise in China currently? Thank you.

Q

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

Yeah. Sure, Joe. I'll take this one. I think, it's interesting. I'm not exactly sure what numbers you're looking at. I think, our split between managed and franchised as the pipeline plays out has been pretty consistent, right? Our existing supply is 75% franchised led by the US and the Americas, of course. But more and more, our pipeline today is 40% franchised outside – in – sorry, 40% franchised in EMEA and nearly half franchised in APAC as our franchisee business grows in those regions. And so over time, what had been happening is growing outside the US, more of those deals had been managed and that was sort of skewing us back towards managed. And now I'd say we're on a trajectory overall. We'll still add a bunch of managed rooms as we grow outside the US, but more and more we're doing franchising outside of the US. And so maybe I'm missing something in your question and I'm happy to do a follow-up, but I think that's been pretty consistent and not really moving around that much.

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And then interestingly – and so feel free to follow up. But to get to China, it's interesting. Most of the development trends, and I think, we've said this on prior calls, have been following the trend of the virus. So, meaning, as the world has been opening up in those regions, you see a pretty direct correlation to signing activity and approval activity in those regions, so led by the US, Europe had sort of a slow start this year, but then really came on towards the end of the year as things started to open up.

China has been kind of the exception to that rule, meaning even with lockdowns and people not moving around and you would think not being able to travel across the country, would slow the pace of activity, but that just hasn't been the case. So, for us, we – our approvals for 2021 were up 45% for the year and our openings were up 30% over the year. And we think our openings will be up something similar to that over the course of 2022.

So, China has really been strong, led by our Plateno Hampton JV. We've now launched Home2 with Country Garden. We've now launched on our own – an individual franchising program for Hilton Garden Inn, with still a bunch of, Chris mentioned a little bit in our prepared remarks, still a bunch of really great full-service and luxury signings along the way. So, China has been a little bit of the exception to the rule with COVID where even in the face of lockdowns, we've had a lot of activity.

Joseph Greff*Analyst, JPMorgan Securities LLC*

Great. You answered it. Thanks, Kevin.

Q

Operator: And the next question will come from Thomas Allen with Morgan Stanley. Please go ahead.

Thomas G. Allen*Analyst, Morgan Stanley & Co. LLC*

Q

Thank you. Just a follow-up to Shaun's question, maybe a clarification. As I look at 2024 consensus for you, the Street is looking for \$3.1 billion of EBITDA and 70% margin. And your comments earlier, Chris, was we're going to gain 400 basis points to 600 basis points of margin versus 2019, which is how you end up 65%, 66% range. Do you think – what do you think the Street's modeling – mis-modeling? Thank you.

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

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I have no earthly idea. As you know, we haven't been giving guidance for any period of time, let alone for 2024. So, Thomas, I think the best thing to do is let my comments stand as they were. We're confident that on a run rate basis, it'll sort of be in that range. We're very proud of that, of being able to accomplish that. Obviously, we're always looking to under-promise and over-deliver. So that will never change, but not much to add at this point.

Thomas G. Allen*Analyst, Morgan Stanley & Co. LLC*

Q

All right. Chris, just – I mean, I guess asked another way, two things I was thinking of when you said it: one, there's obviously going to be a mix shift of the lower-margin owned business coming back. And then, secondly, when we look at your margins historically, they increased every single year. So, I guess, the point I'm making is, I think your commentary around margins is more of your confidence around resetting margins higher versus commentary that your expense base will grow significantly and you're kind of – you're stuck at a margin level. Is that the right way to think about it?

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

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I'm not sure I understand, but I think so. Yeah. I mean, we have confidence – said another way, just to be clear, we have confidence that the structural changes we have made to the company on a like-for-like basis are going to drive higher margins. So, if you think that margins were going to continue to grow organically under the prior setup, then we agree with that, and we think that there's an incremental piece to it that is a result of structural changes that we've made and that we'll maintain.

Thomas G. Allen*Analyst, Morgan Stanley & Co. LLC*

Q

Yeah. I think that's it. Thank you.

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

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Yeah. I'd probably just add to that quickly on the real estate is, like, you're making a comment about the mix of business, but you should remember that the real estate's been shrinking over time. And even though you've had – you've got different rates of recovery in COVID and different mix, over time, that is going to continue to be a smaller part of the business as we continue to grow the managed and franchised business and continue to work our way out of the risk.

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

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Yeah. And not to beat a dead horse, but to just throw something slightly more on top of the real estate. The real estate, you're right, is a lower-margin business by definition. We have baked that into what we – what our – my guidance – what my summary was of what our expectation is over the next few years. So that was taken into account.

It also, from an EBITDA growth point of view, will be tremendously helpful because it was so beat up, given the structure of how much of it is held that from an EBITDA growth rate point of view over the next few years, real estate's going to be very, very helpful...

Kevin J. Jacobs

Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.

High growth, yeah.

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Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

... very high growth.

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Thomas G. Allen

Analyst, Morgan Stanley & Co. LLC

Thanks for the clarification.

Q

Operator: And the next question will come from Smedes Rose with Citigroup. Please go ahead.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Hi, thanks. I wanted to ask a little bit more about your thoughts on China. And maybe you could just give us a reminder of what the kind of contribution China made to fees in 2019, and maybe kind of how far that fell off in 2021, just because it seems like there's an opportunity for some significant rebounding. Maybe it sounds like it's running behind kind of the rest of the world. And if you have any kind of thoughts on maybe how China addresses its policy around COVID going forward or if they keep the kind of zero tolerance in place indefinitely?

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Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Yeah. I think, China, I'm doing this from memory, I think China in 2019 was like 5 points of EBITDA overall. And I would guess at this point, it is less than half of that. So, I'm looking at Jill. It's probably 2% or something like that. So, I think you're right. There's a significant – I mean, by the way, that's true for the entire international estate, when you think about it. Our Asia Pacific business, our Europe business, they've all been slower to return. And so, our EBITDA, if you looked at 2020 and 2021, was crazy disproportionately US-based, and those numbers aren't fully back to where they were. I mean, we were like 73% US. I think in 2020, we were like 94% or 95%, and last year, we were like 83% or something.

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So, it's coming back and will ultimately return to a more normalized kind of environment, which means not just China, but the whole world. The whole world outside of the US has some significant growth potential as we get to a more normalized environment.

In terms of the regions generally, and I'll end on China and maybe use this as an opportunity to just talk about sort of the rhythms of what's going on, most of which I think is pretty well known because you guys have a lot of data, but if you look at what's going on in the world, the Middle East, which is not a huge part of our business, is sort of leading the world. I mean, you saw our numbers for the fourth quarter. Middle East is already meaningfully above 2019 levels, so they're sort of ahead in recovery. We think that will continue.

The US, I would say, is sort of next and we can – maybe I'll leave it to another question. Our belief is you will see, in the second quarter, a transition and then very rapid recovery, all our earlier prepared comments, in the second half of the year. I think, Europe will be quick to follow in the sense that it's more complicated because you have more countries, the restrictions aren't just one set of restrictions, but you can start to see it sort of sweeping through Europe opening, sweeping through Europe.

Now Asia Pacific, I think, will lag in large part because of China and the policies they've had. My own view, and that's all it is. It's not because of insider knowledge is that as the rest of the world opens and as you get, which I think we are rapidly approaching to an endemic stage of COVID, I think there'll be a lot of pressure economically, culturally and otherwise for China to open up, much like the rest of the world.

So, I think, it will be – it will lag, but I think it will be – I think, Europe and then Asia will be a fast follow. And as I think we – as we – my own view as we get to the second half of the year, I think you're in an entirely different environment across the globe. And within the first half of the year, you're going to see things evolving at a slightly different pace. But I think when you get to the second half of the year, every – the whole world broadly is going to be a lot more open than anything we've seen in two years.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Great. Thank you.

Q

Operator: The next question is from Stephen Grambling with Goldman Sachs. Please go ahead.

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

Hi. Thanks. I'd like to come at margins from maybe the perspective of your owners, which is always key to driving that overall flywheel. How are you thinking owner margins will progress versus pre-pandemic? And could you tie in how you envision the hotel experience will structurally change, whether it's longer stays, charging or opt-in for cleaning or reducing non-consumer-facing labor? And where do you see the greatest opportunity for investing back into your owners to improve the experience amidst some of these shifting preferences? Thanks.

Q

Kevin J. Jacobs

Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.

Yeah. Good question, Steve, and a little bit to unpack there, but I'll sort of try to go in order. I think, if you'd take a step back to the beginning of the pandemic, I think we've done a really good job leading – we did a really good job in the pandemic leading the way with starting out early on advocating for our owners, whether that was for government assistance or otherwise, being really flexible with standards as the business sort of fell apart a little bit. And through recovery, sort of similar to what Chris has been talking about of really taking the opportunity of COVID to drive improvement through our enterprise. We've been doing the same thing at the property level, right? So it's certain big things you mentioned by being innovative with reengineering our food and beverage and particularly, breakfast offerings, looking at housekeeping and opt-in there and then a bunch of little things across

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line item by line item and sort of literally grinding through the P&Ls and standards with our owners to help them – help the properties be more profitable through COVID and using that opportunity to make sure that, that profitability and those efficiencies stand going forward.

Now people talk about we do need service recovery, right? It has been hard to hire labor. We do need to bring some of those service standards back. Obviously, everybody knows what's going on with inflation and wage inflation. But of course, the flip side of that on inflation is that helps on the revenue line, right? We reprice the rooms every night. If inflation is a headwind, on the cost side, it's going to be a tailwind on the revenue side, and the revenue base is obviously bigger than the expense base. And so that ought to lead to higher margins coming out the other side. So, when you put that all together, we think we can do a better job for customers, give them what they want, take away what they don't want and what they won't pay for and use driving revenue through an inflationary environment to get our owners to be higher-margin businesses coming out the other side.

Stephen Grambling*Analyst, Goldman Sachs & Co. LLC*

Helpful. Thank you.

Q

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

Sure.

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Operator: The next question is from Patrick Scholes with Truist Securities. Please go ahead.

Patrick Scholes*Analyst, Truist Securities, Inc.*

Hi. Good morning, everyone.

Q

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

Good morning.

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Patrick Scholes*Analyst, Truist Securities, Inc.*

Morning. When I try to think about some things that have perhaps permanently changed or at least changed from 2019, I'm wondering what your thoughts are on the degree of key money that you're giving today for new hotels under your brand, number one. And how have the franchise contracts changed? Are they more flexible today versus pre-COVID, less flexible? I'd just like to hear your thoughts on those. Thank you.

Q

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

Yeah, I think I'll start with the second part. I mean, really, there's nothing different about our franchise agreements now versus pre-COVID. It's a very well – it's a business that's been around for a long time. The protocols are established, the franchise documents, you can read them, they're public. They haven't really changed over time. I think when it comes to key money, I mean, you could see in our numbers this year that it's been sort of higher than it had been in the past. I think that's a function of a little bit of – I don't think it's COVID versus pre-COVID. It's a competitive environment out there so there's definitely competition.

A

We're leading the way in growth and our competitors are trying to catch up to us. So that makes for competition. But the reality is, is our number of deals that have key money associated with them is about 10%. That's what it was pre-COVID. That's what it is today. So that's been pretty consistent. And we've just been fortunate over the last particularly a year or so, we've signed some really high-profile deals. I think about the Waldorf Astoria Monarch Beach in California. I think about Resorts World in Las Vegas, the deal we did in Cancun and Tulum, those have been deals that we've been working on for a really long time. They're very strategic. They happen to be a little bit higher key money associated with them than we're used to. And so we've been a little bit higher.

And that trend maybe continues for a little while longer. We have some strategic things in the hopper at the moment that I think might keep that number a little bit elevated over the course of 2022 and maybe even for a little while beyond that. But what I'd say sort of in closing, and hopefully, that sort of covers it and Chris may want to add to this a little bit, is relative to our peers, I think we stack up really favorably in terms of what we've been deploying for capital to get to our level of growth, I think, has been exemplary.

Operator: Thank you. And the next question will come from Rich Hightower with Evercore. Please go ahead.

Rich Allen Hightower

Analyst, Evercore Group LLC

Hi. Good morning, everybody.

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Good morning.

Rich Allen Hightower

Analyst, Evercore Group LLC

So I want to go back to a portion of the prepared comments. And Chris, I think you mentioned it was STR's forecast. I know this is not a Hilton forecast, but for business transient demand, I think you get to the low 90s as a percentage of pre-COVID levels this year. So again, not your forecast, but I am wondering if you could take me through the building blocks in your mind as to perhaps how we might get to that level by the end of this year, especially in the context of hybrid workforces, work-from-home and so forth?

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Hi, yeah, it is in our forecast, but I do buy into it. And I think actually, it might be even better than that personally, my own opinion. I think there's a really good chance on a run rate basis that we will end up back at or above where we were in 2019 before the year is out. So why do I think that?

One, there's a lot of pent-up demand. That obviously helps, and Omicron created more pent-up demand because a lot of people didn't do trips. But I can't speak for the industry. I can speak for us. We're out talking to customers all the time, sort of large, medium, small. And what you find is like heretofore during the crisis, the largest corporate customers have been way off on travel. So they've been like 80% – well, I'd say through the third and fourth quarter, they were 70% or 80% off still. But what happened is that SME, small, medium enterprises were out traveling like crazy. I've given these stats before on calls. Pre-COVID, 80% of our business transient was SMEs. 20% of it or 10% of the overall business was large corporate. So it's not that we don't love them and we don't want them, but we were never ultimately that dependent on that.

So what happened in COVID for us is, again, I'm back to what I said in my earlier comments, we were, in March or April of 2020, saying like, all right, what do we do? Where do we pivot? How do we retool our sales force, forgetting whatever business is out there? And what we found, not surprisingly, is the large corporates disappeared, but the SMEs were still out there, maybe not like they are now, but they were out there more than others. Why? Because they're small and medium, they had to. Like, they'd die if they – their business requires it and so they have to be out there. And so we pivoted a whole bunch of our infrastructure and sort of like retooled our entire sales force to make sure that we didn't abandon the large corporates and those relationships. We kept our entire sales team on payroll during the whole crisis, which is unlike, I think, a bunch of our competitors. But we did say, we need to like reorient how we're focusing our time. And we've done – with all – again, I feel like I'm patting us on the back, we've done a really good job. And so, we have replaced, we think, probably already half of what that corporate business was that went away.

And I think the corporate business is going to come back. You don't have to believe it's all going to come back, but the idea is one plus one, I think, can equal three, right? Meaning, pivoting even harder to have a larger demand base to put in the top of the funnel of SMEs, along with corporates coming back gradually, is just going to give us an opportunity to price demand in a way that I think will be superior to what we could price it before.

Last comment I'd make is that people think about SMEs versus the big corporates, and no offense to all the big corporates that are on this call, but the reality is you guys pay less. So the SMEs, I mean, if you look at the rate structure of SMEs, it's like 15%-plus on average higher because the big corporates' beat is up more, they beat everybody up and we discount more. So the reality is not only is there more of it that's been out there and we've retooled to go after more of it, but the reality is it's at a higher price, too. And so that's why I believe in what STR is saying, we're better is because I do think throughout this year, as you release pent-up demand, given our access to SMEs that have been very robust and we have more of them. Corporates are definitely starting to come back, talk to every travel manager in the country, which we do, and they're coming back. When you put all those pieces together, I think it's pretty easy to believe. As you get to the – particularly the second half of the year, you're going to be in a very different and a very positive environment.

Rich Allen Hightower

Analyst, Evercore Group LLC

Great, helpful. Thank you.

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Yes.

Operator: The next question is from Richard Clarke with Bernstein. Please go ahead.

Richard J. Clarke

Analyst, AB Bernstein

Thanks very much for taking my questions. I just want to ask you a question about the kind of construction environment. I noticed your percentage of pipeline that's under construction has dropped below 50% for the first time in quite a while. Is that just phasing? And does that feed into this year's guide on unit growth? Or does that mean we maybe can't expect a recovery in 2023 to return to the normal, 6% to 7% takes a little bit longer?

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

A

Yeah. Richard, I think, look, that's a slight decrease, almost a rounding error in terms of our amount under construction. It really is sort of rounded to half before it rounds to half now. If you look at the industry data per STR, it's down actually a lot more than that. And so we're doing a really good job of both getting and keeping things under construction.

And I'd say the way to think about the trajectory is we actually think we'll start more rooms this year than we started last year. Now, in the US, which is our largest market, we think we have one more year where it's going to decline slightly and 2022 is probably the bottom. And that does play into our forward-looking forecast. And of course, that's just a function of largely input cost, right? If construction costs overall are sort of up year-over-year at the moment in the mid-teens, raw material cost and labor cost inflation is not something that should surprise anybody on this call, that sort of a thing going on globally, especially in the US. And so that does all play into our outlook.

And so we've actually never said publicly when we think we'll get back to our prior 6% to 7% level. But given what's going on now, it probably takes two or three years to get back to that level we think. Again, this year, we'll be – 2021 was the bottom globally for starts. This year, 2022 in the US, we think we'll recover from there. You got to start them to deliver them, right. So we have to have start to recover to be able to get back to that prior level of net unit growth. And so you are seeing that sort of affect our outlook, both for this year and beyond.

And then I guess the last thing I'd say on that is, even with everything that's been going on in the world, for now, a two-year pandemic with the world blowing sky high, we're still delivering 5-plus percent net unit growth. We still think we'll deliver at that rate through this development lag that's going to come from the pandemic and then we'll recover from there. We think that's actually pretty good evidence of the resiliency of the business and the resiliency of our ability to grow.

Richard J. Clarke*Analyst, AB Bernstein*

Q

Very helpful. Thanks so much.

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

A

Sure.

Operator: The next question is from David Katz with Jefferies. Please go ahead.

David Katz*Analyst, Jefferies LLC*

Q

Morning, everyone. Thanks for taking my question. I appreciate all of the detail so far. I wanted to ask about the aspect of the fees, which is non-RevPAR-driven, which are royalties and credit card fees, et cetera. Is there any sort of insights or help that you can offer us as we think about modeling out the next year or two as to what those might grow and any puts and takes? Thank you.

Kevin J. Jacobs*Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.*

A

Yeah, David, I think we've talked about this in the past that we get that it's a little bit hard to model sort of specifically what's going on. Our non-RevPAR-driven fees cover a bunch of different things, obviously, our co-brand credit card and our license fees from HGV being the largest part of that, but we have other things in there like residential development fees and the like.

And we've said this before, that's been less volatile, right? So it declined less than RevPAR declined during COVID. And now, at this point, it's growing less than RevPAR. I think for 2021, it grew about two-thirds of the rate of RevPAR. And that's probably a decent way to think about it going forward. It's hard to say, right? It depends on how those things perform and what goes on. But I think it's going to continue to be a decent growth rate and additive to our fees.

For 2021, it was actually higher. Our non-RevPAR fees, or I think Chris, you might have said this earlier, so sorry if I'm repeating it, but our non-RevPAR fees were higher than they were in 2019. And our credit card program is performing quite nicely. I think just a few stats to give you some color. Our account acquisitions were up 45% last year. Our spend was up about a third year-over-year. And so really strong performance, but, again, at a lower rate than overall RevPAR because RevPAR is growing at a really high rate in recovery. So hopefully...

David Katz

Analyst, Jefferies LLC

So growth, but at a lesser rate?

Kevin J. Jacobs

Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.

At the moment.

David Katz

Analyst, Jefferies LLC

Perfect. Thank you.

Operator: The next question is from Robin Farley with UBS. Please go ahead.

Robin M. Farley

Analyst, UBS Securities LLC

Great. Thank you. Originally, my question was going to be – to clarify the comments, the opening remarks about transient midweek nights for all future periods down only 4% because that seemed like that number was sort of too strong a recovery. But I guess really based on – you really already commented already on the growth in the small and medium.

So I don't know if you have anything else to add on that, only being down 4%. I would think just even the booking window being shorter would make that hard to be at that good of a number. So I'm thinking of a...

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

No, I don't – Robin, I don't have anything to add other than, yeah, it's short. The very nature of advanced bookings and transient only gives you a window so far out in time. It's a relatively short window. But those are the stats. And again, I gave them to you because I think it is indicative not only of the strength that's building in that environment,

but the change from literally the beginning of the year when Omicron was a very big thing to a world where Omicron is becoming a lot less of a thing, and we're getting to more endemic stages of COVID-19.

Robin M. Farley*Analyst, UBS Securities LLC*

Q

Well. And then just for a follow-up, if you could put a little more color around – you mentioned reinstating the dividend in Q2 and returning to share repurchase in Q2. Can you talk about, will you sort of start at a dividend payout or dividend level probably lower than pre-pandemic initially? Or just sort of give us some thoughts around how you're thinking about that balance as you restart that return to shareholders? Thanks.

Christopher J. Nassetta*President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.*

A

Yeah. As I've said a couple of times, we're intending to do it in Q2. We have not formally declared a dividend so we haven't made a final decision. But I think the way to think about it and our intention at this point is to reinstate the dividend at the exact same level we had it before, same \$0.15 a share, which is where we were before to go back to where we were, and then use the bulk of our free cash flow and otherwise to re-implement our share repurchase program.

I know there are different views in the world about this. Our view, my view has always been that having some modest dividend is helpful. It does open the universe of investors up a bit to us, and we proved that pre-COVID and we've talked to lots of shareholders and I think still have that view. But the way to drive the best long-term returns for all of us that are shareholders is to have the bulk of our program be in the form of share buybacks. And so that's what we thought pre-COVID.

We did a whole bunch of work to see, is there anything going on? Jill's nodding her head because she did a lot of it. Is there anything that's changed in the world or with our shareholder base currently that would lead us to a different conclusion? And we have not. We do not believe there is. So that's what we'll do. We'll get started. I think the way to think – we obviously haven't given guidance generally, but I think the way to think about it is we'll start out at least thinking about it at a minimum being the free cash flow that we're going to produce this year.

And the way to think about that, I think, directionally is back to my margin point, while we're not back fully recovered by a pretty decent margin yet to 2019, certainly as you look at the full year 2022, because we have – the business is performing better, we've done these structural things that I described to drive higher margins. Our free cash flow is actually pretty much back this year, we think to 2019 levels. So we'll start at a minimum with that and go from there.

Robin M. Farley*Analyst, UBS Securities LLC*

Q

Okay. Great. Thanks very much.

Operator: The next question is from Chad Beynon with Macquarie. Please go ahead.

Chad Beynon*Analyst, Macquarie Capital (USA), Inc.*

Q

Hi, good morning. Thanks for taking my question. I believe your conversion NUG component of total growth has been in the 20% range. Can you help update us on this in terms of where it was for 2021? And then for 2022

against your NUG guide, how should we think about converts and what that will be as a percentage being slightly offset by higher, I guess, ground-up growth? Thanks.

Kevin J. Jacobs

Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.

A

Yeah. Thanks, Chad. Look, I think it will be – I mean, the short answer, the crisp answer is I think it will be consistent, right? It's been about 20%. We're actually doing more conversions. We've given you some of the stats, but our approvals, our openings for the full year were up 13% year-over-year. Actually, our approvals for full year last year were up 42% in conversion. So we're having nice growth in conversions, and we're doing more, but we're also doing more ground-up development, right?

And so the denominator in that equation is growing as well. And so, will it be slightly higher going for the next couple of years? It could be, depends a little bit on how a couple of big deals break that can move that percentage a little bit here or there. But I would think about it sort of as being pretty consistent around 20% or the low-20s of deliveries. And I think it's actually a good news story across the board. I mean, we – in the Americas, for 2021, we signed almost half of the conversion deals that were done in the Americas. And so we're doing a lot of conversions. But the reason it's not sort of spiking from 20% to 30% is we're delivering a lot of new development as well.

Chad Beynon

Analyst, Macquarie Capital (USA), Inc.

Q

Thank you, very much.

Kevin J. Jacobs

Chief Financial Officer & President, Global Development, Hilton Worldwide Holdings, Inc.

A

Sure.

Operator: Ladies and gentlemen, this concludes our question-and-answer session. I would like to turn the conference back to Chris Nassetta for any additional or closing remarks.

Christopher J. Nassetta

President, Chief Executive Officer & Director, Hilton Worldwide Holdings, Inc.

Thanks very much, everybody, for joining today. Obviously, continuing on with recovery. I think we are, as I've said a couple of times, hopefully, getting through the Omicron variant and very rapidly to an endemic stage of this. We're obviously optimistic as we look to the second quarter and the second half of the year, and overall, beyond that.

And so thanks for the time. We'll look forward to updating you on trends that, I think, will be a lot better the next time we talk. So thanks, and have a great day.

Operator: And thank you, sir. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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